Blended Finance in Clean Energy: Experiences and Opportunities

Climate Policy Initiative
April 2018
What is “blended finance”?

The use of public/philanthropic funds to mobilize multiples of additional private capital.

Focus on concessional capital, extended at below-market terms:

- **Directly**, within the capital stack of an investment vehicle
- **Indirectly**, to catalyze private investment, e.g. through guarantees and project preparation grants
Why blended finance?
Why blended finance?

Mainstreams and mobilizes private investment in impactful sectors, and scales impact more efficiently and effectively.

Successful examples of blended finance address:

- **Demonstration** of project viability, reducing risk perception and building investor confidence.
- Transfer of “pioneer risk” on new technologies or business models to public sector investors.
- Risks and barriers that the project cannot reduce through its implementation, but can be **transferred** to public sector parties through blended finance tools.
**Why blended finance for clean energy?**

➢ Despite steep declines in the cost of clean energy, important barriers to investors remain, especially in sub-investment grade countries.

(*) indicates that the intensity has been qualitatively determined (N/A) indicates data not available

![Diagram showing key barriers and risks for India, Cambodia, and Kenya]

- Key barriers and risks
  - Political and social risks
  - Administrative barriers
  - Policy, regulatory risk
  - Access to capital barrier
  - Construction, financial, and operation costs increase and volatility
  - Currency Risk
  - Counterparty, Offtaker, or Credit Risk
  - Revenues Lack of Attractiveness and Volatility

- Relatively low barrier or risk
- Relatively high barrier or risk
Clean energy also has features that amplify risks to investors

- High risk at early stages
- High upfront costs
- High transaction costs for investors except for largest projects
- Long time horizon
The blended finance landscape in clean energy
We looked at 75+ blended finance initiatives in clean energy to identify gaps in offerings.

We found:

- Not enough focus on most cited barriers, especially currency and off-taker risk.
Blended finance clean energy landscape findings

- Not enough use of guarantees, which have track record of effectiveness in mobilizing private investment.
- Guarantees are 5% of commitments in multilateral institutions but generate 45% of private sector mobilization.
Blended finance clean energy landscape findings

➢ Most initiatives are too small to attract institutional investors.
Examples
There is a great deal of innovation occurring today to address these gaps.
Climate Investor One addresses transaction costs and risks through scale and diversification.

- Whole of life funding through three interlinked funds, matching project life stages
- Recycling of capital
- Active support to development stage

Source: Climate Fund Managers (2017)
Energy Savings Insurance addresses performance risk of energy efficiency investments.

➢ Technology providers purchase insurance to back contractual guarantees to SME clients
➢ Replicated in more than 10 countries on 3 continents, mobilized more than $180m, more in the pipeline
Blended Finance in Clean Energy

- Allows lending in local currency
- Mobilized over EUR 100m in investment
- Currently developing follow on Common Risk Mitigation Mechanism

Long Term Foreign Exchange Risk Management addresses currency risk with a global hedging facility.
Opportunities for the Future
Focus on high potential regions and countries for energy access and climate change mitigation.
Prioritize instruments that address the key risks to investors.

➢ **Risk mitigation instruments** such as guarantees, insurance, and currency hedging.

➢ **Liquidity-generating and aggregating instruments** to bring in new investor classes and recycle capital for new investments on the ground.

➢ **Early stage risk financing** for new projects, technologies, and business models.
Target long term sustainability and scale.

➢ **Scale ideas that work.**
  ➢ This can require different approaches from innovation.

➢ **Develop and support intermediaries.**
  ➢ They can bridge investors and pipeline, the public and private sectors, and international and local institutions.

➢ **Streamline and mainstream.**
  ➢ Reduce transaction costs, incorporate technical assistance, train and maintain staff, align institutional incentives, standardize designs and agreements.
Apply the lessons of clean energy to sectors across the SDGs.

- Adaptation
- Cities
- Energy Access
- Sustainable Land Use
Questions?
Contact

Bella Tonkonogy
bella.tonkonogy@cpiclimatefinance.org

Alex Clark
alex.clark@cpiclimatefinance.org