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FINANCE, COMPETITIVENESS & INNOVATION INSIGHT | LONG-TERM FINANCE

Leveraging Pension Fund Investment for Domestic Development: Namibia's Regulation 29 Approach

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ABBREVIATIONS AND ACRONYMS

DCP	Development Capital Portfolio
GDP	Gross Domestic Product
GEPF	Government Employees Pension Fund (South Africa)
DFI	Development Finance Institution
ESG	Environmental, Social and Governance (issues)
FCI	Finance, Competitiveness and Innovation (Global Practice, World Bank)
GIPF	Government Institution Pension Fund (Namibia)
GNI	Gross National Income
GP	General Partner
IMF	International Monetary Fund
IM	Investment Manager
JSE	Johannesburg Stock Exchange
LP	Limited Partner
NAD	Namibian Dollar
NAMFISA	Namibia Financial Institutions Supervisory Authority
NSX	Namibian Stock Exchange
PE	Private Equity
PDN	Previously Disadvantaged Namibians
RFP	Request for Proposals
SADC	South African Development Community
SME	Small and Medium Enterprises
SPV	*Special Purpose Vehicles*
UIM	Unlisted Asset Managers
USD	United States Dollar
VC	Venture Capital

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EXECUTIVE SUMMARY

The note describes Namibia's approach to mandating investment of a percentage of the large pool of local institutional capital to support domestic economic development via investing in alternative financing vehicles within the context of an underdeveloped capital market.[1] The note describes the investment vehicles and regulatory structure established by the national regulator - Namibia Financial Institutions Supervisory Authority (NAMFISA), summarizes lessons learnt and considers whether such structures could be applied in countries with similar market and economic contexts.

The country initially tried to encourage more domestic investment via a direct investment approach into development projects by the large local government pension fund- Government Institution Pension Fund (GIPF)- through its Development Capital Portfolio (DCP). This portfolio that was managed over the period 1996-2010 failed largely due to governance challenges. Following poor experience with direct investing, NAMFISA devised Regulation 29 to provide a governance framework to allow for local direct investment via regulated vehicles. All local pension funds, including GIPF, were required to invest a small percentage of their funds via these vehicles.

In addressing identified national issues, NAMFISA's approach diverged from international practice in several important aspects. More specifically, NAMFISA instituted mandatory requirements that all pension (and insurance) funds invest in unlisted Namibian companies, formalized the unlisted investment market and created specialized intermediaries (UIMs), and introduced high level of regulatory oversight for both investment managers (UIMs) and investment vehicles (SPVs).

While more time is needed to fully evaluate the impact of Regulation 29 on returns of the pension funds and on domestic and capital market development, early results demonstrate that Regulation 29 and new market structure contributed meaningfully to addressing issues related to the governance of and within pension funds, improving the due diligence of unlisted investments, the investment process, active management and reducing the perception of corruption.

While still in its infancy, the Namibian private equity industry now comprises 22 unlisted investment managers[2] (UIMs) and 11 special purpose vehicle (SPV) structures, most of which are operational. Investment in unlisted companies has been increasing as has committed capital to unlisted companies, as more pension funds enter into agreements with SPVs. As of December 31, 2018, investments in unlisted companies stood at NAD 1.3 billion, an increase of nearly 50 percent from NAD 871 million a year earlier. Committed capital increased by 27 percent to NAD 3.3 billion from NAD 2.6 billion on a year-on-year basis.

In its role as the largest pension fund in Namibia, GIPF has become a key driver of the private equity market in Namibia. Over the long-term the expectation is that these developments could further create opportunities for foreign financial institutions, and other potential investors, to co-invest in Namibia through established structures, alongside with GIPF.

While prescribing assets is not in line with international good practice, such as OECD Core Principles of Private Pension Regulation, and similar approached have not led to successful outcomes in other countries in the region, early observations from Namibian experience suggests ways of managing the risks of requiring domestic investment. In particular:

- Limiting the prescription to the small percentage of total assets allowed for direct investments to be accommodated within pensions funds' overall financial return targets to meet their fiduciary obligations to their members;

- Introduction of secure investment vehicles to channel investment flows to projects with social-economic objectives provided governance and financial structures to mitigate endemic issues with direct investments within the challenging governance context;
- Ongoing development of a robust system to measure development impacts to monitor the investments has been and will be critical to demonstrate benefits to members and maintain credibility within the broader community.

Lessons can also be learnt from the Namibia case on financial market instrument design and regulation. Namibia chose an SPV structure because it did not have the traditional GP/LP structure and ensured its professional management and an appropriate level of transparency. Namibia's started with the highest level of regulation by regulating both investment managers and their instruments, as compared to international market practice of regulating managers alone. The Namibia experience – along with practice in many countries - showed that the development of capital market more broadly and of alternative asset classes in particular is an evolutionary process. Specifically, investment structures should be flexible enough to fit local market circumstances and evolve over time as the local market develops and market participants become more experienced. Similarly, the level of regulation should evolve as the market develops and market participants get more skilled and experienced.

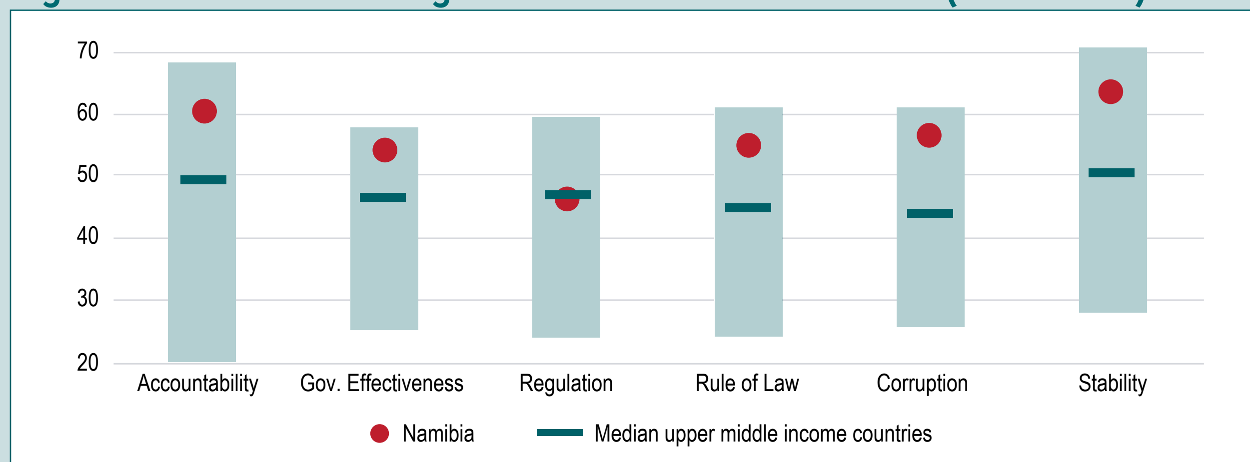
Finally, this approach to domestic investment to work certain enabling conditions need to be developed simultaneously with the regulatory reform. Firstly, in the absence of a pipeline of deals, financial sector reform alone will not be able to stimulate the country's economic development. Secondly, a sufficiently developed financial sector with financial institutions capable of assessing alternative investment opportunities and structuring these appropriately is required.

INTRODUCTION

Namibia has demonstrated remarkable progress in its economic and social development since becoming independent from South Africa in 1990. Since independence, Namibia's GNI per capita has grown quickly, and its success has been attributed to effective governance as the country used the earnings from its natural resources to modernize its physical capital, build human capital, and develop and strengthen its institutions. Please see Figure 1. Over this period Namibia has also shown remarkable signs of political stability and prudent macroeconomic management, helping the country achieve economic growth, social progress, and to reach upper middle-income status.[3] Based on the 2019 IMF article IV report, despite being a small and commodity-dependent economy exposed to external shocks[4], over the last two decades annual per capita GDP growth averaged 2.6 percent, resulting in better living standards and lower poverty, and this in one of most gender-equal countries in the world.[5]

Namibia is characterized by a complex and concentrated financial system that has generated a significant amount of savings from pensions and through other non-financial institutions. Namibia's financial system is dominated by four large and heterogenous financial conglomerates,[6] all with close ownership and funding links to South Africa. The non-bank financial sector is large, with assets around 262 percent of GDP, to a large extent reflecting the pre-funded GIPF. Investment managers (IMs) play an important role in integrating the financial system, linking institutional investors to financial markets and banks. They manage funds on behalf of pension schemes, insurance companies and unit trust products. The bulk of pension funds' assets are managed by IMs, with 37 percent of total assets invested through Namibian IMs and another 41 percent invested through IMs in South Africa and the rest of the world.[7] A snapshot of the Namibian financial sector is presented in Table 1.

Figure 1: Namibia's Strong Governance and Institutions (As of 2017)[8]



Sources: Worldwide Governance Indicators, D. Kaufman (Natural Resouorce Governance Institute and Brookings Institution) and A. Kravy (World Bank) 2017 and IMF staff calculations.

Note: Shaded areas ixclude top and bottom 10% of the distribution of upper middle income countries (sample size: 55 observations). Scores are rescaled to 0-100 range. The 90% confidence interval of the Control of Corruption Estimate for Namibia ranges from 52 to 61.

The Namibian pension system is typical of the South African Development Community (SADC)[9] region – consisting of a universal, non-contributory pension in the form of an Old Age Grant, and private, occupational schemes – and covers approximately 30 percent of the labor force (including GIPF). The Old Age Grant provides a monthly pension of NAD 1,200 to all Namibian citizens and permanent residents over the age of 60 and is funded from government revenues (currently costing around 1.5 percent of GDP). The civil service pension schemes in the SADC region are unusual in that they are typically fully funded, as is illustrated in Figure 2. The GIPF is a fully funded defined benefit scheme and the 2015 actuarial assessment showed the scheme as being 108 percent funded. Private sector employers offer occupational pensions on a voluntary basis predominately through defined contribution schemes in a fragmented market. GIPF is the only Defined Benefit fund in the country and other pension funds are Defined Contribution funds. There is also a number of South African funds which are registered as foreign schemes having Namibian members.

Figure 2. Funding Status of Civil Service Schemes Globally[10]

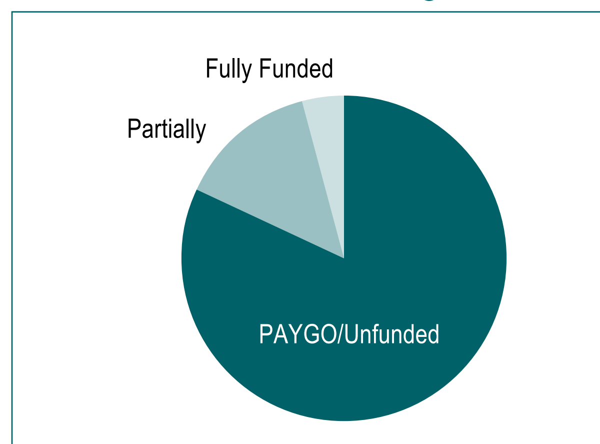


Table 1. Structure of the Namibian Financial Sector[11]

	End-2010		End-2016		
	Percent of Total Assets	Percent of GDP	Percent of Total Assets	Percent of GDP	USD Million
Banks	20	58	22	75	**8,016**
NBFIs	**80**	**233**	76	265	28,004
Insurance Companies	11	31	10	34	3,666
Life insurers	10	29	9	30	3,259
Non-life Insureres	1	3	1	4	407
Insurance Companies	25	72	26	91	9,693
o/w: GIPF			18	64	6,840
Medical aid	0	1	0	1	99
Unit trusts/money market funds	10	29	9	32	3,479
Asset managers	33	98	29	100	10,757
Microlenders	0	1	1	3	310
State-owned financial institutions	**n/a**	n/a	2	8	868
Total	**100**	291	100	344	36,888

At independence Namibia inherited significant pension assets that have continued to accumulate. Highly unusually for developing countries, Namibia's high level of contractual savings of over 50 percent of GDP at the time of independence put it in the category of highest saving countries alongside the Netherlands and Singapore.[12] Over the last two decades Namibia's pension assets grew from 53 percent of GDP in 1996 to about 90 percent of GDP currently.[13] By 2018 Namibia's pension assets reached nearly USD 10 billion across 138 active pension funds comprising about 26% of the national financial system's asset base.[14] At nearly USD 7 billion, GIPF is one of the largest pension funds on the African continent second only to South Africa's Government Employees Pension Fund (GEPF) based on the size of its assets, as well as by far the largest globally across emerging markets in terms of its size in relation to a country's GDP, as is illustrated by Figure 3.

In the decade post independence, Namibia continued to generate substantial savings from pension and life insurance funds, but contrary to policy makers' expectations, savings' growth did not translate into higher levels of domestic investment and economic growth. Post-independence, Namibia pursued four main development objectives: (1) revive and sustain economic growth; (2) create employment; (3) reduce inequalities in income distribution; and (4) reduce poverty. However, during the first decade of independence GDP growth averaged about 3 percent per annum-—far less than the average 5 percent projected under the National Development Plan and 7 percent envisaged in the Vision 2030.[15] This was predominantly due to large capital outflows. A review of the reasons for the capital outflow showed that offshore investments by pension funds and insurance companies constituted a major component of the outflows from the economy.[16]

As Namibian capital markets were illiquid and lacking in the number and types of available instruments in both the stock exchange and bonds markets,[17] Namibian institutional investors were pushed to seek investments outside of Namibia. The Namibian Stock Exchange (NSX) has been dominated since independence by dual listed companies with a primary listing on the Johannesburg Stock Exchange (JSE).[18] Domestic companies therefore are not the majority of listings. Furthermore, the size of Namibia's stock market was and is too small to absorb the large size of pension assets, as seen in Figure 4. Offshore markets, however, provide sufficient market depth and breadth to

Figure 3. Pension Fund Assets Relative to GDP (2018)[19]

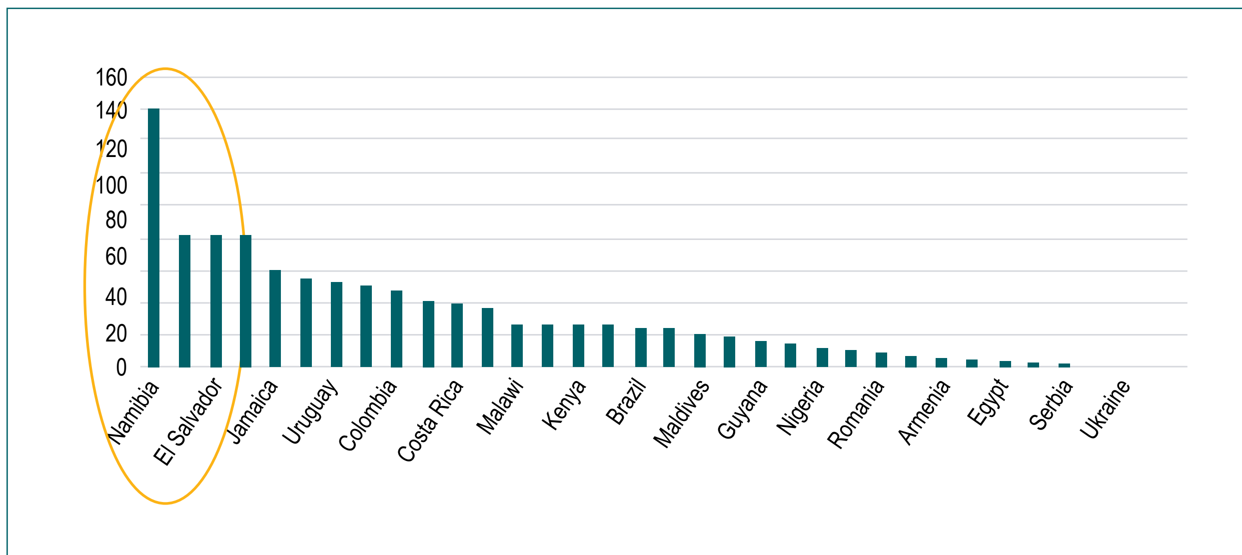
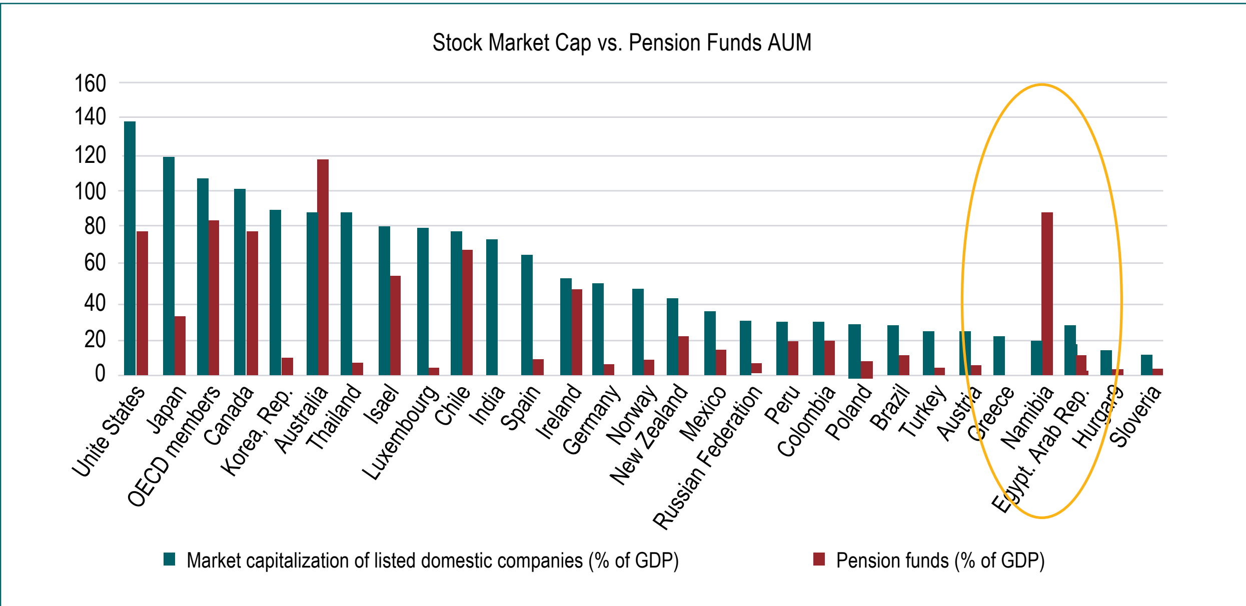


Figure 4. Global Stock Market Capitalization vs. Pension Fund Assets (2018)



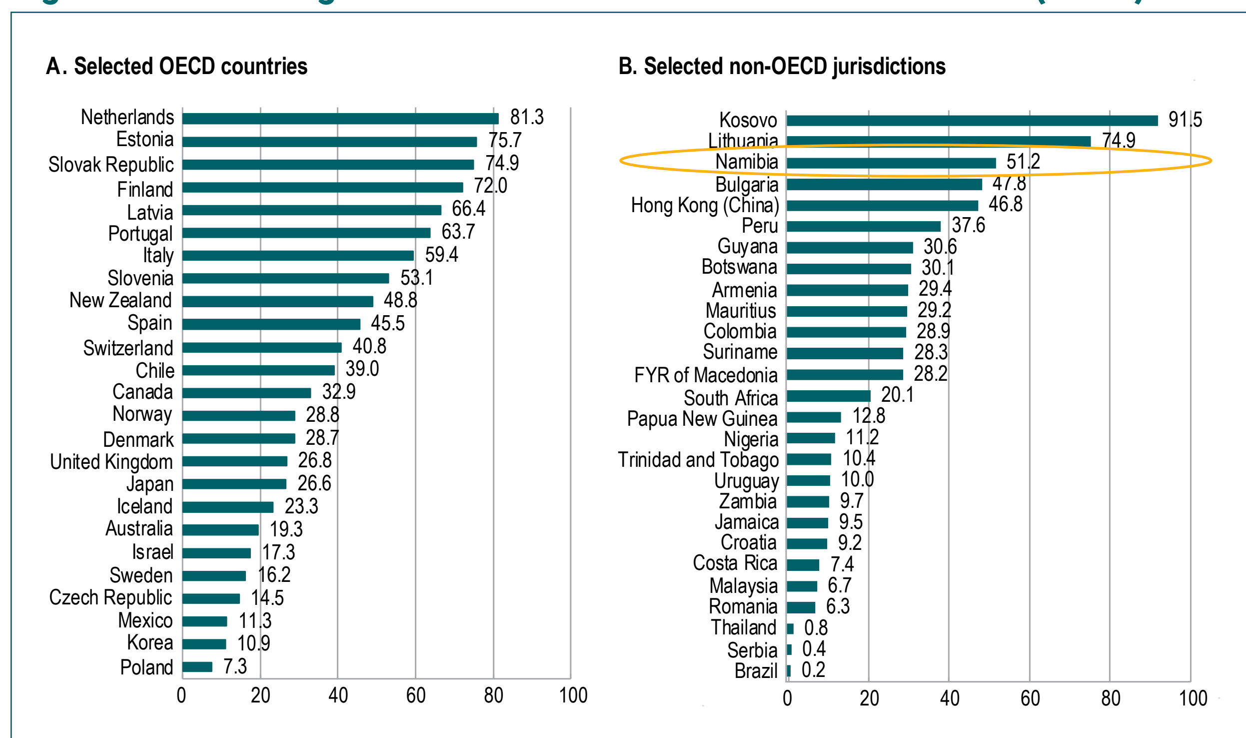
Source: World Bank and OECD Databases.

achieve institutional investment and diversification objectives, and for liquidity management. The level of offshore investment by Namibian institutions has been and is still higher than in most countries (not surprising, given the large size of the assets), supported by relatively liberal offshore investment regulation as reflected by the level of international diversification of Namibian pension funds across global markets, as seen in Figure 5.

Policy makers were concerned that Namibian capital was put to work in other countries, while Namibia only benefited from the investment returns on its assets. The challenge for Namibia was to utilize the abundant savings for productive investments in the country without compromising the returns on the invested savings. Recognizing that savings institutions play an important role in the development of a country's financial system, Namibian policy makers sought to develop a policy solution appropriate for Namibia's specific circumstances, as unrestricted foreign investment was seen as institutionalizing capital flight and preventing domestic markets from benefiting from long-term financial resources of Namibia's pension funds. Global experience has demonstrated that foreign investment limits are sometimes helpful for economies with undeveloped financial markets - by imposing stricter and more prescriptive rules on where and how much to invest, capital was required to invest more domestically.[20] The development of European countries' pension funds and capital markets illustrates that European pension assets not only served as a source of long-term savings to support the development of domestic bond and equity markets, but also as a catalyst for innovation, the privatization process and improvements in corporate governance. In turn, maturing capital markets offered European pension funds the opportunity for better portfolio returns and risk management.[21]

Regulation 28 that was introduced with the objective of retaining more savings within the economy to channel into domestic development required that at least 35 percent of pension fund assets be invested in Namibia. Regulation 28 governs the asset allocation of pension funds; details the jurisdictional limits (i.e. the minimum/ maximum investment in Namibia/elsewhere); prescribes the maximum exposure to a single asset class and; details the maximum exposure allow to an individual issuer and counterparty. All of the

Figure 5. Percentage Pension Fund Assets Invested Overseas (2016)[22]



Source: OECD.

limits were maximums except for the requirement of a minimum investment in Namibia and a minimum investment in unlisted investments and did not require mandatory investment.

Regulation 28 was considered partially successful, since a portion of pension savings was brought back onshore and invested in local bonds, equities and cash, and was credited with the development of the local asset management industry. However, the fact that asset managers invested more in the dual listed shares, i.e. foreign domiciled companies at the NSX, means that a large portion the domestic investment requirement effectively went to fund foreign domiciled companies. A review of the holdings in the early 2000s shows that only 10 percent of pension fund assets could be classified as truly Namibian assets if dual listed shares and cash placed on deposit at local commercial banks were excluded. The same study also found that less than 5 percent of the 35 percent Namibian portfolio consisted of local equity.[23]

REGULATORY PERSPECTIVE: NAMFISA'S TARGETED APPROACH TO DEVELOPING DOMESTIC PRIVATE MARKET

The first attempt of direct investing in Namibian companies was undertaken by GIPF through its Development Capital Portfolio (DCP), which was established in 1996. This occurred without a regulatory framework or supervision. GIPF's objectives were to promote socio-economic development and empowerment of Namibians through the financing of development projects and to assist previously disadvantaged Namibians to enter the mainstream of economic activity; whilst achieving investment returns. Due to the lack of domestic publicly listed companies, and the predominance of dual listed NSX companies, GIPF focused on unlisted companies.

The results of DCP fell short of expectation due to skills and capacity constraints, and lack of governance. GIPF allocated approximately NAD 661 million to the DCP which invested directly into various Namibian companies with little or no intermediation. By 2005 losses on DCP investment became public, several investigations were launched, and the portfolio was closed in 2010. According to the 2008's IMF report, DCP was forced to write off 84% of its investments at that point.[24] DCP's investment record based on portfolio holdings provided by GIPF to the World Bank, presented in Annex 2, is discussed in paragraph 20. The results of multiple investigations into DCP losses were not made public, which fueled wide-spread speculation that the losses were not only due to GIPF's lack of specialized expertise in managing unlisted investments, but also because of external interference in investment decisions. Subsequently, NAMFISA identified the following factors as key issues leading to underperformance: (1) lack of understanding of alternative assets, (2) poor governance of the investment process, (3) lack of due-diligence, (4) lack of active management of the underlying investments, (5) politically motivated investment decision making; and (6) probable corruption.[25]

NAMFISA, established in 2001 to regulate and supervise financial institutions in the financial services industry in the public interest, sought to address the key issues identified from the DCP experience. NAMFISA's policy response to the DCP failure was to: (1) develop a system to address the identified problems; (2) formalize and regulate the alternative asset market; and (3) where possible, address problems of illiquidity and valuation.[26]

Passed in 2014, Regulation 29 was the implementation framework for Regulation 28, which introduced unlisted investments as an asset class and made investments of pension funds in unlisted investments to enhance returns on their investments and diversify their portfolios mandatory.[27] Consistent with the objective of improving investment outcomes for pension funds over the long-term through improved investment opportunities, Regulation 29 targeted the deepening of financial markets, contributing to skills transfer, creating employment and addressing Namibia's social challenges. Through the introduction of Regulation 29, the Government's objectives were to: (1) increase domestic economic development by utilizing contractual savings; (2) enable domestic projects otherwise struggling to acquire funding; (3) bolster promising investment projects; (4) formalize the unlisted investment market and create specialized intermediaries, such as UIM; (5) develop a supply of Namibian private companies that, once public, would contribute to the expansion of the domestic equity market (currently dominated by dual listed companies); and (6) provide a framework for the regulatory authority to regulate these activities.

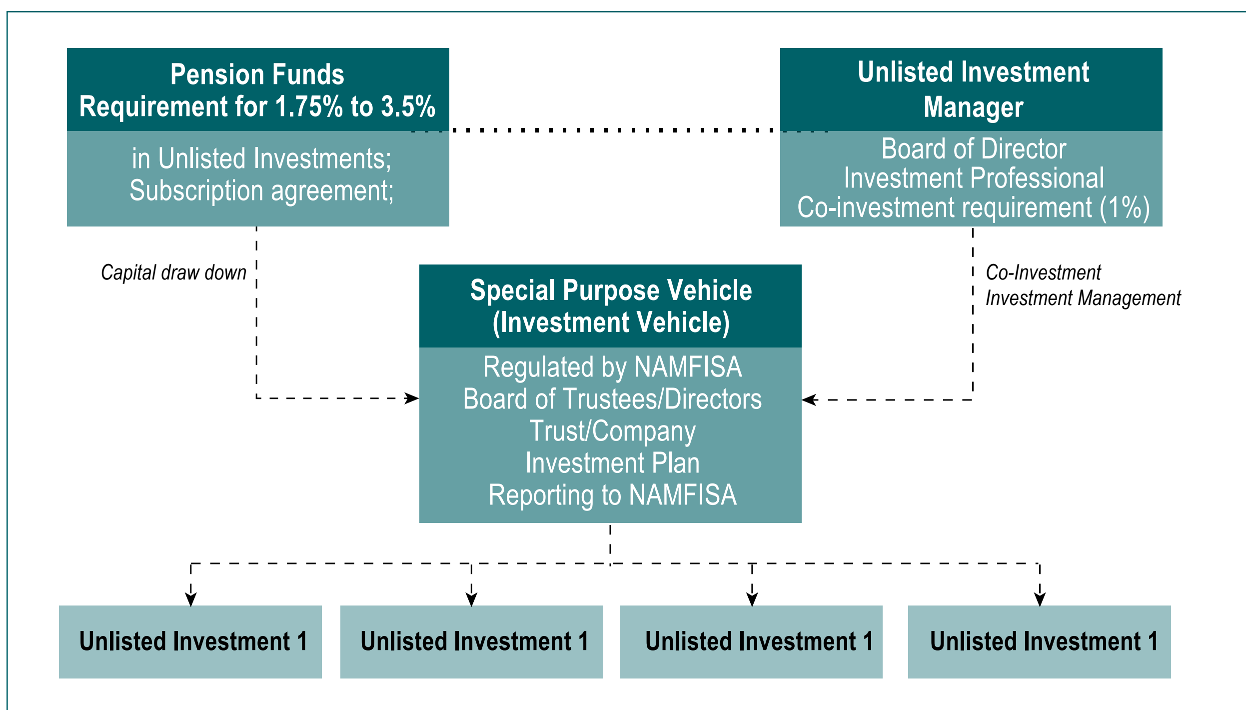
Furthermore, Regulation 29 introduced how pension funds should invest in unlisted investments. Regulation 29 established the compulsory allocation to unlisted assets with a minimum of 1.75% and a maximum of 3.5% of

AUM, and was passed to, among other issues, address governance, transparency and technical skills in creating domestic instruments. Regulation 29 stipulated that pension funds must invest in unlisted investments through an SPV, prohibiting pension funds from directly investing in UIM. An SPV must be either a public or private company (under the Companies Act 2004) or a Trust. It must meet several further conditions, including having its investment plan and directors approved by NAMFISA, and may issue debt. An SPV must enter into a Management Agreement with a regulated UIM. To establish independence in investment decision making, the regulation provided that UIMs could not be a trustee or a principal officer of a pension fund. To have "skin in the game" the regulation also required UIMs to co-invest a minimum of 1% of the contributed capital with investors in any SPV. SPVs are required to report to NAMFISA every six months on a range of issues including valuations for new portfolio investments and submit audited financial statements within 180 days after the end of its financial year according to IFRS. Diagram 1 illustrates the salient features of Regulation 29 and Annex 1 provides further details.

Overall, NAMFISA recognizes the positive impact of Regulation 29 in catalyzing the nascent private investment industry. As there have been no exits from unlisted investments to date and given the long-term nature of unlisted investments,[28] it will be some time before investment results can be quantified to assess the impact of Regulation 29 on pension fund investment returns specifically, and on the Namibian private equity industry more broadly. Still, in the view of NAMFISA the new regulatory environment and new market structure contributed meaningfully to addressing issues related to the governance of and within pension funds, improving the due diligence of unlisted investments, the investment process, active management and reducing the perception of corruption.

Investment in unlisted companies has been increasing as has committed capital to unlisted companies, as more pension funds have been

Diagram 1. Regulation 29 for Unlisted Investments by Namibia's Pension Funds[29]



entering into agreements with SPVs. Since Regulation 29 was introduced, based on semiannual reports by the pension funds to NAMFISA, as of December 31, 2018 investments in unlisted companies stood at NAD 1.3 billion, an increase of 49.3 percent from NAD 871.0 million as at 31 December 2017. Committed capital increased by 27 percent to NAD 3.3 billion from NAD 2.6 billion on a year-on-year basis. As presented in Figure 6 and Table 2, as of 31 December 2018 the manufacturing sector accounted for about 29 percent (NAD 381 million) of the total investments in unlisted assets, which is 38 percent higher than during the previous period (NAD 277 million). The manufacturing sector is followed by the renewable energy sector which accounts for about 11 percent (NAD 144 million). There has been an increase in investments in the renewable energy sector from about NAD 75 million as reported for the period ending December 2017 to NAD 144 million; a significant increase of nearly 93 percent. The financial services and property sectors both accounted for 6.5 percent (NAD 86 million) of the total investments in unlisted assets. Nearly eighty three percent of the total assets invested in unlisted portfolio companies was invested in equities and 17 percent was invested in debt instruments. As at 31 December 2018, the portfolio companies, in which the SPVs invested, employed a total of 4,262 employees—up by almost 9 percent from 3,920 employees from a year earlier. The manufacturing and health services sectors employed the highest numbers of employees, about 1,016 (24 percent) and 780 (18 percent) respectively, of the total employees of the invested portfolio companies.

Still, NAMFISA acknowledges that there have been some challenges with the application of some Regulation 29 provisions and has been engaging with market participants to review and address them. The current features of Regulation 29 were designed in response to specific challenges in the Namibian market, most notably the mandatory nature of the pension funds' investment in private investment and the controversial legacy of the GIPF DCP. However, specific aspects of the regulation are seen by the industry as too onerous and/or rigid, while other aspects don't function as they were intended. While overcoming most of the challenges cited by Namibian UIMs would bring Regulation 29 closer in line with global experience of private markets (most of whom regulate alternative investments on a voluntary basis, as discussed in Box 1), NAMFISA's objectives were to address challenges unique to Namibian context:

Figure 6. Unlisted Investments per Sector (December 31, 2018)

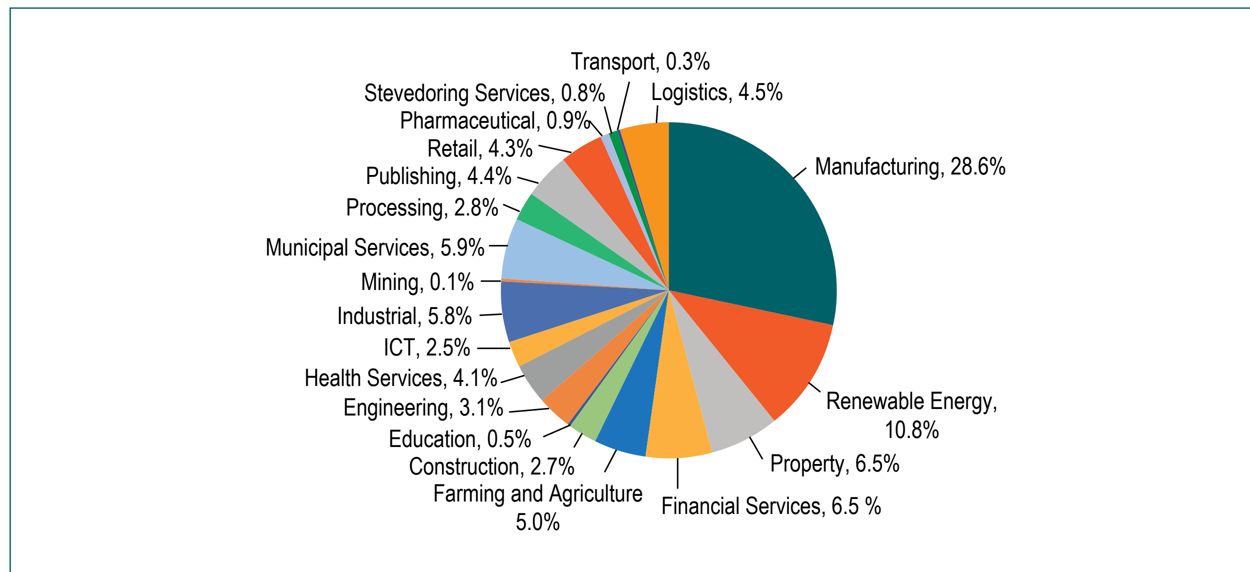


Table 2. Unlisted Investments per Sector (December 2017-December 2018)

	Unvestments in unlisted, %		Investments in unlisted, N$ mill	
Sector, % of total	2007	2018	2017	2018
Manufacturing	34.8%	28.6%	303	372
Renewable Energy	8.6%	10.8%	75	140
Financial Services	5.7%	6.5%	50	85
Property	8.6%	6.5%	75	85
Municipal Services	0.6%	5.9%	5	77
Industrials	7.4%	5.8%	64	75
Farming and Agriculture	0.3%	5.0%	3	65
Logistics	-	4.5%	-	59
Publishing	6.7%	4.4%	58	57
Retail Services	5.5%	4.3%	48	56
Health Services	5.5%	4.1%	48	53
Engineering	2.0%	3.1%	17	40
Processing	-	2.8%	-	36
Construction	3.9%	2.7%	34	35
Information Technology Solutions	1.4%	2.5%	12	33
Pharmaceutial	1.1%	0.9%	10	12
Stevedoring	0.2%	0.8%	2	10
Education	0.8%	0.5%	7	7
Transportation	0.9%	0.3%	8	4
Mining	4.6%	0.1%	40	1
Trolley Service	1.4%	-%	12	-
Total Investments	**100%**	**100%**	**871**	**1,301**

- **Regulation 29's commitment period is 2 years, while the global practice is 5 years.** Regulation 29 specifies that an SPV must enter into a subscription agreement with an investor that specifies the total committed capital of the investor to the SPV; and the period within which the SPV has the right to drawdown the committed capital. However, if the drawdown is not effected within a period of 24 months, the capital commitment lapses, unless the SPV and the pension fund agree upon an extension of the drawdown period, and such extension has been approved by the regulator. The regulator must deregister a SPV, if it fails to invest in unlisted investments within 24 months from the date of registration unless extended by the Registrar upon application not later than 3 months before the end of the 24 months period. If the UIM is not fully invested by the end of the period, it is required to return the money to the investor(s). The reality of unlisted investments more generally and due to the nascent nature of the

unlisted industry in Namibia more specifically, is that it takes much longer than 2 years to find, asses and execute investments, especially if it requires both a commercial return and economic and social impact. NAMFISA's motivation for limiting the commitment period to 2-years was to avoid Regulation 29 being circumvented by making capital allocations, but not drawing on them and was based on NAMFISA's anticipation of pension funds' "reluctance" to comply with new requirements of Regulation 29.

- **Mandatory 1.75 percent to 3.5 percent investment band is seen as too narrow for the Namibian market and is inconsistent with an upper limit of 10% in countries where such**

Box 1. Challenges for SME Financing by Pension Funds in Emerging Markets[30]

As demonstrated by the experience of advanced economies, there is potential for institutional investors more generally and for pension funds specifically in emerging markets to play a stronger role in SME financing, but a few challenges would need to be overcome. Pension funds have a long-term investment horizon and therefore could supply a crucial additional source of patient capital to help SMEs flourish. Nevertheless, in many emerging markets they face regulatory challenges and more structural issues related to the nature of the underlying assets that need to be addressed. Some of these issues that are relevant to Namibia are discussed below.

In most emerging markets the regulatory framework has largely remained rules-based, with quantitative limits placed on investments by pension funds and insurance companies, while advanced economies have applied the "prudent person" standard to institutional investments. This contributes to a lack of flexibility in asset allocation across various asset classes, and typically favors large allocations to government securities and listed corporate securities. Furthermore, in many emerging markets the framework does not allow investment in alternative assets or the limits are too low to provide meaningful flow to develop this asset class.

Limited capacity to assess and monitor alternative assets also contributes to the low levels of pension investment in alternative SME-related investments, even where regulatory restrictions have been relaxed. In Kenya, for example, pension funds were permitted to invest up to 10 percent of assets in private equity and venture capital in 2015; however, to date, actual allocation to PE/VC has remained low predominately as a result of the lack of intermediation. Although other issues are at play, such as the structure of the pension system overall, a lack of internal capacity and knowledge of alternative instruments within Kenyan pension funds have remained a key barrier to investment in SMEs. To remedy this, in Nigeria local pension funds are permitted to invest in private equity only where Development Finance Institutions (DFIs) are among the Limited Partners (LPs) in order to allow for the transfer of knowledge and skills.

Even in cases where regulations or capacity are not a challenge, scale might be. This is a challenge for institutional investors in both advanced and emerging economies. In general, pension funds have a sizable amount of assets under management and, thus require their investments to be a certain size to make an impact in their profitability. In contrast SME related assets are usually small and yet require a similar effort to prepare, execute and monitor than more sizable investments. As a result, institutional investors choose not to invest in them. This challenge could be mitigated by choosing an indirect route of investment; i.e. by investing in funds, which in turn pool the SME assets. This is the way institutional investors have invested in PE/VC and are investing now in minibonds and SME loans in advanced economies.

limit is spelled out. The band for investment is seen as too narrow given the landscape of unlisted investments and of the pension fund industry in Namibia. Once the pension funds are invested, it could be challenging for funds to stay within the upper limit of the investment band due to the illiquid nature of these investments and challenges with their regular valuations. Indeed, allocation to unlisted investments has been breaching the limit since 2016 (at 3.6% in 2016 and growing) according to NAMFISA. Thus, allowing for the value of investments to fluctuate up to, say, 5 percent will provide some breathing room for invested pension funds.

- **Regulation 29 requires that both UIMs and SPVs are registered and are subject to high regulatory oversight.** As presented in Box 2, this approach represents the highest level of regulation globally that differentiates treatment of investment managers and investment vehicles (funds, or SPVs in the case of Namibia) depending on specific objectives of the regulator. NAMFISA's objective to have both UIMs and SPVs be registered was to have an overview of the entire market and a clear understanding of the investment objects of each of the SPVs. The view of Namibian UIMs is that objective of the regulation should be to ensure that the UIMs are sound. Namibian managers managing public assets are not required to register each of the funds, or investment strategy, that they offer to investors. In the case of managers managing unlisted investments, i.e. UIMs as defined by the Regulation 29, each SPV serves as a unique investment strategy for the manager. UIMs shared that requirement that each SPV is registered and complies with the regulation's requirement, adds significant costs to the managers. More generally, market participants perceive that Regulation 29 created more excessive administration and compliance work beyond what would be practical to ensure consistency with NAMFISA's intentions.

- **Currently allowed investment structures (such as a Company or Trust) are limited compared to global practices.** Namibia does not currently have legislation for limited liability partnerships, thus the standard GP/LP structure is not possible. Resulting narrow range of investment instruments is seen by Namibian market participants as hampering further market development and could be considered within the broader legislative framework reform.

- **Regulation is silent on ESG issues, while integration of sustainability issues across financial industry globally is expected to become the norm.** While the unlisted investment industry is still in the early stages of development, there is scope to include ESG issues into the regulatory framework. UIMs recommend that regulation should have specific provisions with respect to ESG issues. This would be in line with the global trend of incorporating ESG and sustainability issues more broadly into regulatory and investment frameworks and would incentivize UIMs to follow international standards[31] in their investment processes and reporting.

Box 2. Overview of Oversight of Alternative Investment Vehicles and Their Managers Internationally[32]

Unregulated—neither the fund nor the investment manager of the fund is categorized as an entity subject to supervision, with no requirement for even an 'information registration' with a regulator: this level could only be applied to non-publicly offered funds but would not conform to the International Organization of Securities Commission requirements.

Information registration—the fund and/or the fund manager must file some information with the regulator concerning its existence and provide statistical data on the fund and its investments and use of leverage relating to systemic risk; this level is usually only applied to non-publicly offered funds and/or their management.

Light regulation—the fund and/or the fund manager is subject to some limited regulatory requirements, is required to report upon its compliance with these and is subject to supervision as to this compliance; this level is usually only applied to non-publicly offered funds and/or their management.

Medium regulation—the fund and/or the fund manager is subject to a series of regulatory requirements, is required to report upon its compliance with these and is subject to supervision as to this compliance; but the regime is not as onerous as the 'heavy' regime applied to publicly offered or retail funds and their management; this level is usually associated with publicly offered funds and/or their management and is often associated with closed ended rather than open ended funds.

Heavy regulation—the fund and/or the fund manager is subject to the detailed level of regulation and supervision usually internationally applied to funds sold to members of the public; this is commonly the case for publicly offered open ended funds – since such funds have an obligation to buy back their units upon request, detailed regulatory requirements are set to ensure that they can meet this obligation and maintain public confidence in these vehicles.

MARKET LEADER PERSPECTIVE: INSIGHTS FROM GIPF EXPERIENCE WITH UNLISTED INVESTMENTS

Since its inception, GIPF has been a major investor in the domestic economy.[33] As the largest manager of long-term capital in the country, GIPF's objective was to contribute to Namibian industrialization efforts and to support the development of local entrepreneurship. Within its fiduciary role, GIPF contribution to the national economy and to the development needs of communities was to provide development capital to unlisted companies and sectors with high growth potential. The fund adopted a broad-based view of socio-economic development in Namibia and implemented this through direct investment, which was a new investment concept in Namibia. Over the 2010-2018 period, GIPF has committed NAD 5.48 billion into the local economy through its unlisted investment program, which has positively impacted the development of the local unlisted market, particularly in the areas of property, private equity, debt and infrastructure. Initially, GIPF committed NAD 3 billion in 2010/2011 to ten unlisted investment vehicles predominantly operating in property, with some exposure in private equity and infrastructure. In 2016, an additional NAD 2 billion was allocated to private equity, venture capital and infrastructure with further NAD 480 million allocated to land servicing and housing. Through this program GIPF invested into at least 56 portfolio companies through SPVs.[34]

GIPF investment in unlisted market, well ahead of Regulation 29, has evolved over time based on lessons learned from its investment operations and in line with the evolving regulatory environment. By investing in private companies, GIPF was well ahead of its global peers – pensions funds in advanced and emerging economies that for the most part were not investing in alternative asset class when GIPR started its direct investments. There are three distinct periods that reflect GIPF's evolving approach to investing in private markets: (1) early experience with DCP from 1996-2008; (2) a revised unlisted investment program based on lessons learned from DCP from 2008-2015; and (3) the introduction of Regulation 29 and the incorporation of ESG in GIPF's investment strategy from 2015 on.

During the first period, 1996-2008, GIPF established the DCP and through it invested NAD 661 million in 21 companies. GIPF's objective was to invest 5% of its assets in DCP. During 1996-2005 GIPF made investments in 21 unlisted companies through equity and debt at the sole discretion of its Board of trustees in accordance with Regulation 28. Over 50% of DCP was invested in secondary and tertiary sectors of the economy, with 28% invested in the industry sector and 11% in the tourism sector.[35] Reports of DCP failures emerged in 2005 and GIPF put a moratorium on the portfolio and started divestment from these 21 investments. This was followed by several investigations into DCP. Review conducted by NAMFISA in 2007 suggested multiple incompetence and in some cases illegal behavior.[36] Some of GIPF administrators and Board members were replaced, but the report by the Auditor General Office was not published leading to widespread speculation about the extend of the loses and of their underlying causes. Based on DCP detailed holdings provided by GIPF to the World Bank and their value as of 2010 (included in Annex 2), 9 out of 21 investments (NAD 501 million out of NAD 661 million of total invested capital) were liquidated at a significant capital loss and 3 (NAD 27 million) had to be completely written off within a year of their original investments. Out of the remaining 9 companies (NAD 138 million) that generated positive return over the period, 6 were still held by GIPF in 2010 with the fair value and paid dividend and interest of about NAD 604 million, while other 3 were liquidated at a profit between 2004 and 2008. Based on these holdings, DCP's loss ratio - defined as the percentage of capital in deals realized below cost over total invested capital—is 80%.[37] As of 2010, the fair value

of DCP's remaining holdings was about NAD 403 million, while the paid dividends, interest and capital repayments amounted to NAD 405 million, resulting in NAD 147 million profit over the original NAD 661 million. Over the comparable period, African VC and PE benchmark returned 12% per annum . If DCP portfolio had returned 12% per annum on average over the period of 1995 to 2010, its total value at the end of the period would have been NAD 2.6 billion.[38]

GIPF's assessment of DCP investment outcomes was that while it fell short of meeting its investment returns target, the fund's objective to achieve a socio-economic benefit was broadly achieved due to positive socio-economic impact on communities where these investments were made. For example, while the GIPF financed mining project failed, mining activities continue to operate in the Tsumeb area attributable to the original investment. Further, GIPF's views the facilitation of Namibia's first formal housing development in the north of the country and the spurring of an entrepreneurial spirit in the minds of many Namibians as social benefits of the underlying investments. GIPF is currently in the process of developing a methodology to quantify and assess the impact of its current unlisted investments as discussed at the end of this section.

While acknowledging the positive social economic benefits of DCP investment, GIPF undertook a thorough review of the policies and practices that led to suboptimal financial results. It was concluded that, due to the lack of specialized skills in-house, GIPF should not undertake investments in unlisted companies directly but instead rely on experts or providers that are specialized in the industries of interest. One of the critical lessons was that essential for the investment process was robust governance: to ensure that investments are made based on financial merit and are insulated from any interference. That included the highest level of transparency, introduction of checks and balances, and oversight throughout the investment process. GIPF also sought to engage with leading global pension funds to learn from their experiences and to incorporate international best practices.

Period two followed the investment review, when in 2008 GIPF developed an Unlisted Investment Policy. GIPF adopted a wholesale approach to investing in unlisted investments to make such investments at arm length by engaging specialized intermediaries with the necessary skills to ensure that the fund's resources are properly invested. GIPF established a dedicated team to manage the unlisted investments that focused on: (1) crafting specialized mandates with careful portfolio construction within the overall portfolio and strategic asset allocation process; (2) ensuring a rigorous process of unlisted investment manager due diligence and monitoring; and (3) ensuring alignment of interest by unlisted investment managers to GIPF's to require that managers invest some of their own capital alongside GIPF's.

Period three followed the introduction of Regulation 29 in 2014, when GIPF incorporated further changes to its governance and investment processes of unlisted investments. Companies and individuals interested in GIPF financing could no longer approach the fund directly but were required to approach UIMs that had been appointed by the fund for this purpose. A number of unlisted investment managers with expertise in private equity, venture capital, debt and infrastructure financing have been appointed through several public tender processes to participate as intermediaries and manage the allocated funds in line with GIPF objectives and according to Regulation 29. The full list of appointed UIMs is included in Annex 3.

As an integral part of its ESG policy, GIPF is currently in the process of developing a methodology to assess the socio-economic impact of GIPF's unlisted investments in the local economy and has contracted a consulting firm to assist with these efforts. In these efforts GIPF is targeting to quantify and asses the following impacts of its investments: (1) the microeconomic impact of the projects; (2) the microeconomic multiplier effects associated with the establishment of the project and the resultant impacts on the ecosystem services and environment; (3) the macroeconomic costs and benefits of the project to Namibia as a whole; (4) the social impact on human well-being; (5) the responsible investing practices by incorporating ESG matters and their impact; (6) the social impact of addressing diversity and equal opportunities; (7) the socio-economic impact of addressing government and community relations; and (8) the socio-economic impact of addressing supply chain management.

PERSPECTIVE OF UNLISTED INVESTMENT MANAGERS AND SPECIAL PURPOSE VEHICLES

Regulation 29 catalyzed the creation of an unlisted investment industry in Namibia, which is currently in its infancy. As of end 2018, there were 22 UIM registered with NAMFISA. The UIM are diverse in terms of their technical capacities and investment operations. The managers founded in response to Regulation 29, started by establishing their governance, developing investment policies and building their teams. Given the lack of skills domestically, these funds called on support from more established managers in the region, with most of the managers now operating in partnership with South African managers, as well as with some from Botswana. Boxes 3 and 4 present case studies of two Namibian UIM (both in partnerships with South African partners) investing in infrastructure: Ino Harith Capital that invests across multiple infrastructure sectors and Mergence Unlisted Investment Managers (Namibia) that focuses on impact opportunities with a primary focus on infrastructure and developmental investments.

As the market leader, GIPF dominates the unlisted investments and has a disproportionate impact on UIMs, with UIM without GIPF allocations struggling to gain a foothold. GIPF has invested with 15 of the 22 UIMs through two public RFP processes since Regulation 29 was enacted, listed in Annex 3. GIPF requires certain level of track record to participate in the RFP process as a qualified investor, and, as a result, the Namibian managers without external partners do not necessarily meet this threshold. Without GIPF mandates UIM do not see themselves as being in a position to demonstrate track-record to other potential (but much smaller) institutions and/or pension funds and struggle to raise capital for their investments. These UIMs perceive that the GIPF RFP process is not fully transparent nor fair, with money already being earmarked for specific managers and that there is insufficient competition between "brand name" UIMs and the rest. Further, as the pension funds' allocations required by Regulation 29 is quite small, UIMs are not in a position to grow technical teams to originate, process and execute investments. All UIMs, especially those without GIPF allocations, have to operate frugally within a challenging economic environment and an unsupportive ecosystem as discussed further.

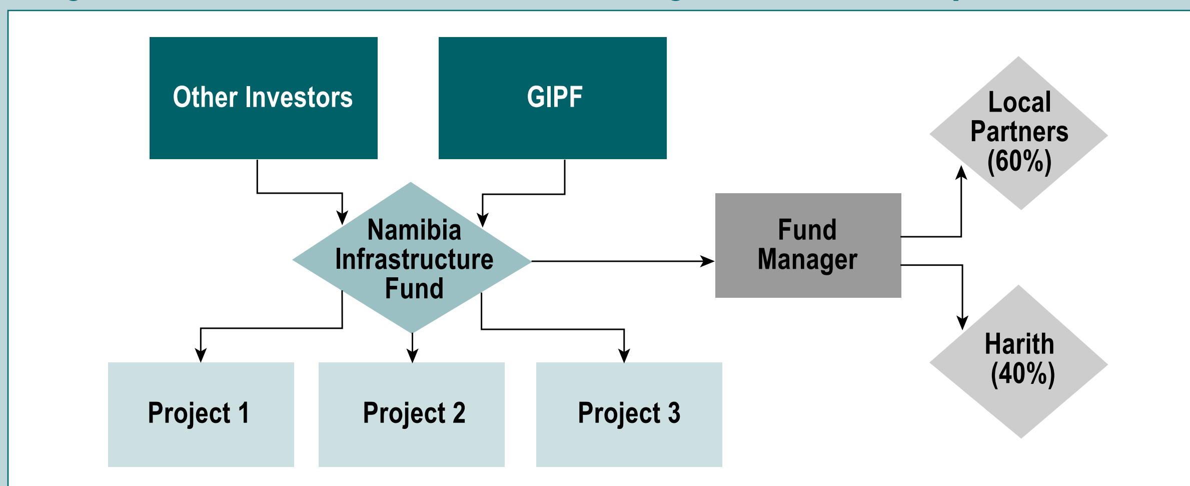
The unlisted market ecosystem in Namibia is under-developed reflective of the early stage of market development. Namibian institutions, which are essential for the functioning and further advancement of this industry, such as the national regulator, auditors, administrators, consultants, etc., do not yet have the specialized skills and sufficient experience. Ongoing implementation and refinement of Regulation 29 would need to be accompanied by a comprehensive ecosystem of relevant policies, regulations and instruments supporting the adequate development of service providers to the industry. Existing institutions would benefit from developing their technical skills and expertise to support the functioning of the market, as lack of expertise and experience was cited as one of reasons for delays in execution of investment transactions. UIMs also shared that further clarification and training on Regulation 29 rules would be essential to build trust among market players and to allow the industry to grow.

Most UIM cited challenges with the availability of projects and infrastructure deals in Namibia as a structural issue in Namibia. While Regulation 29 is designed to address various issues to improve the flow of capital to unlisted investments, the development of the industry is hampered by the limited supply of quality investment projects that the regulation will not be able to address. As a general sentiment, investors report that there is not enough of a supply/pipeline of deals, especially of large deals, or that they are not easily accessible. Most of the deals

Box 3. Ino Harith Capital - Case Study of Namibian Unlisted Investment Manager for Domestic Infrastructure Investments[40]

The Fund Manager: Ino Harith Capital is a Namibian UIM licensed by NAMFISA. The Fund Manager was established to carry on the business of an investor into unlisted companies and to identify, evaluate, negotiate, execute and monitor investments. Established in 2014 Ino Harith Capital is 60% owned by Namibian Investors and 40% owned by Harith General Partners based in South Africa. Harith General Partners is a leading infrastructure private equity fund manager in Africa with over USD 1 Billion in assets under management. Established in 2007 to capitalize on African infrastructure opportunities, Harith provides equity funding to project developers and sponsors to facilitate infrastructure transactions, as shown in the diagram below.

Diagram 2: Structure of the Fund Manager Ino Harith Capital



The Fund: GIPF has championed the establishment of the Namibian Infrastructure Fund managed by Ino Harith Capital referred to as the "NIF". NIF is a dedicated Namibia focused Infrastructure Fund. The fund strictly adheres to ESG principles. The fund currently has NAD 780 million committed capital from GIPF.

Governance Structure: The legal entity for NIF is Bewind Trust registered with NAMFISA (15/SPV/15). The Board of Trustees represents the interests of investors in the fund. The Investment Committee, Audit and Risk Committee, and Conflicts Committee are sub-committees of the Board on key governance issues.

The Fund Objective: To realize superior financial returns through income from and capital appreciation of infrastructure investments made in portfolio companies across Namibia.

The Fund Investment Strategy: The 12-year closed equity and mezzanine fund invests in commercially viable infrastructure projects in Namibia in local currency across a diverse range of infrastructure assets in the energy, ICT, transport and logistics, health, municipal services, water and sanitation sectors. The fund assumes a significant minority investor position in projects. The fund targets about 15-20 deals/assets. Equity investments range between NAD 15 million and NAD 56 million. The fund's target IRR is 15%, with a hurdle rate of 9.75%. The fund's management fee is 2.5% per annum with an incentive fee of 20% net of the hurdle rate.

Box 4. Mergence Unlisted Investment Managers (Namibia) - Case Study of Namibian Unlisted Investment Manager for Domestic Impact Investments Manager for Domestic Infrastructure Investments[41]

The Fund Manager: Mergence Unlisted Investment Managers (or Mergence) is a majority Namibian women-owned asset manager which is registered as an Unlisted Investment Manager in accordance with Regulation 29. The company's primary focus is on infrastructure and developmental investments in line with the Mergence groups' ethos of "creating shared value" as impact investors. Mergence provides debt and/or equity funding to projects as well as plays a catalytic role in developing and implementing public private partnerships between government and the private sector. Mergence was incorporated in 2014. Mergence is 51% Namibian-owned and is a subsidiary of specialist boutique asset manager Mergence Investment Managers (South Africa), which has been a signatory to the United Nations Principles of Responsible Investment (UNPRI) since 2008.

Diagram 3: Structure of the Fund Manager Mergence

The Fund: The Mergence Namibia Infrastructure Fund Trust (15/SPV/07) was launched in 2015. The fund has a capital commitment of NAD 300mill from GIPF and is currently engaging other pensions funds and their consultants for possible mandates.

Governance Structure: Governing Board of Trustees provides overall governance, oversight and control over the Fund. The Board is responsible for the Trust and is required to represent the interests of the investors and ensure that the Fund Manager acts in accordance with the Management Agreement and Investment Plan. The board comprises a majority of Independent Trustees. The board also has two sub-committees: the Investment Committee and the Nomination, Compliance and Conflict Committee.

The Fund Objective: The fund's long-term objective is to build a truly Namibian financial services company that provides world class tailored investment and financial solutions. The fund further aims to be recognized and rated as a premier investment manager by its clients, prospective clients and industry participants.

The Fund Investment Strategy: The Fund's key focus is on Infrastructure and development finance covering sectors such as energy generation, energy efficiency, water infrastructure, telecommunications, and waste management. The fund intends to be a long-term investor (10-year tenure in each portfolio company) in the underlying unlisted equity assets and seeks assets with high quality cash flows, long duration, low volatility and revenues linked to inflation. By incorporating ESG issues into its investment process, the fund engages with companies it invests in to strike a balance between profits and being socially responsible, and to actively manage their environmental impact while maintaining high standards of corporate governance.

are originated by the state or state-owned entities. Those UIM that have established sound partnerships with government and public entities are seen to be well positioned to source future infrastructure PPP opportunities. Managers also source opportunities through a combination of follow-up opportunities from earlier investments, team networks, industry conferences and seminars, advisors and the technical committee networks. Those managers that have partnered with more established (mostly South African) managers, rely on their experience and networks in sourcing unlisted investments. In rural areas, where entrepreneurial activity is particularly low, there appears to be almost no origination. Across the board, most deals are seen as too small to undertake by many UIMs given the shortage of both the human and financial resources to process such deals even if they are seen as potentially having significant economic and social impact. Box 5 illustrates examples of two transaction in the renewable energy space by Mergence Unlisted Investment Managers (Namibia).

UIMs that do see a sufficient supply of projects agree that they face multiple institutional, policy and regulatory challenges at the market and project levels that hinder the development and execution of projects. Among the challenges cited are insufficient publicly available information about industries and specific projects, lack of technical skills and expertise in project development, and limited financial instruments. These factors make it difficult for UIMs to identify attractive projects or make capital available for those projects that are ready to be financed. Some managers engage directly with investors on ways to address specific challenges. One UIM, whose sole investor is GIPF, described the process of engaging with GIPF on the lack of resources required for project preparation. In response, GIPF brought forward 2% of their committed capital that the UIM was then able to deploy to bring the project to financial close.

As the Namibian economy has been contracting since 2016, the economic slowdown presents further challenges for the development of the private industry generally and for unlisted investment managers' search for unlisted investment opportunities in particular. According to the 2019 IMF Article IV, after a period of exceptional growth and rising economic imbalances, in 2016 Namibian economy began contracting after averaging 5.75 percent annual GDP growth during 2010–2015 due to a temporary boost in investment through the construction of large mines and expansionary fiscal policies. In 2016, as construction in the mining sector returned to pre-2010 levels and the government started implementing consolidation plans to stabilize the public debt-to-GDP ratio, real GDP started to contract. Private and public investment continued to decline, and unemployment reached post-global financial crisis highs.[42] Average growth is expected to be significantly lower over the next few years than prior to Namibia's recession in 2016-19 with implications for industries and services making investments across private markets more challenging.

Due to the slow deployment of committed capital the current fees for unlisted investment managers (2 percent–2.5 percent /20 percent) are under pressure. Namibian managers operate with a fee structure typical for private asset managers globally: the investors pay an annual management fee of 2–2.5 percent per annum plus a performance fee of 20 percent above a hurdle rate of profits from investments. As managers' deployment of committed capital is slow due to a variety of factors, there is perception that these fees are too high given the Namibian market realities.

Box 5. Examples of Two Transactions in Renewable Energy (Enjuva and Momentous Solar One projects) by Mergence Unlisted Investment Managers[43]

Ejuva Project (August 2018): Mergence Unlisted Investment Managers (Namibia) provided equity and debt financing for the two solar power plants, Ejuva One and Ejuva Two, which were officially opened on August 23, 2018 with a total build cost of NAD 250 million. Combined, the plant will feed an estimated 25.8GWh per annum into Namibia's national grid. It is among the 14 renewable energy projects commissioned under the interim Renewable Energy Feed-in Tariff program (REFIT program). The Ejuva projects were backed by 25-year power purchase agreements with Nampower with variable tariff or NAD 1.37 with inflation adjustment annually after the Commercial Operations Date.

The local co-development partners, OKA Capital (Pty) Ltd and BPI Energy Solutions (Pty) Ltd, played a key role in successfully bringing the projects to commission. The local partners own 34 percent of the equity, while developer CIGenCo SA owns 49 percent and asset manager Mergence Unlisted Investment Managers (Namibia) owns 17 percent on behalf of its investors. In addition to a 17 percent equity stake in Eujuva, Mergence advanced loans to finance the equity position of the local shareholders in Ejuva. By financing Previously Disadvantaged Namibians (PDN)[44] participation on competitive terms, the local shareholders were able to participate more independently and strongly—unlike some projects where funding structures are too dependent on the lead investor. Two separate SPVs were formed to facilitate the investment: Ejuva One Solar Energy (Proprietary) Limited and Ejuva Two Solar Energy (Proprietary) Limited.

Agreements were executed by the local equity partners and transferred to SPVs, Ejuva One and Ejuva Two. CIGenCo acted as a developer and 49 percent investor in and overseer of the development, construction and operation of the power and electrical infrastructure. Co-developers were OKA Investment (PDN Ejuva Two), Benzel and Partners (PDN Ejuva One), and Solar4Africa. Ejuva project's targeted impact is: (1) diversification of Namibia's energy mix and contribution to increase generation capacity in Namibia; (2) reduction of carbon emissions by producing green, emission-free electricity: (3) promotion of employment and skills development during construction and operation: (4) positive demonstration effects for solar development in Namibia and neighboring countries; and (5) local ownership of the asset, with long-term predictable cash-flows well suited for pension funds.

Momentous Solar One project (June 2019): In June 2019 Mergence Unlisted Investment Managers (Namibia) bought a majority stake in the 6MWp Momentous Solar One solar energy plant, located near Keetmanshoop. The seller was NASDAQ-listed Canadian Solar, one of the world's largest solar power companies. The shares purchased from Canadian Solar will be held in the Mergence Namibia Infrastructure Fund Trust on behalf of the Namibian GIPF with the objective of further localization of the industry—as well as bringing accounting and reporting previously done offshore to be transferred to a local service provider.

Local entrepreneurs, MTJ Investments, have a 30 percent stake in the plant which has been refinanced by loans from Mergence. The restructuring of MTJ's funding by Mergence Namibia makes provision for earlier returns to MTJ Investments allowing MTJ to more fully participate in the project. Post-acquisition, the local ownership of 30 percent will grow to a minimum of 86 percent from the investment of the Mergence Namibia Infrastructure Fund.

The Momentous Solar One project near Keetmanshoop will provide solar power generation for a period of 25 years under the Namibian government's Renewable Energy Feed-In Tariff (REFIT) program, at the rate of NAD 1.37 per kWh. The solar plant has been in commercial operation

since November 2017. Powered by 18,480 Canadian Solar CS6U-325P modules, the plant will generate approximately 14,800 MWh of clean energy each year. Canadian Solar will provide operations and maintenance services to the plant for the immediate future. There will be further localization of on-site jobs as seller responsibility for the plant winds down.

POLICY AND REGULATORY IMPLICATIONS FOR NAMIBIA AND OTHER COUNTRIES

Through Regulation 29 Namibia devised a targeted approach to create an enabling environment to deploy domestic savings, predominately from pension funds, for the benefit of Namibian development. NAMFISA's overall objective was for institutional investors to deploy their capital to private investment domestically, to ensure that management of direct investments in Namibian companies is professional to instill confidence in market participants and the public, and to advance development of Namibian capital markets through creation of a new (alternative) asset class. Namibia's context is unique due to several factors: (1) significant national savings driven by a large government pension fund (GIPF) that has a social mandate; (2) economy that is short of investable instruments and development funding; (3) controversial and lasting legacy of investment failure of the GIPF's early experience in direct investments domestically through DCP.

NAMFISA's approach was to tailor regulation to Namibian circumstances that, while diverging from international practice, was addressing identified national issues. More specifically, NAMFISA instituted mandatory requirements that all pension (and insurance) funds invest in unlisted Namibian companies, formalized the unlisted investment market and created specialized intermediaries (UIMs), and introduced high level of regulatory oversight for both investment managers (UIMs) and investment vehicles (SPVs). While more time is needed to fully evaluate the impact of Regulation 29 on returns of the pension funds and on domestic and capital market development, early results demonstrate that Regulation 29 and new market structure contributed meaningfully to addressing issues related to the governance of and within pension funds, improving the due diligence of unlisted investments, the investment process, active management and reducing the perception of corruption.

While prescribing assets is not in line with international good practice, such as OECD Core Principles of Private Pension Regulation, and similar approached have not led to successful outcomes in other countries in the region, early observations from Namibian experience suggests ways of managing the risks of requiring domestic investment. In particular:

- Limiting the prescription to the small percentage of total assets allowed for direct investments to be accommodated within pensions funds' overall financial return targets to meet their fiduciary obligations to their members;
- Introduction of secure investment vehicles to channel investment flows to projects with social-economic objectives provided governance and financial structures to mitigate endemic issues with direct investments within the challenging governance context;
- Ongoing development of a robust system to measure development impacts to monitor the investments has been and will be critical to demonstrate benefits to members and maintain credibility within the broader community.

Lessons can also be learnt from the Namibia case on financial market instrument design and regulation. Namibia chose an SPV structure because it did not have the traditional GP/LP structure and ensured its professional management and an appropriate level of transparency. Namibia's started with the highest level of regulation by regulating both investment managers and their instruments, as compared to international market practice of regulating managers alone. The Namibia

experience – along with practice in many countries - showed that the development of capital market more broadly and of alternative asset classes in particular is an evolutionary process. Specifically, investment structures should be flexible enough to fit local market circumstances and evolve over time as the local market develops and market participants become more experienced. Similarly, the level of regulation should evolve as the market develops and market participants get more skilled and experienced.

Finally, this approach to domestic investment to work certain enabling conditions need to be developed simultaneously with the regulatory reform. Firstly, in the absence of a pipeline of deals, financial sector reform alone will not be able to stimulate the country's economic development. Secondly, a sufficiently developed financial sector with financial institutions capable of assessing alternative investment opportunities and structuring these appropriately is required.

ANNEX 1. KEY DEFINITIONS AND SALIENT FEATURES OF THE REGULATION 29[45]

Regulation 29 is the implementation framework for Regulation 28, which introduces unlisted investments as an asset class that institutional investors should consider in order to enhance returns on their investments and diversify their portfolios. Regulation 29 was introduced to regulate the investment of pension fund assets in unlisted securities. The regulation sets out the requirements that pension funds must comply with when they invest in unlisted instruments. Regulation 29 stipulates that pension funds must invest in unlisted investments through an SPV.

Regulation 29 covers pension funds and those managing their unlisted investments and instruments, specifically UIM and SPV. Unlisted investments are defined as investments that take the form of prescribed equity or debt capital in a company incorporated in Namibia and are not listed on any stock exchange, but exclude assets such as credit balances, and bonds including debentures issued by government, local authorities, regional councils, state-owned enterprises and corporate.

The requirements for unlisted investments by pension funds are listed as follows:

- All unlisted investments must to be held by SPVs;
- Pension funds are to purchase securities (equity and debentures) issued by SPVs; and
- Pension funds are prohibited from directly or indirectly investing in UIM, except when said indirect investment is through a company listed on a stock exchange.

Special Purpose Vehicles. Regulation 29 specifies that an SPV can be a company or a trust organized and operated for the purposes of holding unlisted investments on behalf of investors and outlines the following requirements:

- Requirement for name vetting by Registrar;
- Requirement for localization, documentation, directors or trustees;
- Restrictions on who can be directors or trustees of SPVs; and
- Requirement for vetting the investment plan by the Registrar.

The Regulation 29 defines an SPV's capital structure as follows:

- If it is a Special Purpose Company (SPC) (Company)—authorized capital forms total "committed capital" if subscribed by investors, drawdown results in paid-up shares in the SPC;
- If it is a Special Purpose Trust (SPT) (Trust) – total subscription interest forms "committed capital" if subscribed by investors, draw-down results in paid-for interests in the SPT;
- If it is an SPC and issues debt, there are two forms of investment: (1) committed (contributed) capital in the form of shares; and (2) holdings of debentures.

The governance of SPVs includes: (1) powers, restrictions and duties of the SPV, including their functions and how they are performed; (2) appointment of auditor and valuator; and (3) de-registration of SPVs.

Unlisted Investment Managers. An UIM is any person who is registered in terms of Regulation 29 and engages in the buying, selling or otherwise dealing with unlisted investments on behalf of an SPV.

The requirements for UIM are listed as follows:

- Name reservation and prohibition of unregistered managers;

- Requirements for registration, including capital requirements, localization, directors and principal officer;
- Restriction on directors of UIMs;
- Duties and co-investment requirements;
- Appointment of auditor and valuator; and
- Deregistration of UIMs.

According to Regulation 29, in relation to SPVs and UIMs the Registrar has the powers conferred upon the Registrar by:

- The Namibian Financial Institutions Supervisory Act, 2011 (Act No. 3 of 2001);
- The Inspection of Financial Institutions Act, 1984 (Act No.38 of 1984);
- The Financial Institutions (Investment Funds) Act, 1984 (Act No. 38 of 1984); and
- Any other financial services law, to regulate and supervise SPVs and UIMs, and any matters incidental thereto.

Further, Regulation 29 states that after due notice, the Registrar has the power to remove a director or trustee of an SVP; or deregister an UIM, if not in compliance with these regulations or any other applicable law.

ANNEX 2. DETAILS OF DCP PORTFOLIO INVESTMENTS[46]

OVERALL PERFORMANCE OF DCP										
Investment	Year of Investment	Year of Exit	Type and Number	% of Total #	Capital Disbursed	% of Total Capital Disbursed	Repayments, Proceeds, Fair Value to Date (Sept 2010)	% of Total Recovery	Estimated Fair Value	Return/Expected Return on Investment
PERFORMING INVESTMENTS - CONTINUING OPERATIONS										
Capricorn Investment Holdings	1997	N/A	Equity		639,220		5,541,194		3,387,023	25.8% p.a.
Etosha Fisheries	1996	N/A	Equity		27,500,000		42,226,757		34,153,754	4.7% p.a.
Preferred Management Services	1995	N/A	Loan		6,988,975		6,942,974		46,041	13.3% p.a.
Windhoek Country Club	1995	N/A	Loan		30,000,000		102,461,006		40,447,123	13.6% p.a.
NHE Collateral Account		N/A	Debenture		15,750,000		14,525,000		1,225,654	8.3% p.a.
City Services & Investment Bank - Converted to FNB Shares	1996	N/A	Equity		12,170,000		431,800,435		317,809,411	25.31% p.a. (Based on value of FNB shares at 30/9/2010 plus dividends received, being N$114m)
		6	**28.6%**		**93,048,195**	**14.1%**	**603,497,366**	**74.7%**	**397,069,006**	

NON-PERFORMING INVESTMENTS—CONTINUING OPERATIONS										
Investment	Year of Investment	Year of Exit	Type and Number	% of Total #	Capital Disbursed	% of Total Capital Disbursed	Repayments, Proceeds, Fair Value to Date (Sept 2010)	% of Total Recovery	Estimated Fair Value	Return/Expected Return on Investment
Ongopolo	2000	N/A	Loan converted to equity		70,000,000		43,461,954		4,151,210	(3.9)% p.a.
			1	**4.8%**	**70,000,000**	**10.6%**	**43,461,954**	**5.4%**	**5,591,435**	
PERFORMING INVESTMENTS—SOLD OR REPAID										
Swakopmund Station Hotel	1995	2008	Loan		15,000,000		40,563,540		0	13.32% p.a.
Multiline Investments	2002	2005	Loan		20,000,000		23,383,168		0	6.45% p.a.
Tutunge Investments	2002	2004	Loan		4,600,000		5,681,699		0	14.15% p.a.
		3	**14.3%**		**39,600,000**	**6.0%**	**69,628,407**	**8.6%**	**0**	

NON-PERFORMING INVESTMENTS - ONSOLD										
Investment	Year of Investment	Year of Exit	Type and Number	% of Total #	Capital Disbursed	% of Total Capital Disbursed	Repayments, Proceeds, Fair Value to Date (Sept 2010)	% of Total Recovery	Estimated Fair Value	Return/Expected Return on Investment
Namibia Pig Farm	2002	2009	Loan		26,420,570		9,842,000		0	37.2% of capital recovered
Namibia Grape Company	1999	2007	Loan		164,638,167	24.9%	56,000,000		0	34.0% of capital recovered
Karas Abattoir and Tannery (fermerrly Ostrich Production Namibia)	1996	2009	Loan & Equity		179,008,792	27.1%	18,582,103		0	10.1% of capital recovered
Omaheke Tannery	2002		Loan		23,039,263		2,012,500		0	8.7% of capital recovered
Karas Ostriches	2002	2007	Loan		1,750,000		500,000		0	26.6% of capital recovered
		5	**23.8%**		**394,856,792**	**59.7%**	**86,918,603**	**10.8%**	**0**	

LIQUIDATED AND WRITTEN-OFF INVESTMENTS										
Investment	Year of Investment	Year of Exit	Type and Number	% of Total #	Capital Disbursed	% of Total Capital Disbursed	Repayments, Proceeds, Fair Value to Date (Sept 2010)	% of Total Recovery	Estimated Fair Value	Return/Expected Return on Investment
Black Square Auto Engineering	2000	2002	Loan		6,992,830		2,153,551		0	30.8% of capital recovered
Namibian Chicken Investments		2005	Loan		9,751,514		403,000		0	4.1% of capital recovered
Namibia Plastice & Liquids	2000	2005	Loan		20,000,000		2,061,737		0	10.3% of capital recovered
Tsogang Investments (IUrilKhubis Abattoir)	2000	2003	Loan		5,000,000		0		0	Nil return of capital
Omina Investments	2002	2003	Loan		12,000,000		0		0	Nil return of capital
Sepiolite Production	2002	2003	Loan		10,000,000		0		0	Nil return of capital
			6	**28.6%**	**63,744,344**	**9.6%**	**4,618,288**		0	
		3	**14.3%**		**39,600,000**	**6.0%**	**69,628,407**	**8.6%**	**0**	

Return Summary As of September 2010 (in NAB Dollars)[47]	
Total capital invested in loans and shares	661,249,331
Fair value of DCP investments still owned by the GIPF	402,660,441
Dividends, interest and capital repayments received	405,464,706
Profit to Date (over the period)	146,875,816

ANNEX 3. GIPF'S UNLISTED INVESTMENT MANAGERS AS OF 2019[48]

No.	Unlisted Fund Managers	Special Purpose Vehicle	Mandate	Physical Addresses	LandLine
1	Business Financial Solutions Pty Ltd	Nampro Fund I and Nampro Fund II	Procurement Debt Fund	C/o of Jan Jonker 7 Lazarette Street, Ausspannplatz	061 388 600
2	First Capital Treasury Solution Pty Ltd	First Capital Real Estate Finance Fund	Property Financing for Government Employees	No. 124 Jphn Meinert Street Windhoek Namibia	061 401 326
3	Kongalend Financial Services	Kongalend Renewable Energy Trust	SME Group Lending and Solar Energy loans	C/o of Haddy & Viljoen Street, Windhoek West	061 241 440
4	Konigstein Capital Pty Ltd	Korigestein Capital Property Investment Fund	Property Development, Affordable Housing and Private Equity	Unit 7, The Village, 18 Liliencron Street, Windhoek, Namibia	061 303 227
5	Preferred management Services	Preferred Investment Property Fund (PIPF)	Property Development	Shop no 9, 78 Bougain Villas Estate, Sam Nujoma Drive, Windhoek	061 248 318
6	Safland Property Group Namibia	Frontier Property Trust	Property, focus on Retail Properties, Offices and Industrial	4th Floor, 1@Steps Office, c/o Grove and Chasie street, Kleine Kuppe, Windhoek, Namibia	061 254 972/3
7	TEMO Capital	VPB Growth Fund	Private Equity and Venture Capital	Unit 6, Trift Place, Corner of Schinz & Trift Streets, Windhoek, Namibia	061 220 069
8	IJG Private Equity Pty Ltd	Desert Stone Fund	Private-Equity and Venture Capital	100 Robert Mugabe Avenue, First Floor Heritage Square, Windhoek	061 383 517
9	Old Mutual Investment Group Namibia	Tunga Real Estate Fund & Expanded Infrastructure Fund	Property (Retail, Residetial and Affordable Housing) and Infrastructure	10th floor. Old Mutual Towers, Altemative Investments Old Mutual Investment Group (Namibia) (Pty) Ltd	061 299 3264
10	Ariya Bridge Capital (Pty) Ltd	Ariya Bridge Infrastructure Fund	Infrastructure & Private Equity	Unit 13 2nd Floor, Bridgeview Building, Dr. Kwarne Nkrumah Street, Namibia	061 222 962
11	Bacbab Capital Pty Ltd	Bacbab Growth Fund	Venture Capital Fund	Unit 1, 13 Liliencron Street Eros, Windhoek	081 773 3237
12	EOS capital Pty Ltd	Allegrow Fund Pty Ltd	Private Equity	Mandela Offices, corner Arians Street and Nelson Mandela Street, Klein Windhoek PO Box 11526, Klein Windhoek	061 304 400
13	Ino Harrith Capital Pty Ltd	Namibia Infrastracture Fund	Infrastructure & Private Equity	69 Jener Street, Windhoek West	061 3088 443
14	Mergence Investment Managers (Pty) Ltd	Mergence Namibia Infrastracture Fund	Infrastructure & Private Equity	1205 Luther Street, Nuyoma Office Park	061 244 653
15	Musa Capital Namibia Pty Ltd	Namibia Mid Cap Fund	Private Equity	A 30 Blohm Street, Windhoek, Namibia	061 246 900

ENDNOTES

1. In this context "capital markets" refer to both publicly listed capital markets, such as stock exchanges and non-government bond markets, and private or alternative capital markets.
2. "Unlisted Investment Managers" is the term defined by NAMFISA in Regulation 29 as "a person who is registered in terms of sub-regulation (38) and engages in the buying, selling or otherwise dealing with unlisted investments on behalf of a special purpose vehicle." While this term is not used in the industry managing unlisted investments, we will use NAMFISA's terminology throughout this note. Annex 1 provides the list of terms and definitions used in Namibia in relation to unlisted investments and their management, as well as specific details of the Regulation 29 that are referred to throughout the note.
3. IMF Article IV, 2019. https://www.imf.org/en/Publications/CR/Issues/2019/09/12/Namibia-2019-Article-IV-Consultation-Press-Release-and-Staff-Report-48675.
4. Based on IMF Article IV, 2019, commodities (e.g., diamonds, copper, uranium) constitute about 45 percent of the Namibia's exports of goods and about 8 percent of GDP.
5. IMF Article IV, 2019. https://www.imf.org/en/Publications/CR/Issues/2019/09/12/Namibia-2019-Article-IV-Consultation-Press-Release-and-Staff-Report-48675.
6. As of September 2017, 10 banks were licensed in Namibia: 7 commercial banks, E-Bank, a branch of a foreign bank, and a representative office. The four large banking groups (three of them subsidiaries of South African banks) hold about 98 percent of total bank assets, according to the IMF's "Namibia Financial Stability Assessment", 2018.
7. "Namibia Financial Stability Assessment", 2018. IMF.
8. "Namibia Systematic Country Diagnostic Concept Note." 2019. The World Bank.
9. South African Development Community (SADC) is a regional economic community that includes 16 member states.
10. See Pallares-Miralles, M., Romero, C., Whitehouse, E., 2012, "International Patterns of Pension Provision II'", 2012. World Bank Social Protection and Labor Discussion Paper 1211. http://documents.worldbank.org/curated/en/143611468168560687/International-patterns-of-pension-provision-II-a-worldwide-overview-of-facts-and-figures
11. "Namibia Financial Stability Assessment", 2018. IMF
12. OECD.
13. "The Structure and Nature of Savings in Namibia", 2003. Bank of Namibia. Bank of Namibia's cited the 1997 World Bank study that distinguished countries across three levels of development: countries where assets of contractual savings institutions are less than 10 percent of GDP, over 10 percent but less than 50 percent, and exceed 50 percent.
14. Ibid.
15. Namibia Financial Stability Assessment, 2018. IMF.
16. Ibid.

17. “The Structure and Nature of Savings in Namibia”, 2003. Bank of Namibia.

18. Namibia Financial Sector Strategy 2011-2021. 2011. Namibia Ministry of Finance. https://www.africanbondmarkets.org/fileadmin/uploads/afdb/Countries/Namibia/Bank_of_Namibia/Namibia_Fin_Sector_Strat-2011-21.pdf

19. Even today, while the market capitalization of the NSX is sizeable at 10 times GDP, there are only 8 domestic equities with a primary listing on the NSX, accounting for 1.85 percent of market capitalization. The rest are dual-listed stocks, most with a primary listing on the JSE.

20. “The Structure and Nature of Savings in Namibia”, 2003. Bank of Namibia.

21. Ibid.

22. Source: OECD.

23. “The Structure and Nature of Savings in Namibia”, 2003. Bank of Namibia.

24. “Namibia: Selected Issues and Statistical Appendix”, 2008. IMF.

25. Vugs, Adrianus. “Investing Pensions for the Long-term.” September 2016. Presentation at World Bank 7th Pensions and Savings Conference.

26. Ibid.

27. “What Is Regulation 29?” NAMFISA. https://www.namfisa.com.na/educates/regulation-29-unlisted-investments/

28. Globally, the average period between identifying and executing unlisted deals is three years while the exit can take many more years, especially in countries with shallow markets and limited options for exiting unlisted investments, such as in Namibia. As an average carry period of such investments is seven years, private equity investors can wait a decade or longer before seeing the results of their investments and in a nascent Namibian market it may take even longer.

29. Ibid.

30. “Capital Markets and SMEs in Emerging and Developing Economies: Can They Go the Distance?” forthcoming World Bank FCI policy note. July 2019. The World Bank.

31. Such as the IFC Environmental & Social Performance Standards.

32. “Best Practices on Oversight and Regulation – Guidelines on Alternative Investment Vehicles and Fund Managers.” (Forthcoming) 2019. The World Bank.

33. As of March 2019, GIPF invests 38% of its assets in Namibia, 27% percent in South Africa, 27% internationally and 8% on the African continent. In terms of its asset allocation, the fund invests in bonds, cash, equity, both public and private, and property. Namibian allocation is 54% fixed income, 29% public equity, 8% private equity and 9% to cash and other equivalents. Thus, Namibian private equity makes up about 3% of GIPF total portfolio.

34. GIPF 2018 annual report https://www.gipf.com.na/web/reports/annual/GIPF_IAR2018.pdf.

35. “Private Equity: Lessons for Namibia”, 2005. Bank of Namibia.

36. “Historical Dictionary of Namibia”, 2012.

37. In the US, loss ratios for Venture Capital and Growth Equity are 35% and 13% respectively from 1992 to 2008 (see table 1 in https://www.cambridgeassociates.com/insight/growth-equity/).

38. https://www.avca-africa.org/media/1867/2017-q2-cambridge-associates-africa-pe-vc-benchmark-for-avca_website-version.pdf.

39. This calculation assumes 12% return for each year during 1995 and 2010 and based on the yearly schedule of DCP capital disbursement as provided by GIPF in Annex 2.

40. Based on the information provided by Ino Harith Capital (Namibia) in 2019.

41. Based on the information provided by Mergence Unlisted Investment Managers (Namibia) in 2019.

42. IMF Article IV, 2019. https://www.imf.org/en/Publications/CR/Issues/2019/09/12/Namibia-2019-Article-IV-Consultation-Press-Release-and-Staff-Report-48675.

43. Project description is based on press releases provided by Mergence Unlisted Investment Managers (Namibia) in 2019.

44. By mobilizing capital in support of PDN participants in infrastructure projects Mergence Namibia aims to ensure that PDN participation in Namibia infrastructure projects is achieved in a sustainable way, and local ownership is able to compete on an equal footing with their international (and professional) counterparts. PDN investors need support to participate alongside international investors, especially in capital intensive infrastructure projects, as they have had challenges in raising capital and making their voices heard. Mergence Namibia seeks to address this by, for example, offering a small equity stake alongside funding the PDN partners to make the economics for the PDN participants more attractive. Mergence Namibia prefers to participate in both the equity and PDN financing tranches (should PDN financing be required) or equity only if PDN financing is not required. For example, in the energy sector the minimum requirement is for PDNs to own 30 percent of an energy project (energy license condition) and yet they are struggling to raise the needed capital.

45. This annex is based on the text of the Regulation 29 and information on NAMFISA's website https://www.namfisa.com.na/educates/regulation-29-unlisted-investments/.

46. GIPF.

47. GIPF.

48. GIPF.

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