

Increasing Energy Efficiency Financing in Brazil: Advances Since the Beginning of the 3CEE Project and Next Steps

Alan Douglas Poole

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Challenges Faced by 3CEE from the Outset

The context for increasing access to financing (especially bank credit):

- Difficult general environment for bank financing – very high interest rates and strict guarantees required.
- Gap in understanding between ESCOs & financing agents of the requirements and opportunities of the other.
- ESCO project developers are small and poorly capitalized.
 - Small size of market relative to potential; relatively slow growth.
 - Scarce and fragmented information about effective and potential market
- Despite substantial public resources for EE in general, no clear commitment or policy to promote the transformation of the market for investment in EE projects.
 - From 2003 through 2005, government priority was to create & operationalize a new institutional supply model for electricity sector.
 - Impediments to procurement of EE projects in the public sector.
 - Positive step: part of utility EE wire-charge applied in performance contracts with consumers. Important resource for subcontracted ESCOs however little movement to leverage with bank financing. Was also politically vulnerable.

Main Lines of Activity

Preliminary work in 2002-3. Most activity since early 2004

- Maintain working level dialogue between stakeholders – especially ESCOs and financial community (Core Group).
- Prepare and review in-depth studies of some subjects identified in the dialogue:
 - Survey of characteristics of the ESCO sector to improve information
 - Guarantee facility for bank credit
 - Utility EE wirecharge
 - Attracting equity for EE projects
- Training of ESCOs to strengthen skills in business development and financing skills
- Support dissemination efforts of ABESCO in public forums and via an electronic newsletter and a new magazine.
- Engage with government entities to present and/or collaborate on proposals; participate in relevant public hearings.

Results of the 3CEE Project

- The gap in understanding between agents has narrowed.
 - **Banks** understand more about characteristics of the ESCO business and EE projects for investment
 - **Government** is more aware of potential benefits of promoting ESCO development and strategic needs for this to occur.
 - **ESCOs** understand better needs for “bankable project”; pros & cons of possible financing approaches and innovations. Received some training
- New ideas have been generated and debated. Clarification of what is needed to increase investment in the EE project sector.
 - Diverse options have merit – not mutually exclusive.
 - Besides financing, need to improve marketing & management capabilities
- A concrete proposal has been made for a pilot credit guarantee mechanism, to be operated by the BNDES.
- Successful mobilization to prevent the extinction of the EE wirecharge.
- Strengthening of ABESCO as an agent representative of the EE services sector.

The main impacts of 3CEE were always to be indirect - small resources. The benefits would mostly result from interacting with and possibly catalyzing other initiatives.

Broader Recent Advances in Brazil

In addition, there have been broader advances in Brazil which improve the outlook for achieving increasing sustainable EE financing.

- Some commercial banks have been developing new credit products, loan appraisal practices & flexibilizing guarantee requirements.
 - Interest rates decreasing, but still high & a period of uncertainty looms.
- Successful procurement of an EE performance contract by a public sector water utility. Advances in the adaptation of “public-private partnerships” (PPP) for public sector EE projects
- Signs of greater government priority for EE in general & specifically for policies to effectively support development of the EE project market.
 - Both financial and other business development aspects

As the 3CEE project ends, the outlook is favorable for progress in transforming the EE project market.

- Follow-up initiatives are beginning to be discussed/developed by both national agents and international donors.
- There is a “pool” of people and ideas to build from. Lessons have been learned about what is needed - what may work and what probably won't.

Recommendations for Next Steps

Build further on this platform & move to implement investment programs. Two central ways of doing this in the short term:

- For the BNDES to proceed with the implementation of a pilot energy efficiency financing program which addresses the issue of the guarantees required, as a way to engage banks at a practical, operational level with concrete EE investment projects.
 - A “lesson learned” is that it is necessary to have concrete projects to actively engage financial institutions in innovative products.
 - The experience gained with the pilot will be valuable.

- For the Government to consider undertaking, possibly together with support from the World Bank and other donors, a strategic review of energy efficiency investment development, as a means to consider the best way to respond to ever-mounting needs over the next 5-7 years.
 - In undertaking such a review it is important to address energy as a whole, as it is viewed by consumers, even though electricity and fuel efficiency issues have been managed separately in Brazil. Ideally, the efficiency of water use should also be included.

Some Key Issues for the Strategic Review

Some initial suggestions for areas of focus are:

- Evaluate current demands and trends for mobilizing energy efficiency investment in the private sector,, and tools to facilitate further investment using medium term debt financing.
 - Examples, besides credit guarantee mechanisms, include a receivables fund and project performance insurance.
- Evaluate future use of the electricity wire charge to promote energy efficiency investment and increase leverage of this important resource.
 - Identify priority objectives and review alternative institutional mechanisms for achieving them.
- Identification of pricing issues hampering energy efficiency investment, and recommendations to overcome them,
- Means to accelerate energy efficiency investment in the public sector, especially in public buildings and water utilities.
 - Includes legal issues in procurement and issues of program management and organizing financing.

Meanwhile.....

..... It is important to follow-up on some of the specific initiatives of the last few years, regardless of broader efforts. Examples include:

- Support to consolidate Brazil's ESCO industry.
 - Has survived the test of time and many operational difficulties to remain an important, market-oriented player in the EE arena;
- Overcome the procurement hurdles for public sector EE projects.
- Support training initiatives for ESCOs on how to develop projects for financing. Also,
 - consumers on when and how to contract ESCO services.
 - continued development and refinement of project appraisal methodologies in collaboration with commercial banks.
- Support the development of improved information about:
 - the potential of the market for EE retrofit projects;
 - more systematic accompaniment of projects being implemented in order to provide improved information for financial agents on results being obtained.

There are possibilities for international donors to collaborate on these and other initiatives which can and should be pursued, though the resources required to promote change are not large.