PRIVATE INVESTMENT MOBILIZATION MODELS (PIMMS) FACT SHEET:

Local Currency Solutions – Private Sector and Public Sector (PIMM12)

EXECUTIVE SUMMARY

PIMM12 is designed to reduce foreign exchange (FX) risk for countries, borrowers, projects, and investors.

OBJECTIVES

PIMM12 is dedicated to deploying catalytic and concessional (C&C) funding to increase the sustainability of private investment in developing countries by reducing currency risk for projects, borrowers, countries, and investors. Currency risk is mitigated most effectively and efficiently on a portfolio basis, therefore PIMM12 is expected to support solutions that will mitigate beyond one project (e.g., support long-term, local currency loans to multiple infrastructure projects in multiple countries as opposed to a $100 million local currency loan to one project).

The private investment mobilized is expected to happen at several levels including:

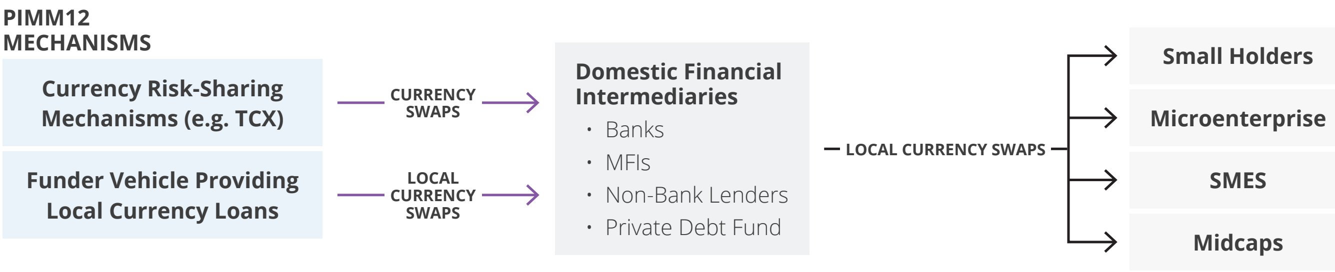
i. loans and bonds for public sector government borrowers and National Development Banks (NDBs) loans, bonds or equity investments into projects and real-economy companies in developing countries;
ii. loans, bonds, or equity investments into financial intermediaries in developing countries;
iii. loans, bonds, or equity investments into funds/portfolios, where the fund/portfolio provides investment in (i), (ii) or (iii) above; and
iv. loans and bonds into multilateral development banks (MDBs), bilateral development finance institutions (DFIs), and NDBs.

Rationale	The Fourth International Conference on Financing for Development Zero Draft describes the importance of sustainable investment, debt sustainability, and local currency mitigation. PIMM12 is intended for C&C funding to mobilize private investment that: (i) improves countries' debt sustainability and (ii) reduces currency risk for projects, borrowers, countries, and investors. A 2010 European Bank for Reconstruction and Development (EBRD) study found that developing countries' local currencies depreciated relative to the US dollar at 2.1% per annum on average, with high volatility. The combination of expected depreciation with high volatility impedes investment in developing countries.
Description	• C&C funding to reduce currency risk for countries, borrowers, projects, and investors • PIMM12 is expected to support systemically important solutions for the Sustainable Development Goals and climate investment.

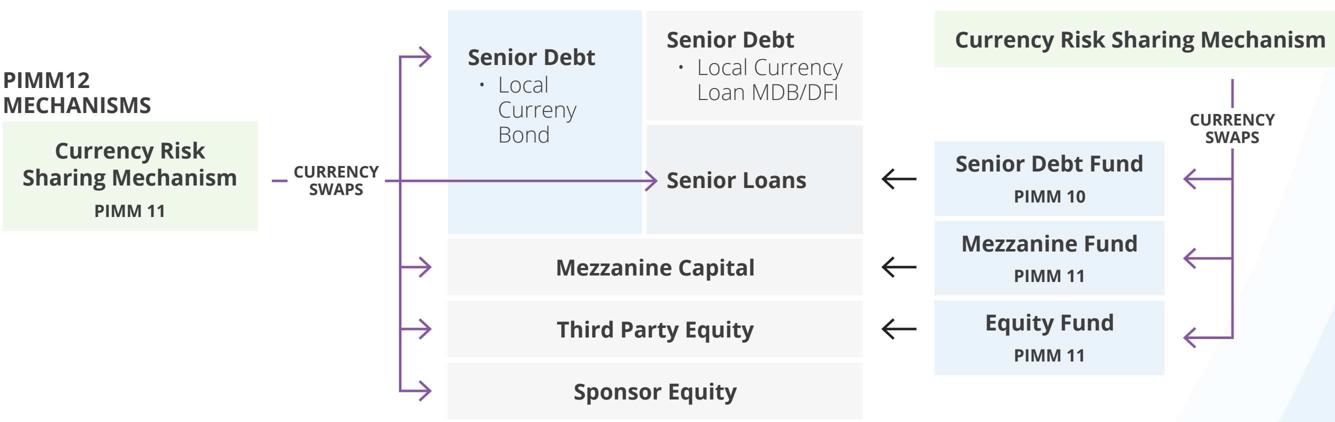
Development rationale	**Development literature is rich with evidence of currency risk impeding economic growth, domestic financial sector development, and improved standard of living.** Around 85-90% of MDB financing in developing countries is hard currency debt (e.g., USD and EUR loans). MDBs and DFIs have adopted self-imposed risk management policies that preclude them from taking open currency on their loan portfolios – therefore only lending in local currency if they can fund or hedge themselves. The large majority of bonds issued by entities in developing countries are denominated in hard currency (e.g., USD or EUR).
Existing comparable precedents of C&C funding	There are many precedents of C&C funding to support local currency solutions. Some examples include: 1. The Currency Exchange (TCX) provides around $1.5 – 2 billion of currency swaps annually. TCX benefits from: (i) around $500 million in junior capital from three governments on highly concessional terms bearing first loss and (ii) around $1 billion of capital from MDBs and DFIs deployed at below-market return expectations. TCX has also benefited from many other forms of concessional funding, including funding from the European Commission. 2. GuarantCo issues guarantees for local currency bonds and loans for infrastructure projects. GuarantCo is capitalized by the public sector on catalytic and concessional terms. 3. The Credit Guarantee Investment Facility (CGIF) operates similar to GuarantCo. 4. African Guarantee Fund (AGF) issues guarantees to African banks for loans – mostly local currency loans. AGF is capitalized by concessional public sector funds. 5. The European Investment Bank has operated the African, Caribbean, and Pacific Local Currency Loan Program for a decade, providing local currency loans with no hedging – evidencing an MDB business model of providing local currency loans on a profitable basis. The trial provided evidence that MDBs can manage a local currency loan portfolio with open currency risk and make profits. The trial was possible thanks to concessional funding from the European Commission. 6. EBRD operates the Small and Medium-Sized Enterprises Local Currency Program backed by $70 million of concessional funds. 7. KfW Development Bank operates the African Local Currency Bond Fund with concessional funding from 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 C&C funding to develop local currency solutions. It is likely most productive for the sub-group to have a broad, open call for proposals signalling the sub-group is prepared to accept proposals to award C&C funding to the best proposals that will develop local currency solutions: (i) aligned with debt sustainability and (ii) that will mobilize private investment. In competitive global calls for proposals, it is expected 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	**The majority of C&C funding is expected to be loans, equity investments, and guarantees for fair/equitable outcomes.**
Expected financial profile of C&C funding (including risk profile)	C&C funding deployed in PIMM12 is expected to take on a risk profile beyond the willingness or ability of MDBs and DFIs. There are likely two possible financial expectations of C&C funding in PIMM12: • Break-even or better expectations: It is likely a portion (potentially a majority) of C&C funding could be deployed at break-even (or better) financial outcomes. • Partial loss expectations: It is likely a portion (potentially a minority) of C&C funding would result in a partial loss.

Expected sources of private investment mobilized	Varied.
Expected leverage	Convergence forecasts reasonable leverage expectations in PIMM12 could range from 5-20 times.
Single-country or multi-country application	Both.
Recommended standardization for this PIMM	Convergence does not recommend any standardization for PIMM12. Over time, the Network might identify the benefits of standardization of PIMM12.

LOCAL CURRENCY SOLUTION ADHERING TO PIMM12 TO SUPPORT DOMESTIC FINANCIAL INTERMEDIARIES TO PROVIDE MORE LOCAL CURRENCY LOANS



LOCAL CURRENCY SOLUTION ADHERING TO PIMM12 TO HEDGE CURRENCY RISK OF DEBT AND EQUITY INVESTORS IN A COMPANY, PROJECT, OR PUBLIC-PRIVATE PARTNERSHIP



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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.