Africa GreenCo – An Overview

Synopsis

Africa GreenCo ("AGC") proposes to interpose a single creditworthy counterparty between buyers and sellers on multiple independent power projects ("IPPs") in sub-Saharan Africa ("SSA"). An intermediary aggregator between buyers and sellers can help attract sustainable investments in the power sector on the strength of a multi-buyer model.

Compared to current market practice, AGC’s intervention will:

1. reduce risk and project development costs for all stakeholders;
2. address inefficiencies caused by the current ‘single buyer single seller’ model;
3. reduce fiscal burden for host Governments; and
4. catalyse private sector debt and equity investment.

AGC responds to Sustainable Development Goal 7 which aims to close the energy access gap and “ensure access to affordable, reliable, sustainable and modern energy for all” through a combination of national action and international cooperation. AGC can act as an implementation tool for key regional initiatives, such as the African Development Bank’s New Deal on Energy for Africa and the Africa Renewable Energy Initiative.

Market Context

Bilateral IPPs

With the exception of a handful of cross-border projects, IPPs within SSA are currently structured on a bilateral basis; i.e., with a single buyer and seller.

Rehabilitation of utilities

African utilities are often poorly funded – running an operating loss due to non-cost reflective tariffs, high overheads and substantial investment needs. In most cases they are entirely state owned and dependent on budget transfers – all of which combine to mean a low credit profile.

Critical steps to rehabilitate utilities are underway but sustainable and material improvements can only occur in the medium to long term.

Lengthy and expensive transaction execution

With notable exceptions such as South African REIPPPP, GET FiT Uganda and Scaling Solar Zambia, IPPs are largely negotiated on an ad hoc project-by-project basis. Negotiations of project documents on individual IPPs are usually very lengthy and often last several years at least. Significant fully ‘at risk’ development costs incurred during those negotiations add materially to total project costs and require a high return to reflect the associated risk profile.

Limited availability, sustainability and effectiveness of third party risk mitigation instruments

Risk mitigants such as liquidity support instruments, early termination buyout regimes and partial risk guarantees are complicated and expensive to negotiate on a project-by-project basis. Even still, they do not fully mitigate the perceived risk of investing in immovable assets in order to sell a commodity (electricity) on a long term basis to a single, often un-creditworthy, buyer. They are also heavily dependent on concessional capital and DFI support.

Host Government fiscal burden

Host Governments are expected to take on contingent liabilities in the form of ‘put and call option’ arrangements on early termination, or more explicit sovereign guarantees. Given the current fiscal position and the medium term macro-economic environment facing most host Governments, this is unsustainable.

Strategy

AGC addresses head on the core issues of (a) offtaker creditworthiness, and (b) the inefficiencies of exclusive bilateral sale and purchase between a single generation company and a single offtaker.

1 The AGC concept was included in the recommendations section of the SE4All Finance Committee Report which was presented to Africa’s Heads of State in Addis Ababa on 13th July 2015 at the Financing for Development Conference.
AGC will play two complementary and synergistic roles in the African power markets:

**Intermediary Creditworthy Offtaker / Aggregator**

AND

**Power Pool Participant / Trader**

The first conceptual step is to interpose AGC between the buyer and the seller under an existing bilateral IPP structure; then repeat this on multiple IPPs so that:

1. AGC is the buyer for multiple generation companies, and
2. AGC is the seller for multiple offtakers.

From this position, AGC will be able to:

1. catalyse third party private capital flows to IPPs by improving the risk profile of projects in the region;
2. lower the electricity tariff required by IPPs for a project to be financially viable by reducing debt costs and investor return requirements to reflect a lower risk profile;
3. provide a route to market for any excess contracted power, thereby mitigating an offtaker’s obligation to pay capacity or ‘deemed energy’ charges for power they do not require; and
4. divert power from a defaulting IPP offtaker to other willing buyers, thereby reducing the likelihood of early termination of an IPP’s power purchase agreement and the resulting crystallisation of host Government contingent liabilities.

More broadly, AGC will:

1. be fundamentally better equipped than a single generation company to mitigate the effect of an un-creditworthy and/or defaulting offtaker;
2. also act as a power trader, thereby increasing liquidity and scale of regional power trade;
3. assist in the development of power pools;
4. support and promote regional standardisation of IPP project documentation; and
5. assist in the development of fair and standardised electricity markets in the countries in which AGC operates.

AGC will act as intermediary offtaker only and would not manage the physical transmission and distribution of energy. It will not own any of the grid infrastructure or seek to replace existing utilities. Rather than replacing existing structures, it complements them, and can further act as a bridge to a future energy regional market liberalization and energy trade integration.

AGC aims to learn from, and where possible replicate, the dynamics of more advanced power markets, in particular building on the experience of the Power Trading Corporation of India (PTC India). PTC India was also set up in order to act as a credit risk mitigating intermediary offtaker for privately-financed regional power generators. In the process, it catalysed the entire Indian regional power sector trading market.

**AGC design principles**

The AGC concept has been developed to fulfil the following key design principles:

- Legally and financially creditworthy
- African-owned and African-led
- Financially sustainable
- Scalable
- Facilitating cross-border trade and investment
- Complementing and collaborating with existing initiatives
- Benefiting IPP investors, utilities and sovereigns
- Catalysing private sector capital
- Incorporating blended capital from concessional and commercial sources

**AGC as an intermediary offtaker and aggregator**

The following is a simple single utility offtaker example:

AGC will purchase capacity and energy from the IPP under a power purchase agreement ("PPA"), and sell that capacity and energy to the utility under a power supply agreement ("PSA"). The PPA and PSA will be on largely back-to-back terms; *save that*. 
AGC will take credit risk on the offtakers, such that upon offtaker default under the PSA, AGC will have the contractual, regulatory and operational ability to keep the PPA ‘alive’ by securing alternative buyers whether on a bilateral basis or through short term trading, and will use all reasonable efforts to do so;

AGC will earn a small margin between the tariff paid under the PPA and the tariff received under the PSA.

The following is an example of a more complex multi-buyer project, which may be suitable for larger IPPs and/or cross-border projects.

In the above scenario, the intervention of AGC will allow:

- individual offtakers to commit to purchase only a portion of the IPP’s total capacity; and
- AGC to better manage the complex risks arising under, and documentation required for, multi-offtaker structures.

This structure will be repeated on multiple projects, building a portfolio of IPPs on one side and a portfolio of offtakers on the other. The portfolio effect will diversify AGC’s risk and enable it to source alternative power or offtakers (as the case may be) in case of default under either a PPA or a PSA.

AGC as a Power Trader

In addition to its role as an offtaker, Africa GreenCo will also participate in the competitive power markets, promoting cross border power transactions and a more dynamic and liquid short term power market.

Impact of AGC on Project Companies

AGC provides the project company with a counterparty which (a) is creditworthy, (b) can mitigate risk via diverting power to third party customers, and (c) can diversify risk over multiple projects.

The intervention of AGC is expected to:

- reduce both total project costs and the cost of capital by:
  - reducing the cost of getting projects to financial close;
  - improving projects’ credit risk profile and in turn:
    - reducing equity investors’ hurdle IRRs;
    - reducing the interest rates and other covenants such as debt service cover ratios on project debt; and
    - increasing the tenors of project debt;
- make investing in, and lending to, African IPPs (whether at the outset or upon a refinancing) attractive to a wider pool of capital than is currently engaged in the market, in particular to private sources of capital, thereby increasing the available pool of capital; and
- allow for more efficient and effective credit enhancement, by building a portfolio of contract exposures which can be de-risked and/or re-insured on a pooled basis.
Impact of AGC on Offtakers and Host Governments

AGC will:

- reduce the financial expense and utilisation of human resources incurred by the host Governments and offtakers in negotiating and executing IPP transactions;
- increase the installed capacity in the power system, facilitating more reliable power supply to end users;
- reduce PPA tariffs (on new IPPs) due to lower IPP development costs and cost of capital;
- lower the average cost of delivered power by utilizing otherwise idle generation capacity for generation and sales to third parties, and offsetting the revenue received from third party customers (less a small margin) against deemed energy charges otherwise payable by the Offtaker;
- help substitute short term emergency power with cross border traded power;
- reduce the fiscal burden on host Governments by reducing the probability of early termination buyout obligations or more explicit host Government guarantees being crystallised, and in certain eventualities reducing the quantum of such obligations;
- reduce risk-weighted capital adequacy requirements in relation to loans to the power sector creating additional debt capacity which can be used to fund sectoral improvements;
- create fiscal space and release Offtaker resources to focus on institutional capacity building, operational efficiency improvements and expansion and upgrades to transmission infrastructure; and
- facilitate the move towards local currency denominated PPAs.

Regional Impact of AGC

AGC will:

- actively trade power in the competitive markets established within the existing power pools (SAPP, WAPP, EAPP etc), increasing liquidity and efficiency;
- be able to disaggregate the contractual supply of electricity from the physical flow of electrons;
- work with power pools, member states and utilities to match power surpluses and deficits, and to maximize the efficient use of natural resources on a regional basis;
- support efforts to integrate planning, power sector regulation and infrastructure investment across member states; and
- help to build the financial and economic case for more investment in regional transmission, interconnection and grid management by increasing traded volumes.

Benefits for projects and investors

Taken together the potential impact of AGC in power markets is substantial. Each dollar invested under a 33% equity scenario generates $5–$6 additional financial benefit that is directly quantifiable. The operating model helps to unlock enough capacity to connect almost one million households to the grid and avoids 7m tonnes of carbon equivalent, while generating over 20,000 new skilled jobs. The table below provides a more detailed breakdown of these impacts with the total value split out over each different investor class. In terms of private sector capital, the model forecasts that AGC will be able to unlock an additional USD 1.31bn of investment in IPPs, which is a conservative estimate as it is based on no private capital incentivised through AGC’s trading activities.
Environmental, Employment, Social and Economic Impact

AGC will:

- avoid 9.3m tCO2e emissions in 10 years and more than 70m tCO2e emissions over the life of the PPAs;
- help create over 22,000 temporary jobs in manufacturing, construction and installation over the first ten years of operations and over 1,000 long term O&M jobs by year 10;
- create additional employment as a consequence of access to more reliable power and savings relative to emergency power costs with a particular impact on small and medium size enterprises, such as women’s cooperatives;
- improve access to basic services such as healthcare and education through improved electricity access;
- stimulate socio-economic development, including reducing infant and maternal mortality rates, improving literacy and facilitating community-based activities and training; and
- help avoid the economic impact of outages that can be as high as 4% of GDP and result in an average annual "drag" on economic growth of 2%.

Operating Strategy

AGC’s operating strategy creates four potential revenue sources for AGC:

- Sale of power purchased under long term agreements;
- Sale of power on short term trades;
- Income from invested capital; and
- Sale of carbon credits.

AGC’s two core operating activities – acting as a PPA offtaker and short term trading - will generate revenues through a margin applied to each unit of power bought and sold. This margin may vary based on the specifics of the actual projects AGC supports. For its role as a PPA offtaker selling power on to utilities/other offtakers through a PSA, AGC aims to select a margin level that generates a net reduction in the price of power paid by a utility/offtaker.

For short term trading, the AGC base model takes a conservative assumption of 10% p.a. growth of the SAPP Day-Ahead /Intra-Day markets and applies an estimated market share for AGC of 5% in year 1, growing to 20% from year 4.

AGC Funding Requirements

AGC has prepared a detailed Feasibility Study (available separately upon request). In assessing how AGC might be financed to implement the proposed operating model, the Feasibility Study considers how much capital AGC will require in order to:

- fund operating costs before AGC becomes cash-flow positive;
- have sufficient liquidity to enter into and deliver on trading and purchase/sale contracts; and
- be perceived as a creditworthy offtaker.

The analysis includes a Monte Carlo simulation of the probability of defaults arising within AGC’s portfolio and suggests that:

- AGC’s equity base should equal 33% of its maximum exposure (being predominately the termination payments which could arise under its PPAs) to be sufficiently creditworthy (investment grade);
- the remaining exposure could be uncovered or covered through guarantees and/or insurance. AGC is working with potential guarantee and insurance providers such as ATI, MIGA and commercial insurers to explore means of leveraging AGC’s equity; and
- the capital structure will draw down additional funds as needed to backstop new exposures created by growth and/or recycle retained earnings to build a robust balance sheet.

The recommended equity structure is a tranched model, with distinct share classes for different investor classes. The main reasons for this are to:

- Promote African ownership and political alignment with AGC’s strategy;
- Return capital to investors in different ways;
- Accommodate donor investors; and
- Allow investors to contribute capital using different instruments.

The size and terms of each tranche will ultimately be determined by investor feedback on appetite and capacity to deploy capital. The capital structure will likely evolve over time as the AGC strategy is proven and adapted to the realities of doing business on the ground.
Assuming that AGC (a) has equity to the value of 33% of its exposure with 50% of such equity comprising non-interest/dividend-bearing returnable capital, and (b) charges a USDc 0.3 / kWh margin on power sales, the model shows concessional returns of 2.8% on the remaining equity and protection of capital; however, the return profile and long term financial sustainability of AGC may be enhanced either by increasing the margin (noting the material tariff reduction expected to be caused by AGC), or for certain classes of investors via tranching.

The process for setting margins should be transparent and operate in collaboration with the key regulators and utilities, but one reasonable input may be selecting a target that is able to attract sufficient capital into AGC (and future trader/intermediary market entrants). AGC is more likely to attract sufficient capital (from a wider universe of investors) if the Class B shareholder IRR is e.g. 6% versus 2.8%. Using illustrative numbers and assuming a 33% equity base, investors can increase IRRs to 6% by increasing the PPA margin to USDc 0.7/kWh or higher. That would be comparable to other impact investment and development finance vehicles. To achieve returns of 10% or more, AGC would need to charge PPA margins of USDc 1.2-1.5 kWh. The margin AGC is able to charge will also be a factor of the reduction in PPA tariffs which AGC can achieve.

Conclusion and Next Steps

Based on the analysis contained in our Feasibility Study, AGC represents a financially viable means of helping more projects achieve bankability and bringing larger volumes and new sources of capital to African power markets. AGC can also help streamline African utilities’ engagement with IPPs, reduce the time and effort required to bring transactions to close, relieve the burden of providing sovereign guarantees and, in the process, help to create the space necessary to implement measures to achieve long term creditworthiness of African utilities and improve domestic power markets. However, many concrete details in terms of the legal structure, governance, operating model, capitalization and financial performance require ongoing feedback from potential investors and promoters of the concept. AGC has garnered significant momentum and interest in the African and international development community. That momentum may require quick action to pilot the AGC concept and it is anticipated that AGC’s business will need to be trialled in a small number of countries initially in order to prove the model before being rolled out across the region and continent.

Political will and endorsement by African institutions such as the AfDB, AU and relevant regional entities (e.g. SADC, SAPP and RERA in the Southern African context) should significantly accelerate this process.

Beyond the strategic activity required to manage and grow this political support, AGC also plans to refine its business case, transitioning from the Feasibility Study’s assessment of whether or not the concept has merit to more detailed and structured approach on how the concept will be implemented. The key components of this will include:

- supplementing AGC’s team to include additional expertise to take the concept to market;
- creating the legal structures required to execute the operating model in AGC’s target geographies;
- planning for and engaging in detailed discussions with potential investors and other stakeholders to further refine the business case and identify specific opportunities for investment;
- developing detailed project development pipelines and execution plans to rapidly progress opportunities identified;
- refining the legal and financial structures to ensure alignment with international best practices and investor preferences;
- refining the operating model to ensure scalability and sustainability;
- developing a robust performance monitoring and reporting framework to track progress against key performance indicators and ensure alignment with the concept’s goals.
finalising AGC’s operating policies and procedures, governance structures and transaction documentation;
identifying suitable projects for proof of concept;
pursuing SAPP membership;
preparing a business case and additional investor outreach materials; and
refining the concept with a small number of potential anchor investors and other stakeholders.
The Africa GreenCo concept and our Feasibility Study are presented to the market solely due the support and funding received from The Rockefeller Foundation’s Innovative Finance team. The Africa GreenCo team is extremely grateful to The Rockefeller Foundation for their trust, belief and for allowing us to present this ambitious concept to the market. A very special thank you to Saadia Madjesiher, Mamadou Biteye and Adam Connaker for guiding us every step of the way and for supporting us in our grant application.

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The Association of Power Utilities of African (APUA) supports Africa GreenCo as a means of securing greater generation capacity at lower cost and supporting African utilities in their transition to creditworthiness. With special thanks to Abel Tella, CEO of APUA.

Convergence supports Africa GreenCo as an efficient way to blend public and private sector finance in support of the development of Africa’s power sector. With special thanks to Joan Larrea, Chris Clubb, Dean Segell and Trang Tran.

Africa GreenCo was honoured to be invited to present the concept at a side event co-hosted with the AfDB and The Rockefeller Foundation at COP22 in Marrakech in November 2016, the output of which was further validation of Africa GreenCo’s ability to help create a liquid power market. Our special thanks go to Said Mouline (COP22 Head of Public Private Partnerships) and Iskander Erzini Vernoit (Project Manager, COP 22 Public Private Partnerships).

NEPAD supports Africa GreenCo as a catalyst for regional integration and a facilitator of cross-border power trade and energy policy harmonisation. Our special thanks go to Ibrahim Mayakai, Mosad Elmsiny and Symerre Grey-Johnson.

Africa GreenCo is extremely grateful for the invaluable support and feedback received from the individuals listed below in their personal capacities.

Abel Tella
CEO, Association of Power Utilities of Africa

Abyd Karmali
Managing Director, Climate Finance at Bank of America Merrill Lynch

Alan Apter
Chief Financial Officer, Eaglestone Advisory

Alex Ruggarma
Director of Regional Integration, AfDB

Alexis Faury
Financial Advisory, Resources and Energy Infrastructure, EC Energy Pte Ltd

Ana Corvalán
Managing Director, Eaglestone Advisory

Andrew Gray
Senior Legal Consultant, Trinity International LLP

Andrew Reicher
Chairman of Berkley Energy Africa

Andy Herscowitz
Coordinator, Power Africa

Anne Baldock
Former Global Head Energy & Infrastructure Allen & Overy

Arnaud Donnel
Lead Financial Sector Specialist, World Bank

Arthur Smith
President, US National Council for Public-Private Partnerships Chair

Batchi Baldeh
Senior Vice President, Africa Finance Corporation

Birr Adams
Senior Director, Global Infrastructure Hub

Brian Countt
Chairman, Infracro Africa

Caitlin MacLean
Director, Innovative Finance, Milken Institute

Callixte Kambanda
Chief Infrastructure Specialist, Secretariat of Infrastructure Consortium for AfDB

Carlos Salle Alonso
Director of Energy Policies, Iberdrola Group

Changala Nowana
Director of Strategy and Corporate Services, ZESCO

Cheikh Bedda
Director Infrastructure & Energy, African Union Commission

Chris Antonopoulos
Chief Executive Officer, Lekela Advisors Ltd

Chris Knowles
Head of Climate Change & Environment Division, EIB

Conal Duffy
Vice President, Emerging Markets, Allian

Crispin Holliday
Commercial Director, Aldwych International

David Baxter
International Development and PPP Specialist and Facilitator

David L. Massie
Chairman & Chief Executive Officer of IAF Capital

David Munene
Former KPLC Director

David Nelson
Executive Director, Energy Finance, Climate Policy Initiative

Eliaj C. Sichone
Executive Secretary, Regional Electricity Regulators Association of Southern Africa.

Eivind Fjeldstad
Managing Director, Norwegian African Business Association

Faruk Yusuf Yabo
Assistant Director, Department of Renewable Energy and Rural Power Access, Nigerian Federal Ministry of Power, Works and Housing

Felice Zaccheo
Head of Unit, Sustainable Energy and Climate Change, DG DEVCO, European Commission

Franklin Amos
Partner, Ansteina Global Advisors / Baylis Emerging Market

George Kotosovos
Director, Mining, Energy & Infrastructure Finance, Standard Bank

George Otieno
CEO at African Trade Insurance Agency

Georgios Pantoulis
Head of Sector – Energy, DG DEVCO, European Commission

Gurdeep Singh
Chairman and Managing Director, NPTC Ltd

Harald Hirschhofer
Director of Energy Policies, Iberdrola Group

Changala Nowana
Director of Strategy and Corporate Services, ZESCO

Helena McLeod
Head of KPMG (IDAS)

Ian Allison
Global Head Climate Resilience, Mott MacDonald

Isabel Rial
Senior Economist, Expenditure Policy Division, Fiscal Affairs Department, IMF

James Bond
Senior Advisor to the Executive Director of the Green Climate Fund and former CEO of MIGA

Jan Martin Witte
Director, KFW Entwicklungsbank

Jean Madzongwe
Transaction Advisor, SAPP Project Advisory Unit

Joao Duarte Cunha
Chief Climate Finance Officer, AfDB

Jocelyn Wessling
Independent Consultant

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Africa GreenCo

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Brief biographies of the team are set out on the following page.

Africa GreenCo in its current form is a UK not-for-profit company limited by guarantee which has been established with the sole purpose of developing the AGC concept to its pre-implementation stage. This UK entity is entirely separate to the operational AGC entity discussed in the Feasibility Study, which will be an African based entity, incorporated subject to political and international community buy in.

**Consultants**

**Financial:** Lions Head Global Partners

Lions Head is a specialized financial advisory firm based in London and Nairobi, experienced in designing, structuring innovative finance platforms, especially for power (Africa50, AREF, GIIF, TCIFF)

With special thanks to: Harry Guinnness

**Legal:** Shearman & Sterling LLP

Sherman and Sterling is a leading international project finance, corporate and commercial law firms, active in Africa for over 50 years.

With special thanks to: Monica Lamb

**Technical:** PPA Energy

PPA’s Energy’s staff are former leaders within SADC utilities and have been involved with the SAPP establishment and operations (governance, regulations, technical constraints, commercial issues, trading etc)

With special thanks to: Lovemore Chillimanzi

**Regulatory & Governance:** GP3 Institute

GP3 Institute is a global advisory network of governance, development, legal and program operation advisors. The institute provides research and advisory support for public-private initiatives comprised of States, subnational units, multilateral development and finance institutions and private sector participants including for profit and non-profit organizations.

With special thanks to: Tim Nielander and Ben Kikko

**Procurement:** Rene Meyer (Senior Procurement and Renewable Energy Policy Expert)

**Risk Management:** Strategia Worldwide

Strategia Worldwide use proven strategic planning methodology to protect companies from risk in complex, volatile, uncertain environments and apply a comprehensive approach to corporate risk management, drawing on their experience of implementing strategy in dangerous and difficult environments and the political, developmental, security and commercial expertise of their highly experienced senior team.

With special thanks to: Iain Pickard
In March 2015, Ana was appointed by the UNECE as the Team Leader for the Southern African Power Pool who was a key member in formulation, implementation, monitoring and revising the Southern African Power Pool rules that enabled launching of a competitive electricity market in the Southern African Region.

Ana trained with Allen & Overy LLP and went on to work for Fulbright & Jaworski LLP and Trinity International LLP, advising on a diverse range of projects within the energy sector, predominately in Sub-Saharan Africa. In March 2015, Ana was appointed by the UNECE as the Team Leader responsible for a Project Team (comprising about 30 specialists) in charge of developing international renewable energy PPP standards as part of the Sustainable Energy for All agenda.

Cathy has more than 14 years professional experience in the infrastructure and renewable energy sectors, both as an adviser and an equity investor. She trained at Allen & Overy LLP where she worked on a diverse range of project finance transactions spanning energy and infrastructure. Before moving into a commercial role at the Infrastructure Fund (which became InfraRed Capital Partners), after 6 years of structuring and negotiating equity investments in a wide variety of public-private partnerships and renewable energy projects, she established her own consultancy to help developers, investors and project companies deliver well-structured and efficiently run investments by assisting them through all stages of project development, implementation and operation and also acted as a consultant to the World Bank. Cathy Oxby

Commercial Director

Lovemore's core skills are in power system strategic management, operations and electricity trading having worked in this area for over 30 years. He has operated hydro and thermal power stations and transmission networks and has negotiated, implemented and managed numerous power purchase agreements. He is a founder member of the Southern African Power Pool who was a key member in formulation, implementation, monitoring and revising the Southern African Power Pool (SAPP) control performance criteria and the SAPP regional trading rules that enabled launching of a competitive electricity market in the Southern African Region. Lovemore holds a Diploma in Electrical Engineering from the Northern Technical College in Zambia, a post graduate Diploma in management studies and an MBA degree from the Buckingham Chilterns University College in the UK. He has lectured power utility Risk Management to utility and insurance executives, and has lectured operations management and human resource management in an MBA programme for more than nine years. He is a senior member of the South African Institute of Electrical Engineers (SAIEEE).

Lovemore Chilimanzi

Technical Director

Penny Herbst has over 30 years of experience in an utility environment most of this in Eskom’s Treasury department, where she was exposed to a diverse set of financial, commercial and legal structures that emanate from its operations. Amongst others she has managed Eskom’s foreign and interest rate risk, money and capital market investments, project finance transactions, where she, and the structuring of projects to mitigate risks associated with projects in Africa. She led the formation of Eskom’s Development Finance Unit where in the role of Development Financing Manager she was instrumental in raising, in excess of $6bn, from DFI and related institutions. This included funding for Eskom’s first renewable projects where she spent some time in Eskom’s Renewables Unit working on bridging the gap between financing and implementation.

Penny Herbst

Non-Executive Director

Philippe Niyongambo is a well-known energy expert on the African continent and beyond. He has a Master of Science in Engineering Management from the University of Lawrence, Kansas, USA and a post-university degree in Energy Planning and Policy from the University of Pennsylvania, Philadelphia, USA. He also hold a bachelor degree in electrical engineering from the ISMI, Mons, Belgium. From February 2005 until October 2015 he was the Head of Energy Division within the Department of Infrastructure and Energy, African Union Commission. During that period he developed key energy programs including the Program for Infrastructure Development in Africa (PIDA-energy sector), the Geothermal Risk Mitigation Facility (GRMF) and the Geothermal Regional Program for the Eastern African Countries and mobilization of over a Hundred Twenty million USD (The GRMF has allocated grants to 15 projects amounting more than 60 million USD), the establishment of Africa-EU Energy Partnership which is the most successful of the eight partnerships joint Africa-EU Strategy launched in 2007, the SE4ALL Africa Hub Action Agenda and Investment Prospectuses for African countries and participation at the elaboration of the Africa Renewable Initiatives supported by G7 and adopted at the COP21 in Paris, France in December 2015.

Mr Philippe NYONGAMBO

Advisory Committee Member

For more information please contact Ana Hajduka (Africa GreenCo Founder and CEO) at ana.hajduka@africagreenco.com or on +647789204363

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For information on the role of the World Bank in the Southern African Development Community (SADC) region, please visit www.worldbank.org/sadc

The Rt Hon Andrew Mitchell MP

Advisory Committee Member

The Rt Hon Andrew Mitchell MP has been the UK Member of Parliament for Sutton Coldfield since 2001. Following the General Election in May 2005, he was appointed Shadow Secretary of State for International Development. He then served as the Secretary of State for International Development from May 2010 – September 2012 and Government Chief Whip from September – October 2012. In November 2003 he was appointed Shadow Minister for Economic Affairs and from September 2004 he was the Shadow Minister for Police. He was previously the Member of Parliament for Gedling from 1987 to 1997 during which time he held office as a Government Whip and was Minister for Social Security. He also served as a Vice Chairman of the Conservative Party 1992–93. Andrew was educated at Rugby School and studied History at Cambridge University. He was elected as President of the Cambridge Union in 1978. He served in the Army (Royal Tank Regiment) and was a United Nations Peacekeeper in Cyprus before joining Lazard, the international investment bank.

For more information on the role of the World Bank in the Southern African Development Community (SADC) region, please visit www.worldbank.org/sadc