OLD MUTUAL ALTERNATIVE INVESTMENTS

MEMBER PROFILE

Paul Boynton, Chief Executive Officer

Old Mutual Alternative Investments (OMAI) is the largest private alternative investment manager in Africa with over US$4.8bn under management across 27 active funds and over 160 portfolio companies. Originating in 1970 as Old Mutual's private equity fund, OMAI is committed to sustainable development in Africa through its infrastructure, renewable energy, affordable housing, education, private equity and fund of funds assets. OMAI seeks to mobilise capital intelligently while building great businesses in partnership with its stakeholders.

AVCA speaks with Paul Boynton, Chief Executive Officer of OMAI about the strategy for its funds, diversification, and the role of public-private-partnerships in realising Africa's long-term growth.

OLDMUTUAL
ALTERNATIVE INVESTMENTS

NAME OF GENERAL PARTNER
Old Mutual Alternative Investments

ASSETS UNDER MANAGEMENT
Over US$4.8bn

REGIONAL FOCUS
Pan-African

Q: How has OMAI developed into a primary player in the alternative investments space?

Old Mutual Group was originally established in Cape Town as a traditional asset management business. Ten years ago, we divided the business into several boutiques each focusing on a specific investment space, e.g. fixed income, quantitative, global equities and alternative investments (AI). Our alternative investments business focuses on four pillars, these being infrastructure, private equity, impact investing and fund of funds. Although we don't cover the whole of the alternatives spectrum - without hedge fund strategies as it stands - we have approximately ZAR60bn in assets under management (US$5bn), 160 employees, five offices in Abidjan, Lagos, Nairobi, Cape Town and Johannesburg, and 180 underlying portfolio positions or portfolio companies.

Q: What is your current focus across the four pillars of the business?

One of our primary focus pillars is infrastructure. Having set up African Infrastructure Investment Managers (AIIM) as a joint venture with Macquarie in 2000, we bought them out three years ago to continue to build our portfolio of bulk infrastructure. Energy is a key sector for us and we're a big player in South African renewables. We've also invested in power in West Africa, the first PPP toll road in Nigeria, as well as in airports, ports, and logistics and telecoms infrastructure. In terms of typical ticket size we tend to invest in the US$20mn – US$100mn range and have a ZAR10bn open-ended South African fund established in 1999 which is relatively unusual in the AI space. We also have a US$500mn pan-African fund.

Our PE business has a South African-focused buyout strategy and we're able to invest up to 20% of the fund outside South Africa. Our current ZAR4bn fund is 70% invested and we're looking to raise a fund in the same series next year. We usually do deals in the ZAR300-ZAR500mn (US$25mn – US$40mn) range, targeting either control deals or minority deals with appropriate minority rights.

Our impact funds are the newest part of the business which focus on three areas: affordable housing, where we build but also have rental stock, affordable schooling, and retirement accommodation. We've also helped alternative mortgage providers with capital to fund affordable housing.

The fund of funds business has two remits - a global one, where we invest in European, Asian and American funds. At the moment, we are in the third tranche of that programme and are continuing to raise capital. The second programme focuses on African GPs, and we've invested 60-70% of the capital raised for our first fund.

Q: How do you incorporate and mitigate political/regulatory risk and currency volatility into your strategies across all funds and what is OMAI's approach to diversification?

For foreign exchange, there are two key issues. The first is ensuring that the exchange rate risk is minimised. In the power sector, for instance, we would look to index the tariff to a hard currency like the US dollar or CFA Franc in West Africa to ensure that we aren't exposed to currency risk on the tariff line. The second issue is remitability - you can take political risk insurance around the asset itself, but you also need to ensure that you've done everything possible to externalise cash flow on the project. There isn't a one-size-fits-all solution - you need to assess how exposed you are, how you can manage that risk, and whether that risk is bankable.

You also need to look at exchange rates across the business. This differs between a dollar fund investing in an asset with local currency exposure and a South African rand return fund raised in rand. For instance, exchange rate risk will impact businesses we invest in if the rand appreciates or depreciates. If the rand depreciates, the cost of sales goes up because of imported elements and margins may be under pressure because you can't fully recover on your sales price. The opposite can also be true.

We have invested ZAR6 billion in equity

We're invested in a tourism business in South Africa, that business benefits from a weaker rand because South Africa becomes more attractive to tourists as they tend to spend more in local currency. The main concern investors raise about investing in Africa is that they want a dollar return.

Q: OMAI has made investments across the continent through the flagship African Infrastructure Investment Fund 3 (AIIF3). What are the investment criteria, and how does OMAI evaluate trends in Africa's under-developed power, trade facilitation, logistics, renewables and communications infrastructure sectors to translate these into compelling investments?

In AIIF3 we are targeting a 20% gross US dollar return and have invested in five assets where we see significant opportunities to date, several of which are in power. In terms of macro trends there are 600 million people in Africa, 50% of the population do not have access to electricity. Because of the enormous deficit in power infrastructure across the continent we've invested in the Azura plant in Nigeria, currently under construction. Nigeria's grid has a capacity of 4,000MW but diesel generation accounts for more than that despite the cost being four times higher. The fact that South Africa - a similar sized economy - has a capacity of 45,000MW provides further evidence of the enormous Nigerian power shortfall. The World Bank has estimated that the infrastructure deficit in Africa requires substantial investment over a decade of US$120bn – US$150bn per annum, so there is an enormous need and opportunity for this type of investment. We've also invested in a port logistics business in East Africa, as well as a gas pipeline company and power plant in Ghana that will add 10% (350-400MW) to its grid.

Q: What are your thoughts on the role public-private partnerships (PPPs) have to play in driving Africa's long-term growth?

We are big investors in South African renewables. There have been 90 projects through rounds 1 to 4 of the Renewable Energy Independent Power Producer Procurement (REIPPP) programme and we have invested in 20 of them. In total, we have invested ZAR6bn in equity, while banks have mainly provided debt. The REIPPP programme is second to none in terms of its quality, reliability and clear bid criteria. The programme also has very thorough documentation. We acknowledge how critical it is to have the right regulatory framework in place to attract bids. We are also noticing continuous opportunities for improvement because of the various rounds of the project. So if one bid fails, you can tweak it and re-submit at a later round. From a PPP point of view, this is the gold standard that should be applied across Africa. The other possibility for financing these types of projects is through bilateral negotiations, which can be quite tricky because of government procurement constraints such as the Public Finance Management Act in South Africa, although it can be the best option in some countries if there are difficulties getting several bidders behind a project.

Investments in our focus areas spur growth in the wider ecosystem with knock-on benefit to our investors

Q: You recently appointed Zom Chizura as OMAI's Head of Impact Funds, a notable move in a time where responsible investing is gaining greater industry interest. Tell us about OMAI's strategy for its impact funds.

We are only active in the impact space in South Africa as it currently stands but have explored launching a fund with an East Africa focus. Our strategy is to identify pressing social needs where we believe we can do something about them. We help investors understand the balance of generating returns commensurate with risk while taking on a liquidity haircut with capital tied up for 12-15 years. This is necessary to generate the outcomes we are focused on, and although investors won't be able to extract the liquidity premium ordinarily awarded for tying capital up for long periods, they are able to make a significant social impact. Another school of thought is that investments in our focus areas spur growth in the wider ecosystem with knock-on benefit to our investors. For instance, we've targeted 80,000 units of stock from our housing fund, which is moderate considering the 2 million unit deficit in South Africa. Nonetheless, investing in our housing fund will contribute to a lot of other economic benefits which a large investor may likely benefit from. Firstly the construction drives GDP and employment growth. New owners over time will acquire furniture or white goods such as a refrigerator, all of which contribute to growing our economy and benefit companies in those areas and which may form part of an investor's portfolio.

Our education fund will have built infrastructure for 40,000 students by the time it's fully invested. Our price point is ZAR1,000 – ZAR2,000 a month and we have produced pass rates 20% ahead of the average at matriculation/school leaver level. In the long-term, these investments will have a profound impact on the economic growth capacity of the country. Like our ambitions in the housing sector, the social impact will equally benefit investors through their other investments.

Q: How does OMAI apply ESG standards across its investment portfolio and how do you align and coordinate with your fund-of-fund investments in this respect?

ESG is a journey for OMAI. A journey to which we've committed resources in terms of staff and consultants working with us. We've developed an ESG framework and architecture along with management structures for each of the four pillars of the business. For each transaction we consider certain key questions. For the fund of fund business, we have a questionnaire that we send out to GPs to see how they think about and manage ESG within their portfolios. We engage with them on this basis to better understand how well developed their ESG processes are and whether we should delve deeper in certain areas. Admittedly ESG as a driver of outcomes is more difficult to achieve with fund of funds than as a GP, especially when you invest in a fund as a minority investor. But we've taken the 17 Sustainable Development Goals (SDGs) and considered their applicability in each of our four business pillars. We have selected those that we believe we can most make a difference on each of the four areas and assess any investments we make against the identical goals. We assess each portfolio company and their metrics both against its peer group and also how it is improving over time.

Q: What is OMAI's approach to regional growth expansion through its investments?

Regional expansion is a theme we have looked at closely. Our PE team has done one or two deals in the rest of Africa, but the main focus has been on South Africa. Within portfolio companies, expansion into Africa has been something that we have been pushing for a long time. For instance, Tourvest has a big African footprint and is one of the largest commercial operators in Victoria falls with a sizeable East African presence. Since our original investment, expansion has been a big part of the strategy, as has also been the case for Tiger Automotive. Our In2Food business is also looking at expanding into Australia because of their work with Woolworths. Achieving geographical development is a big value driver in PE because it makes our businesses more attractive for strategic buyers, especially multinationals. We also see potential for geographic expansion in services, retail and financial services, less so in infrastructure. In logistics, however, we're aiming to build a presence that becomes regionally relevant having invested in rail in Zimbabwe, which was later extended to a concession in Zambia.

Q: By the same token, how important is it to have local fund managers who understand the dynamics of markets?

Local presence is vital. We find that one of the best ways to mitigate risk is to have local managers with local knowledge. We look at who they are, where they've been based, what experience they have, past deals and time spent in Africa when we select managers. In infrastructure, it's beneficial to have investors alongside you who help mitigate risk. An investor with local capital mitigates risk, but we also look at DFIs such as CDC Group or the International Finance Corporation, who have different political capital, as significant risk mitigators.

Q: What are your goals for the next 12 months?

We see a lot of deal flow in the African infrastructure space. It's an exciting area for us. We're also particularly optimistic about the general environment in South Africa, which has been quite tight over the last few years because of the political and economic situation. It's early days but we believe that the situation is more prospective from a deal point of view. In fact, the whole continent has recovered from the commodity slump to a certain extent and we're expecting more of Africa's cylinders to be firing over the next year. There's a lot of opportunity for us and the PE industry in Africa.

CONTACT AVCA

37 North Row
3rd Floor
London W1K 6DH

E avca@avca-africa.org
W www.avca-africa.org
C www.avcaconference.com
T +44 (0)20 3874 7008

African Private Equity and
Venture Capital Association