CLEAN ENERGY FINANCE CORPORATION

Speech by Jillian Broadbent AO, Chair, Clean Energy Finance Corporation to the CEDA Energy Series, Renewable Energy Financing Models

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As an economist and financier, my interest in the Clean Energy Finance Corporation is the role and contribution it can make to the diversity, vibrancy and resilience of the Australian economy.

Despite the differences in the policy approaches of the Government and the Opposition, there is bipartisan agreement that the world is becoming carbon constrained and that Australia requires a Renewable Energy Target and an emissions reduction target to position us for this environment. A shift towards cleaner energy is critical.

This requires continued responsiveness in public policy, and a substantial investment in energy efficiency and the deployment of new generation capacity. Mobility in both our labour and capital resources is vital if we are to prosper through the global drive to reduce carbon emissions.

Australia has shown itself to be very adaptive through several decades of significant changes in the global economy. While economic performance in many countries is patchy and volatile, we have sustained our economic growth and low inflation over a 21 year period without a major downturn.

Our gross domestic product has doubled over that time. Our unemployment rate has fallen from over 10% to around 5%.

These economic outcomes do not just happen- they are a consequence of the responsiveness of public policy, businesses, households and the workforce to the long term structural changes which the global and domestic economies experience.

It is worth considering Australia's economic performance over the last two decades and the changing forces at work, as it is encouraging for our capacity to adjust to a carbon constrained world and to expand and strengthen our clean energy sector to achieve this.

One of the external forces at work is the shift in the source of global growth. The much used label of "the Asian Century" is a recognition that world growth is being driven by Asian developing countries, particularly China and India, rather than the developed world which dominated world growth in the previous century.

Contributing to this shift is the transfer in manufacturing to the lower wage structure of these emerging economies. The jobs created there and the consequent ubanisation it drives is further supporting their economic growth and feeding back into the demand for, and price of, Australia's mining exports.

Consistent with the long term global trend, manufacturing in Australia has become a smaller sector in our economy and the services sector has expanded to provide employment for our growing workforce.

This shift in the share of economic activity to the developing countries (not just in Asia, but more broadly) has accelerated since 2008 (and the GFC), as challenges to the banking system and fiscal imbalances, in Europe, the UK or the US in particular, are slowing the recovery in those economies.

The share of emerging economies in global output has increased from 30% only 20 years ago to around 50% in 2011. In the last two years alone, 75% of global growth has come from the emerging economies. The divergence in economic growth between the developed and developing countries has some parallels for us at a national and an industry level.

The changing global dynamics are feeding into the Australian economy and, in turn, to our individual States. Growth now is favouring the resource rich States. For the first time since Federation, this State is making a net financial contribution to the Federal budget. We are experiencing very different growth paths for the mining related and non-mining related parts of our economy.

For the first 15 years of our 21 years of consistent growth, household demand was prominent in driving growth. The key driver now is mining investment. Importantly we have been able to keep unemployment low through this transition.

We are now building our capacity to meet Asian demand for iron ore, coal and gas. We are undertaking one of the biggest resource investment upswings in our history. The consequent high Australian dollar is a heavy burden for our manufacturing, tourism and education exports.

These changes require significant adjustments.

Despite substantially slower growth in retail sales and housing construction (the non-mining), we have maintained trend growth at a national level. Our continued growth and low unemployment is in sharp contrast to the experience in other developed countries where the transition to lower levels of household leverage and consumption expenditure has been very painful.

The adaptation required in shifting our labour and capital resources, from servicing household demand to mining investment, is not without its pain. It carries losses in jobs and capital.

Parallel challenge for Australia is our transition to a lower emissions economy. Federal and State governments have designed policies to support this transition.

The flexibility and adaptability that has sustained Australia's growth through the global dynamics of the last 20 years needs to be directed into energy production and consumption. Adjustments can be slow and disruptive, as some companies decline and others emerge, but our track record in making them is a good one.

Financing is critical, but traditional finance is slow to move to new areas.

As governments, globally, implemented stimulus packages in response to the negative growth in 2008, many were directed to the clean energy sector. In the US, the package resulted in a doubling of renewable power, unprecedented investment in energy efficiency, advanced bio- fuels and green manufacturing. China, also, was one of the largest investors in renewable energy. With these investments there has been a fall in the component costs of wind and solar.

There are both defensive and opportunistic reasons why the clean energy sector warrants business attention and government support.

It is not just a means of fulfilling our Country's commitment to reducing carbon emissions, but an opportunity to position Australia in an important and growing global industry sector - that of clean energy - energy efficiency and lower emissions. It can support the development of businesses, jobs and export opportunities around this sector, and play a critical role in maintaining a buoyant economy in changing global conditions.

Substantial investment is required in the shift to cleaner energy. The early stage of our clean energy industry, and the market barriers encountered during the industry's development, exacerbate the challenge of mobilising these investment funds.

In October last year, I was asked by the Government to Chair the review to develop an implementation plan for the establishment of the Clean Energy Finance Corporation. A focus of that review was to examine the presence of financial barriers, consider ways of addressing those barriers, and whether the possible externalities justify doing so.

Legislation for the establishment of the CEFC was passed in July this year. A partial Board has been operating since August and we have selected our Chief Executive Officer.

The Clean Energy Finance Corporation is a fund set up to invest its own funds and to catalyse private sector funds into Australia's renewable energy, low emissions and energy efficiency. It is designed as a $10 billion investment fund, off budget. A key principle of its operating framework is to take a commercial approach. *The commercial approach requires investments to be developed beyond the research and development stage, have a positive expected rate of return and have the capacity to repay capital.* This approach is critical to the financial self-sustainability of the CEFC and its intention to operate with minimal budgetary assistance.

Its broad objective is...."apply capital through a commercial filter to facilitate increased flows of finance into the clean energy sector thus preparing and positioning the Australian economy and industry for a cleaner energy future."

With commerciality being the primary filter for investments, in the initial stages of the CEFC, the support of a **co-financier** is expected to be a prerequisite for the CEFC to provide finance. There are two distinct, but related, goals here: to increase the total amount of funding available; and to enhance the expertise and capacity of the financial sector to fund the clean energy sector going forward.

We will be focused particularly on identifying financial barriers in the clean energy financing which the CEFC might be able to impact.

The common financial barriers we identified in the review were availability, tenor and cost of finance. The impact of these barriers is specific to each project and will not apply consistently across the sector.

Ultimately, barriers affect the risk/return assessment of potential financiers and their consequent willingness to invest. The individuality of each project necessitates a case-by-case approach with each project potentially receiving different terms. These terms would be the least generous terms required for the project to go ahead.

As participants in the clean energy sector can attest, the appetite for investment in clean energy has fallen sharply from its pre-2008 levels.

As an economist, I believe in the market being the preferred mechanism for the optimal allocations of capital and resources. In areas of national importance and long lead times on investment, government can play a critical supportive role. Their challenge is to find the right balance between encouraging a sector's development and using the market to support success and allow failure.

The CEFC is intended to support the clean energy market's transition towards greater efficiency. It is a mechanism to mobilise private sector disciplines and skills for a public policy outcome. It has the capacity and flexibility to provide financial support to clean energy projects and technologies.

As a Corporation independent of government with a broad investment mandate, we will be able to adjust quickly to market changes and needs.

While each investment will individually support the sector, it is the cumulative impact of the positive externalities of expanding the sector experience; or lowering first mover barriers and costs; moving down the cost curve and creating third party benefits, which are essential to positioning Australia for a cleaner energy future.

The CEFC Board has been progressing arrangements with other related government programs as the CEFC has the capacity to enhance the impact of these programs.

LCAL

It is the Government’s intention that Low Carbon Australia's programs get incorporated into the CEFC. The two organisations are working on how to make that happen. LCAL have done a great job establishing pilot programs. We are expecting to build on these programs.

ARENA

A critical partnership for the support of renewable energy is between the CEFC and the Australian Renewable Energy Agency (ARENA). As the CEFC seeks to promote technology along the innovation chain, the projects funded by ARENA provide a potential pipeline of projects for us. I am pleased to report that ARENA and CEFC are already in discussions about ensuring a collaborative approach and a clear interface with the market.

The key difference between ARENA and CEFC is that ARENA is primarily a grant-maker while CEFC is a loan-maker or investor. This however does not prevent a project proponent receiving contributions from both organisations.

The electricity industry's future will ultimately be transformed by the widespread adoption of renewable power, electric cars and smart meters. Green energy is expensive, but it is getting cheaper and black energy is getting more expensive. Early action towards the transformation to increased renewable energy, lower emissions and to greater energy efficiency, minimises the ultimate cost of disruption to the economy. No action leaves us very vulnerable.

Australia is an energy exporter. We have been accustomed to a low cost of energy. The recent increase in energy and transmission prices, particularly in the Eastern States, and tougher economic conditions in the non-mining sectors, together with government support has stimulated investment in energy efficiency and lower emissions. Despite our economic growth, electricity consumption has slowed.

The development of Australia's clean energy capacities is essential to our industries readiness for a carbon constrained world.

Our geography, renewable energy resources and our adaptive engineering skills are well suited to Australia playing a significant global role in the clean energy sector.

Australia's strong engineering services skills can certainly add value in the application of cleaner energy technologies and their modification.

As Asia's investment in clean energy grows, so can Australia's prosperity, as we build the technology, design, construction and operating skills to service the sector. These skills can be applied domestically and in the export of services. Finance is critical to this development and the CEFC, a catalyst to mobilising this finance.

FIRST TASK OF BOARD AND CEO

- Determine initial area of focus for Investment
- Communicate to market what they are
- Establish processes for attracting, managing and assessing investment proposals