

INNOVATIVE PATHWAYS: LEVERAGING PARTIAL RISK GUARANTEES (PRGS) FOR FINANCING SOCIAL IMPACT PROJECTS

The executive summary is adopted from an extensive report authored by IIT Delhi. Prof. Sanjay Dhir and Prof. Sonali Jain led the team with contributions from Ms. Kamakshi Sharma and Ms. Tusharika Mahna (Research Scholars)

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Innovative Pathways

Leveraging Partial Risk Guarantees (PRGs) for Financing Social Impact Projects

Background

The COVID-19 pandemic has disrupted global economic and societal norms to an unprecedented degree, further increasing pre-existing vulnerabilities and inequalities across the world. Even before the pandemic, progress towards achieving the Sustainable Development Goals (SDGs) was falling behind, and the current challenges have only grown more formidable. Developing countries now face a daunting financing gap estimated at a staggering US\$4.2 trillion annually. Private capital and wealth, often fail to reach the regions and populations that need them most. To successfully realize the “Agenda 2030” and attain the SDGs, a fundamental shift in policy and a significant reorientation of investment strategies by nations, corporations, and individuals are required.

In this context, the 360 ONE Foundation (formerly known as IIFL Wealth Foundation) has taken a proactive step by supporting a study in collaboration with IIT Delhi, exploring the use of Partial Risk Guarantees (PRGs) as a strategic instrument to mobilize private capital—a vital component in bridging the substantial financing gap and making meaningful progress towards these global goals.

In this project, to provide youth employment opportunities and fortify the healthcare workforce in India 360 ONE Foundation committed CSR grants to the SAMRIDH Healthcare Blended Finance Facility, which is supported by the U.S. Agency for International Development (USAID) and implemented by IPE Global. This partnership is unique, as it marks the first time that Indian Corporate Social Responsibility (CSR) funds were used as risk guarantees to increase youth employment in the healthcare sector. The risk guarantee assisted a social enterprise in obtaining a loan grant of INR 4 crore (3X leverage) from a financial institution (National Skill Development Corporation (NSDC)), with IIT Delhi providing coverage of 33.38% of the loan amount in case of default. The risk guarantee also generated significant social impact by facilitating the training of 2,420 beneficiaries in the initial year, compared to the 800 beneficiaries who would have been trained with a conventional grant. If the risk guarantee is not invoked or partially invoked, it will be redeployed to train beneficiaries in the second year. In case the risk guarantee is not invoked or partially revoked after the second cycle, SAMRIDH and 360 ONE Foundation will mutually decide on the utilization of remaining funds to directly subsidize the fees of the beneficiaries enrolled in skilling programs. Given this structure, it is expected that the guarantee will additionally reach to 4,200 beneficiaries by the end of year three. The case study illustrates the role of the Blended Finance ecosystem in financing the SDG deficit by serving the unprivileged sections of society through financial and economic additionality.

Partial Risk Guarantees (PRGs)

High-impact organizations often encounter challenges in securing affordable private capital for expansion. This difficulty arises from their perception as high-risk ventures, dissuading investors. Consequently, accessing funds becomes a hurdle, limiting their ability to scale their initiatives and maximize their impact. To address this issue, innovative financing approaches and improved risk assessment methods are needed to attract private investment and facilitate further positive change.

PRGs work by absorbing a portion of the losses incurred by investors in case borrowers’ default on loans. This risk mitigation mechanism is essential to attract risk-averse private investors who might be hesitant to fund projects with higher social impact but greater financial risk. As per the latest NSDC funding Guidelines¹, the minimum collateral worth 30% of the proposed loan amount is a pre-requisite for any funding proposal. Upon finalization of collateral, borrower's due diligence and assessment of its credit worthiness and proposed project is carried out.

¹ <https://nsdcindia.org/funding>

Accordingly, to comply with the above guidelines, Bank Guarantee for 33% was obtained in case of Skill Tree Consulting Private Limited followed by a third-party due diligence. By leveraging philanthropic funds as risk guarantees, PRGs encourage private investors to participate in these projects, thereby increasing the pool of available capital for social enterprises.

Need for & Advantage of PRGs

- **Promoting Social Development:** Projects with clear social outcomes are more likely to attract public and private entities when the risk is mitigated through PRGs. This fosters social development and societal growth. For example, PRGs can support initiatives in education, healthcare, and poverty alleviation, contributing to improved quality of life and well-being for disadvantaged populations.
- **Fostering Sustainable Borrowing Ecosystems:** PRGs promote the sustainability of borrowing entities by allowing them to build credit history and access working capital. This, in turn, ensures that borrowers can achieve their goals and maintain cash flow, reducing the risk of default. This financial stability contributes to long-term economic growth.
- **Supporting Multi-Sectoral Development and Economic Growth:** PRGs are applicable in sectors where development is a critical goal. They facilitate private sector participation for social returns, thereby reducing the SDG financing deficit and fostering collaboration among public, private, and philanthropic sectors. This collaborative approach contributes to economic development by providing livelihood opportunities and income generation for individuals.

PRGs offer a strategic mechanism to leverage private investment, reduce the cost of capital, and make social impact and developmental projects financially viable. They enable a collaborative, risk-sharing approach that attracts diverse stakeholders, ultimately leading to more significant positive societal and environmental outcomes.

Structure of PRG and Role of Stakeholder

The structure of PRGs involves a coordinated effort among multiple stakeholders, each with specific roles and responsibilities. This collaborative approach aims to de-risk projects, attract investment, and ultimately achieve positive social and environmental outcomes while promoting financial sustainability. The table below outlines the key stakeholders involved in the structure of PRGs and their respective roles and responsibilities in facilitating these guarantees for the social impact initiatives.

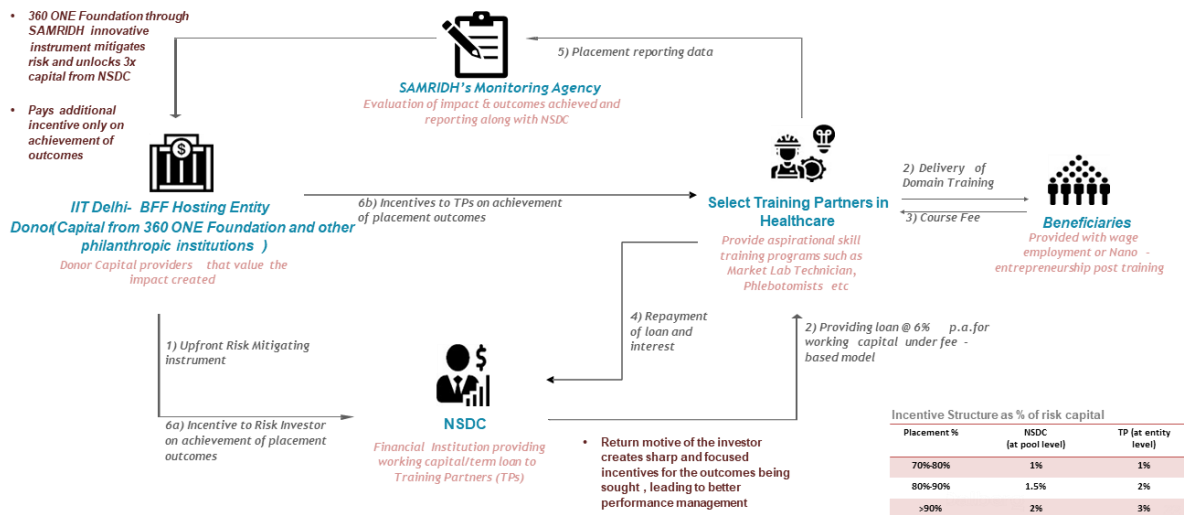
Stakeholders	Roles	Responsibilities
Beneficiary Organization	Borrower	Implement a social impact project that demonstrates how the PRG reduces risks and attracts investment.
Guarantor	Provides the guarantee	Assess project viability and risk levels. Commits to covering specific losses if adverse events occur.
Investors	Provide capital for the project	Assess project attractiveness with PRG risk mitigation benefits in mind and provide the necessary funding,
Regulators and Policymakers	Establish the regulatory framework for PRGs	Ensure PRGs comply with relevant laws and regulations. - Create a conducive environment for PRG implementation
Impact Measurement Organizations	Measure and assess the project's social and environmental impact	Monitor and report on project progress in achieving intended outcomes. - Ensure transparency and accountability.

Case Study

As part of the study, 360 ONE Foundation provided a CSR grant of INR 1.33 crore as PRG facilitated by IIT Delhi. With this guarantee, NSDC disbursed a loan of INR 4 crore to Skill Tree, unlocking additional capital, leading to a leverage of 3x. If the risk guarantee is not invoked or partially invoked, it will be redeployed to train beneficiaries in the second year. In case the risk guarantee is not invoked or partially revoked after the second cycle, SAMRIDH and 360 ONE Foundation will mutually decide on the utilization of remaining funds to directly subsidize the fees of the beneficiaries enrolled in skilling programs. This effectively leads to ~6x financial leverage over the three year period. The structure leads to training of 4,200 young individuals from underprivileged backgrounds in 3 years, a significant increase from the initial count of 800 through traditional grant. IIT Delhi due diligence along with the risk guarantee provided by 360 ONE Foundation supported Skill Tree to reduce its borrowing costs significantly, securing a loan from NSDC at an interest rate of 6% per annum, which is substantially lower than the 10%-18% range offered by conventional financial institutions (Banks and NBFCs). Additionally, it allowed the initial capital of INR 1.335 Crores to remain available to be used in business, which would have otherwise been locked as collateral for obtaining the loan. This project aimed to correct fund distribution, improve economic additionality, and bridge the demand-supply gap for skilled healthcare workers. On achievement of milestones, a component of 360 ONE Foundation's grant will pay additional incentives for overachieving the targeted milestones as per the defined incentive structure.

IPE Global initiated the process to ensure that the transaction is compliant under clause ix(b) of Schedule 7 of the Companies Act.

Livelihood generation via unlocking concessional capital for Skilling



Key Stakeholders

- **Donor:** The 360 ONE Foundation serves as the primary donor for this project. They focus on innovative CSR approaches to improve financial access and inclusion as a lever to improve livelihoods.
- **Risk Investor (NSDC):** NSDC acts as the risk investor, disbursing a subsidized loan of INR 4 crore with a partial risk guarantee, facilitating the training and placement of candidates in the healthcare sector.
- **Implementation Partner (Skill Tree):** Skill Tree, a vocational training partner, trains, and places candidates in the healthcare sector. They have a wide network of training centers and strong

partnerships with healthcare institutions, focusing on creating employment opportunities for underprivileged youth.

- **Partial Risk Guarantor (IIT Delhi):** The Indian Institute of Technology (IIT) Delhi uses a part of the 360 ONE Foundation grant to provide a partial risk guarantee to NSDC, leveraging the loan three times the original CSR grant amount. They cover a portion of the investor's default risk, fostering confidence in the loan arrangement.
- **Technical Partner (IPE Global):** IPE Global played a pivotal role in facilitating the transaction. This involved designing the project's structure, aligning all relevant stakeholders, extending technical assistance to the implementation partner, and ensuring the timely achievement of mutually agreed-upon milestones.

Innovation in the Model

- The innovative use of Corporate Social Responsibility (CSR) capital as a source for Partial Risk Guarantees (PRGs) represents a departure from traditional philanthropic models. By earmarking CSR funds as risk guarantees, the 360 ONE Foundation demonstrated a novel approach to leverage private investment for social impact. This not only transforms CSR from a direct funding mechanism to a risk-mitigating instrument but also ensures that philanthropic capital serves as a catalyst for attracting financial institutions including private and public investment maximizing the impact of social initiatives.
- The innovation in this model lies in the collaborative engagement of diverse stakeholders, each contributing their unique strengths to achieve a common vision. In this case, the 360 ONE Foundation, IIT Delhi, NSDC, Skill Tree, and other partners collaborated to create a blended finance ecosystem. The involvement of multiple stakeholders brings a diversity of expertise, resources, and perspectives, fostering a holistic and sustainable approach to addressing societal challenges.
- The leverage of funds achieved through PRGs in this case study, with a 3x increase over the traditional grant method, is a key innovative aspect. By using a relatively smaller amount of philanthropic capital as a risk guarantee, the project attracted a larger sum from NSDC, significantly amplifying the project's reach and impact.
- Partial Risk Guarantees (PRGs) stand out from conventional guarantees and First loss Default Guarantees (FLDGs) through their selective risk coverage. Unlike conventional guarantees that may cover the entire loan amount, PRGs cover only a portion of the losses incurred by investors in case of default. This strategic risk mitigation encourages risk-averse private investors, in this case NSDC who might otherwise be hesitant to participate in high-impact projects. According to the NSDC funding guidelines, having collateral equivalent to 30% of the proposed loan amount is a prerequisite for any funding proposal. In contrast to FLDGs, which cover all aspects of risk, including market risk, currency risk, and political risk, PRGs are more focused, specifically addressing the risk associated with borrower default. This targeted risk coverage makes PRGs a nuanced and efficient instrument for attracting private investment in socially impactful projects.

Benefits of using Blended Finance Structure (PRG) over Traditional Grant Financing Structure

- **Leveraging Additional Funding & Impact:** Skill Tree's use of PRGs gains NSDC's interest, resulting in a subsidized loan and improved credibility for Skill Tree. This positions Skill Tree to participate in more government schemes with favorable terms, crucial for addressing healthcare workforce needs. While a conventional grant would have been able to support only 800 candidates, this approach has impacted 2420 beneficiaries in first year and aim to impact around 4200 in 3 years, effectively 4X the overall impact.
- **Enhanced Due Diligence:** IIT Delhi's role as a partial risk guarantor in the SAMRIDH project ensures thorough background checks, lowering the risk of default. This benefits Skill Tree by securing loans with no collateral, reducing transaction costs for NSDC, and facilitating access to cheaper debt. This advantage is crucial for smooth project operation and SDG financing.

- **Crowd-in Funding Sources:** 360 ONE Foundation's CSR grant, supported by IIT Delhi's risk guarantee, attracts government support for Skill Tree. This public-private synergy diversifies funding sources, reducing risk for investors, and supporting small businesses.
- **Risk Diversification:** NSDC diversifies risk by involving IIT Delhi as a partial risk guarantor, covering 33.38% of Skill Tree's loan. This lowers the risk premium, benefiting Skill Tree and facilitating significant investments in healthcare.
- **Reduction in Borrowing Costs:** Skill Tree secures a loan from NSDC at a subsidized rate of 6% p.a., significantly lower than market rates. This reduces transaction costs and interest rates, offering Skill Tree access to substantial funds for healthcare development.
- **Cash Flow Improvement:** Skill Tree's working capital loan from NSDC ensures stable liquidity for daily operations and supports productivity and quality in healthcare training.

Way Forward

- Explore the potential to replicate and adapt the model to different sectors and geographies.
- Collaborate with financial institutions and development partners to create a standardized framework for RG instruments that can be easily applied across various projects.
- Develop a technical assistance program that provides capacity-building support to project stakeholders.
- Foster collaboration and partnerships among various stakeholders, including government entities, private sector organizations, and local communities and align the interests of all parties involved in the sustainable intervention.
- Engage in policy advocacy efforts to influence favorable regulations and incentives that promote sustainability.
- Establish a platform for continuous knowledge sharing and learning among stakeholders to enhance collective expertise and innovation.

This executive summary presents the key findings of an extensive IIT Delhi report. The report highlights the importance and benefits of using Partial Risk Guarantees to finance projects with social impact. It examines a specific case of training disadvantaged youth in the healthcare sector and describes the journey from the early stage of using donor funds to draw in additional private and public investment, to the successful enhancement of healthcare problem-solving.

This model is CSR compliant with Clause IX(B) of Schedule 7 of the Companies Act 2013 (Refer Full Report for Details)

Scan the QR code below to access the full report.

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