

Blending from the Ground Up

Multilateral and National Development Bank Collaboration to Scale Climate Finance

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ABBREVIATIONS

ADB	Asian Development Bank
AfDB	African Development Bank
AIIB	Asian Infrastructure Investment Bank
ALIDE	Latin American Association of Development Financing Institutions
BTH	Beijing-Tianjin-Hebei region
BNDES	Brazilian National Bank for Economic and Social Development
BRD	Development Bank of Rwanda/Banque Rwandaise de Développement
BRI	Belt and Road Initiative
CAF	Capital adequacy frameworks
CFF	Climate Finance Facility
COP29	29th United Nations Climate Change Conference
DBG	Development Bank of Ghana
DBN	Development Bank of Nigeria
DBSA	Development Bank of Southern Africa
DFIs	Development finance institutions
EAC	East African Cooperation
EADB	East African Development Bank
EE	Energy efficiency
EIB	European Investment Bank
EGIP	Embedded Generation Investment Program
EMDEs	Emerging market and developing economies
ESCO	Energy service company
ETM	Energy Transition Mechanism
FDN	Financiera de Desarrollo Nacional
FICS	Finance in Common Summit
FIL	Financial Intermediary Loan
FIRA	Trust Funds for Agricultural Development/Fideicomisos Instituidos en Relación con la Agricultura
FiT	Feed-in tariff
G20	Group of 20
GCF	Green Climate Fund
IBRD	International Bank for Reconstruction and Development
ICICI	Industrial Credit and Investment Corporation of India

ICT	Information and communications technology
IDB	Inter-American Development Bank
IEO	Independent Evaluation Office
IFI	International financial institution
I&G	China National Investment and Guaranty Corporation
IsDB	Islamic Development Bank
JBIC	Japan Bank for International Cooperation
JET	Just Energy Transition
JETPs	Just Energy Transition Partnerships
LICs	Low-income countries
MDBs	Multilateral development banks
MFF	Multitranche financing facility
MIGA	Multilateral Investment Guarantee Agency
MSMEs	Micro-, small- and medium-sized enterprises
NDBs	National development banks
NDCs	Nationally determined contributions
PDBs	Public development banks
PFI	Participating financial institution
PPI	Private Participation in Infrastructure
PPP	Public-private partnership
PT SMI	PT Sarana Multi Infrastruktur
RES	Renewable energy sources
SADC	Southern African Development Community
SDGs	United Nations 2030 Sustainable Development Goals
SDIC	China's State Development & Investment Corporation
SIO-GFF	Sustainable Development Goals Indonesia One – Green Finance Facility
SLB	Sustainability-linked bond
SMEs	Small- and medium-sized enterprises
SMV	Special Mission Vehicle
SOV-FIL	Sovereign Financial Intermediary Loan
TDB	Trade and Development Bank
TKYB	Development and Investment Bank of Türkiye/Türkiye Kalkınma Bankası
TSKB	Industrial Development Bank of Türkiye/Türkiye Sınai Kalkınma Bankası
UNCTAD	United Nations Conference on Trade and Development

EXECUTIVE SUMMARY

International financing for development has persistently fallen short of developing country needs. That gap has widened dramatically with the onset of the climate crisis, where the costs of climate inaction far outweigh the financing needed in developing countries to catalyze low-carbon, socially inclusive and resilient growth trajectories and adapt to climate-related shocks that are already damaging development prospects.

There is broad agreement that development finance institutions (DFIs) will have to assume a more central role in helping to mobilize more resources, both international and domestic, for development and climate goals. Although DFIs have upwards of \$23 trillion in assets, until recently they have lacked an effective institutional framework for cooperating amongst themselves to leverage those assets for structural transformation in general and green structural transformation in particular. The recent emphasis on country platforms to coordinate efforts around national plans and strategies provides an opportunity to develop such a framework by placing national development banks (NDBs) and DFIs as the key levers of country-led resource mobilization.

“Blending from the ground up” is a call to establish partnerships across public finance institutions that are clearly aligned with the host government’s development and climate change priorities and focus on transformational programs and projects that would not be realized in the absence of public support. This requires mobilizing private capital which is risk-tolerant, patient as well as willing to share risks and rewards of investments in a policy environment which is enabling but also regulated and accountable to citizens.

The paper is not intended as a comprehensive mapping of potential public-public partnerships but rather identifies a sub-set of such partnerships built around the synergies between NDBs and multilateral development banks (MDBs). Utilizing five case studies, examines how partnerships between the two have worked in practice. These case studies include the Islamic Development Bank (IsDB), the European Investment Bank (EIB), the Asian Development Bank (ADB), the Interamerican Development Bank (IDB) and the New Development Bank. The case studies focus on green energy and provide the empirical foundation for identifying the opportunities and barriers to scaling up MDB-NDB collaboration.

Key Findings

- The report shows that NDBs and DFIs are uniquely poised to serve as key partners for MDB development and climate finance strategies given their potential complementarities accessing external finance, lowering the cost of capital, managing and mitigating risk, identifying bankable projects and capacity building.
- MDBs have had a long, but often forgotten history of collaborating with NDBs. While there is currently an incipient revival of such partnership, this could stall in the absence of a comprehensive MDB-NDB collaboration policy. Most MDBs don’t have specific policies or strategic frameworks for engaging with NDBs.
- Our analysis of the recent wave of partnerships shows strengths and weaknesses that need to be accentuated and addressed.
 - a. The favorable terms at which NDBs obtain financing from MDBs are critical to making capital affordable for the intended beneficiaries and helping hedge risk (especially currency risk) that NDBs can’t manage on their own.

- b. Projects which are embedded in comprehensive programs, clearly aligned with government's priorities and backed by an enabling policy environment are more predisposed to innovation and success.
- c. Local currency lending is still under-utilized due to perceived difficulties.
- d. Technical assistance significantly increases the chances of success of a project, and capacity building at scale can contribute to nurturing a "coherent global ecosystem of public-public financing," while also having a significant financial leveraging impact.
- e. Partnerships between MDBs and NDBs are characterized by a strong reliance on different types of derisking instruments, mostly without the means to assess their additionality and ensure accountability of the private sector involved.

Policy Recommendations

1. **MDBs should institute policies that encourage partnerships with national development finance institutions.** Partnerships between MDBs and NDBs should be embedded with a strategic vision that values and prioritizes the public nature of MDBs and NDBs, both around the delivery of public goods, as well as wider development objectives. This vision should be broader than simply leveraging their combined resources to attract private finance and focused on boosting public investment and should be geared towards unlocking the complementarities and synergies between MDBs and NDBs.
2. **NDBs could play the role of a financing anchor for country platforms by coordinating resources around country-owned plans.** NDBs are not only delivery vehicles but can also be key partners in proactively coordinating technical assistance, policy support to the host government and the design of a financing strategy that best reflects national priorities. The role of NDBs as anchors of country platforms should be reinforced by improved country-level coordination between MDBs as called for by the Group of 20 (G20) Roadmap on Strengthening MDBs.
3. **Additional concessional funding is necessary to scale up green finance and renewable energy investment, including for the development of innovative currency risk hedging instruments and the provision of impactful technical assistance and capacity building.** In a context of high interest rates and currency devaluation, it is critical to put NDBs in the position to access capital at low cost, nationally and internationally, and to focus more explicitly on instruments designed to mobilize domestic savings.
4. **MDBs and DFIs need to experiment with more risk-taking, including through the development of new guarantee products, which are still under-utilized, and NDBs need to expand their potential sources of funding and use of new financial instruments.** Collaboration among donors, MDBs, international financial institutions, and emerging market and development economy (EMDE) governments to implement and scale up currency risk mitigation solutions is urgent and paramount to reduce the delivered cost of capital and unlock private climate finance for EMDEs. MDBs could facilitate experimenting with different solutions by introducing more flexible risk assessments allowing engagement with a wider range of domestic financial institutions and providing technical assistance and capacity building for the development of local financial markets in EMDEs.
5. **MDBs and bilateral agencies should support portfolio guarantees to bolster the financing capacity of NDBs.**
6. **MDB-NDB partnerships would benefit from easier country access to international climate funds, including through easier accreditation processes and harmonization of regulatory regimes.**

São Paulo, Brazil. Photo by Bruno Thethe via Unsplash.



INTRODUCTION

With less than a decade to 2030, the United Nations warned that 85 percent of the UN 2030 Sustainable Development Goals (SDGs) were off track or regressing (UN 2023). The Inter-Agency Task Force on Financing for Development that consists of UN agencies, the International Monetary Fund (IMF), the World Bank and other international institutions estimates that the SDG financing gaps have increased by 56 percent since 2020 (UN 2024). The most conservative estimate of the financing needed to meet the SDGs and related goals of the Paris Agreement is \$3 trillion annually by 2030 for emerging market and developing countries (EMDEs), not including China (IEG 2023). A recent study by the UN Conference on Trade and Development (UNCTAD) (2024) estimated that developing countries require around \$1.1 trillion for climate finance from 2025, rising to around \$1.8 trillion by 2030. At the UN climate conference in Baku, governments agreed on the need to mobilize \$1.3 trillion in external finance from a wide range of sources (UNFCCC 2024).

Achieving this stepwise increase in capital for both traditional development projects and enhanced climate action is critical to driving sustainable development, preventing catastrophic warming, protecting critical ecosystems and adapting to climate shocks that are certain to intensify even under best-case scenarios. Much of this capital is needed for investment in low-carbon and climate-resilient infrastructure and buildings, sustainable agriculture, and nature-based solutions. Not only would the benefits of such investments outweigh the costs of inaction, but if made effectively, they could also trigger transformational growth trajectories across developing countries.

However, despite the ambition professed at global policy fora, far too little capital is invested in developing countries, to the point that net financial flows are falling and even turning negative in some countries (ONE Campaign 2024). This is especially the case for highly indebted countries which, in recent years, have faced booming debt service costs (Zucker-Marques et al. 2024), causing some of the world's poorest and most climate-vulnerable countries to spend more than twice as much to service their debts as they receive to fight the climate crisis (IIED 2024). Some estimates suggest that nearly \$200 billion in bond and loan repayment flowed out of developing countries to private creditors in 2023 (Summers and Singh 2024). Illicit financial flows from developing countries have been estimated (with considerable variation) in the hundreds of billions of dollars (Brandt 2022). But outflows of capital are also due to the fact that significant amounts of savings from developing countries are being invested in assets abroad instead of supporting domestic investment (Volz et al. 2024a).

MDBs Responding to the Challenge of Climate Finance and the Energy Transition

In recent years, and more so since the COVID-19 pandemic, heightened expectations have been placed on development finance institutions (DFIs), and public development banks (PDBs) in particular, as critical actors capable of mobilizing capital for climate and development, managing climate risk and establishing the green infrastructure base (including financing renewable energy, energy efficiency and low-carbon transport) on which sustainable development pathways can be built. The recent outcome documents agreed under Brazil's Group of 20 (G20) Presidency have identified DFIs as key to strengthening transitional planning and consolidating country platforms to deliver on climate ambitions (G20 MDB Roadmap 2024).

Such expectations are justified by the distinct mandate and business model of DFIs, which gives them the potential to provide long run, low-cost financing that can not only be directly employed for crucial investments themselves, but also to "crowd in" private sector resources as well. DFIs depend

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directly or indirectly (through domestic fiscal authorities or government guarantees) on taxpayers to contribute relatively small amounts of capital, which is then leveraged through bond issuances that are subsequently on-lent to borrowing members at costs and maturities that the borrowing member would not be able to replicate in the private market-place (Humphrey 2022)¹.

DFIs are a broad category lacking an agreed definition. They include a variety of arrangements, from local public commercial banks to state-owned sectoral financing institutions to multilateral institutions such as the World Bank. There are more than 500 multilateral, regional and national DFIs worldwide with combined assets of over \$23 trillion (Xu et al. 2021). The Institute of New Structural Economics (INSE) at Peking University mapped 47 multinational (global and regional) DFIs, 369 national and 111 subnational institutions (Xu et al. 2021). In terms of geographic distribution, Asia hosts the largest number of national PDBs and DFIs (117), followed by Africa (92), Europe (78), America (65) and Oceania (17).

In this study we focus on PDBs, operating at the national, regional and multinational levels. With NDBs, we refer to financial institutions established or owned by a central government to serve its national strategy or fulfill public policy. Unlike commercial banks, NDBs are not driven by profit maximization. Projects undertaken by NDBs are usually characterized by long maturity, large scale, high risk and positive externalities.

In this context, multilateral development banks (MDBs) have sought to position themselves as key actors in the energy transition and as mobilisers of climate finance more generally. According to the latest *Joint Report on Multilateral Development Banks Climate Finance*, in 2023 MDBs provided a combined \$125 billion in global climate finance, double what they provided in 2019, of which \$74.7 went to low- and middle-income economies and \$50.3 billion went to high-income economies (EIB 2024). At the 29th UN Climate Change Conference (COP29) in Baku, MDBs announced that they plan to reach \$120 billion of annual collective climate financing for low- and middle-income countries by 2030 (World Bank 2024a).

To respond to the heightened expectations placed on them, MDBs have initiated a broader reform agenda aimed at making them “bigger, better and more effective” at meeting countries’ SDGs and addressing global and regional challenges (G20 MDB Roadmap 2024). Areas of reform include scaling up their financing capacity (by using existing capital more efficiently and developing new forms of capital to expanding shareholder capital), transforming country engagement for better collaboration, enhancing development effectiveness and expanding private finance mobilization capacity (CGDEV 2024).

Most of the progress so far has been achieved in the area of balance sheet optimization (Humphrey 2024), following the 2022 report of the G20 Independent Review of Multilateral Development Banks’ Capital Adequacy Frameworks (CAF Review). MDBs have announced that they plan to mobilize upwards of \$400 billion in new lending from the implementation of the CAF Review recommendations. They have also taken commitments towards working together as a system (IDB 2024a) – for instance, in setting joint goals and financial targets, harmonizing methodologies for impact reporting and strengthening country-level collaboration and co-financing, including through country platforms (World Bank 2024b).² The G20 Roadmap on Bigger, Better and More Effective MDBs builds on

¹ This paper does not consider the potential role of Central Banks in extending credit to DFIs as part of the public financing landscape, on this important issue see Kedward et al. (2024). Carrots with(out) sticks: Credit policy and the limits of green central banking, Review of International Political Economy, May.

² In 2024, MDBs also published a common document called Country Platforms for Climate Action - MDB Statement of Common Understanding and Way Forward, reaffirming their joint support for efforts to foster collaboration between host countries, MDBs, donors, and the private sector.

the progress made in implementing CAF recommendations and encourages MDBs to go further by examining the adequacy of their resources against client needs and shareholder objectives.

One of the key elements of the 'better' MDBs agenda is country platforms. Country platforms are host country-driven initiatives that coalesce a broad range of stakeholders around a national vision for a coordinated approach towards common goals (Hadley et al. 2022). On some interpretations, these are vehicles to substantially scale up blended finance and enable host governments to connect "stand alone" private finance with Nationally Determined Contributions (NDCs) (Carney 2021). Others have identified a typology of options, where country platforms vary by emphasis on public or private finance and narrow or broad goals (Hadley et al. 2022).

Just Energy Transition Partnerships (JETPs) are a type of country platforms whereby bilateral and multilateral finance providers are collaborating with national governments, including national development banks, to develop green financing platforms that can serve as a catalyst for public, private and international capital through a range of financial instruments. PT Sarana Multi infrastruktur (PT SMI) in Indonesia and the Blue Green Bank of Barbados are notable examples (for further details see Box 4). Just Energy Transition Platforms have, however, been unduly optimistic about the engagement of the private sector in these efforts, which reflects the broader logic of the 'billions to trillions' agenda, discussed more below. What does seem clear is that NDBs could be crucial actors in the implementation of country platforms, including by serving as the financing pillar. However, doing so will require an understanding of their roles as being more comprehensive than delivery vehicles alone.

The Risks of Derisking

A defining characteristic of the MDB reform agenda as developed so far is the belief that public capital can and should be used for leveraging private finance, and that doing so can help unlock and scale up new money, going from "billions to trillions." This approach aims at leveraging private international capital to meet climate and infrastructure development goals through "derisking" the desired investments with public money, using a variety of financing instruments that *blend* public and private capital, such as guarantees, public-private partnerships schemes, securitization and more.³

Despite the trust that the World Bank and other MDBs continue to place in this agenda, the efficacy of the billions to trillions approach has been widely discredited. Commentators have referred to it as "as reality-based as a Shrek movie" (Kenny 2022a) or "the magic pony of private finance" (Beattie 2024). The World Bank Chief Economist Indermit Gill, pointing to two consecutive years that have witnessed net positive outflows from developing economies to external creditors, agreed that the 'billions to trillions' had "proven to be a fantasy" (World Bank 2024).

The wry metaphors refer to the meek results achieved so far. A recent World Bank working paper co-authored by Gill assessing the track record of five regulatory and financial instruments for mobilizing private capital (guarantees, public-private partnerships, syndicated loans, sustainable financial contracts, and climate and banking regulations and policies) finds that not only has the volume mobilized by these instruments fallen far short of the anticipated trillions of dollars, but also that there is very limited evidence of their additionality (*ibid*). In other words, it has not been demonstrated that the "innovative" use of public resources has crowded-in private capital to countries that would not have otherwise received it (Cull et al. 2024).

According to one extensive assessment of the blended finance landscape, "each \$1 of multilateral development bank and DFI invested mobilizes on average \$0.75 of private finance for developing

³ This approach has been dubbed the "Wall Street Consensus" and marks a break with the broader policy-driven approach of the Washington Consensus, see Dafermos et al. (2021).

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countries, but this falls to \$0.37 for LICs (low-income countries). Expectations that this kind of blended finance can bridge the Sustainable Development Goals financing gap are unrealistic: 'billions to billions' is more plausible than 'billions to trillions' (Attridge and Engren 2019). An IMF study finds that the multiplier effect of MDB's climate financing averaged to 1.2 in 2020, with the European Investment Bank (EIB) having the highest multiplier effect at close to 2 and the World Bank Group at 0.6 (IMF 2022). Another recent study by the International Energy Agency (IEA) found that for every dollar disbursed by DFIs into energy-related fields between 2016 and 2022, only around 33 cents were mobilized from the private sector. Meeting investment needs under a net zero by 2050 scenario would require instead that each dollar of concessional funding provided by 2035 to unlock a further \$7 in private capital over the same time horizon (IEA 2024). The State of Blended Finance report (climate edition) noted that aggregate annual financing flows in blended finance fell from \$1.3 billion in 2013 to \$0.9 billion 2023, precisely the opposite direction the 'billions to trillions' proponents had hoped for (Convergence 2023).

Particularly disappointing have been trends in Public-Private partnerships (PPPs), which have long been promoted by MDBs as the preferred model for financing infrastructure investments. In fact, PPPs in developing countries peaked in 2012 at \$158 billion and have almost halved since then, dropping to \$86 billion in 2024 (Kenny 2024). Moreover, available data suggest that existing PPPs are very concentrated in a few countries. According to the World Bank's 'Private Participation in Infrastructure Projects (PPI) Database', which collects data for 137 low- and middle-income countries, in 2023 just five countries (China, Brazil, Philippines, India and Peru) attracted \$66 billion, capturing almost 77 percent of global PPI investment. In comparison, 26 International Development Association (IDA) countries received investment commitments amounting to \$4.3 billion in 2023 (World Bank 2023).

Among the reasons for limited uptake of PPPs is their often complex legal and financial arrangements requiring, at a minimum, a certain level of institutional capacity for successful outcomes, which only larger, middle-income countries might have. The lack of available fiscal space and the potential for efficiency gains – in terms of the time and cost of delivering projects – are frequently put forward by policymakers, in both developed and developing countries, as the reason for pursuing them. However, the supporting evidence on their performance is mixed, especially when the ultimate impact on citizens is considered, and for developed and developing countries alike (National Audit Office 2018; Sial and Sol 2022). There can, moreover, be significant hidden costs in PPP contracts, and there is a good deal of evidence to suggest that traditional forms of government borrowing are often cheaper than those involving PPPs (Kenny 2022b).⁴

In addition to the limited success in crowding-in private finance, there is concern that initiatives aimed at leveraging private investment by "de-risking" confine public sector involvement to socializing the risk, which are often hidden and contingent in nature, while the gains are grabbed by the private sector (Sial 2024). There is also the risk that attracting private capital to fund public infrastructure will further advance the privatization of public goods across EMDEs (Arun 2023), which is particularly worrying given the complexity and lack of accountability and transparency of blended finance, which in turn limit its public scrutiny (Mawdsley 2018).

Ultimately, the mobilization of private capital (especially international capital) is constrained by the fact that the returns expected by private investors from investments in developing economies simply does not match with the returns yielded by investment opportunities in developed economies, especially SDG- and climate-related investments (Gabor 2021). Infrastructure investment in developing countries remains overwhelmingly in the realm of public finance. According to a World

⁴ For a more detailed assessment of public-private partnerships, reaching much the same conclusion, see Leigland 2024.

Bank survey, in 2017 83 percent of infrastructure financing was public, with the share of private finance as low as five percent in sub-Saharan Africa (World Bank 2017).

Considering the underwhelming performance of the “billions to trillions” approach, and the scale and urgency of development projects that are truly socially just and environmentally sustainable and cater to the public good, the momentum created around a comprehensive MDBs reform agenda should be used to rethink the kind of partnerships that these institutions can and should develop. A good candidate for such partnerships are NDBs and other related DFIs, focusing on their shared public policy mandate.

Rethinking the Public Development Banks Partnerships Ecosystem

The focus on mobilizing private finance through derisking has *de facto* confined MDBs to the task of absorbing much of the risk attached to large-scale and inherently uncertain investment projects, thereby making their risk-return profile more attractive to private finance, particularly the leading non-bank financial institutions with control over massive asset portfolios.

However, if DFIs, and MDBs in particular, are to catalyze and scale up financing for EMDEs to meet their climate and development goals, and to ensure that the transition is a just one, they need to shift from a “passive” financing strategy to playing a much more proactive and creative role.⁵ Beyond de-risking instruments, they can and should play a strategic role in supporting coordination between various actors in the financial sector, combine their concessionary resources and structure innovative financial instruments and solutions, acting as important actors to scale productive investments, including in greener activities.

They also need to have a greater and more deliberate focus on channeling private domestic savings into domestic investment, while operating on the grounds of more realistic leveraging objectives. This requires transforming partnerships at national level, so that these are more clearly grounded in country priorities and country ownership. Crucially, they need to develop partnerships that can both strengthen the mobilization of public funds and provide more accountability for their use.

It is argued in this paper that an insufficiently explored option for “blending” is with public financial institutions in developing countries, harnessing the unique complementarities of MDBs and NDBs. Both the opportunity and the necessity exist for scaling up these collaborations, in view of the expanding global ecosystem of PDBs (Marois et al. 2024) that can act in the public interest and is centered around meeting the SDGs and the Paris Agreement.

This paper builds a case for scaling up and transforming public sector collaboration around blending the resources of public development finance institutions. With this in mind, Section 2 outlines a rationale and framework for MDB-NDB collaboration and shows examples of where this is already happening. In particular, it illustrates five key complementarities that offer potential for further development and scaling up, provides an overview of instruments and financial mechanism at the disposal of PDBs, and illustrates the main constraints faced by NDBs in expanding their collaboration with MDBs and their engagement in green finance. Section 3 conducts a comparative analysis of five illustrative case studies of MDB-NDB collaborations on clean energy. The case studies offer a snapshot of how the collaboration is playing out in practice, highlighting challenges and factors of success. The fourth section summarizes key findings and lessons learned on the opportunities and barriers to scaling MDB-NDB collaboration to meet shared climate and development goals. Section 5 offers recommendations for further research and policy engagement.

⁵ See also Murau et al. (2024) on the kind of monetary architecture needed to undertake this shift.

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THE CASE FOR NDB-MDB COLLABORATION

The popularity of PDBs has shifted considerably over time: during the 1950s and 1960s, they were considered critical instruments of post-war reconstruction and state-led national development strategies, and proliferated across the world, often with the support and encouragement of the World Bank (Chandrasekhar 2022).

From the late 1970s to the late 1990s, PDBs were progressively downsized and privatized in many developing countries, on the grounds of their apparent ineffectiveness, variously attributed to mismanagement, fiscal losses and political interference, as well as the increasing availability of private capital. Around 250 PDBs were privatized between 1987 and 2003, often as part of World Bank structural adjustment programs (De Olloqui et al. 2013). For instance, in 1955 together with the World Bank, the Asian Development Bank (ADB) supported the creation of the Industrial Credit and Investment Corporation of India (ICICI) as a public development financial institution for providing medium-term and long-term project financing to Indian businesses. ICICI was then transformed into a commercial bank in the 1990s as India liberalized its economy (ADB 2010).

Since the late 1990s, PDBs have come back into vogue, in recognition both of their potential countercyclical role and a willingness to adopt a more patient approach to lending, with their role in China's remarkable investment-led growth story galvanizing a renewed interest. Notably, following the 2008 global financial crisis, their credit portfolio increased by 36 percent, in contrast to a 10 percent increase by commercial banks (De Luna-Martínez and Vicente 2012). Wider attention followed the global financial crisis, with the International Development Finance Club launched in 2011 and accelerated after 2015 with the increasing demand for infrastructure and climate finance and the adoption of the SDGs, especially in the context of the poor performance of the private sector to serve these purposes. The COVID-19 pandemic also gave a new impetus to PDBs, which played a critical countercyclical role, mitigating the economic collapse, catalyzing the financial recovery of firms and achieving different development objectives, including in Latin America (Cipoletta Tomassian and Abdo 2022) and in Africa (Attridge et al. 2022). Since 2020, PDBs and DFIs have convened annually at the Finance in Common Summit, a global forum established to help them align and cooperate in the achievement of the 2030 Agenda for Sustainable Development and Paris Agreement on Climate Change.

There are good reasons to continue more MDBs-NDBs integration and alignment. Supporting a resilient and sustainable low-emissions future implies a big investment push into new energy, food and transport systems that PDBs are well placed to support. Infrastructure development is a multi-faceted challenge that requires large-scale funding and complex financial engineering, an appropriate regulatory framework and, above all, dedicated human, technical and institutional capacities. This not only means financing new green technology and projects but also supporting businesses through the transition. Companies may need to find new or different suppliers, adjust their production processes for energy efficiency, find new markets or even rethink their logistical operations altogether to manage the transition.

This broadly defined challenge around resource mobilization and coordination enjoins mission-oriented public institutions to create and implement the desired public policy agenda instead of trying to fix underperforming markets in the hope these might eventually deliver (Mazzucato 2016). This is particularly true where there is a pronounced strategic role for a project, in the presence of strong complementarities across multiple projects or where the social value of an investment means that its revenues are often hard to appropriate fully for individual investors, as can be the case with large infrastructure projects (Aghion and Howitt 2006). The investment challenge is even more

pronounced when there is an urgency to achieving a desired goal that defies simple market logic, as most vividly demonstrated during military campaigns and their aftermath (Hart-Landsberg 2022).

There is no doubt that, in the face of new and demanding investment challenges, private sector mobilization needs to be improved, but this should also be complemented by mobilizing and coordinating much more domestic public finance, not least in EMDEs. This must in part come from more effective fiscal regimes (at both national and international levels) but it should also involve an expanded role for NDBs.

Unlike the private sector, which is “profit-oriented,” NDBs are “mission-oriented.” In other words, they are attuned, and in important respects beholden, to public policy goals, which, at least on paper, resonate with the stated agendas of the MDBs. Moreover, their business models are such that they can operate with lower expected financial returns on their investments than the private sector—seeking only to meet the objectives of the NDB and maintain credit ratings rather than to maximize profits and ensure adequate dividend payments for their shareholders (Griffith-Jones and Ocampo 2018; Barrowclough et al. 2021). NDBs are, moreover, familiar with the operations of domestic firms and their financing needs and challenges (including small- and medium-sized enterprises who face a perennially tight financing constraint) and tend to have closer connections to domestic service providers, capital markets and policymakers than do MDBs (Studart and Gallagher 2018). Finally, NDBs are uniquely positioned to act on climate risk because they sit at the nexus of key actors within the national economy and financial sector (Smallridge and de Olloqui 2011).

As such, closer collaboration between MDBs and NDBs can be mutually beneficial and unlock potential synergies of considerable value to the scaling-up challenge. Deepening and streamlining such collaboration could help develop a new model of partnerships that is more effective not only in leveraging more capital for climate and development, but also at directing and employing it for the intended objectives. In the following sections, we look at the complementarities that justify a closer MDBs-NDBs collaboration, the instruments at their disposal and the constraints that they face in the process.

Potential Complementarities Between MDBs and NDBs

In recent years, there has been a growing recognition of the potential of MDBs partnerships with NDBs, as testified by the popularity of Finance in Common Summits (FICs) under the auspices of the French Development Agency. Research has begun to examine the conditions under which MDB-NDB partnerships can be scaled up to finance the green transition (E3G-CPI 2023) and to operate more effectively and coherently as part of the global financial architecture (Marois et al. 2023).

In this report, we explore five key complementarities between MDBs and NDBs that offer potential for further development and scaling up in view of nurturing a global system of public development finance: access to external finance, lowering the cost of capital, risk management and mitigation, project identification, and capacity building.

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Table 1: Potential complementarities Between MDBs and NDBs

Barriers	Comparative Advantage		
	MDBs	NDBs	Options for Collaboration
1. Accessing external finance and widening the pool of sources	✓		<ul style="list-style-type: none"> Co-financing On-lending Accessing international funds for green finance
2. Lowering cost of capital	✓		<ul style="list-style-type: none"> Accessing concessional loans and guarantees Accessing international grants and funds for green finance Financial structuring and blending to provide adequate conditions in terms of grace period, maturity, interest rates
3. Risk management and mitigation	✓	✓	<ul style="list-style-type: none"> Cooperating on feasibility study and project preparation such as environmental, technical, financial, social risk assessment Sharing risks through co-financing, blending and PPPs. Accessing foreign exchange, commercial and political risk insurances, risk-sharing facilities and other guarantees
4. Project identification		✓	<ul style="list-style-type: none"> Demand Creation Awareness and embeddedness with domestic service, financial, and technology providers
5. Capacity building	✓	✓	<ul style="list-style-type: none"> Awareness and capacity building of project proponents, domestic service, financial and technology providers Best practice sharing between countries and domestic institutions Support process of Paris Alignment

Source: Authors assessment based on interviews and Smallridge et al. 2012.

ACCESS TO EXTERNAL FINANCE

NDBs are compelled by the significant financing required at the national level to address the socioeconomic implications of climate change to step up resource mobilization at the national and international level, especially in the face of tighter governments' budget constraints (see for instance the case of BNDES illustrated in Section 3) and domestic capital markets that lack maturity and face liquidity constraints. This means expanding their sources of funding to include private investors, MDBs, regional development banks and climate investment funds.

MDBs are well-placed to support NDBs in this process. They can provide capital directly through on-lending and co-financing, and they can help channel international climate finance to developing countries using NDBs as intermediators, including facilitating match-making between domestic policymakers and international investors, technology suppliers and service providers. Beyond on-lending and co-financing, MDBs and vertical climate funds could also purchase hybrid capital of NDBs. Such use of hybrid capital may require policy changes for multilateral funds and DFIs but could unlock value external finance to DFIs (Humphrey 2025a). They can also support NDBs issue green bonds on the domestic and international markets.

LOWERING THE COST OF CAPITAL

A major constraint for domestic DFIs and NDBs is the high cost of capital they face in national and international capital markets. This is determined, in large part, by the sovereign credit rating of the

government that backs them (Almeida et al. 2017), which in developing countries is often weak. In a study examining southern-led MDBs, Humphrey found that these banks need to charge higher prices for their loans to borrowers given their own high cost of borrowing. Therefore, even though there has been an increase in demand for climate finance from borrowers, the high prices limit actual uptake (Humphrey 2025a). MDBs can help address this constraint by providing concessional loans, guarantees and other credit enhancement instruments. For example, an MDB may provide a political risk guarantee which would lower the risk profile and enable the NDB to obtain better terms (longer maturities and lower cost) on the international markets than those markets would otherwise be willing to grant.

RISK MANAGEMENT AND MITIGATION (INCLUDING FOREX RISK AND CLIMATE RISK)

MDB-NDB collaboration can go a long way in improving risk management and mitigation on both sides, especially for climate risk, and increasing overall risk appetite. Risk reduction can take many forms, such as setting up a pool of funds that can provide and scale up collateral and guarantees, facilities that operate with first-loss instruments, offering technical assistance and advisory services, limiting exposure to losses, improving credibility, and eliminating funding gaps. MDBs can also help NDBs to strengthen their institutional capabilities to identify, assess, manage and monitor climate-related financial risks and to use a climate risk lens to identify business opportunities that arise from the energy transition (Netto et al. 2021).

Another important area of untapped collaboration is in the management and mitigation of currency risk and in the provision of local currency lending. MDBs primarily operate in hard currency (USD, EUR and Japanese yen) to take advantage of the lower interest rates and greater liquidity of hard currency capital markets and to preserve their AAA credit ratings, which in turn enables them to borrow and lend on favorable terms. This creates a mismatch between loans issued in hard currency and the returns on the loan investment in the borrowers' local currency. Such mismatch is especially pronounced in clean energy infrastructure projects, which primarily generate revenues in local currency, by selling electricity to the local grid. This mismatch affects borrowers (including NDBs) which face increased debt burdens in the event of currency devaluation (as in the case of the Damu Entrepreneurship Development Fund illustrated in Box 5), as well as loan providers, which face heightened credit risk. Section 2 illustrates the strategies that are being put in place by MDBs, NDBs and DFIs at large to overcome this challenge.

PROJECT IDENTIFICATION

A missing pipeline of bankable projects ready to be financed is a commonly recognized obstacle to a speedy energy transition in many developing countries: it makes it more difficult for MDBs to target lending to the intended objectives and therefore diminishes appetite to scale up financing, including seeking new resources from shareholders.

For example, the abundant solar and wind energy potential of the Southern African Development Community (SADC) is largely unexploited because of the low rate at which renewable energy projects are being developed for bankability (Musasike et al. 2024). A similar challenge is faced by Chinese DFIs seeking to scale up renewable energy investment in countries participating in the Belt and Road Initiative (BRI) (CCICED 2023).

Project identification and preparation are limited by a weak policy enabling environment, limited technical capacity (e.g. for environmental assessment, financial modeling, etc) and lack of pre-feasibility funding for early-stage project development and supporting related infrastructure. On

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the side of NDBs, MDB funding criteria are not always amenable to their local context and clients, requiring advanced levels of project preparation and bankability. Intended beneficiaries – small- and medium-sized enterprises (SMEs) and local communities with limited access to mainstream finance – often struggle to recognize the eligibility of projects and activities.

MDBs can help remove these constraints with targeted technical assistance and adequate support for affordable pre-feasibility funds and project preparation facilities. On their side, NDBs can leverage their increased level of trust and connection with local service providers, SMEs, governments and markets to channel this support into project design geared to the local economy. This is particularly important as PDB focus on financing the energy transition, from scaling up renewable energy to support for more locally embedded sectors, such as climate adaptation infrastructure, circular economy and low-carbon transport, where the closeness to local communities is critical for project success. Moreover, as NDBs are embedded in their local contexts and policy environments, they are also well poised to support the creation of a pipeline of bankable projects. In this manner, there is a major synergy between MDBs that are interested in bankable projects on the ground and the local knowledge and expertise of NDBs.

CAPACITY BUILDING

MDBs have a wealth of experience in sharing best practices, delivering technical assistance and capacity building for banking and financial management. Most often, this is provided to beneficiary governments in the context of a specific project. However, a recent survey conducted by the Overseas Development Institute (ODI) of nearly 500 senior government officials and MDBs senior staff in country offices found that government officials thought that MDBs do not deliver technical assistance and policy advice that has long-term impact (Prizzon et al. 2022).

MDBs should accordingly re-focus their offer of technical cooperation and policy advice to NDBs to ensure it has long-term impact beyond individual project cycles. For instance, they can help existing NDBs build strong governance structures, identify capacity gaps and address them through awareness raising, knowledge- and information-sharing and training sessions, incentivise alignment and implementation of policies, regulations and frameworks. This kind of comprehensive support is particularly required as MDBs accompany NDBs in the process of Paris Alignment, which includes mainstreaming climate considerations in their mandates, institutional strategy, governance and investment portfolios (CPI-E3G 2023).

Instruments of Collaboration

In theory, there are a wealth of financial mechanisms that MDBs can employ in their collaborations with NDBs, including concessional and non-concessional lending, grants, equity and guarantees or other risk management and credit enhancement instruments, depending whether the counterpart operates as a Tier 1 or a Tier 2 institution, or both.⁶ In practice, according to a survey conducted by Marois et al. (2023), non-concessional lending is the most frequently used instrument, followed in order by concessional lending, grants, equity and guarantees.

ON-LENDING

On-lending is the most straightforward and operationally easier option for MDBs. A recent study by E3G looking at MDBs' climate finance lending found 55 cases of on-lending from MDBs to NDBs in EMDEs, with a total volume of \$7 billion during the period 2015-2022 (CPI-E3G 2023).

⁶ Tier 1 institutions provide financing directly to end-users (e.g., loans to SMEs and direct equity investments). Tier 2 institutions provide finance through financial intermediaries (e.g., brokers and banks) that ultimately pass it along to end users.

As underlined in the study, lending arrangements are implemented through a variety of secondary transactions, including direct financing to projects, PPP facilities and corporate credit lines, often with the support of third parties, especially through sovereign guarantees. Credit lines are found to be a particularly fast and flexible instruments of financing, especially if structured as general purpose financing (see Section 3 case study 2 on EIB credit line to the Development Bank of Southern Africa (DBSA). Loans so obtained can be used by beneficiary NDBs to leverage additional financing at the national level through financial intermediation (see Box 1).

MDBs and IFIs can also supply finance to borrower governments to help capitalize NDBs. Recently, the IMF has been involved in the establishment of an NDB through its Resilience and Sustainability Facility loan to Barbados. The \$10 million loan is being used by the government to set up the Blue Green Bank, a sustainable climate finance entity aimed at enhancing climate resilience across Barbados and the wider Caribbean by stimulating growth in securities and loan markets, unlocking extra funds to back projects dedicated to climate change mitigation and adaptation. Several other institutions, including the Inter-American Development Bank (IDB), the World Bank, the Development Bank of Latin America and the Caribbean (CAF), the EIB and the Green Climate Fund have already committed to support the Blue Green Bank through technical support or capitalization (IMF 2023).

Box 1: IDB onlending to Financiera de Desarrollo Nacional (FDN) in support of Colombia's JET and development of a green bond market

In 2024, the IDB approved a loan program of \$139.9 million (including a grant component of \$1.4 million) in support of Colombia's Just Energy Transition (JET) plan. The loan is entrusted to Financiera de Desarrollo Nacional (FDN), a development bank initially created by the government and currently under a mixed ownership structure. FDN is specialized in financing and structuring infrastructure projects with high social returns, and it manages risks and facilitates the entry of financing from private banks and institutions. The government has selected FDN to lead the mobilization of private financing of JET activities.

The IDB is funding the program under its IDB CLIMA facility, which provides concessional financing for the development of thematic and green debt markets. Building on previous experience in promoting sustainability-linked bonds, IDB CLIMA loans include an interest rate abatement of 5 percent upon achievement of three predefined targets for key performance indicators (IDB n.d.).

In particular, the program will focus on:

- increasing the supply of financing for at least five JET-related subprojects involving nonconventional renewable energy sources and for the scaling up of enabling technologies for their deployment;
- strengthening FDN's technical capacity for the identification, design, and management of its climate project portfolio, in view of preparing itself to access the green debt market;
- improving FDN's climate monitoring, reporting, and verification (MRV) capabilities to contribute to national climate reporting efforts and support eventual green debt issuance.

Source: IDB 2024c.

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GUARANTEES AND OTHER CREDIT ENHANCEMENTS

Credit enhancements are risk-sharing instruments that help borrowers obtain financing at better terms than would be otherwise possible. Guarantees, in particular, operate as a form of insurance for the investor and therefore help to mobilize additional private capital. The most common form of guarantee covers credit risk, but increasingly a variety of instruments are being developed. For instance, the IDB has created a flexible guarantee instrument that can be used to cover credit and political risks for green infrastructure financed through public-private partnerships or concessions, which can be issued to sub-national entities, local governments or any other public entity (Netto et al. 2021).

MDBs can also support NDBs through financial and technical assistance in developing guarantee products provided to local financial institutions geared towards green investment, as in the case of Trust Funds for Agricultural Development (FIRA) in Mexico (see Box 2), thereby contributing to advancing and operationalizing national climate and energy goals (ibid). Another innovative approach is the use of guarantees to collateralize the issuance of sustainability-linked bonds (SLB). This was recently seen in Rwanda, where the World Bank provided an IDA credit of RWF10 billion to the government to collateralize the issuance of SLBs by the Development Bank of Rwanda (Banque Rwandaise de Développement, BRD), which raised RWF30 billion (\$24 million) from domestic investors. The pricing on the bonds backed by the MDBs was more affordable than issuances by the bank without the MDB backing (Volz et al. 2024a).

MDBs and bilateral agencies would also extend portfolio guarantees directly to NDBs. As discussed in Humphrey (2025a), MDBs have developed portfolio guarantee platforms that are backed by donor governments. NDBs would also benefit from such portfolio guarantees since it would enable the bank to increase its lending capacity. For example, the World Bank's guarantee arm – the Multilateral Investment Guarantee Agency (MIGA) – backed the borrowing by Trade and Development Bank (TDB) enabled the TDB to benefit from lower cost and longer term financing from commercial banks (Humphrey 2025a).

However, guarantees are still underused and carry their own risks (Sial and Chandrasekhar 2024). A recent study by the Climate Policy Initiative (CPI 2024a), found that while guarantees are among the preferred risk mitigation tools of private investors, their use in developing countries and for climate risk is still limited, fragmented and not well understood.

Box 2: Supporting FIRA in Mexico to develop guarantee products and SME 2nd tier lending

Established in 1954 in Mexico, FIRA (Fideicomisos Instituidos en Relación con la Agricultura) is a second-tier development bank that offers credit and guarantees, training, technical assistance and technology-transfer support to the agriculture, livestock, fishing, forestry and agribusiness sectors. In particular, FIRA offers guarantee products to local first-tier financial institutions to share lending risk, which in turn facilitate access to credit for local commercial investors.

Over the years, FIRA has received financial support and technical assistance from a variety of MDBs and DFIs. For example, the IDB is currently supporting FIRA in developing an \$8 million guarantee, which is expected to leverage \$35 million in loans for the financing of agricultural projects for ecosystem-based adaptation. This includes technical assistance to mainstream adaptation into the institution's structure (IDB 2023). This builds on a previous project in which the Agence Française de Développement (AFD) supported FIRA in the development of a taxonomy of climate adaptation and resilience and in the design of the ProSostenible guarantee (Dalhuijsen et al. 2023). FIRA also received support from the IDB, the World Bank and the Climate Investment Funds for its Energy Efficiency Program, in which FIRA provides a technological guarantee, paying the difference between estimated and realized savings from the adoption of energy-efficient technologies using Clean Technology Fund.

In 2023, the IDB also granted FIRA a \$100 million loan for financing projects for small and medium-sized farmers; agribusiness micro, small and medium-sized enterprises (MSMEs) ; and farmer organizations for resilience and adaptation agricultural activities. The sub-projects are to be identified and financed through FIRA's financial intermediaries network (IDB 2023).

EQUITY CAPITAL

Beyond lending and guarantees, MDBs can go a step further and take a direct stake in NDBs by providing equity capital and becoming shareholders (Volz et al. 2024b). The participation of an MDB as an equity investor would strengthen the NDBs' capital base, boost its lending capacity as well as possibly its governance. The downside is that the NDB could lose autonomy and independence, with the risk of reducing the country's policy space and ability to set its own priorities.

Volz et al. (2024b) illustrate three examples of successful provision of equity and debt capital by MDBs: two NDBs – the Development Bank of Nigeria (DBN) and the Development Bank of Ghana (DBG) – and one regional development bank – the East Africa Development Bank (EADB) (see Box 3).

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Box 3: Equity investment in African national and regional development banks

The DBN was established in 2014 by the Federal Government of Nigeria in partnership with the World Bank, the African Development Bank (AfDB), KfW Development Bank, AFD and the EIB to provide medium- to long-term financing for MSMEs. Its shareholder structure is composed by 18 percent of equity capital (\$50 million) from the AfDB, 7 percent (\$20 million) from the EIB and the remaining 75 percent is held by the Nigerian government through its Ministry of Finance and Investment (60 percent) and the Nigeria Sovereign Investment Authority (15 percent). It has received long-term credit lines from the World Bank, AFD, KfW and AfDB.

The DBG was created in 2021 following the example of DBN. Its mandate is closing the financing gap faced by MSMEs in agriculture, manufacturing, and information and communications technology sectors. Its Board includes representatives as observers from the World Bank and KfW who provide oversight to shield the bank from political interferences (same as DBN). The sole equity owner is for the moment the Ministry of Finance, which received grant and debt capital from AfDB (\$40 million grant), KfW (\$46.5 million loan), World Bank's IDA (\$250 million credit) and the EIB (\$170 million credit).

The EADB is a regional public development bank first established in 1967 under the treaty of the then East African Cooperation (EAC), and then re-established with a new charter in 1980 after the break-up of the EAC. It has a model of equity participation based on Class A equity holders (the member states of the East African Community) and Class B holders (international investors and commercial banks). The latter have the flexibility to exit at any time, and their presence has helped to strengthen EADB standing in credit markets and credit rating agencies. It has been able to borrow from shareholders and development partners (including EIB, AfDB, KfW, NDF, Arab Bank for Economic Development, and the Organization of the Petroleum Exporting Countries Fund for International Development).

Source: Volz et al. 2024b)

GREEN FINANCING PLATFORMS

Finally, an emerging trend involves MDBs relying on NDBs and national DFIs as springboards to develop green financing platforms (also called country platforms). An example of a country platform is a JETP, which involves coordination of international support of accelerated coal retirement select economies. Table 2 provides an overview of the existing JETPs. These platforms are intended to scale up domestic resource mobilization for the energy transition, coordinate international public finance, as well as help attract foreign private capital. By design, they are meant to do so relying on blending approaches and de-risking mechanisms. Given the limitations of these instruments (discussed in section 1), these platforms should be scrutinized to verify that the mechanisms that they employ are fit to cater to the needs of domestic investors and to leverage risk-tolerant, patient capital that is willing to assume some of the risk as well as share the returns with public counterparts – in other words, that they leverage truly additional finance and that this benefits citizens.

Table 2: Overview of Just Energy Transition Partnerships and national development banks

JETP	National Development Bank	NDB's Role
Indonesia	PT SMI	Manager of the Energy Transition Mechanism Country Platform
South Africa	DBSA	Disbursement vehicle ⁷
Senegal	-	No specific role
Viet Nam	Viet Nam Development Bank	No specific role

Source: Authors' compilation.

As Table 2 shows, the role of NDBs in the case of the JETPs can vary, with the PT SMI receiving the clearest mandate on how it can support the country's energy transition. Viet Nam, however, has opted to rely primarily on changes to banking supervision practices to encourage the supply of green credit to increase domestic and international private sector participation in the JETP. While the Viet Nam Development Bank and the Viet Nam Bank for Social Policy have been mentioned in the Resource Mobilization Plan of the Viet Nam JETP, they have not been assigned specific roles (Viet Nam 2023). South Africa's JETP Investment Plan views DBSA and Industrial Development Corporation of South Africa primarily as disbursement vehicles that channel finance from international providers to implementers on the ground.

Box 4: Sustainable Development Goals Indonesia One - Green Finance Facility (SIO-GFF)

In Southeast Asia, the ADB is supporting the Sustainable Development Goals Indonesia One-Green Finance Facility (SIO-GFF), a financing mechanism for green infrastructure projects. The \$150 million sovereign Financial Intermediary Loan (FIL) to the Indonesian Ministry of Finance is onlent to PT Sarana Multi Infrastruktur - Persero (PT SMI). PT SMI is a state-owned infrastructure financing institution set up as a Special Mission Vehicle (SMV) under the Ministry of Finance which lends at commercial rates. While not an NDB, its mandate has been expanding in recent years, in particular since it was chosen as the manager of the Energy Transition Mechanism (ETM) Country Platform in JETP implementation.

The SIO-GFF will finance subprojects that meet green, financial bankability and leverage targets with the aim of catalysing funds from private institutions and commercial sources. Funds will be provided primarily as debt to subprojects but up to 15 percent of total committed funds may be provided as other instruments such as equity, convertible debt and guarantees. It is the first green finance facility in Southeast Asia (Volz and Lee 2024). ADB loan funds will partially finance up to 10 projects worth \$423 million catalyzing around three times private capital into the subprojects (ADB 2022).

The loan is complemented by a technical assistance project aimed at improving PT SMI's institutional capacity for subproject assessment, credit risk appraisal and overall management of the facility. The technical assistance will also support the development of green and SDG subprojects by building the capacities of national and local governments, state-owned enterprises, public-private partnership concessionaires and project special purpose vehicles.

⁷ South Africa. Just Energy Transition Investment Plan. <https://pccommissionflo.imgix.net/uploads/images/South-Africas-Just-Energy-Transition-Investment-Plan-JET-IP-2023-2027-FINAL.pdf>

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The offer of particular financial instruments by MDBs is ultimately driven by the demand from national DFIs and development banks, and by their capacity to use them. Limited familiarity with increasingly complicated instruments can affect NDBs ability to use different instruments appropriately. Fernandez-Arias and Xu (2020) argue that “NDBs often shoot in the dark when it comes to assessing whether their financial programs should be implemented with loans or loan guarantees, be it directly or indirectly through the private banking system.”

Systematic investment by MDBs in technical assistance can go a long way in building the requisite level of sophistication (see case study 5 in this report). However, in assessing what instruments to deploy in MDBs-NDBs collaboration, a key consideration for development banks should be identifying the financial instruments that best encourage economic (and climate) risk-taking, while avoiding transferring too much risk from the private financial intermediary to the development bank, ultimately minimizing the policy direction of the intended projects (Griffith-Jones et al. 2022). Simpler instruments like direct loans and equity tend to have a stronger development impact than more complex instruments such as guarantees, securitisation, on-lending to second tier banks and structured products (including green financial platforms of the kind discussed above), which however may have a larger leveraging potential (ibid). This is particularly a challenge in financing the energy transition and projects with a strong development component, for instance targeting MSMEs or local communities, where the closeness to the needs and specificities of the intended beneficiaries is critical for project impact. In the context of MDB-NDB collaboration for climate and development, these trade-offs need to be carefully taken into considerations so that the mechanisms adopted leverage truly additional finance that contributes to country's investment priorities and benefit its citizens.

Constraints to Scaling up MDBs-NDB Collaboration

Since the establishment of the Finance in Common Summit in 2020, a few studies have investigated the factors that restrict MDBs collaboration with NDBs and national DFIs (Marois et al. 2023), in particular on climate finance and Paris Alignment (CPI-E3G 2024).

These studies point to five broad categories of constraining factors: political economy and governance, public finance mandates, institutional capacity and expertise, and currency risk. Under the first category, the most common barriers to further engagement include political uncertainty and market and fiscal conditions (discussed more in detail below). Collaboration between MDBs and NDBs can be hampered by political changes in the host country. Similarly, market and fiscal conditions shape the types of instruments that are realistic in a given economic context.

The second kind of barriers concerns NDBs' public finance mandate and the operating policy context, which can limit their general risk appetite. NDBs often have mandates which lack clear climate investment objectives and do not always have operating frameworks for implementing them. For example, a Climate Policy Initiative study found that less than half of the public developments tracked in the study have committed to align their portfolios with the Paris Agreement (CPI-E3G 2023). This reduces NDB's flexibility and responsiveness to emerging innovation, and hampers their appetite for climate risk taking.

Third, mismatches in institutional capacity and technical expertise can limit NDB's ability to develop project pipelines for MDBs financing, to play a role as financial intermediators and to engage with the procedures and approval policies that come with MDB loans. Marois et al. (2023) also point to the lack of global reporting standards or institutional commitments to the tracking and reporting of MDB to NDB financing. This makes it difficult to track collaboration and to draw comparisons across regions.

Fourth, a critical impediment to further cooperation is the scarce availability of concessional finance, which is also required to overcome the other types of constraints. NDBs themselves often struggle to

reach MSMEs, due to their limited resources and technical capacities, especially in project financing. NDBs can find it technically difficult to design and set up large aggregate programs for MSMEs financing amenable to MDBs lending, as this usually requires alignment with several intersecting goals such as environmental sustainability, gender, inclusion and others.

Finally, currency mismatches remain a major impediment (Finance in Common 2023). Currency risk can be particularly acute when NDBs borrow in foreign currency while their revenue is denominated in local currency. MDBs loans provided in foreign currency are also ill-suited for programs aimed at MSMEs because NDBs also have to charge for the cost of foreign exchange risk hedging, making the price of loans unaffordable for most MSMEs.

According to a recent study, nearly two-thirds of PDBs recognize exchange rate risk as a significant threat to their profitability but only 20 percent of them have access to a wide variety of hedging products (TCX et al. 2023). Commercial financial products to hedge currency risk are often not available for borrowers in developing countries, especially for projects with long-term maturities. When they are available, they are usually very costly, because priced on the grounds of very uncertain market conditions and reflecting perceived risk of investing in developing countries, to the point of offsetting the lower interest rates available for hard currency loans from MDBs (CPI 2024b). As pointed out by Persaud (2023), some currencies are in fact over-priced, with forward rates exceeding actual (ex-post) rates of currency depreciation and unnecessarily adding to the already high cost of capital.

Analysis in Bonizzi et al. (2024) finds that the risk of local currency lending can in fact be lower than that of foreign currency lending. Their study also shows that only half of the MDBs analyzed (out of a sample of 29) offer local currency lending. Based on data for syndicated loans, Bonizzi et al. (2024) find that only four institutions (CAF, the Asian Infrastructure Investment Bank (AIIB), the Euresian Development Bank and New Development Bank) have local currency loans exceeding 10 percent, with the New Development Bank having nearly two-thirds of its issuance denominated in local currency. Moreover, with the exception of the AIIB, the greatest majority of this issuance is focused on upper-middle-income countries.

Box 5: Challenges to ADB local currency lending in Kazakhstan

In 2005, the ADB introduced local currency products for private and public sector borrowers, but local currency lending remains challenging in practice. In 2023, ADB's local currency loans amounted to \$1.72 billion, just above 1 percent of total lending (ADB 2005; ADB 2024).

In 2010, the ADB approved the Small and Medium Enterprise Investment Program in Kazakhstan, a multitranche financing facility (MFF) for \$500 million. The investment program was designed to provide financial intermediation loans to Damu Entrepreneurship Development Fund (Damu), a state-owned entity, with guarantees from the Government of Kazakhstan. Damu would then on-lend in local currency (*tenge*) to participating financial institutions (PFIs) for lending to small and medium-sized enterprises (SME) (ADB 2010).

The first tranche, which was disbursed in September 2011, and the subsidiary loan agreements with the PFIs, were indeed denominated in *tenge*, with the explicit objective of mitigating the currency risk for Damu while providing capital in local currency. The tranche was funded through a cross-currency swap with an international bank, with ADB leveraging its AAA rating to extend the tenor and lower the cost of funds.

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For subsequent tranches, it was envisaged that the ADB would issue a local currency bond but obtaining all required approvals proved complex and not feasible in the project timeline. In addition, funding of subsequent tranches through international cross-currency swaps also became infeasible following the 2014 devaluation of the *tenge*. As a result, the second and the third tranche of the loan and the related subsidiary loan agreements were denominated in US dollars. The currency risk was transferred to PFIs, which hedged their US dollar exposure through swaps provided by NBK National Bank of Kazakhstan.

Damu expressed dissatisfaction with this arrangement, lamenting the high risk involved, the lack of flexibility and the negative impact on the beneficiary PFIs (ADB 2020b).

Addressing the challenge of local currency lending is a necessary condition to achieve green investment at scale in developing countries, and it requires MDBs and NDBs, as well as donors and IFIs at large, collaborating to devise innovative mechanisms that reduce hedging costs and improve the affordability of local currency financing. While some MDBs and DFIs have been deploying a mix of approaches to reduce the cost of local currency lending, these are still under-utilized and under-developed, in large part because they remain too expensive. Recently, new mechanisms have been proposed and experimented with by different stakeholders that seek to support investments in local currencies, promote onshore local currency operations, and make hedging instruments for climate-related projects more accessible and affordable. The main options and proposals currently available for addressing currency risk are reviewed in Annex 1 of this paper (for a more detailed analysis, see also Bonizzi et al. 2025 and CPI 2024b).

The five sets of constraints illustrated above echo the findings of research looking at the barriers faced by NDBs and domestic DFIs in scaling up green financing activities and investment in the energy transition. Studies based on the IDB's experience with technical assistance and capacity building on green finance point to unclear government mandates for NDBs in engaging with national climate commitments, weak institutional capacity and experience, inadequate finance and risk mitigation instruments, lack of long-term and low-cost capital compounded by the high costs of imported equipment (Smallridge et al. 2013; Abramskiehn et al. 2017; Netto et al. 2021). In particular, many NDBs struggle with financially structuring climate-related projects and overcoming the perception that they offer poor risk-adjusted returns (Netto et al. 2021). These studies emphasize that NDBs need to learn to identify, assess and manage the full scope of the risks and opportunities they face from climate change vis-à-vis the size of their overall assets, their strategic importance to key sectors, and their role in contributing to national and regional growth (Netto et al. 2021). A recent World Bank publication looking at trends and opportunities in green national DFIs also underlines the role inadequate climate policies, funding gaps, lack of capacity and awareness of climate and environmental issues both in the financial and real sectors, and the cost and complexities of green projects (Dalhuijsen et al. 2023).

Shanghai, China. Photo by Yiran Ding via Unsplash.



CASE STUDIES OF MDB-NDB COLLABORATION ON GREEN ENERGY

The breadth, depth and robustness of MDBs-NDBs collaboration varies across regions, countries and institutions, reflecting the diversity of NDBs worldwide, their country context and the specificities of each MDB. According to a recent survey conducted by Marois et al. (2023) MDB to NDB financing is most extensive in Europe, with the EIB and the Council of Europe Development Bank (CEB) funding 22 NDBs between 2017 to 2021, and aggregate financing for the top five NDBs totaling EUR23.85 billion. During the same period, the IDB and the CAF reported lending to 15 NDBs, with financing for the top five totaling EUR8.2 billion. In Asia, the ADB and the AIIB financed 15 NDBs, while in Africa and the Middle East, the Trade and Development Bank (TDB), AfDB and the Islamic Development Bank (IsDB) together financed seven NDBs. Total aggregated financing for the top five NDBs was EUR1.75 billion in Asia and EUR182.64 million in Africa and the Middle East (*ibid*).

In this report, we examine five case studies of MDB collaboration with NDBs in scaling up green finance to advance the energy transition. The MDBs included in the sample are the IsDB, EIB, ADB, IDB and the New Development Bank (Table 3).

The five case studies relate to partnerships with three public NDBs (the Development Investment Bank of Türkiye, the Development Bank of Southern Africa, and the Brazilian National Bank for Economic and Social Development), one private NDB (the Industrial Development Bank of Türkiye), one semi-public guarantee institution (the China National Investment and Guaranty Corporation) and several Latin American public and private DFIs.

The case studies were selected with the aim of including MDBs with a clear climate commitment and a practice of working with NDBs, while offering a broad geographic representation. They were identified drawing from advice and expertise of practitioners in the field, who were interviewed from this purpose. They are not intended to be exemplary or exhaustive of how each of the five MDBs deals with NDBs and other DFIs, but to offer an overview of the diversity of MDBs-NDBs collaboration across Asia, Africa and Latin America in the area of clean energy and green finance (Table 4). The analysis is based on desk reviews of project reports and interviews conducted with MDBs staff and other subject experts between April and August 2024,⁸ and it aims at eliciting insights on how MDBs-NDBs partnerships are playing out in practice and drawing lessons on how to improve collaboration in the dimensions outlined in section 2.

The unit of analysis differs slightly across case studies: in one case (ADB) one single project is considered; in some cases two or more projects are analyzed (for the IsDB, the EIB and the New Development Bank) and one case looks at a full set of programs (IDB). The projects examined are at different stages of implementation, with cases in which outcomes are yet to materialize.

⁸ Staff from the following institutions was interviewed: EIB, DBS, ADB, IsDB, BNDES, New Development Bank, ECLAD, former IDB staff, as well as five experts in the field.

Table 3: Overview of MDBs examined in the report

Bank	Year Established	Total Commitment (2023)	Net or Total Disbursement	Total Equity	Total Equity Investments	Climate Change Target
Asian Development Bank ⁹	1966	\$23.6 billion	\$17.8 billion	\$55.3 billion	\$1.5 billion	\$9.8 billion
European Investment Bank ¹⁰	1958	€320 billion	€54.4 billion	€11 billion	€3.7 million (Equity investments and Infrastructure funds) €1.25 million (other equity investments)	€44.3 billion
Islamic Development Bank ¹¹	1975	\$12 billion	Ordinary Capital Resources disbursements \$2.0 billion	10.8 billion Islamic Dinars	566.7 million Islamic Dinars	The Islamic Development Bank is committing 35 percent of its total annual financing to climate adaptation and mitigation initiatives by 2025 ¹²
New Development Bank ¹³	2015	\$32.8 billion	\$3.4 billion	\$11.5 billion (Q-1 2024)	-	\$5.2 billion committed to climate financing as of 2021 ¹⁴
Interamerican Development Bank ¹⁵	1959	\$13.5 billion (IDB group total: \$24.3 billion)	\$2.9 billion ¹⁶	\$38.8 billion (as on 31/12/2023)	\$32.4 billion (investment after swaps)	\$20 billion in climate finance since 2015 ¹⁷

Source: Compiled by authors.

⁹ Asian Development Bank. (2024b). Financial Report 2023. <https://www.adb.org/sites/default/files/institutional-document/959761/adb-financial-report-2023.pdf>

¹⁰ European Investment Bank. (2023). 2023 Financial Report. https://www.eib.org/attachments/lucalli/20230354_eib_financial_report_2023_en.pdf

¹¹ Islamic Development Bank. (2023). Islamic Development Bank Ordinary Capital Resources - Financial Statements and Independent Auditor's Report. <https://www.isdb.org/sites/default/files/media/documents/2024-05/2023%20OCR%20Signed%20EFS.pdf>

¹² Islamic Development Bank. (2023). Development Effectiveness Report 2023. <https://www.isdb.org/sites/default/files/media/documents/2024-05/Annual%20Development%20Effectiveness%20Report%202023.pdf>

¹³ New Development bank. (2024, February). Investor Presentation. New Development Bank. https://www.ndb.int/wp-content/uploads/2023/10/Investor-Presentation-Q1_2024-NDB.pdf

¹⁴ New Development Bank. (2023). New Development Bank General Strategy for 2022-2026 Scaling up Development Finance for a Sustainable Future. https://www.ndb.int/wp-content/uploads/2022/07/NDB_StrategyDocument_Eversion-1.pdf

¹⁵ IDB. (2023, December 31). Investors. Retrieved September 4, 2024, from <https://www.iadb.org/en/how-we-can-work-together/investors>

¹⁶ S&P Global. (2024, July 17). Inter-American Development Bank 'AAA' Rating Affirmed On Institutional Strategy And Solid Capital; Outlook Still Stable. S&P Global Ratings. Retrieved September 4, 2024, from <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/type/HTML/id/3216008>

¹⁷ IDB. (2023, November 30). IDB group aims to triple climate financing over next decade. Retrieved September 4, 2024, from <https://www.iadb.org/en/news/idb-group-aims-triple-climate-financing-over-next-decade>

Table 4: Five case studies of MDBs collaboration with NDBs

MDB	NDB or DFI	Project/ Program	Financial Support Instrument
Islamic Development Bank (IsDB)	Development Investment Bank of Türkiye (TKYB) (state owned)	TSKB Renewable Energy Program	Restricted Mudaraba Investment Facility \$320 million
	Industrial Development Bank of Türkiye (TSKB) (privately owned)	TKYB Renewable Energy Program	Restricted Mudaraba Investment Facility \$420 million
European Investment Bank (EIB)	Development Bank of Southern Africa (DBSA)	DBSA Climate action facility	Credit line (€22 million)
		DBSA EGIP Facility (Embedded Generation Investment Programme)	Framework loan (€300 million)
Asian Development Bank (ADB)	China National Investment and Guaranty Corporation	Air Quality Improvement in the Greater Beijing–Tianjin–Hebei Region— Green Financing Platform Project	Sovereign Financial Intermediary Loan (SOV-FIL) \$500 million + \$1 million Technical Assistance
Interamerican Development Bank (IDB)	Latin American NDBs and DFIs	LAC Green Finance Program to Mobilize Private Investment in Mitigation Actions and Low-Carbon and Sustainable Business Models through National Development Banks (Phase I – 2016 and Phase II – 2020)	Technical cooperation (\$6 million for Phase I and \$4 million for Phase II)
New Development Bank	Brazilian National Bank for Economic and Social Development (BNDES)	Financing Renewable Energy Projects and Associated Transmission	Non-sovereign loan, \$300 million
		BNDES Clima – Sustainable Financing to Support Global Climate Change Mitigation and Adaptation	Sovereign loan, \$500 million
		Sustainable Infrastructure Project	Sovereign loan, \$1.2 billion sovereign loan

Source: Authors' compilation.

In each of the cases, MDB-NDB collaboration is examined along the dimensions identified in Section 2. The results are summarized in Table 5. The dimensions studied in the case studies are access to external finance, lowering cost of capital, risk management and mitigation, project identification, and capacity building. The relative emphasis of each dimension varies across the case studies as reflected in the write ups in the section to follow. These dimensions informed the questions the research study team asked MDB officials and related stakeholders. For each case study, the challenges and factors of success section identifies the most salient factors and discusses why those factors helped or hindered the achievement of outcomes.

As anticipated, the case studies show that MDB finance offered is indeed in favorable terms and supports the NDB's deployment of green finance instruments. The cases also show that projects that are embedded in comprehensive programs and are clearly aligned with government priorities have a better chance of success than when such alignment is not demonstrable. Even though local currency lending is a major collaboration opportunity between MDBs and NDBs, we find that local currency instruments were underutilized. We found that de-risking instruments were used to mobilize private finance; however, given the lack of frameworks to ascertain impact, the additionality of these instruments is not clear. We also find the provision of technical assistance to be important for effective implementation.

The following section delves into five case studies that explore how multilateral development banks have collaborated together with national development banks on green energy. The case studies are IsDB's engagement with two Turkish NDBs (TKSB and TKYB); the EIB and DBSA joint work on Climate Finance Facility and Embedded Generation Investment Program; the ADB and a Chinese financial intermediary the China National Investment and Guaranty Corporation (I&G); and the IDB's program on NDBs in the Latin America and the Caribbean region. Each case study is structured into background, description and outcomes sections.

Table 5: Summary of findings in five areas of MDBs-NDBs cooperation

	Areas of MDBs-NDBs cooperation				
	Access to External Finance	Lowering Cost of Capital	Risk Management and Mitigation	Project Identification	Capacity Building
IsDB - TKS ^B /TKY ^B	1 st tier on-lending Co-financing with DFIs and project sponsors	Sovereign lending terms	Sovereign guarantee Foreign exchange risk ultimately borne by end users Ability for private sector to benefit from feed-in tariff dependent on project completion date	TKSB and TKYB leading in project identification and sub-borrowers	IsDB provided technical assistance on parameters for eligible projects, monitoring of results
EIB-DBSA CFF and EGIP	1 st and 2 nd tier on-lending Co-financing with Green Climate Fund	Credit line with sovereign lending terms Contribution to increase concessionality of sub-loans	Climate Finance Facility and Embedded Generation Investment Program aim at providing derisking and credit enhancement products to local financial intermediaries, SME and government authorities Foreign exchange risk borne by DBSA	Led by DBSA according to CFF and EGIP's criteria	Not envisioned under the EIB's credit line
ADB - I&G	1 st and 2 nd Tier on-lending Co-financing with Chinese commercial banks and financial leasing companies	Sovereign FIL Financial leasing for purchase of equipment Creation of a yuan account for use of reflow funds	Credit guarantees to SMEs and energy service companies (ESCOs) Credit enhancements for issuance of clean air bonds Foreign exchange risk borne by I&G	I&G leading in project identification in line with broader air quality program criteria.	ADB financed a complementary technical assistance project to strengthen I&G and other stakeholders' management and implementation capacity
NDB-BNDES	1 st and 2 nd Tier on-lending Co-financing (for Fundo Clima)	Blending with other sources of funding to provide better terms for sub-loans		I&G also established a dedicated project management office	Reciprocal learning on how to work together
IDB-LAC NDBs	Support to i) design of proposals for Green Climate Fund; ii) scale up of LAC green bond market	Design of innovative green financial instruments	Support development of Social and Environmental Risk Management System	LATAM Project Hub	Online platforms for knowledge and information sharing

Source: Authors' compilation.

CASE STUDY 1:

ISLAMIC DEVELOPMENT BANK PARTNERS WITH TÜRKİYE'S NATIONAL DEVELOPMENT BANKS TO SUPPORT RENEWABLE ENERGY AND ENERGY EFFICIENCY PROGRAMS

Background

In 2010, the IsDB made the strategic decision to invest in the promotion of the renewable energy sector in Türkiye, through partnerships with two NDBs: the Industrial Development Bank of Türkiye (TSKB - Türkiye Sınai Kalkınma Bankası) and the Development and Investment Bank of Türkiye (TKYB - Türkiye Kalkınma Bankası).

This decision came on the back of the introduction by the Turkish Government of new legislation aimed at incentivizing the domestic production of renewable energy, in view of addressing the growing energy demand while reducing dependency from energy imports and CO2 emissions. In 2005, the government had passed a renewable energy bill (Law No.5346) that provided a guaranteed, feed-in tariff (FIT) for electricity generation from renewable energy sources (RES), which was modified in 2011 to make the guaranteed price more attractive and anchoring it to the US dollar.

Project Description

In 2010, after consultation with the government, the IsDB agreed to a \$100 million (sovereign guaranteed) loan to TSKB for a renewable energy program extended through a mode of financing called *Istisna*. The program initially struggled to deliver because the mode of financing adopted implied that the IsDB had to sign individual financing agreements with the end beneficiary companies, causing legal and regulatory complications and delays to the process. To address the problem, in 2012 IsDB decided to experiment with a mode of financing not yet used in lending to DFIs for infrastructure projects, the *Restricted Mudarabah*. This instrument eliminated the need for the IsDB to enter into individual financing agreements for each sub-project and gave freedom to TSKB as executing agency to adopt its own procedure for appraisal, quality and risk assessment and procurement processes. As a result, the program started to deliver and a second phase of \$220 million was approved by the IsDB in 2013, while the International Bank for Reconstruction and Development (IBRD), EIB and KfW also increased their co-financing for the umbrella program. At the time of project evaluation, the total project cost stood at \$1.73 billion, 215 percent of the planned amount, of which \$320 million funded by the IsDB, \$1.2 billion by international financial institutions and \$300 million by the project sponsors. Overall, IsDB co-financed 10 projects in renewable energy (RE) (including six wind power plants, three hydroelectric power plants and one small-scale rooftop solar power project) and 10 energy efficiency (EE) projects in cement, steel and dye factory.

Following the success with TSKB, a similar renewable energy program was agreed with TKYB. Under the TKYB renewable energy program, 2 EE projects and 43 RE projects were realized (including 31 solar power plant, eight hydroelectric, two geothermal, one wind power and one waste to energy), for a total cost of \$743 million against an initial planned amount of \$550 million. IsDB contributed \$220 million, complementing co-financing from IBRD, EIB, Japan Bank for International Cooperation (JBIC) for \$220 million and the rest by the project's private sponsors.

Outcomes

Overall, the TSKB and the TKYB renewable energy programs were considered highly successful in strengthening Türkiye's energy supply security, reducing energy import dependency and greenhouse gas emissions through the addition of new power generation capacity and the implementation of EE projects. Both over-achieved their intended planned objectives for power generation, CO2 emissions reduction and energy savings. The TSKB program resulted in the installation of 859 MW of new RE generation capacity, 245 percent of the target 350MW and it added 3,276 GWh/year of electricity generation to the national grid. The TKYB program led to 225 MW of installed capacity, in excess of the of 200 MW originally planned and the renewable energy projects contributed 683.4 GWh of electricity to the National Grid in 2016.

The IsDB financing helped spur growth in the renewable energy sector in Türkiye, catalyzing investments from other public development banks and blending with private sector investors. The main risk-sharing mechanism was the adoption by the government of a FiT anchored to the US dollar which protected private investors from the investment and foreign exchange risk, whose implementation was dependent upon investors meeting a pre-determined project completion date.

Challenges and Factors of Success

Three factors were identified as critical to the success of the TSKB and the TKYB renewable energy programs:

First, the strong alignment with the government's objective of increasing the share of RE in total electricity generation to at least 30 percent by 2023. This resulted in a favorable national policy for RE, including the adoption of a FiT at a pre-determined price anchored to the US dollar, and ensured a viable return on investment which made the renewable energy industry attractive to the private sector. The energy producers were shielded from foreign exchange risk because all had earnings indexed to dollar denominated FiT rates. However, domestic end-users paying tariffs in local currency were exposed to price fluctuations.

Second, the intermediary role played by TKYB and TSKB as specialized executing agencies, which, especially in the case of TSKB, had previous experience and institutional commitment to sustainability projects. They enabled the identification of competent beneficiaries among private investors and the assessment and selection of high-quality projects, followed by monitoring through field visits. Technical assistance and capacity building were however necessary before a pipeline of projects with the intended sectoral focus on RE and EE was ready for disbursement.

Finally, IsDB's willingness to experiment with Restricted Mudarabah made it possible to effectively employ TSKB and TKYB as first tier intermediary banks, accessing beneficiaries and transactions that IsDB alone would not have been able to achieve because it is too small and fragmented. However, the effective use of Restricted Mudarabah is dependent on financial intermediary capabilities of the development finance institutions of the beneficiary countries. Currently, IsDB has only nine Restricted Mudarabah projects, of which seven are in Türkiye, one in Benin and one in Egypt.

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CASE STUDY 2:

THE EUROPEAN INVESTMENT BANK (EIB) SUPPORTS DBSA'S GREEN FINANCE FACILITIES

Background

The EIB is considered the world's largest MDB, being active inside the European Union (EU) and in over a hundred non-EU countries. In 2023, it approved close to EUR 77 billion of new projects in EU member states and over EUR 7 billion outside the EU (EIB n.d.). The latter are managed by EIB Global, the arm of the EIB lending to non-EU member states and focused on international partnerships.

The EIB has an established relationship with South Africa and its main public development bank, the DBSA. Since 1995, the EIB has lent more than EUR 3.9 billion to South Africa, including almost EUR 1 billion to DBSA through credit lines. This is made easier by the fact that the EIB issues bonds in South African Rand (ZAR) as part of its funding strategy, meaning that DBSA can draw some of its EIB borrowing in ZAR as well as EUR.

Project Description

The EIB has recently co-funded two important DBSA initiatives aimed at boosting renewable energy production in South Africa and in neighboring countries: in 2020, it provided EUR 22 million credit line (Climate Action Facility) for on-lending to private sector climate action projects; in 2023, it approved a EUR 300 million framework loan for the Embedded Generation Investment Programme (EGIP) (EIB 2019).

The DBSA plans to use the EUR 22 million credit line to co-fund eligible projects under its Climate Finance Facility (CFF). The CFF is a lending facility set up in 2018 by the DBSA with the financial support of the Green Climate Fund (GCF) to incentivize private investment in climate change mitigation and adaptation through (local currency) blended finance instruments and credit enhancements. It targets local commercial banks and businesses in South Africa as well as other ZAR-based countries (Namibia, Lesotho and eSwatini). The initial project cost was \$110 million, of which \$55 million to be provided by the GCF and \$55 million by DBSA. The Facility was meant to be the first in Africa to adopt a "green-bank model" aimed at de-risking climate projects. However, its set up required several adjustments to make it able to serve the intended beneficiary, providing funding to SMEs with otherwise limited access to finance. In particular, the Facility was initially structured as an off-balance sheet trust arrangement with a separate bank account. This set up made it difficult for the DBSA to deploy hedging instruments for the sub-loans extended to the Facility's beneficiaries, with the implication that they would have had to bear the foreign exchange risk. In practice, this hindered the development of a solid project pipeline as well as the mobilization of funding from other investors (GCF 2020). In 2023, the Facility was restructured to a credit line arrangement which allowed the DBSA to take on the Facility's credit risk and handle directly the foreign exchange risk of the GCF's co-funding. Following the restructuring of the CFF, the EIB credit line will be deployed to improve the concessionality of the sub-projects under the CFF (GCF 2023).

The EGIP was established by the DBSA in 2018 with the support of the GCF, to promote the development and scaling up of solar photovoltaic and wind RE embedded generation projects. Embedded generation is the production of electricity from independent smaller-scale power stations, which struggle to access the renewable energy procurement program set up by the South African government because of their weak viability and bankability. EGIP offers a credit support mechanism

through the provision of risk capital to private sector and local government entities. The GCF and the DBSA participate on a matching basis on the subordinated debt and a portion of the junior debt targeted at financing equity for sub-projects by the local communities and SMEs. The total estimated cost was \$537 million, the GCF initially contributed with \$100 million matched by \$100 million from the DBSA. Approximately \$84 million is to be allocated to B-BBEE Broad-Based Black Economic Empowerment (B-BBEE) beneficiaries.

The GCF \$100 million contribution was initially set up as a limited recourse loan, but this arrangement incurred similar challenges with currency hedging to those encountered by the CFF. Similar to the CFF, EGIP's intended end-beneficiaries would have been unable to earn foreign currency earnings and therefore to bear any currency risk. Ultimately, to address the problem the loan was turned into a credit line, which allowed the DBSA to handle the foreign exchange risk directly (GCF 2022). In 2023, the EIB approved a \$300 million framework loan to DBSA for on-lending under the EGIP (EIB 2022).

Outcomes

Both the CFF and the EGIP are still at the early stage of implementation and an assessment of their results is not yet available. However, a preliminary consideration can be made on the role that these facilities can play in South Africa, where, unlike the rest of the continent, the majority of climate finance is provided by (domestic) private actors (86 percent), mostly through debt financing (82 percent). Public sources account for only 14 percent of climate investments, of which 41 percent were from domestic actors and 59 percent were from international actors, including bilateral and multilateral DFIs and climate funds (de Aragão Fernandes et al. 2023). In this context, there is an opportunity for MDBs (and for the EIB in particular) to step up their concessional financing in embedded generation and other renewable projects which are not appealing to private investors but are needed for a just energy transition.

Challenges and Factors of Success

This case study demonstrates the supporting co-financing role that MDBs can play as part of established partnership with NDBs. The EIB was not the main partner in the development of the CFF and EGIP facilities, but it played an important role through the provision of flexible credit lines which improve the concessionality of the sub-loans provided under the CFF and the EGIP. Their set-up was facilitated by the long-standing relationship between the EIB and the DBSA, and it allowed DBSA to deploy them with some autonomy and flexibility. This stands in contrast with the complex process required to devise the right arrangements with the GCF, which contributed to the delay in implementing the two loans. The lack of foreign exchange risk hedging instruments that could be used by DBSA in accordance with its regulatory framework constituted an additional problem.

Overall, the challenges encountered in the process confirmed that the level of concessionality and the ability to hedge forex risk away from end-beneficiaries are critical to promote RE and EE projects that are truly additional to what the private sector can achieve on its own.

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Capetown, South Africa. Photo by Pixelperfektion via Unsplash.



CASE STUDY 3:

THE ASIAN DEVELOPMENT BANK'S SOVEREIGN FINANCIAL INTERMEDIATION LOANS FOR AIR QUALITY IMPROVEMENT IN CHINA

Background

The ADB has a long history of engaging with NDBs and institutions. One of the most heavily used instruments to this end are Financial Intermediation Loans (FIL), provided to domestic (public and private) financial intermediaries to finance specific projects which are individually too small to warrant direct ADB supervision. FILs can be used to target certain types of sub-borrower beneficiaries like MSMEs, women entrepreneurs and low-income groups or to strengthen the capacity and sustainability of a specific financial intermediary. Between 2005-2022, the ADB has approved 84 sovereign FIL (SOV-FIL) projects with a total commitment of \$11.4 billion, out of which 85.6 percent were financed from ordinary capital resources, 12.7 percent from concessional loans and 1.5 percent from other concessional sources. While SOV-FILs in 1970s-1980s were mostly for MSMEs, in recent decades projects have focused on PPP infrastructure projects, MSMEs and clean energy investments. They are also increasingly being used to create platforms and facilities for the mobilization of climate blended finance, as in the case of two recent FILs in China and Indonesia illustrated in this paper.

FILs serve blending purposes well because they allow financial intermediaries to obtain capital at the favourable terms offered in sovereign lending. They also mesh well with technical assistance projects. In this sense they are well placed to support 'green bank' and other green financial intermediation models, supporting the strengthening and transformation of domestic DFI (Volz and Lee 2024). However, it should be noted that FILs are not explicitly designed to cater to the needs of NDBs and do not necessarily prioritize working with public institutions.

In 2017, the ADB approved a FIL of EUR458 million (\$499.60 million) to the I&G, with the purpose of establishing a green financing platform (GFP) aimed at leveraging domestic financing for investment in green energy and pollution reduction. The facility was meant to contribute to diversifying the Chinese green bond market, one of the largest in the world, towards the provision of a wider range of longer-term instruments. It also intended to support projects for emission reduction of SMEs and energy service companies (ESCOs). The projects targeted the greater Beijing-Tianjin-Hebei (BTH) region, one of the most polluted in the country. In 2021, a \$150 million additional loan was approved to scale up the facility (ADB 2020). The two projects were part of a broader multi-year program agreed in 2015 by the ADB with the Chinese government to tackle air pollution in the BTH region and involving six loans for a total \$2 billion commitment (including a policy-based loan).

The project's financial intermediary partner, I&G, is the first national professional guarantee institution in China, with a long-term credit rating of AAA. Initially set up as a State-Owned Enterprise (SOE), it is now a Sino-foreign joint venture, whose largest shareholder is China's State Development & Investment Corporation (SDIC). Its core business includes guarantees and credit enhancements, asset management and fintech.

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Project Description

The ADB FIL had a 15-year term, including a grace period of 10 years, an annuity repayment at the 10 percent discount rate and an annual interest rate determined in accordance with ADB's LIBOR. The loan proceeds were onlent in Euro from the Ministry of Finance to I&G through SDIC on identical terms as the ADB loan. SDIC and I&G bore the foreign exchange risk. A reflow fund was created for reusing loan repayments for new sub-loans. The loans were extended in Euro – the currency was preferred by the borrower because it was cheaper than RMB/CNY at the time of the agreement. I&G hired a foreign exchange expert to help with hedging the risk coming from the loan.

The GFP was envisaged to provide a set of complementary financial products:

- i. credit guarantees to SMEs and ESCOs to enable commercial financing from banks, including a credit enhancement scheme designed to improve the creditworthiness of domestic developers to issue clean air bonds;
- ii. debt financing through entrusted loans managed by commercial banks;
- iii. financial leasing for purchasing energy-efficient industrial equipment and other goods to reduce the substantial capital needs of SMEs and ESCOs; and
- iv. A fintech online lending platform enabling simplified loan application, customer-specific risk-based loan pricing, and credit risk monitoring and management for SMEs.

Outcomes

At project completion in 2022, the ADB had provided €458 million, co-financing banks had provided €1,061 million, sub-borrowers had provided €362 million and I&G had provided €32 million. About €71 million of the reflow fund was utilized to finance seven sub-projects. Overall, 20 sub-loans covering 52 subprojects had been approved by I&G and financed, in the areas of energy efficiency, renewable energy and green transport. More than 15 subprojects were implemented by SMEs, six by ESCOs and 23 by financial leasing companies (ADB 2024).

The GFP project was assessed as highly successful, having overachieved its intended objectives of contributing to increase investment in pollution reduction in the greater BTH region, leading to improved air quality and reduced CO₂ emissions. Investment in pollution reduction reached CNY 250 billion in 2022, far exceeding the outcome-level indicator of doubling the 2015 baseline level of CNY15 billion. All indicators of air quality and CO₂ emissions improved above the intended targets.

Challenges and Factors of Success

The GFP Project's success earned it the ADB's Award of the Best Performing Project in 2018 and in 2019 it was selected as the Best Practice of Nature-Based Solutions in 2019 UN Climate Action Summit. A critical aspect of its success was being embedded in a comprehensive multi-year program encompassing different lending modalities aimed at strengthening policies and regulatory frameworks in close alignment with government's priorities. Another factor of success was the provision of an additional \$1 million Technical Assistance grant which was used to facilitate the establishment of the online platform for subproject application and management, through the organization of workshops and training programs with all the intended stakeholders, including I&G staff, SMEs and commercial banks. To facilitate implementation, I&G established a dedicated project management office with more than 30 technical staff. The ADB's own assessment of the project underscored the importance of strong government commitment to improve air quality is essential, of

an executing agency with strong technical and management capacities, and of flexible project design to accommodate evolving government policies and regulations.

More broadly, the project demonstrated FIL's usefulness in overcoming the problem of project size, allowing for aggregating diverse projects and stakeholders across many sectors. It allowed for the provision of a package of instruments, including guarantees, designed to meet the specific needs of SMEs, which in turn was critical to enabling the achievement a substantial number of sub-projects implemented. However, in absence of more detailed information on the nature of the beneficiaries, it is difficult to assess the overall additionality of the project. It is critical that FILs are used where the concessionality that they bring is truly needed and has potential for additional leveraging.

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CASE STUDY 4:

THE INTER-AMERICAN DEVELOPMENT BANK (IDB) TECHNICAL COOPERATION AND KNOWLEDGE AGENDA WITH NDBS ON GREEN FINANCE AND CLIMATE RISK

Background

The IDB has a long-standing relationship of more than 40 years with NDBs in the region. Together with the Latin American Association of Development Financing Institutions (ALIDE), since the early 2000s it has significantly contributed to strengthening the network of Latin American public development banks, improved their financial sustainability, and grown their technical and financial intermediation capacity to reach more, underserved beneficiaries and markets (De Olloqui et al. 2013).

A key driver of this process has been the recognition of the unique role that NDBs can play in catalyzing and scaling up private sector financing for climate change mitigation projects through the leveraging of international and national climate finance. Between 2008 and 2018, the IDB's total green finance lending to NDBs was \$2.1 billion, including technical assistance for 59 green projects and loan operations with 39 NDB partners (Netto et al. 2021). The projects addressed challenges to green finance, including the lack of capacity for private and public stakeholders, lack of medium- to long-term financial resources and adequate financial instruments, lack of contingent financial tools for disasters, lack of environmental and social risk management systems, and lack of capacity and methodologies to monitor results (Netto et al. 2021).

One comprehensive technical assistance program has been particularly impactful, leading to increased institutional capacity and contributing to catalyse green investment across the Latin American region: the *Green Finance Program to Mobilize Private Investment in Mitigation Actions and Low-carbon and Sustainable Business Models through National Development Banks* (Phase I and II).

Project Description

The first phase of the *Green Finance Program to Mobilize Private Investment in Mitigation Actions and Low-carbon and Sustainable Business Models through National Development Banks* was implemented in 2016 with the support of the International Climate Initiative (IKI) of the German Ministry for the Environment, which contributed \$5 million out of the total \$6.6 million project cost activities (IDB 2016). A second phase was approved in 2020 with a budget of \$4 million, also funded by the IKI through the IDB (IDB 2020).

The first phase of the program (also called *Leveraging Green Investments Program*, LGI) focused on creating capacities for scaling up innovative public-private green financial instruments in Brazil, Colombia, Paraguay and Mexico, relying on three sets of actions (IDB 2017):

1. Tailored support for NDBs to design and promote green financial instruments to mobilize private sector investments in EE and RE and other green investments.¹⁸
2. Financial Innovation Labs to promote dialogue among NDBs and regulators, capital markets and financial sector stakeholders on innovative green and sustainable financial instruments.
3. Scaling up the LAC Green Bonds Market.

¹⁸ NDBs supported included: In Brasil: Banco do Brasil, BDMG, BRDE, Desenvolve São Paulo, and Fomento, Parana. In Colombia: Finagro. In Mexico: BANCOMEXT, BANOBRAS, FIFOMI, FIRA, NAFIN, Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero (FND) and, Sociedad Hipotecaria Federal. In Paraguay: Agencia Financiera de Desarrollo (AFD).

The second phase builds on the successes of the first to further promote financing strategies aimed at mobilizing private sector investments in EE and RE, focusing on beneficiaries in Brazil, Colombia, Mexico, Paraguay, Uruguay and Chile. It expands capacity building activities to public entities beyond NDBs, such as utilities and other public companies; it brings the experience of the Financial Innovations Lab to Chile, Colombia, Paraguay and Uruguay; it supports regional regulatory dialogue and the implementation of the Green Bond Transparency Platform.

Outcomes

Since 2016, the two phases of the Green Finance Program managed to support 17 PDBs and 8 government institutions (including central banks, pension fund regulators and sovereigns), enabling collaboration in all the five areas identified in section 2 and mobilizing over \$2 billion in sustainable investments in Brazil, Chile, Colombia, Mexico, Paraguay and Uruguay (IDB 2024b).

Access to finance for national DFIs was supported through assistance in the design of funding applications for the GCF and in the issuance of green and sustainable bonds. For example, the LGI supported the Development Financial Agency of Paraguay (AFD Paraguay) in the design of a \$40 million energy efficiency credit line for SMEs co-funded by the IDB and the GCF. It also assisted FIRA in the design and issuance of the first green bond for protected agriculture of the country (IDB 2020 and 2024b).

Initiatives aimed at lowering the cost of capital and improving climate risk management include the establishment of public-private platforms (e.g. Financial Innovation LAB in Brazil) for the design of innovative green financial instruments and the blending of public and private investments, and technical assistance for the development of Social and Environmental Risk Management System. For example, the IDB supported the National Bank of Foreign Trade (Bancomext) in Mexico, to develop a credit product that promotes the energy efficiency of the hotel industry. In Chile, the IDB launched a series of Sustainable Roundtables among regulators and financial market players to identify a road map to integrate climate change risks in financial practices and regulations and assisted in the incorporation of sustainability criteria into pension fund investments (ibid). Public-private platforms were also set up to facilitate the identification of viable projects, like in the case of the LATAM Projects Hub, to bring together the most relevant infrastructure and energy opportunities in the region open to private investment (LATAM Projects Hub n.d.).

Finally, the program actively promoted knowledge and information sharing of lessons learned and best practices among PDBs and other stakeholders, for instance through the creation of dedicated platforms such as the *Green Finance for Latin America and the Caribbean (GFL)*.

Challenges and Factors of Success

The IDB is one of the few MDBs with a comprehensive and explicit strategy aimed at engaging with and empowering national development banks. It explicitly promotes institutional transformation, in view of enabling the independent access to climate resources and capital markets funds.

The *Green Finance Program* is exemplary of this approach. It also shows how far a comprehensive approach to technical assistance and capacity building can go when designed to serve a broad strategic objective and accompanied by a range of financing mechanisms. It significantly improved the IDB's knowledge of the constraints faced by NDBs in engaging with green finance and investment in the energy transition (Abramskiehn et al. 2017). It galvanized interest in green finance in the Latin American region, spurring new projects, attracting co-financing and mobilizing new resources.

However, a critical perspective and more research are needed to assess IDB's contribution to develop PPPs that can offer an alternative to traditional blending approaches and ensure additionality. The focus of the programs reviewed in this case study are in fact de-risking and financial market engagement more than institutional strengthening for its own sake.

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CASE STUDY 5:

NEW DEVELOPMENT BANK AND BNDES

Background

The New Development Bank was established in 2015 by Brazil, Russia, India, China and South Africa (the BRICS) to mobilize resources for infrastructure and sustainable development projects in member countries. A defining characteristic of New Development Bank lending programs is the abandonment of policy conditionality and the centrality of country client's needs in shaping the strategy approach. This largely originates from the member countries' state-centric approach to development, and is reflected in the adoption in 2015 by the New Development Bank of a policy on partnerships with NDBs (NDB 2015).

In September 2015, BNDES the first national development bank to sign a memorandum of understanding for a cooperation framework with the New Development Bank. Currently BNDES is a diversified financial institution, providing loans directly (Tier 1) or indirectly through on-lending to commercial banks and equity investment (Tier 2). Over the years, its role and impact has shifted with changing government policy priorities, but acquiring a particularly important role under the administrations led by the Workers Party (Campello 2024).

Since the late 1980s, its main sources of funding have been quasi-public funds provided by worker's insurance funds, returns of outstanding loans, equity investments, bond issuance and international loans (including loans from multilateral institutions and international bonds). In 2024, international lending represented 3.5 percent of BNDES capital structure, for a total of BRL 24.4 billion (approximately \$2.5 billion) (BNDES 2025).

Between 2009 and 2014, the National Treasury provided long-term, low-cost loans for BNDES totaling \$197 billion in view of strengthening its counter-cyclical role in the face of the global financial crisis (Ferraz et al. 2022). This enabled BNDES to lend at very competitive rates, widening the scope of its operations, including to more mission-oriented innovation investments (Mazzucato and Penna 2015), and to spearhead investment in domestic renewable energy, particularly in the local wind industry. BNDES was active in financing, at varying level, 80 percent of the 15.5 GW wind energy projects implemented between 2006-2019 (Ferraz et al. 2022).

In 2009, the Brazilian government established a national climate fund, Fundo Clima, as the financing arm of its national climate change policy. Fundo Clima operates through two windows: a non-reimbursable grant based one, operated by the Ministry of the Environment, and a reimbursable loan window, managed by BNDES. Fundo Clima is mainly financed by government resources, including revenues generated from a tax on oil companies. However, from 2014 onwards, government transfers to BNDES to operate the non-reimbursable window dried up (Bhandary 2022). This interruption coincided with a reverse in the economic cycle and an aggravation of the political climate (with the impeachment of President Dilma Rousseff in 2016 and the election of Jair Bolsonaro in 2018), and it was accompanied by a phase out of the implicit subsidies to BNDES lending rates. As a result, in 2019 BNDES disbursed \$13.9 billion, compared to \$88.2 billion six years before (Ferraz et al. 2022).

With the election of President Lula to lead his third administration in 2022, BNDES has reestablished a central role in driving the country's green transition, including through Fundo Clima. In April 2024, BNDES and the Ministry of Environment signed a contract for the allocation of BRL 10.4 billion (about \$2 billion) for the lending window of Fundo Clima, of which about BRL 10 billion raised

on the sustainable sovereign bonds on the international market and R\$400 million from special participation arising from oil and gas exploration (BNDES 2024).

Project Description

Since 2015, the New Development Bank has extended three loans to BNDES – all denominated in dollars:

1. Financing Renewable Energy Projects and Associated Transmission (\$300 million non-sovereign loan, approved in 2016), focused on renewable energy projects and the development of a secondary market for infrastructure bonds (NDB 2016).
2. BNDES Clima – Sustainable Financing to Support Global Climate Change Mitigation and Adaptation (\$500 million sovereign loan) for on-lending to public and private sector (NDB 2021).
3. Sustainable Infrastructure Project (\$1.2 billion sovereign loan) to support BNDES on-lending to public and private infrastructure projects in the following sectors: renewable energy and energy efficiency, urban mobility, water and sanitation, transport and logistics, ICT and social infrastructure (NDB 2020a).

The Financing Renewable Energy Project, completed in 2020, managed to mobilize co-financing of around \$845 million (including over \$339 million from BNDES, \$399 million from shareholders' equity and \$107 million in bonds issuances) bringing the total investments to around \$1.145 billion. The main project activities were the construction of infrastructure for generating renewable energy, with three major sub-projects implemented across the States of Bahia (wind), Minas Gerais (solar), Pernambuco (wind) and Piauí (wind). Each power plant complex comprised several farms, an individual legal entity and received a separate sub-loan from BNDES, totaling 29 sub-loans. The sub-projects were implemented by Special Purpose Vehicles (SPVs) (IEO-NDB 2023).

The two most recent loans (BNDES Clima and the Sustainable Infrastructure Project) were approved by the New Development Bank, respectively, in 2019 and in 2020 but were fully authorized by Brazilian authorities and turned into contracts only in 2023 (NDB 2020b). In particular, the \$500 million loan was originally intended to support the government's implementation of Fundo Clima. However, following the withdrawal of support to Fundo Clima by the Bolsonaro administration, in 2021 the loan was restructured as a sovereign loan to BNDES.

All three loans were set up so that part of the resources could be deployed by BNDES for investing in debentures, a local debt capital market instruments similar to bonds, usually used to fund infrastructure projects (WEF 2019). BNDES can act as an anchor investor for primary issuances of debentures. In the context of the New Development Bank's loans, investment in debentures aimed at developing an alternative financing source for renewable energy projects and facilitate further development of secondary market for infrastructure financial instruments.

Outcomes

Of the three projects, a final evaluation is available for the Renewable Energy Projects and Associated Transmission, which in fact was the first project in Brazil evaluated by the Independent Evaluation Office (IEO) of the New Development Bank in 2022-2023. The evaluation found that the project contributed to enhancing Brazil's renewable energy capacity overall (additional 835MW annually) and to reduce the country's carbon dioxide emissions by 1.58 million tons annually. It also estimated that the projects generated about 7,500 new jobs, but highlighted that socio-economic, developmental and community-level impact were not clearly pursued as part of the project design. The project also supported the growth of the secondary market for debentures of renewable energy

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projects and helped promote the development of the capital market for infrastructure bonds (IEO-NDB 2023).

With regards to the two more recent New Development Bank climate loans to BNDES, they constitute more than half of BNDES' total foreign borrowing, with a combined total of \$1.7 billion. In this sense, they play an important role in mitigating the cost of capital for BNDES at a moment in which the bank is compelled to diversify its funding sources following changing in the domestic policy framework that used to ensure easy access to cheap capital. The two loans' long-term tenor (24 years) helps to mitigate the additional cost for BNDES of having to swap the loan from dollar to reais and bear the hedging. As of 2024, the New Development Bank had no lending in Brazilian real.¹⁹

Challenges and Factors of Success

Since the signing of the cooperation agreement in 2015, the relationship between the New Development Bank and BNDES has evolved to reflect the shifting context of Brazil's political economy. Relations were more distant during the Bolsonaro administration, when climate action was anything but a priority, and project approval was delayed. A contributing factor has also been the infancy of the New Development Bank, which at the start of the relationship with BNDES still had limited country-focused staff capacities and resources.

This process is well illustrated by the New Development Bank IEO's assessment of the Renewable Energy Projects and Associated Transmission loan (IEO-NDB 2023). In its analysis, the IEO attributes most of the merit of the project's success to the experience and track record of the BNDES in the sector. It found that the New Development Bank had limited involvement in the project besides financing, and while there was strong collaboration with BNDES, engagement with Federal and State Level authorities was limited, as well as with other international development partners. It also pointed to the lack of a dedicated country strategy to guide the New Development Bank-Brazil partnership as a factor constraining synergies across all New Development Bank's activities in the country. Recommendations included further strengthening the relationship with BNDES and other Brazilian Subnational Development Banks, as well as with government institution at federal and state level and enhance global south cooperation at large.

In the meantime, the two institutions have undergone a process of reciprocal learning, and relationships have picked up under the new, more climate and state-oriented administration of the Lula government. In this new context, the partnership with the New Development Bank could play a key role in helping BNDES address its compelling need to diversify its sources of funding in the face of a higher cost of domestic capital, and to maintain access to some concessional borrowing to be blended towards green investment.

Summary of Findings From Case Studies

This paper examined examples of collaboration with NDBs for five MDBs: the IsDB, EIB, ADB, the New Development Bank and the IDB.

All MDBs examined were active in all five dimensions of MDBs-NDBs collaboration discussed in section 2. However, the modalities and the complexity of the collaboration showed important variations (see Table 5), with partnerships including:

- a 1st tier loan for renewable infrastructure projects in the case of the IsDB;

¹⁹ At 2024, the New Development Bank had loans in Indian Rupee, Chinese Renminbi, South African Rand, Swiss Franc, Euro, Dollar (NDB 2024).

- a flexible credit line for co-financing with the Green Climate Fund of financing facilities for renewable energy (EIB);
- a 2nd tier FILs for the set up of green finance platforms (ADB);
- a comprehensive regional capacity building programmes with capital mobilisation impact (IDB); and
- one non-sovereign and two sovereign loans for 1st and 2nd tier on lending to public and private entities in renewable energy and infrastructure projects (BNDES).

The diversity of approaches results from differences across MDBs, across their partner NDBs and across countries' domestic economies and financial markets.

MDB-NDB relationships are embedded in local political economy and are influenced by governments' ideology and approaches to economic policy. Shifting political and national policy priorities can both create the conditions or pose challenges for the viability of long-term partnerships. As an illustration, during the administration of President Jair Bolsonaro in Brazil, which shunned climate commitments, the New Development Bank's climate loans to BNDES were delayed and deprioritized by the government. However, the independence of BNDES guaranteed that the bank could continue to develop the relationship with the New Development Bank including investing in renewable energy. With the new government led by President Lula, BNDES has reestablished a central role in driving the country's green transition, and the partnership with the New Development Bank has been scaled up again.

Building long-standing relationships can generate trust and enable more flexible approaches. The EIB loans to DBSA in support of two programs co-funded by the GCF (EGIP and CFF) demonstrate the usefulness of flexible approaches which provide concessional finance and let the national partner decide how best to deploy the funds. In the case examined, such an approach was enabled by to the long-standing relationship between the EIB and DBSA. This approach is particularly appropriate in the case of development banks and financing institutions with local expertise accompanied by strong technical skills and balance sheets. **Expansion of synergies between MDBs, NDBs and climate funds is hampered by the complex accreditation processes that the latter entail, and the lack of uniform standards and regulations to access their resources.** For example, this challenge delayed the deployment of funding from the GCF for the DBSA's Climate Finance Facility and the overall project implementation.

Key Findings from the Case Studies

- 1. The favorable terms at which NDBs obtain financing from MDBs are critical to making capital affordable for the intended beneficiaries and helping hedge risk (especially currency risk) that NDBs can't manage on their own.** All MDBs loans examined contributed to expanding the borrower's access to finance and lower the cost of capital offered to the final beneficiaries. For instance, the EIB's credit line to DBSA, along with co-financing from the GCF, contributed to improving the concessionality of the sub-loans provided under the CFF and the EGIP, two DBSA programs. Loans from the NDB are helping BNDES address a compelling need to diversify its sources of funding in the face of a higher cost of domestic capital, and to maintain access to some concessional borrowing to be blended for green investment
- 2. Most MDBs don't have specific policies or strategic frameworks for engaging with NDBs.** In the sample of MDBs discussed in this report, only the IDB and the New Development Bank did. MDBs also don't track and report their NDBs financing as a separate category. NDBs are usually but not necessarily treated as eligible for sovereign guaranteed loans. The lack of a standardized approach by MDBs in engaging with NDBs and national DFIs is largely due to the diversity of these institutions and the national legal frameworks that

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regulate them. However, the lack of explicit policies also denotes that NDBs/DFIs are not yet sufficiently recognized as a distinct category of partners that can play a pivotal role in mobilizing capital for climate and development goals, managing climate risk and realizing investment in sustainable infrastructure.

3. **Projects which are embedded in comprehensive programs, clearly aligned with government's priorities and backed by an enabling policy environment are more predisposed to innovation and success.** The success of ADB's FIL to I&G sponsoring the creation of a GFP for air quality improvement in China was facilitated by the fact that it was embedded in a comprehensive multi-year program encompassing different lending modalities aimed at strengthening policies and regulatory frameworks in close alignment with government's priorities. These favorable conditions can stimulate PDBs' appetite for experimenting. The presence in Türkiye of a favorable national policy for RE, including the adoption of a FiT at a pre-determined price anchored to the US dollar, encouraged the IsDB and its national partners TSKB and TKYB to experiment with a new financial instruments (*Restricted Mudaraba*) conceding greater intermediation power and independence to the borrowing banks.
4. **Local currency lending is still under-utilized and considered difficult.** In none of the case studies examined were loans extended in local currency, with the exception of EIB's credit line to DBSA, in which the option was given to draw funds in ZAR. This was made possible by the fact that the EIB issues bond in South Africa's currency. In all cases examined, the burden of foreign exchange risk hedging fell on the borrowing NDBs, adding to the cost of the loan. A commonly mentioned constraint on MDB's sovereign lending in local currency is that this would struggle to be competitive with the cost of capital that a sovereign institution would face on its domestic bond market. As seen in the case of DBSA's CFF and EGIP, the GCF's inability to lend in ZAR created significant hurdles to the project's roll out. Even when MDBs do lend in local currency, as in the case of ADB's loan in tenge to the Damu Entrepreneurship Development Fund in Kazakhstan (Box 5), the willingness to hedge currency risk wanes in the face of currency devaluation. In the case of the IsDB's loans to TKYB and TSKB in US dollars, the sub-borrowers were protected by the currency risk because they were able to generate foreign currency themselves. However, this is not always the case for the intended beneficiaries of investment in renewable energy and other green projects, which are often SMEs that cater to local energy markets.
5. **Technical assistance significantly increases the chances of success of a project, and capacity building at scale can contribute to nurturing a "coherent global ecosystem of public-public financing," while also having a significant financial leveraging impact.** The IDB's technical assistance programs were part of a deliberate bank-wide strategy of nurturing the role of Latin American NDBs in green finance. They were successful in raising awareness on green finance and climate risk, creating demand for partnerships, mobilizing new funding and promoting the development of the sector at the regional level. Lessons from the program and related initiatives have significantly contributed to expanding the IDB knowledge agenda on climate change and green finance. Technical assistance was also a key factor of success in the IsDB project loans and in the ADB FIL to I&G in China.

Appetite for (climate) risk can be generated with the help of technical assistance. The cases examined in this study demonstrate that climate risk appetite can be built with targeted technical assistance (as IDB did in Latin America) and through the careful structuring of financial intermediation platforms that combine different credit enhancement products (as in the case of ADB's SOV-FILs in China and Indonesia – Box 4). However, the imperative of more innovative green finance should be measured against the potential risks of

financial engineering and securitization of climate risk. Adopting complex, layered financial instruments can lead to transferring too much risk to the public sector while losing sight of and impact on the intended development and climate goals. This is particularly a risk in financing the energy transition, given the upfront costs and uncertainty surrounding future revenue streams (Christophers 2024) and climate adaptation, which often requires a focus on SMEs and locally embedded sectors, where the closeness to the needs and specificities of local communities is critical for project success.

- 6. Partnerships between MDBs and NDBs are characterized by a strong reliance on different types of derisking instruments, mostly without the means to assess their additionality and ensure accountability of the private sector involved.** Derisking instruments were adopted in all case studies, with different levels of complexity. The EIB, ADB and New Development Bank's loans were used by the respective borrowing NDBs to provide different kinds of credit enhancements through local financial intermediaries, such as the provision of subordinated debt for SMEs financing in South Africa (DBSA) and credit enhancement for issuance of green bonds in China (I&G) and for infrastructure bonds in Brazil (BNDES). The IDB has made a strategic use of technical assistance to empower NDBs to use green derisking instruments. Where public project assessment reports exist (i.e. ADB-I&G, NDB-BNDES, IsDB-TSKB and TKYB), they find that the projects successfully mobilized co-financing and private finance. However, with the information available it is difficult to assess whether the investments would have happened also in the absence of public finance absorbing their risk.

In only one case of those examined, measures to hold the private sector accountable to their share of the investment risk were explicitly mentioned. The IsDB's loans to TSKB and TKYB were facilitated by the introduction of legislation favorable to RE investments in Türkiye. This consisted in the adoption by the government of a FiT anchored to USD which protected private investors from the investment and foreign exchange risk. However, its implementation within the project was dependent upon investors meeting a pre-determined project completion date. On the downside, while the legislation ensured the profitability of RE investment, it also created additional fiscal expenditures and exposed end-users to price fluctuations linked to fluctuations in USD exchange rate.

In view of improving their capacity to engage as leaders in climate finance and green investment, and to do so in partnerships with MDBs, NDBs need to develop holistic green finance strategies clearly aligned with the Paris Agreement and with national NDC objectives, clear diagnostic tools and innovative financial instruments to implement such systemic transformational changes, affecting all the sectors they work in (e.g., infrastructure, industry, commercial, agriculture and land-use). Overall, the case studies analyzed here show that while these MDBs and NDBs have acquired experience working together, more needs to be done to ensure that MDB – NDB partnerships evolve towards providing an alternative approach to blending and constituting a global system of public finance.

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Since the COVID-19 pandemic, increased attention has been given to DFIs, and PDBs in particular, as key actors in mobilizing capital for climate and development goals, managing climate risk and realizing investment in sustainable infrastructure. MDBs have responded to the challenge by initiating a broad reform agenda aimed at strengthening their financing capacity, enhancing their collective impact and strengthening links to private finance. Much of this discussion has been framed around the use of public private partnerships and the use of blended approaches through derisking instruments. To date, this approach has yet to deliver on its promises and expectations.

Blending from the ground up means establishing partnerships with other public finance institutions that are clearly aligned with government's development priorities and NDC plans and that focus on transformational projects which would not be realized in the absence of public support. This requires mobilizing private capital which is risk-tolerant, patient, and willing to share risks and rewards of investments in a policy environment that is enabling but also regulated and accountable to citizens.

This paper has made the case for MDBs to deepen their collaboration with their sister public finance institutions: NDBs and related DFIs.

In particular, NDBs have the potential to be leading actors in leveraging green finance and investing in the energy transition because of their positioning at the intersection between international climate and development finance, local financial institutions and private investors, and have the potential to align development financing with mitigation actions. Given their development-focused mandates, NDBs are also well-positioned to help marshal resources behind national development plans and could play a coordinating function for finance from diverse sources by anchoring country platforms.

Building on their synergies, MDBs and NDBs can work together to overcome the limitations of existing de-risking instruments and to play a central role in linking political ambition with policy action. They can play a strategic role in supporting coordination between various actors in the financial sector, combine their concessional resources and structure innovative financial instruments and solutions, so that these are more clearly grounded in country priorities and country ownership, while ensuring accountability and additionality of the public funds used.

This paper reviewed five key potential areas where collaboration between MDBs and NDBs can be mutually beneficial, and the main instruments available to put them into action: improving access to capital and widening access to different financing sources (e.g through on-lending and equity injections), lowering the cost of capital and sharing and managing risk (through guarantees, credit enhancement instruments and green financing platforms), and project identification and capacity building. The paper also discussed the main constraints faced by NDBs in expanding their collaboration with MDBs and in their engagement in green finance.

As demonstrated by the examples presented throughout the paper and the case studies illustrated in Section 3, some MDBs have already started to develop a practice of cooperation with NDBs, especially on green finance and energy transition, with promising areas for development and scaling up.

However, the analysis also underscored that they have yet to form a “coherent global ecosystem of public-public financing” for development and climate (Marois et al. 2023). With a few exceptions (notably the IDB and the New Development Bank), MDBs don't have strategies or policy frameworks for engaging with NDBs and lack global reporting standards to track their financing to these institutions. They are also yet to develop a practice of *public-public blending* that truly focuses on country ownership, additionality of the capital leveraged and accountability of the public funds used.

The examples and case studies discussed showed that NDBs are largely seen as actors which can help with the roll out of increasingly sophisticated derisking instruments aimed at mobilizing private capital. However, the value of working with NDBs does not lie in empowering them to channel more public resources to the socialization of private risk and guaranteeing private profit. Instead, their value added lies in being better placed to attract sources of risk-tolerant and patient capital (especially domestic sources), and to identify investment opportunities that are in alignment with government priorities, in recognition of their public mandate. To enable this type of partnerships, governments should provide an enabling policy environment where carrots operate as well as sticks (Gabor and Sylla 2023a; Gabor and Sylla 2023b) in the form of regulations and conditionalities to the use of public funds (see also Independent Report of the G20 TF-CLIMA Group of Experts, 2024).

More efforts are also needed to devise solutions for foreign exchange risk management, which remains a major impediment to local currency lending and a drag on green investment. While some MDBs and DFIs have been deploying different types of measures to reduce the cost of local currency lending, these are still under-utilized and under-developed, in large part because they remain too expensive. The mechanisms most recently proposed and experimented with (see Annex 1), underscore that concessional capital (from MDBs, DFIs, donor governments, philanthropies) is necessary in the short term to develop mechanisms that improve the availability and affordability of local currency loans and currency risk management solutions. On their side, MDBs need to do more to expand local currency lending, both by devising instruments to scale up onshore local currency lending, as well experimenting and enhancing cheaper instruments for hedging currency risk, including through subsidization of such instruments, in collaboration with donors, DFIs and IFIs.

Finally, the scarcity of concessional finance and grants available is a major constraint to scaling up MDBs-NDBs collaboration. To address this, efforts to make MDBs bigger and strengthen their lending capacity through balance sheet maximization and shareholder recapitalization are critical.

MDBs have initiated an important path of reforms to become “bigger, better and more effective.” It is important that as part of this agenda they develop and nurture new and broader partnerships, starting with partnerships among MDBs and between MDBs and national public finance institutions and other related DFIs.

In view of overcoming the barriers to MDBs-NDBs collaboration highlighted in this report, and developing a public-public approach to blending, key policy recommendations for such an agenda are:

- 1. MDBs should institute policies that encourage partnerships with national development finance institutions.** Partnerships between MDBs and NDBs should be embedded with a strategic vision that values and prioritizes the public nature of MDBs and NDBs, both around the delivery of public goods, as well as wider development objectives. This vision should be broader than simply leveraging their combined resources to attract private finance and should be geared towards unlocking the complementarities and synergies between MDBs and NDBs.
- 2. NDBs could play the role of a financing anchor for country platforms by coordinating resources around country-owned plans.** NDBs are not only delivery vehicles but can also be key partners in proactively coordinating technical assistance, policy support to the host government and the design of a financing strategy that best reflects national priorities. The role of NDBs as anchors of country platforms should be reinforced by improved country-level coordination between MDBs as called for by the Group of 20 (G20) Roadmap on Strengthening MDBs.

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3. **Additional concessional funding is necessary to scale up green finance and renewable energy investment, including for the development of innovative currency risk hedging instruments and the provision of impactful technical assistance and capacity building.** In a context of high interest rates and currency devaluation, it is critical to put NDBs in the position to access capital at low cost, nationally and internationally, and to focus more explicitly on instruments designed to mobilize domestic savings.
4. **MDBs and DFIs need to experiment with more risk-taking, including through the development of new guarantee products, which are still under-utilized, and NDBs need to expand their potential sources of funding and use of new financial instruments.** Collaboration among donors, MDBs, IFIs and EMDE governments to implement and scale up currency risk mitigation solutions is urgent and paramount to reduce the delivered cost of capital and unlock private climate finance for EMDEs. MDBs could facilitate experimenting with different solutions by introducing more flexible risk assessments allowing engagement with a wider range of domestic financial institutions and providing technical assistance and capacity building for the development of local financial markets in EMDEs.
5. **MDBs and bilateral agencies should support portfolio guarantees to bolster the financing capacity of national development banks.**
6. **MDBs-NDBs partnerships would benefit from easier country access to international climate funds, including through easier accreditation processes and harmonization of regulatory regimes.**

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ANNEX 1: PROPOSALS FOR ADDRESSING CURRENCY RISK

Strategies currently available to MDBs and DFIs to mitigate the cost of local currency financing include:

1. Issuance of onshore local currency bonds, and onlending in local currencies for domestic projects so that there is no mismatch (Schclarek and Xu 2023). For instance, in 2019 the European Bank for Reconstruction and Development (EBRD) issued local currency bonds denominated or linked to nine currencies of countries where it invests for funding purposes (EBRD n.d.). While this is the most common method used by MDBs to source local currency liquidity, its use is still limited to a small group of upper-middle income countries.
2. Back-to-back funding, whereby DFIs borrow funds in the same currency, amount and tenor as they lend to their clients, or use hedging mechanisms such as swaps to achieve the same effect, so that operations in local currency are fully matched by corresponding liabilities or currency hedges. This mechanism allows for eliminating currency risk, but it has proven insufficient for scaling up local currency lending because of DFIs' inability to secure the necessary long-term funding in local currencies, due to the limited availability of funding and hedging instruments for the currencies of low- and middle-income countries (LMICs) (CPI 2024b).
3. The Currency Exchange Fund (TCX) is a specialized fund created in 2007 to provide (synthetic) local currency loans to DFIs and hedge the resulting currency risk where no commercial markets existed, by using its balance sheet to pool, diversify, and transform risk across maturities and volumes. TCX has a capitalization of approximately \$1.5 billion, supported by the European Commission, five governments and a range of MDBs and DFIs. It has an average annual return of 1.6 percent, and it has experienced significant growth in transaction volume, reaching \$2.5 billion in 2023 (CPI 2024b). However, its scale is still insufficient to support the full demand of local currency hedging, and the cost of its products is still too high to have an impact at scale (Hirschhofer and Kapoor 2023).

Additional approaches that could be considered include: i) borrowing in USD, and onlend to a well-diversified portfolio of loans in different local currencies to diversify risk, as done for instance by the EBRD (Bonizzi et al. 2024); ii) recapitalization of MDBs with USD that they exchange for local currencies to establish Local Currency Funds for local currency lending (Schclarek and Xu 2023).

Avinash Persaud has proposed the creation of an international platform to act as a joint agency of MDBs with IMF liquidity support to offer partial hedges for LMIC currencies at lower cost than the market without fully covering excess cost to facilitate sustainable scale up. Currency risk would be reduced through diversification by pooling MDB assets, while IMF support would provide the necessary dollar liquidity (Persaud 2023).

Other proposals, which are either at the stage of proposal or early implementation, include:

- TCX donor-funded guarantee facility, established to improve the affordability of its hedging products, through the subsidization of the price of hedges to below TCX's standard rates for priority countries and sectors, with a focus on climate projects (TCX et al. 2023).
- Eco Invest Brasil, a partnership between the IDB and the Brazilian Government, housed under its Fundo Clima. It aims at mitigating currency risk for climate projects that are able to increase their local-currency revenue in line with general inflation following a depreciation of the local currency and which are encouraged to use short-term currency hedges available from local financial institutions in Brazil.

- An onshore DFI hedging platform (called Delta) to expand onshore local currency lending by borrowing local currency on a short-term basis, on-lending this to DFIs on a long-term basis, and managing associated liquidity and interest rate risks.
- An MDB local currency transfer model, developed by Financial Sector Deepening Africa, which would test the potential for transferring MDB loan portfolios to local investors, freeing up MDB capital for new lending and potentially supporting local currency financing in targeted emerging economies
- An FX Hedging Facility in India, developed by CPI through the Global Innovation Lab for Climate Finance to manage currency risk for renewable energy projects in India.

