



Case Study:

Financing Climate Friendly Solar Solutions for Energy Intensive Commercial Clients: The Case of Standard Chartered Bank and Uhuru Flower Farms

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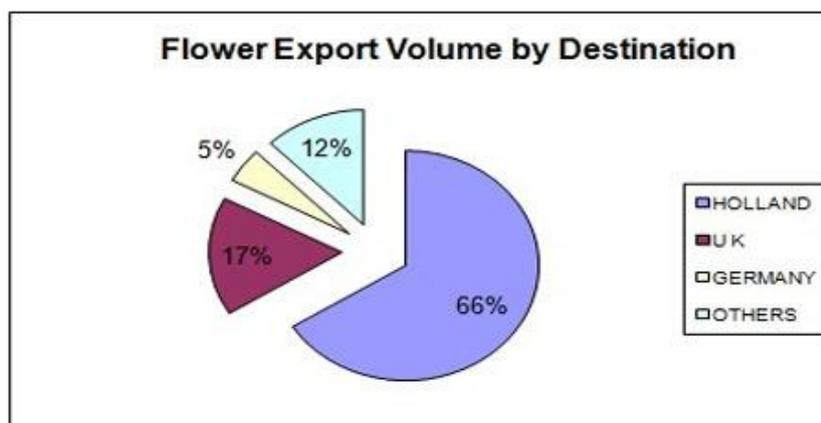
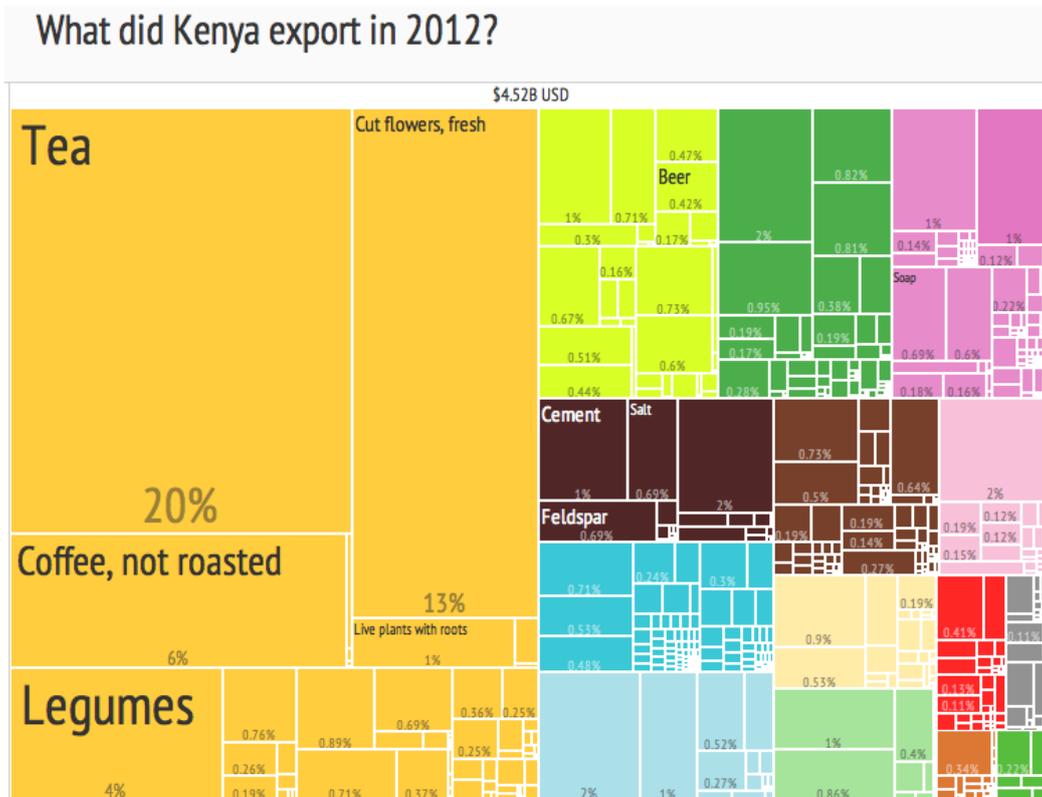
Abstract

In 2013, Standard Chartered Bank approved a three-year loan to Uhuru Flower Farms to purchase an in-house solar system and disconnect from costly and unreliable grid power. The solar installation generated significant cost savings for the company, by eliminating its monthly energy bills and reducing the incidence of perished flower stock. In the tight-knit flower farm industry, news of this led to two other flower farms approaching Standard Chartered for loans to install similar systems. This case study illustrates the growing suite of commercial opportunities which climate-friendly financing represents to Kenyan banks and their customers. It also underlines the opportunities for banks to increase revenues, market share and reputation by financing energy efficiency innovations that improve the resilience and profitability of their clients' operations while supporting the greening of the Kenyan economy.



Background

Cut flowers are big business in Kenya, representing a significant proportion of Kenya's exports. According to the Harvard Atlas of Economic Complexity, cut flowers represented 13% of total exports in 2012 (see below). Kenya's Flower Council reports that the country is the lead supplier of cut flowers to the EU, with volumes growing from 10,946 tons in 1988 to 86,480 tons in 2006 and 124,858 tons in 2013. The Kenya National Bureau of Statistics reported that the export value of floriculture produce in 2013 was KSh46.3bn.



Despite the growth enjoyed by Kenya's flower industry, success is not guaranteed. There are significant costs involved in running a profitable flower farm, from finding sufficient and affordable capital to securing land and setting up the infrastructure.

Key facilities include greenhouses equipped with irrigation and ventilation systems, and cold storage facilities to house the stock between harvesting and transportation. With this equipment operating continuously to ensure that the flowers receive the correct humidity, moisture and temperature, energy can account for 60-70% of total recurrent costs.

Equally important, is the reliability of power to operate these systems. However, the national grid in Naivasha, where the majority of farms are clustered, is reliable only for its frequent power cuts and weak voltage; companies are constantly considering innovative strategies to reduce energy costs and improve energy reliability.

Solar financing transaction



Photo from Uhuru Flower Farm website

By 2013, with Uhuru Flower Farm incurring KSh500,000 in monthly energy bills, suffering regular stock loss due to power outages, and facing increasing costs of fertilizers, labor and airfreight, its owner, Ivan Freeman, had clear incentives to identify and implement cost saving measures to safeguard the business.

Azimuth Power Ltd was identified as a local supplier able to install a solar power plant with sufficient capacity – 72 kW – to meet Uhuru's needs. Although the cost of installing one kilowatt hour of solar power in Kenya is about \$2.20-\$2.70 compared with the United Kingdom's \$1.70-\$1.90, Freeman decided that the total cost of KSh15m (\$177,000), with a forecast of return on the investment in just five years, was



worth incurring.

As Uhuru Flower Farms regular bank and financier, Standard Chartered Bank was approached with the request to provide a loan facility for the solar plant installation. Uhuru's Standard Chartered relationship manager had no previous experience in solar, but nevertheless proceeded to undertake regular transaction due diligence as with any loan request. Their focal concerns included: understanding what the customer needed the loan for, how the loan would benefit business performance, and whether the company had the cash flows to repay the loan and collateral to act as guarantee for the facility. All of these points were satisfactorily met.

Beyond confirming that Azimuth Power Ltd and its UK supplier actually existed, SCB relied on Uhuru Flowers to do detailed due diligence on the capacity of solar systems to provide an adequate, regular energy supply.

Standard Chartered determined that the company was in a position to repay the loan regardless of whether or not the system worked.



Standard Chartered assisted the farm to mitigate risk by providing generous loan terms – 4.5% fixed for 3 months then floating at 0.18% on the Kenyan interest rate but with a cap of 5% – on a €94,500 loan or KSh10m (66%) of the required amount to install the new solar system. The terms conditions were partly practical: with most of Uhuru Flowers' receivables from its European clients in Euros, the bank was confident about the prospects for repayment. At the same time they balanced their exposure to the investment by requiring Uhuru Flowers to raise a sizeable proportion of the required capital.



Outcomes

Standard Chartered reports that the loan has gone well, with the client achieving savings of up to 50% on their prior energy bills, and losing no stock due to power outages. Loan payments have had no financial impact on the client's bottom line, as energy savings have exceeded the amount to be paid on the loan. Other flower companies in the area are copying the model with Standard Chartered and other banks providing the financing.

Despite the new business, Standard Chartered is aware of lost opportunities associated with the lack of incentives for their clients to invest further in the solar systems. For example, Uhuru's solar system has been designed with extra capacity to allow it to generate excess power that could be sold back into the national grid. Unfortunately, the procedural complexity and cost associated with securing a license to serve as an energy provider are disincentives for Uhuru Flower Farms to pursue this, especially as it might divert management time from the core business of flower production. This is a sentiment shared among other flower farms that have implemented solar power systems.

Lessons Learned

1. Financing the acquisition of alternative, green products does not necessarily require much deviation from standard due diligence approaches. Assessing the client's needs and credibility remain the core questions to be answered.
2. In a fast moving economy, banks need to institutionalize new loan products, and proactively cross-sell them wherever opportunities arise if they are to stay ahead of their competitors. New loans in new sectors should therefore be more closely monitored than most, and be seen not just as a risk mitigation strategy but as a business opportunity. Identifying and institutionalizing opportunities for cross-selling remains a challenge.
3. Banks, relationship managers and their colleagues may need to accept that innovation originates more often from a client's desire for cost savings or new business opportunities, than from the bank independently identifying a financing gap in the market. That said, while innovation may indeed be driven by clients seeking a first-mover advantage, banks need to develop systems and incentives that encourage their employees to flag up, package and publicize such opportunities.
4. Mitigating risk in innovative transactions can be achieved in various ways, including limiting exposure to the investment and, where possible, structuring returns based on foreign currency receivables.
5. Banks need to consider ways of developing their policy towards unlocking business opportunities for their clients.

