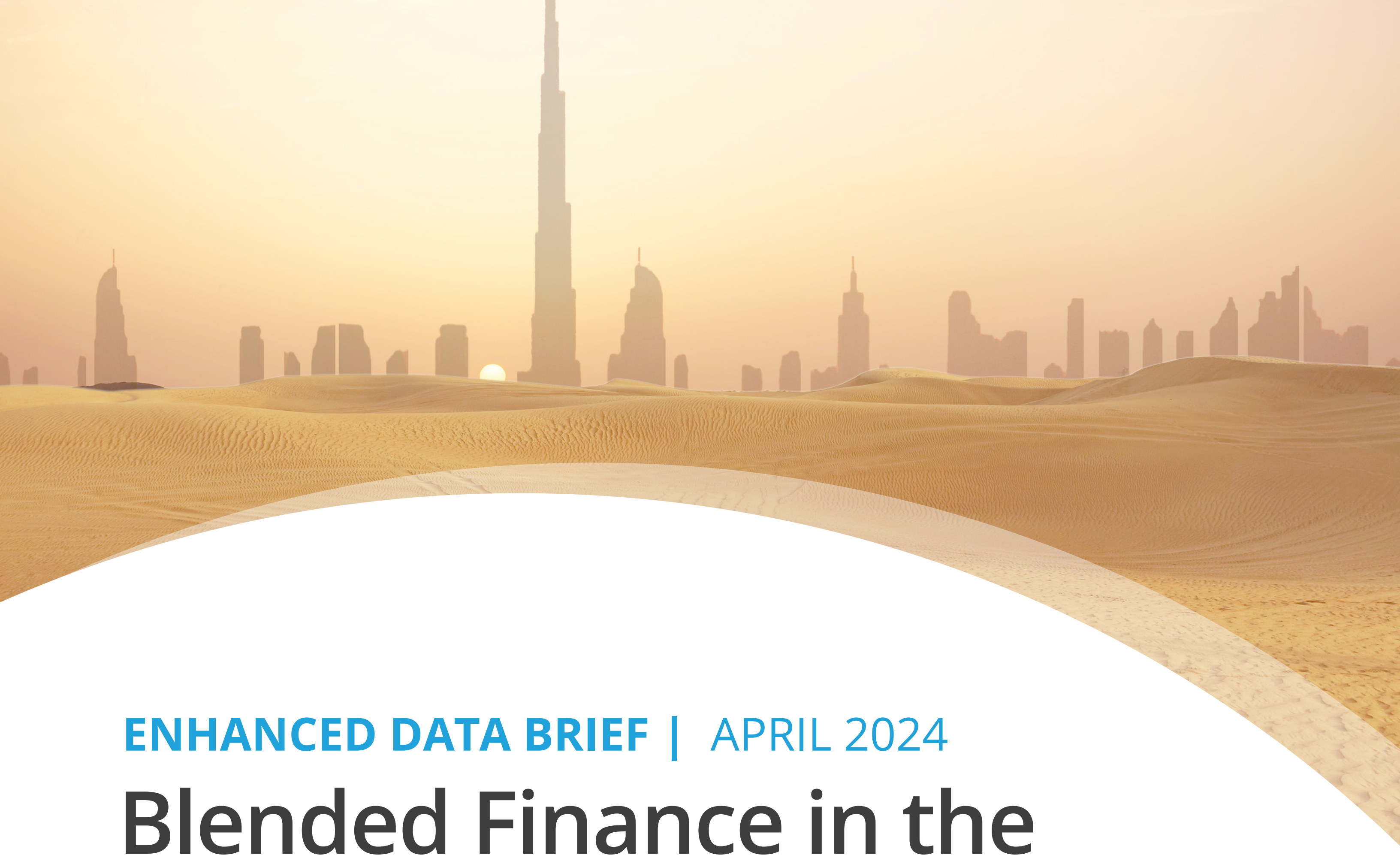

ENHANCED DATA BRIEF | APRIL 2024

Blended Finance in the Middle East & North Africa

HIGHLIGHTS

- Blended finance in the Middle East and North Africa (MENA) is nascent, with Convergence's database recording 83 transactions targeting MENA in part or in full, representing aggregate committed financing of $14.2 billion.
- Perception of risk is the most common challenge to mobilizing private capital in MENA. Meanwhile, regional markets vary by levels of geopolitical stability and currency risk.
- Egypt is the most active blended finance market in MENA, accounting for nearly 24% of all blended finance deals in the region.
- The top three sectors targeted by blended finance transactions in MENA are financial services (36%), energy (22%), and infrastructure (20%).
- Technical assistance (TA) funds have appeared in MENA-focused transactions at a much higher rate than the overall market (42% vs. 26%).
- The most frequent providers of commercial capital in blended finance transactions in MENA are FMO (24), IFC (17), and EIB (14).
- FMO was the top concessional investor, with 18 concessional commitments, followed by BMZ (17) and USAID (8).
- Challenges for increasing the use of blended finance in MENA include the lack of financial intermediation for SME financing, mismatches between humanitarian-led aid systems and private sector mobilization, and regulatory constraints and risks.
- Opportunities to increase blended finance in MENA include experimentation with different vehicles and financing models to enhance private sector mobilization, particularly in more fragile MENA states, and boosting education to catalyze local institutional investors, philanthropy, and grant-makers.

CONVERGENCE
BLENDING GLOBAL FINANCE

UICCA
المسرعات المستقلة لدولة الإمارات العربية المتحدة للتغير المناخي
UAE INDEPENDENT CLIMATE CHANGE ACCELERATORS

HSBC

Foreword

Convergence, UICCA, and HSBC are delighted to present this analysis of blended finance in the Middle East and North Africa. Utilizing insights from key stakeholder interviews alongside analysis of data trends drawn from Convergence's Historical Deals Database, we hope that this report sheds light on key opportunities and challenges for blended finance practitioners operating in the region.

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Introduction

Blended finance in the Middle East and North Africa (MENA) is nascent, with the Convergence Historical Deals Database (HDD) recording 83 blended transactions to date that have targeted MENA in part or in full, representing aggregate committed financing of $14.2 billion. In this data brief, Convergence and UICCA, in partnership with HSBC, seek to explore some of the key challenges and opportunities facing blended finance in MENA, presenting insights from interviews conducted with industry stakeholders.

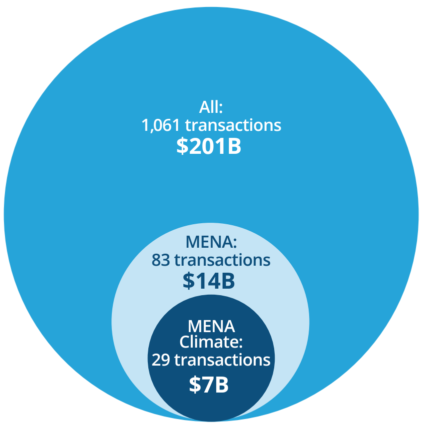

Figure 1: MENA blended finance market compared to the overall market (billions), all time periods

Awareness of MENA's broader investment story has grown in recent years, in part as a result of the 27th and 28th Conference of Parties (COP 27 & COP 28) hosted in Egypt and the UAE, respectively. In this regard, Nadia Boumeziout, Head of Sustainability and Information Governance, Middle East, at Zurich Insurance, highlights that regional interest in impact investment, sustainable finance, and the green bond and green sukuk market have risen. While regional regulators in markets like the UAE, Bahrain, and Qatar have sought to improve environmental, social, and governance (ESG) and sustainability disclosures to bring more transparency into the market, Boumeziout notes that when it comes to catalyzing private investment in MENA, heightened risk perceptions remain the primary challenge.

Rising government debt in markets like Egypt and heightened geopolitical risk in markets like Jordan have presented challenges to regional investors. MENA, of course, is not homogenous. Several of our respondents note that more stable markets like Saudi Arabia, the UAE, and Morocco, have a less acute need for de-risking via concessional support than unstable markets like Syria or the West Bank, in which commercial funds would otherwise not be invested. Heightened capital costs are one consequence of elevated political risks across some MENA markets, observes Frannie Leautier, Senior Partner & Chief Executive Officer, SouthBridge Investments. There is an acute need for blended structures to mitigate the cost of capital in economically depressed parts of MENA. Low access to finance amongst small and medium-sized enterprises (SMEs) remains a major challenge across many MENA economies, with up to 96% of registered companies in the region being SMEs. Many of these enterprises are unable to access adequate financing, particularly in climate or sustainability-related spaces like renewable energy, Boumeziout notes.

Currency mismatches and currency volatility, meanwhile, present another macroeconomic challenge to investors in some regional markets. Rabih Yazbeck, Senior Vice President of Programs & Impact at the Near East Foundation, notes that with many MENA economies being dollarized, any movements toward de-dollarization could produce currency mismatches that investors may find difficult to manage, although the experience of markets like Jordan has been more positive than markets like Iraq, where rapid de-dollarization has risked increasing long-term investment uncertainties. Commenting on the negative impact of currency risk on local private sector activity in MENA's energy transition, Ennis Rimawi, Managing Director at Catalyst Climate Investment Management, notes that with the Egyptian pound being half the value it was in 2022, there has been some hesitation amongst local private investors when appraising domestic climate projects. Political and economic instability presents a key challenge to investment in MENA's climate transition, Rimawi adds:

> *"With MENA bordering Europe and the energy crisis in Europe, there's a significant role for the MENA region to play; transmission lines between North Africa and Europe are currently in process, such as from Tunisia to Italy, opening the opportunity further for renewable energy in MENA. MENA is also looking to boost the proportion of renewable energy in its electricity mix from approximately 4% to 40%. This will be supplemented by export demand such as electricity transmission to Europe and the growth of the green hydrogen/ammonia market. However, the MENA countries with political and/or economic instability present the challenge here."*

When it comes to other core regional challenges that blended finance can help to address, high levels of youth unemployment and gender inequalities in economic participation are major focus areas, observes Maurits Fliehe Boeschoten, Senior Advisor at the Dutch Entrepreneurial Development Bank (FMO). Blended structures targeting job creation and youth unemployment through initiatives like vocational training, through which educated youth would be reskilled in understaffed sectors, would deliver high value while enjoying political and business sector support, adds Leautier. Such political support is often particularly important in MENA markets, Boeschoten notes, given that governments in the region tend to be more actively involved in their economies, with many banks and other enterprises being government-owned. Ultimately, as pioneering projects, blended finance investments can pave the way for other investors to follow suit and create markets, notes Khawaja Aftab Ahmed, Regional Director for the Middle East, Afghanistan, and Pakistan, International Finance Corporation (IFC).

In this brief, Convergence and UICCA, in partnership with HSBC, analyze how blended finance approaches have been deployed in MENA to date, presenting insights from interviews conducted with industry stakeholders.

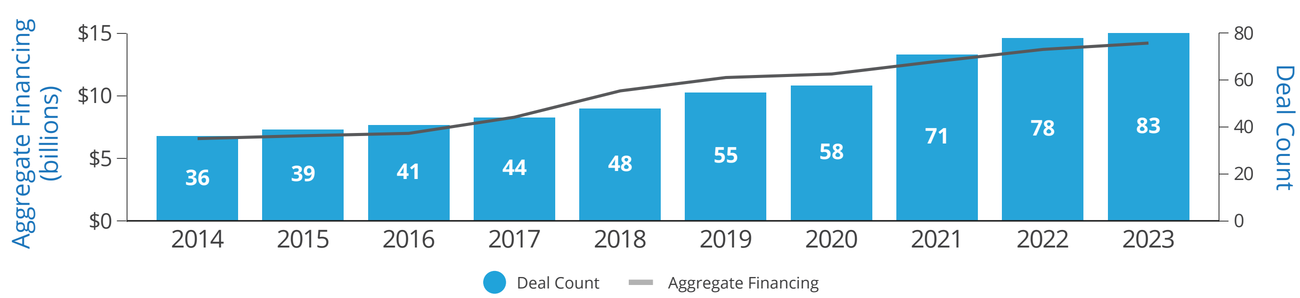

Figure 2: Market size and growth of blended finance in MENA by aggregate financing (billions) and deal count

Blending in MENA: Analysis

SMALL BUSINESS/CORPORATE BANKING: KEY SUB-SECTOR IN MENA

Blended finance transactions in MENA reflect a strong commitment to economic growth and the energy transition. Most blended finance deals have occurred in the finance sector, specifically in small business/corporate banking (24%) and microfinance/retail banking (18%). Renewable energy initiatives represent 16% of blended deals in MENA. The growing focus on renewable energy investments is likely driven by regional efforts to promote a more sustainable energy mix. Various countries in the region, including Jordan, Egypt, and Morocco, have set ambitious renewable energy targets and are scaling up their energy storage capacities. Blended finance has been a key strategy to direct private capital towards these kinds of projects. For instance, Yellow Door Energy secured $31.2 million in senior secured loans for the development, construction, and operation of eight solar plants in Jordan with a total installed capacity of 48.3 MW. This deal was enabled by a $5 million senior concessional loan from Global Environment Facility, a TA grant from the European Union, and results-based payments of up to $1.75 million from the Government of Spain through the European Bank for Reconstruction and Development (EBRD). The remaining project costs are set to be covered by sponsor equity.

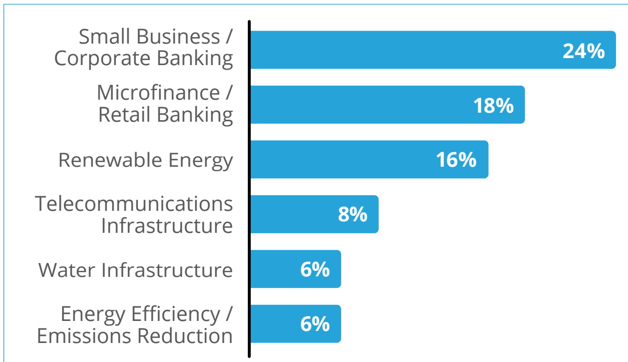

Figure 3: MENA transactions by sub-sector

FUNDS PREDOMINANT IN MENA: PROJECTS AND COMPANIES UNDERREPRESENTED

Funds account for nearly half of all MENA transactions, compared to the overall market, while companies and projects are less prominent. Notably many of these MENA-focused funds also allocate investments to Sub-Saharan Africa. For instance, the Urban Resilience Fund is a private equity fund targeting public and private infrastructure opportunities in urban settings across Sub-Saharan Africa and MENA. Similarly the Canada Investment Fund for Africa makes private equity investments into businesses across the African continent with a focus on larger markets including South Africa, Nigeria, Egypt, Morocco, Algeria, East Africa, and Francophone West Africa.

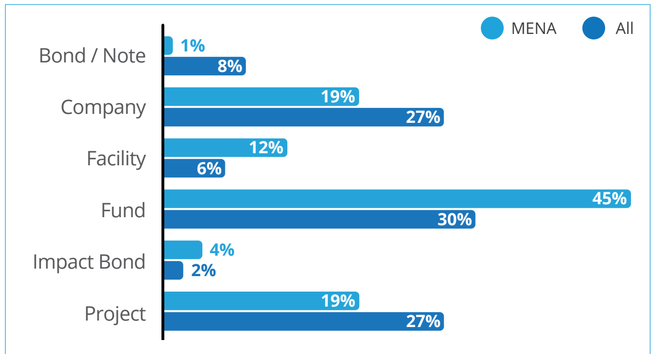

Figure 4: MENA transactions by vehicle type

MENA TRANSACTIONS TYPICALLY LARGER COMPARED TO OVERALL MARKET

MENA transactions have a median size of $83.2 million (compared to $49.6 million for all blended transactions), with 42% above $100 million. The larger deals typically concentrate in the financial services, infrastructure, and energy sectors. There are also various large ticket renewable energy projects funded through blended finance, including the repowering of Koudia Wind Farm at approximately $136 million and Ghoubet Djibouti Wind Farm at $122 million.

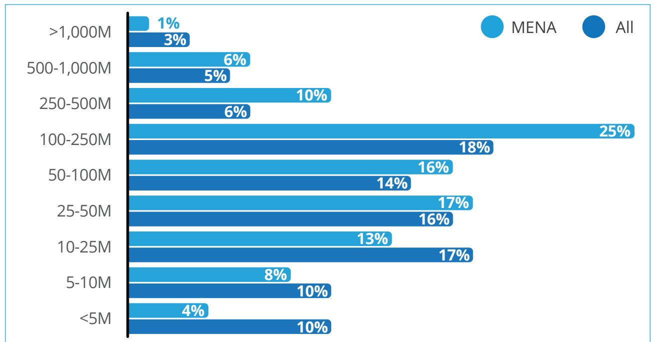

Figure 5: MENA transactions by total size

LOW-INCOME/BASE OF THE PYRAMID CONSUMERS MORE SUPPORTED IN MENA

Low-Income/Bottom of The Pyramid (BoP) Consumers (60% of MENA transactions vs. 49% of all transactions) and the "Missing Middle" (18% vs. 10%) are more supported as end beneficiaries in MENA compared to the overall market. Examples include the KOIS Impact Bond, which is delivering vocational, entrepreneurship, and employment training to refugees of the Syria civil war and their host communities in Jordan. KOIS was awarded grants from Convergence and the IKEA foundation to design, structure and fundraise for the bond. The development impact bond reached its first financial close in October 2021, raising $7.8 million from US Development Finance Corporation and Ferd Norway to finance the upfront costs of the program. These investors will be reimbursed and earn a return based on the achievement of agreed development outcomes by IKEA Foundation, Novo Nordisk Foundation.

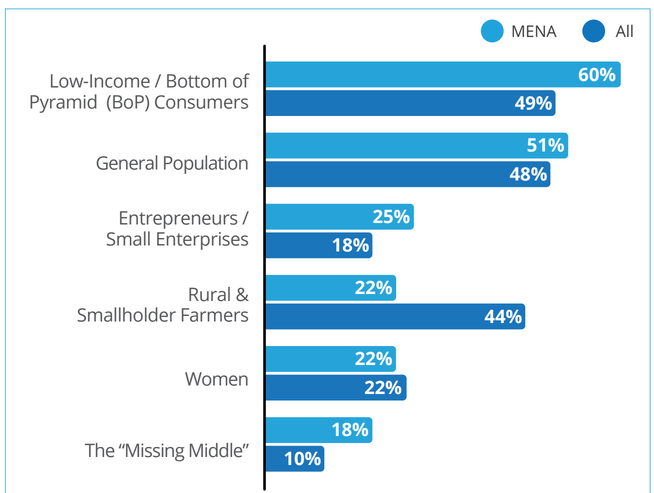

Figure 6: MENA transactions by end beneficiary

EGYPT AND JORDAN ARE THE LEADING MENA COUNTRIES FOR BOTH BLENDED FINANCE AND CLIMATE BLENDED FINANCE

Public-private-partnership (PPP) legislation enabling private investors to play larger roles in supporting the climate transition by increasing their investment in green and low-carbon ventures has risen in MENA markets like Egypt, Jordan, the UAE, and Morocco. Egypt has been the most frequent destination for blended transactions in MENA (20 transactions), with 50% of Egypt's blended transactions targeting climate-related Sustainable Development Goals[1] (SDGs). Examples include the 200MW Kom Ombo Solar Plant, one of Egypt's largest privately developed solar projects, which is expected to generate electricity for 130,000 households and offset carbon emissions of 280,000 tons annually, aligning with the Egyptian government's aim to produce 42% of the country's electricity from renewable energy sources by 2035. Private-sector participation in the plant has benefited from a $3.6 million TA program, co-funded by EBRD and the Green Climate Fund, to support the administration of competitive renewable energy tenders.

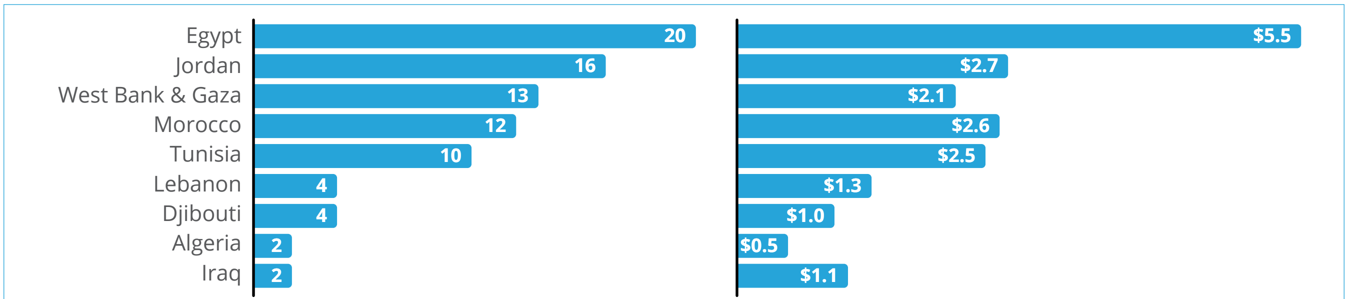

Figure 7: MENA deal count & aggregate financing (billions), by country

TA IS DEPLOYED AT A HIGHER RATE IN MENA

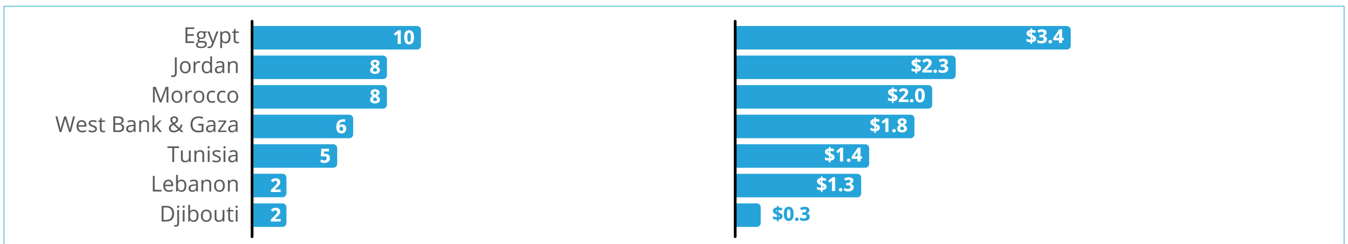

Figure 8: MENA climate deal count & aggregate financing (billions), by country

TA funds have appeared in MENA-focused transactions at a much higher rate than the overall market (42% vs. 26%). In our database, the TA funds leveraged in MENA-focused transactions are most often joined by another archetype (e.g., concessional debt/equity or guarantee/risk insurance) within the transaction. For example, the Azur Innovation Fund by the Moroccan Government combines various concessional components. The seed equity fund is supported by a partial first-loss guarantee provided by the government through its Central Guarantee Agency (CCG), which will cover losses up to 60% of the fund's total investments. The CCG will waive its returns if the Fund's net internal rate of return (IRR) at closure is under 5%. A portion of the CCG's $11 million investment is also earmarked as a TA fund to help develop investments upstream and improve their quality.

Meanwhile, the use of guarantees/risk insurance in MENA is relatively rare compared to concessional debt / equity and TA funds. However, guarantees were identified by our respondents as instruments of particular importance to private capital mobilization in the region. For example, Rimawi notes the role of guarantees in mitigating risk in less stable MENA markets:

> *"There are different levels of intervention in markets where there's instability or non-bankability on the government side, but they would typically involve payment guarantees, or currency conversion guarantees if you're in a market like Egypt. For example, if you are expecting to be paid in Egyptian pounds, but you're not sure if you can convert them to dollars, you'd need a third party to guarantee that convertibility."*

1 Transactions were considered climate-focused first based on their alignment to select SDGs: SDG 2 (Zero Hunger), SDG 7 (Clean Energy), SDG 11 (Sustainable Cities), SDG 13 (Climate Action), SDG 14 (Life Below Water) and SDG 15 (Life on Land).

Similarly, Leautier notes the ease with which guarantees can be tailored to address regional risk perceptions:

> *“Since guarantees can take the same amount of funding and stretch its value over multiple years and multiple users as they’re not always called, their contingent nature allows much more private investment to be crowded in than other blending structures. They can also be more flexibly tailored to target specific risk categories, such that they can offer solutions much better suited to the types of investors entering riskier environments.”*

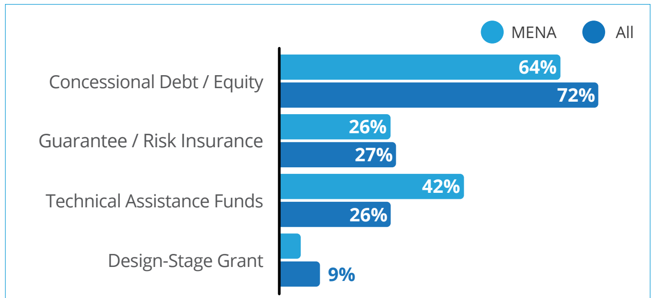

Figure 9: MENA transactions by blending archetype(s)

DFIS/MDBS MORE ACTIVE AS DEAL SPONSORS IN MENA

Development Finance Institutions (DFIs)/Multilateral Development Banks (MDBs) have played a pivotal role in the blended finance market in MENA, where they’ve been much more active compared to the overall market (40% vs. 30%). Meanwhile, foundations/NGOs (6% vs. 10%) and commercial investors (20% vs. 26%) have sponsored a smaller share of deals in MENA compared to their activity in the broader market. Nonetheless, commenting on DFI/MDB activity in North Africa, Leautier notes that more can still be done to better engage with the local private sector:

> *“Historically, some DFIs considered local economies in the region as having per-capita incomes too high to qualify for concessional funding. However, when you see how concessional finance can support platforms from which North African companies can expand into key climate-focused or SDG-focused impact areas, both in North Africa and in the rest of the continent, the need for greater DFI support is clear.”*

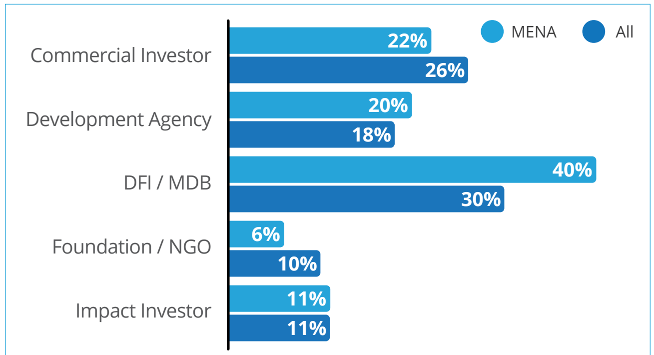

Figure 10: Deal sponsors of MENA transactions by type of organization

FMO, IFC, EIB: TOP COMMERCIAL INVESTORS IN MENA

While every blended transaction mobilizes capital from at least one private sector investor, FMO (24), IFC (17), and EIB (14) have provided the highest number of commercial commitments to MENA-focused blended finance transactions to date.

The mobilisation of local institutional investors into blended finance vehicles, meanwhile, remains a challenge faced by the overall market. Commenting on the regulatory context within which institutional investors in North Africa operate, such that they must deploy large portions of their capital within their domestic economies, Leautier notes the importance of better integrating regulatory standards within well-structured projects to attract local institutional capital:

> *“If domestic investment opportunities aren’t very good, local institutional capital risks creating asset bubbles or parking their capital as cash rather than being invested for return, which can have deleterious effects for the future (e.g., providing income for retirees, etc.). With ongoing changes in climate policy, large domestic infrastructure projects that aren’t properly prepared or structured risk regulatory obsolescence, for example. Using blended finance to better integrate regulatory standards within well-structured projects can help institutional investors in North Africa secure the future of their own populations and economies by accessing good investment opportunities.”*

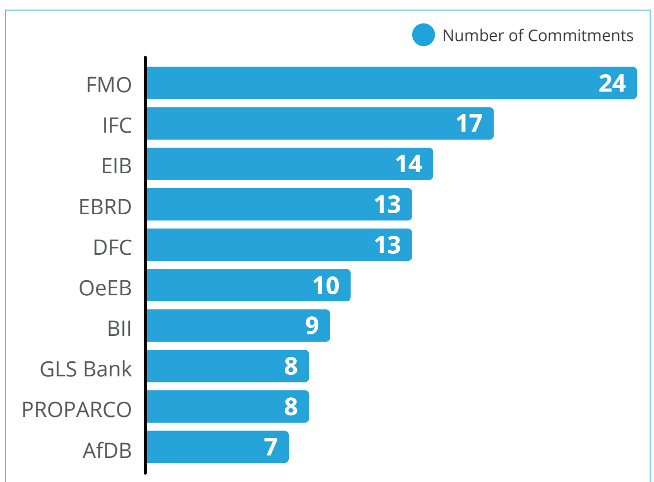

Figure 11: Top providers of commercial finance to MENA transactions by number of commitments

FMO, BMZ, AND USAID: TOP CONCESSIONAL INVESTORS IN MENA

Development agencies (50%), DFIs/MDBs (33%) and foundation/NGOs (10%) have been the main concessional actors in MENA, with FMO (18 commitments), the German Federal Ministry for Economic Cooperation and Development (BMZ) (17), and United States Agency for International Development (USAID) (8) providing the highest number of concessional commitments to MENA-focused blended finance transactions to date. These actors have predominantly committed concessional debt/equity. An example of this is GoMyCode, a Tunisia-based edtech company offering cohort-based trainings for high-demand tech skills. GoMyCode closed a $7.8 million Series A round in 2022, the largest edtech round at this stage on the African continent, and was helped by first-loss, equity-like funding provided by USAID Invest, CrossBoundary and Flat6Labs.

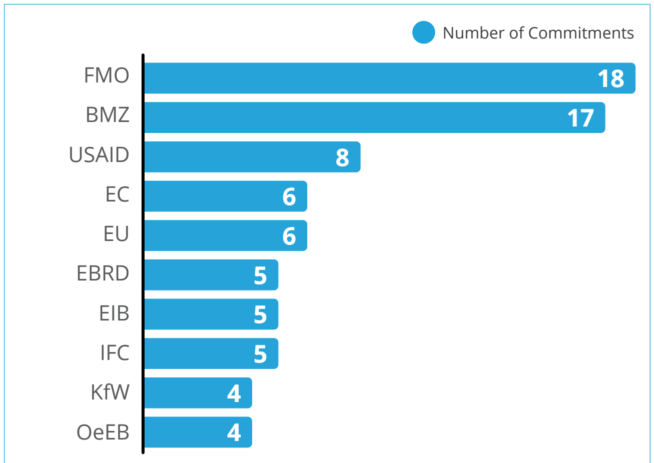

Figure 12: Top providers of concessional finance to MENA transactions by number of commitments

Spotlight on Climate Blended Finance in MENA

MITIGATION: KEY CLIMATE FOCUS IN MENA

As noted previously, several MENA markets have seen positive climate regulatory developments in recent years. Rimawi observes that,

> *"Regulations for private concessions are being formed in some MENA markets to ensure correct market functioning. Jordan and Morocco, for example, are leaders in this regard, with both having implemented laws allowing private energy producers to connect to the national grid (the net-metering and wheeling reforms in Jordan; Law 13-09 in Morocco)."*

Most climate blended finance in MENA to date, by both transaction count and aggregate financing, has focused on climate mitigation. Convergence's database has tracked 16 deals exclusively focused on mitigation in MENA, representing approximately $4.6 billion in financing. Examples include the $100 million Commercial International Bank (CIB) Green Bond in Egypt. This deal involved $1.4 million in concessional capital from IFC in the form of performance-based incentives as well as TA grants from Green Bond Technical Assistance Program - with funding from the Swedish International Development Cooperation Agency (SIDA) - and the Market Accelerator for Green Construction Program - with funding from the UK's Department for Business, Energy and Industrial Strategy (BEIS). The proceeds of the bond are being used to finance businesses looking to invest in green buildings and renewable energy. The predominance of mitigation deals in MENA aligns with trends in the overall blended finance market. Mitigation transactions are generally more appealing to investors than adaptation deals due to their clearly defined nature, familiar greenhouse gas reduction targets, and more obvious revenue-generating potential.

Meanwhile, only 4 MENA-focused deals have focused on adaptation, amounting to approximately $201 million in financing. One example is a recent deal involving Kumulus, a Tunisian tech firm pioneering water extraction from air humidity to tackle water scarcity. The firm secured early-stage grant support from USAID INVEST and CrossBoundary, which helped it raise nearly $1 million in investments from venture and angel investors, including Flat6Labs, Wilco and Bpifrance. In terms of hybrid deals, there have been 10 MENA-focused hybrid transactions, amounting to $2.3 billion.

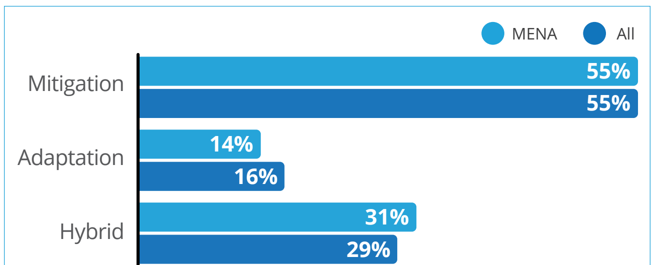

Figure 13: MENA transactions by climate type

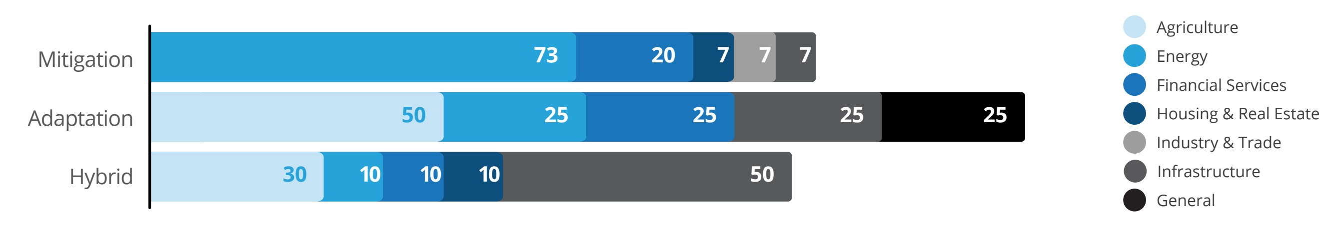

Figure 14: Proportion of mitigation, adaptation, and hybrid MENA blended finance transactions by sector (%)[2]

TA MORE PROMINENT IN MENA CLIMATE TRANSACTIONS THAN IN ALL CLIMATE DEALS

Mirroring the broader MENA market trend, TA is much more prominent in MENA-focused climate transactions than in all climate transactions (57% vs. 29%). Interestingly, guarantees have been used slightly less in MENA-focused climate transactions compared to all climate transactions (20% vs. 25%). Considering less stable markets in MENA with security issues or less bankable governments, like Lebanon, Palestine, Syria, Yemen, Sudan, and Libya, where energy is often badly needed and brownouts and outages are often common, Rimawi notes the importance of donors mitigating risk and stimulating private investment by stepping in as the payor in payment guarantee structures for climate infrastructure projects. Here, donors would either make the concession payments or support governments in making those payments, with the private sector funding the capital expenditure, Rimawi notes:

> *"The kind of intervention needed here would be a third party guaranteeing offtaker payments, or the third party being the payor directly. The Millennium Challenge Corporation did something like this in Benin with the Benin Power Compact, offering to make the payments over a 20-year concession while a private sector consortium would build and operate a 50MW solar PV project to inject electricity into the grid. This would be the highest level of intervention required due to either non-bankability of the government or instability and would help create demonstration effects for private sector concessions in the region."*

Meanwhile, grants and subsidies in the form of viability gap funding will be particularly important to developing battery storage projects in more stable markets in MENA, Rimawi adds:

> *"Where it starts getting more challenging for offtakers is with things like battery storage projects, which help reduce fossil fuel usage for peak periods and stabilize electricity grids or provide stopgaps for when sun and wind energy isn't available. However, even after recent falls, battery prices remain quite high for most regional utilities, and aren't where they need to be. We're trying to develop large-scale showcase battery storage projects across MENA, which in turn could enable solar desalination or solar water treatment initiatives, but grants and subsidies are still needed in the form of viability gap funding to make these projects financially possible."*

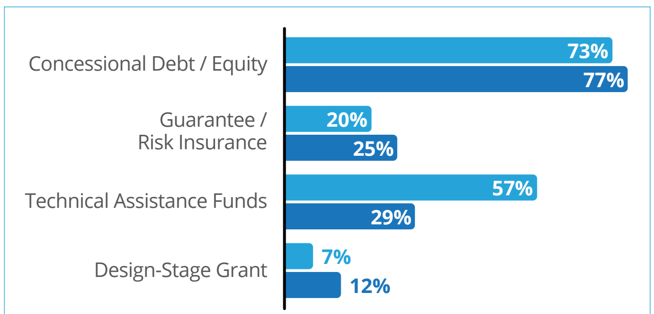

Figure 15: MENA climate transactions by archetype

2 Bars do not sum to 100% given that blended finance transactions can target multiple sectors.

Reflections

Building upon the macroeconomic challenges explored earlier in this report, our engagement with different blended finance practitioners yielded several themes regarding key challenges and opportunities for blended finance in MENA.

CHALLENGES

1 LACK OF FINANCIAL INTERMEDIATION FOR SME FINANCING

A key challenge facing blended finance in general that Convergence has previously identified is the lack of financial intermediation; that is, donors and investors are looking to channel large amounts of capital towards market opportunities aligned with the SDGs, but SDG projects are often small, with few intermediaries in the market to channel these flows. Our respondents similarly identify this as a key challenge within MENA, particularly when it comes to SME financing. Boumeziout observes that commercial banks and investors are typically only interested in very large projects so that they can guarantee their returns and better manage the related risk. Similarly, Yazbeck notes:

"When looking to attract investment to support SMEs, we've found a mismatch between available investments and desired investment sizes on the one hand and demand on the other, which tends to be much smaller in terms of ticket size. SMEs dominate MENA's economies, and their ability to absorb investments is limited. However, the supply and expectations of capital is quite high, with the cost of completing transactions and attaining regulatory protections adding to this further."

2 MISMATCH BETWEEN HUMANITARIAN-LED AID SYSTEMS & PRIVATE SECTOR MOBILIZATION

Another key challenge in some MENA markets relates to the mismatch between aid-focused development systems and international private finance flows classified most often as foreign direct investment (FDI). As Yazbeck observes:

"Markets like Jordan are more pro-investment, with big, well-established regulated frameworks and pre-defined vehicles addressing local development priorities like the existing refugee crisis and attracting grant or subsidized funding. However, these vehicles aren't necessarily designed to attract private investment, which instead tends to flow as FDI. We've worked with the Jordanian government to adapt their development or crisis-oriented processes to attract private capital through innovative finance vehicles like the Refugee Impact Bond.

Across the MENA region, there's a mismatch between existing humanitarian-led systems and the ability to effectively attract private capital with the right regulatory frameworks and vehicles. While channeling small proportions of aid into private sector-led structures can make a significant change, from the perspective of local governments, doing this can sometimes appear quite complex, and in some countries, bureaucracies become a substantial roadblock to opening the economy to the private sector through transparent, competitive processes. The primary issue at present, however, is the complete disconnect between the aid economy and the private sector."

International private capital in less stable MENA markets is faced with the prospect of navigating risks like international sanctions or investing without established banking or financial frameworks, Yazbeck notes. While guarantee instruments can help reduce the private sector's risk exposure when proof of concept that SMEs will repay their loans doesn't exist, private capital will still have to share the risk of investing in more volatile frontier markets, adds Yazbeck.

3 REGULATORY CONSTRAINTS & RISKS

The regulatory environment in MENA can sometimes be an additional constraint, Fernando Rodrigues, Head of Private Sector Operations, North Africa at the African Development Bank (AfDB), observes:

"While North African countries have been amongst the largest FDI recipients on the continent, there are still options to further facilitate foreign investors' investment; for example, land acquisition can be constrained for foreign investors. In some cases, regulation makes it difficult for foreign investors to retain full control over a project. There can also sometimes be issues with the repatriation of foreign currency, while F/X [foreign exchange] risk is an additional layer of particular attention."

Meanwhile, the risk of stranded assets represents another challenge for climate investment in MENA, Lama Kiyasseh, Country and Investment Risk, Multilateral Investment Guarantee Agency (MIGA), notes:

"One of the bigger concerns I see in MENA is the risk of stranded assets. A lot of banks, particularly in the Gulf, are highly exposed to national oil and gas companies and national energy ecosystems; that is, the entire infrastructure across the fossil fuel value chain.

The impending impact of re-evaluating bank portfolios and balance sheets based on stranded assets may create a liquidity squeeze, and in turn who these banks are able to on-lend to, which may limit credit provision for climate transition investments. While banks have been able to offer diverse sustainable finance products, they should strengthen their methodologies for effectively assessing climate-related risks and opportunities."

OPPORTUNITIES

1 EXPERIMENTATION TO BOOST PRIVATE SECTOR MOBILIZATION, PARTICULARLY IN FRAGILE STATES

Our respondents note that experimentation with different types of vehicles and initiatives, particularly in less stable markets in MENA, can begin to help catalyze private sector financing more effectively. For example, commenting on the Near East Foundation's blended social enterprise Siraj Financial Services, which provides Syrian SMEs with access to financial and non-financial services and is structured with $2 million of first-loss loan capital, Yazbeck notes:

"Our vehicle in Syria is one of its kind, but it would be great to replicate it across the board. Why is there nothing similar in other places? We focus on channeling investment into the private sector, but there are many other opportunities; what about insurance products or lending capital to the general population? Vehicles that can also help calculate and quantify risk more effectively would be helpful for private investors; there's a lot of unknowns in the region."

Yazbeck also notes that the evidence collected to-date from the Near East Foundation's activities in markets like Syria to support SMEs is positive, even with SMEs often not being registered or independently audited due to inadequate or non-existent regulatory and financial service infrastructures:

"We've seen very low default rates in these markets, indicating that these SMEs are willing and able to service their debt. Their job creation potential is also quite significant. The likelihood of perceived risks materializing is low, based on our evidence. Risk tolerant private capital can really make a difference to SMEs in the less stable parts of MENA."

2 BOOSTING EDUCATION ON BLENDED FINANCE TO CATALYZE LOCAL INSTITUTIONAL INVESTORS & DRAW IN LOCAL PHILANTHROPY & GRANT-MAKERS

With understanding of blended finance being limited in many MENA markets, enhanced awareness through knowledge dissemination is needed for blended finance to be seen as a tool that can be deployed more broadly across local economies. For example, Ahmed notes that sharing best practices, lessons learned, and knowledge across stakeholders can accelerate the adoption of effective blended finance models in the region. As Leautier observes, this could involve local institutional investors collaborating with international institutional investors to better understand how capital can be deployed for development impact, leveraging knowledge on what has been experimented on elsewhere. Tapping into commercial investors in the Gulf Cooperation Countries to mobilize blended finance and scale climate investments in the region, for example, represents an important focus area in the Middle East, Ahmed notes:

"We see Middle East investors as having major co-investing opportunities in the South-South space and in mobilizing cross-border investments across the Middle East region as well as Africa, Central Asia, and other regions, especially around climate, gender, water, food security, and digital connectivity."

Meanwhile, with MENA's sovereign wealth funds expected to play an increasingly large role in the development of the region's sustainable investment market, which they can approach as part of a broader strategy of national diversification due to their high political visibility, soft power mandates, sovereign backing, and longer time horizons, they can also play a leading role in de-risking commercial investors and developing the blended finance ecosystem in the region.

Another area of significant potential is the alignment of blended finance with Islamic finance, a set of faith-based, asset-backed financial intermediation products and institutions emphasizing the sharing of profits and losses and fostering integration between the financial sector and the real economy. Boumeziout notes that impact investing is well-aligned with Islamic finance, which already has inherent exclusions and a whole-of-society approach in which social co-benefits are sought. Such an alignment could see local philanthropy and local grant-makers become better integrated within blended finance, rather than simply focusing on concessional support from international philanthropy or bilateral aid. Leautier observes:

> *"There's a lot of philanthropy within North Africa that could be tailored towards these solutions, particularly when you consider Islamic finance, in which collecting interest is forbidden. Islamic finance could be structured in a way that aligns with blended finance, wherein concessional actors invest alongside commercial actors to achieve profitability and sustainability."*

Roadblocks to the greater involvement of local philanthropy and local grant-makers in blended finance in MENA include the desire for anonymity. Leautier adds:

> *"A lot of the philanthropy is personal philanthropy from high net-worth families who prefer anonymity and disperse their philanthropy quietly. Developing a platform that can maintain that anonymity but enable broader participation would help solve that problem. Another factor is just a lack of knowledge of how they can blend their resources with other forms of capital to deliver results, since it's not something they've done historically; with typically only one or two family members managing their funds, they're not structured in a way that can contribute to more complex financial structures. Pairing larger external philanthropies with one or two local philanthropies to share learnings will also be key."*

Finally, Leautier notes that something as straightforward as developing deal match-making platforms in the different variants of Arabic spoken across MENA, connecting investors with local opportunities currently fundraising, could enable broader uptake of blended solutions in the region. Ahmed similarly observes the importance of building local capacity in project development and access to reliable data and information on investment opportunities, market conditions, and project performance in MENA.

CONCLUSIONS

While geopolitical risk and currency volatility present key challenges for private investors in some MENA markets, MENA is not a monolith; regional economies vary in their levels of stability and familiarity with private financing flows. Other challenges facing blended finance in MENA include the lack of financial intermediation for SME financing, mismatches between humanitarian-led aid systems and private sector mobilization, and regulatory constraints and risks. However, opportunities to further develop blended finance in MENA include experimentation with different vehicles and financing models to enhance private sector mobilization, particularly in more fragile MENA states, and boosting education to help draw in local institutional investors, philanthropy, and grant-makers. Potential topics in MENA for further exploration include the how best to align Islamic finance with blended finance, and the potential role of sovereign wealth funds in helping to scale SDG investment and blended finance in the region.

Glossary of Key Terms

BII: British International Investment.

BMZ: German Federal Ministry of Economic Cooperation and Development, Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung.

BLENDED FINANCE: The use of catalytic capital from public or philanthropic sources to increase private sector investment in developing countries to realize the Sustainable Development Goals (SDGs). Blended finance is a structuring approach, not an investment approach.

CLIMATE ADAPTATION FINANCE: Climate adaptation involves channeling investment to efforts focused on adjusting to the already apparent and expected effects of climate change. Such climate change effects include, but are not limited to, rising ocean levels, the increasing temperature of the oceans, the increased frequency and intensity of extreme weather events (hurricanes, droughts, monsoons), and irregular seasonality. Climate adaptation interventions are often linked to the concept of the improved "resiliency" of humankind to the changing biological, ecological and geological systems of the planet. The term resiliency encompasses, but is not limited to, resilient food systems, resilient livelihoods, and resilient natural systems, like biodiversity.

CLIMATE BLENDED FINANCE: The use of blended finance structures to deliver private sector investment to transactions that explicitly aim to produce outcomes that combat and/or respond to the effects of climate change in developing countries.

CLIMATE MITIGATION FINANCE: Climate mitigation finance consists of channeling investment towards interventions explicitly aimed at limiting the current level of GHG emission output produced by human activity to reduce the future consequences of climate change. It also involves investing in efforts dealing with the removal of GHG from the atmosphere through carbon sequestration methods.

EC: European Commission.

EIB: European Investment Bank.

KfW: Development Bank of Germany, Kreditanstalt für Wiederaufbau Bankengruppe.

MISSING MIDDLE: The "Missing Middle" or Small and Growing Businesses are commercially viable firms with growth potential. Yet, they typically encounter fundraising challenges because they are too big for microfinance, too small or high-risk for traditional banks, and could be unsuitable for venture capitalists.

MITIGATION BLENDED FINANCE: The use of blended finance structures to deliver private sector investment to climate mitigation transactions in developing countries.

OeEB: Development Bank of Austria, Oesterreichische Entwicklungsbank.

PROPARCO: French Development Finance Institution, Promotion et Participation pour la Coopération Économique.

SMEs: Small and Medium-sized Enterprises

Methodology & Notes

1. **Convergence's database:** Convergence maintains the largest and most detailed database of blended finance transactions that have reached financial close. Given the current state of information sharing, it is not possible for this database to be fully comprehensive. We have made efforts to capture all relevant blended finance transactions; however, there are likely more transactions that have not been captured.
2. **Scope of available data:** This brief analyzes 83 blended finance transactions targeting the Middle East and North Africa, defined according to the World Bank categorization. It includes Algeria, Bahrain, Djibouti, Egypt, Iran, Iraq, Jordan, Kuwait, Lebanon, Libya, Morocco, Oman, Qatar, Saudi Arabia, Syria, Tunisia, United Arab Emirates, West Bank and Gaza, and Yemen. This brief also draws upon stakeholder interviews conducted with Frannie Leautier, Senior Partner & Chief Executive Officer, SouthBridge Investments; Maurits Fliehe Boeschoten, Senior Advisor, FMO – Dutch Development Bank; Rabih Yazbeck, Senior Vice President of Programs & Impact, Near East Foundation; Ennis Rimawi, Managing Director, Catalyst Climate Investment Management; Nadia Boumeziout, Head of Sustainability & Information Governance, Middle East, Zurich Insurance; Fernando Rodrigues, Head of Private Sector Operations, North Africa, African Development Bank; Khawaja Aftab Ahmed, Regional Director for the Middle East, Afghanistan, and Pakistan, International Finance Corporation; and Lama Kiyasseh, Country & Investment Risk, Multilateral Investment Guarantee Agency.
3. **Target regions and countries:** Convergence tracks region and country data by stated region(s) and countries of focus at the time of financial close, not actual investment flows. Often, regions and countries of eligibility are broader than those explicitly stated.

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INTERVIEWEES:

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CONVERGENCE
BLENDING GLOBAL FINANCE

CONVERGENCE is the global network for blended finance. We generate blended finance data, intelligence, and deal flow to increase private sector investment in developing countries.

BLENDED FINANCE uses catalytic capital from public or philanthropic sources to scale up private sector investment in emerging markets to realize the SDGs.

Our **GLOBAL MEMBERSHIP** includes public, private, and philanthropic investors as well as sponsors of transactions and funds. We offer this community a curated, online platform to connect with each other on blended finance transactions in progress, as well as exclusive access to original market intelligence and knowledge products such as case studies, reports, trainings, and webinars. To accelerate advances in the field, Convergence also provides grants for the design of vehicles that could attract private capital to global development at scale.