CONVERGENCE
BLENDING GLOBAL FINANCE

PRIVATE INVESTMENT MOBILIZATION MODELS (PIMMS) FACT SHEET:

Private Sector Blended Finance Equity Fund (PIMM11)

EXECUTIVE SUMMARY

PIMM11 is designed to mobilize fund managers (e.g., general partners) to establish new funds for investing equity in developing countries and mobilize private investors (e.g., limited partners) to invest in the senior capital of the fund. PIMM11 is intended to be the main PIMM to mobilize private investment in the form of equity to developing countries. Given the need to mobilize private investment aligned with debt sustainability, it is critical for PIMM11 to successfully mobilize equity investors.

OBJECTIVES

Mobilize equity investors to invest in private sector equity in developing countries indirectly through funds by reducing risk and improving expected distribution of investment returns.

Rationale	The perceived investment risk of investing equity in companies located in developing countries is driven significantly by perceptions of country and currency risk proxied 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. Indeed, many equity investors have a bias/rule to invest only in countries with investment grade sovereign ratings. PIMM11 is likely the best PIMM to increase the amount of equity financing, thereby supporting debt sustainability in developing countries.
Description	PIMM11 is a fund with two or three tiers of capital. The fund is designed to ensure senior capital is assessed by equity investors from developed countries as representing equal or superior risk-return investment opportunity, compared to equity funds deployed for developed countries. Three primary drivers of risk improvement are: 1. Diversification of investment risk (e.g., exposure to 10-15+ companies from 5+ countries in a fund versus investment in one company or geographic concentration in one country). 2. Diversification of currency risk, with the fund expected to typically invest in 5+ countries. 3. Subordination of junior capital and possibly mezzanine capital of the fund. The most common expected application of catalytic and concessional (C&C) funding for PIMM11 is to capitalize the junior tier of a two or three tiered blended finance equity fund. **C&C funding to increase the supply of equity investment to private sector companies in developing countries allowing companies to raise equity to make more capital investment for the Sustainable Development Goals and climate projects, and improve debt sustainability.**

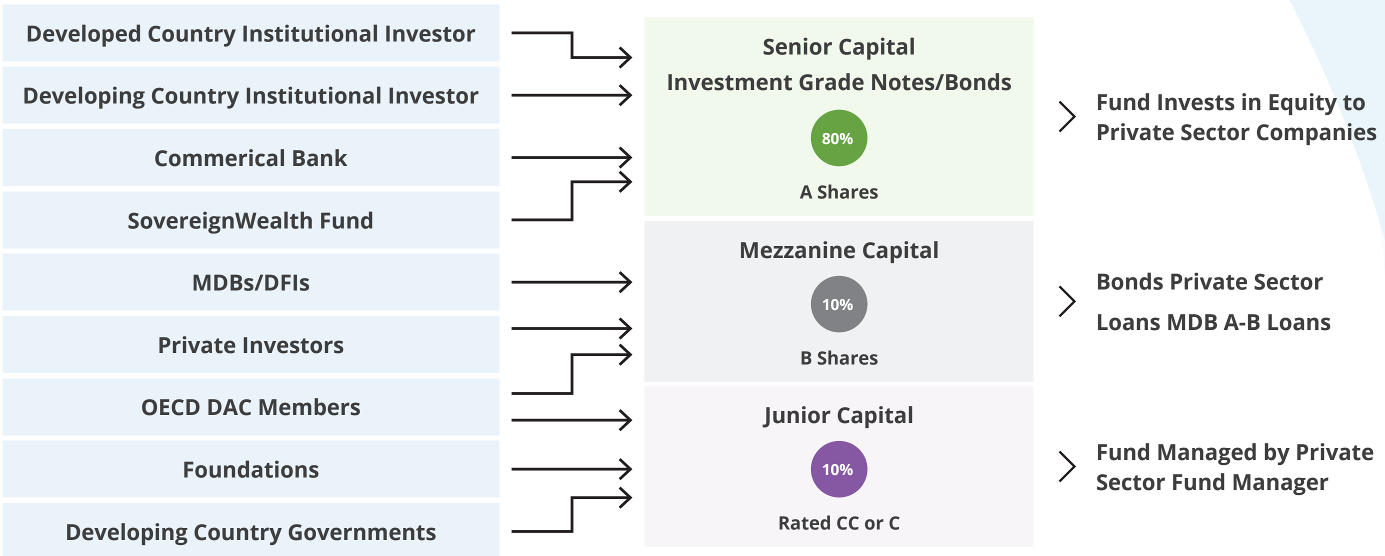
Development rationale	**C&C funding in PIMM11 will capitalize junior capital in two or three tiered blended finance equity funds to mobilize private investors to invest equity in senior capital and indirectly invest in private sector companies.** C&C funding as junior capital in two or three tiered private sector equity blended finance funds supports the development community's view that the perceived risk of investing in developing countries is higher than actual risk. For example, C&C funding as junior capital mostly underwrites the difference between perceived and actual risk including local currency depreciation relative to USD – if risk unfolds at higher levels consistent with private investors' perceptions then the C&C funding as junior capital will likely be depleted (partially or fully). If risk/depreciation unfolds closer to the development community's view, then the fund will likely earn returns at a level sufficient to generate attractive positive returns, thereby preserving C&C funding.
Existing comparable precedents of C&C funding	Convergence has 84 tiered blended finance equity funds in its Historical Deals Database investing equity in private sector companies. PIMM11 consolidates the lessons learned from those 84 private sector equity funds. Good benchmarks are the $672 million Blackrock Climate Finance Partnership, the $200 million Women's World Banking Capital Partners Fund II, and the $350 million Horizon Capital Growth Fund IV.
Indicative activities for Network of C&C Funders	The Network of C&C funders could establish a sub-group of organizations to award funding to mobilize private equity investment into private sector equity through PIMM11. Indicatively, the Network could consider two approaches: 1. Collaborate with multilateral development banks (MDBs) and bilateral development finance insitutions (DFIs): Network members and MDBs and bilateral DFIs investing equity in private sector companies could collaborate to establish two or three-tier blended financed equity fund(s) that would invest equity priced at commercial, market terms. MDBs and bilateral DFIs currently arrange around $10 billion of private sector direct equity investments annually. MDBs and DFIs could increase arranging volumes to $30 billion, retain $10 billion, and distribute $20 billion to the fund(s). MDBs and DFIs could invest in mezzanine equity in a three-tier fund. 2. Call for proposals: where the Network invites private sector fund managers to submit proposals describing how they could deploy C&C funding as junior capital in a two or three tiered equity fund that mobilizes private investment in senior capital. Network members would assess proposals and award their C&C funding to the best proposals. Illustrative proposals could be: (i) a fund that invests equity in banks and microfinance institutions; (ii) a fund that invests in Tier 2 capital to commercial banks; (iii) a fund that invests in project development companies; and/or (iv) a fund that invests equity in nationally determined contributions and Just Energy Transition Partnerships projects. 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(s)	**Majority of C&C funding is expected to be equity as junior capital in funds.** Historically, most C&C funding from Organisation for Economic Co-operation and Development 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 equity (e.g., a PSI).

Expected financial profile of C&C funding (including risk profile)	C&C funding deployed in PIMM11 is expected to take on a risk profile beyond the willingness or ability of MDBs and DFIs. For example, junior capital in most cases will have an expected loss or expected returns below market norms.
Expected sources of private investment mobilized	1. Equity fund managers (e.g., Allianz Global Investors and Blackrock). 2. Developed country institutional investors (e.g., pension companies and life insurance companies) in senior capital of fund(s). 3. Developing country institutional investors (e.g., pension companies and insurance companies). 4. Sovereign wealth funds.
Expected leverage	Reasonable leverage expectations in PIMM11 range from 5-15 times.
A single-country or multi-country application	Both. PIMM11 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. • Single country funds are expected to have domestic government funding as junior capital and to mobilize mostly domestic institutional investors (e.g., pension companies).
Recommended standardization for this PIMM	Based on extensive benchmarks, Convergence recommends four types of standardization for C&C funding for PIMM11: 1. Restrict to two or three-tiered blended finance funds – three tiers will likely produce maximum leverage/efficiency of C&C funding while generating good quality equity investment profiles for private investors that mobilize them to developing countries. 2. Senior tier of capital reserved for private investors (no MDBs or bilateral DFIs). 3. Minimum fund size of $100 million for multiple country funds. 4. Standard waterfall between senior, mezzanine, and junior investors, such as senior investors preferred distributions until break-even internal rate of return or preferred return to senior investors before junior investors catch-up. TO BE DETERMINED IN CONSULTATIONS. 5. In addition, preference for funds with senior capital that can attract liquidity in secondary market. TO BE DETERMINED IN CONSULTATIONS. Over time, PIMM11 is expected to require progressively less C&C funding – indeed one day it could be implemented with only MDB capital in junior position.

EQUITY FUND ADHERING TO PIMM11

Assume the fund is capitalized with three tiers of capital: (i) senior capital 80%, (ii) mezzanine capital 10%, and (iii) junior capital 10%.

PIMM 11 MECHANISMS



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.