

An impressive performance

In a short span of five years, government-linked private equity firm Ekuiti Nasional Bhd (Ekuinas) managed to find 28 local mid-sized companies that have the potential to be market leaders. Its performance so far has been impressive. In this interview, Ekuinas director and CEO Datuk Abdul Rahman Ahmad talks about the journey and the future of the firm.

The Edge: Can you describe the past five years?

Datuk Abdul Rahman Ahmad: It has been an amazing journey. Ekuinas is a start-up private equity firm with a mandate to create the next generation of leading local companies. The team was built from scratch and most of us did not have prior experience in this industry, as private equity is still nascent in Malaysia.

We went through an extremely steep learning curve, and I have come to realise how difficult it is to be a new private equity investor. But with the experiences of the last five years, I hope Ekuinas will keep getting better and better.

As at August this year, Ekuinas has made 28 investments, through our direct and outsourced programme, with a total value of RM2.3 billion. This answers those who ask whether there are sufficient suitable companies in this country. It is very satisfying to have been able to find and execute deals of this magnitude among mid-sized Malaysian companies.

Why is Ekuinas investing via an outsourced programme? Why aren't investments made directly?

Our outsourced fund manager programme is where we work with private equity firms to select and grow high-potential companies. To date, we have selected seven private equity firms to work with us and they have made about nine investments on our behalf.

There are several reasons why we decided on an outsourced programme. The first is to expand the pool of capital. Our private equity partners are required to raise at least 20% of the invested capital. We provide the rest.

This approach is in line with the government's call for more public-private partnerships. Our partners have raised about RM300 million from external sources. In total, our 24 investments have deployed more than RM2.4 billion in economic capital.

We want the outsourced programme to complement our direct investments. Deals in the outsourced programme are typically smaller than our direct investment deals, which are at least RM30 million.

Since it can be very difficult for a new private equity firm to raise capital, partnering them fulfils Ekuinas' development role. The outsourced programme helps them build a track record and experience. With this, they are in a better position to attract funds from other private equity investors.

Can you describe the direct investment programme?

Direct investments refer to companies that we select and acquire an ownership stake in. The aim is to create future industry leaders by supplementing their capital and enhancing their capabilities with our involvement. As at the end of last year, we had made 15 direct investments, including APIIT Lanka and Prima Baguz Sdn Bhd.

A direct investment starts with the deal sourcing stage, where we look for companies with a lot of potential. Each company and each industry is very complex, and we execute an extremely detailed review of every potential investment. Our board of directors makes the final decision on which company to invest in. This practice is probably unique to Ekuinas since management of full-fledged private equity firms typically make their own investment decisions.

Ekuinas chose to be an active private equity fund manager. That means we get very involved in the next stage. This is the value creation stage where we work with the management of the company to grow its business value within a specific duration. This is the premise of all private equity firms.

It is a precondition that the company establishes an executive committee and meets every month. We also take a seat on the board of di-

rectors and meet every three months. But we don't run the daily operations of the company.

At this point, Ekuinas has started on the final phase for Tranche 1 of the direct investment programme — exiting our investments. This is called the crystallisation phase, as it is when we crystallise or actualise our return. It is in our mandate to exit all investments and this should address concerns about heightened government ownership among mid-sized companies.

There are three ways that we can exit — an initial public offering, a trade sale to a company that complements its operations, or by selling our stake to another private equity firm. But as a government-linked company, we don't just look at making a commercial return. It is also important that we find a rightful home for our investments when we exit. For us, it is really important that our portfolio companies continue to thrive and prosper after our exit.

Can you elaborate on Ekuinas' commercial and social objectives, and provide examples of what has been achieved?

The social objective is to enhance individual bumiputera participation in our portfolio companies. The commercial objective is to enhance institutional bumiputera equity and to make an annualised internal rate of return (IRR) of 12%.

We also have an aspirational IRR target of 20% per annum. This was the range concluded by a study, which looked at targeted returns for a private equity firm in an emerging market. As a government-linked company that operates as a commercial enterprise, we wanted to benchmark our target returns against the market.

Last year, we divested our investment in Konsortium Logistik Bhd (KLB), a company that was acquired in 2010. The net gain was RM106.4 million, which is 1.5 times the invested capital, or a gross internal rate of return of 19.4% per annum. During the period that we were invested in KLB, its workforce increased 25% to more than 1,400 employees. Here, we achieved both commercial and social objectives.

KLB was sold to KL Airport Services Sdn Bhd, a wholly-owned subsidiary of DRB-Hicom Bhd. We think DRB-Hicom, a leading bumiputera conglomerate with stakes in Pos Malaysia Bhd and Proton Holdings Bhd, is the rightful home of KLB. It has the necessary platform, resources and entrepreneurial capabilities to continue growing KLB's operations and bumiputera ownership.

Icon Offshore Bhd is another company in our portfolio that we have exited. It was our first initial public offering and it was very satisfying to have grown the company into a larger player with better values.

To measure our performance, we created closed-ended funds, as this is the standard practice among private equity firms. The Ekuinas Direct (Tranche 1) Fund, which is fully invested, made a gross portfolio return of RM655.9 million in FY2013. This is equivalent to a gross IRR of 25.5% and a net IRR of 20.4% for the year. The difference between gross and net return is the management fee. The fund is still invested and the actual return has yet to be realised.

In FY2013, Ekuinas increased bumiputera equity value among our portfolio companies by RM2.8 billion, which is 1.7 times our total invested capital. Total equity value for all shareholders of our portfolio of companies rose to 2.5 times invested capital. The challenge now is to do more of what we have done and keep improving.

Can you describe Ekuinas' position and role among other government-linked organisations that are aimed at developing Malaysian companies?

Many government-linked investment institutions already exist and we were careful to avoid overlapping functions. The private equity industry in the country is still young and largely dominated by venture capital. Organisations such as



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Mavcap [Malaysia Venture Capital Management Bhd], SME Bank, MTDC [Malaysian Technology Development Corp], Malaysia Debt Ventures Bhd typically make investments of RM1 million to RM15 million in small-scale companies. SME Corp, Biotech Corp, CRDF and Cradle Investment give grants to start-ups or to approved ideas on paper. Khazanah Nasional Bhd, 1Malaysia Development Bhd, Permodalan Nasional Bhd, the Employees Provident Fund, Lembaga Tabung Haji and other institutional investors look for large companies with established markets.

Looking at this landscape, we think the missing link is the mid-sized company. This is our focus — mid-sized companies that grow into leaders in their market and/or regional players. Our investment size is about RM50 million via our direct investment programme. Our approach is usually to take a majority stake in a company, turn it into a market leader and exit in three to five years. In contrast, venture capital investors are typically minority shareholders in a company.

Are there any advantages or disadvantages of being a government-linked private equity firm?

The goal of a private equity firm is to boost the value of its investments and then, sell them at a profit. Being a government-linked private equity firm has one advantage — the government commits capital for our investments. So, we don't have to spend time and effort on fundraising, something full-fledged private equity firms have to do.

Our investments have been in sectors such as education, services, FMCG [fast-moving consumer

goods], healthcare and F&B [food and beverage]. These are highly competitive private sectors that are not dependent on [government] contracts. At the beginning, some companies would ask us about contracts that we can bring to the table and my answer was always, 'I'm sorry but we struggle to get our own contracts'.

The business community quickly realised that we operate as a commercial private enterprise and the perception that we can provide government contracts quickly dissipated. Now, companies that we talk to at the deal-sourcing stage are aware that we come in with capital and can enhance their management team, financial discipline, systems and corporate governance.

What is the outlook for this industry and what are your plans for Ekuinas?

Our private equity industry is still young, although it has seen more participation from global private equity practitioners in the past three years. This is good, since increased competition among private equity firms bonds and supports growth of this industry and speaks about the attractiveness of the local SME [small and medium-sized enterprises] sector.

The future is to continue growing SMEs into larger companies that can compete regionally and to build a virtuous cycle in the private equity industry. Here, attractive returns draw even more capital, and this will benefit even more companies, employees and, ultimately, the country's economy.

For Ekuinas, I am looking forward to the crystallisation of more investments and reinvesting our capital. This is the cycle of a private equity firm and it is very exciting.