FAST-Infra

Sustainable Financing Facility (SFF) for National Development Banks

Context

National development banks (NDBs) and other publicly owned financial institutions based in emerging and developing countries (e.g., TSB, FDN, IDCOL, DBSA, BNDES, etc.) are well placed to provide financing to support the transition to a low carbon economy in their domestic markets. Indeed, NDBs and other FIs are an important source of financing for greenfield infrastructure projects. In many developing countries with shallow capital markets, they are the only providers of long term capital. However, in many cases, NDBs lack regular access to international capital markets. We are therefore proposing to set up a facility that would directly finance eligible NDBs and other local financial institutions for on-lending to sustainable infra projects in their domestic market. This could be an effective solution to channel more funds to develop sustainable infrastructure.

The proposal

The proposal is to establish a Sustainable Financing Facility (SFF) for National Development Banks and other FIs, i.e., a special purpose vehicle that would supply funds to eligible NDBs and local institutions for on-lending to sustainable infrastructure projects. Eventually, the facility would provide funding to a well-diversified portfolio of NDBs/FIs from emerging markets and would raise capital in global financial markets. [TBD: The facility could also include a technical assistance facility to support capacity building of NDBs. The technical assistance would focus on project expertise.]

In a post Covid-19 world, the suggested vehicle could help increase available financing of EM sustainable infrastructure to “build back better”. Traditional providers of long-term capital to infrastructure projects, such as private equity and sovereign wealth funds and other institutional investors, face various issues and risks including challenging regulatory and tax environments, weak exit opportunities, small scale, political risk, etc. Instead of project-level risks, the SFF will be designed to take NDB/FI risks, therefore mitigating some of these risks. All funding enabled by the facility will be earmarked to financing sustainable infrastructure projects that are aligned with the label created by FAST-Infra. The facility would help crowd in private capital to indirectly finance the sustainable infrastructure.

The structure

The first iteration of the vehicle is less likely to be a capital markets funding vehicle given that it will be challenging to gather a diversified enough portfolio of NDB/FI borrowers and a sufficient level of first loss to achieve a high rating on the bonds. Initially, the proposed approach would be for a Green Climate Fund / DFI funding tool (possibly with participation from commercial banks), which would then move on to become a capital markets issuer as it builds a wider borrower base amongst NDBs and other FIs (possibly a group of GCF Accredited Entities).
Thus, a three stage build out approach is suggested:

1) DFI / GCF led financing to get an initial critical mass before commercial banks get involved
2) Warehouse financing from commercial banks to build up to a capital markets offering – would expand funding capacity of SFF by complementing the DFIs
3) Capital markets offering – refinance commercial banks / DFIs and allow them to redeploy capital

The end state SFF investment portfolio – in secondaries as well as in primaries – would have to conform to predetermined issuer/geographic diversification as well as absolute/weighted average ratings thresholds.

**Main Stakeholders (throughout various stages)**

- An MDB will originate the loans and subsequently transfer them to an SPV that will continue to be serviced by the MDB.
- Senior lenders: banks, insurance companies
- Mezzanine lenders: MDBs / DFIs.
- First loss investors: GCF, philanthropic and other catalytic capital.

To the extent the SFF’s lending portfolio becomes more diversified over time, we would expect it to tap the capital markets and access a much broader lender base.