

**PROJECT NAME:** Honduras Renewable Energy Finance Facility (H-REFF)

**PROJECT NUMBER:** HO-M1048

**PROJECT TEAM:** Zachary Levey (MIF/ABG) and Paola Pedroza (MIF/ATF), co-team leaders; Susana Garcia-Robles (MIF/ATF), Ignacio Fernandez (MIF/ABG), Filippo Berardi (MIF/ABG), Carlos Jacome (ENE/CHO), Fausto Castillo (MIF/CHO), Claudio Alatorre (INE/CCS), Emiliano Detta (INE/CCS), Michael Hoffman (MIF/ABG), Ruben Doboin (MIF/DEU), Georg Neumann (MIF/KSC), Alex Honjiyo (MIF/ABG), Laura Tora (MIF/KSC), Patrick Doyle (SCF), and Ignacio Barragan (LEG/NSG).

## I. PROJECT SUMMARY

Growing the installed capacity of renewable energy is a priority for the Honduran government. Despite an attractive set of policy incentives to spur private initiative in the energy sector, a critical mass of renewable energy SMEs do not have access adequate and appropriate financing within the local financial markets. Many of these local entrepreneurs lack the capacities and sector experience to present bankable proposals to financial institutions, thereby resulting in a major bottleneck of opportunity for green jobs and low carbon growth in Honduras.

The proposed MIF investment will establish a private sector Renewable Energy Financing Facility for Honduras (H-REFF). The Facility is designed based on the results of an exhaustive study commissioned by the MIF and IFC under the Scaling Up Renewable Energy Program (SREP) on the key barriers facing private actors in the renewable energy sector in Honduras. The Facility will target up to US\$ 44 mm in capital commitments to provide financing for 10 to 20 renewable energy SMEs. The Facility will include reimbursable co-financing from the SREP that will be administered the MIF and will also include investment from other DFIs, such as IFC and Norfund. The Facility will employ primarily mezzanine finance to develop a portfolio of renewable energy companies that use technologies, such as small-scale hydro (<10 MW), biomass, biogas, and solar.

The MIF and other investors will select the management team through a competitive selection process. The selected management entity will be expected to establish a local office and a team in Honduras and will be subject to standard MIF due diligence and analysis. In addition, the Facility will include parallel technical assistance resources with SREP grant resources to support training of local renewable energy SMEs, development of community benefits-sharing activities and engagement strategies and activities for mitigating environmental impact.

The Scaling-Up Renewable Energy in Low Income Countries Program (SREP) seeks to create new economic opportunities and increase energy access through the production and use of renewable energy. SREP grants and concessional funds are administered by MDBs as co-financing and can be used for the following purposes: (i) provide concessional financing instruments in order to catalyze, leverage and maximize finance provided by MDBs, commercial financial institutions and other partners for investment in renewable energy; (ii) provide capacity building and technical assistance to projects, project developers, local financial institutions and communities.

## II. PROJECT CONTRIBUTION TO THE ACCESS FRAMEWORK

**Project Contribution to MIF's Mandate:** The project will contribute to achieving the MIF's mandate of advancing private sector development, with an emphasis on filling a critical financing gap for renewable energy SMEs that will create new jobs in rural areas and reduce the countries dependency on dirty and expensive fossil fuel imports.

**Project Alignment with MIF Agendas:** The project is aligned with the MIF's agenda for expanding access to basic services and clean energy as well to the "Start-Up and Early Stage Equity Funds for High Growth Firms" Agenda, and aims to address knowledge gaps of both agendas. The project is also consistent with the MIF's early-stage equity investment approach, which seeks to consolidate the VC segment and to support innovative and highly differentiated vehicles achieving developmental impact.

**Project Contribution to Agenda Results and Knowledge:** The project will be the first multi-investor investment facility to use resources from the SREP. It will provide important contributions to the MIF's basic services and energy agendas on climate finance and also the appropriate structures for investing in renewable energy. The main knowledge gap that project will contribute to is on understanding what are the most effective financing models are for renewable energy SMEs.

## III. INFORMATION

<b>COUNTRY:</b>	Honduras	<b>TECHNICAL COOPERATION:</b>	\$ 000	
		<b>INVESTMENT:</b>	US\$ 4,000,000	
		<b>LOAN:</b>	\$ 0	
		<b>TOTAL MIF FUNDING:</b>	US\$ 4,000,000	9 %
<b>LOCATION:</b>	Honduras	<b>COUNTERPART:</b>	US\$ 10,000,000	43%
		Norfund	US\$10,000,000	
		IFC		
<b>EXECUTING AGENCY:</b>	To be selected through a competitive process	<b>COFINANCING :</b>	US\$20,000,000	48 %
		SREP Investment (equity or debt)	US\$1,900,000	
		SREP Grant		
<b>ACCESS AREA:</b>	ABG and ATF	<b>TOTAL PROJECT:</b>	US\$45,900,000	100 %
<b>AGENDA:</b>	Access to Basic Services and Clean Energy	<b>NUMBER OF DIRECT BENEFICIARIES:</b>	<u>Firms</u> - 10 to 20 renewable energy SMEs <u>Environment</u> - 70 to 130 MW - 100 to 150 K tCO2-e reduced	

<b>COMPLEMENTARY BANK OPERATIONS (IF ANY):</b>	HO-T1184 : Institutional Strengthening for Energy Sector Stakeholders	<b>NUMBER OF INDIRECT BENEFICIARIES:</b>	3,000 temporary jobs and 375 permanent jobs created <sup>1</sup>
	HO-L1106 : Transmission Program for Renewable Energy in West and North Zones  SREP Honduran Self-Supply Renewable Energy Guarantee Program (SCF	<b>QED SCORE:</b>	

#### IV. PROBLEM DIAGNOSIS

Growing energy demand and concern over energy security are driving the need for greater private sector investment in renewable energy in Honduras. Honduras relies heavily on imported fossil fuels for power generation, which translates into major economic burdens and strains on local businesses and the Honduran economy. In 2013, Honduras spent 13.2% of GDP on fossil fuel imports, which accounted for 57% of energy generation. The average cost of thermal power in 2014 was US\$162/MWh, while the average cost of non-conventional renewable energy was US\$117/MWh. In addition to having an expensive generation mix, Honduras also suffers from high technical losses and very high commercial losses. The inefficiencies, fossil-fuels orientation, power subsidies, late payments and import-reliance of the power sector have accumulated a high level of debt for state-run utility (ENEE) and contributed substantially to the national deficit. The IDB energy division is currently supporting the government to carry out a process of structural reforms to tackle the most important problems of the power sector to facilitate the long-term financial sustainability through the technical cooperation HO-1178.<sup>2</sup>

As part of the effort to reduce the country's dependency of fossil fuel, the Honduran government aims to reverse the present fossil fuel and renewable energy ratio to achieve 65% renewables and 35% fossil fuels by 2017. However, despite the government's commitment to increasing the share of renewable energy in the country's energy mix, an array of challenges abound for local renewable energy entrepreneurs. A substantial pipeline for small-scale renewable energy remains untapped, which could be developed by local SMEs and create new opportunities for employment and investment in rural areas.

<sup>1</sup> NREL has a toolkit for estimating these numbers. The final job numbers will vary based on SME size and nature.

<sup>2</sup> The Energy Division of the Bank is already moving forward with a Technical Cooperation (HO-T1178) to make important advances in the to support a long-term energy policy to increase the share of RE in the energy mix, legislation and technical standards appropriate for each Renewable Energy Technology (RET), incentive models (including tariffs) for the effective development of each RET, which fully reflects their associated benefits, guidelines for obtaining construction, operation and supply permits for RE installations, and definition of intra and inter-agency responsibilities, while building capacity in order to improve the integration of RE in the energy sector

Renewable energy entrepreneurs encounter a litany of interrelated challenges in the nascent renewable energy market in Honduras. In 2013, the MIF and IFC commissioned an exhaustive assessment of the market barriers facing local private sector actors in Honduras, which identified several key challenges that could be addressed. First, local renewable energy SMEs need capital in flexible terms that is tailored to a renewable energy project's long-term and less volatile cash flows; however, many local entrepreneurs do not have access to access adequate and appropriate financing within the local financial markets. They are often confronted with a distinct mismatch between the needs of the projects and the conventional financial sector products, including such issues as loan terms and collateral requirements. Second, many renewable energy SMEs that were awarded power purchase agreements (PPAs) do not have the financial management capability or sufficient funds of their own to present bankable proposals to financial institutions. Third, many renewable energy SMEs do not know how to properly engage with communities and create benefits-sharing schemes, which creates significant risks of social opposition by local communities. Fourth, local financial institutions lack practical experience in and knowledge of the field of renewable energy and renewable energy finance.

**Classification of the problem:**

Market failure

☒

Skill deficit

☒

**Beneficiaries:** The primary beneficiaries of the project will include: (i) 10 to 20 small and medium-sized renewable energy enterprises in Honduras, with annual revenues of up to US\$5 million and less than 100 employees; (ii) local communities that will participate in benefits sharing schemes; and (iii) the environment through lower carbon emissions.

## V. PROJECT DESCRIPTION

The main objective of Honduran Renewable Energy Finance Facility (H-REFF) is to bridge a critical financing gap in the renewable energy sector in Honduras and to provide capital and know-how to bring projects to financial close. Although there is general consensus that there is sufficient availability of senior debt, early-stage financing and risk capital is very scarce or almost unavailable for renewable energy SMEs.

The MIF, Norfund and the IFC have expressed interest in capitalizing a renewable energy investment facility for Honduras and selecting a dedicated facility management team. The Facility will provide primarily mezzanine financing instruments, including convertible debt or other securities, preferred shares, golden shares, senior debt with revenue participation, subordinated debt with warrants and options, or other performance-based instruments. Some portion of capital commitments may be used as direct equity as long as the Facility maintains its nature as a primarily mezzanine finance facility. It is expected that the H-REFF will focus on renewable energy SMEs that use non-convention renewable energy technologies to deliver self-supply and grid-connected power generation, such as small hydro (less than 10 MW), biomass, biogas, and small-scale solar.

The Facility will have a target capitalization of up to US\$ 44 mm, although upon reaching up ~US\$30 mm in commitments the Facility could be launched. Honduras currently has US\$10mm of committed SREP financing for the Grid-Connected Renewable Energy Development Support (ADERC) program and an additional US\$15 mm from the SREP private sector side, amounting to a total of up to US\$25mm in capital commitments from SREP. Up to \$20 million of these funds will be administered by MIF as co-finance and up to US\$5 mm will be administered by the IFC.

As the Facility will primarily utilize debt and quasi-equity instruments, exits will be more straightforward, based on amortization payments with the possible upside structured as golden

shares or other performance-based instruments. The Facility may be structured as a closed or open ended Facility with a dedicated management entity. The specific structure and investment strategy are expected to be defined by the Facility management team once selected. The Facility will be established in a legal jurisdiction agreeable to the MIF and other investors.

An additional US\$1.9 mm in grant resources from SREP is available to create a technical assistance facility to support training and building capacity of local teams in fund management, training of local project developers in social and environmental management, feasibility studies, legal fees, and other expenses.

**Pipeline and Demand:** The MIF has compiled a catalogue of all renewable energy projects with a PPA and have ranked them based against 6 criteria: (i) Permits and contracts approved including environmental, power interconnection, operation, grid stability and others; (ii) land properly acquired or secured; (iii) level of previous experience of project developer and level of participation in the Honduras power sector of project owner; (iv) adequate socialization of the project with the community; (v) equity secured or identified; (vi) financial and technical considerations of the signed power purchase agreement (PPA) with the national power utility. In addition, the MIF hired a local consultant to conduct structured interviews with project developers and sector experts to validate and refine pipeline ranking and prioritization. The pipeline contains over 40 small-scale, grid-connect renewable energy projects with PPAs and permits obtained but that are lacking sufficient project owner equity and experience for them to be financed by local banks in the near-term. The full pipeline and its analysis is available on request in excel.

The MIF and IFC held multiple in-country workshops and consultations with local banks interesting in financing renewable energy, the government who is interested in have more renewable energy developed, project developers and owners that are looking for financing, and the renewable energy producers association (AHPPER). These consultations were carried with a corresponding review of existing financing mechanism currently offered and analysis of lessons learned and best practices. All these efforts suggested the need for risk capital facility that could take the form a mezzanine finance fund.

#### **Components:**

**Component I:** MIF Equity Investment of up to US\$ 4 mm to capitalize the Honduras Renewable Energy Financing Facility.

**Component II:** Investment of up to US\$ 20 mm of SREP resources as co-financing in the Honduras Renewable Energy Financing Facility in the form of an equity investment into the Facility or as highly concessional long-term debt to leverage the Facility, or both.

**Component III:** Up to US\$ 1.9 mm in technical assistance resources from the SREP to support the following: (i) training and capacity building of a local Facility's management team and set up of local office; (ii) feasibility studies needed for prospective projects; (iii) trainings of local project developer in financial and environmental management and community engagement; (iv) development of community-benefits sharing schemes for facility investments; (v) Environmental and Social Responsibility (ESR) training for the Facility's management team; (vi) up to three rounds of independent evaluations; (vii) legal costs associated with the investment; (viii) supervision activities of MIF and SREP resources; (ix) creation of case studies and dissemination of lessons; (x) mandatory contributions to the agenda and impact evaluation accounts of the MIF and (xi) rating of the Facility under the Global Impact Investment Rating System (GIIRS) for the first years.

The training and support on community engagement will include: (i) an assessment of capacity to manage social issues, (ii) Development of a Company-Community Project Engagement Plan (CCPEP); and (iii) Completion of Training activities and Capacity Building workshops. A more detailed draft terms of reference is available upon request.

**Knowledge Sharing, Communication Strategy:**

The main knowledge gap that project will contribute to is on understanding what are the most effective financing models are for renewable energy SMEs. The knowledge objective is to systematize, document, and disseminate the experiences and lessons generated within the Facility, in order to raise awareness about and encourage the replication of renewable energy investment in Honduras and the LAC region. The main audiences will be investors, MDBs, and SMEs interested in replicating this model. To this end, a Project Fact Sheet will be developed containing key results from the project as well as main lessons learned, a How-to-guide explaining the model of the training for developers, a Thematic study on a mezzanine finance facility for renewable SMEs in low income countries, an infographic and participation in events to share the model and lessons learned.

**MIF's experience and lessons learned:**

The MIF has an extensive track record in supporting innovative models for expanding access to cleaner and more efficient energy and with investing in Seed and VC funds in the region. In the past 18 years, the MIF has invested in more than 65 VC and Seed funds over the region. Specifically the MIF has approved investments in seven investment funds dedicated to clean energy and in four other funds with an environmental focus. Lessons from these experiences have been incorporated into the design of this project. These lessons stress: (i) the importance of industry expertise for fund managers, for instance, NGOs generally lack the skills necessary for effective fund management; (ii) minimum fund size: small funds under US\$ 20 mm do not usually generate the management fees needed to cover expenses and/or have adequate capital for follow-on investments; (iii) proper application of financial instruments: fund managers may need to blend equity with mezzanine instruments and debt when necessary; (iv) smaller funds are unable to exert influence over the firms in the fund portfolio, and (v) economics of small leveraged funds have been unsatisfactory.

**Collaboration with the IDB Group**

This project was developed in coordination with other members of the IDB Group, such as ENE, CCS, and SCF. The project will attempt to derive synergies from Bank initiatives, such as the Energy divisions support for the energy sector reforms and transmission, SCF green lines to local banks, as well as synergies with the SCF Honduran Self-Supply Renewable Energy Guarantee Program.

**VI. MIF ADDITIONALITY**

As one of the region's most recognized institutions with more than 16 years of experience in supporting renewable energy finance, the MIF will provide both financial and non-financial additionality to the project.

**MIF Non-Financial Additionality:** The MIF has been the leading force behind the creation of this Facility and as a strategic partner for the Honduran government in implementing the Scaling Up Renewable Energy Program (SREP). The MIF will ensure that the Management Company structures the Facility according to international best practices and terms and adheres to environmental and social best practices for renewable energy projects. Through its participation in the Facility's governance structure and relevant investment and advisory committees, the MIF will promote best practices in the Facility's corporate governance.

**MIF Financial Additionality:** The mobilization of SREP resources is contingent upon MIF financial participation in the Facility. Therefore, the MIF will provide an investment to an asset class that is of limited supply in the Honduran market. It will improve the credibility of the Facility by helping to bring other investors during its first and subsequent closings.

## VII. RESULTS INDICATORS

**Results Metrics:** The project's expects to achieve the following results:

- i) 10 to 20 renewable energy SMEs receive financing from the Facility (CRF 230400)
- ii) US \$44 million in financing to firms placed by the Facility (CRF 230700)
- iii) 40 renewable energy SMEs (firms) receiving training or otherwise strengthened to provide new goods or services. (CRF 130100)
- iv) US\$ 36 million of additional investments mobilized into the Facility (10:1 mobilization ratio).
- v) US\$ 150 million from local banks mobilized into renewable energy SMEs
- vi) Additional installed capacity of renewable energy (MW)
- vii) Additional renewable energy power generation (MWh/year)
- viii) 30 investors and MDBs access MIF knowledge products or knowledge transfer activities (CRF 150100)

## VIII. IMPACT INDICATORS

**Metrics:** The expected impact will be measured by:

- i) Number of net jobs created annually by firms. (CRF 330301)\*
- ii) Average number of net jobs created annually by firms (CRF 330300) \*
- iii) Tons of CO2 reduced (CRF 340100)
- iv) Number and percent of the Facility's portfolio companies exited successfully.

\* denotes sex disaggregation by individual or firm owner or leadership

## IX. SYSTEMIC IMPACT

The project's strategy to promote market transformation and systemic change is based on: (a) the demonstration effect it expects to provide by supporting the first Honduras-focused mezzanine finance facility that will advance a critical portfolio of RE technologies and projects. By sharing knowledge and helping to reduce initial project development barriers (high due diligence and legal costs), the project will catalyze project development and access to financing for these projects, establishing a track record of their technical and financial performance. Such demonstration is expected to reduce risk perception associated with these technologies and financing models, thus enhancing access to financing and further replication in the future. (b) The building capacities among the stakeholders in the renewable energy sector to identify, evaluate, develop and finance these projects as well as engage with local communities and implement environmental impact mitigation strategies. In addition, the project will seek to build the capacities of local management team, which will be Honduras' first management team focused on small-scale renewable energy development. To support the market transformation objective of the program, the IDB will profile the lessons learned through the projects supported by disseminating case studies, as part of the Knowledge Management component.

## X. BASELINE DATA, MONITORING MECHANISMS AND EVALUATIONS

**Baseline Data:** The Management Team will capture the necessary data to monitor and evaluate performance and development impact of the companies. This data will come primarily from the

companies' investment memorandums presented in the Investment Committees, and may be complemented by interviews and additional data requests when needed. Other relevant baseline data that cannot be provided through the aforementioned means could be obtained through the GIIRS rating process, which we encourage for all our invested Funds.

**Monitoring Mechanisms:** The Facility will be responsible for setting up a monitoring mechanism and report to the MIF through the Annual Fund Supervision Report (AFSR) platform. As is characteristic in investment funds, the H-REFF is expected to apply a data-driven and hands-on supervision model in each of the portfolio investments. As a result, the Facility will prepare investor reports on the state of the portfolio on a quarterly basis and provide audited financial statements on an annual basis. The MIF will conduct monitoring through participation in the different Facility's committees, supervision missions, and the preparation of AFSR. In addition, when appropriate, the MIF will leverage the local and sector expertise available through the IDB country office.

**Evaluations:** The project will be subject to up to three independent evaluations throughout the Facility's life. Key evaluation questions include: i) what is the appropriate financing instrument for renewable energy? ii) What is the impact and benefit of a facility with a longer lifespan in the renewable energy sector; iii) What is the impact of SREP resources on market transformation?

## XI. EXECUTING AGENCY

The Facility's management entity will be selected through a competitive selection process by MIF, Norfund and the IFC. There are certain minimum requirements with which the candidates who wish to participate in the selection process must fully comply. The Requirements include the following: (i) compliance with all relevant laws and regulations; (ii) qualified Management Team with track record in renewable energy finance preferably with experience in Honduras; (iv) proven expertise in eligible sector-related projects and/or companies; (v) proven active experience in the structuring and management of similar investment/lending vehicles; (vi) in case the candidates are managing other similar trust/funds in the capital raising phase, investment phase or divestment phase, explanation of how the candidate plans to manage the proposed H-REFF vis-à-vis other funds under management avoiding conflict of interests; (vi) creation of local capacity, including a strong preference for teams that incorporate diversity and local professionals (Hondurans) into the management team through a local office; (vii) demonstrated ability to cover the costs associated with the development and creation of H-REFF prior to the initial closing; (viii) and are nationals of a member country of the IDB Group. The *terms of reference* is currently being finalized pending final input from other investors.

The assessment criteria that will be applied for the selection of the management team will comprise of both qualitative and quantitative attributes that are considered key indications of the most suitable candidate to act as the Facility manager. The assessment criteria will consist of an evaluation of the requirements described above as well as other aspects including, without limitation, the candidate's institutional profile, the track record of the proposed investment committee and management team, the proposed financing structure, and experience in renewable energy finance. The attributes of the Facility management team will be looked at holistically and selected by a committee of professionals from IDB/MIF, IFC and Norfund. The selected management team will be required to develop a more detailed Facility concept and will be subject to standard MIF due



diligence and analysis. The selection of the facility management entity will not translate into any legal and financial obligation of the MIF or other parties.

**Other partners:** Norfund and IFC have expressed interest in providing co-investment into the Facility of up to US\$ 10 mm in the case of Norfund and up to US\$ 5 million in the case of IFC along with another US\$ 5 mm in concessional funds from the SREP that will be administered by the IFC.

## XII. PROJECT RISKS

**Management Risk:** Even though the Management Team has not been selected, this will be MIF's first Honduras focused renewable energy fund and it is possible that the management entity may be first time fund managers or will be working together for the first time. **Considerations:** The MIF will encourage the local fund management team to pair up with an experienced management company with international and local experience. In addition, the technical assistance facility will provide additional training and support for building the capacity of the local management team.

**Financial and Exit Risk.** The Facility may incur in losses and be unable to find suitable exit options to liquidate investments. **Considerations:** As the Facility will primarily utilize debt and quasi-equity instruments, exits will be straightforward, based on amortization payments with the possible upside structured as golden shares or other performance-based instruments.

**Access to Debt Finance:** The Facility will invest in renewable energy projects, which will need complementary debt financing to reach project completion. Therefore, there may be some risk associated with the cost and availability of debt for financing for energy projects. **Consideration:** Honduras has seen a growth in access to senior debt for renewable energy with Banco Atlántida, FICOHSA, BANPAIS, and LAFISE all with dedicate lines for renewable energy that they provide denominated in US Dollars and Lempiras for tenors as long as 15 years.

**Hydrology Risk:** Run-of-the-river hydro power relies on the natural flow of a waterway. If the water flow in a stream is reduced due to drought or other factors, so is the available power output of a hydro turbine placed in the stream. Therefore, it is possible that there could be a drought that could significantly reduce revenues of the project in a specific year of operation. **Consideration:** Determining average expected water flow for a hydroelectric run of the river power plant requires a highly specialized analysis. The Facility management team will be expected to perform downstream measurement of water flow during the due diligence process of the individual investments. Further, this risk is mitigated by the fact that, if it materializes, its effects will be limited to a determined year and geographic area so it may not necessarily affect all power plants, and will likely have minimal impact on the present value calculation of the power plant portfolio. Moreover, the H-REFF will seek to have some technology diversity in its portfolio to include biomass, small scale solar and wind.

**Curtailment Risk:** Taking into account the existing capacity and newly awarded PPAs, the expected installed capacity of renewable energy will be 350 MW of wind, 619 MW of solar, and 562 MW of hydro, 390 MW of biomass and 80 MW of geothermal, compared to Honduras' maximum capacity of about 1,336 MW. Therefore, oversupply and grid instability due to intermittency of the ramp up in renewable energy may cause curtailment of solar and wind production. **Consideration:** The Facility will focus on primarily non-intermittent power sources such as hydro, biomass and biogas. In

addition, wind and solar power have a strong complementarity in time of production. Furthermore, the Central American Electrical Interconnection System (SIEPAC) is expected to allow for evacuation of excess capacity up to a bandwidth of 300MW with a potential expansion up to 600 MW.

**Currency Risk:** Local currency fluctuations could have some impact on the Facility's returns to investors. The Facility will be capitalized and may make investments in Lempiras. As a result, returns to the MIF could be negatively affected by a depreciation of the local currency, as the MIF will receive its returns in US dollars. Considerations: This is a risk that cannot be fully mitigated, as there is no possibility to hedge currencies in an investment fund, given its high costs. **Consideration:** H-REFF's long-term investment horizon will help mitigate the currency risk. The strength of return drivers including multiple and earnings growth should also further help mitigate any adverse currency fluctuations over the life of the Facility.

**Untested regulatory environment:** This project will operate under the new PPA environment, which has just been introduced. In the case of outright termination of PPAs, the project would be forced to find alternative buyers, likely through sale to the spot market. **Consideration:** These risks will be critically evaluated by the Facility Management team when negotiating specific financing.

**Systemic risk:** Deterioration of the political, regulatory or financial environment may negatively affect operations, valuations and overall returns. **Considerations:** The Facility will have a long enough life-span to operate and could withstand moderate fluctuations in the operating environments.

### XIII. ENVIRONMENTAL AND SOCIAL ASPECTS

The Facility is not expected to produce negative social or environmental outcomes. H-REFF will manage the funds in accordance with the IDB/MIF's environmental and social guidelines for MIF Financial Intermediary Operations, and will participate in the MIF/IIC approved training course on environmental and social review for financial intermediaries. The project will also provide tailored training and capacity building for project developers to ensure they adhere to best practices for community engagement and implementation of environmental risk mitigation strategies.

Another important benefit of the program is the displacement of fossil-based generation, thus contributing to reducing fossil fuel imports and enhancing energy security and trade balances (particularly if replication of these types of investments achieves in the mid/long term a sizeable scale).

In terms of environmental benefits, the Program will support projects expected to reduce GHG emissions and depending on project type, may include benefits in terms of waste reduction (i.e. economic use of waste for energy production), in the cases of biomass and biogas projects. The non-reimbursable component of this project will include a number of evaluations that will ensure that the Facility Manager has a procedure in place to ensure review and management of potential risks and impacts, and that the all investments comply with national environmental and social legislation and with the IDB List of Excluded Activities.

**XIV. COUNTRY OFFICE COMMENTS**

Both Fausto Castillo, the local MIF specialist, and Carlos Jacome, the local energy specialist, have been involved in the design of this Project over the last three years. Their comments are incorporated into the project document.

Carlos Jacome (INE/ENE): Es un proyecto importante viendo el nivel de interés del sector privado y la importancia para el País que el Banco financiar el equity de los proyectos de ER que no han podido avanzar.

Fausto Castillo (MIF): Es un proyecto importante para el país. Mis comentarios ya se incorporaron en el documento.