

The State of Blended Finance 2020



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- Liquidnet
- Organization for Economic Development and Coordination (OECD)
- Sanlam Investments
- Shell Foundation (UK-based charity)
- responsAbility Investments AG

This acknowledgment does not imply endorsement by these individuals or institutions of the analysis and views presented in this report.

Letter From CEO



I am pleased to introduce the 4th edition of Convergence's flagship report, *The State of Blended Finance*. In four years, *The State of Blended Finance* has become an authoritative reference point on the global blended finance market, presenting data and analysis from the largest and most detailed database on historical blended finance transactions.

Since the first publication, we have written this report in-house, as a team, with the goal of using our unique position at the core of a growing ecosystem to reflect objectively on the field, and to help investors and funders strategically place their capital in support of the Sustainable Development Goals. We issue the report with humility, knowing that our data will never be complete, and we are always looking for ways to increase its value as a public good.

This year, for the first time, we supplement our analysis with perspectives from key stakeholders and a forecast of where the blended finance market is going. These additions were made possible because our own network of funders, investors and practitioners has grown and become more representative of the field, and because the fundraising activity unfolding on our live transactions platform has reached significant scale.

2020 has been turbulent, with aid budgets in distress and investors retreating from countries and transactions most in need of development assistance and capital injection. Yet, it has also been a time of abrupt awakenings to the linkages between money, society, and nature, and a time of reimagined collaboration and dialogue among divergent sources of capital. This increased awareness and collaboration happen to be two prerequisites for composing blended transactions. We proceed with the hope that more and better-designed blended finance will come from this disruptive moment.

Our deepest thanks to the investors and funders putting their capital to work, and to those who contributed their expertise to the report.

We look forward to the conversations and deals ahead.

A handwritten signature in black ink that reads "Joan M. Larrea". The signature is written in a cursive, flowing style.

JOAN M. LARREA
CHIEF EXECUTIVE OFFICER, CONVERGENCE

Executive Summary

The Sustainable Development Goals (SDGs) target a range of development challenges, from combating climate change to ending poverty and hunger. To achieve the SDGs in developing countries, a significant scale-up of investment is required. Blended finance is the use of catalytic funding (e.g., grants and capital) from public and philanthropic sources to mobilize additional private sector investment to realize the SDGs. Blended finance is one of several approaches to financing the SDGs, with the United Nations (UN) member countries reaching consensus on its importance at the Third International Conference on Financing for Development in 2015. Since then, blended finance has become a familiar concept for a diverse set of organizations across the public, private, and philanthropic sectors.

This report uses blended finance data and insights compiled by Convergence to provide an updated analysis of the blended finance market, including blending approaches, sectors, regions and investor trends. We are also excited to include the following additions for the first time to this year's report:

- Interviews with leading experts in the blended finance market, including representatives from development agencies, multilateral development banks (MDBs), development finance institutions (DFIs), impact investors, and institutional investors ('Voices from the Field')
- A forecast of emerging trends in the blended finance market, leveraging Convergence's collection of data on transactions seeking blended capital, including from our proprietary matchmaking platform

The State of Blended Finance 2020 concludes with reflections on the journey to advancing blended finance at scale, exploring key challenges and progress made to date. Lastly, the report considers the impact of the COVID-19 pandemic on the blended finance market and the attainment of the SDGs in developing countries.

Deal Trends

Convergence has captured nearly 600 blended finance transactions, representing aggregated financing of nearly \$144 billion¹ to date. Key findings from this report include:

- Blended finance activity has remained fairly consistent year-on-year, by transaction count and by deal flow, since the adoption of the SDGs in 2015. These trends mirror broader development finance flows; current blended finance flows will mobilize "billions to billions," not "billions to trillions."
- Funds have consistently accounted for the largest share of blended finance transactions, indicating that these structures have achieved some level of efficiency in the market relative to other vehicles. At the same time, vehicles are diversifying, including a notable uptick in the prevalence of bonds from 2017-2019.
- There has been a decrease in the concurrent use of multiple blending approaches (e.g., concessional debt or equity and technical assistance grants) in financial structures. Convergence views this as a preliminary but positive signal, indicating less complexity is being incorporated into blended finance products as more structures become streamlined.
- Sub-Saharan Africa remains the most targeted region for blended finance; however, we continue to see a shift towards greater blended finance activity in Asia, in line with our previous predictions.
- Overall, blended finance activity continues to be heavily focused on two sectors: energy and financial services. However, using Convergence's live market data as a leading indicator, we expect increased momentum in agriculture, health, and to some extent, education, in the years ahead.

¹ Note all \$ figures are in USD.

Investor Trends

This report identifies over 1,274 organizations that have participated in blended finance to date. Key findings on investor trends include:

- MDBs and DFIs have been the most frequent investors in blended finance to date.
 - Development agencies, MDBs / DFIs, and foundations / non-governmental organizations (NGOs), together, have accounted for the bulk of concessional financing.
 - Amongst commercial investors, financial institutions (e.g., commercial banks) and corporates (e.g., multinational companies) have been the most frequent investors in blended finance.
 - The number of debt commitments and debt investors in blended finance is rising.
 - Local investors and institutional investors remain underrepresented in blended finance.
- Key efforts include the Catalytic Capital Consortium (C3), the DFID-led Blended Finance Scale Working Group, the OECD-led Tri Hita Karana (THK) Roadmap for Blended Finance, the launch of the Response, Recovery, and Resilience (R3) Investment Coalition, and the launch of Liquidnet's Billions to Trillions (B2T) Initiative.
- There is good potential to scale blended finance for health, bolstered by positive evidence from Convergence's fundraising data, and driven by a renewed urgency due to the COVID-19 pandemic.
 - In line with previous reporting, Southeast Asia has proven to be a key emerging area for blended finance, with activity increasing over the past three years.
 - Lastly, gender lens investing in blended finance has also received greater attention, as shown by the proliferation of resources, toolkits, and initiatives led by actors across the public, private, and philanthropic sectors.

In our conversations with key blended finance stakeholders, we explore some of the factors behind the low participation of local institutional investors in blended transactions, including requirements for liquidity in their investments.

Ecosystem Trends

Blended finance is moving from policy to practice; over the past year, blended finance has experienced an uptick in coordinated activities in an effort to achieve more effective and efficient uses of blended finance approaches.

Reflections

For blended finance to mobilize private capital at scale and meet the challenge of COVID-19...

...We urge concessional finance to become more efficient, prioritizing portfolio approaches and simplifying structures...

...While embracing greater transparency and targeting capacity-building amongst local institutional investors

While knowledge and understanding of blended finance continues to increase amongst different stakeholders, important challenges, new and old, stand between catalytic capital providers and the effective mobilization of private capital at scale and the achievement of the SDGs.

Although blended finance has maintained a steady number of transactions year-on-year, current volumes will fall short of the “billions to trillions” needed to meet the \$2.5 trillion annual investment gap to achieve the SDGs by 2030. The supply of donor and philanthropic capital is not changing dramatically – official development assistance (ODA) and concessional financing have been relatively unchanged in recent years. Therefore, we urge concessional capital providers to become more efficient and prioritize portfolio approaches and standardized structures to help mobilize institutional capital at scale.

Meanwhile, there is greater collaboration amongst private actors, whose deep pockets blended finance looks to mobilize. Examples include Liquidnet’s Billions to Trillions Initiative (B2T), HSBC’s Finance to Accelerate the Sustainable Transition-Infrastructure (Fast-Infra) Initiative, and JP Morgan Chase’s \$100 billion development finance institution. This is an opportunity we urge providers of catalytic capital to pursue.

The urgency of the task at hand has been heightened by the COVID-19 pandemic, which currently poses the biggest challenge to the blended finance industry. The scale of its economic impact and its threat to the achievement of the SDGs is such that big, creative thinking is required to ensure blended finance can mobilize the amount of private capital needed to effectively build back better in the post-pandemic economic reconstruction. In this challenge lies the opportunity. The time for blended finance at scale is now.

Other challenges also remain. The low participation of local institutional investors in blended finance, for example, must be tackled by an extensive process of capacity-building and education. This must be accompanied by progress in finding what works and in achieving a level of standardization, simplicity and replicability across blended structures. Boosting engagement between providers of catalytic capital, fund managers and institutional investors will require a continued focus. We also call upon catalytic capital providers to continue experimenting with new approaches in their efforts to mobilize private capital at scale, better right-size first-loss protection, support project preparation, provide greater volumes of credit enhancement also targeting domestic investors.

In addition, we call upon the blended finance community – and the donor community – at large – to increase transparency (including on investment terms and conditions) and impact reporting within transactions, especially ex-post. Greater transparency is an essential step towards improving the coordination, accountability and effectiveness of blended finance, with greater transparency around returns and terms also supporting standardization in the market. Meanwhile, impact reporting in the blended finance market to date has been low, reflecting an overarching challenge in the official development community. Currently, over 40% of blended finance transactions do not report impact publicly. Encouragingly, stakeholders are making good progress here, with initiatives such as the THK Roadmap leading the charge. To achieve the full potential of blended finance, the focus on scaling up solutions must be accompanied by increased transparency and measurable impact.

Introduction

Blended Finance

The SDGs are a set of 17 global goals set by the United Nations (UN) to tackle a range of development challenges, from combating climate change to ending poverty and hunger. The SDGs aim to create a world that is more sustainable and that offers real opportunities to leverage the expertise and resources of the private sector.

To achieve the SDGs, a significant scale-up of investment is required. The UN estimates that the annual funding needed to achieve the SDGs by 2030 is nearly \$4 trillion – much greater than the estimated current SDG-focused funding of \$1.3 trillion from domestic and international sources.² The \$2.5 trillion gap dwarfs official development flows and philanthropic commitments: the Organization for Economic Cooperation and Development (OECD) reports total official development assistance (ODA) from the 30 OECD Development Assistance Committee (DAC) members at nearly \$153 billion,³

while Development Initiatives estimates private development assistance (e.g., development assistance from non-public sources like foundations, corporations, and NGOs) to be around \$45 billion.⁴

Blended finance is one critically important approach to mobilizing new sources of capital for the SDGs. This was realized at the Third International Conference on Financing for Development in 2015 in Addis Ababa, when UN member countries reached a consensus on the importance of deploying public funds to attract private investment. Convergence

² OECD. (2019). “Development aid drops in 2018, especially to neediest countries”. Paris: OECD. April 10, 2019. Accessed August 8, 2019. <https://www.oecd.org/newsroom/development-aid-drops-in-2018-especially-to-neediest-countries.htm>

Note: Official development assistance (ODA) from the 30 members of the OECD’s Development Assistance Committee (DAC) totalled \$153 billion in 2018 as calculated using the new “grant-equivalent” methodology adopted as a more accurate way to count the donor effort in development loans. Under the “cash-flow basis” methodology used in the past, 2018 ODA was \$149.3 billion.

Note: The 30 DAC members include Australia, Austria, Belgium, Canada, Czech Republic, Denmark, European Union, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, the Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, United Kingdom, and United States.

³ OECD. (2020). “Aid by DAC Members increases in 2019 with more aid to the poorest countries”. Paris: OECD. April 16, 2020. Accessed October 1, 2020. <https://www.oecd.org/dac/financing-sustainable-development/development-finance-data/ODA-2019-detailed-summary.pdf>

⁴ Development Initiatives. (2016). Private development assistance: key facts and global estimates. Bristol: Development Initiatives. August 15, 2016. Accessed August 8, 2019. <http://devinit.org/post/private-development-assistance-key-facts-and-global-estimates/>

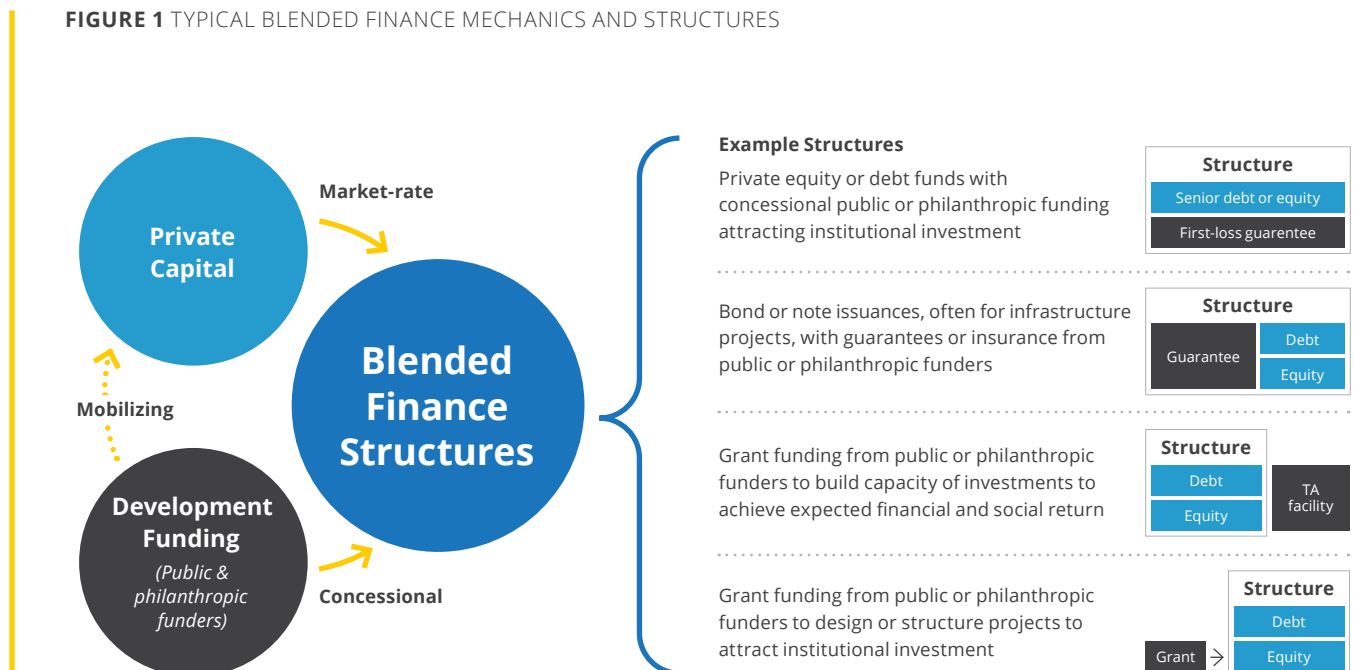
was established out of the Addis Ababa Action Agenda to build the blended finance market to attract significantly higher amounts of private capital to the SDGs. Since then, blended finance has become a familiar concept for various stakeholders – from development agencies to private foundations, impact investors to commercial banks.

Convergence defines blended finance as the use of catalytic capital from public or philanthropic sources to increase private sector investment in developing countries to realize the SDGs. Blended finance allows organizations with different objectives to invest alongside each other while achieving their own objectives (whether it's financial return, social impact, or a blend of both). The main investment barriers for private investors addressed by blended finance are (i) high perceived and real risk and (ii) poor returns for the risk relative to comparable investments. Blended finance creates investable opportunities in developing countries, which leads to more development impact.

Blended finance is a structuring approach, not an investment approach, instrument, or end solution. *Figure 1* highlights four common blended finance structures:

- i. Public or philanthropic investors provide funds on below-market terms within the capital structure to lower the overall cost of capital.
- ii. Public or philanthropic investors provide credit enhancement through guarantees or insurance on below-market terms.
- iii. Transaction is associated with a grant-funded technical assistance facility that can be utilized pre- or post-investment.
- iv. Transaction design or preparation is grant-funded (including project preparation or design-stage grants).

FIGURE 1 TYPICAL BLENDED FINANCE MECHANICS AND STRUCTURES

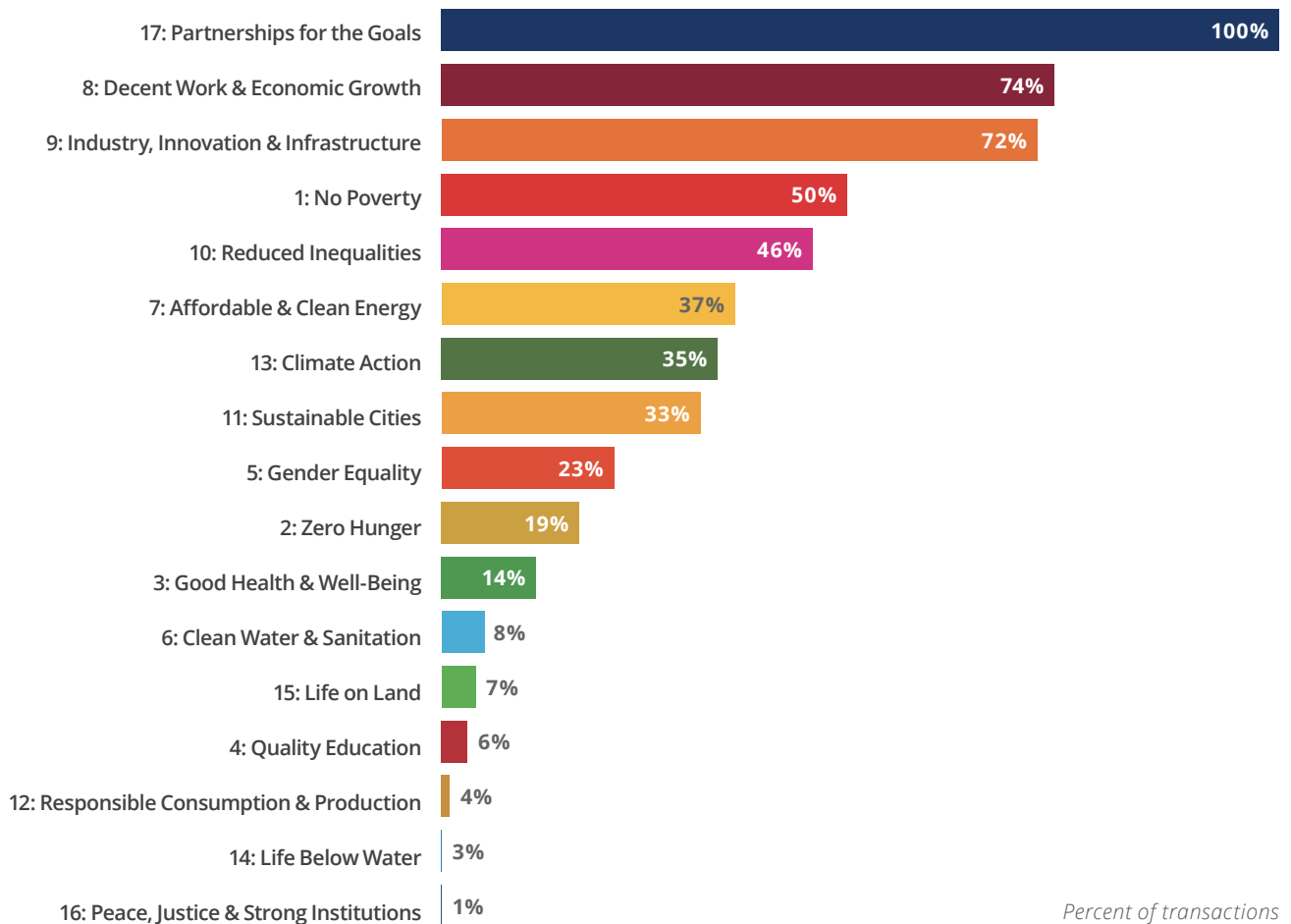


Concessional capital and guarantees / risk insurance are used by the public and philanthropic sectors to create an investment opportunity with acceptable risk-return profiles for the private sector by (i) de-risking the investment, or (ii) improving the risk-return profile to match with the market for capital. Concessional funding includes scenarios where the public or philanthropic funder takes a higher risk profile for the same (or a lower) rate of return, or the same risk profile for a lower rate of return. Design-stage grants are not direct investments in the capital structure but improve a transaction’s probability of achieving bankability and financial close; similarly, technical assistance funds operate outside of the capital structure to enhance the

viability of the endeavor and improve impact measurement.

It is important to note that blended finance can only address the subset of SDG targets that are investable. According to analysis conducted by the Sustainable Development Solutions Network (SDSN, a global initiative of the UN), approximately half of the funding required to achieve the SDGs in developing countries can be in the form of investment finance. For example, blended finance is highly aligned with goals such as Goal 8 (Decent Work and Economic Growth) and Goal 13 (Climate Action) but is less aligned with SDGs such as Goal 16 (Peace, Justice and Strong Institutions).

FIGURE 2 ALIGNMENT BETWEEN BLENDED FINANCE TRANSACTIONS AND THE SDGS (2014-2019)



Report Methodology and Overview

The State of Blended Finance is Convergence's annual report on blended finance trends, opportunities, and challenges. It builds on the inaugural report released in July 2017.⁵ The State of Blended Finance 2020 provides an updated analysis of the blended finance market based on Convergence's continuous data and intelligence collection efforts, and outlines key blended finance trends and developments in the past year. The report includes input from Convergence's 200 member institutions and other key market participants.

Convergence curates and maintains the largest and most detailed database of historical blended finance transactions to help build the evidence base for blended finance. Given the current state of information reporting and sharing, it is not possible for this database to be fully comprehensive, but it is the best repository available globally to understand blended finance trends. Convergence continues to build out this database to draw better insights about the market, and disseminates this information to the development and investment communities to improve the efficiency and effectiveness of blended finance targeting the SDGs. This year, Convergence also leverages in-house data from its proprietary live deals database to provide a forecast on emerging trends in the market. Given the preliminary nature of fundraising data, this forecast is an early indication of the market and is subject to change. All data in this report reflects Convergence's collection efforts as of September 2020.

Information is collected from i) credible public sources such as press releases, ii) information sharing agreements with key data aggregators like the OECD, and iii) validation exercises with Convergence's members and partners. To be included in Convergence's database, a deal must meet three main criteria:

1. The transaction attracts financial participation from one or more private sector investor(s)
2. The transaction uses catalytic funds in one or more of the following ways:
 - Public or philanthropic investors provide catalytic and concessional capital, bearing risk at below-market returns to mobilize private investment, or provide guarantees or other risk mitigation instruments
 - Transaction design or preparation is grant-funded
 - Transaction is associated with a technical assistance facility (e.g., for pre- or post-investment capacity building)
3. The transaction aims to create development impact related to the SDGs in developing countries

⁵ The State of Blended Finance 2017 was jointly produced by Convergence and the Business and Sustainable Development Commission's Blended Finance Taskforce (BFT). The purpose of the working paper was twofold: (i) to expand the evidence base around the potential of blended finance to help close the SDG funding gap and (ii) to inform the recommendations the BFT intended to deliver to unlock systemic barriers in the blended finance ecosystem that were preventing the flow of mainstream capital into blended finance transactions at scale. Based on the work of Convergence and others, the BFT produced an Action Programme in early 2018.

This report has four main sections:

- 1. Deal Trends** provides an updated analysis of blended finance solutions in the market, including blending approaches, sectors, regions, and development impact.
- 2. Investor Trends** highlights the most prominent investors in the space, key investment trends, and new developments from investors over the past year.
- 3. Ecosystem Trends** provides an overview of key initiatives in the field as the blended finance community moves from policy to practice, as well as emerging trends.
- 4. Reflections** looks back on the progress made in the practice of blended finance over the past year and the key challenges that remain, including considerations for scaling the most impactful development solutions in the wake of COVID-19.





Deal Trends

Convergence curates and maintains the largest and most detailed database of historical blended finance transactions that mobilize private investment towards the SDGs in developing countries. The Deal Trends section and the following Investor Trends section present an updated market analysis and review of key developments and trends to help practitioners who are considering or evaluating new blended finance transactions.

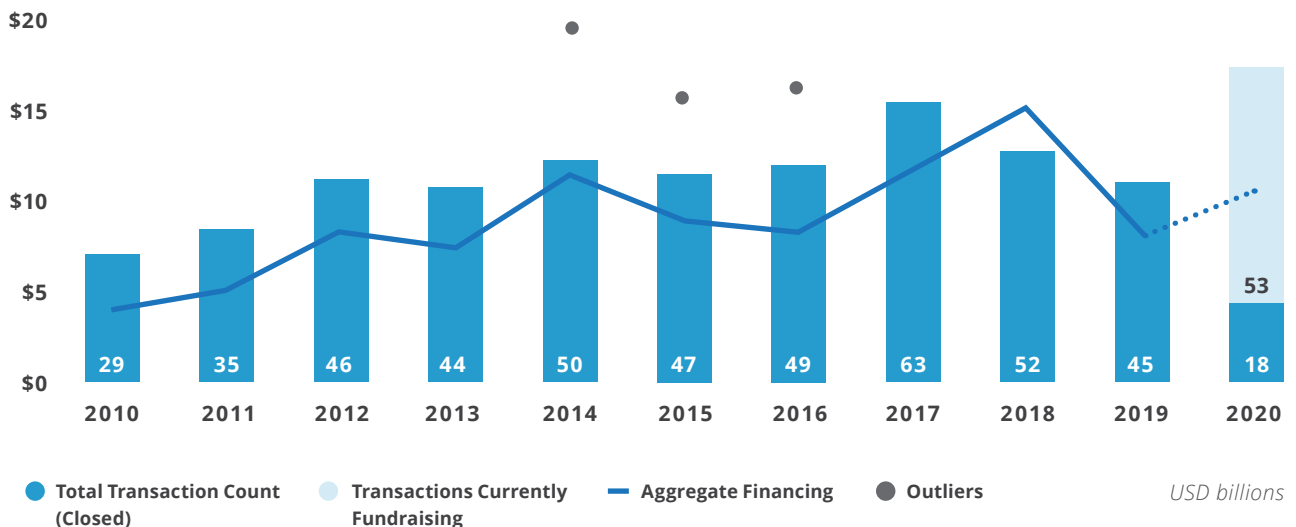
Overall Market

This report looks at nearly 4,300 financial commitments and nearly 600 blended finance transactions, representing nearly \$144 billion in aggregate financing (as of September 2020). The blended finance market has experienced a consistent number of 45-50 annual transactions since 2015, with 45 launched in 2019 (collected so far).⁶ Annual financing has remained fairly consistent, averaging ~\$11 billion per year over the course of 2014-2019; though, this value has varied as a result of several large-scale, billion-dollar initiatives.⁷ Relatively stable year-on-year blended finance flows also map closely to development financing trends, as reported by donor governments

and development finance institutions (DFIs) / multilateral development banks (MDBs). For example, [preliminary data](#) on official development assistance (ODA) for 2019 reveals relatively unchanged numbers, with ODA increasing by 1.4% compared to 2018. Similarly, the DFI Working Group on Blended Concessional Finance for Private Sector Projects [reports](#) that concessional financing provided by DFIs was about the same in 2019 as in 2018 (around \$1.1 billion).

Based on provisional data for 2019, blended finance flows totalled approximately \$8 billion, falling below average flows recorded for 2017

FIGURE 3 OVERALL BLENDED FINANCE MARKET (2010-2020)



⁶ Blended finance data collected for 2019 reflects a preliminary estimate, based on publicly available data. Due to a time lag in publicly available information for closed transactions, Convergence is confident that this figure is a conservative estimate. In addition, Convergence does not consider transactions that have raised commercial capital from only public sector institutions as blended finance (referred to as public-on-public blending), or vehicles that are purely concessional but whose downstream investments raise public and private commercial capital. This differs from the methodology of other key blended finance players such as the OECD and the DFI Working Group on Blended Concessional Finance.

⁷ Grey dots in Figure 3 denote outliers, representing aggregate financing if individual transactions >\$5 Billion in 2014, 2015, and 2016 are included.

and 2018. This follows broader market trends for developing countries. For example, the [World Investment Report \(WIR\) 2020](#) found that FDI flows to developing economies declined marginally from 2018 to 2019, by 2%. This slump was particularly acute in Africa, which experienced a 10% decline; this region also accounts for a sizeable proportion of blended finance activities (for example, 33% of transactions targeted Sub-Saharan Africa between 2017-2019). Decreased aggregate financing in 2019 could also reflect a time lag in information becoming available on recently closed transactions.

Convergence's 2020 State of Blended Finance report also draws upon Convergence's in-house knowledge of transactions raising blended capital, including those posted on Convergence's fundraising deal platform. Convergence has collected data from over 50 transactions currently fundraising, with aggregate financing of approximately \$10 billion. This includes blended finance transactions that have completed a first close prior to 2020 and are currently seeking another round of capital, as well as new blended vehicles.⁸

Deal Sizes and Types

Convergence collects data on five common transaction types: (i) bonds / notes (including development impact bonds (DIBs), (ii) companies, (iii) facilities, (iv) funds, and (v) projects. Funds (e.g., equity funds, debt funds, and funds-of-funds) have consistently accounted for the largest share of blended finance transactions (38% of transactions over 2017-2019, and 43% historically). This prevalence suggests that funds introduce a level of efficiency and comfort for investors, relative to other blended finance vehicles

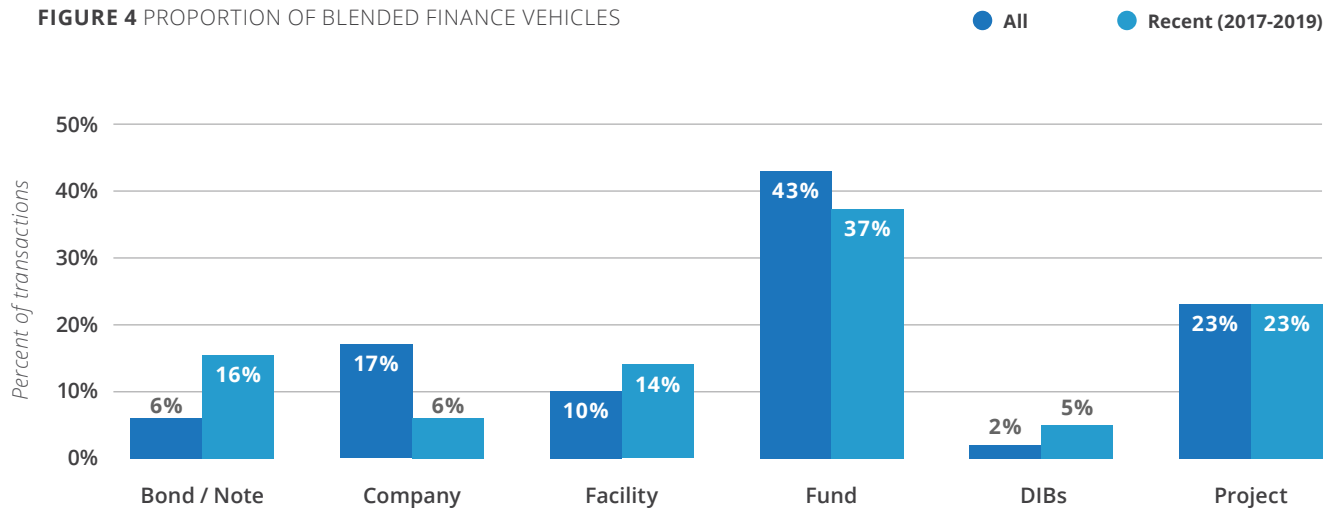
where transactions costs may be higher. Given their dominance in the market, blended funds represent an important vehicle for mobilizing private capital to achieve the SDGs. Convergence maintains that for the blended finance market to reach scale, it is crucial that structures reach a level of standardization and simplicity that appeal to the mandates of institutional investors. The traction achieved by blended funds suggests that a level of standardization in the use of blended structures has been attained.

“Effectively standardizing funds is still very hard. Here, we are speaking about debt funds. In private equity, it is a little bit cleaner and clearer, because the private equity world is a lot more standardized, and you do not see as much blended finance there. In the blended finance world, we are still testing different models and structures, and we are not yet at the final point where we can say, these are the six structures that work best. That might take another 5-10 years. It is currently pretty similar to where microfinance was in the 1990s.”

SIMON GUPTA, HEAD OF BUSINESS DEVELOPMENT DFI / IFI, RESPONSABILITY INVESTMENTS AG

⁸ To avoid double counting, the \$10 billion figure referenced here does not include capital that has already been raised by transactions that are currently undergoing a successive fundraising round. Similarly, the 53 transactions included in the light blue 2020 bar in Figure 3 do not include transactions already included in Convergence's Historical Deals Database from an earlier close, which are also currently fundraising.

FIGURE 4 PROPORTION OF BLENDED FINANCE VEHICLES



Fund sizes have consistently remained around a median of \$60 million, increasing only slightly in the past three years to a median of \$65 million. However, this could indicate a comfortable size for fund managers rather than a scale challenge. Nevertheless, we have seen a number of large-scale blended funds emerge in the past three years. Examples include Climate Investor One, comprised of three underlying funds, including the blended Construction Equity Fund (\$800 million). Other examples include the SDG 500 platform (currently fundraising for a target close of \$500 million across six underlying funds), the Sub-National Climate Fund (currently fundraising for a target goal of \$750 million), and the Blackrock Climate Finance Partnership (targeting an initial \$500 million raise).

Consistent with previous findings, there has been more diversification across transaction types over the past three years, with funds accounting for a smaller proportion of vehicles (37% of transactions compared to 43% historically). In addition, we have observed increased traction in the use of bonds / notes, which account for 16% of transactions in 2017-19; indeed, 65% of the bonds and notes captured in Convergence's database were launched in the last three years. This includes the launch of several credit-enhanced bonds in

the past few years that have been publicly listed and attracted local investors. A recent example includes the [Acorn Holdings Corporate Bond](#), which launched in 2019 to finance green-certified student accommodation in Kenya. This transaction received credit-enhancement from GuarantCo, and was subsequently listed on the Nairobi Securities Exchange (NSE) and London Stock Exchange (LSE) in January 2020 with a B1 rating by Moody's. Another example is the [Quantum Terminals Corporate Bond](#) that launched in 2018, and achieved a dual listing on the LSE and the Ghana Stock Exchange (GSE).

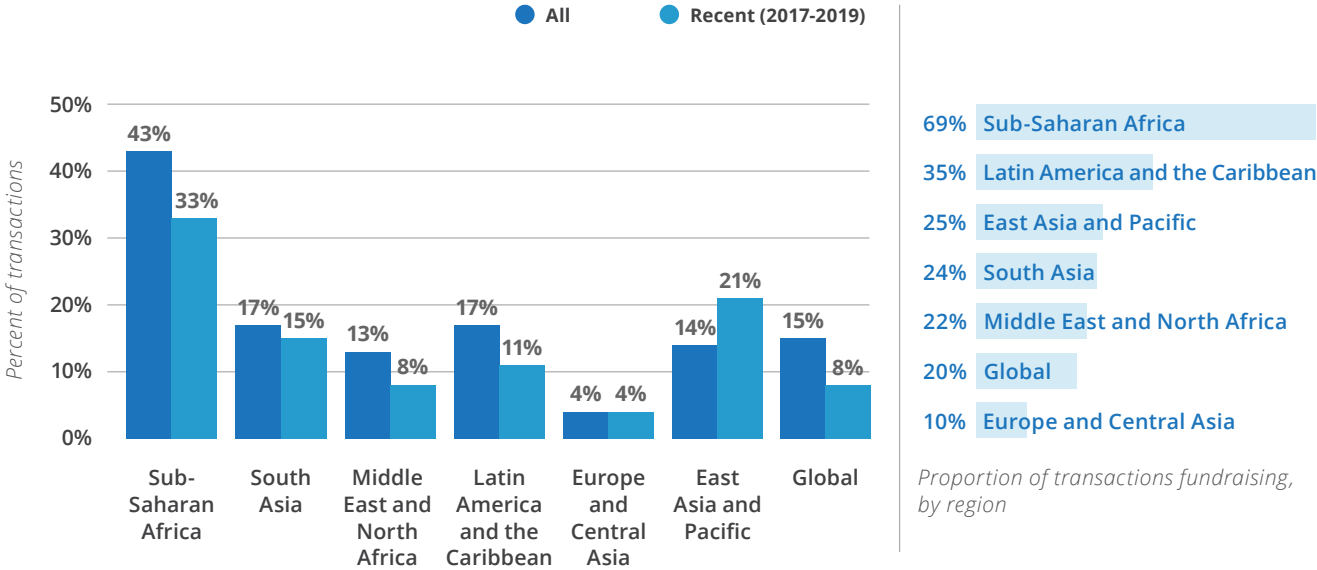
"Listed bonds are typically more attractive to investors because they offer some form of exit, depending on where their risk appetite sits. Bonds also offer greater transparency and price discovery for investors. They can see what the risk/return of a bond is and decide whether that would fit within their portfolio, and whether they can apply the liquidity to get out of it.

So, it is a very powerful way of addressing the information asymmetry that typically exists in developing markets."

LASITHA PERERA, CEO, GUARANTCO

Regions and Countries

FIGURE 5 PROPORTION OF BLENDED FINANCE TRANSACTIONS ACROSS REGIONS



Consistent with previous findings, Sub-Saharan Africa has been the most targeted region for blended finance transactions to date, representing 33% of blended finance transactions launched between 2017-2019, and 43% of the market historically. Despite the high incidence of blended finance in the region, smaller transaction sizes have led to relatively lower aggregate capital flows; aggregate financing accounted for 22% of blended finance flows between 2017-2019, but account for 33% of transactions by count. Indeed, over half (53%) of transactions targeting Sub-Saharan Africa have been between \$10-100 million in size, with a median transaction size of \$52.5 million.

We have also seen a decline in transactions targeting Latin America and the Caribbean, accounting for 11% of transactions launched between 2017-2019. However, this region might

experience renewed interest in the near future; 35% of transactions currently fundraising, as captured by Convergence, are targeting Latin America and the Caribbean.

In line with our previous forecast, Asia is emerging as a new centre of gravity for blended finance, with increased traction in East Asia and the Pacific. For example, East Asia and the Pacific has demonstrated upward growth, on both a proportional and an absolute basis in the blended finance market, representing 21% of transactions from 2017-2019, compared to 14% across all time periods. Indeed, 38% of all transactions targeting East Asia and the Pacific have launched during or after 2017. Aggregate financing to the region has been proportionate to the number of deals; the region represents 21% of blended finance deals, and 19% of financing between 2017-2019.

Looking at the most targeted countries from 2017-2019, the top countries for blended finance have been Kenya (18 transactions), India (16 transactions), Uganda (15 transactions), Indonesia (12 transactions), and Tanzania (10 transactions). There are several factors affecting the frequency of blended finance transactions in Kenya:

“The market in Kenya is more progressive in terms of product innovation, particularly fund managers. This innovation lends itself to designing products and creating strategies that are more investable.”

LOCAL INSTITUTIONAL INVESTOR,
SUB-SAHARAN AFRICA

Other stakeholders point to the logistical advantages of Kenya, noting the number of regional offices headquartered in cities such as Nairobi, allowing for greater collaboration and ease of investments.

While many of these countries have consistently represented the top countries for blended finance flows, we also see traction in new countries, with particular growth in Indonesia; 36% of blended finance transactions focused on Indonesia have been launched since 2017. Moreover, while low-income countries continue to account for a small proportion of blended finance flows, countries like Uganda and Senegal have emerged in the list of the top 10 targeted countries between 2017-2019.

Looking ahead, regional stakeholders like multi-donor fund GuarantCo and the South African insurance company Sanlam pointed to increasing activity in Nigeria, which is one of the top target countries for transactions currently fundraising. While Convergence’s fundraising data maps closely to historical country trends in the market, based on deals currently fundraising we anticipate more blended finance activity in Ethiopia, Colombia, and Malawi.

FIGURE 6 NUMBER OF BLENDED FINANCE TRANSACTIONS ACROSS COUNTRIES (2017-2019)

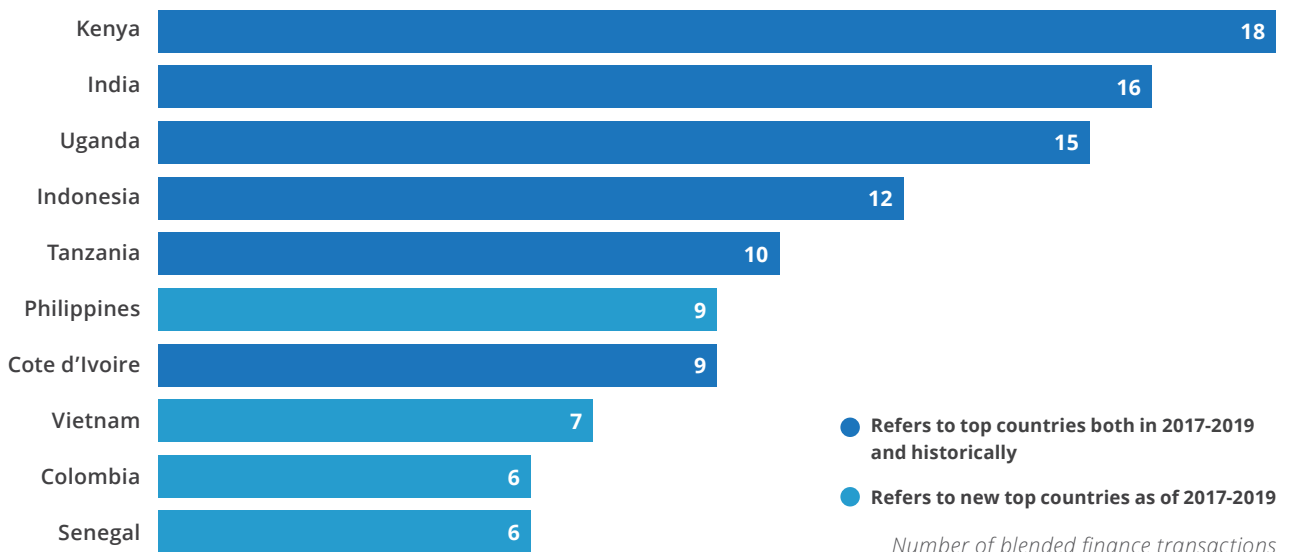
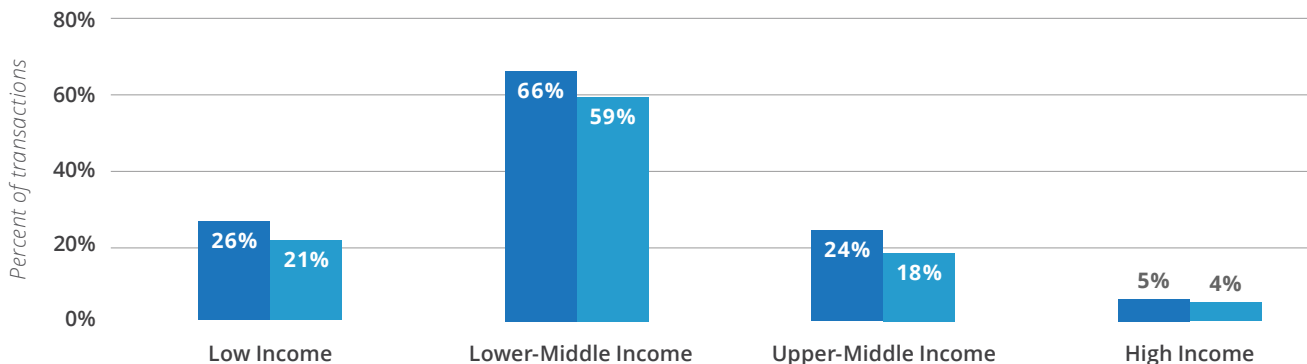


FIGURE 7 PROPORTION OF BLENDED FINANCE TRANSACTIONS ACROSS INCOME-LEVELS

● All ● Recent (2017-2019)



Convergence’s database consistently finds that most blended finance transactions have mobilized capital for middle-income countries, including lower-middle income and upper-middle income countries. These findings are consistent with other reports, including the [2019 version](#) of the DFI Blended Concessional Finance Working Group Joint Report, which found that the largest share of concessional funds, as well as DFI commitments, targeted lower-middle income transactions, followed by upper-middle income countries. Convergence’s data also indicates that blended finance transactions are less frequently targeting multiple regions, given the proportional decrease witnessed across all income levels.

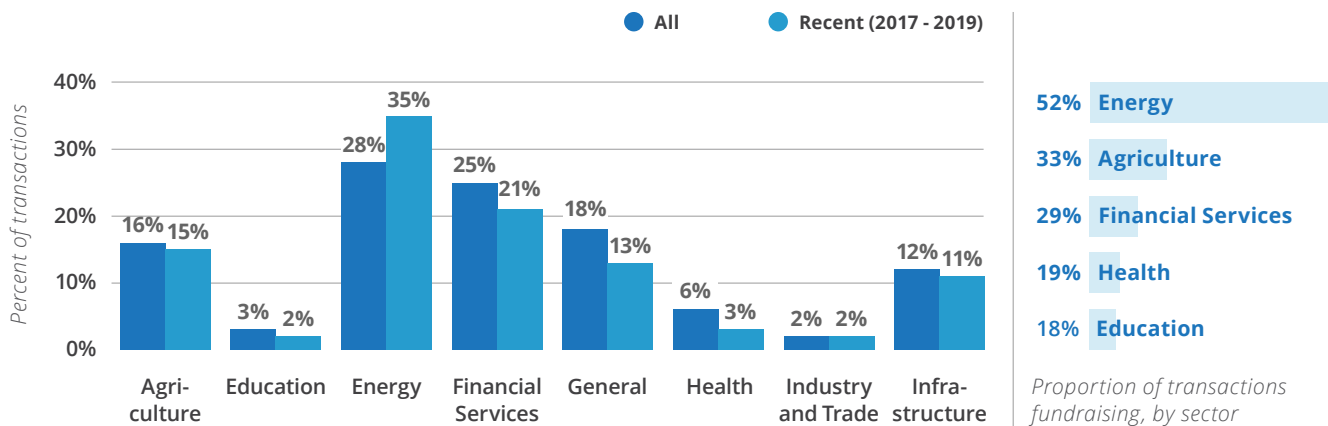
While there has been considerable focus over the past few years on blended finance in the least

developed countries (LDCs), we are yet to witness sustained activity in these markets. Blended finance transactions targeting LDCs are smaller when compared to transactions targeting middle-income and high-income countries, both in terms of average size (\$140 million vs. \$250 million overall), and median size (\$50 million compared to \$57 million), and tend to require more bespoke structures. This customized approach presents a major challenge to achieving scale and requires relatively high costs given the small size of transactions. Blended finance can therefore play a small, but important, role in increasing additional financing into these countries, led by development funders and impact investors. However, traditional sources of aid will continue to be critical.



Sectors and Sub-Sectors

FIGURE 8 DISTRIBUTION OF BLENDED FINANCE TRANSACTIONS ACROSS SECTORS



Energy has consistently accounted for the largest number of blended finance transactions in the market, comprising 35% of all transactions between 2017-2019. These projects are prominent in East Asia and the Pacific, with nearly 38% of all energy projects targeting the region between 2017-2019. Most focus on power generation, including the financing of greenfield and brownfield projects. Around 80% of energy transactions have focused on renewables, including biogas, biomass, geothermal, hydropower, wind, and in particular, solar (including off-grid solutions). Approximately 20% of energy transactions focus on fossil fuels, including projects aiming to increase energy efficiency and develop, store, and transmit fossil fuel resources to advance energy access and affordability. Energy is one of the few sectors where blended finance is commonly structured at the project level; nearly half of blended finance transactions targeting the energy sector have been individual projects, which is double the proportion of projects seen across all blended finance transactions. Transactions in this sector have also been larger; the median blended finance transaction being \$123 million in total size, approximately double the median size across all sectors. Given the commercial traction in the sector

and the imperative for climate-smart solutions, we anticipate clean energy will continue to be the dominant sector for the blended finance market. This prediction is bolstered by Convergence's fundraising platform; energy is the top sector represented amongst transactions that are currently fundraising, representing over half (53%) of transactions captured. To date, other non-energy infrastructure has featured in a smaller proportion of blended finance transactions, most commonly water infrastructure (38% of infrastructure transactions), transportation (29% of transactions), and telecommunication (34% of transactions).

Financial services also account for a sizeable proportion of blended finance transactions, although we have seen this decrease moderately on a proportional (as well as absolute) basis over time; financial services account for 25% of transactions in the database across all years, but 21% of transactions between 2017-2019. Convergence posits, a reduced focus on financial services reflects its track record as a proven asset class, particularly in microfinance and small and medium enterprise (SME) banking, thereby suggesting a reduced need for risk mitigation to attract commercial interest to the sector.

While the proportion of transactions targeting the agriculture sector has remained fairly consistent, Convergence expects more activity in the sector. Agriculture has accounted for a steady proportion of transactions in the market, consistently hovering at about 15% of transactions over time. We see blended finance as a viable solution for the agriculture sector, specifically for agri-finance, agricultural inputs and farm processing, and climate resilient / sustainable agriculture. For example, [Aceli Africa](#), a Convergence grantee, launched in September 2020 with support from 31 partner financial institutions and lenders, to provide financial incentives, including first-loss capital and technical assistance, to lenders who finance agri-SMEs in East Africa. The scale of transactions in the agriculture sector has also increased in recent years. While the median transaction size for Agriculture has been \$35 million across all years, that number increases to \$46 million when looking at transactions launched between 2017-2019. To date, blended finance transactions in conservation have been larger, with a median size of \$87.5 million, and more than twice as likely to be \$100-\$250 million in total size, compared to all blended finance transactions captured by Convergence.

Over the past few years, Convergence has observed a drop in blended transactions with a generalist focus (e.g., multi-sector transactions). This can largely be attributed to a decrease in the concentration of funds in the market, which tend to pursue generalist strategies.

To date, we have not seen sustained activity within the health and education sectors, with both sectors combined accounting for less than 10% of the blended finance market. In recent years, most transactions captured in these sectors have been development impact bonds (DIBs), accounting for 67% of transactions in the health sector, and 75% of transactions in education. DIBs have been lauded for their use in targeted interventions for development outcomes. However, they are often more resource-intensive and smaller in size, therefore posing challenges when looking to scale. Nevertheless, our fundraising platform points to growing interest from

investors in both the education and health sectors. Nearly 19% of transactions actively fundraising are targeting, in full or in part, the health sector, while 18% are targeting education. Given the important role of the public sector in both education and health, blended finance activities must be targeted in areas where there is an additional role for the private sector.

“For us, the main area has been higher education; we have funded traditional universities, a variety of university networks, and some online universities, where we’re seeing a lot of growth, for obvious reasons. The biggest barrier to growth is students’ paying ability; creating innovative structures for student funding could be really helpful in growing the space, as would structures directly linking education to employment. The other area where we have seen growth is early, pre-K education, which is becoming more corporatized and well-structured.”

ELENA STERLIN, SENIOR MANAGER FOR HEALTH AND EDUCATION, INTERNATIONAL FINANCE CORPORATION (IFC)

Meanwhile, Convergence continues to see a greater role for blended finance in advancing healthcare solutions. With the health implications of COVID-19 creating added pressures on health services across developing countries, there is an important opportunity for blended finance to play a greater role. Of course, health covers a broad set of areas, of which only a sub-set are well-suited to blended finance. Current challenges to blended finance in health include: (i) the perception that health should be a public responsibility, (ii) possible negative distortionary effects of greater private engagement in health systems, and (iii) difficulties in achieving the market returns necessary to attract the mainstream investors needed for scale. According to the Convergence database, blended finance has particularly been useful in crowding in capital for health under three spheres: the delivery of health services, SME financing, and pharmaceuticals and vaccinations.

VOICES FROM THE FIELD:

Health and Education in Blended Finance

Interview with Elena Sterlin, Senior Manager for Health and Education, IFC

Q: *Where in the health sector does blended finance hold the most potential?*

A: If you separate health into chronic and infectious disease, all the donor money has been going into infectious disease rather than chronic disease, which is traditionally where the private sector has focused. There is more potential for governments and donors to enter and help reduce the cost of preventing and managing chronic diseases, and there is a lot of space for the private sector to come in on the infectious disease side.

One area where blended finance could be focused is in **local currency financing**. Healthcare services in particular (but even some production) really requires long-term, local currency funding, which very few of the more challenging markets have. So, blended structures de-risking investors' currency exposure could be very interesting. We just closed a deal, **CIEL Healthcare** in Uganda, where we funded a hospital with a blended component that took care of the swap, so we are not taking the currency exposure in this transaction.

Secondly, in poorer countries **SMEs really dominate the health space**, and often do not have access to products or basic medical equipment. So, using blended de-risking structures, we have been putting mechanisms for either leasing or selling equipment on a long-term payment basis to SMEs. But, because they are small, untested, and usually without credit records, more de-risking is required through blended finance.

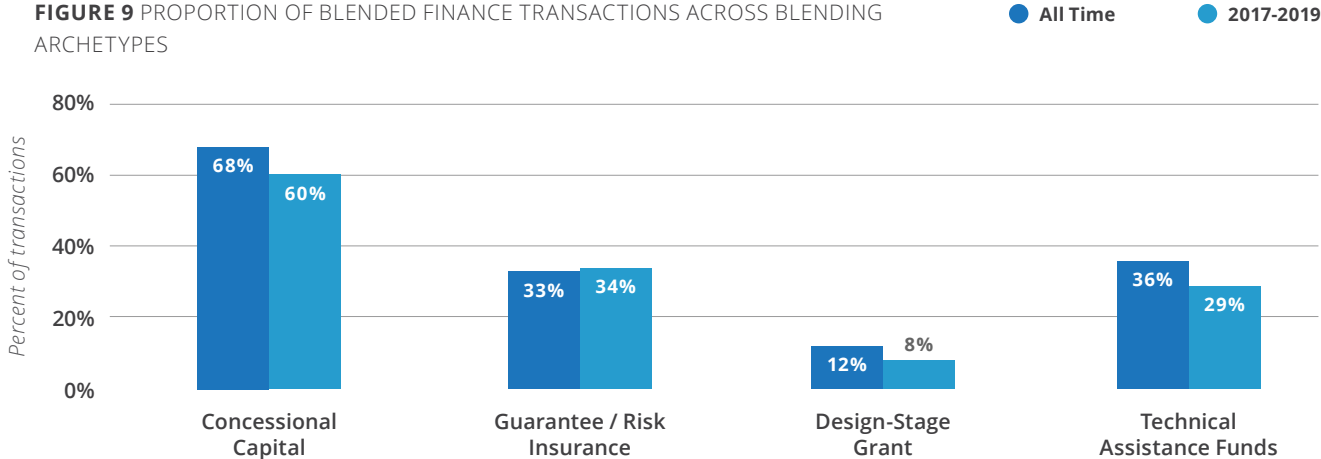
Lastly, is consolidation. Creating networks in healthcare is key for quality standardization and economies of scale. **Creating consolidated networks** in the SME market requires both a high risk appetite and patience. Patient capital can help promote the consolidation of the market and thereby build economies of scale. For example, in this area, we supported the expansion of **Cerba Lancet Africa**, a network of clinical diagnostic laboratories trying to consolidate the African lab test market. However, trying to consolidate, increase volumes to reduce prices, and instill certain standards, is a long journey; we as investors need to be very patient and risk tolerant. For this reason, we supported the company with a first-loss guarantee.

Blending Approaches

Convergence identifies four common blended finance approaches: (i) public or philanthropic investors provide funds on below-market terms within the capital structure to lower the overall cost of capital or to provide an additional layer of protection to private investors (i.e., “concessional debt or equity”), (ii) public or philanthropic investors provide credit enhancement through guarantees

or insurance on below-market terms (i.e., “guarantees or risk insurance”), (iii) the transaction is associated with a grant-funded technical assistance facility that can be utilized pre- or post-investment to strengthen commercial viability and developmental impact (i.e., “technical assistance funds”), and (iv) transaction design or preparation is grant-funded (i.e., “design-stage grants”).

FIGURE 9 PROPORTION OF BLENDED FINANCE TRANSACTIONS ACROSS BLENDING ARCHETYPES



Between 2017-2019, Convergence has observed that blended finance transactions have less commonly use multiple types of concessional capital (i.e., blending archetypes) in a single structure, as indicated by the proportional decrease in blending archetypes across the board. This suggests that these structures are generally becoming less complex. This trend is a positive step towards achieving scale in the blended finance market, given that institutional investors are more drawn to structures that are familiar and easily comparable with other investment opportunities.

Concessional debt or equity continues to be the most common form of blending. However, its prevalence has moderately decreased in recent

years, representing 60% of transactions between 2017-2019. Concessional debt or equity have been commonly used as blending approaches in recent years across funds and companies (71% and 69%, respectively).

Guarantees and risk insurance have been used consistently in the market over time, appearing in a third (33%) of transactions. Guarantees can mobilize more funds per dollar than direct lending or equity investments. For example, the Organization for Economic Co-operation and Development (OECD) [found](#) that more than 40% of the private finance mobilized between 2012 and 2017 was through the use of guarantees. We have seen some vehicles draw more heavily on this type

of risk-mitigation instrument compared to others; for example, 46% of projects and 67% of bonds / notes launched between 2017-19 used guarantees or risk-insurance. In contrast, only 12% of funds launched between 2017-2019 used guarantees / risk insurance. Earlier research conducted by Convergence supports these findings, suggesting that guarantees are particularly well-suited to i) support individual projects (as opposed to a portfolio of projects), and ii) credit-enhance bonds for the development of local capital markets. Benefits of guarantees at the project level include (i) issuance on a temporary basis to bridge the gap between when a project is near-bankable to when it is bankable and (ii) the ability to direct concessionality to specific risks impeding private investments (e.g., political risk or off-take risk) to prevent over-subsidizing investors. In addition, guarantees have played an instrumental role in credit-enhancing bonds, including increasing their likelihood of achieving investment grade ratings, a requirement of many institutional investors. This is largely due to the role of specialized guarantee providers such as GuarantCo (A1 rated), and InfraCredit (AAA), an infrastructure credit enhancement facility established by the Nigerian Sovereign Investment Authority in collaboration with GuarantCo. The Acorn Holdings transaction is a good example of how a credit enhancement can be used to attract local institutional investors and produce investment grade ratings.

In line with previous findings, the use of technical assistance has declined over time, but still accounts for a sizeable portion of blended finance transactions. Almost a third (29%) of the transactions launched between 2017-2019 have used technical assistance or capacity building to support both pre-investment and post-investment activities. Technical assistance can be classified as ODA, explaining its high use as a tool amongst donors and development agencies. Technical assistance has helped support blended finance in new markets through capacity building and

boosting the appetite of local investors. Technical assistance has also served as an important instrument in increasing the commercial viability of social sectors such as health.

Transactions that have received design or project preparation grants accounted for 8% of transactions launched between 2017-2019. Design-stage grants have commonly been used to support deal sponsors developing proof of concept (e.g., completing design and structuring activities before launching a financial vehicle), and / or conducting feasibility studies (e.g., market scoping studies). Meanwhile, project preparation grants have been used to define a project's legal and regulatory requirements, support technical and financial feasibility studies, and determine a project's overall viability.

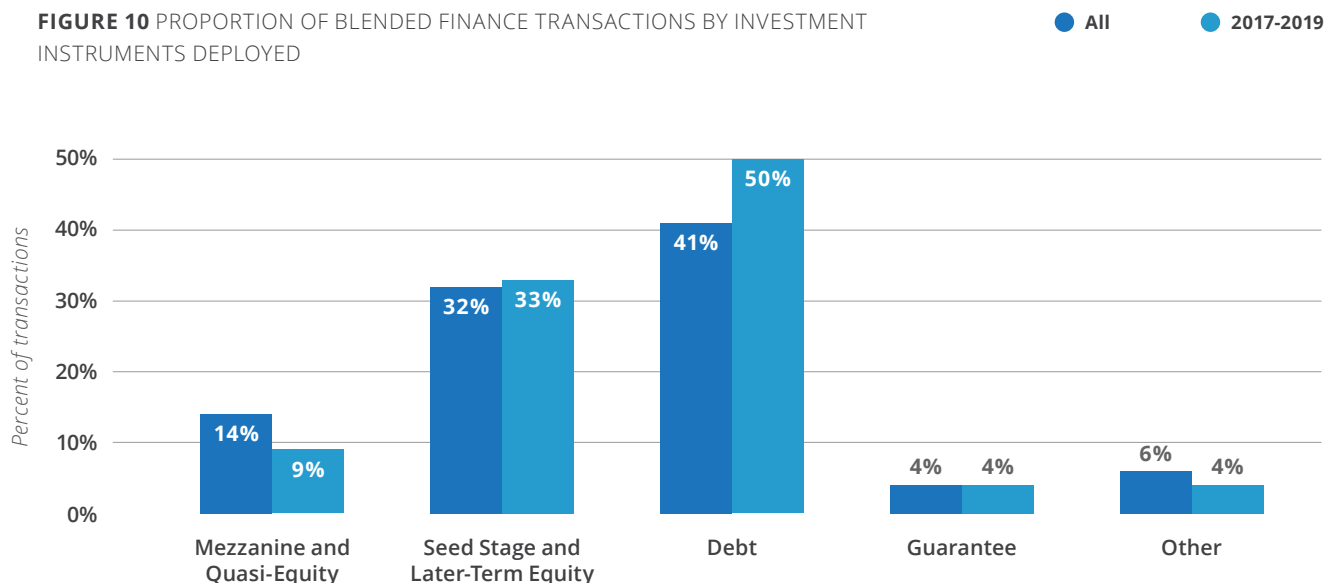
To date, transactions that have received design or project preparation grants have been smaller, both in terms of average (\$127 million vs. \$250 million overall) and median (\$26 million vs. \$57 million) transaction size. This makes sense since design grants support the introduction of innovative, first-time transactions going to market, rather than the scaling up existing constructs. Design and preparation-stage grants have been provided by a variety of organizations and have taken on many forms. Notable programs include those with a more general focus, such as The Rockefeller Foundation's Zero Gap Portfolio and USAID's Development Innovation Ventures program, alongside other sector-specific or region-specific programs. For example, the International Union for Conservation of Nature (IUCN) Blue Natural Capital Financing Facility supports businesses and projects in coastal regions that combine commercial activities with conservation, while the Seed Capital Assistance Facility provides co-financing for clean energy projects in frontier markets. Meanwhile, the Africa Enterprise Challenge Fund is a challenge-oriented fund, which supports agribusinesses and renewable energy companies in Sub-Saharan Africa.

We expect the proportion of transactions using design funding to increase over the next one to two years as more transactions complete proof of concept and launch. As an indicative example, Convergence's design funding program has expanded over the past year to include two additional funding windows, beyond its existing Global Emerging Markets Window, funded by Global Affairs Canada. These include: the Indo-Pacific Design Funding Window, funded by the Australian Government (DFAT) to support solutions focused on sustainable & resilient infrastructure and gender equality, and the Asia Natural Capital Design Funding Window, funded by the RS Group, to preserve and protect natural capital in Asia.

There have been some regional differences in the types of blending approaches used in the market. For example, transactions in Latin America and the Caribbean have been more likely to deploy concessional capital compared to other regions (80% of all transactions), and less likely to use guarantees and / or risk insurance (16% of all transactions). Meanwhile, transactions in East Asia and the Pacific and in Europe and Central Asia have been more likely to use guarantees and / or risk insurance (43% and 47% of transactions respectively). Technical assistance has been most commonly deployed in transactions targeting the Middle East and North Africa. Meanwhile, transactions in Sub-Saharan Africa largely mirror overall market trends.

Investment Instruments and Target Beneficiaries

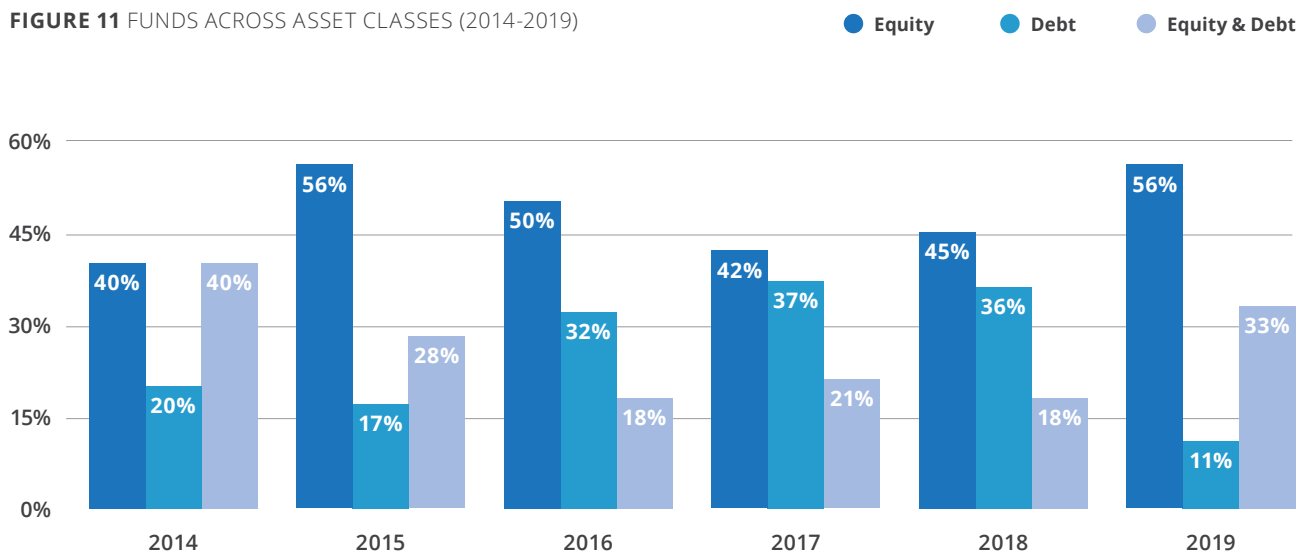
FIGURE 10 PROPORTION OF BLENDED FINANCE TRANSACTIONS BY INVESTMENT INSTRUMENTS DEPLOYED



Blended funds, facilities, and some companies deploy downstream financing to a set of direct beneficiaries, from entrepreneurs and small business owners to financial institutions. To date, blended finance vehicles have been most likely to provide debt. For example, debt was the primary instrument used by 50% of blended finance vehicles between 2017-2019, and accounts for the primary instrument for 41% of downstream transactions in the market overall. Debt has been used by all vehicle types, including funds (51%, including funds that deploy debt and equity), companies (33%; i.e., loans to direct beneficiaries),

and facilities (53%). Between 2017-19, equity has been another common instrument used by blended finance vehicles (33% of transactions). This is largely accounted for by funds (64%, including funds that deploy debt and equity), and to a lesser extent, companies (28% of which have invested equity in direct beneficiaries). There has been a moderate decrease in the downstream use of mezzanine and quasi-equity capital by blended vehicles in the past few years relative to all years; mezzanine and quasi-equity capital accounted for 9% of transactions, and 14% when looking at the market overall.

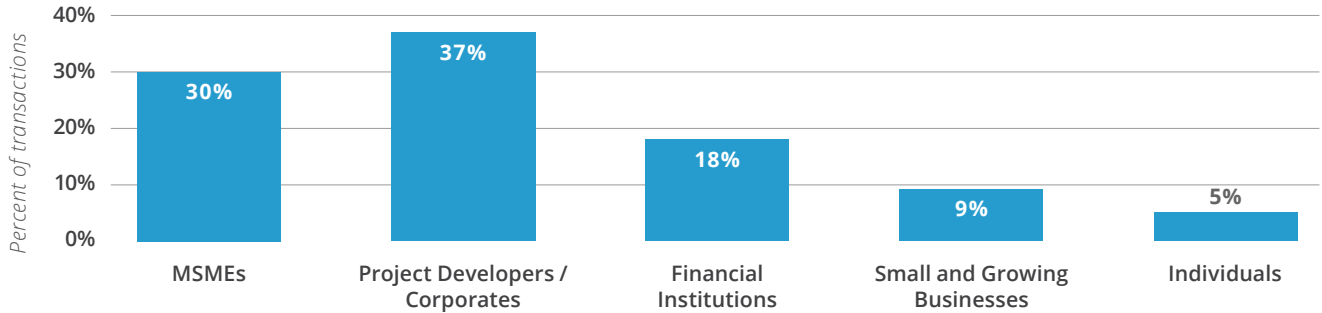
FIGURE 11 FUNDS ACROSS ASSET CLASSES (2014-2019)



In recent years, there has been an increase in the number of private equity funds in the market (defined here as funds deploying equity as their primary instrument), accounting for 48% of funds launched since 2014. Meanwhile, private debt funds account for 25% of the funds launched since 2014. In addition, 24% of funds since 2014 have pursued a combined

equity and debt strategy, including seed-stage, common, and quasi-equity, as well as short-term and medium to long-term debt, prevalence of funds with a combined equity and debt strategy, including seed-stage, common, and quasi-equity, as well as short-term and medium to long-term debt, accounting for an average of 24% of funds since 2014.

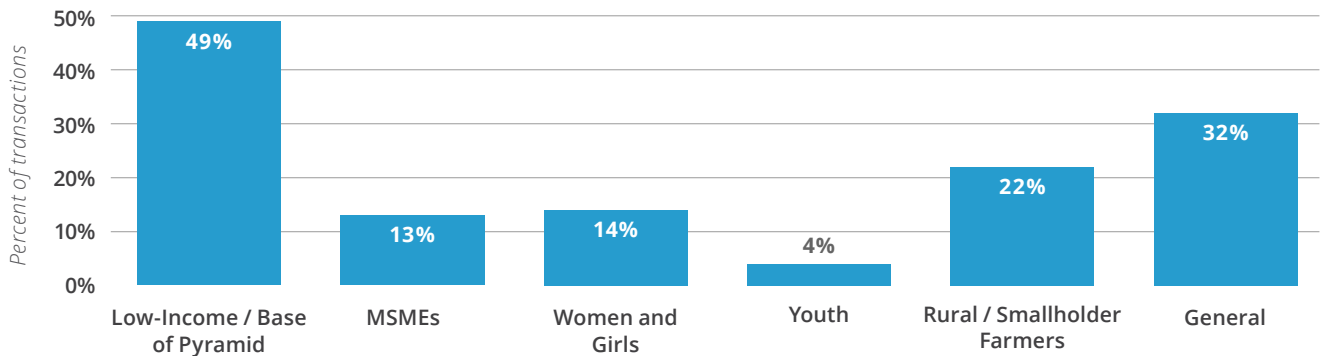
FIGURE 12 DIRECT BENEFICIARIES OF BLENDED FINANCE TRANSACTIONS (2014-2019)



The most commonly targeted direct beneficiary of blended finance vehicles over the past five years (2014-2019) has been companies, including micro, small, and medium-sized enterprises (MSMEs; 30%) and small and growing businesses (9%). These include companies across diverse sectors, including microfinance institutions, social enterprises, and farmer cooperatives. These findings are similar to results from the [OECD 2018 Survey on Development Performance](#), which found that the most frequent investees of blended funds and facilities are companies, the target beneficiary of 70% of blended funds and 61% of blended facilities. In contrast, only

a small proportion of blended finance transactions have directly targeted individuals (including for example, entrepreneurs or smallholder farmers). Project developers and large corporates have also represented a large share of direct beneficiaries in Convergence’s database – including those where the project itself absorbs the capital raised and those where the entity lends or invests the funds downstream – accounting for 37% of all direct beneficiaries of blended capital. This aligns with the number of blended finance transactions supporting one or more infrastructure projects (including energy projects) in developing countries.

FIGURE 13 END BENEFICIARIES OF BLENDED FINANCE TRANSACTIONS (2014-2019)

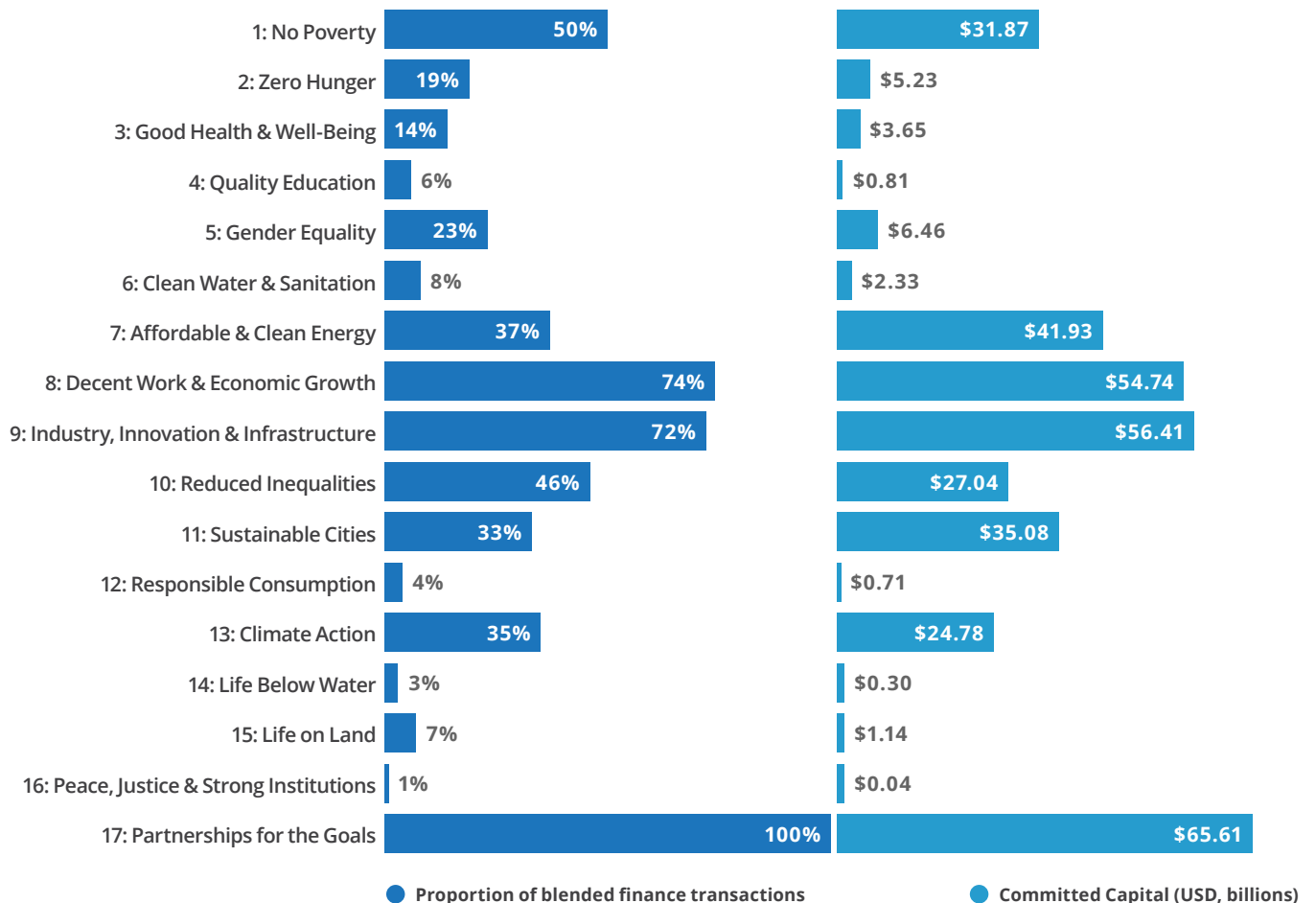


Blended finance transactions have most commonly targeted low-income and base of the pyramid (BoP) consumers (49% of end beneficiaries between 2014-2019) as their ultimate beneficiaries. Transactions focused on rural populations and smallholder farmers have also represented a sizeable portion of the market, accounting for 22% of target end recipients of blended deals.

MSMEs can also be the end beneficiary of blended finance transactions, most commonly through intermediaries such as financial institutions and mid-sized businesses (e.g., value chain finance). Between 2014 and 2019, 14% of blended finance transactions overtly identified women and girls as end beneficiaries.

Sustainable Development Goals and Impact Measurement

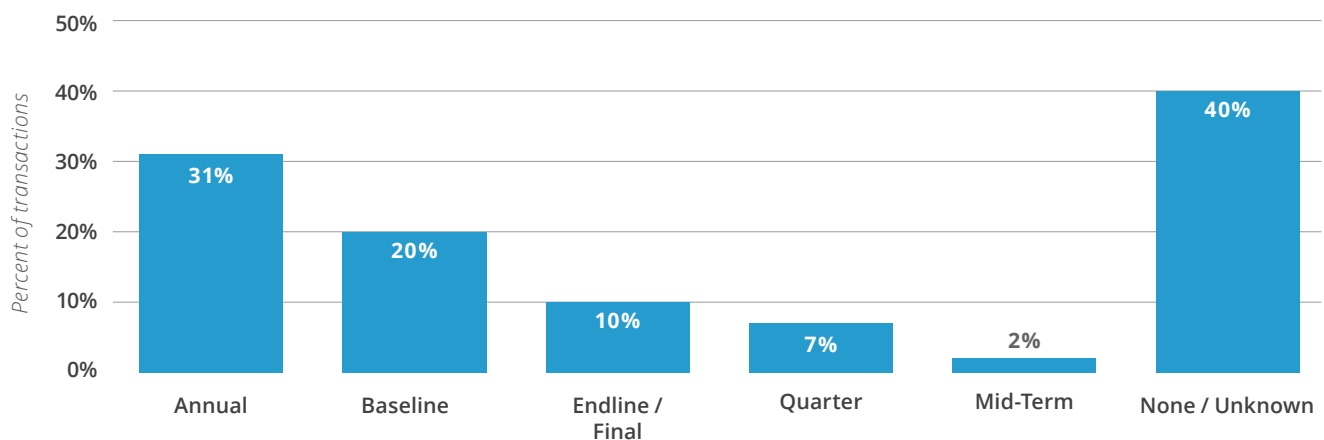
FIGURE 14 SDG ALIGNMENT AND AGGREGATE FINANCING IN BLENDED FINANCE TRANSACTIONS (2014-2019)



Blended finance mobilizes private investment to underlying activities with cash flows that can remunerate private investors. Accordingly, blended finance is a suitable approach for only a sub-set of SDGs. The alignment between blended finance and the SDGs, by number of blended finance transactions aligned to each SDG, is understandably strongest for Goal 17 (Partnerships for the Goals), specifically Targets 17.3 (additional financial resources) and 17.17 (effective partnerships). Beyond Partnerships for the Goals, blended finance transactions across all time periods have been most concentrated on Goals 9

(Industry, Innovation, & Infrastructure), 8 (Decent Work & Economic Growth), and 10 (Reduced Inequalities), and this trend has stayed consistent over time. This reflects sector trends as these SDGs map to financial services and infrastructure, where blended finance is most prominent. 50% of blended finance transactions launched between 2014-19 have addressed Goal 1 (No Poverty), including Targets 1.2 (reduce poverty), 1.4 (equal access), and 1.5 (build resilience). Blended finance has also been demonstrated to be a potential development tool for Goals 2 (Zero Hunger), 5 (Gender Equality), and 3 (Good Health & Well-Being).

FIGURE 15 IMPACT REPORTING IN BLENDED FINANCE TRANSACTIONS (2014-2019)



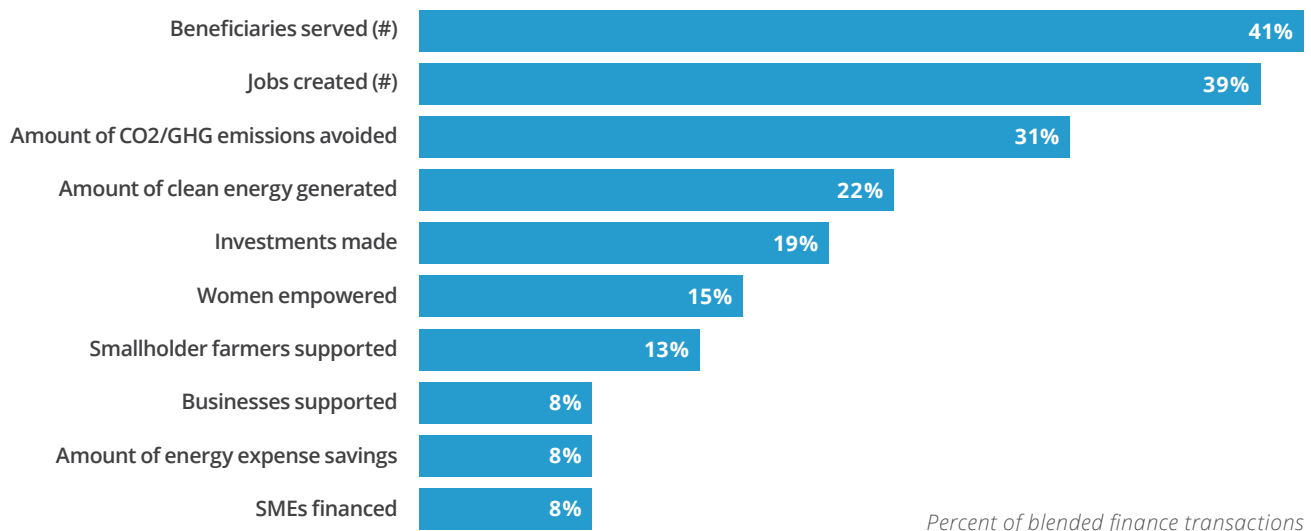
Using Convergence’s fundraising dataset as an indicative example, nearly 42% of transactions currently seeking blended capital are aligned with SDG 5, indicating increased attention toward gender equality and gender lens investing. Earlier analysis conducted by Convergence found that most of the transactions aligned to SDG 5 were “gender aware” (58%), suggesting that a gender lens has been incorporated into the transaction in some form. Meanwhile, 42% of these transactions are “gender-intentional,” with a comprehensive focus on gender and the empowerment of women or girls.

Of the latter transactions, there is an outsized focus on microfinance (25% of transactions), health (15% of transactions), and water, sanitation and hygiene (17% of transactions). We have also seen an emerging interest in health. Our historical data indicates that blended finance can be used to support specific streams of healthcare activities, including the development and roll-out of pharmaceuticals and vaccinations, as well as the delivery of health services, including through private clinics and SMEs.

Aggregate financing for each SDG between 2014-2019 has been greatest for Goals 9 (Industry, Innovation, & Infrastructure), 8 (Decent Work & Economic Growth), and 7 (Affordable & Clean Energy). Goals 13 (Climate Action) and 11 (Sustainable Cities) also account for a sizeable portion of aggregate financing from blended finance transactions. Indeed, climate finance, including climate finance transactions aligned with SDG 7, 13 and 11, represents over half of all

aggregate flows in the blended finance market. The smallest portion of aggregate financing historically has been earmarked for Goals 16 (Peace, Justice & Strong Institutions), 12 (Responsible Consumption), and 14 (Life Below Water). Nonetheless, it is important to note that there have been a limited number of smaller-scale solutions for these goals (e.g., Sustainable Ocean Fund, Media Development Investment Fund).

FIGURE 16 IMPACT METRICS PROVIDED BY BLENDED FINANCE TRANSACTIONS (2014-2019)



As donor governments, MDBs, and DFIs look more toward blended finance as a tool for development, they are calling for better impact measurement, reporting and standardization. While a lack of transparency in blended finance and development outcomes can make it more challenging for some policymakers and development practitioners to fully endorse the use of blended finance, the call for transparency reflects a broader and long-standing theme in the development community.

Development practitioners themselves have a significant role to play in terms of disseminating impact data and promoting transparency – these efforts are reflected in initiatives such as the International Aid Transparency Initiative (IATI). According to Convergence’s database, 40% of transactions have not, or do not intend to, publicly disclose impact reporting, although these transactions may report impact to stakeholders (see Figure 15). Meanwhile, 31% of transactions report on an annual basis, 20% report baseline

information, and 10% report final / end-line results (2014-19). These findings echo survey results from the OECD Funds and Facilities 2018 Survey on Development Performance, [which finds](#) that nearly 60% of funds and approximately 40% of facilities only share evaluation results with investors. Impact reporting has also differed across transactions at the portfolio level versus the project level, with data collected by Development Initiatives in their [report](#) “How Blended Finance Reaches the Poorest People,” finding that impact is more regularly captured at the portfolio level. One area that has seen some positive traction has been the prevalence of gender-disaggregated data. According to Convergence’s database, approximately one-third of all transactions (34%) have reported gender disaggregated data – this suggests that the majority of transactions that report impact data also disaggregate findings by gender. Collecting gender-disaggregated data is an important first step in developing evidence-based approaches for equitable development and assessing the impact of the blended finance market on women and girls.

“Total beneficiaries served” and “number of jobs created” are the most common metrics used to measure impact across all blended finance transactions, irrespective of focus sector or SDG alignment (See Figure 16). Climate-related metrics, particularly “volume of CO2/GHG emissions avoided,” are also widely used, even among blended finance transactions that do not focus on climate change. These basic sector-agnostic metrics are measurable (i.e., straightforward to collect) and comparable (i.e., standard across multiple projects); however, most metrics used in blended finance transactions are specific to the development activities financed. Metrics vary significantly between sectors, but also within sectors according to those specific activities. Sector-specific metrics are critical to ensure context and nuance are captured, allowing impact results to be compared in a meaningful way.

In 2019, the Global Impact Investing Network (GIIN) launched its [Evaluating Impact Performance](#) series, rigorously comparing impact results of investments within specific sectors (including [Clean Energy](#) and [Housing](#)). They found impact performance varied based on the impact objectives, target stakeholders, geography, product or service, and investment features of the investment.

From the donor community, we have seen growing demand for, as well as greater willingness to provide, increased transparency and impact, especially through efforts led by the OECD. The OECD is currently preparing its Development Assistance Committee (DAC) Blended Finance Principles Guidance Notes, which provide practical guidance on implementing the OECD DAC Blended Finance Principles. In addition, the OECD is leading efforts to support greater transparency and impact measurement in blended finance through the Tri Hita Karana (THK) Roadmap on Blended Finance. The THK seeks to foster a common language and collective action to deliver financing to support the SDGs, and is composed of five actions areas, including promoting transparency and impact. While Convergence captures impact ex-ante, more data is needed on specific results and who benefits ex-post. This data will need to be provided by the participants of those transactions.



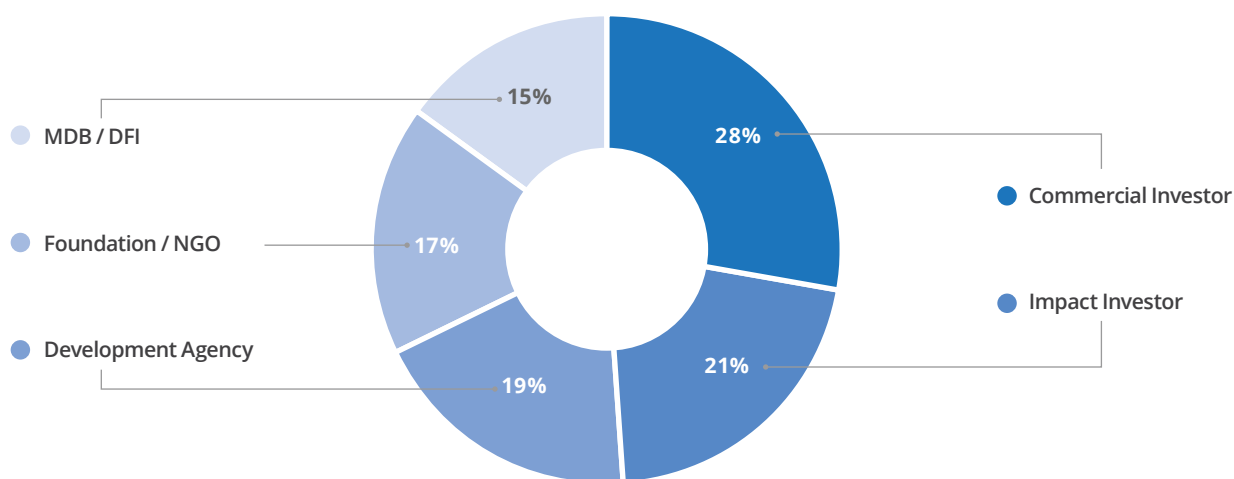
Investor Trends

Overall Landscape

According to Convergence’s database, over 1,274 unique organizations across the public, private, and philanthropic sectors have made financial commitments⁹ to one or more blended finance transaction(s). Over 255 or 20% of these organizations are ‘active investors’ that have invested in three or more blended transactions. Half (49%) of the active investors are in the private sector, subdivided into: (i) private investors with traditional commercial mandates (i.e., commercial

investors), and (ii) private investors with additional impact mandates (i.e., impact investors). The public sector accounts for a third (34%) of active investors, subdivided into: (i) organizations with pure development mandates (i.e., development agencies) and (ii) organizations with commercial development mandates (i.e., most MDBs and DFIs). Philanthropic organizations (i.e., foundations and NGOs) constitute 17% of active organizations.

FIGURE 17 ACTIVE INVESTORS IN BLENDED FINANCE BY ORGANIZATION TYPE, ALL YEARS



Comparing the most recent 901 financial commitments made to 160 blended finance transactions in 2017-19 with all transactions recorded in the Convergence database, Figure 18 shows that MDBs and DFIs are consistently the most prominent organization type, accounting for 35% of financial commitments in recent transactions compared to 32% across all years.

Commercial investors account for over a quarter (27%) of financial commitments to blended finance transactions in 2017-19. Impact investors and foundations continue to play a relatively small but important role in the flow of blended finance transactions, accounting for 8% and 10% of financial commitments in recent years, respectively.

⁹ Convergence uses the term financial commitment to refer to any concessional or non-concessional capital provided to a blended finance transaction, including, but not limited to, through grants, debt, equity, and guarantees.

FIGURE 18 SOURCES OF FINANCIAL COMMITMENTS TO BLENDED FINANCE TRANSACTIONS

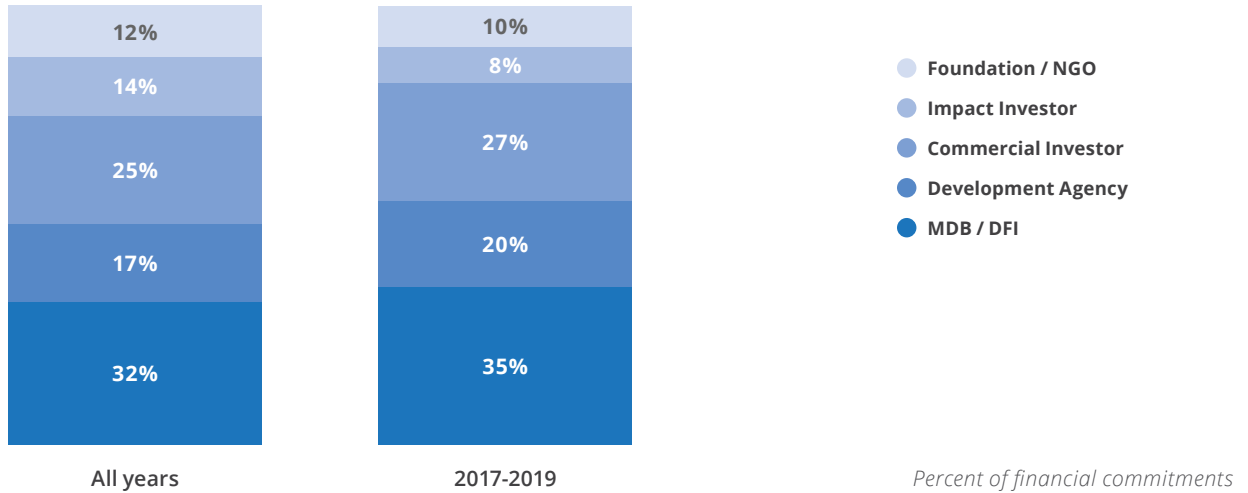
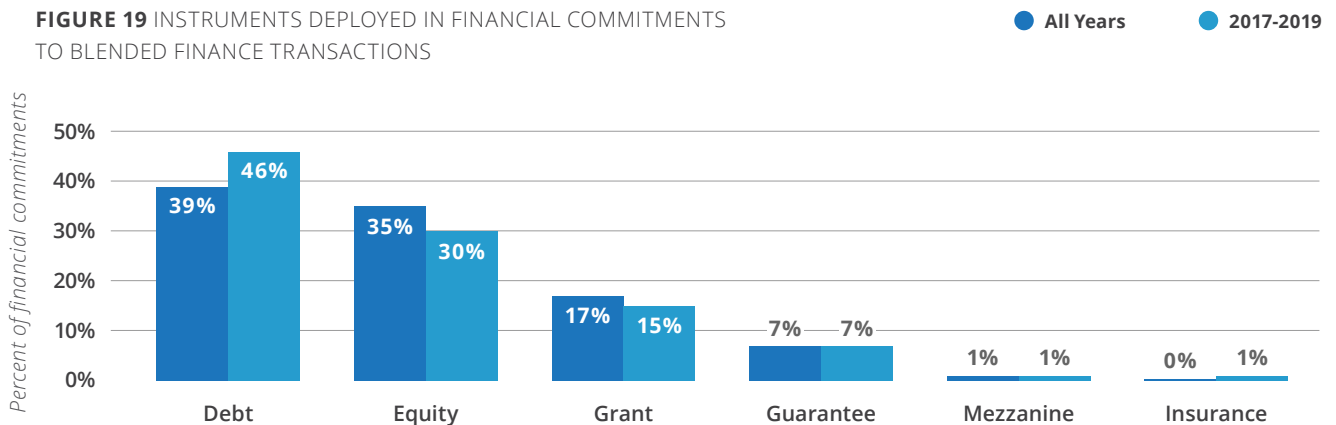


Figure 19 illustrates the shifting profile of instruments deployed in financial commitments to blended finance transactions over time. There has been an uptick in the deployment of debt in financial commitments to blended finance transactions, accounting for 46% of commitments in 2017-19, compared to 39% across all years; concurrently, there has been a slight dip in the deployment of equity, from 35% across all years to 30% for 2017-19. With further analysis, Convergence found that the number of investors (i.e, number of organizations) making debt commitments to blended transactions

has been steadily increasing (195 in 2017-19, compared to 163 in 2014-16 and 149 in 2011-13), as has the number of debt commitments made overall (391 between 2017-19, compared to 331 during 2014-16 and 263 from 2011-13). Meanwhile, the number of investors making equity commitments to blended transactions has not been on a linear trajectory (137 during 2017-19, compared to 200 between 2014-16 and 134 from 2011-13), and neither has the number of equity commitments being made (256 in 2017-19, compared to 337 in 2014-16 and 215 in 2011-13).

FIGURE 19 INSTRUMENTS DEPLOYED IN FINANCIAL COMMITMENTS TO BLENDED FINANCE TRANSACTIONS

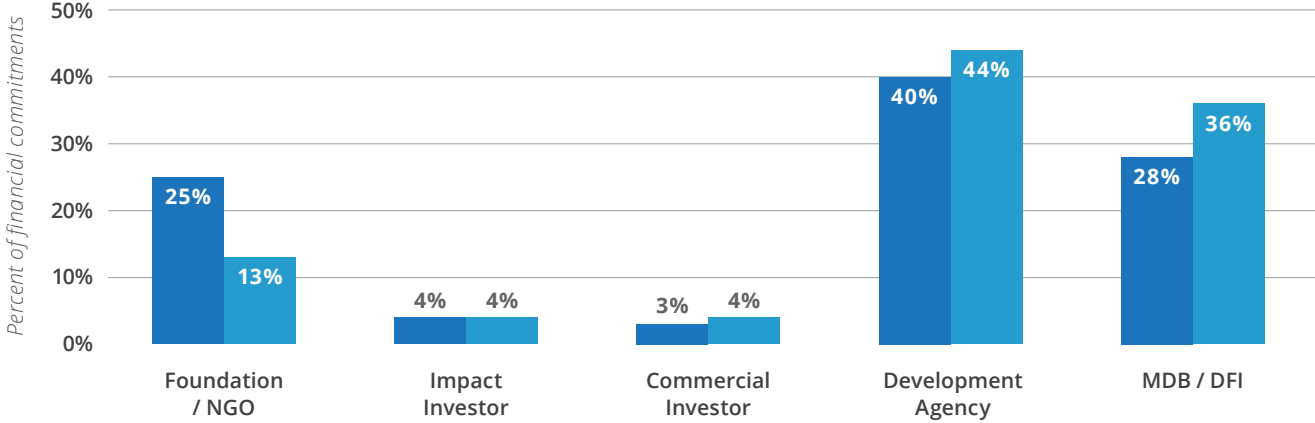


Historically, MDBs / DFIs and commercial investors have made the most debt commitments to blended finance transactions, accounting for 37% and 34% of debt commitments to blended transactions across all years, respectively. Meanwhile, the data in figures 18 and 20 suggests that in addition to participating in more blended transactions, MDBs / DFIs are also increasingly recognizing concessional capital as a crucial tool of deployment. As Figure 20 shows, MDBs / DFIs have been major providers of concessional financing in their financial commitments

to blended finance transactions, both historically and in recent years: they account for 28% of all concessional financing across all years, which rises to 36% when considering the years 2017-19. However, development agencies have been the largest providers of concessional financing to date, accounting for 40% of all such financing, and 44% of all concessional financing in 2017-19. Figure 20 also illustrates that foundations / NGOs represent a smaller proportion of overall concessional commitments to blended transactions.

FIGURE 20 SOURCES OF CONCESSIONAL FINANCING IN FINANCIAL COMMITMENTS TO BLENDED FINANCE TRANSACTIONS

● All Years ● 2017-2019



Looking ahead, while development agencies and MDBs / DFIs have been the most frequent providers of concessional capital in blended transactions, they can do more to mobilize private capital at scale, from right-sizing levels of first-loss protection, to providing greater volumes of credit enhancement also targeting domestic investors, to

providing greater support for project preparation. To be truly catalytic, concessional capital providers must shape concessional structures to the expressed needs and preferences of those whose capital they seek to mobilize.

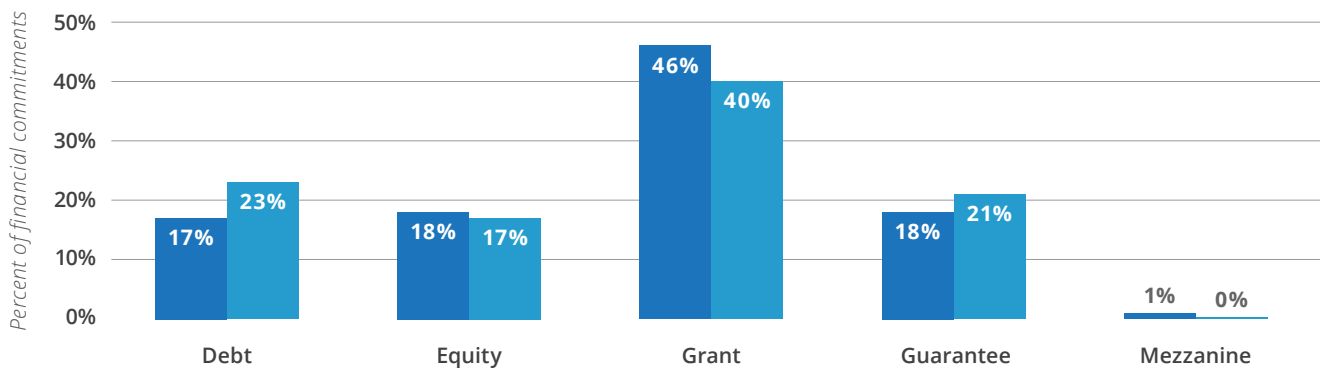
Development Agencies and Multi-Donor Funds

Although donor governments allocate only a small fraction of their international development funding to blended finance (e.g., less than 3% of their ~\$150 billion allocated annually to ODA), development agencies (directly and through multi-donor funds) have been major providers of grants; development agencies are the source of half of all grants made to blended finance transactions in general. Moreover,

almost half (46%) of the financial commitments made by development agencies are grants. Meanwhile, development agencies account for only 9% and 10% of the debt and equity commitments made to blended finance transactions to date, respectively. They have typically been involved in larger transactions, with a median transaction size of \$110 million.

FIGURE 21 INSTRUMENTS DEPLOYED BY DEVELOPMENT AGENCIES AND MULTI-DONOR FUNDS TO BLENDED FINANCE TRANSACTIONS

● All Years ● 2017-2019



Over the past five years, the most prominent development agencies and multi-donor funds have been USAID (29 commitments), GuarantCo (29), the World Bank (24), the Green Climate Fund (22), and the Dutch Good Growth Fund (17). There are key differences regarding the instruments deployed in blended transactions between the major development agencies and multi-donor funds; for example, GuarantCo exclusively deploys guarantees, whereas USAID provides grants as well as debt and equity, in line with their blended finance INVEST Initiative. For example, in June 2019, USAID INVEST structured the

first contract-based, first-loss tranche transaction in the history of the agency, committing \$500,000 in first-loss capital to Women’s World Banking Capital Partners Fund II, alongside \$100,000 in technical assistance. Meanwhile, in October 2019, GuarantCo provided a KES 2.5 billion partial credit guarantee to investors subscribed to the Acorn Holdings bond program.

Looking at recent activity amongst development agencies and multi-donor funds more broadly, the Green Outcomes Fund was launched in January 2020

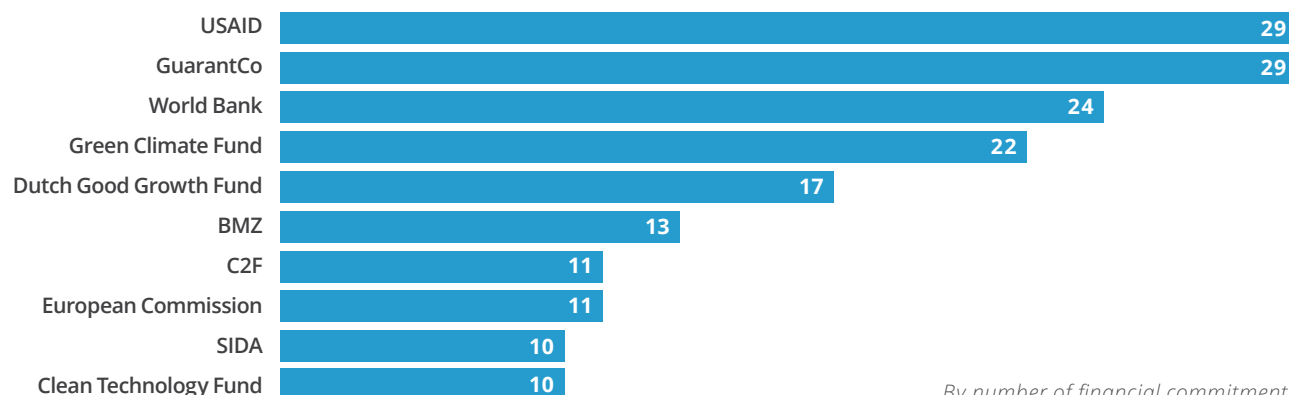
to incentivize local South African fund managers to increase their investment in green SMEs by offering outcome-based matched concessional funding. The Green Outcomes Fund, launched by the South Africa National Treasury's Jobs Fund and the impact investor GreenCape, received catalytic grant support from the RMB Fund, a division of the FirstRand Foundation. Elsewhere, the Dutch Ministry for Foreign Affairs also announced plans to become an anchor public investor in the sustainable agriculture and forestry initiative AGR13 Fund by contributing \$40 million, an amount matched by Rabobank. The fund, which looks to unlock at least \$1 billion in commercial finance, will provide de-risking instruments for banks, enabling them to provide clients with loans on sustainable and deforestation-free transactions that would otherwise be too risky due to a longer tenor. It will also provide grants for technical assistance to food value chain actors and farmers.

Development agencies and multi-donor funds are increasingly moving beyond their strict grant-focused roles. The Global Environment Facility's latest funding round (GEF-7) boosted its Non-Grant Instrument Program, which deploys instruments like debt, guarantees and equity and looks to catalyze private investment; its envelope for blended finance expanded to \$136 million. Also, the Millennium Challenge Corporation (MCC) is looking to develop

a new \$30 million Lesotho Impact Investment Fund, alongside a Technical Assistance Fund, to promote business development and private investment in Lesotho. Another example of development agencies' recent non-grant activity is provided by USAID, which provided a \$2.5 million 'design funding' award through their Women's Global Development and Prosperity (W-GDP) initiative to US-based non-profit Kiva, to develop the Kiva Invest in Women Fund (K-IWF). Elsewhere, the Australian Government, through its Frontier Brokers Program, is supporting Brightlight Consortium in the design of the Asia Pacific Notes Series, the world's first fixed income securities to aggregate bespoke loans to social enterprises from across the Asia Pacific region. Also, in late 2019, USAID awarded Palladium its \$250 million CATALYZE contract – a project that looks to mobilize \$2 billion in blended finance for developing countries through to 2027.

Finally, efforts to boost collaboration amongst development agencies on scale blended finance solutions were accelerated by the launch of the DFID-led Scale Blended Finance Working Group in 2019. Jointly established by DFID and Convergence, the Working Group aims to coordinate the deployment of concessional capital from donor governments and development agencies into blended finance transactions that can achieve scale, development impact and private investment mobilization.

FIGURE 22 TOP DEVELOPMENT AGENCIES AND MULTI-DONOR FUNDS IN BLENDED FINANCE (2014-2019)



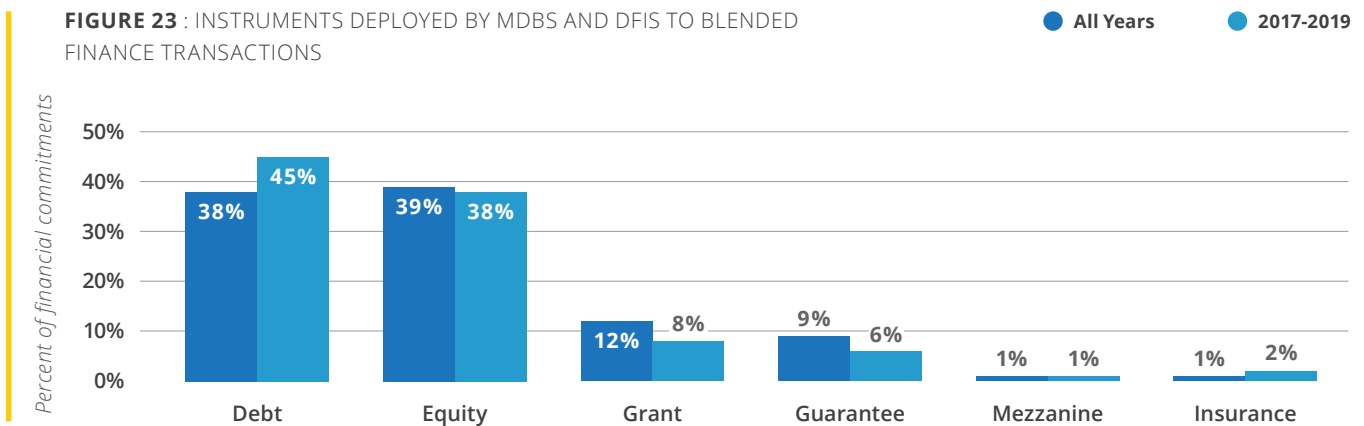
By number of financial commitments

Multilateral Development Banks and Development Finance Institutions

By the number of financial commitments to blended finance transactions, MDBs and DFIs continue to be the most prominent investors in blended finance. They have been the major providers of equity (41% of total equity deployed), and debt (37% of total debt deployed) in blended finance transactions,

and to a lesser extent have also invested through guarantees and deploying donors' grants. They have typically invested in the largest blended finance transactions of all the investor groups, with a median transaction size of \$135 million across all years, and \$140 million from 2017-19.

FIGURE 23 : INSTRUMENTS DEPLOYED BY MDBS AND DFIS TO BLENDED FINANCE TRANSACTIONS



Over the past five years, the most prominent MDBs and DFIs have been IFC (92 commitments), FMO (74), the European Investment Bank (38), the African Development Bank (29), and PROPARCO (27), with MDBs and DFIs engaging in a range of blended finance activities. According to the DFI Working Group on Blended Concessional Finance for Private Sector Projects' October 2019 update of their [joint report](#), DFIs financed blended projects with a total volume of over \$6 billion in 2018, using approximately \$1.1 billion in concessional funds and \$2.4 billion in DFI account resources, mobilizing private sector finance of \$1.7 billion. More recently,

the MDB / DFI community has been highly active in structuring responses to the COVID-19 pandemic, committing billions of dollars to support companies and fight the economic impact of the crisis. For example, the African Development Bank raised \$3 billion by issuing a [three-year Fight COVID-19 social bond](#), the largest dollar-denominated social bond launched in the international capital markets to date, and the largest US dollar benchmark issued by the bank. However, [questions remain](#) over whether the conservative business models and existing resources of the DFIs can meet the scale of the challenges resulting from the COVID-19 pandemic.

Looking beyond the pandemic, in February 2020, IFC and the Dutch government launched the MENA Private Sector Development (PSD) Initiative, a multi-sector programme that looks to support the private sector and job creation in the MENA region by using concessional capital to catalyze investment in potentially high-impact projects. Also, the Dutch government, alongside a consortium consisting of the Dutch Development Finance Company (FMO), Climate Fund Managers, SNV, and WWF-Netherlands, launched the EUR 160 million Dutch Fund for Climate and Development in November 2019, which looks to mobilize over EUR 500 million from private investors for investment in climate adaptation and mitigation.

Encouragingly, some MDBs and DFIs have reoriented their internal strategies to focus more explicitly on development impact in addition to financial returns.

“Our new strategy puts in place ambitious targets for ADB’s private sector financing, and focuses strongly on development impacts, targeting poverty reduction, climate change, gender equality, rural development and food security, urban development, governance and institutional capacity, and regional cooperation and integration. In addition to monitoring total financing amounts, by paying close attention to the number of deals we sign, especially in challenging geographies (including fragile and conflict-affected states and small island developing states), we zero-in on the development impacts offered by smaller transactions. With mobilization or co-financing targets, we are often incentivized to reduce the ADB portion of financing in a transaction and to bring in as many other players as we can, like other banks, and leverage commercial financing.”

DAVID BARTON, SENIOR INVESTMENT SPECIALIST,
ASIAN DEVELOPMENT BANK (ADB)

Meanwhile, there have also been signs that DFIs are increasingly looking to cooperate in transactions to further development impact.

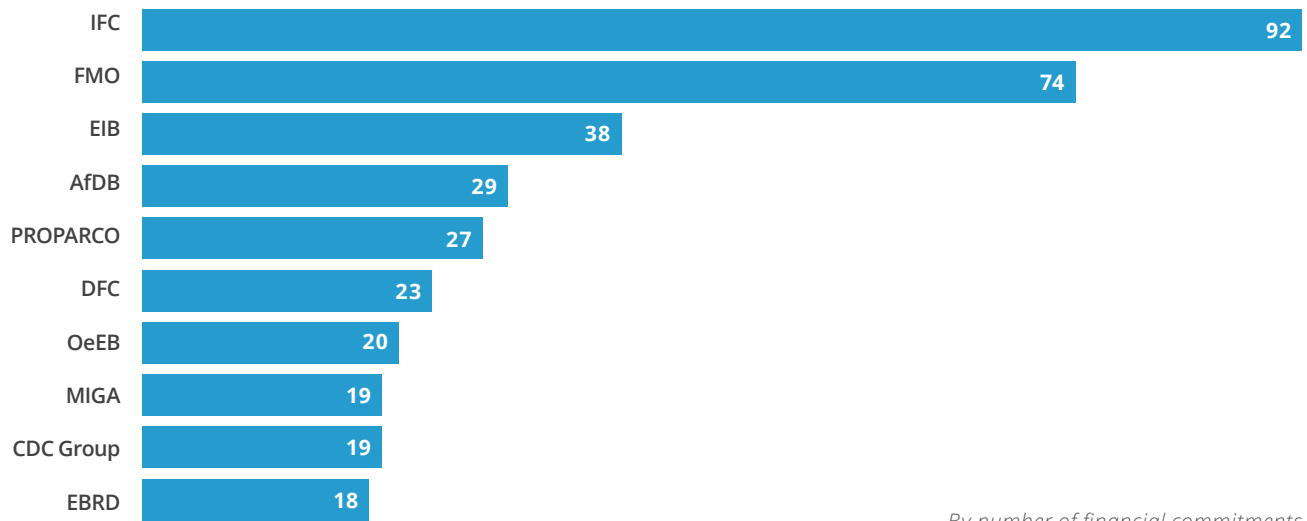
“We are increasingly trying to work with other development institutions in sharing risk. We are looking at seeing what the smallest proportion is that we can take in a transaction while still ensuring that the transaction takes place. It helps us to minimize individual project risk in doing so, while still being able to demonstrate development impact. It is a measure of the catalyzation or multiple effect of our money versus the capex that we are managing to unlock for sectors like sustainable infrastructure.”

MOHAN VIVEKANANDAN, GROUP EXECUTIVE,
ORIGINATION AND COVERAGE, DEVELOPMENT BANK
OF SOUTHERN AFRICA (DBSA)

Finally, the United States’ DFI – the Overseas Private Investment Corporation (OPIC) – became a new agency called the US International Development Finance Corporation (DFC) in January 2020. Strategic changes providing the new agency with a stronger development mandate include: i) doubling the maximum size of its portfolio, from \$29 billion to \$60 billion; (ii) its authorization to make equity investments; (iii) the abolition of US eligibility requirements for the beneficiaries of guarantees and political risk insurance; and (iv) the transfer from USAID to DFC of the Development Credit Authority, which uses partial credit guarantees to mobilize local currency financing in developing markets. Having approved over \$3.6 billion worth of investments in Q3 2020, more than 60% of which are in low- and lower middle-income countries, DFC has now begun to take equity stakes in development projects, such as the women-focused e-commerce

start-up Kasha, operating in Kenya and Uganda, and the Kenya-based e-commerce and logistics start-up Copia Global. Looking ahead, we expect DFC to use its new investment authorities to deliver a strong flow of blended finance transactions, given DFC/OPIC's status as one of the top DFIs active in blended finance by number of commitments.

FIGURE 24 TOP MDBS AND DFIS IN BLENDED FINANCE (2014-2019)



By number of financial commitments



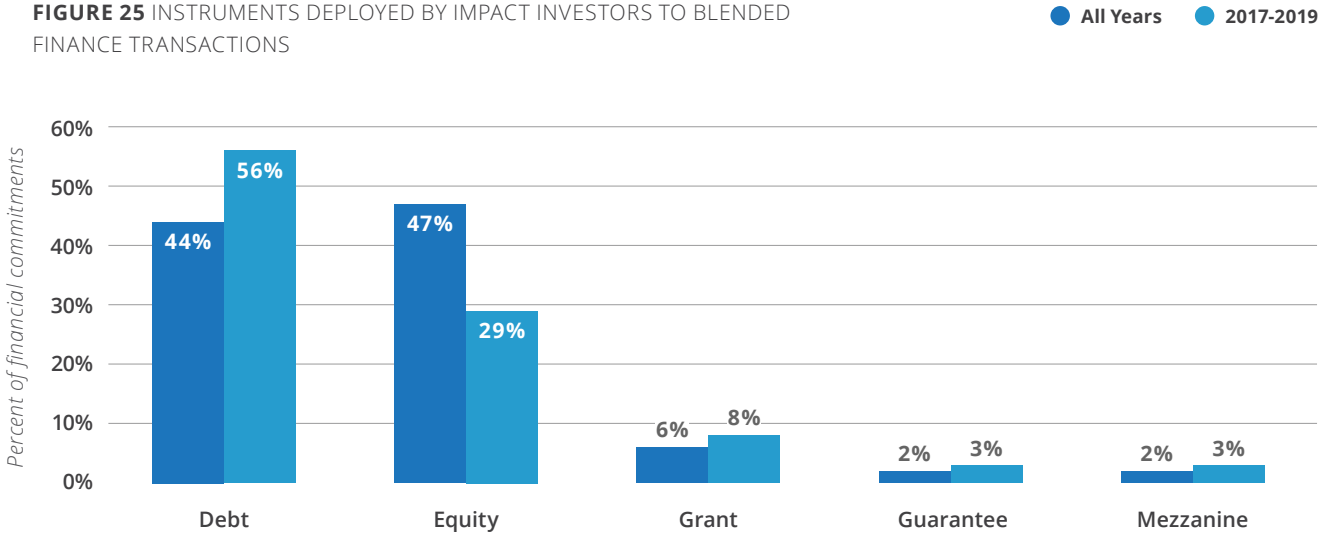
Impact Investors

Impact investors appear in a small minority of commitments to blended finance transactions. Their commitments to blended transactions have fallen in absolute terms over time (from 137 in 2011-13 to 70 in 2017-19), and they account for a falling proportion of total commitments. Impact investors accounted for 8% of financial commitments to blended finance in 2017-19, most of which was deployed through debt (56% of their commitments compared to 44% across all years). Meanwhile, their use of equity in their commitments fell from 47% across all years, to 29% in 2017-19. Inspecting the data more closely, Convergence found that (i) only 14 impact investors deployed equity in their commitments to blended transactions in 2017-19, down from 35 in 2014-16 and 28 in 2011-13; (ii) 17 equity commitments were made by impact investors in 2017-19, down from 44 in 2014-16 and 32 in 2011-13; (iii) 22 impact investors deployed debt in 2017-19, compared to 23 in 2014-16 and 23 in 2011-13; and (iv) 33 debt

commitments were made by impact investors in 2017-19, compared to 35 in 2014-16 and 30 in 2011-13. In sum, the number of debt commitments and the number of impact investors making debt commitments have been stable; however, both the number of equity commitments and the number of impact investors making equity commitments have fallen. This may reflect a movement amongst impact investors towards seniority in transactions and a reduction in their willingness to assume risk.

Impact investors represent over a fifth (21%) of active investors in blended finance (investing in three or more transactions) across all years, behind only commercial investors (28%), but their share falls to 12% when considering active investors in blended finance between 2014 and 2019. They have typically invested in smaller blended finance transactions (with a median transaction size of \$50 million across all years).

FIGURE 25 INSTRUMENTS DEPLOYED BY IMPACT INVESTORS TO BLENDED FINANCE TRANSACTIONS

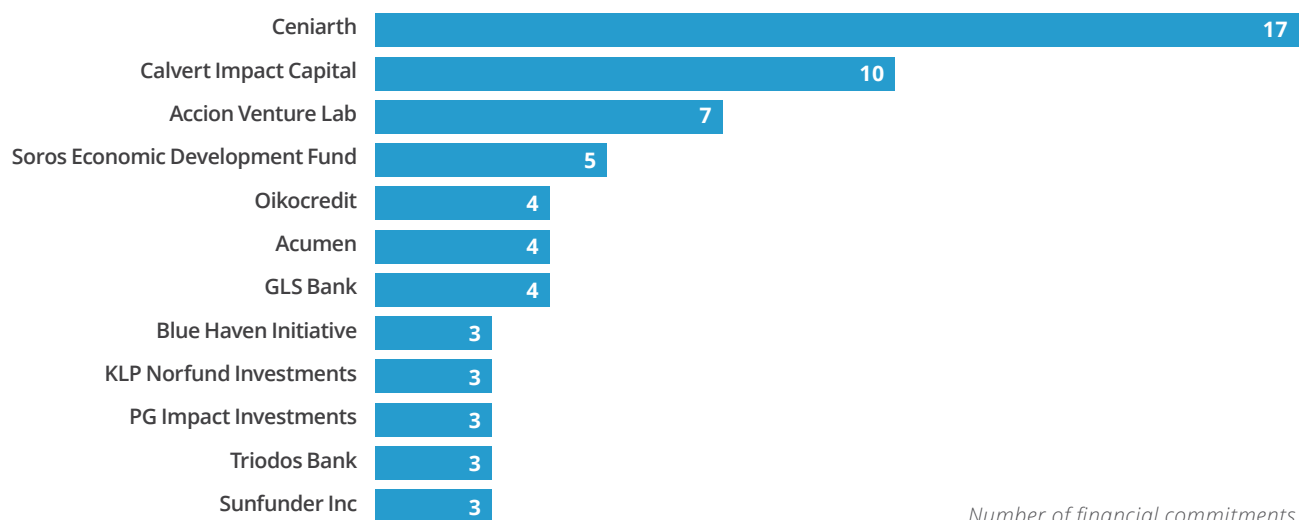


Over the past five years, the most prominent impact investors in blended finance transactions have been Ceniarth (17 commitments), Calvert Impact Capital (10), Accion Venture Lab (7), Soros Economic Development Fund (5), Oikocredit (4), Acumen (4), and GLS Bank (4). Significant new transactions include the launch of SDG500, an impact investment vehicle comprised of six funds looking to support the achievement of the SDGs, by the UN Capital Development Fund, alongside a consortium of partners.

Meanwhile, Swiss asset manager, responsAbility Investments, launched a \$3 million technical assistance facility (backed by Good Energies Foundation and Swiss SECO), tied to its blended climate finance private debt fund. The fund, which achieved a first close in January 2020, looks to improve access to clean power in developing countries. Mirova's Althelia Sustainable Ocean Fund, which looks to invest in marine and coastal projects supporting coastal ecosystems and the blue economy, announced a final close of \$132 million in August 2020, exceeding its \$100 million target size. The fund is supported by a risk-sharing guarantee provided by USAID/DFC's Development Credit Authority.

Impact investors are also leveraging new instruments to drive development impact, such as the RS Group, who partnered with Convergence to launch a \$3 million design funding window for catalytic blended finance solutions focused on natural capital in Asia. Elsewhere, building on the success of its first two impact investment funds, US-based asset manager WaterEquity launched its \$150 million Global Access Fund in November 2019, providing debt capital to financial institutions in emerging markets to enable them to scale their water and sanitation microfinance portfolios. Finally, impact investors have also sought to coordinate their responses to the COVID-19 pandemic. For example, the Response, Recovery, and Resilience Investment Coalition (R3 Coalition), launched in May 2020 and managed by the GIIN, aims to streamline and accelerate impact investing efforts addressing the social and economic consequences of the COVID-19 pandemic, connecting likeminded impact investors with each other and with the information and investment opportunities that can direct their responses to the crisis.

FIGURE 26 TOP IMPACT INVESTORS IN BLENDED FINANCE (2014-2019)



Number of financial commitments

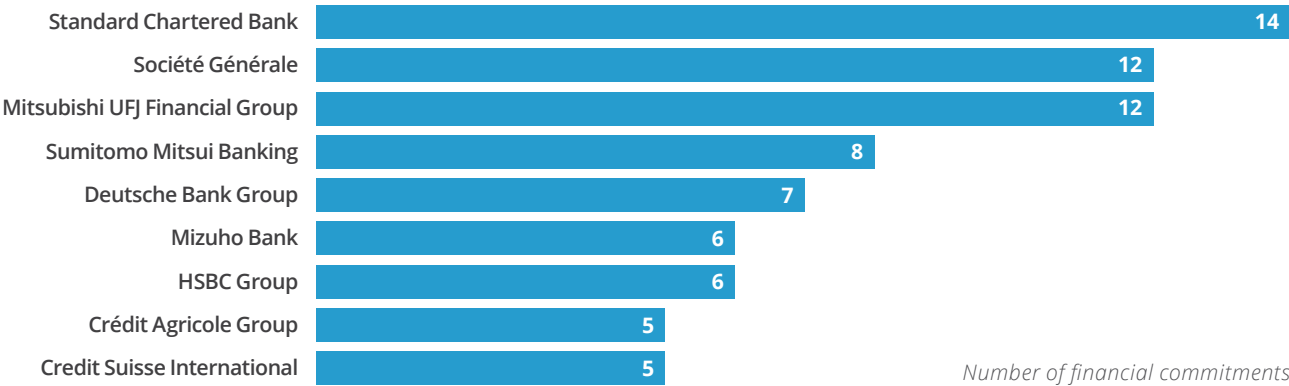
Commercial Investors

The mobilization of commercial investors is central to the purpose of blended finance. When evaluating this group’s activity overall, commercial investors account for the biggest proportion of active investors across all years (28%), deploying approximately a third (34%) and a quarter (25%) of all debt and equity committed to blended finance transactions, respectively. Commercial investors have also often been involved in larger transactions (\$105 million median transaction size across all years). The most prominent commercial investors in blended finance over the past five years have been Standard Chartered (14 commitments), Société Générale (12), Mitsubishi UFJ Financial Group (12), Sumitomo Mitsui

Banking Corporation (8), and Deutsche Bank Group (7). Standard Chartered has been the top commercial investor in blended finance transactions due to its portfolio of infrastructure project loans.

For example, in October 2019, it committed \$50 million in a dual-currency corporate term loan to the Pakistani power-utility company K-Electric, supported by a partial guarantee from GuarantCo. Elsewhere, Dutch multinational cooperative bank Rabobank became the first senior debt investor in the Good Fashion Fund, which looks to finance supply chain innovations in Asia to drive environmental and social impact.

FIGURE 27 TOP COMMERCIAL INVESTORS IN BLENDED FINANCE (2014-2019)



Number of financial commitments

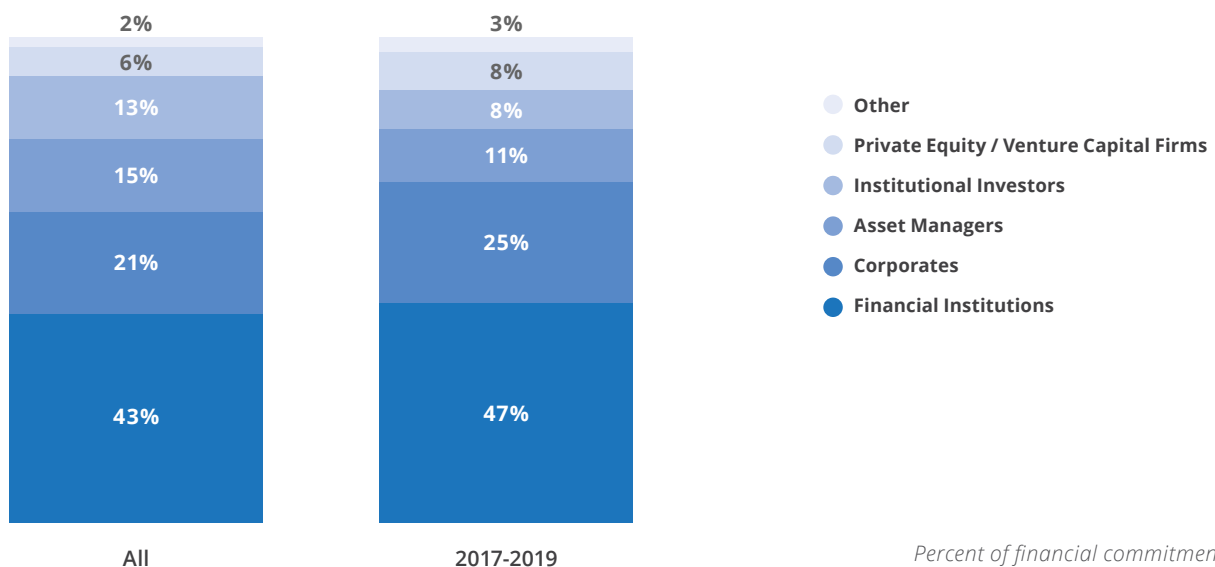
Looking more broadly at private finance, there have been recent efforts to draw commercial investors more fully into SDG-related investing, such as the launch of the Global Investors for Sustainable Development (GISD) Alliance in October 2019 by the UN Secretary General. The GISD will leverage the insights of the private sector (i.e., from major global banks such as Standard Chartered and UBS Group) to identify policy, institutional, market, and other

impediments to financing sustainable development, and viable solutions, over a two-year period. Indeed, one of the GISD’s recommendations detailed in a July 2020 report was the creation of a blended finance fund for the SDGs, modelled after IFCs Managed Co-Lending Portfolio Program (MCP), to scale blended finance and mobilize private capital by making ‘unbankable’ projects investable through donor and concessional capital, and aggregating them to reach

scale. Also, Liquidnet, a tech-driven institutional investor network, launched the B2T (Billions to Trillions) community in Q2 2020, in partnership with the philanthropic initiative Schmidt Futures. This collaborative effort looks to overcome the lack of intermediaries connecting different actors in blended finance by forming a virtual community in

which deal originators, institutional investors, and catalytic capital providers can connect. B2T looks to structure impact-agnostic commercial capital and impact-driven concessional capital into replicable institutional-caliber blended finance investment products that solve the climate emergency and other critical development goals.

FIGURE 28 FINANCIAL COMMITMENTS FROM COMMERCIAL INVESTORS TO BLENDED FINANCE TRANSACTIONS, BY ORGANIZATION TYPE



As Figure 28 shows, financial institutions (i.e., commercial banks) and corporates (i.e., multinational companies) have consistently been the major participants in blended finance transactions amongst commercial investors. Financial institutions and corporates both account for larger proportions of commercial participation in blended transactions when compared with all years (47% vs 43% for financial institutions; 25% vs 21% for corporates).

In a [joint paper](#) published in April 2020 by Convergence and UK DFID entitled “How to Mobilize Private Investment at Scale in Blended Finance,” we attribute the strong capacity of commercial banks to participate in blended transactions as arrangers and distributors to their ability to leverage expertise

from different divisions (e.g., debt capital markets, asset management, research) and broader global networks and subsidiaries. For example, financial institutions with established networks in developing countries are more familiar with the processes for underwriting and sourcing opportunities in those contexts and are therefore better positioned than their counterparts whose networks remain in developed markets. A recent example of a commercial bank’s increasing involvement in development finance is the [\\$100 billion DFI launched by JP Morgan Chase](#) in January 2020, to expand its development-oriented financing activities in emerging markets and galvanize private capital towards the SDGs.

However, the picture changes when other groups are considered: asset managers only accounted for 11% of commercial participation in blended transactions in 2017-19, down from 15% across all years. A similar downward trend is visible amongst institutional investors: 8% in 2017-19, down from 13% across all years. Commercial investors face common constraints when investing in projects in developing markets (e.g., high perceived risk for low expected returns, small investment sizes, and insufficient liquidity), but looking at asset managers in particular, their ability to participate in blended transactions is complicated by the regulations that apply to their clients (e.g., pension funds and insurance companies). They also may lack the expertise and resources to navigate blended transactions. Similarly, turning to institutional investors, insurance companies face significant regulatory constraints like capital charges for risky assets or assets with longer tenors, requirements for investment grade risk ratings, and liquidity requirements. Despite this, we have seen insurance

companies like Allianz and AXA participate in blended finance transactions, with Allianz, for example, investing \$120 million in the Emerging Africa Infrastructure Fund in 2018. Meanwhile, pension funds face diverse constraints when participating in blended transactions, including restrictions in certain asset classes and geographies, and the requirement of them being able to show that assets can be sold in the event of a market downturn. Nevertheless, pension funds like PensionDanmark and Christian Super have been able to make investments in blended finance transactions.

Finally, we continue to see a low uptake of local investors in blended finance, with no institutional investors domiciled in Sub-Saharan Africa or Latin America amongst the top 10 commercial investors in blended transactions (three Asia-domiciled banks do appear amongst the top 10, however). The Q&A with Todd Micklethwaite, Head of Strategy & Impact (Alternatives) at Sanlam Investments, presents some more detail on key factors at play in South Africa.

VOICES FROM THE FIELD:

Mobilizing Local Institutional Investor Capital in Blended Finance

Interview with Todd Micklethwaite, Head of Strategy & Impact (Alternatives), Sanlam Investments

Q: *How can blended finance better attract local institutional investors?*

A: In our markets, for a long period of time, institutional investors have largely achieved what they needed from listed markets in terms of delivering on their fiduciary responsibilities to members and beneficiaries. There has not really been a massive need to venture into private

markets, and the impact investing movement has not yet become mainstream. Pension funds have therefore typically not previously felt the need to start engaging in the complexities and practicalities of investing in private markets. With listed markets having come under pressure over the past few years, and with a growing need to support the development of our economy, private markets are increasingly on the agendas of trustee meetings.

In South Africa, industry bodies have set up asset owner forums to galvanize investment into these asset classes, and this is starting to gain some momentum. There has also been a concerted drive on the part of the South African government to bring institutional investors along at an early stage as they develop their long-term infrastructure program. As part of this strategy, the government awarded a mandate to the Development Bank of Southern Africa (DBSA), who are looking to set the Infrastructure Fund up as a blended finance structure. Structures that de-risk the investment without compromising on the likely return outcomes will certainly play their part in bringing in institutional investors that typically have not ventured into alternative asset classes before.

Q: *Are there any more systemic factors at play here?*

A: Traditionally, pension fund allocations have predominantly been made to listed markets, where returns have historically been sufficient – in the double-digits in local terms. The penetration of private markets as a whole by pension funds in South Africa is low, with an average allocation of just under 2.5% of total portfolios. Globally, it is about 25%, so that is a wide dispersion already – but one further exacerbated by the extent to which that 2.5% is dominated by some of the larger public pension funds, like the Government Employees Pension Fund (GEPF) and the Eskom Pension and Provident Fund. Also, over the past few decades, there has been a shift in South Africa away from defined benefit to defined contribution pension plans, necessitating that trustees offer adequate liquidity at any given point in time. So, even though trustees may be open to allocating to private markets, liquidity constraints may not allow them to invest to the extent desired. However, the poor returns of listed markets more recently and an increasing social conscience in light of the difficulties our economies and people are facing

is leading asset owners to engage more around private markets. This is where catalytic capital and blended finance structures have the potential to help unlock investment in a meaningful way.

Q: *Can you tell us a bit more about your engagement with investors?*

A: Locally, the pension fund community has not had to delve into more complex asset classes and structures to a great extent and there has been a general aversion to doing so. While, globally, service providers and fund managers have been able to put workable solutions in front of institutional investors that include donor or concessionary capital providers in the structures, locally we have not yet reached a place where all stakeholders are ready to engage. In addition, the relationships between traditional players in the retirement fund industry and potential providers of donor capital or concessionary capital are still in their infancy. You will definitely see the market growing rapidly to the extent that we can get all parties aligned; we are just further behind when it comes to the offerings that we can put in front of investors that fit their mandates and levels of comfort.

Currently, we are engaging with DFIs that can provide guarantees, but it takes a long time to get a commitment to mobilize a structure. This is at least matched by the time it then takes trustees to get comfortable with unfamiliar concepts that involve more complex asset classes than they are used to. The more elegant the structure, the easier it will be to engage with trustees. Despite some of the successes of one or two funds in South Africa, we haven't seen a big succession of replicated structures. We believe that the more conversations we have in the market, the more pension funds will start looking at blended structures as a way to address their concerns around risk when investing in private market investments that address the needs of our people and planet.

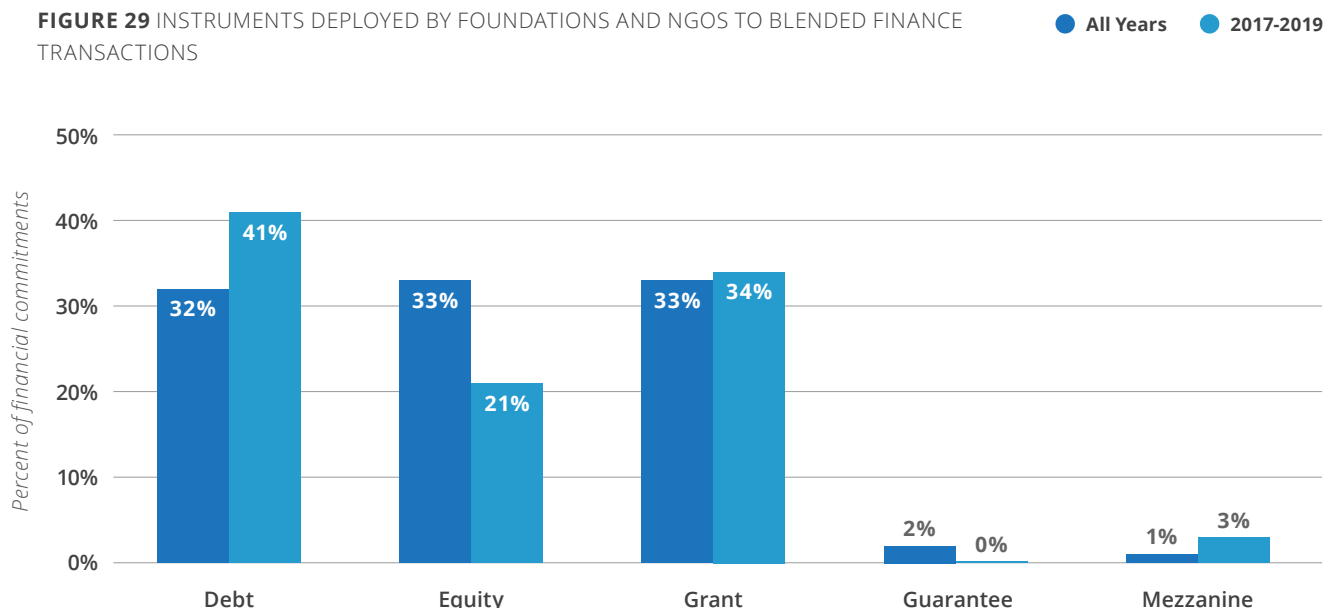
Philanthropic Organizations

Amongst foundations and NGOs, grants (33% of commitments), equity (33% of commitments), and debt (32% of commitments) have historically been the instruments most often deployed in blended finance transactions. In recent years, however, debt has advanced (41% of commitments in 2017-19) while equity has declined (21% of commitments in 2017-19). Further analysis shows that: (i) only 12 foundations and NGOs deployed equity in their commitments to blended transactions in 2017-19, down from 19 in both 2014-16 and 2011-13; (ii) 15 commitments of equity were made in 2017-19, down from 20 in 2014-16 and 27 in 2011-13; (iii) 24 foundations and NGOs deployed debt in 2017-19, compared to 14 in 2014-16 and 20 in 2011-13, and (iv) 29 debt commitments were made by foundations and NGOs in 2017-19, compared to 15 in 2014-16 and 24 in 2011-13. In sum, the number of debt commitments and the number of foundations and NGOs making debt commitments have increased over the course of the decade (barring

a slight dip in 2014-16), but the number of equity commitments and the number of foundations and NGOs making equity commitments have fallen.

Foundations and NGOs have typically invested in blended transactions of the smallest size compared to other investor groups (\$36.3 million median size across all years), and account for a smaller proportion of financial commitments to blended transactions than at the start of the last decade (10% in 2017-19 compared to 14% in 2011-13). Finally, commitments by philanthropic organizations have historically been concessional in nature (77% of commitments), but this has lessened in recent years, with concessional commitments accounting for 51% of their contributions to blended transactions in 2017-19. The rise in their commercial commitments to blended transactions (from 10 in 2011-13 to 30 in 2017-19) suggests that they're increasingly investing for impact across their entire portfolio.

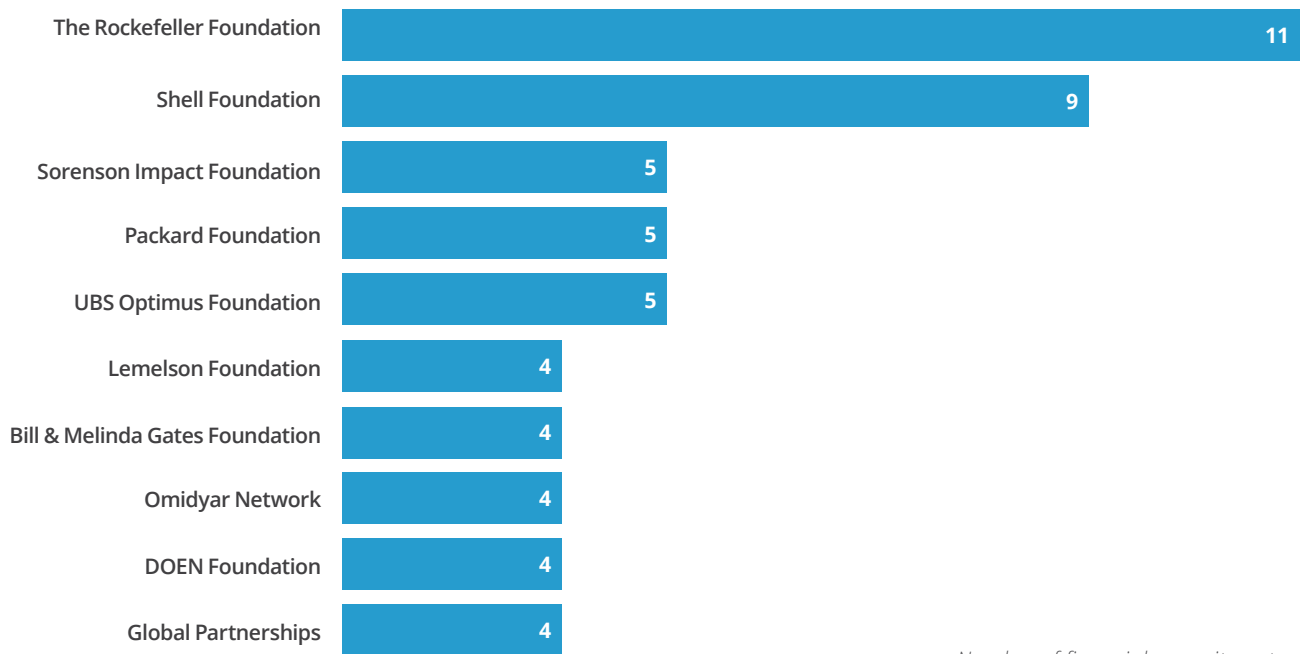
FIGURE 29 INSTRUMENTS DEPLOYED BY FOUNDATIONS AND NGOS TO BLENDED FINANCE TRANSACTIONS



The most prominent foundations and NGOs over the past five years have been The Rockefeller Foundation (11 commitments), Shell Foundation (9), Sorensen Impact Foundation (5), Packard Foundation (5) and UBS Optimus Foundation (5). Foundations and NGOs active in blended finance transactions have distinctions in terms of the blended vehicles through which they invest and the sectors that are targeted. For example, Shell Foundation specifically targets climate change and clean tech, typically investing in companies, while UBS Optimus Foundation has been active in development impact bonds, targeting health and education. Looking at recent activity amongst foundations and NGOs, the Catalytic Capital

Consortium, a \$150 million initiative launched by the John D. and Catherine T. MacArthur Foundation (alongside The Rockefeller Foundation and Omidyar Network) in March 2019 to invest in funds or intermediaries demonstrating a powerful use of catalytic capital, has made a series of investments since inception. This includes a 10-year, \$10 million subordinated loan to One Acre Fund, a non-profit social enterprise supporting smallholder farmers in East Africa. Alongside a guarantee provided by the Ezra Charitable Trust and loans from other anchor investors, the aim is to reduce risk for other lenders and attract up to \$100 million in senior debt and lines of credit.

FIGURE 30 TOP FOUNDATIONS AND NGOS IN BLENDED FINANCE (2014-2019)



Number of financial commitments

Blended Finance Ecosystem Trends and Themes



From Policy to Practice: Coordinating For Better Blending

Over the past few years, Convergence has witnessed increased coordination in the blended finance market, as practitioners have grown more aware of the value of working together to improve and scale blended finance transactions. This past year has been no exception, with actors from across the public, private, and philanthropic sectors coming together in the form of working groups, policy convenings and joint initiatives to better coordinate activities in an effort to achieve better blending. These efforts include

the emergence of new schools of practices, such as the DFID-led Scale Working Group, and the advancement of existing initiatives, such as the [OECD-led Tri Hita Karana \(THK\) Roadmap](#). Such dialogues are essential in bridging siloes between the donor community and private sector, building replicable and scalable structures, and better allocating concessional funds to attract private investment efficiently and effectively. We highlight some of these initiatives below:

Catalytic Capital Consortium

The Catalytic Capital Consortium (C3) is an investment, learning, and market development initiative bringing together leading impact investors who believe that greater, more effective use of catalytic capital is essential to realizing the full potential of the impact investing field, including its role in achieving the Sustainable Development Goals (SDGs).

Members: MacArthur Foundation, The Rockefeller Foundation, Omidyar Network

Activity to date: MacArthur is finalizing investments of up to \$150 million in the aggregate that demonstrate a powerful use of catalytic capital across diverse sectors and geographies. Current blended finance structures supported by C3 to date include (with additional investments anticipated later in 2020) a \$10 million program related investment loan to the One Acre Fund, a nonprofit social

enterprise. This investment will support smallholder farmers in Africa with financing and training through a new capital structure demonstrating the way catalytic capital can bridge financing gaps, spark additional investments, and help sustain and grow high-impact nonprofits. In addition, C3 provided \$20 million in debt in collaboration with the David and Lucile Packard Foundation to launch Terra Silva, an impact investing initiative designed to respond to global climate change by making investments focused on the conservation, restoration, and sustainable management of tropical forests worldwide. The C3 partners are also supporting field-building work to advance learning and market development related to catalytic capital, helping to answer critical questions about the scope of the need for catalytic capital, when and how catalytic capital can be most effective, and what tools and practices are needed.

DFID Scale Working Group

The UK Department for International Development (DFID) and Convergence launched the Scale Working Group in the Fall of 2019, convening a group of development-focused organizations to collaborate on scaling blended finance vehicles.

Members: The Working Group has convened ministries, development agencies, and philanthropic foundations prepared to consider allocating catalytic (i.e., concessional) capital to blended finance solutions.

Activity to date: Over the course of Fall 2019 and Spring 2020, the DFID Scale Working Group has convened three times to shortlist potential scalable blended finance solutions. In addition, the DFID Scale Working Group has supported the publication of two research papers: 1) [Scaling Blended Finance for the SDGs](#) (published December 2020), and 2) [How to Mobilize Private Investment at Scale in Blended Finance](#) (published April 2020).

Liquidnet + Schmidt Futures: B2T Community (Billions to Trillions)

Recognizing that commercial investors often perceive investment products targeting climate and development outcomes, particularly in low income countries, as “high risk, low return,” B2T launched in Q2 2020 as a collaborative effort to mobilize more blended finance at institutional scale. B2T aims to overcome many challenges to scale, including market fragmentation, high transaction costs, information asymmetry, and misalignment of incentives, by building a community of diverse market participants who can more efficiently discover and connect with relevant counterparties. B2T seeks to identify impact-driven concessional capital that can be structured into replicable investment products that directly tackle the climate emergency and other critical development goals, while meeting the risk/return expectations of impact-agnostic commercial investors.

Members: Launched with 20 members, the community has expanded to include 60+ professionals from diverse organizations, including institutional investors, development finance institutions, family offices, foundations, fund managers, and NGOs. B2T developed the following terms to clarify the different roles in the community: **“Builders”** (deal originators, structurers, and fund managers), **“Buyers”** (impact-agnostic institutional investors), **“Catalysts”** (providers of concessional capital seeking development outcomes), and **Service Providers** (intermediaries and supporting organizations).

Activity to date: B2T has developed a shared vision for its future product roadmap; has begun mapping the investment and impact preferences of Catalysts and Buyers; and has refined its process for presenting different investment structures for education and feedback.

OECD Tri Hita Karana (THK) Roadmap

Initially launched in 2018, the Tri Hita Karana (THK) Roadmap for Blended Finance is a shared value system and action plan built upon the recognition that market-wide coordination is necessary to more effectively and efficiently deliver the financing and development impact needed to achieve the SDGs. The THK Roadmap is centred around five action areas: i) Practice, ii) Mobilization, iii) Transparency, iv) Inclusive Markets, and v) Impact.

Members: Supporters include Global Affairs Canada, the Government of Indonesia, Swedish International Development Cooperation Agency (Sida), the Development Bank of Southern Africa (DBSA), the Blended Finance Taskforce, Convergence, the Sustainable Development Investment Partnership (SDIP), World Economic Forum, and the OECD.

Activity to date: Over the past year, each of the five working groups have come together to draft reports to support practitioners in the field, addressing the current state of play and providing recommendations for further action. These deliverables were presented at the THK quarterly meeting hosted in April 2020. In June 2020, the THK held a series of technical workshops for each Working Group to discuss achieved deliverables. Also in 2020, the OECD partnered with Convergence and Sida to launch the [THK Hub](#), a central depository of all relevant knowledge on blended finance and the THK initiative. The THK Roadmap published a [summary report](#) in October 2020 outlining key deliverables and recommendations from each Working Group. Finally, the THK community has also published a [report](#) exploring how DFIs can be strengthened such that they are better prepared for the post COVID-19 rebuilding effort.

Response, Recovery, and Resilience Investment Coalition (R3 Coalition)

Launched in May 2020, the R3 Coalition aims to streamline impact investing efforts addressing the large-scale social and economic consequences of COVID-19. This initiative is managed by the GIIN, and supported by a group of leading foundations. As an immediate response, the R3 Coalition will showcase investment opportunities, including blended finance opportunities – particularly related to health interventions and access to capital – for investors seeking access to capital.

Members: The R3 Coalition is being launched with broad collaboration across the global impact investor community and with financial support and guidance from leading foundations, including

David and Lucile Packard Foundation, the DOEN Foundation, Ford Foundation, John D. and Catherine T. MacArthur Foundation, Open Society Foundations, The Rockefeller Foundation, and Sorenson Impact Foundation.

Activity to date: The R3 Coalition has released three issue briefs to date on “[The Impact Investing Market in the Covid-19 Context](#),” including: [An Overview](#) (June 2020), [Due Diligence](#) (July 2020), [Investor Support of Enterprises](#) (July 2020), and [Advancing Social Equity to Build Resilience](#) (September 2020).



Blended Finance in Global Health

Global health is ripe for an uptick in blended finance. Low health budget-allocations across developing countries have resulted in a \$134 billion annual health funding gap in low and middle-income countries. If funding trends continue, this gap is expected to reach \$371 billion annually by 2030. The impact of the COVID-19 pandemic is expected to only further exacerbate this funding gap, particularly in developing countries where healthcare systems are relatively weak, supply chains remain vulnerable, and difficulties persist in proper infection prevention and control.

To date, the health sector has only accounted for 6% of blended finance transactions, and a mere 3% of transactions over 2017-2019. However, change may be on the horizon. Convergence data on transactions currently fundraising reveal significant efforts are underway, with 19% of transactions currently seeking blended capital in health field. Areas where we believe blended finance could contribute include the delivery of health services, SME financing, and

vaccinations and pharmaceuticals. For example, blended finance has been touted as one way to help mobilize additional financing towards vaccine development, such as, for example, through advance market commitments (AMCs), where concessional funders guarantee the future purchase of a service or product not yet available, or not available in a particular market at a specific price. We have also seen good traction for blended finance in the health SME space, including examples such as the [Medical Credit Fund](#), which draws on blended capital to provide local currency financing to health SMEs in Africa. As emphasized by Elena Sterlin, Senior Manager for Health and Education at IFC, healthcare services require long-term local currency financing, which can be very difficult to secure in developing markets. Blended structures that can de-risk investors' currency exposures will thus be critical going forward. We believe these transactions are an indicative example of the potential role that blended finance can play to further finance health outcomes in the future.



Towards Gender Mainstreaming in Blended Finance

There is a broad consensus that blended finance is a useful tool to advance gender equality. However, while we have seen greater focus on gender lens investing in recent years, gender equality remains underrepresented as an investment theme in the blended finance market, with 18% of transactions aligning with SDG 5 (Gender Equality) from 2017-2019. Of transactions aligned with SDG 5 in our database, analysis conducted by Convergence earlier this year found 58% of them to be gender-aware (e.g., transactions that explicitly target women as beneficiaries while reporting gender-disaggregated data), while 42% of transactions signaled an intentional aim to achieve women's empowerment or gender equality. On the upside, Convergence found that more than a third of all historical blended finance transactions third (34%) report gender-disaggregated data, an important first step in developing evidence-based approaches for equitable development and assessing the impact of blended finance on women and girls.

Over the past year, we have also seen positive market developments in mainstreaming gender in the blended finance community. For example, in May 2020, Women's World Bank Capital Markets Fund II (WWBII) achieved a first close of \$75 million, with

commitments from organizations including USAID INVEST and DFC. WWBII, a Convergence grantee and blended fund, draws on first-loss funding and technical assistance to support financial service providers that focus on women, including as employees and clients. Other initiatives include the IFC Women Entrepreneurs Finance (We-Fi) initiative, which uses blended finance to increase private investment for women entrepreneurs. In 2020, IFC We-Fi invested \$1 million in equity into TIDE Africa, a venture capital fund in Sub-Saharan Africa that invests in technology and tech-enabled enterprises in the early stages of growth. Concessionality was provided in the form of a performance-based incentive of \$125,000, to help fund managers absorb the costs associated with adopting sourcing strategies to generate a pipeline of high-growth women-led technology start-ups.

Also taking place this year, Convergence launched the Indo-Pacific Design Funding Window with funding from the Australian Government, to provide grant funding for the design and launch of catalytic blended finance solutions in certain countries in the Indo-Pacific region focused on sustainable and resilient infrastructure, and gender

equality. Design funding can be an important tool for integrating a gender-lens early into the design of blended finance vehicles.

Foundations are also taking innovative approaches to integrate gender within their portfolios, including in non-traditional sectors such as climate and clean energy. For example, Shell Foundation is incorporating a gender lens across its entire portfolio, including tracking how women are empowered as consumers, entrepreneurs, employees, and distributors and suppliers within its value chains.

As investors become increasingly sophisticated in their gender lens approaches, new resources have emerged on incorporating gender within investment strategies and processes. Pacific RISE and the Criterion Institute jointly developed the world's first investment due-diligence tool for gender-based violence. The Small Enterprise Assistance Funds (SEAF) published the SEAF Gender Equality Scorecard Manual in July 2020, which focuses on integrating a gender lens in growth-oriented SMEs. In the same month, the GIIN, CDC and the 2X Challenge released a new guidance note, "[How to Measure the Gender Impact of Investments](#)," which details the application of 2X Challenge indicators and maps them to the

IRIS Catalog of Metrics. Lastly, the Criterion Institute, in partnership with the impact investment firm Dreilinden, published "[Investing with an LGBTQI Lens](#)," a guide on investing to further the rights and empowerment of lesbian, gay, bisexual, transgender, queer, and intersex (LGBTQI) individuals.

"Design funding is a really useful way of incorporating a gender lens, because it allows gender to be structured into investment vehicles upfront. Otherwise, it can be very difficult to bring in in a meaningful way later. Gender-lens investing is not just about counting women beneficiaries or reporting sex disaggregated data at the end of our program; gender lens investing is about integrating gender analysis up front into program design, including fund structuring and pipeline development, so that when investment products go to market, gender is baked into the solution."

DIRECTOR, DEVELOPMENT AGENCY

Blended Finance in Southeast Asia

"Asia's population growth is driving much of the economic growth in the region. Within these economies, many populations are young, particularly in Southeast Asia, and levels of skill and education are rapidly increasing, with primary economies transitioning into secondary economies defined by greater discretionary spending and purchasing power, more services becoming available, an increased focus on urban infrastructure and transport, and increased power consumption. Sector-wise, there is ample space for new financing for infrastructure, financial services, agribusiness and health and education. **Given the scope of financing gaps across Asia and the Pacific, there is enormous scope for blended finance to catalyze and demonstrate high development impact initiatives.** What remains imperative is donor appetite for new financing facilities, and the DFIs prompting donors to fund these different vehicles."

DAVID BARTON, SENIOR INVESTMENT SPECIALIST, ASIAN DEVELOPMENT BANK (ADB)

Earlier in this report, we highlighted the upsurge of blended finance activity in East Asia and the Pacific, accounting for 21% of total transactions from 2017-19, compared to 14% across all time periods. Several Asian-domiciled investors, including Mitsubishi UFJ Financial Group, Sumitomo Mitsui Banking Corporation, and Mizuho Bank, appear in our league table for commercial investors active in blended finance transactions. Finally, between 2017 and 2019, Indonesia (12 transactions), Philippines (9 transactions), and Vietnam (7 transactions) were ranked in the top 10 countries for blended finance by deal count. In these markets, and others within Southeast Asia, investor focus has been on sectors like renewable energy, infrastructure, agribusiness, and financial services. Private-led renewable energy projects and independent power producers have been actively promoted in recent years in countries like Thailand and Vietnam.

According to David Barton of the Asian Development Bank, geographically, concessional financing can be particularly useful in less established markets, where it can provide a much-valued cash cushion in early-stage development projects to account for unexpected events post-financial close, such as construction delays or changes in regulatory environments.

Looking ahead, Barton predicts that some of the greatest challenges will relate to improving the enabling environments in the region. While some countries have been more supportive of reform, eager to incentivize private developers, the situation in other markets can be more difficult. Here, the biggest challenge pertains to getting legal and regulatory reforms in place to create a stable and level playing field for private companies, allowing them to make estimates, plan projects and invest capital. Similarly, according to an assistant director at a development agency, it remains critical that donors support partner governments in the region in building their capacity to structure and regulate PPPs in the infrastructure space to effectively crowd-in private finance and promote development.

Continuing to create bankable projects supported by blended finance in key emerging sectors will also be critical going forward. Convergence has previously argued that climate finance is a particularly ripe area for new approaches, as Asia and the Pacific is increasingly prone to severe weather events, with consequences for regional economies.

“Blended finance has been deployed in the renewables sector, but not as much in other important areas like low-carbon urban infrastructure and transport, or land use. In the land use sector, there is substantial misperception of risk that needs to be addressed. Here, the need is for the integration of people and conservation into bankable projects and partnerships with NGOs and others to build these projects. For now, it is bridging the language barriers between NGOs who are working locally and investors who want to make sure the projects are bankable. Essentially, we are creating new business models that integrate environmental and social considerations, using blended finance to get private investors over the hurdle. We do feel blended finance is critical to building bankable climate finance projects in the region.”

LISA GENASCI, CEO, ADM CAPITAL FOUNDATION

Reflections



Blended Finance and COVID-19

“The pandemic has been a significant shock to investors’ outlook, both in terms of actual and perceived risk. But, one of the silver linings is that investors have realized that risk is everywhere, not just in the developing world. We are starting to see institutional investors reassess how they make commitments. Where they traditionally had a heavy developed market bias, a combination of factors has shown them that volatility is everywhere, and that the returns are in the fastest-growing markets.”

SENIOR MANAGER, DEVELOPMENT AGENCY

The COVID-19 pandemic has had a seismic impact on the global economy, upending health systems and societies worldwide, while having an outsized impact on developing countries without the fiscal wherewithal to effectively fight it. For example, the OECD estimated that external private finance inflows to developing economies could fall by \$700 billion in 2020 compared to 2019 levels, a drop 60% greater than the immediate impact of the 2008 global financial crisis.

Convergence has discussed the threat COVID-19 poses to the achievement of the SDGs in more detail, while also identifying specific challenges in the real economy that are well-conditioned for blended finance solutions, including in the area of global trade and supply chains, where blended solutions can help lower the cost of critical goods like medicine or medical diagnostic equipment, catalyze private capital to fund the digitization of global trade finance post-pandemic; and free up DFIs’ balance sheets by shifting their trade finance guarantee portfolios to the private sector, particularly insurance companies.

However, challenges remain. A paper from the THK community highlights elements of DFIs’ business models that must be addressed for DFIs to effectively tackle the myriad challenges raised by the pandemic. This paper questions whether

Convergence has argued that the role for blended finance is in the medium- to long-term response to the pandemic, by accelerating economic reconstruction, improving pandemic resiliency and responding to the global health crisis (where possible), and also in turbocharging the collective efforts towards the achievement of the SDGs.

DFIs’ traditionally conservative business models allow them to lend countercyclically and at scale, with DFIs’ financial responses to the pandemic to-date seldom containing new commitments, and DFIs likely being unable to serve struggling existing clients in middle-income countries while funding new projects in hard hit low-income countries. Indeed, the pandemic has engendered liquidity constraints affecting the capacity of public and private investors alike to deploy capital.

“Our own access to liquidity was impacted by the COVID-19 crisis, and it was multiplied by the fact that South Africa had been further downgraded by some of the rating agencies during the same period. We have equity from the South African government that had previously been granted, and we retain our profits annually, but we then add to that equity with borrowings from the commercial markets and from other development banks. On the liability side of our balance sheet, borrowing costs had increased during the COVID-19 crisis, and it became more difficult for a few months to be able to access longer tenor debt, and so it became harder for us to support projects in Southern Africa and in the rest of the African continent. Fortunately, things are now starting to improve.”

MOHAN VIVEKANANDAN,

GROUP EXECUTIVE, ORIGINATION AND COVERAGE, DBSA

Similarly, a director at a development agency notes the liquidity issues faced by regional institutional investors:

“Funds are acutely aware of the need for liquidity in their portfolios, which is likely to have implications for how much they are willing to allocate to our priority areas in blended finance. On the broader impact investor front, many investors are focusing on impact closer to home, particularly if they have not already got regional investments. Not surprisingly, as a result of COVID-19, there seems to be increasing risk aversion; an inclination to maintain existing portfolios and wait and see how the pandemic and its economic impacts develop before investors look at new opportunities and new regions.”

DIRECTOR, DEVELOPMENT AGENCY

The COVID-19 pandemic has also presented funds seeking to build their pipelines with unique challenges.

“It has slowed project development. Clearly, site visits are impossible, and fundraising is more of a challenge, but ADM Capital has been around since 1998, and has deep networks across Asia.”

LISA GENASCI, CEO, ADM CAPITAL FOUNDATION

Fortunately, we see increasing momentum across the field in thinking about how the development community can respond to the pandemic in a more effective, longer lasting, and sustainable way (following the initial emergency responses focused on scaling up existing approaches). For example, the THK [paper](#) on DFIs and their response to the pandemic pushed for the creation of a new COVID-19 Stretch Fund to widen the spectrum of investments and environments in which DFIs can participate and open up more investment opportunities by including high-risk tranches. Such a fund would target MSMEs and the financial institutions supporting MSMEs, and would deploy equity, guarantees and first loss protection, and subordinated debt, including in local currency. Similarly, there have also been [calls](#) for the creation of a Global Health Security Challenge Fund, which would blend resources from national governments, global financial institutions like the World Bank, bilateral development agencies, international philanthropies and the private sector, to help at-risk economies improve their preparedness for epidemic scenarios.

Overall, it is at this juncture where we see blended finance playing a vital role: in aligning the private, public, and philanthropic sectors in developing innovative solutions that can turbocharge the post-crisis economic reconstruction.

The Time for Blended Finance at Scale Has Arrived

2020 marks the beginning of the Decade of Action, with less than 10 years left to achieve the SDGs. While some progress has been made, financing to meet the SDGs has not advanced at the scale or speed required. Current blended finance flows, averaging ~ \$11 billion over the past five years (2014-2019), will result in “billions to billions” rather than the needed “billions to trillions.” Since the emergence of the COVID-19 pandemic, the need to achieve scale is greater than ever – the time for blended finance at scale has arrived. With traditional sources of development funding reaching a plateau — including concessional funding provided by MDBs and DFIs, coupled with consistent levels of ODA — limited concessional funding must be used efficiently to maximize additionality. At the same time, there has never been a more ripe time for the private sector to engage in blended finance; the growth of private sector interest in investment themes and strategies such as responsible investment, sustainable finance, ESG investment, green investment and impact investing presents an unprecedented opportunity for investments aligned to the SDGs in developing countries.

Yet, current challenges for blended finance transactions looking to achieve scale persist, including i) a lack of a robust pipeline of bankable projects due to small transaction sizes, (ii) complex and unfamiliar structures, and (iii) continued siloes between the donor community and the private sector. Encouragingly, we are seeing blended finance practitioners meet these challenges with innovative and streamlined solutions. Based on engagement with leading stakeholders in the blended finance market, Convergence identifies the following strategies to scale blended finance:

1. **Focus on portfolio approaches rather than stand-alone projects to mobilize investors at scale.** Portfolio approaches are preferred for three key reasons:
 - i. Only a small number of stand-alone projects are a suitable ticket size for private investors. Aggregating multiple projects can achieve the required critical mass.
 - ii. Diversification across projects reduces risk and risk-return variance for investors. Indicatively, the Big 3 rating agencies’ methodologies allow for a two-notch upgrade for diversification across multiple borrowers in Non-Investment Grade Countries – that is, a portfolio of “B” projects can be enhanced to “BB-,” simply through diversification. In countries with very high country risk (e.g. Low-Income Countries), diversification across multiple countries is highly beneficial.
 - iii. Bundling transactions accelerates taking transactions to market and lowers transaction costs as compared to individual projects.

“We have taken from the lessons learned from the South African Renewable Energy Independent Power Procurement Programme (REIPPPP). The lesson learned from that is: you approach a sector from a programme lens – meaning that you are not trying to unlock a single renewable energy project, a solo PV project in location A or another wind project in location B, but you ask: what are the energy needs of our country? How much of that should come from renewable projects? You then set some basic standards and create a very open, transparent process for the private sector to participate in - then you can have significant amounts of capital coming in, and generally very good project results as well.”

MOHAN VIVEKANANDAN, GROUP EXECUTIVE,
ORIGINATION AND COVERAGE, DBSA

2. **Standardized and simplified blended finance structures should be pursued aggressively.**

Admittedly, it will take time for the blended finance market to reach standardization. On the one hand, the use of concessional financing in blended finance structures – whether it is concessional debt or equity, technical assistance funding, guarantees, or design funding – must be fit-for-purpose and adapted to the local context of investment opportunities. Moreover, innovative and bespoke structures are needed when entering nascent sectors or low-income countries. At the same time, complexity should be reduced as much as possible, particularly when looking to attract institutional capital. Institutional investors are seeking familiar, simple and replicable structures that are comparable to other investment opportunities – regardless of blending.

- ## 3. **Catalytic capital providers should be more transparent on the availability and terms of concessional capital to help private investors better understand their investment opportunities.**
- Meanwhile, concessional capital providers aim to attract private investors without over-subsidizing, while mobilizing capital to higher impact sectors (e.g., WASH, health) and lower-income regions (e.g., LDCs).

However, as evidenced by the growing schools of practice dedicated to advancing the field of blended finance, the gap between actors is beginning to narrow as greater coordination occurs on both sides of the aisle. For example, through the DFID Scale Working Group, C3 Initiative, and the DFI Working Group on Blended Concessional Finance, official development providers and philanthropic organizations are working together to prioritize funding blended finance initiatives that are scalable, while collaborating to establish standards on minimum concessionality. In turn, private investors are also coordinating to participate in new investment opportunities in emerging markets, including through new initiatives such as the R3 coalition and Liquidnet’s B2T community.

“Information asymmetry is a real issue – people don’t know who the counterparties might be or how to signal to the market to find the right people that they should be connecting with on different transactions.”

BRIAN WALSH, HEAD OF IMPACT, LIQUIDNET, AND CO-FOUNDER, B2T COMMUNITY

VOICES FROM THE FIELD:

Standardizing Blended Funds in Blended Finance

Interview with Simon Gupta, Head of Business Development
DFI / IFI, responsAbility Investments AG

Q: *When designing products, how do you balance innovation and customization against simplicity to attract the private sector?*

A: They must be private sector ready. Simplicity is key because most money managers in the private sector must understand the structure fast. Therefore, the more it resembles standardized structures, the better it is. Some of our blended finance debt funds have a lot of structural features inspired by PE funds because we knew that private investors would be more familiar with them.



Q: *What structural features have been lifted from PE funds and applied to your debt funds?*

A: One is the **lifetime of the fund**—we do not create open-ended debt funds. We look at what is the classical fund lifetime; 10 years as in PE. Even though you might not solve the underlying development problem in 10 years, you have a determined timeline and can set up a second fund if the problem persists beyond the fund's lifetime.

Second is the **single share class** like you normally have in PE, so everybody has the same rights and there is no differentiation on risk and return, and we really simplify that to the degree possible. Having different rights for different share classes is where you can very easily increase the complexity enormously.

Then, the third involves **manager incentives**. You need to have a very classical simple management fee; usually in PE, that is around roughly 2%, and then you have a performance fee, which measures whatever the performance measurements or the impact indicators of the fund are. When those are reached, the manager gets an extra carry or performance fee. Like in PE, this aligns managers and investors.

We see that in 2020 **risk is not the main problem for most private investors; it is mostly returns and the simplicity of the structure that brings success.**

Local Institutional Capital in Blended Finance

The limited participation of local institutional investors in blended finance transactions to date is an obvious challenge facing the industry, with most private investors in our blended finance league tables being institutions domiciled in North America or Europe. Local investors' understanding of the real risks of investing in their immediate geographies, and their ability to invest in local currency, position them to invest where foreign investors might require a higher risk premium. Their presence in a transaction can also provide comfort to foreign investors. However, local

institutional investors can face unique barriers to investing in blended finance transactions, from low exposure to private markets, to overly complex blended finance transaction structures, to regulatory factors shaping the profile of institutional investors' asset allocation mixes. However, organizations like GuarantCo, for example, have specific mandates to develop local capital markets and have worked to enable dual listings of local currency bonds on developed country exchanges to introduce greater liquidity into developing markets.

VOICES FROM THE FIELD:

Building the Capacity of Local Institutional Investors in Blended Finance

Interview with Lasitha Perera, Chief Executive Officer, GuarantCo

Q: *How can blended finance better mobilize local institutional capital?*

A: The fundamental gap that we are seeing on the institutional investor side in developing countries is one of knowledge, a capacity gap. If you speak to them about blended finance or credit enhancement, they will not understand what that means until it is explained to them,

with the benefits being made clear. If you present an investment opportunity to local institutional investors without in parallel carrying out the capacity building element, what you will find is that you may succeed once but you will not create the replication effect desired in the long run.

Q: *Can you provide an example?*

A: With GuarantCo, in Nepal, we provided a guarantee for the first local currency project financing into a hydropower plant. We found that the Nepalese banks were quite liquid and happy to provide very long-term, 16-17-year financing in local currency to the project; however, they had limited experience or grounding in project finance. So, we used some grant money to run a project finance training programme for them, then took them through the due diligence process alongside us on the project, and then got them to invest under our guarantee.

Subsequently, we were looking at another hydropower project in Nepal about 12-24 months later, and we approached the same banks. In the original transaction they had started with a 100% guarantee requirement from GuarantCo, and after the training programme they went down to a 90% requirement. That 10% differential in dollar terms was about \$2 million equivalent, and the cost of the programme that we ran was about \$200,000. **So, you could argue that from a blended finance perspective, \$200,000 of public sector capital or grant money mobilized \$2 million, a 10x multiple on that investment.** In the next project we came along in the hydropower sector, the banks were happy to look at a 30-50% guarantee (depending on which institution we were considering at the time).

So, the key step that we made with those banks was educating them and building their capacity, and then using a guarantee to mobilize them, and then realizing later on that we needed less of that to actually get them to lend to the second project. While the second project ultimately did not happen, this was for reasons beyond the financing, relating to the equity and the developers.

Another example relates to InfraCredit Nigeria, who have guaranteed three energy bonds over the last couple of years. In parallel to providing those guarantees, InfraCredit Nigeria has been running training on due diligence, capital markets, and project finance alongside those bond issues to help institutional investors build their capacity and to look beyond the AAA guarantee, so that they can fully understand the fundamentals of the investment they are making.

Recently, another energy company in Nigeria issued a bond that was oversubscribed, with no credit enhancement attached. Several of the pension funds that had invested in the previous energy bonds had chosen to invest in this particular bond without any credit enhancement. That demonstrates that capacity building alongside the product is quite key.

Q: *In your experience, what is the credit rating 'sweet spot' when trying to mobilize local debt investors?*

A: Although it depends on the market, investors typically want AAA ratings because they are not used to investing in non-sovereign paper. From our perspective, we want to get them comfortable investing in debt instruments with BBB ratings, and we have found that the movement can be quick when investors' capacity is increased such that they fully understand what they are investing in.

The Blended Finance Community Must Heed Calls for Better Impact Reporting and Transparency

As blended finance becomes a mainstream tool, there have been growing calls for greater transparency around impact reporting and impact outcomes. As evidenced by Convergence data, over 40% of blended finance transactions do not publicly report impact (2014-19). The lack of transparency on impact outcomes reflects a larger issue in the official development community. For example, the Aid Transparency Index 2020 [report](#), by the Publish What You Fund campaign, found that only a small minority of donors published the results of their projects, and even fewer published project reviews and evaluations. This information is important in helping stakeholders monitor the effectiveness of their aid and the impact of their projects, and in extracting and sharing learnings from successes and challenges.

This is equally as important for advancing the uptake of blended finance. Based on Convergence's data, we

know that blended finance structures ultimately aim to benefit low-income populations, with over 50% of transactions targeting BoP populations, and over 50% of transactions aligned with SDG 1 (No Poverty). However, little information is collected ex post. This limits our understanding of how blended finance has supported beneficiaries, and the quality of the impact delivered. As highlighted by Development Initiative's report, entitled "[How Blended Finance Reaches the Poorest People](#)," published in October 2019, major gaps include data on the quality of investments, who benefits, and the systemic (long-term) effects.

The official donor community has taken heed of these shortcomings, and over the past year, we have seen timely progress led by organizations such as the OECD THK Roadmap, including the Impact Working Group and Transparency Working Group.



In 2020, the Impact Working Group published a Checklist for Assessing the Impact of Blended Finance on the Poor as a tool for exploring ex ante and measuring ex post impact. Moreover, the THK Impact Group has worked with the GIIN to align the THK Checklist to IRIS metrics, enabling greater standardization as public and private blended finance providers are presented with a common and comparable method to measure impact.

Transparency is an essential step towards improving the design, accountability, and effectiveness of blended finance. Similarly, public information relating to impact as well as returns and financial performance are important for purely commercially-motivated investors. To this end, the OECD Transparency Working Group [developed recommendations](#) for advancing the blended finance transparency agenda. Other initiatives progressing transparency work include the DFI Working Group on Blended Concessional Finance. Since 2017, the DFI Working Group has published three Joint Reports (2017, 2018, and 2019) on blended concessional

finance for the period of 2014-2018, across private sector operations of 23 DFIs. This is a notable step forward in terms of both availability of information and standardization of reporting across key blended finance actors. In October 2019, IFC committed to publicly disclosing the level of concessionality for blended finance activities supported by the IDA-Private Sector Window, including across its four facilities: Local Currency Facility, Blended Finance Facility, Risk Mitigation Facility, and MIGA Guarantee Facility. Additional initiatives that advocate for increased transparency and disclosure include the Publish What You Fund's [DFI Transparency Initiative](#), launched in November 2019, which aims to increase public information sharing amongst DFIs. This initiative is funded by the Bill and Melinda Gates Foundation and will work to increase transparency on DFI's private sector portfolios. While transparency in blended finance is limited by a number of challenges, including confidentiality concerns held by public, philanthropic, and private actors, we are seeing good momentum towards a more transparent and accountable blended finance market.



About Convergence

Convergence is the global network for blended finance. Convergence generates blended finance data, intelligence, and deal flow to increase private sector investment in developing countries and sustainable development. Convergence works to make the SDGs investable through transaction and market building activities:

- **A Global Network:** We have a global membership of over 200 public, private, and philanthropic organizations like USAID, the Asian Development Bank (ADB), First Rand, and the John D. and Catherine T. MacArthur Foundation. We create many opportunities for Convergence members to connect, including through the Convergence deal and investor matchmaking platform and exclusive networking events.
- **Data & Intelligence:** We curate and produce original content that builds the evidence base for blended finance and supports practitioners in their efforts to execute blended transactions, including (i) data on deals and investors, (ii) case studies, intelligence briefs, and market reports, (iii) workshops and trainings, and (iv) webinars.
- **Deal Flow:** We have built an online matchmaking platform for investors and those seeking capital to connect. As of September 2020, there are live opportunities seeking to raise over \$5 billion, representing over \$9.6 billion in aggregate deal value. All deals are screened by our team to ensure that they fit within our mandate.

- **Market Acceleration:** Our Design Funding program offers grants for the design of innovative blended finance vehicles that aim to attract private capital at scale. As of September 2020, grantees have raised nearly \$600 million of additional capital – that’s more than an 85x multiple on the close to \$7 million that Convergence has awarded. In 2020, Convergence is also supporting the UN Joint SDG Fund in operationalizing the [Call on SDG Financing Component 2: Catalyzing Strategic Investments](#). So far, \$4 million in grant funding has been awarded to UN country teams designing investable solutions to finance the SDGs.

Convergence focuses exclusively on blended finance to catalyze private investment. Other important stakeholders and initiatives, such as the DFI Working Group on Blended Concessional Finance for Private Sector Projects (DFI Working Group), focus on a broader scope of blended finance that includes the use of development funding to mobilize commercially oriented public capital (e.g., capital from MDBs and DFIs). Convergence works closely with the OECD, the DFI Working Group, and other key stakeholders to coordinate blended finance activity.

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Convergence is the global network for blended finance. Convergence generates blended finance data, intelligence, and deal flow to increase private sector investment in developing countries and sustainable development. The State of Blended Finance is Convergence's annual report on blended finance trends, opportunities, and challenges. It builds on the inaugural report released in July 2017.

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