Risk appetite of banks for small merchant renewable energy plants remains low

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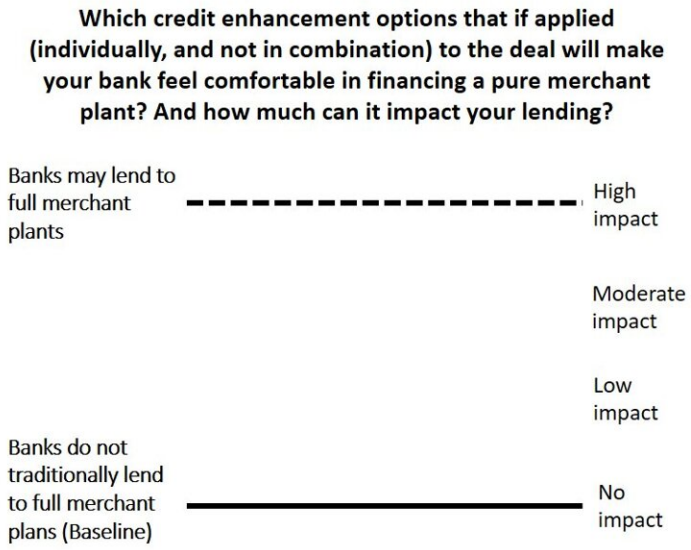

	Option	Private bank
1	Government as equity investor	Low
2	Large buffer in spot market prices	Low
3	High Debt Service Reserve Account	Low
4	Short tenor	Low
5	Limited dividends for investors	Low
6	Lower debt-equity ratio	Low
7	Partial contracting	Low
8	Sculpted debt payments	Low
9	Higher interest rate	Low
10	Sponsor's guarantee	Moderate - High

A graphic representation of the survey Dr. Sunio and his team conducted with six commercial banks. Credit: Varsolo Sunio

As the global demand for power continues to rise, so too does the number of small merchant renewable energy plants, which augment the supplies of existing energy companies. These plants are independent, typically small scale, and focus on renewable energy sources, such as solar and wind.

With more commercial banks pursuing bold sustainability targets in

support of the Paris Agreement, there was an expectation that these plants would now find it easier to secure bank financing. However, a study published in the KeAi journal *Global Transitions*, suggests this is far from true.

Dr. Varsolo Sunio, the research lead, explains that "it used to be nearly impossible for developers of renewable energy projects to secure loans from commercial banks, especially if they were not backed up by long-term contracts with distribution utilities, or guarantees by large conglomerates. However, recently, with the trend towards the 'greening of banks', we were hopeful that this would open up more financing possibilities.

"But, contrary to our expectations, this is not really the case—the risk appetite of banks for small developers of merchant renewable energy plants remains low."

For the study, the research team presented representatives from six banks in the Philippines with 10 options for appraisal, and asked them to assess their potential as credit enhancements or risk mitigants. Dr. Sunio reveals that "they found that commercial banks continue to base their funding decisions on the presence of 'offtake agreements', in other words, guaranteed customers, plus a 'strong principal sponsor'. For small and independent developers of renewable merchant plants, obtaining either of these poses great difficulties."

However, Dr. Sunio and his team found that government banks in the Philippines were more open to providing credit to small developers, even in the absence of offtake agreements and sponsor guarantees. He attributes this flexibility to the government banks' mandate to support national development.

He adds that their "findings show that while banks acknowledge the role

they play as catalysts in mobilizing capital to finance the transition to renewable energy, merchant plants continue to be considered risky. We believe that more policies, strategies and innovations need to be explored to provide merchant plants with an opportunity to raise financing."

More information: Varsolo Sunio et al, Does the greening of banks impact the logics of sustainable financing? The case of bank lending to merchant renewable energy projects in the Philippines, *Global Transitions* (2021). DOI: 10.1016/j.glt.2021.12.001

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