Water for Women
WASH Blended Finance Research Report

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Executive Summary

There is general consensus that traditional foreign aid and public sector resources will not be sufficient to meet the investment gap required to achieve Sustainable Development Goal (SDG) 6 of universal WASH access. In response, the development finance industry has embraced a host of ‘blended’ or ‘innovative’ financing approaches premised on the idea that public sector and donor funds can be used to incentivize/accelerate the entry of additional capital sources. Although examples of successful blended finance can be found globally across many sectors, the WASH sector and certain market contexts in the Asia Pacific face particular challenges when it comes to the application of blended finance, such as lack of demand for WASH goods/services, low absorptive capacity of WASH providers, lack of funder coordination, and limited track record of blended finance successes.

DFAT has been a leading catalytic WASH funder for the Asia Pacific region through the Water for Women Fund, where DFAT’s funding mode to date has been that of traditional grantmaking through a single-funder vehicle. But in the areas where Water for Women partners work, there is some potential for DFAT to increase its impact and leverage of external capital sources with the use of blended finance. As it goes about exploring potential opportunities, some general suitability and success considerations include:

- The intervention being funded envisions and helps facilitate the market’s transition towards a sustainable steady-state
- Users of the financing demonstrate sufficient absorptive capacity
- It is feasible for stakeholders (such as funders, implementers, local government) to see the blended finance initiative through
- The blended finance structure makes use of the comparative advantages of each funder’s different risk-return-liquidity-impact appetites
- The blended finance structure aligns incentives appropriately
- The provision of blended finance is supported by complementary interventions to address market bottlenecks other than lack of financing, such as lack of demand, lack of capacity, lack of appropriate policies/regulations, etc.

In the current Water for Women portfolio, 12 opportunities have been identified that present near-term or future potential for DFAT to engage in blended finance for inclusive WASH. These opportunities span a diverse spectrum in terms of both 1) the type of WASH intervention (WASH infrastructure, microfinance, SME finance, results-based financing), as well as 2) value-adding role for DFAT in the blended finance approach. Overall, DFAT has the potential to play several types of value-adding roles for inclusive WASH blended finance, including taking innovation risk, ensuring inclusion, funding WASH ‘software’ of capacity building and institutions building, encouraging CSOs along the blended finance journey, holding them accountable for their performance, while also supporting their capacity building to do more blended finance, and funding targeted research.

A key theme echoed by many interviewees is that blended finance is a tool that must be tailored to the specific intervention and market context to ensure its suitability and success. The key question now is not whether blended finance works or not, but when does it work for whom, and what tools/approaches are needed to make that assessment. To that end, although there is always a need for more research and better evidence, blended finance actors are also urged to boldly engage and experiment in order to generate more robust evidence and support iterative learnings and case studies.
Blended Finance for the Inclusive Wash Sector

Blended finance is one tool in the WASH financing toolkit. There is general consensus that traditional foreign aid and public sector resources will not be sufficient to meet the investment gap required to achieve Sustainable Development Goal (SDG) 6: “ensure availability and sustainable management of water and sanitation for all”. The OECD estimates that annual investment needs to meet water, sanitation and hygiene needs by 2030 to be USD 114 billion.¹ Private capital will be essential to meet this need, yet there are a host of complex reasons and market failures as to why these private capital flows are not flowing more quickly on their own.

In response, the development finance industry has embraced a host of ‘blended’ or ‘innovative’ financing approaches premised on the idea that public sector and donor funds can be used to address some of the market failures and bottlenecks that can then incent/accelerate the entry of private capital, as well as achieve a variety of other development objectives—if deployed in ways other than traditional grant funding for implementing traditional social projects.

To clarify some of the terminology used in this paper:

The general rationale for blended finance is that different types of capital providers have different levels of cost, time, risk tolerance, and financial return requirements—which gives some a comparative advantage over others at different stages of a market’s development lifecycle:

- Private commercial actors have high cost and sometimes high risk tolerance, but require high returns within a short period
- LMIC governments are more patient but have less capacity and risk tolerance
- Impact investors step in to provide more patient funding than commercial actors, but is more limited in quantum
- Donors have the highest risk and time tolerance, but limited, taxpayer-funded resources call for careful stewardship (i.e. low reputational risk tolerance) and targeting to the specific gaps that will facilitate the most efficient transition to the market steady state. Donors also have the highest impact return expectations in terms of their funding contributing to equitable development outcomes.

² Definition of blended finance is drawn from Convergence; other definitions are from Volta Capital.
Blended finance is also thought of by development finance practitioners not as a goal in and of itself, but as a **means to an end**—a tool to transition a given market toward its **sustainable steady-state**. And the sustainable steady-state of a market may be one in which **either** the private sector or the public sector is the owner/provider or funder of the goods/services—or some intersection of the two (e.g. R&D Product Development Partnerships, PPPs, government mandates, etc). As such, the pursuit of blended finance does **not** mean that:

- the end goal must result in an exclusively private sector, profit-maximizing solution that releases the public sector from its obligations to support public goods;
- nor that the blended finance structure itself is the permanent way that a program/intervention should be funded going forward – indeed, blended finance is often most useful to transition the market from a current funding structure that is less sustainable to one that is more sustainable in the long-run.

This raises the question of what is meant by current v. future funding structures, less sustainable v. more sustainable, and pathways from one to the other. Funders provide funding to programs that they believe will facilitate this market transition to its ultimate steady-state, spanning a diverse range from R&D to infrastructure to human capacity-building to behaviour change, and more. And those programs or solutions can follow a variety of different scaling pathways over its lifecycle as it transitions from piloting to scaling to maturity. Some interventions will only ever be appropriate for donor funding, but within a finite period. Others may involve some combination of donor, local government, and/or private funding over time. These funding structures, their pathways towards sustainability over time, and the applicability of blended finance to facilitate each type of pathway, is illustrated below.

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3 Volta analysis.
### Figure 3: Funding Pathways of Development Interventions and Applications of Blended Finance

<table>
<thead>
<tr>
<th>DONOR ONLY</th>
<th>DONOR ➔ GOVT.</th>
<th>GOVT. ONLY</th>
<th>DONOR/GOVT. ➔ PRIVATE</th>
<th>PRIVATE ONLY</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Solution is initiated and led by a donor</td>
<td>• Solution may be donor initiated, but in partnership with government</td>
<td>• Solution is a public sector initiative and primarily funded through public financing</td>
<td>• Solution has commercial market viability but requires donor/govt catalyst/subsidy</td>
<td>• Solution is a market-based initiative led and funded by private market actors</td>
</tr>
<tr>
<td>• Primary financing objective is to crowd in other donors</td>
<td>• Primary financing objective is to transition solution to public sector ownership and funding</td>
<td>• Private actors may co-finance downstream delivery</td>
<td>• Core financing objective is to crowd in private funders and delivery partners</td>
<td>• Donor/govt support may include enablers like infrastructure investment, consumer education, favorable policies, etc.</td>
</tr>
<tr>
<td>• At maturity, solution may be multi-donor initiative or phased out after market failure is addressed and intervention is no longer needed</td>
<td>• Technical assistance funds can be applied to build govt. capacity to take over from donor</td>
<td>• Donor support may include enablers like institutional and systems strengthening, policy advocacy, etc.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Application of blended finance**

<table>
<thead>
<tr>
<th>DONOR ONLY</th>
<th>DONOR ➔ GOVT.</th>
<th>GOVT. ONLY</th>
<th>DONOR/GOVT. ➔ PRIVATE</th>
<th>PRIVATE ONLY</th>
</tr>
</thead>
<tbody>
<tr>
<td>• BF is less applicable, unless referring to “blending” different types of donors, e.g. public donors crowding in private philanthropy / CSR donors</td>
<td>• Use of donor funds to incentivize and capacitate government investment, e.g. debt buydowns, impact bonds, PPPs etc.</td>
<td>• Public financing structures may involve blending, e.g. sovereign/muni debt de-risked by concessional funders, PPPs, etc.</td>
<td>• Donor/government funds used to crowd in private investment for market-based solutions</td>
<td>• BF is less applicable if private sector can provide full solution</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Donor/government support may be used to enhance the ability of private investment to achieve specific impact objectives</td>
</tr>
</tbody>
</table>

Within this framework, blended finance has different levels of applicability for different pathways, without presupposing that the end result must be an exclusively private sector profit-maximizing solution. Fundamentally, this means that blended finance must be designed to serve the needs of the specific intervention it is supporting, and appropriate to the market context of that intervention. This principle is universally held (if not always well-executed) among all blended finance interest groups.

## WASH Financing Context

In the WASH context and particularly the areas where Water for Women partners work, blended finance has clear utility in some areas, as well as clear limitations in others, as with any tool. On the one hand, the WASH sector has certain distinctive features that present challenges to either market-based solutions, blended financing approaches, or both. On the other hand, a recent report on blended finance for DFAT summarized the benefits well: “Blended finance could be adopted to address the perceived risks of WASH investments (responding to the above challenges) and help attract parties with different risk appetites and return expectations...Blending aims to make the funding transaction attractive for all parties, thus achieving goals critical to impact and sustainability. These goals include increasing the overall pool of capital, attracting new, nonconventional participants, and building more heterogenous partnerships for strengthened systems resilience and impacts.”

The sector’s implementers, funders, and researchers are still building the evidence base for when blended finance is most suitable, how to design blended finance approaches to best serve collective impact goals, and defining what success looks like.

### Challenges & opportunities in the areas where WfW works

In the WASH context, market-based solutions and blended finance approaches may be less suitable or more difficult to enact when certain challenges are present. In the context of WfW’s focus in

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4 Volta analysis.

particular, these challenges may be frequently present given that Fund partners often work in remote or rural areas, with marginalized communities, with the goal to improve health, gender equality and well-being of Asian and Pacific communities through inclusive, sustainable WASH.

- **Challenges associated with demand:** market-based solutions are premised on matching market supply and demand, so lack of fundamental demand and prioritization for WASH goods/services makes market-based models difficult to enact—which in turn is a fundamental disincentive for capital to flow:
  o Low consumer demand: low-income households that have to prioritize resources carefully may deprioritize WASH as not immediately contributing to household income-generation capacity and/or whose benefits to health/safety are too long-term and diffuse (unlike other goods/services like energy for instance).
  o Low local public sector priority: WASH is also generally thought to have many public goods features and therefore should be a priority for public sector support to ensure a basic foundation of health and safety; yet local governments may choose to prioritize other competing sectors for government funding that are more direct drivers of economic growth.\(^6\)

- **Challenges associated with supply of goods/services and absorptive capacity:** suppliers of WASH goods/services can either be private sector or public sector providers, but the low capacity of either and therefore their ability to absorb funding and make productive use of it (whether grant or investment) can be a major challenge:
  o Low public sector capacity: When the public sector directly provides WASH goods/services or contracts/regulated private sector providers, low government capacity, weak regulatory oversight, vulnerability to political influence, are impediments to productive use of funds and therefore disincentives for capital to flow.
  o Low private sector capacity: Likewise, if a given WASH market is still nascent and/or dominated by donor support, there may be weak private sector activity; this can be the case for either piped infrastructure, where low-capacity utility operators poorly maintain/operate/monetize expensive capital investments, as well as emerging “off-grid” solutions where small local entrepreneurs have low capacity and access to finance.

- **Challenges associated with supply of WASH financing:** characteristics of the development finance market for WASH, as well as the cultivation of WASH blended finance opportunities can slow down or complicate the flow of funding:
  o Traditional aid can crowd out other sources of capital and potential blended finance opportunities, particularly when donor strategies are siloed, coordination between donors is low, and donors “compete” to fund limited supply of better-performing programs in a given market.
  o Limited track record of proven, at-scale blended finance vehicles for successful WASH programs and lack of robust evidence base, particularly isolating the impact of the financing approach rather than the WASH program itself, makes some funders more cautious about undertaking WASH blended finance.
  o Market context can vary widely, making it hard to develop a uniform approach that can replicate/scale easily, particularly in the Asia Pacific region where South Asia, Southeast Asia, and Pacific Islands present such a wide range of WASH market maturity and market dynamics; the still-limited supply of aggregating mechanisms like funds, facilities, holding

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\(^6\) For example, in Vietnam, local governments have in some cases chosen to prioritize public sector support for sectors like ICT that are more immediate economic growth drivers than WASH. Source: Thrive Networks interview, September 2021.
companies, etc. makes it hard for funders who need to deploy larger amounts of capital to find blended finance opportunities of sufficient size and quality.

- The successful identification, structuring, negotiation and management of blended finance initiatives may present novelty and complexity challenges that require a higher level of capacity than current actors have.

Although these challenges are important to acknowledge, WASH sector programs can also present many different opportunities for blended finance. One of the first things that come to mind for most people when speaking of the utility of blended finance is to raise more money for a program. And indeed, as with any development finance tool, blended finance can be used to mobilize more resources as a basic and important goal. However, identifying suitable opportunities for blended finance can also be facilitated by looking for situations when there are other specific development finance goals to be targeted. These include catalyzing private sector entry, incentivizing public sector investment, improving value-for-money, sharing risks, incentivizing innovation, incentivizing better service delivery, and increasing access/affordability.

**FIGURE 4: MULTIPLE DEVELOPMENT FINANCE GOALS SERVED BY BLENDED FINANCE APPROACHES**

For the WASH sector, besides the need for more funding across the board, many WASH initiatives, including many within Water for Women’s portfolio focus, can also benefit from these other specific goals. And opportunities for blended finance often arise when programs are targeting these other goals.

**Suitability and success considerations**

Given the various challenges as well as opportunities around blended finance for the areas in which WfW works, a key question is then how to identify those areas that are more versus less suitable for blended finance. Some general suitability and success considerations are suggested below, along with the risks associated when such conditions are not in place. The suitability considerations speak more to the identification of potential opportunities, whereas success considerations speak more to how the blended finance opportunity is structured. The scope of this paper is limited to these
generalized considerations, although one should apply more detailed assessment criteria and structuring best practices when pursuing a specific opportunity. As this paper outlines some current blended finance opportunities in the WfW portfolio, these general suitability and success considerations will be discussed for each identified opportunity.

**FIGURE 5: GENERAL SUITABILITY AND SUCCESS CONSIDERATIONS**

<table>
<thead>
<tr>
<th>Key suitability considerations</th>
<th>Description</th>
<th>Potential risks otherwise</th>
</tr>
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<tbody>
<tr>
<td>1) The intervention being funded envisions and helps facilitate the market’s transition towards a sustainable steady-state</td>
<td>The underlying intervention design is sound and based on a clear vision for the market development objective, e.g. establishing viable private markets, capacitating public sector service delivery, etc.</td>
<td>Financial engineering cannot solve for interventions that are fundamentally unsustainable and the blended finance approach may only be a temporary fix</td>
</tr>
<tr>
<td>2) Users of the financing demonstrate sufficient absorptive capacity</td>
<td>Neither donors nor investors should fund actors that lack sufficient capacity to make productive use of their funds</td>
<td>Access to finance and financial engineering cannot solve for lack of capacity, and funding such actors may lead to underutilization of reserved capital, overindebtedness, etc.</td>
</tr>
<tr>
<td>3) It is feasible for stakeholders (e.g. funders, implementers, local government) to see the blended finance initiative through</td>
<td>The providers and users of the capital should have sufficient organizational buy-in and capacity to engage with novel financial concepts, legal/regulatory requirements, stakeholder negotiations, monitoring &amp; evaluation requirements of a given blended finance initiative</td>
<td>Insufficient capacity by any one party may lead to asymmetrical cost/benefit-sharing being negotiated and/or lack of feasibility of the initiative over time</td>
</tr>
</tbody>
</table>

**Key success factors**

| 4) The blended finance structure makes use of the comparative advantages of each funder’s different risk-return-liquidity-impact appetites | The key rationale for blended finance v. conventional finance approaches is the ability to pool resources from different funder profiles, making it important that the structuring intentionally takes advantage of their comparative strengths | Blended finance is not needed, and a conventional financing approach involving less multi-stakeholder coordination, would have been an easier, less costly, quicker at achieving the same results |
| 5) The blended finance structure aligns incentives appropriately | The financial structure results in sufficiently attractive cost/benefit for each party within the structure, while at the same time ensures equitable sharing of costs/benefits across all parties | If one party bears disproportionate risk/burden or nets disproportionate gain, the full benefits of a blended structure may not be realized, or intractable conflict between parties is more likely if there is underperformance |
| 6) The provision of blended finance is supported by complementary interventions to address market bottlenecks other than lack of financing, such as lack of demand, lack of capacity, lack of appropriate policies/regulations, etc. | Provision of finance, blended or otherwise, is most effective when lack of finance is the key bottleneck | Underlying market failures remain unaddressed, and provision of financing is a superficial stopgap and/or further distorts the market |
Current models in use in the broader WASH sector

Based on the desk research and interviews on existing WASH blended finance initiatives, the four most prevalent categories of blended finance application in WASH are identified as:

1. WASH infrastructure finance
2. Microfinance for WASH
3. WASH SME finance
4. Results-based finance

Examples in each category can be found in Annex.

WASH infrastructure: WASH infrastructure investments to install or refurbish reservoirs, treatment facilities, pipe networks, etc. present generally more prevalent funding opportunities in WASH, as well as more prevalent blended finance opportunities. Projects are typically financed through project finance vehicles, which facilitate the pooling of different funding sources with different risk/return/impact preferences. Typically, more junior/subordinated classes of investors and guarantors in such a project finance structure can absorb first losses for more senior investors. In a commercial transaction, subordinated investors would receive a higher return to compensate for their higher risk-taking, but more concessional funders may play a catalytic role to reduce risk/enhance returns for commercial investors who otherwise would not enter. Donors who provide grant capital also have a useful role to play in such a blended finance arrangement by funding for example technical assistance to ensure operator capacity-building for sustainable service delivery, institutional capacity-building to ensure sound infrastructure stewardship, and community-level interventions to build demand for WASH. Donors can also provide subsidies to bridge a finite period when revenues are not yet sufficient to cover costs.

Microfinance for WASH: A recurring theme of universal WASH is to facilitate both household ability to pay for WASH assets or service, as well as microenterprise delivery of such products/services. Microfinance is a well-established business model and industry to provide this, capable of reaching vulnerable populations not served by commercial lenders. Microfinance institutions (MFIs) can be supported by blended finance in which more concessional investors/guarantors blend their capital with more commercial investors to offer wholesale credit to MFIs specifically for on-lending to WASH microentrepreneurs and households. Grant funding can be blended in to provide a variety of technical assistance support to the MFIs and their clients. Many of these MFI partnerships often have a gender component by targeting women-led household purchases or women-owned microenterprises.

WASH SME finance: WASH products/services, particularly ‘off-grid’ solutions, can often be provided by local WASH SMEs such as product suppliers and distributors, masons, desludging operators, etc. These enterprises can face significant challenges in accessing finance, which presents opportunities for blended finance. A common approach is blending of either financing provided either directly to SMEs or indirectly via an intermediary SME fund or credit facility. Again, more concessionary funders can help absorb risk and/or enhance returns for more commercial funders, and donors can also offer technical assistance funding to support SME growth.

WASH results-based financing: Results-based finance refers to any financing approach which provides financial payments based on the achievement of agreed-upon results. Results-based finance does not have to involve blended finance if it refers to grant or payment contracts that disburse based upon achievement and verification of pre-agreed metrics. In the sanitation sector for instance,

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7 Note: These categories are not necessarily mutually exclusive nor collectively exhaustive but are intended to provide a qualitative indication of some of the more prominent types of blended finance application seen in the WASH sector globally.
performance-linked annuity mechanisms for scheduled desludging presents one such example where an annuity funded by a sanitation tax disburses regular payments based on performance of desludging services.\(^8\) Blended finance can come into play in the case of impact bonds for instance, in which a third-party investor provides bridge funding for the intervention’s costs until a donor/government pays for successful outcomes. A key rationale for results-based funding is to enable donors/governments to share risk of ineffective interventions with service providers (or investors). This also provides the ability to develop more precise evidence for what interventions are effective, at what cost, and should therefore be scaled up by other capital providers in future.\(^9\)

**WfW Blended Finance Opportunities**

**Role of CSOs in blended finance**

CSO partners in the WfW expressed many perspectives in interviews regarding the roles CSOs themselves can play in a blended finance ecosystem, as well as needs to enable better preparedness for blended finance. The most commonly cited roles for CSOs to play, by the CSOs themselves are:

- Identifying blended finance opportunities
- Designing and developing blended finance opportunities (including overseeing technical expert service providers)
- Fundraising or brokering/intermediating parties in a blended finance transaction
- Recipient/implementer of programs funded by blended finance

CSOs often cited capacity-building needs in order to better fulfill these functions (which will be explored further in the section “Preparedness for Increased Blended Finance Adoption”). Elsewhere, among CSOs engaging with blended finance or innovative finance globally (WASH and non-WASH), some are starting to pursue other roles, which often require a higher level of organizational capacity such as:

- Researchers and thought leaders
- Advocates
- Owners or managers of (social) enterprises supported by blended finance
- Blended finance capacity-builder for their peers or other market actors
- Fund managers or financial intermediaries of blended finance vehicles
- Investors or guarantors alongside other capital providers in a blended finance structure

In addition to varying levels of blended finance organizational capacity, WfW CSOs have varying organizational structures. The CSOs with organizational structures that have restrictions on receiving different sources of capital, limitations on potential revenue generating activities, or desires to avoid influencing the market towards one private sector actor over another face additional blended finance suitability considerations which may restrict or limit their involvement in blended finance activities.

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Volta Capital conducted interviews with the WfW CSO and research partners to discuss their perspectives on blended finance, as well as identify blended finance opportunities that could be explored further. Interview information-gathering was supplemented by publicly available information about the CSOs and potential opportunities. Seven opportunities were identified that present more immediate potential for DFAT to engage. These opportunities are not all necessarily prototypical blended finance structures that would involve DFAT simultaneously co-financing into a structured facility alongside private investors, but may involve approaches that more broadly link public and private capital sources with a purpose of sharing risk at different stages. These opportunities for blended finance within WfW’s current CSO partners’ programming are either in design phase, fundraising phase, or implementation and scaling phase, and span a diverse spectrum in terms of both 1) the type of WASH intervention (WASH infrastructure, microfinance, SME finance, results-based financing), as well as 2) value-adding role for DFAT in the blended finance approach (design/TA grants, risk absorption, scale-up funding). Five more programs were identified as potentially applicable for blended finance in the future, but whose blended finance component is still in conceptual or pre-design phases. It is important to note that all these opportunities are presented for ideation and discussion purposes only. Detailed due diligence would need to be conducted on each potential opportunity to develop more specific funding recommendations, which is outside the scope of this research.

To protect the confidential nature of these blended finance opportunities, only a high level overview of the opportunity and the proposed CSO role within the opportunity are included below.

1) RTI: Sewage Treatment and Water Supply for Industrial Applications

- **Intervention**: Construction and operation of PPP sewage treatment plants that treat wastewater and provide clean water supply directly to local private industrial users.
- **CSO role**: RTI is supporting project development, providing TA to the private operators, and linking privately owned/operated sewage treatment plants to local industrial offtakers.

2) RTI: SATO Mason Mart Program

- **Intervention**: SATO is a WASH-focused social enterprise that specializes in developing toilet and sanitation products for vulnerable populations. The SATO Mason Mart program helps masons who live in vulnerable communities establish and grow small enterprises by selling

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10 Convergence official definition of blended finance would encompass a variety of such structures: “Blended finance is the use of catalytic capital from public or philanthropic sources to increase private sector investment in sustainable development.”
toilet and plumbing products/services. SATO covers the cost of identifying, sourcing, and training the entrepreneurs, but entrepreneurs often need access to start-up and working capital. A blended finance facility can offer this as part of the whole package to entrepreneurs.

- **CSO role:** RTI has conceptualized, designed, and is fundraising for the blended finance vehicle. RTI is also providing TA to the program participants.

### 3) RTI: Eram Micro-enterprises for Sanitation

- **Intervention:** Eram Scientific Solutions is a social enterprise focused on WASH product R&D. They formed a consortium with other enterprises (Vitor Health Sciences, and Apollo) to operate a program supporting women-led “self-help groups” (community / cooperative groups) to own, operate, and maintain a WASH micro-enterprise which is half multi-utility kiosk (selling WASH products, FMCGs, nutritional products and health services) and half pay-per-use public toilet.

- **CSO role:** RTI has conceptualized, designed, and is fundraising for the blended finance vehicle. RTI is also providing TA to the program participants.

### 4) SNV: ‘Project Wave’ Private Water Operators in Rural Cambodia

- **Intervention:** Project Wave supports a Cambodian water utility holding company. The holding company has 5 private water stations serving households/businesses in rural and semi-rural communities. It is seeking investment to expand to 9 stations. Private commercial investment is viable but is de-risked and enhanced when combined with grant funding to support TA for building the technical, operational, and financial expertise of private water operators to run their businesses effectively.

- **CSO role:** SNV partnered with the holding company on a previous safe drinking water project is now supporting technical assistance and scale up of Project Wave.

### 5) CFAR: SME Desludging in Urban India

- **Intervention:** CFAR operates a faecal sludge management program which addresses the sanitation needs of the urban poor living in informal settlements by linking them to affordable, responsible and safe desludging provided by local SMEs. CFAR’s activities to date include building awareness / demand, SME trainings, creating efficient route maps, and creating single platform to house all the different municipal wards. It is now looking to scale by helping entrepreneurs buy necessary desludging equipment and machinery.

- **CSO role:** CFAR currently manages the grant-funded program to support the targeted SMEs and has identified the application of a blended finance approach for SME finance.

### 6) iDE: ODF Cambodia DIB 2.0

- **Intervention:** The open defecation free (ODF) Cambodia Development Impact Bond (DIB) is focused on increasing toilet coverage, namely the total number of toilets supplied to households across Cambodia. iDE has already successfully launched the first DIB worth US$10 million to cover 6 provinces in Cambodia. iDE is now looking to scale coverage by issuing a follow-on ODF DIB.

- **CSO role:** iDE has been the driving organization for this DIB, partnering with technical financial experts and the outcome funders/investors to design, fundraise, and implement the DIB. iDE is continuing in this role for the DIB 2.0.

### 7) iDE: Multiple-use Water Systems RBF Nepal
• **Intervention:** iDE designs and constructs MUS infrastructure which taps, stores and distributes water to rural communities to meet both household and agricultural needs. To date, iDE has utilized traditional donor grant funding to provide capacity-building support to build, maintain, and govern the MUS systems. As iDE seeks to scale and sustain the MUS initiative, they are considering results-based financing to drive better performance.

• **CSO role:** iDE implements the MUS program and driving the design and development of the proposed RBF approach.

Besides the developed blended finance opportunities highlight above, there are number of programs are worth noting that may become candidates for blended finance if they can continue to progress in the blended finance development:

• **Thrive / East Meets West** - The CSO has identified an opportunity to support rural Cambodian SMEs who provide sustainable WASH products and services but are still in the process of conducting research on their financial profile and suitability for blended finance.

• **WaterAid** – There is a potential opportunity in their Papua New Guinea program to provide piped water to informal settlements who are currently paying inflated prices for bottled water, thereby providing safe access at lower costs, which may have potential for blended finance applications in future.

• **Plan International Australia** – In the Solomon Islands, Plan is supporting MJ Enterprises, an SME producing reusable sanitary products and other health products and services. Specifically, those grant-funded activities include linking the SME to more sustainable supply chains, capacity-building, and various behaviour change programs. The enterprise has been able to tap various sources of finance to date, but continued growth financing needs may provide a blended finance opportunity for DFAT.

• **Plan International Australia** – Plan supports community-level institutions, like hospitals and schools, some of whom are private institutions, to get involved in WASH product/service delivery. Part of Plan’s support includes helping these organizations source funding, which may open up avenues for blended finance in future.

• **World Vision** – In Bangladesh, World Vision has identified opportunities for local female entrepreneurs to construct community and/or household latrine pits while also selling sanitary products to the women in the surrounding local community. Currently, World Vision provides small ventures grants for these entrepreneurs to use as start-up capital. In the future, this could evolve towards a community co-op revolving fund structure, blending different sources of capital.

**Opportunities and Recommendations for DFAT**

This report has outlined some specific WfW portfolio programs that represent blended finance opportunities and a role for DFAT’s funding in such blended structures. Based on the general landscape for WASH blended finance, as well as WfW partners’ specific feedback, the following have been identified as ways in which DFAT can be particularly value-adding in blended finance structures, as well as broader WASH blended finance market-building:

- Providing **early-stage** grant/investment funding to test/pilot innovative approaches for inclusive WASH → Attracts other funders by taking early-stage risk and generates evidence base/track record for effective innovations that merit scaling; particularly important for DFAT to take a rigorous M&E approach to assessing what populations are truly being reached and which markets are truly being accelerated.

- Providing funding that ensures **inclusivity** → CSOs note that a key value of WfW has been its emphasis on socially excluded groups, which has in turn helped set the global WASH financing agenda and built the evidence base; in a blended finance structure that may support
programming benefiting a diverse array of social groups, DFAT’s targeted support to socially excluded beneficiaries within those groups can ensure DFAT additionality.

- Funding the **public goods component** of an intervention that involves elements of private and public goods; for example, funding behaviour change component of a WASH service delivery program to build public health awareness (and demand for a WASH service) → Attracts private sector providers and funders by supporting a component that is important to long-term success of an integrated initiative, but for which private sector actors may not deem a part of their business model to provide.

- Funding ‘software’ of service provider capacity-building and institutions strengthening to ensure sustainable service delivery, which is generally a far more pressing need, than investments in more ‘hardware’ of WASH infrastructure or products → Attracts other funders by increasing absorptive capacity for WASH investments as well as overall systems sustainability.

- Providing transaction design/development funding, either as a grant, or as bridge loan repayable upon project financial close and implementation → Brings blended finance transactions to market that otherwise may languish as mere ideas.

- Encouraging CSO leadership to explore blended finance more actively, holding them accountable for their performance, while also supporting their capacity building to do more blended finance → Encouraging **CSO leadership buy-in** enables on-the-ground program teams to unlock more opportunities; **CSO capacity strengthening** will be important as they can be key agents in cultivating and implementing blended finance opportunities.

- Continuing to fund **WASH blended finance research**, particularly that which can isolate the financing component from intervention itself → Better understanding is needed for the differential impact of various financing approaches compared to the impact of the interventions themselves

These roles can apply for attracting not just more private commercial capital, but other funding sources, including governments, donors, and household investments. For example, setting the stand for social inclusion can set an agenda and benchmark for other donors to focus on this more. Financing instruments like debt buy-downs, results-based financing, or institutional capacity building can incentivize as well as capacitate more public sector investment in WASH.

Importantly, DFAT’s own provision of capital in any blended finance structure can either be in the form of non return-seeking or return seeking capital. Where DFAT’s current WfW funding has been entirely non return-seeking, future DFAT participation in WASH blended finance can maintain this approach, deploy new forms of return-seeking capital through the WfW channel, or be channelled through other DFAT blended finance vehicles such as the Emerging Impact Investment Fund (EMIIF) which deploys return-seeking capital. Indeed, EMIIF’s mandate now includes a new climate finance window to provide investment and technical assistance to climate finance intermediaries such as fund managers and project developers who support climate mitigation, adaptation, and resilience companies/projects.12 This may include WASH sector intermediaries and their underlying investees.

A key theme echoed by many interviewees is that blended finance is a tool that must be tailored to the specific intervention and market context to ensure its suitability and success. The key question now is not whether blended finance works or not, but when does it work for whom, and what tools/approaches are needed to make that assessment. To that end, although there is always a need for more research and better evidence, blended finance actors are also urged to boldly engage and experiment with blended and innovative finance opportunities. To that end, CSO partners see value

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in testing blended financing approaches within the WfW portfolio through open and competitive tender processes so that the best projects are selected based on transparent criteria.

**Preparedness for Increased Blended Finance Adoption**

Clearly CSOs can play a variety of critical roles in a blended finance ecosystem. The actual pace and effectiveness of their adoption can be supported through a variety of preparedness measures by CSOs and/or their funders:

- **Increased human resources and expertise/capacity** on private sector engagement and financing topics
- **Increased flexibility of donor capital** because when donor funding windows are very narrowly earmarked, requiring specific geographies, timings, target populations, it can constrain CSOs flexibility/creativity in identifying and developing blended finance approaches
- **Increased cross learning opportunities between CSOs** given that some CSOs operate in market contexts that are more amenable to blended finance and therefore have more experience or opportunity for experimentation, with the potential to translate those learnings to other contexts: even within the WfW portfolio blended finance opportunities, this can be seen for example in the microfinance/SME finance opportunities cited earlier in markets like India, that may provide useful learnings for similar approaches cited in less mature WASH markets like rural Cambodia.
- **Increased partnerships with technical financial experts and intermediaries** to support blended finance design, access new funder networks.
- **Adapted operational systems/processes** that are more aligned to tracking how activity and costs directly drive headline impact performance and financial bottom-line performance, rather than how activity and costs comply with traditional grant contracting requirements.

**Conclusion**

Traditional grants and donor/government funding will always have a key role and responsibility in the WASH funding ecosystem. There are many important development objectives that private capital cannot be relied on to serve. These include reaching the most vulnerable and marginalized, safeguarding consumer interests and market regulation, providing public goods whose benefits are long-term and diffuse, and institutional strengthening/capacity-building to transition WASH markets to greater self-sufficiency. At the same time, blended finance can be a useful tool under the right conditions to crowd in additional financing from new sources and help transition a given WASH context/market to a steady state where either the public sector, the private sector, or some combination of the two can sustainably deliver inclusive WASH goods and services.

DFAT has been a leading catalytic WASH funder for the Asia Pacific region through the Water for Women Fund. The current portfolio of partners and their programs already presents some interesting near-term and future opportunities for DFAT to participate in blended finance approaches. The key question now is not whether blended finance works or not, but when does it work for whom, and what tools/approaches are needed to make that assessment. To that end, although there is always a need for more research and better evidence, blended finance actors are also urged to boldly engage and experiment in order to generate that evidence base and produce iterative learnings.
Annexes

Annex A: Blended Finance by Sectors

As far as the use of blended finance, the WASH sector lags behind other sectors. As estimated by Convergence, only 8% of blended finance transactions launched between 2014 and 2019 addressed SDG Goal 6 – Clean Water and Sanitation.\(^\text{13}\)


**Figure 7: Blended Finance Alignment with SDG Metrics**

| SDG 17 - Partnership for the Goals | 100% |
| SDG 8 - Decent Work & Economic Growth | 74% |
| SDG 9 - Industry, Innovation & Infrastructure | 72% |
| SDG 1 - No Poverty | 50% |
| SDG 10 - Reduce Inequalities | 46% |
| SDG 7 - Affordable & Clean Energy | 37% |
| SDG 13 - Climate Action | 35% |
| SDG 11 - Sustainable Cities | 33% |
| SDG 5 - Gender Equality | 23% |
| SDG 2 - Zero Hunger | 19% |
| SDG 3 - Good Health & Well-Being | 14% |
| **SDG 6 - Clean Water & Sanitation** | **8%** |
| SDG 15 - Life on Land | 7% |
| SDG 4 - Quality Education | 6% |
| SDG 12 - Responsible Consumption | 4% |
| SDG 14 - Life Below Water | 3% |
| SDG 16 - Peace, Justice & Strong Institutions | 1% |
Annex B. Non-WfW WASH Blended Finance Examples

WASH Infrastructure – Oxfam Septage Management Revolving Fund

Oxfam together with local governments in Philippines initiated the creation of a septage revolving fund aimed at improving sanitation systems in the country. The program is designed to not only to provide finance to local governments for sanitation infrastructure improvement but to also to engage the community to increase demand for sanitation services and to increase capacity and technical assistance to local government on proper waste disposal. Local government can use the funds ($500,000 revolving fund) to buy infrastructure equipment (collection and transportation equipment) or build sanitation treatment plants. However local government can only access the capital upon meeting minimum conditions such as having tariff structures and tariff regulations in place or having required provision for the treatment facility land.14

WASH Infrastructure - Kigali Bulk Water Supply Project

This large-scale water treatment facility (~US$ 61 million) development project was financed via a public-private partnership that leveraged 80% development finance (provided as debt and technical assistance) and 20% equity from a private water treatment developer who in charge of building, operating, and maintaining the plant which at the end of the contract period will be transferred to the Rwandan Water and Sanitation Corporation.15

WASH Microfinance – WaterEquity Global Access Fund

WaterEquity launched a $150 million Global Access Fund in November 2019 based off the success of their previous 2 WASH MFI funds. The Global Access Fund will provide debt capital to financial institutions in emerging markets across the globe (including in South Asia, and East Asia and the Pacific) to enable them to scale their water and sanitation MFI portfolios which will provide low-income families with access to finance to purchase WASH products and services. The Global Access Fund raised capital by pooling and blended capital from different investors including development finance corporation (US DFC), institutional investors (Bank of America), impact investors (Ceniarth) and various foundations (Skoll, Osprey Foundation).16

WASH SME finance – Sanivation

Sanivation is as a social enterprise focused on-site sanitation through 1) distribution of container-based toilets for free with a monthly charge on collection and transportation, 2) construction of treatment plants to treat waste once collected, and 3) production and sale of by-products i.e. briquettes for cooking. With original equity investments by the founder, Sanivation has utilized grants from USAID and CDC (subsector of USA government) to keep growing and expanding operations. They have received additional equity investments from FINCA ventures and have a plan for financial sustainability through revenue generation from collection and transportation of waste to treatment plants at an affordable rate to households, sale of charcoal briquettes to the local community, and by maintaining and expanding their government contracts.17

WASH SME finance – Water Access Acceleration Fund

14 Oxfam Septage Management Revolving Fund; Volta analysis.
16 “WaterEquity scales up with new global loan platform” Global Water Intelligence, April 2021
The Water Access Acceleration Fund, which was initiated by private sector food conglomerate Danone, and now managed by Incofin will invest in innovative water businesses that provide affordable and safe drinking water to underserved populations. The Fund will pool capital from various investors (impact oriented investors, DFCs, institutional donors) to invest in ‘innovative water businesses that provide affordable and safe drinking water to underserved populations’. The investments of this fund will look to catalyse further growth and additional capital for the water sector. Additionally, the Water Access Acceleration Fund will have an accompanying TA facility which will provide TA services to the Fund's portfolio companies.²⁰

Results-based financing (RBF) – Desludging in India (Wai and Sinnar)

Two cities in India (Wai and Sinnar) developed performance-based contract for scheduled private sector desludging where private service providers make investments in necessary equipment (trucks, pumps, etc.) and they are rewarded with an assured business opportunity and monthly payments based on scheduled desludging. Payments to the services providers were made through a performance-based annuity mechanism where an escrow account vehicle was created between the government (who received funds from a new sanitation tax), the private sector, and a local bank. Additionally, these initiatives were supported by a WASH focused research / advisory organization which received funding from the Bill and Melinda Gates Foundation.¹⁸

Results-based financing (RBF) – MCC Sierra Leone Water and Electricity Capacity Strengthening

The Millennium Challenge Corporation (USA government donor agency) used a US$5 million results-based financing facility to incentivize improved service delivery and regulatory capacity of the water and electricity utilities and their regulatory bodies within Sierra Leone. This RBF facility was part of a larger $44.4m grant to the Government of Sierra Leone for water and electricity TA support. The RBF provides payments to the utilities providers contingent on them meeting the specified negotiated service delivery KPIs and also provides financial incentive to the regulator based on increased performance on monitoring utilities.¹⁹
Annex C: Relevant Funding Actors and Supply in Asia Pacific Region

National/local governments: Governments play a major part in the WASH ecosystem as the often implied “rightful” or “sustainable” provider of basic WASH infrastructure/services. However, levels of WASH prioritization can vary widely, with some governments placing a higher priority and dedicating more public resources for WASH, and other governments de-prioritising WASH because it is not seen as a direct economic driver and benefits often only occur over a long time horizon. Additionally, important variations are seen in terms of policy/regulatory regime, and institutional capacity for public finance and blended finance, which are also important factors for blended finance feasibility.20

Figure 8: Public vs Private WASH Expenditure in Select Countries

Public vs Private Expenditure (as a % of GDP) on Water Supply and Sanitation in Select East Asian, Southeast Asian, and Pacific Countries

Investors: The primary sources of global WASH investment are multilateral development banks, development finance institutions, commercial institutional investors, and impact investors.21 This is also the case for the Asia Pacific region. Multilateral development banks, such as the World Bank and Asian Development Bank provide national/local government financing for WASH projects, typically in large investment sizes focused on infrastructure projects and associated technical assistance. Besides public donor/lenders, private institutional investors can also play in this space. There are some commercial private investors in the WASH sector, but these types of investors are still relatively new to the sector and lack the scale and impact of larger institutional investors such as DFIs, and MDBs. For example, IndusInd Bank is an institutional investor that provides loans to Indian private sector sewage treatment plants (which is in part of largely funded ADB Rajasthan Urban Infrastructure Development Project). Ceniarth invested US$3 million in the WaterEquity Global Access Fund, which includes many applicable South Asia, Southeast Asia and Pacific countries. Acumen has a dedicated WASH sector portfolio with ~US$8.4 million worth of investments mostly in South Asia.

Donors: Despite some common perceptions, ODA for WASH funding globally actually increased 9% between 2015 to 2019\textsuperscript{22}, but is relatively concentrated. The vast majority of increased ODA WASH commitments can be attributed to just six donor agencies: World Bank, France, Germany, Asian Development Bank, EU Institutions, and United Kingdom\textsuperscript{23} and their increased commitments of WASH concessional lending and ODA grants. Bilateral donors consistently provide the most WASH non-domestic grant funding through targeted funding windows which have specific geographic scopes and target populations. The largest bilateral donors to Southeast Asia and the Pacific are highlighted below.\textsuperscript{24}

\textbf{FIGURE 10: LARGEST ODA FUNDERS FOR SOUTHEAST ASIA COUNTRIES}

<table>
<thead>
<tr>
<th>Country</th>
<th>Gross WASH ODA Disbursements to Southeast Asia (USD millions)</th>
<th>All Other ODA (USD millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Korea</td>
<td>$187</td>
<td>$1.284</td>
</tr>
<tr>
<td>Japan</td>
<td>$836</td>
<td>$7.820</td>
</tr>
<tr>
<td>Australia</td>
<td>$96</td>
<td>$1.159</td>
</tr>
<tr>
<td>Germany</td>
<td>$93</td>
<td>$3.283</td>
</tr>
<tr>
<td>USA</td>
<td>$39</td>
<td>$2.771</td>
</tr>
</tbody>
</table>

\textsuperscript{23} “Raising the high-water mark for WASH aid - Assessing the performance and potential of Official Development Assistance in accelerating progress toward the global goals for water, sanitation, and hygiene”, WaterAid, October 2020.
Corporations are also a source of funding for WASH initiatives from their Corporate Social Responsibility funds, particularly corporations in industries with a strategic interest in WASH (construction, industrial manufacturing, food & beverage, etc). CSR is especially prominent in India which has set minimum CSR spending requirements for firms of a certain size (~2% of average yearly net profits). Additionally private philanthropies and foundations such as the Bill and Melinda Gates Foundation, Stone Family Foundation, and JSW Foundation (the social development arm of JSW group – a Mumbai based multinational conglomerate) are also strong advocates and funders for WASH programming, although each has distinct geographic focus within Asia Pacific.

**Market builders:** Diverse actor groups are helping to build the WASH blended finance sector in Asia. These include CSOs previously discussed in detail, technical experts, and researchers. Technical experts contribute in many important ways to WASH blended finance such as designing structures, connecting funders to projects, and managing financing programs. Examples of finance specialists include **Social Finance** which worked with iDE to develop the Cambodia ODF DIB; **Volta Capital** which provides TA to SME fund managers as part of DFAT’s blended finance platform EMIIF; **Samhita-Collective Good Foundation** which provides CSR strategy consulting. Researchers are also contributing to the evidence base. Besides the research organizations already in the WfW portfolio other researchers contributing to the WASH sector include the Stockholm International Water Institute (SIWI), the World Bank which sponsors many research reports through its subsidiaries (ie. The Global Water Security & Sanitation Partnership published “Knowledge Highlights from the Water Global Practice from 2016 - 2020”) and UN Water which publishes the World Water Development Report every year.

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