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Case study

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The North West Evergreen Fund 1 and the Greater Manchester Fund of Funds

1.1 Context

The North West Evergreen Fund 1 (Evergreen Fund 1) was established by the local authorities of the Greater Manchester Combined Authority (GMCA) and other North West authorities to provide debt financing for development phases of commercial property and regeneration projects. During the initial investment phase of the fund, **its initial capital** of GBP 30 m **doubled**, reaching the total size of GBP 60.8 m, out of which 58 per cent comes from the ERDF financing. The fund was established during the 2007-2013 programming period and is still in operation. Following the end of the programming period, the Evergreen Fund 1 is now **reinvesting its capital** in accordance **with a wider investment strategy** compared to the initial scope in the beginning of its operations.

In order to oversee the investment of GBP 60 m of the ERDF funding for the 2014-2020 programming period, as well as to facilitate the city's sustainable economic development, the GMCA established the **Greater Manchester Fund of Funds** (GM Fund of Funds), following the experience with the **Evergreen 1** Fund, established two 'sub-funds' the **Evergreen Fund 2** and the **Low Carbon Fund**, responsible for the investment of an additional GBP 45 m and GBP 15 m of ERDF, respectively.

Priority areas of the GM Fund of Funds
Science, technology and innovation assets: Investment in the commercial floor-space of adequate volume, specifications and flexibility
Low-carbon infrastructure: Investment supporting transition to low-carbon economy including the energy and waste infrastructure

1.2 What is interesting about the North West Evergreen Fund?

The Evergreen Fund 1 is an example of the city fund that has **adjusted its offer during the lifespan of the fund** in order to reflect the needs of the projects and to address the market gap. This approach enabled the creation of **investment opportunities** that support the delivery of the city's sustainable urban development strategy. The fund has also successfully developed the **ecosystem of strategic investors**, who were involved in the delivery or co-financing of the projects. Following the commitment of its initial capital resources, the fund was able to maintain a high output and to maximise the impact delivered by **selling part of its loan book** and consequently **reinvest its funds**. This approach might be replicable if the cooperation between the city and investors, with the right motivation and capacity to become involved in the fund, is developed.

From the analysis, three main points of interest have been identified:

i. **Evolution in line with financing needs and opportunities**

ii. **Development of the ecosystem of investors**

iii. **Experience of the loan selling**

I. Evolution in line with financing needs and opportunities

The Evergreen Fund 1 evolved over the time and created its own financing opportunities to stimulate the city's economic development. In the beginning of its operations, the fund offered **mostly senior debt** to support initial development phases of construction projects with an emphasis on commercial properties and buildings' regeneration. The fund embraced such approach, since at that time (post financial crisis) the market was not in a position to provide low-risk senior debt to these investment opportunities. However, as soon as the private sector investors returned to provide senior debt financing, the fund broadened its focus to include provision of **higher-risk capital by providing mezzanine financing** (i.e. subordinated debt).

Flexibility and the market-adjusted offer enabled to address projects financing needs and reach city objectives

The Evergreen Fund 1 has **developed the ecosystem** of investors for the city's projects and has **created the financing capacity** for the Evergreen Fund 2. The Evergreen Fund 2 was set up together with the Low Carbon Fund, as a sub-fund of the GM Fund of Funds. This evolution shows how the **fund structure has been adjusted** to the investment needs, subsequently its structure has evolved from the single fund structure (Evergreen Fund 1) to the fund of funds structure in order to **respond to the evolving needs of the city**.

The fund strived to continuously **support the creation of investment opportunities**, also by ensuring a continuous availability of funding (through the sale of its portfolio of loans as explained later) in the most suitable form needed.

II. Ecosystem of strategic investors

The **creation of the eco-system of investors** and identification of the right profiles of investors are important drivers underpinning the successful evolution of the Evergreen 1 and set the scene for the loans selling experience described in the section below. The development of strategic network of investors is an activity that needs to be coordinated and managed by both: the Fund Manager and the city.

The experience of the Evergreen 1 proves that it is beneficial to involve strategic investors early on in the discussion stage and to keep them informed about the project pipeline development. This approach prepares the investors to join the investment scheme when their risk appetite meets projects' needs.

III. Experience of the loan selling

The sale of part of the Evergreen 1 loan book is an important takeaway from the experience of the Evergreen Fund 1. The **sale of a portfolio of four loans with a value of ca GBP 30 million** to the Greater Manchester Pension Fund allowed the early repayment of the capital investment to the fund**.** This allowed the capital to be **reinvested** in new projects without prejudicing the financing projects sold to the Greater Manchester Pension Fund (GMPF), which continued to benefit from financing on the same terms from the new lender.

2 The Northwest Evergreen Funds

2.1 The Northwest Evergreen Fund 1

The Northwest Evergreen Fund (Evergreen Fund 1)[1] was set up in 2010 under the JESSICA initiative[2] by the Greater Manchester local authorities and authorities from the adjoining sub-regions of Cheshire and Lancashire. The fund was one of two urban development funds set up under the North West Urban Investment Fund, the Holding Fund set up by the regional authority and ERDF Intermediate Body the North West Development Authority.

Evergreen 1 was set up with the following six investment priorities:

- Create a high-employment region;
- Invest in science, research and innovation;
- Build on the region's strengths in culture and media;
- Supporting strong and diverse town centres;
- Promoting a wider, stronger and more sustainable industrial base;
- Ensuring sustainable sites are ready for development.

The fund was established as a Limited Partnership under UK law. This structure allowed each authority to act as a Limited Partner with rights to receive information but not to manage the operation. The Limited Partnership was managed by a General Partner set up for that specific purpose which in turn appointed an independent professional services organisation, CBRE, to act as a Fund Manager of the financial instrument.

The governance of the fund was built around a strong appraisal process that was undertaken by CBRE, the independent Fund Manager. Potential projects were initially reviewed for ERDF compliance, additionality and deliverability. Projects that passed the initial assessment were reported to the General Partner board for Stage 1 approval, which would allow consideration of consistency with local priorities. Following Stage 1 approval, the Fund Manager would negotiate final terms of investment and report to the General Partner Board for final, Stage 2, approval prior to signature.

The fund's first investment was made in 2011 and, following a series of further investments from the Holding Fund, the fund achieved full commitment of resources by the summer of 2014. The outcome of the first round of investments was as follows:

Evergreen £'000	Public £'000	Private £'000	Total £'000	m2	B'field (ha)	Jobs
64,940	19,420	135,876	220,236	160,725	117.84	6,931

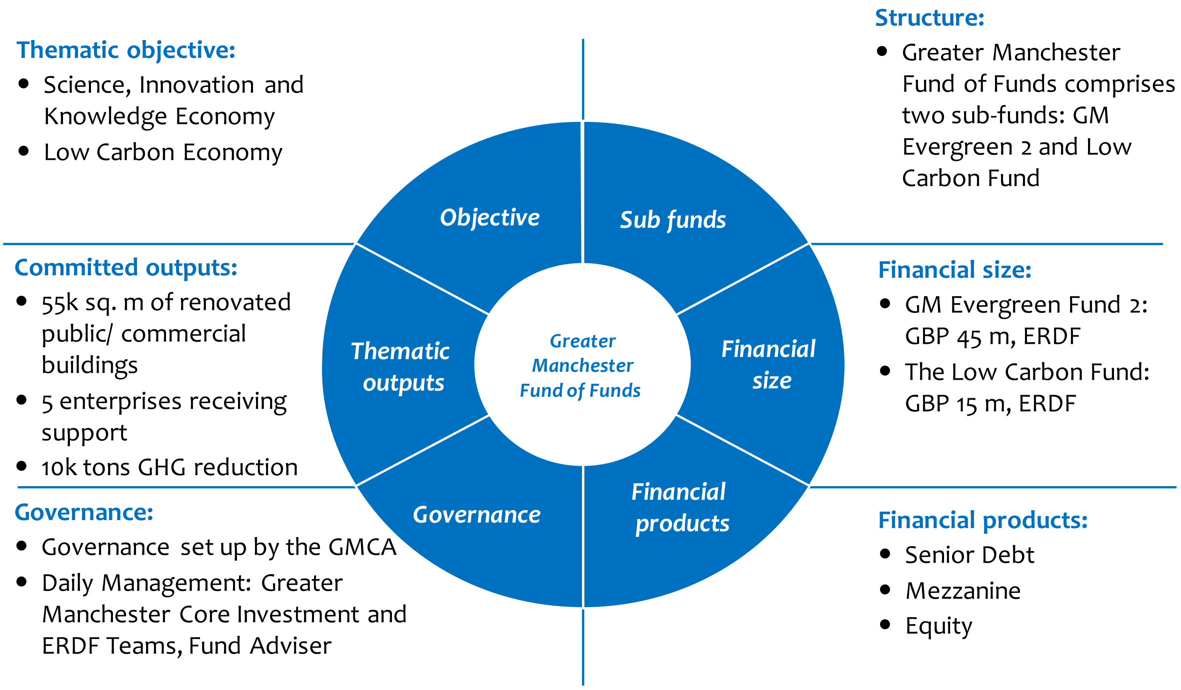
[1] http://www.northwestevergreenfund.co.uk/
[2] http://ec.europa.eu/regional_policy/en/funding/special-support-instruments/jessica/

2.2 The Greater Manchester Fund of Funds

The GM Fund of Funds was developed to utilise ERDF from the 2014-2020 programming period. The GMCA used its experience gained from the Evergreen 1 operation to develop the new fund to address both existing demand, which could not be met from Evergreen 1 alone and support new areas of operation, including Low Carbon projects. The GM Fund of Funds overall operation is made up of two 'sub-funds', known as the Evergreen Fund 2 and the Low Carbon Fund, responsible for the investment of an additional GBP 45 m and GBP 15 m of ERDF, respectively.

The GM Fund of Funds can be summarised in the figure below.

Figure 1: Summary of the Greater Manchester Fund of Funds



Following a competitive procurement process CBRE were appointed as independent Fund Manager of both Evergreen 2 and the continuation of Evergreen 1, which was included in the same tender process.

Furthermore, as part of the process to set up the Evergreen Fund 2, the GMCA established the GM Fund of Funds with separate governance arrangements to manage the overall financial instruments operation in Greater Manchester. Investment strategy – evolution to meet changing needs.

2.3 Investment sectors

The GM Fund of Funds focuses on the two main priority sectors: (i) science, technology and innovation and (ii) low-carbon infrastructure.

These strategic priorities can be further broken down into the investment priority axis divided between the two sub-funds of the GM Fund of Funds, i.e. the Evergreen 2 and Low Carbon Fund. The table below illustrates the ERDF allocation across the sub-funds and priority areas.

Table 1: Allocation of ERDF between the GM Fund of Funds sub-funds: Evergreen Fund 2 and Low Carbon Fund

Investment area	Evergreen Fund 2 (GBP m)	Low Carbon Fund (GBP m)
Science, Innovation and Knowledge Economy	30	N/A
Low Carbon	15	15
Total	45	15

Source: 'Greater Manchester Fund of Funds Investment Strategy', January 2017. Compilation by PwC.

As the Evergreen Fund 1 and the Evergreen Fund 2 coexist, in order to avoid any conflict of interests, investments eligible under the 2014-2020 operational programme are prioritised for the Evergreen Fund 2. Investments that are not aligned to the priorities of Evergreen Fund 2 can be considered for Evergreen Fund 1. In addition, at present, only Evergreen Fund 1 may be invested outside the Greater Manchester. The GM Fund of Funds revises its investment strategy on annual basis, with purpose of aligning it to the market conditions and strategic priorities.

2.4 Size of the Fund

The GM Fund of Funds manages GBP 60 m of ERDF funding, the provisional allocation of which is divided among the Evergreen Fund 2 (GBP 45 m) and Low Carbon Fund (GBP 15 m) as well as up to GBP 65 million of potential reflow capital from Evergreen 1. However, the Evergreen 2 resources are subject to reallocation between the sub-funds depending on their performance. Both sub-funds are required to attract the match funding, which can be secured both on the project, as well as the sub-fund level, depending on the source of the additional financing. Match funding is expected at project level for private sector projects and will be 50/50. The GMCA's public sector contribution at fund/sub-fund level is also at 50/50 alongside ERDF. The table below summarises information on assumptions of expected leverage as outlined in the GM Fund of Fund Strategy.

Table 2: Provisions for securing match funding

The match funding provided by:	Leverage measured at the project/sub-fund level	Expected leverage
Public sector	At the fund/ sub-fund level	Capped at 50 per cent alongside ERDF of the eligible project costs
Private sector	At the project level	Capped at 50 per cent of total costs

Source: 'Greater Manchester Fund of Funds Investment Strategy', January 2017. Compilation by PwC.

2.5 Financial products

The experience of the Evergreen Fund 1 indicates that **90 per cent** of financing has been provided by the means of **senior debt**, while the remaining **10 per cent** through **subordinated debt.**

Similarly to the Evergreen Fund 1, the Evergreen Fund 2 provides debt products including **senior debt** and **subordinated debt.** The tenor of the individual loan should not exceed a period of 5 years.

After this time, projects should complete their development phase and refinance its costs using loans from commercial banks.

The majority of the loans are paid on the monthly basis and are aligned to the construction costs incurred by the recipients. This approach provides assurance that the asset against which the investment is secured increases in value as the loan decreases.

Table 3: Characteristics of the GM Fund of Fund financial products

	Evergreen Fund 2	Low Carbon Fund
Financial products	Senior debt, subordinated debt, equity (subject to additional approval)	
Tenor of loans	5 years	15 years
Investment range	Varies from GBP 2 to 12.5 m	Under development
Conditions of debt lending	Aligned to commercial terms based on the profile of the borrower, paid on the monthly basis and aligned to the construction costs incurred by the recipients	

Source: Based on information provided by the Fund Manager.

2.6 Investment period and lifespan of the Fund of funds

The lifespan of the GM Fund of Funds is indefinite, with the minimum lifespan until 2031. This is in order to ensure the redeployment of recycled funding for the eight years after the end of the eligibility period. The majority of requirements will not be applicable to the recycled capital and accordingly, such funds will be available for the broader scope of investments, as long as they are aligned to the strategic priorities of Greater Manchester.

The initial investment period of the Evergreen Fund 2 the 7 years to December 2023 compared to five years under the Evergreen Fund 1. The Low Carbon Fund has the initial investment period of 7 years. The investment period can be extended, subject to the agreement of the Investment Board and the relevant output targets defined by the GM Fund of Funds. The investment period of both sub-funds relates to the capital deployment in accordance with the parameters of 2014-2020 programming period, as well as subsequent recycling.

Table 4: Targeted outputs to be achieved by the Evergreen Fund 1 and the Low Carbon Fund

Promoting Research and Innovation	Supporting shift towards low carbon economy	
Public/commercial buildings renovated	**Number of enterprises receiving support**	**Estimated GHG reduction**
55,000 sq. m floor space	*5 enterprises*	*10,000 tons*

3 Building an ecosystem of investors

During the implementation of the Evergreen 1 operation, the City of Manchester and its GMCA, partners engaged with a diversified group of investors and project promoters during the process of project pipeline development. Potential promoters including private sector property developers, property equity funds and public private partnerships were all identified. Similarly, the fund engaged with private sector banks and the wider development community to raise awareness of the fund.

The experience of the Evergreen Limited Partners authorities with the Evergreen Fund 1 demonstrates the strategic importance of developing a network of promoters and investors with the right motivation and capacity to become involved in the Fund and the projects it supports. For example, when the fund was first launched, third party investors had left the market, due to the global financial crisis. As a result, the initial projects were led by property development companies who had access to significant amounts of equity.

The experience of the Greater Manchester authorities shows that a flexible offer that reflects the current financing needs is a critical driver to support important investment opportunities that are strategic for the city. The investment strategy of Evergreen 1 was flexible enough to adapt to the changing demands of projects, allowing the Fund Manager to develop a variety or structured finance solutions including mezzanine products to support larger schemes as the market (and availability of senior debt) recovered in the city.

Following the successful experience of the city with the revolving instruments, the GMCA has built on the knowledge and practice gained with the single fund by embracing a more complex Fund of Funds structure. This is a direct response to the city's financing needs and existing funding gap.

Reinvestment after the end of the programming period addresses earlier constraints present at the fund level. Upon its termination, the fund can become more flexible in terms of products, terms and investment areas. The thematic areas of the investments can go beyond the scope of the Thematic Objectives and focus solely on the strategic objectives of the city.

The deployment of the ERDF financing in the fund is directly linked with the investment areas supported by the current programming period. For example, urban development, an investment area for the Evergreen Fund 1 was included in Thematic Objectives of the 2007-2013 programming period. Upon the termination of the programming period, the fund could reinvest its capital, including the interest earned, with more flexibility.

3.1 Project pipeline

The table below shows examples of some of the projects committed/financed by Evergreen Fund 1 and 2 (the project pipeline of Low Carbon Fund is under development).

Table 5: Example of projects in Evergreen Fund I and Evergreen Fund II Project Pipeline

	Purpose	Loan size [GBP m]	Fund
Project 1	Restoration and development of biomedical research centre	22.2	Evergreen Fund 1 and

			Evergreen Fund 2 (Research & Innovation)
Project 2	Commercial development at the Siemens Campus area in South Manchester	2.0	Evergreen Fund 2 (Research & Innovation)
Project 3	Construction of the industrial road to facilitate development of logistics and distribution hub	9.6	Evergreen Fund 1
Project 4	Development of 377,600 sq. ft of office and retail space to regenerate the Chester area	4.8	Evergreen Fund 1
Project 6	Redevelopment of former factory into 235,512 sq. ft business floor space	5.7	Evergreen Fund 2 Carbon Efficiency
Project 7	Development of the media city and 56,000 sq. ft of creative office space	6.25	Evergreen Fund 1
Project 8	Urban regeneration scheme in the city's business district resulting in creation of 13,660 sq. m of office space	10.9	Evergreen Fund 1
Project 9	Construction of science park, home to the city's innovation programme with 55,000 sq. ft office and conferencing space	4.5	Evergreen Fund 2 (Research and Innovation)

4 Sale of portfolio of loans

4.1 Background

In 2014, after the Evergreen 1 fund was fully committed, the fund was seeking to identify additional resources to allow it to continue to meet the demand for finance from its pipeline of projects. The Evergreen Fund 2 was in development but not expected to become operational until 2016 and therefore, unless other funding could be found there was a risk of a damaging hiatus in the fund's lending operations. As well as the impact on future projects (which would not proceed without funding), a period of dormancy would have also damaged the fund reputationally and put at risk the future success of Evergreen 2.

In order to address this issue, the Fund Manager, CBRE, proposed the possibility of a sale of part of the loan portfolio. Under the proposal, a portfolio of four loans would be offered for sale where the purchaser would acquire the loans, with the rights to receive interest and repayment of the capital in return for a capital sum representing the value of the portfolio being transferred.

The sales transaction of part of the fund's portfolio of loans **accelerated the Evergreen Fund 1's reflows, unlocked its liquidity and enabled reinvestment of the funds, thus increasing its impact** in targeted sectors**.** It allowed to avoid any gap in the offering of funding, which is key to promote the continuous creation of investment opportunities.

4.2 The role of the Greater Manchester Pension Fund

One of the key factors that enabled the successful sale of the loans was the **existence of a trusted partner**, the GMPF. The GMPF had been a member of the Evergreen 1 steering group that had been established to support the creation of the fund prior to the formation of the Limited Partnership. The GMPF provides pension schemes for employees of the Greater Manchester local authorities and other related public sector organisations. The GMPF is a trusted partner, with a commitment to the local area, as well as with the capacity and motivation to become involved in the fund.

The involvement of GMPF is specific to the circumstances present in Greater Manchester. In a different urban context, national promotional banks could potentially be partners in a similar way. The capital market investors have been excluded from the group of the potential lenders due to the much shorter investment horizon, as well as more aggressive investment profile.

4.3 The loan portfolio

A portfolio of selected loans represented the equivalent of **approximately fifty per cent of the fund's loan book.** The portfolio was made up **of four real estate loans worth over GBP 30 million** and included a range of different investments both inside and outside the Greater Manchester.

In order to facilitate the loan selling transactions a set of specific conditions needed to be met:

Balanced portfolio of projects: the loans were sold only if the projects were substantially underway. This way, **their risk profiles have been reduced**, while at the same time the required return has been achieved.

Borrowers' consent: the sale of loans was consulted with the borrowers who gave their agreement to proceed with the sale of loans. This step has protected the Fund Manager from adverse reputational costs.

Due diligence: before proceeding with the sale of loans, due diligence on the financial conditions of the transaction and the state of the investments have been undertaken and documented to increase the confidence of the buyer.

The **loan selling was beneficial for all parties** involved in the transactions. The GMPF took on substantially developed investments, which met their desired rate of return on capital invested, the Evergreen Fund 1 unlocked its liquidity, while the borrowers continued to receive the financing, despite having exceeded the initial development phase period.

Following the sale of the loans in 2016, all of the projects within the portfolio of the loan sale have been completed. It is understood that GMPF were subsequently able to extend further support to a number of the projects through the greater range of financing products that they offer, to the benefit of both developer and investor alike.

Portfolio of loans:

1. *'Tomorrow', a 54,000 sq. ft office and 112-bedroom hotel at MediaCityUK, developed by Peel Media;*
2. *'No1 Spinningfields', the 260,000 sq. ft office under construction by Allied London in Manchester;*
3. *1 City Place, 'Muse Developments' completed 70,000 sq ft office in Chester;*
4. *'Nikal and Abstract Securities' 400,000 sq. ft Soapworks in Salford Quays.*

The sale of the loans provides a potentially attractive model for securing investment into urban development projects from public and private lenders. In many cases, the initial risk profile of urban development projects is too high for the other investors to be accepted. However, after the first years, when the projects have advanced and the **development risk** (together with other risks such as the bankruptcy of the developer) **have been reduced**, investments into these projects become more attractive for investors, who would not have invested in the projects at inception.

It is important to highlight that borrowers were consulted and agreed to the operation. Moreover, **the terms and conditions of the loans for the final recipients remained unchanged**, with an exception (by agreement between borrower and new lender) of the tenor of loan and transferring the repayment directly to the GM Pension Fund, under the same terms as agreed with the Evergreen Fund 1. Finally, the GMPF also agreed that CBRE would continue to manage the loans and maintain the relationship with the borrower. All these measures minimised the impact on the borrowers, as well as provided a complete implementation solution for the investors.

5 Conclusions

5.1 What and how can be replicable from this model of the city fund?

The experience of the Greater Manchester authorities has a number of lessons that can apply in other cities in Europe. The **appointment of the Independent Fund Manager** was crucial to the success of the fund. By developing a strong partnership with the private sector fund manager, the cities were able to harness the market know-how and best practice within the fund manager to help achieve the objectives of the operation.

The importance of this collaboration can be seen in the further development of the relationship in the context of Evergreen 2. In this second fund, the city expanded the scope of the investment strategy to include low carbon projects. Following a competitive selection process, the same fund manager was appointed to manage this fund. This suggests that cities looking to broaden financial instruments into new sectors may benefit from existing relationships with its fund managers.

A close collaboration between the city development team and the independent Fund Manager is a critical driver to successfully implement the city strategy.

The evolving needs of the city was supported by the development of the Evergreen Fund 1 as a **flexible instrument** that addressed the needs of the projects and the market gap. The strategy undertaken by the city enabled to follow the investment opportunities in sustainable urban development.

One of the key success factors of Evergreen Fund 1 was **development of the ecosystem of strategic investors**. The fund benefited from existing strong relationships between the city's regeneration unit and the property development community in the city. This helped identify early win projects and open doors for the fund to potential investment opportunities. At the same time, the independent fund manager brought its own knowledge and experience in the market to allow the fund to develop a prominent position in the market.

As awareness of the fund's potential to support strategically important projects grew, property development companies were more prepared to commit resources to develop **investment-ready propositions** to be submitted to the Evergreen Fund Manager for investment. The pace of this virtuous cycle of investment increased as successful projects were delivered, further driving demand for Evergreen's products and, importantly investment in the city-region.

Investment-ready projects become attractive for private sector investors and can be co-financed by private capital at the project level.

As demand grew for the fund's products the fund's board and Fund Manager began to explore possibilities to mobilise further investment. The city had been working with the GMPF from the beginning of the project, with a member of the GMPF executive team being a member of the Evergreen 1 steering group since the creation of the fund. This existing relationship allowed the development of the proposal for the GMPF to **acquire part of the loan book from the fund**. This transaction provided the fund with additional liquidity, to allow it to support further projects, whilst the GMPF benefited from the revenue generated by the loans it acquired, many of which subsequently sought to negotiate the extension of the repayment period financing for further phases, to the benefit of the GMPF.

Finally, the experience of Evergreen 1 has paved the way for the Evergreen 2 funds which is currently operational. These funds are now all managed within a single Fund of Funds structure which is managed by the Greater Manchester Combined Authority and its **specialist core investment team**. In addition to supporting the Evergreen 1 and 2 funds, the core investment team has also developed further non-ERDF funds to support housing, science and other priority sectors. This further highlights how the development of ERDF financial instruments can help build capacity within cities to mobilise investment to support sustainable investment in the city over the long term.

Loan selling transactions support capacity building and development of the urban development fund.