

2014 East Africa Private Equity  
Confidence Survey  
Clarity and Distinction



# Survey Introduction & Methodology

This year's survey is our fourth annual survey since we launched in 2010. The survey was conducted between December 2013 and February 2014 and targeted General Partners (GPs), who primarily invest in East Africa. Out of the total group, we received 42 usable GP responses and three responses from Limited Partners (LPs). As was the case in the 2013 survey, the responses from LPs were too few to represent the general views of all LPs; nonetheless we were able to get valuable insights from them, which we have included here.

Our annual survey has continued to elicit great interest among the Private Equity (PE) community, especially within Eastern Africa, seen by year on year higher response rates, with the highest in 2014 since our launch. In this fourth round, we maintained all the questions asked in the previous survey to allow for ease of comparison as well as to assess whether past views expressed by respondents about the future have materialised. Given the similarity of the questions over the four year period, our analysis will therefore, reveal trends and key developments in the PE space.

Africa Assets, a Kenya-based research and consulting firm covering Private Equity and Venture Capital in sub-Saharan Africa, worked closely with us on this report by providing data and analysis. Such data included, but was not limited to, key deals undertaken and announced in 2013, deal numbers and sizes, fundraising activity as well as information used to understand the current PE market and expectations going forward.

In defining 2013 PE deals, direct investment by Development Finance Institutions (DFI) and debt nature deals have been excluded.

## List of Abbreviations

bn	Billion
CBT	Consumer, Business and Transportation
DFI	Development Finance Institution
EAC	East African Community (regional bloc)
GP	General Partner
IPO	Initial Public Offering
LP	Limited Partner
m	Million
PE	Private Equity
TMT	Technology, Media and Telecommunications
trn	Trillion
SME	Small and Medium Enterprises
SSA	Sub Saharan Africa
SME	Small and Medium Enterprises
US\$	United States Dollar

# Foreword

In what has become characteristic of markets in 'The Next Frontier', the Private Equity (PE) market in Sub Saharan Africa (SSA) has continued in its year on year growth path with an increasing number of funds being closed, a marked improvement in the fundraising environment, and a higher number of exits and new investments buoyed by an increasingly positive attitude to PE in SSA.

Despite this growth, the PE industry is still in its nascent stages, compared to other more advanced emerging markets. Increasingly, more and more funds are setting up offices in the region attracted by high returns and the large number of opportunities. The survey findings indicate that majority of players are in the investment phase, with most expecting increased competition for deals. Of immediate interest is whether the growth in PE activity has outpaced growth in the number of deals. The survey indicates that deal hunting now faces great competition for lucrative deals, with most ideal targets in the region commenting that they get visits from PE players looking to invest in them every so often. This is a pointer to the fact that with development in financial services and more financial intermediation alternatives, financing for SSA companies is no longer the greatest challenge. PE players are now not measured by the size of their pockets, but rather by the value-add they bring to the investee company.

In this edition of the survey, we continued to elicit responses from the Eastern, Western, Southern and Central African region and received the highest response rate since our launch in 2010. However, the focus is still on the Eastern Africa region. The survey responses continue to show that Eastern Africa is still the most attractive region – perhaps also reflected by the founding of the new East Africa Venture Capital Association (EAVCA) in 2013 - even if the majority expect the performance of investments, when compared to Western Africa, to be the same.

PE players in SSA are still principally investing in the traditional markets of Kenya, Nigeria and South Africa where the majority feel that there is more certainty. However, interest in other countries like Ethiopia, Rwanda and Côte d'Ivoire, where players are looking for affordable deals is rising. In terms of the sectors, consumer driven sectors are most popular, even though some PE firms narrow their focus on sectors like energy or real estate.

It will be interesting to see what 2014 will bring in terms of deal activity and competition for transactions, though from the number of deals announced so far, it looks promising.

We wish you a good deal year and look forward to helping you grow your portfolio in Eastern Africa and beyond.



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Africa Assets

# 1 Market Outlook

## 2013 in Review

### Deals

84 deals were completed in SSA in 2013, of those 46 reported total values of US\$3.69bn, according to Africa Assets data.

Private Equity funds invested more than three times as much in sub-Saharan Africa in 2013 as they did in 2012. What happened? For one, there were a lot more deals: 84 in 2013 compared to 58 in 2012. This reflects a slump in deal-making in 2012, likely linked to lack of confidence in global markets and fallout from the Eurozone crisis that depressed growth in many African countries that year. 2011 was a much stronger year for PE in Africa – are 2013 numbers a return to trend?

Confidence for PE in Africa is certainly increasing. Track records are deepening, growth is strong, risks are manageable and LPs continue to rate the region highly amongst their emerging market options. But PE in Africa is still a young and volatile industry. And 2013's large investment total was quite sector-specific, pushed up by three large energy deals (see chart below) that together accounted for 63% of the year's total reported investment. In 2011, the top three deals by value only accounted for 43% of the year's total, and were spread across three different sectors. The largest deal done in 2012 barely topped US\$200m.

### Big Money Trends: Large African PE Deals 2011 – 2013

Year	GP	Company	Geography	Sector	Value (US\$m)
2013	Helios, BTG Pactual JV w/ Petrobas	Oil and gas exploration platform	Africa	Oil and Gas	1,530
2013	Warburg Pincus	Delonex Energy; African exploration and production platform	Africa	Oil and Gas	600
2013	Actis	AES Corp.'s power assets	Cameroon	Infra-Energy	220
2013	ECP	IHS Plc	Africa	Infra-Telco	1,053*
2013	CapitalWorks	Construction Products Africa	South Africa	Manufacturing	135
2013	Abraaj Group & Danone	Fan Milk	Ghana	FMCG	400*
2012	Carlyle, Standard Chartered PE	Export Trading Group (ETG)	Tanzania	Agribusiness	210
2011	Actis	Tracker	South Africa	Retail	434
2011	ACA-led Consortium	Union Bank	Nigeria	Financial Services	750*
2011	Helios, Vitol Group	Shell's downstream assets	Africa	Oil and Gas	1,000*

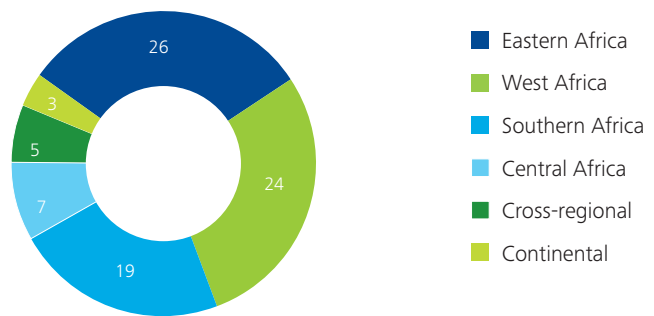
Source: Africa Assets

\* Note: Wherever possible, Africa Assets calculates annual deal totals to include only equity capital deployed through a Private Equity fund. Our 2013 sum, therefore, does not include the entire US\$1.035bn capital raise for ECP's IHS, which included direct investment from many different non-PE investors and a lot of debt. Similarly, our aggregated total for Fan Milk, Union Bank and the Shell assets have been adjusted down from the total deal sizes shown in this table.

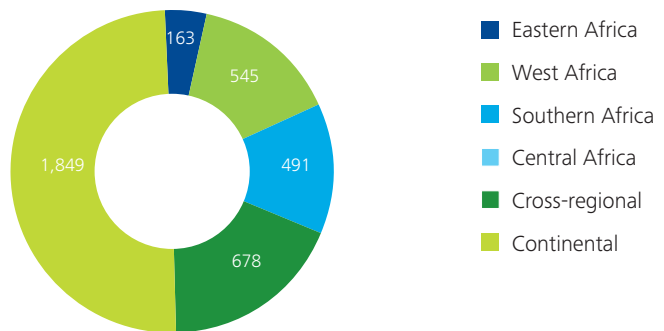
What does this tell us? Big annual investment totals in Africa will often have something to do with infrastructure or extractive industries. Big deals are possible in other sectors, too: namely financial services, manufacturing, retail and trade. Many larger deals outside of infrastructure and extractives are still restricted to South Africa. But transactions such as the Abraaj-Fan Milk deal – reportedly the largest FMCG PE deal in African history – offer hope for diversification across sectors and countries.

Africa’s small to mid-cap space is also still buzzing. As in recent years, deals continue to spread further across sectors and countries as the industry matures. Even as the top three country destinations remain the same – Kenya, Nigeria, South Africa –, other stars are rising. Ghana and Tanzania drew a nice mix of small and large deals in 2012 and 2013. Ethiopia has performed less consistently, producing several deals and plenty of excitement in 2012, followed by a quieter year in 2013 – a reflection of the country’s alluring yet difficult-to-realise potential. Interestingly, Cote d’Ivoire has emerged as a regular destination for PE funds, thanks to the country’s strong growth, stable politics, solid infrastructure – the country has one of the best electricity availabilities on the continent – and connections to Francophone Africa. Consumer-facing deals remain very popular, with a focus on banks and fast moving consumer goods. Agribusiness was also a favourite in 2013, dominated by small investments in input/service providers.

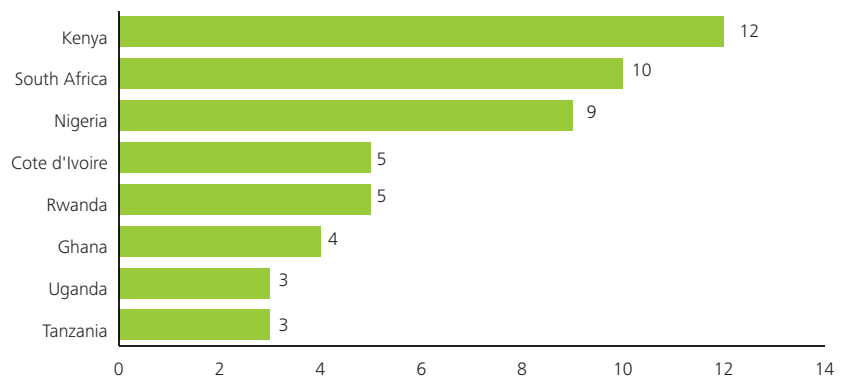
### 2013 Number of Deals by Region



### 2013 Reported Deal Values (US\$m) by Region



### 2013 Number of Deals by Top SSA Countries



**Country Focus**

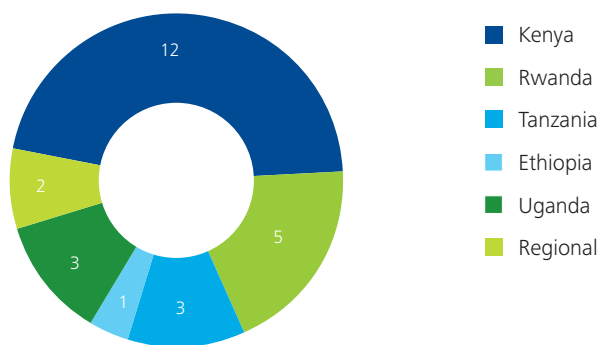
Kenya accounted for 46% of the total number of deals in Eastern Africa and 69% of total reported values. This reflected the views by respondents, in all our surveys, that Kenya remains a top destination country in Eastern Africa as well as Africa wide. The key deal in Kenya in 2013 related to Norway’s Norfund and Africa Infrastructure Investment Manager investment of US\$60m in equity to build a wind power project in Kenya worth US\$150m (US\$90m would be funded by debt from Standard Bank Group).

Tanzania had three deals valued at US\$5m, a significant drop from 2012, where two large deals were completed by Carlyle and Standard Chartered PE. Kenyan investment firm TransCentury sold their entire stake in Tanzanian Chai Bora Ltd, a tea manufacturer, to Catalyst Principal Partners. The deal value, however, was not disclosed.

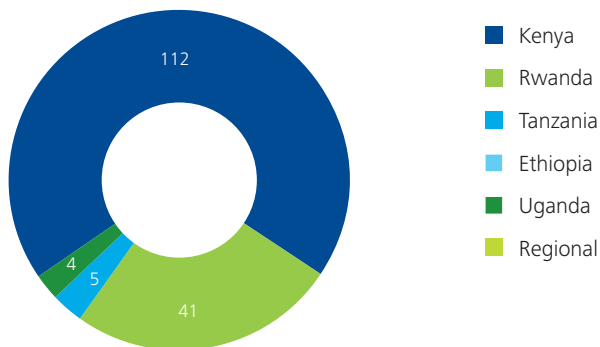
Rwanda saw a surprising increase in number of deals, with five deals with a reported value of US\$41.3m. These deals mainly involved Fusion Capital’s US\$34m investment in a real estate development project in Kigali and a US\$2m investment in Rusororo, a stone extraction mining company. Another deal was Fanisi Capital’s first investment made outside Kenya, US\$2m in Sophar Limited, a pharmaceutical wholesaler.

In what was a slight change in the trends observed recently, Ethiopia only attracted one deal. This was an investment, for an undisclosed sum, by Catalyst Principal Partners, an East African-focused Private Equity firm, which acquired a 50% stake in Yes Brands Food & Beverages PLC. Ethiopia’s high economic growth (the second fastest in Africa with GDP growth averaging 8% and 10% over the past five years) and population of 85m presents an attractive market for emerging players within the consumer sector. However, deals are difficult and time consuming to complete.

**2013 Number of Eastern Africa Deals by Country**



**2013 Value (Where Disclosed) of Eastern Africa Deals by Country (US\$m)**



**Sector Focus**

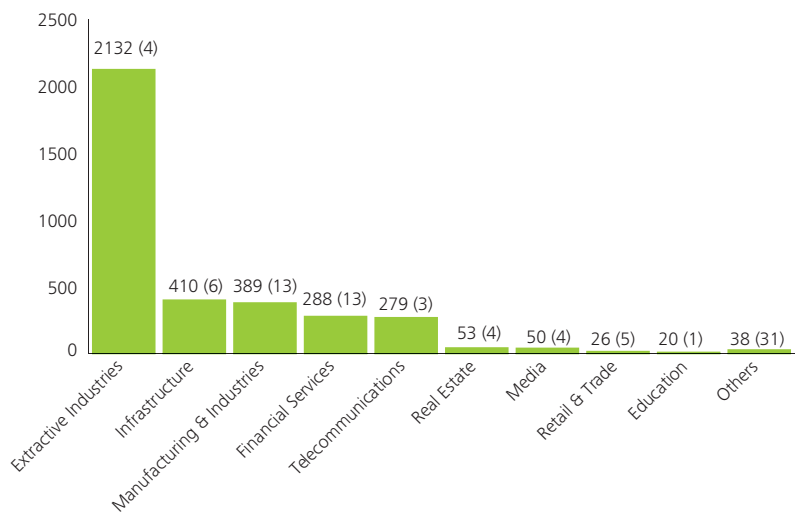
The extractive industries had the highest value of reported deals in SSA in 2013. The largest deal in this sector was US\$1.53bn, involving Helios Investment Partners alongside BTG Pactual in a 50/50 joint venture with Petrobras International Braspetro B.V., a subsidiary of Petrobras, to explore and produce oil and gas in Africa, through a specialized investment vehicle. The other major deal was Warbug Pincus' US\$600m early-stage investment into Delonex Energy, a start-up Africa-focused resources exploration company in Central and East Africa.

However, by number of deals, the manufacturing and financial sectors recorded the highest number (13 each), followed by agribusiness (12), TMT (7) and infrastructure (6). The majority of these deals' values were not disclosed, though they involved Small and Medium Enterprises (SMEs). This continued to reflect the trend in previous years, where majority of investments target SMEs, with the lack of large potential targets limiting deal sizes.

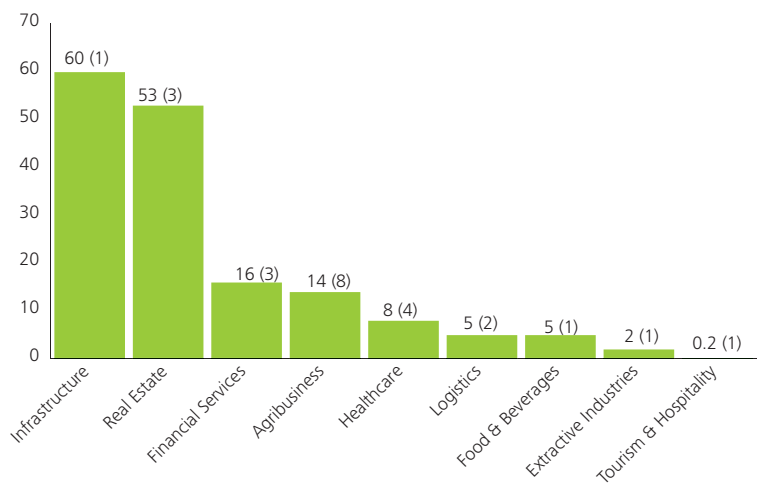
Deals in Eastern Africa were concentrated in agribusiness, healthcare and financial services, with a large deal of US\$60m from Norfund's and AIIM investment in a wind power project in Kenya. Deal sizes continued to remain small, the same as last year, with all reported deals lower than US\$20m (except for Fusion Capital's real estate deal and the Norfund and AIIM deal).

Going forward, deals are expected to concentrate on SMEs in the consumer driven sectors, where an expanding middle class is seen as a key driver of future revenues. A few large deals might also be seen in the extractive or related industries, driven by the ongoing exploration activities of oil and gas in Eastern Africa.

**2013 Reported Value (US\$m) and Number of SSA Deals by Sector**



**2013 Reported Value (US\$m) and Number of Eastern African Deals by Sector**



### Select Deals in East Africa in 2013

PE firm (s)/DFI acquiring	Target company	Country where target operates	Sector	Value of deal
Fanisi Capital	ProDev Group Holdings	Rwanda	Agribusiness	US\$3m
Pearl Capital Partners	Freshco Kenya Ltd	Kenya	Agribusiness	US\$600,000 (in quasi-equity)
Catalyst Principal Partners	Chai Bora	Tanzania	Agribusiness	Undisclosed
Amethis Finance	Chase Bank	Kenya	Financial services	US\$10.5m
8 Miles Fund	Eleni LLC	Kenya	Logistics	US\$5m
Swiss investment firm	Chase Bank	Kenya	Financial services	US\$5m
Centum	Almasi Beverages	Kenya	Food and beverage	US\$5m
Agri Vie	Tanzanian Food Corporation	Tanzania	Food and beverage	US\$4.9m
Catalyst Principal Partners	Yes Brands	Ethiopia	Food and beverage	Undisclosed
Pearl Capital Partners and Voxtra	Biyinzika Enterprises Ltd	Uganda	Food and beverage	US\$4m
Abraaj Capital	Nairobi Women's Hospital	Kenya	Health	US\$2.5m
Fusion Capital	Rusororo Aggregate	Rwanda	Mining	US\$2m





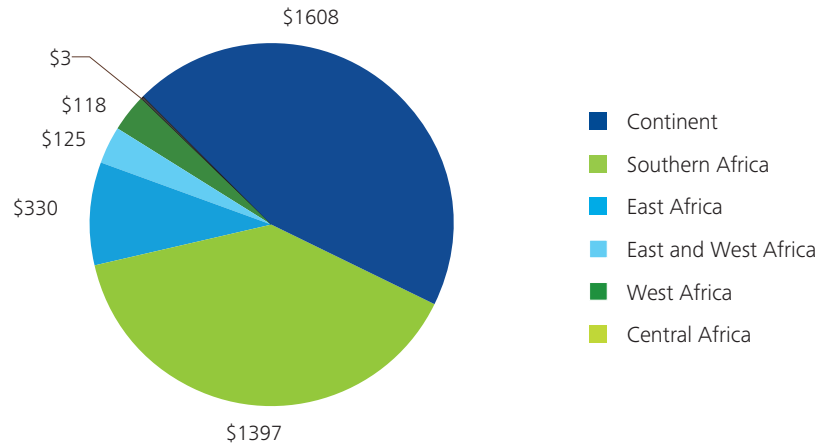
**Funds**

Fundraising for Africa-focused PE funds was strong in 2013, totalling US\$3.58bn. The good news from an industry development viewpoint is that nearly half of that capital went to funds with a continent-wide mandate. Notably, after plenty of expectation and speculation, Carlyle achieved a massive US\$591m first close for its maiden sub-Saharan Africa vehicle in July 2013, much higher than expected. This signals confidence, at least partly in the Carlyle brand, but also in the strong team that Carlyle has banded together to invest this fund, and in the potential for large-scale deal flow across the continent. Carlyle has already made two investments through the fund: Tanzanian agro-logistics firm Export Trading Group (ETG), and J&J Africa, a Mozambique based regional transport company. Both deals were co-investments with well-established PE firms – apparently a good strategy for a first generation fund in a difficult market.

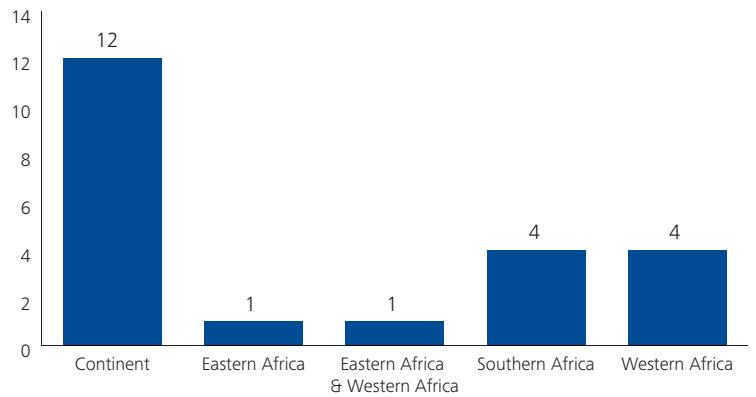
Another enormous chunk of 2013 fundraising went to funds targeting South Africa. A few of these will opportunistically target deals across the continent, but most of that capital will likely end up in South Africa. However, this does not necessarily indicate that fundraising will steer away from other sub-regions in favour of southern Africa in the coming years. Few deals were completed in SA in 2013 because the main focus of funds there, over the last two years, has been fundraising. With fundraising successes achieved by many of those GPs, including Ethos PE, Capitalworks, Lereko Metier and Convergence Partners, we can expect to see fundraising go down and deal activity pick up for the sub-region over the next few years.

South Africa’s largest pension fund, the GEPF, allocated a lot of money to South African Private Equity in 2013. This may have been disappointing to funds outside of SA that were hoping to diversify their LP base through African institutional capital. Much of the capital raised in 2013 still came from DFI sources. However, we know of at least one fund nearing the successful end of its courtship with local pensions in East Africa. This will be a fundraising space to watch in 2014, as one success could lead to other pension funds following suit.

2013 Value of Fund Launches by Targeted Region (US\$m)



2013 Number of Fund Launches by Targeted Region



At least 22 funds were launched in 2013 targeting sub-Saharan Africa, three with a global mandate including Africa. Only one fund was launched dedicated solely to eastern Africa, compared to four in 2012. Most new funds have a continental, generalist mandate. Notable launches included Abraaj's US\$800m Africa Fund, signaling the firm's strong confidence in the African market following its acquisition of well-established African GP Aureos in 2012. This new fund is twice the size of Aureos's last Africa fund, which also indicates that Abraaj intends to move away from the SME segment that has dominated Aureos investing for the last decade.

And finally, infrastructure will be an important sector to watch in coming years. Six infrastructure funds, with an African mandate, were launched in 2013. GPs also raised nearly US\$400m in 2013 for renewable energy and sustainability-focused funds. The greatest challenge for these funds will continue to be unreliable policy frameworks that make it difficult to bring infrastructure projects online in a timely and profitable way.

#### Selected Funds Closed in 2013

GP	Fund Name	Target (US\$m)	Close Date	Close Amount (US\$m)	Region	Sector
Carlyle	Carlyle sub-Saharan Africa Fund (TBD)	700	First close	592	Sub-Saharan Africa	Consumer
Lereko Metier	Lereko Metier Sustainable Capital Fund (LMSC)	65	Final close	68	Southern Africa	Infrastructure
Vital Capital Investments	Vital Capital Fund I	500	Final close	350	Sub-Saharan Africa	Agribusiness, education, healthcare, housing
Ethos Private Equity	Ethos Fund VI	750	Final close	800	Southern Africa, Sub-Saharan Africa	Open
Phatisa Group	African Agriculture Fund	300	Final close	243	Sub-Saharan Africa	Agribusiness

## Exits

At least 13 exits were completed by GPs in sub-Saharan Africa in 2013. Five of these exits followed the most common exit route in Africa, the trade sale. But, interestingly, the other eight came through a mix of strategies including secondary sales to other PE firms, initial public offerings, share sales and a management

buyback. This diversity is an encouraging sign of maturation and depth for the African PE market. Nearly half of this year's exits came through financial services assets, perhaps indicating why the sector is so popular amongst PE firms in Africa. Banks and insurance companies are generally easy to sell to eager market entrants and/or to exit on public markets.

### Selected Exits Announced or Completed in 2013 in SSA

Company	Exiting PE firm	Country	Sector	Exit route	Buyer
Chai Bora	TransCentury Ltd	Tanzania	Agribusiness	Secondary sale to PE	Catalyst Principal Partners
DFCU Bank Ltd	Actis	Uganda	Financial Services	Strategic sale	Rabo Development, Norfund
MTN Côte d'Ivoire	Emerging Capital Partners	Côte d'Ivoire	Telecommunication	Other	Planor Capital International
Express Life Insurance	LeapFrog Investments	Ghana	Financial Services	Strategic sale	Prudential
Surgical Innovations	Lereko Metier	South Africa	Healthcare	Strategic sale	Ascendis Health
Reatile Timrite	*Standard Bank Private Equity	South Africa	Manufacturing	Strategic sale	Thebe Investment Corporation
HFC Bank Ltd	The Abraaj Group	Ghana	Financial Services	Strategic sale	Republic Bank Ltd
Banco Nacional de Guinea Ecuatorial (BANGE)	African Development Corporation (ADC)	Equatorial Guinea	Financial Services	Repurchase by shareholders	Shareholders
Capital Properties	Actis	Tanzania	Real Estate	Secondary sale to PE	Sanlam

# PE activity across Africa is expected to improve, spurred by higher economic growth leading to demand for expected expansion, and a marked improvement in acceptance of PE as an alternative to debt financing.

## Overall Private Equity Market Activity

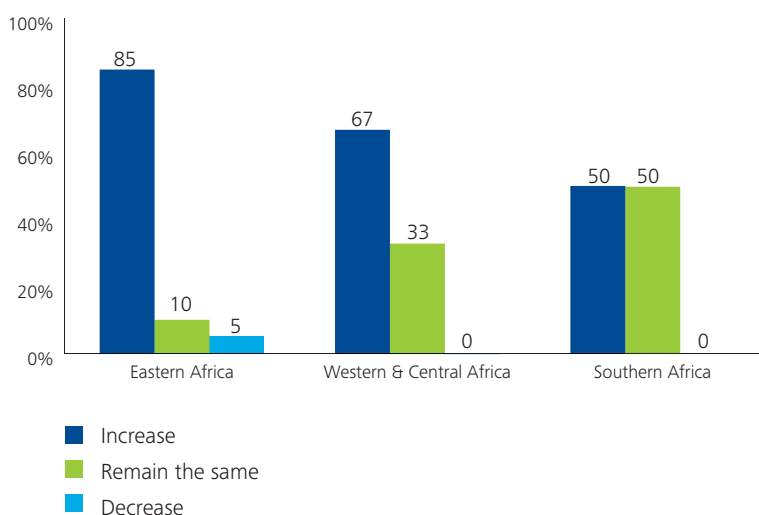
Respondents expect general PE activity in Africa to increase. Similar to last year's results, respondents expect increase in PE activity to be seen in the Eastern, Central and Western Africa regions. Reasons given for the expected increase included favourable economic growth, leading to higher demand for funding to ensure expansion and a marked improvement in acceptance of PE as a viable alternative to debt financing.

PE activity in Africa is mainly driven by strong macroeconomic fundamentals, rising consumer spending from a growing middle class, improvements in political governance and possibility for high returns on investments. According to Euromonitor International, consumer spending in Sub Saharan Africa (SSA) equalled nearly US\$600bn in 2010, accounting for almost 8% of all emerging-market spending, and is expected to reach nearly US\$1trn by 2020.

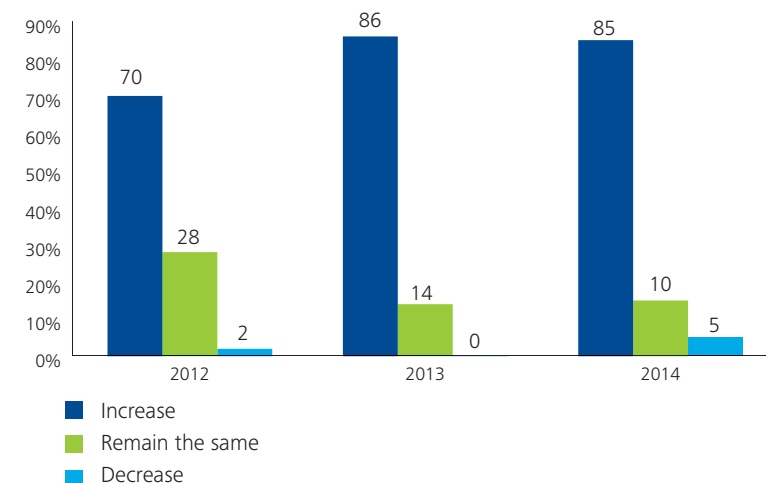
Given that PE is still in nascent stages in Africa, the region is expected to continue attracting investments buoyed by expectations of high returns. According to the African Development Bank, Private Equity penetration is still low in Africa. For instance, in 2013, Private Equity investments represented only 0.1% of GDP in SSA compared to 0.4% in India and 0.2% in China and Brazil.

In Eastern Africa, the establishment of more funds in the region and entrance in the market of commercial foreign investors with larger deal sizes is going to contribute to increased PE activity. This was reflected by 85% of respondents who see PE activity increasing in Eastern Africa over the next 12 months. Enablers supporting this trend include high projected GDP growth, a stabilising political environment, growing middle class, discovery of natural resources like oil and gas and increased infrastructure developments.

Overall Private Equity market activity across Africa over the next twelve months is expected to:

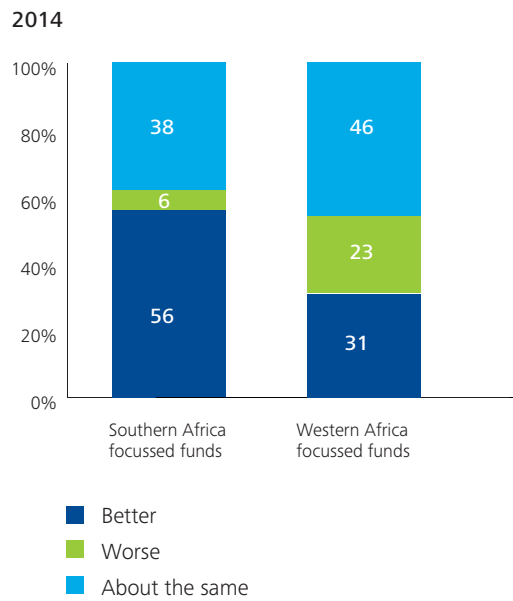


Overall Private Equity market activity in Eastern Africa over the next twelve months is expected to:



Eastern Africa performance against Southern Africa is expected to be better in 2014, a similar view held by respondents in 2013. However, compared with Western Africa, the majority (46%) expect the performance to be the same while 23% expect Western Africa to perform better than Eastern Africa. This is a significant change from 2013 where 87% of respondents expected the performance in Eastern and Western Africa to be the same. According to respondents, compared to West Africa, Eastern Africa's expected better performance is due to higher economic growth rates and large infrastructure projects in Eastern Africa while Southern Africa is considered more developed, hence presenting fewer opportunities for high returns.

**Expected Eastern Africa Performance Compared to Other Regions in Africa**

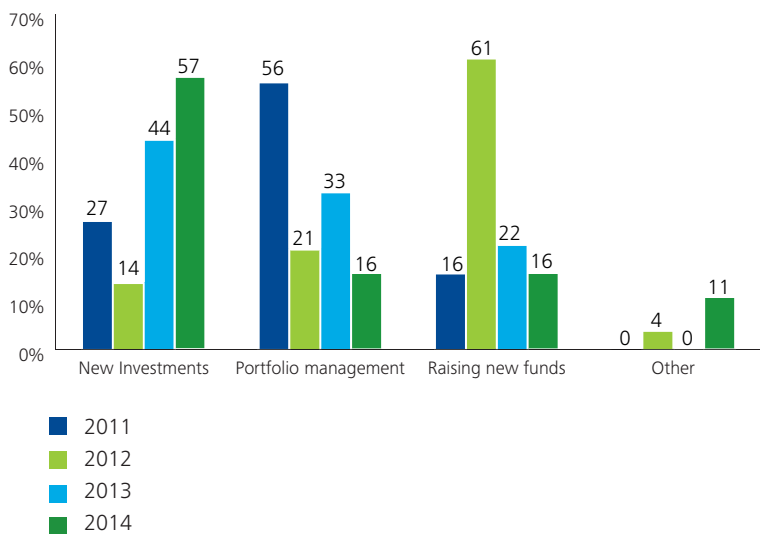


**Focus Areas**

Over the next year, most of the respondents are focused on new investments (57%). This reflects the decreasing trend in time spent on raising funds with respondents (majority being GPs) now focussed on deploying the funds raised to deliver on the promises made to the LPs and to fulfilling their mandate. The majority also explained that they had recently closed or were about to close their funds and were, therefore, within their investment phase.

11% included respondents whose time would be equally spent on either of the activities (buying, selling or portfolio management) while others indicated that time would be spent on other activities such as exiting investments and vocational training of SMEs.

**Over the next twelve to eighteen months, I expect to spend the majority of my time focusing on:**



### Private Equity in Sub Saharan Africa: Adaptations and Competitors

Much hype around the potential for PE in Africa is related to oft-cited GDP growth numbers. Growth is often equated to potential because so much of the growth in Africa is happening amongst private companies (as opposed to the shallow public markets) and amongst companies operating in prime sectors for PE investment, e.g. consumer-facing industries like FMCG and financial services.

But in practice, over the last five years, we have seen a noticeable gap between the growth of the PE industry and the growth of Africa's economies, with PE lagging just a bit behind in pace. This could be due in part to the crowded space for investment in private companies in which PE firms find themselves. In Africa, a number of investors play in the same space as PE firms, such as family offices, DFIs doing direct investments, corporate VCs, holding companies, asset managers, investment companies, and other financial services firms.

Many large companies in Africa are family owned, and many of them finance their own expansion with family wealth or have well-established relationships with local banks.

Family offices have less capital to deploy than PE funds, but they are good at doing deals quickly within and beyond their own sectors. They have less red tape and they can take on higher-risk deals where corporate governance standards are lacking – companies that would not pass a standard PE due diligence. And those are a lot of companies in Africa.

Holding companies, investment firms and asset managers have more flexibility to make opportunistic deals and to hold companies for longer without the pressure to exit. We have seen a lot of PE funds transition to the holding company model in Africa – Brait in SA, Chayton Capital in agribusiness, and Africap in microfinance. This signals another issue that we have raised in our analysis several times – that the traditional Private Equity model is not perfectly suited to Africa, where companies take

longer to develop, are less formal, where economic and political volatility can make it difficult to exit on time, and where debt and mezzanine are often easier types of financing to wield than equity, from a risk hedging and cash flow perspective. There is a lot of money that moves in Africa through investment firms like Centum and TransCentury, using a model similar to PE and certainly playing in the same space, competing for similar deals and with very strong local networks.

Related to the grey area of defining what PE really is in Africa, we have also seen plenty of captive vehicles doing deals in the PE space. Many of these are housed by banks and financial services firms, others in the corporate venture capital space, and others via foundations.

The same applies to high volume lenders like BPI, Grofin and other mezzanine funds that offer hands on investment, or simply less restricted investment, mostly to SMEs, via some form of debt. It is much easier for these firms to get deals done than for a traditional SME PE fund even though many have questioned their ability to generate and capture real value.

Not many people agree on whether impact investors should be classified as Private Equity funds, but they have certainly entered the PE space. While many of these look for deals that would be too small or unprofitable to draw traditional PE players, there is some crossover, particularly in consumer-facing businesses that service low-income demographics, such as financial services, off-grid energy, health care and housing. Because so many PE firms carry DFI capital, these GPs must contend with developmental mandates to a lesser degree, but in a similar way as impact funds.

We have also seen un-classifiable investment platforms enter the PE space, such as Atlas Mara, a specialised investment vehicle launched in 2013 by former Barclays head Bob Diamond and Ashish Thakkar, founder of the Uganda-based Mara Group. Atlas Mara will invest in financial services acquisitions across Africa, with a focus on close involvement in operations post-takeover.

Real estate and construction – integral to Africa's expansion boom – are overflowing with capital from local specialist firms, direct investments by local pension funds and insurance companies, local investment clubs, and local family wealth. This does not leave much room for PE investors.

DFIs love to do direct investments: CDC recently changed its strategy to focus more on direct investments and less on support of external funds. Despite their development mandates, DFIs are also self sustaining and are therefore looking to make money via large, profitable deals. This puts them squarely in the center of a very crowded space, in competition for PE funds looking for scarce large deals. For this reason, we often see DFIs co-invest on large deals with GPs. This is good for the businesses, but less optimal for PE management fees. That said, as co-investors DFIs do inspire confidence, and have helped to bring other foreign investors into Africa who could serve as LPs for PE funds in the future.

It is worth bearing in mind that the PE industry still quite young in sub Saharan Africa, and therefore still finding its feet. There will probably be more modifications, but we expect its influence in relation to other types of investors to grow as institutional investors become more familiar with the asset class, and as businesses formalise and become better PE targets. PE is a great way to mobilise lots of cash, but funds will need to prove their track record, deepen their local networks, and make businesses and investors more comfortable before they can overtake more familiar sources of local capital.

# 2 Economic Climate

## Across the African regions, investors are somewhat less optimistic than last year, with a significant increase in those who expect the economic climate to remain the same

SSA is one of the fastest growing regions in the world. According to the World Bank, GDP growth in SSA is projected at 4.9% in 2013, rising to 5.3% in 2014 and 5.5% in 2015. Fast paced economic growth is to be supported by strong domestic demand, increased investments and higher production in the mineral resources, agriculture and service sectors.

The majority of the respondents expect the general economic climate in Africa to improve or remain the same in the next 12 to 18 months. In 2013, Eastern, Western and Central Africa scored above 75% improvement expectation, so the optimism levels have declined.

30% of respondents in Western and Central Africa expect the region to post higher growth while 61% expect the region's economic growth to remain the same. The respondents in Western and Central Africa identified political instability and challenges in governance reforms as key downside risks to higher growth.

Eastern Africa's improved economic growth is expected to be supported by political stability, especially after the peaceful elections that were held in Kenya in March 2013, and given that there are no major political events scheduled to take place in the region in 2014. Recent oil and gas discovery in Kenya, Tanzania and Uganda coupled with increased investment in infrastructure developments in the region are also expected to contribute to strong economic performance.

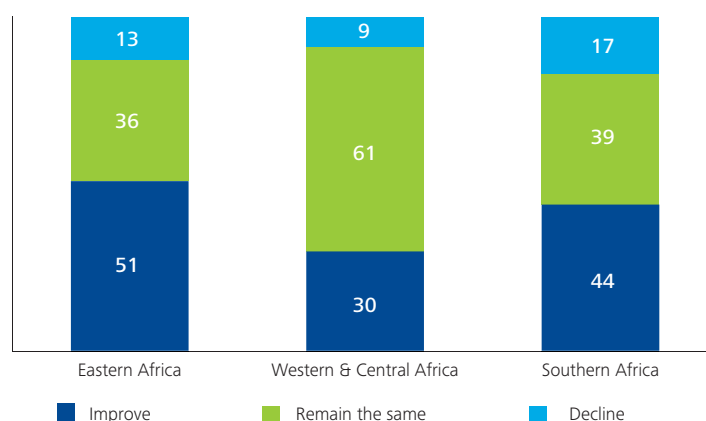
The World Bank forecasts Kenya's growth to reach 6% in 2014, the highest growth since 2007, when the economy grew by 7%. The key drivers of this growth are expected to be increase in aggregate demand fuelled by strong consumption and investment growth.

South Sudan's economic performance in 2014 is uncertain following political conflict spilling over into civil war in late 2013. Respondents were equally divided in their expectations of the country's growth prospects in 2014. In 2013, 17% of respondents expected South Sudan's economy to decline, reason being the political tension between North and South Sudan at the time.

Respondents were most buoyant about Ethiopia: 89% expect the economy to improve, with infrastructure developments and strong macroeconomic fundamentals expected to continue spurring the country in its growth trajectory.

Rwanda and Burundi saw a decline in expectations of improvements in part, due to fears over the political stability going forward in the two countries. The key drivers of economic growth in Rwanda are expected to be the increased investments in the country coupled with the ease of doing business. The 2013 World Bank Doing Business Report ranked Rwanda 52 out of 185 globally and 9th in SSA on ease of doing business.

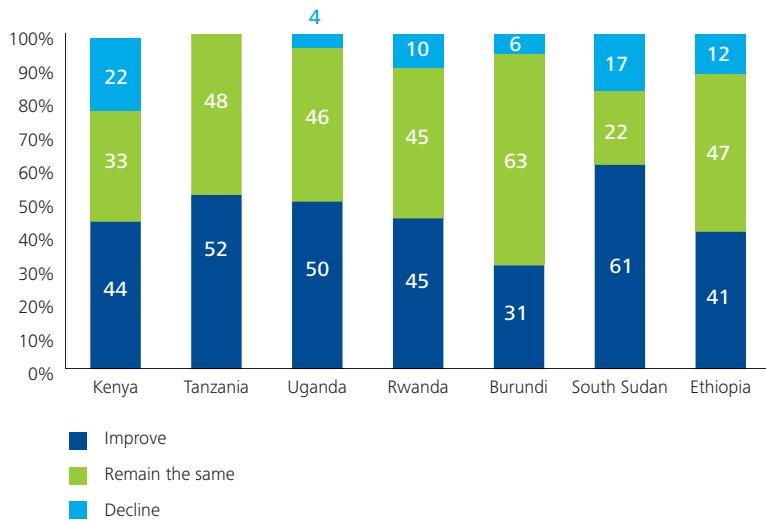
Expected overall economic climate in Africa in the next 12 to 18 months



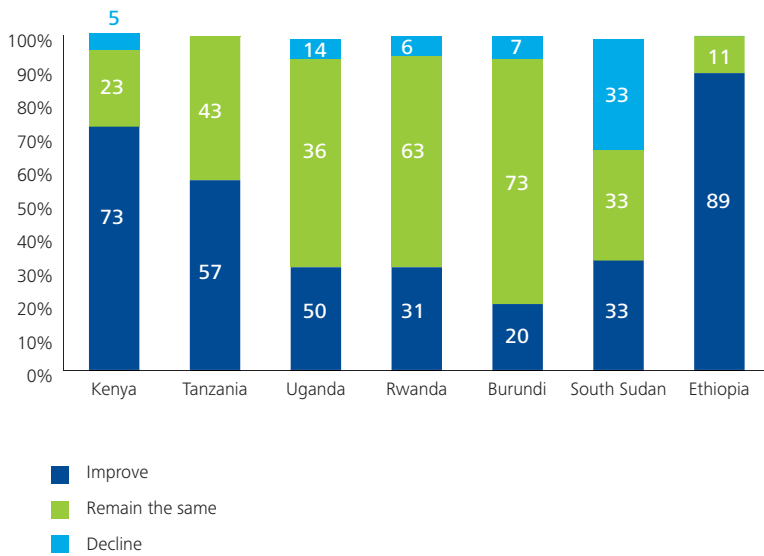


I expect the overall economic climate in Eastern Africa in the next 12 to 18 months to:

2013



2014



### What Is Private Equity Doing About Risk?

What does risk look like in the New Africa, with its impressive headlines on growth, investment, and the emerging middle class? The truth is that risk in Africa today is murkier than ever: lessened by reforms, muddled by continued misperceptions and shifting reputations. What does this mean for PE investors – buyer beware? Yes and no. You just have to know where to look, and who to ask.

Many of the elements that characterise African Private Equity portfolios are also their principal risk factors. Investors must plan for longer term engagements: projects in Africa can take triple the time of other markets to get off the ground from inception to income flow. Most deals are growth investments that require hands-on engagement. And the prominence of development finance in African PE means that investors must further contend with impact mandates and consider what acceptable risk looks like for any DFI partners.

**Operational risks** are the number one concern for most PE investors in Africa. GPs want to work with strong companies and good management teams, but those can be difficult to find in what is still a relatively immature corporate environment. The lack of larger deals and resulting focus on SME investing lessens the amount of track record information that investors have to work with. Many smaller deals are also minority stakes, and in those cases it is especially important to understand the people you are doing business with. Reputational risk looms large, and can become particularly critical for sensitive DFIs who answer to tax payers in their home markets. Investors need to assess the type and extent of corruption risks they face. In principle, corrupt staff members can be replaced. But if corruption is intrinsically linked to the company, it will be hard to work around.

**Political risk** today is much more nuanced than exploding headlines, and often linked to corrupt local politicians who like to disagree with the ‘nature of the investment’. Citizens are also legitimately becoming more vocal, helped by stronger media and, importantly, by their ability to expose wrongdoings on social media. However, even for the best behaved investors who tick all the right ESG boxes, risks remain: In a corrupt environment, it is still easy for vested interests to mobilise the local population against investors, and feed a distorted media campaign. This is a particular challenge for any investment involving land rights, whether in extractive industries or in large-scale commercial agriculture: land is a notoriously emotive and mismanaged asset.

**Regulatory risk** in Africa varies widely across sectors and countries – as do corresponding political risks. The risk of corruption and the risk of government interference in a deal will increase commensurate with both the strategic status of the sector in the country and also with the size of the sector. For strategic sectors such as oil and gas, mining, infrastructure, land-related agribusiness or financial services, investors face increased risk of political interference, hidden ultimate beneficial owners, corruption and legislative change. Larger, expanding, multi-jurisdictional sectors like retail and fast-moving consumer goods offer a happy medium, with more opportunities and less vulnerability.

**Due Diligence:** Most PE firms do initial due diligence in house. The model, in any emerging market, is very relationship driven and even more so in Africa, where all investors will need to build up capacity on the ground quickly to keep up, whether through local offices, on-the-ground teams, fly-ins or local partners. There is a historical impression that you need to identify a Mr Whatever-the-Country is that you’re working in who can open doors for you, but that is changing. More PE funds do the ground work themselves these days.

**Risk Insurance:** Once in bed, political risk insurance as offered by MIGA and ATI or guarantee schemes can hedge further risks, but PE funds have not traditionally gone this route. Cost is a disincentive for GPs and LPs alike – just a few percent per annum can cut into your returns. And for private investors, most of whom still avoid real frontiers like CAR, insurance is not enough to make them comfortable with the risk. At that level, you're either in or you're out. Many investors in Africa hedge using mezzanine structures, pure debt or convertible loans.

**Veterans and Newcomers:** Overall, seasoned investors that have been in Africa for years – Aureos (now Abraaj), ACA in Nigeria, or ECP to name a few – are better equipped to manage these risks. They are more accustomed to long-term investments, more familiar with local regulations, have more support built up in house, and more deeply rooted networks. They may have also already made mistakes that taught them crucial lessons. But there are so many opportunities across Africa that even PE outfits new to the market can find their way around it as long as they invest time and resources identifying the right deals for their investment profile and finding partners they can trust.



# 3 Deal Activity

## Looking Forward

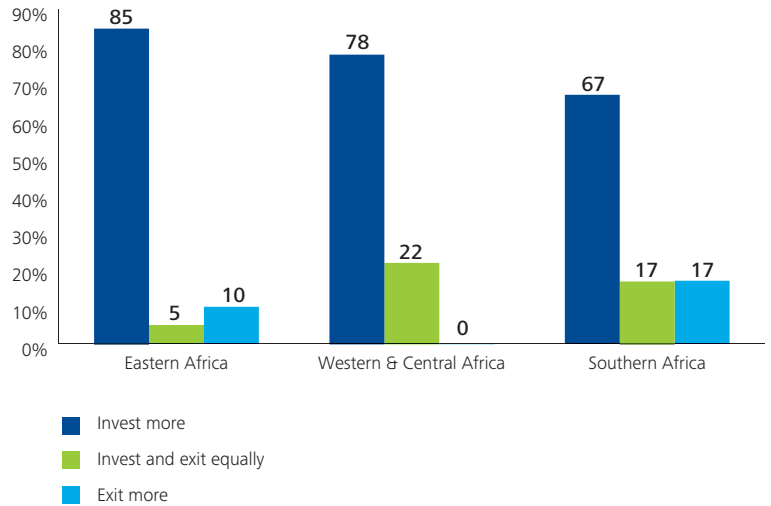
### Investment Readiness

PE activity in Africa in 2014 is expected to be concentrated more on investing rather than exiting. This is reflected by increased PE investment in the region attracted by strong projected economic growth, increasing demand from a growing middle class and improved awareness of PE by entrepreneurs and potential target companies.

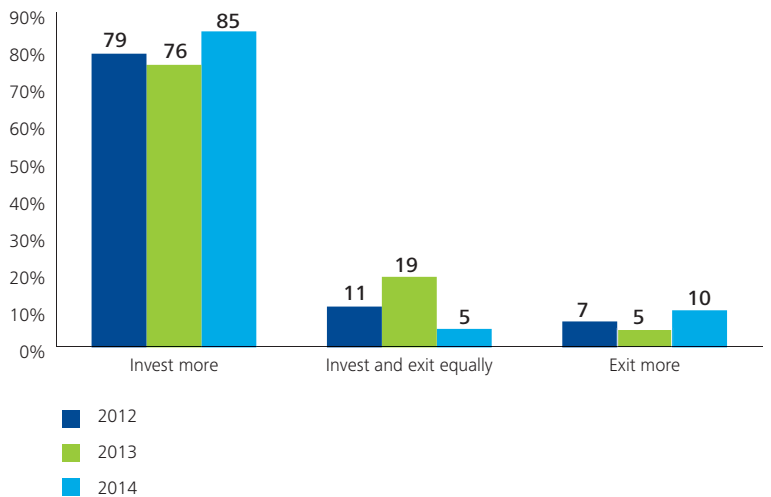
Consistent with the view by the majority of the respondents that their time would be spent more on new investments in the next 12 months and that PE activity is expected to increase generally across all regions, respondents expect to be buying more in 2014 rather than exiting.

Due to the increase in the number of new players in the Eastern Africa PE market, the survey results indicate that there will be more buying than selling. The majority of the GPs report that their funds are in the investment and strategic growth phases. In 2014, a higher number of respondents indicate that they will invest more.

Over the next twelve months, I expect to:



Eastern Africa: Over the next twelve months, I expect to:

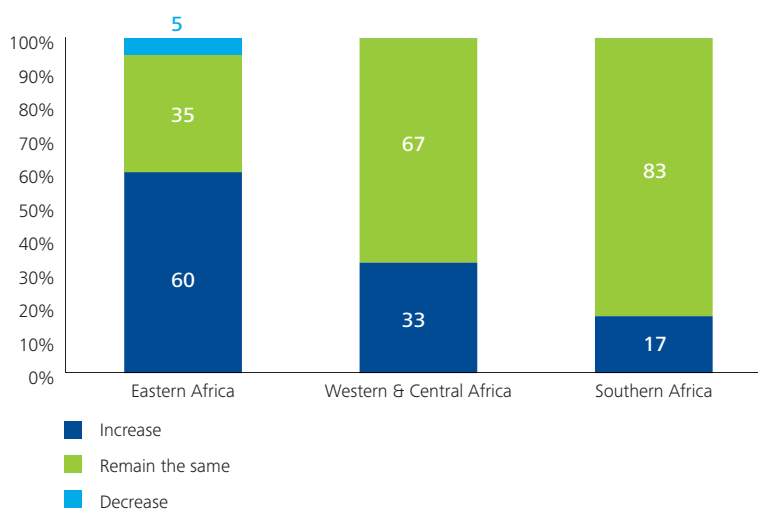


### Entry Multiples and Competition

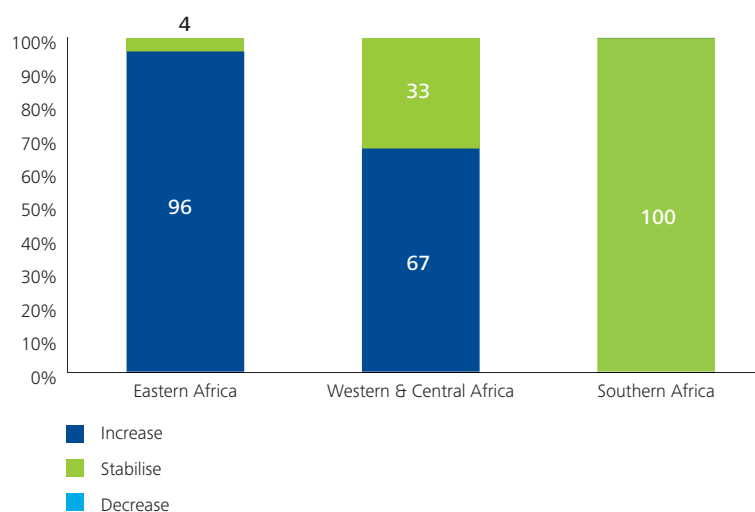
Across all regions, respondents expect competition and entry multiples on transactions to either increase or remain the same.

In Eastern and Central Africa, the majority of the investors expect entry multiples on transactions to increase. Competition for new investment opportunities is also rising across all regions, except Southern Africa, where respondents expect competition to stabilise. With the continued development of the PE market in Eastern Africa, the pace of increased investment has not been matched by a rising number of investable companies. As such, lucrative deals will continue to attract a lot of attention, hence pushing up entry multiples and making 'cheap buys' difficult.

Over the next 12 to 18 months, I expect entry multiples on transactions to:

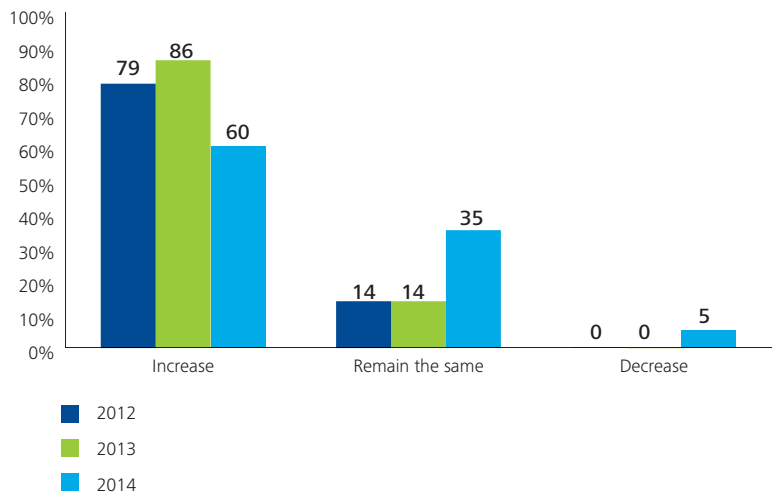


Over the next 18 month, I expect competition for new investment opportunities to:

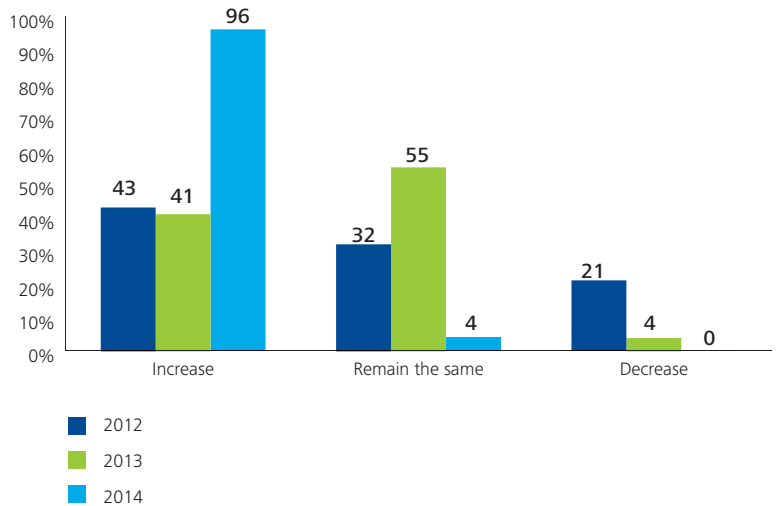


In Eastern Africa, 96% of investors expect increased competition in 2014 compared to 41% in 2013. Respondents said that the main reason for this was the expectation that the growth rate in the number of PE funds will be higher than the growth in opportunities. The increase in the number of fund managers, larger funds and more strategic investors without a corresponding increase in the number of deals will lead to stiffer competition.

Over the next 12 to 18 months, I expect entry multiples on transactions in Eastern Africa to:



Over the next 18 months, I expect competition for new investment opportunities in Eastern Africa to:



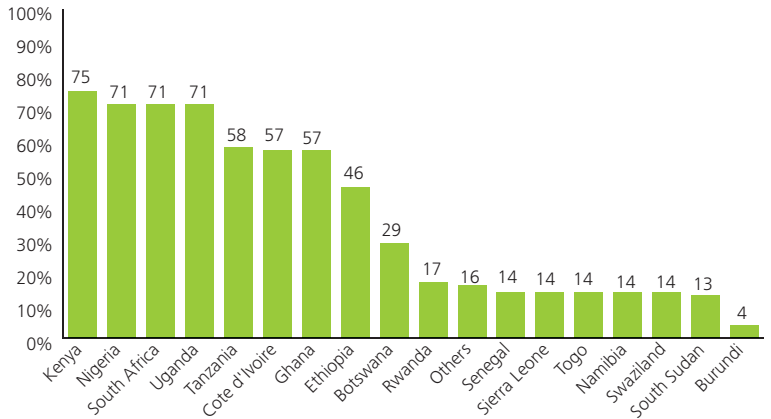
**Country focus**

**2014 investment focus per country**

The main focus of investors in SSA continues to be the key economies of South Africa, Nigeria and Kenya where PE players seek to ride on established systems and more certainty, i.e. lower risk.

In Eastern Africa, as was the case in the previous surveys, Kenya ranked first as the country that most investors are focussing on. It was followed closely by Uganda and Tanzania. However, these three countries have experienced a decline in investor focus compared to 2013. There is also growing interest in Ethiopia, which has recently started loosening its strict policy on foreign ownership/investments.

**2014 Investment Focus per Country in the Region**

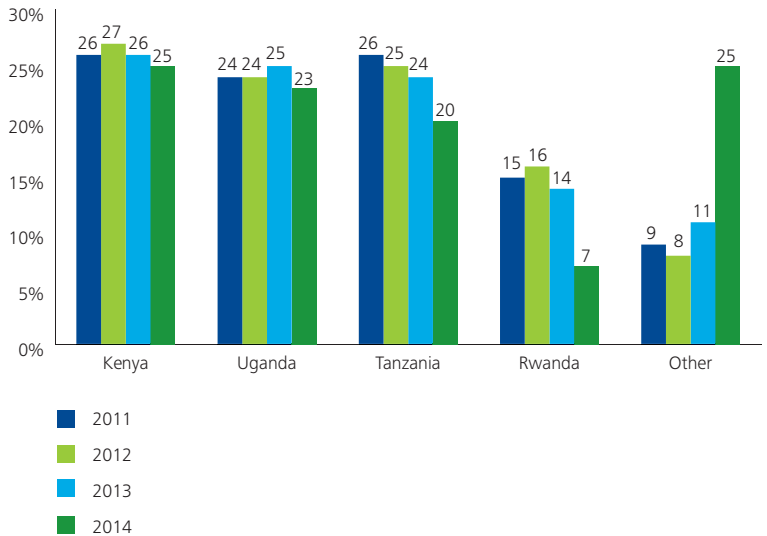


**Investment Focus in Eastern Africa: The Trend**

Overall, the core EAC economies (Kenya, Uganda and Tanzania) have received almost equal level of attention from investors. There was a decrease in focus for Tanzania and Rwanda in 2014, although this could be the result of a different mix of respondents.

The 'other' category includes countries like Burundi, Ethiopia and South Sudan. There was a sharp increase in 2014, with the main contributor being Ethiopia. In Eastern Africa, it was the country in which majority of the respondents were most optimistic about in terms of economic growth. Favourable economic prospects and loosening of strict policies, e.g. foreign exchange restrictions and unfavourable labour laws, are seen as driving the increased focus in the country.

**Country Focus in Eastern Africa in the Next 12 to 18 Months**

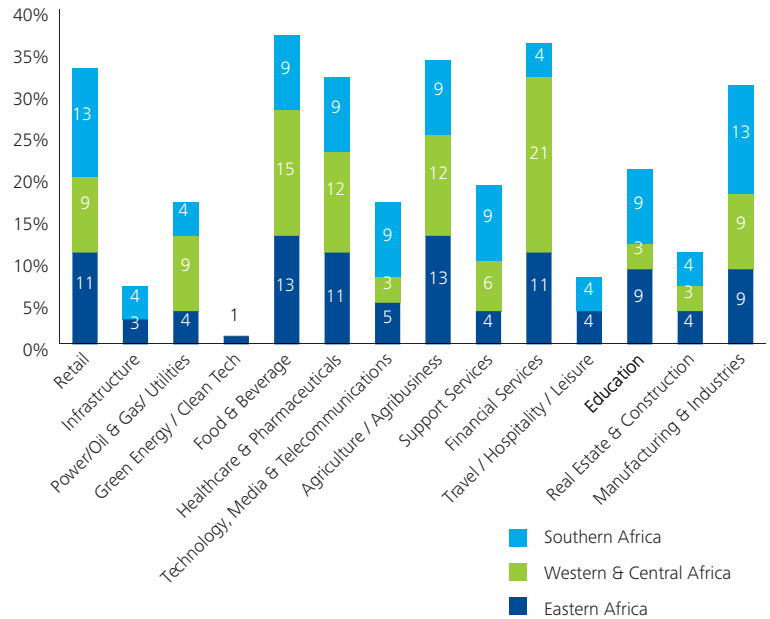


### Regional Sector Focus

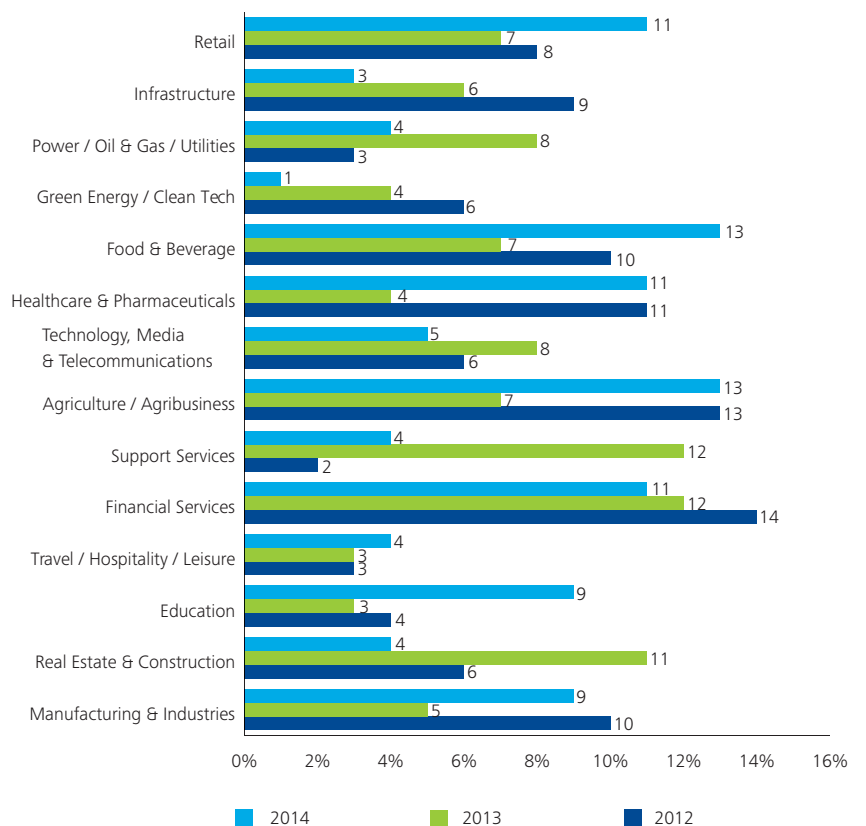
In Eastern Africa, PE investor focus is on the food & beverage, agribusiness, retail, healthcare & pharmaceuticals, and financial services sectors. In Western and Central Africa, the focus is mainly on the financial services, food & beverage, healthcare & pharmaceuticals, and agribusiness. In the Southern Africa region, focus is on manufacturing, food & beverage and retail, all of which are consumer driven and have a direct link to a growing middle class.

There was a significant decrease in focus on real estate, reflecting recent reports indicating that the previous boom in the industry may be tapering off. While the financial services sector is still thriving, it showed a slight decline in interest in 2014 compared to 2013. Interest in the support services, green energy, power/oil & gas/utilities and infrastructure have all dropped in 2014 compared to 2013.

Sector focus in the next 12 to 18 months



Sectors to focus on in the next 12 to 18 months in Eastern Africa





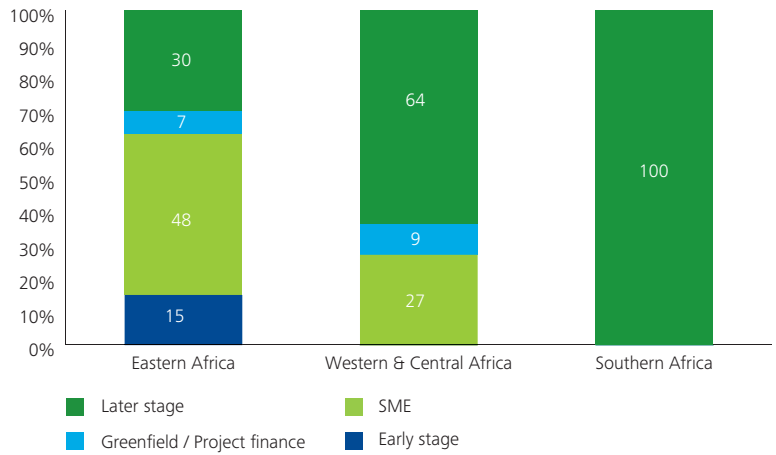
**Strategy and Size**

Most of the respondents in Africa target later stage companies and SMEs. According to the survey data, only investors in Eastern Africa are willing or targeting to invest in early stage companies. Southern Africa investors will target later stage companies.

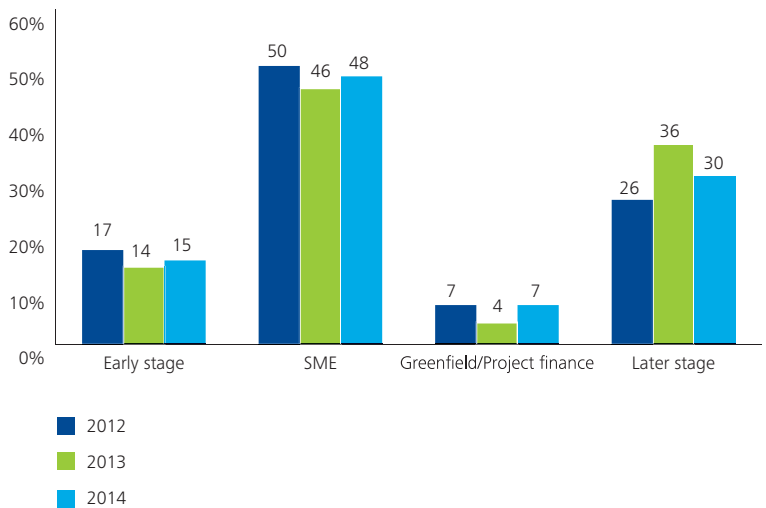
Reflecting the characteristics of the Eastern, Western and Central African economies, which are characterised by a large number of SMEs and a relatively smaller number of large, mature corporates, the majority of the investors will target SMEs in these regions. Probably for the same reason, PE investors in Eastern Africa, Western and Central Africa are the only ones that have shown interest in greenfield/project financing.

Comparing 2013 and 2014, we find that there has been slightly increased interest in SMEs in Eastern Africa region (from 46% in 2013 to 48% in 2014).

**In the next eighteen months, I expect to target the following companies:**

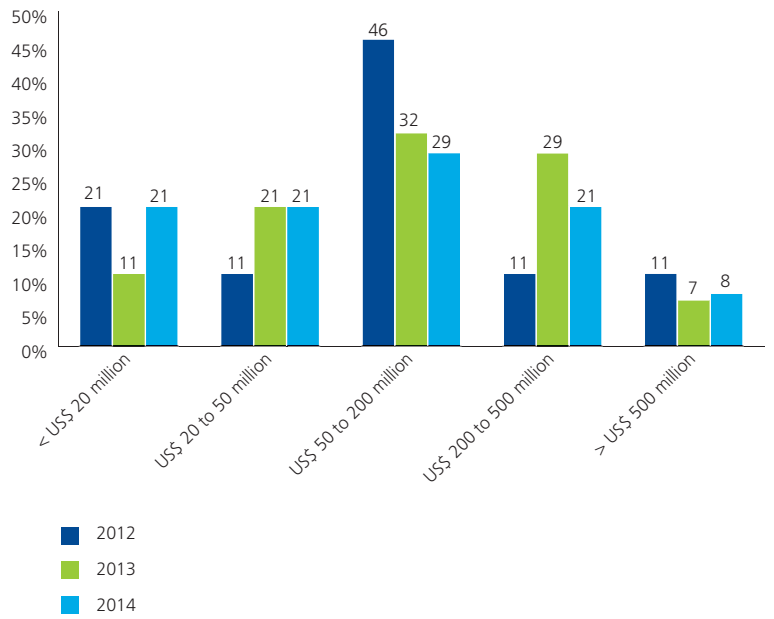


**In the next eighteen months, I expect to target the following companies in Eastern Africa:**

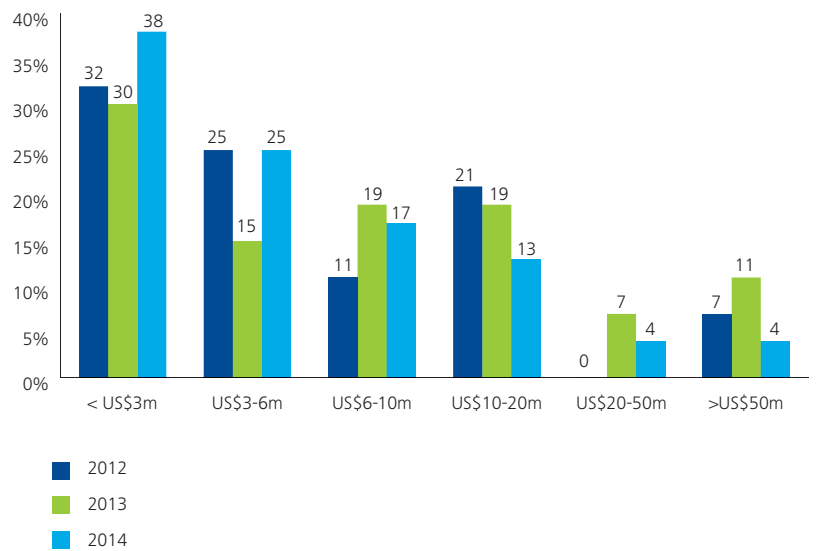


The majority of respondents (still) manage funds worth between US\$50m to US\$200m.

### Total Size of Fund Managed



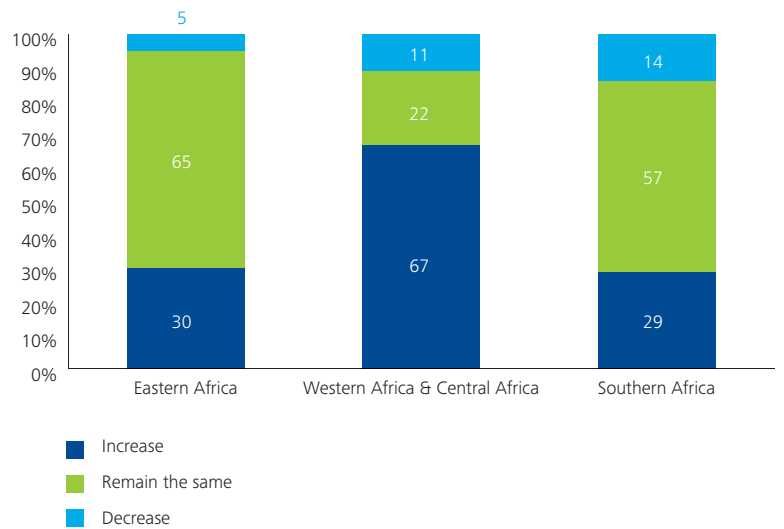
### Investment Size per Transaction



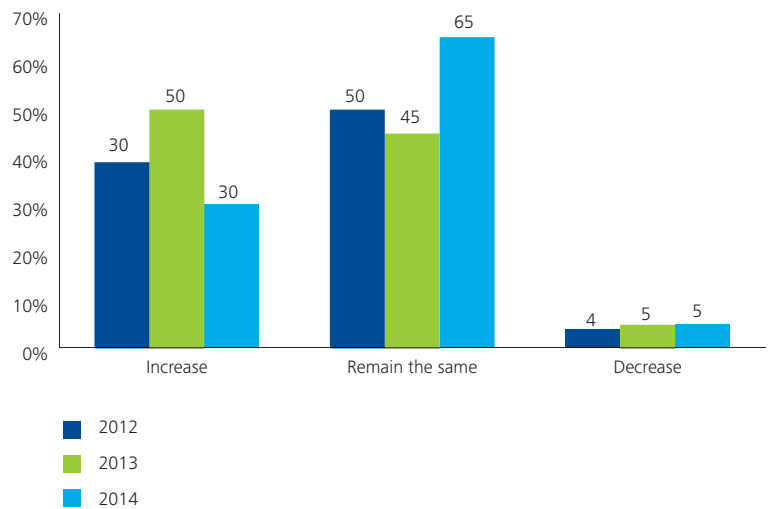
Average sizes of transactions are expected to remain largely the same in Eastern and Southern Africa, but to increase in Western and Central Africa.

In Eastern Africa, 65% of respondents believe that there have not been significant changes in the market structure to result in changes in transaction size. The majority believe that there will be an increase in opportunities across all the sectors of the economy and in businesses of all sizes.

Over the next twelve months, I expect the average size of transactions regionally to:



Over the next twelve months, I expect the average size of transactions in Eastern Africa to:



### Sector Snapshot: Financial Services

Financial services has fast become a favourite industry amongst Africa-focused growth funds. Nearly every African growth story report cites the sector's potential, which is not surprising as the financial sector is the backbone to Africa's fast economic growth. Much of the focus thus far has been on banks. Where market growth is driven by consumption, banks benefit from both the corporate and, helped by advances in technology, consumer finance sides, effectively double dipping. Investors are also experimenting with insurance companies and payment processing – both underdeveloped sub-sectors with enormous potential.

**Banks:** For PE investors, banks offer the potential for large deal sizes – hard to come by in Africa – and consistently strong growth. In 2011 we saw the monster USD750m Union Bank recapitalisation, one of the largest deals in African PE history, where an ACA-led consortium benefitted from the overhaul of Nigeria's overstretched banking industry. Consortium member Africa Development Corporation (ADC) have now changed their strategy to focus entirely on bank investments.

Tightening regulations in many key markets are improving investability. Following crises in the 1980s and 90s, Kenya's banking sector is now well-regulated, with strongly capitalised institutions keeping transparent books. With its more recent banking crisis, Nigeria is heading quickly in the same direction. Recently heightened capital requirements in Nigeria and Ghana have also created opportunities for PE investors to supply the funds needed for banks to shore up stocks and expand.

**Insurance:** Insurance deals entail an entirely different set of considerations for PE investors: In principle, under-penetration presents huge potential for growth, but uptake is still slow. As banks have done, insurers are experimenting with technology to reach lower income customers. In February 2013, PE house

LeapFrog Capital invested in BIMA, a company pioneering mobile-based delivery of insurance services in Africa and Asia. BIMA's mobile services can bring premiums on life, accident and health insurance down to as low as USD0.20-6 per month.

The entire industry remains very green, and companies are still learning how to properly price their own products. In many markets, health and motor vehicle insurance turn out to be loss leaders that provide a cash base for investments that bring in real revenue. GPs must therefore also assess an insurance team's ability to manage a diversified investment strategy resilient to local economic shocks. As with banking, regulation has a lot to do with PE opportunities in insurance. In 2012, the new Kenyan Insurance Act capped individual ownership at 25%, forcing groups to restructure and bring on new investors – ADC's investment in Resolution Health was one of the results. The act also requires insurers to separate general and life insurance products under different businesses, opening investment opportunities through demergers.

**Payment Processing:** The final frontier in African financial services appears to be payment processing – a sub-sector with enormous growth potential, but that is still largely a greenfield market. Actis jumped on this nascent opportunity in 2010 by establishing a start-up platform company in Egypt, Emerging Markets Payments Holding (EMPH), which has since made four acquisitions of payment services companies in Africa and the Middle East, two of these in South Africa. Nigeria is already leapfrogging payments technology, having introduced chipped smart cards to replace magnetic strips in 2011. In the same year, PE houses Helios Investment Partners and Adlevo Capital invested over USD100m in Interswitch, a Nigerian integrated payment and transaction processing company.

**Exit Options:** Both banks and insurance companies are also more likely to be listed or seeking an IPO than other traditional PE targets. This can make it easier for a GP to exit the investment, but may also add an extra layer of red tape to an already highly regulated sector. GPs exiting listed banking or insurance assets will need to contend with central bank and insurance regulator stipulations, as well as those imposed by the capital markets authority. In some countries, if you want to sell more than 20-25% of a listed bank, the stock exchange may require a takeover process where the buyer must bid for all of the equity – a problem for someone who only wants a minority share. That said, we have seen successful PE exits from listed banks. And non-listed entities offer attractive exit routes through eager strategic buyers.

**Why respondents in Eastern Africa expect the size of transactions to remain mostly unchanged**

‘There haven’t been significant shifts in the market to warrant changes in size. The only difference is that more and more companies will emerge to increase the number of opportunities.’

‘Investment opportunities will arise across all sectors of the economy in businesses of all sizes, from start-ups to mature companies.’

**Why respondents expect the size of transactions to increase in Eastern Africa**

‘Most transactions focus on larger and relatively well-developed companies that will keep on growing.’

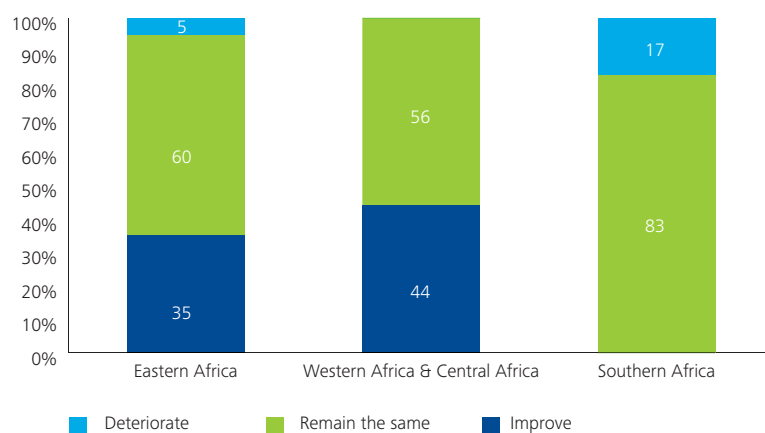
‘More mergers and acquisitions are likely to take place. Additionally, businesses are looking to expand within East Africa and will require larger funding to support this growth.’

# 4 Fundraising

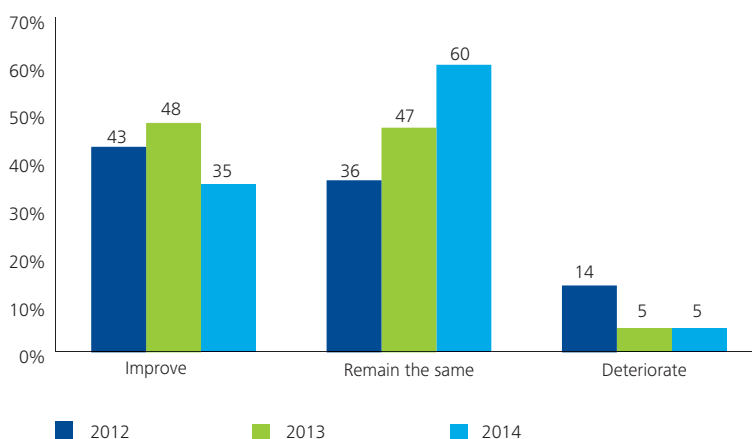
Across the regions, investors are cautiously optimistic, with 35% of respondents stating that they expect the fundraising environment to improve in Eastern Africa. In Western and Central Africa, a higher number of investors expect the fundraising environment to remain the same.

Africa is still seen as a viable risk by most investors, given the track records from investors already in the market, strong regional fundamentals, relative political and social stability and growing infrastructure investments. Some respondents were a little more cautious, stating that it will be a tough sell due to the many funds in the market fighting for investors.

Over the next 12 to 18 months, investors expect the fundraising environment for Private Equity to:



Over the next 12 to 18 months, investors expect the fundraising environment for Eastern African Private Equity to:

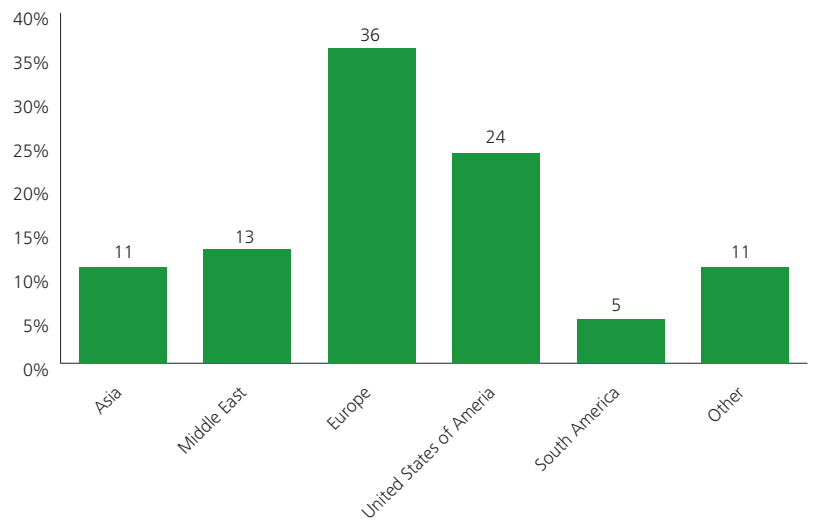


### Debt and Capital Raising

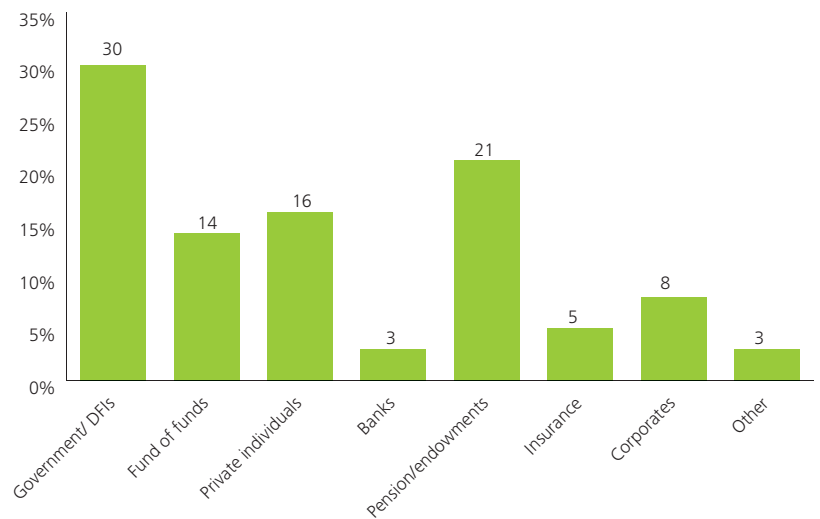
36% of the respondents stated that they would seek funding from Europe, while 24% would lean towards the US. Some respondents also stated that they would consider seeking funding from local pension funds in East Africa, specifically Kenya.

The most popular sources of third party funding were governments and DFIs at 30%.

If you intended to raise funds within the next 12 months, which geographical source would you raise capital from?



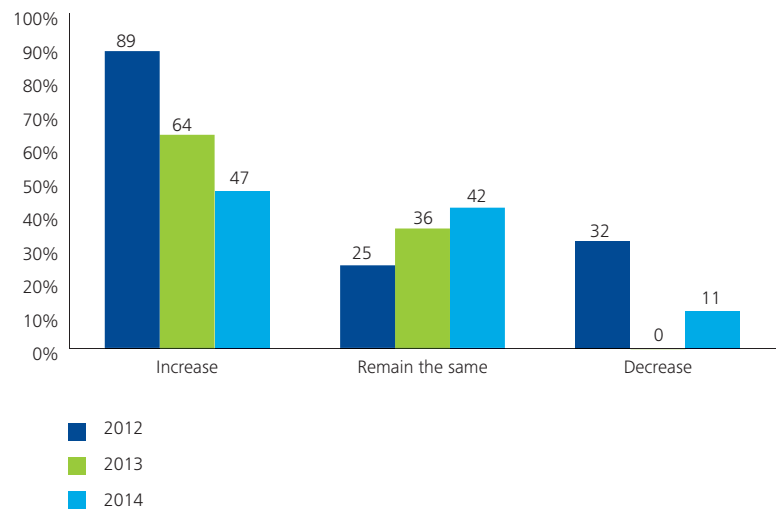
If you intended to raise funds within the next 12 months, which source of third party funding would you raise capital from?





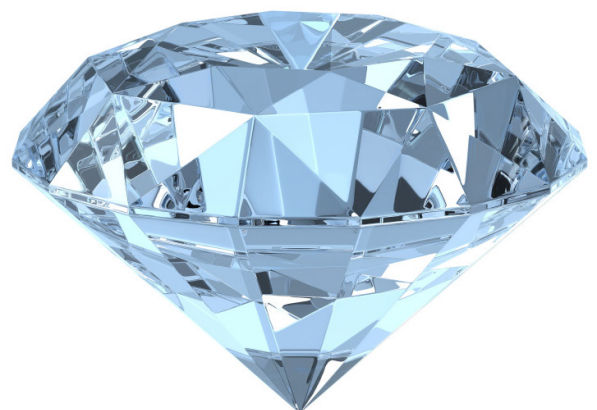
Compared to 2013, there has been a decline in confidence in investors' expectations of access to debt finance for transactions in 2014. Only 47% of the respondents expect the access to debt finance to improve in 2014, down from 64% in the 2013 survey results. According to some respondents, this is because of the perceived high risk profile of lending to African companies.

Over the next eighteen months I expect access to debt finance for transactions in Eastern Africa to:



**LP Insights**

- East African fundraising is still very much dominated by Development Finance Institutions (DFIs), who are mandated to invest in least developed regions such as sub-Saharan Africa (excluding South Africa).
- DFI investors are attracted to East Africa's strong growth and demographic dynamics. In recent years, we are seeing more joint DFI-commercial LPs deal activity in the region.



### Sector Snapshot: Investing in Healthcare – Upmarket, Downmarket

Private equity investments in healthcare are driven by two dynamics: First, many governments on the continent are not very strong on public service delivery, so as soon as people can afford to pay for an alternative, they will do so. This ties in with the second dynamic, Africa's much publicized nascent middle class. At the lower end of this demographic (which may look quite different from what one would typically expect the middle class to look like), service delivery is helped by new technologies, now rendering an even lower-income demographic more commercially attractive to investors. And of course, a more conventional middle class creates a significant demand for quality healthcare and related services.

Abraaj Group manages a dedicated Africa healthcare fund – this was initially set up and managed by Africa PE fund manager Aureos who were acquired by Abraaj Group in 2012. Another fund fully dedicated to healthcare in Africa is the Netherlands based fund Investment Fund for Health in Africa (IFHA), with investments in Nigeria and East Africa. And sector-agnostic funds have also made a number of investments in healthcare and related industries. The number of deals is still limited, but some of the deals in recent years illustrate investor interest and investment potential:

- On the retail end, SME PE funds have invested in pharmacy chains, e.g. Fanisi Venture Capital Management in Halton's, a Kenyan pharmacy chain that aims to use the funding to expand their branch network across the country. Fanisi have also invested in Rwandan Sophar, a wholesaler of pharmaceutical products. Abraaj Group acquired a stake in Ugandan Vine Pharmaceuticals.
- Healthcare groups are a popular acquisition target: Abraaj Group's healthcare fund has announced an investment in Nairobi Women's Hospital in November 2013. Abraaj (back then as Aureos) already invested in Kenya Avenue Group, also a mid-market healthcare provider, in 2011. In Botswana, Venture Partners Botswana invested in the Ongwediva Medipark. Often these acquisitions are still middle-class focused companies, but interestingly, more PE

funds have indicated an interest in companies that provide services to the lower-income demographic of the market.

- Africa Development Corporation (ADC) acquired a stake in Kenyan healthcare insurer (now full service insurance firm) Resolution Health in late 2011. In February 2013, Impact investment fund Leapfrog made an investment in emerging markets insurance firm BIMA. In sub-Saharan Africa, BIMA is present in Ghana, Tanzania, Senegal and Mauritius and focuses on using mobile phones as the delivery channel for their insurance products to reduce the premium price and make the services more affordable. BIMA acts as an intermediary between their low-income target clientele and insurance firms to help the latter reach this demographic.
- IFHA opened the PE play in healthcare centres in 2010 by investing in AAR, at that time covering both health medical centres and health insurance. In the recent past the activities were split into different companies, both still AAR. IFC has invested in 2013 in the AAR health insurance business. AAR, backed up by IFHA have acquired a hospital in Uganda.

This indicates that private equity funds do see the commercial potential in the healthcare industry. However, it is worth bearing in mind that the private equity industry in sub Saharan Africa itself is still a young industry, and the vast bulk of funding to PE firms in sub Saharan Africa comes from development finance institutions (DFIs) who will consider developmental alongside commercial objectives. Commercial capital is still cautious and looking for a track record of successful exits as well as, often, scale.

# 5 Exit Environment

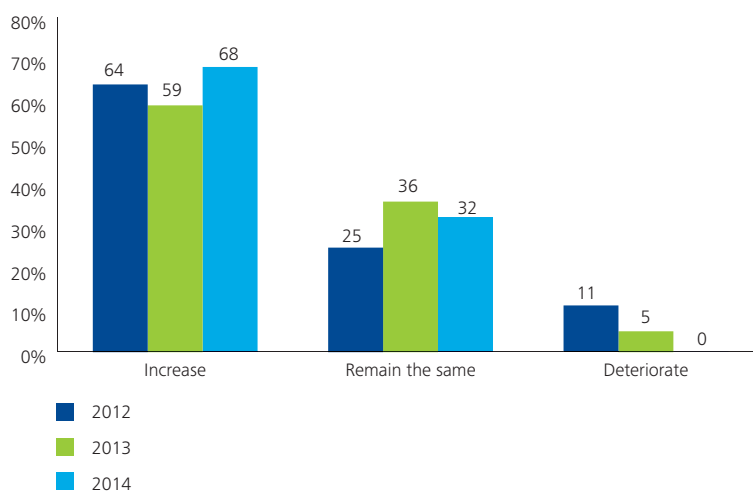
68% of respondents expect Eastern Africa's exit environment to improve over the next eighteen months, as large multinationals and pan-African companies looking to make an entry into the region, create opportunities for strategic sales.

Moreover, in Eastern Africa, 65% of the respondents feel that there will be an increased number of exits in 2014.

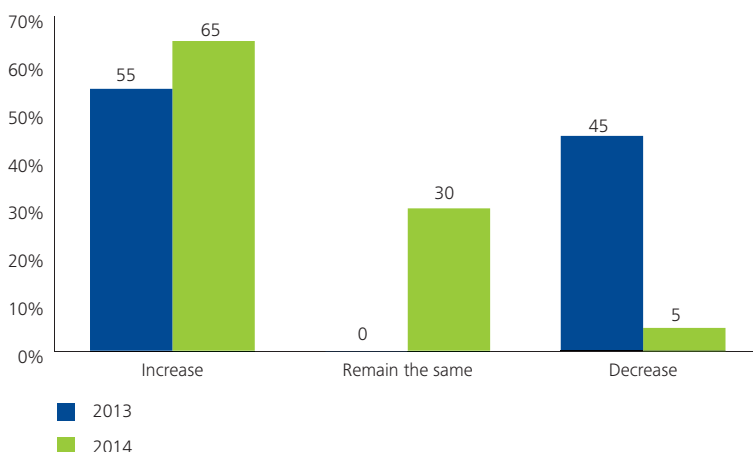
The most dominant exit routes across Africa are sales to strategic investor followed by exits via secondary sale to other Private Equity funds. It is interesting to see that 12% of the respondents see IPOs as a viable exit option in Eastern Africa, an improvement compared to previous years' results. This could be a result of the improved stock performance in recent years. However, most respondents still think IPOs are less probable due to the lack of sophistication of the capital markets.

In Eastern Africa, the most viable exit route is still seen as selling to a strategic investor, as indicated by 33% of the respondents. Respondents are optimistic about the exit environment because of more funds and trade buyers looking for investment opportunities in Eastern Africa.

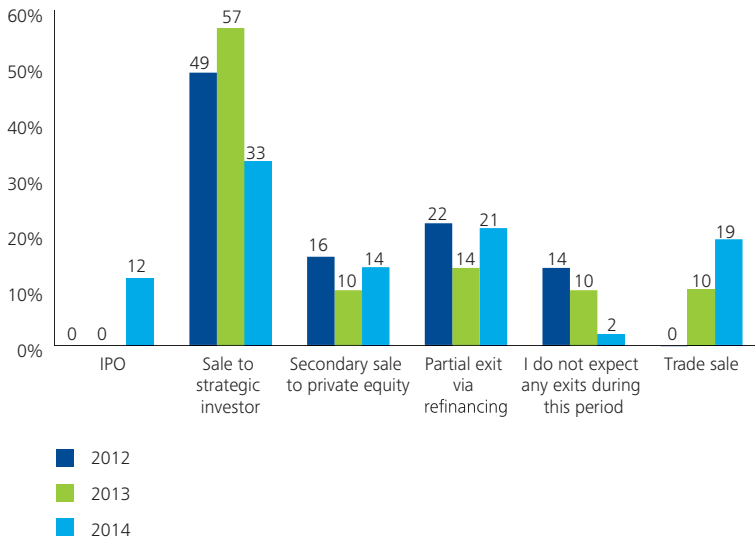
During the next 18 months, investors expect the exit environment in Eastern Africa to:



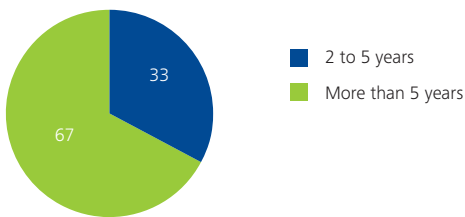
During the next twelve months, I expect the volume of exits in Eastern Africa to:



**Dominant Exit Routes Across Eastern Africa**



I expect the average lifecycle from initial investment to exit for investments made in the current year to be:



67% of the respondents expect the average lifecycle, from initial investment to exit, to be more than five years.

### Private Equity as a Catalyst?

In the larger scheme of things, Private Equity still plays a relatively small role on the continent. However, several deals completed in 2013 suggest that the asset class may be hitting above its weight by catalysing capital from a range of other, often foreign, investors:

In June 2013, Abraaj announced their plan to buy out Fan Milk International, a West African dairy goods producer. In October 2013, it was reported that international food group Danone would join Abraaj in the deal by acquiring 49% of the company, and would acquire a controlling majority in the coming years. Would Danone have done such an Africa acquisition on their own? More international strategic investors are looking at sub-Saharan Africa, and teaming up with an experienced Private Equity investor may ease the way.

Or consider Leapfrog's Ghana exit: In December 2013, LeapFrog Investments announced their exit from Express Life Insurance Company (Express Life) in Ghana to British insurer Prudential plc, who will acquire 100% of the company for an undisclosed sum. The transaction is Prudential's first insurance investment in sub-Saharan Africa.

Express Life was founded in 2009 and the backing of a PE investor has clearly contributed to a significant turnaround in the company: Leapfrog, alongside their USD5.5m, helped grow the company's customer base from 60,000 to 730,000, recruited a new management team, redesigned and developed new products, rebuilt the agency force from 40 to 250 agents, and introduced the distribution of products via cellphones. Through their exit, LeapFrog brought a global insurance player to the market.

In one of the largest PE-related deals completed on the continent last year, Emerging Capital Partners (ECP) helped their investee company IHS Mauritius Ltd raise USD1.035bn in additional equity and debt funding to finance tower upgrades and new tower purchases. The fundraising process was led and managed by ECP, who brought together some of the usual suspects with a few unexpected investors: The World Bank Group's International Finance Corporation (IFC), pan-African Ecobank, existing investors and ECP co-investors, and an Asian sovereign wealth fund, for whom this was the first Africa investment. (ECP also completed a similar, although much smaller, capital raise for its portfolio company Oragroup in May 2013.)

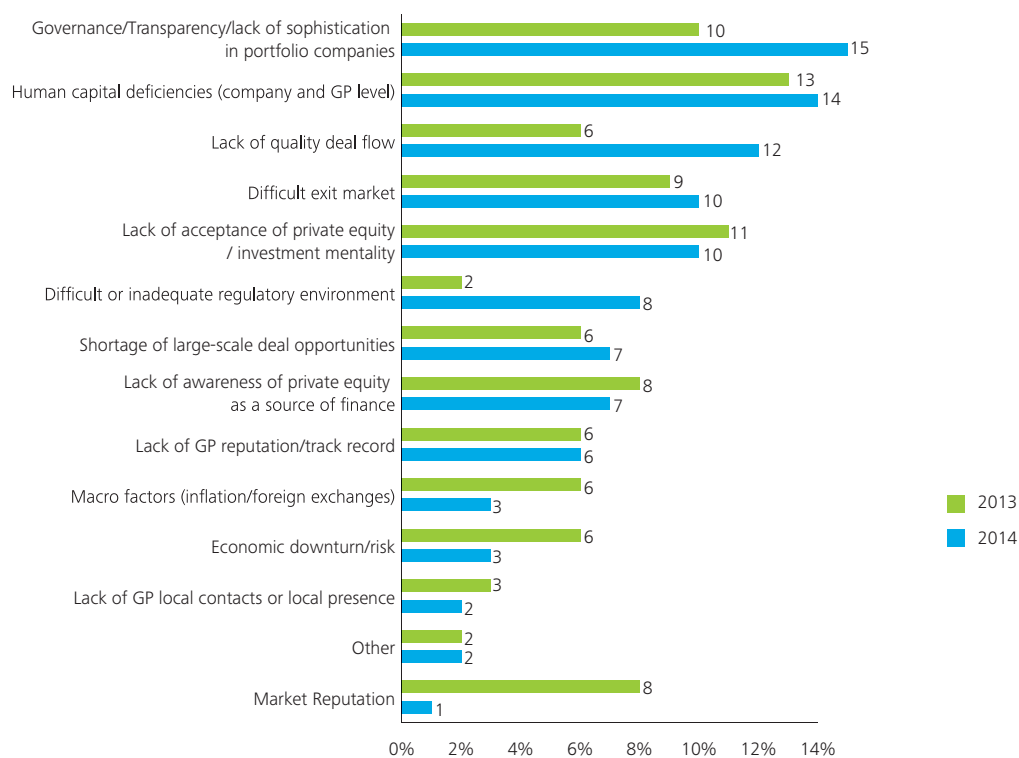
If the IHS deal goes well for ECP's SWF friend, the institution will most likely look for additional opportunities in Africa, whether as an LP or a direct investor.

This is all good news for formalising Africa's investment landscape and bringing more capital and players into the mix. One note of caution for PE firms: co-investments may reduce the amount of money that LPs put directly into PE funds, and therefore reduce the associated management fees. Some investors, notably DFIs, are reluctant to pay fees directly on co-investments. However, many other co-investors are happy to pay a fee. Some GPs have also brought co-investor money into a special one-time, one-deal fund managed by the GP at a fee. As more investors bring their money hesitantly, deal-by-deal, into the region, if those deals go well, those investors may also be more comfortable with acting as LPs in a blind pool in the future. Their entrance also provides more exit opportunities, at scale, for PE firms.

# 6 Challenges Ahead

Generally across the regions, Private Equity parties are more concerned about human capital deficiencies, a lack of sophistication amongst portfolio companies as well as lack of quality deal flow.

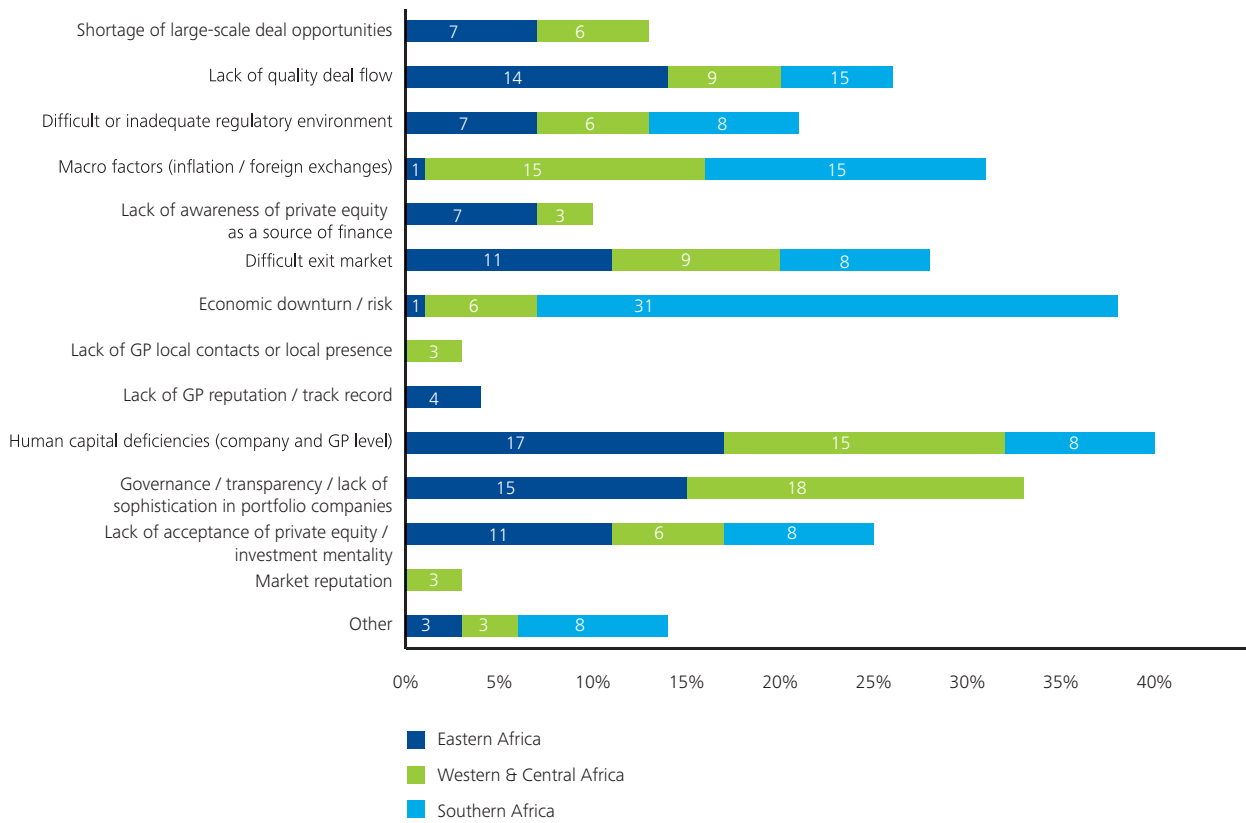
## Biggest Challenges and Barriers to Growth



Other issues brought out by the respondents that need to be addressed include:

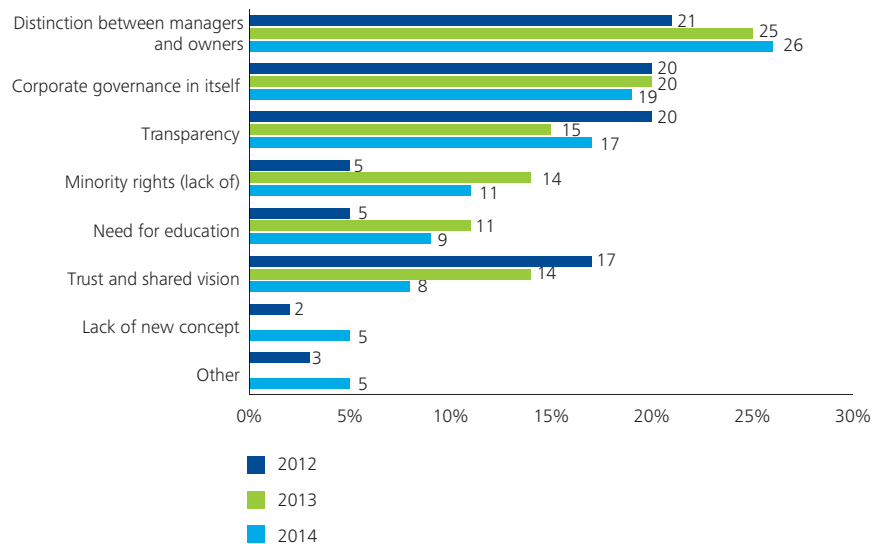
- Lack of a wider pool of fund investors (LPs).
- Inability of investors to adequately price risk and structure investments to take advantage of opportunities in a difficult environment.

### Challenges and Barriers per Region



### Biggest Challenges in Improving Corporate Governance

The three biggest issues affecting corporate governance are the distinction between managers and owners, corporate governance in itself and transparency at 26%, 19% and 17% respectively.



### **New PE Kid on the Block: Ethiopia?**

It is not just the business community in neighbouring Kenya that is eagerly watching whether Ethiopia will let foreign players into its economy: With a GDP of USD43bn, a population of almost 90m people and GDP growth rates of roughly 10% (although there is some dispute over the accuracy of government reported data), Ethiopia currently has many suitors in all sectors, whether consumer goods or infrastructure.

Private Equity funds of course share this attraction. We have seen growing PE interest in Ethiopia recently: Duet Africa PE invested an undisclosed amount in Dashen Brewery at the beginning of 2012, and in June 2012, Silk Invest Ltd, through their Silk African Food Fund, acquired a minority stake in Ethiopian biscuit producer NAS Foods Ltd. In May 2013, Nairobi-based Private Equity firm Catalyst Principal Partners announced the acquisition of a 50% stake in Ethiopian Yes Brands Food & Beverages for an undisclosed sum – all of these investments that are banking on a growing consumer class. The country's large population implies a potentially extensive consumer class, although its pervasive poverty means that it is still not clear how rapidly it will expand.

Fund managers are also raising funds for Ethiopia: In 2012, Schulze Global Investments (SGI) announced that they are raising USD100m for Private Equity investments through a dedicated country fund, with a first commitment of USD15m by British DFI CDC Group. Jacana are fundraising for a USD75m fund that they intend to invest partially in Ethiopian SMEs. Ethiopia is clearly not for the faint of heart, and will no doubt be difficult to tackle for anyone without good local connections. Following plenty of excitement amongst PE investors for the Ethiopian

opportunity, we only saw one investment in 2013 into an Ethiopia-based company. We know of other GPs who were working on deals in Ethiopia during the year, but these take a long time to close. Also, for a foreign direct investor, the high level of government control may be less of a concern as they have a longer-term perspective. PE firms, in contrast, typically need to exit in five to seven years. But the restrictions on market entry for foreign financial institutions means that Private Equity players can hope for an even stronger financing demand from local corporates.

Almost all private businesses are small: family-owned vendors and repair shops, and credit is hard to come by for the unconnected. Only licensed exporters consistently benefit from repeated devaluations of the currency. PE funds see the potential to invest in the best of the many SMEs – but in this challenging environment, can they help them grow, and be able to exit?

And not everybody is allowed in: Several sectors, including media and banking, are still closed to foreign investors. The telecoms sector remains in the hands of the monopoly parastatal. Therefore ICT, a rapid growth sector across the continent and one of its great success stories, has remained underdeveloped in Ethiopia, holding back related dynamics as e.g. the growth of tech start ups and mobile money.



# 7 Interviews & Insights from PE Firms

‘The costs of IPOs still outweigh the benefits. We may see some strategic buyers from within and outside the region, but refinancing and, possibly, sale to PE investors (provided mutually attractive valuation can be reached, which is difficult) will be the most likely exit route for the smaller deal sizes that we do.’

‘As the economy grows, businesses are expanding and will require equity financing. Additionally, PE is slowly being de-mystified and more entrepreneurs are now understanding the value add of a PE investor.’

‘GPs ARE feeling the pressure to deploy capital and deliver on the Africa promise they sold to their LPs.’

‘Existing investors are raising new money so I expect their deal sizes to increase. More commercial foreign investors with larger deal sizes are increasingly entering the market.’

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