The complementary role of official development finance: some observations and recommendations.

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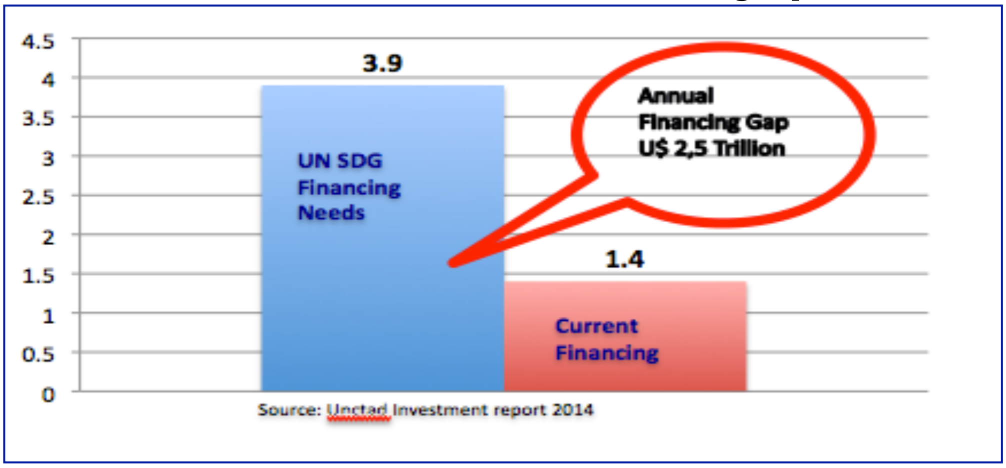
I. Introduction.

In various studies of the World Bank and other development finance institutions (DFIs[1].) it is highlighted that the financing needs of developing countries to meet the UN Sustainable Development goals (UN SDGs) are enormous. These SDGs cover a broad range of development topics among which infrastructure, climate change, poverty reduction, education and health. UNCTAD estimates that the UN SDGs require an additional investment of $2.5 trillion a year over the next 15 years.

Estimated annual investment needs & UN SDG Financing Gap in U$ trillion.



The international aid community broadly recognizes there is a huge financing gap between the UN SDG financing needs and the financing that is available from developing countries' own resources and funds from bilateral aid donors and DFIs. This implies that mobilization of non-developmental sources of capital – both public and private – is of utmost importance. In their joint report "from billions to trillions", published in April 2015, leading DFIs among which the World Bank Group, ADB, EIB, EBRD, IaDB, AfDB and the IMF state that "*to meet the investment needs of the SDGs, the global community needs to move the discussion from "Billions" in ODA to "Trillions" in investments of all kinds: public and private, national and global, in both capital and capacity".*

It is also recognized by leading DFIs that the SDG agenda and their efforts to mobilize non-developmental sources of capital require "*not only just more money"*, but also "*a global change of mindsets, approaches and accountabilities"*. In other words a fundamental redesign of the aid architecture is needed.

A substantial part of the UN SDG financing gap is caused by the lack of bankable projects. This means that more efforts have to be put into project development. An interesting initiative of the DFI community is SOURCE, which is a public project management tool

[1] There are multilateral and bilateral DFIs. The most well known multilateral DFIs are IBRD/IDA, IFC MIGA, ADB, IaDB, AfDB, EBRD, IDB and EIB. Recently two new multilateral DFIs were established, namely the AIIB and NDB. Examples of bilateral DFIs are public sector development banks / agencies such as KfW (Germany) and AfD (France) and private sector development banks such as OPIC (USA), DEG (Germany), Proparco (France) and FMO (The Netherlands).

enabling government and public sector agencies to improve their project preparation activities.[2]

II. The role of the OECD DAC.

In light of these developments the OECD Development Assistance Committee (DAC), which is the most important international forum dealing with the international aid architecture, has made some important changes that have an impact on the development finance community and other providers of finance for developing countries. The main topic in the OECD DAC concerns Official Development Assistance (ODA), which is basically a soft or concessional form of development finance. The international donor community has committed to allocate 0.7% of their Gross National Income (GNI) to ODA for developing countries, which explains the importance of ODA. ODA consists of bilateral ODA from donor countries to aid recipient countries and contributions from ODA donor countries to multilateral development finance institutions. A grant to for example IDA is recognised as ODA. Disbursements under bilateral aid loans with a minimum concessionality or grant level of 25% can also be reported as ODA. Repayments of these loans are treated as negative ODA. This is why the current ODA framework recognises gross and net ODA.

According to preliminary OECD DAC statistics the net ODA disbursements of all DAC members were in 2016 approximately U$ 170 billion, of which U$ 128.6 billion concerned bilateral ODA and U$ 41.6 billion financial contributions to multilateral institutions.

Current ODA definition.

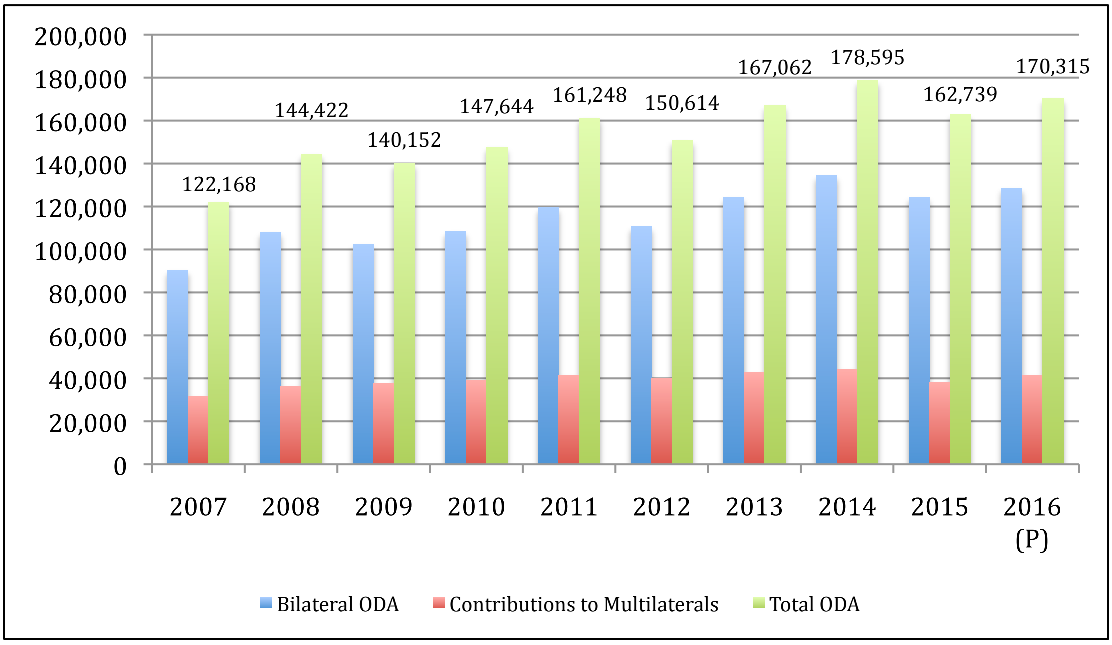
The DAC defines ODA as "those flows to (1) countries and territories on the DAC List of ODA Recipients and to (2) multilateral institutions which are:
i. ***provided by official agencies***, including state and local governments, or by their executive agencies; and
ii. each transaction of which:
a) is administered with the promotion of the **economic development and welfare of developing countries** as its main objective; and
b) is **concessional in character** and conveys a grant element of at least 25 per cent (calculated at a rate of discount of 10 per cent)."

Source: OECD DAC.

In 2014 the OECD DAC agreed to implement a new methodology to measure the minimum concessionality level for Official Development Assistance (ODA). With concessionality calculations the OECD DAC donor countries measure in essence the amount of subsidy provided by a donor to distinguish ODA from other forms of (official) financing.

[2] SOURCE has been developed by the Sustainable Infrastructure Foundation (SIF), which acts as executing agency for all participating development banks among which ADB, AfDB, BNDES, DBSA, EBRD, IaDB and the World Bank group.

Net ODA disbursements in million U$ (at current prices).



Source: OECD DAC.

III. Development of a new ODA framework.

In the current OECD DAC system to measure concessionality a grant leads to a concessionality level of 100%, whereas a commercial bank loan (without any official subsidies) leads to a concessionality level of 0%. According to the current ODA definition the minimum concessionality level for a loan to qualify as ODA is 25%, but for many years a fixed – highly doubtful – discount rate of 10% has been used, irrespective the tenor of the loan, the relevant currency and market interest rates of the financing. Today market discount rates are substantially lower than the fixed 10% of the OECD DAC. In the context of OECD tied aid regulations in the OECD Arrangement for officially supported export credits (which is governed by a different OECD forum than the DAC) more realistic discount rates are used. They are currency specific; take into account market interest rates for sovereign borrowers and the tenor of the loan. Today's discount rates for tied aid credits with a tenor between 15 and 20 years are for the Euro 1.7% and for the U$ 3.7%[3]. They are therefore substantially lower than the 10% discount rate for ODA. For many years it has been quite easy for many donors to lend at or slightly above their own long-term sovereign bond rates, while still meeting the 25% ODA concessionality threshold. The artificial high ODA discount rate led therefore to a highly inflated ODA performance of donor countries during the past decade. This was an important motive for the DAC to redefine ODA.

At the end of December 2014 OECD DAC members agreed to count only as ODA development grants and for development loans only the "grant portion" of the loan. This "grant portion" is in essence the aid subsidy involved and is calculated on the basis of new specific ODA discount rates. These new discount rates are now differentiated in three country categories, namely 9% for Least Developed Countries (LDCs) and Low Income Countries (LICs), 7% for Lower Middle Income Countries (LMICs) and 6% for Upper Middle Income Countries (UMICs). Unfortunately the new ODA discount rates are again not an accurate reflection of market interest rates and still much higher than the

[3] These are the so-called Differentiated Discount Rates (DDRs) that are published by the OECD Export credit secretariat. The DDRs vary by currency and tenor of the financing.

more realistic discount rates for tied aid credits. It implies that ODA will remain highly inflated in the future.

Interesting is that the IMF and World Bank apply a fixed 5%[4] discount rate to measure minimum concessionality levels for loans to countries that fall under the IMF / World Bank Debt Sustainability Framework (IMF/WB DSF). The DSF was developed to avoid unsustainable borrowing by developing countries. It applies to all Low Income Countries (LICs) of which many in the past two decades benefitted from debt relief.

As a consequence of these recent changes there are currently three different methodologies for concessionality calculations for aid loans of which the one for ODA is the least realistic. This is likely influenced by the desire of DAC member countries to meet the 0.7% ODA/GNI commitment.

In addition the OECD DAC agreed in 2014 to new minimum concessionality levels, which further complicate the ODA framework. For Lower Middle Income Countries (LMIC) the minimum concessionality level is set at 15% and for Upper Middle Income Countries (UMIC) it is 10%. This implies that for aid loans to these countries less aid subsidies are required than under the old ODA framework. Furthermore the concessionality level for the Least Developed Countries (LDC) and other Low Income Countries (LIC) have been increased from 25% to 45%, which implies that for these countries aid loans require a higher amount of subsidy to qualify as ODA. Important is that these new ODA rules are not only relevant for bilateral ODA loans, but also for the concessional lending activities of multilateral donors such as IDA and the regional development banks. For concessional loans of Multilateral Development Banks (MDBs) have to meet the applicable ODA minimum concessionality levels.

The rationale of the ODA changes of minimum concessionality levels is to encourage donors to provide more ODA to countries that are highly dependent on aid and less ODA to countries that have reasonable access to alternative sources of finance. But the unintended side effect could very well be that ODA loans to LMICs and UMICs will increase, because donors require substantial less aid subsidies for aid loans to these countries. The new concessionality rules could therefore be completely counterproductive. Additional measures are needed to avoid a misallocation of ODA.

Table 1: Aid architecture and concessionality calculations

	Old ODA	New ODA	IMF / WB DSF	Tied Aid
Grant Element Thresholds	25%	• 45% for LDCs and other LICs • 15% for LMICs • 10% for UMICs	35%	• 50% for LDCs • 35% for all other countries
Discount Rates	10%	• 9% for LDCs and other LICs • 7% for LMICs • 6% for UMICs	5%	• Euro: 1.7% (1) • U$: 3.7% (1)

(1) These interest rates are according to the OECD arrangement on officially supported export credits the applicable discount rates for tied aid credits with a tenor between 15 and 20 years in March 2017.

In the IMF/ WB DSF, which applies to LICs, the minimum concessionality level is 35%, while for tied aid credits the minimum concessionality levels are 50% for LDCs and 35% for all other countries. It is unclear why the DAC has opted for its own minimum concessionalty requirements. Fact is that the new ODA minimum concessionality levels and discount rates have complicated the international aid architecture.

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[4] The IMF / WB adopted a 5% discount rate for simplicity reasons.

Currently the OECD DAC is discussing how ODA can be used to encourage mobilization of private sector sources of capital. This concerns a discussion on Private Sector Instruments (PSI), which includes loans, guarantees and equity investments. The focus of the current discussion is to determine the so-called ODA component (i.e. aid subsidy) of these PSI-instruments. Very arbitrary calculation methodologies are suggested to distract the ODA subsidy from these financial instruments. This ODA component can then be reported as ODA, which will likely imply an increase of the ODA performance of donors. The intention of the OECD DAC is to seek first an agreement on these ODA aid subsidy calculations and at a latter stage a discussion will take place on the complementary role of ODA. One of the problems is that again unrealistic discount rates are used to calculate the ODA component of the PSI–instruments, which has also an impact on others forms of official finance.

A challenge in all these OECD DAC discussions is that the entire new ODA framework is discussed in complete isolation without properly taking into account market realities and the potential negative impact of new regulations on alternative (non-ODA) sources of capital that are available to developing countries. Instead of crowding in non-developmental sources of capital ODA may crowd out these alternative sources. Clarity about the complementary role of not only ODA, but also other forms of officially supported development financing, is therefore of utmost importance. It is in the interest of the donor community and the SDG agenda at large to use scarce subsidized aid financing only for projects in countries that do not have adequate access to financing that requires no or less official support. The higher the aid subsidies involved the more prudency is needed to avoid crowding out.

In other words a clear understanding on the complementary role of development finance is critical and urgently needed to enhance aid efficiency and aid effectiveness and achieve the UN SDGs.

IV. ODA and other sources of finance available for developing countries.

Countries make use of various sources of finance. These sources include market based debt finance from domestic and international bank and capital markets (without any form of official support), ODA and Other Official Flows (OOF). OOF, which is also reported to the OECD, concerns official (government supported) financing, which does not meet the ODA conditions, either because it is not primarily aimed at development of developing countries or because it has a concessionality level of less than 25%. OOF includes officially supported export credits of official Export Credit Agencies (ECAs) and loans from bilateral DFIs that provide financing on non-concessional terms, either at preferential interest rates (but too high to qualify as ODA) or on market based terms. Other examples of OOF are official investment loans[5] of EXIM banks and ECAs that are in particular used in project finance, private sector market based lending of bilateral DFIs (e.g. loans from FMO, DEG, Proparco) and so-called bilateral "promotional loans[6]" to sovereign borrowers, whereby the bilateral DFI passes on the benefits of its low funding costs to the loan to the sovereign. The German development bank KfW is quite active in this area of promotional sovereign loans.

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[5] Investment loans or investment guarantees from EXIM banks and ECA-insurers are formally not tied to exports from the ECA country, but tied to the nationality of the investor.

[6] It is unknown whether these bilateral promotional loans will qualify as ODA or OOF under the new ODA regime. It all depends on the level of concessionality of these promotional loans.

The role of official Export Credit Agencies (ECAs).

ECAs exist in many OECD and non-OECD countries. Their main objective is to support exports and foreign investments from their home country. Leading ECAs are member of the so-called Berne Union, which is a global association of credit and political risk insurers. Berne Union members supported in 2016 11.1% of global exports. At the end of 2016 the total MLT exposure of Berne Union members in both export credits and investments was approx. U$ 961 billion. This amount is more than 200% of the outstanding exposure of leading DFIs on developing countries, which in 2016 stood at approximately U$ 419 billion.

Outstanding exposure of leading MDBs in 2016 (in million U$)

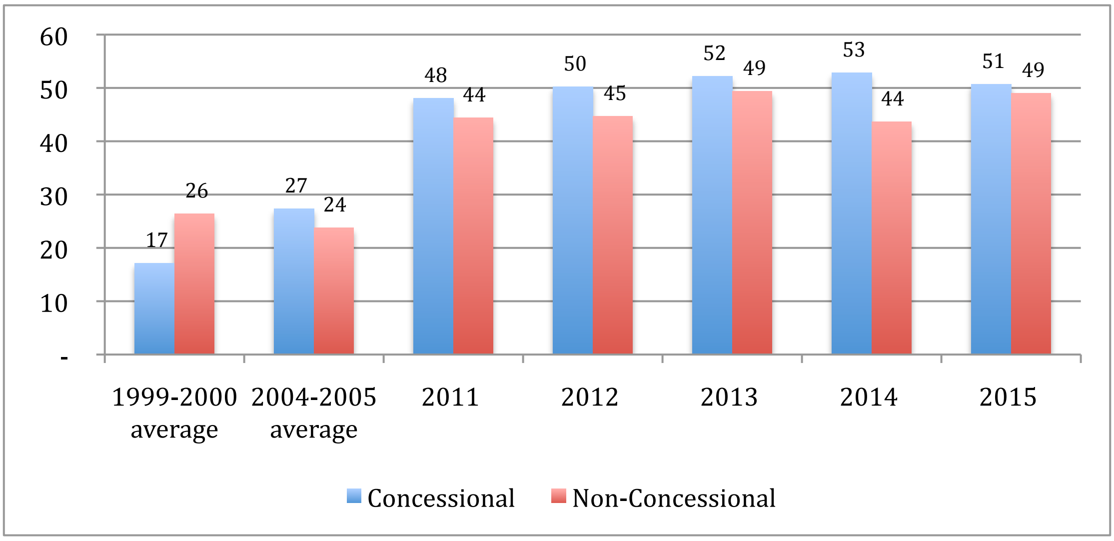
	Loans	Equity	Guarantees	Total
IBRD/IDA	167.643	0	5.198	172.841
IFC	23.910	10.793	3.478	38.181
ADB	67.599	1.187	2.105	70.891
IaDB	81.952	0	230	82.182
AfDB	21.641	104	565	22.310
EBRD	26.213	5.949	638	32.800
Total	**388.958**	**18.033**	**12.214**	**419.205**

Obviously the mandates of ECAs and DFI's differ. DFI's have a developmental mandate, whereas ECAs have primarily an export promotion mandate. It is, however, a fact that both DFIs and ECAs have an important developmental impact, for they are both key in financing the import and investment needs of developing countries.

Source: Berne Union and MDB annual reports 2016.

Developing countries borrow also substantial amounts from Multilateral Development Banks (MDBs). Such financing provided by entities like the IBRD/IDA is reported to the OECD under "multilateral concessional lending" (which is the ODA equivalent for MDBs) or "multilateral non-concessional lending" (which is the OOF equivalent for MDBs).

Multilateral gross disbursement in billion U$.



Source: OECD DAC

Non-concessional loans of MDBs include market-based loans to private sector borrowers. Examples are private sector loans provided by IFC and the private lending departments of ADB, EBRD, IaDB and AfDB and sovereign loans to the public sector at preferential subsidized interest rates. The latter concerns loans whereby the MDB passes on the benefits of its low funding costs (based upon its AAA credit rating and preferred creditor status) to the loans for their sovereign borrowers. These sovereign preferential loans are under the current ODA regime not concessional[7], but benefit from a substantial subsidy. The interest rates are not market based. Although each MDB applies its own pricing system and pricing differs among MDBs, the interest rates of individual MDBs are for all their sovereign borrowers the same, irrespective their credit standing. An IBRD loan to a country like China, Mexico, Brazil, Turkey or India has for example the same interest rate as an IBRD loan to a high risk country in Africa.

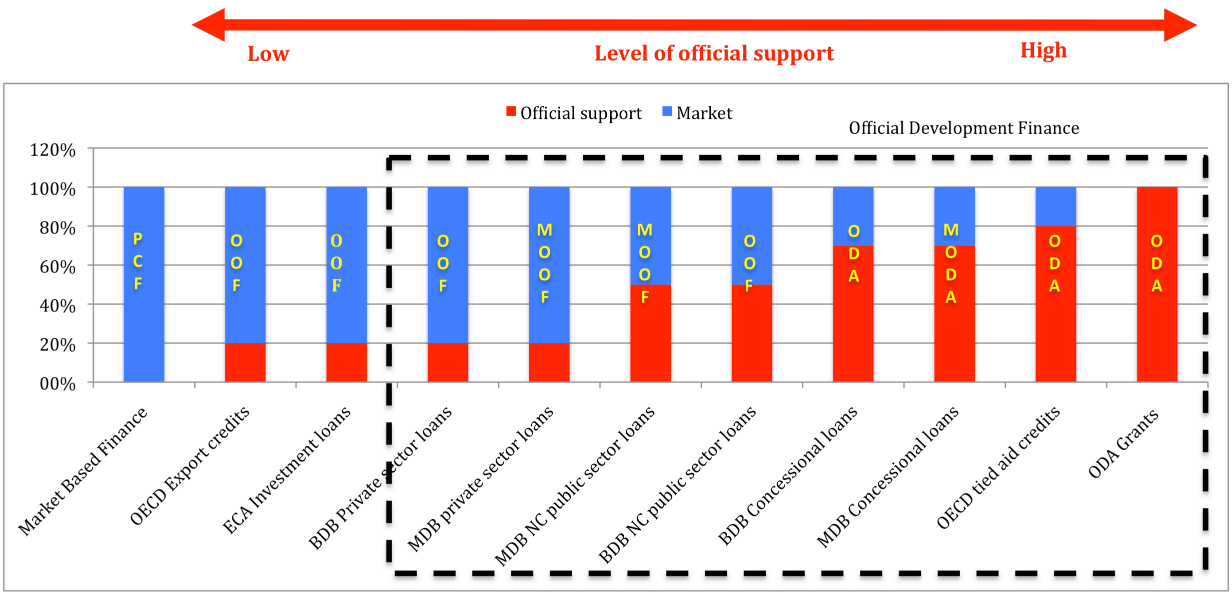
Indicative non-concessional U$ lending interest rates of MDBs for sovereign loans with an average maturity of 15 years (Sept 2017).

	IBRD	**ADB**	**IaDB**	**AfDB**
Floating Base Rate for U$	6 month Libor	6 month Libor	3 month Libor	6 month Libor
Base rate	50 Bps	50 Bps	85 Bps	80 Bps
Maturity premium	30 Bps	20 Bps	Not Applicable	10 Bps
Funding rebate / costs	- 5 Bps	- 5 Bps	+ 10 Bps	- 2 Bps
Total spread over LIBOR	**75 Bps**	**55 Bps**	**95 Bps**	**88 Bps**

Sources: IBRD, ADB, IaDB, AfDB.

In the OECD DAC discussions on the ODA component of PSI instruments the DAC is in fact looking at the "ODA aid subsidy" in OOF financing statistics. Would it not be easier for donors to partially reallocate ODA funds to OOF financing instruments? Most OECD DAC donors are apparently not in favor of that because this would likely negatively affect their international commitment to spend 0.7% of GNI on ODA.

Main sources of official finance for developing countries and the level of official support involved.



Source: Sustainable Finance & Insurance

PCF: Private capital flows
OOF: Other official flows
MOOF: Multilateral OOF = multilateral non-concessional lending
ODA: Official Development finance
MODA: Multilateral ODA = multilateral concessional lending.

[7] It is unknown whether these preferential MDB sovereign loans will be reported as concessional or non-concessional loans under the new ODA framework. It will depend on the concessionality level of the MDB loans.

The table above summarizes all main forms of official financing available to developing countries. It provides also indications of the '"level of official support" for each financing modality. Obviously an "ODA grant" constitutes the highest form of official support and "market based finance", such as a commercial bank loan, involves no official support. Between "market based finance" and "ODA grants" there are various forms of official finance, with different levels of official support. Official non-development finance concerns (1) OECD ECA exports and (2) OECD ECA investment loans. The other forms of official finance concerns Official Development Finance (ODF), which is the sum of ODA + OOF provided by DFIs.

IV. How to avoid crowding out of market based finance or other sources of official finance.

Given the enormous financing needs of developing countries mobilization of private capital is high on the agenda of the international aid community. This implies that the DFIs and their guardian authorities need to be fully aware of which other sources of finance are (potentially) available to developing countries and how these other sources can be tapped.

There is tendency within the aid community to narrow the discussions on the mobilization of private capital to the development of public private partnerships (PPPs), in particular through project finance. The latter concerns projects that have the potential to generate sufficient income to repay commercial debt financing and pay dividend to equity investors. The too narrow approach ignores amongst others that private capital can not only be mobilized for private sector sponsored PPP projects, but also for typical public sector projects, whereby the government (sovereign) or a sub sovereign entity (e.g. municipality) or state owned enterprise (SOE) acts as borrower or guarantor. This is for example relevant for most transport, electricity distribution, climate adaptation and water projects. Most roads, railways, regional airports, harbours, drinking water & sanitation projects are and will likely remain typical public sector projects in many developing countries[8].

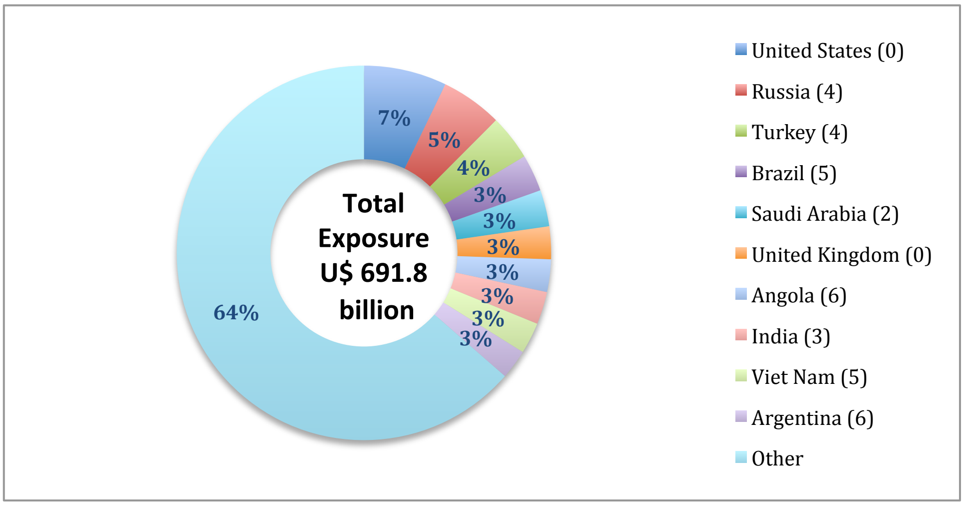
In India, which is the most advanced in private sector participation in infrastructure, 64% of the country's infrastructure is still financed and managed by the public sector. In most other developing countries the share of public sector infrastructure is likely substantially higher. PPP can contribute to bridging the infrastructure financing gap, but is clearly not the panacea. DFIs' mobilization strategies should therefore also focus on mobilizing capital for public sector projects. This is currently hardly discussed in the DFI community, whereas the opportunities for the mobilization of capital for public sector projects are substantial. Many governments in developing countries – in particular middle-income countries – have good or reasonable access to the private market and can obtain financing (support) from for example official Export Credit Agencies, commercial banks and private insurers. This concerns in particular countries that are rated in OECD ECA risk categories 2 – 4, but opportunities also exist in countries with a higher risk profile[9]. The impressive overlap of exposures of for example IBRD/IDA and Berne Union members on many countries show there are huge opportunities for cooperation and alignment of operations. More or less similar overlaps exist with the portfolios of other Multilateral Development Banks (e.g. ADB, IaDB, EBRD, EIB, AfDB).

[8] It is noteworthy that most PPP projects in developing countries concern electricity generation / energy and telecom projects. See the PPI database of the World Bank.

[9] More information about the OECD country risk classification can be found via the following link: http://www.oecd.org/trade/xcred/crc.htm

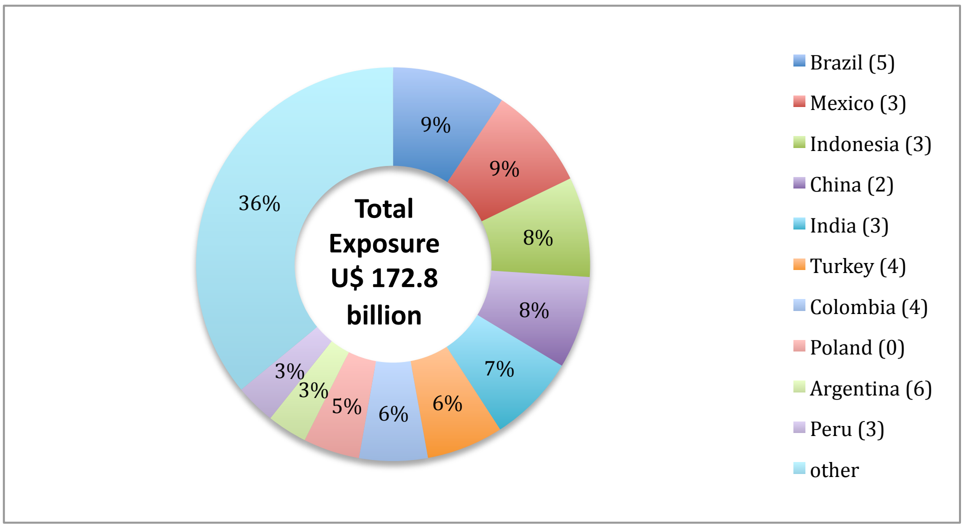
Enhanced cooperation through among others guarantee and risk transfer operations should be explored and utilized to mobilize more financing for development and to improve aid efficiency and aid effectiveness.

Top 10 MLT export credit exposure countries Berne Union members 2016. Between brackets the OECD ECA country risk rating of Oct. 2017.



Source: Berne Union.

IBRD top 10 exposure countries in % of total exposure in 2016 Between brackets the OECD ECA country risk rating of Oct. 2017.



Source: IBRD Annual report 2016.

The aid community focuses on mobilizing private capital, but this ignores that important public – non-developmental – sources of capital can be catalyzed for developing countries, This concerns among others insurance capacity of official export credit agencies and lending capacity of EXIM banks and investment capital from sovereign wealth funds. These three public sources have substantial capital available to support SDG projects in developing countries. That's why (governments through their) multilateral and bilateral DFIs should include these potential sources in their mobilization strategies.

DFI mobilization strategies require not only clarity on which public or private funds can be crowded in, but also a clear view on how potential "crowding out" of other forms of finance without or with substantial less official support, can be avoided. In other words:

clarity about the complementary role of official finance. In this area the OECD DAC has thus far made little progress. There is the intention to discuss "additionality" in the near future, but this is limited to ODA PSI-instruments. The upcoming DAC discussion should also include additionality of non-ODA forms of official development finance and development finance for public sector borrowers.

Participants to the OECD Arrangement on officially supported export credits have made some important regulations on this topic. They have amongst others defined minimum premiums to avoid distortion of competition between various ECAs that are caused by pricing differences. Furthermore the rules have been set to avoid a credit subsidy race between OECD governments, because ultimately the ECA export promotion schemes involve scarce governments budgets and tax payers' money. These considerations are obviously also relevant for other forms of official finance, including development finance.

The minimum OECD ECA risk premiums are based upon a joint risk assessment by all OECD ECAs of the financial, economic and political situation of countries. In the design of the minimum premiums market based pricing benchmarks were also taken into account. The system is furthermore fed by the joint payment experiences of OECD ECAs with developing countries. These minimum premium rules have been highly effective to avoid pricing distortion of competition in the export finance business between OECD ECAs.[10]

The minimum OECD premium rules do not apply to bilateral investment loans provided by EXIM banks or supported by investment guarantees from ECA-insurers, because these loans or guarantees are not tied to exports but tied to the nationality of the (equity) investor. Reliable data on ECA pricing practices for these investment loans or investment guarantees are unfortunately not available. There are, however, indications that these untied investment loans are crowding out official export credits. During the past 6-8 years the volume of untied investment loans and guarantees have substantially increased[11]. They are mainly used for debt financing of greenfield project finance transactions in which foreign equity investors are involved. This concerns the largest share of Public Private Partnership projects.

The problem of crowding out of official export credits by these official investment loans / guarantees could be avoided if for these EXIM / ECA investment loans the OECD minimum premiums would apply. For the ECAs involved this should technically not be a problem, because they are already familiar with the OECD pricing system and the risks to which they are exposed under their investment programs are very similar to the risks under their export credit programs.

[10] More information about the OECD minimum premium for officially supported export credits can be found on the following website of the OECD: http://www.oecd.org/tad/xcred/

[11] Important providers of untied investment loans are amongst others JBIC (Japan), KEXIM (South Korea) and OPIC (The United States).

The complementary role of different forms of official finance

No.	Type of financing	OECD Statistics reporting	Level of official subsidy involved (Scoring 0 – 5 of which 0 means no subsidy involved and 5 concerns the highest subsidy level)	Regulations to avoid "crowding out" (e.g. minimum pricing to avoid distortion of competition?)
1	Market based financing from domestic or international bank / capital markets	Domestic: Not available International: Private capital flows (1)	**Subsidy level: 0** The market provides financing; there is no official support involved.	Not applicable
2	Officially supported financing			
2A	Officially supported Export Credits supported / provided by official ECAs /EXIM banks	OOF	**Subsidy level: 1** Official support is provided, but there are no aid subsidies involved.	Yes, for officially supported export credits the OECD ECA minimum premiums apply, which are risk based.
2B	Officially supported Investment loans (not tied to exports, but tied to the nationality of investor) supported / provided by official ECAs / EXIM banks	OOF	**Subsidy level: 2-3** Official support is provided, but the level of official support is unknown, because there is no transparency on the pricing of investment loans	No, OECD ECA minimum premiums for officially supported export credits do formally not apply,
3	Official Development Finance provided by bilateral and multilateral DFIs			
3A	DFI market based investment loans for private sector borrowers	Bilateral DFIs: OOF Multilateral DFIs: non-concessional loans	**Subsidy level: 2-3** Official support is provided, but the level of subsidies is unknown, because there is a lack of transparency on the pricing of DFI loans. DFIs price their private sector loans market based, but there is a lack of transparency on the pricing practices.	No
3B	DFI "promotional loans" (non-concessional)	Bilateral DFIs: ODA or OOF depends on concessionality level of the loan Multilateral DFIs: Concessional loans or non-concessional loans depends on concessionality level of the loan	**Subsidy level: 4** Official support is provided. DFIs pass on their funding benefits to sovereign borrowers. Pricing is not risk based but subsidized and pricing practices differ among bilateral and multilateral DFIs for each DFI has its own pricing system.	No
3C	DFI concessional loans	Bilateral DFIs: ODA Multilateral DFIs: concessional loans	**Subsidy level: 5** Official support is provided. Loans are not risk based, but concessional and benefit from substantial aid subsidies	No
4	OECD tied aid credits	Bilateral DFIs: ODA	**Subsidy level: 5** Official support is provided. Min concessionality of 35% or 50% and DDRs for concessionality calculations	OECD tied aid rules in OECD "Arrangement on Officially Supported Export Credits apply, including a "commercial viability test"
5	ODA grants	Bilateral DFIs: ODA Multilateral DFIs: concessional	**Subsidy level: 5** The highest level of official support is provided.	No

Source: Sustainable Finance & Insurance

(1) It has to be mentioned that bank loans and other forms of debt financing (e.g. bonds) that benefit from guarantee support of ECAs, DFIs and specialised multilateral insurers are in current OECD statistics included in "private capital flows". This means that a substantial part of these flows is officially supported. This concerns in particular medium and long term commercial bank financing.

Multilateral or bilateral DFI investment loans for private sector borrowers are usually provided on market based terms, but unlike the ECAs, DFIs do not have a system of minimum risk based premiums. In this area DFIs compete with market financiers (without official support) and ECA supported loans and even among each other. "Unfair competition" caused by different pricing practices could be avoided if the DFIs would implement the OECD minimum premiums for trade related foreign currency denominated export or import financing[12]. It would therefore not apply to general DFI credit lines to local banks to encourage them to lend to certain parts of the economy in developing countries. (e.g. climate friendly investments, SME sector, microfinance). For many private sector oriented DFIs this credit line business concerns approximately 25% of their total lending to the private sector. Minimum premiums for trade related business would reduce the risk of private sector DFI loans crowding out other sources of finance that require no or less official support. For private sector oriented DFIs implementation of the OECD minimum premiums should also technically not be a problem, because they currently apply market-based rates. If needed, they can, like ECAs and EXIM banks, charge higher rates. The advantage of the OECD ECA minimum premiums is also that it will reduce pricing competition among DFIs. An issue is likely that most DFIs are not familiar wit the OECD minimum premium rates and do not like to be bound by (new) rules. On the other hand the OECD export credit rules are formally already applicable to bilateral DFIs if and when they support an export transaction from their home country. It may be the case that bilateral DFIs are not fully aware of the potential relevance of export credit regulations. It is therefore recommended that ECAs and DFIs work together to compare their pricing practices and experiences.

Promotional loans of bilateral DFIs and non-concessional preferential loans from MDBs, which in general are only provided to sovereign borrowers, have a larger subsidy component than the DFI private sector loans or ECA supported export credits. They may therefore potentially not only crowd our market based financing, but also these two other officially supported sources of finance. To avoid this from happening relevant DFIs and MDBs should check whether their more favourable financing terms are indeed required. It is also in the interest of bilateral DFIs and MDBs to harmonise their pricing practices for these preferential / promotional loans, because today they differ quite substantially from one another, resulting in pricing competition among the various providers of "promotional" development loans.

Bilateral ODA loans and concessional MDB loans have even a greater risk of crowding out other forms of finance for these loans involve a substantial higher aid subsidy. These funds should therefore only be used as "finance in last resort", when other sources of finance are not (adequately) available. In this way it can also be ensured that ODA is mainly provided to the least developed countries and low-income countries, which currently fall under the IMF / WB DSF.

This complementarity ranking could help official financiers, in particular bilateral and multilateral development financiers, to allocate their subsidized development financing only for those (parts of) projects and countries that truly require subsidized development financing. The suggested additionality check will contribute to aid efficiency and aid effectiveness and achievement of the UN SDGs.

An interesting additional tool that can be introduced to check potential distortion between (highly) subsidized development finance and market based finance or ECA export credits or market based DFI loans could be the so-called "commercial viability test" that has been developed for tied aid credits[13]. This test ensures that non-market based tied aid finance operates complementary to the market. A similar commercial viability test could be introduced for non-market based untied development finance. In this way it can be avoided that scarce non-market based funds are unintentionally

[12] Due to the lack of reliable data on trade related DFI financing the volume of such DFI business activities is unknown.
[13] See the OECD Arrangement on officially supported export credits.

crowding out private capital or public capital that involves less official support. The OECD DAC could benefit from the extensive "body of experience" of OECD export credit Participants with their discussions about tied aid eligibility.

A commercial viability test for non-market based untied aid will also contribute to define more precisely the complementary role of non-market based DFI finance (including ODA) and enhance the developmental impact of DFI operations. This is obviously of great importance to developing countries and the global SDG agenda.

VI. Conclusions

Enormous amounts of financing are needed to achieve the UN SDGS, which implies that a strong alignment of development finance with other forms of finance is critical. Mobilization of non-developmental sources of capital is important to achieve the UN SDGS. The discussion should not be limited to mobilizing private capital. There are important non-developmental sources of public capital that can be catalyzed. Non-developmental sources of capital cannot only be catalyzed for private sector projects, but also for public sector projects. A focus on "crowding in" other sources of capital requires a different mindset, incentives and business approaches of DFIs. Of equal importance is the question how "crowding out" of market based finance without support or official finance with substantial less official support can be avoided.

It is therefore very important that the OECD DAC starts with a fundamental discussion on the complementary role of ODA and other forms of development finance, both for the financing of public and private sector projects. For that purpose the OECD DAC should invite non-development financiers to the table. In this way it can be avoided that new ODA regulations will be developed that negatively affect private or other official (financial) flows to developing countries. Clarity on the complementary role of development finance is also critical to improve aid efficiency and aid effectiveness.

OECD members should therefore seriously consider applying the OECD ECA minimum premiums to:

(1) untied investment loans of EXIM banks and /or untied investment guarantees for debt financing of ECA insurers.
(2) Investment loans or guarantees for debt financing from both multilateral and bilateral DFIs for private sector projects.

Furthermore a commercial viability test could be introduced for non-market based development finance with relatively high subsidy levels. This could be used to assess the need for sovereign "promotional loans" and concessional loans. Concessional loans should preferably only be provided to countries that have no or limited access to market based finance or official finance that requires less official support. This includes amongst others the IMF/ WB DSF countries.

These suggestions could assist OECD DAC members and MDBs to enhance lending to those countries that really need ODA or other forms of officially supported development loans and improve the effectiveness and efficiency of their development finance activities.

ODA can be used for project development to increase the number of bankable projects. In this way ODA can contribute very effectively to the achievement of the UN SDGs.

Last, but not least: the OECD export credit and DAC member countries and the international DFI community should reach an understanding with non-OECD countries on both export credit and development finance (tied and untied aid) topics. For some non-OECD countries have become important official financiers of the SDG needs of developing countries. These non-OECD countries are currently not bound by international export credit and aid regulations. Both OECD and non-OECD providers of official finance should therefore work closely together on additionality of official finance. A global understanding on the complementary role of official finance is critical for the achievement of the UN SDGSs.

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