April 12, 2016

[APPROVE BY MAIL]: TANZANIA: RURAL ELECTRIFICATION EXPANSION PROJECT (SREP) (WORLD BANK) (XSRETZ028A)

COMMENTS RECEIVED FROM SWITZERLAND AND WORLD BANK RESPONSE

Tanzania - Rural Electrification Expansion Project

Responses to comments from Switzerland

April 2016

	Comments	*Reviewer*	*Team's response*
1.	From your answer to our question 2c, we understood that the TIB credit line of USD 28 million will cover 70% of the cost/price of installed solar PV products, which according to the results framework corresponds to 1 MW distributed on 30'000 connections (i.e. 33.3 Watt per connection). This leads to a cost of 40'000 USD per installed kW or 1200 USD per connection with an average of 33 Watt power. This compares rather unfavorably with solar systems from recognized suppliers in other but similar contexts (e.g. a price of $450 for a solar kit consisting of a 70W panel plus 5 lights, battery and phone charging set in Kenya). Also the Loan Loss Reserve Fund represents 35% of the total TIB credit line which corresponds to a rather high default rate. Hence our perception of an inefficient use of SREP grants. a) Please explain. b) How could a better value for the money be guaranteed during the project implementation? c) How will it be assured that the Loan Loss guarantee does not entice Tanzania Investment Bank to grant loans too easily or for suboptimal projects?	Switzerland	The solar credit line will be initiated by the allocation of $10m ($9m SREP; $1m IDA) through TIB who will on-lend to eligible solar companies to grow their businesses. The $10m allocation can support up to $14.3 m in loans directly (with 70% loss coverage rate). TIB has indicated that they are willing to lend beyond the $10m, up to a maximum (in the $20m to $28m range) after experience is gained and confidence in the PV market and companies increases. As TIB will have capital at risk (the remaining 30% of the loan that is not covered by the LLRV), TIB will utilize their own due diligence of the loan and will have a direct financial interest in ensuring that the recipient is a quality company. We expect that as a result, the moral hazard risk is avoided. a) The Bank's estimate is that the $10 million from the Bank will enable $14.3 m from TIB to be lent to companies to support roughly 28,600 solar home systems, at an estimated average delivered cost of $500 apiece. These are the assumptions that we deployed to obtain

	Comments	*Reviewer*	*Team's response*
			approximately 30,000 systems, which is a rough estimate as the real number of systems to be sold and the average cost will be based on market preferences and may differ widely from these assumptions. However, this is a very conservative number which assumes that none of the loans are repaid and the funding, therefore, is never used more than once. We have been deliberately conservative in our estimation of this indicator and would expect that if things go well, this number of systems and the MW's deployed are both higher than what we conservatively assumed. By our calculations, the second window on the Credit Line or LLRF represents 25% of the TIB Credit Line (\$10m/\$42m total). b) Better value for money will be achieved under the LLRF if some of the loans are successfully paid back. As mentioned above, the team used the most conservative assumptions possible to calculate these indicators. If the full amount of the LLRF is used and only 50% of the loans fail, the results will likely double, to 2MW and 60,000 systems. c) Given that the losses will be shared pari pasu, it is unlikely that TIB will be faced with a moral hazard situation and make unattractive loans just for the sake of "moving money".

	Comments	*Reviewer*	*Team's response*
2.	Regarding your answer to our question 2d, we took note that 25.31% is the economical internal rate of return (EIRR) of the base case and that this is at the same time the best case. Have you made any calculation of the Financial IRR, e.g. from the perspective of TIB or of the typical SPP investor, which you could share with us?	Switzerland	As a PforR operation, we do not make explicit financial analyses for the parties concerned. We have not fully done a credible assessment of the program from TIB or the individual IPP developer's perspectives. For the SPP developers, they will only follow through on the proposals if they consider them financially attractive, after evaluating the likely return on investment. The "hurdle rate" is set by some increment to the prevailing interest rate, and the only projects moving ahead are those which will have satisfied due diligence from the PFI, TIB, and REA, as well as their own directors. TIB will only support a deal if it is satisfied that the deal is eligible and financially viable. The Credit Line is available only for refinancing, not initially financing deals, so the private actors will make the decisions.