

PRIVATE EQUITY FUNDS MOVE TO THE FORE

Below is a précis of an address by Mohamed Younes, CEO of the Concord Group to the Channel Islands Stock Exchange international business summit held on 11 September 2009, prepared by Advocate William Simpson of Ogier Guernsey, finance lawyers and fund administrators

Private Equity in the Middle East is rapidly becoming the major regional industry primarily because of the unprecedented flow of funds, as a result of the high oil prices coupled with the repatriation of funds to the region by Arab investors. This trend will continue in the foreseeable future. The immediate impact was a massive increase in local investments resulting in spectacular price increases, which in turn created an overheated initial public offering (IPO) market. A natural consequence was the birth of a so-called private equity market. In fact, most of the deals were essentially pre-IPO funds who acquired existing companies, which were then sold into the public markets. In that process approximately 30 private equity firms with over \$18 billion in funds were created in the Middle East.

With the frenzy in the Saudi Arabia, Abu Dhabi and Dubai stock markets, the newly formed private equity firms were able to bid for existing companies and fold them into new vehicles

that were then offered in the IPO market at substantial premiums over a very short-term span. This burst of new offerings almost disappeared once the stock markets in the area came on sharply and we are now returning to a more interesting phase where the accumulation of surplus funds is continuing at a rapid pace. More importantly, several of the major international private equity firms are looking at investing in some of the major markets of the Middle East.

Middle East paradox

In looking at the regional industry we face a 'Middle East Paradox': with the exception of Saudi Arabia, the countries with the largest surpluses are the countries with the smallest populations, the smallest non-oil industries and the smallest native populations. As a result, most of the private equity firms are concentrated in these smaller countries. However, the smaller countries cannot absorb these funds and cannot offer sufficient diversification. Most of these countries have

one major industry - oil - followed by banking and real estate. On the other hand, countries such as Egypt and Saudi Arabia and to a lesser extent Morocco, Tunisia and Jordan offer significantly more private equity opportunities because of their size, economic diversification, larger populations and larger domestic markets.

Egypt is regarded by some as the single most important private equity market at the moment. With a population exceeding 75 million and with a GDP growth rate of 7.2% before the world crisis, it is presently enjoying its strongest macro-economic position in over 100 years. The growth rate has slowed, but its economy is fairly well diversified, with over 10,000 companies active in 22 different industrial sectors covering a full range from food, retailing, banking, pharmaceuticals, mining, tourism and real estate, for example. There are over 350 companies listed on the stock exchange. Thanks to the very conservative policy of the Central Bank, the banking system has emerged from the crisis in a very strong position and is highly liquid. The loan to deposit ratio is around 52%.

Recent economic figures suggest that the economy is on its way to full recovery. In this context, the government's forecasted growth rate for 2009/10 of 5.3%-5.5% looks reasonable, albeit higher than forecasts of some international organisations

The Concord Group

The Concord Group is a New York-based Securities and Exchange Commission registered investment management firm with offices in New York, Cairo and Tokyo. The firm is one of the leading firms managing portfolios of Egyptian securities. The total assets under management as at June 2009 were US\$1.8bn of which US\$1.4bn were invested in Egyptian-listed securities and Egyptian private equity. These assets are managed through 14 mutual funds of which six are listed on the Channel Islands Stock Exchange with others listed on the London Stock Exchange, the Dublin Stock Exchange and the Luxembourg Stock Exchange.



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Furthermore, the first hurdle the private equity investor will face is credibility with the sellers and with management and employees. The second hurdle and the more important one relates to the labour force, their unions and their perception of the buyer. The third one relates to the availability of financing if the transaction is leveraged, taking into account the availability of

and brokerage houses. Egypt is also likely to be the second-largest growing economy, following Qatar which continues to benefit from its status as the world's largest liquefied natural gas exporter.

Despite the recent hike in prices, data reveals that out of the 100 most active stocks on the Egyptian Stock Exchange, on 26 August 2009, 96 companies were still trading at lower price levels than on 30 June 2008, with 78 of these trading at prices more than 40% lower than in mid 2008. Price-to-earnings ratios range from five-to-eight times earnings.

In addition, recent private equity transactions are noteworthy. For example the 500-million-dollar acquisition of Amoun Pharmaceuticals, Egypt's largest privately owned generic manufacturing company. The acquisition was made by a consortium of sovereign investors together with the Concord Group, with legal support on Guernsey and Cayman Law by Ogier.

Change of approach

As a result, the largest participants, with rare exceptions, are physically

located near the source of their funds and far from the major and most attractive markets for acquisitions.

However, going forward, private equity in the Middle East will require more of a venture-capital approach. In other words, the successful private equity firms will be the ones who have the know-how and capability to help develop the investor company, much along the same lines as venture capitalists.

Therefore any successful business model for private equity in the Middle East must be based on physical presence in the target country directly or in partnership with a well-established local firm.

financing.

There are no legal obstacles to acquisition financing, although the official attitude concerning the desirability of foreign investors using domestic resources to acquire domestic assets will vary from case to case.

As we now stand and until the Saudi market opens up, Egypt, Morocco and Jordan will remain as the most promising private equity market in the area and there is a great potential for the private equity markets over the coming year. The successful players will be the ones who adapt their business models and their structures to the reality on the ground.

WHY USE GUERNSEY?

With five decades of experience, Guernsey has become the leading location for private equity and investment funds business. Its reputation, location and tax-neutral status has attracted a global spread of leading investment management companies to establish investment funds in Guernsey. They have found high-quality legal, accounting, valuation, registrar, company secretarial and audit services for the structuring, launch and administration of their investment funds. At the end of December 2009, the overall value of funds under management and administration in Guernsey stood at more than £184bn.

With modern legislation and regulation it was no surprise that Guernsey was placed on the OECD White List by the G20 in 2009. The Guernsey Financial Services Commission, established in 1987, operates within statutory powers regulating the local finance industry. The approach has ensured that Guernsey remains one of the best pragmatically regulated jurisdictions in Europe and a premier location to conduct business. Only organisations complying with international standards of practice are licensed to operate in Guernsey.

The island received a significant boost with the establishment of the Channel Islands Stock Exchange (CISX) in 1998. The CISX, based in Guernsey, has seen considerable growth since its inception, having completed its 3500th listing in January this year and provides wide recognition for Guernsey-based investment funds and companies from around the world.