GREYCHAPEL
LEGAL

March 2025

LEGAL AND REGULATORY CONSIDERATIONS IN THE EXIT STRATEGIES FOR PRIVATE EQUITY INVESTMENTS IN NIGERIA

Abstract

A fundamental characteristic of private equity investment is that it has a limited timeline within which the investment is expected to reach its maturity and return profits to its investors/limited partners. As a result, private equity fund ('PE fund') managers often structure their investments in a portfolio company with an exit in mind. The identification of potential exit opportunities may influence a PE fund's decision to invest in a company.

The exit stage is therefore a very important stage in the lifecycle of a private equity investment, allowing the PE fund to realise returns on its investment.

This article will discuss common exit strategies for PE funds, while also highlighting the legal and regulatory considerations that these funds typically consider when making a decision on which exit strategy to pursue.

Introduction

Every private equity investment has a lifecycle that begins with an investment in a portfolio company, making operational changes that drive up the value of the portfolio company so that the PE fund can make returns on its investments and then divest from the company.

PE fund managers will usually conduct a thorough due diligence on the portfolio company, examining its business environment, industry, and the potential for realizing returns on investment into the company. Most importantly, they assess how to exit or liquidate their investment to create value for their limited partners.

The exit phase is the most important stage in this life cycle as it is the stage, where unrealized gains are turned into tangible returns for the PE fund.

PE funds typically have limited lifespans, typically between 7 to 10 years, and exits are essential to redirecting the capital invested in the portfolio company to other investment opportunities.

In Nigeria, exits by PE funds (whether the timing of it, the structure, or the strategy to be adopted) can be influenced by various legal and regulatory considerations such as compliance with corporate and securities laws, compliance with rules regarding importation and repatriation of foreign exchange where the investment is structured in foreign currency amongst other applicable regulatory frameworks.

The Importance of Exits in the Private Equity Investment Lifecycle

An exit in the context of private equity investment is the process by which a PE fund divests from a portfolio company with the sole aim of realising a significant return on its investments. Exits are very important for PE funds because they mark the climax of the relationship and fulfilment of the fund's objective to deliver returns to its investors.

Aside from providing significant financial returns to the PE fund and its investors, exits also validate the investment strategy and expertise of the fund manager. A successful exit demonstrates that the fund manager was able to identify a promising investment opportunity, create value during the holding period, and ultimately realize that value through a well-timed and strategic exit or divestiture.

Likewise, exits are also great for the portfolio company because it facilitates growth milestones for the portfolio company by providing access to new investors, strategic buyers, or public markets.

Preparing for an Exit

As noted earlier, the purpose of private equity investment in a portfolio company is to achieve growth on the capital at the end of the investment period. All private equity investments are typically structured with an exit or divestment in mind. Therefore, preparing for an exit begins at the time the PE Fund contemplates an investment into the portfolio company and continues on to the investment holding period where PE Fund focuses on building value in the portfolio company.

Common Strategies for Private Equity Exits in Nigeria and Key Legal and Regulatory Considerations

There are several exit strategies available to PE funds, each with its own advantages, challenges, and regulatory implications. In the Nigerian context, the following are the most common exit strategies:

- **Initial Public Offering (IPO)**

  An IPO occurs when the portfolio company offers its shares to the public and may also list them on a stock exchange (e.g., the Nigerian Exchange Group). This provides the PE fund with an opportunity to sell its stake, either partially or fully. IPOs are seen as a more lucrative exit strategy for PE funds because the portfolio company can get a higher valuation during the IPO. On the converse, IPOs make the portfolio company subject to a lot of scrutiny in terms of the financials, there is also the requirement to comply with the strict listing requirements of the NGX as well as of regulatory approvals of relevant bodies like the Corporate Affairs Commission ('CAC'), Securities and Exchange Commission ('SEC') etc.

  In Nigeria, a private equity-backed company contemplating an IPO would have to consider the following:

  - compliance with the provisions of the Companies and Allied Matters Act, 2020 ('CAMA') and of the CAC regarding conversion from a private company to a public company;
  - compliance with the SEC Rules governing public offerings of securities;
  - compliance with the NGX's requirements for listing on the NGX and obtaining the approval of the NGX to list on the exchange;
  - compliance with certain disclosure requirements required for public listed companies such as publication of annual reports, audited financial statements etc.; and
  - adherence to corporate governance standards required for public companies.

Sale to a Third Party

A sale to a third party also known as a trade sale entails the acquisition of the portfolio company by a strategic buyer, such as a competitor or industry player. This exit strategy allows the PE fund to capitalize on the value or competitive advantage that the buyer sees in the portfolio company, often resulting in favourable valuations and a likely change of the management of the company.

In contemplating a sale, the PE fund must take note of key legal points such as the Nigerian competition laws and compliance with merger control regulations of the Federal Competition and Consumer Protection Commission ('FCCPC'). If the proposed sale triggers a change of control issue, or the financial threshold set by the FCCPC, the parties would need to notify the FCCPC of the sale and seek its approval to proceed with the transaction.

There is also a requirement for compliance with the CAMA in terms of the transfer of the shares in the portfolio company to the new owners.

Secondary sale

A secondary sale is another exit option for PE funds, and it is similar to an acquisition. However, the distinction of a secondary sale involves the sale of the PE fund's stake in the portfolio company to another private equity fund or institutional investor.

A secondary sale allows the selling PE fund to realize returns on its investments while allowing the acquiring PE Fund or institutional investor to gain access to the portfolio company and drive further growth of the company.

Just as with a trade sale, the PE fund must be aware of merger control regulations as issued by the FCCPC if the proposed sale to another PE fund raises issues related to a change of control or meets the financial thresholds established by the FCCPC.

Further, both PE funds would be required to notify and seek the approval of the SEC in respect of the transaction considering the fact that private equity funds are usually registered with and regulated by the SEC. They will also have to comply with the CAMA and file requisite notice at the CAC.

Management Buy-out

A management buyout has the effect of preserving the ownership structure of a portfolio company. It involves the portfolio company's management team acquiring the PE fund's stake in the portfolio company. It often involves a combination of personal investment from the management team and debt financing sourced from banks or other financial institutions. This strategy creates a continuity in leadership and allows the management team to take full control of the company. The existing management team, being familiar with the company's operations, business and market dynamics, can be well-positioned to guide the company to its next phase of growth.

Furthermore, the management team is incentivized to further enhance the company's performance and increase its value, ultimately benefiting both the management team and the private equity fund during the exit process.

Conclusion

The exit phase is a critical stage of the private equity investment lifecycle, representing the culmination of the value-creation process and the realization of returns. In Nigeria, private equity investors must carefully evaluate the legal and regulatory considerations associated with each exit strategy to achieve successful outcomes.

Whether through an IPO, a trade sale, secondary sales, or management buyout, PE funds in Nigeria must navigate Nigeria's complex business and regulatory environment to maximize returns and while ensuring that they are complaint with the applicable laws.

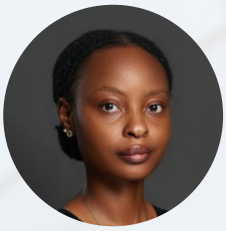
References

Private Equity: Law and Practice by Darryl J Cooke, pages 17-19

Understanding Private Equity Exits: A Comprehensive Guide, an article by Investology Hub accessed at Understanding Private Equity Exits: A Comprehensive Guide - Investology Hub on March 4, 2025.

For any comments and additional information on the issues discussed, please contact the under-listed persons:

Adebola Babatunde
Managing Associate



Oyeronke Oyeyemi
Associate

CONTACT US:
Plot 17B, Emmanuel Abimbola Cole Street, Lekki Phase 1, Lagos   +234 (0) 815 291 4717   info@greychapellegal.com