

> **DEBATE:**

Challenge funds **ARE** the **BEST** way to engage the private sector effectively

Are you against or in favour?



BEAM CONFERENCE

19-20 MAY, 2016 | LUSAKA, ZAMBIA

➤ **Challenge funds:**
**The best way to manage the private
sector interface**

James Blewett
Maxwell Stamp PLC



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› Three myths and an observation

- Challenge funds are not compatible with market systems approach
- Challenge finance does not work
- Challenge funds distort markets by picking winners

- Facilitation is necessary but frequently insufficient to achieve development objectives

> Privately funded examples



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**SPACESHIPONE WINS \$10 MILLION
XPRIZE**

> A donor funded example

InFrontier takes stake in Afghan pharmacy chain

UK private equity group says deal shows the country is opening to business and foreign capital



› Three myths and an observation

- Challenge funds are not compatible with market systems approach
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> Shared objectives and common problems

- Shared objectives:
 - We all want to see sustainable change and deliver impact at scale
 - We all want to use our resources in the most effective way
 - We all recognise that the private sector has a vital role to play in economic growth

> Shared objectives and common problems

- Common problems:
 - How to engage with partners capable of delivering scale?
 - How to get the best results for our money?
 - How to influence private sector towards business models that promote inclusive growth?

How to accelerate the “right” kind of investment?

> The unique beauty of the challenge process

We set the
strategic
objectives

We inspire
and
promote
innovation

We choose
who to
work with
and what
to support

We choose
how much
to give

We
maintain
leverage
throughout

The private sector gets it!



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> Choosing who to work with/what to support

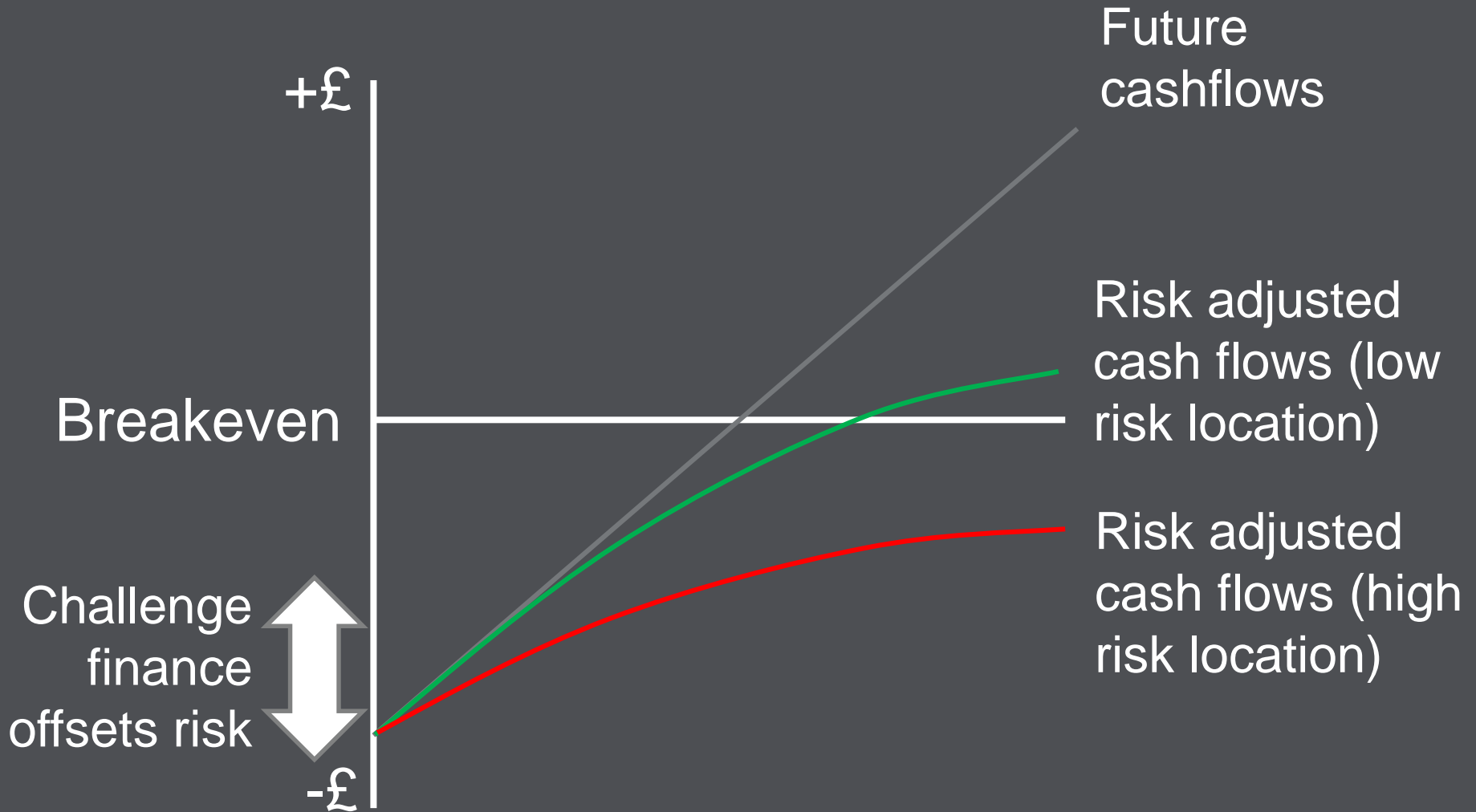
Business
ideas...

Scalable

Financeable

Commercially
viable

> Choosing how much to give



› Refinements to the model

- Challenge funds traditionally about matching grants, but smart challenge finance uses other mechanisms:
 - Risk adjusted grants
 - Patient equity capital/impact equity finance
 - Blended debt finance
- The objective is to use the unique qualities of development finance to allow the right kind of investment to take place

> Summary

- Challenge finance is an ideal mechanism to deliver market development objectives
- Smart challenge finance uses the right amount of money to incentivise private sector innovation
- Challenge finance unlocks commercial finance
- Challenge process is simple, transparent and delivers some spectacular results

> Further information

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➤ **Challenging challenge funds:
Not the best way to engage the private
sector**

Mathew Rupanga, Palladium

Livelihoods and Food Security Programme – Market
Development (LFSP-MD), Zimbabwe



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➤ Key weaknesses of Challenge Funds

Competitive calls for proposals limit the ability to identify and execute effective interventions and engage with the best partners:

- Limitation of RFPs in providing strategic information
- Poor engagement with high potential partners
- Inability to shape & facilitate business models & partnerships
- Distortion of market signals
- Crowding out private investment
- Ineffective for aligning interests
- Limited coordination

➤ Is this an efficient and effective mechanism for sourcing the best interventions?

- Of 71 concepts submitted to LFSP MIF Challenge Fund - only 5 selected
- Of 16 partnerships facilitated, 14 succeeding, 8 genuine scale and transformation potential
- The MIF challenge fund failed to generate effective interventions and to develop dynamic partnerships with a diverse range of actors



> Lessons from LFSP

- Challenge funds have catalysed a new business model – the “private sector NGO”
- Artificial design parameters pre-established by call for proposals were a barrier for some players (both too big or too small).
- The open competitive process discouraged firms from investing time and effort into developing high quality proposals.



> “Challenge funds cause businesses to propose what they think the funders want to hear. There is no scope for a shared approach to developing a sound business model.”

Max Makuise – Makera Cattle Company



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> Further information

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