

Bridging the Financing Gap Using Pension Funds: GapFund

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Executive Summary

There is a huge gap in funding emerging and frontier sustainability markets. This is partly due to high investment risk (loss) perceived by institutional investors in markets such as sub-Saharan Africa, for example. However, there are investment and funding channels that can eliminate the risk perception held by investment institutions through employing a de-risking mechanism which will eliminate the first loss (10%) from the institutional investor (pension funds – PF) and push that risk to (DFI) funding such as that of SIDA (the Swedish International Development Cooperation development finance institution Agency). This process of bridging the financing gap using pension funds focuses on using the pension funds to invest transparently in sustainability projects (markets). In sum, the project would like to establish a sustainability investment fund using pension funds.

Keywords

Sustainability; pension fund; Institutional investor; de-risking mechanism; development finance institutions (DFI); emerging and frontier markets; investment risk; Commission de Surveillance du Secteur Financier (CSSF); solar energy

The Core Challenge

The core challenge is attaining the 2030 agenda for sustainable development (Sustainable Development Goals – SDGs) and maintaining a sustainable living for more generations to come. Interesting examples are the regions in developing nations, especially in sub-Saharan Africa, which face difficulties in financing sustainable projects (businesses). Specifically, there is insufficient financial muscle to drive the sustainability processes needed to attain the SDGs. Public funds alone are inadequate; as such private capital is necessary in the equation. Although this is the case, there are recurrent obstacles that make the process far from straightforward. The challenges include scale of investment, added value, transparency, investor awareness, and bad perception of risk by private capital in emerging and frontier markets.

GapFund: Model Development

The innovative solution is to develop a de-risking mechanism to scale up impact investment which engages both the private investors in the form of pension funds, and the development finance institution (DFIs) to cover the first loss on investment or guarantee loss sharing. Furthermore, the solution will add value to the investment by including non-financial key performance indicators (KPIs) that are appealing to investors and enhance investment accessibility.

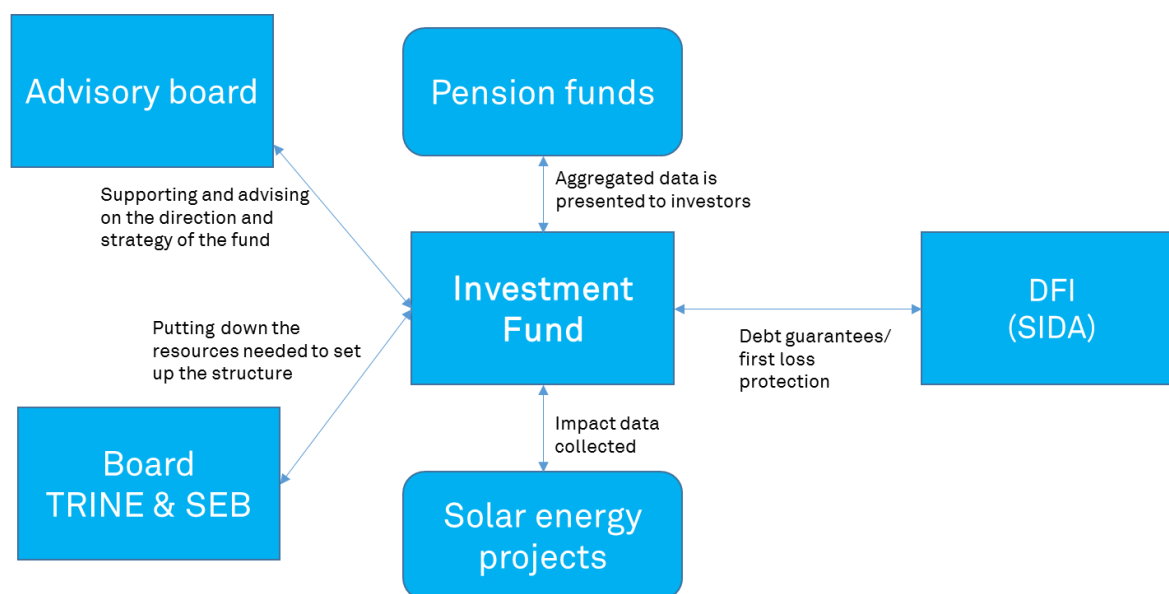


Figure 1: Investment Fund Architecture

Consequently, pension funds will be more inclined to place investments in risky markets.

The Investment fund will comprise different stakeholders. Key stakeholders will be the advisory board and the executive board. The advisory board will be responsible for supporting and advising on the direction and strategy of the fund. The executive board will comprise experts and professional firms from the financial/investment (corporate) sector, and project management (implementers) sector, which will

be responsible for developing the structures and resources needed to set up such a structure.

The DFI will set up an agreement to take a proportionate liability to the first investment outcome (loss) that the fund will invest on the sustainability project. The DFIs will also be provided with the metrics of impact that this investment will have on sustainable development projects.

The Investment fund will in return, aggregate data and present it to the pension fund investors to stir the investment process.

Consequently, the funds will be invested into sustainability businesses in sub-Saharan Africa with a good track record in the solar energy business. There will be a constant, strong and positive feedback loop (information flow) on the outcomes of all investments from the last beneficiary of a solar energy project to the specific pension investor and to the DFIs.

Pilot Project: Solar Energy Investment

The pilot project will focus on off-grid solar energy investment for emerging markets in sub-Saharan Africa with a budget of 50 million Euros.

Step-by-step Approach

1. Draft of the fund structure and corporate backers
2. Present the structure and potential impact to a DFI to obtain de-risking mechanism
3. Present the final product to potential investors (pension funds)
4. File prospectus to the CSSF in Luxembourg
5. Create pipeline for the portfolio funds with off-grid solar companies
6. Start investing; start reporting to investors on impact

Scalability and Replicability

A positive test would:

- Open the way for large-scale investment (to all investment firms) in sustainable business in emerging markets.
- Build confidence in the market that public and private sector can work together.
- Open the way for application to any investment instruments aimed at solving any Sustainable Development Goal challenges.

About the Swedish Institute Sustainability Forum

GapFund was inaugurated as part of the Swedish Institute Sustainability Forum (SISF) 2016.

SISF is an exclusive and highly creative 48-hour global think-tank with a selected sustainability theme. It is held annually in the tranquil outskirts of Stockholm, Sweden. High-level individuals from all over the world gather to share experiences and discuss new solutions for current global sustainability challenges in an informal and productive atmosphere.

Known for its low-key and inclusive approach, the Forum serves a dual purpose: to help companies deal effectively with some of the key sustainability challenges of the 21st century, and to address pressing societal issues. The Forum's objective is to foster engagement and commitment towards collective action and co-creation of open-source innovation.

In 2016, the Swedish Institute organised SISF in content collaboration with International Integrated Reporting Council (IIRC), Centre for Responsible Business, India, with input from Mistra Financial Systems.

For more information about SISF, please visit www.si.se/sisf or contact us at sisf@si.se

Swedish Institute Sustainability Forum



Swedish Institute
Svenska institutet
Slottsbacken 10
SE-103 91 Stockholm
Sweden
T +46 (0)8 453 78 00