Small-scale Renewables Financing Facility

Small-scale renewable energy can play a key role increasing energy access and driving low-carbon development. However, obtaining adequate financing for small projects can be a major challenge.

This instrument aims to increase investment in small-scale renewables from 1-20MW that typically do not have access to project finance. It will do so by increasing access to long-term debt and construction finance through a "Discounting Facility" and a "Mezzanine Facility." At this stage, only the Discounting Facility has been developed while the Mezzanine Facility will be developed in a subsequent stage.

The Discounting Facility will allow operational renewable energy projects to refinance into long-term debt and increase its financial leverage by "discounting" its future cashflows from a power purchase agreement. These cashflows will serve as collateral, reducing the amount of equity needed and improving financing terms. This approach is very attractive, for example, in countries like Nepal, where banks only provide loans for 5-7 years – much too short for renewable energy – and Indonesia where bank collateral requirements approach 50% tying up equity capital that project developers could use to invest in abundant solar, wind, and hydro resources. These barriers are common in other markets including most of Africa, Southeast Asia and Latin America.

The Discounting Facility refinances operational projects, significantly improving financing conditions and freeing up equity.

While this instrument focuses on refinancing, its aim is to increase new investments. It will do so by working exclusively with project owners interested in investing in new projects. Investors with suitable portfolios of projects will be able to refinance them and free up excess collateral, which would have to be invested in new projects as a condition to accessing the facility. A review of projects with potential for refinancing found more than 100 projects totaling 540MW in Nepal and Indonesia – two of the most promising markets for a pilot.

A USD 100 million pilot can mobilize USD 261 million of investment in new small-scale renewable projects, which can generate 18 TWh of clean electricity and reduce 11 million tons of CO_2.

Lab Secretariat estimates indicate that a regional pilot with USD 10 million in donor funds and USD 90 million from development finance institutions and/or commercial investors could mobilize USD 90 million in equity and up to USD 260 million in total investment for new small-scale renewable energy projects. The instrument can reduce the cost of renewable energy by up to 20% in the long-term while improving project financials and easing capital requirements.

The Discounting Facility is at an advanced conceptual phase with a high-level operational and financial structure already defined. The next step of development is undertaking detailed due diligence to assure investor needs, develop a deal pipeline and ensure market additionality as this instrument is highly market specific.

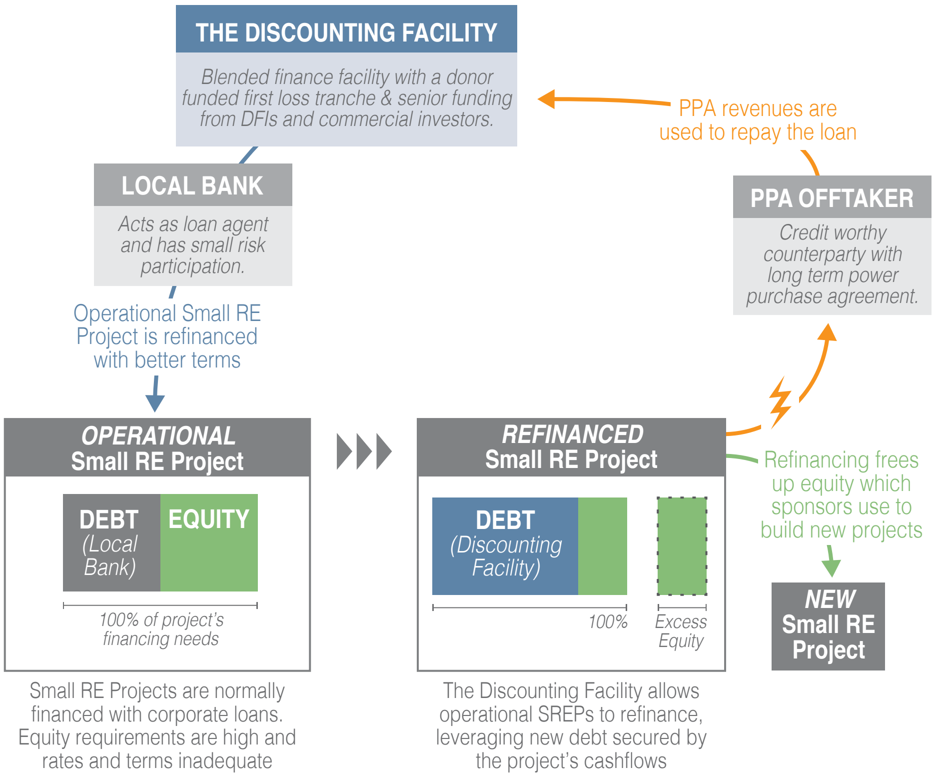
A pilot of the Facility could be operational by 2017. To implement a pilot of this instrument, a donor-funded first loss tranche of USD 10 million is being sought as well as start-up and due diligence funding. Regional implementation partners are also needed.

DESIGN

The Discounting Facility is based on the premise that a renewable energy project that is operational and has a power purchase agreement carries limited risk.

Large-scale renewable projects already have access to financing vehicles that allocate risks reasonably well. They are often financed using bridge loans for construction and are then refinanced at better terms post-completion. However, better terms are not normally available to small projects. The Facility will offer a financing package to small projects that recognizes the reduced levels of risk post-completion. It will use a corporate finance approach to simplify financing and due diligence, but base the financing decision on the cash flows of the project rather than the balance sheet of the sponsor.

The Discounting Facility will be structured as a blended finance facility with a donor-funded first loss tranche and senior funding from development finance institutions and commercial investors. It will be managed by a fund manager or a development finance institution with some regional presence. Loan origination will be carried out by one or more local banks in each target country, which will act as agents and be responsible for interfacing with borrowers, establishing eligibility and disbursing funds. The local bank will receive an origination fee and will also guarantee a portion (10-20%) of the loan. Once a project is refinanced, the sponsor will pay back the loan using power purchase agreement revenues and invest equity taken out from the operational project into new projects.



__The Global Innovation Lab for Climate Finance__ is a public-private initiative that supports the identification and piloting of cutting edge climate finance instruments. It aims to drive billions of dollars of private investment into climate change mitigation and adaptation in developing countries.

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