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# **BLENDED FINANCE**

or how to leverage the scaling up of social businesses

What is it? Is it relevant for SDC? Luca Etter, Program Manager, SDC GI

Savings and Credit Forum, March 3, 2016, Bern

#### Blended Finance – what is it?

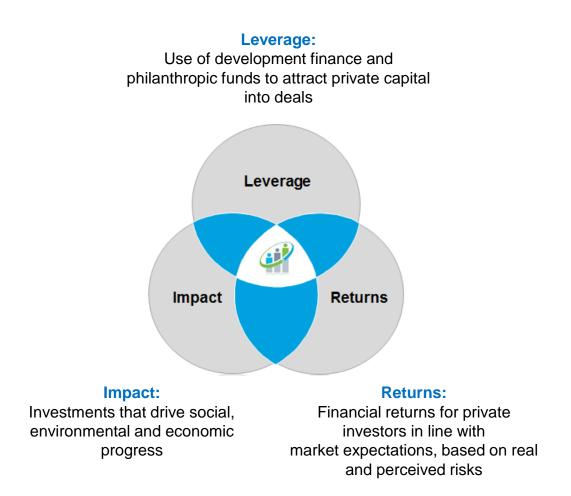
• "...blended finance, [which] combines concessional public finance with non-concessional private finance and expertise from the public and private sector, special-purpose vehicles, non-recourse project financing, risk mitigation instruments and pooled funding structures. Blended finance instruments including public-private partnerships serve to lower investment-specific risks and incentivize additional private sector finance across key development sectors..."

Addis Ababa Action Agenda, Para 48

 "The strategic use of development finance and [/or] philantropic funds to mobilize private capital flows to emerging and frontier markets, resulting in positive results for both investors and communities."

WEF ReDesigning Development Finance Initiative

### Blended Finance – what is it?

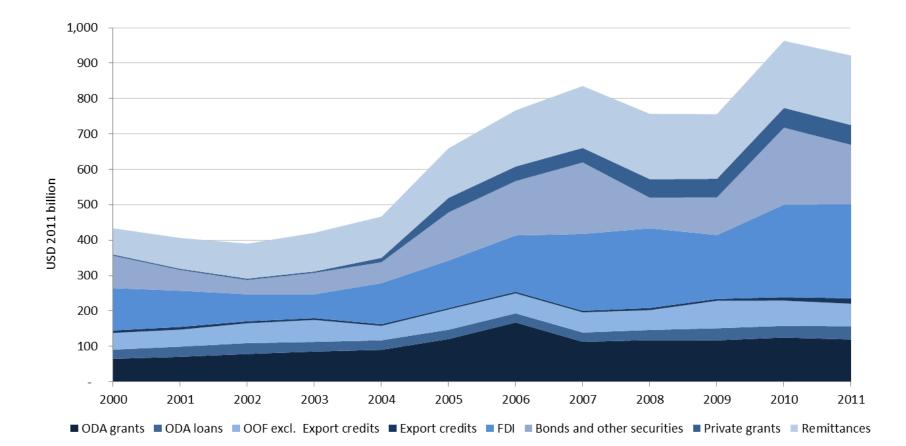


### Blended Finance – what is it not?

- Social Impact Investing does not require concessional public finance; social impact is intended by all investors.
- Development Impact Bonds financing model that shifts incentives and accountability to results, transfers performance risk to the private sector, and increases efficiency in program implementation.
- **PPPs / PPDPs –** may not always be impact driven, concessional public finance not necessarily involved.
- **Splendid Finance** wishful thinking...

All these can be Blended Finance mechanisms, but defining elements (impact, leverage, return) are not the same!

#### Blended Finance – Motivation I



#### **Blended Finance – Motivation II**

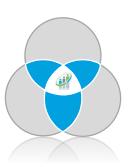


### Blended Finance – Instruments

#### **Mitigating Risks**

Public investors can mitigate risks for the private sector, including:

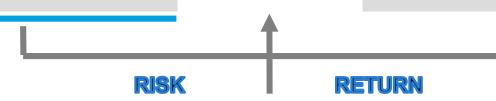
- Improving credit worthiness
- Limiting downside loss exposure
- Insuring against unforeseen market and catastrophic events
- Providing technical assistance and other advisory services
- Eliminating funding shortfalls
- Encouraging necessary risk taking
- Providing support with governments



#### **Managing Returns**

Public investors can also apply mechanisms that enhance returns for the private sector, including:

- Absorbing transaction and project preparation costs
- 'Topping-up' returns by sharing or forgoing any returns to public capital
- Providing incentives for successful performance outcomes
- Providing low cost leverage
- Taking subordinate positions
- Extending or deferring term provisions



## **Blended Finance – Opportunities**

ΠŻ	Preparing	Pioneering	Facilitating	Anchoring	Transitioning
MARKET SEGMENT	High upfront costs; binary risk that a project will not happen	Early-stage projects with high business model risk; high transaction costs	Sectorial or project risks; returns below commercial rates	Macro or sectorial risks; liquidity, refinancing and exit risks	Lack of local markets knowledge and deal pipeline; inefficient markets
PUBLIC SECTOR ROLE	Funds upfront costs and activities reducing uncertainty, creating transparency, and building a pipeline of bankable projects	Little to no return expectations and absorbs costs, reduces business model risk and provides advisory services; can defer rights or enhance private returns	Takes a subordinate position with higher risk or provides low cost leverage to enable private capital to meet their risk-return thresholds	Signaling effect and 'stamp of approval' by achieving 'first- close' or demonstrating viability to 'crowd-in' private funds	Exit mature and sizeable investments that provide a pipeline for commercial actors
<b>DIRECT</b> FUNDING	Grants, Repayable Grants, Highly Flexible debt	Grants, Repayable Grants, Junior Equity, Flexible Debt	Equity, Flexible Debt	Market Rate Debt, Equity	Market Rate Debt, Equity
ORTING	Technical Assistance (Technical/Operational Expertise) – Advisory or preparatory services, assistance, and training to facilitate private investment in high-impact projects and enterprises in order to supplement the capacity of investees and more generally lower the transaction costs				
ANISMS	training to facilitate priva	ate investment in high-imp	pact projects and enterpri		
MECHANISMS	training to facilitate priva investees and more gen Risk Underwriting (C	ate investment in high-imp	oact projects and enterpri on costs - Risk reduction tools tha	ses in order to suppleme	nt the capacity of
MECHANISMS	training to facilitate priva investees and more gen Risk Underwriting (C various forms of risk, eff Market Incentives (R	ate investment in high-imp lerally lower the transaction Capital Preservation) -	act projects and enterpri on costs – Risk reduction tools tha k of capital losses ng/Price Guarantees)	ses in order to supplement t fully or partially protect to - Guarantees of future	nt the capacity of he investor against payments contingent on

Life Cycle of Projects & Enterprises

# Blended Finance – is it for SDC?

Potential Avenues for SDC to engage in Blended Finance:

- Contribute to finance vehicle for social enterprises
- Finance innovation in products and services for the poor through innovation fund
- Leverage investments in financial institutions that serve the poor
- Expand finance instruments to include loans, guarantees, equity investments
- Contribute to policy discussion on global level via multilateral partners (WEF; OECD)

### THANK YOU!

