

PACIFIC RISE CAPITAL STRUCTURE ANALYSIS PROJECT

BRIGHTLIGHT



PURPOSE AND OUTLINE OF THE CAPITAL STRUCTURE ANALYSIS



IMPORTANCE OF PACIFIC CAPITAL FLOW ANALYSIS

- Create an understanding of not only what capital is available, but who is providing it, what are their intentions, and how is it moving.
- Through this understanding, a solutions-based approach can be undertaken to more productively move this capital (e.g. blended finance solutions).
- Providing of analysis to key stakeholders in the area allows for a common set of information for stakeholders to convene on to create solutions.
- An understanding of why capital isn't being used productively creates insights into what restrictions are 'locking' it, and thus preventing it from reaching its intended destination.
- An analysis of the investment mandates behind investors currently providing (or with potential to provide) capital allows for the appropriate tools and products to be created to attract further investment and provision of capital.

INVESTMENT ANALYSIS GUIDING PRINCIPLES

- Attention to how power might be disrupted in existing capital flows in the Pacific.
- Market engagement with the various sources of capital to question and analyse capital flows.
- Ensure analysis is across a wide range of sources of capital, asset classes and financial instruments.
- Focus less on the transactional nature of monetary flows and more on the relationships, trust and knowledge shared between market participants.
- Privilege and bias are baked into existing institutions, laws and structures which allow for the advantage or disadvantage of some over others in the Pacific context. Therefore, the proposed analysis will seek to question the assumptions behind capital flows in order to understand how structures might change.
- Gender Lens analysis requires us to move beyond just thinking about women, to applying a gender analysis to systems, process, and structures of power.

RESEARCH METHODOLOGY

- Research was conducted into the types of capital in the Pacific through an initial in-depth review of literature compiled both by Brightlight and by Pacific RISE.
- A desktop review of industry databases, government websites, and other resource collections was also conducted.
- Upon this research, a narrowing of the types of capital was executed so as to focus the research and create further depth in analysis.
- A Roundtable discussion was conducted in order to gather a group of stakeholders in the area to share thoughts on what a capital structure analysis of the Pacific should look to include. Members of the Roundtable and key learnings are included in the Appendix.
- The capital structure analysis was then continued with consideration given to the most notable interests and concerns arising from the Roundtable regarding such analysis.
- All research and observations were conducted both with a view to the investment themes of Pacific RISE and with a lens of analysing instances of power, privilege and bias in the way capital moves in the Pacific.
- A final capital structure analysis was then delivered to Pacific RISE, including next steps for how such analysis should be executed in further phases.

PROPOSED CAPITAL STRUCTURE ANALYSIS FRAMEWORK

- Brightlight believes a two-dimensional approach to capital structure analysis is most beneficial for the purposes of this exercise.
- The first dimension is the sources of capital, a key component to any capital structure analysis. A look at the different sources of capital available in the Pacific, along with potential for a further deep-dive 'case study' approach, allows for an initial understanding of 'what' can be used to develop lives in the Pacific.
- The second dimension is the components of this capital, which is what binds this structural analysis together. An understanding of what capital is available isn't enough. Instead, a look at who is providing this capital, who are their involved intermediaries, what instruments do they use, and perhaps most importantly, what do they want to achieve with this capital (and how they intend to do it) is critical for this exercise.



CAPITAL STRUCTURE ANALYSIS

Capital Structure Types*

1. Sovereign Wealth & Retirement Funds – Case Study: Nasfund.
2. Multilateral Development Banks – Case Study: Asian Development Bank.
3. Commercial Banks – Case Study: ANZ Banking Group.
4. Corporate Social Responsibility from Pacific Businesses – Case Study: Ok Tedi Development Foundation.
5. International Remittances into the Pacific – Case Study: Developing Markets.
6. Non-traditional Types – 2-3 Case studies: E.g. Churches, Native land trusts.

Components of Capital

1. Asset Holders – “What are the interests of the Asset Holders?”
2. Benchmarks of the Asset Class – “How could blended finance incentivize different interests?”
3. Intermediaries – “Can process – cost/ revenue incentives be shifted?”
4. Instruments & Vehicles – “Can more appropriate structures be built?”
5. Types of Enterprises – “What can become investible? How?”
6. Economic Activity – “Should assumptions about the future be revalued? If so, How?”

* These 6 capital structure types have been chosen to reflect different types of capital flows and data is presented as an example rather than the entirety of the flow

CASE STUDIES OF TYPES/COMPONENTS OF CAPITAL

	Who are the asset holders and what are their interests?	What is their benchmark?	Who are the involved intermediaries?	What instruments/vehicles are used?	What types of enterprises are being targeted?	What economic activity is being generated?	Total capital committed/available?
Sovereign Wealth and Retirement Funds (Case Study- Nasfund)	Members seeking a return on their savings	Return (unspecified) above CPI	Development companies (property), domestic companies (equity), banks, fund managers	Domestic and international equity and fixed income, domestic property, domestic infrastructure and domestic cash	Mostly infrastructure, hospitality and tourism	Economic development through infrastructure and tourism generation	\$\$\$\$\$
Multilateral Development Banks (Case Study- ADB)	Governments from around the world as shareholders of the ADB seeking global economic development	Return is risk-weighted according to country/investee	Local banks, Governments, Funds	Loans, grants, guarantees, equity	Transport (54%), water and sanitation, ICT, energy	Investments target improved connectivity, better infrastructure and particularly economic shock resilience	\$\$\$\$\$
Commercial Banks (Case Study- ANZ Banking Group)	Those who have invested their savings into ANZ for a financial return	Return is risk-weighted according to country/investee	Usually direct lending. ANZ and other banks may also use consulting services for impact investing such as Good Return	Personal Loans, Insurance, Credit, Business Loans, Asset Financing	Tourism, mining, agriculture	SME development, mining sector development, agriculture	\$\$
CSR from Pacific Businesses (Case Study- Ok Tedi Development Foundation)	Business stakeholders seeking development of the communities of the Western Province of PNG	Soft funding provided with only social return on investment being sought	Various sub-trusts of the Foundation, e.g. Middle Fly Trust and Wai Tri Trust	Grants	Predominantly agribusiness and transportation enterprises	Development of value chain in target enterprises	\$\$
International's Remittances into the Pacific	Vast majority are men who come to Australia on seasonal work and send money to support families	Personal/family impact	A total of 61 listed on Send Money Pacific. Examples include Western Union, ANZ Bank, Westpac	Online and branch transfers, and personal gifts	Predominantly cashflow for family business	Local market engagement and increasing the purchasing power/spending capacity of the recipient	\$\$\$\$

CASE STUDIES OF NON-CONVENTIONAL TYPES/COMPONENTS OF CAPITAL

	Who are the asset holders and what are their interests?	What is their benchmark?	Who are the involved intermediaries ?	What instruments/ vehicles are used?	What types of enterprises are being targeted?	What economic activity is being generated?	Total capital committed /available?
NGOs	NGO themselves targeting development	Only social return is sought	Local partners, particularly community organisations. Major donors are also involved	Grants	Agriculture programs (E.g. Fresh Produce Baseline for CARE)	Varies widely. For instances such as CARE and Oxfam, it is typically smallholder farmer production systems	\$\$\$
Churches (ADRA)	Various donors attempting to create social impact in ADRA's target areas. Donors include grants, donations and investment income	NFP, social return only. Specifically, it is a public benevolent institution (main objective is to relieve poverty, sickness or disability)	Project owners	Project investments, grants	Any transformational development and/or relief projects seeking primarily poverty relief	Broadly any economic activity generated by the increased consumption associated with poverty relief	\$
Native Land Trust (TLTB)	iTaukei landowners seeking productive (both social and financial) use of their land	Whatever the respective rent on land is, as well as a level of social benefit deriving from the land's use	iTaukei landowners	Leases	Agricultural, commercial, educational, forestry, government, residential, industrial and tourism	Any business and economic development in the areas that leases are given to	\$\$-\$\$\$
Diaspora Community in Australia	The wealthy individuals from the Pacific community living in Australia seeking to develop communities in their native countries	Varies depending on the individual but often seeking both social and economic development	Depends on funding type but likely to be crossovers with intermediaries involved in remittances	Dependent on size of funding and the individual but loans and equity can be used	Likely to be small enterprises but also likely to not be sector specific	Very broadly activity and development within the areas being targeted. Very dependent on the individual	\$\$-\$
State-Owned Enterprises (China Exim Bank)	Chinese government facilitating national development strategies and build a policy bank	Varies, depending on type of loan/credit given. Must promote social and economic development	Government, State Council	Export credit, import credit, loans, bonds	Particularly those targeting foreign trade, transport, financial services and environment	A more open economy through transport initiatives, trade policies. Take a policy-based approach to lending	\$

KEY INSIGHTS FROM THE CAPITAL STRUCTURE ANALYSIS

1. Preliminary conclusion is that there is sufficient capital in the Pacific. However, this capital is largely misaligned against the investment thesis. Redirecting that capital will require innovative structured investment solutions.
2. Attracting foreign co-investment into developing local projects or enterprises that creates employment outcomes.
3. Driving unofficial/shadow capital (remittances etc.) into formal financial markets so that savings can be leveraged into financing local SMEs to service the local markets (e.g. agriculture and tourism).
4. The majority of money flows through traditional intermediary sources. These flows are mostly many-to-many transactions with low cost or no return.
5. Most intermediaries moving high volumes of capital do not have an impact focus, despite the interests or intent of asset holders.
6. Multiple small impact investments are difficult for large investors.



POTENTIAL PATHS TO CAPITAL RESTRUCTURING

SHIFT FROM SHORT-TERM TO LONG-TERM INVESTMENT BEHAVIOR DRIVEN BY SOVEREIGN WEALTH AND PENSION FUND INVESTMENT HORIZONS

- Institutional investors typically have higher liquidity requirements and lower-risk tolerance than, for example, venture philanthropy.
- Important to mandate sovereign wealth funds to invest for the advancement of the national interest.
- Pension Funds should also be encouraged to seek a mandate from their membership base to invest in inclusive economic growth (e.g. Christian Super sought such mandate).
- Closed-ended funds with locked-in capital would be the most likely investment form, however, it would be important to create the right risk-return profile for this.
- As mentioned, part of de-risking could be an interacting between potential investors and those in the diaspora community, who have a better understanding of the risk profile of the Pacific region.
- Example- In Australia under the Social Enterprise Development Investment Fund (SEDIF), the government seeded Foresters Community Finance Fund with first loss capital in return for investors committing to locking in their capital for at least 5 years, eliminating the need for liquidity in the intervening years and encouraging longer-term thinking.

THE INTRODUCTION OF NEW INSTRUMENTS & VEHICLES THAT ENABLE FORMS OF BLENDED FINANCE TO MOVE CAPITAL INTO TARGETED ENTERPRISES

- Given the diverse types of capital with similar purposes, blended finance can be used to:
 - Create structured products that combine the risk underwriting and development appetite of Government institutions and Foundations
 - Help enhance the risk-return profile of Pacific opportunities
 - Crowd-in commercial and institutional investors
- Example- Climate Investor One (CIO)
- CIO is a blended finance facility mandated with delivering renewable energy infrastructure projects in emerging markets.
- CIO has three distinct but interlinked funds; The Development Fund, The Construction Equity Fund, and The Refinancing Fund.
- It provides access to finance for Developers seeking an end-to-end finance solution, with offerings of up to 50% of development costs, up to 50% of post-construction, operational debt, and all equity financing of up to 75% of construction costs.
- Currently investing in Africa and Asia.
- Example- ANZ Pacific is currently working with a syndicate of wealthy Australian and U.S. venture philanthropists to introduce a blended finance concept to the Pacific in 2019.

TRANSITION OF CSR FUNDING FROM GRANT DISBURSEMENTS TO TARGETED SOCIAL INVESTMENTS

- CSR is currently funding activity in isolation from various capital sources. Therefore, how those funds are considered in the broader capital ecosystem is important.
- Important to leverage the significant capital bases of these companies in a way that targets specific outcomes, rather than simple capital provision.
- Example- Nestlé Farmer Connect program focuses on training farmers in good agricultural practices, helping them grow safe, high-quality raw materials, and develop resilient, sustainable farms.
- Nestlé works directly with 716,000 farmers around the world. In 2018, 440,000 farmers were trained.
- Example- Unilever has an 'Opportunities for Women' program, part of which seeks to enable women to access initiatives aiming to develop skills. By 2018, 1.72m women were enabled.
- Training includes agricultural training for smallholder farming families which is supplemented by education on nutrition for dietary diversity.
- Example- Olam Livelihood Charter identifies holistic factors that impact productivity both within and beyond the farmgate. The Charter targets 8 principles and, now in its 7th year, is embracing around 363,000 smallholders. Olam currently has operations in PNG.

DEMOCRATIZATION OF INSTITUTIONAL CAPITAL IN THE PACIFIC

- There is a need to translate the desires and aspirations of the members of pension funds or the members of the public for Sovereign Wealth Funds into the investment strategy. Providing the means for ultimate owners of the capital to provide input into how their individual or national savings should be invested will disrupt the power dynamics and empower individuals.
- The current development in technology (Smart Phones, Blockchain, etc.) is making it much cheaper and easier to collect the views of a large pool of people and analyse them for the purpose of designing investment strategy.
- Example- Christian Super conducted a survey for members whereby it sought to gain a mandate to shift its portfolio towards an ethical/impact direction.
- This mandate was a combination of Christian Super leading its members, as well as being led by members.
- Started with negative screening and iterations over a decade led to impact investing. This process was largely driven by values-alignment between members and organisation.
- Christian Super engaged with a regulator to ensure that strategy and disclosures were aligned.
- Significant number of Christian Super members list 'values-aligned investing' as key reason for membership.

INVESTMENT STRUCTURES THAT CAPTURE REMITTANCE FLOWS FOR TARGETED ENTERPRISES

- Remittances are typically received for consumption and not investment (and therefore traditionally have little impact on growth), however a report by Bjuggren, Dzansi and Shukur outlines that there is a growing trend of remittances being used for investment.
- They find that the use of remittances for investment depends on the institutional quality of the region and the depth of financial intermediation.
- Therefore, sound financial institutions make third party capital more prevalent.
- Banking more of the unbanked would be a good start to creating these investment structures to ensure the efficient and productive use of remittance flows for the development of SMEs.
- Example- A Wendell Samuel case study of Caribbean outlined structures for improving the product use of remittances. These include an exchange control regime, governments offering similar tax breaks enjoyed by foreign investors to migrants investing in local securities, and credible macro-economic policies to ensure low inflation and stable exchange rate.

SUPPORT NON-TRADITIONAL TYPES OF CAPITAL TO INVEST WITH IMPACT

- As discussed, non-traditional sources of capital include Churches, diaspora, native land trusts etc.
- Diaspora may be attracted to these solutions due their higher risk appetite (greater understanding of risk profile of Pacific region).
- Further, due to the diaspora's overriding goal being the development of the 'home' country, they are more likely to be willing to take part in blended finance vehicles.
- Native Land Trust are a significant holder of capital which is purposed for the development of the community as a whole.
- Example- Anitua Group is a local landowner group of companies owned by landowners on Lihir Island, PNG. The activities of the different business units of the Group range from mining services, to retail, to agribusiness, and its subsidiaries employ around 1,500 people. The Anitua Group is chain-owned by six clan groups, the local government, and 2,500 individuals are shareholders.

SUMMARY POINTS

COMPARISON OF ANALYSIS WITH PACIFIC RISE'S INVESTMENT THEMES

- In-line with the presented capital structure analysis and the outlined research methodology, the alignment of the 6 Investment Themes of Pacific RISE with this analysis was also assessed.
- The findings suggest that capital types and components in the Pacific are strongly aligned with the theme of technology and transport connectivity, especially across more institutional types such as Funds and Multilateral Development Banks.
- There was similarly strong alignment between capital flows and the development of domestic labour and purchasing power strength, with much of committed capital being linked to some level of domestic economic development. This was similarly found for the development of value chains.
- Climate change resilience and expanding value in the informal sector were less prevalent in the analysis. Aforementioned institutional types did display some alignment to climate impact, whilst non-traditional capital types, although not observed in the analysis, are likely to seek to capitalize on this theme. A similar link was noted between non-traditional types and the informal sector, however for more traditional capital, it was more small-scale types such as commercial banks and CSR that displayed alignment.
- Geography mitigating political risk displayed little to no alignment with capital types and structures in the Pacific.

NEXT STEPS

- Further deep-dive analysis following a case-study approach outlined in these slides.
- Case-study approach is implemented through further one-on-one interviews with key personnel.
- Particular focus of the interviews is identifying potential products/instruments/vehicles that could be created to facilitate productive capital flows into the Pacific. We expect a significant degree of cross-pollination between these interviews where solutions might emerge.
- Part of case study will also be an explicit outlining of the investments themes of Pacific Rise and how accurate/attractive these opportunities are to key personnel.
- Further analysis to also be conducted with a more specific gender lens with a view to identifying well-defined solutions to inherent power, privilege and bias in the way capital moves into and within the Pacific.

APPENDIX

ROUNDTABLE DISCUSSION MEMBERS

- The discussion was conducted at Pacific Trade Invest on May 15, 2019.
- Members of the roundtable were:
 - Leata Alaimoana-Roberts, Pacific Islands Trade and Invest
 - Chad Morris, Pacific Islands Trade and Invest
 - Caleb Jarvis, Pacific Islands Trade and Invest
 - Samantha Cook, Pacific Legal Network
 - Jinita Prasad, The Difference Incubator
 - Kylie Charlton, Australian Impact Investments
 - Erik Aelbers, ADB
 - Amanda Jupp, Coffey
 - Joy Anderson, Criterion Institute
 - Tania Black, Criterion Institute
 - Mark Ingram, Brightlight Impact Advisory
 - Simba Marekera, Brightlight Impact Advisory
 - Ben Gavazzi, Brightlight Impact Advisory

KEY LEARNINGS FROM THE ROUNDTABLE

1. Most important factors are who the investors are, what they are looking for (interests, products etc.), and what their investment mandate is.
2. These factors that influence *why* and *how* the capital moves are considered far more important than simply the volume of the capital.
3. Part of the reason for this is volume is not the problem- there is plenty of capital flowing into and within the Pacific.
4. The issue is often how accessible this capital is. Much of it is trapped due to regulations.
5. Land is another key aspect of capital that is plentiful but difficult to convert into productive use.
6. A solutions-based approach to create the right products and vehicles for investors is regarded as the most likely method of addressing capital issues in the Pacific.