Version of April 2022

Note requesting authorization from the United Nations Economic and Social Council/General Assembly for UNICEF to utilize financing instruments in support of its operations

Summary

This document presents the business rationale for the Executive Board to consider the use by UNICEF of financing instruments[a], including concessional and flexible loans, for support of UNICEF operations. These instruments will be used in support of UNICEF resource mobilization efforts and the organization's plans to enhance and expand funding from the private sector to achieve the Sustainable Development Goals and related outcomes for children.

[a] Financing instruments include debt instruments, concessional and flexible loans and similar financial structures that require repayment, usually with interest. Debt instruments provide borrowers with upfront funding in exchange for repayment of this funding (the "principal") along with interest, based on predetermined time frames and interest rate terms.

I. Overview

1. The coronavirus disease 2019 (COVID-19) pandemic has created unprecedented challenges and has threatened financing – and achievement – of the Sustainable Development Goals. It has never been more important to protect and enhance existing resources while also finding new sources of financing to safeguard development gains and achieve planned progress towards the Goals.

2. The sources of funding for achievement of the child-related outcomes of the Sustainable Development Goals primarily come from two channels: the public sector and the private sector (private domestic/international capital). With official development assistance likely to remain a challenge due to the impact of COVID-19, the ability to tap into additional sources of finance from the capital markets, which leverage private sector resources, will be essential for the achievement of the Sustainable Development Goals. This requires UNICEF to adopt a business approach to financing that does not generate a liability on its regular ("core") resources and that utilizes an effective risk management and oversight strategy.

3. To broaden financing options linked to the private sector within the parameters of Executive Board oversight, UNICEF plans to utilize financing instruments that will include concessional and flexible loans (see the annex). These financing instruments will be an innovative way of collaborating with the private sector to increase investment in private sector fundraising and other critical operations of UNICEF. Use of such financing instruments will generate significant resources for repayment of principal amounts while making substantial resources available, especially regular resources, to fund UNICEF country programmes.

4. UNICEF requests that the Executive Board consider the business rationale presented in this paper for the use of financing instruments on an ongoing basis, subject to oversight mechanisms, and bring its recommendation in this regard to the Economic and Social Council. This is the first procedural step that UNICEF hopes will ultimately lead the Council to endorsing and forwarding the request to the General Assembly. For UNICEF to avail itself of financing instruments on an ongoing basis, the General Assembly must give authority to the UNICEF Executive Board to oversee the use of such financing instruments by UNICEF, in line with risk management parameters to be established by the Board.

II. Scope and objectives

5. As the Secretary-General of the United Nations stated in October 2020, "The timely achievement of the Sustainable Development Goals is at serious risk. To reverse our course, a fundamental change of financing and investment is needed to place sustainability at the core of the global economic and financial system… Private sector leadership will be more important than ever."[1]

6. Even prior to the COVID-19 pandemic, the financing gap to achieve the Sustainable Development Goals by 2030 was estimated to be $2.5 trillion per year. The health, economic and social consequences of the pandemic are expected to increase this gap: as a result of the pandemic, for example, there is a projected $1.7 trillion shortfall for 2020 that adds to the existing gap of $2.5 trillion in annual financing

[1] "UN Secretary-General and top business leaders agree on steps to scale up investment in sustainable development", 14 October 2020, available at www.un.org/development/desa/en/news/financing/global-investors-for-sustainable-development-alliance.html.

needed to achieve the Goals.[2] Yet new sources of financing are available to close this gap, with global gross domestic product and global gross financial assets estimated, pre-pandemic, at more than $80 trillion[3] and $200 trillion,[4] respectively. The Addis Ababa Action Agenda of the Third International Conference on Financing for Development underscores the role of capital markets, which can be supportive of economic growth and sustainable development. The challenge is that financing via the capital markets is not being channelled towards sustainable development and to those countries most in need, nor is it being tapped to meet the needs of children.

7. Reform of the United Nations development system must be leveraged to increase support to countries on strategic financing for the Sustainable Development Goals. This will include catalysing new sources of finance and encouraging collaboration between public and private actors to unlock all sources of finance and financial innovation.[5]

8. Despite the global economic downturn and the uncertainty created by the COVID-19 pandemic, UNICEF reported an annual income of more than $8 billion in 2021. This is a testament not only to the ability of UNICEF to adapt to an evolving crisis, but also to the strength of public and private sector support for the organization's mandate. That said, growth in recent years has been largely in restricted income. The proportion of unrestricted income (regular resources) to total income decreased from nearly 50 per cent in the early 2000s to 17 per cent in 2021.

9. Of the regular resources received in 2021, public sector income totalled $536 million and private sector income totalled $756 million. Public sector regular resources income has continued to decline as a proportion of total public sector income, despite commitments by Member States in the funding compact to achieving a level of at least 30 per cent of core resources as a share of voluntary funding for development-related activities.

10. Private sector regular resources income, on the other hand, has steadily increased in recent years, in absolute dollars and as a proportion of all private sector income to UNICEF. This is largely as a result of investments made in the fundraising activities of the National Committees for UNICEF and the UNICEF country offices that are engaged in private sector fundraising – activities that were funded through regular resources. These investments have been made possible by budget allotments approved by the Executive Board and financed from UNICEF unrestricted income. Investments in private sector fundraising totalled $390 million during the integrated budget, 2018–2021 period. The private sector fundraising investment strategy targeted and successfully achieved a 3 to 1 rate of return over 36 months.

11. The long-term growth of UNICEF private sector income depends on the level of investments made (i.e., investment funds) to acquire new donors, replace lapsed donors and increase the overall pool of donors generating monthly income. Given the continuing decline in the ratio of regular resources to other resources, the current model of fundraising efforts being exclusively funded from regular resources will constrain the long-term strategy of increasing the overall pool of donors.

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[2] Organisation for Economic Co-operation and Development (OECD), *Global Outlook on Financing for Sustainable Development 2021: A new way to invest for people and planet*, OECD Publishing, Paris, 2020.

[3] World Bank, Databank, 2017, gross domestic product, available at https://databank.worldbank.org/source/ICP–2017, accessed 31 March 2022.

[4] Allianz, Allianz Global Wealth Report, Munich, 2018.

[5] United Nations, *UN Secretary-General's Roadmap for Financing the 2030 Agenda for Sustainable Development: 2019–2021*, New York, 2019.

12. Based on the actual and projected reduction in the proportion of regular resources to total income and the consequent reduction in investment funds available for fundraising, UNICEF has identified the need for alternative sources of funding to support the expansion of private sector fundraising. These alternative sources of funding have great potential to diversify the organization's current sources of investment funds for private sector fundraising. The World Bank instrument is one of these alternative sources and has been approved by the Executive Board only as a pilot project; the financial instrument cannot be used on an ongoing basis unless there is approval by the General Assembly.

13. Given the current gap in funding needed to fully achieve the Sustainable Development Goals and with the current composition of UNICEF funding, UNICEF is proposing to secure alternative sources of financing for its investment in private sector fundraising and pre-financing (e.g., upfront financing for certain interventions) of cost-reimbursable grants. Strategic deployment of these alternative financing sources would tap into new sources of predictable capital and thus leverage additional resources for UNICEF programmes.

14. The new UNICEF Innovative Financing for Children – IF4C Global Vision and Strategy sets out a clear vision and goals, and a plan that identifies more innovative ways to finance and invest using a diverse spectrum of capital, including through the National Committees. The use of financing instruments is an essential part of innovative financing initiatives and the new strategy.

15. During its first regular session of 2021, the UNICEF Executive Board authorized the UNICEF Executive Director, with the advice of the UNICEF Comptroller, to execute a financial instrument in partnership with the World Bank to raise additional financing for investment in private sector fundraising as a pilot project limited to an amount of $50 million. The instrument was executed in March 2021 and leverages the expertise of the World Bank in financial markets. Based on income generated through private sector fundraising in the 18 emerging fundraising markets in 2021, the $50 million target has been already achieved, and has triggered the obligation for UNICEF to repay the borrowed funds in full at the end of the five-year maturity period, thereby eliminating the risk of default. While still preliminary, 2021 results indicate that country offices have already raised well above the $50 million allocated in the first year.

16. The financing instrument was offered to a United Nations organization by the World Bank for the first time, making UNICEF a pacesetter for other United Nations organizations and creating alternative modalities for the United Nations to leverage the capital markets in pursuit of the financing for development agenda.

17. Following the successful execution of the World Bank instrument, several other opportunities have been considered. However, the UNICEF Financial Regulations and Rules do not include any reference to the possible use by UNICEF of financing instruments beyond the exceptions that could be provided in a pilot project.

18. In its approval of the pilot project in 2021, the Executive Board also requested that the United Nations Office of Legal Affairs assess the financial arrangement and determine whether an update of the UNICEF Financial Regulations and Rules would be required to enable future transactions of this type to occur beyond the pilot. The United Nations Office of Legal Affairs opinion acknowledged the approval of the pilot project by the UNICEF Executive Board and advised that, if UNICEF desired to engage in further such transactions on an ongoing basis, the organization would need to seek the approval of the General Assembly.

19. The United Nations Office of Legal Affairs opinion further stated that if the General Assembly were to authorize the Executive Board to grant approval to the

UNICEF Executive Director for such transactions on an ongoing basis, UNICEF would then need to appropriately amend the UNICEF Financial Regulations and Rules to provide for such transactions.

20. The ability to use financing instruments (including concessional and flexible loans) on an ongoing basis, under pre-defined conditions and with the oversight of the UNICEF Executive Board, will provide additional sources of investment for private sector fundraising activities and other critical operations. These additional sources of investment will complement the current investment funds that are available from regular resources to support the growth of unrestricted resources and ensure full funding of country programmes.

21. The financing instruments will also leverage the appetite of investors and high-net-worth individuals for investment in the Sustainable Development Goals.[6] Several high-net-worth individuals have expressed their interest, through the National Committees, to provide resources through financing mechanisms for UNICEF to reach more children, with repayment of the principal amounts and the possibility of zero interest, or at a concessional rate.

22. Concessional loans have more generous terms than market loans. Concessional loans generally include below-market interest rates, grace periods in which the loan recipient is not required to make debt payments for several years, or a combination of low interest rates and grace periods.

23. UNICEF has made significant efforts to map the untapped alternative sources of financing to meet the critical needs of children during this last decade of work towards achievement of the Sustainable Development Goals.

III. Value and impact for UNICEF in using financing instruments

24. The proposed financing instruments aim to finance the growth of private sector fundraising, including in emerging markets, and other critical operations of UNICEF to achieve the child-related Sustainable Development Goals.

25. The ability to utilize new financing instruments for fundraising investments will generate additional resources for UNICEF programmes. Programme-related investments, for example, are a new, but mostly underused, area of philanthropy that offer non-profit organizations resources at low or no interest. This makes programme-related investments a real opportunity for UNICEF to explore as a potential recipient of such investments.

26. Access to no-interest financing will also be attractive and beneficial to UNICEF programme delivery linked to donor grants where resources only become available on a cost-reimbursement basis. No-interest financing will address the need for upfront working capital and mitigate the constraints around upfront funding imposed by using regular resources reserves.

27. The innovative nature of the proposal to utilize financing instruments outlined in the present report will solidify the status of UNICEF as a pacesetter in the use of private sector financing for other United Nations organizations, and further delineate alternative modalities for the United Nations to leverage capital markets. The financing instruments will also provide much-needed flexibility that will allow their proceeds to be used in the emerging markets that deliver the best return on investment.

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[6] United Nations, *United Nations Secretary-General's Roadmap for Financing the 2030 Agenda for Sustainable Development: 2019–2021*, New York, 2019.

IV. Risks and proposed risk management

28. The first risk is the risk of default related to the potential lack of return on investment, with investments not generating enough resources to repay principal amounts and interest due, with UNICEF ultimately having to utilize the regular resources reserves. This risk will be managed through a rigorous review of each proposal, sound business planning and cash flow analysis based on historical data and financial analysis. During the Strategic Plan, 2018–2021 period, the private sector fundraising investment strategy targeted and successfully achieved a 3 to 1 rate of return over 36 months, thus making the risk of default highly unlikely.

29. The exposure will be further managed, where possible, by structuring the financing agreement without recourse (i.e., the legal obligation to repay in case of default) similar to the conditions used in financing arrangements with the World Bank bonds issuance, or use guarantees provided by traditional donors (similar to those provided for the Vaccine Independence Initiative) as an extra protection for UNICEF. Furthermore, the UNICEF Executive Director will operate within parameters to be established by the Executive Board, upon advice from the UNICEF Comptroller, to ensure that a proper governance and oversight mechanism is in place.

30. A second risk is potential currency volatility in markets whose cash flows are the source of repayment of these financing instruments. The monetary value of the instruments utilized will be closely monitored to ensure cash flows are more than sufficient to cover currency volatility against the United States dollar. Thus, the overall cash flow in United States dollars derived from use of the instruments will grow from year to year, despite currency fluctuations that may occur in one or more of these markets at any given time. UNCEF has demonstrated the capacity to adequately mitigate foreign exchange impact in past years.

31. A third potential risk is related to the capacity of UNICEF to demonstrate the impact of the private sector fundraising income generated from the proceeds of these financing instruments in a manner that appeals to a new audience. Illustrating the ultimate impact on the lives of children and families is extremely important. Because potential investors will be new or non-traditional donors, UNICEF will adapt existing reports to make them appropriate for and accessible to this new audience.

32. A final area of risk includes the potential exposure of UNICEF to criticism for using donations to repay principal and interest on a financing instrument. The deployment of resources from the financing instruments in private sector fundraising is expected to generate sufficient resources to cover repayment of the principal and related interest, as well as significant resources for UNICEF programmes. Most of the individual donations from private sector fundraising are made towards the overall mandate of UNICEF; they are not earmarked for a specific use, and therefore there are no restrictions as relates to using part of the donations to meet the obligations on the financial instruments. UNICEF plans to convey this to the public transparently and to explain the value and use of these donations.

V. Roles, responsibilities and oversight

33. Once authorization from the General Assembly has been obtained by the Executive Board, the UNICEF Financial Regulations and Rules will be amended to include the authority of the UNICEF Executive Board to oversee the utilization of financing instruments.

34. The Executive Director shall, during the first regular session of each year, submit to the Executive Board for its approval an indicative borrowing programme for that year. The borrowing programme will be drawn up in conformity with the financial and

borrowing policies of UNICEF. All borrowing activities will be carried out consistent with the borrowing programme as approved by the Executive Board.

35. The Executive Director shall, in respect of borrowing transactions completed by UNICEF, submit to the Executive Board a report in such form, frequency and content as the Executive Board may determine.

36. Interest, charges, expenses and amortization payments made in respect of a borrowing transaction shall be borne by the resources generated by the fundraising investments.

VI. Conclusion

37. Past experience and emerging trends have shown the limits of relying solely on voluntary grant funding to implement such an ambitious development effort as the Sustainable Development Goals.

38. The challenging global environment, combined with the increased demand and expectation that UNICEF deliver more in the face of the COVID-19 pandemic, makes it vital to utilize financing instruments to leverage the potential of capital markets to support achievement of the Sustainable Development Goals. The approval of this proposal will diversify the sources of funds needed to grow private sector fundraising income so that UNICEF will not have to rely exclusively on regular resources to fund its private sector fundraising activities. This will ultimately add to and diversify the resources that are available to predictably fund UNICEF country programmes and deliver results for children.

39. UNICEF is therefore seeking endorsement from the Executive Board of the business rationale set forth in the present paper. UNICEF requests that the Board then share this proposal with the Economic and Social Council, which would then seek to bring the matter to the General Assembly. Ultimately, it is desired that the General Assembly grant the Executive Board the authority to oversee the use of such financing instruments by UNICEF on an ongoing basis, within parameters to be established by the Board.

40. Once the General Assembly grants the UNICEF Executive Board the authority to oversee the use of such instruments on an ongoing basis, UNICEF will take steps to amend the UNICEF Financial Regulations and Rules through the appropriate process.

Annex

Financing instruments: costs, risk parameters and partners

Type of financing instrument	*Nature of instrument*	*Cost of capital (per cent)*	*Use of instrument*	*Risks, parameter and safeguards*	*Partners/potential partners*
Bonds – unrated	Debt instrument issued as notes	≤ 2%	For investment in private sector fundraising	Capital at Risk Notes may result in the loss of the entire investment to the lender, with no payment of any type made at maturity by UNICEF.	World Bank Global Debt Issuance Facility (International Bank for Reconstruction and Development Capital at Risk Notes). Implemented a pilot project approved in February 2021 by the UNICEF Executive Board
Pre-financing mechanism	Release of liquidity for programme implementation in advance of receipt of funds from donor partners	0%	For programme grants implemented on a cost-reimbursement basis	There is no risk of default to the lender and by UNICEF. Funding partners always fulfil grant obligations. Only meant for cash flow and working capital solution purposes.	UNICEF National Committee (UNICEF USA Impact Fund for Children)
Concessional loans	Loans that are made with extended terms that are substantially more generous rate than market loans	≤1.5%	For investment in private sector fundraising	Without recourse of repayment, or Backed by default guarantees where guarantor(s) pay(s) debt in the event of default by UNICEF.	Institutional investors/ Governments/ sovereign institutions
No-interest loans	Loans for which only the principal is repayable	0%	For investment in private sector fundraising	Without recourse of repayment, or Backed by default guarantees where guarantor(s) pay(s) debt in the event of default by UNICEF.	High-net-worth UNICEF philanthropic donors UNICEF National Committee (UNICEF USA Impact Fund for Children)