FC Financial products - Development loans

KfW uses development loans as a financing instrument in Financial Cooperation (FC) with developing countries and emergingeconomies.

The commissioning party is the Federal Government

In order to increase the impact of the budget available for development cooperation and to increase the German funding volume, KfW, together with the Federal Ministry for Economic Cooperation and development (BMZ), created the so-called “development loan” instrument. Development loans represent a mixture of loans and grants from the federal budget together with KfW's own resources, which KfW takes on at favorable conditions on the capital market.

Essential characteristics

- In principle, development loans can be used in all politically important sectors.
- The borrowers are usually states or state project sponsors.
- The mix of budget and KfW funds is determined in such a way that the projects can bear the financing costs and the loans comply with the international agreements on Official Development Aid (ODA). Lending conditions of development loans are higher than those of loans on mere budgetary resources, but well below the market conditions.

The product group of development loans includes interest-reduced loans and composite financing. In the case of low-interest loans, KfW uses only funds borrowed at the capital market. In general, a Federal guarantee framework is used to limit KfW’s credit risk. Loan interest rates are further lowered for the borrower using budgetary funds. Low-interest loans are made available to local financial institutions, for example, to increase their scope for lending and to improve the supply of credit to small enterprises. These loans are also used to support infrastructure projects worthwhile to support for political reasons. In many cases, the provision of favourable and reliable financing paves the way for innovative and sustainable energy, environment and climate technologies to be put to use. In composite financing, the credit risk of KfW Development Bank is largely covered by a guarantee framework of the Federal Government. As with low-interest development loans, politically important projects in developing countries are being promoted. In this case, favorable loans from budget resources with long terms are supplemented by KfW’s own resources and handed out as two tranches to the partner. The lending rates of the KfW tranche are fixed on risk-based terms and are not subsidised by the Federal Government. Composite financing is particularly suitable for (infrastructure) projects with long amortisation. The provision of long loan terms meets the specific needs of long-lasting infrastructure projects.

Initiating loans and preparing projects

The promoted projects, which are to be financed by a development loan, are proposed by the governments of the partner countries and pledged to the partner in the course of government talks. In the further course of the project preparation, KfW examines on behalf of the Federal Government whether the projects are politically sensible and eligible for promotion. This is usually done on the basis of a detailed feasibility study, which also analyses social and environmental risks, as well as an on-site project appraisal. In addition, a detailed credit risk analysis is carried out for development loans. A sustainable financing concept (including collateral) is developed together with the project participants. If the project is approved, the loan can be granted to the partner. KfW accompanies the projects throughout the whole project term.

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