WORKSHOP

WHAT'S NEW IN INNOVATIVE FINANCING?

Tuesday 20 March – 9:00/12:45

Ministerial Conference Centre, Ministry of European and Foreign Affairs
27, rue de la convention, Paris 75015

Ferdi and Iddri, together with the French Ministry of European and Foreign Affairs, organize a workshop on innovative financing. The aim is to review the existing mechanisms based on evidence from key players involved in implementing certain forms of financing, and discuss opportunities that have not yet been explored, in particular the estimated potential for innovation and "replicability" of mechanisms applied to some of the most underfunded areas

PURPOSE

The adoption of the 2030 Agenda and the Sustainable Development Goals (SDGs) have, among other things, raised the question of how the activities that contribute to these objectives will be financed. While the scale of the funding required is dizzying (the United Nations has indicated that several thousand billion dollars a year will be needed to achieve the SDGs (UNCTAD, 2014)), the key issue is working out how to direct the significant resources available worldwide towards financing these goals. Given that Official Development Assistance (ODA) is far from sufficient to finance the SDGs in full, an innovative approach needs to be taken, in order to implement mechanisms that can be used to direct the resources available towards sustainable development – hence the term "Innovative financing".

Hidden behind this phrase is a set of financial practices and mechanisms designed to raise funds to support development, in addition to the assistance traditionally mobilised, and optimise their impact. Innovative financing is also supposed to be characterised by its predictability, stability and sustainability.

Used in its various accepted meanings, the term "innovative" financing is not intended to be misleading. In practice, there is a wide range of so-called "innovative" financing mechanisms. Some of the oldest are designed to increase the resources available to support development policies or a related purpose. Others, which are more complex and more recent, associate additional funding with the notion of outcomes. The Dalberg report (2014) estimates the amount of innovative financing for development mobilised between 2001 and 2013 at US$100 billion, with an annual increase in volume of 11%[1]. Understanding innovative financing means making a distinction between several different categories.

The first category consists of mechanisms viewed as innovative because of their *capacity for mobilising additional resources* to support development policies. Most of the time, these are financial mechanisms that are adapted to address specific situations or applied to particular purposes. Within this category, there are two distinct groups.

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[1] Dalberg (2014) *"did not include bonds to fund infrastructure or public private partnerships (PPPs) that focus on infrastructure investment. In addition,* [it] *only considered mechanisms where resources were deployed in developing countries"*.

i) The first consists of new tax bases, particularly those linked to globalisation, such as taxes on plane tickets, financial transactions, carbon emissions trading or mining resources, which make it possible to redistribute a very small proportion of the income from these activities. While the principle of taxation is well established, its application to new areas is viewed as innovative and provides a means of releasing new resources. International taxation still offers significant potential for development financing.

ii) Another group consists of mechanisms that are innovative in terms of seeking a leverage effect, such as guarantees[2] and combining private-sector and government revenue[3].

A second category of innovative financing consists of mechanisms whose *primary objective is to achieve outcomes.* Again, there are two distinct groups within this category.

i) Impact investing which aims to generate social and environmental impacts at the same time as delivering a financial return. This capital-investment targets "*companies with significant social impact and/or enterprises that are too small to meet the criteria of eligibility of traditional investors*"[4].

ii) Mechanisms based on contracts between a public-sector stakeholder and a public or private-sector provider, linking the payment of the service provided to specific outcomes to be achieved. In this case, the private-sector provider covers the investment and is paid by the public-sector stakeholder later, with interest, according to the outcomes achieved[5].

Development impact bonds and social impact bonds are a specific and relatively new type of these mechanisms. They aim to finance service public costs by a private provider. In fine, the public ordering institution reimburses and remunerates investors according to the outcome obtained. The return on investment is thus depending on the achievement of pre-defined objectives that are measured by an independent institution. These "bonds" are also contracts (they are not bond securities). One of the strengths of this kind of mechanisms is that investors have an interest at least equal to that of the public ordering institution in ensuring the achievement of the objectives.

iii) We can also include here thematic bonds, as green bonds for instance, that are aiming to orient investors towards projects concerned with a specific cause (environmental quality in the case of green bonds) for which traditional financing instruments are not relevant. They are issued by public development banks, local authorities, large companies or States.

[2] See in particular, Benn et al. (2015). A case study on the guarantees applied to city financing has been carried out by Iddri (Criqui and Vaillé, 2017)

[3] See in particular Benn et al. (2017), OECD (2018)

[4] https://blog.secteur-prive-developpement.fr/2016/06/06/promouvoir-durablement-les-petites-entreprises-africaines-le-defi-des-investisseurs-de-mission/

[5] To a certain extent, public-private partnerships can be viewed as a simple form of innovative financing

A third category is composed by mechanisms whose innovation is in the financing modalities:

i) Original ways to manage debt as loans that are indexed against GDP and other countercyclical instruments[6], and debt-swap.

ii) Mechanisms based on bonds issuance for which several donors pledge to reimburse, in the long run, in order to ensure the immediate financing of the provision of a public service that a developing countries is unable to finance alone. The International Finance Facility for Immunisation (Iffim) is an example.

iii) Mechanisms that aim to create a market, such as Gavi's Advance Market Commitment (AMC), through which donors commit to finance the purchase of vaccines over the long term, to encourage laboratories to develop vaccines and sell them at affordable prices.

iv) There are numerous specific mechanisms in the climate area. Examples include index-linked insurance, flexible savings schemes and loans designed to address the risks associated with natural disasters, and "carbon offset"-type mechanisms based on market principles, such as payment for environmental services, e.g. REDD+ for forests (Angelsen, 2015).

These mechanisms seek to reconcile market imperatives and public benefit. They are particularly well aligned with the spirit of the Addis Ababa Action Agenda on development finance (United Nations, 2015) and the SDGs.

Another aspect of the topic is technological innovation to support development finance. The digitisation of the economy and current practices, particularly in banking, offer new opportunities to raise funds, for example, the ability to make a donation via text message and wider access to traditional financing mechanisms in the economy.[7] This is one of the aspects this workshop is aiming to cover.

The workshop will consist of three sessions, each of which will address one of the three categories of innovative financing.

Each session will deal with two or three mechanisms, each one introduced by a 5/6 minutes speech. Then, each specialist will have 4 minutes to share his ideas and views on topic under discussion. A debate with the floor will follow.

<u>Discussion will be held under Chatham House Rules</u>. Number of expected participants, around 50, implies that each speaker will have to be concise (3 or 4 minutes) in order to allow everybody to speak.

[6] See Panizza (2015), among others

[7] Digitisation has various other consequences on how economies are financed (the "blockchain" revolution, for example) but it is not possible to cover everything in one event.

AGENDA

08:45 Welcome

09:00 Introductory remarks – Cyrille Pierre (French Ministry of Foreign Affairs) and Patrick Guillaumont (Ferdi)

09:08 Keynote – Mariam Jashi, President of Leading Group on Innovative Financing for Development

09.15 1st session: **Innovative financing to generate additional resources**.

09.15 New tax bases

09.45 Blending mechanisms and guarantees for development

10:20 Coffee break

10:30 2nd session: **Innovative financing to generate results**

10.35 Impact Investment, Output-based payments and Thematic bonds,

11.30 Debate with the floor

11:45 3rd session: **Innovation through financing modalities**

11.50 Innovative management of debt, Climate finance and other mechanisms and aspects of innovative financing

12.25 Debate with the floor

12:40 Conclusion

12.45 Lunch

EXPECTED OUTCOMES

- Sharing the experience of key players involved in implementing innovative development finance mechanisms. It is expected that each speaker will provide input that will contribute to an assessment of what has worked well or less well.
- Discussion on the opportunities these lessons offer in terms of:
  - "replicability" to other sectors;
  - the effectiveness of development cooperation;
  - capacity for covering financial needs

RÉFÉRENCES

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