African Infrastructure Guarantee facility.

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The Guarantee Issue – a personal experience

• In 2015, Ghana had one of the most advanced renewable energy frameworks in Africa. Along with a comprehensive PPA, the country offered one of the highest feed in tariffs in Africa.

• Like various companies, Acropora Capital, allocated resources to exploit the attractive framework and set up offices in Ghana.

• Our team spent eight months in the country, identifying local partners, securing land, permits, and developing two 15 MW solar projects in the North of Ghana in Wa state.

• Having spent a great deal of time and getting the projects PPA ready, we lined up the finance from a European investment fund.

• The Ghanian utility, ECG, was not considered a reliable off-take by our investors and those of other projects. Instead of a sovereign guarantee the government offered Government Consent and Support Agreement.

• At the time the government was having major economic challenges and was negotiating a loan from the IMF. As a result, they couldn’t afford more liabilities on their balance sheets and whole solar sector was put on hold.
Payment Risk – the ultimate obstacle

• One of the biggest concerns investors have is the ability of the off-taker to stick to agreed payment schedule.

• While all infrastructure projects might suffer from this issue (road / fibre optics) it is a very significant issue for the power sector.

• Investors into a IPP are relying on revenue from a long term Power Purchasing Agreement (PPA) with the off-taker who will normally pay for the electricity on a monthly basis.

• All the off-takers in Sub-Saharan Africa are state utilities and considered to not be credible off-takers due to poor balance sheets and payment issues

• Many of the pension funds contacted for the issues paper stated that while they were interested in African power projects, they remain concerned about the lack of credible off-takers.
Off-Taker Issues

There are a few reasons why off-takers in Africa have poor ratings.

1) **Payment collection issues** - many off-takers inefficiently collecting payments.
2) **Non-cost reflective tariffs** - major issue governments buying from IPPs at high price and selling to consumer much lower price.
3) **Budget Issues** Off-takers are not self-sufficient and at mercy to government budgets
4) **Technical Issues** – poor grids and transmission lines = loss of revenue.
The Elusive Sovereign Guarantee

• Due to a lack of credible off-takers, investors started asking for sovereign guarantees from governments. Essentially Ministry of Finance stating if utility defaults they will pick up bill.

• Contingent liability – some governments do not like them as are a long term commitment despite what changes might happen.

• Issues with Donors – sovereign guarantee is a liability on a government’s balance sheets. Can reduce borrowing ability e.g. Ghana. Studies indicate can push economy over threshold in times of economic crisis.

• Even when sovereign guarantees are issues governments still might not pay e.g. TANESCO not paying Songas in Tanzania.
Alternatives to Sovereign Guarantees

• Due to the various issues with sovereign guarantees several alternatives have emerged:

• Letter of support: an alternative to sovereign guarantors is a letter of support however this is seen to have little value in the industry. E.g. Kinangop wind farm arbitration.

• Liquidity facility: gives the project company protection against short term defaults / revenue interruption. World Bank / ATI provide short term liquidity facilities, normally up to six months. Escrow accounts.

• Partial Risk Guarantees- normally offered by DFIs like World Bank / AfDB these will protect the lender up to a certain value.

• Put Call Option: if either side breaches the contract then this gives the project company the ability to initiate ‘call’ option requesting the government to buy back the asset / shares in SPV. Alternatively, the ‘put’ option enables the government to request the same from project company.
Case Study : Azura-Edo (Nigeria)

- The Azura power plant project is a 450-500 MW gas-fired open cycle power plant located in the North Eastern outskirts of Benin City in Edo, Nigeria, with an estimated project cost of US$877 million.

- At the same time, the risks of construction, cost overruns, accidents, or any other incidents as well as financial risks, such as global collapse in credit, will be borne by taxpayers because the government is acting as guarantor.

- This put-call option has now become a template for projects across Africa, and is being used by several investors to develop projects. It is expected that it will change the game in the energy sector and bring many more much needed energy projects to financial close.
While there is quite a pressing need for guarantees in Africa, it is important to point out that even in developed markets like Europe there is still a need for government guarantees to support risky and ground-breaking infrastructure projects.

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If the project went over the insurance level, then the government support agreement would pay the extra. If the project cannot raise debt due to unforeseen reasons then the Secretary of State will provide a back-up temporary liquidity facility under the Market Disruption Facility Agreement.
Infrastructure Initiatives (not dependent on sovereign guarantees)

• Scaling Solar: An initiative by IFC to streamline and de-risk the development of solar in Africa. One ‘stop shop’. Access to suite of World Bank risk guarantees and optional finance.

• African GreenCo: By acting as intermediary off-taker and power trade, the initiative aims to eliminate the reliance on sovereign guarantees. Utilise power pools to give both IPPs and off-takers a credit worthy off-taker and a selection of off-takers to reduce payment risk. South African Power Pool

• African Energy Guarantee Facility: Guarantee by EIB for $1 billion and reinsured by Munich RE. Private insurance solution with 15 year tenor, which is very long tenor for Africa.
NEPAD Guarantee Facility

• Despite some good initiatives already in place, given the large funding gap. There is a need for more solutions and funds for coverage.

• Replicate the African Energy Guarantee Fund financing model: raise capital from DFIs / MDB, to guarantee ATI and reinsurance company. Have long tenors. Not just renewables but all infrastructure projects.

• Tender based – cut out development times, project to project negotiations. Use DFIs to identify and develop projects and then go to tender with risk guarantees pre-allocated.

• How can the facility help innovative intermediary off-takers like Greenco. Can we issue guarantees to them as off-taker?
For Discussion..

• How can the facility help governments bring in more cost reflective tariffs?

• International private insurance companies don’t want to take on Africa, what partnerships can encourage them without donor first loss. (e.g. Allianz and IFC)

• Need to pool countries together for power pools and also share risk burden. World Bank tried in West Africa but failed, what can be done?

• Guarantees are not the only issue – how can the facility improve transmission lines, governance issues, utility technical capability.

• Do we need a more private sector led solution – less reliance on DFIs / Donors. African governments and companies finding sustainable solutions to Africa’s problems.