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EVALUATION SUMMARY INVESTMENT STUDIES

ACCELERATING PRIVATE SECTOR INVESTMENT IN RENEWABLE ENERGY

CIO FACTS

- SCOPE: Blended finance facility
- SECTOR: Renewable Energy
- REGIONS: Africa, Asia & Latin America
- SIZE: USD 930 million
- PERIOD: 20 years

CIO ANTICIPATED IMPACTS

- Electricity Generated: ~5,100 GWh p.a.
- Greenhouse gas (GHG) or equivalent emissions avoided: ~1.9 million tCO2e p.a.
- Number of People Served: ~13 million
- Private sector funds catalyzed at construction phase: ~2.5+ billion USD
- Direct job creation: more than 10,000 jobs

INTRODUCTION

Climate Investor One (CIO), is FMO's first 'blended finance' investment vehicle to accelerate private sector investments for climate mitigation and adaptation in developing countries. Managed by Climate Fund Managers (CFM), CIO provides financing at each project stage to renewable energy (RE) projects across Africa, Asia, and Latin America.

CFM raised USD 930 million for the Development Fund (DF) and the Construction Equity Fund (CEF) from a total of 21 public and private investors. It is fundraising for the Refinancing Fund targeting the ongoing operations phase. CIO plans to recycle capital into different projects over 20 years.

CIO's unique financing approach seeks to reduce the time and cost of developing RE projects and improve the quality of delivery via CFM's engineering, financial, and environmental, social and governance (ESG) experts.

By March 2023, CIO had committed USD 577.6 million and contracted 20 projects, of which 15 are active. One project has already exited.

As co-founder, FMO invested USD 50 million in CIO and has also taken a stake in CFM. The Dutch Government has also invested USD 55.6 million.

SCOPE OF THE STUDY

In 2022, FMO, on behalf of the Dutch Government, commissioned SQ Consult to conduct an independent learning-focused evaluation, five years into CIO's 20-year implementation period.

The evaluation assessed CIO's current functioning and progress towards its investment and development impact objectives. Given the early stage of implementation, this evaluation focused on assumptions underpinning the CIO's logic and early indications of impacts.

This evaluation was conducted between November 2022 and July 2023, and covers the period from operationalization of CIO in 2017 through first quarter 2023 reporting, which was available mid-June 2023.

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KEY FINDINGS AND CONCLUSIONS

The evaluation found that CIO is relevant and to a large extent effective in supporting RE projects to complete construction and achieve ongoing operations. CIO is more effective at addressing financial than non-financial barriers. CIO investments already operating include wind projects in Vietnam, hydro in Uganda and rooftop solar across Asia. The evaluation's overarching conclusions are:

#1: Overall, CIO's pilot of the bundled concept is a success. At year five of a 20-year period, CIO is making good progress in contracting and supporting project developers to complete projects despite early challenges and the COVID-19 pandemic.

#2: CIO's financial and non-financial support is helping projects succeed. CIO demonstrated both financial and non-financial additionality for all projects reviewed, though the nature and extent varies. Project developers are satisfied with CIO overall, though some find the multi-stage contracting and limited financing options challenging.

#3: CIO is operating differently than assumed in the 2019 strategy, which is fixed for 20 years. CFM has shifted towards investing in developers with a pipeline of projects, termed 'platforms', rather than single projects. The types of financial structuring, additionality and viability assessments originally assumed do not fit platforms well. CIO is also coming in later in the development cycle. These variances are partly due to the long implementation period, outdated assumptions on market characteristics, and the fast pace the RE sector is evolving.

#4: CIO's ability to meet lifetime targets will depend on the size and type of projects it supports due to trade-offs inherent in project selection. Each project has a unique impact profile, and the types of projects CIO engages and markets it operates in are constantly evolving. To date, CIO appears on track to meet the lifetime quantitative targets of installed capacity of RE, total RE power production and annually avoided GHG emissions. It may miss those on number of equivalent people with improved access to RE and finance catalyzed, depending on investments over the next 15 years.

#5: Overall, CIO's governance structure is functioning as intended, though requires proactive management for donors and CFM. There are tensions arising out of different priorities, such as between financial return and development impacts, and ways of working for public and private investors that require ongoing proactive management from all involved. FMO has an unusually large number of ongoing roles, which can create inefficiencies and information imbalances.

#6: The concept is not being fully replicated in part due to the complexity. While private equity funds for RE are now more common especially for later project stages, CIO's bundled concept has not been replicated for RE. The most direct examples are later facilities developed by CFM that target different sectors, such as Climate Investor Two (CI2). Public investors find CIO's operational and fee structures complex and challenging to fully understand the implications of in practice over time.

#7: Several suboptimal elements and obsolete assumptions of CIO's operational structure have been identified, which CFM seeks to address within contractual limitations. For example, CFM is not able to change the requirement to replicate the CEF tier structure (i.e., proportions for each investor class) at the fund level to the project finance level, which causes delays.

#8: Though often necessary, requirements and restrictions impede progress. The more requirements and restrictions investors place on a fund manager like CFM, the more contortions they must do to find projects that will be successful, which slows progress. Lengthy approval processes due to public investor requirements also reduce CIO's attractiveness to developers relative to other options.

#9: The 20-year fixed investor funding contracts are too long for such a rapidly evolving context. The length was intentional to allow an opportunity to (i) go through two to three project funding cycles and (ii) respond to preferences of some investors. However, this creates risks as CIO lacks periodic milestones to adapt contracts, including fee structures, eligibility or financing parameters and overall strategy to reflect updated understandings and context.

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#10: CIO's current monitoring framework is suboptimal for reporting against its Theory of Change (ToC), but CFM is already addressing this. The key impact indicators (KIIs) do not capture all the impacts targeted by CIO's ToC. Comprehensively tracking intended impacts will be necessary not only to understand the full development impact of CIO but also to better understand the benefits for the end-beneficiaries. CFM is currently working to refine the ToC, develop a detailed results framework including additional impact indicators, and develop a monitoring and evaluation (M&E) framework.

#11: CFM's systems and operational capacities are still maturing. While CFM has highly experienced staff, they are still building capacities which creates challenges, such as with back-office capabilities, communications and reporting requirements. Some areas of the organization are well developed, such as project development teams and fundraising for other facilities, while others such as managing diverse and increasing reporting requirements for CIO are still being developed or upgraded.

RECOMMENDATIONS FOR CFM

The evaluation generated several recommendations for CFM. These include the recommendation that CFM should continue to apply lessons learned within the limitations of CIOs agreed structure. More in-depth improvements, such as increased flexibility in financing options, are being incorporated into CFM's later facilities (e.g. CI2). Furthermore, as a new organization, CFM needs to continue to expand internal capacities and operational systems, including ways to streamline the experience for project developers. Finally, CFM is recommended to seek to better reflect CIO activities and results to public investors, such as by exploring ways to incorporate ESG in asset valuation and calculate impact per dollar spent.

RECOMMENDATIONS FOR FMO

The evaluation also included two recommendations for FMO. First, FMO should designate a person at the senior management level to have an overview of all ongoing FMO roles in CIO for the remaining 15 years of implementation. Second, FMO should conduct an assessment of all its roles, to consider how the roles can be optimized for future funds.

WHAT WE LEARNED?

- **Any RE fund should be prepared for rapid evolutions in RE markets throughout the lifetime of the fund.**
- **When setting up innovative funds, funds should ensure contracts have sufficient flexibility to incorporate learning, especially if the fund has a long lifetime.**
- **Funds likely need to provide both financial and non-financial additionality to facilitate successful RE projects.**
- **It is challenging but possible to navigate the differences in priorities and requirements of public and private investors.**

FURTHER INFORMATION

FMO roles in CIO:
https://www.fmo.nl/governance-related-to-cio-and-cfm

CFM website:
https://climatefundmanagers.com

SUGGESTIONS FOR FUTURE FACILITIES

Evaluators have three suggestions for public investors as they consider supporting blended finance mechanisms in the future:

1. Seek to fully understand the core parameters, how the strategy may evolve and how the fee structure will manifest over the life of the fund.

2. Maximize flexibility for the fund by limiting restrictions attached to contributions and clarifying expectations as the context evolves.

3. Standardize reporting requirements and timetables across public investors as feasible.