**[Time to Think Outside the Box: Buy-Downs as an Education Financing Option](https://norrag.wordpress.com/2015/09/29/time-to-think-outside-the-box-buy-downs-as-an-education-financing-option/)**

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Late last week, world leaders met to adopt ambitious new sustainable development goals (SDGs) that will shape international development for the next 15 years. There is a great deal of optimism surrounding the new agenda. Yet it is almost certain that the SDGs will fail if equally ambitious and innovative financing strategies such as debt and loan buy-downs are not adopted. This is especially true for education – a sector that has been slow to capitalize on the growth of alternative sources of finance.

SDG 4 is to “ensure quality education for all.” The cost of achieving universal basic and secondary education by 2030 [is estimated at US$340 billion per year](http://unesdoc.unesco.org/images/0023/002321/232197E.pdf) for low and lower middle income countries. This represents an annual financing gap of [US$40 billion per year](http://unesdoc.unesco.org/images/0023/002321/232197E.pdf) if current spending levels continue. Given this gap, there is an urgent need to find bold new financing solutions. The adoption of the SDGs presents a unique opportunity for education to break from the status quo and embed innovative finance, such as debt and loan buy-downs, as an integral part of the next financing architecture.

Although the mechanics of a buy-down can be complex, the idea itself is not. Buy-downs are an arrangement where a third party agrees to pay the interest or principal of a loan, thereby releasing the borrowing country from all or some of its future repayment obligations.

There are two types of buy-downs, debt and loan.  Debt buy-downs are current debt that is bought down by a third party. In a loan buy-down, future loans are either softened ahead of time or triggered when the borrowing country achieves pre-defined targets. For example, the [Global Partnership for Education](http://www.globalpartnership.org/) could agree to buy-down a future [IBRD](http://www.worldbank.org/en/about/what-we-do/brief/ibrd) loan to Bangladesh if they meet the target of 100% lower-secondary enrollment.

These are attractive options for several reasons.

One, buy-downs have the potential to “crowd in” resources for education. The buy-down option based on triggers could greatly incentivize countries to meet key development targets, demonstrating effectiveness and thereby encouraging more lending.

Second, buy-downs could free up resources that would have otherwise gone to debt servicing. As a rough example, before the Heavily Indebted Poor Country (HIPC) Initiative, eligible countries were on average spending more on debt service than on health and education combined. Since the HIPC Initiative, spending on health and education is about five times the amount of debt-service payments.[[1]](https://norrag.wordpress.com/2015/09/29/time-to-think-outside-the-box-buy-downs-as-an-education-financing-option/%22%20%5Cl%20%22_ftn1) The use of buy-downs could potentially have a similar effect.

Third, loan buy-downs could open capital to countries otherwise deemed ineligible or credit unworthy. These would include low-income countries unable to take on more debt but in serious need of external support for basic education, such as Afghanistan, Burundi, Chad, Democratic Republic of Congo and Tajikistan. Any buy-downs for these countries would essentially be similar to a grant.

Loan-buy downs could also soften the loan terms for countries in both sides of the IDA/IBRD threshold. These countries also have some of the largest out-of-school populations in the world. They include countries such as Angola, Bangladesh, India, Nigeria, Pakistan and Sri Lanka. The immediate potential seems greatest with regard to lending by the World Bank Group (both non-concessional IBRD and concessional IDA) and the Islamic Development Bank (mainly non-concessional).

Fourth, the potential of buy-downs are too immense to ignore. The World Bank estimates that loan buy-downs could “leverage funding so that $1 translates into $3 in development assistance.” In other words, buying down the interest rate and parts of the principal with $10 million today would release the borrower from $30 million in future repayments.

Why is this important? Research shows that traditional sources of finance, although extremely important, will not be able to sufficiently mobilize the needed resources to achieve the education SDGs. According to the Education for All Global Monitoring Report, government spending on basic education in low and lower middle income countries will need to increase from 3.5% to 6.3% of GDP to meet the $340 billion annual cost. Most low income countries already fall short of the required level to meet current education targets.

The recent decline in aid to education is also worrying. [From 2010 to 2012](http://unesdoc.unesco.org/images/0022/002281/228184E.pdf) aid to total education fell by 10%, a considerable decline when compared with the overall aid decline of 1% in the same period. Countries like the Netherlands, France, and Japan have reduced their aid to education during the same period. In addition, new policies have also hardened the terms in which countries can borrow loans or receive grants – with some requiring repayment of the entire “grant.”

Given these developments, financing strategies for education will need to go hand in hand with innovative financing and buy-downs are one option that has the potential to unlock significant financial resources.

If the international community is ever to meet the education SDGs, innovative financing such as buy-downs must become part and parcel of the global financial architecture. The adoption of broader and more ambitious SDGs will only make the availability of traditional funds scarcer. Unless alternative financing options are embraced, education will continue to be underfunded and traditional – and the world will truly miss the chance to ensure that everyone has the right to a quality education.

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[[1]](https://norrag.wordpress.com/2015/09/29/time-to-think-outside-the-box-buy-downs-as-an-education-financing-option/%22%20%5Cl%20%22_ftnref1) International Monetary Fund