

Annual Review - Summary Sheet

Title: UK Climate Investments		
Programme Value: £200m		Review Date: November 2016
Start Date: June 2015	End Date: November 2018	https://aidstream.org/files/documents/UKCI-business-case-2018-01-15-20180308030342.pdf

Summary of Programme Performance

Year	June 2015- Nov 2016	Dec 2016- Nov 2017	Dec 2017- Nov 2018
Programme Score	B	Not yet assessed	n/a
Risk Rating	Major	Not yet assessed	n/a

Outline of the programme

UK Climate Investments (UKCI) is a joint venture between the UK Green Investment Bank (GIB) and the Department for Business, Energy and Industrial Strategy (BEIS). The aim of UKCI is to demonstrate that the transition to low carbon development is possible, replicable at scale and commercially viable, whilst simultaneously contributing to economic growth and poverty reduction.

The GIB has a successful track record in mobilising private sector investment into the UK's green infrastructure and economy in the UK. In 2015, the Department of Energy and Climate Change (now BEIS) established UKCI as a joint venture with the GIB in order to trial a new approach to investing UK climate finance, with a strong UK renewable energy investment brand and leveraging UK expertise in green finance.

UK Climate Investments Limited Liability Partnership (LLP) has been mandated to invest in a pilot phase (2015-2018) up to £200 million from BEIS's portion of the International Climate Fund (ICF) in low carbon projects in emerging markets. The Investment Mandate requires UKCI to make equity investments into 8 to 12 renewable energy (RE) and energy efficiency (EE) projects in India, South Africa and East Africa (Tanzania, Rwanda, Kenya).

The central objectives of the pilot are to:

- Use a private sector actor to have a **demonstration effect, build a successful track record and prove commerciality of low carbon investments** to the broader market by making a strong return on investment
- Achieve better value for money by **more effectively and nimbly interacting with the private sector**
- Increase the **visibility of UK climate finance** compared to the rest of the ICF low carbon development portfolio through the GIB's strong brand and reputation.

The original business case estimated that the pilot was expected to make carbon savings of 32Mt CO₂e in developing countries, create around 3,000 jobs and leverage £360m of private investment over the lifetime of the assets. These results were based on an indicative investment portfolio and actual results will depend on the specific investments made.

UKCI uses Official Development Assistance to make investments which is not to be tied to providing contracts or direct benefits for UK companies. However UK Climate Investments forms part of a portfolio of projects aimed at stimulating markets to attract private investment into low carbon sectors. The UK is at the forefront of the low carbon transition and therefore stands to benefit from expanding global markets into low carbon goods and services.

Summary of progress and lessons learnt since last review

This is the first review of the pilot and covers progress in its first 18 months, between June 2015 and November 2016. The reason that this review covers 1.5 years is that the original pilot was planned for three years but the pilot has been subsequently extended by 6 months to account for the significant delays that the privatisation of the GIB caused to the delivery of the pilot. Subsequent reviews will be annual.

The progress made by the pilot over the review period was below the expectations of both partners at the set-up stage, as the pilot did not make any investments in the first 18 months. One investment was approved at the Investment Committee but did not complete. These initial expectations were based on assumptions from the experience of both partners (GIB and DECC) but this pilot is very innovative and commercial experience of investing in these markets at the time was limited.

The overall score given to the pilot for the first review is a B. Despite the lack of progress in investments reaching completion, there has been considerable work in the first period to set up UK Climate Investments, build the team, network, originate and progress deals. We consider the practical experience of executing deals and better understanding of the barriers and challenges in these markets and sharing these with BEIS have been valuable outputs of the first year. However not all these efforts have been fully captured by the outputs in the logical framework - 'logframe (the tool used to assess progress of the ICF's projects against an agreed set of milestones) which accounts for the lack of positive results. Furthermore the privatisation of the GIB which was announced shortly after the business case for UK Climate Investments had been approved and signed, proved to be a major drain to resource and a barrier to building the investment team up to full strength.

A key aim of any pilot is to test a theory, this annual review provides an opportunity to reflect on the experiences on the first 18 months and adjust our approach in future years. As part of the sale of the GIB, the original LLP Agreement had to be renegotiated (to ensure that it is contractually appropriate under new ownership) and therefore provided an opportunity to agree changes to the parameters of the pilot based on what we have learned so far. It is also important that the lessons learned from this pilot in making renewables and energy efficiency investments in similar geographies. These can be shared and incorporated into the strategy of the ICF which is a key benefit of this pilot.

Summary of recommendations for the next year

1. Improving performance- deployment of funds

The biggest risk to the pilot is the inability to deploy funds into equity investments (see Section C - Output 1). Expanding the flexibility in the investment criteria could help, however we want to ensure that the only changes that are made we consider essential so that we can continue to test the mandate as originally envisaged. As part of the UKCI joint venture contract (re)negotiation during the sale process both parties to the LLP agreed to expand the target geographies in Africa to include all of sub-Saharan Africa.

We also consider the privatisation to have been a limiting factor in particular due to its impact on resourcing. Therefore to make up for time lost during the early period of the pilot BEIS has agreed to

a six month extension to the investment period which will now end in November 2018 instead of June 2018. Both of these changes are effective as of the completion of the sale of the GIB.

BEIS will also agree an action plan with the new owner post-privatisation with a particular focus on improving the resourcing, management and implementing the changes outlined above.

Action	Deadline	Lead
Put in place an action post-completion of the GIB sale to ensure new owners are up to speed on the requirements of the mandate including additionality, transformational change and poverty reduction.	Q3 2017 (dependant on sale)	BEIS Project Lead
Ensure UKCI Investment team is built up to capacity and with the right level of experience and the right leadership and access to in-country expertise (this is contingent on the sale completing as UKCI will struggle to attract/ retain staff in the interim).	Q3 2017 (dependant on sale)	New Owner / UKCI Managing Director

2. Governance - Investment Committee

Linked to the deployment of funds is the governance and role of the Investment Committee (IC). We will work with the new IC which will be reconstituted by the new owner (BEIS will retain its current role and membership) to encourage assessment of specific projects in the context of the wider portfolio we are looking to build. (ensuring we have a good mix of deals of different sizes and technologies and geographies should encourage the team, to not focus only on commercial aspects in order to test the concept. We will also encourage the new IC to expand on the level of debate taking place at the IC as this would further help the learning process for BEIS and the UKCI team.

The UKCI partners have also agreed as part of the contract re-negotiation to appoint an independent member with experience investing in developing markets or development experience if BEIS considers that this is required.

Action	Deadline	Lead
Discuss with new owner membership and new processes for the IC. If agreed, necessary commence recruitment of independent member.	Q3 2017 (dependant on sale)	G7 Strategy lead/ UKCI team / New owner

3. Promotion of UK Climate Investments

One of the original aims of the pilot was to bring more visibility to UK Climate Finance as opposed to the current level of visibility being achieved investing through multilateral development banks.

As UKCI has not yet made any investments, promotion of the pilot widely has not been appropriate.

Once a first investment is completed, an agreed strategy to external communications will be needed. Therefore BEIS recommends setting up a workshop to discuss with UKCI / GIB government relations team and the new owner to agree an approach to promotion activity.

This should include the use of branding for the website and events plus using the Foreign and Commonwealth Office (FCO) / Department for International Development (DFID) networks in raising the profile of the the pilot.

Action	Deadline	Lead
Set up workshop to discuss promotion activity and agree comms strategy	Q3/4 2017 Dependent on timing of first investment	Project manager, BEIS, and New Owner Comms teams

4. Aligning expectations and understanding of transformational change and poverty reduction

Following the sale, we will work with the UKCI team and new owner to ensure they understand our ambition for transformational change, delivery of Official Development Assistance and poverty alleviation. Related to this issue, we also aim to agree a joint UKCI risk appetite and risk management process as to date both BEIS and GIB staff have followed their own processes.

Action	Deadline	Lead
Agree and implement joint risk appetite and management process	Q3 2017 (dependant on sale)	Project team and Board

5. The external evaluation - capturing and embedding experience from the pilot

Due to the delay in completing investments the independent evaluation has not been able to progress as originally envisaged. BEIS will consider how to get the most out of the evaluation in the time that is left and whether it should be reduced in scope. We also need to ensure that lessons coming out of the evaluation are incorporated as the pilot progresses and are also disseminated more widely around the ICF programme. We will consider therefore holding workshops or similar to disseminate findings of the evaluation provider.

Action	Deadline	Lead
Agree scope for evaluation contract	Q2 2017 (depending on rate of disbursement)	Project Manager, Ipsos MORI

6. Logframe

The annual review process revealed some potential weaknesses with the current logframe.

Between now and the next annual review the BEIS project manager, GIB and BEIS analytical teams, and Ipsos MORI will consider whether it contains the right outputs/outcomes.

One area already flagged for consideration is how we can make learning a specific output we record progress against as we think it is important for improving both the investment process and institutional learning within BEIS.

Finally we will consider whether the milestones for the remainder of the pilot are realistic and achievable. We will discuss with the new owner, when they are in place and have had some operational experience of the UK Climate Investments mandate what they think the final portfolio of investments will look like, and if appropriate, adjust the value for money case (VfM) accordingly. If we do consider it necessary to adjust the milestones in the logframe we will concurrently review the analytical mode used to project likely results of the pilot to ensure that all our assumptions are up to date.

Action	Deadline	Lead
Discussion of logframe output/ outcome indicators, possible including interim indicators and lessons learned, methodology for cost of capital and milestones (see Section B page 8).	Q2/3 2017 (depending on timing of the sale)	Project manager, BEIS analysts, Ipsos MORI, GIB analysts

B: PERFORMANCE AND CONCLUSIONS

Annual outcome assessment

The vision of success is for UKCI to have invested in a diverse portfolio of projects, which demonstrates transformational impact and is additional (i.e. would not have happened without the intervention of UK Climate investments).

In the first 18 months of the pilot, UK Climate Investments did not make any investments. Our assessment is that, as it stands, the UKCI investment team will have difficulty disbursing all the funds, particularly without a significant increase in rate of executing investments. If this occurs, the funds earmarked for this project will be made available to invest in other ICF projects.

One of the key learnings from the first year is about the challenges for GIB in making investments that meet the UK Climate Investments Mandate. The lead time to making these investments is longer than originally expected, but as the pilot progresses we expect this lead time to decrease and the likelihood of deals in the pipeline being converted into successful investments to increase.

Additionally, it became clear in the first reporting period that the views between the GIB and BEIS about how you effect transformational change were not aligned. In the first part of year two (last six months of this reporting period) BEIS and GIB have had a number of discussions at the UKCI Board and Investment Committee to address this misalignment. It is essential that post-privatisation BEIS's expectations are communicated clearly to and understood by new senior management. Below are the intended outcomes of the pilot and the assessment of them at this stage:

Outcome One – Strong Climate Outcomes

If the full allocation is not disbursed into a portfolio of investments with similar characteristics to the model portfolio in the business case by the end of the pilot, climate outcomes in absolute terms for the pilot are likely to be lower than originally modelled (though they are not expected to be different in terms of tonnes Co2/£ invested).

Outcome Two – Strong Development Outcomes are secured from the Project: total number of direct jobs created by UKCI projects

As above, lower disbursement of UKCI's allocation and a smaller portfolio of investments could result in lower number of jobs overall for the pilot than the number originally modelled.

Outcome Three – Decreased Cost of Capital, Reduced Cost of Capital to similar Projects

This outcome was included in September 2015 as a result of the updates to the logframe with the revised theory of change however we have yet to agree a methodology as it is challenging to attribute any reduction in the overall cost of capital to in these technologies in these markets to UKCI's investments specifically. This will be discussed by BEIS, GIB and Ipsos MORI the evaluation provider before the second annual review.

Outcome Four – UK Climate Investments pilot improves risk perception, demonstrates feasibility/return of RE/EE investments (return on investment of portfolio, speed of implementation)

In spite of the delays we expect UK Climate Investments to pursue deals that provide a strong rate of return (in the logframe the target is constant at a 10% return on investment).

In terms of speed of implementation, also included as part of the logframe update, we expected to see the time between deal origination and execution to decrease over the course of the investment period as the team built up experience and networks. Already we have seen th at this has been slower than

expected, which could be the result of macroeconomic factors in the target geographies, for example in South Africa, as well as a lack of capacity in the team and a lack of in-country presence.

Overall output score and description

The overall output score for the Pilot is a B

Output 1 - *Pilot improves risk perception, demonstrates feasibility/return of RE/EE investments*

Weighting 65%

Score-B. The pilot has not made any investments or mobilised any private or public finance.

Output 2 - *Strong international network established (for both deal origination and effective dissemination)*

Weighting 35%

Score B. The pilot has made positive progress in a number of areas: building up a network in target geographies, deal activity, origination and developing a pipeline.

Output 3 - *Renewable energy and energy efficiency measures are installed*

These outputs are not weighted in year one (as we were not expecting to see any results) and therefore do not factor into the overall scoring.

For further discussion of these outputs and evidence please see Section C.

As there has also been significant activity in the first year to set up the pilot and to originate a pipeline, as well as a number of other activities arising unexpectedly, there is a summary of progress that was not reflected in the output scoring in **section D**.

Has the logframe been updated since the last review?

This is the first review of the pilot. However, the logframe has been updated during this review period. In order to better align BEIS and the delivery partner's understanding of transformational change and our vision of what success looks like, the third party evaluation provider (a consortium provided by Ipsos MORI) facilitated a Theory of Change workshop and produced a revised theory of change document reflecting views of all parties. The revised logframe was subsequently developed by BEIS in collaboration with Ipsos MORI and GIB to align with the revised theory of change and signed off in September 2016. The main changes were:

Impacts

- Promotion activity for the pilot (number of events held) has been moved to an output from an impact.

Outcomes

- Climate (GHG reductions) and development (jobs) outcomes have been separated into two distinct outcomes
- *Volume of finance mobilised and co-investors brought into markets* has been moved to the outputs section from outcomes.
- *Improving energy access* has been removed; the ICF key performance indicator (KPI) refers to off-grid access whereas UK Climate Investments will principally look at on-grid projects.
- *Rate of fund disbursement* was removed as it was not considered to be providing any new information than the cumulative number of investments in the outputs section and could incentivise the investment team to focus on larger deals which are not always the most innovative/transformational.

Outputs

- 'Building up networks' has been clarified to communicate better what BEIS intended with regards to these activities.
- 'Using a team with relevant experience for due diligence' was removed BEIS sees this as baseline requirement rather than an explicit objective.)
- 'Renewable energy and energy efficiency measures are installed' has been changed from 'expected' to 'actual' to align with ICF KPIs which measure actual measures installed.

Milestones

- The milestones in the revised logframe themselves are consistent with expectations that were set at the start of the pilot, using the model and assumptions from the business case and not retrospectively changed to align with actual progress.
- It is worth noting that although these milestones were drawn from the original model and assumptions from 2014, these had not all been inputted into the original logframe or communicated and agreed with GIB as they were designed to be indicative. However, BEIS does not think this will have affected GIB's attainment of the milestones as the incentives were in place for the team to complete deals and activities associated with this process.
- If our joint expectations for the pilot change post-privatisation we will update these milestones and change the value for money (VfM) case accordingly.

Weightings

- Weightings for each set of outputs were added when the logframe was updated as they were not included in the original logframe.
- Output 3 – *Renewable energy and energy efficiency measures are installed* in the revised logframe was updated (as above) from 'expected' results to 'actual' results. In year one we were not expecting any actual results against this output as we expected a lag between making an investment and increased capacity or energy savings due to construction times. Therefore it was not considered appropriate to this output any weighting for the first review as even if UKCI had made investments we would not have seen any results in this area. Therefore greater weightings have been accorded to Outputs 1 and 2 (65% and 35% respectively).

Conducting the annual review process revealed some weaknesses with the revised current logframe. The BEIS teams' views are that the logframe, as it stands, does not necessarily capture all of the valuable outputs of the pilot (including lessons learned which was a core aim at the start) as well as fully measure progress and achievement of poverty reduction objectives. Therefore, BEIS, alongside GIB and Ipsos MORI, will consider making further changes to be finalised three months before the next review which will take place in November 2017.

Actions

Action	Deadline	Lead
A methodology for the new outcome in the revised logframe – <i>'Reduction to cost of capital'</i> - does not yet have an agreed methodology - we intend to have a workshop to agree how we will measure and attribute any changes to cost of capital in relevant markets.	3 months prior to next review	GIB Green Team, BEIS Analysts, BEIS Project Lead
With <i>'Number of people with improved energy access'</i> removed as an outcome, we should	3 months prior to next review	GIB Green Team, BEIS Analysts,

consider whether we could include additional indicators that capture development and poverty reduction effects of the pilot.		BEIS Project Lead
Having only 'actual' installed capacity and demand reduction instead of expected means there are results to discuss in the early years. We should consider including both expected and actual,	3 months prior to next review	GIB Green Team, BEIS Analysts, BEIS Project Lead
We should consider how the logframe could be used to capture the lessons learning process in a more systematic fashion: if recording and embedding lessons learned is something that is reported on it this could create a greater incentive to focus on this aspect of the pilot. The BEIS project and Compass (ICF wide monitoring and evaluation) teams should consider how to operationalise this idea in the second reporting period.	3 months prior to next review	GIB Green Team, BEIS Analysts, BEIS Project Lead
We should update milestones post-privatisation with agreement from new owners to ensure they are realistic.	Once the new owners are in place	BEIS Strategic Lead, UKCI Management and Investment Team

C: DETAILED OUTPUT SCORING

Output Title	Private and public investment mobilised directly by UK Climate Investments funding		
Output number per LF	1	Output Score	B
Risk rating:	Major	Impact weighting (%):	65%
Risk revised since last Annual Review?	This is the first review	Impact weighting % revised since last AR?	n/a

	18 month milestone	18 month achieved
1.1 Cumulative number of investments and capital invested by the fund	3	0
1.2 Volume of public finance mobilised for climate change purposes as a result of portfolio (ICF KPI 11)	0	0
1.3 Volume of private finance mobilised for climate change purposes as a result of portfolio (ICF KPI 12)	0	0
1.4 Number of private and public sector investors across portfolio	0	0

Key points

- This year the pilot has scored a B for this output as the pilot did not meet the target milestone. These outputs are the most highly weighted in the assessment of progress in this first review period and therefore the score for this section will strongly influence the overall score for the review.
- Between May 2015 and November 2016 the LLP did not make any investments. The expectation for the first 18 months was that the pilot would make three investments, and the resulting mobilisation of public and private finance would follow in year two and three.
- One investment was close to signing (Project Moon¹, a solar project in India) having received final approval at the Investment Committee on 24 March 2016 - however the deal including UKCI's equity did not reach financial close.

¹ In this review we refer to the projects by code names e.g. 'Moon', 'Hallway'. This is for commercial reasons as we cannot name the companies UKCI considered entering into an investment with or decided not to enter into an investment with. Upon completion of investments these company names will be made published and each investment will be accompanied by an official press release or statement.

- None of the other deals in the pipeline made it through to the final stage of the Investment Committee process during the reporting period. Project Sigma was approved for investment shortly after this review period but has yet to complete.
- Given that the total pilot investment period is currently 3.5 years, and 18 months into this period the pilot had not completed any investments, the likelihood of achieving the original target of 8-12 investments is reduced. Our risk rating for this output is Major (risk of not being achieved).
- There are a number of factors contributing to this situation, including the privatisation of the GIB which this section will explore in more detail.

Output Indicator 1.1

Progress against milestones

Before the start of the pilot, the expectation had been that the LLP would make around three investments in the first year. However, this was then revised down to one investment at the start of the pilot to reflect BEIS's experience with other programmes regarding the time it takes to build up a pipeline of investments.

The Investment Committee considered a total of twelve projects in the first year of the pilot, with two Hallway and Chroma being considered at a stage where a term sheet could be agreed and one project (Moon) getting to final stage (of a three stage process) where an investment was expected to be signed imminently (see Table One below). [The deal fell down on commercial grounds - one of the aims for the pilot is for the vehicle to be profitable and commercial to have a 'demonstration on the market.' Information received from the GIB investment team was that at the final moments, the risk / return profile of the deal deviated from what had been originally agreed with the co-investor. Consequently, the GIB team felt that the revised deal would not meet the commercial hurdles required and, as a result, an agreement could not be reached.] Overall, few projects were developed to final stages which meant the pipeline was not resilient and therefore UKCI was not able to meet its targets.

Table One - Projects considered by Investment Committee

Investment Committee	Preview Stage	Structure Stage	Pre-Final/Final Stage
Jul-15	Moon*		
Sep-15	Hindustan	Moon	
Oct-15	Hava	Moon	
Jan-16	Lime, Hava III, Spot, Chroma		
Feb-16	Hallway		
Mar-16		Hallway	
Mar-16			Moon
Apr-16		Chroma	
Investment Committee	Preview Stage	Structure Stage	Pre-Final/Final Stage

Aug-16	Helios	Hallway (update)	
Sep-16	Saturn; Sigma		
Oct-16		Lime	

Factors limiting progress

The main areas of challenge identified through interviews conducted by Ipsos MORI in September 2015 with stakeholders of the LLP were:

1. Design elements

There is broad agreement that the scope of the investment mandate - designed in order to deliver as much transformational impact as possible - coupled with a commercial imperative, has proved challenging to deliver in practice.

a) **Geographies:** During the design of the pilot, BEIS and GIB considered a wide list of target geographies on the basis of a country analysis by KPMG - before settling on the three regions: India, East Africa and South Africa. At the time it was believed these three region/countries presented the most favourable characteristics to meet the pilot’s objective of transformation within the context of commercial investment (for more on how the markets in these geographies have changed see the external factors below).

At the set up phase the GIB was confident as to how quickly investments could be made in these geographies. However during the course of this period, macro-economic changes and additional investment challenges meant that the limited country selection made investment more challenging. In South Africa, political and economic challenges served to stall the Renewable Energy Investment IPP Procurement Programme (REIPPP). Also, the difficulty of achieving financial close on power projects in Kenya and Tanzania became more apparent, something that perhaps should have been picked up earlier in the process.

In India, UKCI has had to consider a variety of complex investment structures and instruments in order to ensure compliance with Indian Foreign Direct Investment, regulatory and legal requirements, whilst also meeting the UKCI mandate (including the need to ensure that the deployment of funds was consistent with Overseas Development Assistance rules). A subsidiary of UKCI was created after the end of the first year with the intention of facilitating the investment process, but this did not solve the problems associated with deal structuring. In South Africa, UKCI has created innovative structures to allow its funding to support Black Economic Empowerment investments and this has required significant legal consideration.

Although BEIS considers that the team has worked hard to put in place the essential foundations for making investments in these geographies, BEIS’s assessment is that i) there was a failure to fully recognise in the GIB planning process the technical difficulties of operating and investing in these countries; ii) the time taken for GIB to adapt to investing in these markets was significantly underestimated in the business planning and iii) the lack of presence on the ground in these

geographies has made originating and agreeing investments significantly harder.

- b) Financial Instruments:** UKCI's mandate requires that the vehicle invests using equity or 'equity like' instruments in order to comply with UK Overseas Development Assistance Rules whilst also retaining the required commercial imperative of investing "at market". This limits the structures that UKCI can use to invest and therefore limits the universe of potential investment opportunities. The investment team considers that the inability to make shareholder loans in projects has made UK Climate Investment's offer more expensive overall and that has made investing much more challenging. Their view is that allowing a wider range of instruments to include debt or debt-like instruments would make UK Climate Investments a more nimble investor. BEIS has agreed to explore the ODA eligibility of using shareholder loans in the future.
- c) Ticket size:** Particularly in the case of India, the UKCI investment team considers that the £30million maximum size per investment is also a limiting factor. At the beginning of 2016, the investment team brought an assessment of the market opportunities to BEIS for discussion. This included a request to increase the maximum size of investment to allow investment in companies at a platform level, rather than investing in specific assets or projects. The investment team's analysis suggested that in India there are more opportunities with these larger companies and platforms. The Board of UK Climate Investments in principle can agree to waive the size, but the team have not yet brought any investments of this form that are sufficiently transformational and additional to the Board. The team brought Project Chroma, an Indian deal, to the Board, but while it has transformational elements and is with a strong local developer, it was felt to be insufficient for the board to relax the restriction of £30m. However, that ability to relax the restriction can be used in future assuming the other requirements are sufficiently met.
- d) Deal structuring:** The UK Climate Investments mandate implies a restriction on being exposed to pre-financial close development cost risk which means that complex financial structures have to be developed to accommodate the developer to avoid that exposure. Deal structuring is therefore proving a lengthy process and the investment team are concerned that this restriction in the mandate limit opportunities for UK Climate Investments, partly outlined above in the consideration of financial instruments. In the case of Project Moon, the main issue of disagreement with the counterparty related to the allocation of development cost risk and return between the parties which provided ultimately unacceptable to UKCI.

BEIS had hoped the UKCI team would be able to structure deals creatively within the parameters set by the mandate and has requested evidence of these limitations in order to help identify where changes need to be made. We have agreed to allow more flexibility in the mandate (where investments align with our priorities) with Board agreement, and the UK Climate Investments is now regularly approaching BEIS early in the investment process to test specific cases which we hope will increase the likelihood of investments being made.

2. Delivery factors

- a) **Resourcing:** Since the beginning of the pilot the team has been under-resourced and below the level of experience that was set out in the agreed original business plan. This has meant that often senior team members are analysing data and writing papers (which should usually be the role of junior team members) rather than originating and transacting deals (as envisaged in the team structure in the UK Climate Investments business case). BEIS raised this issue on a number of occasions at board meetings. However it is worth noting that, by the end of the first year, the ability for the GIB to recruit, given the uncertainty around the sale of the GIB, was very limited. The GIB tried to address the capacity issue with core GIB staff whose developing country market experience was limited.
- b) **Finding the right deals/risk appetite:** BEIS, the UKCI Investment team, and GIB have spent significant time and effort discussing the balance between additionality (that other private sector investors will not be crowded out by our investment), the ability of investments to transform markets and the commercial viability of projects. Halfway through the first year BEIS raised concerns about the visibility of the transformational aspects in the deals. As discussions progressed, mis-alignments in risk appetite between BEIS and GIB became clear and it also became apparent that GIB's preference was to try and replicate its UK business model and approach by trying to partner with large-scale project developers operating in the target geographies which, in BEIS's view, was excluding more transformational deals and also reduced the additionality case.

GIB's view of what shifts markets is fundamentally different to BEIS's, seeing commercial success as the most important driver (this was likely to be a difference in view when delivering through a commercial organisation). At the end of the first year the Board discussed this in the context of Project Chroma and agreed to create a joint UKCI risk appetite. For example, in January 2016, the team spent considerable time investigating an off-grid solar project in East Africa (Project Spot) which was one of the areas of opportunity identified by UK Climate Investments in its strategy. UK Climate Investments needed to assure the Investment Committee that an income in local currency for a growing company was sufficiently secure to provide adequate return on the perceived risk. Ultimately, UK Climate Investments did not invest and the company eventually found alternative sources of capital.

- c) **Due Diligence:** GIB undertakes a professional and detailed due diligence approach for its UK investments and applied the same level of rigour to the UKCI investment process. A strong level of due diligence is vital to ensuring strong value for money for UKCI. However it also means that it has slowed the deal process as well as being a transaction cost burden on the potential investments which has effectively made UK Climate Investment money more expensive (as generally deal costs are charged back to the company to be invested in). There tends to be a higher level of uncertainty in emerging markets investing where the investor needs to take a view without full information and consider this as part of the risk/return trade-off. As an institution, GIB is not accustomed to investing outside the UK or the risk environment that exists in emerging markets.

d) **Management/Governance:** The BEIS team considers the senior management of the GIB did not fully grasp BEIS ambitions for risk appetite or transformational change and that our concerns raised at the Board about the way the pilot is progressing were not fully reflected in working practices (in terms of the types of deals being brought forward or the way transformational change was reflected in the papers). It is also BEIS's view that the GIB senior management team as a whole does not have sufficient experience of emerging market investments. Lack of developing country experience within GIB was identified as a key risk in the original business case and therefore is something that BEIS has been working with GIB to manage where possible. Interviews with staff from BEIS and GIB assessment suggests that there was a tendency at Investment Committee for these meetings to be overly choreographed which limited debate.

The UKCI pilot could benefit from more open conversations about the value of the projects, which would allow members to develop a sophisticated approach to investing in emerging markets by taking into account a wide range of views, instead of one previously agreed view.

3. External factors

- a) **GIB Sale:** The sale of GIB represented a change from the expectation when the pilot was being designed - that only part of the organisation would be privatised. BEIS has worked extensively with GIB and UK Government Investments to protect the objectives of the pilot. However, the privatisation process has had two significant impacts on UK Climate Investments: 1) it has taken significant resources on both the GIB and BEIS side that arguably could have been spent on the delivery of the pilot; and 2) created a huge amount of uncertainty exacerbating issues around staff management, retention as well as recruitment.
- b) **Macroeconomic factors** have had an effect on the universe of potential investments in the target geographies and potentially the deal flow available to UK Climate Investments. Ongoing currency and macroeconomic changes have affected investment levels in both East Africa and South Africa. According to the investment team and their networks, there have been few projects reaching financial close in Africa during the first year and a half of the pilot and the small number of projects that have reached financial close were already spoken for by other development finance institutions. This means that, while two projects have been developed by the UKCI team in South Africa, these did not complete and deal origination has been difficult. In India, the success of the renewable energy sector and government support has attracted significant interest which has reduced investment return expectations dramatically in a short space of time. This has made negotiating deals very difficult as the market pricing has been moving significantly during the negotiation.

Output Indicators 1.2 and 1.3

We were not expecting to see results against Outputs 1.2 and 1.3. as a result of investment entered into by the pilot until year two (due to drawdowns matching construction profiles of 6-24 months).

Output Indicator 1.4

As the LLP did not make any investments, the number of private and public investors in the UK Climate Investments portfolio is zero.

However as a result of their involvement in Project Moon, UK Climate Investments effectively helped to bring a new investor into the renewable energy sector in India as the investor followed through with the project even though ultimately UK Climate Investments involvement was terminated.

Recommendations:

The extent to which other design features raised by some stakeholders warrant further consideration needs to be balanced against the objective of the pilot to trial some of these specific elements to learn about their investment and transformational change potential.

There are a number of options for expanding flexibility in the investment criteria. Some of these have already been agreed between both members of the LLP through the contract (re)negotiation process as part of the sale including the expansion of the target geographies to include more African countries. The UKCI LLP members also agreed, as part of the contract renegotiation, for BEIS to have the right to appoint an independent Investment Committee member with experience investing in developing markets or development experience.

When the new owner is in place, BEIS will agree an action plan with a particular focus on improving the resourcing, management and implementing the changes outlined above.

Output Title	Strong international network established for both deal origination and effective dissemination		
Output number per LF	2	Output Score	A
Risk Rating:	Minor	Impact weighting (%):	35%
Risk revised since last Annual Review?	This is the first review	Impact weighting revised since last AR?	Not previously weighted

Indicators	18 month Milestones	18 month achieved
2.1 Number of people accessing information from GIB's website on the international pilot aggregated by geography	N/A	7,790 unique page views This number will act as the baseline for comparison against year two.
2.2 Number of meetings with stakeholders in project origination (potential) project investors, project developers	300	361 (Project developers only)
2.3 Number of meetings with stakeholders promoting UKCI and GIB overseas	12	30

Key points

- The pilot has scored an A for this output as the pilot met the expectations in this regard.
- This output is weighted 35% of the annual review scoring in year one.
- UK Climate Investments has performed as expected in terms of deal origination – the investment teams considered a wide range of projects in the target geographies even though this activity did not result in completed transactions or a resilient pipeline (for the reasons described in Output 1).
- Both GIB and UKCI have been very active in events, conferences and networking opportunities to promote UKCI alongside the GIB.
- Promotion of the pilot was used at the beginning of this period to raise the profile of the vehicle for business development. However, it will become difficult for UKCI to continue to promote the pilot without a deal history so this activity slowed down towards the end of the period.

Output Indicator 2.1

The BEIS ICF team did not set a milestone for the first reporting year as we did not consider there to be an 'appropriate' number of hits that would demonstrate adequate evidence of promoting the pilot.

The number of hits received in this period will act as the baseline. In the next review we would expect to see this number increase as a result of investment activity (deals completed) and promotion activity and have set an initial target of a 10% increase (though this will be reviewed as appropriate).

However, going forward, the website could be updated to explicitly make the link to UK Climate Finance and therefore meet the desired outcome of increasing visibility of UK climate finance. We could also capture how website visits are converting into actual enquiries.

Recommendations

Explore how to make an explicit link from the UKCI webpage (on the main GIB website) to UK Climate Finance/Aid.

Output Indicator 2.2

The reporting against this milestone shows significant activity in the deal origination space which is a necessary step towards building a strong pipeline.

UKCI has provided BEIS with a long list of the projects the investment team identified as potential opportunities pre-screened against the investment criteria in the first 18 months, which amounted to over 300 projects.

However, we have found that large amount of origination activity does not directly translate into a high number of deals coming through the Investment Committee, nor does it imply they are targeting sufficiently transformational projects. The main reasons for origination not leading to actual deals are:

- A large number did not fit the mandate in terms of country, the type of finance requested and the scale of investment (as the UKCI mandate requires that it is a minority investor).
- In some cases UKCI assessed that the developers were too early in their fundraising process and asked them to return later.
- A number of projects, including those that were previewed at the investment committee, did not meet the GIB's required standards.

In year two, we would expect this number to remain constant or reduced but see a higher rate of conversion as the team's efforts become more targeted.

Output Indicator 2.3

During the first review period the UKCI team participated in 30 events to raise awareness of the project and most notably around the official launch of the pilot during the Indian Prime Minister's State Visit in November 2015 (see Table One.)

The wider GIB team also attended a large number of stakeholder events and international conferences.

The list below documents the events that the UKCI investment team participated in. The team reported that in the vast majority of cases this lead to follow up discussions and new leads on deals.

The GIB also hosted a number of international delegations where they would include reference to UKCI as part of their presentations - see Table Two. (Although BEIS assessment of the materials used is that UKCI was not a significant part of these discussions)

In the logframe, we had envisaged these events would consist of UKCI having a platform to make the wider investment community aware of the types of opportunities available in these countries to demonstrate the commercial viability of these investments. This is why the target was set at a relatively low number. However we consider the types of events that the team did participate in to have been

appropriate at this stage of the pilot and therefore have included them in the results.

Aside from the launch there have been few of these types of events as the team feel that they would need to have a proven track record in order to do so. Therefore this type of promotion has been deferred until the first few investments have completed.

Once a number of investments have been made we would expect an increase in the promotion of the pilot (particularly overseas) to showcase its achievements and the impact of UK Climate Finance. A key objective of the business case is to receive credit in international negotiations and demonstrate mobilisation of private capital (towards the “\$100billion/year by 2020” goal).

Table One

	Date	Event	Audience
1	19 May 2015	UK-India Solar Day – Eversheds London	Investors, advisers and developers of Indian solar projects
2	20 May 2015	Africa Investment Forum – PE Invest Africa - London	Investors, advisers and management of African energy & other businesses
3	24 June 2015	GIB Annual Review 2015 - Edinburgh	Investors, advisers and renewable energy stakeholders
4	25 June 2015	GIB Annual Review 2015 - Edinburgh	Investors, advisers and renewable energy stakeholders
5	26 June 2015	RBC Capital Markets Renewables Conference - London	Investors, advisers and renewable energy stakeholders
6	6 October 2015	Solar Plaza – Delhi – investor roadshow PANEL: Opportunities and Challenges for Project Finance and Equity Raising	Investors, advisers and renewable energy stakeholders in India
7	7-10 October 2015	Solar Plaza Conference Hyderabad	Investors, advisers and renewable energy stakeholders in India
8	15 October 2015	EQCFS – Mumbai	Investors, advisers and renewable energy stakeholders in India
9	30 October 2015	London Stock Exchange – Indian Railways Minister Roundtable	Investors, advisers and renewable energy & transport stakeholders in India
10	8 January 2016	India Solar conference – Eversheds London	Investors, advisers and renewable energy stakeholders in India
11	11 February 2016	Young Renewable Energy Professionals Event - London	Investors, advisers and renewable energy stakeholders in India
12	17-19 February 2016	Making Solar Bankable conference, Amsterdam	Developers, Development Finance Institutions (DFIs), Investors

13	22 February 2016	India Innovation Lab seminar – Delhi	Investors, advisers and renewable energy stakeholders in India
14	17 March 2016	Clean Energy Finance India – IOD London	Investors, advisers and renewable energy stakeholders in India
15	23 March 2016	Solar Tenders in Africa, EBRD London	EBRD, AfDB, IFC, Investors
16	19 April 2016	Confederation of Indian Industry – seminar and roundtable with Indian Minister of Energy – London	Investors, advisers and renewable energy stakeholders in India
17	20 April 2016	City of London – Indian Renewables Roundtable	Investors, advisers and renewable energy stakeholders in India
18	20 April 2016	London Stock Exchange – Indian Energy Seminar - London	Investors, advisers and renewable energy stakeholders in India
19	27 April 2016	India roundtable: Clean Energy Summit - London	Investors, advisers and renewable energy stakeholders in India
20	5 May 2016	India Exim Energy Roundtable – London	Investors, advisers and energy stakeholders in India
21	19 May 2016	Alternative Africa Seminar, Fieldfisher London	Legal and financial advisers, DFIs
22	7 June 2016	Solar Finance & Investment India Speaker Invitation	Investors, advisers and renewable energy stakeholders in India
23	14 June 2016	BNEF - Energy Access networking - London	Investors, advisers and energy access stakeholders
24	24 June 2016	Renewables and Energy Innovation Investor Day – London	Investors, advisers and renewable energy stakeholders
25	21 June 2016	Trinity International 10 th anniversary event, London	Developers, Africa-focused investors, lenders
26	22-24 June 2016	African Energy Forum, London	Governments, developers, lenders, investors - anyone interested in power sector investments in Africa

27	30 June 2016	GIIC – London Stock Exchange Event of renewable energy IPPs in London	Investors, advisers and renewable energy stakeholders in India
28	15 Sept 2016	KPMG – India Solar Event – London	Investors, advisers and renewable energy stakeholders in India
29	9 November 2016	Private PPA Roundtable, Johannesburg	Nedbank, Standard Bank, DBSA, IDC, Power X, Lereko Metier
30	15-17 November 2016	COP 22, Marrakech	Governments, government backed entities

Table Two

1	7 October 2015	GIB-NAFIN [Mexican development bank] launch of MoU	Investors, advisors with an interest in renewable energy primarily in South American
2	2 November 2015	Delegation from the Ministry of Environment, Brasilia	Civil servants with an interest in renewable energy in South America
3	18 February 2016	Delegation of Indian solar investors: event hosted by FCO at King Charles Street	Investors in the Indian solar sector and Indian civil servants
4	18 February 2016	Delegation from the Estonian Environment Council	Policy officials in energy efficiency

Recommendations

It will be necessary for the pilot to complete some investments first to provide an opportunity to consider how we promote specific deals. Once this is happening we should also take stock of the effectiveness of events / promotion activity at regular intervals.

Actions

In this context, we recommend setting up a discussion between both members of the LLP to agree approach to promotion activity, once investments have been made.

Output Title	Renewable energy and energy efficiency measures are installed		
Output number per LF	3	Output Score	<i>n/a</i>
Risk Rating:	Major	Impact weighting (%):	0
Risk revised since last AR?	This is the first review	Impact weighting revised since last AR?	Not previously weighted

Indicator(s)	18 month Milestone	18 month Achieved
Level of installed capacity of clean energy as a result of UKCI investments (MW)(ICF KPI 17)	0	0
Electricity demand reduction (MWh) resulting from the UKCI investments (ICF KPI 16)	0	0

Key Points

- These outputs were changed from the original logframe to align with ICF KPIs which measure *actual* renewable energy capacity and electricity demand reduction achieved by ICF projects in each year (rather than *expected*).
- In the first reporting period we were not expecting to see any results in the target geographies as a result of UKCI investment activity (as we assume there to be a lag due to construction between making an investment and having new clean energy capacity installed or a reduction in demand).
- Therefore this output **is not weighted** in year one.
- As there were no investments made in the first 18 months we would expect an impact on the achievement of the original milestones for the next two review periods.
- However, if the full fund is disbursed in line with our original expectations (as per the indicative portfolio used to model expected results) then we would expect to see renewable energy capacity and demand reduction over the lifetime of the pilot to remain the same (provided our assumptions hold).

Recommendations

To consider whether these indicators are appropriate for measuring the progress of the pilot during the investment period (given that we do not expect to see any results until 2018, at the end of the investment period). For instance, we could update the current logframe to include interim milestones capturing *expected* capacity/ energy demand reduction for deals that have been made (as was the case in the original logframe).

Given the information we now have about deals UKCI are considering and the expected energy capacity these would deliver - BEIS and GIB have also agreed to update the model used to assess likely outputs of the pilot with the latest assumptions to give more accurate expectations and milestones.

D: Progress Not Captured by the Outputs

The first year and a half of the pilot included significant work by both GIB and BEIS to establish the UKCI vehicle:

- GIB transferred and recruited staff to UK Climate Investments and by January 2016 the Managing Director was joined by an Investment Director, a Vice President and two associates.
- The Investment Committee was established and met for the first time in July 2015 with delegated authority established allowing directors and staff to effectively administer the pilot.
- The UKCI Board and other governance and reporting mechanisms have all been put in place. There were six Board meetings held in the first 18 months of the pilot.
- In January 2016, UK Climate Investments presented an investment strategy to the Board based on an updated understanding of the deals available in the market. This identified opportunities in projects with commercial and industrial offtakers, off-grid solar and in larger platform companies.
- There has been significant work to ensure that the objectives of GIB and BEIS are aligned. There has been significant discussion for a number of investments to understand what is happening in each market and how the investment team can document it. At a strategic level, there was a joint session on the Theory of Change run by Ipsos MORI that examined how each investment contributed to the overall aim of transformational change.
- Spending for all ICF projects is more limited during the January - March period than the rest of the year however this was originally not thought to affect UKCI. It was discovered that UKCI does have to comply with this which has potential commercial implications for the pilot and creates financial accounting risks for BEIS. In this reporting period, BEIS and GIB teams (including finance and legal teams) scoped out the issue and explored possible technical solutions resulting in revised terms in the contract around financial management. [This issue has not yet had an effect on deal making as the pilot has not needed to disburse material amounts during the January – March period].
- During the latter part of this period significant resource on the part of the BEIS project and respective commercial and legal teams was diverted to the due diligence of the potential bidders for the purchase of the GIB and then the preferred bidder, followed by the renegotiation of the LLP Agreement which needed to be updated to reflect the change in GIB's owner.

E: VALUE FOR MONEY & FINANCIAL PERFORMANCE

BEIS employs the 'three Es' assessment of value for money (VfM): economy, efficiency and effectiveness.

Key cost drivers and performance

The key cost drivers for UK Climate Investments are the equity capital investments and remuneration to GIB:

- **Equity capital investment:** the novel application of Official Development Assistance (ODA) in commercial investments means that the UK may realise more than its initial investment (which includes associated due diligence costs). The timescale for this is expected to be in the long term.
- **Remuneration to GIB and the evaluators:** costs are driven primarily by the remuneration paid to GIB for the services it provides to UK Climate Investments, including the services of the dedicated UKCI team, GIB senior level and junior support, legal and financial management, green advisory services and investment activities. Generally, asset managers are remunerated through a fixed annual fee (in UKCI's case) the 'priority return' and in addition a share of the profits from the investment after the return of capital to the investor. A hurdle rate was negotiated (i.e. GIB does not receive any share of the returns from the investment until the investors receive their original capital plus an agreed percentage). The percentage share of profits accruing to GIB, after the hurdle rate is reached has been agreed. The fee arrangements were negotiated by BEIS and supported by written independent expert opinion that the fees agreed were market based.
- There is also a contract with a specialist monitoring and evaluation (M&E) provider. A consortium, led by Ipsos MORI including Mott-MacDonald, SQ Consult and Ernst and Young, were contracted following a competitive procurement process in December 2015 to evaluate the programme from 2016-2020.

VfM performance compared to the original VfM proposition in the business case

The original VfM proposition in the business case was based on GIB's ability to invest effectively and deliver results. The expectation at the start of the pilot was that they would make three investments during the first 18 months of the pilot and this is reflected in the milestones in the logframe. The timing of the investments affects the economy and efficiency of the pilot, but there is still the potential for UK Climate Investments to achieve value for money if investments are made. Expectations are still that UK Climate Investments will disburse all or the majority of the funds, however this will be assessed once the new owner is in place and any changes to the pilot agreed. Ideally this will have taken place before the next annual review (however the timings of the sale are outside the control of the pilot) so that any changes to expected VfM performance can be reflected.

Economy

As outlined above, GIB receives both a 'priority return' for the investment services and a share of any profits on the investments above a hurdle rate. The design of these arrangements is still an incentive to investing for UK Climate Investments and remains market competitive. However, as outlined in detail in the Outputs sections, we have concerns about GIB's ability to transact investments and therefore if there continue to be weak performance we will have weaker economy from the priority return payments.

The annual priority return payments to date are now less economic than envisaged in the business case when compared to the level of investments that have been made. The priority returns are effectively capped as they are calculated on the size of the total commitment to UK Climate Investments, £200m during the investment period.

While there is uncertainty around whether the full fund can be invested, these priority returns have the potential to represent overall value for money for the lifetime of the pilot. However, next year's annual review will need to look at whether the total will be invested and consider value if the £200m is not likely to be invested fully.

Effectiveness

It is too early in the project to make an overall assessment of the effectiveness of the pilot until some or any investments have been made. Throughout this review period BEIS had concerns about the transformational impact of the deal pipeline selected. The business case is predicated on the ability to unlock flows of private capital that transforms markets, something GIB has had a strong track record for in the UK. Significant work on this with the Investment Team and Board means that the first investments should in theory perform well on this aspect, but it will need monitoring over the next year.

Further advantages of UK Climate Investments highlighted by the business case include ability of the delivery partner to work nimbly within the private sector / investment environment and deploy a range of financial instruments (and large amounts of capital); until the first investments are made it is hard to assess the ability of UK Climate Investments to meet these expectations.

Similarly, uncertainty over performance of processes like activities under 'building network' indicator makes it difficult to assess the value of these outputs until transactions are completed.

Overall, until the investments are made, the benefits as envisaged in the business case are at risk.

Efficiency

One area where the pilot is deviating from expectation is the scale of the project management needed on the BEIS side of the project. The business case highlights that a core reason for choosing this delivery model was to minimise need for intensive management from the BEIS ICF team. In both the set up period and first 18 months of the pilot, there has been significantly more resource intensive than expected requiring at least one Grade 7 FTE, half an HEO FTE, a commercial advisor (as the BEIS Investment Committee member) and significant Senior Civil Service time, plus external advisory services and significant input from BEIS legal and finance teams.

It is worth noting that part of this resource is attributable to the sale of the GIB and the need to negotiate new terms with the winning bidder (which has been exacerbated by several delays to the overall sale). In the period covered by the next Review, the resource requirements are unlikely to decrease given that the sale process is likely to continue. After the sale, resource needs are expected to reduce. Resourcing should therefore be monitored closely.

Assessment of whether the programme continues to represent value for money

The premise in the original value for money proposition, that the pilot has the potential to deliver strong climate results, and development results and ability to engage with the private sector, will only be proven once there are investments.

It is also too early to assess whether the delays will affect the final size and characteristics of the UK

Climate Investments portfolio but if the delays continue to the end of the second year of the investment period it will make it more likely that UK Climate Investments cannot disburse the full fund and build a portfolio of transformational investments in line with original expectations, and therefore that UK Climate Investments does not represent value for money as envisaged. It is worth noting that other than the priority return / management fees and transactions costs already occurred, any funds not invested via UK Climate Investments can be spent elsewhere in the International Climate Finance portfolio on other projects to ensure value for money for the tax payer.

We recommend this likelihood is assessed and the possible impact of VfM analysed in the next reporting period.

Quality of financial management

The quality of financial management for UK Climate Investments has been high. The legal agreements for the LLP set out the requirements.

The GIB finance team have been proactive in clarifying their understanding of BEIS's requirements, and providing the information that is needed in the required format.

The accounting for the LLP is carried out by the GIB finance department.

The audited accounts of the LLP were submitted on time following the end of the financial year.

Date of last narrative financial report	June 2016
Date of last audited annual statement	June 2016

F: RISK

Overall risk rating: Major

Our current assessment is that, with the progress update presented in this annual review, it is considered that the pilot at the end of this period is at risk of not being able to achieve its intended level and type of investment within the timeframe. As one of the ICF's largest projects this is also a portfolio level risk.

Overview of programme risk

In the business case the following were identified as key risks to the programme:

- As an institution, the GIB had no international experience of investing development finance.
- Despite their strong 'green' credentials, there is a risk that they will deliver investments that are less transformational than BEIS is targeting (i.e. market leading, pioneer investments which ensure strong additionality).
- The GIB did not have a strong track record in energy efficiency in its investments in the UK which may affect its ability to make this type of investment through UK Climate Investments, and due to the tension between ODA concessionality requirements for loans and the commercial focus of the pilot, we are concerned they may not be able to deliver on their business plan in terms of energy efficiency.
- Risk of future strategic misalignment: at the time the project was approved the GIB wanted to attract private capital into the bank; whereas our priority was to ensure the pilot would continue to operate as envisaged under such circumstances.
- Risk of reputational damage to BEIS and HMG given public concern over fee and profit share arrangements.

BEIS has put significant additional resource onto the pilot to proactively manage the relationship with senior management and the investment team.

The risks have been managed in year one by:

- Weekly meetings with the UK Climate Investments team to keep abreast of changes to the pilot and the progress of the investment team.
- Engagement with the UK Climate Investment Board through quarterly board meetings and ad-hoc discussions to address issues including risk appetite and transformational change
- Utilising a project board of senior BEIS expert advisors, commercial, financial, procurement, economists and legal, who have reviewed the risk register to the project board every 4 months.

Changes to risk profile of the pilot

Sale of the GIB

A considerable change to the overall risk context since the design of the pilot was the sale of GIB. We considered two main risks which were legal and strategic risks of new ownership. Other risks were quickly established to be low or mitigatable.

These risks have been mitigated by:

- Conducting necessary due diligence of the bidders and assurances provided by the potential new owner.
- Agreeing changes to the pilot's legal agreement in the first few months of the second year of the pilot to provide assurances under new ownership. Key changes include providing further controls on future change of terms, ensuring UK Government visibility through maintaining UKCI and UK Government branding and continuing management and governance of the pilot in line with our accounting and propriety objectives. On the latter, we have ensured that we will continue have sufficient oversight of the pilot in line with the Government's 'Managing Public Money' framework.

Macroeconomic risks

Finally, the risk that policy and regulatory changes in target geographies may undermine investments made under the pilot in our selected countries is increasingly a concern. Since the market assessment was undertaken in early 2015, the African geographies' economies have slowed down considerably. The UK Climate Investments team have actively adapted to these circumstances. However, there are ongoing challenges, for example, limited investments can be made in South Africa until Round 4 of the REIPPP closes.

Outstanding actions from risk assessment

The remaining risks and actions are:

- Policy and regulatory changes may undermine investments made by the pilot. The UK Climate Investments team have identified a range of market constraints in Africa and are considering how to approach the African market in a different manner. As part of the renegotiated contract both the tier one and tier two list of African geographies give UKCI more flexibility to find appropriate deals.
- Recruitment of a full UKCI project team takes longer than anticipated.
- Disbursement of funds - UKCI investment team fail to convert deals into completed investments.
- GIB investments distort the market and crowds out the private sector or are not sufficiently transformational.

To address these risks, we have developed a joint risk matrix with the GIB risk team - we expect to turn this into an action plan with the new owner of the GIB and work closely with them to put systems in place to manage these risks.

G: COMMERCIAL CONSIDERATIONS

Delivery against planned timeframe

The programme is currently not delivering against the expected timeframe.

The difference between expected and actual progress we consider results from a combination of optimism bias, design issues, issues with the UK Climate Investments and GIB management processes, in addition to the sale of GIB was not foreseen when the business case was produced.

Given the progress now starting to be made on the pipeline, and following the completion of the privatisation, BEIS expects the LLP to make some investments by the end of the second reporting period. However, cumulative investments for this second period are likely to be lower than the milestone originally set. Therefore we expect there to be a backloading of investment towards the end of the investment period and potentially a lower rate of disbursement overall than expected.

As part of the sale of the GIB the length of the investment period has been extended by six months (until the end of 2018) making the investment period three and half years instead of three years which gives UKCI more time to make investments.

We have the option of extending the investment period by one or two years with the agreement of both sides of the LLP and extending the commitment period correspondingly. However, if there is no improvement in performance and UK Climate Investments does not invest in a range of transformational projects these extensions are unlikely to be implemented.

Performance of partnership

As discussed in the risk section, there are a number of concerns at this stage around the performance of the pilot. As limited liability partners in UK Climate Investments there have been some differences in the strategic approach to UK Climate Investments that have been apparent in discussions by the UK Climate Investments Board and by through discussions around risk appetite for UK Climate Investments. Over the next reporting period we will work closely with the new owners of GIB to improve understanding and shared objectives.

Asset monitoring and control

As of the end of this reporting period there are no assets under management by the LLP.

H: MONITORING & EVALUATION

Evidence and evaluation

The evidence compiled to assess progress in the Annual Review consisted of:

- Ipsos MORI Phase one scoping report
- Board papers and internal board effectiveness survey
- Investment committee papers
- Google data analytics of website visit
- UKCI investment team records
- Discussions with BEIS project and commercial teams and UKCI investment team

Summary of evaluation progress and plans.

In early 2016 Ipsos MORI in partnership with Mott MacDonald, Ernst & Young and SQ Consult, were contracted to evaluate the UK Climate Investments Pilot following a competitive tendering process.

The consortium will take theory based evaluation approach which utilises contribution analysis and employs varied data sources to triangulate findings. They are utilising a real-time approach, sharing feedback on findings as they emerge to help improve delivery.

Monitoring progress throughout the review period

As part of the inception activities the consortium facilitated a workshop between BEIS and GIB in April 2016 where we participated in a visioning exercise of what success of the pilot would look like in 2018. As a result of the discussions Ipsos MORI undertook a revision of the Theory of Change (included as part of the Inception Report which will be published alongside the annual review) involved some minor refinements of what was in the original business case, which was agreed by both parts of the LLP in September 2016.

As a result, the logframe was revised between May and September 2016 to ensure it was in line with the updated theory of change.

Monitoring

Other than the 6 monthly and annual reporting on the milestones in the logframe, the pilot does not currently have a formal plan for more granular monitoring arrangements. Of the three sets of outputs only Output 1 is monitored regularly, by way of BEIS participation in the Investment process (weekly pipeline call, having a BEIS member of the Investment Committee, preparatory meetings for the Investment Committee).

As discussed in the section on Output 2 - we did not have regular discussions for promotion activity, which, once investments have been made could benefit from more regular monitoring and lessons learned.

At the outcome level, we also have oversight of Outcome 4 (*'UKCI pilot improves risk perception, demonstrates feasibility of renewable and energy efficiency investments'*) – rate of return and speed of implementation (the time taken between deal origination and completion) – through the investment process. We expect there to be a lag for other outcomes (climate and development outcomes, and reduction in cost of capital) between having made investments and seeing the results and we will collect

these results bi-annually.

KPI 15 Rating

There is currently a methodology for transformational impact at both the individual project (investment) level and the pilot level (below). We have provided our assessment of current progress for the pilot as a whole during year one of KPI 15 using the following scoring:

0	Transformation judged unlikely
1	No evidence yet available - too soon to revise assessment in business case
2	Some early evidence suggests Transformation likely
3	Tentative evidence of change – transformation judged likely
4	Clear evidence of change - transformation judged very likely

Our assessment is that the pilot scores a **1** - as there is insufficient evidence available due to the lack of investments. Further assessment of each transformational change criteria is found below.

Evidence and evaluation

The external evaluation provider will be assessing progress against all KPIs including transformational change by collecting and analysing data at the project level.

Each investment will be assessed using the following methodology for transformational change to give an overall assessment of transformational change potential for the project:

- *Political will and local ownership*: need for the change is agreed locally and the process is locally owned. For widespread changes, notably changes to the patterns of development, this will require high level political buy-in and broader support from across society;
- *Capacity and capability can be increased*: countries and communities have the capacities and capabilities necessary to bring the change about;
- *Innovation*: innovative technologies are piloted, with the potential to demonstrate new ways of doing things, which could lead to wider and sustained change;
- *Evidence of effectiveness is shared*: approaches which have proved successful in one location are made widely available and lessons on their usefulness are credible and shared widely;
- *Leverage*: create incentives for others to act;
- *Replicable*: the costs of climate action are reduced to the point that acting on climate is a sensible decision for commercial firms and private individuals. These cost reductions may need to be steep enough to overcome behavioural inertia;
- *At scale*: interventions (such as national, sectorial or regional programmes) that have sufficient reach to achieve institutional and policy reform, or drive down costs of technology deployment
- *Sustainable*: change is likely to be sustained once ICF support ends.

Once an investment is made the evaluation provider will baseline the data for each project and monitor

investments over the investment period. Once investments have been made we expect this process to begin.

Delays to the pilot and privatisation of the GIB have meant that the Ipsos Mori Consortium has not been able to deliver the workplan they had envisaged including the publication of the Inception Report which will be published alongside this review. We will therefore need to review and potentially rationalise the plans for the external evaluation to ensure they are appropriate in scope and timescales to how we think the pilot will progress.

In terms of risks, whilst the UKCI at present is still confident of meeting all targets, it could be inferred that the lack of any investments during this period increases the risk of UKCI failing to fully meet its transformational potential and this merits ongoing close monitoring.

Recommendations

1. To improve monitoring, we will discuss with UK Climate investments having a monitoring plan and potentially increasing the number of results collections and discussions around deal origination and promotion activity, incorporating 'lessons learned' activities throughout the year.
2. Once investments have been made, there should be a full review of this methodology's applicability and effectiveness once an investment has been made.
3. As a result of the delays to the pilot, and therefore evaluation activity, BEIS and Ipsos MORI need to review, and potentially rationalise the plans for the external evaluation. This will ensure they are appropriate in scope and timescales to how we think the pilot will progress and that we can extract maximum value in terms of learning from the contract.