Renewable Energy Finance Facility (KAZREFF)

Country / Region: **Kazakhstan** | Project Id: **PCTFKZ021A** | Fund Name: **CTF** |

MDB : **European Bank for Reconstruction and Development**

Comment Type	Commenter Name	Commenter Profile	Comment	Date
Comment 1	Ina von Frantzius	Germany	thank you very much for submitting the CTF project proposal for Kazakhstan on the renewable energy finance facility. This is a very ambitious and promising program with a lot of potential. We welcome this proposal and have no objections. We do have some suggestions and observations that might be helfpul to be taken into consideration for the further project development in order to fully develop the potential of the program. Please find our comments enclosed. Overall the Framework Program is in line with most of the CTF objectives and can also meet the purposes of the CTF Investment Plan. The program will deliver substantial CO2 emission reductions at a comparatively low investment cost with co-benefits, and start the market transformation of power generation in Kazakhstan towards a lowcarbon power supply structure. However, we have some suggestions to taken into consideration for the further project development and some questions and we would be grateful for more information or clarification regarding the following issues: General Comment on the Financing Terms - The low interest rates of the on-lent loans, blended with EBRD conditions, will certainly be attractive to the private sector which has to overcome big administrative and institutional hurdles. However, given the very small size of investments and the resulting large expected share of transaction cost, it remains to be seen whether the concessionality of the loans will suffice to overcome the reluctance of local investors and FIs in this sector. This should be monitored closely to allow for timely reaction if required. - The project proposal mentions the possible use of CTF-funded local currency loans. While local currency loans might indeed be very useful to local entrepreneurs and project developers, the implications in terms of additional risk and foreign currency exposure when offering local currency loans with CTF funds have not yet been analyzed. Therefore we would urge the EBRD take into account the upcoming work on a risk monitoring and management framework and the analysis of feasibility of using local currency loans. - Project financials are provided inconsistently in both EUR and USD while exchange rates used are varying quite a bit. To avoid confusion, we would appreciate if all numbers would be provided either in EUR or USD. General Comments on the project proposal - Format and substance: we would very much welcome if structure and substance of MDB CTF project proposals would strive to respect a minimum standard and criteria of CTF proposals. Otherwise a meaningful assessment of project proposals is difficult for a lack of comparability and required information. According to the Kazakhstan Country Investment Program of November 2010, renewable energy production is one of the 3 strategic priorities to apply CTF resources. One might add, it will be the most tedious one in terms of GHG mitigation efforts given that the focus is on small scale hydro and wind projects, compared to large scale district heating modernization and DSM, both of which are somehow more likely to produce larger GHG benefits in a shorter time frame and at a lower cost. The project's principal justification is that the CTF scheme will have a significant demonstration effect as it will be the first major effort to tap Kazakhstan's significant renewable energy resources. By demonstrating the bankability of RE projects and assisting the development of a legal/regulatory framework, the project intends to achieve major replication effects and ultimately trigger the local production of RE technology. While the above intended ambitious outcome is in line with Kazakhstan's investment plan and CTF objectives, it hinges on 2 critical factors: (i) The swift and radical transformation of a still rather un-conducive national regulatory and institutional framework for RE (persistence of fossil fuel subsidies, cheap coal, lack of fiscal frameworks/feed in tariffs, lacking capacity of govmt. institutions, legal uncertainty etc.); (ii) a profound market transformation through significantly improved capacity of critical (non-government) sector stakeholders, in particular project developers, local FIs and local industry.	Sep 28, 2012

While the former has been prominently addressed throughout the proposal, there is hardly any evidence for planned capacity building activities catering the needs of the latter. (TA is almost exclusively focusing on govmt. institutions &legislative /regulatory framework, with little attention paid to building project developers' capacity to develop bankable projects. Similarly, TA for- and cooperation with local financial institutions seems equally underrepresented in the proposal (despite their important role in the investment plan). - Next to the capacity building program for energy regulatory issues, it might be advisable to create a capacity building program on financing renewable energies for project developers, local FIs, local industry and local financial institutions. - Given Kazakhstan's starting point with regard to the needed change of institutional and regulatory frameworks, the required radical transformation is likely to take many years. Meanwhile, local financial institutions and private sector are still dealing with the impacts of the financial crisis and are less and less willing to enter into a new, subsidized sector. Consequently, major awareness raising and capacity building efforts will be necessary to work against this development. - The proposal refers to the lessons learnt from the Direct Lending Facilities the ERBD developed in the Ukraine and the West Balkans, but does not further elaborate these. We would be interested in the principle lessons and how these will be integrated into the project design. - Another concern we have relates to the question how the current level of end-user tariffs (according to the IP still largely below long-term cost coverage) will allow to fund the planned feed-in tariffs for renewable energies in the medium to long-term. As long as the share of RE will remain negligible, the feed-in tariff could potentially be sustained. However, if the project develops as planned, and consumer tariffs will continue to rise only very moderately, then the funding gap arising from the adoption of feed-in tariffs is likely to swiftly grow beyond the narrow limits and reforms will rapidly become unsustainable. Given that the increase of tariffs to cost recovery levels, despite significant efforts and support by donors, including EBRDs Sustainable Energy Action Plan (SEAP), has only been progressing very slowly so far, we are not sure how the proposed project will ensure the needed dramatic acceleration. Consequently, we would appreciate if EBRD could elaborate on the envisaged approaches or roadmap for sector reforms that will reduce the likelihood the above outlined outcome. - Implementation of feed-in-tariff (FiT) Scheme. Given the above mentioned circumstances, we are also wondering whether nation-wide feed-in tariffs would be the most effective solution for Kazakhstan, or if other models and strategies (e.g. investment/production tax credits, loan guarantees, interest rate and/or capital subsidies, system benefit charges, net metering, portfolio standards, etc.) should (at least temporarily) be followed until end-user tariffs are more in line with actual production costs, so that sector reforms will be more sustainable and will represent less of a burden to end-users and/or the national budget. It is questionable whether a FiT is advisable in a country that has had so far none experience with fluctuating renewable energy and plans to only gradually increase the installation of renewable energies. In this context it should be evaluated whether alternative policy frameworks, such as a competitive auction scheme has been considered, which could be implemented as a first step to evaluate how much the market is willing to pay for certain technologies. This could than later be complemented by the introduction of a feed-in-tariff. We are therefore a bit concerned that feed-in tariffs have already been identified as the best solution, without evidence of any in-depth analysis that would typically be needed to reach a conclusion of comparable importance and long-term budgetary implications. It is not clear from the proposal, whether the recommendation to implement a feed-in-tariff is aligned with KAZ energy policy. Here further information is needed. In addition, the time frame for the implementation plan seems to be very ambitious (market transformation indicators: "feed-in tariff methodologies and procedures approved and effective by 2012")- While the proposal mentions KAZ high hydro (21 TWh) and wind power (18 TWh) potential, besides the 1 TWh target by 2014, the proposal does not give any information about KAZ long-term renewable energy strategy/targets. - Furthermore, we are not sure about the proposed order of reforms, e.g. how will the proposed small scale RE projects be able to compete with cheap Kazakh coal given the absence of CO2 emissions legislation (according to the CTF Investment Plan, legislation on GHG emissions trading is still in the early proposal stages). - We are not sure what is meant with the proposed "cost settlement center" mentioned in the context of feed-in tariffs and best practices and would appreciate further elaboration on this component. - According to the proposal, the project also intends to consider financing the manufacturing of RE technologies. Given the overall level of ambition and short timeframe of the project, we are not sure whether this exceeds the realistic expectations of what this project will be able to achieve, and whether a more narrow focus would be recommendable. - The RE project pipeline identified so far (Annex D) appears very small and consists exclusively of investments below 25

			MW. Within this context, we would appreciate further elaboration with regard to your strategy for the rapid identification and development of the much larger pipeline needed for the swift and ambitious scale-up of RE generation capacity laid out in the proposal. - While the CTF Investment Plan mentions the "Kazakhstan Sustainable Energy Financing Facility (KAZSEFF)" as a potential source of support and financing for small scale RE projects. Given KAZSEFFs prominence in the investment plan, we are wondering why it is not mentioned in the proposal. On investment criteria„Potential for GHG Emissions Savings". Technology Development / Abatement Potential: The technologies involved can be considered commercially, yet the potential is to be demonstrated in Kazakhstan. According to UNDP and others, the abatement potential through RE schemes (mostly wind and small hydro) in Kazakhstan is likely to be very significant. Nonetheless, the potential is not well documented and detailed resource assessments have just been initiated. "Demonstration potential at scale" Emission Reduction by Replicating the programme approach: The report states that Kazakhstan has a large untapped reserve of renewable energy, the development of which, however, is held back by various barriers and impediments (regulatory, financing). Expectations are high but it is doubtful whether they are also realistic. in concrete figures: 4 Mio tons of CO2 are given, based on the "market potential for renewable energy". Nobody knows how much of it will be realized. Appraisal of chart on expected emission reduction: Not covered. „Development Impact" Impacts on energy intensity of the gross national product: Not specified; But the economic development benefits of the proposed Program could potentially be significant, such as: i. Improved availability of electric power, ii. Improved security supply iii. Increasing private sector involvement by the demonstration of private sector operations in RE production, iv. Reduced local pollution due to the displacement of coal or other polluting fuels for local energy needs, v. Transfer of skills: The facility is expected to build and transfer expertise related to renewable energy and energy efficiency project development to Kazakh companies. vi. Legislative reforms and capacity building: Creating a proper framework for the development of RE projects in Kazakhstan will help the country in building the necessary institutional capacity for implementation both at the project level and within the enabling institutions such as the regulator and grid operator. However, it has to be stated, that these potentially positive economic development effects can only be realized on a long-term basis and only if the regulatory framework will trigger substantial RE-investments. MDG-Relevance: There is no reference made on the MDGs. „ Implementation Potential and Project risks" Institutional Framework: Weak regulatory and institutional frameworks are considered as chief obstacles to be overcome by Technical Assistance. Due to this finding it is nevertheless surprising, that only EUR 2 Mio of the EUR 6 Mio is secured for TA. Who will bridge the important gap for TA? The challenging elements for the successful implementation of the Framework Program will be to coordinate the financial instruments of KazREFF with national programs, which also target the support of start-up businesses in new and sustainable technology areas, and to ensure that the foreseen, regulatory advisory services result in a longterm power take-off guarantee. Both should be examined and monitored as the Program proceeds. Furthermore the planned concessional conditions of the financial instruments bear the risk of the distortion of the RE market (crowding out), thereby delaying the transition to commercial viability and the competitiveness of the RE sponsoring companies. However, since the RE-business is in its infancy, these interventions are justified and necessary until a self-sustaining industry has developed in Kazakhstan. As the planned facility will also help Kazakhstan in creating a reliable regulatory framework and introducing market mechanisms to incentivize new RE-investments it is expected that these interventions will ultimately create a self sustaining industry and enhance the know-how and experience of local financial institutions in financing RE-investments. Consistency with activities of other bilateral & multilateral donors The project document does not elaborate on cooperation with bilateral partners. The investment components of the presented CTF programme are being coordinated with EBRD activities and the European investment programme.	
Comment 2	Eddie Tsibulevskiy	United States	verall, the proposed program is consistent with the CTF investment criteria and meets the objectives of the CTF Investment Plan. The program will deliver substantial CO2 emission reductions at a comparatively low investment cost, leading to significant market transformation of power generation in Kazakhstan. While we approve this program, we have a few comments and clarification questions on the following: Use of Local Currency in CTF-funded Projects In principle, when appropriate, we are supportive of the use of local currency for the CTF portion of projects. However, we would like to better understand how the risk for the use of	Oct 02, 2012

local currency will be hedged and who will bear the cost of such hedge. Demonstration Potential at Scale: While the program proposal states that Kazakhstan has a large untapped reserve of potential renewable energy, it is unclear to what extent these resources can be realistically developed. Additional information on the realistic scale of development of these resources would be helpful.