Capital Mobilization Roadmap

Discussion Draft

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CLIMATE POLICY INITIATIVE

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While this paper is based on the discussions between participants during the 9th meeting of the San Giorgio Group, CPI takes full responsibility for all assumptions made in its recapping of these discussions. Comments are not attributed as discussions take place under Chatham House Rules.

ABOUT CLIMATE POLICY INITIATIVE

CPI is an analysis and advisory organization with deep expertise in finance and policy. Our mission is to help governments, businesses, and financial institutions drive economic growth while addressing climate change. CPI has six offices around the world in Brazil, India, Indonesia, the United Kingdom, and the United States.

ABOUT SAN GIORGIO GROUP

The San Giorgio Group convenes climate finance leaders who are actively engaged in accelerating the transition to more sustainable, lower-emission economies. Bringing together key stakeholders across the public and private sectors, the Group leverages diverse viewpoints and frank discussion to assess and prioritize critical issues that require our collective effort to address in the near term.

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RELATED CPI WORKS

An Innovative IFI Operating Model for the 21st Century

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INTRODUCTION

This roadmap seeks to build on the discussion paper, An Innovative IFI Operating Model for the 21st Century, by describing pathways for implementing some of the most promising risk-sharing instruments and business models described briefly in the paper, with a focus on mobilizing private capital. This is not meant to be a comprehensive document. Rather, it will isolate 4 high-impact instruments and initiatives that address:

- **Credit risk** with increased and purposeful guarantees
- **Currency risk** at scale by creating markets, with more funding to existing initiatives, guarantees, and blending to improve affordability
- **Development risk** by scaling project development business models and tailoring models to attract earlier investment
- **Mis-aligned MDB incentives** by standardizing mobilization targets, underwriting criteria, and asset classes

These reforms are most appropriate for the private sector arms of MDBs as well as DFIs that directly lend to the private sector, municipalities, and via financial intermediaries. While some are well established and in need of scaling, others are relatively undeveloped and not guaranteed to work, but do have significant potential. Our focus is on short run reduction of risk and cost of capital, to accelerate private investments that target both climate and broader development priorities. Many of these initiatives will facilitate capital mobilization for both infrastructure development and to support businesses where climate impacts are crucial. In order to focus on the above opportunities, and given the excellent work done by many in the field, we are not addressing sovereign lending, policy reform technical assistance, and business models related to those. This is not to say that they are not important – they are arguably more important in the long run for private capital mobilization by building better enabling environments.

As this roadmap developed, we encountered a wide variety of key operational questions. As such, the roadmap outlines questions that need to be answered for each instrument or initiative and suggests key events and convenings to agree on either basic frameworks or more detailed approaches for scale up. Another key aspect is determining both the decision makers and the supporting actors for each initiative or instrument, and determining who needs to be included in the discussions, in what capacity, and at what stage. While 2024 political milestones like the Brazil G20 meetings and the 80th Bretton Woods Anniversary will be critical for shaping conversation and supporting momentum for fundamental long-term reforms, they are not included as their political context at the moment is too uncertain.

We believe that these initiatives are achievable in the next 18-24 months based on existing track records and consultations with key stakeholders. However, it will require significant capacity and unparalleled collaboration among public and private finance institutions, shareholders, advocacy and civil society organizations, donors, philanthropies, and external experts. The goals and political milestones listed here are intended to be picked up by MDBs, government shareholders, developing country clients, and advocacy groups that are best situated to make concrete progress in these areas, with CPI and many other field builders, as well as private sector stakeholders, providing technical expertise and helping to connect relevant initiatives.

This is a draft for consultation. CPI welcomes feedback on this roadmap to framework@cpiglobal.org.

1. ADDRESS CREDIT RISK WITH INCREASED AND PURPOSEFUL GUARANTEES

SHORT TERM REFORM

A credit guarantee facility with standardized contracts and agreed criteria to accelerate both the creation of the guarantee and the payment in case of default, and requiring only the estimated default rate to be used as capital to seed the guarantees. The facility could be jointly capitalized by MDBs.

What it builds on and existing impact: There are a number of successful institutions with a track record of guarantee issuance, such as PIDG's GuarantCo, MIGA, and SIDA. Green Guarantee Company and Greenmap are recent initiatives.
Decision makers: MDBs to provide capital for guarantees at expected default rate.
Who else needs to support: Donors could provide grants for set-up costs and fees, project sponsors (e.g., developers, municipalities).
Impact potential: Mobilization potential at least 6x lending[1], some papers suggest 25x or more[2]. A USD 10 bn facility could mobilize USD 25 -100 bn. Standardizing and coordinating guarantees across institutions and across countries would lower the transaction costs.
Key questions:

- Where will this facility be housed? Would it be more straightforward to develop it through an increase in MIGA's range of risks covered (beyond political risks), or does it need to be operationalized outside of MIGA and/or the MDBs to ringfence?
- Can existing products, including those offered by MIGA, be repurposed or enhanced to create interim synthetic solutions?
- Is it possible for MDBs to capitalize the guarantee facility directly, similar to how they capitalized TCX at the outset?
- How would the facility be capitalized?
    - Can a facility outside the MDBs, or within MIGA, use MDBs' callable capital as a backing for some of the guarantees to increase liquidity?
    - Is donor capital necessary for facility development and launch? Should donor capital be used to provide guarantees directly to PDBs in emerging markets and developing economies? Are there any early lessons learned from the IF-CAP efforts to provide guarantees to ADB?

[1] Blended Finance Taskforce, Better Guarantees Better Finance Consultation Paper, 2023, Exhibit 5
[2] CPI discussion paper, June 2023, Cost of Capital for Renewable Energy in Developing Economies

- What is the default rate on a global level that should be used in instrument calculations? How do geographic and technology variations need to be considered?

LONG TERM REFORM

Change capital allocation rules to incentivize guarantees under existing structures:

1) MDB internal risk weightings,
2) Overseas Development Assistance accounting rules, and
3) clarification of key bank regulatory regimes vis-à-vis participating in co-financing with MDBs and other public finance institutions.

What it builds on and existing impact: Current MDB and ODA rules require capital to be set aside at higher-than-expected default rates, typically indistinguishable from a loan of the same value. Changing the accounting rules would allow for guarantees to be based on estimated default rates, rather than requiring the full amount of the guarantee to be held, which could allow for guarantees to be used over loans. Commercial bank regulations are often silent on how to treat public risk sharing in capital adequacy and therefore banks take a risk-averse stance. Clarifying capital adequacy rules when investing alongside MDBs and other public finance institutions could free up commercial capital.
Decision makers: MDB shareholders, financial sector regulators, MDB leadership, OECD Development Assistance Committee.
Who else needs to support: G7, Lower-income and Middle-income country governments, developing country public and private financial institutions and project developers.
Key questions:

- Can an MDB use a probabilistic approach (like MIGA does) to guarantees and estimated default rates in house, or do guarantees need to be ringfenced?
- How much capital could be freed by changing the ODA accounting rules?
- How can increased guarantees be complemented by partnerships with domestic and international finance institutions and project sponsors to make sure they are utilized?

CREDIT RISK ROADMAP

	Summit for a New Financial Pact	Africa Climate Action Summit	Finance In Common Summit	India G20 Summit	2023 Annual Meetings	COP28	2024 Spring Meetings	2024 Annual Meetings
	June	September	September	September	October	November	April	October
Credit guarantee facility	Convene with MDBs, PDBs, and V20 governments to discuss basic facility organization	Feedback on guarantee potential and design in Africa	Convene interested PDBs to agree on basic needs and best practices for guarantee instruments	MDB Expert Group highlights need for more guarantees as a short- & medium-term solution	Facility announced with support of two or more MDBs Convening to agree on basic facility organization Expanded financing for PIDG announced	Donors announced for facility set up costs Convening to stress test and discuss facility organization with developed and developing country governments, MDBs, PDBs, and private sector stakeholders	Update on facility & mention of importance Convening to fully flesh out and agree upon detailed facility organization	Credit guarantee facility launched
New capital allocation rules	Convene with MDBs and PDBs to discuss changes to guarantee risk weightings	Call for changes to the guarantee system to increase climate finance to EMDEs	Convene with MDBs and PDBs to agree on basic tenets of guarantee risk weighting changes		MDB risk weighting evaluation announced ODA rules & regulatory clarifications included in reform discussions	Convening to discuss MDB risk weighting changes, effects on global climate finance Convening to agree on basic ODA rule and regulatory clarifications changes	ODA rules & regulatory clarifications included in direct discussions with WB shareholders as necessary change Convening with governments, MDBs, and PDBs to agree upon final MDB risk weighting changes	MDB risk weighting launched ODA rules changes announced Convening with governments, MDBs, PDBs, and private sector to discuss regulatory clarifications

2. ADDRESS CURRENCY RISK WITH MORE FUNDING TO EXISTING INITIATIVES, GUARANTEES, AND GREATER USE OF LOCAL CURRENCY

SHORT TERM REFORM

1) Scale up the market creation capacity of TCX by adding capital and increasing the scale and scope of its blending program to improve affordability, and
2) Explore other proposals such as Just Environment Transition - Foreign exchange Investment Trust ("JET-FIT") to use SDR-backed guarantees to further reduce hedging costs in JETP countries.

What it builds on and existing impact: TCX has created long-term price hedges for a wide range of currencies and can scale significantly with additional investment, including concessional investment that allows below-risk rates.[3] An additional $5b investment would allow TCX to reach $60b in hedging capacity by 2025. The JET-FIT concept seeks to leverage IMF's capabilities to guarantee SDR exchange rates in the long run.
Decision makers: MDB leadership & shareholders, TCX leadership, Government Investors, IMF, JETP countries.
Who else needs to support: Domestic and commercial banks, and institutional investors.
Key questions:

- How can affordability of currency hedging be improved while supporting the creation of markets?
- What are the capacity needs of countries, for example for better currency risk management?
- Is the JET-FIT proposal technically viable, including its assumptions on short and long term risk premia?
- What is the role of IMF?

LONG TERM REFORM

Increase use of guarantees and capacity for local currency lending as well as MDB direct currency lending

[3] For example, the EU Market Creation Facility – Pricing Component program blends capital to increase affordability. https://www.tcxfund.com/projects-initiatives/eu-market-creation-pricing-facility/#:~:text=TCX%20has%20established%20a%20program,local%20currency%20in%20development%20finance.

What it builds on and existing impact: One example of an initiative under development is the Rwanda Green Investment Facility, spearheaded by FONERWA in partnership with other local DFIs, which proposes a Green Guarantee Facility to reduce interest rates and encourage the local currency market by guaranteeing local financial institution green lending.
Decision makers: DFIs, MDBs, EMDE country governments, donor countries.
Who else needs to support: Local financial institutions, IMF.
Key questions:

- Would guarantee funds depend on local currency being available through local banks? What is the role of intermediary lending between MDBs and PDBs?
- What are ways MDBs and local governments can support efforts to increase direct loans in local currencies?
- What would be the optimal way to approach direct currency lending by MDBs? What are the implications for others, e.g., credit rating agencies?
- What are the capacity needs of countries, for example for better risk management?
- What is the role of IMF?

CURRENCY RISK ROADMAP

	Summit for a New Financial Pact	Africa Climate Action Summit	Finance In Common Summit	India G20 Summit	2023 Annual Meetings	COP28	2024 Spring Meetings	2024 Annual Meetings
	June	**September**	**September**	**September**	**October**	**November**	**April**	**October**
TCX expansion & JET FIT	Convene TCX, TCX investors, and borrower representatives to discuss potential changes and expansion	Agree on basic tenets of foreign exchange risks and climate finance impacts to gather support for short- and medium-term FX and local currency solutions	PDB discussion on how to best support TCX expansion and local currency lending and guarantees	Expert working group supports TCX expansion as a short-term solution to currency risks and assesses potential for SDR exchange rate guarantees	MDBs announce additional investments in TCX; IMF issues statement on SDR guarantees	TCX announces new government capital that will allow below risk rates to more climate projects; JET FIT program announced	TCX releases impact report for climate investments since COP28	JET FIT facility launched
Local currency guarantees and capacity for local lending	Convene developing country governments, PDBs, and MDBs to discuss using guarantees to hedge local currency lending and increased local currency lending from MDBs			Expert working group recommends further work on the use of local currency guarantees and recommends local currency lending.	Convening to agree on details of local currency guarantee instruments Convening to discuss direct local currency lending from MDBs	Pilot guarantee instrument announced with support of 1 MDB and 1 developing country government.	Pilot facility launched Announcement on direct currency lending	Pilot facility replicated for 2 or more additional EMDE countries Launch of direct currency lending instruments

3. ADDRESS DEVELOPMENT RISK BY SCALING PROJECT DEVELOPMENT MODELS AND TAILORING MODELS TO ATTRACT EARLIER INVESTMENT

SHORT TERM REFORM

Increase funding for existing project development models and platforms to scale proven, working programs and increase the amount of bankable, investment-ready projects in EMDEs. Improve efficiency of existing models through standardization and data sharing.

What it builds on and existing impact: There is a strong track record of existing project development facilities, funds, and advisory services, including the Global Infrastructure Facility (GIF), regional clean energy facilities like Southeast Asia Clean Energy Facility (SEACEF), now being replicated in other geographies by Allied Climate Partners, Gap Fund, and Climate Investor One's Development Fund. The SOURCE platform provides standardized infrastructure project preparation management software to countries. Fast-INFRA provides a sustainable infrastructure label towards creation of a standardized asset class.
Decision makers: Donors, philanthropies, MDBs/DFIs.
Who else needs to support: Private sector financial institutions and developing country-based project developers.
Impact potential: Project development is typically 2-5% of total project cost on average, and on the higher end of this range in EMDEs, so leverage can be 20-50x early-stage investments.
Key questions:

- How much funding could potentially be deployed by existing facilities?
    - How much concessional funding will be required to scale up the existing models?
    - What limits the availability of grant funding for project development?

- Which communities, regions, or technologies are underserved by project development facilities? Could the existing organizations expand to these areas?
- What improvements on ease of access for both project developers and private investors will reduce frictions in the system?
- How can PPFs better align with investors, and what platforms exist to facilitate those conversations?
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- How can MDBs invest directly in the GIF or other project development facilities, similar to how they invest in TCX or other equity platforms?

LONG TERM REFORM

Improve impact and dramatically scale up MDB and DFI support for project development

What it builds on and existing impact: MDBs currently fund some early stage project preparation activities, mostly via grants and technical assistance. More sustainable financing models need to be adopted.
Decision makers: Donors, Philanthropies, MDBs, shareholders, borrowers.
Who else needs to support: Domestic and international public and private sector financial institutions
Impact potential: Project development models with returnable grants and investments, and lower transaction costs, can reduce reliance on grants, allowing for longer term sustainability and better targeting of scarce grant capital. Early investment in project development can also create significant bankable assets for private sector investment.
Key questions:

- How can the MDBs support broader coordination and increased effectiveness of their existing project preparation services?
- What is the increase in MDB risk by investing in project development directly, rather than relying on grants, and how can that be mitigated by the capital adequacy framework reforms?
- What kinds of funds (grant, concessional equity/debt, commercial) are needed for which technologies in which geographies?
- How can we better coordinate and construct a continuum of support between pure grant (or returnable grant) models and investment or returnable capital financing models, based on differing development risks?

DEVELOPMENT RISK ROADMAP

	Summit for a New Financial Pact	Africa Climate Action Summit	Finance In Common Summit	India G20 Summit	2023 Annual Meetings	COP28	2024 Spring Meetings	2024 Annual Meetings
	June	September	September	September	October	November	April	October
Scaling existing project preparation models	Convening with existing project development models to share best practices	Collective call from group of African nations for MDBs, donors, and private capital to support project pipelines	Convening with PDBs to discuss early domestic financing in PPFs and finance accessibility challenges Existing project development models to announce plans for increased cooperation and data sharing		Project development facility success stories shared with MDB shareholders	Funding announcements from philanthropies and donors, MDBs, and private funds to scale up existing models Convening of project development facilities and PDBs to discuss access to financing improvements		
MDB project development reforms	MDBs discuss potential for increased project development investments		Project development facilities and PDBs discuss improved collaboration and how PDBs can better support project development	Expert working group issues recommendations on MDB project development investment	Announcement of initial MDB commitments to invest in project development		MDBs make pilot investments in project development	Announcement of MDB early investments in project development facilities and project preparation

4. ADDRESS MIS-ALIGNED MDB INCENTIVES BY STANDARDIZING MOBILIZATION TARGETS, UNDERWRITING CRITERIA, AND ASSET CLASSES

SHORT TERM REFORM

Align staff performance and institutional targets to better incentivize private sector mobilization and total investment volumes, rather than institutional volumes.

What it builds on & existing impact: In 2021, MDBs climate finance mobilization for LMICs was only $13B against $51B of climate finance. $10B of the $51B was for private borrowers, but there is no reporting on private capital mobilization per borrower type (e.g., public vs private).
Decision makers: MDB leadership & shareholders.
Who else needs to support: MDB operations.
Key questions:

- What are the right metrics for measuring effective mobilization and real economy impacts?
- Should they be included in the KPIs for executive compensation?
- How can the KPIs be standardized across the MDBs in a manner that accounts for regional differences?
- Can inter-MDB cooperation regarding mobilization be included as a KPI?
- What is the appropriate level of reporting?

LONG TERM REFORM

Standardize underwriting criteria and asset classes to allow "originate-to-distribute" models to be implemented.

Purpose: Originate-to-distribute models could crowd in significant private sector investment upstream and better leverage MDB capital.

What it builds on and existing impact: A relatively new idea that builds on the success of MDBs being able to source new deals and de-risk transactions (particularly for private financing) and the potential for these MDBs to effectively bundle diversified projects into attractive portfolios through securitization or other similar means by using pre-agreed underwriting criteria.
Decision makers: MDB leadership and shareholders.
Who else needs to support: Private sector financial institutions.
Key questions:

- How should originate-to-distribute models adjust to different MDB types, particularly between sovereign and private MDB arms?
- How can the model be standardized to facilitate ease of use?
- How will the securitization of the loans impact the financial models of the MDBs themselves?
- What is the market appetite for such securitizations, and does it change by region?

MDB INCENTIVE ROADMAP

	Summit for a New Financial Pact	Africa Climate Action Summit	Finance In Common Summit	India G20 Summit	2023 Annual Meetings	COP28	2024 Spring Meetings	2024 Annual Meetings
	June	September	September	September	October	November	April	October
Mobilization targets	Convening of MDBs to agree on need for and basic outline of new KPIs	Call for MDBs to create standardized KPIs that focus on capital mobilization and support EMDE SDG goals	Convening of PDBs to discuss KPI standardization	MDB expert group makes a statement in support of standardized, mobilization-focused KPIs	Announcement of new KPIs, promise to implement by July 1 (start of new FY)	Convening of MDBs, donor governments, and CSOs to agree upon new KPI framework	Final KPIs announced, along with approach to measure and report progress against KPIs	Initial KPI results shared
Underwriting criteria and asset classes	Convening of high-level experts to discuss "originate-to-distribute" idea and agree on basic framework		Convening of MDBs and financial actors to discuss changes needed to the system to broadly support an "originate-to-distribute" model	MDB expert group calls for MDBs to cooperate on data sharing and standardization of criteria	Underwriting criteria and asset classes discussed as part of reform package and with shareholders Coordinated MDB pilot of originate-to-distribute model announced at Marrakesh	Private sector institutions state support for "originate-to-distribute" model with capital estimates	MDB shareholders express support for "originate-to-distribute" Announcement of underwriting criteria and asset class evaluation and standardization	Full scale implementation announced for July 1, 2025, in line with new fiscal year

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