UK-India Development Cooperation Fund (UKIDCF) Early Market Engagement (18^{th} April 2024)

The UK-India Development Cooperation Fund (UKIDCF) convened an Early Market Engagement (EME) event on 18^{th} April 2024 at Mumbai.

The objective of the EME was to share information about future investment plans and to gather feedback on the proposed design and investment strategy. A brief description of the three programmes is as below:

- **Pioneering Climate Investments in India Programme (“PCII”)** - Up to £150 million of anchor funding towards climate adaptation and emerging mitigation sectors such as sustainable agriculture, cooling solution, water treatment/ desalination and green hydrogen. Focus will be on large scale enterprises with investment ticket sizes in the range of £15-50 million. Ticket size could be smaller for path-breaking adaptation solutions. The programme aims to help people cope with climate change while creating green jobs and reducing greenhouse gas emissions.
- **Investments in Green Enterprises (“InGreen”)** – Up to £125 million of anchor funding towards high potential green enterprises in sectors such as e-mobility, waste to value, sustainable energy, cold chain and sustainable agriculture. Focus will be on enterprises in their growth and expansion stage with investment ticket size in the range of £5-15 million. The programme aims to support green enterprises contributing to India's climate commitments and empowering women entrepreneurs while creating new jobs.
- **Tech Start-up Fund Programme (“Start-up”)** – Up to £110 million of anchor funding towards breakthrough technologies for development in sectors such as climate-tech, agri-tech, health-tech and edu-tech. Focus will be on early stage (Seed, Pre-Series A/Series A) enterprises with investment ticket sizes in the range of £2-10 million. This programme aims to support tech startups working on development issues.

All programmes aim to catalyse new investments into underinvested sectors on a pan-India basis.

UKIDCF set out the key objectives and indicative investment metrics of the three programmes during the EME.

Key market feedback/ suggestions consolidated through the EME:

1. Investment strategy and pipeline

1.1. What traction are you seeing in the market on climate and tech sectors? What are the high potential sub-sectors within these themes?

- There is increasing traction in climate sector for investment. Sectors such as e-mobility are dominant in attracting investments but there are others such as grid efficiency, storage, water, circular economy, waste management, plant-based protein, etc. which are not seeing traction. There is lack of effective measurement of climate related parameters (beyond GHGs), such as impact on waste, soil, pollution. The RFP should factor in flexibility to accommodate these sectors.
- Early-stage climate tech companies have a strong tech orientation and require varying types of capital to scale to growth. The investment strategy should factor this in while deciding on instruments.

1.2. Is there an investible pipeline in adaptation sectors? How can we increase?

- Investing into adaptation is difficult given that localised impacts need to be measured. There is lack of understanding for the sector and its return profiles.
- Blended finance is important in this sector - government capital and concessional capital can enable capital from private sources. Innovative fund structures and flexibility can aid further. Other DFIs, MDBs can be encouraged to participate/invest after UKIDCF commitment.
- To increase pipeline for adaptation at portfolio levels, fund managers could adopt an approach where they invest in both adaptation and mitigation in the same vehicle to balance risks and returns.
- There is evidence for investment in early-stage tech-led innovations in adaptation themes such as startups working on building materials, food security, resilience in food production, improving efficiency, water and innovations for recycling, cooling solutions. The investee funds should consider these sectors as part of investment themes.

1.3. Is it viable to have a large single sector tech fund e.g. AI for climate? Is there a market for a dedicated AI focused fund for development?

- The market is at nascent stage for tech funds hence this approach may not work well. It is advisable to have flexibility for Fund Managers.

1.4. What levers can ensure that Fund Managers stay at the cutting edge of development impact i.e. no 'mission drift'?

- UKIDCF could have clear standards for management of fund. This could include evaluation for investments, governance arrangements like the Development Impact Committees, and standard documentation to convey the requirements clearly.

1.5. Is there a sufficient pipeline of women led enterprises? How can we increase the number of such green enterprises?

- There are not many women led enterprises and by adding a climate filter will make it even more limiting to get women led enterprises.

2. Fund Structure

2.1 On adaptation, is there a need for innovative financial structure e.g. concessionality? How can these be structured?

- Risk appetite across different classes of investors vary. Fund Managers need more flexibility that can appeal to a diverse set of investors given objective is to crowd in investments. Adaptation as a sector specifically might require sub-ordinate capital.
- There is limited evidence of commercial capital in adaptation. Presently, Fund Managers are facing challenges in attracting commercial capital to climate funds. Ability to attract commercial investors during first close of the Fund will be a demonstration of success.
- Structure like First / Second Loss coverage may help in mitigating risks for commercial capital. These can be considered in fund design and will help Fund Managers balance returns for different classes of investors.

2.2 UK government has a policy of capital preservation. Considering that, what structures can be used for PCII?

- Waterfall with provisions for higher hurdle rate for private investors to incentivise their participation can help.
- Ability to accommodate lower hurdle rate specifically for investments in hard to penetrate sectors / regions. Dedicated capital for Tier 2, 3 geographies can help incentivise Fund Managers.
- Incentives to Fund Managers for fulfilling non-financial metrics for example on policy, development returns, etc.
- It was clarified that while there is some flexibility for concessional capital, this will be deployed only across sectors that need the support. This will not be available for funds under InGreen and Start-up.

2.3 What should be the size for InGreen? Considering 3x of anchor (125m), is 500m a viable fund size? Or how many funds should need to be considered?

- A single large fund can make a substantial impact in the target sectors and provide benefits of branding for UKIDCF. Allocating the funding to 3-5 funds (£75-150m each) can help mobilise more capital into a bigger number of companies.

3. Mobilisation

3.1 What is the potential for mobilisation under each of these programmes?

- The mobilization ratios range between 1:3 and 1:4.

3.2 Which category of investors would find it attractive to invest in proposed themes?

- Investors focused on sustainable enterprise solutions are drawn to segments where portfolio companies drive efficiency gains, particularly in reducing energy consumption and carbon emissions, showcasing tangible environmental impact.

4. Inclusion & Diversity

4.1 What can be done more to increase investments in women led businesses?

- Support for smaller women led funds will help create an ecosystem. UKIDCF should encourage fund managers to screen and select women led investees.
- Innovative structuring might work. For example, higher returns in waterfall for women led investees.
- Capacity building of fund managers and strategic workforce training can help. Few sectors have greater potential for inclusion than others.
- UKIDCF should request Fund Managers to have gender action plans to encourage women at senior levels.
- UKIDCF should have diversity of teams as one of the evaluation criteria.
- UKIDCF can explore using technical assistance to support the evaluation on inclusion parameters for investee funds.

5. Systemic impact

5.1. How can we encourage the Fund Manager and investee level to feed into government policy to build the market in target sectors?

- UKIDCF can incentivise Fund Managers by building into fee structure as it needs dedicated efforts. Monitoring through Development Impact committees, Investor Committees, Impact assessment are some ways which may help.
- UKIDCF can consider having GoI experts as members of advisory committees to build B2G connect. Additionally, identifying key themes and publishing whitepapers in conjunction with think tanks, GoI (eg. NITI Aayog) can be useful in building policy inter linkages with investments.
- Individual Fund Managers may not directly have levers to work with Government on policy. Working alongside industry platforms and bringing in Government stakeholders can help.

- UKIDCF can develop indicators to monitor the performance of a fund. This may include indicators spanning systemic impact on wider ecosystem, policy inputs, mobilisation efforts to ensure impetus on systemic impact via policy.
- Some sectors need policy support to scale. UKIDCF can help identifying these pockets where Fund Managers can work alongside central and state governments. This will also help the overall portfolio under UKIDCF.

5.2. What can UKIDCF do here?

UKIDCF could consider first time fund managers who otherwise have experience of running businesses. This will build capacity within the industry.

5.3. What are key policy enablers to catalyse investments under the target sectors?

- Priority sector lending helped banks achieve both commercial and impact goals. Creating something similar for investment funds will help.
- Climate is a global problem and needs global solutions. Bringing innovative solutions from the UK will attract funding. UKIDCF can help unlock access to best-in-class technology. This will also help in generating higher returns.
- Incentivise banks, insurance companies to invest. Earmarking corpus for such investors can also help.

6. Strengthening India UK corridor

6.1. What are the opportunities you see in the UK-India corridor (in terms of investment and tech partnerships)?

- Partnering with UK pension funds can help manage risk and incentivise investors to explore opportunities in India, especially in markets they are familiar with.
- In the past, the strategy of innovating in the UK and executing in India has proven successful, highlighting the need for fund managers to increase their awareness where much match making can help.

6.2. How can we increase mobilisation from the UK?

- Collaborating with UK enterprises to expand operations to other regions, such as Africa, presents an opportunity for global market penetration.

  VCs from Japan bring their company representatives to visit their investee companies in India, facilitating the formation of partnerships and fostering collaboration opportunities. Same model can be replicated by UK VCs.

6.3. What role can Government play in strengthening the linkages between UK and India?

- Extending the tax benefits enjoyed by individual angel investors in the UK to Indian Alternative Investment Funds (AIFs) could significantly enhance capital flow and stimulate investment in India's burgeoning startup ecosystem.
- Roadshows, interactions with UK Government / UKIDCF can help create confidence amongst UK investors. They need soft reassurance while making key investment decisions, particularly in emerging markets like India.
- UK Government could also support by organising seminars in both the UK and India, targeting family offices, to familiarise investors with Indian fund managers, thereby fostering trust and confidence in investing in India.

7. Question and Answer:

7.1. What is the expected time frame for the launch of the funds and the process for selection of Fund Managers?

- An RFP is intended to be released in coming weeks. These timelines are indicative in nature and subject to internal approvals. The details of process shall be included in the RFP. We shall follow an open and transparent process for selection of investee Funds.

7.2. Is there any geographical focus within India and on poverty alleviation?

- UKIDCF will be open to investments across India. However, development scorecard mechanism will have criteria for penetration in tier 2/3, rural and other hard to reach geographies to encourage fund managers to be inclusive. Poverty alleviation is our statutory objective given these are Official Development Assistance (ODA) funds.

7.3. Is there any support from Government of India for investee funds? Is it mandatory for Funds to have matching funds from Government?

- The Fund Managers need not have Government commitments before applying. UKIDCF will not directly facilitate any investment from Government in Funds.

7.4. Any preference on structure and GP commitment? Such commitment may be built into the proposal itself.

- This will be covered in the RFP.

7.5. Is the fund mandate to support women-led or women-benefitting businesses?

- Inclusion is an important criterion for all our investments. We encourage our investee funds to have diversity and inclusion in teams and encourage the same at investee level. This is monitored by way of our reporting requirements and governance mechanisms. In case of Ingreen, there may be funding specifically earmarked for women led businesses.

7.6. Is there any geographical focus under the proposed investment funds?

- We are open to funds which are proposing to invest across India.

7.7. How many Funds will be selected under each Programme?

- We plan to have a small number of large funds for effective implementation strategy. We have noted the feedback received from participants and will finalise the approach internally.

Next Steps:

- An RFP is expected to be published in coming weeks, subject to internal approvals.
- Fund Managers are encouraged to refer to UKIDCF website for updates.