FINANCE IN FOCUS

USING INNOVATIVE FINANCIAL STRUCTURING TO RESPOND TO THE CHALLENGES OF DECENTRALISED ENERGY PROJECTS – MWENGA AND MALILE

Decentralised renewable energy has a pivotal role in enabling countries in Sub-Saharan Africa to significantly increase power generation capacity and deliver energy access to rural communities, thereby delivering improved livelihoods and supporting economic growth. As REPP's investment manager, Camco Clean Energy works with distributed energy companies to help them build their businesses and generation and distribution assets through creative financing.

A key challenge currently hindering progress across the sector is linked to the fact that most decentralised projects are carried out under a structure whereby the company generating the electricity is also the one selling it on directly to households and businesses. The demand from these end-users is typically uncertain since they buy power when they need it, rather than signing a long-term purchase agreement, meaning cashflow is unpredictable. As a result, financiers (particularly lenders) need to be more flexible in their approach and have the confidence to do so.

A good example is the Mwenga project, a ground-breaking 2.4MW wind farm providing clean power to 4,500 rural homes and businesses connected to a private rural distribution network in Tanzania. In the face of uncertain demand from the network, the REPP team developed a structure with variable interest rates linked to demand. By providing a USD 1.2 million mezzanine loan from REPP with a base case interest rate relatively low compared to the risk-return profile of the project, developer Rift Valley Energy and its investors were able to meet their hurdle rate, thereby attracting further investment. As electricity demand increases, the interest rate increases proportionately via a step-up mechanism that was determined using an analysis of past demand and assuming a certain growth rate.

This relatively simple structure gives investors and the investee what they both seek: investment in a relatively new and untested structure, with a potential upside to reward the investor for the risk it takes.

Another challenge facing the sector is the need for more complex structures to enable the financing and construction of renewable energy technology to operate alongside existing fossil fuel power assets.

A case in point is the Malile project being developed by LIDERA Green Power PCC in Madagascar, which is hybridising three heavy fuel oil (HFO) plants that provide power to three cities with solar power via isolated grids. The financing structure involves the provision of a USD 6 million bridge loan at the holding company level. This funding is then on-lent to each special purpose vehicle that owns the PV assets, each of which has a rental agreement with the HFO operator. The solar plants sell the generated electricity to a local company which then on-sells it to the Malagasy utility, Jirama.

Unfortunately, there is no one-size-fits all solution when it comes to financial structuring to counter demand uncertainties and greening of decentralised power assets, which means that constant innovation is required for the decentralised energy sector to thrive. These two examples nonetheless show the potential that can be realised through creative financing and investor flexibility.

VARIABLE INTEREST RATE LOAN

Borrower:	Mwenga Hydro Limited (part of Rift Valley Energy Group)
Lender:	Renewable Energy Performance Platform
Facility type:	Mezzanine loan
Amount:	USD 1.2 million
Tenor:	10 years
Interest rate:	Variable, with a floor
Location:	Tanzania
Use of funds:	Financing of construction and the costs and fees incurred with preparing the facility agreement and other security documents
Arranger:	Camco Clean Energy
Legal counsel:	Norton Rose Fulbright
Co-investors:	CRDB Bank PLC, Eastern and Southern African Trade and Development Bank

SOLAR HYBRIDISATION STRUCTURE

Borrower:	LIDERA Green Power PCC
Lender:	Renewable Energy Performance Platform
Developer:	LIDERA Green Power PCC
Facility type:	Bridge loan
Amount:	USD 6 million
Tenor:	2 years
Interest rate:	Fixed
Location:	Madagascar
Arranger:	Camco Clean Energy
Legal counsel:	Trinity International LLP