

> Bridging the Gap: unlocking synergies between private sector development and development finance

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BRIDGING THE GAP



Unlocking Synergies between
Private Sector Development
and Development Finance

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What did we find?

A lot of nascent and emerging interest... but few examples of successful strategic collaboration

“

Many people say that there is money everywhere, but not enough good opportunities. It seems like market shaping programmes would be key to creating more opportunities.”

The development world focuses on enabling environment and capacity building, but doesn't have capital. DFIs have capital but aren't doing market shaping. Bringing them together is a dream outcome.”

The two worlds almost always miss each other. There are very few examples where efforts are joined up and aligned.

Models of alignment

Model 1

IN-HOUSE OFFER

- BII Plus market shaping
- Gatsby Africa, FSDA investment capability
- Implementer fund arms

Model 2

STRUCTURED COORDINATION

- Dutch Fund for Climate & Development
- FCDO's IMSAR and NUTEC programmes

Model 3

AD-HOC ENGAGEMENT

- USAID INVEST
- FCDO's Manufacturing Africa

Themes : Success factors and challenges



Strategy and
Incentives

Knowledge,
Perceptions
and
Capacities

Operational
Models and
Toolkits

Theme 1	Theme 2	Theme 3
Align strategies and incentives around common opportunities	Build or buy crossover knowledge, and coordination infrastructure	Close the gap between product offers
<ul style="list-style-type: none"> ⚡ 1. Develop common sector selection criteria 2. Engage the ‘other side’ in setting strategy 3. Increase use of smart investment indicators in PSD results frameworks 4. Increase emphasis on market shaping as part of investment screening 5. Strengthen handover and exit strategies to maintain momentum 	<ul style="list-style-type: none"> 6. Strengthen ecosystem mapping 7. Support coordination at country level 8. Pool DFI TA around joined-up initiatives ⚡ 9. Pilot cross-organizational secondments ⚡ 10. Implement training (e.g. mini-CFA) 11. Utilise specialist investment advisory and facilitation expertise 	<ul style="list-style-type: none"> ⚡ 12. Build commercial relevance of PSD offers 13. RBF / pay-for-performance financing 14. Re-align systems change terminology ⚡ 15. Proactively support first-time local fund managers & experiment with new fund model

⚡ Represents quick-wins.

Top tips for the design of PSD/MSD programmes

- ✓ Map and understand the investment ecosystem
- ✓ Involve investors early on in the design
- ✓ Consider which mode of involving investors is most practical and efficient
- ✓ Build in scope for experimentation
- ✓ Think of smart investment metrics/KPIs that incentivise the right behaviours
- ✓ Budget for investment expertise which can be more expensive
- ✓ Dedicate resources toward engaging with investors and collaboration
- ✓ Expand the intervention toolkit to help make investments happen

Taking this agenda forward...

'Top Tips' guidance
note for donor
programmes

Providing advisory to
donors under DCED
on how best to align

Piloting
collaborations

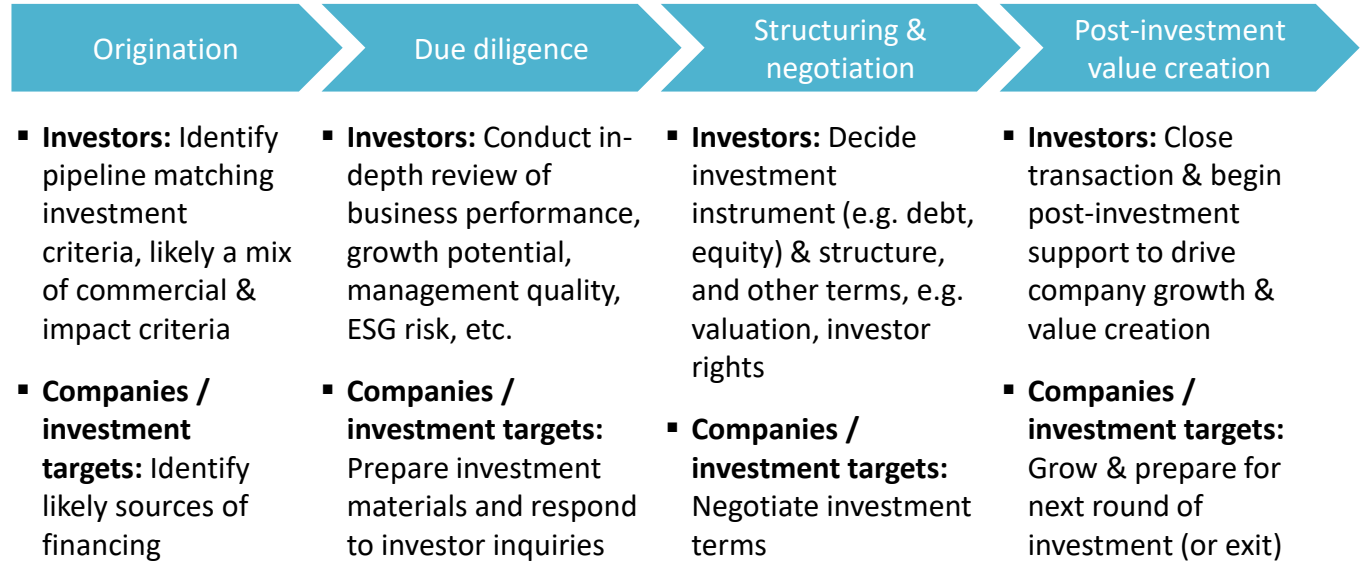
DEFINITIONS: WHAT TYPES OF “INVESTMENT” ARE INCLUDED?

WHAT DOES AN INVESTMENT PROCESS LOOK LIKE?

INVESTOR TYPES

- **DFIs** (direct and indirect investment)
- **Impact investors** funded by DFIs or other concessional capital sources; focus on both impact and returns; ability to invest at “missing middle” ticket sizes
- **Investment arms** of foundations & other donor programmes making high risk, early-stage investments

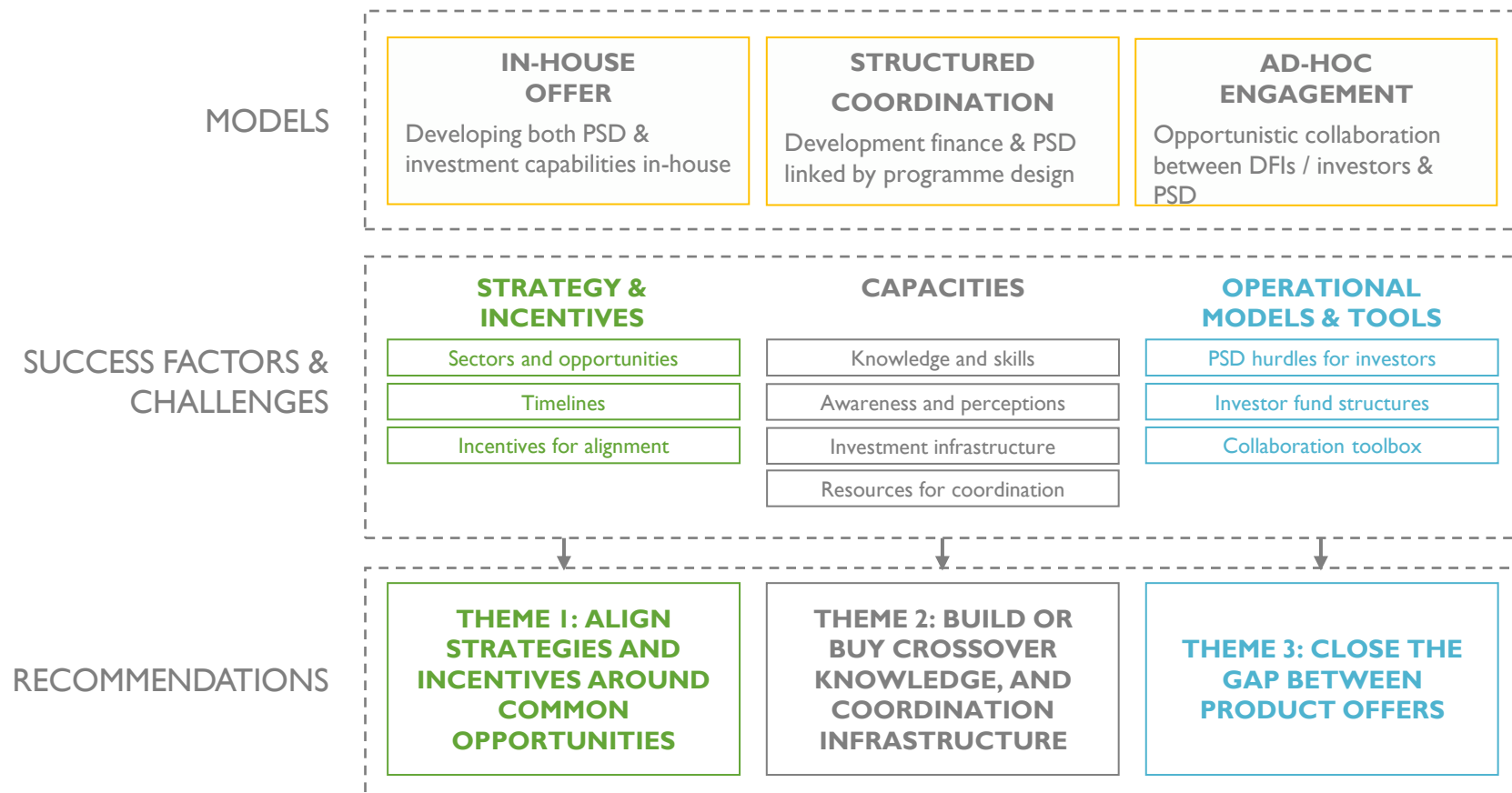
INVESTMENT PROCESS



GENERAL OBSERVATIONS

- There was interest across the board in closer alignment:
 - *“Many people say that there is money everywhere, but not enough good opportunities. It seems like market shaping programmes would be key to creating more opportunities.”*
 - *“The development world focuses on enabling environment and capacity building, but doesn’t have capital. DFIs have capital but aren’t doing market shaping. Bringing them together is a dream outcome.”*
 - *“The two worlds almost always miss each other. There are very few examples where efforts are joined up and aligned.”*
- There was mixed awareness of the full offer of the ‘other side’, and some misconceptions (sometimes based on perceptions rather than experience).
- There were few ‘model’ examples i.e. market-shaping initiatives and development finance successfully working in unison.
- Coming out of the study, we are excited about the potential to support more alignment (under the right conditions).

OVERVIEW OF FINDINGS AND RECOMMENDATIONS



CURRENT MODELS OF ALIGNMENT

MODELS



- Three broad models of alignment:
 - **Model 1: In-house offer** refers to DFIs building expertise in market shaping technical assistance (TA), and PSD initiatives expanding beyond grants to provide returnable capital.
 - **Model 2: Structured coordination** refers to a deliberate approach to linking development finance with PSD, with pre-defined investors either incorporated at design stage or formally engaged during PSD implementation.
 - **Model 3: Ad-hoc engagement** – which involves more opportunistic collaboration between DFIs and PSD programmes – is the most common model.
- The research did not identify a single ‘best practice’ model. Each model has its advantages and disadvantages, and not all models are feasible for every actor interested in closer alignment.
- Further to this, the study highlighted that closer alignment should not necessarily be a default aim for every PSD initiative and development finance-related investment.

HOW CAN WE DRIVE MORE ALIGNMENT?

THEME I: ALIGN STRATEGIES AND INCENTIVES AROUND COMMON OPPORTUNITIES

Current barriers to alignment:

- Different views on the role of the firm presented a key point of divergence ('starting races versus picking winners')
- Selecting common sectors and opportunities – different prioritisation of impact vs. commercial considerations – has been challenging
- Divergent timelines between investors with limited fund horizons & long-term PSD objectives; PSD implementation cycles can kill momentum
- Mismatched incentives for alignment on both sides

Recommendations	For whom?				Quick win?
	PSD donors	Implementers	DFIs	Other investors	
1. Develop sector and opportunity selection criteria based on both impact & commercial viability	✓	✓			⚡
2. Engage the 'other side' in setting investment strategies & programme design	✓	✓	✓		
3. Increase focus on investment in PSD results frameworks, without creating perverse incentives	✓				
4. Increase emphasis on market shaping as part of investment process; tie it to performance incentives			✓	✓	
5. Build exit strategy into PSD programme design to maintain strategic alignment, including handovers of key investment-related activities	✓	✓			

HOW CAN WE DRIVE MORE ALIGNMENT?

THEME 2: BUILD OR BUY CROSSOVER KNOWLEDGE AND COORDINATION INFRASTRUCTURE

Current barriers to alignment:

- Mixed mutual perceptions & limited awareness of ‘other side’, particularly in terms of approaches, value proposition, & mechanics of engagement
- Lack of internal capacity around investment within PSD programmes, and vice versa, market systems thinking within investors
- Infrastructure specific to investment facilitation often needed
- Coordination critical but usually under-resourced

Recommendations	For whom?				Quick win?
	PSD donors	Implementers	DFIs	Other investors	
6. Assign responsibility and resources for mapping of country-level economic development ecosystems	✓		✓		
7. Recognise and support effective investor-PSD coordination initiatives at country level	✓	✓	✓		
8. Pool DFI TA around joined-up initiatives			✓		
9. Pilot cross-functional or cross-organizational secondments	✓	✓	✓		⚡
10. Implement training for donors, implementers, programme teams, and investment personnel (investment 101, mini-CFA, market systems in practice)	✓		✓		⚡
11. Utilise investment advisory & facilitation expertise	✓	✓			

HOW CAN WE DRIVE MORE ALIGNMENT?

THEME 3: CLOSE THE GAP BETWEEN PRODUCT OFFERS

Current barriers to alignment:

- Real and perceived hurdles to engaging with PSD initiatives; many investors view donor engagement as resource-intensive & overly prescriptive
- Current investor fund structures & return expectations constrain investment ticket sizes & risk
- Investors most value technical expertise from PSD programmes, but both sides work from limited 'toolboxes' that constrain collaboration

Recommendations	For whom?				Quick win?
	PSD donors	Implementers	DFIs	Other investors	
I2. Build the commercial relevance of the PSD 'offer' to investors/investees	✓	✓			⚡
I3. Experiment with increasing use of RBF / pay-for-performance financing as part of PSD programmes	✓	✓			
I4. Re-align systems change terminology to resonate with investors	✓	✓			
I5. Proactively support first-time local fund managers & experiment with new fund models	✓		✓		⚡