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PERU

SOCIAL ENTREPRENEURSHIP PROGRAM

**PROPOSAL FOR FINANCING AND TECHNICAL COOPERATION FUNDING FOR
RENEWABLE ENERGY AND RURAL MICROENTERPRISE**

(SP/TC-99-03-01-0-PE)

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EXECUTIVE SUMMARY

Amount and source:	IDB:	US\$	EURO
	Financing:	300,000	298,800
	Technical-cooperation funding:	200,000	199,200
	Local counterpart:	<u>241,000</u>	<u>240,036</u>
	Total:	741,000	738,036

The resources will be drawn on the European Community Special Fund for Microenterprise. The funds will be committed and disbursed by the Bank in EUROS.

* Exchange rate: US\$1.00 = EURO 0.996

Financial terms and conditions:	Amortization period:	20 years
	Grace period:	5 years
	Disbursement period:	48 months
	Interest rate:	2% in local currency

The interest rate charged will include a maintenance of value component, to be based on the most recent six-month annualized Consumer Price Index (CPI), reported by the Central Bank or some other official source. The grace period will apply to payment of principal only, not to interest.

Objectives: General objective. The general objective of the program is to improve living conditions in remote rural communities in Jaén, San Ignacio, and Bagua, by establishing small sustainable companies that generate power from renewable energy sources and promoting new productive uses of energy.

Specific objectives. The specific objectives are (i) to improve the availability of electricity for remote rural communities by installing 17 micro hydroelectric power plants (MHP), (ii) to institute or reinforce proper, sustainable management at approximately 30 MHPs (17 new ones and 13 existing ones) to ensure their efficient and permanent long-term functioning, (iii) to create jobs and raise personal income by promoting 150 rural microenterprises in the communities in which the MHPs are located, and (iv) to make more sustainable the model for promoting and strengthening rural micro power utility companies developed by the Intermediate Development Technology Group/Peru (ITDG).

Description:

The ITDG used financing from a 1992 small project to launch a program to establish micro hydroelectric power plants in rural areas. In 1998, an evaluation of the project found that despite the fact that the systems had been successfully established and benefits flowed to these communities, this alone was not enough to ensure that the systems were efficiently administered and that the beneficiaries made the most of the new power source. In order to make the system more sustainable and better utilize the MHPs, the evaluation recommended that ITDG: (i) design and put in place a suitable organizational model for strengthening MHP management, (ii) provide technical assistance to communities in order to promote and spark interest in the business opportunities offered by the productive and commercial use of the new energy resource, and (iii) arrange for additional resources to expand the program to other remote rural areas in Peru. The present project is ITDG's initiative to implement these recommendations.

This project will use reimbursable IDB funding to cofinance approximately 17 new micro hydroelectric power plants in isolated rural areas of northern Cajamarca (Jaén), a region in which ITDG recently established a presence. These power generation systems will provide electricity to between 8,000 and 10,000 persons and will serve as input for the creation of new productive microenterprises.

The technical-cooperation funding will make it possible to expand the program to a new area and will help the ITDG to apply and consolidate a new operating model for administration of the MHPs and to encourage the beneficiaries to strengthen and/or create microenterprises in rural areas. The new model will support the creation of local micro utility companies to administer the MHPs efficiently on a sustainable basis. To achieve this aim, the funding will be used: (i) to put in place an operating model and management team (MT) in the Jaén area, and (ii) to hire specialists to improve the technical and operating capacity of the management teams and the ITDG in general, particularly in terms of community organization,

economic analysis of power plants to be financed, environmental considerations, and the standardization of criteria for analysis and selection of the MHPs to be established.

**Environmental
Classification:**

The Committee on Environment and Social Impact reviewed this operation on May 14 and July 27, 1999, and made recommendations on the environmental and social criteria for the MHPs and the requirements for the environmental and social evaluation of the plants. The project team designed the operation, taking these recommendations into account.

Beneficiaries:

The program will have three types of beneficiaries: (i) residents of the communities in which the MHPs are built, (ii) the local micro utility companies that will have the organizational and economic capacity to operate the systems profitably on a sustainable basis, and (iii) the residents of the beneficiary communities receiving support for the promotion of new rural microenterprises based on the productive energy use. In quantitative terms, it is projected that 1,700 families (between 8,000 and 10,000 persons) will benefit directly from the project.

Risks:

There are two main risks that could affect the success of the program objectives:

The first risk, which is cultural in nature, is that the communities are not accustomed to having to pay for services paid services. The ITDG will minimize this risk through a campaign for promotion, training, and instruction in communities receiving MHPs.

The second risk has to do with management. Shortcomings stemming from administrative, economic, or structural dispersion in the municipalities managing the plants usually lead to increases in arrearages. These risks will be mitigated by means of the *new mixed or pure management model*, planned under the program as one of its innovations and the improved agreements with the municipalities.

**The Bank's
country and
sector strategy:**

The country paper for Peru (document CP-1279 of April 10, 1998) outlines *inter alia*, the importance of (i) promoting private-sector investment in productive infrastructure, with a focus on electric power generation and transmission, (ii) supporting microenterprise and small business, and (iii) reducing poverty, particularly among the very poor in the sierra and jungle regions. In this regard, the operation fits in with the Bank's strategy for the country.

**Special
contractual
conditions:**

As conditions precedent to the first disbursement, the ITDG will present, to the Bank's satisfaction: (i) the new format of the agreement between the ITDG and other cofinancing agencies that will be used for cofinancing the MHP, (ii) the new format of the agreement for granting MHPs to micro utility companies in which the new management model reflects the new responsibilities and powers of the parties and contractual conditions intended to minimize the problems identified in municipalities as a usual source of arrearages, (iii) the new agreement between the ITDG and the lender (AFIDER) that makes part of the service payment for coverage conditional on the Fund's at-risk level, (iv) the selection criteria for MHPs, and (v) the strategy for selecting the metering plan to be used in MHPs (meters or interrupters).

At the same time, the ITDG shall carry out the financing and technical-cooperation funding component for a period of 42 months from the date on which the respective agreements are signed.

Prior to the first disbursement of the technical-cooperation funding, the ITDG shall present to the Bank: (i) the annual operating plan for year one of the program, (ii) the definitive terms of reference for the project coordinator and the consultants in charge of implementing the program in the Jaén area.

The conditions of the technical-cooperation component are such that the program will need to have funding made available immediately. Accordingly, the Bank shall set up a revolving fund of up to 35% of the total amount of the component.

During program execution, the ITDG will take such steps as are appropriate to ensure that the proportion of its portfolio over 30 days past due remains below 8% of the total. Should this condition not be fulfilled, the Bank will be entitled to suspend disbursements, always taking into consideration any circumstances that might justify such a temporary increase in the level. To this end, during program execution, the ITDG shall submit quarterly reports to the Bank on the status of its loan portfolio which will be reviewed during program evaluation.

Two evaluations of the program will be performed, the first to be conducted when 50% of the financing has been disbursed, and the second 36 months into the program. The evaluations will gauge the extent to which the proposed objectives have been fulfilled, management of the loan portfolio, the social and environmental impact, and what the technical cooperation has accomplished. The Bank will hire the evaluators out of the proceeds of the technical-cooperation funding and future disbursements for the operation will

depend on its findings.

Because the technical-cooperation funding will finance part of the initial expenses incurred by the microenterprise promoter, the community promoter, and the project coordinator for a limited time, the ITDG shall guarantee payment of these expenses for a period of at least five years after the technical cooperation funding has been fully disbursed.