March 7, 2016

APPROVAL BY MAIL: DPSP II KENYA: CONCESSIONAL FINANCE PROGRAM FOR GEOTHERMAL GENERATION (CTF) (AFDB)-PCTFKE604B

Comments Received from the United Kingdom

Additional Comments received from the United Kingdom

March 7, 2016

Hi CIF Admin unit,

Thanks to the AfDB for providing answers to the UK's original questions. We are still going through the responses but have two follow up questions at this stage:

- Regarding Question 6, the response provided doesn't answer our question. What is the reason underlying the GoK's strategic decision not to provide a Sovereign Guarantee? If the Letter of Comfort is unable to provide a guarantee, what purpose does it serve?

- In response to our question 10 'Can useful lessons be learned from existing projects?' the answer provided was that the Oilkaria geothermal project was fully funded by the project owner with recourse to equity only. Given this, we'd be interested to know why the current projects require concessional finance (e.g. how it differs from the Oilkaria project which didn't require it).

Thanks,

Lawrence

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February 29, 2016

Dear Mafalda,

Thanks for sharing this proposal. We have a number of questions for clarification that we'd like to see answers to before we approve:

- Of the $29m CTF funding, $15m will go to be for long term concessional debt. What will the $14.65m be used for (is this for a second geothermal project- it's unclear to us)?
- How many projects will the facility cover? Paragraph 2.2 mentions "two geothermal generation projects". In paragraph 2.3 it says "The three projects are expected to have a combined installed capacity of 105MW". In paragraph 2.4 it says "Following a preliminary assessment of the two projects . . ." Paragraph 2.9 mentions 2 transactions over an investment period of one year. Paragraph 5.12 mentions "AfDB will aim at supporting one to two projects with this programme".

- On GHG emissions, page 2 of the Cover Sheet mentions 11,528,160 tCO2 as the GHG emissions savings over the lifetime of the project in section 12. Under the Core Indicators it mentions 8,646,120 tCO2 over the lifetime of the project. Can the project team please clarify?
- On the emissions reductions calculations (in Annex 2), could you explain the 0.8tCO2/ MWh Grid Emissions Factor – what is the marginal supply source assumed? In the calculations it looks like a Grid Emission Factor of 0.75 was actually used instead of 0.8: (432306 tCO2) / (576408 MWh/year) = 0.75

We also have a number of additional questions which we'd also like to see a response to before approval:

- Paragraph 2.4 mentions factors that would need to be improved for projects to reach financial close. It mentions "insufficient cash-flows to ensure an appropriate risk-return profile to investors". Does the AfDB have any guidelines as to what it regards as an acceptable risk-return profile or is this determined solely through the competitive process?
- What are the reasons for the Government of Kenya not providing a Sovereign Guarantee? Short of a Sovereign Guarantee, what comfort can the GoK provide to investors?
- Regarding the apportionment of risk and the difference in what is expected from the CTF funds vs. the AfDB funds, it would be useful to have an idea of the expected pricing gap between the CTF funding and the AfDB funding, and more generally some further details on the additionality of the CTF investment (e.g. how was minimum concessionality determined in practice? Who will make the final decision on pricing? How has the appropriate level of CTF funding (USD 15 million) been determined? If this is too high it will crowd out private investment.)
- Separately from the interest rate differential it seems as though other concessions will be required from the CTF funding, namely a grace period and potential interest capitalization during the grace period.
    - I wasn't clear whether the grace period would be for interest payments, principal repayments or both?
    - Is the AfDB prepared to also offer a grace period and consider a capitalization of their interest during the grace period?
- Regarding the credit worthiness of GDC and KPLC, it would be useful to have more information on the financial profile of these companies, including their ownership structure (who are the shareholders, are they publically or privately owned) the size of their balance sheet and their degree of leverage (i.e. how much corporate debt they already have).
- Regarding GHG emissions savings, how are these calculated? What is the counterfactual – is it based on the existing mix of technologies in the Kenyan power market?

- Can useful lessons be learned from existing projects? Paragraph 1.7 mentions that “the Olkaria field is already under operations”. How was this project funded? Who supplies the steam to this project and how is the production of electricity remunerated? Is the project proving viable financially at that level of remuneration?

Thanks,

Lawrence