Background Paper
The Learning Generation

Enhancing Multilateral Loans for Education
Intervention Rationales, Mechanisms, Options and Decision Criteria

Andrew Rogerson and Maria Ana Jalles d'Orey
Overseas Development Institute
Enhancing multilateral loans for education: intervention rationales, mechanisms, options and decision criteria

Andrew Rogerson and Maria Ana Jalles d’Orey, ODI

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Abbreviations

ADB - Asian Development Bank
CD - (World Bank) Country Director
CGD - Center for Global Development
CM - (World Bank) Country Manager
CRS - Credit Reporting System
DAC - Development Assistance Committee
EC - Education Comission
EWEC - Every Woman, Every Child
FY - Financial Year
GE - Grant Element
GFF - Global Financing Facility
GFFE - Global Financing Facility for Education
GPE - Global Partnership for Education
GPG - Global Public Good
HRITF - Health Results Innovation Trust Fund
IADB - Inter America Development Bank
IBRD - International Bank for Reconstruction and Development
IDA - International Development Association
IMF - International Monetary Fund
ITFGPG - International Task Force on Global Public Goods
MDB - Multilateral Development Bank
MDG - Millennium Development Goals
MIC - Middle Income Countries
MoE - Ministry of Education
MoF - Ministry of Finance
ODA - Official Development Assistance
ODI - Overseas Development Institute
OECD - Organization for Economic Cooperation and Development
OOF - Other Official Flows
R4D - Results for Development
RAS - Reimbursable Advisory Services
RMNCAH - Reproductive, maternal, newborn, child and adolescent health
SDG - Sustainable Development Goals
TA - Technical Assistance
UN - United Nations
WB - World Bank
1. Introduction and scope

The Education Commission Secretariat originally commissioned this paper to look at the specific case of the proposed “IDA Plus” facility and how it might be enhanced to boost global education lending. This special case is still covered, but we also looked more broadly at whether, given the large financing gap facing many countries in education, it is possible for leveraging and blending of grants and loans, particularly through the multilateral banks, to play an expanded, catalytic role. We also ask how such interventions can best be designed so as to help crowd in domestic and private finance along with international grants and loans.

We review current trends in international education financing and identify the (so far) relatively modest role of loans, the dominant role within them of the World Bank’s two windows, IDA and IBRD, and recent initiatives taken by the institution to boost the scope of their education operations in general, and results-based and girl’s education in particular.

We consider the generic mechanism of “buying down” or blending loans to improve their terms, plus two specific models of global financing facilities and buy-down funds associated, respectively, with maternal and child health (RMNCAH), and, potentially, with the future IDA-Plus lending capacity. We look at rationales relevant to the education sector for such interventions, and possible institutional options and criteria for selection of such initiatives in future.

This paper draws on an earlier report on buy-downs for education prepared by Results for Development (R4D) for the Global Partnership for Education (GPE) (Isenman and Thomas 2013, Results for Development Institute). This was augmented by interviews in Washington DC in January and March 2016, and subsequent contacts, with, among others, staff of the World Bank (WB), GPE, the Commission Secretariat, R4D, Brookings Institution and the Centre for Global Development (CGD). Kevin Watkins, Overseas Development Institute (ODI) Director, kindly provided peer review comments. None of them however bear any responsibility for the views expressed here, which commit only the authors. A list of persons consulted is at Annex A.

A further component of this study was a tailor-made opinion survey of 31 World Bank senior country staff and their national government counterparts, conducted in April/May 2016 across some 30 countries, probing factors which may affect demand for loan-based financing of education. These findings are summarized in section 3 below, and the survey design is explained in Annex B.

An overall health warning is in order. It is notoriously hard, first of all, to demonstrate (Pearson et al., 2010), that the form in which official financing is delivered, other things equal, significantly affects development outcomes. Thus we may agree intuitively with the proposition that “payment by results” generates improved outcomes, compared to equivalent spending via conventional, input-based contractual arrangements. But we typically lack adequate like-for-like comparisons from which to evidence such conclusions.

Related difficulties arise when we try to track whether an increase in international loans leads to a durable increase of government spending on education, or any other broad area of
expenditure (given the “fungibility” dilemma). And moreover, whether a given reduction in the price of some loans, or of a blended package of loans and grants, creates a strong enough incentive to persuade a borrower to take up more of them in the first place.

To that extent, the success of the mechanisms we discuss here will depend at least as much on political economy judgments as on hard impact evidence.


In our private sphere as parents and students, most of us are strongly motivated to help fund our children’s and our own education, including by borrowing from any available sources. We believe in education’s long-term benefits and are prepared to make significant up-front commitments to enable them.

Human capital, famously, does not provide good loan collateral (Schultz, 1962; Becker, 1964; among others). This is a leading cause of credit market failure for education which justifies specific public intervention, for example to guarantee education loans. Poverty and inequality further aggravate the risk that foregone future incomes, let alone indirect social benefits, substantially exceed the costs of education not undertaken.

When we turn to the behavior of developing country governments in considering external loan-based finance to support their education systems, a loosely comparable reluctance to borrow arises: education is still overwhelmingly funded via domestic government budgets, family contributions (in part borrowed informally), and where relevant, international aid, mostly in grant form. A partial exception is higher and technical education, whose labor-market payoff is often seen by governments as both more tangible and shorter-term.

There are a number of reasons why, granted their repeatedly stated belief in the longer-term economic and social returns of education, governments do not rely much on external borrowing to fund it. We discuss these factors in the next section. Suffice it to say here that the lack of loan collateral is not the major constraint. These are, after all, sovereign debts, usually requiring no loan-specific security.

Public compulsory (basic) education is overwhelmingly funded as a grant-in-kind from tax revenues, usually free from direct tuition charges to parents and students (who nonetheless face ancillary costs for e.g. uniforms, materials, boarding and extra tuition, as well as the opportunity cost of the child’s labor) (Steer and Smith, 2015). Further levels of education may involve additional formal tuition fees, whether for private or public provision, although here again grant funding by the state, including for boarding scholarships, still predominates in most developing countries.
The relatively small share (Steer and Smith, op cit) of education spending in developing countries that is financed by aid on either concessional (ODA) or less concessional (OOF) terms is similarly grant-based for the most part. Of the $12.2 billion in gross ODA (2014) for education (Table 1), the main loan-based component ($1.6 billion) is within the (highly) concessional window of the World Bank, IDA. Of this about 25% is itself in the form of outright grants, the rest in IDA 35-40 year “Credits”, i.e. loans with a high implicit grant element.

The share of health spending, within a roughly doubled ODA envelope, has risen strongly, while that of education has remained flat (as also reported by Shaefehoff el al., 2016, using different base years). Notice also that the share of education in IDA disbursements has risen slightly, contrary to that of health. The shares of both health and education loans on non-concessional terms (see below and Box 1) have fallen, both in general and from the World Bank, their largest source, in particular.

The figures for official lending for education on terms not qualifying for ODA are reported to the OECD as “Other Official Finance” or OOF. Reporting of OOF by end-purpose is less tightly prescribed than is the case for ODA, but some $2.0 Billion of these loans are now

Table 1. Shares of Education and Health (and gross disbursements in current USD billions) ODA and OOF

<table>
<thead>
<tr>
<th>% (USD $ billions)</th>
<th>2002</th>
<th>2010</th>
<th>2014</th>
<th>Change in share 2002-2014</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>TOTAL ODA</strong></td>
<td>($54)</td>
<td>($153)</td>
<td>($165)</td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>6% ($3.3)</td>
<td>8% ($13)</td>
<td>7% ($12.2)</td>
<td>17%</td>
</tr>
<tr>
<td>Health</td>
<td>8% ($4.4)</td>
<td>12% ($18.3)</td>
<td>13% ($21.4)</td>
<td>63%</td>
</tr>
<tr>
<td><strong>TOTAL OOF</strong></td>
<td>($12)</td>
<td>($66)</td>
<td>($59)</td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>7% ($0.8)</td>
<td>8% ($2.6)</td>
<td>2% ($1.4)</td>
<td>-71%</td>
</tr>
<tr>
<td>Health</td>
<td>4% ($0.5)</td>
<td>3% ($2.1)</td>
<td>2% ($1.1)</td>
<td>-50%</td>
</tr>
<tr>
<td><strong>TOTAL IBRD (OOF)</strong></td>
<td>($9.7)</td>
<td>($28)</td>
<td>($16)</td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>8% ($0.8)</td>
<td>8% ($2.1)</td>
<td>5% ($0.8)</td>
<td>-38%</td>
</tr>
<tr>
<td>Health</td>
<td>5% ($0.5)</td>
<td>8% ($2.1)</td>
<td>2% ($0.3)</td>
<td>-60%</td>
</tr>
<tr>
<td><strong>TOTAL IDA</strong></td>
<td>($7.7)</td>
<td>($13)</td>
<td>($14)</td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>10% ($0.8)</td>
<td>10% ($1.3)</td>
<td>11% ($1.6)</td>
<td>10%</td>
</tr>
<tr>
<td>Health</td>
<td>12% ($0.9)</td>
<td>7% ($0.9)</td>
<td>6% ($0.9)</td>
<td>-50%</td>
</tr>
</tbody>
</table>

*Source: Data from OECD.stat (2016). Health includes Total Health (code 120) and Population and Reproductive Health (code 130).*

Box 1. ODA concessionality thresholds

The ODA threshold tests of concessionality for official loans have been changed by the DAC recently. Until 2015, the full face value of loans (such as IDA) with a minimum grant element of 25%, measured against a discount rate of 10%, are scored as ODA, even if the actual grant element was, say, only 26%. In the future, only the (absolute) grant equivalent (grant element * face value) itself will count as ODA, the rest scoring as OOF. At the same time, the discount rate has been lowered to a base of 5% (the IMF’s Unified Discount Rate, varying from time to time and according to country income category), plus progressive risk premia, to a current maximum of 9% (OECD, July 2015, Financing for Development Conference).

The likely combined effects of these changes will be, first, to shift more official lending into the OOF category overall, thereby incidentally lowering the adjusted amount of ODA loans for education, as nearly half of IDA credits (55% grant equivalent) would no longer score. However, second, they will provide strong incentives for donors to target softer terms towards the poorest/least creditworthy borrowers (ibid).
thought to be disbursed annually for education. Note also that the DAC concessionality definition (Box 1) has changed recently, with considerable implications for future ODA and OOF reporting.

Two multilateral institutions—the hard window of the World Bank, IBRD, and the Inter-American Development Bank, IADB—account for the overwhelming majority of this OOF figure, dwarfing all bilateral loans combined.

Taking its two windows, IDA and IBRD, together ($2.4b disbursements in 2014, using CRS-reported numbers), this places the World Bank as the largest single international source of funding for education, as well as (after deducting the quarter or so of IDA face value which is provided as pure grants to the least creditworthy countries), by far the largest provider of official loans to the sector. As such, no attempt to mobilize globally greater volumes, or achieve a more effective overall deployment, of loan finance for education, can succeed without the World Bank’s fully committed participation.

Much of the rest of the paper is therefore based on the World Bank’s experience with education lending over the past decade, with some additional inputs from staff of the Inter America Development Bank (IADB) and the Asian Development Bank (ADB), as well as GPE.

In terms of recent trends, (Table 2 below), the World Bank as a whole hit its high watermark for education commitments in the immediate aftermath of the global crisis, FY09 and FY10. Most crisis response packages involved substantial fiscal support, partly allocated to education and related social spending, alongside more traditional investment funding. This was immediately followed by an exceptionally “lean” year, FY11, falling well below the previous decade’s average, then a resurgence for the past 4 years, to a level some 50% higher than past trends and moving steadily closer to the FY10 peak. IDA and IBRD have mostly maintained roughly equal shares in this rising total.

In September 2010, at the UN MDG summit, WB president Zoellick committed to increase new IDA basic education commitments by $750 million over 5 years above the baseline. The baseline used by the Bank was the annual average of the previous decade, FY00-10, at $742 million per year. Despite a very poor start in FY11, the year of the pledge, table 2 shows that the target was massively overshot overall in the past five years, when more than $2 billion, or three times the pledge, was committed for basic education IDA over and above the baseline.

This episode illustrates the power of priority-setting and heightened public commitment and accountability by top managers— even in a lending institution where sectoral choices must remain borrower-driven to a considerable extent.

1 IBRD accounts for the largest shares of total OOFs to education (53% of total OOFs) followed by the IADB (40%). The other contributors are the African Development Bank, the Asian Development Bank, the Council of Europe Development Bank and the Fund for International Development (OECD statistics 2016).

2 The African Development Bank’s Board decided on capacity and specialisation grounds in 2014 to withdraw from basic education lending, continuing however to support higher levels of education.
In 2015, President Kim made a new commitment to double, to $5b over five years, the portion of the World Bank’s education commitments which are in the form of results-based lending (implying a proportion of some 12.5% of today’s $4 billion, rising to 25%, holding total lending constant).

This heightened emphasis on results also has incentive implications for borrowers, given that the Bank is overwhelmingly loan-based. When disbursements are fully results-based, debt is drawn down when results are proven, and not otherwise. This makes it a less predictable financing flow than most conventional input-based support, and transfers project risk more visibly to the country, but the debt risk of the alternative (spend on inputs and borrow now, hope for results later) is also mitigated. In any case, results-based loans will only reach roughly a quarter of new education commitments, so less than a quarter of the Bank’s cumulative portfolio, after several years. And they will presumably continue to be provided against a range of outputs, over which borrowers typically have more control than they do over ultimate outcomes. In any case, it is also true that input-based project designs often involve large and unpredictable delays from e.g procurement processes.

Table 2: New World Bank commitments for education, $ million, selected fiscal years

<table>
<thead>
<tr>
<th></th>
<th>FY09</th>
<th>FY10</th>
<th>FY11</th>
<th>FY12</th>
<th>FY13</th>
<th>FY14</th>
<th>FY15</th>
<th>Average FY00-10</th>
<th>Average FY11-15</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>IBRD and IDA</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Education</td>
<td>4180</td>
<td>5400</td>
<td>2123</td>
<td>3178</td>
<td>3376</td>
<td>4010</td>
<td>4280</td>
<td>2352</td>
<td>3393</td>
</tr>
<tr>
<td>Basic Education</td>
<td>2948</td>
<td>3593</td>
<td>1129</td>
<td>2587</td>
<td>2122</td>
<td>2608</td>
<td>2535</td>
<td>1550</td>
<td>2196</td>
</tr>
<tr>
<td>Basic as % of total</td>
<td>70.5</td>
<td>66.5</td>
<td>53.2</td>
<td>81.4</td>
<td>62.8</td>
<td>65.0</td>
<td>59.2</td>
<td>66</td>
<td>65</td>
</tr>
<tr>
<td><strong>IDA only</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Education</td>
<td>1976</td>
<td>2151</td>
<td>1159</td>
<td>1737</td>
<td>1788</td>
<td>2426</td>
<td>2124</td>
<td>1150</td>
<td>1847</td>
</tr>
<tr>
<td>Basic Education</td>
<td>1290</td>
<td>1213</td>
<td>403</td>
<td>1502</td>
<td>1260</td>
<td>1598</td>
<td>1079</td>
<td>742</td>
<td>1169</td>
</tr>
<tr>
<td>Basic as % of total</td>
<td>65.3</td>
<td>56.4</td>
<td>34.8</td>
<td>86.5</td>
<td>70.5</td>
<td>65.9</td>
<td>50.8</td>
<td>65</td>
<td>63</td>
</tr>
</tbody>
</table>

Source: World Bank historical education finance data 2016. The World Bank does not publish disbursement data by sector. IDA and IBRD education commitment figures for some recent years significantly exceed those reported by the Bank to the OECD-DAC, a discrepancy we are unable to explain and which the World Bank is investigating. Our understanding (March 2016) is that the DAC figures will need to be corrected upward. IDA reported figures by sector also do not distinguish between grants and credits. WB and DAC basic education definitions also vary. Overall about 25% of IDA commitments are on a grant basis. In addition this table reports the fiscal year commitments and not the calendar year.

In terms of country concentration and the distribution of IDA and IBRD lending for education, relatively few (5) large borrowers, 3 IDA (India, Pakistan and Bangladesh) and 2 IBRD (Mexico and Brazil), still account for the majority of the Bank’s education portfolio. They do not map closely to the countries with the most acute educational needs, as proxied for example by largest out-of-school populations. See figure 1 for IDA commitments to basic education in IDA countries with the highest populations of out of school children. This distribution is similar to the overall pattern of ODA (including IDA) funding for education, in

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4 This data refers to IDA and IBRD commitments to total education, total 2000-2014.
which the most disadvantaged countries accounting for two thirds of the out-of-school population receive about a third of education ODA (Schaeferhoof et al., 2016, Education Commission 2016). The biggest gaps are in fragile contexts (Nigeria, Democratic Republic of Congo and Afghanistan.)

**Figure 1. IDA commitments to basic education in IDA countries with the highest populations of out-of-school children, 2000-2012**

![Graph showing IDA commitments to basic education in IDA countries with the highest populations of out-of-school children, 2000-2012.](source: Results Education Fund (2013) with data from the World Bank Project Database 2013. The World Bank definition of basic education is used as 100% of “pre-primary education” funds, 100% of “primary education” funds, 50% of “secondary education” funds, 75% of “general education” funds, and 75% of “public administration – education” funds.

The World Bank, finally, has long been engaged in girl’s education, given both its intrinsic benefits but also its high indirect returns as a powerful determinant of better health and other social outcomes. Most recently (April 2016), it pledged⁵ to invest at least $2.5 billion in education projects targeting adolescent girls (ages 12-17), a decision publicly applauded by Michelle Obama. About 75 percent of these investments are expected to be from IDA, and largely in Sub-Saharan Africa and South Asia, which have the highest number of out-of-school girls. Programs to be supported will include a range of efforts to provide adolescent girls with access to quality education at the secondary level, ensure they are enrolled in and stay in school, and provision of scholarships, conditional cash transfers, and schools with basic facilities like clean drinking water and toilets that promote enrollment.

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3. Rationales for interventions to promote greater/more effective international lending for education.

Here we first revisit the broader case for international intervention for education spending, then the narrower case for incentives for education loans.

**Externalities**. Education spending does not have the strict characteristics (non-rival, non-excludable) of a true global public good (GPG), but can have some GPG-like elements which can justify targeted interventions, including subsidies. For example, perceived domestic returns to education do not factor in spillover benefits via health and good citizenship/good governance, ultimately also affecting neighboring countries’ and wider global stability and prosperity. More broadly, education is agreed by the global community as a basic human right, and a key MDG and now SDG. The International Task Force on Global Public Goods (ITFGPG, 2006) also recognized education in its wider “GPG” definition, while noting that this is not the standard technical usage.

**Overcoming myopia and other public policy failures.** In the specific context of the government demand for international public loans for education, incentive schemes (via a variety of possible arrangements including subsidies, buy-downs, blends and special facilities we discuss in the next section) are a direct and proportional response to myopia in the part of borrower governments. These arguably discount too heavily education’s ultimate pay-off in higher wages and taxes and undervalue the cumulative savings it generates for e.g. health services.

This myopia is analogous to poor households being mis-informed that schooling’s impact on wages is too remote or uncertain, and/or having an excessively high discount rate for such investments (Birdsall, 2016, personal communication). Softer, longer maturity loans, possibly engineered via buy-downs, and other forms of risk mitigation are well suited to such myopia-based market failure.

There is anecdotal support for the argument that knowledge of high economic returns to education (compared to say, transport infrastructure investments) may not be widespread. Moreover, many policymakers advocating for better health, particularly maternal and child health, appear unaware of empirical findings that health returns alone more than justify basic education investments—even were one to ignore labour market outcomes altogether. Also, contrary to widespread perceptions that the payoff to education is only in the very long run (and hence highly sensitive to discounting), there is recent evidence that the payoff periods are considerably shorter (Jamison et al., 2016 for Education Commission, unpublished).

Unless governments fully understand these relationships between (efficient) education investment, growth and human development, the chances are they will disproportionately over-commit to so-called “productive” infrastructure spending, and over-borrow for those purposes.
We tested for this tendency to under-borrow (and perhaps under-invest) for education in our mini-survey of World Bank country staff and national ministries of Finance (details in Annex B).

Among the three top reasons cited by respondents which limit education loan demand, featured in declining order, are: (1) other national development priorities (2) overwhelming competition for scarce IDA/IBRD from other sectors and (3) concerns with high education recurrent costs, via an ever-expanding teacher wage bill. The first concern clashes with repeated World Bank client survey findings (World Bank, 2015) that education ranks as their top sectoral priority. A plausible explanation is our survey’s narrower focus on the perspective of senior officials making specific, constrained borrowing decisions, as against expressing general development statements. Another interesting finding from the survey is that whereas “other country development priorities” ranks as number 1 or 2 for subgroups, the high recurrent costs concern was most pronounced for WB Country Director/Manager staff, who were asked to put themselves in the shoes of their national counterparts.

Beyond these three reasons that might explain low demand for education loans, there was much less agreement with the propositions that the positive impact on the economy of greater public education spending is uncertain, or that the availability of grants from other sources of finance makes borrowing from IDA/IBRD education unnecessary (see Figure 2).

Figure 2. Respondents’ opinions on key statements related to financing education

1. Education is one of the top three priorities for external development finance in your country

2. The positive impact on the economy of greater public education spending is uncertain or not convincing

3. The high recurrent cost stream discourages external borrowing for education (e.g. large teacher wage bill)

4. Most education investments do not generate tax or fee revenues sufficiently rapidly to service loans

5. Foreign loan conditions are especially unwelcome in education (curriculum, pay etc.)

6. The imported technology or other import needs of education are insufficient to justify borrowing in hard currency

7. The arguments above related to not borrowing for education are particularly relevant for Basic Education* *Basic Education includes pre-primary, primary and lower secondary education.

8. There is overwhelming competition for limited IDA (and / or IBRD), especially from other sectors with a clearer cash flow

9. The availability of grants from other sources of finance makes borrowing from IDA/IBRD for education unnecessary

STRONGLY DISAGREE  DISAGREE  NEUTRAL  AGREE  STRONGLY AGREE
Related to the latter, GPE was considered the most competitive alternative external source of finance to IDA/IBRD, followed by bilateral donors, other multilaterals and private/philanthropic support. In IBRD-loan-only countries, other multilaterals (despite the absence of GPE) nonetheless rank as the most competitive source (see Figure 3).

**Figure 3. World Bank’s competing external sources of finance for education**

![Pie chart showing competing external sources of finance for education](chart)

In terms of potential remedies, there was support for the views that: offering longer loan maturities and lower interest rates would increase demand; and that grants were more appropriate for basic education. This response was broadly consistent across Finance minister officials and World Bank country director/managers (see Figure 4).

**Figure 4. To what extent do you believe the following three changes in financing terms could increase the demand for loans to education in your country/focus country?**

<table>
<thead>
<tr>
<th>Change</th>
<th>0%</th>
<th>10%</th>
<th>20%</th>
<th>30%</th>
<th>40%</th>
<th>50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Longer loan maturities/grace period</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Lower interest rates</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Use only grants for basic education</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Respondents might, of course, be shading their responses tactically, in the belief that this might result in World Bank financing terms to their country being improved in some way. However, the push-back against education borrowing spans a wide country spectrum. At one end, there are upper-middle income, IBRD-only borrowers, who have long exited from
“transition” financing discussions with the World Bank, and indeed from most grant aid financing altogether. At the other, there are heavily debt-distressed low-income countries, for whom only IDA grant terms are anyway being offered, for the foreseeable future. Tactical responses are less plausible for such cases, compared for example to large “blend” countries whose IDA allocations are already severely rationed and/or who may also be subject to single-country borrowing limits from IBRD.

Dealing with the “missing middle” This picture indeed needs to be differentiated by country context. At the transition point between low and middle-income countries, IDA and IBRD, we know that concessional aid is falling off faster than non-concessional and domestic public resources rise (Kharas et al., 2014). In this “missing middle” moreover, competition for scarce concessional loans (like IDA blend terms) becomes fierce, just as partial access to financial markets tends to focus attention on investments yielding clear cash flows, such as power and water utilities, and away from the social sectors like health and education. Many of them (e.g. Nigeria, Ghana, Zambia) are also facing large fiscal deficits and a rising risk premium in financial markets, which further limit their financing options, and may be creating the seeds of a new debt crisis.

Improved terms (such as buy-downs) for education could help correct this bias for a transitional period, until government revenue and education spending patterns became more robust. The World Bank reports anecdotal evidence that the demand problem for IBRD lending for education is concentrated on countries that have in the past had IDA financing for it, which is consistent with the view of “concessionality” being associated with “softer” sectors in the minds of borrowers, a labelling as much as substantive problem.

Significant numbers (Morris and Gleve, 2015) of high-performing IDA borrowers are set to graduate to Middle Income Contry (MIC) status over the next 15 years. In graduating IDA countries, such as Vietnam, Pakistan, Nigeria as well as India, which is already using a “transitional” facility on harder terms than blend-IDA, there are already serious volume constraints on remaining concessional loans. These countries also account for a large proportion of the out-of-school burden, not to mention other indicators of education SDG. The top 10 countries in terms of numbers out of school with 67% of the total, receive only 24% of education ODA (Schaeferhoff et al., 2016)

Balancing grants and loans in low-income contexts. The current evidence base on competition between grants and loans for funding in education in lower-income countries, and basic education in particular, is not conclusive. While the governments may rationally prefer grant financing wherever possible, client surveys by the World Bank and Asian Development Bank suggest that demand for basic education support is quite high even for loan funds (World Bank, 2015).

There also appears to be neither compelling statistical evidence of substitution, nor yet of clear-cut complementarity, between IDA (mostly loans) and GPE (all grants), for example, in countries where both operate, when based on comparable definitions. Both are on modest upward real-terms trends, or at worst flat-lining in some country groups, although this data is not externally validated yet (given the above-referenced discrepancies between the World Bank’s self-published education numbers and its education ODA and OOF, as reported to the DAC). We also know that the largest combined (GPE and IDA) volumes of education assistance
flow to countries assessed by the World Bank as “moderately debt distressed”, and therefore receiving both IDA grants and credits, rather than the smaller groups at high risk, receiving only grants, and low risk, receiving only credits (see chart at Annex C). Whatever substitution effect GPE might initially have had on IDA, moreover, seems to have been more than outweighed by the conscious and successful efforts, such as the Zoellick, 2010 pledge (Section 2), to increase IDA for basic education.

There are stronger signs of substitution between bilateral and multilateral grant aid (R4D, 2015, independent Interim evaluation of the GPE). And certainly the share of multilaterals in education ODA (25%) is much lower than that in health (36%) (Schaeferhoff et al., 2016, op cit). Health also has far greater volumes of grant-based multilateral funding: education essentially only has GPE and about a quarter of IDA, as mentioned.

**Achieving systemic effects.** The main logic of a loan subsidy or “buy-down” (these mechanisms are explained in next section) is that it can induce a country that would not otherwise borrow to do so. This is especially true where the loan is “bundled” with systemic reforms that might not otherwise be achieved, whether such reforms are used as a buy down trigger (prior condition) or not. These reforms in turn may be associated with an improvement in the effectiveness of a much bigger public spending basket. This way funding can actively “crowd in” additional government spending in the medium and longer terms, as well as help attract private resources. (This has been built in to the design, for example, of the Global Financing Facility for maternal and child health, discussed in section 6).

**Front-loading.** As will become clearer when we discuss typical loan/credit buy-down arithmetic (see Box 2 in next section), a grant donor who is able to “sweeten” the terms of a loan enough to overcome the borrower’s reluctance to take on loans at harder terms, achieves two related things. First, they save financing costs, of course, for the country, increasing its fiscal space. And second, they are having an immediate multiplier effect on their own contribution. Say, for example, it costs 15% of face value to convert an IBRD loan instantly into the equivalent of an IDA blend credit—what we might call the cost of a “synthetic IDA blend” (Note that transition countries are already paying more for IDA).

Another way of looking at this relationship is that this 15% grant stake potentially mobilizes a (100/15)= 6.7 times larger spend, up front, compared to using the same sum as a standalone grant. Such leverage could go quite a way to help close the global education financing gap sooner. A $100 million trust fund, for example, could hypothetically be converted into more than $650 million of new education commitments on IDA blend terms, starting with standard IBRD terms which are entirely market-based.

A related option, with similar “raw leverage” potential, might be to offer zero-charge, zero-interest loans, which would have a grant element of some 13 basis points higher than standard (38-year) IDA credits, for the same maturities, or of some 17 basis points more than IDA blend (25 year) loans.

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Remember however, in all of this we are assuming that a relatively modest reduction in borrowing terms/costs from will encourage some transition countries to borrow more. Such a reaction is quite reasonable, and confirmed by anecdotal evidence, for example in the recent decisions by Jordan and Lebanon, IBRD countries, to borrow for education using the new enhanced IDA facility for the subregion. But we simply do not know just how responsive to such price incentives borrowers will be. So, for example, we cannot reasonably expect that there is effective demand out there to blend, say, $1b in grants to mobilise over $6.5 billion in new lending-this demand needs to be tested.

Further down the pricing scale, a standard IDA credit can also be converted, at today’s terms and discount rates, to a pure grant, at an additional cost of some 45% of its face value. In a low-debt distress country where IDA can no longer offer grants directly, and there is resistance to using scarce IDA credits for education, an education donor would, hypothetically, more than double its financial impact at a stroke (100/45=2.2) if it simply bought down IDA credits to grants, either releasing more credits for other purposes, as against deploying its own grants directly, or increasing the share of IDA allocated to education.

GPE could even in theory also take that route itself, accepting of course that would imply to that extent closer integration with the World Bank. Leverage is of course not the only driver-one has to consider quality of dialogue, the expertise and policy relevance bundled along with the funds, administrative burdens etc. However, the education financing gap is so acute in certain country contexts, as already suggested and as argued forcefully by the Commission, that passing up any opportunity to “scale up” in these kinds of proportions should not be done casually.

Additionality-a caveat. Funding used to “crowd in” loans and government expenditure should not be at the expense of “crowding out” other grants for education, obviously. These interactions make it imperative to collect reliable and comparable figures for all donors (including resolving apparent discrepancies between the World Bank’s self-reported education commitments and those reported via the DAC), as well as robust national spending data, with and without buy-downs. As the early Global Financing Facility (GFF) experience shows (section 6), this monitoring process is by no means a trivial undertaking. These interactions also underline the importance of clear agreements with governments about financing from domestic resources and of at least informal equivalent understandings with relevant donors to education.

4. A range of incentive mechanisms.

Multilateral banks and their owners and partners have come up with a wide array of often ingenious instruments and incentives to promote more, and more effective, support in high-priority sectors—from climate change and governance to multiple health-related initiatives and partnerships.

At one level, these can be straightforward statements of strategic intent, often supported by publicly stated spending, output or outcome goals, and bolstered by internal and external accountability mechanisms. The examples already given of the Zoellick pledge to raise IDA
commitments for basic education by $750 million over five years (fiscal 2010-2015) and the subsequent $5 billion commitment by President Kim for results-based education, are cases in point. The impressive multi-stakeholder partnership behind Every Woman, Every Child (EWEC), even without the subsequent, World Bank-managed Global Financing Facility, which we discuss in section 6 below, is another exemplar. There are several other initiatives in, in particular, good governance, health, food security and climate change we could point to.

Further on in the continuum, there is a suite of financial engineering products, all of which have the effect of combining grants and loans to achieve particular effects. It is perhaps easiest to view these under the general rubric of “creating synthetic concessional products”, whether the actual mechanism is a buy-down or a looser package (or “blend”) of grants and loans, or debt swaps, and so on.

**Buy-downs** (see Box 2 below) are an arrangement whereby a third party buys down all, or part, of either or both of the interest and the principal of a loan between a country and a lending organization, thereby releasing the borrowing country from some or all of its future repayment obligations. That generates fiscal room for maneuver which can be used to fund domestic development (Isenman and Thomas, 2013, op cit.).

In the simplest case, the loan is entirely written off (at the grant giver’s expense) before any interest or charges accrue or principal falls due, thus converting the loan instantly into a grant. Even that relatively clear-cut situation is not, importantly, necessarily equivalent to the funding having been offered as a grant in the first place. The borrower must first incur a sovereign debt, and then be completely confident that the grant to extinguish that obligation is forthcoming immediately, without significant further conditions or contingencies. This is akin to time-bound refinancing or debt restructuring situations, such as those enabling post-conflict countries which historically fell into default to IDA to resume normal borrowing. Confidence (ex-ante) that an education loan, in our case, will be bought down to grant terms is also critical to changing the borrower’s inter-sectoral allocation decisions.

This instant 100% buy-down, sometimes called “buy back” or simply refinancing, is just one of a suite of possibilities where loan terms are softened, by some combination of buying down principal (reducing both future interest and principal payments) and buying down the interest rate (reducing future interest payments, but leaving the schedule of principal payments untouched.) These can involve formal three-way contractual negotiations between the lender, grant source and borrower, as was the case for example in the DFID-IBRD-China packages discussed below. They can be quite time-consuming.

Beyond a buy-down or formally blended construct as such there is a wider array of less formal and intermediate possibilities. In these, the country agrees to take on two or more parallel funding streams, of which at least one on a grant or highly concessional basis and at least one on harder loan terms, deeming the overall “package” to have satisfactory terms for the purposes intended.

While such arrangements may well be more flexible and faster to set up than more structured products, it can be difficult to track subsequently whether they really provide any additional resources (compared to all the previous commitments, or stated intentions, of all the participating lenders and granters). And in all probability, they will not have the same
psychological impact as a direct and well-publicised switch between “concessional” and “non-concessional” terms (or equivalent labels), especially for transition countries well accustomed to making borrowing decisions based on such terms.

BOX 2. Some buy-down mechanics

The attractiveness of buy-downs rests in large part on the arithmetic of discounting and net present value, and this is crucially affected by the gap between actual interest rates charged and the reference discount rate used (by the borrower and/or lender).

So, for example, consider (1) a typical IBRD loan, (2) a harder or “blend” terms IDA credit, and (3) a regular IDA credit, typical of terms also offered by other MDBs. Their terms range from typically 12 to 38 year maturities, with 4 to 6 year grace periods, and carry US$ interest rates currently around 2.5% (IBRD and IDA-Blend) plus service charges of 0.75% (IDA-Blend and IDA) and commitment fees of around 0.25% (IBRD).

Discounting these different loan and credit service flows by the current WB/IMF unified discount rate of 5% produces the following percentage grant elements (GE):

- IBRD 18%
- IDA-Blend terms 33%
- IDA- standard credit 55%
- IDA grant 100% (by definition)

(Source: World Bank, Development Finance Institutions staff, personal communication, February 2016. NB Such GEs (validated by the authors using the Bank’s Web-based calculator tool) are sensitive to changes in the timing of repayments and especially to any up-front costs)

One way of thinking about these grant elements is that a lender using a 5% discount rate (like the World Bank itself, currently) should therefore in principle be willing to accept an upfront payment of, approximately:

1. 15% (33-18) of face value, to convert IBRD to IDA blend terms,
2. 22% (55-33), to convert an IDA blend to standard IDA credits,
3. 37% (55-18), to convert IBRD to standard IDA credits,
4. 45% (100-55), to buy IDA credits down to full grant terms,
5. 67% (100-33), to buy IDA-blend credits to full grants, and finally
6. 82% (100-18), to buy down IBRD loans to full grants.

The first four cases therefore all achieve a potential “grant multiplier” of two or more, meaning that a cash donor could hypothetically “buy down” to the next softer level a loan or credit with a face value of roughly two (100/45), three (100/37) five (100/22), or seven times (100/15) the grant funds at their disposal. These examples represent quite large potential leverage for grant donors, and very substantial front-loading of overall funding, IF one believes that such pricing changes will be sufficient to persuade reluctant governments to borrow.

However, to actually deliver this kind of leverage on a large scale for education, borrower preferences across sectors would need to change significantly (which takes us back to underlying perceptions of the returns to education, relative to other investments).

Results Triggers. Buy-downs have sometimes been associated with results-based “triggers”, or conditions of release of the grant funds which extinguish, or at least soften, the loan. So for example, in an historic series of IDA credits for polio eradication in Pakistan and Nigeria,
the buy-backs to grant terms, financed by the Bill and Melinda Gates Foundation and others, were triggered by satisfactory audits that immunization targets had been reached.

The results trigger approach is potentially interesting for the education sector from an innovation and of course from a development outcomes perspective. It does however involve a potential “double jeopardy” problem from the borrower perspective. If trigger targets are not met, not only will important development objectives be missed, but also the country will be saddled with those higher loan repayment obligations it was planning to avoid, with nothing (or not enough) to show for them. The objectives of encouraging countries to borrow more for education and of being more results-oriented might therefore be working at cross purposes if the trigger is not well designed. It would be preferable to make loan disbursements themselves result-contingent in the first place (see Section 2 above on President Kim’s results-based lending pledge), hence automatically eligible for buy-downs, than to have input-based loans subject to subsequent outcome triggers prior to buy-down.

As in other results-based designs, the suitability of triggers also hinges on how much control the country feels it has on project management, input choice etc. China, in a series of operations involving DFID buying down the (then much higher) IBRD terms to roughly 2%, for education, TB control and rural development, shortly after graduating from IDA, undertook no such triggers.

Evidence from buy-down cases. As alluded to in the introduction section, there is not yet a wide enough range of recent case studies from which to draw definitive lessons, and those that are documented (Isenman and Thomas, 2013, op cit) appear to have been quite context-bound and transactions-intensive.

The 3 polio cases, 3 China IBRD- DFID blend and 1 Botswana IBRD-EC blend cases (7 out of a total of 8 cases reviewed by R4D) were very much set in specific historical contexts. The China-Botswana blends were at a time of significantly higher IBRD interest rates than today, and the two countries’ specific policy decisions against borrowing on IBRD terms for non-revenue generating projects. We cannot assume that relatively strict position is still widely held today, though it may be. In our survey, for example, respondents agreed that lowering interest rates would increase loan demand. The 3 polio cases, on the other hand, are archetypal examples of a “weakest link” global public good, where the benefit to humanity of eradicating the disease in the last countries where it still lurks vastly exceeds the direct benefit to the country itself- an externality which will not apply to education to anything like the same extent.

Beyond these cases, and a smaller power operation in Samoa between the Asian Development Bank and Australia, there has been recent exploration by GPE of a possible set of buy-downs of Islamic Development Bank loans to (effectively) concessional terms. These discussions have not been conclusive. The GPE board has not so far sanctioned the use of regular GPE funding for buy-downs, but has left open the possibility of raising additional funds for this purpose. There were also questions raised of standards the GPE would apply to judge loan eligibility. GPE staff are currently developing approaches to these questions.

The European Investment Bank and the European Commission have also deployed a larger number of blended instruments working together, usually based on the EIB receiving a grant
from the Commission and using it to improve lending terms and/or provide first-loss guarantees, particularly but not only for infrastructure investments with climate-change or other (eg water/sanitation) benefits. These instruments go well beyond the scope of this paper, and are not directly applicable to education.

Finally, under advanced development by the Global Financing Facility at the time of writing is a buy-down for maternal and child health in India, precisely converting IBRD terms into IDA-Blend terms. This Facility is discussed further under Section 6 below.

**Buy-downs: an historic window of opportunity?**

Part of the attractiveness of buy-downs currently relates to the unprecedented low levels of market-related rates, such as those of the Multilateral Development Banks (MDBs)’ non-concessional windows. The gap between these variable costs and any assumed fixed point, such as zero-interest loans or the standard IDA charge of 0.75%, has never been lower. By the same token, as and when market rates start to rise, that gap will balloon and with it the costs of buy downs to any such pre-determined levels. These current “bargain” gaps also determine the high apparent “leverage” ratios, which in the case of a generalized interest rate rise would then fall sharply, making buy-downs less of a superficially attractive instrument.

We are not here in the business of making market predictions (for brief analyses of medium and long-term supply and demand of global savings, see for example Kharas et al., 2014 op.cit), but it is worth pointing out that, if a return to higher rates is envisaged at some point, deploying buy-downs now could lock in favorable terms for the several decades typical of IDA maturities. Conversely, it is plausible that borrower government demand for such interventions would rise in a higher-interest environment (as was the case for China and IBRD a decade ago) precisely because the authorities are rightly sensitive not just to the labelling of a loan (as concessional or not) but also to the actual gap in terms offered. Under this assumption, demand for buy-downs may at some point rise rapidly, just as its supply falls.

5. **IDA-Plus: a major potential boost to World Bank lending capacity.**

IDA plus (IDA+) (or IBRD-plus, as will be clear in a moment) is a proposal to use the stream of future repayments (receivables) on past IDA credits, now amounting to some $150 billion, as collateral to raise more funds from markets. Effectively, this would boost the overall World Bank balance sheet without further direct capital injection by shareholders. Unlike in the parallel recent case of the Asian Development Bank, though, there would not necessarily need to be a formal merger of the World Bank’s equivalent of the ADB’s “concessional” and “ordinary” capital windows, i.e. IDA and IBRD.

There are some overarching policy questions raised in connection with IDA Plus, for example concerning the long-term structure of ownership of the World Bank Group as a whole, which we will not address here, and indeed may not need to be addressed in the context of an initial programme of modest scale.

The current plan is to test an initial new window of perhaps $5b additional borrowing a year, for several years. It is expected from market soundings that the funds so raised could be
made available, without explicit subsidies, on equivalent terms to IBRD. However, consideration is currently also being given to buying down these terms in bulk (in much the same way as discussed in the last section), using funds mobilised as part of IDA18, to IDA blend and standard IDA terms.

This “synthetic IDA”, as we understand it, would then be allocated across countries using the same rules (need and performance-based) as other IDA, with a (likely) strong emphasis on fragile states.

Financially, the cost of buying down $1 billion of IBRD/IDA + to IDA/Blend terms, as explained earlier, would be approximately $150 million, potentially achieving quite impressive leverage of roughly 6.5:1 (see box 2). Lower multiples apply to standard IDA credit terms and of course to grants.

This across-the-board buydown approach substantially reduces the case for an education-specific bulk buy-down facility, as against case-specific interventions as in the case of the health-related GFF (see next section). Any fund set up to generate additional “synthetic” IDA terms for education alone should also not be counted toward IDA contributions. This argues for any such buy-down pot to be financed from non-core trust funds, specifically with systemic education objectives, for the relevant categories of countries.

Any such future approach would arguably best be structured as a systemic trust fund, rather than a series of ad-hoc transactions, so as to reduce transaction costs. Working as far as possible within the World Bank’s normal loan approval processes would also help a great deal, as was the case in the design of the GFF.

6. The case of the Global Financing Facility (GFF)

The GFF was launched in 2015 to support the “Every Woman, Every Child” (EWEC) initiative and global partnership for Reproductive, Maternal, Neonatal, Child and Adolescent Health (RMNCAH). EWEC is in turn closely associated with the SDGs.

While not specifically designed around buy-backs, which are but one among a variety of tools it can deploy, the GFF does have the stated objective of mobilizing substantial additional amounts of IDA, mainly through catalytic/blended deployment of its grants funded by participating donors, particularly Norway, the UK and Gates. It also, importantly, aims to both crowd-in and extend the time horizon of Government spending commitments for the initiative’s purposes, and thirdly, it aims to help attract private resources to them.

Its design was influenced by the widely held concern that in the next 10-15 years many low-income countries would transition to middle-income status and needed to put in place sustainable health financing strategies for the longer term, less and less dependent on concessional aid in general and vertical health funds in particular, from whom they will be graduating progressively. It has already (April 2016, Secretariat personal communication) obtained some $420m in signed commitments, and has an initial program underway for 12 countries of this size, associated with some $3 billion in IDA and IBRD funding, with a further round planned for launch in the summer/autumn of 2016. It is an extension, financially and
in some design features, of a precursor trust fund focused on health results innovations (HRITF).

The “blended” link with concurrent IDA RMNCAH-related operations (and in at least in one case discussed below, IBRD) is a required feature, and the current average proportion of trust fund to IDA funds is approximately 1: 4. (This is not to say that the IDA funds are necessarily all additional to what would have been the case without the GFF, although considerable efforts are made to track additionality, see below).

Operations are therefore fully integrated into World Bank processes, with the grant and credit/loans processed together. A “Country Platform”, representative of the main stakeholders at country level (including nongovernmental actors), develops a 10-15 year horizon “financing strategy”, fully reflecting domestic priorities, which is then discussed by all funding sources (including global funds, donors, as well as the Bank and Government). Within this perspective, a shorter term (3-5 year) “investment case” is made, linking back to the financing agenda, results targets, disbursement priorities etc. The key relationship of the Bank with the national finance authorities, in ensuring resources are well spent, is critical to this process.

This approach looks to mobilize threshold levels of grants necessary to get significant additional funding effort from all other sources, and this GFF stake can take different forms. For example, an IFC (International Finance Corporation, the private-sector arm of the World Bank Group) investment program will work with local banks to fund private health care provision in some 5/6 GFF countries, involving a guarantee fund supported by GFF. In India, a $1.6 billion IBRD loan will be bought down to blend terms using a GFF grant, subject to specific outcome triggers. A Social Impact Bond on maternal health care will also be piloted by Canada with GFF support. As a substantial part of the targeted maternal and child mortality decline depends on non-healthcare factors, moreover, GFF will eventually be investing in multiple related sectors, such as social protection and some aspects of education, such as nutrition curricula. This all speaks to a quite flexible, learn-by-doing design, with GFF acting as a “pathfinder”.

Demonstrating outcomes as well as (financial and development) additionality is a major challenge, assumed by an Independent Accountability Panel reporting to the EWEC partnership, GFF’s apex supervisory institution, at political level, and working with a variety of as-yet perfectible tools (such as national health accounts and public expenditure reviews). There is also in GFF a major emphasis on results metrics in both financing strategies and investment plans.

The governance structure of GFF, which grew out of experience with the earlier Norwegian-funded Human Resource Innovation Trust Fund, is intentionally very lean, anchored by a secretariat of a handful of dedicated staff within the World Bank’s Health Global Practice. This core team is augmented by many more task managers, working through their regular operations associated with GFF. GFF country allocations, but not individual operations (which go through regular Bank approval) are signed off by a Trust Fund Committee, which is in turn a subset of the Investors Group, a contact network of bilateral donors, partner countries, global funds and others, all investing their resources in parallel to the GFF.
Potential lessons for education include: Comprehensive, participatory and long-term approach to funding of intended results; close partnership with national ministries of finance; flexibility in choice of instruments and ability to take risks; close integration with existing Bank/IDA funding and country advisory processes; requirement of catalytic funding/leverage for every operation; strict accountability for results and additional resources; minimal added transaction overheads; deliberate reaching out to new funding sources, including private and social entrepreneur providers.

7. Possible institutional options for global education buy-down interventions

The preceding discussion points toward at least three alternative, but largely complementary, institutional design options for buy-down and blending interventions for education. They imply different levels of institutional complexity and ambition.

1. **A dedicated trust fund for education loan buy-downs, operated entirely within the World Bank.** This would be justified mainly by the potential multiplier effect, and mainly in regard to blend countries, depending partly on decisions taken within IDA 18 to have an overall buy-down facility for IDA Plus borrowings (section 5). Fund release could be triggered by attainment of specific education results, at any level of education. In such cases, loan disbursements would also need to be results-based, to ensure confidence in the buy-down. It would operate within the current IDA and IBRD country allocation systems.

2. **A multi-lender buy-down trust fund, operated by GPE.** This could increase the synergies between IDA and GPE in IDA-only countries for basic education, assuming GPE’s mandate remains focused on that level. It could help multiply the impact of GPE funding via IDA. It could also be deployed to support buy-downs for other multilateral banks, such as the Islamic Development Bank. There would need to be clarity in the trust fund’s design about what were the minimum additional standards required by GPE for release of the buy-down funds, as compared to the policies and review procedures of the lenders themselves. In the case of IDA or other lenders approved by the GPE Board, these additional standards should preferably be limited to a few simple, easily assessed and outcome-related tests. (NB We have not assessed here GPE’s capacity to implement such a scheme, or what changes might be needed to strengthen it. A workstream on future buy-down approaches and their implications already exists within GPE).

3. **A Global Financing Facility for Education (GFFE), mainly used to catalytic effect, i.e blended, primarily with IDA (and possibly other MDB facilities).** It could also be targeted at a large, multi-tiered subset of education, such as “building skills for life”, as against the whole sector. The GFFE would have more ambitious aims, compared to the first two options, in terms of crowding-in both domestic government, and potentially private-sector, resources for education.
It would need to be country-driven, as the current GFF for EWEC is, and be flexible in terms of instruments, which could include buy-downs, but also results-based mechanisms, guarantees etc. It would monitor, on behalf of a broader collective, longer-term financing strategies and additionality of effort.

GFFE would probably need to be managed by, or at least in very close coordination with, the largest associated source of loan-based and private sector-linked financing, which is likely to be IDA/World Bank Group, including potentially IFC. But a Joint venture between IDA and GPE might also be a valid approach, at least for a transition period. This could reduce the risk of GFFE competition with replenishment efforts of both IDA and GPE, minimize transaction costs and facilitate financing (including buy-downs) of operations implemented by other lenders than the World Bank.

Again, we have not assessed here GPE’s capacity to implement (its share of) such a joint venture, and any related institutional strengthening needs. The same applies strictly speaking to the World Bank itself, but the exemplar of the current health-related GFF, among other global initiatives the Bank has helped to manage, provides a positive frame of reference.

8. Suggested selection criteria

Let’s remind ourselves of some implied or explicit selection/decision criteria that should underpin any new buy-down designs for education (not at this stage in any implied order of priority)

1. Value for Bulk. Limit/spread transaction costs, and avoid lengthy, case-specific review and negotiation as well as small stakes that are unlikely to shift borrower preferences. Lean against “pilots”.

2. Quality. Define early and simply what is a sufficient quality (or systemic impact) standard of loans eligible for buy-downs.

3. Financial Additionality. Buy-downs should include monitoring volumes of education financing activities by the grant donor, the lender, and the government: their sum must rise. Preferably none of the three components should fall, though grant donors may re-balance their activities within a broadly similar envelope.

4. Development effectiveness/systemic reform. Linked to 2, probably not worth the transaction costs of a buy-down for a single standalone investment project, especially one which has low systemic priority for the country. Ideally has to have a reform thrust, preferably improving resource allocations sector-wide.

5. Leverage. A special case of (3): try to ensure, other things equal, a relatively high ratio of loan face value mobilized directly to grant funds used, preferably 2 to 1 or more. This allows for, for example, the crowding in of standard IDA credits using GPE
(or other) grants. Be careful however not to assume that leverage equates with additionality, especially in the critical area of Government spending.

6. **Simplicity/coordination.** Ensure that there is maximum synergy and minimum duplication between review and approval processes of grant resources and lenders. Where these are in different institutions, establish clear eligibility standards (point 2) and pre-qualify lenders as much as possible.
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- **Kevin Watkins**, Director, Overseas Development Institute (ODI)
- **Liesbet Steer**, Secretariat Director, Education Commission (EC)
- **Luis Benveniste**, Practice Manager, Global Engagement and Knowledge, Education, WB
- **Monique Vledder**, Head, GFF Secretariat, WB
- **Nancy Birdsall**, President, Center for Global Development (CGD)
- **Nicholas Burnett**, Senior Advisor EC
- **Padraig Power**, Chief Finance and Operations Officer, GPE
- **Paul Isenman** Senior Advisor (EC)
- **Stephane Guimbert**, Manager, Development Finance, WB
- **Susan McAdams**, Senior Adviser, Development Finance, WB
- **William Savedoff**, Senior Fellow, CGD
Annex B – Survey Methodology & Further Results

Methodology

In order to explore which factors affect demand for loans in education a survey was conducted with World Bank senior country staff and their national government counterparts involved in making major resource allocation decisions about education and in particular about if and when countries should borrow from IDA/IBRD for that purpose.

The survey objective was to compare and contrast, across country contexts, but also between World Bank staff and their borrowers, views on what drives preferences for and agains using credits and loans to fund education at all levels. World Bank staff were asked to express opinions from the perspective of their national Ministry of Finance counterparts, as they understood it.

An initial case country study selection informed the choice of countries to be included in the sample. A final list of 72 countries made the final sample which followed 4 criteria for the inclusion: 1- Top 30 IDA and IBRD borrowers between 1945-2015, 2- Top 30 recipients of GPE funding in 2014, 3- All blend countries and 4- Population higher than 1 million.

The survey was developed in surveymonkey and a survey link was circulated to the respondents by email. The survey was conducted in April and May 2016. The full survey template is attached,

Survey Results

41 responses were recorded initially, however after checking for data validity and consistency, 31 responses were considered for the purpose of the analysis.

The composition of the responses was as follow: 8 responses from a Finance Minister or National Government Official, 15 responses from WB Country Director (CD) /Manager (CM) and 8 responses from WB Task Managers. Most of the background of the respondents is in economics (18 out of 31), 10 of those from WB Country Director/Manager (Figure 1A). Unusually (some World Bank country staff do have human development backgrounds, but not the 15 surveyed), none of the Government or Bank CD/CM respondents claimed any human development, let alone education, background (Figure 2A).
27 respondents said that “their” country gets financial support from the WB for education. 12 countries receive IBRD Loans, 12 receive IDA credits, 4 receive IDA Grants, 2 receive IDA Blend credits and 7 receive other forms of support (including trust funds managed by the World Bank, IDA transition support and reimbursable advisory services). The total is 37, as some responses list more than one type of support.

In terms of the importance of funding to the education sector, the top 3 sub-sectors were: 1- Primary Education, 2- Vocational Training and 3- Systems Strengthening. If we consider just responses from the Finance Minister or equivalent, the first priority is instead Early Child Development or Systems Strengthening (they score the same results). Vocational training scores in 2nd place both for the Finance Minister Group or WB Country Director/Managers.

There was strong agreement that the role of the WB in education is mainly important for knowledge and systems strengthening, followed by financing and convening/coordination.

GPE scored as the most competitive external source of finance vis-a-vis the WB, followed by bilaterals, other multilaterals (not specified) and private/philanthropic support. Disaggregating by country group it is interesting to note that IBRD-only countries still see
other multilaterals as the main competitive source. GPE ranks number 1 in IDA Credit, IDA grant and other type of countries (Figure 3A).

**Figure 3A. World Bank’s competing external sources of finance for education**

When respondents were asked to indicate the extent to which they think that the Minister of Finance of the main country they work with would agree or disagree with some statements the following responses were obtained (Figure 4A):

- 55% of respondents agree or strongly agree that *education is one of the top three priorities for external development finance in your country.*

- 68% disagree or strongly disagree that *the positive impact on the economy of greater public education spending is uncertain or not convincing.*

- The high recurrent cost stream discourages external borrowing for education (e.g. large teacher wage bill) has a more nuanced response with 39% disagreeing or strongly disagreeing with the statement and 35% agreeing or strongly agreeing.

- 32% have a neutral position when it comes to the statement that *most education investments do not generate tax or fee revenues sufficiently rapidly to service loans,* with 48% agreeing or strongly agreeing with the statement.

- 42% are neutral in what relates to the statements: *Foreign loan conditions are especially unwelcome in education (curriculum, pay etc.) & The imported technology or other import needs of education are insufficient to justify borrowing in hard currency.*

- The statement that *the arguments above related to not borrowing for education are particularly relevant for Basic Education* is disagreed or strongly disagreed by 45% of the respondents, followed by 29% that have a neutral view and 26% that agree with the statement.
74% agree or strongly agree with the statement that there is overwhelming competition for limited IDA (and/or IBRD), especially from other sectors with a clearer cash flow.

61% disagree or strongly disagree that the availability of grants from other sources of finance makes borrowing from IDA/IBRD for education unnecessary.

When ranking the above priorities, the statement that ranks first as the top factor seen as constraining demand for loans to education is: there are other country development priorities. This is followed by the concern that overwhelming competition for scarce IDA/IBRD from other sectors and, in third place, high concerns with education recurrent costs, via an ever-expanding teacher wage bill also constrain demands for loans to education. An interesting finding from the survey is that whereas “other country development priorities” ranks as number 1 or 2 for all subgroups, the high recurrent costs concern was uppermost for WB Country Director/Manager staff.
Most of the respondents tend to agree that longer loan maturities/grace periods, low interest rates and using only grants for basic education could increase the demand for loans to education in their country. These responses are consistent across Finance Ministers and WB Country Director/Managers (Figure 5A).

Figure 5A. To what extent do you believe the following three changes in financing terms could increase the demand for loans to education in your country/focus country?

Finally, respondents were asked about other factors that they thought to be relevant in shaping the demand for loans for education. The responses (14) are listed below:

- “Education is national responsibility” (i.e. national identity and national pride). Boko Haram (also in former Soviet republics)
- 1. bring in new knowledge and building domestic capacity rather than equipment  2. demonstrate clear and measurable outcome evaluation
- Focus on quality improvement, enrollment rates and national expenditures on education are typically relatively high already in southern Africa, but it is the quality of education that is the key challenge.
- India’s demand is strong and as such, the survey is biased in the wrong direction, making it only slightly relevant
- Investing in dialogue/communication and outreach with broader audience prior to having an investment in the sector.
- lack of in house capacity in strategic development across education ministries and institutions
- Limited borrowing space and difficult federal subnational coordination
- Limited IDA is really the main constraint in Haiti. The demand is there.
- MoF needs to borrow but the Ministry of Education [MoE] does not need to borrow since the law has guaranteed that MoE has 20 percent of the annual state budget yearly. MoE perceives that loan only a burden with so many rules and reporting
- Reduction of conditions
- Results that could be sustained.
- We need to think beyond lending. Countries can pay for [Technical Assistance] TA through Reimbseable advisory Services (RAS) and do not have to borrow all the time if they need expertise but not financing. This should be an option for all IDA and IBRD countries.
- Workforce development (adult training/lifelong learning) is also an important area where the Government of [country omitted] has requested financial support
- World Bank assistance to the education sector in three projects over a 15-year period, ending some 10 years ago, was unsatisfactory, and the government does not want to risk repeating an unsatisfactory experience.
Survey Template
Factors affecting demand for loans in Education

1. What is your country (national official) or main country of focus (WB staff):
_______________________________________________________________________________

2. Which of the following best describes your current position? (Please mark only ONE response)
☐ Finance Minister or other national government official (specify)
☐ WB country director
☐ WB country manager
☐ WB education task manager
☐ Other (specify)

3. Which of the following best describes your background? Choose up to two responses.
☐ Economics
☐ Finance
☐ Education
☐ Other human development
☐ Other (specify)

4. Does your country/focus country currently get financial support from the World Bank for education?
☐ Yes
☐ No

5. If yes, what form of World Bank financial support does your country/focus country receive for education?
☐ IBRD Loan
☐ IDA Credit
☐ IDA Blend Credit
☐ IDA Grant
☐ Other (specify)

6. When considering external finance mobilization for your country/focus country from any source, which sub-sectors below are the most important? (Please rank the top 3 in order of importance)
☐ Early Child Development
☐ Primary Education
☐ Secondary Education
☐ Tertiary Education
☐ Vocational training
☐ Systems strengthening

7. When thinking about the World’s Bank role in education which do you believe is of the greatest value in your country/focus country? (Please rank your answers 1-3)
☐ Knowledge and system strengthening
☐ Financing
☐ Convening/Coordinating

8. Which external source of finance for education do you believe is the most competitive with the World Bank? (Please mark only ONE response and specify main source if known)
☐ Other multilaterals
☐ Global Partnership for Education
☐ Bilaterals
☐ Private / Philanthropic support
9. Please indicate the extent to which you think that the Minister of Finance of the main country you work with would agree or disagree with these statements (Please note: this does not ask for your own personal view unless you are the Minister of Finance)

<table>
<thead>
<tr>
<th>Statement</th>
<th>STRONGLY DISAGREE</th>
<th>DISAGREE</th>
<th>NEUTRAL</th>
<th>AGREE</th>
<th>STRONGLY AGREE</th>
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<tbody>
<tr>
<td>1. Education is one of the top three priorities for external development finance in your country</td>
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<td>2. The positive impact on the economy of greater public education spending is uncertain or not convincing</td>
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<td>3. The high recurrent cost stream discourages external borrowing for education (e.g. large teacher wage bill)</td>
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<td>4. Most education investments do not generate tax or fee revenues sufficiently rapidly to service loans</td>
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<td>5. Foreign loan conditions are especially unwelcome in education (curriculum, pay etc.)</td>
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<td>6. The imported technology or other import needs of education are insufficient to justify borrowing in hard currency</td>
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<td>7. The arguments above related to not borrowing for education are particularly relevant for Basic Education?</td>
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<td>8. There is overwhelming competition for limited IDA (and / or IBRD), especially from other sectors with a clearer cash flow.</td>
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<td>9. The availability of grants from other sources of finance makes borrowing from IDA/IBRD for education unnecessary</td>
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10. From the list above please RANK the THREE main factors you think the Minister /Ministry of Finance see as constraining demand for loans to education

<table>
<thead>
<tr>
<th>Rank</th>
<th>Factor</th>
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<tbody>
<tr>
<td>1</td>
<td>Other country development priorities</td>
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<td>2</td>
<td>Returns to education spending are unclear</td>
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<td>3</td>
<td>High recurrent costs</td>
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<td>4</td>
<td>Limited tax/fee generation, not sufficient to service loans</td>
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<td>5</td>
<td>Foreign loan conditions unwelcome</td>
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<tr>
<td>6</td>
<td>Low import needs for education</td>
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<td>7</td>
<td>Overwhelming competition for scarce IDA/IBRD from other sectors.</td>
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<tr>
<td>8</td>
<td>Availability of grants for education from other sources makes borrowing unnecessary.</td>
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</tbody>
</table>

7 Basic Education includes pre-primary, primary and lower secondary education.
11. To what extent do you believe the following three changes in financing terms could increase the demand for loans to education in your country / focus country?

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<th></th>
<th>STRONGLY DISAGREE</th>
<th>DISAGREE</th>
<th>NEUTRAL</th>
<th>AGREE</th>
<th>STRONGLY AGREE</th>
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<tbody>
<tr>
<td>1. Longer loan maturities/grace period</td>
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<td>2. Lower interest rates</td>
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<td>3. Use only grants for basic education</td>
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12. Are there other factors that you think are important in shaping the demand for loans for education? Please list.

Thank you
Annex C- Funding and debt risk distress

Figure 6A. GPE countries, IDA funding and debt risk distress (2014)

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