DETERMINANTS OF FUND MANAGERS INVESTMENT IN PRIVATE EQUITY IN KENYA

BY

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UNITED STATES INTERNATIONAL UNIVERSITY - AFRICA

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KINYUA MARVIN MWENDA

A Project Report Submitted to the Chandaria School of Business in Partial Fulfillment of the Requirement for the Degree of Masters in Business Administration (MBA)

UNITED STATES INTERNATIONAL UNIVERSITY- AFRICA

SUMMER 2019
DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University – Africa for academic credit

Signed:
____________________________________________Date:__________________

Kinyua Marvin Mwenda (ID -636544)

This proposal has been presented for examination with my approval as the appointed supervisor.

Signed:
____________________________________________Date:__________________

Prof. Amos Njuguna

Signed:
____________________________________________Date:__________________

Dean, Chandaria School of Business.
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ABSTRACT

Private equity investments have different dynamics compared to public equity. These dynamics include; transparency, management fee, value creation, target companies, fund raising, regulations and disclosure, transactions and deal volumes, exits and returns, strength and condition of local financial markets.

This study sought to investigate the factors that have an effect on the investment decision-making in private equity by fund managers in Kenya. The study sought to determine the effect of PE firm characteristics on the decision to invest in Private equity, effect of external factors impact on the decision to invest in Private equity and the strategies that can be used to enhance investment in private equity by fund managers in Kenya.

The study took a descriptive research design whereby the registered fund managers by the RBA were the identified population comprising of 22 registered fund managers. A census technique was adopted by the study. The data was analyzed using descriptive and inferential statistics in the form of Pearson’s rank correlation. The findings were then presented through bar charts and tabular formats.

Findings from the study show that the following PE firm characteristics have positive correlation with the amount invested in PE; the firm track performance record, experience of PE managers, the deal activity, types of financing strategies, value creation and the PE firm ability to fundraise. Of high importance were the value creation in invested companies, ability to fundraise, having a local presence, having a performance track record and the type of financing strategies used.

The external factors that impact on the fund managers in regard to making investments in PE are; the illiquidity factor of PE investments, trade sale as an exit strategy, return on investment of PE as an alternative investment class, number of successful recorded exits by PE firms, track record of positive returns on investment after exit in the PE ranked highly as important to the fund managers.

The study found that the establishment of a local regulatory PE body in Kenya was appreciated and strongly supported. Other statistics to enhance PE are; the development of a commitment strategy towards PE investments, the aligning of PE investments to the corporate investment strategies and the strengthening of the local financial markets.
The study concluded that PE firm characteristics and external factors have a significant impact on the investor’s decision to allocate funds towards PE investments. PE offers much benefit to institutional and wealth management clients. As such, there should be an informed awareness among these investors that the lack of transparency and regulatory restrictions are not the only factors that should be considered while investing in PE. Factors such as illiquidity of PE investments, value creation, the performance track record, trade sale as an exit strategy are also crucial to the investment decision as supported by the study.

The study recommends that research be done on other factors that are potential influences to investing in PE by other investors as the study was limited to fund managers. These factors for instance may include deal structuring between the general and limited partners, management of investments made and agency costs. The study also recommends that research be conducted on the PE firms in regard to the selection criteria that they adopt when engaging and targeting institutional investors to come on board as potential PE investors.
ACKNOWLEDGEMENT

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<tr>
<td>PE</td>
<td>Private Equity</td>
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<tr>
<td>AVCA</td>
<td>African Private Equity &amp; Venture Capital Association</td>
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<tr>
<td>EAVCA</td>
<td>East Africa Venture Capital Association</td>
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<tr>
<td>EY</td>
<td>Ernst &amp; Young</td>
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<td>SAVCA</td>
<td>South Africa Venture Capital Association</td>
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<td>RBA</td>
<td>Retirement Benefit Authority</td>
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<td>KES</td>
<td>Kenya Shilling</td>
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<td>NSSF</td>
<td>National Social Security Fund</td>
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<tr>
<td>US</td>
<td>United States</td>
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<tr>
<td>IPO</td>
<td>Initial Public Offering</td>
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<tr>
<td>LBO</td>
<td>Leverage Buyouts</td>
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<td>GPs</td>
<td>General Partners</td>
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<td>M</td>
<td>Mean</td>
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<td>SD</td>
<td>Standard deviation</td>
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<td>ROI</td>
<td>Return on Investment</td>
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<td>SME</td>
<td>Small Market Enterprise</td>
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<td>BRICs</td>
<td>Brazil, Russia, Indonesia &amp; China</td>
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background

Appelbaum and Batt (2012) refers to PE firms as financial intermediaries where the general partner (the PE firm) raises capital from financial institutions (limited partners) such as pension funds, mutual funds, insurance companies, sovereign wealth funds and wealthy individuals. The purpose then, is to obtain a portfolio of assets that generate returns or acquire company with the end goal of a profitable exit expected from the funds invested. The general partner oversees the creation of the PE fund and its investment portfolio as well as makes the decisions concerning the company such as which investment to buy, lease and its management. Additionally, a fund has life span of ten years where the first three to five years, the injected capital must be invested or else returned as uncommitted capital along with the management fee to the limited partners (Appelbaum & Batt, 2012; Malamud & Martelanc, 2013).

According to Sullivan (2017), Venture capitalist primarily aim to avail funding and business guidance to companies in the early stages of growth with the hope of achieving quick return on investment. However, Sullivan cautions that one must not confuse between PE and venture capital. He illustrates simply that venture capital firm are like companies in the home construction industry - building from scratch while PE firms are those that only specialize and buying existing homes.

The term ‘Alternative’ is used to show investments such as hedge funds and PE as other options to equities and bonds which are considered the staples of asset management (Robertson, 2017). Alternative investments captured a $ 1.28 trillion inflow of funds growth between 2009 and 2014, making them a fast growing and noticeable asset class with tremendous financial impact in the global asset management industry as reported by McKinsey (2015). Blundell-Wignall (2007) attributes the rise and success of PE to the market responses on prices and regulations which is based on rational behavior. Blundwell-Wignall lists expensive financing via equity, reduction of the ability to award managers with options and corporate governance pressures, strong corporate balance sheets that are in a search for cash yield, cheap debt funding, short-term performance pressures on fund
managers and increase in asset allocation to the alternative asset class that has increased capital as causes of this success.

The main challenge of PE players, both at an international and regional level is the establishment of a local footprint that presents a chance to develop useful local contacts, nurture relationships, achieve operational experience and develop a robust pool of investment potential partners for future business opportunities (Klonowski, 2011a). Moreover, most of the emerging markets operate in impervious external environments where corruption, a limited rule of law and violation of human freedoms and rights pave way for the investor uncertainty and risk of PE firm investments (Klonowski, 2011a). More so, to the investor, Baker, Filbeck, and Kiymaz (2015) highlight the lack of transparency, regulatory constraints and liquidity concerns faced by PE as contributing factors to their unattractiveness.

A survey done by AVCA, SAVCA, & RisCura (2014), where they interviewed 48 limited partners across four continents found that the main challenge of PE market in Africa was its relative youth which has led to there being few well experienced general partners (a 25% response rate from the LPs) coupled with a weak exit opportunities environment (a 24% response rate from the LPs). More so, political risk came in third at a 19% response rate, regulation/tax issues at 15%, lacking opportunities at 9%, high entry valuations at 6%, too competitive at 2% (AVCA et al., 2014).

According to Hasan (2014) the PE industry started experiencing major changes of exponential growth in the early 2000s due to investor focus on emerging markets (Brazil, Russia, India and China). From recent data, around 4762 companies in 2008 received PE investment while from 2008 to 2013, PE firms invested their funds of $168 billion in emerging market companies. Additionally, PE managed to get a dedicated fund commitment amount of $248 billion from limited partners (pension funds, institutional investors and wealthy individuals).

A study done by Babarinde (2012) brings into focus why the PE industry in Africa has been receiving a lot of attention. It reveals that it’s as a result of fund managers ambition and longing to diversify their portfolios outside of developed and mature markets such as Western Europe and North America. Secondly, it’s also due to the return on investment metric, in which emerging markets are outperforming developed world markets. The study
also points out that the need capital for development by the African continent will always attracts private equity investments as sources of financing as long as it’s underdeveloped.

The role of development finance institutions is diminishing as more traditional limited partners such as sovereign wealth funds and pension funds are increasing accounting for a bigger share of PE capital (Dupoux, Becker, Hammoud, & El Fihri, 2016). South Africa, Botswana, Kenya, Namibia and Nigeria have quantitative ceilings of fund allocation to PE at 10%, 5%, 10%, 1.75-3.5% and 5% respectively in regard to pension fund investment interest in them. These ceilings maybe comparatively lower compared to other asset class allocation but they signal the gradual emergence and development of PE within the African space (Ashiagbor & Vidal, 2016).

Fund managers such as those of African pension funds are affected in their ability to invest in PE owing to the size of assets under management (Ashiagbor, Satyamurthy, Casey, & Asare, 2014). Botswana has asset under management (AUM) allocation to PE at 5%, Namibia at 1.75-3.5%, Rwanda at 10%, South Africa at 10%, Tanzania at 5%. As a result of countries where AUM represent 80% (Namibia) and 40% (Botswana) of the GDP, there is mounting pressure in other countries to use the accumulated pension funds to diversify from traditional investments (government bonds and listed equities) to new alternative asset classes especially PE. However, the resistance to this pressure has been duly justified by the lack of familiarity and experience with the PE industry (Ashiagbor et al., 2014).

In 2011, Asia PE managers targeted a raise of about $160 billion through approximately 400 funds while Africa-focused firms targeted a raise of about $10 billion through 22 funds. While the difference between the two narratives is largely noticeable, it is important to note that Africa now boasts of over 100 PE firms that mainly focus on the continent exclusively or inclusively thus highlighting the growth of the PE industry on the continent. This translates into a good investment opportunity for fund managers regionally and locally from financial institutions into PE investments (Babarinde, 2012).

A report by Private Equity Africa (2017) identifies the following firms in Kenya as among the most active private equity investors in East Africa by 5-year volumes: Abraaj, Fanisi capital, Fusion capital, Old Mutual, AfricInvest, Leapfrog investments. Centum Investments and Trancentury Group are also some of the well-known PE firms in Kenya, listed and trading in the NSE. There has been an increase in the number of PE joining the Kenyan market such as the Abraaj Group, Carlyle Sub Saharan Africa Fund and Emerging
Capital Partners African Fund (Njau, 2013). Fanisi Capital had successive raising of capital from pension fund as internal investors while the International Finance Corporation came in to invest Ksh 750 million for an equity stake not exceeding 20%. The firm, Fanisi aimed at that time to raise an initial sum of up to Ksh 3 Billion from both external and internal investors, with the balance to be sought in the course of the 10 year fund. The first phase was between 2010 and 2015 where the firm raised Ksh 5 billion (Steadfast capital, 2016).

**Statement of the problem**

McPhee (2015) observes that the awareness of PE has increased in East and West Africa. This is supported by the growing number in deal volumes in South, West and East Africa. However, as these investments become active, there comes the danger of financial instability stemming from their activity as evidenced in developing countries in Asia and Latin America (Mwirigi, 2014).

Private equity are argued to be unwise investments due to the lack of perceived transparency and non-conformity or subjection to regulating markets and organized markets. The high nature of risk, illiquidity concerns and means of evaluation brings about caution in considering private equity as an alternative asset class as well (Khort, 2015).

A study on international allocation determinants of institutional investments in venture capital and PE limited partnerships found that the expected deal flow plays a crucial part in determining asset allocation and cross-examination of investments (Groh & Liechtenstein, 2011). In the same study, public subsidies as aid or support from the government were not considered as a key factor by the international investors in the decision-making process of asset allocation to PE (Kiplangat, 2013).

A survey done by Deloitte, (2016) featuring general and limited partners as respondents identifies Uganda, Kenya and Tanzania as attractive destinations for investments due to increased investment opportunities driven by government expenditure, an innovative private sector and a stable economy. In 2015, 79% of the respondents foresaw an increase in PE market activity in terms of investments while in 2016, the percentage dropped to 75% respondents having the same view. In the same study, in 2015, none of the respondents foresaw a decrease while in 2016, 5% registered a decrease in private market equity activity. This brings in the query about the negative perceptions by these respondents to what could be the cause the level of investment and market activity decline in PE which
aligns itself with the objective of this study; finding the determinants of investment in PE investors especially fund managers.

A study done by (Oluoch, 2013) recommends that there is need to fully utilize and maximize on the use of fund assets to generate returns. This can be achieved by investing in more productive investments that yield high returns such as alternative assets. Oluoch recommends the need to invest in productive asset classes that will generate income for pensioners but does not state which asset class and the factors that would determine the selection of that class. In view of the mentioned studies, the researcher seeks to investigate what propels investors especially fund managers of financial institutions in Kenya to invest in PE.

1.3 Research objective

The purpose of the study is to find out what are determinants of investments in Private equity by fund managers in Kenya.

1.4 Research questions

The study sought to answer the following questions:

1.4.1 What is the impact of PE firm characteristics on the decision to invest in Private equity by fund managers?

1.4.2 What external factors impact on the decision to invest in Private equity by fund managers?

1.4.3 What strategies can be used to enhance investment in private equity by fund managers?

1.5 Significance of the study

1.5.1 Private equity firms

The study will prove useful to PE firms as they will be able to know some of the factors that weigh heavily on the decision to invest in them by traditional institutional investors such as pension funds, endowments, foundations and Development Financial Institutions. Based on the knowledge gained they will be able to strategize and develop diverse financial models and investment instruments to address and amend any arising issue thus making them a more attractive destination for investor investments.
1.5.2 Fund Managers

The collective knowledge and insights from this study will prove useful to fund managers in terms of investment decision-making. Additionally, findings will also play a cautionary and advisory role in regard to what factors their peers consider highly in terms of investing in Private equity.

1.5.3 Academic scholars

The study will benefit academicians in regard to gaining perspective understanding on how dynamic factors in the private equity alternative class affects choice in investments, particularly those made by fund managers. It will give recommendations based on the findings that will aid in conducting further research thus contributing significant knowledge of investments made in private equity.

1.6 Scope of the study

The study focused on 22 licensed fund managers by the Retirement Board Authority (RBA) in Kenya as per 2018. RBA is the main regulator of retirement benefit schemes. The study was limited to fund managers located in Nairobi and was conducted from May to December in 2018.

1.7 Definition of Terms

1.7.1. Private Equity (PE)

Private equity (PE) is an asset class that consist of equity securities and debt in companies which are not quoted on the public exchange (Baker et al., 2015).

1.7.2 Alternative investments.

Alternatives investments can be defined as core diversifiers that are a high source of potential return. They include hedge funds, commodities, venture capital and real assets such as real estate (Hung, Onayev, & Tu, 2008).
1.7.3 Exits

An exit refers to the point in which the illiquid investments are monetized by the private equity firm and sold off (Klonowski, 2011b).

1.7.4 Fire sale

A fire sale is a rapid asset sale that occurs when illiquid assets or investments are sold off quickly by managers (Lindsey & Weisman, 2016).

1.7.5 Risk and return

Risk refers to the probability of a loss. If an asset has a high probability of incurring loss, it is then defined as a risky asset. Return, on the other hand is a measure of total gain or loss over a specified time period in an investment (Senthilnathan, 2016).

1.7.6 General Partner (GPs)

General partners are private equity firms that raise capital from endowments, insurance companies, sovereign wealth funds, wealthy individual, pension funds and mutual funds (LPs) (Appelbaum & Batt, 2012).

1.7.7 Limited Partner (LPs)

Limited partners are investors in private equity who acquire equity stakes in the PE fund or investment. They include pension funds, endowments, wealthy individuals, insurance companies, mutual funds and sovereign wealth funds (Froud & Williams, 2007).

1.7.8 Diversification.

Diversification refers to allocating an individual’s wealth to different risky assets that are not correlated in a portfolio that contains investable risky assets which holds them in different proportions (Chambers, 2010).

1.8 Chapter Summary

This chapter elaborates on the background on private equity across the globe and how investors of different caliber are making their investment strides in it. It also highlights major statistics on allocations to private equity on the continent alongside challenges that come with it. It goes further to present the statement of the problem which leads to identifying the general and specific objectives, significance and scope of the study and ends with the definition of terms. Chapter 2 discusses in detail the literature review that supports
the study while chapter three presents the research methodology used. Chapter four presents the data analysis and interpretation in which chapter five discusses and draws both the conclusion and recommendation.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter reviews in detail the scholarly work conducted by various researchers on PE and their investments. It discusses the effects of PE firm characteristics and external factors on fund manager’s decision to invest in PE. Additionally, it explores various strategies that can be used to enhance investments into PE by investors of diverse backgrounds.

2.2 Effect of PE Firm Characteristics on Fund Managers Investments

2.2.1 Experience of PE Fund Managers

PE funds are managed by PE fund managers whose managerial skill level is considered by the IFC to be a differentiating factor in the quality of a fund (Wilton, 2012). The PE firm therefore as a general partner of a particular fund through its representative fund managers then is placed on a high pedestal of experience and maturity if well versed in skill for different models in areas of corporate operations, entrepreneurial consulting, and investment banking Wilton (2012). These skills are taken to match the driver returns of growth in earnings, margin expansion, improved transparency and governance and multiple expansion due to growth or profits. Choosing of PE firms with experienced managers has therefore proved critical over time. (Wilton, 2012).

Investors need to be cautious in manager selection due to the gaps in performance that may arise when well scrutinized (Lamm & Ghaleb-Harter, 2001). This is supported by the study done by Lamm and Ghaleb-Harter (2001) which points out consistency as a top managerial attribute in excellent performance among top managers who control a high percentage of capital raised over a time period. As a result, such managers record high IRR that allows them to control a high percentage of capital raised over their industry peers.

2.2.2 A Local presence

Building and strengthening of local networks is important for PE firms due to additional benefits that they bring into a deal such as sourcing and buying, creating value and exiting. Firms that head out to new markets should ensure that they have the appropriate and robust contact base as well as reliable and sound knowledge of the local economy and its macroeconomic variables (EY & AVCA, 2013). A study conducted by EY & AVCA
shows that 48% of PE deals originated from close network relationships while a third through company and sector tracking while only 14% of these deals were brought to the PE firm. The reports additionally notes that getting to have success in Africa is dependent on getting familiar with the country, its macro story and potential company information especially for firms that have less operational experience. However, building robust networks, establishing crucial relationships, knowing management teams and sellers, having reliable insights and information of a company and the business environment are time extensive thus require proper cultivation (EY & AVCA, 2013).

Additionally, Dupoux et al., (2016) note that identifying and assessing high-potential targets will take more effort in Africa than in matured private equity markets by PE firms. They further note that owing to the shortage of experienced intermediaries and reliable information, private equity firms will have to invest in building capability to originate and screen deals. More time must also be given in performing of due diligence as rewards of such efforts tend to be high.

The performance record and operational expertise of the African PE fund manager according to AVCA, SAVCA and RisCura (2014) are cited oftenly by limited partners as important factors. More so, the presence and length of an already existing relationship with the core team of the PE firm also counts as significant in selection of the general partners.

2.2.3 Track performance record by PE firms.

New Frontiers conducted a study on South African pensions and asked respondents about their interest in allocating funds to private equity which do not have a track record as a team. From 14 respondents, only 10 were willing to consider investing with a private equity fund in which team members do not have a track record. To aid in their decision to invest in such as alternative asset class, they would take in consideration their individual track record of the partners within the private equity firm and weigh it heavily against their decision to allocate the funds. To add also unto their evaluation criteria, the proposed strategy and focus would also be taken into consideration (SAVCA, 2014).

Gohil and Vyas (2016) highlight studies done by Kaplan and Schoar (2005) on performance persistence which show that PE funds perform better with increased fund flows from potential investors. This ties with the skill and quality of the PE firm who have proprietary deal flow. In the same study, they cite Phalippou (2010) who found out that factors such as the fund size and sequence play an influential role in performance(Gohil & Vyas, 2016).
They further explored a study by Chung who sought to find if the persistence of performance for PE funds is affected by how much future information can be found in past performance, the strength of the current and future performance relationship. Additionally, Chung also considered the relationship between the performance of current funds with immediate follow-on fund and the second and third follow-on fund where he found no persistence for the second and third. However, a significant positive relationship between the current and immediate follow-on fund and thus concluded that the similarity of market conditions and the length of the overlapping investment period potentially affect the performance of a PE fund. More so, capital flow of already better performing PE funds can positively or negatively affect future performance (Gohil & Vyas, 2016).

2.2.4 Deal Activity

The growing deal activity in private markets has established a rising interest from traditional institutional investors such as pension funds and sovereign wealth funds (Kaplan & Schoar, 2005). Therefore this creates the need to seek alternative asset classes with high returns which the emergence and gradual growth of private equity firms has indeed provided. This diversification into alternatives is supported by the Modern Portfolio Theory which advocates for optimal portfolio construction by investors who are seeking to high return on based on a certain level of market risk while stating that the desired return is commensurate to the risk level (Kaplan & Schoar, 2005).

According to Gohil & Vyas (2016), PE deals have the potential to indicate capital structures, lower interest coverage and high-priced transactions thus highlighting the importance of what makes and leads to successive PE deals. Furthermore, the competition for deals alongside the availability of investments affect the PE fund performance in the long term thus highlighting the importance of deals and their actualization.

Much of the deal activity on the continent is concentrated on few larger markets, namely South Africa, Nigeria and Kenya as reported by the United Nations Development Programme (2016). In East Africa, 90% of the respondents from a survey done by Deloitte said that they expected to invest more owing to improved economic climate and increased investment opportunities.

Majority of private equity firms stated that they had raised new funds (Deloitte, 2016). Private equity tends to invest in growth stage enterprises that offer a higher chance of securing market-related returns and getting exposure to low risk (United Nations
Development Programme, 2015). Therefore, 2014 saw investments of $8.1 billion in 149 deals made in Africa which represented a 24% increase from the previous year with South Africa, Kenya and Nigeria becoming favorable investment preferences stable macroeconomic factors (United Nations Development Programme, 2015).

**2.2.5 Sector investments**

Focusing on selected drivers such as operating income growth and dispersion of earning forecasts poses as a more promising strategy as different industries may be prone and sensitive to different drivers (Sommer, 2013). For instance, volatility of a particular industry may vary therefore resulting to abnormal valuation levels (Sommer, 2013).

According to the KPMG and EAVCA (2017) report, funds raised by private equity globally from 2015 to 2016 were USD 1.1 trillion, those raised from African focused funds were USD 6 billion and USD 1.1 billion in East Africa. From the same report, volume deals in Kenya increased significantly to 23 in 2016. The financial sector has seen an increased deal activity at 42, energy and Natural Resources at 16 and FMCG at 12. In the year 2017, the total value of deals was boosted up to USD 2.6 billion by the Safaricom Limited deal and Vodacom Group. The deal numbers in Kenya per sector were as follows in 2015-2016; Agribusiness (2), Healthcare (3), Renewable energy (3), FMCG (3), Manufacturing (4), Financial Services (4), Real estate (1) and Transport and logistics (2) (KPMG & EAVCA, 2017).

Given the above statistics by the KPMG and EAVCA (2017) report, deals are seen to be more in the manufacturing, healthcare, energy and FMCG sector which implies more investment expertise and experience in those industry sectors. In support of the report, McPhee (2015) notes that financial services, agribusiness, food and beverage, pharmaceuticals are the focus of investments in East Africa, especially Kenya as most of these areas are consumer-oriented and driven.

**2.2.6 Private Equity Financing Strategies.**

Private equity strategies vary in investment strategy and design thus perfectly addressing different forms of financing and investments. Among them are buyouts (BOs), venture capital and mezzanine financing (Wright, Gilligan, & Amess, 2009). Buyouts can be categorized into; insider driven deals such as management buyouts (MBOs) and outsider driven deals such as management buy-ins (MBIs) and investor-led buyouts (IBOs). Early
studies done in the US have highlighted that these buyouts are typically funded leveraged buyout associations (Wright et al., 2009).

Povaly (2007) defines leverage buyouts (LBO’s) as equity investments used to attain a controlling interest in a company with the use of financial leverage. Advocates of LBO’s financing suggest that the transactions within this strategy generate wealth through promoting managerial incentives and overseeing the efficient use of surplus free cash flow. Moreover, he adds that critical voices counter this by stating that these gains come about due tax savings courtesy of the tax shield on interest payment (Povaly, 2007).

Venture capital deals with investing in a company before its initial public offering and in most cases, early in the life cycle of the company while mezzanine( a type of buyout) involves the use of both equity and debt (Daglioglu, 2016). PE funds vary with the use of strategy, structure and objective compared to traditional investments funds. These financing strategies pose unpredictability in both timing and cash flow over the life of the PE fund. Therefore Daglioglu (2016) stresses that the life stage of the fund is pivotal to the selection of a strategy to enforce.

A study conducted by Gachoka (2012) of Private equity firms in Kenya shows that 45% adopt venture capital, 33% adopt leveraged buyouts and 22% adopt mezzanine financing as investment strategies. The study found out that investment strategies had a positive effect on the performance of the private equity firms thus influencing their returns on investments. The adoption and proper implementation of these strategies are vital. The chosen strategy and its effective implementation to yield returns on investments greatly inform investors and affects the funds raised from traditional investors such as pension funds (Gachoka, 2012).

2.2.7 Value creation
Choosing the correct financing strategy is crucial for PE firms due to goal of value creation to be attained in the portfolio company which translates into a successful exit and gains to the PE investors. Loos (2006) states highlights value creation in buyouts results from different drivers that have direct effect on the operational efficiency and utilization of assets thus terming them as direct, intrinsic or operational value drivers. Also, there are others that non-operational in nature that are termed as indirect drivers but lead to value created between the realization of the investment and the acquired company (Loos, 2006).
Direct drivers tend to have most effect on the free cash flow generation of the company by either, increasing revenues, reducing expenses or using financial engineering to utilize capital which translates positively into enhancement of financial performance and value creation of the acquired buyout company (Loos, 2006). Additionally, Loos notes that the performance of the acquired company is not directly affected indirect drivers but rather boosted by them as they relate to changes in the organizational, corporate and governance structure (Loos, 2006).

Sommer (2013) states that value creation is more pronounced in venture capital investments due to the exposure venture capital targets to information asymmetries. The asymmetries arise from the normal ways of investment by venture capital in new or changing companies linked to high technological sectors owing to the consideration that they have the skills and expertise needed to effectively monitor investee companies.

According to Ernst & Young (2015), some of the ways that PE firms bring value creation to the invested portfolio of companies (exited) is by bringing in their extensive networks. These networks add value by: bringing on board expertise to the portfolio of companies, helping identify potential acquisition targets, assisting with legal and regulatory compliance, identification of potential clients and future business partners. Secondly, they help the management of the invested companies by transferring and sharing ideas, skills and knowledge unto them. Most importantly of all, they help the portfolio of companies improve their environmental, social and governance policies. This is in areas such as management incentive schemes, financial reporting, health and safety protocols and encouragement of involvement in community projects (Ernst & Young, 2015).

2.2.8 Fund Raising

Kaiser & Westarp (2010) points to the observations of Kaplan and Schoar (2005) that fund raising is influenced positively and to a great extent by fund performance of the PE firm. As a result, only the best performing PE firms attain a large measure of success in raising of funds in the life cycle of a fund. This is so owing; to the expertise and high competency held by best performing PE firms thus granting them a sustainable competitive advantage and investors who are able to recognize PE firms with a sustainable competitive advantage.
A survey by KPMG & EAVCA (2017) reveals that globally that USD 4.8 trillion was raised in between 2007 and 2016 with 0.6% (USD 28 billion) being reserved for Africa and 0.06% (USD 2.7 billion) for East Africa. Statistics by the same survey highlight that between 2015 and 2016, PE firms raised Africa focused funds worth USD 6 billion. Similarly, PE funds raised for East Africa were in the same period were USD 1.1 billion. Respondents from the survey, by a 75% representation acknowledged that their main source of funds by country was from Europe, followed by North America, East Africa and others.

2.3 Effect of External Factors on Fund Managers Investments in PE.

2.3.1 Development of Private Equity markets

PE is an investment strategy that has nearly achieved 30 years, according to (Robertson, 2009) with its boom period being in the mid-2000s. The first buyout was initiated in the US in the periods of 1976 and 1980s. This gave swift momentum to leverage buyouts funds with the highest record being of transaction standing at $25 billion. This was the acquisition of Nabisco in 1988. Firms such as Kohlberg, Kravis and Roberts (KKR), Blackstone and Carlyle are associated with the early development of LBO models in the 1980s (Robertson, 2009).

The PE industry has proved to be an important source of equity to emerging economies due to its financing ability and muscle through private equity funds according to the Asian Development Bank (2008). Nonetheless, characteristics of PE are different across regions and sectors as they are influenced by economic conditions, quality and strength of the legal and institutional environment, corporate governance standards, accessibility to both foreign and institutional investors and availability of liquidity posed through the stock exchange (Asian Development Bank, 2008). These markets are not without challenges, such as limited access to crucial markets, a lack of skills in management coupled with illiquid local capital markets (Asian Development Bank, 2008).

Lack of regulation increase the risk of PE investments as the funds raised are invested in companies that are privately owned (Robertson, 2017). PE is taken to be a highly complicated and competitive business environment that it generates a de facto efficient assumption leading to possible reason to necessitate any regulatory attention to managers and investors within the industry. More so, regulators give lee way to large investors such
as financial institutions than retail investors under the consensus opinion that these large investors are able to look out after themselves compared to the retail investors (those that invest on their behalf of their own personal account). The practice then has become the writing of optimal contracts in their investment deals with the PE investment managers. (Morris & Phalippou, 2012a). From the financial liquidity crisis in 2008, legislators and regulators have held PE as significant factor that can lead to a market collapse. Therefore, identification of risk has become expedient tagging along necessary government intervention and regulation (Ordower, 2010).

2.3.2 Maturity of the PE market

A report by Ernst & Young (2015) shows that emerging markets have evolved to become a key pillar to global investors strategies on financing. Private equity firms turned to these markets as global growth rates declined after the credit crisis. The emerging markets represented approximately 12% of the total private equity fund raising in the past 5 years. A change is now seen as they represent more than 20% (Ernst & Young, 2015).

The presence and establishment of international funds has also had an impact on African Private Equity. This is evidenced by the private equity share of transactions in investments by geography from 2011 to 2014 as shows in West Africa (25%), South Africa (24%), East Africa (18%), North Africa (14%), Southern Africa (7%), and Central Africa (5%) and at a multi-regional level (7%). In the past decade, Africa been one of the prime destinations for private equity investments. More than 200 funds manage a total of USD 30 billion upwards on the continent (Allen & Overy, 2015).

Dupoux et al., (2016) highlight a concern as to whether the private equity boom is being driven by economic fundamentals, a lot of capital chasing few instruments that prove to be sound and feasible. In response, they note that Africa has economic strengths that present continuous growth. They further argue that Africa’s expanding companies have the capacity to absorb immense foreign investment and generate high returns for investors. Most importantly, Africa has a great need for private capital to fund its continuous growth thus providing a chance for private equity to come in (Dupoux et al., 2016).
### 2.3.3 Exits

Exits occur for PE when the company that had been invested in performs well after a certain period of time, e.g. two to five years with the aim of the PE firm being to recoup its initial investment plus gains made from the investee entity. The gains net of carry are then redirected to investors of the PE fund (Kaiser & Westarp, 2010). The successful exit of any PE firm carries weight in regard to making the decision to invest in PE by limited partners. It is so because the initiative to participate in PE is anchored on the cash returns received from the general partner in view of investments made. When evaluating PE firms, the track record of positive returns acts as a useful decision making tool. Hence the famous quote of Henry Kravis, “Don’t congratulate us when we buy a company, congratulate us when we sell it.” This quote alludes to a successful exit through a sale to other strategic investors (Klier, Welge, & Harrigan, 2009).

As expounded by Chandrasekhar (2007), an exit by a PE investor usually takes on the following forms: having a direct sale to investors looking for a shareholder positioning in the acquired company by the fund, through an IPO in an equity market after post-purchasing listing, recapitalization through the increase of outstanding leverage thus using the cash to make dividend payments to its limited partners and making a sale to another PE firm.

Exits, more often not for PE investors in the global industry are usually through Initial Public Offering (IPO) or trade sales. IPOs in Africa are deemed to be rare due to the underdevelopment of equity markets (Babarinde, 2012). Babarinde cites that many African bourses lack the liquidity thus contributing to large scale IPOs (of about $100 million) that are preferred by PE investors. In the western markets, at the time of exit, an Initial Public Offering (IPO) usually is the primary means of exit. Management buyouts are usually ready alternatives for exits but are minimally used due to bringing in lower returns compared to the IPO. On the contrary, trade sales to strategic investors in emerging economies account for exits (Asian Development Bank, 2008). In support of this, Klonowski, (2011b) claims that the best exit results are usually attained when strategic investors are involved as they stir up competitive bidding for an investee business.
2.3.4 Successful exits
According to EY & AVCA (2013), successful exit preparation is key to PE firms. Having an exit plan from the beginning developed by the acquired company’s management and PE firm plays out to the gain of the general and limited partner at the time of exit. From 2014, the number of successful PE exit has been rising: 2014 (39 exits), 2015 (44 exits) and 2016 (48 exits). Over the last 10 years, South Africa at 42%, Nigeria (9%), Egypt (9 %), Kenya (6 %) and Ghana (5%) accounted for 70% of the PE exits in Africa. Additionally, the number of PE houses achieving successful exits increased has been on the increase with 2014, 2015 and 2016 registering 26, 30 and 31 successful exits respectively.

In 2016, PE firms in Africa recorded 24 exit routes via trade sales, an increase of 1 from 23 in 2015 while management buyouts were at 1, a decrease from 4 in the previous year in 2015. These demographics are crucial to institutional investors (local and foreign), wealthy individuals, foundations and endowments as they act as health and performance indicators of the PE industry regionally and locally within countries and on the continent. Furthermore, they prove to be reliable tools and of much aid to the investment decision making process (EY & AVCA, 2017).

2.3.5 Positive ROI in PE Investments
PE firms tend to be more conservative in their investment approach following periods of high return after exit (Sommer, 2013). In Kenya, exits have been few that have been within the duration of two years. Many exits, about 50% happen after more than 2-5 years. For instance, Centum Investment has held its stake in General Motors since the early 1990’s which is tied to high dividends payout and returns on investment (Mwirigi, 2014).

Though such investee companies seem lucrative for investments by PE firms and other investors, they are deemed expensive due to the transaction costs which makes getting a holding stake in them difficult thus discouraging investments. A PE firm can exit through the issue of an IPO or secondary deal or corporate acquisition. Though IPO’s are not preferred exit options, one such exit has been reported in Kenya where Centum Investments exited from Carbacid in 2011 via sales of shares making a profit of KES 800 million from a KES 418 investment deal in 2009 resulting in a sale of KES 1.2 billion in 2011 (Mwirigi, 2014).
2.3.6 Access to PE as an alternative asset

Alternatives investments can be defined as core diversifiers that are a high source of potential return (Hung et al., 2008). By nature, they tend to attract different risks and have low correlation to assets in an investor’s portfolio. They include hedge funds, commodities, venture capital and real assets such as real estate (Hung et al., 2008). The perception around alternatives is that they are “high risk, high rewards” investments thus not only creating a set of myth around them but bringing about an implicit understanding that they are illiquid, carry with them great cost of investment, are highly volatile and seem to be inaccessible to investors (Hung et al., 2008).

The Modern Portfolio Theory, according to Henry Markowitz (1953) is a theory that tries to bring to understanding of how one can maximize the expected return of a portfolio for a specific level of risk by choosing from a pool of various assets. It therefore promulgates asset diversification to investors as a way of diversifying risk within portfolios. (Schulmerich, Leporcher, & Eu, 2015). However, Bosco and Bocconi (2011) gives caution of greater information asymmetries in assets that are private to investors. This is partly due to the use extensive time and resources that comes examining the PE investment before arriving at a decision. Bosco and Bocconi (2011) therefore offers the use of large equity share as leverage to investors that aids them in gaining better access to information which helps them to have an informed entry point into PE.

2.3.7 Return on Investment of PE as an alternative asset.

Return on alternative assets are subject to variations in interest rates, investor perception of valuing risky cash flows as is evidenced in valuations of the equity market and credit spreads. The high returns achieved by this alternative asset class and their strategies are presumed to be as a result of significant diversification that gives rise to the misconception that they are “free lunch” which comes about due to the lack of mark-to-market data (Pedersen et al., 2014) Additionally, the misconception is fuelled by the fact that return indices for privately held investments are artificially smoothed which skews their correlation and volatility estimates downwards. Consequentially, fund managers result to using a risk factor approach to improve portfolio diversification (Pedersen et al., 2014).

Conversely, Lee, Kwon and Lee (2016) cautions that alternative investments call for a high level of specialization to attain superior returns due to the various types of risks that it tags
such as valuation and increased liquidity risk. As a result, it necessitates that the investment decision of funds are presented and handled by investment managers who design specific alternative strategies. An example given by Lee, Kwon and Lee (2016) is where PE investments have an expert deal team which collects and consolidates information to make sound investment decisions.

Recent academic studies go on to prove that PE returns are affected by significant exposure to the Pastor Stambaugh liquidity factor. The Pastor Stambaugh factor captures functions by capturing excess return on stocks with significant changes in aggregate liquidity; with the premise that lower-liquidity stocks will register high returns reversals following times of high volumes (Pedersen et al., 2014). Changes in illiquidity thus affect returns through availability and costs of financing for PE deals. More so, due to the nature of high dependency on leverage, they are made sensitive to capital challenges faced by the providers of debt i.e. banks and hedge funds (Pedersen et al., 2014).

2.3.8 Illiquidity factor of PE investments

Private equity investments have components of low liquidity, a long-term horizon and asymmetric knowledge which affect the earnings of PE investors. These components do not only increase risk but also expected return (Nix & Chen, 2013). In an interview with the Chief Investment Officer of Old Mutual Investment Group (Kenya), Mr. Peter Anderson states that the J-curve effect is a barrier to investments made by fund managers who want to make an impact in their three year tenure in owing to the slow maturity period of private equity returns (Ashiagbor et al., 2014).

PE are exposed to three types of liquidity risks according to Franzoni: liquidity risk that has its source from uncertainty over cost incurred in transactions, a high liquidity risk tolerance by the PE investor which influence the PE firms to take on more liquidity risks and lastly, the high leverage nature of PE investments that makes them susceptible to refinancing (Scarpati & Ng, 2013). Liquidity beta represents a critical component of investment risk in most alternative asset classes (Pedersen et al., 2014).

Earnings for general and limited partners in PE are sourced from: operating profits from the holding period of the fund investment such as acquisition and exit from the portfolio companies, the difference between the buying and selling price at the time of acquisition and exit respectively, financial engineering methods such as use of leverage to bolster returns and payment of recapitalization dividends or by selling off the assets of the
operating company (Appelbaum & Batt, 2012).

The J-curve phenomenon explains the trend of private equity funds to deliver negative returns in the early years of the investments and gains later on as the investments come into maturity. Due to the unpredictability of the timing and long-term horizon of the private equity investments, the tenure of a fund manager might end without them achieving their short term goals. This factor thus greatly influences fund manager’s decision to invest in the private equity market despite the promises of high returns. From the onset, fund fees are incurred and more cash outflows rather than inflows occur. This cash outflow therefore results initially in a decline, then level off and turn positive thus forming a j-curve (Daglioglu, 2016).

It can be used to show the impact of private equity market on investments made by investors over certain periods of the life-cycle of the investment. The j-curve effect takes longer to report a positive internal rate of return. The timings of cash flow and market performance are factors that influence this model of the j-curve. A basic understanding of these factors by fund managers and other potential investors is necessary when making the decision to invest funds into private equity. (Diller, Herger, & Wulff, 2009).

2.4 Strategies to Enhance Fund Manager Investment in PE

2.4.1 Risk Measures and corporate strategy alignment

The term “Risk” refers to the probability of a loss. If an asset has a high probability of incurring loss, it is then defined as a risky asset. Return, on the other hand is a measure of total gain or loss over a specified time period in an investment. Portfolios should be designed with assets that aim to diversify risk (Senthilnathan, 2016).

Risk diversification in such portfolios is then set up with meaningful correlation coefficients of returns of assets within the portfolio. An efficient portfolio therefore will aim to maximize the returns and minimize the risk for any given level of risk (Senthilnathan, 2016). Despite the need to seek risky investments that promise high yields, PE investors expose themselves only to a consume rate level of risk that is in accordance
to their corporate strategy thus investors such as fund managers apprehensive in behavior responses to risk (Farooq, Afzal, Sohail, & Sajid, 2015).

Schulmerich, Leporcher and Eu (2015) pose that a set of optimal portfolios is one that combines risk-free assets and the market portfolio where the market portfolio is pivotal to the CAPM. It contains risky assets such as bonds, stocks, options, real estate, antiques and human capital. Additionally, these risky assets are measured and given weights according to their current market value where the beta of a portfolio increases by its sizes thus making size to be negatively correlated to the return of the portfolio (Schulmerich, Leporcher, & Eu, 2015).

Identifying the sources of risk in PE is important for investors due to the framework that they will build to mitigate against this risk. Other than illiquidity, risk in PE is present: at the company level where implementation of the investment program is taking place and thus necessitating room for any adjustments to mishaps, the portfolio level in regards to the diversification outcomes, in manager selection with regard to performance of due diligence when it comes to picking of the PE fund manager and the execution of the private equity program where implementation of the PE program is at a higher level making its relationship to the entire investment portfolio be at significant risk (Kojima & Murphy, 2011).

Kojima & Murphy (2011) propose the following steps in regards to mitigating these risks. Step one is evaluating the score by penetrating the fund structure where one will look into the details of the company to the basic level and deliberately ignore all the excellent and pleasant advertising. Step two is mapping and conducting granular exposures that are easy to identify as they direct portfolio risk. Thirdly, one should test their hypothesis across various scenarios in order to understand any underlying issue relating to the health of the exposure, timing of capital calls and distributions and future funding prerequisites. Afterwards, the investor private portfolio should be triangulated by developing of proxies based on the public market using a risk-factor approach to determine volatility, beta and alpha assumptions. These can be through Sharpe ratio, Jensen’s alpha and the risk-adjusted performance metrics. Lastly, management of the diversity and dynamics of the presented PE risk should be done through strategic-specific and portfolio-wide modifications risk (Kojima & Murphy, 2011).
2.4.2 Commitment Strategies

Investment in PE require investor to commit a certain amount of capital to PE funds for a certain time period. In the PE industry, these funds are irretrievable and are thus invested gradually (called) over time at the discretion of the general partners (fund’s management). Therefore exposure to risk only comes with the invested capital (investment degree) as not all capital is invested upfront Oberli (2015). Therefore Oberli argues that this investment degree is what the investor should be aware of in their recommitment decision as they aim for a desired allocation level to PE asset class. Therefore, a commitment strategy from the onset comes out as a key factor to have just as is the initial decision to make allocations to PE owing greatly to illiquidity as a factor Oberli (2015).

However, Oberli (2015) extensively writes to caution that committing little capital to PE may result to disappointment as the returns expected may not match what was expected. If too much is committed, a risk of liquidity pressure may arise causing the investor to liquidate attractive and rewarding assets at a high cost in fire sales. A fire sale, also known as a rapid asset sale occurs when illiquid assets or investments are sold off quickly by managers. They happen largely due to factors that are not within the investor’s control (Lindsey & Weisman, 2016). More so, defaulting can result which has the potential to ruin an investor’s reputation. In his study, Oberli (2015) therefore recommends that these strategies should factor in distributions, commitments that are not expected to be called again and the amount needed to restore a balance to the asset classes in the strategic policy portfolio.

Illiquidity of the market and unpredictable cash flows pose a challenge for institutional investors in regard to keeping their PE investments at the desired level. However, being overly cautious and underinvested in PE can lead to poor portfolio performance of an investor given the highly rated perception in this alternative investment class( De Zwart, Frieser, & Dijk, 2012) The liquidity crisis in 2008 in the US taught investors that liquidity shortfall can be of adverse consequences especially for institutional investors with high allocations to illiquid asset classes. To ward off the reoccurrence of such a crisis, an efficient recommitment strategy becomes necessary to mitigate any opportunity cost that come due to underinvestment ( De Zwart et al., 2012).

The main finding of a study done by De Zwart, Frieser and Dijk (2007) found that having a recommitment strategy proved beneficial in sustaining a stable investment degree that is
near the target allocation of the investors while keeping in mind the probability of being over-exposed to risk within reasonable parameters. A further test of sensitivity analysis in the study revealed that having strategy towards PE investments for portfolios proved successful when restricted to the choice of PE capital investment (venture capital or buy-out), to a specific region or to varying experience of fund managers.

2.4.3. Regulation and Disclosure of information.

A weak regulatory environment that is supposed to oversee product, labour and capital markets leaves room for new financial intermediaries who can prove opportunistic and operate with few constraints (Appelbaum & Batt, 2012). More often than not, regulators have a crucial role to play any market environment thus should not constrain themselves to preventing systematic risk. At the top of their agenda should be market failure prevention as well, pursuing enforcement of efficiency through proper channeling and availability of information in the interest of all investors (Morris & Phalippou, 2012b). Recently, there has been recognition from capital market participants, public officials and researchers that highlights that investment fund managers are imperfect agents for their client which gives rise to an agency problem derived from the agency theory (Bebchuk, Cohen, & Hirst, 2017).

Jensen and Meckling (1976) developed the agency theory that postulates the theoretical rationale by managers on maximizing the shareholder’s value. The theory argues that agency problems arise when managers (agents) pursue their own interest instead of those of the shareholders (principals) (Appelbaum & Batt, 2012). There are two main relationships in PE: between the PE managers and the portfolio company and between the managers of the PE firm and their investors. Agency problems arise when there is information asymmetries between the parties in the two mentioned relationships. A solution to this problem, according to Morris & Phalippou (2012) is through the simplifying of contracts and availing of quality data that allows the principal( LP’s) to keep in check and hold accountable the agent ( GP’s). Alternatively, appointing of independent directors onto the portfolio’s company board and aligning the interest of principals and agents aid in reducing the agency problem (Beuselinck, Deloof, & Manigart, 2008).

Disclosure of information, on the flip side tags along a number of outcomes that may fall along the positive and negative spectrum. First, it can result to a higher demand of
disclosure momentum across the PE industry. This has significant effect outcome of possibly increasing transparency into the PE deals done. Secondly, it may result to external demand from potential buyers/owners of private equity investment funds. This positively adds to the efforts by PE houses when fundraising. Lastly, disclosure may lead to less competitive costs for PE firms compared to non-PE firms. This is due to the distinctive PE “war chest” that hinders potential competitors from joining the industry. By and large, disclosure of information has the capability to reduce information asymmetries thus reducing the cost of capital, thereby enhancing the firm investment and growth (Beuselinck et al., 2008).

Availability of information is crucial for the efficient working of any market. This information itself needs to be presented forth with a clear and concise yet consistent format to all interested parties to allow for independent scrutiny. PE firms do provide information to their investors but lack to meet the aforementioned conditions as it is varies and is fragmented, being limited only to the funds in which the investors invest in (Morris & Phalippou, 2012b). The information given cannot also be independently be verified and ascertained as true as it is not made available to other parties such as outsiders. Therefore the overall effect and consequences come out then as investors having no information on funds that they did not invest in, PE managers not being able to access information on the portfolio of companies that are in the acquisition of their peers and causing the longevity of the struggle experienced by academics and policy makers to gather representative and large samples of data for analysis that would prove beneficial (Morris & Phalippou, 2012b).

2.4.4 Strengthening of local financial markets
Most PE firms pursue an exit through the modes of either a public listing that entails an initial public offer or a trade sale to a strategic investor. Klonowski (2011b) notes that robust local securities exchange can either play friend or foe to the PE industry as the PE firms rely on the efficiency and liquidity nature of these public markets. For instance, 46 exits have been achieved successfully in Poland through public listing which translates into 10% of firms listed on the stock exchange to being PE- backed firms (Klonowski, 2011b).

On the contrary, the development and strengthening of local security exchanges to enable successful exits can make it turn into a challenging competitor towards the PE industry. This is due to the owners of the PE firms being able to list their shares on the same security exchange thus attaining high and strong valuations for their business, having unrestricted
access to capital and being able to maintain operational independence (Klonowski, 2011b). Strengthening of local securities exchange therefore becomes paramount and needful for the exiting of PE investments (Klonowski, 2011b). Povaly (2007) also supports the strengthening of local public financial markets as they aid in achieving a successful IPO issue thus impacting on it as an important choice of an exit route by PE investors.

The development of exit strategies is done by fund managers who include all precautionary measures to liquidate all investments and assets attained to the highest possible rate of return. Therefore, fund managers add the control clause into their contracts with the portfolio firm (Orata A, 2008). Additionally, fund managers need to be wary of the strength and condition of the local securities exchange in order to make the right and informed exit strategy if it’s to use the securities market as a platform of exit. Of all clauses, the most prevalent are drag along rights, warrants and put options which serve the purpose of enabling the PE fund the right to device a desired and optimal exit strategy at the most opportunistic and well-timed as desired by the investor (Orata A, 2008).

Kelly (2012) emphasizes the importance presence of deep and liquid capital markets. These markets, if deep and liquid, provide an important exit route that permit investors to regain their funds in future. Secondly, they ensure supply of investment capital through IPO issues which help reduce information asymmetry thus lowering transaction cost. Thirdly, they act as an important proxy for financial depth availing financial leverage in the long run which is essential for buyout models (Kelly, 2012).

2.4.5 Exit Market Development

An exit may be the last phase of PE investments in portfolio companies but it is certainly the most crucial as it’s the point where all illiquid assets or investments are monetized (Klonowski, 2011b). An exit serves as a final confirmation that their initial selection and analysis of the portfolio company, negotiations efforts in terms of investor and investee legal requisites and protection, and their team work throughout the partnership in regards to expansion and operational execution have performed well (Klonowski, 2011b). A well-developed exit market with an oversight body as proposed by Orata A (2008) in her study therefore goes not only in helping realize attractive returns to investors but potentially sees additional raising of capital for the next investment, raise investor confidence due to its
well defined roles and guidelines for its operations as a local and recognized regulatory authority.

IPO’s become attractive as exit strategies as they may indicate the successful achievements of PE investors within their portfolio companies which acts as a signal to lure in potential limited partners investments. IPO’s in Kenya are the least preferred exiting route to fund managers due to the constraints posed by the regulatory environment (Orata A, 2008). Trade sales, another exit route where the PE fund offload their shares in the portfolio firm to another PE firm via sales is the most preferred exit route used by fund managers in Kenya owing to less regulatory restraints (Orata A, 2008).

Despite the different alternatives to achieving exit by the PE firm, the different dynamics of each alternative should be considered along the lines size and traits of the portfolio company, execution timing of the exit, cost implications, public disclosure requirements and tax impact (Povaly, 2007). These factors have the potential to determine the usage of any exit route and add to its popularity. Such factors also add up to the maturity of the exit environment thus can be a determining factor in the decision by potential fund and PE managers to invest in PE industry (Povaly, 2007).

2.5 Chapter summary

This chapter discusses how different dynamics of private equity have played out to influencing limited partners investing in them. It further discusses the global and regional growth and impact of the private market and how it has caused growth in returns to investments thus making it a continuous attractive alternative investment asset class among traditional institutional investors. The next chapter focusses on the research methodology used on this study.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter covers the methodology that will be used in the study. It discusses the research design, population, sampling design, framework and techniques, instrumentation and data collection and analysis procedures that the study will use.

3.2 Research Design

Research design is a plan to guide the researcher on how they will go about answering their research questions. As a result, the design tends to be concerned with the overall plan of the project. The nature of the study takes to a descriptive design approach thus making it orient to a qualitative methodology. Qualitative studies derive meaning and findings from words and opinions (Saunders, Lewis, & Thornhill, 2016). Studies that undertake a descriptive approach go on to seek accurate accounts of persons, events, or situations thus explaining and exploring the characteristics of the subject under the study. This allows the data to be qualitative (Cooper & Schindler, 2014). As the objective of the study is to find out the determinants of fund manager’s investment in private equity, the descriptive design was the best fit used as it helped in identifying the investment behavioural attitudes and perceptions that go into the investment and decision making process of fund managers as representatives of limited partners.

3.3 Population and Sampling

3.3.1 Population

A population refers to a complete group of elements that are of interest to a study and in whom inference can be made. Alvi (2016) defines the target population as a group in whose all members match the selection criteria for the study. From the desired population, a target population was acquired for the use of the study. Target population by definition are the people, records or events that hold the needed information thus making them suitable to provide answers to the research questions (Cooper & Schindler, 2014).

3.3.2 Sampling Design

A sample is defined as a sub-set of the chosen population (Burgess, 2001). Sampling design represents the method used to select the appropriate sample size (Saunders, Lewis, & Thornhill, 2016).

3.3.2.1 Sample Frame

This represents the whole and correct list of all members of a population. It represents a list that may be inclusive of individuals, organizations or even businesses at a small and large scale level (Cooper & Schindler, 2014). The sample frame of the study was derived by using only the registered fund managers by RBA as shown in the appendix on page 83.

3.3.2.2 Sample Technique

Minimizing the sampling error is the main aim of every sampling technique (Salkind, 2009). Therefore, the sampling technique is the method used to obtain a representative sample. This study adopted the census approach that advocates for the collection of data and analysis of every individual within the specified population therefore there was no sampling error (Saunders et al., 2016).
3.3.2.3 Sample Size

Selecting an optimal sample size is crucial in reducing the cost of sampling error (Bambale, 2014). The study did not have a sample size as it took on a census approach in data collection.

3.4 Data collection Method

The collection of data can vary from observing a particular group in one location to a grand scale survey of many organizational groups in a different location or same location (Cooper & Schindler, 2014). The study employed the use of questionnaires to collect primary data from the registered fund managers. As the study leaned towards the descriptive approach, questionnaires were best suited to collect primary data. The researcher adopted the use of a five level likert scale in the questionnaire. The five levels range from very important, important, neutral, less important and not important. Primary data is new data collected on a first-hand basis while secondary data is that which has been collected and used in various capacities to make interpretations and convey knowledge (Saunders et al., 2016).

3.5 Research Procedure

A research procedure is the defined process observed by a researcher while conducting the study (Cox & Hassard, 2005). The researcher sought a letter from of approval from the institution’s research office to conduct the study. This letter then presented to the fund managers to facilitate collection of data through administration of questionnaires using a pick and drop. A pilot test was also conducted to aid in making any corrective changes to the questionnaires to ensure the reliability and validity of the overall research before the main collection of data was done. The fund managers on whom the pilot test was based on was identified from the registered fund managers as shown in the appendices.

3.6 Data Analysis Methods

Researchers create information by analysing raw data. Data analysis entails the conversion of raw data to useful summaries, patterns using applied statistical techniques (Cooper & Schindler, 2014). The study used the Statistical Package for Social Studies (SPSS) as the data tool of analysis after the data was coded and cleaned using the same SPSS tool.

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Descriptive statistics that included means, standard deviations and percentages were conducted on the collected data and presented in bar charts and tabular format. The study also conducted inferential statistics using Pearson’s correlation rank on the independent and dependent variables to determine the existence of meaningful relationships. The dependent variable was the amount invested in private equity while the independent variables were the PE firm characteristics and selected external factors. Correlation is used as an index to measure the strength of association of variables. It can range from zero which indicates no association to positive or negative one to show perfect association (Healey, 2011). Furthermore, a high index shows a strong correlation factor while a low index level shows a weak correlation between selected variables. The analysed data was then be presented in bar charts and in tabular form with figures.

3.7 Chapter Summary

The chapter has discussed the research methodology that the study will implement. The chapter started by expounding on the research design that was to be used, followed by definitions of both populations and sampling aspects giving clarity on the chosen target population, sample size and sampling technique. The data collection methods and research procedures followed suit ending with the data analysis. The next chapter presents the findings and results of the study.
CHAPTER FOUR

4.0 DATA ANALYSIS AND PRESENTATION OF FINDINGS

4.1 Introduction

This chapter presents data analysis of the collected data. From the analysis, the findings and results of the study are presented. Descriptive and inferential statistics have been used to present the study’s findings and results in all sections. The first section presents findings of the respondent’s demographic information. The second section looks at the impact of PE characteristics on fund manager’s investments. The third section analyses the impact of external factors on PE investments by fund managers while the last section examines responses towards the strategies that can be used to enhance fund manager’s investment in PE.

4.2 Demographic Information

The demographic information presented in the study on; the age group, types of funds managed, experience of fund managers in handling investors funds, overall size of funds managed by the fund managers, if a fund manager invest in PE, amount of funds invested in PE and the form of strategy invested in by fund managers all provide essential insight about the respondents. This goes to inform the study greatly thus aiding in making relevant conclusions and recommendations in the following chapter.

4.2.1 Study Response rate

The study targeted 40 respondents from which 37 responded fully to the study via the data collection method, administration of a questionnaire where 3 did not respond.

![Figure 4.1: Study Response rate](imageurl)
This skewed in favour of the study by 93% as showed by figure 4.2.1 thus was accepted for use

4.2.2 Age Distribution

As figure 4.2 shows, most of the respondents were aged in between 31-40 years, a representation of 46%, followed by 27% of ages between 20-30 years, 22% of 41-50 years and 5% of 51-60 years.

![Age Distribution Chart]

**Figure 4.2: Age distribution of respondents**

4.2.3. Types of Funds managed

The study sought to find out what type of funds were managed by the fund managers in their portfolios. The figure 4.2.3 showed that pension funds were the major funds managed with a percentage of 23% thus informing the study that they were a significant source and part of capital in-flows when a PE firms made a call to fund raise for potential investments identified in various economic sectors in Kenya, followed by investment banks at 20%, Insurance companies at 19%, collective investment schemes at 15%, wealthy individuals at 14%, endowments at 7% and Foundations at 2%.
4.2.4. Experience of Fund managers

The study according to figure 4.4 revealed that most of the fund managers had 4 to 6 years of experience of managing investor’s fund with a representation of 44%, followed by 1-3 years at 31%, 7 to 9 years at 19% while above 10 years registered the lowest percentage of 6%.
4.2.5. Overall Size of Fund managed

Figure 4.5: Overall Fund size managed in KES

According to the study results shown in figure 4.5, a fund range of KES 801 to 1 billion was the most commonly managed with a representation of 27%, followed by a tie between ranges KES 0 to 200 million, KES 401-600 million and KES 601-800 million. In the same manner, fund sizes of KES 201-400 million and KES 1-10 Billion both had a management representation of 11% among the respondents. The lowest fund size managed as per the study was between a range KES 41 Billion and above at 3%.

4.2.6. Investment in Private Equity

Figure 4.6: Investment in Private Equity
From the findings of the study according to figure 4.6, 83% of the fund managers affirmed to make investments in Private equity while 17% reported that they do not make any investments in Private equity.

4.2.7. Level of investment in Private Equity.

The study highlighted that the highest level of investment in monetary terms in PE as per the below figure 4.2.7 stood at a range of KES 0-200 million, represented by 34% by fund managers. Following closely and at a tie was the range of KES 101-600 million at 22%, KES 201-400 million at 19% while the least at 3% was the range of KES 801-1 Billion.

4.2.8. Forms of Private Equity Strategies used

![Figure 4.7: Investment in Private Equity](image)

Figure 4.7: Investment in Private Equity

![Figure 4.8: Forms of Private Equity Strategies used](image)

Figure 4.8: Forms of Private Equity Strategies used
Venture capital as PE investment strategy at a 63% representation was more preferred by the fund managers according to the study results, followed by leverage buyouts at 32% and mezzanine at 5%.

4.3. Effect of PE Firm characteristics on Fund Managers Investment.

The purpose of the first objective was to determine the impact of a Private firm characteristics on the investment decision in Private equity by fund managers.

4.3.1 Experience of PE Fund Managers

The study sought to find what level of importance experience of PE fund managers had on the respondent’s decision to invest in PE investments. The findings were that 43% of the respondents strongly agreed and 24% agreed that experience of PE fund managers weigh in importantly as factors to consider when making investments decisions in PE. On the contrary, 16% of the respondents maintained a neutral position on the importance of PE fund managers experience while 11% considered it less important and 5% as not important.

![Figure 4.9: Experience of PE Fund managers](image)

The mean and standard deviation attained (M=3.8, SD=1.24) showed that the experience of PE fund managers lied on a strong neutral point that leaned towards importance thus impacting positively the investment decision in PE.
4.3.2 A local Presence

Respondents viewed having a local presence and being a mature firm in the PE industry weighed in very importantly at 46% and importantly with a 35% in their decision to invest in PE investments as per the study findings. Few respondents were at a neutral stand point at 11% with the remaining considering local presence and maturity to be less important at 5% and not important at 3%. According to the finding of the study, having a local presence and attaining maturity does impact and determine investment in PE investments as shown a mean and standard deviation of (M=4.16, SD=1.01).

4.3.4 Track Performance recorded by PE Firms

Figure 4.11: Track Performance recorded by PE Firms
Looking at the track performance record of the PE firm, respondents viewed this as very important as supported by a 43% and 30% as important. Only 22% of the respondents viewed it neutrally while 5% deemed as a less important factor. None of the respondents though it was not important as shown by a 0%. Therefore, having a track performance record as per the study findings, does affect and impact on the decision to invest in PE by investors as supported by mean and standard deviation of (M=4.11, SD= 0.94).

4.3.4 Deal Activity

![Bar chart showing deal activity preferences](image)

**Figure 4.12: Deal Activity**

The study findings pointed out also that respondents viewed the deal activity i.e. locally, regionally and internationally of the PE firm to be very important at 35% and important at 35% while 16% of the respondents maintained a neutral perspective on its importance. 11% of the respondents considered it be less important while 3% regarded it as not important at 3%. The mean and standard deviation of (M=3.89, SD=1.10) attained showed a strong neutral view point that leaned towards having importance thus does impact on the investment decision in PE.

4.3.5 Sector Investments

The study found that the sector of investment by the PE firm was considered very important at 24% and important at 43% by the respondents. A neutral perspective at 24% was adopted by the respondents while 5% thought of it as less important and 3% as not important. The mean and standard deviation attained (M=3.81, SD=0.97) presented a strong neutral stand point of the respondents that leaned towards having importance thus having an impact on the investment decision in PE.
4.3.6 PE Financing Strategies

Respondents viewed very importantly at 35% and 46% the types of financing strategies used by PE firms. A neutral stand was adopted at 11% by the respondents while 5% held that the strategies were less important at 5% and not important at 3%. The mean and standard deviation attained (M=4.05, SD=0.97) showed that the type of finance strategy used by PE firm does impact on the decision to invest in PE investments.
4.3.7 Value Creation

Value creation by PE firms was regarded as very important and important at 43%, while 11% of the respondents adopted a neutral viewpoint to its importance with the remaining at 0% as less important and 3% as not important. The mean and standard deviation attained (M=4.24, SD=0.86) presented value creation in invested companies as having an impact on the investment decision on PE investments.

4.3.8 Fund Raising

The PE firm ability to fundraise was considered very important at 57% and important at 19%. 11% of the respondents adopted a neutral opinion while 14% regarded it as less important with 0% as not important. The mean and standard deviation (M=4.19, SD=1.10) showed that the ability to fundraise by a PE firm does affect the investment decision in private equity by investors.
A further analysis of the results from the study was done to determine relationships between the demographic variables of experience in managing investor funds, overall size of the fund managed and the amount (KES) invested in PE by the fund managers and PE firm characteristics. The results were as shown in table 4.1.

Findings from the study showed that the experience of the PE fund managers had a weak positive correlation against the respondent’s demographic factors of experience in managing investor funds at (R=0.436, P<0.01), overall size of fund managed (R=0.358, P<0.03) and amount invested in PE (R=0.368, P<0.038). The experience of PE firm managers showed statistical significance thus weighed in importantly to the decision to invest in PE.

The PE firm track performance record attained a weak positive correlation at (R=0.356, P<0.033) and moderately positive correlations against the overall size of fund managed (R=0.532, P<0.001) and amount invested in PE (R=0.578, P<0.001). The PE firm track performance record showed statistical significance against the selected demographic factors proving to be a determinant of the investment decision in PE.

Having a local presence and maturity attained a weak correlation score against all three selected demographic factors of experience in managing investor funds (R=0.263, P>0.121), overall size of fund managed (R=0.131, P>0.440) and amount invested in PE (R=0.128, P>0.484). A local presence and maturity of the firm did not prove to have any statistical significance thus does weigh in importantly in the investment decision in PE.

Figure 4.16: Fund Raising
### Table 4.1: Correlation between demographic factors and PE firm characteristics

<table>
<thead>
<tr>
<th>Demographic factors</th>
<th>Statistical test</th>
<th>Experience in managing Investor funds</th>
<th>Overall size of fund</th>
<th>Amount (KES) invested in PE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Experience of PE managers</td>
<td>Pearson Correlation</td>
<td>.436**</td>
<td>.358*</td>
<td>.368*</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.008</td>
<td>.030</td>
<td>.038</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>PE firm track performance record</td>
<td>Pearson Correlation</td>
<td>.356*</td>
<td>.532**</td>
<td>.578**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.033</td>
<td>.001</td>
<td>.001</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Local presence and maturity</td>
<td>Pearson Correlation</td>
<td>.263</td>
<td>.131</td>
<td>.128</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.121</td>
<td>.440</td>
<td>.484</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Deal activity</td>
<td>Pearson Correlation</td>
<td>.186</td>
<td>.235</td>
<td>.398*</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.277</td>
<td>.161</td>
<td>.024</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Sector of investment</td>
<td>Pearson Correlation</td>
<td>.304</td>
<td>.125</td>
<td>.299</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.071</td>
<td>.460</td>
<td>.096</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Types of financing strategies</td>
<td>Pearson Correlation</td>
<td>.411*</td>
<td>.345*</td>
<td>.423*</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.013</td>
<td>.037</td>
<td>.016</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Value creation</td>
<td>Pearson Correlation</td>
<td>.265</td>
<td>.347*</td>
<td>.443*</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.118</td>
<td>.036</td>
<td>.011</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>PE firm ability to fundraise</td>
<td>Pearson Correlation</td>
<td>.209</td>
<td>.357*</td>
<td>.513**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.220</td>
<td>.030</td>
<td>.003</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
</tbody>
</table>

The deal activity of the PE firm likewise attained a low but positive correlation against the selected demographic factors of experience in managing investor funds (R=0.186,
P>0.277) overall size of fund managed (R=0.235, P>0.161) and amount invested in PE (R=0.398, P<0.024). Deal activity showed statistical significance only against amount invested in PE thus making in important to the investment decision in that regard.

Similarly, the sector of investment attained low but positive correlations against the experience in managing investor funds (R=0.304, P>0.071), overall size of fund managed (R=0.125, P>0.46) and amount invested in PE (R=0.299, P>0.096). There was no statistical significance attained therefore the sector invested in did not weigh in importantly as a determinant of investment in PE investments.

Types of financing strategies also attained low but positive correlations against the experience in managing investor funds (R=0.411, P<0.013), overall size of fund managed (R=0.345, P<0.037) and amount invested in PE (R=0.423, P<0.016). The type of financing strategies used by PE firms proved to be of statistical significance thus weighed in importantly to the investor decision to invest in PE investments.

Value creation followed the same trend, attaining low but positive correlations against experience in managing investor funds (R= 0.265, P>0.118), overall size of fund managed (R=0.347, P<0.036) and amount invested in PE (R=0.443, P<0.011). Value creation in invested companies was only statistically significant in relation to the overall size of the fund and amount invested in PE.

The ability to fund raise by PE firms attained a low but weak correlation against experience in managing investor funds (R=0.209, P>0.220), overall size of fund managed (R=0.357, P<0.03) but a moderate high but positive correlation of (R=0.513, P<0.003). Ability to fund raise by a PE firm was of statistical significance regarding the overall size of fund managed and amount invested in PE by the respondents hence weighed in importantly in the decision to invest in PE.

4.4 Effect of External factors on Fund Managers Investments in PE.

The purpose of the second objective was to determine the impact of selected external factors on the decision to invest in Private equity investments.
4.4.1 Development of the PE Market

The respondents held that the existing number of PE firms in the industry was very important and important at 30% and 19% respectively while 27% respondents held a neutral view with 11% and 14% taking to a less important and not important viewpoint. The mean and standard deviation attained (M=3.41, SD=1.384) showed that a neutral point was adopted by the respondents thus the number of PE firms is not highly important to the investment decision in PE.

4.4.2 Maturity of the PE Market

The maturity of the PE market was regarded as very important and important at 38% and 35% respectively with a neutral view attaining 14% while less important and not important viewpoints attained 11% and 3% respectively. The mean and standard deviation attained (M=3.95, SD=1.104) showed that a neutral point though moderately strong was adopted by
the respondents. Therefore, the maturity of the PE market does come relatively close to be an important factor to the decision to invest in PE investments according to the study findings.

4.4.3 Exits

Respondents appreciated this factor as important by 49% with 35% deeming it very important, 11% holding a neutral perspective, 0% being convinced of it as less important and 5% as not important. The mean and standard deviation attained (M=4.08, SD=0.983) goes to appreciate positively the importance and influence of the number of successful recorded exits by PE firms on the investment decision in PE as per the study findings.

Figure 4.19: Exits

4.4.4 Successful exits

IPO as an exit strategy was regarded as very important and important at 35% and 41% respectively with a 14% neutral following and both a 5% less important and not important viewpoint by respondents. The mean and standard deviation (M=3.95, SD=1.104) attained showed a moderately strong neutral point that skewed to it being an important factor. Therefore, the IPO as an exit strategy does weigh in importantly in the decision to invest in PE.
Trade sales as an exit strategy was very important and important at 38% and 43% with a neutral following of respondent at 14%, 5% at less important and 0% at not important. The mean and standard deviation attained (M=4.14, SD=0.855) favoured highly trade sales as an exit strategy thus showing it as important and impactful in the decision to invest in PE.
Figure 4.22: Secondary Buyouts Exits

Using secondary buyouts as exit strategy was very important and important at 27% and 49% respectively with respondents being having a neutral view at 11%. The remaining viewed it as less important at 8% and not important at 5%. The mean and standard deviation (M=3.84, SD=1.093) attained implied a moderately strong neutral view point which skews in favour of importance and positive impact to the investment decision in PE by the respondents.

4.4.5 Track record of positive ROI in PE

Figure 4.23: Exits
The existence of track records that show positive ROI after exit in the market was regarded as very important at 43%, important at 27%, less important at 8% and not important at 0% with respondents adopting a neutral stand at 22%. The mean and standard deviation attained (M=4.05, SD=0.998) disclosed that existing track records of positive ROI after exit does weigh in importantly and considerably in the investment decision in PE by the respondents.

### 4.4.6 Access to PE as an alternative asset

The ROI of private equity as an alternative investment class was regarded both as very important and important by respondents at 41%, 14% at less important, 5% at not important with 14% adopting a neutral viewpoint. The mean and standard deviation (M=4.11, SD=1.022) presented ROI of private equity as an alternative investment class as a factor that weighs in importantly in investment decision in PE by the respondents.

![Figure 4.24: Access to PE as an alternative asset](image)

**Figure 4.24: Access to PE as an alternative asset**

### 4.4.7 Return on Investment of PE as an alternative asset.

Availability of PE as a diversifier asset in a portfolio was viewed as very important and important at 30% and important at 46%, less important at 5%, 0% as not important and at a 19% neutral point by investors. The mean and standard deviation (M=4.00, SD=0.85) presented the availability of PE as a diversifier asset in a portfolio as an equally important and impactful factor in the investment decision of the fund managers in PE.
Figure 4.25: Return on Investment of PE as an alternative asset.

4.4.8 Illiquidity factor of PE investments

The illiquidity nature of PE investments was highly considered to be very important at 57%, important at 24%, less important at 3%, not important at 0% with a neutral value of 16% from the respondents. The mean and standard deviation (M=4.35, SD=0.857) strongly hinted out that this factor of illiquidity from PE investments was of high significance unlike its counterpart to the making of the investment decision in PE.

Figure 4.26: Illiquidity factor of PE investments
A further analysis of the results from the study was done to determine relationships between the demographic variables of experience in managing investor funds, overall size of the fund managed and the amount (KES) invested in PE by the fund managers and external factors. The results were as follows in table 4.2

**Table 4.2: Correlation between external factors and selected demographic factors**

<table>
<thead>
<tr>
<th>Demographics</th>
<th>Statistics</th>
<th>Experience in managing Investors funds</th>
<th>overall size of fund</th>
<th>Amount invested in PE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Existing number of PE firms in the PE industry</td>
<td>Pearson Correlation</td>
<td>-.047</td>
<td>.178</td>
<td>.611**</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.784</td>
<td>.292</td>
<td>.000</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Maturity of the PE market</td>
<td>Pearson Correlation</td>
<td>.059</td>
<td>-.148</td>
<td>.333</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.732</td>
<td>.383</td>
<td>.063</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Number of successful recorded exits by PE firms</td>
<td>Pearson Correlation</td>
<td>.299</td>
<td>.169</td>
<td>.226</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.076</td>
<td>.317</td>
<td>.214</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>IPO issue as an exit strategy</td>
<td>Pearson Correlation</td>
<td>.150</td>
<td>-.096</td>
<td>.276</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.384</td>
<td>.572</td>
<td>.127</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Trade sale as an exit strategy</td>
<td>Pearson Correlation</td>
<td>.344*</td>
<td>-.065</td>
<td>-.145</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.040</td>
<td>.700</td>
<td>.429</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>36</td>
<td>37</td>
<td>32</td>
</tr>
<tr>
<td>Secondary Buyout as an exit strategy</td>
<td>Pearson Correlation</td>
<td>.304</td>
<td>.192</td>
<td>.209</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.072</td>
<td>.255</td>
<td>.250</td>
</tr>
</tbody>
</table>
The existing number of PE firms had a negative correlation against the experience of fund managers in managing investors funds (R=-0.047, P>0.784), a weak but positive correlation against the overall size of the fund managed (R=0.178, P>0.292) and a strong positive correlation against amount invested in PE by the respondents (R=0.611, P<0.01). Therefore, the existing number of PE firms in the industry was only significant in relation to the amount invested.

The maturity of the market attained a weak positive correlation against experience of fund managers in management of funds (R=0.059, P>0.732), a negative correlation against the overall size of the fund managed (R=-0.148, P>0.383) and a weak positive correlation against the amount invested (R=0.333, P>0.063). The findings of the study proceed to show that the maturity of the market does not hold statistical significance therefore does not impact the investment decision in PE in relation to the selected respondents’ demographic variables.
The number of successful exits recorded by PE firms attained a weak but positive correlation against the experience of fund managers in managing funds (R=0.299, P>0.76), a negative correlation against the overall fund size managed (R=0.169, P>0.317) and a weak positive correlation against the amount invested in PE (R=0.226, P>0.214). From the findings, the number of successful exits does not hold any statistical significance in relation to the selected respondent demographic factors thus does not influence the investment decision in PE.

IPO as an exit strategy presented a weak positive correlation against the experience in management of funds by the respondents (R=0.150, P>0.384), a negative correlation against the overall fund size managed (R=-0.096, P>0.572) and weak positive correlation against the amount invested (R=0.276, P>0.127). IPO’s as exit strategies from the study findings are not statistically significant in relation to the selected demographic factors thus do not influence the investment decision of the respondents in PE.

Trade sales as an exit strategy attained a weak positive correlation against the experience in management of funds by the respondents (R=0.344, P<0.04), a negative correlation against the overall fund size managed (R=-0.065, P>0.7) and negative correlation against the amount invested (R=-0.145, P>0.429). Trade sales as exit strategies from the study findings was only statistically significant based on the experience in management of funds by the respondents therefore causing impact on the investment decision in PE.

A secondary buyout as an exit strategy presented a weak positive correlation against the experience in management of funds by the respondents (R=0.304, P>0.072), a weak positive correlation against the overall fund size managed (R=0.192, P>0.255) and weak positive correlation against the amount invested (R=0.209, P>0.25). Secondary buyouts as exit strategies from the study findings were presented as not statistically significant in relation to the selected demographic factors. Therefore, they do not influence the investment decision of the respondents in PE.

Track record of positive ROI attained a weak positive correlation against the experience in management of funds by the respondents (R=0.166, P>0.332), a weak positive correlation against the overall fund size managed (R=0.378, P<0.021) and moderately strong positive correlation against the amount invested (R=0.517, P<0.002). Having a track record of positive ROI was statistically significant in relation to overall size of fund managed and amount invested in PE therefore impacting on the investment decision in PE.
The ROI of PE as an alternative investment class got a weak positive correlation against the experience in management of funds by the respondents (R=0.32, P>0.057), a weak positive correlation against the overall fund size managed (R=0.445, P<0.006) and weak positive correlation against the amount invested (R=0.479, P<0.006). Return on investment of PE as an alternative investment class proved to be of statistical significance in relation to the overall fund size managed and amount invested in PE thus impacts on the investment decision in PE.

Availability of PE as a diversifier asset in a portfolio attained weak positive correlation against the experience in management of funds by the respondents (R=0.392, P>0.018), a weak positive correlation against the overall fund size managed (R=0.235, P>0.161) and weak positive correlation against the amount invested (R=0.308, P>0.086). Availability of PE as a diversifier asset in a portfolio proved to be of statistical significance in relation to the experience in management of funds by the respondents therefore causing impact on the investment decision in PE on that basis.

Illiquidity factor of PE investments presented a weak positive correlation against the experience in management of funds by the respondents (R=0.04, P>0.819), a weak positive correlation against the overall fund size managed (R=0.197, P>0.243) and weak positive correlation against the amount invested (R=0.354, P<0.047). Illiquidity factor of PE investments were of statistical significance in relation to amount of funds invested in PE by the respondents therefore causing impact on the investment decision in PE.

4.5 Strategies to enhance Fund Managers Investments in PE

The study also sought to find out what strategies could be used to enhance private equity investments in its third objective.

4.5.1 Risk Measures and corporate strategy alignment

According to the findings, 36% of the respondents strongly agreed, 39% agreed, 0% disagreed and 8% strongly disagreed with 17% being neutral on development of risk monitors/indicators for PE as an enhancement strategy. The mean and standard deviation (M=3.94, SD=1.145) attained showed a strong neutral view point that leaned towards agreement that indeed the development of risk monitors/indicators was a strategy that can be used to enhance PE investments.
Figure 4.27: Risk Measures

Respondents agreed that aligning of PE investments to the corporate investment strategies was a useful strategy as showed by 31% who strongly agreed, 50% that agreed, 8% disagreeing and none at 0% who strongly disagreed with 11% being neutral. The high mean and standard deviation attained ($M=4.03$, $SD=0.878$) attained favoured the use of this strategy to enhance PE investments.

Figure 4.28: Corporate Strategy Alignment

4.5.2 Commitment Strategies

Development of a commitment strategy towards PE investments as a strategy was favoured by respondents as shown by 44% who strongly agreed to it, 39% who agreed, both a 3% disagreeing and strong disagreeing leaving 11% adopting a neutral stand point. The high
mean and standard deviation attained (M=4.19, SD=0.951) leans in favour of this strategy being used as an enhancer in PE investments according to the study findings.

![Commitment Strategies Diagram]

**Figure 4.29: Commitment Strategies**

4.5.3 Regulation and Disclosure of information.

![Regulation and Disclosure Diagram]

**Figure 4.30: Regulation and Disclosure of information.**

From the findings, 42% of the respondents strongly agreed, 19% agreed, 6% disagreed and 3% strongly disagreed with 31% adopting a neutral standpoint on the development of regulations that call for more information disclosure as an enhancement strategy. The mean and standard deviation (M=3.92, SD=1.105) attained presented a strong neutral view point
that closed in on agreement that deemed the development of regulations that call for more information disclosure as a useful strategy enhance PE investments by investors.

4.5.4 Strengthening of local financial markets

As a strategy, the strengthening of the local financial markets was supported as a strategy by 38% respondents who strongly agreed to it, 43% who agreed, with 0% disagreeing, 8% strong disagreeing leaving 11% choosing to be neutral. The high mean and standard deviation attained (M=4.03, SD=1.003) recognized the implementation of this strategy as useful in enhancing PE investments according to the study findings.

![Figure 4.31: Strengthening of local financial markets](image)

4.5.5 Exit Market Development

![Figure 4.32: Establishment of a Kenyan PE Regulatory Authority](image)
Establishment of a local (Kenyan based) PE regulatory body as a strategy was appreciated as a strategy by respondents as shown by 56% who strongly agreed to it, 28% who agreed, 6% disagreeing, 0% strong disagreeing leaving 6% maintaining a neutral stand point. The high mean and standard deviation attained (M=4.28, SD=1.003) significantly recognized the implementation of this strategy as an enhancer in PE investments according to the study findings.

Figure 4.33: Exit Market Development

Respondents agreed that the development of the exit market was a useful strategy as showed by 41% who strongly agreed, 30% that agreed, 16% disagreeing and none at 0% who strongly disagreed with 16% being neutral. The mean and standard deviation attained (M=3.97, SD=1.067) showed that a strong view point was adopted that leaned towards agreement in its use as a useful strategy that can enhance PE investments.

4.6 Chapter summary

The chapter has presented result and findings from the study from the various statistical test used of frequencies and correlations. They have been presented in tabular and graphical format. Various positive and negative correlations with statistical significance observation that highlight unique relationships have been presented that will be discussed in detail in the next chapter, alongside the conclusion and suggested recommendations based on the study findings.
CHAPTER FIVE

5.0 DISCUSSION, CONCLUSIONS AND RECOMMENDATION

5.1 Introduction

This chapter discusses the study’s summary, results and findings in great length and detail thus drawing conclusions and making various recommendations in the end. The summary is discussed thematically while the findings and results are discussed in view of the theoretical and empirical literature. Afterwards, the study draws conclusions and makes recommendations based on the findings. Additionally, recommendations for practice and further studies are made.

5.2 Summary

The study sought to find what the determinants of fund manager’s investment in PE in Kenya were. The research questions were as stated; what is the effect of PE firm characteristics on the decision to invest in Private equity by fund managers? What are the effects of external factors on the decision to invest in Private equity by fund managers? What strategies can be used to enhance investment in private equity by fund managers?

The study used a descriptive research design that enabled it to be of qualitative nature targeting fund managers in Kenya within Nairobi. The study took on a census approach that gathered data from 22 registered RBA fund managers. Data was collected by use of questionnaire administration then analyzed using descriptive and inferential statistical test. Using descriptive statistics; frequencies, means and standard deviations were run while Pearson’s correlation test was used inferentially using SPSS.

The study targeted 40 respondents of whom 37 responded thus attaining a response rate of 93%. The types of funds managed originated from pension funds which were the most managed and present funds as supported by 23%, followed by investment banks at 20%, insurance at 19%, collective investment schemes at 15%, wealthy individuals at 14%, endowments at 7% and foundations at 2%. This goes hand in hand with a study by Gilligan & Wright (2010) that highlights pension funds, banks and insurance companies as the highest investors in private equity. Most fund managers had 4-6 years in experience in managing investor funds at 44%, followed by 1-3 years at 31%, 7-9 years at 19% and above 10 years at 6%. The study also found that out of the 40 respondents targeted, 83% invested in private equity while 6% did not. Respondents that did not invest in Private equity cited
the following reasons such investing in private equity not being in their business model, its need for extra attention due to little disclosures and restrictions by regulation of collective investment schemes which allows for little room for PE investments. The most amount of funds invested in PE in terms of range were of KES 0-200 million at 34% while the least in terms of range were KES 801-1 Billion. This goes to show the fund managers cautious approach while investing in PE. The most preferred form of private equity strategy as per the study was venture capital at 63%, followed by leverage buyouts at 32% and mezzanine financing at 5%. This shows that venture capital is highly preferred and is a more invested in form of private equity by fund managers. These findings go hand in hand with a study done by Gachoka (2012) who states that 45% of PE firms in Kenya adopt venture capital, 33% adopt leverage buyouts and 22% adopt mezzanine as PE financing strategies.

The PE firm characteristics were analyzed and were found to be of importance in the investment decision in PE by fund managers. These characteristics helped inform the fund managers of the various firm dynamics thus proving to be essential determinants in PE investments. The experience of PE managers within the PE firm (M=3.89), PE firm track performance record (M=4.11), local presence and maturity of the PE firm (M=4.16), deal activity of the PE firm (M=3.89), sector of investment by the PE firm (M=3.81), types of financing strategies used by the PE firm (M=4.05), value created in invested companies by the PE (M=4.24) and the PE firm ability to fundraise (M=4.19) were all of crucial to the fund manager’s decision to invest in PE.

The second research question addressed the importance of external factors to the investment decision in PE by fund managers. The most important factor was the illiquidity factor of PE investments (M=4.35) followed by trade sale as an exit strategy (M=4.14), return on investment of PE as an alternative investment class (M=4.11), number of successful recorded exits by PE firms (M=4.08), track record of positive returns on investment after exit in the PE market (M=4.05), availability of PE as a diversifier asset in a portfolio (M=4.0), maturity of the PE market (M=3.95), IPO issue as an exit strategy (M=3.95) and secondary Buyout as an exit strategy (M=3.84). Considering the existing number of PE firms in the PE industry (M=3.41) did not prove to have any impact on the investment decision in PE. Additionally, it was of no importance at all.

The study in its third research question sought to find out to what level of agreement the fund managers agreed to the various strategies to enhance PE. The fund managers agreed
with all strategies differently with establishment of a local (Kenyan based) PE regulatory body being most opted (M=4.28), followed by development of a commitment strategy towards PE investments (M=4.19), strengthening of the local financial markets (M=4.03), aligning of PE investments to the corporate investment strategies (M=4.03), development of the exit market (M=3.97), development of risk monitors/indicators in PE investments (M=3.94) and development of regulations that call for more information disclosure (M=3.92).

5.3 Discussion of findings

5.3.1 PE Firm characteristics and investment in Private equity.

The study found that all the PE firm characteristics were all important and impactful factors of consideration in the investment decision of fund managers when opting of PE investments. The experience of PE fund managers was statistically significant thus ascertaining Wilton (2012) observation that it’s an important differentiating factor in terms to the quality and perhaps the confidence it brings to investors who invest in PE funds as a form of investment. Experience potentially does translate into a meaningful skill-set such as a well-averse and decision making investment conscience that enhance consistent performance and proves to be a force to reckon for a manager among fellow peers.

Track record in terms of performance of the PE firm attained statistical significance thus proving a key factor of influence in the decision to invest in PE investments by fund managers. From the study by New Frontiers, 71.4% respondents were willing to invest in a PE firm where its members did not have an outstanding track record performance thus not attaching much weight to the influence a performance record in their investment decision. This aligns itself with Gohil and Vyas (2016) who pose that performance of PE funds increases with the funds flows from potential investors. Findings from the study come in favour of the same report where 73% of the fund managers cited having a track performance record to be of importance.

The respondents in the study agreed to the importance of having a local presence by a PE firm as a factor that they esteem highly in relation to their choice of investment in PE. Though not statistically significant as per the study findings, an AVCA (2016) report highlights key learnings from doing business in East Africa in which having a local presence is not only important but assists in bringing understanding on the in-dealings of identified markets, selection of partners and the creation of value in SME markets. The
fund managers based from the study share the same thought process as the report thus ascertaining the importance of a local presence by PE firms either locally or regionally. Additionally, the findings of the study agree with the sentiments of a report by EY & AVCA, (2013) that points to what having success in Africa by PE firms comes close to i.e. getting acquainted with a country, its macro story and market potential in terms of industrial growth in the private and public space.

The deal activity of a PE firm was viewed as important by the respondents but only proved statistically significant in relation to the amount invested by the fund managers. A possible hypothesis would be that the amount invested is determinant on how much in terms of public awareness the PE firm is known to be actively sourcing for investment deals to increase its bottom line and in the process fulfil its obligation to its various shareholders. In relation to this, Kaplan & Schoar, (2005) notes that deal activity of PE firms is on the rise as a result to meet the need to diversify into alternative assets.

The study showed that factoring in the sector investment by PE firms was important despite it not proving to be of any statistical importance in relation to the amount invested in PE and experience of the fund managers. Consequently, the focus on consumer-driven industries according to McPhee, (2015) contributes to its importance. Sommer (2013) states that focusing on selected drivers such as operating income growth is useful in making a strategy that helps investors choose the industry to invest in. Despite the study not finding this factor as significant, respondents appreciated its importance in line with Sommer (2013) observations.

The type of financing strategies used by PE firms proved to be of statistical importance as per the study. This supports Daglioglu (2016) observation on the importance of fund strategies used as they count in the life stage of the investment fund. More so, the study compliments Gachoka (2012) findings where by venture capital is the form most adopted by PE firms, followed by leveraged Buyouts and then Mezzanine. Venture capital was adopted by 63% of the fund managers, leverage buyouts by 32% and Mezzanine by 5%.

Value creation was the most important factor to consider in their investment decision. As a factor of influence, it measured up to be of statistical importance thus making it a key and needful aspect to the investment decision making criteria. By adding value to the invested company, not only do opportunities of a successful exit present themselves bringing along monetary rewards due to investors but also helps achieve a social economic impact through
betterment of environmental, social and governance policies. Loos (2006) adds that non-operational drivers such as the environmental, social and governance policies bring about impactful change and a much needed boost to the invested companies.

The ability of a PE firm to fundraise was also a crucial factor for the fund managers in their investment decision making criteria. According to Kaiser & Westarp (2010), they note that the firm that raise a significant amount of capital seem to be the best performing firms due to their in-house expertise and competency held by their own fund managers. Logically, investors are drawn to well performing investments and companies. Taking that into account, the ability to fundraise by a PE firm then becomes a key factor when making allocations to PE investments by fund managers.

Other characteristics viewed as important by fund managers were in terms of; the management, governance and regulation structure of the PE firm, ability to exit investments and contractual commitment of the firm and obligations therein.

5.3.2. External Factors

The study reveals that the existing number of PE firms did not count strongly to be a factor of importance. However, it did prove to be statistically significant in relation to the experience of the fund managers in investing investor funds. This can be attributed to PE becoming an alternative source of equity in emerging economies thus providing access to large pools of capital for projects based in different economic sectors such as health, energy and real estate. As the report by Ernst & Young, (2015) put it, PE fund raising and investments is now represented by more than 20% compared to the past. This highlights the progressive growth of the PE market thus identifying it as a key factor.

As the quote by Henry Kravis goes, “Don’t congratulate us when we buy a company, congratulate us when we sell it,” goes to depict one of the major purpose of any exit, a successful exit to be more specific. The trade sale was the only statistically significant exit strategy/route thus affirming the Asian Development Bank (2010) observations of them being more rampant in emerging markets. The fund managers viewed it as more important by a representation of 81% compared to the IPO at 76% and the secondary buyout at 76%. The findings of the study agree with the Asian Development Bank (2010) which observes that trade sales account for more exits in emerging economies. Additionally, the respondents favour Babarinde (2012) sentiments that IPO are preferred as exits in African
bourses but face a challenge of liquidity. The route of exit therefore matters to fund managers as they would desire to receive handsome returns upon exit.

The study reveals that the track record in the market of positive returns on investment after exit was of great importance to the fund managers and of statistical significance with a representation of 70%. Investments in PE are usually made with the end goal of a successful exit that translates into investors achieving the projected ROI. The report SAVCA (2014) show findings that investors would weigh heavily against their decision to allocate funds to PE when compared to the individual track records of the investment managers in a PE firm. Bearing in mind that these investment managers are representatives of the PE firm, the firm itself is taken to task on its market performance thus posing as image of either non-attraction or attraction to potential investments by different categories of risk averse investors.

Access to PE as an alternative asset class or diversifier investment has gained momentum over the past years as evidenced by increased allocations to the alternative asset class which have been permitted by regulatory bodies. Bosco and Bocconi (2011) states that investors face information asymmetries when looking into making investment in PE. The respondent’s attitude in the study is positively aligned with the caution given which shows the level of awareness towards the challenges posed by PE. In response to this, fund managers should take into consideration bringing large equity stakes as a bargaining chip for an acquisition strategy when getting into PE investments which spares them of a costly fact finding endeavor in terms of resources used and time. Consequently, this helps them to be more informed when making the PE investment decision.

The study revealed that return on investment of PE as an alternative asset was statistically significant with fund managers taking it in as an important factor in their investment decision protocol. This aligns well with Pedersen et al. (2014) statement that the returns of PE are considered highly in regards to the result of wealth creation as a result of diversification. Nonetheless, investors need to bear in mind as Lee, Kwon and Lee (2016) warns that PE investments require a high level of specialization to achieve superior returns due to the risks posed thus they should chose the well versed and highly experienced PE general partners.

The illiquidity nature of PE investments was the most important factor of consideration compared to the other factors. A majority of the respondents adopted it as the most
important factor to consider given its mean in their investment decision making protocol. Given the short span of a manager’s tenure in office, the illiquidity of PE investments and the j-curve effect that leads to a long-term horizon leave fund managers in a tight tussle in regards to wealth maximization and investment decisions despite the high returns thus accounting for its importance (Daglioglu, 2016). The findings of the study also go to support Mr Peter Anderson statement while in an interview that the j-curve effect that comes about due to illiquidity is a significant barrier to investments by fund managers who would like to make an impact in their short tenures in office. Therefore this adds to the caution concerning illiquidity by fund managers making it a key factor of importance to consider while investing in PE (Ashiagbor et al., 2014).

5.3.3 Strategies to enhance Investment in PE

The study revealed that the respondents agreed to the development of risk measures that can safeguard investments in PE as a key step in enhancing PE investments. As the most averse and common risk factor is illiquidity, fund managers should adopt the steps discussed in the study by Kojima and Murphy (2011). Diversification into PE bring great risk thus exposing the fund managers to uncertain market eventualities that are not often anticipated. Therefore, alignment of investment decisions in PE must be in line with the overall corporate investment strategy to avoid investment flops that put investors’ confidence and monetary investment at jeopardy. This goes to show the necessity and value of policies and frameworks that are built as a result of risk identification which are part of the corporate strategy. Fund managers need not only to know the risk mitigation strategies but have an in-depth understanding of their applicability (Kojima & Murphy, 2011).

The study also shows that having a commitment strategy to PE is important to fund managers. This echoes literature in the study by Oberli (2015) who advocates for its formulation and adoption. Given the clarity from which Oberli presents his case and presents suggestions to include in a recommitment strategy combined with the study’s findings, the researcher also supports the need to have both commitment and recommitment strategies that aid the strategic policy portfolio in terms to allocations to PE. The affirmative response of the fund managers goes also in tandem with De Zwart, Frieser and van Dijk (2007) main finding in their study that found it beneficial to have a recommitment strategy as it helps sustain a stable investment degree that brings it close to its target allocations while accounting for risk exposure to investors.
“Information is power,” as it said nowadays. This modern day proverbial statement comes true in the PE industry where information is limited to only those involved in the PE deals hence giving rise to the lack of transparency and full information disclosure perspectives by would-be investors. From the study, fund managers agreed to the development of regulations that call for more information disclosure while a noticeable 31% maintained a neutral position. As is discussed in the study’s literature, information disclosure brings with it different outcomes that are both positive and negative. The important question then would be, “What crucial gain would such a regulation of information disclosure to all investors have in order to strongly support it?” (Beuselinck et al., 2008).

A strong local financial market is crucial for PE investments when they approach the exit stage. Klonowski (2011) alludes that the strength of a local financial market can present itself as foe or friend depending on the efficiency and the overall market liquidity position. From the study’s findings, the fund managers strongly agreed to this as a way that investments in PE can be enhanced. Nonetheless, it should be understood that the strengthening of these markets is not an overnight affair or a one man show as many factors are constantly in play. Kelly (2012) emphasizes on the importance and need to have strong financial markets that have depth and liquidity as this enhances exit option such as IPO’s, the availability of financial leverage and investment capital.

According to Povaly (2007), a well-developed exit market does not only ensure attractive returns but also possesses potential to enable raising of capital a second round for the next investment. 70% of the fund managers appreciated this strategy as a way to enhance PE investments into the country. In light of this, then the question would be, “What exit route is highly favoured by the Kenyan market?” The answer to this, which is the trade sale according to the literature in the study that is also backed up by preference of the fund managers can then be used to provide insight into what methodologies and platforms can be adapted to enhance it while also not ignoring the IPO and leverage buyout exit routes. Orata A (2008) sights regulatory constraints that make the IPO a less attractive and common exit route. This in turn has the potential to negatively contribute to the development of the exit market thus shunning investors who target IPO as their main core strategies.

Lastly, the establishment of a local (Kenyan based) PE regulatory body was the strategy that gained most approval by the fund managers. This affirmation of this strategy by fund
managers supports Orata A (2008) recommendations in her study which advocate for its setup. She goes on to compare its potential benefits, if set up to that of the Kenya Bankers Association which has had successful collaborations with the main regulatory body of banks, the Central Bank of Kenya. The researcher also agrees with this view that such a regulatory body would be of great significance thus accelerating the growth and development of the exit market and the entire PE industry at large

5.4 Conclusions

5.4.1 PE Firm characteristics and investment in Private equity.

The study concluded that the value created in invested companies, ability to fundraise, having a local presence and maturity presence, firm track performance record, the types of financing strategies used by the PE firm (LBO’s, Venture capital), the experience of PE managers within the PE firm, the deal activity of the PE firm e.g. locally regionally and internationally and the sector of investment by the PE firm e.g. healthcare, real estate were all of importance and meaningful impact to the investment decision in private equity fund allocation by fund managers.

5.4.2 External Factors

The study concluded that the illiquidity factor of PE investments, trade sale as an exit strategy, the ROI of private equity as an alternative investment class, the number of successful recorded exits by PE firms, the track record of positive ROI after exit, the availability of PE as a diversifier asset in a portfolio, the maturity of the PE market, IPO issue as an exit strategy, secondary buyouts as an exit strategy and the existing number of PE firms in the PE industry all had an impact on the investment allocation of funds to PE by fund managers in various degrees as supported by the findings and elaborated in the discussions of the study.

5.4.2 Strategies to enhance Investment in PE

The study also concluded that the establishment of a local (Kenyan based) PE regulatory body, development of a commitment strategy towards PE investments, the alignment of PE investments to the corporate investment strategies, strengthening of the local financial markets, the development of the exit market, the development of risk monitors/indicators in PE investments and the development of regulations that call for more information disclosure were all strategies that would prove beneficial if formulated and implemented.
This is in line with the affirmation that the fund managers brought forth as per the findings of the study.

5.5 Recommendations

5.5.1 Suggestions for improvement

5.5.1.1 PE Firm characteristics impacting investment in PE

The study concluded that PE firm characteristics have an impact on the investment decision in PE by fund managers. Therefore, fund managers are recommended to always perform due diligence surrounding the characteristic posed by the PE firm and where they direct their fund investments. This goes ahead to prevent any agency problems that may arise.

5.5.1.2 Selected External Factors impacting investments in PE.

The study concluded that the selected external factors do have an impact on the decision to invest in PE in Kenya and are of importance to the fund managers. Therefore, fund managers are recommended to extensively perform their due diligence on these factors bearing in mind that they are not within their control unlike the choosing a firm with the needed characteristics. Additionally, the fund managers are recommended to consult other experts within the professional field of PE investments to provide constructive and well informed advice which can prove beneficial in terms of manoeuvring around risks and other unexpected outcomes. Lastly, the study also recommends that fund managers should also benchmark against other countries which have financial markets that allow the private equity market to thrive to see what external factors affect investments in private equity.

5.5.1.3 Strategies to enhance PE investments.

The study concluded that all the strategies being investigated gained affirmative support from the respondents. It is therefore recommended that the fund managers adopt these strategies as they help in steering through risks posed by PE investments. It is also recommended that the fund managers should research and benchmark against strategies that other investors are using in the BRICS countries with the aim of improving their investment and allocation portfolio strategies.
5.5.2 Recommendations for Further Research

The study recommends that more research should be done on other factors that are potential influences to investments in private equity within the Kenyan context. These factors include; financial cost and implications, deal structuring between GP’s and LP’s, management and oversight of the private equity fund and agency cost and taxation. Additionally, the researcher recommends for investigation into the current strategies used by fund managers to determine their allocations to private equity for the purpose of finding out their effectiveness and improvement.

The study was limited to the registered RBA fund managers as limited partners with the PE firm coming under examination of the study. The study recommends that research should be conducted on the PE firms as general partners revolving the criteria that they take into consideration when engaging limited partners such institutional investors to come on board as potential investors.
REFERENCES


Robertson, J. (2017). Emergent new finance: hedge funds and private equity funds in East


APPENDICE

Appendix I: Cover Letter

TO WHOM IT MAY CONCERN.

6th August, 2018

Dear Sir/Madam,

REF: PERMISSION TO CONDUCT RESEARCH – KINYUA MARVIN MWENDA
STUDENT ID. NO. 636544

The bearer of this letter is a student of United States International University (USIU) -Africa
pursuing a Master of Business Administration.

As part of the program, the student is required to undertake a dissertation on “Determinants of
Fund Managers Investments in Private Equity in Kenya” which requires him to collect data.

Please note that information provided will be treated with utmost confidentiality and will only be
used for academic purposes.

Kindly assist the student get the appropriate data and should you have any queries contact the
undersigned.

Yours Sincerely,

[Signature]

Prof. Amos Njuguna,
Dean – School of Graduate Studies, Research and Extension
Tel: 730 116 442
Email: amnjuguna@usi.ac.ke
Appendix II: Questionnaire

RESEARCH QUESTIONNAIRE
The purpose of this study is to collect data that will assist in identifying the determinants of investment by fund managers in private equity in Kenya. The information collected will be treated as confidential and used only for the purpose of the study. For any inquiry you may have, kindly contact me on 0735-146-063 | mkinyua2@usi.ac.ke and I will be glad to respond.

Instructions:
Please fill-in the questionnaire provided by ticking appropriately or filling in as directed.

Section 1: General information
Kindly tick (√) the appropriate answer in the box.

1. Please tick against your age group bracket.
   ( ) 20-30 years       ( ) 41 – 50 years       ( ) Above 61 years
   ( ) 31-40 years       ( ) 51-60 years

2. What are the type of investor funds that you manage? (Tick all that applies, please)
   ( ) Pension Funds       ( ) Wealthy individuals
   ( ) Endowments          ( ) Foundations
   ( ) Insurance companies ( ) Collective investment schemes
   ( ) Investment Banks

3. How many years of experience do you have in managing investor funds?
   ( ) 1-3 years           ( ) 7-9 years
   ( ) 4-6 years           ( ) Above 10 years

4. What is the overall size of the fund that you manage?
   ( ) 0-200 million       ( ) 1 - 10 Billion
   ( ) 201-400 million     ( ) 11 - 20 Billion
   ( ) 401-600 million     ( ) 21 - 30 Billion
   ( ) 601-800 million     ( ) 31 - 40 Billion
   ( ) 800-1 Billion       ( ) 41 Billion and above
5. Do you invest in Private Equity? If no, kindly state the reason why you do not.  
( ) Yes  ( ) No

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6. If yes, what amount of funds do you invest in Private equity? (kindly tick to that which applies)

( ) 0-200 million       ( ) 1 - 10 Billion
( ) 201-400 million     ( ) 11 - 20 Billion
( ) 401-600 million     ( ) 21 - 30 Billion
( ) 601-800 million     ( ) 31 - 40 Billion
( ) 800-1 Billion       ( ) 41 Billion and above

7. If yes, what forms of Private equity strategies do you invest in?

( ) Venture Capital    ( ) Leveraged Buyouts (LBO’s)    ( ) Mezzanine

( ) Other’s (please specify) .................................................................

Section 2: -A) Private Equity Firm characteristics

Kindly tick (√) the appropriate answer in the box. Please note: PE represents Private Equity.

What degree of importance would you attach to the following in regard to your decision if you were to invest/you are already investing in Private equity? Where is 1- Not important 2- Less important, 3- Neutral, 4- Important, 5- Very important

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
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</thead>
<tbody>
<tr>
<td>Experience of PE managers within the PE firm</td>
<td></td>
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<td>PE firm track performance record</td>
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<td>Local presence and maturity of the PE firm</td>
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<tr>
<td>Deal activity of the PE firm e.g. locally regionally and internationally</td>
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<tr>
<td>Sector of investment by the PE firm e.g. healthcare, real estate</td>
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<tr>
<td>Types of financing strategies used by the PE firm (LBO's, Venture capital)</td>
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<tr>
<td>Value created in invested companies by the PE</td>
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<tr>
<td>PE firm ability to fundraise</td>
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</tbody>
</table>
What other characteristic would you consider as important to your decision?
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Section 2: -B) External factors

Kindly tick (√) the appropriate answer in the box.

What degree of importance would you attach to the following in regard to your decision if you were to invest/you are already investing in Private equity? Where is 1- Not important 2- Less important, 3- Neutral, 4- Important, 5- Very important

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td>Existing number of PE firms in the PE industry</td>
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<tr>
<td>Maturity of the PE market</td>
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<td>Number of successful recorded exits by PE firms</td>
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<tr>
<td>IPO issue as an exit strategy</td>
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<td>Trade sale as an exit strategy</td>
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<tr>
<td>Secondary Buyout as an exit strategy</td>
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<tr>
<td>Track record of positive returns on investment after exit in the PE market</td>
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<tr>
<td>Return on investment of PE as an alternative investment class</td>
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<tr>
<td>Availability of PE as a diversifier asset in a portfolio</td>
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<tr>
<td>Illiquidity factor of PE investments</td>
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</table>

What other external factor would you consider as important to your decision?
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Section 2: - C) Strategies to enhance PE investments

Kindly tick (√) the appropriate answer in the box.

To what extent do you agree that the following strategies can enhance investments in Private equity in the industry by fund managers? Where is 1- Strongly disagree 2- Disagree, 3- Neutral, 4- Agree, 5- Strongly Agree.
<table>
<thead>
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<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Development of risk monitors/indicators in PE investments</td>
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<tr>
<td>Aligning of PE investments to the corporate investment strategies</td>
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<tr>
<td>Development of a commitment strategy towards PE investments</td>
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<tr>
<td>Development of regulations that call for more information disclosure</td>
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<tr>
<td>Establishment of a local (Kenyan based) PE regulatory body</td>
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<tr>
<td>Strengthening of the local financial markets</td>
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<tr>
<td>Development of the exit market</td>
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</table>

What other strategies would you recommend be put in place to enhance Private Equity investments locally?

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Thank you for taking time to fill in this questionnaire.
## Appendix III: Registered Fund Managers

<table>
<thead>
<tr>
<th>REGISTERED FUND MANAGERS - 2018</th>
<th>TELEPHONE</th>
<th>POSTAL ADDRESS</th>
<th>PHYSICAL LOCATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>2. Allan Gray Kenya Limited</td>
<td>20 5147016</td>
<td>3946-00619, NAIROBI</td>
<td>2nd Floor, Eaton Place, United Nations Crescent</td>
</tr>
<tr>
<td>3. Alpha Africa Asset Managers Limited</td>
<td>2595448</td>
<td>34530-00100, NAIROBI</td>
<td>Crawford Business Park, 4th Floor Suite 26, State House Road</td>
</tr>
<tr>
<td>4. Amana Capital Limited</td>
<td>2351738</td>
<td>9480-00100, NAIROBI</td>
<td>Block C, Suite C5, Saachi Plaza, Argwings Kodhek Rd</td>
</tr>
<tr>
<td>5. Apollo Asset Management Company Limited</td>
<td>3641000</td>
<td>30389-00100, NAIROBI</td>
<td>Apollo Centre, Ringroad, Westlands</td>
</tr>
<tr>
<td>7. CBA Capital Limited</td>
<td>2884444</td>
<td>30437-00100, NAIROBI</td>
<td>CBA Centre, Mara &amp; Ragati Roads</td>
</tr>
<tr>
<td>8. CIC Asset Management Limited</td>
<td>2823000</td>
<td>59485-00200, NAIROBI</td>
<td>8th Floor, CIC Plaza II, Mara Road</td>
</tr>
<tr>
<td>9. Co-op Trust Investment Services Limited</td>
<td>3276000</td>
<td>48231-00100, NAIROBI</td>
<td>Co-operative Bank House, Haile Selassie Avenue</td>
</tr>
<tr>
<td>11. Fusion Investment Management Limited</td>
<td>2738460</td>
<td>47538-00100, NAIROBI</td>
<td>1st Floor, ACK Garden House, 1st Ngong Avenue</td>
</tr>
<tr>
<td>12. Genafrica Asset Managers Limited</td>
<td>2323343</td>
<td>79217-00200, NAIROBI</td>
<td>1st Floor, Arlington Block, 14 Riverside Drive, Westlands</td>
</tr>
<tr>
<td>13. Genghis Capital Limited</td>
<td>709185000</td>
<td>9959-00100, NAIROBI</td>
<td>1st Floor, Purshottam Place, Westlands Road</td>
</tr>
<tr>
<td>No.</td>
<td>Company Name</td>
<td>CR No.</td>
<td>Phone No.</td>
</tr>
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</tr>
<tr>
<td>14</td>
<td>ICEA Lion Asset Management Limited</td>
<td>2221652</td>
<td>46143-00100, NAIROBI</td>
</tr>
<tr>
<td>15</td>
<td>Kenindia Asset Management Company Limited</td>
<td>316099</td>
<td>44372-00100, NAIROBI</td>
</tr>
<tr>
<td>16</td>
<td>Madison Asset Management Services Limited</td>
<td>2864502</td>
<td>20092-00100, NAIROBI</td>
</tr>
<tr>
<td>17</td>
<td>Nabo Capital Limited</td>
<td>2286000</td>
<td>10518-00100, NAIROBI</td>
</tr>
<tr>
<td>18</td>
<td>Natbank Trustees and Investment Services Ltd</td>
<td>2828356</td>
<td>72866-00200, NAIROBI</td>
</tr>
<tr>
<td>19</td>
<td>Old Mutual Investment Group Limited</td>
<td>2829000</td>
<td>11589-00400, NAIROBI</td>
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<tr>
<td>20</td>
<td>Sanlam Investments East Africa Limited</td>
<td>4967000</td>
<td>67262-00200, NAIROBI</td>
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<tr>
<td>21</td>
<td>Stanlib Kenya Limited</td>
<td>3268508</td>
<td>30550-00100, NAIROBI</td>
</tr>
<tr>
<td>22</td>
<td>Zimele Asset Management Company Limited</td>
<td>2246273</td>
<td>76528-00508, NAIROBI</td>
</tr>
</tbody>
</table>

Appendix IV: NACOSTI Research license