Meeting Summary

Venture Capital for Renewable Energy and Energy Access in Africa

EUEI PDF Informal Roundtable Discussion, 26.03.2013, Hotel Bloom, Brussels

Moderator: Andrew Reicher / Participants: see last page

1) Key Messages

- Conventional way of "doing energy business" is not sufficient, in view of access and generation gaps, delays of large projects, and a shortage of a viable project pipeline

- More projects, a greater project diversity, and more private sector participation is required to meet both African industries' requirements of baseload power generation, as well as the needs arising from bridging the energy access gap

- Small and medium sized, innovative projects are difficult to handle for conventional finance, both development as well as commercial banks, due to their inherent disadvantage in terms of the ratio between complexity, risk and transaction costs on the one hand and deal volume on the other

- In particular early stage project financing remains a major challenge, as perceived and actual risk is highest at that stage and the "appetite" of external financiers accordingly is lowest

- New and innovative ways of managing risks and financing are needed, with parallel support to policy and technical capacity development to address the root causes of the risks

- There is no shortage of capital in general, and there are also established as well as emerging players ready to engage in early stage / high risk project financing, e.g. "angel" or "impact investors", both individuals as well as funds

- There is however a lack of linkage between such capital sources and the projects "on the ground". There is a clear need to facilitate exchange and possibly create direct links between potential financiers on the one hand and projects or project developers in Africa on the other

2) Detailed Discussion Summary of Challenges and Action Points

General Challenges & Opportunities

1) Lack of common understanding of market development, vision and objectives, the envisaged process and the role of different actors.
   - Contradiction or synergy between bottom-up vs. top-down? Africa needs baseload capacity for development; no dogmatism or trade-offs either way (e.g. renewable vs. conventional energy); need to find most appropriate solutions on cost-benefit basis, and an appropriate vision across the market segments to reflect this.
   - A better understanding of and distinction between different market segments is imperative. This in turn has to be matched with instruments available from donors and other sources (e.g. angel/impact investors).
   - Do instruments fit the "renewed drive" of supporting energy access and renewable energy market development in Africa, is there still an instrument gap?
2) Harness the opportunity of skilled and financially endowed returnees / African expats coming home.
3) There are substantial opportunities to be harnessed: "social impact investment does not have to yield low returns"
4) Need to ease access to funding, as it is difficult for the EU and yet inevitable in order to compete with China (where "money [at times is available] on the basis of coffee and a handshake").

Access to Information

5) Lack of transparency / access to information in terms of
   - Donor activities
   - Government policies
   - Private sector initiatives, including projects and project pipelines

→ Action points

- JPM has done a study on impact investments. Possible follow-up with JPM on below need for "match-making"
- Review literature, publish / share and if need be develop activity mapping (e.g. along these three categories)

Policy and Regulatory Environment

6) Duration of project development (~7 years) is a key problem and cost driver for both small and large projects; in turn, a key driver for delays are issues in the policy & regulatory environment
   - Example: despite efforts (e.g. introduction of FiTs) lengthy negotiations often persist: be it due to weak design or because precedents need to be created → persistent lack of capacity.
7) Governments need to provide viable and transparent tariffs to attract investment, while also balancing socio-economic preferences

→ Action points

- Support for governments in the form of short/medium-term TA (e.g. flexible, demand driven policy support services) to help create an attractive, coherent and reliable environment.
- The first projects have to be carefully guided through the systems to create precedences → creating public goods.

Project Development

8) Capacity constraints, lack of experience, established procedures and other factors in the enabling environment continue to hamper project development and jeopardize a healthy project pipeline

"DFI need to spend more ahead of lending money"

9) Governance / organizational aspects in project development are

→ Action points

- Enhance project development skills in Africa, both technical and financial, as well as skills of local banks and project proponents
- Need more technical assistance for project development, i.e. smart subsidies / grants for project preparation and business development, compilation and access to information, and the enabling environment

often underestimated, e.g.

- differences in the “doing business” attitude/culture between project developers and financiers
- complications of multinational settings or
- conflicts arising in the nexus of project developers vs. technology providers vs. regulators vs. financiers.

(e.g. standards).

- Need for more to be projects developed, financed and run locally →need for active support for local project developers, energy SMEs and local banks in early stages of market development.

Financing (General)

10) DFIs want to increase activities in smaller scale RE/access projects, but traditionally are not internally “wired” for these projects nor have the “appetite” for the associated risks
    - Transaction costs (i.e. for financiers) arising from small projects are disproportionally high, i.e. are practically “the same” for a project of 500.000 as for one of 5 Mio.
    - The risks, due to the lack of experience and track record, are actually much higher in relation to the deal volume

    “You are too small, too young, and too risky”

11) ‘Financing’ actually refers to a range of different financing needs, depending on type and size of project, and stage of project development (project development financing vs. investment financing) as well as various market segments and project models. Needs for start-up and roll-out of business models/projects differ.

12) Additional constraints in funding SME:
    - Not possible to do / manage remotely, i.e. from the EU
    - Donors want to support SME, yet suitable intermediaries (e.g. commercial banks) are reluctant or lack capacity
    - Different assessments and preferences of business models of start-ups: e.g. project developers may insist on hybrid business models for diversification, whereas investors may insist on focus for a coherent business model
    - Conflict for partners / donors: nature of start-ups vs. track record requirements.

→ Action points

- Getting to scale: need to design / promote innovative approaches for packaging and bundling projects and/or financial intermediaries at local level (e.g. commercial banks) capable of financing smaller projects
- Local financiers (e.g. commercial banks) need to be informed and supported in developing in energy sector (little experience to date)
- Identify and avail different financing solutions with different balances of up-front and working capital

- Possibly semi-commercial finance, incl. CSR, can help bridge the gap.
- Other vehicles needed to take on risk (e.g. philanthropic angel investors)
- Additional and innovative instruments are needed to hedge the various risk elements, e.g. political risk or currency risks etc.
- DFIs could work through local financial intermediaries

Venture Capital Specific Financing

13) Important parameters for venture capital investors include:
    - Need to understand business models, manage diversity and complexity
    - Require strong track record and a strong team
      → poor match with many RE projects; generally new by definition and thus don’t have track record.
    - A clear vision for the exit, incl. how to sell the project is required

→ Action points

- Financing is available, also local financing, but a concerted effort involving new players such as angel investors / impact investment funds is needed
- Need to bridge the gap between development partners and philanthropic actors, e.g. through foundations and/or networks.
- Build up information clearing house link opportunities (i.e. projects and project developers with angel investors.

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