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ACCELERATING INSTITUTIONAL INVESTMENT FOR DEVELOPMENT IMPACT AT SCALE: LEARNING BRIEF

March 2022

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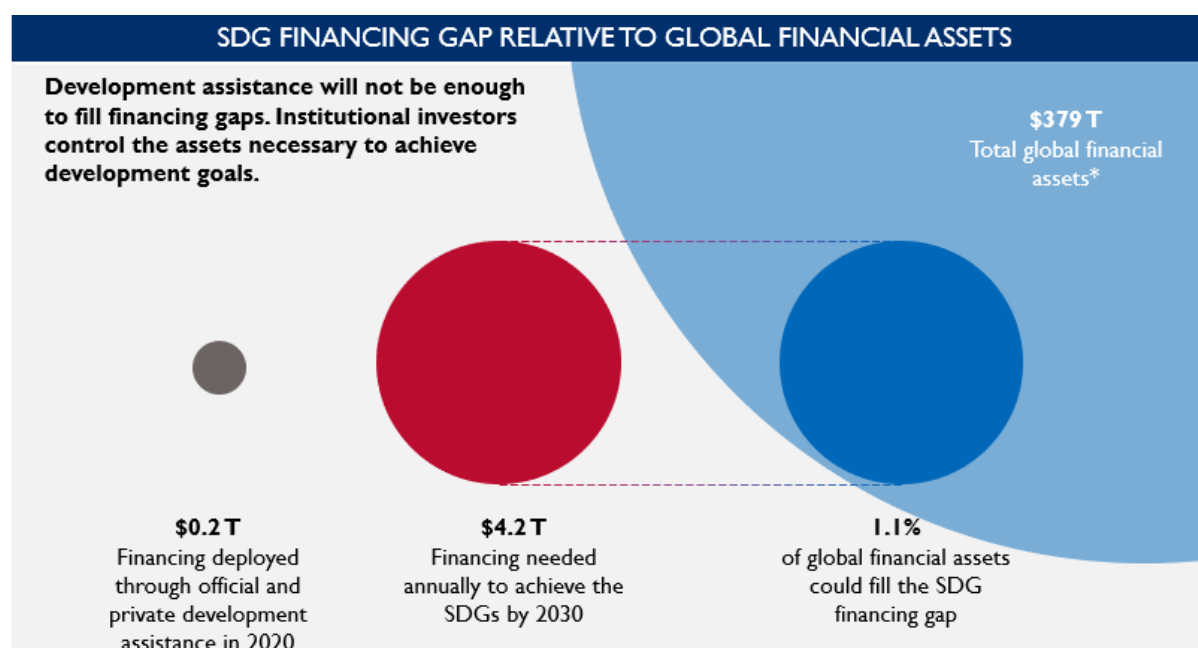
ACRONYMS AND ABBREVIATIONS

AOFSA	Asset Owners of South Africa
CRRH	Caisse Régionale De Refinancement Hypothécaire
COVID	Coronavirus Disease
DFI	Development Finance Institutions
ESG	Environmental, Social, And Governance
GDP	Gross Domestic Product
GEMs	Global Emerging Markets Risk Database
IFC	International Finance Corporation
MDB	Multilateral Development Bank
NGO	Non-Governmental Organization
ODA	Official Development Assistance
OECD	Organization for Economic Co-Operation and Development
RAAI	Responsible Asset Allocator Initiative
SDGs	Sustainable Development Goals
UN	United Nations
USAID	United States Agency for International Development
USD	United States Dollars
USG	United States Government

EXECUTIVE SUMMARY

Accelerating institutional investment is essential to achieving the Sustainable Development Goals (SDGs). The widening SDG financing gap has only been exacerbated by COVID and is currently estimated at USD 4.2 trillion. With official development assistance estimated at USD 161 billion, an all-time high, the development community must rely on alternative sources of funding. Globally, USD 379 trillion is held in financial assets. [1] With 80 percent of this held in developed economies, there is massive opportunity to reallocate even just a small portion of these assets to fill the SDG financing gap. [2] With emerging market GDP growth outpacing that of developed economies, 6.5 percent compared to 5.0 percent respectively, and this trend set to continue into the foreseeable future, emerging markets could be an attractive destination for institutional investors who typically seek longer-term investments if barriers to investment can be overcome.[3] The longer-term, larger investments of institutional investors are particularly well-suited to drive development impact in sectors such as sustainable infrastructure which require patient capital. Moreover, institutional investors in their own right are becoming increasingly interested in ensuring that their investments drive social impact, as illustrated by initiatives such as the Principles for Responsible Investment and Net Zero Asset Managers initiative which aim to integrate environmental, social, and governance (ESG) factors into investment decision making.



* $379 T represents financial assets held by all financial entities including bank deposits, cash, bonds, etc. $184 T represents financial assets held by all financial institutions that are not central banks, banks or public financial institutions, a closer estimate of assets held by asset managers and institutional investors.

Despite the potential for accelerating institutional investment, several barriers must be addressed, including internal barriers related to investors themselves and external barriers related to the emerging market ecosystem and transactions. To begin with, institutional investors seek low-risk investments and have rigid mandates, since they are first and foremost responsible for ensuring that they can meet their long-term liabilities (e.g., pension payouts in retirement). Moreover, because institutional investors have historically invested in developed markets, it is difficult for them to overcome this inertia and the lack of emerging market awareness, access, and capabilities that comes with this. Intersecting with these internal barriers are external barriers related to the emerging market environment and transactions. These include real or perceived risks of investments and returns, underdeveloped investment pipelines, lack of reliable information,

lack of liquidity, lack of ecosystem intermediaries, both specific and unclear regulatory requirements, and sub-investment grade credit ratings, and high costs to private transactions.[4] Until these barriers are appropriately addressed, institutional investors have little incentive to invest in emerging market contexts that are outside of their status quo.

Donors can play a critical role in removing barriers and providing support to institutional investors by addressing information asymmetries, managing and reallocating risk, and reducing transaction costs. To address information asymmetries, donors can support generation of trusted, relevant insights and disseminate these to institutional investors through the following interventions:

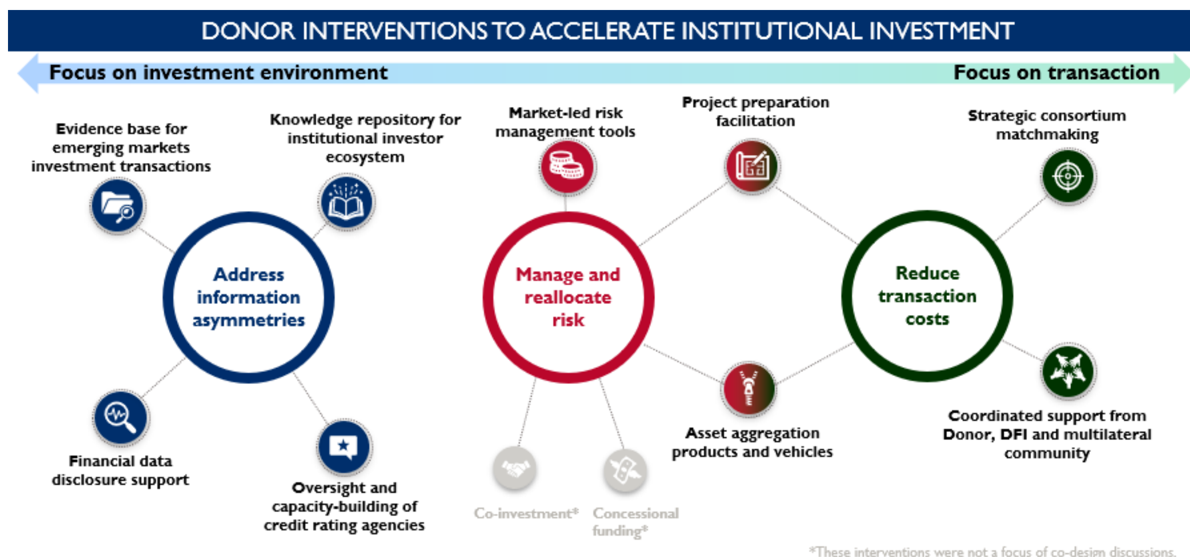
- Evidence base for emerging market investment transactions
- Knowledge repository for institutional investor ecosystem
- Financial data disclosure support
- Oversight and capacity-building of issuers and credit rating agencies

To manage and reallocate risk, donors can scale risk management tools and asset aggregation through the following interventions:

- Market-led risk management tools
- Asset aggregation products and vehicles

To reduce transaction costs, donors can convene the development and investor community strategically and target project preparation through the following interventions:

- Coordinated Support from Donor, DFI and multilateral community
- Strategic consortium matchmaking
- Project preparation facilitation



To maximize additionality and impact, donors must focus on how to deliver interventions strategically: in combinations, that prioritize for scale, through intentional coordination within the donor community, and which utilize appropriate impact management and measurement methods. Donors should combine key interventions to provide complimentary services which result in more effective investment acceleration together than they would have alone. To create lasting changes in risk-return for institutional investors, donors should prioritize interventions that drive change at a market level rather than on a single-project level. To maximize the effectiveness of donor inputs, donors should coordinate to harness each actor's unique skill set and scale support activities. When measuring and managing impact, donors should utilize metrics that will generate interest from institutional investors in impactful investing

To maximize additionality and impact, donors should deploy interventions…

…in **combinations…**

…that prioritize for **scale…**

…and in **coordination with other donors.**

This learning brief offers a clear justification for the role of donors in accelerating institutional investors to drive development impact at scale. The brief lays out the necessity of increased institutional investment to reach development goals, followed by practical interventions for donors to accelerating this institutional capital. Finally, the report provides operational recommendations for how donors should deploy these interventions.

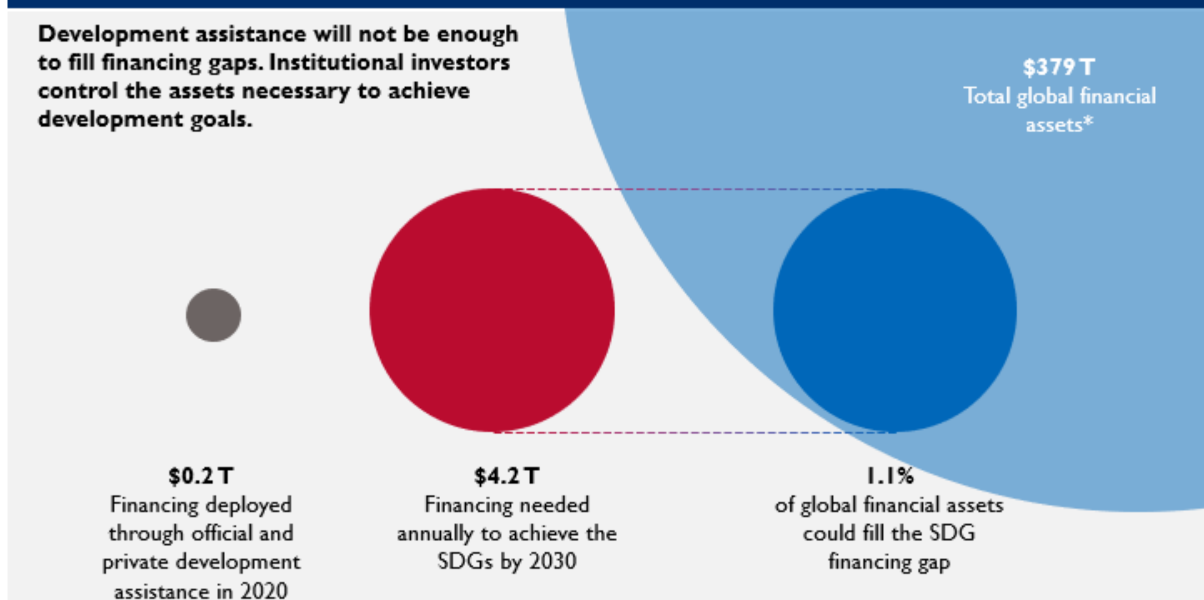
1 WHY IS ACCELERATION OF INSTITUTIONAL INVESTORS NECESSARY TO REACH DEVELOPMENT GOALS?

There is a significant need for greater volumes of capital to achieve development goals in emerging and frontier markets, a need further exacerbated by the COVID-19 pandemic shock. This capital will need to come from currently untapped, large sources that have traditionally been absent from emerging markets. Moreover, the need is urgent, with financing for sustainable development at risk of collapse due to COVID-19 and all resources available to developing countries under stress.[5] Historically, the widening SDG financing gap can be attributable to not only increasing needs but also declining resources, and this has been magnified due to the pandemic. COVID-19 has led to the first rise in extreme poverty in a generation, with an additional 120 million people pushed back into extreme poverty in 2020.[6]

> **"We have to evolve, from a relationship based mostly on aid, to one based on trade. We must strengthen private sector ties between our countries, spur economic investment at a scale that could never be matched by foreign aid."**
>
> *USAID Administrator Samantha Power on financing new pathways to a stronger U.S.-Africa Economic Partnership*

Developing countries are set to see a USD 700 billion drop in external private finance resulting in increased risk of climate disaster, increased poverty levels, and exacerbated inequality.[7] Taken alongside an estimated USD 1 trillion in emergency response spending in developing countries, COVID-19 is estimated to exacerbate the SDG financing gap to USD 4.2 trillion, which represents a 70% increase from pre-pandemic estimates.[8] As shown in Figure 1, official development assistance (ODA), despite having reached an all-time high of USD 161.2 billion in 2020, does not come remotely close to filling this gap.[9] Furthermore, private development assistance is estimated at less than a third of ODA, with roughly USD 45 billion provided by non-public sources like foundations, corporations, and NGOs.[10]

FIGURE 1: SDG FINANCING GAP RELATIVE TO GLOBAL FINANCIAL ASSETS



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Institutional investors are a critical source of financing to reach development goals. Institutional investors pool and manage individual sources of capital, seeking lower-risk, longer-term investment opportunities (see Box 1). Financial institutions that are not central banks, banks, or public financial institutions hold USD 184 trillion in financial assets, a rough estimate of the assets held by institutional investors and asset managers.[13] Institutional investors and asset managers – those actors who manage capital on institutional investors' behalf – could meet the global development financing gap by targeting just 2.3 percent of their investment towards the SDGs. [14] Currently, developing countries hold less than 20% of global financial assets despite representing 84% of the world's population, indicating a huge opportunity for the donor community to support institutional investors in reallocating their capital towards to drive impact in developing countries.[15] Institutional investors are well-suited to help reach development goals not only because of the scale of assets, but because of the longer-term, more stable nature of their investments. Climate-related investments and infrastructure require longer-term, patient investments. Further, developing countries require stable investments to develop capital markets that are resilient to economic downturns.

Box 1: *Who are institutional investors?*[16]

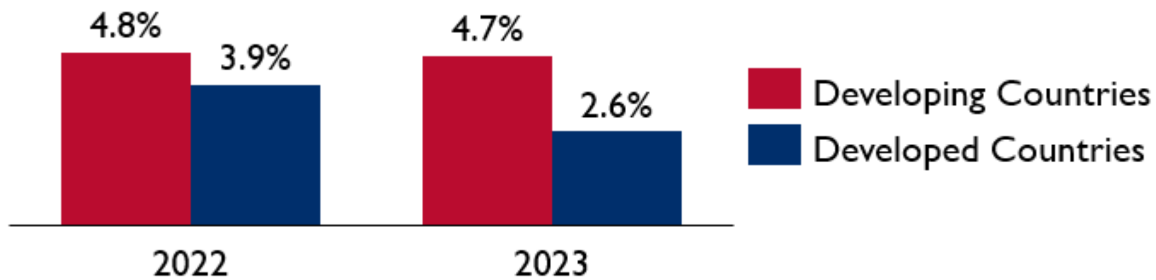
Institutional investors pool, manage, and invest others' investments, which means they typically hold a significant amount of assets to invest. The contributions that institutional investors pool can come from a variety of sources, including employers, unions, or other organizations (in the case of pensions); policy holders (in the case of insurance companies); and various government sources (in the case of sovereign wealth funds). Institutional investors have a low risk tolerance due to their long-term liabilities – for example, funds due to pensioners in retirement – and prefer investing with large sums at once due to managing a large amount of assets. Within institutional investors, there are varying mandates, constraints, and risk-return preferences, resulting in different methods of effective engagement by donors. Examples of institutional investors include pension funds, insurance companies, sovereign wealth funds, and asset managers (see Table 1). Institutional investors allocate significant capital to asset managers who make specific investment decisions on their behalf, particularly for private asset classes and smaller institutional investors, though it is worth noting that institutional investors are increasingly making direct investments. Institutional investors, particularly pensions in the US, often rely on investment consultants to advise asset allocation and investment decisions.

Table 1: Key Actors in the Institutional Investor Ecosystem

	Actor	Description[17]	AUM (2021)	Examples
Institutional Investors	Pensions	Pensions invest contributions from policyholders to pay future retirement benefits. Pensions are risk-averse, long-term investors due to their responsibilities to beneficiaries. Pensions often represents the largest type of institutional investor in many countries.	$56 trillion[18] ($350bn assets in Sub-Saharan Africa in 2018[19])	APG, CalSTRS, CPP
Institutional Investors	Insurance Companies	Insurance companies invest premium payments from policyholders to provide funding for future claims. Insurance companies are risk-averse and invest directly.	$40 trillion[20]	Allianz, Prudential, Sanlam
Institutional Investors	Sovereign Wealth Funds	Sovereign wealth funds invest money generated by the country's government. Typically, sovereign wealth funds have a higher risk tolerance and preference for returns than other institutional investors.	$10.53 trillion[21]	ADIA (Abu Dhabi), CIC (China), NSIA (Nigeria)
Intermediaries	Asset Managers	Asset managers are often hired by Institutional investors to coordinate and oversee investment portfolios.	~ $69.2 trillion[22]	BlackRock, CPP Investments, PGGM
Intermediaries	Investment Consultants	Investment consultants advise institutional investors on asset allocation and investment decisions.	$47.14 trillion[23]	Cambridge Associates, Mercer, Russell Investments

Emerging markets are an increasingly promising investment opportunity for institutional investors. For institutional investors that have traditionally invested in developed markets, emerging markets represent a way to diversify their portfolios. While yields on emerging market assets can be greater, this is primarily attributable to higher risk – which, as discussed, is less of a draw for institutional investors – and greater growth. In the International Monetary Fund's most recent World Economic Outlook, GDP growth in developing economies for 2021 was estimated at 6.5 percent, compared to 5.0 percent for developed economies. While growth globally is projected to moderate in the near-term, largely due to COVID, emerging market and developing economies are still expected to continue to outperform advanced economies in terms of GDP growth rate, 4.8 percent compared to 3.9 percent in 2022, and 4.7 percent compared to 2.6 percent in 2023, respectively (See Figure 2).[24] The fact that this trend of emerging markets outperforming advanced economies is set to continue aligns well to institutional investor preferences to match long-term investments to long-term liabilities. In summary, emerging markets have been attractive to institutional investors due to the wider investment opportunity set, higher longer-term growth potential, and broader diversification, and this is evidenced by institutional investors increasing their allocations to emerging markets since the 1990's.[25] Despite this increase in asset allocation, institutional investors still only invest 20 percent of their assets in developing countries.[26] With respect to US pension fund investment in Africa in particular, less than 1 percent of their USD 18.8 trillion is being invested in Africa.[27]

FIGURE 2: DEVELOPING ECONOMIES ARE PROJECTED TO HAVE GREATER GDP GROWTH RATES



Emerging markets investments that create development impact have potential to be attractive to institutional investors. Institutional investors increasingly value driving social impact through their investment, as evidenced by many large institutional investors publicly committing to integrate ESG (environmental, social, and governance) factors into their investment decisions. In early 2005, a 20-person investor group was assembled by then UN Secretary General Kofi Annan to develop the Principles for Responsible Investment, a body that today includes nearly 4,800 signatories in over 60 count ries representing more than USD 120 trillion in assets. The goals of the initiative continue to be to understand the investment implications of ESG issues and integrate these into investment decisions.[28] Of the 4,800 signatories to PRI, 14 percent are institutional investors, 75 percent are asset managers, and 10 percent are service providers.[29] In addition to PRI, the Net Zero Asset Managers initiative launched more recently in December 2020 in an effort to galvanize the asset management industry to commit to a goal of net zero emissions. Governed by six investor networks (of which PRI is one), the Net Zero Asset Managers initiative currently has 236 signatories representing USD 57.5 trillion in assets under management.[30] In an effort to identify best practices, the Responsible Asset Allocator Initiative (RAAI) provides the RAAI index to analyze and assess the investment practices of sovereign wealth funds and government pension funds. The most recent indexing cites an average global RAAI score of 52 percent, which has continued to rise steadily from 44 percent in 2017.[31]

Despite the opportunity, there are critical barriers which deter institutional investors from investing in emerging markets. Institutional investment in emerging markets has been hindered by a multitude of barriers, both real and perceived, which can relate to the institutional investor itself or to the broader environment or transaction.[32] Internally, institutional investors face barriers related to a limited risk appetite, rigid policies and mandates, lack of awareness and access, and lack of capabilities and expertise. These internal barriers intersect with external barriers related to the emerging market investment environment and transactions. These include real or perceived risks of investments and returns, underdeveloped investment pipelines, lack of reliable information, lack of liquidity, lack of ecosystem intermediaries, both specific and unclear regulatory requirements, and sub-investment grade credit ratings, and high costs to private transactions.[33] In the sections that follow in this learning brief, donor support interventions speak to the multitude of these barriers, addressing how to support institutional investors' internal barriers as well as those barriers related to the external investment environment, including both the broader ecosystem and transactions more specifically. These donor support interventions can broadly be understood in three broad categories:

Less than 1% of US institutional investors' USD 18.8 trillion is being invested in Africa

1. **Addressing Information asymmetries**, which addresses the lack of investment-related data, lack of relationships and experience from investors, and limited track record of projects,

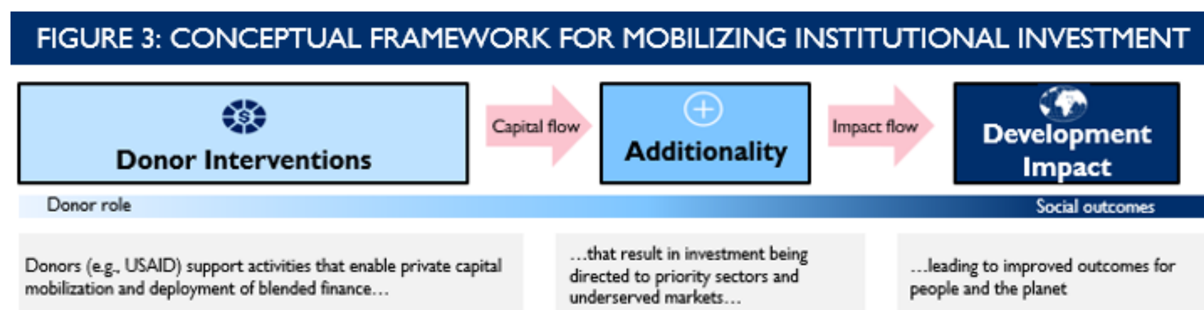
resulting in difficulty assessing potential investment performance and consequently higher perceived risk for investors.

2. **Managing and reallocating risk**, which addresses the context by which emerging markets involve currency risk and greater political risk, and institutional investors lack an understanding of possible risk mitigation tools. As a result, institutional investors perceive that high risk prohibits emerging market investment.
3. **Reducing transaction costs**, which addresses the fact that deal sourcing, partnership building, and investment management come with new and higher costs in markets in which an investor has limited experience or footprint.

II WHAT CAN DONORS DO TO ACCELERATE INSTITUTIONAL INVESTMENT FOR DEVELOPMENT?

USAID and other donors can play a key role in mobilizing institutional investment to achieve development impact. Donors are uniquely positioned to play this role due to their power to coordinate actors within the development ecosystem, ability to take on and transfer high levels of risk, expertise/footprint in emerging markets, and mandate for development impact.[34] Leveraging this positioning, donors can provide essential support – both directly and through implementing partners – to shift the risk-return expectations for institutional investors, enabling them to make investments in emerging markets which would not have occurred otherwise. Moreover, investments in priority sectors, such as sustainable infrastructure and real estate, lead to development impact in the form of increased incomes and livelihoods, access to products and services, equity, and climate benefits. This impact pathway of how donor interventions lead to additionality which leads to development impact is illustrated in the conceptual framework for mobilizing institutional investment (see Figure 3).[35]

FIGURE 3: CONCEPTUAL FRAMEWORK FOR MOBILIZING INSTITUTIONAL INVESTMENT



Donor interventions create additionality when they attract institutional capital that otherwise would not invest in transactions that create development impact. Additionality is defined as achievement of a goal that would not have happened without donor intervention. For additionality to be present, it is important to be confident that donor efforts are not replacing private sector or market actors since this would have a distortionary rather than catalytic effect. There are two categories of additionality: financial additionality and ecosystem additionality.

More details on additionality can be found in the Using Blended Finance To Generate Additionality And Human Impact: Guidance Note[36]. While blended finance can be broadly understood as the use of capital from public or philanthropic sources to increase private sector investment in sustainable development, the conceptual framework can be applied more narrowly to institutional investment as a subset of the private capital flows being mobilized.

Financial additionality mobilizes institutional capital into transactions that it otherwise would not have participated in. When donors create financial additionality, investment projects receive financing that otherwise was not available at similar terms, at similar quantities, or for similar development purposes. Examples of types of financial additionality include:

- Innovative financial structures which shift the risk-return for institutional investors
- Risk mitigation tools increase likelihood of returns
- Resource mobilization which coordinates and catalyzes investments

Example of Donors Creating Financial Additionality: Bayfront Infrastructure

The Asian Development created an **innovative financial instrument** which allows foreign institutional investors to invest in Asian infrastructure projects

Ecosystem additionality leads to benefits at the policy, regulatory, sector, and business activity levels. When donors create ecosystem additionality, institutional investors operate in a more knowledgeable or efficient investment environment. Examples of types of ecosystem additionality include:

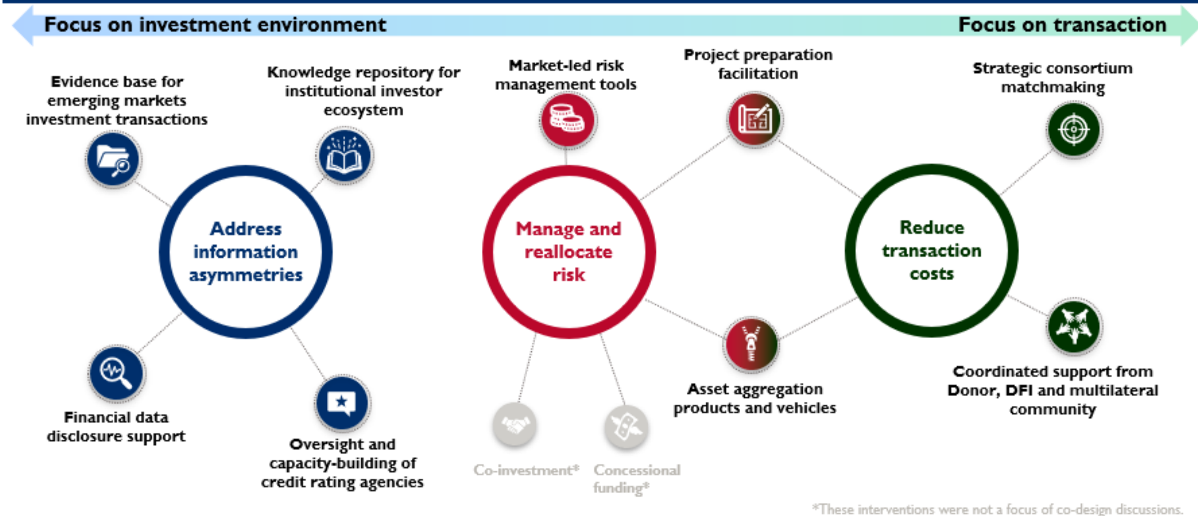
- Demonstration effects which involve showcasing innovative blended finance projects to incentivize replication
- Sector-wide growth which involves building the capacity of businesses, funds, and intermediaries in a previously underdeveloped sector
- Policy, institutional, or regulatory change to enhance institutional investment opportunities

Example of Donors Creating Ecosystem Additionality: Asset Owners of South Africa

USAID, in partnership with MiDA and CrossBoundary, **developed the pension ecosystem in SA**, increasing coordination in investments and creating potential for demonstration effects which lead other pensions to invest in infrastructure.

Development impact is the long-term social effect of the additionality from institutional investment. The conceptual framework aligns these impacts to the SDGs across four categories: income and livelihoods, access to basic products and services, equity and empowerment, and climate and environmental benefits.

Donors can deploy the following interventions to address key barriers and shift the risk-return calculus for institutional investors. Donor interventions were generated through extensive desk research, 20+ expert interviews, and a multi-week co-design series with donors, implementers, and experts in mobilization of capital.



Evidence base for emerging market investment transactions

Barrier to address

Institutional investors are lack awareness of how they could successfully invest in emerging markets, due to a lack of accessible information about the emerging markets investment performance and available donor support activities.[37] Donors lack awareness of successful efforts to mobilize institutional investors, making it difficult to scale successful mobilization efforts. There is no systematic evidence base which fills this investor and donor knowledge gap and provides knowledge on best practices for emerging markets investing.[38]

Detailed intervention

To address this lack of evidence, donors can organize consistent touchpoints between the development community and institutional investor ecosystem to collect information on successful emerging markets transactions and high-additionality donor efforts. To clarify available support for institutional investors, donors can organize the variety of available risk-management tools that IIs can utilize for emerging markets investment and channels to access these.

Knowledge repository for institutional investor ecosystem

Barrier to address

There is currently a lack of organized, accessible information for institutional investment in emerging markets and lessons learned during investing. [39] Donors and implementers mention that mobilization successes are not clearly consolidated and communicated to investors, resulting in institutional investor's lack of comfort with entering emerging markets.

Detailed intervention

Development actors can create a widely accessible repository of emerging markets investment information that includes lessons and examples for entering emerging markets, key actors in the donor and investor space, and available donor support. Particularly, the repository can include emerging market investment lessons and successes to create demonstration effects and clarify how institutional investors should enter emerging markets. [40] Additionally, the repository can include key actors/relationships in the donor and institutional investor ecosystem and available donor support

for investments, particularly risk management instruments.

Donors can enhance existing efforts to collect lessons and data relevant for institutional investors such as the OECD Financing for Sustainable Development Website and World Bank Private Participation in Infrastructure Database, by including lessons for investing in emerging markets and organizing available donor resources such as risk management tools.

Financial data disclosure support

Barrier to address

The main factors that influence investment decision-making of institutional investors are past performance of an asset class, previous success/failures with similar investments, and expected return from the asset class.[41] Private investments in emerging markets often provide non-standardized, limited and unreliable information.[42] As a result, institutional investors, who particularly demand standardization of reporting, struggle to accurately assess risk of investment and remain hesitant to invest in emerging markets and alternative asset classes.[43]

Detailed intervention

Donors can encourage multilateral development banks and development finance institutions to disclose their data on loans and repayment to increase investor's ability to assess emerging markets investments. The Global Emerging Markets Risk Database (GEMS) is one example of pooling together data from MDBs and DFIs to increase financial transparency in emerging markets and can be built upon to increase access to private investors (See GEMS Description on Page 15). In addition, donors should subsidize and/or co-develop emerging markets data with data collection agencies and market intelligence providers (e.g., supplementing the work of UN statistical services). At a policy level, donors can facilitate initiatives to make financial reports consistently available in order to enable accurate credit ratings (e.g. emulating the South African municipal borrowing bulletin which publishes public debt financial data quarterly).

Oversight and capacity building of issuers and credit rating agencies

Barrier to address

Institutional investors rely on credit ratings to assess risk of investing in emerging markets, particularly seeking investment-grade assets[1] due to their low-risk preferences. However, the sovereign ratings for most emerging markets are sub-investment grade and these sovereign ratings create ceilings for the ratings of other assets in the country. One reason for these low ratings is that large credit rating

Detailed intervention

To improve the data available for credit ratings, donors can work with regulators, both at the regional and global levels, to improve information disclosures for companies, projects, and public institutions that can be used by credit rating agencies when assessing risk. On the issuer side for credit ratings, donors can engage issuers (i.e., companies who seek credit ratings for their assets) by educating them on the ratings process

[1] An investment-grade rating signifies that a bond has a relatively low risk of default, namely bonds receiving a rating above Baa (by Moody's) or BBB (by S&P and Fitch).

agencies biased ratings downwards in emerging markets when information was inaccessible or lower quality, since it was reputationally safer for them to provide a credit rating that under-promises but over-delivers, rather than vice versa.[44] To illustrate, the credit ratings of developing countries were downgraded more extensively than those of developed countries despite worse economic performance of developed countries as a result of COVID-19, with advanced economies contracting and increasing their debt ratio more drastically than emerging and developing economies.[45] These more extensive downgrades, which were assessed as not justified from an economic point of view, result in institutional investors perceiving greater risk than actually exists, inhibiting investment in emerging markets.[46]

and create a structured approach to collect/disclose the right information and data for accurate ratings. To capacitate local credit rating agencies and lead to more accurate rating of assets, donors can support global and local talent exchanges in which credit rating agencies share technical expertise and on-the-ground knowledge. In addition, guarantees, in particular by highly rated MDBs and DFIs, can provide substantial support to improve the credit rating of a vehicle portfolio.[47] (For more on guarantees and other risk management instruments, see the Market-led risk management tools intervention.)

To manage and reallocate risk, donors can scale risk management tools and asset aggregation

Market led risk management tools

Barrier to address	Detailed intervention
Emerging market investments often involves greater currency, political, and country risk than domestic, developed market investment.[48] Recall that institutional investors in particular are typically more risk-averse due to responsibilities to dependents such as pension plan holders. While risk management solutions exist for institutional investors, they struggle to access or utilize these. Current risk management tools provided by donors are expensive, difficult to access and utilize, and not well-known by institutional investors.[49]	Donors can educate and build awareness about existing risk management tools, such as guarantees provided by the Development Finance Corporation, as there is a current lack of awareness and connection to available risk management tools for investors[50]. For forex de-risking, which is particularly relevant for foreign institutional investors, donors can support scale of existing forex hedging solutions such as The Currency Exchange to transfer currency risk from investors to development assistance organizations. Additionally, donors can work with implementing partners to support local exchange listing and trading of forex derivatives, instruments which allow institutional investors easy access to hedge against currency risk, which would in turn help to develop local capital markets.

Asset aggregation products and vehicles

Barrier to address	Detailed intervention
Institutional investors are not equipped to diligence opportunities and invest on a single-project basis. Institutional investors hold large amounts of capital and invest with large amounts	To reduce transaction costs associated with sourcing and diligencing single projects, donors can support the aggregation of investments into a portfolio. Aggregation of assets creates

at once. As a result, institutional investors require large or consolidated investment opportunities, as they do not have the risk appetite for individual projects or the capacity to research several small investments to deploy their capital.[51]

opportunities which satisfies IIs' requirement of large ticket sizes and leads to a more diversified investment opportunity. Further, aggregated assets can be securitized[2] to satisfy the needs of investors with various risk appetite and ticket size preferences. To aggregate assets to create lower-risk investment products and vehicles, donors can support use of simple aggregation instruments, such as listed investment trusts in which investors can buy shares of a fund that is listed on the market. Additionally, donors can support and strengthen local and regional institutions already involved in intermediation for aggregating assets (e.g., Development Bank of South Africa Infrastructure Fund) rather than taking a portfolio of assets and securitizing from scratch. (See CRRH Description on Page 15 for an example of how donors can support local African asset aggregation and listing on U.S. capital markets.)

To reduce transaction costs, donors can convene the development and investor community strategically and target project preparation

Coordinated Support from Donor, DFI and multilateral community

Barrier to address

The investment mobilization space lacks coordination in goals, activities, and partnership opportunities. Donors, DFIs, MBDs, and other development assistance actors do not effectively coordinate their mobilization effort, resulting in missed opportunities to pool resources and scale support activities. [52] The lack of coordination makes development assistance actors less strategic in providing support that addresses gaps in the ecosystem and more likely to provide less effective, duplicative interventions.

Detailed intervention

Donors can convene key stakeholders in blended finance (DFIs, MDBs, other donors, etc.) periodically to reduce isolation among stakeholder efforts. At an international level, donors could consider supporting the creation of a neutral institution to connect actors in the institutional investment ecosystem and champion change within OECD and G7. Withing MDBs and DFIs, donors can target a shift at the governance level to focus on mobilizing private investment rather than deploying the organization's resources. To leverage the specialized resources of other organizations, donors can collaborate with guarantors such as DFC to support provision of guarantees where risk is prohibitive.

Strategic consortium matchmaking

Barrier to address

Consortiums find it difficult to source investments which would satisfy varying

Detailed intervention

To create more effective investment consortiums, donors can determine

[2] **Securitization is the process in which certain types of assets are pooled so that they can be repackag**ed into interest-bearing securities

investment preferences of their members, such as varying risk appetites, asset class preferences, and liquidity requirements. As a result, consortiums have struggled to source and close investment transactions.[53] In addition, local institutional investors, which are often smaller frequently lack the capacity to venture into big-ticket projects commonly found in infrastructure.[54]

commonalities and engage institutional investors based on key characteristics such as mandates, risk appetites, asset class preferences, liquidity requirements, and tenor/return expectations. Particularly, donors can prioritize connection of local and global institutional investors to facilitate exchange of on-the-ground knowledge and technical skills. For more effective decision-making, donors can support establishment of common fund structures and expand the use of fund managers who understand the landscape in the emerging market context.
To illustrate strategic consortium matchmaking, the Asset Owners of South Africa (AOFSA) selected larger local pension funds that were willing to invest in South African infrastructure and able to create demonstration effects for smaller, less-experienced pensions. To tailor investment opportunities, consortium organizers developed a pipeline of opportunities that were aligned to common investor preferences in terms of types of assets, timeline to deploy capital, investment instrument, and alignment to impact goals.

Project Preparation Facilitation

Barrier to address

Institutional investors experience a lack of investable infrastructure deals in part due to insufficient project preparation, particularly at early stages. Large infrastructure projects require a great deal of planning in the pre-investment phase, including studies that address the technical, environmental, social, financial, and legal challenges associated with a project.[55] Poor project preparation at early stages is a critical driver of infrastructure project failure rates, especially for projects in sectors like transport and water.[56] In the Global Infrastructure Hub Project Pipeline, 61/74 stalled infrastructure projects are halted in the first two phases of concept and feasibility.[57] However, few infrastructure project preparation facilities focus consistently on the earliest stages in emerging markets, making quality project preparation expensive and/or difficult to access.[58]

Detailed intervention

When supporting project preparation, donors can identify projects which would lead to demonstration effects in the investor ecosystem and target donor efforts where they would be most additional — during the earliest stages of the project (concept and feasibility). To streamline bureaucracy which often stalls projects, donors can leverage their close relationships with governmental organizations.[59] Further, donors can draft targeted landscape research that responds to stakeholder needs to avoid ignored/repetitive reports and provide technical assistance which may not otherwise be accessible such as specialized feasibility studies.

III HOW SHOULD DONORS DELIVER THESE INTERVENTIONS?

When delivering these interventions, donors should deploy interventions in combinations that prioritize for scale while focusing on how coordination can be most additional. Four operating principles for donors to deploy interventions that maximize investment that would not have occurred otherwise and development impact:

- **Recommendation 1: Deliver interventions in combination:** While each unique intervention drives towards additionality and impact, it is important to recognize when delivering interventions together might result in the combination being greater than the sum of its parts. Donors should combine key interventions to enhance additionality, providing complimentary services to overcome critical barriers to investment.
- **Recommendation 2: Prioritize scale:** Though every intervention that leads to ecosystem or financial outcomes is additional, some outcomes may not scale as much as others. With that in mind, donors should prioritize interventions that drive change at a market or platform level rather than on a single-project level to create lasting changes in risk-return for institutional investors. Certain interventions, when combined, have amplified potential to result in aggregation, replicability, and demonstration effects.
- **Recommendation 3: Coordinate activity much more intentionally across the donor community:** Each donor brings a unique knowledge set, reputation, resource set, and network of connections. Greater donor coordination allows for greater scale and organization of donor activities, ensuring that donor inputs are maximized for additionality. Failing to effectively coordinate the value that each donor brings may result in redundancies in support provisions, lack of clarity in vision, not maximizing resources for support, and a prolonged process to achieving additionality.
- **Recommendation 4: Utilize impact management and measurement methods that adapt to the unique realities of institutional investors:** Many institutional investors are early in their journey of investing for impact, a journey which goes from awareness to understanding to the investment transaction itself. To move investors along this journey, metrics should be simple, aligned to any impact-related interests of the investor, and focus on direct outputs of activities to show evidence of progress that will generate further investor interest. Without these institutional investor-focused considerations, the metrics collected may fail to enable demonstration effects, as they would be seen as too complex or irrelevant for investor interests.

III.I DONOR INITIATIVE SHOWCASES

The following initiatives illustrate combinations of interventions that have potential for scale and use donor coordination to effectively shift the risk-return calculation for institutional investors. Donors can take lessons from and/or scale these interventions to also create additionality and impact.

CRRH Bond Issuance with DFC Guarantee
A West African regional mortgage re-financing company is issuing a bond in the U.S. to raise long-term capital for mortgages at a lower cost than was available in West Africa, with support from USAID, DFC, MiDA, and CrossBoundary.[60] The mortgage company, Caisse Régionale de Refinancement Hypothécaire (CRRH), will raise USD 320 million in two capital market bond offerings with USD 256 million raised through bonds issued to U.S. institutional investors. *This transaction brings CRRH, a local African bond issuer, to U.S. capital markets for the first time. Access to U.S. capital markets is valuable because it has readily available long-term patient capital at lower interest*

rates than most developing countries. In Africa, local, long-term financing is in limited supply. As a result, mortgages are prohibitively expensive for many individuals and more broadly, companies struggle to access financing. This bond issuance allows CRRH to increase and diversify its investor base, decreasing their cost of capital and possibly increasing the affordability or mortgages in West Africa.

Combine interventions: To support this transaction, donors combined the following interventions: **asset aggregation products and vehicles** and **market-led risk management tools**. The transaction aggregates West African mortgages into a vehicle for issuing bonds on U.S. capital markets for easy access by U.S. institutional investors. To mitigate potential risk for U.S. investors, the DFC will provide an irrevocable, unconditional payment guaranty, meaning that if CRRH defaults on its debt, the DFC would make payments owed to U.S. investors. As a result, CRRH will be able to provide an investment opportunity for U.S. institutional investors that is easily accessible on U.S. capital markets, issued with the support of trustworthy actors, and large enough to satisfy investment needs.

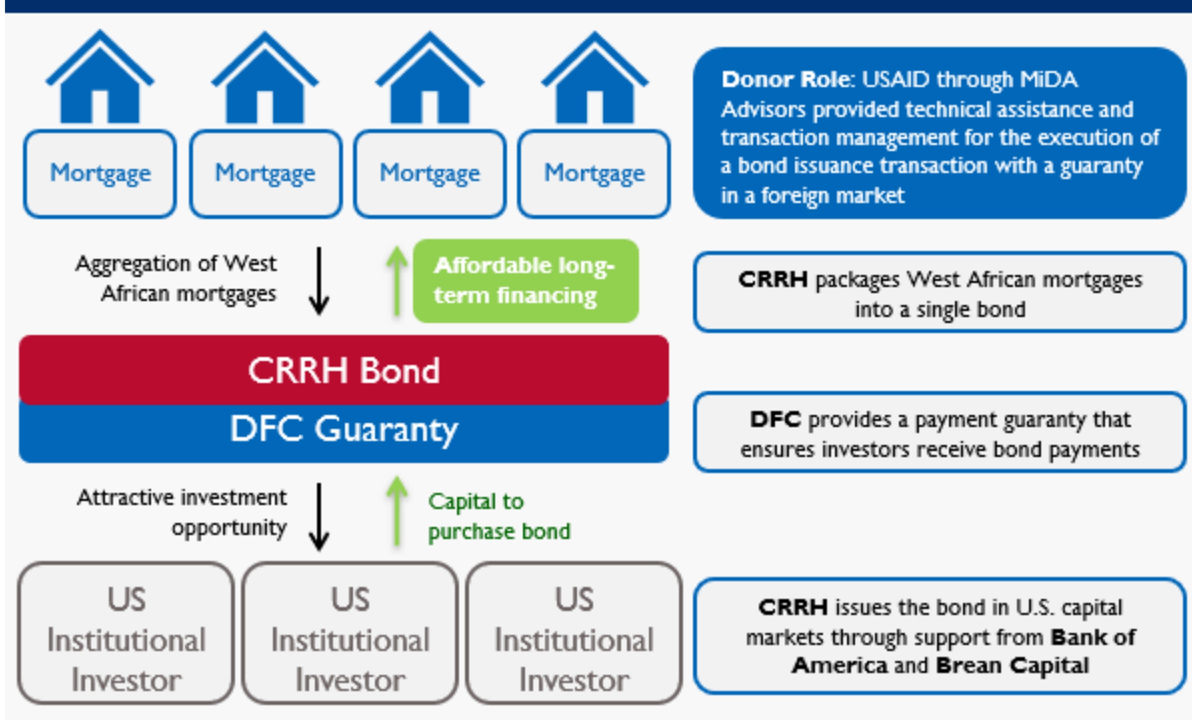
Donors and stakeholders recognized that securitizing assets into a bond would not be sufficient to get risk-averse institutional investors to invest, and that the de-risking guaranty instrument was necessary shift investors' risk-return calculus and generate investment.

Prioritize scale: The CRRH transaction will demonstrate how local African issuers can access U.S. capital markets through a bond issuance and how bond issuances can develop local African capital markets through access to affordable financing. By exposing U.S. investors to attractive African investment opportunities, this transaction will help to strengthen relationships between the U.S. and African financial communities and scale up the use of U.S. institutional assets to help finance development in emerging markets going forward.

Donors can apply a similar transaction structure to harness the long-term affordable capital in advanced economies to support development of local capital markets in emerging economies.

Coordinate with other donors: Execution of this transaction required coordination amongst various implementors and development agencies: USAID partnered with MiDA Advisors and CrossBoundary — financial advisory firms that mobilize investment into Africa — to help CRRH tap into U.S. capital markets. The MiDA Advisors consortium supported the execution of the bond issuance including transaction support during due diligence for bond structuring and transaction management related to relationships and management. CrossBoundary will support the creation of the development impact assessment to identify the effect of this transaction on increasing access to affordable housing. Particularly critical for the success of this transaction, USAID and the US Development Finance Corporation (DFC) collaborated to provide a payment guaranty which will play a powerful role in increasing the confidence and ability of U.S. institutional investors to invest.

Donors can seek collaboration with other development agencies to utilize their comparative advantages and provide comprehensive interventions to address each key barrier to institutional investment.



The Global Emerging Markets Risk Database (GEMs)

The Global Emerging Markets Risk Database (GEMs) pools together data on credit defaults on loans extended by contributing MDBs and DFIs. In return, these contributing members receive greater transparency on the performance of emerging markets transactions.

The scarcity of readily available, standardized, and transparent high-quality data on investment projects in emerging markets has led to skewed risk perceptions and therefore sub-optimal investment decisions. By anchoring risk perceptions with actual data evidence, GEMs help unlock capital from MDBs and DFIs to fill these investment gaps.

Combine interventions: To create this database, donors combined the following interventions: **financial data disclosure support** and **coordinated support from Donor, DFI and multilateral community**. To improve financial data disclosure, GEMs collects data from MDBs and DFIs on defaults on loans extended, the migration of their clients' credit rating, and the recoveries on defaulted projects. In return, data contributors gain access to aggregate statistics on observed default rates, changes in ratings and recovery rates by geography, sector, time-period and other dimensions.

GEMs success required data disclosure from various MDBs and DFIs to maintain anonymity, highlighting how development actors can work together to collectively achieve more than they could do alone.

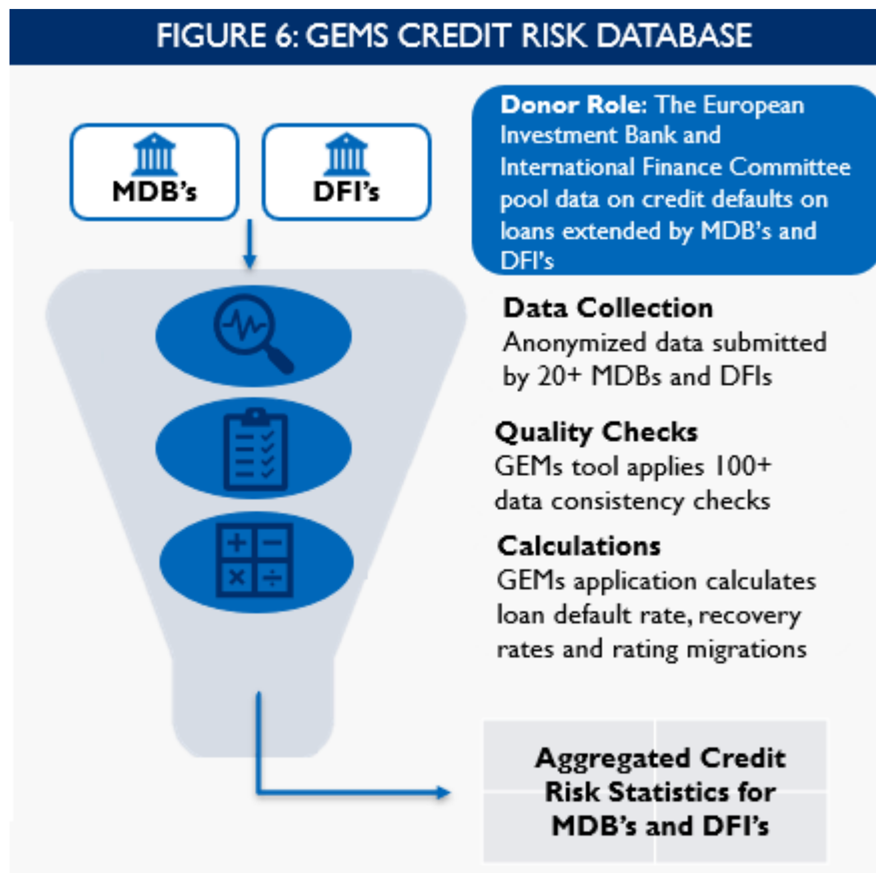
Prioritize scale: The historical returns and losses for DFI loans to private sector borrowers in developing countries captured in the GEMs Database have been better than credit rating agency and market perceptions suggest.[61] This discrepancy in expected and actual risk highlights how data disclosure could lead to a scaled recalibration of investor risk perceptions of emerging markets if the data is widely accessible.

To scale the effects of this effort and maximize additionality, donors can go support increasing investor access to GEMs and data disclosure. For example, GEMs can expand access to its database to institutional investors, allowing to recalibrate their risk expectations in emerging markets.[62] While the 2021 public

release of default statistics was a productive step forward for data transparency, private investors require greater nuance and disaggregation to assess risk of investment. [63] *Additionally, to increase the quality of the database, donors apply collective pressure to increase participation in data disclosure from other international finance organizations.*

Coordinate with other donors: Coordination among various development actors was critical to the establishment and success of GEMs. Since its establishment in 2009 as a joint initiative between the European Investment Bank and the International Finance Corporation (IFC – World Bank Group), the GEMs consortium has grown to include 25 members mainly comprised of MDBs and DFIs.

Further donor coordination would be helpful to apply collective pressure to expand access to GEMS outside of contributing DFIs and MDBs, particularly increasing access for private investors. [64]



Adapted from GEMS Risk Database

III.II METRICS CONSIDERATIONS FOR DONOR INTERVENTIONS TO MOBILIZE INSTITUTIONAL INVESTMENT

Donors should utilize impact measurement to shape ongoing support, to set and reset expectations, and to capacitate institutional investors and stakeholders themselves to target development impact more intentionally. The following metrics considerations allow donors to capture metrics which generate enthusiasm from institutional investors for participation in impactful investments and inform future donor support decisions.

1. **To capture outcomes which would generate enthusiasm for impactful investment among institutional investors, donors should focus on collecting simple metrics related to the direct output of activities.**[65] Direct outputs of donor activities are short-term metrics, such as increased institutional investor knowledge for a donor intervention

providing education, rather than longer-term outcomes such as transactions closed and amount of capital mobilized. Financial outcomes measure the longer-term goal of mobilization, not capturing the direct effects of many donor-supported activities which involve relationship-building, education, or ecosystem coordination. By focusing on outputs, especially in the near- and interim-term, impact measurement can create metrics that align with the stage of the impact investing journey that institutional investors are on – from awareness to understanding to interest to the actual investment transaction. To move investors along this journey, metrics should be simple, aligned to any impact-related interests of the investors, and focus on direct outputs of activities to show evidence of progress that will generate further investor interest in impact. Without these institutional investor-focused considerations, the metrics collected may fail to enable demonstration effects, as they would be seen as too complex or irrelevant for investor interests. To ensure that impact measurement is useful to the ultimate outcome of acceleration of institutional investment to achieve development impact, the measurement of direct outputs should set and reset expectations for project milestones, inform how donor support can evolve, and generate further investor interest in impact.[66]

2. **To ensure that the long-term outcome of donor support is measured, donors should coordinate with and capacitate stakeholders to collect long-term outcomes after USAID project close.[67]** Outcomes such as financial close of transactions may take years to materialize from donor-supported activities, such as building relationships between institutional investors and emerging markets asset managers. Capture of these outcomes is central to understanding the impact of donors, but difficult due to the shorter timeline of donor engagements. To ensure measurement of long-term outcomes, donors should capacitate stakeholders such as implementors and investors with the ability to collect long-term outcomes and coordinate who is responsible for their measurement. To capture metrics which motivate investment from institutional investors, donors should capture simple metrics such as ESG and "do-no-harm" metrics, showcasing those investors can make desired returns alongside impact.
3. **To ensure that high impact activities are selected for implementation, donors can us a framework that estimates relevant additionality and impact metrics for prospective projects.[68]** Donors can screen potential support activities for financial additionality, ecosystem additionality, and development impact through a framework which asks questions such as those in Table 2. This screening framework allows donors to strategically provide support which lead to investments and development impact that would not have occurred otherwise.

Table 2: Screening Framework for Donors to Estimate Additionality of Support Activities

Category	Indicative Question	Implication
FINANCIAL ADDITIONALITY	Do investors need donor support to address challenges that prevent them from investing their own money?	If investors face multiple financial and non-financial barriers that donors are well-positioned to help solve, the need for donor support is high.
ECOSYSTEM ADDITIONALITY	Will the investment opportunity help create demonstration effects for the market?	If the investment opportunity can provide proof of concept for an innovative finance structure and incentivize replication of this structure to strengthen the investment ecosystem, then there is potential for ecosystem additionality.

DEVELOPMENT IMPACT	What is the current equity and empowerment gap (for women and other vulnerable groups) that stakeholders could potentially address for end beneficiaries? What is the potential scale of the stakeholder's solution to address the equity and empowerment gap?	If there is currently low participation of vulnerable groups in economic empowerment programs and the stakeholder solution can help a large amount of those in vulnerable groups join economic empowerment programs, then there could be high potential for development impact.

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