Case Study

Blended finance: The Regional Education Finance Fund for Africa

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Introduction

Initiated in 2012 by the German Development Bank (KFW), with funding from the German Ministry for Economic Cooperation and Development (BMZ), the Regional Education Finance Fund for Africa (REFFA) is the first fund to exclusively support the education sector in Africa to improve access and quality of education in the region (REFFA, 2020). It does so by providing debt investments and technical assistance to local financial intermediaries (investees) who, in turn, offer loans or education savings products to education providers, students and their families. REFFA is funded through a blended financing mechanism composed of funding from Development Finance Institutions (DFIs) and private investors (REFFA, n.d.-a).

The problem

In African countries, universal access to primary, secondary, and technical vocational education is still a serious challenge to overcome although momentous progress has been witnessed in the last several decades. According to the World Bank, approximately 50 million children remain out of school in Africa and those represent 45% of the globally out-of-school children (Bashir et al., 2018). The increasing demand for decent primary and secondary education puts rising pressure on African countries' public budgets. The public financial difficulties to provide quality education have led to the emergence of a private education sector, which has burdened households in filling the education financing gap (REFFA, n.d.-b).

Regional Education Finance Fund for Africa

Aiming to respond to this problem, in 2012, REFFA was initiated by KFW, with funding from BMZ. The fund aims to improve access and quality of education for low and lower-middle income households across Africa by directing funds through local financial intermediaries (investees) to education providers, students and their families (end clients). (REFFA, n.d.-c; REFFA, 2021).

REFFA offers both debt investments and technical assistance to financial institutions in ODA-eligible African countries. The loans vary between US$ 0.5 million and US$ 5 million (paid in the local currency) with tenors of up to seven years (REFFA, 2020). Generally, loans tend to be long-term: 87% of investments have been lent for over 36 months (REFFA, 2021). REFFA loans are available to any type of financial institution as long as they are professionally managed, show good financial results, and have a strong interest in education (REFFA, n.d.-a; n.d.-c). The participating financial institutions also benefit from tailor-made technical assistance (TA) to enhance their institutional capacity for sustainable education finance lending. Although the TA services will vary, they will typically include: 1) analysis of the education market; 2) support for the design of customised finance products; 3) strengthening internal processes; and 4) training of staff in education finance products (REFFA, n.d.-d).

Financial intermediaries use the REFFA funds and TA to offer education loans and savings to two main client groups: 1) private education providers; and 2) private households that consume education. Private households comprise learners and their families whose income derives either from micro, small and medium enterprises (MSMEs) or from salary income, as well as students who want to finance their own education (REFFA, 2021). For the majority of investees, a significant portion of their portfolio is MSMEs and/or consists of loans to low-income individuals. A general overview of the loans and savings products offered through the REFFA are presented in Table 1, although they are always adapted to the local market environment.

Table 1

Education loans and savings products offered by REFFA's financial intermediaries

Education loans Support both supply and demand sides of the education market.	Education provider loans (supply) Loans with customisable repayment schemes available to education providers for the purpose of investing in their institutions.
	Education loans for students and their families (demand) Short, medium or long-term loans to support students and their families in paying tuition fees.
Education savings products As well as offering loan products, REFFA also promotes savings for learners and families	Cumulative deposits for education A deposit account with a maturity of up to 12 months to enable students and their families to save for educational purposes (i.e., tuition fees) for the upcoming year or term. Account holders may add to the account at any time. To ensure the end amount needed is available at maturity, a predefined savings target is set, and a no-withdrawals rule is in place.
	Savings plan for education An account with the purpose of saving for future education costs. Account holders deposit monthly fixed amounts over a period of one to three years. A limited number of withdrawals are allowed prior to maturity.
	Savings account for education A savings account for students and families who wish to save for the purpose of education but do not want or cannot afford to stick to a predefined savings plan.

Source: REFFA, n.d.-c.

As of March 2022, REFFA is providing funding and TA across 9 countries[1]. Through its investees (financial intermediaries), it is serving 2,923 education providers and approximately 125,720 students (REFFA, n.d.-b). Additionally, more than 30 capacity-building or market research projects have been successfully completed (with a further 17 under implementation) through REFFA's TA component (REFFA, 2020; REFFA, n.d.-d; REFFA, 2021).

Funding sources

Funding for REFFA derives from a blended finance fund structure. It is based on a unique public-private partnership (PPP) structured fund whereby funding from DFIs and private investors are blended in one funding structure, based in Luxembourg (REFFA, n.d.-a). The fund is split into three different tranches: junior, mezzanine and senior which allows for some funders to receive below-market returns, while others receive market-rate returns (Gallicchio & Marszalek, 2020).

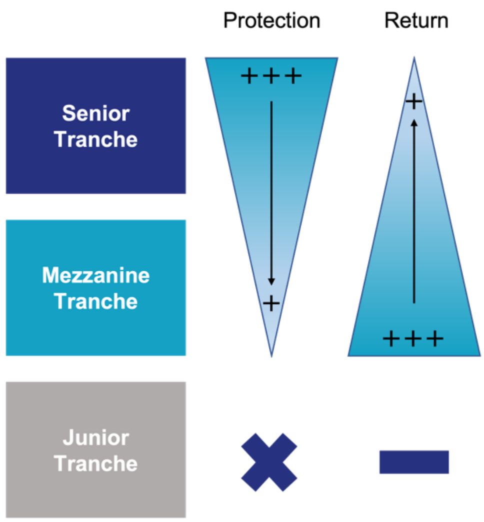
The junior tranche is funded by BMZ, represented by the German Development Bank (KFW). This tranche sees low returns and no protection, but it is catalytic for attracting investments from DFIs and private sector investors that share the objectives of the Fund but may otherwise be put off by financial risk. In 2017, the United Kingdom's (UK) Development Finance Institution, British International Investment (BII, formerly CDC) and the Organization of the Petroleum Exporting Countries (OPEC) Fund for International Development (OFID) joined, committing funding (US$ 15 million and US$ 5 million, respectively) to the mezzanine tranche. Blue Orchard – the fund manager – has also invested US$ 600,000 in the mezzanine tranche (REFFA, 2021; Blue Orchard, 2018b). To date, the senior tranche

[1] Botswana, Burkina Faso, Cameroon, Côte D'Ivoire, Ghana, Senegal, Tanzania, Tunisia, and Zambia (REFFA, 2021; REFFA, n.d.-b)

has received investments from two private investors who benefit from significant credit enhancement and risk mitigation as losses are firstly absorbed by junior and mezzanine investors (Blue Orchard, 2018b). The target fund size is US$ 100 million (REFFA, n.d.-a).

Figure 1

Financial protection and returns through REFFA's tranche funding



The main purpose of public and DFI investors is to mobilise private sector capital so that they can scale up the investment capacity. As Figure 1 above shows, the subordination of the junior and mezzanine tranches has acted as a de-risking mechanism for senior tranche investors because depending on the level of seniority, investors in different tranches receive higher or lower levels of capital protection (Blue Orchard, 2018a). Conversely, BMZ will incur the first losses and accept below-market or minimal investment returns. This three-tiered structure results in different risk-return profiles and allows private investors to receive benefits in a feasible investment environment (Blue Orchard, 2018a; Gallicchio & Marszalek, 2020). REFFA has continued to grow, with disbursements increasing by 76 % from US$ 8.5 million in 2019 to US$ 15 million in 2020 (REFFA, 2021).

Financing for the TA component differs slightly. Equally managed by Blue Orchard, it is endowed with public and private grant funds. Additionally, some junior (i.e., BMZ), mezzanine (i.e., BII) and private investors have also combined their investment in the Fund with a donation to the Technical Assistance Facility (REFFA, n.d.-a).

Critical reflections on blended finance

Blended finance has appeared as a key tool for mobilising and channelling private sector resources into investments for sustainable development within the broader development agenda (OECD, 2020). While DFIs are conventional funders in the international development area, blended finance mechanisms use this traditional funding source to leverage private sector investments. This leveraging of traditional sources of financing to crowd in new sources (private capital) is a truly innovative part of the mechanism (Gallicchio & Marszalek, 2020).

Nevertheless, the blended finance mechanism of REFFA has its limitations. Specifically, the target beneficiaries (lower-income households) are not integrated into the blended finance structure meaning that the educational impact is rarely measured nor discussed. Educational outputs are more commonly referred to, such as the number of beneficiaries reached, rather than monitoring the improved quality or affordability of education. REFFA is aware of this challenge and has started improving impact measurement and evaluation tools for monitoring the quality and affordability of education promoted by the Fund structure (REFFA, 2020).

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