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To Blend or not to Blend
Towards a Belgian Blended Finance Policy

Hugo Couderé

Institute of Development Policy (IOB), University of Antwerp
Email : hugo.coudere@uantwerpen.be

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Preamble and Acknowledgements

BeFinD is a consortium of four Belgian research centres at three different universities: CRED at the University of Namur (CRED), IOB at the University of Antwerp (IOB), and HIVA and GGS at the University of Leuven (HIVA & GGS). It performs policy-oriented research related to Financing for Development. The research is done on behalf of the Belgian Federal Public Service Foreign affairs, Foreign Trade and Development Cooperation, and hosted by the Flemish Inter-university Council (VLIR-UOS). This Working Paper was written by Hugo Couderé under supervision of Professor Danny Cassimon, who is leading the BeFinD programme at IOB. I also wish to thank Gaëlle Jullien of the Inclusive Growth department of DGD, Pieter Vermaerke, OECD/DAC coordinator at DGD, Dirk Brems EU coordinator at DGD, Luuk Zonneveld CEO BIO, and Mirco Goudriaan and Peter Stoffelen of the DGGF. The Working Paper is based on literature study, on information provided by the persons who were mentioned and on live practical experience in blended finance of the author. The author was not a member of the Blended Finance Working Group of the Belgian Development Cooperation and as such this Working Paper is an "outsider's view". Finally, I would like to express my sincere gratitude to Paul Bottelberge, OD Practitioner, for his supportive feedback. The views and opinions expressed in this paper are those of the author and do not necessarily reflect those of the resource persons and institutions mentioned.

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Abbreviations

AAAA	Addis Ababa Action Agenda
ADB	Asia Development Bank
AfiF	Africa Investment Facility
AgriFi	Agriculture Financing Initiative
AIF	Asia Investment Facility
BF	Blended Finance
BIO	Belgian Investment Company for Developing countries
BMI	Belgian Corporation for International Investment
BTC/CTB	the former Belgian Development Agency (until 31/12/2017)
CGIAR	Consultative group on international agricultural research
CIF	Caribbean Investment Facility
CREDENDO	Belgian based European credit insurance group
CSA	corporate social accountability
CSR	corporate social responsibility
DAC	Development Assistance Committee
DEVCO	The EC's Directorate-General for International Cooperation and Development
DFI	Development finance institution
DFID	Department for International Development (United Kingdom)

DG NEAR	Directorate-General for Neighbourhood and Enlargement Negotiations
DGD	Directorate General Development Cooperation
DGGF	Dutch Good Growth Fund
DIBs	Development Impact Bonds
EBRD	European Bank for Reconstruction and Development
EC	European Commission
EDF	European Development Fund
EDFI	Association of European Development Finance Institutions
EDFIMC	EDFI Management Company
EEIP	European External Investment Plan
EFSD	European Fund for Sustainable Development
EIB	European Investment Bank
ElectriFi	Electrification Financing Initiative
ENABEL	the Belgian Development Agency (since 1/1/2018)
ENI	European Neighbourhood Instrument
EU	European Union
EU-AITF	EU-Africa Infrastructure Trust Fund
EU-BEC	EU Platform for Blending and External Cooperation
EU-ITF	EU-Africa Infrastructure Trust Fund
EUR	Euro
FAO	Food and Agriculture Organization
FDI	Foreign Direct Investment
FINEXPO	the Belgian inter-ministerial advisory committee for support to exports
FMO	Netherlands Development Finance Company
FPSF	Federal Public Service of Finance
FPSFA	Federal Public Service of Foreign Affairs
HIPC	heavily indebted poor countries
IBRD	International Bank for Reconstruction and Development
ICRC	International Committee of the Red Cross
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IFC	International Finance Corporation
IFP	Investment Facility for the Pacific
IFRS	International Financial Reporting Standards
ILO	International Labour Organisation
IMF	International Monetary Fund
IOB	Instituut voor Ontwikkelingsbeleid en -Beheer/ Institute of Development Policy
IPA	Instrument for Pre-Accession Assistance
LAIF	Latin America Investment Facility
LDC	Least developed country
LMIC	Lower middle-income country
M	Million
M&E	Monitoring and evaluation
MDB	Multilateral development bank
MDGs	Millennium Development Goals
MDR	Multilateral Debt Relief Initiative
MFI	Microfinance institution
MSMEs	Micro, Small and Medium Enterprises
NGAs	non-governmental actors
NGO	Non-governmental organisation
OD	Organisational Development
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
OPIC	Overseas Private Investment Corporation
PbF	Performance-based Financing
PbR	Payment by Results

PPP	Public-private partnership
PS4D	private sector for development
RbF	Result-based Financing
SDGs	Sustainable Development Goals
SDSN	UN Sustainable Development Solutions Network
SME	Small and medium-sized enterprise
SPV	Special purpose vehicle
SSA	Sub-Saharan Africa
TCX	The Currency Exchange Fund
ToC	Theory of Change
TOSSD	Total official support for sustainable development
USAID	United States Agency for International Development
USD	United States dollar
UWE	Union Wallonne des Entreprises
VOB-FEB	Federation of Enterprises in Belgium
VOKA	Vlaams netwerk van ondernemingen
WBG	World Bank Group
WEF	World Economic Forum

Executive Summary

Since the third international conference on Financing for Development in Addis Ababa (July 2015) and the proclamation of the Sustainable Development Goals (SDGs, September 2015), the aid industry has a new mantra: "From Billions to Trillions"[1], and Blended Finance is declared to be the outspoken path to get there.

The catalytic use of Belgian Development cooperation towards the private sector and an SDG engagement of the private sector requires a comprehensive Blended Finance policy. This paper wants to contribute to such a policy, by clarifying concepts, giving some necessary theoretic background, giving an overview of the state of global Blended Finance and situate Blended Finance in the Belgian and European context.

In the first part of this paper we explain what Blended Finance is, what it entails and if it doesn't take us in the wrong direction.

Blended finance is based on subsidies from development finance to the private (commercial) sector. The "From Billions to Trillions" guiding theme, has obscured the fact that subsidising markets can only be done if there are externalities or equity imperatives to do so. Therefore, it is at the demand side of the investable projects that one finds the rationale for subsidising the private sector.

Using a public grant together with public concessional debt to mobilise private finance, is often not more than the illusion of creating additional finance, while in essence it only makes already available finance cheaper. This is a case of subsidising the supply side, rather than looking at the demand side of investable projects.

As Carter puts it: "The right objective of blended finance is to subsidise investments where there is a case for doing so based on public economics. Turning a small number into a large number is the wrong objective."[2]

Even so, until now, statistics do not show that Blended Finance will fulfil its promise of mobilising the necessary trillions to achieve SDGs by 2030. Moreover, some SDGs fall clearly outside the Blended Finance scope and their achievement depends much more on (international) regulation and institutional development than on finance [e.g. 'Life below water' (SDG 14), 'Life of land' (SDG 15) and Peace & Justice (SDG 16)].

This doesn't mean that Blended Finance cannot play an important role in development. There is growing evidence that Blended Finance accelerates the development of the private sector and that it is key in pre-financing investments for which it is impossible to get enough funding from annual public budgets.

There are several ways to crowd-in commercial finance in Blended Financed investments. All of them try to improve the risk/return ratio. This can be done by mitigating risks through subsidised insurance or guarantee schemes, by adding concessional capital in junior or first loss positions financed by development finance. Commercial investment can also be stimulated through enabling the environment and building capacity of private actors.

To ensure that optimal impacts are achieved, and additional finance is mobilised without disturbing markets, "Principles" for Blended Finance have been developed and agreed upon by DAC/OECD These principles provide a framework for policy standards and guidance for the member-state governments to base decisions on scaling-up and mainstreaming blended finance.

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[1] Actually these "Trillions" were already mentioned in the UCTAD "World Investment Report 2014". In this report (p. 140) UNCTAD estimated that total investment needs in developing countries alone could be about $3.9 trillion per year. With the 2014 investment levels at 1.4 trillion per year this meant a gap of some $2.5 trillion, per year!

[2] Carter, P. (2015), Why Subsidise the Private Sector? What Donors are Trying to Achieve, and What Success Looks Like, Overseas Development Institute, London, www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9948.pdf ,.p.24.

Seen the use of Development Finance in Blended Finance set-ups, tracking, monitoring and evaluating is of utmost importance. It is probably only when the DAC's TOSSD information system will be functional, that a more global view on Blended Finance will be possible. A monitoring and evaluation framework for each individual Blended Financed investment is not only needed for accounting for the Development Finance that was used, but also to learn to what extent the Blended Finance set-up was efficient and effective in achieving targeted SDG.

While the conclusions of this paper suggest scepticism regarding the claim that Blended Finance will bring finance for development from "billions to trillions", it is without doubt that it is of utmost importance that development interventions should be used catalytically, where possible, as to mobilise additional finance from private sources and bring SDGs closer to their necessary funding. This catalytical role of development finance is also embedded in both the 2030 Agenda for Sustainable Development and the Addis Ababa Action Agenda. However Blended Finance is more than mere mobilisation of additional private resources, it is also about engaging the private sector in the SDG agenda and to make entrepreneurs and investors aware of their responsibility of making the development of our planet more inclusive and more sustainable.

In the second part of this paper we situate Blended Finance in the context of Belgian (Federal) Development Cooperation. Under the present Minister for Development Cooperation, Alexander De Croo, private sector development as well as private (commercial) finance mobilisation have become more prominent in Belgian Development Cooperation policy. Examples of this are the launching of a Humanitarian Impact Bond in collaboration with the International Committee of the Red Cross (ICRC), opening of the funding of BIO investments for private investors via a private co-investment fund, reform of the Belgian Development Agency (ENABEL) and the launching of a Belgian SDG Charter including representatives of the Belgian private sector.

The complex political structure of Belgium as a Federal State with three Regions and three Communities has made that powers regarding the private sector are spread over different levels. A coordinated policy to engage the private sector in SDGs is difficult as for instance most of the subsidies to the private sector are a regionalised matter. Nevertheless, the Belgian Development Cooperation can appeal to several existing institutions and programmes to develop and scale up Blended Finance. All of these however need reorientation and/or strengthening. The Directorate General Development Cooperation (DGD) is the obvious actor for developing policy guidelines and designing strategy to integrate Blended Finance in Belgian Development Cooperation. It is in this framework that DGD has asked BeFinD to give substantiated input on the subject.[3] DGD also actively participated in the DAC debates on the formulation of OECD Guidelines for Blended Finance that were approved by the end of 2017. The OECD/DAC Guidelines for Blended Finance are an obvious source of inspiration for developing a Belgian policy and strategy for Blended Finance, though also other concerns must be taken into account, such as not creating an unsustainable debt level and focusing more on the most poor and vulnerable populations.

A Blended Finance policy will also need to consider different legislation that exist on national and international (European) level that regulates finance in general and blending of different sources of funding in particular.

Some steps have already been taken to make Belgian Development Cooperation more catalytic. This is noticeable in recent legal reform and in changes of the respective management contracts of ENABEL and BIO. These are the two main implementing actors in Belgian Development Cooperation and although both already interact with the local private sector (mainly BIO), interacting with the Belgian private sector in a systematic way is recent or new to them.

The transformation of BTC into ENABEL was also done in view of making the private sector and its blended funding more prominent in ENABEL's activities. However, having experience mainly as the

[3] BeFind as such was not a member of the Blended Finance Working Group that brought together the main public actors in Blended Finance, in this sense this paper gives a view from the outside.

implementor of Belgian governmental development programmes, ENABEL will need organisational changes and capacity strengthening as to be able to operate programmes that will demand for interaction with local and Belgian commercial partners, using financial instruments such as debt, equity and guarantees.

BIO on the other hand has collaboration with the private sector in its DNA, nevertheless its experience relates in the first place to the local private sector. In 2018 BIO has initiated the set-up of a private investment fund, the "SDG Frontier Fund", that will be financed for 75% by private funds, along a 25% BIO participation. The SDG Frontier Fund will co-invest alongside BIO, mainly in local SME investment funds.

Other actors that are not part of the Belgian institutional framework for development cooperation, but that due to the nature of their mandate could or even should be involved in a Belgian Blended Finance strategy are CREDENDO and FINEXPO.

Although the Minister of Development Cooperation is represented in its board of directors, CREDENDO is not involved in any of the programmes of the Belgian Development Cooperation. However, there is certainly potential to integrate CREDENDO in a Belgian Blended Finance policy. Belgian impact investors, such as Alterfin and Incofin, are looking for ways to mitigate certain risks for instance in fragile states. CREDENDO is not offering any services in these "level 7" states. It is clear that in this case collaboration between the Belgian Development Cooperation and CREDENDO would be meaningful and an ODA financed risk mitigation could have an important impact on SDG oriented investments.

FINEXPO has been developed as an export promoting tool and it has no explicit SDG orientation, although a large part of its funding comes from the budget for development cooperation. For 2018 this budget amounts to EUR 73,6 million. FINEXPO has six concessional financial instruments, ranging from the untied state loans to grants for technical assistance. A limiting factor to use FINEXPO as a Blended Finance instrument is the fact that for most FINEXPO instruments the ultimate local beneficiary/client must be a government institution or the like. Together with its complicated governance and its lack of SDG oriented policy, this makes that FINEXPO in its present form is difficult to use in an SDG inspired Blended Finance programme. The Dutch Good Growth Fund (DGGF) that has similar supporting instruments might be a good source of inspiration for a reform of the FINEXPO programme in that sense.

Key in an institutional framework for Blended Finance is how the relation with the private (commercial) sector takes form. Therefore, a coordinated policy to engage the private sector in SDGs is needed, which is not an easy job taking into account the complex political structure of Belgium. Some initiatives such as the "SDG Charter" and "SDG Voices" have already been taken, though more can and needs to be done for instance on regional, but also and sectoral level. The recent initiative of the "Belgian Sustainable Cocoa Program" might be a good example.

Sensitising the private sector for SDGs and mapping needs of the private sector to have them invest in line with SDGs, should be followed by appropriate programmes to respond to those needs. Blended Finance facilities should in the first place have their rationale in the local context (in the developing countries), but then also should respond to the need and interest of private partners in Belgium.

There are existing institutions (mentioned above), that can develop, scaleup and manage Blended Finance facilities and some groundwork to make this possible from a legal point of view has been done (ENABEL, BIO) or is being prepared (the Royal Decree on Innovative Financing). What is needed further is (1) a clear Blended Finance policy framework based on the OECD Blended Finance Principles (2) strengthening of the institutions (mainly DGD and ENABEL) to develop, monitor and execute Blended Finance programmes (3) sensitisation of the Belgian private sector for the SDGs (4) strengthening and bringing together Blended Finance instruments that already exist but lack the development focus and (5) development of levers to attract private investment (risk mitigation tools, technical assistance programmes, enabling environment programmes).

Some of these levers mentioned in point 5 exist in CREDENDO or FINEXPO but have until now not been used in an SDG framework. An ODA supported facility within CREDENDO could be created for those investments that are SDG inspired. As for FINEXPO, the programme needs an SDG "overhaul". Its ODA financed instruments should be conditioned based on clear SDG contribution. This would also make it possible to open facilities for having the local private sector as ultimate beneficiary.

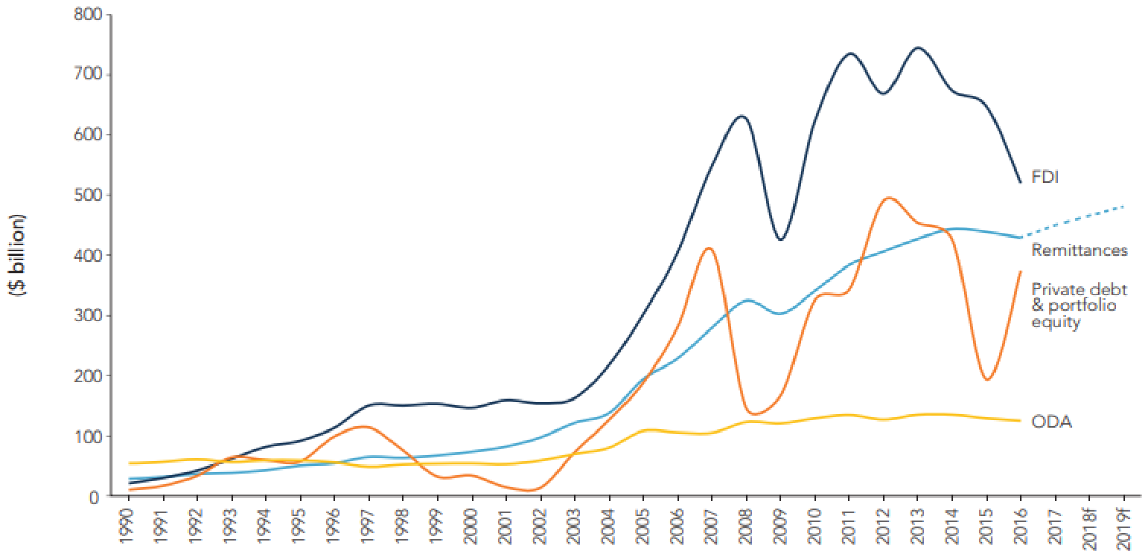
Finally, a Belgian Blended Finance strategy should include the use of European Blended Finance facilities. Although these European facilities such as the European External Investment Plan do not create important additional commercial funding, they could strengthen Blended Finance strategies of both ENABEL and BIO. AgriFi and ElectriFi, are two thematic European Blended Finance programmes that are open to the private sector. A Belgian Blended Finance strategy could include assistance for those Belgian private sector actors that seek access to these funds.

1 The General Framework of Financing for Development

"We the heads of State and Government, gathered in Monterrey, Mexico, on 21 and 22 March 2002, have resolved to address the challenges of financing for development around the world, particularly in developing countries. Our goal is to eradicate poverty, achieve sustained economic growth and promote sustainable development as we advance to a fully inclusive and equitable global economic system."

This is the opening paragraph of the Monterrey Consensus (United Nations, 2002). The Consensus recognised that all sources of financing, public and private, domestic and international were needed to reach the development goals. While the Monterrey consensus still emphasised the central importance of development cooperation, soon it became clear that this source of finance would not be sufficient to produce the Millennium Development Goals (MDGs) and certainly not sufficient to reach the even more ambitious Sustainable Development Goals (SDGs). Moreover it became clear that, over the years, Official Development Assistance (ODA) lost relative significance in comparison to other much more important international financial flows such as Foreign Direct Investment (FDI), Remittances and Portfolio Debt and Equity flows as can be seen in the graph below.

Figure 1-1 International financial flows to developing countries



Source: "Migration and Remittances, Recent Developments and Outlook". Migration and Development Brief 28, World Bank Group, October 2017.

However, domestic public and private resources are and should remain the core of any policy for financing development in a sustainable way. The combined international financial flows to developing countries as depicted in the graph above, do not reach more than USD 1.7 trillion, while domestic capital formation in those countries are a multiple of that figure and reach not less than USD 9 trillion[4]. While more effective and efficient fiscal policies can grow and sustain public supported development, this can only be done if economic growth provides a broader base to mobilise resources for public finance.

Nevertheless, neither the growth of domestic fiscal resources, nor the envisaged growth of international financial flows, including ODA, would suffice to fill the funding gap facing the SDGs. So, the idea grew that existing flows need to be leveraged to reach exponential growth of funding. Blending Finance became a key strategy in development finance and the chosen path to go "From Billions to Trillions".

[4] Average Gross Capital Formation in GDP in developing countries is 31%. Their combined GDP reaches USD 29 trillion. Data from World Bank: https://data.worldbank.org/indicator/NY.GDP.MKTP.CD and https://data.worldbank.org/indicator/NE.GDI.TOTL.ZS?view=chart .

2 What is Blended Finance?

According the DAC/OECD Blended Finance (BF) can be understood as "the strategic use of development finance for the mobilisation of additional finance towards the SDGs in developing countries"[5]

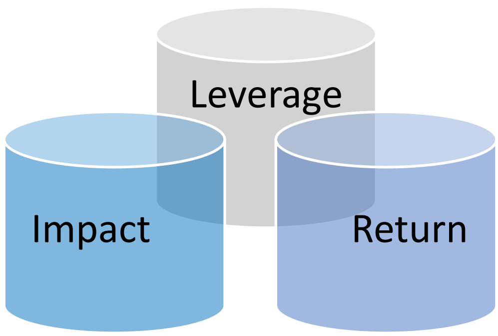
BF in Development Cooperation is thus about blending financial resources of different origin (public and private) and with different rationales (the development rationale and the commercial one).

The key point is the mobilisation of commercial, 'non-development' finance, that normally would not be available for financing SDG-aligned investments.[6] This additionality is a key principle, to organise, monitor and evaluate blended finance. The lever to mobilise these additional commercial funds can be of public and/or of philanthropic origin, but in view of the purpose of this paper we mainly consider the public origin.

This also means that mixing public finance with public finance, is not really considered to be Blended Finance as it does not lever additional financing for development and might better be called 'Pooled Finance'.[7] An exception are the public-public partnerships with Development Finance Institutions (DFI's), that create some additionality as these DFI's can in their turn mobilise private (commercial and/or impact) funding. It is in that sense that some of the European BF mechanisms should be understood. The principle of these mechanisms is to combine EU grants with loans or equity from public and private financiers.[8]

BF is built around three key pillars which align the interests of both private commercial capital and development funders:

Figure 2-1 The interests of development and commercial finance aligned by three pillars



- Leverage: development funder resources that attract private/commercial capital into development finance;
- Impact: products, services, transactions that provide social, environmental and economic benefit for their communities (SDG aligned impact);
- Returns: improved risk/return ratios that make projects attractive for private/commercial capital.

A point of discussion is the question if the public part of the BF should be concessional in nature or not, whereby "concessional finance" is considered to be provided on terms that are clearly more favourable than those explicitly available in the market.[9] The 2nd meeting of the Senior Advisory Group on Developing Blended Finance Principles (within the DAC/OECD) left out the concessional nature as a necessary aspect of BF. However, as the aim is to attract additional private commercial finance, this probably can only be done if the return/risk ratio can be made more attractive by a concessional element. This concessional

[5] Definition taken from the final draft of the OECD DAC Blended Finance Principles. DCD/DAC (2017)28, p.2.
[6] DCD/DAC (2017)9, p.6.
[7] "Private-Finance Blending for Development". Oxfam Briefing Paper, February 2017, p. 5.
[8] https://ec.europa.eu/europeaid/policies/innovative-financial-instruments-blending_en
[9] "DFI Guidance for Using Investment Concessional Finance in Private Sector Operations". Private Sector Roundtable, April 15th, 2013, p. 3.

element can take different forms like technical assistance, concessional interest rates, de-risking instruments, supporting enabling environments, etc.[10]

3 The Drivers of Blended Finance

The main driver for BF is the need for significant additional resources to reach the ambitious development goals set in the context of the SDGs, the Paris Agreement on climate change and the Addis Ababa Action Agenda (AAAA)[11] (see Annex 1). This need for additional resources goes beyond the possibility of potential growth of existing ODA budgets, hence the need to mobilise private resources. In particular the AAAA mentioned BF as an important way of mobilising additional resources. However, BF is more than the mere mobilisation of additional private resources, it also engages the private sector in the SDG agenda (see for instance the Belgian SDG Charter[12]).

The need for mobilising private resources coincides with the 'private turn' in Development Cooperation, which is a second driver of BF. Not only has the development of the private sector been a growing topic in Development Cooperation, but also has the inclusion of the private sector for development (PS4D) gained attention in Development Cooperation policy. There are different push and pull factors for the growing importance of the private sector in the development context[13], but it is certainly a trend that will stay and probably even grow.

A third driver, be it maybe of lesser importance, is the growing interest from the side of the private sector for emerging markets and for bottom of the pyramid markets. This growing interest stems from the search for new business opportunities, but also from new attitudes towards entrepreneurship visible in the increasing attention for social entrepreneurship, inclusive business, corporate social responsibility (CSR) and accountability (CSA), and hybrid business models (Vaes & Huyse, 2015). This growing interest in sustainable business is also seen in the growth of impact investment funds[14], that specifically target investments with a positive impact on a more sustainable society.

4 Blended Finance: Magnitude, Geographical and Sectoral Scope and SDGs

4.1 Magnitude

BF, or the use of development funds to leverage commercial investments in development, is said to have the potential to provide part, if not all, of the solution to the funding gap facing the SDGs. This is no small

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[10] The related question on how this element of concessionality in BF is then to be amply represented in aid accounting metrics such as ODA, or the newly development broader metric of TOSSD (Total Official Support for Sustainable Development) falls beyond the scope of this paper. See e.g. Robrecht Renard and Danny Cassimon, "On the Pitfalls of Measuring Aid", WIDER Discussion Paper No. 2001/69, Helsinki, WIDER, 2001; Danny Cassimon, Robrecht Renard and Karel Verbeke, "How to account for concessional loans in aid statistics", IOB Analysis and Policy Brief No.9, Institute of Development Policy (IOB), 2014; Kris Bachus and Emilie Bécault, "Public Climate Finance: the challenge of reporting equity, BEFIND Working Paper No.17, February 2017; OECD DAC, "TOSSD: A New Statistical Measure for the SDG Era", Paris, OECD DAC, May 2017.

[11] See for instance the document submitted for the DAC meeting on March 9, 2017: "Blended Finance for Sustainable Development: moving the agenda forward", DCD/DAC (2017)9, unclassified.

[12] https://theshift.be/uploads/media/57f3a8cfcfffe/Charter%20SDG4D%20-%20DEFINITIEF.pdf

[13] See for instance: Sarah Vaes & Huib Huyse: "Private Sector in Development Cooperation". Research Paper, 2015 HIVA-KU Leuven.

[14] Impact investments are investments made into companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return (See for instance https://thegiin.org/)

undertaking since it is estimated that there is an annual 2.5 trillion finance gap until the 2030 deadline.[15] No wonder the appetite is strong to look beyond traditional development co-operation and see how commercial finance can be better mobilised to meet the SDGs. But when it comes to BF, some fundamental issues need to be considered before scaling up ODA investments in this area.

The SDGs are very diverse. They include no less than 17 goals, 169 targets, and 232 indicators[16], in contrast to the Millennium Development Goals (MDGs) that focused on eight goals, 18 targets, and 48 indicators. Therefore, the SDGs have been called by some "Senseless, Dreamy, Garbled"[17]. The diversity of the SDGs makes it impossible to generalise about theories of change and their underlying financial models. Saying that blended finance and thus commercial finance can contribute to all 17 SDGs might be an overconfident statement. Many SDGs are in the first place impacted by policies in the political and institutional domain.

While interest in BF is increasing, the evidence base on Blended Finance is still limited. One of the most comprehensive studies is the evaluation of blending as an EU aid delivery mechanism. This study gives insight in the strategic relevance and the value added of blended finance mechanisms.[18] There is however no single database that gives an overview of all BF transactions, as the DAC provides for ODA. In future a new measure called Total Official Support for Sustainable Development (TOSSD) that is under development by the OECD, should capture development flows beyond ODA, like blended finance.

Presently, there are mainly two organisations (of completely different nature) that collect data on Blended Finance transactions: Convergence and DAC/OECD. Launched in January 2016, Convergence is the global network for blended finance, that generates blended finance data, intelligence, and deal flow to increase private sector investment in developing countries.[19]

In 2017 the OECD Development Assistance Committee conducted a survey with its members countries, that demonstrated that the majority are participating in some blending.[20] The survey considered Blended Finance facilities and funds. There is no blending as such within facilities; rather facilities provide finance that supports blending further downstream at the fund or project level. In contrast, funds are pools of private or public-private capital in which blending also can occur at the capital structure level.[21] The OECD survey carried out in 2017, builds on the approach and dataset developed by the Association of European Development Finance Institutions (EDFI) in a 2015 survey. The new OECD survey distinguishes between funds and facilities, extends the scope to all Development Assistance Committee (DAC) members, and includes new types of funds such as private equity funds. The 2015 EDFI survey considered 140 funds and facilities in total. The 2017 OECD survey supplemented the EDFI sample and considered 167 facilities and 189 funds, or a total of 356 entities.[22]

The 2018 OECD report mentions that between 2012 and 2015 Blended Finance has generated over USD 81 billion for development goals. The Convergence Blended Finance dataset that is used by their September 2018 report represents in total USD 100 billion and covers the period 2005-2017.[23] As these figures are based on different datasets, they are not comparable as such, but they give a good idea of the level of flows Blended Finance has been mobilising.

[15] OECD (2018), Making Blended Finance Work for the Sustainable Development Goals, OECD Publishing, Paris P.15 http://dx.doi.org/10.1787/9789264288768-en

[16] https://unstats.un.org/sdgs/indicators/indicators-list/

[17] Easterly W. The SDGs should stand for senseless, dreamy, garbled. Foreign Policy (Washington, DC), Sept 28, 2015. http://foreignpolicy.com/2015/09/28/the-sdgs-are-utopian-and-worthless-mdgsdevelopment-rise-of-the-rest

[18] European Commission. "Evaluation of Blending". Final Report. Volume I – Main Report. December 2016.

[19] Convergence is an independent entity, registered as a non-profit corporation in Ontario, Canada. Convergence's funders include the Government of Canada, Citi Foundation, and Ford Foundation. Conceived under the World Economic Forum and OECD-DAC's Re-Designing Development Finance initiative, Convergence was designed and launched by the Global Development Incubator and Dalberg Global Development Advisors: https://convergence.finance/

[20] The 2017 OECD survey builds on the approach and dataset developed by EDFI in a previous survey commissioned in 2015. The new OECD survey distinguishes between funds and facilities, extends the scope to all Development Assistance Committee (DAC) members, and includes new types of funds such as private equity funds.

[21] OECD (2018), o.c., p.97.

[22] OECD (2018), o.c., p.98.

[23] CONVERGENCE. "The State of Blended Finance 2018". Report, September 2018, p.12.

Although these statistical data are not complete, so far, the evidence does not demonstrate that Blended Finance can take us from billions to trillions. In the funds targeted by the 2017 OECD survey of funds and facilities, the share of commercial investors is still quite limited when compared with development investors. According to the 2018 OECD report, until now BF has been mainly combining different sources of public development finance and barely mobilising 1 USD of commercial finance for each 8 USD invested by development finance.[24] The same study suggests that If ever we want to come closer to the trillions, the proportion should be reversed.

4.2 Geographical Distribution

Most of the geographically earmarked Blended Finance transactions go to Sub-Saharan Africa (27%, DAC; 42%, Convergence), though the deal size of the African BF transactions is relatively 'small' (USD 125 M in average) , which makes the SSA Blended Finance portion of the flows much smaller: 16% of total capital mobilised according Convergence.[25]

The assumption made by critics that Blended Finance would be mainly an instrument for middle income countries, cannot be confirmed. At least not by the Convergence database which shows that 26% of the blended flows goes to Low-Income countries and 48% to Lower-Middle Income countries[26]

4.3 Sectoral Distribution and SDGs

Blended Finance cannot address all the SDGs. Blended Finance can only be deployed for activities that can produce asset value and cash flows that give investors an acceptable return, that is at least comparable to alternative investment opportunities. The SDSN Working Paper by Guido Schmidt-Traub[27] estimates the investment needs to achieve the SDGs and gives also some estimates on the potential contribution of commercial finance within Blended Finance set-ups. For all SDGs combined up to 45% of the needed investments could potentially be done through private (commercial) finance. Energy, different infrastructure and agriculture and food are the sectors with the greatest potential for investment through commercial finance.[28]

Empirical data from previous Blended Finance transactions show a slightly different picture. The table below displays the sectoral distribution of the Blended Finance transactions in numbers and amounts, based on a previous OECD dataset and the Convergence dataset of the 2017 report. Both datasets show the importance of Financial Services and Energy & Climate for the number of BF deals and the BF flows. In the more recent Convergence dataset, the Health sector seems much more present in BF while Infrastructure is less. The difference regarding the Health sector can be explained by the more recent data of Convergence. The fact that Convergence reports less BF transactions in the infrastructure sector, can only be explained by not having included certain Infrastructure funds.

[24] OECD (2018), o.c., p.17.
[25] See OECD (2018), o.c., p.102 and CONVERGENCE (2017), o.c., p.5.
[26] CONVERGENCE (2018), o.c., p. 16.
[27] SCHMIDT-TRAUB G. "Investment Needs to Achieve the Sustainable Development Goals". SDSN Working Paper. November 2015. Retrieved from: http://unsdsn.org/wp-content/uploads/2015/09/151112-SDG-Financing-Needs.pdf
[28] SCHMIDT-TRAUB G., o.c., p.102.

Table 4-1 Sectoral data comparison between OECD and Convergence datasets

	OECD ('14)				Convergence			
	#		*usd (M)*		#		*usd (M)*	
Financial Services	41	29,29%	7.258,7	27,36%	70	25,74%	7.508,8	14,65%
Energy and Climate	30	21,43%	7.387,3	27,85%	62	22,79%	15.375,9	30,01%
Healthcare	5	3,57%	413,2	1,56%	38	13,97%	15.181,9	29,63%
Education	1	0,71%	0,7	0,00%	21	7,72%	283,5	0,55%
Agriculture	15	10,71%	1.361,7	5,13%	34	12,50%	1.511,1	2,95%
Infrastructure	14	10,00%	3.605,3	13,59%	12	4,41%	1.708,5	3,33%
Housing/Real Estate	0	0,00%	0,0	0,00%	11	4,04%	337,5	0,66%
General	34	24,29%	6.501,31	24,51%	24	8,82%	9.336,0	18,22%

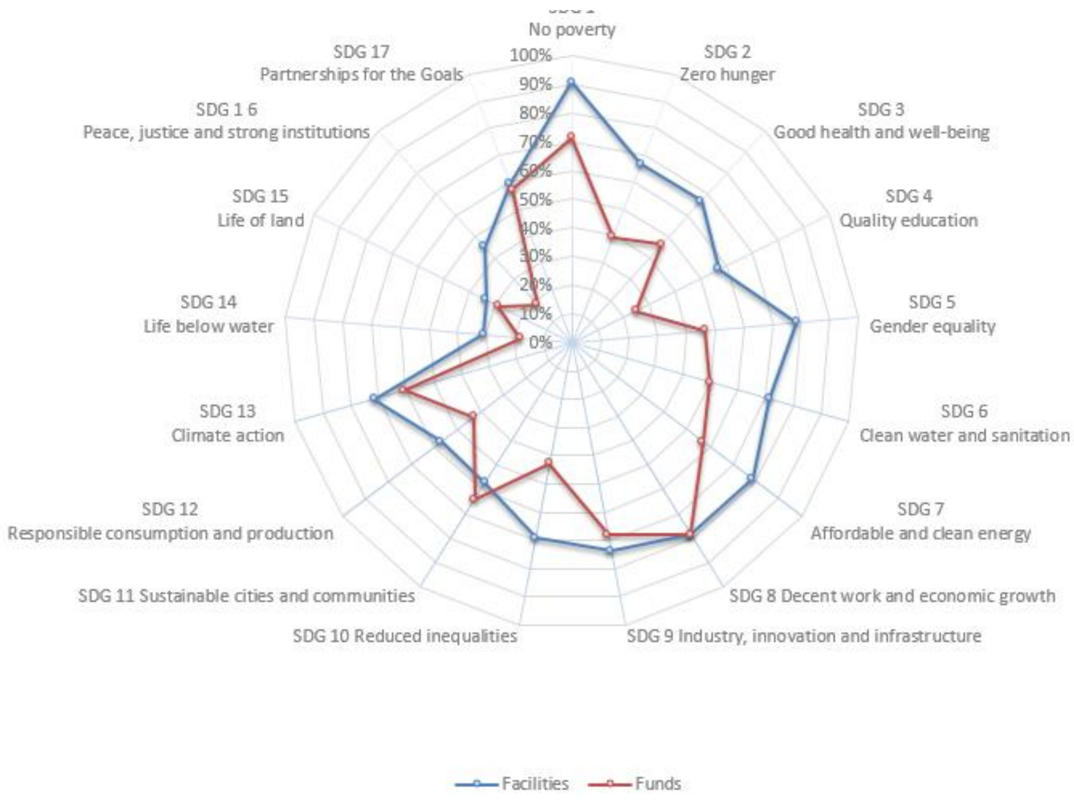
Source: CONVERGENCE. "The State of Blended Finance". Working Paper, July 2017, p.25.

The OECD (2018) report gives information on the distribution of the BF facilities and funds over the different SDGs. As is shown in the graph below taken from the OECD study "Making Blended Finance Work for the Sustainable Development Goals", BF is unevenly distributed amongst SDGs. This is not surprising as not all SDG domains are evenly suited for Blended Finance. Certainly those SDGs that are closer to the domain of Public Goods, such as 'Life below water' (SDG 14), 'Life of land' (SDG 15) and Peace & Justice (SDG 16) are not suitable for Blended Finance and are more linked to appropriate policies in the political and institutional domain.

The graph below only gives information on the distribution of the targets of the surveyed blended finance funds and facilities over the different SDGs. However, there is still little information available on the actual performance of the different BF transactions regarding their contribution to the SDGs. This is closely linked to the lack of monitoring and evaluation practice and communication of the different BF transactions. The 2018 OECD report mentions that Evaluation practice vary greatly depending on the vehicle, with 81% of the surveyed blended finance facilities reported having
undertaken at least one evaluation compared to 56% of the funds only. Less than half of final evaluation reports from surveyed facilities and funds were made public. [29]

[29] OECD (2018), o.c., p.138.

Figure 4-1 How blended finance funds and facilities target the SDGs



Source: OECD 2017 Survey on blended finance funds and facilities; number of respondents to question: facilities 42 (out of 43); funds 28 (out of 31). http://dx.doi.org/10.1787/888933648214 [30]

As far as Blended Finance is using concessional development funding in order to catalyse commercial investment, it is actually another term for subsidising the private (commercial) sector, be it in the context of development finance. Therefore, BF should also be investigated from this perspective. This is the subject of the next chapter.

5 The Case for Subsidising the Private Sector

As is mentioned above, so far BF has not met the expectation that it would mobilise trillions of commercial funds. The Director General of DEVCO of the European Commission claimed that the European BF programme was reaching a leverage of 20. However if all development finance is taken into account, meaning not only development grants from the EU but also development debt of the DFIs, who have privileged access to the EU BF facilities, the leverage was not more than 1.[31] This confirms the BF scepticism expressed by Paddy Carter and others to use subsidies in view of the objective of going from billions to trillions.[32]

[30] OECD (2018), p.27.

[31] € 2billion of grants and €19 billion of development debt were needed to attract €21 billion of commercial finance. https://www.euractiv.com/section/development-policy/news/commission-says-blending-of-funds-produces-huge-results/

[32] CARTER P. Why subsidise the private sector? What donors are trying to achieve, and what success looks like. ODI, London, November 2015. https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9948.pdf

Moreover, using a (small) public grant together with public concessional debt to mobilise private debt finance, is often not more than the illusion of creating additional finance, while in essence it only makes already available finance cheaper. This is a case of subsidising the supply side, rather than looking at the demand side of investable projects. It is at the demand side of the investable projects that one finds the rationale for subsidising the private sector.

The theory of welfare economics gives at least two grounds on the basis of which subsidies to the private sector can be justified efficiency and equity. Different kind of market failures might make markets not operate efficiently or even fail to exist. A failing market will allocate and/or produce in an inefficient way, meaning that resources are not used in an optimal way to satisfy the needs of a maximum number of people.

Agriculture is a classic example of an industry where such market failures exist, certainly in a developing context. One market failure associated with agriculture is that prices do not reflect the level of environmental impact. High input intensive agriculture for instance might lead to increased discharge of a variety of pollutants like nutrients, pesticides, sediment, and greenhouse gases, that are not reflected in the prices of the produce. In such a situation the market does not induce investment in more environmentally friendly agriculture that does not produce these external effects.

In a development context market failure are often associated with non-competitive markets (e.g. monopolies, oligopsonies, …), incomplete or broken value chains and information asymmetries. This is also certainly true for small-holder agriculture. Between small-holder producers and urban consumers often different links in the value chain are missing, leading to inexistent markets. Often investments in the missing links are not attractive due the high transactions costs: producers are scattered, and collection centres might not exist. But also, climatic risk and associated volatility of prices make it difficult to reach an acceptable risk/return ratio.

Agricultural markets are also often dominated by a concentration on the buyers' side, leading to oligopsonies such as is the case in the cocoa sector, where few multinationals dominate the market. In such a case the price will not reflect the marginal cost of the producer, including a reasonable remuneration of her/his work. In some countries this has led to price regulation, as is for instance the case for cocoa in Ivory Coast. Other ways of creating "fair" markets is the introduction of minimum prices linked to a certified benefit for the small producer.

In a context of failing markets, such as in small-holder agriculture, subsidies can improve the two parameters on the basis of which private investors will take a decision to invest: return and risk. The challenge is to calibrate the subsidy so that it delivers the minimum uplift needed to induce investment without producing excess profits (economic rents) for investors[33] and without worsening the externalities again that were at the origin of the subsidies.

The second ground for subsidies is equity and associated poverty (SDG 1, 2 and 10, ANNEX 2). Even If a market works efficiently and there is a Pareto optimal allocation of resources, the underlying local or international distribution of wealth (and the associated poverty) might not be the desired one. In this case subsidies (or taxes[34]) might shift the Pareto frontier to a more desirable situation of wealth distribution. Subsidies (or taxes) will lead investments towards sectors or social groups that need support.

Subsidies for rectifying market failures, managing externalities, changing distribution of wealth and alleviating poverty can take different forms depending on the causes that inhibit the producers or the consumers to act according a desired market outcome. In chapter 6 we discuss the different forms that subsidies can take.

As market failures are often time bound, also the subsidies to address these failures should be restricted in time. If not, they might create undesired market distortion. Subsidised debt or equity finance might for

[33] CARTER P (2015), p.3.
[34] The analysis of taxes and subsidies is symmetric. In development finance taxes are an important topic as they are part of domestic resource mobilisation. In the context of Blended Finance, we focus on subsidies.

instance crowd out other investors that are willing to invest after the market failures have been addressed. In such a case the subsidised investment is in conflict with the required additionality of Blended Finance.

In case concessional finance is motivated by distribution or poverty considerations, rather than efficiency issues related to conventional externalities, the correct targeting and conditioning of the subsidies is essential.[35]

Markets work best when goods possess certain characteristics. One is "excludability," where a producer can prevent someone who has not paid for the good from obtaining it. Another is that the good is "rival," where a buyer's purchase will not benefit any other individual. For instance, a farmer can obtain a tractor only by purchasing it from a dealer. And, once he obtains it, he alone enjoys the benefits. Goods with these characteristics are known as private goods. Markets evolve naturally to provide private goods.

Public goods lack one or both characteristics. With a public good, a provider cannot exclude someone from obtaining a good even if he or she has not paid a price. For example, a farmer contemplating the sale of improved water quality by establishing vegetative buffers on his or her farm cannot exclude downstream users from benefiting; the downstream users are "free riders." In this situation, the farmer does not have an economic incentive to provide the good.[36]

Market failures and the intervention by the government through subsidies, taxes or otherwise are also closely linked to these different types of goods or services, based on characteristics of excludability and rivalness. Although these characteristics are not always inherent properties of the good itself and can be politically constructed, they will lead to the need for public intervention and even public provision rather than market provision. A classical distinction, based on characteristics of excludability and rivalness, is often made between private, public, common and club goods, as is shown in the table below.

Table 5-1 Types of Goods

	Excludable[37]	**Non-excludable**
Rival[38]	Private goods	Common goods
Non-rival	Club goods[39]	Public goods

However non-rivalry and non-excludability are independent and not always good-inherent characteristics and they can be present in varying degrees. Therefore, one must be aware that goods can have characteristics of different types of goods and do not necessarily fit in the four-box taxonomy above.[40]

Non-excludable and rivalrous goods will need some sort of intervention out of the market, in order to manage their use. This is closely linked with the externalities that were mentioned above. Wild fish stocks (SDG 14) for instance are an example of a common good that if not regulated might face depletion. Regulation might be externally organised through (inter)governmental intervention[41] or internally through

[35] BUITER H. and SCHANKERMAN M. "Blended Finance and Subsidies: An Economic Analysis of the Use of Grants and Other Subsidies in Project Finance by Multilateral Development Banks" EBRD, London, 2002, p.18.

[36] Drawn from: RIBAUDO M. et al. "The Use of Markets to Increase Private Investment in Environmental Stewardship". USDA, Economic Research Service, September 2008

[37] A good or service is called excludable if it is possible to prevent people (consumers) who have not paid for it from having access to it. By comparison, a good or service is non-excludable if non-paying consumers cannot be prevented from accessing it.

[38] A good is said to be rivalrous or rival if its consumption by one consumer prevents simultaneous consumption by other consumers, or if consumption by one party reduces utility/ability to use to another. A good is considered non-rivalrous or non-rival if, for any level of production, the cost of providing it to a marginal (additional) individual is zero (See for instance CORNES, R., T. SANDLER. 1986. The theory of externalities, public goods, and club goods. Cambridge University Press.)

[39] The discussion of these goods goes beyond the scoop of this paper, but it might be interesting to note that, while formerly this type of goods were often linked to natural monopolies and thus government intervention, more recently some of these goods are now provided under collaborative or sharing arrangements, resulting in the sharing economy.

[40] ADAMS R.D. and McCORMICK K. "The Traditional Distinction between Public and Private Goods Needs to Be Expanded, Not Abandoned" Journal of Theoretical Politics, Volume: 5 issue: 1, page(s): 109-116, January 1, 1993. http://doi.org/10.1177/0951692893005001005

[41] See for instance the European Common Fisheries Policy: https://ec.europa.eu/fisheries/cfp_en

for instance the introduction of certifications or labels that guarantee a sustainable use of the common good[42].

Public goods such as law and order (SDG 16), national security, flood protection will not be provided by the (free) market as there is no price incentive to do so. Every person can enjoy these goods without paying for them, called the free rider effect. These goods will lead to government provision rather than subsidies for market provision.

Goods like education (SDG 4) and health care (SDG 3), sometimes called "merit goods"[43], are not strictly public goods and they can be provided by the market. However, treated as private goods, market provision will necessarily exclude certain groups on the basis of pricing. Most often it is considered that individuals have equal rights to have access to these goods.[44] In a situation of unequal distribution of income (and wealth), the equal provision of these goods will necessarily require government intervention.

There is another characteristic of these "basic needs" goods, that make some sort of government action expedient, namely they induce certain positive externalities: better educated, healthier individuals are also beneficial to the society at large.

However, there is a reflection to be made on the philosophical foundation of these basic needs approach, where poverty is implicitly defined as the deprivation of (basic needs) goods. The "capability" approach, as it was largely developed by Amartya Sen[45], argues that material consumptions alone do not necessarily promise well-being lives. People must be free to choose their valued ways of life. As such the capability approach puts emphasis on values and freedom, which rephrases poverty into a broader concept of human development.[46] The practical consequence of the capability approach is that the people themselves must be involved in the choice of the "consumption bundles", which constitutes an empowerment element in a development policy. This is also an argument to involve civil society organisations in the definition of development goals often in those areas were the entitlements are not based on property but on "human rights". One can refer to certain public goods like clean air and sources of information, but also to commons like grazing grounds and irrigation systems.

Blended Finance is under the spell of the "private turn" in Development Cooperation, but the above indicates that subsidising the market is not always the appropriate way towards achieving SDGs, and often the public sector as well as civil society need to be involved and empowered (financed) to play their respective role.

The more a good is "public" the less it will be eligible for being financed and allocated through the market. The private sector can however play a role as service provider (e.g. by tender) and pre-financer (e.g. Development Impact Bonds, see chapter 11).

Different models can be set up and different instruments can be used to subsidise the private sector through Blended Finance. These models and instruments all try to address the causes of market failure and try to improve the return/risk ratio for the investors so as to attract them in an SDG oriented investment.

[42] See for instance the Maritime Stewardship Council: www.msc.org/

[43] Merit Goods were introduced as a concept by MUSGRAVE, R.A." The Theory of Public Finance: a Study in Public Economy", New York, McGraw-Hill, 1959.

[44] CARTER P., o.c., p.9-10

[45] SEN A. The Standard of Living: Concepts and Critiques. Cambridge University Press, 1987.

[46] Wong, Shing Yip, Understanding Poverty: Comparing Basic Needs Approach and Capability Approach (May 8, 2012), p.8-9. Available at SSRN: http://dx.doi.org/10.2139/ssrn.206617

6 Blended Finance Models and Instruments

Blended Finance is about attracting commercial finance in areas where it is absent or only sporadically present and where it could contribute substantially to achieving SDGs. The reason for investors to be absent, has to do with market failures in general or more specifically the return/risk ratio that is not attractive for the players in these markets. So, all Blended Finance will or need in some way or another address these market failures and/or the unattractive return/risk ratio. Therefor different models can be followed, and different instruments can be used. Each blended financed instrument will need to start from an analysis of the market failures and the problematic return/risks ratio's it wants to address.

6.1 The Types of Risks

Risk is one of the main reasons why private actors do not invest. Development finance can mitigate or help manage this risk using different instruments depending on the type of risk it wants to address. We can distinguish the following types of risks[47]:

Macro Risk

- Political (Country) risk: country risk is the degree to which political instability, unrest and violence affect doing business in a particular country and impact negatively the attractiveness of an opportunity.
- Regulatory risk: the uncertainty of regulatory volatility. For instance, uncertainty of contractual enforceability, changes in property law or changes in monetary regulation, including transfer regulation.
- Currency risk: the volatility of local currencies against hard currencies, creates uncertainty about the return expressed in hard currency.

Market risk

- A project starting activities in an undeveloped market can grasp opportunities, but at the same time it faces risks that will increase costs.
- Undeveloped markets create demand/supply risks, with unsecure sales and reduced commercial viability as a consequence.

Financial Risk

- Access to (local) finance: risk of not being able to secure enough financing
- Credit risk: the risk of default from borrowers
- Liquidity Risk: the inability to exit/sell an asset when desired

Operational Risk

- Construction/Operational Risk: Risk of project not completing as planned or the asset does not perform as planned post-completion
- Procurement risk: risk of not being able to secure long-term resource procurement

6.2 Ways to Improve the Risk/Return Ratio and to Address Market Failure

[47] See for instance: Blended Finance Taskforce. "Better Finance Better World". Consultation Paper, London, 2018, p.27.

There are different ways to address the above risks with the support of Development Finance. The objective is always to improve the risk/return ratio and to address causes of market failure, so that an investment becomes attractive also for commercial actors.

A distinction can be made between support to address the underlying risk and ways to diminish the impact of the actual risk. Supporting the enabling environment, developing markets and their organisations and developing the competences of personnel are each ways of reducing the underlying risk and increasing the rate of success. By doing so Development Finance improves the risk/return ratio. It can finance programmes to improve and stabilise the regulatory environment. It can develop markets. In the agricultural sector it can for instance support the missing links in the agricultural value chain, by supporting the organisation of farmers or developing commodity platforms and networks. It can support the upgrade of competences of human resources by financing key training programmes. In general, it can support those programmes that will tackle the causes of failing markets and improve the easiness of doing business. Then there are ways to reduce the impact that actual risk has on the return of the investment. The table below gives an overview of the different instruments and their use.

Table 6-1 Blended Finance instruments

Risk Mitigation	**Insurance**
	Guarantees
	Hedging
	Risk sharing
Concessional Funding through	**Debt**
	Equity
	Grants
	Other
Other Supporting Mechanisms	**Market development and growth**
	Increasing private actor capacity
	Enabling the environment

Risk Mitigation

Mitigate the impact of risks is an important way of improving the risk/return ratio and to attract commercial finance. Table 6-2 gives an overview of the different risks and different instruments that can mitigate their impact. The following blended financed instruments can be used:

- Insurances: these are financial instruments that cover events of risk that are beyond the control of the private actor, such as political and transaction risk, disaster and weather risk. Examples are CREDENDO and MIGA for political and transaction risk, African Risk Capacity for disaster risk.
- Loan guarantees: these are financial instruments, whereby the private lender can off-load part of the debtor's risk to a development financer or specialised insurer. In Belgium CREDENDO is offering this service.
- Local currency hedging: cross currency swaps or other currency risk covers are used to stabilise the value of a local currency vis-à-vis the foreign currency in which a private actor invests. Commercial banks can offer these services for the more mainstream currencies of emerging markets. For more volatile currencies from development countries the Currency Exchange Fund (TCX) is probably the only fund that can offer such cover. TCX is a Dutch fund specialised in covering local currency risks through swaps and forward contracts. (see ANNEX 2)

- Risk sharing: financial instruments whereby development finance providers share non-repayment risk through pari passu or first-loss clauses within structured debt or other type of funds.

Table 6-2 Instruments for risk impact mitigation

		Risks					
		political risk	transfer risk	climate disaster risk	currency risk	operational risk	financial risk
Risk Impact Mitigation	Insurance						
	Guarantees						
	Hedging						
	first loss provisions						

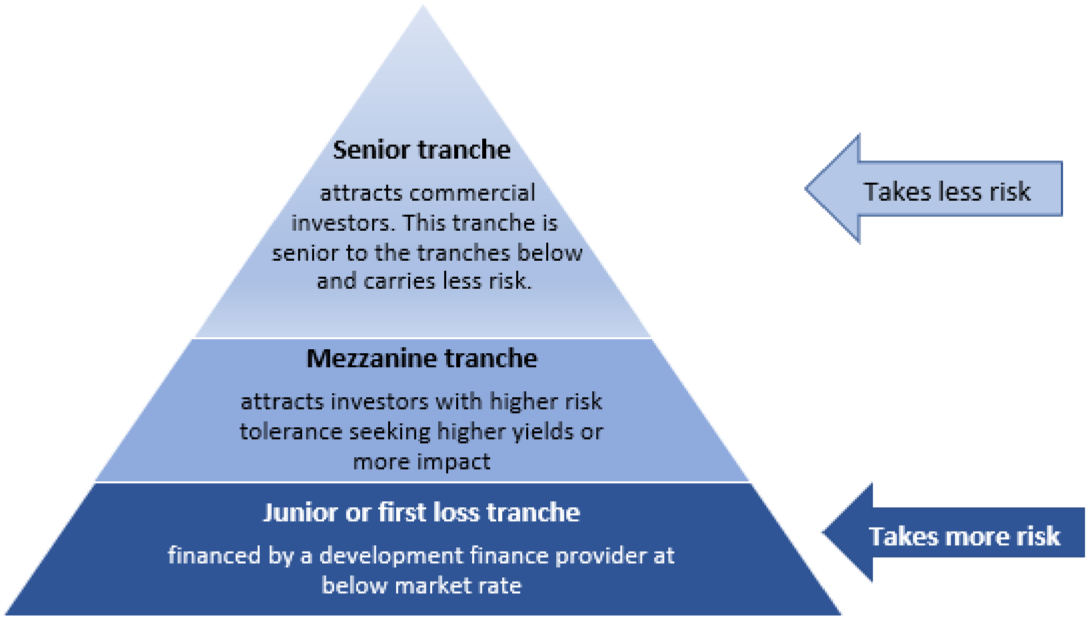
Based on: "BETTER FINANCE BETTER WORLD". Consultation Paper of the Blended Finance Taskforce. Business & Sustainable Development Commission, London, 2018, page 11. https://convergence.finance/knowledge-detail/3LKg6aU4bC0skyQ4ICykio

Increase concessional finance

Provide concessional finance is also an important way of improving the risk/return ratio and to attract commercial finance. This type of finance can take different forms.

- Debt instruments. Development actors can co-finance private investments with identified development impact, through debt finance that can be concessional based on price, tenor, subordination, repayment profile, and/or security. Typically, development actors will take a junior or mezzanine position in structured funds that pool funds from both development and commercial actors.
- Equity. Development actors can directly or indirectly through funds, provide risk bearing capital as to stimulate investments or improve debt/equity ratios in markets that have clearly development impact but are undercapitalised. The capital participation can be "junior" or subordinated to other shareholders and absorb higher risk (see figure below). A specific form is the participation in or the support to impact investment funds.

Figure 6-1 Structured vehicle mitigating risks for institutional investors



- Grants: a development actor can disburse grants in the form of operational subsidies, interest rate subsidies or periodical payments for achieved and verified development results (SDGs). An example is a "Challenge Fund" that awards public grants through competitive selection to a private project with development potential.[48] "Challenge Funds" have gained in popularity as a way of encouraging private investment and entrepreneurship in areas where social benefits are perceived to be high but so too are the investment risks.[49]
- Other instruments such as development impact bonds, frontloading of ODA[50] or certain forms of public private partnerships (PPPs), can also be mentioned, though they are more often used in development programmes regarding public services/goods.

Other supporting mechanisms

Market strengthening

Markets might be insufficiently developed to receive the required investment. Links in the value chain might be missing, small producers might lack aggregation points to link up to markets or to processing facilities, information might be lacking. Market capacity building might therefore be an effective way for the development actor to attract more private investment. Markets can be strengthened by supporting/financing market transparency (e.g. commodity platforms) or by reducing first offtake risk (e.g. advance market commitments).

Increasing private actor capacity

Also, at the level of the private actors there is a need for strengthening technical and business capacities. The capacity of investees / borrowers can be built by transferring know-how; train personnel and help

[48] Pompa C. "Understanding Challenge Funds". ODI report. October 2013

[49] Poulton C. "An Assessment of Alternative Mechanisms for Leveraging Private Sector Involvement in Poorly Functioning Value Chains". AAACP Paper Series – No. 8, August 2009.

[50] Front-loading ODA or upfront disbursements of official development assistance can mitigate risks and incentivise the commercialization of certain services and products such as new vaccines.

improving their systems and processes. Financing this type of technical assistance, could reduce costs for commercial investors and increase success rate.

Enabling the environment

Often the development actor can induce private investment by strengthening the enabling environment. An enabling environment has many dimensions: a stable macro-economic environment, adequate physical infrastructure, effective property rights and contract enforcement, adequate standard setting, a level playing field, … Supporting the enabling environment often needs the scale of bilateral and multilateral development programmes.

The use of these different Blended Finance models and instruments to attract commercial private finance is discussed in the next chapter.

7 Mobilising Private Resources

Blended Finance is about using development finance in a catalytic way to mobilise finance from the Private (commercial) Sector. The graph below shows the Blended Finance set-up. At the core of the set-up is the Blending instrument organised or financed by the Blending intermediary. As discussed in chapter 6 there are different forms this instrument can take, but all Blended Finance forms will try to improve the risk/return ratio using Development Finance and make the investment more attractive for Commercial Finance. The Blending intermediary is either the Development Actor who finances the instruments for risk mitigation (e.g. insurances, guarantees, hedging) or a DFI or Multilateral Development Bank (MDB) that can structure transactions or funds in such a way that it takes a more junior position in a transaction or a fund and as such improves the risk/return ratio for private commercial investors who want to join.

To make the Blending instrument successful, often there is a need for supporting mechanisms that strengthen the market, increase the private actor capacity and enables the environment in general. Also, on the investors side the regulatory environment must be adapted in order to enable the different investors to work together in a Blended Finance set-up.

Within the Blended Finance set-up, we can distinguish three types of finance and different sources (see the table below). The concessional flows form bilateral or multilateral aid agencies and from private foundations and NGOs are used to improve the risk/return ratio in the ways we have seen in 6.2. These flows can also be used to improve the external and internal enabling factors. Development finance from DFIs and MDBs is often used to set-up structured funds that give more possibilities to invite private investors to invest in a way that means less risk or higher return. The third type is commercial finance, mainly coming from private investors, though "Sovereign Wealth Funds" can also play an important role. Apart from corporates from the real economy that can invest in investment projects with which they often have operational and commercial links, there are different types of institutional investors that can provide commercial capital for investment projects with SDG relevance.

Figure 7-1 Blended Finance Set-Up

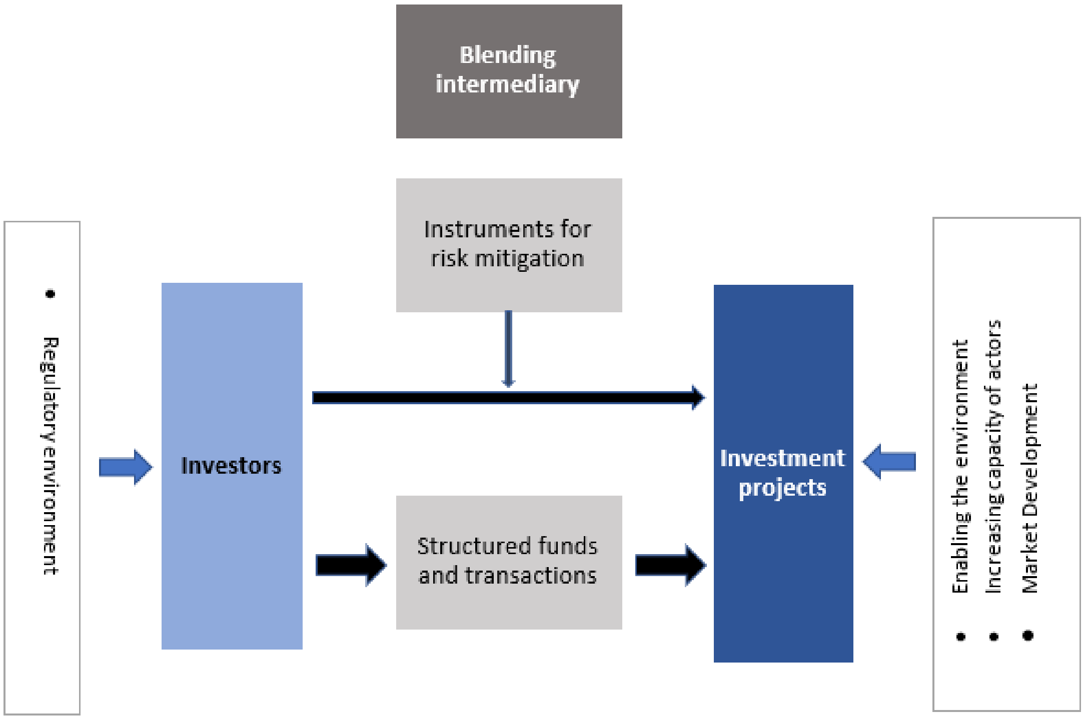


Table 7-1 Types and Sources of Blended Finance

Concessional flows (development aid)	Development finance at quasi-market conditions	Private commercial finance
(Public) bilateral development agencies (AFD, DFID, …)	Bilateral Development Finance Institutions (DFIs) (FMO, BIO, …)	Corporates (companies that link their activities to an investment). These can be big multinationals (e.g. Mars, Danone, …) or local SMEs.
Multilateral development agencies (UN, EC, …)	Multilateral DFIs (IFC, IDB Invest, …	Pension Funds
Private foundations and NGOs (Gates, Oxfam, …)	Multilateral Development Banks (MDBs) (EBRD, AfDB, …)	Insurance Companies
	Private Impact Funds and Investors	Banks
		Private Equity
		Asset/wealth managers
		Sovereign Wealth Funds (though not private these funds act as an important source of commercial finance)

Local investors: a largely untapped opportunity

Although not often included in BF set-ups, local investors in developing countries are critical for blended finance. In comparison to international investors, the barriers to entry for local investors in developing countries are lower as certain risks do not exist or are less as acute (e.g., currency, political, foreign exchange). Moreover, local investors have a better knowledge of the local environment and are better connected to the local economy. To illustrate the importance of local institutional investors: pension funds in Africa are expected to reach $620 billion by 2020 – as a result of expanding economies and of the growing workforce. However, Africa pension funds currently allocate only 1% of their assets to domestic private equity investments, representing a largely untapped opportunity for blended finance.[51]

Driving factors of private investment

To leverage the private sector as a source of financing for the SDGs, Blended Finance should be used to produce attractive investment opportunities. This requires a better understanding of potential private investors and their mandates, constraints, motivations, and investment preferences.[52]

Research from Convergence indicates that there are several considerations that will determine whether and to what extent an institutional investor participates in blended finance. Amongst those the most important are: i) risk-adjusted return ii) policy and regulation, iii) mandate, allocation and capacity, and iv) factors related to the deal or transaction.[53]

Risk-adjusted return

While in developed countries institutional investors typically expect returns between 10-14%, in developing countries expected returns are easily 200 basis points higher due to the country and other risk premiums.[54] Risk-adjusted return expectations are based on past performance of an asset class, which is problematic given the rather short track record of Blended Finance and the lack of data. So, there is need for clear communication in familiar language for the investors as to demonstrate how Blended Finance instruments or Blended structuring of the investment will reduce risk and increase the expected risk-adjusted return. (see chapter 6.2)

Communication is also needed to the shareholders, clients or depositors of the institutional investors, as to inform them how financial return can be combined with SDG impact thanks to Blending solutions. This way these share- and stakeholders of the institutional investors are invited to mandate (even pressurise) the investor to look for SDG impact in Blended Financed investment opportunities.

Policy and Regulation

After the 2008 financial crisis a whole set of global and national policies and regulations was put in place with the objective to ensure a stable global financial system and reduce unnecessary risk-taking by institutions that have a fiduciary responsibility to their shareholders and/or policyholders.

Examples of these in the European context are Solvency II and Basel III. Solvency II is an EU directive that has established a tougher capital-adequacy regime for insurance companies. The same directive also creates constraints outsourcing investment decisions and portfolio management to entities that are not regulated, making it difficult for European insurance companies to participate in transactions that are managed by DFIs/MDBs, which are not regulated.

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[51] CONVERGENCE. "Who is the Private Sector? Key Considerations for Mobilizing Institutional Capital through Blended Finance". Working Paper, January 2018, note 3.
[52] JOHNSTON J. "Engaging the Private Sector in Blended Finance". Ecdpm Great Insights. Volume 7 – Issue 2, Spring 2018, p. 20.
[53] CONVERGENCE (2018), o.c., p.2.
[54] Convergence (2018), o.c., p.21.

Under the Basel III regulatory framework, commercial banks are required to allocate high levels of capital when lending to high risk borrowers, particularly in countries with non-investment grade sovereign risk ratings.

Also the accounting standards IFRS 9 place severe restrictions on commercial banks allocating medium and long-term funds in developing countries through Blended Finance operations, as these investments have to reflect the risk rating of the country.

Therefore, Blended Finance initiatives need to take into account the possible impact of proposed investments on the balance sheets of the targeted institutional investors.

However, there is also internal regulation and policy that drives institutional investors to more or less SDGs aligned investments. One example is the fact that many institutional investors can only invest in listed assets. This reduces considerably the possibility for these investors to invest in developing countries and in non-listed assets. Internal policies and regulation are driven by the mandate that is given by shareholders and influenced by stakeholders.

Mandate, allocation and capacity

In general, the main mandate of institutional investors is return oriented taking into consideration certain risk levels. Often the risk is capped by restricting investments to certain financial instruments and by using ratings of countries, companies and financial instruments. Institutional investors will direct investments to SDG related projects, only if their share- and stakeholders are pushing them to do so. There is growing awareness of share- and stakeholders (clients!) of the negative development effects of certain asset classes, which present also investment risks in the long run. Therefor more and more investors use exclusion lists that reflect this awareness. Classic asset classes that are excluded are health related (e.g. tobacco) or related to high carbon footprint (e.g. coal energy). There are also a growing number of institutional investors demonstrating an appetite to explore investment approaches aligned with the SDGs. This is illustrated by the fact that even big mainstream banks now offer impact products. An example is the pledge of HSBC to invest USD 100 billion in sustainable financing investment by 2025.[55] Another example is the creation of an impact advisory and finance department by Credit Suisse. This department clearly states that the initiative is a consequence of rising demand from clients for products and services that incorporate environmental, social and governance aspects.[56] This initiative also illustrates that institutional investors like banks need to develop the specific organisational and technical capacity to source and manage this type of investments and take into account the growing importance of corporate responsibility within the private sector.

Also, asset / wealth managers face increasing pressure to build out capacity to offer alternative product offerings. Some of them have specialised in alternative assets, assets in emerging markets, and even investments aligned to the SDGs (e.g. Blue Orchard, responsAbility).[57]

Deal factors

There are several factors related to the terms of the deal or the investment that influence the attractiveness of blended finance opportunities for institutional investors: the currency in which the investment is made, the size, the tenor or investment horizon and the structural complexity of the investment.

Foreign currency risk is one of the main factors that will make investors restrain from investing. This risk exists for all foreign investment but is considered as more important in developing countries. As already discussed above (see 6.2), TCX is probably the only fund that can offer a foreign currency cover in these developing countries. (more on TCX in ANNEX 2) So there is certainly a need for more blended finance facilities that can offer similar) services as TCX does.

[55] https://www.hsbc.com/our-approach/sustainability/sustainable-finance
[56] https://www.credit-suisse.com/corporate/en/responsibility/banking/sustainable-products-services.html
[57] That these are not all success stories is illustrated by the downfall of the famous Abraaj Group: https://www.bloomberg.com/news/articles/2018-06-14/the-downfall-of-arif-naqvi-s-abraaj-group-dubai-s-star-investor

As local investments are often complex, size is an important factor as to keep the relative operational and administrative costs under control. Across all segments, institutional investors generally prefer a minimum investment size between USD 10 and 15 million and for their investment to be no more that 20% of total transaction size.[58] This type of transactions are rather rare in developing countries. That is why many investments are pooled in funds and in funds of funds. Even then most funds tend to concentrate on large scale initiatives, which are not always the right answer for specific developmental challenges.

The complexity of Blended Finance set-ups increases the transactions costs of institutional investors that are willing to invest. More streamlining and standardisation will certainly help. Also, administrative simplification is important to attract more investors. An example for instance is the introduction of single window systems, whereby different blending facilities are offered through the same window.

Time horizons

Tenor and tradability of the investment titles will also affect the possibilities for institutional investors to participate in Blended Finance operations. Different types of institutional investors have different time horizons. Pension funds, sovereign wealth funds, and asset/managers can hold illiquid credit, infrastructure debt, and other debt investments for periods of up to 10 years, while investors like banks prefer shorter tenors of not more than 3 years.[59]

As to attract the targeted commercial investors, Blended Finance operations have to be tailor-made taking into account the factors explained above. Although BF has made some progress, there is still a long way to go; certainly in finding ways to increase investment from the different types of commercial investors. Until now Blended Finance has mainly focused on international financial (debt) investors, while from the table below one can see that still other interesting boxes need to be "filled".

Table 7-2 Types of commercial investors

	Domestic investors	Regional investors	International Investors
Real Economy Companies			
Financial Investors (Debt)			
Financial Investors (Equity)			

It is difficult to define what leverage Blended Finance operations should attain. Or in other words how many euros of commercial finance should be mobilised by one euro of development finance. According to Convergence research the amount of commercial investment catalysed in blended finance structures varies greatly across structure types and sizes, focus sectors, and target countries. Convergence conducted an initial analysis of 56 blended finance transactions that use concessional debt/equity to attract commercial investment and found a median leverage of 2.6, with a minimum leverage ratio of 0.32 and a maximum leverage ratio of 24.[60] The fact that leverage is context specific and varies across sectors, geographies, and the different stages of the investment life-cycle is also specifically recognised by the DAC/OECD Blended Finance principles. DAC/OECD has developed five guiding principles[61] as to ensure that optimal impacts are achieved and additional finance is mobilised.

[58] Convergence (2018), o.c., p.23.
[59] Convergence (2018), o.c., p.23.
[60] Ibid, p.8.
[61] Other fora such as the DFI Working Group on Blended Finance have also developed guiding principles. Most of these principles concur with these of the OECD. In this paper we focus on the OECD BF principles as these have probably a broader reference framework.

8 Guiding Principles

"The OECD DAC Blended Finance Principles provide a five-point checklist to ensure blended finance meets accepted quality standards and achieves impact, based on a development rationale promoted by DAC members"[62].

These principles were agreed upon by the OECD DAC High Level Meeting end 2017 and they clarify the position of the OECD regarding BF, particularly in the context of its exchanges with its partners.

These Principles are considered as important guidelines if Blended Finance wants to achieve its double objective of additional finance and sustainable development. The five principles all look quite straightforward apart maybe from the fourth principle that is opting for a strict separation of both parties' commitment and mandate: Development Finance remaining only connected to the development mandate and Commercial Finance remaining within its commercial framework. Blending however is also an opportunity for development finance to learn from the financial sustainability of commercial actors and at the same time it can strengthen the sensitivity of commercial actors for their social and environmental responsibility. This would be in line with new attitudes towards entrepreneurship visible in the increasing attention for social entrepreneurship, inclusive business, corporate social responsibility (CSR) and accountability (CSA), and hybrid business models (see p. 12).

OECD DAC is not the only institution or group that has developed Blended Finance Guiding Principles. Also, the DFI Working Group on Blended Concessional Finance for Private Sector Projects has further developed such kind of principles.[63] However these principles focus more on combining concessional finance from donors alongside DFIs' normal own account finance and/or commercial finance from other investors. Seen the broader scope of the OECD DAC BF principles, we consider them as more appropriate in the context of this paper.

Below we represent the five principles as we find them in the OECD/DAC document.[64]

1. Anchor blended finance use to a development rationale
2. Design blended finance to increase the mobilisation of commercial finance
3. Tailor blended finance to local context
4. Focus on effective partnering for blended finance
5. Monitor blended finance for transparency results

- **Anchor Blended Finance to a Development Rationale:** This is the starting principle of Blended Finance (and of course of any development finance). Blended Finance should have a clear development rationale and objective as it is defined in the SDGs. This principle is further qualified by adding that **i)** development finance within the Blended Finance should be used as a driver to **maximise development outcomes and impact**; **ii)** the development objectives and expected results should be defined as a basis for deploying development finance and **iii)** Blended Finance should demonstrate a commitment to high quality and it should be based on high corporate governance, environmental and social standards.

- **Design Blended Finance to mobilise Commercial Finance**[65]: i) thereby Blended Finance needs to ensure **additionality**, by being deployed only for uses where commercial financing is not currently

[62] DAC/OECD. OECD DAC BLENDED FINANCE PRINCIPLES for Unlocking Commercial Finance for the Sustainable Development Goals. January 2018, p. 3. Retrieved from: http://www.oecd.org/dac/financing-sustainable-development/development-finance-topics/OECD-Blended-Finance-Principles.pdf .
[63] See for instance: DFI Working Group on Blended Concessional Finance for Private Sector Projects. SUMMARY REPORT. October 2017.
[64] The principles are given as we find them in the document mentioned in the footnote above. In a separate technical note for DGD we give a broader discussion of the principles.
[65] The Principles contained herewith focus on the increased mobilisation of additional commercial finance. As such, they are narrower than the complete scope of blending activities, which also comprise some DAC members' use of blending for the mobilisation of additional public

available for deployment towards development. ii) Blended Finance should, when appropriate, efficiently leverage commercial finance to achieve development impacts. **Appropriate leverage** is context specific and varies across sectors, geographies, and the different stages of the investment life-cycle. While increasing leverage over time is not necessarily an indicator of increased development impact, it is a sign of increasing market maturity and of successful mobilisation. It also serves as a signal for the need for eventual exit of development finance. iii) Blended Finance should be used **to address market failures**, while **minimising the use of concessionality**. Pioneering investments may require considerable concessionality but as markets mature, the magnitude of public contributions should decline. iv) Blended Finance must focus on **commercial sustainability**. In supporting the evolution of nascent and immature markets, there is the need for effective safeguards to ensure optimal resource allocation and avoidance of market distortion. This implies amongst others that at programmatic level sunset/exit clauses should be announced ex-ante to shape the appropriate expectations.

- **Tailor Blended Finance to Local Contexts:** Development finance should be deployed to ensure that Blended Finance supports local development needs, priorities and capacities, in a way that is consistent with, and where possible contributes to, local financial market development. This means i) supporting **local development priorities**; ii) ensuring consistency of Blended Finance with the aim of **local financial market development** and iii) using Blended Finance alongside efforts to promote **a sound enabling environment**.

- **Encourage Effective Partnering in Blended Finance:** Blended finance can only work if it meets the requirements of both sides, i.e. the development objectives for development actors, and the financial or commercial objectives of the commercial investors. This means that i) each party should be enabled to engage on the basis of their mandate and obligation, while respecting the other's mandate; b) risks are allocated in a targeted, balanced and sustainable manner and c) scalability is aimed for.

- **Monitor Blended Finance for transparency and impact:** To ensure accountability on the appropriate use and value for money of development finance, Blended Finance operations should be monitored on the basis of clear result frameworks, measuring, reporting on and communicating on financial flows, commercial returns as well as development results. This implies i) agreeing on performance and result metrics from the start; ii) tracking financial flows, commercial performance, and development results; iii) dedicating appropriate resources for monitoring and evaluation; iv) ensuring public transparency and accountability on Blended Finance operations.

The OECD DAC Blended Finance principles provide a framework on policy standards and guidance for the Belgian Government to base its decisions on scaling-up and mainstreaming blended finance. Having these principles as a basis for a Belgian Blended Finance policy will also facilitate the tracking of Belgian Blinded Finance in the OECD DAC tracking, monitoring and evaluation framework as is discussed in the next chapter.

However as is also mentioned in the 2018 Convergence report[66] the OECD DAC Blended Finance principles do not cover all or do not cover enough some of the concerns of certain policymakers and development practitioners. These concerns include:

- Debt sustainability: Blended Finance should be assessed and structured in the light of not adding to unsustainable debt-levels of Developing country governments and organizations.

development finance ("Blending 1.0"). The narrower focus of these Principles reflects the evolution of blended finance, in light of the importance of increasing the mobilisation of commercial finance ("Blending 2.0") to meet the financing needs of Agenda 2030.

[66] CONVERGENCE (2018),o.c., p. 36.

- Extreme poverty: Blended Finance should focus on least developed countries, including the need to design structures that respond to the specific needs of the most poor and vulnerable populations
- Aid effectiveness: Blended Finance structures should be compared to more classical use of ODA, to see whether it has advantages compared to grant-based ODA programmes in attaining certain SDGs.

9 Tracking, Monitoring and Evaluating Blended Finance

9.1 Tracking and Measuring Blended Finance

The fifth OECD DAC Blended Finance principle urges for appropriate tracking, monitoring and evaluation of Blended Finance. Until know there is little systematic data available on Blended Finance. Moreover, different actors understand and define blended finance differently and produce data that is are not necessarily comparable. Globally only OECD DAC and Convergence collect data based on surveys. OECD DAC is working on a new measurement framework of Total Official Support for Sustainable Development (TOSSD). TOSSD will track all financing provided by official bilateral and multilateral institutions – regardless of the level of concessionality involved or instrument used. It will also capture private resources that are mobilised through official means.[67] However there is still a long way to go for TOSSD to be operational. As a first step, a special TOSSD Task Force has been established to further elaborate the features of TOSSD and prepare a first set of Reporting Instructions. An agreement in 2019 on the scope and method of TOSSD reporting will enable the integration of TOSSD in the SDG monitoring framework in 2020. Until then we can only rely on data provided by the DAC and Convergence surveys.

As BF uses development finance to lever commercial funding there is a high need for transparency and accountability. This transparency can only be reached by agreeing on clear protocols for tracking and measuring BF's different components. These tracking and measuring systems must reveal how much development finance is being channelled towards blended approaches and what is being mobilised as a result, how this financing is being allocated in terms of countries and sectors, what impact is being achieved through blending, which instruments are most effective in mobilising commercial finance and addressing different Sustainable Development Goals etc. [68]

With its variety of actors and mechanisms BF presents a complicated tracking environment. BF combines or can combine public development finance, private development finance and commercial finance flows. There is no overarching system that covers and/or connects on these types of flows and that can measure and track them.[69] The TOSSD measurement framework mentioned above has the ambition to remediate this situation.

Seen the involvement of commercial finance the need for transparency goes beyond the mere tracking or measuring of the flows. Monitoring and evaluation need to provide the necessary information to assess to what extend the subsidy to a private actor was founded and what the contribution is on the achievement of the targeted SDGs.

9.2 Accounting for the Development Finance Subsidy

[67] http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/tossd-task-force.htm
[68] OECD (2018), o.c., p.129.
[69] Ibid, p.129.

In order to document the extent to which a subsidy to the private actor was justified, three factors of the Blended Finance set-up need closer documentation and monitoring: additionality, catalytic effect and sustainability.[70]

- Additionality is the core of Blended Finance. It refers to the fact that commercial finance would not have been available without the development finance lever, but additional also means going where other investors do not go: investing in underserved geographies (e.g. LDCs), sectors (e.g. smallholder agriculture) and segments (e.g. SMEs), or by taking a long-term approach.
- The catalytic effect means that Blended Finance should develop the market (instead of disturbing it), promoting other investors and other companies to come in and share the risk.
- Sustainability means reducing the dependence on development finance (aid), on the level of the private investor as well as on the level of the targeted SDG thereby applying responsible business standards for environmental, social and governance concerns.

These three dimensions of the justification for subsidies by development finance to commercial finance have to be situated in the specific context where the Blended Finance project is operating. Therefore, it is difficult to set general benchmarks. Each geography, each sector, each market will have its own requirements regarding the three dimensions. The monitoring and evaluation of these three factors therefore need to be contextualised, which means that a baseline study should include ex ante information on the financial and real economy of the market in which the BF project is situated.

Demonstrating the need for Development Finance subsidy in a Blended Finance set-up has to be completed by monitoring and evaluation of the development objectives.

9.3 Monitoring and Evaluation of the Development Objectives in a Blended Finance Setting

As Blended Finance includes Development Finance also BF should follow the Busan principles for effective development cooperation.[71] These include: i) following the development priorities of the investee's country ii) a focus on results iii) partnerships for development: development depends on the participation of all actors and recognises the diversity and complementarity of their functions. Iv) transparency and shared responsibility: Development Cooperation must be transparent and accountable to all citizens.[72]

At the core of development effectiveness is agreeing by the different partners involved on common development goals and the way to reach them. This qualifies further the first DAC principle that says that blended finance use should be anchored to a development rationale.

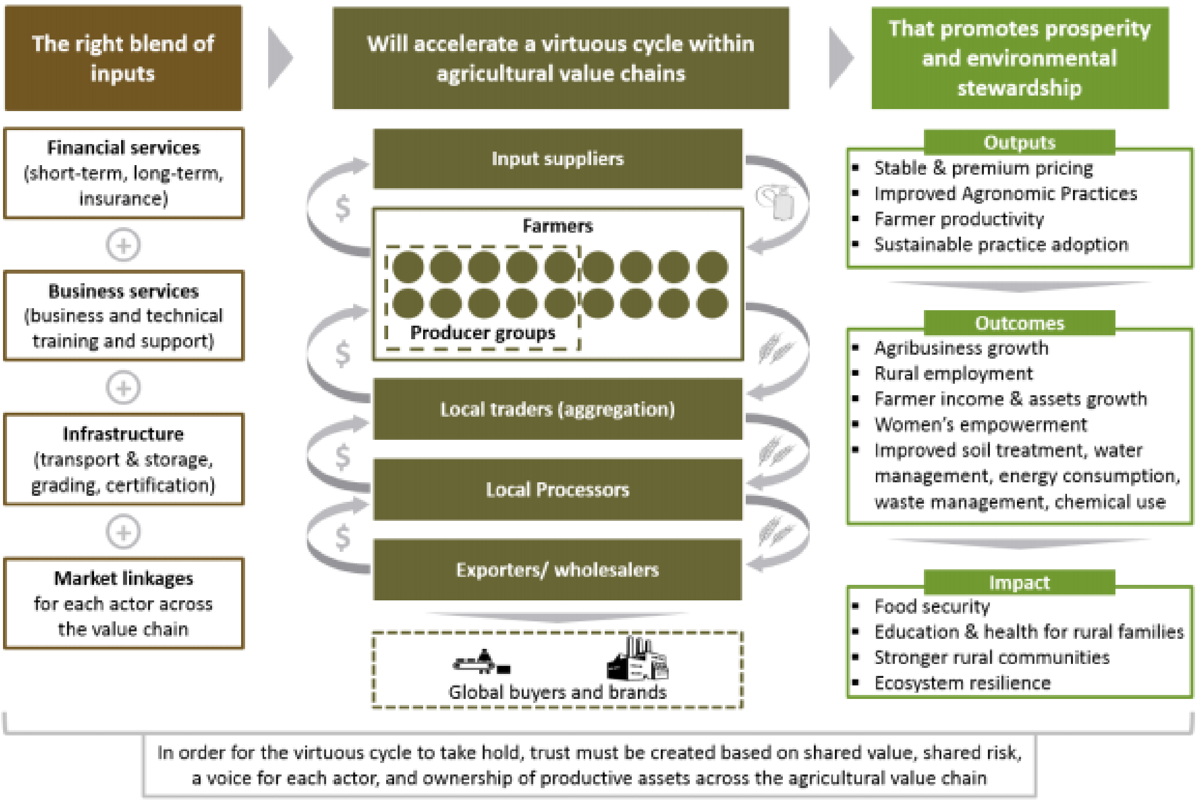
Development goals and the way to reach them, should be translated in a Theory of Change (ToC) that shows how a certain investment will contribute to the targeted SDG and what assumptions this entails. Based on this ToC a monitoring and evaluation (M&E) framework can be established. ToCs are often more complicated than the classical linear framework of inputs, outputs, outcome and impact. An example is the Smallholder ToC as it was developed by the Initiative for Smallholder finance (see Figure 9-1). As can be seen one activity or one input (e.g. financials services to smallholder farmers), can only contribute to for instance farmer income growth, if others factors and actors play their role and other assumptions and contextual factors are fulfilled.

[70] See for instance: Commons Consultants. "The Pitfalls of Innovative Private Sector Financing". Summary Report, 25 August 2015. Retrieved from:https://www.norfund.no/getfile.php/134022-1484725409/Bilder/Publications/Pitfalls%20of%20Innovative%20Private%20Sector%20Financing_Commons%20Consultants_final_150826.pdf

[71] For an elaborate discussion to what extend Blended Finance can or should be aligned with the Busan principles of development effectiveness we refer to: LONSDALE G. "Aligning blended finance with the Busan principles of development effectiveness". Development Initiatives Discussion Paper. October 2016.

[72] Taken from http://www.oecd.org/dac/effectiveness/49650173.pdf

Figure 9-1 Smallholder Theory of Change



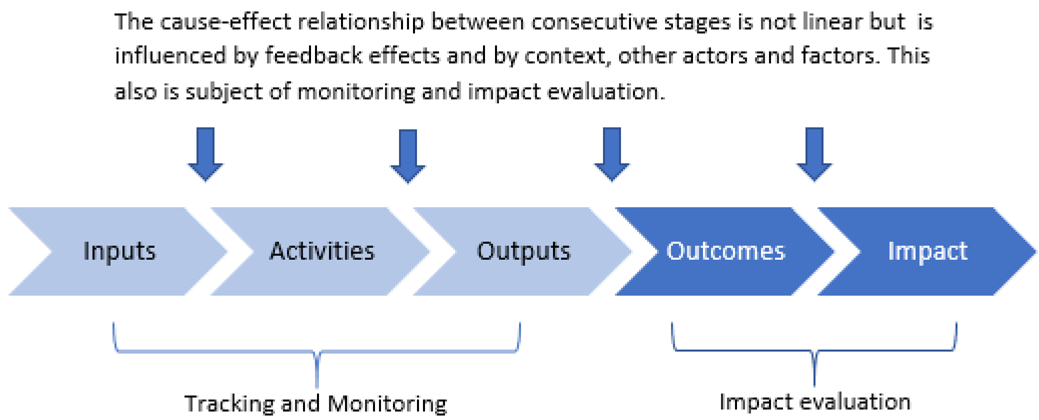
Source: The Initiative for Smallholder Finance. "SMALLHOLDER IMPACT AND RISK METRICS: A LABYRINTH OF OPPORTUNITY". Briefing 03. March 2014, p. 4. retrieved from https://www.raflearning.org/sites/default/files/smallholder-impact-and-risk-metrics-a-labyrinth-of-opportunity1_0.pdf?token=60xRRJ0n

The monitoring framework will need to collect data on those inputs/activities that are being financed and those outputs that are targeted by the BF set-up. At the same time, it will need to take into account the changes of other factors/actors and changes in the context (in the case above mainly the smallholder agriculture value chain). For these activities/inputs/outputs, indicators must be agreed upon by the different stakeholders. For these indicators ex ante data have to be collected and targets have to be set. The monitoring data will give the factual evidence of the progress that has been made reaching the planned output within the BF set-up.

The medium-term outcome and the long-term impact of the Blended Financed programme will be subject of evaluation ad mid-term or ex post of the programme. The impact-evaluation will not only need factual information, but also counter-factual information of how the situation would have evolved if the programme had not taken place. This will substantiate the relevance of the programme. Producing this counter-factual evidence is a methodological challenge. Experimental
approaches may produce such evidence, but they are quite resource consuming and now always feasible. ToC-based evaluations instead will validate the underlying assumptions of the public intervention against the observed outcomes by analysing the causal mechanisms, possible unintended effects and the specific context in which they work.[73] [74]
Schematically the monitoring and evaluation framework can be depicted as in the figure below.

[73] OECD (2018), o.c., p.149.
[74] For an extensive discussion of Impact Evaluations, we refer to the NONIE Guidance on Impact Evaluation: "Impact Evaluations and Development". 2009. That can be retrieved from: http://siteresources.worldbank.org/EXTOED/Resources/nonie_guidance.pdf

Figure 9-2 The Monitoring and evaluation framework



Monitoring and evaluating a Blended Financed investment are not just a technical exercise. There is an important political dimension to it. First of course the investment is value driven as it has an SDG as objective and not all stakeholders might have the same idea on the objective or the way to get there. Lack of alignment of the different stakeholders will also influence the monitoring and evaluation exercise. Apart from the alignment problem, a Blended Finance investment can also be seen as a complex chain of principal-agent relationships that will lead to different situations of asymmetric information. In a situation of Blended Finance where Development Finance is used to lever Commercial Finance, privileged information on risk and return by the commercial financier can lead to wrong allocation of Development Finance. The designs of the Information flows that are used to manage, to monitor and to evaluate the Blended Financed investment should take this into account. The problem of asymmetric information is even more acute in combinations of Blended Finance and Result Based Finance.

10 Blended Finance and Result Based Finance

Blended Finance is there to grow the financial flows for development in general and for the SDGs specifically. This only makes sense if also the development impact per invested dollar can grow. Improved targeting and monitoring are therefore essential and the 17 SDGs with their 169 targets and 232 indicators have been developed for that purpose.

A number of donors have started to use an approach called Result-based Financing (RbF), Payment by Results (PbR) or Performance-based Financing (PbF), assuming that this way they can increase the effectiveness of ODA and Blended Finance. By conditioning payment on the achievement of results, these approaches build in a more rigorous focus on outputs and outcomes and provide more flexibility to the implementing partner to reach these pre-defined targets.

PbF is defined as a financing mechanism that gives financial payments based on the achievement of predetermined targets, goals or outputs after being verified for quality. This approach has three key features:

- Payments for pre-agreed results
- Recipient discretion over how the results are achieved
- Independent verification as the trigger for disbursement

In the context of PbF in the health sector this definition is often considered too narrow and is broadened in the following way: "performance-based financing is a supply-side reform package that is guided towards improved performance (defined as increased predefined services and improved quality measures) by using performance-based financial incentives for health providers (facilities and/or workers) through internal contracting and strengthening this with most or all of the following elements: a separation of functions (purchaser, provider, verifier), (spending) autonomy for the health facilities, strict monitoring and verification of services, community involvement, result-based planning and accountability arrangements."[75]

Also, this broader definition includes the three key features, but it situates the PbF in the broader perspective of a (health) policy reform package and highlights more the shift in the (contractual) relations between the different stakeholders.

Traditional funding models provide financing up-front. Money is disbursed irrespective of the attainment of outputs or outcomes. Based on previous experiences, it is assumed that financing certain inputs and activities will result in the attainment of specific outputs and outcomes. Evaluations have however shown that reality is sometimes different.

Under results-based approaches, (partial) payments are only disbursed after pre-agreed targets have been achieved. It is here also that asymmetric information might diminish the efficiency and the efficacity of a RbF programme. The executing agent has often much more information on cost structures and the realisation of objectives than the principal and other stakeholders. Independent verification therefore is necessary. Though even then not all risks associated to situations of asymmetric information can be excluded.

RbF is an "ex-post" funding approach which creates a pre-financing need at the level of the implementer. Certain implementers like governments or NGOs might have the liquidities to do so, but when this is not the case, external investors might be invited to bridge the funding-gap and Blended Finance might play a role in this, for instance by creating a Development Impact Bond.

11 Development Impact Bonds

Development Impact Bonds (DIBs) are a way to pre-finance PbRs funded development programmes. A DIB only makes sense as far as the underlying PbR makes sense. Therefore, before venturing into launching a DIB, it is crucial to assess if a PbR is the most appropriate way to fund certain development objectives.

In case the implementer of a development programme has not enough liquidities to pre-finance a PbR programme, a DIB might be the appropriate way to provide this necessary finance. A DIB is a way to pre-finance and should not be seen as additional finance. It merely mobilises reimbursable funds. In this sense it does not really comply with the additionality condition of Blended Finance. However, it shifts wholly or partially the risk of the investment from the traditional donor (the Outcome Funder) to the Investor. The risk shift is one of the core issues of the DIB.

DIB has been seen as a way to commit private commercial funds to a development cause. Until now this has appeared to be a fallacy as the Brookings study[76] has revealed. This is not surprising as the risk-return profile of a DIB is such that it will be difficult to attract commercial investors, unless the private investor gets a more "senior" position in the DIB structure and the return is more market conform.

The Development Impact Bonds (DIBs) are a way to mobilise funds with external investors for pre-financing the PbR financed programme. DIBs involve several actors that need to collaborate under the Development Impact Partnership (Bond). The actors that are shown in the figure below are the following.

[75] RENMANS D. et al. "Performance-based financing: the same is different". Health Policy and Planning, Volume 32, Issue 6, 1 July 2017, Pages 860–868 retrieved from https://academic.oup.com/heapol/article/32/6/860/3091187
[76] Gustafsson-Wright E. et al. "Impact Bonds in Developing Countries: Early Learnings from the Field". Center for Universal Education at Brookings, September 2017.

The Investor: is the party to the Development Impact Partnership that is pre-financing the Service Provider for delivering certain services with the aim of achieving a certain development output/outcome. This pre-financing is done under a "loan" contract, of which the beneficiary is the Service Provider, but the repayment obligation lies with the Outcome Funder. The repayment obligation only exists as far as certain pre-defined output/outcome targets are achieved. This means that the Investor carries the risk of non-achievement. The Investor is rewarded for this risk and for the cost of funds by an interest paid on the loan amount. Investors can be foundations, philanthropists, multilaterals, bilaterals, intergovernmental financial institutions (IFI), impact investing companies, institutional investors and theoretically also commercial actors such as banks and investment funds.

The Outcome Funder: is the party that at the end will pay for the development output/outcome and will reimburse the Investor as far as certain pre-defined output/outcome targets are achieved. In the Belgian case the Outcome Funder would be DGD or by delegation Enabel. However, the DIB can also be structured by a Development Impact Fund, in case which several Outcome Funders will collectively reimburse the Investor.

The Service Provider: is the party that is responsible for executing a programme that will lead to the targeted development outputs/outcomes. A "simple" DIB shifts the risk for non-achievement towards the Investor. Therefore, other ways for making the Service Provider accountable should be included. The Service Provider can be local government agencies, non-profits, international organizations, nongovernmental organizations, development organizations or community organizations.

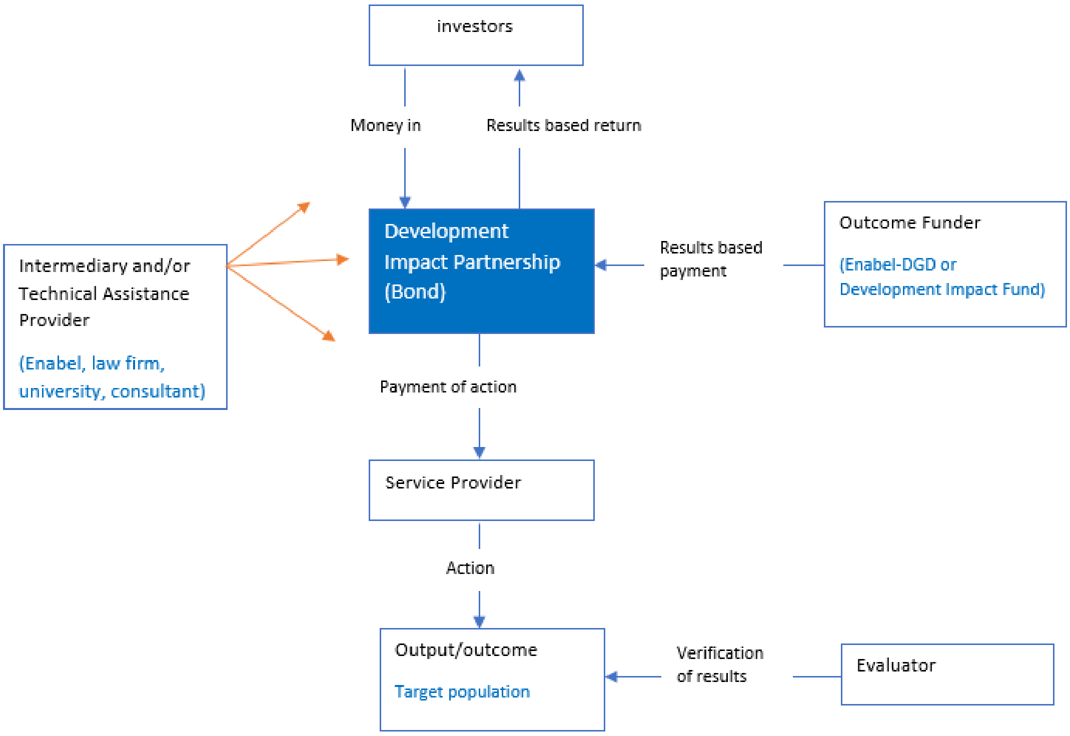
The Evaluator: is the party that is responsible for assessing the outcome metrics and for determining to what extent the ex-ante defined targets have been reached. The assessment of the outcome metrics is key in the DIB and as such the Evaluator has also a very important role to play and must be able to execute this role independently from any other party to the DIB and without any possible conflict of interest. The Evaluator can be research institutes, academics or professional services firms.

The Intermediary: is not a party of Development Impact Partnership itself but will mediate between the different parties of the DIB. Depending on the mandate the intermediary might also be responsible for structuring the DIB and mobilising the funds (the **Investors**). In the Belgian context the Intermediary might be Enabel or by delegation more specialist companies such as impact investors, law firms or fund managers.

The Technical Assistance Provider: is the entity that can provide more specific technical assistance in, for example, selection of outcome metrics and repayment terms or specific legal requirements. The Technical Assistance Provider can be research institutes, academics, professional services firms and law firms.

Raising capital and structuring the financial product is the critical test of the "funding" feasibility of the DIB. Raising capital from commercial private investors might be the ambition of many DIBs, however, to date, impact bonds have relied heavily on investors who do not seek market returns. This is not surprising as the DIB is a financial product that is a "bond" only in name. The risk is not related to the issuing party but to the achievement of certain development goals. The risk of non-achievement is not easy to assess and cannot be "rated". So, it is difficult for the investor to know what return would match with the risk. The DIB has more the characteristics of an equity product, though it has the disadvantage that it punishes for the "downside": no repayment without "success" but does not reward (more) for the "upside": same return for success and beyond. Therefore, to attract commercial investors (including many impact investors), the bond needs to be structured in such a way that non-commercial investors carry the main risk (junior and mesa funds) while commercial investors can invest at lower risk and higher return.

Figure 11-1 The Development Impact Bond structure



As can be seen from the figure on page 37, a Development Impact Bond creates even more complicated chains of principal-agent situations than a grant funded PbF. Transparent management of the information related to the DIB is therefore of utmost importance.

Setting up a DIB is costly and complex as many actors are involved. However, under the right conditions, it might create dynamics that are beneficial in the end in terms of innovation, effectiveness and efficiency.[77]

12 The Belgian Institutional Framework for Blended Finance

The policy documents 2017-2018 of the Minister of Development Cooperation mention the two axes of the present Belgian policy for Development Cooperation. The first one is based on a Human Rights approach and the second one on inclusive and sustainable growth. The support of the local private sector, domestic resource mobilisation and innovative financing are specifically mentioned as new "instruments" for development.[78] This means that at policy level there is certainly the intention to use ODA in a more catalytic way and to lever private investment when possible.

The Belgian Development Cooperation, for executing its Blended Finance strategy, can appeal to two actors that have 'interacting with the private sector' in their mandate. These are: BIO, the Belgian Investment Company for Developing Countries and ENABEL, the "new" Belgian Development Agency (the former BTC). The central actor at the policy level is the Directorate General Development Cooperation (DGD).

[77] A more elaborate discussion of the Development Impact Bond can be found in Cassimon D. and Couderé H. "Development Impact Bonds. BeFinD Technical Note, 18/05/2018.
[78] See: "Verantwoording van de Algemene Uitgavenbegroting voor het begrotingsjaar 2018: 14. FOD Buitenlandse Zaken Buitenlandse Handel en Ontwikkelingssamenwerking" Belgische Kamer van Volksvertegenwoordigers, 24 Oktober 2017, DOC 54 2691/008.

With the legal reform of both BIO[79] and ENABEL[80] and the changes of their respective management contracts with the Belgian State[81], the legal framework is set to make them the main public actors in a Belgian Blended Finance strategy. With the upcoming Royal Decree on Innovative Financing Instruments, there will also be a legal framework for innovative financing instruments that can be used in a Blended Finance set-up.

Other actors that are not part of the Belgian institutional framework for development cooperation, but that due to the nature of their mandate can or could be involved in a Blended Finance strategy are: CREDENDO, FINEXPO and the Belgian Corporation for International Investment (BMI-SBI).[82]

Apart from the Belgian actors there are also multilateral actors that play or can play a role in a Belgian Blended Finance strategy. Some of the Belgian multilateral development cooperation has a clear private sector linkage. Besides debt relief operations of the heavily indebted poor countries (HIPC) and the Multilateral Debt Relief Initiative MDR, the Belgian mandatory contributions to the World Bank also finance the International Development Association (IDA) and are used for capital increases of the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC). All three IDA, IBRD and especially IFC have a private sector development agenda. In fact, the IFC's prime goal is private sector development in developing countries, through provision of loans and advice and participation in equity. Or, as their website states: "IFC blends investment with advice and resource mobilization to help the private sector advance development". Belgian support to other multilateral organizations, such as for example the International Labour Organisation (ILO), the International Fund for Agricultural Development (IFAD) and the Food and Agriculture Organization (FAO) can also have a strong private sector component, for example when looking into increasing agricultural production or impacting on labour conditions, but is arguably less oriented at mobilizing private (financial) resources for development.

On the European level, different European Blended Finance facilities have been developed (see Chapter 13). Until now Belgian Development Cooperation does not access these facilities, although these could fit in a comprehensive Belgian Blended Finance policy. ENABEL has a pillar 6 assessment[83], which in theory gives access to the different European BF facilities except for guaranties. BIO will have pillar 7 assessment, so it can access all the facilities of the European External Investment Plan. At the European level, Belgium with its representatives from the Federal Public Service of Finance (FPSF) and DGD is participating in the EU Platform for Blending and External Cooperation (EU-BEC). A more active Belgian participation in the European Blended Finance facilities would then also seem logic.

Finally, also on the radar should be the synergy that is aimed at between the agendas of climate change mitigation and adaptation on the one hand and private sector engagement on the other. Many instruments that fund climate change mitigation and adaptation in developing countries attempt to leverage additional private finance or facilitate private development and implementation of projects contributing to low-carbon development. For example, the Green Climate Fund, to which the federal government contributed 50 million Euro from the budget for development cooperation, also has a Private Sector Facility. [84]

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[79] The law of July 21st, 2016 : Wet tot wijziging van de wet van 3 november 2001 tot oprichting van de Belgische Investeringsmaatschappij voor Ontwikkelingslanden en tot wijziging van de wet van 21 december 1998 tot oprichting van de "Belgische technische coöperatie" in de vorm van een vennootschap van publiek recht.

[80] The law of November 23d, 2017 - Wet tot wijziging van de naam van de Belgische Technische Coöperatie en tot vaststelling van de opdrachten en de werking van Enabel, Belgisch Ontwikkelingsagentschap

[81] December 20th, 2016 Bijkomende Overeenkomst bij het eerste Beheerscontract tussen de Belgische Staat en de Naamloze Vennootschap van Publiek recht "Belgische Investeringsmaatschappij voor Ontwikkelingslanden" (BIO) van 1 april 2014 and December 17th, 2017. - Koninklijk besluit houdende goedkeuring van het eerste beheerscontract tussen de Federale Staat en de naamloze vennootschap van publiek recht met sociaal oogmerk Enabel, Belgisch Ontwikkelingsagentschap

[82] The Regions are left out here, as they are beyond the scope of this paper.

[83] Under indirect management the Commission can entrust budget implementation tasks to certain countries, organisations and bodies (referred to as 'Entities'). Entities wishing to work with EU funds under the indirect management mode must successfully pass a "Pillar Assessment". These entities must meet requirements in up to seven areas relating to 1) the internal control system, 2) the accounting system, 3) an independent external audit 4) rules and procedures for providing financing from EU funds through grants, 5) procurement 6) financial instruments and 7) Sub-Delegation.

[84] Reference is made to the "begroting voor Buitenlandse Zaken, Buitenlandse Handel en Ontwikkelingssamenwerking": http://www.dekamer.be/FLWB/PDF/54/2691/54K2691008.pdf

12.1 Directorate General Development Cooperation

The central actor of Belgian Development Cooperation at the policy level is the Directorate General Development Cooperation (DGD), situated in the Federal Public Service of Foreign Affairs, Foreign Trade and Development Cooperation. DGD delegates the implementation of development policy to several other actors: ENABEL, the Belgian Development Agency, the Belgian Investment Company for Developing countries (BIO), different non-governmental actors (NGAs) (such as NGOs and trade unions) and several multilateral institutions.

DGD coordinates several thematic platforms - e.g. on agriculture, food security or health - that bring together different stakeholders. Although the role of the private sector in these domains is at times subject of discussion, it is not a standing item on the agenda of these platforms. The strategy note on the private sector announced the establishment of such a platform on 'entrepreneurship for development' in which representatives of public, private, and non-governmental organizations as well as advisory councils and representatives of the private sector could participate. Finally, after some 'test-runs' the idea for the platform was not continued. [85]

Within DGD and until September 2018, the Direction Inclusive Growth (D2.2) is the sole department that has inclusive growth and the private sector in developing countries as focal points. Its tasks are:

- Monitoring international institutions such as the World Bank, IMF, ADB, FAO, CGIAR;
- Support towards the (local) private sector, including monitoring BIO and ENABEL as far as it concerns private sector support;
- Agriculture and food security;
- Innovative financing mechanisms;
- Digitalisation for development.

Additionally, D2.2 advises DGD on other partnerships with non-governmental actors, it participates in relevant international policy discussions and maintains communication with other departments. Its involvement in international policy discussion on mobilizing private resources for development is illustrated by joining the FSPF[86] for the Belgian participation in the EU Blending Committee (EU-BEC), where it has essential input regarding Belgian ODA in European and international files. This includes also participating in the different relevant political and technical EU-BEC committees

D.2.2 maintains basic contacts with the Directorates Bilateral Affairs (DGB) and European Affairs (DGE) of the FPSFA[87], which both have competences related to the role of private sector in international cooperation: the latter is involved in the follow-up of the aid for trade agenda at the European level, whereas the first is responsible for Belgian economic diplomacy.

D2.2 has a personnel capacity of 6 full time equivalent personnel, which is obviously very limited seen the scope of tasks and seen the ambition to focus more on the private sector and the development of innovative financing mechanisms. Moreover, a new focus on the private sector also needs specific competences, that maybe are not enough available yet. At the time of writing this paper there was a vacancy for one more person to strengthen the D2.2 team in this regard.

[85] See for instance: https://www.alexanderdecroo.be/federale-regering-stelt-bio-open-voor-private-investeerders/
[86] The Federal Public Service of Finance
[87] The Federal Public Service of Foreign Affairs

12.2 ENABEL

The main implementing actor is ENABEL, the Belgian Development Agency, until 2017 working under the name: BTC/CTB (Belgische Technische Coöperatie / Coopération Technique Belge). BTC was established in 1999 and was responsible for the execution of the direct, bilateral cooperation. Based on the "ENABEL law" of November 23, 2017 and the Royal Decree of December 17, 2017, a new reform took effect from the 1st of January 2018 onwards. This reform includes a name change from BTC/CTB to ENABEL.[88] With this reform, the federal government wants to prepare the Belgian Development Agency for the implementation of Agenda 2030 for Sustainable Development. Besides governments, civil society and the private sector also play an important role in the new development agenda. ENABEL will deploy activities in domains that are important in this respect: such as strengthening local entrepreneurship and supporting digitalisation as lever for development. Developing innovative development financing is also mentioned explicitly as one of the new tasks of ENABEL.

Thanks to the ENABEL Law and the Royal Decree under preparation, ENABEL will be able to broaden its funding by also attracting private finance[89] and at the same time it can diversify its financing instruments by extending subsidies and loans towards private entities. Nevertheless, ENABEL cannot engage in activities/products that are earmarked for BIO (see below). This will probably lead to some borderline discussions.

At the moment however, ENABEL's activities remain focused on governmental development cooperation, supporting private sector development and promotion of sustainable trade. Most of the tasks regarding the private sector, have been clustered until now in a specialised program: The Trade for Development Centre (TDC). The specific objective of the TDC is to improve access to markets for producers-based organisations in one of the partner countries, and to promote sustainable trade. It provides financial and technical assistance to MSMEs in developing countries and is supposed to support DGD as well as the geographical desks within ENABEL, on their approaches to or interactions with the private sector in partner countries. Most of the technical assistance assignments towards private sector partners (MSMEs) is delegated towards consultants.

Until recently, with the exception of their Trade for Development Centre, ENABEL had little experience in interacting with the private sector and with setting up other than grant financing. Within ENABEL most private sector competences are geared towards organisational strengthening and marketing. There is less capacity regarding business and finance. If the "new" ENABEL wants to pursue the political ambition with respect to private sector interacting, it will need to strengthen its capacity to develop financial instruments/vehicles and manage debt finance. There is certainly also a need at the implementing level, to increase capacity in terms of personnel, financial instruments and working methods. Increasing this kind of capacity is not only needed to access existing Blended Finance facilities at European level or with Multilateral Agencies but is also needed to engage with the Belgian and local private sector and to mobilise additional private resources.

[88] ENABEL is the on purpose misspelled "Belgian" variant of the English verb enable, as it is said to express the philosophy of the new Belgian international development policy.
[89] The new ENABEL law explicitly mentions the possibility for the minister to instruct ENABEL to develop "innovative financial instruments". A new Royal Decree on innovative financial instruments is under preparation. This Royal Decree will foresee the conditions for issuing Developmental Impact Bonds and Blended Finance instruments.

12.3 The Belgian Investment Company, BIO Invest

Second heavy weight is the Belgian Investment Company, BIO. BIO was established in 2001 with a start capital of 4,957,873 EUR, of which 50% of the shares were in the hands of the Belgian state and 50% in the hands of the Belgian Cooperation for International Investment (BMI). However, in view of the limited prospect for synergies between BMI's and BIO's investment approaches, BMI withdrew. At the end of 2013 the Belgian state became sole owner of BIO, of which the total capital at that moment amounted to 600 million EUR. At the same moment a campaign organised by civil society organisations, questioned the role of BIO, which set the scene for an important reform.[90] It was aimed at improving the development and relevance of BIOs activities as well as their complementarity with the other activities of the Belgian development cooperation, and in particular those of ENABEL. Again in 2018 an update of the BIO law was voted and a new management contract between BIO and the Belgian State was prepared.[91]

The main mission of BIO is to invest in the development of micro, small and medium enterprises either directly in these enterprises or indirectly through financial intermediaries. Apart from this, BIO can also invest in the "social economy" and in projects that improve access to energy, access to digital technologies, and projects that contribute to the fight against climate change or provide basic services to the public.[92]

BIO can use medium- and long-term loans, participation in equity, guarantees, and hybrid financial instruments. The BIO law mentions 4 conditions under which these investments can be made.

Investments should: 1° aim to contribute to the economic and social progress of the intervention countries and thus offer sufficient perspective on development returns; 2° lead directly or indirectly to sustainable productive employment, with respect for fundamental social rights as defined in the conventions of the International Labour Organization; 3°offer a perspective of return (see further); 4° be additional (not defined).

The Belgian State can grant resources to BIO by: 1° contributing to capital; 2° subscribing to "development certificates" (quasi capital); 3° giving capital subsidies; 4° subsidies other than capital subsidies; 5° fees for certain assignments (fund management).

The use by BIO of the resources under 1° and 2° above, is bound by a return objective that ensures that the contribution can always be classified as a participation within the public sector in accordance with the European system of national and regional accounts. The capital subsidies on the other hand can be used to realize investments that have a lower return objective. The allowances for write-downs and the capital losses on these investments are charged directly to the capital subsidy, as are the costs related to the management of the investments made with the capital subsidies.

Subsidies other than capital subsidies (see 4° above) Can be used to finance the following interventions: 1° training programs; 2° technical assistance programs; 3° feasibility studies; 4° investment support for innovative SMEs, in the form of a financial intervention for certain costs and assets with a view to starting or improving an enterprise or a new activity; 5° the analysis and layout costs of investment files in the context of a probable financing by BIO.

The recent reform of the BIO law gives BIO extensive possibilities to have a fully "blended" approach towards private sector development.[93]

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[90] See the Laws of January 20, 2014 and of July 21, 2016.

[91] See 25 OKTOBER 2018. - Wet tot wijziging van de wet van 3 november 2001 tot oprichting van de Belgische Investeringsmaatschappij voor Ontwikkelingslanden en van de wet van 23 november 2017 tot wijziging van de naam van de Belgische Technische Coöperatie en tot vaststelling van de opdrachten en de werking van Enabel, Belgisch Ontwikkelingsagentschap

[92] December 2018: Ontwerp tweede beheerscontract tussen de Belgische Staat en naamloze vennootschap van publiek recht "Belgische Investeringsmaatschappij voor Ontwikkelingslanden" (BIO) and December 20th, 2016 'Bijkomende Overeenkomst bij het eerste Beheerscontract tussen de Belgische Staat en de Naamloze Vennootschap van Publiek recht "Belgische Investeringsmaatschappij voor Ontwikkelingslanden" (BIO) van 1 april 2014'.

[93] In budgetary terms this means that it can combine code 8 labelled resources (not accounted for as an expense in the national budget) with code 5 labelled resources.

Also, at the level of the different investments there is blending with sources of private origin. Until now Belgian private financial resources where not mobilised at portfolio level. In 2018 however, BIO has initiated the launch of a private investment fund, the "SDG Frontier Fund", that will be financed for 75% by private funds, along a 25% BIO participation, reaching a total capitalisation of EUR 30 million. The SDG Frontier Fund will co-invest alongside BIO, mainly in local SME investment funds in Africa and Asia. This way the fund can benefit from the financial assessment and social screening that is done by BIO.

BIO will also be pillar 7 assessed, which would make it eligible for accessing the European Blended Finance Facilities. However, BIO has initiated this process in the first place to have a quality label that would show it complies with the "fit for purpose" criteria set by the Belgian government.

Apart from ENABEL and BIO, there are three Belgian institutions promoting international trade and investment, that at a certain point could play a role in Blended Finance operations. These are CREDENDO, FINEXPO and BMI

12.4 CREDENDO

The Nationale Delcrederedienst | Office National du Ducroire, known today as CREDENDO – Export Credit Agency has a long history (since 1921) of supporting Belgian export and international trade worldwide. In their own words their mission today is: "… *to support trade relations. We provide customised solutions of insurance, reinsurance, guarantees, bonding and financing related to domestic and international trade transactions or investments abroad. We protect companies, banks and insurance undertakings against credit and political risks, and facilitate the financing of such transactions.*" As the CREDENDO group has bought in or taken over other European trade insurers it can now be considered as a European insurance group. The group is offering services in EU countries, in CIS countries and in developing countries or emerging markets. Services are related to covering commercial, financial and political risks and to financing export. It has a special programme for Belgian SMEs that extends financial guarantees for bank credits and direct or indirect credit (through forfaiting) for foreign buyers.

CREDENDO has no specific SDG oriented policy though it has a corporate social responsibility policy that analyses environmental and social impact of the different projects for which its services are requested. The basis of the impact analysis is inspired by the OECD 'Recommendation of the council on common approaches for officially supported exports credits and environmental and social due diligence (The "common approaches")'. Environmental and social assessment of projects has further to be done in accordance with different international standards like the Performance Standards of the International Financial Corporation (IFC).

Although the Minister of Development Cooperation is represented in its board of directors, CREDENDO is not involved in any of the programmes of the Belgian Development Cooperation. CREDENDO does not get funding from the Belgian Development Cooperation except for some debt-service funding for a remediating loan of the former Nationale Delcrederedienst (non-ODA accountable), dating back from 1991. However, there is certainly potential to integrate CREDENDO in a Belgian Blended Finance policy. CREDENDO is for instance already insuring political risks of some investments of two private Belgian Impact Investors[94]. Unfortunately, several investments of these and other investors are excluded if they are done in fragile states, where the CREDENDO risk scoring is at "7", being the maximum. Given the small investment amounts used by impact investors such as Kampani, the transaction cost is also high relative to the investment size. This means that investments are not supported where it is needed the most from an SDG point of view. It is clear that in this case collaboration between the Belgian Development Cooperation

[94] These are Alterfin and Incofin.

and CREDENDO would be meaningful and an ODA financed risk mitigation could have an important impact on SDG inspired investments.

12.5 FINEXPO

FINEXPO was created by Royal Decree of 30 May 1974 'to reinforce the Belgian instruments for financial support to export'. FINEXPO is an export support programme under the supervision of an inter-ministerial advisory committee managed by the Directorate Financial Support for Exports (B2) within the Federal Public Service Foreign Affairs, Foreign Trade and Development Cooperation, and by the Administration for International and European Financial Affairs of the Federal Public Service Finance. The name FINEXPO combines two key words: financing and export. FINEXPO's aim is to support exports of Belgian capital goods and related services to developing countries, taking into account the development needs of these countries and the need for economic, environmental and social sustainability within the international regulatory framework.[95]

The WTO, the World Bank and the OECD only authorise export support in the form of tied or untied aid to developing countries. FINEXPO operates within this framework.

FINEXPO has no real development objectives in the sense of a targeted contribution to SDGs. However, condition for support is that a project is adapted to needs and interests of the beneficiary country. The project should fulfil rational economic, social and environmental needs of the host country and should significantly contribute to its economic and social development. Four out of five FINEXPO instruments are eligible as ODA due to their concessionary nature. These instruments ensure that aid includes a grant element representing at least 35% of the total cost of the contract.

FINEXPO has seven financing instruments at its disposal, of which one is commercial: the interest stabilisation programme (no grant element) and six are concessional[96] (with grant element). These concessional instruments are further subdivided in a tied and an untied aid programme. The untied aid programme has only one instrument being: the untied state loans (for government institutions only).[97] The tied aid programme has five instruments being: grant, interest rate subsidies with or without additional grant, mixed credit: a combination of a State-to-State loan with a commercial loan, grant for technical assistance (for public institutions only) and a (Belgian) SME oriented financing instrument for innovative products (also for public clients only).

The budget for all these financial instruments appears on the budget for development cooperation. For 2018 the budget for State-to-State loans amounts to EUR 47 million, while all other instruments have a combined budget of EUR 26.6 million.

FINEXPO is managed by the FINEXPO Secretariat under the supervision of the FINEXPO Committee. The FINEXPO Secretariat is made up of representatives from FPS Finance and FPS Foreign Affairs. It coordinates the day-to-day activities of FINEXPO. The Secretariat handles applications for interest rate subsidies, grants, technical assistance, stabilisations (FPS Foreign Affairs), and State-to-State loans (FPS Finance). The Secretariat is the point of contact for exporters.

The FINEXPO Committee provides advice on the projects for which a valid application has been submitted to the Ministerial Council for approval. The Committee is chaired by the Director-General of Bilateral

[95] Federal Public Service Foreign Affairs, Foreign Trade and Development Cooperation, Federal Public Service Finance. "FINEXPO VADEMECUM. August 2017, p.4.

[96] 'Concessionality level' refers to the fact that public buyers in developing countries do not have to repay the entire loan amount at market conditions. FINEXPO grants longer repayment terms to the buyer, or reduced interest rates and/or a grant. These concessional, or soft, conditions change every year since FINEXPO has to calculate the concessionality level of its financing instruments according to a reference rate determined by the OECD, the so-called Differentiated Discount Rate (DDR).

[97] The provision of state to state loans to Least Developed Countries and Heavily Indebted Poor Countries (HIPCs) must be untied to be in line with OECD agreements. The tied aid programme can operation in all developing countries.

Affairs (FPS Foreign Affairs). The Committee is composed of representatives from (not less than five!) federal administrations (including Development Cooperation), Credendo and three regional export agencies.

In some way FINEXPO can be considered Blended Finance 'avant la lettre', as it uses financial instruments with an ODA component to lever commercial trade and investments. However, there is no real development policy as to integrate this type of export promotion in an SDG framework. Moreover, with an institutional complexity of involvement of 5 federal administrations and 3 regional export agencies, it is not easy to come to a clear unified SDG oriented development mission. This complexity is probably also the main reason why FINEXPO did not change substantially after a 2010 evaluation. This evaluation revealed amongst others that FINEXPO was operating without clear guidelines regarding development relevance of project proposals and that these were not cross-checked with development strategies of countries involved. [98] Moreover it seems that, apart from the SME oriented financing instrument for innovative products, FINEXPO is benefiting mainly large companies with large projects.

Another limiting factor to use FINEXPO as a Blended Finance instrument is the fact that for most FINEXPO instruments local beneficiary/client must be a government institution or the like. Together with its complicated governance and its lack of SDG oriented policy, this makes that FINEXPO in its present form is difficult to use in an SDG inspired Blended Finance programme. The Dutch Good Growth Fund that has similar supporting instruments might be a good source of inspiration for a reform of the FINEXPO programme. (see ANNEX 4)

12.6 The Belgian Corporation for International Investment (BMI-SBI)

The Belgian Corporation for International Investment (BMI-SBI) is maybe the odd man out with respect to Blended Finance. BMI-SBI was established in 1971. BMI-SBI is a Limited Liability Company (S.A.). 63% of its shareholders' capital is held by the Belgian government through the Belgian Federal Participation and Investment Company and the National Bank of Belgium, while the remaining 37 % is held by banking institutions and other private companies.

According to its website BMI's mission is: "to provide medium- or long-term co-financing to business ventures made by Belgian private companies abroad. BMI-SBI supports projects that are of general economic interest, (to both Belgium and the host country), financially viable and that offer realistic prospects of profitability whilst respecting the principle of sustainable development and social corporate responsibility."

Although BMI is a member of EDFI, it has no SDG orientation. Its focus lies on assisting Belgian Companies in their investments. BMI-SBI can invest worldwide; its reach extends to emerging or developing countries as well as to countries in the industrialized world. BMI-SBI can invest in all sectors, but preference goes to investments in the industry sector. It invests through equity, quasi-equity (subordinated and convertible loans) and long-term loans.

It has a portfolio of EUR 37 million in 21 projects (end 2017). 99% is in equity while 1% is in loans. These figures show that it has never become an important player in the field. Moreover, since it withdrew from BIO as a shareholder, BMI has little or no commitment to development left. In theory it is an instrument in the hands of the Belgian Government that could be used to lever private equity investment in SDG relevant projects. In this respect however, it would compete with BIO and seen BMI's total lack of SDG orientation it is probably better to remove it from the Blended Finance radar (Its membership of EDFI is then also questionable).

[98] Special Evaluation Office of International Cooperation. "Evaluation of The Belgian Instruments in Support of Foreign Trade Eligible as Oda – FINEXPO". FPS Foreign Affairs, Foreign Trade and Development Cooperation. February 2011.

12.7 The Belgian Private Sector

Key in an institutional framework for Blended Finance is how the relation with the private (commercial) sector takes form. As Blended Finance involves the mobilisation of commercial finance towards SDGs in developing countries, a first step to take is to sensitise the private sector for SDG's and to make companies' policies' and ongoing investments contribute to SDGs. This was one of the objectives of the Belgian SDG Charter for International Development. The SDG Charter was a co-initiative of The Shift[99] and the Minister of Development Cooperation Alexander De Croo. It was launched in October 2016 and in the meantime signed by over a hundred organisations: private companies, social organisations and representatives of the public sector. The signatories commit themselves to sustainable and inclusive growth in Belgium and in developing countries where they work.

Other initiatives such as the "SDG Voices"[100] have tried to engage also other private sector organisations like VOB-FEB for SDGs. Much more can be done, amongst others by working more through federations of different sectors and regional platforms of the private sector (VOKA, UWE). The complex political structure of Belgium as a Federal State with three Regions and three Communities has made that powers regarding the private sector, are spread over different levels.[101] A coordinated policy to engage the private sector in SDGs is difficult as for instance most of the subsidies to the private sector are a regionalised matter.

Nevertheless, sensitising the private sector for SDGs remains a necessary step before specific effective Blended Finance facilities can be set up. These Blended Finance facilities need to build on the need of the private sector for support to invest in emerging markets and their interest to engage in SDG related investments. In that sense Blended Finance facilities should not only be demand driven locally (in the developing countries), but also respond to the need and interest of private partners in Belgium.

As mentioned in chapter 7 the private sector is diverse. It includes large companies and SMEs in the real economy, different actors in the financial sector such as banks, insurance companies, pension funds, private equity firms and asset/wealth managers. A special category are impact investors, that have both (often limited) profit-seeking and SDG impact in their DNA.

Different categories of the private sector have different needs as to lead them to SDG related investments and there are several regulatory issues that need to be solved before the private sector can engage in a Blended Finance set-up as we discussed in chapter 7.

The lowest hanging fruit for a Belgian Blended Finance facility would be to engage with private social lenders such as Alterfin or private impact investors such as Kampani (the only one of its kind in Belgium). They are already exclusively oriented towards SDGs and they have the mandate and the capacity, financially and operationally, to step into BF set-ups. Moreover, both Alterfin and Kampani invest in smallholder agriculture in developing countries (Kampani exclusively so).

When it comes to providing finance to producer organisations, Alterfin typically provides short term senior debt to pre-finance harvests and to a lesser extend longer term senior or collateralized investment loans. Kampani provides long term equity or quasi equity (so-called junior or uncollateralised and subordinated debt) for capital expenditure (heavy investments). It does so with small ticket sizes (between 100k and 500k EUR) which responds to a challenging funding need, referred to as the missing middle.

[99] The Shift is the Belgian Sustainability Network, bringing together private commercial and social sector and representatives from the public sector. Their objective is to realise the transition to a more sustainable society and economy

[100] https://www.sdgs.be/nl/sdg-voices

[101] The Regions have powers relating to the economy, employment, agriculture, water policy, housing, public works, energy, transport (except Belgian Railways), the environment, town and country planning, nature conservation, credit, foreign trade, supervision of the provinces, communes and intercommunal utility companies. Important is that they have also powers relating to international relations in those fields.

The risk-adjusted return of these investments is slim and often negative. That this is inherent for this type of investments has been demonstrated by the financial benchmarking report conducted by Dalberg.[102]

13 EU Blended Finance

13.1 Blended Finance according the EU

The EU defines Blending as "an instrument for achieving EU external policy objectives, complementary to other aid modalities and pursuing the relevant regional, national and overarching policy priorities. The principle of the mechanism is to combine EU grants with loans or equity from public and private financiers."[103] Starting point of this EU definition is more the blending of non-concessional finance with concessional finance or aid.

EU Blending foresees a grant element that can be used to attract additional financing for important investments in EU partner countries by reducing exposure to risk. On a case-by-case basis, the EU grant contribution can take different forms to support investment projects:

- Investment grant & interest rate subsidy - reducing the initial investment and overall project cost for the partner country
- Technical assistance - ensuring the quality, efficiency and sustainability of the project
- Risk capital (i.e. equity & quasi-equity) - attracting additional financing
- Guarantees - unlocking financing for development by reducing risk

At the moment it are mostly institutions, such as DFI's and development banks, that have successfully passed a Pillar Assessment[104], that have gained access to the EU BF facilities. Though apparently there is also the objective of giving direct access to private actors and create bigger leverage on the aid money.

13.2 EU Blending Facilities

Already in 2007, the EU started to put blending facilities in place. There are geographically and thematically oriented blending facilities. In 2016 the more comprehensive European External Investment Plan was launched

13.2.1 Geographic Blending Facilities

Under the responsibility of Directorate-General for International Cooperation and Development (DG DEVCO), we find two EU blending frameworks some of which were later integrated in the European External Investment Plan. One is the Development Cooperation Instrument (DCI) Blending Framework, that has blending facilities for Latin-America (LAIF), Asia (AIF) and Central Asia (IFCA). The second blending framework is the European Development Fund (EDF) Blending Framework, with facilities for Africa (AfiF and EU-ITF), for Caribbean (CIF) and for Pacific (IFP).

[102] Dalberg. 'CSAF Financial Benchmarking'. Final Learning Report, July 2018. Retrieved from: https://www.agrilinks.org/sites/default/files/usaid_-_csaf_financial_benchmarking_final_learning_report.pdf
[103] https://ec.europa.eu/europeaid/policies/innovative-financial-instruments-blending_en
[104] Under indirect management the Commission can entrust budget implementation tasks to certain countries, organisations and bodies (further referred to as 'Entities'). These entities must meet requirements in up to seven areas relating to the internal control system, the accounting system, an independent external audit and rules and procedures for providing financing from EU funds through grants, procurement and financial instruments and Sub-Delegation.

Under the responsibility of Directorate-General for Neighbourhood and Enlargement Negotiations (DG NEAR), we find also two Blending Frameworks: the European Neighbourhood Instrument (ENI) Blending Framework[105] and the Instrument for Pre-Accession Assistance (IPA) Blending Framework.

The first beneficiaries of these blending facilities are the pillar assessed institutions (DFI's, development banks, …), though also actors in the private sector are directly targeted.

From the end of 2016 onwards, Geographical Blending Facilities for Africa and the Neighbourhood countries have become part of the new European External Investment Plan (see 13.2.3) and are operated under the EEIP regulation.

13.2.2 Thematic Blending Facilities

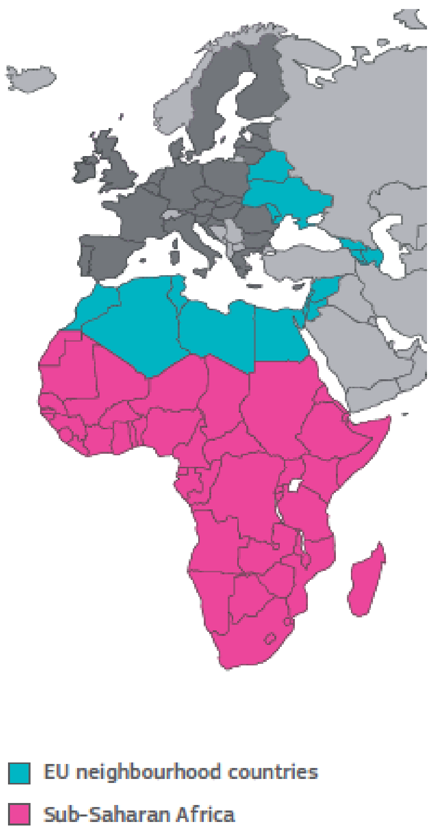
More recently two thematic blending facilities were set-up, with special focus on inclusive and sustainable private sector development:

- Electrification Financing Initiative (ElectriFI) aims at accelerating access to electricity and modern energy services through intervention at the development stage of a project.
- Agriculture Financing Initiative (AgriFI)'s objective is to unlock, accelerate and leverage investments with a value chain approach focusing on smallholder's inclusiveness and/or MSME agri-business.

Both ElectriFi (2016) and AgriFi (2018) are managed by EDFI Management Company (EDFIMC)[106]. In contrast to the geographical blending facilities, thematic blending facilities can finance directly private partners. The AgriFi product sheet mentions that it targets existing private sector enterprises working with smallholder farmers on financially, environmentally and socially sustainable projects with potential to scale. That this concept with a minimum threshold amount of half million euro is a workable concept has still to be proven.

[105] NIF projects operate in the following Neighbourhood partner countries: Eastern Neighbourhood region: Armenia, Azerbaijan, Georgia, Republic of Moldova, Ukraine as well as regional east-wide projects. Southern Neighbourhood region: Egypt, Jordan, Lebanon, Morocco, Palestine, Tunisia as well as regional south-wide projects.
[106] EDFIMC is an asset management company established in 2016 on behalf of EDFI's members, as a full subsidiary of the EDFI Association in Brussels.

13.2.3 The European External Investment Plan



In 2016 the European External Investment Plan (EEIP) was set up. According the European Commission: "The EEIP provides, for the first time, a coherent overall framework to improve investment in Africa and the Neighbourhood, in order to promote sustainable investment and tackle some of the root causes of migration. It will do so by leveraging funds from the EU, its Member States, other donors, financial institutions and the private sector." [107]

The driving factor of this Investment Plan is 'to tackle some of the root causes of migration', which of course can be compatible with reaching SDGs. However, in part the EEIP is old wine in a new bottle as it integrates (and strengthens) the already previous existing African and Neighbourhood Blending Facilities (see above).

The EEIP has three pillars: Financing, Technical Assistance and Investment Climate.

The first pillar is financing: the European Fund for Sustainable Development (EFSD) is composed of the two Regional Investment Platforms (Africa and the Neighbourhood). It manages the already existing regional investment facilities and the new EFSD guarantee that has five thematic investment "windows", under which guarantees will be provided.[108] Together with some member state contributions the EFSD has a budget of € 4,1 billion of which € 2,6 billion for the already existing regional investment platforms and € 1,5 billion for the new guarantee facility. In theory direct access by private actors is possible and substantial leverage of aid money can be achieved. For the moment there is not yet much evidence that this is indeed the case.

The EFSD guarantee is very broad, in the sense that in can mitigate different types of risks: commercial risks–losses due to a borrower or counterparty failing to meet its obligations in accordance with agreed terms (e.g. payment risk, performance risk, etc.) ; political and country risk–all risks relating to actions of a state or a government, over which the investors have no influence (e.g. expropriation, coup d'état, civil war, legal and regulatory risk) ; currency risks–potential losses due to fluctuations, convertibility, transferability and exchange rates ; and climate change and environmental risks (e.g. droughts, flooding, extreme weather events, temperature rises, etc). [109]

The second pillar of the EEIP is stepping up technical assistance and help beneficiaries to develop financially attractive and mature projects.

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[107] European Commission Fact Sheet. State of the Union 2016: European External Investment Plan: Questions and Answers, Strasbourg, 14 September 2016. And REGULATION (EU) 2017/1601 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 September 2017
establishing the European Fund for Sustainable Development (EFSD), the EFSD Guarantee and the EFSD Guarantee Fund.
[108] On 23 November 2017 the European Commission approved 5 investment windows or priority investment areas: Sustainable Energy and Connectivity, Micro, Small and Medium Sized Enterprises (MSMEs) Financing, Sustainable Agriculture, Rural Entrepreneurs and Agribusiness Sustainable Cities, Digital for Development.
[109] EC. "Your guide to the EU External Investment Plan". Release N°1, November 2017.

The third pillar of the EEIP is about improving the investment climate and business environment in EU partner countries, with EU Delegations playing a key role, notably through: Structured dialogues with businesses at country, sector and strategic levels, including through the promotion of European and local business fora; Policy and political dialogues with partner governments to address key constraints to investment and promote good governance; Support to regulatory, policy and governance reforms building upon market, sector and value-chain intelligence at country level.[110]

With the European External Investment Plan, the European Commission has set in place a comprehensive Blended Finance programme. Both ENABEL and BIO could benefit from this programme. A coordinated policy how this would fit in a Belgian Blended Finance policy would then also be appropriate.

[110] ibid

ANNEXES

ANNEX 1. The Addis Ababa Action Agenda

The third international conference on Financing for Development in Addis Ababa (July 2015) agreed on a global framework for financing development. The conference agreed that the post-2015 development agenda needed increased finance, both local and international and that private financial flows have to be boosted in order to contribute to ambitious development goals. (The Sustainable Development Goals had yet to be approved in September 2015.) Domestic and international private business and finance were earmarked as an area for action.[111] Blended Finance in particular was mentioned as an important way of resource mobilisation in this area. Below we quote the relevant paragraphs 43, 48 and 54. (bold is ours)

"*Paragraph 43 - We also recognize the potential of new investment vehicles, such as development-oriented venture capital funds, potentially with public partners,* ***blended finance****, risk mitigation instruments, and innovative debt funding structures with appropriate risk management and regulatory frameworks. We will also enhance capacity-building in these areas*

*Paragraph 48 - We recognize that both public and private investment have key roles to play in infrastructure financing, including through development banks, development finance institutions and tools and mechanisms such as public-private partnerships***, blended finance, which combines concessional public finance with non-concessional private finance and expertise from the public and private sector, special-purpose vehicles, non-recourse project financing, risk mitigation instruments and pooled funding structures***.* ***Blended finance*** *instruments including public-private partnerships serve to lower investment specific risks and incentivize additional private sector finance across key development sectors led by regional, national and subnational government policies and priorities for sustainable development. For harnessing the potential of* ***blended finance*** *instruments for sustainable development, careful consideration should be given to the appropriate structure and use of* ***blended finance*** *instruments.*

Projects involving ***blended finance****, including public-private partnerships, should share risks and reward fairly, include clear accountability mechanisms and meet social and environmental standards. We will therefore build capacity to enter into public-private partnerships, including with regard to planning, contract negotiation, management, accounting and budgeting for contingent liabilities. We also commit to holding inclusive, open and transparent discussion when developing and adopting guidelines and documentation for the use of public-private partnerships, and to build a knowledge base and share lessons learned through regional and global forums.*

Paragraph 54 - An important use of international public finance, including ODA, is to catalyse additional resource mobilization from other sources, public and private. It can support improved tax collection and help to strengthen domestic enabling environments and build essential public services. It can also be used to unlock additional finance through ***blended or pooled financing*** *and risk mitigation, notably for infrastructure and other investments that support private sector development.*"

[111] "Addis Ababa Action Agenda of the Third International Conference on Financing for Development". United Nations, New York, 2015, p. 17.

ANNEX 2. The 17 sustainable development goals (SDGs)

Goal 1	End poverty in all its forms everywhere
Goal 2	End hunger, achieve food security and improved nutrition and promote sustainable agriculture
Goal 3	Ensure healthy lives and promote well-being for all at all ages
Goal 4	Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all
Goal 5	Achieve gender equality and empower all women and girls
Goal 6	Ensure availability and sustainable management of water and sanitation for all
Goal 7	Ensure access to affordable, reliable, sustainable and modern energy for all
Goal 8	Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all
Goal 9	Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation
Goal 10	Reduce inequality within and among countries
Goal 11	Make cities and human settlements inclusive, safe, resilient and sustainable
Goal 12	Ensure sustainable consumption and production patterns
Goal 13	Take urgent action to combat climate change and its impacts
Goal 14	Conserve and sustainably use the oceans, seas and marine resources for sustainable development
Goal 15	Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss
Goal 16	Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels
Goal 17	Strengthen the means of implementation and revitalize the global partnership for sustainable development

For more detail see: https://sustainabledevelopment.un.org/

ANNEX 3. TCX

The Currency Exchange Fund ('TCX')[112] was founded in 2007 by a group of development finance institutions (DFIs), specialized microfinance investment vehicles (MIVs) and donors to offer solutions to manage currency risk in developing and frontier markets. The Government of Netherlands, though the Minister for Development Cooperation, and the German Government, through the Federal Ministry for Economic Cooperation and Development (BMZ) and the Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety (BMU), are the anchors of the fund as they provided support in the form of subordinated convertible debt, and a first loss loan. They were followed by 21 more investors, most of them DFI's, MDBs, bilateral development departments and impact investors. [113]

TCX focuses on providing currency solutions for its investors. These have accounted for over 90% of the volumes transacted by TCX to date. This means that you have to invest in the TCX fund in order to receive the benefits of its services. As the minimum threshold investment (USD 5 million) was quite considerable for some of the development investors, they pooled funds together in the American MFX fund, that in its turn invested in TCX and this way MFX got access to the TCX services for its members. Another advantage of the MFX fund is that it received guarantee facilities from OPIC and FMO, which made it possible for MFX to trade on favourable terms with TCX and commercial banks, while minimizing MFX's liquidity requirements. The OPIC guarantee is the key reason MFX can trade on attractive collateral terms with its clients.

The solutions that TCX is offering, consist of financial instruments – swaps & forward contracts – that enable TCX's investors and clients to provide their borrowers with financing in their own currency, while shifting the currency risk to TCX. The fund operates on the basis of the following principles:

- additionality: providing solutions where markets are thin or inexistent;
- risk-reflective pricing: price in accordance with prevailing market rates and methodologies;
- non-speculation: only hedge actual underlying exposure to the real economy.

After 10 years of operations TCX has converted USD 4 billion of development finance loans into 54 local currencies across 5 regions globally. 67% of the financing was situated in LDCs, other low-income and lower-middle income countries. Most of the financing went to microfinance (64%) and SME finance (17%).[114]

However, what is not clear from the 10-year evaluation study of TCX, is how much commercial funding was generated through the TCX facility. All in all, this seems to be rather limited as most of its investors are DFIs or MDBs. The only "commercial" funding was probably mobilised through the impact investors and MFX. The main contribution of TCX lies in the fact that it has supported local financial markets by making it possible for local MFIs and other financial institution to borrow in local currency abroad, and thus solve in part the problem of the "original sin", that says that most (developing). countries cannot borrow in their own currency.

[112] Most information is taken from: https://www.tcxfund.com/ and from: http://mfxsolutions.com/

[113] Present investors are: Ministry of Foreign Affairs (Netherlands), BMZ, BMU, EBRD, FMO, KfW, EIB, JBIC, AFD, IFC, AFDB, IADB, DBSA, OFID, BIO, MFX, Proparco, EFSE, COFIDES, Oikocredit, ASN Novib, Oxfam Novib, Blue Orchard MF, Fondation GCA

[114] "The development impact of local currency solutions, An evaluation of 10 years TCX". TCX – Carnegie Consult, 2017. Retrieved from: https://www.tcxfund.com/wp-content/uploads/2017/10/Impact-report-TCX-10Y.pdf

Figure Annex 3-1 TCX hedging by region

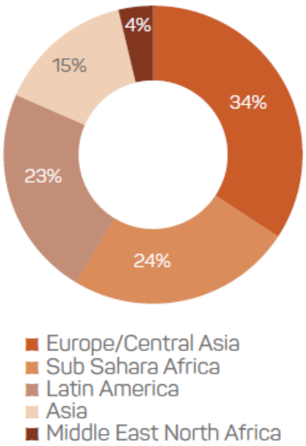
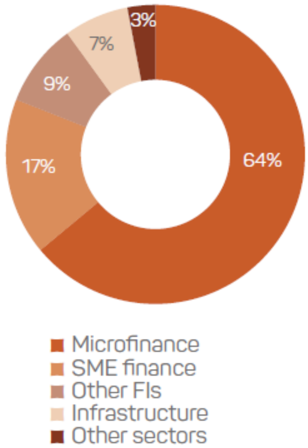


Figure Annex 4 2 TCX hedging by sector



Source: "The development impact of local currency solutions, An evaluation of 10 years TCX". TCX – Carnegie Consult, 2017. Retrieved from: https://www.tcxfund.com/wp-content/uploads/2017/10/Impact-report-TCX-10Y.pdf

ANNEX 4. DGGF: An Inspiring Programme for Blended Finance

In 2014 the Dutch Good Growth Fund (DGGF) did not start as an explicit blended finance initiative, but it created an interesting environment for a) stimulating the Dutch private sector to invest in and to trade with 68 developing countries and emerging markets and for b) investing in local SMEs through intermediary funds. DGGF strengthens and brings together instruments that previously existed but lacked the development focus.[115]

DGGF overarching goals and outcomes

DGGF's overarching goals fall under three overall **policy goals** of the Dutch government on trade and aid:

1. Poverty reduction
2. Sustainable and inclusive economic growth
3. Success for Dutch SMEs in international markets

DGGF also has an additional "intermediary" goal of financial sector development. DGGF aims to reach these goals by supporting transactions and investments by Dutch and local SMEs that contribute to the development of the local economy and the following **outcomes**:

1. Employment growth: Increasing direct and indirect employment in low- and middle-income countries
2. Knowledge transfer: The sustainable transfer of knowledge, skills and techniques
3. Production capacity growth: Increasing the production capacity of the local industry

DGGF aims to achieve these outcomes by addressing the **financing gap** that prevents Dutch and local SMEs from these without additional financial support, addressing the 'missing middle' in developing countries – local SMEs that have outgrown microfinance but have not secured regular financial services.

The programme gives special attention to young and female entrepreneurs and entrepreneurs in fragile states. The underlying assumption is that entrepreneurs from these groups typically have more difficulty with obtaining access to finance. DGGF also measures employment growth specifically for youth, women and in fragile states, but these are not explicit target groups.

DGGF tracks and investments

DGGF employs several instruments to deliver the above results. The Fund covers three separate tracks, each of which has its own scope, financing mechanism and strategy. DGGF also funds technical assistance (TA) to Dutch and local SMEs and Intermediary Funds (Ifs) across all three Tracks.

- Track 1 offers financing to Dutch SMEs to enable them to invest in DGGF countries, where Dutch SMEs face funding constraints to investing in developing countries. Netherlands Enterprise Agency (RVO) is the fund manager and offers different types of financing, ranging from loans to guarantees, as well as combinations of both. In addition to financing, Track 1 offers TA to SMEs. Projects should have a positive overall impact on (direct and indirect) employment generation, production capacity and knowledge transfer. Specific target groups are female and young entrepreneurs and entrepreneurs in fragile states.
- Track 2 aims to increase access to finance for local SMEs by investing in Intermediary Funds (IFs) and financial institutions in DGGF countries. Track 2 specifically targets the so-called 'missing middle' which consists of small and medium-sized entrepreneurs who do not have access to the right type of finance. It is a fund-of-funds managed by PwC and Triple Jump. DGGF invests in existing or new IFs. These IFs in turn offer a variety of customised financing to SMEs. The Seed

[115] Information was retrieved from https://www.dggf.nl/ and was obtained from the "EXTERNAL EVALUATION FINAL BASELINE REPORT". DGGF, Ministry of Foreign Affairs, the Netherlands, 15 August 2018.

Capital and Business Development (SC&BD) programme complements track 2 services and includes: financing technical assistance and business development services for IF clients; testing new financing concepts and strengthening institutional capacities and infrastructure; sharing knowledge built; building international ESG, tax and impact measurement capacity.

- Track 3 offers export credit insurance and export financing to Dutch SMEs wanting to export capital or investment goods to DGGF countries. Atradius Dutch State Business (ADSB) is the implementing agency. DGGF offers export credit insurance for export transactions that do not qualify for the regular export credit insurance offered by ADSB, for example, due to high country risk and payment risk. ADSB also offers export financing when banks are not willing to provide any, thereby filling a financing gap.

In addition to the above, each track has access to a budget for TA, which in total amounts to €70 million for all tracks combined. These are available to Dutch or local SMEs (tracks 1 and 3) or to IFs (track 2) which can in turn then train local SMEs. TA is available for a variety of reasons including: the exchange of knowledge; development of new financial concepts (local); institutional strengthening of IFs (local); catalysing financial infrastructure improvements (local); promotion of international ESG and tax standards; and, the promotion of impact measurement.

68 Target Countries

The Dutch Good Growth Fund is available for 68 developing countries and emerging markets. Fragile countries are marked with an F. Afghanistan (F) Albania Algeria Angola Armenia Bangladesh Benin Bhutan Bolivia Bosnia Herzegovina (F) Burkina Faso Burundi (F) Cambodia Cape Verde Colombia Congo Dem. Rep. (F) Djibouti Egypt Eritrea (F) Gambia Ethiopia Georgia Ghana Guatemala Guinee India Indonesia Jordan Kenya Kosovo (F) Liberia (F) Libya (F) Laos Macedonia Madagascar (F) Malawi (F) Maldives Mali (F) Morocco Moldova Mongolia Mozambique Myanmar (F) Nepal (F) Nicaragua Niger Nigeria Pakistan Palestinian Territories (F) Philippines Peru Rwanda Sierra Leone (F) Sao Tome Senegal Somalia (F) South Africa South Sudan (F) Sri Lanka Suriname Tanzania Tunisia Thailand Uganda Vietnam Yemen (F) Zambia Zimbabwe (F).

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Wet van 23 November, 2017 - Wet tot wijziging van de naam van de Belgische Technische Coöperatie en tot vaststelling van de opdrachten en de werking van Enabel, Belgisch Ontwikkelingsagentschap

Wet van 25 Oktober 2018. - Wet tot wijziging van de wet van 3 november 2001 tot oprichting van de Belgische Investeringsmaatschappij voor Ontwikkelingslanden en van de wet van 23 november 2017 tot wijziging van de naam van de Belgische Technische Coöperatie en tot vaststelling van de opdrachten en de werking van Enabel, Belgisch Ontwikkelingsagentschap

Koninklijk besluit houdende goedkeuring van het eerste beheerscontract tussen de Federale Staat en de naamloze vennootschap van publiek recht met sociaal oogmerk Enabel, Belgisch Ontwikkelingsagentschap

Bijkomende Overeenkomst bij het eerste Beheerscontract tussen de Belgische Staat en de Naamloze Vennootschap van Publiek recht "Belgische Investeringsmaatschappij voor Ontwikkelingslanden" (BIO; December 20th, 2016

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