CASE STUDY – AFRICAN CDM PROJECTS

What Makes Carbon Transactions Bankable’

Muyi Kazim – Head of Carbon Origination Africa

Nigeria Sustainable Finance Week – Sept 2011
2. Standard Bank in Climate Finance
**Standard Bank in the Carbon Markets**

- One of the earliest banks to enter the carbon emissions space and a market leader
- Emerging market strength of the group gives us a natural advantage in the CDM project based market
- Operates within both primary and secondary markets. This adds to the flexibility that we can offer clients; a mixture of investment in primary projects to trading guaranteed credits
- We partner with other product groups from Investment Banking and Global Markets within Standard Bank to deliver the optimal solution
- Completed several ‘first to market’ transactions and award winning structures in carbon
- Unique Public private partnership through ACAD to help boost carbon credit activity in Africa

### Products

- Guaranteed CERs (certified emission reductions)
- Non-guaranteed CERs
- European allowances (EUAs)
- CER delivery guarantees
- EUA and CER options
- EUA and CER commodity repos
- VERs, ERUs, AAUs and other carbon credits

### Services

- Risk management
- Trading
- Structuring
- Financing
- Distribution
- Advisory
Standard Bank in the Carbon Markets

Finance
- Project
- Transactional
- Structured
- Origination
- Primary

Structured
- Trading
- Structuring
- Lending & Distribution

Traders & Funds

Compliance Buyers

CDM Project

Investors

Trading
- Primary
- Secondary
- Structured

Risk Management
- Cross Commodity

EUA/CER Swaps
- Repo Financing
African Carbon transactions mandated in 2010 and H1 2011

- **Tanzania**
  - 650,000 CERs
  - Efficient Lighting – POA

- **South Africa**
  - 1 millions CERs
  - Solar Water Heating – POA

- **Kenya**
  - 1.4 million CERs

- **Ghana**
  - 393,000 CERs
  - Municipal Waste Composting

- **Nigeria**
  - 270,000 CERs
  - Fuel Switch

- **Kenya**
  - 80,000 CERs
  - Small Hydro Power
African Carbon transactions mandated in 2010 and H1 2011

- **Nigeria**: 1.2 million CERs
  - Energy Efficiency

- **South Africa**: 5 million CERs
  - 3 REFIT Projects: 2 Wind, 1 PV

- **South Africa**: 2 millions CERs
  - 2 Solar Parks - PV
We can identify two significant challenges for any CDM project:

- Private Sector Capital for Financing Climate Change and CDM
- Public Sector Capital for supporting the private sector capital flow

The Question is Will there still be the ability for the Non-LDC Middle and Lower Middle Income African countries to do this?? Banks need to know in order to decide which projects to support.

Mobilising and Accessing Finance for Non-LDC CDM projects in Africa will increasingly be subject to the answer to the above question in the next 12 months.
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<td>Equatorial Guinea</td>
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<td><strong>Total</strong></td>
<td><strong>168</strong></td>
<td><strong>65</strong></td>
<td><strong>99368</strong></td>
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The Long Standing African Issue and Solutions

Why has the Clean Development Mechanism and resulting carbon credits been slow to implement in Africa?

Lack of Knowledge, **FI’s**, Industry, Regulators

Restricted availability of finance as a result of the above

Pricing of power from grid – Regional Grid Emission Factors

Tax rules uncertainty

What are recent improvements – creating solutions

Need for viable power and pricing of grid sourced power. Regional Grids

Increase in funding for ‘Real’ capacity building - Learning By Doing - Today

Increase in funding availability, if you have the know how to access it.
Actions to improve carbon finance in Africa

- Ability to use LDC CERs post-2012 and moves toward favouring African CERs

- New efforts to boost sub-Saharan African CDM
  - Working internally and with other African FIs to develop financing capacity in programmatic projects, small-scale and less ‘conventional’ projects
  - JV with UN agencies ‘ACAD’ aimed at supporting CDM process financing, supplying access to consultants, at no cost

- Requires cooperation across private and public sector
  - To meet challenges of:
    - 1. Feasibility study financing
    - 2. Early stage Equity financing......AfDB, DBSA the World Bank and other DFI’s as Guarantors projects or/and of Carbon offtake.
Carbon Credits are Like any Commodity – Price is Set by Demand and Supply Forces

- Sale of power and reactive power under PPA
- Incorporation of Carbon Credits into Normal Finance Instruments
  - Securitising carbon credit contracts in USD and EUR
  - Project Finance
  - Structured Trade Finance
  - Corporate Finance
  - Etc.
- Sale of carbon credits under ERPA

Energy Project

Utility

Compliance Buyer
Financing of CERs via trades
With Risk Factors

- **Spot trade:**
  - Wait until issuance and then sell
  - Highest price but exposed to price movement risk until issuance
  - Documentation: Spot ERPA or ISDA confirmation

- **Forward:**
  - Sell now for future delivery and payment
  - Avoids price risk but no up-front finance
  - Discounted price compared to spot but buyer takes price risk
  - Documentation: ERPA

- **Futures**
  - Enter a derivative contract for a fixed future price
  - Hedges price risk but penalties for non-delivery and need sophisticated trading arrangements
  - Documentation: ISDA
CER Forward Sale

Diagram source: Carbon Capital Markets. Prices indicative only and may not be accurate.
Making Carbon Transactions Bankable ……….
Financing needs of a project fall into a number of categories

<table>
<thead>
<tr>
<th><strong>Total capital requirement of a project</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Equity</strong></td>
</tr>
<tr>
<td>(ownership)</td>
</tr>
<tr>
<td>Initial project development costs</td>
</tr>
<tr>
<td>First X% of capital expenditure</td>
</tr>
</tbody>
</table>

**Gearing or leverage:**
If project is 70% debt funded, it has “70% leverage”

**Equity is typically spent on:**
- Design & feasibility
- Permits & approvals, EIA
- PIN, PDD, registration
- Legal & financing costs
- Initial project construction

**Debt is typically spent on:**
- Construction costs
- Re-financing equity once the project is at a less risky stage

- The riskier a project, the more equity is required compared to debt
- The earlier stage or riskier a project, the more expensive the debt

Stanbic IBTC Bank
A member of Standard Bank Group

Standard Bank
Typical sources of equity Needed To Be in Place to Assist Finance Inflow

- Owner investment ("Sponsor’s equity")
- Equity investors & funds
  - Banks often have equity investment arms and/or know equity investors
- Grant funding
- "Sweat equity": the owner works for free, this is limited (5 – 10% max)
- Pre-payment on CERs
Some Financial Products we can use in the CDM Projects Market

- Offtake Agreements (ERPAs)
- Pre-payments
  - 20-50% depending on project
  - Banks can pay more for good quality projects
- Corporate equity
- Corporate debt
  - Senior
  - Mezzanine
- Project finance
- Structured commodity finance & securitisation
Contracts for Buying Carbon credits from a Project

- Standard Bank have one of the most active trading desks in the carbon markets.
- Due to our high level of experience in markets and sophisticated valuation tools we can accurately price primary project risk and offer competitive price on primary carbon projects.

Carbon Contracts

- Advance Payment Agreements - APA
- Letter of Intent
- ISDAs
- ERPAs

Alternative pricing tools under ERPA agreements

- Fixed price over the term of ERPA – both pre and post 2012.
- Floating price over the period (On every delivery the current market price – less % is paid)
- Floating price with a floor and cap (limiting downside – showing possible financing a minimum income)
- Guaranteed delivery of a portion of the volume (this has a potential downside for the project owner)
- Ability of SB to prepay and cover CDM costs
<table>
<thead>
<tr>
<th>Project Types and Current Ease of Finance</th>
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<tbody>
<tr>
<td><strong>Typical finance type/difficulty</strong></td>
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<tr>
<td>HFCs, PFCs, N2O</td>
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<tr>
<td></td>
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<tr>
<td>Landfill gas</td>
</tr>
<tr>
<td>CMM/CBM/VAM</td>
</tr>
<tr>
<td>Cement-based</td>
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<tr>
<td>CHP/Cogen</td>
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<tr>
<td>Renewables</td>
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<tr>
<td>LULUCF-based</td>
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<tr>
<td>Energy efficiency (distributed)</td>
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</table>
What Risks are there in a Carbon Project?

- Construction
- Performance
- Credit
- Country
- Market
  - Carbon
  - Other
- CDM
  - Registration
  - Baseline
  - Performance/volume
  - Verification
  - Delay
  - Eligibility (Art.17)
  - Methodology
Risks Associated with Carbon Credit Projects

1. Carbon reduction assessment
   - Political risk
   - Counterparty credit risk
   - Resources and supplies delivery risk

2. Construction
   - Technology risk
   - Eligibility and approval
   - Delay in startup

3. Carbon transaction
   - Natural hazards
   - Business interruption

4. Issue of credits
   - Verification and certification

5. Conventional project cycle
6. Carbon related project cycle

Project risks
Carbon risks
Focusing on the ‘Traditional’ CDM risks

- Registration: Whether the project will be registered

- Baseline: What emissions are being displaced by the project?

- Performance/volume: Will the project perform? What volume of CERs will it produce (versus PDD)

- Verification: Will it be done? Properly? On time? What volume? Will the verifier find any problems?

- Delay: Will registration, verification or issuance be delayed? Why? What impact?

- Eligibility: Will the country remain qualified for carbon trading under the Kyoto Protocol (No Agreement for 2nd commitment phase yet)

- Methodology: Will the methodology change? Eg., HFC23

- Market risk: Is the developer selling guaranteed volume or un-guaranteed volume?

- Is the agreement subject to any rules and regulations remaining in place; EU ETS compliance?

- Pre-2013/Post-2012
### Investment Trends linked to CDM

64% of Investment in African CDM has been in the last 2.5 years; 50% in last 18 months

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Source: July 2011, UNEP Risoe CDM Pipeline
3. Case Studies
Structuring: Prefinancing against a single project

How a prepayment against carbon credits can enhance a financing structure

- For government-owned projects in emerging market countries, the following structure or similar have been used.
- Standard Bank would contract under an ERPA with project owner to purchase their carbon credits.
- Against this forward stream of income to the project, the bank would provide an upfront payment. This can be made in local currency if desired.

Diagram:

- **Emerging Market Government**
- **Parastatal Carbon Project Owner**
- **Standard Bank (Carbon)**
- **Standard Bank Project Finance**

Possible Guarantee of Payment obligations

Carbon Credits (under ERPA)

Prepayment against Carbon Credits

Term Loan and % of supply contract
Case study: Compliance buyer For a Primary Market Project in Africa

UK Cement Company given emissions cap of 1,000,000 tonnes for year, as shown in the UK NAP

- UK Cement Company allocated 950,000 EUAs by Government
- The company must purchase 50kt to have credits to ensure they have enough credits to meet their cap
- Standard Bank can sell the outstanding 50kt EUAs in spot or forward market to the company
- With an allocation of 1mt for the year the company is able to replace up to 9% of their EUAs with CERs
- Providing CERs remain at a discount to EUAs Standard Bank would offer a package to buy EUAs from the company, sell them back CERs
- Standard Bank Would act as the purchaser of the Primary Credits from the African Project, assisting their cash flow and immediate project support
- Standard Bank can offer fixed and floating price to the African project, and as it has access and experience of the market it would be able to meet long term requirements of the compliance buyer as a one-stop shop
CDM (Primary Market): Nigerian Industrial Project Being developed

Standard Bank Plc offered the client the following:

- Assistance in identification of projects and link up with suitable project developer to complete CDM process
- Through project finance offer funding for infrastructure changes required
- Forward contract agreed for stream CERS to help support project funding argument and projected cashflows
- Simple fixed or floating purchase of forward CER/carbon credit stream

Use of Gas and Capture of waste heat to generate power
- Gas previously vented?
- Current power grid mix?

Fuel Substitution
- Fossil fuel to gas or biofuel (grid mix?)
- Good supply?
- New equipment required?

- Substitution of clinker with slag and fly ash
- Consider what investment is required?

Nigerian company looking at various other projects to reduce emissions. Has opened up new business opportunities from the Carbon project development including Power Generation.
Standard Bank enters into contracts to purchase carbon credits from the implementation of energy efficiency projects with various building owners in South Africa via the Power Company.

These projects were registered under a PoA financed by Standard Bank. Building owners electing to register their energy efficiency projects under the PoA will sell CERs to SB.
Case study: Structured product for project developer

- A “first to market” transaction where we assisted an aggregator of carbon credits (Camco), structured and placed a proportion of their primary credit portfolio in the market

![Diagram showing structured product components and relationship with Standard Bank]
# Contact details

<table>
<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Email</th>
</tr>
</thead>
<tbody>
<tr>
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<td>Head of African Carbon Origination</td>
<td><a href="mailto:muyideen.kazim@stanbic.com">muyideen.kazim@stanbic.com</a></td>
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<tr>
<td>Geoff Sinclair</td>
<td>Head of Carbon Sales &amp; Trading</td>
<td><a href="mailto:geoff.sinclair@standardbank.com">geoff.sinclair@standardbank.com</a></td>
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<tr>
<td>Bill Pazos</td>
<td>Head of Carbon Origination, Asia</td>
<td><a href="mailto:bill.pazos@standardbank.com">bill.pazos@standardbank.com</a></td>
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1. Overview of Standard Bank Group
Standard Bank Group

- A global emerging markets bank, headquartered in South Africa
- In terms of total assets, Standard Bank is the largest bank domiciled in Africa
- Full-service bank covering
  - Personal & Business Banking
  - Corporate & Investment Banking
  - Investment Management & Life Insurance
- Leading financial services provider in South Africa – one of the fastest growing emerging market banking sectors. Growing market share across all sectors and a consistent track record of increasing profitability and franchise value
- The largest bank in Africa with presence in 17 countries
- Global reach on the ground in 14 countries outside Africa with distribution capabilities in the world’s leading financial centres: New York, London and Hong Kong
- Signed strategic partnership with the Industrial and Commercial Bank of China Limited (ICBC), one of the largest banks in the world by market capitalisation
- Total assets approximately US$202 billion (December 2010)
- Market capitalisation of approximately US$26 billion (December 2010)
- Present in 32 countries around the world
- Employs over 53,000 people (including Liberty Life)
Standard Bank Group

Locations

- Operates in 32 countries worldwide
- 17 African countries
- 15 countries outside Africa
- Universal banking capabilities
- Expanding global footprint

Note: Hong Kong, Beijing and Shanghai are counted as part of China
Unrivalled presence in Africa

Key points

- Over 150 years of experience in Africa
- Largest bank in Africa
  - Over 40,000 employees in Africa
  - Headquartered in Johannesburg
- Growth on the continent is a key strategic focus area
- Investment banking presence across the region and in key markets strengthened by recent acquisitions:
  - IBTC Chartered Bank, Nigeria
  - CFC Bank, Kenya

Unrivalled knowledge of sub-Saharan Africa

On-the-ground presence in 17 countries

- Angola
- Botswana
- DRC
- Ghana
- Kenya
- Lesotho
- Malawi
- Mauritius
- Mozambique
- Namibia
- Nigeria
- South Africa
- Swaziland
- Tanzania
- Uganda
- Zambia
- Zimbabwe
## Standard Bank Group structure

<table>
<thead>
<tr>
<th>The Standard Bank of South Africa (SBSA)</th>
<th>Stanbic Africa Holdings</th>
<th>Standard International Holdings</th>
<th>Standard Bank Offshore Group</th>
<th>Liberty Life</th>
</tr>
</thead>
<tbody>
<tr>
<td>West Africa</td>
<td>Standard Bank Plc London</td>
<td>Jersey</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nigeria, Ghana</td>
<td>SB Plc branches</td>
<td>Isle of Man</td>
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</tr>
<tr>
<td></td>
<td>and representative offices</td>
<td></td>
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<tr>
<td>East Africa</td>
<td>Central Africa</td>
<td>Mauritius</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kenya, Tanzania, Uganda, Malawi</td>
<td>DRC, Angola, Zambia</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Southern Africa</td>
<td>Standard Bank Asia</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Namibia, Botswana, Zimbabwe, Mozambique, Lesotho, Swaziland</td>
<td>Standard Bank Brazil</td>
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<td></td>
<td>Standard Bank Argentina</td>
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<td></td>
<td>Standard New York</td>
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<tr>
<td>Indian Ocean Islands</td>
<td>Other entities/Partnerships (e.g., Standard Resources (China) Ltd, Standard Ünlü)</td>
<td></td>
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</tr>
</tbody>
</table>
Asia: Strategic partnership with ICBC

The Industrial & Commercial Bank of China Ltd (ICBC) bought a 20% strategic shareholding in Standard Bank in March 2008 for USD5.5 billion

- Established a gateway between Africa and China
- Accelerates the banks’ respective international strategies
- Provides support for Standard Bank’s next phase of growth
- Provides unrivalled access into China and its state owned enterprises (“SOEs”)
- Formal commitment to support Standard Bank’s activities in Africa and other emerging markets, providing balance sheet access and syndication
- Has facilitated strategic alliance with China Africa Development Fund
- Facilitated co-operation principles with Sinosure for credit and trade guarantees
- Partnerships established for fund management activities

Key facts and figures

- ICBC has more than 385,000 employees
- Over 16,500 branches
- 190 million personal clients
- 3.1 million corporate clients

Product capability

- ICBC is a full service universal bank

Key strengths

- Largest bank in the world by market capitalisation (2008)
- Market leader in all its businesses
- Strategically keen to grow in emerging markets and build on the significant China-Africa trade flow
<table>
<thead>
<tr>
<th>Awards</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Standard Bank awarded ‘Best Investment Bank in Africa 2009’</strong></td>
</tr>
<tr>
<td><strong>Best Investment Bank in Africa – EMEA Finance 2009</strong></td>
</tr>
<tr>
<td><strong>Best Investment Bank in Nigeria – EMEA Finance 2009</strong></td>
</tr>
<tr>
<td><strong>The Banker Bank of the Year</strong></td>
</tr>
<tr>
<td>Africa, Botswana, Lesotho, Malawi, South Africa, Swaziland, Tanzania</td>
</tr>
<tr>
<td><strong>Best Trade Finance Bank in sub-Saharan Africa 2009</strong></td>
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<tr>
<td><strong>Africa Power Deal of the Year – Morupule B 2009</strong></td>
</tr>
<tr>
<td><strong>Energy Resources, Mongolia</strong></td>
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<tr>
<td>Agro Traders Limited, Nigeria</td>
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<tr>
<td>Wataniya Palestine Telecom</td>
</tr>
</tbody>
</table>
Awards (cont’d)

EUROMONEY ProjectFinance
Morupule B – Africa Power Deal of the Year;
Paladin Energy - Kayelekera Uranium Mine Africa Mining Deal of the Year;
Lakatabu Expansion – Africa Industrial Deal of the Year;
MTN Uganda – Africa Telecoms Deal of the Year;
Zain – Middle East Telecoms Deal of the Year

Trade Finance
Energy Resources (Mongolia)
Agro Traders (Nigeria)
Cocobod (Ghana)

Best Syndicated Loan Deal in CEE & CIS for Ukrexim’s June 2009 EBRD Senior Unsecured A/B Syndicated Loan, 2009
Best Syndicated Loan Deal in Africa for Naspers $1.6 billion Forward Start Facility, 2009