Comments on EBRD's Responses : CTF Private Sector Proposal "Ukraine Renewable Energy Direct Lending Facility"

Financial Volume: up to 27 Mio. USD CTF Loan,
+ 352,800 USD Grant for administrative cost
+ 250,000 USD Grant for knowledge management
+ 8.45 Mio. USD for advisory services component (GEF grant)

Purpose of the program:
The Ukraine Renewable Energy Direct Lending Facility aims at supporting and financing of renewable energy projects in Ukraine.

July 2010

Sectoral Issues of the Project Proposal

1. In their response to a question from Spain EBRD staff clarified satisfactorily that the CTF will seek to bring in commercial banks, other IFIs and investors to co-finance in individual projects. This answers affirmatively the question which we raised whether other could in general be welcome in this project.

2. An error was acknowledged in estimating the Administrative Budget. A further mistake was found in estimating the cost-effectiveness rate. Both are corrected.

3. There was doubt whether the low implementation potential on the Ukrainian side, especially the slow pace of legislative and regulatory framework, could easily be overcome. (One of our concerns, too.) EBRD staff responded that heavy consulting services were to be employed to speed up the processes. This is a case of good hope.

The remaining questions focus on project details which, in our view, are non-controversial. We consider the responses concerning the content of the project satisfactory.

Financing Terms of the Project Proposal

Some concerns remain regarding the financing terms.

1. We would very much welcome further clarification and justification for the financial terms for this private sector program. A range should be sufficient in this case, but we would appreciate it a bit more detailed, since maturity, grace period, rank and interest should form an appropriate package. The financial terms currently considered correspond to the terms for public sector projects (harder concessional terms: 20y term, 10y grace period, 75bps). Private sector financial terms would either have much shorter maturity, shorter grace periods and/or higher interest rate to balance the higher risk and avoid market distortion. Thus, public sector terms do not seem appropriate as bottom line for private sector projects. We would like to ask for a new proposal on the applicable range of terms for these projects.

EBRD Response (Oct 2010): *These terms outlined within the proposal are not intended to be based on public sector terms. Instead they are based on maximum limits of principal financing terms which may be provided by private finance through a project finance structure. The nature of project financing is such that longer maturity loans with longer grace periods are commercially viable as risk within the project is managed through long term contracting. Loans with tenors up to 20 years and extended grace periods are not uncommon in more advanced markets. If the financial terms were to be restricted to mirror the terms available from private banks in the Ukraine, the transformational benefit of the facility would be lost. The purpose of this facility is to provide bankable renewable projects with the required long term project finance which they are unable to access within the highly constrained debt markets in Ukraine.*

Having said this, the terms outlined within the proposal are very much viewed as the outer limits. The Bank works on the basis of sound banking principles and our mandate requires us to price accordingly. However, every project is different and the terms of debt provision within project finance are highly project specific. The terms outlined in the proposal allow the bank flexibility to support well structured bankable projects on the basis of sound banking principles.

2. We are still sharing the concerns of, e.g., DFID and the UK Treasury that here the Trust Fund Committee is asked to approve a general exception to the rule that MDBs rank pari-passu with the CTF Funds which contradicts the principle in Sect. 27 of the CTF private sector terms. We are hesitant to agree to such a general exception – very likely forming a precedent for coming project proposals. We would like to propose to explicitly introduce to the project proposal document the intention to restrict subordinating CTF funds relative to MDB/EBRD loans to very qualified and exceptional cases. EBRD has already done so in its answers to the comments from Japan (p. 3, (2a), second bullet point), DFID (p. 3, similar wording), or Spain (p. 2). Again, we would appreciate this to be reflected in an updated proposal that confirms the general rule. We would also ask for confirmation that any exceptions to this rule will be verifiably justified at least internally with EBRD.

EBRD Response (Oct 2010): *Our understanding is that subordination is permitted within the CTF private sector terms and that we are not requesting a general exception to the rules. We refer you to Section 16 titled CTF subordination to MDB investments and Section 28 which details requirements if CTF funds are to be made available for subordinated debt instruments. Section 27 details requirements if and when CTF funds rank pari-passu with MTBs.*

For further discussion on the role of CTF subordination within the facility we refer you to the detail response provided to the UK Treasury including a risk analysis. We also agree to limit the proportion of CTF funding provided on subordinate basis to not more than 30% of total CTF funding.

3. We would appreciate some explanation of the 250,000 US$ for “knowledge management related to the CIFs”. Will this be used for purposes not covered by “administrative costs” or EBRD’s fees for on-lending?

EBRD Response (Oct 2010): *It is our understanding that CTF donors agreed that each project and programme should have a knowledge management component attached to it and agreed that the maximum cap would be $250K. The EBRD intends to utilise these resources as and when appropriate to develop specific terms of reference and to recruit a consultant to undertake the knowledge management assignments. The knowledge management budget is extra to the administrative budget (as decided by the admin unit / donors) and does not represent a fee for EBRD on-lending.*