


PE IN AFRICA – A LOCAL INVESTOR’S PERSPECTIVE

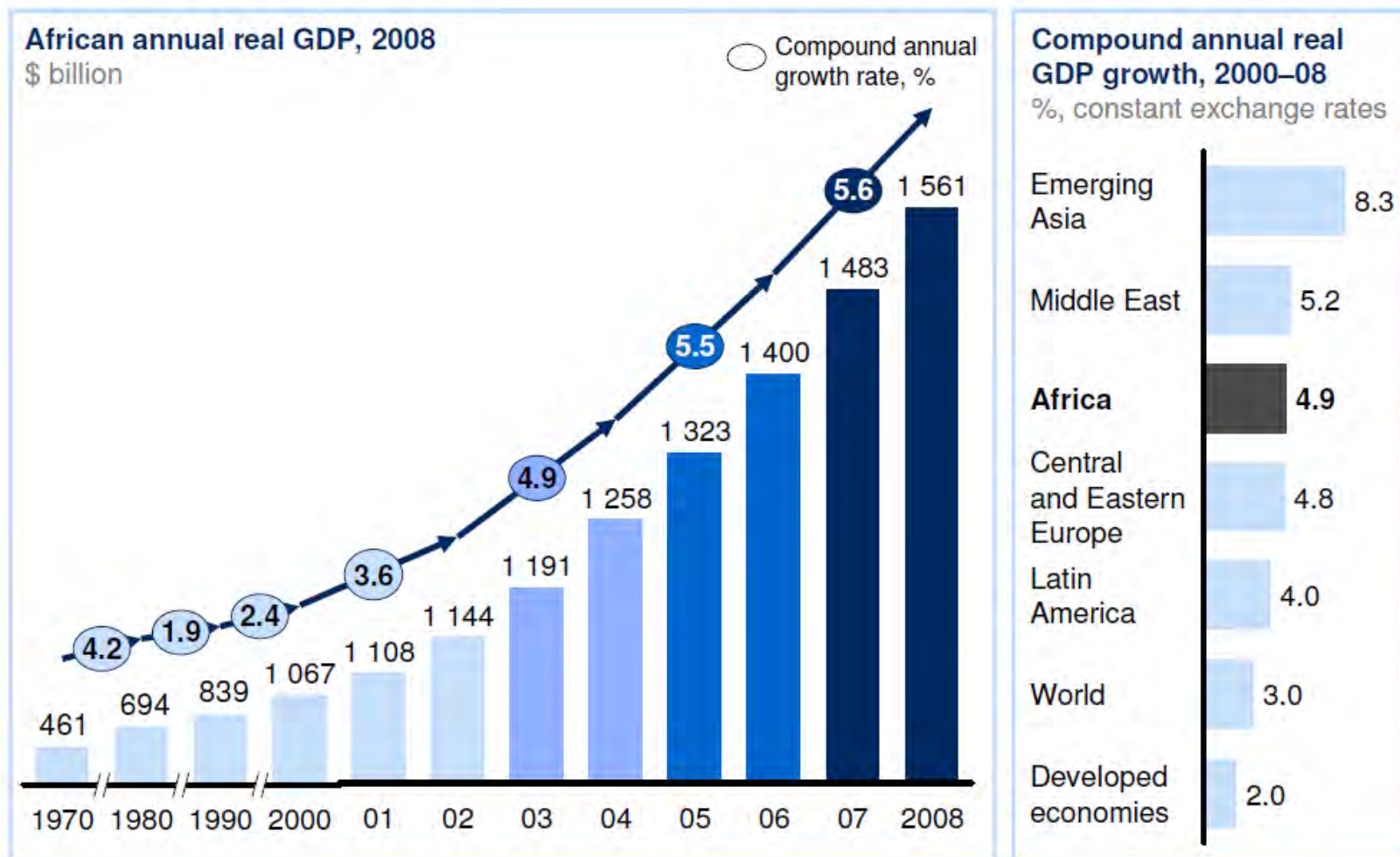
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Investment Advisory

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THE CONTEXT FOR AFRICA – SOME SURPRISING FACTS

- Consumption grew more in Africa than in India or Brazil over the last decade
- Africa has as many cities with 1 million people or more as Europe
- Africa today is more urbanized than India, and just below China
- African returns to FDI were the highest in the world by 2007
- Productivity growth was widespread and jumped to 2.7% p.a. across the continent

AFRICA'S ECONOMIC GROWTH ACCELERATED AFTER 2000, MAKING IT THE WORLD'S THIRD-FASTEST GROWING REGION

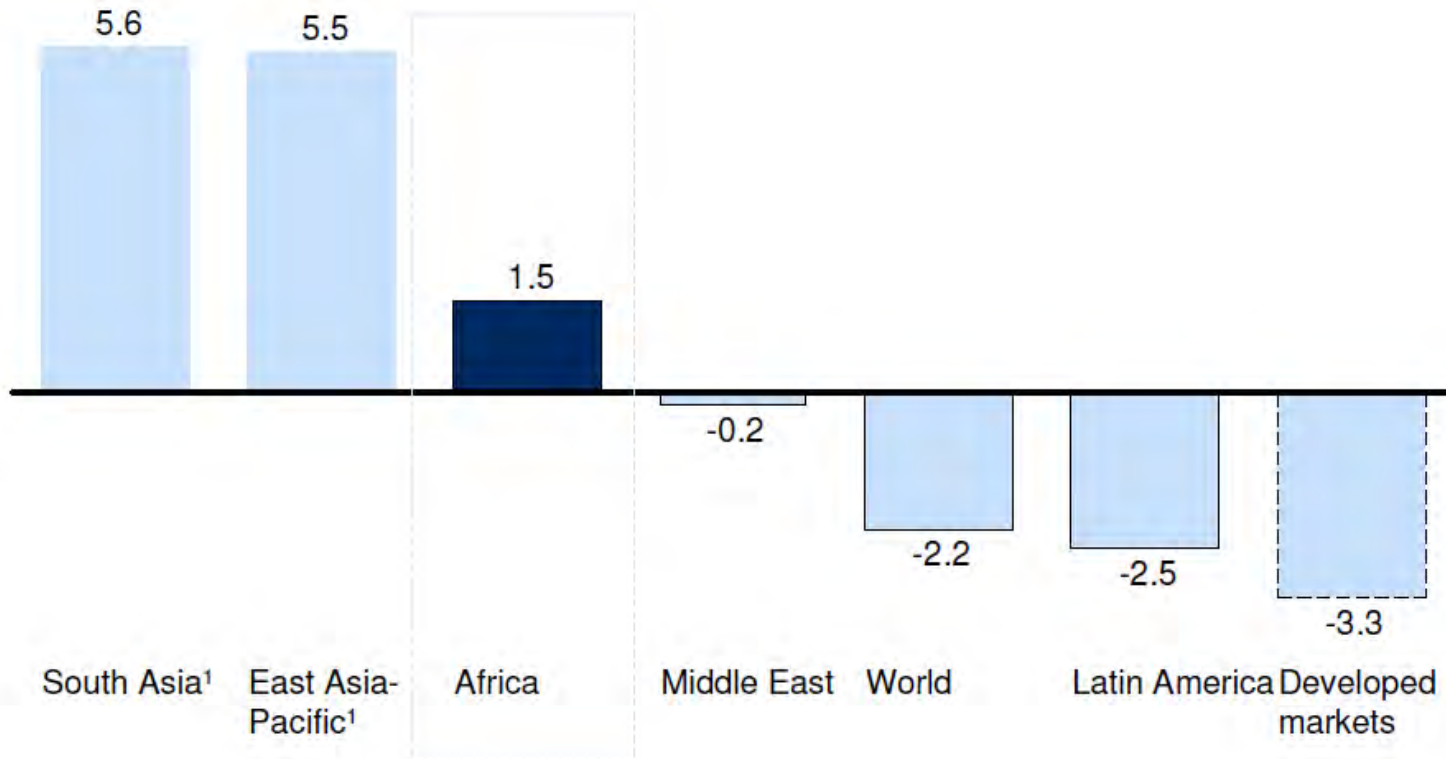


SOURCE: International Monetary Fund; World Bank World Development Indicators; McKinsey Global Institute

McKinsey & Company

DESPITE A STEEP FALL IN REAL GDP GROWTH, AFRICA WAS ONE OF ONLY THREE REGIONS TO GROW IN 2009

2009 real GDP growth
%, constant exchange rates



¹ Only developing and emerging countries

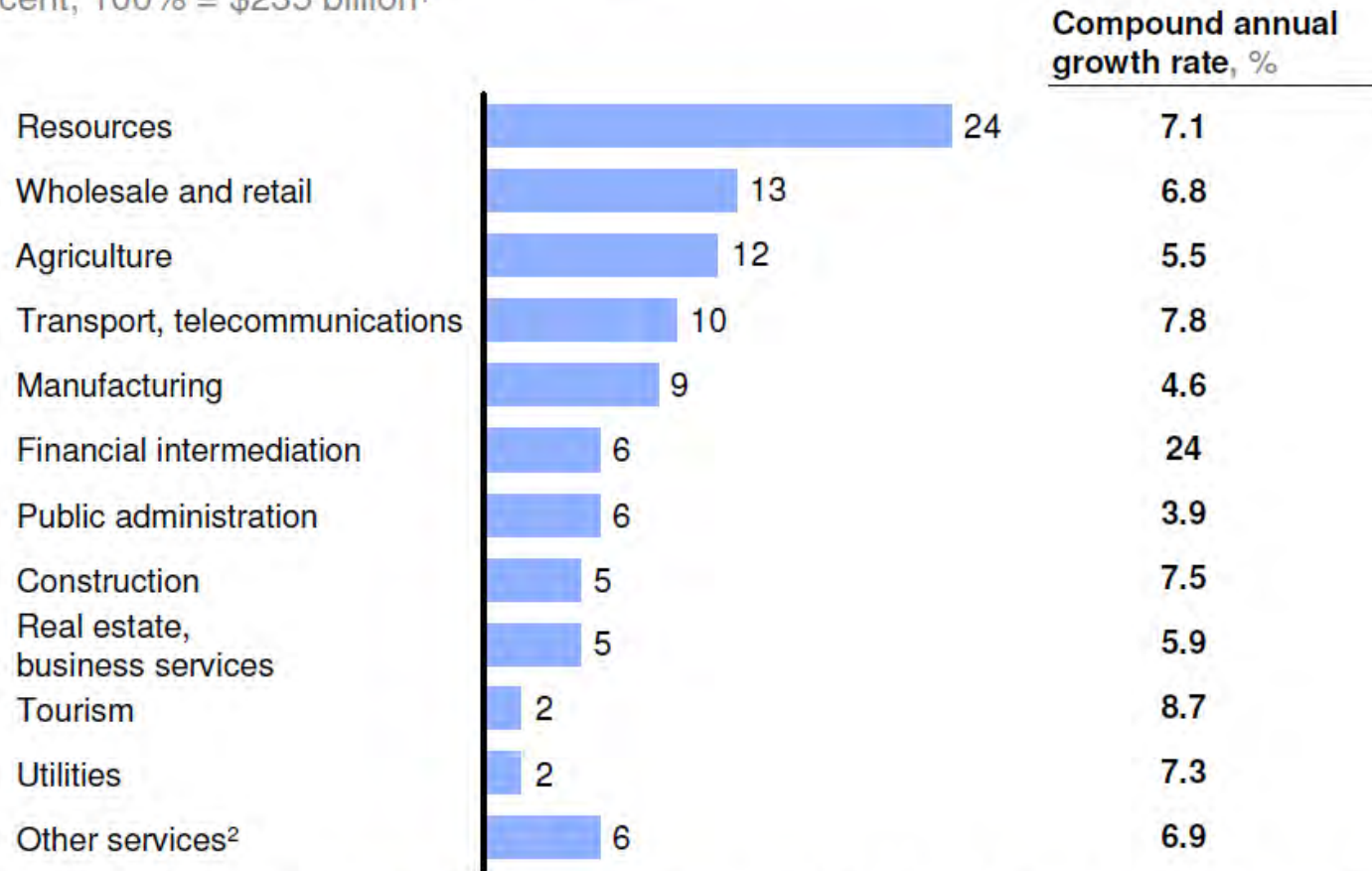
SOURCE: Global Insight; McKinsey Global Institute analysis

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AFRICA'S GROWTH WAS WIDESPREAD ACROSS SECTORS...

Sector share of change in real GDP, 2002–07

Percent, 100% = \$235 billion¹



¹ In 2005 dollars. Includes 15 countries that account for 80 percent of Africa's GDP: Algeria, Angola, Cameroon, Egypt, Ethiopia, Kenya, Libya, Morocco, Nigeria, Senegal, South Africa, Sudan, Tanzania, Tunisia, Zimbabwe.

² Education, Health, Social Services, Household Services.

SOURCE: Global Insight; Arab Monetary Fund; African Development Bank; McKinsey Global Institute McKinsey & Company

AFRICA'S GROWTH ACCELERATION HAS BEEN DRIVEN BY THE COMMODITY BOOM, GREATER STABILITY, ECONOMIC REFORMS, AND HEALTHY URBANISATION



¹ Conflicts with more than 1,000 deaths per annum
SOURCE: Team analysis

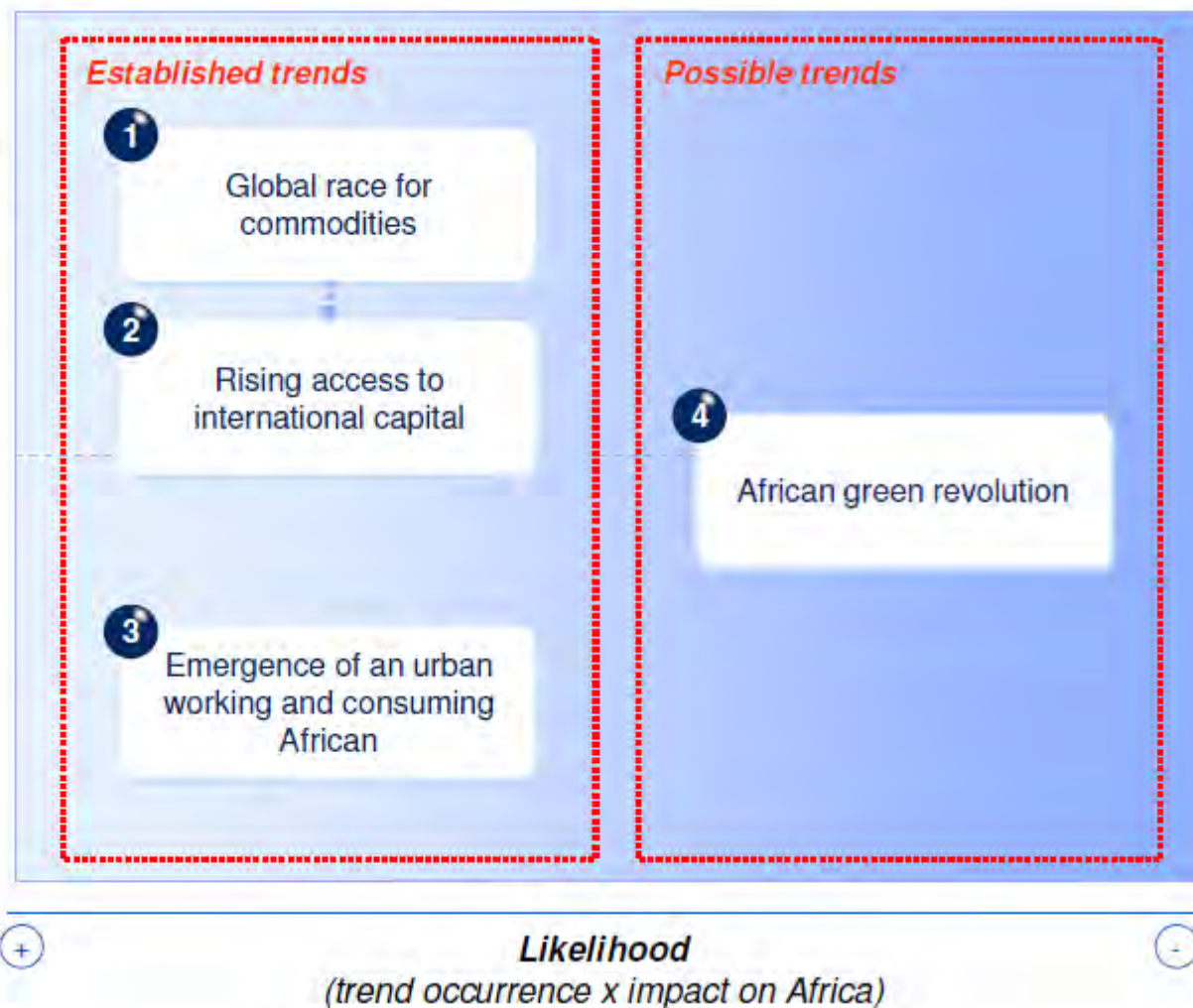
FOUR STRUCTURAL TRENDS POINT IN AFRICA'S FAVOUR



*Africa's role
in the world
economy*

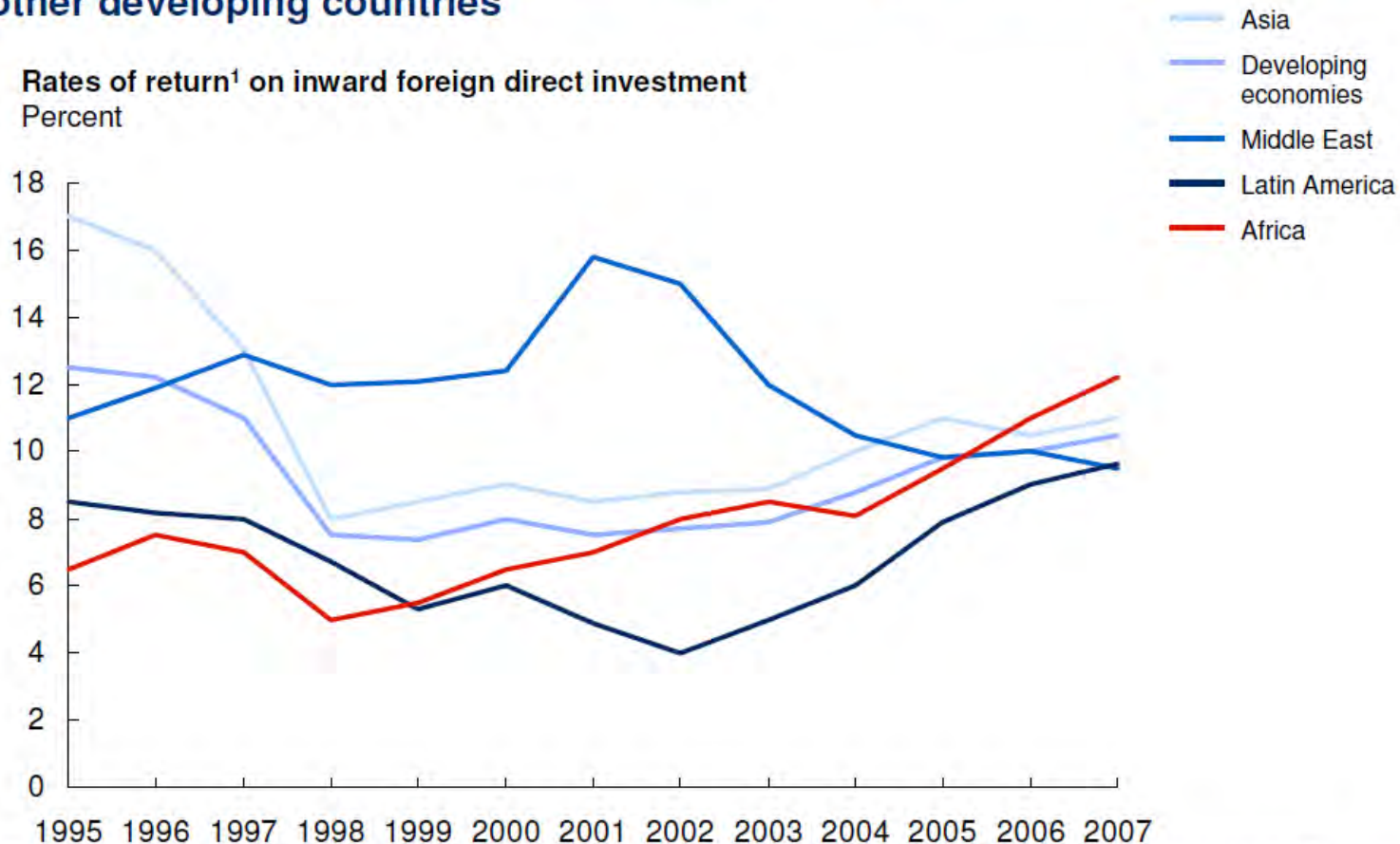


*Africa's
domestic
dynamics*



The rate of return on foreign direct investment in Africa is higher than in other developing countries

Rates of return¹ on inward foreign direct investment
Percent

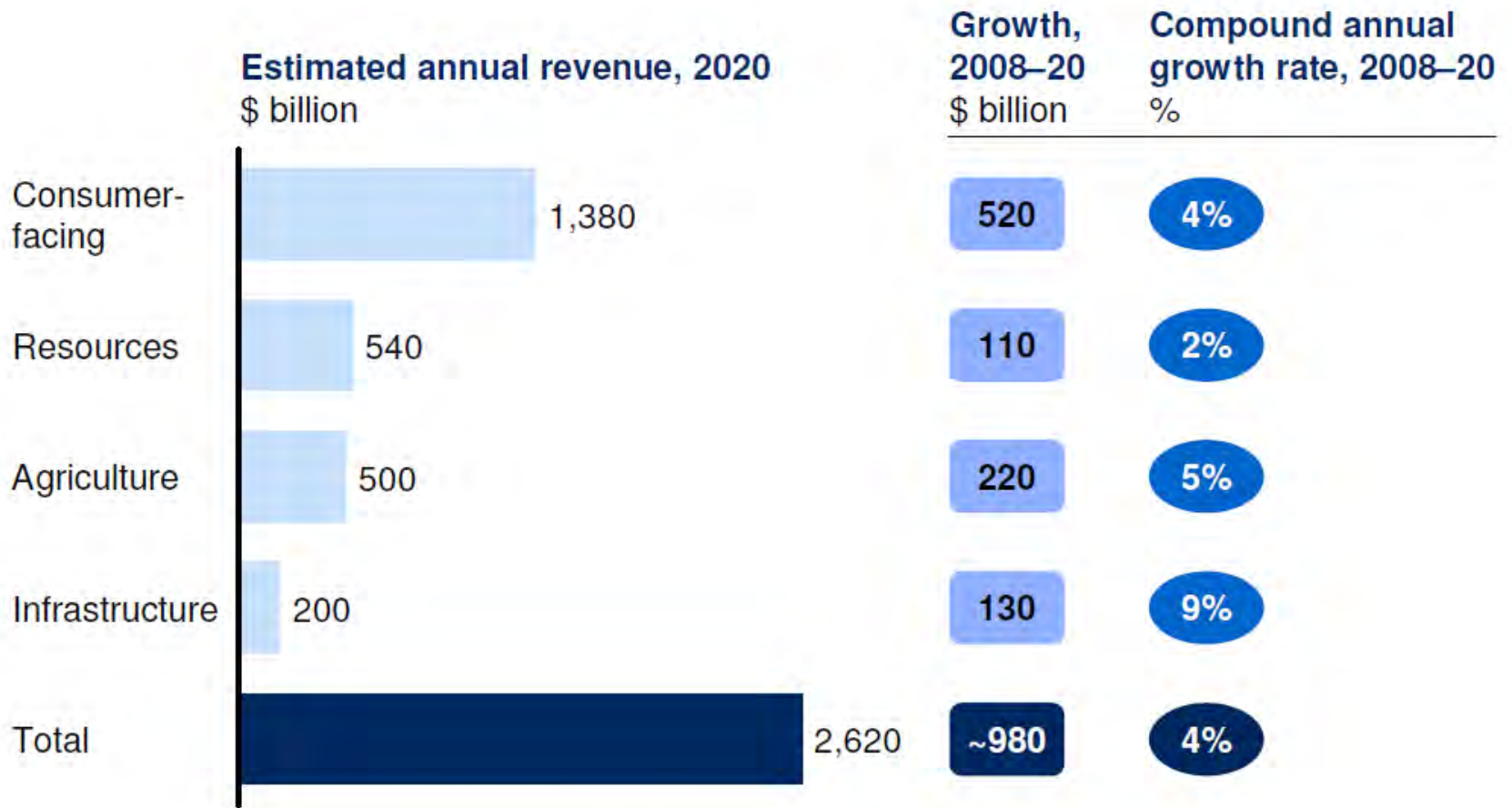


¹ The rate of return is calculated as direct investment income for the current year divided by the average of FDI stock of the previous year and the current year. The figures for 2007 rates of return are based on 39 countries in Africa, 33 in Latin America and the Caribbean, 11 in West Asia and 18 in Asia

SOURCE: United Nations Conference on Trade and Development; McKinsey Global Institute

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FOUR GROUPS OF INDUSTRIES COULD HAVE COMBINED REVENUE OF \$2.6 TRILLION BY 2020



1 Took 2030 value of \$880 billion and calculated straight line equivalent for 2020.

2 Represents investment. Assumes need remains as same share of GDP through 2020.

SOURCE: McKinsey Global Institute

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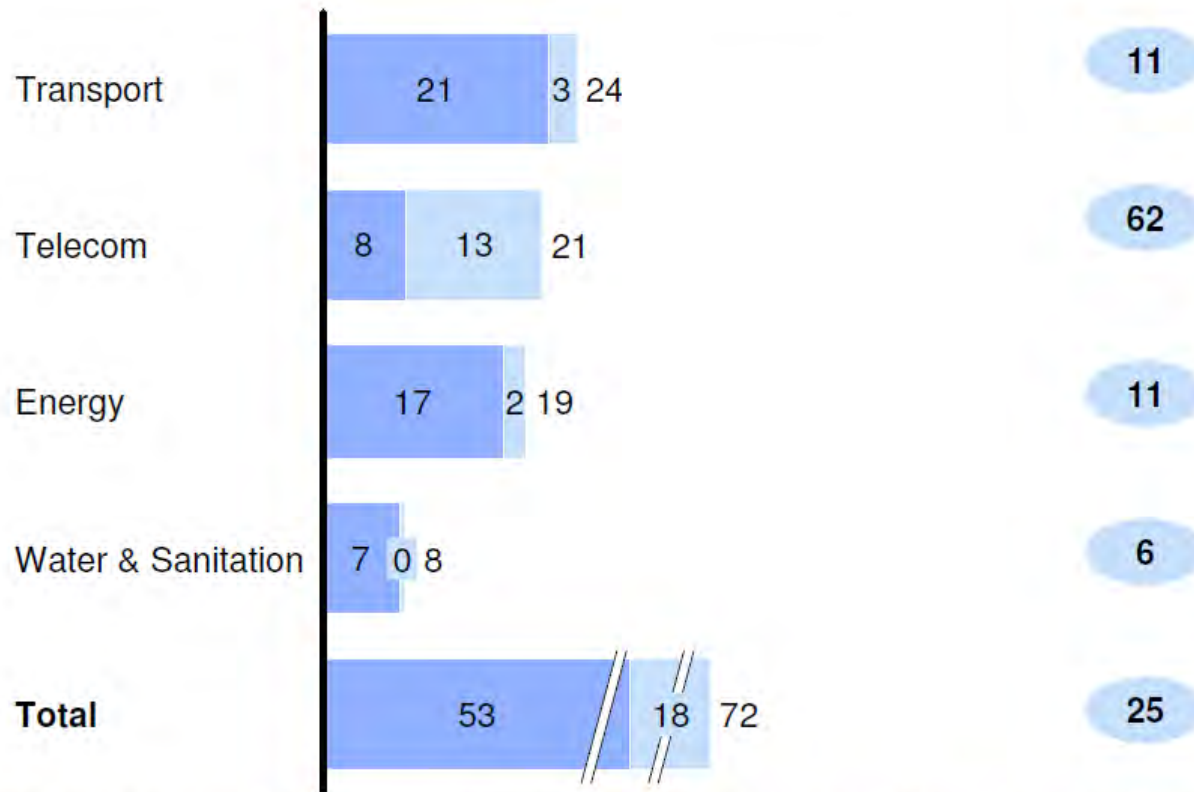
INFRASTRUCTURE

Africa invests \$72 billion annually in infrastructure today – but that figure could rise to \$200 billion by 2020

Private
Public and Donor

Annual average infrastructure investment, 2005–08
\$ billion

Private share
%



SOURCE: Private Participation in Infrastructure (PPI) Database, Africa Infrastructure Country Diagnostic; National budgets; McKinsey Global Institute
McKinsey & Company

WHAT DOES THE FUTURE HOLD?



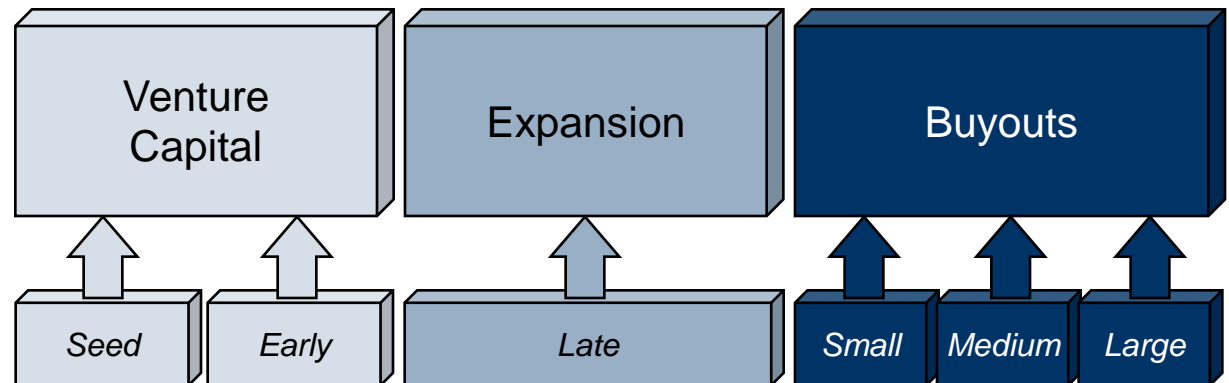
THE STORY IS GETTING BETTER!

- SSA – Lower correlation to global equities and private equity follows.
- Attractive valuations relative to other emerging markets, low sovereign debt levels.
- Higher GDP growth relative to the developed world.
- Natural resources – much more to explore.
- Investment and consumption from China (US\$ 10bn in 2000, to US\$100bn in 2010).
- Need for infrastructure – electricity, roads, air, broadband.
- Integrated trade.
- Corruption levels – need to get lower.
- Political risks – improving but still need to mitigate.
- Demographics – Africa's youth is the engine. It is growing and needs to be well educated.

PHILOSOPHY

- Private markets *cannot* be timed
- A successful private equity program rests on *continuous* rather than episodic exposure to the asset class
- Portfolio risk can be mitigated by diversification

- Size
- Stage
- Strategy
- Industry
- Geography



HOW TO TRANSLATE PHILOSOPHY

- Experience in managing a diversified portfolio - take a holistic view.
- Africa is one part.
- Equities--public or private.
- Fund managers, co-invests, directs, partnerships, get the right footprint.
- Avoiding market timing.
- Increasingly inefficient markets.
- Balance experienced managers vs. new managers/opportunistic situations.
- Generalist vs. sector specialists.
- Track record matters – know your criteria.
- Governance and terms of the investment matters – understand it.
- Focus on incentives.
- Who are these people anyway, and who knows them?
- What can go right? What can go wrong?
- If you don't know, get experienced help – specialists and reliance on outside managers, advisors.

OPPORTUNITIES AND CHALLENGES - BUSINESS AS USUAL?

- What has the world just experienced?
- Alternative investments are an intensely cyclical business:
 - Has been true from industry's earliest days.
 - 2006-10 mirrored what happened before, but in more dramatic form.
 - No reason to expect it to be the last cycle.

NOT REALLY.....

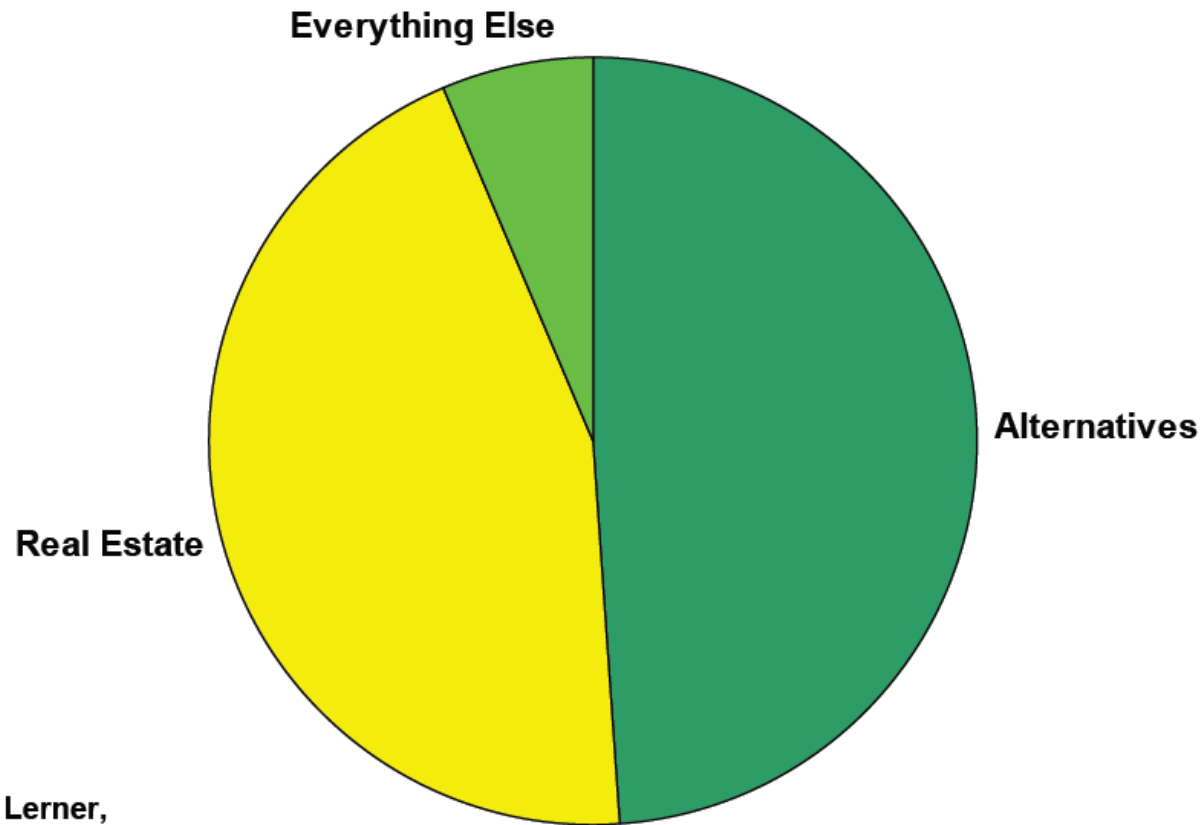
- Acceleration in change of investment opportunities, with emphasis on emerging markets.
- Liquidity-constrained and suspicious limited partners. If you are local – you probably have an advantage.
- Changing investor mix.
- Emboldened regulators and politicians – attractiveness of markets shifting, changing attitudes.



AN UNCONVENTIONAL MIX

	<i>Yale</i>	<i>Peers</i>	<i>All Univs.</i>
Bonds	4%	16%	22%
Public equities:			
Domestic	12%	25%	46%
Foreign	15%	17%	7%
Private equity	16%	9%	2%
Real estate	29%	11%	4%
"Absolute return"	23%	20%	9%

WHERE DOES THE IVY LEAGUE'S OUT PERFORMANCE COME FROM?



Source: Lerner, Schoar and Wang [2008]. Data from 2002-05.

SPECTACULAR SUCCESS IN ALTERNATIVES

- Yale - Investor since 1973.
- Repeated investments in partnerships formed by a select group of organizations.
- Emphasis on value-added strategies.
- Focus on incentives.
- Success in venture capital, buyouts, and oil & gas:
25% over 21 years--well above benchmarks.

CONTRASTING STORY IN FY 2009

- Contrasting story in FY 2009
- Many of investors that pioneered private equity have been challenged:
 - Yale: -25% loss in FY 2009.
 - Harvard: -27%.
 - Stanford: -27%, and 10% pay cuts!
 - Other endowments down 30% or more.
- Moreover, liquidity issues from “over-commitment” to funds:
 - Responses include secondary sales, slow-down in new commitments, and strategy shifts.

Source: Press accounts.

WHAT EXPLAINS CHANGES?

- Hypotheses:
 - Fundamental changes in PE markets themselves.
 - Hyper-competition in alternative investments:
 - Ability to get gains rapidly depleted.
 - Excessive risk taking in endowments:
 - Perhaps bred by turnover, organizational problems?
 - There are no problems...endowments are far ahead of where they would have been with a low risk strategy.

WHAT DO INVESTORS SEEM TO BE LEARNING?

- We shouldn't be investing as much in many alternatives.
- Especially high-risk categories!
- We should be driving tougher bargains with general partners.
- We should be doing more direct deals.
- Some of these are the "right" lessons and some of these are the "wrong" ones.
- Ability to absorb history, and apply it to your own programs
 - Staff turnover
 - Politicization of governance, investment committees
 - Entry of new LP's – Experience really matters!

HOW DO WE APPLY THIS 'LEARNING' TO THE AFRICA STORY?

- Liquidity matters – don't be dismissive of the 2009 crisis, balance allocations and strategy to alternatives.
- Need to think about risk carefully. Mean variance analysis does not always show what is really happening. Models are important but thinking critically about risk and return on alternatives is too.
- Fiscal policy must reflect investment realities, growth and sustainability, tempered approach.
- Investment committee – needs to be highly effective.
- Don't compromise on quality – me too's generally don't work - evaluate opportunities and seize them.
- Effects of firm size.
- Huge performance differences linked to decision making.
- Going it alone is not a 'cure-all'.

WHERE IS INDUSTRY GOING?

- Fund sizes adjusting to global liquidity.
- Deals looking different.
- Operational expertise will be a key differentiator.
- More co-investments.
- Focus on exits.
- More investors committing to PE over the long-term – need for returns.
- Investor base will change.
- Separate accounts more attractive.
- Activity will rebound.
- Expanding role played by global and established PE firms outside of the traditional financial centres of the US and Western Europe. This would include Sub-Saharan Africa!

CONCLUSIONS

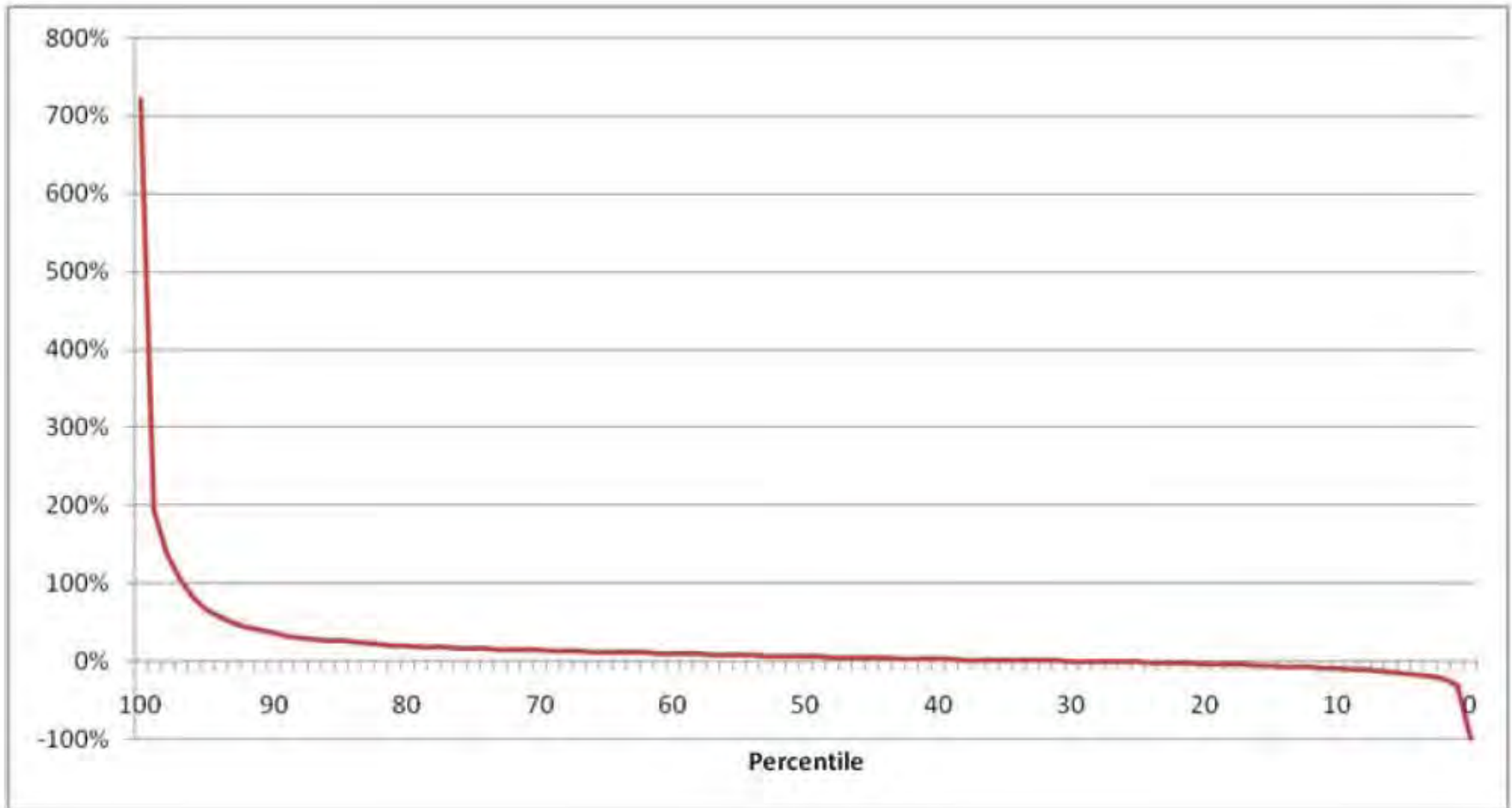
- Experience in investing in Africa – the story is getting better, tempered approach, the right partners, capture the opportunities.
- Traditional investments have become more risky.
- Private equity complements an already existing asset mix.
- Distinct lessons to be learned from successful investors, history and recent debate.
- More focus and opportunity in emerging markets, including SSA.
- Where are the next generation of quoted stocks going to come from unless there is a vibrant private equity market????

APPENDICES



“We structured the deal so it won’t make any sense to you.”

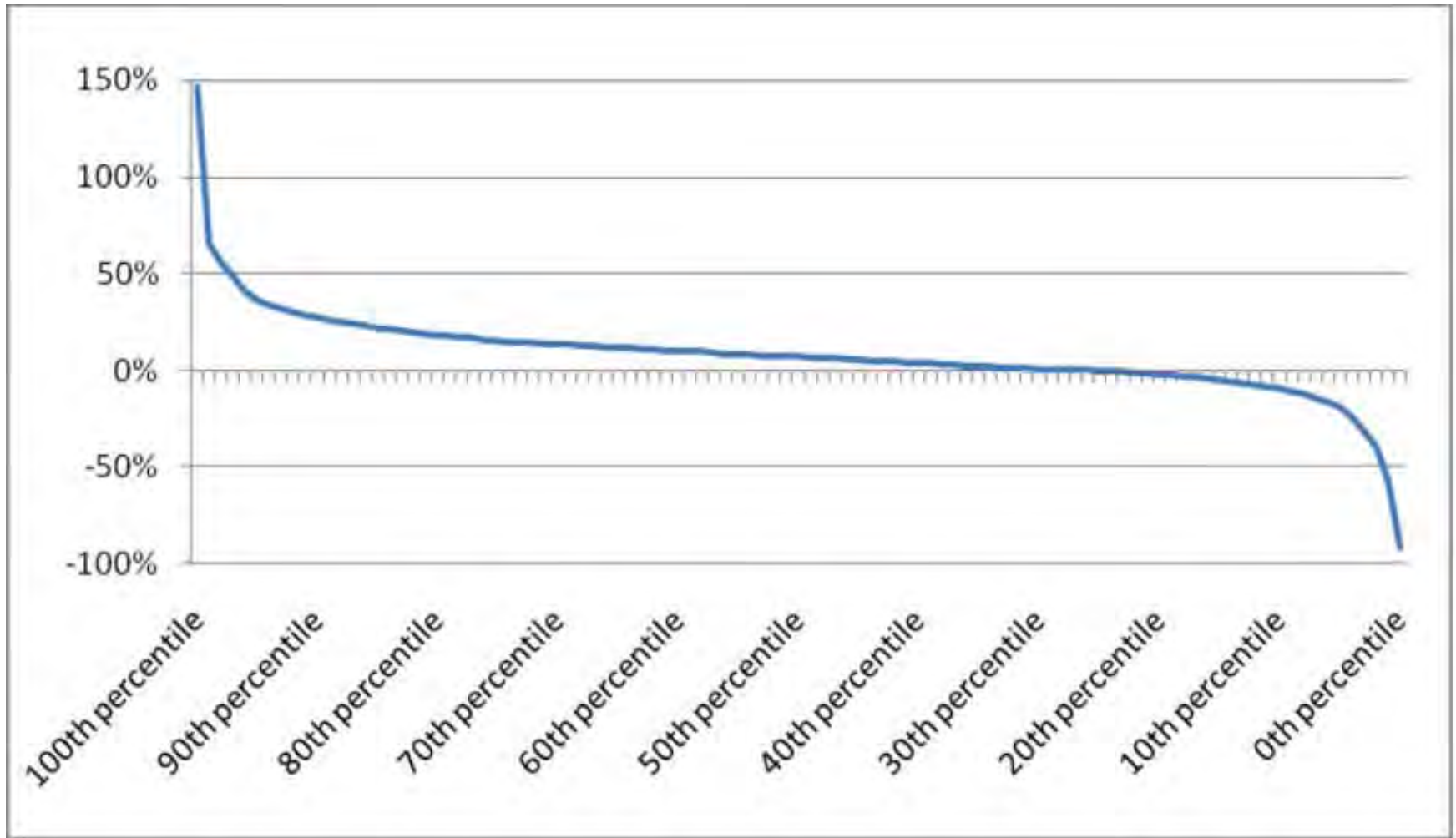
RETURNS OF U.S. VENTURE FUNDS



Returns from inception to 12/31/09.

Source: Authors' analysis of Thomson/Reuters data.

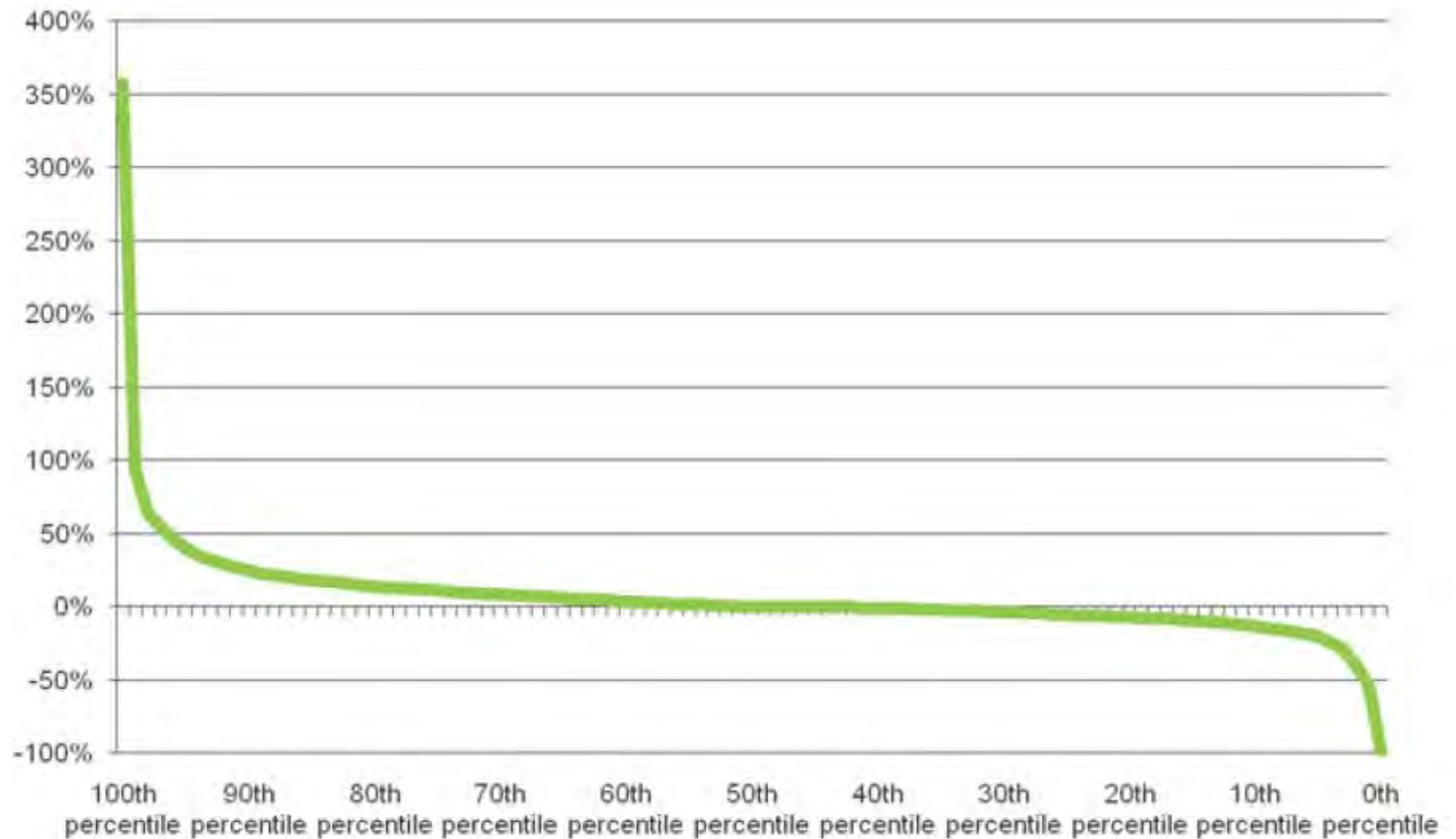
RETURNS OF U.S. BUYOUT FUNDS



Returns from inception to 12/31/09.

Source: Authors' analysis of Thomson/Reuters data.

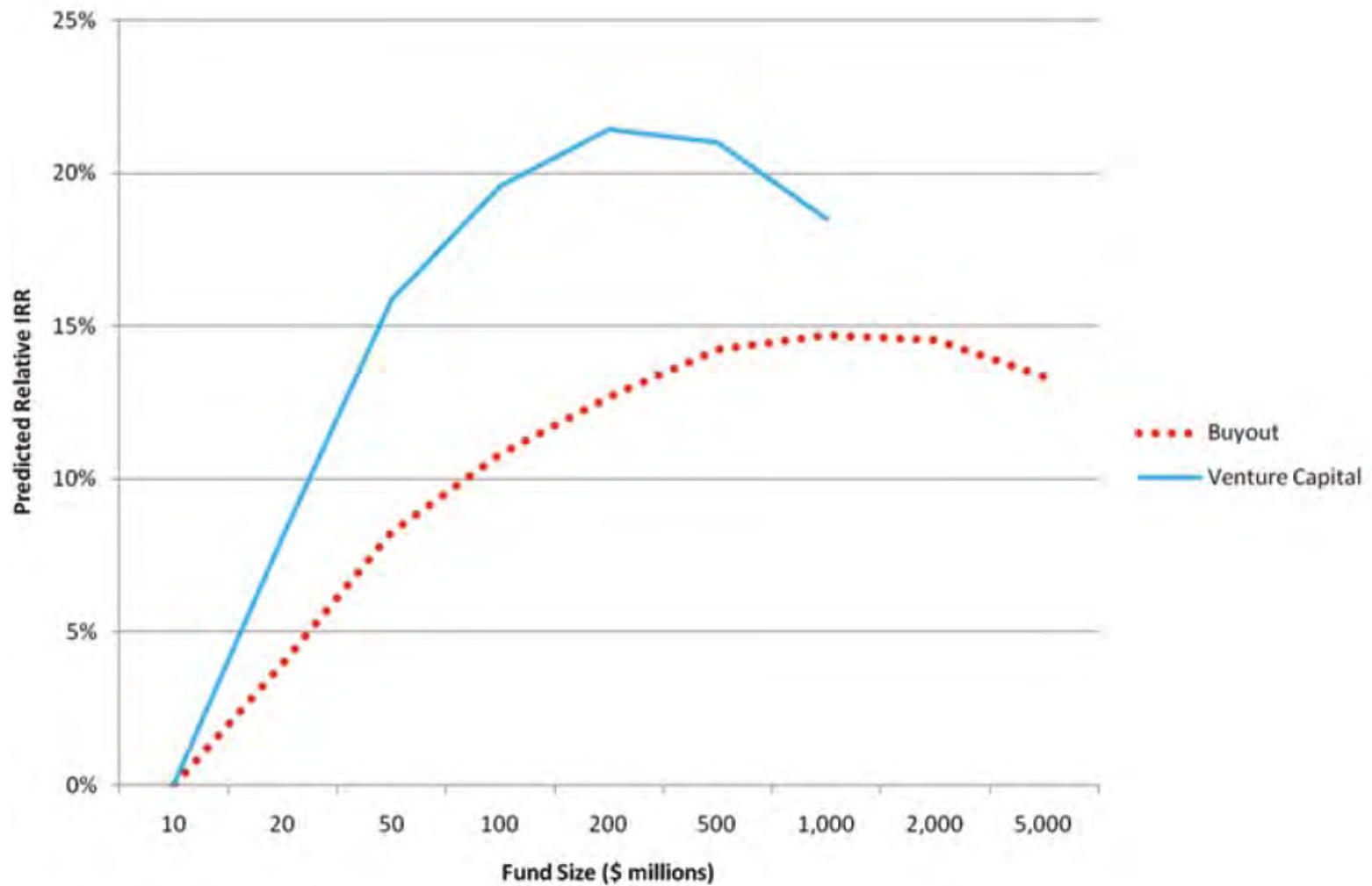
EUROPEAN PRIVATE EQUITY RETURNS



Returns of 1227 funds from inception to 12/31/09.

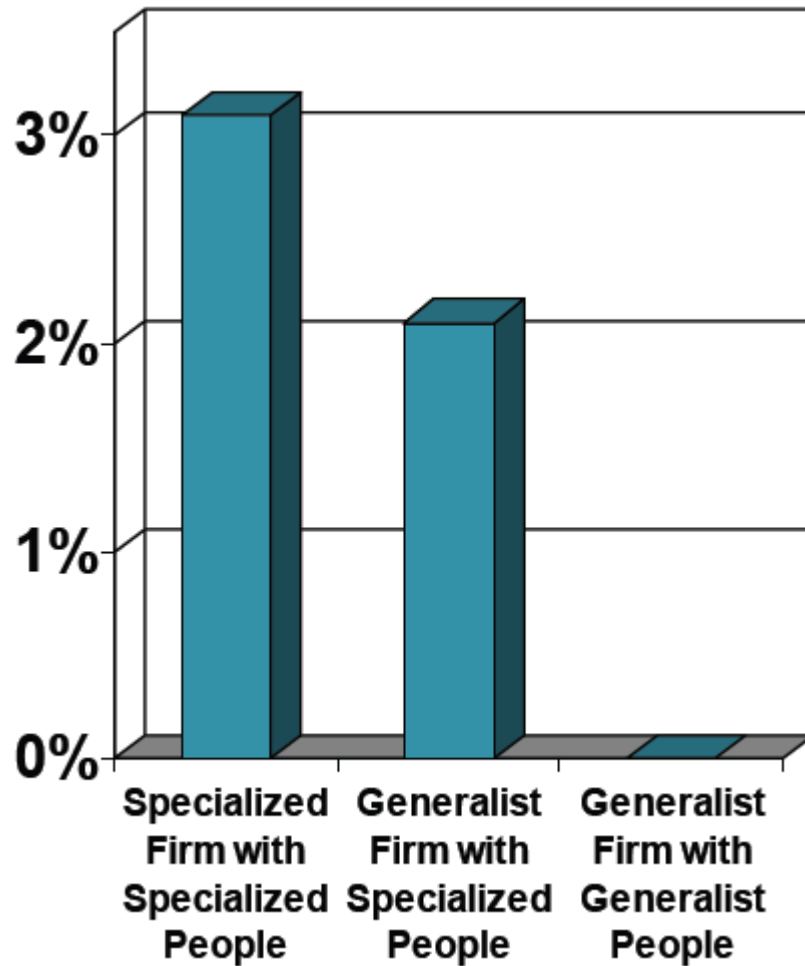
Source: Venture Economics.

LOOKING AT VENTURE AND BUYOUT FUNDS SEPARATELY



Source: Lerner, Leamon and Hardyman [2011]

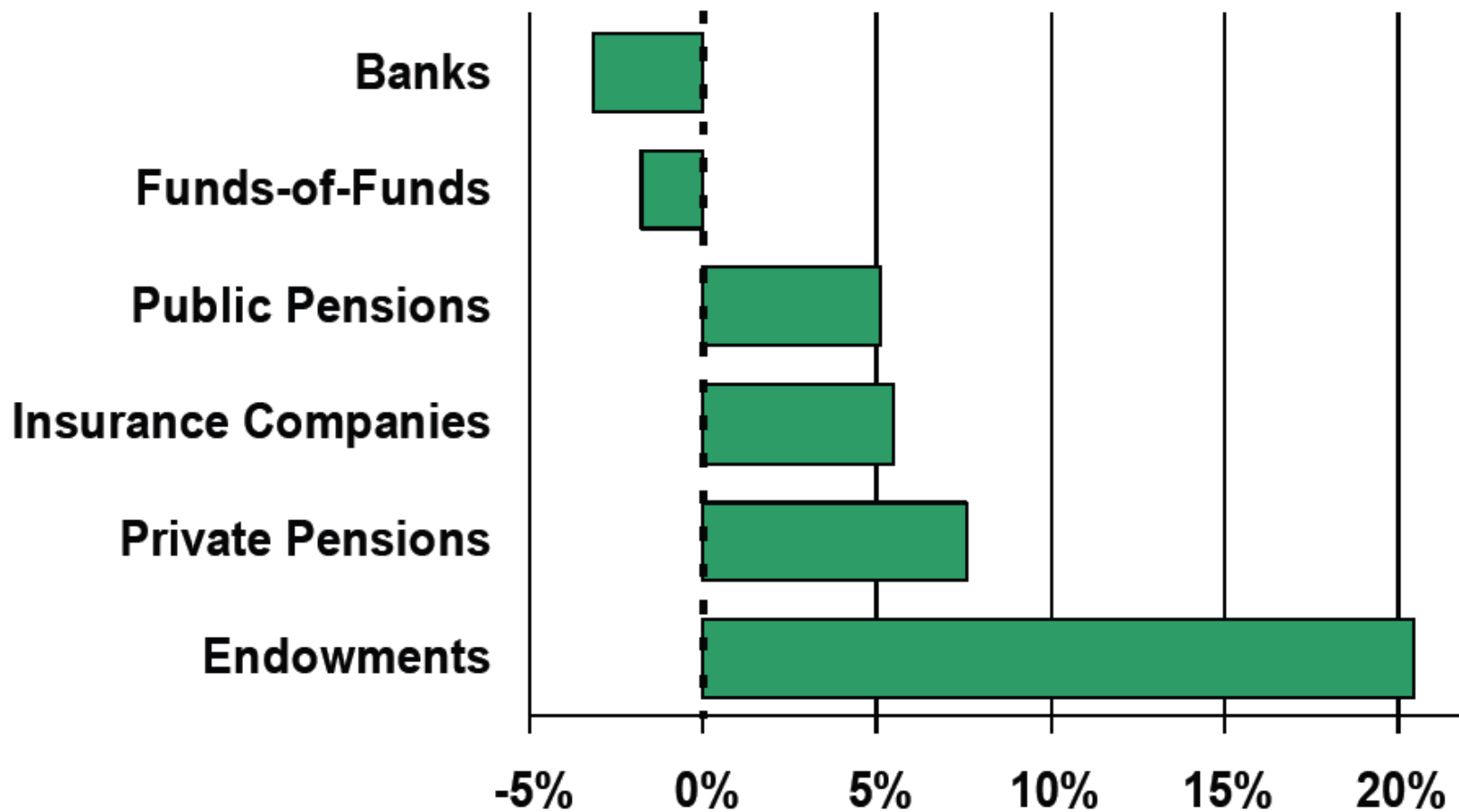
DIFFERENCE IN DEAL SUCCESS RATE



- Specialist firms are more likely to have successful deals.
 - i.e., 30% vs. 32.1% vs. 33.1%.
- Partners' focus especially matters.

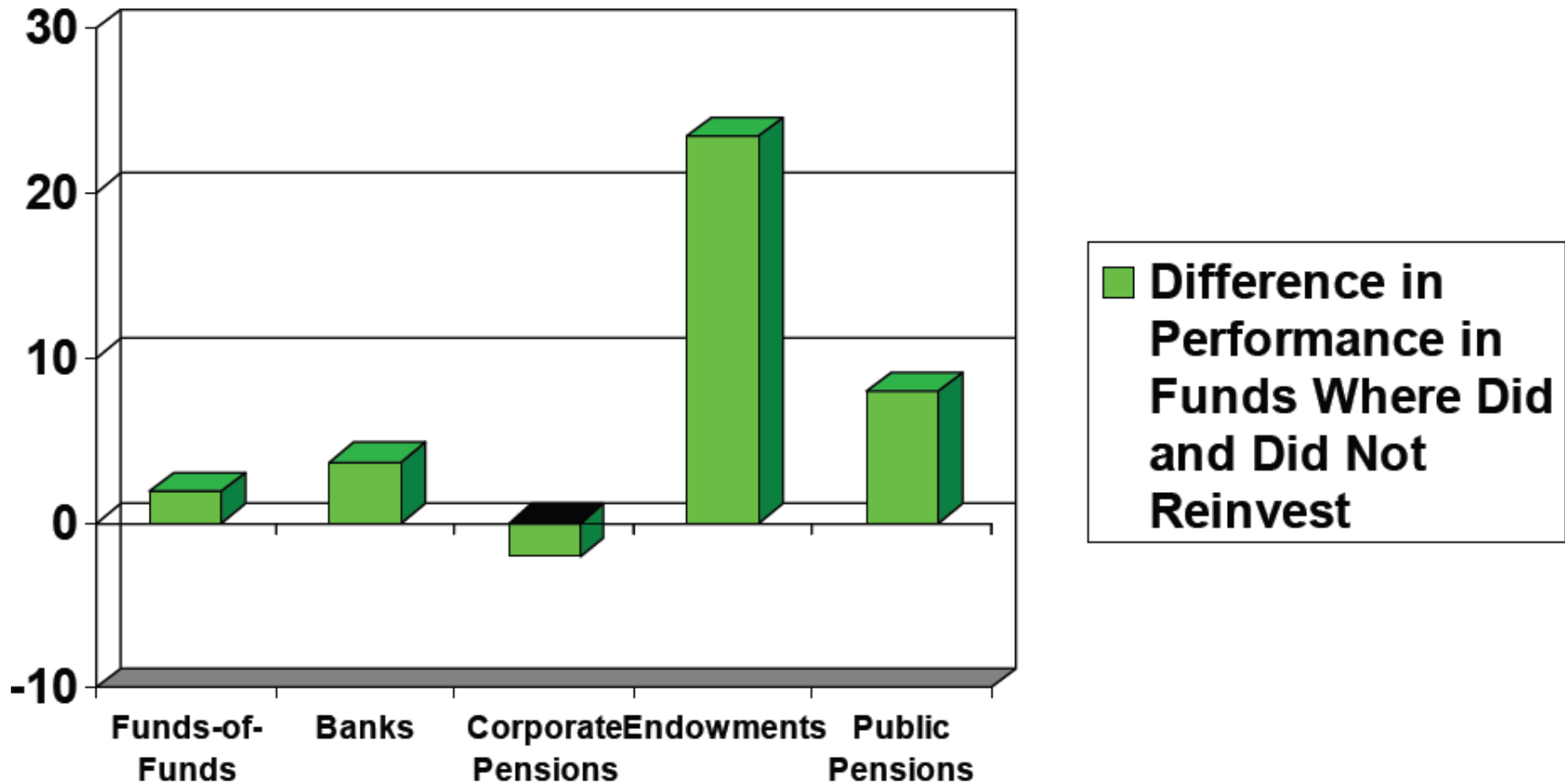
Source: Gompers, Kovner, and Lerner [2010]

PERFORMANCE BY INVESTOR TYPE, PRIVATE EQUITY FUNDS BETWEEN 1992-2001



Source: Lerner, Schoar and Wongsunwai [2007]

REINVESTMENT AND FUTURE RETURNS



Source: Lerner, Schoar and Wongsunwai [2007]

CHANGE IN P/E RATIO IN COUNTRY AND INDUSTRY IN YEAR AFTER INVESTMENT

	P/E change after domestic investment	P/E change after foreign investment
Asian sovereign funds	-4.3	+0.7
Middle East sovereign funds	-5.3	-0.9

Source: Bernstein, et al. [2010].

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