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Time to Accelerate

Capital Mobilisation for the SDGs in Emerging Markets

A Progress Report on the Last Two Years of Capital Mobilisation for the SDGs

Input Paper to the Impact Taskforce

Prepared by the GSG // December 2023

About the Authors

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We want societal and environmental impact to be at the heart of investment and business decisions.

About the GSG

GSG is a global community committed to creating a better and more equitable world for all.

Our mission is to make life better for people and the planet by building impact economies, where impact is as important as risk and return in every policy, business, and investment decision. We firmly believe that, with greater transparency, finance, and business can be a catalyst for transformation and private capital can be a powerful tool for delivering public good. We use our influence to make this happen.

What makes us unique is our global network of affiliated National Advisory Boards (NABs), which address opportunities in their countries and beyond, driving forward global solutions. They are the heart of our movement. There are currently over 40 National Advisory Boards across the globe and we are growing this to 55 countries, covering 2/3 of the world's population. We work collectively to transform systems and advance a shift to impact-led economies at a local and global level. We develop and implement innovative approaches and products that drive investments towards positive impact.

GSG's team supports the development and work of our National Advisory Boards, leverages our collective voice in advocating for impact globally, and advances impact through innovation, knowledge sharing, convening, and collaboration.
We impact through partnerships.

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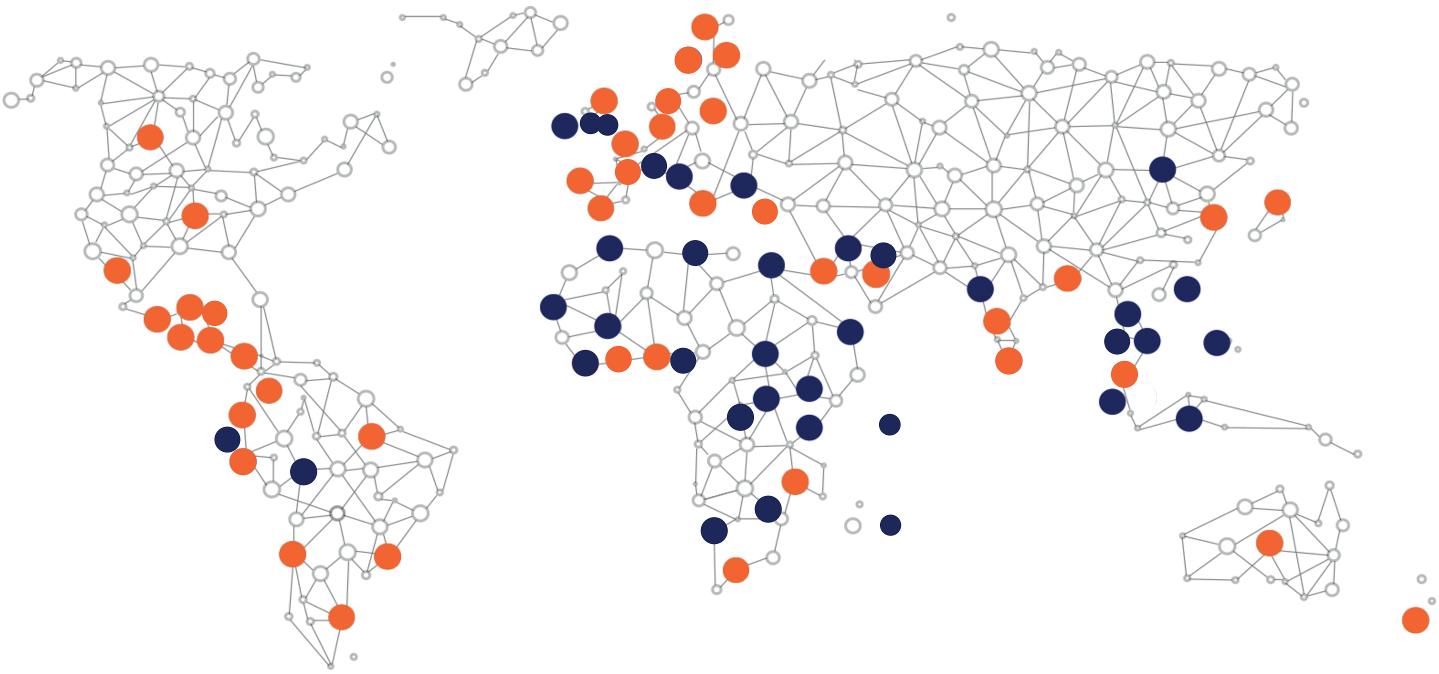

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Acknowledgements

Methodology

Desktop research was carried out by the GSG between May - November 2023. Alongside, the GSG carried out 23 semi-structured virtual interviews via Zoom between June - August 2023. During this period, four Knowledge Partners to the Impact Taskforce (ITF) were selected; the Impact Investment Institute (III), The Blended Finance Taskforce, housed by Systemiq, Convergence, and the Collaborative for Frontier Finance (CFF); each organisation has provided case studies or a standalone input paper to the Impact Taskforce. Two papers were compiled from research gathered, the ITF Annual Report, and this standalone GSG Input Paper. Drafts of both papers were shared with members of the ITF SteerCo and the NABs in October and November 2023, with written comments integrated accordingly.

Acknowledgements

GSG is extremely grateful to the dedicated members of the ITF Steering Committee for their diverse, rich, and insightful guidance and leadership throughout the drafting of this paper. We especially thank the 35 global experts who were generous and giving with their time and shared candid views on capital mobilisation and the reforms needed to make a true and lasting impact. Special thanks go out as well to GSG colleagues who aided in the editing and drafting of this report and to our tireless and passionate Summer Associates Karyn Miller (Said Business School, Oxford University) and Masaya Kobayashi (Cambridge Judge Business School, Cambridge University and JICA). Finally, we convey heartfelt thanks to our reviewers: Laurie Spengler, David Krivanek, Katherine Stodulka, Yvonne Bakkum, and Simon Meads. We are grateful for your comments and nuance, and for holding us to account to create a paper that will help us move the agenda forward. The list of contributors can be found at the end of this report.

ITF Knowledge Partners

We recognise the rich and thoughtful insight provided by our fellow ITF Knowledge Partners:

The Impact Investing Institute was launched in 2019 with a mission to accelerate the growth and improve the effectiveness of the impact investing market in the UK and internationally. Its vision is for capital markets to be fairer and work better for people and the planet, in order to deliver sustainable and inclusive economic growth. The Impact Investing Institute is GSG's affiliated UK National Advisory Board (NAB).

The Blended Finance Taskforce hosted by Systemiq was Established in 2017 to help mobilise large-scale capital for the UN Sustainable Development Goals (SDGs). The Blended Finance Taskforce is advancing an ambitious Action Programme to increase mainstream private investment for high-impact sectors, with a focus on emerging markets. A certified B Corp, Systemiq is a highly collaborative system designer, developer and disruptor.

Convergence is the global network for blended finance. The organisation generates blended finance data, intelligence, and deal flow to increase private sector investment in developing countries.

The Collaborative for Frontier Finance is a multi-stakeholder initiative that aims to increase access to capital for small and growing businesses in emerging markets.

Executive Summary

The SDG and Just Transition financing gap has increased, and capital is still failing to go where it is needed, at the volumes required.

- The COVID-19 pandemic has widened the financing gap to meet the SDGs, with the world also off-target to meet the 1.5C temperature increase goal laid out by the 2015 Paris Agreement. An estimated $40-60 trillion is needed over the next five years alone to address pressing environmental and social challenges
- Climate finance broke through the $1 trillion mark in 2022, but remained a fraction of fossil fuel subsidies that still amount to $7 trillion as economies contend with inflation and the impact of conflict in Ukraine on energy supply
- Renewed market volatility and rising interest rates have put pressure on investor appetite for EMDE assets, meaning that international investment is failing to reach the geographies that need it most. Only 13% of global climate finance is going to EMDEs and private finance to EMDEs (excluding China) is estimated to have declined by 22% from 2021 to 2022
- Governments and institutional investors have acknowledged the importance of a Just Transition to Net Zero. However, initiatives have yet to deliver on promises and have largely failed to integrate social considerations (i.e. the ways in which climate change will affect jobs, access to water, food, and other resources, human security and livelihoods) into environmental and climate targets
- DFI and MDB mandates and investment practices are evolving but have been slow to mobilise private capital through appropriate investment opportunities. In 2021, their efforts only mobilised $40 billion of private investment in EMDEs, down from prior years. With less than $1 of private capital mobilised for every dollar invested by DFIs and MDBs, these institutions are under increasing pressure from the G7, G20, EMDE policymakers, think tanks, and other actors to mobilise significantly more private capital to deliver higher development impact.

DFIs and MDBs remain the best-placed organisations to mobilise private capital, and have the tools at their disposal, but must undergo a mandate change to meet their potential.

- DFIs and MDBs need to rethink their traditional origin-to-hold strategy and take higher levels of financial risk. In doing so, they can generate more investment opportunities for institutional investors
- Larger DFIs and MDBs can also select and bundle pools of assets, which can be sold or securitised to free up their balance sheets for further investment
- Increased use of blended finance and guarantees that shield institutional investors from losses can de-risk investments and encourage the flow of private capital into EMDE opportunities. At the same time, better understanding and mitigating of currency risk, as well as better access to performance data can help investors address real and perceived risks, especially when it comes to investments in EMDEs
- Only 18% of financial instruments in DFI and MDB portfolios have private capital mobilisation as a main objective, meaning that mandates must be reformed to incentivise and drive private capital participation. Efforts are underway at both G7 and G20 levels but must be accelerated to address the urgency of unlocking investment for the SDGs, of which only 12% are on track.

Focus and support need to be directed to domestic EMDE initiatives, delivering locally relevant solutions for SDG investments and offering opportunities at scale to unlock further institutional capital.

- EMDE pensions are growing rapidly and are among the highest priority routes to unlock private capital for domestic investment. Local players have a stronger understanding of their domestic markets and invest in local currency, which is often more secure for recipients of investment
- Public Development Banks hold over $23 trillion in assets but need to work more closely with investors to promote opportunities that support the SDGs and Just Transition. Their local knowledge and relationships can act as a catalyst to encourage and mobilise domestic and international private capital investment
- EMDE impact fund managers and funds of funds are critical to direct capital where it needs to go. Such funds can address investor challenges around scale and access to a pipeline of opportunities in critical small and growing businesses
- Domestically-led initiatives, such as those led by the GSG-affiliated National Advisory Boards (NABs) in Ghana, Nigeria or Zambia, are a great example of collaborative efforts, connecting public and private finance with the demand side, solving for the multiple issues around SDG finance in EMDEs at once.
- It is time to structure new catalytic capital facilities. Echoing calls to action in the ITF Annual Report 2023, we encourage new facilities to be set up to invest for high impact in priority areas, such as facilitating access to appropriate capital for job-creating micro-, small, and medium-sized enterprises (MSMEs).

Recommendations

MDBs, DFIs, INVESTORS, AND CATALYTIC CAPITAL PROVIDERS: Support, collaborate with and invest in financing structures and initiatives led and developed by domestic stakeholders in EMDEs, aimed at improving access to finance for SMEs and the achievement of the SDGs. Specifically, increase the supply of catalytic capital in EMDEs, with the view of creating regional catalytic capital facilities that would boost such domestic solutions.

MDBs, DFIs, AND THEIR SHAREHOLDERS: Material reform of DFIs and MDBs, ensuring clear capital mobilisation strategies, with ambitious targets, moving them from less than 1X to multiplied mobilisation ratios that will allow greater impact to be achieved within the next 5 years, and transparency and accountability enshrined in their mandates.

MDBs, DFIs, AND CATALYTIC CAPITAL PROVIDERS: Systematic and more efficient use of de-risking mechanisms, including the scaling up of existing successful facilities, to leverage private capital investment and increase the number, size and quality of investable opportunities aligned with the SDGs in EMDEs

MDBs, DFIs, AND CATALYTIC CAPITAL PROVIDERS: Unlock data and evidence about financial and impact performance of investments in EMDEs. Specifically, DFIs and MDBs should keep to the proposed timeline of making the GEMs database available to third parties early 2024, allowing investors to make better informed investment decisions.

Introduction

There will never be enough public money to achieve the UN Sustainable Development Goals and ensure a Just Transition. That was the starting point for The Impact Taskforce's (ITF) work two years ago and it is as true today as it was then. In contrast, upwards of $230 trillion is traded annually in the capital markets[1] and institutional investor appetite to deploy capital into investments with environmental, social, and governance (ESG) and impact objectives is growing. The inescapable conclusion is that only private capital, often layered with public or philanthropic capital, has the capacity to support projects and initiatives that will drive the world towards Net Zero[2] and ensure that no one is left behind.

ITF 2021 Workstream B posed the question
How can we accelerate the volume and effectiveness of private capital seeking to have a positive social and environmental impact in emerging markets and developing economies?

The answer focused on the creation of clearly defined investment opportunities within institutional structures that meet investors' fiduciary requirements. It highlighted Multilateral Development Banks (MDBs), Development Finance Institutions (DFIs), and institutional investors as key actors with the potential to bridge the aspirations of policymakers with the needs of vulnerable communities and a dramatically changing planet. It spotlighted emerging markets and developing economies (EMDEs) where investments are often smaller, markets less liquid, and hence perceived as more challenging for institutional investors to invest in.

Two years on, findings show the volume of private capital being mobilised is insufficient to address today's environmental and social challenges and that its trajectory falls far short of what is needed to meet the SDGs and global climate goals. Moreover, EMDEs continue to lag behind in allocated capital to finance the SDGs, leaving the very populations most at risk of climate change with few resources to combat it.

So now the question more pointedly becomes:
How can we realise the full potential of DFIs and MDBs to mobilise private investments for positive impact on the SDGs and a Just Transition in EMDEs?

Our report examines the role of DFIs and MDBs in mobilising private capital and how changing their mandate and allowing them to take on more risk can stimulate and facilitate more private investment.

Critical as they are, these finance institutions are not the only part of the puzzle. Domestic EMDE capital sources, such as pension funds and public development banks with national financing agendas, are among the best-placed to support SMEs that are the lifeblood of their economies and have a central role to play in delivering the SDGs and a Just Transition.

This report examines the evolution of the financing challenge facing the world and the role of key actors in mobilising private capital in EMDEs. It provides recommendations for accelerating investment where it is needed most.

The good news is that most of the structures and tools needed to mobilise private capital at scale already exist. Moreover, many are already in use, with private investors increasingly shifting allocation strategies towards achieving sustainability and impact outcomes. Better apportioning and understanding of risk can help break down the barriers that are holding back investment in EMDEs, just as better use of resources at a domestic level can unlock the capital that can support home-grown companies well-positioned to support a Just Transition and the achievement of the SDGs.

The time for discussion and debate has long passed. The time for urgent action at scale is now.

CHAPTER 1

Meeting the SDGs and Achieving a Just Transition: The Target Is Moving Farther Away

Key Messages

- ▲ Markets need to move from a narrative of need to one of opportunity
- ▲ Investors and investment managers must integrate social with environmental objectives in all climate investments
- ▲ Investment managers should work with and engage affected communities and key stakeholders in Just Transition initiatives

1.1 Investment Still Misses the Mark and Fails to Tackle Social Dimensions of Climate Change

$60tn
p.a. needed in the next 5 years to address social and environmental challenges

1.1.1 Global Just Transition funding gaps widen as fossil fuels subsidies continue

In the last two years, private capital mobilised for the UN Sustainable Development Goals has dropped whilst environmental and social challenges have increased. The COVID-19 pandemic delivered a major setback to global poverty reduction efforts while global warming has continued unabated.[3] The latest IPCC report released in April 2023 places us on a path toward 2.3C temperature by 2050.[4] The time to course correct is now. The longer we wait, the more constrained and limited our responses will be.[5]

The costs of addressing climate change and putting the world back on track to meet the SDGs are vast. Estimates put the annual investment requirement at $8-12 trillion over the next five years, equating to $40-60 trillion over that period alone.[6]

Changes in market conditions over the last two years, including higher interest rates and higher exchange rates have further deterred global investors from investing in emerging markets. Private finance to emerging markets and developing economies (EMDEs), excluding China, is estimated to have declined by 21%.[7] Furthermore, restrictions put in place during the financial crisis, such as quantitative limits, capital and solvency considerations, and valuation methods, are hindering allocations to emerging markets.[8] (See **Table 1**)

Public aid to developing countries, or official development assistance (ODA), is sizable and amounted to $204 billion in 2022.[9] However, it is ultimately insufficient to make the difference needed. To reach the sums that are needed capital must be brought in greater quantities and through more ambitious initiatives.

$1tn Climate finance VS **$7tn** Fossil fuel subsidies

Global climate finance was reported to have passed the $1 trillion mark for the first time in 2022,[10] but pales in comparison to fossil fuel subsidies which stand at $7 trillion, up $2 trillion since 2020.[11]

Furthermore, the social dimensions of climate change are still not sufficiently integrated into climate strategies. In much of the world, jobs and training opportunities are still heavily reliant on the fossil fuel industry, and failure to take that into account has led to backlash from people who see the path to decarbonising the economy as a threat. This has resulted in a pushback from investors, businesses, and the general public to implement environmental, social, and governance (ESG) considerations in their investments. Even national governments once committed to net zero are now rolling back their commitments, yielding to public opinion, 'sowing uncertainty and instability that could hinder regulatory advances precisely when they are needed most.'[12]

TABLE 1

Zoom in on Africa - a region where more needs to be done towards a Just Transition

	Africa
Annual GDP loss because of Climate Change	up to 15%[13]
FDI flows in 2022	-44%[14]
Total AUM in 2021	$1.5 trillion (1.4% of global AUM)[15]
ESG AUM in 2021	$0.1 trillion (0.5% of global ESG AUM)[16]
Climate Finance needs p.a (2022)	$280 billion[17]
Climate Finance p.a (2021)	$30 billion[18]
Share of global renewable investments (2021)	0.6%[19]

1.1.2 Climate finance is missing in Emerging Markets and Developing Economies where it is needed most

13%
of climate finance goes to EMDEs

$2 tn
market value of climate adaptation in 2026

Climate finance is not only far below needed levels, but it is also not flowing to where it is needed most. The Blended Finance Taskforce estimates that over 75% of climate finance pledges are not deployed.[20] Of the money that has been mobilised, only about 13% of global climate finance flows to EMDEs,[21] regions known to be the most vulnerable to climate change.[22] And the capital reaching those countries is only a fraction of what is required. EMDEs require about $2.2 trillion in investment per year to support their energy transition needs.[23] In comparison, in 2022, only $544 billion in investment flowed into renewable energy projects in EMDEs, according to estimates.[24]

Renewable energy is an important part of the puzzle for climate change-resilient economies, but investment in climate adaptation is more likely to determine people's ability to live and prosper safely and sustainably in their countries and communities.[25] Adaptation initiatives like the construction of sea defences, resilient buildings, environmental restoration, or drought-resistant crops, currently represent only 7% of climate finance.[26] In EMDEs, climate adaptation costs are expected to reach $160-340 billion per year by 2030,[27] but climate adaptation also represents a potential market of $2 trillion pa through 2026.[28]

We, therefore, must move away from a discourse of need to one of opportunity if we truly want to move private investors to allocate more capital to achieving a net zero future and a Just Transition.

1.2 Governments and Private Investors Send Positive Signals, But Action is Lagging

1.2.1 Positive signals from government and investors

Governments in developed markets have sent strong signals that achieving a just transition is becoming a key priority, and have introduced large-scale industrial policies. The European Union's **$827 billion European Green Deal** aims to make the EU climate-neutral by 2050 while promoting sustainable economic growth.[29] And the US's **$500 billion Inflation Reduction Act**, introduced in 2022, sets the stage for the largest level of climate investment in US history.[30]

Constrained by growing debt burdens, many EMDEs lack the resources and capabilities to replicate similar strategies in their home countries. The Bridgetown Initiative, an initiative calling for reform of the global financial architecture signed in Barbados in July 2022, signalled a **stronger and more unified stance in EMDEs to create a more equitable and fit-for-purpose financial system** that would unlock financial resources needed to support decarbonisation initiatives in EMDEs. It was followed by the Summit for a New Global Financial Pact held in Paris in June 2023, which sought to encourage more financial solutions toward allocating domestic and international resources to addressing poverty, curbing emissions, and elevating the importance of protecting nature in EMDEs.

Private sector actors, including asset owners, asset managers, and corporates have added their voices with pledges for sustainable action. Collaborations such as Business for Inclusive Growth (B4IG), the Global Investors for Sustainable Development Alliance (GISD), the Financial Centers for Sustainability (FC4S), as well as the Sustainable Markets Initiative (SMI), the Investors Leadership Network (ILN), the Blended Finance Taskforce, the Institute of International Finance (IIF), and more have raised awareness and driven peer-led momentum and coordination.

Unfortunately, most private initiatives have been slow to deliver. The Glasgow Financial Alliance for Net Zero (GFANZ) was launched in April 2021 by UN Special Envoy on Climate Action and Finance Mark Carney and the COP26 presidency to unite net-zero financial sector-specific alliances from across the globe into one industry-wide strategic alliance. To date, its 550 members have pledged $130 trillion of private capital to decarbonise the economy. Similarly, 12 UK pension funds representing $501.6 billion (£400 billion) of assets under management have committed to supporting the climate transition in emerging markets.[31] However, progress has been slow and such coalitions have been criticised for not working more systematically to create stronger collaborations with non-financial actors, namely, non-profits, citizen action, and civil society groups, whose voices and experiences must also be involved in shaping the solutions, whilst showing little progress on promised deliverables. Critics have expressed further dismay over members of GFANZ continuing to fund fossil fuels.

Similarly, government-led proposals are held back by political disagreement. COP27 in November 2022 resulted in the establishment of a Loss and Damage Fund to help channel money from the world's largest emitters to those suffering the worst climate effects, arguably, 'one of the most significant breakthroughs in the climate negotiations of the past 30 years.'[32] However, one year on, national governments remained sharply divided on where the fund should be based and which countries should be required to contribute to it.

> With JET-P, we have to build the ship as we fly it. But the need remains capital, especially flexible capital that can be used to encourage innovation.
>
> **Adviser, Donor Agency**

1.2.2 Public climate-focused initiatives show promise, but mobilisation levels remain low

Responding to EMDEs' call for enhanced support, G7 countries have responded with new packages to mobilise private capital, announcing Just Energy Transition Partnerships (JET-P). Just Energy Transition Partnership (JET-P) initiatives starting in South Africa, and later announced for Vietnam, Indonesia, and Senegal aim to link national infrastructure development and decarbonisation plans with public and private financing. The precise aims of each JET-P differ from country to country. For example, while South Africa and Indonesia's packages both aim to expand renewable energy, South Africa's JET-P focuses on the substitution of renewables for coal, while Indonesia focuses on increasing the share of renewables. (See **Table 2**)

These initiatives aim to mobilise private capital but have not delivered a clear implementation strategy on how to do so. They have also been criticised for missing an appropriate social and community voice component and would do better if led and driven forward by host governments, anchored within their own domestic priorities.

TABLE 2

JET-P Packages by Country and Amounts Pledged

Country	Amount Pledged
South Africa	$8.5 billion[33]
Vietnam	$15.5 billion[34]
Indonesia	$20 billion[35]
Senegal	$2.7 billion[35]

Despite the challenges, more JET-Ps are being explored for a broader range of goals. The first non-coal JET-P was announced at COP27 in November 2022 to focus on water, food, and energy (WFE) security in Egypt.[37]

BOX 1

Zoom in on Solutions - The Blended Finance Taskforce Donor Principles for Climate Finance

The Blended Finance Taskforce offers a set of principles in "Making Climate Capital Work" for equitable, catalytic and fit-for-purpose JET-Ps which builds on the ITF's approach to JET-Ps. ITF partners – BII, NinetyOne and the Blended Finance Taskforce also developed a set of just transition Principles for Africa.[38]

DONOR PRINCIPLES TO ENSURE CLIMATE FINANCE COMMITMENTS ARE FIT-FOR-PURPOSE

- Embed transparency & accountability into climate pledges, specifying the source and type of funds and establishing disclosure & reporting requirements
- Establish donor coordination & standardisation mechanisms to reduce transaction costs and streamline deployment, avoiding unnecessary burdens on South African counterparts
- Make greater use of catalytic instruments to ensure pledges are fit for purpose to solve the challenges at hand, which include just transition funding, debt sustainability, capacity building to strengthen the enabling environment, and mobilisation of private capital
- Deploy donor funding in a way that is complementary and coordinated with other catalytic capital, including philanthropic funds, to deliver scale and accelerate just transition outcomes
- Ensure funding allocation is demand-driven, responding to domestic market and political structures. Take a whole-of-society approach, fostering multi-sectoral engagement, prioritising local partnerships and capital mobilisation, and engaging communities as engines for lasting social impact
- Shift decision-making power in the development finance system, establishing robust and inclusive principles of cooperation and capital deployment
- Integrate environmental and social objectives, acknowledging that both are necessary to achieve a sustainable and inclusive transition

Source: Blended Finance Taskforce (2022)

Public Private Partnerships (PPPs) have also been a key strategy adopted by governments to mobilise capital for a Just Transition. PPPs advance strategic investment opportunities in priority sectors and often help to streamline project procurement and other regulatory processes that might otherwise drag on over time.

A promising model includes the Institutional Investor-Public Partnerships (IIPP) Legal Regulatory Framework, developed by the African Green Infrastructure Investment Bank (AfGIIB) and Africa Investor. These partnerships between government and institutional investors are specially designed to fast-track, de-risk, and scale private capital participation in green infrastructure projects.[39] IIPPs have been endorsed in the New Financial Pact Summit private sector recommendations as a means of mobilising private capital at scale in EMDEs, paving the way for further adoption and scale across African countries.[40]

Public (National) Development Banks are already driving a number of Just Transition initiatives, and require further support and engagement to partner with international investors. (See more on National Development Banks in Chapter 3). The Initiatives in **Table 3** highlight notable examples.

TABLE 3

Examples of Just Transition Instruments and Initiatives by PDBs[41]

Financiera de Desarrollo Nacional (FDN)	Colombia	FDN is a private, specialised, technical and independent development bank that invests in the infrastructure sector. In August 2023, FDN signed a USD $98 million of credit agreement with the French Development Agency ('AFD') to finance electric mobility projects. FDN has started disclosure aligned with SASB and TCFD sustainability/climate disclosure frameworks since 2022.
PT Sarana Multi Infrastruktur (Persero) (PTSMI)	Indonesia	PT SMI is a state-owned development bank that supports infrastructure development, especially through the Public-Private Partnership (PPP). PT SMI was appointed as the Country Platform Manager (CPM) Energy Transition Mechanism (ETM) at the G20 Indonesia in 2022. This new mandate gives PT SMI the authority to push energy transition policies in Indonesia and seek creative financing sources that address the positive impact on economic, social and environmental aspects.
Development Bank of South Africa (DBSA)	South Africa	DBSA is a government-owned development finance institution with the mandate to promote economic growth as well as regional integration for sustainable development in South Africa and other African nations. At COP27 in 2022, DBSA agreed to European Investment Bank (EIB) financing in South Africa, aiming to unlock $416 million (€400 million) for private sector investment in renewable energy across South Africa.
National Bank for Financing Infrastructure and Development in India (NaBFID)	India	NaBFID was established in 2021 as a national development bank to fill the gap in infrastructure financing in India through the development of innovative financing instruments and deep bond and derivatives markets. NaBFID signed a MoU with IFC in June 2023, aiming to identify and develop PPP projects in alignment with the national target of achieving economic growth while ensuring low-carbon and climate-resilient growth. NaBFID also issued its first bond in the public market in June 2023.
Development Bank of Rwanda (BRD)	Rwanda	In July 2023, the World Bank issued a new $100 million line of credit to support the development of a Sustainability-Linked Bond (SLB) instrument to be issued by the Development Bank of Rwanda (BRD) in local currency, a first for a World Bank. Part of a wider SLB issuance program, the support is designed to strengthen the institutional capacity of Rwanda's public development bank by helping to diversify its funding sources via capital markets while maintaining its role and commitments to local sustainable economic development.

Finally, some EMDE governments are embracing Green, Social, Sustainability and Sustainability-linked (GSSS) bonds to finance sustainable development. Among EMDEs with eligible credit ratings, Chile has been a leader in the field. Since the debut of its first GSSS bond in 2019, it has raised more than $38 billion through a combination of the products. In 2023, the Ministry of Finance plans to raise at least two-thirds of its $15 billion planned bond issuance from GSSS bonds, including $7 billion from Sustainability Linked Bonds (SLBs). This strategy has allowed Chile to tap into an increasingly diversified investor base, and achieve the lowest yield for a sovereign bond in Latin America.[42]

By issuer type, EMDE sovereigns accounted for 13% of GSSS issuances since 2014, (financial institutions responsible for 41% of issuances and corporates 37%,)[43] attracting capital for sustainable development goals with coupons on the debt tied to the achievement of green or sustainability-linked KPIs.

These innovations and initiatives demonstrate that investment is going towards the SDGs and a Just Transition. They also show public and private actors working together, mobilising private capital to make a difference in EMDEs.

However, the capital being raised and deployed is far from the levels needed to ensure that goals are met and no one is left behind. Moreover, the DFIs and MDBs that were identified in the ITF's 2021 report as key mobilisers of private capital have yet to step up to the challenge.

1.2.3 The social dimensions of climate change are still not sufficiently integrated into private investments

Finance for a just energy transition will be a primary driver of private capital mobilisation in EMDEs. We continue to argue that support amongst impacted communities, trade unions, politicians, and other domestic key stakeholders will be essential to delivering a Just Transition. Words need to be underpinned by visible flows of social investment to support the communities most vulnerable to job losses in the transition and the physical risks of climate change.

While the appetite to invest in the Just Transition has been growing, many businesses and investors still need practical guidance on what it means and how to do it. Responding to that knowledge gap, market builders like the **Impact Investing Institute (GSG's affiliated UK NAB) and The Blended Finance Taskforce have worked with asset managers** to further their understanding of the Just Transition and the linked nature of social and environmental issues, and to give them the tools to develop investment vehicles that can attract and deploy private capital. The **UN Global Compact's Think Lab has done the same for businesses.**[44]

BOX 2

Investors are increasingly incorporating Just Transition investment strategies

- **Just Climate's Climate Asset Fund I**, established by Generation Investment Management, targets asset-heavy and hard-to-abate industries with high transition potential. Its new investment strategy explains how the firm is incorporating Just Transition into its investment portfolio
- **PIDG's new 2023-2030 investment strategy** is premised on promoting social outcomes as much as climate-related objectives through its infrastructure projects. The firm has also committed to engaging more with local communities, as well as youth to ensure projects are shaped with the needs and concerns of local residents
- Backed by the U.S. Agency for International Development (USAID), with the support of Amazon, **The Climate Gender Equity Fund**, 2X Global's latest initiative, aims to invest $60 million to increase access to climate finance for gender-responsive, women-led, and women-benefiting organisations that address climate change

BOX 3

Zoom in on Solutions - Impact Investment Institute's Just Transition Finance Criteria and Handbook for Engaging Communities in Place-based Impact Investing

Heeding the need for practical guidance, in 2022, the Impact Investment Institute, GSG's affiliated UK National Advisory Board for Impact Investing, launched the Just Transition (JT) Finance Challenge. The Challenge builds on III's co-leadership of ITF 2021 on capital mobilisation in emerging markets. It brings together 24+ global financial institutions with over $6.27 trillion (£5 trillion) of assets under management that are committed to financing a Just Transition in developed and emerging markets. JT Finance Challenge participants have co-designed a set of Just Transition Criteria, a tool for fund managers to design and structure investment products.[45]

Just Transition Criteria provide a tool for designing new products, adapting existing products to deliver Just Transition outcomes, and identifying and engaging with underlying investments according to their contribution to Just Transition outcomes. They are applicable to investments in all asset classes.

The Criteria also provide a useful framework that asset managers can use to embed Just Transition considerations into formalised communications with distributors and reporting in relation to the positive (and potentially negative) outcomes of investments.

The Criteria are composed of three Elements that constitute a common frame of action for all actors who are instrumental in mobilising capital for a global Just Transition. An overarching principle is that, regardless of the primary area of priority of the chosen strategy, all three Elements must be present to qualify as a Just Transition investment.

JUST TRANSITION CRITERIA

Timeframe

Element 1
Advance climate and environmental action

Element 2
Improve socio-economic distribution and equity

Element 3
Increase community voice

Product (T)

Criterion 1: There is a product-level commitment to the three Just Transition Elements

Demonstrated via, e.g., a theory of change, commitment statement or investment objective and supported by a description of the processes applied to investment selection, monitoring and divestment - see Criteria 2 and 3

Criterion 2: Each investment within the product is assessed to avoid harm to any of the three Elements

Demonstrated via selected disclosures and indicators and, where appropriate, identified safeguards

Criterion 3: Through its investments, the product makes a positive aggregate contribution to all three Elements and, over time, each underlying investment contributes to all three Elements

Demonstrated via selected KPIs at product and investment level

Product
(T+N* years)
*N defined as part of Criterion 1

Product seeks to deepen and broaden aggregate positive contribution to all three Elements at product-level and at the level of each underlying investment

The Institute's ambition is that, in the next five years, 50% of the estimated $2.8 trillion invested in sustainable funds focused on climate incorporate Just Transition considerations using the Just Transition Criteria.

The Institute is piloting the Criteria with a number of asset managers and also engaging with actors such as catalytic capital providers to ensure part of these funds also supports a Just Transition in EMDEs.

Complementing III's JT criteria, investors can also refer back to a roundup of community voice tools and frameworks, referenced in the 2021 ITF Workstream B paper. They also provided examples of Just Transition financing strategies and examples of what good JT vehicles across asset classes look like. More recently the III also released a new handbook for guiding investors on how to integrate community voice in place-based Investments. *Fostering Impact: An investor guide for engaging communities in place-based impact investing*[46] empowers investors to identify and pursue community engagement opportunities within a place-based impact investment approach. It lays out different ways and methods of incorporating community engagement into investment decision-making.

A STEP-BY-STEP GUIDE FOR DOING COMMUNITY ENGAGEMENT

Planning community engagement	What does **good community engagement** look like? What **role** should the investor play in community engagement?	
	Direct community engagement	**Community engagement through others**
	What is the **purpose** of the engagement? What is the **public participation goal** of the engagement? What is the **scale** of the engagement? What **outcomes** and **outputs** should the engagementproduce? What are the **timescales** for the engagement? What **information** already exists? What **resources** are available? How will success be **measured**?	Through intermediaries (e.g., by **engagingthe fund manager** or **management of an investee or asset**)
Delivering community engagement	**Who** should be engaged? Who can be a suitable**partner**? Which **method(s)** should be used? How should investors **communicate** with the communityengaged?	
Sustaining community engagement	How can investors **embed** community engagement in their activities? How can investors **communicate externally** about their community engagement?	

Source: III (2023)

Recommendations

INVESTORS: Systematically consider both social and environmental objectives in all investments. Specifically, social objectives need to be included in all climate investments. All funds aimed at fighting climate change should include Just Transition criteria (such as those developed by the III), with both social and community dimensions, by end 2025.

INVESTORS: Work with and engage impacted communities and other key local stakeholders in all Just Transition initiatives and investments.

ALL PLAYERS: Move from a narrative of need to a narrative of opportunity. Investors specifically should become more proactive in investing in SDG aligned EMDEs opportunities, as many are already aligned with their risk-return-impact expectations.

CHAPTER 2

Development Finance Institutions Hold the Key to Unlocking Private Capital

Key Messages

- DFIs, MDBs and PDBs urgently need mandate reform alongside change in strategies and operations to be able to scale up private capital mobilisation
- Private capital often requires more de-risking in EMDEs, and guarantees and blended finance are proven tools that work to support such investments
- DFIs, MDBs and government shareholders must share essential data - making the GEMs database accessible - for better investor understanding of risks and rewards in EMDEs, and boosting capital allocation

MDBs and DFIs are vital for mobilising private investment flows to EMDEs, where financial markets are still developing. While precise private capital mobilisation mandates differ by institution, DFIs invest in sectors and industries critical for sustainable development (e.g. energy, infrastructure, banking, health, etc.) and support regional cooperation, economic integration, and intra-regional trade within the region or between states.

BOX 4

Defining Capital Mobilisation

Private capital mobilisation refers to additional financing from private sector entities that occurs because of a bilateral or multilateral development bank (MDB), or development finance institution (DFI)'s investment. Two definitions are generally used by practitioners:

- **MDB Harmonised Definition**: The sum of private direct and indirect mobilisation, where direct refers to financing from a private entity on commercial terms due to the active and direct involvement of an MDB leading to commitment and indirect refers to financing from private entities provided in connection with a specific activity for which an MDB is providing financing where no MDB is playing an active or direct role leading to the commitment of the private entity's finance.[47]
- **OECD**: the ways in which specific mechanisms stimulate the allocation of additional financial resources to particular objectives." In line with the OECD's thinking, the methodologies for reporting on amounts mobilised are defined by instrument.[48]

To mobilise capital amidst real and perceived risks, many employ a range of de-risking tools and instruments, including subordinated capital offerings, guarantees, risk insurance, securitisation, local currency financing, and various partnership models. The ITF's 2021 report detailed many of these instruments and strategies and called for the immediate scaling up of their use.[49]

> DFIs are facing a trilemma: invest in the poorest countries, make money **and** mobilise private capital. Those are often mutually exclusive objectives.
>
> **C-Suite leader, DFI**

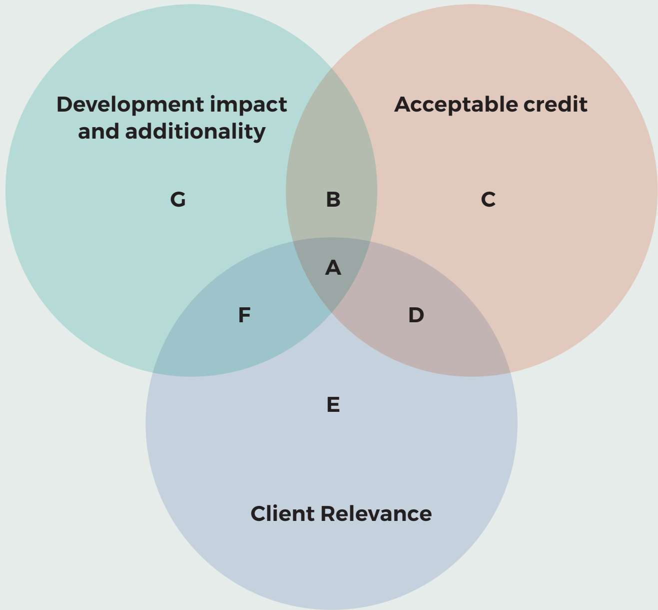
In the two years since, mobilisation figures have not improved and MDBs and DFIs have been placed in the hot seat, at the heart of heated debates on how they can deliver higher impact whilst being additional and mobilising private capital. At the same time, a series of studies and articles have provided a more sophisticated understanding of how DFIs operate, their respective constraints and the trade-offs they face,[50] while still calling for swift change at the system-wide and DFI levels.[51]

One important trade-off that MDB and DFI stakeholders often grapple with is that capital mobilisation at a scale usually happens in middle to high-income countries with deals that are commercially attractive for private investors, whereas market-building objectives in lower-income geographies or riskier innovations typically have lower-potential of private capital mobilisation. Both approaches will require different financial instruments and investment processes, therefore with an important impact on MDB and DFI strategies and business models.

As is discussed in the next section, a global MDB/DFI reform agenda is underway to address the need for clarity and targets on such issues.

IMAGE 1

Trade-offs in private sector development finance



A: Good combination of development impact and additionality, credit quality, and client relevance.

B: Good combination of development impact and additionality, and credit quality, but the client may not be motivated.

C: Good credit, but weak development impact and additionality, and client may not be motivated.

D: Deal may be bankable and the client may be motivated to work with DFIs, but with little development impact or additionality.

E: Client may be motivated but DFI may not have a product to offer, credit may be weak, with no development rationale.

F: Strong development impact and a motivated client, but very high credit risk.

G: Strong development impact and additionality but credit and client fit may be missing.

Notes: 'Acceptable credit' is a proxy for a risk-adjusted return for a given credit, as explained further below. 'Client relevance' refers to the client's general level of motivation to work with DFIs, including whether or not DFIs have a suitable financial product that fits the client's requirements.

Source: LSE (2023)

2.1 Advancing reforms: crossing the line from talk to action

2.1.1 MDB/DFI Mandate Reform is Essential to Drive up Adoption

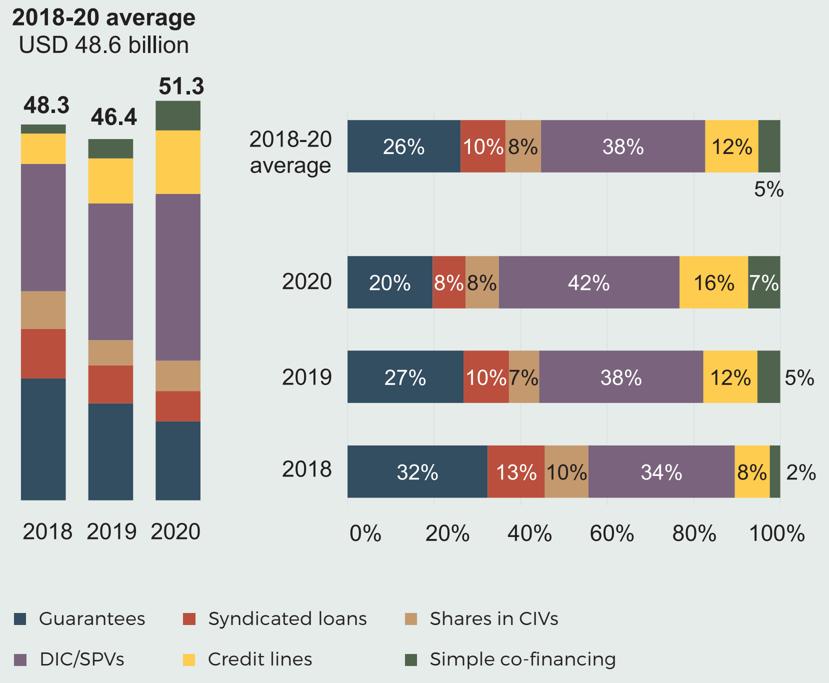
$0.37
mobilised in low-income countries for every dollar of DFI investments

Private capital mobilisation figures have not significantly increased in the last two to five years. The scale of the challenge necessitates urgent reform to mandates with appropriate safeguards, clear targets and incentives.

Private sector finance mobilised in 2021, the most recent year of data available, amounted to $40.3 billion according to the OECD, augmenting $186 billion channelled through Overseas Development Assistance (ODA),[52] yet considerably lower than amounts mobilised in the last five years (see **Image 2**). **Relative capital mobilisation figures are disappointingly low, estimated to range between 0.1x to 1.5x,[53] and just 0.37x in low-income countries.[54]**

IMAGE 2

Mobilised Private Finance by Leveraging Mechanism (2018 - 2020)

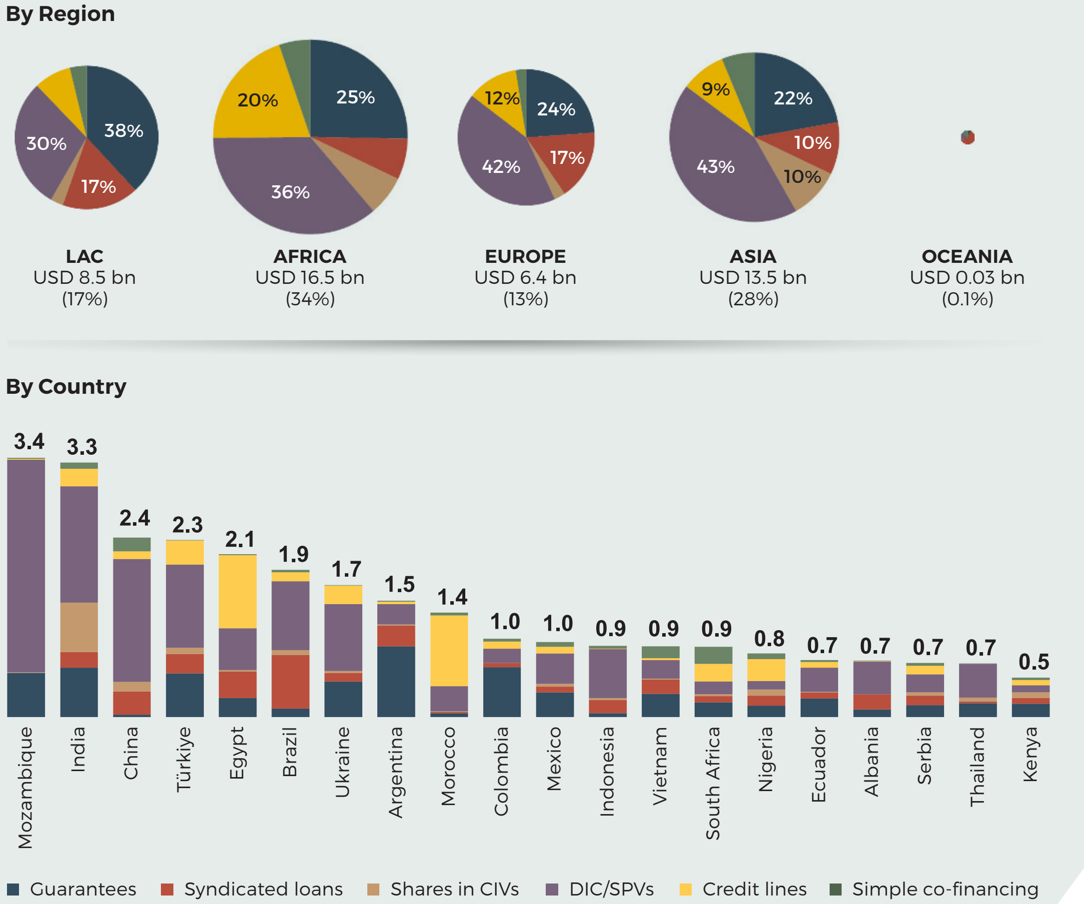


Source: OECD (2023)

Between 2018-2020, most private capital was mobilised through direct investment in companies and special purpose vehicles (SPVs) (38%), guarantees (26%), credit lines (12%), and syndicated loans (10%).[55]

IMAGE 3

Geographic Distribution of Mobilised Private Finance (2018 - 2020)



Source: OECD (2023)

There are positive signs that DFIs and MDBs are succeeding in mobilising capital for the regions and countries that need it most. Between 2018 and 2020, Africa was the largest region for mobilised private capital, accounting for 34% of the total $16.5 billion annually. It was followed by Asia at 28%, or $13.5 billion each year and Latin America and the Caribbean at $8.5 billion per year and 17% of the total. Between 2018-202, Mozambique and India were the main beneficiaries of private capital.[56] In 2021, India and Brazil received the highest amounts.[57]

34%

$16.5 bn

Mobilised capital for Africa

28%

$13.5 bn

Mobilised capital for Asia

To build on that progress, global forums have called for DFI and MDB reform that challenges institutions and their shareholders to do much more. During this time, influential actors from emerging markets and developing economies have assembled a unified stance to address systemic inequality within the financial system. This is exemplified by the Bridgetown Initiative unveiled in Barbados, in July 2022, and the ensuing Summit for a New Global Financial Pact, held in Paris in June 2023, which sought to encourage more financial solutions to poverty, curb global emissions, and elevate the importance of protecting nature.

BOX 5

Our Ambition: From less than 1X to 10X of private capital mobilised

A new data visualisation site created by the OECD provides details on the Total Official Support for Sustainable Development – TOSSD, which amounted to $435 billion in 2021, of which ~$41 billion of private capital was mobilised. A simplistic calculation tells us that **if we were to multiply private capital mobilisation by 10, we would be much closer to closing the SDG funding gap** which stands at approximately $4 trillion pa, with only $3.9 trillion potentially available (as per OECD figure below). Although difficult to quantify, it is also fair to predict that with a level of private capital mobilised close to $0.5 trillion, more investment opportunities would be created to unlock institutional investments for the SDGs in EMDEs, priming a much-needed pump.

However, a range of experts approached for this report, including those working outside of DFIs and MDBs, cautioned about the lack of realism in such a target, for all of the reasons explained in this report. The barriers for such a shift to happen are numerous: from the lack of incentives and targets at all levels to credit ratings constraining business models, from operating processes to organisational cultures. However, there is consensus to push for courageous revisions of risk models, better understanding of what works and where to set more ambitious mobilisation targets by business segments - the result being more realistic mobilisation ratios of 4-5X, and the implementation of new approaches to capital mobilisation, such as those described in BII's latest paper on this issue.

AVAILABLE FINANCING FOR SUSTAINABLE DEVELOPMENT IN DEVELOPING COUNTRIES SHRANK BY USD 774 BILLION, OR 17%, IN 2019-20

2019: USD **4.6** trillion — **-17%** (USD-774 billion) — 2020: USD **3.9** trillion

	2019	Change	2020
TOSSD	USD **292** billion	+22%	USD **355** billion
of which ODA	USD **166** billion		USD **195** billion
Remittances	USD **504** billion	-1%	USD **499** billion
Capital flows	USD **729** billion	-20%	USD **586** billion
Available government revenue	USD **3119** billion	-22%	USD **2430** billion
of which: Government revenue	USD **3481** billion		USD **2781** billion
Debt service	USD **362** billion		USD **351** billion

Source: OECD (2023)

Following these initiatives, there is a growing movement calling for greater steps to be taken to address and reform the unjust debt burden placed on emerging and frontier market countries, affecting their credit risk ratings and resulting in a higher cost of capital for foreign investors. To address this challenge, MDB and DFI shareholders, as well as EMDE governments have been called upon to engage with the private rating agencies in order to adjust ratings in line with the available data.

According to these and other local stakeholders, EMDE government and private sector actors have been penalised by perceived risk higher than real risk, forcing them to channel funds toward debt repayments rather than local investment needs.[58]

BOX 6

Further readings and relevant resources

Resources are available on Focus 2030's summary page for the Summit for a New Global Financing Pact, held in June 2023 in Paris. These include:

- The reform of the multilateral development banks
- Special Drawing Rights (SDRs)
- Taxes and innovative financing
- Global debt
- Financing global public goods
- The Bridgetown Agenda

Source: Focus2030

of the financial instruments used by MDBs & DFIs had private finance mobilisation as a main objective

2.1.2 The MDB & DFI reform agenda is progressing

In 2023, G20 Delhi tasked the Independent Experts Group (IEG) to identify areas ripe for change. IEG's two reports issued this year lay out key topics: opportunities to expand MDB and DFI lending capacity, 'whole-of-bank' approaches, diversifying financial instruments, managing greater risk, and building partnerships at scale across MDBs and DFIs and with the private sector.[59,60] Broadly speaking, the reform agenda has called on MDBs and DFIs to reform their mandates and introduce necessary safeguards, set mobilisation targets, and incentives that will create the underlying governance and the organisational culture to work much closer with the private sector to channel investment to bankable deals and sustainable development.

> A lot of the required changes will be about DFI governance. Today, DFI Board members make comments, but then nothing happens.

Independent Expert

BOX 7

Capital Adequacy Frameworks - A Topic at the Heart of MDB and DFI Reform

A key topic cited in the Independent Experts Group (IEG) reports is the need to reform capital adequacy frameworks to enable MDBs and DFIs to take more risk. Besides IEG's findings, independent research has also been conducted into capital adequacy frameworks, often cited by institutional investors as a hurdle to investing in EMDE debt. A recent publication by the Netherlands Advisory Board on Impact Investing, *Changing Perceptions: An Analysis of Private Debt in Emerging Markets under Solvency II*,[61] found that capital requirements are not excessively high and that - if embraced by insurers - could translate into an additional $52 billion (€50 billion) of impact investments to emerging markets from Dutch investors.

Alongside reform to capital adequacy frameworks, mandate and business models account for one of the key constraints limiting most DFIs from mobilising greater sums of private capital. A paper published by the OECD, *The Funding Model of Bilateral Development Finance Institutions*,[62] unpacks the funding models of three DFIs - FMO, AfD, and BII to show how funding models have material implications on how DFIs mobilise private capital and the instruments they can employ to do so. Greater transparency around these funding models will not only help shareholders hasten to adoption of needed reforms, but it can also have the benefit of fostering improved synergies between MDBs and DFIs, as well as external stakeholders, who can develop pipeline in alignment with what the specific DFIs are able to support. (See **Image 4**)

IMAGE 4

A tale of three cities: Pros & Cons

	Pros	Cons
British International Investment	▲ High risk tolerance and positioned to take on longer investment horizons ▲ Operational simplicity	▲ Limited growth paths ▲ Cannot use debt issuance for mobilisation ▲ Single currency funding
FMO Entrepreneurial Development Bank	▲ Flexibility to develop funding strategy ▲ Strong, explicit support from Dutch government, now with debt ceiling. ▲ Off balance sheet vehicles for high- risk investments.	▲ Low economies of scale. ▲ Hedging> large collateral flows > cash holdings ▲ Max 12-yr maturity due to gov. agreement
	▲ Benefits from economies of scale » Debt issuance » Hedging » Risk management ▲ Insulation leads to high efficiency, high leverage ▲ AFD guarantees to manage headroom.	▲ Limited responsibility mean limited power and flexibility: decisions taken at group level. ▲ Leveraged model means limited capital 'wriggle' room

Source: OECD 2023

The April 2023 launch of the MDB Reform Accelerator by leading think tanks across the globe illustrates the intensification of work around this issue.[63]

BOX 8

Breaking the MDB and DFI Originate-to-Hold Model

Most DFIs and MDBs still operate under an 'originate-to-hold' model, originating investments that they hold for the long-term. However, most of those institutions can afford to take bigger risks, and by doing so can de-risk assets for private investors, arguably without jeopardising their balance sheets.[64] This shift to an 'originate-to-share' model faces a number of systemic barriers that must also be overcome.

- **Mandate**: DFIs and MDBs need a stronger mandate from shareholders to mobilise capital and create pipelines
- **Business Model**: operational misalignments exist with regard to fees, portfolio balance, origination, and operations
- **Regulatory accounting and treatment**: some DFIs and MDBs operate under regulatory regimes that may inhibit mobilisation activity, limiting their ability to issue bonds or equity
- **Scale**: Small investment programmes make it hard to cover the fixed costs of syndication desks, funds or other structures to share assets, while small portfolios offer less risk diversification and smaller ticket sizes for investors
- **Pipeline**: DFIs and MDBs must identify, qualify and structure assets with a risk-return profile acceptable to commercial investors.
- **Lack of targets and incentives**: According to a 2022 OECD survey of MDBs and DFIs, only 18% of the financial instruments used had private finance mobilisation as a main objective[65]
- **Perception biases**: A G20 report found that government agencies and credit ratings agencies have overestimated the financial risks facing DFIs and MDBs. Their core strengths, risk mitigation, technical assistance, that would diminish or even preclude extreme risks from occurring[66]

Source: Center for Global Development (2023)

In response to better understanding of the hurdles, DFIs are starting to implement reforms to address these barriers and increase mobilisation rates. For instance, some institutions such as the EBRD and the United States' Development Finance Corporation (DFC) have started to review their strategies to ensure their portfolios are truly catalytic (See **Box 9**).

BOX 9

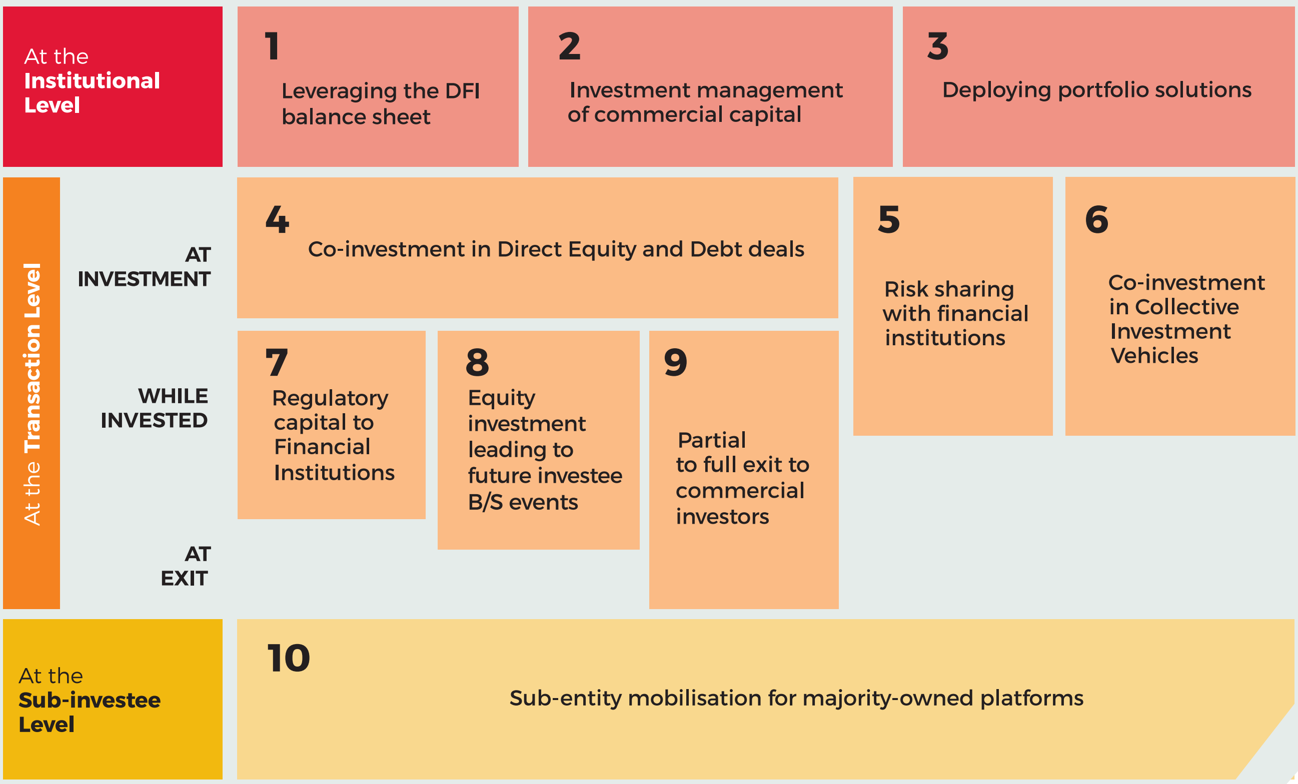
Honing the way capital mobilisation is accounted for

For some DFIs, leading definitions have proven to be too narrow in light of the varied activities undertaken by DFIs. This has led some to develop more comprehensive strategies to account not only for direct flows into DFIs but also support for sub-investees, investments supported by DFI's direct investments.

In addition, in some cases, market creation is more applicable than capital mobilisation. Some DFIs call for greater capital mobilisation for specifically high-impact projects, while others place importance on the scale and depth of impact generated rather than the specific mobilisation figures.

In an effort to expand current definitions of private capital mobilisation, BII's 2023 paper, *Understanding Mobilisation*,[67] suggests 10 specific moments of measurement, at the institutional level, transaction level, and sub-investee level.

TEN MOBILISATION PATHWAYS



Source: BII (2023)

2.2 Reducing risks for private capital investors by scaling what works

2.2.1 Increasing the use of blended and concessional finance

Blended finance is a widely used approach for de-risking transactions and making them more investable. It is becoming a more widely used approach for mobilising private commercial and philanthropic capital for sustainable projects in emerging markets but is still severely underutilised. Convergence, which curates and maintains the largest and most detailed database of historical blended finance transactions, reports that blended finance has mobilised $198 billion since 2014.[68] Depending on the aims of the transaction, blended capital can be provided either at market or concessional rates by institutional investors.[69] Blended finance provided at concessional rates is commonly referred to as catalytic capital and is typically provided by philanthropic foundations or donor countries. Both are needed with urgency.

BOX 10

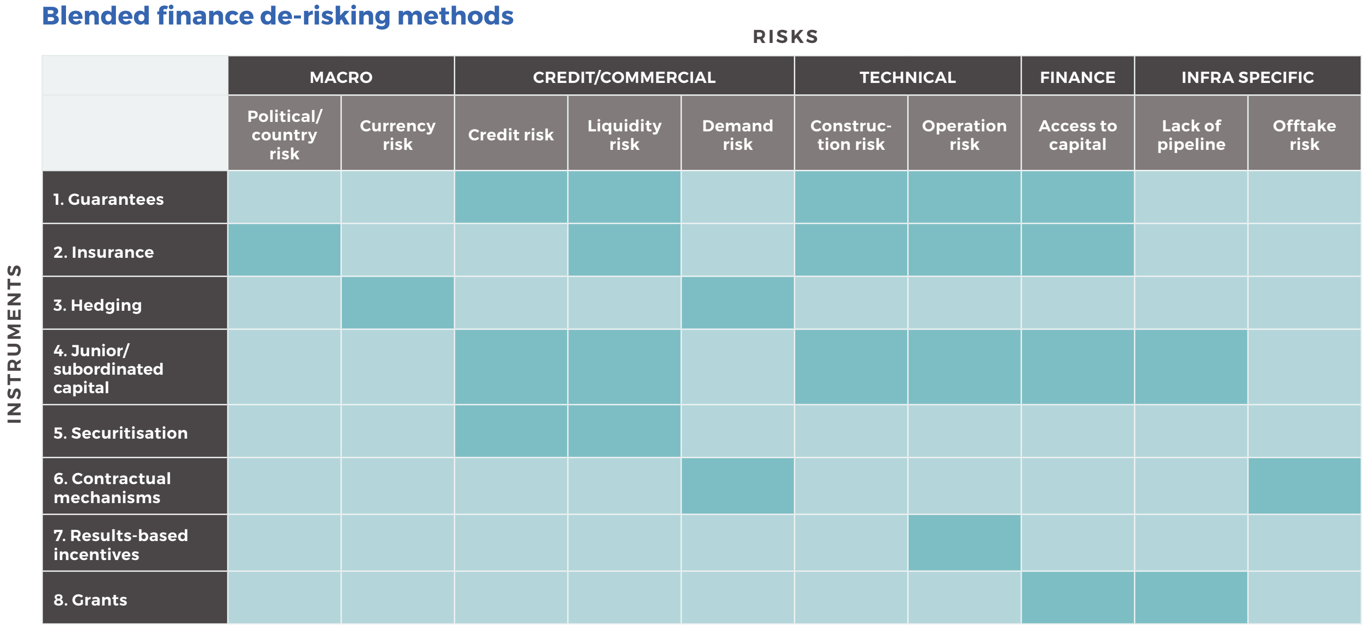
$1 billion blended finance SDG Loan Fund originated and managed by FMO Asset Management

Announced in November 2023, FMO's **SDG Loan Fund** will mobilise $1.1 billion of investor capital to advance SDGs in emerging and frontier markets, using an innovative blended finance model. Investors in the fund include institutional investors (Allianz Global Investors, FMO, and Skandia) and a charitable foundation (the MacArthur Foundation). The fund will provide capital for high-impact, SDG-aligned loans to local companies and projects across Latin America, Asia, Africa and Eastern Europe.

The SDG Loan Fund's large-scale and multi-sector reach is enabled by a first-loss investment from FMO, coupled with the MacArthur Foundation's USD 25 million guarantee. The investment of USD 1 billion in private capital for affordable energy, financial inclusion and sustainable agriculture in emerging and frontier markets.

IMAGE 5

Blended finance de-risking methods



Source: The Blended Finance Taskforce (2018)

-45%

of blended finance transactions, in deal volumes in 2022

Despite net growth between 2014-2021, information from Convergence's State of Blended Finance 2023 Report finds that blended finance transaction deal volumes were down 45% in 2022 compared to the previous year, from $14.3 billion to $6 billion, and climate blended finance transactions were at a ten year low.[70] The data is especially troubling given blended finance's private sector mobilisation potential. **Blended finance solutions have been found to leverage $4 of commercial capital for every dollar of concessional capital**. Unfortunately, only a fraction of this commercial capital ($1.10) has come from the private sector, with the balance largely provided by MDBs and DFIs.

$4

of commercial capital mobilised for every dollar of concessional capital in blended finance solutions

BOX 11

From good examples of capital mobilisation to a more systematic approach to private capital mobilisation

Many examples can be highlighted when it comes to above-average private capital mobilisation ratios by MDBs and DFIs, for instance:

- Private Infrastructure Development Group (PIDG) $284 million in 2022[71], developing and creating infrastructure assets that private investors can invest in. Mobilisation ratio of 1.9X.
- The ILX Fund, an emerging market credit fund that invests in MDB and DFI-originated loans, was set up with seed funding from the German, Dutch, and UK governments. It has raised $1 billion from Dutch pension funds.
- DFC mobilised $4.7 billion in private capital between 2018-2020.[72]
- FMO-initiated Climate Investor One (CIO), a $850 million blended vehicle targeting renewable energy infrastructure projects in emerging markets, mobilised over 5X its original investment.
- MIGA issued $6.4 billion of guarantees in 2023[73] mobilising $5.7 billion in financing from private sources (0.89X ratio)

However, with its high mobilisation potential in mind, Convergence calls on MDBs and DFIs to work harder at originating and arranging more blended finance deals at bigger volumes and for them to collaborate to achieve scale, pointing out the strategic role blended finance can play in new transactions.[74]

- Reduce the risk levels of transactions and thereby making them 'investable' by commercial terms
- Enhance the positive impact of transactions (for example, incentivising gender equality practices)
- Increase risk-adjusted returns (for example, by providing mezzanine debt to enable institutional investors to meet their fiduciary obligations
- Expose investors to new asset classes and geographies leading to subsequent future investments

For more examples, see Convergence's ITF 2023 Input Paper to the Impact Taskforce and their learning library.[75]

More can be done. For one, better discipline is required to ensure that blended structures are being used by the right actors, under the right terms, and for the right goals. Another area of concern is the need for more philanthropic capital to de-risk and design a new pipeline of investable deals. Critically, the supply of concessional capital to climate blended finance deals has been stagnating since 2017 (only a minor increase from $967 million per year between 2017-2019 to $1.08 billion 2020-2022) and is nowhere near the levels required to reach key mobilisation targets. To address the gap, Convergence has called for the creation of a critical mass of catalytic funding, spearheaded and optimised by launching a Catalytic Funding Network of public and philanthropic organisations.[76] With just energy transition constituting a primary driver of private capital mobilisation in EMDEs, catalytic funding in the form of social investment will be especially needed to support the communities most vulnerable to job losses in the energy transition and the physical risks of climate change.

Importantly, philanthropic capital is not only needed within transactions themselves for de-risking purposes, but it is also needed to design a new pipeline of fit-for-purpose instruments that bridge the finance gaps with economically sustainable solutions that can be taken up by local actors, governments, banks, pension funds, fund managers, and more. Convergence's design funding platform, similar to programmes GSG has run in 2022-2023 with backing from the Catalytic Capital Consortium (C3), has mobilised $12 million to date since 2017 under its market acceleration program providing early-stage grant funding focused exclusively on the design of innovative blended finance solutions. Vehicles and mechanisms designed under this programme have gone on to raise upwards of $1.9 billion for the SDGs.[76]

2.2.2 Boosting the use of guarantees to de-risk investment

Blended finance transactions can be boosted and further de-risked through the adoption of guarantees. The three types of guarantees most often used for this purpose include credit guarantees, risk guarantees, and currency guarantees. Other types of guarantees relevant in the context of scaling investments are liquidity extension guarantees, payment guarantees and performance guarantees.[78]

$1.50
of private capital mobilised by guarantees for every dollar

but

<5%
of total commitments

A 2023 paper from the Blended Finance Taskforce calls for a smarter use of public capital in guarantee products. According to its research, guarantees show the highest mobilisation ratios among other de-risking instruments, on average mobilising $1.5 of private capital for every dollar of MDB capital and outperforming the average mobilisation ratio of loans and equities by six times.[79] However, they represent less than 5% of total commitments in the analysed data.[80]

A smarter use of public capital that addresses credit and currency risks, streamlining guarantees to reduce transaction costs, and linking projects to national plans can help meet the 5X scale-up in climate finance needed in EMDEs.[81]

BOX 12

Sovereign Guarantees help to de-risk investment and ensure competitive returns for private investors

- The Room2Run Guarantee is a risk-sharing instrument offered by the African Development Bank (AfDB) that transfers its sovereign lending portfolio risk to both sovereign entities and private investors, especially insurance companies, to create more lending headroom in AfDB's balance sheet. In October 2022, AfDB transferred the risk on a total of $2 billion sovereign loan portfolio from 11 countries to a group of private insurers and the UK's FCDO.
- The European Fund for Sustainable Development Plus (EFSD+) is a guarantee programme designed to increase the guarantee issuance by European financial institutions towards investments in EMDEs. The instrument makes available $41.6 billion (€40 billion) in guarantee capacity. EFSD+ covers a share of the risks. DFI partners can match the EFSD+ guarantees with their own resources to attract additional investors. A beneficiary of the EFSD+ programme is GAWA Capital's Huruma Fund, a $228.8 million (€220 million) Spanish private equity fund that invests in financial service providers and SMEs in the agriculture value chain in EMDEs. GAWA Capital is a member of GSG's affiliated Spanish NAB. The fund receives contributions from the EFSD+ and Spanish DFIs for de-risking components, $10.4 million (€10 million) for the first loss tranche and $20.8 million (€20 million) for subordinated debt, to enhance its risk-return profile. The EFSD+ guarantee effectively acts as a revenue-enhancing instrument, ensuring pension funds that have co-invested in the fund are able to meet their fiduciary duties.
- The experience of guarantee providers like InfraCredit in Nigeria and GuarantCo shows that projects can get off the ground with appropriate guarantees. Blended finance mechanisms like green guarantees are one of the primary routes to unlock and mobilise more domestic institutional capital for the real economy. These solutions are essential to address both the rising cost of capital and perceived risks.
- The ASEAN Catalytic Green Finance Facility (ACGF) is an innovative finance facility dedicated to accelerating green infrastructure investments in Southeast Asia by supporting ASEAN governments to prepare and source public and private financing for infrastructure projects. The facility, which brings together $1.9 billion in co-financing commitments from Public Development Banks and international government agencies, will cover a portion of the upfront capital costs of a project and provide additional funding for technical assistance and learning. Through one of its key projects, SDG Indonesia One, a sovereign financial intermediary loan to Indonesia will be lent onwards to PT Sarana Multi Infrastruktur (PT SMI) for SIO-GFF implementation, to catalyse green funds from private, institutional, and commercial sources.

2.2.3 Harnessing the growing engagement of institutional investors

Impact investing, a rapidly growing subset of a wider environmental, social and governance (ESG) market valued at $35.5 trillion (2020) is effectively doubling year on year, up from $164 billion in 2016 to ~$3 trillion in 2023. With the pace of new ESG disclosure regulation proliferating globally,[82] the impact and sustainable investment market is expected to continue growing, and with it, demand for new investment opportunities, especially in higher growth EMDE markets.

To meet this pending demand, more bankable projects must be developed and new pathways generated allowing capital to flow both to large-scale and capital-intensive solutions in EMDEs, such as infrastructure (see **Box 13**), private debt, and firms on listed markets, as well as to local capital providers working to meet extensive financing gaps facing small and growing businesses.

BOX 13

Zoom in on infrastructure - A key area for further development

As referenced in our ITF 2021 report, *Mobilising Capital for a Just Transition and the SDGs in Emerging Markets*,[83] Infrastructure presents immediate investment opportunities for domestic and international institutional investors. The global infrastructure market currently has a $3.6 trillion annual funding need, according to the World Bank.[84] In emerging markets, McKinsey estimates the total annual infrastructure investment needed over the next 15 years, just to keep up with GDP growth, to amount to more than $2 trillion pa.[85]

With a lack of available performance data, most global investors are hesitant to approach the sector. Yet, as explored by the Financial Times 'African projects have a reputation for risk, but in reality, default rates are often lower than elsewhere'.[86] This is because these projects often integrate blending and de-risking components that make them compelling for institutional investors.

Sustainable infrastructure to meet the needs of a changing climate
EMDE Firms like PIDG, AIIM, Ninety One, along with initiatives like the Global Infrastructure Facility, are providing local solutions while mobilising large pools of capital. Their efforts should be supported, scaled and replicated to channel investment to where it is needed most.

PIDG TA: supporting Technical Assistance to enable more sustainable infrastructure
PIDG TA supports Private Infrastructure Development Group (PIDG) companies by providing grants for technical assistance and feasibility gap analysis. Its core business, backed by a number of governments, provides guarantees for infrastructure projects across Africa and Asia that support early-stage infrastructure development projects. Through this combination of technical assistance and local currency investment, PIDG has been able to leverage $1.9 billion ODA to $25 billion.

African Infrastructure Investment Managers: multi-layer de-risking strategies
African Infrastructure Investment Managers (AIIM) develops and manages private equity infrastructure funds and works predominantly in East and West Africa. With offices in South Africa, Nigeria, Kenya and Cote d'Ivoire, the firm has raised $3.7 billion for infrastructure projects. According to the firm's direction, projects are de-risked following a multi-tiered approach to address both perceived and real risks. "The firm puts various layers of risk mitigation in place to make projects investable for international pension funds, bringing projects essentially to a AAA credit status. De-risking initiatives include government guarantees, contracting with global first-tier contractors and contracts are in hard currency. With these measures in place, investors are able to gain exposure to returns that outweigh the risks."[87]

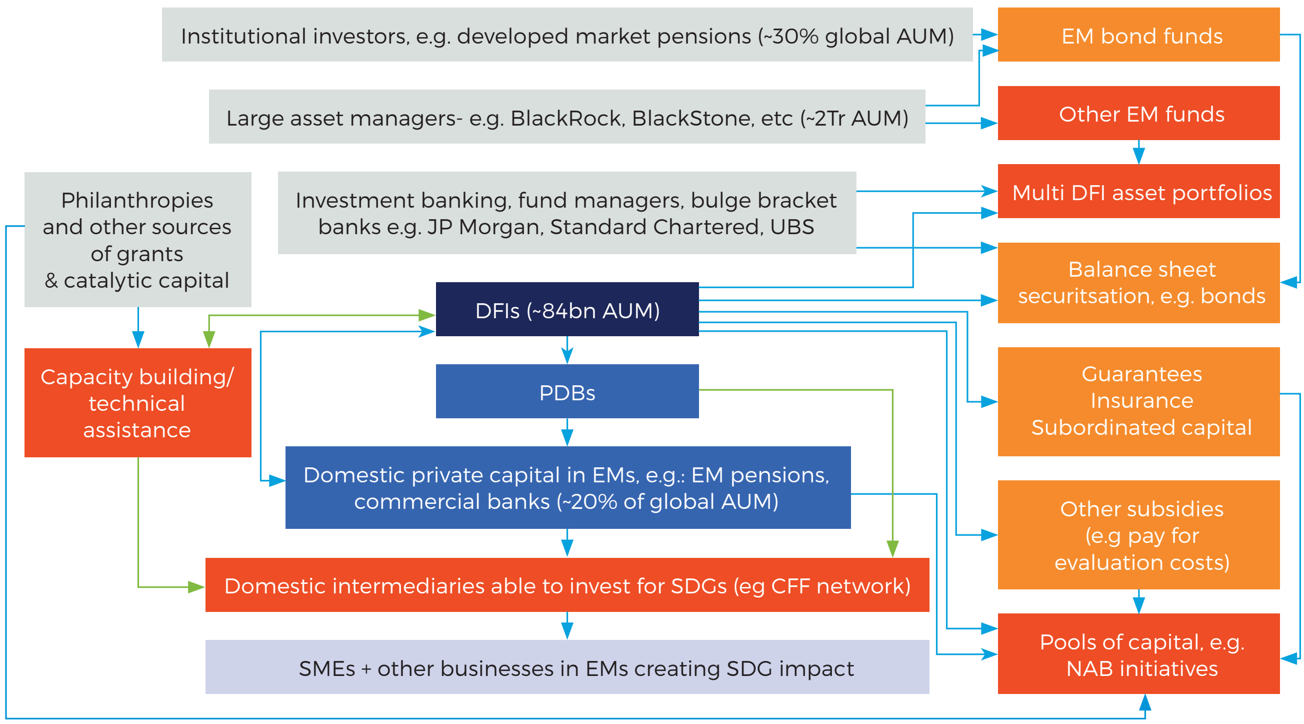
Ninety One: supporting domestic private sector actors
Ninety One is a $123 billion AUM global asset management focused on investing in EMDEs. Its Emerging Africa Infrastructure Fund has committed just over $1.3 billion to 55 infrastructure projects across Africa. In contrast with most approaches, the fund only supports private sector developers of infrastructure, as opposed to lending to state actors. The firm's support for private sector initiatives has helped to facilitate solar power in Rwanda and transportation infrastructure in East and West Africa.

Global Infrastructure Facility: a multi-sector platform worthy of scale
The Global Infrastructure Facility is a G20 initiative established to address the shortage of high-quality, bankable sustainable infrastructure projects in emerging markets. Housed at the World Bank, GIF brings together governments, MDBs, developers, investors, and other stakeholders in mobilising private capital in infrastructure projects in EMDEs. The GIF is an example of an existing platform channelling private capital for sustainable development that should be scaled further. To date, GIF has a global portfolio of over 120 projects under preparation in 58 countries, spread across the transport, energy, social infrastructure, water & sanitation, and digital development sectors, with a total investment need of $74 billion. Through the GIF's support, $50 billion of this capital is expected to be mobilised from private investors.

One of the notable developments to solve for some of these issues was the launch in July 2023 of the 'the Private Sector Investment Lab,' by Ajay Banga, who assumed the role in early 2023 as the new President of the World Bank.[88] Banga has made clear commitments to boost the bank's lending capacity, especially through private capital mobilisation. The Lab is composed of 15 CEOs of large financial institutions such as AXA, BlackRock, Ninety One, Standard Chartered, Temasek and others who will focus on specific approaches that can provide solutions to unlock large amounts of institutional capital for the SDGs in emerging markets. The Lab's first order of business will be developing new financing structures and partnerships for scaling transition finance in renewable energy and energy infrastructure.

IMAGE 6

'The hourglass EMDE investment chain' - unlocking institutional investment opportunities for the SDGs



Source: GSG

Invests / implements — Capacity building — Critically missing or insufficient — Not enough or not maximising impact

2.2.4 Additional routes to increase private capital mobilisation

> "In the last ten years, we've become a better originator. In the next ten years we will become a better distributor and fundraiser."
>
> **C-Suite leader, DFI**

In the last two years, focus has been placed on encouraging DFIs to take greater risks and do more to create pipeline opportunities of different sizes; large scale to be able to absorb institutional capital, and smaller scale to meet the needs of micro, small, and growing businesses.[89] Having explained guarantees and blended finance in depth, this section references additional high-potential instruments and tools that can be harnessed by MDBs and DFIs to direct institutional capital to the SDGs in emerging markets. The discussion below draws, in particular, upon guidance provided in *Mobilising Capital for the SDGs and a Just Transition in Emerging Markets*[90] and *MDB and DFI Innovations for Mobilising Private Capital*[91], which call on MDBs and DFIs **to distinguish between riskier assets that will be held on the balance sheet versus less risky assets which can mobilise more private capital into areas with high impact, such as** climate. Suggestions published by the Center for Global Development provide an especially useful guide for mapping out key opportunities that should be pursued.[92]

BALANCE SHEET MOBILISATION

- **Equity issuances**: These issuances are suitable for cases in which MDBs or DFIs can take on higher investment risk. This enables the MDB or DFI to expand its equity base, which can be leveraged with borrowing, thereby expanding the amount of capital available for investment. The minority equity can be on equal, or different terms, to government equity. The private investment also often comes with commercial expertise through appointments to the board of the development finance institution. (See **Box 14**)

BOX 14

Example of equity issuance

MOBILIST, a flagship initiative by the UK government and FCDO, helps products list on global and local public exchanges. To date, the programme has made two commitments with 12 more in the pipeline and/or under review. MOBILIST invested $31.4 million (£25 million) in the ThomasLloyd Energy Impact Trust PLC, the first ever emerging markets renewable energy fund, which later went on to raise $115 million in December 2021 at IPO. Through partnerships with stock exchanges in London, Singapore, Johannesburg, Sao Paulo, Manila, Mexico and Nigeria, MOBILIST is helping to channel more capital for sustainable development via listed products on those exchanges.

- **Bond issuances**: Issuances are contingent on the size of the bond market in question and on the MDB or DFI's mandate. For example, a DFI may be mandated by its shareholders to maintain an investment grade rating. However, many MDBs and DFIs could pursue a less conservative risk management policy, while maintaining their credit ratings, allowing them to raise capital that can be lent on to private sector subsidiaries for investment, or invested on the same balance sheet as sovereign lending.
- **Local currency bonds**: The ability to issue bonds is contingent on the size of the MDB or DFI, as well as the level of local capital market development. Nonetheless, they are a growing option as low and middle-income countries accumulate savings and their universe of pension funds, insurance companies and sovereign wealth funds matures, creating demand to invest in local currency.

SINGLE ASSET MOBILISATION

Experts call on MDBs and DFIs to operate two distinct lines of business, which will be pursued in different markets and sectors. For example, in areas where there is potential to attract private capital, MDBs and DFIs should focus part of their business on originating assets using replicable structures which can mobilise private capital as part of multi-asset portfolios.[93] The article calls on governments to allow their bilateral DFIs to leverage their equity by issuing thematic bonds backed by their investment portfolios, not by government guarantees.

- **Syndicated Loans**: In the case of syndicated loans, the MDB or DFI acts as both the agent and lender of record for the loan, with private capital co-investors participating in the loan, thereby reducing the institution's financial exposure.[94] (See **Box 15**).

BOX 15

Example of syndicated loans

Managed Co-Lending Portfolio Program (MCPP) One Planet is a $3 billion global loan syndication platform for climate-smart investment aligned with the Paris Agreement. The facility enables institutional investors to directly provide capital for sustainable lending in emerging markets. Since its launch in 2013, MCPP has been able to raise $10 billion from 11 investors and provided financing to more than 200 firms across 55 developing countries, a truly geographically diverse portfolio. Experts are calling to scale the MCPP platform by 10X, given its proven model.

- **Unfunded Risk Transfers**: MDBs and DFIs are able to free up capital, and in turn expand their lending, by transferring some part of the financial risk to another party. (See **Box 16**)

BOX 16

Example of unfunded risk transfers

Through recent examples from leading DFIs, we are beginning to see how collaboration with insurance companies is opening up new pipeline opportunities for DFIs. For example, EBRD's Unfunded Risk Participation (URP) is a risk transfer product that enables insurance companies to take on exposure in EMDE transactions. URP has mobilised more than $3 billion in partnership with 14 private insurers since its launch in 2014, accounting for more than 40% of EBRD's annual mobilisation volume and is expected to grow further in the future.

- Client bond issuance (including local currency bonds, GSSS bonds) - MDBs and DFIs can help clients issue bonds, often in local currency and to local institutional investors, using the market knowledge and - where needed - their balance sheets to bring issuers and private investors together. (See **Box 17**)

BOX 17

The high potential of GSSS bonds to address SDG financing gaps in EMDEs

A fast-growing market that amounted to $3.8 trillion at the end of 2022.[95] GSSS bonds could help mobilise capital at scale and reduce the cost of capital, especially for Just Transition projects, while ensuring that funds are directed towards impact. However, issuance in developing markets only makes up 15% of the global GSSS bonds market.

As we explain in our recent publication, *Financing SDGs in Emerging Markets*,[96] DFIs have a key role to play in supporting the adoption of GSSS bonds in EMDEs. They can issue bonds themselves to demonstrate feasibility, but also provide anchor funding to build investor confidence and catalyse investments from a wider pool of private actors. They can also de-risk investments, by issuing guarantees, purchasing first-loss or more subordinated tranches, or offering insurance to investors. DFIs are well positioned to offer technical assistance to issuers that possess the right enabling factors, and other EMDE stakeholders, and facilitate market connectivity by leveraging their convening power.[97]

It should be noted that efforts should be made to ensure more EMDE countries can make sovereign issuances by utilising special drawing rights (SDRs) to issue debt for climate swaps.[98]

DFIs are active in launching GSSS Bonds as anchor investors as well as bond issuers themselves. For example, IFC invested about $50 million in a sustainability-linked bond issued by Tata Cleantech Capital, the first of its kind to be issued by a private financial institution in India to support the shift to a clean energy economy.

AFD's SDG Bond Issuances Since 2020, AFD, France's Public Development Bank, has given priority to issuances that reflect the overlap of environmental and social impacts, with this approach aimed at supporting the Just Transition. Its newest issuance, a $520 million (€500 million) 15-year sustainability bond, was 12X oversubscribed. Proceeds will go to one of six defined themes generating a neutral or positive impact on the SDGs. To date, the development agency has raised $13.9 billion (€13.35 billion) in SDG and climate bond issuances.[99]

MULTI-ASSET MOBILISATION

To scale up mobilisation at the transaction level MDBs and DFIs (especially smaller ones) should assemble multi-asset portfolios which can be invested in by institutional investors, including insurance companies, pension funds and sovereign wealth funds. By bundling assets, DFIs and MDBs can create portfolios large enough and risk-diversified enough to attract institutional investors.

- **Portfolio Sales**: By operating an originate to distribute or share, larger MDBs DFIs can bundle pools of assets ($500 million or more), tailoring the underlying investments and portfolios to meet investor demand. They can either sell those assets or securitise them, freeing up more risk capital to keep investing in the markets or countries with the most need. Additionally, large asset managers with a number of institutional investors among their clients (e.g. sovereign wealth funds and developed economy pensions) could use this route as a major R&D opportunity in markets where product offerings are limited but institutional investor demand is growing. Furthermore, MDBs and DFIs can be encouraged to collaborate with their peers to create investment-grade portfolios that aggregate assets from multiple DFIs. Such a move could have the potential to mobilise trillions rather than billions of private capital over time.[100]
- **Portfolio risk insurance**: MDBs and DFIs can take our insurance cover for some of the risk exposures in their investment portfolios. In doing so, the insurer puts its capital at risk, while the MDB or DFI frees up capital for further investment. (See **Box 18**)

BOX 18

DFC Political Risk Insurance Portfolio

The need for FDI is greatest in emerging economies. However, most capital flows (~65%) 4 are invested into high-income countries and upper middle-income countries.[101] This imbalance of flows is partially attributed to both perceived and real political and other non-commercial risks. By taking out political risk insurance on debt issuances, DFIs can effectively transfer capital exposure to insurance providers that are less risk averse and more capable to bear the risk. This provides investors with a credit enhancement on their investment, making investments into lower income markets more favorable and feasible.

A leader in the utilisation of political risk insurance, DFC currently has 174 active Political Risk Insurance (PRI) contracts and eight commitment letters, amounting to a $7.7 billion Political Risk Insurance portfolio. Through these contracts, DFC directly mobilized approximately $2 billion in private sector capital, with five contracts accounting for $1.7 billion. According to a May 2023 impact assessment of its PRI portfolio, its strategy has also contributed to second order impacts, including decreasing risk perception of the host countries, improving critical infrastructure, and pioneering better institutions.[102]

Source: DFC (2023)

- **Privately-managed DFI debt funds**: DFIs and MDBs have long been investors in funds managed by general partners. In many cases, fund managers in emerging and frontier markets aim to attract DFIs and MDBs as anchor investors in order to draw in other institutional capital. More recently DFIs and MDBs have taken a more active role in creating new funds, which they design and then put out to tender for private fund managers to manage. (See **Box 19**)

BOX 19

Example of private debt fund

ILX Fund is an emerging market-focused credit fund that provides institutional investors access to development finance assets by investing in private sector loans originated by DFIs. The fund set up with seed funding from the German, Dutch, and UK government has reached the target fund size of $1 billion from Dutch pension funds.

- **Platform companies**: some equity-focused DFIs and MDBs have created holding companies which originate and manage portfolios of assets in a particular industry. Selling equity stakes, or offering debt, in these platform companies offers investors access to a portfolio that is diversified by country, while the DFIs and MDBs can free up capital to invest in new opportunities. (See **Box 20**)

BOX 20

Example of a platform company

In 2017, British International Investment (BII) established Ayana Power to develop renewable energy infrastructure in India. BII invested an initial $100 million in equity and appointed the management team and independent board of directors. Ayana Power received additional equity from the Indian government's National Infrastructure Investment Fund and a private European investor. By 2021, Ayana had over 1.1GW of renewable power under development and is expected to add up to 1.5GW of new capacity a year.

Source: Center for Global Development (2023)

2.3 Systemic shifts are still required to mitigate key risks and improve risk pricing

2.3.1 Addressing and mitigating currency risk has become a top priority

$100bn
of local currency risk guarantees needed p.a.

Tackling foreign exchange (FX) risk and scaling de-risking instruments in local currency are both needed to crowd in more institutional investors and to protect borrowers in EMDEs. As referenced by LSE's International Growth Center (IGC) in mitigating foreign exchange risk in local currency lending in fragile states (2023), DFIs provide finance mostly through equity and debt; equity investments are typically left unhedged, and subject to local currency risk. Similarly, DFI lending, due to operating constraints, mostly takes place in foreign currency. This can shift currency risks onto borrowers and constrain DFI investment pipelines.[103] Investors in developed economies require hedging solutions to protect against currency fluctuations which could erode returns, while borrowers in emerging markets, for example, public development banks or SMEs, need assurances to protect them against currency fluctuations that can dramatically increase their debt burdens.

As the Blended Finance Taskforce references in *Better Guarantees, Better Finance*,[104] "currency risk management mechanisms are becoming a higher priority in the broader development finance system reform agenda as they are key to mobilising international capital."[105] The Bridgetown Initiative insisted that $100 billion of local currency risk guarantees are needed per year to boost private sector investment into EMDEs and that the IMF and MDBs should take a step forward in providing these guarantees.[106] (See **Box 21**)

BOX 21

Enhancing foreign currency risk and hedging solutions

Recent survey findings by Finance in Common, TCX, and Deloitte in *The Impact of Currency Risk on PDBs and their Ability to Maintain Sustainable Resilience*,[107] show that two-thirds of PDBs are exposed to currency risk and 64% of PDB respondents consider currency risk a significant threat to their organisation's profitability. To address these challenges their paper calls to enhance the use of solutions offered by FX hedging providers and emphasises the role of blended finance in drawing in additional sustainable capital. Specifically, the paper recommends the following measures:

- Scale up the local context and regulatory frameworks by strengthening capital markets, ensuring effective regulation and supervision
- Highlight existing responsible financing solutions by promoting local currency financing and lending from MDBs to PDBs, enhancing the use of solutions offered by FX hedging providers and emphasising the role of blended finance in drawing in additional sustainable capital
- Improve PDBs' capacities to mitigate currency risk by supporting and reinforcing internal capabilities through training, knowledge sharing and promoting inter-PDB cooperation

Source: Finance in Common (2023)

> Mitigating currency risk is like buying insurance for your house when you know it will burn down. The issue is macroeconomic and we should not use concessionary capital to protect people from poor economic policies.
>
> **C-Suite leader, DFI**

A variety of proposals are being explored that would enable the scaling of hedging solutions and look to fix the root causes of currency volatility. Among them, The International Growth Center's 2023 paper, *Mitigating foreign exchange risk in local currency lending in fragile states*[108] suggests forward-looking proposals for the DFIs community, including **providing technical assistance (TA) to central banks to support the development of money markets and financial stability, and facilitating cross-currency swaps and a local currency credit guarantee that takes on part of the credit risk facing local counterparties in local currency loans.**

Another solution may be to further scale The Currency Exchange (TCX) Fund. Established in 2007 by a group of DFIs, TCX allows foreign lenders to provide local currency loans in EMDEs by pooling foreign currency risks in a globally diversified fund with a cushion of first-loss capital. TCX took on $1.4 billion of currency hedges in 2022 across 42 countries, with some 65% of those hedges in the least developed and lowest-income countries. Their fund was active in Sub-Saharan Africa, hedging $382 million for the year, while volumes in Asia and Latin America more than doubled versus the prior year. TCX offers opportunities to hedge local currency risk in SDG-aligned projects, ranging from financial inclusion to renewable energy.

2.3.2 Increasing transparency and access to data for better decision-making

Supporting the roll-out of structural solutions that can de-risk investments for private capital is the need for greater transparency and access to data for investors. Better data will enable investors, and credit agencies, to discern between real and perceived risk in EMDEs, while improving accountability and decision making towards achieving the SDGs.

> It is an absolute shame that the GEMs database is not available for third parties. It is a public good, containing data about public investments.
>
> **C-Suite leader, DFI**

Much of that data already exists and is shared among DFIs and MDBs on the GEMS database, which contains historic performance data of their deals. Publishing the GEMS database to third parties through an independent organisation, with appropriate safeguards, is an action a large array of development finance actors have called for and one we unequivocally support.[109] It is also critical that credit rating agencies and regulators use this data to inform risk assessments and rating evaluations to reflect real not perceived risk.

The GEMS database has about 10,000 individual records of MDB and DFI credit loss and recovery data across EMs from the last 33 years. Its utility is around the strength of specific types of underlying investments. This kind of data is absolutely critical for private investors to calibrate their understanding of risk in markets less familiar to them. (See **Box 22**)

BOX 22

Petition to Unlock the GEMs Database

In early 2023, the Dutch National Advisory Board circulated a petition to the European Investment Bank, the custodian of GEMs, to release the data and make it accessible on an ongoing basis. Its call to action included:

- Make the GEMS database independently managed
- Combine the GEMS database with other data sets
- Make it possible to slice and dice the information to build new investment thesis and vehicles

Petitions like these have helped to focus the international community around solutions. In the G20 Delhi Communique (September 2023), Finance Ministers stated their appreciation for 'the ongoing collaboration among MDBs on the timely release of Global Emerging Markets (GEMs) data and the launch of GEMs 2.0 as a stand-alone entity by early 2024'. Despite the urgency to make GEMs 2.0 a reality, experts wonder if the timeline will actually be upheld. The latest World Bank meeting statement (October 2023) now only talks about releasing 'new and more comprehensive statistics' in early 2024.[110]

Source: Center for Global Development (2023)

> It is reasonable to conclude the release of GEMs database would reduce the EM premium by around one-third. This equates to $15.6 billion of saved interest payments per annum [among borrowers in EMDEs].

Independent expert[111]

> DFIs should address an existential question: what is the most strategic use of the additional capital that MDBs and DFIs would get?

C-Suite leader, DFI

Acknowledging the need for accessible and transparency data, while discussions at the G20 around the topic ensue, some DFIs have cooperated with the **Publish What You Fund Initiative, a global campaign for aid and development transparency, which publishes an annual DFI Transparency Index**, ranking sovereign and non-sovereign DFIs on the availability, quality, and consistency of data across 47 indicators, disclosure of financial information at the organisational and project levels.[112] Discussions around unlocking the GEMs database have also supported further ideation around greater performance data sharing and disclosure on the part of pensions and insurance companies on the African continent,[113] or an aggregation of performance data among donors supporting SME finance.[114]

Another major development in the direction of further progress on transparency was the launch in June 2020 of the Climate Data Steering Committee, which released recommendations later in 2022 **towards the development of a Net-Zero Data Public Utility** (NZDPU or Utility). The NZDPU would be an open, free, and centralised data repository that would allow all stakeholders to easily access key climate transition-related data, commitments, and progress of businesses and financial institutions toward those commitments. In September 2023, NZDPU announced a collaboration with CDP, which will provide NZDPU with access to core climate data from hundreds of companies.[115]

Measures to mitigate and promote understanding of risk must be supported by capacity building and technical assistance. This can include research, organisational and legal policy change, training, and the formulation and dissemination of new learnings. Ultimately, awareness of successful investment examples can drive understanding and dialogue amongst pension funds and other institutional investors.

Recommendations

MDBs AND DFIs: Scale existing instruments and vehicles that have demonstrated success in mobilising private capital for the SDGs. This is an immediate action which can be implemented now. Guarantees and catalytic capital in blended finance deals and vehicles are well known instruments and have proven to mobilise around $4 for every public development finance dollar invested. Similarly, successful solutions like MIGA, MCCP, PIDG or TCX, could create higher SDG impact with increased funding.

MDBs, DFIs, AND THEIR SHAREHOLDERS: To urgently work with MDB and DFI leaders in defining new and ambitious targets and incentive systems around private capital mobilisation, possibly increasing the risk appetite of such institutions towards a better alignment between their business model and development mission, whilst focusing on the higher impact they could achieve with such additional capital mobilised.

MDBs, DFIs, AND THEIR SHAREHOLDERS: Improve information that would enable better risk pricing in EMDES, especially by releasing relevant data. Specifically, MDBs and DFIs need to accelerate the process of making GEMs a new independent entity, enabling investors and third parties to access disaggregated EMDE investment data. This should happen as soon as possible and no later than the end of 2024.

CHAPTER 3

Domestic EMDE Actors and Initiatives Leading the Way

Key Messages

- ▲ SMEs are critical to the achievement of the SDGs, but inherent real and perceived risks need to be addressed
- ▲ Domestic pension funds and PDBs are underutilised sources of capital and must be incentivised to invest more in EMDE alternative investments
- ▲ EMDE impact fund managers have local knowledge that can channel capital into SMEs but requires greater investor support, specifically in the form of catalytic capital
- ▲ Stronger regulation, including definitions of SMEs or incentives towards formalising businesses, is essential to encourage domestic capital to invest locally

As we've explored in chapters 1 and 2, the financing gaps to achieve the SDGs and a Just Transition are staggering. So far, our report focuses mostly on the need to mobilise more capital more effectively from developed markets to EMDEs, and how it can be done. With needs so great, all actors are called upon to play a role. In some EMDE there are large, fast-growing pools of domestic institutional capital which can also be harnessed to meet the needs of a changing planet.

The following chapter examines notable developments in the domestic EMDE landscape that can help unlock institutional capital for the SDGs and a Just Transition. We explore the case for mobilising domestic sources of capital, referencing recent initiatives that are helping to engage those investors with impact investing and global issues and suggest opportunities for greater collaboration between domestic actors and MDBs and DFIs.

Domestic capital providers, including pension funds and public development banks (PDBs), are well-placed to invest in home-grown assets, helping to drive development in their home markets. While pension funds in particular are being given greater ability to invest in alternatives, many lack understanding of the asset class, with the GSG and its national partners working to bridge this education gap.

Local fund managers also have a central role to play. They have unparalleled local knowledge and the ability to invest in SMEs that are critical to the achievement of the SDGs. By supporting them in their fund structuring, fundraising and other fund operations we can in turn strengthen the investment opportunities and business propositions for domestic institutional investors. Once again, international DFIs and MDBs can contribute to the overall capital mobilisation agenda with guarantees and first-loss capital that can de-risk investments and serve as a catalyst for domestic institutional investors.

3.1 Mobilising domestic EMDE actors is a priority for SDG financing

Since early 2021, the cost of capital has increased across the globe as a consequence of monetary tightening to address high inflation, making investments into EMDEs less favourable for investors in developed markets.[116] The increasing cost of capital from international markets adds to the urgent need to unlock pools of domestic capital that can be invested in local currency. Mobilising these sources of capital will be essential for meeting the SDGs and supporting a Just Transition and can address several factors, including:

- **Advancing opportunities that are locally led**. Domestic capital providers know and understand their own local market contexts. In many cases, they are better equipped to direct capital to where it is needed most.
- **Providing access to capital in local currency**. In today's rapidly shifting macroeconomic environment, local currency is less susceptible to foreign currency risk. Having the ability to access local funding adds a layer of protection for domestic borrowers and investees.

3.1.1 Unlocking domestic institutional investments starts with pension funds

While rising interest rates and inflation in the last two years have made investing in EMDEs more challenging for developed market investors, domestic EMDE asset owners and institutional investors in certain countries have been experiencing increasing profitability.[117] As referenced by the IMF, institutions with longer-term financial obligations, such as insurance companies and pension funds, have benefitted in certain respects from elevated global interest rates, which in some instances have reduced the present value of liabilities, improving their financial status.[118] With the majority of beneficiaries of domestic pension funds far from pensionable age, these funds are well positioned to consider longer-term investments tied to the real economy.

TABLE 4

Select EM pension funds by growth rate (end 2022, total AUM ($ millions) and % GDP

Country	% Change (since December 2021)	AUM 2022 ($ million)	Asset as a % of GDP
LATAM			
Chile	4.4	174,792	57.7
Brazil	9.2	454,805	23.9
Asia Pacific			
India	22.1	103,086	3.1
SSA			
Kenya	1.9	12,776	11.5
Nigeria	11.7	32,593	7.4
Zambia	3.2	709	2.7
Uganda	9.1	5,191	11.3

Source: OECD 2022

In recent years, new push factors stemming from government debt defaults and debt restructuring have created even further impetus for pensions to seek to diversify away from treasury bonds and invest more into alternative assets, including infrastructure, funds of funds, and SME financing.[119]

Investing domestically in real assets provides institutional investors with an opportunity to contribute to national growth priorities while supporting social and environmental resilience in the long term. EMDE institutional investors are increasingly being called upon to contribute to country-wide priorities referenced in their National Development Plans or comply with newly adopted ESG, sustainability, or climate regulations introduced by local regulators, Capital Markets Authorities and/or Central Banks.

These factors and others have led to a loosening of asset allocation limits to alternatives in select jurisdictions,[120] such as South Africa[121] and Colombia[122], that are paving the way for greater investment into alternative assets, for example, renewable energy, infrastructure, climate technology, and more.

While limits are being raised, in practice, many EMDE pension funds invest only a negligible percentage into alternatives. For example, in Ghana in 2020, less than 0.03% of pension assets were invested in alternatives, despite a regulatory limit of 15%.[123] Domestic institutional investors are very new to alternatives as an asset class, and most are still very far from utilising their full allotments.

Through direct engagements with domestic pension funds, the GSG and affiliated NABs are working to bridge these knowledge gaps and familiarise pensions with alternatives, and within this, the growing cadre of SMEs aligned to the UN SDGs, as an asset class.[124] Through its engagements, the GSG and NABs have learned that in order to move forward with allocations, domestic actors require better access to information, including investment and performance data, access to case studies and peer support, as well as access to the domestic investment pipeline.

To meet these needs, the GSG, NABs, partners and other global stakeholders, have worked to set up industry collaboratives and peer-led support networks. In 2022, a consortium of international partners including WEF Global Alliance for Social Entrepreneurship, Collaborative for Frontier Finance, the GSG, and Sustainable Development Investment Partnership worked closely with local market-building organisations including Impact Investing Ghana, the Zambia National Advisory Board for Impact Investing, and Impact Investing South Africa, as well as pension fund collectives in three countries (Ghana Pension Industry Collaboration, Zambian Pension Industry Association and Batseta/Asset Owners Forum South Africa) to identify common barriers and solutions and develop investment pipeline opportunities.[125]

The World Bank and select DFIs have also been active in this domain, setting up collaboratives in Kenya, South Africa, and the Asia Pacific region to familiarise pensions with infrastructure, real estate, private equity, and venture capital investing, while sharing due diligence responsibilities, reducing transaction costs in smaller deals, and increasing investor confidence in new geographies. (See **Table 5**)

With new knowledge and skills, these collaboratives are already playing an important first mover role that should be further leveraged to grow allocations in investments linked to the real economy, Nationally Determined Contributions, and thematic areas identified in EMDE National Development Plans linked to the SDGs.

TABLE 5

Asset owner alliances and pooled pension initiatives

Title	Country	Description
Kenya Pension Funds Investment Consortium (KEPFIC)	Kenya	The World Bank has worked with small pension funds and trustees to form the Kenyan Pension Fund Investment Consortium. It provides training at a group level on various asset classes, among other topics, and reviews new investment opportunities as a group.
Asset Owners Forum South Africa (AOFSA)[126]	South Africa	In partnership with the U.S. Agency for International Development, MiDA Advisors, and the World Bank, the Batseta Council of Retirement Funds for South Africa (Batseta), the Asset Owners Forum South Africa (AOFSA) works to mobilise South African retirement funds to invest in infrastructure, real assets and other alternatives. With 13 funds forming the core membership base, this Forum works to enable retirement funds to collaboratively increase their awareness and allocations to infrastructure by creating opportunities for co-investments and for local retirement funds to realise economies of scale by shared information and due diligence research.
Pension Industry Collaborative	Ghana	Ghana NAB's IIGH Pensions Industry Collaborative brings together the largest Pension Funds and Fund Managers to work together to address some of the key issues preventing the industry from investing in alternative assets. This work complements the Fund of Funds that the NAB has recently launched (see below).
Pension Fund Collective	Zambia	Zambia's Pension Fund Collective aims to unlock local institutional capital to increase the capital supply for alternative investments, particularly those intentionally seeking to create positive social or environmental impact.
The Pacific Islands Investment Forum	Pacific Islands	The Pacific Islands Investment Forum is a co-investment platform composed of domestic pension funds. Members work together to develop new pipelines and also co-invest in IFC deals.

3.1.2 Public Development Banks (PDBs) are the most evident and under-utilised partners to mobilise private capital

$23 managed by PDBs globally

Given the current monetary tightening in advanced economies, development experts have continued to consider how international public development capital can engage with local institutions to leverage and mobilise local pools of capital.

Building PDBs in emerging and developing economies into the international policy framework for climate and transition finance will support private capital mobilisation due to their knowledge of local markets, needs and capacities, as well as long-held relationships with stakeholders. As ODI lays out, PDBs can play roles as mobilisers, blenders of concessional finance, pipeline developers, and policy influencers to help remove barriers to capital mobilisation into emerging and frontier economies.[127]

Recognising the need for more collaboration between DFIs and PDBs, in 2020, the French development agency AFD launched Finance in Common, a network representing PDBs and DFIs with an aim of making PDBs more visible and strengthening their role in financing the SDGs. There are 450 PDBs around the world (roughly one or more per country). Though varying widely in size and mandate, **they manage over $23 trillion**, representing perhaps one of the least well-known yet well-placed groups of organisations for economic development.[128]

Despite their ability to deploy de-risking instruments and act as catalysts for private sector investments, most PDBs lack experience in collaborating and co-investing with private investors to support the implementation of national development strategies or structure innovative financial vehicles toward the SDGs at a national scale. Strengthening collaboration with PDBs in EMDEs can further boost domestic private capital mobilisation and more specifically, SME finance, due to their knowledge of local markets, as well as long-held relationships with stakeholders in those markets.[129]

A 2023 Finance In Common paper, *The Role of Public Development Banks in Scaling up Sustainable Financing*,[130] lays out key recommendations to get PDBs more focused on supporting the SDGs and a Just Transition, including aligning PDB mandates, strategy and governance to the SDGs, introducing data management, measurement and impact taxonomies, and pursuing effective collaboration and international support (see **Box 23**).

BOX 23

Actions to Enable PDBs to More Readily Scale Sustainable Finance

- **PDB mandate, strategy, and governance aligned to SDGs**: PDBs' mandates and activities should be aligned with the Paris Agreement and SDGs through the right incentives, as well as with the national/sub-national government policies. An integrated approach towards the SDGs, combining negative screening with positive impact assessment, should be pursued at a strategic and project level
- **Lending and guarantees, pricing and currency risk**: Enabling PDBs to access lower costs of capital would support their longer-term and lower-cost finance. Specifically, reducing the cost of currency risk for PDBs is vital
- **Effective collaboration and international support**: Collaboration with the private sector potentially helps evolve PDBs' business models aligned with future needs. Commitment from the development community including the G20 also supports their mobilisation

Source: Finance In Common (2023)

For instance, to ensure that PDBs fulfil their potential of private capital mobilisation, capacity building and technical assistance targeted to PDBs, as well as access to a pipeline of domestic investors will be required.

3.2 Domestic initiatives are underway to finance SMEs

$5.2 tn
financing gap facing SMEs globally

One area where both domestic EMDE pensions and PDBs can play a strong role in sustainable development and market building is by supporting the growth of small and medium-sized enterprises (SMEs).[131] Supporting micro, small and medium-sized enterprises in EMDEs can play a significant role in promoting inclusive growth and building resilience in the face of macroeconomic shocks worldwide.[132] SMEs account for 50% of employment and contribute up to 40% of GDP in some EMDEs, but have an unmet financing need of $5.2 trillion per annum, equivalent to 1.4X the current level of global SME lending.[133] Building domestic capability and capacity can help support small and growing businesses that are often overlooked by investors.

In this section, we focus on opportunities to build the capacities and channel capital to domestic SMEs that contribute significantly to employment and local development outcomes.

3.2.1 Supporting SMEs is still the most important yet most challenging priority for achieving the SDGs

Without SME growth, EMDEs cannot achieve economies that work for all and a Just Transition. SMEs need access to affordable finance for working capital and business growth. They also require other support mechanisms to increase their chances of growth and positive impact, and to qualify for, receive, and manage loans and investments as required.

On the demand side, inherent real and perceived risks facing small and early-stage businesses hinder financing. (See **Box 24**) These inevitably inform supply-side challenges, leaving financing needs unmet and opportunities gravely overlooked by investors, international and domestic.

BOX 24

Demand side risks to address to facilitate greater credit flows to SMEs[134]

1. Information asymmetry challenge: SMEs may present little to no visibility of their cash flows, past performance, nor how financing is used. This increases the perception of risk among commercial banks who in turn attribute a credit score higher to the business, to the detriment of the SME borrower.
2. Performance risk: SMEs may lack access to accounting or financial experience to know how to pay back the loan. In addition, high-interest rates in some countries confine lending to trading activities, and fail to support the growth financing needs of small businesses.
3. Resilience risk: Factors outside the control of the SMEs may hinder their ability to pay a loan, such as climate, currency or other conflict-related risks.
4. Recovery risk: In instances where SMEs cannot cover their monthly payments, collateral is seized at a high cost to borrowers. Some SMEs lack collateral to begin with, preventing them from being able to access commercial bank financing.
5. Keyman risk: In certain instances, SMEs are not well structured and do not have the proper governance in place, creating challenges for lenders or investors to ensure accountability in the face of bankruptcy or other risks.[135]

Source: Zambia Design Works team (unpublished)

The solution to meeting the financing gap is a holistic one. It involves implementing varied solutions geared toward reducing or mitigating demand and supply-side risks - real and perceived. On the demand side, small businesses must improve their management and operational capacities, including being able to present balance sheet and cash flow statements, invoices, payroll, staff training, and more. On the supply side, lenders and investors must begin to gather data on client businesses and the wider value chain, enhance credit risk scoring mechanisms, build skilled origination teams, and hone lending and investment practices accordingly. Needs on both sides are urgent and require technical assistance support, as well as the acknowledgement that both businesses and lenders will need time to adapt. Suitable pools of capital must be created to underwrite these initiatives, and learnings must be better gathered, shared, and disseminated. (See **Box 25**)

BOX 25

Business Development Support Services for SMEs - Learning from Best Practices

Business development support (BDS) is integral to helping SMEs grow and mature. BDS covers a wide range of training, mentorship, and capacity-building activities that range from helping enterprises better understand their market and gauge demand, to overseeing a budget, managing inventory, and complying with regulation. Depending on how they are provided they can enable enterprises to tap into a network of peers or partners and increase access to funding opportunities or to pools of talent. Enterprises that have received BDS support are perceived by capital providers to be less risky, and better equipped to generate or raise revenue and run a business.[136]

BDS support organisations have been proliferating, expanding the range of support services available to SMEs and the actors underwriting and administering them. In practice, BDS support services differ vastly in terms of effectiveness and cost efficiency, and with wider availability and quantity of services, focus must be placed on the quality of programmes to ensure they have the intended impact of building well-run businesses and boosting job creation.

Fortunately, new efforts are underway to better segment BDS models and determine their effectiveness. The SCALE Toolkit developed by the Argidius Foundation, for example, guides BDS providers and funders on how to implement practices that improve the effectiveness of BDS programs.[137] A subsequent study produced by ISF Advisors focusing on BDS providers for agri-SMEs in Africa found that peer-to-peer BDS approaches have the potential to increase impact and reduce the cost of support. It also called for better data collection on outcomes (revenue, jobs, investment, etc.) to gain further insights into programme effectiveness.[138]

3.2.2 Local fund managers are punching above their weight to finance SMEs at scale

Micro and small enterprises are often too small and too risky for DFIs and institutional investors to invest in directly. This has led to a shortage of growth capital for small and growing businesses (SGBs). In light of the sustainable development and Just Transition challenges that lie ahead, addressing this issue more effectively would make a significant impact.

This is the thesis of the Collaborative for Frontier Finance (CFF) which sees the need for more domestic fund managers to spur economic growth and create positive impacts aligned to the SDGs.[139] Their local capital provider network supports a critical and missing piece of the market-building puzzle, fund managers managing less than $20 million and investing $50–500K in businesses poised for growth. (See **Box 26**)

BOX 26

Debt vs. Equity: Zoom in on Best-in-Class Models for SME Financing

The suitability of traditional venture capital models has been contested, both for local fund managers and SMEs. The Argidius Foundation has conducted research looking at the best ways to finance SMEs at scale, whether and under what conditions commercial bank financing is ideal for growth capital for EMDE SMEs, and when equity capital, managed by smaller fund managers, is optimal.

The KCB bank, headquartered in Kenya, developed a new specialised SME lending programme developed with the Women's World Banking NGO, with support from Argidius. The initiative found that better segmenting the SME market specifically the existing SME portfolio of the bank, and providing business development support services to its clients, allowed the bank to design better products and provide more targeted services. This, in turn, generated growth and success among women-led SMEs, a previously underserved segment. In 10 years, KCB's loan portfolio is slated to grow from $4 million (2017) to $2 billion in 2027, with $500 million already deployed in 2022 across 13,000 loans.

On the equity side, while the private equity and venture capital closed-end fund models have worked in developed economies with larger deals, they are arguably less appropriate for underwriting and managing smaller transactions, argues CFF in its ITF input paper.[140] Sized and managed appropriately, however, equity financing is still greatly needed to support the growth ambitions of smaller-scale businesses. In the coming year, respondents to CFF's Annual Local Capital Provider Survey are seeking to raise $1.5 billion for small and growing businesses in Africa and the Middle East.

$1.5 bn

target fundraising of local fund managers in Africa & the Middle East

As they and others working in the space recognise, local capital managers possess knowledge of the local ecosystem, customers, market needs and supply chain, and must be supported to leverage these factors to achieve further market development.

On the topic of gaps, in CFF's network alone, fund managers in Africa and the Middle East are looking to raise and put to work $1.5 billion in the year ahead and are not allowing the lack of early-stage growth capital to deter them. As they seek to build the market, fund managers are getting creative about building compelling businesses even in the absence of capital. CFF's *2023 Annual Local Capital Provider Survey*[141] details how local capital providers are working at the forefront of an evolving asset class to address the 'missing middle' finance gap ($100K - $1 million) facing small and growing businesses. Using pioneering combinations of vehicle structures, investment instruments, and partnership models, they are able to address the specific growth capital needs of small businesses in EMDEs.

Other programmes are also working to address the resourcing and capacity gaps facing smaller-ticket local fund managers. Through peer-led support networks, fund managers are positioning themselves as a bridge between locally-led solutions developed by SMEs, and domestic institutional investors, pension funds, and commercial, and national development banks.

BOX 27

Examples of capacity building programmes for local fund managers

- The Collaborative for Frontier Finance runs a 100+ member Early Stage Local Capital Provider Network which provides opportunities for peers to work collectively to find innovative solutions to the resourcing and finance challenges.
- The International Climate Fund Accelerator (ICFA) based in Luxembourg, a two-year acceleration programme for climate finance fund managers has trained 34 fund managers through seven cohorts, providing opportunities for fund managers to gain skills and networks to fund the next generation of green businesses globally. To date, the emerging fund managers supported by the initiative have raised $937 million to finance climate-oriented projects
- 2X Global has provided guidance for women fund managers and many DFIs have offered capacity-building support to investees
- Capria is a global venture capital platform helping early growth tech firms in Southeast Asia, India, Latin America, the Middle East, and Africa raise capital

In addition, intermediaries are being set up to pool impact capital and accelerate the growth of the market. Over the past few months, countries such as Australia, Canada, Ghana, Nigeria and Spain (see **Box 28**), have committed to inject a combined $1.5 billion into local wholesalers and fund of funds, learning from the model of Big Society Capital, the UK's impact investment wholesale fund that has played a leading role in scaling fit for purpose financing for UK social enterprises, start-ups and SMEs, helping to channel $11 billion (£9.4 billion) to UK SMEs.

BOX 28

Zoom In: GSG-affiliated NABs are developing national solutions to grow local financial intermediaries that can invest in SMEs & the SDGs

The GSG works with national partners in more than 50 countries to accelerate the flow of capital towards impact. To address some of the issues around financing the SDGs in emerging markets, the GSG and its national partners, called National Advisory Boards (NABs), are actively working to change policy and build pools of impact capital to improve SME finance in Ghana, Nigeria, Zambia and other EMDEs. However, structuring these vehicles is costly and challenging because of the double imperative of making them commercially viable (e.g. attractive for local pensions and other private investors) and designed to deliver impact at scale in less developed capital markets, where a range of risks and liquidity concerns apply. More resources are therefore needed to support the design of such vehicles with financial or non-financial resources, alongside technical and capacity building support to enable the blueprinting and dissemination of such locally grown and relevant solutions.

GHANA: CI-GABA FUND OF FUNDS

The Ci-Gaba Fund-of-Funds is a $75 million blended finance vehicle that will provide funding for West African venture funds and SMEs. 70% of the fund will be raised locally and focus on investing in SMEs in sectors aligned to SDGs. The use of local currency is designed to encourage local market development and capital mobilisation from Ghana's pension industry. The vehicle consists of two tiers of capital, a senior tier structured as preferred shares with return expectations based on the 10-year government bond rate; and a second tier covering a percentage of the first loss from donors or DFIs.

The vehicle will be managed by Savannah Impact Advisors. It is sponsored by Impact Investing Ghana with support from the GSG, FMO Ventures and the Research and Innovation Systems for Africa (RISA) Fund of UK International Development.

NIGERIA: WHOLESALE IMPACT INVESTMENT FUND (WIIF)

The Wholesale Impact Investment Fund (WIIF) is a $1 billion fund with a first close of $100 million that is being set up to finance social enterprises and micro, small, and medium-scale enterprises in the agriculture, education, health, energy, and creative industries sectors, with climate and gender as cross-cutting topics. In May 2023, the Nigerian Ministry of Budget and National Planning pledged to contribute 50% of the fund's first close ($50 million). 90% of the fund will be naira-denominated while the remaining 10% will be dollar denominated. The fund will invest through intermediaries and will provide equity, quasi-equity, debt, guarantees, technical assistance and grants. It is envisioned to be set up as a Shariah-compliant fund.

The WIIF is sponsored by the Nigeria NAB, with learning and research support from the GSG, and design funding from GIZ, the German development agency.

ZAMBIA: CREDIT RISK GUARANTEE SCHEME

Zambia's NAB (NABII) and the Bank of Zambia (BoZ) are collaborating to design a $150 million Credit Risk Guarantee Scheme (CRGS) that will provide low-cost credit to formal and informal SMEs operating in the agriculture value chain. Through a grant supported by the C3 collaborative, the NABII and partners, including GSG, the Collaborative for Frontier Finance, and USAID Edge, are working to assess demand and supply-side gaps in order to create a mechanism that would meet the needs of commercial banks to expand and extend their loan portfolios.

TURKIYE: IMPACT FUND OF FUNDS

The Regional Venture Capital Financial Support Programme for Impact Investment is a $14 million impact fund of funds that will support existing and newly established funds deploying capital to high growth ventures generating a measurable social and environmental impact in the areas around Ankara and the provinces affected by the 2023 earthquakes. Launched by the Ankara Development Agency in 2022, the Agency will contribute up to 25% of the total commitment size to eligible VCs.

ASIA PACIFIC: AUSTRALIAN DEVELOPMENT INVESTMENTS (FORMERLY EMIIF)

The Emerging Markets Impact Investing Fund, rebranded in August 2023 as Australian Development Investments (ADI), is a $250 million Australian government-backed impact wholesaler that supports SMEs and projects in Asia Pacific. The Australia NAB was active in promoting its renewal and expansion.

3.2.3 Strengthening the regulatory environment for the benefit of SMEs

Besides championing greater flows and more effective financing instruments for SMEs, broader systemic reforms are needed to create an enabling environment that is truly supportive of SMEs. To back the effort, domestic policymakers and regulators can pursue tangible steps to enhance the regulatory and governance environment that would enable more domestic actors to channel capital in support of SMEs. Specifically, Central Banks and ministries overseeing SME activities and finance can institute the following reforms that would have a lasting impact on SME growth and access to finance.[142]

1 PROVIDING A MARKET-WIDE DEFINITION OF MICRO, SMALL, AND MEDIUM ENTERPRISES

The lack of a definition for what constitutes an SME creates confusion among market actors. (See **Box 29**)

BOX 29

Zambia's Ministry of SMEs issues official classification

The lack of official guidance on what constitutes a micro, small, or medium enterprise led most commercial banks in Zambia to develop their own proprietary classifications to define these segments.[143] This has made it difficult for national authorities to gather aggregated findings on the key characteristics, policy, and financing gaps facing small businesses. Fortunately, a standardised definition was finally adopted, thanks to a newly established Zambian Ministry for SME Development. It outlined four criteria - turnover, number of employees, legal status, capital investments) against which the three categories of businesses will be determined.

An example of turnover amounts within the new classification is provided:

Size	Turnover
Micro	K1 - K1,000,000
Small	K1,000,001 – K10,000,000
Medium	K10,000,001 - K50,000,000

Banks are aligning their lending segments to the new definition, providing access to better and more transparent data for national authorities who can use this information to develop policies and funding instruments that can better meet the needs of the different business segments.

250,000
informal businesses were registered in Nigeria and supported by the government's COVID-19 Survival Fund

2 SME REGISTRATION

While official numbers are hard to come by, it is estimated that one-third of low- and middle-income countries' economic activity is generated in the informal sector,[144] covering about two billion workers, or 60% of the world's employed population.[145] Moving businesses from the informal to the formal sector is an important step in reducing poverty and ensuring inclusive business practices.[146] Business registration initiatives are important as they provide data for national entities and help generate tax revenue. COVID-19 served as a catalyst for registering businesses, since in many countries only businesses that were registered with the tax authority would be eligible for aid relief. The Nigeria NAB was instrumental in helping to register 250,000 informal enterprises as part of the government's COVID-19 Survival Fund, an NGN 75 million fund designed to support distressed SMEs.[147] More initiatives like these are needed to incentivise enterprises to enter the formal economy, which will in turn help governments set favourable policies and financing opportunities that meet needs.

❸ CREDIT BUREAU/ENFORCEMENT OF LOAN PAYBACK/BANKRUPTCY LAWS

Governance and enforcement of credit reporting, both positive and negative, is especially important when thinking about SMEs. Data managed by credit bureaus helps to reduce uncertainty about borrowers' creditworthiness, allowing banks to extend appropriately sized loans.[148] These institutions add to a culture of accountability within the lending sphere, helping entities roll out new lending programmes over the long term. IFC runs a credit bureau programme aimed at helping central banks to set up and maintain nationwide platforms to collect credit and payment history. To date, the programme has helped to establish credit bureaus in eight West African states - Benin, Burkina Faso, Ivory Coast, Guinea Bissau, Mali, Niger, Senegal and Togo.

3.3 Linking MDBs and DFIs to Domestic Capital Mobilisation Initiatives to Enhance Support for SMEs

As demonstrated, growing gaps and a rapidly changing planet require an 'all hands on deck' approach by all stakeholders to mobilise capital at pace. From where we sit, we see particular opportunities for MDBs and DFIs to strengthen cooperation and support local actors and initiatives to channel capital more efficiently and effectively for the SDGs.

These efforts include helping domestic institutions de-risk their investment in SMEs through the establishment of emerging market private debt funds and guarantee schemes, growth equity funds or impact investment wholesalers.

3.3.1 Facilitate de-risking initiatives with clearer SME finance and SDG impact outcomes

One way for DFIs to channel capital to SMEs is to do so via guarantees. Guarantees to support local currency lending for SMEs have been rolled out by DFIs in cooperation with public institutions (ministries, central banks) and as well as with commercial entities (commercial banks and microfinance institutions).[149]

SME Guarantees have been criticised in the past for not providing sustainable solutions to EMDEs. Two key problems lie in the fact that loans must be paid back within the guarantee period, often challenging for SMEs in certain sectors, and once the guarantee period is up and incentives and safeguards are removed, commercial banks are no longer incentivised to continue their lending programmes. **To ensure they are sustainable, guarantees need to be designed as holistic schemes that integrate Business Development Services (BDS), technology solutions, value chain and regulatory reforms.** Additionally, commercial lenders must commit time and resources during the guarantee period to ensure the lending programmes become key facets of their corporate offerings. Examples of bond funds and guarantees enabling local lenders to extend credit to SMEs and build a sustainable pipeline are shown below. (See **Box 30**)

BOX 30

Guarantee Programmes encouraging domestic lending to SMEs

EURIZ SME GUARANTEE FACILITY

EURIZ, a $873 million guarantee facility targeting MSMEs in African, Caribbean and Pacific countries. The programme, which completed its investment period in 2022, was co-financed by the European Union and the Organization of African, Caribbean, and Pacific States, and implemented by the Agence Française de Développement (AFD), PROPARCO and the Swedish International Development Agency (SIDA). Financing from SIDA and AFD, a public development bank, helped absorb additional costs generated by hedging mechanisms implemented to deploy credit lines in local currency. The partnership also enabled the deployment of technical assistance to build the capacities of the financial institutions to lend to SMEs, while strengthening the capacities of SMEs to access commercial financing.

AFRICA LOCAL CURRENCY BOND FUND

The Africa Local Currency Bond Fund (ALCBF) was established by KfW on behalf of the German Ministry for Economic Cooperation and Development in 2012 to support low-income households and SMEs, advancing financial inclusion, infrastructure, agriculture, housing, education, healthcare and renewable energy. The ALCBF promotes primary corporate bond issuances in local currency by working with African issuers, investors and intermediaries to bring new deals to market. The Fund acts as an anchor investor and provides technical assistance to bring new deals to market. To date, the fund has raised $170 million from DFIs and impact investors, including FSD Africa, FMO, OPIC, Calvert Impact Capital, AfDB and IFC. The ALCBF is an example of how DFIs can structure an investment that de-risks local lending for SMEs.

FMO NASIRA PROGRAMME

The Nasira Programme is a loan portfolio guarantee programme deployed in Sub-Saharan Africa and countries bordering Europe that encourages banks to lend to groups they would usually consider too risky, such as agriculture SMEs, and young, female, and migrant entrepreneurs. As of 2022, the programme had made 11 investments and deployed some $175 million (€160 million). Thanks to EU funding from the EFSD+ guarantee scheme, the programme was positioned for further expansion into Asia, Latin America, the Caribbean, and Turkiye, as well as into 'new' sectors, including rural/agri-SMEs, to stimulate local production and food security and clean energy solutions.

3.3.2 Co-Designing and investing in catalytic capital approaches

Given the high level of corporate debt that has followed the COVID-19 pandemic, combined with higher costs of capital due to interest rate hikes in advanced economies in the past few years, the credit environment surrounding SMEs has become tighter. More instruments that blend public, private, and in some cases, philanthropic capital are needed to encourage financial intermediaries to expand their lending to SMEs. Catalytic capital has been shown to be an essential tool to bridge capital gaps.[150 151]

Catalytic approaches warrant further expansion and resourcing from all organisations. They have the potential to help investors better understand the financing gaps, generate new pipelines, and contribute to local capacity building. DFIs and institutional investors especially stand to benefit greatly from enhanced market opportunity by providing first loss tranches in new funds, and technical support to build the management skills and capacities of fund managers.

BOX 31

Catalytic capital funding platforms and programmes

CATALYTIC CAPITAL CONSORTIUM (C3)

The MacArthur Foundation in partnership with the Rockefeller Foundation and Omidyar committed $150 million to support the design and development of investment instruments funds that address some of the world's most pressing challenges. C3 aims to demonstrate the power of catalytic capital to extend and deepen the reach of the impact investing field. Its in-depth learning library provides invaluable resources and evaluation studies on the topic.

Now in its fifth year, its support has amongst others helped design the first forest resilience bond, and an impact investment model to tackle the needs of informal settlements, a GSG-led project. The consortium has also provided funding to design a credit risk guarantee scheme on behalf of the Bank of Zambia, a project co-led by NABII Zambia, the Zambian National Advisory Board for Impact Investing, GSG's affiliated national partner.

MASTERCARD FOUNDATION AFRICA GROWTH FUND

Mastercard Foundation Africa Growth Fund is a private-led catalytic fund of funds initiative that supports narrowing the gap in impact investment for growth-oriented African SMEs. The initiative will invest $150 million in African investment vehicles committed to advancing gender equity in entrepreneurship and $50 million in business development programmes to de-risk those vehicles, aiming to enable 30 million young people to access decent work opportunities by 2030.

FSD AFRICA

FSD Africa is a regional development agency funded by UK aid that delivers policy and regulatory reform and capacity strengthening to address systemic challenges within Africa's financial markets. It also invests risk capital in cutting-edge ideas with potential for significant impact. FSD Africa aims to leverage investments of $153 million (£122 million) to mobilise over $2 billion (£1.6 billion) for projects that address both climate change and the needs of low-income, marginalised groups and women between April 2021 and March 2026.

CONVERGENCE DESIGN FUNDING PLATFORM OFFERS

Convergence Design Funding Platform offers a unique market acceleration opportunity for practitioners to secure feasibility studies and proof of concept stage funding to develop and launch catalytic blended finance vehicles that aim to attract private capital to sustainable development at scale.

Recent opportunities include grants to design a fund for climate resilience in Asia and the Indo-Pacific region sponsored by the Australian government, a programme by UBS Optimus Foundation to support financing mechanisms to improve financing for tertiary education, and catalytic blended finance solutions for emerging markets, sponsored by Global Affairs Canada.

In 2022, Convergence and USAID published the Action Plan for Climate and SDG Investment Mobilization,[152] which outlines strategies for MDBs and DFIs to enhance the deployment of catalytic financing, emphasising the need for shareholders to establish key performance indicators to align these institutions with the 2030 Agenda and prioritise the mobilisation of private investors. Their action plan lays out a mobilisation blueprint for development stakeholders including:

- Increase the supply of flexible catalytic funding by crowding in a larger universe of resources and innovation
- Make MDBs and DFIs catalysts of mobilisation
- Maximise the investable pipeline through more integrated development and climate finance systems
- Provide investors with access to the best investment data and mobilisation resources
- Empower local capital markets and financial intermediaries

BOX 32

Impact Investment Institute's Bridging Divides: A guide on using catalytic capital for a Just Transition

A paper released in November 2023 by the Impact Investment Institute (GSG-affiliated UK NAB)[153] provides guidance and case studies for catalytic capital providers, including development finance institutions, governments, philanthropic organisations, private investors, and corporations, seeking to mobilise private capital for a Just Transition that combines climate action with social justice and local development needs.

BOX 33

Blended Finance for SMEs - Fostering Shared Learning Opportunities between Developed and EMDE Markets

A new collaboration between Big Society Capital (UK) and the European Bank for Reconstruction and Development (EBRD) is sharing learnings around financing models for SMEs sourced across developed and developing countries, broadening the toolkit of models that can be implemented or iterated upon according to country context, available opportunities and constraints.

Village Capital has also developed an innovative finance tool called Capital Explorer, providing access to descriptions of innovative financing vehicles that are fit for purpose for social enterprises, and micro, small, and growing businesses.

Other examples include the Climate Policy Lab which focuses on the development of new climate finance instruments, and Anglo American which is looking to apply catalytic capital to designing new investment instruments for South African SMEs.

BOX 34

Zoom in on Catalytic Capital to Provide Access to Tech-Enabled Solutions

Better access to technology has the potential to play a significant risk mitigation role that can benefit SMEs, both from a financial and environmental sustainability perspective.

- **Financial sustainability**: Today there are an estimated 1.6 billion registered digital money accounts, with the number of accounts and amounts transferred growing 13% and 22% respectively year on year.[154] Financial technology is helping SMEs to maintain a data trail of transactions, facilitate payments, and widen market access, among other benefits. Lending platforms enabled by fintechs have the potential to reduce the number of non-performing loans.[155] Technology is also making insurance for SMEs affordable and accessible for the first time, improving entrepreneurs' willingness to pay, an important advance in light of the many market, currency, and climate-related risks facing SMEs.[156]
- **Environmental Sustainability**: Technology is helping SMEs in climate-vulnerable sectors to gain added control of their environment, helping them plan in advance, utilise resources more efficiently, and optimise production, contributing resilience not only to employees but to their entire value chains. Greater access to climate technologies stands to benefit both SMEs and capital providers. From a capital provider perspective, these actions help to mitigate information asymmetry and performance risks.[157]

In developed countries, early subsidies provided by public entities or angel investment have been shown to have a demonstrable effect on the future growth of SMEs.[158] Public programmes in the form of grants, including match funding, and convertible loans, have been shown to provide SMEs with a solid base to develop operations.[159]

Catalytic capital can help domestic investors and government actors alike integrate technology into their investment and risk miitigation processses.

Despite up to half of their portfolios being made up of financial intermediaries,[160] **DFIs have not adequately prioritised investing in domestic impact fund managers, missing opportunities to build up local capital markets that can enable SMEs to access capital when they require it, and in the form needed to grow.** Experts acknowledge the role DFIs have played in developing private equity and venture capital in emerging markets by backing new fund managers but believe they can do more to invest in local fund managers, especially smaller funds.[161] They also see the need for more transparency on the impacts of their investments via financial intermediaries, which would lead to a clearer demonstration of SDG outcomes achieved through such investments.

DFIs can also engage more actively by supporting business development support services and using these platforms to source new pipeline opportunities. This ensures entrepreneurs are exposed to sound social, environmental, and governance practices even from an early stage. Accelerator programmes also adequately prime entrepreneurs for commercial success through effective managerial and operational training.

Amidst the critique, DFIs have initiated programmes to boost their involvement in venture capital investing. In the last two years, DFIs have launched catalytic financing programmes. Most are still new and learnings are still emerging. (See **Box 35**)

BOX 35

DFIs launch programmes to support SMEs and domestic fund manager development and investment

Growth Investment Partners Ghana is a local currency financing vehicle launched by BII in July 2023, with a commitment of up to $50 million. The vehicle aims to provide long-term capital that addresses a financing gap for Ghanaian SMEs, which account for over 80% of all employment. The vehicle will directly support up to 150 SMEs in Ghana over the next 15 years.

Prosper Africa is a US government programme designed to help businesses and investors gain access to government grants, loans, and other financing opportunities sourced from 17 U.S. Government agencies. To date, it has helped close 1,236 deals between the US and African countries amounting to $70.8 billion in investment.

In August 2023, the programme announced the Prosper Africa Catalytic Investment Facility, which will co-invest in 10+ African fund managers. The programme currently supports 10 African fund managers, including an accelerator programme for first-time female fund managers, a female-led fund deploying capital into medium-sized businesses in the high-growth sectors of food, climate, health and education in East Africa and Zambia, as well as a pre-seed impact fund and accelerator that will catalyse capital into high-impact tech startups working in the climate space.

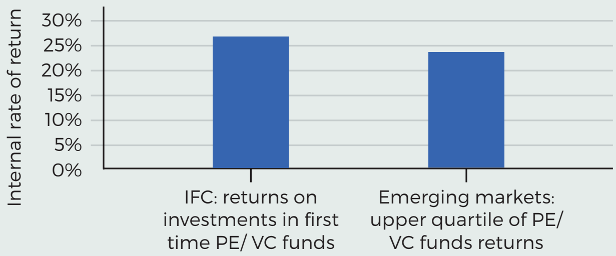
BOX 36

IFC's commitment to invest in best-in-class first-time fund managers

To help develop emerging fund managers, IFC invests a substantial proportion of its funds with new fund managers. During the early 2000s, IFC supported many first-time PE/VC funds in nascent markets with little previous PE/VC fund activity. **IFC's investments in first-time funds outperformed global benchmarks and, as shown, also outperformed IFC's investments in follow-on funds in more established markets.**

*Note from the authors: We acknowledge that the data provided is dated. Our assumption is that the outperformance remains true. However, the lack of information and data on such kinds of essential questions only reinforces the call to significantly accelerate the disclosures of disaggregated historic DFI investment performance data to improve information and create further incentives for private capital investments in EMDEs. See **Box 23** about GEMs.*

IFC'S Returns from Investing in First Time PE/ VC Funds Outperform Follow on Funds and Industry Benchmarks (2000-2010)



Source: IFC (2010)

Mobilising growing sources of domestic investment relies on many of the same considerations as drawing international institutions into EMDEs. For example, domestic pension funds also require de-risking, with DFIs and MDBS able to offer the guarantees and first-loss capital that can facilitate their investment. However, it is also essential to recognise the differences in mobilising international capital sources.

Domestic private investment ecosystems are relatively undeveloped, with investors requiring more education - and again data - on investing in alternative assets, such as infrastructure and SMEs, than their developed market peers. And while local fund managers are among the best-placed to understand the landscape and needs of their domestic markets, they also need assistance with capacity building, with the creation of a fund of funds and other vehicles that can bridge the gap between large investors with sizeable capital to deploy and SMEs with smaller investment requirements.

Developing and leveraging domestic investment is an essential part of the private capital mobilisation puzzle. Capital needs to be encouraged to flow internationally to meet the SDGs and ensure a Just Transition in EMDEs. But for that to happen, many international investors will want the reassurance of domestic pension funds and other institutional investors supporting opportunities on their home turf.

Recommendations

INVESTORS AND GOVERNMENTS: Better support the development of investable opportunities. This can only happen with strategic and concerted efforts to back businesses with high impact and high growth potential, alongside innovations and local funds with the potential to scale capital flows towards them. As in developed markets, this requires public subsidies and grant capital.

MDBs, DFIs AND CATALYTIC CAPITAL PROVIDERS: Support domestic initiatives, such as the ones led by GSG-affiliated National Advisory Boards, working to deploy locally designed solutions at scale. Specifically, increase the supply of catalytic capital available to boost such solutions, through, for instance, the creation of regional catalytic capital facilities.

DOMESTIC EMDE INVESTORS: Unlock domestic capital for SDGs. We know that domestic public and private capital may not be sufficient to achieve the SDGs. However, while collective work progresses to revamp the global financial architecture towards a just and sustainable world, it is essential to focus efforts on unlocking capital most proximate to needs, from PDBs and domestic institutional investors.

Conclusion and Recommendations

Increasing risk appetite & supporting domestic collaborations

We have polished the problem long enough. Common ground has been established around what needs to be done, most notably reform of DFI and MDB mandates and greater risk mitigation for private capital. There is now consensus within the G20 and other high-level forums about the need to implement difficult but essential shifts if we are to achieve the SDGs by 2030.

The solutions to help channel significantly more private capital towards the SDGs are known. There needs to be an active push at all levels to disseminate and implement those solutions at scale and with urgency. Specifically, we call on investors, DFIs & MDBs, donors and others to:

MDBs, DFIs, AND INVESTORS: Support and invest in domestic initiatives led by coalitions in EMDEs, such as those led by GSG NABs (versus global coalitions that seem slow to deliver or are hard to be held accountable for their pledges). This includes increased support, especially subsidised or grant-funded capacity building and technical assistance for local business development, local early-stage impact funds, efforts to launch domestic impact funds (attracting domestic capital investments), and the structuring of new assets, with a focus on countries with significant need and/or mobilisation potential. The increase in the supply of catalytic capital will help boost the deployment of such local solutions, for instance through new regional catalytic capital facilities.

MDBs, DFIs, AND INVESTORS: Invest in and deploy existing solutions for a Just Transition and SDGs. Green, Social, Sustainable, and Sustainability-linked bonds, insurance or securitisation of DFI assets, dialling up the amounts available for guarantees, recapitalisation or replication of successful facilities (such as MIGA, MCCP, PIDG or TCX), and more efficient deployment of de-risking instruments are already available and will lead to higher amounts of institutional capital flowing to the SDGs in EMDEs. The de-risking solutions exist but need to be implemented at scale, more frequently by MDBs, DFIs and PDBs. In turn, private investors need to get out of their comfort zones and stop waiting for MDBs and DFIs to systematically de-risk their investments in EMDEs. Numerous profitable opportunities are investment-ready and will lead to attractive returns.

MDBs, DFIs, AND THEIR SHAREHOLDERS: Develop and implement mobilisation strategies for DFIs, alongside ambitious targets and accountability towards them as part of DFI mandates and operations. This can significantly move the needle for private capital mobilisation overall, from less than 1X closer to an ideal, although as-yet unrealistic, 10X. The setting of such overall targets should start with a more sophisticated approach to capital mobilisation, with much clearer strategies about whether and where to pursue capital mobilisation targets or market-building objectives. There should also be clearer setting of targets for DFI business segments, coupled with more focus on and support for the demand side of such investment.

MDBs AND DFIs: Unlock data and evidence, specifically data housed in the GEMs database, to enable investors to develop a better understanding of which investments are most impactful. All the other actions highlighted above can be significantly accelerated if more data is made available at all stages of the process. Data and a better understanding of success factors for capital mobilisation will inform key considerations, such as the relationship between risk and reward, development impact and mobilisation, as well as the portion of DFI portfolios or balance sheets that should be used for capital mobilisation.

Speed and scale are the two most important considerations.
Solutions must be implemented that can draw in investors who are most proximate to the needs, whilst all actors need to step up to the mark and take more risks in the investment process.

Glossary

Blended Finance	The strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries, where additional finance refers to commercial finance that does not primarily target development outcomes in developing countries, while development finance is public and private finance that is being deployed with a development mandate. (OECD, 2020)
Capital Adequacy Framework	A set of regulations and guidelines established by financial regulators to ensure that banks and financial institutions maintain an adequate amount of their own shareholder capital to cover their risks and potential losses.
Catalytic Capital	Debt, equity, guarantees, and other investments that accept disproportionate risk and/or concessionary returns relative to a conventional investment in order to generate positive impact and enable third-party investment that otherwise would not be possible. (MacArthur Foundation, 2019)
Climate Adaptation	Adjustment in natural or human systems in response to actual or expected climatic stimuli or their effects, which moderates harm or exploits beneficial opportunities. (IPCC, 2007)
Climate Finance	Climate finance refers to local, national or transnational financing, which may be drawn from public, private and alternative sources of financing aimed at climate mitigation or climate adaptation. Climate finance is critical to both reduce emissions and allow countries to adapt to the adverse effects and reduce the impacts of climate change. (UNFCCC)
Climate Mitigation	A human intervention to reduce the sources or enhance the sinks of greenhouse gases. Examples include using fossil fuels more efficiently for industrial processes or electricity generation, switching to solar energy or wind power, improving the insulation of buildings, and expanding forests and other “sinks” to remove greater amounts of carbon dioxide from the atmosphere. (UNFCCC)
Development Finance Institution (DFI)	A government-backed institution that invests in private sector projects in low and middle-income countries to promote job creation and sustainable economic growth.
Guarantees	A legally binding agreement under which the guarantor agrees to pay some or all of the amount due on a loan in the event of non-payment by the borrower.
Impact Investment	An investment made with the intention to generate positive, measurable social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets, and target a range of returns from below market to market rate, depending on investors’ strategic goals. (GIIN)
Informal Economy	All economic activities by workers and economic units that are – in law or in practice – not covered or insufficiently covered by formal arrangements. (ILO)
Just Transition	Ensuring that no one is left behind or pushed behind in the transition to low-carbon and environmentally sustainable economies and societies. (UN, 2023)
Multilateral Development Bank (MDB)	An international financial institution established by two or more countries to encourage economic development. MDBs play a key role in providing capital for impact investment in emerging markets.
Nationally Determined Contribution (NDCs)	A climate action plan to cut emissions and adapt to climate impacts. Each Party to the Paris Agreement is required to establish an NDC and update it every five years. (UN)
Net Zero	Cutting greenhouse gas emissions to as close to zero as possible, with any remaining emissions re-absorbed from the atmosphere, by oceans and forests for instance. (UN)
Private Capital Mobilisation	Attracting additional capital from private entities to support development projects. It Includes both private direct mobilisation and private indirect mobilisation. Multilateral development banks have defined this as investment by a private entity, which is defined as a legal entity that is (i) carrying out or established for business purposes and (ii) financially and managerially autonomous from national or local government (World Bank, 2020).

Small and Medium-Sized Enterprises (SMEs)	Businesses that employ fewer than 250 people. SMEs are further subdivided into micro enterprises (fewer than 10 employees), small enterprises (10 to 49 employees), and medium-sized enterprises (50 to 249 employees). (OECD)
Small, Medium and Growing Businesses (SGBs)	Commercially viable businesses with five to 250 employees that have significant potential, and ambition, for growth. Typically, SGBs seek growth capital from $20,000 to $2 million. (ANDE)
The Real Economy	The part of the economy that includes all businesses that produce goods and services and distribute them on the market. Within the real economy, enterprises seek resources to make their own productive investments in equipment, technology and human resources.
UN Sustainable Development Goals (also known as the Global Agenda)	The Global Goals is another term for the UN Sustainable Development Goals, a set of 17 interconnected social and environmental priorities that should be achieved by 2030 to safeguard people and the planet.

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End Notes

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[68] Data is based on Convergence's database. Information accessed October 2023. Available at: https://www.convergence.finance/blended-finance#blending-trends; Convergence is a recognised Knowledge Partner of the 2023 ITF.

[69] ITF (2021). *Mobilising institutional capital towards the SDGs and a Just Transition*. Available at: https://www.impact-taskforce.com/media/xe5dsend/workstream-b-full-report.pdf

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[74] See Convergence (2023). *ITF input paper*. Available at: https://www.impact-taskforce.com/media/znod30u3/convergence-itf-input-paper.pdf

[75] Convergence. *Capacity building*. Available at: https://www.convergence.finance/capacity-building/library

[76] Convergence (2022). *The action plan for climate and SDG investment mobilization - high-level summary*. Available at: https://www.convergence.finance/resource/the-action-plan-for-climate-and-sdg-investment-mobilization-high-level/view

[77] See Convergence (2023). *ITF input paper*. Available at: https://www.impact-taskforce.com/media/znod30u3/convergence-itf-input-paper.pdf

[78] SystemIQ (2023). *Better guarantees, better finance*. Available at: https://www.systemiq.earth/wp-content/uploads/2023/06/Blended-Finance-Taskforce-2023-Better-Guarantees-Better-Finance-1.pdf.

[79] The Blended Finance Taskforce was established to help mobilise large scale capital for the UN SDGs and includes ~ 50 experienced practitioners and experts, from across the finance, business, development and policy community. It publishes sector focused reports detailing how blended finance can be brought to bear to achieve more impact and mobilise more private capital.

[80] SystemIQ (2023). *Better guarantees, better finance*. Available at: https://www.systemiq.earth/wp-content/uploads/2023/06/Blended-Finance-Taskforce-2023-Better-Guarantees-Better-Finance-1.pdf.

[81] SystemIQ (2023). *Guarantees can help unlock $2.4 trillion for climate in emerging markets*. Available at: https://www.systemiq.earth/guarantees-climate-emerging-markets/

[82] See PRI's Responsible Investment Regulation Database. Available at: https://www.unpri.org/policy/regulation-database#:~:text=Methodology%20and%20categories,last%20updated%20in%20Q1%202022.

[83] ITF (2021). *Mobilising capital for a Just Transition and the SDGs in emerging markets*. Available at: https://www.impactinvest.org.uk/wp-content/uploads/2023/02/Workstream-B-Report.pdf

[84] World Bank (2020). *Annual report on global economic prospects*. Available at: https://www.un.org/development/desa/dpad/publication/world-economic-situation-and-prospects-2023/

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[86] Financial Times (2021). *Wanted: funding models that deal with Africa's infrastructure paradoxes*. Available at: https://www.ft.com/content/58536842-4856-4476-bdb1-58bb2d629486

[87] Excerpt from remarks provided by Vuyo Natoi, Co-MD of African Infrastructure Investment Managers at GSG's Impact Summit Series in September 2023.

[88] World Bank (2023). *World Bank names 15 leading CEOs and chairs to join the private sector investment lab*. Available at: https://www.worldbank.org/en/news/press-release/2023/07/10/ceos-and-chairs-to-join-private-sector-investment-lab

[89] See '2.4.2 Institutional investors' key barriers to investing in emerging markets in private transactions' (pages 58-68) in ITF (2021). *Mobilising capital for a just transition and the SDGs in emerging markets*. Available at: https://www.impactinvest.org.uk/wp-content/uploads/2023/02/Workstream-B-Report.pdf

[90] ITF(2021). *Mobilising capital for a just transition and the SDGs in emerging markets*. See pages 73-84 for a broader presentation of instruments and tools to accelerate and expand the flow and effectiveness of capital.

[91] CGD (2023). *Taking stock of MDB and DFI innovations for mobilizing private capital for development*. Available at: https://www.cgdev.org/sites/default/files/taking-stock-mdb-and-dfi-innovations-mobilizing-private-capital-development.pdf

[92] CGD (2023). *Taking stock of MDB and DFI innovations for mobilizing private capital for development*. Available at: https://www.cgdev.org/sites/default/files/taking-stock-mdb-and-dfi-innovations-mobilizing-private-capital-development.pdf

[93] Devex (2023). *Opinion: Private capital for development requires new business models*. Available at: https://www.devex.com/news/opinion-private-capital-for-development-requires-new-business-models-105515

[94] Other examples and perspectives on syndication can be found in this article published by FMO: https://future-minded.fmo.nl/future-minded-blended-finance/multiple-perspectives-on-syndications/

[95] World Bank (2023). *Green, Social, and Sustainability (GSS) bonds market update - January 2023.* Available at: https://thedocs.worldbank.org/en/doc/98c3baab0ea4fc3da4de0e528a5c0bed-0340012023/original/GSS-Quarterly-Newsletter-Issue-No-2.pdf

[96] GSG (2023). *Financing SDGs in emerging markets*. Available at: https://gsgii.org/reports/financing-sdgs-in-emerging-markets/

[97] It should be noted that none of these initiatives should come at the expense of an EMDE country's debt position. To prevent such scenarios, MDBs and DFIs can consider ways in which to de-risk private and lower the costs of capital for private sector actors in EMDEs to issue these bonds.

[98] Activating special drawing rights (SDRs) refers to activating an international reserve asset created by the IMF to supplement the official reserves of member countries. It involves a claim on the freely usable currencies of IMF members, with the aim of providing a country with added liquidity. To date, the largest allocation amounted to SDR 660.7 billion (equivalent to about $943 billion) to support countries affected by COVID-19. As highlighted in a 2022 article by the Centre for Global Development, "SDRs can provide some of the capital needed to ramp up MDB lending to LMICS for climate change and other critical development tasks." See CGD (2022). *How we can put SDRs to work in the fight against climate change—the multilateral development bank option*. Available at: https://www.cgdev.org/blog/how-we-can-put-sdrs-work-fight-against-climate-change-multilateral-development-bank-option. Debt swaps are viewed as a way to accelerate access to finance while simultaneously reducing a country's debt burden, an area that can have positive knock-on effects for further investment. Debt for Nature swaps have been applied in countries like the Seychelles and Belize, where $21 million and $553 million in debt, respectively, were forgiven in favor of local nature conservation efforts. Brookings (2023). Debt-for-adaptation swaps: *A financial tool to help climate vulnerable nations*. Available at: https://www.brookings.edu/articles/debt-for-adaptation-swaps-a-financial-tool-to-help-climate-vulnerable-nations/

[99] For more information on AFD's SDG Bond Framework, see https://www.afd.fr/sites/afd/files/2020-10-07-38-47/sdg-bond-framework-afd.pdf

[100] CGD (2023). *Taking stock of MDB and DFI innovations for mobilizing private capital for development*. Available at: https://www.cgdev.org/sites/default/files/taking-stock-mdb-and-dfi-innovations-mobilizing-private-capital-development.pdf

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[105] The Blended Finance Taskforce (2023). *Better guarantees, better finance*. Available at: https://www.systemiq.earth/wp-content/uploads/2023/06/Blended-Finance-Taskforce-2023-Better-Guarantees-Better-Finance-1.pdf.

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[114] Based on multi-stakeholder discussions at GSG's Global Leadership Meeting (GLM), June 2023.

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[116] IMF (2023). *Global financial stability report, October 2023.* Available at: https://www.imf.org/en/Publications/GFSR/Issues/2023/10/10/global-financial-stability-report-october-2023

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[123] CFF (2022). *Unlocking local pension fund capital*. Available at: https://static1.squarespace.com/static/59d679428dd0414c16f59855/t/6336d650d647c054b1336fbd/1664538207001/CFF+Unlocking+local+pension+fund+capital.pdf

[124] For more on GSG-affiliated NAB engagement initiatives in 15+ countries aimed at increasing awareness among the pension industry representatives on sustainable and impact investing, see GSG(2023). *Pensions and impact investing: How are NABs engaging with pension funds to advance the market*. Available at: https://gsgii.org/reports/pensions-and-impact-investing/

[125] See the consortium's learning output, Unlocking local pension fund capital for small business finance. Available at: https://static1.squarespace.com/static/59d679428dd0414c16f59855/t/6336d650d647c054b1336fbd/1664538207001/CFF+Unlocking+local+pension+fund+capital.pdf

[126] More on the objectives of engagement, investment terms, performance, and regulatory constraints for the initiatives in South Africa, Ghana, and Zambia are accessible here: CFF (2022). *Unlocking local pension fund capital for small business finance*. Available at: https://static1.squarespace.com/static/59d679428dd0414c16f59855/t/6336d650d647c054b1336fbd/1664538207001/CFF+Unlocking+local+pension+fund+capital.pdf. Information on Kenya, Rwanda, Uganda, and Tanzania is available here: FSD Africa (2019). *Private equity investing for pension funds in East Africa*. Available at: https://www.fsdafrica.org/wp-content/uploads/2019/10/Market-Study-Report1.pdf

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[134] Based on the written submissions of Elias Chipimo, CEO and Co-Founder of Mentor Me, part of the Design Works team working with the National Advisory Board for Impact Investing Zambia (NABII Zambia), GSG, CFF, and USAID EDGE

on the design of a Credit Risk Guarantee Scheme with the Bank of Zambia. See https://mentormeafrica.com/; The Argidius Foundation has also published extensively on this topic noting lack of understanding of customer needs, fragmented business models, and lack of collateral. See https://www.argidius.com/en/learning/2-billion-for-women-led-small-and-medium-sized-enterprises

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[142] This section is informed by knowledge and expertise shared and developed by members of a technical team of which GSG is a member, including the National Advisory Board for Impact Investing Zambia, the Collaborative for Frontier Finance (CFF), and MentorMe, tasked with designing a new credit risk guarantee scheme in collaboration with the Bank of Zambia. The project is funded by the Catalytic Capital Consortium (C3).

[143] Based on information gathered at an SME financing workshop, part of the Design Works for the CGRS with Zambian commercial banks in Lusaka, October 31, 2023.

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[151] For more on catalytic capital see Catalytic Capital Consortium. *Introductory resources on catalytic capital*. Available at: https://newventurefund.org/wp-content/uploads/2021/03/C3-Introductory-Resources-1.pdf

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[157] For more information see the work of Adapta.earth, a climate and agriculture data intelligence company developing solutions for financial intermediaries. Available at: https://www.adapta.earth/

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