Case Study

Education, Youth, and Employment Bond—Inter-American Development Bank

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Introduction

In 2014, the Inter-American Development Bank (IDB) issued its first set of bonds to direct funds to-ward governmental projects targeting education, youth, and employment (EYE) in Latin America and the Caribbean (IDB, 2014). EYE bonds are a type of social bonds. Social bonds are any type of bond instrument that is exclusively applied to finance, or re-finance in part, new or existing eligible social projects.

By 2019, the IDB reported having cumulatively raised USD 1.82 billion through 36 EYE bonds across 8 currencies. In 2019, the total available funds from active EYE bonds were invested into scaled pro-jects located in countries in South and Central America as well as the Caribbean: USD 716 million was invested into 20 projects dedicated to education, USD 60 million was invested into 6 youth projects, and USD 95 million to projects targeting employment.

According to the projected impact of the EYE bond programs, the investments from 2018 to 2022 will benefit 3 million students and train 179,000 teachers. Further, the investments will benefit 288,000 young people through youth programs and 529,000 people in the workforce by developing opportunities and training skills (IDB, 2019b).

Why education, youth, and employment bonds?

Owing to the historic developments of the global economy, countries in South and Central America as well as in the Caribbean are facing challenges of poverty and inequality to date. The Economic Commission for Latin America and the Caribbean (ECLAC) reported that of the total adult population belonging to the middle-income strata, more than half had not finished their secondary studies as of 2017. Further, in 2018, 30.1% of the region's population was below the poverty line, whereas 10.7% lived in situations of extreme poverty. In 2019, these rates reportedly rose to 30.8% and 11.5%, respectively (ECLAC, 2019).

Considering these systemic challenges, the IDB states as its vision "to work in partnership with the region to increase productivity and reduce inequality in a sustainable way, and to ultimately transform Latin America and the Caribbean into a more inclusive and prosperous society" (IDB, 2019b). The IDB aims to resolve these issues by means of "a multi-faceted, carefully planned approach that coordinates investments in human capital—people—over the course of a lifetime" (IDB, 2019b). The IDB focuses on a "life cycle" approach that aims to build human capital from "early childhood care and education, through formal primary and secondary education, as well as programs that facilitate labour market placement by improving the transition from school to work through vocational training" (IDB, 2019b).

The EYE bond programs are divided into three areas: education, youth, and employment. The educational projects invest in early childhood development and school readiness, foster high-quality teacher training, and prioritize graduates' ability to handle work and life by means of acquired skills. The programs also ensure adequate resources for learning as well as improvement of school infrastructures. For example, a project implemented in Peru set the objective to improve and expand employment centre services for formal job placement of the economically active youth population of seven different regions in Peru. In Belize, the project aimed to improve the quality of primary education and the governance of the education system by means of training for classroom teachers and instructors who train future teachers, school principals, and administration staff (IDB, 2019a).

The youth projects consist of interventions aiming to ensure the acquisition of practical life skills among young people to reduce their likelihood to engage in high-risk behaviour that may translate into economic and social costs for the individual as well as the society as a whole.
The employment projects focus on assisting the design, implementation, and evaluation of the policies that aim to improve job opportunities and develop workforce skills. Further, IDB invests in projects that increase the coverage and sustainability of social security while improving the efficiency and productivity of the workforces.

How do the EYE bonds work?

EYE bonds work as normal bonds, except for the particular use of proceeds; their mechanism can succinctly be described as follows: a private or public entity issues a bond, which is bought by investors who thereby commit their funds for a specific amount of time. The proceeds from selling the bonds are invested into a social project during the predefined time period of the bond. Upon the completion of the time period, the net investment plus coupons are paid back to the investor by the initial entity who issued the bond. Social bonds are encouraged to follow the social bonds principles, which are voluntary process guidelines that recommend transparency and disclosure regarding the payment of the proceeds to the social projects.

The EYE bonds are issued by the IDB, which was established in 1959 and is a leading source of long-term financing for economic, social, and institutional development in Latin America and the Carib-bean (IDB, 2019c). It is owned by 48 member countries: 26 Latin America and Caribbean countries as well as 22 non-borrowing member countries (IDB, n.d.).

The IDB serves as an intermediary between investors and the government entities that implement the social projects. The IDB commits to invest the total amount of the net proceeds from the sold bonds into the social projects. Owing to the multilateral nature of the IDB, it has the AAA rating, the highest international rating to guarantee return in investment, which makes its bonds an attractive secure investment (IDB, 2019a).

The EYE bonds issued by the IDB were set between three- and five-year fixed rates, meaning the investment is paid back to investors after said time period. The coupons are paid back on agreed dates generally toward the end of the established time periods in order for the projects to make a profit.

The first pricing of EYE bonds in 2014 included 24 different investors and amounted to a total of USD 500 million. The investors were mostly institutions managing income and wealth portfolios, such as Mirabaud & Cie Geneva, but also included insurance companies such as the Zurich Insurance Group as well as both central banks such as the Bank of Korea and regional banks such as the Chugoku Bank. The United Nations Development Program and the Threadneedle U.K. Social Bond Fund, a U.K. credit fund that specialized in social bonds, were among the first group of investors.

The funds raised by means of the EYE bonds are allocated by the IDB to specific projects of local governments. The project lending cycle consists of the following stages: preparation, approval, implementation, completion, and reporting. The IDB's Board of Executive Directors consists of 14 directors representing the member countries, who must individually approve each investment into a project.

The IDB has a rigorous selection process for the projects. Further, the implementation of the project is strictly supervised with the progress monitoring report (PMR) tool to guarantee the project's success. The PMR monitors activities on disbursement, financial management, procurement procedures, risk management, and/or safeguards compliance policy. It further strives to identify the delays and deviations during the project implementation phase and the changes needed during execution using a quantitative and qualitative approach that includes tracking the achievement of a project's outputs and outcomes relative to its estimated time and cost parameters (IDB, 2019b).

Overall, the IDB considers its EYE bond programs to be not only beneficial for the government and its population who benefit from the social investments but also attractive to its investors. Bob Annibale, the global director of Citi Microfinance, considers that "IDB's EYE bond enables investors to participate in financing innovative projects that lead to increased social and economic inclusion of youth, including greater employment opportunities" (IDB, 2014). Akashi Hibino, the president of Daiwa Securities Co., Ltd., further comments that they "applaud the IDB in bringing to the international investment community the opportunity to participate in their 'life cycle' approach of enriching the lives of young people in Latin America and the Caribbean. As an institution focused on social development, Daiwa regards the EYE bond as the next stage in the evolution of the ESG [Environment, Sustainability, and Government] capital markets" (IDB, 2014).

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