PRIVATE INVESTMENT MOBILIZATION MODELS (PIMMS) FACT SHEET:

Private Sector Blended Finance Debt Fund (PIMM10)

EXECUTIVE SUMMARY

PIMM10, along with PIMM9 and PIMM5, is designed to deliver the most important driver of private investment mobilization at scale – investment grade (BBB) ratings:

- PIMM5 will produce BBB-rated guarantors that provide BBB guarantees for loans/bonds at the project level.
- PIMM9 will aggregate public sector sovereign credit risk in a portfolio/fund, capitalized with three tiers of capital, with senior capital rated at investment grade (BBB).
- PIMM10 will aggregate private sector credit risk in a portfolio/fund, capitalized with three tiers of capital, with senior capital rated at investment grade (BBB).

Based on leverage assumptions below, $1 billion of catalytic and concessional (C&C) funding could mobilize $18 billion of private investment in senior capital (and more in mezzanine capital).

NOTE: Securitization is also a powerful mechanism to create investment-grade ratings. During consultations in March-June 2025, it will be determined whether to include securitization: (i) as a separate PIMM or (ii) as part of PIMM9 and PIMM10.

OBJECTIVES

Mobilize debt investors to invest in private sector debt in developing countries indirectly through funds. The use of the fund approach would reduce the expected loss for senior capital in the fund.

Rationale	PIMM10, by delivering scaled, investment-grade opportunities appropriate for global institutional investors, will mobilize a large universe of investors who will not/cannot invest in individual private sector borrowers/projects. PIMM10 is expected to use C&C funding more efficiently and mobilize significantly more private investment than guarantees. The perceived risk of private sector borrowers in developing countries is driven primarily by the sovereign risk ratings of the Big 3 rating agencies. For the 142 developing countries, the median sovereign rating is currently B- and 76% of countries are rated B or lower. Applying the sovereign ceiling convention, most private sector borrowers have implied ratings of CCC, B, and CC. As a result, most private sector borrowers fail to attract debt financing from the market.

Description	PIMM10 is a fund with three tiers of capital designed to ensure senior capital is rated at investment grade (BBB). Three primary drivers of risk improvement are: 1. Diversification of investment risk across many exposures (e.g., a fund may lend to 40+ borrowers in 10+ countries). Big 3 rating agencies' methodologies indicate diversification can result in a 2-notch upgrade from the underlying average risk rating of individual borrowers, (e.g., from CCC+ to B). This upgrade in many cases is not sufficient to mobilize at scale. 2. Presence of capital subordinated to the senior capital (e.g., junior and mezzanine capital which can deliver a 1-2 notch upgrade depending on the size of subordination[1]). Senior capital rated investment grade (BBB) is likely the optimal rating to mobilize private investment at scale using C&C funding efficiently and effectively. 3. Diversification of currency risk, with the fund expected to typically invest in 10+ countries. The most common expected application of C&C funding for PIMM10 is to capitalize on the junior tier of three-tiered blended finance funds. C&C funding will increase participation of institutional debt investors in fund structures, thereby increasing the supply of debt capital to private sector borrowers in developing countries.
Development rationale	The largest sources of the $428 trillion of global financial assets held by the private sector seeking long-term investment (e.g., pension companies and insurance companies in developed countries) typically: (i) invest more debt than equity and (ii) require investment grade risk. Since only 11% of developing countries are rated investment grade, investors are not able to achieve their preferred investment in developing countries. World Bank International Debt Statistics estimate that all private sector debt in developing countries (excluding China) owed externally is only $2 trillion (less than 1% of global financial assets), and only $271 billion is owed to bondholders. Corporates in developing countries are either: (i) unable to raise as much debt as they like, (ii) are required to pay prohibitive interest rates, and/or (iii) are required to borrow in foreign exchange (FX) debt, jeopardizing debt sustainability. • C&C funding in PIMM10 to increase the supply of mainstream debt financing, via fund structures, to private sector borrowers in developing countries, allows borrowing companies to make more capital investments for the Sustainable Development Goals and climate projects. • C&C funding in PIMM10 is expected to start mostly with FX debt, but once standardized, is expected to spawn a significant increase in local currency debt. C&C funding as junior capital in three-tiered private sector debt funds supports the development community's view that the perceived risk of investing in developing countries is higher than the actual risk. C&C funding as junior capital underwrites the delta between perceived and actual risk – if the risk (i.e., defaults and losses) unfolds at higher levels consistent with private investors' perceptions then the C&C funding as junior capital will be depleted. If defaults and losses unfold closer to the development community's view, then the fund will likely collect interest payments at a level sufficient to cover actual losses, thereby preserving C&C funding. The development community's stance is supported by: • Data from the Global Emerging Markets Risk (GEMs) Database on defaults on multilateral development banks (MDBs)' private sector loans and recovery rates given default. • The consistent profitability of the International Finance Corporation (IFC), which primarily provides market-priced loans to medium-risk private sector companies in developing countries. IFC's median risk rating for its loans is BB-.

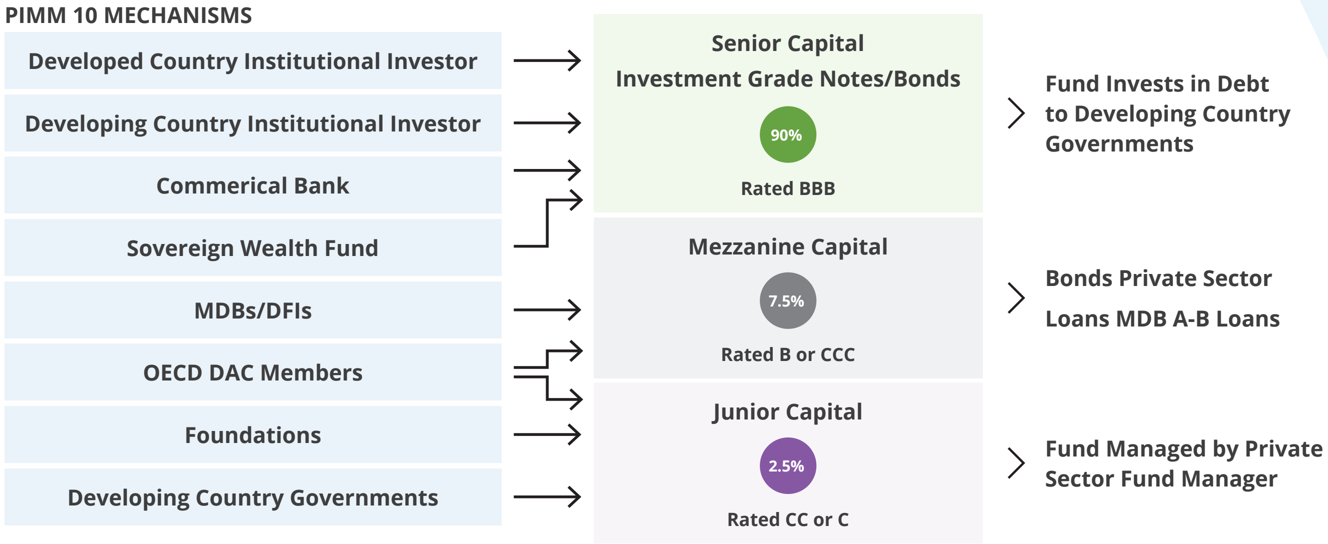
1 Accordingly, senior capital in the fund structure could have implied ratings ranging from speculative non-investment grade (e.g., BB), to low investment grade (BBB), to strong investment grade (AA). Likely targeting BBB is the most effective and efficient use of C&C funding to mobilize at scale.

Existing comparable precedents of C&C funding	Convergence has recorded 122 tiered blended finance funds in its Historical Deals Database that invest debt in private sector borrowers. PIMM10 consolidates the lessons learned from those 122 private sector debt funds. Good benchmarks are the IFC-Swedish International Development Cooperation Agency Managed Co-Lending Portfolio Infrastructure Program, the Dutch Development Bank-Allianz SDG Loan Fund, BlueOrchard funds, Finance in Motion funds, Symbiotics funds, and funds capitalized with junior capital by KfW Development Bank and BMZ.
Indicative activities for Network of C&C Funders	The Network of C&C funders could establish a sub-group of organizations interested in awarding funding that mobilizes private debt investment through PIMM10. Indicatively, the Network could consider four approaches: 1. Collaborate with MDBs and bilateral development finance institutions (DFIs): Network members and MDBs and bilateral DFIs lending to the private sector could collaborate to establish three-tiered blended finance debt funds where MDBs and DFIs would arrange A-B loans and the fund would invest in the B-loans. MDBs and bilateral DFIs currently arrange $30-40 billion in private sector loans annually. MDBs and DFIs could increase the volume of loans arranged to $160 billion A-B loans, retain $40 billion A-loans, and distribute $120 billion B-loans to PIMM10 fund(s). 2. Collaborate with national development banks (NDBs): Network members and NDBs could collaborate similar to MDBs and bilateral DFIs above. 3. Collaborate with export credit agencies: Network members and Organisation for Economic Co-operation and Development Group of export credit agencies could collaborate similar to MDBs and bilateral DFIs above. 4. Call for proposals: where the Network invites private sector fund managers to propose how they could deploy C&C funding as junior capital in a three-tiered fund that mobilizes private investment into a senior tier. Illustrative proposals could be: (i) a fund that invests debt in loans and bonds for nationally determined contributions and Just Energy Transtion Partnerships (JETPs) projects and issues green bonds as senior capital; (ii) a fund that invests in climate adaptation loans and bonds and issues green bonds as senior capital; and (iii) a fund that invests in education loans and issues impact bonds as senior capital. In competitive global calls for proposals, the Network could receive hundreds of proposals annually, facilitating the awarding of C&C funding on a quasi-auction basis.
Expected C&C funding instrument(s)	**The majority of C&C funding is expected in the form of debt or equity as junior capital in three-tier funds.** Historically, most C&C funding from OECD Development Assistance Committee (DAC) members as junior capital has been grants. But given the 2023 change in official development assistance rules for private sector instruments (PSIs), and the Fourth International Conference on Financing for Development Zero Draft about public and private sectors "sharing risks fairly," it is fairer with better value for money to deploy C&C funding as loans or equity (e.g., a PSI).
Expected financial profile of C&C funding (including risk profile)	C&C funding deployed in PIMM10 is expected to take on a risk profile beyond the willingness or ability of MDBs and DFIs; the rating of junior capital is expected typically to be CC or C. Financial expectations of C&C funding in PIMM10 are likely: • Break-even: Likely most uses of C&C funding would earn break-even or small positive financial outcomes. • Partial losses: Likely some uses of C&C funding would be deployed at partial losses. Full losses are unexpected.

Expected sources of private investment mobilized	1. Debt fund managers (e.g., PIMCO and Amundi). 2. Developed country banks, institutional investors (e.g., pension companies and life insurance companies), money market funds, and investment funds in senior capital of fund(s). 3. Developing country institutional investors (e.g., pension companies and insurance companies). 4. Sovereign wealth funds.
Expected leverage	Based on precedent from private sector debt funds, and the GEMs Risk Database defaults and losses for sovereign loans, a reasonable expectation of a typical three-tiered capital structure could be 90% senior capital from private investors, 7.5% mezzanine capital from MDBs, and 2.5% junior capital for C&C funders. Actual amounts in each tier will be driven by the objectives: (i) to achieve an investment grade BBB rating for senior capital from a major rating agency and (ii) to achieve a rating for mezzanine capital that will meet MDBs' investment mandates as governed by shareholders (e.g., CCC). Convergence estimates a reasonable leverage expectation of C&C funding for PIMM9 could be 36 times. This will require MDBs to be governed to invest in mezzanine capital. If $200 billion of investment by PIMM10 funds is targeted annually, this would require around $5 billion of C&C funding annually. Assuming a 3% interest rate saving for sovereign borrowers (compared to capital markets interest rates), this would yield $6 billion of interest rate savings in the first year.
A single-country or multi-country application	Both. PIMM10 is expected to be deployed mostly for multiple countries but also for a single country: • Multi-country funds are expected to mobilize primarily institutional investors located in developed countries, with C&C funding provided primarily by OECD DAC members, OECD DAC participants, and philanthropic foundations. • Single country funds are expected to have domestic government funding as C&C funding to mobilize primarily domestic institutional investors (e.g., pension companies) and secondarily developed country investors.
Recommended standardization for this PIMM	Based on extensive benchmarks for PIMM10, Convergence recommends five types of standardization for C&C funding for PIMM10: 1. Restrict to three-tiered blended finance funds – three tiers will produce maximum leverage/efficiency of C&C funding in the third tier while generating investment grade (BBB) assets for private investors. 2. Require external ratings at investment grade (BBB) for senior capital (as PIMM10 is standardized, investors might become prepared to invest in senior capital with BB ratings). 3. Require mezzanine capital to have explicit or implicit ratings of B or CCC – within the mandate of MDBs to invest (e.g., IBRD has 21% of debt investments rated CCC or lower). 4. Senior-tier capital is reserved for private investors. 5. Minimum fund size of $2 billion. 6. In addition, preference for senior capital: (i) that can attract liquidity in the secondary market and (ii) in the form of notes/bonds that can be listed and traded (e.g., Eurobonds). Over time, PIMM10 is expected to lead to several derivatives: A. Funds that invest in local currency debt. B. Funds that invest debt in sub-sovereign borrowers. C. Funds that invest debt in national development banks. Over time, PIMM10 is expected to require less and less C&C funding – indeed one day it could be implemented with only MDB capital in a junior position.

DEBT FUND ADHERING TO PIMM9

Assume the fund is capitalized with three tiers of capital: (i) senior capital for 90% in the form of notes/bonds rated at investment grade (BBB), (ii) 7.5% mezzanine capital in form of bonds/notes with a rating aligned with MDB and DFI investment mandates, and (iii) 2.5% junior capital.



CONVERGENCE is the global network for blended finance. We generate blended finance data, intelligence, and deal flow to increase private sector investment in developing countries.