MENA Private Equity Association

Private Equity and Venture Capital in the MENA region

2016 REPORT

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Foreword

Arif Amiri,

Chief Executive Officer, DIFC Authority

The MENA Private Equity Association's 11th Private Equity and Venture Capital annual report – (MENA PEA 2016) once again highlights the strategies, structural changes and significant trends influencing and shaping the investment industry. This comprehensive study is an essential reference and knowledge resource, which gives a clearer picture of this unique industry to private equity investors looking to operate in the region.

This year's report reveals that, despite the various regional and global geopolitical issues and economic challenges, investor confidence remains high sustained by encouraging investment activity in the region.

Predictably, as a result of the drop in oil prices, private equity investors and venture capitalists have been strengthening their portfolios in sectors away from oil and gas, further adding to the diversity of the region's contemporary equity landscape.

While traditional sectors such as transportation have enjoyed the highest investment activity, accounting for 31% of total investment value. Pointing to a growing regional need, 17% of total investment activity was found to be in the space of IT, FinTech and E-Commerce, showing the emerging industries which continue to go from strength to strength in the region.

We commented last year that the region's technology focused entrepreneurial base was continuing to grow and mature, affording increased early stage investment opportunities. Indeed, the 2016 report reflects this in the upsurge in deal volumes, with VC commitment to this area standing at 55% of all investment, including in Information Technology (27%), FinTech (13%) and E-Commerce (15%).

In line with this strong trend, at DIFC, we have made the growth of FinTech and the opportunities it brings to Dubai and the region a priority for our own investment activities. Earlier this year, we launched FinTech Hive at DIFC, a first-of-its-kind accelerator in the region, aligned with the UAE National Innovation Strategy and Dubai Plan 2021, which will make Dubai one of the smartest cities in the world.

FinTech Hive at DIFC is an enabler for technology and finance, building on the Centre's existing FinTech ecosystem and providing a platform for innovators to adapt and develop their products and solutions to meet the needs of the broader Middle East, Africa and South Asia region. The accelerator is well-positioned to unlock further investment opportunities in the FinTech space, stimulating deal flow across the region and further contributing to DIFC's 2024 Strategy, which will see the Centre grow three-fold over the course of a decade.

In this spirit and on behalf of DIFC I thank the MENA Private Equity Association for this comprehensive report which will undoubtedly help shape the future for private equity and venture capital in the region through profound insight and meaningful analysis.

With Gratitude

The MENA Private Equity Association extends its sincere appreciation to Thomson Reuters for sharing primary data used for this annual report. We are most grateful to our knowledge partners Deloitte for developing the report analysis.

Deloitte.

Sam Surrey, *Principal Director, Financial Advisory, Deloitte Middle East*

Ali Taki, *Assistant Director, Financial Advisory, Deloitte Middle East*

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Rabih Sader, *Head of Content – Thomson Reuters*

Youmna Akiki, *Research Associate, Investment Monitors, Thomson Reuters*

STEERING COMMITTEE OF THE MENA PRIVATE EQUITY ASSOCIATION

We also thank the association's steering committee members as well as the thought leadership and survey participants, for their contributions towards the development of this report.

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Nahed Ashour, *Head of Media Relations and Arabic Content,*
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1. Important Notice

1.1 Basis of the Annual Report Preparation

This report has been prepared based on data sourced from Thomson Reuters Private Equity Monitor and primary research initiated by Deloitte.

Historical data was updated from that used in the 2015 annual report to reflect increased disclosure of information in the market.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is or will continue to be accurate. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

In analyzing and determining the parameters of available data, it has been necessary to apply certain criteria, the most significant of which are as follows:

- Private equity is defined to include houses that have a General Partner/Limited Partner structure, investment companies and quasi-governmental entities that are run by, and operate in the same way as, a private equity house.
- Venture capital for the purpose of this report is defined as a fund specifically dedicated to venture capital investments. This includes funds by venture capital firms, and venture funds under private equity firms.
- Funds managed from MENA, but whose focus is to invest solely outside the region, are excluded from the fundraising and investment totals.
- MENA includes Algeria, Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Morocco, Oman, Palestine, Qatar, Saudi Arabia, Sudan, Syria, Tunisia, the United Arab Emirates, and Yemen.
- Investment size represents the total investment (both the debt and equity portions). However, fund size only considers equity invested, as we have no visibility on debt exposure by funds.
- The fund raising totals are the amounts closed/committed for fund raising funds, closed funds, investing funds, fully vested funds, and liquidated funds.
- Exits are defined to include partial exits, although simple dilutions have not been included.

1.2 Definitions and Assumptions

For analytical purposes, we have considered the following types of funds, as defined by Thomson Reuter's Private Equity Monitor:

- **Announced:** Official launch of funds which are yet to commence fund raising.
- **Rumored:** Funds expected to announce their intention to commence fund raising.
- **Fund raising:** Funds that have been announced and are in the process of raising capital.
- **Investing:** Funds that have closed and are actively seeking and/or making investments.
- **Fully invested:** Funds that have invested all capital raised. Some of the investments may have divested in this stage, but not all.
- **Liquidation:** Funds that have divested all investments and have fulfilled all obligations to shareholders.

1.3 Data Filtering

The primary data sourced from Thomson Reuters has been filtered according to the definitions used in the Emerging Markets Private Equity Association (EMPEA) research methodology. In particular, we have used the following definitions:

Fund Size: In the case of funds yet to make a first close, or where no close information is available, fund size is equivalent to the target amount, and is noted as such. For funds achieving at least one official close, fund size is reported as the capital raised to date, while for funds that have made a final close, the fund size is the total capital raised. All amounts are reported in USD millions. Rumored funds are excluded.

Currency: Where funds data has been provided in a currency other than USD, exchange rates applied are from the last day of the month in which each close is reported, e.g. first close reported in € on 15 April 2016 would be calculated using the exchange rate for 30 April 2016, taken from publicly available sources.

Funds of funds or Secondaries are excluded.

Region: Statistics are based on the "market" approach and funds are categorized based on the intended destination for investments (as defined in a fund's announced mandate) as opposed to where the private equity firm is located. With regard to multi-region funds, we have included these to the extent that there is a focus on the MENA region. EMPEA methodology includes only those multi-region funds whose primary intention is to invest in emerging markets. However, the source data does not provide visibility on primary geographic intention.

Funds established with a specific mandate to invest in real estate are excluded from the fundraising, investment and exit totals. The remaining real estate investments relate to funds with mixed investment mandates.

Conventional infrastructure funds, or funds investing directly in greenfield infrastructure projects (e.g. bridges, roads, etc.), are excluded from fundraising totals. However, funds that make private equity investments (determined based on target returns) in companies operating in the infrastructure sector are included.

EMPEA does not track or report other alternative asset classes, including hedge funds, real estate funds, and conventional infrastructure funds. In our analysis, we have excluded data from investment-type companies, real estate firms, and sovereign wealth funds.

2. Deloitte Introductory Message

For the third year in a row, Deloitte is pleased to have partnered with the MENA Private Equity Association in its annual report on the regional private equity and venture capital industry. We have collaborated on an analysis of performance (including investments, divestments and fund raising activities in 2016) and in surveying fund managers to gauge their outlook for the industry going forward in a continuation of our regular Deloitte Private Equity confidence survey.

The private equity industry experienced significant growth over the period to 2014/2015, but 2016 saw a slow down, reflecting the sustained impact of lower oil prices on the broader economies of the region, pockets of geopolitical instability and shocks to the wider global macro environment, all of which affected broad investor sentiment. Fund managers generally expect this trend to continue in 2017. Adapting to a "new normal" of lower growth is therefore high on the agenda of private equity investors in MENA.

Driving the profitability, growth, and performance of portfolio companies will therefore remain primary objectives for private equity firms. With slower growth, internal controls and transparent business processes increase in importance. With a greater focus on value creation in portfolio companies and overall operational efficiency, highlighting the value-add brought by private equity firms will potentially be critical to convincing businesses of the benefits of working with private equity partners.

At the same time, fund managers highlight that the importance of private equity as an available source of alternative capital is expected to increase in an environment where bank and public market financing may become more restricted.

The fight to raise capital is also getting more intense with 2016 witnessing the lowest number of closes and funds raised in the past five years. Notwithstanding, a number of managers are adopting the "deal by deal" approach to fund raising. Thus announced funds understate the level of raised capital in the industry.

A central and critical theme of the year was the acceleration of venture capital and early stage investing in the region. Notable regional venture capital successes such as Souq.com and Careem have raised the profile of the industry and the number of disclosed investments increased by 44% to 175. We expect this trend to continue as the asset class attracts ever greater interest from both within and outside the region.

The promotion of the venture capital industry has become increasingly prominent, with numbers of incubators and accelerators increasing, alongside a developing legislative framework. Significantly, this in part reflects a government led emphasis, notably in the UAE and KSA, to reduce reliance on the oil and gas sector and foster the development of entrepreneurialism and SMEs.

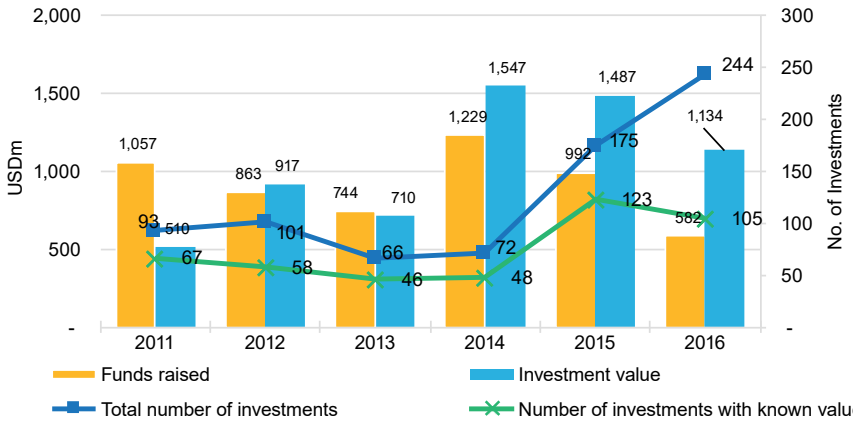
We would once again like to thank Thomson Reuters, the MENA Private Equity Association and the members of the annual report committee for their assistance in the development of this report. Their contribution of both data and insight has been invaluable.

Sam Surrey, *Principal Director, Financial Advisory,Deloitte Middle East*

Ali Taki, *Assistant Director, Financial Advisory,Deloitte Middle East*

3. Overview on Private Equity in The MENA Region

3.1: Funds raised and investments completed

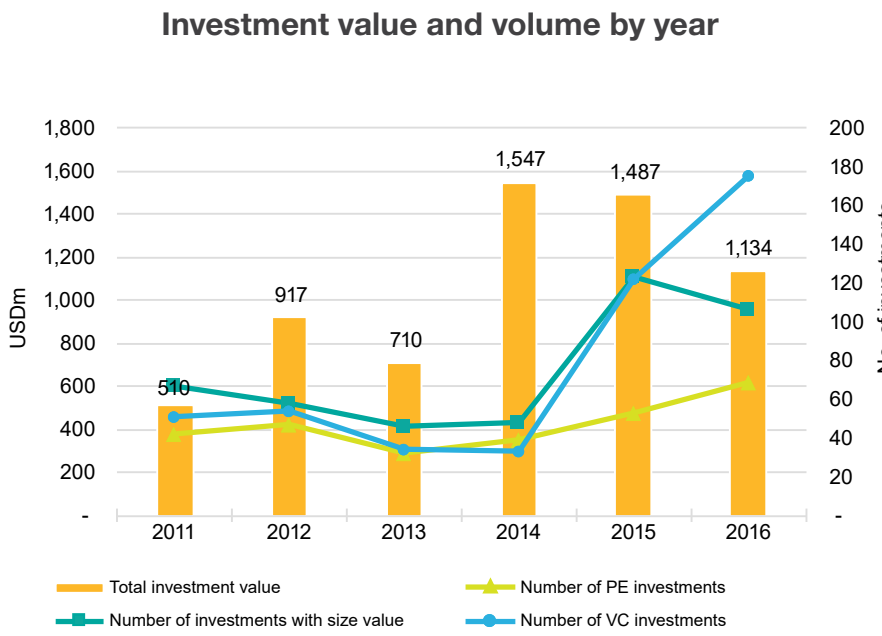


Source: Thomson Reuters and Deloitte

- In 2016 there was a more marked divergence between trends in private equity and venture capital than has been seen in previous years. The overall number of deals increased, as venture capital investment levels continued to grow but the decline in the number of higher value private equity transactions precipitated a decline in the total value of investments made.

- Average disclosed private equity deal sizes remained consistent with the prior year at approximately USD50m. This value is consistent with target deal sizes for a number of firms in the region. While there are notable variations, most regional private equity firms target equity investments of over USD20m and only a limited number invest in excess of USD200m. The consistency in average deal size suggest that those investment criteria have remained largely unchanged.
- Investment activity was notably concentrated in the UAE in 2016. This reflects a perceived flight to safety as the largest alternative markets of Egypt and Saudi Arabia experienced a variety of challenges. In KSA the continuation of lower oil prices and consequent economic slowdown led to investor caution with private equity investors increasingly adopting a wait and see approach. Inflation and currency volatility similarly impacted investor sentiment towards Egypt.
- Private equity GPs focused on consumer driven sectors such as retail, healthcare, transportation, F&B and education with a continued aversion to investing in the oil and gas sectors given the depression of and volatility in oil prices. A number of GPs commented that they wanted greater certainty that the sector had bottomed out before considering making investments.
- We forecast last year that private equity would experience challenges in effecting exits in 2016, with seller and buyer price expectations showing divergence resulting from the headwinds in the market from the impact of oil prices. This proved to be the case with the number of disclosed divestments reducing year on year.
- The fund raising environment continued to be a challenge given the economic climate and regional geopolitical factors impacting external investor perceptions. While fund raising is certainly achievable for those managers with a demonstrably strong track record, the relative youth of the industry means that the number of houses in that position is relatively limited.
- As a result, the prevalence of the deal by deal model, where GPs raise funds for specific transactions, continues to gain in popularity across the MENA region. Fund managers, however, have stressed that when such arrangements are in place that certainty of funding is important to gain a seller's confidence in the deliverability of a transaction.

3.2 Investments



Source: Thomson Reuters and Deloitte

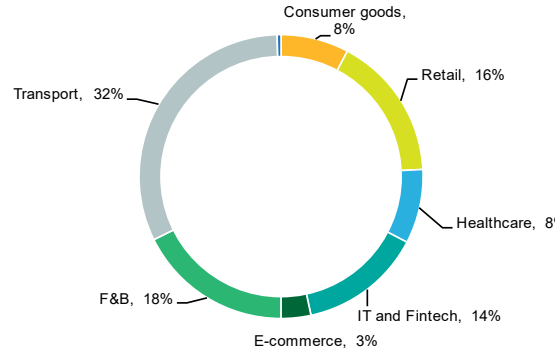
- Investment information is necessarily not fully comprehensive as it is estimated that up to 30% of PE and VC transactions in the MENA region are not announced, and not all announced transactions include details regarding the size of the investment.
- As in prior years, there is a lack of visibility over the funding structures used by fund managers to effect transactions and therefore investment values reflect total transaction size rather than equity investment.
- 244 disclosed investments were made in 2016, continuing the upsurge in activity levels seen in 2015 and representing the highest number of deals in any year post 2008.
- The most pronounced investment trend was in the continued growth of venture capital transactions from 122 in 2015 to 175 in 2016, with private equity transaction numbers increasing more marginally from 53 to 69. We commented last year that the region's technology focused entrepreneurial base was continuing to grow and mature, affording increased early stage investment opportunities, reflected in the upsurge in deal volumes.

- There have been a number of initiatives that are designed to favourably influence the future development of the industry, including the UAE's introduction of a legal framework for venture capital funds and the continued emphasis on incubators, accelerators and governmental support across the region.
- The value of disclosed investments decreased by 25 per cent to USD 1.1 billion, owing to the drop off in the number of deals with disclosed transaction values, and may also be a reflection of the more challenging investment environment. While there were a number of significant transactions including Careem's USD350m fundraising from a range of parties including regional financial sponsors, there is no doubt that a combination of factors hindered the effective deployment of capital. Alongside economic headwinds, fund managers have commented that the divergence in price expectations between buyers and sellers of businesses has continued to be a challenge in the successful execution of transactions.
- It should be noted that the analysis shown excludes a number of transactions led by investor groups that, while not falling within the strict definition of private equity, could be considered as financial investors. A prominent example of such an investment in the year was Adeptio's USD2.35 billion investment in the Kuwaiti food group, Americana.
- There were ten disclosed transactions in the MENA region with an investment value greater than USD 25 million, compared to 14 identified in 2015, although we emphasise that these numbers are understated due to the unwillingness of some fund managers to disclose transaction values.
- As we discuss in more detail below, investment activity in 2016 was more concentrated in the UAE than in prior years.

3.2.1 Investment activity by value

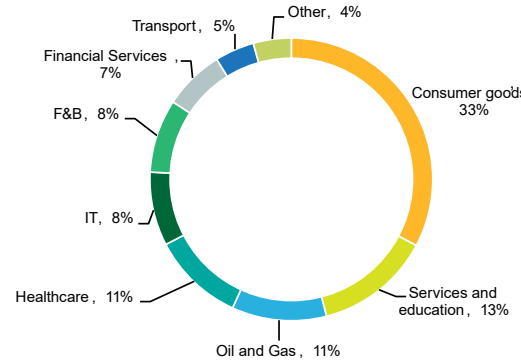
- As evidenced by executed transaction data, investment sentiment continues to favour consumer driven sectors such as retail, healthcare and F&B. This is a trend that was forecast last year and we expect no major shift in the coming twelve months.
- Education related businesses are also popular but opportunities to find assets that meet private equity's investing criteria appear to be more scarce than in these other sectors.
- Both healthcare and education remain areas of particular focus although this has made deals in these sectors often intensely competitive and thus pricing from the investors' perspective has sometimes been viewed as challenging.
- Given the challenge in finding attractive assets at suitable valuations, GPs have expressed their broad desire to remain opportunistic and will consider investing in a wider range of sectors.
- Transport was the largest sector in terms of investment value in 2016. This was largely driven by the USD350m investment in Careem.
- Investments in the oil and gas sector continued to dwindle, with financial sponsors reluctant to commit capital while price volatility and uncertainty remained major factors. Understandably, GPs have expressed their ongoing interest in the sector and related support services and it is likely to be a matter of timing before investments resume.

Investment value by sector in 2016



Source: Thomson Reuters and Deloitte

Investment value by sector in 2015



Source: Thomson Reuters and Deloitte

3.2.2 Investment activity by volume

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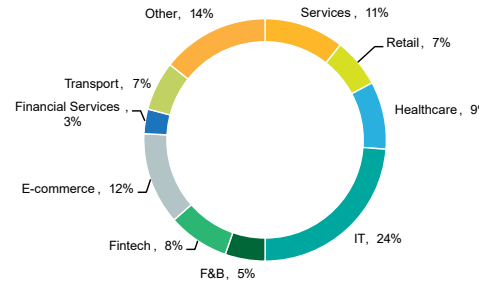
Investment volume by sector in 2016



Source: Thomson Reuters and Deloitte

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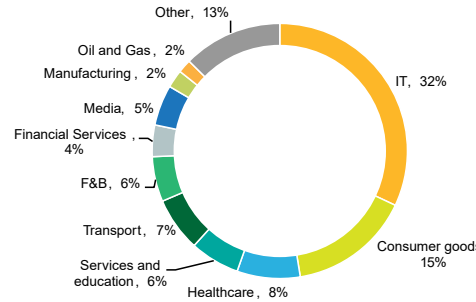
Investment volume by sector in 2015



Source: Thomson Reuters and Deloitte

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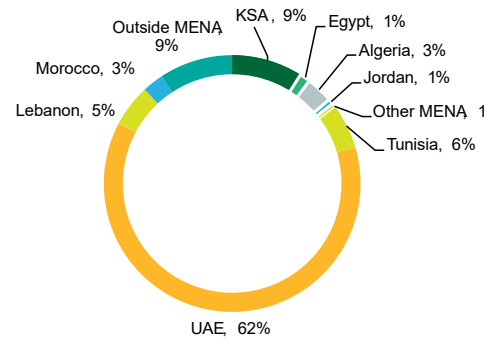
interest in the sector and related support services and it is likely to be a matter of timing before investments resume.

3.2.3 Investment activity by region

- The UAE attracted 62% of MENA investment activity by value in 2016, a substantial increase from 2015. This was a year in which private equity increasingly viewed the UAE as the most attractive MENA market in the short term in regards to stability and availability of large and quality assets. More uncertain market conditions in other GCC markets attracted fund managers more towards investing in the UAE and adopting a wait and see approach with other countries.

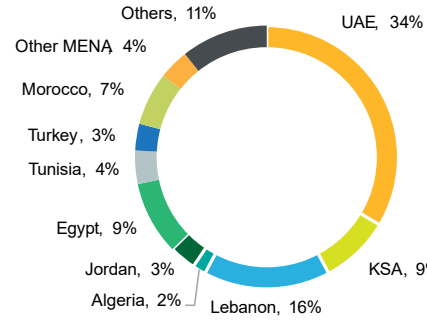
Investment value by region in 2016



Source: Thomson Reuters and Deloitte

- KSA witnessed a considerable decrease in deal value and volume in 2016 driven by the persistency in low oil prices and uncertainty regarding the impact of regulatory and fiscal reform. A number of investors commented that this makes the forecasting of a potential investee's future results more difficult resulting in a lower level of deals in the Kingdom.

Investment volume by region in 2016



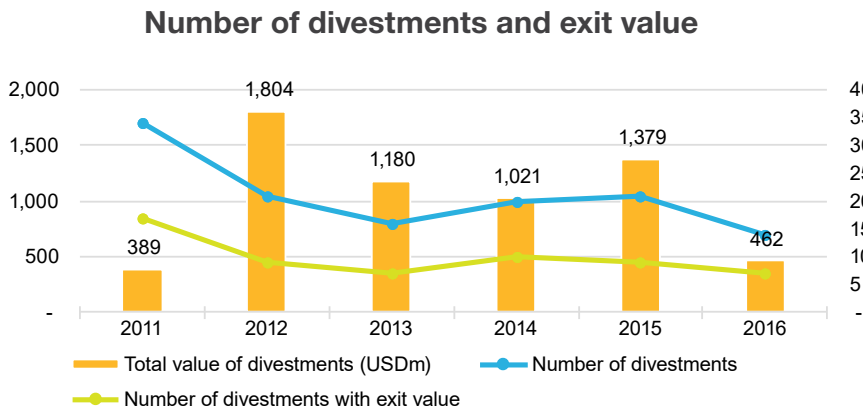
Source: Thomson Reuters and Deloitte

- Egypt experienced a fall in investment activity levels in 2016, which was anticipated given foreign exchange instability and political factors. It is early to assess the full impact of the float of the currency in November 2016 but Egypt will remain a market that investors have strong desire to access, should conditions prove suitable.
- In terms of volume of deals, UAE was also the largest market in 2016 whilst Lebanon transaction volumes reflect the country's active venture capital industry.

SUMMARY:

- The continued low level of oil and gas related transactions was in line with expectations of fund managers as reflected in last year's report, as the decline in oil prices has largely led private equity investors to steer clear of the sector for the time being.
- The largest number of transactions by volume was once again in the technology sector, reflecting venture capital's focus on entrepreneurial, technology driven businesses. The growth in volume terms of technology deals therefore results from the overall significant growth in venture capital transactions.
- Deal trends in 2016 are expected to continue in 2017, with fund managers continuing to indicate a strong preference for consumer driven, defensive sectors.

3.3 Divestments



Note: PE divestment values not provided were estimated at original deal values
Source: Thomson Reuters and Deloitte

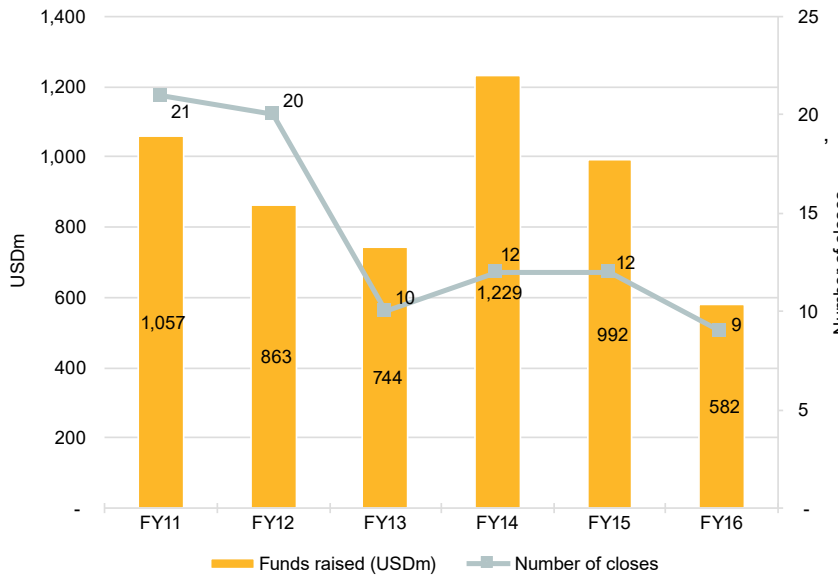
- As in 2014 and 2015, divestments remained a major focus for portfolio managers in 2016, with GPs being under pressure to monetise returns on assets held in vintage funds from pre-crisis years.
- However, exits have proved to be difficult as lengthy holding periods and the slow down in recent years may have depressed IRRs on portfolio investments. Whilst this may encourage further extension to the holding period to allow time for recovery, current growth levels may still not be adequate to regain returns to levels initially forecast.
- The difficulty of effecting attractive exits in 2016 is evident from the lack of available information regarding exit valuations, which may be an indication of exit prices being below target. However, as in previous years the limitations of the data set mean caution must be exercised when drawing conclusions regarding exit trends.
- The extension of 2016 market conditions into 2017 and the continued gap between buyer valuations and target IRRs from sellers indicate that exits that satisfy fund managers are expected to remain challenging in 2017.

SUMMARY:

- Divestment values decreased from USD1,379m to USD462m and volumes from 21 to 14.
- As with previous periods the data set does not reflect all divestments as a number of exits are either not announced or when disclosed do not include deal values.

3.4 Funds

3.4.1 Funds raised

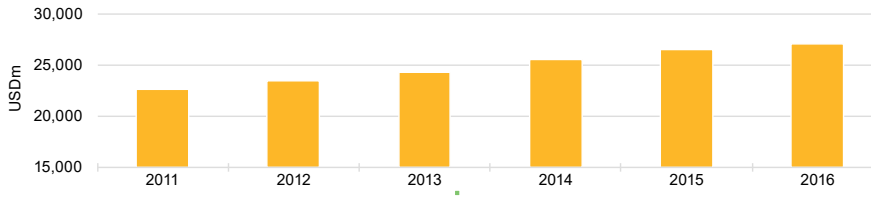


Source: Thomson Reuters

- The underlying trend continues to be that funds are raised by the major industry players with a confirmed track record who are able to continue to attract investors to the blind pool concept with 2016 appearing to be the most challenging year since 2011 in terms of fund raising and closes.
- In 2016, seven funds were raised, number of closes declined to nine and funds raised were at a low of USD582 million.

- Fund raising in the region remains a major challenge faced by GPs. The main causes continue to be a combination of economic slowdown, external views on geopolitical factors and the inability of some players to exit and recognise profits for investors on vintage funds.
- The above factors have led to deal by deal arrangements remaining in favour with GPs exploring alternative fund raising solutions including co-investment options.

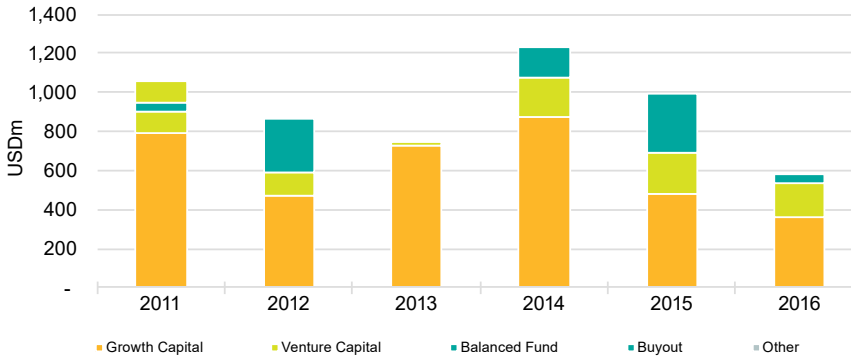
3.4.2 Cumulative funds under management since 2000



Source: Thomson Reuters

- Cumulative funds under management increased to USD 27 billion in 2016.
- In 2016 four funds disclosed closes in excess of USD 50 million compared to five in 2015. Two funds were raised in excess of USD 100 million, compared to three in 2015.
- The largest MENA focused fund raised was the Gulf Capital's USD 250 million Gulf Credit Opportunities Fund II, a mid market focused debt fund. Other major funds raised included the USD 110 million NBK Mezzanine Fund also focused on providing credit solutions for investee companies.
- Five out of seven of the funds raised were announced and raised within 2016 in comparison to 2015 with four funds announced and closed.

3.4.3 Funds raised by type



Source: Thomson Reuters

- Growth capital remains the main focus of fund managers. However, some funds classified as growth capital will consider investments where there is a buyout element.
- The Gulf Credit Opportunities Fund II and NBK Capital Mezzanine Fund II are both classified as growth capital in this analysis.
- As in previous years, the dominance of growth capital can be seen as a result of the target of PE firms in the region to increase value from growing the business and profits rather than the use of leverage which is a reflection of an emerging market where returns are predominately measured by earnings growth as opposed to leverage.
- To grow businesses, PE firms tend to be extensively involved in providing support through direct involvement and additional resources.
- Venture capital fund raising levels have witnessed a slowdown compared to 2014 and 2015 levels that were the highest since 2008. Given the increasing focus on venture capital in the region this trend is somewhat surprising but reflects the broader short term fund raising challenges faced by alternative asset managers. We also caution that, as with private equity, not all investments are being made through the “blind pool” structures that are captured in this survey.

SUMMARY:

- Fund raising in the region remains one of the major challenges faced by market participants. The combination of economic headwinds, external views on geopolitical factors and the absence of a lengthy track record for some players have combined
- As a result, and emphasising a trend seen in 2014 & 2015, GPs are continuing to explore alternative fund raising solutions. This reflects the increasing willingness of LPs to consider direct or co-investment options as a viable alternative to blind pool investing.
- Regional family offices are also continuing to invest directly, setting up private equity style operations to support the co-invest model, in acknowledgement of the opportunities in the region.

3.5 Healthcare supply-demand gap draws investors to the MENA Region

By Dr Helmut Schuehsler,

Chairman and CEO of TVM Capital Healthcare, discusses the growth of companies that are addressing the supply-demand gap in MENA healthcare

The rapid growth of healthcare across the MENA region and other emerging markets is offsetting slower growth in North America and Western Europe, drawing investors to make shrewd investments that address health service capacity gaps and improve quality of care and access for patients.

The growth has been particularly fast across the GCC, where a supply-demand gap for hospital beds, doctors and nurses has risen from a growing and aging population, the rising prevalence of chronic diseases, and a growing number of high-income households. Healthcare spending has increased significantly across the GCC in recent years, with a five-year compound annual growth rate of 11 percent (2010–14).

Despite this, public expenditure as a percentage of GDP lags the developed world by a significant margin. GCC governments increasingly rely on the private sector to help meet rising demand for health services and transfer the burden of healthcare costs, especially in the wake of oil and gas prize squeezes.

To support this shift toward privatisation, some Gulf countries have introduced mandatory health insurance, a move that has ushered in an era of rapid growth for private care facilities, significantly increasing the private sector's share of health infrastructure capacity and health services utilization.The most recent push towards privatization of parts of the Saudi healthcare system is a testament to this overall trend.

As a result, over the next five-to-ten years private investment in the sector, and medical cities in the GCC will boom, fueled by large healthcare agglomerations by private players across the region and consolidations between SMEs and large hospitals looking to reach public listing size thresholds. The region will also become an increasingly important hub for medical tourism.

This growth will be accentuated by increased focus on tackling non-communicable diseases such as stroke, diabetes, and cancer, which are rising in prominence due to changing demographics and lifestyle patterns. Holistic models focusing on prevention and treatment are already bringing healthcare into the home and other personalized environments outside of hospitals to focus on these diseases.

We will also see increased demand for high-tech pharmaceuticals and medical technology, much of which is not yet available in local markets, as a result of real income growth. Private healthcare companies will be looking to adopt new

technologies in the information technology, emergency response, and mobile health spaces to improve patient interaction and monitoring, and access to information and advice.

Growing costs for state-of-the art equipment mean that demand for high-tech products and treatments will need to be met with higher efficiency business models.

Meanwhile rapidly evolving regulatory environments across the GCC can create inherent risks for investors due to a certain lack of predictibility and licensing timelines. Markedly different healthcare systems across the region further increase country-by-country risks of tailoring a private care business model exactly to fit the local requirement and regulatory environment.

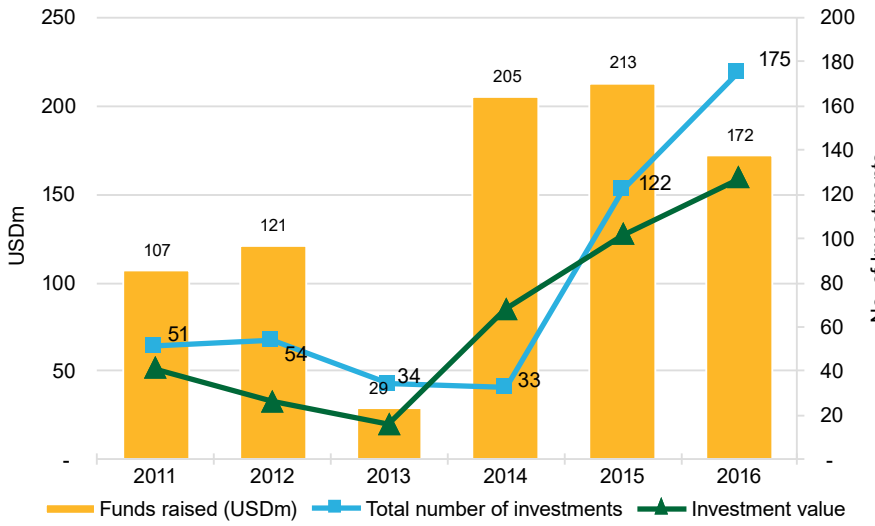
Companies that are close to regulatory authorities and remain aligned with the various licencing rules and reimbursement systems will be able to adapt to changes as they come. Additionally, natural hedges against these risks can be developed through strong analytical capabilities and country networks, flawless execution on licensing needs, and an overall realistic view on timelines. As such, emerging market investors need to be very realistic about the speed of execution in these challenging environments, and focus on how they can add value to a company's operations. And that means it often pays to be a specialist – to use deep sector expertise, to promote efficiency and good governance, as well as to create new business opportunities from own research and sector knowledge.

At TVM Capital Healthcare, for example, we are committed to running a strong "operations group" steeped in healthcare expertise – an accelerator and advisory company that supports our growing businesses. It provides general management support including the provision of strategy development, interim management, as well as a host of back office services, such as legal, information technology, marketing, accounting, human resources. Setting up this ecosystem is a significant investment in itself. But it brings huge benefits for the companies we invest in, provides a platform for exchange of ideas and developments across the portfolio, and reduces risk for the companies and our co-investment partners.

We continue to find opportunity in scalable service busineses that address expanding medical needs with a technological advantage or a specialized workforce. Investors need to look for high operating margins, low-to-mid capex requirements, and clear and transparent reimbursement schemes with accepted private pay or co-pay mechanisms. Beyond this, life science companies offering medical products across pharma, device or diagnostics, healthcare IT services that provide software solutions and mobile health services will continue to provide good investment opportunities.

4. Venture Capital in The MENA Region

4.1 VC Investments and deals activity



Source: Thomson Reuters and Deloitte

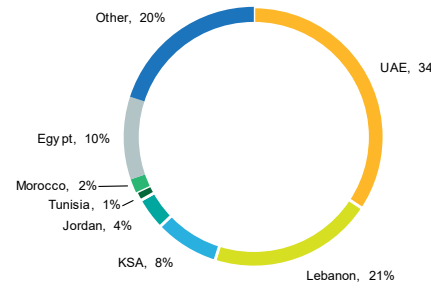
- 2016 saw the continued development of venture capital as an asset class in the MENA region. We commented last year that the growth in transaction activity might be a reflection of fuller disclosure by VCs in addition to an encouraging trend for the sector and it is clear from the 2016 results that the theme of a developing asset class has been sustained.
- Number of investments: 175
- Investment value: USD 127 million
- Total funds raised: USD 172 million

- There were a number of significant transactions in the year for venture capital backed businesses. Careem, the UAE headquartered regional provider of transportation solutions, followed its USD60m fund raise in 2015 with a USD350m round in 2016. The Careem fund raise in 2016 was categorized as a PE investment given the profile of investors.
- The macro environment offers support for the industry. Global trends in ecommerce, developments in Fintech and other disruptive technologies including the move towards a more cashless economy are combining to drive entrepreneurship and while region has lagged developed economies in this regard there is a recognition that this now offers a major opportunity for entrepreneurs and investors alike.
- Fund raising levels declined from 2015, in part reflecting overall short term investor outlook on the region. However, given the levels of VC investment activity and positive sentiment regarding the asset class it will be of interest to see if this trend can be reversed in the coming periods.

4.2 VC investments by region

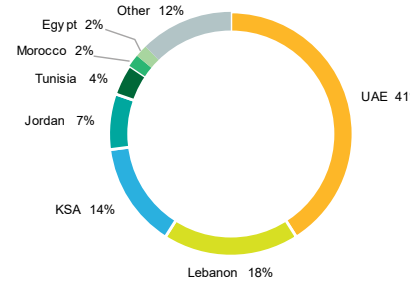
- The UAE once again saw the highest levels of VC activity in the region, with overall investment destinations similar to those seen in 2015. There is an evident theme that the UAE, Lebanon and to a lesser extent, KSA are the major hubs for venture capital activity in the region.
- In Lebanon this continues to reflect the entrepreneurial strength of the country, one driver being the level of human capital resulting in part from a strong educational system. Support from the banking system has also helped stimulate VC activity.

VC investment volumes by region in 2016



Source: Thomson Reuters and Deloitte

VC investment volumes by region in 2015

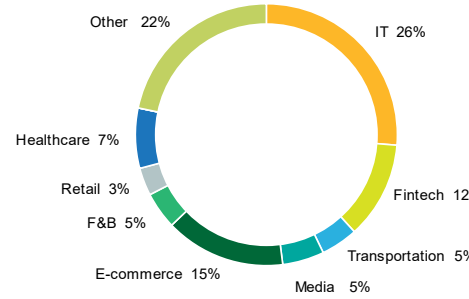


Source: Thomson Reuters and Deloitte

4.3 VC investments by sector

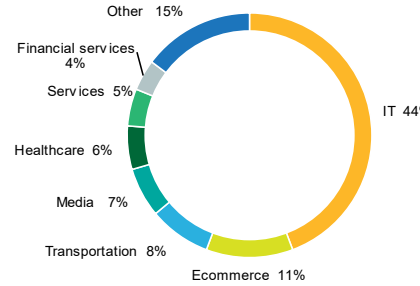
- As we would expect technology driven businesses form the major focus for venture capital investors. This trend is consistent with previous years and is further emphasised when considering that other sector investments often have a critical technology component.

VC investment volumes by sector 2016



Source: Thomson Reuters and Deloitte

VC investment volumes by sector in 2015



Source: Thomson Reuters and Deloitte

SUMMARY:

- There was extended speculation regarding the development of souq.com which was concluded in March 2017 with the announcement of its acquisition by Amazon. Regional success stories such as these are will further stimulate interest in exploring the sector from both regional and international investors.
- Burgeoning entrepreneurship is supported by a young and growing consumer market with high rates of technology adoption. The level of ecommerce penetration in the region is growing and for VC investors this is regarded as a major opportunity over the coming years. It has been estimated that the value of ecommerce in the MENA region will reach $200 billion by 2020.
- Lebanon remains an important hub with the prevalence of SMEs in the economy and support from the Lebanese Central Bank (Circular 331) have both stimulated VC activity and boosted the Lebanese startup scene, with a reported trend of Lebanese investors and entrepreneurs returning to their home country to launch startups and establish VC funds as evidence by the number of VC funds announced in 2016.
- In line with 2015 and prior years, the major areas of investment for VC practitioners have primarily been technology related, as would be expected given the nature of the industry. In addition to investments classified as IT, other sectors tend to have a critical technology component, such as ecommerce, FinTech, EduTech and HealthTech.

4.4 The Newest String to the Middle East Bow, Venture Capital…

By Philip Dowsett,

Partner - Morgan Lewis & Bockius LLP

Dubai has maintained a pedestal position as jurisdiction of choice for operating in or out of the Middle East and by virtue of this prevalence, Dubai has arguably, by default, in recent years found itself as the Middle East and North Africa (MENA) region jurisdiction of choice for the start-up and venture capital (VC) industry. Now, notwithstanding this somewhat serendipitous facet of Dubai's growth and stature as a hub of business in MENA, over the last few years Dubai has promulgated many efforts to cement this status and ensure it remains the VC centre of the Middle East. It's difficult with certainty to ascertain figures relating to start-up domiciles, but according to a recent report, the UAE leads the Middle East and North Africa region (MENA) as home to 42% of its start-ups, followed by Egypt 12%, Lebanon 9% and Jordan 8%. However, in attempts to capture a portion of this fledging market and to knock Dubai of its mantle, a number of other MENA countries have and are launching similar venture capital and fintech initiatives.

For example, in the last year, Saudi Arabia has launched ambitious plans in the country's 2030 Vision plan to depart from the notion of being an oil-dependent economy, and encouraging female participation in the workforce, which was emphasised by a Saudi wealth fund's high profile US$3.5 billion investment into a leading US tech company. Oman and Qatar have also launched venture capital funds, backed by government investment arms in an effort to encourage VC investment.

Taking a step back, the VC industry in itself is an established industry and market in the West, with VC investment in the United States last year totalling around US$58.6 billion and Europe $16 billion, which dwarfs that in MENA, which stands at around US$400 million (excluding Careem and Souq deals which are categorized as PE deals given the profile of the investors). Therefore, the MENA region is playing a challenging game of catch-up, but against the backdrop that the MENA VC industry is still in its infancy and has arguably only become an industry in itself in the MENA region within the last decade (if that, and arguably only with real traction in less than the last five), yet its progress and achievements in that period are notable.

The rise of VC in the Middle East has primarily been led by a select band of protagonists that have each, and in certain cases, all, been involved in financing rounds for the highest profile start-ups in the MENA region. This roster includes Wamda Capital, STC Ventures/Iris Capital, Middle East Venture Partners (MEVP), and BECO Capital, but which now has numerous other investors vying for a piece of the VC action in the MENA region. It's fair to say however, that this interest has, and in

the large part remains to be, from MENA-based investors, and the lure of investing in MENA start-ups has not quite yet gained mainstream interest from across the various ponds. That said, there has recently been noticeable increased interest from foreign investors into MENA-based start-ups, including Series A and B investment in Fetchr which attracted considerable interest from Silicon Valley VC firms (and recently closed a US$ 41 million Series B round), the Series A investment by Russian VC, Addventure, in Service Market (formerly movesouq), a majority European-based investment in Sprii (formerly MiniExchange), and, of course, the recent high profile buy-out of Souq by Amazon.

Thus, given the that the nature of many tech-based start-ups means that locality and operational bases are potentially flexible compared to traditional asset based businesses, and the attractive tax-free opportunity that basing an operation in a MENA country may afford, one may question why the MENA region has not attracted more start-ups. There are a number of potential explanations for this:

1. Operations in the MENA region are not without their hurdles. Although of course operating across state-lines in the US and across Europe comes with managing different laws and regulation, there are numerous synergies and similarities. However, in MENA operating across the region often involves grappling with laws and regulations that are generally more simplistic in their nature and often which have not modernised to address technology business, resulting in ambiguities and uncertainty around operations. This is coupled with often complex issues relating to foreign ownership (which differs in each country), as well as varying demographics.

2. On the ownership issue, several Gulf Cooperation Council (GCC) countries require local ownership, and this can be a struggle for foreign investors to get to grips with. On the positive side, several such countries have “freezones” affording 100% foreign ownership which circumvents this concern (although sometimes, and depending on operations, an “onshore” subsidiary may be required).

3. We need a Unicorn (or two)… In the same way proof of concept is often vital in a start-up, MENA needs those headline grabbing deals and exits to legitimise its standing. And with the Souq exit and the recent US$100 million investment by STC in Careem (the “MENA Uber”) creating a paper Unicorn, this is getting there.

4. The cost issue. Setting up in the GCC can be notable more expensive than doing so in Europe and the United States. However, there more cost efficient options, including establishing in Egypt, Jordan or Lebanon which are cheaper to set-up and have start-up culture.

5. Geopolitics and negative press. Unfortunately, one thing holding back investment in MENA (on many fronts), are negative headlines which have, in the past, had the tendency to overshadow the many successes, growth, and increased stability throughout much of the MENA region.

The MENA region is not Silicon Valley. One of the further challenges as a start-up in the MENA region is the lack of transparency over financing terms and investment criteria, as well as the difficulty in obtaining information on potential suitors for investment, as compared to considerably greater flow of information in the more developed Western world. Part of this is due to the more limited number of deals, meaning benchmarking terms is more difficult, but there is also no real access to the same reports or insight into financing terms that can be at the hands of start-ups in the US and Europe. The MENA Private Equity Association has sought to redress this and provide more visibility on structures, terms and investors, and despite movement, information and comparatives are still difficult to obtain. Consequently, VC investors are potentially in a stronger negotiating position in the MENA region than outside of MENA and the luxury of term-sheet shopping as a start-up in MENA is generally rare, and, arguably, the investors hold most of the cards.

On the positive side, notwithstanding the infancy of VC in the MENA region, many of the principals working for the leading VC firms in the region are sophisticated and seasoned, and with the advent and maturing of the VC industry in the MENA region, these individuals and firms have endeavoured to adopt best international practices and proper documentation to ensure that even if by size the MENA region is playing catching up, at least it can compete from a sophistication perspective and operate on these standards.

Ultimately however, the VC industry is quickly becoming an industry in its own right in MENA and is a key focus for many of the jurisdictions looking to move away from the legacy dependency on oil and create alternative means of wealth and income. Concerted efforts have been made by a number of the MENA governments to foster entrepreneurial spirit and accommodate start-ups, from the launch of incubators and accelerators, to accommodating 100% foreign ownership structures, coupled tax-free regimes. With proven increasing interest from non-MENA VC firms into MENA start-ups and off the back of the Souq acquisition and Careem, the paper-Unicorn, more and more eyes from the international stage are on the MENA VC industry. Based on the last few years and the determined, albeit ambitious, plans of various governments, the MENA region is seemingly positioning itself well capture its own share of the global VC market and it will be increasingly interesting to see if anyone can topple, or at least start to unbalance, Dubai off its current pedestal as the home of MENA VC.

5. DIFC: The Centre for Development

Salmaan Jaffery,

Chief Business Development Officer, DIFC Authority

In last year's edition of the MENA Private Equity & Venture Capital Report, we discussed the inevitability of change. Specifically, how 'global change' creates genuine opportunities for regional businesses. The last 12 months have been no different. While the industry has continued to face pressure due to lower oil prices, there is still an abundance of opportunity to deploy capital into attractive companies.

As a leading international financial centre, DIFC is responsible for ensuring that the operating environment supports the financial services industry. Doing that doesn't mean simply responding to change – it means we must look ahead and anticipate change. This is imperative for us to maintain our position as pioneers in the regional financial services sector.

Market developments

More broadly, DIFC understands the importance of building on its existing strengths, yet engaging new markets, especially in the area of alternative investments.

The Indian asset management industry is a great example of a new market opportunity. Key regulatory reform is fundamentally affecting how Indian asset managers raise foreign capital, and many are reconsidering where they structure their funds.

Recent changes to the India-Mauritius tax treaty, the implementation of domestic General Anti-Avoidance Regulation and Place of Effective Management rules, mean that asset managers are having to think longer and harder about future-proofing their fund structures.

In the future there will be a greater emphasis of funds and fund managers being in the same location. Given our proximity to India, our strong NRI population, accommodative regulation and deep regional asset pools, DIFC is seeing significantly increased interest from the Indian market.

We continue to proactively engage with Indian asset managers via targeted meetings and partnerships with groups such as the Indian Venture Capital Association. Additionally, we recently brought several India-based fund advisers to Dubai for them to understand and appreciate how DIFC can support their asset management clients.

Africa is another market opportunity with tremendous investment growth potential. The population is growing, private capital is available and innovation is booming.

However, Africa faces headwinds. When viewed from a global perspective, Africa is often regarded as vulnerable to corruption, misappropriation of funds and political risk. These challenges afford DIFC a real opportunity due to its proximity to the region, logistical connectivity through Dubai International Airport and its robust governance framework, which provides confidence to international investors.

Closer to home, the Middle East has always been a hot-bed of entrepreneurship and innovation. We are seeing experienced and start-up fund managers acquiring licenses in DIFC to take advantage of the vibrancy and opportunity across the region.

Strategic developments

Over the course of the last year, DIFC has seen a number of strategic developments. In September 2016, the DIFC Authority approved a new regime for the establishment of Intermediate Special Purpose Vehicles ("ISPVs"), complementing the existing Special Purpose Company ("SPC") structure. ISPVs allow fund managers, regional companies, family businesses and other corporate groups with an existing presence in DIFC to use the Centre to establish intermediate holding companies. For fund managers, ISPVs can be used to ring-fence assets and liabilities from other fund structures within the same company group. Both ISPV and SPC structures support a broad spectrum of industry sectors including transport, education and energy. There has been tremendous recent growth in this area, and the number of ISPVs and SPCs currently exceeds 200.

The first half of 2017 also saw DIFC sign two ground-breaking Memoranda of Understanding, with the Dubai Economy and Dubai Land Department (DLD). The agreement with Dubai Economy will allow companies operating in the Centre to obtain licenses to operate in mainland Dubai, while the strategic collaboration with DLD will simplify the land owner registration process with DLD for DIFC-based entities.

Earlier this year, the DIFC Wealth Management Working Group presented a Report underlining the importance of DIFC in becoming a regional hub for family businesses and offices. Family businesses are the source of 60% of GDP and an employer of over 80% of the workforce in Middle East economies. The study was based on an extensive consultation process, during which a number of areas were explored, including trusts; foundations; Sharia'a compliance; DIFC entities and structures outside the Centre. The

outputs from the study are currently being implemented to strengthen our position and establish DIFC as the ideal place to structure a family business or a family office.

Our growth plans have not ignored the crucial role of innovation. We launched FinTech Hive at DIFC earlier this year. The accelerator will encourage innovation and the development of cutting-edge financial services technology, while providing a platform that brings financial and technology firms together.

Regulatory developments

As the Centre's independent regulator, the Dubai Financial Services Authority (DFSA) is a key component of the overall DIFC proposition. In January 2017, the DFSA's regulatory framework for central counterparties (CCPs) was classified as equivalent to that of the European Union. The determination, made by the European Commission, acknowledged the work undertaken by the DFSA to instil internationally-recognised best practices, including a robust framework that promotes financial stability through a reduction in systemic risk. The distinction will encourage cross-border activity between European clearing members and CCPs located in the DIFC by reducing the regulatory burden to participate in the market.

This development is evidence of the DFSA's commitment to implementing a regulatory framework for DIFC that is in line with international standards set out under the Principles for Financial Market Infrastructures issued by the International Organisation of Securities Commissions. In so doing, the DIFC continues to cement its position as the leading hub for international financial services in the region.

In February 2017, the DFSA announced a reduction in base capital requirements for managers of DIFC funds from $500,000 to $70,000 for Qualified Investor Funds and Exempt Funds. Meanwhile, the requirement for Public Funds was reduced from $500,000 to $140,000. This makes DIFC a much more attractive jurisdiction to register funds, especially for smaller asset managers.

As DIFC continues to take the necessary steps to respond to major developments in the industry, it is important to remember that the main things we stand for haven't changed. DIFC still provides the leading funds jurisdiction in the region and we allow for rapid speed to market with a globally recognized regulatory regime. We still allow 100% foreign ownership and 100% capital repatriation, while corporation tax is still at 0%. And we have the only 'tested' common law legal jurisdiction in the entire region.

6. Confidence Survey

Deloitte and the MENA Private Equity Association are pleased to present their survey of confidence levels within the regional private equity industry. The survey addresses the key issues facing fund managers and acts as a barometer for changing attitudes

6.1 Survey of General Partners (GP's) in the MENA Region

The survey focuses on GPs in the MENA region. The aim of the survey was to obtain a greater understanding of the sentiments of the MENA region's PE industry from the perspective of GPs.

METHODOLOGY

The survey was prepared by Deloitte and was conducted in a series of face to face meetings and teleconferences in the first and second quarters of 2017. Participating firms had investments in a range of industries across a wide geographical area.

SCOPE OF THE SURVEY

The survey briefly examines the impact of the fall in oil prices and the associated economic impact has had a significant impact on investor attitudes. Over the past 12 months the belief has developed that the current market situation is the "new normal" and PE houses are adapting their strategy accordingly. Reflecting the adaptation, the majority of respondents believe investment activity will at least remain the same or improve over the coming twelve months

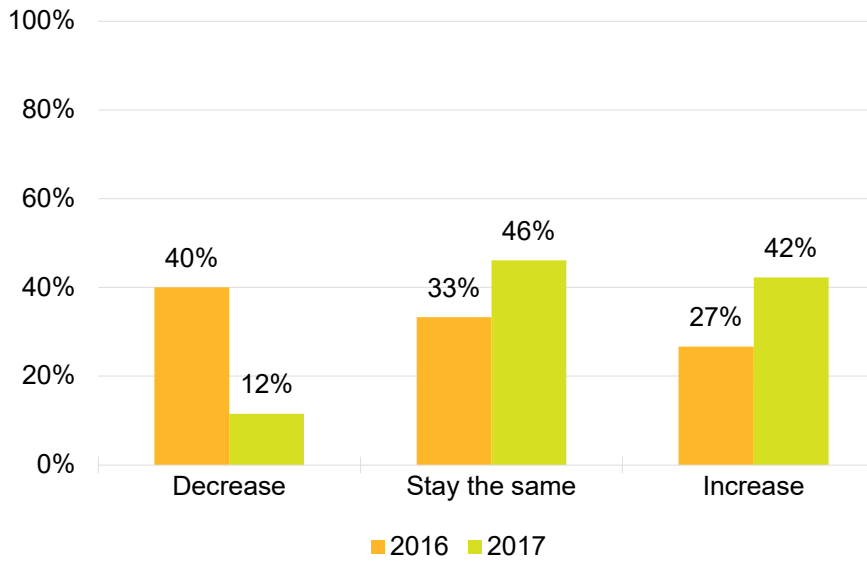
6.2 INVESTMENT ACTIVITY

Deloitte and the MENA Private Equity Association are pleased to present their survey of confidence levels within the regional private equity industry. The survey addresses the key issues facing fund managers and acts as a barometer for changing attitudes.

The fall in oil prices and the associated economic impact has had a significant impact on investor attitudes. Over the past 12 months the belief has developed that the current market situation is the "new normal" and PE houses are adapting their strategy accordingly. Reflecting the adaptation, the majority of respondents believe investment activity will at least remain the same or improve over the coming twelve months

INVESTMENT ACTIVITY

Over the next 12 months, what do you expect to happen to investment activity in the MENA private equity market?



"A number of funds were raised over the last few years and are ready to be deployed. Seller price expectations are becoming more realistic and this should drive activity levels"

"Family offices that were not willing to sell are now willing to in order to diversify by investing their money outside MENA."

"Valuations are getting better – they are still high but not so unacceptable."

"The decline in oil prices and introduction of new regulations and taxes in the KSA market have made the market less predictable and attractive for foreign investors and driving local investors to seek investments outside of the GCC."

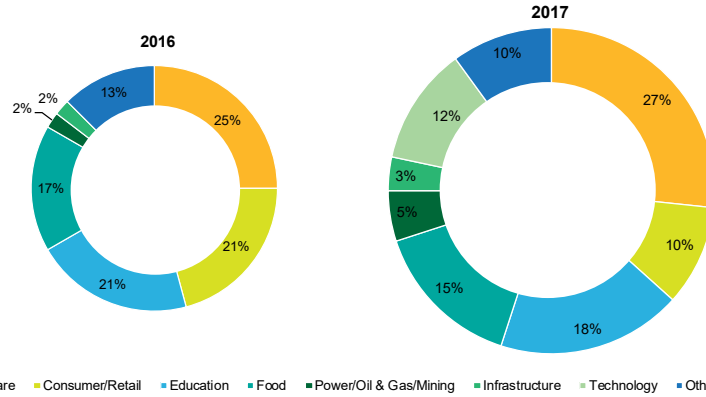
- Respondents have expressed mixed views on what they expect to happen to investment activity in the MENA private equity market over the next 12 months. However, participants are more optimistic with only 12% believing the market will decrease compared to 40% in 2016.
- There appears to be a general consensus that we have entered an era of the "new normal" where reduced growth rates are here to stay in the short to medium term. There is less consensus on the implications for deal activity levels.
- 42% of respondents believe that the market has reached its low over the last 12 months and activity will start to pick up. The driver of the increase is broadly believed to be the stabilization of oil prices and the better matching of valuations between buyers and sellers.
- The remaining 46% of respondents expect deal volumes to remain the same mainly due to ongoing economic challenges and the continued adoption of a wait and see approach.
- There was widespread agreement that any upturn would be delayed until the third and fourth quarters of the year.
- A perceived increasing focus of family groups to diversify and invest outside of the region was also noted as a key trend.

"The expected Saudi Aramco IPO is expected to increase liquidity, boost government expenditure and drive an increase in investment activity."

"Investment activity will stay the same as market conditions do not indicate any improvement. However, the quality of deals will improve."

INDUSTRY SECTORS

In which industry sectors do you expect to see most deal activity over the next 12 months?



With a continued stagnation in expected deal flow from oil & gas related businesses, GPs are looking to consumer-driven and defensive sectors for investments over the next 12 months

- Private equity firms remain opportunistic, investing in a broader range of sectors as investors consider this reduces sector specific risks.
- Given the continuation of the slow down in economic conditions, PE firms remain focused on consumer driven sectors such as retail, healthcare, F&B and education (accounting for 70% of respondent preferences), with an expected continued unwillingness to invest in the oil and gas sector given the decline of and volatility in oil prices
- In 2017 participants have shown an increased interest in the technology sector and expect to spend more time considering technology related opportunities in the next 12 months.

"We will focus on sectors that will enable us to expand and enter other geographies as moving beyond the GCC will help us generate expected PE returns."

"Stable assets remain the main area of interest for PE firms and mainly assets in the healthcare, education and F&B sectors ."

"Despite retail having suffered over the last 12 months, long term prospects remain promising and it is still a key focus sector."

"Privatisation will be an important catalyst in more non core healthcare assets being divested."

"Technology will play a big role in the PE industry especially given the overhype in education, healthcare and retail."

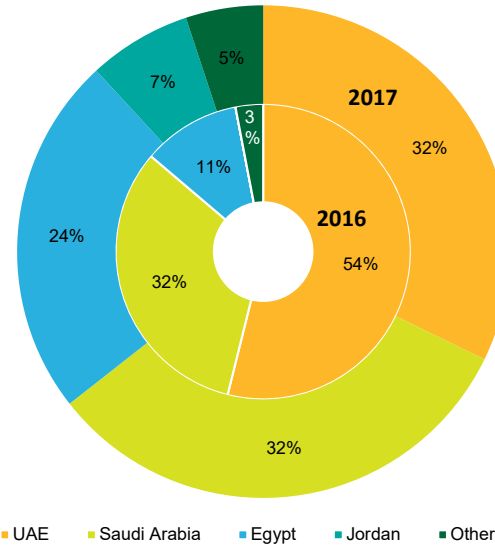
"Digital is becoming mainstream. There is no reason why MENA should be different from any other region."

"We like asset-lite businesses that are scaleable."

GEOGRAPHY

Over the next 12 months, which particular countries will see the majority of regional investment activity?

Participants continue to believe that the UAE and KSA will witness the highest level of investment activity but noted an increased interest in Egypt with market size and favourable demographics being the main driver of this interest, coupled with the perception of a more stable economic and political situation



- The UAE and KSA remain the most attractive countries for investors due to their size, favourable demographics and strong domestic economies from residual oil wealth.
- The increase in perceived political stability in Egypt and currency devaluation has resulted in a rebound in interest from investors. 24% of respondents (11% in 2016) consider Egypt a focus market. However, challenges around currency volatility and remittance of funds from the country remain a concern for investors.

- Participants this year have also expressed an increased interest in Jordan due to its favourable demographics and relative underexploitation in a region where challenges around deal flow remain an important consideration.

"Until we see an upturn in the economic situation, we will focus on the UAE as it is the easiest place to invest."

"The UAE is the easiest place to invest because of the large number of expatriate owned businesses. This means there is a natural exit for the owner at some point."

"The expected Saudi Aramco sale will boost liquidity in the KSA market and lead to an increase in investment activity."

"There are two main reasons why we see KSA and UAE as target markets – families looking for liquidity through asset sales and the impact of privatization."

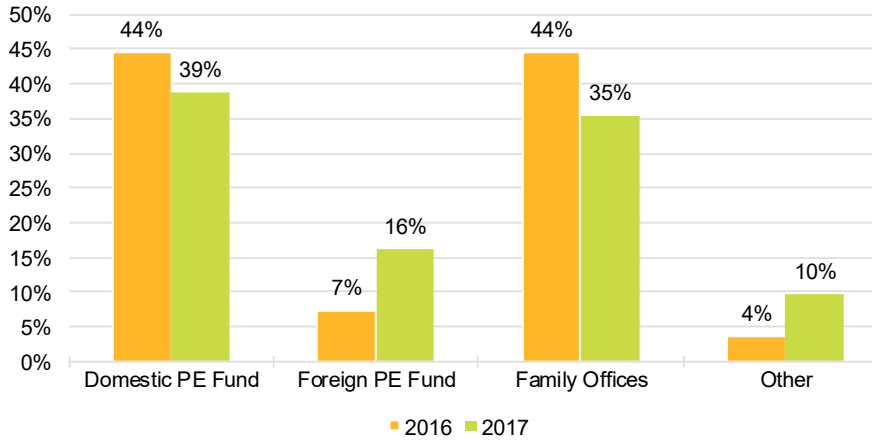
"The unpredictability in the KSA market including the lift of fuel related subsidies, introduction of taxes and fees and Saudization will discourage investors and lead to a decrease in investment activity."

"The currency devaluation in Egypt coupled with a calm in the political turmoil will play a big factor in increasing investment activity in Egypt over the next 12 months."

"The key is not where a business is based – it is the ability to take it regional."

INVESTOR TYPES

Over the next year, which types of investor do you expect to be most active in the MENA private equity market ?



The market is still expected to be dominated by domestic PE funds and family offices, as international investors are more sensitive to the geopolitical and oil related economic factors and uncertainty in legislation and tax related matters

- 74% of respondents consider domestic PE funds and family offices will be the most active investors in the region over the next year, broadly in line with 2016.
- There is a continued recognition that family offices have a desire to establish their own private equity style investing operations, albeit in many cases to look at co-investments with existing PE players. However, there is also a belief that there may be an increasing desire from family offices to look for financial investments outside the region.
- International private equity is not regarded as one of the more likely active asset classes, given relatively limited numbers of investment opportunities of adequate scale, and a greater sensitivity to a more unsettled geopolitical environment.

"Family offices are becoming bigger players in the market and some are developing PE style structures, independent from the family business."

"We think family offices will be big players. They are cash rich with a stomach for risk. Given what has happened they will not deploy in the US and they are worried about real estate in the UK."

"In the past, family offices invested through PE funds. However, the same offices are now happier looking directly at investments."

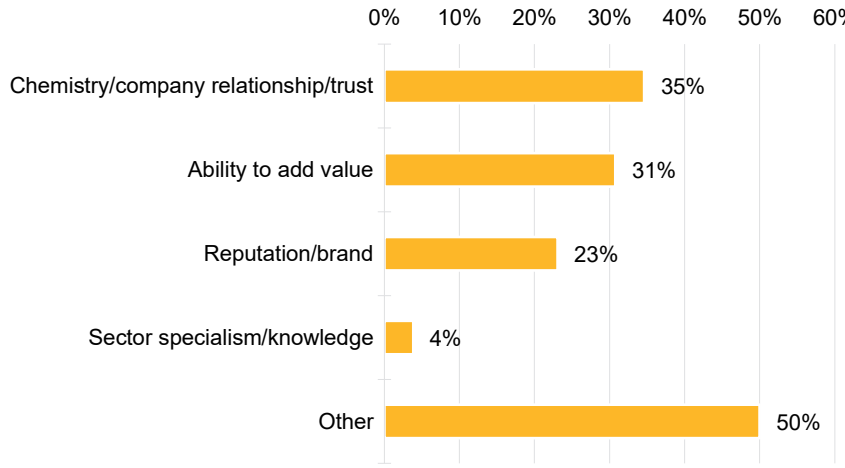
"We tend to see other regional private equity firms as our biggest competitors as we tend to find the same sort of assets attractive."

"With the current uncertainty in the region, the MENA region remains unattractive to foreign investors and particularly with plenty of opportunities for foreign investors in Europe and the US. "

"Family offices will be less active in MENA over the next 12 months as they look to diversify outside the region."

COMPETITIVE DIFFERENTIATORS

What do you believe are the most important competitive differentiators for private equity firms in the MENA market when it comes to winning deals and why?



- After price, the majority of respondents consider building strong relationships to be the most important factor when it comes to winning deals.
- Given the dominance of growth capital transactions and accordingly an ongoing relationship between buyer and seller, the ability to build strong relationships and adding value is key.
- Price is considered a less important factor in growth capital transactions but plays a bigger role when it comes to buyouts.

- The ability to demonstrate certainty of funding and deliverability of transactions along with speed of execution are also considered important factors.

"Relationships play an important role. Many deals that come round the first time often fail as buyers think they can get a better deal. The key is to maintain a good relationship with these parties."

"Aside from price, which is usually the key consideration, the ability to execute quickly, the chemistry with partners and reputation play a key role."

"Relationships are key. Sellers need to have a level of comfort and confidence in who they are dealing with."

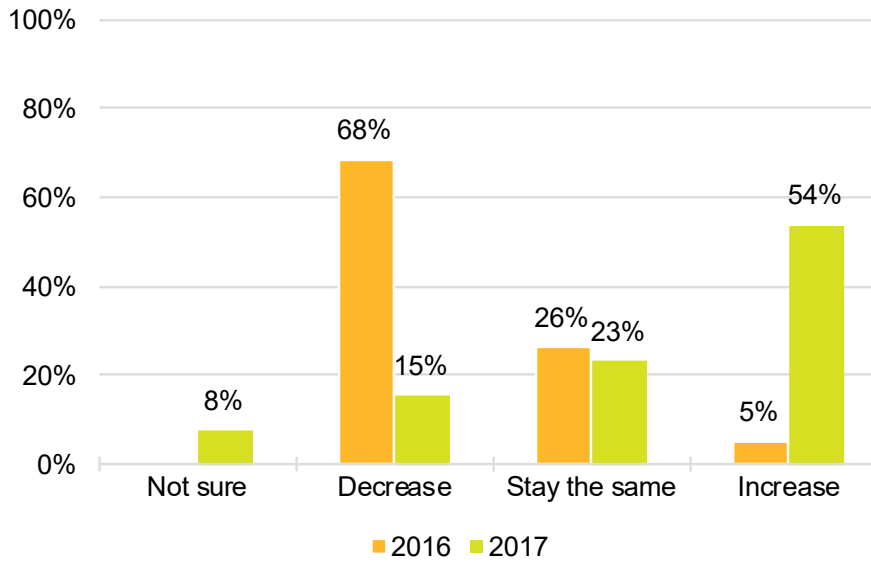
"When it comes to buyout deals, price is always the number one determining factor."

"Proprietary deals are popular in the region so building a wide network is key."

Beyond pricing, the most important factor when it comes to winning deals in the MENA region remains the ability to build a strong relationship with sellers.

EXIT ACTIVITY

Over the next 12 months, what do you expect to happen to exit activity in the MENA private equity market?



54% of respondents expect the number of exits to increase as LPs seek returns. However, respondents also acknowledge that exiting at desired returns is challenging given the slow down in the economy

- In 2017, 54% of respondents expect exit activities to increase compared to only 5% in 2016. Respondents believe the main driver of the increase is pressure from LPs to realise returns. A demonstrated track record in this area is also key for PE firms' ability to raise new funds.
- However, participants acknowledge that in the current market conditions it will be difficult to achieve desired returns, which may result in some assets being held for longer than ideal timeframes.
- Another limiting factor is the availability of exit routes. Respondents expressed some concern over current capital market conditions.

"Exit activity is expected to increase, however exiting is proving to be a challenge in the region with not many exit route options."

"I am more positive on exits than I was two years ago. If you have a good asset you can sell it."

"We expect to see more exits. The legacy assets are there."

"The economic slowdown means buying prices are on a decline. We will hold off on exiting as long as we can and focus on enhancing trading in the meantime."

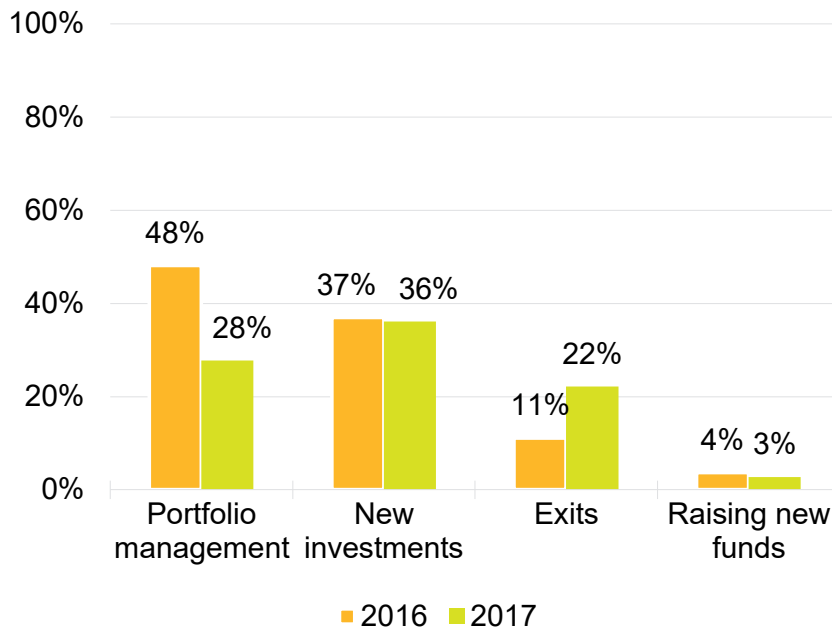
"We see exit activity remaining the same and the majority of exits pertaining to only good quality assets."

"One of the issues is that some portfolios contain minority percentage investments that are too small for strategic buyers."

"There is a higher probability of IPOs happening, but the question is where do you list."

GP TIME ALLOCATION

Over the next 12 months, which elements of your business do you expect to spend the most time on?



- New investments, portfolio management and exits are expected to be the activities GPs spend the majority of their time on.
- New investment activity will be a major focus, as there are a number of houses with funds to deploy, allied to those firms operating a deal by deal by model, who are keen to demonstrate that this model can execute transactions competitively and effectively.
- Increasing pressure on GPs to monetize returns on vintage assets is expected to increase the time spent by GPs on exits. However, in the current market conditions, exiting may be difficult at desired return levels.
- Portfolio management is also expected to be a key focus area for PE houses to ensure assets are ready to exit once the economic environment improves.
- Fund raising activities are expected to be at a low level in 2017. The key factors are that several funds were raised in 2014 and 2015, current market conditions and external caution in regards to the region.

"We plan to work closely with our portfolio companies. The basis is that we recognize the environment is not going to change in the short term and we need to focus on reducing risk."

"With our new fund in place, we have plenty of liquidity and are looking to deploy funds within the next two to three years."

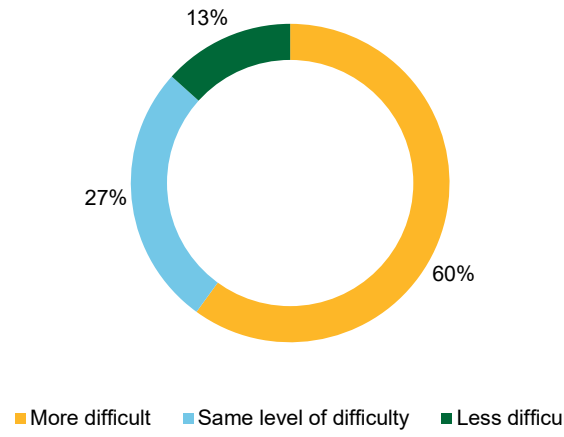
"We have structural changes taking place, therefore our focus will be on exits to remove legacy assets. However, these assets are more difficult to exit when they are minority stakes."

GPs plan to spend most of their time on new investments, managing their existing portfolio and exiting vintage assets in order to maximize returns for LPs and are expected to spend the least time on fund raising in 2017.

FUNDRAISING

Over the next 12 months, how difficult is fundraising going to be?

- 60% of participants continue to believe that fundraising is becoming more challenging.
- The drivers of this belief continue to be current market conditions and a limited number of PE houses with a track record.
- The difficulty in raising funds has given rise to more PE houses adopting deal by deal structures which is becoming a more preferred method particularly for family offices, keeping them more involved and in control of the destination of their funds.



"Fund raising is getting more difficult since family offices have less appetite to invest in the region due to not so promising market prospects. These offices have shifted their focus to outside the region."

"Fund raising remains easier for big players and extremely difficult for smaller players."

"Existing LPs are the best route to raise funds if they still trust you. Once you can demonstrate this, it is easier to go in the wider market."

"Fund raising is very difficult but the key factors are track record and having convincing vision for the fund."

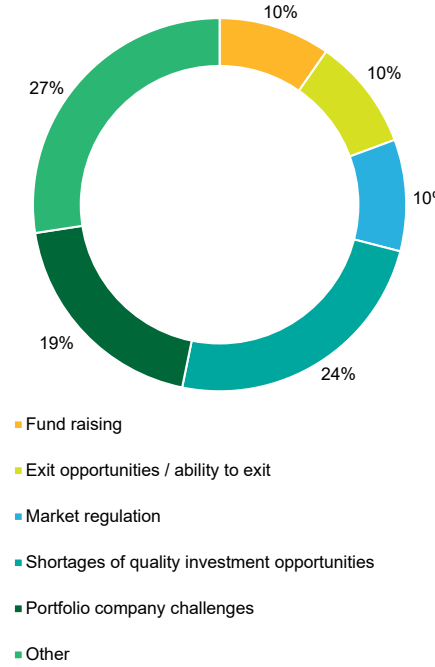
"The biggest issue is that all emerging markets are difficult right now."

With the challenging market conditions and inability of PE houses to demonstrate a track record of returns, fund raising is expected to continue to be a challenge. In addition, more houses are shifting to a deal by deal model

CHALLENGES AND BARRIERS

What do you see as the biggest challenges and barriers to growth for the MENA private equity industry to overcome?

- Overall, a wide variety of challenges were mentioned by respondents, mostly including the shortage of quality investments, portfolio company challenges and fundraising and exit difficulties highlighted earlier.
- While the market has adapted to the challenges around blind pool fund raising, the fact that difficulties in this regard are cited as a leading concern, does suggest that this is still the preferred source of capital for GPs, if achievable.
- The hurdles around exiting, including limited exit routes in the current market conditions, are also a source of some frustration.



Note: *respondents could each provide an unlimited number of challenges and barriers they think need to be overcome*

"The biggest challenge for us is the limited number of quality deals available. Pricing expectations should be less of an issue as vendors are becoming more realistic."

"It is the age old issue that there are not enough quality assets available. Families control significant element of these economies and they are still reluctant sellers."

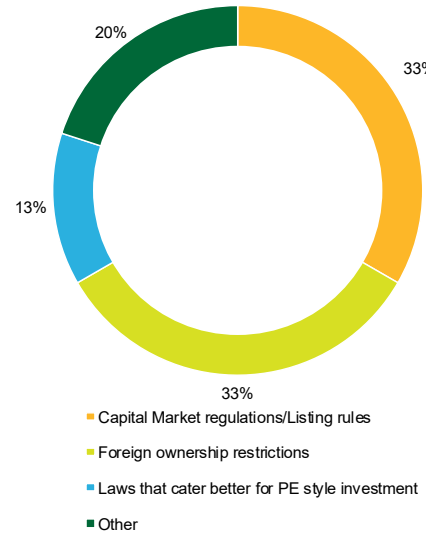
"We have assets that we need to exit but with IPOs not being an option due to the market conditions, our options are limited"

"Until the current uncertainty relating to new market and tax related regulations in the GCC and particularly in KSA are cleared, investors will look to invest outside of the region."

LEGISLATION

If you could change any element of the legislation affecting the MENA private equity market, what would it be and why?

- The biggest legislative hurdles to effective deal doing in the region challenging have remained consistent: capital market regulations and foreign ownership restrictions.
- While respondents highlighted that there are elements of legislation that could be developed or refined, other issues included the ability to enforce agreements more effectively, and the need to increase minority shareholder protection.
- Overall, however, legislations was not cited by many respondents as an area they felt to be a particular concern. In contrast, the relative legislative stability compared to other emerging markets was considered to be a potential advantage."



Note: *respondents sometimes provide a number of elements they find are affecting private equity in MENA*

"We still think there need to be changes to the capital markets rules to make listings easier."

"Foreign ownership in certain sectors in KSA remains a challenge."

"We would like to see changes in regards to ownership rules and classes of shares but low taxation and flexible labour laws more than compensate."

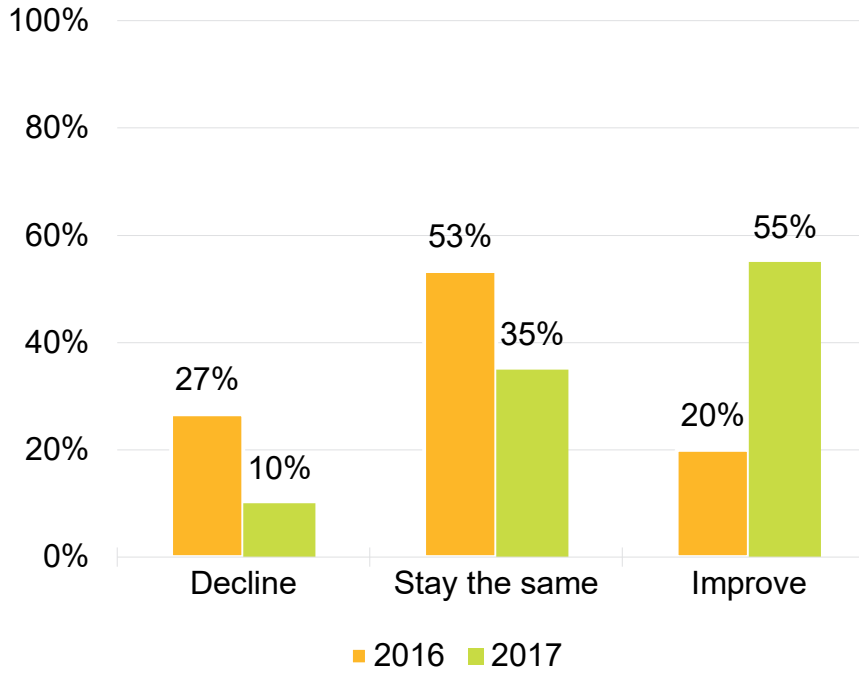
"To some extent local sponsor rules are a competitive advantage for us are they are more of a challenge for non regional investors."

"The consequences of VAT implementation are still an area of major uncertainty for us."

"I don't see legislation being a major issue when it comes to our investments."

REGIONAL ECONOMIC CLIMATE

Over the next 12 months, what do you expect to happen to the overall economic climate and why?



- This year's survey witnessed a shift in respondents' outlook on the market. 55% of respondents believe that the overall economic outlook will improve in the next twelve months. In last year's survey 82% of respondents believed the market would decline or stay the same.
- The downturn in economic conditions was evident in the last two years' surveys. The majority of respondents, however, now believe that economic conditions have reached the bottom of the cycle and we will start to see an improvement. The drivers of the upturn are: the stabilisation of oil prices and the adaptation of oil dependent states to current prices, allied to Egypt's currency devaluation.
- However, 35% of respondents still believe that there are not enough indications that the market conditions will improve over the next twelve months.

"I am optimistic that if oil prices remain stabilized and do not fall below USD50 per barrel, the pace of reforms will lead to economic growth."

"Every economy goes through a cycle and I believe we have already been through the worst of this one."

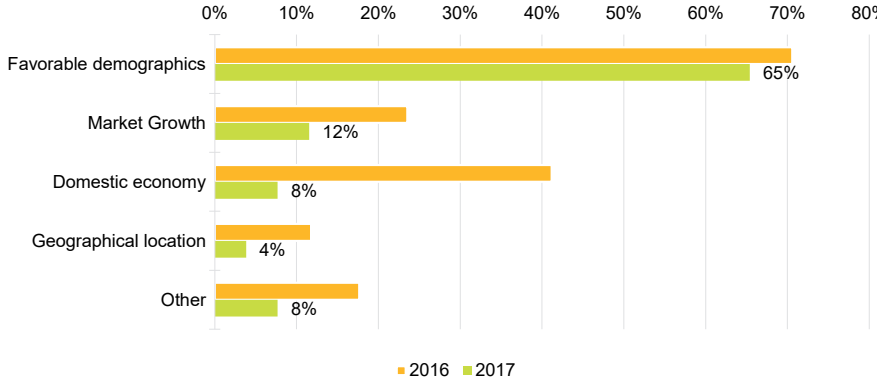
"Market conditions do not indicate any change in the next twelve months. I believe market conditions will remain the same for the time being."

"Our attitude is not one of doom and gloom but we do not see conditions improving materially."

55% of respondents expect the economic climate to improve over the next twelve months while 35% expect it to stay the same

REGIONAL STRENGTH OF MENA

What do you see as the key strengths of MENA relevant to the long-term growth of the private equity market?



Note: *respondents could each provide an unlimited number of strengths they think are most relevant for long-term growth*

- Favourable demographics continue to be seen as the key strength for the MENA private equity market
- The drop in oil prices has shifted respondents' views in earlier years of the survey from considering liquidity from wealth and oil prices to be most important strength to favourable demographics.

"The relatively fast demographic growth and young population will remain key points of attractiveness, particularly for KSA and Egypt."

"Our geographic location, demographics and our proven record of being a growth market all give me great confidence in the region."

"People had got used to an environment that was hugely consumer driven and to some extent companies benefited with rapid growth and profitability. Now people are starting to adapt which we think means more conservative valuations of businesses."

"The peg with the dollar remains a critical driver of economic stability in the region."

"There is lots of opportunity – this is not a saturated market."

"There are more pockets of opportunity in this market – a greater ability to add and extract value from companies than in developed markets."

"Governments working with the private sector and incentivising PE houses to invest are important factors in our view."

LONG-TERM CONFIDENCE

On a scale of 1-10 (10 being the highest), how confident are you in the long-term growth prospects of the MENA private equity industry?

Despite the views on the current market conditions, participants are marginally more confident of the long-term growth prospects

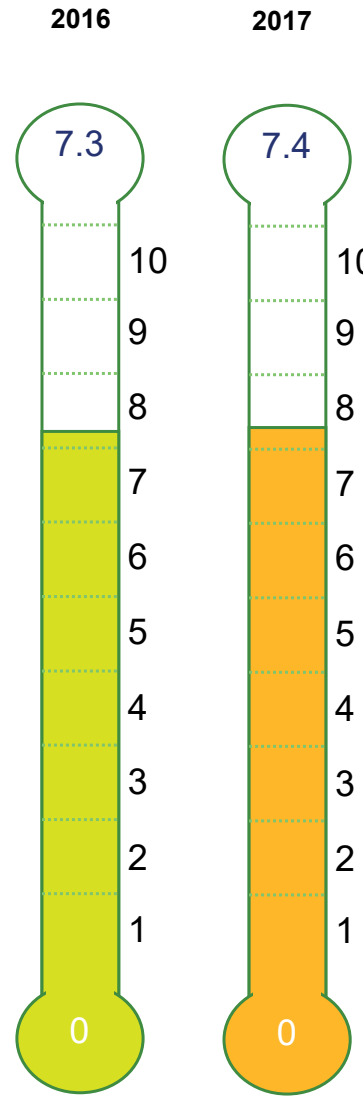
"The key is that governments are doing the right thing in respect of driving diversification and transformation."

"The GCC has first world economics and third world demographics. It is a powerful combination."

"Remember, the industry here is still at a very early stage. Private equity is just a way of raising capital and it will contninue to grow and prosper."

"The strong players will thrive and keep raising funds but the second tier may suffer."

"I am more concerned about the prospects for growth post 2022."



7. Appendix

About the MENA Private Equity and Venture Capital Association (MENA PEA)

The MENA Private Equity and Venture Capital Association (MENA PEA) is a non-profit entity dedicated to supporting the private equity (PE) and venture capital (VC) industries in the Middle East and North Africa and acts as an ecosystem enabler.

The association was established in 2010 in Dubai to support the development of a nascent private equity and venture capital industry in the MENA region. It represents the largest MENA based funds with more than US$ 30 billion in assets under management.

To further advance the interests of its members and wider industry players, the MENA PEA issues research and industry reports that highlight the PE and VC successes to local and international stakeholders.

It also hosts a number of industry discussions and workshops that bring together PE and VC fund managers, Family businesses, Limited partners, Industry practitioners, Investment Bankers, Advisors and Lawyers.

As an industry body, The MENA PEA aims at boosting the entrepreneurial ecosystem in the region and UAE in particular, and believes that moving towards innovation will foster greater economic prosperity. Because innovation occurs at the intersection of ideas and diversity of skills, cultures and backgrounds, the MENA PEA and its members have regular dialogues with every legislative body in the region through its legal task force who's aim is to petition regulators where necessary to bring about some key regulatory changes across the MENA region. These include removing barriers to capital and supporting new innovative models of equity funding.

MENA Private Equity Association

For more information, please visit our website www.menapea.com

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- Mobily Ventures
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