

Green Africa Power (GAP): Overview

Background and need: More than 700 million inhabitants of sub-Saharan Africa lack access to electricity. There is a shortage of all power generation projects in sub-Saharan Africa, but particularly of renewables. Pronounced market failures inhibiting the growth of renewables in the region are:

1. Lack of cost reflective tariffs;
2. High upfront cost which makes projects harder to finance, particularly when only short term loans are available from local banks;
3. Specific risks e.g. of construction delays and off-taker payment default, deterring potential financiers.

Objective and intervention: GAP's mandate is to encourage renewable energy power generation projects in developing countries in sub-Saharan Africa. It aims to address the above barriers by:

- reducing the upfront cost of capital, while maintaining overall commercial returns;
- providing cover for specific construction phase risks;
- policy dialogue to move towards cost reflective tariffs.

GAP incorporates key design **principles** of clear policy and project additionality (GAP is explicitly restricted to projects which would be highly unlikely to otherwise proceed because of existing market failures), minimum subsidy, demonstration effect, minimum distortion and strong governance.

Instruments: GAP will deploy two financial instruments and one policy instrument, each of which will be individually negotiated and tailored to fit the specific circumstances of the project concerned:

1. **GAP Quasi Equity Loan:** The primary instrument of GAP. Each GAP loan to an Investee Company will be subordinated to any senior debt and any intermediate capital/mezzanine debt loans (other than any shareholder loans) to the Renewable Energy Project but will rank ahead of the Investee Company's equity and any shareholder loans so may be perceived by the Investee Company as a form of debt and by senior lenders and third party providers of intermediate capital/mezzanine debt funding as equity.
GAP will set the interest rate and fees to be earned over the life of the GAP loan such that the expected internal rate of return to GAP is between the internal rate of return expected to be earned by any senior lenders and equity's expected internal rate of return at financial, reflecting the fact that the GAP loan is risk-bearing intermediate capital/mezzanine debt funding.
The tenor of each GAP loan will not be longer than the term of any Power Purchase Agreement signed by the Investee Company with its off-taker for the Renewable Energy Project.
GAP may structure the terms of a GAP loan to allow the shareholders in the Investee Company to reach an agreed threshold equity rate of return on an accelerated basis, subject only to the performance of the Renewable Energy Project, to help offset some of the factors inhibiting investment in Renewable Energy Projects.

GAP will set a repayment profile for a GAP loan which is as rapid as the economics of the Renewable Energy Project will allow. In the event that the Investee Company is able to re-finance its Renewable Energy Project at some point after the start of operations, GAP will require repayment of its loan either in full or so far as the re-financing may permit. GAP may also at any time seek to reduce the amount of any of its Investments on terms which are beneficial to GAP in accordance with the terms of the loan.

2. **Contingent Line of Credit:** A guarantee which provides additional comfort to lenders on top of the debt service reserve account, to be drawn down in case of delays or cost over-runs in construction. If drawn, the advance would have the same features as detailed in paragraph 1. above.
3. **Policy Dialogue:** GAP will encourage host countries to move towards cost-reflective tariffs, providing them with support to do so and buying them time to build political and public support for tariff increases. The off-taker, its government sponsors and regulators might agree a power purchase agreement ('PPA') with a graduated rise in tariffs to the level required for the project to be viable, with the low GAP return enabling the project to achieve financial viability in the early years. The additional cash-flow in the later part of the PPA period would allow GAP support to be repaid and a reasonable return delivered, while allowing the developer to make a fair equity return and supporting on commercial terms a conventional debt package, making up the full amount of capital needed for the project. In this way, GAP will help, over time, to "nudge" client power systems towards cost reflectivity for their renewable energy power plants.

The funding which GAP receives from the UK is part of the UK's International Climate Fund obligation, GAP will seek commitments from projects which they will not register for Carbon Emission Reduction Certificates (CERs) or if they do so, the CERs will be assigned to and cancelled by GAP. For the remaining projects it finances, GAP will require that it be assigned the majority of the available CERs, which may be sold on at the Board's discretion.

Results: GAP aims to support projects which will install ~900MW of renewable energy in DAC I, II and III countries in sub-Saharan Africa in six years, avoiding an estimated 39 million tonnes of CO₂ emissions. It is expected to leverage twice as much private sector finance and an equal amount from Development Finance Institutions. GAP will be a long term source of financing support to projects meeting its Investment Policy to facilitate such projects achieving financial close and being successfully implemented.

Management: GAP is an initiative of the Private Infrastructure Development Group (<http://www.pidg.org>). PIDG is a multi-donor organisation to promote private sector investment in infrastructure in the poorest countries, principally Africa. Like all PIDG operating units, GAP is aimed at supporting specific, discrete projects. The PIDG structure and system of governance involves, wherever possible, PIDG operating units, also known as facilities, being established as public-private partnerships. A competitive procurement exercise is undertaken to select individuals, usually from for-profit private sector backgrounds to manage the facilities, with the optimum combination of effectiveness and value-for-money. The PIDG's governance system, its code of conduct, specific facility's "made-to-measure" investment policy and operating procedures, together with the facility's independent Board of Directors balance the Donors' principal concern for development



impact and diminution of the market failures reducing private investment in infrastructure in the poorest developing countries with the manager’s pursuit of profit. An advantage of the PIDG system is that private sector individuals make commercial judgments and development policy officials make development policy decisions which come together to create shared value. GAP is a PIDG facility under the PIDG Trust, with an independent Board and, under the Board’s aegis, a manager procured competitively. Project level decision making will be the responsibility of the GAP Board, in response to recommendations from the Manager. GAP became operational in 2014.

Funding: The UK has approved funding of up to £95 million to capitalise GAP and £3 million for Monitoring and Evaluation and knowledge management. This includes contributions from DFID’s Climate and Environment and Private Sector Departments and from the Department of Energy and Climate Change (DECC), via the International Climate Fund. The Norwegian Ministry of Foreign Affairs has also committed NOK 300 million (~ £25 million) of funding.

