

Executive summary

The challenge

While turning the “billions into trillions” is essential to bridge the Sustainable Development Goals (SDGs) financing gaps, there is a need also to focus on the quality of resources mobilised and how they reach those being left behind. While international and domestic public finance remains essential to meet the SDGs, public resources alone will not be enough. The challenge is particularly acute in the least developed countries (LDCs), which have experienced a recent decline in official development assistance (ODA). LDCs also often find it difficult to attract private investment, including foreign direct investment. Increased public and private financial flows must therefore be made to work for the world’s most vulnerable countries, for underserved markets, and for smaller projects in the so-called “missing middle” – those small and medium-sized enterprises that are too big to access microfinance but too small or seen as being too risky to access commercial loans offered by mainstream financial institutions.

In these settings, blended finance offers potential opportunities to increase the resources available to LDCs and the missing middle. But such approaches are not without limitations or risks, and need to be deployed carefully. To improve how blended finance strategies can best work for LDCs, it is essential to understand not only the quantities of finance they mobilise and the regions and sectors they are benefitting, but also how these strategies are being applied, and, more broadly, how the financing for development architecture is evolving and supporting LDCs to meet the SDGs and ensure no one is left behind.

This report, the second in a collaboration between the United Nations Capital Development Fund (UNCDF) and the Organisation for Economic Co-operation and Development (OECD), outlines the latest trends in blended finance approaches in LDCs. It updates the previous 2018 report with the latest available data from the OECD, which now cover the six years from 2012 through 2017. It also features seven guest pieces by practitioners and experts working in the blended finance space, which showcase the opportunities and challenges of applying blended finance solutions in LDCs. The report concludes with a review of the next steps for the blended finance and development communities, and flags some emerging issues revealed in the report.

Recent trends

LDCs receive a small piece of the blended finance pie. Of all the private finance mobilised by official development finance interventions between 2012 and 2017, approximately USD 9.3 billion, or 6%, went to LDCs, whereas over 70% went to middle-income countries. Gaps in the data mean it is unclear whether this represents a fall relative to the 7% of private finance mobilised for LDCs observed for 2012-2015.

On average, blended finance deals in LDCs mobilise less private finance than those in other developing countries. Over 2012-2017, the average amount of private finance mobilised in LDCs was USD 6.1 million per deal, compared to USD 27 million in lower middle-income countries and over USD 60 million in upper middle-income countries.

Some LDCs benefit more than others. The top five recipients - Angola, Senegal, Myanmar, Bangladesh, and Zambia - together received approximately 44% of the total volume of private finance mobilised and almost 22.5% of all deals in the LDCs in 2012-2017.

Some LDCs receive no blended finance, but do receive official development assistance (ODA). There is a weak but positive relationship between ODA received and private finance mobilised.

Credit and risk guarantees continue to mobilise the most private finance in absolute terms, at 63% of the total volume reported in 2012-2017. The average volume of private finance mobilised in LDCs is consistently lower for all leveraging mechanisms. Simple co-financing agreements are instead the most frequent leveraging mechanism, as they represent 56% by number of deals overall.

Energy, banking and financial services are the largest, and growing, sectors, representing 23% (USD 2.16 billion) and 19% (USD 1.8 billion) respectively over the six years analysed. Data for 2016-2017 indicate this share is growing. Education and healthcare are scarcely addressed.

Multilateral donors mobilised the largest amounts of private finance in LDCs: USD 5.2 billion or 56% of all private finance over 2012-2017. Yet, bilateral donors are increasingly important blended finance players in LDCs.

Most mobilised private capital reaching LDCs comes from high-income countries. While LDCs themselves remain a significant source of additional capital, their importance has diminished from 42% of finance mobilised in 2012 to 14% in 2017. However, the average volume of private finance mobilised from domestic investors in LDCs increased from USD 4.5 million in 2012 to USD 5.8 million in 2017.

The number and variety of players entering the blended finance space is increasing. While some donors are taking steps to increase their engagement in LDCs, the data suggest that many providers still tend to overlook these markets when it comes to blending. This in turn implies there is a need for further risk-taking and experimentation at both the balance sheet and project level to get more private finance invested in LDCs when appropriate. Blended transactions typically also require greater levels of concessional support in LDCs than in other developing countries.

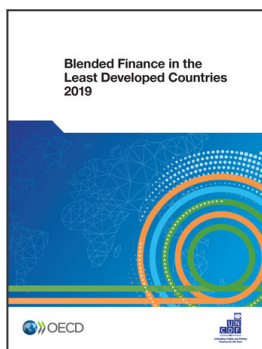
Making blended finance work for least developed countries

Blended approaches can help mobilise much-needed additional resources for the LDCs and they can create demonstration effects that narrow the gap between actual and perceived risks of investing in these markets. But such approaches need to be considered and deployed carefully. In signing the Addis Ababa Action Agenda, Member States have agreed on a set of overarching principles for blended finance and public-private partnerships (PPPs). The OECD principles on blended finance provide a policy framework to ensure the sustainability of blended finance, while initiatives such as the multi-stakeholder Tri Hita Karana Roadmap and the UNCDF action agenda on LDCs are also focused on improving the effectiveness and efficiency of blended operations. Specific lessons from this report include:

- Blended finance solutions should respect national ownership, be aligned with national priorities and applied as part of a broader national SDG financing strategy that takes into account domestic and international, public and private sources of finance.
- In crisis-affected contexts, where ODA plays an essential role, blended approaches must be particularly transparent and accountable, and avoid doing harm by widening disparities.
- Technical assistance plays an important role in blended finance transactions in LDCs, including by helping to put in place the right capacities and institutions to identify, analyse and structure blended operations; and to strengthen investees' operational efficiency and environmental, social and governance (ESG) compliance.

- A local presence, be it an investor or a fund manager, can help build local capacity and understand risks and opportunities attached to each investment.
- There is a need for further research and efforts to strengthen SDG impact monitoring and measurement.

If blended finance continues to become an increasingly important modality of development co-operation, then development partners will need to ensure that this does not come at the expense of support for LDCs and other vulnerable countries – those where blending has been more challenging. It may be that there is a need to accept that the mobilisation agenda in LDCs will be different – but that those blended finance deals, where they are appropriate, are pursued because of their sustainable development additionality. Ultimately, different financing models - public, private or blended - will be best suited for different SDG investments in different contexts and governments should be in the driver's seat in determining which approach works best where.



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