



The World Bank Carbon Funds: Buyers Perspective

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www.CarbonFinance.org



What buyers want...

- Purchase CERs preferably valid under EU ETS
 - ⇒ no sinks, limitation on hydro
- No post 2012 vintage of CERs
- Typically fixed price contracts
- Payment on delivery of CERs
 - Limited upfront payments usually on a case-by-case basis for most public sector/ multilateral funds
- Currency: mostly in \$ till now, shifting to €
- Low counterparty (seller) risk
 - Sound equity investors in the project
 - Lending by reputable commercial banks
 - Solid off-take agreements for the underlying product, e.g. power purchase agreement
- Preference for projects close to financial closure



What buyers want (2)...

- Penalty for under-delivery
 - Most carbon funds (all World Bank funds, KfW fund, Japan Carbon Fund) have no penalty
 - Private sector buyers and brokers pay premium for delivery guarantee
- Over-collateralization to manage under-delivery risk
 - World Bank carbon funds < 80% of the expected ERs; KfW fund < 50%, etc.
 - Over-collateralization and Unilateral CDM
 - The ability of host country entities to hold CERs in the CDM Registry account of the host country and sell subsequent to initial issuance
 - Inability to do this prohibits
 - Project sponsors from profiting from price increase in the future
 - Private sector in the host country to enter in to brokering
 - Private sector in host country from intermediating and speculating



What buyers want (3)...

- Most carbon funds look for country and technology diversification for risk management
 - Most buyers have regional preferences
- Size of transactions
 - Minimum
 - in CDCF about 30,000 TCO₂e/year
 - Other funds not less than \$3 million of ER purchase
 - Over 100,000 TCO₂e/year desirable
 - Maximum of about \$20 million
- Low country risk
 - KP ratification status, DNA, CDM approval process
 - Host country approval of a project



Key Lessons ...

- Enabling policy environment helps
 - CDM strategy development is only a first step.
Learning by doing (i.e. projects) is the way forward.
 - Successful CDM projects require a minimum **national framework** (legal & institutional).
- Key prerequisites for successful projects:
 - Project makes basic business sense
 - Project sponsor / owner commitment
 - Project reasonably well prepared (feasibility study, underlying finance)
 - Host country commitment



Local Regulatory and Business Environment...

- ✓ CDM/ JI is a competitive market
- ✓ To attract investments in CDM /JI countries, private sector more likely to invest if host country has:
 - Clear and consistent approach to sustainable development
 - Clear procedures for project approval (or refusal!) with specific timelines
 - Single window approach: DNA to assist project proponents in complying with all applicable laws, including those regarding environmental impact assessment
- ✓ Above all, approving a project under the CDM/JI should be transparent and predictable and within clearly stipulated time-frame



What works and what doesn't...

Local (Financial) Intermediaries help to

- Identify project opportunities at lower cost
- Get equity and debt financing
- More effectively design and/or evaluate projects
- Reduce transaction costs

Insufficient project preparation doesn't help...

- Underlying projects must be well prepared (feasibility study, risk assessment, financing).
- Committed project equity partners
- The project must be viable business proposition.
- The sector must be competitive if a project is to be viable.



In conclusion...

- Things that help:
 - Enabling policy and environment (including a effective DNA and simple approval procedures)
 - Experienced and committed project sponsors
 - Mature project idea prepared competently
 - Domestic credit market liquidity and ability to take informed risks
 - Local financial institution as intermediaries
- Things that **don't** help
 - Projects at very early stage of development
 - Projects that don't make business sense
 - Projects that are inconsistent with
 - Sector development goals
 - Environmental, social and other policies