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Private Debt, Private Equity and Real Estate in Middle East and Africa

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Introduction

Over the preceding year, marked by unprecedented developments, we witnessed notable macroeconomic shifts, including record-high inflation rates and an aggressive monetary policy tightening campaign across advanced economies.

Such headwinds have precipitated a global downturn, injecting a considerable degree of uncertainty into markets. Private markets, in turn, have borne significant pressure in light of such headwinds in 2023, albeit with some notable exceptions across strategies and regions.

In 2024, a more optimistic landscape emerges, fuelled by expectations of major central banks implementing rate cuts and inflation stabilising at levels close to target. This optimism sets the stage for a potential resurgence in private market activity. Nevertheless, a broader sense of uncertainty is still expected to linger, driven in part by geopolitical tensions, the prospect of a significant shift in the global political order amid the numerous elections slated for 2024, and persistent macroeconomic challenges.

Against this intricate backdrop, we delve into the examination of how these conditions will influence the outlook for private markets in 2024. Our comprehensive series of reports will scrutinise the prospects for three specific asset classes — **private debt, private equity and real estate** — across diverse geographical regions, in light of developments in each region. Accordingly, we provide insights into how investors across various segments can navigate current market dynamics, leveraging opportunities strategically to their advantage.

Macroeconomic overview

Inflationary dynamics across the MEA region have exhibited significant variation. Gulf nations have maintained relatively stable rates due to their currency pegs, in contrast to African nations contending with elevated inflation amidst currency volatility. These divergent trends underscore the diverse economic landscapes within the MEA region, from oil-centric economies witnessing fluctuations in global oil prices to non-oil African nations striving for economic stability.

Despite this diversity, the overall outlook for 2024 maintains some optimism, fuelled by a gradual resurgence in oil-exporting countries and persistent efforts towards economic diversification in non-oil sectors.

Monetary policy responses within the MEA region mirror global trends, with central banks adopting tightening measures in response to supply shocks emanating from supply chain constraints and geopolitical tensions. Consequently, interest rates remain elevated throughout the region, reflecting both global economic conditions and domestic factors. The outlook for interest rates within the region is mixed, as economies must weigh the imperative of keeping rates high to curb inflation against the necessity of aligning interest rates with the US Federal Reserve to prevent undue currency devaluation, which would fuel second-round inflationary impacts via cost-push inflation.

Consequently, projections for GDP growth in 2024 present a nuanced landscape, with oil-exporting countries poised to benefit from still elevated global energy prices, despite lower oil production, and diversification to non-oil sectors, while African economies navigate through structural reforms and infrastructure improvements. Moreover, prevailing geopolitical tensions, particularly in the Middle East, significantly influence economic stability, fostering an environment of uncertainty that may impede foreign direct investment and impact broader the economic climate.

Nevertheless, amidst these challenges, the MEA region presents avenues for cautious optimism and strategic investment in private asset classes, including that of private equity, private debt and real estate. The region's economic diversity and robust consumer base growth offers potential to foster sustainable growth in 2024 and beyond, notwithstanding the challenges posed by the prevailing economic dynamics.

Private equity

Mergers and acquisitions (M&A) in the MEA region experienced a notable downturn in 2023, marking the lowest levels in nearly a decade both in terms of transaction value and volume.

The year saw 1,062 deals totalling $45.6 billion, a significant decline from the 1,412 transactions valued at $76.6 billion in 2022. This decline underscores a departure from the robust M&A activity witnessed in previous years, especially due to the withdrawal of private equity firms relying on debt financing, reflecting a broader trend of global uncertainty.[1]

Indeed, fundraising in 2023 experienced a significant slowdown when considering the MEA region, amounting to $5.7 billion, a stark contrast to the $10.7 billion raised the year before, though 2022's figure was an outlier historically.[2] Traditionally, governments have been the primary source of investment capital in the Middle East. However, there are indications of diversification in the fundraising landscape.[3] Several general partners (GPs) have recently established offices in the region, while new funds are actively seeking external commitments from limited partners (LPs), suggesting a shift towards a more varied investor base in the region.

Historically, private equity in the MEA region has seen sporadic bursts of high-value deals, focused mainly on strategic sectors like energy, infrastructure, and real estate due to abundant natural resources and growing consumer markets. However, challenges like commodity price fluctuations, geopolitical tensions, and regulatory uncertainties have hindered sustained activity. Economic downturns, like the 2008 global financial crisis and the 2014 oil price crash, have also had impacts on investor confidence.

Nonetheless, recent years have seen a notable investment shift towards non-oil sectors in the MEA region, particularly within the Gulf Cooperation Council (GCC), driven by diversification strategies. This transition is marked by increased investments in technology, healthcare, education, and consumer goods, in a bid to foster long-term economic growth. Technology, media, and telecommunications led in M&A volume (173 deals) in MEA region in 2023, while materials rank first in deal value ($11.0 billion).[4] Historically, the Middle East relied heavily on oil and gas, but private equity now offers a pathway to diversify away from these sectors, aligning with their economic strategies.

Regulatory reforms across the MEA have enhanced the investment climate for private equity firms, promoting transparency and investor confidence.

Initiatives like Saudi Arabia's Vision 2030 and legislative changes in the UAE have streamlined business regulations and attracted foreign capital into sectors such as technology and healthcare.[5,6] Egypt's economic reform program has similarly improved corporate governance standards, fostering a more investor-friendly environment in industries like infrastructure and manufacturing.[7] Such reforms have prompted private equity players to redirect their attention towards the MEA region, leveraging partnerships with wealthy sovereign wealth funds and influential families. This shift is crucial given current fundraising challenges worldwide, amidst hopes that such partnerships could help alleviate such issues.

Looking ahead, the future outlook for private equity in the MEA region appears promising, driven by favourable demographic trends, economic diversification initiatives, optimal location as hub between East Asia and Europe, and increasing investor interest the region.[8]

Despite optimism for the future of private equity in the region, there are downside risks.

Elevated interest rates, particularly in emerging economies battling inflation persistence, may lead to wide bid-ask spreads, selective offerings, and hinder exit pathways for some time. This uncertainty could dampen investment returns and fundraising efforts.

Moreover, structural barriers, such as legal complexities, hinder deal execution and exit strategies, especially in non-GCC countries. Geopolitical instability and regional conflicts further threaten investment stability, requiring careful risk management, local expertise, and strategic partnerships to seize growth opportunities while minimising risks.

Private debt

Historically, the concept of private debt as an investment avenue within the broader MEA region was largely overlooked by investors. This disregard stemmed from its perceived lower returns compared to private equity and the hesitance surrounding less liquid debt instruments. Notably, the Middle East witnessed only a handful of local debt funds engaging in mezzanine financing activities a decade ago.[9]

However, prevailing sentiments among investors have undergone a notable shift in recent times.

Factors contributing to this shift include the comparatively subdued performance of private equity, the allure of potentially higher returns in private debt amidst\tighter monetary policies, and the scarcity of viable high-yield and distressed debt opportunities within the region.[10]

Indeed, while fundraising for private debt slowed in 2023, to $1.4 billion, from $2.7 billion in the year prior, 2023's figure was still historically elevated.[11] Mirroring global trends, the MEA private debt market stands poised to capitalise on the withdrawal of traditional banking institutions, amidst stringent regulatory frameworks and a cautious lending climate. Consequently, private debt funds are increasingly being recognised as a viable financing alternative for businesses, particularly in regions where access to conventional financial services remains restricted.

A discernible financing gap exists in the current market landscape, notably for transactions falling within the $25 million to $50 million range.[12] This deficiency has left numerous SMEs (Small and medium-sized enterprises) without adequate debt financing, thereby positioning private credit as a promising solution to address this shortfall in the region.

This trend is further underscored by the expanding consumer base within the region, which has served to bolster SME growth. However, without requisite financial backing, SMEs may encounter challenges in sustaining their operations. Consequently, regulatory bodies within the MEA region have taken proactive measures to foster the growth of private credit, aiming to alleviate financing constraints. For instance, the regulatory framework introduced by the Financial Services Regulatory Authority (FSRA) of the Abu Dhabi Global Market (ADGM) intends to facilitate the origination and investment activities of private credit funds within the ADGM jurisdiction.

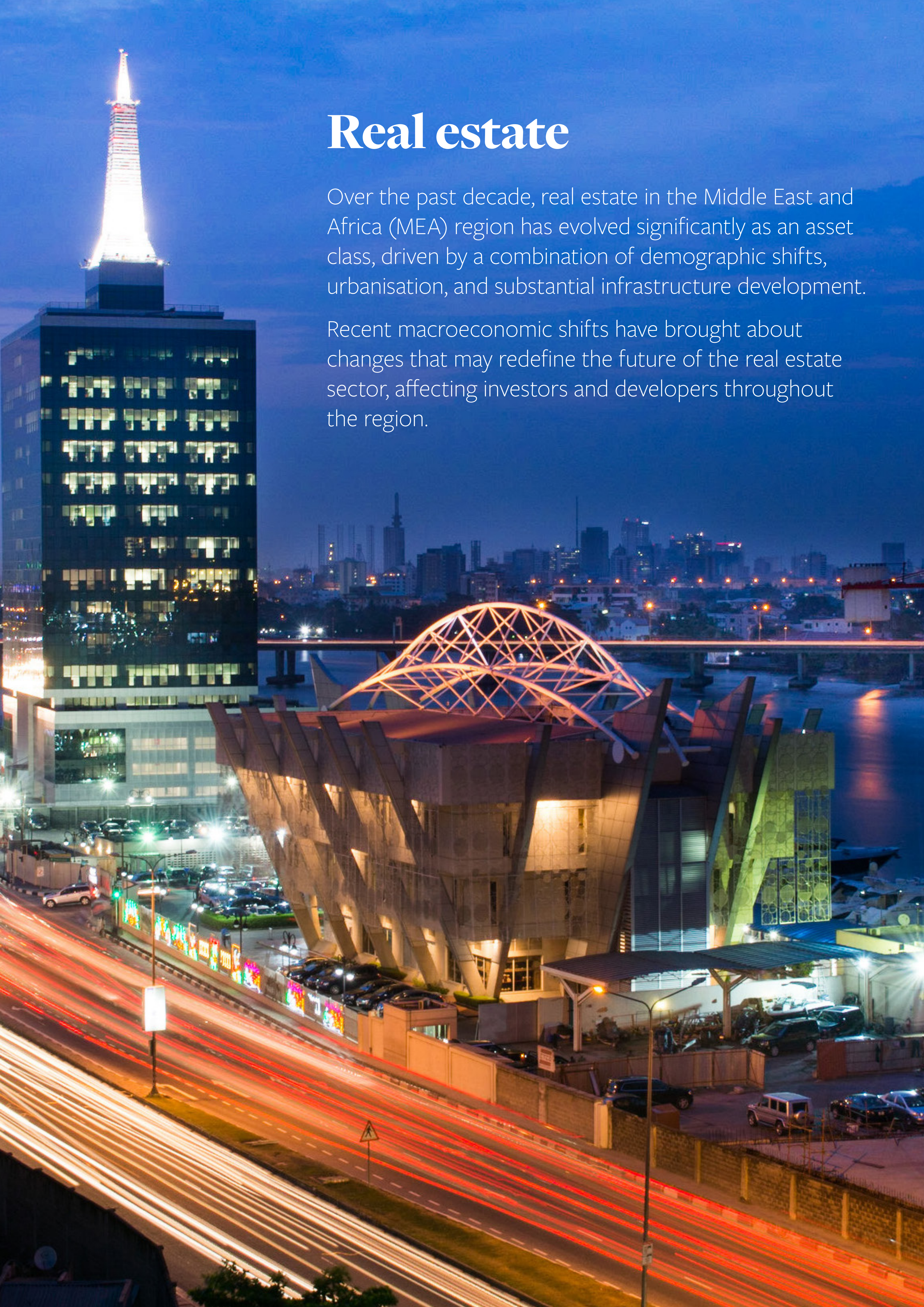
Moreover, indications of a burgeoning appetite for private debt are discernible among sophisticated sovereign wealth funds and family office institutions, backed by affluent families.[13] These entities are incentivised by the prospect of achieving returns comparable to those historically yielded by private equity, albeit without the accompanying volatility associated with buyout activities. This trend suggests a potential shift in the private debt market landscape within the region, as increasing participation from sophisticated investors could lead to greater diversification, innovation, and competition, ultimately reshaping the dynamics and opportunities in the sector moving forward.

Looking ahead, the future outlook for private debt within the MEA region appears promising. As traditional financial institutions continue to recalibrate their strategies in response to evolving regulatory landscapes, private debt stands poised to emerge as an increasingly vital component of the regional financial ecosystem. The ongoing commitment of regulatory bodies and the growing interest from investors further signal a sustained trajectory of growth and development for the private debt market within the MEA region.

Real estate

Over the past decade, real estate in the Middle East and Africa (MEA) region has evolved significantly as an asset class, driven by a combination of demographic shifts, urbanisation, and substantial infrastructure development.

Recent macroeconomic shifts have brought about changes that may redefine the future of the real estate sector, affecting investors and developers throughout the region.



These changes are evident in the fundraising arena for real estate in the MEA region, which experienced a slowdown in 2023, totalling $1.1 billion, a decrease from $2.1 billion in 2022. This figure for 2023 marks the lowest level of fundraising recorded since 2018.[14]

The prevailing macroeconomic climate has posed challenges to real estate financing in the MEA region, with liquidity-constrained banks limiting cheap financing options. Such a development has compelled real estate developers and investors to adapt their business models and strategies to navigate these challenges. This adaptation involves redefining operating models, optimising asset management practices, and exploring alternative financing avenues to mitigate risks and capitalise on emerging opportunities.[15]

Stakeholders are also prioritising value creation strategies to maximise returns from existing land and property portfolios. This trend is particularly evident among large real estate portfolio owners, who are actively exploring opportunities for value optimisation and cashflow generation across their assets.

Governments in the GCC region are increasingly embracing public-private partnership models to enhance private sector participation in real estate development initiatives, leveraging sovereign wealth funds to support such endeavours. For example, in Saudi Arabia, the King Abdullah Financial District is a significant project aimed at creating a major financial hub. In the United Arab Emirates, the Dubai public-private partnership law facilitates projects like the Al Maktoum International Airport expansion. Meanwhile, in Africa, the Eko Atlantic City in Nigeria is a notable initiative, where reclaimed land is being developed into a new bustling economic zone intended to alleviate the urban constraints of Lagos.

In the past, conventional debt and equity structures have largely dictated real estate financing in the MEA region. Yet, a noticeable shift is occurring towards more diverse and inventive financing approaches. This transition has seen the rise of private real estate funds, club deals, and the advent of real estate investment trusts (REITs).[16] Notably, the implementation of REIT regulations in GCC economies offers investors access to varied revenue sources, simultaneously reducing risk exposure and fundamentally altering the sector's financing landscape, amidst tighter monetary conditions and the subsequent challenges associated with debt financing.[17] Nonetheless, the maturity and acceptance of REITs vary significantly across the region, which in turn will affect investment flows.

Moreover, the increasing demand for affordable housing and changing consumer tastes have instigated a transition towards experiential offerings within the region. Developers and investors are now prioritising comprehensive experiences over conventional products, in line with the requirements of urbanisation and demographic shifts. With developers showing a strong inclination towards adaptability and innovation, coupled with the demand for these offerings, ample opportunities for expansion persist, promising favourable prospects for real estate investors.

As mega-projects advance in the Gulf and urbanisation spurs growth in the African real estate market, the region's real estate sector is poised for continued transformation and growth. This trajectory is fuelled by innovation, adaptability, and strategic collaborations, painting a promising picture for real estate as an asset class in the region.

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Opportunities for new funds/emerging trends in Middle East and Africa

Degree of opportunity for private asset markets posed by macroeconomic conditions

Development	Degree of opportunity for asset class
Regulatory changes, reforms and elections	
Regulatory reforms throughout the MEA region have markedly enhanced the investment environment, boosting foreign direct investment and strengthening corporate governance. For example, Saudi Arabia's Vision 2030 aims to diversify the economy and increase private sector participation, and the UAE has updated its business laws to simplify market entry and operations for foreign companies. However, given that this is an election year in many African countries, there may be more challenging governmental conditions, potentially leading to adverse effects on the commitment to improving regulatory frameworks essential for the growth of various asset classes.	HIGH / **MEDIUM ✓** / LOW
Diversification away from oil sectors	
Many countries within the MEA region, particularly those in the GCC, are actively pursuing strategies to diversify their economies beyond traditional oil and gas sectors. This shift includes substantial investments in sectors such as renewable energy, technology, healthcare, and education. By diversifying their economic bases, these countries aim to create more sustainable and resilient economic structures that are less susceptible to global oil price fluctuations and can offer a broader range of opportunities for investors.	**HIGH ✓** / MEDIUM / LOW
Geopolitical instability and regional conflicts	
The MEA region, while rich in opportunities, is also prone to geopolitical tensions and conflicts, which can significantly deter investment. These instabilities can disrupt markets, pose risks to physical assets, and create unpredictable operational and financial challenges for investors. Such environments require robust risk management strategies and often necessitate higher returns to compensate for increased risks, potentially limiting the range of investors willing to engage in the region.	HIGH / MEDIUM / **LOW ✓**
Access to financing amidst tighter monetary conditions	
Tightening monetary policies globally and regionally have led to higher interest rates and reduced liquidity, which pose challenges particularly in sectors like real estate and private equity that rely heavily on financing. Banks have become more cautious, and traditional lending has contracted, leading to a gap that private debt instruments could potentially fill. This environment offers an opportunity for private debt markets to expand but also presents challenges as costlier financing can deter new projects and slow down economic activity.	HIGH / **MEDIUM ✓** / LOW
Growing consumer markets and urbanisation	
The MEA region is experiencing rapid demographic changes, including population growth and urbanisation, which drive demand in real estate and necessitate enhanced infrastructure and services. This shift supports the growth of consumer markets and increases the demand for residential and commercial real estate development. Urbanisation also presents opportunities for private debt and equity to finance infrastructure projects, real estate developments, and SMEs that cater to these expanding urban populations.	**HIGH ✓** / MEDIUM / LOW

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Key contacts

Pazani Vaitilingon
CHIEF COMMERCIAL OFFICER AFRICA, INDIA AND MIDDLE EAST

E pazani.vaitilingon@iqeq.com
T +230 213 8961
M +230 5255 0032

Tariq Nakhooda
COUNTRY HEAD, UAE

E tariq.nakhooda@iqeq.com
T +971 5028 68207

Joe Ives
COMMERCIAL DIRECTOR, UAE

E joseph.ives@iqeq.com
T +971 5471 17354

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