

From Donations to Discount Rates: Aligning Commercial and Development Markets

Nick Kolev and Amil Aneja

- This is Article 2 of *'The Great Development Finance Write-Off'* series.
- A Ministry of Finance contends with undisclosed concessional flows that distort project viability, skew debt-sustainability and economic-growth metrics, and undermine medium-term fiscal planning.
- Untagged grant-equivalents misstate the actual economic cost of projects and lead to under-recognition of sovereign commitments, thereby eroding parliamentary and investor confidence.
- Read on to learn how monitoring latent concessional elements (below-market pricing or pro bono in-kind support) and donation elements empowers a Ministry of Finance to steer public resources towards the highest-impact priorities.

A Ministry of Finance (MoF) safeguards macroeconomic stability—raising revenue, allocating expenditure, managing debt, and sustaining growth—while also supervising a growing stream of exposures through concessional instruments and Blended Finance structures, the terms of which are seldom disclosed in a format consistent with domestic borrowing. When grant-equivalents are embedded in exposure prices, MoFs cannot trace concessional terms through fiscal tables, explain them to parliament or rating agencies, or estimate and forecast their costs or benefits. The result is avoidable uncertainty that undermines both annual appropriations and debt-sustainability planning.

At the same time, many MoFs—especially in low- and middle-income countries—lack the tools to price financial instruments, quantify embedded grants, or evaluate the budgetary impact of Blended Finance structures on national budgets. In sovereign guaranteed operations, multilateral development banks (MDBs) extend loans either at fixed rates or at fixed spreads over MDBs' borrowing costs, as determined by member countries. Yet, the MoFs of borrowing member countries often fail to integrate concessionality into unified fiscal frameworks or to distinguish the benefits of concessionality from a project's underlying viability. In non-sovereign guaranteed operations (NSGOs), where a formal "no objection" is required from a development finance institution (DFI) or an MDB, MoFs rarely identify or restructure below-market terms. This opacity, compounded by limited internal capacity to model concessional terms, perpetuates inefficiencies in the international financial architecture and constrains MoFs' abilities to deploy scarce resources for maximum development impact.

Another constraint on the optimal deployment of scarce resources is the absence of a clear definition of development impact. Despite the use of proxies—such as number of jobs created, volume of transactions approved, or percentage of emissions reduced—even development professionals struggle to articulate the concept or agree on its unit of measurement. In *"Pricing Development Assets in Non-Sovereign Guaranteed Operations,"* Nick

Kolev, recognizing that individuals ultimately finance and control both firms and governments, models development impact by drawing a parallel between the behavior of a development agent and the behavior of an economic agent:

1. While economic agents maximize utility as a function of consumption, development agents maximize development impact as a function of donations;
2. In NSGOs, because interventions must satisfy the principle of Additionality, commercial markets and development markets are segmented;
3. Both agent types use investments for intertemporal transfers—development agents in the development market and economic agents in the commercial market;
4. Development agents require regular resource injections because, due to the principle of Non-Distortion, both development agents and economic agents finance projects on commercial market terms, but only development agents offer donations;
5. A development agent determines donation volume based on incentives provided by its sovereign shareholders; and
6. While concessionality is the difference between the commercial market—or fair—price and the traded price, donation is the difference between the development market price and the traded price.

From this, concessionality represents a price difference from the perspective of a commercial institution, while donation represents a price difference from the perspective of a development institution. Crucially, if the traded price equals the commercial market price, there is no concessionality element, but there can still be a donation element.

In effect, Kolev's model requires every element of concessionality and donation—whether an interest rate discount or pro bono advisory work—to be explicitly and systematically recorded. Tracking and benchmarking these elements enables MoFs to negotiate balanced risk-sharing, align concessionality with sustainability targets, steer DFI and MDB operations, and rank projects by impact-to-cost metrics.

By recognizing development investments as means of intertemporal transfer of donation capacity, MoFs can also calculate a “future donation frontier” and embed it into medium-term budget frameworks. Under this view, each commitment expands rather than constrains future fiscal space, enabling greater social spending. Integrating Kolev's framework into core MoF operations is both feasible and essential: it transforms opaque aid flows into actionable data, safeguards macro-fiscal stability, and positions MoFs to secure and allocate concessional capital on transparent, impact-driven terms.

Lastly, by measuring donations and linking them to resource injections, Kolev's model provides MoFs with a direct policy lever to influence DFI and MDB behavior in NSGOs. First, development impact, which has been historically nebulous, can be enforced by focusing exclusively on activities within the remits of development agents. Second,

countercyclicality, which has been frequently uncertain in NSGOs, can be incentivized through explicit linkage of general capital increases to actual grant-equivalent deployment.

Acknowledging legitimate reservations—around legacy systems, headcount constraints, political calendars, donor pushback, and the unfamiliar “development market” benchmark—implementation can nonetheless proceed in a single, time-boxed pilot. By mandating a ministerial decree to designate a single owner for grant-equivalent accounting and empowering a small cross-functional team with off-the-shelf yield benchmarks and reporting templates, MoFs can demonstrate turnkey tagging of below-market differentials as line items without overhauling core technology systems. This phased proof-of-concept dispels doubts, delivers immediate gains in fiscal transparency and debt-sustainability forecasting, and creates the conditions for full-scale adoption.

In our next article, we shall explain how institutional investors and asset managers can use these same principles to protect fiduciary duties while channeling private capital into emerging market and developing economies.

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 typically obtained by private-sector investors for similar financing.