Rope private equity into COVID-19 fightback

It can even help in finetuning how various stimulus funds can be used to revive SMEs

Published: April 11, 2020 11:25
Taimoor Labib, Special to Gulf News

Private equity firms, with their extensive investment and portfolio management expertise, are well positioned to partner with governments in creating bespoke investment funds to select and support well managed companies.
Image Credit: Supplied

ALSO IN THIS PACKAGE

- COVID-19 outbreak hurts Italian fishermen's business
- Photos: Ugandan vendors sleep in markets to curb the spread of coronavirus
- Emirates resumes limited flights post COVID-19 suspension
- Jet on wheels! Is this the ultimate limousine?
- Coronavirus: Automotive sales plunged in March due to COVID-19

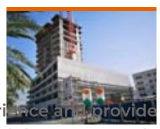
The COVID-19 crisis is having a profound and severe impact on the global economy and will continue to be a generational test for companies, shareholders and their management teams on multiple fronts.

TRENDING


Emirates to fly from Terminal 3 on April 12


UAE's Indian rupee remittances take a dive


UAE private landlords yet to relent on rent waivers


UAE contractors will need to cut project values

Businesses must ensure the safety and wellbeing of their employees while addressing burning issues that will include massive sales declines, supply chain disruptions and liquidity constraints.

Most governments have been fast to act to halt the tide of the virus through various methods while also initiating massive stimulus packages. The $2.2 trillion fiscal stimulus package is the largest in US history at 10 per cent of US GDP, with further stimulus packages expected in the near future. The UK stimulus package announced to date is at least 50 per cent higher than its Global Financial Crisis (GFC) package a decade ago and is expected to be 5-10 per cent of GDP depending on the evolution of the COVID-19 crisis.

Systemically vital

Closer to home, Saudi Arabia and the UAE Governments were very fast to respond, rightly so, and activate emergency stimulus measures to support households and small businesses in order to mitigate the impact of the COVID-19 shock. Saudi Arabia has announced a 170 billion riyal package to support the local economy, the UAE has announced a Dh256 billion package to support lenders and boost local small and medium enterprises, and Egypt has announced a 100 billion pound.

SMEs are a key pillar of our regional economies. In the UAE, for instance, SMEs constitute 98 per cent of the companies operating in the country amounting to 52 per cent of the non-oil GDP. Governments have taken the right decision by making SMEs and mid -ap companies a key beneficiary of their stimulus programmes.

In our view, the COVID-19 crisis is inherently different from the 2008 financial crisis. The 2008 GFC was predominantly a credit crisis, which had a massive spillover effect on the broader economy. Once the credit markets stabilized, the stimulus helped restore credit flows in the economy.

The 2008 recession was relatively short as the damage was more contained and did not touch everyone globally.

Targetted relief

As for the COVID-19 crisis, this started as a health crisis and is turning into a large-scale economic crisis resulting in a drastic slowdown in global economic growth and, unfortunately, will have a significant and direct impact on almost all businesses. We therefore believe that the government stimulus programmes will need to be very specific and direct in their responses (as opposed to the liquidity and credit focused measures of 2008).

The economic recovery in our region will substantially depend on the recovery and growth of SMEs who previously had solid business fundamentals and promising growth prospects but are now suffering from liquidity issues caused by the COVID-19 impact. Many companies built on unsound business models and capital structures, unfortunately, will not survive.

We believe that private equity firms, with their extensive investment and portfolio management expertise, are well positioned to partner with governments in creating bespoke investment funds to select and

[Nearly half of UAE consumers to keep shopping habits]

[Are stocks now on a path to definite recovery?]

LATEST IN

[Oil firmer on OPEC deal, equities unable to shake fears]
6 minutes ago

[COVID-19 Easter: Empty pews, live streamed Mass]
13 minutes ago

[This time don't bet all on the Fed's moves]
33 minutes ago

[Oil prices get a boost as deal finally hits the mark]
47 minutes ago

[US records 1,514 COVID-19 deaths in past 24 hours]
1 hour ago

READ MORE

COMMENT
[This time don't bet all on the Fed's moves]

[Nature of work itself is set to change]

[Are stocks now on a path to definite recovery?]

[India banks are as exposed as other sectors]

support well managed companies. The focus should be on companies with the highest potential of supporting the local economy in the medium to long term (e.g., creating the most jobs, building local expertise, and thriving businesses once the worst is behind us).

This partnership can be accomplished in a variety of ways including setting up dedicated SME focused private equity funds or through co-investment programmes.

Global IT systems are now even more vulnerable

COMMENT

Virus-racked US housing is in for a perfect storm

Go local

For governments, targeting SMEs make a lot of sense – they are locally owned, employ a large share of the workforce and are likely to create the most meaningful economic impact. However, identifying eligible small and medium businesses can be challenging and tricky.

The focus must be on supporting good quality businesses that are fundamentally sound and are impacted negatively solely due to COVID-19. Private equity firms can work closely with governments to identify suitable recipients of government investments – essentially, well-run companies with good business models that are likely to make a meaningful economic impact with the support of an equity infusion from local governments and hardcore oversight from their private equity partners.

They will need it

SMEs and mid-cap companies in our region have limited access to private capital sources as the penetration of private capital in our markets is much lower than that of developed markets. SMEs therefore seek to benefit from private equity investments as well as traditional stimulus programmes in the form of tax breaks or subsidized loans.

An equity injection into small and medium businesses will initially address solvency and capital structure concerns and will subsequently allow small businesses to fully leverage the stimulus programmes to grow and expand their operations. Whereas an additional debt burden, irrespective of whether it is subsidized or otherwise, can still lead to an unmanageable capital structure.

In addition to the financial backing, private equity investors can provide extensive leadership support in navigating crisis situations by working closely with founders and management teams to optimize liquidity, introduce key KPIs, improve capital structure, help attract senior talent, and capitalize on market share growth opportunities through accretive expansions and acquisitions.

To reinvigorate the economy out of the COVID-19 crisis, the government stimulus programmes are well intentioned and are a fantastic start. However, the specifics of how the money is deployed and in what form within the capital structure will be critical to getting the regional and global economies back on track.

Private equity can be a valuable partner in ensuring that the stimulus benefits reach the companies with best long-term viability and we stand ready to do our part in building and growing our markets.

- Taimoor Labib is a founding Partner at Affirma Capital where he is the Head of Middle East & North Africa (MENA) and Chairman of Africa Private Equity. Affirma Capital is independently owned by the former global leadership team of Standard Chartered Private Equity and manages $3.5 billion in assets in the Middle East, Africa, and Asia.