

SCALING UP BLENDED FINANCE IN DEVELOPING COUNTRIES

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Abstract

This paper was prepared at the request of the Indonesian G20 presidency. It presents an overview of the current state of blended finance in developing countries, with a focus on least developed countries (LDCs) and small island developing states (SIDS). It assesses opportunities and constraints on the way to mobilising the amounts needed to deliver on the 2030 Agenda and leave no one behind.

Foreword

In recognition of the potential of blended finance to help fill the SDG financing gap, a number of international efforts are under way to define, standardise and guide good practices in that area. However, current flows remain low, in particular to the least developed countries (LDCs) and small island developing states (SIDS), as well as in social sectors.

In this context, Indonesia has led the development of *G20 Principles to Scale up Blended Finance in Developing Countries, including Least Developed Countries and Small Island Developing States* (hereinafter 'G20 Principles'), and related implementation guidance. The G20 Principles were formally agreed by the G20 Development Working Group (DWG) in September 2022. This work is a contribution to the G20 Framework on Finance for Sustainable Development, endorsed in 2020, and builds on the work undertaken by the Italian G20 presidency on innovative financing instruments.

The OECD has supported this process with data and analysis, aiming to help increase blended finance flows in developing countries, across country contexts, sectors and themes. This Stocktake Report thereby served as an analytical basis which informed discussions within the G20 DWG and which led to the development of the *G20 Principles*. It points to the need for dialogue and consultations with developing countries, including LDCs and SIDS, and private sector stakeholders, as a way to enhance ownership, and prepare policy changes that can lead to the improvement of blended finance approaches.

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This report benefitted from insights gathered in consultations with a variety stakeholders. These were launched by a meeting jointly convened by the OECD and Indonesia on 15 December 2021, which introduced the programme of work on scaling up private and blended finance in developing countries, including the least developed countries (LDCs) and small island developing states (SIDS) in the context of the G20 Development Working Group (DWG).

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Executive Summary

Blended finance is the strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries. While only one element in the toolbox for Financing for Sustainable Development (FfD), it is an effective approach that leverages development finance to mobilise commercial finance. By deploying development finance in a way that addresses investment barriers and improves the risk-return profile of investments, blended finance operates as a market-building instrument that helps to attract commercial finance for the Sustainable Development Goals (SDGs).

Despite existing efforts and agreed Principles, blended finance flows are not yet holding up to expectations. Alongside a broader array of efforts by the G20 Development Working Group (DWG) under Indonesia's presidency, this Stocktake Report draws attention to a three-dimensional gap in blended finance efforts, including:

- Missing blended finance policy and practitioner frameworks on how developing countries, including Least Developed Countries (LDCs) and Small Island Developing States (SIDS) can engage more effectively in attracting, deploying and scaling blended finance;
- Need for additional insights and guidance on how to scale up blended finance in the context of social sectors, and
- Lack of implementation and capacity challenges that impedes blended finance flows reaching scale in developing countries, including in LDCs and SIDS.

This report identifies several entry points, or action areas, for developing country governments, including in LDCs and SIDS, to scale up blended finance. They may underpin and inform the *G20 Principles to Scale up Blended Finance in Developing Countries, including Least Developed Countries (LDCs) and Small Island Developing States (SIDS)* and accompanying guidance tools. These entry points for blended finance actors and policymakers, both at policy-level and at operational-level, fall into four broad areas:

1. Target blended finance solutions to local contexts and employ blended finance to catalyse finance in the last mile of commercial profitability

There is a need for building inclusive capital markets, including greater local currency investment, for mobilising private sector investment in developing countries, including the LDCs and SIDS, through public and regulatory reform, enhanced local ownership and capacity building.

- Use blended finance to add value to local development priorities, and be aligned with local financing priorities.
- Choose target sectors for blended finance carefully, and ensure that project attributes and context, such as financial sustainability, are taken into account.

2. Support domestic financial systems and market development

For the greatest impact, and to reach the most vulnerable and underserved communities, blended finance operations must be designed to respond to local needs and realities from the very outset. Effective and meaningful dialogue and engagement with local development partners and beneficiaries is therefore crucial for ensuring developing country, including LDC and SIDS perspectives, are well represented within blended finance plans. Aligning blended finance with integrated national financing frameworks (INFFs) offers entry points for achieving this. Furthermore, it is key to improve international development partners' knowledge and understanding with respect to market structure, regulations, institutions and local political economy dynamics within developing countries, including LDCs and SIDS, for sustainable and informed decision-making. This is especially important for mapping SDG investment opportunities and target sectors.

- Ensure that a conducive institutional, policy and regulatory framework to scale up blended finance is in place.
- Enable local actors to engage in blended finance transactions, including to mobilise themselves.
- Build local capacities and create the ecosystem beyond a transaction-based approach.

3. Aim for scale through systemic and transformational approaches.

To contribute to building stronger, more resilient and sustainable economies in developing countries, including in the LDCs and SIDS, blended finance needs to be aligned with the broader policy context of multilateral crisis response and national recovery plans. Portfolio approaches, de-risking facilities and increased ticket size (such as through aggregating projects) are important avenues for mobilising private investment to scale through blended finance in LDCs, SIDS and social sectors. To achieve such systemic and transformative change, effective collaboration among stakeholders across the public and private sectors is a necessary condition.

- Ensure that a pipeline of projects stands ready to attract blended finance.
- Facilitate portfolio and programmatic approaches to unlock private finance at scale.
- Promote multi-stakeholder coordination while respecting all parties' mandates.

4. Improve impact management and measurement, and promote transparency

Impact management and measurement are at the core of successful and responsible blended finance operations. Hence, developing impact and results measurement frameworks are important elements for effective engagement of financiers, governments, and development partners. Transparency and accountability are also key to providing investors with a deeper understanding of risk and return expectations. Furthermore, transparency promotes a culture of learning and knowledge sharing of best practices, which will contribute to a track record and increase donors as well as investors' confidence in blended finance.

- Enable an understanding of the why, where and how of blended finance, including through sound monitoring and evaluation systems.
- Promote transparency and accountability on blended finance operations.

Abbreviations

AAAA	Addis Ababa Action Agenda
ABDE	Associação Brasileira de Desenvolvimento
ADB	Asian Development Bank
AFD	French Development Agency
AICS	Italian Agency for International Cooperation
AIIB	Asian Infrastructure Investment Bank
AUM	Assets under management
B2B	Business to business
BMZ	Federal Ministry of Economic Cooperation and Development, Germany
CAF	Development Bank of Latin America
CDP	Cassa Depositi e Presiti, Italy
CFR	Country Financing Roadmaps
CIV	Collective investment vehicle
CRS	Creditor Reporting System
DAC	OECD Development Assistance Committee
DFC	Development Finance Corporation
DFI	Development finance institution
DWG	G20 Development Working Group
EAIF	Emerging Africa Infrastructure Fund
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
EC	European Commission
EFSD	European Fund for Sustainable Development
ESG	Environmental, Social and Governance
EU	European Union
FAO	Food and Agriculture Organisation
FCDO	Foreign, Commonwealth and Development Office
FfD	Finance for Sustainable Development
FMO	Entrepreneurial Development Bank (Netherlands)
FONGIP	Senegalese Central Guarantee Fund
EU	European Union
G7	The Group of Seven

IFC	International Finance Corporation
INFF	Integrated national financing frameworks
KES	Kenyan shilling
LDC	Least Developed Country
LIC	Low-income country
LMIC	Lower-middle income country
LSE	London Stock Exchange
MCPPI	Managed Co-Lending Portfolio Program
MDB	Multilateral development bank
MIC	Middle-income country
MSME	Micro, small and medium-sized enterprises
NDB	National development bank
NDF	Natural Disaster Fund
NSE	Nairobi Securities Stock Exchange
PIDG	Private Infrastructure Development Group
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OPIC	Overseas Private Investment Corporation
PFI	Policy Framework for Investment
SDIP	Sustainable Development Investment Partnership
SIDS	Small Island Developing States
SME	Small and medium-sized enterprises
SNA	System of National Accounts
SPV	Special purpose vehicle
TA	Technical assistance
THK	Tri Hita Karana
TOSSD	Total Official Support for Sustainable Development
UCCRTF	Urban Climate Change Resilience Trust Fund
UMIC	Upper-middle income country
UNCDF	United Nations Capital Development Fund
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
USD	United States Dollar

1 Blended finance in the international financing for sustainable development landscape

Blended finance – the strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries (OECD, 2018^[1]) – is an effective approach that leverages development finance to mobilise commercial finance. By deploying development finance in a way that addresses investment barriers and improves the risk-return profile of investments, blended finance operates as a market-building instrument that helps to attract commercial finance for the Sustainable Development Goals (SDGs). For further insights in the concept of blended finance, including its instruments and actors, please refer to the Annex.

Blended finance has become an established pillar of the financing for sustainable development landscape, which started with the adoption of the Addis Ababa Action Agenda (AAAA) in 2015 (United Nations, 2015^[2]). The agenda constitutes the framework for international action on Finance for Sustainable Development (FfD). The FfD sets out principles for harnessing the potential of blended finance. For example, it stipulated that careful consideration should be given to the appropriate structure and use of blended finance instruments. Furthermore, projects involving blended finance, including public-private partnerships, should share risks and rewards fairly, include clear accountability mechanisms and meet social and environmental standards¹. In conjunction with the SDGs, the agenda provides a clear direction as to how blended finance can help to finance development impact and ultimately eradicate poverty. Importantly, blended finance is only element in the toolbox for FfD, and will not be able to solve the myriad of challenges in bridging the SDG investment gap. For example, particularly in sectors concern global public goods, government funding and official development assistance (ODA) will continue to be a major source of funding.

Recognising the importance of international action on Blended Finance in support of the FfD, the Tri Hita Karana Roadmap (THK) for Blended Finance, which was launched in 2018 by Indonesia, represents a multi-stakeholder platform for formulating shared values and guidance on scaling up blended finance in support of the SDGs (OECD, 2017^[3]). At the outset, actors from the public and private sector came together under leadership of Indonesia and the OECD to develop a common set of values to ensure high quality blended finance transactions and efforts². Complementing this set of values, the THK has identified action areas to scale up blended finance in quantity and quality, including to translate the values into good practices; mobilisation drivers such as incentives and standardisation; address transparency issues and opportunities, as well as specificities in the enabling environment with a particular focus on working with local actors such as national development banks, and with respect to impact measurement and management. These action areas have been taken forward by dedicated working groups that continue to develop guidance material available (Convergence, 2022^[4]). The THK's community platforms and its activities to create mutual understanding, build capacity and strengthen technical assistance are examples of multi-stakeholder approaches to scale up blended finance.

The THK Roadmap builds on efforts by different actors in blended finance that have developed actor-specific principles and guidance to ensure a standardised and high-quality approach to blended finance, such as the OECD's Development Assistance Committee (DAC) and the development finance institutions (DFIs).

In 2017, OECD DAC members adopted five *Blended Finance Principles for Unlocking Commercial Finance for the Sustainable Development Goals* (OECD, 2021^[5]). In line with the development mandate of DAC members, these principles aim to maintain high standards and achieve development effectiveness, and are a tool for donor governments, multilateral donors, development co-operation agencies, philanthropies and other stakeholders. The Principles also highlight the importance of monitoring blended finance for transparency and results in order to build an evidence base for blended finance operations. To guide the application of the principles in development co-operation action, a complementing guidance note has been published (OECD, 2021^[5]). For each of the five principles, a how-to-guide, including a checklist for all providers of development finance, including good practices for different policy areas, has been developed.

Moreover, the *DFI Working Group Enhanced Principles on Blended Concessional Finance for Private Sector Projects* (DFI Enhanced Principles) have been adopted by the major MDBs, i.e. the African Development Bank (AfDB), the Asian Development Bank (AsDB), the Asian Infrastructure Investment Bank (AIIB), the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), the Inter-American Development Bank Group (IDBG), the Islamic Corporation for the Development of the Private Sector (ICD), and the European DFIs (EBRD, 2013^[6]); (IFC et al., 2017^[7]). These principles frame good practices of the MDB/DFI operations with respect to the level of additionality, minimum concessionality, and commercial sustainability, among others.

1.1. Policy gaps to scaling blended finance in developing countries, including the LDCs and SIDS

Despite existing efforts and agreed Principles in the field of blended finance, the flows are not yet holding up to expectations. Blended finance remains a small segment of the global financing for sustainable development landscape, next to ODA and total official support for sustainable development (TOSSD), as well as private flows such as FDI, remittances, etc. (see Annex: The foundations of blended finance).

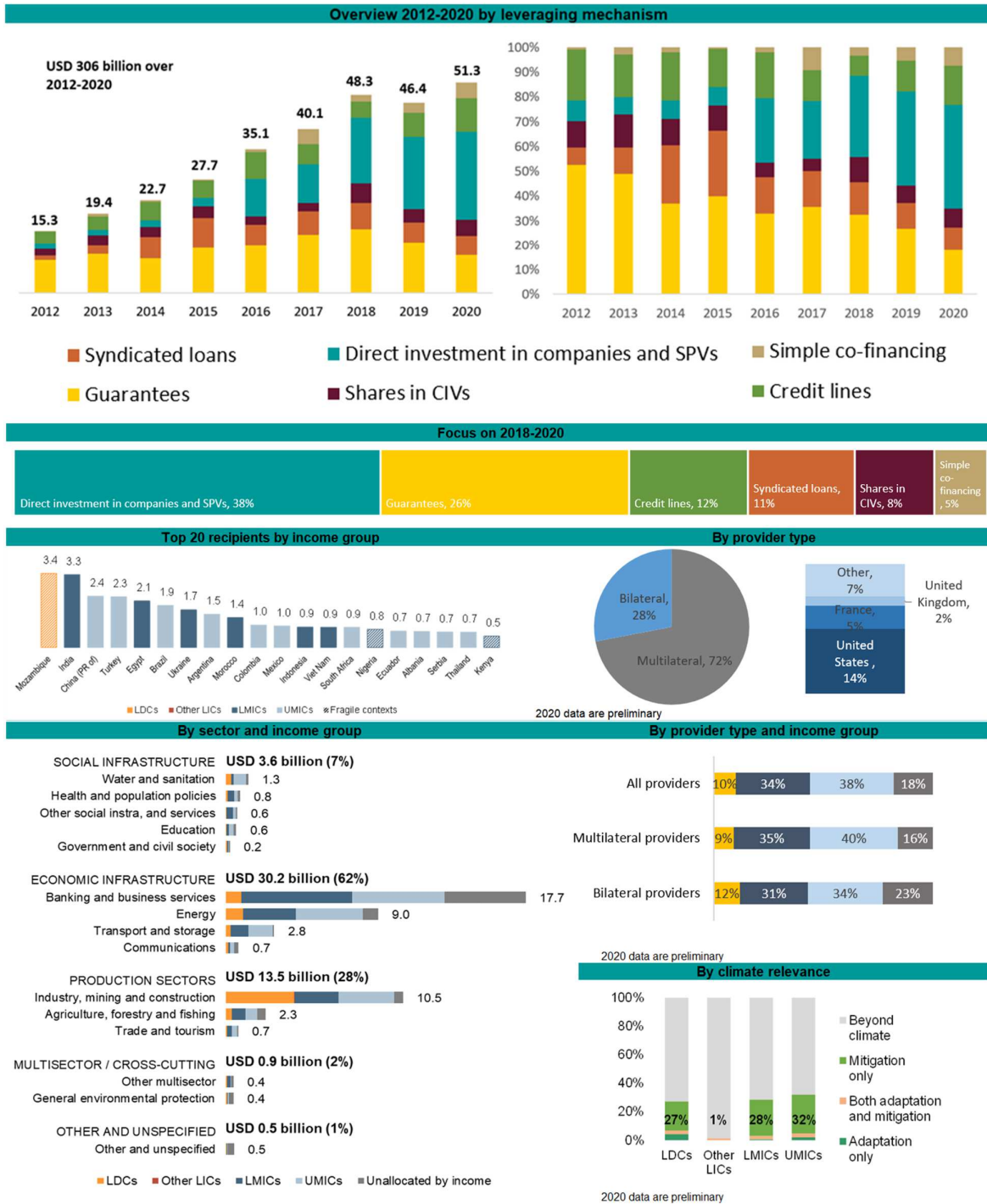
The COVID-19 pandemic exacerbated the financing gap for the implementation of the 2030 Agenda in developing countries, estimated at USD 3.9 trillion in 2020 (OECD, forthcoming^[8]). Compared to pre-pandemic years, it was estimated to amount to USD 2.5 trillion (UNCTAD, 2020^[9]). Shifting only a fragment of the assets held by institutional investors worldwide – over USD 100 trillion in 2019 – towards sustainable activities in those countries would be enough to fill that gap (OECD, 2021^[10]).

Despite the growing needs, blended finance has not reached the scale needed to significantly contribute to filling this gap, let alone in LDCs and SIDS. Rather, blended finance flows, as proxied by the amounts mobilised from the private sector by official development finance interventions, are showing a decreasing trend even pre-COVID-19, amounting to USD 48 billion on average per year in 2018-2020 (see Figure 1.1), with only 15% mobilised in LDCs (see Annex for further data on blended finance).

The contrast between the established policy landscape and the sobering figures points to a significant gap between what is available and what is needed to scale blended finance in developing countries, including LDCs and SIDS. Alongside a broader array of efforts by the G20 DWG under Indonesia's presidency, this Stocktake Report aims to draw attention to that gap, which is identified to be three-dimensional.

First, established blended finance policy and practitioner frameworks are largely focusing on providing guidance and standards to donors or development finance providers, with less emphasis on how developing countries, including LDCs and SIDS, can engage more effectively in attracting, deploying and scaling blended finance. Additionally, some MDBs and DFIs do not necessarily include LDCs among their countries of operation. Yet, developing countries and in particular, LDCs and SIDS, ought to be the target countries for any blended finance transaction, where SDG investments are most needed. Partner governments should hence be enabled to take an active role in attracting or developing blended finance transactions, building local capital markets with the help of blended finance transactions, and work closely together with local public and private actors. Respective blended finance standards and guidance are not available at this stage.

Figure 1.1. Private finance mobilised by official development finance interventions in developing countries



Source: (OECD, 2022_[11])

Secondly, current blended finance flows are mainly targeting sectors where the business case for private investors is clear, including energy and banking (see Figure 1.1 and Annex). At the same time, in many developing countries, including in LDCs and SIDS, social sectors are underfunded, which constitutes a structural impediment to achieving the SDGs. Thus, additional insights and guidance on macroeconomic fundamentals, governance, regulatory framework, infrastructure, market characteristics and others, and at an operational level on contract risks, costly and time-consuming pipeline origination and project preparation, high transaction cost due to small deal size, untested business models, and information and data gaps, are needed to scale blended finance in the context of social sectors and other as well as oftentimes related development priorities such as promoting agri-MSMEs. Blended finance hence should operate as a financial tool that allows developing countries, including LDCs and SIDS, to increase the finance available in areas where it is needed most³.

Thirdly, implementation and technical capacity challenges may impede blended finance flows reaching scale in developing countries, including LDCs and SIDS. While the concept of blended finance and principles may be increasingly established in the international community, awareness and understanding in developing countries is still limited (Taskin, Bellesi and Moller, 2020_[12]). Additionally, the all-important ‘how-to’ guidance for developing country actors is still missing. Any set of standards focusing on the developing country perspective should be complemented with actionable take-aways, capacity building and institutional support (see Chapter 3).

The G20’s DWG is well placed to conduct and endorse work that adds value to the three gaps identified given its interest in and mandate to foster sustainable development in developing countries, including LDCs and SIDS. This paper aims to support the G20 DWG efforts to set a vision for supporting developing countries, including LDCs and SIDS, to mobilise more private finance to meet the whole of the 2030 Agenda and in line with their development priorities.

2 Scaling up blended finance in developing countries, including in LDCs and SIDS: opportunities and challenges

This section presents the levers and opportunities available to developing countries, including LDCs and SIDS, governments, G20 governments and development actors in order to bring blended finance to scale for sustainable development. It also looks at an array of case studies (Table 2.1)⁴.

Table 2.1. An overview of case studies

The following case studies have been elaborated in boxes throughout the note

Box	Case study name	Country	Sector	Blended finance instrument
Box 2.1	NASIRA Risk-Sharing Facility	Sub-Saharan Africa; countries neighbouring Europe	MSMEs	Portfolio credit guarantees
Box 2.2	IFC's African Medical Equipment Facility (AMEF)	Cameroon, Côte d'Ivoire, Kenya, Rwanda, Senegal, Tanzania and Uganda	Healthcare; MSMEs	Portfolio credit guarantees
Box 2.3	ADB's role in creating the ecosystem to improve access to green affordable housing for women	India	Housing; Gender Equality	Blended finance loan structure and technical Assistance
Box 2.5	GuarantCo's support for a local currency green bond issuance for student housing	Kenya	Housing	Green bond with partial credit guarantee
Box 2.6	Strengthening BNDES' as mobiliser	Brazil	Cross-cutting / institutional change	Various, incl. green bond, equity investment
Box 2.7	UNCDF's 'BUILD' Malawi Fund	Malawi	SMEs; Agriculture	Structured fund
Box 2.8	UK's and BMZ's Natural Disaster Fund	Multiple	Climate change adaptation	Structured fund

Source: Authors

Entry points for action and change that address bottlenecks preventing blended finance to reach scale in developing countries, including in LDCs and SIDS, and in particular in social sectors, exist both upstream at the policy level and downstream at the operational and transactional level. These entry points fall into four areas:

- Target blended finance solutions to local contexts and employ blended finance to catalyse finance in the last mile of commercial profitability;
- Support domestic financial systems and market development;
- Aim for scale through systemic and transformational approaches;
- Improve impact management and measurement, and promote transparency.

Importantly, the entry points aim to address lessons learned from previous experience with blended finance implementation. Underpinning all entry points for action and change is increased awareness and understanding of the concept of blended finance (Taskin, Bellesi and Moller, 2020_[12]).

2.1. Target blended finance solutions to local contexts and employ blended finance to catalyse finance in the last mile of commercial profitability

2.1.1. Blended finance should add value to and be aligned with local development and financing priorities

Blended finance is one source of funding among many others (see Chapter 1). As such, the ambition of developing countries should not be to scale mobilisation of private finance for the sake of mobilisation of private finance, but to increase the financing available to achieve sustainable development in their countries. Blended finance is a tool that may help to increase the overall amount of financing available for investments such as into social sector by unlocking additional capital from private investors that did not invest before in such sectors.

Clearly, funding with public budget remains an important tool in particular in social sectors that concern public goods such as health or water⁵. In order to be most effective, blended finance should be aligned with local financing priorities and as such be fundamentally embedded in national financing strategies as one potential source of finance. Two relevant tools can be used by developing countries and private sector partners to establish a common understanding of investment opportunities for blended finance.

Indeed, integrated national financing frameworks (INFFs) – country-led efforts to define national priorities and the financing needed to deliver on them – have been featured prominently on the G20 agenda with the *G20 Framework for voluntary support to a greater uptake and operationalization of the Integrated National Financing Frameworks (INFFs) for SDGs Finance and COVID-19 Recovery in developing countries* (G20, 2021_[13]). Financing is traditionally the least developed aspect of national plans, with the majority lacking specifics on how costs will be covered; INFFs connect financing strategies with other related policies for long-term decision-making and help to identify the best sources of financing to address country, sector and risk characteristics (United Nations and Inter-agency Task Force on Financing for Development, 2019_[14]). Lastly, INFFs can work towards aligning the full spectrum of actors involved for cohesive and country-owned sustainable development and recovery strategies (G20, 2021_[13]).

Blended finance can feature among the range of financing sources available to countries, and the financing and risk strategies outlined in INFFs can likewise better inform blended finance investments (OECD/UNCDF, 2020_[15]). Bangladesh offers an example of instrumentalising INFFs for developing an SDGs financing plan through its five-year National Development Plan (2016-2020). The Government of Bangladesh's SDG Financing Strategy sets a total share of target financing from private capital and public-private partnerships (OECD/UNCDF, 2020_[15]), creating an opportunity for blended finance.

Additionally, tools such as the UNDP SDG investor maps have a role to play in facilitating the alignment of blended finance with local development and financing priorities in practice at the sector and sub-sector levels. The SDG investor maps build upwards from country-level office data analysis and research, in turn informing policy priorities and development plans, which equip relevant stakeholders with important country, region and sector-level findings on the investment ecosystem and opportunities for strong, profitable business models that are aligned with local policy priorities and development needs (UNDP, 2021^[16]).

For example, micro, small and medium enterprises (MSMEs) are widely recognised for their important contributions to sustainable development. That is, MSMEs in the agri-food sector can contribute to eradicating poverty (SDG 1), achieving food and nutrition security (SDG 2), promoting inclusive growth (SDG 8), achieving climate action (SDG 13) and protecting water, land and biodiversity (SDG 15) (OECD, 2021^[17]). Accordingly, MSME promotion can feature as a development priority for developing countries, yet many MSMEs, independent of their sector of operation, do not have sufficient access to finance to fulfil their potential. Different blended finance instruments can facilitate the mobilisation of commercial finance for MSMEs in different contexts. Risk mitigation instruments often hold particular potential, given that credit risk is often a key obstacle to financing in this market segment. The case study in Box 2.1 illustrates how risk sharing facilities can reduce the perceived and real risks associated with lending to MSMEs, including those led by women entrepreneurs.

Box 2.1. Supporting the growth of microenterprises and MSMEs

NASIRA Risk-Sharing Facility (2018)

Nasira is an FMO-managed risk-sharing facility (RSF) that guarantees local banks' and microfinance institutions' loan portfolios in sub-Saharan Africa as well as countries neighbouring Europe.

Development finance partners: FMO, European Commission via the European Fund for Sustainable Development (EFSD), Dutch government via MASSIF fund

Private sector partners: Local financial institutions

Challenge: Micro, small and medium-sized enterprises (MSMEs), and women entrepreneurs, migrant, young and COVID-19 affected business owners in particular, struggle to access finance. Among the primary causes are perceived high credit risk, also caused by the absence of a track record and a lack of knowledge regarding due diligence. Yet, MSMEs play a major role in formal employment (responsible for seven out of every ten new jobs created in emerging markets), economic growth (contributing up to 40% of emerging-market GDP), and innovation, creating more resilient and competitive economies (World Bank Group, 2017^[18]).

Solution: Nasira reduces both the perceived and real risks associated with lending to such underserved groups for local financial institutions and thereby incentivises future lending to this group. The RSF covers up to 95% of the credit risk for a portfolio of loans. Under the Nasira loan portfolio guarantee, the loan portfolio is divided into first loss and second loss tranches, whereby the local financial institutions cover the first loss tranche; the second loss tranche is supported by the EFSD program, and the Dutch government's MASSIF Fund. In addition, the EC also financed technical assistance (TA) of USD 4 million for developing local financial institutions' capacity to serve end beneficiaries' needs (e.g. digitalisation programmes, improving credit risk functions). Transactions under the facility include USD 50 million for Equity Bank Kenya and USD 30 million for Bank Al Etihad in Jordan, as well as a closure of USD 15 million to Sidian Bank Kenya in January 2022, which will be made available in local currency. Technical assistance is part of the package to build lending capacity and processes in particular for agriculture.

Source: (OECD, 2021^[19]); (FMO, 2022^[20]); (European Union, 2019^[21]); (FMO, 2022^[22])

Relatedly, promoting gender equality is often among local development priorities, yet the focus on gender equality needs to be strengthened, including in LDCs and SIDS and in particular in blended finance transactions involving larger ticket sizes (OECD/UNCDF, 2020^[15]); (OECD, 2022^[23]). For example, systematically supporting women and girls represents an opportunity for blended finance and the medium to long-term recovery from the COVID-19 crisis (OECD/UNCDF, 2020^[15]). In addition to supporting women-led enterprises by establishing risk-sharing facilities as outlined in Box 2.1 above, liquidity or working capital can be provided to financial intermediaries that incorporate a gender lens (additionally, see case study in Box 2.3).

2.1.2. Target sectors for blended finance should be chosen carefully, taking into account project attributes and context

Target sectors for blended finance – as one instrument in the government’s toolbox to attract private finance – should be aligned with government priorities (see above). Clearly, there is a huge demand for financing social sectors in developing countries, including in LDCs and SIDS. Yet, a stringent assessment is needed to understand if blended finance, i.e. the involvement of private finance, is feasible in the first place. Additionally, it is important to ensure that blended finance attracts additional non-development financing towards different SDGs and is not solely employed in sectors for which the potential for commercial gains is more apparent.

The attractiveness of investments from a private sector perspective is strongly influenced by a project’s financial sustainability, i.e. the ability to generate sufficient cash-flows, for example, in the form of revenues. In water and sanitation, utilities collect tariffs and fees from customers. Yet, tariffs often do not fully cover operational costs in practice, and nor capital expenditure. Similarly, off-grid sanitation revenues could stem from the sale of toilets, collection fees or concession contracts from local governments, among others (OECD, 2019^[24]). In cases where revenues are limited to covering external financing costs, stand-alone private finance is unlikely. Blended finance can play a role in enhancing returns for private investors; however, steady and projectable revenues need to be available in the first place. Indeed, private finance mobilised in water and sanitation are only small compared to other sectors where the business case is clearer, e.g. energy projects that benefit from revenues generated through purchasing power agreements (PPAs), for example (see Annex).

Still, social sectors can facilitate projects and business models that generate sufficient revenues to attract blended finance, as the case studies on MSMEs and young, female and migrant entrepreneurs (Box 2.1. Supporting the growth of microenterprises and MSMEs); healthcare businesses (Box 2.2. Encouraging lending to private healthcare SMEs); gender-responsive, green and student housing (Box 2.3. Promoting demand and strengthening the ecosystem for a housing market that is gender-responsive and climate-resilient; Box 2.5. Blended finance enabling affordable, green housing solutions); agriculture businesses and climate change adaptation (Box 2.7. Blended finance to support SMEs in the LDCs; Box 2.8. Leveraging private risk coverage capacity with development finance for climate change adaptation); as well as show.

Box 2.2. Encouraging lending to private healthcare SMEs

The IFC's African Medical Equipment Facility (AMEF) (2020)

The IFC's Africa Medical Equipment Facility is designed to help private healthcare providers secure loans to either purchase or loan the required equipment. Launched in 2020, the facility is covering seven African countries, including Cameroon, Côte d'Ivoire, Kenya, Rwanda, Senegal, Tanzania and Uganda.

Development finance partners: IFC, International Development Association Private Sector Window (IDA-PSW) Blended Finance Facility, Global Financing Facility for Women, Children and Adolescents (GFF).

Private sector partners: Co-operative Bank of Kenya, NSIA Bank, Côte d'Ivoire, GE, Philipps and others

Challenge: In the COVID-19 pandemic, many healthcare providers in Africa lack funds to equip their health professionals with specialised medical gear, such as MRI machines and CT scanners. According to a WHO member state survey, only 11 percent of respondent countries in Africa had at least one MRI machine per 1 million people—and only 24 percent had at least one CT scanner. In sub-Saharan Africa, small and medium private healthcare providers (SMEs) form the backbone of the healthcare system, serving over half of the African population including low-income patients. Their inability to access the loans needed to purchase such equipment stems from high risks associated with the investment.

Solution: AMEF is a risk-sharing facility that allows SME healthcare businesses to access finance by enabling and incentivising local financial institutions such as the Co-operative Bank of Kenya to lend to such businesses. The facility is backed by the IDA Private Sector Window (PSW) Blended Finance Facility (BFF) and the Global Financing Facility (GFF), which provide a first loss guarantee of up to USD 18 million and USD 6 million, respectively. The total target facility size for AMEF is up to USD 150 million in unfunded portfolio guarantees. The ambition is to unlock up to USD 300 million of future loans and leases to private healthcare SMEs with a tenure of up to seven years.

Under AMEF, IFC also provides technical assistance in the field of procurement processes, financial management, business planning and equipment maintenance to private healthcare providers, and capacity building to participating financial institutions for strengthening their credit underwriting capabilities.

Source: Project description provided by IFC, (IFC, n.d.^[25]; IFC, 2022^[26])

Again, blended finance is one financing source among many others and, particularly in sectors convening global public goods such as health or water and sanitation, government funding and ODA will continue to be a major source of funding. Indeed, the involvement of private actors in financing healthcare as a service has been critically assessed as it is associated with higher overall financing costs than traditional public investment (Wemos, 2021^[27]).

At the same time, blended finance is about attracting additional non-development financing. To effectively increase financing for sustainable development, blended finance should be employed only in sectors and countries where commercial financing is not currently available for deployment towards development outcomes – especially if it involves concessional resources⁶. Maximising mobilisation is however not a goal in itself, but rather has to be viewed in relation to the underlying development objective. Increasing leverage over time is a sign of increasing market maturity where development finance is no longer required (OECD, 2018^[1]). Overall, blended finance should be used in sectors and contexts where there is a need to address

market failures, and should thus be based on an ongoing analysis of market conditions and commercial maturity of technologies.

Rather than being a target sector, gender equality as an investment priority can be an objective of investing (see Box 2.3. Promoting demand and strengthening the ecosystem for a housing market that is gender-responsive and climate-resilient). With respect to blended finance vehicles such as funds and facilities, it is found that two-thirds of such vehicles integrate gender equality as a mainstreamed objective, while one this does not identify gender equality as an objective at all. Blended finance vehicles integrating gender equality encompass a variety of sectors, including energy, transport, banking and environment (OECD, 2022^[23]). Investments in gender equality are viewed as crucial for social and economic sustainable development.

Box 2.3. Promoting demand and strengthening the ecosystem for a housing market that is gender-responsive and climate-resilient

ADB's role in creating the ecosystem to improve access to green affordable housing for women in India (2021)

The Asian Development Bank (ADB) is administering the Urban Climate Change Resilience Trust Fund (UCCRTF), a USD 150 million trust fund capitalised by the Rockefeller Foundation and the Governments of Switzerland and the UK. ADB also administers the Canadian Climate Fund for the Private Sector in Asia (CFPS), a USD 82 million concessional financing facility funded by Global Affairs Canada that aims to catalyse private investment for mitigation and adaptation in the region of Asia and the Pacific.

The objective of the project is to foster an ecosystem for green, affordable housing in India, particularly for women and vulnerable groups, including low-income households and economically weaker segments of India's economy.

Development finance partners: ADB, Canadian Climate Fund for the Private Sector in Asia (CFPS) and the Urban Climate Change Resilience Trust Fund (UCCRTF) under the Urban Financing Partnership Facility of the ADB.

Private sector partners: India Infoline (IIFL), housing finance institutions, housing developers

Challenge: The challenge identified is 2-fold, including (1) increase the supply of climate-resilient affordable housing to protect vulnerable groups from climate risks, and (2) trigger demand for green affordable housing.

Solution: The USD 10 million blended finance loan structure complements a USD 58 million loan from ADB for an Indian housing finance institution to fund loans to housing developers and thereby increase the supply of green certified and affordable housing projects in India. ADB complemented the debt package with grant-based technical assistance from UCCRTF to broaden the knowledge base for key stakeholders on the affordable housing supply and demand side.

Concessional financing from the CFPS was instrumental in overcoming cost and technical barriers at the nascent stage of India's green housing market. It was further essential in continuing to scale proof of concept of adapted designs and the use of climate-resilient materials for affordable housing.

This accompanying USD 1 million technical assistance grant from the UCCRTF contributes to increased supply of climate resilient and certified green affordable housing. The grant will be used to (1) build capacity on climate change adaptation and certification process of green affordable housing, (2) knowledge exchange, including the support of an Indian housing finance institution led platform for industry experts and housing developers to create climate resilient and green affordable housing, and

(3) market research and testing of innovative technologies for green construction to establish a base level of understanding and awareness for green building amongst buyers, publishing a unified green buildings system, and implementing innovative green construction technology.

The overall ambition is hence to build a market for climate resilient green certified affordable housing in India, by creating the expertise and capacities on the supply side, as well as providing the financing needed to unlock private lending for the benefit of women and vulnerable populations. 100% of the mortgage loans provided by the project will be for women from the Economically Weak Segments and Low-Income Groups as defined by the Government of India.

Source: Project description provided by ADB; (Asian Development Bank, 2021^[28])

2.2. Support domestic financial systems and market development

2.2.1. Institutional, policy and regulatory frameworks need to be in place to scale blended finance

Blended finance models aim to unlock private finance into countries, sectors or projects that would not receive stand-alone private finance. At the same time, transactions cannot make up for the right conducive investment and regulatory environment that enables private investment. Rather, blended finance can support market building by, for instance, addressing information asymmetries between private sector investors and investees. Contributing to market creation and development has significant transformative potential, yet governments need to work more structurally in parallel to reduce investment barriers related to regulation and institutional frameworks.

For example, the most important challenge identified in Bangladesh in attracting blended finance funds is identified as a “prudent, investor and development friendly regulatory and institutional framework to ensure the governance and accountability” of private finance mobilised (Khatun, Shadat and Kabir, 2021^[29]). In order to develop adequate and conducive institutional frameworks, it is recommended that the government takes an inclusive approach and coordinates with and integrates views of regulatory entities such as the Bangladesh Bank (Khatun, Shadat and Kabir, 2021^[29]).

Moreover, the OECD’s Policy Framework for Investment (PFI), as a further example, examines countries’ readiness and pathways to formulating policies that attract more private finance for sustainable development from an institutional and regulatory perspective (OECD, 2015^[30]) (see also Box 2.4). Recent developing countries assessed include for example Myanmar (2020), Egypt (2020), or Cambodia (2018) (OECD, 2022^[31]). Similarly, UNCTAD’s Investment Policy Reviews have recently investigated the Seychelles (2020), Côte d’Ivoire (2019) and Angola (2020) (UNCTAD, 2022^[32]). This action also links to the “Governance and Coordination” building block in INFFs, which serves to align existing regulations and policies.

Box 2.4. Enabling environments for investment are key in bringing blended finance to scale

One critical element of capacity to mobilise private finance for investment is the enabling environment for investment in a given country. While there is no universally agreed definition of ‘enabling environments’, it is clear that a range of policy issues matter. For example the OECD’s Policy Framework for Investment (PFI) – used by over 25 countries as well as regional bodies to assess and reform the investment climate – identifies 12 policy areas: investment policy; investment promotion and facilitation; trade; competition; tax; corporate governance; promoting responsible business conduct; human resource development; infrastructure; financing investment; public governance; and investment in support of green growth (OECD, 2015^[30]). Three principles apply throughout the PFI: policy coherence, transparency in policy formulation and implementation, and regular evaluation of the impact of existing and proposed policies.

Countries’ with higher levels of country income typically have more developed capacity to attract private finance for investment, as illustrated in Infographic 1. Importantly, this capacity is often driven by a country’s enabling environment for investment, which is generally stronger for countries with higher levels of country income and development. For example, countries with medium or relatively low-risk profiles - as assessed by the Allianz Medium-Term Country Risk Ratings which captures a range of elements relevant for a country’s enabling environment for investment – mobilised relatively larger shares of private climate finance (OECD, forthcoming^[33]). Broadly speaking, as countries transition through development stages, private resources progressively substitute public financing (Piemonte et al., 2019^[34]).

LDCs and SIDS face specific issues in strengthening their enabling environments for investment and attracting private finance (OECD, 2018^[35]); (OECD/UNCDF, 2020^[15]). For instance, they typically have a weak presence on capital markets, and either lack a sovereign credit rating or have one which is not of investment grade. May also incur high political volatility, increasing their risk premia required by investors. Relatedly, many LDCs and SIDS face limited fiscal space and are heavily indebted. Adding climate change considerations, LDCs and SIDS are often experiencing the phenomenon of dual vulnerability: On the one hand, they experience fiscal vulnerability and macroeconomic instability, and on the other, extreme climate vulnerability. Hence, it is in particular important in the case of LDCs and SIDS to strengthen enabling environments for investment, in addition to efforts in blended finance.

Beyond general private sector investment readiness efforts, specific regulation hindering blended finance instruments should be identified and addressed. For example, in the context of the listed green bond issuance for student housing in Kenya issues by a private project developer (see Box 2.5. Blended finance enabling affordable, green housing solutions), the development of a regulatory framework for green bonds in Kenya was crucial. Here, the UK government has worked with the Kenyan government to develop capital markets and to mobilise investments (Private Infrastructure Development Group, 2020^[36]).

Box 2.5. Blended finance enabling affordable, green housing solutions

GuarantCo's support for a local currency green bond issuance for student housing (2020)

With the support of GuarantCo the largest student accommodation property developer in Kenya, Acorn Holdings, listed its KES 4.3 billion green bond programme on the Nairobi Securities Stock Exchange (NSE) and the London Stock Exchange (LSE) – the first project bond to receive green certification in Kenya.

Development finance partners: GuarantCo, Emerging Africa Infrastructure Fund (EAIF), PIDG Technical Assistance Facility (all part of the Private Infrastructure Development Group (PIDG)), the UK government

Private sector partners: Stanbic Bank Kenya Limited, SBG Securities Limited and Standard Investment Bank as arrangers and placement intermediaries; private investors as bondholders

Challenge: Kenya currently faces a shortage of student accommodation: while university enrolment has grown significantly over the past decades, limited student housing options are available in the universities, with damaging consequences for the number of young Kenyans able to pursue higher education.

Solution: Acorn Holdings raised KES 4.3 million for the construction of student accommodation for 5,000 students in Nairobi via project bond issuance. This bond programme is characterised by (1) its green certification as defined by the Climate Bonds Initiative, (2) its listing on both the Nairobi Securities Stock Exchange (NSE) and the London Stock Exchange (LSE) since 2020, and (3) having obtained a credit rating by Moody's. While this is non-investment grade at B1, it is still one notch above the Kenyan sovereign rating. GuarantCo enabled the credit rating by providing a partial credit guarantee. Moreover, technical assistance provided by the Technical Assistance Facility, via GuarantCo, further enables the transaction through a part returnable grant to Acorn contributing towards the costs of the loan note issue.

While currently the Emerging Africa Infrastructure Fund (EAIF), which participated in the issuance of the bond, is the largest single investor, the ambition is that this issuance has built the market for corporate bonds that attract institutional investments. In addition, the bond listing in local currency in London can mobilise and open the door to a global investor base and allows those to build a track record in Kenya and the local currency.

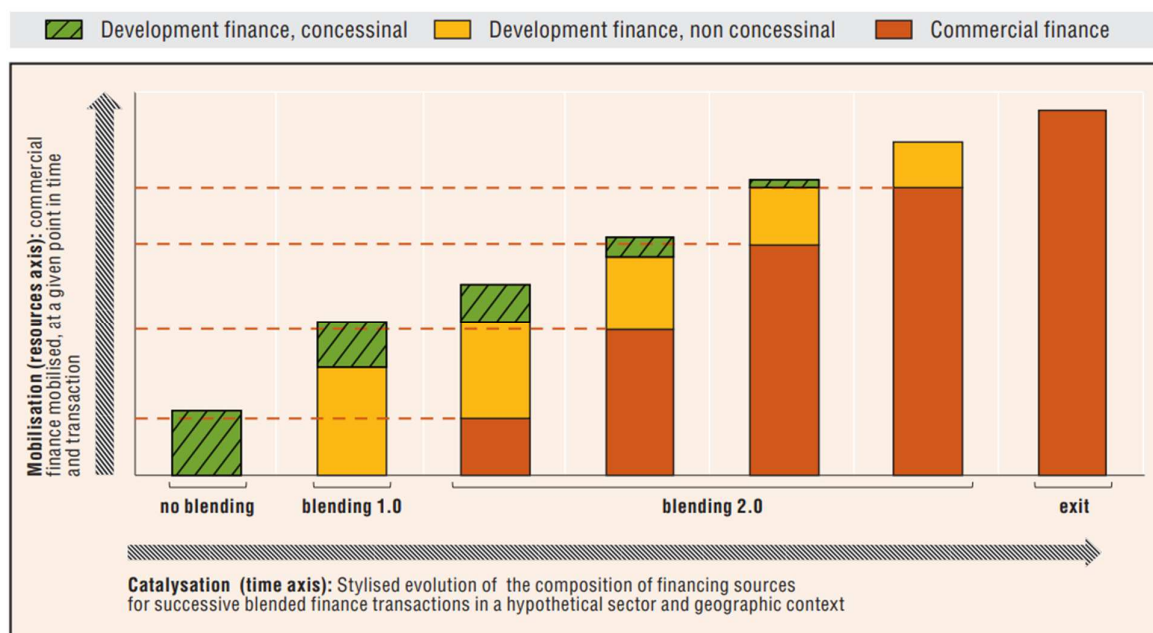
Source: (Private Infrastructure Development Group, 2020^[36]; GuarantCo, 2020^[37])

Similarly, capital adequacy frameworks should be in place for financial institutions to leverage private capital in the first place, including securitisation. Under the Africa Securitization Alliance, for example, the Milken Institute brings together public and private stakeholders to share knowledge and overcome barriers to securitisation. Partaking regulators include the Capital Markets Authority of Kenya, the Securities and Exchange Commission of Ghana, the West African Regional Council for Public Savings and Financial Markets, and the Capital Markets Authority of Uganda (Schellhase and Mohsin, 2021^[38]). Additionally, strengthened disclosure rules can contribute to transparency on social and environmental impact (AVPN, 2022^[39]).

While efforts in blending need to be accompanied by improvements in the investment framework as well as measures to increasingly develop and deepen local financial markets, blended finance can also support market building – including by demonstrating project viability and addressing information asymmetries. In particular, the focus on attracting non-development, commercial finance underlines the catalytic, market-

building intention of blending (OECD, 2018_[1]). Tracking the concessional terms and mobilisation effects of different blended finance transactions in comparable contexts over time, for example in similar geographies and sectors, can indicate if catalysation and market building indeed took place (see Figure 2.1).

Figure 2.1. Stylised representation of transaction-level mobilisation and catalytic market building over time



Source: (OECD, 2018_[1])

Relatedly, avoiding market distortion is a major concern where donors work with and through the private sector, and is accordingly a key objective of blended finance (OECD, 2020_[40]). While concessional finance can help make projects with high development returns commercially viable, the use of minimum concessionality is an accepted principle in blended finance (OECD, 2018_[1]); (OECD DAC, 2017_[41]); (IFC et al., 2017_[7]). Importantly, concessionality is not a pre-requisite for blending: While many blended finance examples to date have been based on concessional development finance, concessionality is not always needed in order to mobilise commercial resources (OECD, 2018_[1]). In advancing the blending agenda, it will be important to ensure there is a clear case for achieving development results in the use of blended finance, calibrating the use of concessional finance and balancing the risk-return relationship for individual transactions as needed. When concessional finance is deployed, this should only be done to the extent required to attract non-development, commercial finance and a clear exit strategy should be in place (OECD, 2018_[1]).

2.2.2. Governments should enable local actors to engage in blended finance solutions, including to mobilise themselves

Building local markets is one of the major ambitions of blended finance. Indeed, in its transitory nature, blended finance approaches should include an exit-strategy from the outset (OECD, 2021_[5]; OECD, 2020_[42]). Where possible, concessionality should be reduced over time, and subsequently the share of development finance needed to unlock private investment, with the ambition to enable self-sustainable financial markets.⁷ To get there, building, strengthening and leveraging local actors is important.

For example, local financial institutions can be incentivised to initiate or start lending to MSMEs, women-led enterprises, young entrepreneurs, or new sectors such as healthcare by providing liquidity via a credit line or risk sharing capacity via portfolio guarantees. For example, the IFC's African Medical Equipment Facility enables local banks such as the Co-operative Bank of Kenya to provide loans to healthcare businesses to purchase medical equipment; the FMO-managed Nasira risk sharing facility provides incentives and risk-taking capacity to local banks such as Bank Al Etihad in Jordan so that they on-lend to MSMEs such as women entrepreneurs, migrant, young and COVID-19 affected business owners (see Box 2.1. Supporting the growth of microenterprises and MSMEs and Box 2.2. Encouraging lending to private healthcare SMEs). Additionally, increased awareness and knowledge of blended finance of local firms could contribute to scaling up blended finance in developing countries (AVPN, 2022^[39]).

Moreover, beyond single transactions, in order to engage and scale local development actors such as NDBs or local DFIs' ability to mobilise private finance for sustainable development, government owners should develop and implement clear and coherent mandates, incentive systems and capacities (OECD/The World Bank/UN Environment, 2019^[43]); (Taskin, Bellesi and Moller, 2020^[12]). Such systemic approaches will be crucial for inducing system-level change that will elevate local development actors such as NDBs from a funding to an enabling role (Box 2.6). In this regard, NDBs can hold a comparative advantage over their multilateral counterparts given their embeddedness in national policy contexts, their proximity to the local private sector and their provision of financing in local currency (OECD, 2019^[44]). These roles mutually reinforce each other and elevate the relevance of national development banks in local capital market development and bringing blended finance to scale. Local intermediaries also play a crucial role in building the sustainable housing market in India, facilitated by an ADB project including housing finance institutions (Box 2.3), as well as in the issuance of a green bond for housing finance in Kenya, where the financial advisors and structurers were local actors (see Box 2.5. Blended finance enabling affordable, green housing solutions).

Box 2.6. Strengthening the role of National Development Banks as mobilisers

Brazil's National Development Bank BNDES

Worldwide, over 250 National Development Banks (NDBs) exist, and while their focus is mostly on domestic operations, their collective financial footprint (USD 5 trillion in AUM) is significant larger than that of internationally-operating MDBs (USD 1 trillion) (Gallagher and Kring, 2017^[45]). Independent of the size of individual institutions and their scope of operations, NDBs have two specific comparative advantages over internationally operating counterparts, including for blending and bridging the SDG investment gap (Abramskien et al., 2017^[46]); (OECD/The World Bank/UN Environment, 2019^[43]); (OECD, 2019^[44]): They have an unmatched proximity to local markets and national policy contexts, and they provide financing in local currency.

Despite these comparative advantages, NDBs remain to date an underused conduit for the mobilisation of commercial capital, for reasons internal and external to them. At the same time, an increasing body of literature underscores the critical role of NDBs in bridging in particular the investment gap for low-emissions, climate-resilient infrastructure (OECD, 2017^[47]); (Abramskien et al., 2017^[46]); (OECD/The World Bank/UN Environment, 2019^[43]); (Morris, 2018^[48]); (GIZ, 2019^[49]); (Smallridge et al., 2019^[50]); (OECD, 2019^[44]); (Griffith-Jones, Attridge and Gouett, 2020^[51]). In Brazil, and notably spurred by awareness of the limitations of public finance and the need for more investment in social and economic infrastructure, BNDES – Brazil's main NDB – and its public shareholders have pushed for the bank to start transitioning from its traditional role as provider of long-term finance to mobiliser of private capital (OECD, 2019^[44]); (Taskin, Bellesi and Moller, 2020^[12]). For example, one of BNDES' updated mission over recent years recognised the importance of its ongoing work on capital markets development. In May 2017, BNDES issued a USD 1 billion green bond which was the first international green bond

issuance by a Brazilian bank. Another example, is the bank's BRL 500 million Sustainable Energy Fund (Fundo de Energia Sustentável), which builds on an established securitisation framework to finance the construction of sustainable energy projects and securitise the less risky operational phase of sustainable energy projects. More recently, BNDES started to additionally engage in direct equity investment, including for example in Sunew, a company manufacturing and commercialising Organic Photovoltaic (OPV) films to generate solar energy.

Institutions involved: BNDES, CSEM (a Brazilian research centre), Sunew and private investors

Blending instrument: Direct equity investment in company

Challenge: Financing research and development for innovative and green technologies, as well as subsequent commercialisation can be particularly challenging, due to the investment needs as well as the typically high risks of innovation. Financing innovation and technological developments for green solutions can have huge potential for promoting sustainable development requires patient capital, a long-term horizon, willingness to take risks and experiment, as well as innovative partnerships.

Solution: Sunew is a spin-off company aiming at the large-scale manufacturing and commercialisation of Organic Photovoltaic (OPV) films to generate clean solar energy. The OPV technology was developed by the Brazilian research centre CSEM, which BNDES financially supported in 2013 through FUNTEC, a technology fund that provides grants for R&D projects developed jointly by research institutions and companies. The FUNTEC agreement provided for the pre-emptive right for BNDESPAR to eventually participate in the start-up companies created to produce and commercialise the products resulting from the research. This right was exercised by BNDESPAR in the context of Sunew, CSEM's spin-off company. In 2015, BNDESPAR subscribed shares in Sunew for an amount of BRL 4.5 million (USD 1.3 million), which gave it right to 30% of the company's shares, with the rest held by CSEM (45%), a private investor (15%) and the company's funders (10%). Subsequently, there have been further capital increases, mainly needed to enable commercialisation of the OPV films, in which Sunew was successful in attracting capital from four new private investors, including some angel investors. BNDESPAR then approved subsequent capital increases to maintain its ownership interest in Sunew (BNDES, 2018^[52]).

Results: The company Sunew is considered an innovation pioneer in Brazil, positioning itself at the forefront of the solar energy technology market. The company offers a variety of products with Organic Photovoltaic (OPV) films, an innovative technology to generate clean solar energy. According to Sunew, each square meter of the OPV avoids the emission of 120 kg of CO₂ per year.

Source: (BNDES, 2018^[52]); BNDES internal documents and interviews with staff; (Taskin, Bellesi and Moller, 2020^[12])

Likewise, developing country governments can step in and should step up to unlock private finance. For example, the Ghanaian government has facilitated an innovative approach to mobilise private finance for education infrastructure in the country (the 'GETFund'). That is, with the support of a securitisation structure, private investors were mobilised to provide additional financing by purchasing bonds that are backed by dedicated and ring-fenced future consumer tax flows (levy). The two bonds emerging from the programme are publicly listed on the Ghana Stock Exchange. The Ministry of Finance enables these bond issuances by providing a guarantee to repay bondholders should the cash flows not suffice to do so. Moreover, local regulation has been put in place by the Securities and Exchange Commission (SEC) to enable this securitised structure and mobilise private investment for education in Ghana (Schellhase and Mohsin, 2021^[38]). The government employed two local financial advisory firms to develop and design the solution.

More broadly, the current global environment of rising interest rates will increase the attractiveness of the de-risking function of blended finance, in turn attracting local institutional investors seeking diversification and adjusted market conditions (Convergence, 2022^[53]).

2.2.3. Governments should build capacities and create the ecosystem beyond a transaction-based approach

While the concept of blended finance is well-established and the potential of blended finance has been assessed, it remains a challenge to get to a point where the rubber hits the road. A key question for developing country governments is where to start once the decision has been made to leverage blended finance for sustainable development in the country. Clear, actionable implementation guidance and associated capacity building is therefore needed as the tools to turn concepts and ambitions into reality.

While capacity building programmes are a key constituting factor of blended finance's ambition to build markets, it is important to identify what the main capacity building needs are in order to attract more private investment via blended finance, and align them with development priorities.

In doing so, developing countries can work closely with development actors. For example, since 2019, Italy's CDP is jointly with the the Italian Agency for International Cooperation (AICS) coordinating an initiative named PASPED in Senegal, which received grant funding from the European Commission. The ambition of the technical assistance programme is to support the local Senegalese Central Guarantee Fund, FONGIP, to improve its processes and procedures for risk management, pricing and the reporting and monitoring processes on the issuance of guarantees. The ambition is to enable the fund to become eligible in the near future to access guarantees made available by the EU. Strengthening local actors is indeed crucial to build the ecosystem needed to scale blended finance (European Commission, 2017^[54]).

Developing countries should be interested in and aiming at creating an ecosystem – for blended finance, and for private stand-alone investment in the long run rather than taking a transaction-by-transaction approach. Including local institutions – such as financial institutions but also private enterprises – as development partners in blending finance transactions is a critical lesson in delivering blending solutions that result in positive impacts on individual transactions but also market development, including through the emphasis of improving the ecosystem (OECD, 2021^[17]). Relevant guidance for implementing such approach remains unavailable, while notable efforts have been made for providers of development finance, for example (OECD, 2021^[5]). In addition, the INFFs “Assessment and Diagnostic” process could help identify capacity building areas based on the assessment of countries' policy and institutional binding constraints.

2.3. Aim for scale through systemic and transformational approaches

2.3.1. Make sure a pipeline of projects is available to pivot towards scale

A lack of a pipeline of projects, or investment opportunities, is considered a main challenge to scale blended finance. Project preparation at scale and on a continuous basis is necessary to ensure that the private sector can come in in the first place. Technical assistance (TA) is therefore a vital element for capacity building in blended finance (see Annex). Technical assistance can address constraints at the capital provider level, as in the Nasira risk sharing facility example, the European Commission provided financial contributions for TA that are used to enhance capacities of local financial institutions via digitalisation programmes and improving credit risk functions in financial institutions (OECD, 2021^[19]). Moreover, TA is often applied or at the use of finance level, for example in the context of UNCDF's BUILD Malawi fund, where UNDP and the Food and Agriculture Organisation (FAO) provide TA to the enterprises in the agriculture sector to build and strengthen pipelines and supply-chains (see Box 2.7). More

structurally at the enabling environment level, the UK government has worked with the Kenyan government on a regulatory framework for Kenyan green bonds (see Box 2.5) and ADB is administering a TA facility that aims to enhance the knowledge of industry experts and housing developers to create climate resilient and green affordable housing (see Box 2.3). Importantly, the TA accompanies a blended finance loan to a housing finance institution from ADB.

At a programmatic level, the combination of TA as a project preparation tool and blended finance as a financing tool is prominently featured in the European Commission's External Investment Plan (EIP), which includes both a pillar on TA for the development of dedicated projects or more general for a conducive investment environment, and a pillar for blended finance. The latter is using, under the European Fund for Sustainable Development (EFSD), guarantees and grants (see Box 2.1. Supporting the growth of microenterprises and MSMEs) for supporting SDG investments in Africa and the EU's neighbouring countries (with a focus on fragile contexts) (European Commission, 2022^[55]). New research outlines that the recovery from COVID-19 may create significant scope for more extensive and better use of guarantees (Garbacz, Vilalta and Moller, 2021^[56]). They are particularly relevant in the context of LDCs due to their ability to increase local currency financing, and their use could be scaled up through e.g. better co-ordination between guarantees and insurance products, agreement by the OECD Development Assistance Committee on their ODA-eligibility, and the promotion of partial guarantees.

Box 2.7. Blended finance to support SMEs in the LDCs

UNCDF's BUILD Malawi Fund

The BUILD Malawi Fund is a blended finance fund launched by Bamboo Capital Partners as the fund manager and UNCDF as investment advisor with the ambition to provide finance to small-and-medium sized enterprises (SMEs) in Malawi. The BUILD Malawi Fund is thereby a sub-fund of the BUILD Fund SICAV-RAIF, an umbrella investment vehicle incorporated in Luxembourg, which aims to mobilize international private capital has a cross-country focus onto providing finance to “missing middle” businesses in least developed countries (LDCs).

Development finance partners: Joint SDG Fund, UNCDF, UNDP and FAO

Private sector partners: Bamboo Capital Partners as fund manager

Challenge: Access to financing for SMEs in Malawi is challenging given the general low rate of investment in the country. As such, enterprises cannot grow, and agriculture businesses are limited in their capacity to support ending poverty and hunger. Additionally, the country currently suffers from a shortage of hard currency availability and a dearth of international capital more generally.

Solution: In partnership with UNDP and FAO and with initial first-loss funding from the Joint SDG Fund, UNCDF has established the BUILD Malawi Fund. This structured blended finance fund aims to mobilise USD 35 million offering two classes of shares (mezzanine tranche of UDS 20 million and catalytic first loss tranche of USD 15 million) for investing debt, quasi-equity, and equity into 50 businesses in Malawi in partnership with Bamboo Capital Partners. The deal size is between USD 250,000 to USD 2.5 million. The UNCDF as anchor investor has deployed “beneficiary units”, which are flexible security instruments allowed under Luxembourg law but conferring no ownership, economic rights or voting rights, to route the Joint SDG Fund's initial contribution into the Malawi sub-Fund. is the anchor investor, Through this innovative solution, which can used when donors encounter internal restrictions internal restrictions on directing their funding directly into privately managed blended finance vehicles, UNCDF enabled the Joint SDG Fund to provided almost 50% of the targeted first loss tranche.

UNCDF, through its partnership with Bamboo Capital Partners, also serves as the investment advisor to the Fund; in doing so, UNCDF undertakes pipeline development and assessment of investment

prospects, working with various entrepreneurship support programs, including the ones managed by UNDP Malawi, to identify companies for the pipeline. The goal is to build a pipeline of “bankable” SMEs and projects in Malawi, by taking them from “too small and too risky” to commercial viability and bankability. The Fund is sector agnostic with a cross-cutting focus on women’s economic empowerment and supporting youth. BUILD Malawi Fund will invest with likely higher concentration of food security and agribusinesses and green economy and renewable energy business and will also explore other opportunities, especially in local infrastructure and financial inclusion. UNDP and FAO provide technical assistance to enterprises in the agriculture and other manufacturing sectors and service supply-chains. The focus is on increasing financing available to agriculture and other manufacturing and service supply-chains SMEs, as well as increasing productivity within these supply-chains through technology and innovation,; and achieving gender equality by supporting business where women are significantly represented in boards, management, staff, suppliers, or buyers.

This Fund will be accompanied by a technical assistance facility for sourcing an investable pipeline pre- and post- investment support, assisting business to improve their SDG impact and mitigate risks and costs. The Joint SDG Fund has provided funds to capitalize the technical assistance facility. UNDP will manage the facility and, with FAO and UNCDF, will provide technical assistance to enterprises in the agriculture and other manufacturing sectors and service supply-chains.

Source: Project description provided by UNCDF; (Joint SDG Fund, n.d.^[57]) (UNCDF, 2020^[58])

2.3.2. Facilitate portfolio and programmatic approaches to unlock private finance at scale

Private sector investment is seeking adequate risk-return relationships in investment opportunities, whereby in particular return considerations are – among other parameters – driven by the investment volume, so-called “ticket size”. For example, agriculture is a sector where small-scale transactions are common, which might hinder the use of blended finance at scale, despite the fact that small family farms and SMEs make up the majority of enterprises in the agri-food sector in many developing countries and notwithstanding their potency to advance a range of SDGs (OECD, 2021^[17]). First-time investments in unknown sectors or jurisdictions, associated due diligence and capacity needed will increase the transaction costs that hence drive return expectations. Similarly, concentration risk is significant when investing in single exposures.

Portfolio approaches are playing an increasingly important role in blended finance to scale private investment volume and enable risk diversification for private investors (see Annex). A well-known example of portfolio approaches is the IFC’s Managed Co-Lending Portfolio Program (MCP), which enables institutional investors to have access to IFC-originated loans in, for example, infrastructure projects in developing countries and emerging markets (IFC, 2021^[59]). The structured debt fund allows not only for a tailored risk-return approach for institutional and development actors (e.g. IFC holds the first loss tranche in its infrastructure loan portfolio in the MCP, which is also benefitting from credit enhancement by a guarantees issued by the Swedish International Development Cooperation Agency (Sida)), but also access to a portfolio of homogenous assets such as infrastructure loans. Currently, institutional investors such as Allianz Global Investors can invest at investment-grade in senior tranches. Going forward, portfolio ideally, approaches should avoid a sole focus on sectors where transactions already occur at large-unit scale, and should additionally consider the need to target local development priorities and reach the last mile of commercial viability.

Similarly, the BUILD fund by the UNCDF is pooling financing for up to 50 businesses in Malawi, thereby creating a portfolio of assets (Box 2.7. Blended finance to support SMEs in the LDCs); the Natural Disaster Fund (NDF) sponsored by the Foreign, Commonwealth and Development Office (FCDO) and KfW on behalf of the German Federal Ministry of Cooperation and Development (BMZ) mobilises private reinsurance risk capacity for a variety of projects that protect poor and vulnerable population from climate disaster risk (see Box 2.8. Leveraging private risk coverage capacity with development finance for climate change adaptation).

Box 2.8. Leveraging private risk coverage capacity with development finance for climate change adaptation

The Natural Disaster Fund (NDF) (2019)

The Natural Disaster Fund (NDF) is joint development project of the UK and Germany under the InsuResilience Global Partnership. The UK Foreign, Commonwealth and Development Office (FCDO) and KfW on behalf of the Federal Ministry of Economic Cooperation and Development (BMZ) have capitalised the NDF as a risk pool (GBP 25 million and EUR 34 million respectively) that underwrites protection against climate disasters in developing countries and emerging markets, benefiting mostly poor, and vulnerable populations.

Development finance partners: UK Foreign, Commonwealth and Development Office (FCDO) and KfW on behalf of the German Federal Ministry of Cooperation and Development (BMZ)

Private sector partners: Global Parametrics as fund manager, Hannover Re as private reinsurers, with more private insurers expected to join the fund

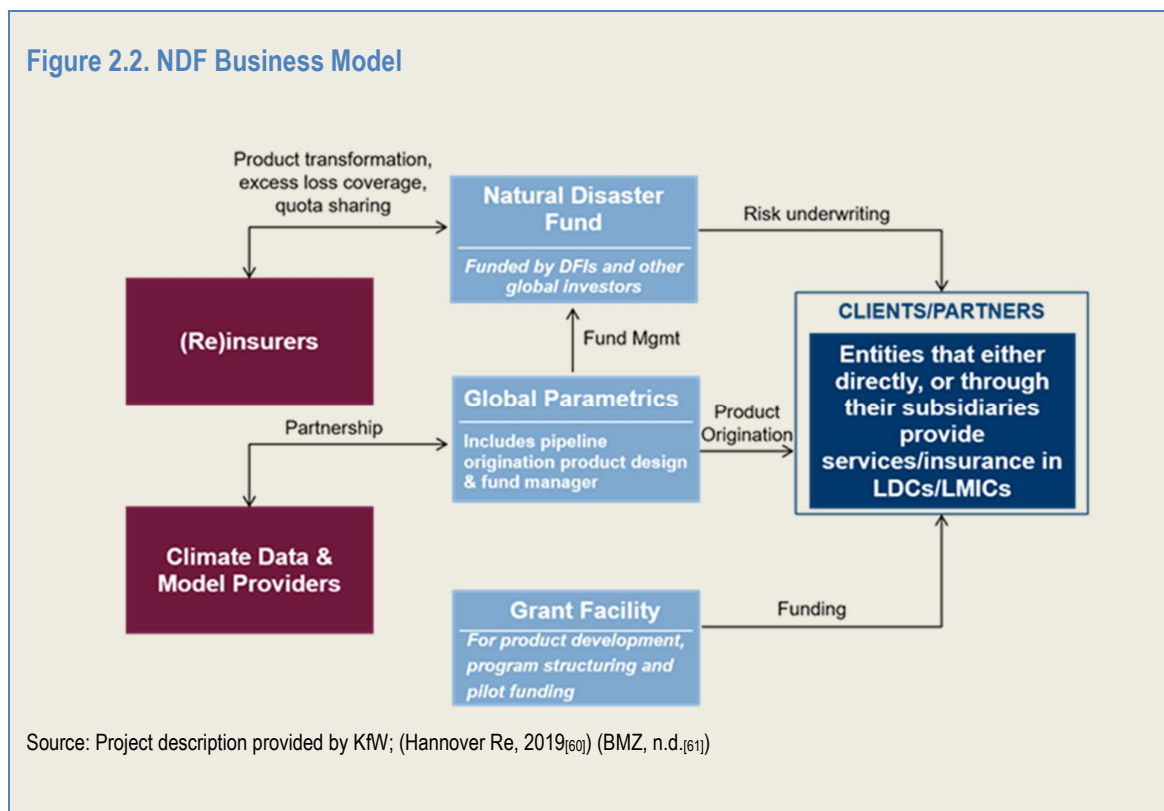
Challenge: Insurance products can support sustainable development by covering specific residual climate risks. Yet, insurance products are often not available due to high upfront development costs and the uncertainty regarding financial sustainability. Hence, losses from disasters in developing countries remain largely uninsured to the disadvantage of small businesses and communities.

Solution: The NDF's development finance partners bring a long-term and concessional view towards capital returns. The development funds provided by donors enable the development of such products available to clients in LICs and MICS.

The first client was the microfinance network VisionFund International, an affiliate of the humanitarian NGO WorldVision. Together with the client, GP developed a combined climate risk protection solution for the VisionFund microfinance institutions around the world, providing both contingent credit and insurance pay-outs based the severity of natural disasters.

Almost from the start, the NDF has been able to mobilise private reinsurance risk capacity to double its activities. In fact, one of the world's largest reinsurers, Hannover Re, is sharing the first USD 100 million the risks underwritten by NDF 1:1 pari-passu. Currently, there are discussions with an additional multinational insurance company to join, which would increase the leverage to 1:4. Larger leverage effects are expectable with a growing portfolio. As of September 2021, the three largest clearly definable exposures were in Morocco, the Caribbean and Mexico.

Figure 2.2. NDF Business Model



Clearly, such considerations about private sector preferences should be considered when designing blended finance solutions. Ideally, private sector actors should be involved early on in the design process for blended finance solutions to ensure that the products are indeed attractive and able to unlock private finance. Coordination and communication (see below) are key to ensure this.

Another project attribute that facilitates the involvement of the private sector is standardisation (see also (OECD, 2020^[40]; 2021^[5])). Programmatic approaches to blended finance projects and transactions will enable to bring down due diligence and, hence, transaction cost, thereby complementing portfolio approach ambitions. While bespoke transactions are important to showcase and innovate, scale can only be reached in repeat transactions. Developing countries ambition to scale blended finance should take into account programmatic approaches to unlock private finance at scale. At the same time, it remains important to address LDC-specific characteristics when designing blended finance instruments, projects and programmes. Portfolio approaches that can cater to both ends, i.e. scaling private investment for instance at the fund level and tailoring the fund's financing products to local SMEs' needs, can be a tool to address this dual challenge.

2.3.3. Multi-stakeholder coordination is crucial to scale blended finance

Blended finance is a multi-stakeholder financing concept whose success strongly relies on bringing actors together that have different mandates, including developmental mandates and commercial mandates, as well as on combining different financial flows, including concessional or non-concessional development finance and private financial flows. To exploit the potential that blended finance can play in financing sustainable development, it is important to coordinate across the different stakeholder groups. The success of blended finance significantly depends on deploying development finance in such way that private investment is unlocked, while respecting all parties' respective mandates and risk appetites. This includes

the need to allocate risks between development and commercial parties in a balanced and sustainable manner (OECD, 2020^[42]).

Coordination is relevant at the country-level, at the actor-level and even possibly at the sector level. Coordination is for instance found to prevent project delays in the water and sanitation sector, as a result of, for example, foreign exchange discussions, late notice from regulators failing to support the impact on water and sanitation tariffs or procurement-related challenges. Moreover, more structural coordination in the water and sanitation sector is needed to address issues of subsidisation and concessional finance in particular in the context of mobilising private finance for water utilities (OECD, 2019^[24]).

Such issues can be addressed upfront by government-initiated coordination at the project as well as at the policy level. Coordination on blended finance should bring together governments and policy makers that can drive the enabling environment, intermediaries as commercial banks that structure transactions or asset managers, as well as providers of development and commercial capital. To bring partners together, efforts are being made through the Indonesian-led Global Blended Finance Alliance⁸.

For example, coordination on blended finance at an actor-level is taking place at the level of local development financial institutions in Brazil. The development actor landscape in Brazil is characterised by a decentralised and interlinked system, including national and sub-national development banks and agencies of different size and with different sectoral and geographic focus. Many of those are members of the Brazilian Association of Development Banks (Associação Brasileira de Desenvolvimento, ABDE), a platform for knowledge sharing to advance strategic priorities – including, for example, promoting the use of blended finance (Taskin, Bellesi and Moller, 2020^[12]). Such platform is a good example how official actors can initialise coordination on blended finance.

An example of a coordination approach at the country level is taken forward by the Sustainable Development Investment Partnership (SDIP), a joint initiative launched in 2015 by the World Economic Forum and the OECD. It brings together public and private stakeholders to increase private financing available to development outcomes. The Country Financing Roadmaps (CFRs) aim to identify priorities and pathways from a developing country perspective to scaling up financing (World Economic Forum, 2021^[62]). These roadmaps are developed in consultative efforts with local stakeholders, including governments and domestic private sector partners, as well as development actors. In 2020, such roadmaps were developed for Saint Lucia and Ghana. For Saint Lucia, a gap of local coordination was identified, in particular with respect to increasing private finance for the energy transition. As a result, a platform is planned to be created. For Ghana, two main areas for additional private investment were identified, including sustainable infrastructure and MSMEs. In response, it is for example planned to set up a dedicated Project Preparation Facility.

A crucial element of coordination is also communication. It is important that public and private parties speak “the same language”, formulate clear ambitions and expectations, and trust each other. On a fundamental level, a lack of clear and consistent language is crucial in developing and advancing a common understanding and framework of blended finance (OECD, 2018^[1]); (AVPN, 2022^[39]). To this effect, it may make sense to identify, implement and leverage the concept of “embedded advisors”, dedicated blended finance advisors, who bridge that gap between governments and private sector actors, for example as a hub for coordination and with respect to pipeline development, and capacity building. Additionally, in recognition of the need for close co-ordination and effective communication, the ADB is coordinating closely with other MDBs and DFIs, donors and commercial lenders to align reporting standards for projects, and ultimately avoid market distortions.

2.4. Improve impact management and measurement, and promote transparency

2.4.1. Understanding the why, where and how of blended finance is crucial for its targeted use

To navigate blended finance to where it can best play out its added value, an understanding of the opportunities and challenges of blended finance is needed, which includes transparency about financial and development impact-related characteristics (see Annex for an overview of blended finance data and evidence). While blended finance does not necessarily need a concessional element to unlock private investment, softer terms of financing are sometimes needed to direct private investment to sectors that do not (yet) attract stand-alone private finance. Information on the financial aspects such as volumes, terms and, in particular, the level of concessionality is needed at a sectoral and even transaction level to better understand how to crowd-in (and not crowd out) private financing. Additionally, information on results achieved through blended finance can help ensure that it helps mobilise quality private capital, e.g. private finance for investment in line with local development priorities.

This especially holds in the LDC context, where a higher level of concessionality may be needed to unlock investment, due to missing track records, market infrastructure or a challenging enabling environment. For example, the average concessionality levels in a selected sample of the IFC's blended concessional finance projects between 2010 and 2020 is highest in low-income and fragile and conflict affected states, compared to other themes such as agriculture, SME finance or gender finance (Karlin and Sierra-Escalante, 2021^[63]).

To that end, it is important that providers and developing countries work together towards enhanced transparency on blended finance by (1) supporting existing reporting efforts such as on the TOSSD, (2) making their finance – including when implemented by a third-party organisation – conditional with certain disclosure requirements, and (3) investigate additional transparency needs to make blended finance work, such as publishing data at the transaction level. For example, securitisation transactions require a substantive level of transparency – institutional investors require that data and definitions align with international standards such as Basel IV regulation for compliance purposes.

Similarly, it is essential to have a thorough understanding of the concept and impact of blended finance. Again, the choice for blended finance should be made based on the assessment that it is delivering the best outcomes on sustainable development within a given project among all financing options available. Importantly, blended finance needs to ensure both financial and development additionality. Therefore, stringent impact management and measurement practices should be embedded in any plan to scale blended finance flows.

The Impact Standards for Financing Sustainable Development, developed by the OECD and UNDP, are such an impact management tool that help to establish a beneficial collaborative role between implementing organisations and developing country governments. The Standards seek to optimise contributions to the SDGs, promote impact integrity and prevent impact washing. Grounded in International Labour Convention 169, IFC Performance Standard 2, the United Nations' Guiding Principles on Business and Human Rights, as well as the Busan Principles for Development Effectiveness, the Standards urge investors to fully and transparently align with local development priorities. As such, developing country governments can use the OECD-UNDP Standards help build a database as to what works and what does not in the local context - thus creating a positive feedback loop that serves to stimulate further investment (OECD, 2021^[64]). Standard 3, Transparency and Accountability, calls on partners to promote SDG- and impact-integrity by requiring them to disclose the sources of their data with investors and end-beneficiaries (as well as other relevant stakeholders), both ex-ante and ex-post, for the purposes of development results and monitoring. In addition, partners are encouraged to extend transparency to the more granular, operational level and to demonstrate the impact of their investments to their stakeholders (including at the local beneficiary level).

Blended finance – as a multi-stakeholder concept bringing together public and private sectors – has much to gain from efforts to align transparency and reporting standards. The finance and development communities are already beginning to adhere to various guidelines, standards, taxonomies as well as reporting and disclosure practices following Environmental, Social and Governance (ESG) criteria or the SDGs, respectively⁹. Therefore, it is important to align finance and frameworks and possibly move from ESG frameworks to the SDGs, which were initially designed as a government framework. While initial work is ongoing, more insights are needed as to the challenges developing countries face in adhering to ESG and SDG frameworks and how they can be better aligned with the needs of developing countries. Efforts in this direction could also be supported by work done under the INFF, especially INFFs building blocks “Financing Strategy” and “Monitoring and Review”.

2.4.2. Transparency and accountability on blended finance implementation and results are key in ensuring positive impact of blended finance

Transparency has been recognised as a crucial condition for private market growth (OECD, 2019_[65]). Yet, transparency remains a significant obstacle to the scaling and improvement of blended finance operations. This is despite the proliferation of investment organisations pledging alignment with impact management and measurement (IMM) initiatives. A recent blended finance report from the Tri Hita Karana Working Group underscored the urgency of greater transparency, as seen in the limited nature of impact data from blended finance projects (The Tri Hita Karana Roadmap for Blended Finance, 2020_[66]).

Research by Publish What You Fund (PWYF), the global campaign for aid and development transparency, has uncovered that examples of DFIs providing assurance of community disclosure are few and far between (under Work Stream 3 of their DFI Transparency Project). Among the examples that were found, assurance largely consisted of stakeholder engagement plans, which are limited to earlier stages in the investment cycle and future disclosure plans (Publish What You Fund, 2021_[67]).

Why is transparency so important for ensuring the positive impact of blended finance transactions? Access to data and the methodologies used to process it provides investors with the knowledge they require to make well-informed decisions. Additionally, it provides invaluable learnings for the improvement of future blended finance operations and increased knowledge of hitherto less advanced and active private markets. However, while more reliable and robust disaggregated and gender-sensitive data is needed to assess the results of blended finance (OECD/UNCDF, 2020_[15]), this data is still lacking and in many cases access to information – in particular on financial terms – remains limited to due confidentiality concerns (Winckler Andersen et al., 2019_[68]).

Accountability to stakeholders is a further key consideration that blended finance actors should strive to achieve. Transparency can, in this sense, be understood as a dual upstream (i.e. towards stakeholders such as donor governments, asset owners, asset managers, etc.) and downstream (i.e. towards local stakeholders and intended beneficiaries) process (OECD, 2020_[69]). Donors and private sector partners must uphold their responsibility to ensure that transparent, reliable, disaggregated and interoperable data on people and the planet “creates constructive feedback loops with affected stakeholders” (Impact Taskforce, 2021_[70]). The OECD Blended Finance Principles Guidance similarly emphasise that “transparency should not be seen as an end goal in itself, but rather as a facilitator of greater accountability, learning and trust” (OECD, 2020_[69]). Accountability to local stakeholders can, in turn, improve the quality of blended finance transactions through facilitating partnerships for access to in-depth local knowledge regarding the identification of good investment opportunities and understanding the effectiveness and compatibility of impact targets and results with local development priorities.

3 Suggestions for further G20 DWG dialogue and work

Blended finance flows are significantly lacking behind expectations. The COVID-19 pandemic has exaggerated the imperative for blended finance to work as an effective means of financing to contribute to filling the SDG financing gap. Actors across the blended finance ecosystem, including development actors and private sector actors, have to step up in making blended finance work for the SDGs. This scoping note outlines levers that developing country governments can pull in order to scale the flows of blended finance flows to their countries and their investment priorities. The G20 DWG is invited to consider the following suggestions, emerging from the analysis of various blended finance approaches and projects:

1. Take note of this Stocktake Report note and the opportunities outlined with the areas for action for developing country governments.

The Stocktake Report aims to build the basis for understanding the concept of and evidence on blended finance, as well as to distil opportunities to scale blended finance for sustainable development from a developing country government perspective, including addressing the associated challenges. Thereby, this effort aims to complement the existing evidence, standards and guidance in the blended finance landscape, including by (1) taking a developing country, including LDC and SIDS, government perspective, as opposed to a provider perspective (e.g. the OECD DAC Blended Finance Principles and Guidance, the DFI Working Group Enhanced Principles on Blended Concessional Finance for Private Sector Projects, etc.), (2) focusing on blended finance and its challenges associated with investments in social sectors (as opposed to well-established blended finance approaches in sectors such as energy and banking), and (3) paves the way to inform and derive actionable how-to-tools that help developing country governments to start and scale efforts on blended finance.

2. Discuss and develop G20 Principles to Scale up Blended Finance in Developing Countries, including in Least Developed Countries and Small Island Developing States

There is a gap in standards that speak to developing country governments' role in blended finance. A G20-led effort to provide Principles to *Scale up Blended Finance in Developing Countries, including Least Developed Countries and Small Island Developing States* can be considered an essential tool for these governments to enter or scale the blended finance ecosystem in their countries, with a view on increasing financing available for sustainable development. In order to fill the massive financing gap it is crucial to make the most out of all potential flows available, including blended finance. Such G20 Principles could help to confidently communicate about and act on blended finance ambitions vis-à-vis the development actors as well as the private sector.

3. Develop implementation guidance to turn the principles into an actionable how-to-tool

A complementing implementation guidance on the *G20 Principles* could turn those into a practical tool to achieve bigger impact on sustainable development. Such guidance could outline concrete actions to address the Principles, including tools as step-by-step processes, identifying the main actors of each step, or to-do lists. Guidance could be developed for official providers and MDBs, for corporates and private sector actors, and for developing countries in the form of a "How-to-Guide". This could serve to turn the

G20 Principles into reality and initiate policy change in developing countries that should be accompanied by notable progress in terms of blended finance flows going to LDCs, SIDS and into social sectors. The OECD stands ready to provide an update on analysis and data on a regular basis to identify and display any progress in that respect.

4. Engage in a dialogue with developing countries and with private sector representatives on the G20 Principles and related guidance

The OECD stands ready to support Indonesia in engaging further in dialogue with developing countries and with private sector representatives by mobilising stakeholder views across the blended finance spectrum in an inclusive way. This could take place for instance, through existing communities, such as the Tri Hita Karana Roadmap. Seeking the perspective of developing countries, including LDCs and SIDS, will be essential to create ownership and prepare policy changes that would lead to the improvement of blended finance approaches; similarly, it is essential to seek the perspectives of private sector stakeholders. The THK community is well placed for such a dialogue, as a multi-stakeholder effort to advance blended finance. Other dialogues and consultations could support this as well¹⁰.

4 Annex: The foundations of blended finance

4.1. Setting the scene on blended finance

4.1.1. Blended finance can bring together actors with a development mandate and actors with commercial return expectations

Blended finance is a financial structuring approach to support development outcomes (OECD, 2018^[1]). By deploying scarce development finance in a way that addresses investment barriers and improves the risk-return profile of investments, blended finance aims to attract commercial finance towards the achievement of the Sustainable Development Goals (SDGs) where stand-alone private investment is currently not available. In doing so, it has the ambition to be a market-building instrument that helps to create long-term impact by enabling private financial markets that are no longer dependent on grant and other donor financing.

Blended finance is the “strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries” (OECD, 2018^[1]), whereby additional finance concerns commercial finance that has not been invested for sustainable development before and that in general does not have a development purpose. This can for example include private financiers as commercial banks and other institutional investors such as insurance companies, but also official/public actors such as sovereign wealth funds that invest for market-level returns. By incentivising such private investors into transactions, geographic areas or sectors that they have not invested in before, blended finance models can help to build a track record, knowledge and capacity, as well as confidence of commercial investors in these areas. In line with its transitory nature, blended finance models aim to mobilise more and more commercial finance over time towards creating SDG compatible markets.

Development actors include governments, their ministries of development co-operation and their aid agencies that have traditionally provided grants, other forms of concessional financing but also non-concessional finance for development. Their development finance can be either provided and invested directly, e.g. by their aid agencies, or indirectly, e.g. via funds and facilities managed by public and private partners. They are major providers of official development assistance (ODA), which in 2021 amounted to USD 178.9 for all DAC member countries combined, it's peak to date (OECD, 2022^[71]).

Similarly, developing countries' and emerging markets' partner governments have a development mandate. Moreover, as policy makers and regulators they are responsible for creating a conducive investment climate for commercial and private finance. In addition, they can act as concessional finance providers in blended finance solutions (OECD, 2021^[5]; OECD, 2020^[40]).

In the same vein, national development banks (NDBs) are important development actors by providing crucial funding and mobilising private investment in support of the SDGs in their respective countries. Just under two-thirds of LDCs have an NDB (OECD/UNCDF, 2020^[15]). NDBs can provide longer-term, affordable local currency financing than is available on the market as a result of their development mandate

and financing models (Taskin, Bellesi and Moller, 2020^[12]). Their knowledge of local markets and long-standing relationships with local private and public sector actors should be built upon and exploited for an integrated approach to scaling blended finance in developing countries and LDCs.

Multilateral development banks (MDBs) and development finance institutions (DFIs) have a dual mandate to invest for development and at the same time being commercially sustainable while doing so. That is, commercial returns are sought in their private sector operations, in which they can act as mobiliser of private finance and hence arrange blended finance approaches. At the same time, they engage also in deploying concessional capital provided by donors via e.g. facilities or technical assistance programmes.

Philanthropic actors can provide the catalytic development finance needed to mobilise private finance into projects for sustainable development in developing countries and LDCs. Often, those actors provide grants, technical assistance and, increasingly, repayable funds, such as programme- or mission-related investments. Latest OECD data (OECD, 2022^[72]) shows that foundations' financing for development has grown steadily, with a peak at USD 10.3 billion in 2020, of which 10% was provided in non-grant form. The foremost financing priorities by far include the health and population sectors (USD 4.9 billion), mainly driven by the Bill and Melinda Gates Foundation (66%) and the Wellcome Trust (11%).

Finally, market makers such as Convergence Blended Finance provide a matchmaking platform and grant funding for project design to increase the number of blended finance transactions, bringing together public, private and philanthropic actors for sustainable development. The database features almost 680 blended finance transactions with over 1450 public, private and philanthropic organisations of USD 160 billion (Convergence, 2021^[73]).

Such development finance providers can strategically deploy their funds to unlock commercial investment, which stems from sources that have a commercial mandate and seek market-level returns and, at the same time, would not invest in development-related projects in developing countries and LDCs otherwise. This includes commercial banks, who can provide loans or arrange transactions, national investment funds such as pension funds or sovereign wealth funds, institutional investors such as insurance companies, asset managers or asset owners, as well as project developers that prepare infrastructure projects (OECD, 2021^[5]; OECD, 2020^[40]).

Institutional investors have the capacity to fill a significant portion of the SDG investment gap in developing countries, holding trillions in assets worldwide (OECD, 2020^[74]). Moreover, they have the long-term outlook required for investing in the SDGs over a long horizon (OECD, 2018^[1]). However, institutional investors have a low-risk appetite, typically preferring long-term (and investment-grade) fixed income assets with low liquidity requirements – which does not match the needs of investees in developing countries and the LDCs (OECD, 2020^[42]; OECD, 2021^[10]). Indeed, in 2017-18 pension funds allocated a meagre 8% of their assets to developing countries, countries in Asia such as People's Republic of China or India. In the same vein, insurance companies allocated an even smaller share to developing countries with 2% in 2017-18 (OECD, 2021^[10]). Blended finance models can help to de-risk, enhance return and reduce information asymmetries for international institutional investors in developing countries. At the same time, investment regulation in countries that host such institutional investors is also identified as a recommendation to tackle in order to scale this share.

For now, pension funds and insurance companies represent only 4% of the assets under management across blended finance funds and facilities (Demebele et al., 2022^[75]). Crucially, when considering scaling the potential role of institutional investors in developing countries, local institutional investors need to play a much stronger role. They are significant in the development of local capital markets; much like NDBs, local institutional investors benefit from an in-depth understanding of the local investment landscape, enabling them to take better informed risks, and local institutional investors such as pension funds or sovereign wealth funds are crucial providers of local currency finance (OECD, 2021^[10]).

4.1.2. Blended finance can refer to a variety of financial instruments that unlock private finance at the project or portfolio level

Rather than a financial instrument in itself, blended finance refers to a set of established financial instruments (or mechanisms) that are deployed (1) in a way that development finance unlocks private finance and (2) in the context of sustainable development in developing countries and LDC.

Instruments include for example direct investments in companies and project finance vehicles (so-called “Special Purpose Vehicles” (SPVs)) that are exclusively set up for one particular purpose, i.e. a solar power plant), which can take the form of debt, equity or mezzanine/hybrid finance. Such traditional financial instruments provided by development finance providers in the context of blended finance and financing for sustainable development more broadly can back private investors’ confidence in particular projects – which is also the case when finance is priced at market-rates. They can furthermore improve the risk-return relationships for private investors when placed at concessional rates, or with an extended repayment schedule, or addressing pricing gaps. Concessional finance can reduce the weighted average cost of capital for the investee and hence improve financial sustainability of the business, which in turn can mobilise other private investors.

Aside from direct investment in companies and SPVs, debt instruments also include for example credit lines that provide liquidity to local financial institutions that can be drawn upon during a certain timeframe up to a certain amount, for example to on-lend to a specific borrower group that has not been catered to before. Mobilisation of private finance can take place at the financial institutions’ level, which matches or tops-up the finance drawn from the official credit line, or the additional equity invested into a project by the end-borrower (OECD, 2020^[76]). Moreover, syndicated loans are an effective tool to mobilise private finance. Multilateral Development Banks (MDBs) and some bilateral Development Finance Institutions (DFIs) typically take the role of the arranger in a certain credit exposure, while the total loan amount can also combine financing from other lenders, for instance from the private sector that would not lend to a developing country recipient without the arranger.

Equity investments can also mobilise significant private finance. For example, some MDBs and DFIs acquire stocks in private enterprises in developing countries, alongside with other private investors. This also allows them to exercise their additionality through active ownership to enhance the development impact of the companies’ daily business.

Guarantees have emerged as a prominent instrument that can unlock private finance at scale. In a guarantee in the context of blended finance, typically a development actor such as an MDB or government agency guarantees to pay an agreed-upon amount. This amount is paid to a commercial investor that provides a loan to a local borrower or injects equity in a project in a developing country in case a full or partial default occurs. Some providers also issue portfolio guarantees to local banks. The default can stem from various credit or political risks. While guarantees have benefits with respect to building markets and unlocking private finance, they require that e.g. a sound enabling environment is in place in developing countries and LDCs, such as the legal framework to deal with guarantee claims and recoveries (Garbacz, Vilalta and Moller, 2021^[56]), but also in respect to providing guarantees. That is, the institutional set-up and capacity required for underwriting credit guarantees needs to be created (OECD, 2021^[19]). Finally, in the context of political risk guarantees, partner governments are closely involved for example with providing a counter-guarantee or providing approval before issuance (Garbacz, Vilalta and Moller, 2021^[56]).

Similarly, insurance instruments can protect investors against losses occurring from non-payment of borrowers. These instruments are often conditional to particular risks, situations, types of damage and contingent damages and losses such as adverse weather events (Garbacz, Vilalta and Moller, 2021^[56]). Insurance products have proven effective in mobilising private finance in the infrastructure space, for example with respect to covering physical risk or technical risk. At the same time, their importance in the

context of mobilising private finance for climate change adaptation is increasing (see Box 2.8. Leveraging private risk coverage capacity with development finance for climate change adaptation).

Grants and technical assistance have an important role in the context of blended finance and unlocking private finance. Grants are direct monetary contributions without the expectation of repayment in the future. For example, technical assistance (TA) grants can prove of key importance during the project preparation phase, including in the form of feasibility studies that contribute to the overall success of a project and consequently boost investor confidence (OECD, 2018^[11]).

The strategic use of development finance hence has the potential to crowd-in private finance at a project-by-project level. At the same time, to reach scale, and to address private investor concerns for example with respect to small ticket size and risk diversification, portfolio approaches to mobilising private finance have proven to be effective, though so far not at large scale.

Blended finance funds – or collective investment vehicles (CIVs) – enable private investors to access a portfolio of projects, for example a portfolio of loans to microfinance institutions (MFIs) or equity investments in SMEs in developing countries and LDCs. Such vehicles can be structured in a way that different tranches of risk and return exposure are available to different types of investors – naturally, the riskiest first loss tranche is associated with the highest risk and hence highest return expectations, in the absence of concessional development capital. Any losses incurred to the investment fund would first be attributed to the riskiest tranche investors, which provides risk protection to the investors of senior tranches. To attract private capital, official investors in CIVs often seek to play a de-risking role, for example through acquiring first-loss shares or improving the fund's market profile through anchor investing. This way private investors are mobilised into structured funds.

CIVs are playing an increasingly important role in blended finance. The assets under management (AUM) captured by the OECD Blended finance Funds and Facilities Survey have steadily increased since 2017. The 2020 survey captures 198 CIVs with USD 75 billion assets under management, with most of this amount (USD 45 billion) channelled through blended finance facilities. The value of these AUM represents an increase of 24% over the 2018 survey (USD 60.2 billion) and a 152% increase over the 2017 survey (USD 29.6 billion) (Dembele et al., 2022^[75]).

Credit risk sharing or transfer mechanisms are another set of instruments to increase financing available for SDG-relevant projects in developing countries and LDCs, and mobilise private investors into such portfolios of projects which they would not have access to normally. This includes, among other tools, securitisations, risk sharing facilities or portfolio guarantees. While these types of instruments are long established, development actors can exploit these instruments strategically and engage to unlock private investment at scale. In doing so, these instruments become blended finance. Securitisations for example enable originators of loans – such as MDBs¹¹ or commercial banks – to share the credit risk of an existing portfolio of SME or infrastructure loans with private and/or developmental investors. As a result, by selling such risks, those financial institutions are able to do more of their day-to-day business. Credit risk sharing facilities, furthermore, work similarly by providing risk protection to financial institutions in developing countries and LDCs in such way that those are enabled to expand their operations to areas of perceived higher risk, including MSMEs, women and youth entrepreneurs, for example (see Box 2.1. Supporting the growth of microenterprises and MSMEs).

Bonds, another type of debt instrument, are an asset class that allow institutional investors to gain access to tradable securities linked to a diversified range of underlying SDG-relevant projects in developing countries. Simultaneously, 'Green, social, sustainable and sustainability-linked' (GSSS) bonds allow issuers – such as governments, financial institutions or corporates - to diversify their sources of funding (Dembele, Schwarz and Horrocks, 2021^[77]). An important advantage is that bonds provide long-term financing, especially where the short maturity of bank liabilities and a lack of instruments to hedge duration risks fall short of the longer-term horizons of SDG-linked projects (Dembele, Schwarz and Horrocks,

2021^[77]). Such longer horizons have the added benefit of drawing in institutional investors seeking long-dated bonds.

Yet, bond markets in general remain limited in many developing countries. A key limitation preventing greater investments in green (or social, sustainable and sustainability-linked) bonds is that institutional investors typically look for investment-grade rated projects, filtering out higher-risk projects. Without credit-enhancement mechanisms that would improve the risk-return profile of GSSS bonds, many projects remain unfeasible (Dembele, Schwarz and Horrocks, 2021^[77]).¹²

4.2. Latest trends on the mobilisation effect of blended finance interventions in developing countries and the LDCs

Most blended finance activities aim at mobilising private investment for development purposes and, therefore, involve both private and public finance. This section presents the main trends and characteristics of private finance mobilised by official development finance interventions in developing countries. It describes the distribution and characteristics of the resources mobilised from the private sector by blended finance interventions in developing countries over the last decade, with a specific focus on LDCs. It also offers additional insights from the TOSSD data on the public interventions themselves.

4.2.1. Measuring mobilised private finance at the international level

Mobilising finance for the implementation of the SDGs from all sources, particularly from the private sector, has been at the heart of the 2030 Agenda, in particular given the massive financing needs (see Chapter 1). Accelerating the mobilisation of additional finance especially towards the LDCs is urgently needed as these countries face specific challenges in implementing the 2030 Agenda and are lagging behind in most of the SDGs, notably due to limited access to basic services, lack of human capital and financial resources, weak economic growth, high economic and environmental vulnerabilities and other.

In consultation with bilateral and multilateral providers, and following a high-level mandate provided by development co-operation ministers (OECD DAC, 2014^[78]), the OECD has established an international standard for measuring and collecting data on the amounts mobilised from the private sector by official development interventions. Work to develop this standard has been carried out over multiple years through successive rounds of research, surveys and workshops. Methodologies have been developed and implemented for measuring the amounts mobilised from the private sector for all main mechanisms used by bilateral and multilateral development finance providers: syndicated loans, guarantees, credit lines, direct investment in companies or special purpose vehicles (SPVs), shares in collective investment vehicles (CIVs) and simple co-financing arrangements.

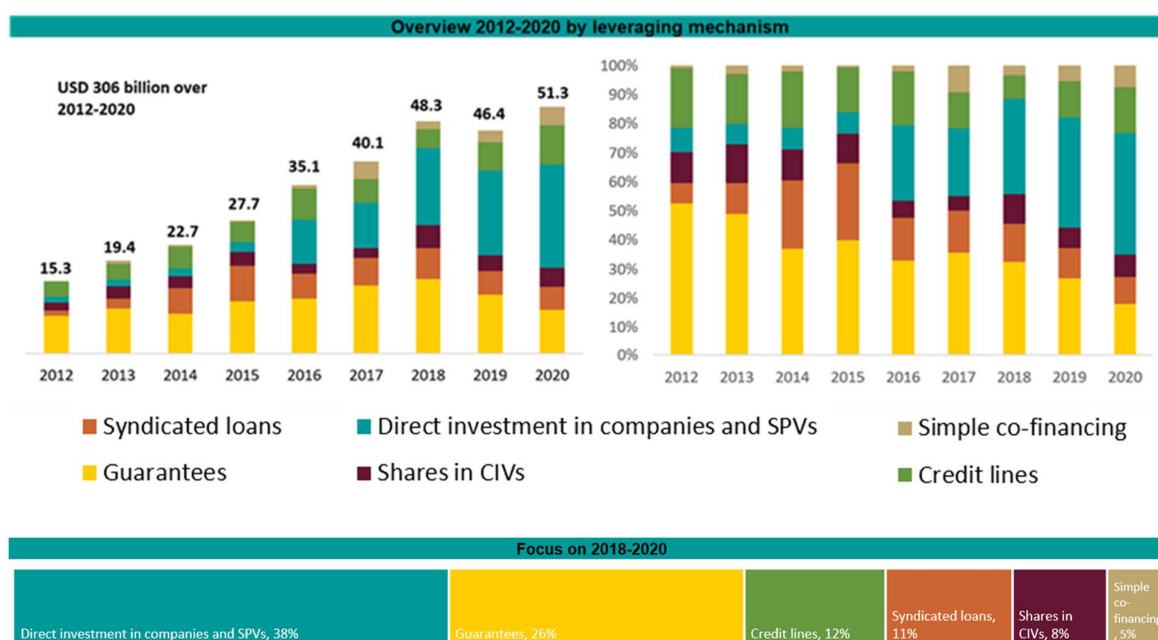
Over the last decade, blended finance activities, in particular their potential to mobilise private finance at scale, has become an increasingly important element in development co-operation providers' toolkit and policies. The new international statistical standard Total Official Support for Sustainable Development (TOSSD) aims to measure the full array of resources in support of sustainable development (see Figure 4.10), including blended finance operations and the resources they mobilise from the private sector. Blended finance activities are separately identifiable in TOSSD as a distinct financing arrangement, and mobilised private finance constitutes a key building block of the new framework. TOSSD is meant to bring further transparency on these operations and to incentivise greater use of leveraging mechanisms in countries and sectors in need – such as the LDCs and social sectors – where the perceived risk by potential investors is high.

4.2.2. Mobilised private finance mainly benefitted economic infrastructure and services in MICs

Between 2012 and 2020, USD 306 billion were mobilised from the private sector by official development finance interventions (Figure 4.1). Private finance mobilised towards developing countries grew overall in 2012-20, with a peak in 2020, but decreased from 2018 to 2019.

The latest trends show that, in 2018-20, direct investment in companies and special purpose vehicles (SPVs) mobilised over a third (38%) of private finance, followed by guarantees (28%), credit lines (12%) and syndicated loans (11%). To a lesser extent, shares in collective investment vehicles (CIVs) and simple co-financing also contributed to mobilising private finance, representing respectively 8% and 5% of the total. However, all these instruments play an important role in mobilising private finance by responding to the specific needs and investment barriers of developing countries, such as de-risking, intermediation, project size or actual development in specific sectors.

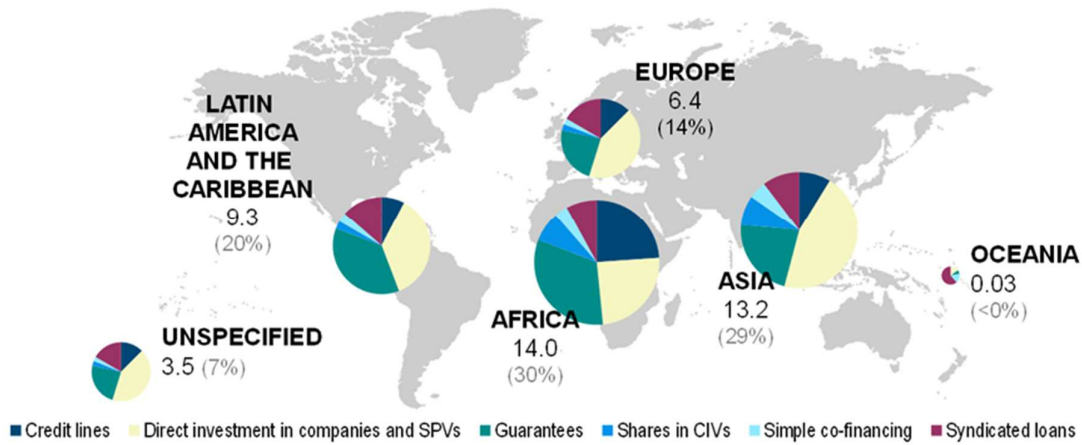
Figure 4.1. Trends of mobilised private finance by instrument, 2012-2020 in USD billion



Source: (OECD, 2022^[11])

Furthermore, in 2018-20, mobilised private resources were evenly distributed across Africa (30%), developing countries in Asia (29%) and Latin America and the Caribbean (20%) (Figure 4.2). Mobilised private finance towards developing countries in Europe accounted for a smaller share (14%). While private finance mobilised for Africa was distributed over a relatively large number of recipients, it was much more concentrated in the case of Asia and Latin America and the Caribbean, with around half of these latter regional totals having benefitted top three recipients only. Moreover, India, People's Republic of China, Turkey, Egypt and Brazil were the top beneficiaries of mobilised private finance during this period, together accounting for 58% of total private finance mobilised in 2018-20.

Figure 4.2. Private finance mobilised by geographic allocation and leveraging mechanism, 2018-2020 average, in USD billion

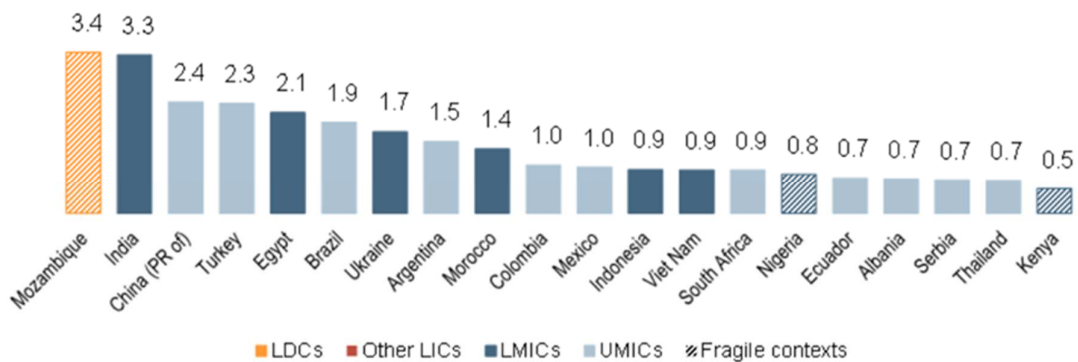


Note: 2020 data are preliminary.

Source: (OECD, 2022_[11])

As regards the distribution by income group, only 15% was mobilised for the LDCs (see Figure 4.3), while around two-thirds (67%) of private finance targeted middle-income countries (MICs), with lower middle-income countries (LMICs) accounting for 33% and upper middle-income countries (UMICs) for 35%. The remaining 18% was not allocable by income group. While being the country that mobilised the largest volumes of private finance in the period of 2018-2020, Mozambique was the only LDC among the top 20 recipients; and the level of private finance mobilised was driven by a few large-scale LNG projects in 2020. Private finance for fragile contexts amounted to USD 10 million per year on average (24%) in the three-year period, whereas projects in SIDS mobilised around USD 0.4 billion (1%) of private finance per year on average over the same period.

Figure 4.3. Top 20 recipients of private finance mobilised by income group, 2018-2020, USD billion



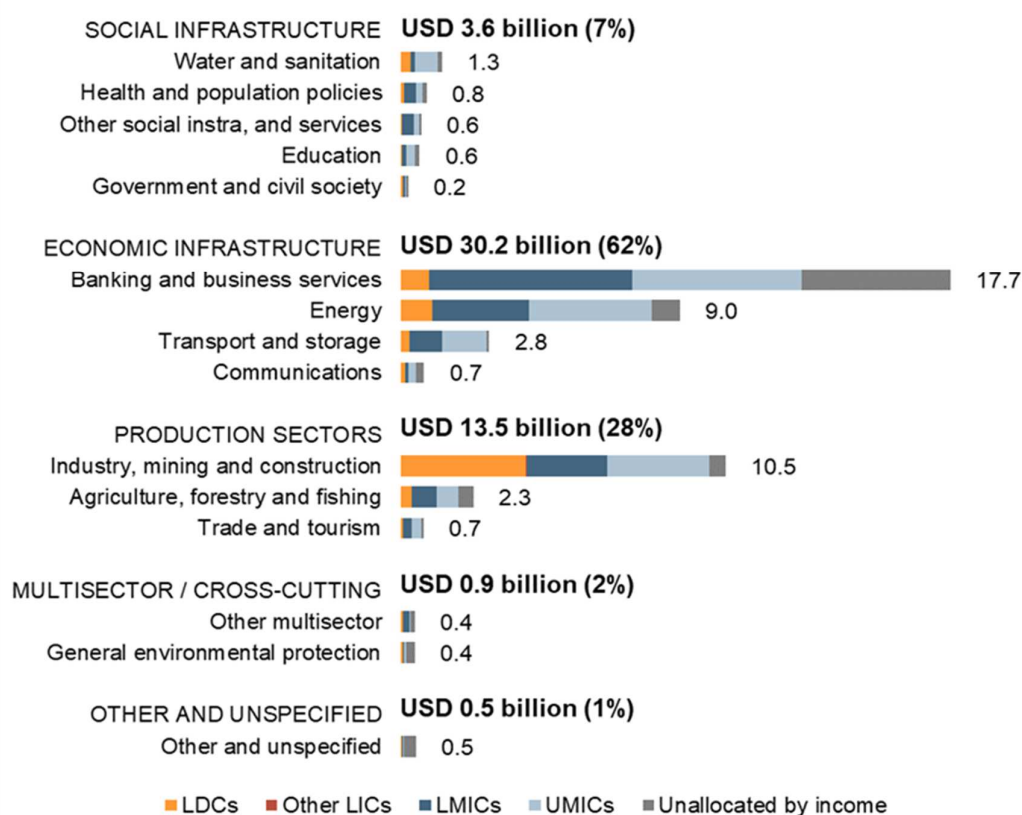
Source: (OECD, 2022_[11])

Moreover, the data show that direct investment in companies and project finance SPVs was the mechanism mobilising the largest shares of private finance – around a third of private finance in the MICS and 56% in the LDCs. However, the relatively high share for the LDCs related to a limited number of large-scale projects in one country. Beyond these specific projects, guarantees are the main leveraging mechanism in the LDCs.

As shown in Figure 4.4, **only 7% of total mobilised private finance targeted social sectors in all developing countries, mainly benefitting water supply and sanitation projects (3%)**. Here, most of private mobilisation related the construction and maintenance of water supply infrastructure, hospitals, laboratories and other health facilities. The majority (62%) of mobilised private finance however targeted economic infrastructure sectors. Mobilised private finance for production sectors, such as industry and agriculture, amounted to USD 14.5 billion (28%). Regarding the latter, it is important to note that small family farms as well as small and medium-sized enterprises (SMEs) are the majority of enterprises in the agri-food sector in many developing countries. While these enterprises can contribute to a range of SDGs, many do not have sufficient access to finance to fulfil their potential. Blended finance models can improve financial inclusion, and can, particularly through technical assistance and/or grants – stimulate the creation of new markets and value chains around agri-SMEs (OECD, 2021^[17]).

Approximately 32% of mobilised private finance aimed at mitigating or, to a lesser extent, fostering adaptation to climate change. The data suggest that the higher the income group, the higher the share of climate finance in total private mobilisation.

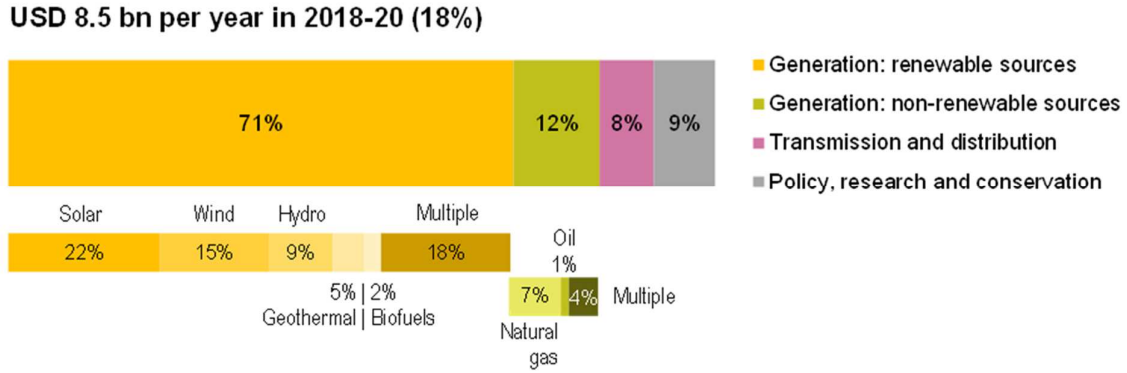
Figure 4.4. Private finance mobilised by sector and income group, 2018-2020, in USD billion



Source: (OECD, 2022^[11])

A focus on the energy sector shows that although over two-thirds (71%) of mobilised private finance for the energy sector targeted renewable energy projects- in particular solar and wind energies – energy generation from non-renewable sources accounted for 12% of the sector (see Figure 4.5).

Figure 4.5. Private finance mobilised for the energy sector in 2018-20

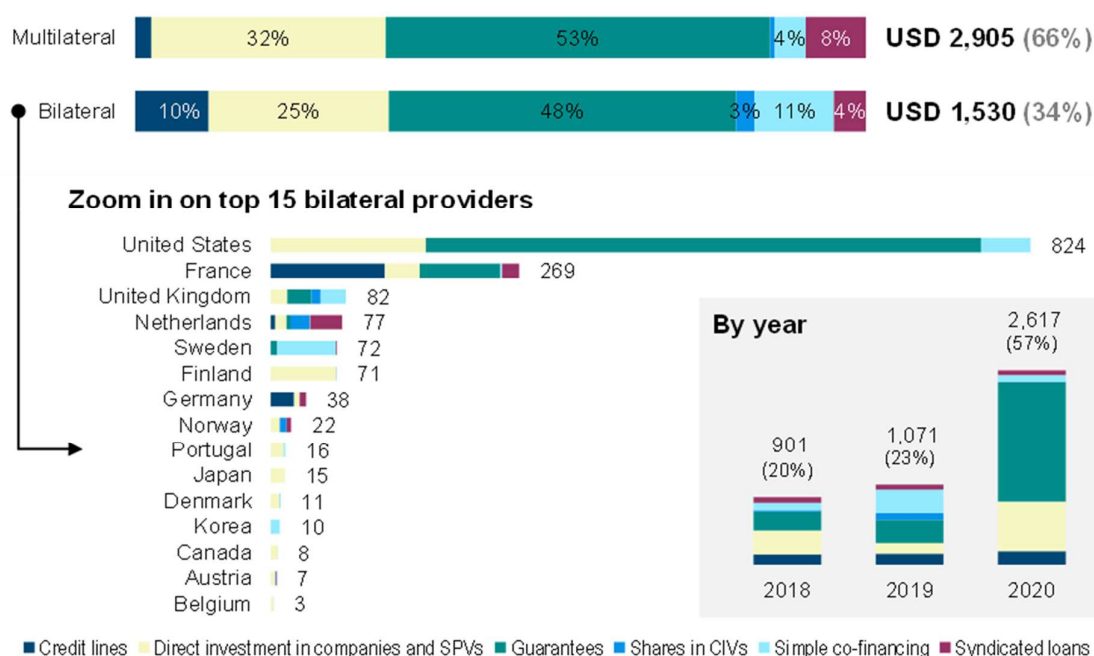


Note: 2020 data are preliminary.
Source: (OECD, 2022_[11])

A deep-dive into private finance mobilised in the LDCs

In 2018-20, multilateral organisations were key players in the LDCs, having mobilised two-thirds (66%) of the total on average in 2018-20 (see Figure 4.6). The remaining resources were mobilised by bilateral providers, most notably the United States (19%), France (6%) and United Kingdom (2%). Over the three years, private mobilisation by bilateral providers increased significantly, although this trend is mainly explained by a few large-scale projects in Mozambique in 2020.

Figure 4.6. Mobilised private finance for the LDCs by provider and leveraging mechanism, 2018-20 average, USD million

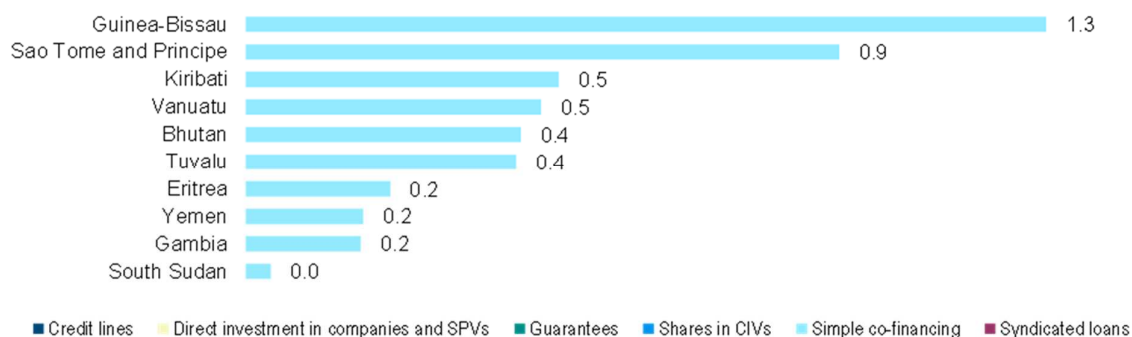


Note: 2020 data are preliminary. Data disclosure rules agreed with the MDBs do not allow for further disaggregation, including by multilateral agency. Other bilateral providers mobilising private finance for the LDCs in 2018-2020 included Luxembourg, Ireland, Spain, Czech Republic, Slovakia, Romania, Slovenia and Estonia.

Source: (OECD, 2022^[11]).

In addition, mobilised private finance for the LDCs appeared rather concentrated geographically, with almost half of the total (47%) benefitting projects in five countries, namely Mozambique, Uganda, Bangladesh, Guinea and Angola. Still, private mobilisation in each of these countries was primarily driven by a few large-scale projects supported by a limited number of providers, which also affects the instrument breakdown. In addition, the bottom 10 LDC recipients together received a mere USD 5 million per year, representing 0.1% of total private finance mobilised for the LDCs. All of these amounts were mobilised through simple co-financing arrangements (see Figure 4.7).

Figure 4.7. Bottom 10 LDC recipients by leveraging mechanism, 2018-20 average, USD million



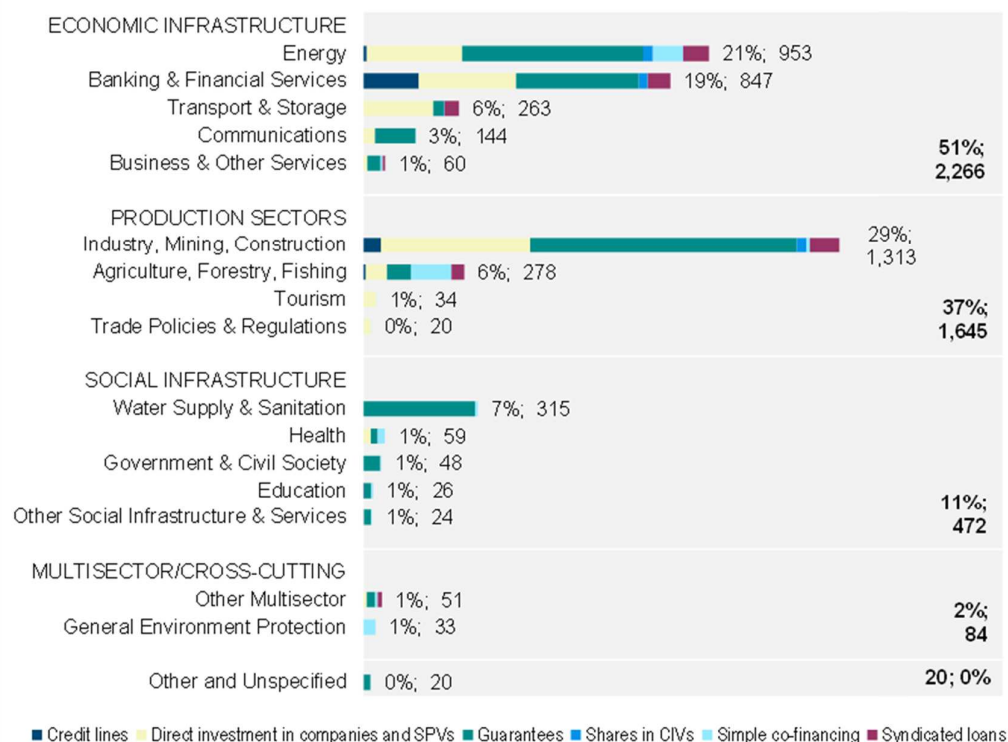
Note: 2020 data are preliminary.

Source: (OECD, 2022^[11]).

As shown in Figure 4.8, the sectoral distribution of mobilised private finance in the LDCs followed a similar pattern as in the rest of developing countries, with economic and production sectors representing most of their total mobilisation. Yet, compared to the MICs, projects in the economic infrastructure and services benefitted from a relatively smaller share of mobilised resources while a larger share targeted the production and social sectors in the LDCs. Nevertheless, **mobilised private finance in the LDCs' social sectors – sectors in most need – remained rather modest, representing only 11% of their total mobilisation for this country grouping.**

Another difference between private finance mobilised in LDCs and the rest of developing countries is the allocation of resources within sector groups. For example, within the energy sector, **the share of energy generation through renewable sources was lower in the LDCs (58%) than across all developing countries (71%).** Similarly, private mobilisation for energy transmission and distribution in the LDCs accounted for 16% of the total allocation of mobilised resources for the energy sector, which is twice the share in comparison to all developing countries. In terms of financial instruments, guarantees – and to a lesser extent direct investment in companies or SPVs – were mostly used in LDCs for mitigating investment risks in the energy, financial and industry sectors, as well as for the supply of basic services such as clean water and sanitation. Interestingly, most of private mobilisation in LDCs' social sectors happened through guarantees, reflecting particularly high-perceived risks and the little incentives for the private sector to invest in these areas.

Figure 4.8. Sectoral distribution of private finance mobilised for the LDCs, 2018-20 average, USD million

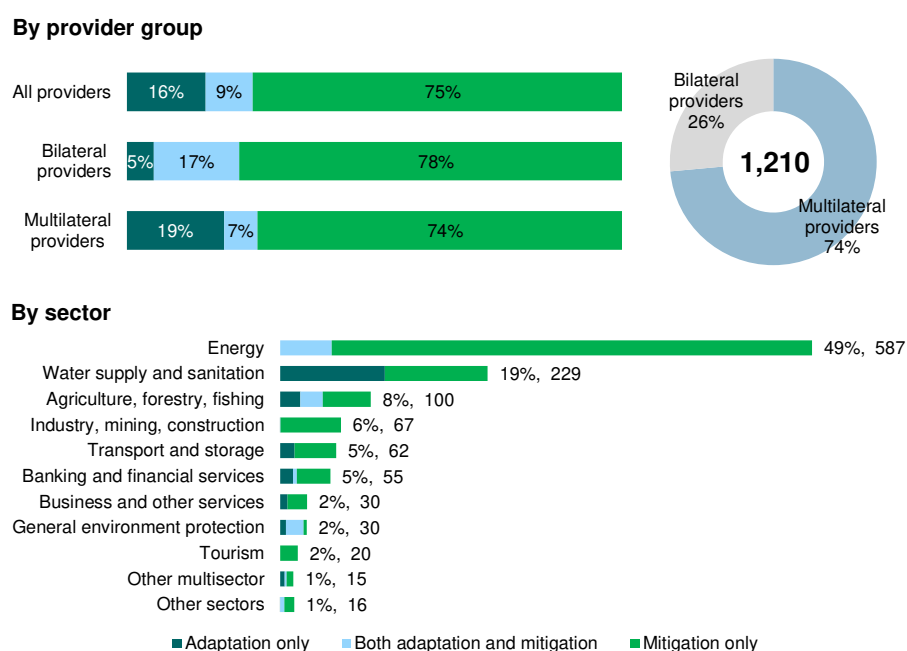


Note: 2020 data are preliminary.

Source: (OECD, 2022^[11]).

On average, in 2018-20, 27% of mobilised private finance for the LDCs aimed at addressing climate change mitigation and/or adaptation (see Figure 4.9). While mobilised private climate finance for both mitigation and adaptation activities followed an upward trend during 2016-19, data for 2020 indicate a significant drop, partly due to the COVID-19 pandemic. Three-quarters of these financial resources aimed at mitigation only, 16% adaptation only and the remainder of 9% targeted both mitigation and adaptation objectives. Although bilateral providers contributed 26% of total mobilised private climate finance, most of such resources resulted from mobilisation efforts by the MDBs and other multilateral agencies. Top bilateral providers in this respect included the Netherlands, Sweden, United States and France. A quarter of private finance for climate action in the LDCs was mobilised for the LDCs, 16% of which was for adaptation only. As indicated in Figure 4.9 most finance for climate change adaptation was mobilised by multilateral organisations. While mobilised private resources for mitigation mostly targeted projects in the economic and production sectors, a majority of private finance for adaptation was distributed over the water and sanitation and agriculture sectors.

Figure 4.9. Climate relevance of private mobilisation for the LDCs, 2018-20 average, USD million



Note: 2020 data are preliminary.

Source: (OECD, 2022_[11]).

Box 4.1. Private finance mobilised for health in the LDCs

Under-five mortality, maternal mortality and stunting are key indicators identifying the LDCs (UN, 2022^[79]). Still, **mobilised private finance for health, population and reproductive health only amounted to USD 59 million per year in 2018-20, representing only 1% of the total mobilised for LDCs**. Although most projects related to small grant subsidies in simple co-financing (mobilising less than USD 1 million each), Japan, United Kingdom, France and a few MDBs also deployed some guarantees, equity investments and loans to attract private sector for the construction of medical education facilities or for-profit health infrastructure and services. Almost two-thirds (60%) of private finance mobilised for health and population in the LDCs benefitted Bangladesh, followed by Benin (32%).

However, this limited focus was counterbalanced by Official Development Assistance (ODA). For example, 18% of bilateral ODA to LDCs extended by DAC members targeted health, population and reproductive health sectors. For some LDCs, ODA to health sectors accounted for more than 50% of their total bilateral ODA receipts, such as Lesotho (85%) and Zambia (55%). Private philanthropic foundations were also key players in supporting health sectors in developing countries (USD 4.5 billion, representing 45% of the total), with USD 1.1bn allocated to LDCs, 44% of which for health sectors.

Overall, this suggests that financing for development in LDCs, and in support of social sectors in particular, still seems to have a limited capacity to attract large volumes of private finance. Therefore, development co-operation providers should continue to use scarce concessional resources (especially ODA) to target countries and sectors most in need.

Source: (OECD, 2022^[11]).

4.2.3. Emerging evidence on the official interventions that mobilise private finance for sustainable development

A new statistical measure for the SDG era: TOSSD

TOSSD is a new statistical framework, specifically designed to measure resources for sustainable development and for the SDGs. It tracks official i) cross-border resource flows to developing countries and ii) global and regional expenditures, in support of development enablers, International Public Goods and to address global challenges. It also includes resources mobilised from the private sector by official development finance interventions. It is designed to provide a coherent, comparable and unified system for tracking SDG-relevant investments that can inform the international community about how the SDGs are being financed globally and at the partner country level.

Following the recognition of TOSSD in the Addis Ababa Action Agenda in 2015, an International Task Force composed of statistical experts and development policy specialists from emerging and developed economies, recipient countries, as well as international organisations was established in July 2017. The main objective of the Task Force has been to develop TOSSD Reporting Instructions, which define the main statistical parameters (definitions, measurement methods, taxonomies) of the framework. The OECD currently hosts the Secretariat of the Task Force and maintains the TOSSD database.

How can TOSSD help tracking support to blended finance approaches?

The new international statistical framework TOSSD can help fill a critical data gap on blended finance activities and aims to valorise the amounts mobilised by official development finance.

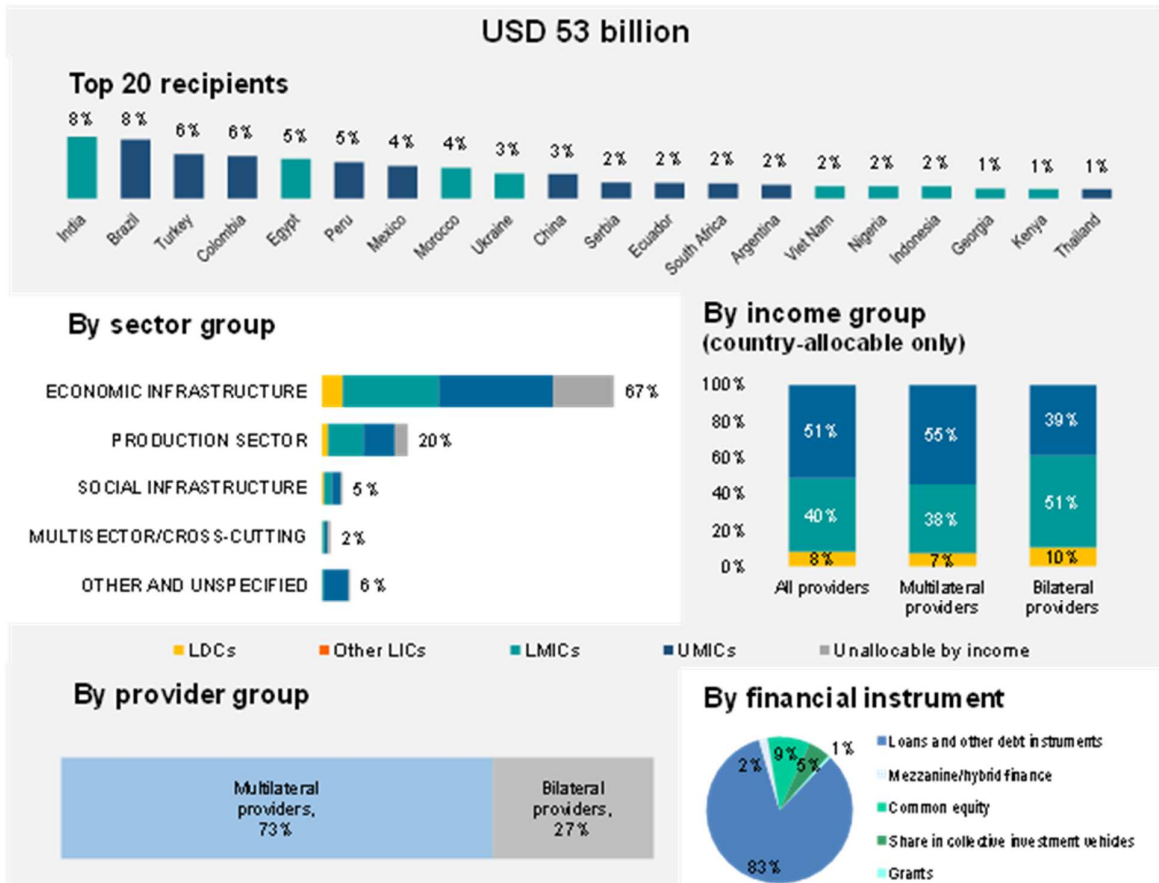
TOSSD makes data available on blended finance activities and the amounts they mobilise, by looking also the allocation of global resources for sustainable development. In addition, TOSSD pillar I brings further transparency on all officially supported resource flows to developing countries in support of the SDGs, including on south-south and triangular co-operation. These do not only include financial flows extended by provider countries and multilateral organisations, but also SDG-aligned investment from sovereign wealth funds and public pension funds.

Insights from the first TOSSD data collections

The first comprehensive set of TOSSD data on 2019 activities was published in March 2021. Around 90 providers had reported their support for sustainable development, including through blended finance mechanisms, to the TOSSD framework in the first regular data collection round. More providers, including south-south providers such as Brazil, are expected in the 2022 TOSSD data release (TOSSD, 2022^[80]). In order to provide a picture of all official interventions that contribute to mobilise private finance, a way that is as comprehensive as possible, the TOSSD data related to blended finance were complemented with “other activities in support of private sector development”.¹³ The latter are defined as loans to the private sector, mezzanine/hybrid finance and equity investments (excluding contributions to the core budgets of multilateral organisations).

According to the available data on 2019-20 at the time of drafting this report, **development co-operation providers committed approximately USD 53 billion per year on average in blended finance and other activities in support of private sector development.**¹⁴ As highlighted in Figure 4.10, almost three-quarters (73%) of this amount was provided by the MDBs and other multilateral organisations, largely driven by the International Finance Corporations (IFC), EU Institutions, European Bank for Reconstruction and Development (EBRD) and Development Bank of Latin America (CAF). Bilateral providers provided the remaining 27%, with finance committed by Germany, United States, France, Norway and the United Kingdom accounting for 24% of the two-year total.

Figure 4.10. Blended finance and other interventions in support of private sector development in 2019- 20, commitments, USD billion



Note: 2020 data are preliminary

Source: TOSSD complemented with CRS for providers not reporting to TOSSD.

Furthermore, similarly to mobilised private finance, evidence suggests that **blended finance and other activities for private sector development are primarily directed to middle-income countries (92%)** with perceived lower commercial and political risks. Fifty-one per cent of country-allocable commitments in this field targeted UMICs across all regions. India, Brazil, Turkey, Colombia and Egypt being the largest recipients of blended finance and other support for private sector development. Only 8% of these amounts targeted the LDCs, with Bangladesh, Myanmar, Mozambique, Cambodia and Guinea accounting for more than a half of the LDC total. The share of blended and other finance for private sector development allocated to the LDCs was somewhat higher in the case of bilateral providers (10%) that the MDBs and other multilateral organisations (7%).

Approximately two-thirds (67%) of blended finance and other activities for private sector development were aimed at developing recipients' economic infrastructure and services, mainly focusing on banking and financial services (45%) and the energy sector (13%). A fifth of these amounts were allocated to production sectors, such as industry and agriculture. **Only 5% targeted social infrastructure and services**, mainly targeting water and sanitation and to a lesser extent also health and population. As regards the LDCs, the sectoral distribution followed a similar trend: 71% aimed at economic infrastructure and services with a particular focus on energy (29%) and banking (23%), 21% for production

sectors and 7% for social infrastructure and services, 5% of which in the water and sanitation sector. Accordingly, SDGs 7, 8 and 9 benefitted from the largest volumes of blended finance and other private sector development activities in the LDCs and beyond.

When compared to private finance mobilised, **blended finance and other private sector development activities show many similarities but also some differences**. In both cases, around 80% of finance benefitted developing countries in Africa, Asia and Latin America and the Caribbean, with private mobilisation mainly supporting projects in Africa and official finance being dominant in Latin America and the Caribbean. MICs were the foremost recipients with four of the top five recipients of official and mobilised private finance being identical, namely Brazil, Egypt, India and Turkey. Looking at the LDCs, three of the first five recipients were the same, i.e. Bangladesh, Mozambique and Guinea. Similarly, both official and mobilised private finance showed a distinct focus on economic infrastructure and services (around two-thirds of the total) and banking and financial services and the energy sector in particular, accounting for around two-thirds of the respective totals. Social sectors benefitted from much lower volumes of official (5%) and private mobilised: (7%) finance, mostly for water and sanitation projects and majority of finance (see Figure 4.10).

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Notes

¹ The principles encompassed an agenda with specified actions, namely: (1) build capacity to enter into public-private partnerships, including with regard to planning, contract negotiation, management, accounting and budgeting for contingent liabilities; (2) commit to holding inclusive, open and transparent discussion when developing and adopting guidelines and documentation for the use of public-private partnerships; and (3) build a knowledge base and share lessons learned through regional and global forums.

² The five shared values are (1) anchor blended finance transactions in the SDGs, (2) aim to mobilising commercial – market-level- finance, (3) strive towards commercial sustainability in blended finance, i.e. plan to fade out concessional and development finance over time, (4) foster the creation of inclusive markets that are owned locally, conducive enabling environment and addressing the root causes that induce the need for blended finance in the first place, and (5) ensure transparency in blended finance, both with respect to financial flows and development results.

³ Such assessment will vary on a country-by-country basis based on development characteristics, conditions, policies and priorities, among others.

⁴ In a consultation process with the Asian Venture Philanthropy Network (AVPN), AVPN members supported the notion that case studies can play an important role in advancing blended finance in developing countries, including in LDCs and SIDS. Further case studies identified in the consultation process include e.g. [Educate Girls Development Impact Bond in India](#); [Quality Education India Development Impact Bond in India](#); [Meloy Fund for Sustainable Community Fisheries in Indonesia and the Philippines](#); [B-Bridddhi Programme in Bangladesh](#); [Cambodia Rural Sanitation Development Impact Bond](#); [COVID-19 Relief, Build Resilience Against Future Economic Shocks in Cambodia](#); [Project Financing and Political Risk Guarantee for Sarulla Geothermal Power Plant Project in Indonesia](#) (AVPN, 2022^[39]).

⁵ Similarly, blended finance, including the use of private finance, does not equal privatisation, i.e. a majority share of the private sector in the ownership structure of projects or enterprises.

⁶ As outlined below, the presence of developed, deep and inclusive financial markets is a further determinant of the ability to attract private finance.

⁷ Again, in particular in social sectors public finance as well as ODA will and should continue to play a dominant role as a source of financing.

⁸ Under the Tri Hita Karana Forum, *The Global Blended Finance Alliance* aims to bring partners together around Blended Finance best practices.

⁹ The IFRS Foundation's International Sustainability Standards Board outlined in early 2022 the necessary steps required to establish a global baseline of sustainability disclosures; and aims to complete by the end of 2022 technical work to launch the main elements of the global baseline. Ultimately, it aims to provide a global disclosure baseline that meets information needs of investors in assessing enterprise value; its scope does not comprise multi-stakeholder concepts such as blended finance. The work has been welcomed by the G20 alongside companies and investors from around the world, and builds on previous work of the Task Force on Climate-related Financial Disclosures, the Climate Disclosure Standards Board and others.

¹⁰ Jointly Indonesia, OECD and GIZ (on behalf of German Cooperation, BMZ) have conducted consultations with Guatemala, the Seychelles, Egypt, Rwanda and Zambia on Developing guidance to the G20 Principles.

¹¹ The G20 is addressing the topic of securitisation by MDBs as part of a set of efforts subsumed under “MDB Action Plan to Optimize Balance Sheets” since 2015; an effort that was reinforced under the 2021 Italian G20 Presidency, establishing an independent Review of Multilateral Development Banks' Capital Adequacy Frameworks (G20 Research Group, 2021^[81]).

¹² The GSSS bonds market in developing countries has been a priority of the DWG under the Italian G20 presidency in 2020. A joint OECD – CDP report has been developed, which highlights further obstacles and solutions to scaling the market in developing countries (Dembele, Schwarz and Horrocks, 2021^[77]).

¹³ Data reported to the CRS were used as proxy for providers not reporting in TOSSD yet (i.e. Germany, Netherlands, Czech Republic, the World Bank Group and the European Bank for Reconstruction and Development).

¹⁴ “Blended finance” transactions were identified through the TOSSD data field “financing arrangement”. Other activities reported with private finance mobilisation were assumed as blended finance too. Furthermore, for the purpose of this analysis, loans from multilateral organisations to the private sector and equity investments were included in the blended finance category as well.