

# PRIVATE INVESTMENT MOBILISATION INSTRUMENTS THAT WORK

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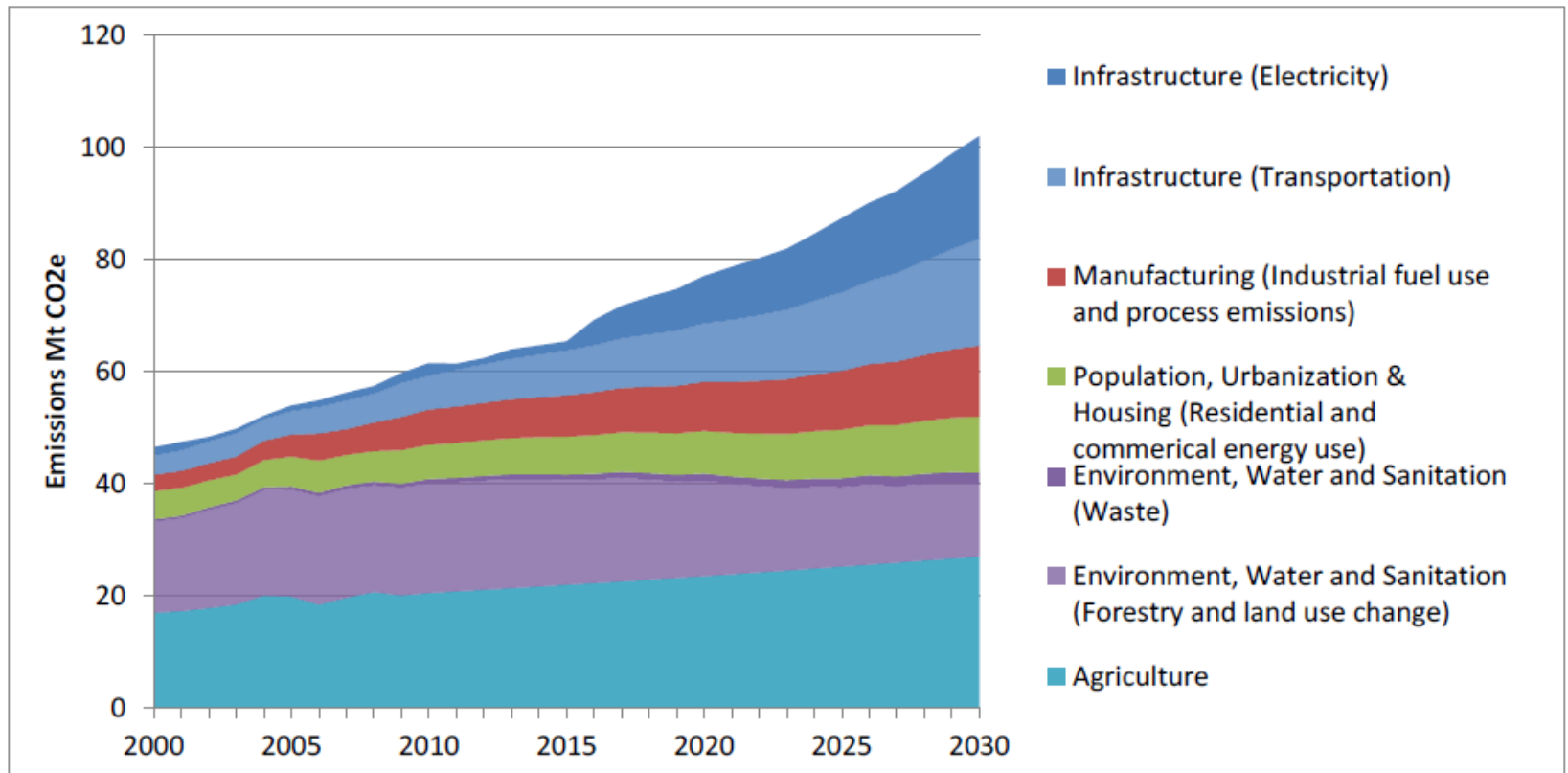


# Introduction

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- Kenya is highly vulnerable to the impact of climate change, particularly its main economic sectors that include agriculture (that contributes 24% to the GDP), energy(15%) and tourism (12%).
- The costs of climate change in the country could be equivalent to a loss of almost 3% of GDP per annum, impacting negatively on Kenya long-term growth prospects as captured in Kenya Vision 2030 of being a *“newly industrializing, middle-income country providing a high quality of life to all its citizens by 2030 in a clean and secure environment”*
- The total estimated investment costs required to adapt to climate change impacts is estimated to be 1.085 trillion Kenya Shillings (US \$12.76 Billion) for the period 2013 to 2017.
- One key source for the climate change funds is the private sector. Kenya has a vibrant, active and dynamic private sector contributing over 80% of the GDP through the various vibrant sectors.

# Emissions levels per sector



Source: GoK NCCAP Mitigation Analysis 2012

**Figure 1: BAU GHG Emissions by MTP2 planning sectors between 2000 and 2030**

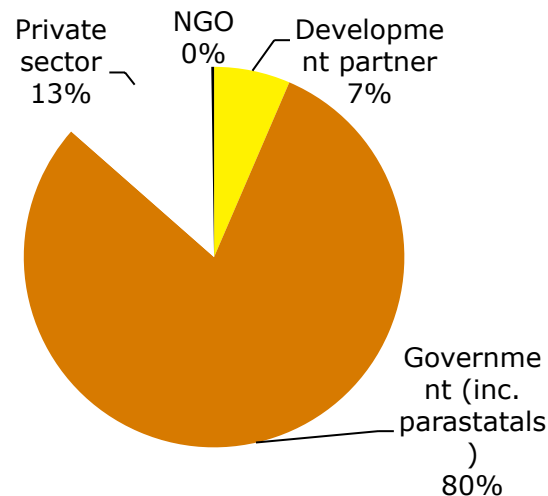
# Climate Financing in Kenya

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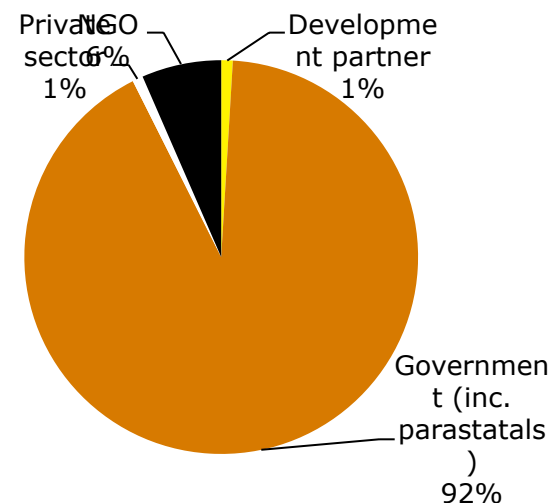
- ❖ Kenya relies heavily on external support, either through bi-lateral agreements or global funds. This funding is highly unpredictable and volatile depending on international commitments and priorities of the donors.
- ❖ Currently there is no comprehensive tracking system able to identify, capture and monitor external climate change financing in Kenya. Plans are though underway to establish the same.
- ❖ The government budget currently records external financing at the project level by sector and by donor.
- ❖ Development partners play a significant role in funding climate change activities in Kenya.
- ❖ There are currently about 120 climate-relevant projects in Kenya, with a value of \$2.5 billion, mainly across energy, agriculture, forestry, coasts and water.

# Current channel of financing & implementing agents

- External finance for climate change is provided both bilaterally and through multilateral funding mechanisms.
- Multilateral (40%) Bilateral (60%)
- The majority of climate-financed activities are implemented by the government, followed by the private sector and NGOs.



Mitigation



Adaptation

# Kenya's experience

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- ❖ The focus on the private sector in the adaptation as well as mitigation debate is wholly relevant.
  - ✧ *The private sector accounts for 85% of all investments worldwide.*
  - ✧ *90% of people in developing countries depend on private sector generated income.*
  - ✧ *The private sector represents close to 75% of global climate finance flows.*
- ❖ Relative to a number of comparator countries, Kenya is already a good place for the private sector to undertake low carbon investment.
- ❖ The features that support private sector investment in Kenya include;
  - ✧ *its high GDP and energy demand growth,*
  - ✧ *its excellent renewable energy resources and high energy efficiency potential,*
  - ✧ *its fairly favorable regulatory environment and its relatively well-developed financial sector.*

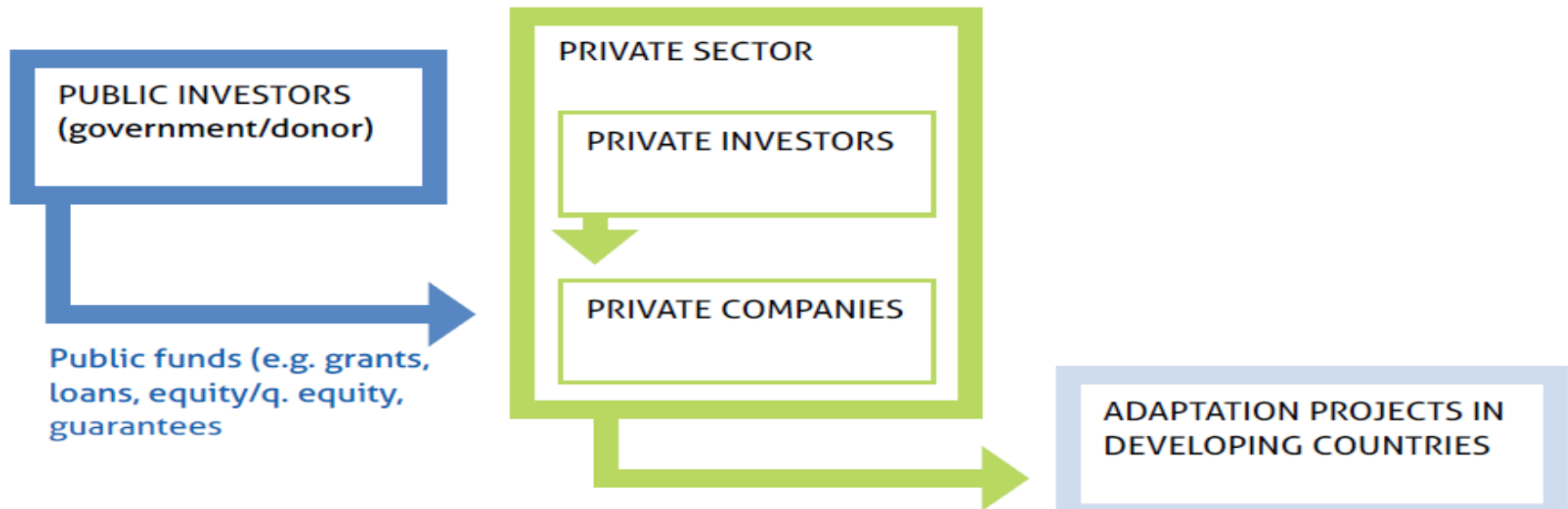
# Mechanisms/Tools

**Mechanisms/Tools** to increase the contribution of the private sector to meet the adaptation needs can be divided into two different groups;

**1. Direct instruments**

- use public funds to incentivize private sector investments in adaptation-related projects directly.
- They entail the use of public funds to increase private sector participation in adaptation projects

DIRECT: public funds are used to support private sector participation in adaptation projects



# Direct Instruments

Type	Definition	Examples
Grants	A transfer "made in cash, goods or services for which no repayment is required." <sup>18</sup> It constitutes a direct subsidy to private companies.	<ul style="list-style-type: none"> <li>• Technical assistance</li> <li>• Grants/subsidies</li> <li>• Grants elements in loans</li> </ul>
Debt	"Transfers for which repayment is required." <sup>19</sup>	<ul style="list-style-type: none"> <li>• Loans</li> <li>• Credit lines (loan to an intermediary for on-lending)</li> <li>• Syndicated loans</li> </ul>
Equity	Investments that involve the ownership of shares in a company. Can be made either directly or through an investment fund.	<ul style="list-style-type: none"> <li>• Public equity</li> <li>• Private equity</li> </ul>
Quasi-equity	Instruments with equity or debt features that have a lower repayment priority in case of liquidation than debt, but higher than equity.	<ul style="list-style-type: none"> <li>• Debt-based: <ul style="list-style-type: none"> <li>– Subordinated or junior loans</li> <li>– Mezzanine loans</li> </ul> </li> <li>• Equity-based: <ul style="list-style-type: none"> <li>– Preferred stocks</li> <li>– Convertible bonds</li> </ul> </li> </ul>
De-risking	Instruments intended to reduce the risk profile of the private sector investment with the idea of facilitating finance.	<ul style="list-style-type: none"> <li>• Loan guarantees</li> <li>• Investment guarantees (political and macroeconomic insurance)</li> </ul>

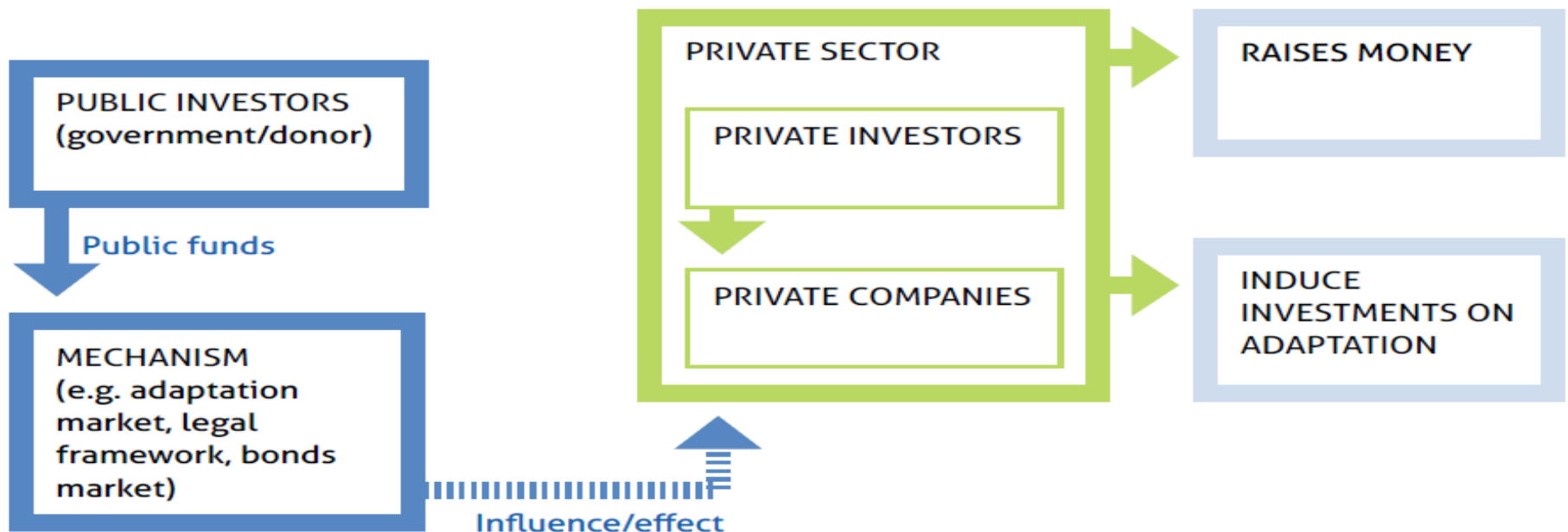


# Mechanisms/Tools

## 2. Indirect Instruments/tools

- Use of public funds to create mechanisms designed to either raise additional adaptation finance or increase private sector investments in adaptation.
- No direct support to the private companies implementing adaptation actions is provided.

INDIRECT: public funds are used to create mechanisms to 1) raise money for adaptation; and/or 2) incentivise private sector investments in adaptation



# Indirect Instruments

Type	Definition	Examples
Market mechanisms	Key feature of market mechanisms (or market-based instruments) is that a price signal is used to promote the production of a certain service or good, or to reduce it (in this case promote adaptation measures). They also can also be used to raise money for adaptation.	Adaptation credit mechanism Carbon market (mitigation)
Bonds	Fixed income financial instruments used to raise money, in this case, for adaptation.	Catastrophe bonds
Internalising adaptations costs	Private investment on adaptation can be increased by encouraging business likely to be affected by climate change to adopt measures to reduce their vulnerability.	Awareness raising Advice and information Accurate climate modelling Legislation
Technology development and transfer	Supporting research and pilot projects can help to lower the risk and deployment costs of adaptation techniques. Also includes dissemination of the technology.	Research Pilot projects

# Kenya' s experience

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- a) **Feed in Tariff Policy in the energy sector**
- b) **Geothermal development model**
- c) **Negotiating and arranging for Partial Risk Guarantees**
- d) **Public Private Partnership Act 2013**
- e) **Kenya Climate Change Fund**
- f) **Policy framework for mini grids ; net metering and wheeling regulations.**
- g) **others**

# Kenya's experience

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## a) Feed in Tariff Policy

- Kenya FIT is a 20 year tenure policy that allows power producers to sell to the national grid and obligates the distributors to buy on a priority basis all renewable energy sources generated electricity at pre-determined fixed tariffs for a given period of time.
- Kenya's feed in tariff policy is targeted at stimulating electricity generated by traditional wind, small hydros and biomass resource generated electricity, as these are the predominant energy sources in the country along with imported petroleum.
- Its objectives are to; facilitate resource mobilization by providing investment security and market stability for investors in Renewable Energy Sources (RES) electricity generation, reduce transaction and administrative costs by eliminating the conventional bidding processes and encourage private investors to operate the power plant prudently and efficiently so as to maximize its returns.
- The key aspects of an FIT include access to the grid, long-term power purchase agreements and a set price per kilowatt hour (kWh).

# Kenya's experience

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## a) Feed in Tariff Policy... cont'

- The advantages of this policy include: environmental integrity including the reduction of greenhouse gas emissions, enhancing energy supply security by reducing the country's dependence on imported fuels while coping with the global scarcity of fossil fuels and its attendant price volatility and enhancing economic competitiveness and job creation.
- FIT has different tariffs per source of energy so that;
  - *Wind energy attracts a fixed tariff not exceeding US Cents 12.0 per Kilowatt-hour of electrical energy,*
  - *Biomass energy sourced from agricultural waste, municipal waste, biofuels and fuel wood, fixed tariff not exceeding US Cents 8.0 per Kilowatt-hour,*
  - *Small hydro projects a stepped fixed tariff of between 8 and 12 U.S cents applied depending on the capacity produced by a firms and between 6 and 10 US cents per kilowatt hour for non-business firms, and For geothermal energy, fixed tariff not exceeding US Cents 8.5 per Kilowatt-hour.*
  - *All of these tariffs apply in bulk of electrical energy supplied to the grid operator at the interconnection point and apply for between 15 and 20 years.*

# Kenya's experience

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## a) Feed in Tariff Policy... cont'

- Some of the FIT projects have started operating, for example the Mumias sugar cogeneration plant adding 26mw to the grid out of the 38mw it produces.
- Various other projects such as Orpower 4 Inc (geothermal power plant) and projects under the other sugar millers are yet to start.
- Other renewable sources such as Biogas are gaining considerable importance in the rural areas where, for instance, Biopower Limited in Kilifi County leads the way generating 150 kW from a mixture of sisal waste and cattle dung, while banana leaves have been used to generate 10 kW at Kamahuha in Muranga County. These projects are yet to reach a FIT stature.

# Kenya's experience

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## b) Geothermal development Model

- Kenya's abundant geothermal energy is a viable alternative to hydropower as the main source of energy, though most of the resource base remains undeveloped as yet. It is ranked as the least cost generation source for base load to sustain Kenya's increasing energy demand.
- The speed of harnessing geothermal resources has been too low necessitating the creation of GDC as a Special Purpose Vehicle to FAST TRACK the development of Geothermal energy.
- Through GDC the cost and risk of infrastructure provision (such as building roads to geothermal generation locations, providing security, etc.) and steam extraction is currently borne by the Kenyan government.
- On striking steam, the Government is keen to collaborate with private sector investors through public private partnerships to facilitate further geothermal expansion, and quite a number of firms have expressed interest in this opportunity.
- GDC is in the process of acquiring 12 modern deep drilling rigs at a total cost of US\$360 million to enable drilling of at least 60 wells per year with 140 MW geothermal generation capacity every year.

# Kenya's experience

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## c) **Negotiating and arranging for Partial Risk Guarantee schemes**

■ Def; a risk mitigation instrument that covers private lenders and investors against the risk of a possible government failure to meet contractual obligations to a project.

■ Background issues;

✧ *The global economic recession and the financial crisis.*

✧ *The traditional security package offered to IPPs by KPLC was not considered sufficient by investors due to their perception of high political risk.*

✧ *Low risk appetite on the part of project developers and commercial banks. To overcome this challenge, and given the tight macroeconomic environment and debt ceiling agreed upon as part of an IMF program.*

■ **The Kenyan government approached MDBs to explore alternative options that would address these constraints.**

### 1. **World Bank's** - US\$166 million

1. This combination of instruments unlocked a total financing package of US\$623 million, including US\$357 million in private sector investments and commercial lending.



# Kenya's experience

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## c) Negotiating and arranging for Partial Risk Guarantee schemes... cont'

### 1. *World Bank's - US\$166 million ...cont'*

1. Under the approved structure, IDA will leverage its ongoing sector engagement through the Partial Risk Guarantees.
2. The aim is to provide liquidity support to the projects by backstopping three months of KPLC's ongoing payment obligations.
3. IDA support is complemented by MIGA political risk insurance covering the equity and commercial lending for the projects.

### 2. *AfDB - €20 Million*

1. The facility is to support the Lake Turkana Wind Power Project in Kenya, Africa's biggest wind power project, and involves the development of a 300 MW wind farm comprising 365 wind turbines of 850kW capacity each and a 33kV electrical network.
2. The average electricity production of the project is estimated at 1,440 GWh per year, and will be sold to the grid at a price of .0752 €/Kwh.

\* *Private sector, both domestic and international, has already invested more than USD2.8 billion in renewable energy production in Kenya.*

# Kenya's experience

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## d) Kenya's Climate Change Fund

- ✦ *The KNCCAP recommended setting up of a National Climate Change Fund (NCCF) to cover both Mitigation and adaptation.*
- ✦ *NCCF will provide a mechanism that will help Kenya to direct finance toward climate change projects and programmes by facilitating the collection, blending, coordination of, and accounting for all climate finance.*
- ✦ *NCCF is expected to provide a Kenyan-driven system that will support climate change goal setting and strategic programming, oversee climate change project approval and implementation, measure performance, offer policy assurance and financial control of climate change funds, and assist with partnership management.*
- ✦ *As a separate legal entity, the Fund will develop in a phased approach, providing relatively simple financial instruments, most obviously grants, in an initial phase, before evolving to provide a wider palette of financing instruments.*
- ✦ *The NCCF is expected to help leverage on private sector investments*

# Kenya's experience

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## e) **Public private partnership Act No 15 of 2013**

- \* *Designed to provide for the participation of the private sector in the financing, construction, development, operation, or maintenance of infrastructure or development projects of the Government through concession or other contractual arrangements.*
- \* *Also provides for the establishment of the institutions to regulate, monitor and supervise the implementation of project agreements on infrastructure or development projects and for connected purposes.*

## f) **Policy framework for mini grids ; net metering and wheeling regulations.**

- \* *Currently being developed*
- \* *Energy generation by private enterprises for their own use or for sale to the grid.*
- \* *Saves energy costs, creates additional revenue source for the company and enhances supply of energy, including in rural areas where grid access is limited.*
- \* *Opportunities include mini-hydro, geothermal, solar, biogas and cogeneration.*

## g) **Others**

- \* *Enforcing regulatory instruments, fiscal incentives (e.g. both imported Solar panels and local manufacturing are duty free making climate related investments relatively more attractive)*
- \* *Other supporting legislations and Policies e.g. Carbon Policy, trading platform etc*

# Conclusion

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## ❖ **Still early to judge**

- \* *Many of the instruments in use, or proposed, that will increase the contribution of the private sector to adaptation are in the early stages of development (e.g. climate change fund, carbon trading platform).*
- \* *Others build on the experience of the private sector in development, yet little is known about the specific contribution of each to meeting the adaptation needs.*
- \* *Varying levels of development, and needs of vulnerable communities within a developing country such as Kenya.*

## ❖ **Budgetary constraints**

- \* *Although crucial to reducing vulnerability, some of the indirect instruments (e.g. internalizing adaptation costs or encouraging technology transfer and development) require huge budgetary allocations which are scarce owing to competing priorities.*

# Conclusion

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## ❖ More Research required

- ✧ *More research is required, based on a bottom-up approach from specific needs to specific tools and instruments. It is important to explore how different tools relate to and complement one another in order to make intelligent policy decisions.*

## ❖ Tracking of Climate Finance

- ✧ *It is essential to develop a common methodology to record and track private finance, including adaptation finance. Without such a system, it will not be possible to ensure an equitable distribution of the scarce climate finance available. Nor will it be possible to hold developed countries to account for their commitments and historic responsibility in climate change.*

## ❖ Safeguards

- ✧ *Safeguards of public organizations that support the role of the private sector in adaptation need to be strengthened. Public organizations must in addition improve implementation oversight to ensure projects comply with such safeguards.*

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**THANK YOU**