RisCura - SAVCA South African Private Equity Performance Report

As at 31 December 2015

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Foreword

May 2016

We are pleased to release the December 2015 edition of the RisCura - SAVCA South African Private Equity Performance Report. This report tracks the performance of a representative basket of South African private equity funds and is published quarterly. The purpose of the report is to provide stakeholders in South African private equity with insight into industry returns, and to establish and maintain an authoritative benchmark for the measurement of private equity performance in this market. Since its inception in September 2010, this report has become a vital component in the marketing of the private equity industry. We would like to thank SAVCA members for making their performance data available, and for their commitment to this project.

Rory Ord
Executive: RisCura

Erika van der Merwe
Chief Executive Officer: SAVCA

Market commentary

Reflecting on 2015, South Africa had to steer itself through some tumultuous waters. Economic turmoil peaked in early December with the surprising replacements of ministers of finance, culminating in Pravin Gordhan being called upon to steer the ship once again. This move saw the rand plummet and business confidence reach an all-time low. Gordhan's re-appointment saw the rand regain some lost ground and it has since stabilised to some degree.

2015 also saw commodity prices continue to fall, compounded for South Africa as the mining and agricultural sectors endured severe droughts, labour disputes, power shortages and declining overseas demand. This together with the slowdown in China charts moderate growth for the country in the year ahead. 2016 is also likely to be a difficult year as consumers become increasingly burdened with increases in petrol prices, electricity tariffs, rising interest rates to buffer increasing inflation, and the knock-on effects of these translating into higher food prices. South Africa is not alone: African and many other emerging markets also faced political turmoil, droughts, declining commodity prices, the impacts of China's slowdown and currency volatility.

There are still many positive aspects that need to be focused on and re-affirms South Africa as being fundamentally sound. We are the gateway to the rest of the continent, boast an extremely sophisticated financial sector and our governance and regulatory structures are founded on strong disciplines. The recent Constitutional Court ruling on Nkandla bears strong testament to this foundation, our tax system is extremely efficient, we have favourable entrenched ties with many first world and emerging economies and are a larger provider of FDI into Africa. Electrical power constraints are also set to be a thing of the past, especially as one looks to the many renewable energy projects that are in the pipeline and that have come online.

Whilst the above reflections are predominantly about South Africa, the world-wide private equity industry also had its ups and downs in 2015:

1. According to AVCA's 2015 data, the value of private equity deals in Africa fell by 69% to US$2.5 billion;

2. PitchBook Data 2015 annual private equity report shows that 2015's impacts on developed markets were not as severe. Deal count in US private equity decreased by 8%, with total deal value dropping less than 5%. In Europe private equity deals with a total value of €401 billion were concluded, recording a 20.8% increase over 2014 with investment count largely the same as 2014;

3. As a large number of record setting buyouts were responsible for the large deal value in Europe, with 18 transactions at or exceeding €2.5 billion in size;

Market commentary cont

4. The mega deals of 2006 and 2007 only match these 2015 levels, but the hype of 2015 was not as marked as before; and

5. The decline in deal value in African private equity was notably different, with the decrease in pan African deal value driven entirely by a sharp fall in the number of large deals above U$ 250 million.

It is expected that the performance from here on out in terms of deal volume and deal value for South Africa will not be as grim as the rest of Africa given the exit activity seen in 2015 and the continued mid-market activity, where growth capital and entrepreneur partnering is evident especially for regional expansion.

After five years of strong performance, South Africa's listed market showed a negative return in 2015. All in all, the JSE All Share Index is now roughly where it was two years ago. This has obviously put pressure on valuations which is reflected in these survey results.

If one considers that there has been over 130 private exits in Southern Africa since 2007 it shows that Southern Africa is still very relevant and that private equity's diversification benefits, long term investment horizon accompanied by active engagement with the management of investee companies, does reap rewards. Notably sales to trade buyers, many to South African companies looking to expand their footprint within South Africa and across the region, accounted for a large proportion of these exits. 2015 also saw an increased deal appetite and a steady level of private equity transaction activity across various sectors in both South and Southern Africa.

Fund manager investment and sector choices, strategies and investee company growth plans will be key determinants of future outcomes. Strategic planning and risk management are key in this period of heightened volatility and the complex environment in which we find ourselves.

Wendy Diamond
CFO, Metier Capital Growth Funds

Private equity in South Africa

Private equity is an asset class which differs in nature from most other assets, including listed equity. Typically, private equity fund investments show low correlation to quoted equity markets and are relatively illiquid, particularly in the early years.

Private equity will normally show a drop in net asset value before showing any significant gains. This is often the effect of management fees and start-up costs on the relatively small capital base of a new fund. Private equity funds in South Africa typically follow a commitment and draw-down model, which means that investors commit a certain total of capital at the start of a fund, but are only requested to transfer cash to the private equity manager as investments are identified or costs are incurred. These funds typically return capital during the course of the fund's life as investments are realised.

South African private equity offers institutional investors the opportunity to invest in an asset class which has historically outperformed listed equity over the long term. It does, however, have a different nature from quoted equity and it is crucial that an institutional investor considers the appropriateness of private equity to its particular objectives.

Methodology

Methods of measuring performance

The most widely accepted method for calculating returns of private equity funds is the annualised internal rate of return (IRR) achieved over a period of time. As a sense check to the IRR measure, we also use the Times Money performance measure. This report measures performance in two ways: by 'since inception' and 'end-to-end' (over three, five and ten years). The IRR calculated in this report is net of fees over all periods.

IRR Since inception

This is the most widely used IRR measure of private equity performance. It measures the return of PE funds based on all cash flows in and out of the fund, as well as the remaining net asset value of the fund. This therefore most closely reflects the return an investor would achieve if they invested at the start of the fund. This is the most likely scenario in South Africa where investors in private equity funds are locked in for the life of the fund, and must catch up initial fees when joining a fund after the initial investors.

End-to-end IRR

End-to-end IRRs allow the computation of the return of groups of private equity funds which do not necessarily have the same inception date. This calculation also allows a better comparison of private equity returns to those of other asset classes over similar periods. While this method has advantages, it must be noted that it allows the returns of funds at different life cycle stages to be combined. Where the period selected contains more new funds than older funds, the return will likely include a higher balance of fees than a time period with more older funds. The longer term IRRs are considered to be the most indicative of private equity performance across different stages of the economic cycle, and are considered to be the headline measures. Shorter term returns should be viewed with caution as private equity is a long term investment. However, shorter period returns may be indicative of the general performance of private equity over this short period.

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Times Money

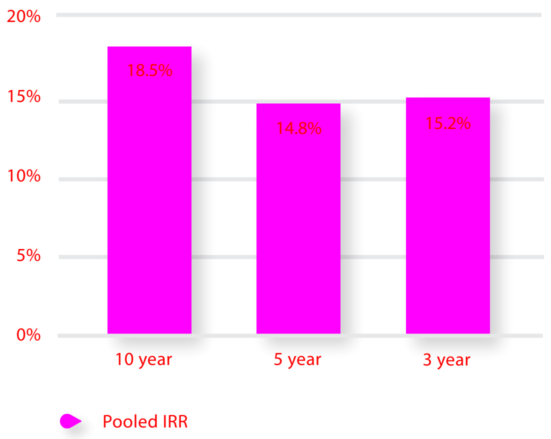
Times Money is the ratio of total capital invested to total capital returned and remaining value. This is a useful cross-check of IRR measures, and is easily understandable. While IRR calculations are heavily dependent on the length of time that capital has been invested, Times Money does not take time into account. A Times Money in excess of 1 means that value has been created for the investor.

Public market equivalent (PME)

This measure seeks to equate the heavily timing dependent returns of private equity funds with the returns of public market indices. The measure is a ratio of the net outflows from PE funds re-invested into the public index to the end of the fund's life, divided by the inflows into a PE fund invested in the public index until the end of the fund's life. A ratio of above 1 reflects outperformance of private equity, while a ratio under 1 reflects under performance.

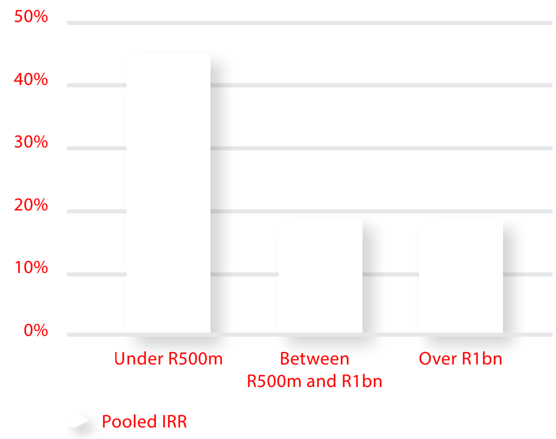
Performance in South African Rands

Pooled IRR by time period

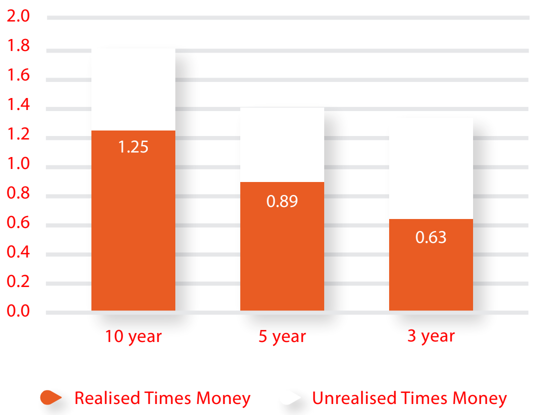


Pooled IRR by vintage year

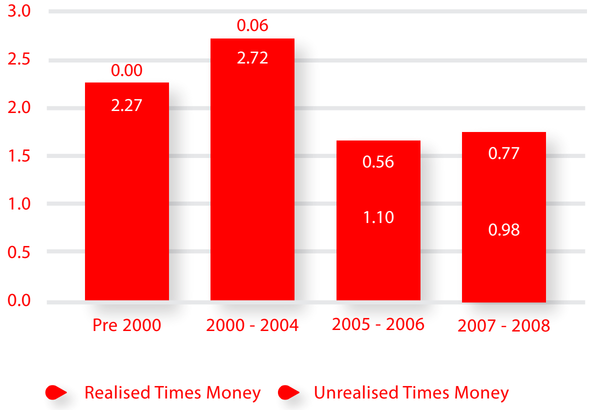
Pooled IRR by fund size



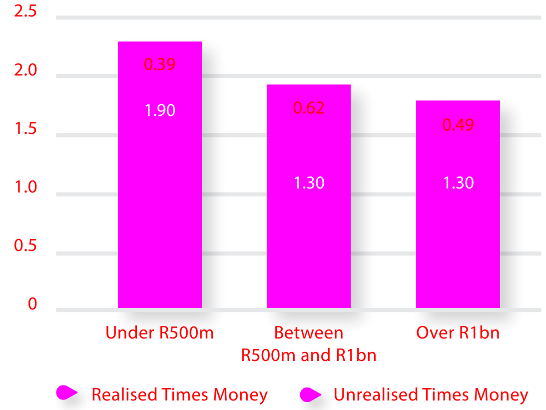
Times Money by time period



Times Money by vintage year



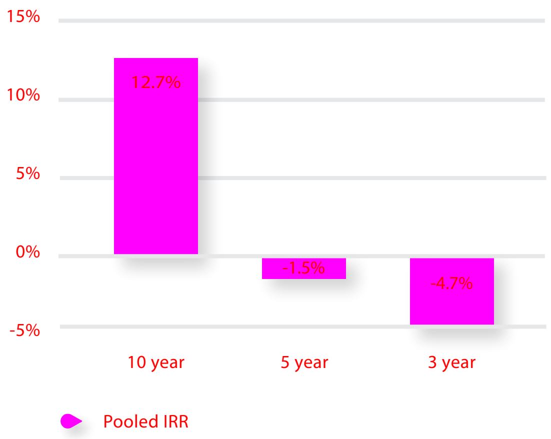
Times Money by fund size



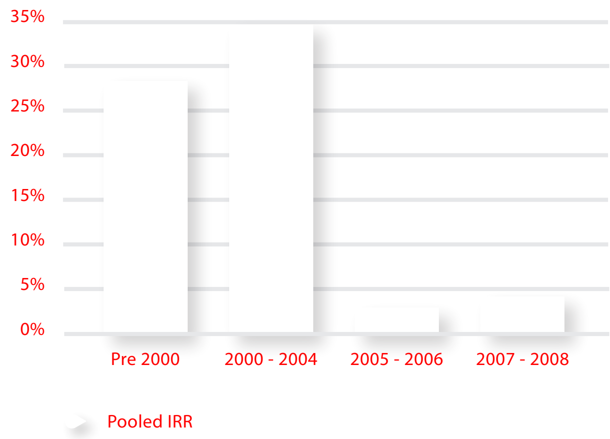
*Fund Size is reflected as committed capital in South African Rands.

Performance in US Dollars

Pooled IRR by time period

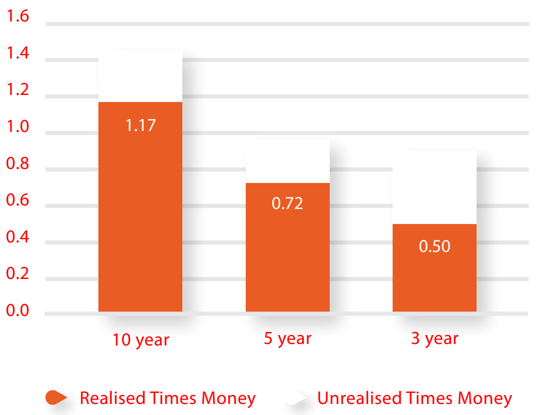


Pooled IRR by vintage year

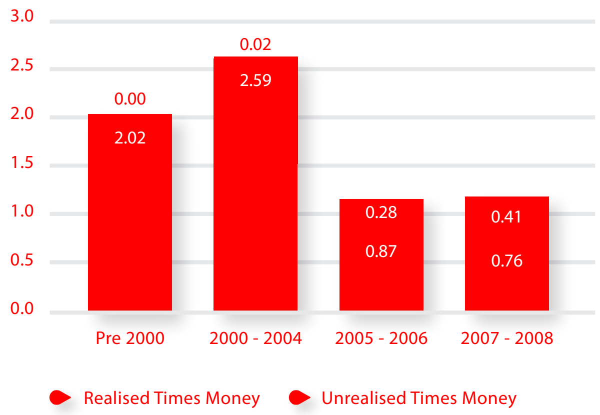


Pooled IRR by fund size

Times Money by time period



Times Money by vintage year



Times Money by fund size

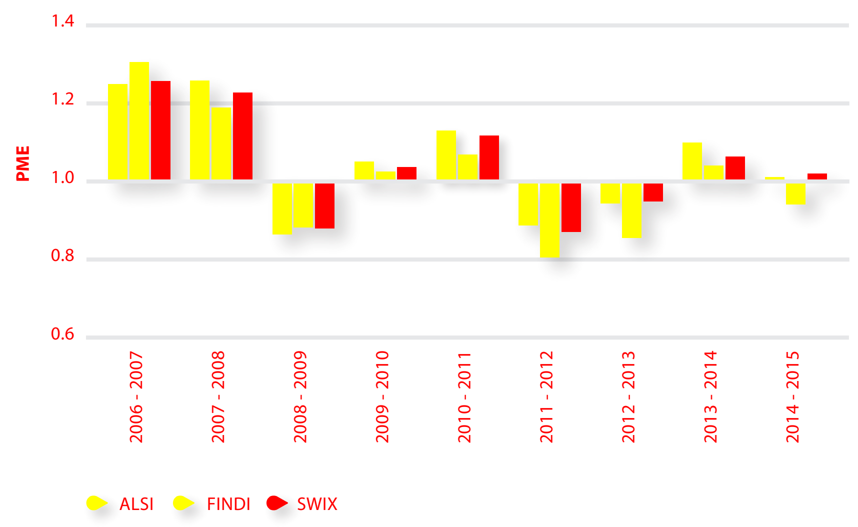
*Fund Size is reflected as committed capital in South African Rands.

Listed equity comparison (ZAR)

CAGR

Time period	Pooled IRR	ALSI TRI*	FINDI TRI*	SWIX TRI*
10 year	18.5%	14.1%	18.9%	14.7%
5 year	14.8%	12.9%	23.6%	14.2%
3 year	15.2%	12.2%	22.5%	12.9%

Public market equivalent results by year



Public Market Equivalent**

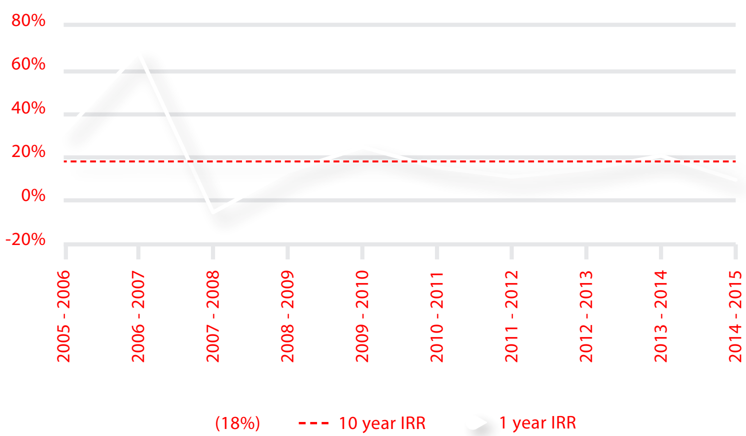
Time period	PME FINDI	PME ALSI	PME SWIX
10 year	1.01	1.16	1.14
5 year	0.85	1.03	1.00
3 year	0.85	1.01	1.00

*Listed index returns are before fees.
**Listed indices used in the computations are total return indices before fees.

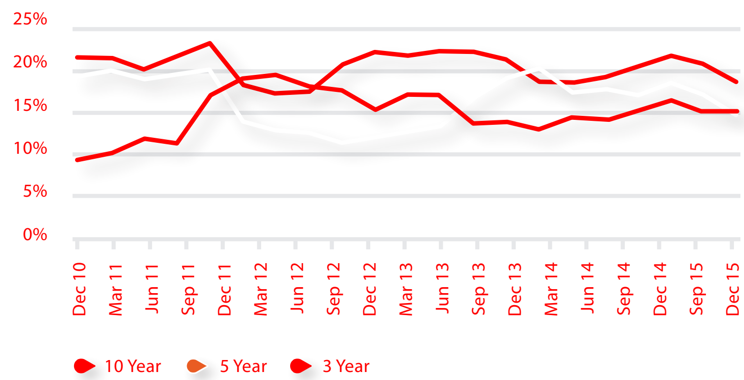
Public market equivalent results by time period

Private equity returns over time

SA PE year-on-year returns (ZAR)



SA PE pooled rolling IRR year on year returns (ZAR)



How to use this report

Useful information:

- Returns of cash flow and portfolio value data from private equity managers are the primary source for information included in this Report.
- The IRR performance calculation solves for the discount rate that makes the Net Present Value of a set of cash flows equal to zero. The calculation is based on cash-on-cash returns over equal periods, modified for the residual value of the fund's equity (NAV). The residual value attributed to each respective group being measured is incorporated as its ending value.
- The database accounts for cash flows on a daily basis wherever possible otherwise a monthly basis, and NAVs on a quarterly basis.
- The End-to-End performance calculation is similar to the since inception IRR, however, it is measuring the return between two points in time. The calculation takes into account the opening NAV, the in-period cash flows and the closing NAV. Returns are then annualised for comparability.
- The pool of funds has been split into subsets where this would enhance the user's understanding of returns. However, this has been balanced with confidentiality considerations, and no such subsets include fewer than four funds.
- Most funds included in this Report have unrealised investments, and therefore rely on the valuation of these investments to determine returns. All participating fund managers are members of SAVCA and apply the International Private Equity and Venture Capital Valuation Guidelines to determine these valuations. RisCura has not verified that these Guidelines have been adhered to.
- Only South African Rand denominated funds have been included in this Report, and therefore none of the returns included are affected by exchange rate movements.

Definitions:

CAGR is the cumulative annual growth rate.

Committed capital is the value of dedicated investment funds pledged by the investors of a private equity fund and available for investment. This is a proxy for the size of the fund.

Fund Size is determined by the committed capital of a fund.

IRRs are money-weighted returns that should be compared to time-weighted returns with caution. Time-weighted returns are used to measure returns in most asset classes where frequent valuations are available.

PME Public Market Equivalent is a measure that determines whether private equity returns have exceeded or underperformed a public market. A PME score of more than one indicates outperformance of private equity.

Pooled IRR aggregates or "pools" all cash flows and ending NAVs to calculate a money-weighted return.

Realised Times Money is the multiple of cash returned to investors divided by total cash invested.

Total Times Money is the sum of the Realised and Unrealised Times Money.

Unrealised Times Money is the multiple of the carrying value of portfolio investments not yet returned to investors divided by total cash invested.

Vintage Year is defined as the year in which a fund first draws down capital from its investors.

About

About RisCura

RisCura is a global, independent provider of professional investment services. RisCura services institutional investors, asset managers, hedge funds and private equity firms with over USD200 billion in assets under advice. RisCura is a leading provider of investment consulting, independent valuation, risk and performance analysis services to investors.

For more information about RisCura visit www.riscura.com

About SAVCA

The Southern African Venture Capital and Private Equity Association (SAVCA) is the industry body and public policy advocate for private equity and venture capital in Southern Africa, representing about R170 billion in assets under management, through nearly 150 members. SAVCA promotes Southern African private equity by engaging with regulators and legislators on a range of matters affecting the industry, providing relevant and insightful research on aspects of the industry, offering training on private equity and creating meaningful networking opportunities for industry players.

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