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World Bank instrument to facilitate sustained investment in private sector fundraising

Summary

UNICEF is pleased to provide the Executive Board with this document that outlines a financial instrument being developed to facilitate a sustained level of investment in private sector fundraising. The financial instrument will entail an arrangement between the World Bank and UNICEF to raise additional financing for investment in private sector fundraising, leveraging the services and expertise of the World Bank in the financial markets The instrument will also help UNICEF to respond to the impacts of the coronavirus disease 2019 (COVID-19) pandemic.

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I. Overview

1. UNICEF is developing a financial instrument to generate resources to facilitate the necessary level of investment in private sector fundraising for an impactful income that can help finance the organization's country programmes of cooperation. The financial instrument consists of an issuance of notes by the World Bank under its Capital at Risk Notes programme and a forward flow arrangement between UNICEF and the World Bank, under which UNICEF will make payments to the World Bank in respect of such issuance, for an amount expected to be approximately $50 million. The payments will be calculated based on future donations to UNICEF from unearmarked private sector fundraising monthly pledge donors in 18 emerging-market countries. The financial instrument proceeds will be utilized strategically in these 18 countries to retain existing donors, to acquire new donors to replace those lost through natural attrition and to widen the donor base. The financial instrument is described in further detail in section III below.

2. Approximately $50 million[1] in proceeds to UNICEF from the forward flow arrangement will be used to finance the growth of private sector fundraising, which, together with other investments, is expected to yield $450 million from private monthly pledge donors in emerging markets over a five-year period. This instrument will be an innovative way of collaborating with the World Bank to increase investment in private sector fundraising. It will generate significant resources to repay the interest and the instrument upon its maturity while making substantial resources available to fund UNICEF country programmes.

3. UNICEF is seeking a decision from the Executive Board to give authority to the Executive Director, based on the advice of the Comptroller, to issue the financial instrument in partnership with the World Bank. A draft decision in this regard is included in the item "Private Fundraising and Partnerships: 2021 workplan and proposed budget".

II. Scope and objectives

4. UNICEF raises a substantial percentage of its private sector income from emerging markets in Asia, Europe and Latin America. Most of the income is composed of monthly pledge instalments from individual donors. The 18 countries from emerging markets that have an active programme for private sector fundraising collectively raised, $130 million in 2019, from 1.4 million individual monthly pledge donors; donations from these countries had a compound annual growth rate of 20 per cent since 2010.

5. A large part of this income is invested locally in the country of donation origin to support the country programme, and some of it contributes to regular resources (RR) for the global programme activities of UNICEF. Some of the country offices in these markets (e.g., Argentina, Thailand and Uruguay) are large contributors to RR.

6. The long-term growth of private sector income in these markets depends on the level of investments made (investment funds) to acquire new donors, replace lapsed donors and increase the overall pool of donors generating monthly income.

7. Based on the actual and projected reduction in RR and the consequent reduction in investment funds available to country offices, UNICEF is looking for ways to use its future donation cash flows to increase – the current investment funds available for

[1] The figures used in this document are based on an assumed issuance size by the World Bank of $100 million.

private sector fundraising activities. UNICEF has identified as a key priority to ensure full funding and RR growth the need for alternative sources of funding to support private sector fundraising growth in emerging markets. UNICEF is seeking to accomplish this by participating in a financial instrument (the Child Bond), which will be issued by the World Bank.

8. The proposed financial instrument will provide additional sources of investment in private sector fundraising activities in emerging markets. These additional sources of investment will complement the current investment funds that are available from RR to ensure full funding of country programmes and support growth in RR. The financial instrument will also leverage the appetite of capital markets for investment in the Sustainable Development Goals.[2] The financial instrument is the first time a United Nations agency (UNICEF) and the World Bank will jointly use a financial instrument to leverage capital markets to finance United Nations operations and fundraising, and spur increasing United Nations system collaboration and partnership.

9. The proposed financial instrument aims to finance the growth of private sector fundraising individual monthly giving in 18 emerging market countries. The proposed financial instrument will raise funding of approximately $50 million, which, together with income generated by existing and new monthly pledge donors, will yield cumulative amount of $450 million over five years in vital funds for UNICEF country offices.

III. Proposed arrangement of the financial instrument

10. It is expected that the World Bank will issue notes with a maturity of five years under its Capital at Risk Notes programme,[3] in aggregate principal amount of $100 million. The proceeds from this issuance will be apportioned between the World Bank and UNICEF, pursuant to a forward flow arrangement between the World Bank and UNICEF. Under the forward flow arrangement[4] between the World Bank and UNICEF, UNICEF will be required to transfer to the World Bank an amount equal to a predetermined amount of future donations from private sector fundraising monthly pledge donors in 18 emerging market countries, which will be used to repay the principal amount of the notes, plus the UNICEF portion of the periodic interest payment under the notes (subject, in all cases, to receipt by UNICEF of sufficient donations during the relevant five-year period to cover such payments).

11. This financial instrument is expected to be denominated in United States dollars and sold to one or more investors globally. In this issuance, the financial instrument is expected to be sold through a private placement (to one or more investors), and it is not expected to be externally rated. Preliminary conversations between the commercial bank acting as underwriter and the potential investors indicate sufficient market appetite without the need for an external rating.

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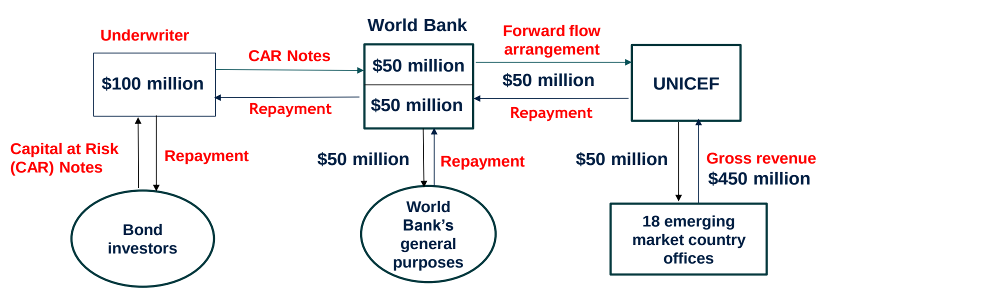
[2] United Nations, *United Nations Secretary-General's Roadmap for Financing the 2030 Agenda for Sustainable Development: 2019–2021*, New York, 2019.

[3] The World Bank Capital at Risk Notes programme facilitates risk transfer solutions for the World Bank and its clients using capital markets. Capital at Risk Notes are issued under the Global Debt Issuance Facility of the World Bank and receive the same tax and securities law exemptions, but may be assigned a lower security rating than the Facility, or may not be assigned any security rating.

[4] UNICEF will report periodically on the cash flow generated from emerging markets until the $50 million is reached. As a reference, in 2020, UNICEF reached $50 million in such cash flow in the second quarter of the year.

12. The World Bank is already an established partner to UNICEF. Since the start of the coronavirus disease 2019 (COVID-19) pandemic, UNICEF has partnered with the World Bank in more than 40 countries to support national emergency response projects in risk communication, community engagement, water, sanitation and hygiene, health system strengthening, nutrition and supplies. In total, UNICEF has signed 64 agreements with the World Bank totalling $270.4 million since April 2020. The World Bank is a global issuer of financial instruments such as bonds, that support the Sustainable Development Goals. The financing of the Sustainable Development Goals requires an annual investment of $5 to $7 trillion, and the World Bank plays a pivotal role in the capital markets for Sustainable Development Goals-related bonds, issuing approximately $55 to $65 billion in bonds linked to the Goals each year. For example, in April 2020, the World Bank sold its most successful Sustainable Development Goal bond, which raised a record $8 billion with an order book of $12.5 billion from 190 investors.

Child Bond – Illustrative structure and flows



- The Bank issues a bond to investors through its Capital at Risk Notes programme for $100 million.
- The Bank retains $50 million for its general sustainable development purposes.
- The Bank enters into the forward flow arrangement with UNICEF under which the Bank pays $50 million to UNICEF on the settlement date as payment for a future stream of donation cash flows.
- UNICEF will repay the $50 million with the overall income from pledge donors in emerging markets ($130 million in 2019 and 1.4 million donors, $450 million projected by 2025).
- UNICEF will repay the interest coupons and principal from gross income as first or senior payment before other costs.
- Repayment terms is five years; first issuance will be a non-rated bond.
- World Bank and UNICEF could in the future consider this as an annual programme with annual issuance.

IV. Repayment approach and associated costs

13. **Principal repayment**. To ensure that UNICEF can repay to the World Bank the UNICEF share of the principal amount (i.e., $50 million) at maturity of the notes (i.e., after five years), and for the purposes of the UNICEF internal budget, the 18 country offices receiving funds from this issuance are expected to start repayment to an internal set-aside fund from the third year. This allows them two years to invest these funds in private sector fundraising activities to generate additional resources. By year three, the investment is projected, based on data trends, to generate enough resources for UNICEF to start setting aside funds for accumulation and repayment. Funds that have been set aside can be invested until the principal is due. Investment will be carried out by the UNICEF Treasury and Structured Finance Services section within the Division of Financial and Administrative Management.

14. **Coupon (interest) payments**. Interest on the financial instrument is payable on a semi-annual basis. Payments by UNICEF to the World Bank in respect of interest payments under the notes for the first two years will be made from the special purpose

budget for private fundraising and partnerships; thereafter, payment will be made from income generated from the fundraising that has resulted from investment of the financial instrument proceeds.

15. The total interest expense on the financial instrument is estimated to be between 1 per cent and 1.5 per cent of the principal. Additional costs for the financial instrument issuance will include legal fees, bank underwriting fees and service fees to the World Bank. These will be paid from the income generated during the five years.

V. Value and impact for UNICEF

16. The proposed financial instrument has several advantages and is expected to have a positive impact on UNICEF. It will contribute to generating an estimated target of $450 million as part of the overall cumulative income generated by existing and newly acquired pledge donors in emerging markets in the 18 countries. This will potentially allow a greater proportion of private fundraising and partnerships special purpose funds for investment in fundraising to be repurposed to National Committees and other private sector fundraising channels. It will pave the way for a unique partnership with the World Bank to use financial instruments to support financing of the growth and operations of UNICEF. The most important impact will be additional financing of the organization's programmes in the target countries and globally.

17. This is the first time that a financial instrument of this type will be offered by the World Bank to a United Nations organization. This makes UNICEF a pacesetter for other United Nations organizations and creates alternative modalities for the United Nations to leverage capital markets. The financial instrument will also provide much-needed flexibility to use its proceeds in the emerging markets that deliver the best return on investments.

VI. Risks and proposed risk management

18. The first risk is related to the potential lack of return on investments, with investments not generating enough resources to repay the World Bank upon the maturity of the financial instrument. However, as illustrated above, the historical cash flow from monthly pledge donors in the 18 countries, converted into United States dollars, is robust in terms of cumulative income over an extended period of time. In addition, UNICEF is required to make payments to the World Bank only to the extent that private donations received by UNICEF during the term of the notes exceed the principal amount received by UNICEF from the World Bank on issuance of the notes. There should therefore be no risk to UNICEF of facing a payment obligation that it cannot meet.

19. This cash flow from monthly pledge donors in the 18 target countries has experienced a compound annual growth rate of 20 per cent since 2010. In 2019, total cash flow from these monthly pledge donors was $130 million – or 2.6 times the $50 million financial instrument amount. Most recently, in the first and second quarters of 2020, the monthly pledge income from these same countries experienced an 8 per cent increase compared with 2019, with pledge income totalling $77.5 million over the first two quarters of 2020. From the perspective of repayment, a $50 million principal payment represents only 8 per cent of $450 million over the next five years, assuming a 3:1 return on investment from year three to year five.

20. A second risk is potential currency volatility in the 18 emerging markets whose cash flows are the source of repayment of this financial instrument. The agreement

with the World Bank is expected to require payments by UNICEF to the World Bank in United States dollars. Historically, the growth of cash flows in the 18 countries has been more than enough to cover currency volatility against the United States dollar, and thus the overall cash flow in United States dollars from these countries has shown constant growth from year to year, despite currency fluctuations that may occur in one or more of these markets at any given time. For example, when the Argentine currency experienced high historical volatility against the United States dollar, this was compensated by flows from other countries.

21. A third potential risk is the capacity of the 18 country offices targeted to deploy the proceeds of the financial instrument (i.e., approximately $50 million) to make investments for private sector fundraising. However, the absorption capacity of these offices is already substantial and growing, and overall, they have had a return on investments consistently as strong as 3:1 since 2010. For example, the total need for such investment for the 18 countries is $58 million just for 2021, well above the $50 million from this financial instrument. Strategic implementation of the $50 million in 2021 will be supported by detailed planning within the country offices and will be closely monitored by the Division of Private Fundraising and Partnerships and the regional support centres.

Total private sector fundraising investment needed in 2021
(in millions of United States dollars)

East Asia and the Pacific	23 600 000
Latin America and Caribbean	20 200 000
Country offices in other UNICEF regions	2 200 000
Additional fundraising opportunities	12 000 000
Total	**58 000 000**

22. A fourth potential risk is related to the capacity to document the impact of the private sector fundraising income generated from the proceeds of this financial instrument. Documenting the ultimate impact of this financial instrument on the lives of children and families in the 18 countries is extremely important. The primary means of data collection – both quantitative and qualitative – as well as reporting mechanisms to meaningfully document impact already exist in these country offices. To report on the impact of the financial instrument, information will be drawn from existing data and evidence streams and organized around the areas of the Strategic Plan, 2018–2021: Every child survives and thrives, learns, is protected from violence and exploitation; lives in a safe and clean environment, and has an equitable chance in life. Because the potential investors will be new or non-traditional donors, UNICEF will adapt existing types of reports to make them appropriate and accessible to this new audience.

23. A final area of risk includes the potential exposure of UNICEF to criticism for using donations to repay principal and interest on a financial instrument. However, all monthly pledge donations are unrestricted and are contributions towards the overall mandate of UNICEF; they are not earmarked for a specific use, and there is no requirement for any donations to be segregated or retained by UNICEF to meet its obligations on the financial instrument. In addition, the following features demonstrate the overall positive benefit to the organization's purposes and sources of funding:

(a) UNICEF, through this financial instrument, will be able to obtain a 3:1 return on pledge donations, which will increase the value of pledge donations and enable them to accelerate impact for children.

(b) UNICEF is diversifying its sources of funding and supporting its country programmes by financing private sector fundraising activities.

(c) UNICEF is not relying solely on grant money (RR) to accelerate implementation of its Strategic Plan, the response to the COVID-19 pandemic and the 2030 Agenda for Sustainable Development.

VII. Conclusion

24. Given the challenging global environment, combined with the increased demand and expectation for UNICEF to deliver more due to the COVID-19 pandemic, it is vital to utilize financial instruments to leverage the potential of capital markets to support the Sustainable Development Goals. This proposed financial instrument will diversify the sources of funds needed to grow private sector fundraising income in emerging markets, so that country programmes in these markets will not have to rely exclusively on RR and the regular budget to fund their private sector fundraising activities.

25. Through this innovative partnership with the World Bank, whereby UNICEF benefits from its Capital at Risk Notes programme, UNICEF will have a unique opportunity to tap into new capital sources to grow resources in emerging markets while minimizing the risks involved. This will be accomplished by trading on part of the robust and stable cash flows from private sector fundraising activities in 18 emerging market countries.

26. UNICEF seeks approval from the Executive Board to move forward with this innovative financial instrument as an efficient and effective response to the reduction in RR and resulting reductions in investments for private sector fundraising, and as a tool to support long-term growth.