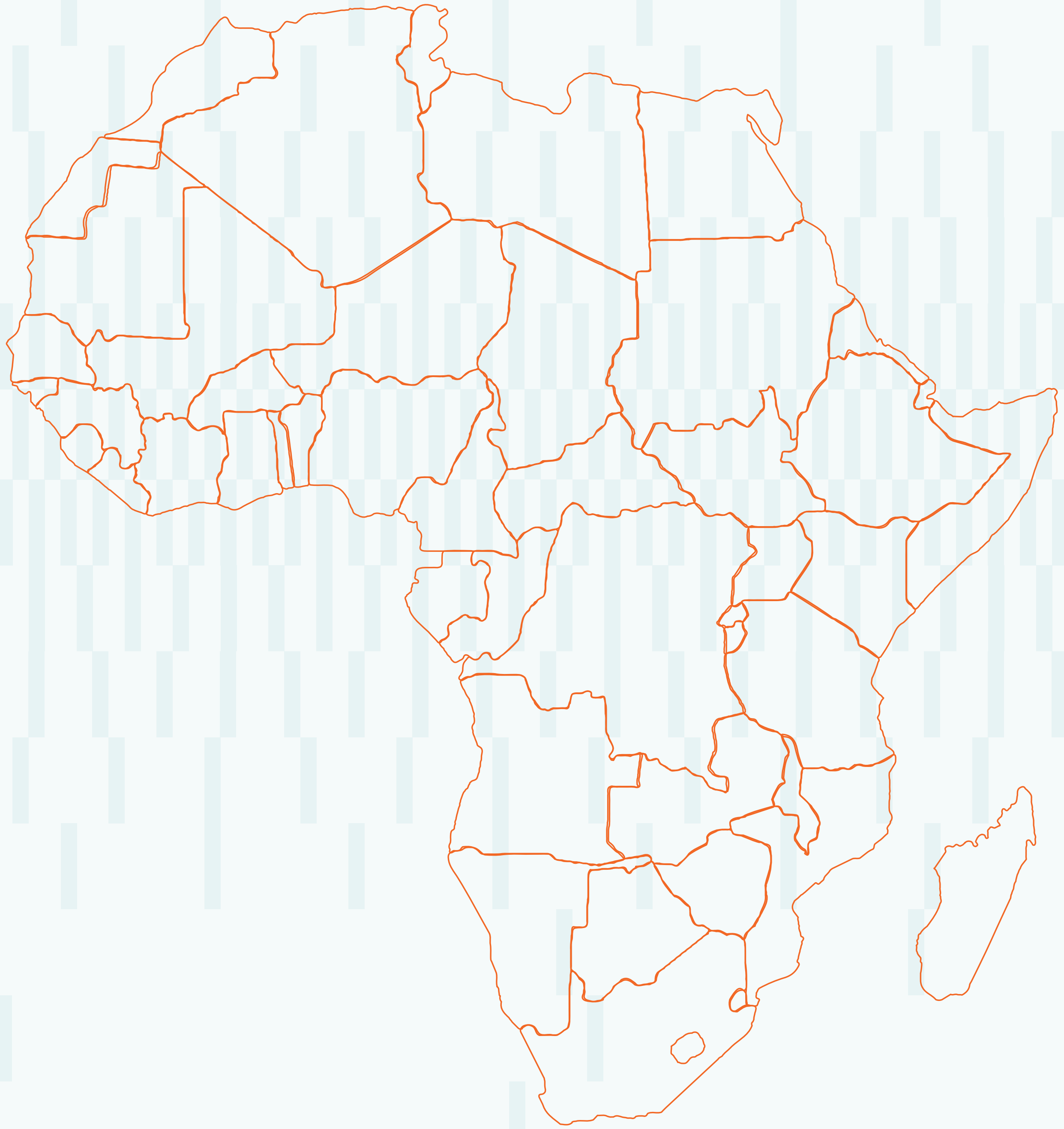
Bright Africa 2021
Private Equity In Africa



Africa continues to punch above its weight

This report aims to highlight the current state of the private equity market in Africa, including South Africa, and trends in prices paid for private equity assets over time.

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Foreword

Since its inception in 2013, Bright Africa has taken various forms depending, in part, on the availability of meaningful data in any given year. Overall, the intention has been to set the scene for investment into Africa by looking at the drivers and enablers of investments and the challenges and changes apparent in the current investment landscape. It is an ongoing research endeavour presented by RisCura together with external resources and data showcasing our unique, on-the-ground perspective.

We launch Bright Africa this year with our perspectives on and analysis of private equity (PE) markets in Africa, looking at fundraising, deal activity and pricing over the last 10 years. The process of compiling this report again highlighted the marked structural differences between regions in Africa. We hope you find it valuable and insightful.

The rebound of most economies following the global Covid-19 pandemic will likely provide an additional boost and shift investor sentiment back towards emerging and frontier markets as investors' risk tolerance increases. The economic recovery in Africa is driven by world-wide economic trends such as elevated commodity prices, a relaxation of lockdowns and travel restrictions, and increased global trade. The continent has also experienced good agricultural harvests in many regions. Economic recovery in Africa was initially slow because of low vaccination rates and the deterioration of the fragile fiscal position of many African governments. This is expected to rebound more strongly in 2022.

Even during this difficult time, some positive structural and regulatory changes on the continent are nurturing the green shoots of economic recovery. The most important of these have been the development of the African Continental Free Trade Area (AfCFTA), which could result in up to USD450 bn more income and significant wage increases. Other long-awaited positive developments include the unification of exchange rates in Sudan, fuel subsidy reform in Nigeria, and opening investment into the telecommunications sector to the private sector in Ethiopia.

Africa has experienced a number of high-profile coups recently. However, it is important to keep in mind that the overall number of these events continues to decrease, which could lead to increased political stability and a gradual maturation of democratic institutions. With the pandemic inducing economic hardship, Africa may continue to see heightened political risk in the short-term. The risk of military coups is still significant – particularly in West Africa. This, coupled with lack of accountability and responsibility within African governing structures, will continue to undermine any efforts towards economic recovery.

With high economic growth and significant tailwinds for investment, the PE industry in Africa has shown strong growth over the last decade from a very low base. This has resulted in temporary mismatches in supply and demand of capital. During the current year, we have observed the normalisation of pricing on the continent, partially because of the slow pace of commitments during the pandemic period. With the size of the industry continuing to grow, the industry should be less subject to mismatches in supply and demand of capital due to the inherent lumpiness of fundraising for the PE industry. This speaks favourably to the returns going forward, with investors entering the PE market at equilibrated prices, allowing them to earn appropriate market-related returns over the investment period.

Broad-based passive investments have not always proven to be the most efficient investment strategy in a less efficient market such as Africa. Risk-related returns are achieved by understanding the nuances of the investment environment and actively investing in companies that address the needs of the population. A positive economic and regulatory environment and excellent management teams enable this to happen. Such opportunities sometimes exist in exactly the areas that have structural inefficiencies, which the private sector can address, occasionally allowing for more efficient uptake of new technology. In the current period, this trend of targeted investment can be observed with tech-enabled businesses attracting large amounts of funds.

As a result of the need for more active investment strategies in African markets, the PE industry continues to grow, with deal activity still increasing and asset prices remaining robust. The growth of Africa's pensions and institutional asset management, and the resulting increase in local capital available for investment, also provide a significant opportunity for increased interest in PE.

Look out for upcoming Bright Africa research – including Listed, Sovereign Debt, Infrastructure, and Real Estate – to be released during the year. Our Bright Africa Pensions research, an in-depth look at the pensions market in Africa, will follow soon. This research will also illustrate how the pool of institutional capital on the continent may be able to contribute increasing amounts into the PE market.

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Daiyaan provides expert independent valuations of private companies across Africa for a range of clients, including private equity funds and institutional investors. He is involved in analysing entity and market information to identify major valuation and risk drivers, develop and interpret financial models, and determine the enterprise and equity values of an entity. He was part of RisCura's *Bright Africa 2021 Private Equity* in Africa report and is involved in business development tasks including preparing client proposals and seeking new business opportunities for the Alternative Investment Services team. Before joining RisCura in 2021, Daiyaan completed his SAICA articles at Ernst & Young and served academic articles at the University of Cape Town in the College of Accounting's Taxation department.

About Bright Africa

Bright Africa was first launched in 2013 and is RisCura's research resource that seeks to answer investors' questions by providing insight into Africa.

About RisCura

RisCura is a purpose-driven investment firm that offers investors unique insights, advice, and investments on their journeys to achieving exceptional performance, while still meeting their broader investment goals. Today RisCura advises clients and manages investments with combined assets of more than R2.5 trillion.

A global leader in emerging and frontier markets, RisCura is known for its investment expertise and offers services to asset owners, investment managers and service providers across the industry. Through constantly exploring new ways to invest with care and meet the needs of clients, RisCura has helped to bring about impactful investment opportunities in the markets we operate in, while steering global capital towards investments that benefit society and the planet in the long run.

RisCura has won numerous industry awards and has a footprint in South Africa, the United Kingdom, the US, China, Hong Kong, Botswana, Kenya, Mauritius, Namibia, Nigeria, Zambia and Ireland.

For more information about its investment services and approach, visit **www.riscura.com**.

Introduction

It is often difficult to interpret changes in private equity (PE) market prices over time because many of the drivers are unobservable. This Bright Africa Private Equity research focuses on the PE ecosystem in 2021 – including fundraising, dry powder, investments and pricing – and considers some interesting trends.

Generally, the same factors that influence PE market prices also influence any investment's price. For example, the balance between supply and demand of capital influences pricing, something that is well illustrated by buoyant equity markets and high prices paid for debt instruments (resulting in low yields) whenever central banks use quantitative easing as a policy instrument.

Within the market, the level of fundraising for PE funds and capital allocated and invested by other investors in the private markets, determine the supply of capital. To gauge this supply, we examined fundraising and dry powder levels for PE funds and deal-making activity. The fundraising directly reflects the capital raised by investment funds. At the same time, deal-making activity is indirect evidence of all capital available in the markets and supply of investable assets – this analysis has revealed some interesting changes and more on this can be found under our Investment Activity section of this report.

Historically, the volume of exits along with the quality of exit routes available in Africa was of central concern for investors looking to access African PE. This is evident in a recent African Private Equity and Venture Capital Association (AVCA) PE survey where many LPs and GPs cited limited exit opportunities as a challenge for PE fund managers in Africa over the next three years. However, data shows that exits are taking place in Africa: there were 270 exits recorded between 2015 and 2020 on the continent. In our Exits section, we look at the exit trends and analyse the recent developments.

The perception of risk and returns, compared to other investment opportunities, influences pricing. To shed some light on this, we explore the theoretical cost of equity, which reflects the perceived risk of the different markets. The gradual recovery following the dramatic impact of Covid-19 has resulted in a normalisation in perceived risk.

Growth expectation is another factor that contributes materially to pricing. Africa's Overall GDP contracted by 2.4% in 2020, which is less than that of global GDP (3.6%), the eurozone (6.7%), and the Americas (4.3%). According to EY's Africa Attractiveness Report 2021, the continent is projected to grow on average by 4% per annum until 2025.

After examining all of these factors that influence pricing, we then looked at price trends in both South Africa and Africa ex SA. We observed a significant difference between South Africa and the rest of the continent driven by notable differences in capital markets and the perception of risk and returns.

1. Fundraising over time

Before the remarkable market contraction in 2020 and 2021, private equity (PE) fundraising activity across Africa showed strong growth between 2016 and 2019. The total value of PE fundraising in 2019 reached USD3.88 bn, the second-highest year of fundraising since 2010.

Driven by a risk-off environment, the low growth persisted and resulted in a low level of funding. This decrease illustrates just how much the pandemic caused uncertainty, economic distress, and other lingering effects. International lockdowns disrupted trade and massively decreased economic activity. These international events – combined with downgrades, currency devaluations, and revised investment sentiment towards Africa – adversely affected fundraising initiatives.

The significant decrease in the funds raised over the past two years stands in stark contrast to the highs reached in 2019. Fundraising highs in 2015 and 2019 were the result of a handful of large funds achieving their final closes in those years. For example, in 2015 Development Partners International (DPI) announced the final close of their second fund at USD750 m, and Helios announced a USD1.1 bn final close of their third Africa-focused fund, with both fund managers exclusively focused on Africa. This lumpy nature of fundraising in the market further contributes to the dramatic contraction in fund-raising levels.

In October 2021, DPI, via the African Development Partners (ADP) III fund, closed almost USD900 m towards innovation-led African companies. The co-founder and chief executive notes that "Africa remains an exciting investment destination with positive demographics, rising adoption of technology, and rising consumer and business spending." Interestingly, the focus will be innovation-driven companies leading the continent's digital transformation with deep integration of impact and ESG, in line with the market focus observed in this report.

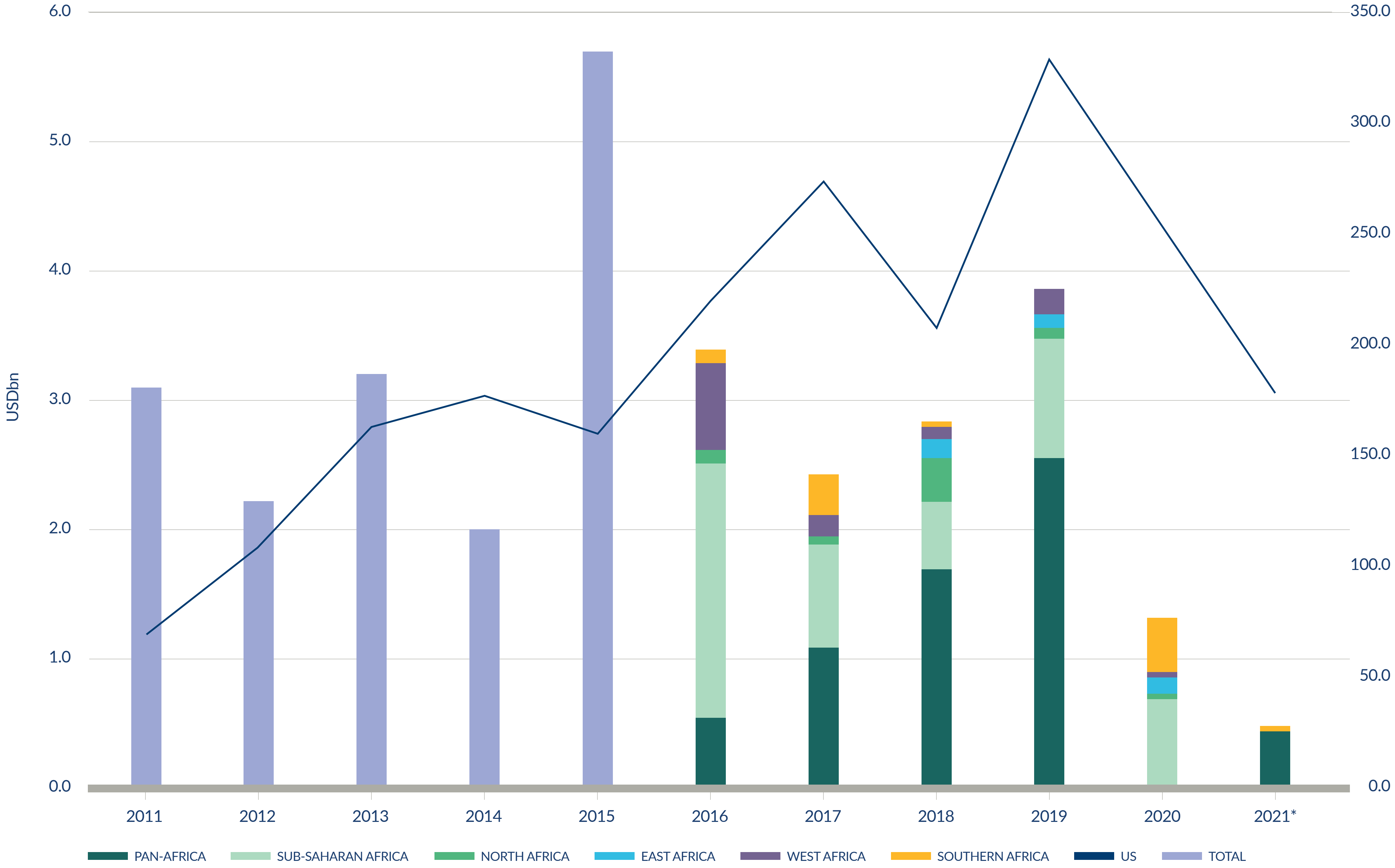
The emerging international trend of focusing on Responsible Investing is also playing out in the African market. Of the funds raised in 2020, USD498 m, or 38%, was allocated to Impact Fund managers as classified by AVCA. This is a welcomed increase from previously held proportions of 15% in 2017 and 6% in 2018 respectively.

MSCI's emerging and frontier market index data showed a significant rebound in investor interest in these markets, returning to pre-pandemic pricing levels around August 2020 and February 2021, respectively. This trend continued throughout 2021 and into 2022. However, the change in sentiment has not filtered down to African PE fundraising. The longer-term and illiquid nature of private equity investment, as well as the recent performance of African private equity, may contribute to this divergence.

Pitchbook's Annual US PE Breakdown reports noted a similar trend in fundraising in the US. Following an all-time high of USD331.5 bn in 2019, up 59% from the prior year, PE fundraising also contracted. It remained buoyant in comparison with the African market (at USD251.9bn in 2020,

Fundraising from 2011 to 2021

REGION FOCUS IN USDbn



*2021 relates to the six-month period ended June 30

Source: AVCA, RisCura analysis chart

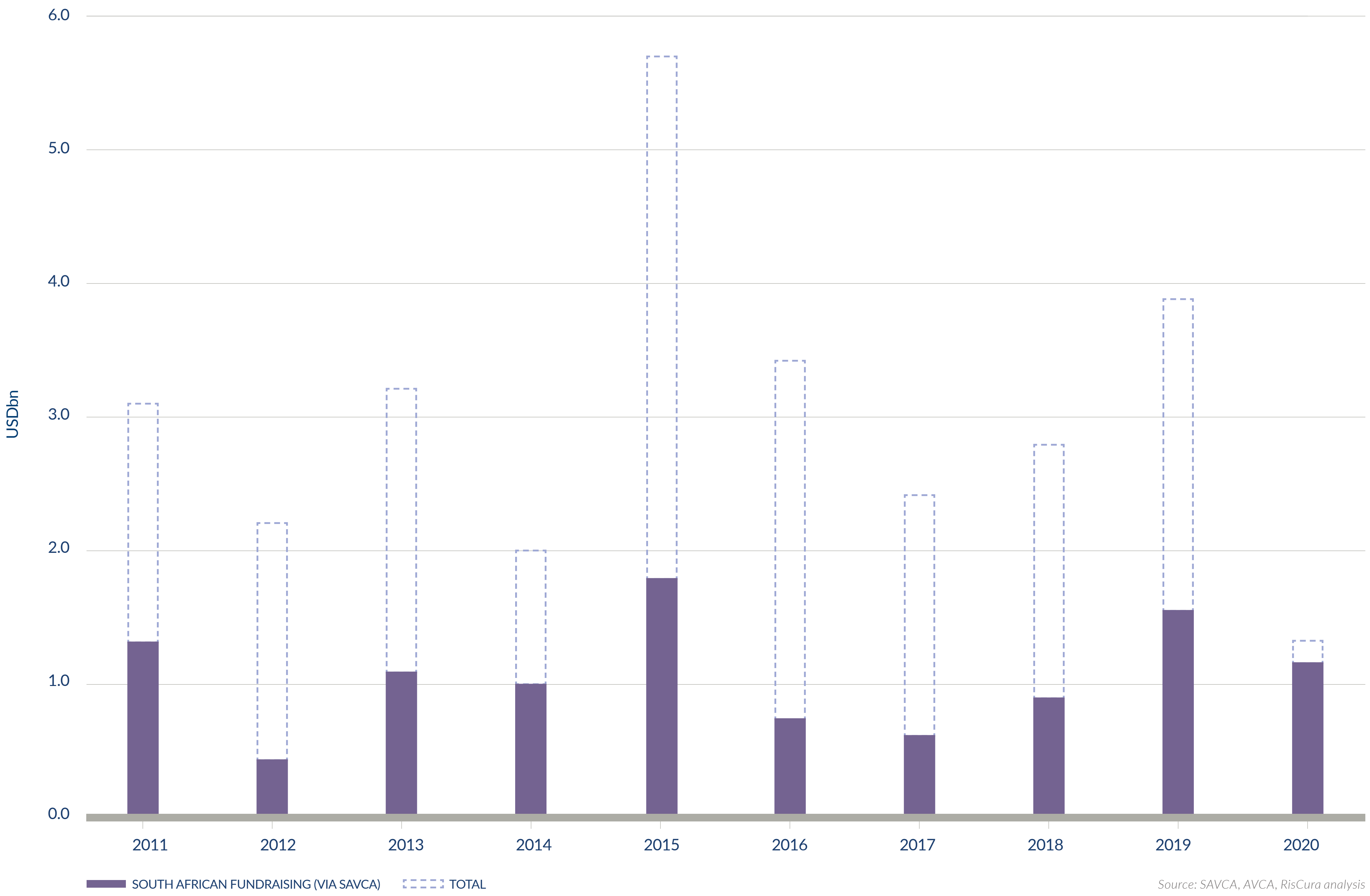
and USD179.6 bn for the six months ended June 2021) suggesting a full recovery. Despite the recent macroeconomic turmoil, the fundraising reflects a continuation of the increased interest in alternative investments from investors worldwide.

1.1 Geographic focus

The trend of Pan African fundraising continued into 2021, with fund managers predominantly Pan African focused as opposed to having a region-specific fund mandate, as observed in the previous graph.

South Africa has not been subjected to the same extreme changes in fundraising as the rest of Africa, illustrating the structural differences between the two markets. According to Southern African Venture Capital and Private Equity Association (SAVCA), southern African fundraising declined in 2020. However, the decline was not as great as that of the 2016-2018 period, despite the headwinds Covid-19 caused. The 22.1% decline in fundraising compares to a 19.1% decline in global PE fundraising. Nonetheless, global PE fundraising rebounded significantly in 2021, with H1 2021 global PE fundraising 57.9% up on H1 2020. It is interesting to observe southern Africa following suit. AVCA is already reporting USD1.3 bn private equity fundraising in Africa being raised for the broader continent in the first half of 2021 when including final and interim closes.

Southern Africa Fundraising



Source: SAVCA, AVCA, RisCura analysis

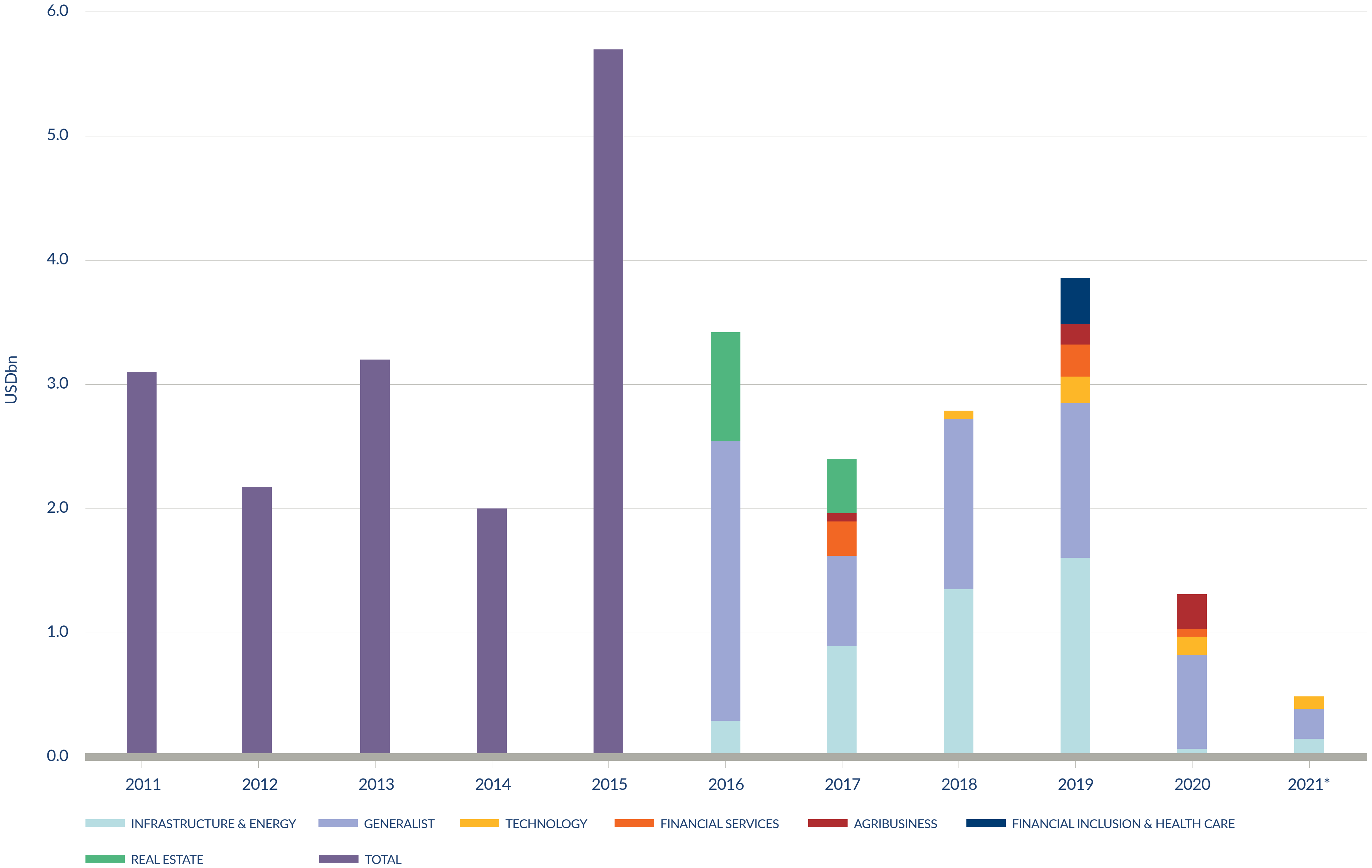
1.2 Sector focus

A trend previously observed in the breakdown of fundraising into investment themes is the high proportion of funding raised for infrastructure themes. The combination of Infrastructure and Energy represents almost half of all fundraising in 2018 and 2019. Of the total USD3.8 bn PE fundraising closed in 2019, USD1.6 bn (42%) was focused explicitly on the infrastructure & energy sectors. This represents an 18% absolute increase when compared to the fundraising closed in 2018. This allocation dwindled to USD156 m in 2021. In February 2022, the draft amendments to South Africa's Regulation 28, which sets the prudential capital allocation limits for pension funds, specifically addressed investment into Infrastructure. These amendments introduce more effective maximum limits for the trustees of retirement funds to invest for the long term in various forms of infrastructure projects. This change may increase capital flows to this asset class in the future.

The data for 2020 and six months of 2021 shows us that the regional split and the investment themes of funds raised indicate that the market continues to favour generalist funds with a broad regional mandate. This may be due to Africa's economies remaining largely informal and fragmented. According to the IMF, the informal sector makes up from 20% to 25% of GDP in Mauritius, South Africa, and Namibia, and up to a high of 50% to 65% in Benin, Tanzania, and Nigeria. Along with small, fragmented, and poorly connected markets and the high cost of compliance, these factors limit the number of investable opportunities available to investors. This limitation necessitates a wider mandate to ensure that sufficient opportunities with a desirable risk and return profile can be identified and evaluated.

Fundraising from 2011 to 2021

SECTOR FOCUS IN USDbn



*2021 relates to the six-month period ended June 30

Source: AVCA, RisCura analysis

2. Dry Powder

Dry powder refers to the amount of committed but unallocated capital a firm or fund has on hand. We have estimated the dry powder of the African Private Equity Industry, using fundraising data and the average deployment period RisCura observed.

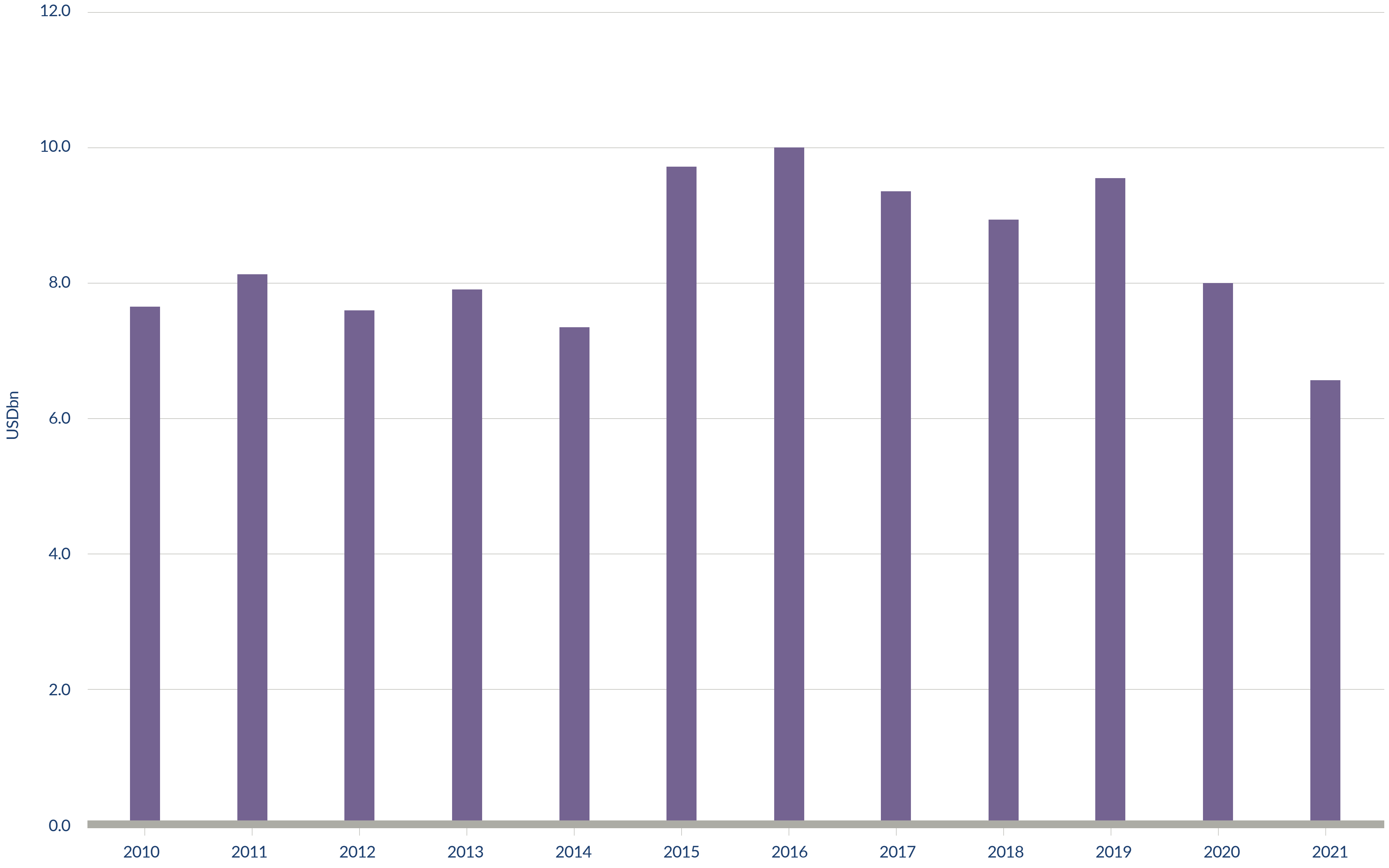
> *Dry powder levels averaged just around USD8.51 bn until 2018, reaching recent highs of USD9.56 bn in 2019, which was previously achieved in 2016. The levels declined to about USD6.5 bn by June 2021. The rebound in 2019 correlates with the spike we saw in broader Africa fundraising noted in the fundraising charts.*

The decline in 2021 was due to investment funds continuing to draw on committed capital – to invest in new businesses and support existing investments through the pandemic – without the corresponding flow of commitments from LPs through fundraising. This reduction in dry powder should contribute significantly to stabilising private equity pricing going forward.

In the remainder of the world, according to Pitchbook current dry powder levels in VC and PE hit unprecedented sums, with around USD1.5 tn available to fund managers worldwide in 2020. While fuelling private equity dealmaking, and with more cash on hand than ever, firms are grappling with how to deploy it and the impacts it could have on returns.

Dry Powder

SECTOR FOCUS IN USDbn



Source: RisCura analysis

3. Investment activity over time

The above fundraising represents the supply of capital available from private equity funds for investment. The extent to which an equal supply of investable opportunities exists cannot be observed directly. However, the level of deal activity and the prices at which investors make such investments can be measured.

Total private equity transaction activity steadily increased by 20% from June 2018 to June 2019. It tapered slightly to a 9% increase from June 2019 to June 2020, defying the collapse in fundraising. Transaction activity then rebounded strongly by June 2021, resulting in a 19% increase from June 2020 to June 2021.

As illustrated in the dry powder discussion, fund managers continue to deploy the significant supply of capital created in the market during earlier fundraising years. A key observation, however, is that while the quantum of transactions occurring is increasing, the value per transaction is not. The average transaction value in our database between 2016 and 2019 was USD40.44 m, whereas between 2020 and 2021 it shrunk to USD11.1 m.

Key drivers underpinning the investment case in Africa include a youthful population boosting productivity, rapid urbanisation, and accelerated technology uptake. These factors continue to support long-term growth in activity.

3.1 Geographic focus

Over the past three periods, South Africa represented a relatively consistent share of transaction activity (approximately 25%). Despite South Africa's limited growth prospects and increased risk profile, transaction activity continues to increase along with the rest of the continent, growing 13% between 2020 and 2021. The South African economy continues to face significant challenges in 2022 and beyond, following sluggish GDP growth, mismanaged state-owned enterprises, increasing unemployment, and policy uncertainty. This has resulted in the country's sovereign credit rating being affirmed at sub-investment grade.

As a continuation of the historic trend, there was a significant uptick of 104% in deal activity in Egypt between 2019 and 2021. Egypt maintained its ranking in RMB's Where to Invest in Africa 2021 report as the number one investment destination in Africa. Egypt has a large and diversified economy and an improved business environment stemming from recent investment-related legal reforms that resulted in improved investor sentiment. Furthermore, Egypt was praised by the IMF for implementing one of the most successful economic turnaround programmes, which commenced in 2016. The improvement in Egypt's business environment is evident in the country's eight-place jump in the World Bank's Ease of Doing Business rankings between 2018 and 2020.

Another notable country is Morocco. Despite being ranked second to Egypt in investment attractiveness, it has not attracted significantly more investment to the region. This may be partially due to reluctance to invest in tourism-sensitive economies such as Morocco, whose economy has taken a hit from the pandemic and may take longer to recover. According to the World Bank, tourism contributes 11% of the country's GDP and accounts for 17% of the workforce. Morocco will remain dependent on Europe for tourism, foreign direct investment (FDI) and remittance inflows.

According to EY's Africa Attractiveness Report 2021, North Africa was one of the regions the pandemic affected the most, with Morocco registering the second-highest Covid-19 cases in Africa. It saw a sharp contraction in GDP of 7.1% in 2020 — its first recession in over two decades. The dual shock of the pandemic and recent severe droughts drove this.

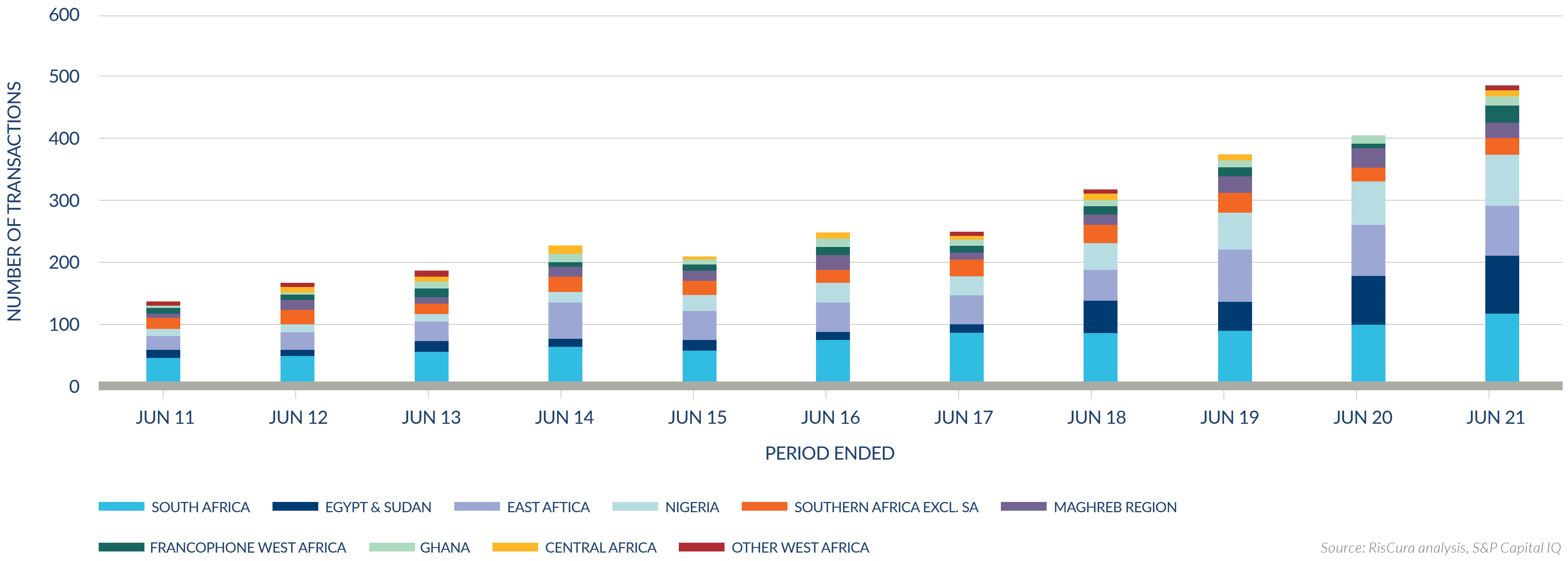
The East African portion of investment activity has remained relatively stable over the past three years at around 20% of African investment activity. Kenya accounts for 64%, the largest portion of East Africa's investment activity for the period ended June 2021, representing an increase from a 52% share as at June 2020. The country continues to dominate the region's PE investment landscape because of its large and diversified economy, pro-business government policies, and relatively low dependence on extractive commodities. East African countries hold a third of RMB's top 10 investment attractiveness rankings, with Kenya expected to be one of Africa's fastest-growing economies over the next five years.

Deal activity in Nigeria followed the continent average and increased by 18% for the period ended June 2021, compared to the 50% and 13% increases experienced for the periods ended June 2019 and June 2020 respectively. Currently, Nigeria has the third most significant proportion of Africa's investment activity, with information technology (IT) investments dominating sector allocations.

As Africa's largest economy, Nigeria accounted for 17% of total transaction activity in 2021, increasing steadily over the previous few years. Improved investor sentiment drives the increase in activity in Nigeria. The improvement is the result of large consumer demand, government incentives, and improved foreign exchange liquidity. According to RMB, the efforts made to support small and medium enterprises through monetary policy reform will be fundamental to Nigeria's development. This should aid the country's efforts as it continues to expand into sectors such as IT and shifts away from being a predominantly commodity-reliant economy.

Activity continues to trend upward

NUMBER OF PRIVATE EQUITY TRANSACTIONS BY REGION



Source: RisCura analysis, S&P Capital IQ

3.2 By sector

Investment activity in the consumer discretionary sector remained stable over the year. Within this sector, investor interest has moved towards internet and direct marketing retail, education and communication services, and publishing. This shows a possible shift from targeting a broader target market with lower income to a smaller market with a higher income.

Investment activity in consumer staples has decreased by a considerable 38% in absolute terms and moved from 13% of total investment activity to only 7% as at June 2021. Consumer products have historically been the focus of private equity in Africa, due to the perceived opportunities resulting from the continent's growing middle-class. The South African and Nigerian markets remained the bulk of consumer staples investments, with other countries attracting less investments within this category.

The Covid-19 pandemic has exposed the importance of and likely greater focus on specific key sectors, such as healthcare and pharmaceuticals, education, and IT, with investors attracted to tech-enabled businesses that can sustain growth through the current and future regional and global disruptions.

Internet and direct marketing retail companies, which are classified as a subsector of the consumer discretionary sector, have enjoyed a 63% growth. Given recent events as a result of the global pandemic, the shift to online retail has been accelerated. E-commerce in many parts of the world is likely to be revolutionised and could present substantial opportunities. Africa's large and growing young population is expected to continue to drive demand for online retail and services. According to the United Nations Conference on Trade and Development's Business-to-Consumer's e-commerce index of 2020, Mauritius, South Africa, Tunisia, Algeria, Ghana, Libya, Kenya, Nigeria and Morocco all rank within the top 100 of the index globally.

Despite the positive drivers for online retail and services, several factors limit e-commerce's expansion throughout the continent. These include high broadband costs, low bank card penetration, and limited e-commerce payment options. Ironically, these same factors present opportunities to invest in innovative infrastructure solutions that enable e-commerce in Africa.

> *Investment activity in the IT sector (excluding internet and direct marketing retail companies) experienced significant growth of 49% from June 2020 to June 2021, with its proportion of total investments increasing from 24% to 30%. Investment in this sector in Africa mostly consists of internet software and services, application software, and data processing and outsourced service companies, with the large majority directed towards venture capital application software. Egypt, Nigeria, South Africa and Kenya attract the highest level of investment into the IT sector on the continent.*

According to Bain & Company's Global Private Equity Report 2021, the number of PE deals slumped across the business landscape compared with the five-year average, except for the technology and telecom sectors. Globally, the broad technology sector attracted the most PE investment in 2020 (29% of total buyout deal count globally, 32% including fintech), with several subsectors standing out. Funds gravitated towards software as a service (SaaS) based businesses with particularly sticky business models.

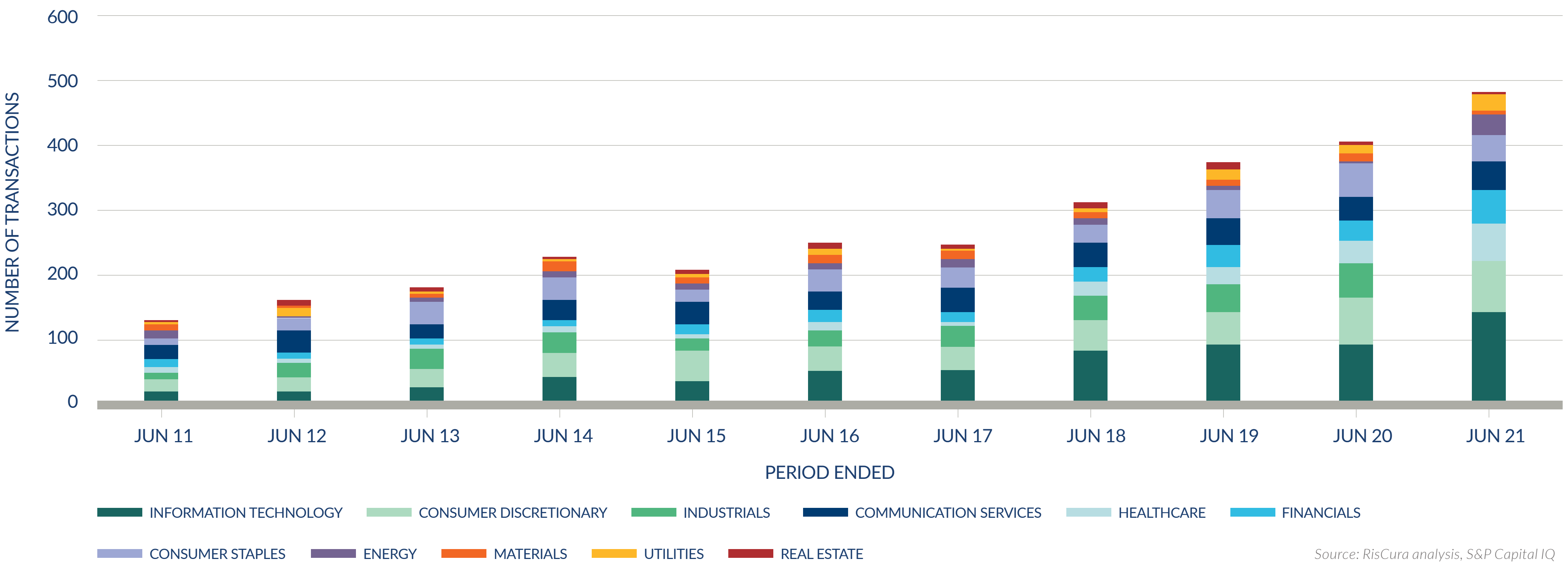
Following a subdued period ending June 2020, investments in the healthcare sector increased by 40% as of June 2021, with venture capital investments in the 'technology healthcare' subsector attracting the most transactions, where Egypt and South Africa are the biggest gainers. This was primarily driven by the increased focus on the sector and opportunities. The 2021 Deloitte Africa Private Equity Confidence Survey notes that the pandemic revealed gaps in the healthcare systems in the region, increasing investments that are expected to improve access to medical equipment and healthcare facilities in the broader health ecosystem.

The other two traditionally large sectors for investment — financials and industrials — have attracted similar levels of investment activity in the period ended June 2021 when compared to the prior year. Industrials include the construction, engineering, transport, logistics, equipment, and machinery industries. Investment is mostly in the light industrial sector with a focus on import substitution. The two above-mentioned sectors have contributed a total of 9% and 13% of the total investment activity respectively as at June 2021.

Weighing in at 10% of investment activity, the communication services sector saw a 43% increase as at June 2021. The largest sub-sector of this category is Interactive Media and Services, which includes companies engaging in content and information creation for distribution through proprietary platforms. Interactive media adoption grew largely on the back of the pandemic, which catalysed the shift towards digital media consumption.

Information Technology in demand

NUMBER OF PE TRANSACTIONS BY SECTOR



Source: RisCura analysis, S&P Capital IQ

Classifications as per the GICS® (Global Industry Classification Standard)

4. Exits

Historically, the volume of exits and the quality of exit routes available in Africa have been key concerns for investors looking to access African PE. Most LPs and GPs in AVCA's 2021 African Private Equity Industry Survey cited limited exit opportunities as a critical challenge for private equity fund managers in Africa over the next three years. Furthermore, AVCA's survey, Volatility and Uncertainty: How Private Equity in Africa Navigates Through Turbulent Times, found that approximately half of the respondents had to amend their exit plans because of political or currency risk in their investment geographies.

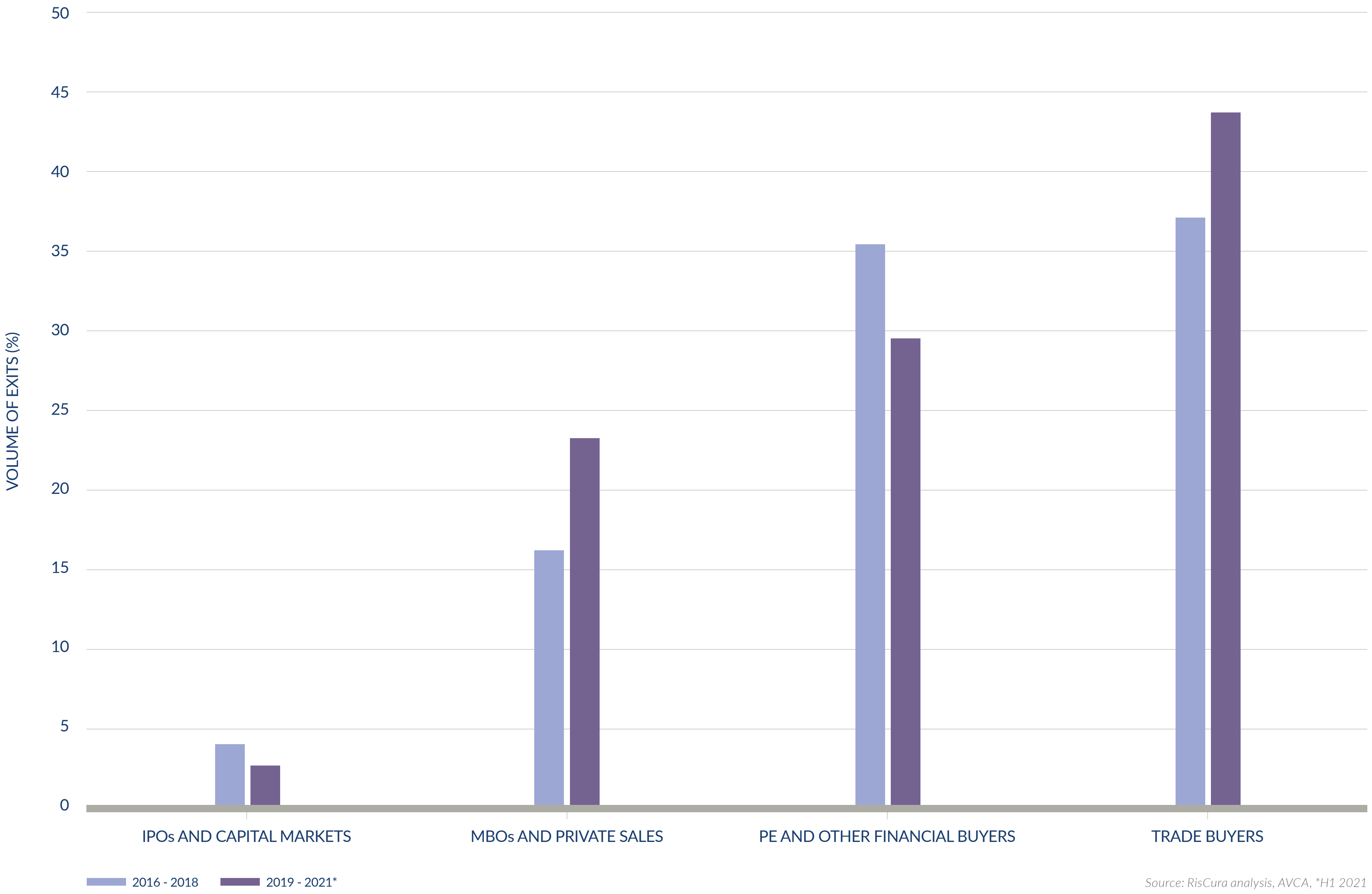
Exit data published to date in Africa does not specify the US dollar amount of exits achieved, but it shows the number of exits. According to AVCA, African PE had an average holding period of 6.4 years between 2010 and 2021, with the holding period reaching its maximum at eight years in 2020.

Trade buyers remain the most popular African private equity exit route. Trade buyers represent existing businesses wishing to synergise the PE company with their current operations. This is followed by exiting through other PE and financial buyers, with the third most popular exit being management buyouts (MBOs). IPOs represent the least popular exit route on the continent, mainly because of the illiquidity that characterises African stock exchanges.

Exit activity reached record highs in 2015 with 56 exits. Subsequently, the volume of exits reported in Africa dropped to an average of 47 per year between 2016 and 2019. More recently, 2020 yielded 33 exits. During the six months ended June 2021, 16 exits occurred. AVCA further noted that lower exit activity is mainly due to a decrease in exits recorded in South Africa, given a backdrop of heightened macroeconomic uncertainty in the country. In 2020, the number of exits reported on the continent decreased significantly to 33. This reflects the economic implications of the Covid-19 pandemic and the fact that GPs prioritised portfolio management to protect their investments.

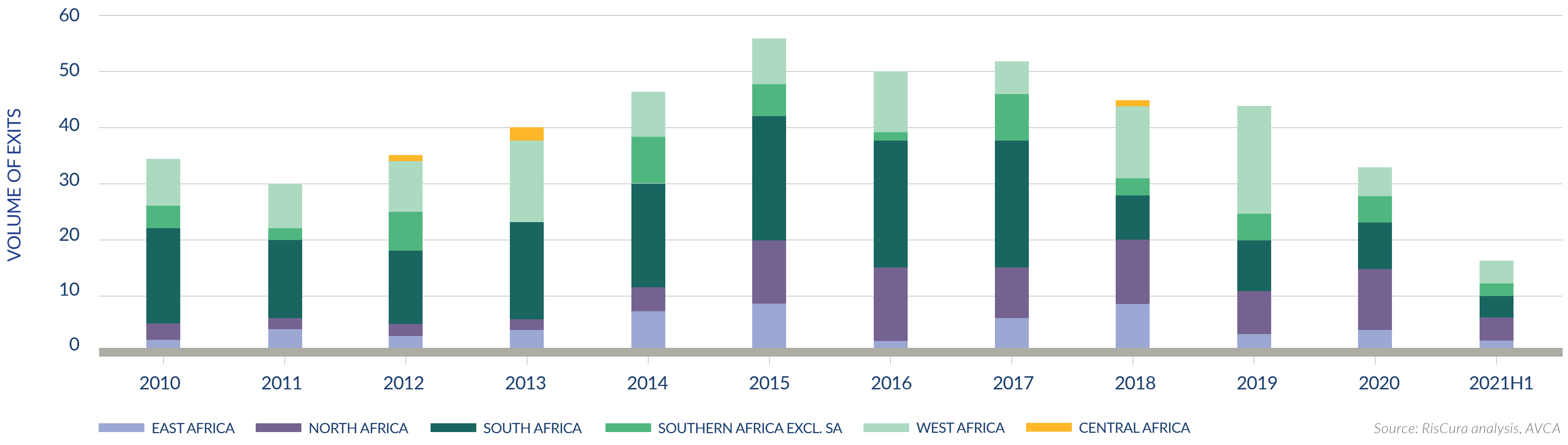
Since 2010, financials have consistently been one of the main sectors of investment, representing on average a quarter of all African exit activity. The industrials sector followed closely behind.

Exit Routes



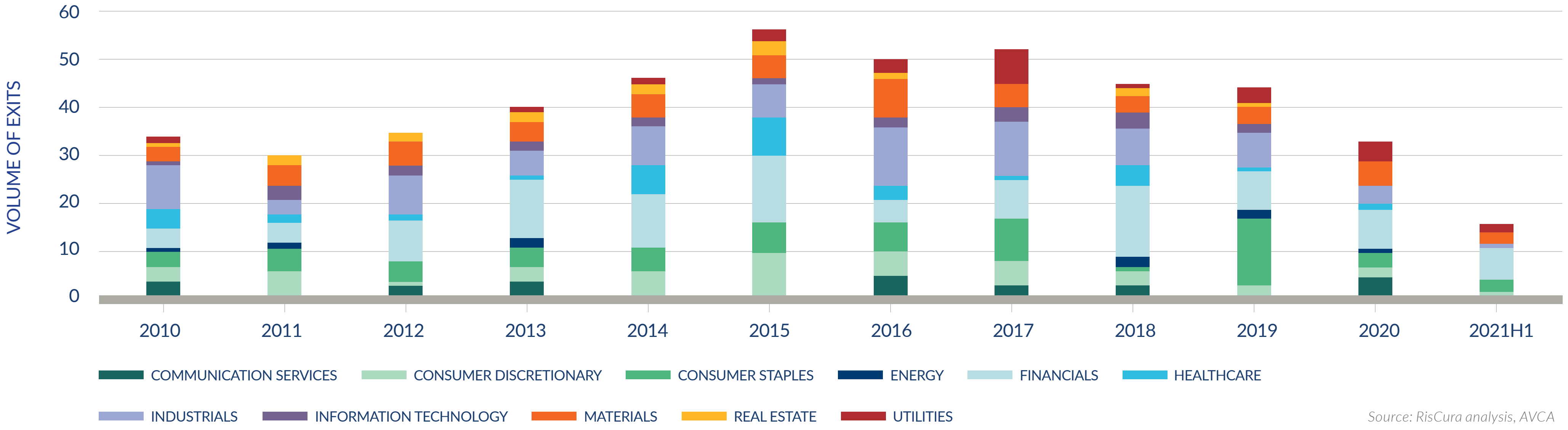
Source: RisCura analysis, AVCA, *H1 2021

Exits per Region



Source: RisCura analysis, AVCA

Exits per Sector



Source: RisCura analysis, AVCA

5. Changes in perceived risk and reward

Along with changes in the supply of capital and investable opportunities, another factor that influences the prices at which assets change hands is the perceived risk and rewards of a particular investment. Cost of equity (COE) represents investors' estimate of a fair rate of return required for an investment based on the risk. To estimate the changes in the risk exposure perceived by investors, we have estimated an average cost of equity for each market.

Comparatively, from December 2019 to March 2020, increases in COEs were experienced in all countries. These include significant markets such as Ghana, Kenya, and Nigeria, where COEs increased by 2.96%, 2.34%, and 2.59%, respectively. This COE increase is attributable to a universal rise in risk due to the global impact of Covid-19. From March 2020 to June 2020, the COE reduced for most markets under review in response to countries loosening monetary policy measures.

The sovereign credit default spread is a quantitative measure of each country's sovereign risk. This measure is used to build up the COE of each country. The graph below illustrates how credit default spreads (CDS) changed from January 2020 to June 2021 for a select group of African countries.

Overall, we saw a steady decrease in sovereign CDS from April 2020 to July 2020. This contrasts with the sharp increase previously observed, which was fuelled by the global risk-off environment ignited by the devasting economic impact of the novel coronavirus. Investors had shifted away from riskier emerging and frontier markets towards safer, more developed markets. As African markets are classified either as frontier or emerging, this impact was felt heavily.

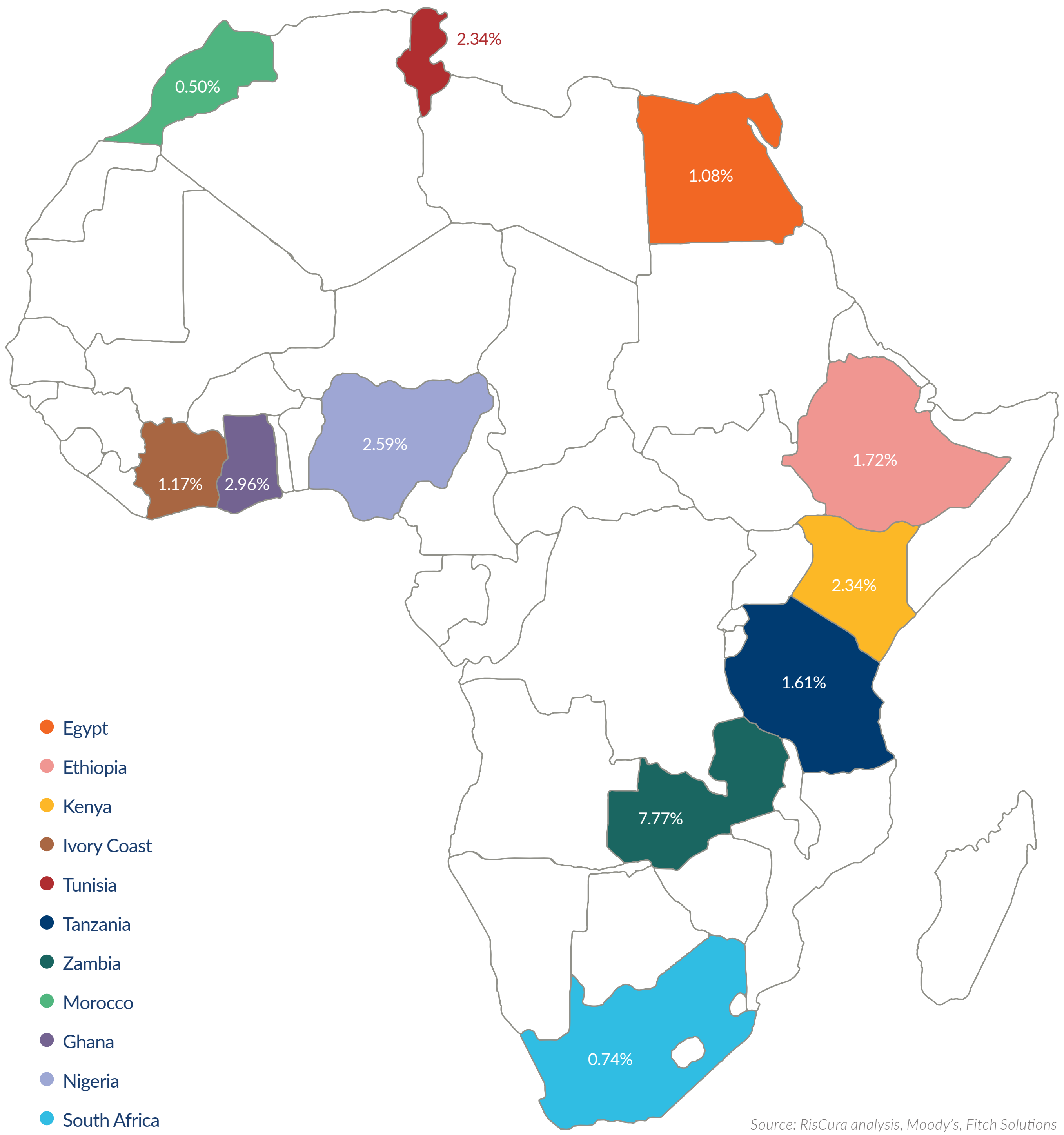
Change in Cost of Equity over time

CHANGE IN COE

DEC 2019 - MAR 2020

MAR 2020 - JUN 2020

JUN 2020 – JUN 2021



Source: RisCura analysis, Moody's, Fitch Solutions

Movements in the CDS from July 2020 to June 2021 indicate a rebound for most markets, with some returning to pre-pandemic risk levels. This speaks to the corresponding decrease in the cost of equities over the period. The movement in CDS represents the stabilisation of markets as global economies recovered from initial lows, as well as the impact of worldwide quantitative easing.

All the countries that form part of the analysis showed a decrease in the cost of equity from June 2020 to June 2021. Egypt experienced the most significant decline: 5.1%. Considerable decreases in Egypt's sovereign CDS and equity risk premiums drove the decline. Egypt's economic prospects, including GDP growth, continue to improve considerably on the back of a strong increase in the services trade surplus and resilient remittance inflows supported by an affirmed B+ stable outlook. Furthermore, FitchSolutions anticipates that Egypt's budget deficit will narrow further into FY22 as the government resumes fiscal consolidation efforts.

The Covid-19 crisis remains a threat given that countries like Egypt are particularly reliant on tourism. The global and local spread of the virus is difficult to predict and could have adverse impacts on our growth forecasts, particularly given the slow rate of vaccination on the continent.

Kenya, Nigeria and Zambia also experienced considerable COE declines of 4.2%, 4.5% and 4.1% respectively. The universal considerable decline in sovereign CDS and varying levels of reduction in equity risk premiums drove the reductions. With ratings affirmed, real GDP in these countries is expected to gradually rebound to pre-Covid-19 levels in 2022.

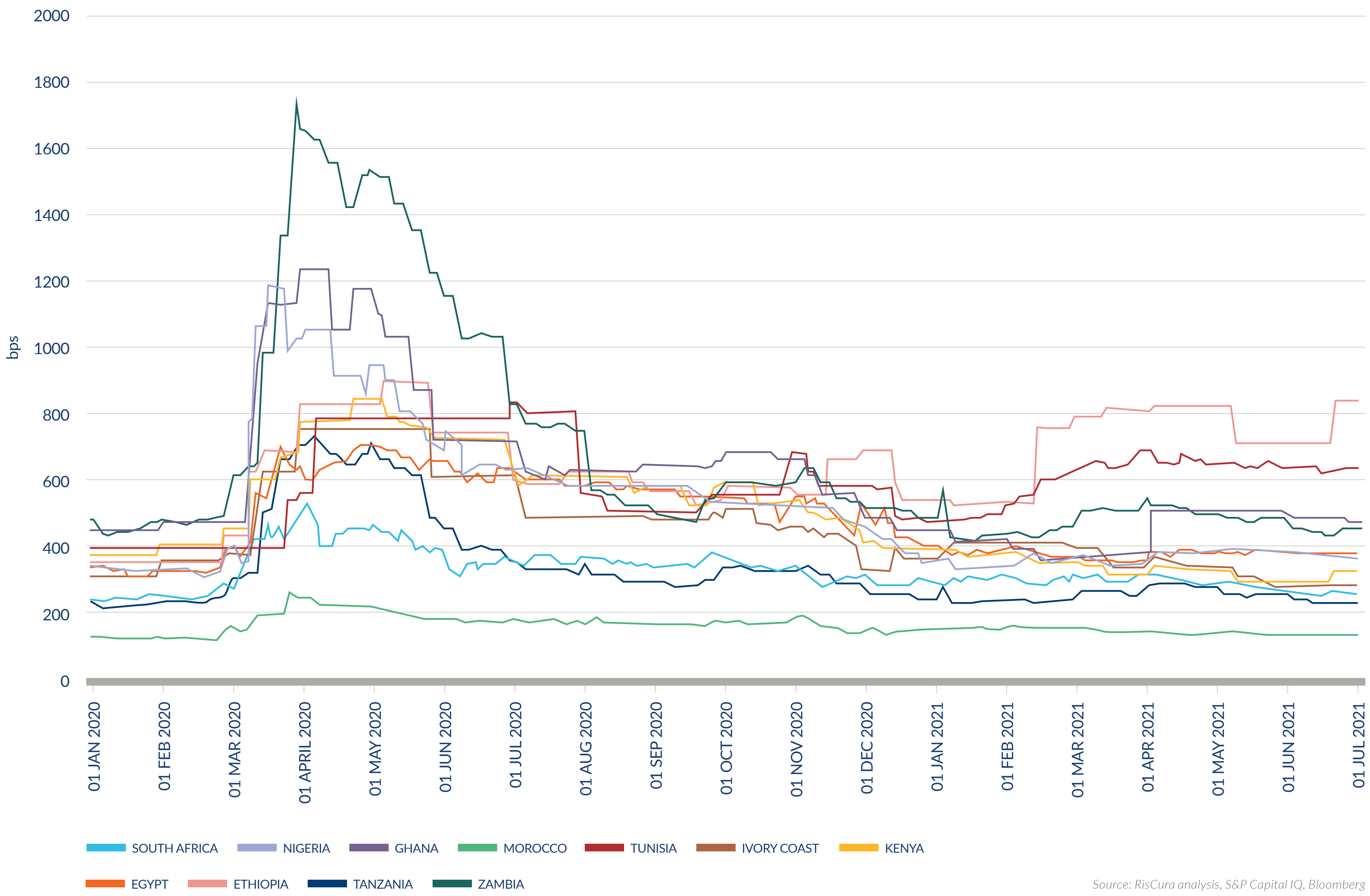
The increase in Ghana's long-term inflation expectations drove the rise in the currency premium. This, in turn, drove the smaller reduction in the country's COE. FitchSolutions forecasts GDP growth to accelerate on the back of a healthy rebound in private consumption and exports.

The reduction in Ethiopia's COE was predominantly driven by the decrease in the currency premium, driven by the decrease in long-term inflation expectations. Fitch anticipates that the Ethiopian birr will continue to face downward pressure over the short term, with the pace of depreciation slowing into 2022. Ethiopia and Tunisia's CDS tails up in the latter part of the period following increased risk sentiment (as illustrated in Graph Credit Default Spreads), and corresponding ratings downgrades underpinned by fiscal consolidation issues.

COE movements experienced for South Africa and Tanzania have been more subdued, which indicates minimal movements in overall investor risk perception in these countries over the past year. Perceived increases in sovereign risk offset expected decreases in COE from the universal increase in appetite for risk. In November 2020, Fitch downgraded South Africa by one notch to BB- and in August 2020, Moody's downgraded Tanzania by one notch to B2.

A rise in country risk following the pandemic

CREDIT DEFAULT SPREADS FROM JAN 2020 - JULY 2021



Source: RisCura analysis, S&P Capital IQ, Bloomberg

6. Private Equity pricing in Africa

6.1. Over time versus listed equity

Africa ex. South Africa

The median EV/EBITDA multiples of listed equity across Africa have trended downwards since the end of 2014 up until June 2020. Conversely, median private equity EV/EBITDA multiples across Africa ex SA have steadily increased since June 2012.

For the two years ended June 2019 and June 2020, the private equity multiples exceeded those of listed multiples. This appears counterintuitive as a result of the liquidity discount that should apply to prices in the private markets. However, the lack of liquidity in the listed markets, the high cost of compliance, and the resultant lack of capital available to these markets complicate a direct comparison.

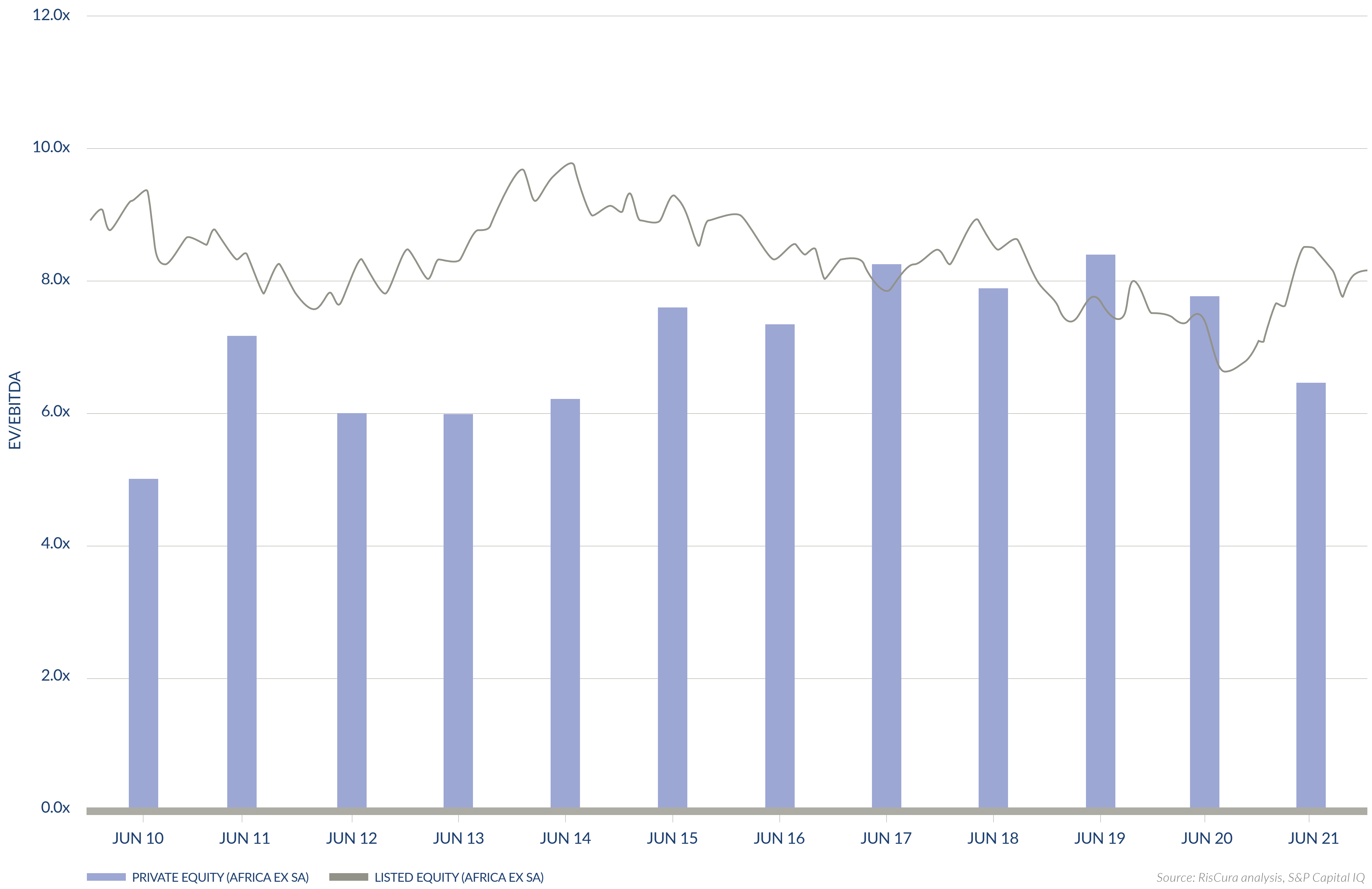
For the period ended June 2021 a more conventional relationship between listed and unlisted multiples is observed. This is the result of a recovery in prices in the listed market and a decline in the private markets. While there may have been a general risk-off sentiment towards Africa, recent reports published by Preqin observe that investor interest in alternative investments in the rest of the world is rising. The reports recognise a strong global exit market since the height of the pandemic, which has translated into high returns for alternative funds. Historically, high entry prices with muted growth resulted in pedestrian African PE performance. The lack of new capital committed to the markets has allowed pricing to normalise as the market reaches equilibrium, increasing prospects for market-related returns.

For the year ended June 2020, the impact of the pandemic and negative market sentiment resulted in a decrease of 7.3% in PE transaction multiples. The median multiple further declined by 16.7% for the period ended June 2021 as lower fundraising and ongoing negative market sentiment affected pricing.

According to the African Development Bank, African economies experienced the worst recession in more than half a century following the pandemic. They were expected to grow by 3.4%, in real terms, in 2021 and still more in 2022, underpinned by an expected resumption of tourism, a rebound in commodity prices, and a rollback of pandemic-induced restrictions. The private market pricing appears to be attractive on a forward-looking basis.

Africa ex. SA private equity prices on the rise

MEDIAN EV/EBITDA OF LISTED AND PRIVATE EQUITY TRANSACTIONS IN AFRICA EX. SA



Source: RisCura analysis, S&P Capital IQ

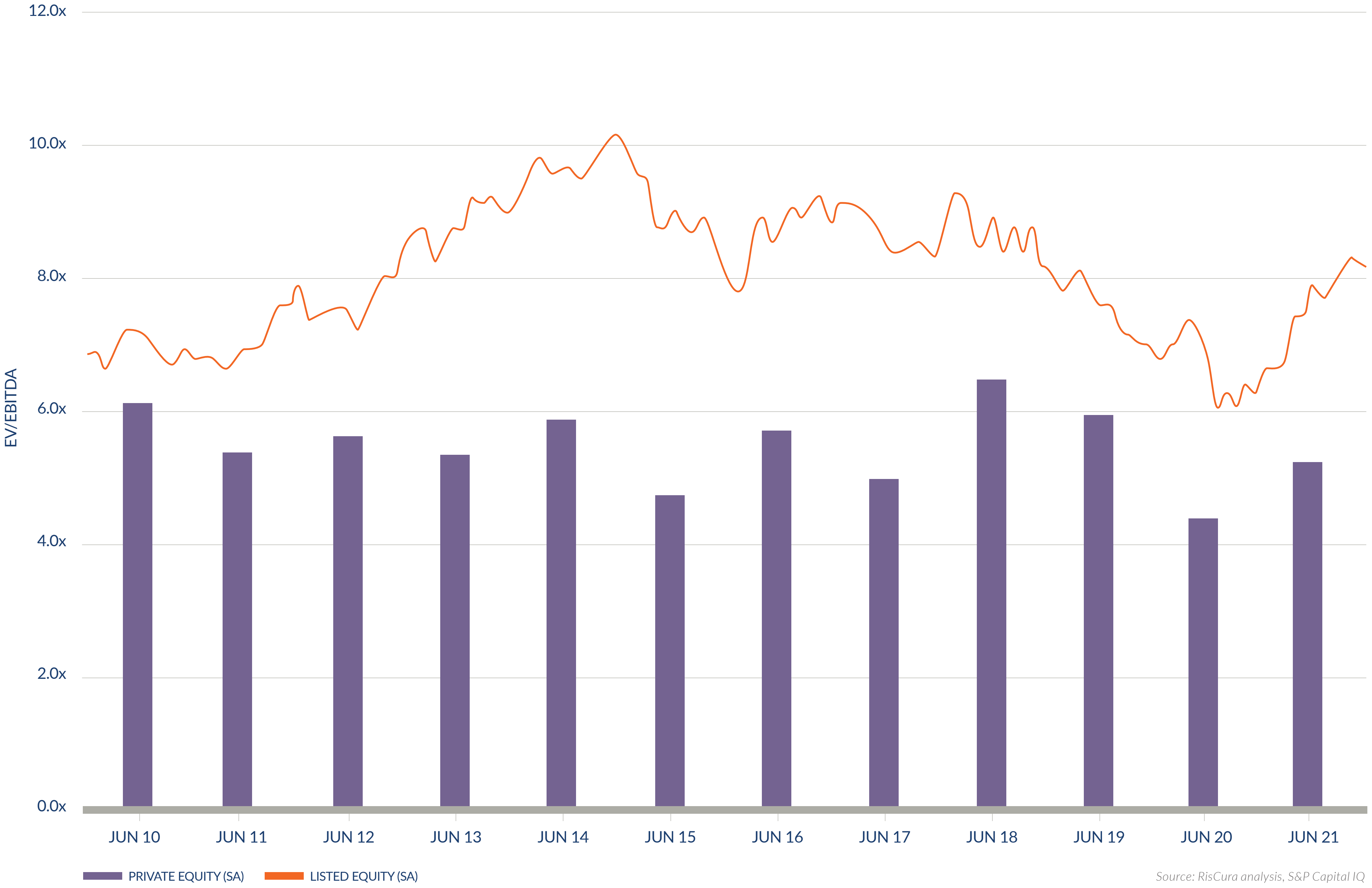
South Africa

By June 2020, the novel coronavirus had reduced demand for South Africa's exports, weakened industrial, air freight and mining activity (among others), and increased the already significant levels of unemployment. The high exposure to growth slowdowns in China and the EU, the decline in international tourists, and downward pressure on commodity prices further contributed to a poor economic performance in 2020. In 2021, there was a rebound in economic activity following the efforts to contain the virus. The South African budget, however, remains constrained. In line with listed pricing, the median South Africa private equity EV/EBITDA multiple steadily decreased between June 2018 and June 2020. However, the June 2021 median multiple improved by 18.8% year-on-year from 2020, with this trend continuing until the end of 2021. Interestingly, the rebound of South African PE prices over the June 2020 to June 2021 period was higher than Africa ex SA, possibly due to South Africa's more robust financial system and established private equity industry.

Listed multiple values similarly have rebounded to pre-2019 levels. Emerging and developing markets continue to benefit considerably from investors seekingers higher yields following the quantitative easing measures implemented in developed markets. However, with tampering efforts at play, markets such as South Africa stand to face risk-off sentiment with funds being remitted.

SA private equity prices on the rebound

MEDIAN EV/EBITDA OF LISTED AND PRIVATE EQUITY TRANSACTIONS IN SOUTH AFRICA



Source: RisCura analysis, S&P Capital IQ

In the US, the availability of debt is consistently a determinant of the multiples paid for PE transactions. Multiples are typically determined by adding a relatively fixed equity margin onto the amount of debt that can be raised. Of the Africa ex SA transactions with sufficient data to analyse, 55% of companies targeted for acquisition between 2010 and 2021 reflected a Net Debt position on their balance sheets. The average Debt/EBITDA position of these companies was 2.33x over the period. This is a considerable increase in the average compared to our last reported 1.60x multiple in the prior period.

> *Possible factors contributing to this movement could be that the industry has become more aware of the purpose of debt and the ability to achieve enhanced returns. Also, investors are slowly experiencing a mindset shift around debt and the risk it entails, specifically in Africa. Fund are managers focusing more on sustainable forms of debt, particularly from new, non-banking players.*

The consistently low levels of debt indicate that the PE industry throughout Africa is not debt-driven and has poorly developed local debt markets. Instead, earnings growth and multiple expansion drive African PE. Most fluctuations in multiples relate to investors' availability and willingness to provide equity funding.

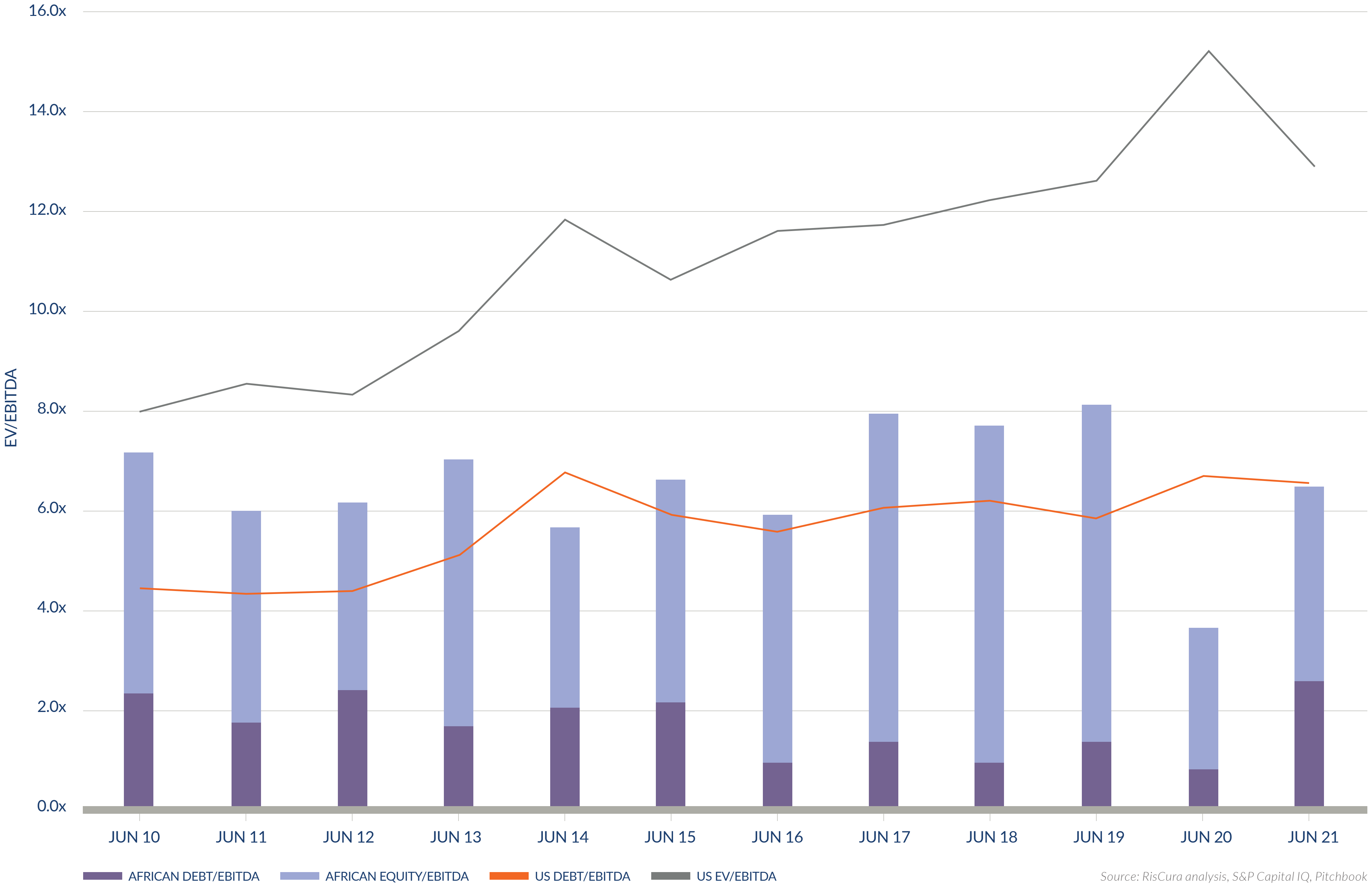
South African companies have largely followed a similar trend. In respect of South African transactions with a reported Enterprise Value, approximately 58.20% of companies entered by PE funds in the 2010 to 2021 period reflected a Net Debt position on their balance sheets. The average median Debt/EBITDA position of these companies was 2.0x over the period. The sophistication of the South African debt market in comparison to other African countries (collectively) can be considered a contributing factor to the slightly higher debt levels.

With the exception of the period ended June 2021, the debt level in African private equity increases marginally with size but hasn't risen considerably over the years. Compare this to the global norm, where Debt/EBITDA rises more quickly and to a higher level as company size increases. For instance, more than 75% of total US leveraged buyout transactions in 2019 had an average Debt/EBITDA ratio of more than 6.0x (Bain & Company, 2020). Similar trends can be seen with Pitchbooks 2021 US PE data.

PE firms provide financing where obtaining affordable debt is not a viable option, as is the case across many African countries. There was a significant uptick in interest in private credit, with several private credit funds being raised in recent years. Furthermore, the ability of private equity firms to obtain financing at an attractive rate forms an integral part of the value addition process on the continent, possibly also contributing to the rise in debt levels, as noted previously.

Availability of debt as driver of equity prices

AFRICAN EV/EBITDA MULTIPLES COMPARED TO US



Source: RisCura analysis, S&P Capital IQ, Pitchbook

6.2 By price range

Transactions in South Africa occur predominantly in the 3.5x – 7.0x bracket. In the remainder of Africa, an ever-increasing majority of transactions occur at a multiple exceeding 7.0x. Between 2012 and 2021, African multiples exceeded the South African multiple by 32% on average.

Our listed EV/EBITDA data shows a similar trend, with higher prices for securities outside South Africa being observed.

Growth expectations outside South Africa's borders could explain the higher multiples paid for the Africa ex SA trend. According to Fitch data, for Africa ex SA, real GDP is expected to grow on average at 1.39% higher per annum than South Africa between 2022 and 2030. Similarly, during 2020, the real GDP downturn in Africa ex SA, was 2.54% lower versus South Africa.

6.3 By deal size

Historically in Africa ex SA, higher-priced transactions tended to take place at the larger end of the deal size spectrum. However, a shift has been noted for African ex SA companies, in that regardless of the price range, the median EV/EBITDA multiples ranged from 5.4x to 8.7x.

For South African companies, following a change in trend observed pre-2015, with higher multiples for deals above USD100 m, the higher multiples are now seen predominantly in the USD25 m – USD100 m category. This has been relatively consistent over the current three-year period versus the prior three years. Notably, multiples within the smaller price range (<USD25 m) declined 21% over the reporting periods by June 2021.

An interesting observation is that we see a higher correlation between the deal size and multiples, in line with international norms, in Africa ex SA versus South Africa alone, particularly in the more recent periods.

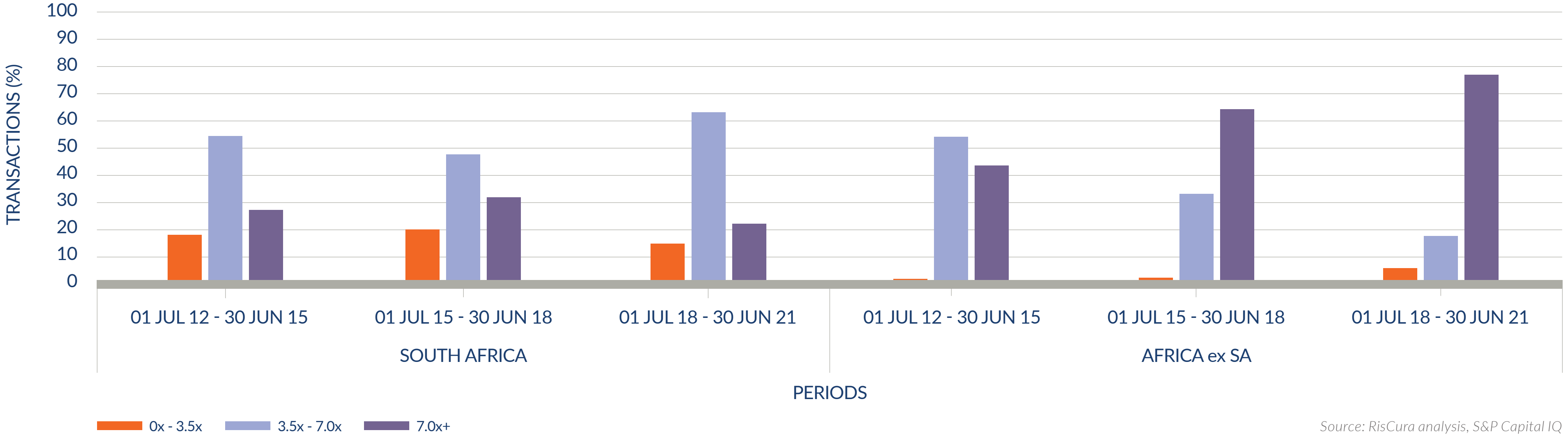
The average deal size in South Africa and Africa ex SA between July 2018 and June 2021 was USD18.97 m and USD11.98 m respectively, with corresponding average multiples of 5.56x and 7.77x. Comparatively, between July 2015 and June 2018 the average deal size in South Africa and Africa ex SA was USD31.8 m and USD54.95 m respectively(or USD36.43 m, excluding a USD4 bn outlier in 2017 from Milost Global Inc Fund towards energy and water investments in Western Africa) with corresponding average multiples of 6.44x and 9.38x.

While smaller transactions in South Africa have maintained a relatively consistent median EV/EBITDA multiple across the periods, the median EV/EBITDA multiple for transactions occurring between the USD25 m – USD100 m price range has almost doubled from the illustrated three-year period ended June 2015 to June 2021.

South Africa's macro-economic headwinds may have made larger companies that are broadly exposed to the country's economy less attractive than smaller firms that can operate in more niche areas.

Transaction multiples relative to their price range

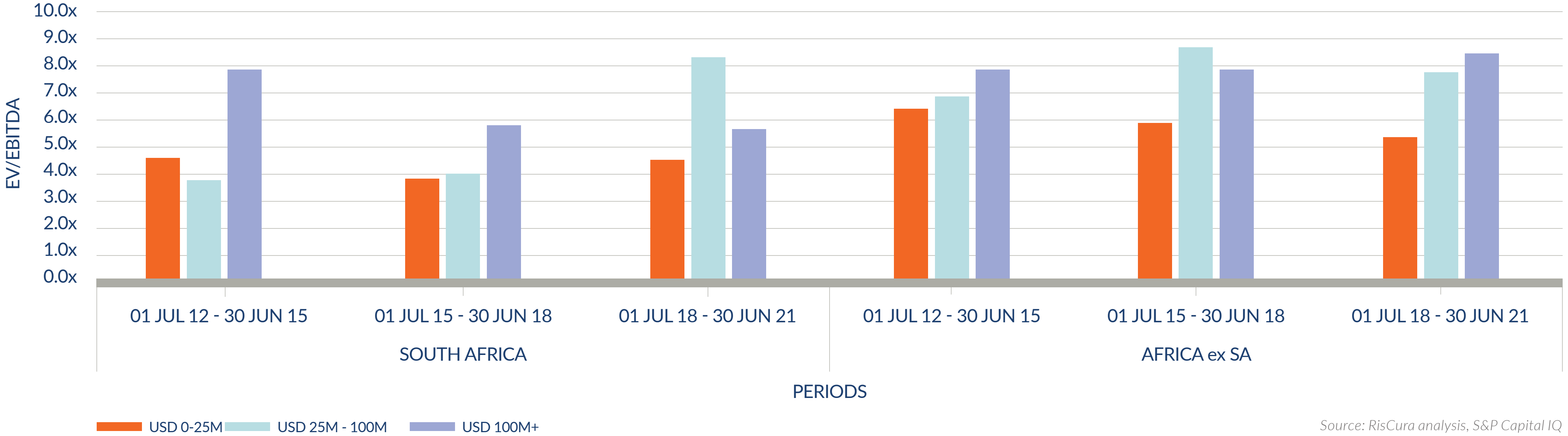
COUNT OF EV/EBITDA MUTLIPLES BY PRICE CATEGORIES



Source: RisCura analysis, S&P Capital IQ

Transaction multiples relative to their size

MEDIAN EV/EBITDA MULTIPLES OF PRIVATE EQUITY TRANSACTIONS



Source: RisCura analysis, S&P Capital IQ

Quantitatively it is notable that most transactions in South Africa are occurring in the under USD25 m price range, followed by the USD25 m – USD100 m price range. Africa ex SA still has considerable transactions within the USD100 m – USD250 m price range. This indicates that larger trades are being executed beyond South Africa's borders.

6.4 By sector

Historically, the range of EV/EBITDA multiples across sectors and company sizes were relatively small. Our latest data indicates that IT and the consumer discretionary sector remain with the highest investment activity. However, the quantum has increased significantly.

Between 2010 and 2015, the highest median EV/EBITDA multiples throughout the Africa ex SA region were seen in consumer staples (6.66x), financials (7.14x), and the consumer discretionary (7.22x) sectors. These promise high growth due to African demographics. Accordingly, they also accounted for the highest number of transactions over the same period. Financial multiples have taken the lead in recent periods.

The median multiple within the IT sector for Africa ex SA of 8.53 slightly exceeded the full period (2006 – 2021) median of 7.2x, following highs reached between 2016 and 2018 at 9.5x. The increased interest in, and maturing of, the sector over the same period most likely drove the growth. Similar trends are observed in the South African market, with highs of 11.1x between 2016 and 2018, and 6.3x in the more recent periods.

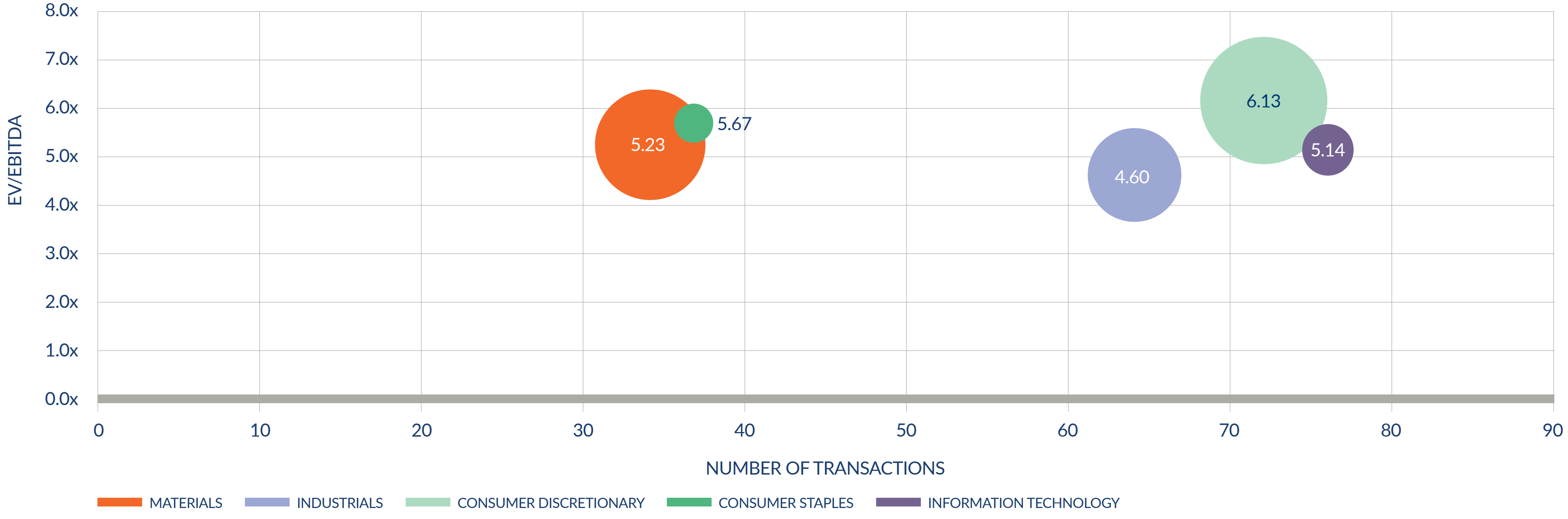
The financial sector has seen an uptick within both Africa ex SA and South Africa, with transaction numbers and multiples in Africa ex SA and South Africa being 46% and 19% higher, respectively. This is possibly a result of the higher growth prospects within the financial sector across the broader African spectrum.

Previously, the largest value transactions fell within the communications sector. However, energy took the lead of highest spend in Africa ex SA in recent periods. This speaks to the increased activity in this sector and significant investment commitments required, notably in western Africa.

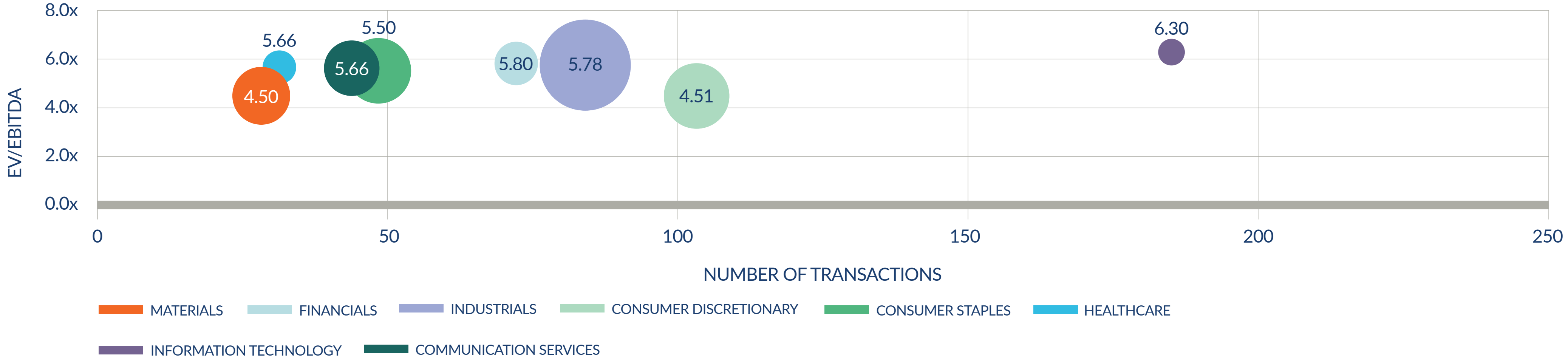
While our data does not show much activity in the communication sector in South Africa between 2010 and 2015, the communication service's multiple increased 54% versus the prior three-year period. Most deals in this sector were focused on interactive media services and wireless telecommunication services companies.

SOUTH AFRICA

(2010–2015)



(2016–2021)

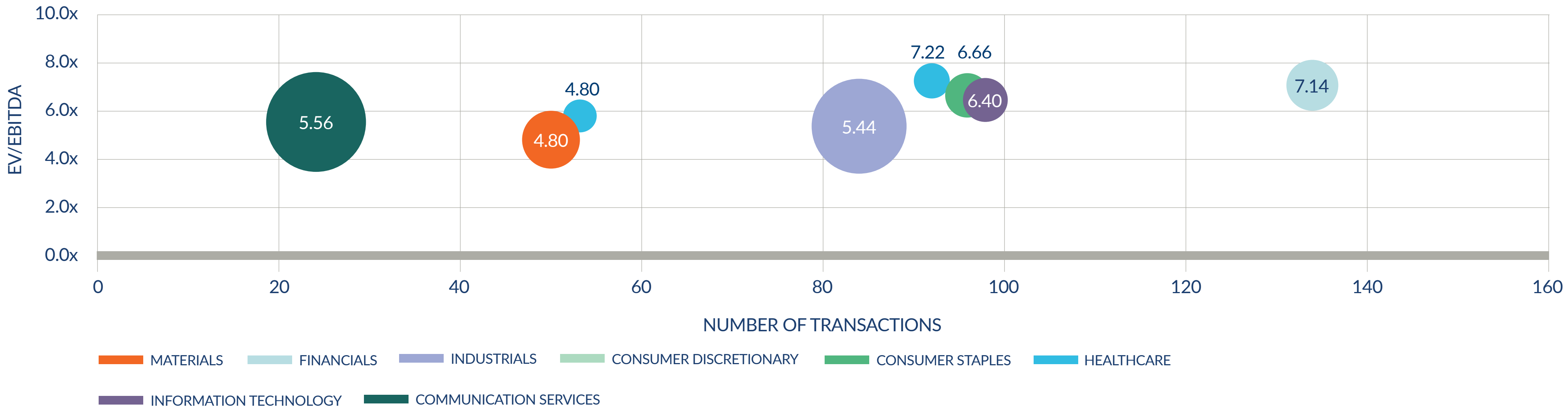


Bubble size – average EV transaction size (USD m)

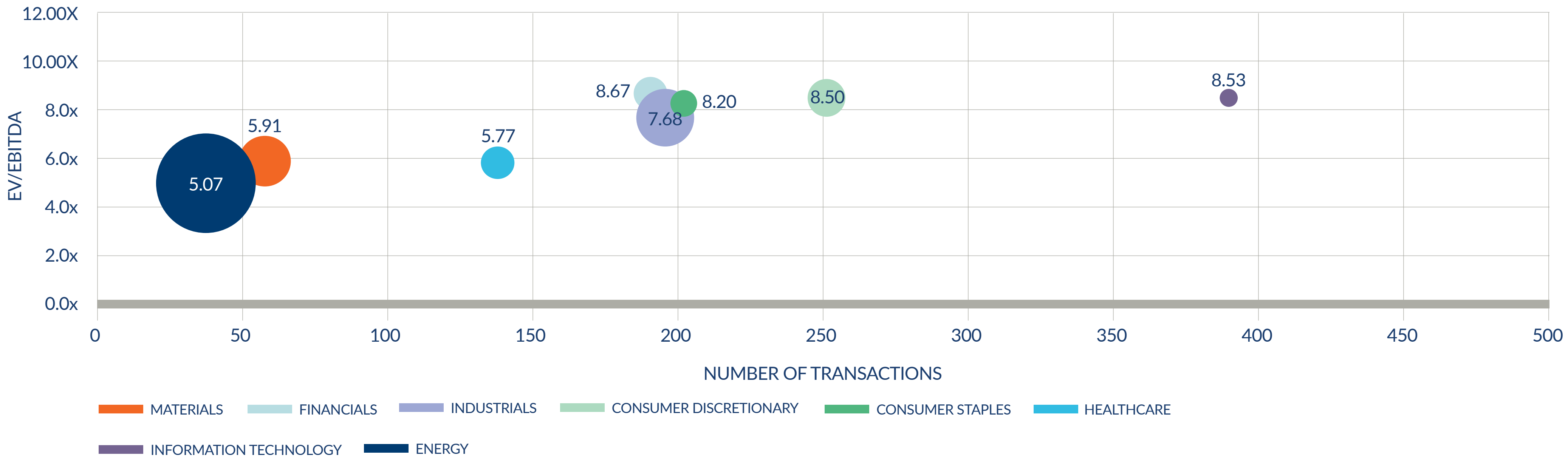
Source: RisCura Analysis, Capital IQ. Only includes aggregate data with sufficient observations to be meaningful.

AFRICA EX SA

(2010–2015)



(2016–2021)



Bubble size – average EV transaction size (USD m)

Source: RisCura Analysis, Capital IQ. Only includes aggregate data with sufficient observations to be meaningful.

Conclusion

When looking at the prices being asked for PE assets in South Africa and Africa, and the landscape that influences those, we can see market fundamentals reflected.

Muted asset prices directly reflect South Africa's poor growth outlook, an increased risk profile, and the lingering impact of the pandemic. While somewhat rebounded, the average EV/EBITDA multiple paid for a private equity asset is still among the lowest it has been since we started gathering data more than 10 years ago. However, the asset class has a proven track record of outperformance in periods of weak economic growth and market volatility. Combined with current low prices, this may indicate that funds currently deploying capital will return good performance relative to other asset classes.

When looking at the prices of African private equity assets excluding South Africa, it can be difficult to understand price movements purely from the cost of equities calculated using CAPM and growth forecasts. To correctly interpret this, you need to understand African capital markets and CAPM well. CAPM relies heavily on several underlying assumptions, which are stretched to breaking point when looking at African capital markets, especially the private equity market. The most relevant are assumptions such as frictionless trading between asset classes, which stands in stark contrast to illiquid capital markets, the fund commitment model, and restriction on the free movement of capital.

Despite erratic fundraising and mixed risk and growth outlooks, market trends in African private equity have remained constant. Despite PE prices dipping below those of listed companies, deal activity is growing significantly. In 2021, notwithstanding the dramatic drop in funding, and the change of risk and growth outlook, our data shows that deal activity had reached new highs (albeit at lower transaction values). Multiples pricing have remained stable, with only a slight decrease in prices observed. The pricing level is, however, well below that of the listed market, which has done well in the current year, returning the relationship between listed and unlisted prices to more conventional levels.

It appears that the significant amount of committed capital has had a stabilising effect on pricing, which survived short-term changes in funding levels and risk profile. However, the committed capital model can only delay the efficiency of markets. Prolonged decreases in fundraising and risk outlook are filtering through to pricing. The sharp decrease experienced in fundraising is expected to gradually recover following the pandemic and the resultant economic slowdown. However, if these trends continue, prices may be less buoyant going forward.

Realising Africa's potential for enormous growth and innovation, given its young population and vast natural resources, will require considerable investment into economic reform, education, healthcare and digital skills development. Africa is still an attractive investment destination, but requires enhanced economic reforms, good governance and a stable political landscape to continue attracting PE fundraising and entrepreneurs. Addressing these factors can play a pivotal role in the development of the continent.

Private Equity in Africa

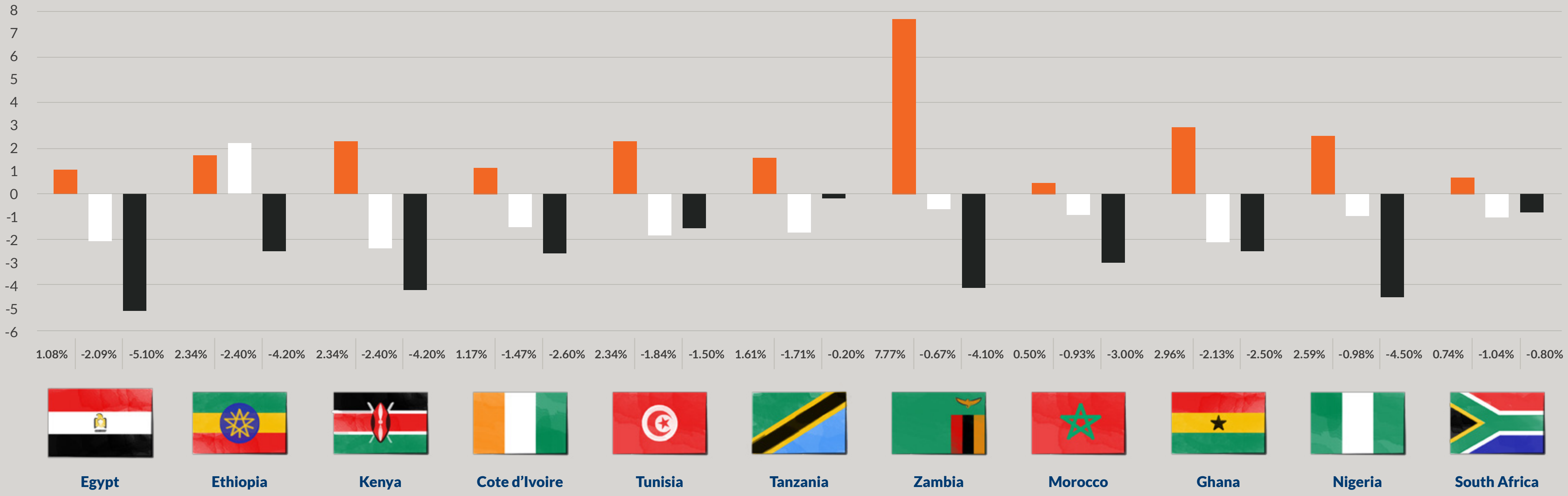
Cost of Equity

Change in COE

Dec19 – Mar20: COE increase is attributable to a universal rise in risk due to the global impact of Covid-19.

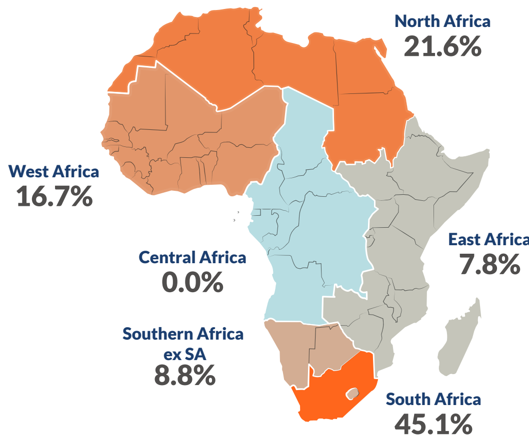
Mar20 – June20: decrease in response to countries loosening monetary policy measures.

June20 – June21: overall decrease following general economic rebound.

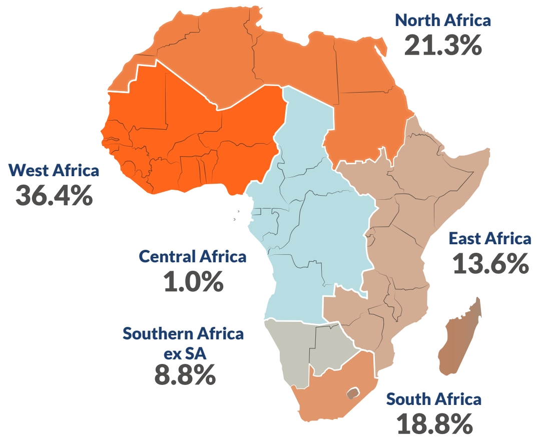


Exits

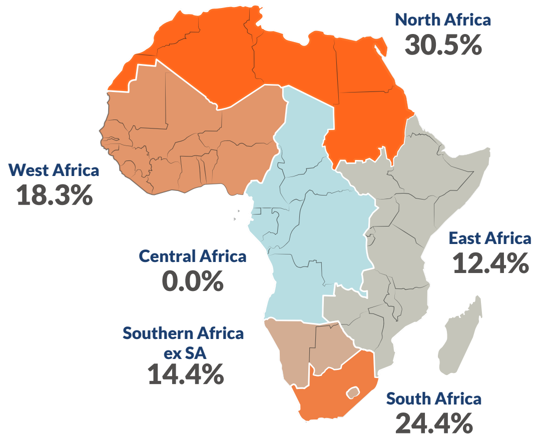
2016 & 2017



2018 & 2019

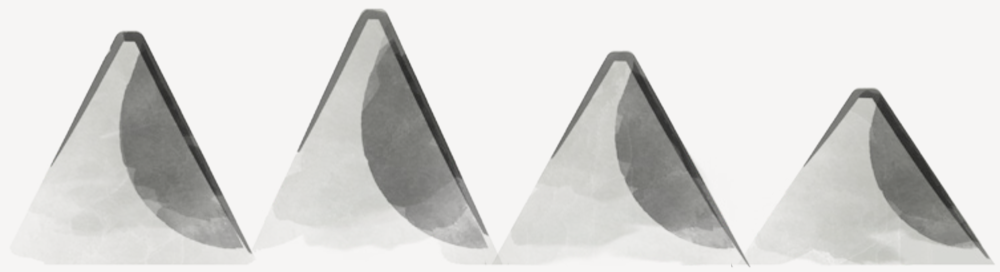


2020 & 2021H1



Dry Powder

Change in levels (USD) from 2018 – 2021 (H1 values inclusive of AVCA interim and final closes)



2018	2019	2020	2021
USD8.37bn	USD9.16bn	USD7.66bn	USD6.34bn

Pricing

Africa ex SA and Africa only deal multiples by sector (median multiple 2016 – 2021)

	Materials	Financials	Industrials	Consumer Discretionary	Consumer Staples	Healthcare	Information Technology
Africa ex SA	5.91	8.67	7.68	8.50	8.20	5.77	8.53
South Africa	4.50	5.80	5.78	4.51	5.50	5.66	6.30