



Futuregrowth Power Debt Fund

Developmental & Social Impact Bi-annual Report
30 September 2023

FUTUREGROWTH
/ ASSET MANAGEMENT



THE PRIVATE SECTOR NEEDS TO FILL THE VOID

As South Africa grapples with increasing stages of loadshedding due to Eskom's inadequate power generation, the spotlight has fallen on the dire state of the utility's coal fleet.

The capacity of the grid to accommodate new renewable energy is a concern



Whilst Eskom's generally aged and defective power plants are the predominant reason for our country's energy predicament, there has been some frustration about the apparent slowness by the private sector to fill the void and roll out large scale renewable energy. Privately produced power is widely acknowledged as a solution to help address Eskom's managed wind-down over the coming years.

Despite the intent and capacity of independent producers to move forward with constructing new energy plants, many are hamstrung by the inability of Eskom's infrastructure to keep up with the pace of new applications ready to connect to the national grid. This has resulted in bottlenecks and delays. The South African government responded to the energy crisis in 2019 with a plan to unbundle Eskom through a separation of its generation, transmission and distribution functions into three separate entities. However, progress has been curtailed by various challenges, including union resistance, Eskom's financial difficulties and the impact of the COVID-19 pandemic.

To ensure that the roll out of large-scale power generation by the corporate, mining and industrial sectors is sustained, it is critical that Eskom upgrades some 2 900km of extra high voltage lines and dozens of transformers across the country. As is the case in many developed nations, the expectation that new equipment will not be needed very quickly is one of the legacies of a centrally planned and controlled national transmission network.

Most of the renewable energy plants currently connected to the national grid are located in the Northern Cape, Western Cape and Eastern Cape. However, given the number of projects added over the past ten years, plus those private sector power sources that have registered projects with the government, the capacity of the grid to accommodate new connections of renewable energy is almost exhausted in these provinces, particularly in the Northern Cape and Western Cape.

In this report

In this ninth bi-annual report, we look at the idea of wheeling where electricity is "wheeled" over the grid through a power purchase arrangement between a producer of electricity and an off-taker. This, for example, could mean that a power producer in the Northern Cape province could potentially produce electricity that is then used through this arrangement by an industrial steel producer located in the Gauteng province. We highlight the complexities surrounding wheeling and "Use of System" charges, and urge the establishment of a comprehensive framework, emphasising the need for streamlined negotiations to expedite renewable power distribution and alleviate the energy crisis.



Jason Lightfoot
Senior Portfolio Manager

In response to the power challenges faced by the country, Government took steps to increase electricity generation by removing the licencing requirements for power generation. These actions have had a positive impact in boosting private sector investment into the power sector in South Africa.

It is increasingly clear that South Africa's energy security predominantly lies in the hands of the Independent Power Producers (IPPs) to generate renewable energy and distribute it to customers over Eskom's electricity grid. However, the lack of a standardised wheeling framework governing the distribution of this energy is creating investment uncertainty and thus hindering progress.

What is wheeling?

Wheeling refers to a bilateral agreement between the renewable electricity generator and the off-taker who uses the electricity. The power is wheeled over the Eskom and/or municipal transmission networks.

Tariffs

Right now, there is ambiguity about the wheeling and use-of-system charges. Eskom charges a wheeling tariff, but that rate hasn't been standardised. In the few contracts concluded between Eskom and the wheeling parties, the wheeling and use-of-system charges have been negotiated on a case-by-case basis, which is both time-consuming and unpredictable.

We believe it is crucial to develop a general wheeling framework that applies to all IPPs, to maximise the potential private sector energy generation can offer to alleviate the power crisis. Simplifying the costs and how the wheeling agreements will work, will provide power producers with more certainty and enable them to fast-track wheeling arrangements with Eskom and the municipalities.

We recognise the work the National Energy Crisis Committee of Ministers (NECOM) is doing to set out the national wheeling framework. However, we think that Eskom and Government should be taking the lead in finalising the process.

It will inevitably take a while to clear up the ambiguity, as the state-owned entity is currently splitting the existing business into three independent divisions: generation, transmission and distribution.

To date, the wheeling arrangements that have been concluded are few and far between, because of the prolonged nature of negotiations with Eskom about how much they will charge

the IPP to distribute the electricity to its end client. It becomes even more complex when the power also needs to be distributed across municipal grids to get to the end customer, as separate agreements need to be put in place between Eskom and the municipalities.

Virtual wheeling platform

Instead of focusing on providing a transparent and standardised framework for one-to-one wheeling arrangements, Eskom has announced its intention to establish a virtual wheeling platform. This differs from direct wheeling contracts between an IPP and a corporate client, in that Eskom controls the platform by connecting multiple buyers with generators.

While clients will be able to source private sector electricity over the grid, Eskom will control the electricity tariff, and there will be no room to negotiate with the IPP on the cost of the electricity provided to them in a one-to-one agreement. The virtual wheeling contract will also be complex in that the client will be charged a set amount for electricity each month. Then, Eskom will calculate the amount of electricity used and determine the buyer's wheeled energy refund. Unlike with one-to-one wheeling arrangements, buyers will be exposed to Eskom's financial risk because they will have to rely on Eskom being able to repay clients for the electricity they haven't used.

Part of Eskom's process is dealing with the significant third-party debt it has built up over the years, and determining which of the three entities will become responsible for that debt after the restructuring. Billions of rands are needed, but the utility is technically insolvent and doesn't have the money to meet its debt obligations. By freeing up private generators' ability to trade power over the grid, Eskom is effectively bringing the private sector on board to assist in servicing that debt. Revenues from the wheeling charges paid by the IPPs are expected to impact Eskom's revenues positively.

The main driver of this is to ease the pain of load shedding on the economy and corporate sector, and achieving energy security as soon as possible. So, it's not a case of choosing one wheeling model over another. Instead, off-takers should be able to choose which energy source suits their need better and, where direct wheeling arrangements are the preferred option, power producers should be able to operate within a standardised framework that allows for simple contracting. This would accelerate much-needed progress.

Fund facts

Portfolio manager	Jason Lightfoot
Benchmark	South African STeFI Composite Index (STeFI)
Performance target	STeFI + 2.75% per annum before the deduction of taxes and fees, with income reinvested
Reg 28 classification	Debt instruments, predominantly unlisted instruments of unlisted entities
Investment focus	Debt and fixed income in energy related industries and sectors
Minimum investment	R50 million (at the manager's discretion)
Asset class	Fixed & variable rate debt instruments
Current structure	Pooled, open-ended
Fund start date	January 2013
Total Fund assets	R10.81 billion
Termination period	12 months (size dependent)

Specialising in renewable energy investments

The Futuregrowth Power Debt Fund specialises in energy-related industries and sectors, and forms part of Futuregrowth's suite of developmental investments.

The Fund may invest in a wide range of debt instruments including those issued by government, parastatals and corporates, as well as securitised assets. The inclusion of assets is subject to credit committee approval.

The Fund is largely invested in renewable energy deals that form part of the Department of Energy's Renewable Energy Independent Power Producer Procurement Programme (REIPPPP). All projects under the REIPPPP enter into an off-take purchase agreement with Eskom for the power they will produce during the next 20 years and these revenue streams will be used by the projects to repay the debt finance.

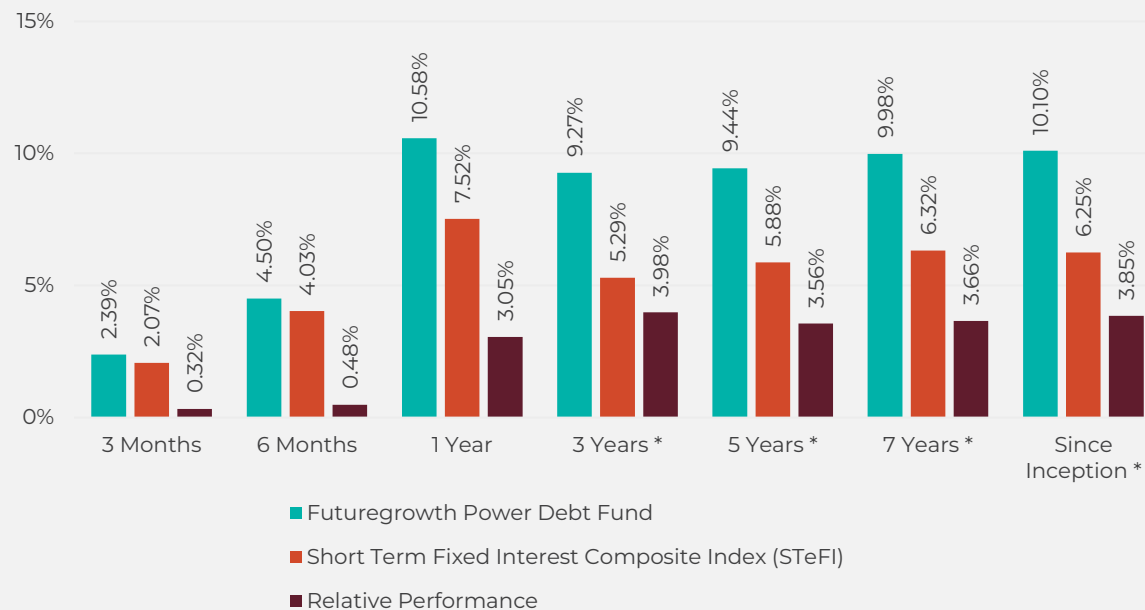
The Fund aims to provide investors with a vehicle that facilitates infrastructural, social, environmental and economic development in southern Africa through investments in energy-related businesses and sectors. These include electricity generation from renewable, alternative and traditional sources, power distribution and reticulation, and supporting industries and sectors.

The Fund delivers on a variety of social impact requirements such as: job creation through employing local labour to build and maintain the plants, SMME development through employing contractors, mentorship and skills transfer from international developers, meeting BEE equity requirements, investment by the projects into local socio-economic infrastructure and services, and compliance with the international Equator Principles.

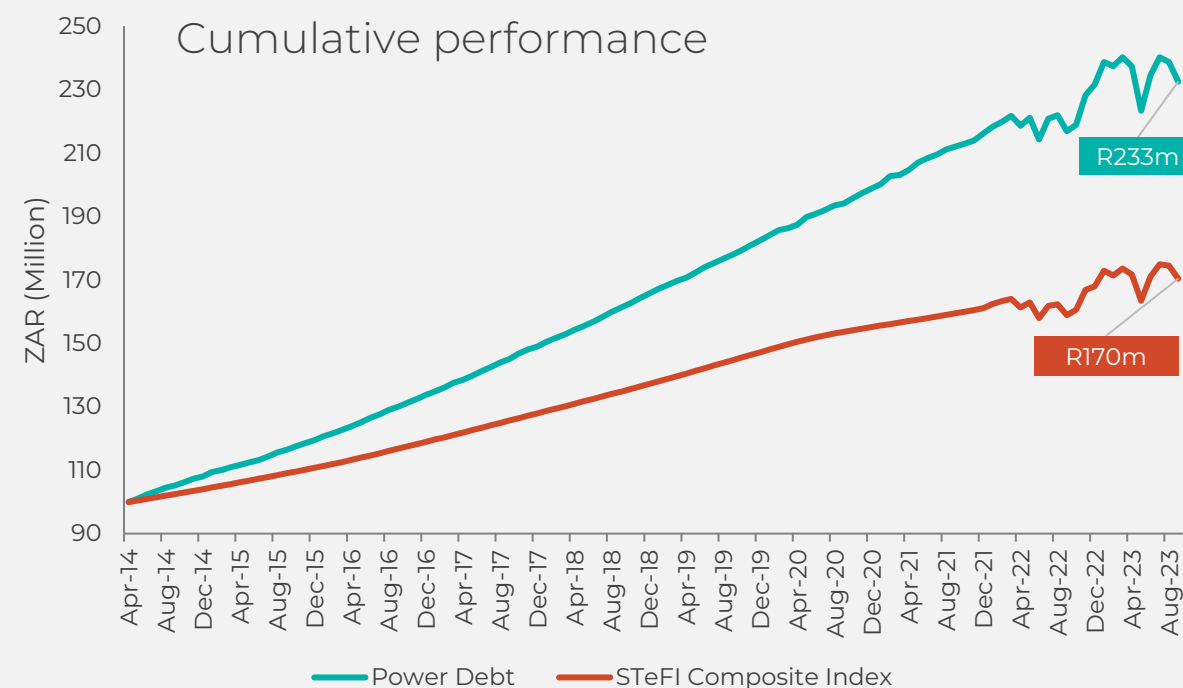
Investment performance

Credit spread accrual continues to be the main contributor

Futuregrowth Power Debt Composite



Data as 30 September 2023 // Since inception date (GIPS Composite): May 2014
 Fund start date: December 2012 // Source: Futuregrowth // *Annualised



The Fund marginally outperformed its benchmark in the third quarter of 2023. Credit spread accrual continues to be the main contributor to performance, through an exposure to primarily energy-related transactions in both the unlisted and listed credit space. On the interest rate side, longer-term government bond yields increased, negatively affecting our performance due to exposure primarily in the 12- to 20-year area of the curve. However, this impact was partially offset by positive base accrual. Furthermore, we experienced some negative performance due to our active swap spread position, which widened during the period under review.

Key qualifying criteria for projects under the REIPPPP programme

The REIPPPP was born in 2012 out of a need and desire to procure alternative, sustainable energy, while simultaneously contributing to social and economic development in South Africa. It allows Independent Power Producers (IPPs) to submit competitive bids to design, develop and operate large-scale renewable energy power plants across South Africa. As a pre-requisite for submitting bids to the REIPPPP, IPPs must show how their project will deliver social and economic development for South Africans.

Bid tariff



- +/- 70% of the bid evaluation weighted towards the bid tariff.
- Tariffs awarded in later rounds of the programme have dropped significantly compared to the first round.

Local procurement



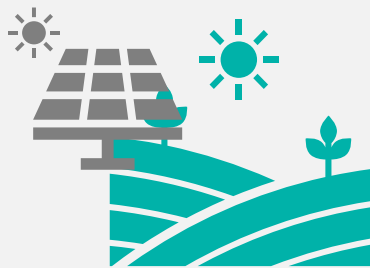
- Minimum of 50% of staff must be RSA citizens, with target of 80%.
- At least 45% of the project's construction materials and services must be procured in SA.

Black & community ownership



- At least 30% BEE shareholding requirement for the IPP.
- At least 2.5% must be held by a trust representing the local community.

Clean & renewable generation



- Environmental Impact Assessment of the proposed site and impact of the project required.
- Renewable energy projects do not use fossil fuels, create toxic emissions or hazardous waste.

Employment & skills transfer



- Many international developers have partnered with local firms to develop projects, resulting in a high level of mentorship and skills transfer from the international developers.

Infrastructural investment & empowerment



- Many of the projects are constructed in remote arid areas where access roads are required for the construction and operation of the project.
- BEE requirements result in local community empowerment.

Geographic diversity & technology capacity

The Fund is invested in a diversity of renewable energy deals, with **R8.3 billion** in committed deals across 31 projects (out of 117 awarded PPAs under REIPPPP Bid Windows 1 - 5).

Wind R4.2bn



1 429 MW

Solar PV R1.3bn



462 MW

Solar CSP R2.2bn



550 MW

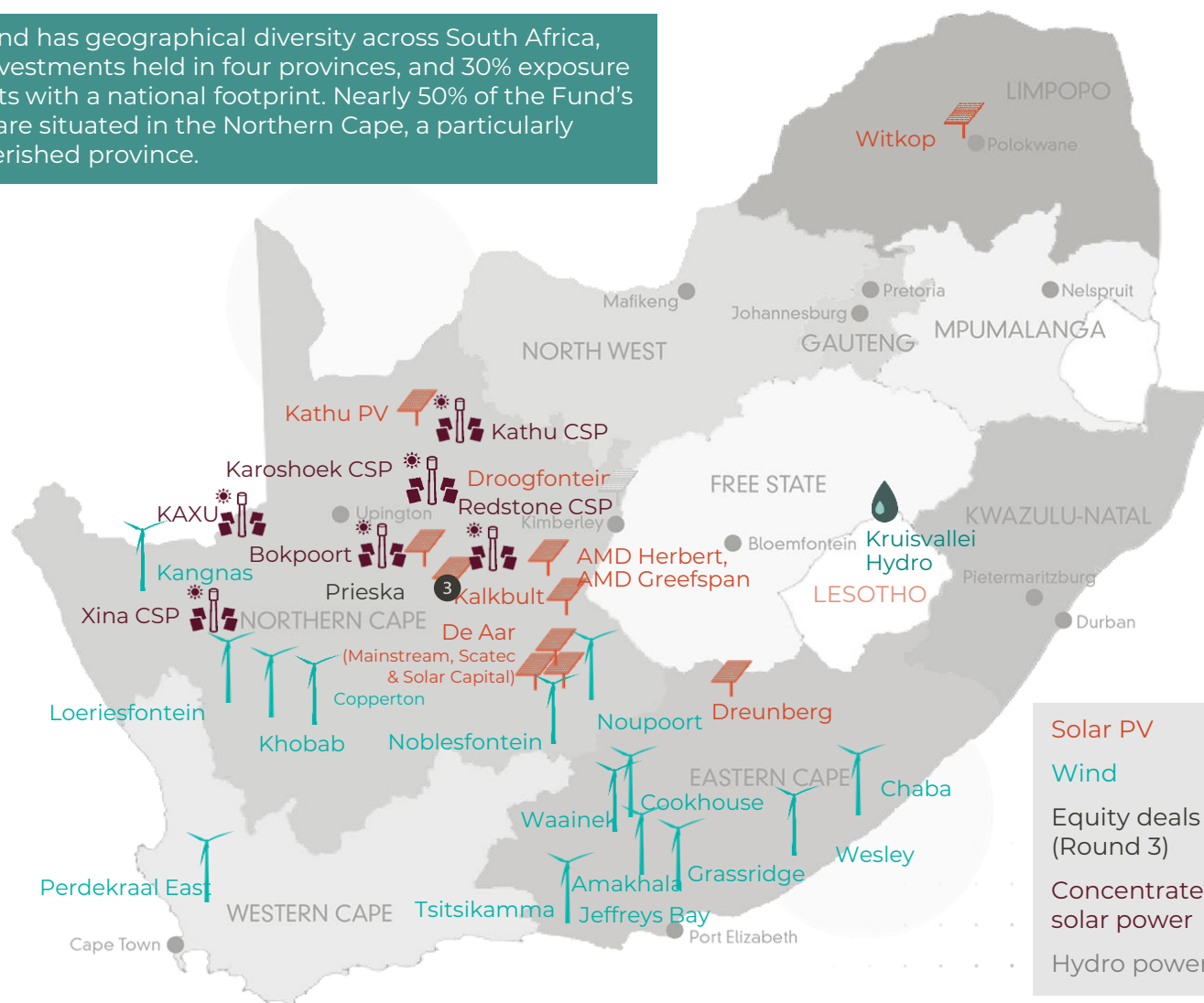
Small Hydro R0.5bn



3.8 MW

Region	% exposure
Northern Cape	49.83%
Eastern Cape	13.38%
Western Cape	3.55%
Limpopo	0.78%
Lesotho	0.55%
National	32.67%
Total	100%

The Fund has geographical diversity across South Africa, with investments held in four provinces, and 30% exposure to assets with a national footprint. Nearly 50% of the Fund's assets are situated in the Northern Cape, a particularly impoverished province.



Our developmental investment philosophy

Developmental product suite

Futuregrowth has a 25-year-plus track record of investing in developmental assets. Our funds provide finance to institutions that may not typically receive support from the traditional banking or lending process. In addition to providing finance (credit), we also invest in equity and retail property with a developmental nature.

Our developmental funds are part of our broader responsible investment strategy and reflect the intention of our clients to do good by investing consciously to make a positive impact on society and the broader environment, and thereby to safeguard our collective future.

Our suite of developmental funds consists of:

- **Fixed Income** (Infrastructure & Development Bond Fund, Power Debt Fund, Inflation-Linked Debt Fund);
- **Unlisted equity** (Development Equity Fund, Agri Funds);
- **Unlisted retail property** (Community Property Fund); and
- **Fund of funds** incorporating our suite of development funds as building blocks (Developmental Balanced Fund).

Futuregrowth is dedicated to the development and empowerment of South Africa and its people. We are constantly looking for opportunities that will yield optimal financial returns for investors while making a meaningful difference. As such, we have become a reliable channel for investor savings and promoting national development.

We define developmental investing as financing that a) provides investors with commercial returns and b) produces a social and developmental impact. In South Africa the primary focus is on the provision of basic services and improvement of infrastructure development.

In order to achieve sustainable, long-term, benchmark-beating performance, we apply a responsible investment filter when screening and analysing new deals for our developmental funds. This is supported by a robust credit process that considers both financial and non-financial risks.

Global contribution

We are also aligned with the UN's Sustainable Development Goals (SDGs), thus contributing to this global "blueprint to achieve a better and more sustainable future for all". The SDGs are covered in detail later in this report, where we link the activities of each deal featured to these global targets.

(See: www.un.org/sustainabledevelopment/sustainable-development-goals/)



How we measure and manage impact

Futuregrowth actively measures and manages for impact. Our impact measurement and management approach is aligned with both global and local development frameworks.



National Development Plan (NDP)

This is a long-term development framework for the elimination of poverty and reducing inequality in South Africa by 2030.

UN Sustainable Development Goals (SDGs)

These goals represent the globally agreed 2030 agenda and are a call to action to end poverty, protect the planet and ensure that all people enjoy peace and prosperity.

Principles for Responsible Investing (PRI)

Futuregrowth is a signatory to the Principles for Responsible Investment (PRI), which is an international network of signatories contributing to developing a more sustainable global financial system by incorporating six defined Principles for Responsible Investment into investment practice.

The Futuregrowth Power Debt Fund

Making a meaningful impact



Kruisvallei Hydro: creating future engineers



Cookhouse Wind Farm :
Supporting daycare centres



REISA Kathu:
Lighting up lives



Noupoot:
creating jobs for the local community.



De Aar solar PV
plants: supporting
local small
businesses.



Droogfontein: supporting community initiatives.

Futuregrowth Power Debt Fund / Key features

R10.81bn
Fund size

Commercial
risk-adjusted
returns

Investments in
electricity generation
from renewable and
alternative sources

Active in
4 provinces

Job creation

- Employing local labour to build and maintain the plants;
- Short- and long-term job creation; and
- SMME development through employing contractors.

Nearly 77% of the
Fund is invested in
rural areas

Skills transfer

- High level of mentorship and skills transfer from international developers; and
- International developers partnering with local firms.

Supports **five**
Sustainable
Development
Goals

Contact information

INVESTMENT TEAM

Jason Lightfoot
Senior Portfolio Manager
jasonl@futuregrowth.co.za
T +27 21 659 5462

Angelique Kalam
Head: Sustainable Investment Practices
angeliquek@futuregrowth.co.za
T +27 21 659 5483

CLIENT RELATIONSHIP TEAM

Maseabi Marageni
mmarageni@futuregrowth.co.za
C +27 84 837 7295

Mzukisi Ralawe
MRalawe@futuregrowth.co.za
C +27 82 809 2013

Ziyanda Tshaka
ziyandat@futuregrowth.co.za
C +27 83 666 0392

Marilyn Gates Garner
marilyng@futuregrowth.co.za
C +27 82 466 0868

Disclaimer

Futuregrowth Asset Management (Pty) Ltd ("Futuregrowth") is a licensed discretionary financial services provider, FSP 520, approved by the Registrar of the Financial Sector Conduct Authority to provide intermediary services and advice in terms of the Financial Advisory and Intermediary Services Act 37 of 2002. The fund values may be market linked or policy based. Market fluctuations and changes in exchange rates may have an impact on fund values, prices and income and these are therefore not guaranteed. Past performance is not necessarily a guide to future performance. Futuregrowth has comprehensive crime and professional indemnity in place. Performance figures are sourced from Futuregrowth and IRESS. This document is for information purposes only and is not intended as an offer or recommendation to buy or sell or a solicitation of an offer to buy or sell a financial product or security. The recipient is advised to assess the information with the assistance of an advisor if necessary, with regard to its compatibility with his/her own circumstances in view of any legal, regulatory, tax and other implications. Personal trading by staff is restricted to ensure that there is no conflict of interest. All employees of Futuregrowth are remunerated with salaries and standard short and long-term incentives. No commission or incentives are paid by Futuregrowth to any persons. All inter-group transactions are done on an arm's length basis. Futuregrowth has comprehensive crime and professional indemnity insurance. Futuregrowth prepared this document in good faith. Although the information in this document is based on sources considered to be reliable, Futuregrowth makes no representation or warranty, express or implied, as to the accuracy or completeness of this document, nor does it accept any liability which might arise from making use of this information.

FUTUREGROWTH

/ ASSET MANAGEMENT

3rd Floor, Great Westerford
240 Main Road, Rondebosch
7700, South Africa
Private Bag X6, Newlands, 7725, South Africa
Tel: +27 21 659 5300 Fax: +27 21 659 5400
www.futuregrowth.co.za

Directors

GL Gobodo (Chairman) PE Rackstraw (Managing Director)
AC Canter* H Beets** P Moodley S Mabaso-Koyana
*American **Netherlands
Reg No. 1996/018222/07
A licensed Financial Services Provider