AIMM ANTICIPATED IMPACT MEASUREMENT & MONITORING

AIMM Sector Framework Brief
Sector Economics and Development Impact Department
International Finance Corporation

DARP
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Development Impact Thesis – The central development thesis of IFC's Distressed Assets Recovery Program (DARP) operation is the counter-cyclical role played by IFC to break the negative feedback loop generated by economic slowdown and/or increased non-performing loans (NPLs) resulting in reduced available capital, which in turn discourages new lending. IFC makes (i) direct investment in DARP servicers; and (ii) investments in DARP platforms that invest in underlying distressed assets (DA) – these can be platforms that either acquire one portfolio or several NPL portfolios or invest in single assets (either in the form of restructuring, special lending or special situations). IFC invests in these instruments to:

Project Outcomes

- → Release capital and inject liquidity in financial institutions as they dispose distressed assets
- → Restore credit and access to finance for individuals and SMEs by normalizing obligations
- → Support viable but distressed SMEs and corporates in restructuring their obligations
- → Support job preservation in SME and corporates by addressing their NPL issues
- → Introduce and enhance NPL resolution practices

Contributions to Market Creation

- → Reduce overall NPL volume in the market
- → Restore lending capacity of financial institutions and strengthen their balance sheets
- → Mobilize capital and expertise for DA investments from domestic and international investors
- → Market-wide adoption of specialized insolvency processes and best resolution practices

Development Gaps Addressed

- Volatile financial systems
- Volatile real sector, growth, and development
- Limited active secondary market
- Shallow capital markets

Rating Construct – All AIMM sector frameworks include detailed guidance notes that help define project outcomes and contributions to market creation, aggregating to an overall assessment of development impact.

- For project outcomes, stakeholders and environmental effects are the key components for which industry-specific benchmarks define the context in which an IFC operation seeks to drive changes. This gap analysis is combined with a separate set of impact intensity estimates that specify the expected results using predefined indicators.

- For contributions to market creation, industry-specific market typologies define stages of development for five market attributes (or objectives): competitiveness, resilience, integration, inclusiveness, and sustainability. These market typologies, when combined with estimates of how much an intervention affects the development of a market attribute, provide the foundation for IFC's assessment of an intervention's market-level potential for delivering systemic changes.

PROJECT OUTCOME INDICATORS		CONTRIBUTION TO MARKET CREATION INDICATORS	
Stakeholders	<u>Impact on Financial Institutions</u> • Number of distressed loans acquired (Individuals/MSMEs/Corporates) • Volume of distressed loans acquired (Individuals/MSMEs/Corporates) • Volume of liabilities supported (for investments in Single Assets only) • Increase in partner FI's capital (for NPL portfolio only) <u>Impact on Borrowers/Investees</u> • Number of borrowers with obligations normalized or restructured (Individuals/MSMEs/Corporates) • Volume of obligations normalized or restructured (Individuals/MSMEs/Corporates) • Gross IRR - Underlying Assets (for investments in Single Assets only) • Knowledge transfer to Borrower/Investee (for investments in Single Assets only) <u>Impact on Employees</u> • Improve employees' skills related to distressed assets acquisition and processing	Competitiveness	<u>Market Structure</u> • Entry of new servicers in the DA market • Market wide increase in investment in DAs (including mobilizing first time investors) <u>Market Regulation</u> • Improvement in legal/Institutional regulatory framework • Market-wide adoption of specialized processes and best practices by servicers (e.g. methodologies, departments, trained officers, resolution practices)
		Integration	<u>Financial Integration</u> • Trigger cross-border investments in DA (e.g. establish regional platform for investment in smaller economies) • Create secondary market for DA investing • Contribute to increased networking among FI and servicers, and regional/global expansion of servicers <u>Capital Mobilization</u> • Capital mobilization potential (e.g. develop platforms for DA (co)investment facilities, first time investment in DA class)
Economy-wide	• Impact on value-added (TBD) • Impact on employment (TBD)	Resilience	<u>Market's Financial Stability</u> • Increase in formalization of DA market

IFC's Environmental and Social Performance Standards define IFC clients' responsibilities for managing their environmental and social risks. While for most IFC investments meeting Performance Standards reflects improved environmental and social performance, effects from implementation of the standards are only claimed in the AIMM framework where a clear counterfactual can be established and where the investment intent is to improve environmental or social outcomes.

Sector Specific Principles or Issues – The following principles will be applied for projects rated under this framework:

Principle or Issue	Treatment Under Framework
Pricing gap	A key challenge in developing a market for NPLs is closing the pricing gap, which is the difference between the price that a prospective seller of NPLs believes those assets should command and the significantly lower price that would convince a prospective buyer that he or she has been fully compensated for the risk and uncertainty associated with the assets and for the initially high transaction costs, especially in a highly underdeveloped market.
Inadequate insolvency regimes	Well-functioning insolvency regimes are particularly important for a highly underdeveloped DA market and have two main functions: (i) to preserve value; and (ii) to distribute value. As these two functions occur successively, certain attributes of an insolvency regime that can initially extinguish value (such as immunities, as they apply to secured or privileged debt) may significantly reduce the ultimate amount of value that is available to be distributed.
Lack of secondary DA markets	An active DA secondary market is needed to attract and maintain investors seeking to deploy capital across multiple types of DA classes. Secondary trades increase the ability for investors to generate liquidity events for its DA portfolio and promote easiness of transacting. However, DA secondary markets are typically underdeveloped in many emerging markets and lower the value of DA.
Data unavailability and information asymmetry	Buyers want to have information regarding the nature and status of defaults, a history of attempts to enforce the loan agreement, lender-borrower correspondence, and inter-creditor correspondence. Adequate transparency regarding potential flaws in the governing legal documents is essential to allow NPL buyers to ascertain their value recovery and financial-return prospects. NPL information and data quality issues with which banks must deal include missing historical data regarding exposures, discrepancies between loan documentation and data records, missing or incomplete documentation, breaks or anomalies in the chain of title, flawed data on loan collateral and valuation methods, and frequent changes in data sources that exacerbate data quality problems.
Treatment of negative effects	No negative effects are anticipated. In cases where negative effects occur, these would be assessed on a case by case basis and only if it is material enough to affect the project assessment.

Project Outcomes – Depending on the type of project, the stakeholders are (i) financial institutions (FIs) and other credit originators, benefiting from balance sheet clean-up, improved profitability, and expanded lending capacity; (ii) borrowers (MSMEs/Corporates/Individuals) or investees (stressed or distressed but viable companies/projects) whose obligations are normalized or restructured and can regain access to credit as well as retain their most valuable assets; (iii) jobs preserved in the firms that benefit from resolution, restructuring or special lending; and (iv) employees of the DARP servicers in which IFC invests.

The development gap is an estimate of the development challenge that is being addressed by the project and provides context for the project's development outcomes. The gap is sector- or segment-specific and is benchmarked against all emerging market countries. The gap assessment uses data collected by IFC from various public sources. The table below illustrates an application of some of the main outcome gap indicators and their benchmarking. Apart from gap indicators that are naturally bound, all gap indicators are normalized to be scale-free (e.g. relative to GDP or to total population).

COUNTRY CONTEXT	Low Gap	Medium Gap	Large Gap	Very Large Gap
Access	The following are >1 STD above EM median: – Quality of the judicial processes index (0-18) – Resolve Insolvency - yrs – Resolve Insolvency - Cost % – Resolve Insolvency - Recovery rate (cents on $) – Resolve Insolvency - Strength of insolvency framework index (0-16) – Change in NPL to Total Gross Loans (%) over 3 yrs – NPLs to Total Gross Loans	The following are within 1 STD EM median: – Quality of the judicial processes index (0-18) – Resolve Insolvency - yrs – Resolve Insolvency - Cost % – Resolve Insolvency - Recovery rate (cents on $) – Resolve Insolvency - Strength of insolvency framework index (0-16) – Change in NPL to Total Gross Loans (%) 3 yrs – NPLs to Total Gross Loans	The following are < 1 STD below EM median: – Quality of the judicial processes index (0-18) – Resolve Insolvency - yrs – Resolve Insolvency - Cost % – Resolve Insolvency - Recovery rate (cents on $) – Resolve Insolvency - Strength of insolvency framework index (0-16) – Change in NPL to Total Gross Loans (%) 3 yrs – NPLs to Total Gross Loans	The following are below EM 15th percentile: – Quality of the judicial processes index (0-18) – Resolve Insolvency - yrs – Resolve Insolvency - Cost % – Resolve Insolvency - Recovery rate (cents on $) – Resolve Insolvency - Strength of insolvency framework index (0-16) – Change in NPL to Total Gross Loans (%) 3 yrs – NPLs to Total Gross Loans

The core outcomes for DARP projects include access to DA finance and economy wide effects through jobs preservation (applicable only for single assets investments). Access refers to the availability of DA finance for both FIs (owners of the distressed loans) and for the companies (borrowers or investees) or households (borrowers) in the FIs' portfolios. In cases where operations involve the acquisition of an NPL portfolio from an FI, the core indicators are (i) volume of distressed loans acquired and (ii) volume of distressed loans normalized/restructured. For investment in single assets, the core indicators are (i) volume of FI debt supported; (ii) gross IRR of the underlying assets; and (iii) knowledge transfer to investee. Economy-wide effects are considered for single asset investment and it is related to the impact of alleviating debt distress on the affected companies and its impact on employment. Due to an inadequate resolution regime and/or underdeveloped DA markets, liquidation is often the only available alternative, and when viable businesses are liquidated instead with unnecessary job losses and loss of human and intangible capital. One measure is the number of jobs preserved at the distressed companies that DARP projects support.

PROJECT INTENSITY	Below Average	Average	Above Average	Significantly Above Average
Access (financial institutions) • Volume of distressed loans acquired • Number of distressed loans acquired • Volume of liabilities supported (note: may only apply to certain Single Assets projects) • Capital increase of partner FI (if DARP platform is set up to acquire NPLs from one specific FI)	– Absolute change in number of NPLs acquired by the respective DARP platform is insignificant compared to the total number of outstanding NPLs in the market for that asset class – Absolute change in volume of NPLs acquired (measured as outstanding balance of the loans) by the respective DARP platform is insignificant compared to the total volume of outstanding NPLs in the market for that asset class – Interest Coverage Ratio: Underlying single assets of the relevant DARP platform have very small volume of liabilities that is at risk of becoming distressed in the absence of new capital/financing provided – Very small increase in the capital of the partner FI compared to the last reporting period	– Absolute change in number of NPLs acquired by the respective DARP platform ranges is slightly significant compared to the total number of outstanding NPLs in the market for that particular asset class – Absolute change in volume of NPLs acquired (measured as outstanding balance of the loans) by the respective DARP platform slightly significant compared to the total volume of outstanding NPLs in the market for that particular asset class – Interest Coverage Ratio: Underlying single assets of the relevant DARP platform have small volume of liabilities that is at risk of becoming distressed in the absence of new capital/financing provided – Small increase in the capital of the partner FI compared to the last reporting period	– Absolute change in number of NPLs acquired by the respective DARP platform is significant compared to the total number of outstanding NPLs in the market for that particular asset class – Absolute change in volume of NPLs acquired (measured as outstanding balance of the loans) by the respective DARP platform is significant compared to the total volume of outstanding NPLs in the market for that particular asset class – Interest Coverage Ratio: Underlying single assets of the relevant DARP platform have a large volume of liabilities that is at risk of becoming distressed in the absence of new capital/financing provided – Large increase in the capital of the partner FI compared to the last reporting period	– Absolute change in number of NPLs acquired by the respective DARP platform is very significant compared to the total number of outstanding NPLs in the market for that asset class – Absolute change in volume of NPLs acquired (measured as outstanding balance of the loans) by the respective DARP platform is very significant compared to total volume of outstanding NPLs in the market for asset class – Interest Coverage Ratio: Underlying single assets of the relevant DARP platform have a very large volume of liabilities that is at risk of becoming distressed in the absence of new capital/financing provided – Very large increase in the capital of the partner FI compared to the last reporting period

PROJECT INTENSITY	Below Average	Average	Above Average	Significantly Above Average
Access (borrowers & investees) • Number of borrowers with loans normalized or restructured • Volume of loans normalized or restructured • Gross IRR of underlying assets (note: may only apply to certain Single Assets projects) • Knowledge Transfer to Investee (note: may only apply to certain Single Assets projects)	– Absolute change in number of borrowers being normalized is insignificant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Absolute change in volume of the obligations of borrowers being normalized (measured as outstanding balance of the loans acquired) is insignificant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Gross IRR is below the average range of gross IRR based on DARP experience – Borrowers/investees do not engage actively with the DARP servicer with limited to no knowledge transfer	– Absolute change in number of borrowers being normalized is slightly significant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Absolute change in volume of the obligations of borrowers being normalized (measured as outstanding balance of the loans acquired) is slightly significant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Gross IRR is within the average range of gross IRR based on DARP experience – Some borrowers/investees engage actively with DARP servicer, who provides some knowledge transfer with a clear hands-on investment management process	– Absolute change in number of borrowers being normalized is significant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Absolute change in volume of the obligations of borrowers being normalized (measured as outstanding balance of the loans acquired) is significant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Gross IRR is above the average range of gross IRR based on DARP experience – Many of the borrowers/investees of the relevant DARP platform engage actively with the DARP servicer	– Absolute change in number of borrowers being normalized is very significant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Absolute change in volume of the obligations of borrowers being normalized (measured as outstanding balance of the loans acquired) is very significant compared to the total borrowers acquired by the relevant DARP platform for the life the project – Gross IRR is significantly above the average range of gross IRR based on DARP experience – Majority of the borrowers/investees of the relevant DARP platform engage actively with the DARP servicer
Employees • Improve employees' skills related to distressed assets pricing	– Employees use rudimentary pricing models and collection practices, while the servicers have not adopted best practices in the acquisition and resolution of NPLs and/or get low ratings	– Employees use basic pricing models and collection practices, while the servicers have not adopted best practices in the acquisition and resolution of NPLs and/or get low ratings	– Employees use standard pricing models and collection practices, while the servicers have not adopted best practices in the acquisition and resolution of NPLs and/or get low ratings	– Employees use pricing models and collection practices that are of global standard, while the servicers fully adopt best practices in the acquisition and resolution of NPLs and/or get very high ratings
Economy-wide • Number of jobs preserved at borrowers with loans normalized (for single assets projects)	– Very few jobs being preserved relative to the total number of employees of the investees at the time of investment	– Moderate number of jobs being preserved relative to the total number of employees of the investees at the time of investment	– Significant number of jobs being preserved relative to the total number of employees of the investees at the time of investment	– Number of jobs being preserved is sizable relative to the total number of employees of the investees at the time of investment

The AIMM methodology considers the uncertainty around the realization of the potential development impact being claimed, making a distinction between the potential outcomes that a project could deliver and what could be realistically achievable in the project's development context. The table below presents the key types of risk factors for water and wastewater services operations.

PROJECT LIKELIHOOD	Project Factors	Sector Factors
Assessment Considerations	• Experience and track record of the investor/servicer in the relevant asset class • Project's projected growth relative to the recent history of the sponsor and available scalable capacity • Expansion into markets (e.g. new country or sub-national) • IFC providing AS or is part of systematic WBG engagement addressing insolvency regime	• Target sector's market risks (e.g. lack of restructuring culture) • Specific regulatory risks (e.g. weak legal framework or lack of framework for asset transfers) • Central bank supervision perimeter and capacity (e.g. lack of clear provisioning framework) • Supporting government policies and programs (e.g. regulatory reform agenda or national bad bank)

Contribution to Market Creation – This assesses the degree to which a project induces systemic changes in the market through catalytic effects and focuses on up to two major attributes for each project. The "market" here is defined as the distressed assets market in emerging market countries or other developed financial markets with overhanging NPLs.

The table below focuses on core market attributes that IFC investment projects typically affect. IFC's detailed guidance note includes more information on how IFC investment projects may contribute to changes in the other market attributes.

MARKET TYPOLOGY	Highly Developed	Moderately Developed	Underdeveloped	Highly Underdeveloped
Competitiveness	– Many servicers, most of them quite sophisticated, for the relevant DA class – Many specialized international/domestic DA investors participating in the acquisition of NPLs on a regular basis, or regular participation of first-time investors in the country and/or the relevant DA class – Strength of insolvency framework index is very high – Quality of the judicial processes index is very high – Very strong legal/institutional regulatory framework in the country – Servicers in the country follow resolution best processes and/or practices at par with other more mature DA markets and, if rated, have strong ratings	– Some servicers for relevant DA class, a few of them with a certain degree of sophistication – Some specialized international/domestic DA investors participating in the acquisition of NPLs on a regular basis and a few investors participating opportunistically, or limited percentage of NPL sale transactions with participation of first-time investors in the country and/or the relevant DA class – Strength of insolvency framework index is high – Quality of the judicial processes index is high – Strong legal/institutional regulatory framework in the country – Servicers in the country have incorporated some resolution processes and/or adopted best practices from other more sophisticated market and, if rated, have medium ratings	– Existing servicers are not active or few unsophisticated servicers for relevant DA class – Few specialized international/domestic DA investors participating in the acquisition of NPLs or very limited percentage of NPL sale transactions with participation of first-time investors in the country and/or the DA class – Strength of insolvency framework index is moderate – Quality of the judicial processes index is moderate – Weak legal/institutional regulatory framework in the country – Servicers in the country follow very basic resolution processes and/or practices and, if rated, have low ratings	– No servicers active in the country – No specialized international/domestic DA investors participating in the acquisition of NPLs or no NPL sale transactions with participation of first-time investors in the country and/or the DA class – Strength of insolvency framework index is low – Quality of the judicial processes index is low – Very weak legal/institutional regulatory framework in the country – Servicers in the country do not follow any standard resolution processes and/or practices and are not rated

MARKET TYPOLOGY	Highly Developed	Moderately Developed	Underdeveloped	Highly Underdeveloped
Integration	– Many domestic servicers or specialized investors in DA operate both in their domestic market and have established multi-country presence. International servicers or specialized DA investors operate regularly in that country – Many banks participate regularly (ownership or commercial) in servicing companies or act as investors in the acquisition of NPLs either from their balance sheet or from other financial institutions – Many established multi-investor DA platforms operating on a regular basis. First time investors in DA class participate regularly in NPL sale transactions alone or in partnership with existing investors. – Many rated securitizations of NPLs either from credit originators (bank, financial institutions, retailers, utilities) or other investors (selling NPLs that they have previously acquired) have occurred in the last three years, with the participation of institutional investors not specialized in DA.	– Some domestic servicers or specialized investors in DA operate in their domestic market and sporadically in other countries. Some international servicers or specialized DA investors operate in that country opportunistically – Some banks have participation (ownership or commercial) in servicing companies or act as investors in the acquisition of NPLs either from their B/S or from other financial institutions – Several established multi-investor DA platforms operating on a regular basis. NPL sale transactions being funded mostly by existing investors and not by first time investors in DA class (being totally or partially) who participate sporadically. – Several rated securitizations of NPLs either from credit originators (bank, financial institutions, retailers, utilities) or other investors (selling NPLs that they have previously acquired) have occurred in the last three years, with the participation of institutional investors not specialized in DA	– Few domestic servicers or specialized investors in DA operate in their domestic market and sporadically in other countries. Limited number of international servicers or specialized DA investors operate in that country opportunistically – Few banks have participation (ownership or commercial) in servicing companies or act as investors in the acquisition of NPLs either from their B/S or from other financial institutions Few established multi-investor DA platforms in the country. NPL sale transactions being funded by existing investors and not by first time investors in DA class (totally or partially). – Few rated securitizations of NPLs either from credit originators (bank, financial institutions, retailers, utilities) or other investors (selling NPLs that they have previously acquired) have occurred in the last three years, with the participation of institutional investors not specialized in DA	– If existing, domestic servicers or specialized investors in DA operate only in their domestic market and do not have multi-country presence. No international servicers or specialized DA investors operate in that country – No banks have participation (ownership or commercial) in servicing companies or act as investors in the acquisition of NPLs either from their balance sheet or from other financial institutions. – No established multi-investor DA platforms in the country. NPL sale transactions being funded by existing investors and not by first time investors in DA class (totally or partially). – No rated securitizations of NPLs either from credit originators (bank, financial institutions, retailers, utilities) or other investors (selling NPLs that they have previously acquired) have occurred in the last three years.
Resilience	– Most of the NPL transactions (either bilateral or competitive) are being made public on a regular	– NPL sale transactions (either bilateral or competitive) are being made public sporadically	– No NPL sale transactions (either bilateral or competitive) are being made public	– No market exists

In general, most individual projects are not expected to make a significant and immediate systemic market change, unless the project is a pioneer in a non-existent or nascent market. Instead, most projects are expected to have incremental effects on the market. In other words, it takes more than one intervention to move a market to the next stage. This means that integrated and concerted efforts are often needed to generate substantial market effects. For example, cumulative World Bank Group efforts over time will have a stronger effect on markets than non-integrated and non-concerted interventions. Where a project is explicitly part of a programmatic approach, the expected movement induced by the program should be the basis for the assessment where timebound movements, market effects, and indicators are available. The most important effects from IFC's DARP operations are:

MARKET MOVEMENT	Marginal	Meaningful	Significant	Highly Significant
Competitiveness	– Entry of new servicers in relevant DA class – Entry of new international/domestic investors in relevant DA class – Improvement in legal/institutional regulatory framework – Market-wide adoption of specialized processes and best practices by servicers (e.g. methodologies, departments, trained officers, resolution practices).			

MARKET MOVEMENT	Marginal	Meaningful	Significant	Highly Significant
Integration	– Triggering cross-border investment in DA through establishment of multi-investor regional platforms and/or entry of international investors – Increased number of FIs initiating participation (ownership or commercial) in servicing companies or as investors in the DA acquisition – Capital mobilization potential (e.g. develop regional/global platforms for DA (co)investment facilities, first time investment in DA class) – Formation of secondary market for DA investing			
Resilience	– Increase in formalization of DA market			

The market likelihood adjustment follows the principles for the likelihood adjustment for project outcome potential. In general, the likelihood assessment includes sector-specific, as well as broad country risks that may prevent potential catalytic effects from occurring, plus political economy or policy/regulatory risks that may constrain market systemic change. Due to the diversity of market creation attributes and channels, most of the likelihood factors are expected to be sector, or intervention specific.

MARKET LIKELIHOOD	Sector Factors	Political / Policy Factors
Assessment Considerations	• Concentration in the distressed assets market (e.g. barriers to entry, number of market participants relative to the size of the DA market, etc.) • Strength of the channel for competitive pressures and incentives to adopt innovations • Presence of WBG upstream work about sector regulation etc.	• Regulatory and legal infrastructure (e.g. Insolvency index for jurisdiction) • Government policies and commitment (e.g. regulatory reform agenda or national AMC) • Medium term macroeconomic outlook, and capacity to absorb sectoral shocks