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INNOVATIVE FINANCING FOR EDUCATION

KHYBER PAKHTUNKHWA

Mobilising Resources, Supporting Delivery, and Sustaining Learning Outcomes

INNOVATIVE FINANCING FOR EDUCATION

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Abbreviations

AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
ADB	Asian Development Bank
ADP	Annual Development Programme
ALPs	Alternative Learning Pathways
ASER	Annual Status of Education Report
BII	British International Investment
BoK	Bank of Khyber
C&W	Communications and Works Department
CSO	Civil Society Organisation
CSR	Corporate Social Responsibility
DFI	Development Finance Institution
DIB	Development Impact Bond
DLI	Disbursement-Linked Indicator
DSCR	Debt Service Coverage Ratio
E&SE	Elementary and Secondary Education Department
ESEF	Elementary and Secondary Education Foundation
EdTech	Educational Technology
EICGF	Education Infrastructure Credit Guarantee Facility
FCDO	Foreign, Commonwealth and Development Office (UK)
FPA	Foreign Project Assistance
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GoKP	Government of Khyber Pakhtunkhwa
GPE	Global Partnership for Education
IFAD	International Fund for Agricultural Development
I-SAPS	Institute of Social and Policy Sciences
IV	Independent Verifier
KIBOR	Karachi Interbank Offered Rate
KPEF	Khyber Pakhtunkhwa Education Foundation
KP-HCIP	Khyber Pakhtunkhwa Human Capital Investment Project
KPRA	Khyber Pakhtunkhwa Revenue Authority
LFPS	Low-Fee Private Schools
LMIC	Low- and Middle-Income Countries
M&E	Monitoring and Evaluation
MDs	Merged Districts
MFI	Microfinance Institution
MIS	Management Information System
MSME	Micro, Small, and Medium Enterprises
NAVTTC	National Vocational and Technical Training Commission
NBFC	Non-Banking Finance Company
NEC	National Economic Council
NFC	National Finance Commission
NGO	Non-Governmental Organization
NHP	Net Hydel Profit
NPL	Non-Performing Loan
OOSC	Out-of-School Children
P&DD	Planning and Development Department
PD	Probability of Default

PEF	Punjab Education Foundation
PFM	Public Financial Management
PKR	Pakistani Rupee
PMU	Project Management Unit
PPAF	Pakistan Poverty Alleviation Fund
PPP	Public-Private Partnership
PSDP	Public Sector Development Programme
QAED	Quaid-e-Azam Academy for Educational Development
RBF-g	Results-Based Financing + Guarantee hybrid
ROE	Return on Equity
SBP	State Bank of Pakistan
SDG	Sustainable Development Goal
SECP	Securities and Exchange Commission of Pakistan
SED	Elementary & Secondary Education Department
SME	Small and Medium Enterprise
SPV	Special Purpose Vehicle
TA	Technical Assistance
TALEEM	GPE/UNICEF initiative
TDPs	Temporarily Displaced Persons
TEVTA	Technical Education and Vocational Training Authority
TPV	Third-Party Verifier
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
WASH	Water, Sanitation and Hygiene

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Executive Summary

Khyber Pakhtunkhwa faces a critical education financing paradox. The provincial government has increased education spending and declared an education emergency, yet record budget allocations coexist with persistent deficits in access, equity, and learning outcomes. Current expenditure consumes the bulk of the budget, leaving constrained fiscal space for transformative investments. With millions of children enrolled in public schools and a significant proportion of girls out of school, business as usual cannot deliver education targets.

Existing budgets are largely committed and fall short of global recommendations for the scale of investment education needs. This report responds to these fiscal limits by examining how Khyber Pakhtunkhwa can increase the volume of resources available for education. Innovative financing mechanisms offer a pathway to mobilise additional capital in a resource constrained context without imposing further debt burden on the provincial exchequer.

The strategic pivot proposed is from spending to leveraging public funds. The core idea is using a small amount of public money to unlock larger sums of private investment. For example, government can set aside funds as a buffer to absorb potential losses, which gives confidence to commercial banks and private investors to put their money into education projects. This approach can multiply the impact of every public rupee. It mobilises commercial bank lending in the province, corporate social responsibility (CSR) contributions and philanthropic funds, ensuring that new resources flow to the most marginalised learners: girls, children in merged districts and those with disabilities.

The report presents a suite of innovative financing instruments tailored to specific bottlenecks. An EdTech blended finance facility uses public funds as a buffer to mobilise commercial lending for education technology vendors, with repayment linked to verified deployment milestones across schools. A girls' retention development impact bond provides upfront working capital for interventions targeting girls, with government repaying investors only upon independently verified enrolment and learning outcomes. An education infrastructure credit guarantee facility enables contractors executing school rehabilitation packages to access bank financing through escrow backed payment security and third-party technical audits.

Additional instruments address the needs of low fee private schools and civil society partners. A working capital guarantee helps registered low fee private schools access finance through cashflow based underwriting rather than physical collateral. A results-based financing hybrid provides bridge working capital to civil society organisations (CSOs) delivering outcomes for out of school children, with outcome payments assigned directly to the lending bank. The proposed Khyber Pakhtunkhwa School Adoption and Catalyst Fund aggregates CSR contributions through the Elementary & Secondary Education Foundation's existing platform to address infrastructure gaps and girls' retention incentives. A Sharia compliant revenue-based financing facility using diminishing musharakah structure provides working capital to low fee private schools with repayment linked to monthly gross revenues. A debt swap facility refinances the province's highest cost debt, generating fiscal savings over five years to be redirected to education priorities.

The government will need to decide which department or agency takes the lead on coordinating implementation across the proposed instruments. Close collaboration will be required between the departments responsible for education, finance, and planning and development, as well as the education foundation. An inter departmental working group, chaired by a senior official from the lead education department, will need to be established to oversee progress and resolve bottlenecks. External transaction advisory support will also be required to help with feasibility studies, legal structuring and engagement with potential investors.

Risks are addressed through multiple safeguards built into each instrument's design. Political risk is managed by consulting widely across government and, where possible, writing commitments into law so they cannot be easily reversed.

To ensure public money is handled properly and that progress is real, every instrument requires independent checks by third parties. Technology plays a key role: geo tagged photographs verify that construction work has actually been done, attendance systems confirm teachers and students are present, and money is held in secure accounts that release funds only when conditions are met. Auditors are rotated regularly to prevent complacency.

The risk of loans not being repaid is managed by spreading lending across different districts and types of schools, using public funds to absorb the first losses if any, and having a clear rule that stops all new lending if defaults cross an agreed limit.

The risk that government departments may lack the capacity to implement these new approaches is addressed by bringing in expert advisory support and testing each instrument through small pilots first, allowing officials to learn and adjust before expanding.

The report is confined to elementary and secondary school education in Khyber Pakhtunkhwa and is intended primarily for the Elementary and Secondary Education Department and development partners. It also serves the Finance and P&D Departments, and financial institutions in the province as a second audience. By demonstrating how limited public resources can leverage private capital at scale, the report offers a practical roadmap for mobilising the additional resources needed to achieve provincial education targets.

The recommendations that follow are suggestions tailored to Khyber Pakhtunkhwa's context and institutional landscape. Each financing instrument has been reviewed by corporate governance, regulatory and legal experts, who provided detailed advice. Their comprehensive instrument-wise advice has not been included in the current text to avoid being too prescriptive at this stage but will serve as technical support once stakeholders agree to design and pilot specific instruments.

1 Purpose and Scope of the Report

Pakistan's economic recovery is stabilising but remains fragile, constrained by structural bottlenecks and external vulnerabilities.[1] Khyber Pakhtunkhwa provincial government is pursuing fiscal consolidation despite challenges, including post-merger integration of tribal districts, climate-induced disasters, and security-related expenditures.

The Government of Khyber Pakhtunkhwa has unveiled a record surplus budget of approximately PKR 157 billion for FY 2025-26. This fiscal prudence, detailed in the White Paper 2025-26, demonstrates a capacity for sound financial management that now creates the enabling environment necessary for deploying innovative financing instruments in education.[2]

The FY 2025-26 budget reflects strong development ambition. Provincial resources are estimated at PKR 2,119 billion, supported by federal transfers (PKR 1,401 billion), Net Hydel Profits (PKR 106 billion), and provincial own receipts projected at PKR 129 billion. Development expenditure has been set at PKR 547 billion, an increase with major allocations for infrastructure, energy, and human capital.

Education features prominently. The Government has allocated PKR 363 billion to Elementary and Secondary Education for FY 2025-26, an 11% increase over the previous year's development allocation for this sector. Major initiatives include a declaration of a special education emergency with PKR 5 billion dedicated to improving literacy and reducing out-of-school children, PKR 5.9 billion for upgrading infrastructure in 32,500 public schools (including furniture and fixtures), and PKR 7 billion for free textbooks to benefit all students.

Yet beneath this expansion lies a structural disconnect between financing flows and educational outcomes. This is the central paradox this report seeks to address.

a. The Paradox of Education Financing

Khyber Pakhtunkhwa has allocated a record sum to education, demonstrating political will. The most significant portion of the budget is committed to recurring expenditure necessary for system maintenance, including teacher salaries and pensions. While this sustains day to day operations, it

[1] Dawn Report. (2026, February 20). Policy efforts taken by Pakistan under EFF helped ‘stabilise economy, rebuild confidence’: IMF. *Dawn*.
[2] Government of Khyber Pakhtunkhwa. (2026). White Paper 2025-26. Peshawar: Finance Department. Retrieved February 15, 2026, from https://www.finance.gkp.pk/whitepaper2025-26.pdf

leaves constrained fiscal space for the transformative investments in access, equity and learning outcomes to which the province is committed under both SDG 4 and its Education Sector Plan.[3]

The challenge is acute. The province has over 5.9 million students enrolled in more than 32,500 public schools, yet significant deficits remain in quality and infrastructure.[4] The merged districts (MDs), formerly FATA, require sustained investment to bring them at par with settled areas, with a development allocation of PKR 139.6 billion in FY26.

This report argues that while Khyber Pakhtunkhwa has made progress in education spending, however incremental budget increases alone cannot address every systemic challenge. What is required is a complementary shift toward innovative financing instruments.[5] These mechanisms can safeguard development expenditure, ensure funds are spent only where results are achieved, and unlock new pools of concessional and commercial finance. The fiscal and institutional foundations laid through Khyber Pakhtunkhwa's prudent financial management make such instruments viable and timely.

b. Why This Report, and Why Now

This report is commissioned by FCDO's B-TAG in response to a dual imperative. First, the fiscal space for education in KP is inherently rigid, with high recurrent costs. Second, the modality of development finance is shifting. Development partners are increasingly demanding results-based, risk-sharing, and leverage-creating instruments.

The purpose of this report is therefore to provide the Government of Khyber Pakhtunkhwa, its legislators, the private sector, and development partners with an evidence-based assessment of innovative financing instruments that can:

- Mitigate risks for private investment in education infrastructure, low-cost private schools, and education enterprises.
- Shift expenditure beyond inputs to outcomes through instruments such as Development Impact Bonds and outcomes-based PPPs.
- Mobilise non-traditional capital: CSR, commercial bank lending, diaspora funds, without imposing additional debt burden on the provincial exchequer.
- Complement public financing by freeing fiscal space for priority areas: girls' education, early childhood education, teacher development, and climate-resilient school infrastructure, particularly in the merged districts.

This report's assessment is framed within the strategic priorities of international development partners, including the UK government's enduring commitment to advancing girls' education and ensuring that all children acquire foundational learning skills.[6] The analysis is anchored in a principle of equity: the purpose is not merely increasing aggregate investment, but ensuring that new and innovative finance

[3] Elementary & Secondary Education Department, Government of Khyber Pakhtunkhwa. (2020). Education Sector Plan 2020-21 to 2024-25. Peshawar: Government of Khyber Pakhtunkhwa. Retrieved February 15, 2026, from https://kpese.gov.pk/education-sector-plan-2020-21-2024-25/

[4] Pakistan Point. (2025, June 12). KP Govt Increases Education Budget To Rs363 Billion For FY2025-26. *Pakistan Point*. Retrieved February 15, 2026, from https://www.pakistanpoint.com/en/story/1996584/kp-govt-increases-education-budget-to-rs363-billion-for.html; Afridi, B. K. (2026, January 22). Of shattered dreams and KP destruction. *Dawn*. Retrieved February 15, 2026, from https://www.dawn.com/news/1968402/of-shattered-dreams-and-kp-destruction

[5] Dreux Frotté, M. (2025). *Bridging the finance gap in education: Is innovative financing the solution?* UNESCO. https://www.unesco.org/sdg4education2030/en/articles/bridging-finance-gap-education-innovative-financing-solution

[6] Foreign, Commonwealth & Development Office. (2023). *Girls and Out of School Children: Action for Learning (GOAL)* (Programme ID: GB-1-205246). DevTracker.

flows directly and demonstrably to the most marginalised learners, specifically girls, children in the merged districts, and those with disabilities, who the current system is failing.

c. Scope and Delimitation

The report is confined to school education (pre-primary to secondary) in Khyber Pakhtunkhwa province.[7] It does not address higher education, technical and vocational training, or informal education systems except where they intersect with school-age out-of-school children (OOSC) through Alternative Learning Pathways (ALPs). The analysis covers the seven financing arrangements:

1. Blended Finance
2. Development Impact Bonds
3. Credit Guarantees
4. CSR-linked Funds
5. Revenue-Based Financing (RBF)
6. Public Private Partnerships (PPPs)
7. Debt swaps

Our narrative is structured to enable a policymaker to answer, for each instrument: “Is this worth pursuing, under what conditions, and what would it take to implement responsibly?” In weak-capacity environments, education financing instruments should prioritise scalable, government-aligned mechanisms that minimise regulatory, revenue, and transaction complexity while leveraging existing public financial systems.

d. Methodology

This report employs a four-layer diagnostic methodology to translate global and local innovative financing models into actionable policy pathways for Khyber Pakhtunkhwa. Layer one analyses macro-fiscal and expenditure trends to identify financing gaps and fiscal headroom; layer two applies a standardised readiness assessment to seven innovative instruments, drawing on global evidence and provincial diagnostics to generate sequenced roadmaps and risk matrices. Layer three integrates findings from targeted consultations with government, private sector, development partners, and civil society, while layer four synthesises technical inputs from private finance, PPP, and legal experts into coherent, policy-accessible recommendations.

Layer three integrates findings from a roundtable convened in December 2025 and subsequent interviews with 38 senior stakeholders across government, development finance, private sector, and civil society.[8] Participants included the senior representatives from Elementary & Secondary Education Department, Khyber Pakhtunkhwa, Punjab Education Foundation, SIFC, ADB, UNDP, PPAF, PMIC, NAVTTC, PTCL, Bank Al-Habib, Faysal Bank, Bank of Punjab, and HUBCO, alongside technical experts from I-SAPS and FCDO.

These consultations provided critical validation of provincial readiness, clarified investor perceptions of risk, and surfaced regulatory bottlenecks that desk-based analysis alone could not capture. The roundtable discussions, in particular, generated consensus on the sequencing of blended finance

[7] This report has benefited from the input provided by Secretary, Elementary & Secondary Education Department, Government of Khyber Pakhtunkhwa.
[8] Institute of Social and Policy Sciences (I-SAPS). (2026, January). Insights from the policy roundtable on innovative financing of education convened under the GOAL: Bridging Technical Assistance for Governments (B-TAG) programme. https://www.linkedin.com/posts/institute-of-social-and-policy-sciences-i-saps-_education-innovativefinancing-educationfinancing-activity-7410228261839912960-fOqg/

instruments and underscored strong cross-sectoral appetite for a Khyber Pakhtunkhwa Financing Dialogue as a permanent multistakeholder platform. The analysis is caveated by the fragmented nature of private school market data, which has been triangulated from available sources and expert scoping.

For this report, innovative financing refers to mechanisms that transfer risk from the government to investors, leverage non-budgetary capital, and link repayment to outcomes. The primary entity responsible for partnering with low-cost private schools may be the Elementary and Secondary Education Foundation (ESEF)[9] or as per decision by the government.

[9] Elementary & Secondary Education Foundation, Government of Khyber Pakhtunkhwa. (2022). *New School Initiative (NSI)*. Retrieved February 15, 2026, from https://esef.gkp.pk/schemes/nsi

2 Education Financing in Khyber Pakhtunkhwa – Key Patterns

Khyber Pakhtunkhwa's education budget has grown significantly. The FY 2025-26 budget allocation of PKR 363 billion for E&SE marks an 11% increase.[10] When viewed against the total provincial expenditure of PKR 1,962 billion, the education sector commands a substantial share, but the flexibility of utilising these funds is limited.

Provincial revenue is heavily dependent on federal transfers (PKR 1,401 billion), which include tax assignments, a 1% share for the War on Terror, straight transfers on oil and gas, and windfall levies. Own revenue, while growing (projected at PKR 129 billion), remains a small fraction of the total. The province's fiscal institutions are configured for resource receipt rather than resource generation, limiting the headroom for entirely budget-financed expansion.[11]

The current-to-development expenditure ratio is a persistent challenge. The total development expenditure for the province is PKR 547 billion, but this covers all sectors. Within the education sector, the focus remains on system maintenance (salaries, pensions, textbooks) rather than transformation, although the Rs 5.9 billion allocated for school upgrades is a step toward addressing the infrastructure deficit.

Donor engagement remains on a decline, with Foreign Project Assistance (FPA) budgeted at PKR 177 billion for FY26 across all sectors. Future development partner engagement will likely be characterised by a push for explicit risk transfer to private investors and outcome-contingent payments. The experience of the Pakistan Skills Impact Bond (PSIB) in the skills sector provides a domestic precedent for such new modalities.[12]

Priority financing gaps that cannot be closed through incremental budget increases alone include:

- Access: Reducing the number of out-of-school children, targeted by the education emergency.
- Infrastructure: Addressing the accumulated backlog in 32,500 schools, including in merged districts.
- Teacher Development: Enhancing the quality of the teaching workforce.

[10] Government of Khyber Pakhtunkhwa. (2026). White Paper 2025-26. Peshawar: Finance Department. Retrieved February 15, 2026, from https://www.finance.gkp.pk/whitepaper2025-26.pdf
[11] Ahmed, V., Javed, M., Ahmed, B., Usama, A., Masud, Z., & Farooq, H. (2021). *Reform of pensions: Lessons from successful examples in Pakistan and Beyond*. Sustainable Energy and Economic Development (SEED) Programme.
[12] British Asian Trust. (2025, December 31). *Launch of first Pakistan Skills Impact Bond marks historic shift toward outcome-based financing*. https://www.britishasiantrust.org/latest-updates/news-events/launch-of-first-pakistan-skills-impact-bond/

- Girls' Retention: Initiatives like the newly launched Insaf Female Education Card, which aims to provide free higher education to over 55,000 female and orphan students, point to the need for sustainable, outcomes-based funding for girls' education from secondary through higher levels.[13]
- Merged Districts: Ensuring the special development needs of the MDs are met with effective and transparent spending.

Khyber Pakhtunkhwa's institutional landscape for education financing includes:

- Elementary & Secondary Education Department (E&SED): Holds policy and budget authority.[14]
- Khyber Pakhtunkhwa Education Foundation (KPEF): Manages partnerships and scholarship programmes. It is currently launching innovative initiatives like the 'Adopt a Scholar' programme to crowd in philanthropic capital for higher education, demonstrating a readiness for innovative models.[15]
- Planning & Development Department (P&DD): Oversees the ADP, monitors development projects, and houses a Public Private Partnership Unit, making it a critical player for blended finance and infrastructure guarantees.
- Finance Department: Exercises fiscal control and has demonstrated prudence with a surplus budget.

The financial institutions and funding sources present in the education space include:

- **Bank of Khyber (BoK):** Has demonstrated capacity to implement government-backed lending schemes. In March 2025, BoK signed an MoU with TEVTA to implement the Ehsaas Hunar Program, providing interest-free loans up to PKR 500,000 to approximately 35,000 skilled youth across the province under a PKR 3 billion government allocation. This experience positions BoK as a potential anchor partner for education-focused credit guarantee facilities. The scheme's emphasis on youth entrepreneurship and its implementation through BoK's branch network demonstrates the bank's ability to deliver targeted, government-supported lending at scale.
- **Microfinance Institutions:** Akhuwat Foundation operates extensively throughout Khyber Pakhtunkhwa, with branches in Peshawar and other major urban centres. The foundation offers specific Education Loans (PKR 10,000–50,000) for students facing financial hardship, alongside Family Enterprise Loans supporting small businesses. Its Sharia-compliant, interest-free (Qarz-e-Hasna) lending model, built on community-based verification and repayment through mosques, offers a ready implementation partner for revenue-based financing structures targeting low-cost private schools.
- **Commercial Banks:** Banks including those represented in our stakeholder consultations maintain branch networks in the province and can provide senior liquidity for blended facilities. The State Bank of Pakistan's updated SME financing guidelines (November 2025) have enhanced enabling conditions, raising lending limits from PKR 10 million to PKR 50 million and mandating digital onboarding, automated credit scoring, and faster turnaround times for SME loan processing.
- **State Bank of Pakistan:** Prudential regulations continue to evolve to facilitate SME financing, including education enterprises. The November 2025 guidelines require banks to adopt board-approved SME strategies, deploy digital credit-scoring models leveraging alternative data, and maintain dedicated SME finance committees chaired by CEOs. While federal youth schemes

[13] Aaj English TV. (2025, November 11). *KP CM unveils free education initiative for girls, orphans*. https://english.aaj.tv/news/330444196
[14] https://kpese.gov.pk/
[15] https://ef.kp.gov.pk/news_detail/12

such as Kamyab Jawan offer subsidised financing, provincial programmes like Ehsaas Hunar demonstrate the growing ecosystem for targeted lending.

- **Securities and Exchange Commission of Pakistan (SECP) and Pakistan Stock Exchange (PSX):** In September 2025, SECP and PSX jointly launched the Investment Awareness Initiative at the Sarhad Chamber of Commerce and Industry in Peshawar, aimed at promoting financial literacy, encouraging equity investments, and strengthening investor protection across the province. Officials announced the initiative would expand from Peshawar to educational institutions and divisional headquarters, signalling growing capital market engagement with Khyber Pakhtunkhwa.

Private Sector Education Actors

- **Low-Fee Private Schools (LFPS):** A significant market of private schools operates in the urban and peri-urban centres, registered with the Private Schools Regulatory Authority. These schools are the primary targets for working capital guarantees and revenue-based financing.
- **Private School Networks:** Individual chains have demonstrated interest in public-private partnerships. In December 2023, Dar-e-Arqam Schools System and Al-Ghazali Trust pledged to expand their networks into the merged tribal districts, with the provincial government assuring full support for such initiatives.
- **Private Schools Regulatory Authority (PSRA):** Established under the Khyber Pakhtunkhwa Private Schools Regulatory Authority Act 2017, PSRA mandates annual renewal registration for all private schools operating in the province. Its online database and regulatory framework provide a mechanism for identifying eligible borrowers and enforcing minimum standards for schools participating in government schemes.
- **Corporate Sector:** Companies with the provincial footprints in cement, tourism, mining, energy, and banking represent a pool of CSR capital that can be channelled through pooled funds. The Sarhad Chamber of Commerce and Industry provides a platform for private sector engagement, having recently partnered with SECP and Pakistan Stock Exchange (PSX) on the Investment Awareness Initiative.

Khyber Pakhtunkhwa's pursuit of innovative education financing is supported by a diverse ecosystem of development partners and technical assistance providers. The FCDO serves as the current assignment sponsor providing core technical assistance. The Asian Development Bank (ADB) maintains engagement in education and infrastructure financing, with potential for co-financing blended facilities. United Nations agencies including UNICEF, alongside the Pakistan Poverty Alleviation Fund (PPAF), implement education programmes in KP, such as ICT-enabled learning initiatives, demonstrating established government partnership models. Karandaaz Pakistan offers technical expertise in guarantee facility design and SME financing to support instrument structuring. This ecosystem, combined with provincial government institutions, creates an enabling environment for piloting the proposed financing instruments.

ESEF's flagship New School Initiative (NSI) targets out-of-school children aged 4-16 in underserved areas where no government school exists within a 2km radius (plain areas) or 1.5km radius (hilly areas), with partner private schools required to meet minimum infrastructure standards including six rooms, electricity, drinking water, computers, and at least five teachers. [16]

Under NSI, the government pays private schools a monthly fee: PKR 1,000 for nursery, PKR 1,500 for grades 1-5, PKR 2,000 for grades 6-8, PKR 3,500 for grades 9-10, and PKR 4,000 for grades 11-12,

[16] Khan, Z. (2022, April 24). KP education foundation to help private sector set up schools. Dawn. Retrieved February 15, 2026, from https://www.dawn.com/news/1686462

plus an annual PKR 5,000 per student for textbooks, uniform, and shoes, with a planned enrolment of 10,000 children and a budget of PKR 590 million.

For the merged districts (formerly FATA), the Merged Areas Education Foundation[17] operates the Sabawoon Schools Initiative (SSI) and Middle Community Schools programme, providing free education from kindergarten to grade 5 and PKR 2,000 monthly stipends for grades 5-8, with plans to establish 25 new schools through public-private partnerships.[18]

All private schools participating in government schemes must be registered with the Khyber Pakhtunkhwa Private Schools Regulatory Authority (PSRA).[19] In the fiscal year 2025-26 budget, the KP government plans to hand over 1,500 schools to the private sector through public-private partnerships and establish 200 new schools through ESEF, alongside Rs 1.2 billion for smart classrooms and technology integration.[20]

Forward simulations indicate that redirecting a portion of the development budget toward guarantees, outcomes funds, and blended finance vehicles could unlock private capital, multiplying the impact of public spending and accelerating progress.[21] The province's growing private sector, corporate CSR, and diaspora represent untapped funding that needs structures to attract investment.

[17] https://mef.gov.pk/
[18] The Express Tribune. (2024, June 11). *25 community-based schools on cards in merged districts*. Retrieved February 15, 2026, from https://tribune.com.pk/story/2470880/25-community-based-schools-on-cards-in-merged-districts
[19] Associated Press of Pakistan. (2026, January 8). *Minister for making registration of private schools easier*. Retrieved February 15, 2026, from https://www.app.com.pk/domestic/minister-for-making-registration-of-private-schools-easier/
[20] CW Pakistan. (2025, July 8). *KP allocates Rs. 364 billion for smart classrooms, school infrastructure, and access expansion*. Retrieved February 15, 2026, from https://cwpakistan.com/kp-allocates-rs-364-billion-for-smart-classrooms-school-infrastructure-and-access-expansion/
[21] Ansari, A. N. (2025). Impact of Public-Private Partnerships in Education: A Systematic Review of Literature from Pakistan. *NORRAG*.

3 Introduction to Financing Instruments

The financing instruments presented in this report respond to a strategic objective: making public resources go further by attracting private capital alongside them. While Khyber Pakhtunkhwa has increased education spending, the incremental increases in budget alone cannot address every gap. The core proposition therefore shifts from allocation to leverage, using limited public funds as a cushion that gives confidence to private investors, potentially multiplying the impact of every public rupee several times over.[22]

Instrument prioritisation reflects Khyber Pakhtunkhwa's institutional strengths and development priorities (Table 1). Public-Private Partnerships rank as a core instrument given the P&DD's established PPP Unit and the government's active pipeline of education PPPs. Blended Finance is feasible, building on E&SED's experience managing donor-funded projects. Debt swaps offer fiscal space expansion potential, leveraging the Finance Department's demonstrated fiscal prudence. Credit guarantees are rated medium-high, anchored by any commercial bank's capacity implementing government lending schemes. CSR funds are feasible through for example, the ESEF platform, though scale requires aggregating CSR given the province's narrower corporate base. Development Impact Bonds and revenue-based finance are rated medium and low respectively, suitable for piloting but requiring transaction advisory support and rigorous independent verification.

[22] See, Antunes de Carvalho, F.; Lee, C.; Byanjeru, Y.2025. Innovative Financing of Education Technology as Part of Maximizing Financing for Development. Education Working Paper Series; No. 19. World Bank. http://hdl.handle.net/10986/43618

Table 1: Instrument Prioritisation for Khyber Pakhtunkhwa

Instrument	Feasibility in KP	Scale Potential	Recommended Role
PPPs	High	High	Core instrument
Blended Finance	High	High	Core instrument
Debt Swaps	Medium	Low	Fiscal space expansion
Credit Guarantees	Medium-High	High	Market development
CSR Funds	High	Medium	Complementary / Scalable
Development Impact Bonds	Medium	Low	Pilot only
Revenue-based Finance	Medium	Low	Niche

Source: Adapted from World Bank (2017)[23]

[23] World Bank. (2017). *Maximizing finance for development: Leveraging the private sector for growth and sustainable development.* Washington, DC: World Bank; OECD. (2018). *Making blended finance work for the sustainable development goals*. Paris: OECD Publishing.

4 Blended Finance: Supporting First-Time Entrants

Blended finance addresses a specific market weakness creditworthy low-cost private schools and infrastructure contractors in Khyber Pakhtunkhwa are systematically excluded from commercial lending due to collateral constraints. The instrument deploys catalytic public or philanthropic capital as a first-loss tranche[24] to absorb initial default risk, thereby rendering senior commercial lending viable. This shifts the public sector's role from direct spender to strategic risk-bearer, unlocking private liquidity for education investments.

Global evidence confirms that blended finance can mobilise significant commercial leverage. In Nigeria, India, and Pakistan (notably through the Kashf Foundation's education loan programme), such mechanisms have expanded access to finance for low-cost private schools. The Kashf Foundation's experience demonstrates that women-focused microfinance institutions can successfully lend to education entrepreneurs when appropriately structured, achieving high repayment rates while expanding access for girls.

KP's readiness for blended finance piloting is assessed as Medium, requiring targeted technical assistance. The ESEF maintains relationships with partner schools under its New School Initiative and Girls Community Schools programmes, providing a pipeline of potential borrowers. The BoK has demonstrated capacity to implement government-backed lending schemes through its partnership with TEVTA. Several local financial sector consulting firms possess recognised technical expertise in guarantee facility design and small and medium enterprise (SME) financing that can support instrument structuring.[25] However, education-specific lending requires dedicated credit officer training and market mapping, particularly in the merged districts where formal financial penetration remains limited.

A robust value-for-money framework is essential to justify public investment in blended finance. Beyond the fiscal multiplier, it is important to demonstrate cost-effectiveness relative to traditional Annual Development Programme (ADP) expenditure. For the EdTech blended facility, the relevant metric is cost per additional child reached with digital learning tools, compared to the government's direct procurement and distribution model. This requires establishing baseline unit costs from existing E&SE Department technology initiatives and comparing them against projected outcomes from blended facilities, incorporating the efficiency gains from private sector execution, usage-based repayment, and third-party verification.

[24] It is a pool of money set aside specifically to cover the first wave of potential losses. By taking the initial hit, it gives comfort and confidence to other investors that their money is safer, encouraging them to participate.
[25] For example, see: Tahir Andrabi, Natalie Bau, Jishnu Das, Naureen Karachiwalla, Asim Ijaz Khwaja, Crowding in Private Quality: The Equilibrium Effects of Public Spending in Education, *The Quarterly Journal of Economics*, Volume 139, Issue 4, November 2024, Pages 2525–2577, https://doi.org/10.1093/qje/qjae014

Safeguarding and GESI covenants must be non-negotiable conditions for any blended finance facility supporting non-state education providers. Preventing phantom actors and ensuring genuine learning engagement requires linking to the province's Integrated Education Management Information System (IEMIS), which now profiles over 5.4 million enrolled children across 34,800 schools in Khyber Pakhtunkhwa, digitising records of 240,000 education employees. For schools and communities not fully integrated into IEMIS, independent third-party monitoring (TPM) should be mandated. Digital platforms enabling real-time usage analytics provide additional verification layers.

A clearly articulated exit strategy is required to mitigate the risk of distorting markets through permanent public subsidy. The facility design should incorporate a sunset clause or a gradually declining first-loss coverage ratio as the market matures and lenders and vendors develop familiarity with education sector risk. This approach builds on international experience where time-bound blended finance facilities have successfully catalysed sustainable markets without creating permanent dependency.

The way public money is used can become more efficient over time, as these facilities build a track record. As lenders gain experience, vendors demonstrate reliable repayment, and loans are spread across different districts and types of schools, the level of public subsidy required can be reduced while the overall amount of funding unlocked continues to grow.[26] This means the same public investment can eventually attract several times more private capital than in the early stages.

Product 1: EdTech Expansion Blended Facility

The EdTech Adoption Blended Finance Facility is a structured mechanism that uses public first-loss capital to mobilise commercial bank lending for EdTech vendors deploying digital learning solutions in Khyber Pakhtunkhwa. It addresses the market failure where banks perceive EdTech lending as high-risk due to lack of collateral and unproven revenue models, despite strong policy demand evidenced by the government's smart classroom initiative and Virtual School Programme. The facility shifts government from direct procurer to strategic risk-bearer, insulating implementation from fiscal bottlenecks while leveraging private sector execution capacity.

A dedicated guarantee vehicle serves as the central institutional mechanism. It does not lend directly; rather, it sells risk protection to banks by providing partial credit guarantees on loan portfolios to pre-qualified EdTech vendors. This structure allows a small capital base to crowd in multiple times its value in private lending. For Khyber Pakhtunkhwa, the vehicle could be housed within the Finance Department, provided it can issue guarantees qualifying for SBP regulatory capital relief.

The facility brings together three layers of capital from different sources, each taking on a different level of risk. The top layer, making up 75 per cent of the total funds, comes from commercial banks. This layer is the safest, meaning it would only lose money if all else fails, and banks charge an interest rate of around 3 per cent above the benchmark rate. The middle layer is provided by a guarantee fund, which covers bank losses after the first layer of protection is used up. It charges a fee of 1.5 per cent for taking on this risk. The bottom layer, sized at 20 per cent of the total, is funded by the Government and if possible, matching development partners. This layer takes the very first losses if anything goes wrong, acting as a buffer to protect the other layers. Because it carries the highest risk, this money is provided as grant or subsidy and does not earn any return.

The public money set aside to absorb first losses is kept in a secure, separate account so it is safe and can only be used for its intended purpose. Banks keep a small share of the risk on each loan, typically

[26] Hornberger, K., & Paya, M. (2024). *Blending Billions: Lessons from more than three dozen big blended finance transactions*. Dalberg / Convergence Analysis. Published in ImpactAlpha, 3 April 2024.

around 5 per cent[27], which gives them good reason to lend carefully and keep a close eye on how the loans are performing throughout the life of the facility.

The order in which losses are paid is fixed and agreed in advance, so everyone knows what to expect. For example, in a PKR 100 million portfolio, the first PKR 20 million in losses could be paid for entirely by the government and development partners' buffer fund.[28] The next PKR 30 million in losses may be shared: the guarantee fund could cover 60 per cent (PKR 18 million) and banks cover the remaining 40 per cent (PKR 12 million), in addition to their share of any losses on individual loans. If total losses cross PKR 50 million, the entire facility stops and no further lending takes place. Several safeguards prevent reckless lending: guarantees never cover more than 60 per cent of any loss, banks must bear some losses themselves, lending stops if defaults get too high, payments to companies are released only after independent verification, and all loans follow standard banking rules.

Bank participation is driven by regulatory advantages under SBP rules, which make guaranteed lending significantly more attractive. This is achieved through three key regulatory benefits. First, capital relief: the guaranteed portion of a loan carries a lower risk weight of approximately 20% compared to the standard SME risk weight of 75-100%, which reduces risk-weighted assets and improves banks' return on equity. Second, provisioning shielding: the guarantee value is deducted from provisioning requirements, meaning that on a PKR 10 million bad loan with a PKR 6 million guarantee, the bank provisions only PKR 4 million instead of the full amount. Third, the clean lending limit: SBP has increased the SME clean (unsecured) lending limit to PKR 10 million, enabling lending against cashflows and guarantee coverage rather than requiring physical collateral.

This facility works like a financial multiplier. By using a small amount of government money as a safety cushion to cover the very first losses, it gives private banks the confidence to lend a much larger amount of their own money. As the programme grows and the banks get better at picking successful businesses, the government's safety cushion doesn't need to be as thick. This allows the same amount of public money to unlock even more private lending over time.

Product Terms: The facility targets EdTech vendors with proven track records, using milestone-based verification to trigger repayments. Table 2 summarises the key terms for pilot implementation.

Table 2: EdTech Facility – Pilot Terms at a Glance

Feature	Pilot Design
Who can borrow	Companies already supplying technology to government schools
How loans are repaid	Through payments from government contracts or school fees
Who bears the risk if things go wrong	Government and donors cover first 20-25% of losses; a guarantee fund covers 60% of further losses; banks carry the remaining 5-10%
How progress is checked	Payments released in stages: 40% on delivery of technology, 30% when schools start using it, 20% after three months of use, 10% after six months of use. All stages verified through government data systems and independent checks
What success looks like	Active student users, course completion rates, evidence of learning improvement
Where it starts	Peshawar (city), Swabi (rural settled areas), Bajaur (merged districts)

[27] Nolan, A.R.G., Mahoney, S.P., & Malakoff, D.A. (2013, November 15). *Regulatory Agencies Re-Propose Risk-Retention Rules for Securitisations*. Harvard Law School Forum on Corporate Governance.
[28] This is a hypothetical scenario for illustration, not a projection of expected defaults.

Implementation Roadmap: The facility can be implemented in five phases over approximately 14 months, with clear responsibilities assigned for each stage. Phase one, covering the first three months, involves securing necessary approvals, establishing an inter departmental working group, conducting market scoping, and finalising the legal structure for the guarantee vehicle. Phase two, months four to six, covers establishment of the first loss fund, approval of the credit policy, selection of pilot districts, and pre qualification of vendors. Phase three, months seven to nine, includes executing agreements with participating financial institutions and the education foundation, disbursing initial funds, integrating data systems for verification, and contracting third party monitors. Phase four, months ten to twelve, involves quarterly reviews, monitoring of guarantee utilisation, and commissioning an independent evaluation. Phase five, months twelve to fourteen, concludes with relevant departments presenting findings to government for a decision on whether to scale up, adjust, or sunset the facility.

The pilot's success will be measured against clear targets across financial and operational dimensions. Financially, the pilot will test whether a defined amount of first-loss capital can mobilise a significantly larger total portfolio, demonstrating whether public funds can effectively attract private capital alongside them. Guarantee utilisation and repayment rates will be tracked against prudent benchmarks to assess financial viability. Operationally, the facility aims to reach a meaningful number of schools and students across the three pilot districts. The entire pilot is designed for completion within a defined timeframe, providing timely evidence for the scale-up decision.

Once the above mentioned arrangements are in place, an EdTech vendor in Khyber Pakhtunkhwa receives collateral-free working capital disbursed against implementation progress (Table 3), repays as revenue is generated, and builds a bankable track record, all while accessing new markets with government-backed school partnerships.

Table 3: EdTech Vendor Benefits

Step	What the Vendor Does	What the Vendor Gains
1. Pre-qualification	Submits application demonstrating 3+ years' experience, e.g., 10+ schools or 1000+ learners reached, and digital platform capability	Access to collateral-free financing and approved vendor status
2. Proposal submission	Works with for example, ESEF to identify target schools and develops deployment plan with financing request	Government-endorsed school partnerships that reduce revenue risk
3. Bank underwriting	Commercial bank assesses proposal based on track record and projected cashflows, not physical collateral	Commercial loan approval despite lacking assets, backed by guarantee structure
4. Agreement signing	Signs three agreements: loan (with bank), guarantee (bank + guarantee vehicle), and service (with ESEF)	Legal clarity, government backing, and defined verification protocols
5. Milestone disbursement	Receives loan in four tranches tied to verified deployment milestones	Working capital aligned with actual implementation progress
6. Deployment and revenue	Implements solution and generates revenue through government contracts or school subscriptions	New markets with predictable revenue streams
7. Milestone repayment	Repays loan in matching tranches as each milestone is verified	Debt service aligned with revenue generation; no debt on undeployed capital
8. Performance pricing	Qualifies for 0.5% interest reduction if achieving e.g., 40%+ girls' active users	Lower financing costs for reaching marginalised learners
9. Track record building	Successfully completes repayment, building credit history in education sector	Pathway to larger, unguaranteed financing in future

5 Development Impact Bonds

A DIB is an outcomes-based financing mechanism in which private investors provide upfront working capital and an outcome funder repays principal plus a risk-adjusted return only upon independent verification of pre-agreed performance targets, thereby transferring performance risk entirely from the public purse. Pakistan launched its first-ever Pakistan Skills Impact Bond (PSIB), a PKR 1 billion pilot tranche designed to shift vocational training from traditional public spending to a *pay-for-success* private-capital model. Backed by a sovereign guarantee from the Ministry of Finance, the three-year instrument links investor repayments to independently verified outcomes such as certification, job placement, and a six-month employment retention for youth.[29]

PSIB provides a domestic precedent. Backed by a sovereign guarantee, it links investor repayments to verified job placements. The local commercial banks' participation in similar government-backed schemes suggests potential appetite for such instruments.

The Educate Girls DIB in rural Rajasthan provides the strongest operational precedent for Khyber Pakhtunkhwa. Over 2015–2018, it achieved 116 percent of enrolment and 160 percent of learning targets, with participants gaining learning equivalent to one additional year of schooling. Its success reflected strong community mobilisation, outcome metrics integrating access and learning, service provider flexibility, and government alignment.[30] Building on this model, the SDG Outcomes Fund, anchored by British International Investment, demonstrates that outcome-based financing can operate at sub-national level in lower-middle-income countries and that portfolio approaches improve scalability and reduce transaction costs.[31]

For KP, a DIB could target Girls' Retention. Chief Minister in 2025 has launched the Insaf Female Education Card to support female and orphan students, demonstrating strong political will for girls' education. A DIB could build on this by tying repayment to verified retention and learning gains for girls transitioning from secondary to higher education.

KP's readiness for a Girls' Retention DIB is assessed as Medium. ESEF possesses experience in scholarship management. An interested commercial bank could act as an investor. Education sector

[29] Govt launches first bond for skill development, Dawn, 31 December 2025.
[30] IDinsight. (2019). *Educate Girls Development Impact Bond: Final evaluation report*. New Delhi.
[31] British International Investment. (2023). *SDG Outcomes Fund*. https://www.bii.co.uk

think tanks could serve as an independent verifier. Key requirements would be a provincial outcome fund commitment and dedicated transaction advisory capacity.

A sequenced roadmap would involve: E&SED policy direction to ESEF, authorisation of an outcomes-based pilot, feasibility study in selected districts (potentially in merged districts or south), and launch with commercial bank as anchor investor.

Product 2: Girls' Retention Development Impact Bond

A DIB employs a four-party structure that separates roles and creates clear accountability. The investor provides upfront working capital and bears performance risk. The service provider implements interventions to achieve agreed outcomes. The outcome payer, in this case, the Government via a ring-fenced Outcome Fund, potentially matched by donors, commits multi-year funds and repays investors only upon verified results. The independent verifier validates whether outcomes have been achieved. The investor could be a commercial bank and development finance institutions. The service provider may be an ESEF-led consortium with relevant CSO partners. The independent verifier could be a third-party monitor with demonstrated education assessment capacity.

The Girls' Education Oversight Committee, established by the KP Commission on the Status of Women, would provide strategic oversight. This committee includes MPAs, education department representatives, civil society actors, and Malala Fund education champions, with the explicit mandate to review enrolment and retention trends, monitor policy commitments and budgetary allocations, and strengthen coordination among stakeholders. Aligning the DIB's governance with this existing structure ensures coherence with broader provincial girls' education strategy and avoids creating parallel oversight mechanisms.

The DIB would target girls in districts with the highest gender disparity in retention, prioritising merged districts and southern districts where dropout rates spike due to poverty, distance to schools, lack of female teachers, inadequate sanitation facilities, and social norms. Interventions would include targeted cash or in-kind stipends linked to attendance (building on the Insaf Female Education Card model), provision of female teachers or teaching assistants, girls' friendly spaces and safe transport where distance is prohibitive, WASH infrastructure improvements (sanitation facilities being a critical driver of dropout at puberty), community mobilisation to address social norms, and remedial learning support.

The outcome structure would link investor repayment to verified targets across enrolment, retention, and learning. For a pilot targeting, for example, 20,000 girls over three years, enrolment of 5,000 out-of-school girls would be verified through IEMIS and community validation, with repayment of PKR 5,000 per girl. Year one retention of 80% of the cohort would be verified through IEMIS attendance data and third-party sample checks, with repayment of PKR 8,000 per girl retained. Year two retention of 70% would attract PKR 10,000 per girl. Learning gains, with 60% of retained girls achieving grade-level literacy and numeracy, would be verified through third-party assessments with repayment of PKR 4,000 per girl. Transition to secondary for 8,000 girls would be verified through IEMIS with repayment of PKR 6,000 per girl.

Risk is transferred through this outcome-linked structure. Performance risk in this structure is primarily borne by the service provider, who will self-finance operations or leverage their own balance sheet to achieve results. The Investors provide the necessary Outcome Fund upfront, ensuring that capital is ring-fenced and immediately available for disbursement upon success. This creates a powerful incentive for the service provider to maintain high efficiency, as they only recover their operational costs and margins through milestone-based payments verified by an independent party. The government’s liability remains strictly capped at the agreed outcome price, while the presence of the Investor-backed fund mitigates payment risk for the service provider, encouraging them to take on the performance risk inherent in girls' retention targets.

A DIB achieves fiscal efficiency by ensuring government funds are spent only on verified results, not on activities that may or may not deliver impact. An outcome fund commitment, representing a capped liability, could mobilise additional private investor capital for upfront implementation, with investors targeting return tiered to outcome achievement. The key efficiency is that the government pays only for what works, transfers implementation risk entirely to investors, and gains access to multi-year funding flexibility that annual budgets cannot provide.

The DIB directly supports multiple government commitments. The Insaf Female Education Card provides free higher education to female students; a DIB focused on retention and transition from primary to secondary creates the pipeline for this initiative. The FY 2025-26 budget includes allocations for the Education Emergency School Support Programme to reduce out-of-school children, girls' community schools, and free textbooks. The DIB complements these investments by providing a results-focused mechanism to ensure enrolled girls stay in school and learn.

The DIB may be implemented in five phases over 24 months. Phase one, Feasibility and Design over first six months, would see the E&SE Department with transaction advisory support conduct a feasibility study assessing target districts, outcome metrics, cost per outcome, and investor appetite; align design with the Girls Education Oversight Committee; develop detailed outcome metric frameworks and verification protocols; and secure Finance Department commitment for a multi-year outcome fund.

Phase two, Stakeholder Alignment over months four to eight, would involve presenting the design to the Girls Education Oversight Committee for endorsement, conducting an investor roadshow with the commercial bank, finalising service provider selection through a competitive process for an ESEF-led consortium, and drafting all legal agreements.

Phase three, Launch and Capitalisation over months seven to nine, would see the Secretary of E&SE and the Secretary of Finance execute the outcome fund agreement with the Finance Department as a ring-fenced multi-year commitment, execute the investor agreement with an anchor investor, execute the service provider contract, and appoint the independent verifier.

Phase four, Implementation and Verification over years one to three, would involve the service provider implementing interventions in pilot districts, the independent verifier conducting baseline, midline, and endline assessments, quarterly review meetings with all parties, and annual outcome verification with investor repayment tranches.

Phase five, Evaluation and Scale Decision at month 24, would commission an independent evaluation of DIB performance, value for money, and lessons learned, with findings presented to Cabinet for recommendations on scale-up, replication, or integration into core budget. Pilot districts would be selected from those with highest gender disparity: Kohistan, Upper Kohistan, Bajaur, and one southern district. The problem is most critical in Kolai-Palas Kohistan with large number of out-of-school children, with neighbouring Lower and Upper Kohistan showing equally high extent of children out of school.

A service provider consortium benefits through a clear process. In proposal development, it submits technical proposals detailing interventions, target districts, and budget, gaining access to multi-year funding with performance-based incentives. In contract signing, it executes service provider agreements with clear outcome targets and verification protocols, securing predictable revenue streams tied to achievement rather than inputs. Through milestone-based funding, it receives quarterly payments against verified progress, ensuring working capital aligns with implementation needs. Implementation with flexibility allows adaptation based on real-time data and community feedback, with multi-year funding enabling course correction. Performance bonuses provide additional resources for expansion if outcomes exceed targets. Independent verification through third-party assessment strengthens reputation through credible external validation. Track record building from successfully delivering verified outcomes for over 15,000 girls positions the consortium for future outcomes-based contracts.

An investor benefits through a parallel process. During due diligence, it assesses DIB structure, service provider capability, and government commitment, gaining confidence that investment is backed by rigorous design. Through investment commitment, it provides upfront working capital, achieving portfolio diversification and alignment with ESG mandates. Risk bearing means capital is at risk if outcomes are not achieved, compensated by target returns. Performance monitoring through quarterly reports on outcome achievement ensures transparency on capital performance. Outcome verification by an independent third party assures that repayments are triggered by genuine results. Repayment with returns delivers principal plus tiered returns based on outcome achievement, providing financial return alongside measurable social impact. Track record building from successful exit with verified social and financial returns positions the institution for future impact investing opportunities.

Once the above arrangements are fully in place, the Girls' Retention DIB creates a win-win structure. The government pays only for verified results. Investors earn returns for bearing risk. Service providers gain multi-year funding with flexibility to adapt and innovate. And girls in Khyber Pakhtunkhwa's most disadvantaged districts stay in school and learn.

6 Credit Guarantees: Unlocking Bank Lending to Private Schools

A credit guarantee company or a dedicated guarantee facility serves as the central institutional vehicle. This leverages a relatively small capital base to crowd in multiple times its balance sheet in private lending.

A three layer structure fits with how the province already works and what different institutions can handle. The safest layer could come from a commercial bank as the main partner (Table 4). The middle layer would need a dedicated guarantee fund, which could sit within the Planning and Development Department's PPP unit or be set up as a separate body under the Finance Department. This fund would charge a fee of 1 to 2 per cent to cover its running costs and build reserves. The riskiest layer, which takes the first losses, would be funded by the Government of Khyber Pakhtunkhwa through Finance Department budget allocations, with potential matching funds from development partners. This layered approach protects the provincial budget while allowing the authorities to get more impact from its development spending on school infrastructure and quality programmes.

Table 4: How the Money is Stacked – Who Provides It, Who Takes the Risk

Layer	Source of Money	Who Takes the Loss First	What it Does	What it Earns
Top Layer	Commercial banks and development finance institutions	Last – protected by layers below	Provides 80 to 90 per cent of the total funds. Safest position because other layers absorb any losses first.	Commercial interest rate (KIBOR plus a markup)
Middle Layer	Guarantee fund	Second – after the first layer is exhausted	Covers bank losses once the first layer of protection runs out.	Guarantee fee of 1 to 2 per cent (like an insurance premium)
Bottom Layer	Government of Khyber Pakhtunkhwa and donors	First – takes the very first losses	Absorbs initial losses. Acts as a buffer to protect the other layers. Highest risk position.	Nothing – it is grant money

The fiscal multiplier scenarios demonstrate how limited public resources can catalyse significant private capital for education in the province. A pilot using public funds as a buffer could attract several times that amount in commercial lending, enough to finance a substantial portion of the province's school rehabilitation and infrastructure pipeline. As the guarantee vehicle matures and builds a track record, with lending spread across different projects and improved assessment of borrowers, the same public investment could eventually attract even more private capital. This would require close coordination between the departments responsible for finance, planning and development, and commercial banks. Achieving this level of leverage would position the province to address its education infrastructure needs at scale while maintaining fiscal discipline.

Across all products, the facility design follows a set of portfolio-level principles: partial coverage, banking sectors explicit involvement, third-party verification, standardised claims rulebooks, and safeguarding covenants.

The product suite directly addresses specific financing gaps in Khyber Pakhtunkhwa's education sector while building on existing institutional strengths (Table 5). Each instrument targets a distinct bottleneck and leverages capabilities already present in provincial institutions.

The Education Infrastructure Credit Guarantee Facility (EICGF) targets contractors executing school rehabilitation packages under the E&SE Department's development programme. It uses escrow-backed payment security and third-party technical audits to reduce risk, a critical safeguard given recent inquiries into donor-funded projects. This facility aligns with the government's school upgrading priorities and can be piloted through the P&DD's existing PPP pipeline.

The LFPS Guarantee addresses working capital constraints for low-fees private schools registered with the Private Schools Regulatory Authority. It uses cashflow-based underwriting that builds on BoK's experience with interest-free lending to youth entrepreneurs. By substituting public risk capital for private collateral, this guarantee makes private schools bankable for the first time, unlocking financing for infrastructure improvements and quality upgrades.

The Results-Based Financing hybrid (RBF-g) would support CSOs and PPP partners delivering outcomes for out-of-school children. It requires independent verification drawing on the E&SE Department's monitoring capabilities, ensuring that public funds flow only where results are genuinely achieved.

Table 5: Summary of the Product Suite

Product	Who it Helps	How it Works	What Prevents Problems	Feasibility in KP
Education Infrastructure Credit Guarantee	Contractors building or repairing schools	Payments go through secure accounts that release funds only when work is verified	Independent technical checks on construction quality	High. Matches government plans for solarisation and school upgrades
Low Fee Private School Guarantee	Registered low fees private schools needing working capital	Uses business earnings history instead of land or buildings as security for loans	Banks share some of the risk themselves, so they lend carefully	Medium to High. Needs mapping of eligible schools first
Results Based Financing Guarantee	CSOs and partners working to bring out of school children into education	Guarantees future government payments so banks can lend against them now	Results checked by independent monitors before payments released	Medium. Requires strong verification systems, learning from health programmes
EdTech Facility	Companies supplying technology to government schools	Government and donor funds absorb early losses, giving banks confidence to lend	Tracks whether technology is actually used in schools before releasing payments	Medium. Good potential for remote learning in merged districts

KP's readiness for a credit guarantee scheme is assessed as Medium-High.

- **Legal Feasibility**: High. Guarantee mechanisms can be structured through existing frameworks, potentially leveraging the KP Companies Profits (Workers' Participation) Act or similar for CSR aggregation.
- **Institutional Capacity**: Medium. ESEF has operational experience, but education-specific lending requires credit officer training. The P&DD's PPP Unit could provide structuring support.
- **Market Appetite**: Medium-High. The success of programmes like Akhuwat's interest-free lending for skills demonstrates demand for structured finance among borrowers. Banks like BoK and microfinance institutions (Akhuwat) have shown appetite for government-supported schemes.

Product 3: Results-Based Financing + Guarantee Hybrid (RBF-g)

This product enables outcomes-based programmes to scale by solving the liquidity constraint for service providers (CSOs/PPP operators) who must pre-finance delivery.

- **Structure**: A commercial bank provides bridge working capital to the service provider, guaranteed by the Guarantee Vehicle. Outcome payments from the government/donor are assigned directly to the bank to repay the loan.
- **KP Fit**: High for programmes targeting OOSC in merged districts. The recent experiences underscores the critical dependency on the integrity and capacity of the Independent Verifier, making rigorous third-party verification non-negotiable.

For the financier, this product offers a secure entry point into outcomes-based financing with reduced repayment risk. The bank provides bridge working capital to CSOs or PPP partners delivering education outcomes, with the guarantee vehicle covering a significant portion of potential losses. The outcome payments from the government or donors are assigned directly to the bank, creating a dedicated repayment stream that bypasses the service provider's balance sheet. This structure means the bank's repayment is tied to verified outcomes but protected by both the guarantee and the direct assignment of government payments, making what would otherwise be unbankable pre-financing an attractive, secured lending opportunity.

Product 4: Education Infrastructure Credit Guarantee Facility (EICGF)

The policy objective is to accelerate public-school rehabilitation (WASH, solarisation, classrooms) in Khyber Pakhtunkhwa.

- **Target borrowers**: Pre-qualified contractors executing approved rehabilitation packages under the E&SED.
- **Operational mechanics**: A participating bank provides project execution finance to a contractor. Contract payments are routed through an escrow account. The Guarantee Vehicle provides a portfolio guarantee. Disbursements are tied to verified milestones (e.g., via geo-tagged photos, technical audits) to prevent fraud.

For the financier, this product transforms contractor financing for public school rehabilitation into a low-risk lending proposition. The bank provides project execution finance to pre-qualified contractors, but with multiple layers of protection. Contract payments are routed through an escrow account, ensuring that funds are available for repayment. The guarantee vehicle provides portfolio-level loss coverage. Disbursements are tied to verified milestones using geo-tagged photos and technical audits, preventing the fraud and cost overruns that typically plague contractor lending. For the bank, this means lending against government-backed contracts with escrowed payments, verified progress, and a guarantee backstop, reducing risk whilst enabling participation in the government's school rehabilitation pipeline.

Product 5: Working Capital + Quality Upgrade Guarantee

The goal is to help registered low fee private schools (LFPS) in Khyber Pakhtunkhwa get bank loans for daily expenses and small infrastructure upgrades. Banks assess the school's ability to repay based on fee records rather than requiring land or buildings as collateral, lending within the State Bank of Pakistan's clean limit of PKR 10 million. A guarantee fund covers a portion of losses after banks have absorbed some risk themselves, and access to loans is linked to promises on education quality and child safeguarding. Feasibility in the province is Medium, as Khyber Pakhtunkhwa first needs to map where low fee private schools are concentrated in urban centres and build partnerships with the ESEF.

For the financier, this product opens a new market segment, low-cost private schools, that was previously inaccessible due to collateral constraints. The bank lends to registered private school operators using standardised underwriting based on fee ledgers rather than physical collateral, staying within SBP's clean lending limit. The guarantee vehicle covers a capped second-loss layer, meaning the bank retains first-loss exposure to ensure prudent underwriting but is protected from catastrophic portfolio losses. For the bank, this creates a scalable portfolio of small-ticket education loans with guarantee-backed risk mitigation, access to a growing market of registered schools, and the ability to build long-term relationships with school operators who may become valuable future customers for other banking products.

7 CSR-Linked Funds: Towards Strategic Pooling

A CSR-linked fund aggregates corporate contributions for deployment through a professionally governed, outcomes-oriented framework. Pakistan's corporate sector contributes significantly to social investment, and Khyber Pakhtunkhwa possesses an existing institutional platform ready to channel these resources into school education. ESEF already operates school-level programmes, Girls Community Schools (GCS), Education Support Scheme (ESS), and New School Initiative (NSI) that partner with private providers to enroll out-of-school children in underserved areas.

ESEF uses per-student subsidy models governed by PPP framework and also operates in merged districts. Khyber Pakhtunkhwa has a ready-made vehicle for CSR mobilisation: the ‘adopt a school’ programme, which created a dedicated web portal showcasing schools' missing facilities (classrooms, boundary walls, washrooms, drinking water, computer labs) and enabled donors to fund specific interventions through parent-teacher councils, with completed work documented through photographs shared with adopters. This mechanism was piloted and can be revived and digitised further. The ESEF's recent partnerships, including an MoUs with donors for inclusive non-formal education, and UK FCDO supported collaboration with PPAF and TeleTaleem for ICT-enabled learning in Chitral and Lower Dir[32] demonstrate its capacity to manage multi-donor, results-oriented interventions.

Institutional Response for KP: ESEF's existing ‘adopt a school’ framework can be scaled and evolved into a broader Khyber Pakhtunkhwa School Adoption and Catalyst Fund (KP-SACF). With independent multi-stakeholder governance, this fund could pool CSR contributions from multinationals, banks (like BoK, which already supports government initiatives), and local industries (cement, tourism, mining, energy sectors), targeting not just missing facilities but also girls' retention incentives, teacher development stipends, and technology integration. KP has smaller corporate base, therefore, KP’s CSR financing mechanism must also aggregate CSR nationally (not just KP-based companies), leverage extractive sector, telecom, and banking CSR.

Readiness and Feasibility: KP shows high readiness for a CSR-linked pooled fund anchored at ESEF. Legal feasibility is high under ESEF's existing law, which explicitly mandates private sector engagement. Institutional capacity is medium-high, building on ESEF's existing programmes and infrastructure, and recent strategic planning for 2025-30 that prioritises out-of-school children targets. Market appetite is medium-high, evidenced by past willingness of donors to engage through the 2014

[32] CW Pakistan. (2018, November 21). *Boosting education through ICT in Chitral: PPAF partners with ESEF*. Retrieved February 15, 2026, from https://cwpakistan.com/ppaf-ict-education-chitral/; Online education programme launched in 14 KP districts; Sultan, K. (2026, February 10). *Khyber Pakhtunkhwa launches Virtual School program with TeleTaleem* [LinkedIn post]. Retrieved February 15, 2026, from https://www.linkedin.com/posts/khurrams_esef-schools-teletaleem-activity-7382399597417074688-VWrQ

programme and ESEF's ongoing coordination with multiple development partners including JICA, UNICEF, and PPAF.

Sequenced Roadmap:

- **Phase 1 (Year 1):** Formalise a dedicated school adoption and catalyst fund as a distinct window within the education foundation. Establish governance structures with representation from government, private sector and civil society. Secure anchor contributors from the province's corporate sector, including banks, cement companies and power companies, by reviving and digitising the existing adopt a school framework.
- **Phase 2 (Years 1-3):** Launch and deploy funds across priority areas targeting missing facilities such as classrooms, boundary walls, washrooms, drinking water and computer labs, as well as girls' retention incentives, teacher development stipends and technology integration. Onboard additional contributors and publish impact reports with photographic documentation of completed interventions.
- **Phase 3 (Years 3-5):** Explore transition to results-based grant making and work with relevant government departments to examine potential fiscal incentives for corporate social responsibility contributions.

Risk Mitigation: Institutional risk is addressed through an independent governance board. Fiduciary risk is mitigated by the education foundation's existing transparent systems, including its established partnership frameworks with various development partners and its legal mandate to ensure transparency in financial, procurement and partnership management.

Systemic Impact: This proposed fund is not a new initiative; it would be a strategic evolution of the existing adopt a school framework and its mandate to engage the private sector for education development, potentially mobilising significant annual resources for school education without creating additional fiscal liability for government.

Product 6: Financing Instrument for Blended CSR

This section outlines the Blended CSR model featuring donor co-financing, emphasising equitable and conflict-sensitive delivery. The approach is specifically tailored for high-poverty, fragile, and merged districts. Donor co-financing, permissions to local CSOs, and blending will be essential in Khyber Pakhtunkhwa to attract national CSR funds and reduce provincial risk exposure.

Three distinct channels may be developed to channel funds toward provincial education priorities including reducing out of school children, addressing infrastructure deficits, teacher development, girls' retention in schools, and meeting the special development needs of merged districts through effective and transparent spending. The first channel focuses on girls' secondary expansion to reduce dropout rates, providing a per girl top up subsidy through the ESEF supplemented by a 25 per cent corporate social responsibility top up for girls in secondary grades, along with transport stipends and female teacher incentives. The second channel addresses merged districts access through district based CSR sponsorship for new school openings and infrastructure upgrades, where private enterprise adopt one or more underserved districts and fund incremental public private partnership seats, structured as a pooled mechanism rather than direct school level branding. The third channel supports quality improvement and addressing infrastructure gaps by funding teacher training, free textbooks, procurement and adoption of digital learning tools, STEM labs, solarisation, flood resistant retrofits and safe school infrastructure, with all spending tracked through the education management information system and verified by independent monitors.

Performance-Based Payments: Disbursements tied to enrollment and attendance, girls retention rates, learning assessment benchmarks, infrastructure completion verification and independent verification prior to CSR top-up release.

Readiness and Feasibility: KP shows high readiness for a CSR-linked pooled fund anchored at ESEF. It builds on existing ESEF PPP mechanism and targets hardest-to-reach populations through non-debt financing that will be politically well-accepted. This product leverages CSR beyond provincial corporate base and blends CSR with donor financing focused on equity and fragility-sensitive design which will need significant governance and oversight.

A governance framework may be developed to establish a governing body within the education department, with representation from the education foundation, relevant finance departments, private sector contributors, an independent education expert, and a development partner as observer. A technical secretariat will also be established within the education foundation to handle contracting and payment management, performance verification, and maintenance of a CSR reporting dashboard.

Risk Mitigation: Safeguards and risk mitigation would also include ring-fenced account, annual third-party audit, public transparency portal and district allocation formula prioritising merged districts.

Implementation Roadmap over the first year includes mapping corporate social responsibility potential from companies operating in the province, completing necessary legal structuring within the education foundation, designing a girls' secondary top-up model, piloting in selected merged districts, and launching a transparency portal. Over the following two years, the focus shifts to expanding district coverage, integrating catalytic donor financing, institutionalising an annual education forum for private sector engagement, and developing blended finance instruments.

For corporate contributors, the Khyber Pakhtunkhwa School Adoption and Catalyst Fund offers a credible, transparent channel that transforms ad hoc charity into measurable social investment with tangible business returns. Companies gain access to a professionally governed platform with ring-fenced accounts, annual audits, and photographic proof of completed interventions, meeting rigorous ESG reporting requirements without the administrative burden of managing projects directly. The pooled structure delivers efficiency gains, stretching each corporate rupee further through blended donor co-financing. For companies with a KP footprint, the fund offers reputational visibility linked to tangible outcomes in the communities where they operate, while governance board seats position them as strategic development partners rather than mere donors, building relationships with provincial institutions that yield broader business benefits over time.

8 Revenue-Based Financing: A Quasi-Equity Approach to School Expansion

Revenue-based financing (RBF) offers a fundamental departure from conventional term lending by linking repayment obligations directly to a school's actual revenue streams, making it intrinsically more resilient for institutions with seasonal fee collections and variable enrolment patterns. For Khyber Pakhtunkhwa's low-cost private schools, where monthly fee income fluctuates with household agricultural cycles, local economic conditions, and term schedules, this flexibility is essential. Diminishing Musharakah, a Sharia-compliant partnership structure, provides the ideal Islamic architecture for this instrument. Under this model, the financier and school proprietor jointly own specified assets (such as school buildings or equipment), with the proprietor progressively purchasing the financier's shares over time through payments linked to school revenues. This structure adapts the global quasi-equity model to province's specific fiscal constraints, market maturity, and risk profile while remaining fully compliant with Islamic principles observed by the province's majority population. Academic research in the province has already begun exploring hybrid sukuk models (Ijarah-based Diminishing Musharaka) for public sector universities, demonstrating growing familiarity with such structures in the province.

Rather than financing individual schools in isolation which would expose investors to concentrated risk, the facility employs district-level Special Purpose Vehicles (SPVs) structured as Musharakah partnerships, each financing 8 to 15 schools. This cluster-based approach reflects the higher risk environment of KP, where individual school failure rates may be unpredictable but portfolio performance across a district can be modelled with greater confidence. Each district-level SPV diversifies revenue risk across multiple schools, reducing investor exposure to any single institution's underperformance. The SPV structure also enables standardised legal agreements, streamlined monitoring, and coordinated recovery mechanisms that would be prohibitively expensive to negotiate school-by-school. The facility will generally operate with smaller average ticket sizes while maintaining portfolio diversification through the cluster model, further reinforced by a strong first-loss cushion to absorb initial shocks.

Product 7: RBF for Low Fee Private Schools

This facility uses a repayment structure linked to each school's monthly income, which means payments automatically go down when revenues are low, protecting schools during difficult periods. Under the proposed pilot design, a defined pool of funding would be made available to a reasonable number of schools over an appropriate period, with financing amounts per school sufficient to support meaningful improvements. Investors would initially provide the bulk of the funding, with repayment calculated as a fixed percentage of the school's monthly fee income rather than fixed instalments. Returns to investors would be capped at a reasonable level above their initial investment, ensuring schools are not burdened with excessive costs. A government funded buffer of 15 per cent would absorb first losses, protecting the main investors and making the structure affordable for schools.

The mechanism operates as follows the financier takes an initial 75% ownership stake in the school assets, with the proprietor holding the remaining 25%. Monthly repayments are calculated as a fixed percentage of the school's gross revenues, not as fixed instalments. This ensures that during low-revenue months, such as summer breaks or local economic downturns, repayment obligations automatically decrease, preserving the school's operating cashflow. A pre-agreed valuation formula determines the share price at which the proprietor progressively purchases the financier's units. Over the 7-year tenor, assuming normal revenue patterns, the proprietor will acquire full ownership. If revenues decline, the buyout slows automatically; there is no default trigger unless the proprietor misreports revenues. This feature eliminates the punitive default cycles that plague conventional school lending, where a single bad month can trigger cascading penalties and eventual closure. The return is capped at 1.5x the initial investment, ensuring that investor returns remain reasonable while school proprietors capture the full upside of improved performance.[33]

The facility incorporates a blended finance layer that makes the structure work for Islamic lenders while keeping costs affordable for schools. A buffer fund of 15 per cent of the total portfolio, provided by the government or matching donors, absorbs the very first losses that inevitably occur in any lending programme, protecting the Islamic financiers who provide the main funding. Because this government buffer takes the initial risk, Islamic banks and microfinance institutions can offer rates below normal commercial levels, making loans affordable for schools while still delivering returns acceptable to their investment committees.

The facility adds a layer of public money that makes the structure work for Islamic lenders while keeping costs affordable for schools. A buffer fund of 15 per cent of the total portfolio, provided by the Government or matching donors, absorbs the very first losses that inevitably occur in any lending programme, protecting the Islamic financiers who provide the main funding. Because this government buffer takes the initial risk, Islamic banks and microfinance institutions can offer rates below normal commercial levels, making loans affordable for schools while still delivering returns acceptable to their investment committees.

Several layers of risk mitigation are embedded in the design. Revenue misreporting risk, the greatest threat to revenue-based financing is addressed through digital fee collection systems where feasible, random third-party audits, and the cluster SPV structure that allows cross-school verification. Portfolio risk is diversified across districts and school types, with the first-loss cushion absorbing initial shocks. Legal risk is managed through standardised Musharakah agreements developed in consultation with Sharia scholars and vetted by the SECP. Governance risk in rural districts is mitigated by initially targeting schools in urban and peri-urban areas with better financial record-keeping, Peshawar, Mardan, Abbottabad, and Swat have significant private education footprints that can anchor the pilot. Schools without adequate financial records will be excluded from the pilot. Revenue volatility is addressed through cluster SPV pooling and digital fee collection enforcement, supplemented by financial literacy support for enrolled schools.

Feasibility is assessed as Medium-Low, reflecting the absence of regulatory precedent for education sector application of Diminishing Musharakah, though the structure is recognised under Islamic banking regulations. Institutional capacity for equity-like investments is low, as exiting expertise lies in grant-based partnerships and the New School Initiative rather than commercial financing. However, the presence of CSOs which operate in the province with proven Sharia-compliant lending infrastructure, provides a potential implementation partner. Market appetite from borrowers is medium-high, as low-cost private school operators in underserved areas consistently seek working capital for expansion and

[33] To make the commercial bank comfortable with a limit on their profits (the 1.5x cap), we add a safety net that guarantees they get a minimum payment every month, no matter how the business is doing. By protecting their original investment with a backup guarantee, the bank is comfortable to trade the chance of a windfall gain for the certainty that they won't lose their money.

quality upgrades. The growing low-cost private school footprint in urban centres such as Peshawar, Mardan, Abbottabad, and Swat provides a ready market for pilot deployment.

International evidence demonstrates that low-fees private schools can sustainably absorb appropriately structured financing, achieving high repayment rates when loans are designed to match schools' cashflow patterns. The LEAPS research project[34], a multi-year study of Pakistani private schools co-led by World Bank and Harvard researchers, provides evidence on the potential of school financing. Research found that the growth in number of private schools in Pakistan is associated with now, one in three primary students enrolled in private schools. More recent experimental evidence demonstrates that providing private schools in low-income communities with access to loans reduced school closure rates compared to similar schools without access. The research further found that larger schools and those previously identified as lower-performing benefited most, suggesting financial support helps stabilise schools most at risk of closure. The credit didn't just fuel growth, it protected schools from unexpected financial shocks, reducing the likelihood of sudden shutdowns due to cash flow problems. For Khyber Pakhtunkhwa, revenue-based financing could unlock working capital for partner schools, enabling them to improve infrastructure, retain teachers, and deliver better learning outcomes, particularly in merged districts where access to formal finance remains constrained.

Implementation Roadmap

A sequenced approach will be essential given the instrument's novelty and province's context. During the next 12 months, a market diagnostic and feasibility study with transaction and Shariah structuring advisory support could examine the viability of Diminishing Musharakah for school financing in selected districts, including a financial scan of at least 100 schools. Legal clearance for the SPV structure from SECP, identification of an anchor Islamic financier, and securing the first-loss donor tranche will follow. During years 1-3, a small pilot in partnership with the financier will test the Musharakah structure with 50 partner schools in 3 districts under New School Initiative, using a standardised reporting toolkit and independent verification of enrolment and repayment performance. In years 3-5, the instrument can be scaled with a larger pool, adding other Islamic banks following successful demonstration of the pilot model.

[34] Andrabi, T., Das, J., Khwaja, A. I., & Ozyurt, S. (2025). *Helping Schools Survive: Experimental Evidence on the Impact of Financial and Educational Support to Private Schools* (NBER Working Paper No. 34042). National Bureau of Economic Research. https://www.nber.org/papers/w34042

9 Public-Private Partnerships: Optimising the Model

Khyber Pakhtunkhwa's engagement with PPPs in education is evolving, with the government now committed to outsourcing underperforming schools under a structured PPP framework to improve learning outcomes and infrastructure. The P&DD's PPP Unit, has been advancing this agenda, completing feasibility surveys of schools across the province and identifying primary schools suitable for immediate transition to PPP management.

The report acknowledges Khyber Pakhtunkhwa's existing PPP framework while suggesting that the provincial government could consider strengthening it through amendments to its PPP Act, including explicit inclusion of social sector and education projects, stronger statutory provisions for Viability Gap Fund and Project Development Facility replenishment, clear takeover powers for failing projects, and formal decentralised monitoring committees.

Public schools suffer from multiple issues, including missing facilities, lack of teachers, poor teaching quality, low enrolment, high drop-out rates (especially for girls in secondary grades), and declining pre-primary enrolment.

Pilot-ready optimisation instruments for Khyber Pakhtunkhwa could include:

- **Double-shift PPPs:** Utilising under-enrolled government schools for second-shift operations by private partners, expanding access without requiring new infrastructure and supporting the existing public sector architecture which has already received substantial investment.
- **Adopt a School (AAS) Evolution:** AAS is generally driven by philanthropy, with no formal accountability on a private sector adopter who may or may not have the experience of school management. Recent developments in Sindh (Education Management Organisations) and Punjab Public School Support Program (PSSP) have seen private sector adopters taking up a more formalised role in overall school management and capacity development.
    - **Model:** Aims to leverage private sector to support low-performing public schools to increase access to schooling and enrolments and improve education outcomes through efficient school management. This instrument is transforming CSR initiatives into performance-based PPPs with explicit outcome targets, building on ESEF's infrastructure that enable private education providers and donors to adopt a public school and/or fund specific facility upgrades.
    - **Payment Structure:** 75% fixed per-student subsidy, 15% teacher attendance-linked, 10% enrolment increases and girls' retention-linked.
    - **Risk Mitigation:** Operator bears performance risk, while government retains infrastructure ownership. Payment released through escrow to reduce delays.
    - A challenge would be to source private sector party with the capacity and willingness to take over a a cluster or significant number of underperforming schools, especially in remote

and rural settings. At the beginning of the programme, government will conduct a mapping exercise to list potential private sector players.

  - Ambiguity over corrective actions should private sector performance be unsatisfactory. If the contract is terminated during a multi-year term it would be challenging to find a replacement. E&SED will develop a strategy where in case of exit by a private partner, schools have been handed over to other private partners operating in the district resulting in smooth transfer of responsibilities or steps to be taken for E&SED to take the school back.
  - Strong resistance by public sector teachers. Private sector will have management control of the adopted public schools, but will not have the authority to hire/fire/transfer existing public sector teachers. This creates management challenges should teachers not cooperate. One of the most common options in such situations is to hire private teachers and bear the additional cost. However, a key role of E&SED will be to develop a guideline in order to offer public sector teachers a transfer that they will like or an option stay in the adopted school. In the case of PSSP in Punjab, all teachers opted for a transfer; while in EMO in Sindh, public sector teachers were retained and the process was politically managed.
  - There is a dearth of specialist teachers in public schools. Private sector to be selected based on their capacity to source and train teachers.
  - **Key elements for success:** Multi-year partnership agreement including key performance indicators on enrolment, assessments, school facilities and teachers among others; periodic progress reporting against agreed upon key performance indicators, output-based contracting to allow the private partner to decide how to deliver the envisaged services. It will enable the government to tap into the private sector's creativity to deliver the agreed-upon education outcomes at lower costs and better quality. Adequate support from the district education office as contracted school may depend on district staff and resources for a variety of services, including facilities and management and identifying OOSC.
  - **Criteria to select low-performing public schools:** Enrolment below a certain threshold, schools where building exists but are not operational/functional, schools with low student retention, lowest-performing schools in terms of standardised examinations, and districts selection should be based on OOSC population.
  - **Management structure and delivery mechanism:** The government will provide a list of low-performing primary schools (along with relevant school details) to the private operator. Before contracts are signed with the private operator, the existing teachers at government schools will be offered a transfer to other nearby government schools. Any missing furniture or infrastructure in the adopted schools will be provided by the private operator under Infrastructure Subsidy, as applicable/required.
  - In the initial phase a total of 4-5 districts will be selected. These districts will be selected on the basis of highest number of low performing primary public schools.
  - The relevant government body to develop a toolkit to engage the private sector, similar to the one based in Sindh on EMO. The toolkit should have information such as criteria for identification of schools, criteria for selecting private sector operator, transaction documents and associated templates (contract management and sample partnership contract), monitoring and evaluation templates and clearly defined exit mechanisms.
- **Partnerships for Merged Districts:** Designing specific PPP frameworks to accelerate quality education delivery in the merged districts, where the Merged Areas Education Foundation has already planned new community-based schools through PPPs with stipends of PKR 1,000 for grades I–V and PKR 1,500 for grades VI–VIII.
  - **Design:** The financing mechanism must work in low-capacity, remote environments, incentivize girls' participation, support community-based school operators, minimise permanent fiscal liabilities, simple enough for rural operators. This is not a standard PPP; it is a community-based, performance-linked public financing instrument.
  - **Financing Architecture:** The proposed financing architecture includes a per-student operational subsidy paid directly to school operators rather than families, along with an additional girls' participation top-up to address gender gaps in merged districts. A one-time

start-up grant would be provided per community school to cover basic classroom setup, furniture and teaching-learning materials. Infrastructure remains community-owned while education delivery is regulated. The overall cost for a pilot group of schools can be structured to fit within the province's development planning framework.

- **Risk mitigation:** Community oversight through School Management Committees. Community involvement reduces elite capture risk. Security disruption is Medium–High and can be mitigated via cluster-based rollout. Ghost enrollment risk is high, introducing digital validation for children would be important. Incentivized recruitment allowance will address the risk of low female teachers availability.

Readiness and feasibility: Pilot implementation is feasible within 12 months. Legal feasibility is medium, requiring a clear education PPP guidelines to complement the existing PPP Act framework. Institutional capacity is medium, with the P&DD's PPP Unit providing structuring expertise and SED contributing domain knowledge, supported by recent budget commitments for boundary walls and washrooms in schools. Market appetite from quality private operators is medium-high, evidenced by the government's confidence in outsourcing existing schools and establishing new schools through ESEF.

Sequenced roadmap: SED and P&DD to jointly develop a education PPP policy; launch pilots for double-shift and fully outsourced schools in selected districts, including merged districts where 500 new classrooms are planned for primary schools ; establish a dedicated education PPP cell within SED with technical assistance from development partners; and implement robust monitoring mechanisms to track the reported 6 percent increase in teacher attendance already achieved through enhanced school monitoring systems. The aim will be to eventually integrate these mechanisms into provincial education financing framework.

10 Debt Swaps: Converting Debt Servicing into Education Investment

A debt-for-education swap is a financial transaction in which a government refinances expensive existing debt on more favourable terms, and the fiscal savings generated are redirected to agreed education investments. Unlike new borrowing or grant financing, a debt swap repurposes future debt service payments that would have left the country, converting them into domestic resources for schools, teachers, and learning outcomes. The instrument addresses a structural challenge facing Khyber Pakhtunkhwa: expensive debt service consumes fiscal space that could otherwise fund education priorities. A well-structured swap transforms this liability into an asset for development.

The core mechanism involves three steps. First, a portion of high-cost existing debt, typically loans or bonds with high interest rates and short maturities is identified for refinancing. Second, credit enhancement, such as a guarantee from a multilateral development bank, enables the government to access new financing with a lower interest rate, longer tenor, and grace period. Third, the government commits to directing the resulting fiscal savings, the difference between what it would have paid on the old debt and what it pays on the new debt, into a ring-fenced education programme with agreed results targets and independent verification.

The World Bank-supported debt-for-development swap in Côte d'Ivoire, completed in late 2024, provides the most relevant precedent for Khyber Pakhtunkhwa. The operation targeted most expensive debt maturing over five years.[35] Using a policy-based guarantee from the World Bank, the government obtained a new loan with a 15-year maturity and a six-year grace period, significantly better terms than the debt it replaced. The transaction freed up budget resources over five years. These savings were directed at an ongoing World Bank-supported education programme, with built-in spending and results monitoring mechanisms that ensured accountability without creating costly parallel structures.

Product 8: Khyber Pakhtunkhwa Education Debt Swap Facility

The proposed Khyber Pakhtunkhwa Education Debt Swap Facility would target approximately PKR 8 billion of the province's highest-cost debt, potentially including existing bonds issued at elevated rates, bank loans, or expensive federal on-lending, for refinancing with support from a multilateral guarantee. Based on the Côte d'Ivoire model and adapted to the province's sub-national context, the structure would operate as per Table 6.

[35] World Bank Group. (2024, December 5). A Pioneering Path: How Côte d'Ivoire is Reshaping Debt Management to Invest in Human Capital. https://www.worldbank.org/en/news/feature/2024/12/05/a-pioneering-path-how-c-te-d-ivoire-is-reshaping-debt-management-to-invest-in-human-capital

Table 6: Debt Swap Facility – Key Parameters at a Glance

Component	Proposed Design
Target Debt	Debt (existing bonds, loans, or federal on-lending) with remaining maturity under 5 years
Credit Enhancement	Policy-based guarantee from Multilateral Bank (40-50% cover) to improve credit terms
New Financing	Bond issuance in domestic capital markets with 10-year maturity and 3-year grace period
Fiscal Savings	May be realised over 5 years
Education Investment	Savings channeled to Elementary & Secondary Education Department's existing high-priority programmes
Results Framework	Agreed targets for school construction, girls' retention, or learning outcomes, monitored through existing IEMIS and third-party verification

The transaction would be enabled by a policy-based guarantee from a multilateral development bank. This guarantee would cover a portion of the new bond issuance (typically 40-50%), giving domestic investors confidence to lend at lower interest rates and longer tenors. Unlike a sovereign guarantee, which creates contingent liability on the national balance sheet, a multilateral guarantee reduces risk without requiring the federal government to assume additional exposure.

The savings generated would be ring-fenced within the provincial budget through a dedicated code or treasury account, ensuring traceability without creating parallel systems. These funds would be allocated to priority education investments already identified in the government's FY 2025-26 budget. These investments would be channeled through existing E&SE Department delivery systems, monitored through IEMIS, and verified by the same third-party mechanisms used for other innovative financing instruments.

These savings represent new fiscal space, resources that would have left the province as debt service but instead become available for schools, teachers, and learning outcomes. They do not require new taxation, new borrowing (beyond the replacement financing), or cuts to other programmes. They simply repurpose future payment streams from creditors to children.

Implementation Roadmap

A debt swap requires sequenced preparation given its complexity and the need for multilateral engagement. The proposed roadmap spans 24 months.

Phase one, Feasibility and Debt Stocktake over first six months, involves commissioning an independent review of the provincial debt portfolio to identify eligible high-cost debt, engaging the Finance Department and Auditor General to validate data, developing a preliminary financial model, and approaching the multilateral banks for an expression of interest. The Finance Department leads with transaction advisory support.

Phase two, Multilateral Engagement over next six months, requires a formal request to the multilateral bank for a policy-based guarantee, alignment with the country partnership framework, demonstration of fiscal discipline and education sector performance, and negotiation of guarantee terms and conditionality. The Finance Department and P&DD lead, engaging with the multilateral partner's country office.

Phase three, Transaction Structuring over months eight to fourteen, involves hiring legal and financial advisors, structuring the new bond issuance with Economic Affairs Division (EAD) and SECP approval, developing a prospectus, securing a credit rating, and finalising the education investment plan and results framework with the E&SE Department. The Finance Department leads with transaction advisors.

Phase four, Investor Roadshow and Launch over months twelve to sixteen, requires conducting a roadshow with domestic institutional investors (banks, pension funds, insurance companies), launching the bond issuance, executing the guarantee agreement, and completing the debt buyback. The Finance Department leads with an investment bank.

Phase five, Implementation and Verification over years one to five, channels savings to agreed education investments through E&SE Department systems, monitors results through IEMIS and third-party verification, and reports annually to creditors and the public. The E&SE Department and Finance Department lead, with the independent verifier.

Feasibility is assessed as Medium across key dimensions. Fiscal capacity is High given KP's demonstrated discipline and surplus budget. Policy alignment is High as the government has already signalled intent to issue Education Bonds. Institutional capacity is Medium, requiring transaction advisory support as bond issuance experience is nascent. Multilateral appetite is Medium, with multilateral banks having demonstrated commitment to debt swaps and active Pakistan programmes. Legal framework is Medium, with EAD and SECP framework existing and sub-national bond issuance precedent established.

Annex 1: Stakeholder Coordination, Risk Framework, and Government Decisions

Delivering the proposed set of financing instruments will require close coordination among different parts of government and their partners. The departments responsible for finance would provide the first loss capital, those setting education priorities would define investment needs, and those overseeing planning and development would help generate a pipeline of bankable projects. A dedicated guarantee vehicle would manage portfolio risk. A commercial bank would serve as anchor lender, the education foundation would maintain links to schools and vendors, and independent monitors would verify results. An inter departmental working group, chaired by a senior official from the lead education department and including representatives from finance, planning, the education foundation and a commercial bank, should oversee implementation across all instruments to ensure coherence and resolve bottlenecks.

Comprehensive risk framework

Risk Category	Mitigation Measures
Credit risk	Spread loans across different districts and school types so a problem in one place does not sink the whole portfolio. A first-loss fund absorbs the first defaults. Stop lending temporarily if unpaid loans exceed an agreed level, such as 5 per cent of the portfolio.
Political and payment risk	Protect contract payments in escrow accounts so money owed to contractors is safe. Make multi-year outcome fund commitments so service providers can plan. Keep first-loss money outside day to day treasury accounts with proper audit trails.
Verification and fraud risk	Use independent monitors for all instruments. Require geo-tagged photos, biometric attendance records, and integration with government data systems. Rotate auditors regularly. Build lessons from past problems into every contract.
Data and privacy risk	Put strict data rules in vendor contracts. Follow data protection laws. Be clear in every agreement about who owns the data and who can access it.

Pilot implementation approach

As a general practice, for credit guarantee instruments, a 12-month sandbox approach will test instruments in controlled settings before scale-up. Phase 1 (months 1-3) establishes legal frameworks, finalises term sheets, selects pilot districts, and secures anchor partnerships. Phase 2 (months 4-6) launches pilots in two districts with capped portfolios, disbursing first loans against verified milestones. Phase 3 (months 7-9) analyses repayment data, stress-tests verification protocols, and adjusts covenants based on operational learning. Phase 4 (months 10-12) expands to additional districts if performance thresholds are met and integrates first-loss capital into ADP planning.

General Decision Guidelines for Government of Khyber Pakhtunkhwa:

- Agreement on piloting 2-3 priority innovative financing products.
- Approving first-loss capital allocations for pilot instruments, including an EdTech facility, an outcomes fund for a girls' retention programme, and a credit guarantee facility, along with establishing a governance mechanism for guarantee operations
- Authorising ring-fenced operating arrangements outside standard treasury processes, with independent audit and public reporting requirements
- Confirming risk appetite parameters, including coverage ranges, portfolio caps, stop-loss triggers based on non-performing loan thresholds, and first-loss tranche sizing
- Approving procurement frameworks for third-party verifiers and independent monitors, with service-level standards aligned to international best practice
- Mandating alignment between the lead education department and planning functions for project pipeline generation, school identification, and monitoring integration with education management information systems
- Endorsing the revival and digitisation of the existing adopt a school framework as the formal platform for pooling corporate social responsibility contributions, building on the education foundation's statutory mandate for private sector engagement

These decisions, taken together, will provide the legal, fiscal, and operational foundation required to move from concept to implementation across the seven financing instruments presented in this report.

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