
THE JUST TRANSITION TRANSACTION:

A DEVELOPING COUNTRY COAL POWER
RETIREMENT MECHANISM

PRESENTATION TO NEDLAC

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BACKGROUND AND SUMMARY OF THE PROBLEM STATEMENT

THE JUST TRANSITION TRANSACTION: A DEVELOPING COUNTRY COAL POWER RETIREMENT MECHANISM

- Conclusive scientific evidence shows that *accelerating* the Just Transition in the power sector is highly desirable for SA:
 - Our economy and power sector is highly carbon intensive
 - We need to avoid catastrophic climate change and the associated near and long term severe economic impact on SA
 - An accelerated, renewables dominated power system expansion is the **least cost** and **fastest** strategy to restore security of supply and decarbonise.
 - This pathway will create **more** investment and **more** sustained jobs and provide a **greater** economic stimulus than any other power sector option available to SA.
- The scale of grid and clean energy investment required over the next 10 years is between R750bn – R1trillion. This will primarily have to be financed from the capital markets.
- However, Eskom's financial problems and stranded debt means that the country currently cannot finance this investment programme:
 - Eskom's sub investment ("junk") credit rating means it is an unviable counterparty for financing new grid or generation investments, or sign IPP power purchase agreements, without government guarantees.
 - And, our severe fiscal constraints mean that National Treasury has reached the end of its capacity to provide more sovereign guarantees.

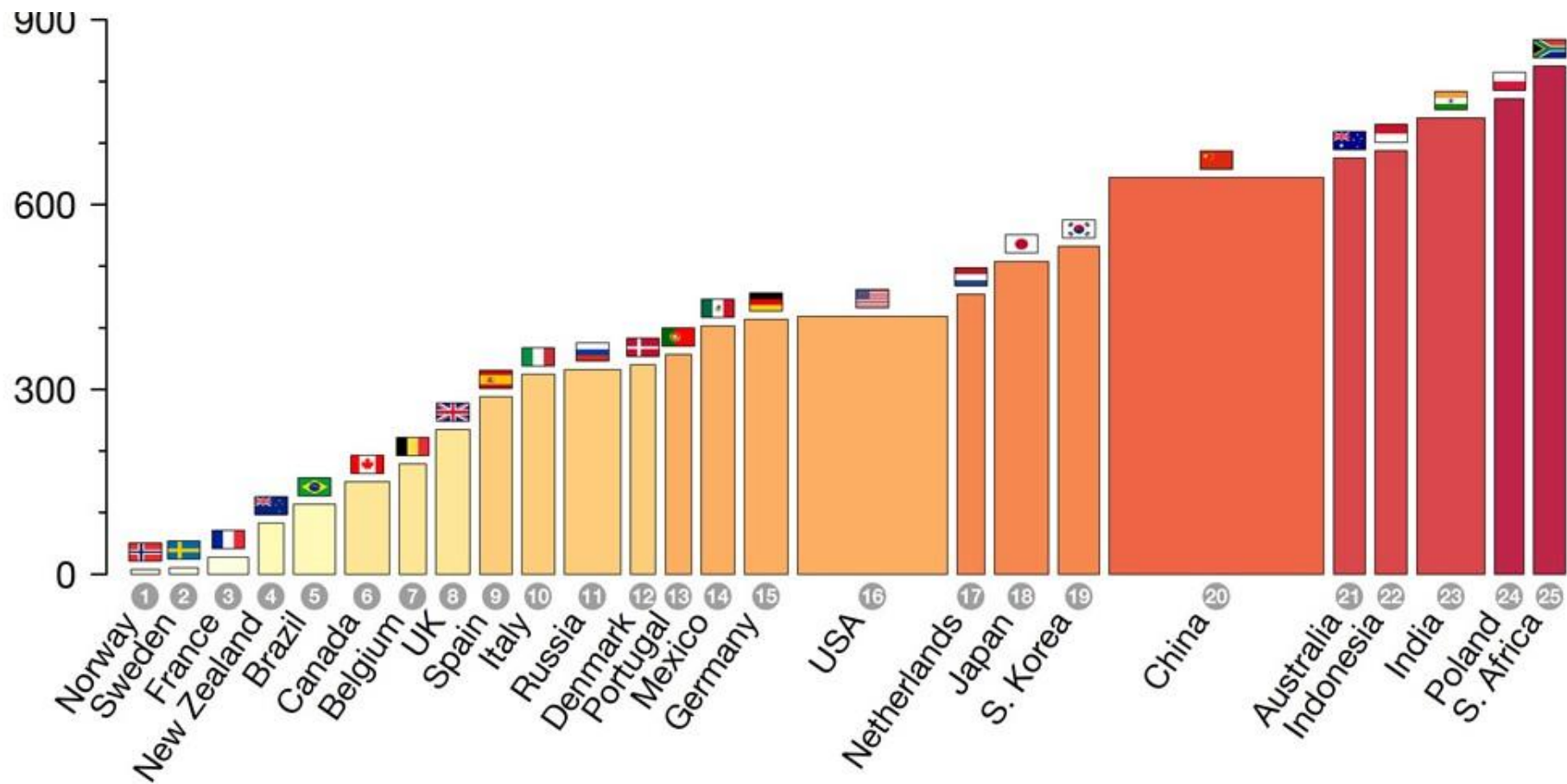


BACKGROUND THE SUMMARY OF PROBLEM STATEMENT (2)

- Socio-economic challenges with decarbonisation
 - SA already has catastrophic unemployment levels (34 – 44%, depending on definition)
 - Need for transition support for coal workers, communities and economy in Mpumalanga
 - A “social licence” for decarbonisation will require a credible, funded, just transition plan
- Meridian’s Just Transition Transaction (JTT) proposals and Eskom’s JETT proposals are complimentary approaches that address different aspects of these challenges.



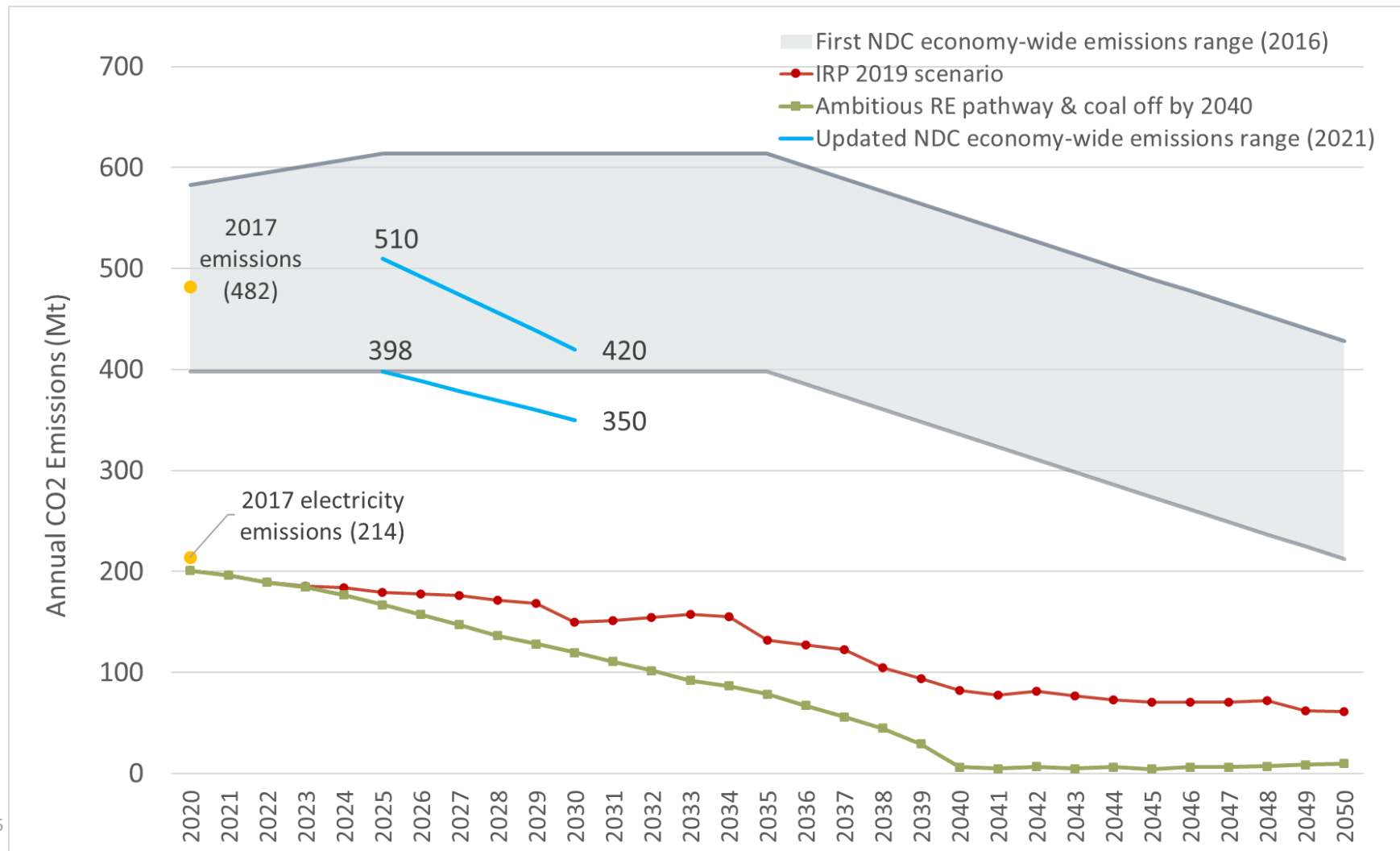
SOUTH AFRICAN ELECTRICITY IS THE MOST CARBON INTENSIVE IN THE WORLD



Source, Carbon Brief, 2018



SA'S NEW NDC REQUIRES ACCELERATED ELECTRICITY DECARBONISATION



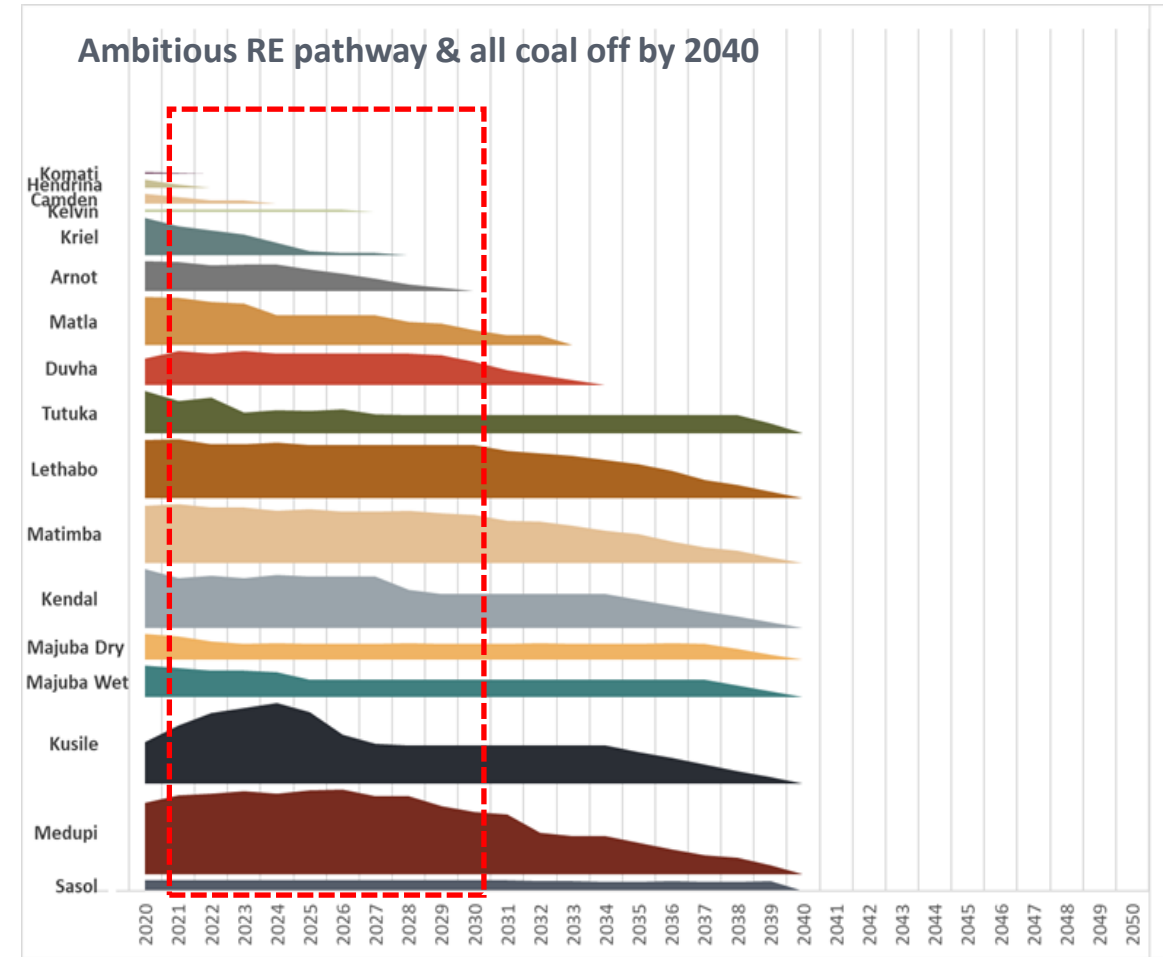
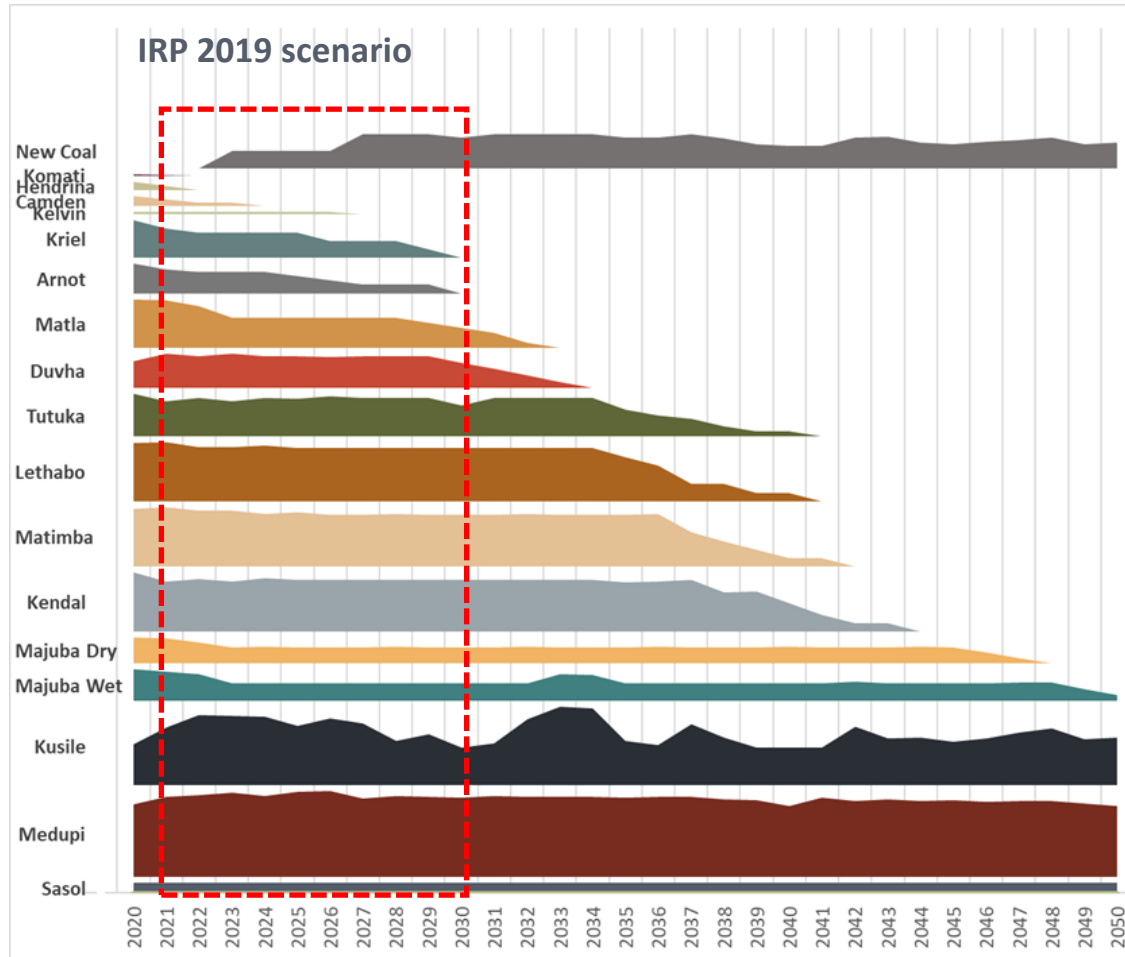
See:

<https://meridianeconomics.co.za/our-work/briefing-note-2021-10-what-does-south-africas-updated-nationally-determined-contribution-imply-for-its-coal-fleet/>



REDUCED COAL PLANT OPERATION AND RETIREMENT TO MEET THE NDC

THE IRP 2019 IS NOW WELL OUT OF DATE



ESKOM'S DEBT CRISIS POSES ENORMOUS RISK TO THE ECONOMY, AND THE CURRENT TURNAROUND STRATEGY IS INSUFFICIENT

- Eskom has seen escalating operational and capital expenses combined with a steady decline in electricity sales over the past few years. Increasing tariffs (though still not cost-reflective) is driving grid defection, resulting in classic 'utility death spiral'.
- Approximately R200bn of Eskom's ~R400bn net debt is not serviceable from available revenues.
- This has compelled National Treasury to commit to large bailouts for Eskom: R56bn for FY2021, and between R21bn and R33bn per year for the next five years, targeted at enabling the utility to meet its short-term debt service costs.
- However, the current drip-feeding strategy is not sufficient to enable Eskom to reach sustainable debt levels:
 - This is due both to the size of debt burden and nature of compounding debt: the longer the timeframe until a full debt solution is provided (i.e. spreading debt relief over several years), the larger Eskom's debt hole grows and the larger the total fiscal package becomes. Current interventions will not fill this hole.
 - A large-scale, immediate additional intervention will be needed in order to maintain Eskom's solvency.
- Eskom faces major refinancing issues: a weak credit rating means the utility needs to refinance long term coal assets with increasingly short-term, more expensive debt, compounding the crisis. R150bn of debt needs to be refinanced in the next five years.

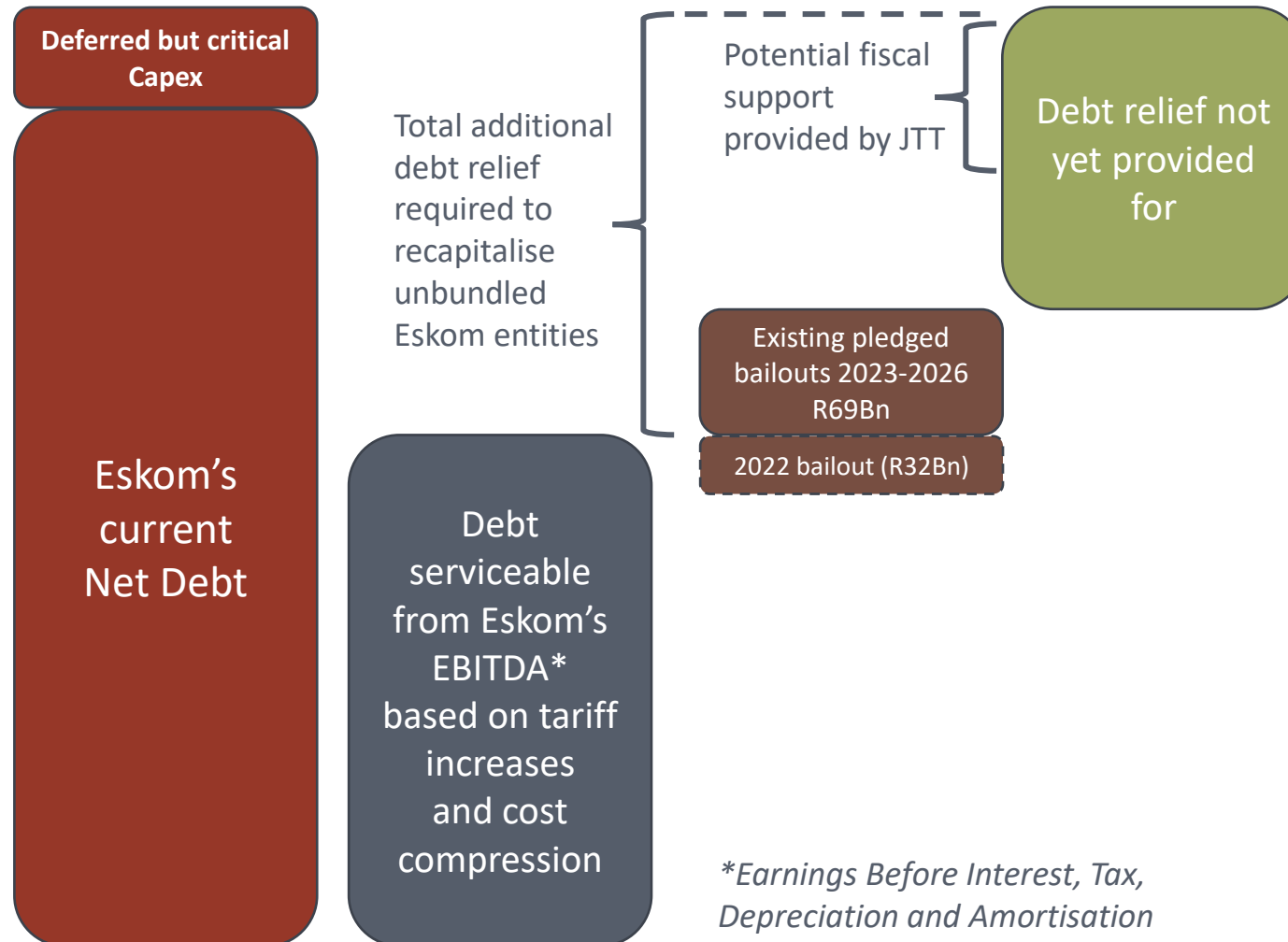


FURTHER, ESKOM'S CRISIS IS A ROADBLOCK TO AN ACCELERATED RENEWABLES PROGRAMME

- Eskom's credit rating weakness has implications far beyond the financial health of Eskom itself.
- Given its central role in the power sector and financial counterparty to most of the sector's investments, Eskom's predicament will increase the cost of the critical infrastructure required to provide South Africa with adequate, reliable and affordable power.
- Without financially viable and independent Eskom entities that can act as credible power purchase counterparties, raise capital and rapidly invest in new transmission and distribution infrastructure, the required accelerated renewables programme simply will not happen:
 - Financing critical grid network expansion and strengthening will remain difficult, expensive and slow.
 - Eskom will remain an unviable counterparty for Independent Power Producers (IPPs) without sovereign guarantees, which are not endless (we will run up against these limits soon).
- This presentation emphasises the need for a critical enabling intervention to create the circumstances that will allow this proposal and other green financing initiatives in the power sector (all renewable energy and associated infrastructure) to proceed at the speed, scale and (low) financing cost required for South Africa to achieve a Paris-aligned just energy transition.



AN IMMEDIATE, ADDITIONAL INTERVENTION IS REQUIRED FOR ESKOM TO REMAIN SOLVENT



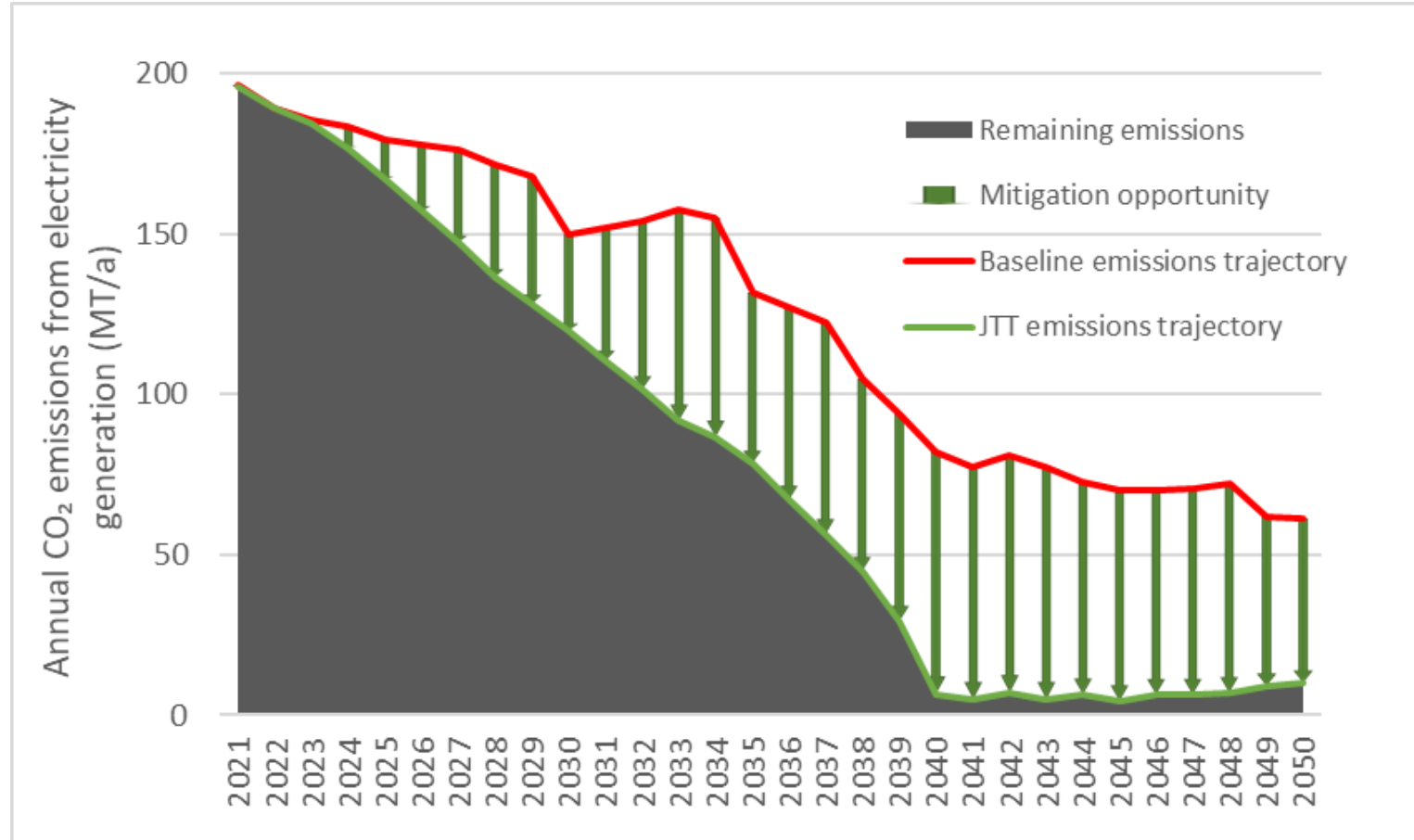
THE JTT AS A MECHANISM TO UNLOCK PARIS-ALIGNED POWER SECTOR DECARBONIZATION IN SOUTH AFRICA

- The Just Transition Transaction (JTT) is a prototype, multi-lateral, 'coal retirement' mechanism. It aims to secure an accelerated, Paris-aligned, affordable, and just energy transition for South Africa's power sector and affected communities.
- As the transaction counterparty, the SA government will support the coal fleet phase down by creating an enabling policy and regulatory environment, committing to no further coal for power in SA, and committing to an ambitious emissions reduction trajectory.
- The JTT concessional value will be used to support National Treasury (create fiscal space) to enable:
 - Catalytic capitalisation of an SA Just Transition Fund
 - Recapitalisation of unbundling Eskom entities to enable market financing of large scale RE and grid roll out.

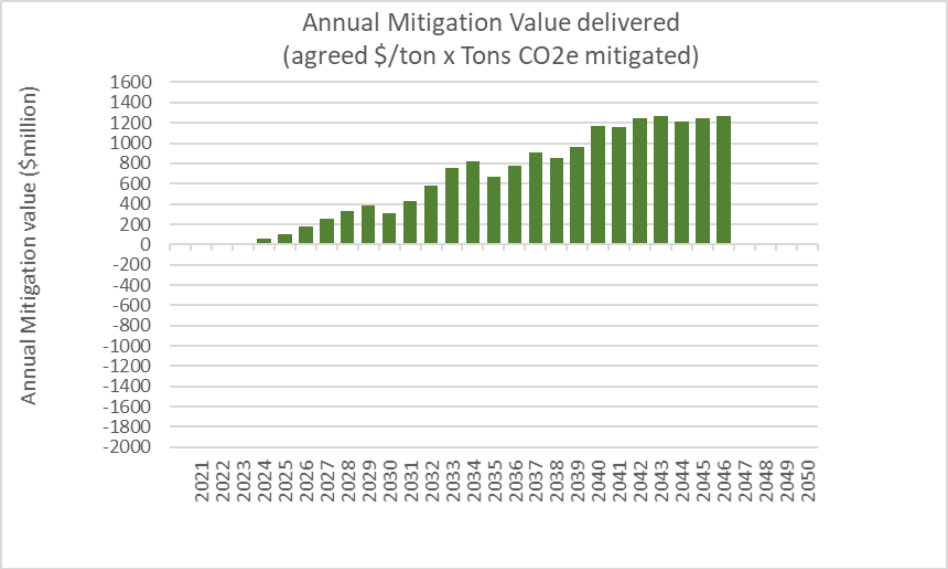
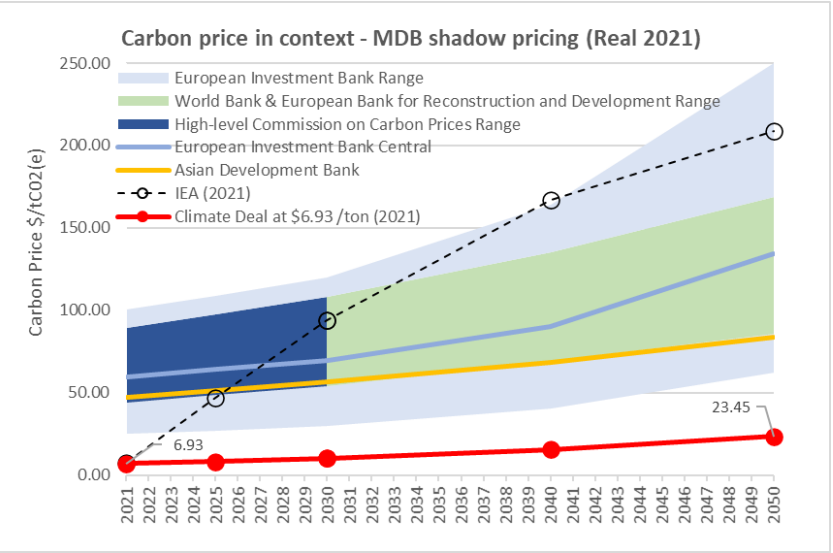
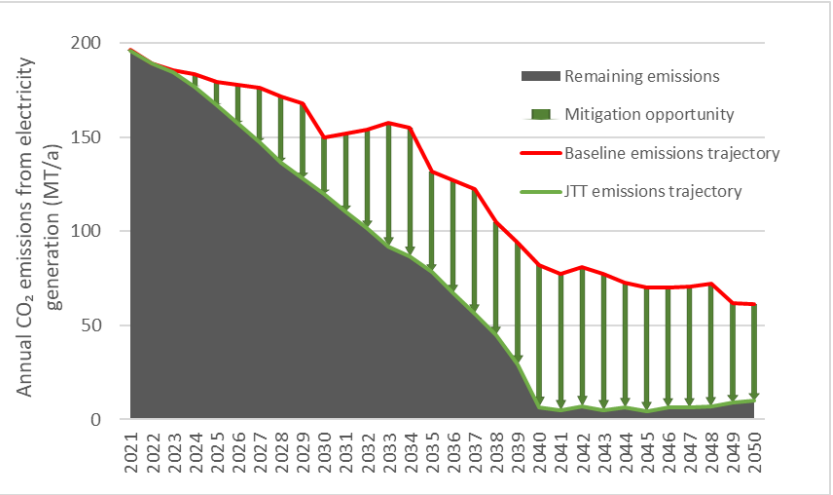


MITIGATION OPPORTUNITY

SOUTH AFRICA CAN DELIVER CLOSE TO 1.5 GT OF EMISSIONS REDUCTIONS OVER THE NEXT 20-30 YEARS



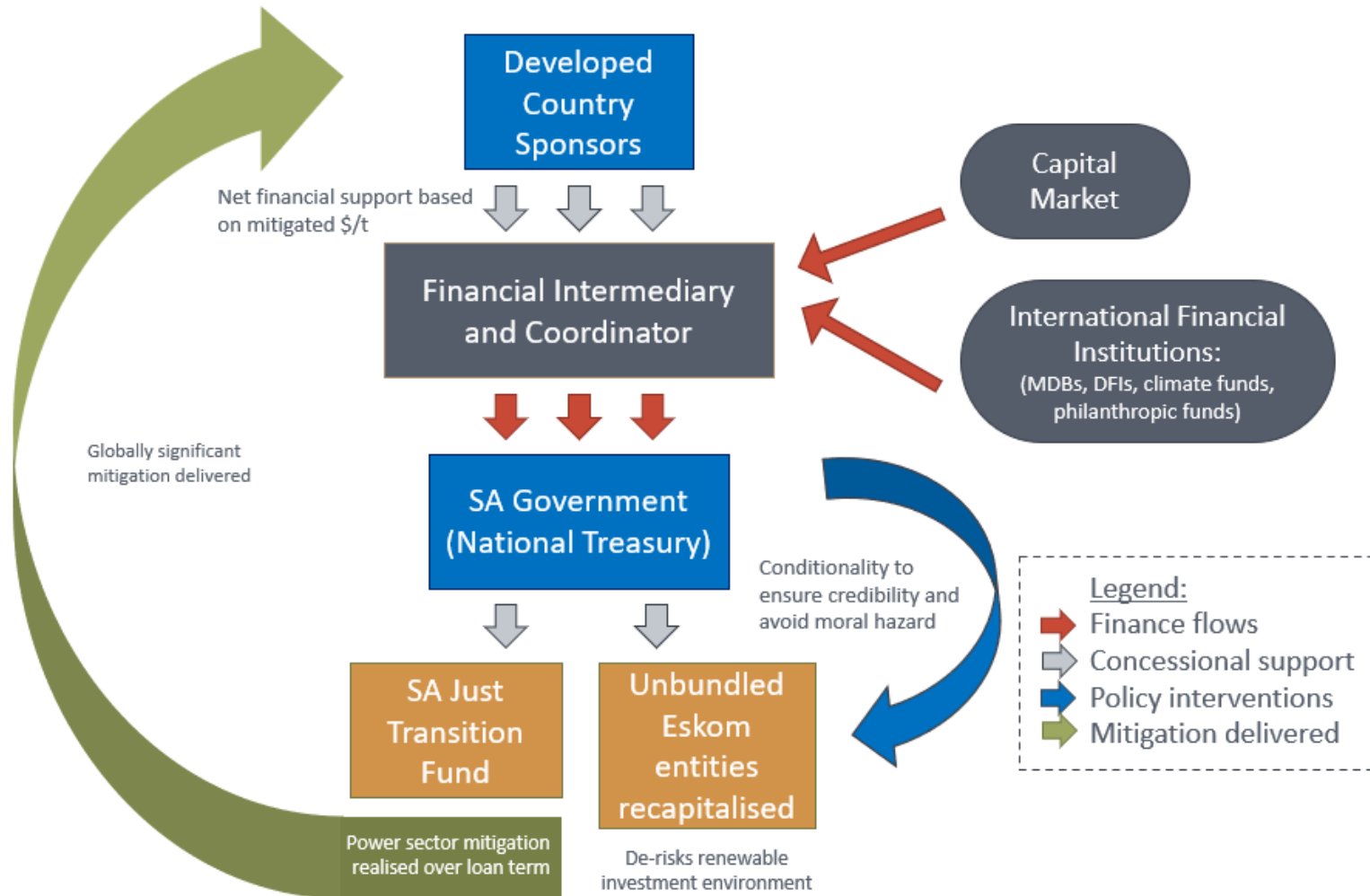
THIS TRANSLATES TO SUBSTANTIAL MITIGATION VALUE



Example: approximately \$7/t yields R100bn
(or about \$7bn) in concessional value (net
present value)

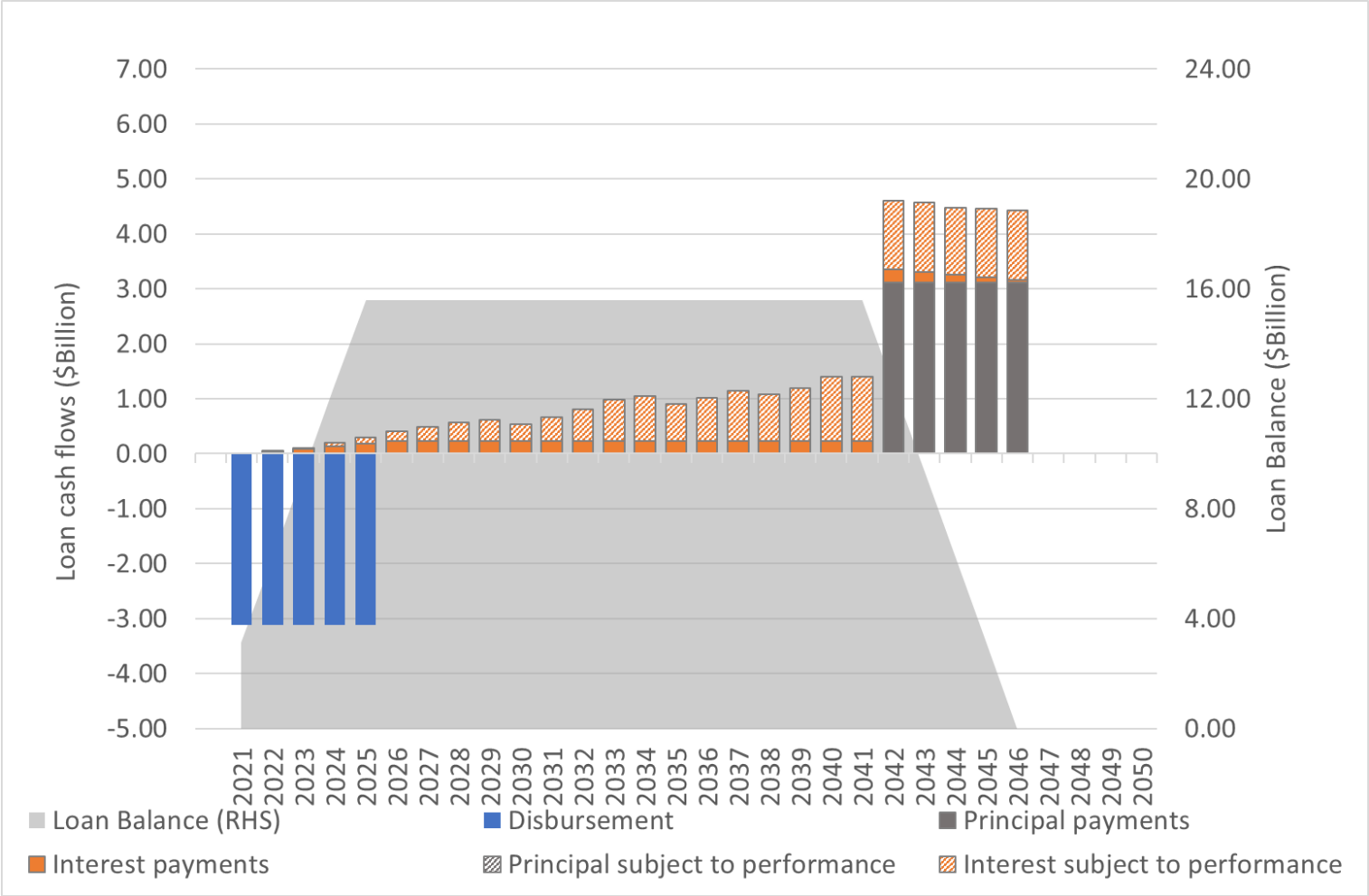


JTT INSTITUTIONAL STRUCTURE AND FLOW OF FUNDS



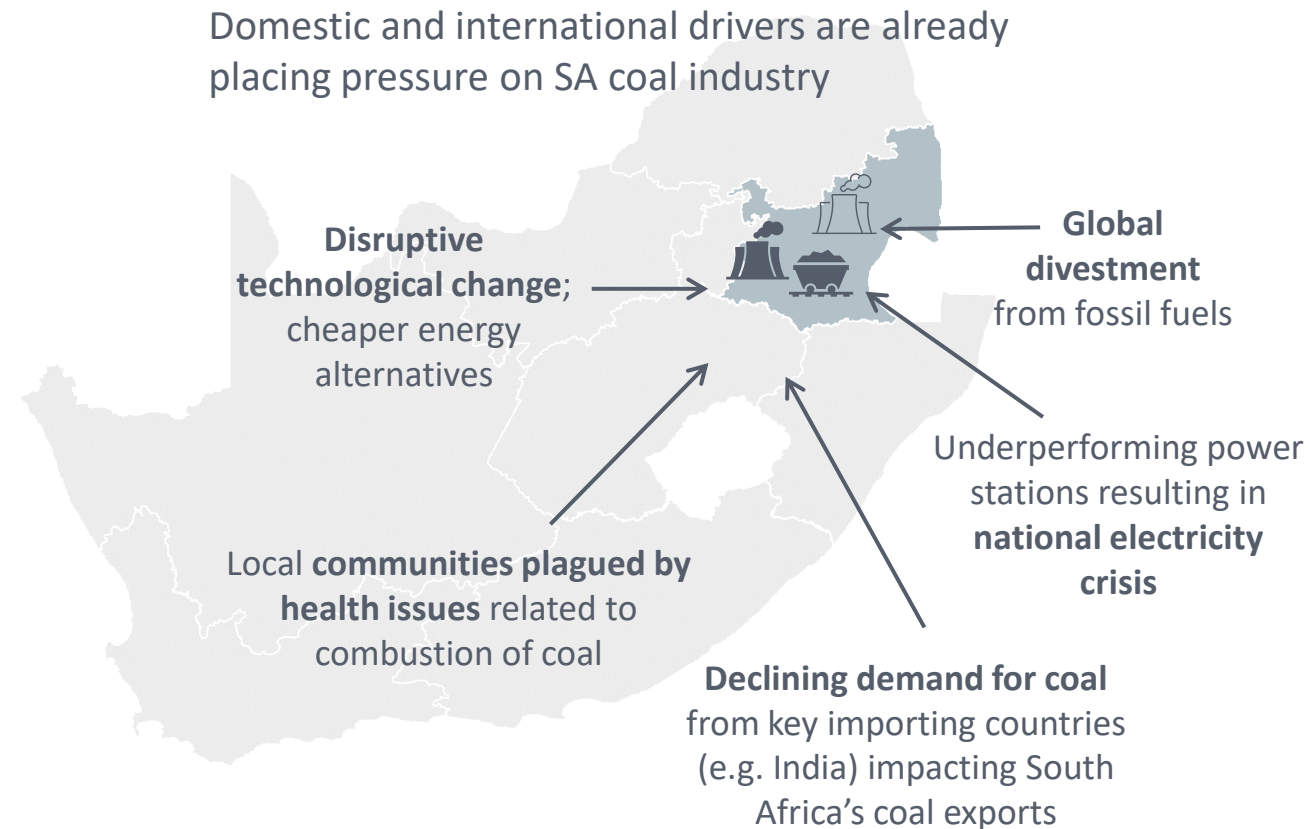
MARKET RATE BULLET LOAN WITH MITIGATION-SCULPTED INTEREST PAYMENTS

Requires a \$16Bn facility



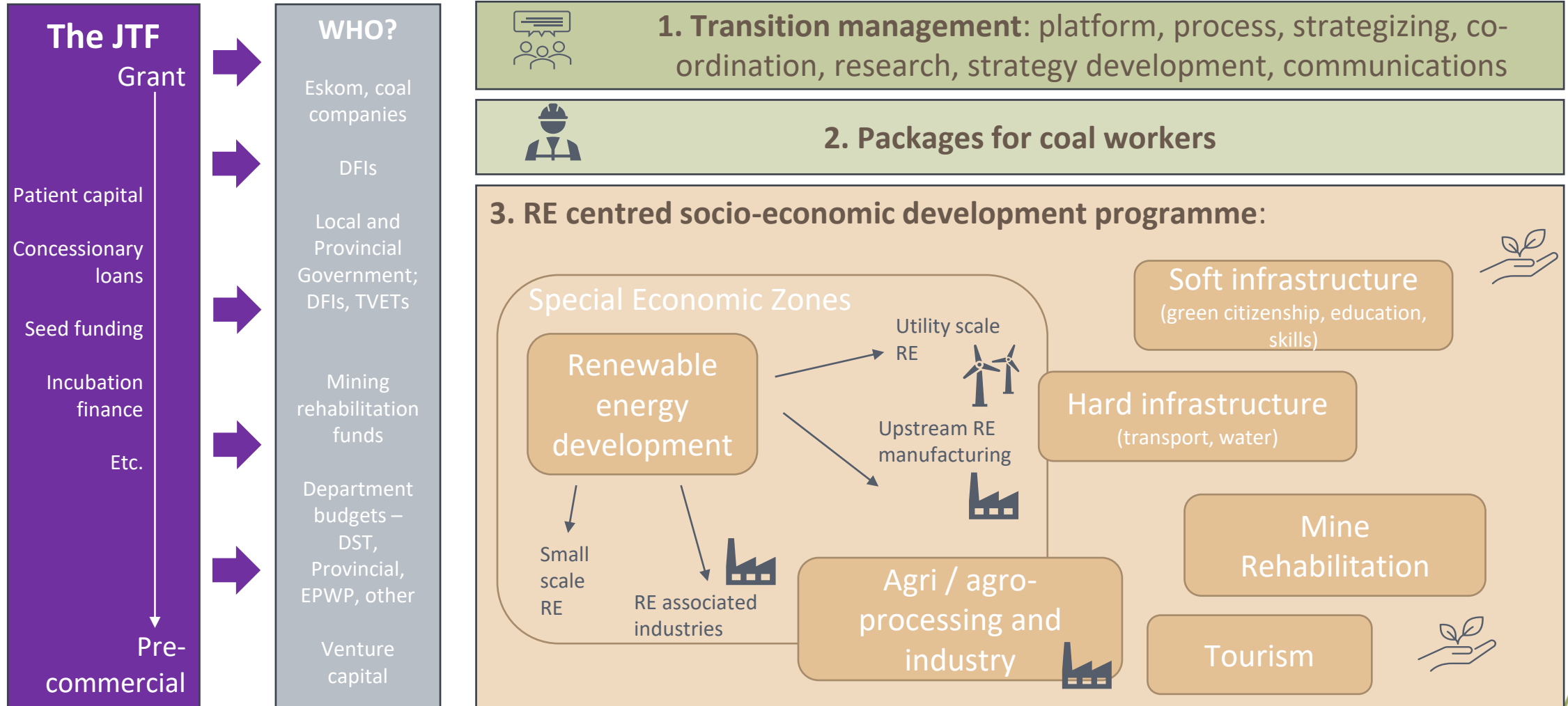
A CREDIBLE, WELL RESOURCED JUST TRANSITION PLAN WILL BE FUNDAMENTAL TO SOUTH AFRICA'S TRANSITION EFFORTS

- South Africa's unemployment levels have recently hit their highest on record. There is a dire need for job creation and economic stimulus across all sectors.
- In the context of the power sector, the negative impacts of coal decline will be concentrated in Mpumalanga Province (hosts 12 coal-fired power stations and a large share of South Africa's coal mines)
- 4 municipalities are particularly at risk due to their high economic dependence on coal production, these municipalities already experience high levels of poverty and unemployment.
- Strategic planning/mapping is already underway in SA under the Just Energy Transition framework, but a credible, adequately-resourced plan is yet to be put in place. This is a major risk for the coal region, and beyond.



THE JTT CAPITALISES A JUST TRANSITION FUND, TARGETED AT THREE JT FOCUS AREAS

- 1 The JTT provides grant finance, catalysing other financing sources.
- 2 Different sources of finance are available depending on the type of project.
- 3 A Just Transition programme in Mpumalanga will involve public and commercial projects and programmes in various sectors to transition coal workers, enable economic and social development and attract investment to the region.



THE MERIDIAN PROPOSED JTT AND ESKOM'S PROPOSED JETT ARE COMPLIMENTARY PROPOSALS

- The JTT is a government level transaction, while the JETT is primarily between Eskom and DFIs (probably requires government guarantees)
- The JETT addresses the *immediate* challenge of making progress with grid expansion and coal plant repurposing and repowering
 - But does so within the constraints of the impaired balance sheet and vertical monopoly structure
- The JTT unlocks the sustained capital market financing of a much larger power sector investment programme by:
 - supporting government with completing the power sector reforms (existing policy), recapitalising the balance sheets of the unbundling Eskom entities and capitalising a Just Transition Fund
- The JETT focusses on financing individual projects (“inputs”)
- The JTT is focussed on ultimate outcomes (measured decarbonisation; and justice in the transition) by supporting sector reforms and JT funding that will crowd in larger volumes of long-term third-party finance
- The JTT provides the *forward visibility* required to achieve large scale localisation of the RE and grid value chains, and green industrialisation
- Justice in the transition
 - The JETT supports important *near term*, but modest, socioeconomic outcomes around the closing power stations
 - JTT provides fiscal support for capitalising a Just Transition Fund for the region, thereby supporting the achievement of a broader “social licence” for the accelerated transition
- Mitigation: The JTT supports the achievement of the lower bounds of South Africa’s NDCs
- Conclusion: A single framework for achieving both the initial JETT and more ambitious JTT should be established with the counterparties.



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