



# PRIVATE EQUITY & VENTURE CAPITAL

NOVEMBER 2011

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**Annual Review • November 2011**  
**Private Equity & Venture Capital**

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# PRIVATE EQUITY & VENTURE CAPITAL

NOVEMBER 2011 • ANNUAL REVIEW

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## UNITED STATES

Jonathan Levitsky, Debevoise & Plimpton LLP

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### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

In 2010 and into the third quarter of 2011, it looked like the private equity market was starting to rebound from a very slow period in the immediate aftermath of the financial crisis of 2007 and 2008. While activity levels never reached pre-crisis heights, we started to see a significant uptick – driven by factors including increasing confidence among sponsors and sellers as to asset values, plenty of ‘dry powder’ (uninvested equity capital), and a highly favourable lending environment in which debt was available at historically low interest rates for leveraged transactions on sponsor-friendly terms. That started to change in the summer of this year, as turmoil in the financial markets introduced substantial uncertainty.

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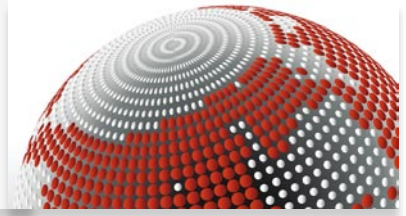
### **What steps are general partners taking to create value throughout their portfolio?**

Sponsors generally refinanced portfolio company debt with near term maturities while the financing markets were favourable. The current focus is on creating value in other ways, including by managing costs carefully, staying close to key customers, maintaining short-term liquidity and being rigorous in ensuring compliance with debt covenants to avoid the need for waivers or amendments. We expect that 2012 may bring an increase in portfolio companies executing ‘tack on’ acquisitions, which we anticipate may be available at attractive valuations.

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### **Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

This is unquestionably a challenging time for exits. Equity market volatility makes the environment for IPOs difficult, and dividend recapitalisation opportunities and sales of portfolio companies to



other private equity sponsors are limited by the current lending environment. While strategic buyers have significant cash reserves and often access to financing on more favourable terms to support the purchase of portfolio companies, reaching agreement on valuation will be challenging until the market finds a measure of equilibrium. While some successful exits were completed in the past 18 months before the current market turbulence, including a number of IPOs, sponsors are sitting on a backlog of increasingly mature portfolio companies that are ripe for exit when market conditions turn around. Where sponsors hold positions in publicly traded equities – typically following an IPO or sale of a portfolio company to a strategic buyer for stock – we see continued interest in exiting those positions at the right price to generate returns for limited partners.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

The dramatic regulatory shifts affecting the fund industry in the last two years make regulatory compliance a key area of concern. By March 2012, a substantial number of private fund managers will have newly registered with the US Securities and Exchange Commission and adopted the concomitant policies and procedures. However, for firms that have not historically been steeped in a regulatory compliance culture, creating functional systems to meet their new obligations will be a significant practical challenge – particularly for an industry defined by entrepreneurial spirit and individual creativity. The balance of power at the negotiating table favours investors in the current environment, making fundraising a lengthier and more expensive process than ever before. Investors' focus on increased transparency and tighter controls often results in more detailed and more frequent reporting requirements, and in some cases greater involvement of advisory committees in operational issues. Implementing and ensuring compliance with these changes may require more resources for managers.

## UNITED STATES

Jonathan Levitsky, Debevoise & Plimpton LLP

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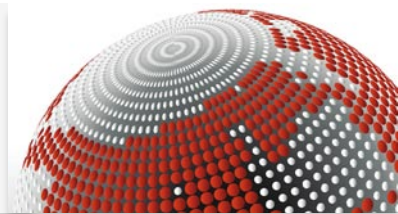
### **To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

The fundraising environment remains challenging but has improved dramatically in 2011 relative to the last two years, with a record number of funds in the market this year. These funds span a broad range of categories, in contrast to 2009 and 2010, when successful fundraising was largely focused on niches like emerging markets, energy and infrastructure. The more active deal market in 2010 and early 2011 allowed mature funds to exit from some long-held investments and return cash to investors, and also permitted funds that entered the downturn with significant dry powder to accelerate the deployment of their capital. The result is that more fund sponsors are ready to return to market, and more investors are willing to invest. Given recent and anticipated market swings, investors are insisting more than ever on the core indicators of stability and strength: a strong track record over different market cycles, a stable and cohesive team, and a consistent approach to investing in the firm's core sectors.

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### **Looking ahead, what developments do you expect to see in the private equity industry in your region?**

On the M&A side, we are in a choppy market at the moment. We are hopeful that deal volumes (both exits and new acquisitions) will return in 2012 as some of the macroeconomic questions driving current market instability are resolved, valuations settle and the leveraged finance market stabilises. Our sponsor clients are mindful that some of their most successful investments have been made in difficult markets, and when we look back on this period that may well be the story of 2012. We anticipate continued slow improvement in the fundraising market, with continued strong interest in niche investment areas such as energy and infrastructure and emerging markets. Within emerging markets, we expect to see expansion from faster growing individual economies like Brazil and China to more regional strategies.



## **JONATHAN LEVITSKY**

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Jonathan Levitsky is a member of the firm's Corporate Department whose practice focuses primarily on public and private mergers and acquisitions and joint ventures. He regularly represents leading private equity sponsors.

## CANADA

Troy Ungerman, Norton Rose OR LLP

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### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

In Canada, private equity activity has been slow in the last 12-18 months.

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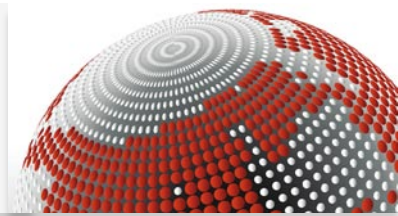
### **What steps are general partners taking to create value throughout their portfolio?**

General partners are trying to raise funds and increase their arsenal in order that when the markets rebound, their firms will have built strength and be prepared to act. While not yet common, more private equity firms are expressing interest in mining activities, mainly because it is a sector that has held up well despite general market volatility.

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### **Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

IPOs have traditionally been the exit route of choice for private equity firms. Even at the beginning of 2011, we saw private equity firms trying to exit through IPOs (for example, Bauer IPO). However, since August, the markets have become very volatile and IPO activity has slowed considerably. Private equity firms are waiting for the markets to stabilise. Once the markets stabilise, there will be renewed interest in IPOs as an exit route. Until then, other exit routes include strategic acquisitions by industry players (private equity firms selling to other private equity firms), and reverse takeover monetisations, mostly in the mining sector but also in some other industries.



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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

One major challenge for fund managers is that institutional investors are starting to demand increased disclosure and transparency to prevent fraudulent activity from occurring. As a result, there is a huge push to adopt governance best practices in sectors where these practices were previously not necessary. For example, a worldwide trend is developing to extend disclosure and transparency obligations to hedge funds.

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**To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

The outlook for fundraising has not been great – it is not overly pessimistic, but it is not positive either. Investors want a landscape where they can see a future. As such, there has been a move to diversify from traditional investments such as industrials and consumer products. The mining sector is generating increased interest from private equity firms since more value is perceived to exist.

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**Looking ahead, what developments do you expect to see in the private equity industry in your region?**

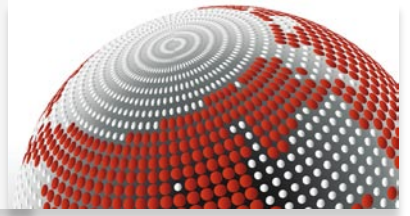
First, the private equity industry can expect to see greater investor demand for enhanced transparency and disclosure. A second development that we can expect to see once the markets stabilise is the proliferation of IPOs. Currently, there is a lot of demand for IPOs; there is a lot of

## CANADA

Troy Ungerman, Norton Rose OR LLP

*continued...*

monetisation taking place, but companies are waiting for the economy to recover in order to launch IPOs. When the market turns, private equity firms will capitalise on that demand and IPO activity will increase. In addition, we will see growth in new technologies such as biotechnology, clean technology and IT. We anticipate that Canada will have to diversify away from resources into a new technology-based economy.



## TROY UNGERMAN

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Troy Ungerman is a partner at Norton Rose OR LLP. His practice focuses on domestic and cross-border private mergers, acquisitions, divestitures, private equity, venture capital investments, strategic alliances, corporate reorganisations and financings. He provides transactional as well as corporate and commercial advice to domestic and foreign clients in a wide array of industries, including the payment card, manufacturing, financial services, telecommunications, technology and health care industries. Mr Ungerman is co-chair of the mergers and acquisitions team and a member of the Canadian diversity committee.

## GERMANY

Peter Memminger, Milbank, Tweed, Hadley & McCloy LLP

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### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

Buyout activity increased significantly from autumn 2010 onwards and the outlook for 2011 was quite positive. This outlook was proved correct in the first five to six months of the year, before the financial crisis caused many transactions to slow down or even stop due to the uncertainty of the economic outlook and limited willingness of banks to provide acquisition debt. The situation has, however, cleared up a bit and transactions continue to some extent, however with reduced speed as uncertainty of the future outlook has increased in recent times. As for the factors driving buyouts and investments, we clearly see that some of the major German conglomerates who have not yet undergone a major corporate restructuring process had thought at the beginning of the year that the increasing valuation for companies, reflected also on the stock markets, offered the change to divest some of their non-core business. These transactions have, however, mostly halted.

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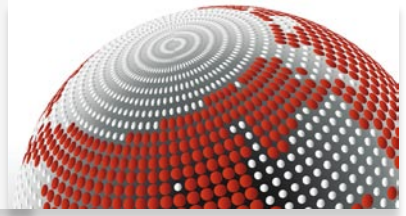
### **What steps are general partners taking to create value throughout their portfolio?**

At the beginning of the year, many general partners intended to take advantage of the renewed seller-friendly environment making use of the availability of debt financing and increasing valuation ratios to exit their businesses. This seemed to be the wave which the market had expected for some years, but it did not really accelerate further due to the financial crisis which kicked in at the middle of this year. One has to acknowledge, however, that another small wave of PE exits may hit the market autumn and winter this year.

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### **Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

At the moment it is only the M&A road which is really available. IPOs or leverage recaps are not feasible in the current market environment. This, again, shows how fast markets can change, as both



had been possible in the first half of 2011.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

In Germany, no significant regulatory changes have occurred in the last 12-18 months. What remains a challenge is keeping the relationship with limited partners, and also intermediaries, in good working condition, given that the deal flow alone does not offer a regular interaction with these actors.

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**To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

With the improved overall environment for buyouts in the second half of 2010 and first half 2011, funds which had been able to take advantage of this nine-month window for exits were able to show positive results to their investors, certainly improving their fundraising prospects – although not every exit achieved this. However, it is too early to say that prospects have improved overall. I would rather expect that they have only improved for some successful general partners, or those with longstanding track records, and remain difficult for others. The experience of the few last years is too fresh, so limited partners would, again, have an unqualified, unspecified approach to committing funds to this asset class.

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**Looking ahead, what developments do you expect to see in the private equity industry in your region?**

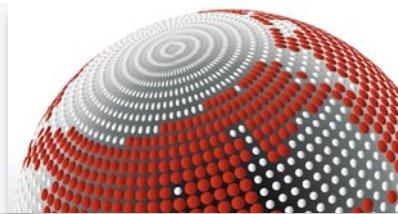
I see a slightly increased deal flow in the imminent future, which I would expect to slow down at the beginning of next year, when it may become obvious that economic growth and outlook will in fact slow down. If this scenario takes place, it is hard to predict how 2012 will develop. There is

## GERMANY

Peter Memminger, Milbank, Tweed, Hadley & McCloy LLP

*continued...*

increasing pressure on general partners to achieve exits with portfolio companies, many of which, in 2012, they will have had well beyond a four to five-year holding period in their portfolio. Whether this will result in an increasing deal flow in 2012 depends on a number of factors such as the dimension of the economic slow-down and the further development of the economic crisis. Of course, if the economic outlook, despite my previous assumptions, remains stable and positive, and acquisition debt becomes available on a more predictable and continuing basis, 2012 could have all the pre-conditions to become one of the most active years in the last five to 10 years.



## **PETER MEMMINGER**

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## THE NETHERLANDS

Gregory Crookes, Clifford Chance

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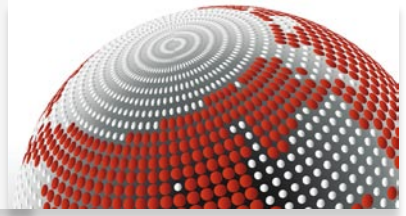
### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

Activity levels picked up significantly in the second half of 2010 and continued through the first half of 2011 with a steady flow of deals, mostly in the mid-market. Secondary deals seem to have been the main feature of the last 12 months, driven by the need for general partners (GPs) to create an exit from existing investments on the one hand and a return of some degree of liquidity to the acquisition finance market and the need for GPs to invest committed funds on the other. Another deal driver has been restructuring activity, for instance debt-for-equity swaps and/or exits from over-leveraged portfolio companies. A particularly interesting deal was the take-private by Gilde and Parcom of Gamma Holding NV, which was the first 'concert parties bid' in the Netherlands. There have also been some successful exits to trade buyers, for instance Permira's agreement to sell Dutch animal food producer Provimi to Cargill for €1.5bn. The second half of 2011 has so far been characterised by caution as a result of the European sovereign debt crisis and broader macro economic circumstances.

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### **What steps are general partners taking to create value throughout their portfolio?**

A range of strategies are being applied, depending on the circumstances. For instance there are some clear cases of buy-and-build but, at the other end of the spectrum, there are still companies which are over-leveraged and are going through a debt-restructuring or where the management equity plan is under water due to a combination of operating factors and adverse tax legislation, and needs to be re-cut. One notable trend is that private equity firms, despite being the holders of ordinary shares and therefore ranked lowest in the capital structure, have regularly been able to salvage fairly significant value and persuade debt investors to take a haircut. We've also advised in situations where a strategic review has led to the business being split and the various divisions being separately groomed for exit. In other cases healthy businesses simply require fresh capital to make the next step in their logical evolution.



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**Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

Given the deep uncertainties in the equity markets the IPO route seems largely closed for now and that leaves a trade sale as the most viable option. That said, the situation can change quickly and we have had involvement with GPs preparing some of their portfolio companies for a listing as and when a window of opportunity presents itself.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

A major challenge facing fund managers at the present time is dealing with the sheer number of regulatory reforms at national, EU and international levels. Private equity funds will have to deal with the increased compliance burden and the significant costs incurred by it. Of the numerous reforms in the pipeline, the Alternative Investment Managers Directive (AIFM Directive) is having the biggest impact, with PE fund managers becoming subject to regulatory supervision. Compliance programs are already being set up by managers to deal with the various aspects of the AIFM Directive, including arrangements with depositaries, capital requirements, governance, delegation, conflicts, and the thorny question of remuneration.

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**To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

Logically, uncertainty and volatility on the stock markets would cause investors to turn part of their funds from public to private investments, for instance, through private equity funds. Private equity fundraising seems poised for a recovery in 2011. An example in the Dutch market is the recent set-up by Waterland Private Equity Investments of its fifth institutional fund, Waterland attracted €1.1bn

## THE NETHERLANDS

Gregory Crookes, Clifford Chance

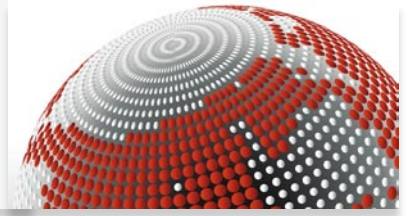
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within just five months, significantly surpassing its €900m target. Both the speed and the volume of the Waterland deal indicate a growing interest in the private equity sector, in particular with institutional investors. This is, however, accompanied by the adoption of a more careful, selective and demanding approach by investors, demonstrated by an increasingly active involvement when negotiating terms. In general, investors focus on transparency, alignment of interest, and governance, a fact illustrated by the publication of private equity principles by the Institutional Limited Partners Association (ILPA).

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### **Looking ahead, what developments do you expect to see in the private equity industry in your region?**

We believe secondary deals in the mid-market bracket are likely to also be a feature of the second half of 2011. Finance for quality assets ought to be available – partly as a result of redemptions on earlier deals triggered by the spate of M&A activity we have recently seen – though terms for new loans will probably tighten again and banks will be very cautious to underwrite as they are still struggling to syndicate loans written in the first half of 2011. However, the European sovereign debt crisis and a number of other macro-economic factors also present a challenging outlook for private equity for the short to medium term and is likely to cause investment and credit committees to be very critical of business cases. As always in a difficult operating environment GPs and CFOs will be cautious with leverage and seek ways to protect operating margins. Also, on the 16th of September, the Dutch government issued the long expected proposals that will limit the deductibility of acquisition finance costs for mid-market and large LBOs, effectively limiting the amount of leverage that can be applied in a tax efficient way. This will create challenges in pricing and structuring new deals. Fortunately, the proposals contain a grandfathering for existing deals. These proposals are expected to enter into force on 1 January 2012.



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Gregory Crookes is a partner in Clifford Chance's corporate practice. Mr Crookes specialises in M&A, particularly private equity, and advises a wide range of large and mid-market players and their portfolio companies. Recent deals include advising Sanoma on the acquisition of SBS Broadcasting and Maxeda – a portfolio company of AlInvest, Cinven, KKR and Permira – in relation to the disposals of various businesses including HEMA V&D, La Place, De Bijenkorf, Hunkemöller and M&S Mode, and the listing of Nielsen Holdings NV on the NYSE.

## LUXEMBOURG

Vanessa Molloy, M Partners

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### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

Generally, there was a good start to 2011 with deal activity in Luxembourg being positive overall. Unfortunately, this has tapered off due to fears of a recession and further market volatility. In certain instances envisaged IPOs have been put on hold indefinitely. Nonetheless there is a pipeline of potential new PE funds that may be launched with enquiries arising from Asia, Eastern Europe, South America and Africa. Luxembourg has the advantage of offering either the pooling/commitment vehicle in regulated or unregulated form and/or the SPV vehicle – formed typically for tax treaty reasons – for entering/exiting the target jurisdiction. It is often difficult to gauge the true extent of Luxembourg's participation in the PE domain as statistics relating to the unregulated form/SPV vehicle are difficult to obtain.

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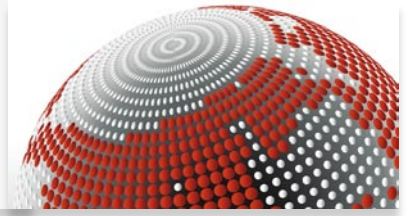
### **What steps are general partners taking to create value throughout their portfolio?**

We are generally seeing a more hands-on approach by general partners at the investment level, particularly focusing on cash flow. Our GP clients have advised us that it has been, and continues to be, tight on both the demand and supply side. This problem has been exacerbated by investors seeking liquidity, which has not typically been offered by PE investments, as well as the problems in obtaining leverage for the deals. Most often leverage is not provided by local Luxembourg banks but city banks with the negotiations taking much longer and sometimes ending unsuccessfully.

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### **Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

With the current limit on debt financing as a means of exit, GPs are seeking other exit opportunities or delaying exiting until conditions have improved. Therefore, we have seen a number of restructurings at the Luxembourg SPV level – liquidations, recapitalisations, mergers, migrations,



and so on. We have also seen increased secondary and tertiary transactions among GPs as a way of exiting.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

Clients are looking closely at the implications of the Alternative Investment Fund Managers Directive (AIFMD). The considerations differ depending on the life cycle of the fund and the location of the manager. Some are concluding that if there is no reason to be in Europe then it is best to stay out even if they like the profile of Luxembourg. Others who need to be in Europe are familiarising themselves with the directive's requirements, such as no asset stripping for two years, valuation, and disclosure, and find Luxembourg with its well-known fund profile suitable. Managers that typically have self-managed Luxembourg SPVs with no AIFM to which to point directly are examining the directive and waiting on ESMA level II measures. There is a concern that the costs of third party service providers may increase due to the additional burden imposed on the depository, auditor and administrator under the directive. There is also concern that the uncertainty in the European banking sector and its regulation will continue to affect the availability of leverage.

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**To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

Fundraising remains difficult and unfortunately the target size is not always reached. First closings take much longer than in 2007 and 2008. We have seen a trend towards purchasing distressed undervalued companies and there is still a great interest in the emerging markets and in the European energy sector.

## LUXEMBOURG

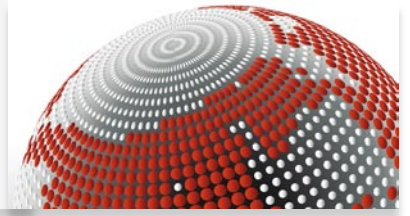
Vanessa Molloy, M Partners

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### **Looking ahead, what developments do you expect to see in the private equity industry in your region?**

On the legislative front there is a drive to encourage the Luxembourg legislator to amend exiting law or introduce a vehicle similar to the English transparent limited partnership. A new category of 'depository' may be introduced into Luxembourg law as envisaged in the AIFM directive. We expect to see further growth in fund set-ups targeting emerging markets. We also expect more public to private deals and strategic buyers that are not necessarily PE investors hoping to pick up a competitor at a good price. Family offices and HNWI are focusing on short-term investments with defined exits due to long-term market uncertainty. Currently, investors are looking for liquidity, which has not typically been offered by PE investments. We have been advised by our clients that if family office investors wish to grow, or even double, the family wealth each generation, they will have to look at PE investments to help achieve this.



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Vanessa Molloy is the Fund Partner at M Partners Luxembourg, a member of the Maitland network of law firms. Ms Molloy has over 10 years of post-qualification experience in the fund industry. She specialises in private equity and other alternative investment funds with a deep understanding of offshore and onshore structures and a focus on Luxembourg. She assists both promoters with evaluating the commercial and legal merits of PE structuring, as well as family offices and HNWI with due diligence on PE investments. Her expertise ranges from deal structuring to post-transaction integration services.

## CZECH REPUBLIC

Alois Šatava, Randa Havel Legal

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### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

According to the statistics available, the volume and number of closed deals in the Czech Republic declined in the first half of 2011 in comparison to previous years. Otherwise, since 2008 the number and volume of deals was comparable each year until 2010. I would say that private equity (PE) and venture capital (VC) funds have been much more careful lately – as have all investors – and more closely evaluate the future potential of any contemplated investment. The small amount of optimism held by investors who, at the end of 2010, may have started to believe that the financial crisis was over, has since turned back into pessimism due to the profound problems in the euro zone.

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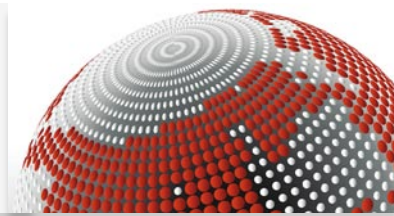
### **What steps are general partners taking to create value throughout their portfolio?**

The steps to create value in the portfolio remain the same. These are, in particular: selecting quality investments with a high potential for growth; a detailed due diligence of the target; strengthening/replacing management after acquisition, if necessary; introducing new synergies; implementing more effective and innovative processes; as well as building strong brands, and so on. One way to create great potential for a successful exit is to be able to change a local Czech/Slovak company into a CEE brand and player; this however requires a suitable company and product for regional expansion. What has changed in the past two years, I think, is the fact that PE and VC funds must really carefully evaluate the potential of any contemplated investment, as only real quality businesses can, in the end, lead to a successful exit. The past years, unfortunately, have showed that not all PE or VC investments are successful.

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### **Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

Unfortunately, an exit through the public market, which should be one of the obvious exit options, is



not an entirely suitable scenario in the Czech Republic. Sadly, the Prague Stock Exchange does not, for many reasons, serve as a market where initial public offerings are done. There have been only a very few IPOs on the Prague Stock Exchange in the past few years. Moreover, there is no secondary market that would serve smaller/medium sized deals such as, for example, the Polish NewConnect. Therefore, the main exit strategy remains a sale to strategic investors from the US, Asia or Europe. Secondary sales to another private equity fund are less common.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

Czech legislation is unfortunately unsatisfactory and does not support PE and VC structures. Therefore, we see 'domestic' funds with holding structures set-out outside of the Czech Republic; accordingly such structures are established and regulated by foreign legal systems. There are initiatives from local PE/VC players to introduce Czech legislation that would allow and support investments through PE and VC structures. Hopefully, these will be heard by the authorities and legislature and new laws supporting development of Czech PE and VC structures will be introduced.

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**To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

Traditional sources of PE funds funding are banks, pension funds, mutual funds, and other financial institutions. However, due to unsatisfactory legislation these fund sources are not practically available in the Czech Republic. At the same time, even though Czech funds have foreign structures, such funds are usually too small to attract material funding from foreign institutions. Therefore, local Czech PE/VC funds are largely dependent on funds provided not by financial institutions, but by private investors as limited partners. Also, we see deals by investors that are not always set up as typical PE/VC funds, but the structures of the deals are similar to classic PE and VC investments. These investors, however, invest their private money without the need to raise funds from limited partners.

## CZECH REPUBLIC

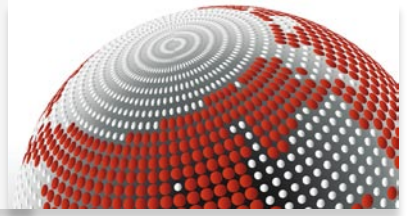
Alois Šatava, Randa Havel Legal

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### **Looking ahead, what developments do you expect to see in the private equity industry in your region?**

The Czech market and economy are rather small. This contributes to the fact that there are fewer investment opportunities for large international funds. On the other hand, this gives advantages and provides opportunities to funds with local knowledge and insight. I expect the further development and growth of local funds investing in the Czech Republic and the CEE countries. Any legislative changes supporting local PE and VC structures, and allowing financial and other institutions to participate as limited partners, have the potential to boost the PE/VC industry.



## **ALOIS SATAVA**

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Alois Satava has substantial experience in the areas of commercial law, M&A, and finance and banking including acquisition finance; syndication; bond issues; private equity transactions; and post acquisition restructuring. Mr Satava has advised both sellers and purchasers on many large and mid-size acquisitions in the steel industry, engineering and machinery, waste management, telecommunications, chemicals, construction, real estate and other industries. He also provides legal services in the energy sector, including nuclear power plants, and in the area of deliveries of complex technological units and steam and gas turbines.

## MIDDLE EAST

Pervez Akhtar, Freshfields Bruckhaus Deringer LLP

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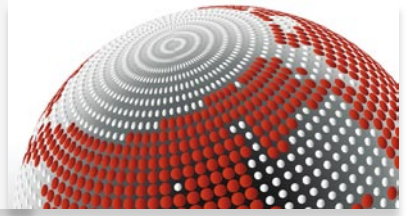
### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

Private equity activity in the MENA region remained somewhat limited over the last 18 months. Deal volumes continued to decline in 2010 with total value of completed transactions estimated to have declined from approximately \$900m in 2009 to \$700m in 2010. The latter figure includes one major transaction, Abraaj's acquisition of Network International, which, if excluded, would further reduce the value of completed transactions to just \$150m. The relatively low investment activity in the region reflects the current limited availability of acquisition finance and the mismatch between sellers' and buyers' expectations, as buyers remain cautious following the global financial crisis and the perceived dangers of a double dip. Market conditions were further affected by the recent events of the Arab Spring especially in Egypt, historically one of the most active markets in the region.

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### **What steps are general partners taking to create value throughout their portfolio?**

Private equity investments in the MENA region are generally growth-oriented, where target companies are typically younger in their development cycle than their counterparts in mature LBO markets such as the US and Europe. This necessitates a relatively more meaningful involvement from general partners in the post acquisition phase of an investment. In addition, over the last two years, private equity managers in the region had to first deal with the repercussions of the global financial crisis on their portfolio, and then work on positioning their companies to take full advantage of an eventual economic recovery and consequently maximise their exit opportunities. As a result general partners have increasingly taken an even more active role in managing their portfolio companies and driving post-acquisition value creation. This involvement typically ranges from closer performance monitoring to higher involvement in setting management's strategic agenda.



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**Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

The number of private exits in the region over the last two years has remained limited, partly because the majority of the deals in the region are still recent and hence too early to exit, but also because of the continued volatility of the public markets and the consequently lower prospects of IPOs. In the current market conditions, the most likely and preferred exit route for PE firms is selling to trade buyers, who tend to have relatively good access to third party financing and consequently superior ability to complete transactions. In addition, and given the low activity in the primary market, the secondary market in the region is expected to develop in the medium term and provide an increasingly likely and attractive exit route for fund managers, just like it does in the US and European markets. In addition to market conditions, the exit strategy is generally a function of the size of the portfolio company and the sector it operates in, the nature and requirements of its future growth plans, and the quality and aspirations of its management team.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

The biggest challenge private equity managers face today is dealing with the large capital overhang in the industry, which has led to increased competition, and higher valuations for attractive investment opportunities. Private equity funds deploying capital are no longer able to rely on leverage and financial engineering to generate returns on their investments, but today have to take on a more active role in post acquisition value creation in order to generate the returns expected and required by LPs. We believe however that private equity in the MENA region is increasingly regarded as an alternate source of capital to the traditional forms of financing that are currently shying away from the market, which is expected to have a very positive impact on fund deployment in the short to medium term. In addition, fund managers in the region continue to face the challenge of dealing with a complex and, in certain instances, unclear regulatory environment.

## MIDDLE EAST

Pervez Akhtar, Freshfields Bruckhaus Deringer LLP

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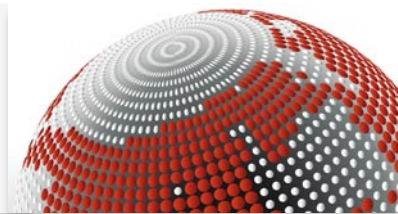
### **To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

Fundraising has been challenging for fund managers over the last 18 months, with total funds raised in the MENA region in 2010 amounting to just under \$1.5bn, significantly below pre-crisis levels. Fundraising prospects in the region have also been impacted by the events of the Arab Spring and the renewed turbulence in financial markets in Europe and the US, although 'local capital' with higher understanding of, and more comfort with the regional dynamics continued to be available. In these challenging conditions, LPs are increasingly focused on fund managers' track records, their ability to generate returns through superior post acquisition value creation at their portfolio companies, and their ability to safely steer their portfolio through turbulent times as proven during the global financial crisis. These conditions strongly favour those firms that have built a solid track record of deploying capital and generating returns on a consistent basis, giving them superior access to LPs.

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### **Looking ahead, what developments do you expect to see in the private equity industry in your region?**

As the gap between the market leaders and weak performers in the private equity sector, and especially in the large buyout funds space, becomes more pronounced, we expect to see a polarisation of capital raising between SME funds on one side, and multi-billion funds on the other. This trend has started in 2010 where approximately 25 percent of total funds raised and 50 percent of investments completed related to venture/SME capital, and is expected to accelerate in the short to medium term.



## PERVEZ AKHTAR

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Pervez Akhtar is the managing partner of Freshfields Bruckhaus Deringer in the Middle East and North Africa (MENA) region and head of the firm's MENA corporate practice. He specialises in advising both local and international private equity houses on their investments throughout the MENA region as well as sovereign wealth funds and government investment vehicles on transactions integral to their strategic investment and economic diversification programmes. He has advised on some of the largest private equity transactions to take place in the MENA region with particular experience of advising on transactions in the finance, energy & utilities and healthcare sectors.

## AFRICA

Hugh Naylor, Trinity International LLP

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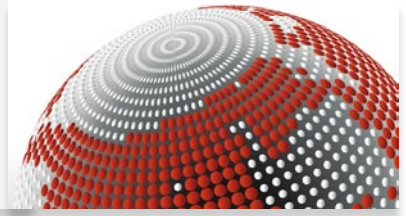
### **How would you describe private equity activity in your region over the last 12-18 months? What factors are driving buyouts and investments?**

Given the lacklustre returns being achieved in Europe and the US, and the feeling that many other emerging markets are currently overpriced, Africa represents one of the better places to deploy capital in order to generate alpha returns. Average annual GDP growth for Africa since 2001 has been 5.4 percent compared to 1.6 percent in the western economies. During the credit crunch Africa experienced growth as the developed economies shrank. The commodities boom has helped nations such as Angola, Zambia and Nigeria, and increasing food prices have made agriculture, and related business such as agri-services and food processing, more attractive. Investment activity remains steady with Helios and Vitol's acquisition of Shell's downstream assets being one of the largest buyouts on the continent. However, deal volumes within Africa for the first three quarters of 2011 remain substantially below many other emerging markets.

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### **What steps are general partners taking to create value throughout their portfolio?**

Private equity in Africa, with the exception of South Africa, has focused more on growth capital rather than leverage/financial engineering. The key is to identify good local businesses, usually leaders in a particular market, and provide additional capital and management expertise to grow and to expand into complimentary products and services. A key driver is the ability to identify good local partners. Historically sellers have tended to retain a stake in the business giving rise to a relationship more akin to a partnership than a traditional Western buy out where the seller exits and the sponsor takes sole control. Leverage is rare, though that is likely to change, not least through increased use of re-financings to generate returns or to enable a sponsor to buy out minority shareholders.



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**Which exit routes are open to PE firms in the current market? What considerations are general partners making when implementing their exit strategies?**

Preqin data shows exits of approximately \$1.2bn so far this year, dramatically up on \$79m for 2010 and \$244m for 2009. The traditional exit routes of a trade sale, listing or re-financing apply but the market simply isn't there to the extent it is in the Western economies. International companies are focusing more on Africa – witness WalMart's acquisition of Massmart – but Africa is competing with other developing countries and the pool of trade buyers for many businesses remains relatively small. Local exchanges are developing but, with the exception of South Africa, Nigeria, and possibly Egypt, tend to lack depth and liquidity. Listing on overseas exchanges such as London's Alternative Investment Market is possible but the costs involved require critical mass. A secondary buyout market, while present in South Africa, has yet to develop elsewhere though that may change as the larger sponsors start to focus on the region, bringing with them minimum ticket size for investments.

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**In your opinion, what are the major challenges for fund managers, such as regulatory compliance, risk management and enhanced disclosure?**

There's a mistaken perception that doing business in Africa is inherently more risky than elsewhere, whether by reason of corruption, political risk, criminality, or otherwise but the reality is that Africa is no different from any other market. As with investing in any jurisdiction the sponsor needs to understand the regulatory framework and ensure both it and the target have a proactive and cooperative relationship with regulators. Political risk is an inherent part of an investment in any developing countries and, in part, can be reduced by structuring investments to take advantage on bilateral investment treaties and applicable international conventions. Political risk insurance is available though not always on economically viable terms.

## AFRICA

Hugh Naylor, Trinity International LLP

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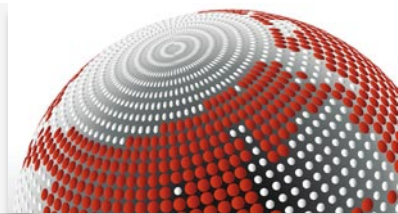
### **To what extent has the outlook for fundraising improved? What types of characteristics and investment strategies are limited partners looking for when committing funds?**

In theory the outlook has greatly improved with LPs showing a lot more interest in Africa as an investment destination. However, the extent to which this is reflected in fundraising has yet to appear. Closure of Helios' \$900m fund was a huge fillip for sponsors focusing on Africa, as was Carlyle's establishment of an investment team focusing on sub-Saharan Africa. 3i Group's focus on expanding into Africa is further evidence of the increasing attractiveness of the continent. However the market remains extremely tough, especially for first time funds. New funds are taking years to get to first close, if at all. That this is due in part to the turbulence in the global markets is not in doubt but the evidence is that LPs remain sceptical of the perceived risk and returns. Regulatory changes in various African countries allowing indigenous pension funds to invest in private equity will help GPs but CDC's increasing focus on direct investments at the expense of investing in third party funds will hit the smaller funds which remain reliant on DFI funding.

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### **Looking ahead, what developments do you expect to see in the private equity industry in your region?**

Increasingly the current upsurge in interest of LPs will turn into actual investment but this may be too late for many of the smaller funds currently on the road. For existing funds there will be increasing pressure from LPs to generate exits and return capital and, for those that do, there is the opportunity to develop a powerful, Africa-centric brand with a greater ability to raise subsequent funds and become a market leader. There is also likely to be increased specialism, such as Adlevo's focus on technology and Silk Invest's focus on food. The continent will continue to present some remarkable opportunities particularly in growth capital and buy and build strategies but also, with a generation of portfolio companies likely to come to market over the next 12 to 18 months, to develop a more traditional buy out market with an increased role for leverage.



## HUGH NAYLOR

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Hugh Naylor is a highly experienced corporate lawyer specialising in private equity and growth/ development capital transactions both in the UK and internationally, with a particular focus on Africa and other emerging markets. Mr Naylor has a broad range of experience advising sponsors, management teams, co-investors, and companies that are raising funds privately. He also focuses on funds work, specialising in private equity fund formation, as well as acting for investors in private equity funds. He has extensive experience of private company and business acquisitions and disposals, re-constructions, re-organisations, joint ventures and general corporate work.



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