



Frankfurt School
UNEP Collaborating Centre
for Climate & Sustainable Energy Finance

REGIONAL PRIVATE SECTOR CONSULTATION

Supporting the Work of the
Transitional Committee for the
Design of the Green Climate Fund

Workshop Report, 25 August 2011



AFRICAN DEVELOPMENT
BANK GROUP

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The Workshop was organized by the Frankfurt School – UNEP Collaborating Centre for Climate and Sustainable Energy Finance in cooperation with UNEP FI. It was supported by UNEP and AfDB.

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UNEP HEADQUARTERS, GIGIRI, NAIROBI, KENYA, 12 AUGUST 2011

BY JAN G. ANDREAS AND ULF MOSLENER

1. BACKGROUND

The workshop was organized by the *Frankfurt School – UNEP Collaborating Centre for Climate and Sustainable Energy Finance* in cooperation with *UNEP FI*. It was supported by the *United Nations Environment Programme (UNEP)* and the *African Development Bank (AfDB)*.

The workshop was moderated by Farrukh Khan, Co-Facilitator of Workstream III. The constructive discussions involved the active participation from private sector and commercial finance institutions of a number of countries including Kenya, Uganda, Zambia, Tanzania and Ethiopia.

About 24 participants from 19 different private sector institutions took part, including commercial financing institutions, project developers and investment funds. (List attached)

The central purpose of the consultation was to secure the private sector input to the GCF design process. A series of questions were posed to them in advance in line with the scoping paper of Workstream III on “Finance Entry Points” (TC-2/WSIII/1, Annex I).

This report briefly reflects the discussion about opportunities that the Green Climate Fund could offer to the private sector in African countries and then more extensively covers the discussions on barriers and potential responses by the GCF. On top of this, other issues were raised, such as the role of environmental and social impact in private sector decisions or the topic of “transformation”.

This report is not a verbatim record of extensive discussion which took place but rather covers the main issues and reactions as they were discussed during this day long interaction.

2. OPPORTUNITIES

Participants generally see an immense number of project opportunities and ideas both on a stand alone basis and within existing business. This includes (i) energy efficiency since electricity generation capacity is often scarce and fossil fuel resources frequently have to be imported, (ii) renewable energy since many countries possess a large potential which remains untapped to date e.g., solar, wind, biomass or geothermal resources, (iii) financing of firms (sometimes SMEs) which are providing services or manufacturing equipment and technologies for energy efficiency or renewable energy technologies, (iv) projects in the agricultural sector, which in most cases inherently carry the character of adaptation, (v) projects which are specifically targeted to adapt to climate change.

3. BARRIERS

INSTITUTIONAL BARRIERS TO MOBILIZE PRIVATE SECTOR INVESTMENT/RESOURCES IN ADDRESSING CLIMATE CHANGE

Absence of Expertise

The private sector cannot make use of the opportunities since , in general, private sector representatives state that the expertise is lacking to translate the large number of creative project ideas and concepts into a so-called **"bankable project pipeline"** which fulfils the conditions needed by commercial local and international banks in order to provide financing for the respective projects and programmes. In addition, financial as well as technical skills with the **local finance institutions** are often not considered suitable to deal with the specifics of clean energy and climate-related projects

The majority of the participants were not specifically concerned about the difference between mitigation and adaptation. A point was made invariably that investments dealing with **adaptation** to climate change are frequently not explicitly identified as adaptation projects.

In a number of cases, participants identified non-transparent or unpredictable **regulatory authorities** as a major barrier to translating the ideas into projects that can get finance and achieve a sufficient rate of return. This concern also referred to the guidelines and regulatory principles of the authorities as well as their specific actions. Among the examples mentioned were alternative regulatory principles in determining a feed-in-tariff: whether a support scheme is based on a certain profitability of a renewable energy project (e.g. a target internal rate of return the regulator considers sufficient) which then determines the appropriate feed-in-tariff or whether a unique and fixed feed-in-tariff is granted. Investors felt more comfortable with a fixed tariff regime rather than a "case by case" approach as have been prevailing in their countries where they operate. Generally, it was felt that in a majority of the countries, the tariff bands were set by government without taking into consideration the private sector and hence such tariff bands increase the risk and decrease the bankability of the project.

Another important barrier identified was with respect to the existing contractual agreements. Nearly all participants underlined that pre-existing long term contracts between the government and the established market actors prevent investment into new and renewable energy projects. In such a scenario, neither the government nor the private sector finds it attractive to get into new markets.

On the financial side a **limited flexibility of internal lending policies** was seen as an impediment. Examples presented include excessive collaterals required to provide a loan, or the mismatch of the economic lifetime of many clean energy projects on the one hand and bank's

expectation and ability regarding the loan maturity on the other. Examples for the technical side were the lack of standardized energy audits based on which energy efficiency loans could be extended to end-customers or the specific requirements coming with clean energy project evaluation and appraisal, including technical and feasibility studies.

Generally, the issue of generating a good quality project proposal to get financing for a project was considered to be more critical than the question of **“availability” of a certain technology**. A critical point highlighted by the participant was adaptation of a given technology to local circumstances for which either incentives from the government or an international entity may be worth exploring.

4. PROJECT-ECONOMICS-BARRIERS TO INVESTMENT

Many participants stated that monetary (as well as other) incentives are often insufficient. Feed-in-tariffs were mentioned; in other cases also the lack of tax waivers was considered a barrier. A generally positive attitude by the national governments that translates into favourable investment environment for clean energy and adaptation was considered helpful.

Lack of equity capital or risk capital was considered a major problem on the way to get financing for clean energy projects: A higher proportion of equity capital in a project means that less bank loans are necessary to finance the project. As a consequence the banks consider the loans as less risky since their loans are paid by the project *before* the equity holders get their return. Typically, local commercial financing institutions provide short-term loans only, which don't fit with the economics of many renewable energy projects whose pay-back period is generally longer. It was pointed out that the current environment and regulatory infrastructure is promoting investment in energy efficiency alone since the pay back was quicker. The reasons cited were that renewable energy generation demands high up-front investment (generating financing costs), while operating costs are relatively low. The **long payback periods** of greenfield investments appear to be a general issue for the private sector in the respective countries.

Also, since in a majority of the countries represented, not many clean energy projects were realized to date, this reluctance to engage in such projects was considered as an impediment due to the lack of corresponding experience in the private sector as opposed to conventional energy projects. Generally, the engagements with project were considered risky unless one will be able to refer to a certain **“critical mass” of experience**. This holds for project development as well as for project execution. As a consequence, technology and project specific risk, or risk perception tend to drive-up financing costs and requirements for collateral.

Finally, the Participants considered the issue of financing small and medium size enterprises or even **smaller loans/financing** very important. A significant part of the potential in addressing climate change in many countries in Africa could only be realized via larger numbers of small- and medium-scale projects. The potential remains untapped since relative financing costs for smaller scale projects are higher as compared to large scale projects; lending practices of the local financing institutions, requiring excessive collaterals or full recourse; and rather different needs of the SMEs who often just don't need loans to invest but also need working capital.

5. RESPONSES

Participants stressed that any increased use of clean energy technologies and innovation – if facilitated by the fund – can be expected to contribute to **bringing technology costs and financing costs down**. Increased investment activity will generate learning effects on the technology application as well on the financing side.

Participants considered funding windows that would also issue **grants as a critical element** of the GCF. Considerable impact was expected if those windows would be targeted at issues such as:

- (i) direct financing: enabling project developers in generating a bankable project pipeline (e.g. a project development facility) including demonstration/pilot-projects in building a track record/references and to establish “green lending” policy environment for the commercial banks and institutions;
- (ii) public sector capacity building: catalysing national regulators’ efforts in establishing transparent processes and national regulations;
- (iii) private sector skill development: assisting commercial financing institutions in establishing project evaluation and appraisal procedures dealing with energy efficiency and renewable energy projects since 50% of the project is skill/service.
- (iv) private sector collaboration: supporting commercial financial institutions in developing new products and business segments in providing financing for energy efficiency and renewable energy projects or in extending dedicated credit lines to the end-user

Participants considered it helpful if the fund could **catalyze contributions of equity and mezzanine finance** for stand-alone renewable energy projects. Similarly, the bundling of small- and medium-scale projects in a portfolio to bring down risks and finance costs (e.g. through pooling) was considered promising.

Risk guarantees would be considered helpful by many participants. These could also be applied in order to increase the predictability of political support instruments – although the issue of moral hazard was recognized as a point of concern in this respect. Some also referred to foreign exchange risk as an important issue. Among other, absence of sovereign guarantee was considered important. Some participants also highlighted that the nature of guarantee for different sectors may differ as well.

Many saw a potentially important role of the fund in facilitating the **provision of insurance products**, however, cost of such insurance product in Africa was considered as a serious impediment. On the one hand this referred to mitigation-projects such as wind, water and solar – e.g. insurance against the provision of those naturally volatile resources, which might also be affected by climate change. On the other hand participants included insurance instruments directed to adaptation, such as insurance instruments against drought or crop-insurance. The issue was also raised whether the fund could find a way to induce some competition between insurers that would potentially provide such products leading to a competitive market and bringing insurance costs down.

In order to allow for a continuous **feedback and improvement between the GCF, national governments and the private sector**, concern was expressed that a sufficient information flow and an exchange between private sector actors and the national level policy makers should be developed. Some participants stated that it would be desirable for the fund to evolve a framework for institutional representation of the private sector, e.g., through a private sector focal point.

Some participants expressed the hope that the fund would leverage the awareness of their respective national governments with respect to the concrete issues that financial institutions face when dealing with investment decisions related to clean energy or adaptation. And that the fund should motivate the governments to provide a more favourable **investment environment** for these projects. With respect to grants and subsidies provided by the fund it has been emphasized that – from the perspective of financing clean energy projects – there are not only helpful, but also **climate adverse subsidies**. Prominent examples were cases where markets are excessively distorted and where energy use is highly subsidized.

6. OTHER ISSUES RAISED

All participants from the private sector considered **environmental and social safe-guards** crucial, and practically all participants explained that their respective institutions are in the process of implementing or already have implemented such safe-guards in their business practice and that it is in their own interest to do so. At the same time concern was expressed that formulating and implementing such standards might put climate friendly investment at a competitive disadvantage in cases, where the projects are in tight competition with other projects, which are typically not concerned about such safe-guards.

Private sector representatives briefly discussed, what they would consider **“transformational change”**. Although the discussion did not provide a clear-cut picture, there were voices that stressed the role of education and awareness in general in this context. While education and continuous learning was seen as a multi level requirement (Private Sector, Government), “awareness” was related not only to the current and future carbon footprint as a result of current activities and decisions, but also to potential co-benefits of the activities, especially such as poverty eradication, with the eventual goal to create an improved quality of life, not just for some but – through distribution of successful models – for all.

It has also been formulated that “transformation” is not just about progress in the “right” direction, but it is also about the “speed” of that progress.

Annex 1

List of Participants



**AFRICAN DEVELOPMENT
BANK GROUP**

UNEP/AfDB Regional Private Sector Consultation to Support the Work of the Transitional Committee for the design of the Green Climate Fund

Venue: UNEP Headquarters, Gigiri, Nairobi, Kenya

Date: 12 August, 2011

Lists of participants

	Delegate's Name	Nationality	Company
1	Aburi Susan	Kenya	Ecobank
2	Achini Mary	Kenya	Cooperative Bank
3	Adcok Tomas	Kenya	Kenergy
4	Aguko Elly	Kenya	K-REP Bank
5	Andreas Jan	Germany	Frankfurt School of Finance & Management
6	Asimwe Paul	Uganda	Sipi
7	Blanchard Kevin	France	Frankfurt School of Finance & Management
8	Dodhia Khilna	Kenya	Kenergy
9	Kaluba David	Zambia	Principal Economist, Ministry of Finance
10	Khan Farrukh	Pakistan	
11	Kihara Vincent	Kenya	Barclays Bank
12	Maladken K.D	Kenya	KCB
13	Malika Peter	Tanzania	E+Co
14	Merlyn Van Voore		UNEP
15	Moslener Ulf	Germany	Frankfurt School of Finance & Management
16	Nasr Mohamed	Egypt	
17	Obse Haileyeus Bekele	Ethiopia	Construction and Business Bank, Ethiopia
18	Osawa Bernard	Kenya	ERC
19	Oyugi Emily	Kenya	UBA
20	Rulagaranga Deogrtias	Tanzania	UBA
21	Sawe Estimah	Tanzania	Tatedo
22	Shah Menka A.	Kenya	Acumen
23	Thiaw Ibrahim		UNEP
24	Wambani Brian	Kenya	Stanbic



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