

Private equity and the pandemic

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By Tim Gocher, Founder & CEO, Dolma Impact Fund

Private equity funds can save companies and jobs. They can also invest in growth opportunities created by the pandemic. But Nepal's slow approval processes restrict what such funds can achieve.

Covid-19 has hit companies with a double whammy. Cash flow has fallen off a cliff for both companies and many of their shareholders. If the banks can't lend, or the government can't step in, shareholders may not be in a position to inject more equity capital to keep their companies afloat on these stormy seas. This is a tragedy for employment, and the economy as a whole, as companies that were healthy before the pandemic face closure.

Private equity funds are shielded from such crises. They typically have a fixed life—often 10-12 years—and a fixed size, regardless of underlying economic conditions. This means that they can think longer term, and back their portfolio companies in a downturn.

Resource constraints

Nepal's government does not have the economic capacity for significant private sector support, as more developed countries do. In the UK, for example, the government is essentially paying salaries to 8.7 million workers—a quarter of the country's non-government workforce—at a monthly cost of £14 billion (around \$17.2 billion), according to the BBC. It has also provided 100 percent government guarantees to banks for loans to small businesses of up to £50,000 (\$62,000), allowing emergency funding to flow rapidly. This massive support programme is financed largely through government borrowing on the international sovereign bond markets at historically low interest rates. And even with this support, the UK economy and employment will suffer a severe blow.

With no sovereign credit rating or international bond issue to date, Nepal does not have this option. Nepal also faces an additional unemployment crisis with workers abroad returning home en masse.

International private equity investment into Nepal can be an essential pillar alongside local investors, government and donors in response to the current crisis. And fund managers of such capital already investing in Nepal are active. In May alone, Dolma Impact Fund approved further investment to cover cost overruns for hydropower projects—in part caused by lockdown delays, as well as growth capital for a technology company. Business Oxygen has five investments awaiting Foreign Direct Investment (FDI) approval—without which no international capital can enter the country. And One to Watch is providing business development support to portfolio companies. Private equity 'has the potential to maintain jobs and bring companies back to revenue after the crisis', says Willem Grimmink, founder of One to Watch.

There are a few caveats to the above. Private equity funds that invest in mature industries with high levels of debt (that is, acquisition through leveraged buyouts) are suffering. But private equity investments in Nepal don't follow this model, and mostly focus on earlier stage, high growth companies or infrastructure investments such as hydro and solar. Also, if a fund is

reaching the end of its life and is fully invested, it won't have the ability to invest further. But the funds currently investing in Nepal still have the cash reserves needed to invest.

In addition to the ability to back portfolio companies with equity, such funds may have access to grant money to cover some of the costs of the crisis. For example, one of Dolma Impact Fund's investors, FMO, has provided a grant for personal protective equipment (PPEs), hygiene management training and awareness programmes for workers and community members. Dolma has also used such facilities to engage international consultants to help manage business continuity risks and plan for strategic growth after lockdown.

Private equity activity is not just about supporting existing investments. There are many investment opportunities arising from the pandemic. The health crisis has exposed a shortage of quality hospitals and clinics, particularly outside of the Kathmandu Valley. New healthcare technology, such as telemedicine and AI-driven diagnostic tools provide an opportunity to enhance healthcare infrastructure and provide services to more remote regions. Online shopping and payment will likely be all the more popular after the pandemic. And the inflexibility of Nepal's run-of-river power generation fleet has been exposed as demand has dropped, causing surpluses at some times, while still relying on imports from India, particularly during peak times. On-grid battery storage solutions can fix this issue and can be installed in months, not years. Batteries store energy when it isn't needed and shift it to times of the day when it is. These are all examples of where private equity will be looking to invest as Nepal emerges from the crisis.

Urgent response necessary

The government and regulators have a vital role to play if private equity's potential is to be realised in Nepal. Nepal's foreign direct investment process is slow and inefficient. Approvals can take anywhere from three months to over a year. The need for capital is urgent, and without an automatic route for foreign investment, as in India, Nepali companies and jobs will be lost before the money can hit the bank. At least in the short term, this could be implemented for internationally regulated, institutional investors and foreign investors who have already invested in Nepal and therefore cleared the necessary Know Your Client (KYC) and Anti-Money Laundering (AML) checks.

To stimulate investment in on-grid battery energy storage systems, specific tariffs are required. If tariffs, power purchase agreements and licences can be issued, the batteries themselves can be installed rapidly.

Private equity is a powerful force around the world in responding to the pandemic-induced economic crisis. The current focus of global investors on healthcare, technology and renewable energy chimes well with recent budget priorities. If Nepal acts quickly, it could benefit at a time when investment, jobs and energy self-reliance are needed the most.