KEPSA
KENYA PRIVATE SECTOR ALLIANCE
The Voice of the Private Sector in Kenya

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Financing Private Sector Climate Change Action

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Major financial investments – from both public and private sources – are required for Kenya's transition to a low carbon climate resilient economy. An estimated Ksh 1,085 billion is required to implement Kenya's National Climate Change Action Plan (NCCAP) from 2013 to 2017[1]. Kenyan private sector engagement and financing will be needed to implement the action plan, and important issues moving forward include:

- Improving the enabling environment to attract climate-friendly investments in key sectors of the economy;
- Securing financing and support for climate innovation;
- Facilitating carbon trading opportunities, where appropriate[2].

Improving the Enabling Environment

Relative to several comparative countries, Kenya is a good place for the private sector to undertake low-carbon investment. The features that support private sector investment in Kenya include its high GDP and energy demand growth, excellent renewable energy resources and high energy efficiency potential, fairly favourable regulatory environment, and a relatively well-developed financial sector. The NCCAP estimates that the private sector, both domestic and international, has already invested more than US$2.8 billion in renewable energy production in Kenya[3].

Experience shows that policy and regulatory reform to overcome barriers and reduce risk can help to incentivise private sector investment for climate change action. The main challenges facing the private sector include a project development process that is long and arduous, and policy interventions and incentives that could be improved or are poorly implemented[4].

Continued improvements to encourage a conducive environment for climate investment include:

- **Establishing a regular platform for continued engagement and dialogue between the Government of Kenya and both domestic and international representatives of the private sector** on matters relating to Kenya's low carbon growth strategy. KEPSA could play a role in promoting this dialogue.
- **Implementing climate change-related policies, strategies and regulations**, such as the draft Climate Change Bill 2014, draft Climate Change Policy 2014, draft Energy Bill 2013 and draft Energy Policy 2014.
- **Building capacity among Kenyan businesses** to develop feasibility studies, understand and develop financing models, and manage and account for finances. Some support is available for firms through such initiatives as the Kenya Climate Innovation Centre, described below.
- **Developing Nationally Appropriate Mitigation Actions (NAMAs)** in areas that promote private sector action. An example is the NAMA that aims to accelerate geothermal power development through the significant scale up of private sector investment and participation, which has been submitted to the United Nations Framework Convention on Climate Change's (UNFCCC) NAMA registry.

Improving Access to Climate Financing

For many private sector entities, innovative climate-friendly technologies, such as solar and wind power, are new and untested investments, and perceived as riskier than their business-as-usual counterparts. Public financing, both domestic and international, can play a critical role in mitigating risk and leveraging greater private investment in climate projects.

Kenyan banks have been increasing their engagement in climate change-related products and deals with the private sector with support from the donor community (see Box 1). These initiatives have increased private sector access to domestic finance by helping banks

Box 1: Climate change-related programs of Kenyan banks

- Cooperative Bank and CfC Stanbic Bank have partnered with the French Agency for Development and the Kenya Association of Manufacturers to provide investment in renewable energy and energy investments.
- Standard Bank Group and its subsidiary CfC Stanbic Bank will underwrite US$90 million of a $150 million wind power plant established by independent power producer Aeolus Kenya, while Norway's Norfund and a large Africa-focused international infrastructure investor will provide US$60 million in equity.
- Micro-Africa Ltd., Rafiki Micro, and Family Bank provide clean energy loan products that assist borrowers in purchasing biogas systems, solar lighting, improved cookstoves and water tanks.

Source: Stanbic (2013), *Standard Bank Group in US$150m deal to build wind power project in Kenya*; and Finance Innovation for Climate Change Fund.

understand the risk profile of climate-related action and overcoming constraints to borrowers, such as high interest rates and collateral requirements and short loan tenors. Banks in Kenya generally have not been interested in financing climate change-related investment projects because they are not fully aware of the returns that can be realized and have limited experience in this area[6].

Kenyan private sector firms can access climate change initiatives to ramp up innovation and move into new markets for climate-friendly goods and services. Initiatives include:

- **Centre for Energy Efficiency and Conservation at the Kenya Association of Manufacturers** – offers subsidized energy audits and energy training (see briefing note #10 on Kenafric's experience).
- **Grassroots Business Fund** – investments in the range of US$ 500,000 to US$ 2,000,000 for environmentally and socially responsible companies with strong management structures, preferably in a growth stage.
- **International Finance Corporation, Housing Finance Partnership** – short-term loans and long-term financing to help pioneer the market for environmentally green housing.
- **Kenya Climate Innovation Centre** – proof of concept (up to US$ 100,000) and seed funding (up to US$ 750,000) for entrepreneurs and small and medium enterprises to scale up and deploy innovative clean technology solutions.
- **Kenya Green Energy Foundation** – start up green grants for sustainable renewable energy initiatives.
- **Regional Technical Assistance Programme, Kenya Association of Manufacturers** – loans to help commercial end-users implement energy efficiency options.
- **Renewable Energy and Adaptation to Climate Technologies (REACT), Africa Enterprise Challenge Fund** – repayable grants up to a maximum of US$ 1.5 million for renewable energy and adaptation technologies.

KEPSA has a list of funds that can be accessed by the Kenyan private sector (please contact KEPSA to obtain the list).


Photo credit: IISD Reporting Services

Improving Understanding of Carbon Markets

Kenya's carbon market experience

Kenya has been active in the carbon market, hosting a series of innovative projects through the compliance and voluntary markets. Kenya's experience includes:

- Sixteen registered CDM projects as of June 2013 in such sectors as reforestation, geothermal, wind and hydro.
- Sixteen CDM Programme of Activities in such sectors as cookstoves, efficient lighting and renewable energy.[7]
- The Kenya Agricultural Carbon Project, supported by the BioCarbon Fund and SCC-VI Agroforestry, which is the first project in Africa to sell carbon credits under the voluntary market for sequestering carbon in soil.
- The Kasigau Wildlife Corridor REDD (reducing emissions from deforestation and forest degradation) Project, the first activity to issue voluntary forestry carbon credits.

Box 2: Improving the policy and regulatory environment in the energy sector

The Government of Kenya is undertaking to reform and improve the policy and regulatory environment for renewable energy and energy efficiency. This includes:

- On-going drafting of the draft Energy Bill 2013 and draft Energy Policy 2014
- Revising the feed-in tariffs policy in 2012
- Enacting the 2012 solar water heating regulations
- Developing templates for power purchase agreements
- Developing connection guidelines for small-scale renewable generating plants in 2012

Source: Government of Kenya (2013), National Climate Change Action Plan 2013 – 2017 (Nairobi: Ministry of Environment and Mineral Resources), pages 83-94.

Limited carbon market opportunities

While Kenya has been successful in accessing finance through carbon markets, current and future market conditions indicate that it will be more difficult for the private sector to access this finance. Carbon markets do not hold the promise they once did for Kenya for three main reasons:

- **Lack of access to the EU-ETS compliance market** – The EU-ETS introduced restrictions on the use of international credits, such that CERs from projects registered after December 2012 will only be eligible if they are hosted by least developed countries or in countries that have a bilateral agreement with the EU. Kenya is not eligible to supply CERs for the EU compliance market because it is not a least developed country and does not have a bilateral agreement.
- **Oversupply of credits** – An oversupply of credits combined with a lack of demand means that the price of CERs is low, around US$ 0.55 per tonne of carbon in early February 2014.[8] Current finance flowing through the CDM is very low, reflective of this very low price signal. The World Bank expects that the supply of CERs and other credits is likely to outweigh the global demand for the 2013 to 2020 period. Without a major change in the supply-demand imbalance, no significant price recovery is expected in the near future. This provides little incentive for project developers to originate new CDM project activities; and the low price does not cover the cost of certification of CERs for some existing CDM projects. Most carbon project developers are limiting their CDM activities as a result of market conditions.[9]
- **Weak carbon markets** – contributed to by:
  - **Uncertainty around an international climate change agreement** – Decisions on new international emission reduction targets and new market mechanisms are not expected before 2015, and implementation of any new international climate change agreement is not expected before 2020. This uncertainty, combined with a lack of ambition in reduction targets in developed countries and continuing effects of the economic crisis, impacts the CDM and limits the allocation of private capital to climate change mitigation.
  - **Uncertain role of international offsets in emerging carbon trading schemes** – Some demand is expected in the New Zealand and Japanese schemes, with reduced demand in the EU ETS, demand limited to REDD+ credits in California, and no demand in other schemes such as the Regional Greenhouse Gas Initiative in the northeast United States.

The World Bank reports that until the lack of demand for CERs is addressed, the CDM market will continue to slow down and uncertainty will remain around the role of the mechanism in the international climate policy landscape.[10]

Voluntary Carbon Market

The voluntary carbon market may provide some limited opportunity for Kenya. Voluntary actors contracted 101 million tonnes of carbon offsets in 2012, at an average price of US$5.90 per tonne (more than the 2012 CDM carbon offset price of less than US$1 per tonne). Ninety per cent of these offset volumes were contracted by the private sector, with corporate social responsibility and industry leadership being the primary motivations for offset purchase. Most private companies channelling financial resources through the voluntary market focused on carbon reduction projects that delivered positive benefits "beyond carbon."

Kenya was the world's fourth largest supplier county in the 2012 voluntary carbon market, supplying over 4 million tonnes of carbon offsets.[11] Kenya attracted corporate support for REDD projects and projects delivering clean cookstoves and water filtration devices.

Climate Finance: What can you do?

Responding to the climate change challenge will require significant resources. Opportunities exist for your business to leverage and access funds to support climate innovation and investment, with your decisions based on a careful assessment of climate finance opportunities. You can take action by:

- **Encouraging and assisting KEPSA to engage with the Government of Kenya to improve the enabling environment.** The right policies could help move investment to climate-friendly-alternatives, and a regular platform for continued engagement and dialogue could allow business representatives to advise on climate-friendly policy and regulation.
- **Assessing climate financing initiatives that may be available to your business**, and your eligibility to apply. Some funds in Kenya support private sector innovation, and increasingly banks are interested in providing loans for climate-friendly technologies. KEPSA can help by providing a list of funds

Box 3: The Carbon Market – Definitions

Carbon market – a market that is created from the trading of units of greenhouse gas (GHG) emissions.

Kyoto Protocol – adopted under the UNFCCC, the international protocol commits developed countries to reduce their GHG emissions.

Compliance market – the regulatory market created through trading of GHG units under the Kyoto Protocol and other international agreements. The European Union Emissions Trading Scheme (EU-ETS) is currently the main compliance market.

Carbon credit or offset – a financial unit of measurement that represents the removal of one tonne of carbon dioxide equivalent from the atmosphere. Carbon credits are generated by projects that deliver measurable reductions in GHG emissions.

Clean Development Mechanism (CDM) – a mechanism created under the Kyoto Protocol that allows emitters in developed countries to purchase carbon credits from GHG emission reduction projects in developing countries.

Certified Emission Reductions (CERs) – carbon credits issued for emission reductions from CDM project activities and certified under the Kyoto Protocol.

Voluntary market – the market created through carbon credit purchases that are made voluntarily. This market is driven by companies for corporate social responsibility reasons.

Verified Emission Reductions (VERs) – carbon credits issued for emission reductions not certified under the Kyoto Protocol. Buyers tend to pay a discounted price in the voluntary market because of the inherent regulatory risks.

Source: *informed by The Gold Standard (2014) Carbon Market FAQs; and Orbeo (2014), The CO2 Market: Glossary.*

that can be accessed by the Kenyan private sector (please contact KEPSA to obtain the list).

- **Assessing carbon market conditions before investing too many resources in trying to access a source of climate finance that is likely to diminish in the short to medium term.** Explore if the voluntary market offers opportunity for your business.

Kenya has been active in the carbon market, hosting a series of innovative projects through the compliance and voluntary markets.

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For further information, please contact Victor Ogalo, KEPSA (vogalo@kepsa.or.ke), or Deborah Murphy, IISD (dmurphy@iisd.ca). Information about KESPA and its work can be found at www.kepsa.or.ke. Information about IISD and its work can be found at www.iisd.org.

Endnotes

1. The NCCAP mitigation analysis determined that implementing six priority low-carbon actions (restoration of forests on degraded lands, geothermal, reforestation, improved cookstoves, agroforestry, and bus rapid transit and light rail corridors) would require investments of Ksh 1,371 to 1,733 billion until 2030. Out of these investment costs, an estimated Ksh 839 to 1,110 billion would have to be borne by the public sector with the remaining costs covered by private sector and household investments. See Government of Kenya (2013), National Climate Change Action Plan 2013 – 2017 (Nairobi: Ministry of Environment and Mineral Resources), pages 144-153.
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3. Government of Kenya (2013), page 88.
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6. Ellis, K., Lemma, A., Mutimba, S. and Wanyoike, R. (2013), Low Carbon Competitiveness in Kenya (London: Overseas Development Institute), page 38.
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9. Ecofys (2013), Mapping Carbon Pricing Initiatives: Developments and Prospects 2013 (Washington, D.C.: Carbon Finance at the World Bank), page 17.
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(T) +254 20 2730371 | 2 | 2727936 | 883
info@kepsa.or.ke | www.kepsa.or.ke

The Kenya Private Sector Alliance (KEPSA)
Shelter Afrique Building, 5th Floor, Mamlaka Road
P.O. Box 3556-00100 Nairobi Kenya