Private Sector Capital for Energy Transition

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Introduction

- According to Eskom, the existing generation fleet is expected to ramp down from c.50GW to c.15GW by 2050.
- Based on current projections, by 2030 new renewable energy capacity of c.50 – 60GW will need to be added even if there is no incremental demand from economic growth.
- This quantum is said to double to c.120GW of renewable energy capacity if a 5% increase in economic growth is assumed.
- Eskom further estimates that R1.2trillion of infrastructure investment will be required by 2030. The Blended Climate Taskforce also estimates that USD250bn will be required by South Arica over the next 3 decades to transform its energy system, and of this amount, two thirds will be required from the Private sector.

Capacity required to mitigate the energy crisis		Estimated cost
Generation capacity	• Firm capacity – 6GW • Variable capacity – 50-60GW • Storage capacity – 10GW	c.R990bn

Transmission capacity	• Expansion and strengthening of transmission network
	  • c.8,000km new line
	  • c. 101 substations
		c.R130bn

Distribution capacity	• Strengthening of the distribution network for embedded generation c.7,500km of new line	c.R56bn

Source: Eskom CEO report

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- There is a long history of private sector investment into infrastructure projects in SA. To date the private sector has invested c.R95bn into Public Private Partnerships and there is significant appetite for these types of assets.
- Looking at the power sector specifically, over the last decade, the government-led projects have attracted c.400bn of investment and support (debt and equity):

Programme	MWs	Investment (R'm)	Number of projects	Employment (job hours)
REIPPP R6 (currently at RFP stage)	5,200	100,000	50	27,000
REIPPP R5 (currently at preferred bidder stage)	2,600	50,000	25	13,902
RMIPPP (currently at preferred bidder stage)	2,000	40,200	11	22,346
REIPPP R1 – 4 (closed and constructed)	6,323	209,600	92	63,292
Total	**16,123**	**399,800**	**178**	**126,540**

- What made the REIPPP programme successful:
  - Process certainty and planning
  - Reverse auction procurement – which has resulted in declining tariffs that are very competitive by a global standard
  - Successive bidding windows – once a year between 2011 and 2015
- Since the lifting the threshold over which a generation license would be required, the private sector has seen tremendous activity in the private power space with mandates over c.R163bn currently awarded or in the process of being awarded in the corporate space led by the energy intensive users. These numbers represent 1 year of activity in private power market.

Source: IPP office

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- The debt component of the investment into the projects above was largely supported by the SA banks with a few of the usual asset managers supporting. The amendments to Regulation 28 of the Pension Funds Act is very positive and should result in more institutions playing in the sector.
- The banks have communicated that they still have strong appetite for power assets. The experience of the market is that there is a shortage of bankable well-structured projects and not necessarily a shortage of capital.
- Using the renewable energy focused Special Purpose Acquisition Companies (SPACs) that were listed in the JSE and didn't perform as well as expected as an example of what is required to encourage large scale appetite from the financial institutions:
  - The pipeline of renewable energy projects was not clear enough (e.g., REIPPP R5 which was bid last year, was the first bidding round since R4.5 in 2015 which was never awarded). There is therefore a need of a clear pipeline that the private sector can plan and invest against. This also relates to the investment that is required for local content requirements.
  - The net asset value (NAV) of the SPACs were declining due to not adding new assets quickly enough and the institutional market wants an investment that is "evergreen" or has an increasing NAV.
  - The SPACs themselves were not large enough to attract appetite of the new institutional players into the market. This resulted in the SPACs trading at deep discounts to NAV and not attracting the private sector investment that they need to grow
- Given the fiscal constraints that SA faces, it is important to structure programmes such that the need for government financial support is minimized. All the government led programmes to date have had government guarantees. In the private power space, for example, we are seeing limited guarantees being offered (3 - 5 years) which are much less comprehensive than what has been provided in the REIPPP programme for example. With the removal/ amendment of certain clauses in the PPAs it is possible to structure PPAs that are less dependent on the state.
- Ways to minimise the impact of infrastructure projects on the fiscus should be explored, these include:
  - Limiting the National Treasury underpin to certain termination scenarios within projects/programmes
  - An analysis of the way the contingent liability relating to infrastructure projects is recognised by auditors and ratings agencies
  - Introducing alternative guarantee mechanism e.g Put Call Option Agreement (PCOA)
  - Using blended financing

Source: IPP office

Conclusion

- South Africa's economy requires a robust and sustainable growth plan that creates jobs and increases household income
- The proposals and recommendations made in this presentation require increased partnership and collaboration between government and the private sector.
- History has proven that where private investment has been used correctly, South Africa has managed to deliver key infrastructure projects that have improved the livelihoods of South Africans