



## EVENT BRIEFING

### Elevate NZ Venture Fund – discussion between Ministers

<b>Date:</b>	18 September 2024	<b>Priority:</b>	Medium
<b>Security classification:</b>	In Confidence	<b>Tracking number:</b>	REQ-0002949

Action sought		
	Action sought	Deadline
Hon Melissa Lee <b>Minister for Economic Development</b>	<b>Note</b> the suggested talking points and reactive questions and answers that can be used to support your meeting with the Minister of Finance and Associate Minister of Finance.  <b>Agree</b> to discuss this issue further with officials on Monday 23 September.	23 September 2024

Contact for telephone discussion (if required)			
Name	Position	Telephone	1st contact
Onnuri Lee	Acting Manager, Investment Policy	Privacy of natural persons	✓
Privacy of natural persons	Policy 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☐ Withdrawn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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### Elevate NZ Venture Fund – discussion between Ministers

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#### Purpose

To provide supporting material for your upcoming meeting with the Minister of Finance and Associate Minister of Finance on 16 October 2024 to discuss whether follow-on investment should be provided to the Elevate NZ Venture Fund (Elevate).

#### Recommended action

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

- a **Note** the suggested talking points and reactive questions and answers that can be used to support your meeting with the Minister of Finance and Associate Minister of Finance.

*Noted*

- b **Agree** to discuss this issue further with officials on Monday 23 September.

*Agree / Disagree*

이문누리

Onnuri Lee  
**Acting Manager, Investment Policy**  
Labour, Science and Enterprise, MBIE

18 / Sep / 2024

Hon Melissa Lee  
**Minister for Economic Development**

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## Background

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1. You are meeting with the Minister of Finance and Associate Minister of Finance on 16 October 2024 to discuss if the Government should provide follow-on investment to Elevate.
2. We have previously briefed you on what Elevate is and the challenges it faces (2425-0670 and 2425-0734 refers). We recommend this advice, alongside 2425-0734 *Further information on Elevate*, is used in tandem to assist the discussion.
3. The following documents are also attached to support your discussion:
  - a. **Annex One:** Suggested talking points.
  - b. **Annex Two:** Reactive questions and answers.

## The key decision is whether to provide follow-on investment to Elevate

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4. In many countries, early-stage capital markets drive technology, innovation, and economic development, but can struggle to develop on their own. This is because of the inherent risks and uncertainties associated with investing in startup businesses, including long investment horizons, exit challenges, and having few investors who have the capacity and capability to invest in them.
5. Governments around the world support early-stage capital markets through a variety of instruments: grants, loans and guarantee schemes, tax incentives, and venture capital and seed funds.
6. Elevate is one mechanism New Zealand has that supports the development of the early-stage capital market and startup businesses.
7. Elevate aims to stimulate a functioning venture capital industry and ensure that high-growth startup businesses have access to capital. This approach also attracts private sector investment and foreign investment into the market so that, over time, the market can be self-sustaining.
8. This supports one of your priorities as the Minister for Economic Development, which is to help grow New Zealand's economy by improving capital availability for businesses through the continued development of the early-stage capital market.

### **New Zealand's early-stage capital market has grown over the past two decades...**

9. New Zealand's early-stage capital market has grown over the last two decades, with Elevate being a key contributor since its inception in 2019. To date, Elevate has committed to nine underlying funds (seven fund managers and two follow-on investments), resulting in at least 120 startups being backed. Approximately 38 per cent of these are deep-tech startups.
10. The funds Elevate has committed to (\$220 million as of March 2024) have been able to raise \$520 million of private investment from domestic and foreign investors.

**...however, Elevate has not yet had the chance to achieve its longer-term aim of supporting the market to become self-sustaining.**

11. Elevate has allocated 81 per cent of its investable capital, but it is still in the early stages of its investment cycle and is only just beginning to demonstrate its impact.
12. This means that Elevate, its underlying funds, and the startup businesses have not yet had the chance to establish a positive track record of return performance. Despite the growth in New Zealand's early-stage ecosystem, it is still small and underdeveloped by international standards (an assessment of this can be found in briefing 2425-0734).
13. MBIE officials do not believe New Zealand's early-stage capital market has yet reached the point of being self-sustainable. This view is supported by the Guardians and New Zealand Growth Capital Partners (NZGCP).
14. To continue the momentum of crowding in private capital, further investment is needed to enable Elevate to reach a point where it starts realising returns, and for the market to mature and become self-sustaining.
15. Industry stakeholders (16 financial sector experts and managed funds, and five founders) we have spoken to believe the sector requires further help until it is self-reliant and have expressed support for follow-on investment.

### **If follow-on investment for Elevate is the preferred approach, we will provide you with options about how it could be delivered**

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16. If Ministers decide that Elevate should be further invested, we can provide you with options and advice on:
  - a. the feasibility of different Elevate funding levels and their impact on the early-stage capital market;
  - b. different phasing and timing options; and
  - c. the different sources of funding.
17. Confidential advice to Government
18. At a high level, the two options for source of funding are:
  - a. **Directing funds intended for NZ Super Fund (current method):** transfer money originally earmarked for the NZ Super Fund to Elevate.

This is fiscally neutral and has no direct impact on Budget as no new money is required. This option requires allocating a portion of budget earmarked for the Guardians to Elevate.
  - b. **Allocating new budget:** transferring new money directly into Elevate from the Crown.

This will have a direct impact on Budget allowances.
19. While a decision does not need to be made on the amount or source of funding at this meeting, this information may help provide insight on what the alternative funding sources are.

## **If no follow-on investment is provided to Elevate, we will work to understand the future of the fund**

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### **Impact on the market**

20. Without adequate growth capital, startup businesses can remain under-capitalised, grow slowly, be forced to sell, or move overseas to be closer to their investors.
21. A decision not to provide follow-on investment will send a negative signal to the market and influence the behaviour of venture capital funds and startup businesses' consideration in raising capital.
22. Without follow-on investment, a deceleration will likely occur in the growth of early-stage capital markets and there will be reduced availability of funding for emerging fund managers and startup businesses.

### **Impact on Elevate**

23. The Guardians and NZGCP will need to focus on making sure correct measures are in place to manage existing investments. This means that Elevate's focus will likely need to change from an investment-focussed fund to an operations-focussed fund.

### **Impact on NZGCP**

24. We will report back to you on the flow-on impact on NZGCP as, without further investment for Elevate, its market development activities and impact might be limited.
25. The Guardians, as overseers of Elevate, assess the foundation factors which must be present for it to invest through a third party on a yearly basis. Recently, it downgraded its conviction rating for NZGCP to 'sub-threshold'.
26. This decision was made to reflect the uncertainty regarding further funding for Elevate, and consequent concerns that it holds around NZGCP's ability to retain critical staff with the right investment management expertise.

## **Next steps**

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27. If Ministers decide to provide follow-on investment, we will provide you with options and advice about how this could be delivered.
28. If Ministers decide not to provide follow-on investment, we will provide you with further advice about managing Elevate, NZGCP, and potential impact and risks to the market. This decision would also need to be communicated to the Guardians, NZGCP, and the market.

## **Annexes**

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**Annex One:** Suggested talking points

**Annex Two:** Reactive questions and answers

## Annex One: suggested talking points

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- Thank you for making the time to meet with me today to discuss the Elevate NZ Venture Fund.
- Recently, MBIE officials have provided us with advice on Elevate, its current state, and its challenges.
- The purpose of today's discussion is for us to reach a view on next steps and whether the Government should provide follow-on investment to Elevate.
- As you are aware, well-functioning venture capital markets are an important part of our innovation ecosystem, providing growth capital for young, technology-based startups, and helping to develop and grow new sectors.
- Elevate aims to stimulate a functioning venture capital industry and ensure that high-growth startup businesses have access to capital.
- This approach also attracts private sector investment, including foreign investment, into the market so that, over time, the market can be self-sustaining.
- New Zealand's venture capital market has expanded substantially in the last few years. Since 2020, Elevate has helped crowd in over \$500 million in private investment from both domestic and foreign investors.
- Five new venture capital funds have also been set up in New Zealand since Elevate was introduced.
- Despite this growth, our venture capital market is still maturing, and is still small and underdeveloped by international standards.
- Furthermore, Elevate has allocated most of its investable capital but it is still in the early stages of its investment cycle and is only just beginning to demonstrate its impact.
- This means that the returns from Elevate's initial investments, the funds it has invested in, and startup businesses have not yet had the chance to establish a positive track record of return performance.
- My officials advise me whilst New Zealand's venture capital market has grown, they do not believe it has yet reached the point of being self-sustainable.
- This view is supported by the Guardians and NZGCP.
- We therefore have two options to consider:
  - a. invest more in Elevate to maintain momentum and allow our venture capital markets to further mature to the point where they become self-sustaining, or
  - b. do not invest more in Elevate and look to manage the impact that could have on the market and flow on effects to the innovation economy.
- Given our tight fiscal environment, I am keen to hear your thoughts on what the Government's next steps in relation to Elevate should be.

## **Annex Two: Reactive questions and answers**

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### **What is Elevate?**

- The Elevate fund was launched in 2020. Its aims are to enhance our economy by:
  - Increasing the venture capital available to innovative, technology-enabled startup businesses, and
  - Developing our venture capital markets to function self-sustainably by crowding in private capital.
- It is a \$300 million 'fund of funds' that aims to invest in venture capital firms, that invest in startup businesses.
- Elevate's investment mandate focuses on venture capital firms that invests in businesses which are in 'series A~B' also inter-changeably described as the venture capital market. This is when businesses require financing to scale and expand their businesses, often internationally.
- The Guardians of New Zealand Superannuation have responsibility for Elevate, who appointed NZGCP to manage it.

### **Why should the government intervene by funding Elevate?**

- Making sure startup companies have access to markets, skills, and capital can give them the opportunity to become high growth, world leading entities that greatly contribute to our economy.
- However, startups are at a stage where they have no, or limited, revenue and will require external financing to develop their business model to scale up through periods of negative earnings.
- Without adequate growth capital, startups can remain undercapitalised, grow slowly, list or sell prematurely, or are picked up by overseas funds or firms.
- Without Government support, it is likely that New Zealand's early-stage ecosystem will fall further behind our peer countries, including Australia, where startups get more Government support.

### **What happens if no further capital is provided?**

- I anticipate that less capital will be available for our most promising startup businesses to quickly grow and internationalise. This will hamper our efforts to rebuild our economic foundations.
- Moreover, I anticipate that our venture capital industry's growth will decelerate, with
  - some established firms likely to wind-up, or look for solutions overseas
  - international funds that have recently established in New Zealand may choose to withdraw.

### **How much more investment is needed?**

- The Startup Advisors report, published in 2023, has estimated that a further \$500 million over 10 years is required to support the market to become self-sustaining. However, I think further advice and analysis is needed before we can be sure of the amount that is necessary or desirable.

**Are there other (non-financial) options to support the development of our venture capital markets?**

- More investment from institutional investors (such as Kiwisaver funds) and foreign investment is desirable. We could explore options to increase investment in our venture capital markets from these sources. For example, more could be done to educate and raise awareness of venture capital investing among institutional investors, as a lack of expertise and experience has been cited as a barrier by some industry stakeholders.
- However, these types of investors will also want to see a stronger track record of returns before increasing their allocation. Therefore, any action to increase investment from other sources would be most effective if done alongside Elevate.

**What about NZGCP's recent cashflow challenges? How does this relate to a decision around Elevate's future?**

- NZGCP's cashflow situation has improved significantly since the Government made a contingency provision in Budget 24 to indemnify NZGCP's operational expenses. This is due to some returns on its investments being realised in recent months.

Commercial Information

**Next steps**

*If there is appetite amongst Ministers to consider providing additional capital:*

- I suggest we direct officials to provide detailed advice on options available for the source of funding, size of investment, phasing, and the delivery options.

*If Ministers do not wish to consider providing additional capital:*

- I suggest that we direct officials to provide advice on the implications for the ongoing management of Elevate, as well as the impact on NZGCP and its operating model. We will also need to communicate this decision to the Guardians, NZGCP and the market.