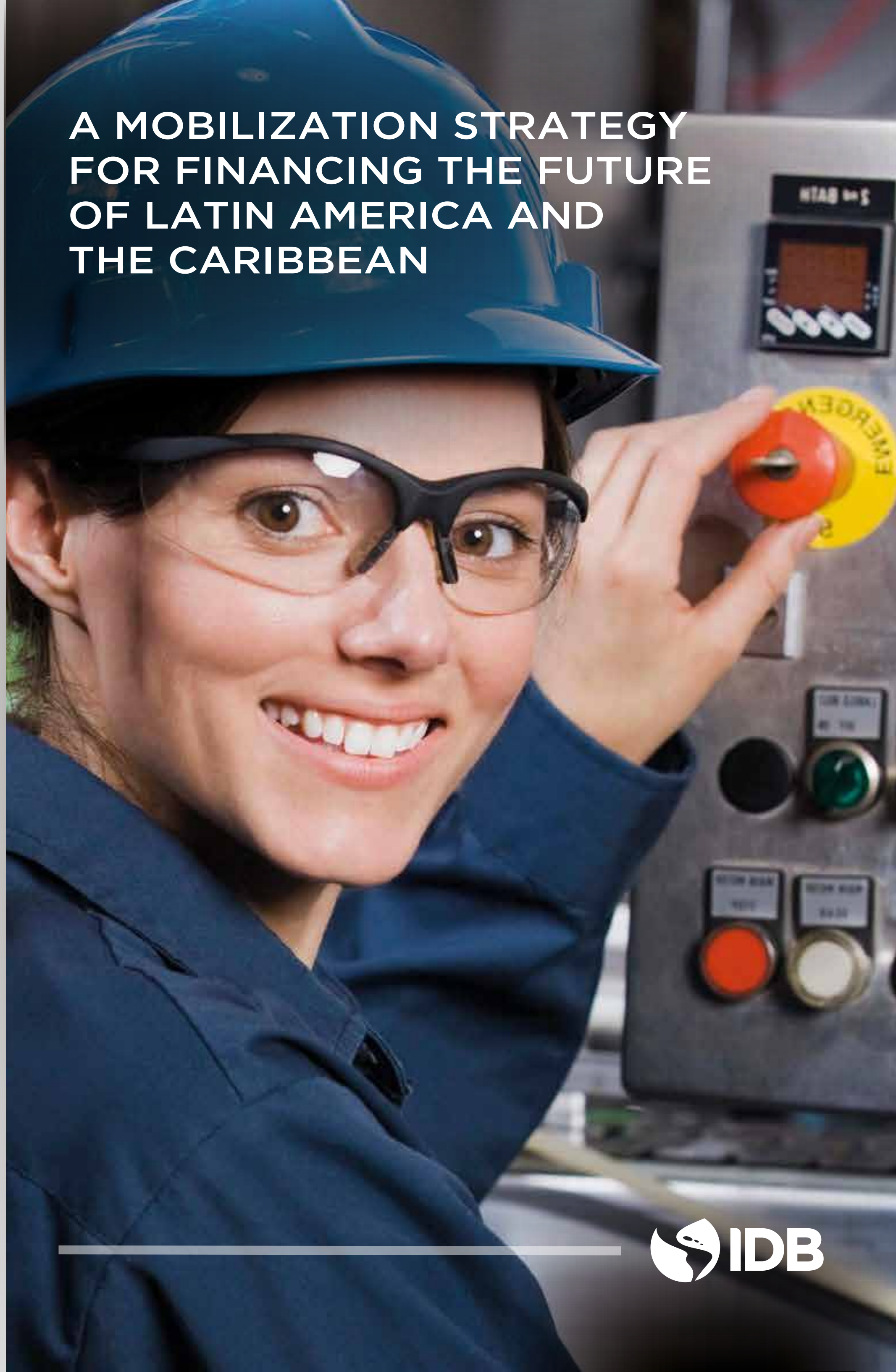
Financing the Future **with the IDB Group**

A MOBILIZATION STRATEGY FOR FINANCING THE FUTURE OF LATIN AMERICA AND THE CARIBBEAN



IDB

Introduction

Mobilizing resources is critical to the successful implementation of the 2030 agenda. To raise the financing needed to achieve the Sustainable Development Goals (SDGs), in 2015 the Addis Ababa Agenda for Action called on the global community to move from "billions" to "trillions" in their development financing efforts, demanding that they look to new, innovative schemes to make the 2030 agenda possible.

To fulfill the Addis Ababa mandate, multilateral development banks (MDBs) in particular have been called upon to look beyond traditional loans and provide technical assistance, policy guidance, and financial instruments to effectively channel public and private resources toward the SDGs. This expanded mission stems from the realization that achieving the SDGs will require resources exponentially larger than what MDBs can provide. Using the infrastructure sector as an example, consider that developing countries worldwide spend a total of about US$900 billion on infrastructure each year. It is estimated that meeting infrastructure demand will require an additional US$1.2 trillion in annual investments,[1] and that making these investments sustainable will require an additional US$260 billion per year.[2] Given that MDB disbursements account for between 3.2% and 3.8% of total current infrastructure spending, mobilizing additional resources is essential.

In that sense, the Inter-American Development Bank Group (IDBG) is committed to enhancing its role as a mobilizer and to investing added efforts in unlocking, leveraging, and catalyzing more public and private financing. By enhancing and institutionalizing resource mobilization, the IDBG can strengthen its position as a development partner for the Latin American and Caribbean (LAC) region, build on its comparative advantages as a development finance institution with strong public-private synergies, and enhance its capacity to deliver competitive financing to achieve the SDGs.

Working through an integrated, public-private approach, the IDBG has created a multidisciplinary task-force to design and articulate an innovative vision that will support the implementation of the 2030 agenda and will be integrated into the IDBG's work and strategy as a core pillar. By investing in an empowered and dedicated mobilization team that will work to mainstream mobilization, drive new product development, and expand external outreach, the IDBG solidifies its position as a leader in creating value for its borrowing member countries and partners. The new products will build on the IDBG's successful experiences and combine institutional, private, and donor funding, allowing them to leverage Official Development Assistance (ODA) and other financial flows to contribute to the implementation of the 2030 agenda in LAC.

1) OECD, Official Development Finance for Infrastructure: With a Special Focus on Multilateral Development Banks, November 2016.
2) Under the 2º Celsius increase scenario. See Christopher Kennedy and Jan Corfee-Morlot, "Mobilizing Investment in Low Carbon, Climate Resilient Infrastructure," OECD Environment Working Papers No. 46, pp. 13 and 37. See also, Partnering to Build a Better World: MDB's Common Approaches to Supporting Infrastructure Development, August 2015, prepared by IDB, World Bank, ADB, AfDB, EBRD, EIB, IsDB and IFAD.

Latin America and the Caribbean at the Forefront of SDG Financing

LAC is a fertile testing ground for innovation in resource mobilization. The region's combination of middle-income economies and less developed ones, the institutional capacity that has been built up throughout the years, and its evolving financial markets create opportunities for the mobilization of significant national and international resources. In many countries, innovative and blended finance can be a capital efficient way of deploying ODA with highly catalytic effects.

LAC offers private investors and donors opportunities for portfolio diversification and country specific interventions alike. The cultural, economic, and social similarities shared by many LAC countries permit the IDBG and its partners to pilot innovative financing models, scale and replicate proven solutions, and report on the application of solutions to other regions. New financing schemes can be tailored-made to specific geographies and sectors. Showcasing the results and impact of innovative and blended finance can catalyze a cascade effect of additional investments that no longer require development finance.

Building on Successful Examples

The IDBG is well positioned to blaze this trail. As early as 2010 and replenished in 2017, the IDBG pioneered the design of the Salud Mesoamerica Initiative, a robust results-based financing scheme that tested and paved the way for results-based loans. In 2011, the establishment of the Canadian Climate Fund for the Private Sector in the Americas permitted the Bank to pilot the application of blended finance to mobilize private investments in climate and gender. In 2017, a series of new partnerships were established to validate the importance – and the return on investment – of this bold experimentation. These partnerships tackled important issues including the IDBG's quest to eliminate malaria in partnership with major foundations, to fill the region's infrastructure financing gap by working with the United Kingdom to provide blended finance for private sector operations, and to catalyze the transformation of the energy matrix of several Caribbean countries through a cutting edge public-private partnership supported by the three largest international climate funds: the Global Environment Facility, the Climate Investment Funds, and the Green Climate Fund. Between 2010 and 2016, donor financing committed through these types of mechanisms represented on average approximately four percent of the IDBG's mobilization commitments. It has since risen dramatically and, in 2017, grew to

comprise 38 percent of all mobilization efforts. Moving forward, the IDBG's partnership efforts will focus on further exploring and leveraging innovative finance, and on expanding its portfolio of blended finance instruments, enhanced-support financing schemes, and de-risking financial tools.

Planning and Implementing a Revamped Mobilization Vision

The aforementioned multidisciplinary task-force is working on new ways to integrate mobilization into the IDBG's work with partners, institutional structure, and strategy. A key priority will be defining internal incentives to increase resource mobilization. A second work stream will focus on enabling internal collaboration and providing staff across the institution with the training, guidance, and support needed to integrate mobilization into client engagement and operations. A third work stream will consist of monitoring mobilization, which requires tracking both actions and results. The task-force will also work to generate cutting-edge corporate ideas for innovative mobilization, and will assist with the development of mobilization instruments for the IDBG.

Join Forces with the LAC Region's Partner of Choice

The IDBG works with borrowers and shareholders to facilitate, structure, and administer innovative mobilization instruments. The IDBG tailors funds and instruments that support the region's development agenda in line with donor objectives and governance preferences. By leveraging its ample knowledge of development financing, experience structuring transactions, solid financial rating, public-private approach, and capacity to convene relevant actors, including commercial investors and governments, the IDBG moves closer to its goal of improving lives.
Join us.

The coming pages outline concrete approaches to financing the future by discussing innovative financing concepts, instruments, and examples. There are diverse applications for each of the tools covered in this document and a great deal of opportunity to further innovate and explore. In this process, the IDBG welcomes aboard new partners committed to identifying novel ways of financing the region's future.

INNOVATIVE FINANCE

KEY FACTS

The IDBG is a pioneer in results-based programs. The Salud Mesoamerica Initiative is a top results-based program at a regional scale in terms of its success improving health in the region.

At the IDBG innovative finance has emerged as an effective approach to development financing that has played a critical role in attaining specific Sustainable Development Goal targets such as child health, malaria, and others.

To implement innovative finance the IDBG relies on guarantees, debt funding mechanisms, performance-based incentives, risk mitigation instruments, public-private partnerships, and enhanced support mechanisms, among others.

What is innovative finance?

When the term "innovative finance" first became ubiquitous in the development finance community, it was originally perceived to encompass any and all efforts to mobilize non-ODA resources for development. However, in recent years the IDBG has sharpened the definition of this term, designed new instruments to enhance the efficiency and results of public and private financial flows, and generated knowledge about innovative finance and its potential impact. Today, the IDBG defines "innovative finance" as novel, more efficient ways of sourcing and deploying development funds; for instance, through mechanisms that pool non-traditional public and private financing, to amplify the impact of each dollar mobilized.

Why use innovative finance in LAC? How can innovative finance help the IDBG's borrowing member countries?

Innovative finance is especially important for middle income countries in the LAC region that are either "graduating" or perceived as "graduating" from the need for international aid support but that still have key development goals that need to be reached. As countries prepare to be more economically self-reliant and less eligible for ODA, identifying new and more effective financing has become a priority for the IDBG in the years to come. Countries and multilaterals alike are encouraged to achieve more scale and unlock further financing by mobilizing resources from non-traditional partners and/or in non-traditional ODA fashion i.e. through blended mechanisms, public-private partnerships, and other de-risking instruments.

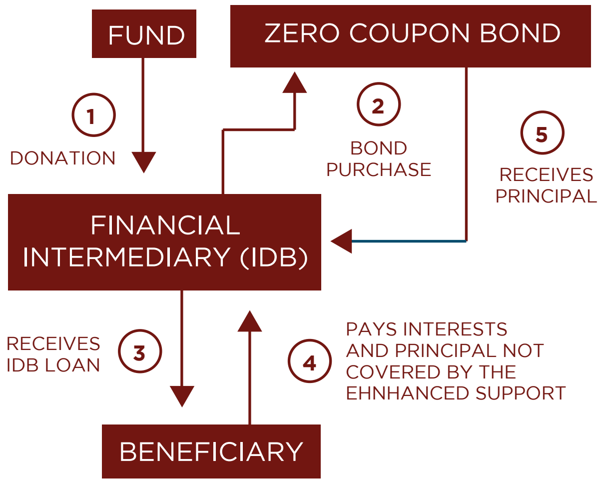
What are some examples of the IDBG's work on innovative finance?

THE SALUD MESOAMERICA INITIATIVE

Founded in 2010 and renewed in 2017, the initiative is a public-private partnership between the IDBG and the Bill & Melinda Gates Foundation, the Carlos Slim Foundation, the Government of Spain, the countries of Central America, and the state of Chiapas, Mexico. The Salud Mesoamérica Initiative (SMI) continues to support countries to achieve results and improve access to health for women and children in the poorest 20 percent of Mesoamerica's population. To date, the initiative has directly benefitted 1.8 million women of reproductive age and children aged less than five years, while indirectly benefitting an additional 4.5 million people in the poorest areas of these geographies. The innovative aspect of this initiative is the results-based financing scheme which provides a grant that represents 20% of the program to help achieve pre-negotiated target indicators. Donors have provided US$114 million in funding, leveraging nearly US$41 million in counterpart resources from country governments for a total of approximately US$155 million. To date, the investment by donors has been leveraged almost US$1 to US$1 by the investment from the Mesoamerican countries.

THE YUCATAN FUND

The Yucatan Fund is a south-to-south infrastructure fund for Mesoamerican and Caribbean countries which leverages IDBG expertise to channel resources to infrastructure projects in the region. By acting as financial intermediary to this fund, the IDBG introduced a financing scheme called "enhanced support" which allows for greater donation size to repay a portion of an infrastructure loan.



Through this fund, Mexico provides a donation that allows the IDBG to acquire a zero-coupon bond on behalf of a borrower member country, the beneficiary. Concurrently, the IDBG provides a loan to the same beneficiary to finance an infrastructure project. At bond maturity, a portion of the loan will be repaid using the proceeds from the zero-coupon bond (i.e. bond face (future)

value = present value plus accrued interest). The beneficiary of the enhanced support will cover the interest on the entire loan amount, as well as the fraction of the loan principal not covered by the zero-coupon bond. The enhanced support mechanism provides the following benefits: i) channels donor resources through IDBG infrastructure projects; ii) allows Mexico and the IDBG to multiply development assistance resources contributed by the Yucatan Fund as it helps the beneficiary to partially repay the principal of the loan with the bond's face (future) value, iii) increases the concessionality level in IDBG financing.[1] Mechanisms such as this one may release IDBG capital requirements as the loans are being partially collateralized, and therefore may allow IDBG to allocate additional resources to other development projects.

MALARIA ELIMINATION BLENDING FACILITY

In 2017 the IDBG partnered with the Bill & Melinda Gates Foundation, the Carlos Slim Foundation, the countries of Mesoamerica, and the Dominican Republic to design a blended finance mechanism to eliminate malaria by 2022. A major focus of this partnership and financial model will be on demonstrating the effectiveness of innovative financing to leverage national resources and ongoing technical assistance, fund new strategies, and build on existing tools. It will also strive to develop tailored elimination strategies, as a one-size-fits-all approach has been deemed insufficient to bring malaria incidence to zero in the region. As such, the initiative will work at both the country-level and via a regional program through a blended finance and results-based financing model. For every dollar invested by the country, donors will contribute an additional US$0.53 for the needed interventions and the leverage is almost US$1 to US$1 when technical and operational assistance, measurement and evaluations are taken into account. The estimated concessionality of the overall financing may vary from 9% to 21%, which is substantially above the standard concessionality of approximately 9%.

What's next for IDBG and the LAC region regarding innovative finance?

The IDBG will continue to push boundaries in the innovative finance space by actively introducing new products and de-risking instruments, bringing existing products to new markets, and engaging new types of investors. It will continue to develop results-based financing instruments beyond the health sector to achieve gender and climate targets and to promote greater private sector investments.

[1] Based on interest rate levels and market data as of March 2018, the Yucatan Fund mechanism more than doubles standard IDB loan concessionality (from 9% to 21%) for a project comprised of an IDB loan of US$90 million and a grant provided by the Yucatan Fund of US$15 million in present value terms, with approximately US$23.6 million value at bond maturity.

BLENDED FINANCE

KEY FACTS

+US$1.5 billion and counting.
Amount of resources committed by donors for blended finance operations and funds with the IDBG since 2010.

US$10.
Average number of commercial dollars for development projects, catalyzed by a US$1 investment of blended finance. with IDBG.

Value for money.
Public-private approach to blended finance. Combination of technical assistance with capital investment. Demand-led and targeted to specific. sectors.

What is blended finance?

At the IDBG, blended finance is defined as the combination of concessional finance from donors with the IDBG's own and/or commercial finance from other investors, to develop private markets, address the SDGs, and mobilize private and public resources.

What instruments does the IDBG use to implement blended finance?

The IDBG implements blended finance solutions through different types of financial products, including risk mitigation (first loss guarantees, local currency), debt (senior, subordinated or contingent loans, bonds), equity (funds, direct equity) and innovative forms of pricing and technical cooperation (performance-based incentives, investment grants, contingent grants).

How does the IDBG use these tools?

The IDBG uses blended finance for **highly catalytic projects** that can help LAC countries expand their development agendas and achieve the SDGs. Blended finance solutions are demand-driven and targeted, defined by factors including the specific market failure or bottleneck to be addressed, the local context, and an adequate risk-return-impact balance, following the principles of additionality, minimum concessionality, commercial sustainability, and market reinforcement. Blended finance solutions can be used to pilot, replicate, and scale catalytic projects.

PILOT

Provide blended finance resources to demonstrate the viability of an innovative finance template or new technology

REPLICATE

Replicate and adapt existing templates to open new markets by supporting early movers through blended finance

SCALE

Structure **blended finance** intervention to maximize private sector investment

- 1st energy savings insurance program for SMEs in Mexico
- 1st industrial scale solar power plant in El Salvador
- 1st cross border solar bond in Latin America and the Caribbean, using IDB invest A/B bond structure

What are some examples of the IDBG's work on blended finance?

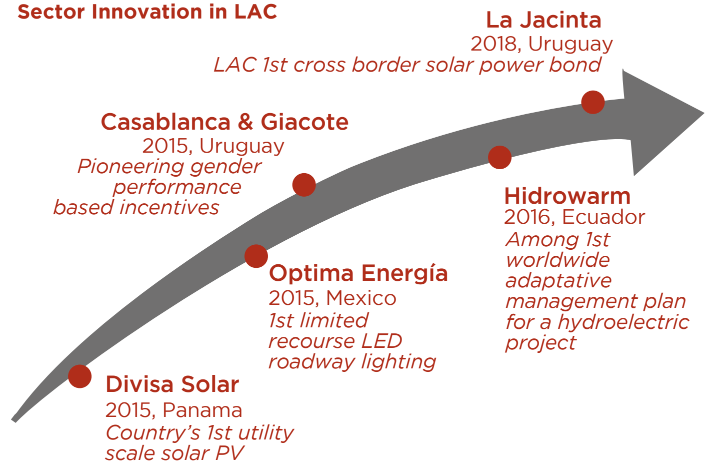
SPEARHEADING THE TRANSFORMATION OF MEXICO'S ENERGY MATRIX

The Renewable Energy Financing Facility (REFF) was a US$270 million blended finance facility that catalyzed private capital for renewable energy projects in Mexico. The facility provided fixed-rate, long-term loans (between 10 and 20 years) to developers who financed new renewable energy projects and provided operational financing support to beneficiary projects through contingent credit lines (liquidity backstops) to address potential temporary cash flow shortages throughout a renewable project's lifetime (i.e., due to weak power generation or because prices are lower than expected). The REFF has been critical to Mexico's efforts to increase the share of renewable energy sources in its overall generation, as well as its greenhouse gas emission reduction pledge to the United Nations Framework Convention on Climate Change. The REFF leveraged more than US$2 billion in private investments and created more than 2.6 GW of wind power generation capacity in Mexico. The REFF was developed in partnership with the Clean Technology Fund and the Government of Mexico.

INNOVATING AT THE INTERSECTION OF GENDER AND CLIMATE THROUGH BLENDED FINANCE

The Canadian Climate Fund for the Private Sector in the Americas (C2F), developed in partnership with Global Affairs Canada, is a US$250 million blended finance fund that catalyzes private sector investments in climate mitigation and adaptation in LAC by providing concessional finance alongside co-financing from IDB Invest. The fund offers a wide array of risk mitigation and debt products and had been pioneering the use of performance based incentives to incorporate gender empowerment in projects supported by C2F. Since its creation, the fund has catalyzed US$1.2 billion in commercial investments to support low carbon and climate resilient investments in LAC. Figure 2 showcases examples of some of the pioneering interventions catalyzed by the fund.

Figure 2: C2F, Driving Private Sector Innovation in LAC



PIONEERING A GLOBAL PROGRAM FOR THE IMPLEMENTATION OF THE PARIS CLIMATE AGREEMENT THROUGH SUSTAINABLE INFRASTRUCTURE INVESTMENTS

The UK Sustainable Infrastructure Program is a £177 million advisory and blended finance program developed in partnership with the United Kingdom's (UK) Department for Business, Energy, and Industrial Strategy (BEIS). It is the most recent blended finance partnership between the IDBG and the United Kingdom. The objective of this revolving fund, where returns would be reinvested into new projects, is to accelerate sustainable infrastructure development in Brazil, Colombia, Mexico, and Peru. The program will catalyze private investment and helping governments improve the business climate for sustainable infrastructure through technical assistance and concessional capital investments provided through diverse financial instruments. The UK decided to first launch the Sustainable Infrastructure Program in LAC in partnership with the IDBG, and lessons and results from this pilot will help the UK develop the program's second phase in Southeast Asia and Africa.

FACILITATING PARTNERSHIPS BETWEEN DEVELOPMENT FINANCE INSTITUTIONS

The IDBG and the European Commission (EC) have a history of working together to pioneer blended finance models that combine lending and grant resources from multiple financiers through the Latin American Investment Facility (LAIF). In countries like Bolivia, the partners are improving access to clean water and sewage through a €15 million grant from the EC, as well as a €55.6 million senior loan from the IDBG and an additional €5 million in financing from the Spanish Agency for International Development Cooperation (AECID). In Jamaica, thanks to financing from the Caribbean Investment Facility, an €8 million grant from the EC will complement a combined US$30 million in lending from the IDBG and the Japan International Cooperation Agency (JICA) to improve energy efficiency in government facilities and promote fuel conservation in Jamaica.

What is next for the IDBG regarding blended finance?

With more than US$1.5 billion in donor funds committed to blended finance since 2010, the IDBG has developed extensive expertise in utilizing partners' concessional resources to mobilize commercial resources for achieving the SDGs in LAC. The institution relies on strong internal controls and dedicated teams that ensure a disciplined, efficient, and impactful use of partners' concessional resources. The IDBG will continue expanding the scope of its blended finance efforts, working with partners to design locally-tailored approaches and new instruments. It will seek to expand into new sectors beyond those traditionally served by blended finance, as well as into new geographies. The IDBG will continue to work on public-private partnerships and regional approaches to tackle the SDGs through blending, while working with donors and governments on innovative financing tools that catalyze commercial financing toward the fulfillment of the SDGs in LAC.

BONDS

KEY FACTS

+US$3.1 trillion. Current SDG funding gap, in comparison with the **+US$90 trillion** global bond market.

The green bond market grew at record levels in 2016 and 2017. **Issuance rose by 61%** year-over-year in 2017.

The current labelled green bond market is valued at **US$221 billion.**

What is a bond for sustainable development?

Bonds for sustainable development were created to fund projects with positive environmental and social returns by crowding-in institutional and non-traditional investors. Bonds for sustainable development are a growing source of financing and create a “demonstration effect” with other investors, helping to close the multi-billion dollar financing gap needed to meet the SDGs while offering them the opportunity to participate in development efforts.

How does the IDBG support bonds for sustainable development?

Bonds for sustainable development are used to structure financing packages that cater to different risk-profiles and crowd-in financing that would be otherwise unavailable. The IDBG supports the development of the market by working both public and private sector. Through its lending and technical assistance products, the IDBG works to strengthen regulatory frameworks and financial supervision to support these structures. The IDBG supports the process from portfolio identification to bond issuance. Some structures may include a credit enhancement feature (guarantees and/or investment anchoring) provided by donors or the IDBG to achieve investment grade and support the ability of the issuer to diversify sources of funding.

PORTFOLIO IDENTIFICATION	BOND STRUCTURING	SECOND PARTY OPINION	ROADSHOW	ISSUANCE
-Develop the capacity of finance/treasury teams related to green bond opportunities. -Assess and classify potential “green portfolio” for bond issuances. -Assess institutional ESG capacity and strategies.	-Define the certification methodology to be applied (climate, green, or sustainable bonds). -Define final pipeline and amount to be issued. -Define use of proceeds. -Define reporting system.	-Review, revision, and approval of the portfolio and strategy package, as well as the use of proceeds and reporting mechanisms by a recognized second party.	-Develop the final public offer package. -Support presentations of the institution and pipeline to national and international investors.	- Comunications and promotion. -Sharing of lessons learned with other national development banks.

→ Institutional Investors

Credit Enhancement Feature

What are some examples of the IDBG's work with thematic bonds?

GREEN BONDS

Through the issuance of green bonds, the IDBG is supporting national development banks (NDBs) in their efforts to raise private funds from institutional and impact investors at adequate maturities in both local and international capital markets. These issuances support the development of national capital markets, and improve issuers' ability to diversify sources of funding, and promote low-carbon investments overall. The program is currently supporting NDBs in Brazil, Colombia, Ecuador, Mexico, and Peru. The IDBG also works with government agencies, regulatory bodies in the financial sector, and domestic stock and bond exchanges to support the design of national strategies to incentivize domestic green bond markets. Pilot projects are currently being developed in Brazil, Ecuador, and Mexico. The program is supported by Switzerland's State Secretariat for Economic Affairs (SECO) in Colombia, Ecuador, and Peru, and the International Climate Initiative (IKI) of the German Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety (BMUB) via the LGI program in other countries. The IDBG is working closely with the Climate Bonds Initiative – an international, investor-focused, not-for-profit that is the only organization in the world working independently to mobilize the US$100 trillion bond market for climate change solutions.

LA JACINTA

IDB Invest closed a landmark 24.5 year amortizing B-bond for US$61.7 million to partly refinance the existing obligations of La Jacinta, a 50 MW utility scale solar photovoltaic plant in Uruguay. In 2014 the IDBG, in conjunction with Norway's DNB Bank ASA and the Canadian Climate Fund for the Private Sector in the Americas (C2F), provided an A/B loan and a C2F co-loan to finance the construction and operations of the solar plant. The current transaction refinances the original A/B Loan via the A/B Bond issue and restructures the C2F co-loan. The C2F's terms were structured to support the investment grade rating of the issue to ensure the innovative investment would be marketable to international institutional investors. IDB Invest acted as lender of record for the entire financing and sells participation to a Special Purpose Vehicle (SPV) which in turn sells notes into the United States private placement market. The private placement notes or B-Bonds were rated by Moody's using its green bond assessment methodology. La Jacinta is the third transaction developed by the IDBG that uses an A/B Bond structure, and the second in Uruguay after the successful placement of Campo Palomas in August 2017. The project has one of the longest repayment periods in the region's history.

SOCIAL IMPACT BONDS OR PAYMENT FOR SUCCESS BONDS

The IDBG, through its Multilateral Investment Fund, launched in 2016 the first Social Impact Bond (SIB) in the region and in emerging markets in general in Jalisco, Mexico. A SIB, which is not a "real bond" in financial terms, is a partnership in which impact investors and philanthropic organizations (not governments) assume the risk of financing a solution to a difficult societal problem. Once non-governmental organizations (NGOs) and social enterprises receive working capital from private investors or philanthropic organizations, they can work directly with their communities to implement an effective social service. If these organizations are successful, the government pays the private investors for the positive outcomes. As a result, governments are able to transfer the risk of testing innovative programs by paying only when results are achieved, NGOs can access flexible and longer-term funding, and taxpayers get more rigor, accountability, and value for

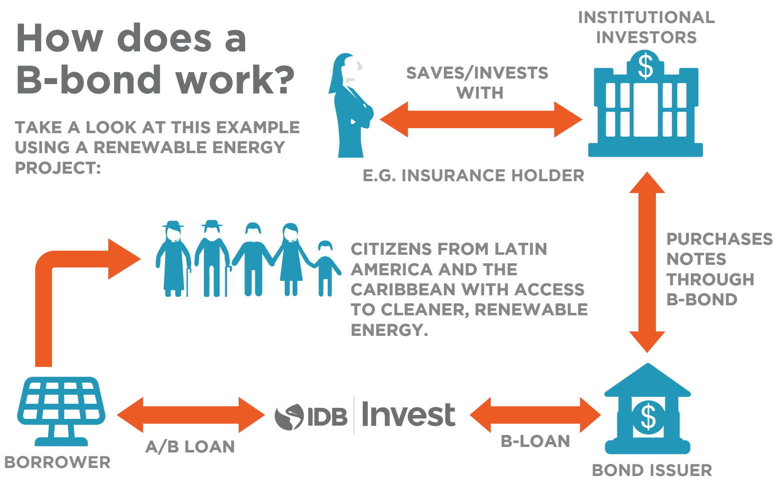
their money. The SIB in Jalisco will be used to fund services that increase the income and resilience of poor, female-headed households with the goal of facilitating their transition out of poverty.

B-BONDS

The B-Bond structure allows IDB Invest to crowd-in institutional investors. The A/B Bond allows the borrower to achieve significantly longer tenors, match long-term asset financing, and provide better conditions than those available in the traditional bank market by: 1) reaching a broader investor base; 2) sharing IDB Invest privileges and immunities, including Preferred Creditor Status (PCS) in member countries, and 3) benefiting from IDB Invest's extensive track record of structuring, financing, and supervising projects. Through this mechanism: 1) IDB Invest enters into a A/B Loan agreement with the borrower; 2) IDB Invest shares it PCS with the B-lender through a participation agreement; 3) An SPV or trust fund is established as the B-lender; 4) Notes are issued by the SPV and purchased by institutional investors; 5) The SPV passes through the interest and principal repaid by the borrower on the B-Loan to the noteholders and; 6) Repayment of the notes are expected to mirror the A/B Loan.

How does a B-bond work?

TAKE A LOOK AT THIS EXAMPLE USING A RENEWABLE ENERGY PROJECT:



What's next for the IDBG regarding bonds for sustainable development?

As institutional investors move into sustainable investments at a growth rate of 17 percent a year,[1] the IDBG will continue to focus on promoting bond programs in LAC.

SDG-THEMED BOND

The IDBG is currently developing a structured scheme to support the issuance (with technical cooperation and credit enhancement mechanisms) of SDG-themed bonds. These bonds would include an obligation to use the proceeds for specific purposes and would thus result in increased available funds to finance targeted investments, using existing bank intermediation channels. Under this scheme, the IDBG and other MDBs would help financial institutions to better access capital markets within a framework that ensures proceeds are used exclusively for sustainable investments.

GENDER-FOCUSED B-BOND

The IDBG is partnering with a major regional Latin American bank with an established product platform to add value to its female clients by structuring a gender-focused B-Bond. The local bank will use the proceeds to finance eligible women-owned medium and small enterprises (SMEs). B-Bonds represent an innovative way to lend to women-owned/led SMEs as they diversify sources of funding and expand the investor base to include entities seeking high social impact. This project marks the first use of a B-Bond structure by a large private bank for on-lending to women-owned/led SMEs.

[1] From 'why' to 'why not': Sustainable investing as the new normal, McKinsey, 2017.

GUARANTEES

KEY FACTS

Globally **US$35.893 million** was mobilized through guarantees between 2012-2015.

3% of total infrastructure investment in the region comes from the private sector. Using guarantees can cover risks to enable greater private sector investment.

Guarantees reduce losses in the event of a default, enhance the **credit quality** of the government and of the project, and **enable bankability** through strong risk mitigation.

What are guarantees?

Guarantees can improve financing conditions for projects and help promote private sector investment. They cover the risks that the private sector is not normally able to absorb or manage. The IDBG can guarantee loans made by private financial sources in public or private sector projects. The potential of guarantees to mobilize resources and catalyze private sector capital has not been fully utilized by donors, multilateral entities, and beneficiaries.

How can donors engage with guarantees?

Donors can provide guarantees to mobilize capital for development purposes. For example, in private sector operations, a donor can guarantee the repayment of a loan to improve the borrower's status; provide a first-loss guarantee to institutional investors at a portfolio level to enable investment in new markets and sectors and to increase financing for the SDGs; and/or provide a liquidity back-stop, which is important for infrastructure projects.

How can guarantees help achieve the SDGs in LAC?

Guarantees are a valuable instrument for mobilizing private resources from institutional investors, investment funds, etc. For a fraction of the potential cost of the risk exposure undertaken, considerable liquid resources can be deployed for investments to improve lives. They can be used in a myriad of ways, such as i) backstopping financing for large-scale, multi-year infrastructure projects, ii) lengthening the maturities of loans to small enterprises, iii) providing liquidity during the construction phase, iv) enabling local banks to enter new markets through such means as microenterprise lending, or v) deepening capital markets by facilitating local-currency bond issues.

What are some examples of the IDBG's work with guarantees?

THE NDF ENERGY EFFICIENCY GUARANTEE FUND

The Energy Efficiency Guarantee Fund is designed to catalyze greater private sector investment in climate change by enhancing the credit profile of IDB Invest borrowers. The Nordic Development Fund (NDF) provided €8 million in support of the Fund, with the objective of facilitating investments in small- and medium-sized projects focused on energy efficiency and renewable energy. The proceeds of the Fund provide partial credit guarantees, enabling the financing of projects that would not otherwise be bankable. The proceeds also provide technical assistance, when needed, to reduce transaction costs and identify eligible projects. The Fund has had a catalytic impact in the region, mobilizing US$6 in financing for each US$1 committed.

DEVELOPING GUARANTEE FUNDS TO LEVERAGE SME PRIVATE INVESTMENTS IN PRODUCTIVITY IN THE CARIBBEAN

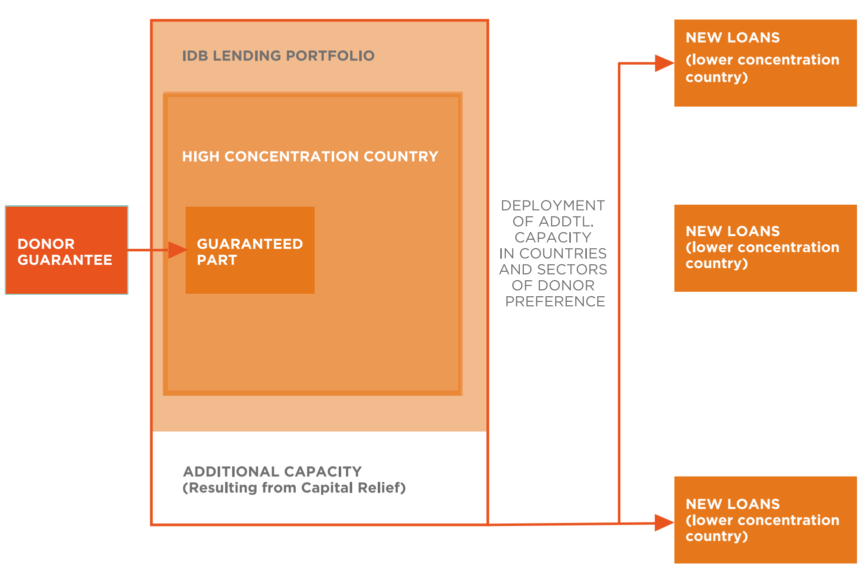
In collaboration with the Central Bank of Barbados, the IDBG developed a US$35 million Special Purpose Vehicle. Financed by IDBG and the China Fund for LAC, the Vehicle provides for a second-tier credit Guarantee Fund that has further leveraged medium and long-term financing from commercial banks to SMEs, allowing them to invest in modernization and technology improvements resulting in higher productivity and competitiveness. With a multi-sector orientation, the Fund also promotes diversification in the commerce and service sectors, construction, and manufacturing industries. Since the Fund was launched in March 2016, it has already authorized 14 guarantees that have endorsed loans for a total value of US$ 15 million (February 2017), executing 25% of the IDBG loan. This successful approach is currently being replicated with the Development Bank of Jamaica and could be expanded across the Caribbean countries, since they face similar constraints regarding access to credit and collateral.

What is next for IDB and IDB Invest in using guarantees?

DELINKED PORTFOLIO GUARANTEE

A donor provides the IDBG with a guarantee that would cover a fixed amount of sovereign-guaranteed country exposure in a specific country with high IDBG concentration. The IDBG utilizes the resulting increase in lending capacity to take on additional exposure of 200% to 400% of the guarantee amount in other countries with lower concentration and in sectors determined by the donor. The guarantee would only need to cover payment delays of Sovereign Guaranteed loans in the guaranteed countries in excess of 180 days and amounts paid by the guarantor would be refunded once the arrears are collected by IDBG.

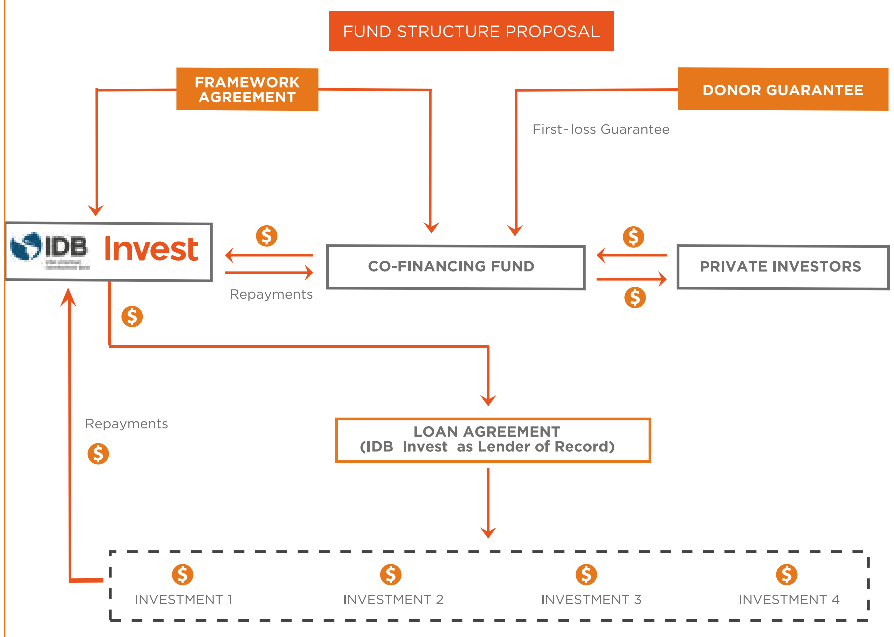
MODEL OF DELINKED PORTFOLIO GUARANTEE



FIRST-LOSS FUND

In the private sector, a donor may provide a first-loss guarantee to institutional investors to support a diversified pool of transactions. The institutional investors would co-finance IDB Invest deals through IDB Invest's A/B loan program. IDB Invest would present eligible projects that meet pre-established criteria for investors to consider and approve on a case-by-case basis. The donor government would help reduce the risk, potentially increasing the credit rating and private financing to development projects. Under such a structure, a donor can incentivize institutional investors to contribute to the SDGs on a portfolio level which would allow for a more efficient use of the donor's resources.

MODEL OF FIRST LOSS FUND



DE-RISKING

KEY FACTS

De-risking financing tools can **target a specific class of risk and attract private investors.**

De-risking supports PPPs. The Sustainable Energy Facility (SEF) has a potential **leverage of US$30 per every US$1 of IDB financing.** The SEF shows that high leverage is possible.

Between 2016-2018 **US$2.9 billion were mobilized** through the A/B program.

What are de-risking financing tools for development?

De-risking financing tools are of growing interest to a wide range of development actors searching for solutions to bridge the development financing gap. Some private investors are deterred by perceived investment risks and expected returns, and these de-risking financing tools can be an efficient way of mitigating risk and leveraging private financing for development initiatives. De-risking financing tools seek to redistribute risk across a “layered”’ set of financing options. Options may include grants, blended finance, subordinated debt, and senior loans. Subordinated debt, while riskier than traditional debt, has a lower claim on assets; that is, it is repaid only after other, more "senior" debt is repaid. Similarly, blended finance can facilitate the effective and efficient use of concessional resources in private sector projects, while avoiding market distortion or crowding-out private capital. Guarantees may also play a role in de-risking a particular investment.

How can donors engage with de-risking tools?

It is key that donors continue to act as leaders in funding the development and costs of experimental initiatives in untested environments that might be considered too costly or risky for private investors, at least in the initial stages. By taking a first-loss on a pool of investments, for example, donors build a risk cushion for institutional investors, such as pension funds, that may not otherwise participate and that could finance through subordinate debt.

How can de-risking financing tools help achieve the SDGs in LAC?

By targeting better risk allocation and management and by enhancing a clients’ access to credit, de-risking tools can foster investment and expand and improve the financing terms of projects in the region, by:

- Disaggregating risks – de-risking tools are an efficient instrument that allows market participants to bear risks according to their capacity to manage them.
- Developing missing markets – de-risking tools can help create or develop markets by addressing specific risks that restrict financing or act as barriers to suitable credit structures, mostly in terms of cost and/or tenor.
- Unleashing a leveraging effect – such tools may improve or enhance credit standing.

How does the IDBG use these tools?

Such tools can be used to structure a financing package that caters to different risk-profiles and crowds-in financing that would be otherwise unavailable to sectors such as infrastructure (particularly in public-private partnerships), productive financing for small and medium enterprises, renewable energy, climate change, energy efficiency, agriculture, and food security. The IDBG can also provide support through a combination of different financial instruments (grants, loans and guarantees) and can help its clients to develop innovative de-risking tools.

IDB Invest's A/B Program

In the case of IDB Invest, banks and institutional investors are brought in as co-financiers in its A/B loan program. Under this program, the IDBG offers the A portion of the loan from its own resources. The Bank partners with other financial institutions to provide the B loan. Under this structure, IDB Invest is the Lender of Record in the transaction and acts as Lead Lender and Administrative Agent for the entire A plus B loan facility. Such structure offers benefits for both the borrowers and the financial institutions partnering with the IDBG because it mitigates the risk of transfer and convertibility of the operation.

IDB Invest enjoys a special relationship with its borrowing governments: de jure immunity from taxation and de facto preferred creditor status. Therefore, no withholding taxes apply to debt service payments on loans. As a result, financial institutions participating as B Lenders benefit from the same status. For borrowers, this reduced risk translates into lower borrowing costs.

Bank regulators from many European and other non-regional member countries recognize the special status of the IDBG and exempt participants in B Loans from compulsory country-risk provisions. The Basel II accord also recognizes that B Loans help to mitigate or transfer convertibility risks. The transfer and coverability mitigation helps crowd-in more financing.

The IDBG can also provide support through a combination of different financial instruments (grants, loans and guarantees) and can help its clients to develop innovative des-risking tools.

What are some examples of the IDBG's work with de-risking tools?

THE SUSTAINABLE ENERGY FACILITY (SEF) FOR THE EASTERN CARIBBEAN

The SEF provides an array of financial instruments to de-risk geothermal development so that Eastern Caribbean governments can establish public-private partnerships (PPP) with geothermal private developers. Through the SEF, governments receive grants for capacity building as well as regulation improvement, environmental studies, and surface assessments for geothermal development. The uncertainty of drilling is mitigated by donor-funded Contingent Recovery Grants (CRGs). Both the grants and the CRGs become the equity of the governments in the new PPPs established by the government and private geothermal developers.

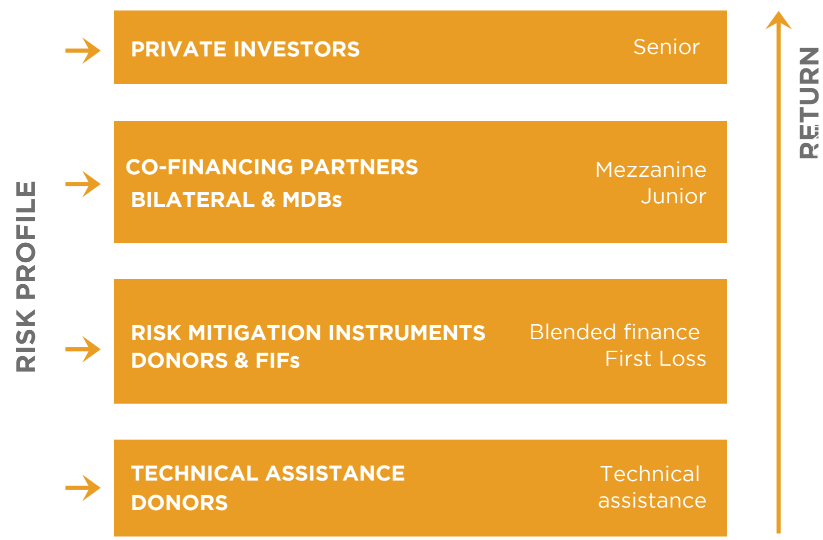
The PPPs assume the loans, allowing the countries to diversify the energy matrix without increasing their debt load or using their sovereign guarantee. The PPPs receive CRGs to proceed with the exploratory drilling. If drilling is successful, the CRGs are transformed into a concessional loan and the PPP continues geothermal development. If not, it remains a non-reimbursable grant. The SEF's concessionality will be reflected in the final tariff to end users, reducing energy bills by approximately 20-30%. Furthermore, geothermal energy will reduce the use of imported fossil fuels by 80%. The SEF is the first project to bring together the world's three major climate funding sources: the Green Climate Fund (GCF), the Global Environmental Facility (GEF) and the Clean Technology Fund (CTF). It was developed in partnership with the Government of Italy and the Caribbean Development Bank. This US$157 million blended facility has also secured parallel financing (US$39 million) from other donors and at least US$360 million in private sector equity and commercial debt contributions.

THE IDBG'S ENERGY SAVINGS INSURANCE PROGRAM

The Energy Savings Insurance Program (ESI), which has ongoing projects in seven countries, is an internationally praised initiative developed by the IDBG to catalyze a new financial product for climate change mitigation through SMEs. ESI overcomes barriers to investment in energy efficiency (EE) through long term financing and risk mitigation packages that incentive SMEs to invest in and adopt energy efficiency solutions. Its innovative approach combines the provision of financing that covers projected energy savings for specifically defined and verifiable EE measures as agreed upon in a standard contract between SMEs and technology services providers. The program offers a package of risk mitigation instruments to compensate firms in the event that promised financial flows associated with EE savings are not realized. ESI was developed in partnership with the Government of Denmark, the Green Climate Fund, the Clean Technology Fund, and local banks. Through partners such as the French Development Agency and BASE Switzerland, this mechanism is now being replicated globally. The A.M. BEST insurance rating agency featured it as one of the most innovative insurance products of 2015, while the Global Innovation Lab for Climate Finance endorsed it as one of the most promising instruments to mobilize private sector investments in EE.

What's next for IDB and IDB Invest regarding de-risking financing tools?

A Layered/Structured Fund. A non-IDB Invest managed fund can aggregate capital, using a "waterfall" structure to offer opportunities for private and public investors with different risk, return, and exit requirements. This would provide a financing package that includes- reimbursable funds, subordinate debt, guarantees, and technical assistance.



GREEN FINANCE

KEY FACTS

#1 in green-to-brown ratio.

The IDBG has the highest "green-to-brown" ratio of assets and infrastructure investments of all MDBs.

#1 in climate mobilization.

Since 2010, the IDBG has mobilized and managed more donor climate resources than any other individual international organization in LAC.

+US$7 billion.

The aggregated amount of climate finance generated in one year alone by the IDBG (2016), including the IDBG's own capital and resources committed by donors, recipient-country governments, and private sector entities.

What is green finance?

At the IDBG, green finance refers to the financing of investments that provide environmental benefits in the broader context of sustainable development in LAC, including the financing of operations and components that deliver climate change mitigation and adaptation activities. Green finance includes the financing of sustainable infrastructure, sustainable landscapes and land management (including REDD+ and conservation), sustainable cities, and sustainable islands.

Why support green finance in Latin America and the Caribbean?

- LAC is a biodiversity superpower. A fifth of the region's territory has been set aside for conservation – far surpassing the developing world average of 13%. Despite conservation progress, current national budgets are not keeping pace with needs.
- LAC needs to invest at least 5% of GDP in infrastructure per annum to meet demand (variously defined), which would require additional infrastructure investment of about 2.5% of GDP annually. Sustainable Infrastructure can play an important role in filling the infrastructure gap in a climate friendly and resilient way.
- Latin America and the Caribbean's institutional and financial capabilities make it a cost-effective location for the testing of innovative approaches and transformational green finance models which can be replicated in other developing regions.

What instruments does the IDBG use to implement green finance?

The IDBG is considered a partner of reference for developing green finance solutions with a high development impact. Given the IDBG's strong due diligence process, ESG safeguards, integrity, and credit risk filters, partnering with the IDBG sends a strong signal and "seal of quality" when mobilizing funds from institutional investors. The IDBG implements green finance solutions through several types of innovative financing instruments, tailoring each solution to the local context. The IDBG can combine multiple instruments to address specific project or market constraints and to maximize the potential development impact of any given intervention. In partnership with donors, the IDBG uses debt solutions to lower the cost of capital and bring down technology costs, guarantees and innovative forms of technical assistance, and contingent and project preparation grants.

What are some examples of the IDBG's innovative green finance partnerships?

BONDS FOR GREEN RESULTS

A notable example developed the world's first green bond aggregation platform by bundling and pooling small-scale energy efficiency projects unlocks long-term financing from institutional investors. Approved by the Green Climate Fund in the first ever approval package, the G20 Climate Finance Study Group (Turkey, September 2015) recognized this structure as the best practice for unlocking financing for energy efficiency projects through capital markets securities. Developed in partnership with the Green Climate Fund and the Clean Technology Fund, one of the objectives of this US$146.9 million operation is to mobilize an additional US$200 million from institutional investors. This project is breaking new ground not only in Mexico but globally as it will be the first ever bond issuance backed by energy savings receivables. It promotes impact investing and opens a new financing channel for small-scale energy efficiency projects.

GRANTS FOR GREEN RESULTS

The Sustainable Colombia Facility is the largest payment for verified GHG emission reduction from deforestation and forest degradation (REDD+) partnership with an MDB in LAC.
This US$280 million facility is the largest payment for verified greenhouse gas emission (GHG) reductions from deforestation program in Latin America and the Caribbean, excluding Brazil. Developed in partnership with the Governments of Norway, Sweden, and Switzerland, the facility will provide significant support to help Colombia achieve its ambitious goals of zero net deforestation in the Amazon by 2020 and halting loss of all natural forest by 2030. The 15-year facility is expected to support the implementation of the SDGs and Colombia's Nationally Determined Contributions to the Paris Climate Accords.

CAPITAL MARKETS FOR GREEN RESULTS

Introducing a natural capital asset class in global exchange markets - the Central Suriname Nature Reserve Company. At the cutting edge of financial innovation and conservation, the IDBG is partnering with the Government of Suriname and the Intrinsic Value Exchange (IVE), a United States company, to demonstrate the viability of a new financial asset class that can bring sustainable investing into the mainstream of the economy. The partnership does this through the introduction, for the first time in the LAC region, of an equity IPO for "natural capital". By creating the first market for natural assets, IVE can directly address a core financial markets failure that today does not properly value natural assets. If successful, this innovation has great potential as an alternative private-led solution, in the context of compliance with the global commitments to climate change and biodiversity.

What is next on green finance for the IDBG?

The infrastructure financing gap will continue to increase the disposition of LAC governments to fund infrastructure through creative structures that minimize the exposure of governments to external shocks. As such, the IDBG will continue to expand its climate and blended finance initiatives through innovative financial instruments that can be replicated to develop smart energy projects, as well as highways, ports, airports, telecommunications and electric mobility. Furthermore, the IDB Group is developing a sustainable infrastructure framework that will help scale up investments.

The IDBG will also continue expanding the scope of its green finance partnerships on sustainable landscapes and land management, natural capital, sustainable cities, and sustainable islands in the region, especially seeking to catalyze the private sector and mobilize commercial and domestic resources to support the implementation of the NDCs.

JOIN US!

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Resource Mobilization Division

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Financing the Future with the IDB Group

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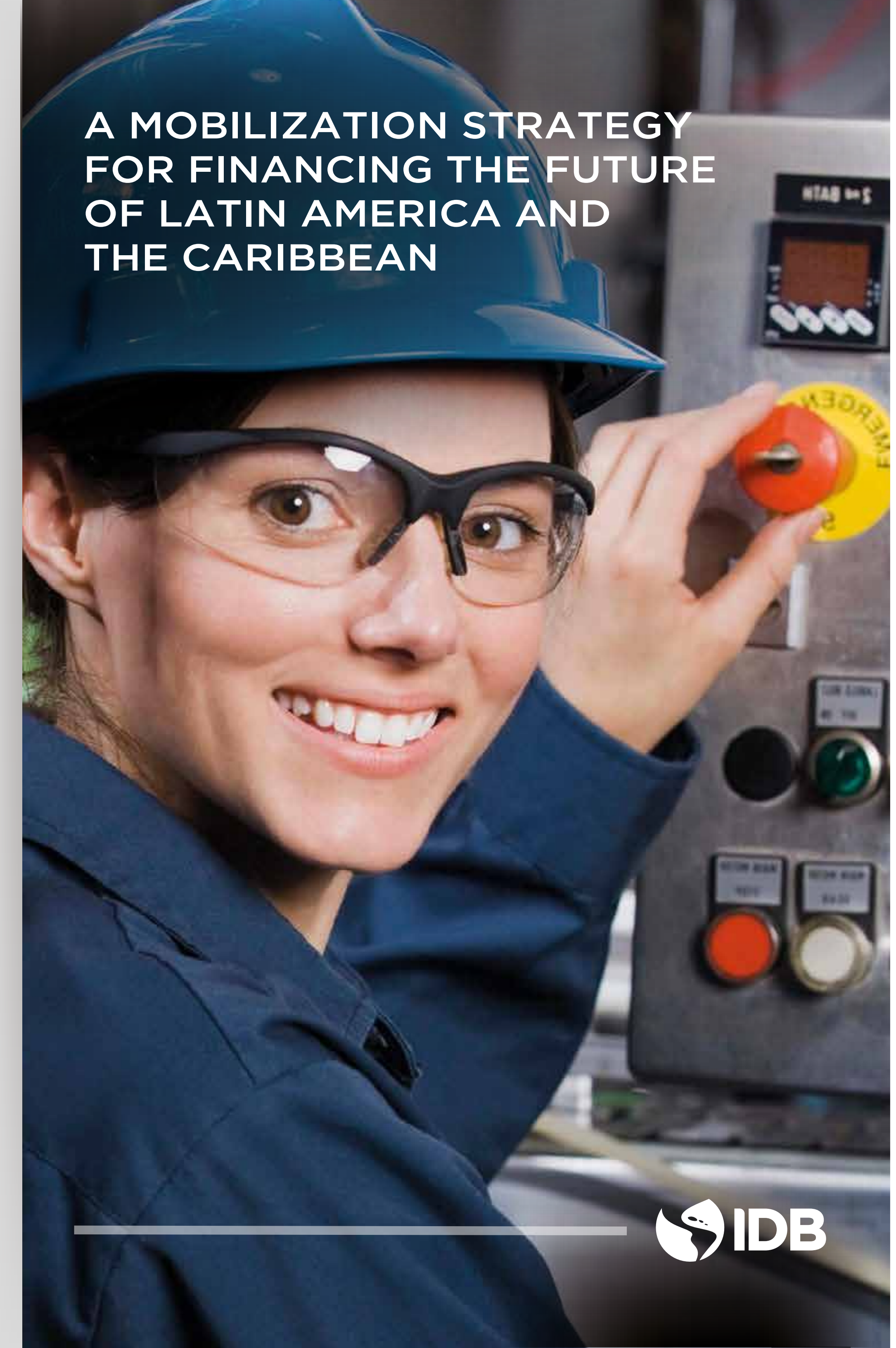
A MOBILIZATION STRATEGY FOR FINANCING THE FUTURE OF LATIN AMERICA AND THE CARIBBEAN



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