Inter-Agency and Expert Group on Sustainable Development Goal Indicators
Working Group on Measurement of Development Support

Research note: Mobilization of private finance for developing countries by official bodies

July 2020

General introduction

The Working Group is tasked to suggest an indicator or indicators to measure progress against SDG Target 17.3, "Mobilize additional financial resources for developing countries from multiple sources". This Target is part of the "Finance" section of Goal 17. It is preceded by Target 17.1 to "Strengthen domestic resource mobilization" and Target 17.2 on the fulfillment of donors' official development assistance commitments.

In addition to Targets 17.1 and 17.3, the concept of "mobilization" is also used in SDG Targets 1.a, 13.a, and 15.a. Taking all its uses into account, it is clear that mobilization in an SDG context can be done by different actors in relation to a wide variety of possible sources of finance.

However, this note focuses on one particular type of mobilization, viz. private finance mobilized by multilateral development banks (MDBs), bilateral development finance institutions (DFIs), and other official institutions in developed countries. The MDBs and DFIs in particular have a special interest in identifying the volume of such funds, since a significant part of their operations is directed to catalyzing and supporting developmental activities on the margin of commercial viability. The volume of private funds mobilized towards these ends is thus an important measure of the success of their activities, and may give some indication of the scale of their potential developmental impacts.

Two methods of estimating private finance mobilized by these bodies are available: one developed by the OECD, and one by MDBs. These are briefly described below, with references to facilitate further research. A final section then attempts to draw out from the analysis some questions the Group will need to answer to settle its position on this issue.

The note does not address other actors' mobilization of private flows. The most important of these other actors are developing countries themselves, which mobilize private finance through bond issues[1], tax incentives, concessional and non-concessional borrowing and lending, co-investments, concessions to investors to operate and collect revenue from their investments, and other measures. Nor does the note consider private funds raised by private actors, such as NGOs' fundraising activities, or foundations' seed funding, prizes or other incentives towards research by private firms into crops, vaccines or technologies for developing countries. Finally, it does not explore official actors' mobilization of non-market private finance, such as government tax incentives or matching schemes for private contributions to developmental NGOs.

Some mobilized private finance is also blended finance, defined in the Addis Ababa Action Agenda as combining "concessional public finance with non-concessional private finance and expertise from the public and private sector". For more information on the uses and purposes of concessional public resources in blended finance, see the discussion in the latest Financing for Sustainable Development Report (United Nations, 2020), p. 90f.

[1] Note, however, that bond issues supported by MDBs/DFIs are covered under the MDB method.

OECD and MDB approaches to measuring mobilization of private flows

Key references:

OECD: *Amounts Mobilised from the Private Sector by Official Development Finance Interventions* *(2017 paper on methodology, with 2012-15 data)*
Amounts mobilised from the private sector by development finance interventions *(2020 presentation of 2017-18 data)*
DAC methodologies for measuring the amounts mobilised from the private sector by official development finance interventions *(2020 draft; includes new methodology on project finance special purpose vehicles)*
Measuring Mobilisation: Briefing on efforts to harmonise OECD and MDB measurement methodologies *(2018 paper)*

MDBs:
Reference Guide *on how MDBs and European Development Finance Institutions calculate and jointly report private investment mobilization (2018 document hosted by World Bank)*
Mobilization of Private Finance by Multilateral Development Banks and Development Finance Institutions *(2019 document hosted by IFC)*

Both the OECD and the MDBs (joined by many DFIs) have developed methodologies for estimating, generally at the commitment stage of an activity, private market finance mobilized for developing countries.[2]

Each of these two methodologies is based on rationales which link specific interventions to private financing flows, and each is able to produce estimates both at official agency level and at the level of the resultant private receipts by individual developing countries. Each has commented on the methodology of the other and reported efforts to harmonize their methodologies. However, the sources above indicate that wide gaps remain between the concepts, methods and results of the two approaches. Below is a brief comparison, focusing on elements of the methodologies that may be especially relevant to the Group's task.

Causal linkage between official institution intervention and private flow

The OECD method proceeds by instrument. For each instrument, a causal link is established on the basis of a "key assumption". For example, in the case of guarantees, "The implicit assumption is that the private investor would not have provided the loan, equity or other finance without the official guarantee." In the case of syndicated loans, "The implicit assumption is that the private investor would not have provided the loan without the official sector involvement as an arranger or as a participant." Thus the OECD method establishes causality based on an assessment of the essential nature of the instruments it covers, which in its view all have a "direct mobilization effect".

The MDB method has two levels of measurement, only one of which – "private direct mobilization" (PDM) – requires the demonstration of a causal link. PDM is defined as "financing from a private entity on commercial terms due to the active and direct involvement of a MDB leading to commitment." The MDB must specifically establish the "due to" based on "evidence of active and direct involvement" which may "include mandate letters, fees linked to financial commitment or other validated or auditable evidence of a MDB's active and direct role leading to commitment of other private financiers."

The MDBs' second level of measurement, which does not require demonstration of a causal link, is called "private indirect mobilization" (PIM), defined as "financing from private entities provided in

[2] The MDB method also estimates the (generally higher) volume of private market flows mobilized for high-income countries.

connection with a specific activity for which an MDB is providing financing, where no MDB is playing an active or direct role that leads to the commitment of the private entity's finance."

PDM and PIM are mutually exclusive, and may therefore be added together to give a figure for total mobilization. In some cases, the same financial flow can be counted as either PDM or PIM, depending on whether the MDB has a verifiable active and direct role in mobilizing the private financier.

<u>Transactions covered</u>

The OECD's latest (2020) draft methodology covers guarantees, syndicated loans, shares in collective investment vehicles, direct investment in companies, credit lines, simple co-financing arrangements and project finance schemes. OECD/DAC statistics focus on long-term flows (those with original maturities over 1 year).

The MDBs' method covers guarantees, loans, equities, Islamic finance, short-term finance (including but not limited to trade finance), unfunded risk transfers (URT), client bond issuance (where the MDB supports the issue of a bond purchased by private entities) and direct transaction support ("advisory services and related assistance to a client where these services are linked to the procurement of funds for a specific activity").

Without detailed investigation, it is difficult to map these two coverages precisely with one another, although it would seem likely that the OECD's method would not cover most if not all short-term finance, URT, bond issuance and direct transaction support. On the other hand, concerning short-term flows, it is worth noting that both ODA and FDI, included in the current 17.3.1, are long-term flows.

<u>Attribution of shares of mobilised amounts among individual institutions</u>

There are important differences between the methods used by the OECD and the MDBs to apportion shares of mobilized among agencies when more than one is involved. For example, for syndicated loans, the OECD attributes 50% of the mobilized private funds to the official arranger, and 50% to all other official participants, pro-rata to their respective financing shares in the syndication. For shares in collective investment vehicles, 50% of mobilized amounts are attributed to each official participant in the riskiest tranche of the CIV equally, with the remaining 50% attributed to all official investors, but this time pro-rata to their shares and regardless of the level of risk.

The MDB approach only attributes private flows mobilized to the MDBs/DFIs involved, and does not attribute anything to other public investors. It also differentiates attribution of private flows by reference to the MDB/DFI's role in the transaction, rather than to the risk tranche of its intervention.

<u>Issues with attributing flows to source countries</u>

Regardless of which of the two methodologies is preferred, some issues would need to be resolved if the Group were to recommend that data should be shown for source countries as well as destination countries. In this respect, there would appear to be two possibilities: attributing the flow based on the country of the mobilizing institution, or attributing it based on the source country of the private flow mobilized.

Consider first the possibility of attributing flows based on the country of the mobilizing institution. A difficulty here is that only DFIs and other national institutions, and not MDBs, are country-based, and therefore only the private flows mobilized by them are directly attributable to countries. These account for about 35% of the flows reported by the OECD method and about 10% of the flows reported by the MDB method (which does not permit attribution to bilateral official bodies other than DFIs). The remaining majority of MDB flows could only be attributed to source countries by applying a coefficient, perhaps based on the share of each developed country in the MDBs' capital base.

Consider next the possibility of attributing the private flows according to the country of origin of the flows. The OECD's 2017 paper referenced above reported that 44% of private funds mobilized in 2012-15 came from OECD or other high-income countries, while 27% came from developing countries, with the remaining 29% having a multiple or unspecified origin. If a "country of origin of flow" method were chosen, the Group would presumably need to exclude the private flows already present in developing countries before being mobilized. This would considerably reduce the amount reportable at the level of developing countries' receipts of mobilized private funds.

*

The foregoing has focused on issues particularly relevant to the Group's task, without attempting to rehearse all aspects of the OECD and MDB methodologies. Both of them are complex, and a full analysis of their differences in theory and practice is beyond the scope of this note. However, it may be useful to note that the OECD method estimated $48.4 billion as directly mobilized in 2018.[3] For the same year, the MDB method estimated $20.2 billion in direct mobilization and $49.2 billion in indirect mobilization, for a total of $69.4 billion – counting long-term finance for developing countries only.

It is also worth noting that these amounts – which represent new funds committed, not net flows in the year concerned – represent only a small fraction of total private finance to developing countries. For 2018, the World Bank estimates that FDI alone to these countries totaled $609 billion *net*, i.e. after deduction for disinvestment. While this figure would include South-South flows, it does not include portfolio investment, bond purchases or commercial bank and other private lending. In 2019 the Institute of International Finance estimated that 2018 non-resident capital inflows into emerging economies totaled $1.14 trillion.

Summary of issues for the Working Group

Perhaps the key question for the Group is whether, in the light of the above considerations, it wishes to limit the consideration of private market flows in a new indicator 17.3.1 to those mobilized by MDBs, DFIs and other official bodies in developed countries.

If the answer is yes, then the Group may select one of the two existing methodologies described above, and then make some further necessary specifications, including:

(a) Whether private flows mobilized for developing countries should or should not include private finance already present in developing countries before it is mobilized
(b) Whether figures should be produced for developing country inflows only, or also for developed countries' outflows
(c) If figures are to be reported for developed country outflows, whether the country attribution should be based on the location of mobilizing agency or the source country of the private flows
(d) If the source country attribution is based on the location of the mobilizing agency, whether and how MDBs' mobilization should be attributed to developed countries (for example, by pro-rating the mobilized amounts by the share of developed countries in each MDB's capital)
(e) If the source country attribution is based on the location of the mobilized private flows, whether it is satisfied that sufficient information can be found on this location (this may necessitate inquiries of the OECD or MDBs as appropriate)

---

[3] Note that, in its 2020 presentation referenced above, the OECD reported $37.8 billion of mobilized private finance for 2017, compared with $40 billion reported in its Key Findings from the 2019 TOSSD Data Survey. The latter document explains that the Survey "prompted efforts to identify additional blended finance operations".

(f) Whether the commitment basis of the data on mobilized amounts means that other components of the new indicator 17.3.1 must also be on a commitment basis, or whether the indicator can be a mixture of commitments in a given year and (gross or net) disbursements in the same year
(g) Whether any discount needs to be applied to commitment figures, or to other figures reported on a "Board approval" basis, to allow for possible non-fulfillment of funding agreements.
(h) Whether the mobilized private amounts would be shown as part of a more inclusive new indicator 17.3.1, or as a separate official indicator in addition to 17.3.1 and the current 17.3.2 on remittances.

If the answer is no, then the Group might still wish to present amounts mobilized by MDBs/DFIs as a "memorandum item", meaning that the data series would be available on the UN SDG database without being part of the official SDG indicator list. In this case, questions (d), (h) and possibly (e) above would not arise; nor would they arise if no source country attribution were made. If memo item reporting were agreed, it might also be possible for the database to present both the OECD and MDB data series.

Again if the answer is no, the Group must decide what alternative coverage of private flows it wishes to recommend for indicator 17.3.1. In this case, the Group would presumably wish to review private flows by category – e.g. FDI, portfolio investment, bank and non-bank lending, bond purchases, private grants – to decide which to include, noting that FDI is the only private flow included in the current 17.3.1.