

# 'POWER' TO THE PEOPLE OF AFRICA –

*social risk management and its returns*



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Stuart Heather-Clark is a Partner and Power Sector Lead for ERM Sub-Saharan Africa. Stuart has more than 20 years' experience in project managing large integrated environmental and social projects, including Environmental and Social Impact Assessments (ESIAs), Strategic Environmental Assessments (SEAs), Environmental and Social Due Diligence and environmental screening studies throughout Africa. Stuart has directed numerous ESIAs and ESDDs for a variety of renewable energy project across Sub-Saharan Africa.



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Deon is the Social Practice Lead for ERM Southern Africa and focuses on impact evaluation, strategy formulation, socio-sustainability, corporate social investment and stakeholder engagement. Deon's integral understanding of the mining industry, initially as a geologist, offers a valuable proposition for the development of strategic stakeholder interventions and solutions. In addition, Deon has exposure to and experience within the South African regulatory framework, specifically related to compliance with social, sustainability and labour requirements.



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Tunde is a Partner with ERM, based in London. He has 20 years' experience in managing and evaluating social performance activities for the power sector in Africa. His key areas of expertise include social impact assessments, resettlement and social investment programmes for the thermal, solar and hydro projects across the continent. He is a key author for the IFC Strategic Community Investment handbook published in 2010.

*Africa has growing appeal for international investors. By 2014 it was the world's second most attractive investment destination, behind North America and ahead of Asia. Sub-Saharan Africa (SSA) has particularly strong pull and in 2013 accounted for 83% of foreign direct investment into the continent<sup>i</sup>.*

Of course, one important focus area for investors is power generation; specifically, the private-sector funding of renewable energy power generation.

At the same time, win-win scenarios are beginning to emerge as investors and independent power producers (IPPs) explore opportunities to 'do good' as agents of positive change while earning good commercial returns.

Opportunities are exciting, but are not without challenges.

An area that warrants particular scrutiny is that of non-technical risk – the subject of the present article. Greater

awareness of this topic is increasingly important as effective mitigation of environmental and social risk is vital if Africa is to capitalise on investor appetite for greater exposure to the continent.

Better understanding is also crucial if community impacts are to be minimised, enabling community members to enjoy improved quality of life.

Africa is a continent, not a country. This states the obvious, but it is important to alert external investors to the fact that each jurisdiction – indeed each individual community – presents a unique mix of challenges and opportunities.

<sup>i</sup> EY's attractiveness survey – Africa 2014: Executing growth



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Africa is blessed with abundant sunshine while the winds across Africa’s coastline and interior offer boundless opportunities for power generation.

Clearly, providers of renewable energy can tap significant natural resources. At the same time, Africa’s power gap, the mismatch between needs and capacity, ensures strong market demand.

Two-thirds of the SSA population – 620 million people – live without electricity<sup>ii</sup>.

Meanwhile, four-fifths of those living in SSA (727 million people) rely on solid biomass, mainly hardwood and charcoal, for cooking. What’s more, 80% of SSA primary schools have no access to electricity<sup>iii</sup>.

According to a World Bank paper (Africa’s Power Infrastructure by Eberhard, Rosnes, Shkaratan and Vennemo), Nigeria, Africa’s largest economy, has installed capacity of only 5,898MW. In Botswana installed capacity falls to only 132MW. Indeed, the entire continent’s total installed capacity has in the past been estimated by the African Development Bank to equate to that of Belgium’s<sup>iv</sup>.

Unsurprisingly, it will be 2080 or beyond before Africans enjoy universal access to electricity.

In response, more and more African countries are making eradication of the power gap a policy imperative. The preferred mechanism is the creation of Independent Power Producers Procurement Programmes (IPPPP) to attract IPPs to invest in power generation.

Some IPPPPs are already operational. For example, South Africa’s Renewable Energy Independent Power Producers Procurement Programme (REIPPPP) has procured over 4,300MW of renewable energy generation in less than four years.

ii Africa Energy Outlook, part of the 2014 World Energy Outlook series

iii EY’s attractiveness survey – Africa 2014: Executing growth

iv The High Cost of Electricity Generation in Africa – African Development Bank, 2013

Africa-wide there is scope for investment in a host of renewable energy power plants; generating not only power but significant revenue streams. But before capital can be committed risks must be assessed.

This is no longer a matter for individual initiative. Mitigation methodologies are set down by several international bodies, including the Equator Principles and the International Finance Corporation with its Performance Standards.

Some painful lessons were learned at the beginning of the new millennium. So much so that major providers of project finance are today unwilling to commit funding unless non-technical risk is thoroughly assessed and appropriate mitigation strategies are put in place.

Experience confirms that companies that ignore environmental and social risk face potential reputational damage and increased costs resulting from project delay or from unforeseen changes to project design.

Social risk is compounded in Africa as there is no standard approach to address these risks, though many African countries have framework environmental legislation.

Another factor that warrants the attention of funders and project developers is the growing stakeholder demand in many emerging markets that commercial interests not only meet legal and regulatory requirements, but establish a ‘social licence to operate’ through ongoing community investment.

Extractive industries have faced these demands for several years and certain conclusions are inescapable.

One is that failure to establish a social licence to operate can have severe financial impact. Indeed, a US study notes that community conflicts over environmental and social concerns can cost up to \$20 million a week in lost value at large operating mines<sup>v</sup>.

v *Cost of Company-Community Conflict in the Extractives – Harvard Kennedy School, 2014*

Company valuations are also impacted when shareholders divest after unfavourable publicity or appeals to the corporate conscience.

An EY study cited the social licence to operate as one of the top three under-the-radar business risks for mining and metals in 2014-15 while analysis by ERM identified social opposition as the top cause of mining project delays in the period 2008-2012 (42% of delays were attributed to this cause).

Community and activist pressure around the social licence to operate can also trigger regulatory change. For instance, South African authorities require mining operations to compile detailed Social and Labour Plans to demonstrate their community investment initiatives.

Mining and power generation are very different industries, but there are commonalities. Indeed, the narrative around mining sector social licence to operate already finds an echo in South Africa's REIPPPP.

The South African REIPPPP entrenches concepts of socio-economic development, enterprise development and local employment into its implementation agreements with IPPs. It requires an investment of 1.5% of net revenue within a 50km radius of the renewable energy plant.

Terminology differs across Africa, but there is common focus on local content, skills transfer, local procurement and recruitment and community development. Nigeria, for example, is currently in the process of drafting local content legislation for the power sector that will mirror that developed for its oil and gas industry.

Meanwhile, social media provides a platform for sharing information on community and environmental issues across industries and continents. New areas of concern continually attract public and media attention, suggesting that IPPs make themselves vulnerable if they rigidly adhere to a government's minimum requirements.

Renewable energy developers need to do more than just address their direct impacts; for example, implementing community development projects that go beyond mitigating ESIA impacts.

Developers are well advised to improve their understanding of social risks, the business case for a social licence to operate and the evolution of corporate social investment programmes, in Africa and elsewhere.

However, opportunities are at least as evident as risks.

Those who take their social and environmental responsibilities seriously are not only positioned to avoid unnecessary risks and unforeseen costs, they also improve the potential for long-term profit and enhanced return on investment (ROI).

Higher profit and a higher purpose often go hand in hand.

This was highlighted recently in the marketing text, *GROW: How Ideals Power Growth and Profit at the World's Greatest Companies*. The book spotlights the relationship between higher purpose and financial performance. Author Jim Stengel demonstrated that investment in brands with strong reputations for sustainability can be 400% more profitable than an investment in the S&P 500.

These insights are not lost on pension funds, private equity investors, banks and project developers. Boards of directors, senior executives and shareholders are increasingly interested in the prospect of doing good business while doing good on a societal and community level.

The desire to make a positive contribution in the previously marginalised continent of Africa is particularly strong. However, certain pitfalls must be avoided.

One is attitudinal.

It is easy to assume that the higher purpose of improved electricity access for a country will be so obvious that local community buy-in is assured. This strategic view – while valid – ignores local priorities and concerns.

Typically, renewable energy projects in Africa are developed in remote rural areas. Poverty may be deeply entrenched. Access to electricity is only one area of need. Villagers living near the project site may also have limited access to schools, water, sanitation, health care and social services.

Each site is different. A standardised approach is simply not possible. Therefore, compliance cannot be achieved by putting ticks in a series of well-established boxes.

An environmental and social impact assessment is a crucial component of the process, but it is just one element in a complex set of variables.



*It is easy to assume that local community buy-in is assured.”*



*Interaction must be constant,  
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The mere prospect of project development is enough to generate numerous expectations around social service delivery and job creation. Therefore, stakeholder engagement, face to face and one to one, is necessary to understand expectations and establish priorities.

Simultaneously, fear and suspicion can be aroused. Will development necessitate resettlement? What about use rights to various paths and water resources? Will graves and burial sites be disturbed?

Social risk mitigation entails continual communication to manage expectations and fears. Interaction must be constant, honest and consistent. The developmental aim may be to generate power, but the local aim is to instil trust.

Government in the national capital may create the market for electricity consumption by guaranteeing predictable pricing over 20 years, but they can rarely guarantee total community acceptance at a remote rural site.

The risk of social opposition must be assessed case by case after thorough community needs analysis.

Interventions should be practical and meaningful for the people on the ground. Experience shows that big gains can often be achieved by relatively small community investments; perhaps ensuring improved water supply by deepening a borehole or achieving better access to schools by helping a local entrepreneur to launch a subsidised mini-bus service. It is also critical to ensure that community institutions and local government are empowered to run and maintain installed facilities. Africa is littered with abandoned community projects that have failed because of the lack of a plan for their upkeep shortly after being commissioned.

Honesty is non-negotiable.

Several hundred workers may be employed during a project's construction phase, but the operational labour requirement

may be limited – perhaps a few dozen workers. It is important to explain these limitations.

Once parameters are understood, expectations can be managed; especially if agreement is reached that a set quota of jobs – no matter how large or small the labour force – will be earmarked for local people.

To some outsiders, rural community members may sometimes appear unsophisticated, but they are extremely sensitive to the motivation for corporate action. It is difficult to win their cooperation if they believe they are an afterthought or only feature on the corporate agenda because they raised objections and began to protest.

As they are directly impacted by the project they believe they should have been consulted from day one ... and they are right!

Social and environmental risk deserves proactive scrutiny from the outset and throughout the project lifecycle, all the way through to decommissioning.

These risks affect site selection, access to funding, ROI projections, operational efficiencies, actual investment returns, corporate reputation and company valuation.

It is therefore in the self-interest of developers that they identify key social risks as early as possible in their investment/project decision-making cycle.

It is also important to realise that long-term community support is unlikely to be secured by a once-only investment in local services.

Local needs won't go away; nor does the need for a sympathetic corporate response. The social licence to operate comes up for metaphorical renewal month after month, year after year. Ongoing engagement is required.

Risk management of this scale and duration is a strategic imperative. In fact, it is a leadership issue.

Social risks are best managed when business leaders promote proper mitigation through personal involvement. These processes are not an add-on or an afterthought. The temptation to regard them as such is best avoided by buy-in from the top.

Issues affecting the long-term success of major capital projects cannot be delegated. The leadership team has to take ownership and demonstrate its commitment to all stakeholders; even to villagers who today are too poor to buy electrical appliances and join the ranks of power consumers.

Uplifting their lives through the delivery of better services goes to the heart of the IPP vision, and the custodians of that vision are the business leaders who drive project investment in the first place. ■