SPECIAL STUDY

EBRD Mobilisation of Private Finance Management Comments

European Bank
for Reconstruction and Development

EvD ID: SS19-140

April 2020

EBRD EVALUATION DEPARTMENT

Executive Summary

- Management welcomes the draft Special Study on Mobilisation as important and timely. Amid global increased focus on the importance of mobilising private sector capital to deliver on the 2030 Sustainable Development Agenda (and SDGs), and the ongoing discussions about the Bank's medium term strategy, this study is useful to inform ambition and approaches for the future.

- Management believes that MDBs, and the Bank in particular, have an important role in increasing private sector mobilisation. Financing from MDBs will never be sufficient and thus mobilising private finance is core to how we add value and deliver on our mandates. Indeed, Article 2.1 (ii) of the Agreement Establishing the Bank requires the Bank to "…to mobilise domestic and foreign capital." in addition to its own investment. This is in line with the ongoing strategic discussions and increased efforts for mobilising more including through co-financing from Impact Investors. Management also recognises the key importance and role of direct mobilisation in relation to fulfilling our mandate as well as operational, risk and financial management: 1) it is core to our mandate and the transition impact related to supporting the availability of a wide and diversified base of investors as a key characteristic to the functioning of a sustainable market economy; 2) it enables the financing of larger projects; 3) it is a useful instrument to manage risk concentrations; and 4) it frees up capital to support the expansion of the Bank's activities, improving value for money for shareholders.

- Management thus considers mobilisation to be a key strategic objective for the Bank in delivering its transition mandate. It is for this reason, as pointed out in the report, that Management has engaged with the Board on the topic on numerous occasions, including FOPC presentations on increasing mobilisation (June 2018), enhancing mobilisation (December 2018), a BIS on impact investment and mobilisation (December 2019) as well as the annual FOPC review of Loan Syndications activities and priorities, with recommendations being highly supported by the Board. As part of the ongoing strategic discussions in the context of the Strategic and Capital Framework (SCF), Management is proposing to continue its efforts to broaden mobilisation in terms of products, countries of operations, and investors. Delivering in this area will require investment in staff and new skills, establishing a more visible market presence, and creating new financing structures. EBRD will also need to strengthen its measurement and reporting of results. The ultimate goal would be to optimise total Bank investments, both ABI and the mobilised investments. Both are needed for the EBRD to deliver transition impact. Own-account financing is critical for influence on policy dialogue, to align incentives, take early risk and bring comfort to private financiers as well as to embed high standards in projects and advocate for policy goals. Mobilised financing is critical to meet the sheer scale of the challenges facing countries of operation and to ensure long-term sustainability.

- Management is broadly supportive of the study's message that mobilisation should become more prominent among the various strategic objectives of the Bank while carefully balancing potential trade-offs (including between its various components of direct and indirect mobilisation and through to catalysation). We agree that the Bank should maintain continuous focus on mobilisation. Indeed, the Bank has been on a positive path with respect to Management prioritisation and signalling of the importance of mobilisation. Essentially, it is important to promote a cultural mind-set of always considering the appropriateness and feasibility of sharing risks of each transaction with other investors. In short, there is no inherent contradiction between the goals of mobilising and ABI. There is simply a balance to be struck. Indeed, the study does not recognise that there may not be a market at par for many of its operating assets. In addition, the study does not acknowledge that a higher turnover of projects may not be possible under an originate-to-distribute model based on the

Bank's origination experience, its knowledge of its markets and efforts are already being made to increase the deployment of capital.

- The Bank's business model has been reaffirmed throughout the preparatory work for the SCF. In this respect, Management notes and welcomes the broader concept of mobilisation including Private Direct Mobilisation (PDM), Private Indirect mobilisation (PIM) and Catalysation, as appropriate for the Bank and MDBs as agreed in the MDB working group on mobilisation. The different definitions being used between EBRD, the MDBs, and EvD leads to some confusion and it is not clear that all parties are talking about the same thing. It would be helpful for the EvD report to clarify upfront and well before section 2.2 that it is using the OECD broad definition of blended finance. We note that the OECD definition is not broadly used by MDBs.

- Moving forward, Management will review these concepts and definitions with a view of increasing the clarity between EBRD's own AMI definition and various components of mobilisation as defined by the MDBs. Clarity is critical to ensure that the right things are being incentivised and reporting is transparent. EBRD will seek to align with others when and how appropriate. The study uses PIM reported by MDBs to compare EBRD against its peers. Such comparisons can be quite misleading, primarily because of the lack of objective and consistent application by MDBs of the agreed metrics. Inadequate MIS systems at EBRD but also other MDBs further compound the challenge.

- As noted in the study, the Bank's catalytic effect and indirect mobilisation, though very difficult to measure properly, are very important and have a larger effect on increasing private sector investments in countries of operations than the direct mobilisation. In the course of usual business the EBRD catalyses private investments through its transition impact, from demonstration effects of championing success supported through its investments, as well as from its policy reform (e.g. improvement in business environment) and capacity building, which in turn trigger more investments from the private sector. In addition, the Bank's work in supporting conditions for developing capital markets through investments and policy engagements, though not associated with immediate mobilisation, is key to alleviating challenges and increasing future mobilisation (in particular through syndication). Beyond the catalytic effect, sustaining the Bank's operating assets is necessary for institutional capacity and financial sustainability, and direct mobilisation, currently and in the future (e.g. project size influences the ability to mobilise commercial bank lending).

- Management notes that an overzealous shift to an originate-to-distribute model would undermine the very role MDBs play in markets and presupposes that MDBs' value added is simply in its financing. In reality, the value added of MDBs compared to other financiers is much broader. The "quality" of MDB financing is higher because with it comes high environmental, social, governance, procurement, and integrity standards, structuring experience, technical cooperation and policy dialogue. Having "skin in the game" allows MDBs to have impact beyond individual transactions – systemic impact. As financial institutions that must be financially sustainable, MDBs must also balance risk and return, capital usage and gross income. Also, a full shift to a originate-to-distribute model, especially if focusing narrowly on direct mobilisation, would not necessarily/always lead to higher total private investments in countries of operations (i.e. projects do not become larger if the Bank mobilises more investors). The key is to provide the right balance for both AMI and ABI, and to continue improving measurement of the results of all aspects of EBRD's work, including the policy work.

- A core goal of the EBRD is to introduce private sector investors to the Bank's countries and projects (related to the Bank's additionality) and therefore have a demonstration effect, considered in our transition impact. In this respect, Management believes the study at times establishes a 'false

dichotomy' between originate-and-hold and originate-to-distribute business models. Holding unnecessarily for too long is not ideal, nor is distributing prematurely or assuming that the only value of EBRD is in the pure origination. That is particularly true given the goal of achieving systemic impact beyond a project-by-project approach. The Bank needs to hold assets on its balance sheet to serve its transition purpose and financial sustainability objectives. It should also seek to dispose of assets when there is a market and where it makes sense from a transition and sound banking perspective and hence distribute amounts to private sector investors that for mobilisation (part of creating markets) and other reasons it chooses not to hold. This creates a win-win, non-zero sum approach to mobilisation.

- Management agrees that increased focus on mobilisation requires clear and coherent objectives and carefully balanced incentives. Opportunities for any clarification of definitions, objectives and strengthening of incentives will be explored as part of the Corporate Scorecard review. Currently, ABI and AMI have equal weight in the Corporate and Banking scorecard. The Corporate Scorecard includes other related objectives such as income generation, portfolio, operating assets and disbursement targets that support investments. Management notes that the Corporate Scorecard also includes measures of transition impact which directly reward mobilisation (such as supporting development of investor base and capital market development), and reflects the catalytic effect of the EBRD investments, advisory services and policy engagements (mobilisation in the broader sense). As part of the Corporate Scorecard review, considerations will be given to better align incentives aimed at optimising total EBRD investments that capture both ABI and mobilisation.

- Management notes that catalysation as a form of mobilisation is difficult to quantify and measure accurately (this is a common issue across MDBs), as the investments often happen outside of the Bank's financing and may occur well after market enhancements have been introduced through the Bank's engagements, including those with donor support. There have been attempts by MDBs collectively in the context of a working group and individually by a number of institutions to define and measure catalysation. None of these attempts has yielded a viable and objective methodology to measure catalysation to date. Hence, the methodology developed by MDBs to report on mobilisation solely and intentionally concentrated on the measurement of private finance mobilised directly.

- In addition, Management believes that targeting an advantage ratio per unit of either ABI or donor funds to optimise mobilisation as suggested by the study is not appropriate as the relationship is not linear (similar to the overall transition impact), and may lead to perverse incentives (for instance in favour of larger projects).

- Management fully agrees that the alignment of objectives and incentives is the key to creating optimal cooperation between the various departments of the Bank (e.g. Banking and Syndications/Finance). However, such alignment can be achieved in a number of ways and does not necessarily require organisational changes. Signalling and leadership from the top is critical as well. A distribution function's success depends on the deep understanding of the markets and close contact with a variety of investors. Finance (through Treasury and Syndications) is in daily contact with investors of all types (Banks, Asset Managers, Pension Funds, SWFs, Central Banks, IFIs, Insurance Companies, Impact Investors, etc.). At a time when mobilisation requires creativity, new instruments and a variety of investor types, such expertise is the key to success.

- Management does not agree with the issues raised by the study and Recommendation 4 related to Bank's accounting and capital adequacy policies, its ability (or inability) to measure financial efficiency of mobilised projects, or the lack of importance attached to the use of RAROC. The Bank's

accounting policies adhere to the International Financial Reporting Standards (IFRS), while its capital allocation framework is anchored in the Basel III Accord and rating agency methodologies. They are subject to periodic reviews (the current Capital Adequacy Policy was approved by the Board in 2019) and external professional scrutiny (e.g. through annual audit by external auditors and rating agency assessments). Those reviews ensure that the policies remain relevant and address emerging needs and industry accepted practices. Indeed the most recent review (2019) of the Capital Adequacy Policy aimed among other purposes at making it more sensitive to continuous variations of LGD, and hence making it suitable to a broader range of products. Furthermore, the EBRD is at the forefront of IFIs in terms of its suite of return on risk measurements and tools. We note, and agree, that return on capital is an important dimension that also needs to be balanced with size (ABI) and transition impact.

- There is a disciplined focus on RAROC embedded in the project decision making and an overall assessment of the return on risk-adjusted capital during the annual SIP process that assesses the effectiveness of the capital deployment and the overall financial sustainability of the Bank (see detailed comments below re. Recommendation 4). RAROC is an important element (amongst many others) to inform the process of pricing and accepting/rejecting debt projects. It is not suitable for the equity business where other metrics should be used to assess return on capital. Hence, the RAROC levels of the debt business should not be compared mechanistically with the levels of RORC achieved at the bank wide level (that includes equity and treasury income). Technical details aside, Management sees return on capital as a key element to ensure the financial sustainability of the EBRD (and that has been a constant tenet of its strategy).

- Management welcomes the study analysis and the insights provided from existing research and other MDBs' experience and practices. EBRD has and continues to work closely with MDB colleagues in developing its own practices. However, Management would have wanted the study analysis and findings to better reflect the practices and lessons from, the EBRD specifically. These relate in particular to the study's suggested areas, instruments and initiatives generally for all MDBs and particularly for the EBRD to achieve higher mobilisation potential.

- Management agrees on the importance of the catalytic effect of donor funds that could offer a platform for more mobilisation and overall higher leverage – whether from EBRD capital or private investors. This in particular, when donor funds are used upstream for market creation and market-supporting activities, especially in the policy and advisory sphere. Though not explicitly targeting more mobilisation, the use of donor funds is guided by the Bank's internal principles that take into account transition impact (through which the Bank catalyses private investments). In particular, technical cooperation and investment grants address, at an early stage, market barriers hindering commercial investments for certain innovative technologies and markets. The study argues that if donor funds were used more explicitly for de-risking, for preparation of pipelines and for the establishment of guarantee/risk-sharing platforms, this could generate additional transactions and be catalytic to a larger degree. Management notes however that this is not always the case and it depends on the type of investment, sector and country. To further transition and address developmental challenges, there are multiple cases of donor-funded projects where affordability constraints dictate the terms with little or no additional mobilisation, especially related to municipal projects. This is in line with our principles for using donor funds. Classifying donor co-investment funds, when offered on concessional terms, as mobilisation, as suggested in the study would create a perverse incentive to maximise use of concessional resources to meet mobilisation.

Management's response to EvD's recommendations is provided below, followed by comments on the study analysis and findings.

Study Recommendations:

Recommendation 1: *Prepare a detailed Mobilisation Approach or Initiative for discussion with the Board, assessing where mobilisation can be used to support the attainment of TI and return on capital objectives. It should cover markets and associated instruments, including advisory services and guarantees, review existing MDB/DFI practices, and set out clear objectives and institutional responsibilities.*

Management partly agrees with this recommendation. Management recognises the importance and role of mobilisation and believes that it is a key strategic objective for the Bank in delivering its transition mandate. Mobilisation has been the subject of a number of presentations to the Board by Management, including FOPC presentations on increasing mobilisation (June 2018), enhancing mobilisation (December 2018), a BIS on impact investment and mobilisation (December 2019) as well as the annual FOPC review of Loan Syndications activities and priorities, with recommendations being highly supported by the Board.

As part of the ongoing strategic discussions in the context of the SCF, Management is reviewing the Bank's approach and aspirations for mobilisation, including an analysis of the main instruments and capacity with respect to the opportunities, challenges, incentives, and potential trade-offs. Management is also actively working for opportunities to tap into the impact investing community. Management agrees with the study message that mobilisation should become even more prominent among the various strategic objectives of the Bank. In the course of re-examining these options, management would want to engage with the Board through a board information session to share views and solicit feedback and guidance. The results of this re-examination would be reflected in the annual Corporate Scorecards and SIPs (see Recommendation 3).

There is no doubt - from the language in the AEB to ExCom's convictions as expressed to the head of EvD - that mobilisation is important. However, Management believes it would be going too far to suggest that mobilisation is the principal objective of the Bank, nor that a fundamental shift to an originate-to-distribute business model is needed or desirable. Indeed, such a model would have limited the Bank's response capacity to the covid-19 pandemic.

Management agrees that it can continue to create a culture – and the incentives and systems that follow – that make it clearer that the ultimate goal of the Bank is to optimise total Bank Investment, both ABI and mobilised investment. This clarity would have be to translated into the Corporate Scorecard. Management also agrees that the alignment of objectives and incentives is the key to creating optimal cooperation between the various departments of the Bank, but such alignment is not necessarily achieved by organisational changes for the reasons mentioned above. A distribution function's success depends on the deep understanding of the markets and close contact with a variety of investors. Finance (through Treasury and Syndications) is in daily contact with investors of all types (Banks, Asset Managers, Pension Funds, SWFs, Central Banks, IFIs, Insurance Companies, Impact Investors, etc.). At a time when mobilisation requires creativity, new instruments and a variety of investor types, such expertise is the key to success.

Similarly, Management agrees that bringing teams working on mobilising donor-funding streams closer together with those designing products is important. However, this does not require new organisational arrangements and the study does not put forward details or compelling arguments for how this should be done.

Recommendation 2: *Include mobilisation objectives and means in all corporate, country and sector strategies, with details on baselines, target ranges and new metrics for mobilisation, types of instruments, expected volumes of blended finance and EBRD investment, and underlying levels of subsidisation and leverage.*

Management partly agrees with this recommendation. Management agrees that increased mobilisation is one of the strategic objectives of the Bank and as such should feature in the medium term strategic planning document (the SCF) and in the annual strategic planning document (the SIP). As such, opportunities and challenges for mobilisation would also be discussed, as relevant, in the country and sector strategies. However, Management does not agree with the study recommendation that sector and country strategies should set the expected amount of blended finance and the EBRD investments. Country and sector strategies set Bank priorities in the countries of operations and outline how they can be delivered, including the types of instruments and relevant metrics to measure performance and results (e.g. volume of capital markets transactions facilitated). The precise level and composition of total investment is not prescribed as the Bank takes a market-driven approach, while also in many cases striving to build and further develop markets. EBRD will do all it can in its countries to deliver on country strategies, and in line with the Bank's three operation principles (and good principles of risk management, for example country concentration). Further, opportunities for mobilisation also depend on market conditions which are difficult to predict. ABI and AMI as well as estimated blended finance are considered and specified annually at the institutional level in the Strategy Implementation Plan.

Recommendation 3: *Include mobilisation target ranges in the Strategic and Capital Framework (SCF) and associated SIPs, developed in accordance with financially sustainable yield on capital criteria in corporate and departmental scorecards. Quarterly reports to the Board, funding to ensure staff skills* and an effective MIS should provide support.

Management agrees with this recommendation. Management agrees that increased focus on mobilisation requires clear and coherent objectives and carefully balanced incentives. Mobilisation (AMI) is already included in the Corporate Scorecard and the way that it is included is being looked at as part of the Corporate Scorecard review. Proposed changes, if any, will be discussed with the board in the context of committee meetings on the Corporate Scorecard review.

Currently, ABI and AMI have equal weight in the Corporate Scorecard and the Banking scorecard. The scorecards include other related objectives such as income generation, portfolio, operating assets and disbursement targets that support investments. Management notes that the scorecards also include measures of transition impact, which directly reward mobilisation (such as supporting development of investor base and capital market development), and reflects the catalytic effect of the EBRD investments, advisory services and policy engagements (mobilisation in the broader sense).

Management believes that it is important to promote a mind-set of always considering the appropriateness and feasibility of sharing risks of each transaction with other investors. There is no inherent contradiction between the goals of mobilising and ABI. There is simply a balance to be struck and the Bank will seek to provide the right incentive for both. As part of the Corporate Scorecard review, consideration will be given to better align incentives aimed at optimising total EBRD investments that capture both ABI and mobilisation.

Recommendation 4: *Upgrade MIS treatment of data on mobilisation and use of blended finance, review policies for provisioning allocating capital and measuring project and corporate performance to ensure yield on capital calculations provide an accurate measure of performance across instruments, and types of investments.*

Management partly agrees with this recommendation. Management agrees that an improvement of processes and investment around MIS systems for data on mobilisation and the use of blended finance is required. Current systems need to properly manage financial instruments such as guarantees and whilst these systems allow tracking of external financing of the Bank's projects, accurate maintenance of project financing information outside the Bank contractual relationships is limited by resources and the information being readily available.

Management disagrees with the rest of the recommendation. The Bank's accounting policies adhere to the International Financial Reporting Standards (IFRS). The provisions, in particular, are governed by the IFRS 9 standard, which requires detailed modelling of expected credit losses on all financial assets not carried at fair value through profit and loss. The Bank implemented IFRS 9 Impairment in 2018 and was advised in this process by PWC. Furthermore, the Bank's financial statements, including provisions, are subject to internal controls and review by external auditors. Indeed the Bank's impairment and provisioning is identified by the external auditors as one of two key audit matters in the Bank's financial statements, and therefore these balances receive an even more thorough scrutiny than usual.

In the context of this recommendation, Management notes that allocation of capital to individual projects is not governed by the Bank's accounting policies but by the Capital Adequacy Policy. The current Policy was approved by the Board of Directors in 2019, following detailed discussions at three Financial and Operational Policy Committee meetings. The Policy is anchored in rating agency methodologies and follows the relevant provisions of the Basel III Accord (the post crisis update of the Basel prudential framework rules). In particular, it follows the mandated approach of equal treatment of risk exposures under guarantees and funded instruments (see rules 78 and 79 in https://www.bis.org/bcbs/publ/d424.pdf).

Furthermore, Management believes that the EBRD is at the forefront of IFIs in terms of its suite of return on risk adjusted capital measures. There is a disciplined focus on RAROC embedded in the project decision making and an overall assessment of the return on risk-adjusted capital during the annual SIP process that assesses the effectiveness of the capital deployment and the overall financial sustainability of the Bank.

Management believes that the current suite of return on risk adjusted capital metrics already provides an accurate measure of performance across instruments. Consequently, and given the absence of specific recommendations how these tools could be further improved, Management is unable to take this recommendation forward. However we will endeavour to continue perfecting the tool set whenever deficiencies are identified.

Comments on the analysis and related findings

Management has a number of comments on the analysis and related findings.

1. Proposed business model to enhance mobilisation and current practices in the Bank

- Management notes that the study proposes the Bank changes its business model (to an originate-to-distribute) and organisational structure (for instance to a matrix similarly to the IDB structure). Yet the report does not clearly outline the benefits of such changes, nor does it elaborate what exactly is meant by an originate-to distribute model. The study refers to models and instruments used by various other MDBs (e.g. WB/IFC, or IDB), without providing evidence on whether and how they result in increasing mobilisation.

- The study advocates for the model of originate-to distribute (sell), once construction risks are mitigated (similar to an investment bank), but does not analyse the trade-offs. The report also makes no attempt to present the impact on the Bank of the proposed fundamental change in its business model, for example on revenue generation (impact on reducing Operating Assets) and mandate considerations (quick exits from large transactions which may need stability post construction and continuation of delivery of transition impact objectives). It also underestimates the overall importance of maintaining the level of Bank investments for successful policy dialogue in support of reforms and advisory services (and for direct mobilisation, both current and in the future).
- Finally, while selling down EBRD holdings of tradeable instruments (such as bonds) before maturity may have many advantages, including from the additionality perspective, the sale would not be recorded as mobilisation of external finance. In addition, not all of B Loans can qualify as PDM and, for example, the FMO participated in two of our syndications in 2015.
- Management notes the study implies that financing in local currency is insufficiently incentivised and even discouraged. These claims are unfounded. The Bank is a leader in this area (at 31 per cent of number of operations in 2019), it does more than any other MDB) and local currency lending is cited as a distinct comparative advance of the Bank in strategic documents. From a transition impact perspective, there is explicit premium in ETI rating for certain types of local currency transactions. Also, there is a dedicated unit in VP3 in place to support local currency operations. The Bank's LCY and capital markets initiative has resulted in a growing share of projects financed in LCY. The study highlights the need to develop FX and other hedging instruments to support LCY transactions; however, there is no analysis on the efficiency of existing instruments to hedge FX risks.
- LCY financing has been an important part of the Bank's business as this is needed by clients and mitigates currency risk. Many countries of operations are building up large, long-term, unhedged and uncosted FX liabilities to fund their infrastructure needs. In discussions at PF4SD, FX - alongside risk profiles – was clearly identified as a major hurdle for mobilisation. In a world of fully developed local capital markets, a far greater percentage of infrastructure investment would be financed using LCY financing to match local revenue streams/local funding. However, this problem cannot be easily overcome, and will take time as countries deepen their capital markets through reforms, which cannot be solved through individual projects. This underlines the importance of the LC2 programme. In this respect, the study suggests that the Bank needs to develop the domestic investor base, but fails to acknowledge the considerable work being done across the Bank and the slow nature of progress on this front across all (undercapitalised) emerging markets.
- With regard to mobilisation, there is lack of evidence that LCY financing can lead to an increase in mobilisation, as often commercial banks do not have access to long-term local currency. Finally, it is important to understand that currently LCY financing have tenors that are too short, and with high pricing, making these a difficult fit for infrastructure projects with long-asset lives and seeking low interest margin financing.

2. Definitions, strategy and reporting

- The study inaccurately states that there is no formal definition of mobilisation or a mobilisation strategy at the EBRD, and that for example the IFC does have the latter. Even though the Bank does not have a formal mobilisation strategy as such, there has been considerable thought and purpose in how the Bank mobilises. As mentioned above, mobilisation has been the subject of a number of presentations to the Board by management, all of which were commended with recommendations

being highly supported by the Board. The Bank has consistently been and remains one of the most successful MDBs in terms of mobilisation on both, absolute and relative terms, with material annual mobilisation amounts. This is a reflection of the Bank's specific private sector development mandate and is a result of a well-developed modus operandi, which gives priority to private sector mobilisation and creates the incentives to actively seek such mobilisation across all deals where possible, prioritising funded private debt providers over other sources.

- IFC's mobilisation success seems overstated throughout the report, given for example what is known about poor returns and uncertain future of the IFC's AMC, as well as on the amounts raised and speed of deployment of its MCPP program.
- Multiple teams across the Bank are key to mobilising external capital; deep technical understanding of the relevant topics is essential for such mobilisation. EBRD has been exceptionally successful in developing and engaging such technical knowledge (e.g. ESG, IPPF). The report should provide clearer credit to this.
- Management agrees that AMI as currently defined in the Bank does not capture all forms of mobilisation. These include advisory services that lead to successful PPPs, for example. As such, with regard to the statement "metrics such as ABI and AMI do not measure mobilisation", Management believes a more accurate phrasing would be that AMI 'does not measure the full extent of mobilisation', as now all private section participation is captured under the AMI definition.
- Management suggests that the study highlight that the DFI principles on the use of blended concessional finance are aligned with the OECD principles, and not contradictory in any way. It would be helpful for the study to highlight that EBRD studies on blended concessional finance and associated investment are part of the DFI working group on blended concessional finance, and that EBRD provides data on blended finance to OECD for their papers. We believe OECD catalytic capital refers rather to TC grants only, and also the OECD has not resolved the issue of attribution of mobilisation to the TC providers.

3. Role of donor funds and donor fundraising model

- Management notes that the study discusses the role of grants in mobilising additional capital. Greater leverage is attributed to TCs (project preparation, policy advice), while concessional loans and capex grants are seen as subsidising. Management notes that this analysis compares absolute volumes of TCs and CAPEX grants/concessional loans and is taken out of context. In private sector operations, EBRD uses more market-like donor funded instruments, while CAPEX grants are mainly used in municipal and transport projects in countries with higher affordability constraints. This needs to be accurately reflected (e.g. page 5). In the MEI sector, especially in Central Asia (but also in some other regions), we have projects where the donor funds (TC and co-investments) are larger/same as EBRD's own investment and many cases where it is about 20-30% of EBRD's investment. In these cases, there are clearly affordability factors at play.
- Management welcomes the study's recognition of the role of advisory services for policy reform for upstream activities and mobilisation. However, Management does not agree that staff are discouraged from providing advisory services. Statements such as "As EBRD mainly acts as an investor, rather than advisor, returns are limited to financial instruments" downplay the Bank's essential role in ESG enhancement and policy reform. The Bank currently uses donor resources plus SSF for upstream activities, and also to create project pipelines and prepare bankable projects. For instance, the work done for project preparation by the IPPF supported by donor funds that open up

space for private sector participation. Our policy dialogue and focused efforts like PPP pipeline development via transactional advisory (i.e. IPPF), where we earn fees from both governments ("transaction support fee") and the private sector ("reimbursement fee") are critical to our business as they open up downstream financing opportunities for all, including the private sector. As these are fee-based services that are part of PDM. The experience of the IPPF has proven to be successful and in demand from both public sector clients (who welcome the expert support our IPPF provides), and the private sector clients who look for the Bank to ensure that projects with bankable structures are being tendered by the governments around the region. IPPF, which is described in Annex 4 of the report, is now an established tool/product that the OLs and sustainable infrastructure group as a whole utilise to build pipeline of PPPs. Our PPP advisory pipeline, launched under our innovative IPPF approach, now includes 12 separate mandates across the transport and social infrastructure sectors. Management agrees that an even more holistic and coordinated approach between our upstream activities and downstream investments would facilitate deeper transition impact across our CoOs.

- The analysis propagates a fundraising model that targets explicitly and strategically higher mobilisation whereby EBRD has power over the use of funds and can centralise donor inflows in a few large vehicles. This would then allow a fund allocation approach dictated by EBRD aspirations for mobilisation, return on capital metrics, etc. potentially through an auction approach, to maximise VfM in the use of donor funds; this mechanism is unclear and unspecified, especially in the light of difficulties to properly measure catalysation mentioned above.

- Management recognises that treating donor inflows as part of a broader mobilisation agenda is worth further consideration. In principle, it would valorise this work, help us set better targets and develop useful metrics, and could kick off new ways of working across the Bank. However, despite many efforts, this is not how our fundraising model works. Donor funds are received on very different terms and the study does not really acknowledge this. Management notes that while we are seeing larger donor programmes, many of which combine reimbursable and non-reimbursable funds or TC plus risk-sharing, they are still typically single donor funds, and donors are very demanding and insist on directing their use. At the same time, Management recognises that while our donors have not very explicitly sought us out for this purpose, there are clear trends in the donor world moving in this direction and we will follow up closely.

- More specifically, the study recommends that pools of pre-committed financing be put in place along the lines of IFC's MCPP finance and MCPP infrastructure. Management recognises that the Bank and MDBs more widely should indeed make a concerted effort to establish refinancing opportunities for operational PPPs to attract the entry of certain institutional investors such as insurers into brownfield PPPs, thus allowing the original investors to reinvestment in fresh greenfield infrastructure projects elsewhere. There may well be demand for a type of new impact investment fund for infrastructure that would see institutional investors buying into the Bank's existing portfolio, thus providing a means for more institutional investment to occur. Management would like to clarify that both have been considered and are under development as indicated in the December BIS, and this would need to be acknowledged in the study.

- The report is silent on EBRD's role in managing NDEP and E5P on behalf of 28 donors and 8 implementing agencies. This is a unique function in the EBRD (similar to the World Bank's role in other climate funds) hosted in ESD, that could be replicated for other funds, and further enhance the profile of the institution and the impact of its grant funds mobilisation.

4. Guarantees and mobilisation challenges

- Management notes that the study often associates increased innovation with an increase in the use of guarantees. It would be helpful to better understand this presumptive link.
- The role of donor funded guarantees is not articulated enough and it would be interesting to focus on how EBRD can use donor funded guarantees to mobilise more. Guarantees are not only used in the ETC region (page 31, 36), but target other countries as well (SEMED).
- Management considers Unfunded Risk Participations (URPs) to be an important tool for the Bank to generate additional operations in key countries and/or with existing clients. They also allow the Bank to mobilise additional investment, and, if desired, scale the approach in a straightforward manner. The use of URPs receive the same treatment as ABI for Banking teams and carry the same lending incentives as direct lending for OLs. Hence, staff incentives do not prioritise direct lending approvals as suggested in the study.
- There is also an established order of mobilisation, with funded options taking priority over URPs. This needs to be recognised in the report.
- The Bank has quite significantly scaled up the use of URPs. A total of nearly 60 URPs worth ca EUR 1.2 billion have been signed since 2014. Annual volume of URPs has grown quickly over recent years (rising from two URPs for EUR 48 million in 2014 to nearly EUR 600m in 2019 across 25 URPs). The Bank has concluded URPs in 10 countries of operation to date, and for instance in the infrastructure sector in 2019, there were eleven URP operations for EUR 260 in total; these transactions freed up nearly EUR 50 million in Bank capital.
- The study states that URPs do not constitute mobilisation, and that AMI is not a good measure of mobilisation. However, MDBs are making substantial efforts to involve the private sector on commercial terms on an unfunded basis via guarantees or credit insurance, and the MDB community is working to ensure that those efforts are recognised as unfunded mobilisation, as the EBRD did when it incorporated URPs in its AMI definition.
- Management believes there is limited acknowledgment in the study about the Bank's initiatives and innovations and the low replicability across markets and MDBs of complex and very specific transactions including the use of guarantees and blended finance. ESFD is another new instrument with added complexity, cost and risks (as described further in the detailed comments at the end), and its replicability is still to be tested. It would be useful if the study were to consider why or acknowledge that new products have not generated broader demand - the innovative Elazig financing was widely publicised, but there has been no opportunity to replicate. Clients consistently feel that these products are expensive for them as borrowers, given the complexity of existing products. Furthermore, in some markets, certain investors would actually prefer to take on more risk to increase returns and therefore do not seek out guarantee instruments, which also have a market price. Accordingly, for all these reasons, clients tend to avoid using guarantees unless there are no other alternatives. This would point to a need to develop or continue to use simplified and replicable approaches that are easier to develop, understand, administrate and scale.
- Providing guarantees or structured instruments at scale for major infrastructure projects to attract additional private sector funds is likely to have limited impact on additional mobilisation in light of the nature of these projects. These projects return only so much financial profit, which will need to be distributed between the different classes of capital. Equity investors in our countries will look for

exceptionally high returns and commercial debt providers will also look for pricing in line with project and country risk. Therefore there may not be sufficient returns left to compensate for the sub-debt/credit enhancement/guarantee risks unless there is an element of (potentially distorting) blending or the infrastructure user charges higher tariffs which could be prohibitive.

- The study recommends the introduction of guarantees in the early stages of project development when risks are greater. However, this may increase the risk that transactions are signed without a market test and therefore without viable long-term funding in place. Systematically doing this would risk introducing market distortions via risks to project execution or costly financing structures for the Bank, should it be unable to refinance/sell down its exposure.
- Finally, the study notes that PDM is lower in infrastructure projects, but fails to explain that this reflects a larger share of sovereign lending for infrastructure, and that sovereign project cannot be syndicated and are usually co-financed by IFIs.

5. Issues related to pricing, costs and structuring including of proposed mobilisation instruments

- The study does not acknowledge that infrastructure transactions, in particular, are structurally market-tested given the frequent presence of other financing parties alongside the Bank. There is an established market for secondary loan trading, the economics of which reflect risk taken at any point in time. Should the Bank wish to sell down assets post-construction, Loan Syndications (LS) would be able to determine market appetite and pricing at that point for each project.
- The study assumes that AMI targets are driven by risk management considerations, whereas, while mobilisation is an effective risk management tool, targets are set to incentivise mobilisation and are delivered through projects that can be syndicated or where large amounts exceed Bank risk appetite.
- It is suggested that full wrap guarantees that increase project ratings could reduce finance costs below levels based on project risks, however this does not take into account the costs of the guarantee, which should reflect project risks. Thus while enabling mobilisation of institutional investors, guarantees are unlikely to reduce financing costs.
- The study suggests that securitisation can be more profitable than debt financing without substantiating such statement by looking at potential costs of a securitisation of IFI assets both in terms of structuring costs and the risk/return distribution within the structure. Creating a slice of a portfolio that is acceptable to the market on a risk/return basis may leave the Bank with a high risk/low return slice, as opposed to a more profitable outcome.
- The study suggests that EBRD create subsidiaries without assessing the impact of the required consolidation of such subsidiaries in the Bank's financial accounts and understanding whether these subsidiaries would have the same privileges and immunities.
- The study suggests URPs are used to avoid losses on projects that perform less favourably. URPs are used to manage exposure and URP providers are seeking well performing assets.