

CLIMATE INVESTMENT FUNDS

SREP/SC.2/4
March 4, 2010

Meeting of the SREP Sub-Committee
Manila, Philippines
March 17, 2010

ELEMENTS OF FINANCING MODALITIES

SREP Financing Modalities

CIF

Second Meeting of SREP Sub-Committee

Manila, Philippines

March 17, 2010

Overview

- Financing needs in low income countries and SREP support.
- Blending SREP funding with MDB assistance.
- Financing guidelines.
- Procedures.
- Financing instruments under SREP.
- Guidance needed from SREP-SC.

Financing RE in Low Income Countries

- Need to maximize resources to address various inter-related barriers:
 - Policy and regulatory barriers.
 - High upfront costs.
 - High transaction costs.
 - Low institutional capacity.
 - Low access to finance (poor credit, profiles, etc.).
 - Partially developed markets.

***SREP** strives to address this need by offering a range of financing in the form of grants, concessional debt, and financial/fiscal incentives based on specific conditions and requirements in pilot countries.*

Blending with MDB Assistance

- SREP financing will be blended with MDB lending programs and other available funds to invest in RE technologies.
- SREP assistance will be ‘additional’ to existing or planned MDB program, and not a duplication.
- SREP could address specific components as a leverage to MDB programs.
- As a complementary program to MDB programs, SREP should contribute to development of a national roadmap for scaling up RETs.

Financing Guidelines

- Grant for project preparation not to exceed \$1 million in the case of public sector projects.
- For private sector, request for preparation grants is included in the relevant program/project proposal submitted for Sub-Committee approval.
- Free-standing Technical Assistance support up to 10% of SREP funds in a Investment Plan.
- Likely leverage from parallel activities of other development partners (e.g. bilaterals) should be projected into Investment Plan design.
- In the investment projects, efforts should be made to maximize actual project operations (e.g. technology deployment and related field operations) compared to 'soft' activities.

Procedures

Funding Approval

- The Sub-Committee will endorse an Investment Plan and a SREP resource envelope.
- Endorsed Investment Plan serves as a basis for the country and designated MDB to proceed with development and preparation of individual investments for SREP (co)financing.
- Sub-Committee approves SREP financing for project or program prior to its appraisal.

Procedures

- Individual operations under each country's Investment Plan will be processed through the MDBs working with the pilot country.
- Each operation will follow the investment lending policies and procedures of the MDB, including its fiduciary standards and environmental and social safeguards.
- Each MDB will apply its own appropriate procedures in appraising, approving, supervising, monitoring and evaluating operations to be financed under SREP.

Financing Instruments

- **Grants**
- **Equity**
- **Concessional Debt**
- **Guarantee Instruments and Risk-sharing**

Grants

Free-standing Technical Assistance to Create Enabling Environment

- Recognizing the special needs of low income countries, SREP will finance free-standing technical assistance projects, possibly through a dedicated support program, to help countries prepare for project implementation. Such technical assistance can support:
 - Policy development.
 - Legal and regulatory reform.
 - Development of market enabling environment.
 - Resource assessment and pre-investment studies.
 - Capacity building including knowledge management.
- Up to 10% of SREP funding per pilot could be used for free-standing technical assistance.
 - Additional free-standing technical assistance, where required, would be sought from other sources, e.g. MDBs or other development partners.

Grants

Upfront support to prepare:

SREP Investment Plans in Pilot Countries

- Enhancing capacity of national institutions for robust policy reform and priority setting.
- Strengthening consensus among key national stakeholders and engaging development partners at the country level.
- Development of quality investment concepts as components of SREP Investment Plan.
- Implementation strategies for different components under SREP Investment Plan.
- Analytical work to ensure SREP activities correlate RE investments to energy access, economic growth and poverty-alleviation strategies.
- Assessing the poverty and social impacts of programs and projects.

Grants

Investments which may justify grant financing could include:

- Projects which have positive social and environmental externalities but high upfront and transaction costs and hence do not attract commercial investors on account of inadequate financial returns.
- Projects which have potential high returns or potential for high replicability, but with high level of perceived or real risk.
- Projects managed by public-private partnerships that build infrastructure for RE deployment (e.g. wind parks or solar farms), which can be utilized by private sector for scale up.
- Project-specific technical and operational capacity building.

Concessional Loans

SREP will provide support through:

- Lending to national governments.
- Lending to national governments for on-lending to sub-national entities.
- Lending to sub-national entities.
- Lending to the private sector.

Concessional Loans

Public Sector Projects

- Offer concessional debt with below-IDA rates for projects with:
 - Rates of return near or above normal market threshold, but below risk premium for project type, technology or country.
 - Rates of return near or above normal market threshold, but where intensified RE investments will have higher opportunity costs.

Concessional Loans

Suggested loan structure for Public Sector Projects

SREP Loan	Proposed Terms
Maturity	40 years (IDA)
Grace period	10 years
Principal Repayments (yr 11-40)	0.1% interest
FY11 MDB Fee	0.1%
FY11 Service charge	0.1%
Grant Element	≈75%

Concessional Debt

Private Sector Projects

- The terms and structures offered for each investment project by the private sector will be determined on a case-by-case basis by the MDBs to address the specific barriers identified in each case. The barriers could include:
 - High costs of early entrants.
 - Perceived and real risks to investors.
 - Combinations of risk and cost barriers faced by investors.

Guarantees and Risk Sharing

- Guarantee instruments are used to improve conditions for investment in, or lending to, public and private sector projects by mitigating risks that lenders and investors would not be willing or able to accept.
- For purposes of SREP support, a distinction is made between conventional risks for which adequate mitigation measures are already available and “incremental” risks that sponsors and lenders will not assume, despite the appearance of financial viability of the investment.
- The additional risks for RE projects can be quantified as the relative variance of a project’s returns, as perceived by the main investors, for a given level of expected return:
 - Technical and economic performance risks.
 - Commercial and financial risks.
 - Country and political risks.
 - Regulatory and institutional risks.

Guarantees and Risk Sharing

Examples of Guarantee Products

- **Loan Guarantees** covering the loss on account of debt service default for lenders up to an agreed portion of the actual loss, with a view to extending maturities of commercial loans for RE projects so that they are competitive with base case technologies, or to address specific incremental operating or management risks that could cause default.
- **Contingent Finance** disbursed to the project upon underperformance of a RE technology and where such risk is not commercially insurable at reasonable costs or has occurred beyond the period for which commercial insurance is available.
 - Depending upon the project and market needs, the amount guaranteed could be up to 100%.

Equity

- Participation in private sector RE projects to improve investor confidence.
- Projects with public-private partnerships to build RE infrastructure for scale up (e.g. inter-connection facilities).

SREP Sub-Committee Guidance

Guidance from the SREP Sub-Committee is requested on:

- Activities eligible for grant support to pilots.
- Activities eligible for concessional loans, guarantees and equity to pilots.
- Terms of concessional loans for public sector.
- Proportion of SREP funding that may be allocated to free-standing technical assistance.