Lifting Prudential Barriers to Mobilizing Private Capital for Development Finance

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Executive Summary

- As highlighted in the 2025 priorities of the South African G20 Presidency, emerging markets and developing economies (EMDEs) will need trillions in external funding to achieve sustainable development goals. However, cross-border capital flows to EMDEs have been lackluster for years, constrained by a range of structural and policy-related factors.
- One key area of focus is the regulatory environment, in particular certain aspects of the prudential framework that inadvertently curtail the degree to which multilateral development banks (MDBs) and development finance institutions (DFIs) can mobilize private capital for vulnerable developing countries.[1]
- Despite MDB pledges to provide $120 billion annually for climate action by 2030, private capital mobilization multipliers remain low—averaging just 0.5x. This means that for every dollar of MDB investment, only 50 cents in private capital is generated, with significant variation across institutions.
- While well-intentioned, certain prudential requirements do not fully recognize the risk mitigation features of certain MDB/DFI resource mobilization products. Targeted adjustments and clarifications to better align the prudential framework with the actual risk profile of these instruments could help to unlock flows of private financing to creditworthy projects. A more risk-sensitive regulatory approach could also help dispel persistent misperceptions about EMDE investment risks.
- IIF analysis of the Global Emerging Market Risk Database (GEMs) underscores that loans made or backed by MDBs/DFIs exhibit less volatile default rates than purely commercial lending, underscoring their stabilizing role during episodes of stress.
- Given the unique nature of the GEMs database, more comprehensive disclosure by MDBs/DFIs, including instrument-level insights, would support more accurate assessment of EMDE risk in areas like sustainable infrastructure and project finance, supporting more opportunities for co-lending and other private capital mobilization products.[2]

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[1] Throughout the paper we refer to MDBs/DFIs as a shorthand reference to Multilateral Development Banks (MDBs) and Development Finance Institutions (DFIs). Note that the definition of DFIs varies across jurisdictions but can include national development banks, export credit agencies, bilateral development finance banks and other entities.
[2] See Box 1 for more details on the product types covered in this paper.

- With respect to prudential requirements, some refinements and clarifications to the Basel Committee on Banking Supervision (BCBS) standards—as well as locally implemented banking regulations—are needed to facilitate a meaningful increase in private sector involvement in MDB/DFI lending structures. Key issues, hereafter referred to as "regulatory barriers",[3] that have been identified include:
    1) The scope of MDBs/DFIs that are eligible for a 0% capital risk weight has changed little over the years, failing to keep pace with newer institutions in some regions.
    2) Prudential standards do not currently recognize the risk-reducing benefits of some co-financing structures offered by MDBs/DFIs, including A/B loans.
    3) Regulatory treatment can fail to recognize the credit risk mitigating effect of some common MDB/DFI products and guarantees, credit insurance or political risk insurance (PRI).
    4) The prudential treatment of project finance is not adequately risk sensitive or reflective of the characteristics of many project finance or infrastructure lending exposures, particularly in EMDEs.

- This Policy Paper includes a set of near-term and medium-term recommendations to the BCBS and jurisdictional authorities to analyze and address the identified regulatory barriers, as well as recommendations to the GEMs Consortium in relation to their uniquely valuable credit risk database. These recommendations are summarized in Table 1.

Table 1: Summary of IIF Policy Recommendations
Near-term recommendations to BCBS and jurisdictional authorities:
• BCBS/Jurisdictional authorities should expand the range of MDBs and DFIs eligible for 0% capital risk weight (or otherwise appropriately lower capital charges) and periodically review the list of eligible institutions.
• BCBS/Jurisdictional authorities should undertake analytical work, leveraging the GEMs database, on the observed risk characteristics of MDB/DFI co-lending and co-investment activities in EMDEs.
• BCBS/Jurisdictional authorities could provide specific guidance on the eligibility of certain MDB/DFI products and guarantees, including PRI, for regulatory credit risk mitigation (CRM) purposes.
• BCBS/Jurisdictional authorities could clarify the criteria for a project to qualify as "high-quality" under the Standardized Approach (SA) for credit risk and consider expanding the criteria to recognize domestic and bilateral development organizations' or MDBs' support for projects.
Longer-term recommendations to BCBS and jurisdictional authorities:
• Explore the evidence for categorizing certain MDB/DFI products as a distinct asset class, to better reflect their risk characteristics particularly for projects in EMDEs.

[3] The term regulatory barrier is used in this paper to indicate an area where the regulatory treatment may not be well aligned with the underlying risk of the activity and therefore can have unintended consequences such as unduly limiting banks' engagement in an activity or making it more costly to provide to the real economy.

• BCBS could evaluate the prudential treatment of PRI, also considering the relatively recent availability of liquidity bridging tools, to assess whether there are conditions under which PRI could meet the requirements for regulatory CRM.
• In relation to MDB/DFI guarantees, the BCBS standards and jurisdictional rules could clarify that banks that use an internal ratings-based (IRB) approach can model the likelihood of a non-payout clause being triggered.
• BCBS should review the risk sensitivity of the calibration of project finance SA requirements and consider adapting the advanced internal ratings-based (AIRB) model formula for project finance, leveraging the GEMs database where possible.
Recommendations to GEMs Consortium:
• Disclose time series for default and recovery rates by instrument type (e.g., A/B loans, guarantees, PRI) to allow risk profiles to be assessed by instrument type.
• Create time series for default and recovery rates by sector and country to improve risk assessment and benchmarking.
• Differentiate default and recovery data for project/infrastructure finance versus corporate finance for a clearer risk analysis.

- The recommendations to the BCBS and prudential authorities contained in this Policy Paper are not intended to bestow a preferential treatment to certain activities on normative grounds. The recommendations are intended to better align the prudential treatment with the underlying risk characteristics in order to avoid unintended effects, which currently include contributing to reduced private capital flows to EMDEs.
- In sum, there need not and should not be a tension between: 1) prudential regulatory mandates of ensuring safety and soundness of individual banks, 2) government commitments to reaching the Sustainable Development Goals; and 3) MDB commitments to scaling the proportion of their operations dedicated to climate finance, and to catalyzing private capital. The available evidence in the GEMs database and from practitioner experience demonstrates that relatively modest adjustments to bank prudential requirements can justifiably be explored on a risk basis. Notwithstanding other non-prudential barriers, small adjustments to the capital rules could have a positive effect on commercial banks' appetite and ability to participate in new EMDE lending and investment opportunities.

Section 1: Balancing act - ambitious development finance goals vs. barriers to private capital mobilization

Mobilizing private capital into emerging markets and developing economies (EMDEs, excluding China) continues to be a critical challenge in 2025 and beyond. Significantly, the external funding needs of countries to achieve sustainable development goals are substantial and growing—a stark contrast to the lackluster cross-border capital flows into EMDEs. The persistent perception of high risk among private creditors significantly hampers many EMDEs' ability to access international markets at reasonable rates. Factors such as geopolitical tensions, supply chain disruptions, climate change, and lingering debt vulnerabilities, are likely to further strain cross-border investments into EMDEs. This comes at a time when such investments are urgently needed to facilitate the energy transition and ensure energy security and affordability. Mobilizing private capital has become even more essential given the rising infrastructure investment needs, and the limited progress in achieving broader sustainable development goals (Chart 1).

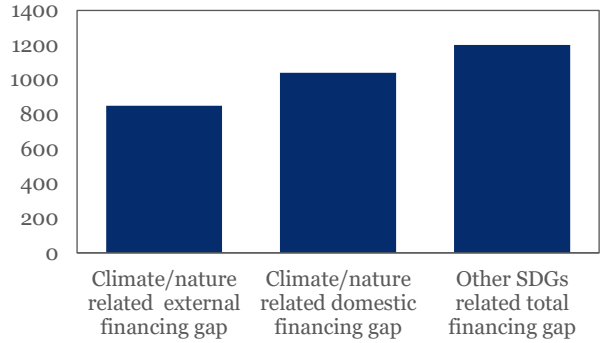
Addressing this critical challenge will require improving the understanding of EMDEs' risk profiles, strengthening sovereign investor relation programs and enhancing data transparency beyond traditional macroeconomic indicators and government debt statistics. Such improvements can better inform private investors' risk and pricing models, ultimately leading to enhanced internal and external credit ratings for EMDEs.

However, uncertainty remains high. President Trump's decision to withdraw from the Paris Climate Agreement underscores the possibility of significant shifts in multilateralism—and, by extension, the private sector's involvement in development finance—in the coming years.

Since the 2015 Paris Agreement, many multilateral development banks (MDBs) and development finance institutions (DFIs) including domestic DFIs and export credit agencies (ECAs) have undergone significant transformations. Increased pressure to address climate funding gaps—both domestic and external—has compelled these

Chart 1: Domestic and external funding needs for EMDEs (ex-China) for development finance remain substantial

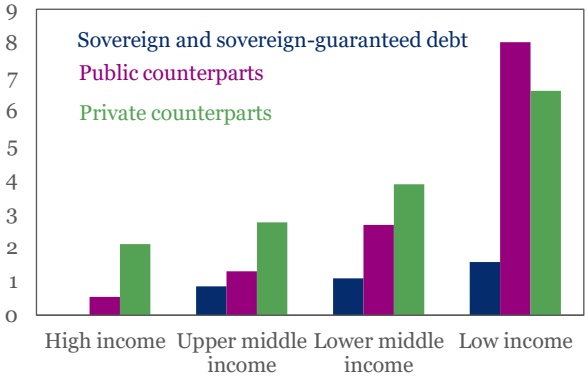
$ billion, annual funding gaps related to climate, nature and other SDG-related spending



Source: IIF; Bhattacharya A, Songwe V, Soubeyran E and Stern N (2024) "Raising Ambition and Accelerating Delivery of Climate Finance"

Chart 2: Default rates on MDB/DFI lending by credit recipient

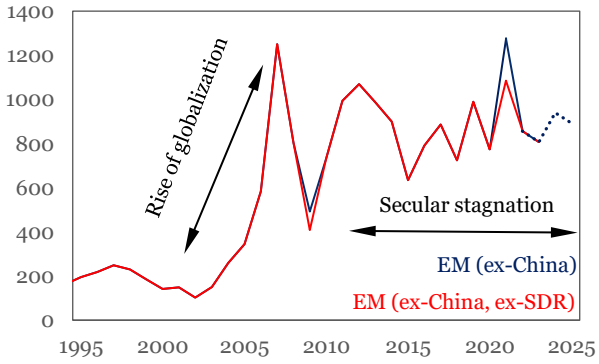
percent, average annual default rate between 1994-2023



Source: IIF, GEMs Risk Database

Chart 3: Non-resident capital flows into EMDEs continue to remain subdued

$ billion, non-resident capital inflows to EMDEs (ex-China)



Source: IIF, IMF

institutions to reshape their business models and funding commitments and has been accompanied by closer collaboration with private creditors.

The recently enhanced statistics from the Global Emerging Markets Risk Database (GEMs) Consortium—offering credit risk data on loans provided by MDBs/DFIs to emerging markets—also mark a significant step forward. These insights provide valuable information on MDB/DFI lending performance and their critical role in catalyzing private sector investments (Chart 2).

Today, around half of MDB operations are dedicated to climate finance—a proportion that continues to grow in line with recent commitments made at COP29 in Baku (see below). This shift has contributed to a substantial surge in global clean energy investment, surpassing $2 trillion in 2024, up from $1.1 trillion in 2015. However, growth in clean energy investment has been relatively limited in EMDEs, which have accounted for only around 15% of total investment over the past decade.

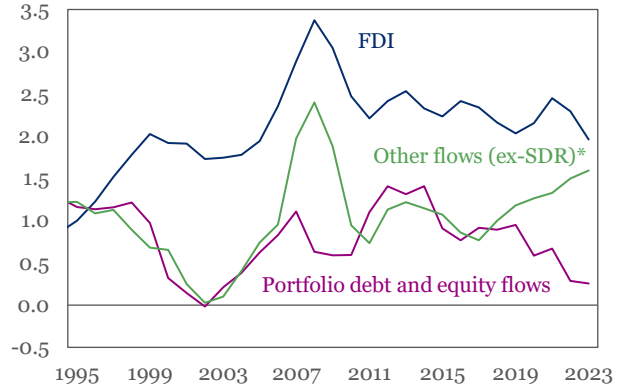
The pace of clean energy investment in these regions has been particularly volatile in recent years, reflecting, in part, the lingering effects of the pandemic and elevated levels of government debt. These factors have dampened investor appetite and hindered governments' abilities to implement large-scale industrial policies essential for mobilizing domestic resources and attracting international private capital to accelerate energy transition and broader climate action.

Modernizing global capital flows infrastructure: Latest estimates from the Independent High Level Expert Group (IHLEG) on Climate Finance suggest that $3.2 trillion need to be mobilized in EMDEs (ex-China) annually for climate action by 2035 in order to deliver on the Paris Agreement and contribute to sustainable growth – up from its current level of around $550 billion per year. Including funding needs for broader sustainable development goals, this figure rises to over $5.5 trillion.

External finance from all sources, international public and private capital flows, will need to cover around $1.3 trillion by 2035, compared to around 150 billion currently. Mobilizing an additional $1.1-$1.2 trillion annually in external

Chart 4: Official flows increasingly become a crucial source of external revenue for many EMDEs in recent years

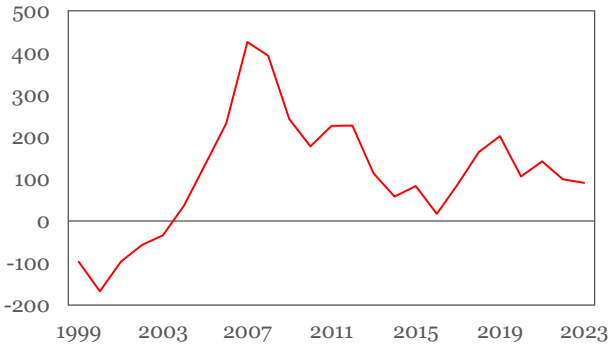
percent of GDP, non-resident capital flows to EMDEs (ex-China)



*Source: IIF, IMF; *includes official bilateral and multilateral flows as well as banking and trade finance flows*

Chart 5: Persistent weakness in cross-border banking flows into EMDEs (ex-China) since 2008 global financial crisis

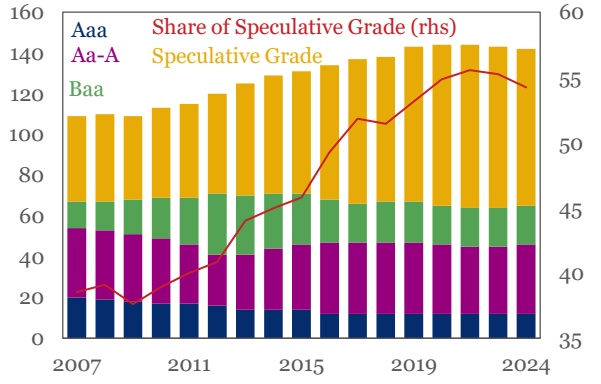
$ billion, cross-border banking flows into EMDEs (ex-China), loans and debt instruments, 3-yr moving average



Source: IIF, BIS

Chart 6: More than half of rated sovereign borrowers have only a speculative grade rating

# of sovereign ratings % of sovereign ratings



Source: IIF, Moody's

capital for climate action will require more than doubling of EMDE capital flows over the next decade (Chart 3).

Efforts by official external creditors, including bilateral and multilateral creditors, have also not been sufficient to meaningfully scale up international private capital flows from developed countries into EMDEs (ex-China). In 2022, such private flows amounted to some $20 billion, suggesting a private-to-public investment ratio of just 0.23x—meaning that for every dollar invested by official creditors, only 23 cents of private capital was mobilized.

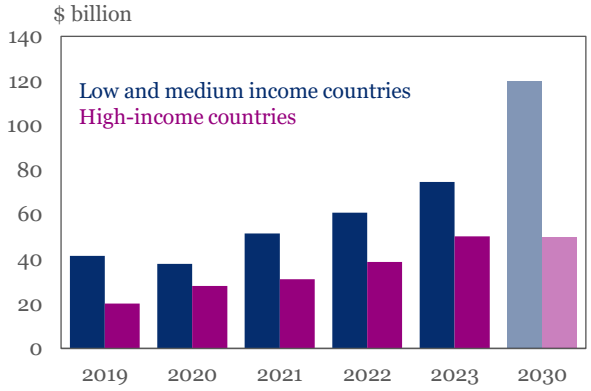
Since the retrenchment in 2009–2010, capital flows to EMDEs (ex-China) have remained relatively stagnant. Foreign direct investment (FDI) flows have been broadly stable, but portfolio flows have persistently declined since 2015, largely due to diminishing investor appetite for EM equities (Chart 4).

Since the onset of the pandemic, as private flows waned, there has been a notable uptick in official multilateral financing. However, cross-border commercial banking flows have been particularly sluggish, constrained by post-2008 banking regulations such as Basel 3 and its national implementations. Aspects of these regulations continue to act as one significant barrier to international commercial bank investments and project finance in EMDEs (Chart 5). In particular, certain aspects of Basel 3 standards—and their varying interpretations by national supervisory authorities—lack adequate risk sensitivity or clarity. This has a direct impact on the risk-weighted capital requirements that banks need to allocate to certain EDME exposures, including some facilitated by MDBs/DFIs, and contributes to a heightened perception of investment risk in EMDEs (see Section 2).

Leveraging MDBs to mobilize private capital: Mobilizing international private capital for climate finance at scale requires addressing the high-risk perception of EMDEs. A significant portion of their sovereign debt instruments are currently rated below investment grade (Chart 6).

Deepening collaboration between private creditors and MDBs/DFIs presents a unique opportunity to mitigate these risks. By leveraging MDB/DFI lending frameworks,

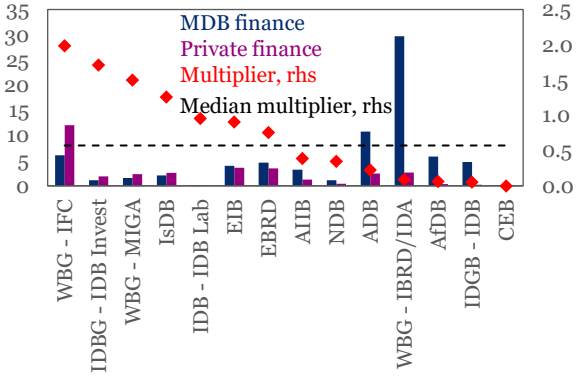
Chart 7: MDBs' climate investment in EMDEs (ex-China) is expected to reach $120 billion annually by 2030



Source: IIF, World Bank

Chart 8: Bridging large climate finance gaps require strengthening MDBs' ability to mobilize private capital

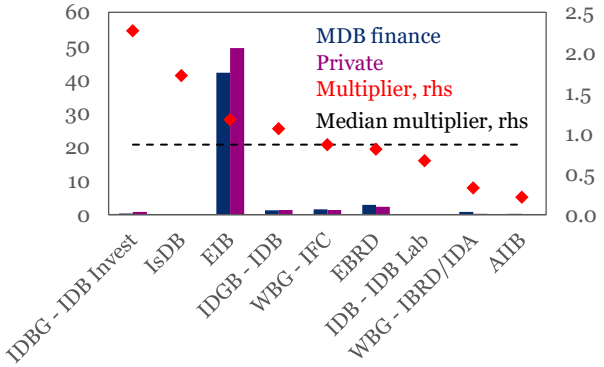
$ billion, climate finance, low/middle income countries, 2023



Source: IIF, Joint Report on MDB's Climate Finance

Chart 9: MDBs more effective at mobilizing private capital for climate action in high-income countries

$ billion, climate finance, high-income countries, 2023



Source: IIF, Joint Report on MDB's Climate Finance

co-lending and concessional blended finance structures can play a critical role in scaling up funding, supported by factors including MDBs': preferred creditor status; rigorous client selection progress; local expertise; in-country presence in many cases; advisory services; and active supervision throughout project implementation.

Greater transparency around MDB and DFI lending operations to EMDEs, and their risk characteristics, can help private creditors better understand MDB/DFI capital mobilization products, increasing their willingness to co-lend.

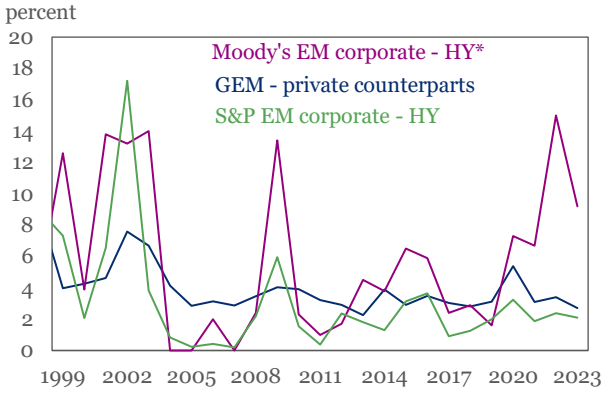
At COP29 in Baku, major MDBs committed to providing **$120 billion annually** to low- and middle-income countries for climate action by 2030—a 60% increase from the current level of $75 billion (Chart 7). This commitment, supported by initiatives such as the World Bank Private Sector Investment Lab, aims to strengthen mechanisms for mobilizing $65 billion in private capital annually, with a primary focus on mitigation projects. These mechanisms include guarantees, political risk insurance (PRI), co-lending programs, credit enhancements, and improved access to reliable data.

While this commitment represents a positive step forward, the private capital mobilization multiplier is expected to remain at around 0.5x (for every dollar committed by MDBs, 50 cents of private capital is mobilized), consistent with recent trends (Chart 8). Of note, this multiplier varies sharply across MDBs and increases to around 1x when lending tools are applied in high-income countries (Chart 9).

What does the evidence tell us about the risk characteristics of MDB/DFI engagement alongside commercial banks?

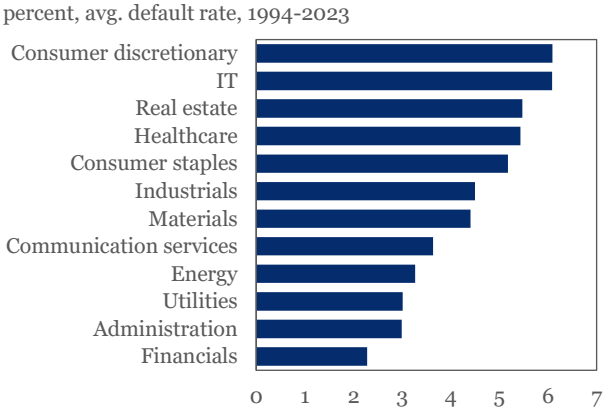
Data from the GEMs Risk Database suggest that MDB and DFI lending exhibits much lower default rates compared to purely commercial lending to EMDEs. However, its current granularity limits definitive conclusions. For example, high-level comparisons with Moody's and S&P data can suggest contradictory results (Chart 10).

Chart 10: MDB/DFI transactions have much lower default rates than commercial lending to non-investment grade EMDE corporates



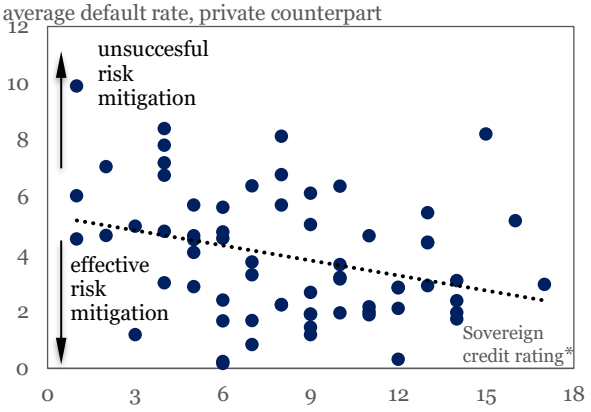
*Source: IIF; GEMs Risk Database, Moody's, S&P; *includes financials but has a smaller country coverage relative to Moody's database which excludes financials*

Chart 11: Financial institutions exhibit the lowest default rates in MDB/DFI lending



Source: IIF, GEMs Risk Database

Chart 12: Co-lending with MDB/DFIs offers opportunities for risk mitigation



*Source: IIF, GEMs Risk Database; * numerical version of Moody's credit ratings on long-term foreign currency debt*

For example, the average default rate for private counterparts in GEMs data over the 1994–2023 period is 3.8%, significantly lower than Moody's default rate for non-investment-grade EM corporates (5.5%)[4] but higher than S&P's rate for EM non-investment-grade corporates (2.9%)[5]. These differences arise partly due to coverage and methodological variations:

- GEMs data includes financial institutions, which historically exhibit much lower default rates than other sectors (Chart 11). A significant portion of MDB/DFI lending (over 35%) in the GEMs database consists of loans to financial institutions. This might contribute to a lower overall default rate compared to Moody's default series, which excludes financial institutions.

- S&P data, on the other hand, includes financial institutions but focuses on a relatively limited number of large EMDEs, resulting in lower aggregate default rates that may give the misleading impression that private sector lending to EMDEs has lower default rates than MDB/DFI lending.[6]

Nevertheless, GEMs data do highlight the potential benefits of MDB/DFI co-lending, particularly during periods of financial stress. For instance, during the 2001 and 2008 crises, MDB loans experienced significantly lower default rates than commercial lending activities. Overall, GEMs default rates are less volatile compared to private sector lending, reflecting the role of MDBs and DFIs as stabilizing forces during crises.[7] However, it is important to note that these conclusions cannot necessarily be made for all transaction types – such as blended finance transactions, concessional loans, A/B loans, or co-lending structures – as currently limited GEMs data by transaction type are published for analysis.

Comparing GEMs default rates with sovereign credit ratings reveals significant risk reduction opportunities through MDB/DFI co-financing in some countries (Chart 12). MDB loans generally exhibit significantly lower default rates for corporates headquartered in countries with higher sovereign creditworthiness. However, in some instances, MDB loans have much lower default rates even than those implied by sovereign credit ratings, underscoring the importance of corporate-level credit quality.

While these findings suggest positive trends, deriving generalized conclusions remains challenging without more granular data. Expanding the scope and depth of GEMs data could help bridge these gaps, providing a clearer understanding of MDB/DFI contributions to risk mitigation and their potential to catalyze private capital in EMDEs.

Access to historical default and recovery rates at the country, sectoral, and credit-rating levels is particularly critical. Additional information on resolution progress, such as the duration required to resolve default cases, would be highly beneficial for better risk assessment. Greater disclosure of transaction-level data, following a sufficient post-transaction period, is also strongly encouraged as it would support global efforts to enhance investor relations and debt transparency practices in EMDEs.

In addition, detailed insights into default and recovery rates based on the types of MDB/DFI transactions (e.g., project finance, A/B loans, PRI) could enable private creditors to more accurately evaluate and price co-lending opportunities with MDBs. This would foster stronger collaboration and significantly enhance capital mobilization.

Box 2 includes five specific recommendations to the GEMs Consortium, which could unlock the granular evidence that is needed to change the

[4] See EM Corporate Default rate will fall further in 2024 and approach advanced economy rate, May 2024, Moody's.
[5] See Default, Transition, and Recovery: 2023 Annual Global Corporate Default And Rating Transition Study, March 2024, S&P Global.
[6] S&P data in general suggests that EM non-investment-grade corporates demonstrate slightly lower default rates compared to their counterparts in other regions. Since 2010, the average annual default rate for EMDE non-investment-grade corporates (including financial institutions) has been approximately 2%, lower than the rates observed in the U.S. (3%) and Europe (2.3%).
[7] See Reassessing Risk in Emerging Market Lending: Insights from GEMs Consortium Statistics, Oct 2024, IFC.

appetite for, and risk/return assessment of, MDB/DFI transactions within commercial banks.

Addressing the barriers to private capital mobilization with MDBs/DFIs

To achieve a meaningful increase in private sector involvement in MDB/DFI lending structures, IIF research indicates the need to address several long-standing barriers to private sector engagement in a range of MDB/DFI transactions (see Box 1 for a summary of major MDB/DFI private capital mobilization transactions). These barriers include the lack of consensus on blended finance and co-lending concepts and definitions; host country risks; the bespoke nature of blended finance and co-lending transactions; the limited availability of project information and pipeline; and restrictive prudential regulatory frameworks that largely undermine the "halo effect" of MDBs and DFIs (see Box 3 for a summary of the key non-prudential barriers). Together, these factors continue to hinder efforts to catalyze private capital through MDB/DFIs.

The remainder of this paper focuses specifically on certain key bank prudential barriers which are misaligned with the risk to commercial banks of engaging in MDB/DFI transactions.

Another significant aspect, which falls beyond the scope of this paper, concerns the effective risk transfer and the interconnectivity of different financial institutions. Supporting the active participation of commercial banks in MDB/DFI transactions necessitates simultaneously enhancing the capabilities of non-bank financial institutions, particularly asset managers, asset owners, and insurers, to engage in MDB/DFI transactions for development finance. This enhancement is crucial for effectively distributing the risk associated with these transactions. Enhanced risk transfer mechanisms, including credit insurance and securitization, would free up additional capital for both private institutions and MDBs/DFIs, thereby creating new funding opportunities.[8] Furthermore, improved risk sharing would help to broaden the investor base, encompassing entities with varying risk appetites, and improve the liquidity of the MDB/DFI instruments. This, in turn, should lead to more robust price discovery mechanisms and greater public understanding, which could foster a broader appetite for development finance.

[8] The prudential regulatory treatment of credit insurance and securitization is beyond the scope of this paper but should be considered as part of a holistic assessment of ways to enhance greater risk sharing opportunities with MDBs/DFIs.

BOX 1:

Private Capital Mobilization via MDBs/DFIs: Overview of Product Types

Products Often Utilized by Commercial Banks

A/B Loans:

A/B loans are structured to leverage private capital alongside MDB/DFI funding. The A loan, funded by the MDB/DFI, generally has a longer tenor than the B loan, which is financed by private creditors. A single loan agreement is used, with the MDB/DFI serving as the lender of record and administering the entire loan. Both parties—MDB/DFI and private creditors—share the project risk, as the loan is not guaranteed by the MDB/DFI. This structure allows private creditors to capitalize on the MDB/DFI's in-depth sectoral and country expertise, and track record as a lender of record.

Parallel Loans, excluding concessional blended finance:

In co-financing arrangements through parallel loans, MDBs/DFIs may serve a catalytic role as arrangers. In many instances, they identify investment opportunities, structure deals, and negotiate loan terms with borrowers, coordinating closely with other lenders. By acting as anchor investors and committing funds before the public launch, they can boost the confidence of commercial investors to participate. Although MDBs/DFIs contribute their expertise to these partnerships, they do not extend their preferred creditor status to co-lenders and expect market-rate returns.

Concessional Blended Finance: [9]

A co-lending structure that includes a pure concessional capital component, providing funding at below-market rates through grants, soft loans, guarantees, first-loss capital or equity investments.

Credit Insurance and Guarantees

MDBs/DFIs can use credit insurance to facilitate funded mobilization by other entities. For example, MDBs can sell (partial) guarantees to catalyze additional private-sector participation in funded transactions.

Products Typically Utilized by Non-Bank Financial Institutions

B Bonds:

B bonds are financial instruments designed to broaden the investor base by accommodating entities that are restricted to investing in securities rather than traditional loans. These bonds are structured similarly to A/B loans, with the MDB/DFI acting as the lender of record and administering the entire loan. The project risk is shared between the MDB/DFI and other investors. However, the B lender in this arrangement is a special purpose vehicle (SPV) or trust, which raises funds by issuing securities to institutional investors.

[9] It is critical to clearly differentiate between blended finance and private capital mobilization, as the MDB/DFI community's use of the term "blended finance" differs significantly from that of private-sector actors. While the official sector views blended finance strictly as involving below-market-rate concessional funding, the private sector typically considers any MDB/DFI engagement—whether concessional or not—as a form of blended finance. Therefore, we use the term **concessional blended finance** to minimize potential confusion and clearly distinguish these concepts.

Credit Insurance as Private Capital Mobilization:

Credit insurance can be utilized similarly to a B Loan: by extending larger loans and purchasing credit insurance from private insurers, MDBs/DFIs can mobilize private capital alongside their own funding, but on an unfunded basis. IFC commonly employs this approach.

Portfolio Solutions:

With portfolio solutions, MDBs/DFIs create diversified portfolios of emerging market private sector loans for institutional investors, sovereign wealth funds and insurers. This can be forward looking, mirroring the MDBs/DFIs own portfolio, or involve a sale of existing assets. They can use a mixture of co-financing products, including B Loans, to create the portfolio.

Securitizations:

MDBs/DFIs can originate loan exposures and then distribute them to third party private investors through a securitization program.

Anchor Investments in Securities Issuances:

Anchor investment entails MDBs/DFIs upfront commitment as an investor in a firm's planned issuance of securities. MDBs/DFIs supplement their anchor investment by performing a range of activities, including initiating the concept, advising clients on the selection of an arranger, and referring inquiries from potential investors.

Anchor investments in funds:

Anchor investment entails MDBs/DFIs upfront commitment as an investor in funds, including growth equity, venture capital, mezzanine, and senior debt funds targeting EMDE borrowers, which catalyzes private capital investment.

Fund management:

MDBs/DFIs can attract third-party capital to invest alongside themselves via managed funds. The outside capital deployed by the MDBs/DFIs managed fund is reflected as core mobilization.

BOX 2:

Suggested Enhancements to the GEMs Risk Database

The existing GEMs risk database offers aggregated data on default and recovery rates in MDB/DFI transactions at the country and sectoral levels. However, this data lacks the necessary granularity for private investors to effectively refine their risk models and adjust their capital allocation strategies. More detailed data would enable commercial banks to undertake a more nuanced, risk-based assessment of projects supported by MDBs/DFIs versus those without such support.

Proposed Enhancements:

1. **Detailed Instrument Coverage Information:**
   - Provide disaggregated data on the volumes and shares of guarantees, A/B loans, co-lending transactions, and blended finance transactions included in the dataset.
2. **Instrument-Level Time Series:**
   - Develop time series for default rates and recovery data at the instrument level, such as A/B loans, first-loan guarantees, political risk insurance, and other co-financing structures. This will provide investors with detailed insights into the risk profiles of specific financial instruments. Creating default series by product type would help verify whether the observed stability in default rates overall applies uniformly across all transaction types, or if the risk profile varies.
3. **Non-Financial Sector Focus:**
   - Establish a headline time series focusing solely on defaults and recovery rates in loans to the non-financial sector. This approach will provide a clearer benchmark comparison to credit rating benchmarks, which typically exclude the financial sector from their emerging market default/recovery statistics.
4. **Sector- and Country-Specific Time Series:**
   - Disclose time series for sector-specific and country-specific default and recovery rates to facilitate more accurate risk assessment and benchmarking against sector and country averages.
5. **Project vs. Corporate Finance Classification:**
   - Classify default and recovery rates by project or infrastructure finance versus corporate finance. This will enable a more differentiated understanding of the risk and recovery potentials within these distinct financing structures.[10]

[10] Earlier editions of GEMs reports included time series to track default rates on loans to financial institutions, along with headline default time series to differentiate default statistics across predefined infrastructure and non-infrastructure sectors.

BOX 3:

Barriers to Private Creditors' Ability to Lend and Participate in MDB/DFI Transactions – Beyond Regulatory Barriers

- **Lack of project pipeline:** The absence of a robust project pipeline is the most significant barrier that limits the ability of some MDBs/DFIs to mobilize private capital at scale.

- **Host country risks:** The potential returns offered by MDB/DFI transaction can be significantly outweighed by host country risks. These risks can stem from reputational issues, economic uncertainty, political instability, currency fluctuations, and credit risks, all of which can deter private investment.

- **Geopolitical risk:** Increasing geoeconomic fragmentation represents a major obstacle, undermining the risk/return profiles of projects for private creditors while also diminishing the pool of bankable projects supported by the MDB/DFIs.

- **Information gaps and lack of transparency:** Information related to MDB/DFI transactions, from project initiation, terms, progress and returns, is often difficult to access and typically incomplete. This lack of transparency obscures understanding and restricts investment opportunities for private creditors. This limited disclosure, in part, arises from confidentiality obligations and commercial sensitivities, which restrict MDBs/DFIs' ability to fully disclose project details.

- **Lack of alignment on concepts and definitions**: There is a wide divergence in the interpretation of concepts related to MDB/DFI transactions, including blended finance, as well as the vehicles, or instruments across MDBs, DFIs, public institutions, and private creditors.

- **Bespoke nature of transactions:** The need for tailored approaches and customized structures to meet specific project needs complicates MDB/DFI efforts to scale private capital mobilization, especially through blended finance. Complex funding structures reduce investor interest and complicate credit rating processes, while a lack of complete understanding of products impedes greater liquidity.

Some of these issues were also discussed in the December 2023 NGFS report, "Scaling Up Blended Finance for Climate Mitigation and Adaptation in Emerging Market and Developing Economies (EMDEs)."

Section 2: Investigating the prudential barriers to climate & development finance

In this section, we examine four specific aspects of banking prudential regulatory requirements that have been identified by several IIF commercial bank members as unduly restrictive or unclear and, therefore, presenting a regulatory barrier to the extension of development finance transactions conducted with or alongside MDBs/DFIs.

For each topic, we examine the global treatment in the Basel Committee on Banking Supervision (BCBS) standards and the jurisdictional implementation in five major jurisdictions: the European Union (EU), Japan (JP), South Africa (ZA), United Kingdom (UK) and United States (U.S.). Desk-based research, working group discussions with a range of industry practitioners and anecdotal evidence from interviews with a sample of twelve commercial banks and six MDBs/DFIs is referenced. Finally, a series of potential short-term and medium-term policy options are proposed to either revise or clarify the BCBS standards and jurisdictional requirements, or align the jurisdictional interpretation of certain standards, in a risk-based way to address the identified barriers.

The analysis accounts for the fact that jurisdictions around the world are currently working to implement the 2017 Basel 3 finalization package (referred to hereafter as "Basel 3.1" for brevity). Some jurisdictions have already implemented Basel 3.1, while others are still finalizing implementation. In the case of countries which are yet to implement the aspects of Basel 3.1 that are most relevant to the prudential barriers discussed in this paper, the regulatory treatment may change in the coming years. For purposes of the analysis, we have examined the current or anticipated future regulatory treatments to understand what may be creating barriers today. Several of the barriers are not affected by changes introduced in the Basel 3.1 standards and relate to aspects of the BCBS standards that pre-date Basel 3.1.

➢ **Barrier 1:** MDB/DFI eligibility criteria and eligibility for 0% risk weight

Issue	Regulatory standards and requirements have long recognized the low-risk nature of banks' exposures to 'supranational entities and MDBs'. This is reflected in the 0% regulatory capital risk weights that banks are permitted to apply to their exposures to at least some MDBs. In the BCBS standards, there are eligibility criteria and a list of eligible institutions. In practice, the set of institutions eligible for a 0% risk weight has been relatively static and has failed to keep pace with newer institutions in some regions (such as GuarantCo, which is funded by the UK and several other Advanced Economies). The BCBS list also comprises MDBs and not other DFIs. This means that some banks need to apply significantly higher capital risk weights to certain MDB/DFI exposures, rather than 0%.[11]
Does this stem from BCBS standards?	**In text:** Yes. CRE 20.13-14, including footnotes 8 and 9. CRE 20.15 specifies the risk weights for other MDB/DFI exposures which are ineligible for 0%. • *"MDBs currently eligible for a 0% risk weight are: the World Bank Group comprising the International Bank for Reconstruction and Development, the International Finance Corporation, the Multilateral Investment Guarantee Agency and the International Development Association, the Asian Development Bank, the African Development Bank, the European Bank for Reconstruction and Development, the Inter-American Development Bank, the European Investment Bank, the European Investment Fund, the Nordic Investment Bank, the Caribbean Development Bank, the Islamic Development Bank, the Council of Europe Development Bank, the International Finance Facility for Immunization, and the Asian Infrastructure Investment Bank."*

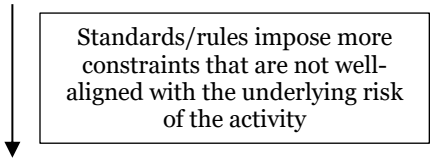
[11] This issue was recognized recently by Emmanuelle Assouan, Director General for financial stability and operations at the Banque de France who noted: *"We have need for more funding in emerging markets … I think we should a bit more room for new multilaterals in the Basel III standards. We have a list of 16 MDBs set in stone – I think we should open the doors and windows a little to make room for new MDBs which could benefit from a new capital charge."*

	BCBS text does state that *"The Committee will continue to evaluate eligibility on a case-by-case basis"* and specifies eligibility criteria for MDBs to be risk-weighted at 0%.
Treatment in national rules, compared to BCBS	• See **Figure 1** for a summary of how the jurisdictional requirements compare to the BCBS standards. **EU**: Specifies the same list of institutions eligible for 0% risk weight (RW) as BCBS. The EU Commission has the power to amend the list of 0% RW institutions. (Does also recognize some additional institutions as MDBs but not necessarily eligible for 0% RW: *Inter-American Investment Corporation, the Black Sea Trade and Development Bank, the Central American Bank for Economic Integration and the CAF-Development Bank of Latin America.) (CRR Article 117(1) and (2)).* **JP**: Specifies the same list of institutions eligible for 0% RW as BCBS. Not as clear as BCBS standards how institutions could become eligible for 0% RW. **UK**: Specifies the same list of institutions eligible for 0% RW as BCBS. (Like EU, does also recognize some additional institutions as MDBs but not necessarily eligible for 0% RW.) As part of Basel 3.1 implementation, the UK noted that: *"The PRA has decided not to publish criteria by which it would determine additional MDBs who would qualify for the 0% risk weight, but notes that it could consult to amend its rules if it considers that it would be appropriate to change the list in future." (*September 2024, PRA Near-final Basel 3.1 policy statement.) **US**: Takes a more restrictive approach to defining MDBs as the U.S. Federal Reserve's definition excludes the International Finance Facility for Immunisation, Asian Infrastructure Investment Bank and International Development Association from the BCBS list of 0% RW MDBs. To be defined as an MDB, the U.S. also requires that the *"U.S. government is a shareholder or contributing member or which the [Federal Reserve] Board determines poses comparable credit risk."* Not as clear as BCBS standards how institutions could become eligible for 0% RW. **ZA**: Specifies the same list of institutions eligible for 0% RW as BCBS. Not as clear as BCBS standards how institutions could become eligible for 0% RW.
Challenges for banking practitioners	If the regulatory capital treatment of MDB exposures is misaligned with the underlying risk, it unduly increases the cost to banks of engaging with MDBs/DFIs, which affects project viability and pricing and ultimately either reduces the availability of certain bank financing products in EMDE markets or increases the cost for end-users in those markets (e.g., governments). Some banks are constrained in their ability to engage with certain prospective clients or regions because their home supervisor does not recognize a particular institution as a low-risk MDB/DFI.
Policy options	**Near-term policy options:** • BCBS could work with member jurisdictions to update and expand its list of MDBs eligible for a 0% risk weight based on current eligibility criteria, also to include other eligible types of DFIs such as domestic development banks. Even if certain MDBs/DFIs are not deemed eligible for a 0% risk weight, they may be eligible on a risk basis for a lower risk weight than currently implied by the Basel standards. • Going forward, we recommend that BCBS commits to periodically reviewing its list of MDBs eligible for a 0% risk weight. • Jurisdictional authorities could review their own lists of eligible MDBs and align with a hopefully expanded list of BCBS-named institutions.

Figure 1: MDB/DFI Eligibility criteria - comparison between BCBS and jurisdictional implementations

BCBS	EU	JP	UK	US	ZA
Standards may lag recognition of emerging MDB institutions eligible for 0% RW	BCBS treatment, but recognizes some additional institutions as MDBs	Aligned with BCBS treatment	BCBS treatment, but recognizes some additional institutions as MDBs	More restrictive than BCBS list	Aligned with BCBS treatment

Color code for Figures 1 to 3:
Standards/Rules may impose fewer or no barriers
Standards/Rules may impose different barriers, or be less clear
Standards/Rules may impose barriers
Standards/Rules may impose more barriers



➢ **Barrier 2:** Insufficient recognition of benefits from co-financing structures, including A/B loans

Issue	Commercial banks can experience several benefits from joint lending or investments with an MDB or DFI, which often result in lower default rates. Reasons for this can include the MDB/DFI's expertise in due diligence and structuring, and their relationships with governments and others which can be beneficial to project success. In some types of transactions, the commercial bank may effectively inherit the benefits of the MDB's preferred creditor status – i.e., in the case of an A/B loan structure when the commercial bank purchases a participation in the B loan which the MDB offers alongside the A loan. This can also provide other benefits to the commercial bank lender such as preferred access to foreign exchange and exclusions from country debt rescheduling. However, prudential standards do not currently recognize the distinct risk reducing benefits of some co-financing structures, including A/B loans.[12]
Does this stem from BCBS standards?	**Not in text:** At present, the BCBS standards only recognize the credit risk mitigating benefits of MDB/DFI guarantees and the lower risk of banks' direct exposures to certain MDBs through the 0% risk weight for named MDBs. BCBS standards do not differentiate for bank lending or investments alongside MDBs/DFIs, even in the case of A/B loan which extend preferred creditor status of MDBs.
Treatment in national rules, compared to BCBS	Reflecting the BCBS standards, jurisdictional authorities in the EU, JP, SA, UK and US also do not differentiate for bank lending or investments alongside MDBs/DFIs, or preferred creditor status when this is inherited through an A/B loan structure.
Challenges for banking practitioners	The lack of regulatory distinction for these types of activities and structures can have several negative implications. It deters some banks from making the internal investments to pursue certain projects or asset types (such as B loans) at scale. Or, if a bank has appetite for these activities despite the risk-insensitive regulatory treatment, it must charge more, and those higher costs are passed on to the clients which runs counter to MDB/DFI objectives in general to mobilize finance to EMDE borrowers in the most accessible and cost-effective way.
Policy options	**Near-term policy options:**

[12] Although not the focus of this paper, the prudential treatment of credit insurance tends to weigh on commercial banks' appetite for investing in EMDEs. Banks generally cannot obtain meaningful capital risk relief from such insurance, even for MDB-originated B loans.

	• BCBS and member jurisdictions, alongside some MDBs/DFIs, could undertake analytical work to explore the risk characteristics of MDB/DFI co-lending and co-investment activities in order to assess the appropriateness of the current regulatory treatment. Ideally, this would leverage the rich GEMs database which, as described in Section 1, contains a significant amount of relevant credit risk data on loans provided by MDB/DFIs to EMDEs. The GEMs Consortium could work directly with the BCBS and potentially provide more detailed data than ordinarily published. **Longer-term policy options:** • Potential creation of new asset class(es) for regulatory purposes to distinguish between lending/investments conducted alongside MDBs/DFIs depending on certain characteristics such as whether or not the bank benefits from preferred creditor status, or certain project characteristics.

➢ **Barrier 3:** Credit risk mitigation recognition of MDB/DFI products and guarantees

Issue	Regulatory rules can fail to recognize the credit risk mitigating effect of some common MDB/DFI products and guarantees if the contracts do not meet requirements of 'unconditionality' and 'ability to pay out in a timely manner'. This can frequently occur, particularly for larger projects, due to insurance-related contractual requirements.[13] This also applies to Multilateral Investment Guarantee Agency's (MIGA) non-honoring public debt guarantee, which requires non-payout clauses for extreme events such as losses related to nuclear waste or weapons (see Article 6.2 in MIGA's template contract) regardless of the likelihood of nuclear activity in a jurisdiction. Other examples are cyber-attack and sanctions clauses in MDB/DFI guarantees, which create interpretation challenges about whether they meet the BCBS credit risk mitigation (CRM) criteria. In addition, the capital recognition of PRI products provided by MDBs/DFIs, which can be an important risk mitigation mechanism for lending to some EMDEs, can be limited under the standardized approach (SA) to credit risk and internal ratings based (IRB) approach. In the case of IRB, this links to the timeliness of payout since these often require an arbitration process before payout which may exceed the 90- or 180-day period in capital requirements after which an exposure is considered to be in default. While liquidity bridging tools can be applied to protect the bank during the arbitration process, it is often not clear to industry participants or MDBs/DFIs whether these would qualify under capital requirements.
Does this stem from BCBS standards?	**In text:** Yes. SA and IRB standards on credit risk mitigation: • CRE 22.71, CRE 21.15 refers to guarantees against convertibility and transfer risk but not political risk • CRE 36.105 **Not in text:** No clear reference to recognition of PRI products.
Treatment in national rules, compared to BCBS	• See **Figure 2** for a summary of how the jurisdictional requirements compare to the BCBS standards. **EU**: Reflects BCBS standards but Competent Authorities can permit greater CRM recognition. *"Conditional guarantees prescribing conditions under which the guarantor may not be obliged to perform may be recognised subject to permission of the competent authorities." (CRR Art 183 (1c) for IRB exposures.)*

[13] Many DFIs and MDBs, including MIGA, reinsure their guarantees in the commercial reinsurance market to manage their risk more effectively. Reinsurance underwriters, who handle pools of risk, typically require uniform, standardized clauses in all contracts within a particular pool. Consequently, to facilitate the reinsurance of their contracts, these institutions often employ standard "boilerplate" language in their guarantee agreements, which can introduce conditional elements.

	JP: Closely mirrors BCBS standards. While not referring to "irrevocable" guarantees, the Japanese rules require timely payment by the guarantee. *(FSA Administrative Notice on Capital Adequacy Rules pursuant to Article 14-2 of the Banking Act, Article 118-6)* **UK**: Reflects BCBS standards but has scope for firm judgement. UK's Basel 3.1 near-final implementation requires guarantees and credit derivatives to be "incontrovertible" and payable in a "timely manner". However, the text states that: *"When satisfying themselves that a guarantee or credit derivative is 'incontrovertible', firms should consider the terms of the guarantee or credit derivative itself and the remedies available under the law that applies to that guarantee or credit derivative."* (September 2024, PRA Near-final Basel 3.1 policy statement.) **US**: Reflects BCBS standards. The U.S. regulation requires a guarantee to be "unconditional" or "a contingent obligation of the U.S. government or its agencies, the enforceability of which is dependent upon some affirmative action on the part of the beneficiary of the guarantee or a third party…" not explicitly use the term "unconditional", its requirements align with the BCBS's intent by ensuring the enforceability and reliability of these instruments. *(U.S. Agencies' Regulatory Capital Rules; see Federal Register / Vol. 78, No. 198 / Friday, October 11, 2013 / Rules and Regulations.)* **ZA**: Closely mirrors BCBS standards, referring to "irrevocable" guarantees. *(Regulation 23, subregulation (7)(c)(v))*
Challenges for banking practitioners	The BCBS standards are overly restrictive/binary (certain products are either eligible or ineligible as a credit risk mitigant) and opaque in terms of CRM benefits of some MDB/DFI products and guarantees, including PRI. This permeates through the jurisdictional implementations but jurisdictional differences in implementation can increase complexity for cross-border banks as the degree of capital relief of a given transaction can depend on supervisory approach or the firm's interpretation of local rules.
Policy options	**Near-term policy options:** • BCBS review some common MDB/DFI products and guarantees and publish guidance to clarify the interpretation of the BCBS CRM standards with respect to common MDB/DFI guarantee clauses. Similarly, jurisdictional authorities could provide guidance about the eligibility of certain MDB/DFI guarantees for CRM purposes under jurisdictional rules. **Longer-term policy options:** • BCBS could evaluate the prudential treatment of PRI, also considering the relatively recent availability of liquidity bridging tools, to assess whether there are conditions under which PRI could meet the requirements for CRM. • In relation to guarantees, BCBS standards and jurisdictional implementations could permit IRB banks to estimate the likelihood of a non-payout clause being triggered and account for this in their regulatory capital treatment.

Figure 2: Credit risk mitigation recognition of MDB/DFI guarantees - comparison between BCBS and jurisdictional implementations

BCBS	EU	JP	UK	US	ZA
Standards may fail to recognize CRM effects of MDB/DFI guarantees due to standard contractual clauses	Competent Authorities can permit greater CRM recognition	Aligned with BCBS treatment	BCBS treatment with scope for firm judgement	Aligned with BCBS treatment	Aligned with BCBS treatment

➢ **Barrier 4:** Risk-insensitive regulatory treatment of project finance

Issue	Infrastructure projects in EMDEs are often developed in partnership with MDBs/DFIs. However, these projects can be less attractive to commercial banks, partly due to higher risk weights on project finance including infrastructure loans. Despite having lower default rates compared to investment-grade corporates and typically high recovery rates, project finance without an issue-specific rating (or in jurisdictions that do not allow the use of external ratings for prudential requirements) incur higher capital charges in the 'pre-operational phase' than unrated corporate exposures (130% vs. 100% RW). While the Basel 3.1 standards do differentiate the SA risk weights for exposures to unrated project finance issuers between the pre-operational and operational phases of a project, as well as for high vs. low-quality projects, the risk weight calibration is insensitive to key features of project finance. For example, there is still insufficient recognition of the declining risk level of many infrastructure projects over time for SA and IRB risk weights (see Chart 13 which shows that the marginal default rate on project finance is less than that of an investment-grade global corporate after five years) or the project characteristics influencing the risk exposure (e.g., construction risk level, project technology or track record of the project stakeholders). This also increases the gap between internal IRB RWA estimates using models calibrated to internal loss data and the SA risk weights, which can also be relevant to IRB banks given the overarching output floor constraint.[14] Furthermore, ambiguity persists regarding the criteria for what constitutes a high-quality project finance exposure to qualify for a lower risk weighting and the BCBS standards fail to fully acknowledge the creditworthiness of the project sponsors, including MDBs/DFIs. Other aspects of the Basel 3 standards, in particular the introduction of the Net Stable Funding Ratio (NSFR), have also been indicated as inhibitors to longer-term investments such as infrastructure investment.[15] However, the focus here is on the specific treatment of project finance within the BCBS standards and national requirements.
Does this stem from BCBS standards?	**Yes.** Standardized approach for credit risk (see Table 2): • CRE 20.50 describes that specialized lending, including project finance, should receive the same RWs as "base" corporate exposures if issue-specific external ratings are available and the bank operates in a jurisdiction that allows the use of external ratings. • CRE 20.51-20.52: For unrated project finance transactions, projects in the construction phase are risk-weighted a 130% and at 100% during the operational phase (where the latter is also the RW applied to unrated corporate exposures). Project finance exposures in the operational phase that are deemed to be high quality according to BCBS-specified criteria, are risk-weighted at 80%. "*For this purpose, operational phase is defined as the phase in which the entity that was specifically created to finance the project has (a) a positive net cash flow that is sufficient to cover any remaining contractual obligation, and (b) declining long term debt.*" Internal ratings-based approach for credit risk: • Basel 3.1 permits banks (subject to supervisory permissions) to continue to apply Advanced IRB or Foundation IRB models to specialized lending exposures, including project finance, in the same way as corporate exposures. The AIRB model formula for PD is linearly increasing in the maturity of an exposure. However, specific to specialized lending, it is also possible to apply so-called "supervisory slotting approaches". Supervisory slotting requires banks without permission to model the probability of default (PD) for specialized lending exposures to map their internal grade for an exposure to

[14] Basel 3.1 introduces an 'output floor' intended to ensure that banks' IRB capital requirements do not fall below 72.5% of capital requirements derived under the SA, applied at the level of total RWAs.
[15] See IIF/GFMA (2018) and others who have analyzed the issues.

	one of several supervisory buckets aligned with a specific RW (see CRE33); the buckets range from '*Strong'* to '*Weak*' or '*Default*'.
Treatment in national rules, compared to BCBS	**EU**: The SA treatment of specialized lending under CRR3 is aligned with Basel 3.1 (CRR Article 122a). However, CRR3 recognizes that *"Specialised lending exposures have risk characteristics that differ from those of general corporate exposures."* (Recital 30) This is reflected in a transitional implementation of the revised LGD input floors[16] for specialized lending under the IRB approach; the European Banking Authority is due to review the calibration of LGD input floors for specialized lending. Further, the EU continues to apply an "infrastructure supporting factor" applicable under both the SA and IRB approaches, which allows certain infrastructure finance and specialized lending exposures to receive a 25% haircut in capital requirements. CRR3 requires such exposures to *"contribute positively to one or more of the environmental objectives"* under the EU Taxonomy Regulation and not significantly harm any of the other environmental objectives (CRR Article 501a). **JP**: Closely mirrors Basel 3.1. **UK**: The UK is in the process of implementing Basel 3.1, so current requirements reflect Basel 3 and the EU's CRR2 requirements including an infrastructure support factor (dating from before the UK exited the EU). The UK authorities' proposed implementation of Basel 3.1 would be similar to the BCBS standards but for project/infrastructure finance but with some additional risk-adjusted accommodations. For SA exposures to high-quality project finance, the UK intends to permit the application of an 80% RW to a wider scope of eligible entities to recognize certain international organizations or MDB support for projects. Under the IRB slotting approach, the PRA proposes to introduce a new "Substantially Stronger" category in the slotting approach for project finance exposures, which would map to a lower RW of 50%. Finally, the UK proposes to remove the infrastructure support factor, but would introduce a firm-specific adjustment to Pillar 2 capital requirements to neutralize the capital impact for infrastructure exposures. **US**: The U.S. is yet to adopt Basel 3.1 and therefore continues to treat specialized lending similarly to corporate finance. As US prudential regulation does not permit reference to external ratings within the SA, a flat RW of 100% is generally applicable to specialized lending (similar to unrated corporate exposures). **ZA**: Closely mirrors Basel 3.1.
Challenges for banking practitioners	While Basel 3.1 takes a more granular approach to project finance, the calibration of SA risk weights is still not fully risk-sensitive and reflective of the characteristics of many project finance or infrastructure lending exposures, and the criteria to qualify for lower risk weights can be unclear. The different rate of implementing Basel 3.1 across jurisdictions, and differences in the detail of its application, create a fragmented regulatory landscape. These factors contribute to making such activities more expensive and complex for banks to participate in.
Policy options	**Near-term policy options:** • BCBS guidance to clarify the criteria for a project to qualify for "high-quality" project finance. • Jurisdictions to review the criteria for which the 80% RW for high-quality project finance may be applied to recognize domestic and bilateral development organizations' or MDBs' support for projects. **Longer-term policy options:** • BCBS to review the risk-sensitivity of the calibration of project finance SA requirements and consider adapting the AIRB model formula to recognize the inverse risk relationship between a project and the residual maturity. GEMs database could be used to inform this analysis.

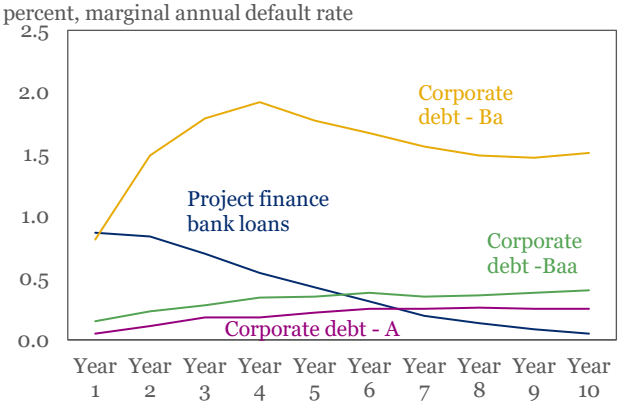
[16] Input floors are regulatory-specified minimum levels of an IRB model parameter – either PD or LGD.

Figure 3: Treatment of project finance and infrastructure finance - comparison between BCBS and jurisdictional implementations

BCBS	EU	JP	UK	US	ZA
Standards are insufficiently risk sensitive to nature of project and infrastructure finance	More recognition that specialized lending and infrastructure finance have a different risk profile to corporate exposures	Aligned with BCBS treatment	More recognition that specialized lending and infrastructure finance have a different risk profile to corporate exposures	Does not reflect latest differentiation between project finance and corporate finance from Basel 3.1	Aligned with BCBS treatment

Chart 13: Marginal default rates for project finance becomes less than that of investment-grade corporate debt after 5-6 years

percent, marginal annual default rate



Source: IIF; Moody's

Table 2: Project finance exposures generally receive the same capital requirements as general corporates, or higher under the standardized approach

Exposures to project finance, object finance, and commodities finance

Exposure (excluding real estate)	Project finance	Object and commodity finance
Issue-specific ratings available and permitted	Same as for general corporate	
Rating not available or not permitted	130% pre-operational phase 100% operational phase 80% operational phase (high-quality)	100%

Source: BCBS, "High-level summary of Basel III reforms," December 2017