SCALING A NEW MODEL OF DEVELOPMENT

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EXECUTIVE SUMMARY

Power Africa, a U.S.-led partnership to expand electricity access in the world's poorest continent, represents a new model for development assistance. This model seeks to mitigate the commercial risks associated with development-critical investments through the provision of a range of publically provided tools. Key principles include leveraging private capital, organizing around private sector needs, focusing on individual transactions, and coordinating U.S. and donor efforts.

INTRODUCTION

The United States Agency for International Development (USAID) understands that partnerships are critical to address today's development challenges, particularly in transformational sectors such as power, water and agriculture, where needs and risks are well beyond the capacity of any one actor. USAID recognizes that new models of development maximize the private sector's potential to drive the economic growth necessary to elevate countries from poverty.

The agency's willingness to experiment with innovative approaches to engage the private sector has deepened the impact of its programs over the years. A critical objective has been to develop strategies for aligning our many public and private sector partners' interests to achieve sustainable development through job creation and economic reform. The quest for better tools has been an exploration; we have learned and integrated improvements along the way. To tackle this challenge, the agency has created an array of tools, including the Development Credit Authority (DCA), the Global Development Alliance (GDA), the Private Capital Group for Africa, and now the Global Development Lab. Approaches have evolved from grants to alliances and loan guarantees, and from ad hoc partnerships to complex, multi-party approaches. At the same time, the motivation for USAID's private sector partners to invest in development has shifted from one driven by philanthropy to one driven by sustainable investment as part of their core business.

Pioneering initiatives, such as Power Africa, Feed the Future and the New Alliance for Food Security and Nutrition, all of which call on the private sector to take a leadership role, along with donors and governments in a coordinated, collective effort, promise most success in attracting new investment, while aligning incentives for policy reforms. The model empowers African governments to accelerate the reforms that will make the greatest difference to their economic future.

This policy paper makes the case that this new model of development—using the full spectrum of U.S. development resources and tools to attract investment and align the interests of investors, donors and governments—is the most effective way to achieve sustainable development. The evidence to date suggests it can lead to significant results on the ground.

While this model is gaining traction throughout the agency and is reflected in a number of programs, this paper focuses on the example of Power Africa as a potential model for other sectors and geographic regions.

POWER AFRICA: A NEW MODEL OF DEVELOPMENT FOR AN ENERGY-SECURE AFRICA

In June 2013, President Obama announced Power Africa—a U.S.-led partnership that seeks to double access to electricity in sub-Saharan Africa. Power Africa mobilizes the collective resources offered by 12 U.S. government agencies, the World Bank Group, the African Development Bank, our host government partners, other multilateral organizations, donors, and most importantly, private sector partners to help lead energy transactions across the finish line and to transform the energy sector in our partner countries.

President Obama identified six focus countries—Ethiopia, Ghana, Kenya, Liberia, Nigeria and Tanzania—where Power Africa is aiming to add 10,000 megawatts (MW) of new power generation and 20 million new electrical connections.

The approach has been successful in attracting investment, financing, technology and capacity-building resources of the private sector to a development priority. The U.S. government committed $7 billion to mobilize private sector investment in the energy sector in sub-Saharan Africa. In advance of Power Africa's launch, USAID (designated by the White House as the lead agency for coordinating Power Africa's efforts) mobilized **more than $15 billion in private sector commitments** towards achieving Power Africa's goals, a two-to-one match of U.S. resources committed. More than 35 partners from the U.S. and Africa made commitments, with hundreds of others interested in participating. Many companies are evaluating for the first time opportunities around Africa's power sector.

USAID built upon Feed the Future and the New Alliance model, using its multi-stakeholder model to encourage the private sector to take the lead in development efforts. The Power Africa model relies on the private sector to provide most of the resources, with government providing strategically targeted and coordinated development finance and capacity-building support.

Power Africa took the model one step further, however, in **aligning incentives at the outset between the private sector, donors and governments to encourage collaboration among them to drive the systemic reforms that in turn, attract and facilitate new investment.** Partnerships have been aligned with existing private sector investment and strategies, rather than asking the private sector to reorient its investments around U.S. development goals.

The model's promise reflects a deliberate effort to align incentives. Investors are most likely to be attracted to a project with development impact when the starting point of the strategy is what is of greatest interest to the private sector—accelerating specific transactions. Incentives are greatest for investors to take risk when donors are coordinated and poised to share risk around specific projects, and governments have the strongest incentives to speed reform. Investors are particularly interested if they can leverage cross-cutting interagency support to address the range of obstacles—guarantee and finance needs, capacity support, regulatory approval or negotiating with local utilities and off-takers—directly related to specific transactions. Governments are more likely to undertake necessary policy and regulatory reforms when the payoff is tangible—in the case of Power Africa, electricity for people and businesses. This model attracts immediate (vs. hypothetical) investment, especially when it is combined with donor funding for capacity building and infrastructure support.

A TRANSACTIONAL APPROACH

Power Africa focuses on delivering transformational transactions now. Alignment of interests between governments, donors and investors to bring transactions to closure and spur new investment is still challenging, but is more likely when partnerships are structured to coordinate public sector efforts to support investment.

Power Africa pays particular attention to the obstacles that delay deals or that prevent deals from coming online at all. By focusing on specific policy, regulatory, technical or financing needs to advance specific transactions—for example, ensuring that a tariff is cost-reflective or that the "grid code" can accommodate new wind electricity generation—U.S., African government, and other donor efforts are prioritized to have the greatest impact. Significantly, the model helps empower African governments to make the reforms of greatest interest to the investors they want to attract.

While aid has historically had mixed success in stimulating policy reform, those interested in policy reform within governments are more empowered to push reform when aid is combined with tangible investment, and when required reforms are project-focused rather than across-the-board.

A focus on transactions also has a potential multiplier effect. Eliminating an obstacle to one Power Africa priority transaction will invariably open the door for others.

By basing Power Africa's headquarters on the continent and by placing interagency teams at the U.S. embassy in each of the six Power Africa focus countries, which are supported by on-the-ground transaction advisers, the U.S. government is working hand-in-hand with the private sector to respond in real time to obstacles or "market imperfections" that otherwise slow down progress. This approach also lends an important local perspective and enhances the ownership of local ministries.

Unlike other development approaches that include hiring experts to review and analyze a sector and make recommendations for interventions, Power Africa takes a practical, private sector-led approach. We sit with the private sector—bankers, developers, and manufacturers—and ask them about the obstacles they face and the tools we can pull from the toolboxes of our 12 U.S. government agencies and many partners to address them. Power Africa also has a standing interagency working group that collaborates on a daily basis, with a one-stop shop on the continent and in Washington, which provides the private sector access to all tools available.

Power Africa deploys its resources in a targeted way, zeroing in on what is needed to accelerate a particular transaction. These tools, especially when combined, can serve as "tipping points" for investment that might not otherwise occur. USAID, the Overseas Private Investment Corporation (OPIC) and the U.S. Trade and Development Agency (USTDA) have combined resources for Power Africa in Tanzania and Ethiopia to help advance projects that otherwise might not have happened—at least not at the rapid pace at which they are proceeding.

This approach brings to bear a coherent U.S. government toolbox end-to-end along the entire value chain of a project, from financing to capacity building to appropriate legal structures, by, for example, engaging the Millennium Challenge Corporation (MCC) for policy reform, the U.S. Export-Import Bank (Ex-Im) and OPIC for financing, along with the Department of Commerce for exporting innovative U.S. technology and USAID for technical assistance. Investors and potential investors find this approach particularly appealing because it can lower costs, reduce risks and save time, helping projects emerge quickly from the early phase of power sector project development, which often is the most difficult, risky, and expensive phase.

In its first year, Power Africa already has either helped financially close or has identified more than 8,000 MW of power projects—enough to light more than 10 million homes in six African countries. We are well on our way to achieving 10,000 MW of new generation in five years, and more than halfway to our goal of providing access to 20 million households and commercial entities.

Within one year, Power Africa has:

- Supported the development of the **Corbetti geothermal plant**, the first independent power producer geothermal plant in Ethiopia. The project signals the opening of the Ethiopian energy sector to new generation models and will provide up to 1000 MW of electricity. (See Box 1.)

BOX 1: POWER AFRICA SPURS INVESTMENT IN RIFT VALLEY RENEWABLES

Reykjavik Geothermal, a U.S.-Icelandic private developer, will invest $4 billion over 8 to 10 years to build and operate a power plant located at Corbetti Caldera. The plant will be built in three phases, totaling 1,000 MW by 2018, and is expected to be the largest geothermal facility in Africa. The Power Africa team helped develop the power purchase agreement (PPA) framework, and worked in partnership with the African Development Bank to provide legal assistance to the Ethiopian government to negotiate the PPA. The USAID-sponsored geothermal risk mitigation facility, funded by the German development bank KfW and managed by the African Union, will provide grant funding to defray the costs and risks of exploratory drilling. All three steps helped lower the risk of the transaction for investors, to accelerate the project's movement toward agreement and encourage further development of Ethiopia's geothermal sector.

- Facilitated the construction in Kenya of the single largest wind power project in sub-Saharan Africa, the 310 MW **Lake Turkana project**. The project is projected to boost installed energy capacity by 20 percent, create over 2,000 jobs during construction and sustain 200 full-time jobs once operational. Power Africa provided technical advice that gave Lake Turkana's lenders comfort that the Kenyan electrical grid could absorb the intermittent power associated with wind farms. OPIC is providing up to $250 million in investment guarantees to support the development, construction, commissioning and operation of the plant. In addition, Power Africa coordinated with the African Development Bank (AfDB) to provide necessary financial guarantees.

- Power Africa also supported the extension of **NextGen Solar's power purchasing agreement** with Tanzania from 15 to 25 years. Power Africa helped **Cummins Cogeneration**, an American biomass energy developer, finalize its agreement with Kenya for electricity production. Cummins equipment will run on invasive mesquite wood, the collection of which will provide jobs and income generation for thousands of rural Kenyans. This innovative model is likely to be replicated in nearly a dozen sites throughout Kenya.

- USAID and the U.S. African Development Foundation partnered with **General Electric for an Off-Grid Challenge.** This contest awarded six first-round, $100,000 grants in Kenya and Nigeria to support community level, off-grid projects and is now in a second round involving all six countries.

- Power Africa launched "**Beyond the Grid,"** a sub-initiative focused on off-grid and small-scale energy solutions, adding 27 new Power Africa partners, committing to invest over $1 billion over the next five years. (See Box 2.)

BOX 2: POWER AFRICA CATALYZES INVESTOR INTEREST IN SMALL SCALE SOLUTIONS TO ACHIEVE NEW POLICY FRAMEWORKS AND FINANCIAL TOOLS

"Beyond the Grid," a sub-initiative of Power Africa, is similarly structured to leverage partnerships with committed investors to advance the policy and regulatory frameworks needed to accelerate projects in the small-scale, off-grid energy space. Over a five-year period, Beyond the Grid will serve as a platform to aggregate investment commitments of 25 partners totaling $1 billion to achieve policy changes relevant to committed transactions. It will also incorporate new financial tools, such as investment structures that blend donor and private capital, aggregating and de-risking small energy projects in Africa and making them available as a new asset class for investment at scale. Combining the resources and expertise of investors, practitioners and donors at the same time on specific transactions will drive the systemic reforms necessary to attract new investment to this underserved market.

WORKING WITH OTHER DONORS

Power Africa is teaching us how to make donor coordination, which is never easy, work. Donors have different legal requirements, budget cycles, and mandates. Nevertheless, donors continue to meet to hash out general principles year after year that only sometimes translate to practical on-the-ground collaboration or actual results.

Power Africa has used transactions as a focal point to drive collaboration. Power Africa is taking a "one-at-a-time," "bottom-up" approach—working with in-country teams to build policy agendas around specific projects. At headquarters, Power Africa works with our partners to identify higher-level corporate goals, such as increasing off-grid access, promoting geothermal development, or identifying gas-to-power solutions. And in each country, our interagency teams work closely with other donors, the host government, and the private sector to determine which particular energy projects should be prioritized for donor collaboration.

For example, Power Africa partnered with the AfDB and the African Union Commission (AUC) to hire a full-time coordinator focused exclusively on developing a multi-donor, regional geothermal strategy for East Africa. That coordinator is embedded within the AfDB and provides a service to not just Power Africa, the AUC and the AfDB, but to all donors. In the first few months since this position was created, donors have worked together to identify specific priorities for specific projects, which will expedite the exploitation of the clean, renewable, inexpensive, and abundant geothermal resources the East Africa's Rift Valley enjoys. Power Africa is replicating that model to support Africa's regional "power pools" to identify specific regional power projects that will "force" energy trade, rather than hoping that high-level policy agreement will exclusively create the environment to encourage countries to trade electricity across borders.

CONCLUSION

Innovation is a cornerstone of USAID's approach to development. Through constant experimentation, USAID has developed solutions that are less expensive, better and faster, whether they are anti-retrovirals or off-grid, clean energy solutions.

In the same way, USAID continues to explore new partnership models to harness what the private sector can bring to development—the jobs, skills and new businesses that are the foundation of sustainable growth. The agency's innovations have not only revolutionized the way the agency does development, but have produced significant results on the ground.

USAID's new model of development reflects an emerging set of guiding principles. These include:

- **Leveraging Private Sector Resources.** The importance of achieving sustainable outcomes by using development resources to attract private investment to development priorities.

- **Responding to Private Sector Needs.** An effective way to attract investment, especially in high-risk, transformational sectors, is to organize public sector efforts to support private sector transactions, using development resources and tools to share risk and coordinate efforts.

- **Transactional Approach to Development.** Aligning investor, donor and government interests around specific transactions holds the greatest promise for attracting investment and achieving policy reforms.

- **Coordinating U.S. Government and Donor Efforts.** Aligning and deploying multiple U.S. government and donor assistance and financing tools helps reduce risks and provides incentives for investment in difficult or unfamiliar environments.

The Power Africa model holds tremendous promise to genuinely align incentives among investors, African governments and U.S. government and other donor agencies to achieve results. Every transaction has its unique obstacles and opportunities to discover new solutions.

The challenge for the donor community is to respond to the private sector's demand for flexible tools that mitigate the commercial risks associated with the investments needed to drive development. As the private sector steps up, so will U.S. government capacity to share risk and provide incentives for sustainable investment through the development of new tools and innovative approaches. This path forward will enable USAID to maintain its momentum and leadership at the forefront of donor efforts to engage the private sector.