ove Office of Evaluation and Oversight

Corporate Evaluation

Evaluation of IDB Invest

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Contents

Acknowledgements

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Acronyms and Abreviations

ADB	Asian Development Bank
ADV	Advisory Services Division
CAR	Capital adequacy ratio
CECL	Current expected credit losses
CTUs	Client Transaction Units
DEA	Development Effectiveness Analytics system
DELTA	Development Effectiveness Learning, Tracking, and Assessment
DRA	Development-related assets
DSP	Strategy and Development Department
DVF	Development Effectiveness Division
EBRD	European Bank for Reconstruction and Development
ECG	Evaluation Cooperation Group
FCR	Financial contribution rating
IFC	International Finance Corporation
INO	Investment Operations Department
MDBs	Multilateral Development Banks
MGM	Management Grievance Mechanism
MICI	Independent Consultation and Investigation Mechanism
MOK	Mountains of Knowledge
MSMEs	Micro, small, and medium-sized enterprises
NSG	Non-sovereign guaranteed
OMJ	Opportunities for the Majority Initiative
OVE	Office of Evaluation and Oversight
PPPs	Public-private partnerships

RAROC	Risk-adjusted return on capital
RSM/SER	Risk Management Department
SCF	Structured and Corporate Financing Department
SEG	Environmental, Social, and Governance Division
SFDs	Sector framework documents
SG	Sovereign-guaranteed
SLA	Service-level agreement
SMEs	Small and medium-sized enterprises
TFFP	Trade Finance Facilitation Program
VPC	Vice Presidency for Countries
XSR	Expanded supervision report

Executive Summary

At the 2015 annual meeting in Busan, the Boards of Governors of the Inter-American Development Bank (IDB) and the Inter-American Investment Corporation (IIC) decided to consolidate the IDB Group's private-sector operations into the IIC. This process of consolidation and capitalization, known as the private sector merge-out, took effect on 1 January 2016. The Busan Resolution set forth a "Renewed Vision" for promoting development in the region through the private sector. This Renewed Vision provides a long-term framework (2016-2025) for IDB Invest and focuses on the objectives of: (i) strengthening effectiveness and additionality; (ii) maximizing synergies between the public and private sectors; and (iii) maximizing the efficient use of resources and ensuring long-term financial sustainability.

This evaluation seeks to independently assess and report on the effectiveness of the implementation to date of the Renewed Vision, aimed at promoting development in the region through the private sector. Specifically, the general question that the evaluation aims to answer is the following: To what extent is IDB Invest on its way to achieving the end objectives set out in the Renewed Vision? To that end, the Office of Evaluation and Oversight (OVE) used a combination of complementary methods, including a review of strategic and corporate documents, financial and portfolio analyses, interviews and surveys, and documentary analyses of a sample of operations. This evaluation covers the 2016-2021 period and uses as reference the findings in OVE's 2017 midterm review of implementation of the merge-out to further analyze areas that had not yet matured at that time. The evaluation was also guided by a reference framework that linked the objectives of the Renewed Vision to the main activities and initiatives undertaken thus far to help achieve those objectives.

A. Overview of the evolution of IDB Invest

The evaluation period saw the rapid growth of IDB Invest. Despite a slower than expected launch of operations, IDB Invest has outperformed the vast majority of the business volume targets set in Busan. The portfolio of development-related assets (DRA) managed by IDB Invest has grown since the merge-out process took effect.[1] The level of commitments has undergone a significant increase, mainly since 2020 as part of the operational strategy in response to the crisis caused by the COVID 19 pandemic. That crisis put IDB Invest's response capacity to the test, and the institution had to revise and adapt its immediate priorities.

To a large extent, this rapid growth has been driven by the development of capacity for operation origination and structuring, deployment of a wider array of products, and mobilization of third-party resources. The committed amounts (excluding short-term financing) have mostly targeted operations for the infrastructure and financial institution segments in Group A and B countries. Despite IDB Invest's efforts, there continue to be challenges to expanding support in certain countries, such as small and island countries.

B. Strengthening effectiveness and additionality

IDB Invest has taken steps in several areas to strengthen effectiveness and additionality, including the implementation of the Impact Management Framework, the expansion of the financial and nonfinancial solutions, the further decentralization of employees, and improvements to operation management processes.

- **Impact Management Framework**

The rollout of the impact Management Framework is an important step forward. During the evaluation period, IDB Invest gradually implemented a series of management tools to shape the different stages of the project cycle. Before the merge-out, the various private-sector windows had differing approaches to effectiveness, and there were few tools available at that time. This presented an opportunity to conceptualize a framework with a system approach from the start. The tools envisioned in the framework were developed, and the framework itself aligns with the principles for impact management developed by financial development institutions. Beyond the need to continuously improve these tools, the extent to which they have been adopted and used varies, which has much to do with the emphasis IDB Invest placed on portfolio building and origination during the evaluation period.

One important challenge is the need to redefine the strategic selectivity approach for selecting operations and clients. The existing tool is not a useful guide for origination efforts because it does not effectively address key dimensions of the selection process, such

1 The DRA portfolio managed by IDB Invest (taking outstanding balances into account) stood at US$10.855 billion at year-end 2021, a significant increase compared to the IDB Group's combined non-sovereign-guaranteed portfolio at year-end 2015 (US$6.99 billion) before the merge-out.

as development gaps, client demand and perspectives, and IDB Invest's offerings, taking into account the institution's comparative advantages, priorities, and mandates.

The system's most developed and institutionalized tool is the Development Effectiveness, Learning, Tracking, and Assessment tool (DELTA), which has implications for decision-making during approval. DELTA scores are useful for evaluating and synthesizing the various dimensions of an operation's impact in support of origination and supervision processes, even though the direct interpretation of aggregate scores is a complex task. The average annual DELTA score at approval rose during the evaluation period, with infrastructure and energy operations boasting significantly higher DELTA scores than operations in other segments. The DELTA has also begun to be used increasingly during the supervision stage, which provides an opportunity to develop targeted corrective actions.

The Portfolio 2.0 approach has been used to help strike a balance between development impact and financial returns in line with its stated objective, ensuring that minimum thresholds for these variables are met in a simple, practical manner. However, the tool is not as widely used to strike a balance between options at the sub-portfolio level.

There is evidence of progress toward a more systematic identification of lessons learned at the operation level, but use of those lessons to inform the design of new operations is still incipient. At the institutional level, the development of a strategy for managing and integrating the knowledge generated by the institution is a pending task.

- **Financial and nonfinancial solutions**

IDB Invest has expanded the financial solutions it offers considerably since the merge out. However, this expanded offering has not yet translated into a more diversified portfolio, especially in small countries.

IDB Invest expanded its offering of short-term products, with Trade Finance Facilitation Program (TFFP) and reverse factoring operations accounting for the bulk of short-term operations. With respect to the TFFP, IDB Invest worked to fine-tune its selectivity to improve additionality, but there is room, from a development outcomes perspective, for continued strides toward expanding coverage for small and medium-sized enterprises (SMEs). The TFFP has high strategic value for IDB Invest because the program is used as a mobilization instrument and as a gateway to get to know potential clients. Even so, its availability could be heavily restricted with the end of the cross-booking period. Reverse factoring is still a relatively new instrument, but emerging findings point to the need to improve the selectivity of these interventions.

IDB Invest also developed a broad array of long-term financing solutions as well as solutions in local currency. Nonetheless, use of some products was limited by internal restrictions (e.g., availability of capital and effective processes in place) or market constraints. IDB Invest has also built significant capacity for resource mobilization, which has translated into a higher volume of resources mobilized and a wider array of mobilization instruments. Though IDB Invest reports US$10.7 billion in core mobilization since the merge-out (US$24.4 billion when including catalytic mobilization as well), these figures are lower than the estimates set out in the Renewed Vision (US$34.2 billion over the 2016-2021 period).[2]

On the nonfinancial front, notable progress has been made in terms of building internal capacity for managing advisory services and nonfinancial risk. The primary focus of the advisory services model was to support operations in priority areas during the origination stage, with a series of challenges at play. Selection of the clients and operations that would receive advisory services was ad hoc and does not have discernible prioritization criteria. The recent development of diagnostic assessment tools for analyzing client capacity is an important step toward building a more robust process for advisory service selection and design. Furthermore, resource use has been hindered by certain constraints associated with the funding model, which relies primarily on resources from IDB Invest donors. In addition, advisory services do not have a results-based monitoring and evaluation system, which is critical considering how the advisory services portfolio has grown, the role those services play in channeling nonfinancial additionality, and IDB Invest's intention of expanding their reach beyond transactional support.

- **Operational aspects: Decentralization and operation management processes**

As its business volume has increased, IDB Invest has been gradually building a more diverse workforce and has expanded its footprint in the region. As of December 2021, IDB Invest had a presence in 25 countries, a significant increase compared to December 2016, when it was in 14 countries. Over the same period, the share of staff in the region rose from 16% to 31%, outperforming the target set out in the field presence plan (30%). Nevertheless, there is room to deepen the decentralization process. The increase of staff in the region has not been accompanied by a decentralization of processes and decision-making. Also, the decentralization process has primarily emphasized expansion of origination capacity, with further decentralization of other support areas proving to be a challenge.

2 Those estimates were for mobilization as a whole and did not distinguish between core and catalytic mobilization (audiovisual presentation CII/PP-149).

IDB Invest implemented process improvements at the operation origination stage under its Operational Excellence initiative, which effectively shortened timeframes (mainly at the eligibility stage) by streamlining documents and requirements and increasing delegation of authority. The implementation of improvements at the supervision stage has gained less traction. Overall, as its business volume has increased, its offerings have expanded, and its products have become more complex, IDB Invest has taken important steps toward enhancing its processes and systems. Significant challenges remain, however, considering the institution's rapid growth. The need to revise and continue to improve processes and systems and, more generally, the institution's backbone, is still a crucial challenge to increasing operational efficiency, developing closer relationships with clients, and scaling up business volumes and products.

- **Results**

Despite the efforts and progress discussed above, **strengthening operation effectiveness and additionality** continues to be a major challenge.

Expanded supervision reports (XSRs) validated by OVE for operations that reached early operational maturity show that effectiveness is one of the lowest rated dimensions, though these ratings are trending slightly up. The main drivers of this underperformance in operation effectiveness were related to macroeconomic developments and to certain issues with design or definition of indicators. Though most operations at the supervision stage analyzed by OVE are proceeding as expected, approximately one-third show signs that their development objectives may be difficult to achieve and thus require active supervision and implementation of corrective measures.

Meanwhile, the vast majority of the operations analyzed by OVE incorporated elements of additionality, which attests to the variety of potential sources of additionality and the diverse paths to achieving it in projects. Considering the evolution of the additionality concept and its sources, and the difficulties to operationalize and justify it, stakeholders within IDB Invest, including its Board of Executive Directors, have differing understandings and expectations regarding additionality at the operation level and the type of evidence needed to demonstrate it. Though IDB Invest developed internal guidelines for assessing an operation's additionality, the institution is lacking an specific strategic framework, shared widely among its various stakeholders, that helps operationalize additionality while fostering a common understanding across all parties. In addition, as at other multilateral development banks (MDBs), at IDB Invest additionality focuses mainly on the operation level, with limited attention being paid to the concept and its analysis at more strategic levels, including the country, sector, instrument, and client levels.

C. Maximizing synergies between the public and private sectors

There is evidence of progress in the area of public-private synergies in recent years, though major challenges remain to maximizing the complementarity of the toolkit of solutions offered by the IDB Group.

IDB Invest has taken significant steps to promote alignment and collaboration with the rest of the IDB Group at the strategic level. Notably, the institution has gotten increasingly involved in the development of strategies at the IDB Group level (e.g., climate change, gender, and diversity). Headway has also been made toward making IDB Invest's involvement in the development of country strategies more systematic. Use of this tool to guide origination efforts continues to be a challenge, however, and there are opportunities to further engage IDB Invest in the process of ongoing dialogue between the IDB and the governments, especially during country strategy implementation, so that this dialogue can continuously inform the operation origination and selection process. IDB Invest has participated in the development of some sector framework documents (SFDs), but its involvement to date has been limited and less systematic than its involvement in the country strategy process.

The expansion of the Country Representative role to make representatives accountable for the IDB Group's public and private-sector windows is a pivotal step forward for the identification and promotion of synergies at the country level. Nevertheless, there are limitations to the effectiveness of this expanded role. Country Representatives predominantly come from the public sector, and their previous experience is mainly in that sector. Staff respondents largely attribute this to the lack of competitive, merit-based processes for the selection of Country Representatives, an issue that was also recently identified by OVE in its evaluation of the IDB's governance. Moreover, IDB Invest's involvement in the candidate identification and selection process has been very limited. In addition, the Country Representatives' newly assigned responsibilities have not been supported by clear performance evaluation, as the criteria for evaluating representatives' performance with respect to their private-sector duties have not been clearly defined, nor is IDB Invest formally involved in the performance evaluation process. Better communication and training for Country Representatives is also needed in order to empower them to perform their IDB Invest-related duties. Moreover, the SG-NSG coordinator role is still in the development process.

In general, there is a positive perception of progress in terms of coordination at the IDB Group. There is still room to improve, however, as this coordination is not yet entirely effective. Until now, coordination has been an ad-hoc process that depends on the individuals involved.

In particular, some of the factors identified by OVE as inhibitors of more effective coordination at the operation level are a lack of staff incentives as well as a lack of institutional processes and mechanisms for identifying and promoting synergies. Given this situation, there are opportunities to leverage complementarities across the IDB Group's windows, including the systematic identification of potential areas for internal collaboration; the clarification of the various windows' roles and the timing and scope of their interventions; and a more coordinated process for operational planning and for managing the knowledge generated by the institutions.

D. Efficient use of resources and ensuring financial sustainability

IDB Invest has made considerable strides toward strengthening its financial capacity and managing its financial and capital risk with the aim of ensuring its long-term financial sustainability. The capitalization process has proceeded as expected, with no major delays. In the first few years, capital was in abundant supply due to such reasons as advance payments of some countries' capital contributions, lower than expected disbursements, and higher than expected use of cross-booking. The high level of untapped capital had an opportunity cost in that it was not generating revenue, but it did enable IDB Invest to significantly increase its business volume during the pandemic. More recently, capitalization levels have settled near the prudential limits. As capital has become scarcer, IDB Invest has taken measures to optimize its use (e.g., by using credit insurance), and its efforts to that end continue.

With a large inflow of new capital contributions and a more ambitious mandate, IDB Invest developed its capital and risk management framework, under which the institution operationalized its mandate of maintaining a minimum "AA" credit rating. However, application of the rating agencies' methodologies results in significantly higher capital requirements, requiring for 67% more capital, on average, than IDB Invest's internal model in 2021. Differentials that large undermine IDB Invest's ability to manage and optimize its capital, an issue that affects other MDBs as well.

While IDB Invest has outperformed its business volume targets, its net income has fallen short of the projections set out in the Renewed Vision (55% less than projected for the 2016-2021 period). On the income front, IDB Invest was able to consolidate its ability to generate revenue through of its own balance sheet. In addition, revenue from services provided to the IDB (mainly due to cross-booking) have performed in line with the projections in the Renewed Vision, with 2023 being the first year in which IDB Invest will not book new operations on the IDB balance sheet. Meanwhile, IDB Invest's operating costs have trended upward, increasing in proportion to the growth of its origination volume and the size of its portfolio. Therefore, the unit costs of origination and supervision remained relatively stable over the evaluation period. IDB Invest posted a net income every year over the 2016-2021 period, amounting to a total of US$197.7 million in cumulative gains and accumulating US$92.3 million in capital.

In addition, IDB Invest built a credit portfolio that has proven to be resilient so far, despite the shock of the pandemic. IDB Invest maintained satisfactory portfolio quality and managed the cross-booking arrangement in line with the established parameters. The risk profiles of the operations booked on the two balance sheets (IDB Invest and IDB) were similar. IDB Invest was able to keep its portfolio's ratio of impaired projects (nonperforming loans) low, and most of those impaired projects were approved prior to the merge-out. As the portfolio has matured, strains on credit quality have not translated into impaired loans, instead coming through as a higher number of projects with potential problems.

Significant progress has been made in terms of the development and implementation of financial planning and analysis tools. Yet there is room for improvement; notably, IDB Invest should expand use of risk-adjusted return on capital (RAROC)[3] beyond the approval stage and increase the granularity of the administrative budget it submits to the Board of Executive Directors, systematically linking costs to output metrics.

E. Conclusions and recommendations

In summary, IDB Invest has made strides toward achieving the objectives set out in the Renewed Vision. More specifically, despite some limitations, IDB Invest has managed to build a sizable portfolio of operations in the region, thereby positioning itself as a development partner through the private sector. IDB Invest has laid a foundation for sound financial management in the interest of ensuring its long-term financial sustainability. **The objective of strengthening effectiveness and additionality continues to be a key challenge**. At present, a considerable share of IDB Invest-supported operations did not fully achieve the development objectives that justified their financing. In addition, although most operations involved elements of additionality, elements of additionality, it is essential to strengthen the institutional focus on this concept at a more strategic level to achieve greater additionality at the country, client, sector, and instrument levels. This is the core objective of the Renewed Vision that led to the merge-out and capitalization of IDB Invest over the

3 RAROC is a tool that is used to analyze the return of an operation while accounting for the economic capital it requires.

2016-2025 period and thus is the institution's greatest challenge that requires priority attention, regardless of any changes that the institution may make to its business model.

Based on the findings of this evaluation, OVE recommends the following:

1. **Strengthen the institutional focus on the concept of additionality and its analysis at a strategic level, beyond individual operations. This entails the following actions:**

    i. **Develop an additionality framework.** With a view to developing a common understanding among all stakeholders within the institution (including the Board of Executive Directors) regarding the concept of additionality, its analysis, and how it is operationalized, OVE recommends that IDB Invest develop an additionality framework that includes: (1) a clear definition of how the concept of additionality is understood at IDB Invest; (2) a taxonomy of the different types of additionality (both financial and nonfinancial); (3) the type of justification and evidence needed to demonstrate additionality; and (4) acceptable evidence and the ways Management will prove that an operation needs IDB Invest support and that the institution would not be crowding out the market. The Board of Executive Directors should be involved in the development of this framework.

    ii. **Implement systematic analysis of additionality at the portfolio level.** As is the case at other MDBs, at IDB Invest there is practically no analysis or reporting on additionality at the aggregate level, with these tasks only being performed at the operation level. Given this situation, the body of data on the different types and sources of additionality that has been built through such tools as the DELTA and the XSRs presents an opportunity for a systematic analysis of how additionality and its sources have performed and evolved, with the aim of informing strategic decision-making (e.g., at the country, sector, instrument, and client levels).

    iii. **Systematically incorporate the concept of additionality and its analysis into the development of country strategies** in order to identify more effectively the areas to be pursued in the country (e.g., sectors, markets, instruments) based on the comparative advantages of IDB Invest, on its own and/or in partnership with other MDBs or bilateral institutions, and its client commitment strategy.

2. **Redefine the strategic selectivity approach for selecting operations and clients.** The existing strategic selectivity tool is not a useful guide for origination efforts at the operation and client levels. An integrated selectivity approach should take into account:

(1) the analysis of the most urgent development gaps at the country and sector levels; (2) client demand and perspectives; and (3) IDB Invest's capacity and comparative advantages, including its additionality and resources. Therefore, when reformulating the selectivity approach, simply fine-tuning the existing tool or developing a new one will not solve the issue. Rather, this reformulation will require the participation and coordination of all of the areas involved in the operation and client selection process, including the strategy, business, and risk divisions. This reworking of the selectivity approach should also address coordination of the various strategies and tools at the institution's disposal, including diagnostic assessments of development gaps, the client strategy, and the business intelligence tool.

3. **Enhance capacity for impact management, primarily at the operation supervision stage and at the portfolio level.** This entails the following actions:

   i. **Place greater emphasis on operation supervision.** (a) Systematically identify issues that hinder achievement of the development objectives and expected additionality during operation implementation; and (b) ensure that corrective actions are identified, implemented, and evaluated to increase the likelihood of project success.

   ii. **Enhance impact management at the portfolio level.** (a) Expand the use of Portfolio 2.0, adding analyses at the segment and sub-portfolio levels and other variables not currently taken into account (e.g., specific outcomes, additionality); and (b) based on the operation-level data compiled during approval and supervision, improve the aggregate-level analysis of the various dimensions of the DELTA that support more active management at the portfolio level.

   iii. **Continue strengthening the DELTA.** With the understanding that impact management is an evolving area, OVE recommends that IDB Invest: (a) continuously adjust the DELTA tool to bring it in tune with new priorities and business areas and continue its methodological development, especially with respect to clarifying definitions and the respective rating criteria; (b) forge ahead with the standardization and streamlining of indicators; and (c) enhance internal and external transparency.

   iv. **Engage in more active management of the knowledge the institution generates and expand its use.** (a) Systematically identify lessons learned from operations and encourage use of those lessons to inform the design of new operations and operations in implementation; and (b) develop a strategy at the institutional level for managing the knowledge that is scattered across the institution, in coordination with the IDB Group.

4. **Develop a strategy and governance for advisory services.** At a time when the advisory services portfolio is growing and its scope may be expanded, it will be important to develop a strategy and governance for advisory services, which should include a clear definition of the different types of services and their objectives, selection and prioritization criteria, sources of financial resources (internal and external), client concessionality mechanisms, and a monitoring and evaluation system.

5. **Systematically identify potential areas for public-private collaboration and strengthen coordination mechanisms at the IDB Group level.** This entails the following actions:

   i. **Create or improve mechanisms at the IDB Group level for the systematic identification of potential areas of collaboration,** including the clarification of the various windows' roles and the timing and scope of their interventions.

   ii. **Strengthen the Country Representative role to better empower them for their private-sector duties.** (a) Establish clear criteria and competitive processes for the selection of Country Representatives, including IDB Invest as a participant in the process; (b) establish clear criteria for evaluating Country Representatives' performance in their private-sector-related duties, systematically including IDB Invest as a participant in that evaluation process; and (c) provide more in-depth training to country representatives so they can effectively perform their private-sector duties.

   iii. **Strengthen IDB Invest's involvement in the development and implementation of country strategies and SFDs.** (a) Establish mechanisms to involve IDB Invest more systematically in the IDB Group's ongoing dialogue with the governments, especially during country strategy implementation, so as to inform the operation origination and selection process; and (b) reframe IDB Invest's role and involvement in the development of SFDs.

   iv. **Realign the existing incentive structure to bring it in tune with the objective of promoting more systematic collaboration among IDB Group personnel.**

6. **Continue strengthening capital management and financial analysis and planning tools.** This entails the following actions:

i. **When designing future capitalization processes, take into account the institution's capacity for deploying capital, while including some headroom for countercyclical responses.** To manage the financial opportunity cost of untapped capital, OVE recommends that IDB Invest take into account its capacity for deploying additional capital when it designs future capitalization processes. However, it should also consider including some buffers so it can respond to emergencies or extraordinary situations, like those that occurred during the pandemic.

ii. **Continue strengthening financial analysis and planning tools.** In particular, (a) expand the use of RAROC and its scope, to include use of the tool beyond the approval stage to detect potential deviation from the return as estimated at approval and the return yielded; and (b) increase the granularity of the administrative budget distributed to the Board of Executive Directors, systematically linking budget line items to their expected outputs, in the interest of working toward a budgeting framework similar to the IDB's results-based budget.

01

Introduction

1.1 At the 2015 annual meeting in Busan, the Boards of Governors of the Inter American Development Bank (IDB) and the Inter-American Investment Corporation (IIC) decided to consolidate the IDB Group's private-sector operations into the IIC (document CII/AG 2/15). This process of consolidation and capitalization, known as the private sector merge-out, took effect on 1 January 2016. In November 2017, the IIC was rebranded as IDB Invest.

A. Renewed vision

1.2 The Busan Resolution set forth a "Renewed Vision" for promoting the development of the region through the private sector. The Renewed Vision provides a long-term framework (2016-2025) for IDB Invest and focuses on strengthening the effectiveness and additionality of operations, as well as maximizing the efficient use of resources and synergies between the IDB Group's public and private-sector activities. The merge-out was selected as the way to implement this Renewed Vision. The Renewed Vision sets out IDB Invest's dual mandate of maximizing development impact within a framework of long-term financial sustainability.[1] The Renewed Vision is based on three strategic pillars (strategic selectivity, systemic approach, and development effectiveness) and identifies a set of priority business areas and crosscutting areas,[2] as well as impact channels for enhancing the institution's development impact and strengthening its financial footing.[3] Other core features of the Renewed Vision relate to strengthening a client-focused private-sector culture and the importance of a more strategically targeted entity with an emphasis on accountability.

1.3 The consolidation of the IDB Group's private-sector activities in the IIC was to be accompanied by significant financial resources for the IIC over a 10 year period (2016-2025). The Governors approved a US$2.03 billion capital increase for the IIC in 2015, consisting of US$1.305 billion in new capital from shareholder countries over the

1 The dual mandate for the IIC would require actively selecting projects based on their potential to generate measurable development impacts alongside a financial return that would ensure the new institution's financial sustainability (document CII/CA-165).

2 The five priority business areas are access to finance, infrastructure, innovation, basic goods and services, and green growth. The three crosscutting areas are environmental and social sustainability, gender and diversity, and an enabling environment for private sector development. Within the framework of the Busan Resolution, the Governors also requested that a strategy be developed to strengthen the commitment to Group C and D countries in order to identify mechanisms and assistance to facilitate these countries' capacity to use IIC resources and achieve a 40% target for financing operations. In accordance with the Busan Resolution, this should ensure, at the end of the capitalization, an increase in total financing for the Caribbean countries and other countries that have benefited to a lesser degree from non-sovereign guaranteed operations.

3 Five impact channels were identified: (i) stable and predictable lending volumes; (ii) mobilization of third-party resources; (iii) more effective use of knowledge products, services, and activities; (iv) capital generation through retained earnings; and (v) generating and maintaining operational synergies.

2016-2022 period and US$725 million in transfers from the IDB to the IIC on behalf of member countries over the 2018-2025 period. This capitalization arrangement was supported by an agreement authorizing the IIC to record its operations on the IDB's balance sheet ("cross-booking") for a seven-year period (2016-2022). As part of the merge-out process, the Governors set a number of conditions, including the requirements that the overall volume of sovereign-guaranteed (SG) and non-sovereign-guaranteed (NSG) operations be maintained in accordance with the Ninth Capital Increase throughout the 2016-2025 period; that the IDB's "AAA" credit rating be protected; that parameters be established for the end of cross-booking (document CII/AG-2/14); and that the IIC maintain a minimum "AA" credit rating.[4] The capitalization proposal included a number of assumptions and projections related to the IIC's operational and financial performance—e.g., in terms of volume of approvals, resource mobilization, revenue generation, and administrative expenditure.

1.4 In 2017, the Office of Evaluation and Oversight (OVE) completed a midterm review of the implementation of the private sector merge-out (document CII/RE-27-5). The review focused on actions undertaken from March 2015 (when the Governors authorized the merge-out) until June 2017, with the aim of identifying lessons that could be helpful in completing the merge-out. The main achievements identified by OVE included completion of a difficult transition process, the work to build a human resource base, and the development of an approach to begin strengthening development effectiveness and additionality. The main challenges included the need for greater strategic selectivity, stronger mechanisms for public-private coordination (including continuing to strengthen the role of the Country Representatives), and better tools for financial planning and monitoring. Based on its findings, OVE made four recommendations that were approved by the IDB and IDB Invest Boards of Executive Directors.

B. Overview of the evolution of IDB Invest

1.5 The portfolio of development-related assets (DRA) managed by IDB Invest has grown since the merge-out process took effect.[5] The DRA portfolio managed by IDB Invest (taking only outstanding balances into account) stood at US$10.855 billion

4 The transfers from the IDB to the IIC are subject to the Governors' annual approval and are contingent upon, *inter alia*, the IDB's compliance with its capital adequacy policies, maintenance of SG financing levels consistent with the Ninth Capital Increase, formation of the Bank's capital buffers, and compliance with other applicable IDB financial policies.

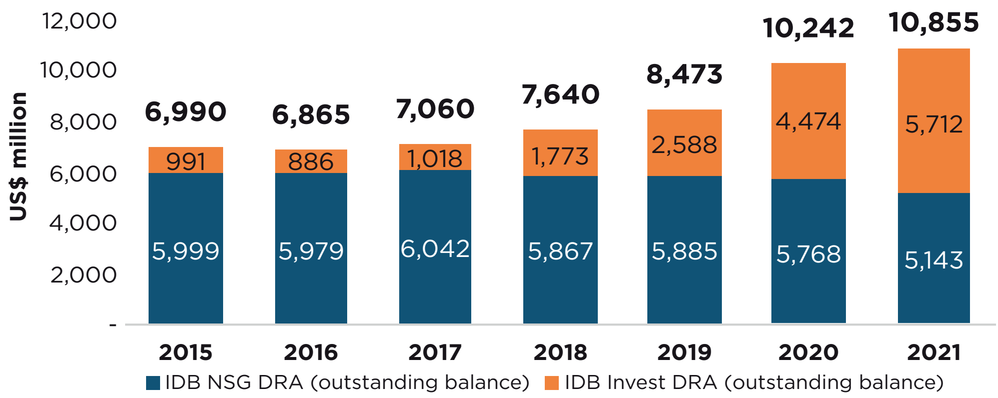
5 The IDB Invest DRA portfolio includes loans, equity investments, debt instruments, and guarantees to promote the economic development of the regional member countries of IDB Invest through the establishment, growth, and modernization of private enterprises.

at year-end 2021, a significant increase compared to the IDB Group's combined NSG portfolio at year-end 2015 (US$6.99 billion) before the merge-out (Figure 1.1).

Figure 1.1

DRA portfolio for NSG operations, IDB Invest and IDB (in millions of U.S. dollars)

Source: OVE, based on data reported by IDB Invest in its quarterly reports and systems.



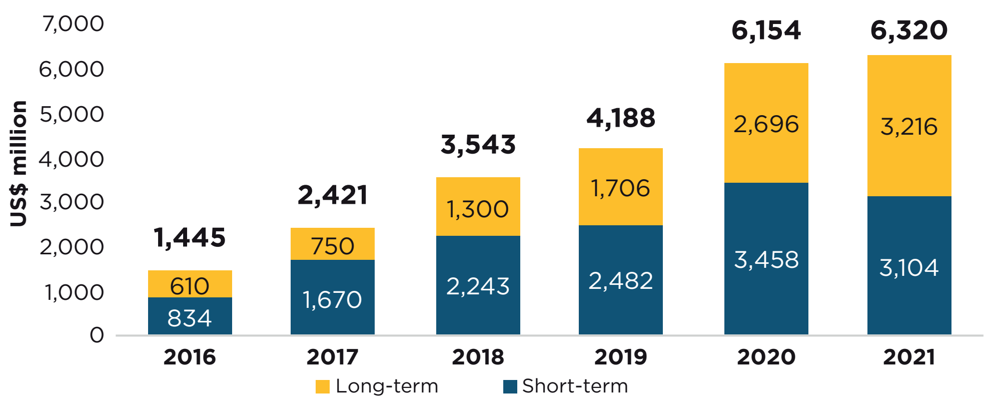
Note: Since 2020, in accordance with the current expected credit losses (CECL) methodology, IDB Invest has reported committed balances as part of the DRA portfolio. As of December 2021, committed balances totaled US$2.517 billion, 80% of which was booked at IDB Invest.

1.6 Portfolio growth has been driven by a significant increase in origination capacity at IDB Invest. After a launch of operations in 2016 that saw lower business volumes than projected in Busan, commitments have risen significantly, mainly since 2020 as part of the operational strategy in response to the COVID 19 pandemic crisis. From 2016 to 2021, commitments averaged US$4.012 billion annual (Figure 1.2), which exceeds the combined commitments under the former private-sector windows (IIC, Structured and Corporate Financing Department (SCF), and Opportunities for the Majority Initiative (OMJ)) prior to the merge-out (US$2.258 billion on average over the 2012-2015 period). Long-term financing accounted for 57% of committed amounts (US$13.791 billion), and this category of financing also increased over this period, particularly in 2020.[6]

Figure 1.2

Commitments, January 2016 to December 2021 (in millions of U.S. dollars)

Source: OVE, based on data from IDB Invest.



6 As a result of the merge-out, IDB Invest also began to manage a portfolio of 506 active operations in early 2016 that had been approved before the merge-out by the "old" IIC and the IDB's private-sector windows (SCF and OMJ).

1.7 The COVID 19 pandemic put IDB Invest's response capacity to the test. The region's challenges, which were exacerbated by the fallout of the economic and health crisis caused by the COVID 19 pandemic, prompted IDB Invest to revise and adapt its immediate priorities (Box 1.1). A core element of IDB Invest's operational response was an increase in short-term financing (Trade Finance Facilitation Program (TFFP) and value chains), which had implications for the mix of short- and long-term commitments. Short-term commitments jumped from 42% of total commitments in 2016 to 51% in 2021 (Figure 1.2). Though the volume of short-term products has increased significantly since 2020, the revolving nature of these products due to their shorter tenors meant that their share of the total portfolio rose from 11.1% in 2016 to 14.5% in 2021.

Box 1.1. Operational response to the COVID 19 pandemic crisis

The 2020-2022 Business Plan was revised in April 2020 to incorporate a strategy for the operational response to the COVID 19 pandemic crisis (document CII/GN-419). A top priority of the crisis response was to increase resources for the region by significantly expanding the 2020 program of operations (from US$4.5 billion, as initially provided for in the Business Plan, to as much as US$7 billion). The crisis response also included implementation of a series of temporary flexibility measures to strengthen IDB Invest's capacity to deliver a nimble, effective response, such as delegating power from the Board of Executive Directors to Management for approval of transactions under a crisis management facility (US$500 million); increasing exposure limits on TFFP operations; raising debt and capital ceilings under the risk appetite policy; and modifying procedures for operations for between US$50 million and US$100 million.

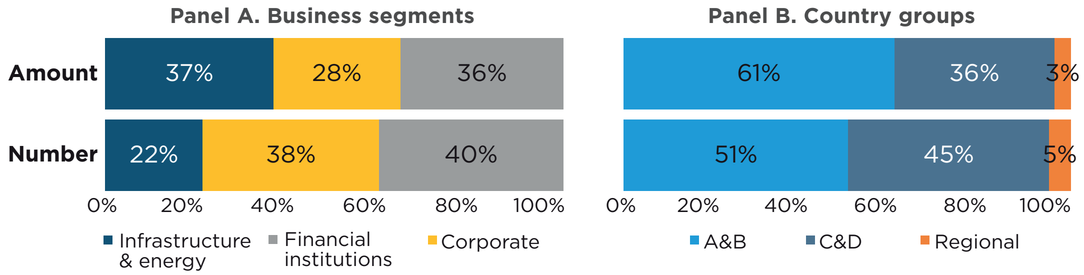
Source: OVE.

1.8 The committed amounts (excluding short-term financing) have mostly targeted operations for infrastructure and financial institutions in Group A and B countries. While committed operations were concentrated primarily in the financial institutions and corporate business segments (40% and 38%, respectively) from January 2016 to December 2021 (Figure 1.3A), infrastructure and energy accounted for 37% of all committed amounts due to the larger average project size in that segment, followed by financial institutions at 36%. In addition, most committed long-term operations (51%) and committed amounts (61%) were in Group A and B countries (Figure 1.3B). Five countries (Mexico, Chile, Brazil, Colombia, and Ecuador) accounted for a combined 47% of the number of committed operations and 58% of committed amounts between January 2016 and December 2021 (Annex II, Table II.1).

Figure 1.3

Distribution of long-term commitments, January 2016-December 2021

Source: OVE, based on data from IDB Invest.



1.9 Considerable challenges to expanding support in certain countries, such as small and island countries, persist despite IDB Invest's efforts. Pursuant to the Busan Resolution, IDB Invest needed to achieve an increase in total financing for the Caribbean countries and other countries that have benefited to a lesser degree from NSG operations by the end of the capitalization period in 2025. Under its Small and Island Countries Action Plans (Box 1.2), IDB Invest set corporate targets for increasing the amount of resources directed toward these countries. Despite the increase in the number of operations and amounts committed in recent years (Annex II, Tables II.2 and II.3), meeting this target has proven difficult.

Box 1.2. Small and Island Countries Action Plan

In 2017, IDB Invest approved a three-year Small and Island Countries Action Plan (document CII/GN-354), which aimed to increase the number of operations in these countries. The action plan set the target of achieving 10% of total commitments in these countries by 2020. In 2020 IDB Invest approved an updated action plan (document CII/GN 354-2), which established new mechanisms, including a more active use of advisory services in these countries, development of a specific risk profile to support small transactions, creation of a multidisciplinary team to support operational management in small and island countries, and a set of communication and knowledge management initiatives. IDB Invest also recommitted to the target of 10% of commitments in small and island countries and stipulated that both short- and long-term commitments should hit that target.

As this was a matter of priority and given the challenges to meeting these commitment targets, in late 2020 IDB Invest also approved a series of temporary changes at the process level to streamline transactions in small and island countries. Those changes included the creation of a task force charged with identifying and fixing transaction-related issues as well as the expansion of internal delegation of authority for making decisions related to these transactions.

The short-term target (14%) was met in 2020, and both the short- and long-term targets were met in 2022 (10% and 11%, respectively).

Source: OVE.

C. Evaluation objectives and scope

1.10 This evaluation seeks to independently assess and report on the effectiveness of the implementation to date of the Renewed Vision, aimed at promoting development in the region through the private sector. Since the Renewed Vision for 2016-2025 is still being implemented, one key focus of this evaluation is to identify lessons learned to provide input for future discussions at the corporate level. The evaluation covers the period from January 2016 (when the merge-out took effect) to December 2021. The evaluation also uses as a reference the findings from OVE's 2017 midterm review of implementation of the merge-out (document CII/RE-27-3), to further analyze financial and operational areas that had not yet matured at that time, such as the strategic selectivity and financial planning frameworks, the portfolio approach, processes to support operations management, and public-private coordination mechanisms. Considerations related to human resources—a major focus of OVE's 2017 midterm review amid the institution's transition at that time—were given limited attention in this evaluation.[7]

1.11 The evaluation was also guided by a reference framework that linked the objectives of the Renewed Vision to the main activities and initiatives undertaken thus far to help achieve those objectives (see Annex I, Figure 4.1). In keeping with the approach paper (document CII/RE-83), OVE referred in its analysis to the IDB Invest mandate of maximizing development impact within a framework of long-term financial sustainability, as set forth in the Renewed Vision and described in various IDB Invest documents. OVE also referred to the evaluation framework developed for its 2017 midterm review of implementation of the private sector merge-out, particularly as it pertains to the end objectives set out in the Renewed Vision, which establishes the long-term strategic reference framework for IDB Invest. Since the merge-out process took effect, IDB Invest has undertaken a series of activities and initiatives in various areas in pursuit of those objectives, including plans, tools, and processes. While those identified in OVE's 2017 evaluation framework were taken into account for the midterm outcomes, they have been adjusted to reflect new institutional priorities consistent with IDB Invest's business plans in recent years.

7 This evaluation did not look at areas such as procurement processes and the current performance, incentives, and compensation framework because those matters require a type of analysis that is not compatible with the scope and timeframe of this evaluation. Other related areas, such as the organizational culture initiative, are at an early stage of development (see Chapter III).

D. Evaluation questions

1.12 The evaluation questions take into consideration the reference framework developed by OVE for this evaluation (see Annex I, Figure 4.1). The general question that the evaluation aims to answer is the following: To what extent is IDB Invest on its way to achieving the end objectives of the Renewed Vision (i.e., strengthening effectiveness and additionality, maximizing public-private synergies, maximizing the efficient use of resources, and ensuring long-term financial sustainability)? The evaluation also aims to answer the following specific questions, based on key midterm outcomes and using an outlook oriented to long-term objectives:[8] (i) To what extent has IDB Invest strengthened its approach for strategic selectivity and development effectiveness? (ii) To what extent has IDB Invest expanded its capacity to mobilize resources? (iii) To what extent is IDB Invest helping to strengthen public-private collaboration within the IDB Group? (iv) To what extent has IDB Invest strengthened the efficient use of its resources? (v) To what extent has IDB Invest strengthened its financial capacity with the aim of ensuring its long-term sustainability?

1.13 OVE used a combination of complementary methods to answer these questions. Those methods included a review of strategic and corporate documents, financial and portfolio analyses, interviews and surveys, and documentary analyses of operations. The main components of the evaluation are discussed in greater detail below (Box 1.3).

Box 1.3. Evaluation components

Analysis of IDB Invest documents. OVE collected and analyzed a series of strategic and corporate documents related to the creation of IDB Invest as well as business plans, action plans, and policies that have guided IDB Invest's activities in recent years. OVE also analyzed documents related to various initiatives, tools, and approaches developed by IDB Invest in recent years (in such areas as finance and development effectiveness). OVE also referred to findings from its midterm review of implementation of the merge-out (2017) and other recent evaluations on specific areas related to IDB Invest's work.

Analysis of the operations portfolio. OVE collected and consolidated general information on the portfolio of operations managed by IDB Invest since its inception, with the aim of analyzing overall trends in the operations portfolio (e.g., approvals,

8 Two midterm outcomes were not included in the scope of this evaluation. As noted above, while this evaluation analyzed overall trends and progress in IDB Invest staffing since the merge-out, it did not look at matters related to human resource management and private sector culture. The scope of this evaluation also did not include the midterm outcome related to the efficiency of the COVID-19 response, as it is still too early to judge its effectiveness. However, this may be analyzed in future evaluations. The scope of future evaluations as it pertains to resource mobilization also may be expanded.

commitments, disbursements, resource mobilization) and general characteristics of financed operations (e.g., countries, financing instruments, Development Effectiveness, Learning, Tracking, and Assessment (DELTA) scores).

Desk review of operations approved by IDB Invest. OVE conducted a documentary analysis of a random sample of 157 operations (excluding TFFP operations)[a] approved by IDB Invest between January 2016 and December 2021 with the aim of exploring aspects related to operation design and implementation, including financial and nonfinancial additionality, evidence of public-private coordination, and achievement of development objectives. The sample included roughly one-third of the operations approved by IDB Invest over that period (excluding TFFP operations). The documentary analysis used standardized questions to ensure consistency in evaluation across operations. The analysis included a review of documentation and information generated in the course of operation origination, approval, supervision, and evaluation, including loan and financing proposals, loan contracts, DELTA scores at approval and during supervision, annual supervision reports, expanded supervision reports (XSRs), and OVE validations of XSRs. The documentary analysis of operations was complemented by interviews with clients involved in 72 committed operations.

Financial sustainability analysis. OVE analyzed progress toward core components of IDB Invest's capitalization arrangement (capital contributions from shareholder countries and annual transfers from the IDB). OVE also collected and analyzed data on the credit quality of the IDB Invest portfolio as well as financial performance, including an analysis of the cost-and-revenue structure and drivers of the institution's long-term financial sustainability. OVE also analyzed the portfolio included on IDB balance sheets through the cross-booking arrangement.

Analysis of IDB Invest's institutional arrangements, processes, and resources. OVE analyzed the main institutional arrangements introduced since the merge-out, including those aimed at promoting public-private coordination and collaboration and supporting the efficient delivery of operations (e.g., timeframes for processing transactions, metrics introduced in recent years to measure costs at the operation level). OVE also analyzed IDB Invest's budgeting and staffing in terms of performance.

Interviews and surveys. The analysis of documents, processes, data, and operations was complemented by more than 140 semistructured interviews with various stakeholders, including IDB Group personnel, Country Representatives, IDB Invest clients, and IDB Invest Executive Directors and Counselors. OVE also conducted two virtual surveys of IDB Invest investment officers and IDB and IDB Lab specialists.[b]

Source: OVE.

Notes: [a]In 2016 OVE completed an Evaluation of the IDB Group's Work through Financial Intermediaries (document RE 486 2), which included a background report on the TFFP and identified a series of findings and recommendations. In light of the foregoing, OVE focused on assessing the extent to which IDB Invest had responded to the main challenges identified in that evaluation. [b]Surveys were sent to 58 IDB Invest Investment Officers and 175 IDB and IDB Lab Project Team Leaders. The response rates were 71% and 51%, respectively.

1.14 This document is laid out in seven chapters and six annexes. The first two chapters focus on some of IDB Invest's efforts to strengthen effectiveness and additionality. In particular, Chapter II takes stock of the implementation of the Impact Management Framework and its tools, while Chapter III analyzes financial solutions, advisory services, and operational developments (staff decentralization and operation management processes) implemented by IDB Invest to bolster its value proposition and its client focus. Chapter IV discusses additionality and effectiveness results at the operation level. Chapter V explores developments related to public-private coordination, with a focus on the mechanisms instituted to promote synergies within the IDB Group. Chapter VI analyzes the institution's long-term financial sustainability. Lastly, Chapter VII presents the evaluation's conclusions and recommendations.

02

Strengthening Effectiveness and Additionality-Operationalization

2.1 This chapter analyzes the Impact Management Framework under which IDB Invest has sought to operationalize the pillars of the Renewed Vision (strategic selectivity, development effectiveness, and systemic impact) with a view to strengthening effectiveness and additionality. According to the Renewed Vision, strategic selectivity meant choosing interventions in areas where the institution could make the greatest contribution so as to maximize its impact; development effectiveness meant that the ex ante and ex post focus should be complemented by a rigorous approach to monitoring results; and systemic impact meant that the organization should ensure that its resources have an impact greater than that of its individual projects. With that in mind, IDB Invest rolled out an Impact Management Framework during the evaluation period, with the objectives of striking a balance between its operations' potential impact and financial sustainability; ensuring strategic alignment; designing efficient, effective, and evaluable operations; managing the portfolio for greater impact; ensuring accountability; and fostering continuous learning.

2.2 The rollout of the Impact Management Framework and associated tools was an important step forward during the evaluation period. To achieve the objectives set out in the framework, IDB Invest gradually implemented a series of management tools that sought to shape the different stages of the project cycle. Before the merge-out, the various private-sector windows had differing approaches to effectiveness, and there were few tools available at that time. This presented an opportunity to conceptualize a framework with a system approach from the start. The tools envisioned in the framework were developed, and the framework itself aligns with the principles for impact management developed by financial development institutions.[9] Beyond the need to continuously improve these tools, the extent to which they have been adopted and used varies, which has much to do with the emphasis IDB Invest placed on portfolio building and origination during the evaluation period.[10]

A. Strategic selectivity

Box 2.1. Strategic selectivity tools

- *Objective:* Operational analysis and prioritization of IDB Invest objectives and targets to guide the selection of projects and clients.
- *Stage:* Project/client identification.

9 Operating Principles for Impact Management (https://www.impactprinciples.org/).

10 For a more detailed discussion of the analysis performed, see: Background Note: Impact Management Framework (Annex III).

• *Components:* Strategic Selectivity Scorecard, country/sector development gap matrix, institutional priorities, adjusted rating system (DELTA adjusted for strategic selectivity).

Source: OVE.

2.3 Operationalization of the concept of strategic selectivity progressed slowly compared to implementation of other tools focused on the early stages of the project cycle. In 2019, IDB Invest introduced a "Strategic Selectivity Scorecard" to operationalize institutional priorities set out in various documents (e.g., the IDB Group Institutional Strategy, country strategies, action plans, and business plans). The scorecard aims to measure and demonstrate an operation's alignment with corporate priorities and business plan targets. To supplement the scorecard, IDB Invest also developed a methodology for measuring private-sector development gaps at the country and sector levels (taking into consideration the dimensions of access, quality, efficiency, affordability, and sustainability). With inputs from the priority alignment and development gap analyses, IDB Invest also developed a selectivity bonus for the impact rating (measured through the DELTA) to create incentives during the origination stage. The official roll-out of the DELTA score adjusted for strategic selectivity took place in 2019, with the adjusted rating appearing on the operation approval document.[11] The methodology is replicable and can be used to standardize and report trends in the portfolio's alignment with the development gaps identified for each country and to measure whether corporate targets have been met.

2.4 IDB Invest does not yet have an integrated selectivity approach that can help guide the selection of operations and clients. The existing selectivity tool is not a useful guide for selection of operations and clients because it does not effectively address key dimensions of the selection process, such as development gaps, client demand and perspectives, and IDB Invest's offerings, taking into account the institution's comparative advantages, priorities, and mandates. First of all, the development gap methodology and indicators yield an incomplete analysis of the specific drivers and circumstances behind the gaps identified, which hinders prioritization in practice. The methodology also does not draw upon other analyses and data developed by the IDB Group to prioritize its activities, such as the fruits of the ongoing dialogue with the governments and the development of the country strategies. Second, the tool does not factor in an analysis of clients that are instrumental to closing the gaps, nor does it set out categories or

11 Both scores (DELTA and DELTA adjusted for strategic selectivity) are reported at project approval.

principles to guide prioritization. Third, the tool does not factor in IDB Invest's comparative advantages and additionality, which are essential considerations to support an efficient use of resources when closing gaps. In addition, most of the personnel involved in origination who were interviewed and surveyed by OVE said the tool did not have much impact on decision-making and thus is not adding much value as a practical guide. In that sense, even though corporate targets at the portfolio level have created incentives for origination and resource allocation,[12] the selectivity tool did not create similar incentives at more disaggregate levels (e.g., at the country and sector levels).

B. Impact rating system for potential impact and operation supervision (DELTA)

Box 2.2. Impact rating system (DELTA)
•*Objective:* Ex ante evaluation of an operation's potential impact and support for supervision during implementation. • *Stage:* Origination-implementation. • *Components:* Economic analysis, and beneficiary, sustainability, additionality, and evaluability analysis. *Source:* OVE.

2.5 The system's most developed and institutionalized tool is the DELTA, which has implications for decision-making during approval. The DELTA measures an operation's potential impact on a scale from zero to ten and factors in several analyses in the areas of development outcomes[13] and (financial and nonfinancial) additionality. The analysis considers two other dimensions (operation evaluability and alignment with institutional priorities) that do not affect the project rating (Box 2.3). Though the DELTA has origins in systems that predated the merge-out (e.g., the Development Impact and Additionality Scoring System (DIAS) and the Development Effectiveness Matrix (DEM)), the tool has undergone repeated updates, including the fine-tuning of its categories and the development of instrument-specific methodologies (e.g., for TFFP and Investment Funds). The rating is

12 The portfolio's alignment with corporate objectives for Group C and D countries; micro, small, and medium-sized enterprises (MSMEs); and gender and diversity has outperformed the targets set for most years. Climate finance outperformed the target in 2017 but hovered around 25% over the 2019-2021 period (when the target was 30%). The targets for small and island countries have proven more difficult to meet (see Annex III, Figure A.2).

13 This includes: (a) several analyses of the operation's contribution to social and economic development (economic analysis and analysis of specific results for beneficiaries); and (b) sustainability of the outcomes (analyses of project/company financial performance and of environmental and social safeguards compliance).

calculated at operation origination and then updated on an annual basis during supervision. The tool has been institutionalized, and there is a team dedicated to DELTA analysis and quality control (the Development Effectiveness Division, DVF), which does not report to the business area.

Box 2.3. DELTA general structure

Strategic alignment: This section captures the project's alignment with corporate and country priorities, as well as its contribution to the sustainable development goals (SDGs). It informs the strategic selectivity tool. This section is divided into: IDB Group Strategic Development Objectives, IDB Invest Strategic Development Objectives, and Contribution to Country Priorities.

Project impact score: This section assigns a score (on a scale from zero to ten) based on two components: development outcomes and additionality.

Development outcomes (65%): This subsection identifies elements of the expected impact. It in turn is subdivided into an economic analysis, an analysis of beneficiaries, and a sustainability analysis.

Additionality (35%): This subsection addresses the key financial and nonfinancial contributions made by IDB Invest to carry out the investment. Transactions must meet a minimum financial additionality threshold to be considered, but there is no required minimum nonfinancial additionality score.

Evaluability Score: This section evaluates, on a scale from zero to ten, the quality of the design of the operation and the indicators for measuring its impact. It is broken down into project logic, results matrix quality, monitoring and evaluation, and financial and economic analysis quality.

Source: OVE, based on DELTA data.

2.6 DELTA scores are useful for evaluating and synthesizing the various dimensions of an operation's impact in support of origination and supervision processes, even though the direct interpretation of aggregate scores is a complex task. An operation's DELTA score is a weighted average of ratings assigned to several dimensions of analysis, which simplifies project-specific contexts and conditions under certain criteria. This means that a given score can be reached in a variety of ways,[14] so comparing projects based on the score alone is no easy task. With that in mind, the score is useful for: (a) standardizing and managing screening processes during origination as the portfolio grows; (b) developing a common language and incentives for discussing and evaluating an operation's impact potential; (c) monitoring operations during implementation; and (d) developing a systematic repository of data on the particulars of each operation. However, the numeric score is abstract and is no substitute for an authoritative, project-specific narrative that discusses the project's expected development outcomes and

14 By way of example, an operation with a development outcome score of 10 and an additionality score of 6 would earn the same DELTA score (8.6) as an operation with a development outcome score of 7.8 and an additionality score of 10.

additionality during the approval process. Furthermore, if the focus is solely on the aggregate DELTA score, data generated during the analysis of its various dimensions (e.g., at the development outcome and additionality levels) may be overlooked. In that regard, several Executive Directors interviewed by OVE spoke of the difficulty of interpreting the aggregate DELTA score at the operation level, given its various dimensions and components. It is worth noting that impact measurement and management is an evolving area, so while there are some general principles, there are no universal models or standards. Even among multilateral development banks (MDBs), for example, there are several different approaches to addressing development outcomes and additionality (Box 2.4).

Box 2.4. Impact assessment systems at other MDBs

Like IDB Invest, other MDBs have developed ex ante impact assessment systems in recent years. Though there are some commonalities across these systems in terms of core definitions and principles, there are different approaches at play. One notable difference pertains to how to address additionality alongside development outcomes. Some MDBs, such as IDB Invest (through the DELTA) and the European Investment Bank (EIB), consolidate the analysis of additionality and the analysis of development outcomes under a single tool. Meanwhile, other MDBs, such as the European Bank for Reconstruction and Development (EBRD), the International Finance Corporation (IFC), and the Asian Development Bank (ADB),[a] perform two separate analyses for these concepts and do not consolidate them under a single score. Furthermore, not all MDBs assign an additionality score. In some cases (e.g., the EBRD), minimum additionality thresholds are set for each project.

There is no consensus among the MDBs as to which is the best approach. Consolidating the additionality analysis and the development outcomes analysis under a single score helps put forward a coherent narrative about the project objectives, the MDB's contribution, and the expected outcomes but also entails certain risks. For example, in some cases the strength of one dimension offsets another dimension that fails to meet an acceptable threshold. IDB Invest has set a required minimum DELTA score for the specific case of financial additionality.

Source: OVE.

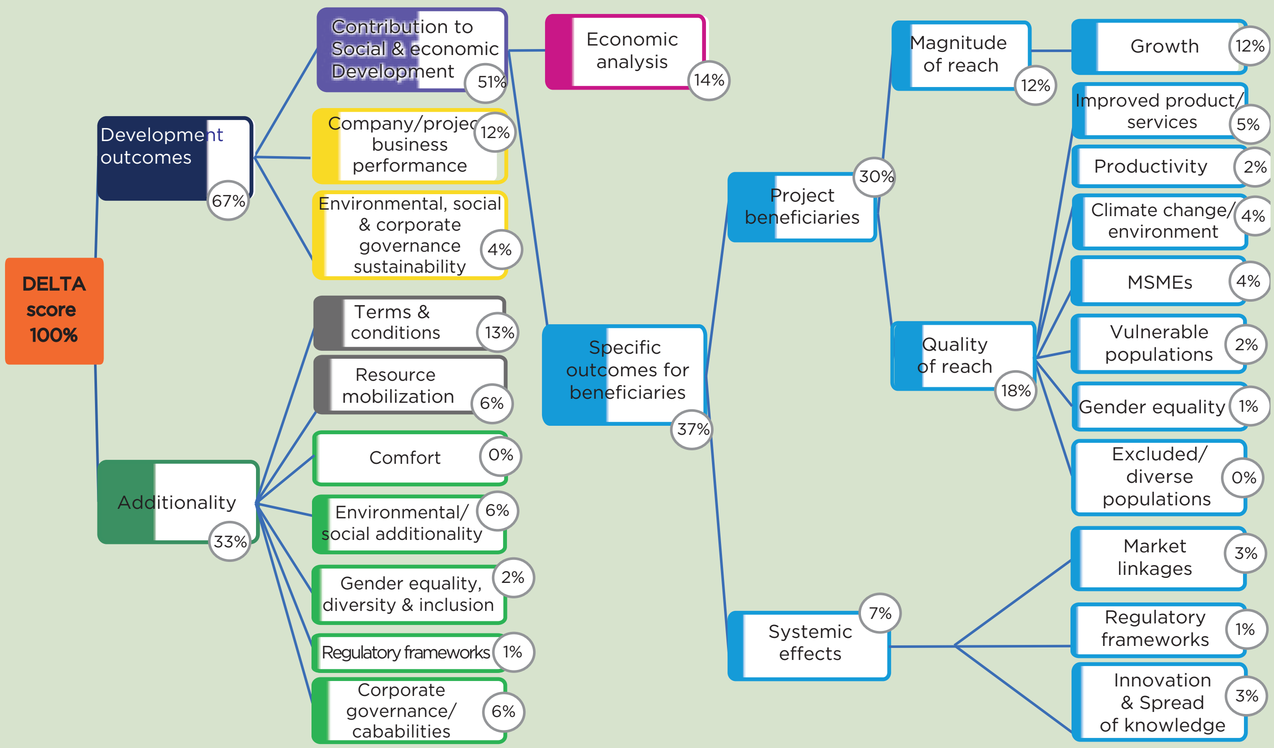
Nota: [a]The ADB is switching to a system that consolidates the two concepts.

2.7 Breaking down the average DELTA score into its component parts yields additional information on operation types and on the portfolio. OVE broke down the average DELTA score (8.3) for the portfolio of operations approved in the 2016-2021 period into its subcomponents, looking at individual ratings and trends (Box 3.3). This analysis also factored in various characteristics of the operations, such as region and instrument. Looking at location (e.g., regional, small and island countries), the differences between the final aggregate DELTA score of each cutoff group was minimal (and similar to the overall average of 8.3). There were slight differences between the average development outcome score and the average additionality score from region to region, but those differences were not statistically significant. The average expected development scores for operations in the "Group C and D countries" subgroup were slightly lower than operations in the "Group A and B countries" subgroup (8.4 versus 8.6). In contrast, projects in Group C and D countries had higher expected additionality scores than those in Group A and B countries (8.3 versus 7.8), a difference that is wider but still not statistically significant. These analyses demonstrate that the DELTA has the potential to be used to perform systematic analyses to inform decision-making using data that already exists.

Box 2.5. DELTA scores at approval

OVE broke down the average DELTA score for all of the operations approved between 2016 and 2021 (average score of 8.3), looking at the frequency and score (rating) of DELTA subcomponents in this portfolio (see figure). In terms of the **development outcomes** (67% of the total), the score assigned to expected **specific outcomes**[a] accounted for 37% of the portfolio's average DELTA score. The subcomponents that made the greatest contribution to the average DELTA score were the expected specific outcomes in the areas of "products and services," "MSMEs," and "climate change/environment." "Diverse/excluded populations," "gender equality," "productivity," and "regulatory frameworks" were the subcomponents with lower contributions to the average DELTA score. As for **additionality (33% of the total)**, the ratio of financial additionality to nonfinancial additionality reported by the DELTA was approximately 3:2 for the portfolio average. The "financial terms and conditions" subcomponent accounted for nearly two-thirds of the total **financial additionality** score. The **nonfinancial additionality** score was driven mainly by two variables: "environmental/social standards" (6% of the DELTA score and 17.7% of total additionality) and "governance/capabilities" (6% of the DELTA score and 16.8% of total additionality). The "gender and diversity" subsection accounted for 5.5% of the expected additionality score, while the contributions of the "regulatory frameworks" and "comfort" (political/regulatory risk mitigation) subsections were minimal.

Contribution to the average DELTA score for the portfolio of operations approved from 2016 to 2021, by subcomponent



Source: OVE, based on DELTA data.

Note: [a] This includes the scores for "quality of reach" of the expected outcomes (18%), "magnitude of reach" (18%), and "systemic effects" (7%). Methodology note: This analysis kept the individual DELTA scores per category but did not factor in the existing caps on the DELTA scores for each section for each operation prior to taking the portfolio averages. That way, the sum of two categories that received the same score in different operations would be equal to the overall average.

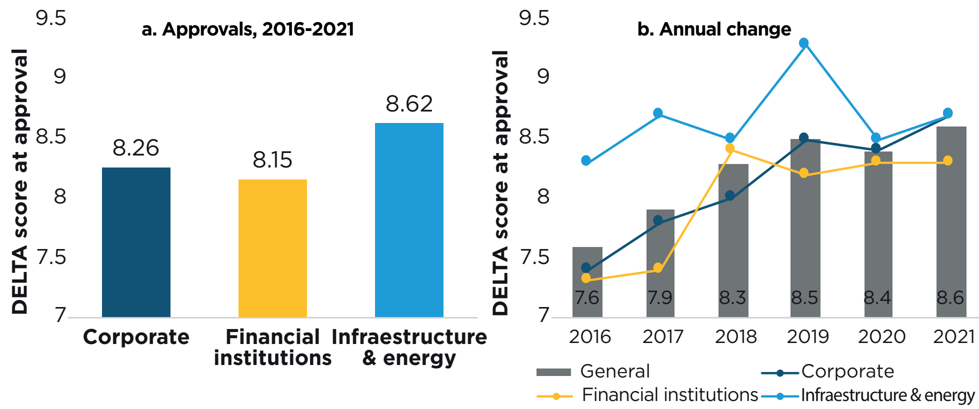
2.8 On average, infrastructure and energy operations had significantly higher DELTA scores at approval than operations in other segments. These higher scores were driven by significantly higher relative scores for specific outcomes in the "quality of reach" and "systemic effects" subsections (especially in "climate change" and "regulatory frameworks"). They can also be attributed to higher relative scores in the "financial additionality" (potential resource mobilization) and "nonfinancial additionality" (support for regulatory frameworks and comfort) sections. Though the average score for projects in the financial institutions segment was lower, their relative scores in the "SME" and "gender" subsections of the specific development outcomes section tended to be higher, as were their scores on the "terms and conditions" subsection of the "financial additionality" section. Lastly, projects in the corporate segment typically had higher relative scores in the "productivity and "market linkages" subsections of the development outcomes section and "environmental/social standards" subsections of the additionality score.

2.9 The average annual DELTA score at approval increased during the evaluation period, in line with the corporate target set. The increase in the average ex ante DELTA score was mainly driven by better scores for operations in the corporate and financial institutions segments (Figure 2.1), since infrastructure projects have always had higher DELTA scores historically. The increase can be attributed to higher scores in the development outcomes and nonfinancial additionality sections.

Figure 2.1

DELTA scores at approval, by business segment

Source: OVE, based on data from IDB Invest.



2.10 The DELTA has also begun to be used increasingly during the supervision stage, which provides an opportunity to develop targeted corrective actions. Even when the DELTA was being designed, the expectation was that the tool would also support the operation supervision process. The "DELTA in supervision" score, introduced in 2018, reassesses the ex ante impact score based on the operation's performance and reexamines the assumptions and circumstances that have changed at the time of supervision. IDB Invest also instituted an alert system in 2019.[15] During supervision, the average DELTA score for the portfolio approved from 2016 to 2021 edged down, with declines in both the development outcomes and additionality sections, especially for operations in the financial institutions and corporate segments (Box 2.6). OVE found a positive correlation between the "DELTA in supervision" score and the XSR project rating, which demonstrates the potential for using the "DELTA in supervision" score to target corrective actions, thereby increasing the likelihood of an operation's success. [16] In response to the decline in nonfinancial additionality during supervision, IDB Invest implemented

15 During supervision, projects are classified as "satisfactory," "alert," "problem," or "insufficient information" based on the deviation from the ex ante DELTA score. This analysis has two stages: a formal reassessment of the DELTA components followed by a holistic assessment that factors in contextual considerations.

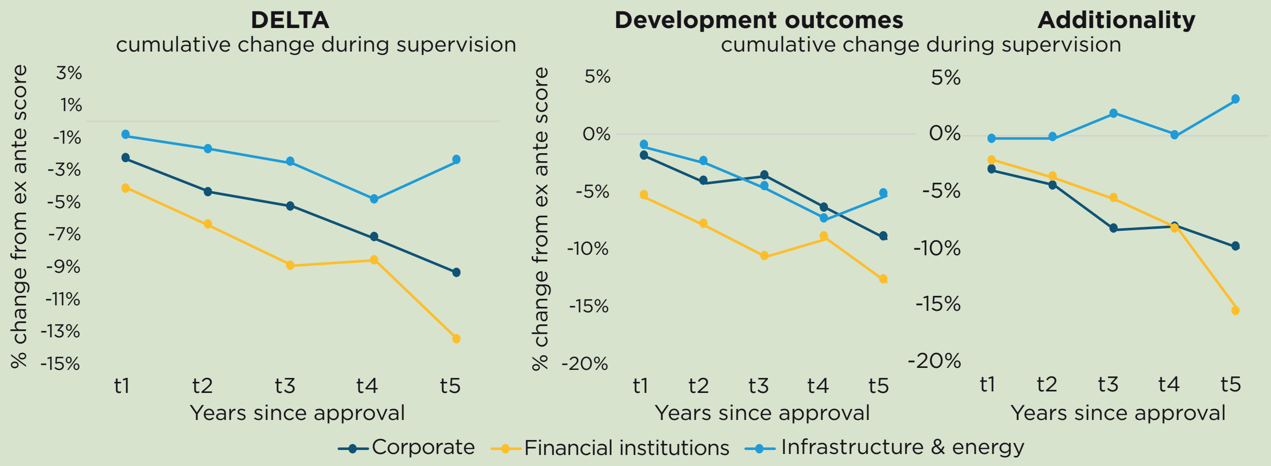
16 In its analysis of the 62 operations that had an XSR and at least one "DELTA in supervision" score, OVE compared the most recent DELTA score with the XSR rating. All told, 78.6% of operations that were classified as "problem projects" by the DELTA system (11 operations) were rated as unsuccessful operations by the XSR (including both "partly unsuccessful" and "highly unsuccessful"). By the same token, 75% of operations that were classified as "satisfactory" on their most recent "DELTA in supervision" score (27 operations) had XSRs with ratings of "successful" or "partly successful." Of the 12 operations classified as "alert," six were rated as "successful" or "partly successful" on their XSRs.

certain changes to improve performance during implementation of advisory services, such as asking clients to sign commitment agreements and relocating the Advisory Services team (ADV), which used to be part of the Investment Operations Department (INO), to the Strategy and Development Department (DSP). In recent years, IDB Invest has also started to more systematically identify corrective actions at the individual project level during supervision. Since these measures were recently implemented, it is still too early to determine how effective these changes have been.

BOX 2.6. DELTA scores in supervision

In terms of development outcomes, the decline in DELTA scores during supervision was driven largely by the magnitude of the benefits being much more limited than expected ex ante (in the case of operations in both the financial institutions and corporate segments) and by the difficulty of achieving the expected outcomes in the "SME" subsection (in the case of financial institutions) and "market linkages" and "innovation" subsections (in corporate operations). These declines during supervision are consistent with the greater risk of not achieving the development outcomes due to changes in business/project priorities or changing market conditions (risks that have less impact on the infrastructure portfolio), an issue that predates the pandemic (Development Effectiveness Overview, 2019). This also may stem from the use of assumptions that are either shaky or overly optimistic in these types of operations.

As for additionality, nonfinancial additionality scores also fell off during supervision, especially for projects in the financial institution and corporate segments. Notable declines were reported in the "capabilities and governance" and "social and environmental additionality" subsections. In general, projects that had low approval DELTA scores performed worse in additionality. Looking at projects that have XSRs, 75% of the drop in the nonfinancial additionality score could be traced to technical assistance projects that were not implemented (these projects have the most weight on the DELTA's nonfinancial additionality score). This could be an indication that clients are losing interest in technical assistance projects after project approval or otherwise could be pointing to issues arising during implementation of those projects (e.g., client financial trouble). Worsening macroeconomic conditions and the impact of COVID 19 also played a role in these declines.



Source: OVE, based on DELTA data.

Note: The analysis contrasted a project's "DELTA in supervision" scores at year "t" since approval with the same project's DELTA score at approval (t0).

2.11 The DELTA tool has the potential to offer more value, both for managing the organization's impact and for clients and investors. OVE identified areas in which IDB Invest can continue to improve the DELTA. First of all, the definitions and rating criteria could be revised, for example, by developing and sharing the assumptions used for the economic analysis and the criteria for how to approach additionality in new business areas. Second, IDB Invest could incorporate into the DELTA assumptions regarding the likelihood that the ex ante expected impacts will be achieved based on the cumulative track record of project and portfolio performance. Third, several aspects of the DELTA, including indicators and processes, could be standardized and streamlined. Fourth, IDB Invest should work toward enhancing transparency by supporting teams with formal resources, such as trainings and distribution of DELTA-related manuals, methodologies, and outlines.[17] Lastly, there is the potential to increase the DELTA's value beyond internal operating procedures. Interviews with clients revealed that their familiarity with the DELTA is limited. The data compiled is not processed in a way that adds tangible value and then returned to the clients, which leads to the perception that providing information beyond financial data is an additional cost of working with IDB Invest. This also comes up in lessons learned from operations (e.g., consider mechanisms for communicating and disseminating development contributions that may align with clients' goals for improving their corporate images) and practices that could be used to align development outcomes with clients' and investors' goals (e.g., blended finance and thematic bonds).[18]

C. Portfolio 2.0

Box 2.7. Portfolio 2.0

- *Objective:* Striking a balance between the financial return (as measured by the financial contribution rating, FCR) and development impact (as measured by the DELTA)
- *Stage:* Origination
- *Components:* DELTA score, RAROC, FCR, graphic representation of portfolio operations

Source: OVE.

2.12 Portfolio 2.0 has evolved out of lessons learned before the merge-out. Building on the "old" IIC's portfolio approach, methodological adjustments have been made to Portfolio 2.0 through both the DELTA and the FCR (a standardized measure of an operation's financial return that takes into account the capital used, RAROC,

17 An important step forward in this area was the recent launch (2022) of a course on the Impact Management Framework and associated tools, which has been made available to IDB Group staff and Executive Directors.

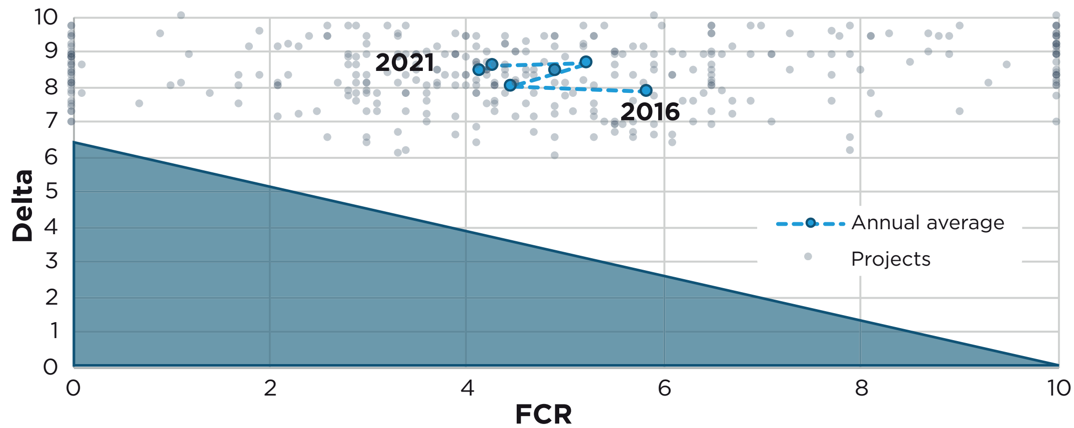
18 In these cases, the framework supports the systematization and standardization of indicators, which would have been endorsed by the market.

and the capital cost). IDB Invest has operationalized its pursuit of striking a balance in the portfolio between impact and financial return by defining a moving minimum for DELTA and FCR values and mapping each operation by those variables. The Portfolio 2.0 tool has been institutionalized and is used as a reference by porject teams, who must ensure that each operation meets the mandated thresholds. The approved portfolio does not include any operations that do not meet those minimums. There is also no correlation between these variables in general or by segment, seeing as the distribution of DELTA scores is clustered at amounts near the target score of 8 (with averages from different portfolios recently converging at similar average DELTA scores, around 8.4).

Figure 2.2

Portfolio 2.0 (2016-2021)

Source: OVE, based on DELTA data.



2.13 IDB Invest has not tapped Portfolio 2.0 to its full potential in terms of actively supporting decision-making at the portfolio level during origination. In keeping with its stated objectives, the tool has been used to help strike a balance between development impact and financial return ensuring that minimum thresholds for these values are met in a simple, practical manner. However, the tool is not as widely used to strike a balance between options at the sub-portfolio level. In addition, the clustering of DELTA scores around the corporate target narrows the search for other options. To address this issue, the tool could be recalibrated, taking into account different targets or thresholds by business segment, for example. The support provided by the DVF to Business Segment Chiefs in the form of processed data on their portfolios is appreciated. There is room to continue scaling up such support through the use of more dynamic tools that can visualize portfolios or run portfolio simulations with different assumptions and scenarios or that incorporate dimensions not currently taken into account (e.g., expected outcomes, additionality). Lastly, there is room to make methodological improvements to not just the DELTA but also RAROC (see Chapter VI). Executive Directors interviewed by OVE emphasized the importance of striking a balance between impact and financial returns but also consistently pointed up the need for more portfolio-level data and discussion of that data and its implications, moving beyond an operation by operation analysis.

D. Knowledge management and systematization

Box 2.8. Knowledge management and systematization
•*Objective:* Continuous learning (knowledge and lessons learned) and accountability. •*Stage:* Closure-Origination •*Components:* impact studies, repository of lessons learned, and other management and dissemination methods. *Source:* OVE.

2.14 Knowledge generation and management tools have shown improvement in terms of product delivery. The framework called for knowledge generation through the investment of resources in areas of specialization (e.g., impact assessments, studies) and the institution building a body of experience (e.g., operational lessons learned). In the area of knowledge product systematization and dissemination, notable steps forward include the improvements made to the Development Effectiveness Analytics system (DEA)[19] since 2018 and the production of impact studies. Having operation data on a single platform (after the integration of operation data on MAESTRO was finalized in 2022) promotes data integrity and traceability and reduces operational risk while facilitating the analysis and reporting process. IDB Invest has also undertaken major efforts to build databases (e.g., integrating approval data, supervision data, and XSR data). During the evaluation period, publication development varied but has been guided by pre-established criteria, at least in the case of impact studies.

2.15 Nevertheless, having codified content and systems in place does not in itself ensure that knowledge and lessons learned are used in practice. Staff interviewed and surveyed by OVE noted that platforms for lessons learned from operations, like the Mountains of Knowledge site (MOK) and the DEA, are readily accessible, and teams regularly review those sites when designing new operations. Recently, IDB Invest has made progress toward systematically identifying lessons learned at the operation level through the XSRs, but use of those lessons to inform the design of new operations is still incipient. Given the situation, IDB Invest is piloting an Automated

19 The DEA platform is integrated with MAESTRO and its features include data on approval DELTA and DELTA in supervision scores, a repository of publications and lessons learned from XSR, and data visualizations (e.g., Portfolio 2.0, XSR findings). The DEA currently includes over 850 lessons learned from operations.

Virtual Assistant (AVA) to automate searches for lessons learned during the origination phase. According to operation team leaders, the largely unsystematic use of lessons learned is mainly attributable to the fact that those lessons vary widely in quality. In some cases, teams feel that the lessons learned are not very useful for a variety of reasons (e.g., many lessons learned are from old operations that are very different from the operations that IDB Invest carries out today). There are no metrics for measuring the impact of studies (produced for internal or external audiences). Information obtained from interviews indicates that the main way that knowledge and lessons learned are disseminated and used within IDB Invest is through team discussions and consultations with teams that have built a body of experience in a specific issue. Interviewees appreciated processes that brought together participants from different divisions to develop and bring to the forefront useful lessons learned (as in the cases of MOK presentations to origination officers, XSR development, and the production of thematic or sector studies involving operational experience, such as the agrobusiness and gender studies).

2.16 At the institutional level, one pending task is the development of a strategy for integrating the knowledge generated by the institution. Gradual progress has been made in the development of knowledge products since 2016, though these efforts have not been entirely cohesive at the institutional level. Given this situation, the 2020-2022 Business Plan (document CII/GA-80-2) identified the need to develop a roadmap to coordinate knowledge management. That document is still in the development process. In 2021, several divisions that support nonfinancial additionality and knowledge creation were consolidated under the new Strategy and Development Department (DSP) (Advisory Services; the Environmental, Social, and Governance Division (SEG); the Development Effectiveness Division (DVF); and the Strategic Planning and Knowledge Division).

03

Strengthening Effectiveness and Additionality- Solutions and Operational Developments

3.1 This chapter discusses a series of (financial and nonfinancial) solutions and operational aspects introduced by IDB Invest with the end goal of strengthening effectiveness and additionality. This chapter discusses IDB Invest's efforts to diversify its financial products and develop an advisory services arrangement to strengthen its value proposition and client focus.[20] It also takes stock of the efforts made by IDB Invest to decentralize its staff and improve its processes for more efficient operation delivery.

A. Financial instruments

3.2 IDB Invest has made significant efforts to reconfigure the financial products it offers. One of the impact channels identified in the Renewed Vision was the expansion of the institution's financial product offerings. As reflected in its business plans, the objective of this expansion of product offerings was to transform IDB Invest from an institution focused on offering dollar-denominated senior loans (document CII/GA-80-2) to an organization with a more diverse offering of financial products geared to its clients' needs.

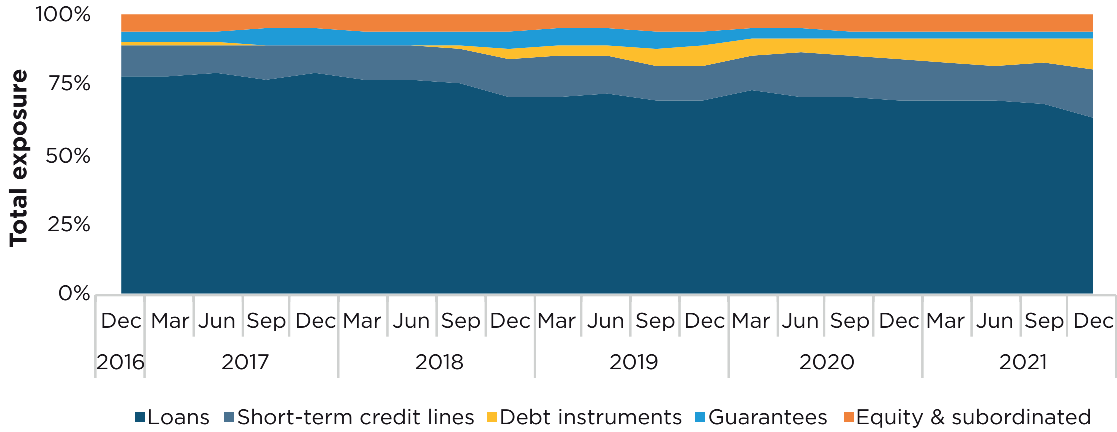
3.3 IDB Invest has pushed ahead with the expansion and diversification of its portfolio, though dollar-denominated senior loans are still predominant, and Group A and B countries account for most of the portfolio diversification. With expanded operational capacity from 2018 onward, IDB Invest worked to diversify and promote a more intensive use of different financial instruments (Figure IV.3.2 in Annex IV). To that end, it reduced its total exposure to senior loans, significantly increasing exposure to debt instruments (from a baseline of practically zero) and short-term credit lines. It should be noted that the current portfolio still partly reflects balances from the portfolio of operations originated prior to the merge-out and the creation of IDB Invest, when there were fewer financial instruments on offer. The following paragraphs discuss the achievements of IDB Invest's efforts to diversify its financial product offerings and the challenges encountered in those efforts.

20 For a more detailed discussion of the analysis performed, see: Background Note: Financial Instruments (Annex IV) and Background Note: Advisory Services (Annex V).

Figure 3.1

Total exposure by product type

Source: OVE, based on data from IDB Invest.



Notes: Includes DRAs booked on the IDB Invest and IDB NSG balance sheets. The "loans" category includes senior loans (in various currencies) and project finance (primarily finance issued to special purpose vehicles (SPVs) in the infrastructure segment). "Short-term credit lines" includes supply chain finance lines, TFFP loans, and TFFP guarantees. "Guarantees" exclusively refers to corporate guarantees. "Debt instruments" includes bonds, the credit receivables investment fund (FIDC), and other asset-based securities (ABS). "Equity and subordinated" includes direct investments, investments through funds, and subordinated, convertible, and mezzanine loans.

1. Short-term financing

3.4 IDB Invest expanded its offering of short-term products, especially in the corporate and infrastructure segments. Since 2018, IDB Invest has launched several short-term financial products, which together with the TFFP (which extends foreign trade finance to financial institutions and has been in operation since 2005) comprise the Trade and Supply Chain Finance (TSCF) portfolio. The products that reported the most growth were reverse factoring and traditional factoring. Reverse factoring is an instrument through which the supply chain (ideally SMEs) of an IDB Invest corporate client can benefit from the larger or "anchor" company's financing cost. Through reverse factoring, IDB invest hopes to cater to its clients' working capital needs and finance supply chain SMEs. Through traditional factoring, IDB Invest seeks to finance the low-income clients of large corporations (e.g., end users of telephone or electricity companies). OVE analyzed the TFFP and reverse factoring since these two products accounted for the bulk of the volume of short-term operations over the evaluation period.

3.5 IDB Invest worked to fine-tune the TFFP's selectivity to improve additionality, but there is room, from a development outcomes perspective, for continued strides toward expanding coverage for SMEs. The TFFP-related findings from OVE's 2016 Evaluation of the IDB Group's Work Through Financial Intermediaries (document CII/RE-18-4) focused on a failure to measure the program's results. To address this issue, IDB Invest developed a program-level results matrix, a DELTA adjusted to the instrument's specifications, and results matrices for credit lines. Management also worked to strengthen reporting on SMEs indirectly supported by the program and enhance controls for identifying noncompliance or risks related to money laundering or to environmental and social standards. In addition, Management performed cost-benefit analyses of the TFFP using RAROC. With respect to selectivity, use of the product in Group C and D countries increased (rising from 45% of total disbursements before 2016 to 53% between 2016 and 2021), as did its use in small and island countries (rising from 5% to 12% over the same period). Over the 2017-2021 period, more than 60% of TFFP lines approved or renewed were in countries with medium or high risk ratings and with banks that are not considered major players in their markets. Though scores on the development outcomes section of the DELTA TFFP score for the program has trended up, there is room to keep working toward expanded coverage for SMEs (Box 3.1).

Box 3.1. Aggregate DELTA scores for the TFFP

Since an analysis of individual TFFP operations was beyond the scope of the evaluation, OVE only analyzed trends in aggregate DELTA scores for the TFFP. The program's score at approval on the development outcomes section (stage 1[a]) held steady at around 6.6 (out of 10) over the 2018-2021 period. The indicator's stage 2 score has improved, increasing from 7.7 in 2018 to 8.3 in 2021. Under the section of "access to finance" indicators, OVE reviewed the "magnitude of reach" variable (which measures the ratio of growth of the client's foreign trade portfolio to that of the country's foreign trade portfolio). This variable's score decreased from averages of 4.3 and 4.5 (out of 6) in 2018 and 2019, respectively, to 4.0 in 2020 and 2021. The decline can be attributed, in part, to the lower than expected growth in foreign trade portfolios as a result of the pandemic.

Lastly, OVE examined the "SME reach" indicator and found that 41% of lines approved or renewed in 2021 targeted SMEs, which is an improvement compared to 2017 (24%).[b] In light of the emphasis that various TFFP strategic documents place on SMEs, there is room to keep expanding SME coverage through the TFFP.

Source: OVE, based on DELTA score data for the TFFP.

Notas: : [a]TFFP operations are assigned DELTA scores at two stages: (1) when the line is approved or renewed; and (2) for each disbursement under the line once its particulars are known (e.g., guarantee versus loan, whether it includes mobilization, whether it finances SMEs, and whether it establishes a new linkage with correspondent banks). As opposed to other instruments, TFFPs can be approved with a DELTA score as low as 5, but as a rule IDB Invest seeks to ensure that the DELTA at the second stage is higher than the first-stage score. [b]By IDB Invest's understanding, a financial institution finances SMEs if at least 15% of its foreign trade portfolio is directed to that segment.

3.6 In OVE's view, the TFFP stands out as a tool that has high strategic value for IDB Invest. Even so, its availability could be heavily restricted with the end of the cross-booking period. Thanks to the low level of risk of underlying operations and the short tenor of these transactions, IDB Invest has been able to use the TFFP as a gateway to get to know potential clients. All told, 63 financial institutions (out of a total of 113) used the TFFP as an entryway to then expand to other instruments. Regarding mobilization, the TFFP's global financial intermediary network consists of more than 100 correspondent banks in over 40 countries. IDB

Invest also carried out syndication operations with 23 financial institutions under the TFFP, thereby mobilizing US$1.175 billion from 2016 to 2021 (11% of its total core mobilization). The TFFP was a core component of the operational response to the pandemic, as IDB Invest temporarily expanded the program limit to US$3 billion. Though use of the TFFP increased significantly during the pandemic, IDB Invest used just 45% of the approved additional amount because government responses to the crisis generally aimed to provide liquidity.

3.7 Reverse factoring is still a relatively new instrument, but early findings point to the need to improve the selectivity of interventions (Box 3.2). OVE has validated XSRs for only two of the 13 reverse factoring operations approved during the 2016-2021 period (those two are the most mature, at four years). OVE performed a documentary review of the 13 approved operations to identify emerging findings (Box 3.2). Of those 13 operations, six are less than two years old, so it is still too early to review their results.

Box 3.2. Reverse factoring - Results of the first few operations/ emerging findings

For the product to work properly, basic regulations and infrastructure need to be in place for the program, including electronic invoicing, platforms that facilitate the exchange of accounts payable, and financial intermediaries that have experience using the instrument. Because of this, Mexico was chosen to pilot the program, since the country has experience with this type of product since 2001. Management is currently in the process of approving regional lines and exploring the program's expansion to other countries.[a] Coordination with the IDB could play an important role in helping to improve legal frameworks to expedite adoption of the instrument in countries where this type of financial product is not available.

The selectivity approach was weak, and efforts were focused on rolling out the program. In its review of operations, OVE found that IDB Invest did not have a systematic analytical approach to identify the economic sectors in which the need to close financing gaps for SME suppliers was greatest (i.e., sectors in which suppliers have longer terms of payment). Furthermore, OVE did not find any tools for identifying which anchor companies had more flexibility or could more easily bring additional SMEs into the program. IDB Invest focused its efforts more on setting up the product and bringing it to a minimum scale.

Additionality depends on a case-by-case analysis. OVE found that: (1) IDB Invest played a tangible role in encouraging anchor companies to bring more SMEs into the program: anchor companies have little incentive to include small businesses in their reverse factoring programs, and OVE found evidence of IDB Invest's efforts to push clients to include smaller suppliers; (2) in some cases IDB Invest, as the lender, played a role in diversifying anchor companies' working capital funding structure; (3) the product afforded IDB Invest the opportunity to establish new relationships with corporate clients to explore their credit quality and their ability to execute a value chain sustainability strategy; and (4) OVE found that the product has the potential to offer significant additionality for improving SME financing conditions in countries where reverse factoring mechanisms are not already in place. These findings depended greatly on the circumstances of each company. For example, one of the clients interviewed said they decreased use of other bank lines because of the IDB Invest financing (market crowding-out effect). However, that same company said it probably would not have included SMEs in its program if not for IDB Invest's encouragement.

Management has taken steps to monitor the risk of deterioration in the terms of payment offered by anchor companies to their suppliers. For several years, IDB Invest has been monitoring a "maximum days until payment to suppliers" indicator so as to identify potential corrective actions if it determines that suppliers' terms of payment are worsening. Since 2022, this indicator has been included in operation results matrices (with specific targets).

In the case of the two operations with OVE-validated XSRs, overall performance was positive (successful or partly successful), though results were mixed in terms of achievement of development objectives. In both cases, financing terms and conditions for SME suppliers improved as expected and the financing extended to SMEs under the IDB Invest line fell within the established parameters. However, this did not translate into the expected growth of the total reverse factoring portfolio (considering all lines).[b] The number of participating companies increased in one operation and remained the same in the other.

Source: OVE.

Notas: [a]Four regional lines were approved as of year-end 2021. Though the anchor companies for these lines are based in Mexico, the lines aim to facilitate discounting for suppliers in at least 10 countries where the product is not yet available. [b]Since money is fungible, it is important to analyze growth of financing to SMEs in the total reverse factoring portfolio as well as in the IDB Invest portfolio. In fact, the rationale for IDB Invest's involvement in the reverse factoring program is that the institution can make an additional contribution to the growth of each anchor company's program.

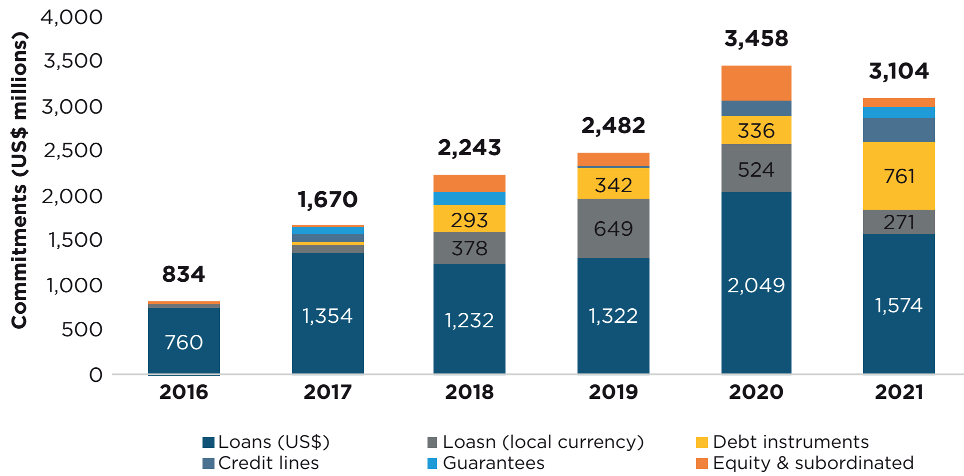
2. Long-term financing

3.8 IDB Invest developed a wide array of long-term financial solutions. To expand its offering of financial solutions, IDB Invest sought to match its development mandate to client demand and the resources and capacity it had available as an emerging organization. The solutions now in existence range from dollar-denominated senior loans (loans in which IDB Invest has the first-ranking right to collect) to equity investments (in which IDB Invest is a shareholder of the companies in which it invests). Between these two extremes lie hybrid instruments like mezzanine debt and subordinated loans (i.e., second-ranking right to collect). IDB Invest developed more sophisticated instruments that fall under the category of senior financial solutions, such as structured loans, debt capital market instruments, and guarantees.

Figure 3.2

Long-term commitments by instrument type

Source: OVE, based on data from IDB Invest.



Note: These categories are not mutually exclusive. For example, credit lines may include debt capital markets program (DCMP) products, such as warehousing lines of credit.

3.9 Implementation of certain products was constrained by operating restrictions. Instruments under the debt capital markets program were one such case. Exposure to this product jumped from US$50 million in 2016 to US$1.505 billion in 2021, which enabled IDB Invest to expand its market presence, participate in high visibility transactions, and play a key role in the creation of the thematic bond market. Nevertheless, the bond subscriptions that IDB Invest was involved in had terms very similar to traditional loans and mobilization was very limited. Only 26% of the bond issues that IDB Invest was involved in were subscribed by other investors. Furthermore, IDB Invest subscribed the entire bond issue in 70% of the bond issues in which it was involved.[21] This diminished capacity for participating in public issues and generating direct mobilization was largely due to operating restrictions, primarily legal ones.[22] Therefore IDB Invest focused its efforts on ensuring that its involvement was viable, while its role as mobilizer and anchor investor was sidelined. One crucial challenge at a crosscutting level is the need to review and continue improving processes and systems in order to scale up business and product volumes.

3.10 In other cases, IDB Invest's economic capital was a constraining factor. Use of equity investments was limited due to their high economic capital requirements. The equity investment portfolio

21 These account for 23 of the 33 products under the Capital Markets program, excluding partial credit guarantees and warehousing lines of credit. Six of the 10 projects in which IDB Invest did not subscribe the entire issue were instruments issued on international markets.

22 Historically, IDB Invest has handled its contractual relationships with clients using bilateral loan contracts under New York State law, which include specific clauses regarding its nature as a multilateral organization, including development data reporting requirements, integrity requirements, and environmental and social standards. In contrast, open market transactions, which tend to be more liquid, use a standardized bond prospectus and contract, which do not include the safeguards required by IDB Invest to participate as an anchor investor and tend to follow local law.

has grown in recent years, but its share of the total portfolio remains minimal (2.3% as of December 2021). Expanding use of this instrument requires a combination of additional capital and efforts to build capacity in terms of staff and processes.[23] Another such example is the case of blended (concessional) finance, which enables IDB Invest to support projects in which the development impact would be difficult to achieve without the use of concessional resources. From 2016 to 2021, IDB Invest approved 55 blended finance projects, using US$377 million in concessional funds and putting up US$1.361 billion of its own resources. Concessional resources depended entirely on donors, since IDB Invest did not have its own capital available for this type of initiative.

3.11 IDB Invest also contended with significant challenges in each of the types of market it served. In Group A and B countries and investment-grade jurisdictions, on one hand, financial markets are deeper and more sophisticated, so IDB Invest must take additional steps to develop financial products so as to provide enough additionality. On the other hand, the low volume of operations in Group C and D countries and countries with higher sovereign risk did not always support the standardization of solutions or the implementation of more complex solutions. Furthermore, increasing operations in small and island countries proved difficult at a time when economic capital was limited and IDB Invest had committed to maintaining specific levels of portfolio risk ("B+" or higher), on top of the unique challenges of working in those countries.[24]

3.12 IDB Invest found niches where it could use its competitive advantages to provide additionality. For example, investments in subordinated and mezzanine loans require a less intensive use of capital than pure equity investments. In addition, these products are still in short supply in the region because commercial banks do not offer them, and few debt funds focus on this type of instrument. In the financial sector, clients appreciate subordinated financing since the product helped them bolster their regulatory capitalization ratios at a relatively low cost. As of December 2021, exposure amounted to 4.2% (US$556 million) of the total portfolio.

23 For a more detailed discussion, see the Comparative Study of Equity Investing in Development Finance Institutions (document CII/RE-20-2).

24 Staff involved in origination efforts in small and island countries who were interviewed by OVE repeatedly cited a series of obstacles to increasing financing in these countries, including high market liquidity, constraints relating to the financial products offered by IDB Invest (e.g., local currency), and the high transaction costs associated with the greater challenges that arise when applying IDB Invest requirements and standards in those countries (e.g., legal, environmental, and social standards), due to such reasons as smaller operation sizes and limited client capacity in certain cases.

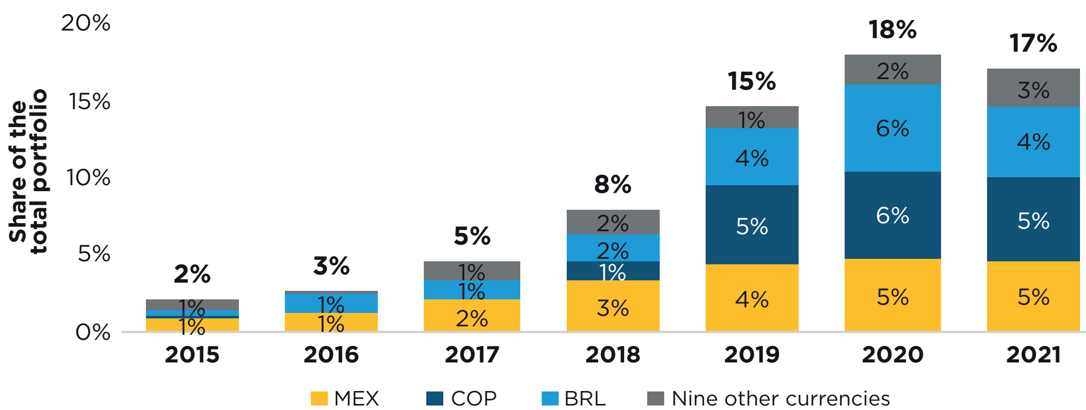
3. Local Currency

3.13 IDB Invest managed to increase considerably the local currency solutions it offers, though implementation has run into some challenges. IDB Invest has increased its capacity for financing local currency operations in several countries in the region.[25] Long-term commitments in local currency rose significantly thanks to the implementation and use of various mechanisms, such as local treasury, swaps, customized local issues, credit lines with local financial institutions, and the IDB local currency facility.[26] However, these solutions are concentrated in Group A and B countries due to internal operating restrictions and market constraints. All told, 87% of long-term commitments in local currency were in countries in which the volume and scale was large enough to operate with local treasury or swap mechanisms (e.g., Mexico, Brazil, and Colombia). The Colombian peso, the Brazilian real, and the Mexican peso are the main currency exposures at the portfolio level (Figure 3.3).[27] Members of the business area interviewed and surveyed by OVE repeatedly cited the availability of local currency solutions as one of the major challenges at the financial solution level. The IDB local currency facility (which uses IDB capital) has been useful for smaller economies whose currencies are not as liquid (e.g., Guatemala and Costa Rica). As of December 2021, approximately half of IDB Invest's local currency exposure was booked on the IDB balance sheet. That figure has trended downward since 2019 as IDB Invest strengthened its own treasury.[28]

Figure 3.3

Local Currency: Exposure by currency

Source: OVE, based on data from IDB Invest.



25 Since the merge-out, IDB Invest has expanded the number of financial solutions available (the combination of currency and rates). At present, IDB Invest offers local currency solutions in 15 countries.

26 Long-term commitments in local currency accounted for 13% of total commitments over the 2016-2017 period and 20% over the 2020-2021 period.

27 IDB Invest has participated in projects involving nine other currencies, including the local currencies of Paraguay, Peru, Trinidad and Tobago, the Dominican Republic, Uruguay, Costa Rica, Chile, and Guatemala, in addition to a lower exposure in Euros.

28 As of December 2021, 53% of local currency exposure was booked on the IDB's balance sheet, while the remaining 47% was booked on the IDB Invest balance sheet. On average, 65% of local currency exposure during the 2018-2021 period was booked on the IDB balance sheet.

B. Resource mobilization

3.14 Though mobilization has always been part of IDB Invest's value proposition,[29] in more recent years the institution has scaled up its efforts on this front. In its 2020-2022 Business Plan (document CII/GA-80-2), IDB Invest began to acknowledge that it had to evolve from a pure lender to an asset manager. Until that time, IDB Invest had focused on deploying its lending capacity using its own balance sheet. Since 2020, it has placed greater emphasis on the mobilization of third-party resources. In fact, interviews with members of the business area confirmed that in recent years (especially after 2020), origination targets began to include the quantity of third-party resources alongside the quantity of IDB Invest resources.

3.15 Resource mobilization increased significantly during the evaluation period but remains below the amounts projected in the Renewed Vision. IDB Invest has built significant capacity for mobilization of third-party resources, which has translated into a higher volume of resources mobilized and a wider array of mobilization instruments. As a result, core mobilization[30] rose from US$860 million in 2016 to approximately US$3 billion in 2021. Continuous, sustained growth began in 2018 when the institution posted average annual growth rates of 22%. Meanwhile, IDB Invest has taken a less proactive approach to catalytic mobilization, which, as a share of total mobilization, fell from an average of 75% in 2018 to 25% in 2021. This was the by-product of IDB Invest's intentional effort to focus its efforts on leading syndicated operations (operations with multiple participants) in which it offered greater additionality, as is the case with core mobilization. Though IDB Invest reported US$10.7 billion in core mobilization since the merge-out (US$24.4 billion when including catalytic mobilization as well), those figures are lower than the estimates set out in the Renewed Vision (US$34.2 billion over the 2016-2021 period).[31]

29 Increasing resource mobilization is one of the objectives of the current IDB Group Institutional Strategy (document CII/AB-1540-2). To bolster its mobilization efforts, the IDB Group also prepared an IDB Group Mobilization Roadmap 2020-2023 (document GN-2988-1), which includes measures to increase resource mobilization in all borrowing member countries.

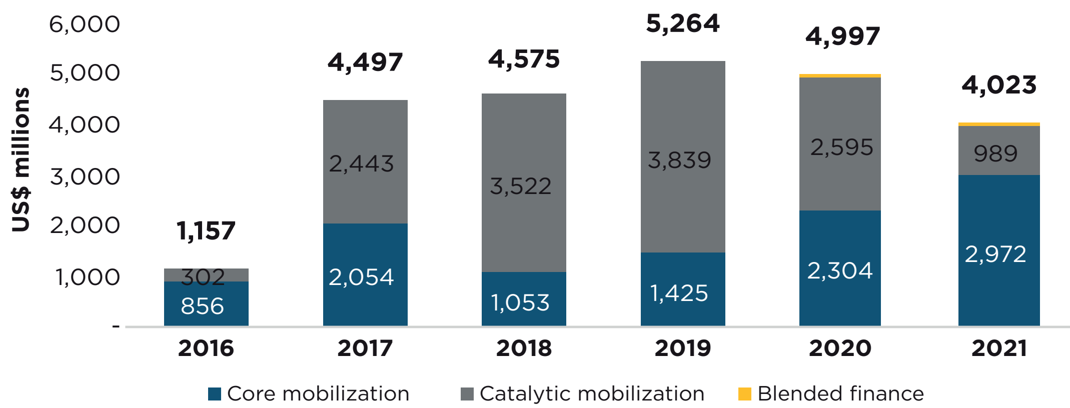
30 **Core mobilization** refers to resources from external partners mobilized directly in support of IDB Invest financing operations. IDB Invest's efforts to guide the investors has to be tangible and verifiable, generally through payment of a mobilization fee and the issuance of a mandate letter. **Catalytic mobilization** (or complementary mobilization) refers to financing in which IDB Invest participates alongside other investors (private investors or public development agencies) to facilitate the investment, but the enlistment of other investors cannot be directly attributed to IDB Invest or there is no verifiable evidence supporting attribution to IDB Invest.

31 Those estimates were for mobilization as a whole and did not distinguish between core and catalytic mobilization (audiovisual presentation CII/PP-149).

Figure 3.4

Mobilization: Amounts mobilized over time

Source: OVE, based on data from IDB Invest.



Note: The mobilization categories and definitions considered (core and catalytic mobilization) do not necessarily coincide with the definitions established in the "MDB Methodology for Private Investment Mobilization."

3.16 Certain market variables adversely affected mobilization capacity in some countries. One example pertains to market size and perceived risk. Some small economies (especially Group C and D countries) are not fully integrated into international financial markets, and their credit ratings are below investment grade (BBB-). This diminishes international institutional investors' appetite, since they are not well versed in these markets or have a low appetite for the low volume these transactions generate. In addition, some countries contend with additional challenges in terms of the level of business maturity in the areas of corporate governance and integrity risk, which further limits international investors' appetite. As recent evaluations of mobilization at other MDBs have shown, the capacity to identify portfolios of projects eligible for financing is a key driver of the success or failure of private capital mobilization. At IDB Invest, in addition to the aforementioned challenges to scaling up financial products instrumental to or explicitly for mobilization (e.g., equity investments and debt capital markets), efforts to systematically identify mobilization potential (accounting for investor preferences) at the country, sector, and instrument level are needed, and systems and processes need to be improved so the institution can more systematically monitor its mobilization efforts.

3.17 IDB Invest deconcentrated its portfolio and went from mobilizing a handful of large projects to having a more diversified pipeline. IDB Invest steadily increased the number of operations that involve a mobilization component from 24 transactions in 2016 to 65 transactions in 2021. Most of this growth came from operations with core mobilization, which jumped from 22 transactions in 2016 to 57 transactions in 2021. As a result, IDB Invest brought down its concentration levels and diversified the average size of its mobilizations, which made its ability to meet volume targets less dependent on a small number of very large transactions. For example, the average amount mobilized per operation fell from a peak of US$220 million in 2017 to US$65 million in 2021 (total mobilization). As regards core mobilization in particular, these figures fell from US$76 million to US$52 million over the same period.

C. Advisory services and compliance

3.18 IDB Invest complementes its financial product offerings with an important client support and advisory services component. Looking at the various sources of nonfinancial additionality, a core area of IDB Invest's work focused on helping clients comply with environmental and social standards, an area in which IDB Invest has significantly improved its internal capacity during the evaluation period (Box 3.3). This section focuses mainly on advisory services, taking into consideration the expanding portfolio of recent years and the important role these services play as a potential source of nonfinancial additionality.

3.19 IDB Invest forged ahead with building internal capacity for mananging advisory services. IDB Invest identified that it could tap advisory services to strengthen the nonfinancial additionality of its interventions through capacity-building and knowledge generation. For that reason, it created the Advisory Services Division (ADV) as a resource for advisory service delivery. During the evaluation period, ADV evolved from a team focused on managing donor resources to a team of specialists in various thematic areas: Gender, inclusion, and diversity; climate change; SMEs and sustainable business; public-private partnerships (PPPs); and, more recently, digital transformation. ADV also took on an important role in the development of the IDB Group's crosscutting agendas (e.g., climate change; gender, diversity, and inclusion) and has been actively involved in working groups at the IDB Group level, including those for value chains, thematic bonds, and SMEs. ADV manages 90% of client advisory services, while the remaining 10% is managed by such divisions as the Environmental, Social, and Governance Division (SEG) and the Development Effectiveness Division (DVF).

Box 3.3. Environmental and social risk management

The Renewed Vision stressed the need to maintain the IDB Group's high levels of environmental and social standards. Before the merge-out, the IIC's experience with projects that entailed high environmental and social risks was limited. Given that limited experience and the growth in the operations portfolio during the evaluation period, IDB Invest focused on building capacity for managing this type of risk at the policy framework level and at the operation level.

SEG expanded its staff and added new areas of specialization during the evaluation period, consolidating its position as a resource for several areas. SEG is responsible for working with clients to structure operations to meet the environmental, social, and governance criteria set out in IDB Invest policy, supporting them with compliance. This is a key source of nonfinancial additionality, inasmuch as commercial sources do not offer this degree of support and rigor and insofar as these standards translate into better development impacts for supported projects. IDB Invest clients interviewed by OVE repeatedly stressed the importance of IDB Invest's support in this area.

In 2019, OVE conducted an evaluation of the IDB Group's Environmental and Social Safeguards (document CII/RE-36-1), which prompted IDB Invest to implement a series of actions to bolster its capacity for managing environmental and social risks. OVE recommended that IDB Invest revise its environmental and social sustainability policy, strengthen monitoring and supervision of environmental and social risks and impacts, and strengthen IDB Invest staff and client capacity for managing environmental and social risks. IDB Invest is on track to complete the actions proposed to address OVE's recommendations. In April 2020, IDB Invest approved its new Environmental and Social Sustainability Policy (document CII/GP-998-16), which adopted a uniform system of standards that is widely used in the market (the IFC performance standards). A manual for implementation of the policy (document CII/GP-16-15) was finalized in December 2020. In this context, IDB Invest implemented a series of training and capacity-building activities for IDB Invest personnel and clients, most notably Sustainability Week. With respect to supervision, IDB Invest has enhanced supervision of projects initially classified as low risk and has made system-level improvements to support the monitoring of environmental and social aspects, including action plans for clients and corrective action plans developed in response to environmental, social, and governance supervision.

Between 2016 and 2021, the Independent Consultation and Investigation Mechanism (MICI) received four complaints related to operations approved by IDB Invest, three of which were registered and later became MICI cases pursuant to the provisions of the MICI policy. As of this writing, two cases are in the investigation phase (Ituango and Ruta del Cacao). As for the third case (Generadora San Mateo and Generadora San Andrés), the MICI concluded its investigation in 2022 and made certain recommendations regarding IDB Invest's responsible exit from the project in the event it decided to withdraw its financing, which it ultimately did. The MICI is currently monitoring the Action Plan proposed by IDB Invest.[a]

In response to a recommendation made by OVE as part of its 2021 Evaluation of the MICI (document CII/RE-56-2), IDB Invest recently established an internal mechanism (the Management Grievance Mechanism, MGM) that communities potentially harmed by project environmental and social impacts can use to resolve their complaints. The MGM is managed by a new unit (the Environmental and Social Risk Department, RSM/SER), which was created under the Risk Management Department in 2021.[b] It is still too early to determine whether the MGM is effective and, more specifically, the extent to which this mechanism coordinates with the MICI and ensures that requesters have access to an expedited, transparent, and secure response to their grievances, as recommended by OVE.[c]

Source: OVE.

Notes: [a]IDB Invest exited the Ituango project in 2022. Over the 2016-2021 period, the MICI also managed the investigation of other cases related to NSG operations approved before the merge-out that have been supervised by IDB Invest since 2016. The Board of Executive Directors did not approve the investigation of the first case (Reventazón). The MICI concluded its investigation of the second case (Alto Maipo) in 2021. The MICI finished monitoring this case in November 2022, at which time it reported that 12 of the 21 actions proposed by Management had been completed. At that time, IDB Invest was on track to complete seven other actions. IDB Invest exited that investment in 2022. [b]RSM/SER is also responsible for supporting environmental and social risk management at the portfolio level and developing and disseminating environmental and social lessons learned. [c]The recommendations from the Evaluation of the MICI were for the MICI, the IDB and IDB Invest Boards of Executive Directors, and IDB and IDB Invest Management. The evaluation's other recommendations for IDB and IDB Invest Management were to reinforce the independence of the MICI and ensure that corrective action is taken when there are findings of noncompliance with the policies and associated harm.

3.20 Over the 2019-2021 period,[32] 255 advisory services were approved, for a total of US$22.9 million. All told, 46% of advisory service engagements focused on climate issues, 25% on gender and diversity, 23% on SMEs, and 7% on PPPs. In all, 54% of the financing operations approved over that period involved advisory services. The segment that benefited from operation-related advisory services the most was financial institutions, which accounted for 46%. Meanwhile, corporate clients accounted for 37%, and infrastructure and energy clients accounted for 17%. The distribution of advisory services across regions was proportionate to their share of the portfolio (Country Department Andean Group (CAN): 17%; Country Department Southern Cone (CSC): 19%; Country Department Central America, Haiti, Mexico, Panama, and Dominican Republic (CID): 29%; Country Department Caribbean Group (CCB): 8%; and regional: 27%).

3.21 The advisory services business model tends to focus on supporting investment operations during the origination stage, is typically financed by donors, and involves high levels of concessionality for clients. All told, 67% of advisory services contracts signed between 2019 and 2021 were geared toward supporting investment operations in priority areas, mainly during origination. Use of advisory services for market and operation pipeline development was more limited. In addition, OVE did not find evidence that IDB Invest was systematically offering its clients advisory services at the supervision stage to help them achieve their development objectives. Donor funds provided more than 92% of advisory services funding, and most advisory services involved a concessional component. IDB Invest has sought to ensure that clients contribute at least 30% of the value of the advisory services but has made exceptions, especially in smaller countries and economies.

3.22 The funding model, which is dependent on IDB Invest donors, has some limitations. IDB Invest was able to leverage existing relationships with donors and find concessional funds to promote crosscutting issues in operations at a time when its administrative budget was limited. For this model to work, however, donor priorities and requirements had to be closely aligned with IDB Invest's strategy and client demand. In some cases, donor resources could not be executed due to a lack of such alignment. IDB Invest currently has US$26.2 million in donor resources at its disposal, approximately half of which (US$12.5 million) cannot be used for the existing pipeline of operations. Since donor funds do not fully satisfy need, IDB Invest contributed resources from its ordinary capital (Technical Assistance and Strategic Partnerships Division (TAS) funds), but those funds were limited (US$1.5

32 Since 2019, IDB Invest has kept more systematic records of advisory service monitoring and supervision.

million executed during the evaluation period). For IDB Invest, it is important to maintain a constant inflow of these administrative funds so that the institution can execute elements of its strategy that are not covered by donors.

3.23 Selection of the clients and operations that would receive advisory services was ad hoc and does not have discernible prioritization criteria. OVE found that, in practice, prioritization was mainly based on a need to improve an operation and its DELTA score, a case-by-case analysis of client capacity for executing the operation, client demand, and availability of resources. From its interviews of personnel involved in origination efforts, OVE found that the first selection filter was swayed by DELTA-score-based incentives for Investment Operations Department (INO) officers, especially when the operation's financial additionality was considered low.

3.24 The recent development of diagnostic assessment tools for analyzing client capacity is an important step toward building a more robust process for advisory service selection and design. For example, IDB Invest has used its Women Empowerment Principles (WEP) tool since 2017 to determine its clients' level of maturity in gender equity, design interventions, and monitor client progress. In addition, SEG has developed a tool to determine the level of maturity of IDB Invest's financial institution clients in the area of environmental and social risk management capacity and to develop green products and receive climate finance. With a broader set of tools, IDB Invest could institute a more systematic process for putting advisory services to strategic use, measuring client development gaps, and determining the extent to which IDB Invest makes a meaningful, lasting impact through its advisory services.

3.25 At the monitoring and evaluation level, there is still no results-based analysis and evaluation framework in place. IDB Invest has taken steps toward ensuring that operation monitoring and evaluation tools (results matrices, DELTA scores, XSRs) address advisory services associated with investment operations. In its analysis of the vertical logic of operations, OVE found that IDB Invest made advisory services available to: (a) improve financing operations' development outcomes (e.g., assisting banks with growing their "banking on women" portfolios); or (b) achieve other, broader objectives at the client level that did not necessarily have a direct link to the individual operation's specific development objectives (e.g., advisory service engagements to improve a company's performance in corporate governance). OVE found that results matrices and approval documents did not always explicitly indicate whether the various advisory service engagements were tied to achievement of the operation's development objectives or if their intention was to support broader development objectives (at the client or market level). In other cases, these documents also did not justify why the advisory services in question were vital to achieving the operation's development objectives or the broader objectives. At the supervision stage, OVE found that operation monitoring (including XSRs) still does not involve a comprehensive analysis of whether the changes the clients experienced as a result of the advisory services were lasting or the extent to which they can be attributed to IDB Invest's intervention. IDB Invest does not have results matrices for advisory service engagements that are not tied to a transaction, and, for the most part, there has been no systematic effort to use the IDB Invest monitoring and evaluation systems to review these engagements.

3.26 These challenges notwithstanding, OVE found that advisory services were an important driver of operation additionality. In its review of operations, OVE found that operations that involved advisory services (41% of the operations in the sample involved such services) had better financial additionality. Of the transactions that involved advisory services, 42% had "excellent" nonfinancial additionality, and 45% had "satisfactory" nonfinancial additionality. In contrast, looking at operations that did not involve advisory services, only 23% had "excellent" nonfinancial additionality, while 53% had "satisfactory" nonfinancial additionality. This better nonfinancial additionality rating was driven by stronger performance in the "knowledge, innovation, and capacity" area, which addresses improved client capabilities.

D. Staffing and decentralization

3.27 IDB Invest has been gradually building a more diverse workforce. As of December 2021, IDB Invest had 522 employees (405 staff, 117 consultants), a 63.6% increase compared to December 2016. IDB Invest's workforce primarily hails from borrowing member countries (72%) and is gender-balanced (49% men and 51% women). Though the share of IDB Invest leadership positions held by women rose from 35% to 45% over the 2016-2021 period, increasing women's involvement at that level continues to be a challenge. IDB Invest division and unit chiefs and managers interviewed by OVE frequently report that talent recruitment and retention (especially in the region) is a critical challenge. A review of the compensation and rewards strategy (CRS) was approved in late 2022. IDB Invest also has plans to implement a major organizational culture initiative with the objective of developing a roadmap to close the gap between the current organizational culture and the culture it hopes to instill.[33]

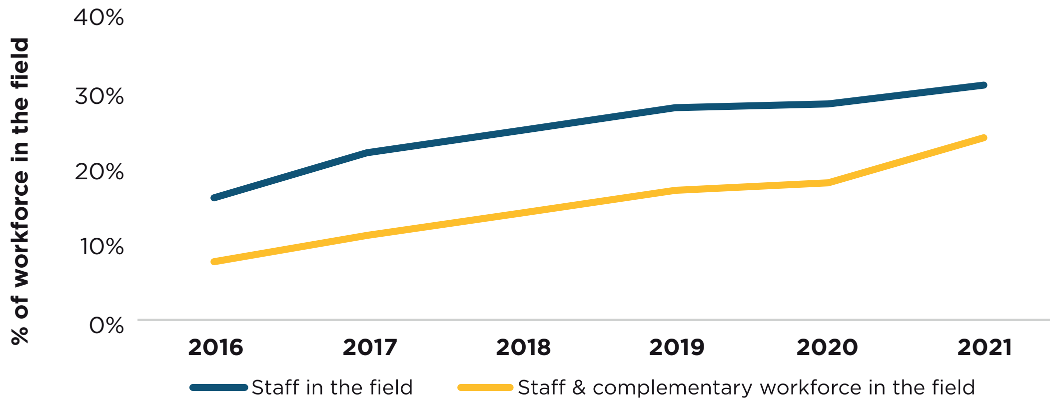
33 The plan was to finalize the development phase and launch implementation of the initiative in 2022. However, amid the discussions of a potential new business model for IDB Invest, the institution is in the process of redefining the timeframes for developing

3.28 As business volume has increased, IDB Invest has expanded its footprint in the region. IDB Invest implemented a field presence plan (document CII/GA-76-2) to increase origination capacity in all countries and consolidate certain support functions in four regional centers (Bogota, Buenos Aires, Panama City, and Kingston) under its new third country national (TCN) contract modality. As of December 2021, IDB Invest had a presence in 25 countries, a significant increase compared to December 2016, when it was in 14 countries. Over the same period, the share of staff in the region rose from 16% to 31% (Figure 3.5), outperforming the target set out in the field presence plan (30%). IDB Invest personnel interviewed by OVE consistently cited the increase in staff in the region as one of the institution's most significant achievements and spoke of the crucial role this played in building closer relationships with clients.

Figure 3.5

Workforce in the field over time (2016-2021)

Source: OVE, based on data from the IDB Group Human Resources Department.



3.29 Nevertheless, there is room to deepen the decentralization process, especially as regards decision-making. Most chiefs interviewed noted that the increase of staff in the region has not been accompanied by a decentralization of processes and decision-making.[34] Only 11% of leadership positions[35] were in the field as of December 2021. Furthermore, the decentralization process mainly emphasized the expansion of origination capacity, which has manifested in the fact that over 60% of the staff of INO's three business segments is in the field (Annex II, Box II.4). Given this situation, some tasks ahead include greater decentralization of other support areas and, in particular, identifying how to keep growing in the region with a model that has, until now, largely depended on recruiting local talent.[36]

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and implementing this initiative.

34 In all, 70.7% of investment officer respondents felt that the degree to which decision-making had been decentralized was inadequate (39%) or partly adequate (31.7%).

35 This includes executive positions and grade A and B staff. Of that total, only one grade A employee and six grade B employees were in the field as of December 2021.

36 In 2021, seven international positions were in the field (four staff positions and three consultants), and 13 positions used the TCN modality. The rest were local staff, who accounted for 88% of total staff in the field.

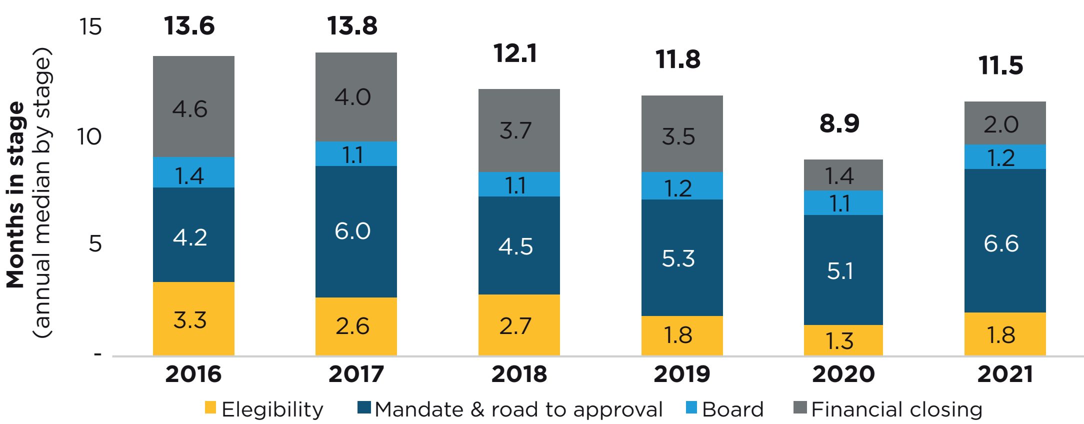
E. Operation management processes

3.30 IDB Invest implemented a series of process-level improvements at the operation origination stage. The first stage of the Operational Excellence initiative, which aimed to simplify and streamline operation management processes, focused on the origination phase with the objective of breaking down internal silos and improving relationships with clients. To achieve this, IDB Invest implemented a series of changes supported by recommendations from a consulting engagement with McKinsey (2017). Those measures included process updates, the creation of transaction units with staff from different offices (CTUs),[37] and the introduction of weekly huddles to incentivize the flow of information. On the whole, INO staff respondents had a favorable opinion of these efforts but stressed that the institution should continue to streamline processes and work to differentiate approval processes for repeat clients or based on project complexity, for example. The origination-focused stage of the Operational Excellence initiative effectively shortened timeframes (mainly during the first stage: eligibility) by streamlining documents and requirements and increasing delegation of authority at this stage (Figure 3.6). The initiative now has a permanent team responsible for identifying continuous improvements to the origination process.

Figure 3.6

Average time in stage, by approval year (months)

Source: OVE, based on data from IDB Invest.



3.31 The implementation of improvements at the supervision stage has gained less traction, and significant challenges lie ahead. The second stage of the Operational Excellence initiative was launched in 2019 to identify improvements for the supervision stage. Notable changes introduced since 2021 include implementation of a WACs system[38] that delegates more authority to investment officers,

37 CTUs, or Client Transaction Units, are operation groups with members from different areas in which investment officers and officers from various support areas work collaboratively on a number of projects. CTUs are divided by segment (for corporate and financial institutions transactions) and, in the infrastructure segment, by region (and were implemented later).

38 WACs = waivers, amendments, and consents (for modifying certain clauses in existing contracts with clients).

development of tools to visualize portfolio exposure, and the first stage of automating annual supervision reports. This second stage of the initiative is less developed and has been less relevant at the institutional level compared to the origination-focused phase and poses pending challenges related to implementation of improvements in the area of operation support and assistance (backbone). Staff involved in portfolio supervision appreciated the initiative but routinely identified a need to continue improving supervision processes and support systems, including through greater automation of processes that continue to be carried out manually. As IDB Invest's portfolio and products have grown, some supervision teams, such as the Portfolio Management Division (PTM), have not expanded their staff at the same rate as origination teams.[39]

3.32 At the institutional level, IDB Invest has taken important steps to strengthen processes and systems, though significant challenges persist considering the institution's rapid growth in recent years. At a time when its business volume is increasing, its product offerings are expanding, and its products are becoming increasingly complex, IDB Invest has identified in its business plans a need to continue improving its backbone and information systems. Progress has been achieved in terms of digitalization, systems, data visualization and management (including improvements to the client experience, such as the client portal), and integration of key features in the MAESTRO system (e.g., advisory services, environmental and social action plans, and development effectiveness tools). In 2018, IDB Invest also implemented a time and labor system that reports time by outputs (Time Invest) to better monitor operation costs. Nevertheless, there is ample consensus among the staff from different areas interviewed and surveyed by OVE that the level of development of processes and systems has not kept pace with the growth of the institution and its complexity.[40] The need to revise and continue to improve processes and systems and, more generally, the institution's backbone, is a crucial challenge to increasing operational efficiency, developing closer relationships with clients, and scaling up business volume and products.

39 Personnel employed by the INO origination team (segments) increased from 60 officers (48 staff, 12 consultants) in late 2016 to 110 officers (81 staff, 29 consultants) in 2021. In contrast, PTM's workforce remained relatively stable over that period: 36 officers in 2016 (29 staff, 7 consultants) compared to 40 officers in 2021 (29 staff, 11 consultants).

40 For example, two thirds of the investment officers surveyed felt that existing operational processes are inadequate (26.8%) or partly adequate (39%). Half rate the existing information systems as inadequate (17.1%) or partly adequate (34.1%). While clients value IDB Invest's flexibility, the vast majority voiced negative opinions about operation processing times (55%) and contractual and information requirements (51%).

04

Strengthening Effectiveness and Additionality-Results

4.1 This chapter analyzes additionality and effectiveness results at the operation level. In keeping with the proposed scope of the evaluation, OVE analyzed the extent to which IDB Invest operations have offered elements of financial or nonfinancial additionality. OVE also analyzed the extent to which operations have achieved their proposed development objectives (or are on track to achieving them, in the case of operations in supervision).[41] OVE reviewed a random sample of 157 operations approved between 2016 and 2021, which amount to approximately one-third of the operations approved over that period. The documentary analysis of operations was complemented by client interviews.

A. Additionality

1. The concept of additionality: Implications and the challenges of operationalizing it

4.2 Additionality is a core element of the IDB Invest mission. Article III, Section 3(g) of the Agreement Establishing the Inter-American Investment Corporation states, *"[IDB Invest] shall not undertake any financing for which, in its opinion, sufficient capital could be obtained on adequate terms."* In broad terms, additionality is IDB Invest's unique contribution to a private investment project that is not offered by commercial financing sources. A core element of the concept is that IDB Invest adds value without crowding out private-sector activity. In other words, IDB Invest should guard against the risk that its interventions could end up financing projects that could be financed by the private sector under adequate terms.

4.3 The concept of additionality has evolved over time, and the MDBs have developed harmonized frameworks and guidelines for defining and measuring additionality. Since the IFC first began using the concept of additionality in the late 1950s, the concept has been adjusted to reflect a new reality in which financial and nonfinancial contributions exist side by side. As certain countries deepened their financial markets, nonfinancial additionality has taken on a more prominent role, since commercial sources are hard-pressed to offer the standards, reputational brand, and advisory support associated with MDB operations. As a result of those changes, in 2018 the MDBs (including IDB Invest) agreed on a harmonized framework for defining and analyzing additionality.[42] According to that harmonized framework, the concept of additionality means that *"interventions by*

41 Though the Impact Management Framework has shown tangible progress (Chapter II), that framework does not guarantee that the organization or its operations will make an impact. For that reason, this chapter analyzes and reports on the effectiveness of operations during the evaluation period separately from the previous discussion of the Impact Management Framework tools.

42 Multilateral Development Banks, "Multilateral Development Banks' Harmonized Framework for Additionality in Private Sector Operations," 2018.

MDBs to support private-sector operations should make a contribution beyond what is available in the market and should not crowd out the private sector." Most MDBs have adopted this approach, though some differences in interpretation arise when putting the concept into practice. The framework also addresses the concepts of financial and non-financial additionality and includes a guide for how to analyze them. In the case of IDB Invest, Management and OVE have also followed the guides prepared by the Evaluation Cooperation Group (ECG)[43] to analyze and rate operation additionality in the XSRs. Given how the concept and its sources have changed, operationalizing additionality also faces significant challenges due to the difficulty of measuring counterfactuals and the risk of crowding out commercial sources (Box 4.1).

Box 4.1. Challenges to operationalizing the concept of additionality

Operationalizing the concept of financial additionality is particularly challenging for a number of reasons. Inherent to the concept of additionality is the need for a counterfactual (what would have happened if the MDB did not intervene?). Formulating this counterfactual is, in itself, a challenging task because there is hardly ever strong evidence of what would have happened had the MDB not intervened. Furthermore, it is not always clear which counterfactual is acceptable for preventing private sector crowd-out. XSR evaluation guides identify two acceptable counterfactuals: (1) the IDB Invest-financed project would not have moved forward without the intervention; and (2) the project would have moved forward, but with suboptimal terms (e.g., unreasonable terms or an unacceptable distribution of risks).

The concept of nonfinancial additionality involves its own unique challenges. In this case, the biggest challenge is that nonfinancial additionality can be an important consideration when justifying an intervention even when its financial additionality is minimal, because nonfinancial additionality offers unique features that are not available from commercial sources. The most common cases identified by OVE in its review of projects was that IDB Invest helped improved project development outcomes through significantly higher environmental and social standards than the client would have achieved if it had used its own resources, or IDB Invest provided some sort of advisory services that significantly reduced nonfinancial risk (e.g., corporate governance risk).

Source: OVE.

4.4 Though IDB Invest developed internal guidelines for assessing an operation's additionality, the institution is lacking a particular strategic framework, shared widely among its various stakeholders, that helps operationalize additionality while fostering a common understanding across all parties. IDB Invest has operationalized the concept of additionality through the DELTA and its associated guidelines, but the institution does not have a consolidated framework that can foster among all stakeholders, including the Board of Executive Directors, a common understanding regarding what the concept of additionality means and how it is analyzed

43 ECG Big Book on Good Practice Standards, November 2012.

and operationalized and that can facilitate a discussion of strategic issues, including acceptable levels of additionality and the types of justification or evidence needed to demonstrate it.[44] Executive Directors interviewed by OVE said the concept was not very clear and stressed the need to better justify the additionality of the operations presented for approval. Executive Directors also expressed different expectations for operation additionality, including varying acceptable minimums. Other MDBs have developed frameworks or guidelines that specifically address how additionality is operationalized. For example, in 2018 the IFC developed a new additionality framework as part of a larger institutional reform (IFC 3.0) to define and discuss additionality more rigorously and more systematically and to align itself with the harmonization with other MDBs. Another example is the EBRD, which developed its "Enhanced Approach to Additionality" in 2019 to better incorporate its analysis of sources of financial and nonfinancial additionality.

4.5 In addition, IDB Invest's ability to offer additionality depends on other factors, such as its internal capacity and financial resources. The ability to offer additionality does not depend solely on IDB Invest selecting clients and projects that require financial conditions that are not available on the market. It also depends on other factors, including the availability of capital, the processes and systems in place, operating capacity, and human resources, as OVE found in its analysis of financial instruments and advisory services for this evaluation. Like other MDBs, IDB Invest contends with financial constraints that largely determine the type of client with which it can work and the type of additionality it can offer. IDB Invest must maintain a minimum risk rating ("AA"). This means that IDB Invest has to ensure that the underlying risk of its portfolio of investments is at least "B+," which it has taken care to maintain during the evaluation period. Furthermore, to ensure operational efficiency, the average size of long-term operations during the evaluation period was US$34 million. This means that part of IDB Invest's work has been with large companies from the region that already had some sort of access to the financial system. In those cases, the additionality approach consisted mainly of offering better financing terms than those available on the market (mostly longer tenors). Consequently, the counterfactual most commonly used to justify interventions was that projects would have moved forward with suboptimal conditions without IDB Invest support.

44 The impact management framework includes internal guidelines for the DELTA that address the categories of financial and nonfinancial additionality included in the tool and the evaluation criteria used by the DVF.

2. Strategic management of additionality at IDB Invest

4.6 As at other MDBs, the concept of additionality at IDB Invest has been focused mainly on the operation level, with limited attention being paid to the concept and its analysis at more strategic levels. A review of strategic and corporate documents, including business plans, action plans, and country strategies, shows that the attention given to the concept of additionality is quite limited. In practice, the concept has been operationalized mainly on an operation-by-operation basis through the DELTA. The experience of other MDBs has shown the consequences of addressing additionality mainly at the operation level. One ramification of this approach is that the institution may be missing out on opportunities to achieve more additionality at the country, client, sector, and instrument levels, as well as the additionality achieved through sequential or complementary interventions. IDB Invest, like other MDBs, has practically no aggregate-level reporting or analysis of additionality.

4.7 OVE found that there was no systematic effort to take advantage of the opportunities to manage additionality through country strategies, despite the fact that additionality depends greatly on the terms offered by each country's financial market. In its review of country strategies, OVE found that country strategies do not address what the role of the organization would be (or the additionality it intended to offer) in each country. Addressing this point could help manage expectations regarding what IDB Invest can realistically offer and facilitate deliberations and operation approval. OVE did not find any proposed approaches to financial or nonfinancial additionality in the country strategies.

4.8 The operation-level focus also held back management of additionality at the client level, even with repeat clients and despite the intention to build longer lasting relationships with those clients. IDB Invest has developed long-term relationships with strategic clients at the regional level, including major banks and infrastructure project sponsors, and has conducted several transactions with them. Even so, additionality was analyzed and discussed at the level of the individual operation. OVE did not find evidence that IDB Invest documented progress at the client level, taking into account the fact that additionality evolves as clients and their specific circumstances change.

3. Additionality results

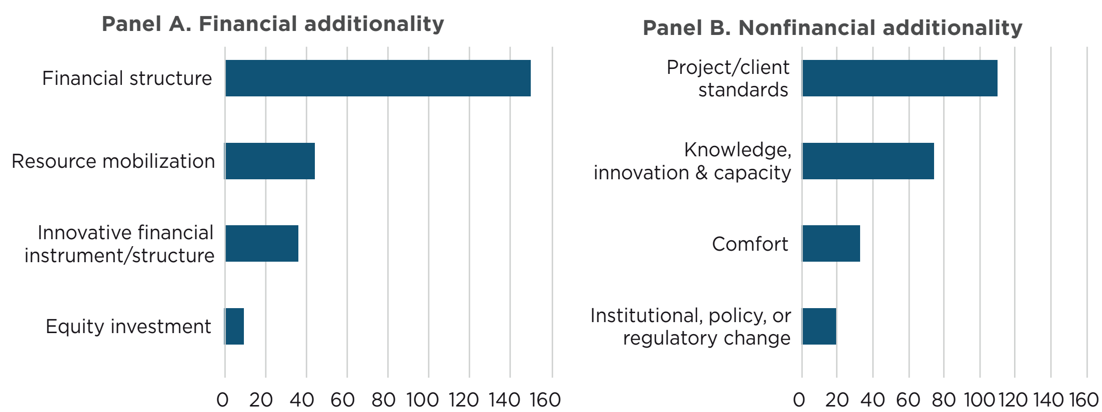
4.9 In its review, OVE ran up against a series of challenges when it attempted to identify and measure additionality in investment proposals. Most proposals systematically discussed the terms available on the market. From a financial additionality perspective, however, the proposals did not clearly, systematically explain why the intervention was necessary for the project in question (e.g., because the project required better financial terms to prevent the risk of the project being carried out with a suboptimal scale or scope). Furthermore, investment proposals did not always systematically provide reasons and evidence to prove that the operation would not be crowding out the market. As for nonfinancial additionality, OVE also did not find evidence that systematically justified whether the advisory services offered by IDB Invest were necessary to achieving the development objectives. The greatest challenge was identifying, based on documentary information, if IDB Invest's contribution was material to achieving the expected outcomes (e.g., better standards or capacity-building).

4.10 The most commonly identified type of financial additionality was associated with improvements to the operation's financing structure.[45] In 150 approved projects (96% of the sample), IDB Invest used the financing structure as the grounds for financial additionality (Figure 4.1). Within that dimension, the main reasons provided were longer tenors (81% of projects), amounts not available (39%), longer grace periods (24%), and currency (23%).

Figure 4.1

Types of additionality found in approved projects

Source: OVE, based on its documentary analysis of operations.



4.11 The most common type of nonfinancial additionality was better project or client standards. With respect to nonfinancial additionality, in 110 projects (70% of the sample), IDB Invest pointed up improvements to project standards, especially in the environmental and social areas.

4.12 Looking at the additionality performance of operations whose implementation is further along, 88% had elements of additionality. OVE also analyzed the additionality performance of operations that are at a more advanced stage of implementation. The project additionality rating takes into account the criteria agreed upon by OVE and Management for evaluation of the XSRs and is based on the evaluation of a counterfactual addressing how the project

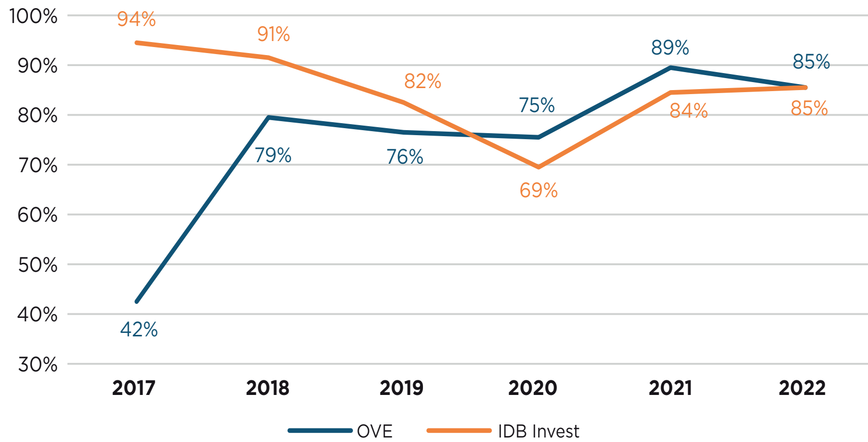
45 OVE reviewed documents from the sample of 157 operations approved from 2016 to 2021 to determine how the operations' additionality was justified. It then classified and tabulated the justifications by the various additionality categories following the definitions set out in the MDBs' harmonized framework.

would (or would not have) proceeded without IDB Invest support. This result is in line with the results of OVE-validated XSRs (Figure 4.2) and reflects the variety of potential sources of financial and nonfinancial additionality as well as the diverse paths to achieving additionality in projects (Box 4.2).

Figure 4.2

XSRs with positive additionality ratings

Source: OVE.



Box 4.2. Examples of projects by additionality rating[a]

Projects with "excellent" additionality ratings

Wind Farm in Argentina. Approved in 2018, this project consisted of the construction, operation, and maintenance of a wind farm with a capacity of 126 MW and associated facilities located in the province of Santa Cruz, Argentina. The general project objective was to contribute to the diversification and the sustainability of the country's energy generation capacity. IDB Invest provided long-term financing (US$50 million for up to 15 years), which otherwise would not have been available at the time due to the macroeconomic conditions for obtaining long-term loans in Argentina. The project was attached to a series of interventions that financed much of the expansion of nonconventional renewable energy in Argentina (the RenovAr program). IDB Invest mobilized US$50 million from KfW IPEX-Bank and the Danish Export Credit Agency (EKF) to complete the financing. Though this was a dollar-denominated loan, the client mitigated exchange risk by pegging power purchase agreements (PPAs) to the dollar. The IDB Group also played a key role in improving the long-term sustainability of the contractual framework and the project's environmental and social standards. The counterfactual scenario for this case was that it is unlikely that the project (a wind farm) would have proceeded without IDB Invest's support at that time.

Bank in Paraguay: This operation was approved in August 2017. Its objective was to finance SMEs in Paraguay's production sector through medium- and long-term loans. Under the operation, IDB Invest extended long-term financing in guaraníes (local currency) to the bank. The client was a niche bank that held a <4% share of the Paraguayan loan market. The transaction helped the bank better match its assets and liabilities. IDB Invest's hypothesis was that a better match between assets and liabilities would facilitate the conditions needed for the client to increase the amount and tenor of loans to the SME segment. It would also reduce currency mismatches in a context where local banks struggle to access long-term financing.

Projects with "satisfactory" additionality ratings:

Energy utility in South America: Approved in 2020, this operation consisted of the creation of a US$80-million facility under which IDB Invest could purchase accounts receivable from the country's fourth largest integrated energy utility, to finance vulnerable energy users and provide liquidity to the utility during the pandemic. Though the company, because of its size, had access to several commercial financing lines that had similar terms, it took the IDB Invest financing to diversify its funding sources during the pandemic. The transaction also included the mobilization of US$16 million in third-party resources. The risk of crowding out commercial sources was mitigated by the fact that the total financing amounted to just 8% of the utility's working capital and supported the diversification of its funding sources. The counterfactual scenario for this case was that the utility probably would have continued to finance its clients and would have obtained commercial financing with similar terms, but IDB Invest helped mitigate the risk of disruption and provided the conditions to allow greater flexibility in the terms of payment for end beneficiaries.

Projects with "partly satisfactory" or "unsatisfactory" ratings

Bank in Argentina: The transaction entailed an unsecured dollar-denominated senior loan for up to US$40 million. The transaction was approved in 2017, and its objective was to increase access to financing for SMEs in Argentina with a specific focus on the Mendoza region. The operation also offered a financing tenor (five years) that the bank could not obtain from its market. Even so, OVE determined that, since this was a dollar-denominated transaction and given the volatility of the exchange rate in Argentina, the transaction resulted in a significant currency mismatch between the IDB Group's dollar-denominated financing and the client's peso-denominated portfolio. Furthermore, the Central Bank of Argentina issued regulations under which commercial banks were no longer allowed to issue dollar-denominated loans, which limited the client's use of the line considerably. Due to all of the above, even though IDB Invest offered financing that was not available on the market, the client could not make the best use of that additionality because it created a mismatch of tenors, so the line did not reach end beneficiaries.

Manufacturing company in Mexico: The objective of this transaction was to provide up to Mex$1 billion in financing to the company's supply chain (consisting mainly of SMEs) through a reverse factoring program. The objective of the revolving line was to provide competitive financing (especially in terms of prices) to SMEs in the company's supply chain, which usually have less access to affordable financing from the financial system. In this case, the project's financial additionality was unsatisfactory primarily because the company is a global leader with access to several working capital lines. The company was also already involved in a number of reverse factoring programs offered by institutions like Nacional Financiera. OVE's analysis verified that, had IDB Invest not gotten involved, the client's reverse factoring program would have continued as usual and would still have included SME clients, because the company had access to multiple reverse factoring working capital lines. The counterfactual scenario for this case is that the client would have developed its reverse factoring program and likely would have achieved the development outcomes even without the IDB Invest intervention.

Source: OVE, based on its documentary analysis of operations and interviews. *Note*: [a]Rating based on OVE's documentary analysis and interviews. The rating assesses additionality at the time of OVE's review, so it does not necessarily coincide with the rating assigned at the time of approval.

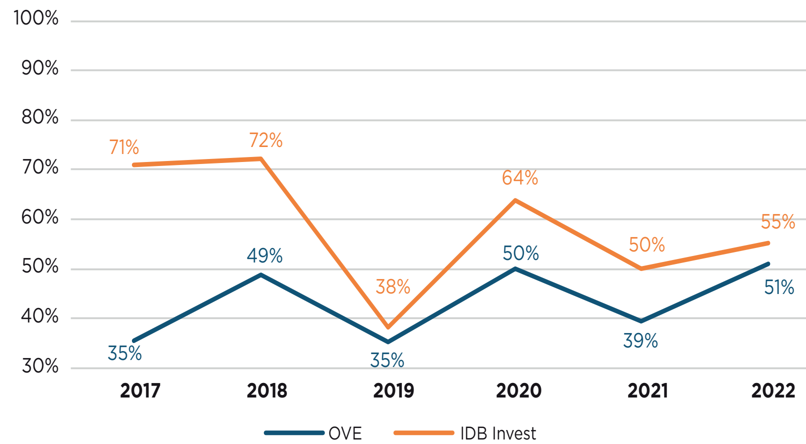
B. Effectiveness

4.13 The XSRs for 47% of the projects validated by OVE from 2017 to 2022 reported positive effectiveness ratings ("satisfactory" or "excellent"). Significantly, the ratings on Management's self-evaluations have been converging with the ratings on OVE's validations in recent years, with OVE's validations trending slightly upward.[46] Although the ratings on all of the XSR's core assessment criteria (relevance, effectiveness, efficiency, and sustainability) converged, effectiveness and efficiency continue to be the XSR categories that report the lowest average ratings, adversely affecting overall operation performance.

Figure 4.3

XSRs with positive effectiveness ratings

Source: OVE.



4.14 Looking at the analysis of the project sample,[47] operations in the financial institutions segment reported the weakest performance in terms of effectiveness. Four of the five projects with "unsatisfactory" effectiveness ratings were from the financial institutions segment. The exception was a transportation project that did not achieve its objectives for road safety, connectivity, and mitigation of environmental impacts. The project was also the continuation of a legacy project from the SCF. A recurring issue in three of the four projects under the financial institutions segment was a failure to help achieve the expected increase in the SME portfolio, while the fourth project did not achieve targets related to promoting mortgage loans. As for the five projects rated "partly unsatisfactory," three were from the infrastructure segment and two from the corporate segment. Of those, two energy projects achieved only some of the expected targets for renewable energy generation and CO_2 reduction between the time they became fully operational until their evaluation in 2020. Other objectives not achieved under the two corporate projects and one infrastructure project consisted of not meeting targets for employment and productivity.

4.15 The main drivers of this underperformance in operation effectiveness were related to macroeconomic developments and to certain issues with design or definition of indicators. Of the 10 projects with low effectiveness ratings, four were adversely

46 Data from 2017 is not fully comparable due to a methodological change made in 2018.

47 As part of the project sample, OVE analyzed 27 operations that had validated XSRs. In all, 63% of those 27 operations had effectiveness ratings of "satisfactory" or better.

affected by macroeconomic issues or market conditions.[48] The operations in the financial institutions segment that received "unsatisfactory" ratings reported issues during supervision even before they reached early operational maturity (EOM), especially in the area of business performance. Seven projects had poorly defined indicators or targets.[49] The energy operations struggled with delays and technical design issues. The pandemic was not a driver of the poor performance in nine out of the ten projects. It only partially affected one infrastructure project, but the impact was mitigated by the involvement of a strategic sponsor. Meanwhile, projects with good effectiveness ratings identified lessons learned related to the importance of client selection, risk mitigation and design, and effective supervision.

4.16 Though most operations at the supervision stage analyzed by OVE are proceeding as expected, approximately one-third show signs that their development objectives may be difficult to achieve. Of the 78 operations in the sample analyzed by OVE that are currently in implementation, 64% received "satisfactory" ratings (in line with the portfolio-level evidence), whereas 29% received "alert" or "problem" ratings, mainly due to external factors. Another 9% reported evaluability issues, including a lack of information or ambiguous data.[50] Of the 19 operations that received an "alert" rating, OVE found that eight (42%) had at least one monitoring action to accomplish before the next supervision. In three transactions, closer supervision of the associated technical cooperation operations was recommended. In another three, the recommended action was monitoring of underperforming impact indicators. Lastly, in the remaining two, monitoring actions in specific areas (e.g., training program to support the staff) had been proposed. As for the 11 operations that had no proposed monitoring actions, OVE found that the "alert" rating assigned to 10 operations could be attributed to exogenous factors, including political crises, macroeconomic conditions, and the pandemic. In two others, no concrete actions had been proposed. Lastly, one of the four operations that received a "problem" rating was transferred to the Special Assets Division. The remaining three reported that exogenous problems, such as the COVID 19 pandemic, prevented them from achieving their midterm targets.

48 While macroeconomic risks can be difficult to predict, lessons learned from several operations stressed the importance of taking into account the country context as part of the analysis of the potential financial, macroeconomic, and political risks during operation design.

49 For example, one agriculture project did not achieve its employment objective (35% of the target), possibly because the workforce was replaced by technology or because IDB Invest set a target that was too ambitious.

50 These are projects in which IDB Invest has performed supervision in some way. In another 51 operations in the sample, no supervision actions had been carried out at the time of analysis due to the projects' implementation status.

05

Maximizing Synergies Between the Public and Private Sectors

5.1 This chapter explores developments related to public-private coordination, with a focus on the mechanisms instituted over the years to promote synergies within the IDB Group. As an acknowledgment of the inherent difficulties involved in the consolidation of the various private-sector windows in the IIC, the Renewed Vision identified the importance of public-private synergies as one of its core objectives. IDB Invest also recognizes that these synergies are a feature that sets the institution's value proposition apart.

5.2 IDB Invest has made important efforts to promote alignment and collaboration with the rest of the IDB Group at the strategic level. In 2019, the most recent update of the Institutional Strategy (2020-2023) (document GN-2933-1) was the first to be jointly developed by the IDB, IDB Invest, and IDB Lab in a bid to leverage the IDB Group's resources. IDB Invest aligned the design of its 2020-2022 Business Plan with the objectives of the Institutional Strategy and the Renewed Vision, which establishes IDB Invest's long-term strategic framework. IDB Invest also adjusted its measurement tools (e.g., DELTA) to report progress toward the IDB Group's strategic objectives.[51] IDB Invest has been increasingly involved in other IDB Group strategies. Notably, it played an important role in designing the Climate Change and Gender and Diversity strategies. IDB Group staff respondents pointed up improvements in terms of collaboration and communication at the managerial level, though the process was not tension-free under the previous Bank Management.

5.3 Strides have been made to ensure that IDB Invest's involvement in the development of country strategies is more systematic, though use of this tool to guide origination efforts continues to be a challenge. Gradually, IDB Invest's involvement in the development of country strategies has become more active and more systematic, and the institution has gotten involved in the process at an earlier stage through inputs for the country development challenges. IDB Invest's strategy department (DSP)[52] has spearheaded this effort, with inputs from other offices. In general, the Country Representatives appreciated that IDB Invest was getting involved in the process earlier and taking a more active role. They also stressed the importance of country strategies as a touchstone for aligning

51 All told, 16 of the 29 indicators (Level 3) set out in the Corporate Results Framework break down the specific contribution to be made by IDB Invest, including projects supporting gender equality, projects supporting diversity, climate finance, and projects aligned to country strategies. Ten other indicators are reported at the IDB Group level (e.g., direct and indirect third-party financing deployed).

52 After the merge-out, this work was led by the Strategy and Development Department's Public-Private Synergies Division, the coordination mechanism envisioned in the Renewed Vision. That centralized office was disbanded in 2019. Its duties, which included coordination of inputs for IDB Group strategies, were consolidated under the strategic planning team, thereby establishing what is now the Planning and Knowledge Division.

IDB Invest's work, given the strong emphasis the institution has placed on origination since its inception. At the same time, several Representatives made the point that the country strategies are ultimately negotiated with the governments (and therefore place greater emphasis on public-sector issues) and underscored the importance of the dialogue that took place afterward through the programming exercise. INO staff interviewed had a more critical opinion regarding whether country strategies were a useful guide for origination, as they found the tool to be static whereas the private sector was constantly evolving. From that perspective, there are opportunities for IDB Invest to become more involved in the IDB's ongoing dialogue with the governments, especially during country strategy implementation, so as to continuously inform the operation origination and selection process. Meanwhile, even though IDB Invest has participated in the development of some sector framework documents (SFDs), its involvement to date has been limited and less systematic than its involvement in the country strategy process.

5.4 The expansion of the Country Representative role to make representatives accountable for the IDB Group's public and private-sector windows is a pivotal step forward for the identification and promotion of public-private synergies at the country level. In its 2017 midterm review of the implementation to date of the merge-out, OVE noted that the decision to expand the IDB's Country Representatives' role in relation to their private-sector responsibilities was an important step. At the same time, OVE recognized that the degree to which Country Representatives would be able to effectively perform their expanded role would largely depend on whether they had clearly defined responsibilities and reporting lines, as well as incentives and adequate training for their new responsibilities. IDB Group respondents repeatedly pointed up the importance of this role and its potential for promoting public-private synergies at the country level, given its proximity to governments and IDB Group clients in the region.

5.5 Nevertheless, there are constraints on the effectiveness of this expanded role, arising in part from the Representative selection process. IDB Invest respondents consistently pointed out that Country Representatives' involvement and effectiveness in private-sector business varies widely and depends on the Representative in question and their background. Country Representatives predominantly come from the public sector, and their previous experience is mainly in that sector. Staff respondents largely attribute this to the lack of competitive, merit-based processes for the selection of Country Representatives, an issue that was also recently identified by OVE in its evaluation of the IDB's governance (document RE- 553-1).[53] Furthermore, IDB Invest's involvement in the candidate identification and selection process has been very limited. Bearing in mind how much Representatives' backgrounds and experience with the private sector vary, the IDB Group, with the active involvement of IDB Invest, has undertaken a series of measures to provide Representatives with a base level of training, mainly since 2019 (e.g., IDB Academy).

5.6 In this context, clearly defining Representatives' role and responsibilities with regard to the private sector is a pending challenge. A profile for the position of Country Representative was developed in 2021. In general terms, that profile states that the Country Representative leads the activities of all of the IDB Group's windows, and familiarity with the Bank's public- and private-sector instruments is included under the technical expertise required for the position. The vast majority of Representative respondents indicated that their private-sector responsibilities were not clearly defined and said they were not familiar with the terms of reference for the position. From its interviews with Representatives, OVE found that their understanding of their private-sector duties varied, with some believing their role to be limited to giving their no objection to operations for integrity reasons, while others viewed the position as having a more active role in the operation identification and origination process.

5.7 Moreover, these new responsibilities have not been supported by a clear accountability. Country Representatives are IDB employees who report directly to the Regional Managers, who in turn report to the Vice Presidency for Countries (VPC). There are no clear criteria for evaluating the Representatives' performance with regard to their private-sector duties, and IDB Invest is not formally involved in this process. The vast majority of Representatives interviewed said the criteria for evaluating their private-sector activities were not well defined, they did not have any objectives or targets for their private-sector work (beyond some pertaining to general issues, like mobilization and partnerships), and they did not know if IDB Invest was involved in the process. As OVE indicated in 2017, only when Country Representatives' terms of reference are fully incorporated into the performance evaluation system will Country Representatives have a complete picture of what it means, in practical terms, to have the authority and responsibility to represent IDB Invest and have the formal incentives to deliver.[54]

53 The evaluation drew attention to concerns expressed by Managers and members of the Board of Executive Directors about the lack of competitive, merit-based processes for the selection of nonexecutive managers, including Country Representatives, implying that these selections were made solely at the discretion of the President of the Bank.

54 In 2022, VPC, in coordination with the Human Resources Department, engaged a specialized firm to analyze and make recommendations to support issues related to the Country Representative position, including: development of a selection process; updating of the position's profile, responsibilities, and required competencies; and

5.8 Representatives also stressed the need for more training and communication to empower them to perform their IDB-Invest-related duties. Approximately one-third of the Representatives interviewed spoke of IDB Invest's transactional focus and the importance of getting more involved and deepening their understanding of IDB Invest activities in their countries, especially during origination, before the transactions reached them for their no objection. They also repeatedly expressed interest in having additional information on operation implementation and, more generally, a more complete picture of IDB Invest's work. While they appreciate the training initiatives, most Representatives said training needed to be continuous and customized. The training topics that Representatives say are critical to making their work more effective varied, reflecting the diversity of their backgrounds and their experience with private-sector issues and with IDB Invest in particular. The most commonly mentioned topics included: IDB Invest's structure, procedures, and organization; financial instruments; financial concepts, and concepts related to portfolio and risk management.

5.9 The regional SG-NSG coordinator role is still in the development process. Four positions were created in the IDB Invest Strategy Department with a second reporting line to the VPC Regional Managers in the interest of facilitating public-private synergies and interactions with operation teams. IDB Group staff respondents expressed different understandings of this role and its value-added. Regional Managers and some Country Representatives felt that the position was useful, mainly to keep information flowing and to support Representatives. In contrast, the vast majority of INO Chiefs said they were not familiar with the role or if it was worthwhile. After an internal IDB Invest diagnostic assessment in 2022, the decision was made to keep these positions. The terms of reference for the selection of new coordinators were updated to strengthen the role's value proposition, and new reporting and coordination channels with IDB Invest were added.

5.10 A series of steps have been taken to promote coordination at the operation level. In its documentary analysis, OVE found that approximately one-fifth of operations (21%) involved some sort of explicit coordination across the IDB Group's different windows, mainly by including specialists on the project team or through groundwork done by the IDB (e.g., reforms or regulations) or IDB Lab (support for early stages).[55] Broken down by segment, infrastructure and energy operations were the most likely to

identification of training and portfolio development needs.

55 OVE's recent evaluation of IDB Lab (2021) pointed up an increase of IDB Lab project teams that had team members from IDB Invest and a series of joint IDB Invest-IDB Lab initiatives (e.g., Rethink Plastics, Beyond Tourism Challenge). For more information, see "Evaluation of IDB Lab: Strategic Relevance" (document MIF-RE-5-6).

involve some sort of coordination (38%), followed by the financial institutions segment (30%) and the corporate segment (18%), which largely reflects the extent to which the public and private sectors overlap in these areas. Staff respondents spoke of the challenges posed by measuring coordination at the IDB Group level and stressed the importance of looking for opportunities for coordination early and often. In addition, IDB invest is participating in a series of initiatives and working groups at the IDB Group level, notably the the single window for PPPs (Box 5.1), financial inclusion, and thematic bonds.

Box 5.1. The experience of the PPP Single Window

PPPs are long-term contracts between a government agency and a private party to deliver a public service or asset, under which the private party assumes significant risk and responsibility for managing the asset. Remuneration is linked to performance. PPPs are an important tool that can help solve problems traditionally associated with the delivery of public infrastructure in the region, as well as a natural area for potential coordination between the public and private solutions offered by the IDB Group.

An evaluation of PPPs in infrastructure prepared by OVE in 2017 (document CII/RE-24-3) pointed up the IDB Group's active role in the PPP space over the 2016-2015 period, particularly in project financing. It also identified a series of issues that are holding back the effectiveness of this support, notably a lack of coordination across the various IDB Group offices working in this area. One indicator of this issue is the dispersion of efforts across the IDB Group with no point person to facilitate decision-making and share lessons learned. Several reforms were undertaken in response to OVE’s recommendations, including the creation of a single window for PPPs attached to the VPC. Notably, all recommendations from that evaluation have been implemented satisfactorily according to OVE’s monitoring.

Since its creation, the single window for PPPs has tackled a series of important actions. The single window has supported more than 30 PPP projects in the preparation and structuring stages and has provided upstream support to 15 countries in the region. Other major initiatives implemented by the single window for PPPs include the creation of consolidated PPP profiles for the 26 borrowing member countries of the IDB and a series of knowledge products (e.g., Infrascope) and dissemination activities.

IDB Invest and IDB personnel interviewed by OVE spoke of how PPP coordination had changed for the better despite some challenges early on, which mostly stemmed from the overlapping of efforts carried out by the IDB Group’s various windows. Under its advisory services division (ADV), IDB Invest has an office specializing in PPPs, whose core work early on was financing preinvestment studies and structuring PPP projects. Most of these projects, however, evolve out of public-sector initiatives in the countries, so there was a lack of coordination and duplication of efforts with the same sort of activities performed by the single window for PPPs, thereby limiting the effectiveness of the IDB Group's support. As part of the recent restructuring of the DSP in 2021, when ADV was transferred from INO to DSP, IDB Invest reconfigured its PPP unit and narrowed its role to make sure its functions do not overlap with the single window for PPPs. At present, IDB Invest personnel hold regular meetings with the single window for PPPs, offering their private-sector-specific expertise. The single window for PPPs is currently being overhauled for a potential institutional redesign, which could involve lines of reporting to IDB Invest. Pending challenges include further clarifying the roles and responsibilities of the various offices working on PPP issues within the IDB Group, including VPS, and developing the best possible structure for managing the various IDB Group resources earmarked for this purpose.

Source: OVE.

5.11 On the whole, the progress made in terms of coordination at the IDB Group level is viewed favorably. There is still room to improve, however, as this coordination is not yet entirely effective. IDB Group personnel interviewed and surveyed by OVE spoke of the gains achieved in terms of collaboration and coordination. One development that has facilitated this coordination is IDB Invest's expanded presence in the region. The pandemic also produced a need for greater coordination at the operation level, with the efforts in social and tourism sectors meriting particular attention. Nevertheless, the vast majority of personnel interviewed and surveyed also mentioned that this coordination is still far from being effective and pointed out a need to continue strengthening coordination mechanisms and forums.

5.12 The general consensus was that coordination was an ad hoc process that has not been institutionalized. IDB Group Representatives, chiefs, and managers consistently reported that coordination depended greatly on the individuals in charge and said there were no incentives in place to foster synergies. OVE confirmed that there are channels for communication between managers and chiefs at the sector level in sectors where coordination is essential (e.g., infrastructure, financial markets), including meetings for reviewing operations in the pipeline and discussing potential opportunities for collaboration. However, these efforts exist due to the initiative of the individuals in charge, not because there are institutional arrangements or incentives to promote them. IDB Group investment officers and team leader surveyed indicated a lack of effective incentives and institutionalized processes and mechanisms to promote the systematic identification of opportunities for collaboration.

5.13 Given this situation, there is significant room to enhance coordination at the IDB Group level. The differences in culture, institutional mandates, and objectives and priorities among the IDB Group's windows impose limits on potential opportunities and forums for coordination. Nevertheless, there are a series of opportunities to improve collaboration, including the systematic identification of potential opportunities for collaboration, the clarification of the various windows' roles and the timing and scope of their interventions, and a more coordinated planning process at the operation and knowledge levels.

5.14 At the corporate level, notable progress has been made in terms of standardizing service-level agreements (SLAs). As of December 2021, IDB Invest had signed 23 SLAs for efficiency gains and cost savings. IDB Invest receives services from 20 Bank departments (e.g., the Knowledge, Innovation, and Communication Sector (KIC); the Office of Outreach and Partnerships (ORP); the Human Resources Department (HRD); OVE; and VPC) and provides a series of services to IDB Lab in such areas as environmental and social risk management, development effectiveness, and legal. An analysis of SLAs performed by the Office of the Executive Auditor (AUG) in 2019 identified a series of recommendations to improve SLA governance and rules, costing methodologies, and processes. The IDB Group implemented all of the recommendations from that audit.

06

Efficient Use of Resources and Ensuring Long-term Financial Sustainability

6.1 This chapter analyzes how the institution has implemented its financial sustainability mandate. The chapter takes stock of the results achieved by IDB Invest in three core areas relating to its financial sustainability: (i) capital adequacy; (ii) internal capital generation (returns); and (iii) its portfolio's credit performance. A fourth section explores how the institution's financial analysis and planning tools have evolved. For a more detailed discussion of the analysis performed, see the Background Note on Financial Sustainability (Annex VI).

A. Capital adequacy and monitoring of the capitalization process

6.2 The IDB Invest capitalization process has received resounding support from its shareholders and has progressed with no major delays. After the first six years, capital contributions have been made on-time, and some countries have even made their contributions early. As of year-end 2021, 91.5% (US$1.151 billion) of the first six subscription installments had been made. The few delays that have occurred were due to isolated issues affecting certain member countries. Capital transfers made by the IDB on behalf of its member countries have also been processed in a timely fashion (US$356.5 million by year-end 2021).

6.3 During the first few years of the evaluation period (2016-2019), capitalization levels were ample and even exceeded the amount required for the level of operations at that time. The ratio of available capital to capital employed exceeded 200%[56] in the first four years of operations (2016-2019). This ample capital level was largely driven by contributions from member countries outpacing IDB Invest's capacity to generate business at that time. Moreover, those first few years were also characterized by heavy use of the cross-booking mechanism, with a high rate of operations booked on the IDB's NSG balance sheet (see Annex VI, Box B.1). Over the 2016-2018 period, 72% (US$5.303 billion) of total IDB Invest commitments were booked on the IDB balance sheet.[57]

6.4 More recently, capitalization levels have settled near the prudential limits. The more intensive use of capital in recent years is the result of IDB Invest stepping up the pace of operation development, leveraging the efforts of previous years, and the greater volume of business under the pandemic response. Though the ample capital levels of the first few years entailed an opportunity cost

56 The Capital Adequacy Policy sets a series of different thresholds based on the capital adequacy ratio (CAR). The "green zone" is set at CAR≥130%, the "close monitoring zone" is 130%>CAR≥110%, the "buffer zone" is 110%>CAR≥100%, and the "non-compliance zone" is CAR<100%.

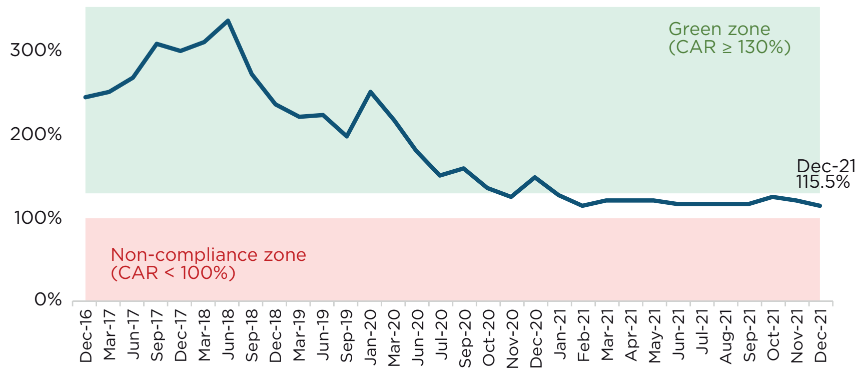
57 The Busan projections (audiovisual presentation CII/PP-149) called for the cross-booking of US$8.5 billion in approvals, 60% of which was to take place in the first three years.

in terms of lower capital accumulation (from lower revenues), the accumulated excess of capital equipped IDB Invest to mount a major response to the pandemic crisis, increasing its business volume 47% year-on-year during the crisis, from US$4.188 billion committed in 2019 to US$6.154 billion in 2020.

Figure 6.1

Capital adequacy ratio

Source: OVE, based on data from Analitika and from document CII/GN 426-14



6.5 As capital has become scarcer, IDB Invest has taken measures to optimize its use, and its efforts to that end continue. For example, in 2018 IDB Invest began to build partnerships with insurance companies to use credit insurance (Unfunded Credit Protection, UCP).[58] Through these contracts, IDB Invest funds 100% of its operations, taking advantage of its competitive resource costs, but exchanges part of the credit risk. This has yielded at least three benefits: it frees up capital up to the amount insured; the insured party deducts a portion of the margins and fees; and it addresses the resource mobilization mandate, since insurance company guarantees are channeled to clients and projects. Yet this vehicle also has its limitations. As the tool has been put to more frequent use, concentration risks with insurance companies have risen (Annex VI, Box 4.2). It is important to clarify that IDB Invest applies its exposure limits to these insurance companies and typically works with investment-grade institutions, which gives it leeway to have higher concentration levels.

1. IDB Invest capital management

6.6 With a large inflow of new capital contributions and a more ambitious mandate, IDB Invest developed its capital and risk management framework in 2017. Under that framework, IDB Invest operationalized its mandate of aiming to maintain a credit rating of "AA" or better. Through that framework, it created a Capital Adequacy Policy, with which it developed a capital management tool as well as a capital adequacy indicator

58 More recently, IDB Invest has begun using unfunded risk participation (URP) as well. This instrument is similar to UCP but differs in that the counterparty that insures the risk is not an insurance agency (as is the case with UCP) but rather a financial institution. IDB Invest is also working on other initiatives to support portfolio management, including activation of the Active Portfolio Management Committee and involvement in several forums for analyzing solutions for more efficient capital management (e.g., the G20's Independent Review of MDBs' Capital Adequacy).

to monitor and manage its solvency. Due to the mandate of maintaining an external risk rating, that model's calculations do not just factor in internal models, but rating agencies' capital requirement methodologies as well. To that effect, the IDB Invest capital adequacy indicator uses the most conservative capital adequacy ratio coming out of its internal capital allocation model or the various rating agencies' methodologies, which tend to be less granular than the internal model.

6.7 However, application of the rating agencies' methodologies results in significantly higher capital requirements, calling for 67% more capital, on average, than IDB Invest's internal model in 2021. In practice, IDB Invest's capital requirements have been determined by rating agencies' metrics, not its internal model, because the institution has to comply with the more conservative criteria. While the rating agencies' metrics (Table 6.1) yielded capital adequacy ratios ranging from 115% to 138%, the IDB Invest model yielded a capital adequacy ratio of 182%. In 2021, Fitch's metrics determined IDB Invest's required capital level.

Table 6.1. Required capital according to the internal model versus rating agencies

In millions of U.S. dollars	2016	2017	2018	2019	2020	2021
Required capital (per internal model)	354	406	399	449	972	1,356
Additional required capital (per the rating agencies' methodologies)	64	73	371	360	440	774
Total required capital	**417**	**479**	**769**	**809**	**1,413**	**2,130**
Available capital	**1,022**	**1,445**	**1,819**	**2,033**	**2,108**	**2,461**

Source: OVE, based on data from Analitika and from document CII/GN-426-14.
Note: Additional required capital (per the rating agencies' methodologies) was estimated based on the difference between the capital adequacy ratio reported at the end of each year and the ratio that would have been reported if the internal economic capital model developed by IDB Invest had been used to calculate required capital.

6.8 Differentials that large undermine IDB Invest's ability to manage and optimize its capital, an issue that affects other MDBs as well. IDB Invest, like other MDBs,[59] has an internal model that is more comprehensive and factors in more information about the underlying portfolio. In practice, however, IDB Invest is restricted to using the model that has the highest capital requirements. At this point in time, IDB Invest follows the Fitch model, which does not consider the risk of the underlying portfolio. As a result, IDB Invest will have to manage two different models and take into account how the differences between them affect incentives and decision-making regarding capital management and use. This issue

59 MDBs are not directly regulated by any authority, so they try to achieve a minimum rating based on the mandates of their governors and taking into account the different methodologies used by rating agencies. However, rating agencies also emphasize qualitative metrics (member country support, Management quality, the importance of the MDB for the public policies of member countries, etc.).

has even been acknowledged by the G20, which commissioned an independent panel in 2022.[60] Among other recommendations, the panel said that MDBs should strengthen communications with rating agencies to inform their views with respect to the importance of MDBs for member countries and begin a conversation with the aim of strengthening their methodologies for rating MDBs.

B. Internal capital generation (returns)

6.9 While IDB Invest has outperformed its business volume targets, its returns have fallen short of the projections set out in the Renewed Vision. OVE analyzed the IDB Invest cost and revenue structure to understand the drivers of its long-term capacity for generating returns. The Busan projections estimated US$540 million in cumulative earnings over the first 6 years of the planning horizon. During that period (2016-2021), earnings amounted to US$241 million (55% less than projected)[61] (Table 6.2). This deviation was mainly due to: (1) an economic environment in which interest rates were lower than initially projected[62] (resulting in a lower return on capital); (2) lower business volumes in the first few years; and (3) the provisioning established for the new portfolio (for example, in 2020 provisioning levels needed to be higher than had been projected in Busan due to the pandemic and the transition to the CECL model).

Table 6.2. Net income (Net gain)

In millions of U.S. dollars	2016	2017	2018	2019	2020	2021
Earnings before operating expenses	99.0	117.2	143.6	178.5	144.7	289.0
Total operating expenses	-80.8	-99.6	-122.5	-130.3	-153.2	-172.5
Net income	**17.8**	**17.6**	**24.1**	**43.9**	**6.9**	**130.9**
Net income (Net gain) (Busan projections)	**28.0**	**49.0**	**73.0**	**99.0**	**128.0**	**163.0**

Source: OVE, based on the IDB Invest audited financial statements and audiovisual presentation CII/PP-149.
Note: Net income also includes the net gain/loss from changes in the fair market value of nonnegotiable portfolios and operations in foreign currency based on the IDB Invest audited financial statements.

60 Boosting MDBs' investing capacity (2022). An Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks.

61 Controlling for the cumulative US$46.2 million impact of the implementation of the ASU 2016-13 accounting standard and US$2.9 million impact of the adoption of new accounting standards, earnings for the period would amount to US$197.7 million, as reflected in the most recent audited financial statements.

62 The Busan revenue projections were mainly based on interest rates and long term projections (forward curves) available at that time. However, IDB Invest revenues have been held back by historically low interest rates during the evaluation period (2016-2021).

1. Revenue

6.10 OVE found that IDB Invest was able to consolidate its ability to generate revenue through its own balance sheet.[63] IDB Invest significantly expanded its portfolio of investments in debt securities, which grew 89% between 2016 and 2021, as it took advantage of its low funding cost driven by its "AA" rating. This gave IDB Invest the ability to significantly increase its financial headroom each year. Thus, in 2021 IDB Invest was able to generate a net interest income that, coupled with its other business lines, covered the entirety of its operating expenses (Table 6.3) and generated a net income of US$131 million. Balance sheet consolidation was a major concern during the merge-out process.

Table 6.3. Financial revenue after provisioning

In millions of U.S. dollars	2016	2017	2018	2019	2020	2021
Financial revenue before provisioning	43.7	52.4	73.1	127.4	160.3	155.3
Loan loss provision	3.5	-14.1	-18.3	-36.7	-111.8	-5.7
Financial revenue after provisioning	**47.2**	**38.3**	**54.8**	**90.7**	**48.5**	**149.6**

Source: OVE, based on the IDB Invest audited financial statements.

6.11 Revenue from services provided to the IDB has performed in line with the projections in the Renewed Vision, with 2023 being the first year in which IDB Invest will not book new operations on the IDB balance sheet. Cross-booking accounts for the bulk of the revenue received from services provided to the IDB. To provide some context, cross-booking was established as a temporary arrangement under which IDB Invest would book and monitor operations on the IDB's NSG balance sheet in order to ensure that the capacity for private-sector lending would not be diminished while IDB Invest was receiving new capital contributions and consolidating the revenue it generated by virtue of its own balance sheet. The framework for SLA between the two institutions stipulated that IDB Invest would be compensated under a cost recovery framework (in other words, without generating a profit margin). In the first few years IDB Invest was in operation, this revenue was substantial, but it peaked at US$76.7 million in 2020. In 2021 it settled to US$68.8 million, and Management projects a similar level in 2022 as IDB Invest cuts back on its use of cross-booking with a larger share of its operations being booked on its own balance sheet. With the end of the cross-booking period, IDB Invest will only perform supervisory activities for the IDB NSG portfolio from 2023 onward. According to Management's

63 This refers to the business of financing clients using its own balance sheet. It encompasses revenue from debt securities and the liquidity portfolio. The funding cost and loan-loss provisions are subtracted from those revenue to obtain an operating cost contribution margin.

projections, the approximately US$45 million loss in revenue from origination services should be offset by revenue from operations booked on the IDB Invest balance sheet.

Table 6.4. Net revenue from services to the IDB Group

In millions of U.S. dollars	2016	2017	2018	2019	2020	2021
Revenue from services to the IDB Group	51.4	63.7	74.6	73.7	76.7	68.8

Source: OVE, based on the IDB Invest audited financial statements.

6.12 Other business lines aligned with the development mission (equity investments,[64] resource mobilization, and advisory services[65]) had a low contribution to revenue. For reference, in the case of mobilization, revenues amounted to 0.4% of the total volume of core mobilization, on average. As for advisory services, the business model is designed to operate mainly through donor contributions, which finance most external advisory services contracts.[66] Lastly, the portfolio of equity investments was established recently, so it is still too early to determine the ultimate return on those investments. Figures from the first six years point to annual returns of around 3.3%.[67]

Table 6.5. Revenue from mobilization, advisory services, and equity investments

In millions of U.S. dollars	2016	2017	2018	2019	2020	2021
Fees from mobilization and other services	5.4	12.8	12.1	11.1	18.2	23.4
Realized and unrealized gains from equity investments	-4.9	2.4	2.0	3.1	1.3	47.2
Subtotal	**0.5**	**15.2**	**14.1**	**14.1**	**19.5**	**70.6**

Source: OVE, based on the IDB Invest audited financial statements.

2. Administrative expenditure and operating efficiency

6.13 IDB Invest's operating costs have trended upward, increasing in proportion to the growth of its origination volume and the size of its portfolio. Total administrative expenditure[68] came in at US$107.3 million in December 2021, equivalent to a compound annual growth rate (CAGR) of 8% for the 2016-2021 period. This growth was proportional to the increase in the volume of commitments (from US$1.445 billion in 2016 to US$6.32 billion in 2021) and to the increase in the total assets in the DRA portfolio (including cross-booking), which grew from US$6.865 billion to US$13.372 billion over the same period.

64 This encompasses revenues from direct equity investments as well as equity investments made through investment funds.

65 This refers to the net revenues for services IDB Invest provides to and receives from the IDB as well as net fees for mobilizing and managing third-party resources.

66 IDB Invest charges a counterpart contribution (in cash or in kind) of around 27% of the cost of the advisory engagement (audiovisual presentation CII/PP-432).

67 This figure was markedly higher in 2021, but 96% consisted of unrealized gains.

68 Total administrative expenditure differs from the total operating expenditure reported in the audited financial statements in that the former excludes certain costs, including the pension program and the equity investment budget.

6.14 Expenditure was primarily driven by personnel costs, which is a rigid cost in the short term. Approximately two-thirds[69] of total administrative expenditure went toward employee compensation. Most IDB Invest personnel were hired as staff (83% as of December 2021), which has made this expense relatively rigid, at least in the short term. Furthermore, IDB Invest personnel are quite specialized,[70] which adds another layer of rigidity because roles are not very interchangeable. That level of specialization, which had been planned since the merge-out, was used to address different mandates and create an institution with specialized expertise in the countries and sectors in which it operates.

6.15 The unit costs of origination and supervision remained relatively stable. IDB Invest processed an average of 57 long-term operations over the 2017-2019 period, which enabled it to take better advantage of its cost structure, thereby maintaining an average cost per committed operation of approximately US$2 million and a cost per million dollars committed of US$55,000. Over the 2020-2021 period, the average number of committed long-term operations rose to 88 in response to the public health crisis, which resulted in better unit cost indicators. At year-end 2021, IDB Invest had kept the same number of operations, which enabled it to maintain the lower per approved operation cost it had achieved in 2020. The cost per million approved, however, reverted to its long-term trend because the operations committed that year were smaller than in 2020. These cost indicators are lower than those of institutions like the IFC (Tables VI.3.6, Annex VI). At the portfolio indicator level, the expenditure ratio (administrative expenditure divided by the portfolio in supervision) also remained stable over the evaluation period.

Table 6.6. Cost and efficiency indicators

	2016	2017	2018	2019	2020	2021
Cost per committed operation (in US$ millions)	1.92	1.99	1.94	2.29	1.82	1.85
Cost per million committed (in US$)	96,799	59,636	54,603	52,486	44,301	55,561
Expenditure ratio[a] (%)	**1.18**	**1.41**	**1.60**	**1.54**	**1.50**	**1.59**

Source: OVE, based on the IDB Invest audited financial statements and IDB Invest quarterly reports.
Notes: For all three indicators, the numerator is total administrative expenditure, taken from the audited annual financial statements. In the case of the first two indicators, the denominator is calculated from the long-term operations and commitments (excluding TFFP, among others). Lastly, the expenditure ratio is calculated from the remaining balance of the total portfolio, including operations booked on both the IDB and IDB Invest balance sheets.
[a]Total operating expenditure divided by the total DRA portfolio balance (including balances on the IDB Invest balance sheet as well as balances on the IDB NSG balance sheet).

6.16 Based on its efficiency analysis, OVE found that Management could improve the information it reports and discloses in its budget exercise, systematically linking costs with output indicators. In

69 More specifically, 65.7% in December 2020 and 67.4% in December 2021.

70 For example, among investment officers (who comprise a significant share of IDB Invest personnel), there are three layers of specialization: (1) origination or supervision; (2) specialization at the subsegment level; and (3) specialization by geographic region.

its business plans, the grounds provided by IDB Invest to justify administrative budget increases was to meet the needs of a growing organization. For example, the 2016-2019 business plans emphasized hiring the investment team and completing the field presence plan; the 2020-2021 plan emphasized strengthening the institution's processes (backbone); and the 2022 plan emphasized bolstering mobilization. Nonetheless, justifications for budget increases and the corresponding results are managed at an anecdotal level. Though IDB Invest has enhanced its tools for estimating operation costs and even for allocating indirect costs to specific operations, it currently only presents to the Board of Executive Directors the big picture of its expenditure, without systematically linking budget increases to output indicators. Such an exercise would enrich discussions regarding the cost structure and would be a step toward a system similar to the IDB's results-based budget.

3. Capital accumulation

6.17 IDB Invest posted a net surplus every year over the 2016-2021 period, amounting to a total of US$197.7 million[71] in cumulative net income and accumulating US$92.3 million in capital. The US$197.7 million in cumulative gains minus the US$105.5 million from the comprehensive income/loss line item (mainly pension liabilities) yields US$92.3 million in capital accumulation over the 2016-2021 period. It is important to bear in mind that the comprehensive income/loss item is a volatile capital component because it mainly covers fluctuations in the market value of some of the organization's assets and liabilities. Therefore, it is likely to revert or vary year to year. As is the case of other MDBs, IDB Invest does not directly control these annual fluctuations, and for that reason its risk models monitor capital use for market risk and pension liabilities.

C. Quality of the development assets portfolio

6.18 IDB Invest maintained satisfactory portfolio quality and managed cross-booking in line with the established parameters.[72] For institutions like IDB Invest, developing a diversified portfolio is a complex task due to the various mandates the institution has to manage and the concentration limits imposed by its risk policies

71 These figures correspond to the increase in the "cumulative gains" account from 2016 to 2021 on the audited financial statements, which mainly encompasses the adjustment for the US$46.2 million in cumulative impacts from the implementation of the ASU 2016-13 accounting standards and US$2.9 million from the adoption of new accounting standards.

72 Responsibility for credit management of both portfolios, including rating, monitoring, supervision, and recovery of investments, falls to IDB Invest per the cross-booking arrangement.

(risk appetite, capital adequacy, and liquidity). Though the launch of operations in the first few years was slow and had lower than projected volumes, IDB Invest has approved and committed significantly higher amounts in recent years. Despite the swift deployment of operations, credit portfolio quality has remained at acceptable levels so far, with no major differences in asset quality between the assets booked on the IDB Invest balance sheet and those booked on the IDB NSG balance sheet. That said, the portfolio of assets booked on the IDB NSG balance sheet had higher levels of concentration, as it includes operations for higher amounts and with longer tenors, mainly due to its higher exposure to the infrastructure segment. This is mainly due to the fact that IDB Invest took advantage of the fact that cross-booking allowed for higher concentration limits than its own capital.

6.19 OVE confirmed the operations booked on the two balance sheets had similar risk profiles. When originating and assigning operations, IDB Invest follows the cross-booking rules and guidelines that determine the minimum amounts kept at IDB Invest and the maximum amounts to be allocated to the IDB's balance sheets. However, as of December 2021, operations booked on the IDB Invest balance sheet had a lower likelihood of default than those booked on the IDB NSG balance sheet. Whereas the average weighted probability of default for the portfolio booked at IDB Invest in December 2021 was 7.1% (equivalent to a "BB" rating), it stood at 10.3% (B+) for the portfolio booked on the IDB NSG balance sheet. This difference is mainly due to the fact that corporate and infrastructure projects belonging to the legacy portfolio booked on the IDB NSG balance sheet have the highest probability of default (four percentage points higher than projects booked on the IDB Invest balance sheet). Another contributing factor is the use of UCP/URP in the IDB Invest portfolio, because the insured portion receives the insurance company's rating. Despite the foregoing, when looking at the total portfolio (IDB Invest + IDB NSG), there are no differences in the probability of default by segment (ranging from 7.4% to 8.8%).

6.20 IDB Invest was able to keep its portfolio's ratio of impaired projects (nonperforming loans) low, and most of those impaired projects were approved prior to the merge-out. As of December 2021, approximately 90% of the impaired portfolio consisted of projects that were originated before 2016 (most of which are infrastructure projects). In all, 93% is booked on the IDB NSG balance sheet. The remaining 10% belongs to the portfolio originated after 2016, and only 10 of these projects are in default (most of which were approved between 2016 and 2018). Looking at the findings of OVE's evaluation of NSG problem projects (document CII/RE-32-3), it is still too soon to determine if the performance of projects approved after 2016 will continue to be satisfactory.[73] This is especially true for the newer portfolio (in other words, projects originated in the 2018-2021 period), which does not yet have a significant number of impaired projects. OVE would like to point out that the rise in global interest rates coupled with worsening conditions in certain sectors could adversely affect default trends in the near future.

6.21 As the portfolio has matured, strains on credit quality have not translated into impaired loans, instead coming through as a higher number of projects with potential problems. For example, operations flagged as "radar" or "watchlist" increased as much as 16% in 2020 due to the deterioration of macroeconomic conditions in some countries, such as Argentina, which prompted Management to monitor certain clients more closely. With the onset of the pandemic in 2020, several clients were proactively added to the portfolio of projects requiring close monitoring, though this exposure eventually decreased due to the impact of the pandemic being milder than expected.

6.22 As of this writing, despite some differences between the two portfolios in terms of make-up, the average rating of the two portfolios is similar and within the parameters established for the cross-booking arrangement. OVE broke the portfolio down into "vintages" based on the commitment year to set apart projects that are more mature, which presumably would have higher impairment rates since more time has passed since origination. In addition, OVE separated the portfolio booked on the IDB NSG balance sheet from the one booked on the IDB Invest balance sheet to analyze whether or not cross-booking created any disparities in the risk profiles of the two portfolios based on the rating assigned to each operation according to its likelihood of default.[74] As the portfolio evolved over time, the impairment rate began to rise (Figure 6.2). This trend is more apparent on the IDB NSG balance sheet, whose portfolio of projects originated in 2016[75] started with an average rating of "B+" but gradually changed to a higher risk rating ("CCC+"). This can mainly be attributed to the fact that, in its first year of operation, IDB Invest booked most large infrastructure projects in Argentina on the IDB NSG balance sheet. However, this

73 Based on its analysis of projects originated under the NSG window from 2007 to 2016, OVE found that the average nonperforming project became impaired about three years after approval. However, most reported their first problematic event, such as the loss of key customers or dramatic regulatory changes, 18 months after approval, on average.

74 To facilitate this analysis, OVE used the credit-rating-based default probabilities used internally by the IDB Invest risk team as of June 2021. Despite some variations in the margins on some scales in the last five years, the conclusions of the analysis hold.

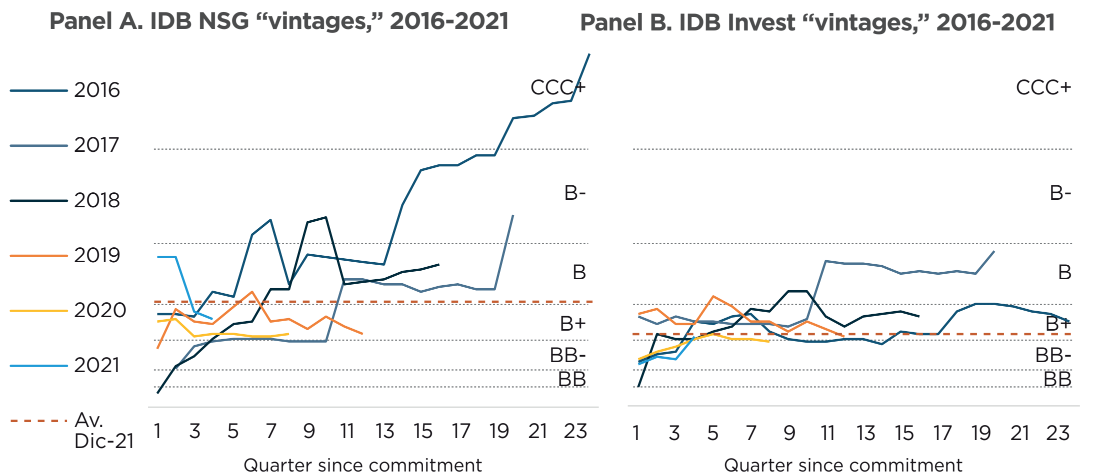
75 The first "vintage" booked on the IDB NSG balance sheet has a high concentration of projects from the infrastructure and energy segment. Though these projects were committed in 2016, most (12 out of 15) were approved prior to the merge-out. At its peak, in December 2017, the IDB NSG 2016 "vintage" had a total exposure of US$429 million. As of December 2021, the exposure was US$164 million.

impairment has been offset as assets originated more recently with better risk profiles have been booked on the IDB NSG balance sheet. Thus, the two portfolios currently have similar risk profiles, in keeping with the cross-booking parameters. It is also important to note that the IDB NSG portfolio is shrinking, a trend that will continue with the end of the cross-booking period. As the size of the IDB NSG portfolio shrinks, impaired operations will have a greater impact on portfolio quality since they will not be offset by the origination of new operations.

Figure 6.2

Ratings by weighted default probability, "vintage," and closing year

Source: OVE, based on data from IDB Invest. Calculation excludes equity and NPL.



Notes: Figure 6.2 presents the rating of each "vintage" based on the weighted probability of default, by year of commitment, in each quarter since the "vintage" started. The numerator is the probability of default weighted by the exposure of each performing portfolio in the "vintage," while the numerator is total exposure of each "vintage's" performing portfolio, both at quarter's end.

D. IDB Invest financial analysis and planning tools

6.23 Significant progress has been made in terms of the development and implementation of financial planning and analysis tools. In line with OVE's 2017 recommendations regarding improvements to financial planning systems and tools, IDB Invest implemented: (1) a risk management framework; (2) a governance framework for managing long-term projections; and (3) more sophisticated models for measuring operation costs and returns. The risk management framework cleared the way for quantitative tools that can pin down and monitor capital adequacy, risk appetite, and the liquidity position. Using these tools, which are grounded in the internal economic capital model, IDB Invest can calculate the capital requirements for the various types of risk it manages (credit risk, market risk, and pension risk) with granularity even at the operation level. While the first part of this chapter analyzed findings related to the capital adequacy model and the second part assessed the portfolio's credit performance, this section discusses implementation of the institution's main financial management tools: RAROC and financial projections.

1. Measuring risk-adjusted returns

6.24 As part of its risk-based strategic management, IDB Invest developed the RAROC tool to analyze operations' returns while taking into account the economic capital they require. RAROC is a highly sophisticated tool grounded in the internal economic capital model that has helped guide the analysis of the financial contribution that each operation makes to the sustainability of the institution. It has also helped operationalize the Portfolio 2.0 tool, which seeks to strike a balance between operations' development impact and the financial contribution (see Chapter II).

6.25 Though the tool was instituted in 2018, there are still challenges to using it ex post. RAROC has been used mainly as a tool for the ex ante analysis of financial returns during operation origination and approval. Nevertheless, OVE found that there are opportunities to scale up its use. For example, teams do not yet perform the exercise of calculating RAROC during implementation to confirm that an operation is producing returns (or to confirm that returns are at least being produced at the portfolio or business segment level). This is a departure from how the DELTA, the other component of Portfolio 2.0, is used, as the latter is updated during implementation. An ex post analysis of RAROC would make it possible to analyze whether an operation's and/or the portfolio's financial results changed over the course of a project.

6.26 There is also room for improvement in how RAROC is discussed at the Board level. While Management has emphasized the Portfolio 2.0 concept to deliver on its dual mandate of impact and financial sustainability (document CII/GA-80-2 and other documents), the Board of Executive Directors does not systematically discuss the use of capital and the associated returns. The only information presented to the Board, as an annex, is the Portfolio 2.0 quadrant the operation falls under. Presentations do not address RAROC per se, instead only addressing the financial contribution ratio (FCR).[76]

6.27 Since RAROC uses IDB Invest's internal economic capital model, the end result does not necessarily reflect the realities imposed by the rating agencies' capital requirements. The rating agencies' methodologies have capital requirements that are much less granular than those of the internal economic capital model. Therefore, even though RAROC is a more precise, more effective tool for distributing capital at the operation level, it does not factor in the impact of the distortions caused by the rating agencies' differing capital requirements. This discrepancy can lead to distortions in portfolio building. For example, in the case of

76 RAROC is the main input for calculating the FCR, which is used to analyze the financial return of an operation as part of Portfolio 2.0.

operations with low credit risk (such as short-term operations[77]), RAROC might reflect a return that is not commensurate with the higher capital requirements imposed by the rating agencies. In other words, it could be overstating the return, because it would assign less economic capital than what the rating agencies require in reality.

2. Long-term financial projections

6.28 IDB Invest reported important breakthroughs in the way long-term financial projections are calculated and disseminated. IDB Invest has made improvements to internal processes and their governance and transparency, developing a series of reports that have been added as inputs for several Board discussions. In addition, business plans and their respective updates include detailed information about the projections. For example, the update of the 2022 Business Plan discussed the most important assumptions, their rationale, and how each of the core variables could potentially impact the results of the projection. There have also been significant improvements in the governance for how projections are developed. Management wrote a manual for how to prepare these projections, and their development currently takes into account inputs from several different IDB Invest units, including the front office, which offers operational insight, and several support offices.

77 By way of example, the capital requirement for an infrastructure operation rated BBB is approximately 3%. Nevertheless, when using the rating agencies' methodologies, that requirement can be up to six times higher, which significantly decreases RAROC.

07

Conclusions and Recommendations

7.1 The Busan Resolution set forth a “Renewed Vision” for promoting development in the region through the private sector. The Renewed Vision established a long-term framework (2016-2025) for IDB Invest focused on strengthening effectiveness and additionality, maximizing synergies between the IDB Group’s public- and private-sector activities, maximizing the efficient use of resources, and ensuring long-term financial sustainability. This evaluation reports on the progress made in the various areas analyzed by OVE, though some challenges remain, which will need to be addressed in order to achieve the end goals set out in the Renewed Vision.

7.2 Despite a slower than expected launch of operations as the institution mounted its own operations, IDB Invest has outperformed the vast majority of the **business volume** targets set in Busan. To a large extent, the institution's rapid growth has been driven by the development of capacity for operation origination and structuring, deployment of a wider array of products, and mobilization of third-party resources. The committed amounts (excluding short-term financing) have mostly targeted operations for the infrastructure and financial institution segments in Group A and B countries. Despite IDB Invest’s efforts, there continue to be challenges to expanding support in certain countries, such as small and island countries.

7.3 IDB Invest has made considerable strides toward strengthening its financial capacity and managing its financial and capital risk with the aim of ensuring its **long-term financial sustainability**. The capitalization process has proceeded as expected, with no major delays. In the first few years, capital was in abundant supply due to such reasons as advance payments of some countries’ capital contributions, lower than expected disbursements, and higher than expected use of cross-booking. The high level of untapped capital had an opportunity cost in that it was not generating revenue, but it did enable IDB Invest to significantly increase its business volume during the pandemic. More recently, capitalization levels have settled near the prudential limits. The institution's earning has increased in recent years yet remain lower than the Busan targets. In addition, IDB Invest built a credit portfolio that has proven to be resilient so far, despite the shock of the pandemic. Progress has been made in the area of financial analysis and planning tools, though there is room for improvement. Notably, IDB Invest should expand use of RAROC beyond the approval stage and increase the granularity of the budget it submits to the Board of Executive Directors.

7.4 There is evidence of progress in the area of **public-private synergies** in recent years, though major challenges remain to maximizing the complementarity of the toolkit of solutions offered by the IDB Group. IDB Invest has fostered alignment and collaboration with the rest of the IDB Group at the strategic level, including by becoming more systematically involved in country strategy development at an earlier stage. Nonetheless, certain key mechanisms established to promote synergies at the strategic level present persistent challenges, including the need to strengthen the Country Representative role and the need to use the country strategies as a tool to guide private-sector efforts. Until now, coordination has been an ad-hoc process that depends on the individuals involved. In particular, some of the factors identified by OVE as inhibitors of more effective coordination at the operation level are a lack of staff incentives as well as a lack of institutional processes and mechanisms for identifying and promoting synergies. Given this situation, there are opportunities to leverage complementarities across the IDB Group's windows, including the systematic identification of potential areas for internal collaboration; the clarification of the various windows' roles and the timing and scope of their interventions; and a more coordinated process for operational planning and for managing the knowledge generated by the institutions.

7.5 IDB Invest has taken steps in several areas with a view to strengthening **effectiveness and additionality**. Implementation of the Impact Management Framework since merge-out has been an important step forward. All of the tools envisioned in that framework to support the full project cycle have been developed. The degree to which they have been adopted and used, however, has varied, which largely reflects IDB Invest's emphasis on portfolio building and origination during the evaluation period. Notable challenges include the need to redefine the strategic selectivity approach for selecting operations and clients, because the existing selectivity tool is not a useful guide for origination efforts, in addition to the need to place greater emphasis on active supervision, so that corrective actions can be implemented as needed. The increasing use of the DELTA during the supervision stage is a step forward in this direction. Similarly, the emphasis on project-by-project analysis needs to shift to active impact management at the portfolio level. Recently, IDB Invest has also made progress toward more systematically identifying lessons learned at the operation level, but use of those lessons to inform the design of new operations is still incipient. At the institutional level, the development of a strategy for managing and making full use of the knowledge generated by the institution is a pending task.

7.6 In its pursuit of strengthening additionality, IDB Invest has also forged ahead with the deployment of **services that offer financial and nonfinancial value**. IDB Invest has expanded the financial solutions it offers considerably since the merge-out. However, this expanded offering has not yet translated into a more diversified portfolio, especially in small countries. Use of some products was limited by internal restrictions (e.g., availability of capital and effective processes in place) or market constraints. On the nonfinancial front, notable progress has been made in terms of building internal capacity for mananging advisory services and nonfinancial risks. The primary focus of the advisory services model was to support operations in priority areas during the origination stage, with a series of challenges at play. The prioritization process for advisory services is ad hoc, and its heavy reliance on donor financing has limitations that have hindered use of these resources. In addition, advisory services do not have a results-based monitoring and evaluation system, which is critical considering how the advisory services portfolio has grown, the role those services play in channeling nonfinancial additionality, and IDB Invest's intention of expanding their reach beyond transactional support.

7.7 Despite IDB Invest's efforts and progress, **strengthening operation effectiveness and additionality** continues to be a major challenge. XSRs validated by OVE for operations that reached early operational maturity show that effectiveness is one of the lowest rated dimensions, though these ratings are trending slightly up. Though most operations at the supervision stage analyzed by OVE are proceeding as expected, approximately one-third show signs that their development objectives may be difficult to achieve and thus require active supervision and implementation of corrective measures. Meanwhile, the vast majority of the operations analyzed by OVE incorporated elements of additionality. This finding, which was not unexpected, attests to the variety of potential sources of additionality and the diverse paths to achieving it in projects. Considering the evolution of the additionality concept and its sources, and the difficulties to operationalize and justify it, stakeholders within the institution, including its Board of Executive Directors, have differing understandings and expectations regarding additionality at the operation level and the type of evidence needed to demonstrate it. As at other MDBs, at IDB Invest additionality has focused mainly on the operation level, with limited attention being paid to the concept and its analysis at more strategic levels, including the country, sector, instrument, and client levels.

7.8 In summary, IDB Invest has made strides toward achieving the objectives set out in the Renewed Vision. More specifically, despite some limitations, IDB Invest has managed to build a sizable portfolio of operations in the region, thereby positioning itself as a development partner through the private sector. IDB Invest has laid a foundation for sound financial management in the interest of ensuring its long-term financial sustainability. The objective of **strengthening effectiveness and additionality continues to be a key challenge.** At present, a considerable share of IDB Invest-supported operations did not fully achieve the development objectives that justified their financing. In addition, although most operations involved elements of additionality, elements of additionality, it is essential to strengthen the institutional focus on this concept at a more strategic level to achieve greater additionality at the country, client, sector, and instrument levels. This is the core objective of the Renewed Vision that led to the merge-out and capitalization of IDB Invest over the 2016-2024 period and thus is the institution's greatest challenge, one that must be addressed as a priority regardless of any changes that the institution may make to its business model.

7.9 Based on the findings of this evaluation, OVE recommends the following:

1. **Strengthen the institutional focus on the concept of additionality and its analysis at a strategic level, beyond individual operations.** This entails the following actions:

    i. Develop an additionality framework. With a view to developing a common understanding among all stakeholders within the institution (including the Board of Executive Directors) regarding the concept of additionality, its analysis, and how it is operationalized, OVE recommends that IDB Invest develop an additionality framework that includes: (1) a clear definition of how the concept of additionality is understood at IDB Invest; (2) a taxonomy of the different types of additionality (both financial and nonfinancial); (3) the type of justification and evidence needed to demonstrate additionality; and (4) acceptable evidence and the ways Management will prove that an operation needs IDB Invest support and that the institution would not be crowding out the market. The Board of Executive Directors should be involved in the development of this framework.

    ii. Implement systematic analysis of additionality at the portfolio level. As is the case at other MDBs, at IDB Invest there is practically no analysis or reporting on additionality at the aggregate level, with these tasks only being performed at the operation level. Given this situation, the body of data on the different types and sources of additionality that has been built through such tools as the DELTA and the XSRs presents an opportunity for a systematic analysis of how additionality and its sources have performed and evolved, with the aim of informing strategic decision-making (e.g., at the country, sector, instrument, and client levels).

iii. **Systematically incorporate the concept of additionality and its analysis into the development of country strategies** in order to identify more effectively the areas to be pursued in the country (e.g., sectors, markets, instruments) based on the comparative advantages of IDB Invest, on its own and/or in partnership with other MDBs or bilateral institutions, and its client commitment strategy.

2. **Redefine the strategic selectivity approach for selecting operations and clients.** The existing strategic selectivity tool is not a useful guide for origination efforts at the operation and client levels. An integrated selectivity approach should take into account: (1) the analysis of the most urgent development gaps at the country and sector levels; (2) client demand and perspectives; and (3) IDB Invest's capacity and comparative advantages, including its additionality and resources. Therefore, when reformulating the selectivity approach, simply fine-tuning the existing tool or developing a new one will not solve the issue. Rather, this reformulation will require the participation and coordination of all of the areas involved in the operation and client selection process, including the strategy, business, and risk divisions. This reworking of the selectivity approach should also address coordination of the various strategies and tools at the institution's disposal, including diagnostic assessments of development gaps, the client strategy, and the business intelligence tool.

3. **Enhance capacity for impact management, primarily at the operation supervision stage and at the portfolio level.** This entails the following actions:

   i. **Place greater emphasis on operation supervision.** (a) Systematically identify issues that hinder achievement of the development objectives and expected additionality during operation implementation; and (b) ensure that corrective actions are identified, implemented, and evaluated to increase the likelihood of project success.

   ii. **Enhance impact management at the portfolio level.** (a) Expand the use of Portfolio 2.0, adding analyses at the segment and sub-portfolio levels and other variables not currently taken into account (e.g., specific outcomes, additionality); and (b) based on the operation-level data compiled during approval and supervision, improve the aggregate-level analysis of the various dimensions of the DELTA that support more active management at the portfolio level.

iii. **Continue strengthening the DELTA.** With the understanding that impact management is an evolving area, OVE recommends that IDB Invest: (a) continuously adjust the DELTA tool to bring it in tune with new priorities and business areas and continue its methodological development, especially with respect to clarifying definitions and the respective rating criteria; (b) forge ahead with the standardization and streamlining of indicators; and (c) enhance internal and external transparency.

iv. **Engage in more active management of the knowledge the institution generates and expand its use.** (a) Systematically identify lessons learned from operations and encourage use of those lessons to inform the design of new operations and operations in implementation; and (b) develop a strategy at the institutional level for managing the knowledge that is scattered across the institution, in coordination with the IDB Group.

4. **Develop a strategy and governance for advisory services.** At a time when the advisory services portfolio is growing and its scope may be expanded, it will be important to develop a strategy and governance for advisory services, which should include a clear definition of the different types of services and their objectives, selection and prioritization criteria, sources of financial resources (internal and external), client concessionality mechanisms, and a monitoring and evaluation system.

5. **Systematically identify potential areas for public-private collaboration and strengthen coordination mechanisms at the IDB Group level.** This entails the following actions:

i. **Create or improve mechanisms at the IDB Group level for the systematic identification of potential areas of collaboration**, including the clarification of the various windows' roles and the timing and scope of their interventions.

ii. **Strengthen the Country Representative role to better empower them for their private-sector duties.** (a) Establish clear criteria and competitive processes for the selection of Country Representatives, including IDB Invest as a participant in the process; (b) establish clear criteria for evaluating Country Representatives' performance in their private-sector-related duties, systematically including IDB Invest as a participant in that evaluation process; and (c) provide more in-depth training to country representatives so they can effectively perform their private-sector duties.

iii. **Strengthen IDB Invest's involvement in the development and implementation of country strategies and SFDs.** (a) Establish mechanisms to involve IDB Invest more systematically in the IDB Group's ongoing dialogue with the governments, especially during country strategy implementation, so as to inform the operation origination and selection process; and (b) reframe IDB Invest's role and involvement in the development of SFDs.

iv. **Realign the existing incentive structure to bring it in tune with the objective of promoting more systematic collaboration among IDB Group personnel.**

6. **Continue strengthening capital management and financial analysis and planning tools.** This entails the following actions:

   i. **When designing future capitalization processes, take into account the institution's capacity for deploying capital, while including some headroom for countercyclical responses.** To manage the financial opportunity cost of untapped capital, OVE recommends that IDB Invest take into account its capacity for deploying additional capital when it designs future capitalization processes. However, it should also consider including some buffers so it can respond to emergencies or extraordinary situations, like those that occurred during the pandemic.

   ii. **Continue strengthening financial analysis and planning tools.** In particular, (a) expand the use of RAROC and its scope, to include use of the tool beyond the approval stage to detect potential deviation from the return as estimated at approval and the return yielded; and (b) increase the granularity of the administrative budget distributed to the Board of Executive Directors, systematically linking budget line items to their expected outputs, in the interest of working toward a budgeting framework similar to the IDB's results-based budget.

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