Start-up Spotlight: Southern Cross Renewable Energy Fund

An overview on the Fund with advice from Fund Manager, Dr Mark Bonnar

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Australian Government
Australian Renewable Energy Agency
ARENA

INTRODUCING THE SOUTHERN CROSS RENEWABLE ENERGY FUND

The Southern Cross Renewable Energy Fund (Fund) was established by Fund Manager, Southern Cross Venture Partners, in 2012. The Fund is a co-investment between the Australian Government (through ARENA) and Softbank China Venture Capital (SBCVC), with each providing up to $75 million of the Fund's committed capital. SBCVC is a leading venture capital and private equity firm based in Shanghai China and focuses on high-tech, high growth companies in a number of different sectors including Clean Tech. The Fund Manager makes all investment decisions based on its own investment criteria and within the guidelines of ARENA's Renewable Energy Venture Capital (REVC) Fund Program.

THE PATH TO INVESTMENT

The Fund Manager, Southern Cross Venture Partners, looks for opportunities to partner with renewable energy entrepreneurs with a clear vision of purpose and global aspirations. The Fund Manager is looking for entrepreneurs and management teams using innovative technology to target markets ripe for disruption. As is typical for a venture capital fund, informal engagement begins with prospective investees engaging early with the Fund Manager and outlining their technology or business proposition and how it fits within the mandate of the Fund. The Fund Manager will then consider the investment opportunity within the overall portfolio. Companies may be invited to make a formal presentation to the Fund Manager and/or the Fund's Investment Committee (IC).

After a period of consideration and due diligence by the Fund Manager, companies may be asked to enter into negotiations for a conditional offer of finance. As a result of any investment, the Fund Manager provides active investment management (including guidance, advice and networks at no cost), investment capital and usually acquires a seat on the company's board. Read our Q and A with one of the Managing Directors of the Fund Manager, Dr Mark Bonnar, below for hints and tips.

SUPPORTING THE NEXT WAVE

Since its establishment in 2012, the Fund has supported a number of start-ups, including:

GreenSync

Established in 2010 in Australia, GreenSync works with energy retailers, network operators, regulators and businesses to reduce energy consumption and stabilise the grid using its proprietary software and the automation and control of distributed energy resources (DER). GreenSync is pushing the boundaries for more flexible and decentralised electricity grids in an effort to increase the safe and reliable penetration of renewable energy generation across networks. GreenSync works to help integrate DERs into the grid through the continued development of their software, combining cloud computing, industrial automation and the Internet of Things.

Wattwatchers

A Sydney-based digital energy technology company established in 2007 to help businesses and households to monitor and manage their energy consumption by empowering consumers with access to real-time energy data. Wattwatchers has developed compact and highly accurate metering technology that monitors multiple circuits sharing data via the cloud in real-time via a range of communication options. Access to data allows customers to better manage equipment, such as pool pumps and air-conditioners/HVAC, enabling consumers to optimise the operation of energy intensive equipment depending on tariff structures or when embedded generation such as solar PV panels are operating at peak efficiency.

Octillion Power Systems

Established in 2015, Octillion Power System's Australian entity is integrating advanced lithium-ion storage solutions for mobile and stationary energy storage applications tailored to the Australian and South-East Asian markets. With access to more than 4GW of manufacturing capacity in China, Octillion combines a cost competitive supply chain with world-class research and development to deliver products relevant to the Australian market and broader international markets. Octillion Australia serves the Australian market for advanced power systems based on battery module and battery management system design expertise, partnering with utilities, solar integrators and original equipment makers (OEMs) to design customers Energy Storage Systems aimed primarily at the solar self-consumption market.

BenAn Energy

BenAn Energy owns the IP and know-how for manufacturing a cost-effective, reliable and environmentally friendly (Aqueous) Sodium Ion Battery (SIB) that expands the use of renewables. The battery incorporates abundant, low cost, safe and non-toxic materials, leading to the expectation that BenAn will ultimately be able to offer one of the safest and lowest installed cost per KWh storage systems available. BenAn Australia is focused on advanced design, research and development to address the unique needs of the Australian and South-East Asian energy storage markets.

INTERVIEW WITH DR MARK BONNAR, MANAGING DIRECTOR, SOUTHERN CROSS VENTURE PARTNERS AND FUND MANAGER OF THE SOUTHERN CROSS RENEWABLE ENERGY FUND.

ARENA: How has the renewable energy start-up landscape changed since the Fund was first established?

MB: Investment and policy certainty has been the biggest changing variable for us. Even between 2010, when the Fund was first conceived, and 2012, when the Fund started, the landscape had changed. In 2012 we had a volatile investment environment in the renewable energy space, but by 2013 there was even more uncertainty around key legislation that underpinned the transition to renewables. Since 2014 we have seen a fairly consistent level of interest in the Fund at about 200-250 fairly well-formed applications per year. Of that, we have an investment rate of about 1-2% of proposals, which is typical for a venture capital fund.

ARENA: What is the role of start-ups in the renewable energy industry?

MB: I see start-ups as the "engine room" of the broader renewable energy economy. It's generally accepted that small companies do innovation better than bigger companies, and it's important that in an emerging sector the industry fills its own sails, and keeps the pipeline full with opportunities. Start-ups are a good indicator of the general pulse of our energy ecosystem. You can't expect talented entrepreneurs to come into our sector without a vibrant ecosystem when these young professionals have so much potential in so many areas, so the volume and success of start-ups is a good indicator of the state of an ecosystem more broadly.

ARENA: Where do start-ups best sit in the path of an idea? Post research and development, or later on in the innovation chain?

MB: I see start-ups as filling a gap in the commercialisation process, to originate and incubate new opportunities coming out of research or being spun off from corporates. Start-ups can't do everything alone though - for the process to be effective there needs to be engineers, designers, consultancies, financers and grants to support the start-ups within a sensible policy and regulatory framework.

ARENA: Has your investment focus evolved over the history of the Fund?

MB: Yes, early on we tended to see more pure-play technology proposals. Across the spectrum the bulk of companies we looked at were focussed on hardware innovation. Now we are seeing more software innovation coming in, and in the past few years, some very innovative business models.

We've funded innovative business models based around distributed energy resources and the digitisation of the grid that can mitigate the need for new technologies to be distributed through traditional channels in wholesale and retail sectors, where many of the incumbents are still grappling with their own renewable energy strategies.

ARENA: What are your key considerations when deciding whether to invest?

MB: There's a number of factors - from our perspective the most important are the calibre of the founders and management team. We look at whether the management team have the right motivations, can they build a great team, do they have a track record? Experience isn't everything, but it is a factor.

We then look at product-market fit, and whether the product or service is coming at the right time for the market. It's easier to establish that a product works, particularly in the technology space, but the big question for us is whether the market (and regulation) is ready for the product. Both in terms of functionality, and timing.

Storage is a good example: I made my first storage investment in 2006 expecting residential storage to boom just around the corner, but it has taken longer to reach an inflection point than anyone expected. There are a range of reasons for that, but it highlights that product timing is important in terms of investment selection.

ARENA: What should budding start-ups keep in mind when they are looking for investors?

MB: I'd encourage founders, entrepreneurs, and CEOs to get to know potential investors early on. The best experiences we've had have been where individuals have proactively sought us out early on in the process. With the prevalence of social media and accessible networks there's no reason for not getting onto us early. Talk to us, warm us up, and don't come asking for money in a time pressured environment - investors need time to familiarise themselves with the value proposition, the entrepreneur and management team behind them. I'd also note that we judge proposals on the quality of material we are provided with, such as an Investment Memorandum, so it goes without saying that it's worth getting your paperwork looking good.

ARENA: What are alternative sources of capital for start-ups?

MB: There are a small number of non-specialist funds investing in energy, so I would specifically name Blackbird and Grok Ventures, both funds in Australia that have made energy investments in the past 12 months. The CEFC's Clean Energy Innovation Fund and the Southern Cross Renewable Energy Fund are the only two specific renewable energy investors focussed on early to growth stage investments that I am aware of.

Research and development tax incentives can be an important element for many start-ups, and we would encourage all of our investees to pursue that support. There are also a number of state and federal grant programs, many through ARENA, as well as an increasing number of state-based initiatives.

ARENA: What challenges do many start-ups face and how can they overcome these?

MB: The biggest challenge for start-ups coming to the Fund tends to be a lack of resources, usually linked to a shortage of equity capital. Often I'll see companies under some time pressure to find a capital injection. Raising private equity requires time and perseverance, so again it's important to start early and to keep cash burn low in the initial phases.

When pitching to investors lots of businesses are trying to do too much - developing multiple products in parallel, simultaneously pushing into international and domestic markets, but often don't have the capital or burn through limited capital too quickly and don't hit their milestones so get stranded.

I'd encourage a start-ups as much as possible to do one thing at a time - trying to be all things to everyone and delivering bespoke solutions to all clients causes problems, try to standardise quickly and maintain a laser focus on early customer validation.

ARENA: Going back to skills and expertise in Australia: is there enough around to fill those roles locally?

MB: There's been a huge improvement in the last 10 years, but things are still a little thin on the ground in Australia - there's a high talent mobility issue we have to work with, so in that regard it's important for all start-ups to be able to retain and attract appropriate talent from overseas on visas. Industry wants to see a permanent mechanism to bring talent into highly skilled roles in early stage technology companies.

It's not just about human resources though, but also giving start-ups support, resources, and access to inspiring work-spaces. There are a couple of examples of virtual or physical accelerators in the energy sector: Origin and AusNet Services are part of Free Electrons and EnergyLab hosts a dedicated hubs in Sydney, Melbourne, Brisbane, Canberra and Cambodia! There could be a real opportunity for Australia to attract entrepreneurs from overseas here in the near-term.

ARENA: What do you think could make the Australian market attractive for overseas entrants?

MB: Very good entrepreneurs tend to want to work in locations with a high quality of life. It's no accident Silicon Valley is great place to live; Shanghai, Tel Aviv, Sydney, Brisbane and Melbourne are all great places to live, and that's the first step to them being attractive for overseas entrants.

It's still cheaper to setup and operate a business in Australia than in Silicon Valley- salaries in Silicon Valley are about 30% higher than Australia (especially when accessing the R&D tax incentive) and rent for space in San Francisco for example is significantly higher than Sydney. Silicon Valley is saturated with start-ups, so in Australia attracting software developers tends to be a bit easier.

But we're still quite some way behind a lot of Chinese cities which are setting themselves up as innovation hubs. Hangzhou, Shenzen, Nanjing and even Shanghai are cheaper from a salary and rent perspective, so that's shaping up to be a challenge for Australia to keep founders here rather than losing them offshore.

ARENA: *Is there a typical fundraising process? If so, what does it look like?*

MB: There's no single rule, but typically I'd say there are three key stages:

1. Informal engagement - we get approached by a company that we think might be in line with our mandate and start early discussions. This might take a few weeks, maybe a few months and sometimes longer. I would encourage anyone hoping for an investment from the Fund to look at the mandate of the Fund on-line - it's a good start to be able to show you fit within our mandate.
2. Typically, we'll then invite the company to make a formal presentation to our investment committee. After this, we typically have a number of subsequent discussions and ask some follow up questions.
3. From here if we agree to proceed, we start detailed due diligence and in parallel discussions about the structure of the deal, and ultimately look to a conditional offer of finance, usually a Term Sheet. In terms of timelines, we typically look to close in 3 months from that point.

ARENA: *And you always look to have equity positions in companies?*

MB: Yes - we're operating in the early growth point in the spectrum. We're looking for a company with a defined product or service, which has a demonstrated line of sight to commercial revenues and thereafter profitability!

ARENA: *Are there any common misconceptions that start-ups have when starting their road to commercialisation?*

MB: Generally start-ups underestimate not just the time it takes to raise funds, but also the time it takes to be successful. It took Ali Baba 15 years to reach IPO, even Apple took over a decade to achieve real success. The gestation period for a successful start-up tends to be long, and energy has its own unique challenges. So don't underestimate the time and the resources it takes to achieve success. It's important to use resources cautiously to make sure you're still standing at the end of the race.

In a market disruption there's constant waves and uncertainty, which creates a lot of a nervousness, and sometimes a lot of cautiousness which stretches out timelines. Those that can come though the cycles with an intact balance sheet and product-market fit can take the final stages to success in pole position.