IDB Board of Governors Approves Transfer of the Net Assets of the Fund for Special Operations to the Ordinary Capital Resources to Strengthen and Sustain Concessional Assistance

How and when does this transfer take place?

- On January 1, 2017 all of the assets and liabilities of the IDB's Fund for Special Operations (FSO) will be transferred to the IDB's Ordinary Capital (OC) resources and reflected in the IDB's balance sheet.
- From that date forward, there will be no new loans financed from the FSO.
- Future concessional lending will be provided by the blending of loans at regular lending spread for Sovereign guaranteed operations and loans at concessional spreads.
- The purpose of the FSO contributions made by member countries will not change; the transferred assets will continue to support concessional lending, potentially expanding the "lifecycle" of the resources and supporting the poorest countries in Latin America and the Caribbean.

What FSO assets and liabilities are being transferred?

- All assets and liabilities of the FSO will be transferred to the IDB's ordinary capital. As of December 31, 2015 the FSO had roughly US$5.4 billion of assets, comprised of US$4.5 billion of loans outstanding and US$0.8 billion of cash and investments. Liabilities represented approximately US$0.3 billion.

Why is this transfer necessary or desirable?

- The transfer is necessary because the FSO's ability to provide concessional assistance in the future would likely have fallen far short of the probable demand.

- The lending capacity of the FSO was projected to diminish after 2016, as all available liquidity would have been allocated to concessional loans.
- The transfer will be symbiotically beneficial for the FSO and OC because, on the one hand, the OC does not have liquidity constraints, while, on the other hand, the FSO's net assets will provide a significant boost to the OC's equity.

How will the transfer affect concessional lending to the poorest IDB member countries?

- The transfer will ensure the Bank's ability to sustain and expand, consistently with growth of Bank operations, concessional lending levels to the poorest IDB member countries.
- Without the transfer, concessional lending from 2017-2028 was projected to amount to US$1.5 billion. By contrast, following the transfer, concessional lending will likely range from a minimum of US$3.5 billion to a maximum of US$4.7 billion over the same period.

Will the grant-element/degree of concessionality provided be affected?

- No, the transfer will not affect the grant-element of concessional loans.
- The degree of concessionality provided will continue to be tailored to the external debt sustainability situation of each concessional-eligible country, in accordance with the World Bank-IMF Debt Sustainability Framework (DSF) for Low-Income Countries.

Will the transfer affect loan terms to the poorest countries?

- Low-income countries currently receive blended loans whereby one part of a loan comes from the FSO and the other part comes from the OC. The system of blending will continue but loans on concessional terms will be granted through the Bank's Ordinary Capital. These loans' concessional terms will remain unchanged compared to those offered through the FSO today.
- The financial terms and conditions of the loans granted on regular terms through the Ordinary Capital will become harmonized with those applicable to OC borrowing member countries. This shift will provide the poorest countries with increased flexibility and options, while not adversely affecting the concessionality of the Regular OC portion of the loan.

Will the transfer affect the performance-based allocation system for concessional assistance?

- The transfer will not affect the framework governing the allocation of concessional resources.

- The IDB will continue to allocate concessional lending resources in accordance with the Enhanced Performance-Based Allocation (EPBA)/Debt Sustainability Framework (DSF), which was introduced in 2007.
- As such, concessional resources will continue to be determined by a combination of country needs and institutional and portfolio performance, using exactly the same allocation formula and methodology currently in place.
- Consequently, the IDB will maintain the harmonization of its performance-based allocation system with other multilateral development banks and international financial agencies.

Which countries will be eligible for concessional assistance?

- As part of the transfer, the criteria regarding country eligibility for concessional resources have been updated.
- The per capita income threshold that the Bank has used to determine eligibility for concessional resources since 1993 will be maintained constant in inflation-adjusted terms. Updated to 2015 prices, it will now stand at a Gross National Income (GNI) per capita of US$2,834.
- The per capita income criterion will be complemented by a creditworthiness criterion. A small and vulnerable borrowing member country with a per capita income above but not higher than two-times the income threshold may be eligible for concessional resources if it is determined that the country lacks sufficient creditworthiness for OC-only borrowing.
- In practical terms, in the short term, no countries will either lose or gain eligibility for concessional lending due the updates in the eligibility criteria.

How will the transfer affect Haiti?

- The transfer will not affect Haiti in the short term. Per the Ninth General Increase in the Resources of the IDB (GCI-9), concessional assistance for Haiti will be channeled through the IDB Grant Facility.
- However, the transfer will provide Haiti with a medium-term path back into the IDB's standard concessional resource framework and access to concessional resources post-2020. Hence, after 2020 the transfer will provide the same assurance to Haiti of the continued availability of concessional resources as it does to other concessional-eligible borrowing member countries.

Will the transfer lessen the focus on the poorest and most vulnerable countries?

- No. On the contrary, although the transfer will benefit all IDB borrowing member countries, the poorest and most vulnerable countries will be the primary beneficiaries.
- Although the concessional assistance-eligible countries accounted for only 1.5 percent of Latin America and the Caribbean's Gross Domestic Product and

4.5 percent of its population, in 2015 these countries accounted for 11.5 percent of the volume of sovereign-guaranteed loans approved by the IDB.

- The share for poor countries will be locked-in at this historically-high level.

What impact will the transfer have on the IDB's Ordinary Capital (OC)?

- The transfer of the FSO's assets and liabilities to the OC will boost the OC's equity by approximately 20 percent, thereby significantly strengthening its capital position in the short to medium term.
- Although the transferred FSO loan portfolio has a slightly lower average rating than the existing OC sovereign-guaranteed loan portfolio, merging the two loan portfolios will bring important portfolio diversification benefits.
- Depending on the evolution of interest rates, the cost of providing concessional lending will over the long run erode the initial benefits to the capital position.
- Overall, the financial impact will be to strengthen buffers against economic downturns and enhance the operational capacity of the Bank.

Will the transfer affect the IDB's AAA credit rating?

- No. On the contrary, the transfer of FSO assets and liabilities strengthens IDB capital position.
- In order to provide an external review of the financial impact of the transfer, the Bank engaged a rating evaluation service from two rating agencies to provide feedback on the potential indicative ratings on several of the principal financial scenarios considered in the transfer for two points in time: 2017 and 2026.
- Both rating agencies concluded that there would be no change to the IDB's AAA rating or its outlook in any of the scenarios presented, either in 2017 or 2026.

Will the transfer affect shareholdings and voting rights in the IDB?

- No. The transfer does not involve an increase in ordinary capital shares, or subscriptions by member countries, under the Charter of the IDB.
- Under United States Generally Accepted Accounting Principles (US GAAP), the transfer should be accounted for following guidance for transactions between entities under common control and as a transfer of capital nature. The difference between FSO assets and liabilities will be recognized as Additional Paid-in Capital (APIC). Member countries will not be required to subscribe to additional OC shares; instead the APIC would be deemed to relate to the OC's existing Paid-in capital stock, but without having an impact on the nominal values of the existing capital stock or voting rights.

Will the transfer affect the organizational structure and staffing at the IDB?

- No. The transfer will not require any organizational restructuring or increase in staffing at the IDB. On the contrary, increased internal harmonization and simplification would tend to slightly reduce administrative costs, after an initial transition.

How does this transfer relate to other reforms the IDB has undertaken?

- Since 2013 the international community – especially the G20 Leaders – have called upon the multilateral development banks to optimize their balance sheets, with a view toward enhancing their lending capacities.
- The transfer represents the fifth step that the IDB has taken to optimize its balance sheet, following net income measures, increased capital efficiency, the development of exposure exchange agreements with other multilateral development banks, and risk-sharing in non-sovereign operations.
- The design of the FSO transfer benefited from the example of a similar reform being undertaken at the Asian Development Bank (ADB).

What is the current status of the transfer and what are the next steps?

- On July 27, 2016, the Bank's Board of Executive Directors authorized submitting the proposal to transfer the FSO assets and liabilities to the OC for the approval of the Bank´s Board of Governors.
- The Board of Governors unanimously approved the transfer on September 1, 2016.
- The transfer will become effective on January 1, 2017.