



## Financing Partnerships

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**INTERNAL**

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# Establishment of the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility

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**Asian Development Bank**

## ABBREVIATIONS

ADB	– Asian Development Bank
DMC	– developing member country
FPF	– financing partnership facility
FPFM	– financing partnership facility manager
GEATTF	– Global Energy Alliance for People and Planet Energy Access and Transition Trust Fund
IF-CAP	– Innovative Finance Facility for Climate in Asia and the Pacific
IPCC	– Intergovernmental Panel on Climate Change
MDB	– multilateral development bank
SDG	– Sustainable Development Goal
UN	– United Nations

## NOTE

In this report, “\$” refers to United States (US) dollars.

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## I. INTRODUCTION

1. Approval is requested to establish the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility (IF-CAP FPF or IF-CAP) and, in connection therewith, to:

- (i) Establish a multi-donor guarantee trust fund (IF-CAP Guarantee Trust Fund) under the IF-CAP FPF that will provide guarantees to the Asian Development Bank (ADB) covering payment defaults in respect of one or more synthetic portfolios of ADB sovereign loans. The guarantee of a portfolio of sovereign exposure will release parts of the capital currently allocated to that portfolio. With the released capital, ADB can then enter into a number of new sovereign and nonsovereign climate loans.
- (ii) Establish a multi-donor grant trust fund (IF-CAP Grant Trust Fund) under the IF-CAP FPF to support technical assistance, grant components of projects,<sup>1</sup> and other activities that may be agreed upon between the fund donors and ADB.
- (iii) Enter into a series of financing partnerships that comprise funded and unfunded guarantees or risk participations<sup>2</sup> under the IF-CAP FPF, pursuant to which official bilateral and multilateral sources and other financing partners—e.g., philanthropies, foundations, and other private sources—will provide, in parallel with the IF-CAP Guarantee Trust Fund, guarantees directly to ADB covering payment defaults in respect of one or more synthetic portfolios of ADB sovereign loans.<sup>3</sup> The guarantee of a portfolio of sovereign exposure will release parts of the capital currently allocated to that portfolio. With the released capital, ADB can then enter into new sovereign and nonsovereign climate loans.
- (iv) Establish other single- or multi-donor trust funds, framework arrangements, and other forms of financing partnerships—such as grants, guarantees, and similar arrangements—that support the objectives and scope of the IF-CAP FPF as described in this paper.
- (v) Accept and administer contributions by official bilateral, multilateral, and private sources to each trust fund, and other financing partnership arrangements (including guarantees) established or entered into under the IF-CAP FPF.<sup>4</sup>

2. ADB's ambition is to reach \$100 billion in climate financing<sup>5</sup> by 2030 to support the development of economies with net zero emissions and climate resilience. The IF-CAP FPF is an omnibus vehicle designed to expand ADB's lending headroom for climate financing through its IF-CAP Guarantee Mechanism (footnote 3), and to supplement ADB's climate financing efforts through grant funding. The IF-CAP FPF will demonstrate an innovative way of mobilizing financial

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<sup>1</sup> The reference to "projects" in this paper intends to include all financing modalities offered by ADB.

<sup>2</sup> The reference to "guarantees" from financing partners in this paper includes funded and unfunded guarantees, guarantee-like instruments such as risk participations, promissory notes, and/or similar arrangements.

<sup>3</sup> Since they are intended to work in conjunction with each other, the IF-CAP Guarantee Trust Fund and the guarantees or risk participations from official bilateral and/or multilateral sources and other financing partners—including philanthropies, foundations, and other private sources—are referred to collectively in this paper as the "IF-CAP Guarantee Mechanism." Synthetic portfolios used in this context are defined in para. 16.

<sup>4</sup> The IF-CAP FPF requires Board approval because (i) it has an indicative funding target exceeding \$200 million across all the financing platforms contemplated under the facility (para. 13), and (ii) presents a novel design and complexity (paras. 11 and 61). See also para. 51(i)(b) and (c) of ADB. [Enhancing Operational Efficiency of the Asian Development Bank](#). 2015. Manila.

<sup>5</sup> "Climate financing" in this paper includes climate mitigation, climate adaptation, and enhanced climate resilience projects, and shall include all projects aligned with the Climate Change Action Plan to be adopted by ADB before the end of 2023.

resources immediately, and will play a key role in the broader range of efforts to strengthen ADB's financial capacity to accelerate climate action.

3. This paper describes the overall concept of the IF-CAP FPF and details the IF-CAP Guarantee Trust Fund, the IF-CAP Grant Trust Fund, the direct guarantees or risk participations from financing partners, and other proposed financing partnerships arrangements for which approval is sought.

## II. BACKGROUND AND RATIONALE

4. **Climate change and the stakes for Asia and the Pacific.** Climate change has far-reaching consequences for human well-being and economic growth. Home to more than half of the world's population,<sup>6</sup> Asia and the Pacific is facing more frequent and wide-ranging climate-related challenges than most other regions. This has translated into significant human and economic loss. More than 40% of climate-related disasters have occurred in the region since the start of the 21st century, affecting nearly 3.6 billion people and causing almost 0.9 million deaths.<sup>7</sup> Rising temperatures, increased frequency and intensity of extreme weather events, and rising sea levels are among the main climate-related triggers and threaten human and physical assets, especially since populations across Asia and the Pacific are concentrated in coastal and urban areas. It is estimated that about 1 billion more people will inhabit urban areas by 2050, with exposure to elevated air pollution and urban heat. The number of people potentially affected by rising sea levels and storm surges will increase accordingly, given the substantial number of urban centers in and around coastal areas.<sup>8</sup> Developing member countries (DMCs) have experienced physical losses worth billions of dollars because of climate-related events. In 2020 alone, the region faced a disaster loss of \$67 billion.<sup>9</sup> Estimates suggest that the increase in annual losses will outpace gross domestic product growth in Asia and the Pacific, if left unaddressed.<sup>10</sup> The region's exposure to climate change is thus substantial, and the poor are being the most vulnerable.<sup>11</sup>

5. **Unlocking local action for global results.** While Asia and the Pacific is heavily affected by climate change, it has also become a major contributor to the global climate crisis. About one-third of global greenhouse gas emissions originate in the People's Republic of China, India, and Indonesia alone,<sup>12</sup> and overall, about 40%–45% of global greenhouse gas emissions come from Asia and the Pacific.<sup>13</sup> Emissions have been rising in the region since the start of the century as rapid economic growth led to increased fossil fuel consumption across key economic sectors like energy, transport, and carbon-intensive manufacturing. The share of coal in the regional energy mix is particularly high at more than 70%,<sup>14</sup> contributing to air pollution and global warming. Indeed, de-fossilizing development pathways is part of the goal towards building a prosperous, inclusive, sustainable and resilient Asia and the Pacific. It is therefore crucial to address climate change in Asia and the Pacific, and take measures that help reduce the overall global carbon

<sup>6</sup> United Nations Population Fund. 2023. [Asia and the Pacific – Population trends](#). Bangkok.

<sup>7</sup> Centre for Research on the Epidemiology of Disasters. 2023. [Emergency Events Database \(EM-DAT\)](#). Louvain.

<sup>8</sup> ADB. 2017. [A Region at Risk – The Human Dimension of Climate Change in Asia and the Pacific](#). Manila.

<sup>9</sup> Munich Re. 2021. [Record Hurricane Season and Major Wildfires – The Natural Disaster Figures for 2020](#). Munich.

<sup>10</sup> ADB. 2020. [Financing Disaster Risk Reduction in Asia and the Pacific](#). Manila.

<sup>11</sup> Women are more vulnerable to the effects of climate change mainly because they constitute a larger proportion of the poor, and they are more dependent on the available natural resources for their livelihoods.

<sup>12</sup> World Resources Institute. 2023. [Climate Watch](#). Washington, DC.

<sup>13</sup> Intergovernmental Panel on Climate Change (IPCC). 2022. [Climate Change 2022. Mitigation of Climate Change. Summary for Policymakers](#). Geneva.

<sup>14</sup> International Energy Agency. 2019. [Fading fast in the US and Europe, Coal still reigns in Asia](#). Paris.

footprint. Locally, climate action will bring about a double effect by reducing both the causes and impacts of climate change at the same time.

6. **Advancing climate action before 2030.** Delays in advancing climate action will lead to more severe climate impacts as well as substantial costs. Therefore, delivering on the targets set in the Paris Agreement<sup>15</sup> and the Sustainable Development Goals (SDGs) of the United Nations (UN)<sup>16</sup> is time-critical. Given the global lag in meeting the climate targets, the Intergovernmental Panel on Climate Change (IPCC) projects that 2030 will be a crossroads year after which it will become considerably harder to meet the climate targets, unless efforts are drastically accelerated before 2030.<sup>17</sup> ADB is fully committed to delivering climate action within the 2030 time horizon. It will fully align its operations with the Paris Agreement by 2025 at the latest (and 100% of its sovereign operations already by July 2023)<sup>18</sup>, and scale up climate finance to at least \$80 billion by 2030,<sup>19</sup> with an ambition to reach \$100 billion from its own resources by then.<sup>20</sup> In addition, it is committed to having 75% of its operations supporting climate change by 2030. ADB has delivered \$21 billion in cumulative climate finance from 2019-2022. Yet, the sheer scale and complexity of climate change will require technical and financial support and collaboration at all levels, including from and with external partners, to ensure a sustainable and climate-friendly pathway for development in Asia and the Pacific.

7. **Need for climate finance to fill funding gap.** Combating climate change comes at extraordinary costs because of the scale, urgency, and complexity of the climate crisis. ADB estimated that, between 2016 and 2030, \$1.7 trillion per year will need to be invested in infrastructure in developing Asia to ensure that both climate and development goals will be met. This translates into investments of 5%–9% of gross domestic product on average, depending on the subregion.<sup>21</sup> With the global coronavirus pandemic waning and public budgets in distress, financing needs are even more urgent. Mobilizing capital of this magnitude will require collective action from both the public and private sectors, as well as innovative financing mechanisms and upstream reforms to close the funding gap. ADB estimates that, on average, every dollar invested in resilience will save \$4–\$7 in disaster response.<sup>22</sup> Hence, investing in climate adaptation and mitigation as quickly as possible and at scale is vital.

8. **Innovative financing from multilateral development banks.** Multilateral development banks (MDBs) such as ADB have an important mandate to ensure that financing is adequately available and well accessible to manage the transition to a climate-friendly future within the DMCs. To this end, ADB has made climate change one of four key shifts of its recent organizational review.<sup>23</sup> Moreover, the Group of 20 (G20), under the leadership of the Indonesian presidency, commissioned an expert panel to review MDBs' capital adequacy frameworks and recommend steps to optimize the approach. This panel identified, among other steps, that MDBs should

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<sup>15</sup> UN. 2015. [Paris Agreement](#). Paris.

<sup>16</sup> UN. [Sustainable Development Goal 13](#) and [Sustainable Development Goal 17](#). New York.

<sup>17</sup> IPCC. 2022. [Climate Change 2022. Mitigation of Climate Change. Summary for Policymakers](#). Geneva.

<sup>18</sup> ADB. [President's Vision Statement – Summary and Highlights](#). Manila.

<sup>19</sup> ADB. 2018. [Strategy 2030](#). Manila.

<sup>20</sup> ADB. 2021. [ADB Raises 2019–2030 Climate Finance Ambition to \\$100 Billion](#). Manila.

<sup>21</sup> Pacific: 9.1%; South Asia: 8.8%; Central Asia: 7.8%; Southeast Asia: 5.7%; East Asia: 5.3%. ADB. 2017. [Meeting Asia's Infrastructure Needs](#). Manila.

<sup>22</sup> ADB. 2020. [Financing Disaster Risk Reduction in Asia and the Pacific](#). Manila.

<sup>23</sup> ADB. 2022. [Organizational Review. A new Operating Model to accelerate ADB's Transformation toward Strategy 2030 and beyond](#). Internal Document. Manila.

explore innovative models to leverage financial resources and increase their exposures through risk sharing or other means.<sup>24</sup>

9. **Strategic alignment.** The proposed IF-CAP FPF is aligned with ADB's Strategy 2030 and its operational plan for priority 3 (tackling climate change, building climate and disaster resilience, and enhancing environmental sustainability);<sup>25</sup> SDG 13 (take urgent action to combat climate change and its impacts); SDG 17 (strengthen the means of implementation and revitalize the Global Partnership for Sustainable Development); and the Paris Agreement. Given ADB's corporate commitment to achieve at least 75% of committed operations promoting gender equality as part of ADB's Strategy 2030, the facility is also aligned with SDG 5 (achieve gender equality and empower women and girls).<sup>26</sup> IF-CAP will complement existing trust funds with a focus on climate change, such as the Clean Energy Financing Partnership Facility, but will be wider in scope in that it covers a broad range of sectors as opposed to funds that are sector-specific.

### III. OBJECTIVES

10. IF-CAP's primary objective is to mobilize, both directly and indirectly, climate finance at scale to provide needed funding for climate action to its DMCs through its guarantee and grant mechanisms.

11. The IF-CAP Guarantee Mechanism will enhance ADB's lending capacity through financial leverage and create lending headroom for new climate mitigation and adaptation projects across Asia and the Pacific. The additional headroom will enable ADB to accelerate its climate support to DMCs, while ensuring development needs are equally met. The leverage effect makes IF-CAP an innovative tool allowing ADB to be one of the first movers in following the global call to increase climate finance and implement the Group of 20's capital adequacy recommendations to introduce innovative financing (para. 8).

12. The IF-CAP grant mechanism will be used to facilitate project preparation, capacity building, and knowledge solutions. Subject to meeting an appropriate minimum level of grant contributions, the IF-CAP Grant Trust Fund may also be used to support grant components of projects or, blended with parallel loans, to reduce the cost and risk of high-impact climate projects.

13. The ambition for IF-CAP FPF's overall size is \$3 billion across all trust funds and other forms of financing partnerships contemplated as part of the facility. As such, IF-CAP is expected to be one of ADB's key financing vehicles to help ADB meet, and possibly exceed, its ambition of reaching \$100 billion in cumulative climate financing from 2019 to 2030. Through IF-CAP, ADB is providing a core example of a regional public good that can be replicated across other MDBs and regions.

### IV. SCOPE

14. The IF-CAP FPF is an operational arrangement to enhance the coordination and administrative efficiency of partnership activities. It will be an umbrella mechanism that helps

<sup>24</sup> Independent Expert Panel. 2022. [Boosting MDBs' Investing Capacity. An Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks](#). Bali. In particular, Recommendation 3C of the panel's report encourages "shareholder guarantees of sovereign repayments on loans related to cross-cutting priorities." The report highlights the International Finance Facility for Education (IFFEd) as an innovative example for achieving leverage through a guarantee and grant mechanism which served as a model in the design process of IF-CAP.

<sup>25</sup> ADB. 2019. [Strategy 2030. Operational Plan for Priority 3](#). Manila.

<sup>26</sup> UN. [Sustainable Development Goal 5](#). New York.



mobilize resources for eligible public and private sector projects to support climate adaptation and mitigation in accordance with ADB's climate agenda, and related policies and financing targets, as well as any other activities that may be agreed upon between financing partners and ADB. IF-CAP will finance projects during an initial 5-year investment period. Guarantees will remain effective for a total of 25 years (5-year investment period plus 20 years, corresponding to the average term of ADB loans). Figure 1 provides a concept overview of the IF-CAP FPF.

15. **IF-CAP Guarantee Mechanism.** Financing partners issuing guarantees or other guarantee-like instruments within the IF-CAP FPF (including through the IF-CAP Guarantee Trust Fund) will agree to guarantee synthetic reference portfolios of ADB sovereign loans.<sup>27</sup> In the event of non-accrual<sup>28</sup> by a DMC that is part of a reference portfolio, the financing partners guaranteeing such reference portfolio will pay ADB the due amounts from the DMC, subject to their respective guarantee coverage<sup>29</sup> limits or until the aggregate first-loss (if any) has been exhausted.<sup>30</sup> The main guarantee types can either be a "pari passu guarantee," where losses are shared proportionally between guarantors and ADB, or a "first-loss guarantee," where losses are fully covered up to predetermined amounts by the guarantors.

16. Notwithstanding the guarantees to be provided by financing partners through the IF-CAP Guarantee Mechanism, ADB will at all times remain the lender of record for all loans covered in the reference portfolios. The reference portfolios will be synthetic and as such will not identify specific ADB loans; instead, they will specify the respective amounts of exposure to the ADB sovereign borrowers included in the portfolio on a synthetic basis. Upon a default on any loan by any DMC borrower, ADB could demand payment from the financing partners whose guaranteed reference portfolio comprises exposure to such DMC. The timelines and payment terms shall be agreed between ADB and the financing partners. ADB will continue to be the lender of record before and after any payment by the financing partners, and will apply its normal process in collecting due and unpaid amounts from the defaulting ADB sovereign borrower. To the extent that ADB subsequently receives payments from the defaulting ADB sovereign borrower, ADB intends to reflow such funds to the financing partners that paid under their respective participations, promptly after ADB receives such payments from the ADB sovereign borrower.

17. **Generation of new projects under the guarantee mechanism.** With guarantors stepping in to shoulder a non-accrual event, ADB can free up the capital it previously allocated to such reference portfolios, creating headroom for new sovereign and nonsovereign lending that supports climate action. The extent to which capital can be released is contingent on various factors such as the creditworthiness and size of the reference portfolios, the credit quality of

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<sup>27</sup> The loans underlying the synthetic portfolios (para. 16) are anticipated to primarily comprise existing ADB sovereign loans. However, depending on the operational mandates and requirements of particular financing partners, guarantees may also be provided for an identified package of new sovereign loans to be engaged in after entering into a guarantee arrangement with the financing partner.

<sup>28</sup> In relation to ADB sovereign loans, non-accrual refers to a payment default that remains outstanding for 180 days. Payment defaults under the IF-CAP Guarantee Mechanism may include non-payment of all or a combination of principal, interest, and/or commitment charges under sovereign loans.

<sup>29</sup> Payouts from financing partners, upon default in any reference portfolio, will be made on a pari-passu and pro rata basis across all the financing partners guaranteeing such reference portfolio, subject to any applicable first-loss or second-loss arrangements.

<sup>30</sup> ADB may also seek to incorporate insurance coverage as part of the overall structure of the IF-CAP Guarantee Mechanism, pursuant to which third-party insurers will cover specified losses on the guarantee portfolio (either on a first-loss basis before payouts by the guarantors or on a second-loss basis, covering a portion of defaulted amounts that exceed the coverage provided by guarantors).

donors, and the type and amount of guarantee received by ADB.<sup>31</sup> The IF-CAP Guarantee Mechanism is therefore an innovative leverage tool<sup>32</sup> that enables ADB to enhance its lending capacity to an extent that would not be possible with ADB's existing resources alone. Guarantees will be accepted through the IF-CAP Guarantee Trust Fund (para. 21) and/or through bilateral financing partnerships (para. 26).

18. **IF-CAP grants.** Grants will support project preparation, capacity building, and knowledge solutions. They may also be used to support grant components of projects or to reduce the cost and risk of high-impact climate projects, subject to minimum threshold contributions being achieved. Grants will be accepted through the IF-CAP Grant Trust Fund (para. 22) and/or any other multi-donor or single-donor trust fund under the IF-CAP FPF.

19. **Eligible financing partners.** ADB will accept contributions under the IF-CAP FPF from official bilateral and multilateral sources and other financing partners,<sup>33</sup> including philanthropies, foundations, and other private sources.

20. **Facility structure.** The following describes the trust funds and other forms of financing partnerships under the IF-CAP FPF through which eligible financing partners can provide guarantees and/or grants. Funds received or generated under the IF-CAP FPF will be allocated according to the project eligibility criteria (paras. 29–33) established through IF-CAP's governance structure (para. 43), except in the case of single-donor grant trust funds under the IF-CAP FPF that will allocate funds according to their own governance decisions (para. 24).

#### A. Multi-Donor Trust Funds

21. **IF-CAP Guarantee Trust Fund.** The IF-CAP Guarantee Trust Fund is a multi-donor trust fund under the IF-CAP FPF with ADB as its manager and administrator. Financing partners may issue guarantees to the trust fund either in cash payable upfront<sup>34</sup> and/or in form of contingent contributions payable upon a default in a guaranteed reference portfolio. The guarantees accepted through the IF-CAP Guarantee Trust Fund will allow ADB to free up lending headroom for projects in line with the IF-CAP Guarantee Mechanism (paras. 15–17) and project eligibility criteria (paras. 29–33).

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<sup>31</sup> The release of capital will also depend on whether the reference portfolios comprise existing ADB sovereign loans, or sovereign loans to be engaged in after entering into the guarantee (which may be a requirement of certain financing partners). To the extent that guarantees are provided for existing loans, the release of capital will be immediate, while in the case of guarantees for new loans, the release will be gradual based on disbursements under the loans.

<sup>32</sup> The IF-CAP FPF will be the first time ADB employs a guarantee mechanism for its sovereign loans at scale and as part of a financing partnership arrangement. It is a structurally novel tool, and reflects technical, legal, and other complexities that will require significant time and resources to establish and implement. Financial leverage is defined as the amount of new lending that ADB can undertake relative to the size of the guarantees it has received through IF-CAP.

<sup>33</sup> ADB will not accept contingent contributions to the IF-CAP Guarantee Mechanism from private sources, given the risk that private sources may not be able to maintain a suitable credit rating for the full 25-year guarantee term.

<sup>34</sup> Official bilateral sources contributing to the IF-CAP Guarantee Trust Fund may provide cash in the form of a "soft loan" made to the IF-CAP Guarantee Trust Fund. Repayment of the loan will rely solely on the assets of the IF-CAP Guarantee Trust Fund, and the contributors will have no recourse to ADB's own assets (including ADB's ordinary capital resources). The loan will be a zero-interest loan, with a maturity matching the average maturity of the new climate loans to be financed with the leveraged capital release. The principal of the loan will be repaid after deducting any obligations by the IF-CAP Guarantee Trust Fund to ADB to cover non-payments in the reference portfolio. The loan documentation between the lender and IF-CAP Guarantee Trust Fund will envisage that the principal may not be repaid if there is a default in the reference portfolio.

22. **IF-CAP Grant Trust Fund.** The IF-CAP Grant Trust Fund is a multi-donor trust fund under the IF-CAP FPF with ADB as its trustee and administrator. Financing partners contribute cash grants to facilitate project preparation, capacity building, and knowledge solutions through technical assistance. Grants may also be used to contribute to the financing of projects or to reduce the cost and risk of high-impact climate projects. Operations supported through the IF-CAP Grant Trust Fund will be in line with the project eligibility criteria (paras. 29–33).

23. **Other multi-donor trust funds.** Any other multi-donor trust funds alongside those specified above may be established or made part of the IF-CAP FPF provided that these funds support the IF-CAP objectives.

## B. Single-Donor Trust Funds

24. **Global Energy Alliance for People and Planet Energy Access and Transition Trust Fund (GEATTF).** The GEATTF is a single-donor trust fund to be housed under the IF-CAP FPF after its establishment.<sup>35</sup> The GEATTF is a grant-concessional finance trust fund to accommodate philanthropic capital,<sup>36</sup> providing climate finance in form of technical assistance, grant components of investment projects, and other concessional lending instruments. It supports renewable energy and energy transition projects to promote affordable and reliable energy access to poor and vulnerable populations. It has its own governance structure and criteria for fund allocation and as such will be housed under the IF-CAP FPF as an autonomous fund, while working toward achieving objectives aligned with the IF-CAP FPF.

25. **Other single-donor trust funds.** Other single-donor grant trust funds may join the IF-CAP FPF provided that their mandate supports the IF-CAP objectives.

## C. Bilateral Financing Partnerships

26. **Direct guarantees.** As part of the IF-CAP Guarantee Mechanism, ADB can form bilateral partnerships to accept guarantees, risk participations, or similar types of instruments or arrangements. In such partnerships, financing partners issue guarantees directly to ADB without an intermediary trust fund. Their contributions will be contingent and payable upon a default in their respective guaranteed portfolios. As with the guarantee provided through the IF-CAP Guarantee Trust Fund, direct guarantees will allow ADB to free up lending headroom for projects in line with the guarantee mechanism (paras. 15–17) and eligibility criteria (paras. 29–33).<sup>37</sup>

## D. Other ADB Funds

27. Stipulated contributions from any other ADB funds may be coursed through, or in parallel with, the IF-CAP FPF to support the IF-CAP objectives and scope. Any other ADB funds may become part of or be associated with the IF-CAP FPF umbrella if these funds support the IF-CAP objectives and scope.

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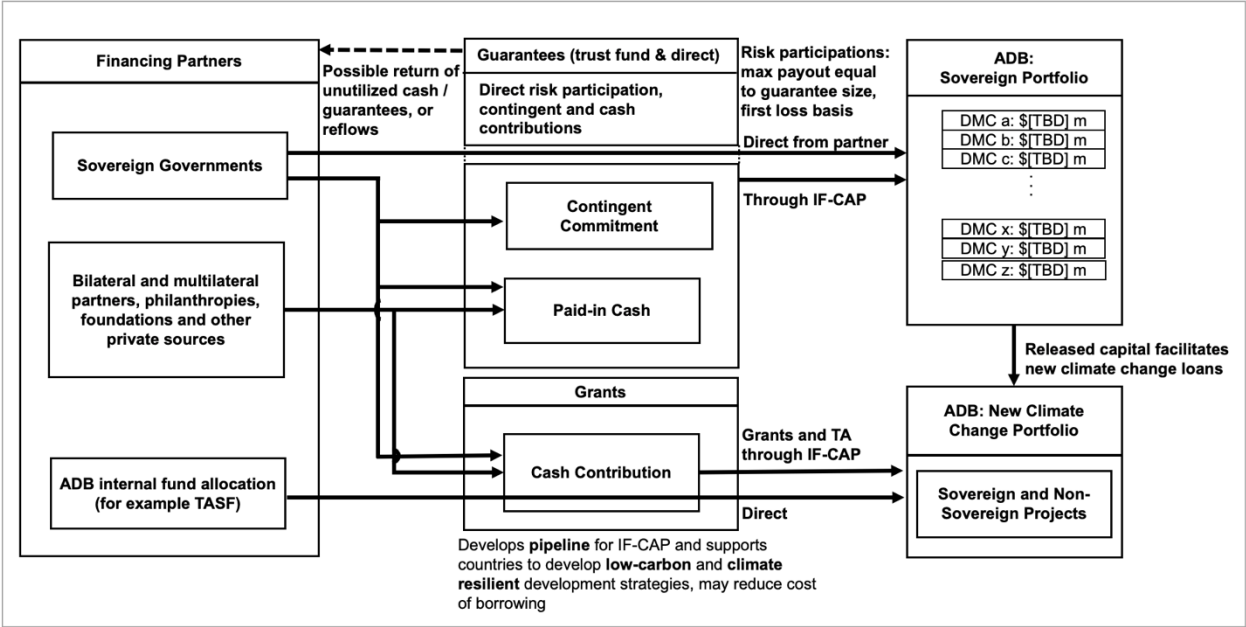
<sup>35</sup> Establishment is scheduled to take place before the end of 2023.

<sup>36</sup> From [Rockefeller Foundation](#), [IKEA Foundation](#) and [Bezos Earth Fund](#)

<sup>37</sup> It is anticipated that the direct financing partner guarantees will generally be made in parallel with the guarantees under the IF-CAP Guarantee Trust Fund providing coverage for common reference portfolios. Accordingly, payouts upon default in a reference portfolio will be made on a pari-passu and pro rata basis across all the guarantees provided in respect of such reference portfolio, subject to any first- or second-loss arrangements for such a portfolio.

28. **Parallel activities in support of IF-CAP.** Financing partnerships supporting IF-CAP’s objectives in tandem with the IF-CAP FPF may include parallel or joint cofinancing of lending and non-lending assistance, including concessional loan packages and/or any other suitable types of cofinancing and/or any other form of assistance and/or collaboration supporting the objectives and scope of the IF-CAP FPF.

Figure 1: IF-CAP FPF Concept Overview



ADB = Asian Development Bank, DMC = developing member country, IF-CAP = Innovative Finance Facility for Climate in Asia and the Pacific, m = million, TA = technical assistance, TASF = Technical Assistance Special Fund, TBD = to be determined.

Source: Asian Development Bank.

29. **Eligibility criteria.** The use of IF-CAP resources from the IF-CAP Grant Trust Fund, the IF-CAP Guarantee Trust Fund, and the direct guarantees will be subject to specific eligibility criteria. The following describes the general principles for the use of these funds, which may be amended following the guidance of the Strategic Partners Forum (para. 44) and the Donor Committee (paras. 45-47).

30. **Eligible members.** All DMCs are eligible for IF-CAP support. This includes all DMC entities eligible to receive assistance from ADB, whether public or private.

31. **Types of projects.** ADB will select project proposals based on criteria agreed with the Donor Committee. Projects shall be generally aligned with the Paris Agreement and the key objectives of pertinent ADB strategies and policies, such as the ADB Climate Change Action Plan (to be adopted before the end of 2023) and Strategy 2030. IF-CAP will not support new fossil-fuel-based electricity generation facilities. Both sovereign and nonsovereign projects shall, in principle, have access to IF-CAP funding unless otherwise decided by the Donor Committee. The Donor Committee may introduce any other project criteria in lieu of or in addition to the ones mentioned in this paragraph.

32. Assistance from the IF-CAP FPF may be combined with other ADB resources and forms of bilateral or multilateral assistance, such as other dedicated funds, to provide the most effective support of IF-CAP objectives. Activities may be implemented in DMCs or other countries in

accordance with applicable ADB requirements and procedures. Assistance may be made available directly or indirectly to central and local governments, government agencies, the private sector, and other entities eligible to receive assistance from ADB. Resources from IF-CAP will be used to finance eligible projects following ADB's applicable guidelines and procedures. Activities to be supported by IF-CAP will be identified, designed, processed, approved, and implemented in accordance with applicable ADB policies, procedures, and guidelines, including consulting services and procurement, social and environmental safeguards, financial management and reporting, and anticorruption measures and governance. Recipients of financing from IF-CAP must ensure that such financing will be used for its intended purpose on the same terms, conditions, and principles as set forth in this paper.

33. **Supported modalities.** To maximize climate impact, the IF-CAP FPF may, in principle, support projects under all ADB financing modalities, including policy-based lending, unless the Donor Committee decides otherwise.

## V. CONTRIBUTION AMOUNTS AND FUND TRANSFER ARRANGEMENTS

34. The IF-CAP FPF will primarily accept contributions in the form of guarantees (either through the IF-CAP Guarantee Trust Fund or through individual guarantees from bilateral sources entered into directly with ADB) and grants (through the IF-CAP Grant Trust Fund or other single-donor and multi-donor grant trust funds established or positioned within the IF-CAP FPF). IF-CAP may also accept other forms of contributions that enhance ADB's lending capacity<sup>38</sup> or enable low-cost borrowing.

35. To ensure cost-effective processing as well as equality among participants, to facilitate economies of scale, and to reflect the material demand for climate finance, the Donor Committee (paras. 45–47) and ADB will establish minimum contributions to each multi-donor trust fund under the IF-CAP FPF, as well as minimum thresholds for combined contributions to trust funds and other financing partnerships under the IF-CAP FPF, except for single-donor trust funds and financing partnerships other than the IF-CAP Grant Trust Fund, the IF-CAP Guarantee Trust Fund, and direct guarantees. Contributions will be held and administered by ADB.

36. Contributions to financing partnerships under the IF-CAP FPF will use trust fund contribution agreements and/or instruments of contribution and/or other agreements depending on the type of contribution, or a combination thereof,<sup>39</sup> whereby the respective financing partners will agree to contribute to the IF-CAP FPF substantially in accordance with the terms set forth in this paper, and through which they may specify any policy restrictions and development priorities applicable to the lending unlocked from their contributions.

37. Cash and contingent contributions to the IF-CAP FPF will be made in a freely convertible currency. Cash contributions and contingent contributions, once called, will be deposited into United States (US) dollar accounts (the Accounts) to be specified by ADB. For contributions received in currencies other than the US dollar, ADB will, upon receipt of the funds, convert them into US dollars and transfer them to the Accounts.

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<sup>38</sup> These include guarantee-like instruments such as risk participations, promissory notes, and/or similar arrangements.

<sup>39</sup> It is envisaged that guarantee and guarantee-like instruments from official bilateral and/or other sources will be documented through guarantee, risk participation, or similar agreements to be entered into directly between ADB and such source. Since it is anticipated that most such agreements will be made on a pro rata and pari-passu basis among the financing partners covering a common reference portfolio, the agreements are anticipated to incorporate common terms applying to all the financing partners, setting out the terms upon which guarantees may be called, subject to first-loss or second-loss arrangements, if applicable.

38. Contributions may also be made through the redirection of available funds under existing externally financed funds in ADB's trust, subject to the agreement of the respective financing partners.

39. Commitments by a financing partner will be untied and not be subject to any conditions, except as provided in this paper and in the implementation guidelines to be prepared. By depositing an instrument of contribution or by signing a trust fund contribution agreement or a similar agreement substantially on the terms and conditions set forth in this paper, the financing partner will be deemed to have accepted the objectives outlined, and the terms and conditions set forth, in this paper.

40. Contributions will be held, administered, and invested at the discretion of ADB in accordance with ADB's policies and procedures. Pending disbursements, ADB may invest and reinvest contributions. Any income earned in respect of such investment and reinvestment, as well as interest accrued in respect of each of the Accounts will be credited to the relevant Account and used for the purposes of the respective fund, including related administration costs.<sup>40</sup> Any losses from the investment portfolio will be charged to the relevant Account.

41. ADB will make disbursement from the relevant Account as necessary to meet the expenditures of projects and activities supported by the relevant trust fund. If other currencies are required for payment to meet eligible expenditures, ADB may purchase the required currencies with the available funds. Any fees and charges relating to such purchase will be paid out of the relevant Account.

42. With respect to funds provided by financing partner(s), ADB will exercise the same degree of care in the discharge of its functions as the trustee as it does with respect to its administration of other external financing resources, and will have no further liability in respect of the contributions.

## VI. ADMINISTRATIVE ARRANGEMENTS

43. **Governance structure.** IF-CAP will be governed by a Strategic Partners Forum, a Donor Committee, a financing partnership facility manager (FPFM), a secretariat, and the ADB Guarantee Committee. Figure 2 below illustrates the governance structure.

44. **Strategic Partners Forum.** The Strategic Partners Forum will gather DMCs, financing partners and other relevant stakeholders to provide strategic guidance on IF-CAP operations with a view to align climate and development needs with available funding. The Strategic Partners Forum will be co-chaired by a representative from the DMCs and a representative from the financing partners. The Strategic Partners Forum will be a highly visible platform organized annually and, where possible, back-to-back with flagship events or similar gatherings to ensure the forum's inputs will effectively reach decision-makers. The Strategic Partners Forum will also offer a unique opportunity to share knowledge and lessons.

45. **Donor Committee.** Taking the Strategic Partners Forum's guidance into consideration, the Donor Committee will take decisions on matters including specific guarantee and grant fund considerations, IF-CAP structure and governance. The Donor Committee will thus set the general

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<sup>40</sup> Administration costs include ADB's service fees, cost of external audits, and finance charges that may be incurred in connection with purchasing required currencies and remitting funds.

framework for operating the IF-CAP FPF and as such will not engage in areas of implementation such as the selection or processing of individual projects. The Donor Committee's mandate does not cover decisions in relation to single-donor trust funds and financing partnerships other than the IF-CAP Grant Trust Fund, the IF-CAP Guarantee Trust Fund, and direct guarantees.

46. The Donor Committee will be chaired by ADB and co-chaired by one of IF-CAP's financing partners<sup>41</sup> selected through a method decided by the Donor Committee. The remaining financing partners will be Donor Committee members or observers. Members shall have decision-making rights unless otherwise decided, while observers may follow Donor Committee discussions without taking part in formal decision-making. All financing partners shall have decision-making rights, except for single-donor trust fund contributors who are subject to an alternative governance structure.

47. ADB will generally abide by the decisions taken by the Donor Committee but shall promptly inform the financing partners of any condition that interferes, or threatens to interfere, with ADB's strategies, policies, and/or other major directions.

48. **Financing partnership facility manager.** The FPFM's core responsibility is to run IF-CAP's operations in accordance with the guidance from the Strategic Partners Forum and the decisions taken by the Donor Committee, particularly in relation to the use of IF-CAP resources. The FPFM will thus be responsible for technical review and project selection, and must ensure that IF-CAP support is provided in line with the project eligibility criteria as prescribed by the Donor Committee. The FPFM will be supported by ADB staff with sector and thematic expertise for the technical review of projects. The FPFM will also have a central liaison and coordination function with the Strategic Partners Forum and Donor Committee on the one hand and ADB's operations departments on the other. A qualified ADB staff member will be designated to serve as the FPFM.

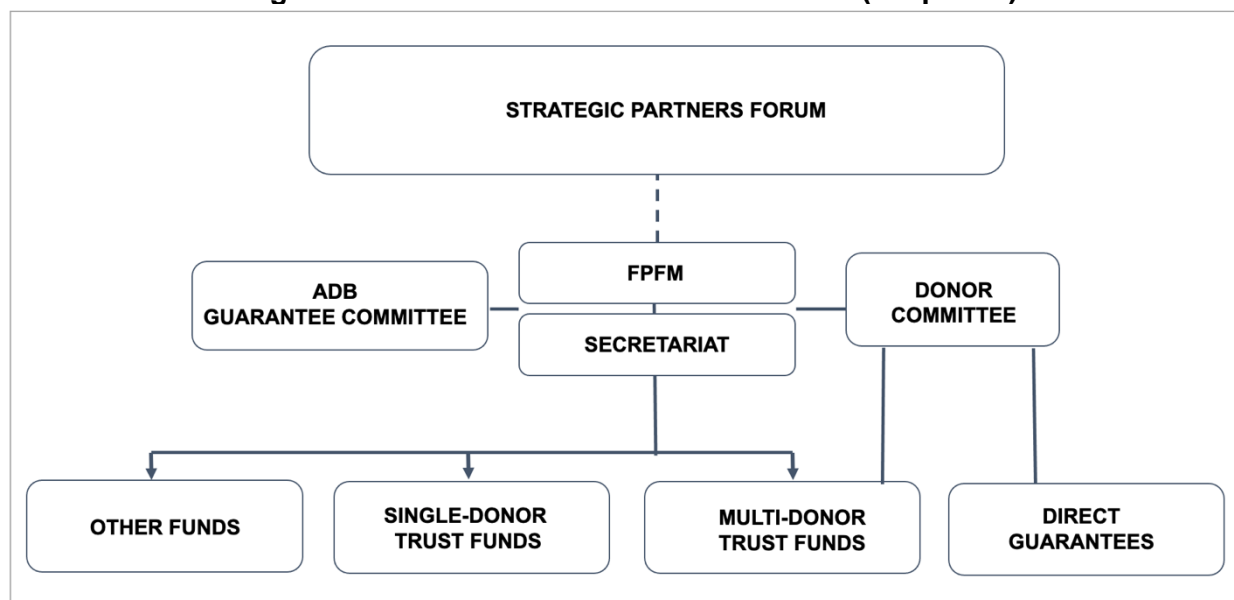
49. **Secretariat.** The secretariat will manage the day-to-day operations of IF-CAP. It will be housed in ADB. It will perform tasks in relation to the administration of the FPF, conduct project monitoring and reporting, arrange the Strategic Partners Forum and Donor Committee meetings, and perform any other duties to ensure the functioning of the IF-CAP FPF as mandated by the governing bodies. The secretariat will be staffed with qualified ADB staff and may be supported by financing partners' secondees, externally funded staff, and consultants.

50. **ADB Guarantee Committee.** The ADB Guarantee Committee will be the focal point for guarantee portfolio monitoring and provide advice on loan default matters and eventual calls on guarantees. The committee will be composed of qualified staff from ADB's Office of Risk Management, Sustainable Development and Climate Change Department, Controller's Department, Office of the General Counsel, Treasury Department, operational departments concerned, and any other department.

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<sup>41</sup> In addition to contributors to the IF-CAP Grant Trust Fund and IF-CAP Guarantee Trust Fund, it will also include financing partners that enter into bilateral guarantees with ADB.

**Figure 2: IF-CAP FPF Governance Structure (simplified)**



ADB = Asian Development Bank, DMC = developing member country, FPFM = Financing partnership facility manager.  
Source: Asian Development Bank.

51. **Implementation guidelines.** The administration of the IF-CAP FPF is governed by the implementation guidelines to be prepared by the FPFM and approved by the Donor Committee on or before the first fund allocation. The guidelines will specify measurable indicators against which IF-CAP's performance will be monitored. The guidelines will be amended from time to time to reflect revisions in IF-CAP's operations. The Donor Committee approves any changes or amendments, and the FPFM communicates the changes and amendments to all ADB user departments concerned. ADB may, from time to time, adopt additional rules for managing and administering the IF-CAP FPF, to be substantially based on the terms and conditions of this paper.

52. **Applications.** The department seeking funds under the IF-CAP FPF applies to the FPFM. The FPFM will review the applications, select qualifying projects, and follow any associated procedures as established in the implementation guidelines.

53. **Reporting requirements.** The FPFM, in consultation with the respective departments, will submit to the Donor Committee the

- (i) IF-CAP annual work program,
- (ii) IF-CAP annual performance report, and
- (iii) financial statements for each trust fund under the IF-CAP FPF.<sup>42</sup>

54. ADB will maintain the records and accounts for the trust funds and other financed activities under the IF-CAP FPF in accordance with its standard procedures, identifying the contributions made, the commitments to be financed out of the available funds, eligible activities, and administration costs. ADB will provide financing partners with annual financial statements on these records and accounts.<sup>43</sup>

<sup>42</sup> The Controller's Department will prepare the financial statements in its standard format.

<sup>43</sup> A financing partner may opt not to have the financial statement audited.



55. If external financial audit is required, it will be undertaken annually by ADB's external auditor with respect to any trust fund under the IF-CAP FPF.

56. The FPFM will also provide to the financing partners, if required, additional reports and information concerning the progress of projects and activities financed under IF-CAP FPF. The contents of such additional reports and information shall be agreed in advance between the financing partners and the FPFM.

57. **Donor Committee meetings.** Donor Committee meetings will convene at least once a year after the establishment of the IF-CAP FPF, to review progress and administrative matters, as well as the work program and strategic directions of IF-CAP.

58. **Communication needs.** ADB will communicate the establishment of IF-CAP to key target audiences—e.g., potential donors, other stakeholders, and the wider public—highlighting its objectives, innovative features, and milestones achieved over time. ADB will also acknowledge contributions from IF-CAP's financing partners in verbal and written statements in the context of its climate-related work.

59. **Service fee and administrative costs.** Since the financing partners are primarily contributing to IF-CAP in an unfunded manner and are not subject to the 2009 Review of the Asian Development Bank's Service Charges for the Administration of Grant Cofinancing from External Sources (the Fee Policy),<sup>44</sup> ADB will not charge any service fees under the IF-CAP FPF. Management's waiver will be sought in accordance with the provisions of the Fee Policy. ADB will cover any associated administrative costs from its own resources unless otherwise agreed with the financing partners. ADB expects to pay guarantee premiums to financing partners issuing direct guarantees or contributing to the IF-CAP Guarantee Trust Fund. Any costs borne by ADB will not be passed on to DMCs receiving IF-CAP support.

60. **Closing date.** Upon completion of IF-CAP's 5-year investment period, the Donor Committee will decide on whether to continue or wind up IF-CAP investments. Notwithstanding the Donor Committee's decision, guarantees issued by financing partners bilaterally or through the IF-CAP Guarantee Trust Fund will remain effective until the completion of the stipulated 25-year term (para. 14), unless otherwise agreed. ADB and the FPFM will consult with the financing partners on how to return or transfer the unused funds,<sup>45</sup> and will take the required actions.

## VII. RISK ASSESSMENT

61. IF-CAP is a novel and complex structure and as such bears a certain degree of risk. At the same time, IF-CAP is inherently designed as a tool seeking to reduce some of ADB's core business risk (default risk). The table describes key risks associated with IF-CAP and the measures taken to mitigate them.

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<sup>44</sup> ADB. 2009. [Review of the Asian Development Bank's Service Charges for the Administration of Grant Cofinancing from External Sources](#). Manila.

<sup>45</sup> This may include transferring any unused funds to other projects, activities, or accounts as agreed with the financing partners.

### Key Risks and Mitigating Measures

Risks	Mitigation Measures
<p>The structure of the IF-CAP Guarantee Mechanism, including the potential sharing of recoveries by ADB with guarantors, may risk diluting ADB's preferred creditor status.</p>	<p>The IF-CAP Guarantee Mechanism has been structured as a multilateral financing initiative for the purpose of enhancing ADB's ability to provide climate finance in line with recommendations made by the G20 Independent Review of the MDBs' Capital Adequacy Frameworks (main text, para. 8). ADB consulted the secretariat of the Paris Club on the structure of the IF-CAP Guarantee Mechanism as described in this paper, which has confirmed that the structure does not, in principle, pose any risk of dilution of ADB's preferred creditor status.</p>
<p>Delay in creating climate impact because of insufficient and/or delayed fund mobilization</p>	<p>ADB's outreach strategy to prospective financing partners led to the successful establishment of a group of IF-CAP founding partners.<sup>a</sup> To secure timely commitment, ADB and the founding partners set up a basic term sheet covering IF-CAP's design features, governance mechanism, and implementation arrangements. Since financing partners must follow their respective budget cycles and processes, their contributions will be staggered; however, first indicative pledges have already been submitted. ADB will keep engaging with the founding partners as well as with new prospective partners to maximize IF-CAP capital in a timely manner.</p>
<p>The additional capital generated exceeds demand from developing member countries and/or appetite to borrow for climate projects.</p>	<p>Through its upcoming Climate Change Action Plan, ADB will work closely and continuously with developing member countries to carefully identify and craft actions that simultaneously meet climate and development goals. Additionally, ADB will keep monitoring and managing the level of IF-CAP's capital relief and issue an early warning if needed.</p>
<p>Lower than expected capital relief</p>	<p>The potential impact of the proposed transaction between ADB and financing partners on ADB's capital and lending capacity is contingent on the final terms of the transaction and may result in lower capital relief than initially assessed. Additionally, given the innovative nature of the transaction, it may not be fully recognized by credit rating agencies. ORM engaged Risk Control Limited to provide independent validation of the IF-CAP structure and its impact on ADB's capital adequacy under the current framework. In due course, ADB will engage with credit rating agencies to discuss their treatment of this mechanism.</p>
<p>Credit evolution risk</p>	<p>Ratings may change over time and the credit quality of either guarantors or the reference portfolio may impact the initial estimated capital relief. Sufficiently creditworthy financing partners may act as guarantors for ADB, subject to binding terms and conditions to ensure timely guarantee payments, and separate measures if partners lose creditworthiness.</p> <p>Overall, the credit evolution risk is mitigated by the fact that ADB's primary capital adequacy metric, the capital utilization ratio, will always be better (lower) than a</p>

Risks	Mitigation Measures
	scenario without IF-CAP, provided that ADB is not required to pay a guarantee fee when the value of the guarantee is zero.
Competing needs take priority over the climate change agenda.	After each investment period, ADB will reassess IF-CAP's viability and may recalibrate its structure as needed subject to agreement with the financing partners.
Various operational risks associated with this complex and innovative structure have been identified. They include risks associated with insufficient processes and controls, legal agreement complexity, or donor funds being used in a manner that does not fulfill the donor's instructions.	The full initial list of operational risks was identified by the project team in coordination with ORM. The financing partnership facility manager and the secretariat will be responsible for the monitoring and management of these risks. In addition, prior to the first transaction, relevant functions such as the Controller's Department, Office of the General Counsel, ORM, and Treasury Department) will provide confirmation that adequate and appropriate controls will be implemented and are documented in the upcoming IF-CAP Implementation Manual.

ADB = Asian Development Bank, G20 = Group of 20, IF-CAP = Innovative Finance Facility for Climate in Asia and the Pacific, ORM = Office of Risk Management.

<sup>a</sup> Financing partners who are not among the founding partners may join IF-CAP at a later stage.

Source: Asian Development Bank.

## VIII. RECOMMENDATION

62. The President recommends that the Board approve
- (i) the establishment of the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility in accordance with the provisions set forth in this paper;
  - (ii) the establishment of the Innovative Finance Facility for Climate in Asia and the Pacific Guarantee Trust Fund, under the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility, in accordance with the provisions set forth in this paper;
  - (iii) the establishment of the Innovative Finance Facility for Climate in Asia and the Pacific Grant Trust Fund, under the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility, in accordance with the provisions set forth in this paper;
  - (iv) the entering into financing partnerships comprising guarantees or risk participations, under the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility, in accordance with the provisions set forth in this paper;
  - (v) the establishment of a trust fund, framework arrangement and/or other form of financing partnership (including guarantees or risk participations) substantially in accordance with the terms and conditions set forth in this paper, in the event of any contribution to such trust fund, framework arrangement, or other financing partnership, under the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility, in accordance with the provisions set forth in this paper; and
  - (vi) the acceptance and administration by ADB of contributions to each trust fund and other financing partnership arrangement (including each of the bilateral risk participations) established or entered into under the Innovative Finance Facility for Climate in Asia and the Pacific Financing Partnership Facility in accordance with the provisions set forth in this paper.