Sweden has through Sida issued a guarantee of US$ 57 million to the International Finance Corporation, IFC. The guarantee enables one billion US$ of private capital investments in sustainable infrastructure in developing countries.

PRIVATE CAPITAL IS NECESSARY

In 2015 the International Community decided to collaborate to implement 17 Sustainable Development Goals, SDGs, by 2030. Earlier that year, the UN member states countries gathered at a conference in Addis Ababa to discuss new funding solutions and the need to mobilize the private actors’ competence, knowledge and capital for the implementation of the SDGs. Infrastructure and access to sustainable energy alternatives were mentioned as particularly important areas for mobilization of private investments.

OECD estimates show that US$ 4.5 trillion in annual investment would be required to implement the SDG goals in developing countries by 2030. Institutional investors such as pension funds, insurance companies, state-owned funds as well as resource-rich organizations and individuals dispose of large volumes of capital, an estimated total of US$ 100 trillion. Institutional investors have long-term financial commitments that fit well with infrastructure investments, that usually have a long economic life. The interconnection between the institutions’ capital and the need for loan financing for sustainable infrastructure development in developing countries has so far not taken place on a large scale. One major reason is that institutional capital is often regulated based on risk levels and the type of investments that can be made.

SIDA GUARANTEES FUTURE IFC LENDING

IFC is part of the World Bank Group and promotes sustainable economic growth through investment and advisory services in the private sector in developing countries. Through equity investments, loans and guarantees on market terms, funding is offered to companies in regions with limited access to international capital markets. In addition to project funding in its own books, IFC also mobilizes capital from other lenders and investors to its projects. IFC is funded through member countries’ equity capital investments in the same way as other multilateral financial institutions are capitalized. One of the key focus of IFC is lending to infrastructure projects, especially energy, but also water, telecom and transport projects. More than 60% of IFC’s energy investments are currently within renewable energy.

Sida and IFC have jointly developed a model where institutional capital is invested alongside IFC in sustainable infrastructure projects. The financing model and the approach have gained considerable international attention as the model shows how large volumes of long-term institutional capital may be mobilised by a multilateral bank, thus being able to finance more projects than before.

The insurance companies Allianz and Eastspring (subsidiary of Prudential) have each set up a US$ 500 million fund, i.e. a total of US$ 1 billion, which will be used for lending to new IFC projects. IFC decides which projects will be financed. In the project evaluation, IFC will follow its regular policies and processes.

IFC covers risks in the two funds through a first loss tranche of 10%. Sida counter-guarantees IFC in all projects related to renewable energy and investments in the poorest countries (except for investments in fossil fuel and mining projects). Sida’s counter-guarantee is expected to cover 20-25 individual projects. Sida’s maximum guarantee coverage is US$ 57 million.

The loans are usually issued to project companies who are responsible for and implement the infrastructure projects. In many cases, IFC is mandated to arrange additional financing from other international and local lenders resulting in further private capital being mobilised into each project, including mobilising local private capital.
Loans covered by Sida’s guarantee will be committed over the next five years and are expected to have an average maturity of 11 years, with isolated loans having a maturity of up to 20 years. Sida’s guarantee to IFC has a tenor of 25 years.

Sida’s guarantee enables IFC to make more sustainable investments in low-income countries and to further invest in renewable energy; two development objectives emphasized in Sweden’s long-term dialogue with the IFC and the World Bank Group.

The projects are followed up by IFC according to current guidelines and procedures, and Sida has allocated funds for a mid-term review and evaluation of the program. Particular attention will be paid to the evaluation of social and environmental issues, as well as poverty reduction and gender issues.

CROWDING IN PRIVATE CAPITAL

Current international regulations (e.g. Basel III and Solvency II) require banks and institutional investors to make large capital provisions for investments in high-risk countries. The fact that Sida and IFC together cover a first loss in the funds, reduces the overall credit risk to a level that makes it attractive for institutional investors to invest.

The fund structure was initially discussed with several institutional investors. Allianz and Eastspring, that eventually chose to move forward, have actively participated in elaborating the final financial structure. Further institutional investors have since begun negotiations with IFC to potentially invest in a similar fund structure. Sida’s objective of creating a demonstration effect of how institutional capital may be mobilized has therefore been met.

WHAT IS A SIDA GUARANTEE?

Sida’s guarantee instrument is a way of mobilizing private capital for development purposes, and plays an important role in Swedish development cooperation. Through providing guarantees, Sida promotes the utilization of private capital in development cooperation through reducing the risk of private actors investing in development projects. Sida guarantees result in increased investments in development projects, thus resulting in development reaching more people and more places.

Through guarantees Sida enables financing of projects in e.g. health, SMBs, sustainable infrastructure, environment and climate. Read more about Sida’s guarantees: https://www.sida.se/English/partners/our-partners/Private-sector/Innovative-Finance/