



BII's Problem Isn't Ambition, It's Capital—and Here's How to Fix It

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A capital model no longer fit for purpose

The challenge facing British International Investment (BII), the UK's Development Finance Institution (DFI), is not a lack of ambition or political support, but a capital model that has yet to catch up with what it is being asked to do by the UK government.

As [UK aid budgets tighten](#) and the government increasingly frames development as an [investor-led endeavour](#), expectations of BII continue to rise: more climate finance, greater private capital mobilisation (PCM), and more investment in frontier markets. The question is no longer whether BII's mandate should evolve but whether its capital model is still fit for purpose.

Until now, this question has barely featured. BII has not been capital constrained, has relied entirely on ODA-funded shareholder equity and retained earnings. But that world is changing. Large new ODA injections are unlikely and [recent UK fiscal reforms](#) have reduced the bias against borrowing by public institutions. BII is undertaking a strategy refresh for 2026 that will double down on these expanded expectations, but with far less attention to how its balance sheet underpins those ambitions.

If BII is to scale its climate ambitions, mobilise private capital, and strengthen its distinctive catalytic role in the hardest markets, it will need to use its balance sheet more strategically. One option explored here is the careful and selective use of leverage. Once seen as radical, leveraging BII's shareholder capital is increasingly becoming a practical necessity.

Why the context has changed

Three shifts make a reconsideration of BII's capital model both timely and unavoidable.

First, fiscal reality.

The UK's development budget is under sustained pressure, with planned reductions from [£15.4 billion to £9.2 billion, a reduction of roughly £6.1 billion](#) by 2027. Against this backdrop, large new shareholder equity injections into BII are unlikely, even as demand for development and climate finance, particularly in low-income and fragile contexts, continues to grow.

Second, a shift in UK public-finance thinking.

Recent reforms have moved away from a narrow focus on [public sector net debt toward broader balance-sheet measures](#), notably Public Sector Net Financial Liabilities (PSNFL) and Public Sector Net Worth (PSNW). These frameworks place greater weight on net assets and risk-adjusted exposure, reducing the automatic fiscal penalty historically associated with borrowing by public entities such as BII.

Third, rising expectations of BII.

The UK government increasingly frames development as an investor-led endeavour, with BII positioned as a central delivery vehicle. Expectations now extend well beyond deploying equity investments: BII is expected to mobilise private capital at scale, support climate mitigation in Middle Income Countries, operate across a wider range of markets, focus on market creation and increase its investment in the most challenging environments.

Together, these shifts expose a growing mismatch between BII's ambitions and an entirely shareholder equity-funded balance sheet.

BII's distinctive role and why it matters

BII is unusual among DFIs. Since 2012, it has focused primarily on Sub-Saharan Africa and South Asia, deploying patient equity investments in high-risk, market-creating investments rather than prioritising short-term mobilisation.

That catalytic role is evident across sectors. In energy, it created [Globeleq](#) and later [Gridworks](#), demonstrating that privately owned power generation and transmission could succeed in Africa. In renewables, it founded [Ayana Renewable Power](#) in India and anchored the [Africa Renewable Energy Fund](#), catalysing follow-on investment. In finance, early backing of [Helios Investment Partners](#) and [M-KOPA](#) helped establish African private equity and digital finance as investable sectors. More recently, through [Growth Investment Partners](#), BII has pioneered a permanent-capital platform to address the SME growth-capital gap by establishing locally based investment companies

This is not incidental. BII's public value lies precisely in its willingness to take risks that others cannot or will not. Any reform to its capital model must protect, not dilute, this function.

Strategy evolution and an emerging tension

BII's 2022–2026 strategy marked a clear evolution. While retaining its core focus on Africa and South Asia, it expanded both thematic and geographic scope. Climate finance moved to the centre of the strategy, with increased investment in green infrastructure, alongside a new push into digital transformation, from large-scale digital infrastructure to early-stage venture capital backing disruptive technologies. The strategy also expanded BII's geographic remit to the Indo-Pacific and the Caribbean. In the Indo-Pacific, particularly in the larger economies of the Philippines, Indonesia, and the Mekong region (Vietnam, Cambodia, and Laos), the emphasis has been on climate investment, especially renewable energy. This reflected both UK foreign-policy objectives and the reality that large-scale climate investment is increasingly concentrated in more commercially viable markets.

The forthcoming 2026 strategy refresh is expected to deepen this trajectory, with four themes likely to feature prominently:

1. A stronger emphasis on private capital mobilisation, implying greater differentiation across markets.
2. More deliberate market-shaping and system-level impact, building on BII's strengths beyond individual transactions.
3. Continued, and expanded, engagement in frontier and fragile markets, where patient capital remains essential.
4. Partnerships as the default model, with other DFIs, MDBs, institutional investors, and domestic financial institutions.

These priorities sharpen a central tension. How can BII operate at scale in more commercial markets without reducing its capacity to make high-risk, catalytic investments that define its comparative advantage? The answer depends critically on how its shareholder capital is used.

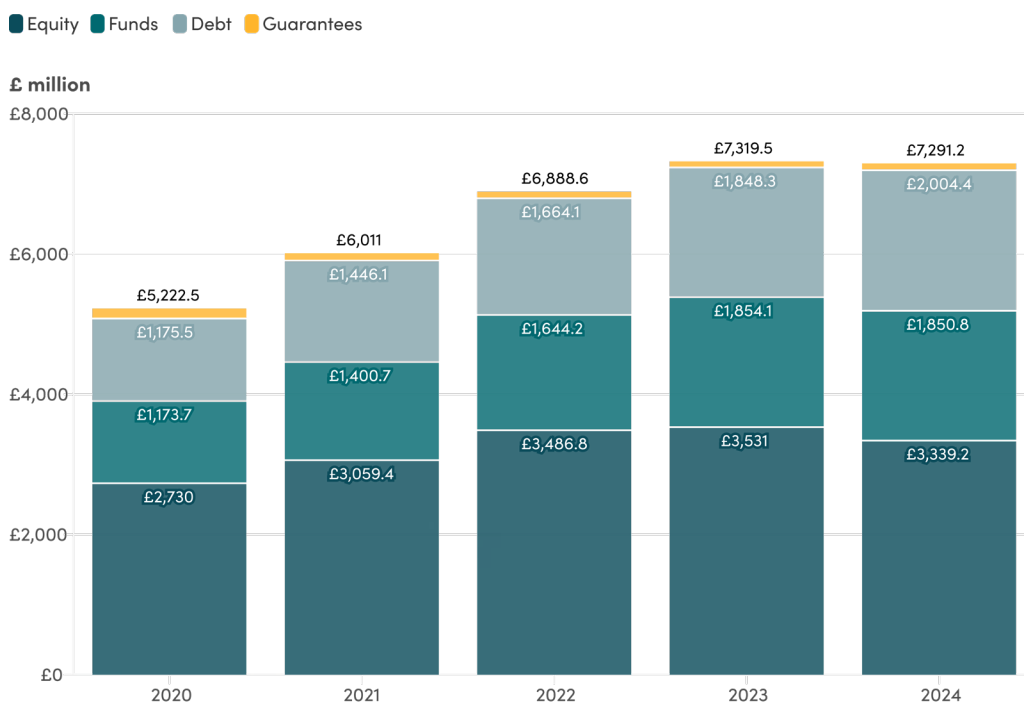
Why the current capital model is increasingly inefficient

BII organises its investments across three portfolios with distinct objectives and risk profiles. The [Growth Portfolio](#), which accounts for the majority of BII's investment, focuses on scaling established businesses and sectors, primarily through debt investments and later-stage equity investments. The [Catalyst Portfolio](#) supports earlier-stage, higher-risk investments in frontier and fragile markets, including market creation and platform building, where private capital is largely absent. BII's recently introduced [Kinetic Portfolio](#) is designed to support highly catalytic investment strategies

and operates with a higher risk tolerance than the Growth and Catalyst portfolios. It is funded by a grant from BII's shareholder, FCDO.¹

Despite these differences, the Growth and Catalyst portfolios are financed entirely through BII's shareholder equity, which raises questions about whether the current capital structure remains well aligned with the risk profile of the portfolio. Shareholder equity is the most expensive form of capital, intended to absorb high levels of risk and uncertainty. Yet a growing share of BII's investments now consists of lower-risk, predictable, income-generating debt. The share of debt in BII's total portfolio increased from 23 percent in 2020 to 27 percent in 2024 (Figure 1), with 92 percent of this debt concentrated in the Growth Portfolio as of end-2024 (Figure 2). This shift sits alongside evidence from GEMS database showing that default rates on MDB and DFI private sector lending are lower than often assumed and recovery rates are high. As BII expands lower-risk lending and climate investment in more commercially viable markets, a growing share of its shareholder equity is therefore tied up in assets that generate steady but modest returns, leaving less capital available for the highest-risk, market-creating investments where BII's additionality is greatest. In this context and noting that many MDBs and some bilateral DFIs finance their investment portfolios using a mix of shareholder equity and debt (Table 1), there may be scope to reassess how different parts of BII's portfolio are funded.

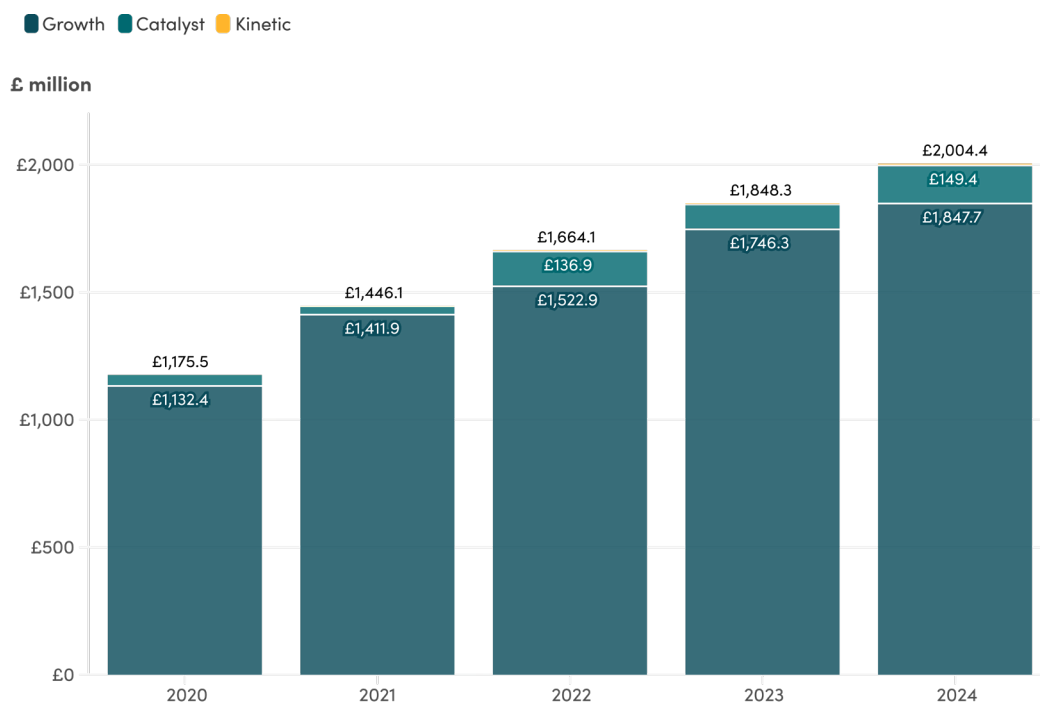
Figure 1. Value of BII portfolio by product



Source: Data provided by BII.

¹ BII's mandate has been extended to allow investment in Ukraine and Ukraine-linked regional funds as part of the UK Government's response to the war and long-term recovery efforts. This extension was accompanied by a £250 million allocation of new capital. Implementation of the Ukraine portfolio began in 2024 through commitments, with no Ukrainian acquisitions recorded in that year.

Figure 2. Value of BII debt investments by portfolio



Source: Data provided by BII.

Table 1. How selected DFIs use leverage

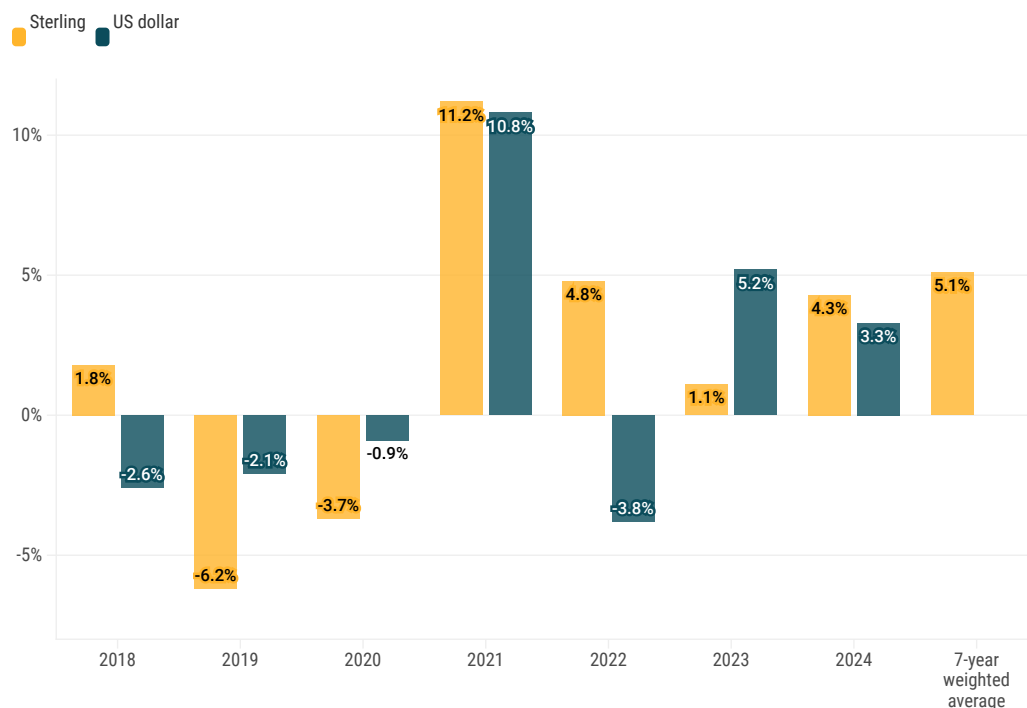
	BII	DEG	DFC	FINDEV CANADA	FMO	IFU	NORFUND	PROPARCO	SWEDFUND
Debt funding directly raised in the capital markets					X				
Debt funding raised in the capital markets by the corresponding controlling entities		X						X	
Debt funding provided by the controlling country shareholder			X	X		X			
Without any debt funding	X						X		X
Debt-to-shareholder equity ratio	NA	2.23	1.37	0.33	1.70	0.28	NA	3.50	NA

* Author's calculations based on DFI annual reports. • Calculated as a simple ratio: gross debt (interest bearing) divided by shareholder equity. • DFC calculated at 30.09.2025, all other DFIs calculated at 31.12.2024. • IFU borrows from Denmark's Central Bank. • NA = not applicable.

Beyond questions of capital efficiency across the portfolio, the funding model also matters for how BII grows over time. When BII relies entirely on shareholder equity, the pace at which it can expand is closely tied to the returns it generates and retains. This makes the relationship between portfolio composition, returns, and future investment capacity particularly important.

BII currently manages a portfolio of around £7.3 billion backed by just under £10 billion in net assets. Over the past seven years, it has generated average portfolio returns of around 5 percent, equivalent to a post-tax return on equity of roughly 2½ percent and annual profits of about £200 million (Figure 3). These are reasonable returns for a catalytic investor operating in difficult markets. But under a shareholder equity-only funding model, they also mean that retained earnings are the primary source of balance-sheet growth.² At current return levels, this allows only gradual expansion, limiting BII’s ability to scale investment at pace as demands around climate finance, private capital mobilisation, and engagement in the hardest markets continue to grow.

Figure 3. BII portfolio return (%)



Source: BII Annual Review 2024.

² Except for new injections of shareholder equity, which look unlikely in the future.

What leveraging BII’s balance sheet could achieve

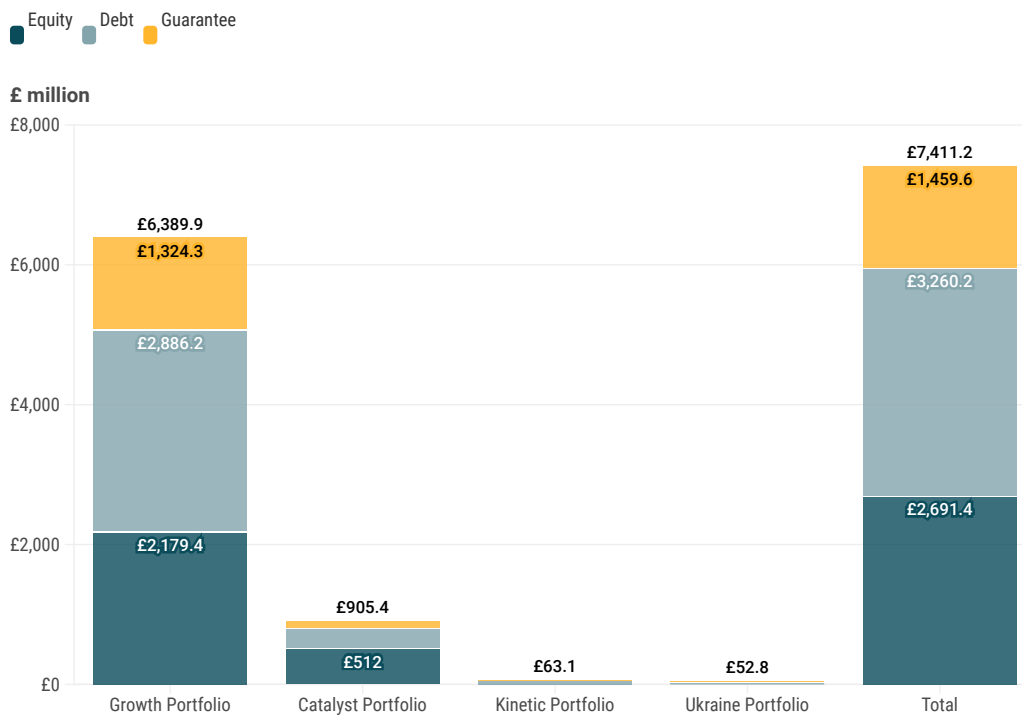
The implication is not that BII should become a “leveraged bank” but that it should adopt a differentiated approach to its capital structure, aligned with typical practices. Much of BII’s shareholder equity³ should be preserved for funding higher-risk, market-creating investments, while most, for example 90 percent, of its lower-risk assets, particularly debt investments in the Growth Portfolio, could be financed more efficiently through borrowing.

Recent UK fiscal reforms strengthen this case. Under PSNFL and PSNW frameworks, borrowing that is matched by financial assets can be assessed on a net basis, rather than treated simply as an increase in public debt. For BII, even modest leverage would materially expand its capacity, though taking on debt would introduce new operational and potential regulatory complexities that would need to be carefully managed.

For example, funding 90 percent of BII’s existing debt investments with new debt funding would imply leverage of around $0.3 \times$ shareholder equity, conservative by any standard, yet equivalent to roughly £3.2 billion in additional cash available to increase investment capacity (Figure 4).

Figure 4. BII portfolio instrument composition

Active direct investment as of December 31, 2025



Source: BII Investment Database, CGD analysis. • Amounts are based on sum invested in USD and translated using Bank of England sterling exchange rate on December 31, 2025. • Analysis excludes investment in funds whereas Figure 1 includes it.

3 Shareholder equity is also required for funding a portion of any type of risk, including expected losses and other operational risks.

Three leverage options

Three broad options merit consideration.

Option 1: Issuing BII bonds

BII could issue bonds directly in capital markets, backed by its balance sheet and shareholder support. These could include use-of-proceeds bonds (such as green or climate bonds) or sustainability-linked bonds tied to corporate-level impact targets. Borrowing could begin modestly and scale over time.

There is sometimes concern that accessing bond markets could make a DFI more risk averse. In practice, much depends on the credit rating being targeted: pursuing the very highest ratings (i.e. “AAA”) typically requires a more conservative capital approach. However, the current MDB reform agenda is prompting a re-examination of what “AAA” capital requirements entail, and this is slowly influencing how a “AAA” credit rating is interpreted and applied in practice. At the same time, other DFIs and vehicles operating with lower investment-grade ratings have demonstrated [that it is possible to sustain high-risk portfolios without undermining financial performance](#).

These bonds could potentially be designed to benefit from [targeted tax relief for UK investors](#), helping to reduce funding costs while encouraging longer-term private investment aligned with sustainable development. Eventually, BII could also issue bonds in domestic capital markets, allowing it to provide debt financing in local currencies.

Pros

- Expands investment capacity without new ODA equity
- Consistent with PSNFL/PSNW treatment
- Improves return on equity and long-term sustainability
- Introduces market discipline and transparency
- Supports local-currency investments and local bond markets
- Introduces the possibility to issue securitizations, resulting in even more increased investment capacity

Cons

- Requires shareholder and Treasury approval
- Introduces fixed repayment obligations
- Risk that taking on debt subtly pushes the portfolio toward safer investments, unless clear safeguards are in place to protect higher-risk, catalytic activity.
- Introduces operational complexity

Option 2: Shareholder debt funding

HM Treasury could raise funds and on-lend to BII, allowing it to benefit from the UK government's funding cost, as is the case for the US Development Finance Corporation.

Pros

- Lower and more predictable cost of funds compared to BII bond issuance
- Faster and administratively simpler than BII bond issuance
- Useful as a transitional step

Cons

- Keeps leverage closely tied to the public balance sheet
- Less market discipline exerted over BII
- Does not build BII's own capital-market presence
- Issuing thematic bonds and local currency bonds may not be possible for the UK government

Option 3: Bank borrowing

BII could raise debt from commercial banks through structured financing,⁴ potentially as a pilot before accessing bond markets.

Pros

- Flexible and quicker to arrange than bond issuance
- Useful for testing leverage at small scale

Cons

- Higher cost and shorter maturities
- Limited scale
- Little catalytic or market-building value
- Introduces operational complexity

Comparing options: trade-offs and sequencing

Taken together, the comparison Table 2 highlights clear trade-offs between scale, cost, speed, and institutional readiness. A phased approach, beginning with more straightforward approaches such as shareholder loans and moving gradually toward market-based issuance as experience, systems, and confidence develop, would allow BII to build familiarity with leverage while retaining flexibility and protecting its catalytic role.

4 Tailored in its maturity, repayment profile, currency, pricing and protections to match underlying assets, risks and cash flows it finances. Distinct from "plain" borrowing.

Table 2. Comparative overview of balance sheet leverage options

DIMENSION	ISSUE OWN BONDS	SHAREHOLDER LOANS	BANK BORROWING
Scale potential	High	Medium	Low-Medium
Cost of funds	Low-Medium	Low	High
Speed	Medium	High	High
Market discipline	High	Low	Low
Build BII market presence	High	Low	Low
Possibility for thematic bonds, local currency bonds, and securitizations	Yes	No	No
Risk shift to safer investments	Medium	Low-Medium	Medium
Operational complexity	High	Low	Medium

Conclusion: Using select leverage to protect and scale

BII’s value lies in doing what others cannot: taking risk, backing platforms, and creating markets in the most challenging contexts. That role must be protected. But with limited prospects for new aid capital and a growing role in climate finance in more commercial markets, BII also needs a capital structure model that supports financial sustainability and scale.

Used well, leverage strengthens, not dilutes, BII’s mission. More profitable commercial lending builds retained earnings, grows capital over time, and creates the headroom to finance riskier, market-creating investments. The challenge facing BII’s shareholder, the FCDO, is not whether to consider leverage, but how to use it deliberately to sustain impact in a more constrained aid environment.

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