



BLENDED FINANCE:

UPDATE &  
FRAMING IMPACT BONDS  
AND RBF MECHANISMS

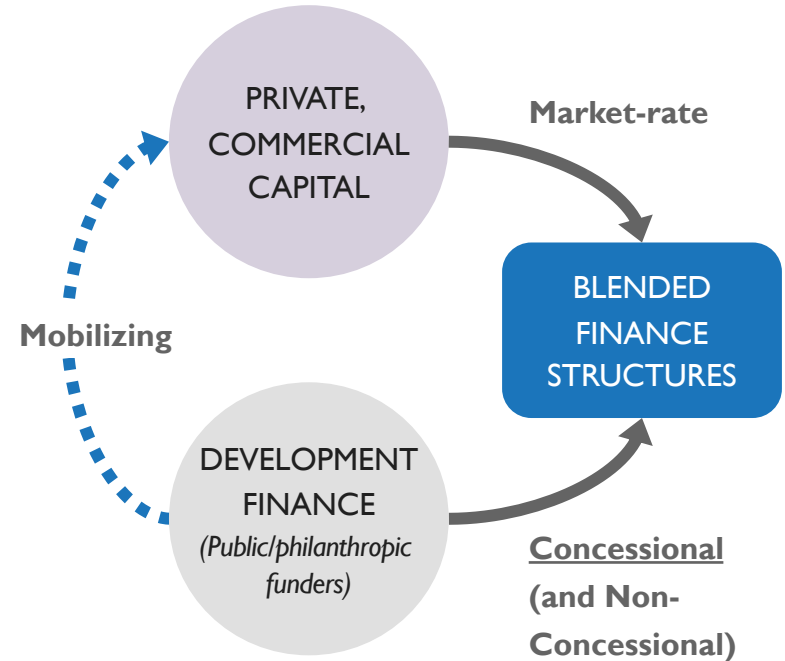
IMPACT BOND WORKING GROUP  
2020 MEETING

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LONDON, MARCH 2, 2020

## DEFINING BLENDED FINANCE

- OECD: “*Development Finance to Mobilise Additional Finance to SDGs in developing countries*”  
– Additional Finance primarily private sector
- Objective: Catalytic grants and risk capital from public & philanthropic sources to achieve impact & mobilise private sector investment.
- Catalytic funds usually deployed at below-market terms to improve unacceptable investment to become bankable / investible by institutional investors & impact investors.
- Blended finance only relevant for sectors and SDGs with revenues to repay private investors



## DEFINING INNOVATIVE FINANCE (GLOBAL AFFAIRS CANADA)

- Definition: “*Financial structures and mechanisms that mobilize, govern or distribute funds beyond traditional donor-country ODA*”
- Three main objectives: (1) Allocate ODA/grants more effectively/efficiently, (2) Demonstrate a public sector good can be delivered more effectively/efficiently and/or (3) mobilise private investment
- Diverse funders/investors with different return expectations, including philanthropic foundations, impact investors and institutional investors
- Can be adapted to support projects in all sectors and themes, including women’s economic empowerment, financial inclusion, climate-smart infrastructure and agriculture and supply chains

# INNOVATIVE FINANCE AND BLENDED FINANCE: MAPPING MECHANISMS

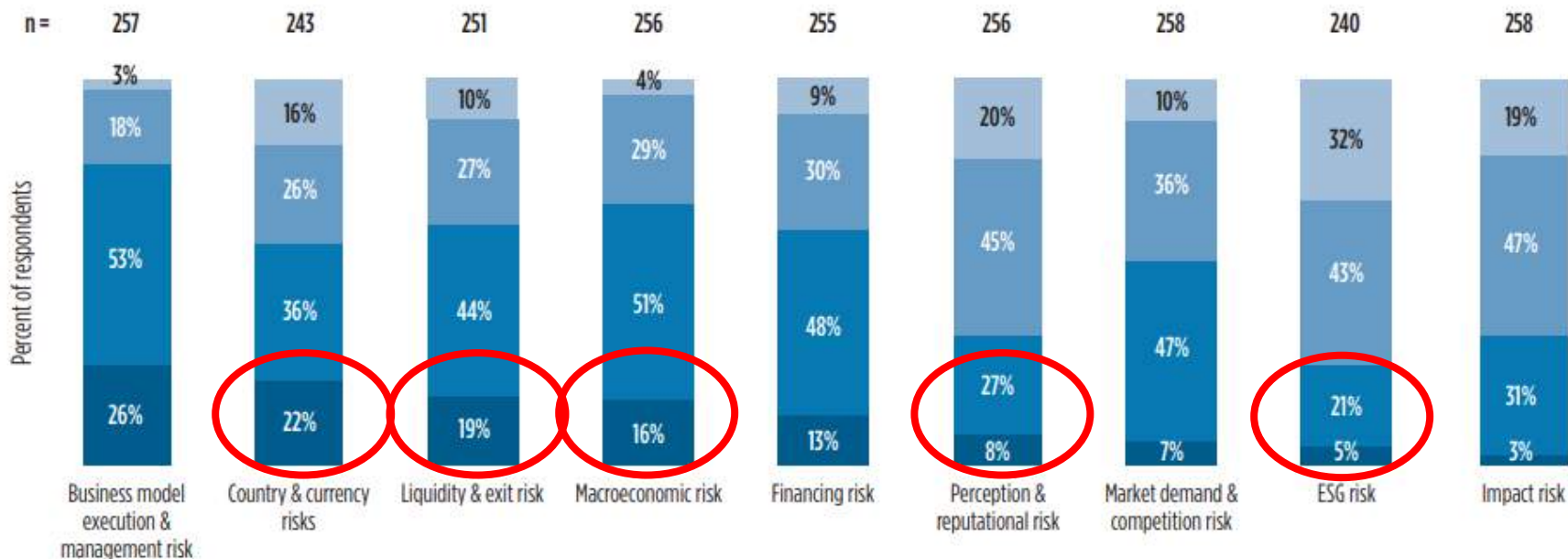
Mechanism (Examples)	Innovative Finance		Blended Finance	
	Efficiency & Effect of ODA funds	Mobilise Private Investment	Concessional Funds	Non-Concessional Funds
Technical Assistance			✓	
Results-Based Financing	✓	✓	✓	
Development Impact Bonds	✓	✓	✓	
SIINCs	✓	✓	✓	
Advance Market Commitments		✓	✓	
Success Notes		✓	✓	
First-Loss Capital from Donors		✓	✓	
Concessional Guarantee		✓	✓	
Syndicated Loans (A - B Loan)		✓		✓
Conventional MDB Loan				✓
Non-Concessional Guarantee		✓		✓

Convergence Area of Focus

# BLENDED FINANCE REQUIRED TO MITIGATE HIGH RISKS IDENTIFIED SYSTEMICALLY BY IMPACT INVESTORS IN DEVELOPING COUNTRIES

Figure 37: Contributors of risk to impact investment portfolios

Number of respondents to each option shown above each column; some respondents chose 'not sure / not applicable' and are not included. Ranked by percent that selected 'severe risk'.



Risks with red bubble systemically high in developing countries making investment unacceptable

# IMPACT INVESTORS REQUIRE MARKET RETURNS FINANCIAL

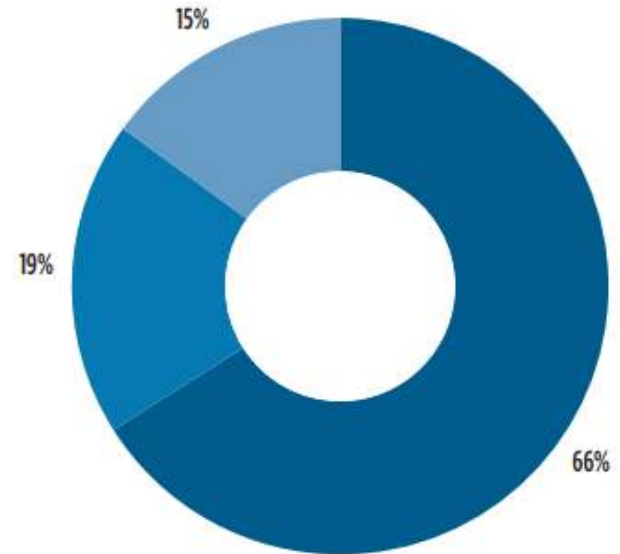
- GIIN's [2019 Annual Impact Investor Survey](#): Most (66%) pursue competitive, market-rate returns. All seek positive expected returns.

Figure 33: Target financial returns principally sought

n = 266

Percent of respondents

- 66% Risk-adjusted, market-rate returns
- 19% Below-market-rate returns: closer to market rate
- 15% Below-market-rate returns: closer to capital preservation



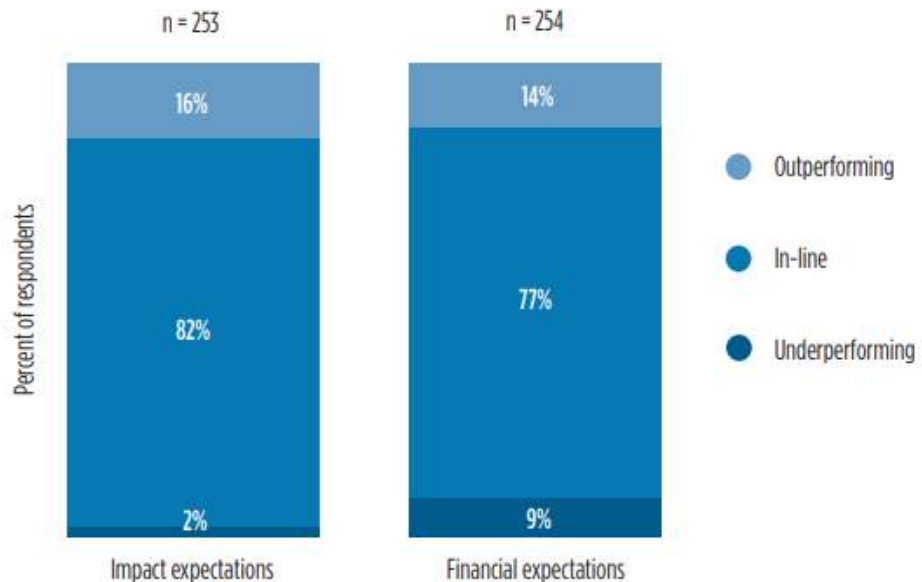
Source: GIIN

# IMPACT INVESTORS: FINANCIAL & IMPACT RESULTS MEET OR EXCEED EXPECTATIONS

- GIIN's [2019 Annual Impact Investor Survey](#): Actual portfolio performance meets or exceeds investor expectations for both impact and financial return
- For (i) developing countries, (ii) developed countries and (iii) globally.

Figure 35: Performance relative to expectations

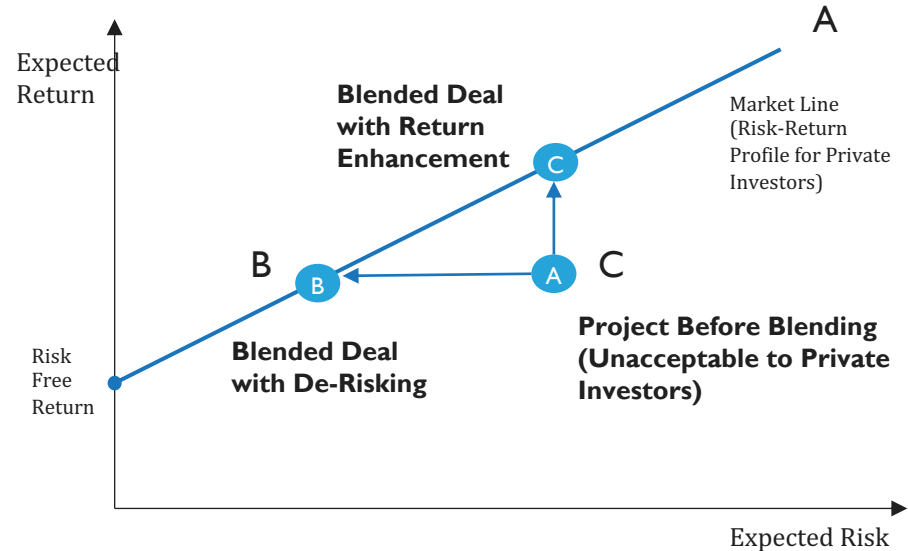
Number of respondents shown above each bar; some respondents chose 'not sure' and are not included.



# BLENDED FINANCE: CREATING “MARKET” RISK-RETURN INVESTMENTS ACCEPTABLE TO PRIVATE SECTOR INVESTORS

- Blue line is the market line from Capital Asset Pricing Model: Efficient range of risk & return combinations available to investors
- Investments below blue market line are below market and not acceptable due to fiduciary duties
- To mobilise private investment, concessional donors can increase returns or reduce risk of investments to market line.
- Large majority of projects in Convergence 500+ project database reduce risk in preference to enhance returns

Deploying Blended Finance To Achieve Commercially Acceptable Risk – Return Profile



Goal of Blended Finance is to create acceptable risk-return profiles to mobilize private sector investment to SDG projects in developing countries

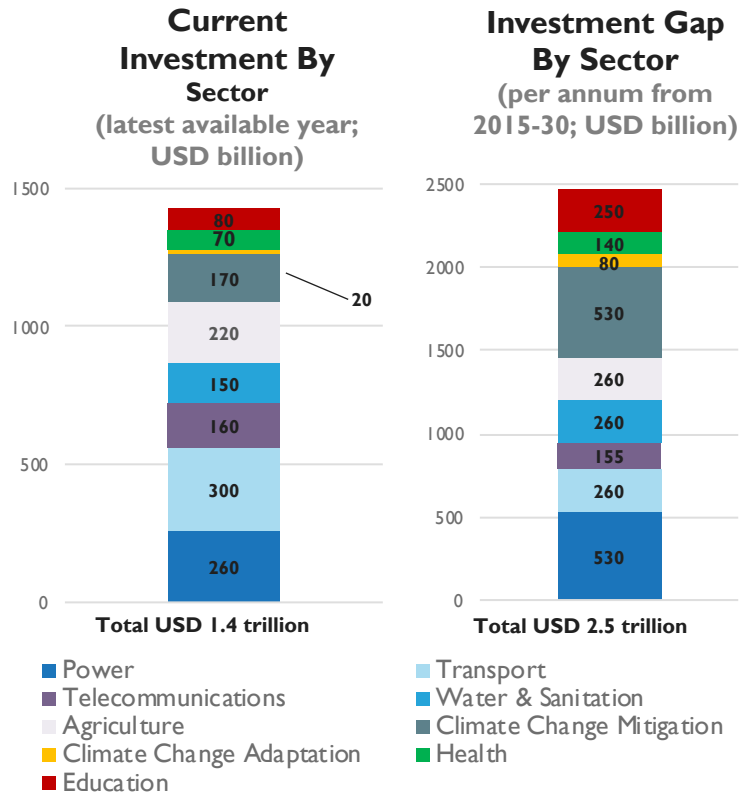


# BLENDING FINANCE CREATES INVESTMENTS ALIGNED TO KEY PRIVATE SECTOR INVESTMENT STRATEGIES & THEMES

Investment Strategy / Theme	Simplified Definition (Various sources)	Alignment with Blended Finance
SDG Investing	Investment to help reach ambitious Sustainable Development Goals' targets; across spectrum of health, education, access to finance and electricity, and more	Always
Social Investing	Managing investment which delivers a social dividend and an economic return	Always
Responsible Investing	Strategy and practice to incorporate environmental, social and governance (ESG) factors in investment decisions and active ownership	Almost always
Environment, Social & Governance Investing	Investing in companies with strong operational performance on ESG, or who aim to improve their ESG performance through the investment	Almost always
Impact Investing	Investments into a company, project or portfolio with intention of gaining a measurable social and environmental return, with or without a financial return	Almost always
Sustainable Finance	Any form of financial service integrating ESG criteria into the business or investment decisions for the lasting benefit of both clients and society at large	Majority
Green Finance	Finance to support the decrease in carbon emissions and increased resilience/adaptation to climate change risk	Substantial Minority

# CURRENT INVESTMENT & FUNDING GAP BY KEY SDG SECTORS

- UN Conference on Trade and Development (UNCTAD) publishes data on investment and funding gaps across key SDG sectors
- This data is expressed in annualized terms, is CAPEX only and is focused on developing countries
- Climate Change Adaptation, Climate Change Mitigation and Education have largest relative gaps with investment equal to 33% or less of actual need



# BLENDED FINANCE GOOD TOOL FOR SUB-SET OF SDGS NOT A GOOD TOOL FOR MANY SDGS

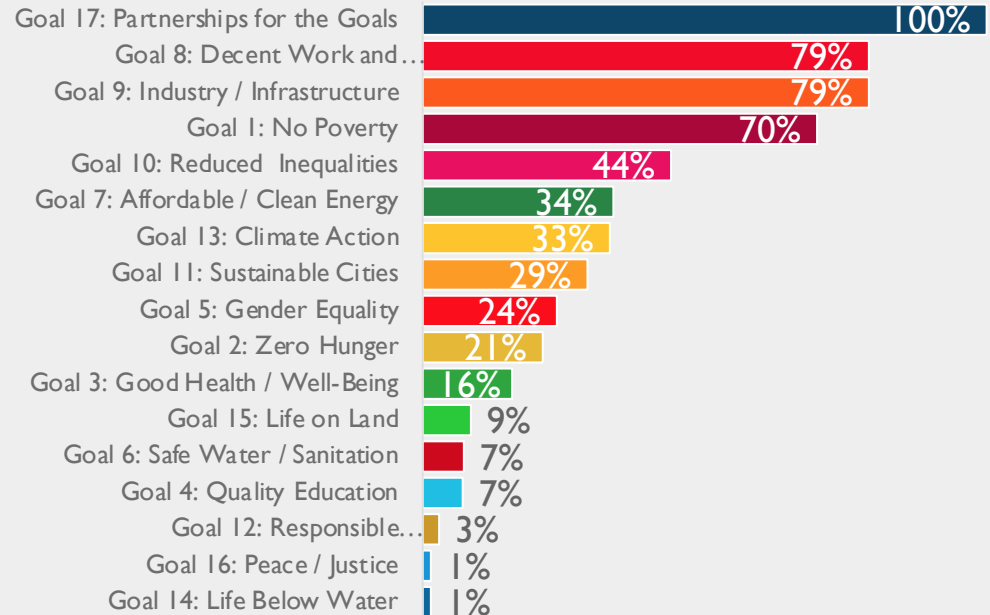
Convergence database of ~500 blended finance transactions mapped to SDG alignment

Blended finance only good tool for SDGs, sectors and projects with **revenues to repay private sector**

- Top 5 SDGs

1. Goal 8 - Decent Work & Economic Growth
2. Goal 9 - Industry, Innovation & Infrastructure
3. Goal 1 - No Poverty
4. Goal 10 - Reduced Inequalities
5. Goal 5 – Affordable and Clean Energy

ALIGNMENT OF BLENDED FINANCE DEALS WITH SDGS  
AS A % OF DEALS IN CONVERGENCE DATABASE



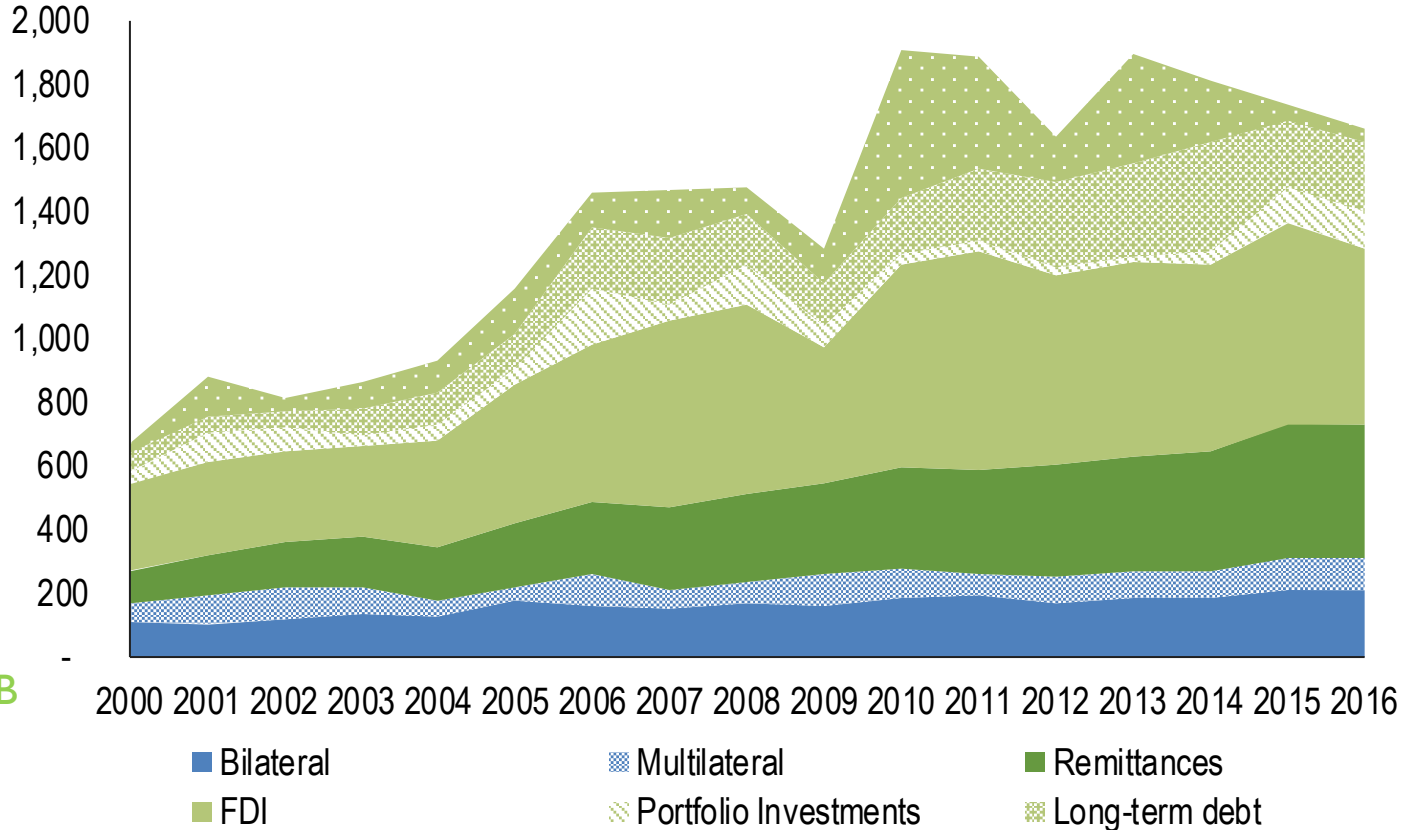
Source: [Convergence Historical Data](#). Note: Data snapshot as of 29 July 2019

# CROSS BORDER FLOWS: LESS THAN 5% OF PRIVATE SECTOR INVESTMENT IN DEVELOPING COUNTRIES.

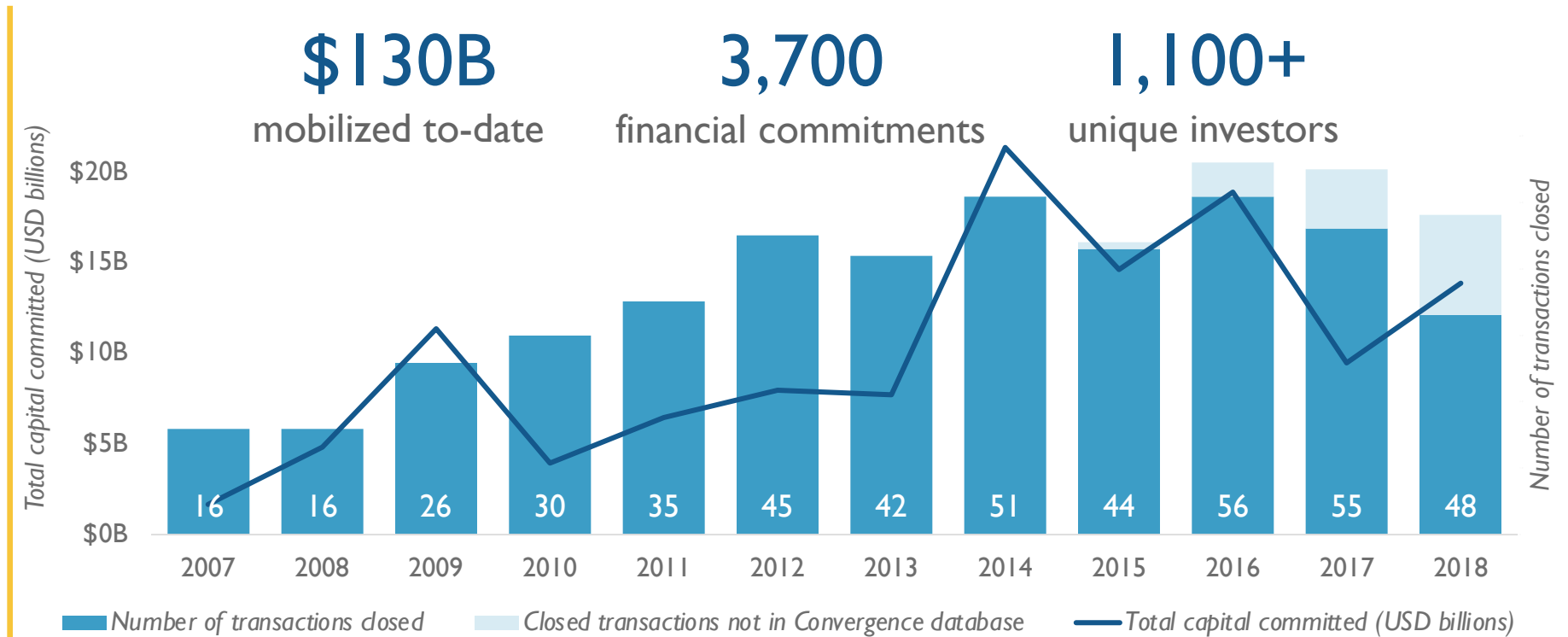
2016 Flows:  
\$1.7 trillion to 145  
developing countries

FDI: \$559 billion  
Remittances: \$417 B  
LT Debt: \$218 B  
Portfolio: \$111 B  
ST Debt: \$41 B  
Bilateral: \$210 B  
Multilateral: \$101 B

Private: (82%) \$1347 B  
Public (18%): \$311 B



# STEADY GROWTH IN BLENDED FINANCE; ANNUAL \$15 BILLION IS VERY SMALL PORTION OF POTENTIAL

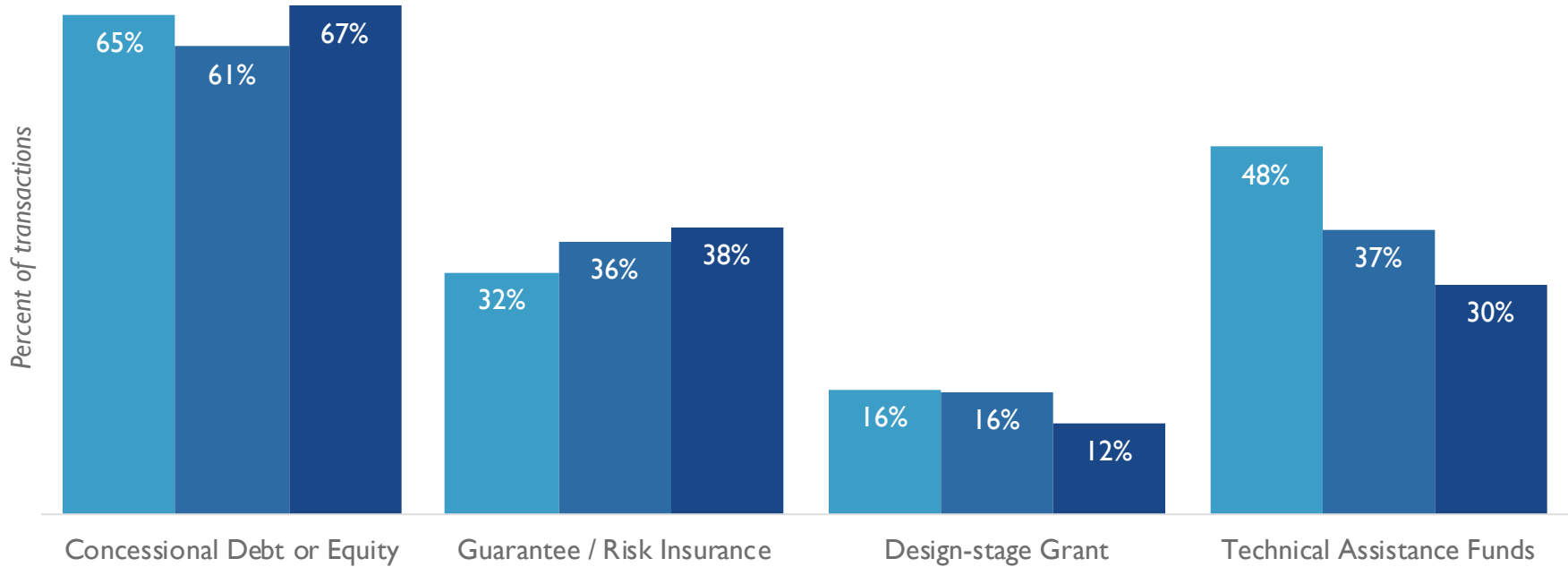


Source: Convergence, The State of Blended Finance 2019

# CONCESSIONAL DEBT & EQUITY (“FIRST LOSS”) PRIMARY FORM OF BLENDED FINANCE; GUARANTEES INCREASING

BLENDING ARCHETYPE

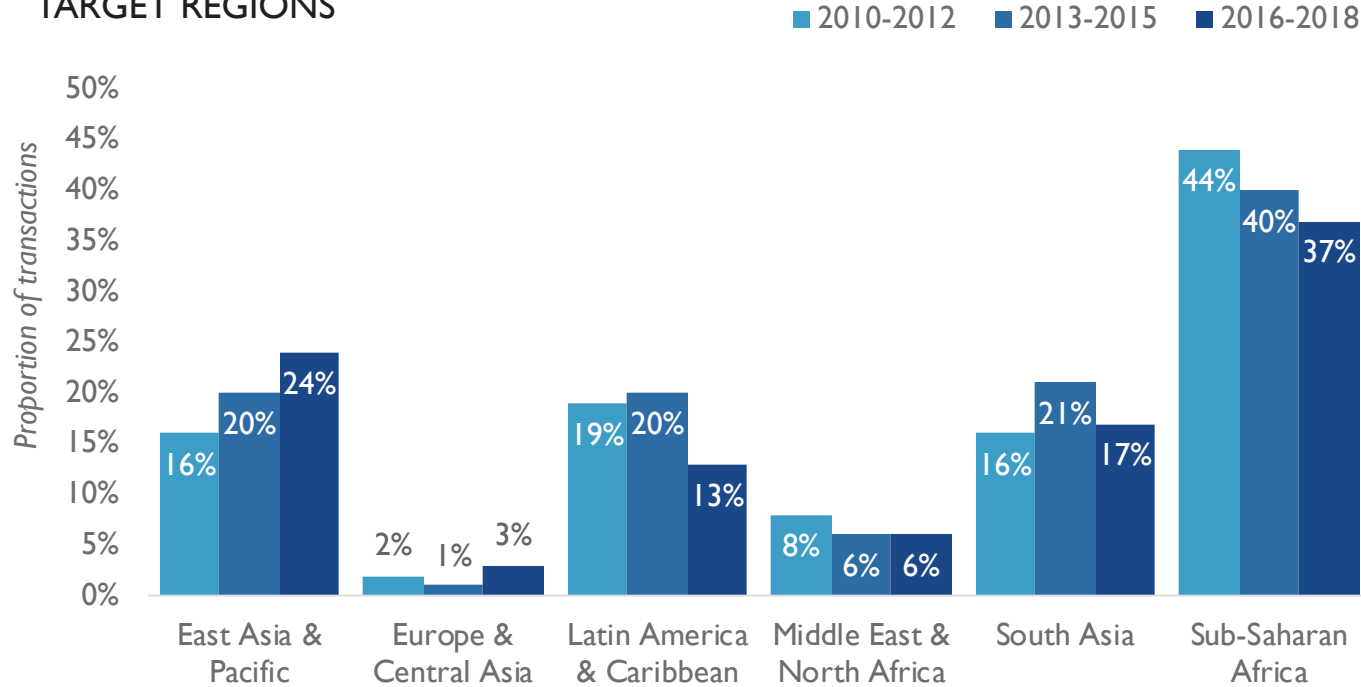
■ 2010-2012 ■ 2013-2015 ■ 2016-2018



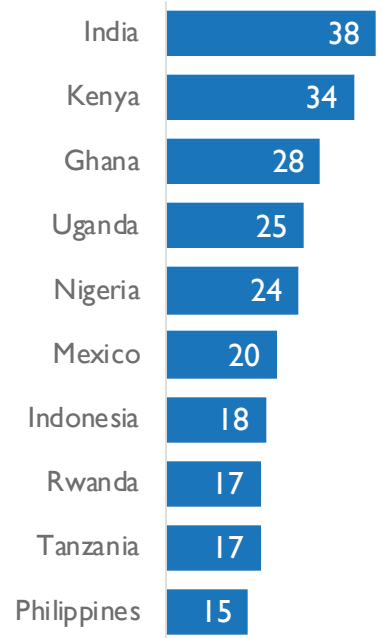
Source: Convergence, The State of Blended Finance 2019

# SUB-SAHARAN AFRICA IS MAIN REGION FOR BLENDED FINANCE; ASIA EMERGING

## TARGET REGIONS

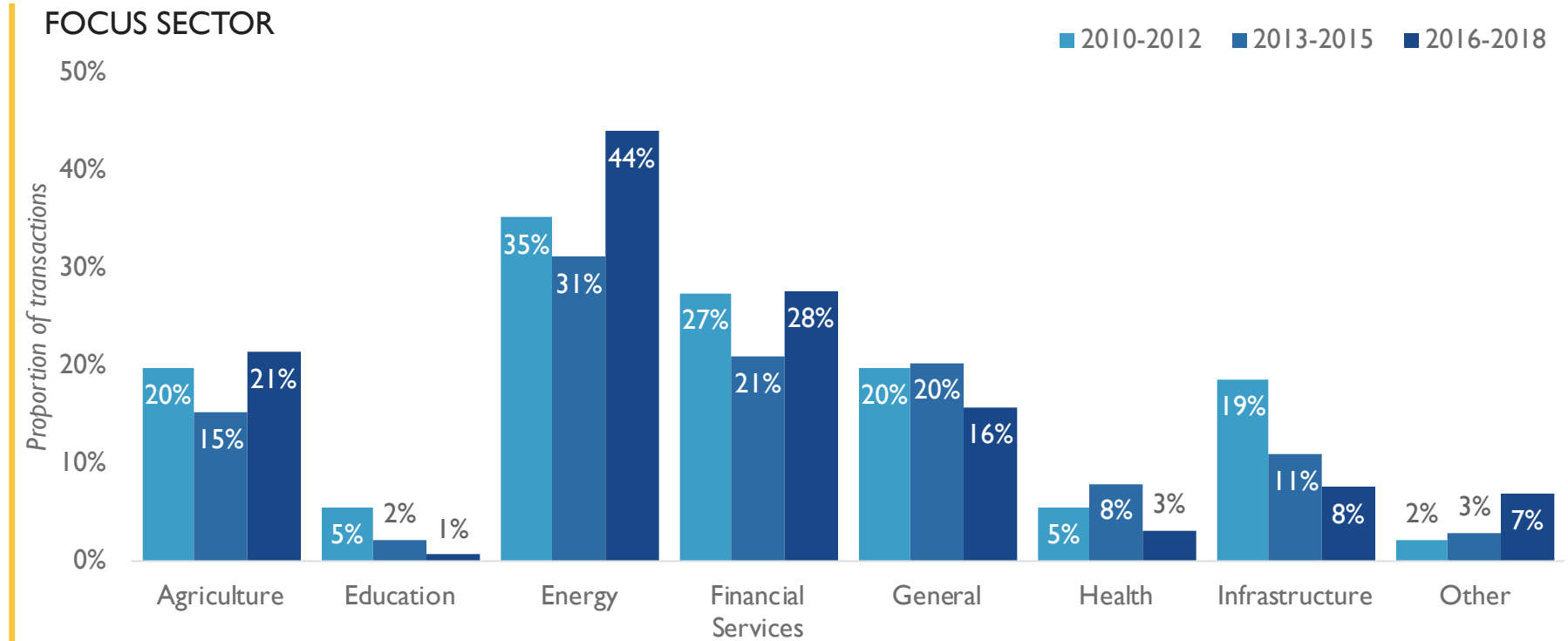


## TARGET COUNTRY



Source: Convergence, The State of Blended Finance 2019

# ENERGY AND FINANCIAL SERVICES STILL DOMINATE; AGRICULTURE, WASH, AND HEALTH PRIMED FOR MORE

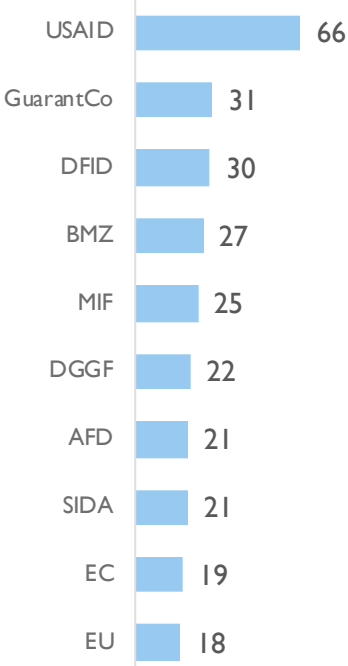


Source: Convergence, The State of Blended Finance 2019

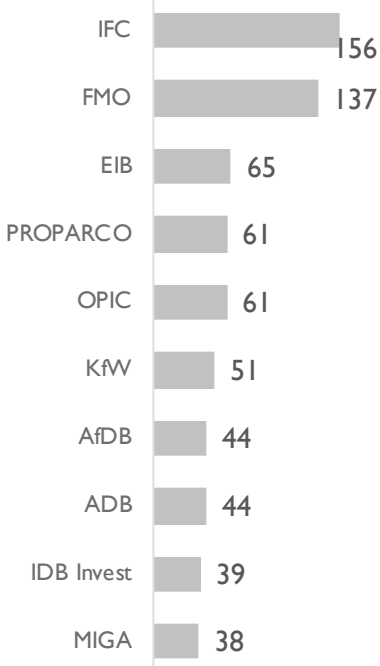


# BLENDING FINANCE TRENDS: TOP INVESTORS

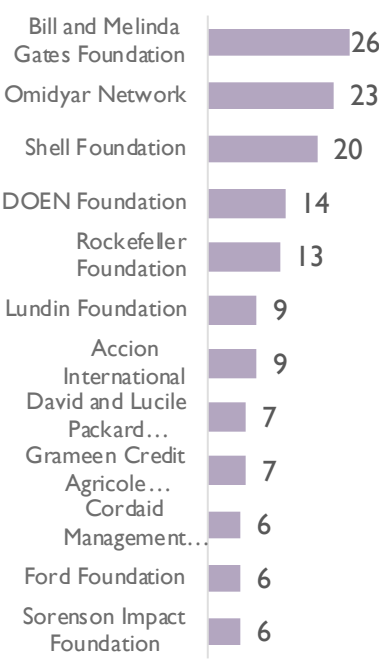
## DEVELOPMENT AGENCIES & MULTILATERAL FUNDS



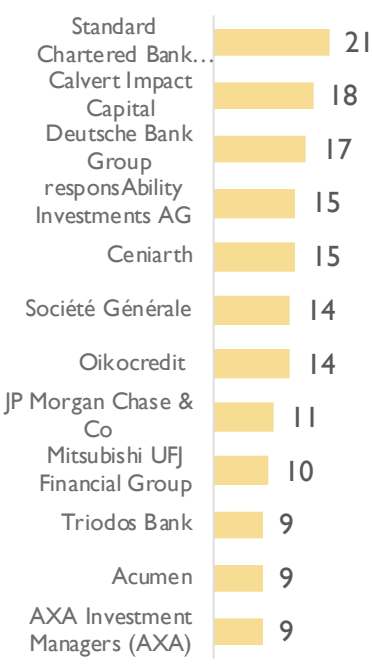
## MDBs & DFIs



## PHILANTHROPIC INVESTORS

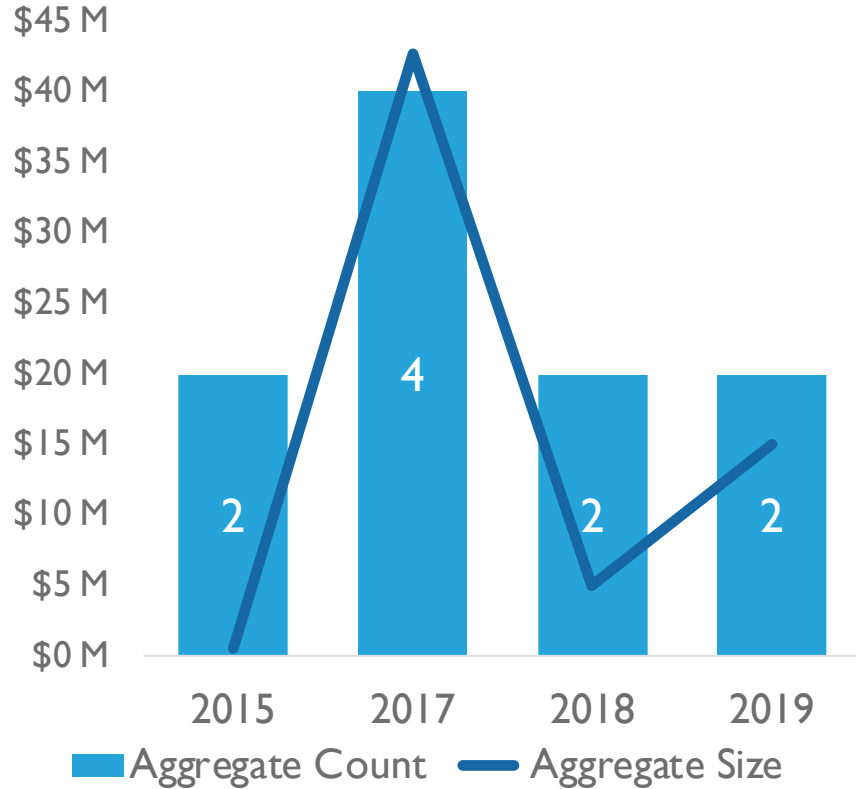


## PRIVATE INVESTORS

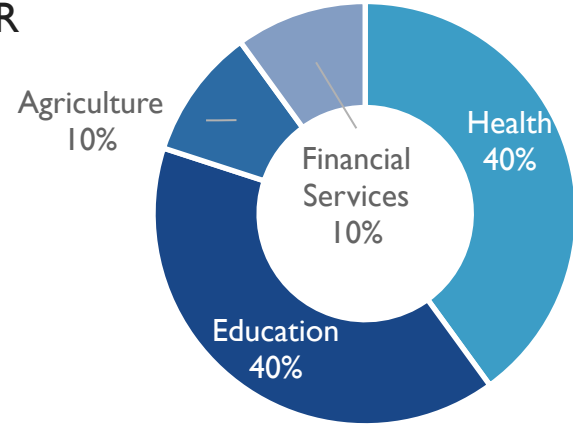


Source: Convergence Historical Data. Note: Data snapshot as of 02 July 2019. Investors ordered by number of investments.

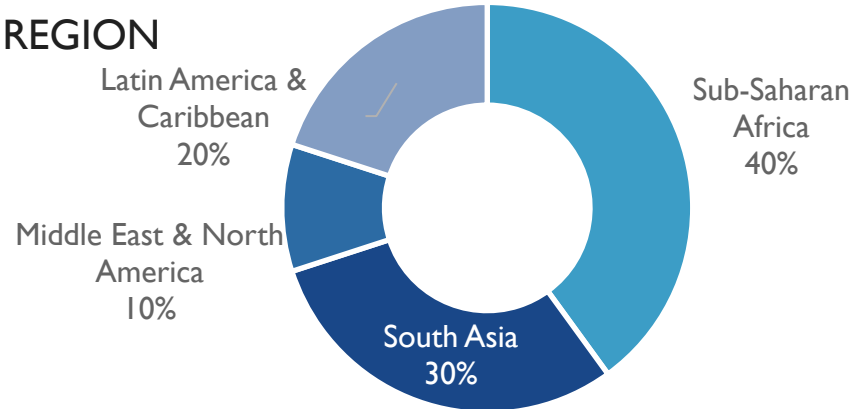
# DIBS IN DEVELOPING COUNTRIES TO DATE – CONVERGENCE HISTORICAL PROJECTS DATABASE



## SECTOR

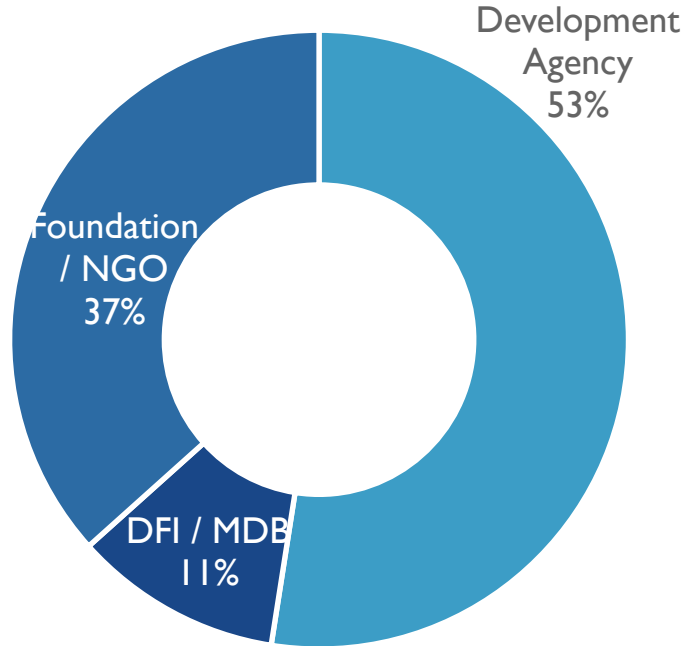


## REGION

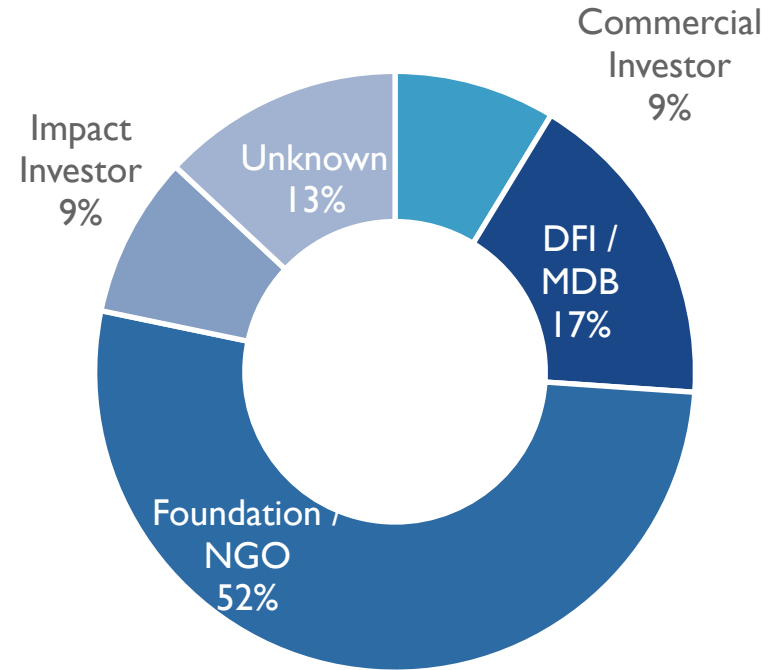


# INVESTORS AND OUTCOME FUNDERS IN HISTORICAL IMPACT BONDS

## OUTCOME FUNDERS



## INVESTORS



# CONVERGENCE FINANCIAL AND EXPERT SUPPORT FOR DIBS

Convergence aligned to IBWG Objective: “*Design and test strategies to make pay-for-success financing instruments cost-effective and scalable to support development agencies and governments to deliver on the SDGs.*” Activities include grants, matchmaking & market building:

## UTKRISHT IMPACT BOND, INDIA

- **Convergence grant to Palladium to complete structuring activities and launch the \$10 million impact bond.**
- DIB funds disbursed to Population Services International and Hindustan Latex Family Planning Promotion Trust to support private healthcare services and facilities to decrease maternal and newborn mortality. Save 10,000 lives.
- Attain level of quality that enables certification under a joint quality standard, and subsequently outcome payment
- Upfront funding provided by UBS Optimus Foundation. Investors will be remunerated by outcome funders, Merck for Mothers and USAID, if services / facilities achieve required quality standards.

## SYRIAN REFUGEE-FOCUSED IMPACT BOND

- **2 Convergence grants to Kois Invest to conduct feasibility study and to fund completion of structuring activities for \$30+ million impact bond.**
- Economic integration for Syrian refugees and vulnerable populations in host countries of Lebanon & Jordan.
- Deploy capital from investors as working capital for refugee livelihoods program for businesses in Lebanon & Jordan.
- Repayment of investor principle and a return component are conditional on the DIB meeting specified business growth targets. A group of outcomes funders to commit to repay program implementation costs and a return to investors contingent on results.

# CONVERGENCE SUPPORTING 3 IMPACT BONDS TO FUNDRAISE ON MATCH-MAKING PLATFORM (CURRENTLY)

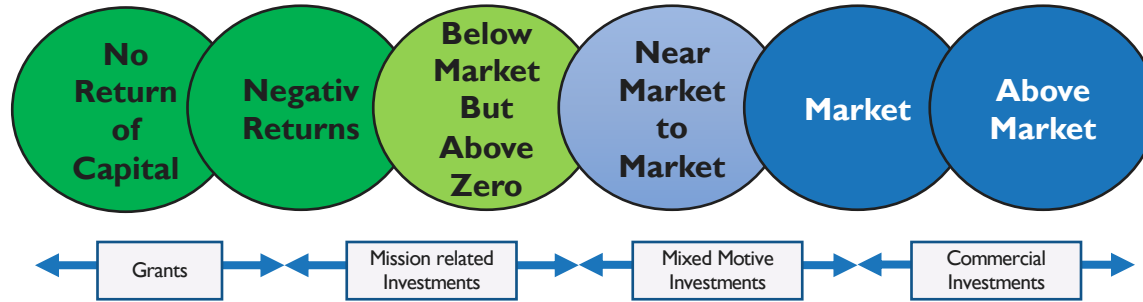
- Kois Invest \$30+ million Development Impact Bonds for Improving livelihoods of refugees and local populations in MENA
- Cardano Development \$11 million Cook & Clean Development Impact Bond
- Rainforest Foundation \$6 million Climate Smart Agriculture Development Impact Bond



ARCHETYPES &  
INSTRUMENTS USED  
IN BLENDED FINANCE

# SPECTRUM OF FUNDING AND CAPITAL TO FINANCE SDG PROJECTS IN DEVELOPING COUNTRIES

Increasing Risk Adjusted Return Mandate and Expectations →



All green is catalytic capital & grants in blended finance

Dark green usually qualifies as Official Development Assistance

Catalytic Grants	Catalytic Capital and Grants - Highly Concessional	Catalytic Capital - Slightly Concessional	Development Finance Institutions Impact Investors	Institutional & Impact Investors Banks Mutual Funds	Hedge Funds Private Equity Funds
Development Agencies Philanthropic Foundations	Global Affairs Canada Innovation Program	Sida Guarantee CDC Catalyst Program	IFC EBRD AfDB FMO DEG	Allianz Prudential HSBC Citibank	Bridgewater Carlyle Blackstone KKR TPG

# BLENDING FINANCE: DEPLOYING DEVELOPMENT FUNDS FOR SDG PROJECTS SUBJECT TO OECD PRINCIPLES

Development Objectives	Primary Archetype(s)
Mobilize additional financing by creating market risk-return acceptable to private investors	Catalytic Capital & Grants: Funded Risk Participation & Unfunded Risk Participation
Reduce up-front or ongoing costs to make an SDG project affordable	Catalytic Grants: Viability Gap Funding & Smart Subsidies
Pay for “social” outcome the project or market can not afford (or will not pay)	Catalytic Grants: Results based Financing, Smart Subsidies & Performance Payments
Support success of SDG project by covering part of the costs or achieve systemic impact beyond individual project	Grants: Technical Assistance
Increase number of SDG related projects	Grants: Viability Gap Funding, Project Preparation & Design Funding
Incentivize innovation and investment into SDGs by committing to pay for results/outcomes (advanced market commitments)	Catalytic Grants: Results Based Financing, Outcome Funding & Pay for Success
Reduce currency risk to make SDG project feasible & sustainable	Currency Risk Mitigation

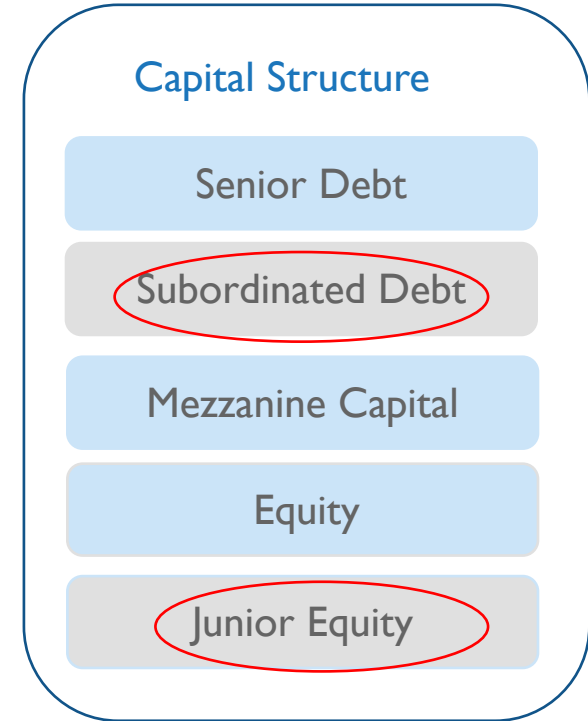


# BLENDING FINANCE: MAIN ARCHETYPES AND INSTRUMENTS

Archetype	Typical Development and Financial Instruments
1. Funded Risk Participation	Investment or Grant: Debt (Loans and Bonds), Mezzanine Capital or Equity
2. Unfunded Risk Participation (Contingent)	Investment or Grant: Guarantee
	Investment or Grant: Insurance
3. Technical Assistance Support	Grant: Technical Assistance
4. Viability Gap Funding, Smart Subsidies and Performance Payments	Grant: Capital Investment and Incentive/Affordability
5. Project Preparation & Design Funding	Grant: Project Preparation or Design Funding
6. Results-Based Financing Outcome Funding	Grant
7. Currency Risk Mitigation	Grant: Similar to Smart Subsidies Risk Sharing: Currency Risk or Credit Risk

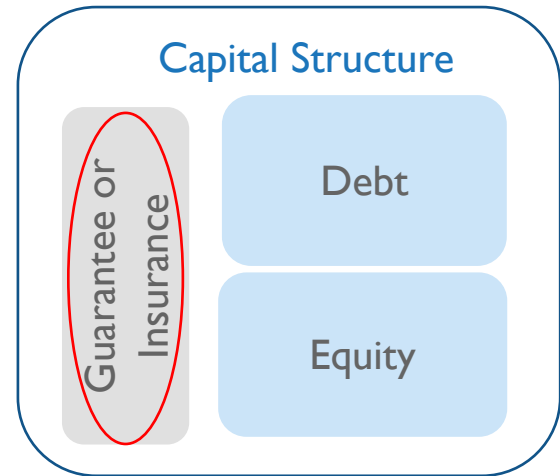
# I. CONCESSIONAL DEBT OR EQUITY

- Concessional debt or equity provide favorable terms of rates relative to market pricing; developmental capital bears non-market risk-return
- Subordinated (debt) or junior (equity) protects senior investors by taking first losses on the value of the security
- The use of direct investment instruments on concessional terms helps shift the risk-return ratio for private investors to an acceptable level
- Concessional finance can help bring down the weighted average cost of capital for a project



## 2. CONTINGENT (UNFUNDED) RISK PARTICIPATION

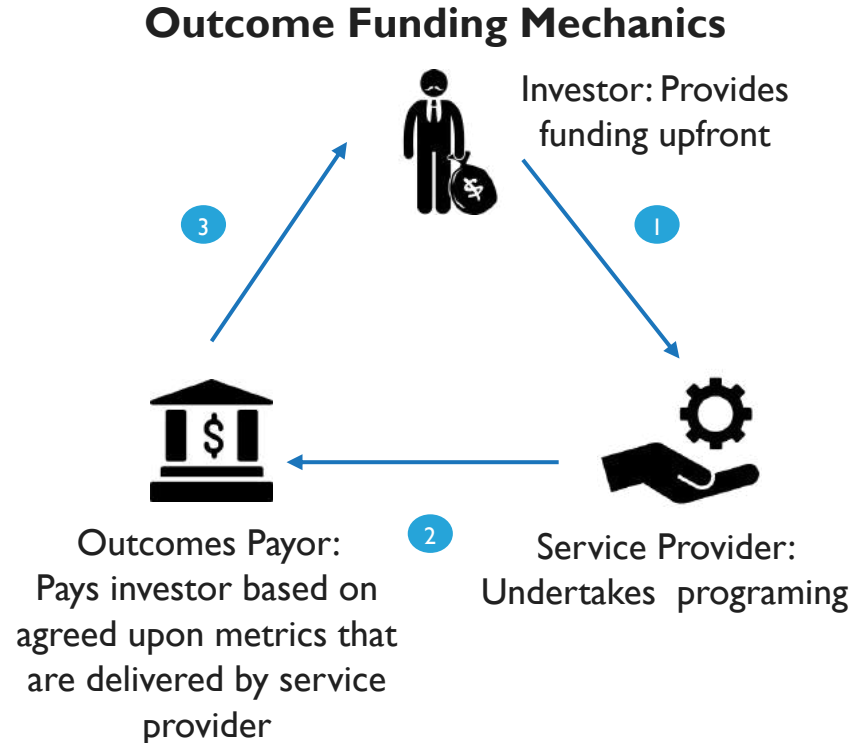
- Risk reduction tools that protect investors against capital losses
  - Guarantee provides protection to investors if guaranteed event occurs (eg: payment default of borrower); Insurance provides protection by promising compensation for specific loss in return for for a premium
- Provides investors secondary level of comfort that investment will be repaid if obligor is not able to fulfill its contractual obligations (payments)
- Lowers cost of financing for obligors as guarantor typically has better credit rating than obligor
- Helps narrow gap between real and perceived risk & typically requires no immediate outlay of cash/capital
- Primarily backstops debt (e.g. loans and bonds) and secondarily other instruments like equity and provide credit enhancements



**AfDB, MIGA, USAID & Sida  
are active users of guarantees  
for development**

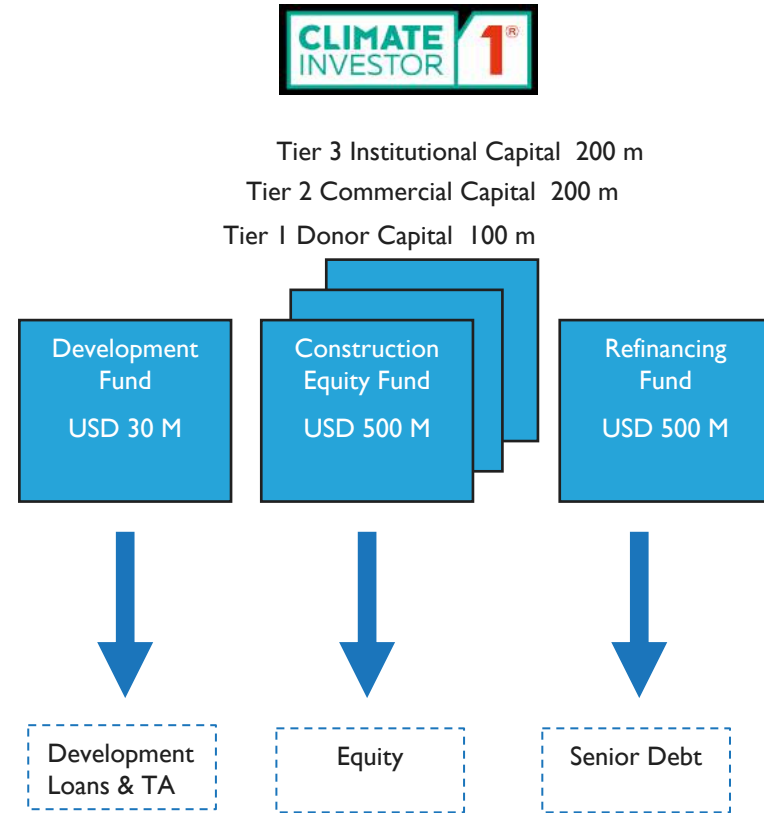
## 6. RESULTS-BASED FINANCING OUTCOME FUNDING

- Donor pays for results instead of paying for inputs
- Payment for service delivery tied to achieving measurable outcomes
- Typically, payor for outcomes (e.g., government or foundation) commits to provide funding if and when the service delivered achieves contracted results
- Examples include Development Impact Bonds (DIBs), Social Impact Bonds (SIBs), Advanced Market Commitments



# EXAMPLE OF CONCESSIONAL DEBT/EQUITY- CLIMATE INVESTOR ONE

- Invest in renewable energy projects that serve 7 million individuals in emerging countries and avoid GHG emissions of 1.2 million tons of CO<sub>2</sub> equivalent
- Offers life-cycle support through three funds that are designed to address barriers specific to each stage
- Mobilizes private sector financing through catalytic public sector funding; investors and donors can participate in a fund and a tranche according to their risk-return profile
- Development Fund comprised of non-repayable donor contributions while Construction Fund has first-loss tranche (Tier I) that is capitalized by donor contributions
- Recently announced third close at USD 535 million

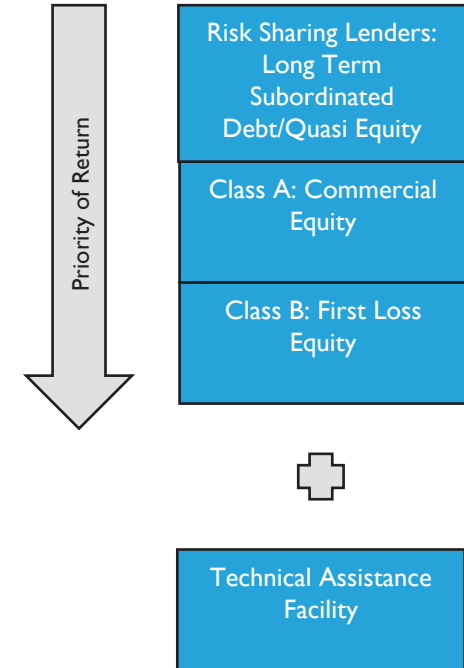


# EXAMPLE OF CONCESSIONAL DEBT/EQUITY: WOMEN'S WORLD BANKING (WWB) CAPITAL PARTNERS FUND 2 (1/2)

- WWB has designed a \$100m blended finance fund that will invest in women focused financial services providers in low-income countries and fragile states
- A concessional first loss equity tranche (\$20M) funded by a development aid agency, will be used to attract commercial investors and DFI's into the Class A tranche (\$50M)
- Fund structure divided into two investment pools to accommodate specific interest in investments in Sub-Saharan Africa; higher risk profile so capital will be drawn and distributed separately
- ~\$28M in commitments till date from EU (\$8M-Class B), USAID (\$0.5M-Class B & \$100K-TA), EIB (\$11.5M-Class A), MEDA-SARONA (\$1M-Class A), BMZ (6M-Class B), GP (\$1M-Class A)

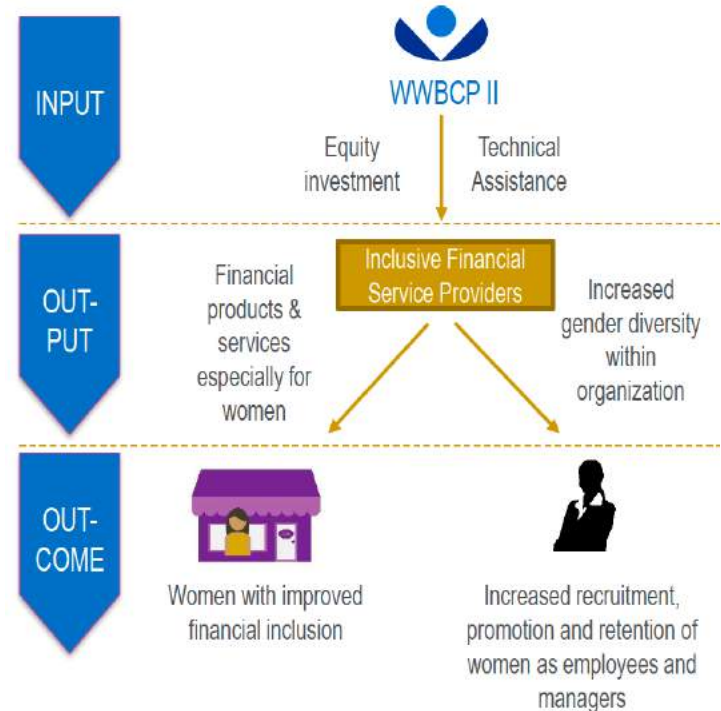


Women's World Banking



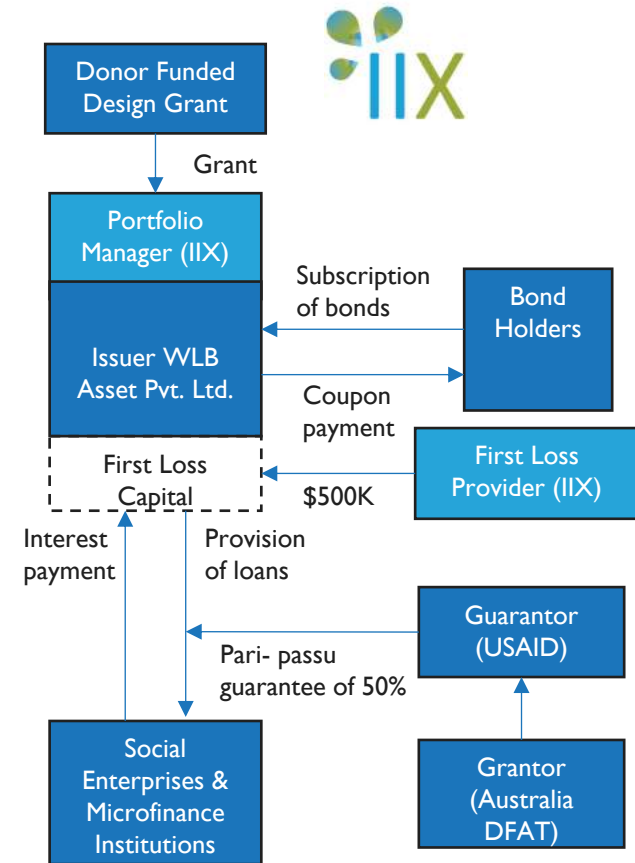
# EXAMPLE OF CONCESSIONAL DEBT/EQUITY: WOMEN'S WORLD BANKING (WWB) CAPITAL PARTNERS FUND 2 (2/2)

- Fund will methodically support its investees in applying a critical gender lens to their operations; creation of Gender Assessment Methodology (GAM) that will evaluate a company's outreach to the low income women's market and the company's own gender diversity amongst staff and leadership
- TA facility will be grant funded and will support the implementation of GAM at the investee level
- Through its Design Funding program, Convergence has provided \$300,000 in grant funding towards fund structuring and publication of the GAM



# EXAMPLE OF CONTINGENT (UNFUNDED) RISK PARTICIPATION- IIX WOMEN'S LIVELIHOOD BOND (WLB)

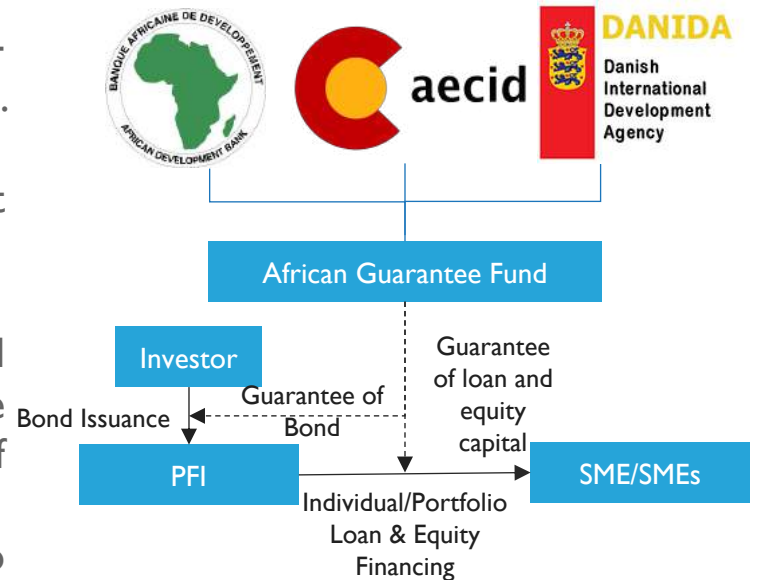
- Innovative instrument that mobilizes private sector capital by pooling loans to social enterprises into a public debt security
- \$8m four-year bond to be listed on Singapore Stock Exchange; proceeds to be lent to social enterprises that focus on empowering women through sustainable livelihoods in SE Asia
- The WLB leverages three blended finance mechanisms
  - 1) Early stage grant funding to support design process (funded by Rockefeller Foundation and Japan Research Institute)
  - 2) Partial guarantee on the underlying loans (provided by USAID-DCA and subsidized by Australian DFAT)
  - 3) Small first-loss capital tranche contributed by IIX
- Looking to target 385K female beneficiaries; Social Return on investment (SROI) will be unique impact metric measured





# EXAMPLE OF CONTINGENT (UNFUNDED) RISK PARTICIPATION - AFRICAN GUARANTEE FUND (AGF)

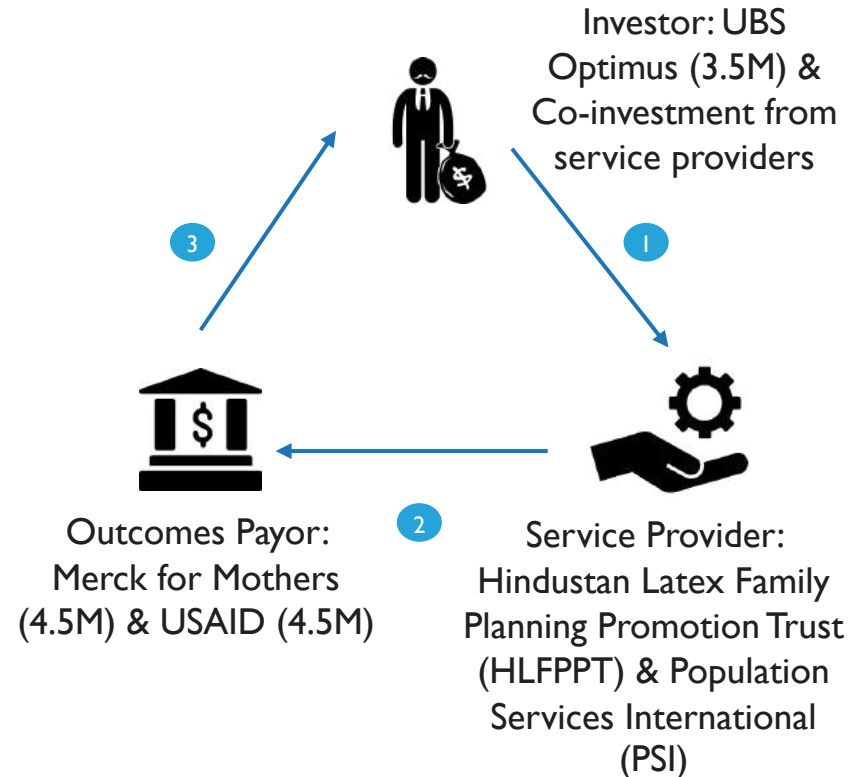
- AGF established to enhance access to finance for SMEs - provide guarantees to Partner Financial Institutions (PFIs). Evolution of USAID DCA.
- Three tiers of capital, including most senior to attract private investment
- AGF provides guarantees to support:
  - (1) Loans made by PFIs to SMEs (on Portfolio & Individual bases)
  - (2) Equity capital financing for SMEs
  - (3) Resource mobilization, i.e. issuance of bonds by PFI's in support of their SME financing activities
- Maximum coverage is 50% of the financing pari passu ; do not cover existing loans to ensure additionality
- At 2018, AGF present in 35 African countries and had signed USD 230 million worth of guarantee agreements



# EXAMPLE OF RESULTS BASED FINANCING: THE UTKRISHT BOND

- 9M three-year impact bond to fund maternal and newborn interventions in Rajasthan
- Investors will fund service providers who will support private healthcare facilities to improve their systems and attain a quality certification
- Investors will be paid by outcome funders upon verification that a facility(s) is ready for accreditation under the new quality standard
- 7.1% expected IRR for UBS Optimus (capped at 8%)
- Projected to impact up to 600,000 pregnant women and save up 10,000 lives over a five-year period

## Mechanics of Utkrisht Impact Bond



# WHAT IS CONVERGENCE?

The Global Network for Blended Finance.

We generate blended finance data, intelligence, and deal flow to increase private sector investment in developing countries.

Not for profit with two sources of funding:

- 1.Revenues and fees for blended finance services
- 2.Grants from governments and foundations

Foundational funding from Global Affairs Canada



Global Affairs  
Canada  
Affaires mondiales  
Canada



## A GLOBAL NETWORK

We have a global [membership](#) of over 200 public, private, & philanthropic institutions



## DATA & INTELLIGENCE

Original [content](#) builds the evidence base for blended finance, including data on past deals, trend reports, case studies, region and sector briefs, and webinars.



## DEAL FLOW

An online match-making platform for investors and those seeking capital to connect on active deals.



## MARKET ACCELERATION

Our [Design Funding](#) program awards grants for the design of innovative vehicles that aim to attract private capital to global development at scale.

# MEMBERSHIP COMPOSITION

Convergence members are part of a global community of institutions and businesses dedicated to driving capital to where it is needed most.

Member institutions include private investors looking to diversify their portfolios, businesses seeking capital, as well as public agencies and philanthropic foundations looking to make their funds go further.

Convergence has over 200 member institutions, and over 570 staff at member institutions actively using the Convergence platform.

