Catalyst

SA's quarterly Private Equity & Venture Capital magazine

Vol 17 No 2
JUNE QUARTER 2020

Maia Capital launches first impact fund

Treasury Loan Guarantee Scheme failure to launch

Foxes circle the Quantum Foods henhouse

FROM THE EDITOR'S DESK

As South Africa's lockdown rumbles along into its fifth month (day 127 at the time of writing), economic surveys; high and low frequency data points; stories of businesses closing – some large, many small; and jobs and incomes lost into the millions (according to the NIDS CRAM study) blur into one frightening picture of an economy obliterated.

And while the COVID scourge provided the fear, it has been government's handling of the lockdown regulations that have provided the loathing. From ignoring the experts' advice on leaving schools open to allow parents to head back to work and the task of reopening the economy (and for students to continue receiving meals), to allowing taxis to carry on imperilling the lives of their passengers at 100% (and more) efficiency, and continuing bans on the sale of alcohol and tobacco on questionable science, the anger and breakdown of trust is palpable.

And it couldn't have come at a worse time, apart from the obvious need to rebuild. Government has finally gazetted 50 infrastructure projects that have been through the new SIDS methodology to ensure delivery and execution on time, on budget, and without corruption.

Speaking to Dr Kgosientso Ramokgopa, head of the investment and infrastructure office in the Presidency, about what makes this time different to other failures to launch grand infrastructure-led recovery programmes, there is an honest admission that government has run out of capacity in key areas and funds. The private sector is the only answer. And the only way to build successful public-private partnerships is to build trust.

Any whiff of the sort of corruption that plagued the Zuma administration, and that which is on display relating to the procurement of personal protective equipment, will send private sector partners packing.

Ramokgopa says that, in effect, the process of gazetting these projects means that they will now be fast-tracked in terms of the Infrastructure Amendment Act and all regulatory approvals, be they water use licenses or EIAs, must be resolved within 57 days of being gazetted.

This is encouraging talk. But we've heard lots of talking up to now. Capital providers in the private equity sector and elsewhere will want to see demonstrable commitment to action now, and a swift and comprehensive response to the spate of corruption that has surfaced around government's COVID relief response, to start repairing the broken bridge of trust. ◆

Michael Avery

Contents

Catalyst

Editor: Michael Avery

Sub-editor: Lee Robinson

Design & Layout: Janine Harms, Gleason Design Studio

Catalyst is published by the proprietor Gleason Publications (Pty) Ltd, reg no: 1996/010505/07 from its offices at 30 Tudor Park, 61 Hillcrest Avenue Blairgowrie, Randburg 2194.

Tel: +27 (0)11 886 6446

Gleason Publications

Goddess of growth

"I see one-third of a nation ill-housed, ill-clad, ill-nourished." "The test of our progress is not whether we add more to the abundance of those who have much; it is whether we provide enough for those who have too little."

The words, immortalised by US President Franklin Roosevelt during his second inaugural address on January 20th, 1937, find particular resonance in South Africa in 2020, as the country – which entered the global coronavirus pandemic on the back of two recessions in as many years – looks to find inspiration for an economic recovery with its own New Deal.

A pair of economic recovery plans during the month of July, the Economic Transformation Committee of the ANC's *Reconstruction, Growth and Transformation: Building a New, Inclusive Economy,* and Business for South Africa's *A New Inclusive Economic Future for South Africa: Delivering an Accelerated Economic Recovery Strategy*, intersect with the Treasury Paper on economic reform, *Towards an Economic Strategy for South Africa*, updated last year, and the NDP, on the issue of infrastructure to catalyse growth.

John Oliphant

"We need to deal with the trust deficit between government and business. If we all believe that we have a vested interest in making the country work, only partnership between government and the private sector will take us out of the current crisis." – John Oliphant

Where they might diverge slightly is on the funding, but already, the building blocks – in the form of the mobilisation of vehicles through which capital can flow into these projects – are being put into place.

And one such building block was announced in June, with the formation of Maia Capital Partners and the launch of a maiden R3bn impact investing fund – the Maia Debt Impact Fund I – as one of the post-COVID-19 economy reset measures to build an inclusive and resilient economy.

The name is inspired by Maia, one of the seven Pleiades and the Goddess of growth.

The Fund is a partnership between Thirdway Investment Partners, the Black-owned infrastructure investor and asset manager, founded by former head of the largest pension fund on the African continent, SA's GEPF, John Oliphant, and Mutle Mogase (Chairman) and Dinao Lerutla (co-founder and managing partner), of Maia capital.

Speaking at the Thirdway Leadership Dialogue webinar to mark the launch of the Maia Debt Impact Fund, former Deputy Finance Minister, Mcebisi Jonas, said there was no shortage of money in South Africa; what we have is a shortage of leadership.

"In times of crisis, we often say that there are also opportunities," says Oliphant. "From a

Third Way perspective, even though the former Deputy Minister of Finance said there is not really a shortage of capital, what I think our problem has been [is] an allocation of capital that is not really optimal and not geared for our type of economy."

"Maia Capital is the evolution of this view that we have sufficient local savings, in the form of our pension funds, to invest in infrastructure, healthcare and other areas. Looking now at what is happening due to COVID-19, we thought that it would be important to invest with Mutle and Dinao in areas of inclusive growth."

Oliphant believes that Jonas' remarks hit the bullseye in that, for the bold infrastructure programme to deliver the spark this economy so desperately needs, it will require bold leadership from both government and business.

"We need to deal with the trust deficit between government and business. If we all believe that we have a vested interest in making the country work, only partnership between government and the private sector will take us out of the current crisis."

Mogase explains that, due to government's constrained finances, with public debt expected to reach 104% of gross domestic product (GDP) by the end of 2021 as a result of the COVID-19 pandemic, and the failure so far of the Treasury's R200bn Loan Guarantee Scheme to deliver on infrastructure, ambitions will require access to mezzanine debt.

"We are looking at mostly mezzanine instruments," says Mogase, "and mostly because during times like these, businesses need a mixture of debt and equity capital and we will deliver a form of quasi-equity which will enable the businesses to raise a little bit more debt, but doesn't dilute them to the detriment of the shareholders.

"That also helps with the inclusiveness, the fact that it helps avoid shareholder dilution. And that is the reason that we are raising a R3bn fund, because we need to play a role in determining the impact and guiding the investment with the investees.

Mutle Mogase

"We've got elected sectors. We are looking at social infrastructure such as health, social housing, climate, and obviously in businesses themselves. We were discussing this recently as the Maia team, that government put up these guarantees, the R200bn, and it's hardly been used because banks are just not geared to deal with this kind of environment, just by their nature, from a risk point of view. And the need is for quasi-equity as opposed to pure debt."

> "We are quite confident that we have done enough work that we are going to be able to deploy capital into these assets fairly quickly" Dinao Lerutla, co-founder and managing partner, of Maia capital

Dinao Lerutla

Lerutla says that there is already a healthy R1bn pipeline of projects that the team has evaluated and lined up.

"And this is only the beginning for us," says Lerutla. "We are quite confident that we have done enough work that we are going to be able to deploy capital into these assets fairly quickly. We have quite a number of offerings in healthcare, which are assets that will enable us to roll out more affordable healthcare facilities in the areas where the need is greatest. We have a pipeline that also includes investing in education. We need more student beds in the country and one of the areas that affects the quality of education is the lack of student housing, and it's a market that has been opened significantly for private sector investment."

Lerutla adds that the asset manager also sees a number of opportunities in financial inclusion and affordable housing.

She explains that this is where the team believe that true economic reform and empowerment will stem from.

"If you look at load-shedding in the townships, like Soweto, for a week at a time during a time where we are supposed to be learning online as schools are only partly reopening, you can imagine the impact on that kind of society. These are the things that are exacerbating inequality."

Lerutla admits that, "it's not an easy landscape", but is quick to add that, "because we've seen quite a number of successful models on the ground that can be scaled", Maia is up to the challenge.

What makes the Maia approach unique is also the fact that the asset manager is not only looking at single assets, but also where it can invest into a portfolio of assets in order to ensure there is sufficient capacity to oversee the investments, while at the same time being able to deploy capital.

"Our sweet spot would be between R100m and R300m for an investment cheque size," adds Lerutla.

The expected IRR is CPI plus 8%, which is typical given the type of product, ranking slightly less than senior debt.

What gives Oliphant confidence that the time is ripe for such a fund?

"Government recently hosted the Sustainable Infrastructure Summit and, by their own admission, they feel that it's important to replicate a model similar to the REIPPP (Renewable Energy Independent Power Producer Programme). Government believes that model will work in other areas of infrastructure. And government is also working hard on generating a pipeline of projects that are bankable."

But Oliphant hastens to add that he's hoping, from the government's perspective, that the Summit was not the measure of success.

"I was just talking to the CEO of the Development Bank of Southern Africa [DBSA], Patrick Dlamini, and he was saying that it's critical, now more than ever, to partner with the private sector and [DBSA], being the custodian of this blended capital injection that's coming from government. He said they have actually accelerated it internally to build capacity so that they are able to engage with partners in the form of pension funds and so on. I get that there is a sense of urgency and everyone is pushing in the right direction. As long as we measure success on actual investments and not on summits; politicians like measuring success by the number of people who have attended their conferences. We want to see the projects coming to the market. Overall, it's exciting."

At the time of going to print, 50 projects that were promised to be gazetted within a week of the Sustainable Infrastructure Development Symposium on June 23rd, had just been gazetted.

Trust starts by sticking to your promises. ◆

Loan Guarantee Scheme Failure to Launch

As we pick through the detritus in the wake of the COVID-19 social and economic wreckage, it's increasingly clear that the theoretical relief offered by government was far removed from the practical realities of so many small business owners in South Africa.

The number of companies announcing plans to retrench staff is growing. From aviation to construction, from entertainment and leisure to hospitality, companies have indicated their intention to retrench staff because of heavy losses incurred over the past four months. In other cases, businesses are closing permanently.

National Treasury's R200bn Loan Guarantee Scheme is a crucial centrepiece of "phase two" of the economic response to the COVID-19 crisis, and is now a few months old. Take-up, however, has been far too low.

We find ourselves in a situation where we ask ourselves why it didn't work; why didn't we see substantial take-up?

"Part of the reason that is believed to be one of the stumbling blocks is that it was fairly slow to market," says Annabel Bishop, Investec Chief Economist. "And some of the criteria as well; the businesses have to have no existing capacity to borrow and need to be in severe financial distress and if you look at the rules around it, individuals could be held personally liable extending over a substantial period."

"From an economists' perspective, it seems to me that the terms were not attractive enough or indeed quick enough (the scheme was rolled out seven weeks after lockdown started)."

Karl Westvig, CEO of Retail Capital, an alternative lender, has been a vocal critic of the scheme.

"We looked at the scheme in detail. First, the principle was reasonable, in that the banks carry some of the risk and Treasury guarantee 94% of the risk, but to access the guarantee, the banks had to prove that they applied reasonable criteria before they could claim that loss back from Treasury and, as a result, banks haven't changed their criteria. Banks have traditionally always funded larger businesses, not small businesses. They've never been great funders of small SMEs. And the R300m cap is a pretty large business. Most of our members are doing R10 to R20m turnover, not R300m turnover.

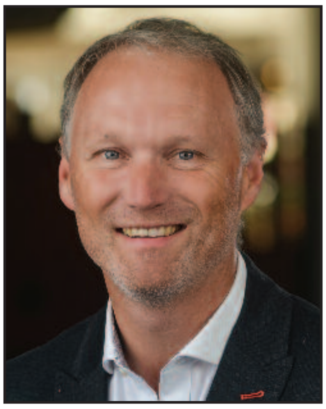
Annabel Bishop

"Part of the reason that is believed to be one of the stumbling blocks is that it was fairly slow to market," says Annabel Bishop, Investec Chief Economist.

The scheme is aimed more at larger businesses."

Westvig believes that a key flaw in the design was its utilisation of traditional credit risk criteria, which is asset-based and surety-based, not based on whether a business is likely to trade.

"The intention was to help businesses that were in distress, but banks' criteria is not to lend to distressed businesses," says Westvig. "Banks' criteria is to lend to solvent businesses with good prospects. How many business owners right now can say, hand on heart, that their business is safe? We are all living in uncertain times. And, as a result, they are saying to business owners that you must now sign surety and put up collateral on a traditional facility which is meant to be for relief when you are not sure whether the business will survive, given the nature of lockdown and restrictions."



Karl Westvig

Westvig believes that a key flaw in the design was it's utilisation of traditional credit risk criteria, which is asset based and surety based not based on whether a business is likely to trade.

Samantha Pokroy, founding principal of private equity firm, Sanari Capital, and SAVCA board member, has helped the private equity and venture capital industry body to draft a response to the scheme, and believes it is critically important that amendments are made so that much needed capital can start to flow to those businesses that need it most.

"I have a portfolio of six businesses, and none have been able to take it up and all would benefit from it," says Pokroy. "We have about two-thirds that would benefit from an actual relief situation, so although they are not in distress as yet, the facilities would be put in place to ensure that they can continue to trade confidently without having to introduce cost saving initiatives that would, for example, result in pay cuts or job losses, knowing that there is a back-up plan. I think that only one will actually need the facility, but it is important to know you have it there in case the downturn is more extended, protracted and severe than we are currently seeing."

Pokroy believes that the risk of second round effects on the economy, due to the lockdown, makes the scheme vital. Companies in the technology and the education space, business services and supplies, will face the second wave as the impact on the economy comes through and this is why it is so critical to get this programme fine-tuned and working properly.

"And then there are the rest of our companies who would benefit from stimulus in the system that triggers confidence in being able to invest in growth and focus on exports which will ultimately help the economy to recover."

Pokroy adds that the lenders and lending criteria are far too risk-averse to be effective in saving businesses and saving jobs in this COVID-19 induced economic crisis. SAVCA surveyed its members and found that although 43% of the portfolio companies with revenues less than R300 million were in need of the COVID-19 loan facility to ensure their ongoing viability and recovery, only 28% of those that applied for funding were granted and drew down on a facility – and many did not apply at all, given the eligibility criteria.

"For the remaining 72% of companies that required funding, but have not yet been granted these facilities, the top reasons provided included the company not being profitable prior to COVID-19 due to a growth strategy, or not meeting the personal suretyship requirements for directors and shareholders."

Although banks have extensive distribution, their inflexible credit models and conservative lending culture mean they may not be best suited to the task at hand. This has been compounded by requirements of the Reserve Bank, in which the Guarantee Scheme backing can be pulled where credit processes have not been followed by the banks in their ordinary course.

Pokroy states that "in our experience, there has been no difference between a normal loan and a COVID-19 government guaranteed loan, which defeats the object entirely. The argument for personal surety in credit application processes is to test for alignment and commitment of owner managers. The philosophy is that owner management will know better than a bank what the prospects are for their business and whether the loan can be repaid. But in these extremely uncertain times, this argument holds less water. Owner managers are unable to anticipate the market conditions any better than the rest of us, and therefore it does not provide the type of reassurance it may have under other conditions."

"In fact, it requires individuals to decide between the risk of losing their homes and trying to keep their businesses open and staff employed. They would have to make this unenviable trade-off based on conditions that are completely out of their control."

Pokroy believes that the risk of second round effects on the economy, due to the lockdown, makes the scheme vital.

Samantha Pokroy

"Rather, the purpose of the Guarantee Scheme should be to underwrite this risk with the full knowledge of the likely costs arising from the fact that, notwithstanding best efforts by all parties, not every business will survive and not every loan will be recoverable. But jobs will be saved, families will be provided for, consumer and business expenditure will continue, and most businesses will survive and be critical role-players in the recovery of our economy", says Pokroy.

When it comes to solutions, Westvig believes that the banks are just operating as they are intended to, to protect depositor funds. And it's a traditional model that has legacy costs.

"From an access perspective, it tends to be quite expensive as they have branch infrastructure, they have large overheads, large levels of compliance."

But Karl says that Retail Capital has submitted a proposal to Treasury which is being discussed at the moment, where he believes the existing rails are good enough.

"We can access between 350 and 400,000 businesses just with our own networks," says Westvig. "So, it's easy to distribute capital. We can see trading history on who's trading and, on the back of that, we can make risk assessment decisions fairly quickly. Within days and weeks, you can distribute large amounts of funding to the right businesses. We saw this happen in the early stages with the Rupert scheme, managed by Business Partners. They were many times oversubscribed and distributed fairly quickly.

"The challenge is that every time we make proposals, it goes back to the Banking Association and the banks are making decisions on it, not Treasury. And the challenge we have is that the R200bn that has been earmarked, has been earmarked for the banking system, so they either have to force us into the banking structure and try and control how we distribute funding, or they have to create a separate allocation and I think that's probably a better way to go for National Treasury."

SAVCA recommends the following amendments to the loan guarantee scheme:

1. Dedicate a minimum amount of loan funding deployment under the guarantee scheme for companies with turnover less than R300 million and implement targets and incentives for bank deployment;
2. Include growth companies that are not yet profitable in the scheme;
3. Remove the requirement for personal suretyships/guarantees; and
4. Consider alternative lending channels and blended finance options, which may include first loss funding for private equity funding in businesses with turnover less than R300 million.

In its latest update on the various initiatives run through the banks to provide customers with relief through this period, the Banking Association of South Africa (Basa) said that R10,6bn in loans has been provided to just under 7,500 businesses.

At the time of writing, Treasury announced sweeping changes to the Scheme including:

- Business restart loans will now be available, to assist businesses that are able to begin operating as the economy opens up.
- Clients can now access the loan over a longer period. The draw down period has been extended from three months to a maximum of six months. For example, a R6m loan can be drawn down over six months, at R1m a month if the business qualifies. The size of the loan is still calculated on operating expenses.
- The interest and capital repayment holiday has been extended from three months to a maximum of six months after the final draw down. For example, in the case of the same R6m loan, drawn down at R1m a month for six months, repayments will only be required from month 13.
- The turnover cap has been replaced with a maximum loan amount of R100m. Banks may also provide syndicated loans for loans larger than R50m.
- The test for good standing has been made easier. This has now moved back to 31 December 2019 from 29 February 2020, which will accommodate firms which were already experiencing cash-flow problems in February.
- Sole proprietorships are now explicitly included. For sole proprietorships and small companies, salary-like payments to the owners (drawings) are included in the use of proceeds. Security, suretyships or guarantees are not explicitly required. Eligible businesses should contact their primary or main banker for further information on the scheme and the qualifying criteria.
- Bank credit assessments and loan approvals will be more discretionary and less restrictive, in line with the objectives of the scheme.

Banks may use their discretion on financial information required, for example bank or financial statements, where audited statements are not available. Suretyships or guarantees may also be required. The provisions of the National Credit Act and Financial Intelligence Centre Act remain applicable.

- No security, suretyships or guarantees are explicitly required in terms of the scheme. Banks may require this in terms of their individual credit risk management practices.
- Banks can consider re-applications from clients declined under Phase 1.
- Loans under the Scheme and other loans will not trigger cross default clauses and vice versa.

Commenting on the announcement, Stuart Theobald, Chairman of Intellidex, the firm that first proposed a similar scheme to Treasury before it was announced, said it was a major improvement. However, the loss sharing arrangements still remain rather vague. And ultimately, much still hinges on whether the banks embrace the space afforded to them by the changes, to relax their lending criteria and open the taps.

South Africa needs the funds to flow urgently. ◆

Reg 28: "This time is different"

Q&A with Linda Mateza, CEO and Principal Officer of the Eskom Pension and Provident Fund (EPPF)

With issues around market volatility, and investing in private equity and prescribed assets keeping pension fund trustees busy this year, Catalyst caught up with Linda Mateza, CEO and Principal Officer of the Eskom Pension and Provident Fund (EPPF).

Mateza has pensions in her blood, having started out with the Transnet Pension Fund in 2002 and subsequently working in the private sector at Standard Bank and Momentum. She then moved to the EPPF for a while in 2008 before joining the Government Employees Pension Fund as Head of Investments and Actuarial Services from 2015 to July 2019. She now returns to the EPPF Fund as the CEO and Principal Officer.

Mateza holds a Master's degree in Finance and Investments from the University of the Witwatersrand, and is a Fellow of the Africa Leadership Initiative. She serves on the Board of Directors of Batseta, the Council of retirement funds in South Africa.

Q: Did you always have a career in finance and investments as a childhood ambition?

A: In fact, I wanted to become a psychologist and my first degree, which I studied at Rhodes University, was Psychology and Anthropology. I happened to pick up economics as one of my electives and found that I was enjoying it a lot more, and I happened to be quite good at it. That really sparked my interest in finance and economics.

Q: The Eskom Pension and Provident Fund is a giant in the institutional investment space – SA's second-largest retirement

fund after the Government Employees Pension Fund (GEPF); what are your assets under management (AUM) and membership?

A: The EPPF has around 80,000 members, split evenly between active members who are currently employed by Eskom, and pensioners of Eskom. The AUM are around R144bn. At the peak, around mid-February, we reached R150bn and around the 23rd of March, we were down to R114bn, so we have managed to bounce back quite well.

Q: You have recently been appointed the new CE and Principal Officer of EPPF. What are your key priorities and strategies going forward, to ensure the fund achieves its goals and executes its mandates?

A: I worked for EPPF previously. I joined in September of 2008, just at the start of the global financial crisis, so I seem to have a knack for these global financial disasters.

I'm focusing on preserving value for members. I think at times like these, growing the assets is a very difficult task but, at the very least, what we should do is preserve value for them; to go beyond just treating members as numbers and actually taking an interest in their lives and being concerned about their wellbeing.

Q: The "hybrid" financial structure of the Fund, where the Fund has a Defined Benefit structure with a Defined Contribution financial underpin, remains a major risk over the long term, and measures to address this situation are still being sought by all stakeholders. How are you dealing with that long-term risk?

A: Yes, the fund is a defined benefit, but it is not guaranteed. The way we've approached this is that our investment strategy is premised on meeting the liabilities of the fund as they fall due into the future. Every year, we conduct an asset liability modelling exercise where the actuaries who consult to the fund project the liabilities well into the future. I'm talking about a 50-70 year horizon. We would then come up with a set of capital market assumptions with their assistance, and independent reviews as well, and from that process determine the optimal strategic asset allocation that would best enable the fund to meet those liabilities over the very long term. So we invest in a liability-driven manner because we are very cognisant of the fact that, should the fund become underfunded, we are not guaranteed to be bailed out.

Q: The Eskom Fund is a known supporter of private equity. One can count on two hands the number of pension funds that invest in the asset class. With respect, it's poor.

A: And many of them use the excuse of liquidity which, with due respect, is not correct. If you're only investing 5% into private equity, which is your prudential limit, you can manage liquidity through the rest of your portfolio very easily.

I think there is reluctance from trustees to take the trouble to learn about the asset class and a concern that, if they get it wrong, they may face certain legal liability issues, if they are seen to perhaps have been negligent. That is another tough nut to crack. The more capital you've got to invest, the more fund managers can put capital to work, the more growth you can get out.

Q: How do you see your role in deepening the pool of capital that flows to private equity and emerging PE general partners?

A: The EPPF has been investing in private equity for many years, and I think it's a daunting space for pension fund trustees because it's not as transparent as listed securities. It is also quite complex in the way the valuations work, and when it goes wrong, it can go spectacularly wrong; you could lose everything. So from a trustees point of view, bearing in mind their fiduciary duty, it's a lot safer to stick with the known and tried asset classes. However, there is such a disjuncture between what is listed and the real economy of South Africa. If we are investing with the purpose of rebuilding the economy, the way to do it is to go directly through the financing of local enterprises, especially in the small and medium sector, as well as financing development opportunities that obviously will earn a return over the long term.

Q: There is a lot of convergence between the economic documents on the table of the ANC, Business 4 SA and Treasury around using infrastructure as a catalyst for growth. Where they diverge appears to be on funding this, and there is talk of using section 28 of the Pension Fund Act to prescribe to pension funds to increase investments into "real assets" and fund infrastructure and capital projects. It didn't work during Apartheid, why will this time be any different?

A: This time is different because the government [during apartheid] was desperate for funding, due to sanctions. Now we have an open economy. However, having said that, the pensions community in general has been quite sceptical about the intentions behind these conversations around regulation 28. I think what's likely to happen, from my engagements in the industry and with government representatives, is that regulation 28 will be amended to include a minimum threshold that must be invested in infrastructure. It wouldn't go as far as prescribing actual investments that should be made and, as such, I don't think it's bad thing. It's a nudge in the right direction. It forces us, as retirement funds, to consider infrastructure as a potential investment.

I must add that it all depends on the quality of available investment opportunities. If the pipeline is not strong, if there aren't compelling investment opportunities in infrastructure, then I understand the reservations of those in the pensions industry who say that prescription would be a very bad thing.

Linda Mateza

My view, and that of the EPPF, is that the country is in dire need of infrastructure, and with blended financing between government, the DFIs (Development Finance Institutions), the financial institutions and ourselves as institutional investors, we can really make a difference. The current crisis right now shows us the effect of under-investment in infrastructure – hospitals are bursting at the seams, water and sanitation is hard to come by in many regions around South Africa, and that's a result of having not invested enough when times were 'normal', and now we are living in very extraordinary times.

And so if, in partnership with the government, viable investment opportunities are created, I, in principle, wouldn't have a problem with there being a minimum prescribed to us as pension funds to say, "invest in infrastructure and grow the economy". Growing the economy also means growing the rest of our portfolio. We invest in listed companies and if the economy is weak and people are unemployed, and infrastructure is poor, that limits the prospects of the listed companies doing well and therefore it's only to our own detriment as investors. In the interest of diversifying, as well, it makes sense to invest in the real economy.

Q: Where do you think the capacity constraints exist to help unlock some of these projects?

A: Structuring the projects is quite a skill and, at times, we may not have the capacity in the public sector to do that, and so it's important that the private sector is also involved so that the structures make sense.

Q: What keeps you awake at night?

A: What keeps me awake at night is the prospects for young people in the country, given what the lockdown has exposed in our education system. I and my peers are in the fortunate position of having computers and Wi-Fi at home, so our children can continue to learn. However, that's something that's not available to the vast majority of people in our country. I worry that the inequalities will deepen and that youth unemployment, which was already a problem before the crisis, will be exacerbated. The things that keep me up at night are many. Another is being able to generate return for our pension fund members, to be able to retire with dignity. We target an investment return of CPI plus 4.5%. We are not likely to see that this year or next, and we certainly didn't see it last year either. There are some real concerns right now and it all comes back to values as South Africans. We used to talk a lot about Ubuntu, which is a sense of community and recognising and supporting each other, and I think if we learn nothing from this crisis, we should at least learn the value of community. ◆

Foxes circle the Quantum Foods henhouse

Not since the heated and acrimonious battle for control of poultry counter Sovereign Foods in 2016 and 2017 have I witnessed such a battle for control of another small food and agricultural counter as has latterly been seen in the frenzy to acquire a stake in small Wellington-based Quantum Foods.

Anthony Clark

Unbundled from Pioneer Foods in October 2014 into a separate JSE listing, Quantum Foods was the highly cyclical agricultural division housed within Pioneer Foods with interest in poultry, animal feeds and eggs. Brands such as Tydstroom Chicken and Nu Laid eggs were well-known.

As a stand-alone entity, Quantum management, under the leadership of CEO Hennie Lourens, embarked on a highly successful programme to de-risk the business to remove much of the latent earnings volatility.

The poultry abattoir business was sold to Sovereign Foods and Quantum decided to utilise its skills as farmers to focus on day-old chicks and broiler rearing as contract farmers. Contracts were landed with poultry leader Astral Foods, as well as Sovereign Foods.

The sale of the poultry unit removed a significant portion of volatility from Quantum, as its regional brand could not compete against the majors and it didn't have economy of scale. Today, as a contract broiler farmer, some 40% of earnings are derived from this function and the unit has remained highly profitable, compared to the violent swings seen from its prior poultry meat incarnation.


Clark

Another 30% of Quantum's earnings are derived from its specialist Nova animal feeds business, with niches in poultry feed, dairy and equine feeds, predominantly in the coastal regions.

The only remaining volatile part of Quantum was its national eggs business under the well-known Nu Laid brand, where the company is the only nationwide eggs supplier. It is this remaining 30% of revenue that remains cyclical, tied to the vagaries of input costs and egg supply and demand. Much has been done to reduce the volatility and the huge losses that the business used to generate in down cycles.

It is this very restructuring and positioning of Quantum, tied to its very low JSE PE rating and high Net Asset Value, that drew out the significant interest in the stock that recently emerged.

Long-standing Quantum Foods shareholder, Zeder Investments, owned a 31% stake and was the largest individual shareholder. Zeder gained its Quantum stake from its vast shareholding in Pioneer Foods at the time of the 2014 unbundling. It was always a steady supporter of the stock.

Suddenly, out of the blue and unbeknownst to Quantum management, they sold the 31% stake to unlisted poultry stock, Country Bird Holdings (CBH), on June 12th for 500 cents a share.

Given that Quantum had been trading on the JSE at around 375 cents per share in the days preceding the sudden sale, Zeder gained a healthy premium and walked away with R308 million.

This story gets interesting as CBH, as the Quantum buyer, was also the same party behind the unsuccessful bid for Sovereign foods in 2016/17 which eventually fell to private equity player, CapitalWorks. CBH walked away with a healthy profit.

Questions were raised, as CBH was a rival poultry company to Astral Foods and Sovereign Foods, which has material contracts with Quantum. There were questions as to whether the culture and strategy of CBH and Quantum were compatible. That answer was swiftly answered when Quantum management came out stating that they had acquired a R20m stake in Quantum to bolster their defences against the advances of CBH, paying 650 cents a share.

From a share price of 375 cents in early June 2020, Quantum started to run, and run hard. Other parties were disclosed as having an interest in Quantum and Luxembourg-based agricultural private equity fund, Silverlands, acquired a 32% stake, paying 600 cents a share.

As the Quantum share price reacted to multiple suitors, the share price in mid-July peaked at 1157 cents, some 235% higher than the pre-Zeder stake sale , and in another twist, poultry giant Astral Foods disclosed a surprise 6.42% stake. Astral seemed intent on protecting its supply agreements with Quantum.

So, as it stands, there are seemingly two distinct camps. The original suitor, CBH with 31%, who sits on a healthy paper profit for two months' endeavours of R150 million, and an alignment of Silverlands (32%) Astral Foods (6.42%) and Quantum Management (8%) who are opposed to a CBH deal.

As I write this article for Catalyst, Quantum Foods is trading at 750 cents a share as the extreme trading frenzy and volumes have died down. We could say that we are at an impasse.

Two competing sides, both with sizable stakes. It's a game of chicken. Who will blink first?

Whispers suggest the private equity/Astral/management grouping has attained a 51% stake in Quantum. At time of copy, this has not been confirmed.

If correct, CBH will find it difficult to proceed with any intended offer to minorities. Perhaps history will repeat itself? As CBH was unsuccessful with its original Sovereign bid, it sold its stock to the private equity party for a profit. Maybe they will walk away with a much bigger profit this time?

Many foxes raided the Quantum Foods henhouse. Only one will walk away with the prize. The winners have been shareholders who say a R600 million, mostly overlooked agricultural company suddenly thrust into a deal frenzy limelight now has a value of R1.4 billion. The story is not yet over, but the easy money has indeed been made for those that held shares in what are now golden eggs. ◆

Clark is an independent analyst at Smalltalkdaily Research

Local and international news

After experiencing accelerated growth for the last three years, sub-Saharan Africa is expected to go deep into contractionary territory in 2020. Highlights from the SAVCA 2020 Private Equity Industry Survey, however, indicate that the private equity industry remained resilient in the face of weak macroeconomic circumstances during the 2019 calendar year, which bodes well for the industry's ability to navigate the COVID-19 crisis.

This is according to Tanya van Lill, CEO of the Southern African Venture Capital and Private Equity Association (SAVCA), who was speaking at the survey launch. "There's no denying that the first half of 2020 has been a total whirlwind, but this latest survey – albeit based on 2019 data – provides useful insight into industry trends and signals the valuable role that private equity will play in the region's economic recovery."

Notably, van Lill highlights a significant increase in funds under management. "The private equity industry had R184,4bn in funds under management (FUM) at 31 December 2019, up from R171bn in 2018, representing a compound annual growth rate (CAGR) of 9.2% since 1999 when the survey first began.

"This increase in FUM is a positive indicator for the industry, as it should lead to increased investment into the region," she explains, adding that despite Southern Africa's tough economic conditions over the past few years, the industry was still able to raise R21,7bn in 2019 – an impressive 69.5% more than the R12,8bn raised in 2018.

"This strong fundraising activity is indicative of the fortitude exhibited by the private equity industry," van Lill comments, adding that of the funds raised, R7,7bn (35.3%) stemmed from South African sources, with R3,7bn of total funds earmarked specifically for investment in South Africa.

"The cost of investments in 2019 totalled R25.4bn – with the top sectors invested in being infrastructure and energy, followed by telecommunications, retail and real estate. Also interesting to note is that – as a proportion of investments made by cost – over 50% of the investments made were to support portfolio companies with expansion and development."

Highlighting the significant surge in infrastructure investment, from 6.1% in 2018 to 34.7% in 2019, van Lill notes the positive knock-on effects this offers. "Private equity investment in African infrastructure has been an emerging theme over the past decade, with funds from various regions investing actively in infrastructure projects in the energy, transport and ICT sub-categories. ◆

The Section 12J Association of South Africa released a report to Parliament and National Treasury, outlining the results of the inaugural survey of its members which details the impact which the s12J incentive has had on the SA economy.

Dino Zuccollo, chairman of the 12J Association of South Africa says, "The 2020 s12J industry report demonstrates that the incentive has not only managed to create jobs, but it has done so more economically to the fiscus than other government-backed job creation incentives Through s12J, SMMEs are being meaningfully supported at a time when funding for these businesses has all but dried up. In the Association's view, the survey findings make a clear case that the June 2021 s12J sunset clause should be extended until at least 2027."

"In only five years, this tax incentive has grown into a mature and successful incentive. At February 2020, s12J has total assets under management exceeding R9bn, the bulk of which has been invested by SA's high net worth individuals (57% of total investment) for a minimum of five years. This is particularly significant in the wake of the devastation caused by the COVID-19 pandemic, at a time when the majority of high net worth investor capital is being invested offshore."

Of the R9bn raised, an approximate R5.5bn (or 59%) has been invested into more than 360 SMMEs, implying an average investment size of R15m per business. These businesses in turn support an approximate 10,500 jobs across a variety of industries including education, agriculture, renewable energy, hospitality and tourism, student accommodation and many others. ◆

International News

AVCA launches inaugural report on venture capital in Africa

The Venture Capital (VC) landscape in Africa has gradually evolved over the last two decades to become a recognised and definable investment theme, simultaneously attracting international investment to the continent while also encouraging the development of local venture capital firms and home-grown financing solutions. That's the headline finding from the inaugural report on venture capital in Africa released by the African Private Equity and VC Association AVCA.

The growth of PE and VC investment in Africa reflects the changing nature and scope of external flows to the continent, where foreign direct investment (FDI) has come to eclipse official development assistance (ODA).

In 2012, 17 African countries recorded receiving more FDI than ODA, climbing to 26 countries in 2017 as investment activity on the continent continued to rise2. Africa's robust macroeconomic growth, averaging 4.6% between 2000 and 2016, was a crucial driver of the continent's VC industry; creating a positive economic environment that catalysed innovation, entrepreneurship and investment. Although Africa's more recent economic growth has been lower than predicted, Africa's GDP growth was above the world average in 2019 and it remained the world's second fastest growing region. PE and VC funding in Africa has developed progressively, buoyed by this favourable economic outlook, the magnitude of the market, the growing middle-class consumer base and the fact that Africa is home to the world's largest free trade areas. ◆

PRIVATE EQUITY DEALS H1 2020 – ASSET IN SOUTH AFRICA

NATURE	PARTIES	ASSET	ADVISERS	ESTIMATED VALUE	DATE
Investment by	Kalon Venture Partners	in Mobiz	Bowmans	$1m	Apr 1
Investment by	Pegasus (group of 11 investors)	in Ingress Healthcare		R6m	Apr 15
Acquisition by	Sana Partners Fund 1	a majority stake in Brenn-O-Kem		undisclosed	Apr 17
Acquisition by	Pape Fund 3 En Commandite Partnership	a significant stake in the E.O.E.C Group	Bowmans	undisclosed	Apr 30
Disposal by	African Infrastructure Investment Managers a member of Old Mutual Alternative Investments (Old Mutual) to IDEAS Managed Fund (AIIM)	14% stake in Cookhouse and 34% stake in REISA	Cliffe Dekker Hofmeyr	undisclosed	May 5
Acquisition by	Umkhathi Wethu Ventures [UW Ventures] and Allan Gray	a stake in CompariSure		undisclosed	May 18
Acquisition by	Naspers Foundry (Naspers)	Aerobotics		R100m	May 20
Acquisition by	Umkhathi Wethu Ventures [UW Ventures] and Allan Gray	a stake in Peach Payments		undisclosed	May 20
Investment by	Edge Growth	in Syafund		R2,5m	May 21
Acquisition by	South Downs Investment LP (Apollo Global Management) from minority shareholders	Atlantic Leaf Properties	Java Capital; Lazard & Co; Perigeum Capital; Cliffe Dekker Hofmeyr; Gibson, Dunn & Crutcher UK; Bedell Cristin; G&P Legal; Addleshaw Goddard; Questco; BDO (UK)	£152m	May 22
Investment by	Spear Capital	in RunwaySale		R100m	May 25
Investment by	uMunthu Fund (Goodwell Investments), UW Ventures (in partnership with Allan Gray) and MFS Africa	in Inclusivity Solutions [second tranche of Series A}		$1,3m	May 27
Investment by	CNBB Venture Partners	in Wyzetalk		undisclosed	May 27
Investment by	Fledge Capital and SLA Capital	in Oasis Water	Benchmark International	undisclosed	May 29
Acquisition by	RMB Corvest (RMB Holdings)	significant stake in Roos Foods	Cliffe Dekker Hofmeyr	undisclosed	Jun 1
Investment by	Lionpride Agility Fund	in BusyMed		undisclosed	Jun 2
Investment by	Platform Capital	in Merge Tech		$100 000	Jun 7
Acquisition by	ARCH Emerging Market Partners (African Rainbow Capital Investments)	stake in SunExchange		$3m	Jun 9
Investment by	Crossfin Ventures	in TruID		undisclosed	Jun 10
Acquisition by	Futuregrowth Asset Management (Old Mutual)	LifeCheq		undisclosed	Jun 16
Acquisition by	Ikamva Lakusasa and Senatla Capital	26% and 34% respectively of Joe Public United		undisclosed	Jun 18
Acquisition by	HAVAIC	a stake in Mobiz		undisclosed	Jun 19
Acquisition by	ViaMedia	a stake in Paymenow		R4m	Jun 22
Acquisition by	Medu Capital	a 25.1% stake in Weir Minerals South Africa	Rothschild & Co (SA); Bowmans	undisclosed	Jun 26
Disposal by	Legae Peresec to Ancilla Capital and SBSA ITF GUI GENERIS LPLF H4 QHF	24 637 469 African Phoenix Investment shares	Java Capital; Mazars	R9,85m	Jun 29