



# **State of Alaska: Economic Context and Agency Review**

## **Senate Labor and Commerce Committee**

February 2017

All data and materials  
as of 8/16 unless otherwise noted

THE BOSTON CONSULTING GROUP

# Project context

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Administrative Order 281 seeks to strengthen the economic development capabilities of the State of Alaska, with the goal to support greater diversification of the economy in the face of a decline in the energy industry. In support of AO 281's goals, in June-July 2016, the Boston Consulting Group (BCG) conducted a study of three public entities – the Alaska Housing Finance Corporation (AHFC), the Alaska Energy Authority (AEA), and the Alaska Industrial Development and Export Authority (AIDEA)

BCG was also tasked with a high-level review and prioritization of relevant state assets, to identify potential opportunities to better leverage those assets to further economic development. Finally, BCG was asked to capture observations on Alaska's economic development efforts and potential opportunities for growth; and to provide additional recommendations to improve the state's institutional ecosystem and capabilities to realize these opportunities

The work was performed using a combination of quantitative and qualitative analysis, with a broad range of internal and external expert and stakeholder interviews. Most critically, the project relied on significant collaboration from staff members and leadership of the three core agencies, the Office of the Governor, the Department of Transportation, and the Department of Natural Resources, among other governmental entities

Throughout the process, these government team members consistently dedicated the required attention and demonstrated commitment to the endeavor. Recognizing the state's current challenges, each of these partners offered learning, insight, and daily engagement to help find opportunities to improve the contribution their organizations can make to the State of Alaska. As the government moves from recommendations to implementation, this focus, energy, and coordination will continue to be critical for success

# Agenda

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## Project overview

Economic development landscape

AHFC summary findings

AEA summary findings

AIDEA summary findings

Next steps

# Executive Summary (I/II)

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**Alaska's economy faces a range of contextual and institutional challenges, however there is opportunity to leverage the State's advantages and improve both the overall enterprise economic development capacity and the ability of existing key agencies to increase their effectiveness in improving the lives of Alaskans**

- States are actively pursuing alternative models to coordinate government activity and outreach to compete for business investment
- A deep dive into Ted Stevens Airport offers one example of how Alaska can drive sector-level growth and increase job creation and economic activity in a key sector

**The three agencies – AHFC, AEA and AIDEA – included in this study, provide many benefits to Alaskans, yet there is opportunity to increase efficiency and strengthen the role they play in the State**

**Our major recommendations include:**

- Maintain AHFC current role in mortgage finance
- Prioritize AEA technology support and strengthen AEA's services provision by linking PCE, grant, and loan funding to incentivize responsible operations and maintenance for rural utilities and a greater shift to a mix of energy technologies matched to community needs
- Integrate AHFC and AEA to better deliver energy and housing services
- Expand Alaska's capabilities to more proactively support large industrial projects in support of Alaska's priority sector growth

# Executive Summary (II/II)

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**These recommendations will have the benefit, among others, of:**

- Potential operational efficiencies and savings from integration of entity operations
- Better use of the state's financial support for energy services provision
- Increased involvement of private sector actors, where possible
- Additional capital directed toward enterprise and community economic development

**These steps will help foster economic development and diversification. They should also be seen as part of continued efforts to address challenges that were beyond the scope of this work**

- Strengthen the "enabling environment"-- factors required for economic growth (e.g., education and skills availability, access to broadband, health care, energy cost)
- Building increased community development coordination and capabilities, in particular for the regional needs of rural Alaska

**While other players (e.g., Commerce) can play a role in fulfilling the study objectives, the project team was asked to retain its primary focus on the core agencies studied**

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# Summary of Economic Development Findings

**Alaska scores poorly on national rankings of business attractiveness with lowest rankings in "enablers" and low-mid rankings on regulatory environment, which can be more easily improved**

**Alaska's current institutional environment is not well equipped to drive a sustained economic development plan and help improve business attractiveness**

- Need for coordinated vision and policy implementation across State, regional, and local entities
- Gaps in capacity and fluctuating resources for State economic development efforts
- Long-term sustainability limited by influence of changing political cycles
- Opportunity to leverage advantages in resource wealth and strong local networks

**Alaska has strengths which create real opportunity including its position as an owner state**

**We recommend Alaska improve its ability to drive economic development with core capabilities in sector strategies and business promotion as well as consider building new capabilities in asset optimization, deal making, and facilitating public private partnerships**

**Benchmarks point to several potential instructional models for driving sustainable economic development, ranging from fully public to public-private blended model to fully privately led**

**A deep dive into Ted Stevens Airport offers a valuable example of how Alaska can use its assets to drive sector-level economic growth and increase job creation and economic activity in a key sector**

# Alaska scores poorly on national rankings of business attractiveness and is mid-range in regulatory friendliness



## Rankings

Alaska ranks **45th** in US state business attractiveness

### Sub-Scores in 10 Criteria for Business Attractiveness

<b>#45:</b> Cost of Living	<b>#37:</b> Infrastructure
<b>#41:</b> Cost of Doing Business	<b>#37:</b> Education
<b>#41:</b> Tech & Innovation	<b>#36:</b> Access to Capital
<b>#41:</b> Economy	<b>#25:</b> Business Friendliness
<b>#38:</b> Workforce	<b>#20:</b> Quality of Life

## Forbes Rankings

Alaska ranks **47th** in US state business attractiveness

### Sub-Scores in 7 Criteria for Business Attractiveness

<b>#49:</b> Quality of Life	<b>#41:</b> Growth Prospects
<b>#44:</b> Population	<b>#34:</b> Labor Supply
<b>#45:</b> Economic Climate	<b>#27:</b> Regulatory Environment
<b>#44:</b> Business Costs	

**There is room to improve relative to other states; regulatory environment is the most effective place to start**



# Alaska's has considerable resources to leverage, but also faces some unique challenges

## Context strengths

**Resource wealth**

**Financial assets**

**Water resources**

**Geographic position**

**Cultural diversity**

## Context challenges

**Dependency on resource extraction vs value-add**

**Success of oil has limited focus on other industries**

**Unique regional needs and mixed development levels**

**Constrained by Federal land ownership (~60%)**

**Limited enablers: technology, education, energy costs**

**Low population density**

**Community development efforts face additional challenges not addressed here**

# Alaska similarly faces unique set of institutional challenges and opportunities for enterprise economic development

## Challenges

**De-centralized planning  
without common vision**

**Fractured coordination across  
wide range of public entities**

**Fluctuating resource levels  
for econ development**

**Gaps in capabilities and  
capacity**

**Political cycles limit  
sustained efforts**

**Focused on regulation vs.  
commercialization**

## Opportunities

**Connected network**

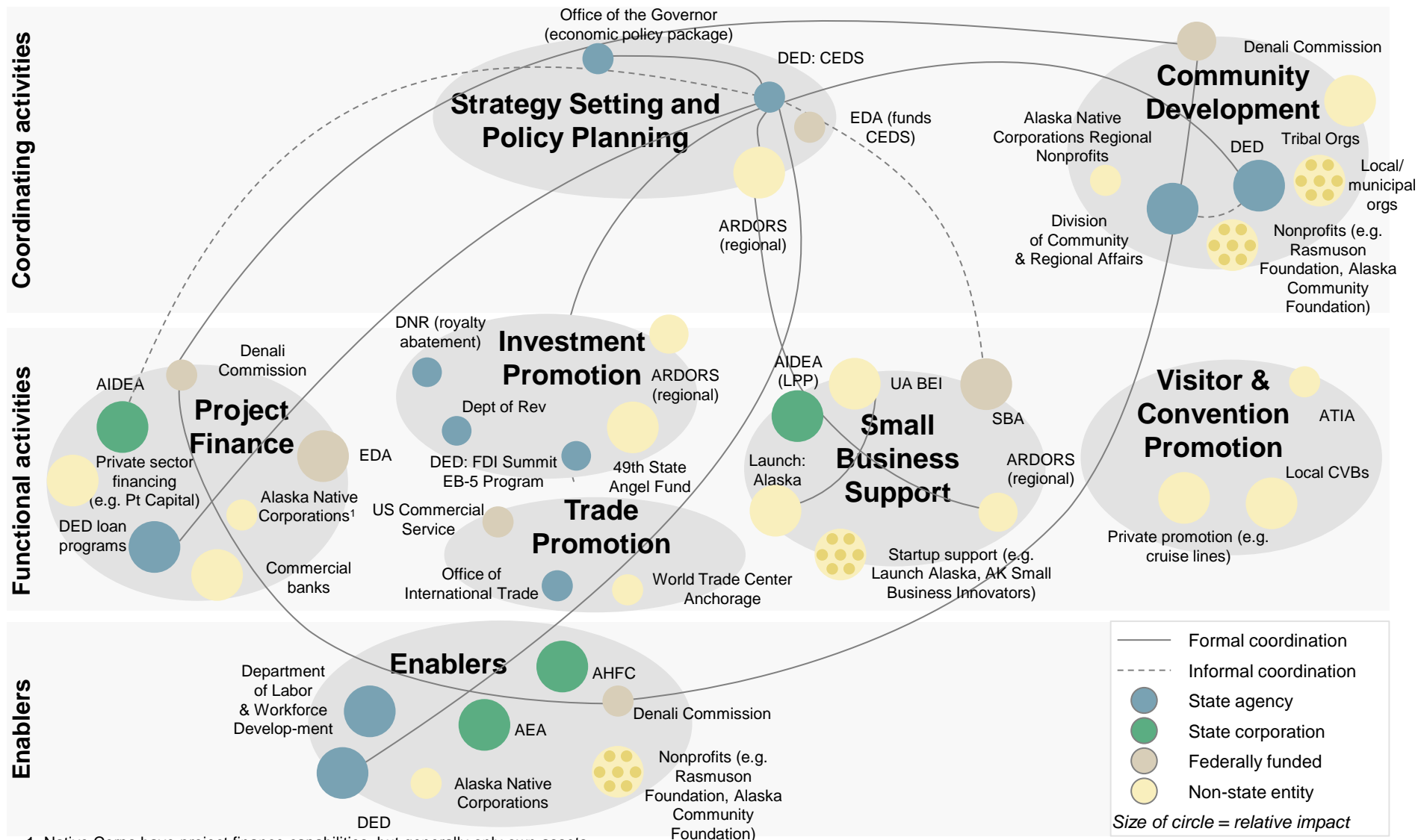
**Openness to private sector  
involvement**

**Native Corporations  
empowered by land base**

**Local knowledge of unique  
context and needs**

**Growing network of support  
for entrepreneurs**

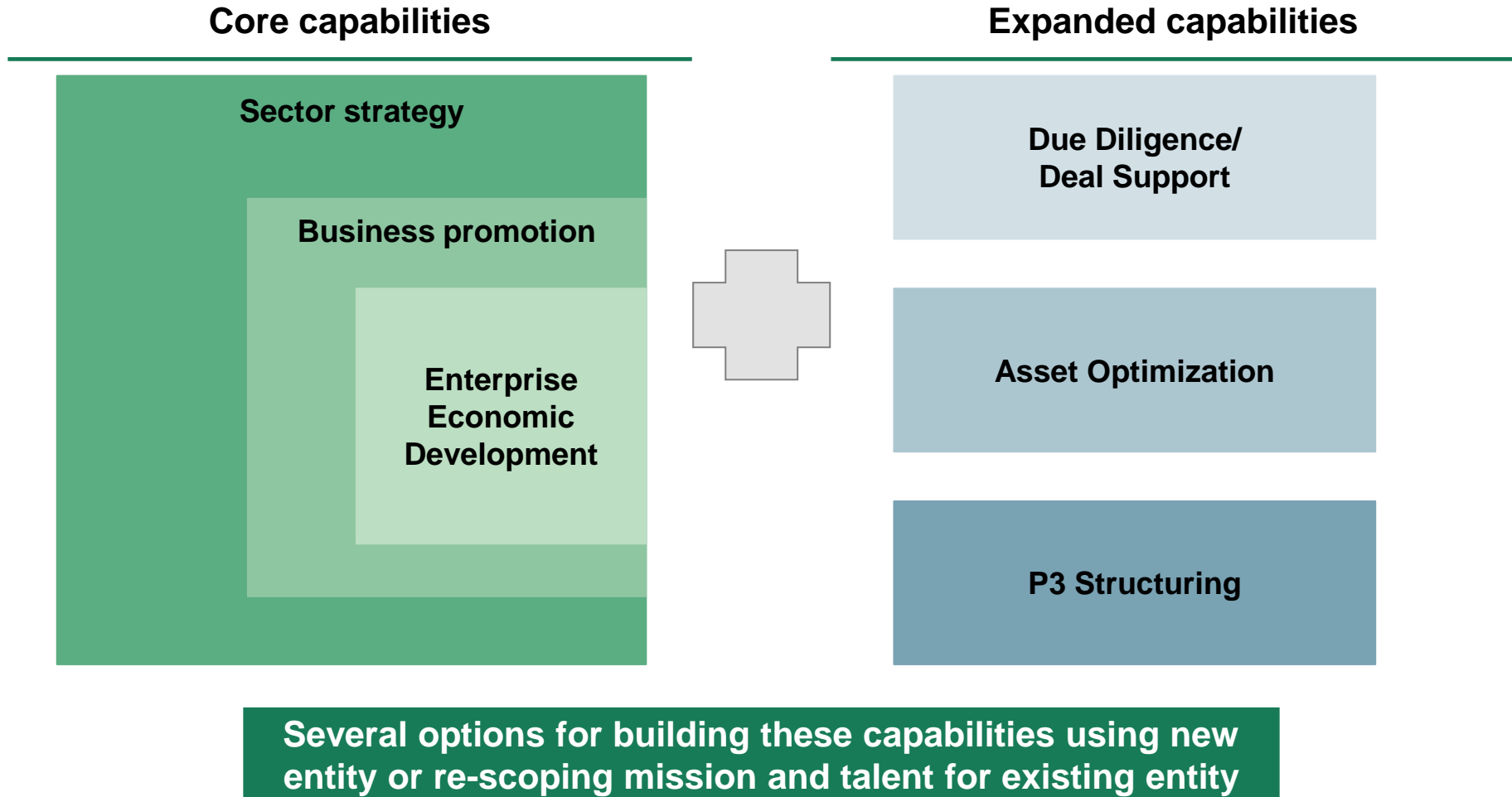
# Currently, Alaska's economic development efforts spread across many entities with need for greater coordination



1. Native Corps have project finance capabilities, but generally only own assets

Source: BCG analysis, Interviews, entity information

# To further support enterprise economic development success, Alaska should build additional capabilities



# Sector strategies can guide investment decisions and asset optimization, in coordinated effort across entities



## Identify vision, goals, and metrics for impact

- Define vision for economic development for the State
  - Different approaches to community vs. enterprise economic development
- Identify in which sectors does Alaska have the "right to win"
- Understand what is required to access these opportunities-- what are the barriers?
- Clarify policy priorities overall, across sectors
- Establish metrics to measure success



## Roadmap investment and implementation

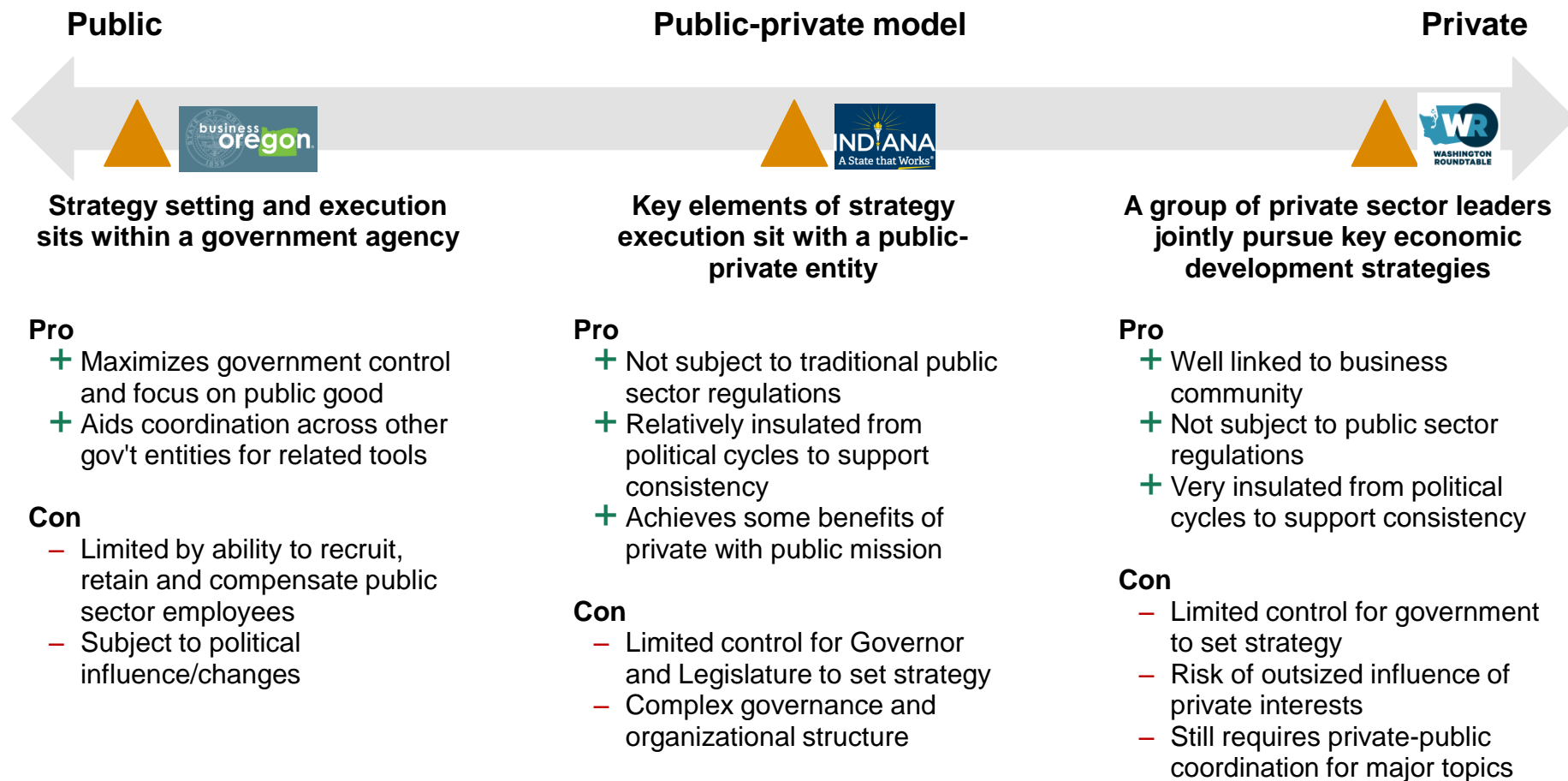
- Review agency activity to drive strong coordination and align any role changes required
- Designate Czars to coordinate in key sectors
- Create implementation task for ownership and accountability
- Consistent messaging and communication plan
- Identify and nurture strong talent and professionalism
- Focus on creating culture of effectiveness
- Identify cross-cutting investments in infrastructure or changes to fiscal strategy to support long term competitiveness








## Detail individual sector strategies

- Clear definition of Alaska's right to win and business case for success in each sector
- For each sector, overall context and trends--what's changing and creating opportunity?
- Understand and define plan to solve for required "enablers" required by sector (e.g., talent, energy, infrastructure)
- Identify what the government needs to do differently (e.g., investments, legal / regulatory changes)
- Identify specific potential target companies and value proposition
- Estimate and track potential impact (growth, jobs, etc)




# A range of models between public and private for building this "ecosystem" of entities



# Review of State economic development approaches provides key lessons to optimize institutional environment

Lesson	Current state in Alaska	Example
<b>1 Develop sector strategy based on long-term, sustainable vision</b>	<ul style="list-style-type: none"> <li>Lack of coordinated approach to economic development</li> <li>Limited resourcing and capability to execute on strategy</li> <li>Fragmented strategic efforts at regional and local levels</li> </ul>	
<b>2 Adopt private sector management practices to the fullest extent possible</b>	<ul style="list-style-type: none"> <li>Heavy public sector / appointee representation on Board for state corporations</li> <li>Inability to attract and incentivize employees through private sector compensation</li> </ul>	
<b>3 Insulate economic development from political interference</b>	<ul style="list-style-type: none"> <li>Fluctuating resources for economic development efforts with administration changes and political context</li> <li>Legislatively mandated projects and efforts prevent focus on cohesive long-term strategy</li> </ul>	
<b>4 Coordinate activities to ensure alignment and avoid redundancy</b>	<ul style="list-style-type: none"> <li>Similar capabilities in functional roles across entities</li> <li>Strong regional coordination through ARDOR program, but limited state-wide coordination of Federal, State, non-profit, and private efforts</li> </ul>	
<b>5 Provide a consistent 'storefront' to potential investors</b>	<ul style="list-style-type: none"> <li>Fragmented resources and access for businesses</li> <li>Existing gap in external knowledge of Alaska</li> <li>Strong Alaskan network enables organic coordination of processes</li> </ul>	

# Given Alaska's ownership of key assets, we also looked at examples overseas and nation-level models

Lesson	Current state in Alaska	Example
<b>6 Comprehensive sector strategies with tightly coordinated incentives</b>	<ul style="list-style-type: none"> <li>Sector strategies are determined by agencies on an ad-hoc basis</li> <li>Incentives and regulations targeted to companies are not well coordinated with sector-level plans</li> </ul>	
<b>7 Coordinated sector strategies, investment and P3</b>	<ul style="list-style-type: none"> <li>Sector strategies do not drive asset management decisions</li> <li>Limited P3 experience and capacity</li> </ul>	
<b>8 Leverage strengths to develop P3s and engage private sector</b>	<ul style="list-style-type: none"> <li>Alaska similar advantages of local knowledge, patient capital, and creative financing ability</li> <li>Opportunity to leverage strengths to engage private sector, P3s, and source projects</li> </ul>	



# Competitor states actively leveraging a broader toolkit of economic development incentives

## Alaska



## Competitor states

### Job creation



No general job creation credit exists



**Arizona** – \$3k per new job for each of first three years, up to 400 employees



**North Carolina** – 3.5% of new payroll for the first 8 years of employment

### Job training



Offers support through an apprenticeship program (must be federally recognized)



**Arizona** – 75% of new employees, 50% of current (\$5k urban / \$8k for rural)



**Virginia** – Reimburses 50% of training costs for 12-26 weeks of training

### Capital investment



No capital investment credit exists



**Arizona** – 10% of investment or \$20k per new job up to \$30M a year



**Kansas** – 10% of purchase/ lease of a facility (includes equip. moved to state)

### Property tax



First player in an industry can receive 100% abatement for 5 years



**Ohio** – 75% abatement available for 10 years

### Financing support



AIDEA can provide loans up to full cost of project at competitive rates



**South Dakota** – Fixed loans up to 45% of project cost, 20 years fixed at 2% interest



Strong general incentive



Targeted incentive



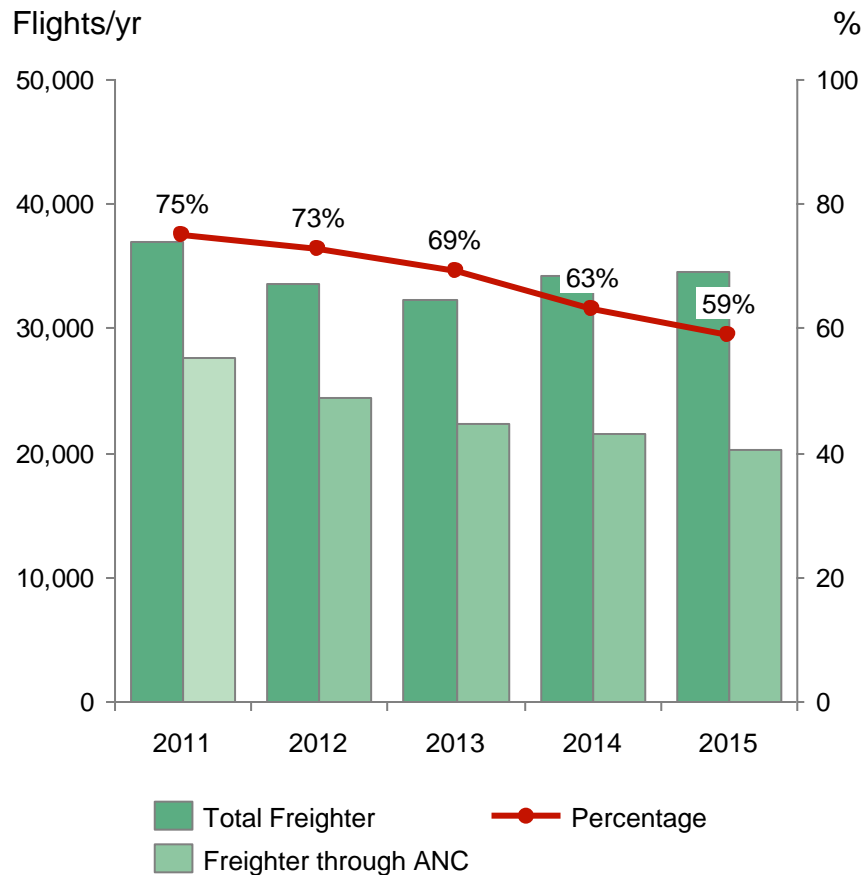
General incentive exists



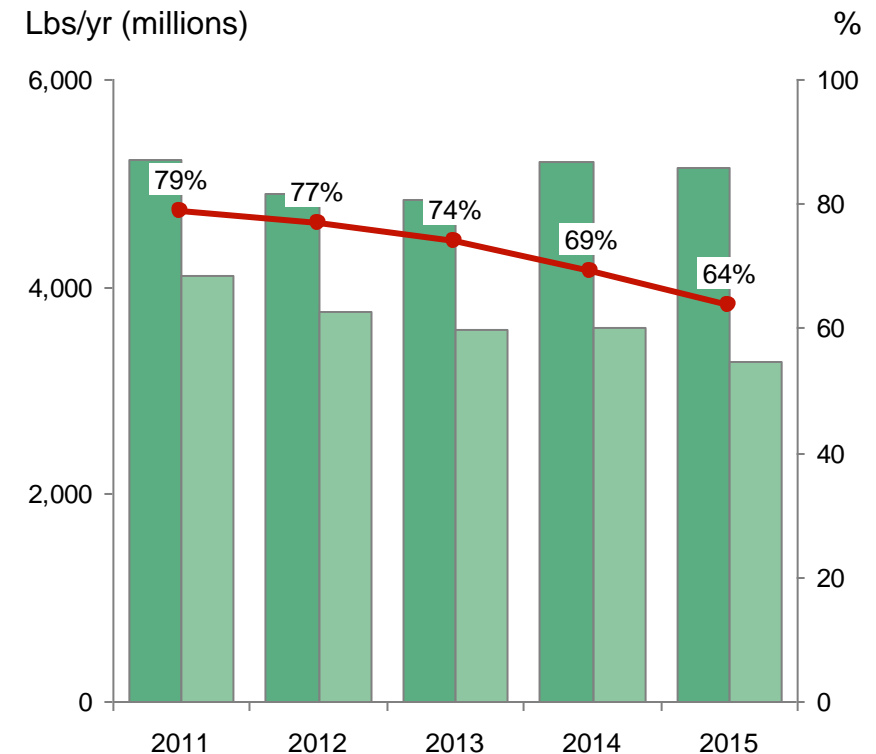
No general incentive

# Despite a commanding position and some natural advantages, ANC transit cargo market share is declining

## Market share by # flights<sup>1</sup>



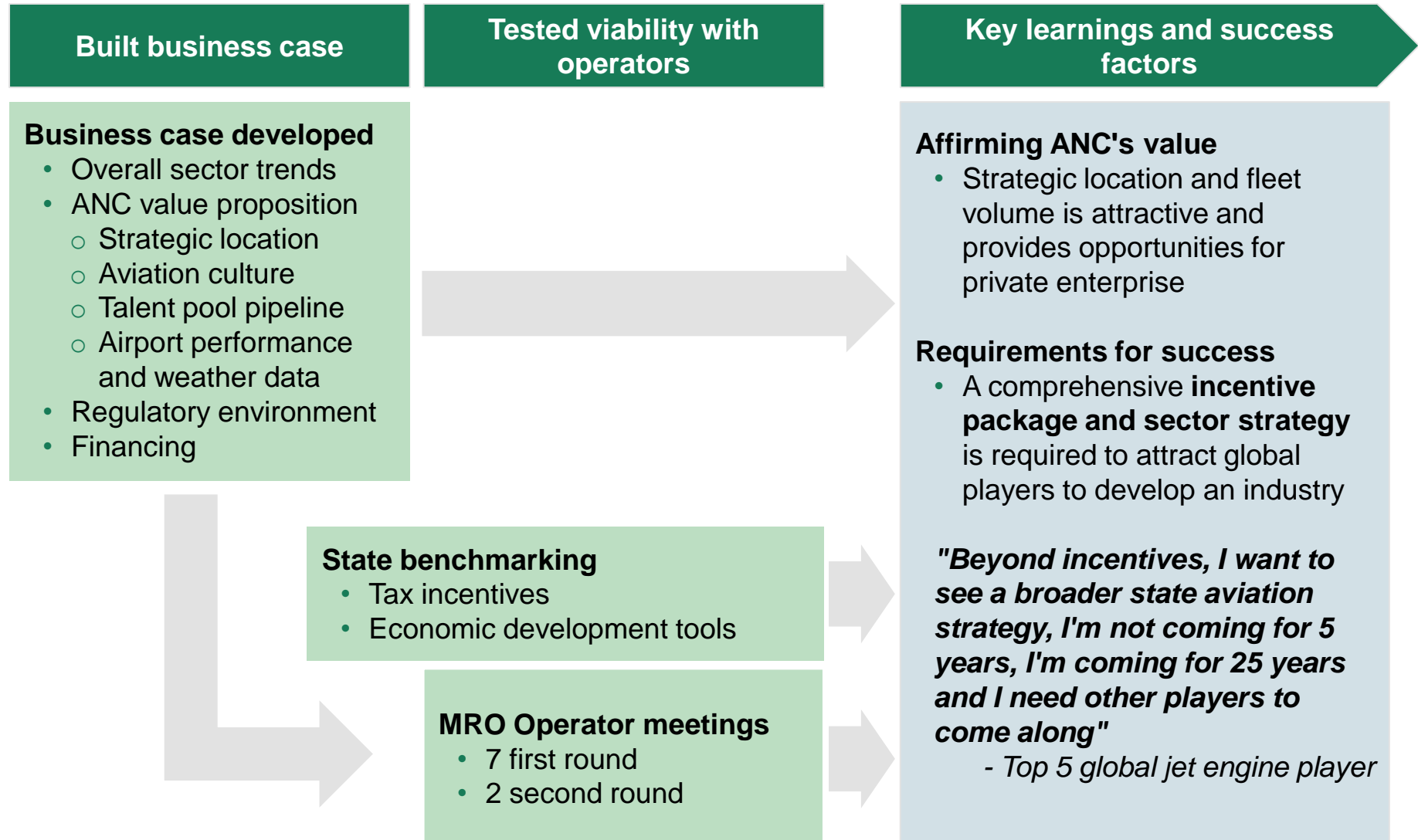
## Market share by lbs cargo



**Market share by cargo weight has declined less than by # of flights due to re-fleeting to more efficient aircraft and higher load factors**

1. Asian companies with flights include China, India, Indonesia, Japan, South Korea, Malaysia, Philippines, Russia, Thailand, Taiwan  
 Source: T100 DOT Data

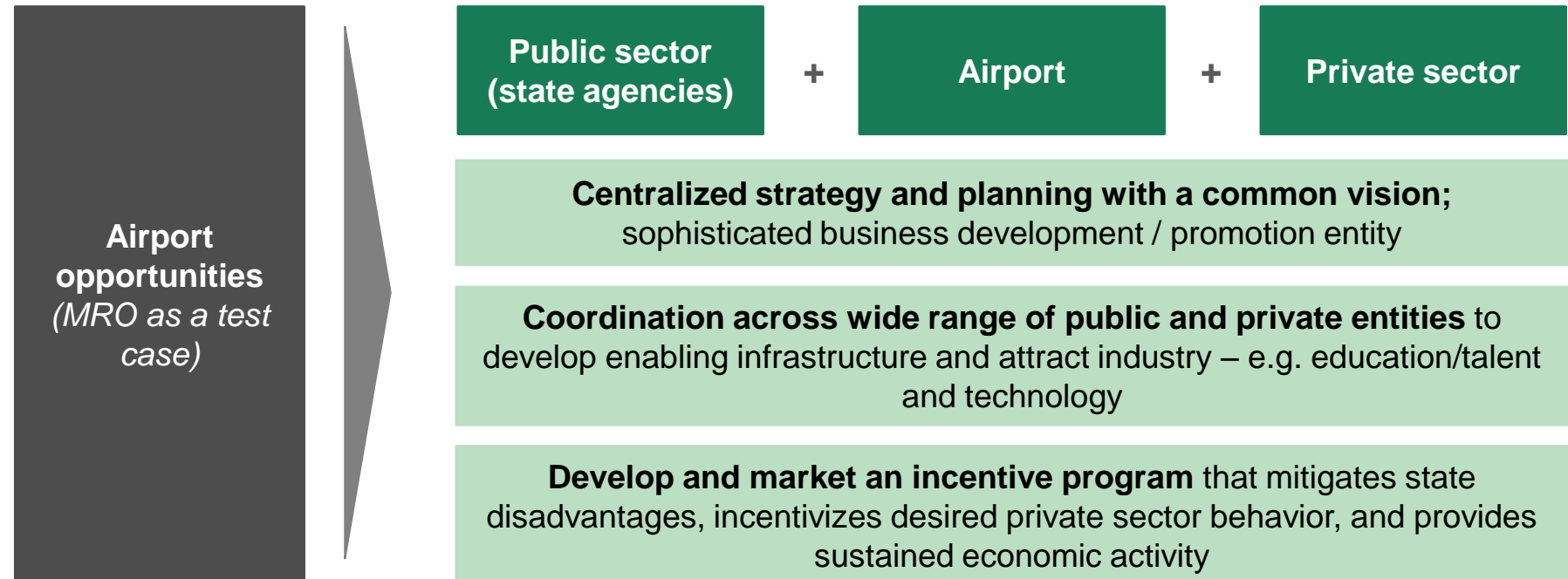
# We rigorously tested the business case for an aviation maintenance business as a path to reverse the decline



# A comprehensive approach for ANC is required to turn the tide on a challenged cargo business

While maintaining the passenger base, the substantial cargo business is losing market share on account of adverse external forces (~15% in the last five years)

There are opportunities to mitigate market pressures and turn the tide by developing ancillary businesses – but success is predicated on broader state engagement



# Alaska lags competitor states in job creation, training, and capital investment

☒ Strong general incentive
 ☒ Targeted incentive  
☒ General incentive exists
 ☐ No general incentive

State Category	State	General job creation credit	Training Support	Capital investment	Property tax Break	Financing Support	Targeted Industries
Overall	AK		<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
MRO locations	AZ	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	CA		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	Yes
	FL	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	Yes
	KS	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	OH	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	SC	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	TX	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	WA	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
Top Business Friendly States Regulatory Environment (CNBC Rank)	NH	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>			<input checked="" type="checkbox"/>	Yes
	SD		<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	VA	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	Yes
	ND	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
Overall Business Attraction (All factors)	UT	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	CO	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes
	NC	<input checked="" type="checkbox"/>		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Yes

Note: Top business friendly states sourced from CNBC regulatory freedom rankings, Top overall business attraction includes all factors (including non-regulatory) from CNBC and Forbes rankings

# Many competitor states have MRO or aviation specific incentives

State	Incentive Type	Description
Colorado	Corporate tax credit	\$1,200 in corporate income tax credit for each new employee involved in the maintenance, repair, modification or completion of aircraft (within Aviation Development Zones)
Washington	Sales tax credit	Tax refund for any taxes paid on labor, services, or materials required to construct an aircraft maintenance facility
	Various tax credits/reductions	Five additional incentives that reduce corporate tax, property tax, and sales/use tax for aerospace companies and manufacturers
Ohio	Job creation credit	A 1.26% payroll credit given to StandardAero, created 120 new jobs at \$5M in payroll and retained \$26M for a credit worth ~\$350k
Oklahoma	Corporate tax credit	Up to \$12,500 in tax credit for each aerospace engineer hired
	Personal tax credit	Up to \$5,000 in tax credit for the hired aerospace engineers for personal taxes paid in first year of employment
North Carolina	Growing Business credits	All growing business credits are only available to 10 target industries, one of which is "aircraft maintenance and repair"

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# Summary of AHFC findings

## **AHFC activities are largely in line with other housing authorities, apart from few exceptions**

- Mortgage financing, grants and subsidies, public housing are common programs for housing authorities
- Energy programs administration is common in housing authorities; research programs are less common and their need is likely driven by Alaska's unique climate

## **AHFC plays an effective role in mortgage financing by providing loans to thousands of Alaskans**

- AHFC plays an active role in the secondary mortgage financing market, in line with peers
  - US housing authorities in 43 of 50 states play in the secondary mortgage market
- AHFC outsources loan servicing, paying high rates driven by higher than average price of Alaskan homes and the "high-touch" servicing" offered
- Among the lowest foreclosure rates in the United States”, and “Dividends totaling nearly \$2 billion in the last 25 years.”

## **AHFC balance sheet has significant assets, and low debt to leverage ratio**

- ~\$3B in mortgage assets, pledged against bonds
  - ~\$500 million in annual mortgage activity
- AHFC maintains ~\$740M in capital restricted to operational use ; this rate in line with benchmarks

## **Dividends totaling nearly \$2 billion in the last 27 years**



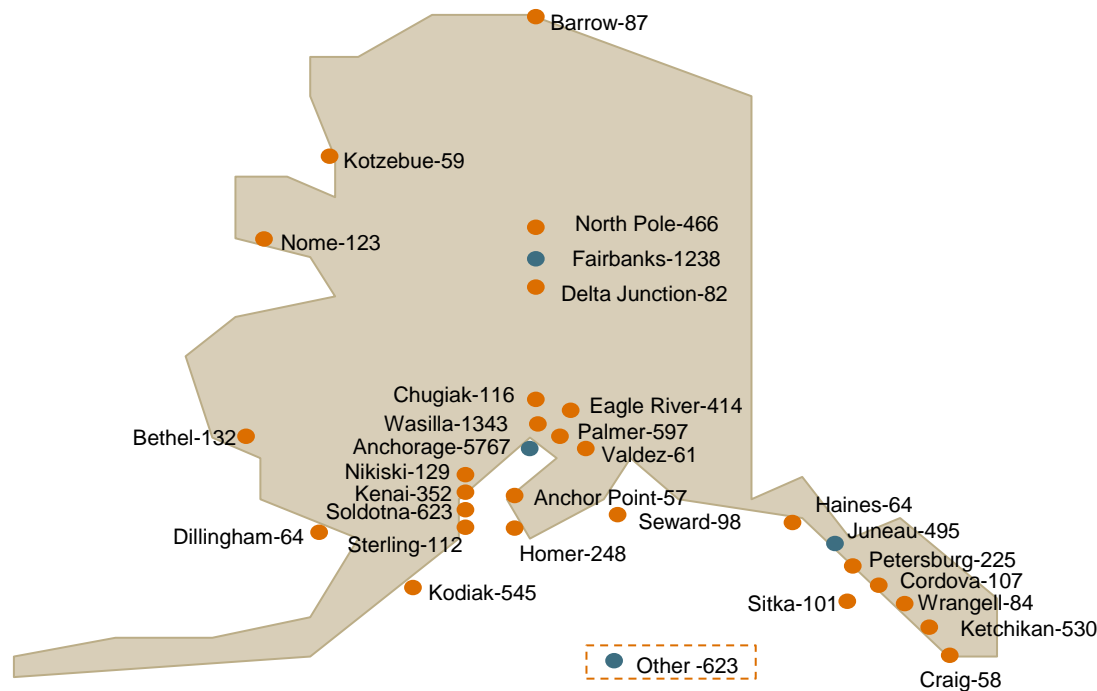
## Context: AHFC focuses on delivery of four main programs

**AHFC's mission is to provide Alaskans with access to safe, quality, affordable housing through delivery of 4 main programs**

- **Mortgage financing**
  - Provides mortgages to ~1,800 Alaskans annually
  - 50% of mortgages focused on rural Alaska
  - Financially self-sustainable through issuance of bonds
  - Subsidizes other programs within AHFC
- **Public Housing**
  - Public housing for ~10,000 Alaskans through 1,612 units & 4,307 vouchers in 29 different sites
  - Federally-funded program
  - Employee ~50% of AHFC staff
- **Grants and subsidies**
  - Competitive funding awarded to non-profits and developers to increase affordable housing in AK
  - Combines AHFC financing, federal and state funds, philanthropic grants, & tax credits
- **Energy efficiency programs**
  - ~6,800 units benefitted from weatherization program, and 10,000 Alaskan benefited from rebates
  - Estimated 30% savings on energy bills

# AHFC serves a broad geography with mortgage products; major focus on rural areas

## AHFC's mortgages by location



## Comments

**Overall, AHFC operates in 114 communities, towns, and/or cities in Alaska**

**Activity of loan portfolio in rural areas twice as much as urban area (relative to population)**

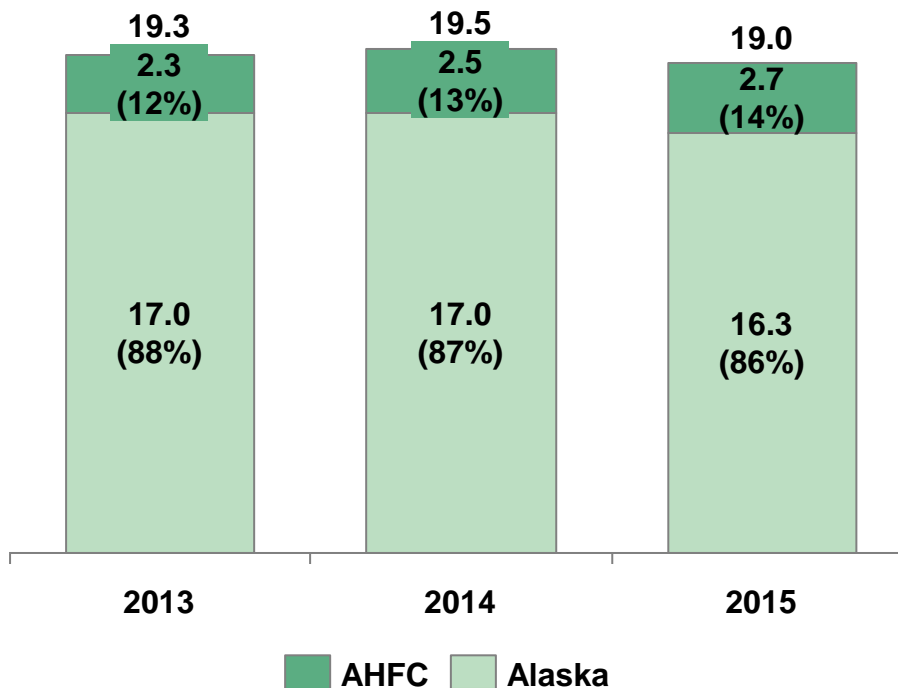
- ~50% of loans in rural areas
- ~30% of Alaska population live in rural areas

Note: 623 mortgages in 84 different locations classified as "other"  
Source: AHFC Mortgage division, BCG analysis

# Alaska's mortgage finance market estimated at ~\$20B, with AHFC commanding ~14% market share

## ESTIMATED FIGURES

### Alaska mortgage market (\$B)



### Comments

**AHFC market share consistently 13-14% for past 3 years<sup>1</sup>**

- AHFC plays in the secondary market space along with other GSEs (e.g. Ginnie Mae, Freddie Mac, Fannie Mae, etc..)

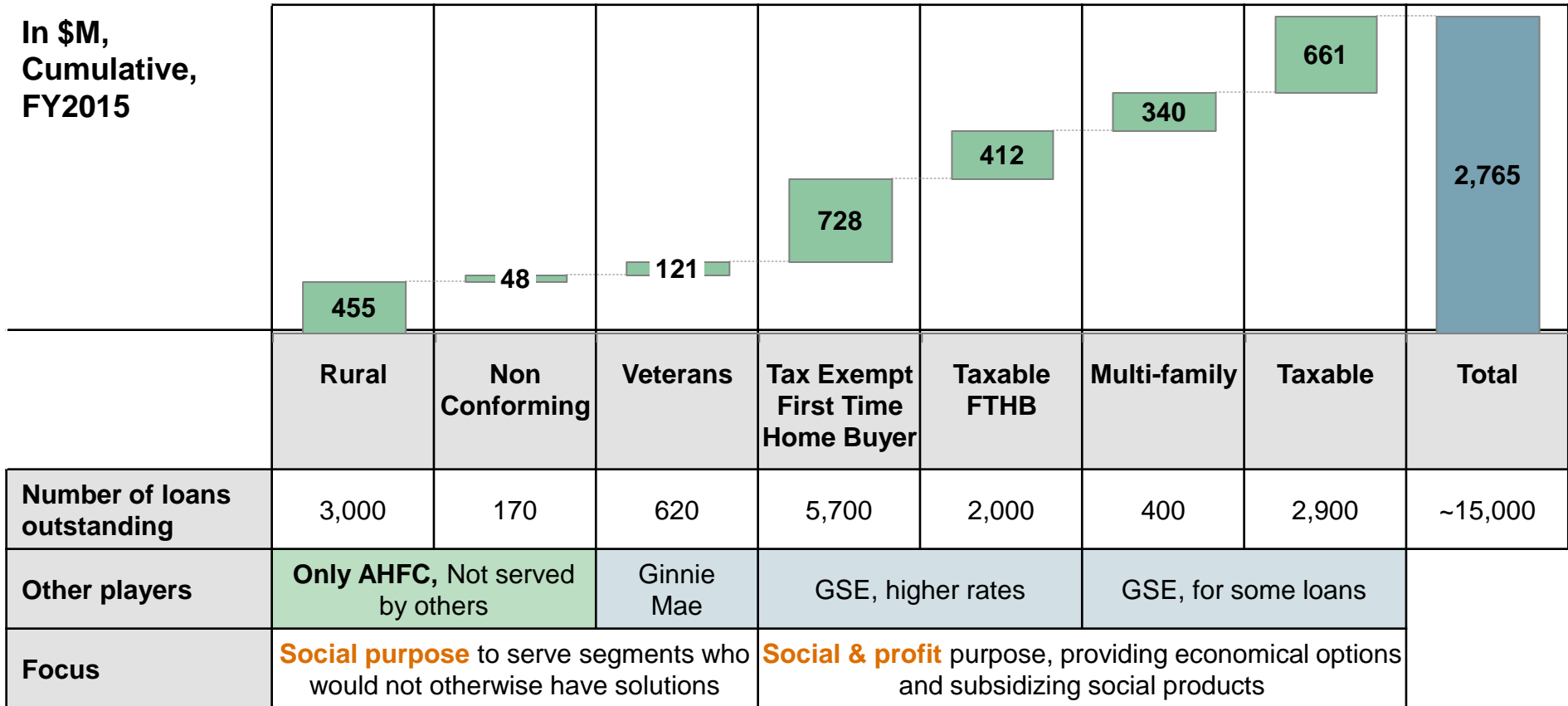
**AHFC's core objectives are to contribute to the housing market stability and provide housing options for Alaskans**

**AHFC does not compete with, but complements, the role of banks because it does not play a role in origination**

**AHFC market share consistent over past 3 years**

1. 10% of mortgages are assumed to be refinancing  
Source: SNL, AHFC reports, BCG analysis

# AHFC serves seven groups, five of which may qualify for GSE loans but find more value in AHFC products



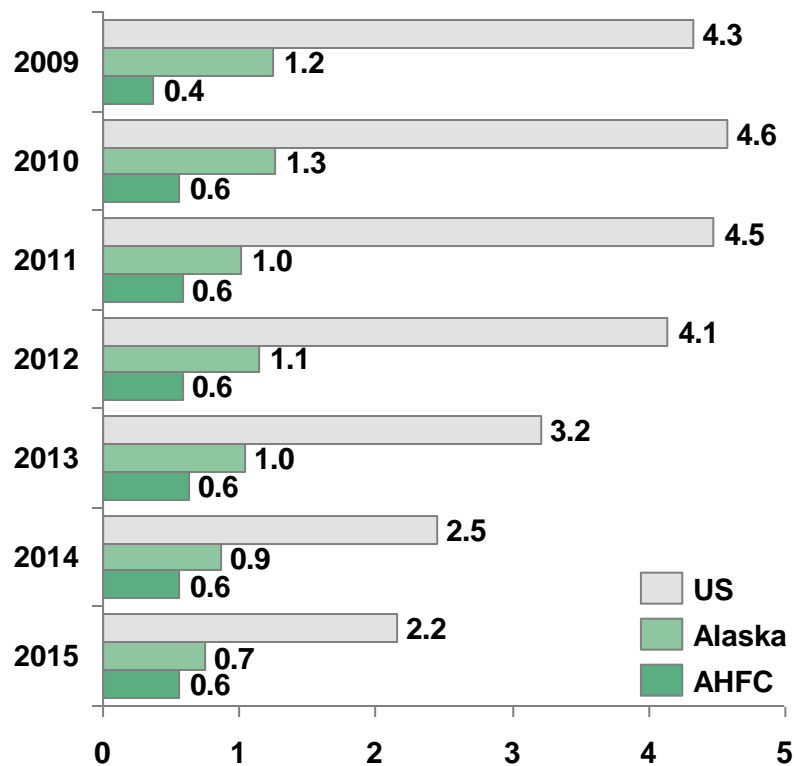
AHFC is able to offer a lower rate than GSEs for some loans, without AHFC some of these customers would likely be priced out of the market

Note: AHFC has a social responsibility to support all other segments. AHFC is also more lenient in collections and servicing practices.

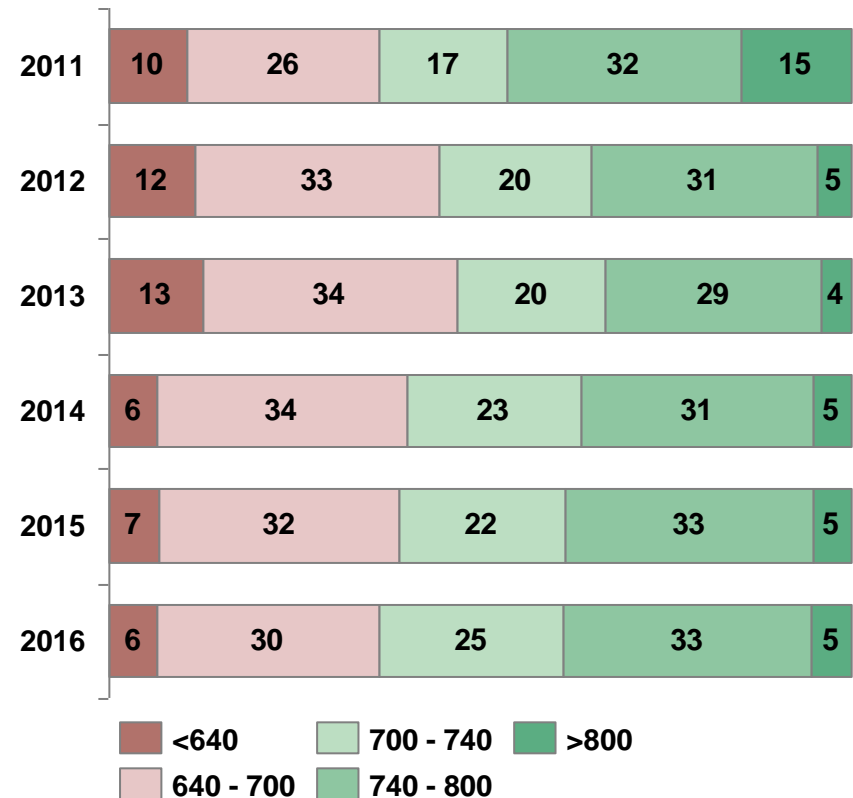
Source: AHFC Mortgage division, BCG analysis

# AHFC's choice of "high touch" servicing may contribute to lower foreclosure rates and a balanced risk portfolio

## AHFC has low foreclosure rates compared to Alaska and US averages



## While serving a balanced risk portfolio



# AHFC's role in mortgage financing should be maintained to ensure the continuation of associated benefits

## Access to home ownership

### Continue serving 1,800 Alaskans annually through mortgages

- Better rates to an "underserved" market
- Provides access to those that otherwise couldn't get loans

## Consistent flow of funds to Alaska

### Provide constant payback to Alaska government through

- dividend payment totaling \$2B over time, representing 2x return on initial investment

## Subsidizing other social programs

### Subsidize Public Housing and some other programs

## Contribution to economy

### Stabilize economy & contribute to GDP

- Housing contributes 3%-5% to GDP
- Homeowner equity traditional source of collateral for SME (SMEs make 54% of AK economy)

## Help keep Alaskans in Alaska

### Avoid exacerbating the existing negative "net migration"

- "net migration" close to 8K, highest since 1988

## Create jobs

### Provide direct/ indirect jobs to many Alaskans

## Other

### Other societal impact

- Stable housing contributes to an average of 20 point increase on standardized reading tests for children (when compared to unstable housing)

**AHFC's role mortgage financing is beneficial to Alaskans and to Alaska's socio-economic wellbeing**

# AHFC delivers ~50 different programs...

Detailed activity review in appendix (figures as of 2016)



## Loans & Mortgages

- Tax-Exempt FTHB (~\$80M)
- Taxable FTHB (~\$93M)
- Taxable Loans (~\$172M)
- Rural Loans (~\$53M)
- Non-Conforming Loans (~\$12M)
- Veterans Loans (~\$7M)
- Refinance (~\$7M)
- Multi-family Loans (~\$29M)
- CCAP (~\$4M)
- Second Mortgage (~\$1M)
- Mobile Home (\$0)

### Attachments to loans

- Interest Rate Reduction for Low Income Borrower
- Energy Efficiency Interest Rate Reduction

### Multi family loan programs

- Senior Housing Loan (MF)
- Assistance Provider Interest Rate Reduction (MF)
- Association Loan (MF)
- Multi-Family, Special Needs, and Congregate Housing (MF)
- Loans to Sponsors (MF)



## Grants and Subsidies

- Senior Citizens Housing Development (~\$4M)
- Home Investment Partnership Act<sup>1</sup> (~\$6M)
- Housing Opportunities for People with AIDS (HOPWA) (~\$600K)
- Special Needs Housing (~\$600K)
- Homeless Assistance Grant (~\$7M)
- Emergency Solutions Grant (~\$300K)
- HUD Continuum of Care<sup>2</sup> (~\$2M)
- USDA Housing Preservation Grant (\$0)
- National Housing Trust Fund (\$0)
- Teacher, Health & Public Safety Housing (~\$6M)
- Low-Income Housing Tax Credit (~\$26M non cash)



## Public Housing

### Moving to Work

- Housing Choice Voucher<sup>3</sup> (~\$35M)
- Empowering Choice Voucher (~\$2M)
- Veterans Administration Supportive Housing (~\$1.5M)
- Karluk Manor – housing first project based vouchers
- Conventional Low Rent Housing Program (~\$10M)
- Capital Fund program (~\$5M)

### Support

- Gateway Literacy
- Family Self-Sufficiency (~\$200K)
- Section 8 Moderate Rehab Program (~\$500K)
- Section 8 New Construction Program (~\$2M)



## Energy Program

- Weatherization (~\$39M)
- Home Energy Rebate (~\$19M)
- Supplemental Housing Development (~\$7M)
- Low-Income Home Energy Assistance (~\$80K)
- Interest Rate Reduction for Energy Efficiency (\$0)
- Cold climate Housing Research Center (\$0)
- Energy Efficiency Revolving Loan (\$0)
- Building Energy Efficiency Standards (~\$400K)
- Research and Information Center (~\$600K)
- Builder & Rater Education Program (\$0)
- Consumer Education Program (~\$660K)

● Federal    ● State    ● Corporate Funds

1. Includes Home Opportunity Program (HOP), Owner Occupied Rehab Program (ORP), Homeownership Development Program, Goal Program, & Tenants Based Rental Assistance (TBRA) 2. includes Short Term Rental Assistance, Shelter plus Care, and Supportive Housing Program 3. Includes Service Coordination of Public Housing Agencies, Mental Health Voucher Program, & Gateway Literacy Programs

Source: AHFC data (actual 2015 spend), interviews, BCG analysis

# Three state funding grant programs provide important social benefit to Alaskans at low cost as of FY17

## Overview

## Impact/ details

### Senior Citizens Housing Development

Funding to incentivize construction of new senior housing and modify existing housing for accessibility

- Growing senior population in AK
- Last resort for senior Alaskans to live independently
- Budget reduced to \$3.5M in FY2017

### Homeless Assistance Grant

Used to provide operating assistance, temporary rental assistance, and prevention/intervention programming for ~13,000 homeless Alaskan per year

- Associated with 61% reduction in recidivism
- Budget unchanged at \$7.7M in FY2017

### Teacher, Health & Public Safety Housing

Funding to support construction of rural housing for teachers and other civil servants

- Critical program to incentivize teachers to live in rural areas
- Budget reduced to \$1.65M in FY2017, of which 650K from private donation



# AHFC recommendations

	Recommendation	Details and rationale
1	<b>Continue mortgage financing role in support of local housing market</b>	<ul style="list-style-type: none"> <li>• Clear social value - builds on Alaska's social well-being/economic stability</li> <li>• Self funded, does not require state budget</li> <li>• Profitable, results in dividends to the state</li> <li>• Potential to add programs to strengthen offering to Alaskans               <ul style="list-style-type: none"> <li>– Convert to rental for delinquent borrowers</li> <li>– Repurposing foreclosed assets either to public housing or other economic development purposes</li> </ul> </li> </ul>
2	<b>Continue public housing grants &amp; subsidies service provision</b>	<ul style="list-style-type: none"> <li>• Maintain important public housing and grants and services programs               <ul style="list-style-type: none"> <li>– Mostly federal funds – requires minimal state funding/budget</li> <li>– Provides sizable social support to those in need</li> <li>– In line with roles of other housing authorities</li> </ul> </li> </ul>
3	<b>Streamline &amp; tighten energy efficiency efforts</b>	<ul style="list-style-type: none"> <li>• Return rebate program budget residual to state               <ul style="list-style-type: none"> <li>– Potential to return budget back to state ~\$12M</li> </ul> </li> <li>• See materials in AEA section related to recommendations</li> </ul>
4	<b>Integrate AEA under AHFC to better provide comprehensive community development services</b>	<ul style="list-style-type: none"> <li>• See materials in AEA section related to recommendations</li> </ul>

# Agenda

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Project overview

Economic development landscape

AHFC summary findings

**AEA summary findings**

AIDEA summary findings

Next steps

## Summary of findings

**AEA connects projects with no-cost/ low-cost financing; opportunity to better prioritize technologies moving forward**

- Recommend prioritized REF supported technologies, reducing from 17 to 5 core programs

**Three key pain points have been identified in processes followed by AEA programs for rural energy support and can be addressed to improve program sustainability**

- Financing programs are not focused on leveraging private capital; potential to foster a private market
- Technical and emergency assistance has not been coupled with requirements for beneficiaries or accountability measures
- Processes have opportunity to better diffuse knowledge across programs and trainees

**PCE subsidy provides relief from high electricity rates in rural Alaska; goals related to rural energy could be advanced by further linking the PCE programs to outcomes**

- Endowment could be used to finance investments in pursuit of lower long-term PCE payments
- Payment formula and eligibility criteria could encourage shift to lower-cost energy and regular O&M

**Changes to these critical programs require deep engagement with stakeholders to test potential solutions, we recommend engaging policymakers, communities, utilities and potential contractors**

**We recommend AEA's core functions should be preserved; there is opportunity for efficiency gains through both co-location and partial or full consolidation with another agency (e.g. AHFC)**

# Approach to recommendations

Four guiding principles to build AEA recommendations

## Carry forward AEA's contribution to rural Alaska

*It is important to find a way forward for AEA's activities; many are critical to meeting the energy needs of Alaska*

## Minimize spend and establish sustainable funding model

*Given budgetary challenges confronting Alaska, key priorities are to reduce spending and establish sustainable funding model*

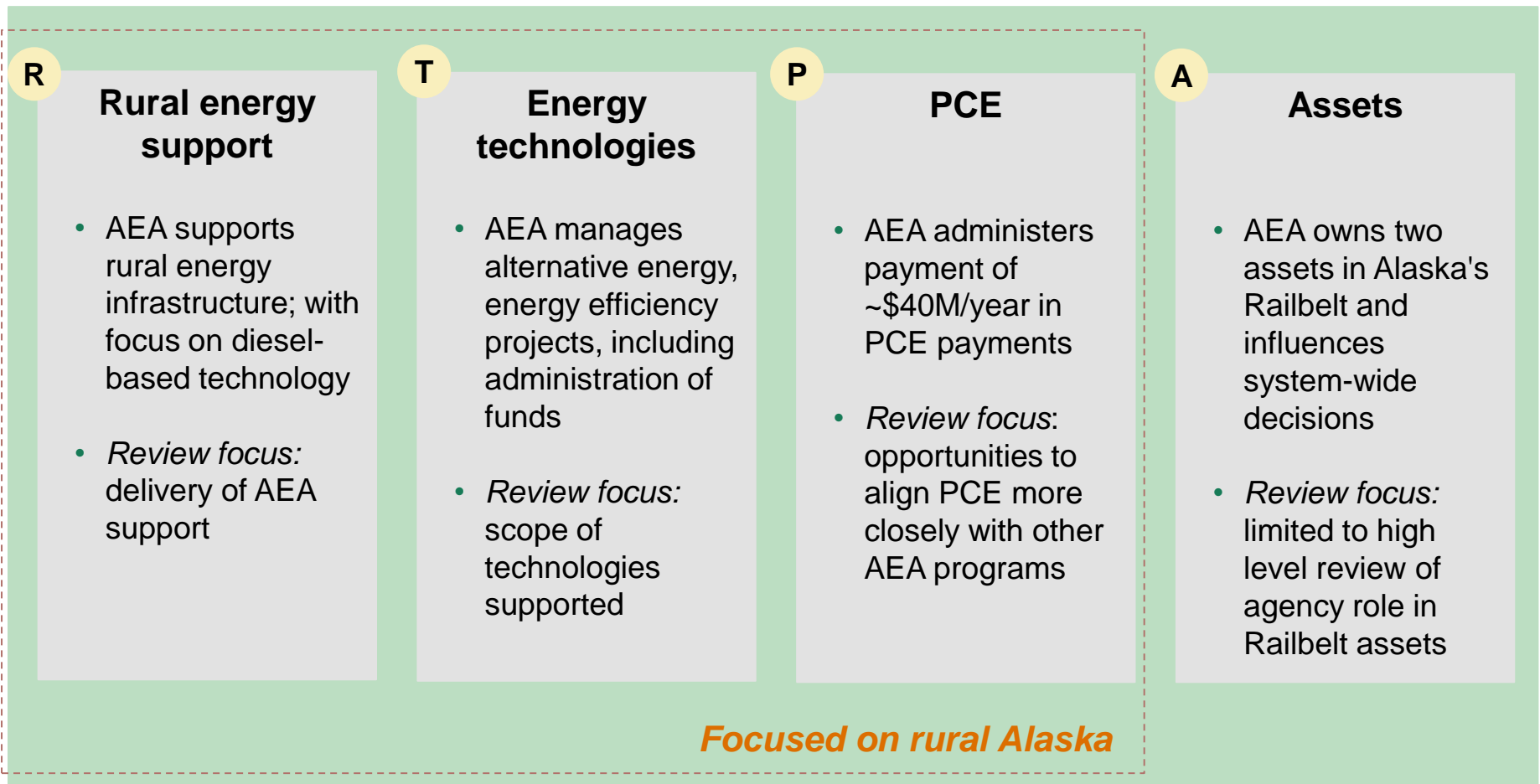
## Broaden the financial toolkit used by AEA

*AEA should shift financing support from grant to loan funding and introduce other types of assistance (e.g., loan guarantees and risk sharing)*

## 'Double-down' on areas of core expertise

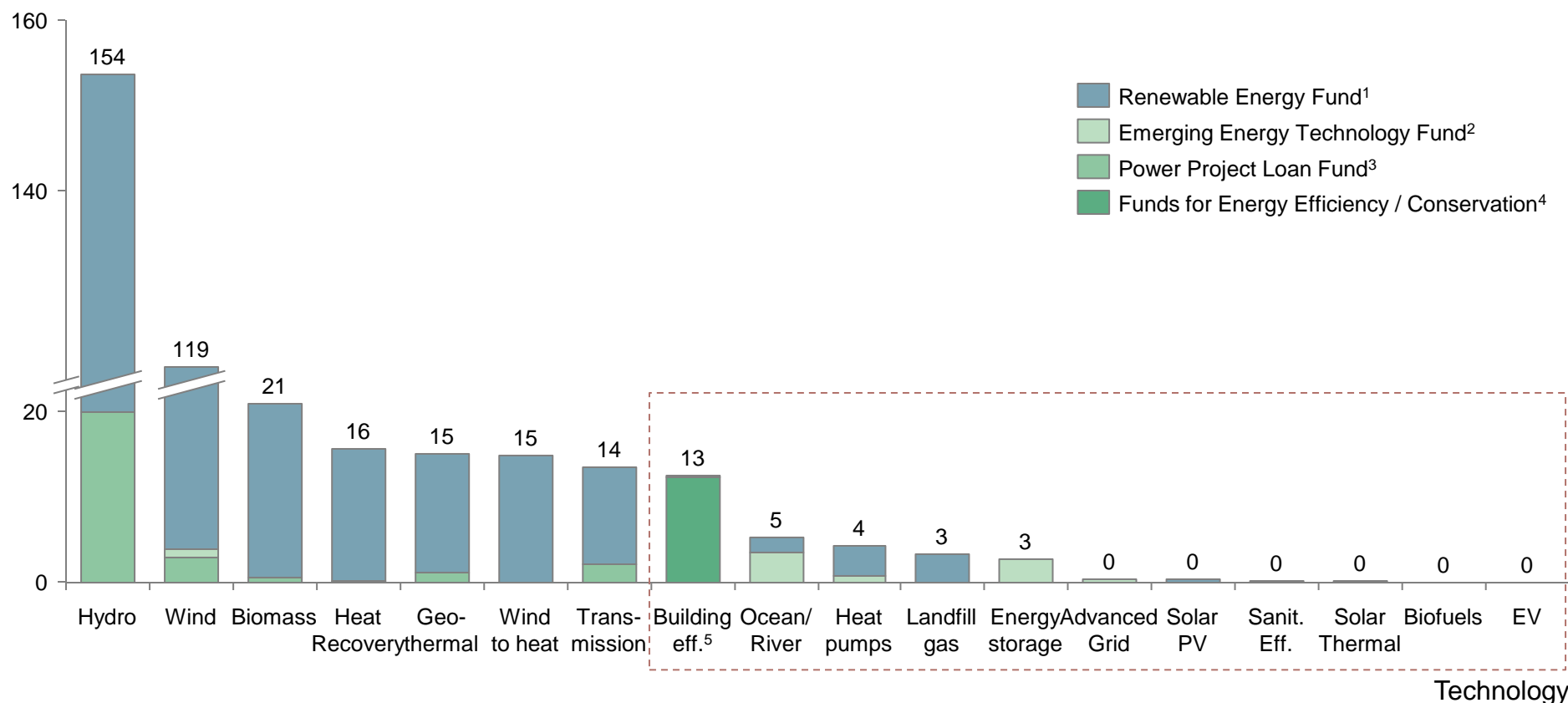
*AEA should focus on areas in which it has core expertise and a competitive advantage (e.g. role as an information provider)*

## Review covers four areas of AEA activities



# Energy technology funding through REF has been fragmented, creating a 'long tail' of supported technologies

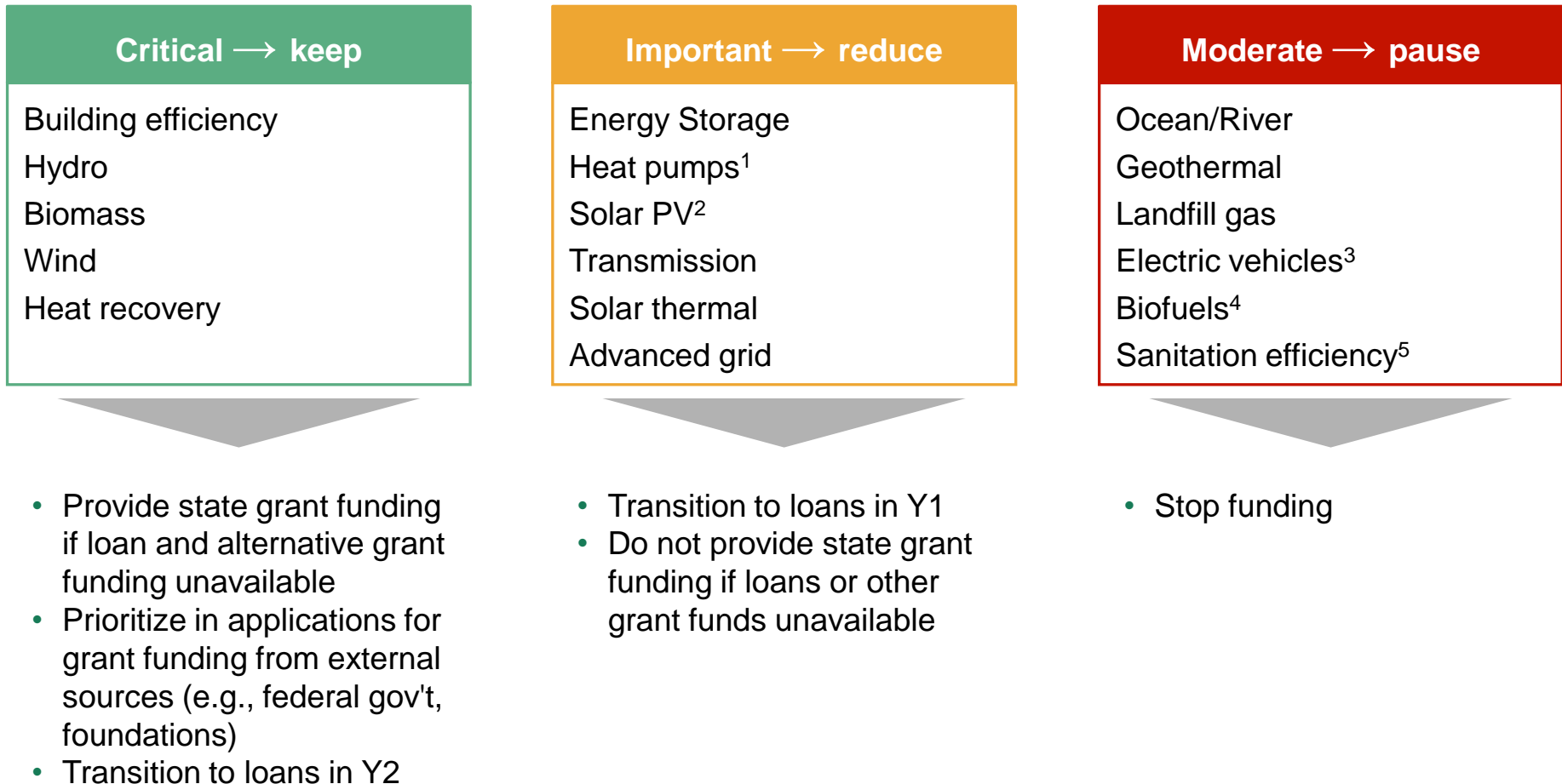
Total Funding (\$M)



1. Total funding for REF-supported projects as of 7/27/2016 was ~\$335M, excluding one cross-technology grant from the REF and one grant from the REF labeled with "other" technology; on EETF; 2. Total funding for EETF-supported projects as of 5/9/2016 was ~\$10M. Includes actual expenses and encumbrances; 3. Includes amounts disbursed as of 8/2/2016. Support for diesel, tank farms, and distribution is not included in funding count, since technologies are not supported by REF/ EETF and are supported by AEA's rural programs. Also does not include one natural gas project; 4. Includes funding for Village Energy Efficiency Program (VEEP), Remote Alaska Communities Energy Efficiency (RACEE) projects, AEA portion of State Energy Program (SEP) funds, Energy Efficiency Conservation Block Grants (EECBG), Commercial Energy Audits, Rural Sanitation Energy Efficiency, and DHSS Energy Efficiency Audits. Includes \$300K in encumbrances for VEEP Bristol Bay project. 5. Includes some community efficiency (e.g., street light replacements); funding for non-building and non-sanitation efficiency technologies are not broken out. Note: Eff.: efficiency, Sanit.: Sanitation, EV: Electric vehicles, PV: photovoltaic.

Source: AEA response to AO281; Alaska Energy Data Gateway; interviews with AEA staff; AEA documentation (PPF Historical by Technology; AEA EETF Funding by Project August 2016 and AEA EETF Encumbrances by Project August 2016; VEEP-SEP-EECBG-CBEA funding to date)

# Focus AEA support on prioritized, critical technologies as push to shift energy mix



1. Moved from "critical" given availability "off the shelf"; 2. Moved from "critical" given limited utility-scale applications; 3. Moved from "important" given low relevance to non-Railbelt Alaska; 4. Moved from "important" given limited relevance to non-Railbelt Alaska; 5. Moved from "important" given capabilities of other entities (e.g., Alaska Native Tribal Health Consortium)  
 Note: Y1—year 1 and Y2—year 2; Given technical similarities, wind to heat can be grouped with wind and/or heat recovery  
 Source: BCG

# Pain points facing rural programs imply potential to optimize value of AEA's support of rural Alaska

*Not exhaustive*

Process	Key pain points	Implications	Potential solutions
<b>RPSU/ BFU</b>	<ul style="list-style-type: none"> <li>Programs depend on grant funding</li> <li>Operation and maintenance of capital assets is not verified</li> <li>Limited input on investment needs received from other rural programs</li> </ul>	<ul style="list-style-type: none"> <li>Grants may "crowd out" private capital</li> <li>~15 – 20% of utilities rely on AEA for "last resort" support</li> <li>Assessment of utility/community needs may be outdated</li> </ul>	<ul style="list-style-type: none"> <li>Shift state support from grant to loan financing or tools to attract private financing (e.g., credit enhancement), where possible</li> <li>Amend reporting/application requirements (e.g., PCE, CR) to: <ul style="list-style-type: none"> <li>Verify O&amp;M, compliance with operational plan</li> <li>Assess investment needs</li> </ul> </li> </ul>
<b>Circuit Rider /ER</b>	<ul style="list-style-type: none"> <li>Incomplete knowledge flow from CR to other programs</li> <li>Support is not coupled with requirements for beneficiaries</li> </ul>	<ul style="list-style-type: none"> <li>Knowledge gained from CR/ER support does not contribute to capital investments planning</li> <li>Some utilities rely on AEA for "last resort" support</li> </ul>	<ul style="list-style-type: none"> <li>Log and share info. on utility requests, support provided, and O&amp;M performed</li> <li>Introduce incentives for O&amp;M compliance and reporting or penalties for non-performance</li> </ul>
<b>Training</b>	<ul style="list-style-type: none"> <li>Curriculum may be outdated</li> <li>Process ends after class delivery, opportunities for: <ul style="list-style-type: none"> <li>Program evaluation</li> <li>Peer network among trainees</li> <li>Incentives for continued skill development</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>Incomplete match between training and skills required in the field</li> <li>Reduces/removes: <ul style="list-style-type: none"> <li>Info. to improve program</li> <li>Spread of technical know-how across operators</li> <li>Investment in continuing education</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>Increase frequency of curriculum refresh, leverage data from CR/ER to identify training needs</li> <li>Facilitate network of utility operators</li> <li>Share utility performance benchmarks, provide incentives for more training<sup>1</sup></li> </ul>

1. E.g., award high performing utilities/operators with refunds on travel fees or course fees (if AEA/AVTEC begin charging for training programs).

Source: Interviews/workshops with AEA staff; BCG



# Potential exists to optimize value of PCE, a critical subsidy program that can be leveraged for sustainable energy use

## Findings

**AEA well positioned to assess energy needs of rural communities due to rigorous tracking of energy consumption data**

**Support for energy equity in Alaska differs from benchmarks:**

- Geography, instead of income, determines eligibility; reflects Alaska's geography and lower cost of power around Railbelt
- Utilities elsewhere include cross-subsidized rates for low-income customers

**Limited incentives associated with PCE to support AEA's mission**

- E.g., formula may yield lower PCE payments and higher effective rates if alternative/ renewable generation is installed

**Reporting requirements challenge rural communities**

## Takeaways

**PCE reduces the cost of energy to hundreds of Alaskan communities**

**Given technical expertise and knowledge base, agency with energy expertise is natural administrator of PCE**

**Potential to better link program to rural energy goals by optimizing incentives in eligibility requirements and formula, e.g.:**

- Apply endowment to finance investments that could lower long-term PCE payments
- Adjust payment formula to further encourage shift to lower-cost energy (e.g., via technologies, efficiency), performance of regular O&M

**Value of PCE program to end user may be further optimized**

- Potential to streamline end-user reporting and invest further in building capacity
- PCE is determine geographically vs by income distribution; opportunity to review

1. Subject to income distribution in non-Railbelt communities, and assumes share of high income individuals outside Railbelt is similar to that within Railbelt  
Source: Interviews with AEA staff and external experts; AEA data in response to AO 281; entity websites; AEA Power Cost Equalization Program Guide; RCA Sample Residential Bills for Electric Usage of 500 and 750 kWh as of June 30, 2015; Power Cost Equalization Funding Formula Review, March 2012 (ISER/NREL), Utility websites (e.g., National Grid, SMUD, SCE, PG&E); BCG analysis

# Critical to engage 4 key sets of stakeholders relevant to rural systems

<b>Policymakers &amp; Funders</b>	<b>Includes:</b> <ul style="list-style-type: none"> <li>• Alaska State Legislature</li> <li>• Federal agencies (e.g., U.S. DOE and USDA)</li> <li>• Communities</li> <li>• Denali Commission</li> </ul>
<b>Contractors</b>	<b>E.g., professional engineers, engineering design firms, etc.; provide:</b> <ul style="list-style-type: none"> <li>• Conceptual design and review, design, and construction of power systems/ bulk fuel storage facilities</li> <li>• Operations and maintenance of energy infrastructure</li> </ul>
<b>Communities</b>	<b>AEA rural programs interact with 200+ rural communities</b> <ul style="list-style-type: none"> <li>• Common for communities to have own power micro-grid and bulk fuel storage facilities</li> </ul>
<b>Utilities</b>	<b>AEA is the primary external source of technical expertise for ~100 rural utilities</b> <ul style="list-style-type: none"> <li>• ~60% high performers: larger communities or members of cooperatives with almost no support needed</li> <li>• ~25% average performers: require some assistance with maintenance</li> <li>• ~15% poor performers: require assistance on an ongoing basis</li> </ul>

Source: BCG; Sustainable Energy Solutions for Rural Alaska; AEA response to AO 281; AEA COO presentation to AEA Board (4/30/2015)

# Potential for strategic and financial benefit in consolidation of AEA and AHFC; suggest AIDEA maintain independence

**AO 281 included a mandate to review the potential for consolidation across AEA, AHFC and AIDEA**

**Any consolidation process should be governed by a few key principals:**

- Maintain core function and skills with greatest possible efficiency
- Minimize disruption in service
- Maximize transparency in all decisions

**Across all three agencies, there is opportunity for shared service integration and co-location to further drive savings**

**Our review found potential for strategic and financial benefit with the consolidation of AEA with an agency with a similar focus. We suggest AEA combine with AHFC for the following reasons:**

- Synergies with existing energy efficiency programs and shared services
- Leverage AHFC's access to capital markets and loan expertise for AEA programmatic work
- AHFC has been designated by US DoE as "Energy Agency" for Alaska, until it was passed to AEA; AHFC maintain 50% of funds from DoE
- Creating an entity that is able to more comprehensively address challenges in rural Alaska and capitalize on AHFC's presence and offices in rural Alaska
- AHFC looking into upgrading IT systems, making timing of integration ideal
- We estimate significant annual savings to support staff reduction following up front systems integration costs, which must be validated as a next step to proceed

**We recommend AIDEA remain independent – and separate from AEA – in order to focus management attention on development finance role**

# Technical energy programs under AEA and AHFC can be combined to achieve synergies

## Overview of AHFC energy programs

### Research and Information Center

- Public library located at HQ, with focus on energy efficiency within residential construction

### Builder & Rater Education Program

- Education provided for developing energy efficiency industry in Alaska

### Consumer Education Program

- Education provided for residential consumers of energy, specializing in "how-to's" for home improvements

### Cold Climate housing research center (Energy Efficiency Monitoring Research)

- Supports work of AHFC's residential energy efficiency programs, including partnership with CCHRC

### Energy Efficiency Revolving Loan Program

## Rationale for combining programs

### Technical programs that require detailed knowledge in energy efficiency

- Energy efficiency ranked by AEA as #1 technology in terms of impact and financial feasibility (i.e. alignment to AEA's mission)
- AEA staff can provide the required technical knowledge to maintain and improve the program

### Potential for synergies with existing AEA energy efficiency knowledge base

- AEA focuses on energy efficiency for non-residential buildings; potential for technical and human capital synergies following the merger

# AEA recommendations overview

	Recommendation	Details and rationale
1	<b>Strengthen energy planning functions to support community energy solutions</b>	<ul style="list-style-type: none"> <li>Support communities by providing perspective on most cost-effective energy solutions</li> </ul>
2	<b>Strengthen PCE with incentives linked to rural energy goals</b>	<ul style="list-style-type: none"> <li>Preserve core technical and financial linkages to rural energy and tech. programs</li> <li>Continue to identify process improvements</li> <li>Optimize incentives to shift to lower-cost energy (e.g., via technologies, efficiency) and to perform regular O&amp;M</li> </ul>
3	<b>Streamline technology assistance programs to prioritize ~5 key technologies (vs. 17)</b>	<ul style="list-style-type: none"> <li>Focus expertise on deployment (i.e., rely on others for R&amp;D) and cost effective, relatively proven technologies</li> <li>Prioritize build of technical expertise and availability of funding for 5 core technologies (building efficiency, hydro, biomass, wind, heat recovery), with "lighter touch" for 6 others</li> <li>Cease 6 technologies (ocean/river, geothermal, landfill gas, electric vehicles, biofuels, sanitation efficiency)</li> <li>Maintain grant funding to priority technologies for one year, and shift to loan financing for "light touch" technologies</li> <li>Reduce longer-term PCE costs with near-term investments</li> </ul>
4	<b>Build markets for private financing of rural energy infrastructure and O&amp;M, where feasible</b>	<p><b>Financing of rural energy infrastructure</b></p> <ul style="list-style-type: none"> <li>Support self-sufficiency and private-sector participation through greater use of loans/loan guarantees (vs. grants)</li> <li>Maximize use of state funding and leverage federal funding</li> <li>Leverage private-sector activity/expertise</li> </ul> <p><b>O&amp;M</b></p> <ul style="list-style-type: none"> <li>Address gap in capital maintenance, prevent 'fire fighting', and limit state liability/cost by potentially requiring utilities to join O&amp;M plans</li> <li>AEA to negotiate preventative/corrective O&amp;M plans with private-sector contractors, building local skills</li> <li>AEA to provide technical assistance as a paid service and expertise for emergency response (e.g., floods)</li> </ul>
5	<b>Determine future of Railbelt ecosystem</b>	<ul style="list-style-type: none"> <li>Prior step to taking any action on Bradley Lake Hydro, Alaska Intertie</li> <li>Evolution of Railbelt ecosystem will inform value of AEA-owned assets</li> </ul>

# Integration of AHFC/ AEA recommendations

Recommendation	Details and rationale
<div>1</div> <b>Integrate AEA under AHFC to better provide energy / community development services</b>	<ul style="list-style-type: none"> <li>Integrating with AHFC can result in many benefits               <ul style="list-style-type: none"> <li>AEA to capitalize on AHFC's presence/offices in rural Alaska</li> <li>Combining in an entity that focuses on rural Alaska</li> <li>Optimize AHFC's access to capital markets</li> <li>Synergies with existing energy efficiency programs</li> <li>Synergies in shared services</li> <li>AHFC has been designated by US DoE as "Energy Agency" for Alaska, until it was passed to AEA ~3 years ago; AHFC maintains 50% of funds from DoE</li> <li>AHFC looking into upgrading IT systems, making timing of integration ideal</li> </ul> </li> <li>AHFC will be better house for AEA given the new design for AIDEA as a risk -taking asset management entity</li> <li>Potential to further integrate AIDEA shared services if separation of AIDEA/AEA proves costly</li> </ul>

# Agenda

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Project overview

Economic development landscape

AHFC summary findings

AEA summary findings

**AIDEA summary findings**

Next steps

## Summary of AIDEA findings

**Alaska has a unique need for enterprise project and infrastructure financing in AIDEA, which plays a critical role in filling a key need through Development Finance**

**Financial returns have been reasonable given AIDEA's role and mission; forward looking return profile targets modest return based on a conservative investment approach and a focus on small and mid-sized projects – potential to consider filling financing role for projects with different risk profiles**

- The Loan Participation Program plays a critical role supporting Alaskan banks and businesses as well as providing economic stability during a downturn; we believe it is appropriately sized despite a larger portfolio than many peers
- AIDEA's Development Finance activities create significant jobs and earn a modest return; there may be opportunities for the state to increase its impact with AIDEA playing a larger role, targeting sector investment and using a broader range of investment tools

**AIDEA operates with significant oversight which may inhibit a more returns-focused approach -- bonding and loans > \$25M require legislative approval, and the Legislature and other state entities can assign development projects**

**AIDEA has deep local market knowledge and has been making ongoing changes to strengthen internal practices. Additional opportunities for improvement include:**

- Developing an overarching investment strategy or systemic approach to key sectors
- Metrics-driven management
- More risk tolerant investment approach



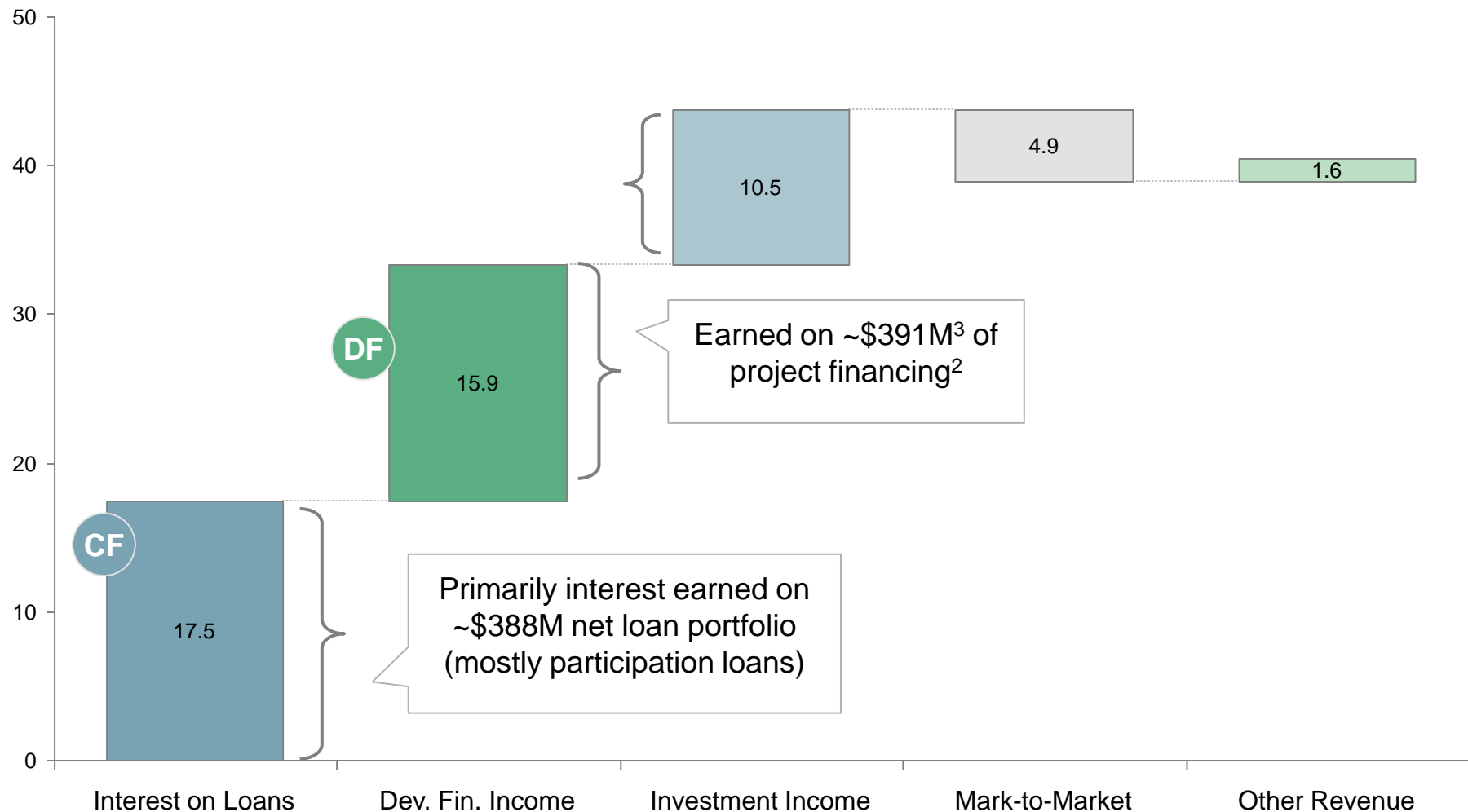
# Commercial and Development Finance activities play distinct roles with different deal profiles

	Commercial Finance	Development Finance <sup>1</sup>
<b>Purpose</b>	<ul style="list-style-type: none"> <li>Support business growth, market values, liquidity</li> <li><b>Fill gaps in the private loan market</b> for longer-term projects</li> <li>Support <b>AK state banks</b> to increase portfolio</li> </ul>	<ul style="list-style-type: none"> <li>Finance large projects that will realize returns and lead to <b>macroeconomic growth</b></li> </ul>
<b>Deal profile</b>	<ul style="list-style-type: none"> <li>Fixed rate loans, at "<b>sweet spot</b>" of <b>\$1-2M</b></li> <li>15-25 yr financing; rates at- or slightly-below market</li> <li>Projects with expected <b>cash flow in out-years</b></li> </ul>	<ul style="list-style-type: none"> <li>Infrequent, larger, riskier deals, often with complex private-public partnerships</li> <li>Commonly involves <b>AIDEA facility ownership</b></li> <li>Some projects arise from AK public need</li> </ul>
<b>Process</b>	<ul style="list-style-type: none"> <li>Loan originated by banking partners which apply for participation</li> <li>AIDEA participates <b>up to 90% of the loan</b></li> </ul>	<ul style="list-style-type: none"> <li>Projects assessed for <b>suitability</b> and <b>feasibility</b></li> <li><b>Due diligence</b> conducted through subcontractors</li> </ul>
<b>Restrictions</b>	<ul style="list-style-type: none"> <li>Loans <b>&gt; \$25M</b> require legislative approval</li> <li>Loan up to 75% value of collateral</li> <li>15 yr term personal property, 25 yr real property</li> <li><b>&gt;\$3M loan requires Board Approval</b>, Loan Committee reviews all loan requests</li> </ul>	<ul style="list-style-type: none"> <li>SETS and Arctic Infra. need <b>legislative approval for loan guarantees &gt;\$20M</b></li> <li>Can finance up to <b>1/3 of project</b> (no cap)</li> <li>Must be located in state of Alaska</li> <li><b>&gt;\$25M of bonding</b> requires state approval</li> </ul>

1. "Development Finance" extends to projects beyond AS 44.88.172, including funds spent on North Slope Pad, Ambler Mining Road, and Interior Energy Project  
 Source: Interviews with AIDEA employees, July and August 2016

# AIDEA's operating revenue<sup>1</sup> driven by loan participation interest and annual revenue from development projects

Operating Revenue 2015 (\$M)

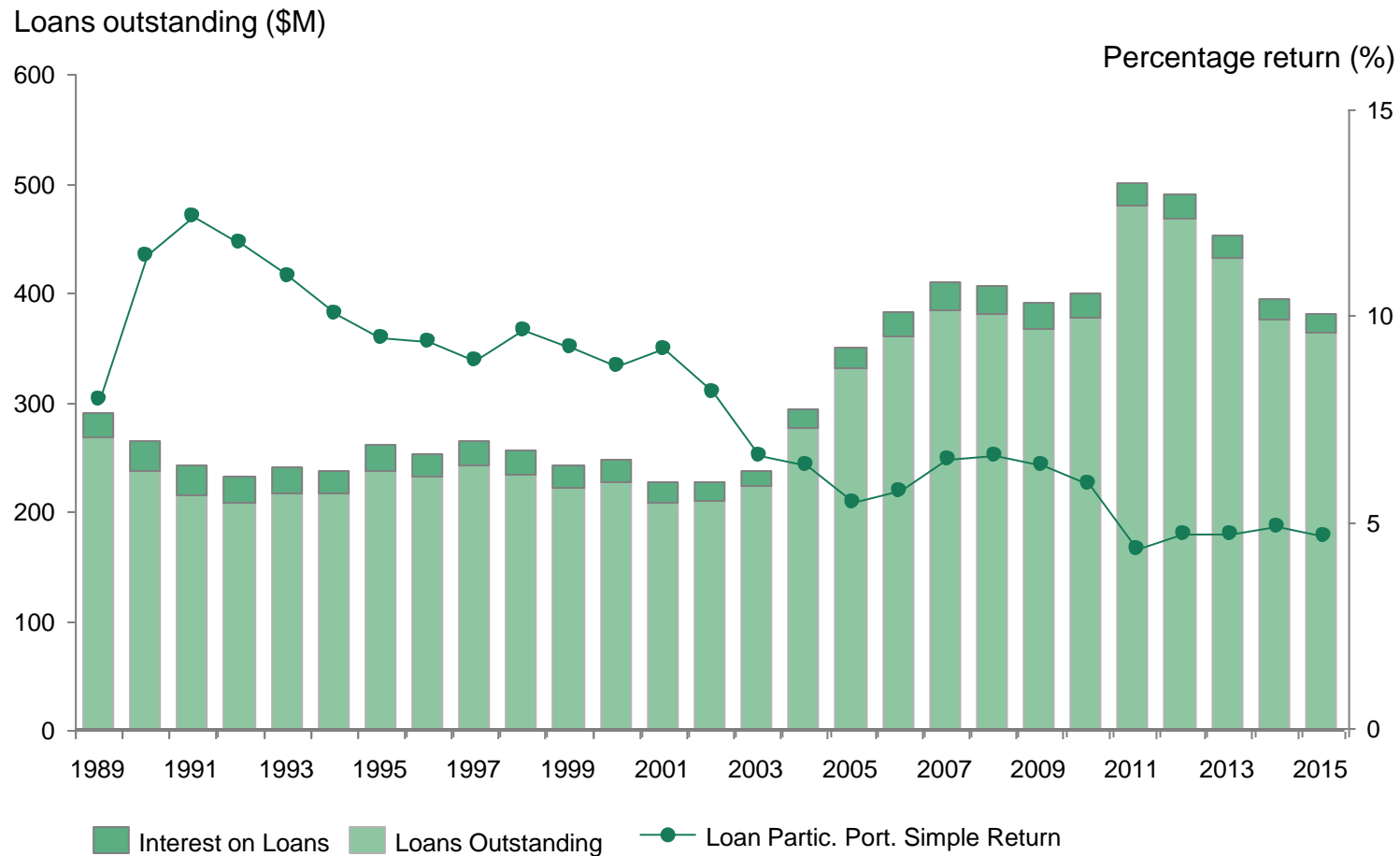


1. Diagram does not include Interest on Snettisham restricted direct financing lease revenue/expense (\$3.753M) or revenue/expense from state agencies (\$8.9M), as they also appear as expense items (neutral income impact) 2. \$10.9M in 2016 revenue driven by DeLong Mountain Transportation System 3. Includes Snettisham, Ketchikan Shipyard, and other "non-172" assets.

Source: AIDEA Financial Statements, 2015; Interviews and email from AIDEA comptroller

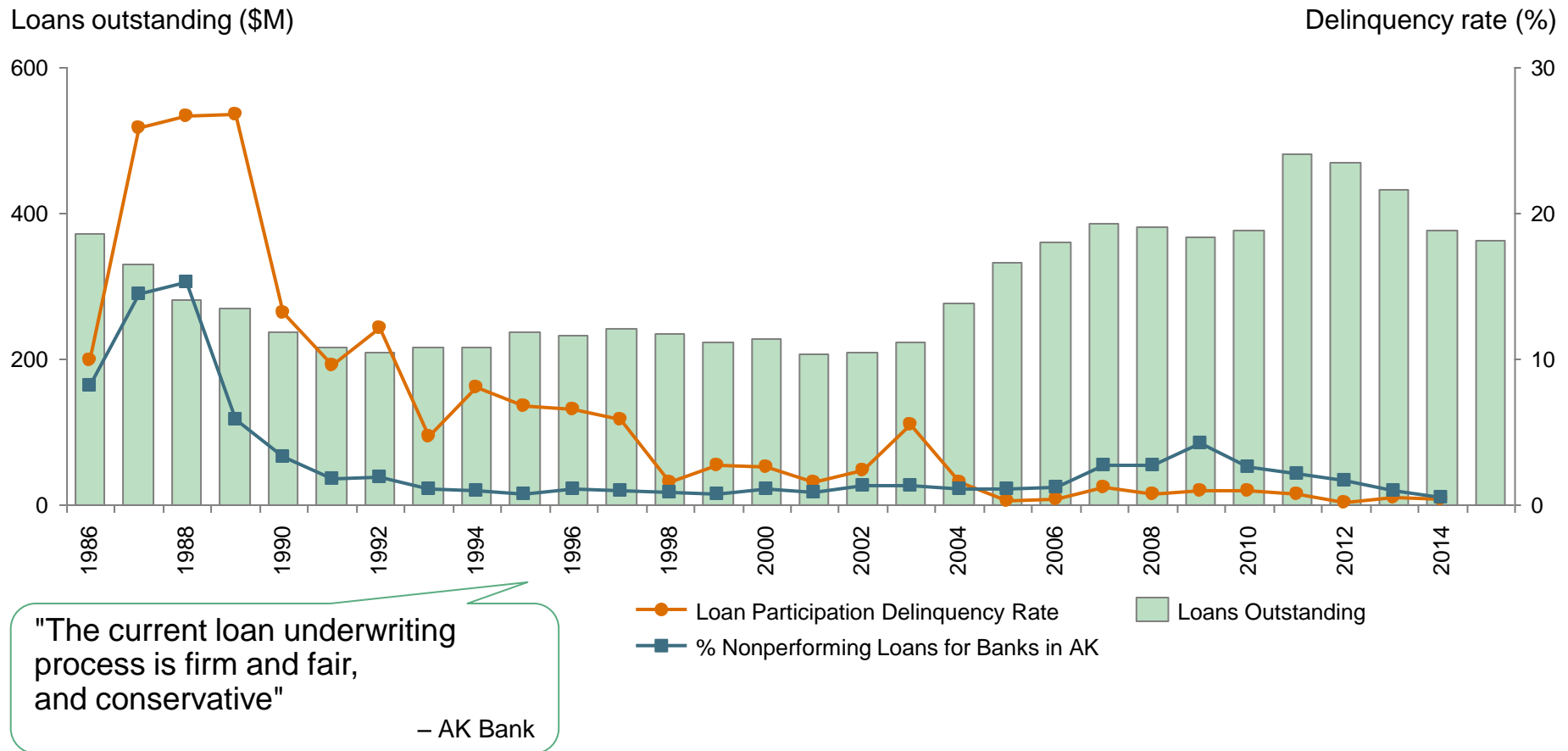
# Loan Participation Program provides consistent revenue source for AIDEA

**Consistent loans outstanding and returns over time provide additional capitalization for AIDEA Revolving Fund**



# Low delinquency rate supported by conservative underwriting ensures consistent financial performance

## AIDEA delinquency below already extremely low-delinquency Alaskan market



Source: AIDEA Presentations and data from Commercial Finance Director; Alaska Benchmark from Federal Reserve Bank: "Nonperforming Loans (past due 90+ days plus nonaccrual) to Total Loans for Banks in Alaska, Percent, Annual, Not Seasonally Adjusted." - this data is for average delinquency on all loans in Alaska as of January 1st of each year.

# AIDEA supports Alaskan economy in several ways

Facilitates Commercial Finance and medium-sized industrial projects

## Commercial Finance

**Fill capital availability gap:** supports commercial loan financing, some of which would otherwise not be issued by a bank

- Presently serves ~174 businesses, with 208 loans outstanding

**Support AK state banks and credit unions:** participate in financing loans with banks that may not otherwise have the capacity to book full value of those loans

- Currently partners with 8 Alaska banks, 2 national banks

## Development Finance

**Serve public needs:** support the needs of Alaska residents by financing and managing projects for public good

- e.g., Interior Energy Project to address pollution issue in Fairbanks

**Finance major state projects:** provide financing for large (>\$50M) state project needs, such as access to resources

- e.g., Amber Mining District access to spur mining development

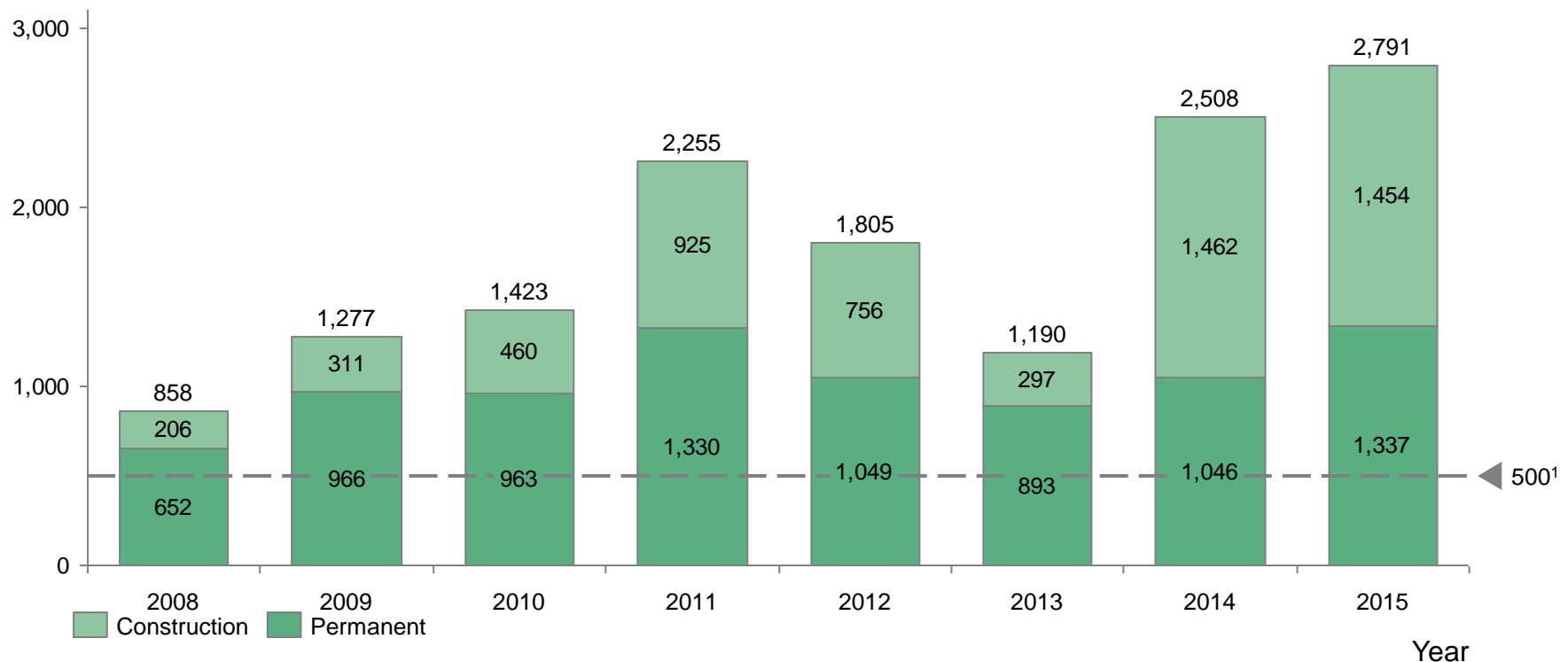
**Facilitate private sector investment:** provide creative financing for partners in projects with macroeconomic impact and strong business case

- e.g., Kenai Offshore Ven. \$23.6M financing leveraged \$103.4M private funding

# AIDEA consistently exceeds goal of 500 direct permanent jobs created each year

Estimated impact at time of application

Direct jobs created or retained



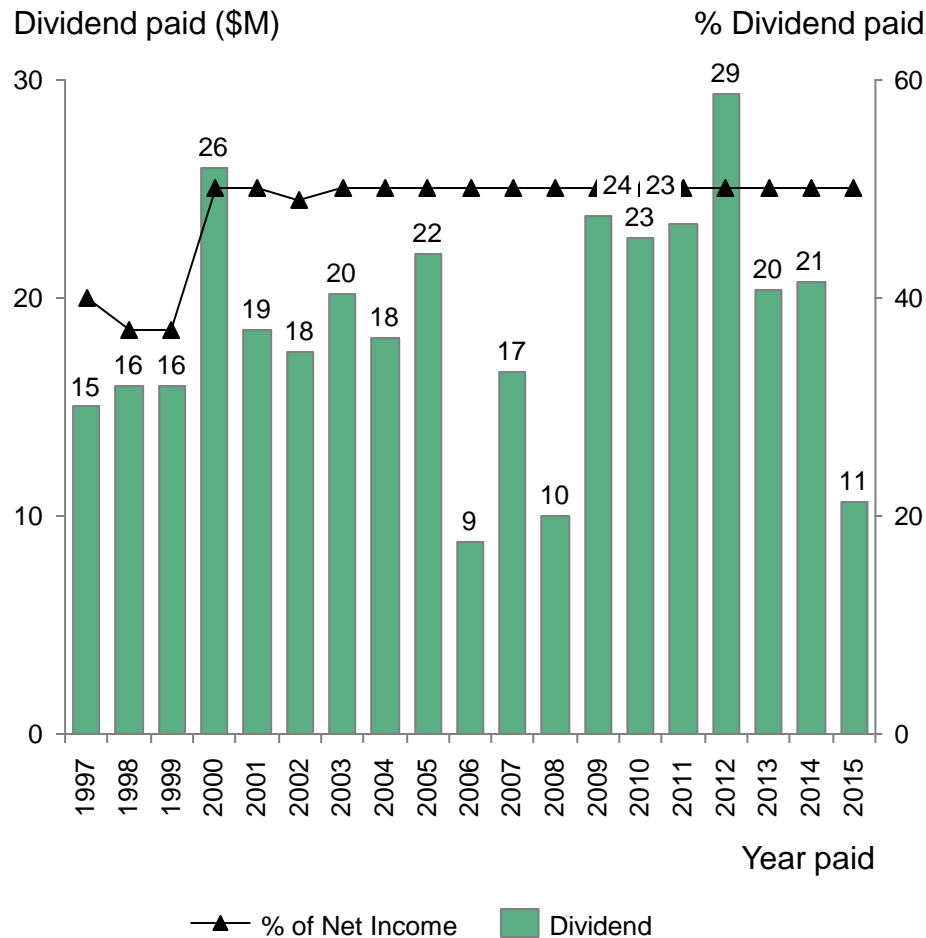
**Consistent and complete macro economic impact figures are critical to the AIDEA value story**

1. DeLong Mountain Transportation System accounts for ~500 permanent jobs, annually

Note: AIDEA additionally targets 400 construction jobs supported each year, and has met that target in 5 out of the last 8 years

Source: AIDEA Financial and Operational Metrics, May 2016

# AIDEA has a history of returning a profit to shareholders in the form of an annual dividend to the State of Alaska



## Dividend Payment

### Dividend frequently paid out at ~50%

- Required to be 25-50% of statutory net income from two years prior<sup>2</sup>
- Statutory net income fluctuations primarily due to "Mark to Market" rules
- Paid back to AK General Fund

**Full initial capitalization of AIDEA repaid to state through annual dividend**

1. Net income is defined in AIDEA statutes for dividend base 2. Per Board policy, AIDEA required to have 2 years expected liquidity managed internally<sup>3</sup>. Bond covenants include maintenance of Revolving Fund Cash Equivalents (as defined in the Revolving Fund Bond Resolution) maturing within one year in an amount at least equal to lesser of \$50M or 25% of outstanding general obligation indebtedness. Source: Data provided via email by AIDEA comptroller, July 2016

# Opportunity for Development Finance to fill gaps in AK market with expanded capabilities

## Strengths

### Knowledge of local markets

- AIDEA employees have close ties with banks in Alaska

### Creative financing

- Can combine funding sources in creative ways to make a project happen
- Can offer flexible pay back terms and range of engagement models
- Can accept and administer federal funds

### Patient capital

- Can withstand project delays and commodity price fluctuations

### Diversity of projects

- Serves many regions in Alaska with a variety of project types (military, shipyards, infrastructure, etc.)

## Challenges

### Lack of inbound "good" projects

- Pipeline unclear, no proactive project sourcing

### Statutory restrictions

- SETS and Arctic Infra. need legislative approval for guarantees >\$20M and can finance up to 1/3 of project (no cap)
- Must be located in state of Alaska
- \$25M bonding limitation<sup>1</sup>

### Lack of coordinated strategy

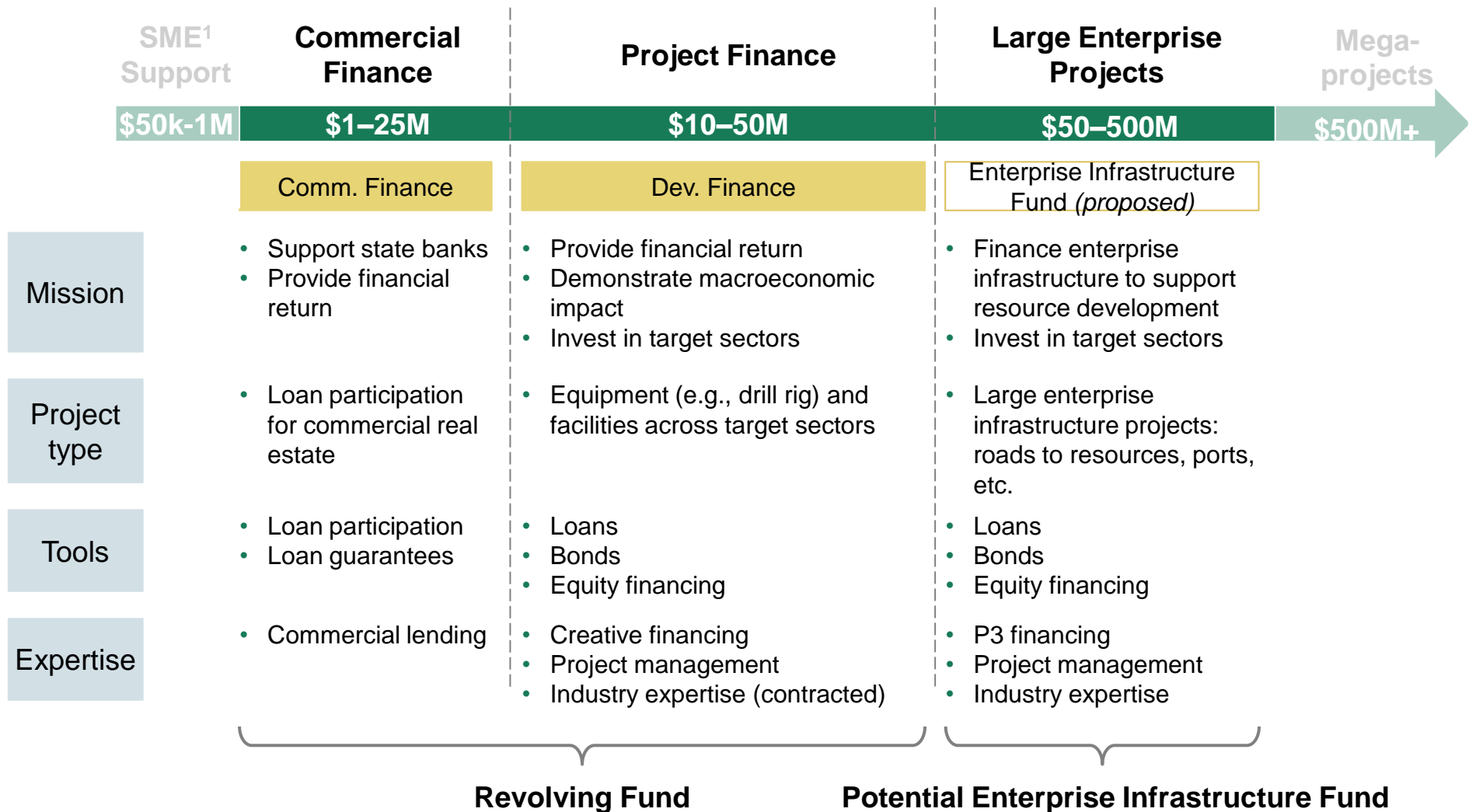
- No sector strategy to inform projects to pursue
- Mandate to finance ad-hoc projects from legislature, other state entities

**Limited ability to operate to the "left" of the risk curve, in either concept phase of project timeline or in higher risk projects**

1. Excludes Conduit Revenue Bonds and Refunding Bonds



# Overview of current and potential additional areas of state financing activity



1. Small and Medium-sized Enterprises

## Takeaways for AIDEA

**Alaska has a unique need for enterprise project and infrastructure financing given its core industrial focus and need for infrastructure to access critical assets**

**Today, AIDEA plays an important role in two aspects: small commercial finance in the form of the Loan Participation Program and investment in small and mid-sized enabling infrastructure through Development Finance**

**However, there is opportunity in the marketplace for a State player to take a larger role in the following ways**

- Invest in larger enterprise infrastructure projects (i.e. \$50-500M), targeting key sectors to diversify the overall economy (e.g. minerals, tourism)
- Proactively source and select projects targeting specific economic sectors that can foster high potential industries and diversify the economy
- Increase the use of a range of investment vehicles (e.g. equity as well as debt) to improve returns

**Further, it is important that AIDEA continue its process of making management improvements including:**

- Track and report financial and macroeconomic impact
- Enhance project assessment and selection rigor/criteria process
- Foster a more risk tolerant culture through governance
- Increase financing and operating budget flexibility

# AIDEA recommendations

		Recommendation	Details and rationale
1	Mission	<b>Refine AIDEA's mission for transparency and specificity</b>	<ul style="list-style-type: none"> <li>Current mission obscures specific programmatic objectives</li> <li>E.g., New mission: "Generate financial returns from Commercial and Development Finance to fund large infrastructure projects benefitting the State of Alaska in key sectors"</li> </ul>
2	CF <sup>1</sup>	<b>Maintain Loan Participation Program, refine rate setting</b>	<ul style="list-style-type: none"> <li>Update rate setting methodology in line with peers to allow differentiated rates by lender</li> <li>Track and report macroeconomic impact of loans beyond direct jobs created</li> </ul>
3	Development Finance	<b>Expand capabilities to finance larger projects</b>	<ul style="list-style-type: none"> <li>Match financing tools to appropriate project risk (e.g., use equity and other tools)</li> <li>Create Enterprise Infrastructure Fund to protect investment in resource and enterprise dev. infrastructure—close links w/DNR, etc.</li> </ul>
4		<b>Use deliberate sector level approach to proactively source and select projects</b>	<ul style="list-style-type: none"> <li>Develop strategic perspective on where AIDEA can add value in core sectors (e.g., minerals, fisheries, oil and gas)</li> <li>Proactively build pipeline insight through engagement with other gov't and private entities</li> <li>Leverage local knowledge to add value as an advantaged investor</li> </ul>
5		<b>Optimize capital structure toward fulfillment of mission</b>	<ul style="list-style-type: none"> <li>Deploy allowable portion of ~\$300M<sup>2</sup> on balance sheet by capitalizing new Enterprise Infr. Fund, potentially funding large projects and/or expanding external investment portfolio</li> <li>Establish long-term targets for capitalization</li> </ul>
6	Operations and Governance	<b>Track and report financial and macroeconomic impact</b>	<ul style="list-style-type: none"> <li>Better articulate and track AIDEA impact<sup>2</sup></li> <li>Financial performance: keep project-level return data</li> <li>Macroeconomic impact: engage third-party for objective analysis of economic impact metrics</li> </ul>
		<b>Enhance project assessment and selection rigor/criteria process</b>	<ul style="list-style-type: none"> <li>Progress made to date, more improvement needed</li> <li>Engage rotating private sector advisors for feasibility review</li> <li>Articulate clear criteria for each phase of assessment</li> </ul>
		<b>Foster a more risk tolerant culture through governance</b>	<ul style="list-style-type: none"> <li>Lengthen Board terms to fixed 5 years, staggered appointments</li> <li>Require mix of financing, banking, industry experience, allow outside-AK representation</li> </ul>
		<b>Increase financing and operating budget flexibility</b>	<ul style="list-style-type: none"> <li>Match approval needs to fund type: increase legislative approval bond issuance limit to \$50M for project finance, \$300M for infrastructure</li> <li>Allocate funds for strategy and pre-diligence activities</li> </ul>

1. Commercial Finance 2. Up to ~\$200M of liquidity may be required by bond and revolving loan covenants 2. . Issue identified, continuous improvement underway

# Agenda

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Project overview

Economic development landscape

AHFC summary findings

AEA summary findings

AIDEA summary findings

Next steps

## Next steps

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**Throughout this process, the BCG team worked closely with leadership and staff from each of agencies, which have been committed to the spirit of continuous improvement**

**Work continues to review and implement the recommendations that came out of this effort**