CLEAN ENERGY FINANCE CORPORATION

Keynote speech by Anna Skarbek, Board Member, Clean Energy Finance Corporation to Carbon Expo 2012

Melbourne Convention and Exhibition Centre
Thursday 8 November 2012

Since the release of the CEFC review in April this year the government has supported the recommendations in that review. Legislation has been drafted and passed in both houses of parliament for the establishment of the corporation.

The Clean Energy Finance Corporation Act was proclaimed on the 3rd of August, this year.

The financing arrangements are part of that legislation such that $2 billion is appropriated to a special account every year for five years commencing from the 1st of July, 2013.

It was set up in this way, which is somewhat unusual with appropriations through legislation rather than through the budget process each year.

It was set up deliberately in this way because the CEFC needs to enter into long-term contracts and its operability and credibility depends on the private sector's acceptance that the corporation will have funds.

So we have the funds.

Those first funds will flow- are available to us - from 1st of July next year.

The CEFC board and the support team that currently is in the secretariat team in the Treasury in Canberra, are working to progress the establishment and set up of the corporation.

Our aim is to be ready to invest when the funds become available from July next year.

We're now in the final stages of the process of selecting a CEO. We were very pleased at the strong field of experienced, interested candidates from within Australia and overseas and we hope to be making an announcement of the successful candidate very very soon.

The CEFC 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 sustainability of the CEFC and its intention to operate with minimal budgetary assistance.

Its objective is to 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.

So with commerciality being the primary filter for our investments, it's expected that in the initial stages of the CEFC, the support of a co-financier will be a prerequisite for the CEFC to provide any finance to projects.

There are two distinct but related goals here:

1. to increase the total amount of funding available
2. to enhance the expertise and capacity of the financial sector to fund the clean energy sector

So in determining the blueprint for the CEFC, the review panel focused particularly on identifying financial barriers in the financing of clean energy projects and technologies that the CEFC might be able to impact.

As many of you here will be aware, the private sector appetite for investment in clean energy has fallen sharply from its pre-2008 levels.

The shortening maturity of bank liabilities and in turn their assets, the retreat of the European bank subsidiaries, who in many cases were the most active in clean energy financing, the absence of a bipartisan approach, and the continuing regulatory uncertainty in Australia have each had a negative impact on the availability, tenor and price of clean energy financing.

So within the CEFC's commercial approach, its mandate allows us to address those financial barriers of **availability**, **tenor** and **cost**.

Let me say a bit about each of those.

On availability, through the co-financing principles, the CEFC can leverage its $10 billion by catalysing private sector capital into the sector. Also the CEFC may channel a portion of its funds through intermediaries that aggregate smaller transactions.

On tenor, the CEFC is provided with specially appropriated funds so it will not have the constraint of requiring matched liabilities. The CEFC can consequently provide longer term debt maturities than private sector lenders.

And to cost, the CEFC will have the ability to provide concessional finance. This concessionality can take the form of lower pricing, higher risk, or longer-term finance.

In offering concessional finance, the CEFC will still assess proposals on a case-by-case basis through its commercial filter. The corporation will seek to provide funds on the least generous terms possible for a project to proceed.

Financial instruments

The CEFC will have capacity to influence the risk landscape by covering investments across the stages of commercialisation. The CEFC will have scope to utilise a full range of financial instruments. In the early stages of the investing phase however, it is anticipated that the majority of the CEFC investments will be loans and not equity.

We know that Australia’s clean energy market is at an early stage, characterised by incomplete knowledge and limited experience of risk. The combination of this with other market barriers is inhibiting the efficient allocation of capital. The CEFC would support the clean energy market’s transition towards greater efficiency.

Investment approach

The CEFC 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, it can adjust quickly to market changes and needs. The streams of investment being renewable energy, low emissions, and energy efficiency, allow considerable scope and its investment mandate will enable a range of investment structures.

The early task of the board and the CEO will be to determine initial areas of focus within those three streams, to communicate with the market what they are, and establish processes for attracting and managing investment proposals.

We envisage that the CEFC will have an open process for investment proposals – that is, a continuous one, not fixed rounds with closing dates etc. We are also progressing arrangements with other related government programs in so far as harmonisation or interaction with those programs supports the CEFC objectives. And the CEFC has the capacity to enhance the impact of these programs.

ARENA

ARENA is obviously a critical partnership for the support of renewable energy with the CEFC. As the CEFC seeks to promote technology along the innovation chain, the projects funded by ARENA provide a potential pipeline of projects for the CEFC.

I’m pleased to report that the CEFC and ARENA are already in discussions about ensuring a collaborative approach and a clear interface with the market. The key difference between ARENA and the CEFC to put it bluntly is the CEFC needs to be paid its money back, and ARENA doesn’t.

ARENA is primarily a grant maker looking for a non-financial return, while the CEFC is a loan maker, or investor. This however, doesn’t prevent a project proponent receiving contributions from both organisations.

A particular project, for example, most likely in the late stage of the development spectrum, could use a grant from ARENA to assist its commerciality, to be in a position to obtain external finance and concessional finance from CEFC.

The project proponent would still need to have a private sector coinvestor to satisfy the CEFC’s requirements for co-financiers.

LOW CARBON AUSTRALIA

Low Carbon Australia is another organisation with which the CEFC is already in discussions. It is the government's intention that Low Carbon Australia's programs get incorporated into the CEFC.

We are already talking closely about how to make that happen.

Low Carbon Australia has done a great job establishing pilot programs that the CEFC is expecting to build on. The Low Carbon Australia team is already on track to fully commit its $84.6 million dollar fund by the end of this financial year.

CLEAN TECHNOLOGY INVESTMENT PROGRAM

There are a number of other programs within the clean energy sector with which the CEFC could collaborate or complement.

For example, the Clean Technology Investment Program provides grants to companies that are large energy users to invest in energy efficiency and emissions reductions by switching to lower emissions energy sources or installing new manufacturing equipment, processes or facilities.

Project proponents must provide matching finance to be eligible for grants, so it's possible that some of those projects may indeed seek to use the CEFC as part of that matching finance alongside other external finance.

ENERGY EFFICIENCY OPPORTUNITIES PROGRAM

The Energy Efficiency Opportunities program (EEO) requires large energy users to identify and report energy efficiency projects that have a payback of four years or less.

The program, however, does not provide financing, and not all projects are implemented as companies often face a range of barriers. So the identification of these projects facilitates the capacity of the CEFC to progress investments in energy efficiency. We're excited at the range of potential projects that the CEFC could finance while staying within its mandate.

The key tenets of that mandate again are, being commercial and catalysing and complementing private sector finance rather than distorting or displacing it.
The work we've done already in looking at those programs I've mentioned and others suggests to us that there's quite an interesting potential pipeline of projects out there that the CEFC could work with.

CONCLUSION

So to finish I just wanted to share some remarks about the economic context. Our Chair, Jillian Broadbent, as is well known, has a strong background in banking, economics and public policy, and she has been clear that she sees the clean energy sector not only as an environmental requirement, but as an economic opportunity.

She has often made this point, that the economy has experienced 21 years of growth and low inflation without a major downturn.

Our Gross Domestic Product has doubled over that time. Our unemployment rate has fallen from over 10 per cent to around five per cent. This economic performance has required considerable adaptability. It has been achieved over a period of significant change in the global economy and the drivers of Australian growth and the accompanying employment opportunities have adjusted very effectively.

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.

There is of course the much used label of the Asian century, in recognition that world growth is being driven by Asian developing countries and in particular China and India rather than the developed world which dominated world growth in the previous century. The shift in the share of economic activity to developing countries is not just in Asia, but more broadly has accelerated since 2008 and since the GFC as challenges to the banking system and fiscal imbalances in the UK or Europe 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% last year. In the last 2 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 the national level. The changing global dynamics are feeding into the Australian economy and in turn to our individual states. Growth is now favouring the resource rich states. For the first time since federation Western Australia is making a net financial contribution to the federal budget.

We're 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 are maintaining low unemployment through this transition. In the decade to 2005 Australian household consumption grew faster than household income. The household savings ratio fell to zero and even negative.

Buoyed by rising house and equity prices borrowings increased and debt to income rose from 70% to 150%. Over that period retail sales and housing construction were the major contributors to Australia's economic and employment growth.

Since 2008 household consumption has been growing more slowly than income. The savings ratio is now back above producing export for the 10%. Mining activity producing exports for the Asian market has picked up to support Australia's trend growth rate. Despite significantly slower growth in retail sales and housing construction we've maintained trend growth at the national level.

Our continued growth and low unemployment is in sharp contrast to the experience in other developed countries as is well known, where the transition to lower levels of household leverage and consumption expenditure has been very painful.

The adaptation required in shifting resources from servicing household demand to mining investment is not without its pain. It requires improvements in our business practices, a flexible mobile workforce and continual investment to remain competitive.

Against this background of an expanding growth contribution from developing countries internationally and from the mining sector domestically, there is a global drive to reduce carbon emissions. There is a recognition and even bipartisan agreement on this in Australia that we are moving to a carbon constrained world and Australia is challenged in transitioning to a lower emissions economy.

Our business practices and our energy sector need to change in this. Current public policies have been designed to support this transition.

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.

China in recent years has been one of the largest investors in renewable energy with $30 billion support from the China Development Bank – 6 of the top 10 solar pv manufacturers are now in China. Some believe that when China's income per head reaches $10 000 (doubling its current levels) they will impose carbon constrains on their import supplies. 25% of Australia's exports are to China.
So there are both defensive and opportunistic reasons why the clean energy sector warrants government support.

The CEFC can be an effective part of this government support.

It is import for Australia to maintain a low cost of electricity as we move to a carbon constrained world. It's 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.

We can develop businesses, jobs and export opportunities around this sector. Such development can play a critical role in maintaining a buoyant economy in changing global conditions.

We need supportive public policies and adaptive business practices to achieve this. Renewable energy targets, a price on carbon and flexibility in the pricing and demand management of energy can each play a part and the CEFC can also make a valuable contribution to this.

So to conclude i just wanted to reiterate that the CEFC Board has been working very hard to progress the establishment phase of the CEFC and we're looking forward to soon being ready for the CEFC to commence its important role of facilitating increased flows of finance into the clean energy sector in Australia.

It's a very exciting and positive opportunity that we each see and it's a committed and energetic Board that are applying ourselves to the task.

We're very very focussed on our aim of being ready to invest from next July. Some people have been telling us that that's too ambitious, others feel that its too slow, or taking too long. We know that it's hard to go from scratch to up and running in that amount of time but that's why we're working very hard and have been for months behind the scenes.

That’s all that I wanted to share with you today about our start up and we hope to be able to make some more announcements very soon about our 1st staff member, the CEO, and the later staffing up.

In the meantime if you need to contact us you can do so via the email address which is cefc@treasury.gov.au

Thank you.