

## **Multiples of capital invested to remain intact even as COVID-19 may drag on IRR: Affirma's Jaisingh**



Affirma Capital founding partner and CEO Nainesh Jaisingh

*By Deviana Chuo June 18, 2020*

When the coronavirus outbreak first began, Nainesh Jaisingh and his team at private equity firm Affirma Capital began reviewing operations at portfolio companies, ensuring there was a six-month cash flow runway.

The seasoned executives had seen their share of crises, including the SARS pandemic in 2003. But as the global health crisis deepened and spread, Affirma Capital CEO Nainesh Jaisingh began to review even those plans.

"It turns out that we had underestimated the impact and none of the old playbooks were really applicable," he told DealStreetAsia in an interview.

Affirma was established in July last year following a management buyout of Standard Chartered Bank's private equity business and backed by Intermediate Capital Group's Strategic Equity funds. The fund, armed with \$700 million of dry powder after the spin-out,

has deployed about \$200 million since then, with investments in India, Southeast Asia and South Korea.

In February, Affirma launched its fifth fund for the South Korean market targeting mid-sized firms in the country. The target is to raise a total of \$450-500 million and to meet its first close by the end of 2020 or early 2021.

“Korea continues to be a very big market for this business and that’s why we’re getting a very good response for our fundraising as well,” he said. Korea Development Bank and National Pension Services were LPs in the previous four funds.

Affirma is also planning an emerging Asia fund for investments in India, China and Southeast Asia as well as an Africa-Middle East fund. Although the target for these funds is still under review, Affirma will likely launch the fundraising exercise in 2021.

In a wide-ranging interview, Jaisingh talks about the impact of COVID-19 on the firm and its portfolio companies and the broader private equity landscape, exit environment, and outlook on the secondary PE market, among others.

*Edited excerpts:-*

**What was the first thing you did when it became clear that a pandemic was happening? What effect do you think that move had?**

When it became clear that this problem was not restricted to China at around the end of January 2020, we dusted off the playbooks that had helped us navigate these earlier crises – particularly the one that we used for SARS. That meant immediately establishing that each of our investee companies globally had a six-month runway on operating cash burn. It would require cost reductions, headcount rationalisation (even if only with temporary measures), capex freezes, and renegotiations with all stakeholders to conserve cash.

People thought we were over-reacting. But as COVID-19 played out, it turns out that we had underestimated the impact and none of the old playbooks were really applicable. This crisis has a different intensity and will drag out for much longer. We are, therefore, now looking at rolling six-month plans.

There was no crisis in the last two decades that has shaken the foundations of so many business models, and of so many macro-economic assumptions. So, while the early part of the reaction was to think about the survival of businesses, we are now spending a lot of time on revival and what the winning business models will look like going forward.

The revival paths and timelines are going to be very different for each country – depending on its economic strength, its political and social structure, and appetite for painful decisions. South Korea and China have effectively resumed business operations. Even within Southeast Asia, we already see different paths emerging out of lockdown for Singapore versus Indonesia or Vietnam. We will need to calibrate the plans for each of our portfolio companies in that context.

### **What impact has the crisis had on your portfolio companies and how are you mitigating it?**

It helps that we have a very diversified portfolio across industries and geographic regions. In the context of the COVID-19 effect, businesses fall into four categories: directly affected such as restaurant chains, indirectly affected through supply chain disruptions, not affected and those that are doing well in some form.

For instance, Affirma's investment in South Korea's waste management business Environment Management Corporation is not affected by COVID-19 due to the nature of their work. Meanwhile, our digital businesses like Momo in Vietnam, or grocery chain Phoon Huat in Singapore is seeing a big surge in retail revenues over the last few months. Our hygiene products company in the Middle East called Fine Hygienic is also making a big positive social impact by producing masks during the crisis.

However, irrespective of category, our directive to management teams was that every business is now a startup – and needs to re-examine all its fundamentals – demand patterns, changing preferences of its clients, unit economics, supply chains, commercial arrangements, financing, as well as talent and skill requirements. Also, we are fully behind each of these companies, financially and with our experienced teams, to transform the businesses for the new reality.

The fact that our investee companies are typically very modestly leveraged makes a big difference in their ability to ride out the crisis. These are also usually leading businesses in their industries, and we are backing them to be the consolidators as acquisition opportunities emerge on the other side of this crisis.

### **Will you and your LPs review the mandate for the existing funds, following the COVID-19 outbreak? Or will you shift your preferable sectors due to this pandemic?**

Our mandate will continue to remain the same, to back mid-sized founder-led or family-owned companies to emerge as national or regional champions. Our sector focus will remain on consumer and derivative spaces (education, healthcare, financial services) and on tech-enabled businesses that play to these themes.

Our deal pipeline is now looking very interesting and we expect to deploy significant amounts of capital over the next 12-18 months. Also, we will take a call on investment periods sometime in mid-2021.

### **What impact does the current crisis have on your funds in terms of returns and exits?**

Some of the exits that we were planning for this year are now going to be put off for a while. Equally, we are receiving early interest for our holdings in companies which have unaffected businesses, or those that are doing well.

Overall, we do expect some drag on IRRs due to the delays, but our expectations on multiples of invested capital (MOIC) remain intact. However, we cannot put numbers on today. I don't

think that it is realistic to expect that the investment horizon is going to be exactly intact, even if we balance out the good and the bad. But I think if you put the whole situation in perspective, we believe we will end up getting the MOICs that we have forecast, with a delay of maybe six or 12 months.

**In terms of the delayed exits, what were your LPs' reactions and expectations?**

Obviously, they would like to preserve the investment thesis or value in this situation. And that is what most GPs should or would be focused on. As you emerge from the crisis, you start looking at how we restart the process of monetization where it's delayed. That would be the foremost consideration, making sure that portfolios are well managed through this crisis. We are making sure our companies come out intact, or with business models that are suited for the new reality. I think that will be the big differentiator amongst the GPs.

On the other side of this COVID crisis, one of the big questions that LPs will ask is, 'How did you guys do during the crisis? And how did you manage to preserve and enhance value through this sort of crisis?' And that can be a big determinant of who actually emerges as the winner on the other side.

**How do you see the COVID-19 pandemic impacting the secondary PE market in Asia and GP consolidation?**

The secondary market is certainly poised to become significantly bigger. A number of funds raised after the global financial crisis have passed their 10th anniversary, and have not exited their positions. They will be candidates for secondary deals. COVID-19 will restrict such funds from getting market exits for their investments in the immediate future. Asian funds have also acquired size over the last decade, making them attractive opportunities for global secondary players.

Meanwhile, GP consolidation is a theme we are seeing across emerging markets. Funds that are not able to produce top-quartile returns have not been able to raise second or third funds, and are better off folding into larger platforms. That works better for their LPs as well.

The real test of private equity businesses is to make strong returns through the inevitable cycles, so we expect a shakeout over the next 12-18 months. The ability to pivot investment styles and thinking to the new realities will also play a key part in determining the winners.

**How do you see changes in asset valuation due to this pandemic?**

High entry multiples will be difficult to justify for the next couple of years unless businesses are reconfigured quickly, and are also able to increase market share through the elimination of competition or through acquisitions.

Having said that, digital businesses or other beneficiaries of the crisis will see upgrades in valuations.

**When do you expect the dust to settle?**

If an effective vaccine is found that can be made and distributed quickly, the economic world would probably recover to pre-2020 levels quite quickly after that. Without a vaccine, and with the probability of resurgent waves of the virus, the impact will probably reverberate for some time in many industries such as aviation, tourism and hospitality.

We will adapt to new ways of living and working, and that will mean that at some time the dust will settle, but potentially in a different time frame, beyond 2021.

**What are some of the biggest lessons to be learnt from this period?**

First, the premium on good leadership just went up. At portfolio companies or within a PE fund, the ability to ride out this sort of crisis is directly dependent on the ability of leadership to make the right decisions in the face of limited information and high uncertainty.

Second, Southeast Asia PE will be an outsized beneficiary coming out of the crisis. The geopolitical winds are already in favour of business moving from China to Southeast Asia. Besides, SEA PE has really taken wing due to the rise of companies driven by digital business models and this crisis has accelerated the digital and tech transformation of most businesses. So, exciting times ahead.

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