

## FINANCIAL MARKETS SUSTAINABILITY ENERGY EFFICIENCY FINANCE

# Energy Efficiency for SMEs

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### Why is energy efficiency important for small businesses (SMEs)?

Rising energy costs can lead to higher production and distribution costs for businesses, eroding long-term competitiveness and profitability. SMEs are particularly vulnerable due to limited resources and tight operating margins. Cutting energy waste can be a quick way for them to reduce costs, but they often lack the knowledge, financing and dedicated personnel needed to identify efficiency opportunities and implement improvements. Potential savings can be unlocked through simple measures, such as retrofitting or replacing old equipment with new technologies, and including energy savings targets into long-term performance strategies. Local FIs can help SMEs finance energy efficiency projects through investments that often pay for themselves and also offer a healthy return over time.

### What do projects involve?

Energy efficiency projects typically include improvements to production lines, energy generation processes, and regulation of energy use in the workplace:

- **Energy efficiency in production process**
  - i) Replacing obsolete and energy inefficient production lines
  - ii) Waste heat recovery
  - iii) Improved regulation and control of the production process
- **Efficient generation of energy inputs**
  - i) Combined heat and power production (CHP), also known as cogeneration
  - ii) High efficiency boilers and decentralization of heat production
  - iii) Improved insulation of heat/steam pipes
  - iv) Fuel switching and/or renewable energy utilization
- **Efficient use of energy in the workplace**
  - i) Improved regulation of indoor temperature
  - ii) Improved thermal insulation of buildings
  - iii) High efficiency lighting systems

### What are the opportunities for financial institutions (FIs)?

- **Large potential market:** Energy efficient technologies are tried-and-tested and widely available on the market, making projects broadly attractive to SME clients and other industries in the FI's portfolio.
- **Improved client cash flow:** Cash flow from implementation of efficiency measures often completely or partially covers necessary financing costs, allowing investments to pay for

themselves over time. Usually most of an SME's energy consumption is regarded as a fixed cost, so cash flow resulting from energy savings is typically less risky than the core business of the SME.

- **Increased debt capacity:** Cash flow generated by energy savings, together with the company's enhanced competitive position in the market, may increase a client's credit quality and enable the SME to access new debt to finance investment necessary for further growth.
- **Value-added services to clients:** FIs can incorporate energy efficiency products into SME lending practices to improve the competitiveness and profitability of existing SME clients; this can also result in new client growth and expanded market reach for the FI.
- **Market differentiation:** FIs that develop products featuring energy efficiency technologies are likely to benefit from "first-mover" advantages in the market; they will also enjoy reputational benefits with policy-makers, shareholders, and customers who support sustainability practices in business.

### Sample SME Project: Heating System Upgrades for Construction Company, Czech Republic

<b>Purpose</b>	Replacement of old and inefficient coal-fired heating system with new, decentralized natural gas-fired system
<b>FI</b>	IFC partner bank, Czech Republic
<b>Borrower</b>	Established manufacturer of construction materials
<b>IFC role</b>	Risk sharing and technical assistance
<b>Project size</b>	US\$ 150,000
<b>Loan amount</b>	US\$ 133,000
<b>Loan maturity</b>	4 years
<b>Simple payback</b>	6 years
<b>Environmental impact</b>	713 tons of carbon dioxide annually





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**What are the key issues—questions to ask?**

- **What is the SME borrower’s knowledge of energy efficiency?** Since energy efficiency improvements are not usually the primary activity of SMEs, do they possess the know-how and skills necessary to operate new equipment?
- **What are the SME’s key objectives?** Are energy efficiency upgrades focused on generating energy savings and increased cash flow for the SME, or improvements in the quality and reliability of the production process? If efficiency upgrades focus on process improvements, the borrower should be aware that energy savings and increased cash flow may not be immediate, and are often realized over time.
- **Is local technical expertise available?** Is an energy audit necessary to identify specific energy saving measures for the SME borrower? Are local specialists available to assist with this technical aspect of projects?

**How can IFC help?**

IFC, supported by world class experts, has ten years of experience working with partner FIs in the area of sustainable energy finance. IFC’s offering includes:

- **Partnership:** IFC partners with selected client FIs to develop approaches to take advantage of energy efficiency and renewable energy market opportunities.
- **Product design and structuring:** IFC can provide sector expertise to FIs to assist in product design and financial structuring.
- **Financial offering:** IFC offers flexible finance options to FIs that develop sustainable energy lending portfolios, including medium to long term credit lines and guarantees. IFC may also offer special financial enhancements such as partial first loss coverage on portfolios and performance incentives.
- **Technical assistance:** IFC may provide customized technical assistance, including advisors, market analysis, feasibility studies, energy savings calculations, project preparation assistance, audits, engineering support, and capacity building programs.
- **Ongoing innovation:** IFC continues to develop sustainable energy finance products based on extensive experience, client needs, and market developments. Future product offerings will enable client FIs and their customers to access carbon credit revenue streams as an additional benefit to implementing sustainable energy projects.



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