

## **Provincial Growth Fund Position Paper**

### **Tier 2: Sector Investments**

#### **Purpose**

The purpose of this document is to outline the Provincial Growth Fund (PGF) approach to Tier 2: Sector Investments; initiatives targeted at priority and/or high value commercial sector opportunities.

#### **Vision**

Sector Investments aim to contribute, along with other PGF investments, to an enduring step-change in regional economies. Sector Investments, in particular, will invest in commercial opportunities that grow the breadth of job opportunities available to New Zealanders, and provide the foundation for regions to generate prosperity on an enduring basis.

#### **Background**

Regional New Zealand has been falling behind on a number of key indicators, such as employment and household income. Despite this, New Zealand's economic base is still largely regionally based and many New Zealanders wish to continue living in the regions, including Māori.

The PGF has been established to ensure New Zealand's regions reach their full potential as part of an economy that is sustainable, inclusive and productive. To do this, three tiers of PGF investment have been established: Tier 1: Regional Projects and Capability; Tier 2: Sector Investment; and Tier 3: Enabling Infrastructure. Between these three tiers, PGF investment will:

1. lift skills in the workforce (tier 1);
2. intensify (physical) capital at the sector and firm level (tier 2);
3. enhance the productivity and long-term sustainability of natural assets (tiers 2 and 3);
4. strengthen infrastructure at the regional level to improve connectivity and resource utilisation, particularly to enable and activate 1, 2 and 3 above (tier 3).

The PGF has identified a number of surge regions where economic outcomes are significantly lower than in other regions: Northland, East Coast, Hawkes Bay, Bay of Plenty, Manawatū-Whanganui, and the West Coast. In line with the wider PGF strategy, Sector Investments will have a particular focus on opportunities to maximise their potential (such as by initiating sector-wide investment in these regions where that is appropriate).

#### **Sector Investment objectives**

Sector Investments will be aligned with broader PGF objectives, in particular, lifting productivity and jobs. Sector Investments should aim to sustainably increase the productivity potential of regions, by enabling an increase in the volume and value of regional economic activity that would otherwise not occur.

To create a sustained lift in productivity potential, the PGF's investments over its lifetime need to leave firms with a stronger basis for generating income on an ongoing basis. This is generally in the form of physical capital, which lifts labour productivity by enabling workers to produce more or higher value output.

New economic activity will broaden the range of employment opportunities in the regions to ensure work is available for people with different levels of skills. It will increase the number and quality of jobs in the regions, providing stronger career development pathways in regions and a stepping stone to a more productive, sustainable and inclusive economy.

### **Sector Investment approach**

*Sector Investments will complement the PGF's wider investment strategy*

The PGF's investments in skills and infrastructure (Tiers 1 and 3) are 'enabling' investments that support economic activity by ensuring firms and sectors have the people, resources and connectivity they need to create and deliver goods and services. Through Sector Investments, the PGF will go beyond enabling to 'partnering', where it invests alongside firms on specific projects that will directly increase the economic activity underway in the regions.

The combination of enabling and partnering investments allows the government to take a systemic approach to challenges in the regions, where social and economic development need to be simultaneously addressed to provide a solid basis for enduring economic activity. By working with firms directly on projects that provide employment, and deliver other benefits, the government can achieve some of its wider social objectives. This is particularly important in the PGF surge regions, where skills, firm-based physical capital and infrastructure have been declining or depreciating for some time.

*The PGF will invest in firms and sectors that generate sustainable jobs for locals*

Sector Investments will invest directly in firms that will grow the number and diversity of jobs available to people in the regions, leveraging opportunities that get locally based, previously excluded, people into sustainable employment. Getting previously excluded people into sustainable employment will contribute significantly to improving the productivity potential of regions, especially where there are high numbers of people not in employment, education or training (NEETs).

*The PGF is focused on laying a foundation for self-sustaining regional economic prosperity*

Sector Investments will also invest in commercial firms and sectors, where doing so will increase the productivity of firms and/or sectors, thus helping ensure regions' ability to continue providing economic opportunities sustainably into the future. Investing in firms and sectors to increase their productivity will also help create opportunities for higher skilled, better paid employment, thus supporting regions' economic resilience and people's ability to achieve their employment aspirations while remaining in the regions.

*To achieve wider public benefits, the PGF will accept a broader risk profile than other lenders*

When investing, the PGF is willing to accept a broader risk profile than market-based lenders. The PGF is willing to accept some additional risks to its investments over and above those accepted by commercial lenders when anticipated wider public benefits of investment outcomes justify them.

The PGF can bring a wider consideration of the benefits a project can provide than market-based lenders are able to do. The Government gets value from the public benefits to a region that a projects can bring, through increased employment and through the increasing the sustainability of income generated by investing in new physical assets. Commercial lenders cannot put a value on these returns as they cannot be captured in commercial returns.

*The PGF will focus investments in mature firms that will deliver*

The following sets out what types of firms or sectors the PGF could invest in:

- **mature or well-established firms or sectors are an area for PGF investment:** these are existing operations with proven success. Investment in firms in this stage is likely to have a lower risk and need a shorter timeframe to realise returns (social and commercial). PGF investment is particularly interested in mature firms operating at scale, or mature firms looking to expand operations into new sectors, upgrading plant and machinery or applying tested technologies in their business that they have not used before;
- **firms in a rapid growth stage may be an area for PGF investment:** these are smaller businesses in a rapid-growth phase, likely under financial and managerial stress. These investments may potentially generate greater returns than investments in more established operations but, they may not do so over the timeframes of the PGF and they may not lead to an increase in the region's productivity or employment. The PGF may still invest in firms in this stage, where they are consistent with the timeframes and productivity and/or employment objectives of the PGF, pending appropriate due diligence;
- **firms seeking start-up or venture capital-type investments are not an area for PGF investment:** given these projects are unlikely to lead to a lift in the productivity of the firm or its employment levels, and that there are other more appropriate sources of government funding for them (e.g. Callaghan Innovation), the PGF will not make these types of investments.

While the PGF will generally invest in mature or well-established firms or sectors, it may invest in the application of new technologies within those firms and sectors. Examples of this are automation and robotics in the horticulture sector, or technology improvements in the energy sector.

*The PGF will make investments at scale that generate high impact*

To generate the sort of impact that will create a step-change in regional economies, the PGF will seek to invest in large-scale high impact projects, or groupings of projects that will cumulatively generate high impact. Within the surge regions, this involves significant investment in skills and infrastructure as well as numerous partnerships with local businesses. In the non-surge regions, the PGF will aim to make two or three such investments in each region. The preferred projects of the PGF enable it to:

- invest in projects that coordinate multiple enterprises;
- invest in common facilities that a range of firms can use;
- invest in industry-wide infrastructure.

*The PGF will invest in a range of opportunities*

The PGF will invest in a range of projects that will deliver a spectrum of opportunities for firms and employees. Sector Investments will aim to create a range of employment opportunities in the regions to ensure work is available for people with different levels of skills. It will increase the

number and quality of jobs in the regions, providing stronger career development pathways in regions. Broadly, the PGF will invest in the following Sector categories:

- **Foundational or sector-wide investments:** investments that have an indirect impact on jobs and productivity, but provide interim jobs and basis for future economic opportunities (e.g. investments in tourism infrastructure, land use studies, sector-wide infrastructure);
- **Plentiful employment investments (typically low-skilled/low wage):** investments that generate a material number of jobs that provide an opportunity for NEETs to attain sustainable employment, or for low-skilled workers to attain more secure employment, and to provide a stepping stone to better paid employment (e.g. investments in tourism, land-based production);
- **Mixed skilled/medium wage employment investments:** investments that generate a more limited number of new jobs, but that put firms on a stronger basis for enduring economic successes by improving their productivity, thus contributing to future viability of regions' economies (especially if they result in the creation of domestic value chains), and providing higher-skilled career pathways for people in the regions (e.g. investments to improve or introduce manufacturing and processing technologies);
- **High skilled/high wage employment investments:** investments that are likely to generate fewer jobs, but jobs that are highly skilled and highly paid, and that will result in significant productivity enhancements for firms and sectors (e.g. investments in Information Communications Technology, or highly transformed niche activities).

### **Priorities for investment**

Priorities for Sector Investments are in the primary, manufacturing and service sectors, especially where there are opportunities to expand into new and emerging products and markets by building on established successes. Consumers are looking for products that demonstrate factors such as product traceability, product sophistication, health benefits, environmental stewardship and animal welfare considerations. Where possible, PGF investment can support industry to position itself to deliver to these preferences and expectations.

#### *Primary sector investments*

New Zealand has a range of existing national and regional comparative advantages, based on our natural environment, people and existing capital investments. New Zealand's strongest comparative advantage is in the primary sector, with economic growth over the past ten years dominated by food and beverage, and forestry (along with tourism).

A key objective for Sector Investments, therefore, is to build on our comparative advantage and established know-how in the primary sector. In line with the Sector Investment Approach, a priority for Sector Investments is opportunities to increase the value of what can be produced in the primary sector, such as through onsite infrastructure investments (e.g. glasshouses) and natural resource enhancements (e.g. small-scale water storage).

As well increasing the value of what is produced in the primary sector, Sector Investments will also seek to increase the volume of primary sector production by extending primary sector activity and job opportunities to areas that have the potential to take up these activities.

### *Manufacturing sector investments*

Sector Investments also provide an opportunity to contribute to the growth of job opportunities in the manufacturing sector, especially where there are opportunities to add value to primary sector inputs. A priority of Sector Investments will therefore be into plant and machinery where firms are looking to expand activities, shift into related products, enhance their processing capacity or processing technology to get greater value from inputs.

By investing in manufacturing projects that add value to domestic inputs, Sector Investments can foster domestic value chains that can stimulate further productivity enhancements. For example, there is significant scope for manufacturing investments that recognise the potential for downstream value-added activities that build on the One Billion Trees programme.

### *Service sector investments*

Depending on the employment needs of regions, Sector Investments can also contribute to the growth of job opportunities in the service sector, such as through the development of physical facilities to support service offerings (e.g. in tourism, or business support services).

### *Investments in emerging sectors*

Sector Investments will consider investments in the waste sector. Sector Investments will prioritise investment in two waste-types: by-products and waste to energy. These types of projects have the greatest potential to contribute productivity gains to the economy, and are in line with Sector Investment principles for investment (see below).

The PGF will prioritise investment in clean energy technology. Given the nature of the energy industry, the PGF will ideally build on previous investment to accelerate growth.

## **Principles for investment**

In addition to the above, the following investment principles will be used to guide Sector Investments. Each application will be assessed on its own merits.

- projects will be considered in the context of regions' comparative advantages, challenges and opportunities;
- projects will not be funded where other appropriate sources of government support are available;
- projects will not be invested in where the primary firm involved is an early stage or start-up firm;
- firms will have already sought private sector funding, and provided a clear explanation as to why it was not approved;
- projects will be supported by a clear and compelling proposal, confirming long-term viability (including understanding and management of risks);
- projects will not be funded until appropriate levels of due diligence on funding recipients is carried out;
- the project will include clearly identified public benefits relating to, in particular, Jobs and Sustainable Economic Development, Māori development; Social Inclusion and Participation; Climate Change and Environmental Sustainability; or Resilience (infrastructure and economic);
- projects will begin within the timeframes of the PGF;
- projects should generally have a minimum 50% co-contribution (applications with potential to generate significant public benefit may be exempt from this requirement).