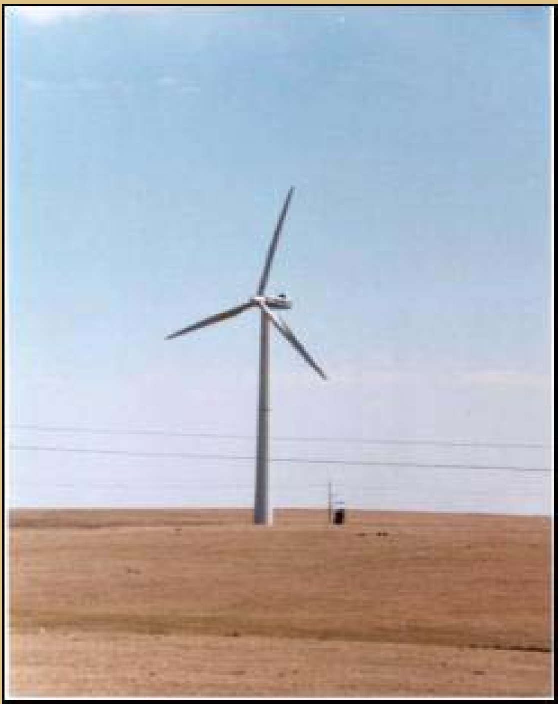
Central America
New Development Credit Guarantee to Fund Clean Energy Investment

A development credit guarantee program that will help finance renewable energy, energy efficiency and cleaner energy production was approved unanimously by USAID's Credit Review Board on Nov. 4, 2004.

Initiated by EGAT's Energy Team, the Central American Renewable Energy and Cleaner Production (CAREC) Facility will offer middle or "mezzanine" financing instruments in seven countries in the region.



Investments in renewable energy, such as windmills, will get a leg up from CAREC

A "facility" is a special purpose fund and "mezzanine" financing serves as a bridge to help entrepreneurs access normal bank loans—such bridge loans make up for a borrower not having enough equity (capital) or collateral to secure the full amount needed to complete a project. The idea is for CAREC to customize its financing products to offer the specific type of support that project developers need in order to secure bank loans. In this way, CAREC will help bring local banks into the clean energy lending business and hopefully lead to sustained lending once CAREC has exited the sector.

To get started, CAREC will need to raise $15-20 million. USAID has agreed to guarantee up to $5 million of CAREC facility's borrowing. CAREC, in turn, will market its loans directly to energy sector companies. It is expected that CAREC will directly support over $60 million in total project costs.

For instance, a bank may offer to lend 80 percent of capital needed for an infrastructure project, although the borrower's own capital only covers 10 percent. A second loan, financed by CAREC, would cover the remaining 10 percent. Or, if an entrepreneur cannot put up collateral that is worth as much as the bank loan for which s/he is applying, a CAREC loan would bridge the difference between a fully collateralized loan and the total amount of capital needed for the energy project.

"The mezzanine financing is designed to provide critical 'bridging' financing to enable project developers and small business owners to access traditional bank loans. It doesn't try to replace or compete with bank lending," said Jas Singh, the CAREC project officer on the Energy Team. "This project offers an excellent opportunity to test these new types of 'mezzanine financing' instruments for small- to medium-scale infrastructure projects," said Singh, adding that "it might be a model for other regions and sectors."

Critical barriers to affordable financing in Latin America and the Caribbean for such projects have not been a lack of capital, but loan requirements that are hard for developers and small businesses to meet, in particular high collateral and ownership (project equity) requirements.

Designers of the CAREC facility see it as a low-cost and low-risk opportunity to test whether a partial guarantee can help overcome these barriers.

(The bridge loans that CAREC will guarantee are “subordinate” to primary loans—they are repaid from the debtor’s assets after the first loan, in case of bankruptcy. They are therefore riskier loans. Credit guarantees help lower the risk.)

The new, independent fund will be managed by E+Co, a non-profit, U.S. financial services company and fund manager with a strong track record in clean energy project finance. CAREC is also supported by the International Development Bank’s Multilateral Investment Facility (MIF), the Central American Bank for Economic Integration (CABEI), a Belgian development bank (BIO) and a Finnish development bank (FinnFund).

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