

# The Cleaner Production Investment Process: Steps for action

## *Introduction*

Firms which aim to adopt Cleaner Production (CP) may take a number of different approaches to identify their technical and organisational options. Experience suggests that frequently, there may be several options which do not require any significant initial capital investments; though these 'low-hanging fruit' opportunities are likely to be limited, and more significant improvements will probably require some initial investment.

The economic feasibility of these opportunities can be assessed by using indicators such as Net Present Value or the pay-back period. However, even if these indicators are positive, this does not automatically guarantee that the projects can necessarily be financed. The hurdle of obtaining capital from internal or external sources can be a constraint that hinders the successful implementation of CP.

The following brief checklist is provided to guide firms who have identified opportunities for CP projects and want to find finance so they can be implemented. The checklist identifies 7 steps in the process of financing CP projects.

When potential CP investments are identified, a number of questions must be answered to understand the economic aspects of the opportunity and to establish the allocation of capital to the project. These questions should be answered by a "yes"; if you cannot answer the question, or the question identifies an omission in your financing process, this indicates that action should be taken.

## **Step 1: understanding the costs and benefits**

- a. Do you have a full overview of the economic costs (e.g. Initial Investment Costs, Operating and Maintenance Costs, Waste Management Costs, Compliance and Liability Costs, Less Tangible Costs) and benefits (e.g. additional revenues and cost reductions)?
- b. Has the financial risk related to the project been identified by calculating the pay-back period?
- c. Is there a clear economic value added to the company demonstrated by the calculation of the Net Present Value of the proposed project?
- d. Is the CP project embedded within a broader business plan of the company?

## **Step 2: past financing history of the company**

In order to identify potential sources for project funding it is important to have full insight into the sources from which capital was allocated to the company in the past. Not only may it be possible to approach the same sources again, but the past experience will still be valuable if approaching other sources.

- a. How is the company currently financed, and what sources have been approached in the past?

- b. What were the reasons for success in past approaches to sources of finance? Can these reasons be applicable to the current need for finance?
- c. What were the reasons for lack of success in obtaining finance from sources approached in the past? Do these reasons currently still apply, and can they be avoided in future?

### **Step 3: Review the full range of financing options**

Early contact with potential sources is useful in order to discuss with them the current program parameters and application procedures. In mapping the full set of capital sources that might be available, the following questions can be helpful:-

- a. Have you considered all the possible options, including:- self-financing from internal funds, raising new equity, debt financing, financing through grants from non-governmental organisations or governmental agencies?
- b. Have you identified which potential sources are the most accessible and most likely to be successful? These are likely to be those with which you have had positive experience in the past and hence understand their terms and conditions of lending. Also, new sources can be contacted that were approached by other companies with similar CP investments (the national centre for CP may be able to help by providing contacts).
- c. Have you investigated the lending parameters and application procedures of the sources that you are considering approaching?

#### **Step 4: Analysing the legal, economic and financial implications of potential sources**

- a. What is the impact of attracting capital from the various potential sources on the management of the company? - would this mean putting constraints on future decision-making (for example, by limiting the ability to obtain further finance in future from other possible sources?)
- b. What impact would finance from the source under consideration have for the firm's liquidity, solvency and profitability?
- c. What impact would finance from the source have on the firm's overall cost of capital (positive, neutral or negative)?
- d. Is the firm able to generate all the information that the potential source is likely to require in order to support an application (e.g. financial statements, business plan, assessment of risks, report on environmental and social performance)?
- e. Will the source require that collateral is provided as security for the finance? If so, will this impose a constraint on the firm's ability to be flexible in how it manages its business?

#### **Step 5: Deciding on how to finance the investment**

When deciding on the source to be approached, ask:

- a. Does this source minimise the total costs that you will incur in connection with raising the finance (interest, and the administrative and reporting costs directly related to the provision of the capital)? If not, is the increase in the firm's cost-of-capital acceptable in the context of its continuing future financial health?
- b. Will the proposed source provide capital for the full lifetime of the project?

#### **Step 6: Approaching a source of capital with a request for financing.**

Answering the above questions will help the firm to become better informed about the finance options available, and their related conditions and implications for the firm. This provides a basis from which to proceed to writing a proposal in accordance with the specific requirements of that particular provider of capital.

- a. Are you aware of the decision-maker's hurdle rates and relevant parameters in deciding to finance the investment?
- b. Have you defined a schedule in order to ensure that you will be able to provide the potential financier with the proposal in accordance with their timetables and formats?
- c. Can you comply with the imposed post-funding management and control conditions that the potential financiers are likely to require?
- d. Has the application form and supporting correspondence been signed by the appropriate persons from the firm?

#### **Step 7: Post-Funding Management and Control**

- a. Has a project implementation plan been drawn up to control the period between the financier's agreement to the finance, and the time when the project is fully running and generating benefits for the firm?
- b. Have responsibilities been allocated within the firm to ensure that it:-
  - complies with the conditions of repayment on the pre-agreed dates each of the initial loan and the interest payable on this?;
  - provides the financier with all information required over the period that the loan is outstanding, for them to monitor its performance (e.g. regular financial statements)

- c. Have performance indicators been defined, and procedures set up to ensure that they are regularly measured and reported, for the firm to monitor the success of the project and compare this against the original plan?