Blended Finance to Mobilise Private Capital for Clean Energy

Summary from side event at UN HLD Thematic Session on Finance and Investment

25 June 2021

Background

The theme report on Finance and Investment prepared for the UN High Level Dialogue on Energy identified as one of its recommendations the need to "Make better use of blended finance schemes to mobilise and maximize private capital for clean energy investments and innovative energy technologies." The report highlighted the potential to attract trillions in clean energy investments by "scaling the use of blended finance mechanisms and de-risking instruments coupled with commercial financing, multilateral portfolio guarantees and result-based financing."

The OECD's work on blended finance, including its 2020 Blended Finance Guidance[1], provides a solid foundation for pursuing further work on mobilisation of private finance for clean energy investments. An Energy Compact on Blended Finance provides an opportunity to promote action and commitments on mobilising private finance, linking the UN HLD on Energy process with the OECD's Development Assistance Committee's (DAC) work to highlight emerging good practice approaches and address barriers to local financial market development, deepening and greening.

Summary of discussion

The theme report on Finance and Investment highlighted nine key recommendations to support the mobilisation of finance and investment for clean energy including one on the use of blended finance to help de-risk clean energy projects to maximise the mobilisation of private capital. Other priority actions included the need to align financing with the Paris Agreement and foster the development of a pipeline of bankable projects. Developing such a pipeline would require support across various areas including sovereign support, policy and regulatory support, creating the right partnerships and blending public and private finance. Actions at the local level working are equally needed to develop solutions that take into consideration the unique situation of each country and build local capacity with the right partners. Countries have also highlighted the need for greater technical assistance to help fill knowledge and skills gaps to enable the creation of project pipelines.

From the perspective of institutional investors, blended finance mechanisms are an effective solution to attract investments in clean energy in emerging economies, as they can help to manage risks that international investors are less equipped to support. The use of public funding to provide a first loss guarantee has been an effective way to bring in private capital from pension funds for investments in clean energy to limit downside risk. For example, PensionDanemark's investment in a wind power project in Kenya that replaced a coal-fired power plant was made possible by a blended finance mechanism that provided a first loss guarantee. This project had wider societal benefits by facilitating energy access that helped to improve gender quality, as women and girls no longer needed to spend time collecting traditional biomass.

The growing interest among institutional investors to align portfolios with the Paris Agreement has increased demand for investments in bankable clean energy projects. The use of blended finance

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[1] https://www.oecd.org/dac/financing-sustainable-development/blended-finance-principles/

mechanisms is seen as an effective option to improve project bankability. Experience with designing and implementing blended finance schemes to facilitate investments in sustainable infrastructure, and in particular clean energy, is growing in a number of emerging and developing economies. For instance, Indonesia and South Africa are two countries where established government-owned financial institutions with development mandates have been actively supporting clean energy project development. In Indonesia, the SDG Indonesia One platform is a blended finance fund managed by PT SMI that allows private partners to access a variety of public support schemes (e.g. grants, concessional finance and access to equity) that can be used to de-risk projects, making them more attractive and suitable for commercial finance. In the clean energy sector, PT SMI has been active in supporting geothermal development with funding to support the highly risky exploration phase of project development. PT SMI is also considering support for the development of small hydro projects.

In South Africa, the Development Bank of South Africa (DBSA) with capital and technical support from the Green Climate Fund (GCF) have set up the Climate Finance Facility, which blends GCF funds to facilitate commercial finance among local banks. This facility uses a green bank model to provide tenor extensions that increases the availability of long-term finance for renewable energy projects. DBSA's embedded generation investment programme supported by the GCF is another example of a blended finance mechanism that helps de-risk projects that do not have a sovereign guarantee backing their power purchase agreement. It uses credit enhancement to support power projects up to 75 megawatts and is designed to create a market for embedded generation. This scheme aims to demonstrate the viability of renewable projects structured outside government-back programmes. Both initiatives also have a focus on gender mainstreaming.

It is essential that programmes supporting sustainable development and clean energy investments consider the inclusion of women. Blended finance incentives can enhance resource mobilisation for clean energy and improve gender equality. Programmes can be designed to provide work experience and opportunities for women in the clean energy sector and can also help to understand better if policies or regulations may prohibit or limit women's participation in the sector. For example, a Canadian funded wind project in Argentina integrated gender inclusion aspects into the programme and identified a law that barred women from participation in the construction of non-traditional sectors such as renewable energy. Canada's gender inclusive blended finance programmes demonstrate that it is possible to combine public and private capital for greater impact, not only with respect to low-carbon and climate-resilient economies, but for gender equality and inclusion.

Blended finance can be an effective means to de-risk projects and mobilise private capital for less mature markets. It can also support technology deployment in emerging and developing economies. Focus is most effective in supporting commercial or near commercial projects, as blended finance cannot address issues where there is a lack of a suitable enabling environment for clean energy development. Development assistance should therefore continue to support countries in strengthening the regulatory environment for the clean energy sector as well as the wider adoption of sustainable finance policies and green finance instruments.

Next steps

OECD will work with partners such as the EIB to further the work on the Blended Finance Principles and Guidelines, including taking forward the development of an Energy Compact on Blended Finance.