

Private equity exits: Will the new Competition Commission merger guidelines stifle or encourage investment appetite?

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In any private equity investment life cycle, the exit environment is a fundamental factor.

For a seller, finding a financially capable and *bona fide* buyer to acquire the asset being disposed is crucial, having regard to while a buyer does not have any statutory protection on acquisitions, and together with the acquisition of an asset, a buyer inherits and takes on the obligations and commitments underlying an asset post-closing.

In this article, we consider some of the impact of the Competition Commission's ("**Commission**") merger guidelines on private equity exit transactions.

Just two months ago (September 2023), the Southern African Venture Capital & Private Equity Association ("**SAVCA**") published its yearly Private Equity Industry Survey setting out the performance of Southern African private equity firms ("**PE**") for the year of 2022.

The survey states that, despite tough environments, PE firms remain resilient in driving revenue and employment growth within underlying portfolio companies. Furthermore, despite a 13% fundraising decline globally, R19.6bn in funds were raised during 2022, which is 21% higher than in 2021.

Despite multiple challenges, SAVCA points out that Southern Africa PE firms witnessed a strong increase in both the value of exit proceeds and the number of exits.

The quality and volume of exits will be a key consideration for any new investor looking to make acquisitions in any market. The role of regulatory authorities is also a key component in the market.

The Commission is mandated to consider public interest conditions during the assessment of reportable mergers and acquisitions.

Recently, the Minister of Trade, Industry and Competition, Minister Patel, pointed out how "*R20-billion in salaries had been preserved as a direct result of these public interest interventions, while approximately 143 000 workers are now shareholders in their respective companies, thanks to the expansion of public interest criteria.*"[1]

The approach being applied by the Commission is that transactions will be thoroughly interrogated and there is an unequivocal commitment by government to use public interest conditions as a strategic tool for advancing economic transformation.[2]

On 6 October 2023, the Commission invited stakeholders and interested parties to submit comments on the draft revised Public Interest Guidelines related to merger control (**Draft Guidelines**).

In 2019, there were amendments to the Competition Act[3], among other things, to "*explicitly create public interest factors that address ownership, control and support to small businesses and firms owned or controlled by historically disadvantaged persons*".[4]

Of particular interest for the purposes of this article on public interest assessments, is the Commission's approach to the public interest provision referred to in section 12A(3)(e) of the Competition Act.

The explanatory note to the amendments to the Competition Act explained that the amendments envisaged, amongst other things, an established framework that incentivises merging parties and active firms to "*proactively address concentration and ownership representativity concerns arising in markets in which they are active.*"[5]

Therefore, all notifiable mergers and acquisitions will be tested against the public interest provision referred to in section 12A(3)(e) of the Competition Act.

Section 12A(3)(e) of the Competition Act requires, when determining whether a merger can or cannot be justified on public interest grounds, consideration of "*the promotion of a greater spread of ownership, in particular to increase the levels of ownership by historically disadvantaged persons and workers in firms in the market.*"

This legislative provision is a feature of every merger assessment, which may very well have a major impact on the overall public interest assessment.

With section 12A(3)(e) in mind, the Draft Guidelines propose that the Commission will consider the following factors (which have been summarised), amongst others, to establish the effect of the merger in question on this public interest provision —

- the extent of the dilution and/or increase of the historically disadvantaged persons and/or worker shareholding within the target firm post-merger;
- the breadth of representation of the shareholding and sector transformation targets;
- the extent of participation of historically disadvantaged persons/worker in the operations of the merged entity;
- the size of the merger parties' respective operations in South Africa;
- whether the acquiring firm is transformed;
- it is also worth noting that, in terms of the Draft Guidelines, the Commission considers section 12A(3)(e) to confer "*a positive obligation on merging parties to promote or increase a greater spread of ownership*" by historically disadvantaged persons and/or workers.

Legal predictability and certainty play a significant role when parties decide to conclude mergers and acquisitions (which have an effect on the national economy).

The Commission must be applauded for giving stakeholders an opportunity to comment and engage the Commission on the proposed Draft Guidelines.

That being said, the impact of the Draft Guidelines (in its current form) on reportable private equity transactions will be felt.

If a merger transaction is reportable to the South African competition authorities, considering a buyer's financial capability and *bona fides* to conclude a transaction will not be sufficient, such a buyer's existing empowerment credentials is also an important factor from a public interest assessment perspective in terms of section 12A(3)(e) of the Competition Act.

Exiting transacting parties have to at all times bear in mind what effect a sale transaction will have on the shareholding by historically disadvantaged persons and/or workers in the target firm.

Transacting parties will have to take a pro-active approach in rigorously considering what commitments may be required and if such commitments are achievable if the anticipated merger and acquisition transaction qualifies to be reported as a notifiable merger to the Commission.

At this point, there may be more questions than answers on the true effect the Draft Guidelines (once finalised) will have on qualifying mergers and acquisitions, however with the opportunity to engage the Commission, all parties involved should endeavour for an outcome that satisfies both the transformational objectives of the Competition Act and the commercial requirements of the transacting parties.

Footnotes

[1] Media Statement: Competition conference highlights impact of merger control on SA economy (Date: 29 September 2023).

[2] *Ibid.*

[3] 89 of 1998.

[4] Competition Commission Draft Amended Public Interest Guidelines Relating To Merger Control (6 October 2023).



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