Small Foundation

Liquidity mechanism

Public report

November 2020

Executive summary

- Small Foundation mandated Palladium Impact Capital to explore innovative liquidity mechanisms for investment vehicles. They have identified, and is seeking to further understand, the opportunities for addressing the tension between the needs of investors (capital at scale) and African SMEs, with a focus on investment tenor. The aim was to scope the liquidity mechanisms available, especially for an an open-ended investment vehicle, which they believe would better address the 'missing middle' challenge for Social Agricultural Enterprises (SAE) in Sub-Saharan Africa (SSA).
- Investors inform the attractiveness and thus the viability of various liquidity mechanism options, as such we reached out to a targeted set of asset owners, asset managers and investment advisors, to refine and enrich the evaluation.
- Different liquidity mechanisms are accessible across various levels within the structure, reflecting strategies to generate liquidity through a combination of routes:
  - *Asset level*
  - *Portfolio level*
  - *Vehicle level*
- Each of the mechanisms have clear benefits and drawbacks and, unsurprisingly, there is no single 'silver bullet' in addressing the liquidity challenge…
- … but the mechanisms, when used in conjunction, could provide a fuller solution – depending on the underlying investment portfolio.
- It is important to differentiate and align liquidity to investors needs as such structuring and building in mechanisms for LP exits are different from liquidity from exiting individual investments, as such different approaches and views on the funds' design and partnerships are necessary.
- This leads to a need to evaluate of vehicle structures to manage the innate tension between providing patient capital through an open-ended structure and yet reducing the investor universe and thus scale, and which is indeed a better fit for the purpose.
- There is currently a slew of new focus on liquidity mechanisms given the current climate, yet much of this will be constrained in emerging markets due to market constraints, size and scale but may be a view into future options. Although there are still options which can provide liquidity exits at the investment level and when structured into the fund provide opportunities for fund liquidity in an open-ended context.

Introduction

Small Foundation in partnership with Palladium Impact Capital, is launching a report on the liquidity mechanisms available for private funds.

- In the first instance, the aim is to understand how to attract larger pools of aligned capital into a critical gap in the finance market for Social Agricultural Enterprises and their intermediaries (SAEs) and to enable the flow of capital to allow commercially-viable SAEs to reach their potential for impact at scale. With the ultimate outcome of improving existing or creating additional income opportunities for Smallholder Farmers (ultimate beneficiaries).

- SAEs tend to grow more slowly, leading to long timeframes to test new processes, services or products. Due to exogenous shocks affecting agricultural production, such as adverse weather or pest outbreaks, SAEs are inherently high-risk businesses. Poor infrastructure and immature commodity and input markets in which many SAEs operate also add to the cost of doing business and limit their profitability. All these factors contribute to a profile that is less attractive to investors.

- The principal assumption and motivation for the research is that while donor and philanthropic funding is often available to support the initial phase testing innovative SAE approaches, only a minimal pool of aligned investment capital is available to support SAEs during their scaling-up, i.e. after the initial proof of concept phase. Accordingly, there appears to be a substantive need to bridge SAEs to the next stage in which sustained growth can be achieved autonomously (i.e. without external financing). This financing need is often lumpy and long term, with patient capital being necessary to ensure fulfilment of the financial and impact objectives.

- Thus the focus is on the conceptualisation of a vehicle that will have the flexibility to better meet the needs of SAEs and at the same time demonstrate to other patient capital providers that it can achieve impact at scale, thereby unlocking significant amounts of capital to be channelled into similar vehicles in the future.

- The initial hypothesis is that an open-ended vehicle is necessary to better meet these needs, yet in order to marry this to investor needs, the mandate was conceived, to provide insight into the various liquidity mechanisms available for such a structure.

Structural market characteristics drive the need to explore innovative liquidity mechanisms

	Key consideration	What this means
Sector	▪ SAEs often (a) have a slow growth profile and (b) are exposed to seasonality. ▪ Value chains are often nascent/ under-developed, inhibiting scalability.	**Longer term horizon to reaching scale**
Instrument	▪ Private equity has a higher liquidity risk due to the reliance on finding an exit. ▪ Private debt is typically more liquid given the predetermined returns distribution profile (and often collateralised).	**Instrument flexibility creates liquidity tension**
Exit	▪ Shallow domestic capital markets, increases the risk of not achieving a successful exit event for equity investments. ▪ Many investors are allocating away from primary agriculture opportunities, which further limits exit opportunities.	**Traditional exit mechanisms are challenged in this context**
Geography	▪ SSA is critical from an agri-production perspective – but the countries carry inherent risk for investors: – Macro volatility: FX, interest rate, regulatory and governance challenges – Infrastructural: poor market access, lack of infrastructure and information.	**External risks are an inherent part of the proposition**
Stage	▪ Earlier stage ventures carry risks which may reduce the probability of a liquidity event within an envisaged investment horizon: – Longer times to scale, with risk on how long/ deep the 'J-Curve' will be – Limited support and infrastructure (vs. early stage ventures in developed markets).	**Longer term horizon and additional support are necessary to scale and exit**

Investors’ requirements should inform decisions on structure and align with the liquidity mechanisms that are available

Liquidity spectrum

Daily liquidity	Quarterly / Annual liquidity	10 year liquidation
▪ **Vehicle:** Listed company ▪ **Liquidity:** Liquidity available constantly depending on trading values ▪ **Investor need:** highly liquid assets, with no liquidation necessary ▪ **Liquidation risk:** Low risk due to high frequency trading and ease of exit	▪ **Vehicle:** Open-ended vehicle ▪ **Liquidity:** Liquidity windows available on a pre-set period (annual/quarterly) ▪ **Investor need:** access to early liquidity if necessary, medium liquidity profile with no liquidation ▪ **Liquidation risk:** medium risk due to set windows increasing ease of early exit	▪ **Vehicle:** Closed ended fund ▪ **Liquidity:** liquidation at fund close (year 10) ▪ **Investor need:** Low liquidity profile throughout life, with liquidation necessary at end of term ▪ **Liquidation risk:** High risk due to difficulty in exiting and a single event
*LPs are looking for **growth** and will hold on to the asset for as long as they see the ability to attain returns aligned to their risk appetite.*	*LPs are looking for an ability to exit (partially or fully) their holding through structured **liquidity windows** whenever they deem fit (in alignment with window timing), yet are purchasing the ability to grow and reinvest over time.*	*LPs are looking for a **structured exits** to their investments that were picked and grown, such that when the fund term comes to an end, full liquidation has occurred.*
Exit mechanisms: *Built in:* ▪ N/A as the listing creates a liquidity mechanism *Not built in:* ▪ Put options	**Exit mechanisms:** *Built in:* ▪ Liquidity window ▪ Backstop agreement *Not built in:* ▪ Put options ▪ Secondary asset transactions	**Exit mechanisms:** *Built in:* ▪ N/A as the fund does not need interim liquidity *Not built in:* ▪ Put options ▪ Secondary asset transactions

There is a implicit tension between complexity and investibility

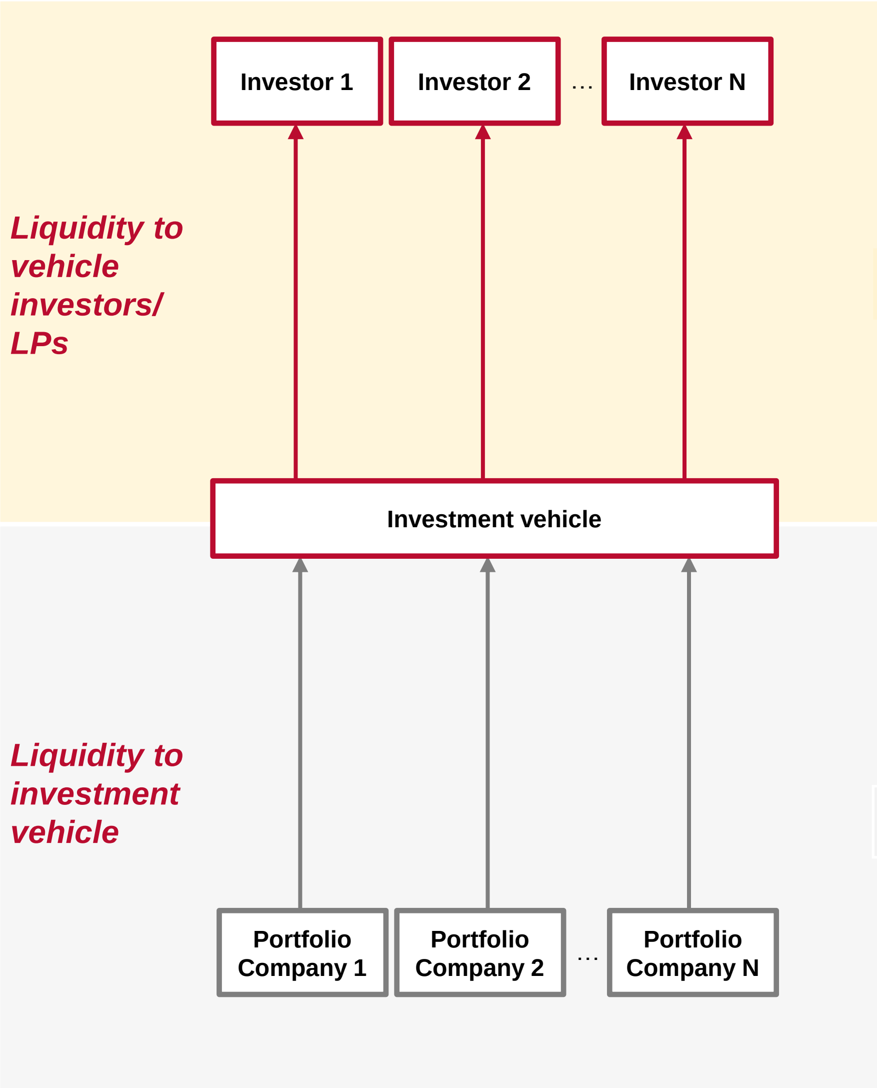
Overview

There are implicit tensions between the need for tailored solutions and the need for standardisation to be aligned with the market. Investors would often like to have less restrictions around capital deployment to further align the investment terms to the market needs, yet often these restrictions are set by others and thus out of the manager's control. The more standardised the investment opportunity, the easier it is to meet these requirements. As such close ended funds are preferred, even when they may not meet the market needs as well.

	Closed-ended fund	Open-ended fund
Advantages	▪ **Duration:** the closed-ended nature mitigates liquidity concerns ▪ **Investor perception:** Offers marketing advantage in that the structure is highly familiar to investors ▪ **Incentives:** More straightforward alignment of incentives with Vehicle team as compared to an open-ended fund ▪ **Valuation:** No on-going valuation needs given the highly defined entry and exit nature of the structure ▪ **Distribution:** No IRR drag from unused cash, as cash is called as needed and distributed immediately after asset divestures.	▪ **Duration:** More liquid than closed-ended structure only if strong liquidity fundamentals exist (i.e. yield and/or secondary market for participations). Moreover, investment duration is adjustable for each particular investor given their flexibility to execute secondary sales. ▪ **Fundraising:** Needs fundraising to scale but is not threatened by fundraising cycles. ▪ **Patient capital:** For invested companies, this provides for the possibility of more patient capital. ▪ **Asset Visibility:** Investors could have visibility on future assets: ▪ **Secondary sales of participations**: secondary investors could be investing in existing assets held by primary investors
Disadvantage	▪ **Duration:** Typical life of closed ended funds (i.e. 10 years) tends to be long for investors, but short for invested companies. ▪ **Fundraising:** Intense fundraising cycles serve to be a drag on operations and hence scalability becomes a challenge for the fund manager. ▪ **Asset Visibility:** Closed-ended funds typically work on a "blind pool" basis and hence there is low visibility for investors on future invested assets.	▪ **Duration:** Highly uncertain exit timeline for investors if assets are illiquid (vs. defined exit in closed ended fund). ▪ **Valuation:** Critical and intensive valuation processes when raising capital or to enable liquidity mechanisms. ▪ **Incentives:** Difficult to balance short term and long term profitability, risk and growth incentives while aligning with compensation for the Vehicle team. As an example, many YieldCos failed as management pursued asset revenue and share price growth at the expense of risk management and quality of assets.

Liquidity routes in open-ended investment vehicles can be considered across two distinct levels

Levels of liquidity creation



Overview of typical liquidity routes

A Redemptions

Detailed overleaf

- Sale of shares/ fund units to the fund, typically during redemption windows.

B Distributions/ dividends

- Ongoing cash distributions made to investors or Limited Partners ("LPs").

C Secondary sales

- Sale of shares in investment vehicle or LP holding to a third-party investor.

A Equity proceeds

- Dividends.
- Proceeds from (full or partial) exit.

B Debt payments

- Interest payments.
- Principal repayment.

C Contractual distributions

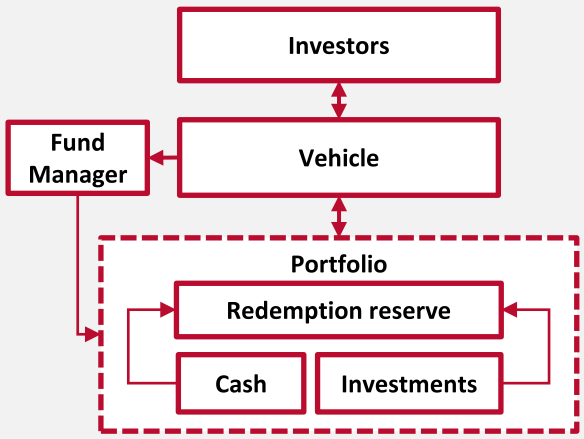
- In quasi-equity/ quasi-debt agreements.

Redemption reserves are a common liquidity route at the Vehicle level

Facility Strategy

- A dedicated redemption reserve account is created to provide liquidity for investors in case of a redemption request. In summary:
  - Pre-agreed part of funds is set in a redemption reserve, that is available for investors/ LPs for redemptions (held in cash or liquid assets).
  - Investors/ LPs are allowed to request a redemption at pre-agreed redemption windows (which can be monthly, quarterly or annual).
  - If several LPs request a redemption, available amounts (i.e. the redemption reserve plus possibly further available cash) are distributed pro rata.
  - Following a redemption, the reserve is refilled.
  - In order to encourage long-term investments, lock-up period are often agreed (during which no redemption is available, and/or redemption discounts or fees applicable over a certain period of time).
  - As an alternative to a funded redemption reserve a funding commitment by a credible third party can also be sought.

Illustration of mechanism



Key challenges

- **Returns**: Cash drag on returns, as part of the committed capital is held as cash or invested in (lower yielding) liquid assets.
- **Cost:** For each redemption window, NAV needs to be established through a time-consuming/ expensive valuation process.
- **Effort**: Liquid investments need to be managed, further also larger redemption requests are managed in dialogue with LPs.
- **Size**: In case of significant redemption requests, funds to meet all requests can be insufficient.

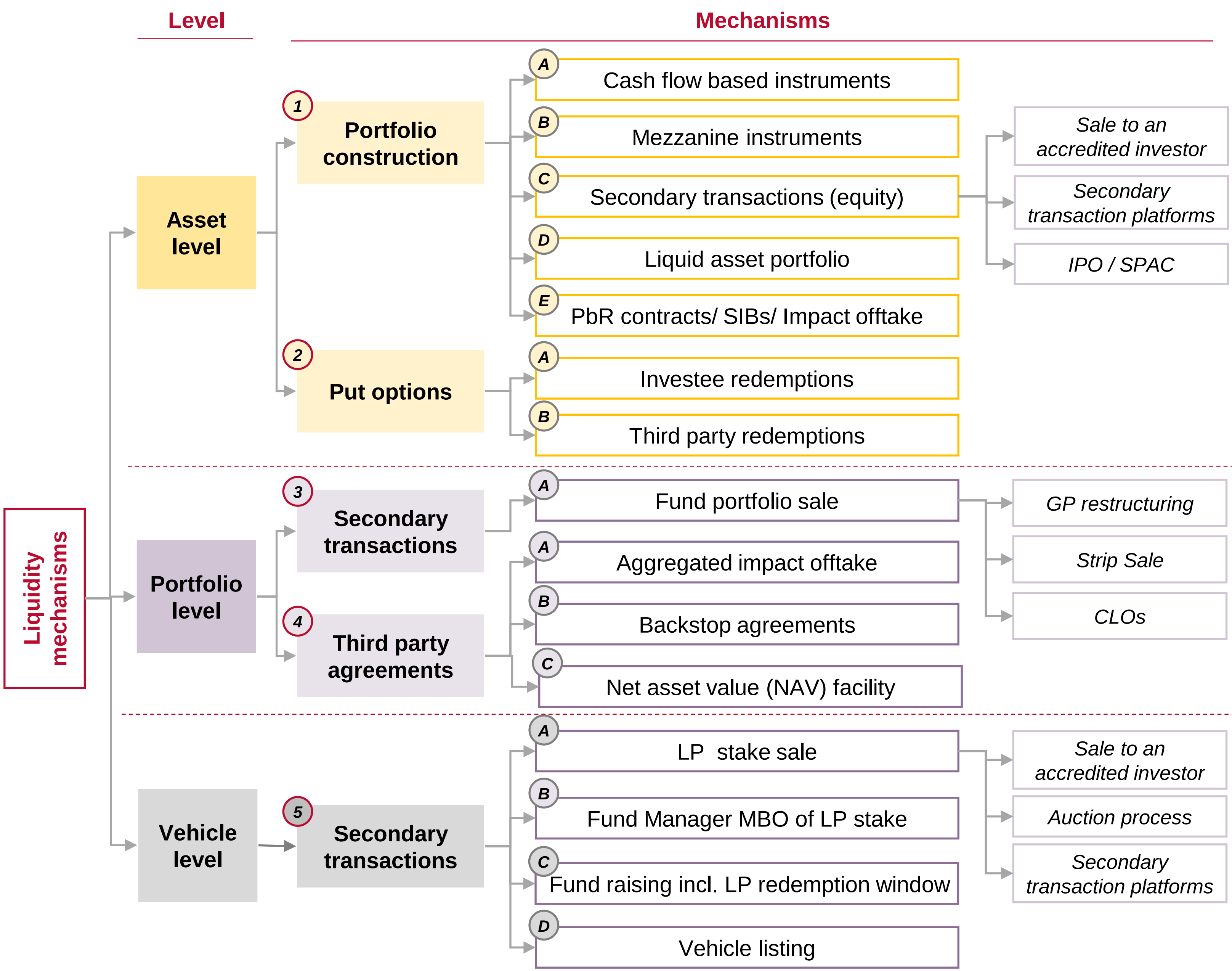
Key benefits

- **Liquidity**: The redemption reserve provides LPs with comfort of a possible future exit, when needed.
- **Long-term investments:** Lock-up period and/or redemption fees or discounts can encourage a long-term hold by LPs.

Example

- **SFRE:** A permanent capital vehicle supporting sustainability-focused financial institutions.
  - Vehicle provides liquidity via a reserve with quarterly liquidity windows, holding a 10% liquidity reserve of cash, cash equivalents and other liquid funds.
  - SFRE has both a lock up period and applies staggered redemption fees if access to the window is requested within the first 10 years of respective LP investment.

Liquidity mechanisms across various levels are set out below



Liquidity route

Generate CF from the fund's portfolio for shareholder distributions through:

1) **Dividend issuance;**
2) **Capital redemptions**: *CF from assets would accumulate in the redemption reserve, which could be distributed to investors at specific times (redemption/ liquidity windows).*
3) **Impact unit sales**

Generate liquidity **through full or partial sale of portfolio assets or impact units** held by equity investors in the vehicle.

Generate liquidity **through full or partial sale of shares or fund units** held by equity investors in the vehicle.

Asset level

Mechanisms available at the asset level

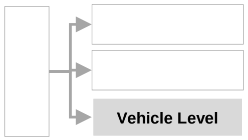
Mechanism	Overview	Challenges	Benefits
1A **Cash flow based instruments**	Self liquidating debt instruments producing cash flow	× Not context specific × Limited additionality × Inflexible	✓ Structured, aligned self-liquidating ✓ De-risked (if collateralised)
1B **Mezzanine instruments**	Portfolio that is fully comprised of or heavily weighted towards instruments that combine characteristics of debt with those of equity	× Equity-like unpredictability of final cash flows	✓ Predictable interest payments ✓ Flexible ✓ De-risked (if collateralisedl)
1C **Secondary transactions**	Exits of equity stakes	× Challenging to value × Unpredictable timing of liquidity	✓ De-risked (primary investor cycle)
1D **Liquid asset portfolio**	Holdings of liquid public assets to provide instant liquidity	× LP restrictions × Limited assets available × Impact story compromised × Increased burdens	✓ Public market liquidity ✓ Liquidity available at short-notice
1E **Impact offtake**	Selling the impact to an offset / output purchaser as another avenue for revenue	× Uncertain outcome × Limited saleable markets × Distracts from impact × Increased burdens	✓ Improved liquidity at minimal added cost
2A **Investee redemptions**	Liquidity accessed via the exercising of a put option on the security issued by the investee	× Difficult to enforce × More expensive × Suggestive of low conviction	✓ Expedites liquidity event
2B **Third party redemption**	Liquidity accessed via the exercising of a put option on the security issued by the investee, against a 3rd party	× Limited issuer market × Discounted price × Suggestion of low conviction	✓ Guarantees liquidity event

Discussed in more detail in the appendix

Available at the portfolio level

	Mechanism	Overview	Challenges	Benefits
3A	**Fund portfolio sale**	Sale of the entire portfolio or a large portion thereof in a single transaction	× Intensive valuation process × Uncertain outcome × Limited precedents	✓ De-risked (primary investor cycle) ✓ Visible and diversified assets
4A	**Aggregated impact offtake**	Selling the aggregated impact to an offset / output purchaser as another avenue for revenue	× Uncertain outcome × Limited saleable markets × Distracts from impact × Increased burdens	✓ Improved liquidity at minimal added cost
4B	**Backstop agreements**	Liquidity provided by a 3rd party offering redemption windows, typically at a discount after a lock up period	× Difficult to find counterparty × Limited precedents × Discounted price	✓ Guarantees liquidity event ✓ Provides downside protection
4C	**Net asset value (NAV) facility**	Liquidity provided through a leveraged share buy-back	× Limited liquidity × Limited precedents × Change of control issues × Mature assets	✓ No cash drag

Discussed in more detail in the appendix



Available at the vehicle level

	Mechanism	Overview	Challenges	Benefits
5A	**LP stake sale**	Liquidity provided by the sale of a partial or full LP stake sale to a secondary investor	× Intensive valuation process × Uncertain outcome × Unproven investor demand × Limited precedents × Unproven DD process	✓ De-risked (primary investor cycle) ✓ Visible and diversified assets ✓ Access retail investors ✓ Bridge financing gap
5B	**Fund Manager MBO of LP stake**	The fund manager agrees to provide liquidity through a purchase of the LP stake at a pre-agreed time, usually with leverage	× Uncertain outcome × Unproven investor demand × Limited precedents × Unproven DD process	✓ Visible and diversified assets ✓ Regulatory support ✓ Access retail investors
5C	**Fund raising incl. LP redemption window**	Set fund raising periods, whereby the use of proceeds is split between growth equity and redemption windows	× Cap raise dependant × Lack of investor appetite × Complex × Intensive valuation process	✓ Visible, mature assets ✓ No cash drag
5D	**Vehicle listing**	Liquidity provided by secondary LP stake sales in the public markets after listing the vehicle	× Market driven liquidity × Price volatility × Uncontrollable outflows × High costs	✓ Low minimum investment ✓ Liquidity bridge ✓ Accessibility and governance

Discussed in more detail in the appendix

Conclusion

Key recommendations include:

A

Evaluate if the vehicle structure is fit for purpose

- Whilst an evergreen nature addresses key challenges faced by potential investees, might other options be more appropriate?
- Open-ended vehicles need further governance structures/ aligned incentives – and may limit the investor universe, yet it will ensure flexibility and a lack of a forced exit event, often with inopportune timing from a financial and impact perspective.
- Longer (but fixed) term vehicles may address the same underlying challenges, yet still create forced exits when running up against the hard tenor and as such would only partly overcome the challenges.
- Thus it is important to weigh up the need for a wide prospective investor base, the investee's need for patient capital and the tension between ensuring the best exit and proactively incentivising that exit. As such further structure evaluation is necessary.

B

Work closely with asset owners to identify and loosen investment restrictions

- Identify the key factors that help inform these restrictions in conjunction with the boards / trustees, etc.
- Identify what proof points are necessary and what evidence could be used to ensure a better alignment between capital demand and supply.
- Find areas that are using developed markets constraints and ensure context specificity is built in.

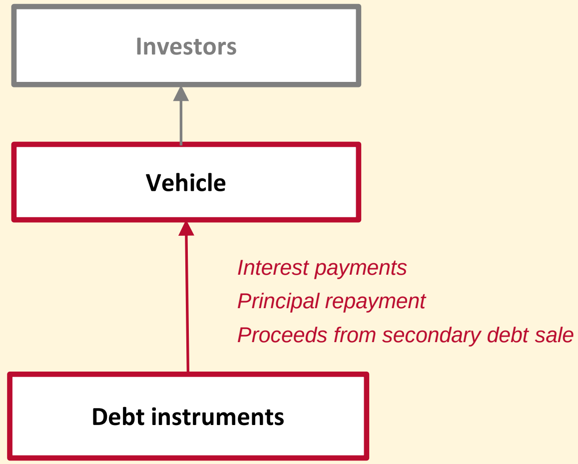
Appendix

1A Portfolio Construction - Cash flow based instruments

Facility Strategy

- **Overview:** Invest using debt heavy instruments which produce a steady cash flow.
- **Mechanism:** The portfolio of debt ensures a steady and predictable cash flow of interest and principal. The return of capital by investees can then be distributed back to the investors. Due to instruments used the predictability of cash flows will be much higher and collateral can be used to ensure the recovery of principal in the predetermined time frame.
- **Alternative**: a reinvestment clause, when reinvesting returns from the various investments (incl. equity), this must be into debt like investments which produces a steady and predictable cash flow in order to meet investors liquidity requirements.

Illustration of potential mechanism



Key challenges

- **Context specific:** Debt in this instance behaves much like equity, it is often seen as being venture debt and therefore lacking in predictability of cash flows and stability.
- **Additionality:** The additionality thereof is particularly lacking as the need for collateral makes is very similar to bank debt and excludes a large part of the potential pipeline.
- **Inflexibility:** This decreases the flexibility of the fund to be able to meet the needs of the investee and further help them scale

Key benefits

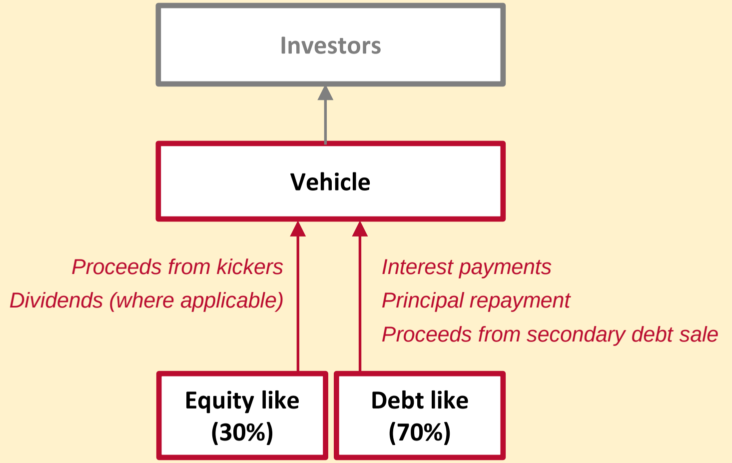
- **Structured, aligned liquidity:** Private debt investments produce a steady and predictable cash flow in order to meet investors liquidity requirements.
- **De-risked:** Collateral can be used to ensure the recovery of principal in the predetermined time frame, if cash flows are unattainable.

1B Portfolio Construction - mezzanine instruments

Facility Strategy

- **Overview:** Invest using mezzanine instruments which produce a cash flow as well as allow for kickers
- **Mechanism:** The portfolio of mezz ensures a cash flow of interest and principal, as well as gives the opportunity for equity like returns from the kickers. The return of capital by investees can then be distributed back to the investors. Due to instruments used the predictability of cash flows will be much higher and collateral can be used to ensure the recovery of principal in the predetermined time frame. Then, further upside can be generated by the use of kickers/warrants.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Equity-like unpredictability of final cash flows:** Mezzanine instruments in this instance can behave much like equity, it is often seen as being venture debt and therefore lacking in predictability of cash flows and stability.

Key benefits

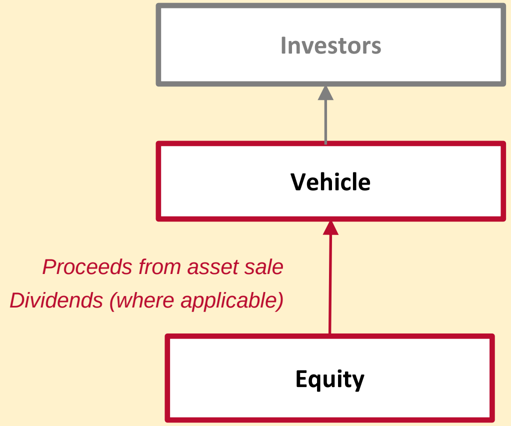
- **Predictable interest payments:** The private debt-like investments produce a steady and predictable cash flow in order to meet investors liquidity requirements. Then the equity like kickers produce further upside.
- **Flexibility:** The additionality and flexibility thereof is apparent as the instrument is flexible and context specific.
- **De-risked:** Collateral can be used to ensure the recovery of principal in the predetermined time frame, if cash flows are unattainable.

1C Secondaries market - Asset secondaries sale (equity)

Facility Strategy

- **Overview:** Sell an asset to a secondaries investor either directly to an accredited investor or through a platform.
- **Mechanism:** The secondary purchaser will purchase an existing investment currently on the balance sheets of the open ended vehicle, thus providing liquidity to their original investors.
- **Alternative**: **A)** IPO / SPAC - A SPAC is a listed holding company without any assets. The SPAC then finds a private target company and purchases shares therein. Thus the LPs would then have indirectly taken the private company public and would have access to liquid holdings of a private company, an IPO is the opposite way around. **B)** Current LP purchases the asset out of the fund

Illustration of potential mechanism



Key challenges

- **Challenging to value:** Critical and intensive valuation processes
- **Unpredictable timing of liquidity:** Liquidity is dependent on ensuring an agreement, therefore it cannot be guaranteed and the context is important. The African Agri sector has struggled to produce exits that are not trade sales; as such, IPOs and SPACs are very unlikely.

Key benefits

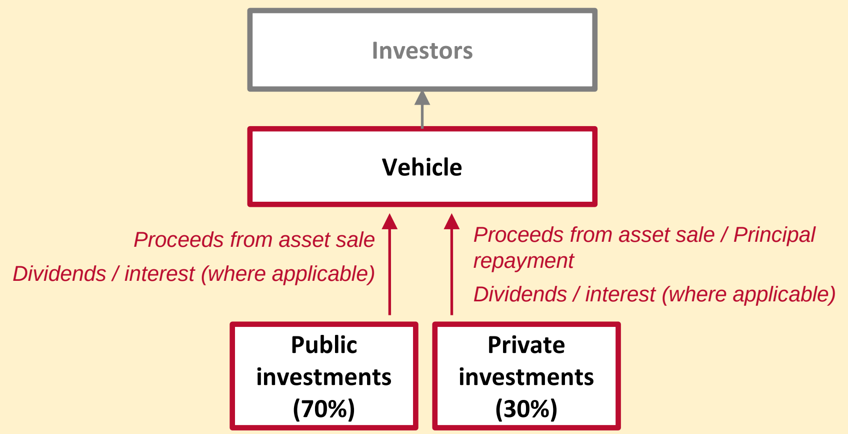
- **De-risked (primary investor cycle):** Secondary investors will be investing fully in existing assets held by primary investors, thus the assets have had a period to mature and benefit from financing and support and thus are less risky.

1D Portfolio Construction - Liquid asset portfolio

Facility Strategy

- **Overview:** Combined the high impact private portfolio with an ‘aligned impact’ or sustainability oriented portfolio of public equities
- **Mechanism:** Building and holding a portfolio which has a large portion of liquid assets. This allows investors to access the liquidity of the public markets for sale of assets at any point that liquidity is necessary for LPs.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **LP restrictions:** LPs may have restrictions on their ability to hold these types of assets, or if they are they may have been looking at this structure as a way to diversify away from public assets (Listed assets).
- **Limited assets available:** There are limited listed assets available that would meet the requirements, such as geography and thematic, as public markets are nascent in many of there markets
- **Impact story compromised:** The Impact angle would be diminished as there would be a focus on listed assets, meaning that the additionality and investment stage would be minimised
- **Expense/ regulatory burden:** Further regulatory and legal requirements would apply as well as a further expense burden.

Key benefits

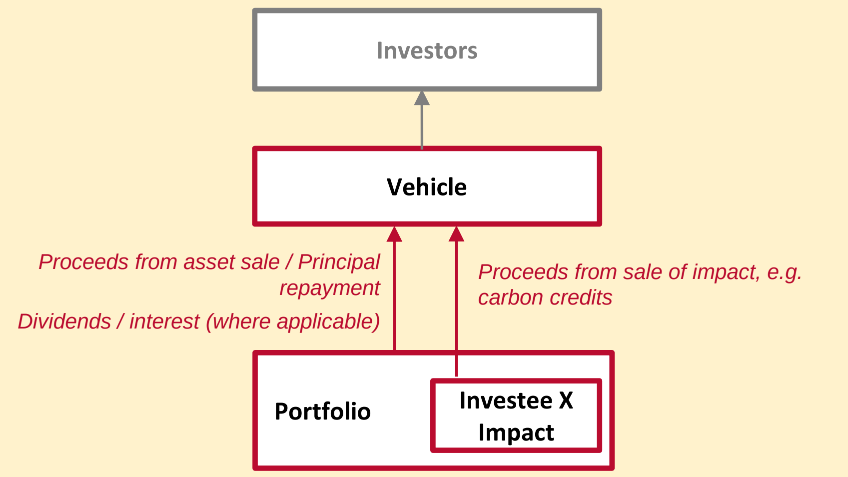
- **Public market liquidity:** The public market liquidity would transfer to a large portion of the fund and thus would provide liquidity to investors.
- **Liquidity available at short-notice:** Liquidity would be available at any point necessary and thus flexible liquidity would be constantly available.

1E Portfolio Construction - PbR contracts/ SIBs/ Impact offtake

Facility Strategy

- **Overview:** Portfolio company focus on sustainably providing a product that also decreases carbon (or equivalent) which is saleable.
- **Mechanism:** Building and holding a company which sells a product or service an also provides for an opportunity to sell the impact, such as carbon or equivalent, to a structed market.. An example of this may be a sustainable forestry company that has the ability to sell the output (hard wood) and the impact (carbon offsets). These offsets can be sold to the market and the earnings used as liquidity to LPs. Such a purchaser could be an airline for example.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Uncertain outcome:** There is no guarantee that the outcome will be achieved and liquidity accessed at a specified point in time.
- **Limited saleable markets:** There are limited markets available to sell this impact
- **Distracts from impact:** The Impact angle would be diminished as there would be a focus on offsetting rather than decreasing carbon for instance.
- **Expense/ regulatory burden:** Further regulatory and legal requirements would apply as well as a further expense burden and capabilities necessary for M&E and market access and verification.

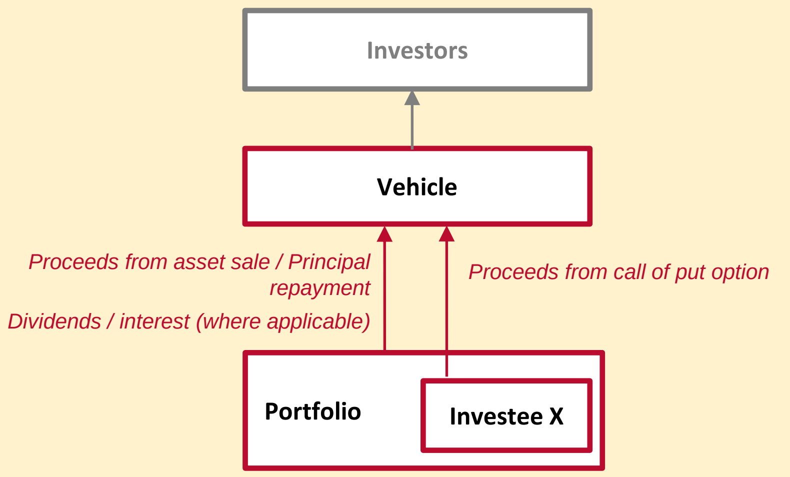
Key benefits

- **Improved liquidity at minimal added cost:** There would be an additional form of liquidity and earnings that could be accessed at limited additional cost.

2A Put option - Investee redemptions

Facility Strategy	▪ **Overview:** an instrument which gives the holder the right to sell an asset, at a specified price, by a specified date to the writer of the put, in this case the management of the portfolio company. ▪ **Mechanism:** Building a put option into the purchase agreement provides the fund manager the option to sell the stake to the management of the portfolio company if they have failed to provide an exit at the agreed upon time. This would look to ensure liquidity at a predetermined time and value from the outset of the acquisition. ▪ **Alternative**: N/A
Key challenges	▪ **Difficult to enforce:** There is no guarantee that the management team will have the ability to provide liquidity at the specified point in time, thus enforceability is difficult. ▪ **More expensive:** This would decrease the bargaining power during negotiations, potentially leading to a higher value being placed on the acquisition multiple. ▪ **Suggestive of low conviction:** The purchase of a put option is interpreted as a negative sentiment about the future value of the underlying stock
Key benefits	▪ **Expedites liquidity event:** There would be further impetus to ensure an exit or liquidity event before the agreed maturity thereof.

Illustration of potential mechanism

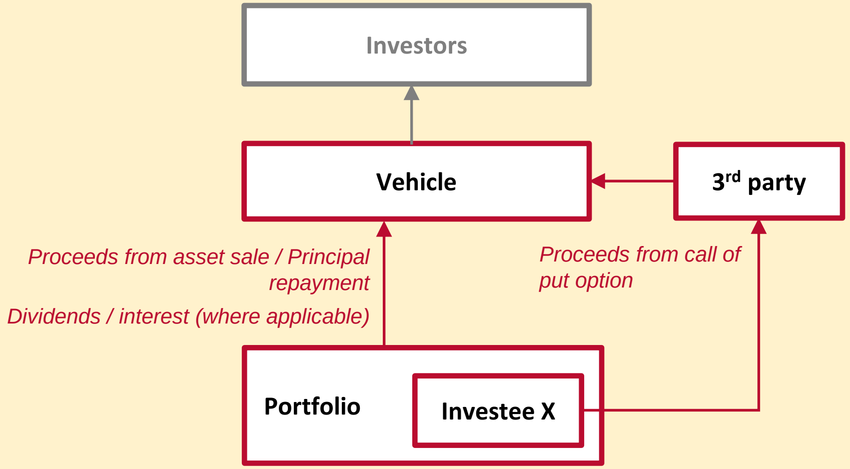


2B Put option - 3rd party redemptions

Facility Strategy

- **Overview:** an instrument which gives the holder the right to sell an asset, at a specified price, by a specified date to the writer of the put, in this case a third party.
- **Mechanism:** Building a put option into the purchase agreement provides the fund manager the option to sell the stake to a 3rd party if they have failed to provide an exit at the agreed upon time. This would look to ensure liquidity at a predetermined time and value from the outset of the acquisition.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Limited issuer market:** There is no guarantee that there will be a willing writer of the put option.
- **Discounted price:** This would normally come at a large discounted value.
- **Suggestive of low conviction:** The purchase of a put option is interpreted as a negative sentiment about the future value of the underlying stock

Key benefits

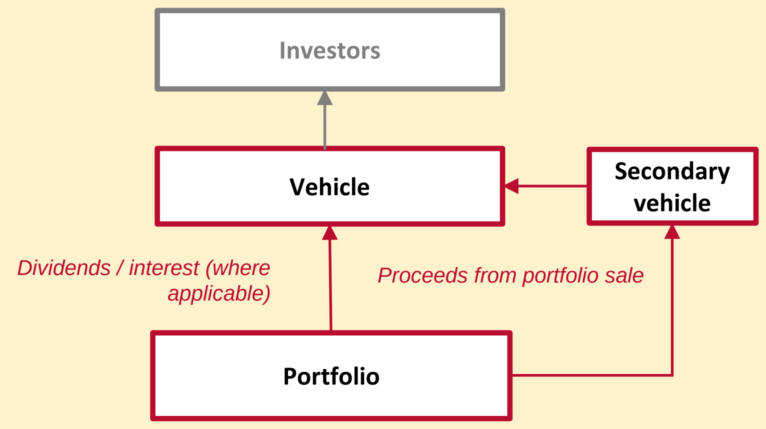
- **Guarantees liquidity event:** There would be a guarantee of a liquidity event, even if it may be at a large discount.

3A Secondaries market - Portfolio secondaries sale

Facility Strategy

- **Overview:** Set up as a feeder fund for a secondaries investor with a portfolio level sale, either assets or LP position.
- **Mechanism:** The secondary purchaser will purchase aggregated existing investments currently on the balance sheets of the open ended vehicle, thus providing liquidity to their original investors.
- **Alternative**: **A)** GP restructuring, funds that have exceeded their expected lifecycle and the remaining assets of a fund are rehoused into a new vehicle. **B)** Strip Sale, A form of fund restructuring which involves the partial sale of a fund's investment (strip) in all/some underlying assets to provide LPs with liquidity at any point of the lfund life. **C)** CLOs, whereby you sell a diversified portfolio of loans in a bundled manner to a pre-agreed offtaker at a specific time

Illustration of potential mechanism



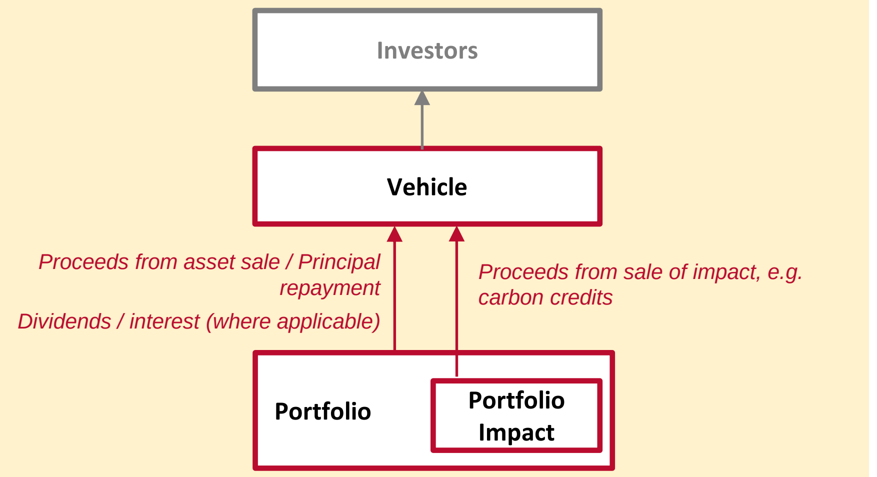
Key challenges

- **Intensive valuation process:** Critical and intensive valuation processes when raising capital or to enable liquidity mechanisms
- **Uncertain outcome:** Liquidity is dependent on ensuring an agreement, therefore it cannot be guaranteed
- **Limited precedents:** There are very few precedents of this and thus convincing investors may be particularly difficult

Key benefits

- **De-risked (primary investor cycle):** Secondary investors will be investing fully in existing assets held by primary investors, thus the assets have had a period to mature and benefit from financing and support and thus are less risky.
- **Visible and diversified assets:** The secondary investor gets a diversified portfolio of assets instead of a single asset and has visibility of each asset therein.

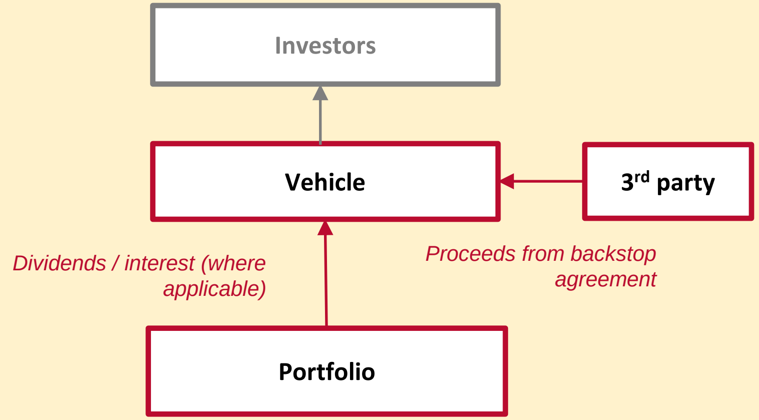
4A 3rd party agreements - Aggregated impact offtake

Facility Strategy	▪ **Overview:** Portfolio companies focus on sustainably providing a product that also decreases carbon (or equivalent) which is aggregated and sold. ▪ **Mechanism:** Building and holding a portfolio of companies which sells a product or service and also provides for an opportunity to sell the aggregated impact, such as carbon or equivalent, to a structed market. This portfolio of offsets can be sold to the market and the earnings used as liquidity to LPs. An example purchaser could be an airline for example. ▪ **Alternative**: N/A	**Illustration of potential mechanism** 
Key challenges	▪ **Uncertain outcome:** There is no guarantee that the outcome will be achieved and liquidity accessed at a specified point in time. ▪ **Limited saleable markets:** There are limited markets available to sell this impact ▪ **Distracts from impact:** The Impact angle would be diminished as there would be a focus on offsetting rather than decreasing carbon for instance. ▪ **Expense/ regulatory burden:** Further regulatory and legal requirements would apply as well as a further expense burden and capabilities necessary for M&E and market access and verification.	
Key benefits	▪ **Improved liquidity at minimal added cost:** There would be an additional form of liquidity and earnings that could be accessed at limited additional cost.	

4B 3rd party agreements - Backstop agreement

Facility Strategy	▪ **Overview:** A third party would provide partial liquidity by purchasing positions of the current LPs. ▪ **Mechanism:** The third party would offer to purchase a specified percentage of the portfolio at a specified period of time at a predetermined value. For example, after 6 years they would purchase 10% of the portfolio per annum at NAV -20%. This would provide liquidity security at specific times if there was a lack of liquidity from the portfolio. ▪ **Alternative**: **A)** a leveraged share buyback, useful in a scenario where exits have not happened, but the underlying investments are healthy enough to take on debt against. **B)** redeemable equity whereby the LP redeems a portion of their stake.
Key challenges	▪ **Difficult to find counterparty:** Identifying and convincing a 3rd party to provide liquidity to a DFI is particularly difficult. ▪ **Limited precedents:** Not many precedents for providing this service exist in the market ▪ **Costly:** Costly for the liquidity backer to hold the cash necessary to provide the guaranteed windows ▪ **Discounted price:** Traditionally a large discount necessary on the NAV to access liquidity for LPs
Key benefits	▪ **Guarantees liquidity event:** Guaranteed redemption windows, even if at steep discounts ▪ **Provides downside protection:** The chance that the portfolio will create enough liquidity to ensure this is not necessary, yet having the guarantee de-risks the portfolio and investment

Illustration of potential mechanism

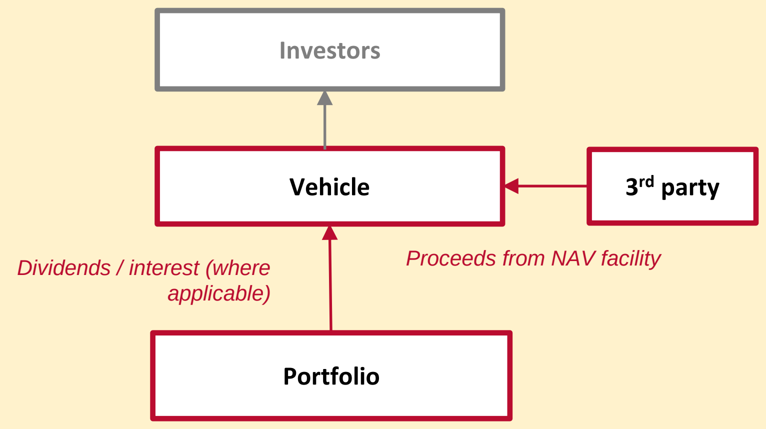


4C 3rd party agreements - Net asset value (NAV) facility

Facility Strategy

- **Overview:** A third party would provide partial liquidity by leveraging a 3rd parties facility to ensure a share buyback.
- **Mechanism:** The third party would provide a facility which is secured against the cashflow and/or net asset value of a fund's entire investment portfolio. The facility is typically provided to an intermediate holding vehicle that sits below the fund and owns all or most of the portfolio companies. The debt provided would then be used for share buybacks, providing partial liquidity to current LPs. The 3rd party would then have preference on repayment in accordance with a debt facility.
- **Alternative**: Some lenders, typically non-bank lenders, can provide liquidity by taking preferred stock in the fund structure rather than by way of a loan facility.

Illustration of potential mechanism



Key challenges

- **Limited liquidity:** The extent of the liquidity would be capped by the borrowing limits in the LPA.
- **Limited precedents:** Not many precedents for providing this service exist in the market
- **Change of control issues:** Given the intermediate holding company sits directly between the investments and the fund
- **Costly:** Costly for the fund to access liquidity
- **Mature assets:** Only applicable to mid- to end-of-life funds holding mature assets.

Key benefits

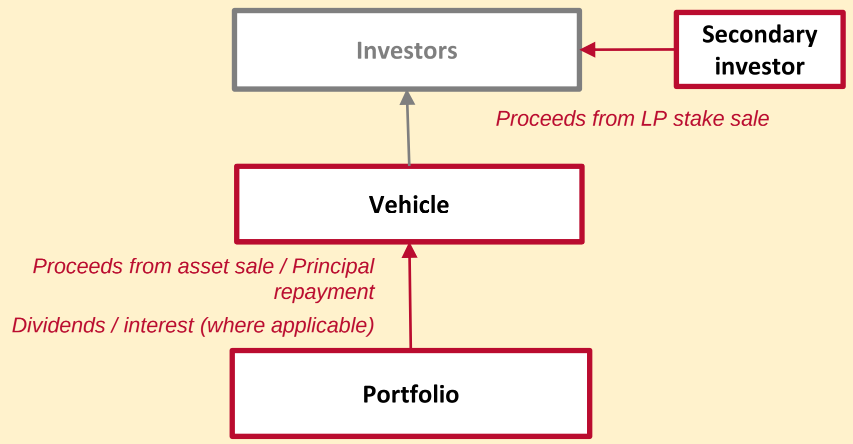
- **No cash drag:** There is no cash drag by holding cash assets for redemption purposes

5A Secondaries market - LP positions sale to accredited investor

Facility Strategy

- **Overview:** Sell the LP position in the fund to an accredited investor.
- **Mechanism:** The secondary purchaser will purchase the LP position within the fund of aggregated existing investments currently on the balance sheets of the open ended vehicle, thus providing liquidity to their original investors.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Intensive valuation process:** Critical and intensive valuation processes when raising capital or to enable liquidity mechanisms
- **Uncertain outcome:** Liquidity is dependent on ensuring an agreement, therefore it cannot be guaranteed
- **Limited precedents:** There are very few precedents of this and thus convincing investors may be particularly difficult

Key benefits

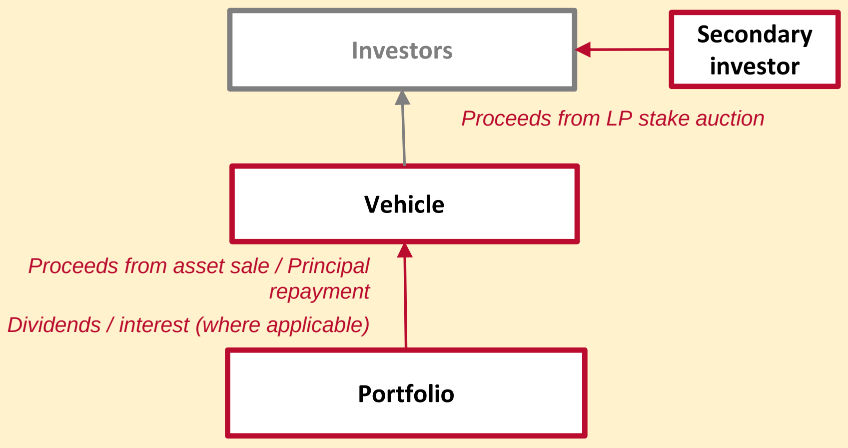
- **De-risked (primary investor cycle):** Secondary investors will be investing fully in existing assets held by primary investors, thus the assets have had a period to mature and benefit from financing and support and thus are less risky.
- **Visible and diversified assets:** The secondary investor gets a diversified portfolio of assets instead of a single asset and has visibility of each asset therein.

5A Secondaries market - LP position auction

Facility Strategy

- **Overview:** Set up as a fund with a mechanism to create liquidity via a secondary sale on an auction platform.
- **Mechanism:** The potential secondary purchasers will bid on an auction platform, and the highest bidder(s) would purchase shares of the current LPs position of existing investments currently on the balance sheets of the open ended vehicle, thus providing liquidity to their original investors.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Uncertain outcome:** Liquidity is dependent on ensuring an agreement, therefore it cannot be guaranteed
- **Unproven investor demand:** There are not many investors who currently use platforms like this and therefore finding investors to bid may be difficult
- **Limited precedents:** There are very few precedents of this and thus convincing investors may be particularly difficult
- **Regulatory burden:** There are added regulatory requirements and legal complexities to offering this mechanism
- **Unproven DD process:** Difficult and unproved DD processes

Key benefits

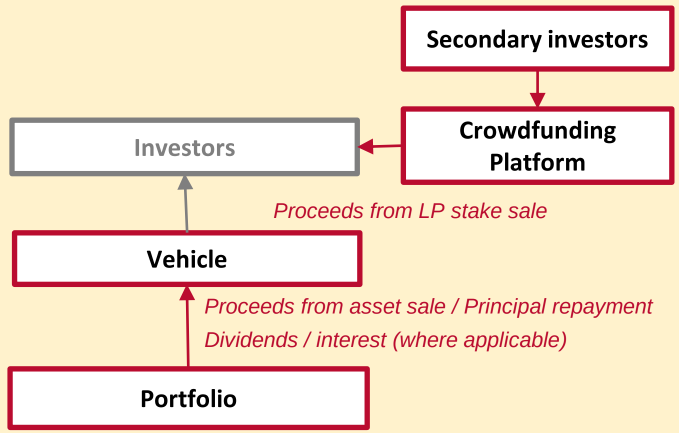
- **De-risked (primary investor cycle):** Secondary investors will be investing in existing assets held by primary investors
- **Access retail investors:** A securities law exemption, allows crowdfunding portals to raise just over $1 million from everyday investors, alongside unlimited amounts from high-net-worth individuals and other "accredited" investors.
- **Bridge financing gap:** The new platforms helps bridge a financing gap for small and mid-sized projects and ventures. Such ventures can make a big difference in communities, yet are typically too small for institutional investors.

5A Secondaries market - LP position sales to crowdfunding platform

Facility Strategy

- **Overview:** Set up as a fund with a mechanism to create liquidity via a secondary sale on a crowdfunding (or equivalent) platform.
- **Mechanism:** The secondary purchasers (retail purchasers) will be aggregated on a platform and purchase shares of the current LPs position of existing investments currently on the balance sheets of the open ended vehicle, thus providing liquidity to their original investors.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Intensive valuation process:** Critical and intensive valuation processes when raising capital or to enable liquidity mechanisms
- **Uncertain outcome:** Liquidity is dependent on ensuring an agreement, therefore it cannot be guaranteed
- **Limited precedents:** There are very few precedents of this and thus convincing investors may be particularly difficult
- **Regulatory burden:** There are added regulatory requirements and legal complexities to offering this to non-accredited investors
- **Unproven DD process:** Difficult and unproved DD processes

Key benefits

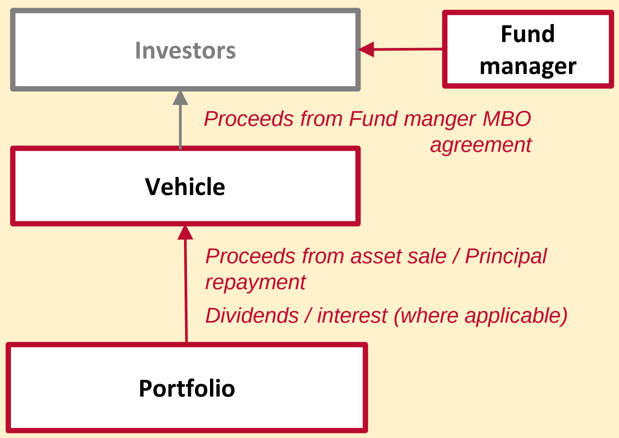
- **De-risked (primary investor cycle):** Secondary investors will be investing in existing assets held by primary investors
- **Access retail investors:** A securities law exemption, allows crowdfunding portals to raise just over $1 million from everyday investors, alongside unlimited amounts from high-net-worth individuals and other “accredited” investors.
- **Bridge financing gap:** The new platforms help bridge a financing gap for small and mid-sized projects and ventures. Such ventures can make a big difference in communities, yet are typically too small for institutional investors.

5B Secondaries market - Fund Manager MBO of LP stake

Facility Strategy

- **Overview:** Set up as a fund with a mechanism that the GP guarantees a liquidity event, and if exits have not been reached, then via a secondary sale of the LP position to the GP.
- **Mechanism:** MBO-like liquidity, the management company (GP), could state that they would play the secondary purchaser role and guarantee liquidity at specific times, if they do not provide it, they would purchase the assets (traditionally by using leverage).
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Uncertain outcome**: Liquidity is dependent on ensuring an agreement, therefore it cannot be guaranteed
- **Unproven investor demand:** There are not many investors who currently use platform like this and therefore finding investors to bid may be difficult
- **Limited precedents:** There are very few precedents of this and thus convincing investors may be particularly difficult
- **Legal burden:** There are added regulatory requirements and legal complexities to offering this mechanism
- **Unproven DD process:** Difficult and unproved DD processes

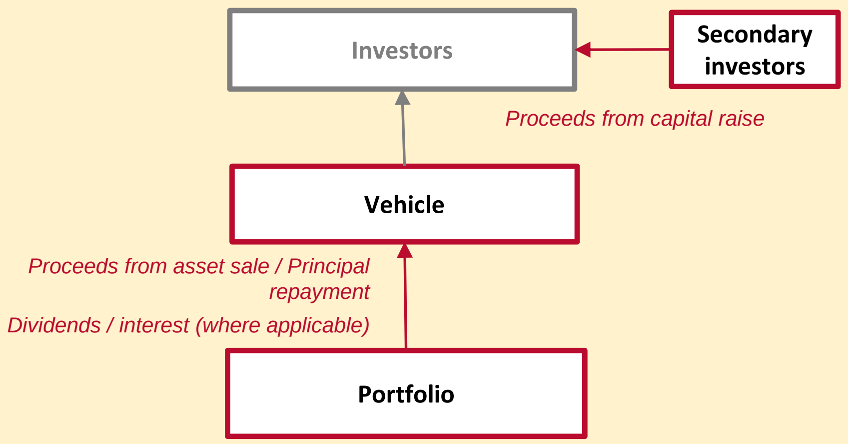
Key benefits

- **Visible and diversified assets:** Secondary investors will be investing in existing assets held by primary investors
- **Regulatory support:** A securities law exemption, allows crowdfunding portals to raise just over $1 million from everyday investors, alongside unlimited amounts from high-net-worth individuals and other “accredited” investors.
- **Access retail investors:** The new platforms help bridge a financing gap for small and mid-sized projects and ventures. Such ventures can make a big difference in communities, yet are typically too small for institutional investors.

5C Secondaries market - Fund raising incl. LP redemption window

Facility Strategy	▪ **Overview**: Set fund raising periods, whereby the use of proceeds is split between growth equity and redemption ▪ **Mechanism:** The open ended vehicle would look to run fund raising at specified intervals. The proceeds of these fund raises will be used partly to redeem current LPs (e.g. 20% of capital raise) and partly as growth / investment equity (e.g. the remaining 80% of the capital raise). ▪ **Alternative**: N/A
Key challenges	▪ **Capital raise dependant:** Liquidity is dependent on ensuring a capital raise, therefore it cannot be guaranteed ▪ **Lack of investor appetite:** There are not many investors who currently use platform like this and therefore finding investors to bid may be difficult ▪ **Lack of precedents:** There are very few precedents of this and thus convincing investors may be particularly difficult ▪ **Complex:** There are added complexities to offering this mechanism ▪ **Intensive valuation process:** Critical and intensive valuation processes
Key benefits	▪ **Visible, mature portfolio:** Further investors will be investing in existing, visible and more mature assets ▪ **No cash drag:** There is no cash drag by holding cash assets for redemption purposes

Illustration of potential mechanism

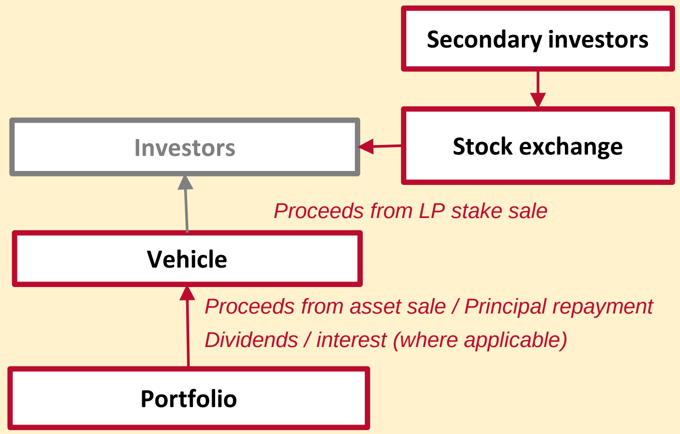


5D Secondaries market - listed impact investing vehicle

Facility Strategy

- **Overview:** Listed investment vehicles makes investing for impact in developing countries available to all categories of investors in a liquid, low minimum investment, highly regulated format
- **Mechanism:** An investment company is created. It raises capital through an IPO on the Stock Exchange, and invests the proceeds in a diversified portfolio of impact investments. If an individual investor wants to exit their investment, they instruct the private bank to sell their shares to another investor through the stock exchange. The investment company is a open ended investment vehicle, its illiquid underlying portfolio is not affected by the stock exchange transactions.
- **Alternative**: N/A

Illustration of potential mechanism



Key challenges

- **Market driven liquidity:** Liquidity is market driven, not guaranteed
- **Price volatility:** Share price is demand/supply driven, not directly linked to the NAV, premiums and discounts are to be expected
- **Uncontrollable outflows:** High volatility and outflows can lead to crippling of the fund

Key benefits

- **Low minimum investment** and **High level of governance**
- **Liquidity bridge:** Bridge the liquidity gap to underlying impact investing funds
- **Accessibility:** Public listing guarantees accessibility, as individual investors from most countries can shares traded on a major stock exchange.

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