Innovative Financing for Development: Scalable Business Models that Produce Economic, Social and Environmental Outcomes

Landscape Overview for the Leading Group Expert’s Workshop

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Need

- Mobilize Resources
- Enable Access to Markets
- Provide Access to Goods and Services
- Supply Public Goods
- Increase Value for Money

International Commitments

- Monterrey Consensus 2003
- Millennium Summit 2005
- Doha Declaration on Innovative Financing for Development 2007
- I-8 Group Created 2008
- General Assembly Resolution on Innovative Sources of Financing 2009
- Busan Declaration and Rio Declaration 2010
Context
Innovative financing remains a small component of public sector assistance

Evolution of funding for public goods in developing countries, 2001-2012
USD billions

Notes: Net Government expenditure does not include general budget support and loan disbursement to public sector; Official aid flows include Official Development Assistance, Officially funded loans and Others Official Flows; Innovative finance data is based on 138 innovative finance initiatives where volume data broken down by year was available.

Source: Development initiatives, “Investments to End Poverty,” 2013, Dalberg Database of Innovative Financing Mechanisms, Dalberg analysis
The Innovative Financing Report describes the market and is a platform for further conversations.
There is no common, clear definition for innovative financing for development

Source: Dalberg analysis.

<table>
<thead>
<tr>
<th>Resource mobilization</th>
<th>Not traditional ODA</th>
<th>Development impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>“..support fundraising by tapping new sources...”</td>
<td>“..go beyond traditional spending...”</td>
<td>“...deliver financial solutions to development problems...”</td>
</tr>
<tr>
<td>“...mechanisms of raising funds...”</td>
<td>“...complementary to official development assistance”</td>
<td>“...correcting the negative effects of globalisation...”</td>
</tr>
</tbody>
</table>

... that inform our definition

Innovative financing mechanisms for development ("innovative financing") encompass approaches to **mobilizing resources** and to **increasing the effectiveness and efficiency** of financial flows that **address** global social and environmental challenges.

Source: Dalberg analysis.
## Methodology
**Bottom-up analysis based on type of instrument and instrument characteristics**

<table>
<thead>
<tr>
<th>Securities and Derivatives</th>
<th>Results-Based Mechanisms</th>
<th>Voluntary contributions</th>
<th>Compulsory Contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Guarantees</td>
<td></td>
<td>12 Auctions</td>
<td>14 Taxes and Levies</td>
</tr>
<tr>
<td>2 Impact Investing Funds</td>
<td></td>
<td>13 Consumer donations</td>
<td></td>
</tr>
<tr>
<td>3 Microfinance Investment Funds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4 Thematic Bonds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5 Thematic Loans</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6 Other derivative products</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### A Maturity and Scope
Did the instrument mobilize resources for a developing country?

### B Innovation
Did the instrument:
- Introduce a new product;
- Enter a new market; or
- Attract new participants?

### C Intention
Did the sponsors of the instrument intend to produce positive social and environmental outcomes?

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Source: Innovative Finance Initiative
Market Size and Distribution
Innovative Financing has mobilized nearly USD 100 billion since 2000

Amount mobilized by innovative financing mechanisms, 2000-2013
Percent of total mobilized (n=278)

- Bonds; 24.8%
- Guarantees; 38.6%
- Development Impact Bonds; 0.0%
- Microfinance; 9.8%
- Investment funds; 8.1%
- Other derivative products; 0.6%
- Performance-based contracts; 5.3%
- Debt-swaps and buy-downs; 1.5%
- Advanced Market Commitments; 1.2%
- Awards and Prizes; 0.3%
- Consumer purchases; 0.2%
- Taxes and Levies; 2.6%
- Auctions; 6.9%

Source: Innovative Financing Initiative Database; Dalberg analysis
Development Focus
Many initiatives tend to have broad sector coverage

Innovative financing mechanism by sector

- Access to Finance: 155 mechanisms
- Energy and Agriculture: 44 mechanisms
- Health: 27 mechanisms
- Disaster Response: 24 mechanisms
- Education: 4 mechanisms
- Housing: 4 mechanisms
- Technology: 2 mechanisms
- Multiple: 83 mechanisms

E.g. microfinance, SMEs, investment funds

E.g. guarantee facilities, funds, currency swaps with multi-sector mandates

Desire by sponsors to diversify exposure and reach and need for cross-cutting solutions to address common financial challenges

Note: Sector information was available for 348 mechanisms. Average initiative size was based on data for 278 mechanisms. Other smaller sectors not shown include Technology, Housing and Urban Development, Water and Sanitation, ICT and Media.

Source: Innovative Financing Initiative Database; Dalberg analysis
Market Evolution
Since 2001, innovative financing has experienced 11% annual growth

Annual amount mobilized, 2001-2012
USD millions (n=137)

Note: The figure does not include 141 mechanisms for which annual mobilized data was unavailable.
Source: Innovative Financing Initiative Database
Potential for Increased Scale
Established mechanisms with simple structures are most likely to scale

Landscape of innovative financing mechanisms

- Securities and Derivatives
- Results Based Financing
- Voluntary Contributions
- Compulsory Contributions

Proven models
- Bonds and Notes
- Consumer Donations
- Loans
- Guarantees

Newer Ideas
- Microfinance Funds
- Development Impact Bonds
- AMCs
- Other Derivative Products
- Carbon Auctions

Replication Opportunities
- Debt-swaps/buy-downs
- Awards and Prizes
- Performance-based Contracts
- Taxes

Note: No known Development Impact Bonds have been successfully issued to date although many are under development.
Source: Innovative Financing Initiative Database; Dalberg analysis
Expectations for the Future
The innovative financing market is still evolving

<table>
<thead>
<tr>
<th>Time</th>
<th>Size of sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995 - 2005</td>
<td>Aid-based pilots mobilize resources</td>
</tr>
<tr>
<td></td>
<td>Public goods related to health, environment and infrastructure</td>
</tr>
<tr>
<td>2005 - 2015</td>
<td>Experimentation with market-based instruments grow the market</td>
</tr>
<tr>
<td></td>
<td>Targeted investment opportunities within agriculture, energy and infrastructure</td>
</tr>
<tr>
<td>2015 - 2030</td>
<td>Outcomes-based finance attracts private capital</td>
</tr>
</tbody>
</table>

**Mechanisms:**
- Taxes, levies and voluntary private contributions
- Foreign-based investment funds, public-partnerships, and solutions to address political constraints
- Risk sharing and incentives to mobilize private enterprises and local investors

Source: Dalberg Analysis
Additional Slides
There is no common, clear definition for innovative financing for development

World Bank

“Innovative financing involves non-traditional applications of solidarity, PPPs, and catalytic mechanisms that (i) support fund-raising by tapping new sources and engaging investors beyond the financial dimension of transactions, as partners and stakeholders in development; or (ii) deliver financial solutions to development problems on the ground.”

OECD

“Innovative financing comprises mechanisms of raising funds or stimulating actions in support of international development that go beyond traditional spending approaches by either the official or private sectors, such as: 1) new approaches for pooling private and public revenue streams to scale up or develop activities for the benefit of partner countries; 2) new revenue streams (e.g. a new tax, charge, fee, bond raising, sale proceed or voluntary contribution scheme) earmarked to developmental activities on a multi-year basis; and 3) new incentives (financial guarantees, corporate social responsibility or other rewards or recognition) to address market failures or scale up ongoing developmental activities.”

Leading Group on Innovative Financing for Development

“An innovative development financing mechanism is a mechanism for raising funds for development. The mechanisms are complementary to official development assistance. They are also predictable and stable. They are closely linked to the idea of global public goods and aimed at correcting the negative effects of globalisation.”

Of the 347 mechanisms in the database, only 278 mobilized resources between 2000 and 2013. This reflects the emergence of new asset classes such as Development Impact Bonds, which did not mobilize any resources during that period, and new products, such as the DFID Innovation Prizes for Environment and Development which was launched in 2013 and has not been implemented yet.

We defined the universe of impact investing and microfinance funds based on the decision of managers to register with ImpactBase, a leading database of impact investing funds. Many fund managers elect not to register with ImpactBase, which makes this a conservative estimate of the market size.

Source: Innovative Financing Initiative Database; Dalberg analysis

### Overview of the Innovative Financing Database

<table>
<thead>
<tr>
<th>Securities and Derivatives</th>
<th>Number in Database</th>
<th>Number that mobilized resources between 2000-2013</th>
<th>Amount mobilized between 2000-2013 (USD M)</th>
<th>Percentage of Total (percent)</th>
<th>Total mobilized (USD M)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonds</td>
<td>14</td>
<td>14</td>
<td>23,200</td>
<td>25%</td>
<td>29,500</td>
</tr>
<tr>
<td>Guarantees</td>
<td>23</td>
<td>17</td>
<td>36,100</td>
<td>39%</td>
<td>56,700</td>
</tr>
<tr>
<td>Impact Investing Funds**</td>
<td>98</td>
<td>82</td>
<td>5,800</td>
<td>6%</td>
<td>5,900</td>
</tr>
<tr>
<td>Loans</td>
<td>6</td>
<td>4</td>
<td>1,800</td>
<td>2%</td>
<td>2,300</td>
</tr>
<tr>
<td>Microfinance Investment Funds</td>
<td>130</td>
<td>112</td>
<td>9,200</td>
<td>10%</td>
<td>9,300</td>
</tr>
<tr>
<td>Other derivative products</td>
<td>13</td>
<td>8</td>
<td>600</td>
<td>1%</td>
<td>600</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td>284</td>
<td>237</td>
<td>76,700</td>
<td>82%</td>
<td>104,300</td>
</tr>
</tbody>
</table>

### Results, output, and performance based mechanisms

| Advanced Market Commitments | 6 | 4 | 1,100 | 1% | 1,100 |
| Awards and prizes           | 18 | 10 | 300 | 0% | 300 |
| Debt-swaps and buy-downs    | 4 | 4 | 1,400 | 1% | 1,400 |
| Development Impact Bonds    | 5 | 0 | - | 0% | - |
| Performance-based contracts | 16 | 13 | 5,000 | 5% | 5,000 |
| **Subtotal**                | 49 | 31 | 7,800 | 8% | 7,800 |

### Voluntary contributions

| Auctions                    | 2 | 2 | 6,500 | 7% | 6,500 |
| Donations as part of consumer purchases | 6 | 4 | 200 | 0% | 200 |
| **Subtotal**                | 8 | 6 | 6,700 | 7% | 6,700 |

### Compulsory Charges

| Taxes                       | 6 | 4 | 2,400 | 3% | 2,400 |
| **Subtotal**                | 6 | 4 | 2,400 | 3% | 2,400 |

| **Total**                  | 347 | 278 | 93,600 | 100% | 121,200 |

* Of the 347 mechanisms in the database, only 278 mobilized resources between 2000 and 2013. This reflects the emergence of new asset classes such as Development Impact Bonds, which did not mobilize any resources during that period, and new products, such as the DFID Innovation Prizes for Environment and Development which was launched in 2013 and has not been implemented yet.

** We defined the universe of impact investing and microfinance funds based on the decision of managers to register with ImpactBase, a leading database of impact investing funds. Many fund managers elect not to register with ImpactBase, which makes this a conservative estimate of the market size.

Source: Innovative Financing Initiative Database; Dalberg analysis
The innovative finance market is still evolving, with some proven models, some ripe for scaling, and some newer ideas still being tested.

<table>
<thead>
<tr>
<th>Funds mobilized to date</th>
<th>Opportunities for Replication</th>
<th>Proven Models</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;100 million</td>
<td>(100 million to a billion)</td>
<td>(&gt; 1 billion)</td>
</tr>
<tr>
<td>Track record</td>
<td>One or more clear success</td>
<td>In use before 2006</td>
</tr>
<tr>
<td>Little or none</td>
<td>stories since 2006</td>
<td></td>
</tr>
<tr>
<td>Complexity</td>
<td>Structure may be complex, but</td>
<td>Simpler structures or many</td>
</tr>
<tr>
<td>Technically difficult to</td>
<td>there are existing templates</td>
<td>pre-existing templates</td>
</tr>
<tr>
<td>structure</td>
<td></td>
<td></td>
</tr>
<tr>
<td>R&amp;D cost</td>
<td>High R&amp;D cost and lengthy</td>
<td>Relatively low R&amp;D cost and</td>
</tr>
<tr>
<td></td>
<td>development runway</td>
<td>quick to launch</td>
</tr>
<tr>
<td>Stakeholder</td>
<td>Multiple stakeholders</td>
<td>Coordination needed for a few</td>
</tr>
<tr>
<td>coordination</td>
<td>required for success</td>
<td>stakeholders or stakeholders</td>
</tr>
<tr>
<td></td>
<td>across public/private/civil</td>
<td>within only one group</td>
</tr>
<tr>
<td></td>
<td>sectors</td>
<td></td>
</tr>
<tr>
<td>Applicability to multiple sectors, asset classes</td>
<td>Many applications but still limited number demonstrated so far</td>
<td>Has been applied to many sectors and asset classes</td>
</tr>
<tr>
<td>Potentially limited to only certain applications</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Examples</td>
<td>• Product Linked Savings</td>
<td>• AMC (AMC for Pneumococcal)</td>
</tr>
<tr>
<td></td>
<td>Accounts</td>
<td>• Impact Investing Funds (The Global Health Investment Fund)</td>
</tr>
<tr>
<td></td>
<td>• DIBs (Malaria in Mozambique Performance Note)</td>
<td>• Performance-Based Contracts (Mexico PES)</td>
</tr>
<tr>
<td></td>
<td>• AMC (AMC for Pneumococcal)</td>
<td>• Microfinance</td>
</tr>
<tr>
<td></td>
<td>• Impact Investing Funds (The Global Health Investment Fund)</td>
<td>• Bonds (WB Green Bond)</td>
</tr>
<tr>
<td></td>
<td>• Performance-Based Contracts (Mexico PES)</td>
<td>• Guarantees (DCA Guarantees)</td>
</tr>
</tbody>
</table>

Source: Dalberg Analysis
Public and Private Collaboration
Most mechanisms support transfers between the public and private sectors

Private sector participation in innovative financing mechanisms, 2000-2013
Number of mechanisms (x-axis) and amount mobilized, USD million (y-axis) (n=278)

Source: Innovative Financing Initiative Database
About the Innovative Financing Initiative

Working with the Global Development Incubator, the Innovative Finance Initiative aims to enable the growth of bankable investments that mobilize resources for development and increase the efficiency and effectiveness of financial flows. The initiative would be held accountable for specific measures of success, including increasing information and transparency on innovative finance successes and failures, demonstrating scalable models to enable innovative finance (such as guarantee mechanisms or new fund structures), and building a global network of investors and entrepreneurs to expand the sector. By combining private sector approaches to achieving risk-adjusted returns with a philanthropic orientation to producing social impact, the initiative will create and popularize new financial instruments as well as new financial technologies, institutions and markets.

As an initial step, Dalberg (www.dalberg.com), in partnership with Citi Group (www.citi.com) and l’Agence Française de Développement (www.afd.fr), is writing a report that examines ways that private and public sector funders can accelerate the development of innovative finance. The report will be the cornerstone of the larger initiative that mobilizes leading international development organizations to promote and develop specific initiatives. Building on past efforts to describe innovative finance schemes, we will identify common characteristics of different initiatives, assess the market demand for new models, and propose three to five mechanisms that can unlock the sector’s potential.

Identifying new opportunities requires a dialog that uncovers common perspectives and understands the incentives of different actors, especially investors, entrepreneurs, and policy-makers from outside of Europe and the United States. We want to talk with donors who want to create more development effects through their investments, corporations open for new business models in new markets, and financial institutions looking for new opportunities.

If you are interested in being part of the conversation, please contact us at innovativefinance@dalberg.com. We look forward to talking with you.
DR. SERENA GUARNASCHELLI, GENEVA PARTNER

Serena is a Partner in Dalberg’s Geneva office and a leading expert in Dalberg’s global Access to Finance practice, with a focus on impact investing, innovative finance and inclusive business models. She advises investors and donors on strategies and vehicles for investing in emerging markets across agriculture, education, energy, health, and SME finance. She supports companies with the design of inclusive business models and strategies, most recently in insurance, energy and water. Serena also advises investors and development finance institutions on impact assessments at the investment and portfolio levels, and has conducted multiple strategic evaluations of private sector development investments and funds in Africa, Asia and Europe. Prior to Dalberg, Serena was a senior manager at McKinsey & Company. Serena has also worked with Mercy Corps in Darfur, where she built an operational office providing public health and education support to 15,000 internally displaced people. Serena holds a PhD in Social Sciences from Caltech, with a specialization in Mathematics for Finance and Behavioral Economics, and a Laurea in International Economics from Bocconi University.

SAM LAMPERT, GENEVA PROJECT MANAGER

Sam is a Project Manager in Dalberg’s Geneva office. He advises governments and international organizations on aligning business operations with long-term strategy and conducts strategic evaluations of how investments in the private sector support development objectives. Sam advised a leading development bank on how to evaluate tradeoffs within its investment strategy and increase the impact of its investments in financial services, agriculture, and energy while maintaining the bank’s profitability. Sam has also assessed market demand for innovative finance mechanisms and developed a social impact bond for malaria control and prevention. Prior to joining Dalberg, Sam was a manager in the Emerging Markets practice of Deloitte Consulting. His professional experience also includes work as a social science researcher for Harvard University and as a finance associate with Doctors of the World – USA. Sam holds an MBA from INSEAD and a BA with Highest Honors from Emory University. He is fluent in French.