



Technical Note

BLENDING FINANCE, THEMATIC INSTRUMENTS AND DEVELOPMENT BANKS

Strengthening Debt Sustainability and
Productive Transformation in Africa

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BLENDED FINANCE, THEMATIC INSTRUMENTS AND DEVELOPMENT BANKS: Strengthening Debt Sustainability and Productive Transformation in Africa¹

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Abstract

This technical note examines how blended finance, thematic instruments and national development banks can strengthen debt sustainability and support productive transformation in Africa. Drawing on a debt dynamics framework and country examples, it argues that financing should be assessed by its contribution to lower borrowing costs, longer maturities, reduced currency and refinancing risks, and productivity growth, alongside capital mobilization. It explores the trade-offs in blended finance design, the opportunities and safeguards associated with thematic bonds and debt-for-nature swaps, and the capacity of national development banks to channel long-term investment. The note emphasizes targeted concessionality, transparent fiscal risk management, independent verification and stronger domestic capital markets. It concludes that these mechanisms are most effective when tailored to institutional capacity and integrated into credible debt management and structural reform strategies.

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BLENDING FINANCE MECHANISMS

Blended finance should be presented as a structuring discipline, not as an instrument catalogue. Its purpose is to combine concessional and commercial capital in a way that creates investable opportunities where private capital would otherwise not participate because risks are too high, returns are too low for the risk taken, or both. A stricter definition therefore requires four elements: strategic use of development finance, mobilization of additional capital, a sustainable development objective or, in our specific case, for a productive-transformation objective, and the use of concessional finance on terms more favorable than the market. That fourth element matters. Without concessional finance, the transaction may still be innovative, but it is not blended finance in the strict sense.

The core policy issue is not whether blended finance is available, but whether it is the right solution to productive transformation financing binding constraints. The recent literature also shows that, despite growing interest, blended finance remains modest relative to overall development finance: in 2024, total blended finance flows reached USD 18.3 billion across 123 deals, and blended structures still represented less than 2% of total Multilateral Development Bank (MDB) investment (Convergence, 2025). In practice, blended finance works by creating asymmetric risk-return profiles for investors with different objective functions. Public investors, development finance institutions and philanthropic actors accept concessional or subordinated risk in order to attract private capital that seeks market-based returns. That is why blended finance is better understood as financial structuring than as a simple financing instrument. It is also why poorly targeted blending can fail: if the underlying barrier is regulatory, operational or institutional rather than financial, no amount of financial engineering will solve it.

The first trade-off is between mobilization and concessional finance. Blended finance is meant to stretch scarce public capital by mobilizing private investment, but doing so too aggressively can reduce the concessional finance actually passed through to the underlying project or borrower. Concessional finance captures how much the blended structure lowers financing terms relative to a fully commercial benchmark, while leverage captures how much commercially priced capital is mobilized per unit of concessional support. Both matter. In simple terms, the higher the leverage ratio, the more thinly the concessional benefit is spread across the total financing package. A transaction may therefore look successful from a mobilization perspective while delivering only a limited subsidy to the underlying project or borrower. This has an important policy implication: blended finance should not be assessed on mobilization ratios alone. Reporting frameworks, including the OECD DAC blended finance principles, should encourage disclosure of both leverage and concessional finance rather than privileging mobilization volume as the headline indicator.

The second trade-off is between leverage and protection of senior investors. In structured vehicles, maximizing the impact of catalytic capital often means making the senior tranche more investable for private investors. But higher leverage is not costless. The same framework shows a clear tension between the size of the junior tranche and the rating or safety of the senior tranche: a larger junior buffer can improve the rating and attractiveness of the senior notes, but it also lowers the leverage ratio; a smaller junior layer increases leverage, but may leave the senior tranche under-protected.

The third trade-off is between standardization and fit-for-purpose design. The market increasingly relies on a small number of repeatable structures (concessional capital, credit enhancement, technical

assistance facilities and design funding) and the data suggests that concessional capital remains dominant across sectors (Amundi, 2025). In agriculture, energy, infrastructure and health, the first structure accounts for the majority of transactions. This supports standardization. At the same time, in practice, structures differ so much in practice: asset risk, maturity, diversification, investor preferences and the sponsor's objective all influence the final capital stack. Standardization therefore helps scale, but only if the structure still matches the underlying asset and risk profile.

A useful way to think about instrument choice is to distinguish four functional blocks. The first is concessional capital, which lowers the cost of financing or absorbs first losses. The second is credit enhancement, such as guarantees or insurance, which protects investors against specific risks and can lower pricing. The third is technical assistance, which builds implementation capacity and strengthens governance. The fourth is design funding, which finances early-stage preparation so that projects become bankable. These blocks are not mutually exclusive. Most effective blended structures combine at least one risk-sharing tool with one capability-building tool.

The right mix of instruments depends on the type of financing binding constraint. When the main barrier is high real or perceived credit risk, credit enhancement is often more effective than subsidized debt in improving risk-adjusted returns and attracting private investors. When the problem lies earlier in the investment chain (such as weak project preparation, poor information or the absence of a credible pipeline) design funding and technical assistance are usually more appropriate than guarantees. Where the constraint is limited investor appetite for innovative, early-stage or higher-volatility activities, subordinated or first-loss capital may be needed to absorb initial risks and make senior investment viable. By contrast, when the central challenge is not the availability of finance but weak incentives for implementation and delivery, results-based mechanisms may be more suitable than conventional blended structures. The guiding principle is straightforward: the choice of instruments should be driven by diagnosis of the most binding constraint, not by the preferences of funders.

A structured diagnostic process allows policymakers and development finance institutions to identify which constraint is binding and whether financial instruments can realistically address it. The first step is to identify the thematic or sectoral challenge. This involves defining the development objective and understanding the structural constraints affecting investment, such as regulatory gaps, market fragmentation or weak demand conditions. Governments must determine whether the policy goal is to expand infrastructure investment, support small and medium enterprises, accelerate the energy transition or improve climate resilience. Clear articulation of the challenge helps align financial interventions with broader productive transformation strategies and prevents premature selection of instruments that may not address the root cause of the investment gap.

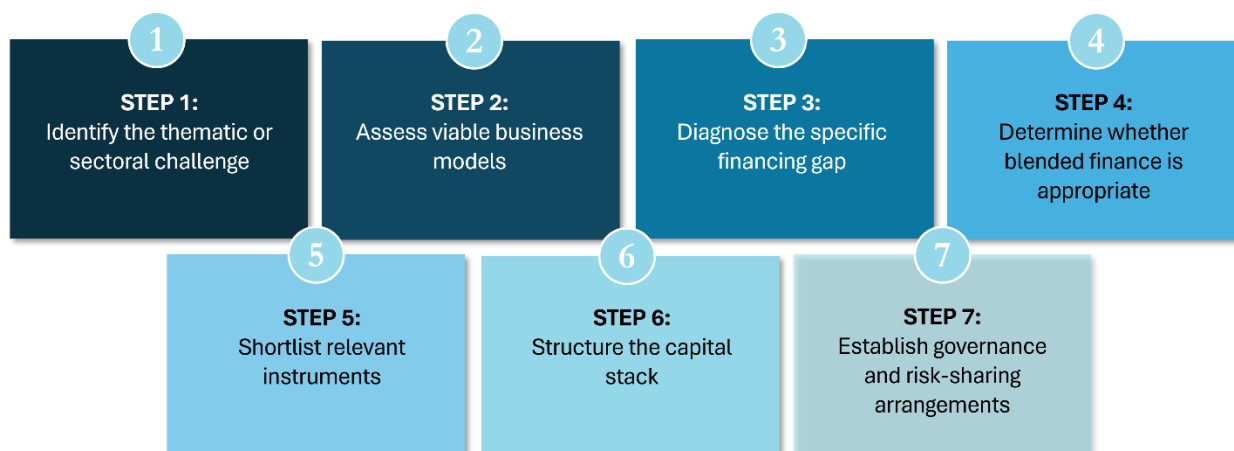
The second step is to assess viable business models. Blended finance cannot compensate for fundamentally unviable activities. Evaluating operating models, revenue streams and cost structures ensures that the proposed intervention has a credible economic foundation. This stage typically involves reviewing sector economics, pricing or fees structures, cost-recovery mechanisms and demand projections. If the underlying activity cannot generate sustainable revenues or deliver measurable public benefits, concessional finance may simply delay project failure rather than unlock sustainable investment.

The third step is to diagnose the specific financing gap. This requires distinguishing between different types of financial constraints, such as limited liquidity, high perceived risk, currency mismatches, insufficient returns or weak financial intermediation. For example, infrastructure projects may suffer from long construction periods that deter commercial lenders, while climate adaptation investments may generate public benefits that are not easily monetized. Accurate diagnosis is essential to determine whether the barrier is financial, regulatory or operational and whether financial instruments are the appropriate response.

The fourth step is to determine whether blended finance is appropriate. In some situations, policy reforms, targeted subsidies or direct public investment may be more effective than blended finance structures. For example, regulatory reforms may unlock private investment more efficiently than risk-sharing mechanisms if the main constraint is legal or regulatory uncertainty. Blended finance should therefore be used selectively, particularly in environments where public resources are scarce and where concessional capital must demonstrate clear additionality.

The fifth and sixth steps involve shortlisting relevant instruments and structuring the capital stack. Once the financing gap has been clearly identified, policymakers and structuring institutions can select appropriate tools, such as guarantees, first-loss tranches, concessional loans or technical assistance facilities. These instruments must be positioned within the capital structure in a way that redistributes risk between public and private investors without eliminating incentives for prudent risk management. Effective capital structuring ensures that public resources play a catalytic role while maintaining market discipline.

The final step is to establish governance and risk-sharing arrangements. Transparent rules for loss allocation, reporting, monitoring and exit strategies are essential to ensure accountability and preserve market discipline. Governance frameworks should specify the responsibilities of public sponsors, private investors and implementing agencies, as well as the mechanisms used to monitor financial performance and development outcomes. Strong governance arrangements are particularly important when concessional capital is involved, as they help maintain investor confidence and protect public resources.



A disciplined diagnostic approach prevents the overuse of concessional instruments. By grounding blending decisions in clear evidence of market failure, policymakers can ensure that public resources are

used to mobilize additional investment rather than substituting for capital that would otherwise be deployed commercially. This approach also improves the credibility of blended finance programmes by demonstrating that concessional resources are deployed only when they generate measurable catalytic effects.

The design of a blended finance structure must also reflect the characteristics of the underlying portfolio. The level of protection required for senior investors depends not only on the size of the junior or concessional tranche, but also on how risk is distributed across the asset pool. Default correlation, portfolio concentration and expected recovery rates can materially affect the resilience of the structure under stress. The same volume of assets may therefore justify very different capital structures depending on whether exposures are diversified across countries, sectors and borrowers, or concentrated in a narrower segment. In practice, this means that structuring choices must be calibrated to the risk profile of the underlying assets rather than applied mechanically across transactions. Highly concentrated or weakly diversified portfolios generally require stronger protection for senior investors, whereas broader and more diversified portfolios can sustain thinner subordinated layers without undermining investor confidence.

Recent market evidence also supports a selective reading of blended finance. The global market has now reached approximately USD 249 billion across 1 350 transactions, reflecting continued expansion compared to earlier estimates (Convergence, 2025). At the transaction level, deal sizes are increasing, with the median reaching about USD 65 million in 2024, up from previous years. Annual flows remain volatile but elevated, with USD 18.3 billion mobilized across 123 deals in 2024, following a peak of USD 23.1 billion in 2023 (Convergence, 2025). Despite this growth, activity remains concentrated: a small number of large transactions account for a disproportionate share of total financing, while most deals remain relatively small and bespoke. These patterns highlight both the consolidation of the market and its structural limits. Blended finance is scaling gradually and attracting larger transactions, but it continues to operate as a specialized segment rather than a fully mainstream financing channel.

The policy message should therefore remain selective and focused on economic justification. Blended finance adds value when it manages three trade-offs effectively: it mobilizes private capital without eroding concessionality, it increases leverage without leaving senior investors insufficiently protected, and it promotes standardization without losing fit-for-purpose design. The appropriate mix of instruments depends on the specific financing failure being addressed, and the structuring process should begin with diagnosis rather than with a pre-selected product. Detailed typologies of instruments remain useful, but the central policy issue is whether blending is economically justified, how the instrument mix should be chosen, and how structuring choices affect leverage, concessionality and investor protection.

Table 1 provides an overview of key blended finance instruments; additional details are available in the annex.

Instrument	Primary Objective	Typical Size / Coverage	Position in Capital Structure	Main Risk Addressed	Sovereign and National Development Bank (NDB) Relevance
Concessional debt (below-market loans)	Reduce overall cost of capital; enable longer tenors	10–40% of total capital stack	Senior or subordinated	High financing cost; tenor mismatch	Extend maturities for infrastructure; support on lending through NDBs; improve debt profile

					through lower blended interest rates
Subordinated / first-loss capital	Absorb initial losses to crowd in senior investors	10–25% of capital stack (higher in high-risk sectors)	Junior tranche	Portfolio credit risk; early-stage volatility	Strengthen NDB balance sheets; de-risk SME or infrastructure lending; mobilize domestic institutional investors
Partial credit guarantees	Reduce probability of default; improve pricing	30–80% of principal covered	Off-balance-sheet credit enhancement	Credit risk; refinancing risk	Lower sovereign or sub-sovereign bond spreads; extend bond maturities; support domestic bond market development
Partial risk guarantees / political risk insurance	Cover regulatory, policy or political risks	Project-specific; often tailored coverage	Credit enhancement linked to specific risks	Policy instability; expropriation; convertibility risk	Support energy and infrastructure reforms; reduce foreign investor risk premia
Design-stage grants (project preparation)	Improve bankability; reduce early-stage transaction risk	1–10% of total project cost	Pre-investment support	Feasibility and structuring risk	Prepare PPP pipelines; structure thematic bonds; design refinancing facilities
Technical assistance facilities (TAFs)	Strengthening governance, operational and reporting capacity	5–15% of facility size	Linked to investment vehicle	Operational, governance and implementation risk	Improve debt reporting transparency; strengthen NDB credit risk systems; support thematic bond reporting frameworks
Results-based financing / impact bonds	Align payments with measurable outcomes	Transaction-specific; often outcome-based payments	Separate performance-linked contract	Performance risk; service delivery inefficiency	Improve public expenditure efficiency; attract private capital to preventive or social sectors
Equity participation (including private equity)	Provide growth capital; share upside risk	Varies widely; often minority stakes	Equity tranche	Revenue volatility; business growth risk	Capitalize NDB subsidiaries; support strategic sectors aligned with industrial policy
Mezzanine / quasi-equity instruments	Provide flexible capital between debt and equity	5–20% of capital structure	Subordinated, convertible or hybrid	Capital adequacy constraints; refinancing pressure	Strengthen NDB capital ratios; support transformation sectors requiring longer repayment profiles
Thematic bond enhancement (e.g. green or social bonds with guarantees)	Improve pricing and investor confidence for labelled instruments	Guarantee or subordinated support varies (10–50%)	Credit enhancement layer	ESG reporting risk; investor uncertainty	Reduce spreads on GSSSB bonds; diversify investor base; align capital markets with climate and SDG objectives

Table 1: Blended Finance Instruments

BLENDING FINANCE MUST STRENGTHEN DEBT SUSTAINABILITY AND PRODUCTIVE TRANSFORMATION

BLENDING FINANCE MUST MOVE BEYOND MOBILIZATION AND ADDRESS SOVEREIGN DEBT RISKS

Blended finance should not be judged by mobilization ratios alone. In Africa's current macro-financial environment, the central constraint is no longer only project risk but sovereign balance-sheet stress. Many countries face rising interest burdens, compressed fiscal space and growing domestic rollover risks. Under these conditions, blended finance must improve the quality and sustainability of public debt, not merely increase financing volumes.

Mobilizing private capital does not automatically improve debt sustainability. Blended finance aims to use public or concessional resources to attract commercial investors. This approach can unlock investment in difficult markets. However, if it does not reduce borrowing costs, extend maturities or raise economic growth, its macroeconomic impact remains limited. In some cases, poorly structured operations can increase contingent liabilities and weaken fiscal transparency.

Policy makers should evaluate blended finance against sovereign-level criteria. Four questions are central: i) does it reduce effective borrowing costs; ii) does it extend maturities or smooth refinancing peaks; iii) does it reduce foreign exchange risk; and iv) does it support productive transformation sectors that raise economic growth? Framing blended finance around these criteria anchors it in debt sustainability.

FROM PROJECT BANKABILITY TO BALANCE-SHEET RESILIENCE

Debt dynamics are driven by the gap between interest rates and growth. When the effective interest rate on public debt exceeds nominal GDP growth, debt ratios rise unless governments maintain sustained primary surpluses. African countries currently face increased interest costs relative to pre-2022 market conditions combined with moderate growth prospects. This increases vulnerability to shocks.

Blended finance can improve debt sustainability only through two channels. First, blended finance can reduce the effective cost of capital through risk-sharing mechanisms, guarantees, or concessional tranches. Second, it can finance investments that raise productivity and expand economic output. If neither channel operates at scale, blended finance does not alter debt trajectories.

Sovereign debt dynamics can be expressed as:

$$b_t = \frac{1+r}{1+g} b_{t-1} - s_t$$

Where:

- b_t is the debt-to-GDP ratio at time t ,
- r is the real interest rate,
- g is the real GDP growth rate,

- s_t is the primary surplus as a share of GDP.

Blended finance affects debt sustainability only if it changes either:

- the real cost of debt (r),
- real economic growth (g) through productive investment,
- or the volatility of these variables.

If blended finance structures reduce project-level risks but do not translate into lower sovereign borrowing costs in real terms (or if they increase contingent liabilities) their macroeconomic impact may be neutral or even negative. A concrete illustration clarifies the stakes. Consider a country with a debt-to-GDP ratio of 60%, a real interest rate of 8%, real GDP growth of 4%, and a primary surplus of zero. Under these conditions, the debt ratio rises by approximately 2.3 percentage points per year, reaching roughly 83% of GDP within a decade absent adjustment. If a blended finance operation — through a combination of guarantees, concessional tranches and improved sovereign credit metrics — reduces the effective real borrowing cost by 150 basis points (from 8% to 6.5%), the annual debt-ratio deterioration falls to approximately 1.5 percentage points, a meaningful improvement in fiscal space over a 10-year horizon but still insufficient to stabilize the debt ratio without complementary growth or fiscal measures. By contrast, if the same operation finances productive investments that raise the real growth rate by one percentage point (from 4% to 5%), the combined effect of lower r and higher g produces near-stabilization of the debt ratio even without a primary surplus. This arithmetic underscores two policy conclusions: first, that modest improvements in borrowing costs alone are unlikely to alter debt trajectories materially; and second, that blended finance operations which simultaneously reduce r and raise g , through productive investment, generate fiscal returns that dwarf those of pure cost-reduction strategies.

A note on terminology is also warranted. The debt dynamics framework operates in real terms, but most observable financing variables — bond coupons, NDB lending rates, blended facility pricing — are quoted nominally. The translation matters, but the appropriate deflator depends critically on the perspective being adopted and conflating the two leads to analytical error. From the sovereign's standpoint, the relevant correction is a broad domestic price index, CPI or GDP deflator, because what matters for debt sustainability is whether the real burden of obligations is rising or falling relative to the economy's productive capacity. Nigeria's third sovereign green bond, carrying a nominal coupon of 18.75–19.25% in 2025 against a backdrop of inflation above 20%, implies a near-zero or negative real borrowing cost for the sovereign in domestic terms — a materially different fiscal picture from the nominal rate alone. From the investor's standpoint, however, headline CPI in a high-inflation African economy is largely the wrong deflator. Foreign institutional investors evaluate returns against dollar or euro benchmarks, not domestic consumer prices. Even domestic institutional investors, e.g., Nigerian pension funds, compute portfolio returns relative to liability structures and asset-price dynamics that are poorly proxied by headline CPI, whose basket is heavily weighted toward food and household consumption categories that are structurally irrelevant to institutional portfolio economics.² Applying headline CPI to deflate investor returns therefore risks overstating the real yield concession that investors are making and

² For example, Nigeria rebased its CPI in 2022 with food carrying approximately 51.8% weight. See NBS, Consumer Price Index Methodology, 2022 Base Year.

understating the market's actual appetite for the instrument at the offered terms. Practitioners and policymakers should therefore report real borrowing costs consistently but explicitly from the sovereign's perspective, using GDP deflator-based adjustments where CPI is volatile or unrepresentative, while evaluating investor return adequacy against dollar-equivalent or liability-relative benchmarks appropriate to investor classes.

The central question therefore becomes: how can catalytic capital and risk-sharing instruments be structured to improve sovereign-level credit metrics, particularly by reducing real borrowing costs and supporting sustained growth?

Macroeconomic implications must guide transaction design. Project-level viability is not sufficient. Blended operations should be assessed for their aggregate fiscal effects, including their impact on debt service, maturity structures and growth multipliers. A narrow focus on project bankability risks overlooking systemic vulnerabilities.

GUARANTEES MUST REDUCE REFINANCING RISK, NOT ONLY PROJECT RISK

Risk mitigation instruments should target sovereign refinancing constraints. Guarantees can attract private capital by reducing downside exposure. They are particularly useful in markets where investors demand high risk premia. However, not all guarantees influence sovereign spreads or maturity profiles.

Guarantee design determines their effectiveness. Instruments that cover longer maturities or specific refinancing peaks can reduce rollover risk. Guarantees linked to policy milestones can strengthen credibility. By contrast, untargeted guarantees may mobilize capital without lowering financing costs. Precision in structuring is therefore essential.

Transparency is critical for guarantees to support credit quality. Guarantees create contingent liabilities. If these liabilities are not properly disclosed, they may weaken investor confidence. Clear reporting standards and integration into debt management frameworks are necessary to ensure that guarantees strengthen, rather than undermine, fiscal credibility.

CONCESSIONAL CAPITAL SHOULD IMPROVE CAPITAL STRUCTURES, NOT SUBSIDIZE RETURNS

Concessional capital is effective when it absorbs identifiable and temporary risks. Below-market tranches can reduce the overall cost of capital in a transaction. They can also provide first-loss protection to crowd in senior investors. Yet concessionality should not permanently subsidize commercial returns.

Targeted concessional layers can address specific market failures. These include construction risk in infrastructure, early-stage risk in new sectors, or transition risk in energy reforms. Once these risks decline, concessional support should be phased out. Time-bound and clearly defined objectives prevent long-term market distortions.

Domestic capital markets must not be crowded out. Blended finance should complement domestic institutional investors, not displace them. Strengthening local capital markets contributes directly to

resilience by reducing reliance on volatile external financing. Designing structures that integrate domestic investors enhances sustainability.

TECHNICAL ASSISTANCE CAN DIRECTLY INFLUENCE BORROWING CONDITIONS

Institutional quality shapes sovereign borrowing costs. Credit ratings and investor perceptions depend heavily on governance, transparency and debt management capacity. Weak reporting systems and opaque contingent liabilities increase risk premia.

Technical assistance can therefore act as a credit-enhancing tool. Strengthening debt recording systems, publishing credible issuance calendars and improving investor communication can reduce uncertainty. Transparent reporting of domestic debt and state-owned enterprise liabilities builds confidence. These institutional improvements can translate into lower spreads and longer maturities.

Blended finance should systematically integrate institutional strengthening. Technical assistance should not be treated as an optional add-on. It should be embedded within financing operations to reinforce policy credibility and financial discipline. This approach aligns financial structuring with governance reform.

PRODUCTIVE TRANSFORMATION IS ESSENTIAL FOR SUSTAINABLE GROWTH: ENSURING $G > R$

Blended finance must prioritize productive transformation sectors that raise productivity and export capacity. The debt dynamics framework makes the growth channel analytically central, not secondary. When the real interest rate on public debt exceeds the real growth rate (the $r > g$ condition that characterizes a substantial share of African sovereign debt positions today) debt ratios deteriorate continuously unless offset by primary surpluses that are themselves politically and socially costly to sustain. Blended finance that reduces borrowing costs without raising growth therefore addresses only one side of a two-variable problem, and the arithmetic of the previous section demonstrates that cost reduction alone is unlikely to stabilize debt trajectories at plausible parameter values. The growth channel is not merely complementary to the cost-reduction channel, in many African fiscal contexts, it is the dominant one.

The dominance of the growth channel has direct implications for sector prioritization. Not all productive investment generates equivalent fiscal returns. The empirical literature on infrastructure investment in Sub-Saharan Africa suggests output multipliers in the range of 1.5 to 2.0 over five-year horizons for transport and energy investments in supply-constrained economies, with higher multipliers where complementary investments in human capital and institutional capacity are present (Izquierdo, et al., 2019). By contrast, investment in sectors with weak backward and forward linkages, limited employment intensity or high import content generates lower domestic value-added and weaker fiscal returns per dollar deployed. Blended finance pipelines should therefore be explicitly prioritized toward sectors where the growth multiplier is highest and where productive transformation effects (measured by export diversification, domestic value-chain development and technological upgrading) are most durable.

Energy, transport, agro-processing and digital infrastructure satisfy these criteria in most African economic contexts. Energy investments reduce production costs economy-wide and unlock capacity

utilization in manufacturing and services. Transport connectivity reduces trade costs and supports regional market integration, for instance, corridor investments can reduce shipping times from 45 days to 48 hours, with large implications for trade and productivity (OECD, 2025). Agro-processing deepens domestic value chains, reduces commodity export dependence and supports rural income growth, improving the breadth of the tax base over time. Digital infrastructure generates cross-sector productivity spillovers and supports the formalization of economic activity; despite its importance, access gaps remain substantial across regions, highlighting both unmet demand and high marginal returns to investment (OECD, 2025). These are not merely development priorities, they are fiscal investments whose returns, properly accounted, justify concessional support on debt sustainability grounds.

Productive transformation also reduces external vulnerability, which matters for debt sustainability through a separate channel. Economies dependent on a narrow range of commodity exports face pronounced revenue volatility that complicates debt service and elevates risk premia. Structural diversification — supported by blended finance directed at manufacturing, services and agro-industry — dampens this volatility over time, reducing the tail risks that rating agencies and sovereign bond investors price into spreads. A blended finance programme anchored in productive transformation therefore generates a compounding fiscal dividend: higher g improves the primary debt dynamic, while reduced external vulnerability lowers r through spread compression. These two effects are mutually reinforcing and, in combination, can shift debt trajectories substantially more than either channel operating in isolation.

The practical implication for blended finance design is that project selection criteria must incorporate growth multiplier assessment alongside conventional financial viability analysis. A project that is bankable at the transaction level but generates weak economy-wide linkages delivers limited debt sustainability value relative to the concessional resources deployed. Development finance institutions, NDBs and governments should therefore establish explicit productive transformation criteria, including sectoral multiplier estimates, export orientation, domestic content requirements and employment intensity thresholds, as conditions for accessing concessional blended finance support. This shifts the evaluation framework from project-level internal rate of return to sovereign-level fiscal return, which is the metric that ultimately determines whether blended finance strengthens or merely accompanies Africa's debt trajectory.

EFFECTIVE BLENDED FINANCE REQUIRES ALIGNMENT ACROSS DEVELOPMENT ACTORS

Blended finance brings together actors with different incentives. Governments seek lower financing costs and longer maturities. Development partners aim to support policy reform and development impact. Private investors require stable risk-adjusted returns.

Clear governance frameworks ensure alignment. Transparent risk allocation, defined exit strategies and robust monitoring systems reduce uncertainty. National Development Banks can play a catalytic role by coordinating concessional and commercial capital while maintaining prudent risk management.

Interactions with Multilateral and bilateral development banks can strengthen balance sheets. Guarantees, subordinated instruments and co-financing arrangements can improve credit profiles. However, these mechanisms must be integrated into national debt management strategies to avoid fragmentation.

BLENDING FINANCE CANNOT SUBSTITUTE FOR SOUND FISCAL POLICY

Blended finance cannot substitute for sound fiscal policy. Blended finance is not a remedy for unsustainable debt paths. Where debt trajectories are already unstable, additional layered financing may delay necessary adjustment rather than resolve underlying imbalances. Structural reforms, revenue mobilization and expenditure efficiency therefore remain fundamental to restoring and maintaining debt sustainability.

Blended finance must be embedded within medium- and long-term debt sustainability frameworks. The effectiveness of blended instruments depends on their consistency with macro-fiscal strategies, including medium-term debt management strategies (MTDS) and debt sustainability analyses (DSA). Without such alignment, blended structures risk increasing fragmentation, obscuring fiscal risks or creating contingent liabilities that are not adequately captured in debt metrics. Ensuring coherence between blended finance operations and sovereign debt frameworks is therefore critical to preserving fiscal credibility and avoiding unintended deterioration in debt dynamics.

Blended finance is most effective where reform momentum exists. In such contexts, catalytic instruments can accelerate investment, deepen markets and reduce risk perceptions. They can support the implementation of credible fiscal and structural strategies by improving financing conditions and mobilizing additional capital. However, their role remains complementary: they are tools to reinforce sound macroeconomic frameworks, not substitutes for them.

Blended finance should be understood as a means to achieve debt sustainability and productive transformation, not as an objective in itself. The policy focus should therefore shift from the volume of capital mobilized to the quality of outcomes generated at the sovereign level. In practice, this implies that blended finance operations must be assessed against their ability to improve core macroeconomic fundamentals: reducing the cost and risk profile of public debt, strengthening institutional capacity and financing investments that raise long-term productivity and growth. Mobilization metrics alone are insufficient if they do not translate into stronger debt dynamics or structural transformation. This reframing is particularly important in the African context, where financing needs are large but fiscal space is constrained. Blended finance should therefore be deployed selectively, as an instrument to support credible development strategies and enhance sovereign creditworthiness, rather than as a standalone financing solution.

THEMATIC INSTRUMENTS: OPPORTUNITIES AND SAFEGUARDS

Thematic financial instruments have emerged as an important channel for aligning capital markets with sustainable development objectives. Instruments such as green, social, sustainability and sustainability-linked bonds (GSSSB bonds), as well as debt-for-nature and sustainability swaps, allow governments to mobilize capital while signaling commitments to environmental, social or governance priorities.

These instruments can expand the investor base and improve financing conditions when properly structured. Institutional investors increasingly allocate capital to environmental, social and governance

(ESG) assets. Thematic instruments can therefore attract new categories of investors and potentially reduce financing costs, particularly when supported by credible frameworks and verification mechanisms.

However, thematic instruments must be carefully integrated into debt management strategies. Without strong safeguards, they may increase complexity without improving fiscal sustainability. Transparent reporting, credible performance metrics and integration with medium-term debt strategies are therefore essential to ensure that these instruments contribute to sustainable financing rather than merely re-labelling existing debt.

GSSSB BONDS (GREEN, SOCIAL, SUSTAINABILITY AND SUSTAINABILITY-LINKED BONDS)

Sovereign green bonds can strengthen debt sustainability only when they improve market access and finance high-return public investment. A green label does not change debt dynamics by itself. The debt impact comes from two channels: i) whether the issuance expands and stabilizes the investor base (thereby reducing refinancing risk and supporting tenure extension), and ii) whether the funded expenditures raise productivity and resilience in ways that support growth and fiscal capacity over time.

Nigeria's sovereign green bond program illustrates how repeated issuances can build market infrastructure and credibility. Nigeria issued its debut sovereign green bond in 2017 and followed with a second issuance in 2019 and a third in 2025, using the Debt Management Office as the executing institution. The 2017 offer raised ₦10.69 billion with a 5-year tenor and a 13.48% coupon, and it closed slightly oversubscribed (₦10.791 billion subscribed vs ₦10.69 billion offered), with participation reported across banks, pension funds, asset managers and retail investors. This first issuance mattered less for its size than for its signaling value: it established a template for eligible expenditures, allocation processes and reporting expectations that subsequent issuances could scale (Nigeria, 2021).

Subsequent issuances helped deepen the domestic investor base and demonstrate the repeatability of the instrument. Nigeria's second sovereign green bond, issued in 2019, offered ₦15 billion and achieved strong investor demand, with subscriptions exceeding twice the offer size. The bond carried a 7-year maturity and was listed on domestic exchanges, reinforcing the integration of thematic bonds into the country's broader capital market development strategy. By repeating the issuance under the same framework, authorities strengthened investor confidence and improved familiarity with the instrument.

More recent issuances demonstrate the capacity of thematic bonds to scale within domestic markets. Nigeria's third sovereign green bond issuance in 2025 was structured as a ₦50 billion 5-year bond maturing in 2030, with a coupon range between 18.75% and 19.25% and semi-annual coupon payments, with principal repaid at maturity. The issuance attracted strong demand, with total subscriptions reaching approximately ₦91.4 billion, equivalent to about 183% of the offered amount. This level of demand indicates that thematic bonds can mobilize substantial capital even under high interest rate environments when governance and reporting frameworks are credible (Nigeria, 2025). The oversubscription of Nigeria's third green bond at nominal coupons of 18.75–19.25% is sometimes interpreted as evidence that investors accepted compressed real returns in exchange for the green label. This interpretation requires care. As noted in the debt dynamics discussion above, the relevant deflator differs by investor class: foreign investors computing dollar-equivalent returns and domestic institutional investors benchmarking

against liability structures were not necessarily accepting negative real yields, their effective return calculus was largely decoupled from headline Nigerian CPI. The oversubscription is better interpreted as evidence that the instrument's governance credentials, reporting framework and liquidity profile were sufficient to clear the market at those nominal terms. Disentangling these effects, genuine pricing benefit from the green label versus demand driven by instrument quality and market scarcity, remains an open empirical question for African sovereign green bond markets and one that future issuance data, as the pipeline deepens, will be better positioned to answer.

Robust governance arrangements are essential to maintain the credibility of sovereign green bonds. In Nigeria's case, project execution is assigned to sector ministries and implementing agencies, while a dedicated green bond team oversees allocation, monitoring and reporting. Proceeds are managed through treasury-linked sub-accounts that track the allocation of funds and prevent diversion to unrelated expenditures. This approach strengthens transparency and ensures that funds remain tied to eligible climate and environmental investments.

Independent post-issuance verification and impact reporting further reinforce investor confidence. Nigeria's green bond programme includes post-issuance assurance that reviews compliance with the bond framework across four areas: use of proceeds, project selection, management of proceeds and reporting practices. Verification exercises have confirmed alignment with the framework and provide project-level data on environmental outcomes, including renewable energy generation and greenhouse gas emissions reductions. Such reporting is essential for building long-term credibility in sustainable finance markets.

The debt-management value of sovereign green bonds depends on their integration into broader financing strategies. Thematic bonds contribute to debt sustainability when they support predictable issuance calendars, broaden the investor base and finance investments that enhance economic resilience. When embedded within a medium-term debt strategy, they can also support the development of benchmark instruments that deepen domestic capital markets.

International experience confirms that strong frameworks and credible governance can translate into tighter pricing and oversubscription. Egypt's 2020 inaugural sovereign green bond is widely cited as a milestone example of building a sovereign green finance framework and attracting strong investor demand, including reported oversubscription that allowed the issue size to be increased and the coupon lowered relative to initial expectations (Hussain, 2022). The relevance for African issuers is not to replicate templates mechanically, but to internalize the lesson: the market rewards clarity on eligible expenditures, verification, and governance arrangements that make proceeds traceable and impacts auditable.

DEBT-FOR-NATURE AND SUSTAINABILITY SWAPS

Debt-for-nature and broader "sustainability" swaps are increasingly used as liability-management operations that also create protected fiscal space for priority spending. In practice, they are not a substitute for comprehensive debt restructuring when solvency is impaired; rather, they are best understood as *targeted refinancing* or *selective exchanges/buybacks* that (i) reduce near-term refinancing risk and/or interest costs, and (ii) earmark a portion of quantified savings into pre-agreed, independently governed expenditures. The policy logic is therefore twofold: swaps should be judged on whether they improve the sovereign's debt dynamics under stress (not only in a baseline) and whether they lock in credible, measurable "transformation" outcomes without weakening budget integrity.

Well-designed swaps directly address the current constraint binding many African issuers: high marginal cost of foreign-currency borrowing driven by perceived credit risk and policy uncertainty. When spreads are elevated, even modest maturity extensions or coupon reductions can materially lower annual gross financing needs (GFN) and smooth Eurobond redemption humps, especially around “bullet” maturities. In that context, swaps can function as a bridge instrument that buys time for reforms, improves debt-service liquidity, and creates space for climate/adaptation or natural-capital investments that reduce long-run fiscal risks (e.g., disaster losses, commodity-linked revenue volatility).

Most market-facing debt-for-nature swaps executed recently follow a “credit-enhanced refinancing” structure rather than a classic bilateral Paris Club-style cancellation. In these transactions, a new bond is issued with a credit enhancement such as a guarantee or political risk insurance. The proceeds are used to repurchase existing sovereign bonds trading in the secondary market. The transaction generates savings through lower interest rates or longer maturities, and part of these savings is committed to environmental or development investments under a dedicated governance framework.

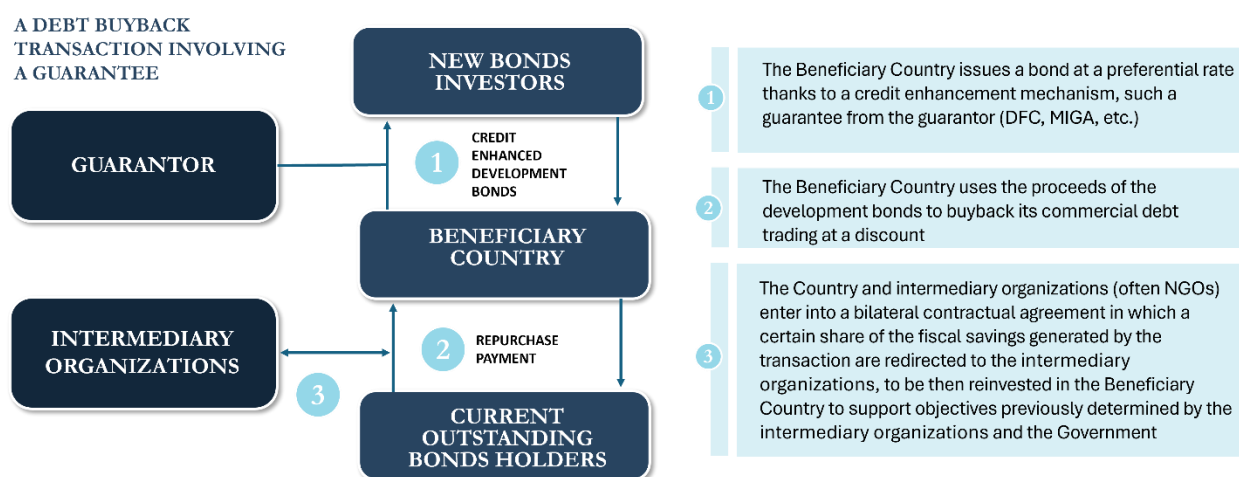


Figure 1. Intermediary Organizations may include examples such as The Nature Conservancy, WWF, or Conservation International

In some cases, the transaction is implemented through a special purpose vehicle (SPV) supported by political risk insurance. The SPV issues credit-enhanced bonds to investors and on-lends the proceeds to the sovereign through development-linked loans. The sovereign uses these funds to repurchase outstanding bonds in the secondary market. As in guarantee structures, the refinancing savings are partially redirected toward sustainability or conservation programmes.

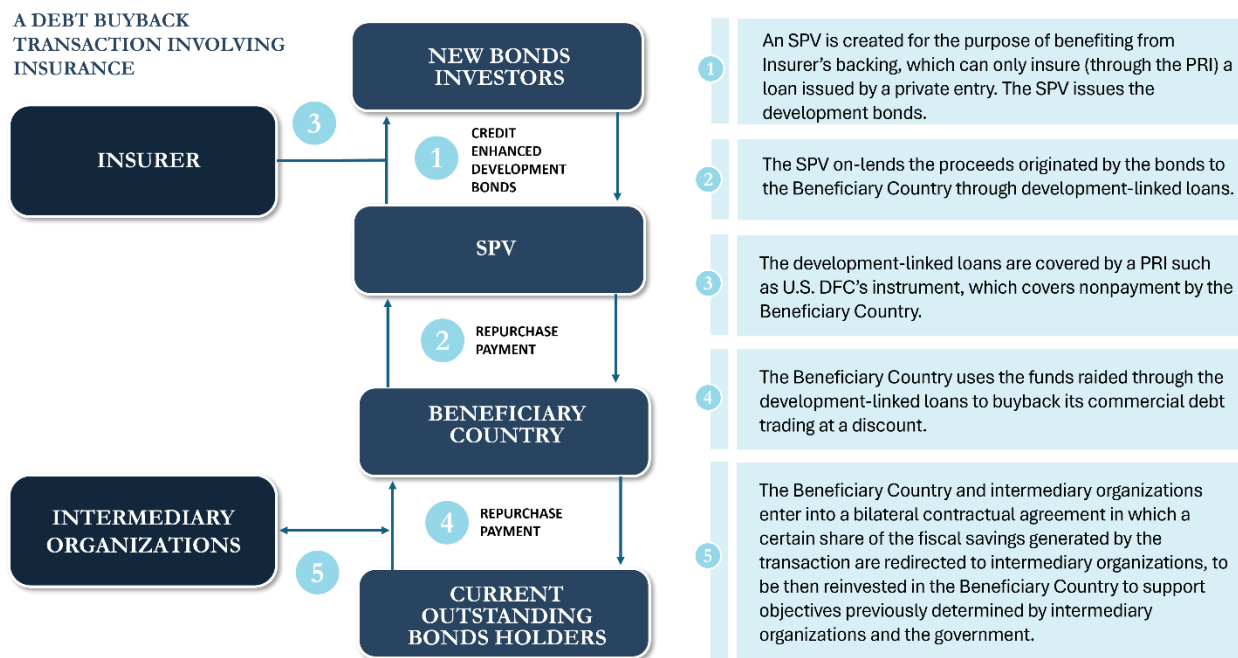


Figure 2. Intermediary Organizations may include examples such as The Nature Conservancy, WWF, or Conservation International

The operational core is a liability-management transaction whose economics depend on secondary-market pricing and the strength of the credit wrap, not on philanthropic concessionality alone. If the sovereign's existing bonds trade at a discount, the buyback can crystallize a reduction in the present value of obligations; if the new, wrapped instrument prices closer to investment grade, the all-in cost of refinancing can fall enough to generate a measurable savings stream. This is why swaps are typically executed with an arranger/underwriter and a guarantee/insurance provider, and why deal documentation must specify (a) eligible debt, (b) pricing/discount mechanics, (c) allocation of savings, and (d) enforceability of policy commitments.

Gabon's 2023 transaction illustrates how political-risk insurance can compress pricing and extend maturities even when the sovereign is sub-investment grade. The deal refinanced USD 500 million of Gabon's debt and was designed to mobilize substantial conservation funding over time (Conservancy, 2023). It relied on DFC political risk insurance supporting a USD 500 million "blue bond" financing package (DFC, 2023).

The most policy-relevant feature is that the transaction primarily reduced refinancing risk rather than delivering large stock relief. According to a critical transaction summary, Gabon bought back three bonds totaling USD 500 million (including one 2025 maturity and two 2031 maturities) and replaced them with a new USD 500 million bond maturing in 2038; the reported coupon on the new instrument (6.097%) was below the coupons on the repaid bonds (6.625–7%). This structure, retiring nearer maturities and pushing duration outward, maps directly to the objective of smoothing the Eurobond curve and lowering rollover peaks, which is typically the first-order priority for debt-distressed but still market-access countries (AfronomicsLAW, 2023).

The development finance additionality is created through a rules-based “savings capture” mechanism that channels a defined portion of refinancing gains into pre-agreed outcomes. In Gabon’s case, the transaction commits the government to allocate USD 5 million per year over the next 15 years from the refinancing savings to marine conservation programmes. In parallel, part of the resources will capitalize a dedicated endowment fund that is expected to grow to approximately USD 88 million by 2038, providing long-term financing for marine protected areas and biodiversity management. The strategic lesson for Africa is that the conservation (or climate) component must be treated as a contractually protected claim on savings, otherwise it risks being diluted by budget pressures and losing credibility with both investors and domestic stakeholders.

Belize’s 2021 “blue bond/blue loan” transaction provides a useful benchmark because it demonstrates how credit enhancement can materially improve sovereign refinancing outcomes while linking debt operations to conservation financing. The transaction refinanced Belize’s external commercial debt by repurchasing USD 553 million of its “Superbond” at approximately 55 cents on the dollar, allowing the government to replace the liability with a USD 364 million Blue Loan arranged by The Nature Conservancy through a dedicated subsidiary. This restructuring generated a principal reduction of about USD 189 million, equivalent to roughly 12% of GDP, while extending the maturity profile by about 6.5 years and lowering the overall debt service burden. The Blue Loan was financed through the issuance of highly rated “Blue Bonds” backed by political risk insurance from the U.S. International Development Finance Corporation (DFC), which enabled the bonds to obtain an Aa2 rating from Moody’s, far above Belize’s sovereign rating at the time. By attaching the credit enhancement to the new refinancing instrument rather than the legacy debt, the structure enabled the country to refinance distressed debt on more favorable terms while simultaneously committing a portion of the resulting savings to marine conservation investments. The refinancing also generated an estimated USD 180 million in conservation financing over 20 years, including average annual payments of about USD 4.2 million and a USD 23.5 million endowment expected to grow to roughly USD 92 million by 2041, illustrating how liability management operations can simultaneously support debt sustainability and long-term environmental investment (Conservancy, 2021).

Box 1. U.S. International Development Finance Corporation (DFC): key financial instruments

DFC represents a central channel of U.S. support for international development through market-based financial instruments. Established in 2019, DFC reflects a shift toward mobilizing private capital alongside public resources, using a range of financial tools designed to address investment constraints in developing economies.

Instrument	Description	Main Risk Addressed	Typical Use Cases
Political risk insurance (PRI)	Covers non-commercial risks such as expropriation, currency inconvertibility, transfer restrictions, political violence and breach of contract	Political and regulatory risk	Cross-border investments, sovereign-linked transactions, bond issuances (e.g. credit enhancement)
Loan guarantees / credit enhancement	Partial guarantees on loans or bonds to reduce expected losses and improve investor confidence	Credit risk, refinancing risk	Sovereign or sub-sovereign borrowing, project finance, capital market access
Direct lending	Provision of long-term senior loans to private sector borrowers or project companies	Long-term financing constraints	Infrastructure, energy, financial institutions, industrial projects

Equity investments	Direct equity stakes or investments through funds to support higher-risk or early-stage projects	Revenue and growth risk	Early-stage sectors, private equity funds, strategic industries
Investment funds / co-investment platforms	Participation in blended finance funds and structured vehicles to mobilize institutional capital	Market development and scale constraints	Blended finance facilities, sector-specific funds (e.g. climate, SMEs)

Seychelles’ 2016 transaction remains relevant because it shows how relatively smaller buybacks can still institutionalize durable governance through a dedicated fund vehicle. Public sources describe a buyback of roughly USD 21.4 million of debt and a mechanism to redirect repayments into a conservation and climate adaptation trust. For African countries where debt stocks are large, the scale effect is important: smaller swaps may not move headline debt ratios, but they can pilot the governance, reporting, and monitoring infrastructure required for larger future operations (UNFCCC, 2020).

The most transferable African template is arguably the “Debt-for-Development (D4D) swap” model, which generalizes nature swaps into a policy-linked refinancing platform. In this approach, the transaction is explicitly framed as restructuring external debt at a lower cost of borrowing using a sponsor-supported credit enhancement, with savings split between fiscal relief and ring-fenced domestic spending aligned to agreed priorities. The steps are conceptually simple, debt buyback at a discount, new financing on improved terms due to the wrap, and a development investment commitment funded by the savings.

The sovereign value proposition depends on integrating swaps into a DSA-anchored liability-management strategy rather than treating them as one-off ESG transactions. A robust approach starts with baseline and stress DSAs and uses those metrics (e.g., interest-to-revenue, GFN) to define quantitative “red lines” that any swap must improve. This distinction is important. If a transaction improves indicators under the baseline scenario but worsens tail risks, such as vulnerability to foreign exchange (FX) shocks, commodity price shocks, or the accumulation of contingent liabilities, it may ultimately weaken debt sustainability even if the ESG branding of the transaction appears attractive.

Anchoring swap evaluation to published DSA thresholds gives this recommendation operational content. The IMF’s Debt Sustainability Framework for Market Access Countries flags gross financing needs (GFN) above 15% of GDP and interest-to-revenue ratios above 25% as indicative of elevated vulnerability requiring close monitoring; for low-income countries under the LIC-DSF, the relevant thresholds are defined through the composite indicator and traffic-light system (IMF (2022), “Staff Guidance Note on the Sovereign Risk and Debt Sustainability Framework for Market Access Countries”). A well-designed swap should demonstrably improve at least one of these indicators, reducing GFN by smoothing redemption humps, or lowering the interest-to-revenue ratio through coupon reduction, without worsening others, particularly external debt service ratios or the stock of contingent liabilities. Stress-testing the post-swap debt profile against standard IMF shock scenarios (a 200-basis-point interest rate shock, a 30% exchange rate depreciation, and a growth shock of minus two standard deviations from the historical mean) provides a minimum analytical standard for assessing whether the transaction genuinely improves debt resilience or merely improves the baseline optics while leaving tail risks unaddressed. Finance ministries and their advisors should require this stress-tested DSA comparison as a condition of transaction approval,

and development partners structuring or guaranteeing swap transactions should make it a standard component of their due diligence documentation.

Debt transparency and fiscal accounting safeguards are essential because swaps can create complex contingent liabilities and opaque side agreements. A recurring critique is that some recent swaps have not met debt transparency expectations in terms of public disclosure of key documentation. OECD-facing analysis should therefore recommend minimum disclosure standards: legal terms of the new instrument (including arbitration clauses), insurance/guarantee triggers, collateral arrangements (if any), and the precise mechanism that transfers savings to the dedicated fund (AfronomicsLAW, 2023). DevTech’s Debt Transparency Monitor (DTM) demonstrates that transparency in disclosure of public debt information, financial reporting, and fiscal risk management can enhance fiscal credibility and improve governments’ engagement with international financial institutions. These improvements contribute to more favorable risk assessments and, in some cases, support stronger creditworthiness by enabling more informed and transparent fiscal decision-making.

Independent verification and performance measurement safeguards are necessary to avoid “greenwashing” and to protect the credibility of thematic sovereign markets. Market standards for thematic instruments typically rely on external review and verification, and concerns have been raised when second-party opinions or third-party verification are unclear in swap-linked issuances or swaps, the safeguard architecture must operate across three distinct layers. The first is use-of-proceeds verification, confirming that refinancing savings are actually transferred to the designated fund or programme rather than absorbed into general budget revenues. This requires contractually protected transfer mechanisms, independent trustee arrangements and ring-fenced accounting that is auditable by third parties, the governance structures used in the Belize and Gabon transactions provide a working template, though neither achieved full public disclosure of all legal documentation. The second layer is outcome verification, confirming that the environmental or development investments financed by the savings are delivering measurable results. This goes beyond financial reporting to require independently verified impact metrics: for marine conservation programmes, relevant indicators could include protected area coverage, enforcement patrol hours, fish stock assessments and ecosystem health indices; for climate adaptation programmes, relevant metrics could include avoided losses from extreme weather events and resilience scores for vulnerable populations. These indicators should be aligned with established international frameworks to ensure comparability across transactions and credibility with institutional investors increasingly subject to ESG disclosure requirements in their home jurisdictions. The third layer is framework integrity verification, confirming that the overall transaction structure — including the eligible debt definition, the pricing and discount mechanics, the savings calculation methodology and the governance arrangements — meets minimum market standards. For bond-financed swap structures, alignment with the International Capital Market Association (ICMA) Green Bond Principles or Sustainability-Linked Bond Principles provides a recognized baseline; the EU Green Bond Standard provides a more stringent benchmark for transactions targeting European institutional investors. Second-party opinions from recognized providers should be required, and their scope should explicitly cover the swap mechanics and savings-capture framework, not only the use-of-proceeds component. Transactions should meet these three layers of verification to strengthen their positioning as sustainable finance instruments.

A structural limitation of most market-facing debt-for-nature and sustainability swaps executed to date deserves explicit recognition. The Belize, Gabon and Seychelles transactions all involved the refinancing of dollar-denominated external debt with new dollar-denominated instruments, albeit on improved terms. While this approach addresses refinancing risk and can reduce interest costs, it does not resolve, and in some cases extends, the underlying currency mismatch that represents a first-order vulnerability for many African sovereigns. A government whose revenues are predominantly denominated in local currency but whose debt service obligations are in dollars faces an asymmetric exposure: exchange rate depreciation directly raises the real domestic cost of debt service, compresses fiscal space and can trigger rapid deterioration in debt sustainability metrics independent of the primary balance or growth trajectory. Swap transactions that exchange one dollar liability for another dollar liability with a longer maturity improve the temporal profile of this exposure but do not reduce its structural magnitude. For African sovereigns with significant commodity export revenues denominated in dollars, partial natural hedging may mitigate this concern; for others, particularly those with domestically oriented economies and limited foreign exchange earnings, extending dollar obligations through swap structures may improve short-term liquidity metrics while leaving the sovereign more exposed to exchange rate shocks over the extended horizon. Development partners and transaction structurers should therefore assess currency mismatch explicitly as part of swap due diligence, and where local currency financing is feasible, through domestic bond issuance supported by partial credit guarantees or currency hedging facilities such as those provided by the Currency Exchange Fund (TCX). should be evaluated as a complementary or alternative liability management strategy before defaulting to dollar-denominated refinancing structures.

Box 2 . Debt-for-nature swaps in practice: Gabon, Belize and Seychelles

Debt-for-nature and sustainability swaps combine liability-management operations with mechanisms that redirect part of the refinancing savings toward environmental investments. Transactions in Seychelles (2016), Belize (2021) and Gabon (2023) illustrate how these structures can reduce refinancing pressures while generating predictable financing for marine and biodiversity protection.

Country	Year	Debt refinanced	Maturity / debt impact	Coupon / cost impact	Conservation funding / savings capture
Seychelles	2016	About USD 21.6 million of external debt restructured through a debt buyback financed by concessional and philanthropic capital	Reduced debt service obligations and improved debt profile for a small island economy	Financing terms improved through concessional loans and guarantees provided by development partners	Creation of a Seychelles Conservation and Climate Adaptation Trust (SeyCCAT) to channel roughly USD 430,000 annually into marine conservation and climate adaptation programmes
Belize	2021	USD 553 million “Superbond” repurchased and refinanced through a USD 364 million Blue Loan, generating a USD 189 million principal reduction	Maturity extended by 6.5 years and weighted-average life increased	Blue Loan internal rate of return about 6.1%, significantly below distressed borrowing conditions prior to refinancing	Estimated USD 180 million in conservation financing over 20 years, including USD 4.2 million annual payments and a USD 23.5 million endowment expected to grow to about USD 92 million

Gabon	2023	Approximately USD 500 million of external bonds refinanced through a credit-enhanced blue bond structure	Bonds maturing in 2025 and 2031 replaced by a new bond maturing in 2038, significantly extending duration	New bond issued at about 6.1%, below coupons on the refinanced bonds (around 6.6–7%)	Commitment to allocate USD 5 million annually for 15 years to marine conservation and to capitalize an endowment expected to reach about USD 88 million
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These cases highlight two important lessons for sovereign debt management. First, debt-for-nature swaps operate primarily as liability-management operations that smooth repayment profiles and reduce refinancing risk, rather than as large reductions in the stock of debt. Second, the environmental impact depends on clearly defined “savings-capture” mechanisms that redirect a portion of refinancing gains into long-term conservation funds governed by transparent and independent institutions.

The development of domestic capital markets is itself a debt sustainability intervention. Deeper local currency bond markets reduce sovereign dependence on external financing, lower rollover risk during periods of international market stress, and support the development of a domestic institutional investor base whose liability structures are naturally aligned with long-term local currency assets. These structural benefits compound over time: each successful local currency issuance extends the yield curve, builds investor familiarity and reduces the information premium that domestic investors require for unfamiliar instruments. Blended finance programmes targeting domestic market development should therefore be evaluated not only on the immediate financing they mobilize but on their contribution to this structural deepening, a return that is diffuse, long-term and not captured in conventional mobilization metrics but that is central to the debt sustainability objective this paper advances.

The policy implication is that blended finance strategies for African sovereigns should incorporate a domestic market approach. This can be done by explicitly allocating a portion of available concessional and risk-sharing capacity to local currency instruments, even where the immediate mobilization volumes are smaller than foreign currency alternatives. A portfolio approach, combining foreign currency instruments for scale with local currency instruments for structural market development, better serves the long-term debt sustainability objective than a strategy that maximizes near-term mobilization at the cost of perpetuating currency mismatch.

THE STRATEGIC ROLE OF AFRICAN NATIONAL DEVELOPMENT BANKS (NDBS)

African NDBs vary so substantially in mandate, capitalization, governance model and market orientation that aggregate observations about the sector risk obscuring more than they reveal. A working typology helps discipline the subsequent analysis and allows more precise policy recommendations for different institutional archetypes. Two dimensions are most analytically useful for blended finance purposes. First, whether the institution operates primarily as a policy bank, deploying capital in direct pursuit of government development objectives, often with directed lending mandates and sovereign backstop, or as a commercially oriented development bank, operating with a development mandate but subject to financial sustainability constraints, credit discipline and market-based pricing. Second, whether the institution has meaningful capital market access, the ability to issue bonds domestically or internationally, borrow from MDBs on its own balance sheet, and attract institutional co-

investors, or relies on captive funding from government budget transfers, statutory deposits or compulsory savings schemes. These two dimensions generate four institutional archetypes with distinct implications for blended finance.

	Capital Market Access	Captive Funding
Commercial Orientation	Type I: Sophisticated blended finance platform; can structure layered transactions, attract private co-investors, issue thematic bonds. Examples: DBSA, TDB, CDG.	Type II: Commercially disciplined but funding-constrained; blended finance role limited by liability structure; priority is balance sheet strengthening and MDB credit lines.
Policy Bank Orientation	Type III: Policy mandate with market access; high potential for catalytic role but governance risk if lending decisions are politically influenced; requires strong ring-fencing of blended finance operations.	Type IV: Constrained on both dimensions; limited blended finance capacity in near term; priority interventions are capitalization, governance reform and technical assistance before blended finance structuring.

Table 2: Institutional Archetypes of Blended Finance

Applying Type I recommendations to Type IV institutions risks creating contingent sovereign liabilities without generating commensurate development impact. Type I institutions, exemplified by DBSA, TDB and Morocco's CDG, are the natural anchors for sophisticated blended finance platforms, thematic bond issuance and MDB co-financing arrangements. The policy recommendations in the following sections apply most directly to this archetype. Type IV institutions, which characterize a significant share of smaller African NDBs, require a sequenced approach: governance and capitalization strengthening must precede, rather than accompany, the deployment of complex blended finance structures.

AFRICAN NDBS AND LONG-TERM INVESTMENT

NDBs play a key role in financing long-term investment in African economies. Financial systems across much of the continent remain dominated by short-term lending structures and limited financial depth. In Sub-Saharan Africa, domestic credit to the private sector averages about 30–40% of GDP, compared with more than 100% of GDP in many emerging Asian economies, reflecting a relatively shallow financial intermediation capacity (WB, 2022). Bank lending is also concentrated in short maturities: in several African banking systems, over 70% of loans have maturities of less than five years, which reflects liquidity management practices, funding constraints and prudential regulations (IMF, 2025).

Commercial banks also allocate a substantial share of their balance sheets to sovereign securities rather than long-term project finance. Government bonds and treasury bills frequently represent 20–40% of total banking sector assets in several African countries, and in some cases an even higher share, as banks seek low-risk assets and comply with liquidity requirements. While these investments provide stability to banking systems, they can crowd out lending to long-term productive sectors.

The financing requirements of strategic investment sectors are significantly longer than the maturities available in domestic financial systems. Infrastructure projects, renewable energy investments, industrial development and agricultural value chains typically require financing horizons of 10–25 years, particularly where projects involve long construction periods and delayed revenue generation. However, most African banking systems rely heavily on short-term deposits as their primary funding source, which limits their ability to provide long-tenor loans without significant maturity mismatches.

The scale of investment needs further highlights the importance of institutions capable of mobilizing long-term capital. According to (AfDB, 2025), Africa requires approximately USD 130–170 billion annually in infrastructure investment, while current spending is estimated at USD 80–90 billion per year, leaving a financing gap of USD 40–100 billion annually. Similar financing gaps exist in sectors such as climate adaptation, industrial development and agricultural transformation.

This mismatch between long-term investment requirements and the structure of domestic financial systems creates persistent financing gaps in strategic sectors of African economies. In this context, National Development Banks play a critical role by providing longer maturities, structuring investment projects and mobilizing blended finance from development partners and private investors. By leveraging their balance sheets and policy mandates, NDBs can help bridge the gap between development objectives and available financial instruments in domestic and international capital markets.

NDBs help address the structural shortage of long-term finance. Their public mandate allows them to provide longer maturities and assume higher levels of risk than commercial lenders. In addition, development banks often adopt countercyclical lending strategies, maintaining credit flows during economic downturns when private lenders may reduce exposure. This stabilizing role is particularly important in economies that experience strong macroeconomic volatility or limited access to international capital markets.

NDBS CAN ACHIEVE GREATER IMPACT AS INTERMEDIARIES BETWEEN PUBLIC POLICY AND CAPITAL MARKETS

NDBs serve as institutional bridges between development strategies and financial markets. Governments typically define strategic priorities in areas such as energy transition, industrial development or SME financing. NDBs translate these policy objectives into structured investment programmes by preparing projects, structuring financing packages and mobilizing co-financing partners. Through these activities, development banks help transform policy priorities into investable opportunities.

Project preparation and pipeline development are core functions of development banks. Many investment opportunities in Africa fail to attract private capital because projects are not sufficiently prepared or structured. NDBs can address this constraint by supporting feasibility studies, transaction advisory services and financial structuring. By improving the quality of project pipelines, they reduce investment risks and make projects more attractive to private investors.

NDBS AS PLATFORMS FOR BLENDED FINANCE

Development banks are well positioned to structure blended finance transactions. Their hybrid institutional nature allows them to combine public mandates with financial expertise. This makes them natural intermediaries for structuring financing arrangements that combine concessional capital from development partners with commercial capital from private investors.

Blended finance structures implemented through NDBs typically involve layered capital arrangements. Development partners may provide concessional capital in the form of grants, guarantees or first-loss tranches. These instruments absorb part of the investment risk, improving the risk-return profile of projects for private investors. Private lenders and institutional investors can then participate in senior tranches with lower risk exposure.

Blended finance can significantly increase the leverage of limited public resources. By absorbing initial risks, concessional capital allows development banks to mobilize larger volumes of private investment. In several blended finance facilities supported by development finance institutions, leverage ratios between 1:4 and 1:10 have been achieved.

Well-capitalized development banks can mobilize investment at scale and play a catalytic role in economic transformation. By combining public policy mandates with market-based financing instruments, NDBs are able to structure financing solutions that support infrastructure development, industrial upgrading and climate transition. Their balance sheets allow them to provide long-term loans, guarantees, equity participation and blended finance structures that crowd in private capital. In sectors such as renewable energy, transport infrastructure or agribusiness value chains, development banks can assume higher levels of risk or longer maturities than commercial lenders, thereby enabling projects that might otherwise remain financially unviable. Through this catalytic role, well-capitalized NDBs can significantly increase the total volume of investment directed toward strategic sectors of the economy.

Strengthening NDBs can help mobilize investment while preserving the sustainability of sovereign balance sheets. In a context of rising global interest rates and tightening fiscal space, many African governments face increasing constraints in financing large public investment programmes through direct sovereign borrowing. Development banks offer an alternative institutional mechanism through which financing can be channeled toward productive sectors without immediately increasing central government debt. By mobilizing capital from multilateral partners, institutional investors and private lenders, NDBs can expand the pool of available financing while sharing risks across multiple actors. Their ability to structure blended finance platforms, investment funds and co-financing arrangements makes them particularly well suited to mobilizing private capital alongside public resources. As African economies seek to accelerate investment in infrastructure, industrial development and climate adaptation, NDBs are therefore likely to remain central institutions in the evolution of blended finance ecosystems across the continent.

Tighter fiscal space has increased reliance on development banks as financing platforms. Rising borrowing costs and growing debt-service obligations have constrained the ability of governments to finance large investment programmes directly through public budgets. In this context, NDBs offer an institutional mechanism through which investment can be mobilized while limiting direct increases in sovereign debt.

African development banks collectively represent a significant financial platform. Public development banks across the continent manage assets estimated at more than USD 500 billion, although the distribution of these assets is highly uneven across countries (AfDB, 2025). In economies where NDBs are well capitalized and professionally managed, these institutions can support investment in priority sectors while reducing pressure on public finances. More details are provided box.

Box 3. Case studies of African NDBs

Several African NDBs illustrate how development banks can mobilize capital at scale. These institutions provide practical examples of how development banks can support infrastructure development, private sector growth and climate finance.

The Development Bank of Southern Africa (DBSA) has become a major platform for infrastructure financing. DBSA manages assets exceeding USD 12 billion and finances projects across sectors including energy, transport, water and municipal infrastructure. The institution also manages climate finance facilities such as the Green Fund, which supports renewable energy and low-carbon infrastructure investments (DBSA, 2025).

The Trade and Development Bank (TDB) plays a major role in regional trade and infrastructure finance. With assets exceeding USD 10 billion, TDB provides trade finance, project finance and structured financing solutions to both public and private sector borrowers across Eastern and Southern Africa. Its regional mandate enables it to support cross-border investment and trade integration (TDB, 2025).

The Development Bank of Nigeria (DBN) demonstrates the effectiveness of wholesale lending models. Rather than lending directly to firms, DBN provides credit lines to commercial banks and microfinance institutions, which then extend financing to small and medium enterprises. Since its establishment in 2017, the bank has helped expand financing to hundreds of thousands of SMEs (DBN, 2024)s.

Morocco's Caisse de Depot et de Gestion (CDG) illustrates how development institutions can mobilize domestic institutional investors. CDG manages long-term public savings and invests in infrastructure, housing and strategic sectors of the Moroccan economy. Through investment funds and co-financing platforms, the institution channels domestic capital into large-scale development projects (CDG, 2025).

PARTNERSHIPS WITH MDBS AND BILATERAL DEVELOPMENT BANKS

International partnerships play a central role in strengthening the financial capacity of African NDBs. MDBs and bilateral development finance institutions frequently collaborate with African NDBs through co-financing arrangements, credit lines and risk-sharing facilities. These partnerships allow NDBs to access longer-term funding and diversify their sources of capital beyond domestic markets, which are often shallow and dominated by short-term instruments. By combining the balance sheets of multiple institutions, such arrangements increase the scale of financing available for infrastructure, climate investments and private sector development. They also allow development banks to structure more complex financial operations, including blended finance facilities that combine concessional capital with commercial funding.

MDB partnerships can significantly improve financing conditions and expand the operational capacity of development banks. Institutions such as the African Development Bank (AfDB), the World Bank Group, the European Investment Bank, Agence Française de Développement (AFD), KfW Development Bank, the Japan International Cooperation Agency (JICA) and the Korea Development Bank (KDB) provide a range of financial and technical instruments to African NDBs. These include long-term credit lines, subordinated debt, guarantees and technical assistance facilities. Access to such instruments can extend the maturity of NDB liabilities, reduce borrowing costs and improve the overall structure of their balance sheets. For example, AfDB and World Bank support to national development banks has enabled co-financing of large-scale regional infrastructure such as the North-South transport corridor in Southern Africa and energy interconnection projects under the West African Power Pool. Similarly, partnerships between KfW, AFD and local development banks have supported renewable energy investments, including solar and

hydropower projects in countries such as Morocco and Senegal. In East Africa, MDB-backed credit lines and guarantees have facilitated regional transport and logistics investments linked to the Northern Corridor, strengthening trade connectivity across Kenya, Uganda and Rwanda. In addition, MDB partnerships often support the strengthening of internal systems, including risk management frameworks, environmental and social safeguards, and project appraisal procedures. These institutional improvements enhance the credibility of NDBs and enable them to manage larger and more complex investment portfolios.

MDB participation also generates important signaling effects that help mobilize private capital. When international development institutions participate in transactions structured by NDBs, private investors often interpret their involvement as a signal of strong due diligence and project quality. MDBs typically apply rigorous project preparation standards, environmental and social safeguards, and monitoring mechanisms, which can reduce perceived risks for other investors. As a result, their participation can crowd in additional capital from commercial banks, institutional investors and impact investment funds. In several cases, MDB-backed transactions have enabled NDBs to structure financing platforms that attract private co-investors into sectors that would otherwise struggle to mobilize capital, such as renewable energy, infrastructure or SME financing. Through these catalytic effects, partnerships between NDBs and international development institutions can significantly expand the total volume of investment available for development projects while maintaining sound financial standards.

FINANCIAL INSTRUMENTS USED BY NDBS

African development banks deploy a wide range of financial instruments to address structural financing gaps in their economies. These instruments include guarantees, mezzanine financing, credit lines to commercial banks and co-investment funds targeting priority sectors such as infrastructure, energy, agriculture and SMEs. By using multiple financial tools, NDBs can respond to different types of market failures, including credit constraints, risk perceptions and limited access to long-term capital (AfDB, 2025).

Guarantees play an important role in expanding access to credit by reducing the risks faced by private lenders. Under guarantee schemes, development banks commit to covering a portion of potential losses in the event of borrower default. This partial risk coverage improves the risk-return profile of loans extended by commercial banks and encourages them to finance sectors that they might otherwise perceive as too risky. Guarantee facilities are particularly useful for expanding credit to SMEs, which often lack sufficient collateral or credit histories. They can also support infrastructure investments or climate-related projects with long gestation periods and uncertain revenue streams. By sharing risks with commercial lenders, NDBs can stimulate private sector lending while preserving market discipline (KOIS, 2022).

Mezzanine financing strengthens the capital structure of investment projects and facilitates the mobilization of private capital. Positioned between senior debt and equity in the capital stack, mezzanine instruments absorb losses before senior creditors while still providing a fixed-income return to investors. This subordinated position improves the security of senior lenders and can therefore attract additional commercial financing into projects that might otherwise struggle to secure funding. Mezzanine capital is particularly useful in sectors such as infrastructure, renewable energy or industrial development where projects require large upfront investments and where equity capital may be scarce. In addition to

providing flexible financing, mezzanine instruments can improve governance discipline because they may include conversion features that allow lenders to obtain equity participation in the event of default or restructuring.

Development banks also act as anchor investors in sector-focused investment funds to mobilize domestic and international capital. By committing capital to investment funds targeting sectors such as renewable energy, agribusiness or digital infrastructure, NDBs signal confidence in the underlying investment strategy. This anchor role can help attract institutional investors, including pension funds, insurance companies and sovereign wealth funds, that may be reluctant to invest in unfamiliar markets without a credible public partner. Co-investment platforms and blended finance funds managed or supported by development banks can therefore play an important role in scaling up investment in priority sectors. Through these mechanisms, NDBs help create investment ecosystems that combine public policy objectives with private sector financing.

GOVERNANCE AND CAPITALIZATION CHALLENGES

Strong governance is essential for the effectiveness and financial sustainability of development banks.

In several countries, African NDBs face constraints related to weak risk management frameworks, political interference or unclear institutional mandates. Because these institutions operate with public backing and policy mandates, weaknesses in governance can have significant fiscal implications. If lending decisions are driven by political considerations rather than sound financial analysis, development banks may accumulate non-performing loans and weaken their balance sheets. For example, past experiences in countries such as Nigeria and Ghana have shown that periods of weak governance and directed lending in state-owned financial institutions contributed to elevated non-performing loan ratios and required public sector intervention. In some cases, these risks can translate into contingent liabilities for the sovereign, particularly when governments are required to recapitalize underperforming institutions. Ensuring strong governance is therefore critical not only for the operational effectiveness of NDBs but also for preserving fiscal credibility and maintaining investor confidence.

Improving governance requires robust institutional frameworks and adherence to international best practices. Effective development banks typically operate under clearly defined mandates that distinguish policy objectives from day-to-day lending decisions. International experience highlights the importance of independent and professionally qualified boards, transparent appointment procedures for senior management and strong internal risk management systems. Institutions such as South African's DBSA and Morocco's CDG provide useful examples of governance frameworks that combine public mandates with professional management and relatively strong disclosure practices. Transparent financial reporting, including the publication of audited financial statements and disclosure of portfolio performance, is also essential to maintain accountability. In addition, strong credit appraisal procedures, environmental and social safeguards, and systematic monitoring of project outcomes help ensure that development banks allocate capital efficiently while managing financial risks. These governance mechanisms not only improve institutional performance but also enhance the credibility of development banks when they seek to mobilize funding from international capital markets and development partners.

Limited capitalization remains a structural constraint for many African NDBs. In several countries, development banks operate with relatively small balance sheets compared with the scale of national

investment needs. As a result, their ability to finance large infrastructure projects or to support industrial transformation programmes may be constrained. For example, while institutions such as DBSA or TDB have reached multi-billion-dollar balance sheets and can support large-scale regional projects, many smaller NDBs operate with significantly more limited capital bases, restricting their capacity to finance long-term investments.

The structural constraint of African NDBs is reflected in the overall size and distribution of assets across its banks. With assets and financing dominated by a handful of institutions, the development banking landscape remains characterized by a large number of relatively small and undercapitalized institutions. Although total financial assets of African NDBs increased by 14% (from USD 83 billion in 2018 to USD 94 billion in 2022), they still represent less than 1% of global NDB assets. In 2022, African NDB assets accounted for only about 3.4% of GDP, significantly below levels observed in other regions. By comparison, nine of the world's twenty largest NDBs are located in Asia, with a combined asset base exceeding USD 6 trillion, more than 60 times that of Africa (AfDB, 2025). Expanding the financial capacity of NDBs often requires a combination of measures, including government capital injections, long-term credit lines from multilateral development banks and access to international capital markets. Strengthening capital bases can also enable development banks to expand their lending portfolios while maintaining prudent capital adequacy ratios.

ANNEX

BLENDING FINANCE INSTRUMENTS AND STRUCTURING MECHANISMS

Blended finance relies on a combination of financial instruments that modify risk-return profiles to mobilize additional investment. These instruments operate across debt, equity and hybrid structures and can be deployed at project, fund or intermediary level. In practice, they are used to address specific financing frictions, including high cost of capital, elevated risk perceptions, weak project preparation and limited institutional capacity.

CONCESSIONAL CAPITAL

Concessional capital reduces financing costs and improves the overall structure of transactions. It typically takes the form of debt or equity provided on below-market terms, including lower interest rates, longer tenors, grace periods or subordinated positions. Its primary function is to reduce the weighted average cost of capital (WACC), enabling projects to reach financial viability without increasing the burden on the borrower.

Concessional capital can also play a risk-absorbing role within the capital structure. When deployed as subordinated or first-loss capital, it absorbs initial losses before senior investors are affected, thereby improving the risk profile of the transaction. In practice, concessional layers typically represent 10% to 40% of the capital stack, depending on sector risk and maturity (Convergence, 2025).

In sovereign and NDB contexts, concessional capital supports balance sheet strengthening and long-term lending. It can improve capital adequacy ratios, enable longer-tenor on-lending and support financing of infrastructure and transformation sectors. However, concessionality must remain targeted and time-bound to avoid distorting markets or creating dependency.

GUARANTEES AND RISK INSURANCE

Guarantees and insurance instruments reduce downside risk and improve access to finance. By transferring part of the credit or political risk to a stronger counterparty, they enhance the risk-return profile of investments and make them accessible to more risk-averse investors.

These instruments affect financing conditions through risk reduction, capital relief and pricing effects. Guarantees lower expected losses, may reduce regulatory capital requirements for financial institutions and compress risk premia, thereby improving pricing and extending maturities.

A range of guarantee structures can be deployed depending on the risk addressed. These include partial credit guarantees, partial risk guarantees, portfolio guarantees, first-loss guarantees and political risk insurance. Coverage levels typically range between 30% and 80% of exposure and must be carefully calibrated to ensure additionality without crowding out private risk-taking (OECD, 2021).

In sovereign applications, guarantees can improve debt profiles and capital market access. They can support longer maturities, reduce spreads on bond issuances and contribute to domestic market development. However, they also create contingent liabilities that require transparent fiscal reporting and integration into debt management frameworks.

DESIGN-STAGE GRANTS (PROJECT PREPARATION)

Project preparation is a critical constraint in many investment environments. Upfront costs for feasibility studies, environmental assessments and transaction structuring can represent 3% to 10% of total project costs, which can be prohibitive in low-capacity contexts (OECD, 2018).

Design-stage grants address early-stage risks and improve project bankability. By financing technical studies, advisory services and proof-of-concept activities, they reduce uncertainty and strengthen the credibility of investment proposals before commercial capital is mobilized.

These instruments are particularly relevant for complex or innovative transactions. They support the development of public-private partnerships, aggregation models for small-scale producers and the structuring of thematic or innovative financial instruments.

In sovereign contexts, design support contributes to market development. It can help establish benchmark yield curves, structure refinancing platforms and prepare blended finance facilities anchored in National Development Banks.

TECHNICAL ASSISTANCE FACILITIES

Technical assistance facilities (TAFs) strengthen the implementation capacity and governance of blended finance operations. They provide grant-funded advisory support to improve operational performance, financial management and impact measurement.

TAFs are typically embedded alongside investment vehicles. They often represent 5% to 15% of total facility size, reflecting the importance of addressing non-financial constraints to ensure effective deployment of capital (Convergence, 2025).

These facilities operate at both firm and system levels. They support borrowers through capacity building and compliance, while also contributing to regulatory improvements, market development and institutional strengthening.

In sovereign and NDB contexts, technical assistance can directly improve credit fundamentals. It can enhance debt management practices, strengthen auction systems, improve credit risk assessment and support environmental and social standards. These improvements reduce both real and perceived risk, contributing to better financing conditions over time.

FIRST-LOSS AND SUBORDINATED CAPITAL

First-loss capital is a key instrument for reallocating risk within blended structures. It absorbs initial losses, thereby protecting senior investors and improving the overall attractiveness of the investment.

This mechanism is widely used in structured funds and pooled vehicles. By altering the loss distribution, it reduces expected losses and tail risks for senior tranches, making them compatible with the risk-return requirements of institutional investors such as pension funds and insurance companies.

The size and calibration of first-loss tranches are critical. They typically represent 10% to 25% of total capital, depending on sector risk and portfolio diversification. In large or complex portfolios, modelling default correlations and loss distributions requires advanced techniques and robust data.

For NDBs, first-loss capital expands risk capacity and supports strategic sectors. It can enable SME lending, support infrastructure financing and strengthen co-lending platforms with commercial banks.

Additionality remains the key policy criterion. First-loss capital should be deployed only where it demonstrably mobilizes private investment that would not otherwise occur.

RESULTS-BASED FINANCING

Results-based instruments link financing to measurable outcomes rather than inputs. These include development impact bonds, pay-for-success contracts and performance-based grants.

They shift performance risk from the public sector to investors. Private capital finances service delivery upfront, and repayment occurs only if predefined outcomes are achieved.

These instruments improve accountability and efficiency. By tying payments to results, they incentivize better monitoring, data collection and service delivery, particularly in social sectors.

In fiscal terms, results-based mechanisms can improve expenditure efficiency. They direct resources toward effective interventions and can reduce long-term liabilities by rewarding only proven outcomes. However, they require strong data systems and independent verification frameworks.

DEBT, EQUITY AND HYBRID INSTRUMENTS

Blended finance structures rely on conventional financial instruments adapted to specific risk profiles.

Debt instruments are suited to projects with predictable cash flows, while equity is appropriate for higher-risk activities where returns depend on long-term growth.

Hybrid instruments, such as mezzanine finance, provide additional flexibility. Positioned between debt and equity, they offer subordinated claims and flexible repayment structures. They can strengthen capital bases and improve leverage ratios while preserving incentives for performance.

Instrument selection must reflect sector characteristics and financial risks. Factors such as revenue stability, project maturity and currency exposure are critical. Poor alignment between instruments and underlying economic fundamentals can create financial vulnerabilities.

INTEGRATION WITH DEBT AND CAPITAL MARKET STRATEGIES

Blended finance instruments should be integrated into broader debt and capital market strategies.

When properly designed, they can support the development of domestic bond markets, strengthen yield curves and improve access to local currency financing.

For sovereigns and NDBs, blended structures can improve financial resilience. They can extend maturities, enhance capital adequacy and reduce foreign exchange mismatches. However, fragmented or poorly coordinated use of blended instruments may increase complexity without strengthening financial stability.

BLENDED FINANCE AS A COMPLEMENT TO STRUCTURAL REFORM

Blended finance instruments are not substitutes for sound economic fundamentals. While they can improve risk allocation and financing conditions, they cannot compensate for weak fiscal management, regulatory instability or inadequate policy frameworks.



Their effectiveness depends on alignment with broader reform agendas. When embedded in credible debt sustainability strategies and development plans, blended finance can mobilize long-term capital at scale. When misaligned, it may increase complexity and obscure underlying risks.

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