

## **High-profile bankruptcies in the off-grid sector: Where do we go from here?**

### **Executive Summary:**

The high-profile bankruptcies of some of the African off-grid industry's best-known brands has raised questions on the long-term viability of current off-grid business models. **The Alliance for Rural Electrification (ARE) remains undoubtedly positive and convinced of the long-term health of the market**, buttressed by its core *raison d'être* which is to deliver about 75% of all new electricity connections at least-cost to achieve universal energy access by 2030 (SDG7).

With this article, ARE seeks to flesh out some of the core challenges and sector trends, and proposes a number of key recommendations on how to move forward and turbocharge the sector, so that SDG7 can move from being a global political goal to an actual reality on the ground.

**Brussels, 5 June 2019** - The high-profile bankruptcies of two of the off-grid industry's most well-known companies active in African (Mobisol and Solarkiosk) have grabbed headlines. This seems to have cast a shadow in the eyes of some investors over the prospects of the off-grid market and particularly the viability of business models in rural electrification.

The Alliance for Rural Electrification (ARE), which brings together market actors all along the decentralised renewable energy value chain, remains justifiably optimistic about the long-term prospects of off-grid market and the crucial role it plays in actually delivering on the global goal to achieve universal access to energy by 2030 (SDG 7). Without delving into the specifics of the two companies, ARE is convinced of the long-term health of the off-grid sector, provided some conditions are met.

### **Financial challenges**

**In order to move forward, one must first observe the financial challenges of the off-grid sector which are of are highest relevance for Africa, too.**

First, in any economic sector, companies go bust. Starting a business in any sector always involves some level of risk, and even more so in a complex market like the African rural electrification sector. The fact that some actors survive and others do not can thus be seen that the off-grid market is maturing. Moreover, there are plenty of thriving companies across the off-grid space, so the fact that some companies struggle is not representative of an industry trend.

Second, over the last few years, there has been a clear trend whereby public investment in the sector has moved from grant-like instruments to blended finance. This has had a positive impact in that companies needed to futureproof their business models and incentivised them to think more long-term in the deployment of their projects. However, perhaps the pendulum of providing adequate de-risking support swung too far in the other direction, with the rural electrification sector now expected to be achieving full commercial viability; this in a sector which targets the hardest-to-reach clients – i.e. the rural energy poor - and faces a distorted market situation in view of the heavily subsidised central grid and fossil fuel sectors.

Third, in addition to partial public funding, many rural electrification projects and companies need to rely on venture capital and private equity funding, as large swathes of the sector are perceived to be risky. In addition to raising the weighted average cost of capital (WACC), this also creates a potential conflict of interest whereby an industry that is fundamentally long(er)-term needs to rely on investors with a shorter time horizon.

Moreover, because of the reliance on investors seeking high returns in a fairly short time horizon, companies are incentivised to develop scale-up strategies seeking growth at any cost, which can jeopardise the sustainability of the business model and the quality of the value proposal to clients.

Fourth, as appears from the ARE "[Energy Access from the Bottom Up: Start-up and SME Showcase 2018](#)" publication, access to finance remains a huge barrier limiting the growth and rapid upscaling of clean rural electrification. In particular, off-grid companies often struggle to access working and medium to long-term capital, whether through debt or equity.

Fifth, policies and regulations are still not designed to really enable decentralised renewable energy deployment across rural areas. For example, in many cases it is not clear what will really happen when the central grid arrives to an area that a mini-grid has already electrified. Or who will pick up the tab when VAT or import duties on renewable energy equipment tick up. Or how a company can effectively confront the issue of substandard goods in the market.

The inadequacy of many policy frameworks (as well as other risks like off-taker or currency risk) means that some risks remain, which in turn are expensive to hedge against. ARE has identified some [core recommendations](#) that public stakeholders may consider when reviewing their frameworks, and always stands by to engage in stakeholder consultation.

### **Positive macro-economic outlook**

Having taken stock of some persistent challenges, it is also worth considering the major trends, dynamics and emerging issues across the sector.<sup>1</sup>

Firstly, renewables have become the technology of choice, making up almost two-thirds of global capacity additions to 2040, thanks to continuously falling costs and supportive government policies.<sup>2</sup>

Secondly, electricity is the fastest-growing source of final energy demand, and over the next 25 years it continues to outpace energy consumption as a whole. The power sector now attracts more investments than oil and gas combined. As a result, this will transform the global power mix, with the share of renewables in generation rising to over 40% by 2040, from 25% today.<sup>3</sup>

Thirdly, distributed technologies can provide power where the traditional grid is non-existent, inadequate, not cost-effective or too distant for connection. These technologies, and the innovative business models that deploy them can deliver not just energy but also economic opportunities to the two billion people not reliably served by the energy industry today.<sup>4</sup>

**As a result, decentralised systems, led by solar PV in off-grid and mini-grid systems, will be the least-cost solution for three-quarters of the additional connections needed to provide universal electricity**

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<sup>1</sup> See also IEA's [Energy Access Outlook 2017](#)

<sup>2</sup> <https://www.iea.org/weo2018/>

<sup>3</sup> <https://www.iea.org/weo2018/electricity/>

<sup>4</sup> <https://medium.com/climatescope/distributed-energy-in-emerging-markets-a6319604e947>

for all,<sup>5</sup> and are essential to enable the productive use of renewables and thus local economic development.

However, fourthly, as SEforALL notes in its flagship Energizing Finance 2018 report, that the electrification investment gap remains large where it is most needed and its urgency is even intensifying,<sup>6</sup> while there has been a dramatic and encouraging increase in electricity access investments over the last four years overall in the 20 high-impact countries – which accounted for 79% of the global access deficit in 2016.

### Way forward

Having outlined a series of challenges and key trends, the question becomes, what can be done to improve the prospects of the off-grid sector? How can the decentralised energy sector not only survive, but thrive and deliver on the goal of universal energy access? A big part of the answer lies in the financial fundamentals of the sector.

Indeed, in our view, the key to unlock the required capital mainly lies with public sector investors, whether donors, development finance institutions, governments in energy-poor countries and, to a lesser degree, charitable and impact investors. These are the prime stakeholders with a mandate to strive towards clean energy access in the public interest, as well as the financial and technical acumen to deliver it.

**In essence, public investors should drive the development of innovative financing mixes, crowding in private capital, boost their internal procedures, as well as set up mechanisms to de-risk investments in the off-grid sector. Initiatives such as the recent EU External Investment Plan and ElectrIFI are great examples of how public bodies could design and implement such actions. Other ideas that could be experimented with further is more public-private-partnership (PPP) pilots as well as result-based financing (RBF) which can contain a healthy combination of grants and concessional finance.**

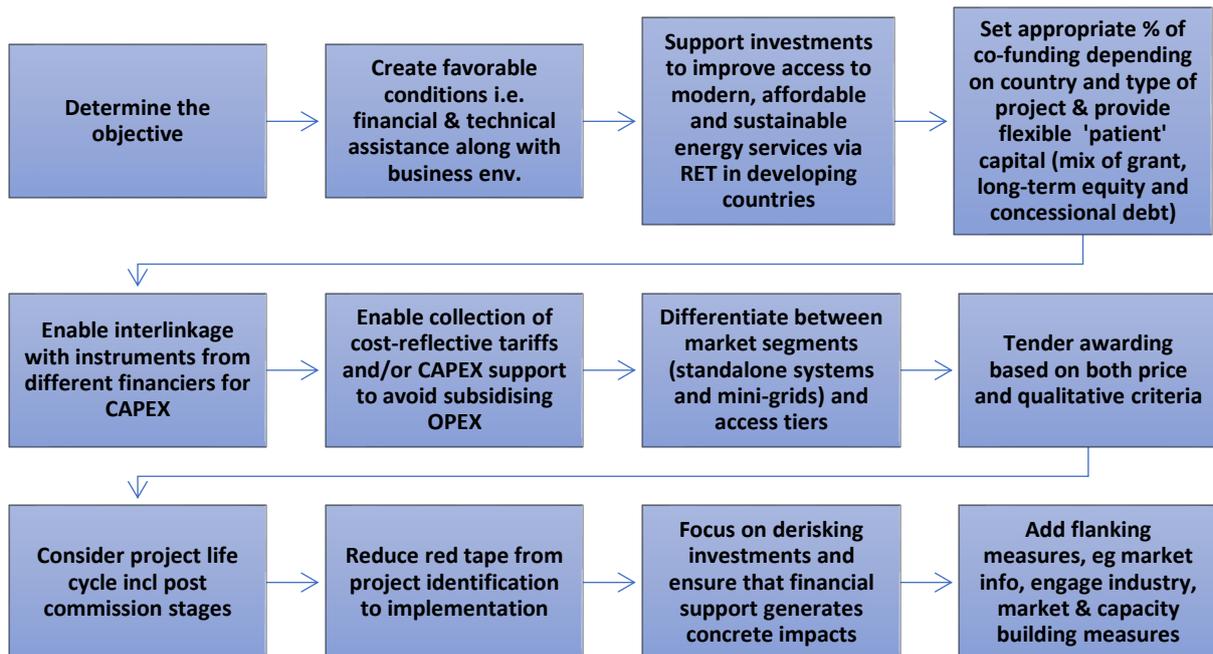
### Recommendations by ARE

Building on a strong partnership between the public and the private sector, ARE developed the following concrete recommendations to encourage investment in DRE rural electrification:

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<sup>5</sup> <https://www.iea.org/energyaccess/>

<sup>6</sup> <https://www.seforall.org/energizingfinance>



In the end, we believe that public, private and other stakeholders need to work together to deliver on clean energy access both to eradicate energy poverty and enable local economic deployment through productive use. Together they have the public interest in mind and can come up with ways to harness the power and creativity of the private sector to deliver on public objectives. And indeed, the private sector is up to the task, provided the right market conditions are created. Or to [quote](#) one ARE Member (THEnergy): “We are convinced that private start-ups are much more efficient than most of the local utilities in electrifying rural areas in developing countries”.

#### Contact:

Marcus Wiemann, ARE Executive Director – [m.wiemann@ruralelec.org](mailto:m.wiemann@ruralelec.org)

David Lecoque, ARE Senior Policy and Business Development Manager – [d.lecoque@ruralelec.org](mailto:d.lecoque@ruralelec.org)

#### Note to the editor

[The Alliance for Rural Electrification \(ARE\)](#) is an international business association that promotes a sustainable decentralised renewable energy industry for the 21st century, activating markets for affordable energy services, and creating local jobs and inclusive economies. We enable improved energy access through business development support for more than 130 Members along the whole value chain for off-grid technologies.