INVESTING IN THE CLIMATE TRANSITION

The role of development banks, development finance institutions and their shareholders

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The global community has spoken loud and clear: more financial resources must be mobilised to mitigate climate change and support communities to adapt to the impacts of climate change and increase resilience. Development banks and development finance institutions (DFIs) are key actors to mobilise commercial resources and help bridge the climate investment gap. Shareholders of development banks and DFIs need to base their steering and guiding function on a good understanding of the institutions’ potential in supporting developing countries meet the Sustainable Development Goals (SDGs) and the Paris Agreement on climate change.

This Policy Perspectives draws on published OECD work, including the G20-mandated report *Financing Climate Futures: Rethinking Infrastructure*, and work under the OECD Development Assistance Committee (DAC) on measuring the amounts mobilised by official development finance interventions.
Executive summary

Making development banking fit for the 21st century: Implications for shareholders

While development banking has transformative potential to boost finance for climate action, shareholders must ensure development banks and DFIs can fully harness this potential. Evidence points to five areas of action for shareholders.

1. **Broaden the use of development banking**

To date, development banks and DFIs largely focus on direct financing. Blended finance approaches and instruments to mobilise commercial resources for development outcomes like climate action, are still only a small part of what development banks and DFIs do. Additionally, between 2012 and 2018, the majority of private finance mobilised through official development finance interventions was in middle-income countries (43% in upper middle-income countries), with a minority being mobilised in least developed countries and other low-income countries (6%). Within finance mobilised for climate action, there is a particular need to scale up support for adaptation: in 2012-18, 85% of finance mobilised targeted climate change mitigation only, compared with 3% of climate change adaptation only, and 12% targeting both mitigation and adaptation.

Shareholders of development banks and DFIs need to re-envision the way development banking can best support development outcomes, and assess whether their provision of concessional resources supports a stronger focus on mobilisation, including in different contexts and sectors. Additionally, shareholders need to strengthen institutional mandates to deliver transformative climate action by integrating development, mobilisation and climate more closely.

2. **Support and back a stronger focus on mobilising commercial finance**

In order to meet the objectives of the Paris Agreement and keep sustainable development within reach, mobilisation must focus on those financial resources that are not already deployed for climate action. Shareholders need to support and back development banks and DFIs to target their institutional focus on bringing new investors and sources of finance to climate investments, and facilitate the development of future-proof markets.

To enable an institutional re-wiring and shift of business models towards mobilisation, shareholders should reduce their expectations for ROE and re-think their allocation of concessional resources to allow development banks and DFIs to engage in policy support and capacity development, alongside direct financing, and thereby facilitate market creation and a systemic increase in finance for investment across a range of financial actors. Additionally, lower ROE expectations can also enable development banks and DFIs to engage in higher-risk activities to scale up mobilisation of private finance for example in LDCs and adaptation.
3. Target performance indicators towards mobilisation and impact

Strengthening performance indicators towards mobilisation must be based on a thorough review of what works and what doesn’t. However, there is a lack of evidence on specific incentive structures at corporate and staff level across different development banks and DFIs. While there have been various efforts to make the case for a stronger focus on mobilisation, and political support for this agenda is increasing, a consistent and comparable database that covers different institutions and the evolution of incentive structures, is lacking.

Shareholders, in particular donor shareholders, should build the evidence base for incentive systems and performance indicators, and their implications on mobilisation and impact on climate ambition. This evidence base and resulting impact analysis can inform changes to incentive systems and performance indicators, with the goal of better targeting them towards mobilisation and impact on the ground.

4. Think beyond mobilisation

In efforts to scale up finance and investment for climate action, development banks and DFIs have focused mostly on the mobilisation of commercial capital for specific transactions. To embark on their sustainability transition, developing countries are however beginning to implement efforts to shift financial decision-making across entire economies. For example, tax systems, government budgets and financial markets are ‘greened’ to catalyse broader financial flows towards climate action.

Shareholders should support development banks and DFIs to engage more strongly in mobilisation, and at the same time, support developing countries in catalytic activities. Ultimately, support to developing country-owned catalytic activities can contribute to achieving to Article 2.1(c) of the Paris Agreement: Ensuring consistency of all financial flows with a pathway towards low GHG emissions. To allow development banks and DFIs to consciously engage in direct financing, mobilisation, policy support and capacity development that can support country-owned catalytic activities, shareholders should assess their expectations on ROE and their provision of concessional finance for development banks and DFIs.

5. Support systemic change

Political momentum for climate action is increasing in the run-up to COP26. For example, the COP26 Presidency announced mobilisation of private finance in developing countries as a priority, and DAC members have recently committed to strengthen efforts to support developing countries to meet their climate goals. DAC members are cognisant of the relevance of development banks and DFIs, in particular MDBs, in achieving these objectives. At the same time, donor governments can guide and steer policies and activities of multilateral and bilateral development banks and DFIs.

Shareholder governments must collaborate to further strengthen mobilisation and catalysisation, and facilitate change across the ecosystem of development banks and DFIs. This will require further collaboration on a stronger focus on mobilisation, catalysation and climate ambition: (i) internally (between different ministries of one country); (ii) externally (across different countries); (iii) between development banks and DFIs.
Development finance can help bridge the estimated USD 70 billion annual adaptation and USD 2.5 trillion energy transition investment gaps in developing countries.

There is still a clear gap in action and investment required in developing countries to meet the commitments made under the Paris Agreement and deliver the SDGs. In 2020, global mean temperature was already 1.2°C above pre-industrial levels, and the period of 2011-2020 is the warmest decade on record (WMO, 2020[1]). According to the UN Environment Programme, current annual costs in developing countries to adapt to the impacts of climate change are estimated at USD 70 billion, and could increase to USD 140-300 billion per year up to 2030 (2021[2]). Additionally, 70% of the USD 3.5 trillion of investment required for the global energy transition will need to take place in developing countries (IEA and IRENA, 2017[3]); (Carney, 2020[4]). Beyond climate action as its own defined SDG, an indivisible link between sustainable development and ambitious climate action exists (OECD, 2019[5]).

At the same time, the landscape of financing for development is constantly evolving, with private flows – such as foreign direct investment and remittances – dwarfing official development finance (ODF) in developing countries (Figure 1). This is also true in key climate priority areas: ODF is estimated to contribute only 6-7% of infrastructure financing in developing countries, with developing country governments and the private sector financing significantly larger shares (Miyamoto and Chiofalo, 2016[6]). In fragile contexts, private investment continues to remain a small component of the financing landscape.

ODF remains an important support for developing countries but it needs to increasingly focus on mobilising commercial finance, and channelling existing resources towards the Paris goals. Multilateral and bilateral development banks and DFIs are crucial (OECD/The World Bank/UN Environment, 2018[8]): Their development mandate, range of instruments and infrastructure financing implies a key role, but they need to expand their portfolio beyond direct financing, and focus more strongly on mobilisation and achieving broader development impact. Beyond internationally-operating development banks, national and sub-national development banks from developing countries also need to increasingly engage in mobilisation.

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1 Official development finance refers to official interventions, regardless of their concessionality, extended with development as their main objective.

2 In addition to differences in regional scope, development banks and DFIs generally differ in their scope of clients. While variations exist, development banks work predominantly with public sector clients, and often have specific operations focused on private sector clients. DFIs are typically understood to be specialised private sector-oriented institutions that provide financing on non-concessional terms (OECD, 2020[9]).
The COVID-19 crisis presents significant challenges and opportunities for climate action. While developing countries face significant fiscal constraints in providing economic stimulus, the recovery presents a pivotal opportunity to ensure a structural decline of emissions, spur economic growth, create millions of clean jobs, and increase electricity access for almost 270 million individuals (IMF, 2020[9]; IEA, 2020[10]). Many development banks and DFIs will implement investments that are part of these stimulus packages.

Shareholders of development banks and DFIs – and in particular DAC members – can, and need to, enable development banks and DFIs to fully harness their transformative potential, help bridge the climate investment gaps and accelerate climate action by developing countries.

Figure 1. Official development finance is only a small share of external finance to developing countries overall

Note: In constant 2019 prices. ODF = Official development finance; FDI = Foreign direct investment

Source: (OECD, 2020[7]) Global Outlook on Financing for Sustainable Development 2021: A New Way to Invest for People and Planet

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The business model of development banks and development finance institutions leads to a focus on direct project finance, but they also engage in policy support and capacity development.

While heterogeneous in their specific structure and scope of interventions, development banks and DFIs share two defining features: (1) Their business model and (2) their functions or levers to promote sustainable development.

First, development banks and DFIs are financial institutions built around the provision of financial products. Facilitating development is their overarching goal, but their business model follows the same laws as that of any financial institution: The terms and conditions of financing provided, including expected financial returns, need to cover the cost of operations and funding (Figure 2). As a result, non-grant financing products, such as loans that are being repaid and enable continued operations and financing of new activities, constitute their core operations. To engage in activities that do not ensure full cost-recovery, such as financing on concessional terms, policy support and capacity development, development banks and DFIs require additional grant or concessional funding from donor shareholders, or shareholder agreement to use retained earnings.

Development banks and DFIs raise debt financing in capital markets, based on and in addition to the equity provided by shareholders (Figure 2). As such, they operate on the basis of the funding cost of their shareholder governments, which differs across institutions.

2 Why focus on development banks and development finance institutions when looking to scale finance?
The second common defining feature of development banks are their three main functions or levers to promote development. Development banks mostly provide direct financing (with an increasing focus to also mobilise additional investment); support governments in policy reform and the creation of markets; and develop capacities of public and private actors in developing countries (Figure 2).

Activities of policy support and capacity development however do not generate financial returns, and therefore exist beyond the business model of development banks. Development banks nonetheless offer this support as it can increase the viability of direct financing, and catalyse a broader set of financial flows for development. Given that DFIs are private sector-oriented institutions, their provision of capacity development and in particular policy support is limited, and often intended as ancillary outcomes of their financing.

In reflection of their business model, corporate and staff performance of development banks and DFIs is measured largely by financial indicators, such as financial resources committed or disbursed. This encourages an emphasis by institutions and individual officers on direct financing, but does not necessarily encourage the mobilisation of commercial resources. Similarly, there are few incentives to engage in policy support or capacity development, as these activities generally involve smaller amounts of grant resources. At the same time, however, the climate investment gaps require stronger efforts of development banks and DFIs on mobilisation, policy reform and capacity development.

Procedures for the provision of grant or concessional funding, in addition to the provision of capital by shareholders, to enable financing at subsidised rates, risk mitigation, policy support, and capacity development are already in place. For example, shareholders provide grant funding in periodic replenishment rounds to e.g. concessional windows of multilateral development banks (MDBs). Indeed, the World Bank’s International Development Association (IDA), which works with the world’s poorest countries and in fragile contexts, is dependent on concessional resources to engage in these activities. The most recent replenishment round provided USD 82 billion to IDA and included a focus on, inter alia, climate action.
What are the trends in mobilising finance for climate action?

Official development finance mobilised USD 52.5 billion from the private sector in 2018. Since 2012, an increasing share of amounts mobilised targets climate action.

OECD statistics highlight that official development finance interventions from bilateral and multilateral providers mobilised USD 213 billion of private finance between 2012 and 2018 for development outcomes (Figure 3). Since 2012, mobilisation increased from year to year, and reached USD 52.5 billion in 2018.

Information on private finance mobilised is relevant in enabling development banks and DFIs to engage more effectively in mobilisation. Beyond institutional aspects of development banks and DFIs and their impact on mobilisation, mobilisation is relevant in the context of the United Nations Framework Convention on Climate Change (UNFCCC) and efforts to estimate progress towards the goal of developed countries to jointly mobilise USD 100 billion per year by 2020 (OECD, 2015[11]); (OECD, 2019[12]); (OECD, 2020[13]). The figures on private finance mobilised for climate in this Policy Perspectives differ from those estimated for the UNFCCC process (see Annex), but the general trends observed are similar.

Private finance mobilised by official development finance interventions for climate increased from 2012-18 in absolute and relative terms (Figure 3). In 2012, official development finance interventions mobilised USD 3.9 billion of private finance for climate action, or 26% of private finance mobilised overall. In 2018, mobilisation for climate reached USD 17.7 billion, or 34% of amounts mobilised overall. Multilateral and bilateral development banks mobilised the vast majority (82% in 2018), with the remainder mobilised by bilateral DFIs. Preliminary data for 2019 suggest a decrease of total private finance mobilised of more than 10%, potentially affecting amounts of private finance mobilised for climate action as well.
Figure 3. Private finance mobilised by official development finance interventions
2012-2019, overall and by climate focus, in USD billion and shares

Note: Data collection on amounts mobilised, including for climate, was work in progress for the years 2012–2015 and conducted through surveys. The amounts presented in this period may therefore underestimate the level of private finance mobilised. Data for 2019 are preliminary. Source: (OECD, 2021[14]), Amounts mobilised from the private sector for development https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/mobilisation.htm.

In 2017-18, the banking and financial services sector attracted the highest volumes of private finance mobilised for development in general (on average USD 14.3 billion), followed by energy (on average USD 12.9 billion). Other key sectors for the sustainability transition (such as transport; agriculture, forestry and fishing; water supply and sanitation) were also under the top sectors for private finance mobilised overall. Vast potential for scaling up the amounts mobilised for climate action, and adaptation specifically, exists in these sectors.

Mobilisation by country income group

Private finance mobilised is concentrated in middle-income countries (MICs), with 70% of private finance mobilised for climate action targeting upper middle-income countries (UMICs, 43%) and lower middle-income countries (LMICs, 26%) in 2017-18 (Figure 4). In contrast, least developed countries (LDCs) and other low-income countries (LICs) accounted for only 6% of total private finance mobilised, and on average 73% of private finance mobilised in these countries did not include a climate focus. Unlocking private finance remains difficult in these countries, and concessional resources (including to support policy frameworks and market building), could support development banks and DFIs to make progress.
Figure 4. Private finance mobilised is concentrated in middle-income countries and largely targets mitigation outcomes

Average 2017-18, in USD billion and shares

Note: MADCTs are More Advanced Developing Countries and Territories, referring to recipients, which were included on the DAC List of ODA Recipients in the time of data reporting but have graduated from the list in the meantime. Examples include Chile, Seychelles and Uruguay.

Mobilisation by instrument

An analysis of instruments – guarantees, syndicated loans, credit lines, direct investment in companies and shares in common investment vehicles (CIVs) – highlights that these are not only mobilising different magnitudes of finance, but they are also applied in different country contexts and for different development outcomes (Figures 4 and 5). In 2017-18, guarantees mobilised the highest volumes of private finance for development overall (on average USD 15.7 billion in 2017-18, Figure 5), but direct investment in companies mobilised the largest volume of private finance for climate (on average USD 5.8 billion, or 49% of total private finance mobilised). Guarantees mobilised the second largest amount for climate projects in developing countries overall (USD 4.8 billion), followed by syndicated loans (USD 3.0 billion) and credit lines (USD 1.4 billion). In terms of country income groups, guarantees mobilised the most in LDCs and other LICs (55%), while direct investment in companies mobilised the largest amounts in MICs (around 35%, Figure 4).

Figure 5. Different leveraging instruments mobilise different magnitudes of private finance and are targeting different climate outcomes

In absolute terms, average 2017-18, in USD billion

In relative terms, average 2017-18, in shares


3 Including special purpose vehicles (SPVs).
The share of private finance mobilised for climate was the lowest in credit lines and guarantees (both 30%, Figure 5) and shares in CIVs (21%). Reporting issues, such as insufficient earmarking in portfolios and on-lending activities, could explain these findings but more information and evidence is needed to better understand the reality behind these figures and to more effectively enable development banks and DFIs to mobilise. The expected increase of guarantees in the COVID-19 recovery (OECD, 2020[15]) further highlights the need for an improved evidence base.

While OECD statistics on private finance mobilised are continuously growing, they generally focus on private finance mobilised by MDBs, bilateral development banks and DFIs. A growing body of literature highlights the important role of national development banks (NDBs) of developing countries in mobilising private finance for climate (Box 1), but comparable data on private finance mobilised by these institutions is still missing (OECD, 2019[16]).

**Box 1. The role of national development banks in mobilisation**

Worldwide, over 250 national development banks (NDBs) exist, with a collective financial footprint (USD 5 trillion in assets under management, AUM) that is significantly larger than that of MDBs (USD 1 trillion) (Gallagher and Kring, 2017[17]). Some of the larger NDBs hold assets that correspond to a significant share of national GDP, and NDBs more generally have specific comparative advantages for mobilisation over their internationally operating counterparts:

- **Proximity to local markets and embeddedness in national context**: NDBs are part of the local financing context and work directly with national and local governments as well as companies. As such, they act as policy influencers and pipeline developers that can support mobilisation.
- **Provide financing in local currency**: NDBs provide financing in local currency and thereby help develop local capital markets, which facilitates mobilisation.
- **Intermediate international development finance**: NDBs work with their international counterparts and climate funds to channel development finance to local projects, including with the purpose of mobilising commercial capital.

The recent Finance in Common Summit placed specific focus on NDBs, highlighting their crucial role in the global ecosystem of development banks and DFIs (Finance in Common Summit, 2020[18]). Just as multilateral and bilateral development banks need to become mobilisers of commercial capital, national development banks and their shareholders are required to implement the same change agenda to make a meaningful contribution to bridging investment gaps.

Most NDBs are however concentrated in middle-income countries, with NDBs in LICs only accounting for 7% of total NDB AUM (Xu, Marodon and Ru, 2020[19]). The marginal role of LIC NDBs further adds to the difficulties of mobilising commercial capital in these contexts (Figure 4).
How can development banks and domestic finance institutions move from sole financiers to mobilisers?

Institutional leadership and shareholder support are at the heart of re-thinking development banking.

Development banks and DFIs are increasing efforts to mobilise commercial investment, including for climate outcomes. Different institutions are at different levels in focusing on mobilisation, and differing capacities, regulatory and supervisory environments (for example of NDCs in LICs) further impact approaches and progress made. Overall, however, mobilisation is still only a small part of what development banks and DFIs do.

Shareholder governments are important drivers of change within development banks and DFIs. Across different types of institutions, they guide activities, and can further support targeted operations through the provision of capital and concessional finance. The latest capital increase of the World Bank Group, for example, encourages mobilisation for climate. Amidst demands for support on a variety of development challenges, efforts to mobilise private capital and finance high-risk, high-development impact projects need to take place within development banks’ and DFIs’ prudential and risk management regulations and capacity. In both regards, shareholders are essential, through their role in setting expectations on return on capital, and resulting implications of what constitutes an efficient risk-return frontier.

Targeted provision of concessional finance by donor shareholders is instrumental in expanding the scope for greater ambition on mobilisation. Using concessional finance strategically can help bridge viability gaps for investments in countries where markets are maturing and not yet optimal for mobilising commercial finance at market terms. At the same time, donor shareholders often face opposing pressure in using scarce public resources in high-risk, high impact environments and ensuring development additionality on the one hand, and domestic taxpayers’ pressures on the other hand that leave minimal tolerance for losses.

The case of the Development Bank of Southern Africa

While differences between development banks and DFIs exist, the Development Bank of Southern Africa (DBSA) provides an interesting case to highlight the role of shareholders in enabling development banks to evolve from sole financiers to mobilisers of additional resources. The experience of DBSA in re-envisioning its operations will be outlined in the remainder of this policy brief.
Beyond the strategic provision and use of concessional resources, scaling up mobilisation requires shareholder governments, development banks and DFIs to achieve three key elements:

- Institutional leadership, as well as support and backing of shareholders for the change agenda;
- Performance indicators on mobilisation at corporate and staff level;
- A rewiring of institutional culture to bring in new investors and sources of finance to create climate markets.

**Institutional leadership, support and backing of shareholders**

Development banks and DFIs have made ambitious commitments to scale up climate action and increase their climate finance activities. But to make a meaningful contribution to bridging investment gaps – in particular under consideration of their balance sheets and predetermined debt-to-equity ratios – they require institutional leadership to go beyond business as usual, and shift the focus of development banking from sole financiers to mobilisers. At the same time, shareholders need to realise the potential development impacts of promoting this change agenda in the institutions they own.

Providing development banks and DFIs with stronger, more coherent mandates on mobilisation and climate or environment is an important element increasingly taken up by different institutions. For example, the mandate of the newly established Canadian DFI, FinDev Canada, includes an explicit reference to environmental preservation, and mobilisation is at the core of the mandate of DBSA (FinDev Canada, 2020[20]); (OECD, 2019[16]). The G20 also recognised the need to shift business models from direct lending towards mobilisation (G20 Eminent Persons Group on Global Financial Governance, 2018[21]). Operationalising stronger mandates on mobilisation requires institutional leadership and shareholders to adjust institutional metrics, performance priorities and expectations, such as expectations on return-on-equity (ROE).

**Shifting institutional focus and adjusting expectations on financial return to deliver development impact**

In the case of DBSA, the National Treasury, as the bank’s shareholder, pushed for a stronger focus on development impact on the ground in 2014. In aiming to respond to this demand, DBSA realised its limitations to deliver impact in terms of addressing South Africa’s infrastructure needs, given the constraints posed by the bank’s balance sheet.

To contribute meaningfully to impact on the ground, DBSA instead embarked on a process of changing its institutional focus towards mobilisation and catalysation of additional finance, and the National Treasury and DBSA’s board of directors reduced their expectations for ROE to enable this change: Whereas in 2014/15 expectation on ROE stood at 7.5%, this was decreased to 4.9% for 2016/17 and 4.5% for 2020/21. This change allowed the bank to shift towards programmatic approaches, where financing is consciously provided alongside capacity development, policy and regulatory support, to facilitate market creation and a systemic increase in finance for infrastructure investment across a range of financial actors. In general, lower expectations on ROE can also enable development banks and DFIs to engage in higher-risk activities to mobilise private finance in contexts where mobilisation is currently not (yet) taking place.

**Target performance indicators towards mobilisation**

In order to implement the vision of a stronger focus on mobilisation, corporate and staff performance systems in development banks and DFIs need to include indicators on mobilisation and development impact, alongside disbursements or commitments. To date, leadership and shareholders often assess
institutional performance via resources disbursed or committed, and individual officers can typically advance their careers by focusing on projects that tie up large volumes of resources rather than closely involve the private sector and mobilise its resources. These incentive and performance systems instil the function of sole financier into the institutional DNA; a tension exists between these systems and the call for development banks and DFIs to evolve into mobilisers of additional resources.

Integrating mobilisation indicators in corporate scorecards and considerations of career advancement paths of individual officers will be key to aligning incentive systems, and thereby operational outcomes, with mobilisation objectives. Considering development impacts alongside mobilisation indicators in performance systems can help to ensure development additionality. Given the indivisible link between sustainable development and climate action, it is important to further ensure that mobilisation is well aligned with mitigation and adaptation goals.

**Introducing mobilisation alongside disbursement targets to shift institutional focus**

To further increase the focus on mobilisation, DBSA reduced its disbursement target in 2016, and simultaneously introduced a mobilisation target in its strategic objectives and corporate scorecard. These changes integrated mobilisation into DBSA’s DNA, and the bank further integrated metrics to measure catalysis of resources towards development and climate outcomes into its performance system. The same idea also underlies the World Bank’s ‘cascade approach’, which aims to guide staff to prioritise mobilisation where appropriate, and reserve scarce public financing for those areas where private sector engagement may not be feasible. It also scales up bank support to improve the enabling environment for private investment.

**Rewire the institutional culture to bring in new investors and sources of finance to create climate markets**

Ultimately, the institutional culture of development banks and DFIs needs to be re-wired to focus more strongly on mobilisation and market creation. This can entail a development bank to work with governments and private sector partners to develop solutions that may or may not involve the provision of financing by the development bank with associated financial returns. In particular shareholders, and where applicable donor shareholders, need to drive this cultural shift.

**Creating dedicated capacity on upstream processes to facilitate market development**

While undertaking efforts to place a stronger focus on mobilisation, it became clear that DBSA’s organisational structure still reflected the previous focus on direct financing, and needed to be re-wired in a sequenced approach to focus more strongly on the new institutional outlook of mobilisation. In view of this, DBSA created dedicated offices and resources for mobilisation and catalysis as well as pre-financing functions of the bank – such as project preparation, programmatic approaches and planning – which elevated the visibility and prioritisation of these objectives within the bank. These offices focused on working with public and private sector clients to find longer-term solutions for infrastructure promotion by bringing in new actors and supporting market creation, and did not necessarily focus on the outcome of e.g. loan provision by DBSA.

Underpinning all three key changes to drive the transition of development banks and DFIs to mobilisers of additional resources is the provision of dedicated resources by shareholders, including concessional resources for example by donor shareholders, to enable this shift in business models.
To fully tap into their transformational potential, development banks must work towards catalysing broader sets of finance to drive the climate transition.

The Paris Agreement was created with the critical basis of country ownership in mind, in recognition that countries hold primary responsibility for their economic and social development, including through action on climate change. Official development finance is only a small share of financing for development (see Figure 1), but it can be used strategically to support developing countries in shaping their development pathways and policies. Many developing countries are already engaging in efforts to channel financial flows, such as privately held capital, towards climate action, and official development finance should support these efforts.

Catalysis refers to development interventions such as policy support and capacity development that help create a more conducive environment for private sector investment. It goes further than mobilising resources for individual transactions, by aiming to channel resources across the economy towards broader development choices such as climate action – even after the development intervention itself is completed. Examples of catalytic activities include, for example, support provided for green financial sector reform, green taxation and budgeting, and carbon markets (World Bank, 2019[22]). Additionally, generating and using climate data, including for long-term modelling of climate change and its impacts as well as long-term low-emissions development strategy development are activities with catalytic potential.

A focus on direct financing limits the ability of development banking to support countries’ broader development choices and influence financial decision-making across economies. To effectively support development, a stronger focus on programmatic approaches is needed, that makes use of all levers of development cooperation – financing, policy support and capacity development. Beyond internationally operating development banks, NDBs are well positioned to develop more programmatic approaches of direct financing, policy support and capacity development, given their embeddedness in local policy contexts and proximity to local markets (Box 1).

While development agencies already engage in policy support and capacity development, there is a need for development banks to engage in these efforts as complementary action to direct financing and mobilisation. For example, development banks have increased policy support and capacity development to address political economy challenges for the promotion of renewable energy, adjacent to financing energy projects. In particular in LDCs and other LICs, policy support and capacity development, including for NDBs, national and local governments, are needed to increase the scope for mobilisation (see also section 3). To effectively support developing countries in delivering their broader development choices, cooperation and co-ordination on financing, policy support and capacity development across different development banks, DFIs and development agencies, is needed.
Engaging in financing, policy support and capacity development to fully harness the potential of development banks

An example of DBSA’s increased focus on catalysation is the bank’s engagement in South Africa’s Renewable Energy Independent Power Producer Procurement programme (REIPPP) (McNicoll et al., 2017[23]); (OECD, 2019[16]). First initiated in 2011, REIPPP includes a state-run competitive auction mechanism for renewable energy projects, and is largely attributed to have driven down cost of renewables in South Africa and mobilised private investment. While it involved a large variety of actors and mechanisms, including the state-owned utility, National Treasury, private project developers and South Africa’s Integrated Resource Plan, the inclusion of DBSA in different functions is regarded among the programme’s key success factors.

First – in its role as direct financier – DBSA contributed financing to every bidding round under the REIPPP, is the sole debt funder for community participation in the majority of projects, and joint-lead arranger and underwriter. Additionally, DBSA provided programme management advice and supported the creation of an office to implement REIPPP. These activities are typically not associated with financial returns, but rather generated cost for DBSA. However, these were key factors in facilitating market development and channelling broader investment towards renewable energies over the medium and long-term. The case of REIPPP and the favourable evolution of renewable energy in South Africa outline the need for programmatic approaches to financing, policy support and capacity development, in order to achieve broader development objectives as well as development banks’ mandates.

Engaging in activities such as policy support and capacity development to catalyse broader flows of finance towards the climate transition requires the provision of grant or concessional resources by donor shareholders and the strategic, targeted use of these resources by development banks and DFIs. A stronger focus on programmatic approaches that situate direct financing and mobilisation in a context with complementary policy support and capacity development needs to be part of re-envisioned development banking that effectively supports developing countries in achieving their own development objectives. To deliver on this vision, the encouraged provision of policy support and capacity development needs to be reflected in development banks’ internal systems and metrics. Development banks’ and DFIs’ engagement in programmatic approaches will be especially important in the COVID-19 recovery, which represents a significant and not-to-miss opportunity to shape the nature of private sector investments.
Annex A. Differences in accounting for private finance mobilised for climate

Since 2015, the OECD has been measuring progress made by developed countries towards the goal of jointly mobilising USD 100 billion per year by 2020 for climate action in developing countries. Following two first assessments (OECD, 2019[12], OECD, 2015[11]) the most recent report adds figures for 2018 to the previously released 2013-17 time series, as well as deepens the analysis by providing not only aggregate figures but also breakdowns in terms of recipients and characteristics of climate finance commitments (OECD, 2020[13]).

The figures and analyses are based on an accounting framework and methodology consistent with the scope of the USD 100 billion goal as well as with the outcome of the UNFCCC COP24 as regards modalities for the accounting of financial resources provided and mobilised through public interventions. The figures include four components: bilateral public climate finance; multilateral climate finance attributed to developed countries; climate-related officially supported export credits; and private finance mobilised by bilateral and multilateral public climate finance, attributed to developed countries.

The annual figures for the private climate finance component differ from those presented in this Policy Perspectives. The main reasons behind these differences are summarised in Table A.1.

Table A.1. Main differences in accounting for private finance mobilised for climate

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<tr>
<td>1. DAC members</td>
<td>1. “Developed countries”, i.e. Annex II Parties to UNFCCC, EU Member States, Lichtenstein and Monaco.</td>
<td></td>
</tr>
<tr>
<td>2. Non-DAC countries</td>
<td>2. Multilateral organisations with shareholding by developed countries. Importantly, volumes of private finance mobilised by such multilateral organisations are adjusted to only account for the share attributable to developed countries. Depending on the institution, such share ranges from 5% to 100%.</td>
<td></td>
</tr>
<tr>
<td>3. Multilateral agencies</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| Data sources | Mobilised private finance data recorded in OECD DAC statistics. | Mobilised private finance data recorded in OECD DAC statistics, complemented (for a small number of providers) by ad hoc data collection and OECD estimates to fill data gaps. |
References


OECD (2020), *Climate Finance Provided and Mobilised by Developed Countries in 2013-18*,
OECD (2020), *COVID-19 Survey – Main Findings*,

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