OECD

OECD DAC BLENDED FINANCE PRINCIPLES

for Unlocking Commercial Finance for the Sustainable Development Goals

« Blended finance will contribute to faster economic growth, but to achieve this it is vital to get donors into alignment. »

MARTIN WOLF, CHIEF ECONOMICS COMMENTATOR, FINANCIAL TIMES

« The private sector recognises that donors need an effective framework in order to take blended finance forward to the next level, these Principles provide the step in that direction, which now needs to be taken. »

JULIA PRESCOT, HEAD OF STRATEGY, MERIDIAM

« The OECD DAC Principles are another important step forward to align the international community, and especially, the key development participants, around mobilizing the funding that can help deliver the SDGs. »

H.E. LUHUT PANJAITAN, COORDINATING MINISTER FOR MARITIME AFFAIRS, REPUBLIC OF INDONESIA

FOREWORD

CHARLOTTE PETRI GORNITZKA,
CHAIR OF THE OECD'S DEVELOPMENT ASSISTANCE COMMITTEE

JORGE MOREIRA DA SILVA,
DIRECTOR OF THE DEVELOPMENT CO-OPERATION DIRECTORATE (DCD)

With 2030 fast approaching, financing the Sustainable Development Goals (SDGs) is one of the starkest challenges faced by providers of development co-operation. Blended finance is the strategic use of development finance for the mobilisation of additional finance towards the SDGs in developing countries. It is a growing practice, as 17 of the 30 DAC members already carry out blended finance activities and more donors are looking to enter this field. Official development assistance (ODA) plays a fundamental role, having unlocked an additional USD 81 billion in private finance for development over three years based on recent OECD analysis.

While existing blended finance initiatives aim to bring in much-needed private finance, their strategies, objectives and approaches vary greatly. Some governments have been undertaking blending activities for a considerable amount of time, while others are just beginning to use such instruments. Some may be particularly risk averse and prefer standard approaches such as concessional loans; others have focused on one particular instrument, for instance guarantees. Some donors prefer to focus on priority sectors or regions, others may want to pursue a broader approach.

Finding an agreement amongst all stakeholders on what constitutes good practice and aligns with the SDGs has become critical. The OECD has responded by bringing together key players from the private sector, civil society and governments to elaborate a common framework, the *OECD DAC Blended Finance Principles for Unlocking Commercial Finance for the SDGs*. Building on OECD analysis and best practices, these Principles were shaped by the DAC members and external stakeholders who provided country-level perspectives from their constituencies. As a result, the *OECD DAC Principles for Unlocking Commercial Finance for the SDGs* were approved at the DAC High Level Meeting on 31 October 2017.

The OECD DAC Principles give a clear definition and provide a five-point checklist to ensure blended finance meets accepted quality standards and achieves impact, based on a development rationale promoted by DAC members. The OECD DAC Principles represent a critical first step towards ensuring that donors engage in the right way, by guaranteeing that the policy framework is fit for purpose. Whether a donor is looking to begin a blending programme or already has one, we recommend that the OECD DAC Principles be used to test assumptions about how blending is currently being undertaken on critically important aspects such as the engagement of local capital markets, the use of concessionality as a precondition to blending, or the provision of monitoring and evaluation mechanisms.

The *OECD DAC Blended Finance Principles for Unlocking Commercial Finance for the SDGs* will be used to further inform our key partners such as the United Nations, the European Union and the World Economic Forum in progressing best practices in blended finance, including through forums such the G20 and G7. We look forward to further engaging with these actors and others in order to deliver the SDGs.

INTRODUCTION

Blended finance is one approach in the 'toolbox' of development finance which the OECD DAC Blended Finance Principles aim to make more effective and efficient. The OECD definition of blended finance is "*the strategic use of development finance for the mobilisation of additional finance towards sustainable development*[1] *in developing countries*", with 'additional finance' referring primarily to commercial finance.[2] The focus thus lies on the mobilisation of commercial finance which is not currently being directed towards development-related investments. All relevant, higher level, commitments made by DAC Members in relation to development co-operation apply to blended finance in the same way as to other financing approaches. These include, amongst others, commitments on official development assistance (ODA) financing targets, the commitment on leaving no one behind, commitments related to development effectiveness, as well as those related to untying aid. Furthermore, these commitments are addressed in the *OECD DAC principles* and will be further integrated into the design and implementation of blended finance policies and approaches in bilateral and multilateral development co-operation.[3]

Blended finance is a key tool for direct mobilisation of commercial capital and offers an opportunity to move towards fully market-based financing in support of the SDGs. The private sector plays an important role in developing, launching and executing projects in developing countries. Both dimensions of the private sector, as the financier and as the investee, are crucial in the context of blended finance. The Principles focus primarily on commercial actors as a source of potential financing for development that has not yet been targeted towards the SDGs.

The Principles have been developed in close co-ordination with other international initiatives on blended finance. This includes notably the *DFI Enhanced Principles on Blended Concessional Finance for Private Sector Projects*[4] which address critical blended finance topics at the operational level by taking the perspective of implementing institutions. Meanwhile, the Business & Sustainable Development Commission has focused on gathering the private sector perspective.[5]

The Principles are targeted at the policy level, reflecting the development mandate of DAC donors, and the policies and instruments under their political oversight. They aim to ensure that blended finance is deployed in the most effective way to address the financing needs for sustainable development as set out in the Addis Ababa Action Agenda (AAAA), by mobilising additional commercial capital and enhancing impact. Whereas both concessional and/or non-concessional development finance can be part of blended structures, the use of concessional resources requires particular care, given its scarcity. Moreover, potential competitive distortions need to be minimised and complementary objectives, such as structural reforms, pursued.

The global context leaves no doubt about the importance of, and the opportunity for, blended finance. The need for mobilising sources beyond development finance for achieving development targets, and the importance of using development finance in a catalytic way is well accepted and reflected in Agenda 2030, the Paris Agreement on Climate Change, and the AAAA. Increasing evidence of the superior long-term performance of sustainable investing points to a shift in the alignment of development and commercial financing. New, evidence and data generated through blended finance can play a key role in demonstrating the potential to substantially enhance commercial actors' information on and understanding of investment performance in developing country markets. By allowing more effective and sophisticated assessments of risk, blended finance can thereby contribute to market building, and provide an accelerated pathway towards sustainable development investments as an asset class.

In conclusion, blended finance carried out effectively holds the promise of yielding substantial additional gains for all parties, especially to the benefit of those, whose development needs require financing. The Principles serve as a call to action to deliver optimal blended finance and to seize the opportunities that come with it for all sides.

1. Until 2030, the Sustainable Development Goals provide the universally agreed results framework in this regard.
2. Development finance, in the context of this definition, includes Official Development Finance as well as private funds that are governed by a development mandate e.g. financing provided by philanthropic organisations. The Principles contained herewith focus on the increased mobilisation of additional commercial finance. As such, they are narrower than the complete scope of blending activities, which also comprise some DAC members' use of blending for the mobilisation of additional public development finance ("Blending 1.0"). The narrower focus of these Principles reflects the evolution of blended finance, in light of the importance of increasing the mobilisation of commercial finance ("Blending 2.0") to meet the financing needs of Agenda 2030.
3. Policy Guidance will be developed to support the operationalisation of the Principles by DAC Members.
4. https://ifcextapps.ifc.org/ifcext/pressroom/ifcpressroom.nsf/0/875D484A28F7A2A7852581BB006BB88B
5. http://businesscommission.org/our-work/blended-finance-taskforce-for-the-global-goals

PRINCIPLE 1 : ANCHOR BLENDED FINANCE USE TO A DEVELOPMENT RATIONALE

PRINCIPLE 2 : DESIGN BLENDED FINANCE TO INCREASE THE MOBILISATION OF COMMERCIAL FINANCE

PRINCIPLE 3 : TAILOR BLENDED FINANCE TO LOCAL CONTEXT

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PRINCIPLE 5 : MONITOR BLENDED FINANCE FOR TRANSPARENCY AND RESULTS

PRINCIPLE 1 : ANCHOR BLENDED FINANCE USE TO A DEVELOPMENT RATIONALE

All development finance interventions, including blended finance activities, are based on the mandate of development finance providers' to support developing countries in achieving social, economic and environmentally sustainable development.

A) Use development finance in blended finance as a driver to maximise development outcomes and impact.

B) Define development objectives and expected results as the basis for deploying development finance.

C) Demonstrate a commitment to high quality.

1a) Use development finance in blended finance as a driver to maximise development outcomes and impact. The development mandate provides the rationale for deploying development finance through blended finance, as an effective and efficient financing approach towards its policy objectives. Consequently, the SDGs are at the core of how and why official development finance is used in blended finance.

1b) Define development objectives and expected results as the basis for deploying development finance. Development objectives and expected results should be defined before the deployment of blended finance. They should be mutually agreed and embraced by all parties, as a key basis for the deployment of blended finance. The overarching objective for the use of blended finance is the expansion of sustainable, market-based solutions for development financing needs.

1c) Demonstrate a commitment to high quality. High quality in the design and execution of projects financed by development finance, including blended finance, are central to the objective of supporting the development of functioning and effective markets. Blended finance should be based on high corporate governance, environmental and social standards, as well as internationally recognised responsible business conduct instruments, providing an opportunity for commercial partners to acquaint themselves with quality standards in unfamiliar markets.

« Private sector financing will be critical to reaching the 2030 goals. DFIs have recently adopted joint guidance for the use of blended concessional finance in our private sector operations. We also welcome the OECD's efforts to bring donors and other stakeholders together around policy principles for blended finance. These initiatives will help us make the best use of scarce development finance resources, having more development impact and mobilising more than would otherwise be possible, without getting in the way of the private market. »

NANNO KLEITERP, CHAIRMAN, EUROPEAN DEVELOPMENT FINANCE INSTITUTIONS

PRINCIPLE 2 : DESIGN BLENDED FINANCE TO INCREASE THE MOBILISATION OF COMMERCIAL FINANCE

Development finance in blended finance should facilitate the unlocking of commercial finance to optimise total financing directed towards development outcomes.

A) Ensure additionality for crowding in commercial finance.

B) Seek leverage based on context and conditions.

C) Deploy blended finance to address market failures, while minimising the use of concessionality.

D) Focus on commercial sustainability.

2a) Ensure additionality for crowding in commercial finance. Development finance is a scarce and precious resource, and mobilisation of additional funds from commercial investors is indispensable to meet the financing needs of Agenda 2030. To effectively increase total financing for development, blended finance needs to: 1) ensure additionality, by being deployed only for uses where commercial financing is not currently available for deployment towards development outcomes, especially if it involves concessionality; and 2) have an explicit focus on opportunities to crowd in financing from commercial sources into transactions that deliver development impact.

2b) Seek leverage based on context and conditions. Blended finance should, when appropriate, efficiently leverage commercial finance to achieve development impacts. Appropriate leverage is context specific and varies across sectors, geographies, and the different stages of the investment life-cycle. While increasing leverage over time is not necessarily an indicator of increased development impact, it is a sign of increasing market maturity and of successful mobilisation. It also serves as a signal for the need for eventual exit of development finance.

2c) Deploy blended finance to address market failures, while minimising the use of concessionality. Blended finance holds a pathfinder role of bringing commercial financing into sectors and geographies with substantial development finance needs. In this context, blended finance should be used to overcome barriers to market formation and withdrawn once functioning markets have been established. Pioneering investments may require considerable concessionality but as markets mature, the magnitude of public contributions should decline. Blended finance should not become a static or permanent approach in a given context, and the use of concessional development finance in blended finance, if any, should be minimized.

2d) Focus on commercial sustainability. Blended finance transactions, particularly those involving concessionality, should be designed to eventually ensure commercial sustainability, including having a clear strategy for the duration of and exit of concessional finance. In supporting the evolution of nascent and immature markets, there is the need for effective safeguards to ensure optimal resource allocation, maintaining a level playing field and avoidance of market distortion. The focus of concessionality should be towards development impact. Blended finance should also ensure competitive approaches and support that includes equal information, requirements and standards be applied to different market participants.

« The EBRD was created to catalyse private sector investment in its region and therefore welcomes the adoption of the OECD DAC Blended Finance Principles. These are highly complementary to the principles adopted by the development finance institutions, which together are important in ensuring best practice. »

ALAN ROUSSO, MANAGING DIRECTOR, EXTERNAL RELATIONS AND PARTNERSHIPS, EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

PRINCIPLE 3 : TAILOR BLENDED FINANCE TO LOCAL CONTEXT

All development finance interventions, including blended finance activities, are based on the mandate of development finance providers' to support developing countries in achieving social, economic and environmentally sustainable development.

A) Support local development priorities.

B) Ensure consistency of blended finance with the aim of local financial market development.

C) Use blended finance alongside efforts to promote a sound enabling environment.

3a) Support local development priorities. Achieving positive development impact means meeting people's needs. Blended finance can fulfill local development priorities by enabling the financing of businesses that serve local consumers and create decent jobs. Blended finance should support investments that are aligned with national priorities as is the case with all development finance interventions.

3b) Ensure consistency of blended finance with the aim of local financial market development. The emergence of efficient local financial markets will be essential to sustainable financing for development. Hence, blended finance should seek opportunities to work with local financial sector actors, where possible, and should avoid approaches that discriminate against the local financial sector.

3c) Use blended finance alongside efforts to promote a sound enabling environment. A sound enabling environment is a vital condition for mobilising private investment. Blended finance can be a means of achieving development impact in challenging environments, but it can also be an important complement to reform efforts, and should seek to be supportive of them where relevant.

« The need for the effective delivery of finance for development is a critical issue and a core component of achieving the billions to trillions objective; the OECD DAC Blended Finance Principles set out a useful framework which will provide a strong enabling environment. Their adoption by the DAC is an important milestone. »

BERTRAND BADRÉ, CEO, BLUE LIKE AN ORANGE SUSTAINABLE CAPITAL

PRINCIPLE 4: FOCUS ON EFFECTIVE PARTNERING FOR BLENDED FINANCE

Blended finance works if both development and financial objectives can be achieved, with appropriate allocation and sharing of risk between parties, whether commercial or developmental. Development finance should leverage the complementary motivation of commercial actors, while not compromising on the prevailing standards for development finance deployment.

A) Enable each party to engage on the basis of their mandate and obligation, while respecting the other's mandate.

B) Allocate risks in a targeted, balanced and sustainable manner.

C) Aim for scalability.

4a) Enable each party to engage on the basis of their respective development or commercial mandate, while respecting the other's mandate. All parties need to have a stake in the success of the transaction. The objective of blended finance is not to change the motivation of commercial or development actors, but to create opportunities for investments that yield both development and commercial returns, and thus that can be supported by commercial finance. Conversely, development actors should not compromise on their standards – as well as relevant international standards – for the design, terms and execution of interventions.

4b) Allocate risks in a targeted, balanced and sustainable manner. Mobilising commercial finance in a sustainable manner requires addressing the risk-return profile of a transaction through balanced and sustainable risk allocation between development and commercial parties, whether through concessional or non-concessional instruments. The ability of development finance providers to effectively and efficiently allocate, take and manage risk is therefore central to blended finance.

4c) Aim for scalability. Both the magnitude of development financing needs and its relevance for commercial financing, make scalability an important factor in ensuring blended finance reaches its potential. Development finance providers should collaborate through standardisation and harmonisation, including on programme approaches, where possible, so as to encourage the increase in scale and scalability of blended finance. Whereas tailor-made transactions will continue to be required, notably in more challenging markets and in proof of concept investments, development finance providers should share lessons learned and best practices in order to support scalability over time in these markets or sectors, wherever possible.

« IFC recognises the importance of effective policy settings to scale up and mainstream blended finance and therefore welcomes the OECD DAC Blended Finance Principles, which are complementary to the Enhanced Principles that IFC and other DFIs have adopted in the context of private sector operations. »

NENA STOILJKOVIC, VICE PRESIDENT OF BLENDED FINANCE AND PARTNERSHIPS, IFC

PRINCIPLE 5 : MONITOR BLENDED FINANCE FOR TRANSPARENCY AND RESULTS

To ensure accountability on the appropriate use and value for money of development finance, blended finance operations should be monitored on the basis of clear results frameworks, measuring, reporting on and communicating on financial flows, commercial returns as well as development results.

A) Agree on performance and result metrics from the start.

B)) Track financial flows, commercial performance, and development results.

C) Dedicate appropriate resources for monitoring and evaluation.

D) Ensure public transparency and accountability on blended finance operations.

5a) Agree on performance and result metrics from the start. Since inception, development and commercial actors taking part in blended finance operations should adopt a common monitoring and evaluation framework. Performance and result metrics should be applied to both direct engagement of donors in blended finance and to intermediated operations, while specific reporting arrangements may be tailored to context. Establishing a common set of key performance indicators should be a priority to ensure a transparent, harmonised and comparable assessment of results, thereby also providing a common framework of intervention for all parties to a given blended finance operation.

5b) Track financial flows, commercial performance, and development results. In order to assess the effectiveness and efficiency of blended finance operations, the financial and development performance of all parties should be assessed against predefined and agreed upon metrics. These should cover development finance, additional commercial finance mobilised (including financial returns), and the results achieved on development objectives.

5c) Dedicate appropriate resources for monitoring and evaluation. Adequate systems should be put in place to allow the monitoring and evaluation of the development interventions supported through blended finance. Donors should align on a common understanding of blended finance assessment methodologies to ensure consistency in data collection and reporting.

5d) Ensure public transparency and accountability on blended finance operations. Information on the implementation and results of blended finance activities should be made publicly available and easily accessible to relevant stakeholders, reflecting transparency standards applied to other forms of development finance. Besides accountability, external communication on blended finance performance is instrumental in mobilising further commercial capital, by improving the availability of market information and the quality of risk assessment for the efficient pricing of investments.

« Donors must clearly spell out whether blended finance can meet the challenge of reducing poverty and inequality. So far, there is simply no evidence to tell us whether or not blended finance can have a positive impact on people and planet. »

WINNIE BYANYIMA, EXECUTIVE DIRECTOR, OXFAM INTERNATIONAL

PUTTING PRINCIPLES INTO PRACTICE

In the future, the OECD will work on more detailed guidance for policy makers to support the implementation of these Principles. The guidance will provide best practice examples, support the development of effective policies and facilitate accountability. The OECD Blended Finance work aims to further deepen the analysis of blended finance practices, with a practical orientation on performance, focusing on development and financial metrics.

Work on blended finance stands to benefit substantially from further analysis and guidance on issues such as the effective targeting of economies and sectors that are important in ensuring blending can deliver on its potential of mobilising capital, delivering impact and transforming economies. To achieve this, greater transparency is needed both for blended finance and other development interventions – such as common harmonised results frameworks, performance measurement and product standards.

The Blended Finance Principles will be further used to inform our key partners such as the UN, EU and World Economic Forum in progressing blended finance best practices, as well as through forums such as the G20 and G7. We therefore look forward to further engaging with key stakeholders in order to deliver the SDGs.

« Official development assistance continues to be a key way to finance efforts aimed at eradicating extreme poverty. However, the challenge is more than governments alone can manage. We must all think, work, finance and deliver development differently to mobilize private-sector resources and expertise to help the world's poorest and most vulnerable people. Canada continues to promote innovative approaches to finance development and achieve sustainable growth for everyone. »

THE HONOURABLE MARIE-CLAUDE BIBEAU,

CANADA'S MINISTER OF INTERNATIONAL DEVELOPMENT AND LA FRANCOPHONIE

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