WEBINAR:
DECODING THE FUNDAMENTALS OF DEVELOPMENT FINANCE

International Financial Institutions: Who and what they are, how they operate

Natalia Toschi
Head of Funding, Treasury Services Division, IFAD

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Features of MDBs, DFIs and Vertical Funds

1. What is an IFI?
2. What is a vertical fund?
3. Membership structure
4. Clients
5. Size
6. Financial model
7. MDBs’ reform and G20 recommendations
An International Financial Institution (IFI) is a financial institution that has been established by more than one country, and hence is subject to international law (as opposed to national law of one Government).

The two important types of IFIs are:

- Multilateral Development Banks (MDBs)
- Development Finance Institutions (DFIs)
What is a Multilateral Development Bank (MDB)?

**Multilateral**: they are established by several sovereign states that are the shareholders of the bank

**Development**: with the mission to fostering economic and social progress in developing countries by financing projects, supporting investment and generating capital for the benefit of all global citizens

**Banks**: they borrow money to lend money and make margin to cover admin costs
The big 7 MDBs

International Bank for Reconstruction and Development (World bank group) (IBRD), 1944

International Finance Corporation (World bank group) (IFC), 1946

European Investment Bank (EIB), 1958

Inter-American Development Bank Group (IDB), 1959

African Development Bank (AfDB), 1964

Asian Development Bank (ADB), 1966

European Bank for Reconstruction and Development (EBRD), 1991

But there are many others:

Central American Bank for Economic Integration (CABEI), 1960
CAF - Development Bank of Latin America (CAF), 1970
Islamic Development Bank (IsDB), 1973
China Development Bank (CDB), 1994
New Development Bank (NDB), 2014
Asian Infrastructure Investment Bank (AIIB), 2016
What are International Development Finance Institutions (IDFIs)?

**International:** they are established by several sovereign states that are the shareholders of the bank

**Development:** with the mission to fostering economic and social progress in developing countries by financing projects, supporting investment and generating capital for the benefit of all global citizens

**Finance Institutions:** that provide financial support primarily in highly concessional loan and grant form
Some important international DFIs are:

- **International Development Association** (World bank Group) (IDA), 1960
- **African Development Fund** (AfDF), 1972
- **Asian Development Fund** (AsDF), 1966
- **International Fund for Agricultural Development** (IFAD), 1977
- **OPEC Fund for International Development**, 1976
What about National Development Finance Institutions (NDFIs)?

**National DFIs**: majority-owned by national governments or benefit from government guarantees. This ensures their creditworthiness, which enables them to raise large amounts of money on international capital markets and provide financing on very competitive terms.
Some important national DFIs are:

Kreditanstalt für Wiederaufbau, Germany (KFW), 1948

Agence Française de Développement, France (AFD), 1998

FinDEV, Canada, 2018

Swedfund, Sweden, 1979

But there are many others:

- OeEB (Austria)
- BIO (Belgium)
- BMI-SBI (Belgium)
- IFU (Denmark)
- Finnfund (Finland)
- CDP/SIMEST (Italy)
- FMO (Netherlands)
- Norfund (Norway)
- SOFID (Portugal)
- COFIDES (Spain)
- SIFEM (Switzerland)
- CDC Group (United Kingdom)
- OPIC (United States)
KEY MESSAGE 1:
The essence of MDBs and DFIs

- MDBs and DFIs provide financing for a broad range of development topics.

- MDBs and DFIs do not have a profit-making mission.

- MDBs and some national DFIs are “banks” which provide primarily loans and have to make enough income to finance their ongoing operations.

- International DFIs are institutions that require periodic injection of capital from Members as they are “loss making” by design because they provide primarily highly concessional loans and grants.
2. What is a vertical fund?

“Vertical funds” are development financing mechanisms confined to single development domains with mixed funding sources.

Some vertical funds are:

- **The Global Environmental Facility (GEF), 1991**
- **The Adaptation Fund (AF), 2001**
- **The Green Climate Fund (GCF), 2010**
- **The Global Fund to fight AIDS, tuberculosis (TB) and malaria, 2002**
- **The Global Alliance for Vaccination and Immunization (GAVI), 2000**

The entities are funded by the public and private sectors. The operating model is typically relying on accredited entities and delivery partners who work directly with developing countries for project design and implementation.
KEY MESSAGE 2: Vertical Funds

- Vertical funds are focused on one specific development topic and operate through accreditation-models and implementing agencies.
3. Members of MDBs and DFIs are shareholders and have voting rights

<table>
<thead>
<tr>
<th>MDB</th>
<th>Largest shareholder</th>
<th>2nd largest shareholder</th>
<th>3rd largest shareholder</th>
<th>4th largest shareholder</th>
<th>5th largest shareholder</th>
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<td>Japan</td>
<td>South Africa</td>
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<td>Japan, US</td>
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<td>India</td>
<td>Australia</td>
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<td>EBRD</td>
<td>US</td>
<td>France, Germany, Italy, Japan, UK</td>
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<td>EIB</td>
<td>Germany, France, Italy, UK</td>
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<td>IADB</td>
<td>US</td>
<td>Argentina, Brazil</td>
<td>Mexico</td>
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<td>IDA</td>
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<td>France, UK</td>
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<td>IFAD</td>
<td>US</td>
<td>Italy</td>
<td>Germany, Japan</td>
<td>Netherlands</td>
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Source: A guide to multilateral development banks, ODI, 2018
KEY MESSAGE 3: Vertical Funds

- Members of MDBs and DFIs are **sovereign states**. No private entity or individual can be a member or shareholder of an MDB/DFI.
4. Who are the clients?

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<tr>
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<th>Sovereign States</th>
<th>Private Sector</th>
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KEY MESSAGE 4: Global clients

- MDBs and DFIs provide assistance to the public and private sectors
5. How large are these institutions?

MDBs', DFIs' and Vertical Funds' total assets compared to commercial banks (USD million)

MDBs are large institutions that however do not compare with large multinational commercial groups

Source: MDBs' and commercial banks' financial statements December 2023 (and June 2023 for WB group)
*2022
How large are these institutions?

MDBs', DFIs' and Vertical Funds' annual disbursements (US$million)

Source: MDBs' and DFIs' financial statements December 2023 (and June 2023 for WB group)
6. How is an MDB’s/DFI’s/financial model?

Equity/Capital from Members (Replenishments) → Grants and Concessional loans

Equity/Capital from Members (Replenishments) → Investments

Equity/Capital from Members (Replenishments) → Less-Concessional loans

Borrowings

Reflows and Operating results
Where do MDBs borrow from?

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<tr>
<th>Country/Region</th>
<th>IFAD</th>
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<th>IBRD</th>
<th>AfDB</th>
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Source: IDA and AfDF websites and bloomberg
New funding mechanisms

**Hybrid capital:** an innovative form of capital which increases sustainable lending capacity

**Equity content of 100% by Fitch, Moody's and S&P,** and 100% equity under the IFRS accounting rules

**Perpetual with fixed rate coupon of 5.75%** payable annually with a reset mechanism

**AfDB has the option to redeem all of the notes** on the first reset date and every reset date thereafter
KEY MESSAGE 5: Size and financial model

- MDBs/DFIs/Vertical Funds can be sizable institutions but smaller than large commercial banks
- MDBs and National DFIs use their ratings to source cheap financing from capital markets to on-lend
- International DFIs need capital injection to provide HC loans and grants
7. MDBs’ reform and G20 recommendations (2022)

Boosting MDBs’ investing capacity.
G20 Recommendations

**Recommendation 1:** Redefine the Approach to Risk Appetite in Capital Adequacy Frameworks

**Recommendation 2:** Incorporate Uplift from Callable Capital into MDB Capital Adequacy Frameworks

**Recommendation 3:** Implement Innovations to Strengthen MDB Capital Adequacy and Lending Headroom

**Recommendation 4:** Assess CRA Methodologies and engagement

**Recommendation 5:** Improve the Enabling Environment for Capital Adequacy Governance
KEY MESSAGE 6:
G20 report on MDBs

- Increase lending by becoming less depended on credit rating agencies, more risk takers
Thank you

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