MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

BRIEFING

Elevate NZ Venture Fund

Date:	9 August 2024	**Priority:**	Medium
Security classification:	In Confidence	**Tracking number:**	2425-0670

Action sought		
	Action sought	**Deadline**
Hon Melissa Lee **Minister for Economic Development**	**Note** that the Guardians informed MBIE on 5 August that they have downgraded their annual conviction rating of NZGCP to 'sub-threshold' reflecting the uncertainty regarding capital for Elevate NZ Venture Fund. **Agree** to discuss with officials on Monday 12 August and to forward this advice to the Minister of Finance and Associate Minister of Finance	12 August 2024

Contact for telephone discussion (if required)			
Name	**Position**	**Telephone**	**1st contact**
Iain Southall	Acting Manager, Investment Policy	Privacy of natural persons	✓
Privacy of natural persons	Principal Advisor, Investment Policy		
	Senior Advisor, Investment Policy		

The following departments/agencies have been consulted

Minister's office to complete:

☐ Approved
☐ Declined
☐ Noted
☐ Needs change
☐ Seen
☐ Overtaken by Events
☐ See Minister's Notes
☐ Withdrawn

Comments

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Purpose

To provide an update on the Elevate NZ Venture Fund (Elevate).

Recommended action

The Ministry of Business, Innovation and Employment recommends that you:

a **Note** New Zealand Growth Capital Partners (NZGCP) manages the Elevate fund, on behalf of the Guardians of the NZ Superannuation Fund, which invests in New Zealand's (Series A & B) venture capital markets

Noted

b **Note** that the Guardians have downgraded their annual conviction rating of NZGCP to 'sub-threshold', reflecting uncertainty regarding further capital for the Elevate fund

Noted

c **Note** that without any additional capital, this will affect Elevate's ability to support the development of New Zealand's venture capital markets

Noted

d **Note** that the key decision for Ministers is whether to provide additional capital to Elevate or not

Noted

e **Agree** to discuss this issue further with officials on Monday 12 August and to forward this briefing to the Minister of Finance and the Associate Minister of Finance.

Agree / Disagree

Iain Southall
Acting Manager, Investment Policy
Labour, Science and Enterprise, MBIE

09 / 08 / 2024

Hon Melissa Lee
Minister for Economic Development

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Background

1. In December 2023, we briefed you on the role of early-stage capital markets in supporting the growth of startups, and current government support for these markets (briefing *2324-1405 Introduction to early-stage capital markets* refers). We advised that New Zealand's markets are relatively small and are yet to be self-sustaining, with the Economic Development portfolio providing two main interventions – the Aspire NZ Seed fund (targeting the seed and pre-seed stage) and Elevate NZ Venture Fund (targeting Series A & B venture capital), both of which are managed by New Zealand Growth Capital Partners (NZGCP).

2. Commercial Information

3. This briefing provides an update on the Elevate NZ Venture Fund (Elevate).

The Elevate Fund

4. Elevate is a fund of funds programme, designed to crowd in private sector investment into venture capital funds, which then invest in New Zealand's high-growth tech businesses. Elevate is overseen by the Guardians of the NZ Superannuation Fund (Guardians). The key role of the Guardians is to ensure that Elevate is being invested into New Zealand's venture capital markets using best-practice investment management.

5. Elevate invests into venture capital funds that are primarily looking to make Series A and B stage investments (round sizes of $2-$20 million) directly into high-growth New Zealand entities. This is important to:

    - provide New Zealand startups the better access to capital for their "break out" stage (New Zealand startups were found to take twice as long to raise Series A/B funding than in similar ecosystems)
    - allow promising young companies to scale in New Zealand, maximising the economic impacts i.e. employment, supply chain expertise, spinout companies etc
    - develop a capable domestic venture capital industry that can guide these startups to the next "scale-up" phase where they have sufficient scale and exposure to attract foreign investment and venture capital (Series C and beyond).

6. While a formal review of Elevate will be conducted later in the year, we consider that Elevate has had a significant impact, helping to catalyse over $1 billion into New Zealand's VC markets. Since 2020, Elevate has allocated 81% of investible capital into nine underlying funds (7 fund managers + 2 follow-on investments), leaving approximately $50 million remaining to commit. Each of these funds has also raised significant amounts of private capital. The total amount raised by these funds from sources other than Elevate is expected to exceed $750 million, and has been used to back around 120 Kiwi tech companies, with roughly 38% of these being deep-tech.

Recent Developments

7. One of the conditions NZGCP must meet as part of its obligations in managing Elevate is an annual ‘conviction review’ which assesses the foundation factors which must be present for the Guardians to invest through a third party.

8. The Guardians informed MBIE on 5 August that they have downgraded their conviction rating of NZGCP to ‘sub-threshold’, reflecting the uncertainty regarding further funding for Elevate, and consequent concerns that they hold around NZGCP’s future viability and ability to retain critical staff.

9. The conviction downgrade triggers an internal process under which the Guardians consider whether to retain or terminate NZGCP as manager of Elevate. The Guardians’ investment committee has endorsed a recommendation to retain NZGCP as manager for now, subject to the receipt of a cost reduction plan and a plan for future investments (discussed in paragraph 11), that have been requested by mid-August.

10. The Guardians board will meet on 22 August to consider NZGCP’s new conviction rating and the investment committee’s recommendation to continue to retain NZGCP as manager. At this stage, we anticipate that the Guardians board will accept this recommendation, and that NZGCP will continue to be the manager of Elevate.

11. It is not entirely clear what the immediate implications of these developments are for NZGCP but to avoid further uncertainty for them (and the potential for them to lose key personnel) we would suggest Ministers make decisions about Elevate’s future and communicate these to NZGCP and the Guardians in the coming months.

12. The Guardians have asked NZGCP to develop a plan for the investment of Elevate’s remaining funds that will limit market harm as far as possible, working on the assumption it will not receive further funding in the near term. The Guardians expect that this plan will likely support a limited number of more established fund managers future investments.

13. We would that with no additional capital for Elevate that there is a risk of a hollowing out in capacity in the investment community. Some of the VC funds that have received Elevate investment are at the stage in their investment cycle where they are looking to raise capital for their next round. Without Elevate to act as a ‘cornerstone’ investor, there is a risk that the number of VC funds active in New Zealand will decrease:

    - Emerging/first-time fund managers will be unlikely to raise further funds to continue to be viable because they have not yet demonstrated a track record of delivering returns to investors (because it is too early in the investment cycle to see significant returns). If these funds are unable to raise their next vintage, they would have to exit the market. Three or four of Elevate’s underlying funds fall within this category.

    - International funds that have recently established in New Zealand, may choose to withdraw from New Zealand if it proves too difficult to raise further capital.

    - Some New Zealand funds and fund managers (and some of their portfolio companies) will likely leave the country to pursue more favourable environments (stakeholders have cited Australia as a highly attractive alternative).

14. Therefore, the key decision for Ministers is to decide whether to provide additional capital to Elevate or not.

New Zealand's early-stage capital markets have grown, but are still maturing

15. New Zealand's early-stage capital markets have seen significant growth over the last two decades:

    - VC investment (Series A and beyond) has grown from $120 million per year in 2001 to $388 million per year in 2023.
    - The number of VC funds of scale (i.e. those that have over $50 million under management) has grown from one in 2006, to 12 in 2023.

16. However, these markets are still small by international standards. The 2022 Startup Genome report found that while Auckland exhibited signs of the 'globalisation' phase (with around 1,400 startups), the rest of New Zealand was still in the initial 'activation' phase (refer to Annex two). New Zealand's VC funding per capita is $1,300. While this is on par with Australia, it is behind other small-advanced economies like Israel ($10,300 per capita), Singapore ($10,200 per capita) and Ireland ($2,400 per capita).

17. Countries such as Ireland, Australia, Singapore and Israel and Sweden have invested in their early-stage capital markets, with sustained funding over 10-15 years helping to catalyse VC markets in these economies. In Australia, the Investment Innovation Fund, established in 1997, was a "fund of funds" model that had three vintages over an eleven-year period and supported the development of Australia's private VC markets. Australia now has over 80 venture funds that have invested $AU16 billion since 2020.

Next Steps

18. We would like to discuss this briefing with you on Monday 12 August. Following that discussion, we recommend you discuss this issue with the Minister of Finance and the Associate Minister of Finance (who has been delegated responsibility for NZGCP). We recommend you forward this briefing to them both with additional background information on NZ's early stage capital markets and comparisons with other jurisdictions. You may also like to discuss this issue with the Minister for Science, Innovation and Technology given her interest in supporting start-ups,

19. Following those discussions, if Ministers wish to pursue exploring options for further investment into Elevate, officials can provide advice on options around funding and phasing.

20. Conversely, if Ministers confirm that no additional capital will be provided to Elevate, we recommend you direct officials to develop advice on a strategy to communicate this decision to the relevant stakeholders.