Scaling -up Development Finance beyond Covid-19: Is a paradigm change needed?

Private finance for development: Time to think ‘outside the box’?

Dr. Judith Tyson

ODI, Research Associate

IFI mobilization of private finance has increased but is still far below needs

- Progress has been made …
  - Increased 13% annually from 2010 to 2019… but dropped in 2020 and 2021 during pandemic
  - Higher proportion went to LICs (but still only 6.4% of total)
  - Leverage ratio up from 49c:$1 to 69c:$1
- But policy remains concentrated in TA and guarantees
- And $10-20 billion being mobilised annually remains hugely below that needed
  - The annual financing gap from SDGs alone estimated to have increased from $2.5 trillion to $4.2 trillion

- Source: Attridge and Gouett, 2021, ODI; OECD, 2020; CDG Blog, March 18, 2022

What’s working?

- IFI value recognized by co-investors
  - Expertise in project development, ESG and political risk
- Infrastructure
  - Majority of private finance mobilized
  - But only some sectors: Power, ICT, transport
- Funds
  - Behind rise in leverage at MDBs
  - Investors value diversification and accessible product

- Source: IFC, MDB Mobilization Results, 2020

What’s not working…

- Bankable assets pipeline not solved
- Technical assistance… a waste of time (without capital)?
- Funds: too small, too few, unlisted
- Risk appetite not overcome …
  - Not just ‘perception’… i.e. this is not a ‘data problem’
  - Against background of heightened global uncertainty and rising interest rates in advanced economies

- Source: IFC, MDB Mobilization of Private Finance (2019 Results), 2021

Time to think ‘outside the box’ on IFIs?
(1) Challenging IFI ‘business as usual’ model

- Alternative is IFI adopt ‘originate to distribute’ model
  - Leverage their unique competitive advantages and value to investors
  - Key role to develop projects to provide ‘product’ to scale funds
  - Recycle scarce donor capital
- Commoditize project preparation
  - Commoditised, not tailored, project preparation facilities … ‘any colour as long as it’s black’ approach
  - Sounds ‘way out’? … but it’s similar to the ‘Chinese model’ of infrastructure development
  - Shift capacity building to ‘core’ institutions and move project and financing into PPFs
  - Let the private financial sector do the structuring!

(2) Tap ‘development-aligned’ pools of capital for green and ESG assets

- Very rapid growth in these global markets are creating more demand than supply for high quality assets… IFIs can provide them
- Needs focused funds with tailored and certified investment products for these investor classes
- Broaden ESG and green assets
  - Beyond microfinance and infrastructure where ’impact investors’ currently concentrate their assets
  - Into assets that accelerate pro-poor development eg manufacturing, agriculture
  - And non-power climate and biodiversity assets eg green housing, restorative agriculture, landscape approaches to climate and biodiversity, ‘micro’ access to carbon markets

(3) Market building interventions... especially in domestic markets

- Capital markets and private equity
  - Issues in domestic markets and local currencies
  - New assets categories: Green bonds, municipal bonds and SME and agricultural funds
  - Less emphasis on domestic banking
- Closing financial market gaps
  - FX, interbank, securitization intermediaries
- But evidence on impact remains ambiguous

Thank you!