

Additionality by Design, Not Assertion: From Opaque Concessionality to Credible Mobilization

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- This is Article 1 of *'The Great Development Finance Write-Off'* series.
- DFIs and MDBs have latent donation layers that compromise their risk-return metrics and capital ratios.
- Left unchecked, opaque grant-equivalent components can trigger covenant breaches, rating downgrades, and donor mistrust—undermining institutional reputation.
- Read on to see how tagging every grant-equivalent component—from interest rate discounts to advisory fee waivers—safeguards capital buffers, enforces risk limits, and delivers fully transparent ODA reporting.

Boards of Development Finance Institutions (DFIs) and Multilateral Development Banks (MDBs) overseeing non-sovereign guaranteed operations (NSGOs) strive to maximize development impact while safeguarding balance-sheet strength and maintaining best-in-class standards. However, development impact is not well-defined: DFIs and MDBs use incommensurable proxies with inconsistent units (number of jobs created, percentage of emissions reduced, volume of transactions approved, etc.) that defy aggregation, hinder cross-institutional benchmarking, and rarely help differentiate between public-sector mandates from private-sector finance. In the absence of commensurable and consistent metrics, NSGOs are instead constrained by the principle of Additionality. Yet, being a constraint, Additionality cannot guarantee optimality. Moreover, claims of so-called “financing gaps” further distract from the core objective of maximizing development impact. In practice, DFIs often prioritize USD volumes mobilized—a metric that bears no direct relationship to development impact. This fixation on size over substance undermines mission alignment.

Predictably, the wrong focus leads to the wrong process. This misalignment fractures pricing, risk management, concessionality accounting, and impact measurement into separate silos. As a consequence, Additionality and mobilization are viewed narrowly as preventing the crowding-out of the private sector and promoting the crowding-in of the private sector, respectively. This narrow view obfuscates the reality that both the private sector and the public sector serve the interests of individuals. Individuals elect managements and governments, and individuals finance firms and countries: individuals finance both private and public goods and services. When Additionality and mobilization are not clearly defined, public resources may be channeled into interventions that do not meet the core criteria of non-excludability and non-rivalry for public goods and services. Conversely, when Additionality and mobilization are clearly defined, catalyzation can be identified as a performance metric, and replicability and scalability can be properly appreciated.

Besides Additionality, NSGOs are constrained by the principle of Non-Distortion: DFIs and MDBs must transact on commercial market—or fair, according to commercial markets—prices, with minimum concessionality, which is defined as the difference between the commercial market price and the traded price, permitted only in Blended Finance. Thus, Additionality and Non-Distortion are not naturally aligned: Additionality, which demands that DFIs and MDBs not displace private finance, causes market segmentation, while Non-Distortion forces DFIs and MDBs to operate on commercial market terms.

The model proposed in Kolev's *"Pricing Development Assets in Non-Sovereign Guaranteed Operations,"* acknowledging the market segmentation mentioned above, introduces a new concept: "donation," defined as the difference between the development market price and the traded price. It advances a coherent economic logic that parallels generally accepted Financial Economics thinking: a development agent, such as a DFI or an MDB, seeks to maximize development impact via donations and uses development investments to transfer donation capacity across time. Hence, Additionality requires targeting true market failures, and Non-Distortion juxtaposes the perspectives of commercial institutions and development institutions. To secure the firm backing of their member countries, DFIs and MDBs should value correctly and record explicitly price differences, pro bono advisory work, and technical assistance as donations. They should structure co-financed projects with distinct risk-return layers for private and public tranches. Finally, linking general capital increases from member countries to donation metrics motivates DFIs and MDBs to shift institutional priorities from transactional volume approved to development impact delivered.

Once the distinction between commercial markets and development markets is acknowledged, DFIs and MDBs can assess their performance and manage their balance sheets effectively. The added clarity enables superior pricing of risks and views of exposures. With concessionality and donation well-defined, DFIs and MDBs can compute concessionality elements to comply with Non-Distortion, and they can compute donation elements to determine impact-maximizing donation paths. Member countries can affect optimal paths—and, thereby, strengthen key functions, such as countercyclicality—through incentives linked to donation elements. Also, by structurally requiring DFIs and MDBs to value and record price differences, pro bono advisory work, and technical assistance, member states can ensure that official development assistance (ODA) associated with their equity capital is transparently reported.

ODA, which is rooted in the concept of government aid, is operationalized through grants and grant equivalents. The terms "aid," "concession," "donation," and "grant" are conceptually distinct yet economically interlinked. In Kolev's model, since individuals finance and control both firms and governments, DFIs and MDBs can be recognized by their donation deployment activities. Taxes—the source of government aid—are therefore not burdens but the price paid for public goods and services. Because a government's aid allocation cannot possibly reflect the optimal aid allocations of individuals, philanthropy emerges as a complement. Since individuals can only add onto—and not subtract from—a

government's aid allocation, DFIs and MDBs—being sovereign policy tools—must maintain additional, impact-maximizing, measurable, and transparent donation paths. Overreliance on approval volumes, concessional amounts, impact proxies, and crowding-in ratios fosters institutional opacity, undermines accountability, and ultimately erodes legitimacy and support.

The need is evident. In the case of NSGOs, a necessary condition for Additionality is for DFI and MDB positions to be lower in the capital stack relative to the positions of private investors. Furthermore, for mobilization—which is also known as co-financing—to be defensible, any concessionality element should be appropriately separated and transparently reported by commercial institutions. When asset quality is not masked by concessionality, capital adequacy and solvency metrics are preserved. Similarly, all donation elements should be rigorously calculated and regularly disclosed by DFIs and MDBs, enabling informed discussions with member countries on general capital increases.

To operationalize the framework, DFIs and MDBs should establish a small cross-functional team (Evaluation, Legal, Risk, and Treasury). Should they wish to apply consistent methodologies and uniform standards, DFIs and MDBs may establish such a team jointly across institutions. The team's role would be to create pricing models for commercial and development markets, monitor concessionality and donation patterns for compliance with Non-Distortion and impact-maximization principles, and maintain records of pro bono advisory work and technical assistance that accompany development investments. In addition, recognizing that Additionality is merely a constraint rather than an objective, the team could assess the viability of projects, ensuring that, while seeking to achieve bankability, concessionality does not transfer value among the various investors unreasonably. Lastly, as a service to member countries, the team could quantify the ODA associated with their equity capital.

Once concessional and donation elements are correctly tagged, catalytic effects can be distinguished from ordinary co-financing with consistency across transactions. By modeling development agent behavior, *"Pricing Development Assets in Non-Sovereign Guaranteed Operations"* provides a framework that clarifies the true meaning of mobilization. If a DFI and an asset manager co-finance a project on identical terms, how can they be distinguished, and who, if anyone, "mobilized" whom? Neither originating nor sponsoring a deal constitutes mobilization, nor does acting as an "anchor investor" in an oversubscribed bond issue managed by leading banks. Likewise, syndication, which is primarily about risk sharing and resource pooling, is not mobilization. Scarce DFI and MDB resources should instead be prudently directed towards high-impact initiatives that, while satisfying the principles of Additionality and Non-Distortion, mobilize the private sector by taking junior positions and quantifying concessionality.

In our next article, we shall show how Ministries of Finance can embed explicit grant-equivalent tagging in national budgets, benchmark concessional and donation elements

within their debt-sustainability frameworks, and deploy a “future donation frontier” to align fiscal planning with development impact.

Definitions:

1. *Non-sovereign guaranteed operation* (NSGO): An investment made by an MDB without a sovereign guarantee. By definition, all DFI operations are NSGOs.
2. *Concessionality*: The difference between the commercial market price and the actual traded price of an instrument, e.g., the subsidy embedded in loan terms.
3. *Donation*: The difference between the development market price and the actual traded price, i.e., the public-sector “grant equivalent” component.
4. *Additionality*: The principle that, in NSGOs, DFIs and MDBs do not undertake any financing for which sufficient private capital can be obtained on reasonable terms.
5. *Non-Distortion*: The principle that, in NSGOs, DFIs and MDBs undertake financing on terms and conditions normally obtained by private-sector investors for similar financing.