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BUILDING A JUST WORLD
AND A SUSTAINABLE PLANET

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SESSION 5: FINANCING DEVELOPMENT: CAPITAL FLOWS, GLOBAL DEBT AND MDBs REFORM

G20 Progress Report

Implementing the Recommendations of the G20 Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks

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CONTENTS

I. EXECUTIVE SUMMARY

This report reviews the progress of multilateral development banks (MDBs) in implementing the 17 recommendations proposed by the G20 Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks in its report of July 2022. Building on a similar effort undertaken by the Indian G20 presidency in 2023, the report takes stock of reform implementation and provides forward-looking guidance to continue reform progress.

The capital adequacy framework (CAF) agenda is increasingly well embedded across the MDB system. Compared to nine MDBs reporting in the previous exercise, 15 MDBs responded to requests for information this year and two others are observing the process closely with a view to participating in 2025. This is a testament to the continued relevance of the CAF reforms as a key component in the broader agenda of strengthening MDBs to help address the development challenges facing our world.

Overview of recommendation implementation

Implementation has progressed notably in the past year, although substantial work remains on several recommendations. CAF-linked reforms have already opened up $170 billion in additional lending headroom across the major MDBs, with $113 billion more projected to be finalized by end-2024 and more gains expected going forward. Beyond headroom, the CAF agenda has promoted convergence toward generally agreed standards on MDB capital adequacy issues among shareholders, market actors and the broader development community, and has encouraged MDBs to increasingly see themselves as a common set of institutions benefiting from greater coordination and collective action.

Recommendations related to core capital adequacy (1a-1c) and callable capital (2a) have progressed since July 2023 but still fall short of expectations, in part due to the complexity and sensitivity of the issues involved. Remaining reforms include prioritizing internal metrics in setting CAF risk thresholds, collectively establishing MDB-wide standards for preferred creditor status and portfolio concentration risk and valuing callable capital in CAFs. While the benefits of these reforms are not easily quantified, they are deep and long-lasting: capital adequacy gains means that every dollar of shareholder capital will work even harder for development outcomes, every year going forward for as long as the MDBs operate. Further reform effort is merited.

Financial innovation and balance sheet optimization (Recommendations 3a-3f) have advanced considerably and can be considered on track. MDBs have successfully piloted a variety of new financial innovations such as hybrid capital and risk transfers, partly spurred by the CAF report and also building on earlier balance sheet optimization efforts supported by the G20. These innovations show significant potential going forward. It is incumbent on the MDBs to work together to achieve greater scale, while remaining mindful of the limits and trade-offs involved.

Collective engagement with credit rating agencies (CRAs) (4a-4c) has accelerated and deepened, with a growing number of MDBs working together to present evidence and feedback as input to CRA methodologies. Issues around CAF governance and information (5a-5d) have shown some gains, but shareholder governments may want to consider if and how they might wish to press ahead. Work is ongoing in some areas (such as benchmarking and GEMs), while board capacity for CAF issues and system-wide information arrangements have seen uneven progress across MDBs.

Financial Headroom Gains Thus Far from CAF Reforms

Caution must be taken in assessing financial gains due to CAF reforms, as many reforms will take time to materialize, depend on factors not always under MDB control and, in some cases, are intended to promote improved CAF governance and broadly accepted standards across the asset class without immediate or direct headroom benefits. Efforts to generate precise estimates can be misleading and may distract from the content of needed reforms. Nonetheless, it is informative to have a broad sense of how recommendations have translated into MDB lending gains to better evaluate system-wide operational capacity and to share CAF reform experiences.

Collectively, MDBs report that CAF reforms already have unlocked around $170 billion in lending headroom to be deployed in the coming decade across the reporting MDBs, with $113 billion more projected to be finalized by end-2024 and an additional $74 billion targeted. This total of $357 billion is in line with the $300-400 billion estimated in the Heads of MDBs Viewpoint note of April 2024 for CAF reforms across the major MDBs over 10 years. Much of the targeted headroom is expected to be driven by hybrid capital and risk transfers to commercial and official counterparties as described in Recommendation 3, although the final amounts will depend on investor demand and market conditions. Other balance sheet measures related to the CAF agenda but not specifically recommended in the CAF report have already generated an additional $7 billion in lending capacity and are projected to create a total of $41 billion in coming years.

Should shareholders and MDBs press ahead with Recommendations 1 (adjusting CAFs) and 2 (incorporating callable capital), this could result in substantially more gains beyond the $357 billion reported by the MDBs.

Separately, MDBs and shareholders could consider setting CAF risk limits without the constraint of always needing to achieve a AAA rating from all three major CRAs. This would potentially allow for more flexibility given the significant variation across CRA methodologies. This approach would aim to retain a AAA with all three CRAs but accept the possibility of having only two AAAs in certain circumstances and depending on shareholder-defined priorities. The potential impacts on MDB funding market access would need to be thoroughly investigated prior to such a policy change.

The G20's role going forward

The role of the G20 and the International Financial Architecture Working Group is crucial to drive this agenda forward, all the more now that the "low-hanging fruit" have been plucked and a more challenging reform agenda lies ahead. Many CAF reforms requiring further progress revolve around MDBs as a unique sector or asset class that lacks commonly accepted standards to orient stakeholders and enable more efficient use of resources. The G20 is well positioned to facilitate the collective approach needed to make that happen.

Substantial further gains can be achieved with concerted effort by MDBs with the strong backing of the G20. CAF reforms by themselves are not replacements for core equity capital, which is the bedrock of MDBs' financial strength and market reputation. But systematically and collectively following through with the CAF reforms—improved risk assessment, better utilizing paid-in and callable capital, financial innovations and engagement with rating agencies—will allow all stakeholders to have a common basis for understanding MDB financial capacity to inform discussions on how to match available capital with development ambitions, to the extent possible and together with other development partners.

II. BACKGROUND

The G20 Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks was established under the 2021 G20 Italian presidency. As defined in the terms of reference,[1] the objective of the review was to:

- Provide credible and transparent benchmarks on how to evaluate multilateral development bank (MDB) capital adequacy frameworks (CAFs)
- Enable shareholders, MDBs and CRAs to develop a consistent understanding of MDB CAFs
- Encourage shareholders to consider potential adaptations to the current frameworks to maximise MDB financing capacity

The Independent Review delivered its report in July 2022 under the Indonesian presidency to G20 finance ministers and central bank governors, who agreed to make the report public. The report contained 17 recommendations grouped in five areas:

- Adapt approach to defining risk tolerance
- Give more credit to callable capital

1. G20 (2021). "An Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks Terms of Reference", 9-10 July 2021.

- Expand use of financial innovations
- Improve credit rating agency assessment of MDB financial strength
- Increase access to MDB data and analysis

At the November 2022 Bali Summit, G20 leaders called for an implementation roadmap for these recommendations, which was tasked to the International Financial Architecture Working Group (IFA WG) in 2023 under the Indian presidency. The first CAF implementation roadmap was delivered in July 2023, building on information gathered from MDBs in a standardized reporting template to facilitate comparability and uniformity. The first report presented implementation updates from AfDB, ADB, AIIB, EBRD, EIB, IDB, IsDB, NDB and the World Bank Group (WBG); independently assessed progress to that point; and pointed to future directions for further reform.

In light of the positive reception and perceived utility of the roadmap and the continued high relevance of CAF recommendations within the broader MDB reform agenda, a second round of reporting was considered appropriate under the Brazilian G20 presidency. The proposal was discussed at the IFA WG meeting in April 2024 and received strong support from the membership.

Based on updated CAF implementation reporting by 15 MDBs, this report was prepared for consideration and discussion at the IFA WG meeting in Fortaleza on June 10-12. It was subsequently revised based on feedback from G20 members and MDBs for submission to the Finance Ministers and Central Bank Governors meeting in July 2024.

III. OBJECTIVE OF THE PROGRESS REPORT

The CAF agenda is increasingly well embedded across the MDB system. Compared to nine MDBs reporting in the previous exercise, 15 MDBs reported this year. This includes two new MDB participating (Development Bank of Latin America—CAF and Caribbean Development Bank—CDB) and disaggregated reporting by the major operational divisions of the World Bank Group (IBRD, IDA, IFC and MIGA) and the IDB (IDB and IDB Invest). The Council of Europe Development Bank (CEB) and FONPLATA were invited to submit this year but chose to closely follow the exercise with a view to reporting next year.

This next iteration of progress reporting is intended to anchor discussions on CAF-related issues moving forward. The objective mirrors that of 2023 in providing forward momentum to continued reforms by undertaking two key tasks:

- Taking stock of the implementation status of CAF recommendations based on MDB updates.
- Providing forward-looking G20 guidance on how to expand and accelerate implementation of the recommendations subject to each MDB’s governance structure and mandate.

The reporting template given to the MDBs was revised slightly, seeking to simplify the reporting burden by building on lessons learned from the previous reporting process and the numerous CAF-related developments in the intervening year. A draft revised template was shared with IFA WG in April, and the final version incorporated comments from members as well as MDBs.

Fifteen MDBs completed the reporting template and reverted to the IFA WG in a timely fashion: African Development Bank (AfDB), Asian Development Bank (ADB), Asian Infrastructure Investment Bank (AIIB), Caribbean Development Bank (CDB), Development Bank of Latin America (CAF), European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB), the Inter-American Development Bank (IDB and IDB Invest), Islamic Development Bank (IsDB), New Development Bank (NDB) and the major divisions of the World Bank Group: International Bank for Reconstruction and Development (IBRD), International Development Association (IDA), International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA). CAF and CDB participated in the reporting exercise this year for the first time, while CEB and FONPLATA are expected to join in the next round.

The G20 is grateful to the management of the MDBs for their constructive engagement in this process, timely responses and transparency in sharing information.

IV. MDB SELF-REPORTED PROGRESS ON IMPLEMENTING CAF RECOMMENDATIONS

Progress on implementing all 17 CAF recommendations was reported by each MDB, as summarized in Table 1 below. For every recommendation, each MDB is grouped into one of four categories based on their response:

- Implementation completed
    - *Note: This may indicate that implementation is ongoing but advancing strongly and with momentum*
- Implementation underway
- Implementation under consideration
- Not considered appropriate

Table 1 represents the assessments of the MDBs themselves. The subsequent section provides an independent evaluation of implementation progress undertaken by the technical team working for the Brazilian G20 presidency. In some cases MDB self-reporting differs from the independent evaluation. This is in part the result of MDBs including elements in their reporting that are related to capital adequacy but were not included in the CAF recommendations, and also because MDB responses at times reflect a broader interpretation of CAF recommendations than that spelled out in the G20 CAF report. The discrepancies are noted in the evaluation section and may form a useful basis for discussion between G20 members and MDBs on the current progress and future trajectory of CAF reforms.

Table 1: Self-reported update by MDBs on the implementation of CAF recommendations

Implementation completed	Under implementation	Implementation under consideration	Not considered appropriate
1a Shift risk appetite definition toward shareholder-defined limits			
ADB, AfDB, AIIB, EBRD, EIB, IBRD/IDA, IDB, IFC, IsDB, NDB	CAF, CDB		
1b Ensure frameworks account for MDB-specific features			
ADB, AfDB, EBRD, EIB, IDB, IBRD/IDA	CDB, IsDB	AIIB, NDB	CAF, IFC
1c Relocate specific numeric leverage targets from MDB statutes			
	ADB, EBRD, IBRD/IDA	AfDB, AIIB, EIB, IDB, CDB	CAF, IsDB, IFC, NDB
2a Incorporate uplift from callable capital into MDB capital adequacy frameworks			
EBRD, IBRD/IDA, IDB	IsDB	AIIB, CDB	ADB, AfDB, CAF, EIB, IFC, NDB
3a Endorse MDB consideration of non-voting capital classes (paid-in equity or hybrid) to contribute to available capital.			
AfDB, IBRD/IDA	ADB, CDB, EBRD, IDB, IsDB	AIIB, CAF, IFC, NDB	EIB
3b Scale portfolio risk transfers to the private sector of MDB non-sovereign loans to facilitate additional lending			
ADB, AfDB, AIIB, EBRD, IBRD/IDA, IDB	IFC, NDB	CAF, CDB, EIB, IsDB	
3c Encourage shareholder guarantees on loans related to crosscutting priorities			
ADB, AfDB, EBRD, EIB, IBRD/IDA, IDB	IsDB, CDB	AIIB, CAF	IFC, NDB
3d Support collective shareholders commitments of pools of additional callable capital			
AfDB		AIIB, CDB, IBRD/IDA	ADB, CAF, EBRD, EIB, IDB, IFC, IsDB, NDB
3e Support adaptation of MIGA's products & reinsurance capability to partially transfer portfolio level risk from MDB balance sheets			
	ADB, AfDB, EBRD, IBRD/IDA, IDB, IFC, MIGA	AIIB, CAF, CDB, NDB	IsDB, EIB, IFC
3f Consider ways to provide MDBs access to central bank liquidity			
EIB, IsDB	IDB	AIIB	ADB, AfDB, CAF, CDB, EBRD, IBRD/IDA, IFC, NDB
4a Strengthen communication with credit rating agencies; increase mutual understanding			
ADB, AfDB, AIIB, CAF, CDB, EBRD, EIB, IBRD/IDA, IDB, IFC, IsDB, NDB			
4b Encourage steps by rating agencies to strengthen their MDB evaluation methodologies			
ADB, AfDB, AIIB, CAF, CDB, EBRD, EIB, IBRD/IDA, IDB, IFC, IsDB, NDB			

Implementation completed	Under implementation	Implementation under consideration	Not considered appropriate
4c Take proactive approach to incorporation of ESG factors in rating methodologies			
ADB, AfDB, CDB, EIB, IBRD/IDA, IFC	EBRD, IDB	AIIB, IsDB	CAF, NDB
5a Strengthen the ability of shareholder boards to effectively set parameters of capital adequacy policies and oversee their implementation			
ADB, AfDB, AIIB, EIB, IBRD/IDA, IDB, IFC	AfDB, CAF, CDB, EBRD	IsDB	NDB
5b Establish yearly capital benchmarking report presenting key elements & statistics in comparable format harmonizing definitions over time. Support regular reviews of capital resources in light of MDBs' strategies			
AIIB, EIB	ADB, AfDB, CDB, EBRD, IBRD/IDA, IDB, IFC, IsDB, NDB		CAF
5c Establish enhanced dialogue and cooperation on capital adequacy, risk management and risk mitigation tools			
ADB, AfDB, CAF, EIB, IDB, IsDB	CDB, EBRD, IBRD/IDA, IFC, NDB	AIIB	
5d Transform GEMs into stand-alone entity to support improved understanding of MDBs by private investors and CRAs			
	ADB, AfDB, AIIB, EBRD, EIB, IBRD/IDA, IDB, IFC, IsDB, NDB	CDB	CAF

Note: The wording of the recommendations was taken from G20 CAF report Table 4.1 (pp. 52-53). IDB Invest did not submit data to include in this table, although it did supply data for lending headroom in Table 2 later in this report.

V. EVALUATION OF CAF IMPLEMENTATION PROGRESS AND FUTURE PROSPECTS FOR REFORM

Notable progress has been made implementing the 17 CAF report recommendations in the past year, although substantial work remains. This should come as no surprise, as CAF reforms represent a modernization of the MDB financial model that touches on sensitive aspects of MDB governance, shareholder risk and access to funding markets. Further progress requires openness to re-thinking established patterns, cooperation and coordinated action across the system and a commitment to sustained effort by shareholder governments and MDB management, supported by the G20.

Further implementation of CAF reforms can lead to a substantial increase in MDB lending capacity, as well as strengthen the basis for discussions on MDB capital needs for all stakeholders. CAF-linked reforms have already opened $170 billion in additional lending headroom across the major MDBs, with $113 billion more projected to be finalized by end-2024 and further gains expected going forward. Shareholders, market actors and the broader development community have a far more sophisticated and nuanced understanding of MDB capital adequacy issues than two years ago when the G20 CAF report was published, to the benefit of all. This is critical not only for shareholders and MDB management to consider the financial capacity of MDBs, but also because MDBs are increasingly seen as an asset class by private investors.[2] The CAF agenda has encouraged MDBs to see themselves as a common set of institutions with similar strengths and challenges, helping develop sector-wide standards and benefiting from coordination and collective action.

Overview of recommendation implementation

Recommendations related to core capital adequacy (1a-1c and 2a) have made some progress since July 2023, but a considerable reform agenda remains. This includes prioritizing internal metrics rather than credit rating agency (CRA) methodologies in setting CAF risk thresholds, collectively establishing sector-wide standards for PCS and portfolio concentration risk and incorporating a prudent share of callable capital in CAFs. These reforms involve not just MDB management and shareholders, but also three different CRAs. While the benefits of these reforms are not easily quantified, they are deep and long-lasting: capital adequacy gains means that every dollar of shareholder capital will work that much harder for development outcomes, every year going forward for as long as the MDBs operate. Further efforts are merited.

Recommendations related to financial innovation and balance sheet optimization (3a-3f) have advanced considerably and can be considered on track. MDBs have successfully piloted a variety of innovations such as hybrid capital and risk transfers, partly spurred by the CAF report and building on earlier balance sheet optimization efforts also supported by the G20. These innovations show significant potential going forward and it is incumbent on the MDBs to work together to achieve greater scale, while remaining mindful of the limits and trade-offs involved.

Recommendations related to the CAF operating environment show mixed outcomes. Collective engagement with CRAs (4a-4c) has accelerated and deepened, with a growing number of MDBs working together to present evidence and feedback as input to CRA methodologies. This agenda has advanced considerably and has positive momentum going forward. Issues around CAF governance and information (5a-5d) have shown some gains, but more effort is needed. Work is ongoing on CAF benchmarking and the Global Emerging Markets Risk Database Consortium (GEMs), while board capacity for CAF issues and system-wide information arrangements show uneven progress across MDBs.

The G20's role going forward

The role of the G20 and the IFA WG is crucial to drive this agenda forward, all the more now that the "low-hanging fruit" have been plucked and a more challenging reform agenda lies ahead. Decisions on policy, strategy, lending capacity and capital needs are and will remain entirely in the hands of each MDB's shareholders. Many CAF reforms requiring further

2. The growing variety of private sector mobilization instruments and platforms—such as syndication arrangements, hybrid capital, commercial risk transfers, guarantees and more—mean that investors would benefit from more standardized approaches to MDB financial policies and metrics, in the absence of regulatory guidance. MDB debt is moving toward being seen as a distinct asset class with a particular attraction to ESG-oriented investors. See, for example, UBS (2022), "Impact investing through Multilateral Development Banks," 01 November 2022.

progress revolve around MDBs as a unique sector or asset class that lacks commonly accepted standards to orient stakeholders and enable more efficient use of resources. The G20 is well positioned to facilitate the collective approach needed to make that happen. As well, G20 support can give greater comfort to MDB management and individual shareholders to push ahead with more sensitive but potentially transformative CAF-related reforms. In their reporting to the IFA WG, MDBs were broadly supportive of the G20 continuing to engage on CAF issues.

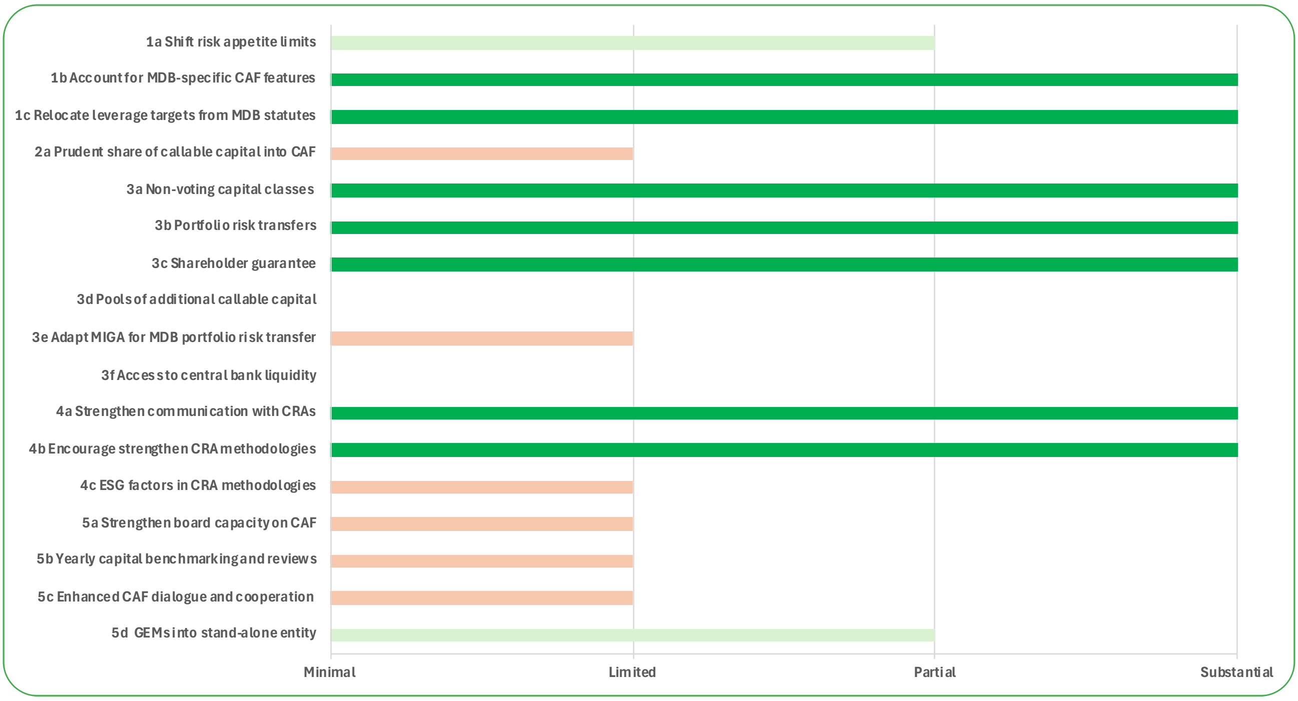
Substantial further gains can be achieved with concerted effort by MDBs with the strong backing of the G20. By working toward generally accepted standards for MDB capital adequacy, shareholders will feel more confident that their capital contribution is being used as efficiently as possible to promote development goals. CAF reforms by themselves are not replacements for core equity capital, which is the bedrock of MDBs' financial strength and market reputation. But systematically and collectively following through with the CAF reforms—improved risk assessment, better utilizing callable capital, financial innovations and engagement with rating agencies—will allow all stakeholders to have a common basis for understanding MDB financial capacity to inform discussions on how to match available capital with development ambitions, to the extent possible and together with other development partners.

VI. INDEPENDENT EVALUATION OF CURRENT STATUS AND PROSPECTS OF CAF RECOMMENDATIONS

This section provides a brief outline of each recommendation, a progress assessment (see Figure 1 for summary) and suggestions of a path forward. Current status is assessed in four categories: Substantial, Partial, Limited or Minimal Progress. These categories are descriptive rather than normative. A low assessment may reflect the fact that a given recommendation was deemed by management and shareholders to be inappropriate for one or more MDB and was hence not pursued by common agreement.

This evaluation is based on a precise reading of the CAF recommendations. It was done independently from the MDBs but is informed by their progress reporting. Discrepancies between MDB self-reporting in Table 1 and the independent assessments described in this section are highlighted and can form the basis for discussions between the G20 and MDB management on potential future directions for CAF reform.

Figure 1. Assessment of System-Wide Progress on CAF Recommendations



Note: Progress as depicted here is descriptive rather than normative. Limited or minimal progress may not necessarily be negative: it could be the result of an assessment by shareholders and MDBs that a given recommendation is not appropriate.

Recommendation 1. Adapt approach to defining risk tolerance

1a: Shift risk appetite definition toward shareholder-defined limits

The goal of this recommendation is to encourage shareholder governments to establish risk tolerance thresholds within MDB CAFs based on their own assessment of institutional goals and risks, rather than anchored in credit rating agency (CRA) methodologies. This is motivated by the fact that CRA methodologies vary widely and in some cases do not appear to adequately account for MDB financial strength. As a result, obtaining a target rating from all major CRAs can lead MDBs to build in excessive buffers. The recommendation is informed by the guidance of the Financial Stability Board[3] that financial institutions should reduce reliance on bond ratings as a proxy for risk tolerance and strengthen in-house risk assessment capacity.

Assessment: **Partial Progress**

Shareholders and MDBs have made some progress on this reform. IBRD and ADB have made notable changes to CAF risk tolerance thresholds in response to the recommendation,

3. Financial Stability Board (2010). "Principles for Reducing Reliance on CRA Ratings." October 2010.

which has released an additional $40 billion and $100 billion (respectively) in lending headroom over ten years. IDB Invest also revised its risk tolerance thresholds to unlock $2 billion in lending capacity, although details are not available. Several other MDBs report having revisited risk discussions with shareholders as part of capital adequacy reviews to verify appropriate CAF risk thresholds.

ADB's CAF shift involved refining the risk appetite statement and changing the approach to risk measurement by moving from expected shortfall to value at risk and aligning the confidence level to the desired AAA risk, and by introducing lower and differentiated loss given default assumptions for sovereign borrowers. To offset the risks of operating at a lower level of capitalization, ADB introduced a more granular appetite for sovereign risk, a predefined countercyclical lending buffer and a predefined recovery plan. ADB´s approach highlights the potential headroom gains for other MDBs that follow a similar strategy, although outcomes will depend on each MDB's size and level of capitalization.[4] IBRD's change is discussed under Recommendation 2a below, due to its link to callable capital.

Despite this commendable progress, the fundamental tension between shareholder assessment of risk tolerance as expressed in internal MDB CAFs and CRA-defined limits to MDB capital adequacy remains largely unchanged across the major MDBs. The major MDBs are still directed by their shareholders to maintain a AAA rating with all three major CRAs as the key indicator of risk tolerance, superseding internal assessments of risk. As such, CAFs of the major MDBs continue to be built around CRA-defined limits. While all MDB shareholders support retaining AAA ratings, some would be in favor of exploring the trade-offs of reducing the requirement to retaining a AAA rating with only two rather than three CRAs, provided that this would not negatively impact funding market access.

MDBs with sub-AAA ratings face fewer challenges with this recommendation, although they face higher market funding costs and therefore offer less affordable financing conditions. As shareholders are unable to fall back on defining risk tolerance with reference to AAA ratings, they instead make more nuanced decisions considering the trade-offs between bond rating and capital market access, MDB operational contexts and the risk of financial stress.

<u>Path Forward</u>

Further progress on this recommendation is contingent largely on the willingness of shareholders of the AAA-rated MDBs to take a new approach to defining risk tolerance thresholds and directing MDB management to embed that threshold into CAFs, while protecting their privileged access to funding markets and ability to provide low-cost financing to clients.

To achieve this, the G20 may wish to encourage MDBs to propose options for a new approach to defining CAF risk tolerance thresholds prioritizing internal MDB financial metrics. The recent callable capital clarification exercise is an example of how collective work by the

4. ADB was in a unique situation when it undertook the CAF reform in part because of the results of the 2016 merger of the concessional and non-concessional balance sheets.

MDBs can improve system-wide understanding of MDB CAF issues. These proposals would be discussed and decided at the level of MDB boards, although the IFA WG may wish to closely track the process to encourage coordinated changes across the MDB system. The resulting CAF could indicate, through providing detailed data, that an MDB has more lending headroom than currently considered by CRA methodologies. This disjunction could be explicitly quantified in each MDB's annual capital adequacy review, identifying the CRA methodology in question. The April 2024 Heads of MDBs Viewpoint note supports further work in comparing CAFs across MDBs.

Such a shift to MDB CAF risk tolerance limits would have potentially important benefits:

- Clarifying the interaction between internal MDB CAFs and CRA methodologies, thus more accurately focusing discussions on obstacles to expanding MDB lending capacity and risk considerations.

- Giving shareholder governments and MDB management a more proactive role in defining standards for the sector, rather than reacting to the methodologies of three different CRAs.

- Offering clearer shareholder signals to MDB management to enable the design and implementation of CAF policies that more efficiently align risk, capital base and operational goals.

A further step would be for the G20 to call on MDBs to undertake systematic and evidence-based analysis of the benefits and risks of reducing the requirement to maintain a AAA rating with two CRAs, instead of three as is currently common across the MDBs. This is in line with practice of many MDBs (including the World Bank) to solicit ratings from only two CRAs, although in practice they continue to ensure a AAA with all three MDBs. It is also in line with the way that the Bank for International Settlements (BIS) evaluates financial institutions and would have no impact on the risk-weighting of MDB bonds according to BIS rules. Undertaking such a shift in a coordinated fashion across the major MDBs with explicit support from the G20 and MDB shareholders would strengthen how such a move would be perceived by funding market actors. Such a policy shift could increase MDB lending headroom due to the high divergence across CRA methodology metrics, although the amount would vary at each MDB.[5] MDBs would not make use of this headroom until shareholders and management were confident that it would have no negative impact on funding market access.

1b: Ensure frameworks account for MDB-specific features

The credit risks faced by MDBs are substantially different from commercial lending institutions, in particular due to preferred creditor status (PCS) and the highly concentrated nature of MDB loan portfolios. These factors are especially relevant for MDB lending to

5. A study by Risk Control (2022), commissioned by the CAF panel, showed that a stylized MDB could expand its loan portfolio by 197% and still retain a AAA rating under S&P's methodology, compared to only 34% expansion for Fitch and 11% for Moody's.

sovereign borrowers. However, methodologies for incorporating the value of PCS and portfolio concentration into MDB CAFs are not uniform. The recommendation is intended to i) ensure individual MDBs appropriately account for PCS and concentration risk and ii) encourage a more uniform approach to these factors to converge toward accepted standards across the sector by MDBs, CRAs and other stakeholders.

Assessment: **Substantial Progress**

At the individual MDB level, this recommendation is well advanced. All MDBs account for PCS and portfolio concentration in ways that recognize their unique nature and differ from commercial banks. This is reflected in credit risk weightings, projected potential credit losses and other relevant CAF aspects. Some of the newer MDBs, such as AIIB, have relied on commercial bank risk weightings due to their limited credit history, and are transitioning to risk weightings based on probability of default (PD) and loss given default (LGD) data from other MDBs. AIIB estimates that this transition has already opened up an additional $15 billion in lending headroom over 10 years. AfDB undertook a re-evaluation of the weight of PCS in its CAF in 2022 resulting in a 20% improvement in risk capital usage, although the $1.2 billion additional headroom cannot yet be used due to constraints imposed by the Fitch methodology. ADB's CAF revision discussed in the previous recommendation also addressed these issues. Prior to the CAF report, EBRD undertook a revision of its approach to PCS that led to a lending capacity gain of $3.2 billion.

At the sector-wide level, progress has also been considerable. Independent technical studies have provided evidence-based assessments of PCS and concentration risk.[6] The World Bank published a detailed historical overview of sovereign credit history in March 2024, and other MDBs are reportedly preparing similar studies. The results of these assessments have already and will continue to be used by MDBs in their discussions with CRAs on their methodologies, especially via the chief risk officer/chief financial officer (CRO/CFO) forum meetings organized by a number of major MDBs. This collective action speaks to a strong and growing appreciation among MDBs for the need to work together to help establish generally agreed standards on PCS and concentration for their own CAFs as well as CRA methodologies.

Path Forward

The forthcoming studies by MDBs on their credit history, combined with the World Bank's recently-published work as well as GEMs data and the results of external studies, will form a substantial body of evidence to evaluate the financial implications of PCS and concentration risk.

Further progress is needed to promote more uniform approaches to incorporating PCS and concentration risk into CAFs and CRA methodologies. While every MDB can and should adapt techniques to suit their operating contexts and shareholder preferences, a more

6. On PCS: Risk Control (Forthcoming). "Quantifying Preferred Creditor Treatment for Multilateral Development Bank Sovereign Loans." On concentration risk: E. Lüktebohmert-Holtz, J. Sester and H. Shen. (2024). "On the Relevance and Appropriateness of Name Concentration Risk Adjustments for Portfolios of Multilateral Development Banks." Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4642039.

uniform approach to incorporating these critical factors would benefit all stakeholders and would help promote standards across the sector.

The next step would be for MDBs to work with one another, under the guidance and with the explicit support of the G20, to agree on standardized approaches to incorporating PCS and concentration risk into CAFs. These standards would be kept at the conceptual level, be voluntary and can be adapted as appropriate to individual MDB needs.

This effort could be led by a dedicated working group under the auspices of the CRO/CFO forum and with the active engagement and tracking of the G20 IFA WG. The key issues to be addressed would be:

- How to translate MDB credit history into risk weightings and expected credit losses (PDs and LGDs) to be embedded into each CAF to a degree that prudently reflects the benefits of PCS to MDB financial strength.

- The appropriate model parameters to assess portfolio concentration risk, including correlations across exposures.

The G20 IFA WG may organize an event at the margins of the World Bank-IMF Annual Meetings in October 2024 on PCS and portfolio concentration, which could be an appropriate forum for further discussion of this agenda.

1c: Relocate specific numeric leverage targets from MDB statutes

MDBs have traditionally incorporated specific limits within their founding statutes mandating that loan portfolios may not exceed a certain ratio to subscribed capital (paid-in plus callable) and reserves. In almost all cases, this ratio is 1:1. Statutory limits served as a useful de facto CAF in the early decades of MDB operations but have since been superseded by more sophisticated approaches to evaluating financial risk and operational capacity. As such, the CAF review panel called for their removal from statutes and relocation of numerical portfolio limits to the level of policy to modernize MDB statutes and clarify CAF discussions.

Assessment: **Substantial Progress**

The recommendation met with broad support by shareholders and MDB management. The Boards of Governors of the ADB, EBRD and the World Bank's IBRD[7] have all approved removing the statutory limits, although this will not formally occur until the change is ratified by shareholder governments. AfDB, CDB and IDB have indicated that they may consider a similar change should the statutory limits become binding, but they are not prioritizing the issue currently. EIB is in discussions with shareholders about relocating the statutory limits to the risk appetite framework, with a decision on whether and how to proceed expected before the end of 2024. AIIB, IsDB and NDB have concluded that their current statutory

7. The World Bank's IDA, IFC and MIGA do not have statutory limits.

frameworks are appropriate to their circumstances. AIIB's statutes foresee the possibility of adapting statutory leverage limits to evolving circumstances based on Board of Governor approval.

Path Forward

This recommendation is well advanced and is likely to be fully completed in the near term at ADB, EBRD and IBRD, with EIB likely to follow in the medium term. The G20 may wish to hear from AfDB, AIIB, CDB, IDB, IsDB and NDB on why they do not consider it necessary to move ahead in tandem with the other MDBs.

Recommendation 2. Give more credit to callable capital

2a: Incorporate a prudent share of callable capital into the calculation of capital adequacy

Callable capital is a specialized type of guarantee offered by shareholders to MDBs to strengthen their access to capital market funding with a nominal value of roughly US$1.3 trillion in the MDBs evaluated in the G20 CAF report (as of 2021). CRAs incorporate callable capital in different ways in their assessment of MDB financial strength, but MDBs themselves have not generally done so.

The recommendation proposes that MDBs incorporate a prudent share of callable capital into their CAFs based on their own evaluation of the instrument's financial benefit. The rationale behind the proposal is that, as the report states, "the financial backup provided by callable capital would allow MDBs to increase risk-bearing capacity, thus increasing operational headroom either for regular operations or as a crisis buffer."[8] The recommendation does not suggest that a portion of callable capital can be incorporated into CAFs directly just as paid-in capital, but rather that its existence can influence the risk parameters embedded into the CAF.

Assessment: **Limited Progress**

This recommendation has proved challenging. The complex nature of the recommendation is exemplified by the widely varied responses of MDBs with substantial callable capital9 in the reporting exercise. Three reported that the recommendation is fully implemented (EBRD, IBRD and IDB), four that it is not appropriate (ADB, AfDB, CAF and EIB), one that it is under implementation (IsDB) and two that it is being considered (AIIB and CDB). This variance responds to divergent understandings of what the recommendation is proposing and its overlap with recommendation 1a.

The three MDBs that report completing the recommendation all indicate that they have incorporate callable capital into their CAFs already prior to the CAF report, and IBRD further took a 2023 board decision to lower its benchmark equity to loans ratio allowed by a better

8. G20 (2022). "Boosting MDBs' Investment Capacity: An Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks", p. 32.
9. IFC and IDB Invest do not have callable capital while CAF has a much smaller amount compared to the other MDBs, and from governments that are lower rated than the CAF itself.

recognition of the value of its callable capital to its risk appetite threshold, resulting in an additional $40 billion in lending capacity over 10 years. IBRD notes that the existence of callable capital enables it to use a lower risk tolerance threshold than other MDBs that do not have callable capital.

These steps are positive, but do not fully reflect the intention of the CAF recommendation. None of these MDBs place an inherent value on callable capital as a risk-mitigating instrument that can impact internal CAFs. Instead, they reference the degree to which CRA methodologies give rating benefit for callable capital. Because callable capital can in some cases result in a final "issuer rating" above an MDB's "stand-alone" rating, these MDBs rely on callable capital to maintain an issuer AAA rating, rather than targeting a stand-alone AAA rating. This approach effectively embeds CRA methodologies directly into MDB CAFs but does not provide any guidance to CRAs, who have pointed out that the fact that MDBs themselves do not take callable capital into account in their CAFs makes it more difficult for CRAs to value it.[10]

Five major MDBs—AfDB, ADB, EBRD, IBRD and IDB—undertook studies at the request of a group of shareholders on: i) the legal context of callable capital; ii) a statistical reverse stress test on the likelihood of actually requiring a capital call; and iii) the fiscal context of callable capital at major shareholders. These highly informative studies were published in April 2024 and were complemented by a statement by several shareholders reiterating their firm support to callable capital commitments. An independent study also published in April 2024 reviewed similar aspects of callable capital.[11] Moody's released a briefing indicating that the results of this work would have a direct beneficial impact on how they evaluate MDB callable capital, saying that the new information allows them to consider MDB callable capital as providing "a larger buffer against the potential deterioration of an MDB's credit metrics elsewhere, such as higher leverage or weakening loan asset credit quality or asset performance."[12] One smaller CRA has already incorporated the results into their ongoing MDB methodology revision.[13] Shareholders are currently considering further actions related to this recommendation.

Path Forward

Due to the collective nature of the agenda and the need to present a united front to establish standards for callable capital, designing the approach to incorporating callable capital would best be undertaken by a cross-MDB working group, which could report to shareholders and the IFA WG. Such a step would be in line with the call in the Heads of MDBs Viewpoint note (April 2024) to further explore callable capital. The methodology could be based around the approach that callable capital is a valuable risk mitigating instrument that justifies modifying the risk thresholds build into MDB CAFs, as described in the G20 CAF recommendation. This approach is in line with modern financial theory and recognizes that callable capital is not equivalent to paid-in, Tier 1 regulatory capital.

10. See for example Global Capital (2024). "Fitch highlights political risks of callable capital." 18 April 2024.
11. C. Humphrey, C. McHugh, E. White and B. Getzel (2024). "Maximising the developmental impact of multilateral development bank callable capital: Project findings and path forward." ODI Working Paper, April 2024.
12. Moody's (2024). "Greater transparency of MDB callable capital strengthens our view of shareholder support." 30 May 2024.
13. Scope (2024). "Scope publishes updated supranational rating methodology and calls for comments." 10 May 2024.

Building on the callable capital exercise undertaken in early 2024, MDBs and shareholders could move ahead with related reforms further clarifying processes for making and implementing a capital call, including, where necessary, issuing board-level interpretations of MDB statutes and ancillary policies. This could include more precisely defining the financial continuum between normal operations and non-viability, and where a capital call would occur in the unlikely event of need. These actions would strengthen the confidence of MDB bond investors and CRAs on the reliability of callable capital.

Moving forward with this agenda would not increase the risk of triggering an actual capital call, which remains extremely low. For example, the reverse stress test undertaken by EBRD in April 2024 test found that the likelihood of a capital call "is lower than a 1 in 10,000-year event."[14] Other MDBs found similar results in their reverse stress tests. Incorporating the value of callable capital into MDB CAFs as proposed in the G20 CAF recommendation would not materially change that likelihood.

Nor would any MDB need to risk a rating downgrade due to the application of modified risk thresholds. As described above for Recommendation 1a, the policy directive of obtaining a AAA rating can be maintained, but the CAF report calls for it to be distinct from internal MDB CAFs based on shareholder-defined risk thresholds. Should CRA methodologies indicate a potential downgrade, MDBs could decline to utilize lending headroom even if their internal CAFs indicate that doing so would be prudent.

Recommendation 3. Expand uses of financial innovations

3a: Endorse MDB consideration of non-voting capital classes (paid-in equity or hybrid) to contribute to available capital

MDBs have traditionally relied on direct paid-in contributions from governmental shareholders to build equity capital, along with allocations from net income to equity reserves. This recommendation encourages MDBs to consider other forms of non-voting capital, both paid-in and hybrid, to increase their capital base and lending capacity.

Assessment: **Substantial Progress**

Several MDBs are moving forward with hybrid capital instruments in three different forms: i) to commercial investors; ii) to shareholder governments or philanthropic investors in regular currency; and iii) to shareholder governments denominated in Special Drawing Rights (SDRs). These initiatives have greatly expanded the potential for strengthening MDB capital, although hybrid instruments are limited as a total share of the capital base of any financial institution (normally 25% for Tier 2 capital). Among the notable developments on this recommendation are:

- AfDB successfully executed the first MDB commercial hybrid in January 2024 for $750 million, with very strong investor appetite (eight times oversubscribed).

14. EBRD (2024). "Callable Capital Review." 17 April 2024, p. 2.

- IBRD has structured a shareholder hybrid with several governments already committed and has board approval for a commercial hybrid, with the aim of unlocking $7.4 billion in additional lending. Explorations are underway for an IDA hybrid as well.

- AfDB and IDB have led discussions on an SDR-denominated hybrid, with IMF approval given in May 2024, and are seeking government investors to proceed. ADB, IBRD and IsDB are also considering moving forward should the instrument prove viable and investors are found.

- All other reporting MDBs are exploring different hybrid types and will consider proceeding based on i) the experience of other MDBs; ii) financial terms and investor demand; and iii) their own financial situation.

Rechanneling SDRs to MDBs via hybrid capital instruments was mentioned but not explicitly considered in the G20 CAF report. However, it has subsequently gained considerable momentum through the efforts initially of AfDB and subsequently also IDB, including a recent positive decision by the IMF.[15] This route may have substantial upside potential, although IMF guidance currently limits SDR use to about $20 billion. The next hurdle would be to find at least five governments willing to deploy a share of their SDRs in this fashion.

<u>Path Forward</u>

This recommendation is well on track, with strong interest at all the major MDBs and substantial cooperation across MDBs. It may be useful for G20 to encourage further cooperation in standardizing hybrid design and collectively engaging with CRAs, market participants and potential shareholder/philanthropic investors to reduce transaction costs and ensure the greatest benefit from hybrid issuance after a careful review of the potential effects on the cost of funding for beneficiaries. This could be in the context of the CRO/CFO forum (which MDBs are planning to formalize), or as a dedicated working group on CAF recommendations (as suggested in Recommendation 2 above).

<u>3b: Scale portfolio risk transfers to the private sector of MDB non-sovereign loans to facilitate additional lending</u>

A number of MDBs have for some years transferred individual exposures to investors. Supported by earlier G20 efforts, MDBs began in the past decade experimenting with risk transfers at the portfolio level, notably AfDB's two 2018 Room2Run transactions and the active use of credit insurance by ADB and AIIB for non-sovereign portfolios. This recommendation encourages MDBs to scale up these efforts, while remaining sensitive to concerns about PCS (particularly in relation to sovereign risk transfers to commercial counterparties) and MDB net income generation and portfolio quality.

<u>Assessment:</u> **Substantial Progress**

15. IMF (2024). "Use of SDRs in the Acquisition of Hybrid Capital Instruments of the Prescribed Holders." IMF Policy Paper May 2024.

MDBs have undertaken further transactions since the CAF report was published, notably with the insurance industry and pioneering the transfer of risk embedded in sovereign loans. AfDB undertook a third Room2Run transaction in 2022 with a group of commercial insurers and with the support of the UK government on a portfolio of sovereign loans (freeing $2 billion in headroom over 10 years). IDB created US$550 million in headroom through a sovereign portfolio risk transfer transaction in 2023 with commercial insurance firms, while IDB Invest has unlocked $1.56 billion additional lending already and aims to scale up commercial risk transfers substantially in the coming years. EBRD has been highly active in risk transfers with $1.6 billion in lending space already created (although deployment is limited due to CRA constraints) and another $3.2 billion aspired to in the medium term, and ADB has opened $2 billion in new lending capacity through risk transfers. CDB intends to explore using these instruments in the medium term.

A notable development is IFC's work in creating the new Warehouse Enabled Securitization Program (WESP) to facilitate risk transfers to commercial investors via securitization vehicles. The aim of WESP is to co-finance new loans by MDBs at origination, with the intention of only holding the loans until they can be packaged and transformed into investable securities for institutional investors – thus shifting to an originate-and-distribute model for appropriate non-sovereign loans. Work on WESP is underway with a view to undertaking the first transaction with IFC assets by end-2024 and subsequently opening the facility to other MDBs and DFIs. IFC expects to create $130 million in headroom by end-2024 with risk transfers and aims to generate $1.8 billion more in the medium term.

A related risk transfer innovation that was not addressed in the CAF report is exposure exchange agreements (EEAs). These involve the "synthetic" transfer of the repayment risk of portions of one MDB's portfolio with another MDB. The portfolios are structured to have similar risk characteristics, but because they involve different sovereign borrowers, EEAs help reduce the concentration of MDB loan portfolios, thus increasing lending headroom under CRA metrics (especially of S&P). This is particularly relevant for regional MDBs with structurally concentrated portfolios. EEAs can be more difficult to structure with sub-AAA-rated MDBs, an issue that MDBs may consider working on collectively to address. EEAs are a highly useful tool, although the CAF report focused (in Recommendation 1b) on developing standards on portfolio concentration to provide guidance to CRA methodologies, which would reduce the need for these transactions.

Path Forward

The basic structure, pricing and capital adequacy benefits of commercial risk transfers appear to be evolving well, and the limited number of further transactions thus far may be more a reflection of MDB cost-benefit analysis rather than any structural obstacles. Following on the recommendation of the CAF report as well as last year's CAF progress report, the G20 continues to see merit in more collective engagement among MDBs (possibly in combination with the proposal of a cross-MDB working group noted in 2a and 3a, above) to standardize transaction templates, reduce transaction structuring times and improve pricing and capital headroom benefit calculations by investors and CRAs.

The G20 strongly supports expansion of commercial risk transfers for non-sovereign exposures—with appropriate caution related to the implications to MDB net income and portfolio structure—and commends IFC's efforts to develop the WESP. The G20 suggests caution on scaling up commercial risk transfers with sovereign exposures due to the potential implications of diluting PCS. The G20 proposal in last year's CAF progress review to develop a common approach to mitigating PCS risk to sovereign transactions remains outstanding.

3c: Encourage shareholder guarantees on loans related to crosscutting priorities

MDBs and shareholders have for the past decade begun piloting portfolio guarantees by which a willing shareholder government covers the repayment risk of a set of MDB loans. Depending on shareholder rating and the views of CRAs, this frees MDB lending headroom. The first transaction was pioneered by Sweden and ADB in 2016, and other transactions have followed with different governments and MDBs. The recommendation encourages MDBs and shareholders to seek new opportunities to deploy portfolio guarantees, possibly in combination with other financial mechanisms, as an efficient means to expand MDB lending capacity using an unfunded instrument.

Assessment: **Substantial Progress**

Several MDBs have moved ahead with new transactions and innovative structures in the wake of the CAF report. ADB launched a platform involving multiple shareholders for climate investments in 2023 (Innovative Financing Facility for Climate in Asia and the Pacific, or IF-CAP), which is expected to unlock $10 billion additional lending in the next decade. A group of shareholders came together to provide guarantee support for EBRD's lending in Ukraine despite elevated risks, which will allow an additional $3.2 billion in lending over the coming decade. The World Bank's IBRD expanded the limit for guarantees and established a Portfolio Guarantee Platform and expects to generate $74 billion in lending space through a combination of bilateral and portfolio guarantees. IDA is also exploring options. AfDB has engaged in several transactions including a $1 billion guarantee from the UK to support South Africa's Just Energy Transition Partnership. IDB and Sweden are currently finalizing a transaction to unlock $469 million in lending as part of the Amazonia Forever program. EIB benefits from first loss protection from the EU or EU member states on higher risk exposures, which results in substantial de-risking and allows the EIB to deliver higher volumes of higher-risk operations. Making use of currently unused capital (as a new MDB), AIIB has acted as a provider by guaranteeing $1 billion of IBRD's portfolio[16] and may provide guarantees to other MDBs in the near term.

Path Forward

This recommendation appears well advanced. The G20 may want to encourage the creation of platform approaches involving multiple shareholders to support already established MDB priorities. Further collective engagement by MDBs to strengthen and clarify the benefit

16. Because the guarantee covered IBRD loans rated above AIIB's target average portfolio rating ("B"), the transaction allows AIIB to lend to B-rated countries beyond what would otherwise have been the case, thus providing benefits to both IBRD and AIIB.

of these transactions to MDB lending headroom would also be beneficial. As noted in the 2023 CAF progress report, it remains important to ensure that portfolio guarantees are fully aligned with shareholder-established lending priorities (sectoral and geographic), to ensure no dilution of appropriate MDB governance.

3d: Support collective shareholders commitments of pools of additional callable capital

The recommendation notes that MDBs maintain substantial capital buffers to be able to lend during times of crisis when other types of financing tend to retreat and when the assessed riskiness of MDB loans (and hence capital usage) may increase. Pools of pre-committed callable capital may serve as a counter-cyclical buffer, thus reducing the need to lock up risk capital for counter-cyclical purposes.

Assessment: **Minimal Progress**

For the most part, MDBs and shareholders have elected not to pursue this recommendation due to governance implications and uncertain benefits in line with CRA methodologies. Of the reporting MDBs, only the World Bank's IBRD indicated that it is considering action in this direction via its enhanced callable capital proposal currently under discussion. AfDB has used temporary callable capital to address rating constraints.[17] Other MDBs, including ADB and IDB, report that they may consider such a move if circumstances merit.

Path Forward

In the view of the G20, this recommendation has been well considered and is not the best way for most MDBs to address the counter-cyclical component of their development operations. The stipulation from last year's CAF progress report that such measures should be only on a temporary basis to address exceptional circumstances remains valid. Additional callable capital commitments can be useful in relation to specific CRA methodology constraints as AfDB's experience shows.

The G20 encourages MDBs to consider other approaches to addressing counter-cyclical lending capacity, including other types of contingent instruments (such as portfolio guarantees) that are pre-committed and could be activated in well-defined circumstances. The goal would be to give MDBs the security they need to reduce capital buffers and to ensure adequate recognition by CRAs.

3e: Support adaptation of MIGA's products & reinsurance capability to partially transfer portfolio level risk from MDB portfolios

The World Bank Group's Multilateral Investment Guarantee Agency (MIGA) has a well-developed ability to offer insurance and guarantee products, and to efficiently recycle a substantial share of its exposures to the commercial reinsurance industry. MIGA services

17. See AfDB (2024) "African Development Bank Group Board of Governors Approves $117 billion General Callable Capital Increase." 02 June 2024.

are already available to other MDBs in defined circumstances and partnerships could be expanded, especially in relation to MDB country exposure constraints.

Assessment: **Limited Progress**

Pursuant to this recommendation, MIGA engaged in discussions with risk teams of multiple MDBs and confirmed the potential benefits to MDB lending headroom. In September 2023, MIGA's Board authorized the creation of the Non-Honoring of Sovereign Financial Obligations to a Multilateral Development Bank (NH-MDB) program, with an initial program size of up to $1.5 billion per year over two years. MIGA has since been in discussions with three MDBs (ADB, AfDB and IDB) to identify potential viable transactions that meet both MIGA's eligibility criteria and MDB needs, and NDB is also considering seeking opportunities with MIGA depending on pricing and uplift benefits. Discussions are expected to conclude in the coming months to define next steps.

Path Forward

The G20 considers this recommendation to be on the appropriate path forward, despite as-yet limited results. A number of technical issues remain to be resolved (including pricing, subrogation issues and individual exposure vs. portfolio transactions), and discussions continue, with several MDBs interested in exploring opportunities. Successful implementation may require tailored solutions for MIGA coverage of MDB exposures. At this stage, and barring significant changes to MIGA's mandate, it appears this recommendation will generate modest gains, particularly related to loan concentration for the regional MDBs.

3f: Consider ways to provide MDBs access to central bank liquidity

MDBs carry high levels of liquid assets to ensure continued operational capacity in the case of funding market disruption and to address CRA criteria. Access to central bank liquidity lines, as for commercial banks, may free MDB balance sheet space to carry additional loans and avoid costly liquidation of MDB assets in the face of market stress. EIB has access to European Central Bank liquidity facilities, while the IsDB has a liquidity line with a shareholder central bank. EIB notes that its arrangement with the ECB is only possible due to the alignment of ECB and EIB membership, and that it comes with supervisory requirements from ECB. Outside of the MDBs considered in this report, the West African Development Bank maintains a liquidity line with the Central Bank of West African States, a facility that is considered a rating positive by CRAs.

Assessment: **Minimal Progress**

Apart from existing liquidity lines at EIB and IsDB, none of the other MDBs have actively pursued this recommendation for a variety of technical and governance reasons as well as uncertainty on the benefits. IDB has developed a proposal for shareholder governments to commit liquidity support (beyond existing callable capital commitments) in pre-defined circumstances as an alternative approach. Such a facility could reduce the cost of carrying liquidity and provide relief from non-risk-weighted metrics in some CRA methodologies.

Path Forward

The G20 recommends no further action at this stage, although it would suggest socializing the results of IDB's efforts should they move forward.

Recommendation 4. Improve credit rating agency assessment of MDB financial strength

4a: Strengthen communication with credit rating agencies; increase mutual understanding

4b: Encourage steps by rating agencies to strengthen their MDB evaluation methodologies

4c: Take proactive approach to incorporation of ESG factors in rating methodologies

These three sub-recommendations are addressed jointly due to their close inter-relation and overlapping actions.

MDB business models and developmental effectiveness are built around reliable access to low-cost funding, which for the large MDBs is almost entirely from bond markets.[18] As such, the views of the three major CRAs—Standard and Poor's, Moody's and Fitch—on MDB creditworthiness are extremely important. However, the CRAs have widely divergent methodologies due to the unusual characteristics of MDBs and the lack of any regulatory guidance. The shareholder mandate of maintaining a AAA rating with all three means that MDBs must model to the most restrictive elements of each methodology, which leads them to be highly conservative in their financial management. Some external studies have highlighted that some CRA metrics do not match up with MDB performance and are overly restrictive to MDB lending capacity.

These recommendations propose that MDB management and shareholders take a more coordinated and active role in engaging with CRAs such that their methodologies better reflect the true creditworthiness of the MDBs. Recommendation 4a focuses on the role of the G20 and shareholder governments in communicating their strong support to MDBs, which is an important component of all CRA methodologies. Recommendations 4b and 4c propose that MDB management work collectively to present evidence on MDB-specific metrics to encourage CRAs to adapt their methodologies, including on issues such as PCS and concentration risk (4b) and ESG factors (4c). The goal is for MDBs and shareholders to provide coordinated evidence and signalling to encourage refinement and convergence across CRA methodologies, while recognizing that these methodologies are unlikely to become uniform.

18. Sub-regional MDBs with majority ownership of developing countries rely on a mix of bond issues, bank loans (syndicated or otherwise), external official funding sources like other MDBs and, in some cases, deposits by shareholder country central banks.

Assessment: **Substantial Progress (4a and 4b); Limited Progress (4c)**

Coordinated engagement with CRAs by MDB management and shareholder governments has strengthened considerably since the G20 CAF report was published. MDB CROs and CFOs have developed an increasingly well-attended working group to engage with CRAs on methodology questions. The CRO/CFO forum has organized bi-annual roundtable engagements in the past three years with each of the three CRAs. The most recent event, in April 2024, was attended by 17 MDBs and DFIs and included presentations by external experts on issues such as PCS, concentration risk and MDB risk transfer mechanisms.

This collective effort has had a powerful impact on building a system-wide approach to addressing aspects of MDB CAFs and CRA methodologies. While a number of CRA metrics could be improved, change will occur slowly only over time: CRAs are disinclined to shift methodologies too abruptly as it can damage market credibility and they cannot be perceived as being influenced by the institutions they rate.

Nonetheless, some gains have been registered. This includes improved treatment of hybrid capital and risk transfer arrangements, which facilitates the ability of MDBs to evaluate the costs and benefits of moving ahead with transactions. Proposed changes in the ongoing methodology revision of Fitch reflects MDB concerns by increasing use of risk-weighted asset measures, which could result in lending headroom gains for some MDBs. Moody's recently indicated that it will give greater credit to callable capital in its methodology as a result of the combined efforts of MDBs and shareholders.[19] CRA methodologies already reflect ESG considerations based in part on MDB data, and MDBs indicate that further changes are unlikely in the near term and would in any event not result in substantial lending headroom gains.

G20 and shareholder governments have taken a more active role in engaging directly with CRAs on their MDB methodologies, led by the Canadian government which has organized workshops with different CRAs and shareholder groupings. A joint statement by a group of shareholders expressing their commitment to MDB callable capital in April 2024 is a further positive move in this direction. This statement was highlighted by Moody's in its recent decision to increase the benefits of callable capital, pointing to the potential value of active G20 and shareholder engagement.

Path Forward

The G20 considers this set of recommendations to be generally on track and encourages MDBs to continue their coordinated efforts to engage with CRAs on aspects of their methodologies, as supported in the Heads of MDBs Viewpoint note (April 2024). Taking a system-wide approach encourages convergence toward broadly accepted standards for the sector, while acknowledging that full methodology harmonization is neither likely nor necessarily desired. MDB shareholder groupings, including the G20, should consider more opportunities to directly engage with CRAs and to explicitly express their support for MDB

19. Moody's (2024).

financial policies and operational strategies. Shareholder support can play an important role in shaping some of the more subjective assessment elements embedded in each of the CRA methodologies.

Further progress may be expected if MDBs and shareholders move forward toward a more standardized approach to incorporating PCS, concentration risk and callable capital in their own internal CAFs, as per Recommendations 1a, 1b and 2a (discussed above). CRAs are independent, private firms over which the MDBs have no authority, and revisions to their methodologies happen on timeframes and for reasons based on their own internal considerations. As such, it is important for MDBs, shareholders and other stakeholders to recognize that the content and timing of changes to how MDBs are evaluated by CRAs are uncertain.

Recommendation 5. Increase access to MDB data and analysis

5a: Strengthen the ability of shareholder boards to effectively set parameters of capital adequacy policies and oversee their implementation

The role of shareholder boards in providing clear and informed direction to management is critical to the proper design and implementation of capital adequacy policies at MDBs, as at all financial institutions.[20] Unlike commercial banks, MDB boards are often staffed by ministerial officials from member countries rotating in and out on a regular basis and responsible in some cases for overseeing regular operations as well as higher-level strategic decisions. This can impede adequate discussions of capital adequacy issues and lead to an information imbalance between boards and management. The recommendation seeks to strengthen board capacity by including independent experts on boards or as technical advisors, and/or (in conjunction with 5c below) creating an independent body to provide system-wide analysis and training on CAF issues to board members.

Assessment: **Limited Progress**

To date, no MDB boards or shareholder groupings have made significant changes in response to this recommendation, although the quality of board discussions of CAF issues has improved due to heightened awareness of their importance. MDBs contend that current arrangements are sufficient to achieve the aims of this recommendation, although that differs from the assessment laid out in the G20 CAF report.

Examples illustrate steps that can be taken to strengthen board capacity. Both EIB and AIIB boards (and relevant audit and risk committees) include independent experts to support discussions on capital adequacy and other issues, and their input is highly valued by shareholders. Beyond the MDBs considered in the CAF review, Africa's Trade and Development Bank also includes non-executive members selected for their expertise on technical issues to strengthen financial and capital adequacy governance.

20. See for example BCBS (2019) on the importance of board governance for commercial banks.

Path Forward

The G20 may wish to call on individual MDB boards to more actively consider implementing this recommendation. The appointment of technical experts to board positions (and to relevant board committees) in non-voting roles could be a useful addition to strengthen informed CAF discussions and would not impact existing governance arrangements. It would also be possible for MDB boards and/or individual shareholder governments to present preferred qualifications and specialized training on financial issues before assuming a board position. A further voluntary option would be for individual board chairs to employ a financial expert to support deliberations on CAF-related matters.

5b: Establish yearly capital benchmarking report presenting key elements & statistics in comparable format harmonizing definitions over time. Support regular reviews of capital resources in light of MDBs' strategies

MDB CAFs vary in a number of important internal aspects and reporting metrics, which makes it difficult to compare across institutions to inform shareholder policy decisions at individual MDBs as well as system-wide evaluations of MDB capacity at the G20. In many cases these differences are justified by shareholder preferences and operational context, although in other cases they may have evolved over time for idiosyncratic reasons in the absence of sector-wide MDB CAF standards. The recommendation encourages MDBs to prepare regular capital adequacy benchmarking reports that, as far as practical, use harmonized metrics and definitions to better inform shareholder decision-making.

Assessment: **Limited Progress**

MDBs have thus far shown limited progress in issuing standardized benchmarking of capital adequacy, although this appears likely to soon change.

Path Forward

In late 2023 and early 2024, the World Bank's IBRD and EBRD led an initiative under the auspices of the CRO/CFO forum to develop a template for a CAF benchmarking, with input from ADB, AfDB, AIIB, EIB, IDB, IFC, IsDB and NDB. The MDBs report that this work should be completed before the end of 2024, with benchmark tables using common metrics presented to shareholders along with an explanatory note for each MDB. These notes are expected to contextualize each MDB's results and explain aspects that are unique to the MDB. The benchmarking exercise is expected to be repeated annually.

The G20 recognizes the efforts underway by MDBs to jointly develop a harmonized benchmarking template and supports releasing the reports in due course, and further encourages shareholders and management at each MDB to establish regular reviews of alignment of each MDB's resources with its strategic objectives. At the system-wide level, the IFA WG is currently engaged in a high-level MDB capital review, the results of which may inform potential future steps.

5c: Establish enhanced dialogue and cooperation on capital adequacy, risk management and risk mitigation tools

The G20 CAF report considered that system-wide institutional arrangement tasked to address MDB CAF issues could provide useful services to MDBs, shareholders and market participants. Potential services include collating and evaluating MDB benchmarking, sharing best practices, providing CAF-related training to MDB executive directors, convening discussions on CAF issues and undertaking analysis. The recommendation provided general conceptual guidance and left discussion of potential institutional arrangements to the G20 and MDB shareholders.

Assessment: **Limited Progress**

In response to this recommendation, MDBs have enhanced their engagement on CAF issues via stepped-up activity of the CRO/CFO forum, which the G20 considers to be a highly positive initiative that should be further encouraged and strengthened. At the same time, this arrangement fulfils only a limited subset of the activities that was envisioned by the G20 CAF panel. In particular, the CRO/CFO forum does not offer independent input or a systemic view of how CAF issues fit strategically within the wider goals of MDBs in a way that could be useful to shareholders.

Path Forward

Consensus has not yet been reached among G20 members or MDB management on whether further efforts are merited to pursue this recommendation, and if so, what form it might take. A number of factors need to be taken into account, including data confidentiality, independent views, continuity of knowledge function and administrative status, among others. Options put forward by the G20 presidency expert team, which may merit further discussions within the IFA WG and among MDBs, include:

Create a dedicated MDB CAF unit either as an independent entity or (more realistically) linked to existing structures such as the IFA WG secretariat or the Bank for International Settlements.

Deploy the CRO/CFO forum to engage more systematically on CAF issues. While the CRO/CFO forum could remain in its current form on all other issues, it could be tasked with a dedicated team to track, share information and undertake studies on CAF issues to report to MDB boards and the IFA WG. MDBs have indicated that they are intending to formalize the status of the CRO/CFO forum to take the lead on CAF-related issues. The G20 may wish to request further information to understand if such a step meets the goals of this recommendation.

A modest step up from the status quo requiring the least administrative resources would be for the IFA WG to invite a sub-set of CAF panel members and/or independent experts on a regular basis to provide continuity on CAF matters.

5d: Transform GEMs into stand-alone entity to support improved understanding of MDBs by private investors and CRAs

The Global Emerging Markets Risk Database Consortium (GEMs) began in 2009 as a joint initiative between the EIB and IFC and has since grown to have 25 DFI and MDB members. GEMs shares anonymized data from members on credit defaults, client credit rating migrations and recovery statistics, which inform MDB and DFI financial calculations and policies. This unique data could help other actors—including private investors, rating agencies and sovereigns considering development-related transactions—to better evaluate risks, but GEMs data is for the most part not publicly available. It may also be useful to evaluate and quantify the potential existence of PCS for MDB lending to non-sovereign borrowers, which could be reflected in CRA methodologies. The recommendation proposes to convert GEMs into a stand-alone entity with a new governance structure better able to share anonymized granular data.

Assessment: **Partial Progress**

Despite considerable attention and effort on the part of MDBs to move to a "GEMs 2.0" following publication of the G20 CAF report, institutional and legal obstacles appear to have prevented the creation of a new stand-alone arrangement. Efforts have instead turned toward strengthening the governance and management model of GEMs to create an improved ring-fenced entity that will continue to be hosted by EIB. This solution provides an effective way to move quickly towards the dissemination of GEMs statistics. In March 2024, GEMs published the first Recovery Statistics report for private and sub-sovereign lending from 1994 to 2022, complementing the annual default frequency reports published since 2020. As well, IFC published a Default Rate Analysis report with disaggregated default rates on commercial loans from 1986 to 2023 and EBRD released a similar study at their 2024 annual meeting. A second major GEMs study will be released in the fall of 2024, and in parallel an in-depth market study is being implemented to better understand potential demand for GEMs statistics by private investors.

Path Forward

Based on feedback at the June 2024 IFA WG meeting in Fortaleza, G20 members are comfortable with the strategic path taken by the GEMs Steering Committee to no longer pursue a stand-alone entity and instead focus on accelerating the provision of granular data to achieve the goals articulated in the recommendation. The efficacy of this approach will be judged primarily on the granularity (country, sector, lending institution) and quality of data that GEMs is able to produce. The IFA WG may wish to revisit this discussion after the upcoming GEMs report is released, to evaluate its quality.

VII. FINANCIAL HEADROOM GAINS THUS FAR FROM CAF REFORMS

Caution must be taken in assessing financial gains due to CAF reforms, as many reforms will take time to materialize, depend on factors not always under MDB control and, in some cases, are intended to promote improved CAF governance without direct headroom benefits. Efforts to generate precise estimates can have misleading results and may distract from the content of needed reforms. Nonetheless, it is informative to have a broad sense of how recommendations have translated into MDB lending gains to better evaluate system-wide operational capacity and to learn from CAF reform experiences across different MDBs. The outcomes are summarized in Table 2.

Collectively, CAF reforms already have unlocked an estimated $170 billion in lending headroom to be deployed in the coming decade across the reporting MDBs, with $113 billion more projected to be finalized by end-2024 and an additional $74 billion targeted. This total of $357 billion is in line with the $300-400 billion figure in the Heads of MDBs Viewpoint note of April 2024 for CAF reforms across the major MDBs over 10 years. Much of the targeted headroom is expected to be driven by hybrid capital and risk transfers to commercial and official counterparties as described in Recommendation 3, although the final amounts will depend on investor demand and market conditions. Other balance sheet measures related to the CAF agenda but not specifically recommended in the CAF report have already generated an additional $7 billion in lending capacity and are projected to create $41 billion in coming years.

Should shareholders and MDBs press ahead with Recommendations 1 and 2, this could result in substantially more gains beyond the $300-400 billion estimated by Heads of MDBs. One independent study suggested that Recommendation 2 alone could result in gains of between 6% and 25% in loan portfolio capacity at individual MDBs, depending on the approach used.[21] Further substantial gains can be generated if CRA methodologies are reformed through MDB and shareholder influence to more appropriately account for PCS[22] and concentration risk.[23] Reducing the requirement to obtain AAA ratings to two instead of three CRAs could also boost to lending capacity due to the high variance across CRA methodologies.

21. Humphrey et al. (2024). "Maximising the developmental impact of callable capital: Project findings and path forward," p. 27.
22. Risk Control (Forthcoming). "Quantifying Preferred Creditor Treatment for Multilateral Development Bank Sovereign Loans."
23. E. Lüktebohmert-Holtz, J. Sester and H. Shen. (2024). "On the Relevance and Appropriateness of Name Concentration Risk Adjustments for Portfolios of Multilateral Development Banks." Available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4642039.

Table 2. Incremental Lending Capacity Gains from CAF Reforms (US$ billions over 10 years)

Recommendation	Implemented as of June 2024	In Progress (end-2024)	Expected	Total
1a Adjust CAF Risk Tolerance	ADB: $100 bln IBRD: $40 bln* IDB Invest: $1.98 bln			$141.98 bln
1b MDB-specific Factors in CAFs	AIIB: $15 bln			$15 bln
2a Incorporate Callable Capital				
3a Hybrid Capital	AfDB: $2 bln	ADB: $20 bln IBRD: $7.4 bln	AfDB: $4.8 bln EBRD: $3.745 bln IDB: $15 bln NDB: $4 bln	$56.945 bln
3b Commercial Risk Transfer	ADB: $2 bln AfDB: $2 bln (combined with 3c) EBRD: $1.605 bln IDB: $550 mln IDB Invest: $1.56 bln	IDB Invest: $1.13 bln IFC: $130 mln	CDB: $350 mln EBRD: $3.21 bln IDB: $1 bln IDB Invest: $34.56 bln IFC: $1.8 bln	$49.895 bln
3c Shareholder Portfolio Guarantees	EBRD: $3.21 bln IDB: $469 mln	ADB: $10 bln IBRD: $74 bln	IDB: $1.5 bln NDB: $3 bln	$92.179 bln
3d Counter-cyclical callable capital				
3e MIGA risk transfers			IDB: $1 bln	$1 bln
3f Central bank liquidity lines				
4b Rating agency methodologies				
TOTAL	**$170.374 bln**	**$112.66 bln**	**$73.965 bln**	**$356.999 bln**
Other Non-CAF Balance Sheet Measures				
Exposure Exchange Agreements	IDB: $5.5 bln	ADB: $3 bln CDB: $700 mln IDB: $10 bln NDB: $4 bln	IDB: $15 bln	$38.2 bln
Guarantees from other MDBs	IBRD: $1.5 bln AIIB: $400 mln			$1.9 bln
Non-shareholder guarantee			CDB: $600 mln	$600 mln
TOTAL	**$7.4 bln**	**$17.7 bln**	**$15.6 bln**	**$40.7 bln**

Source: Reporting by MDBs to IFA WG. MDBs not reporting data for this table include CAF, EIB and IsDB.

Notes: All figures under "In Progress" and "Expected" reflect the best estimates of MDB management at reporting date but may change going forward. One-time transactions or policy changes have been pro-rated over a 10- year period to facilitate comparisons. Increases to paid-in or callable capital are not included. Impacts of some recommendations (like 4b) cannot yet be assessed due to degree of uncertainty but will be reassessed for subsequent reporting.

*IBRD chose to report this headroom gain under Recommendation 1a, although in the text of this report it is discussed under Recommendation 2a due to the link with callable capital.

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AfDB (2024) "African Development Bank Group Board of Governors Approves $117 billion General Callable Capital Increase." 02 June 2024.

Basel Committee for Banking Supervision (2019). "Core principles for effective banking supervision." Update December 2019.

European Bank for Reconstruction and Development (2024). "Callable Capital Review." 17 April 2024

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Moody's (2024). "Greater transparency of MDB callable capital strengthens our view of shareholder support." 30 May 2024.

Risk Control (Forthcoming). "Quantifying Preferred Creditor Treatment for Multilateral Development Bank Sovereign Loans."

Risk Control (2022). "MDB Portfolio Expansion: Agency Ratings and Value at Risk." 28 June 2022.

Scope (2024). "Scope publishes updated supranational rating methodology and calls for comments." 10 May 2024.

UBS (2022). "Impact investing through Multilateral Development Banks." 01 November 2022, available at https://www.ubs.com/global/en/assetmanagement/insights/asset-class-perspectives/etf/articles/impact-investing-through-mdbs.html.

ANNEX 1: TEMPLATE FOR MDB REPORTING ON IMPLEMENTATION OF CAF REVIEW RECOMMENDATIONS

The template circulated to MDBs in spring 2024 was substantially the same as that of 2023. With the approval and input of the IFA WG and MDBs, it was modified slightly with the aim of: i) simplify reporting burden for MDBs; ii) accounting for CAF-related developments in the preceding year; and iii) seeking more detailed information on specific issues. The revised template and accompanying instructions are reproduced below for reference.

For each CAF reform, please answer in one of three ways:

1. Reform is fully implemented

If this is an MDB's answer, please specify further:

a. What policy was modified and in which way

b. Project financial impact, including causal mechanisms leading to impact. If not quantifiable, explain why and detail other impacts.

c. Why no further reforms in this area are feasible.

2. Reform is in progress

If this is an MDB's answer, please specify further:

a. Progress thus far and what remains for further or full (as relevant) reform implementation

b. Project financial impact, including causal mechanisms leading to impact. If not quantifiable, explain why and detail other impacts.

c. Estimated time for completion (or, if an ongoing effort, project plans going forward)

3. Reform is not appropriate for the MDB

If this is an MDB's answer, please specify further:

a. Why the reform is not appropriate or applicable.

b. Whether it may be appropriate if certain obstacles are addressed, and if so, what those are.

For each recommendation, please specify the degree to which you are working in conjunction with other MDBs, including a) which MDBs; b) which type of forum; and c) future plans for continued or expanded collaboration in this area.

Apart from the above questions, see specific questions below related to individual reforms.

Implementation of CAF review recommendations

It is noted that all the questions may not be applicable to all MDBs and that MDBs governing bodies will decide ultimately which recommendation of the CAF Review each MDB can implement and to what extent they will do it.

Area	Recommendation	Comments
General		Summary of recommendations already implemented and estimated or targeted financial impact over 10-year horizon.
		• What high level guidance can the G20 provide to facilitate a cross MDB approach on specific recommendations where such an approach is warranted? • Which recommendations need support from G20 and how do you expect G20 to provide support for implementing each recommendation?
		- Are there other measures, apart from the CAF recommendations, that you are considering in order to expand your lending capacity?
1. Adapt approach to define risk tolerance	**1a. Shift risk appetite definition toward shareholder-defined limits.**	**Status:** **Comments:** **If already/to be implemented:** • How will you shift the risk appetite definition toward shareholder-defined limits? How are you considering this recommendation in conjunction with recommendations 1b and 2a? If not considered: Why not? Impact on the rating: Expected timeline and milestones over the next 3 years:
	1b. Ensure frameworks account for MDB-specific features.	**Status:** **Comments:** **If already/to be implemented:** • How do you plan to implement this recommendation? • Which difficulties have you identified to implement it and how could they be overcome? • NOTE: PCT/concentration risk will be addressed in deep dive exercise as part of 2024 G20 IFA agenda If not considered: Why not? Impact on the rating: Expected timeline and milestones over the next 3 years:

<table>
<tr><th>Area</th><th>Recommendation</th><th>Comments</th></tr>
<tr><td>1. Adapt approach to define risk tolerance</td><td>1c. Relocate specific numeric leverage targets from MDB statutes.</td><td>Status:
Comments:
If already/to be implemented:
• Which ratio would you remove/modify? What could be the potential implications and risks, and how to mitigate?
• Does it require modifying the Articles of Agreement? Which changes should be made?
Impact on the rating:
Expected timeline and milestones over the next 3 years:</td></tr>
<tr><td>2. Give more credit to callable capital</td><td>2a. Incorporate a prudent share of callable capital into the calculation of capital adequacy.</td><td>Status:
Comments:
If already/to be implemented:
• List measures taken by MDB and shareholders of the MDB to clarify and/or modify (as appropriate) rules and procedures related to callable capital.
• Does the MDB include a portion of callable capital in its internal capital adequacy calculation, and if so, how?
• Has the MDB explored ways to better reflect the value of callable capital in capital adequacy calculations? If so, how would this be done and what would be the financial impact? If not, what are the difficulties to overcome?
• Would this reform be facilitated by modifying MDB statutes, and if so, how?
If not considered: Why not?
Financial impact:
• If implementation were possible, what would be the estimated impact on lending headroom, and based on which assumptions?
Impact on the rating:
Expected timeline and milestones over the next 3 years:</td></tr>
<tr><td>3. Expand uses of financial innovations</td><td>General</td><td>Comments:
• Have you been collaborating with any of the other MDBs to implement any financial innovations? If yes, kindly elaborate. If no, please indicate the reasons preventing you from doing so.</td></tr>
</table>

<table>
<tr><th>Area</th><th>Recommendation</th><th>Comments</th></tr>
<tr><td rowspan="2">3. Expand uses of financial innovations</td><td>3a. Endorse MDB consideration of non-voting capital classes (paid-in equity or hybrid) to contribute to available capital.</td><td>Status:
Comments:
If already/to be implemented:
How do you plan to implement this recommendation? Would this be a one-off transaction or a regular/semi-regular issuance?
Who are principal target investors (shareholders, foundations, private sector, etc.)?
What would prevent implementing this recommendation and how to overcome? Would it impact on the terms of borrowing for MDB client countries (if to commercial investors)? Would it impact MDB project selection priorities (if to official investors)?
Is SDR rechanneling appropriate for the MDB, and does the MDB have plans to implement if the instrument moves forward?
Should system-wide standards be encouraged for comparable treatment of SDR-backed hybrids across MDBs?
How can the G20 and shareholders support the cross-MDB coordination needed to implement the rechanneling of SDRs?
If not considered: Why not?
Impact on the rating:
Financial impact:
Have estimates of potential headroom gains due to recommendation changed in the past year due, and if so, why?
Expected timeline and milestones over the next 3 years:</td></tr>
<tr><td>3b. Introduce & scale portfolio risk transfers to the private sector, including through outright shares, insurance and securitization.</td><td>Status:
Comments:
If already / to be implemented:
What risk transfer instruments/approaches are you using already and what is their scale? What impact are they having on different risks? Are they for sovereign or non-sovereign exposures (if both, specify amounts or percentages)?
What collaboration is underway with other MDBs to develop this instrument and engage with CRAs and investors?
Do you see this as a limited or ongoing type of transaction?
If not considered: Why not?
Financial impact:
Have estimates of potential headroom gains due to recommendation changed in the past year due, and if so, why?
Impact on the rating:
Expected timeline and milestones over the next 3 years:</td></tr>
</table>

Area	Recommendation	Comments
3. Expand uses of financial innovations	**3c. Encourage shareholder guarantees on loans related to crosscutting priorities.**	**Status:** **Comments:** **If already/to be implemented:** • What implications do these instruments have for MDB governance and project selection priorities? • What volume of shareholder guarantees are used currently, reasoning behind it (concentration, portfolio risk etc)? • Do you use both targeted and portfolio-based guarantees? If not considered: Why not? Impact on the rating: Expected timeline and milestones over the next 3 years:
	3d. Support collective shareholders commitments of pools of additional callable capital.	**Status:** **Comments:** **If already/to be implemented:** • What benefit could you expect from this measure if implemented? If not considered: why not? Impact on the rating: Expected timeline and milestones over the next 3 years:
	3e. Support adaptation of MIGA's products & reinsurance capability to transfer portfolio level risk from MDB balance sheets.	**Status:** **Comments:** **If already/to be implemented:** • For MIGA only: What have management and shareholders concluded in terms of the feasibility and desirability of implementing this recommendation? • How do you plan to work with other MDBs in this regard, and what interest have other MDBs shown in working with MIGA in this area? If not considered: Why not? **Financial impact:** • Have estimates of potential headroom gains due to recommendation changed in the past year due, and if so, why? Impact on the rating: Expected timeline:

<table>
<tr><th>Area</th><th>Recommendation</th><th>Comments</th></tr>
<tr><td>3. Expand uses of financial innovations</td><td>3f. Consider ways to provide MDBs access to central bank liquidity.</td><td>Status:
Comments:
If already/to be implemented:
• What benefits could you expect from this measure, if implemented?
• What support could the G20 offer to facilitate its implementation?
• Have there been any discussions with shareholders on this issue?
If not considered: Why not?
Financial impact:
• Have estimates of potential headroom gains due to recommendation changed in the past year due, and if so, why?
Impact on the rating
Expected timeline and milestones over the next 3 years:</td></tr>
<tr><td rowspan="2">4. Improve credit rating agency assessment of MDB financial strength</td><td>4a. Strengthen communication with credit rating agencies.</td><td>Status:
Comments:
If already/to be implemented:
• How do you communicate with CRAs? Who participates in meetings between the MDB and the CRAs?
• How could the G20 help improve this communication and improve the analysis of CRAs?
• How have CRA criteria changed in the past year as relevant to the MDB?
Impact on the rating:
Expected timeline and milestones over the next 3 years:</td></tr>
<tr><td>4b. Encourage steps by rating agencies to strengthen their MDB evaluation methodologies.</td><td>Status:
Comments:
If already/to be implemented:
• What are currently the most critical parameters of CRA methodologies that constrain the MDB? Is it possible to quantify their impact in terms of lending headroom?
• How can MDBs or the G20 more effectively provide information relevant to foster changes in CRA methodologies?
• What benefit could you expect from this measure if implemented?
If not considered: Why not?
Financial impact:
• Have any specific CRA criteria changes resulted in greater lending headroom? If so, please detail.
Expected timeline and milestones over the next 3 years:</td></tr>
</table>

Area	Recommendation	Comments
4. Improve credit rating agency assessment of MDB financial strength	**4c. Take proactive approach to incorporation of ESG factors in rating methodologies.**	**Status:** **Comments:** **If already/to be implemented:** • What impact will it have on the MDBs lending? How could MDBs implement this recommendation? • What benefit could you expect from this measure if implemented? If not considered: Why not? **Financial impact:** • How much amount of lending headroom would the implementation of the relevant recommendations create? Impact on the rating Expected timeline and milestones over the next 3 years:
5. Increase access to MDB data and analysis	**5a. Strengthen the ability of shareholder boards to effectively set parameters of capital adequacy policies and overseeing their implementation.**	**Status:** **Comments:** **If already/to be implemented:** • What actions have been taken toward this recommendation? • Would you set up a group of audit and risk experts to support board's decision-making process? • How would it affect the split of responsibilities between the board and the management? • Would formalized and systematic training provision be appropriate for board members on CAF issues? If not considered: Why not? Expected timeline and milestones over the next 3 years:
	5b. Establish yearly capital benchmarking report presenting key elements & data in comparable format with harmonized definitions. Support regular reviews of capital resources.	**Status:** **Comments:** **If already/to be implemented:** • When was most CAF recent update; summarize key changes from previous; when is the next update planned? • Would you agree to have this yearly report? How could it be conducted? If not considered: Why not? Impact on the rating Expected timeline and milestones over the next 3 years:

Area	Recommendation	Comments
5. Increase access to MDB data and analysis	5c. Establish enhanced dialogue and cooperation on capital adequacy and risk management.	**Status:** **Comments:** **If already/to be implemented:** • Would you agree to set up such a forum? How could it be implemented? If not considered: Why not? Expected timeline and milestones over the next 3 years:
	5d. Transform GEMs into stand-alone entity to support improved knowledge for MDBs, private investors and CRAs.	**Status:** **Comments:** **If already/to be implemented:** • How can the G20 and shareholders support the cross-MDB coordination needed to implement this recommendation? • Which data do you already share and which additional ones could you share? • Which difficulties do you need to overcome to implement this recommendation? If not considered: Why not? Expected timeline and milestones over the next 3 years:

Innovations not included in CAF report (VOLUNTARY REPORTING ONLY)	Other innovations the MDB would like to report	**Status:** **Comments:** • Here please include other CAF or balance sheet optimisation innovations that the MDB considers noteworthy to highlight and which can provide lessons learned for other MDBs. • In all cases, include: i) type of innovation; ii) scale of current/potential implementation; iii) challenges; iv) estimated financial impact. Impact on the rating: Expected timeline and milestones over the next 3 years:

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