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How development finance can enhance the impact of market systems approaches

Thinkpiece

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1. Introduction

Successful private sector development (PSD) is fundamental to the achievement of all of the UN's Sustainable Development Goals (SDGs), and has three elements. First, the creation and expansion of competitive firms that provide quality jobs and affordable goods and services. Second, the fostering of supply chains to link these firms with smaller providers and larger buyers. And third, the creation of an institutional framework within which such firms and value chains can emerge and thrive.

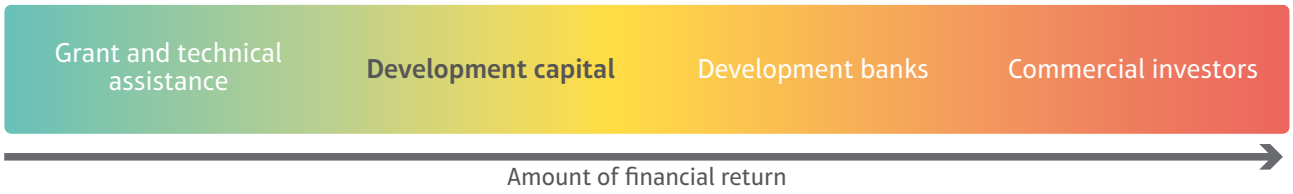
Donor resources being deployed in these areas have grown significantly over the last decade, and this is likely to continue. Development finance institutions (DFIs) provide finance to help firms become more competitive and to grow. Market systems development (MSD) approaches work on the linkages between these firms, supporting functions (e.g. finance and infrastructure), and the 'rules of the game'. A range of other donor interventions such as technical assistance (TA) and policy advice also aim to address the wider institutional framework within which firms operate. A key question is whether the resources being devoted to these activities will be sufficient to help trigger self-sustaining PSD? While it may not be possible to answer this definitively, it is clear that the more effectively resources are used, both individually and in combination, the more likely the answer will be yes.

This thinkpiece sketches a framework to think through and begin to operationalise this. It starts by setting out a 'spectrum' of different forms of donor finance, and examining donor experience relevant to two fundamental questions: (a) what type of donor finance is likely to achieve the greatest level of PSD in a particular context; and (b) how should donor resources be combined to maximise impact and value for money? The concept of 'market failures' is used as a framework to show how different PSD interventions could be complementary, particularly how commercial and concessional forms of finance might complement market systems activities. Finally, the paper suggests the appropriate mix of finance could begin to be assessed, as well as who should make the interventions.

1. Spectrums of finance

Finance is not neutral. Different forms of finance are suited to different activities, and this may be particularly true of donor investments. Figure 1 depicts a 'spectrum' of financing in terms of financial returns. These range from market-level returns on the far right, to grant financing on the far left, where pure grants can be thought of as investments with a 100% return.

Figure 1: Spectrum of financial returns



Source: Adapted from DFID 2015, page 4.

The purpose of grant financing is not to lose money of course, but to achieve other goals. We might think of these as 'development returns'. PSD generates such returns in two ways. First, the private sector is the main supplier of livelihoods[1], where 'returns' refer to the number of livelihoods created, the extent to which these are sustainable over time, and their quality in terms of income and working conditions.

1 Defined here to mean employment and self-employment, both formal and informal.

Second, the private sector is the main supplier of goods and services (G&S), where again the 'returns' generated would depend on their quality, sustainability and affordability.[2]

Different types of donor investments will generate different forms of PSD impact. These may be direct (e.g. providing growth capital that enable firms to expand and provide more jobs and G&S), or indirect (e.g. supporting infrastructure or the ability to enforce contracts).

Different types of investment will also generate different levels of financial return over different periods of time, affecting how much and how soon resources can be recycled for future use, and thus for further impact.

Central to this question is the relationship between development and financial returns in the context of PSD. In each of the cases identified below, it is assumed that the aim is to achieve the maximum possible development returns. What varies is the amount of financial return on investment that is compatible with this goal. In some cases, financial returns increase in step with development returns. In others, no financial return can be expected from the investment as with grants, but the expected development returns remain high. Within these two extremes, we can identify four other levels of financial return that would be associated with maximising development returns:

1. **Fully positive:** financial and development returns increase together proportionally. High financial returns are thus associated with high development returns. From a PSD perspective, creating or fostering competitive, expanding businesses that provide affordable G&S and generate lots of high-quality jobs are examples.

2. **Partially positive:** positive financial returns are compatible with high development returns, but only at a sub-commercial level. This could be investments in certain types of infrastructure where commercial returns are constrained by the need to achieve development impact. It could also be pioneer firms entering new markets or innovating with different business models, where risk-adjusted returns are below those commercial investors would accept.

3. **Partially negative:** a proportion of the initial investment is expected to recouped, though less than the initial amount. This could involve investment in 'pioneer' firms facing particularly difficult conditions, or support for entities such as business support or information providers, which charge a fee but only partially cover their costs.

4. **Fully negative:** pure grant financing, where there is no expectation of repayment. These are investments to support the environment in which firms operate, or enhance firm competitiveness. This might relate to infrastructure, contract enforcement, or education and skills, but would also cover research and practice into PSD.

A first question is whether investments in these categories are on a temporary or permanent basis. Pioneer firms may lose money for a while (category iii), and then make a positive but sub-commercial returns (category ii). The expectation, however, is that they will become commercially viable (category i) in time. Concessional finance (including grant finance to support non-remunerated activities that promote PSD) is thus deployed on a temporary basis. If the aim is to maximise the use of donor resources, then the transition to commercial viability should be as short as possible.

Another way of looking at this is that investing in only category i) type investments would maximise the donor resources available for PSD as these could be recycled and reused. This would not see PSD returns maximised, however, as the high development returns obtainable from categories 2 - 4 would not be realised.

2 In both areas, returns might be weighted for equity – e.g. creating jobs in areas of high unemployment, or the provision of affordable G&Ss to poorer groups not previously reached might attract some kind of premium.

Other issues are 'crowding out' and additionality (i.e. if investments generate high financial returns, then donor finance is simply displacing potential private investment, and there is thus no additional benefit from donors making them once this has been demonstrated).

These factors suggest that development returns will be enhanced when the most appropriate type of donor investment is used. How should this decision be made, however? The next section examines some recent examples that may provide useful lessons in this regard.

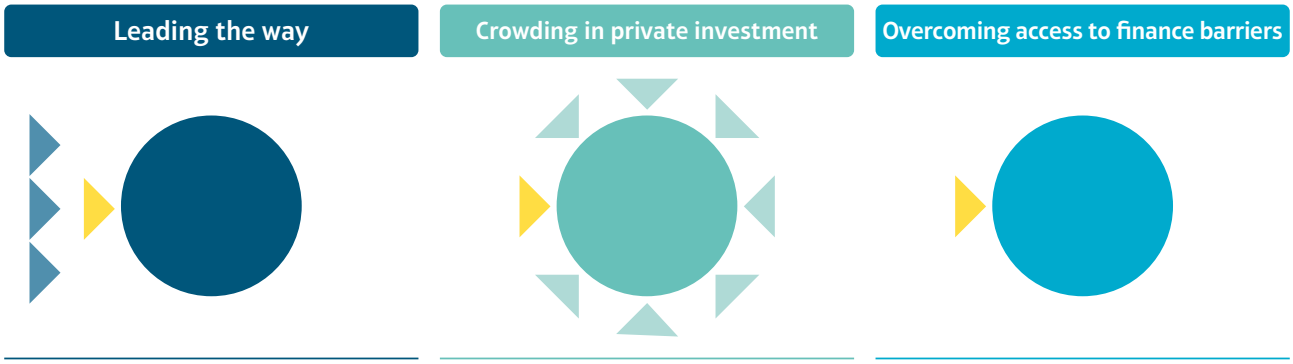
2. Donor experiences

2.1 Matching investments to PSD activities

Some key development actors are now giving considerable thought to these questions. In 2015 for example, the UK's Department for International Development (DFID) launched an initiative called 'Development Capital', aiming to achieve "modest financial returns alongside significant development impact." For DFID[3], investments using Development Capital have two aims: to generate *direct* development impacts in terms of jobs, infrastructure and the supply of G&Ss; and *indirect* impacts by leveraging additional finance through one of the three mechanisms shown in Figure 2.

The 'Leading the way' approach is investing in pioneer firms. The second and third approaches both concern risk. Development capital (DC) would 'crowd-in' private co-investment, by taking on additional risk, thus boosting risk-adjusted returns for investors. In shallow markets where finance is not available as risks are considered too high, development capital would provide direct investment capital.

Figure 2: Development capital catalyses private finance



Source: Adapted from DFID, 2015, page 3

Impact investment funds are another source of innovative thinking on these questions. The Omidyar Network, for example, categorises its activities in a 'returns continuum' framework.[4] The primary criterion for accepting below market rates of return is where they are: "intentionally pursuing 'market-level impact'" either through the activities of pioneer-type firms or through improvements in the institutional framework for PSD.

In this context, market-level impact refers to changes that improve the overall market environment for incumbent and potential new firms. For Omidyar, the greater the sacrifice of financial returns (which may be up to 100% in the case of grants), the greater the market impact required to justify the investment.

3 DFID (2015) Development Capital: Catalysing investments to benefit poor people, http://bit.ly/2q47IeH

4 Bannick, M., Goldman, P., Kubzansky, M. and Saltuk, Y. (2017) 'Across the Returns Continuum', Stanford Social Innovation Review, Winter. http://bit.ly/2nFBlkR

They have not always taken this approach: the experience of the Omidyar Network led them to conclude that market development requires a variety of interventions, many of which will not yield a commercial return and some of which will not yield any private financial return.

A related way of tailoring financial investments to achieve development impact is through the use of blending, where commercial finance is combined with concessional or grant financing to lower the rate of return the borrower sees. Deciding on whether to use blended finance, and what the proportions of commercial versus concessional finance should be, involves thinking through the same issues that are presented in the categories above. European institutions such as the European Bank for Reconstruction and Development (EBRD) have been at the forefront of these approaches, as have multilateral actors like the International Finance Corporation (IFC).

2.2 Combining interventions to maximise PSD impact

As well as deciding on which types of finance to use in different contexts, a key question is how these types should be combined with each other, and with other interventions to support PSD. Given its mandate to support the transition to market economies, it is unsurprising that the EBRD is again a valuable source of experience and wisdom on these issues.

The World Bank Group (WBG) has also begun to develop innovative and potentially very important initiatives in this area. Through its role working with governments (both advisory and through the provision of grants and loans), the EBRD has a unique ability to influence this for the better. At the same time, the IFC has unparalleled experience investing in firms that can succeed within these environments, while the Multilateral Investment Guarantee Agency (MIGA) is able to help leverage private investment by mitigating risk.

The different parts of the WBG have always collaborated of course, but this has not always been as strategic as it might have been, and institutional disincentives have inevitably developed. The more these agencies can coordinate their activities, therefore, the better. For this reason it is very much to be welcomed that they have recently announced a new Private Sector Window as part of the International Development Association (IDA) 18 process, and the 'Forward Look' strategic review.[5] As well as introducing new instruments and facilities, staff from IFC, IBRD and MIGA will be incentivised to cooperate strategically. The goal is for projects to be structured in the most appropriate way in terms of the finance mix, and to reduce incentives for different institutions to automatically favour either private or public finance.

Knowing that private and public finance (including guarantees) can be strategically combined to differing degrees, and that the impacts of these investments can be enhanced by other forms of complementary intervention, is not the same as actually doing this. Here, IFC's experience with blended finance in the climate change space, where it is has combined commercial and concessional donor finance, provides valuable experience, as well as a set of rigorous procedures.[6]

From this foundation, a set of principles are being developed to operationalise this across the WBG, with the aim of maximising the quantity of private finance that can be leveraged with official and public finance.[7] These principles are being formalised in a set of diagnostic tools designed to achieve the maximum development impact with the minimum use of concessional resources, and to deploy these resources in as strategic and complementary a manner as possible.

Where the diagnosis finds that development impacts can be achieved with commercial finance only, perhaps supported by non-financial interventions to address the market failures identified,

5 World Bank (2016) Forward Look – A Vision for the World Bank Group in 2030 – Main Messages, prepared by the World Bank Group for the October 8, 2016 Development Committee meeting http://bit.ly/2nTezqL

6 Sierra-Escalante, K. (2016) 'Target and Discipline: IFC's Approach to Blended Finance', IFC blog http://bit.ly/2oEM00d

7 For example, see: Morris, S. (2017) 'New Leadership at the IFC Aims to Get Us from Billions to Trillions', Center for Global Development blog http://bit.ly/2oEC3jf

there is no need to use any scarce concessional finance. If this is not possible, the minimum amount of concessionality needed to achieve the required development impact will be deployed.

The IFC's experience with blended finance suggests that it is possible to measure the level of concessionality required to deliver development impact accurately. As well ensuring value for money, minimising concessional finance also minimises market distortions, which is essential for sustainable private sector development.

These are early days, but this is precisely this kind of joined-up thinking that will be required of all development agencies if the potential private sector contribution to the SDGs is to be realised. One type of intervention that has always looked at PSD in a 'joined-up' way, and thus has the potential for learn from (and perhaps contribute to) these initiatives, is the market systems approach.

3. Market systems development: correcting market failures

Market systems practitioners seek to catalyse the productive exchange of goods and services in ways that benefit the poor. To achieve this, they are concerned with developing forward and backward linkages in supply chains that poor people can benefit from, identifying the 'supporting functions' that are needed to facilitate this (e.g. infrastructure, finance or fertilizers), and fostering 'rules' (i.e. institutional frameworks) that create the necessary conditions to support this process.

As with the WBG framework, therefore, the approach is one of diagnosis and cure. In this case, 'diagnosis' entails identifying the market failures that are preventing the development of a healthy market system, and the 'cure' is the intervention designed to correct these failures. The main market failures identified in the literature, are:[8]

1. **Insufficient competition**. Formally, markets only yield welfare-maximising outcomes where there are enough competing firms that none can influence prices: they are all 'price takers.' In many cases, this will not hold and oligopoly or monopoly may result.

2. **Public goods.** These will not be supplied, or may be under supplied, by private actors. Core characteristics are that they are 'non-rival'[9] and 'non-excludable'.[10] It is accepted that governments should provide public goods, partly or in full, directly or indirectly.

3. **Externalities.** These arise when actors not directly involved in a market activity are affected by it. They can be negative or positive. Where private actors do not bear the costs of their activity (e.g. polluting), they will do more of it than is socially desirable. Where they do not capture the benefits in full they will do less of it.

4. **Missing markets.** These arise where a good or service could be profitably supplied but is not. In a competitive system, such opportunities should be exploited. Lack of finance is a key example, with information asymmetries and transaction costs often seen as causes for these finance market to be "missing".

5. **Incomplete markets**. This is where an activity is only viable when another is undertaken. In supply chains it only makes sense to produce a component if all the others are also produced. Problems of coordination and information are central to this market failure.

8 The original concept of market failure was based upon violations of the assumptions underpinning the Arrow-Debreu (1954) general equilibrium model. This model is the basis for the First Fundamental Theorem of Welfare Economics (i.e. market-outcomes are welfare maximising) but is based on very strict assumptions: perfect competition; perfect information; complete markets (in space and time); no externalities or public goods. Where these conditions do not hold, the market cannot be expected to deliver welfare-maximising outcomes, in that better outcomes (in a Pareto efficiency sense) could potentially be achieved through other mechanisms. It is these situations that have come to be known as 'market failures'.

9 Where the consumption of a good by one person does not reduce the capacity of others to consume.

10 Where it is difficult to prevent people consuming the good.

6. **Imperfect information** can lead to missing and incomplete markets, but also affects R&D and innovation. As with positive externalities, private actors will not engage in the socially optimal level of R&D and innovation.

In Table 1, we give some examples of market systems activities that relate to these market failures, compiled by reviewing programme information on the BEAM Exchange website.[11] As we can see, some types of market failures feature more than others. No interventions relating to externalities were found, for example. Some projects seek to address public good provision (e.g. infrastructure or regulatory issues) though fewer than might be expected given the importance of these issues. For competition, the focus appears more on curbing the power of buyers than spurring competition between producers, although many activities listed under 'incomplete markets' do aim to improve the competitiveness of existing producers.

Interventions related to 'missing markets' focus on financial sector development. Together with those addressing incomplete markets – particularly developing and improving supply chains (i.e. coordination), and equipping producers to participate in these by improving quality and reliability – these type of interventions were the most numerous found.

Table 1. Market failures and market systems activities

Market failure category	Sub-Category	Examples identified with market systems approaches	Solutions identified through MS approaches
Public goods	*Infrastructure to access market lacking*	ACLP: dairy, beef and sheep producers limited ability to access market	Large-scale renovation of key market access infrastructure
	Weak/absent institutions	FSIP Uganda: ineffective legal financial framework	Enhance the legal and regulatory structure for the financial sector
Imperfect competition	*Prices too low to enable profitable production*	GROW Liberia: domestic price of rubber too low	Develop capacity to access export market
		GROW Liberia: buyers suppress cocoa prices	Develop capacity to access export market
Missing markets	*No finance*	GROW Liberia: agricultural input suppliers	Loan guarantee facility provided (with First Bank Liberia)
		BIF Malawi: low income customers cannot afford solar power products	Develop innovative financing mechanisms (lease-own)
		LIFT Ethiopia: farmers have limited access to finance	Develop loan products with 'second level land certification' collateral
			Provide matching grants for financial institutions in agriculture
			Facilitate information exchange between lenders and farmers to reduce asymmetries
			Develop Islamic finance products
		AFR Rwanda: lack of financial products for poor	Develop insurance and pension products; foster growth of SACCOS
		FSD Zambia: lack of finance for SMEs and households	Improve credit information supply
			Facilitate expansion of digital finance (reduce transaction costs)

11 https://beamexchange.org/practice/programme-index/

Incomplete markets	*Higher value chain activities inaccessible*	GROW Liberia: rubber price too low	Create learning centres for smallholders to produce ribbed smoked sheets (RSS) rubber
	Supply chain undeveloped	MADE Ghana: lack of supply chain for farmers	Improve supply chain for vegetables, groundnuts and rice
	Supply chain niche inaccessible	BIF Nigeria: product poor quality and supply chain hard to access	Work with input providers (seed) and off-takers
	Uncertain/absent property rights	LIFT Ethiopia: lack of secure tenure reduces agricultural incentives	Facilitate rural land rental scheme
	Lack of coordination between actors	LIFT Ethiopia: farmer unable to access appropriate inputs and obtain good prices	Develop contract farming scheme to satisfy unmet demand for high quality products by providing inputs, supervision and price.
	Transaction costs too high	PSP4H: lack of affordable health services	Development of low-cost delivery models
Imperfect information	*Poor access to best practice knowledge*	GROW Liberia: farmers not using best vegetable production techniques	Train 250 local farmers
		LIFT Ethiopia: livestock requires fresh fodder but grazing lands decreasing	Spread knowledge on high-yielding grass varieties
	Knowledge lacking on feasibility of new products	BIF Malawi: lack of market intelligence on solar product market	Facilitate market intelligence on solar products market
	Lack of innovation	BIF Myanmar: lack of good tourist products	Create Tourist Product and Package Innovation Competition
		FSIP Uganda: lack of innovation in financial services for the poor	Provide matching grants to financial providers to encourage innovation

Source: Author's elaboration based on programme information provided by the BEAM Exchange: https://beamexchange.org/practice/programme-index/

While these activities are certainly important for market development, this does not mean that total PSD impact – i.e. the development returns discussed above – could not be increased. The remainder of this note addresses the following three questions which concern how this might be done.

1. To what extent could PSD objectives be furthered by strategic coordination between market systems approaches and other development finance actors?
2. Who should coordinate this process and what criteria should they use?
3. Are there important aspects of PSD that market systems approaches are not sufficiently addressing at present, but could do so in the future?

4. Towards greater coordination of development finance and market systems approaches

The market failure approach is a useful starting point for thinking about how different donors' PSD interventions might complement each other. The first column of Table 2 lists the most common market failures associated with market systems interventions. The other three columns provide examples of how commercial (DFI) and concessional (DC) development finance and market system (MS) approaches might complement each other.

Table 2. Potential complementaries between market systems and development finance

Market failure	DFI potential	DC potential	MS potential
Infrastructure to access market lacking	Invest in commercially viable infrastructure	Invest in sub-commercial return infrastructure	Ensure sufficient demand and remove other obstacles to infrastructure
Weak/absent institutions	-	-	Enhance the legal and regulatory structures
Prices too low to enable profitable production	Support new market entrant (buyer)		Develop capacity to access markets
No finance	Encourage larger institutions to enter market		Develop capacity to access markets
Higher value chain activities inaccessible	Support development of processing industry	Finance pioneer firms developing sector	Provide loan guarantee facility
Supply chain undeveloped	Encourage firms to source from local supply chain	Finance local sourcing at concessional rates until becomes viable	Develop innovative financing mechanisms
Supply chain niche inaccessible	-	Invest in firms with potential to enter supply chain	Develop innovative financing mechanisms
Uncertain/absent property rights	-	-	Provide matching grants for new institutions
Lack of coordination between actors	Liaise with MS actors to identify and align different actors	As with DFIs	Facilitate information exchange to reduce asymmetries
Transaction costs too high	Support investments that lower transaction costs (e.g. energy, transport, communications)	Support investments that lower transaction costs, but which yield sub-commercial returns	Develop innovative business models
Poor access to best practice knowledge	Establish links where investees can share best practice	-	Develop insurance and pension products; foster growth of SACCOS
Knowledge lacking on feasibility of new products	(Where appropriate) share market intelligence		Improve information supply
Lack of innovation		Support companies to innovate on products/ business models.	Facilitate expansion of digital finance (reduce transaction costs)

For example, where a diagnosis identifies infrastructure constraints as the key problem, but there is potentially sufficient demand to pay for these services, DFIs could invest to meet this demand, working in combination with market systems interventions to ensure sufficient demand and remove other obstacles to infrastructure development. If time was needed before this could be done commercially then DC could be deployed. Where prices are restrained by a lack of competition amongst buyers, DFIs could invest in potential competitors, or use their management influence to highlight and exploit these opportunities, while market systems actors could support capacity to access these markets. The same logic applies to missing financial markets and financial institutions supported by DFIs, or to investment in processing to enable firms to move up the value chain.

A good example of the latter is the ginger sector in Nepal. The country is the second largest producer in the world, specialising in a form of ginger that is particularly popular in the Asian market. This has been exported unprocessed but there is an unexploited opportunity to develop processing capacity and export higher value-added products to Japan. What is missing is investors willing to invest in processing capacity. Both domestic and international investors are unable, unaware or uninterested. The fact that a market opportunity has not been exploited is explicable in a market failure framework – missing (financial) markets, incomplete markets (processing capacity) and information asymmetries (about the opportunity). This is a good example of a situation where DFIs could address market failures and spur local market development, while also furthering their own goals.

Here and elsewhere, the key criterion for DFI involvement is that an unexploited and demonstrable *commercial* opportunity exists. If this is not the case, but could be once market conditions improve, there is a potential case to use concessional finance instruments and market systems approaches.

How could this would work in practice? There are two parts to this question: first, what criteria should be used to determine the financing mix; and second, who should make this assessment? On the first question, much can be learned from the experience with blended finance, particularly the IFC's approach to minimising concessionality. As described on page 1 of this paper, the goal is to maximise the total PSD impact of donor investments of different forms. This can be equated with the principle of minimising concessionality, assuming that the process for assessing this is accurate.

It is important to be clear about what the word 'minimising' means in this context. This means that a *sufficient* degree of concessionality to achieve the desired impact is used, *but not more than this*. From a PSD perspective the level of concessionality may be 100% in the case of grants, but these are targeted interventions designed to reach a point where PSD is self-sustaining. Where the obstacles to reaching commercial viability are large, financial returns may be negative for a time, but with a share of investment recouped, or positive but less than the market rate. In many cases, no concessionality at all will be needed. These options correspond to the four categories on page 2.

If this can be assessed accurately, and the degree of concessionality is minimised (both in level and over time) then donor resources will be recycled to the maximum extent consistent with achieving the desired development impact. If these resources are used in a complementary way as suggested in Table 2, then we begin to move towards a framework to maximise PSD investments.

As well as getting the right composition of financing, it is important that complementary interventions are made, particularly to improve the investment climate. This equates to the 'rules' level of the market systems framework. Of the three levels, market systems interventions focus more on 'core transactions' and 'supporting functions' than 'rules'. The WBG has the influence needed to affect these 'rules' and it may be that market systems actors are just too small to be able to do this.

This brings me to the second part of the question posed above: who should undertake the diagnosis and coordination suggested? There are three options. First, a dedicated organisation could be created for this purpose. Second, existing organisations could perform the role in combination with each other. Third, one of the existing actors could take responsibility for doing this. Given concerns over value for money, the first option is not very attractive.

The second option is certainly feasible, but would require different organisations to use common diagnostic tools and also to apply a common conceptual frame to the problem being assessed. This is not impossible, but given different mandates, incentives and cultures, this would take time to achieve.

With the third option, one set of actors would be responsible for analysing the problem (i.e. diagnosis), determining the minimum degree of concessionality needed to address this, and the portfolio of interventions required (prescription), and coordinating the interventions to achieve this. This has the attraction of clarity, but could face strong obstacles, not least buy-in from the actors being coordinated from elsewhere.

If these obstacles could be overcome, the question is who would be best placed to do this? As they already focus on identifying obstacles to market development, there is a case for market systems specialists to perform this role. While this would need to operate on a larger scale and in different sectors, the fundamentals of systems thinking are very relevant. Where a sector or value-chain is identified as having high potential development impact, one could imagine a diagnosis taking place to identify the key market failures preventing this potential from being realised, with a portfolio of investments designed according to criteria similar to those being developed by the World Bank Group. The diagnosis should also identify non-financial interventions (i.e. the 'rules').

Assuming the obstacles could be overcome, both the second and third sound reasonable in principle. Which would work best in practice, would depend on the particular institutional context of course, but detailed research into the options would also be needed. What is certainly true, however, is that neither of these options are just going to happen. The final part of this paper looks at what might be needed to begin to make this a reality.

5. Recommendations and concluding comments

Many people working for DFIs have a background in the commercial investment sector. Those working on market systems are more likely to work for one of the large consultancies, and/or have a development policy or academic background. Initiatives to design and use concessional finance may emerge from donors such as DFID or from multilateral development banks. The first obstacle to operationalising the approach sketched out above is thus one of culture. People often have very different assumptions and starting points, and use language quite differently. A relatively straightforward way of beginning to address this would be to initiate secondments, where staff spend time working in other parts of the development finance/donor/market systems nexus.

As well as culture there is also the question of incentives. As discussed above, the WBG has recognised this is an important obstacle to increasing the strategic coordination of their activities. Sometimes this will be a formal issue – IFC staff have traditionally been remunerated on the basis of deal flow and leveraged investment, for example. In other cases, less formal issues such as career progression may be relevant. Understanding these formal and informal incentives, and modifying them to encourage rather than discourage a coordinated approach, is important.

A third issue is mandate. Different institutions and frameworks have specific mandates or objectives, which would need to be modified to facilitate cooperation in the areas described. In simple terms, how do you ensure that an opportunity identified as suitable for DFI investment and passed to a DFI is taken seriously? A related issue is the tools that are used by different agencies. Here the development of standard diagnostic tools is clearly the way to go. The more DFIs and market systems practitioners use common diagnostic tools, the more likely they are to agree on the nature of the problem. The more they feel part of the same strategic system of interventions to foster PSD, the more they will understand the potential value of other parts of this system, particularly how these can complement their own activities.

The fact that impact investors, donors and DFIs are thinking seriously about these questions is very encouraging. For the private sector to fulfill its potential with respect to the SDGs, these actors need to learn from each other's experience and put in place systems that facilitate – rather than discourage – strategic and complementary cooperation.