

The business case for private equity in SA during challenging times

By [Tshepiso Kobile](#).

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Numerous headwinds stemming from both macroeconomic pressures as well as internal challenges have put the South African investment market on the backfoot.



Source: Supplied. Savca chief executive officer, Tshepiso Kobile.

Investor confidence has been eroded by issues such as the deteriorating energy crisis, the country's recent greylisting and a stagnating economy. On the other hand, the high inflationary environment caused by geopolitical tensions in Europe and America's banking failures, have dulled investors' appetite for risk, and by extension, the willingness of investors to commit capital to developing markets.

The turbulence of the economic downturn has resulted in a fiercely competitive environment, with asset managers vying for investor interest. All indicators point to the fact that it is indeed not 'business as usual'. In the current climate, investments need to 'do more' and 'be more' in order to derive real value. For several reasons, the solution to meeting these evolving demands may very well reside in the realm of alternative investments.

A recent panel discussion held during the two-day 2023 Private Equity Conference shed light on this perspective. The annual event is hosted by The South African Venture Capital and Private Equity Association (Savca) as a platform to build and solidify relationships with industry players such as investors, fund managers, regulators and advisors.

PE as a driver of transformation

The PE industry's ability to 'go beyond profits', was a recurring theme at the conference. Panelist Theriso Pete, associate principal - multi-management: private markets at PIC noted that for local limited partners (LPs), "transformation is at the top of the agenda".

This of course speaks to national objectives such as employment equity and more equitable industry representation – both of which Pete argues do not "compromise a fund's ability to produce positive commercial returns".

Despite being faced with a "black swan event", PIC recently backed a 100% black-owned fund, sticking closely by its commitment to contracting general partners (GPs) who demonstrate a high level of impact on the governance and social fronts.

The result of this steadfast commitment was a top-performing fund. The team went on to win an industry award for its proficiency in deal-making and was able to raise a subsequent fund. This, as Pete proudly explained, "is testament to the fact that PIC backed the right jockey."

Greater access to untapped market potential

Presenting a further point on the business case for PE was Janina Slawski, head of investments consulting at Alexander Forbes, who argued that collaborative efforts, such as a fund of funds, can grant higher levels of access for smaller pension funds to private markets. Unlisted markets represent an untapped opportunity for these funds to unlock the potential

of private markets to produce returns, as well as to have a meaningful impact.



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Opportunities for diversification

This opinion provided a segue into a discussion that unpacked the diversification benefits of PE. Maximising the potential of this asset class; especially for first-time investors, involves chartering a path through several challenges presented by the current market. The answer, for panelist Mardé van Wyk, principal consultant – private markets at 27Four, lies in diversification.

As she asserted, fund managers need to apply their minds and expertise to “design solutions that reflect the level of sophistication needed to help investors mitigate the current volatility of the market by leveraging the value of diversification”.

A more balanced outlook

Furthermore, in light of the pressing need for transformation within the local market, key players need to think of investments in terms of their ability to fulfill the yield requirements of pension funds as a matter of priority, but also in terms of their broader social impact.

This strategic approach also needs to align with the shared mandate of several pension funds to drive responsible investing. As a collective however, the panelists shared the view that a focus on real-world impact should not involve a compromise on commercial viability – which will always be the ultimate objective for PE.

“ Profit with purpose! Investing in sustainable, ethical companies leads to better returns. 82% of PE fund managers are stepping up efforts to manage ESG performance. Discover how PE drives environmental & social impact in companies here [#INVESTINGFORGROWTH](https://t.co/XQfhHV0WcE) pic.twitter.com/w3wKpcHk5k— SAVCA (@SAVCAssociation) July 4, 2023 ”

On this, Phathutshedzo Mabogo, deputy chief investment officer of the Eskom Pension and Provident Fund (EPPF) said: “Money allocated to private markets goes directly into the economy where fund managers, investors and other stakeholders can see what their money is doing on the ground. Investments therefore need to make practical and financial sense.”

And as Christian Roelofse, investment officer – private equity at FMO explained, this dual focus on commercial prospects and social impact is reflective of the more balanced investment approach taken by the PE sector.

“About 21 of our funds have exposure to South African markets - many of them being pan-African - within specific target sectors that promote job creation. But impact does not have to come at the expense of returns. There can be no impact without profits. Critical selection is key to achieving both,” he concluded.

Tangible results

To this point, the most recent study commissioned by Savca and published in partnership with Intellidex, illustrated the role of PE as an important driver of job creation.

According to the report, prior to 2021, as pressures from Covid-19 lockdowns took their toll on the economy, companies owned by private-equity funds were able to receive assistance with liquidity and restructuring related issues, while investee

companies were able to grow employment by 4.4%, even though the wider economy experienced a 4.2% drop in employment.



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The report is part of a broader campaign called #InvestingForGrowth, which aims to assess and showcase the impact of PE as an asset class on local public-policy priorities and set up a strong investment case for both PE and venture capital (VC).

Performance levels looking up

While the panellists agreed that the turbulence of recent years contributed materially to the muted performance of PE, several indicators suggest that more positive prospects lie ahead.

According to panel moderator, Gergana Ivanova, the associate director in strategy and transaction at EY, 2016 saw a declining trend of returns and the value of exits. However, 2022 saw a substantial rise in exits both in number and value – a hugely positive and encouraging development.

In the opinion of Hale Matsipa, founder and chief executive officer of Kleoss Capital, the onset of the pandemic dealt a deafening blow to the industry. However, one of the firm's most recent exits took place amidst this uncertainty in 2020. Post-pandemic will see the market succeed in catching up, with an increasing number of overseas investors seeing value in the local market.

Tough economic conditions notwithstanding, there is clear evidence of renewed interest in new markets, on the back of African private market growth in volume and value of deals. South Africa, in particular, is beginning to show positive signs in PE and infrastructure.

ABOUT THE AUTHOR

Tshepiso Kobile is the chief executive officer of Savca.

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