PUTTRU

Looking for Funding?

A Guarantee Alone Won’t Seal the Deal

September 2024

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How much can having a guarantor really help you close that funding deal? If you're an off-grid renewable energy business in Nigeria, our experience shows that a guarantee alone is often not enough to secure financing from lenders. Contrary to the findings of the International Energy Agency's (IEA) World Energy Investment Special Report, which suggests that "payment and revenue risks can be offset by the wider availability and use of guarantees,[1]" the reality on the ground tells a different story.

In Nigeria, one factor outweighs the strength of any guarantee—a solid company balance sheet with diversified and predictable revenue streams. Here is why financial stability is the true key to success in securing funding.

The Challenges of Off-Grid Renewable Energy Businesses in Nigeria

Off-grid renewable energy businesses in Nigeria face unique investment risks, making them less attractive to financial institutions—both commercial and development-focused. These risks stem from a combination of market characteristics and business models that are often challenging to sustain.

1. **Serving Low-Income, Price-Sensitive Communities**

Off-grid renewable energy companies typically serve remote areas where the national grid doesn't reach. These areas are home to low-income households, who already spend a large portion of their income on energy. As a result, they are highly price sensitive. Even a small increase in energy prices can lead to a disproportionate drop in energy consumption compared to wealthier communities. This makes revenue generation unpredictable and increases perceived risk in the eyes of lenders.

2. **Limited Revenue Diversification**

Many off-grid renewable energy businesses focus solely on installing and operating mini-grids, leaving their revenue streams tied entirely to low-income, price-sensitive customers. This lack of diversification weakens their balance sheets, making them more vulnerable to fluctuations in demand or pricing challenges. Financial institutions see this heavy dependence on a fragile customer base as a significant risk.

3. **Reliance on Government Grants**

A large number of these businesses exist primarily due to the availability of government grants, such as those provided through the Rural Electrification Agency (REA) performance-based grant programs. Without these grants, many of these companies would struggle to survive. Additionally, few of these businesses have a track record of projects that have been generating solid, sustainable revenue for over five years without relying on grant support. This lack of long-term financial viability further discourages investment.

How Lenders Respond to Investment Risks in Off-Grid Renewable Energy

One of the most critical lessons we've learned is that guarantees, while often highlighted in theory, hold less value in practice. Lenders don't

[1] IEA (2024): World Energy Investment Special Report: Reducing the Cost of Capital: Strategies to unlock clean energy investment in emerging and developing economies.

want to resort to calling on a guarantee or taking over your legal mortgage in the event of default. As one lender put it, “We’re not in the business of owning properties.” So, what are lenders actually looking for?

1. **Debt Servicing Capability**

Lenders want to ensure that your company can service its debt on time, regardless of whether your mini-grid project generates the expected revenue. They are not interested in dealing with the consequences of underperformance. This is why they prioritize companies with a diverse balance sheet and stable, low-risk revenue streams. Simply put, they want the debt to be paid without relying on the success of a single, unpredictable project.

2. **Guarantees and Grants Aren't Enough**

Although performance-based grants and guarantees may look promising on paper, they can’t compensate for a weak balance sheet and unpredictable revenue streams when it comes to raising debt. Lenders want financial resilience, not just promises backed by grants or guarantees.

3. **Introducing Credit Risk Report (CRR) and Project Proposal Development (PPD)**

To address these issues, we at Puttru introduced the Credit Risk Report (CRR) and Project Proposal Development (PPD) services, both tied to our Resource and Fund Mobilization (RFM) service. We don’t just connect businesses to lenders—we save time for both parties by ensuring we only engage with companies that meet the following criteria:

- Have a solid balance sheet sufficient for raising capital.
- Possess collateral (e.g., legal mortgages or properties) and the ability to secure guarantors.
- Demonstrate a track record of successfully implemented projects that continue to generate and sell electricity at commercially viable rates.
- Operate a mature business with a diverse balance sheet, reducing the risk if a mini-grid project underperforms.

By filtering clients through these criteria, we help ensure that both companies and lenders are set up for success from the start.

Conclusion

Off-grid renewable energy businesses play a crucial role in providing essential electricity services to underserved communities that lack access to the national grid. Their importance is especially evident from the perspective of energy justice, which justifies the significant subsidies and grants they receive. At Puttru, we advocate for the strategic use of public funds to stimulate growth in this sector.

However, as governments shift their focus from providing grants to encouraging the development of commercially viable businesses capable of securing financing on their own, it is imperative for companies in the off-grid renewable energy sector to address the investment risks we have discussed. Lenders are increasingly seeking businesses with strong financial foundations and proven track records, rather than relying on guarantees and grants alone.

For off-grid renewable energy businesses aiming for commercialization, understanding and adapting to these realities is crucial. Companies must build robust, diversified balance sheets and demonstrate sustainable revenue models to attract and retain investment. By taking these factors seriously, businesses can position themselves for success in a competitive financing landscape.