

is either listed for a long time or in the process of being liquidated, etc" says Greenhill.

With regard to the Merger and Acquisition industry, Greenhill says that M&A activity in South Africa has obviously been muted, which he believes is a function of market conditions.

He adds that a substantial deal that springs to mind is the Life Healthcare deal that is valued at some £138 million in cash.

Regulatory issues

It's no secret that banks are presently reluctant to lend, and when they do,

the lending rates are significantly higher to those experienced by the Private Equity industry in the past several years.

The lack of available funding, together with declining valuations, means that many deals are being funded from Private Equity investors' own funds. In other words, fewer deals are structured on an aggressively leveraged basis.

According to Cliffe Dekker Hofmeyr's Director, Peter Hesselning, where leveraged buy-outs are done, these deals are often structured as outright assets purchases, largely funded by

DEAL CARD 3

Name of investment: INM Outdoor
 Equity Providers: RMB Corvest, Helios Investment Partners, CVCI, MSG Afrika Investment Holdings
 Total Funding: R1.100 million
 Type of investment: Leveraged buy out
 BEE Status: Black empowered company (More than 25% owned by black people)

debt, or as share-sale transactions followed by subsequent restructuring in order to introduce interest bearing debt.

SERVICES ENTREPRENEURS SHOULD EXPECT FROM PE ADVISORS

As a key driver of funding, Private Equity is important in spurring economic growth and consequently, creating jobs. Private Equity has been credited for the massive growth of Black Economic Empowerment and women-owned businesses which have trebled since the inception of BEE.

According to Kgomotso Lekola, Managing Director of LGC Capital, employment figures from Stats SA released in June emphasize how precarious local economic growth is with 79 000 jobs lost in the first quarter of 2010.

"A study by the Global Entrepreneurship Monitor (UCT) shows how a shortage of capital combined with a deficit in skills is a major hindrance to business activity in South Africa. There is significant research showing that the skills level in an economy dictates the growth of capital formation in that economy and that a similar relationship exists in organisations of all sizes," says Lekola.

In some economies it is possible for capital formation to grow concurrently with skills. However, where the gap between required capital and skills is particularly large, it becomes necessary to have a step change in skill first in order to acquire capital. In South Africa, the skills lag is evidenced in the quality of business plans and how start-ups fail to package their business ideas in order for them to be saleable to funders.

According to The Global Entrepreneurship Monitor (UCT) the following are obstacles to entrepreneurial activity in South Africa:

- Shortage of capital (81%)
- Business planning (68%)
- Insufficient information knowledge (75%)
- Quality of employees (57%)
- Marketing of products/services (57%)

Lekola adds that a 2008 Deloitte study on global trends in Venture Capital showed that the South African Private Equity sector has a tendency toward later stage investment. South Africa's early stage investment at 6% of total unrealised portfolio at cost by 31 December 2008 is lower than North America's (11%) and Europe's (9%).

"The 2009 SAVCA/DBSA study on the economic impact of PE surprisingly found that buyout firms were slightly more innovative than early stage firms in terms of bringing new products and services to market. This finding is counter intuitive because one would expect to observe the opposite. This could therefore, point to the fact that either there is risk aversion to new enterprises by investors or that early stage firms in general lack the skills to develop a proper plan around their ideas and as such many of them never get to be funded in the first place," says Lekola.

Clearly, if South Africa is to build a strong economy with new companies entering the market with new and innovative solutions, more early stage investment is needed. Fundamentally there needs to be more early stage investment in high growth potential enterprises, but this cannot happen if the risk is significantly increased, a method to manage and limit risk is required. "More consulting and advice firms are required to assist new businesses in the various stages of development by providing them with essential skills thus vastly increasing their rate of success. As a result of this realisation the issue of new venture creation is beginning to receive much academic attention with some South African business schools beginning to design courses and entire degrees around it," concludes Lekola.

Bedeveling the industry!

Investor certainty as regards the regulatory framework is an important factor that could drive the growth of the Venture Capital and Private Equity market in South Africa.

"An issue, which continues to create uncertainty is the application of the Financial Advisory and Intermediary Services Act, 2002 (FAIS) to the Private Equity industry. It is not altogether clear whether Private Equity and Venture Capital firms require a financial services provider licence under FAIS and if a licence is required, which entity within the fund structure should apply for such licence," says Hesselning.

SAVCA has applied to the Financial Services Board for certain exemptions and clarifications. Most of the larger Private Equity fund managers have now taken the view that they should be licenced and are in fact licenced. Certain amendments to FAIS are also proposed and it is hoped that a clear distinction will be drawn between the regulations of financial service providers that transact with retail customers versus those dealing with sophisticated clients.

Gaps in the Venture Capital market

Private Equity and Venture Capital has internationally been proven to be a key driver of growth and efficiency of an economy or a particular industry. It is therefore important, from a policy perspective, to create a favourable environment for investors. There is also an obvious need for government to incentivise investment in small and medium enterprises, which play a key role in the South African economy.

Hesselning says that against this background it is unfortunate that the highly anticipated tax incentives for Venture Capital investments announced