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Report of the Taskforce on Innovative Financing

Pre-read

For Decision

Decision Point

The Board acknowledges that the Task Force for Innovative Financing for Malaria has fulfilled its mandate in developing the Business Plan for the Malaria Bond and acknowledges the Business Plan and its recommendations. The Board endorses the recommendations of the Taskforce on Innovative Financing for Malaria regarding the next steps, specifically:

- Governance. Establish a new taskforce or mandate the Task Force for Innovative Financing for Malaria to take on the role as Multi-stakeholder Design Team which will take responsibility for the next phase of the malaria bond.
- Outreach. Implement the marketing and outreach towards key stakeholders
- Technical design. Refine the analysis on the structure of the bond

The Board notes and agrees the Task Force's recommendation that the Multi stakeholder design team works actively on engaging in outreach activities and refining the technical design in the next six months and report back at the 22nd Board meeting.

The Board also takes notes of the two concept papers on the Diaspora Bond and a Private Sector Bond and suggest that the experiences of establishing the Malaria Bond will be used to assess the actual feasibility of implementing a Diaspora Bond or tapping into existing Diaspora Bonds. The Board further suggests the Multi-stakeholder Design Team to explore further the Private Sector bond while establishing the Malaria Bond.

This decision is expected to have a budgetary implication of USD 150K, which will come out of the overall setup budget (USD 550K-800K). However it should be noted that funds have been identified for this and therefore it will not have budgetary implications for the PWP 2012.

PURPOSE:

The Taskforce on Innovative Financing for Malaria was set up by the Resource Mobilization Sub-Committee at its first meeting on March 1st 2011. During the board meeting of May 2011, the Board endorsed the recommendations of the Taskforce on Innovative Financing for Malaria regarding the development of specific business plan for the Malaria Bond. This report informs the Board of the work that the Taskforce has carried out during the past weeks to develop the business plan. A list of the Taskforce members can be found in Annex 1.

I. Background

The Resource Mobilization Sub-Committee created the Taskforce to map innovative financing mechanisms and assess their potential to raise additional and predictable funding for the Global Malaria Action Plan (GMAP). Following the Board decision in May 2011, the Task Force was tasked with developing a business plan for the launch of a Malaria Bond as well as prioritizing the remaining options. This prioritization led the Task Force to decide to look more specifically at diaspora bonds, and it was decided by the group to develop a concept note on the diaspora bonds, but postpone the final analysis until learnings had come through on the Malaria Bond.

This pre-read shows the findings and recommendations of the business plan. The Board is requested to approve moving forward with the set-up of the malaria bond. The approach and findings are summarized in the sections below.

II. Summary of Achievements to Date

Below is a short summary of the main sections in the Business Plan for the Malaria Bond:

Description of a Malaria Bond – The most promising option is a mechanism where a donor fully pays only if implementers deliver results. As the implementer requires additional funds to complete the interventions, the bond allows the implementer to borrow these funds from socially-minded private sector investors.

The bond creates value by realizing cost-efficiencies in funds disbursement, funds allocation and/or program implementation. These cost efficiencies are realized by aligning the incentives of donors and implementing agencies through pay for performance. Monetary contribution and financial risk incentivize the implementer to increase efficiency, and may ultimately translate in reduced payments by the donor for the same intervention.

Costs and benefits –The malaria bond's possible benefits are the following:

- **Lowering costs of malaria interventions**, by paying for performance and thus aligning incentives and stimulating cost efficiencies
- **Tapping into the private investor market**, thus potentially freeing up donor resources
- **Strengthening the development and economic growth of endemic countries**, as increased malaria interventions will have strong societal benefits, for example by lowering health care costs due to decreased hospitalization and by enhancing workers' productivity in the long run

The bond aims to reach these objectives by measuring and compensating performance, and by dividing the risks and returns across a range of stakeholders, including private sector investors.

Set-up options - We have identified three main options for the malaria bond. Each of the options includes performance incentives for the implementer. The options are different with regards to risk for the individual investors (e.g. can they lose their principal) and with regards to the different parties sharing the risk.

The options and their implications in case of success or failure are presented below:

Option	Private investor	Donors	Implementing organization	Issuing agency
Full risk	<p>Action: the private investor buys a bond to finance malaria intervention (transfer of funds to the issuing agency)</p> <p>Success: the investor receives the principal and a return</p> <p>Failure: the investor loses part of the principal</p>	<p>Action: it commits to pay the issuing agency based on the success of the intervention</p> <p>Success: it pays principal and return to the issuing agency. It also pays an additional contribution to the implementing organization</p> <p>Failure: no disbursement</p>	<p>Action: Responsible for execution of the initiative. The implementer is required to pre-finance part of the intervention out of its own resources</p> <p>Success: it receives the second tranche of the investment and an additional contribution</p> <p>Failure: it does not receive any additional funds</p>	<p>Action: it provides the implementing organization with the first tranche of investment, as the first tranche of the investors' funds</p> <p>Success: It provides the implementing organization with the second tranche</p> <p>Failure: it repays the second tranche to the investor</p>
Risk participation	<p>Action: <i>same as above</i></p> <p>Success: the investor receives the repayment of the principal and the return</p> <p>Failure: the investor receives the repayment of the principal</p>	<p>Action: <i>same as above</i></p> <p>Success: <i>same as above</i></p> <p>Failure: it pays to the issuing agency the share of the principal invested in the initiative</p>	<p>Action: <i>same as above</i></p> <p>Success: <i>same as above</i></p> <p>Failure: <i>same as above</i></p>	<p>Action: <i>same as above</i></p> <p>Success: <i>same as above</i></p> <p>Failure: it repays the principal to the investor</p>
Guaranteed return	<p>Action: <i>same as above</i></p> <p>Success/Failure: the investor receives the repayment of the principal and a low guaranteed return</p>	<p>Action: <i>same as above</i></p> <p>Success: <i>same as above</i></p> <p>Failure: it pays principal and a low guaranteed return to the issuing agency</p>	<p>Action: <i>same as above</i></p> <p>Success: <i>same as above</i></p> <p>Failure: <i>same as above</i></p>	<p>Action: <i>same as above</i></p> <p>Success: <i>same as above</i></p> <p>Failure: it repays the principal and a low guaranteed return to the investor</p>

Based on preliminary analysis, it seems that the *full risk* and the *risk participation* options are the most feasible. The risk profile of the first option may be too aggressive for a pilot; however it can represent an opportunity to engage a diversified group of investors such as social and diaspora investors for follow-on malaria bonds. The second option is less aggressive, as the repayment of the principal is guaranteed, and probably more suitable for the pilot.

The Taskforce agreed that **a structure that aggregates the two options above is probably the most feasible solution**. This will allow the malaria bond to consist of two individual financial products, one product for investors who seek guaranteed principal and one where the principal is at risk.

In addition the Taskforce agreed that, independently from the option selected, **the success of the intervention should be defined across a range of different levels. The donor's repayment should be structured accordingly in line with the level of success.**

Possible commodities - These options can be applied to the provision of multiple commodities such as indoor residual spraying (IRS), artemisinin combination therapies (ACTs) and rapid diagnostic test (RDT), long-lasting insecticidal nets (LLINs), or vaccines for malaria¹. A few principles need to be considered in order to choose the most suitable commodity or commodities:

- Interest of donors for the specific commodity
- Interest of investors for the specific commodity
- Applicability and relevance of the intervention to the malaria situation in-country
- Availability of implementers that can carry the risk and are willing to participate
- Possibility to be measured by indicators

The Business Plan presents emerging thoughts for the selection of the most suitable commodity.

Possible implementing organizations - Once the commodity has been selected, further analysis is needed to select the implementer. The implementing organization should meet the following requirements:

- Strong governance and financial management
- Significant cash reserve/equity to contribute to the upfront part of the upfront investment / take liability for part of the risk of the intervention
- Strong managerial and operational practices, to maximize probability of success and cost efficiencies

The implementing organization's experience in monitoring and evaluation of malaria interventions should not be a critical requirement. The M&E function will most probably be carried by a third party as illustrated by the two options below:

- **Option 1:** the implementing organization collects and analyzes the data and a third party auditing entity validates the results
- **Option 2:** the third party auditing entity collects and analyzes the data, and validates the results

^{1 1} Due to the complexities in measuring performance the initial proof-of-concept offering would likely be for commodities only, future offerings could also address the critical need for funding Research and Development into new, innovative interventions against malaria (drugs, insecticides, RDTs and vaccines) in line with the elimination/eradication agenda.

In addition, a variant of the setup for the malaria bond could be to have a back-up implementer to step in if the first implementer would not show the desired results. However, there would be additional costs associated with setting up a back-up implementer, and part of the funds will already be spent by the first implementer.

Set-up and ongoing costs – The Taskforce prepared a preliminary budget for setting up and managing a four year malaria bond. This budget is based on a \$50 million bond issue. The total costs for set-up and ongoing operations are estimated to be ~\$1.7-2.3 million (~3.4-4.6% of issue). The detailed estimate of annual costs is included in the business plan.

Global Health Metrics – The health metrics are essential for setting up the model of pay for performance. The Task Force agreed that indicators should have high scores on attribution, measurability, objectivity, and cost efficiency. The indicator should be **attributable** to the intervention financed by the bond, and not be unduly influenced by external events such as weather patterns, or by similar interventions of other implementers. The indicator should not **measure** a result that is not part of the intended results of the intervention. The data for the indicator should be collected by an external **objective party** that has no conflict of interest vis-à-vis the outcomes of the indicator. Moreover, the data collection should be straightforward and replicable, allowing all parties to validate the results. Finally, the collection of indicators should be **cost efficient** by maintaining a balance between cost incurred and benefits provided.

A select group of output and outcome indicators seems the most useful instruments to measure success of funded interventions. Impact indicators give maximum freedom to implementers to choose the most effective interventions to reach their goals. However, impact indicators such as mortality and morbidity take time to manifest, and may require more expensive data collection and analysis. Furthermore, the attribution to a specific intervention is weak.

Governance and organization - The governance structure of a malaria bond should demonstrate the following principles:

- Simple transparent cash flows
- Credible treasury manager
- Oversight function to ensure achievement of financial sustainability and developmental goals
- Independence of funding and performance decisions from parties with financial vested interests
- Multi-stakeholder Design Team ceases to exist after the launch of the mechanism

These principles can be converted into a structure that ensures decisions are made with no vested interests, whilst ensuring there is one body responsible for overall decision making. The Executive Manager Board, Treasury Manager and Performance Management Committee functions should be kept separate and independent from each other to ensure transparency and oversight. The Multi-stakeholder Design Team should ensure that each entity has a clear mandate and that no duplication occurs. In addition the organization should be committed to use the existing structure as much as possible in order to avoid duplications.

Concept notes – The Board decides that the Task Force should look at the possibility of creating a diaspora bond. The Task Force developed the attached concept note on the feasibility of either creating a specific diaspora bond or tapping into existing diaspora bonds for malaria. During the development of the Business Plan another concept was discussed, namely the possibility of using the bond mechanism to implement malaria activities in the Private Sector, to be repaid by the Private Sector based on performance such as reduction in number of sick days, increased productivity etc. A concept note for this type of bond is attached.

III. Next Steps and Challenges Ahead

The key next steps to move towards the launch of this mechanism are outlined below. As mentioned under the marketing and communication plan, the key success requirement for the next phase is obtaining donor interest, both for the overall feasibility of the bond and for unlocking resources to further develop the technical design.

- **Governance.** Establish a new taskforce (Multi-stakeholder Design Team) which will take responsibility for the next phase of the malaria bond, including outreach towards donors and development of the technical design
- **Outreach.** Implement the marketing and outreach towards key stakeholders
- **Technical design.** Refine the analysis on the structure of the bond

IV. Request Board Action

Decision Point

The Board acknowledges that the Task Force for Innovative Financing for Malaria has fulfilled its mandate in developing the Business Plan for the Malaria Bond and acknowledges the Business Plan and its recommendations. The Board endorses the recommendations of the Taskforce on Innovative Financing for Malaria regarding the next steps, specifically:

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V. Contacts

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Annex 1 – List of Task Force Members

Chair

Mikkel Vestergaard

Vestergaard Frandsen

Other members

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Medicines for Malaria Venture

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