INDIA – Partial Risk Sharing Facility for Energy Efficiency Project
World Bank Response to Comments by CTF TFC
June 5, 2014

#	Comment	Team Response
	GER, CAN, FRA COMMENTS	
1	GER, CAN and France had the chance to review the project proposal and we can only reiterate that from a technical perspective the facility looks interesting and worthy of CTF support. This project seems to be relevant in terms of sector / actors perspective. Reducing energy consumption in this country is crucial in view of the pressure on both demand and supply, and constraints that generate difficulties to change the energy mix. Companies wishing to finance an EE project are struggling to find adequate funding and initiatives will therefore be encouraged by a model where the ESCO takes the technical risk or financial risk on these investments. However, ESCOs are new players in India and they have difficulties in accessing the finance they need, especially if they want to make the investments on their balance sheets instead of beneficiaries. Mechanism guarantees / risk sharing in this case is still very relevant, sustainable (financial institutions "get used" to these new customers at lower risk) and has a strong leverage for a minimum use of funds (guarantee up to 40-75 % of the loan amount). In addition, the technical assistance provided on GEF funds will be crucial to funding projects in this very nascent market. There are a number of issues that we would like to discuss	Thank you for the endorsement and support. The project aims to demonstrate the ESCO-based implementation approach in the Indian EE market and is designed to address the barriers faced in the market. The team believes that a combination of TA with financial incentives (through risk sharing will help unlock the complex EE ecosystem and trigger large scale market transformation.

	further with you, to help inform our positions.	
2	We have noted that the project proposal is inconsistent with two aspects of the CTF guidelines as per the following document "Financing products, terms and review procedures for public sector operations, dated Nov 7, 2013". Specifically: • The Pricing of 10 bps for the guarantee facility – According to article 3c) "Outgoing financing cannot be more concessional than incoming financing". Thus, if the project is to be funded from all CTF contributions, the absolute floor pricing for the full amount of the guarantee over the tenor of the guarantee is a minimum of 75 bps. In addition, this project carries private sector, not public sector risk, given the fact that the CTFs' ultimate credit risk might predominantly be industry and ESCOs. Given the above, we do not consider this pricing acceptable and would ask the IBRD revise the pricing, accordingly.	The 0.10% guarantee charge is based on CTF Financing Products, Terms and Review Procedures for Public Sector Operations ("Public Sector Financing Paper"). The project design followed the pricing presented in the Public Sector Financing Paper, which was approved by the CTF Trust Fund Committee. However, the project team interpreted the "committed and undisbursed amount" on which the charge woud be levied to be the annual available amount of the CTF Guarantee. We also wanted to point out that the proposed India PRSF project is similar to the PHRED Philippines CTF guarantee program (already approved by CTF) where a government facility would provide sub-guarantees to private lenders (already approved by the CTF) and where the pricing of the CTF guarantee was similarly 0.10%. The project includes several design aspects to minimize the likelihood of a call on the CTF Guarantee. First, the CTF Guarantee is provided as second-loss cover, i.e. it will only be called once the GEF Grant, which is provided as a first-loss reserve, is fully exhausted by calls from PFIs. Based on financial analysis carried out by the team, the average payout ratio (after recoveries) would have to be more than 15 percent on all sub-guarantees issued before CTF would have to pay under its Guarantee. The project incorporates several oversight mechanisms (e.g. business plan reporting and review, consent requirements for material technical changes, an Operations Manual made legally binding through incorporation into the legal agreements) such that the implementing entity SIDBI can be directed to take appropriate corrective action if losses under the program come close to the CTF call threshold. The program also comes with a legal stop-loss provision, which means that SIDBI would be legally prevented from issuing additional sub-guarantees if actual losses start deviating from expectations. Please also note that many public sector loans for projects with higher concessionality requirements have been provided at 40 year maturity and 25bps in accordance with the pricing set in the the financing paper.

		For this project the World Bank cannot follow any other pricing. Should the TFC decide to reconsider pricing, we would apply it to future operations. Furthermore, the project clearly falls under CTF's public sector operations from a risk perspective and has been designed to comply with all requirements under CTF's corresponding operational guidelines. The underlying financial risk associated with the energy efficiency sub-projects complies with article 26(b) of the Public Sector Financing Paper which states that CTF Contingent Finance can be disbursed in the case of "underperformance of a low carbon technology where such risk is not commercially insurable at reasonable costs". In India the reason that such risk is not commercially insurable has to do with lenders' unfamiliarity with ESCO-based energy efficiency projects and associated high risk perception, rather than with the commercial or technological viability of the proven EE technologies themselves (see article 25(a) and (b)). The project also complies with the requirement that the borrower (or obligor in the case of guarantees) is a public sector entity since the CTF Guarantee is backstopping a government controlled guarantee facility where the issuer of guarantees is a publicly owned development bank.
3	• Furthermore, we have noted that this project is a stand alone project without further blending from IBRD or any other MDBs. This is also inconsistent with the above-mentioned guidelines (articles 6 – 8). India's investment plan for the CTF indicates that IFC was originally intended to participate in the partial risk sharing facility ($50M). We would appreciate further information from the IBRD on the reason for the IFC's withdrawal from the facility.	The proposed project structure is consistent with the India Investment Plans which did not envisage any WB co-financing at this stage. The project is designed as a pilot and, if successful, could be scaled up with IBRD or other MDB support. Blending is being done with GEF resources (similar to the precedent set by the CTF-approved Philippines ECPCG project) and with capital mobilization from the private sector. It is expected that the PRSF project will start to provide upstream support to the Indian EE market by addressing the key barriers and

		triggering the scale up of EE investments through ESCO-based implementation in India. At the same time, the IFC could support the overall development objective by contributing to the developmental elements of this sector by helping strengthen the ESCO industry as well as private sector end-user host entities and the banking sector by taking equity positions and/or providing debt support and through capacity building. Undertaking PRSF itself would conflict IFC in taking debt or equity positions in these participating ESCOs, host entities and FIs. Also, current regulatory restrictions of the Reserve Bank of India do not allow IFC to directly support and float risk-sharing guarantees, the issue being much larger of financial regulations.
4	In addition, we seek clarification on the following issues: • The project document indicates that, in the event of a claim, the minimum amount for a CTF contingent financing payment will be US$500,000, even if the cash shortfall in the participating financial institutions (PFIs) sub-account is less than that. We would request more information from the IBRD on the rationale for setting this minimum requirement, as it does not appear to be an efficient way to manage CTF resources, including by potentially committing unnecessary resources and creating a situation of moral hazard with the PFIs. •	The $500,000 minimum payment amount is intended to minimize the transaction costs in the unlikely event of a call on the CTF guarantee. Having a minimum CTF payout amount is more efficient in terms of transaction costs and processing in an operation involving potentially hundreds of sub-guarantees. As our financial analysis shows, there may be as many as 570 sub-guarantees in the base case scenario, and even more in upside scenarios. Allowing calls on the CTF Guarantee for small amounts could hypothetically lead to hundreds of calls on the CTF Guarantee for such amounts (once the PFI sub-account was depleted), generating additional transaction costs in order to deal with the mechanics of making payment from CTF, processing, and so on. The $500,000 increment would thus allow payment to be made in respect of such sub-guarantees and provide a cushion for further sub-guarantee calls so that the number of calls on the CTF Guarantee would be minimized and manageable. Finally, a minimum payment does not translate in any way into an overpayment for any sub-guarantee. Nor would it mean that any PFI would be pre-paid on any sub-guarantee claim so that a situation of moral hazard would not arise. Any excess amounts remain in the CTF account and will be returned to CTF when they are no longer needed. The team will assess during the upcoming appraisal if the amount can be

		reduced or the threshold eliminated without potentially incurring high transaction cost.
5	The project document indicates that the likelihood of CTF capital being called is sensitive to the pricing of the partial risk sharing facility's sub-guarantee by SIDBI. We would appreciate receiving more information from the IBRD on the conditions for monitoring how SIDBI will price the CTF sub-guarantee. •	With respect to sub-guarantee terms monitoring, those terms will be set out in the Operations Manual. SIDBI will provide annual reports (Annual Implementation and Business Plans) to IBRD, and while it would have discretion to change the sub-guarantee terms within a financially sustainable range agreed with IBRD and with consent of the PRSF Executive and/or Advisory Committee, any change outside that range (which is set to protect CTF capital among other considerations) would require IBRD consent.
6	There appear to be unresolved legal restrictions related to SIDBI's ability to issue guarantees to participating financial institutions in support of loans to medium enterprises (see page 81). SIDBI's ability to issue loans to medium enterprises is a key risk affecting the financial sustainability of this project; accordingly, we request further information from the IBRD on the steps it will take to mitigate this risk. •	We would like to clarify that SIDBI would be able to lend to medium-size institutions under the PRSF. As such, risk coverage for such lending would only be able to come from the SIDBI window of the PRSF, which is **not** guaranteed by the CTF due to SIDBI's status and our guarantee policy. It is funded only by GEF (initial capital of US$6 million). We acknowledge the need for clarification of the way SIDBI will cover loans made by SIDBI under the PRSF. The team has requested such information from SIDBI and will require that the OM, among other documents, clearly set out how that would take place. SIDBI has clarified that its loans under the PRSF would need to meet the same criteria as those of the Participating Financial Institutions (including, for example, in respect of sub-project eligibility).
7	The intermediate indicators outlined on page 15 of the project appraisal document are based on financial metrics and not well aligned with the key outcome indicators, which report on environmental outcomes. We request that the IBRD review the results based management framework, accordingly.	Thank you for the comment. The team will review the Results Framework and ensure alignment and consistency of the indicators and metrics.s
8	At this fairly early stage, the nature of the technical assistance is not well defined and we would appreciate more information on:	The participating financial institutions (PFIs) will be selected from a broad set of large, well known commercial banks and NBFCs in India, using an eligibility criteria which will include factors like past experience

	Financial institutions that may be involved in the project (including on operational procedures to implement the project); and, Benchmark of existing ESCOs on the market (sectoral, technological and geographical positioning, size, financial health…).	in EE and renewable energy lending, capacity, number of EE projects successfully implemented, etc. and will be included in the Operations Manual. The PFI eligibility criteria will ensure that factors generally considered in detailed due diligence of FIs are also incorporated. ESCOs in India are currently accredited by the Bureau of Energy Efficiency (BEE) on a regular basis as per their benchmarking criteria. In PRSF, the eligible ESCOs will be the BEE-certified ESCOs. Currently, there are about 140 ESCOs which have been certified by BEE and they range from small to big ESCO operations, which cover all end use sectors, and from all over India. In the TA component (EESL TA component is for $2 million and SIDBI TA component is for $4 million) some analysis may be included to develop some simple system of "rating" of ESCOs, using global experiences and best practices from other countries.