# Private sector investment in dangerous places – lessons from post conflict projects of the AECF

## Draft Report from the Fund Manager

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This report was prepared by IPE Triple Line on behalf of KPMG IDAS

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The Fund Manager of the AECF is KPMG International Development Advisory Services Africa



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# 1 Background

The Africa Enterprise Challenge Fund (AECF) is a multi-donor funded financing mechanism designed to stimulate private sector entrepreneurs in Africa to find innovative and profitable ways of improving market access and the way markets function for the rural poor. The Fund awards grants and non-recourse loans to projects engaged in agriculture, renewable energy and adaptation to climate change, and access to financial services and information. It aims to improve household incomes and reduce rural poverty. Funding is awarded through competitions, with applicants judged on the commercial viability, innovation, and potential development impact of their projects.

A key element of the work of the AECF is providing funding to private sector companies in sectors and in geographies where the market will not. Supporting companies emerging in the aftermath of armed conflict can have significant impact both directly in the form of jobs and income but also indirectly through the stimulation of usually completely moribund economies. AECF investments are frequently the first external investment after aid funds and thus also have high additionality.

The AECF's Post Conflict Window (PCW) was established in 2012 with US$18m (120mSEK which was US$20m at time of contracting and reduced following the depreciation of the Krona) in grant only funding from the Swedish International Development Cooperation Agency (Sida). Following a global review of Sida's strategy particularly in the light of the refugee crisis from conflicts in the Middle East, funding was further reduced to US$14.5m in 2016.

The PCW is designed to catalyse private sector investments that are commercially viable, have significant developmental returns, and lead to wider systemic impact on market systems. In total, 18 projects have been funded in Sierra Leone, Somalia/Somaliland, Democratic Republic of Congo and Liberia. 58,920 households received an average net benefit of US$334 in 2015 with supported businesses also creating 795 additional jobs generating US$5.8m in wages for a total benefit of roughly US$25.6m.

## Scope and content of this report

The AECF has been managed since its inception by KPMG but the fund management responsibilities will transfer in May 2017 to a new entity established by AGRA specifically for the purpose. It is important that key aspects of the institutional memory of the current Fund Manager are captured before this institutional transition occurs. Designing and implementing challenge funds successfully in post conflict and fragile state environments suggests the need for novel approaches, more flexible management and the acceptance of lower performance and greater failures. The purpose of this paper is to review these assumptions and consolidate the experiences of the Fund Manager in delivering support to the private sector in post conflict environments through the use of challenge funds. This is an initial exercise to gather the institutional memory from the Fund Manager and is intended to be followed by a more substantial and comprehensive performance of interventions in post conflict and fragile state environments. This report will consist of a review of who the AECF supported in post conflict environments, how they were targeted by competitions, what has been their performance and how they were treated differently to those in the rest of the portfolio in the form of management and reporting.

## Scale and scope of the PCW

Although this report is not intended to provide an assessment of the achievement of results with the PCW, to set the context an overview of the Window is provided in the table below. This summarises the projects, the countries in which they are located and their current status to give a general understanding of the types of projects which have been financed under the Window.

The PCW funds a wide range of enterprises covering primarily food production and processing (oil palm, rice, peanuts/sesame nutrient foods, cocoa, fruit juices, macadamia, fish and cassava) but also financial services, essential oils, information, animal feed and veterinary services. Within food production and processing, most of the products are targeting the domestic markets with only cocoa clearly going for export. This is principally due to limited competition for local quality processed products, high costs for imports (both in the form of the need for hard currency and protection from formal and informal tariff barriers) and high transport costs for export, especially of commodity products which face world market prices.

The AECF normally targets projects which are innovative and additional – ie. they would not have been undertaken by the company without the provision of external financial assistance. Whilst innovation is at a low level for truly novel products, many of the projects are introducing innovative ideas on the local level simply because of the dearth of economic activities. Similarly, the lack of alternate sources of finance and the very limited competition in most sectors means that most post conflict or fragile state countries will have very high rates of additionality.

Also included in the table below is the ownership of the individual enterprises, to determine whether the window specifically targets indigenous entrepreneurs. There is an assumption that countries which are difficult to work in will be less attractive to external investors and more accessible to local business people who have the networks and risk appetite to navigate unfavourable local conditions. As can be seen, this is highly polarised with Somaliland being exclusively the preserve of local entrepreneurs whereas West Africa operations appear more open to external investors – a factor here is also the kind of products produced, which is West Africa is heavily oriented towards high capital and scale of commodity tree crops.



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**Table 1: Summary of PCW projects, ownership and current status**

| Company Name | Country | Ownership | Project activity | Current status (April 2017) |
|---|---|---|---|---|
| Somaliland Beverage Industries | Somalia/ Somaliland | Indigenous | Juice pulp processing mainly from guavas grown by smallholder farmers in Hargeisa as an outgrower scheme, and mangoes collected from farmers in South Central. | Additional co-financing needed to purchase the juice line after the withdrawal of main backer |
| Bulsho Tv Media Network | Somalia/ Somaliland | Indigenous | Information services on better agricultural practices and opportunities to improve rural livelihoods through their free to air TV services | TV shows continue to be developed and aired despite ongoing financial issues |
| Zamzam Food Industries | Somalia/ Somaliland | Indigenous | Production of nutritional snacks based on locally grown sesame seed and ground nuts with farmers organised in an outgrower scheme | Production ongoing but sourcing groundnuts from Sudan due to drought |
| Tawakal Livestock Company | Somalia/ Somaliland | Indigenous | Purchasing of the weaker sheep and goats ('shoats') in the dry seasons, holding and fattening of the livestock through fodder cultivation and water provision, and later sale for exportation to the Haj in Saudi Arabia. | Buying operations in place but negatively affected by both drought and export ban |
| VetCare - Veterinary Service Provider | Somalia/ Somaliland | Indigenous | Sale of quality veterinary drugs and veterinary advice to pastoralists to improve livestock keeping practices and improve animal health and productivity. | Significant reach reduced recently due to large scale drought. |
| MicroDahab Limited | Somalia/ Somaliland | Indigenous | Mobile enabled microfinance – savings and loans. The objective is to offer shariah-compliant, secure, accessible and affordable microfinance services. | Largest MFI in Somaliland |
| Kaah Express Financial Services, Inc. | Somalia/ Somaliland | Indigenous | Microfinance services targeting owners of small businesses combined with business training to improve collections of repayments. | Second player in Somaliland with nationwide network for MFI operations |
| Habo Fish and Tuna Canning Factory | Somalia/ Somaliland | Indigenous | Addition of a canning line for sardines to extent the productive season of the fish canning factory and the production of fish-based silage for animal feed and/or fertilizer using mainly fish waste and by-catches. | Production facility and boats are in place but business is stalled awaiting additional working capital |
| Neo Trading Company | Somalia/ Somaliland | Indigenous | Establishment of a distilling facility for locally collected gums and resins (frankincense, myrrh) | Increase in world market price for gums and resins led to strong profits |
| Huilerie - Plantations - Élevages du Kwilu-Kwango | DR Congo | Expatriate | Establishment of an oil palm plantation and outgrower scheme in the former palm oil producing province of Kiwit. It is hoped to produce sufficient palm oil to attract investors for the development of a processing plant. | Outgrower scheme established but further investment needed for capital investment in oil palm processing |

| Company Name | Country | Ownership | Project activity | Current status (April 2017) |
|---|---|---|---|---|
| Freshco Kenya Ltd | DR Congo | Expatriate | Establishment of macadamia nut orchard and adding production through an outgrower scheme of smallholder farmers in the Eastern DRC. | Remains in the establishment phase due to insecurity and long period to maturity |
| Esco Kivu S.P.R.L. | DR Congo | Expatriate | Improved cocoa collection infrastructure in Eastern DRC to enable ESCO Ltd to purchase and export more cocoa. Small scale cocoa growers will be able to sell more and obtain better prices for their cocoa. | Highly successful buy and processing facility serving upwards of 20,000 HH |
| LAYUKA S.P.R.L. | DR Congo | Indigenous | Establishment of a cassava outgrower scheme with improved varieties and cultural methods to supply a processing plant for cassava flour for both consumption in the Kinshasa market and industrial starch more widely. | Large generator installed to overcome local power issues and potential to generate significant benefit in place |
| Liberia Cocoa Corporation | Liberia | Indigenous | Establishment of a nucleus farm and outgrower scheme for cocoa production. | Cocoa production started to scale after year 3 |
| Goldtree | Sierra Leone | Expatriate | Establishment of a network of transport operators to provide smallholder oil palm growers/owners with access to the revitalised Goldtree oil processing mill. | Significant (US$20m) third party investment has upgraded mill |
| Mountain Lion | Sierra Leone | Expatriate/ Indigenous | Production and processing (par-boiling) of rice using an outgrower scheme on both the uplands and lowlands. | Large scale production established with services added to outgrower scheme |
| Capitol Foods | Sierra Leone | Indigenous (Lebanese) | Development of a juicing plant for the purchasing and processing of smallholder grown pineapple (and potentially other fruit) into juice for local consumption and export. | Profitable juice and water bottling operations established |
| Pajah | Sierra Leone | Indigenous | Establishment of a maize outgrower scheme to secure the access to maize for chicken feed for their poultry production. | Outgrower systems established but challenges remain with establishing a viable market for both eggs and DOC |

# 2 Design of the Post Conflict Window

## Planning the Window

*Expose the approach to designing the intervention, identifying how donors treated post conflict funding – including the expectations in terms of financial and development impact, extent of due diligence required, provision, amount and form of matching funds, administrative application and reporting requirements, type of projects – including what donors were expecting to achieve in post conflict environments that they would not expect in more normal agricultural environments;*

**Background to the design of the PCW**

The AECF was originally designed to support large established agribusinesses reach smallholder farmers, generally in the context of creating or expanding outgrower schemes for small scale farmers with limited access to land and technology. The design of the Fund and the competitions upon which it selected projects was made very much with the post-colonial Eastern and Southern Africa agriculture value chains in mind – large, well developed agribusinesses working with educated smallholders in capitalist economies and with at least some access to factors of production.

The AECF had, though its first General Window (GW) also invested in post conflict and fragile states, providing funding for projects in Sierra Leone and Democratic Republic of Congo. It was experiences of the challenges faced by businesses applying from these countries that in part started the motivation for the establishment of a specific Window with different rules and approaches. In these markets, differing national development histories mean cultural and economic conditions are markedly different. Climatic conditions, crops grown and traditional markets vary from the cereal based agricultural economies where the AECF was conceived.

The adoption by Sida of the PCW was an attempt to expand the concept of investing in the private sector in fragile or conflict states to its priority areas of sub Saharan Africa which at the time were Somaliland, South Sudan, Democratic Republic of Congo (DRC), Liberia, Sierra Leone and Zimbabwe. The PCW itself was born out of the South Sudan Window (SSW) and the Zimbabwe Window (ZW). The SSW was a smaller US$4m fund established by the United Kingdom's Department for International Development (DFID) to provide grant and repayable grants to six companies in the agriculture sector. Zimbabwe was the target of a significant $16.8m Window funded by DFAT and also implemented by the AECF. Given that funding had already been provided to these two countries, they were excluded from the PCW.

**Intervention logic**

The rationale behind the establishment of the PCW was a desire to provide capital in fragile state economies that were moving out of a conflict environment but which had not yet reach the level of development of other African states. In the continent wide competitions that had been held by the AECF up to that point, less developed economies would not be able to produce the kind of elaborated or scaled proposals for investment that could compete fairly for funding. Equally, innovation is not invention and is highly context specific. Ideas that are not considered innovative in these economies would be considered innovative in more fragile states – for example, smallholder seed multiplication is standard business in Kenya but innovative in South Sudan where it has never been undertaken before.

It is important to appreciate that the naming of the *Post Conflict Window* was more an exercise in communication ('fragile state' was perceived as being too negative) rather than an attempt to define the type of country that was to be targeted. Of the selected countries, Sierra Leone, Liberia and DRC had emerged from civil war around ten years before the start of the PCW - although conflict still continued in the eastern parts of DRC. Civil war in Somaliland finished in 1991. All countries could also be classed as both less developed and fragile states – although in 2011 at the time of designing the PCW only Somalia (as a whole) and DRC were categorised as the most at risk by the Fund for Peace in their Failed State Index.

**Window Design**

The overall design of the PCW was the same as the other windows that had preceded it – a US$10m minimum donor investment with simultaneously launched country level competitions for applicants to compete with each other at the window level. Sida chose to take two 'units' for its initial US$20m contribution. Individual funding remained in the US$250K to US$1.5m range of other windows with the only significant difference being that all funds would be provided in grants rather than the previous blend of grants and repayable grants. This decision was principally based on the lack of an administrative instrument to manage returnable capital at Sida, but also reflects a perhaps realistic assessment of the extent to which collections could have been enforced. Given the dearth of alternative capital in the target countries, the Fund Manager fully expected applicants to also accept repayable grants. As an indication, the largest loan ever given by MicroDahab in Somaliland was US$2.5m so injections of even repayable grants of US$1.5m represents a significant contribution to the availability of finance.

The specific amount provided to successful applicants was, as is the usual case, determined by the Investment Committee (IC). As the Committee members obviously lack understanding of the specific financing demands of the very wide range of investments proposed to them, this is essentially a negotiation aiming to reduce financing requests and thereby make funds available more broadly, rather than an analytically based approach to improve efficiency. There has been no analysis by the Fund Manager on the effects of reducing the scale of requested funding and this is perhaps something that can be analysed more comprehensively in the future.

The PCW was also marketed to the diaspora following an assumption that this was probably the main source of investment capital for the target countries and also likely to be where many of the more economically competent nationals are located. Sierra Leone and Somalia in particular have large populations of their citizens in Europe and specifically the United Kingdom. It is possibly worthy of note that Liberian emigrees are principally in the United States and a lack of marketing directly to these people may have contributed to the lower than expected response from this country.

Within the PCW itself there was an expectation from Somaliland that they would not be able to equally compete with applicants from the other countries due to their lack of experience in the private sector donor space (in part due to the non-recognition of the country internationally that had limited aid flows). In reality, many of the best ideas came from this country and it was the largest recipient of the PCW funding. This is likely to be due to a historically strong education system, a culture promoting business and trade and an economy integrated into a regional market.

## Implementing the competitions

*Detail the approach taken by the Fund Manager to marketing the PCW and designing the competition for attracting credible applications from the more limited pool of potential grantees in the post conflict environment. Describe how the selection process differed and why, what worked and what didn't and what would be an appropriate approach in the future. Specific consideration should be given to thematic issues such as gender in the project selection process;*

**Competition Design**

Competitions were designed in the same way as with other funding windows, with national level in-country marketing efforts followed by competition launch for concept notes, review and selection and further support to applicants in the design and finalisation of business plan phases. There was some attempt to market the competitions in the UK to a diaspora population for Sierra Leone and Somaliland with the expectation that these groups of people would provide capital and business acumen. In the South Sudan window, the lack of skills, money for matching funds and, perhaps most importantly, higher character risk, led to a significant effort being made to support either emigres seeking to return home or those that had returned after the conflict had finished.

A key aspect of investing in marginal and post conflict areas is those who have the capacity, contacts and funds to realistically implement commercial businesses are often also those who have benefited from the conflict itself. Identifying potential investors, their backgrounds and the people and organisations that have enable them to get to their current positions is therefore a crucial part of due diligence – the brother of Jean-Pierre Bemba, who was convicted in 2016 of crimes against humanity in DRC, applied for funding under the PCW.

Although the competition followed the same processes as with a normal competition, there was a need to accept a lower standard of documentary evidence in some cases (in DRC it is often difficult to gather formal company documents, in Somaliland there is no accounting standards so no company has three years of financial records). It is also important to understand the background of the competency of the potential applicants in preparing applications which makes it difficult to take a blind assessment of all applications. Applicants from DRC may be French speaking and face difficulties with English in the application. The whole point of the PCW is to create a competition that enables less technically competent companies to compete, but as the different countries have little in common it is also unfair for them to have to compete between each other. In essence therefore, although the approach was common, the selection process took into account the varying backgrounds of the countries involved.

There was no consideration given to gender in the competition design and indeed this did not appear as an objective selection criteria of competition design of the AECF until much later, in the AAW R2 competition held in 2015. The challenges of attracting applications from enterprises in the countries was expected to be significant without adding a further gender lens to the process. Only one project, Neo Trading, had any involvement of women in its senior management although the early project manager for MicroDahab was female (she was subsequently relocated by the company to Nairobi as it was too difficult for her to operate in Hargeisa). In fairness to the PCW, the majority of the beneficiaries of the finance projects in Somaliland are women day traders. Clearly, there are no reasons why a post conflict or fragile state environment should not take due consideration of gender aspects, particularly as there are frequently fewer opportunities for women business people in male dominated, recently militarised societies. Although finding women entrepreneurs may be more difficult, there should certainly be a focus on value chains that benefit women or at the absolute minimum a clear analysis of the potential gender impacts from the investments. With the PCW, the majority of the investments were going to Somaliland and the majority of the agribusiness in Somaliland is livestock based, an industry traditionally dominated by men. That said, there are still market segments where women lead business, such as the camel milk trade, which could have been targeted.

**Grantee selection**

The PCW included four countries and although they were expected to compete against each other for the overall funding allocation, in reality there was an expectation that there should be investments in each country. This led to the selection of the 'least worst' project in Liberia and to some extent DRC which if the country pool had been larger would probably have been omitted. A clear lesson is to either include a greater range of countries to dilute the perception of failure, or make it explicitly clear with the donor that there is no quota or expectation that every country should have at least some projects.

The vast majority of the grantees selected are indigenous to the countries concerned. This was a specific target of the selection process but the challenging social and physical environments also limited the number of foreigners working in these locations. The lack of formal financial information on companies in many of the PCW countries meant that, more than in other windows, the selection process was based around an evaluation of the individuals behind the enterprises rather than the enterprises themselves. With an implicit desire to fund locally well connected individuals and companies rather than well presented on-message imports, the Fund Manager put in more work to present the strengths of the individuals and the IC more effort to interrogate the individual and trust their instincts on the human aspect.

Short-listed grantees were, as is usual with the challenge fund model, provided with advisory support to develop their business models. For PCW this support was greater than normal to address capacity issues in the applicant companies and also to fit the kind of business models being proposed into the financing model of the AECF. Many of these struggle to fit into the traditional design of working with smallholders and so work was needed to translate the investment needed into an impact on poor people to make the application fit into the funding requirements. This is not uncommon across the AECF where targeting market system change with innovation may not generate immediate benefits for the target group but they will potentially benefit in the longer term as innovation cascades through the value chain.

In fragile states generally, including not just the PCW and SSW but also countries such as Mozambique, the AECF is often funding companies that are introducing novel (for them) approaches and business models. They tend to face very specific local management issues – corruption, local taxes, human resources, infrastructure - so it is difficult for an assessing sector specialist to make an objective determination of the likelihood of business success or to compare the performance of the model elsewhere with the applicant country. It is very important to recruit both sector and country specialists into the assessment and due diligence teams to provide as much credible analysis as possible.

## 3 Experiences of the Fund Manager in implementing the Post Conflict Window

*Outline how the Fund Manager's management of grantees varies, including acceptance of differing standards of reporting and accounting, levels of due diligence and the provision of additional guidance by the Fund Manager to grantees;*

In the pre-contract due diligence phase the Fund Manager identified areas of weakness where either greater flexibility had to be adopted or advisory support provided (principally in *ad hoc* accountancy and financial management through staff visits). This gave a clear understanding of expectations for reporting quality and resources were targeted towards individual grantees accordingly. Whilst there were not, officially, differing levels of standards between PCW grantees and those in other parts of the AECF, there was a realisation of what was possible to expect and an acceptance of lower standards than elsewhere in the portfolio.

The Fund Manager is required to visit each grantee twice per year to oversee their reporting and performance obligations. Difficulties in physically accessing some areas led to increased costs and the use of external consultants but quality issues in reporting can usually be addressed by the use of a standard reporting template and training. Where the window manager cannot get to a project however, it tends to suffer from a lack of management sight. Management problems and the whole relationship with HPK may have been improved if the window manager had been able to have more of a hands on relationship with the grantee in their place of business. A regional HQ in Hargeisa would have helped in especially the cross cultural understanding of a very different place to where the AECF usually works but given costs and the scale of funding, was never likely to be a practical option. The AECF works in 24 countries and cannot have offices in all of them. A regional office in West Africa (based out of an operational office of KPMG in Accra from where these projects are managed) enabled some commonality of management approach for all AECF projects in this region, but it was important for the window management team to also regularly visit projects to get an overall perspective of how the window was performing.

The PCW was established to address a perceived lower competence in competing for funds across the continent, but there is also a great variation in competence between the four countries of the Window. It would have been more logical to include the management of the West Africa projects in with other non-PCW projects in the region as the management issues in Sierra Leone are more common to Senegal, Mali etc than they are to Somaliland.

**Appetite towards risk**

Working in risky places requires a softer set of skills from the Fund Manager and a greater tolerance of risk from the donor. Institutions usually react to risk by increasing the amount of controls that they put in place and reducing the amount of funding that they commit to minimise the effects when things go wrong. The result of this is that it becomes very hard to mobilise money and the impact achieved when funds are finally mobilised is limited, especially when compared to the costs of management. The PCW has been implemented with a higher than normal tolerance for risk matched by careful project selection and pre-screening. The AECF selection process has a very human face – the IC is very experienced and the due diligence team of the Fund Manager well versed in generating subjective as well as objective assessments of the company, but more importantly the individuals who apply. The PCW selection process, more so than with other windows, is based on gathering what information and intelligence is available and then 'going with the gut'. In supporting this, the AECF has been fortunate to have a donor who was both trusting and brave and who understood that the potential upside from mobilising large amounts of funding outweighed the risks of individual project failure.

In many ways, the PCW is actually a lower risk portfolio than other windows that invest in more stable environments. As the only provider of investment finance at scale in many instances, it can select the very best of the offerings available from the private sector. It has also led to the selection of companies that have established presences in the countries concerned, which is critical at being able to navigate the social and economic landscape for business success. Even those companies not run by indigenous citizens had very long associations with the country, usually over more than one generation. Picking this low hanging fruit has generated a portfolio which has performed extremely well, with no instances of fraud and with performance concerns around only two projects in the portfolio (HPK in DRC and Habo Fish and Tuna in Somaliland).

## Updating Risky Business – promoting private sector development in fragile states – the Fund Manager's early experiences

The following chapter seeks to update some of the preliminary findings from an earlier study prepared by the Fund Manager in mid 2013 based on its initial experiences from the implementation of both the SSW and the PCW. It was written as the SSW and PCW were recently contracted and highlighted key aspects that had affected the competition process and were expected to influence implementation.

- *Informal private sector with capacity constraints*: With potential grantees often lacking formal corporate or financial systems, the Fund Manager has developed a more active management approach to provide alternative, context specific, administrative oversight that relies on a subjective assessment as well as available formal documents;

This has remained a key issue throughout the implementation of the PCW and the Fund Manager has both developed mechanisms to base assessments on more subjective criteria but also provided support to improve the capacity within grantee companies, particularly in accounting. In some instances, this has been of great benefit to companies who have learned that an audit process helps them to understand how their business works, but in others where there is less management will to implement modern accounting systems the interventions have been less successful.

- *Dealing with insecurity*: The Fund Manager reviews the plausibility of the business plans in the light of expected security issues, including existing evidence of the ability of the applicant to adapt to local security issues. In terms of management, additional consideration is given to risk assessment and the costs of managing projects in highly risky areas;

Insecurity has been a recurring issue in some areas of Somaliland, especially outside Hargeisa during the drought over the last two years. This has made it increasingly difficult for non-Somalis and even non-clan members to visit affected areas and has precluded the use of field verifications. In DRC, the changing security picture has meant that visiting projects has been irregular and also often contracted out to local consultants. This has had some negative consequences for the results measurement and makes due diligence and oversight challenging, but also further highlights the importance of providing capital in these places.

- *Fewer alternatives for financing:* Lack of formal financing systems, including the use of property as collateral means that potential grantees are usually short term trading companies rather than longer term investors. The Fund Manager has put a greater emphasis on the provision of investment funds in the form of grants, more funds up front to cover establishment capex and a broader definition of matching funds. Consideration should also be given to follow up funding, given the lack of alternative sources in post conflict environments;

The majority of projects required up front capex financing and this also required more trust than usual on the part of the Fund Manager – there is little recourse or leverage if things are not going as well as expected. In a number of instances, the PCW disbursed very large amounts of money for capex and the final results have yet to be achieved. More consideration needs to be given to directly funding suppliers or other mechanisms to retain control or oversight over capital assets until the benefit for poor people can be seen to be being achieved.

There were no top-ups or additional financing made available to companies in the PCW principally due to the change in funding priorities of the donor. The idea to continue financing businesses identified after lengthy selection processes and where the full sight of investment needs are rarely known in advance, makes logical sense. There are aspects of additionality that need to be addressed and the concept of top up funding more systematically across the AECF has yet to be well embedded. Of greater importance perhaps is a clear understanding of the need for subsequent financing rounds and a more specific objective of using the knowledge and experience of the AECF to de-risk and bring other financiers, such as impact investors, into the fragile country space.

- *Understanding the links between PSD investment and political and social issues.* External investment can be both a positive and negative factor in the peace process, providing employment or emphasising divisions between communities. The Challenge Fund is a particularly blunt instrument in this regard as there are limited funds to do the kind of detailed ex ante analysis that would identify these issues. With a limited pool of potential applicants, it may be hard to avoid local actors who have less than white roles in recent political and economic events.

By selecting a relatively limited number of companies in each country and working on the basis that with an almost complete lack of private sector funding at scale the AECF could pick the best opportunities, these concerns have been avoided. It has, however, taken some due diligence and recruitment of local knowledge to do so and in very challenging markets such as South Sudan the only practical approach is to bring in émigré investors. If funding scale or scope were to increase and therefore a greater number of investees needed to fulfil the donor funding it is likely that a much more comprehensive due diligence process would be needed. The AECF approach has worked, but it is clear that every country is different and there is no standard method that can be promoted.

## 4 Measurement of Results

*Compare and contrast how results and impact are measured in post conflict environments by the Fund Manager and the challenges faced with both effective reporting and measurement of results and impact.*

The results of the AECF are recorded through an aggregation of the performance of all of the projects that are funded. It is therefore critical that all projects across all windows follow the same results measurement mechanisms and standards.

The Fund Manager in principle did not develop different results measurement tools for the PCW and in fact subjected the window to the same level of additional research and diligence as the Africa Agribusiness Window until funds were curtailed due to Sida strategic planning reasons. All projects were subjected to additional results measurement work, which included desk based results verification. High impact projects have been studied through field verification surveys and a number of projects (Escu Kivu in DRC, Century Seed in South Sudan and Capitol Foods in Sierra Leone) were also included in the longer term impact study implemented by the external Evaluation Management Unit.

Post conflict and fragile states do however offer different challenges for results measurement. The second stage of the Evaluation Management Unit RCT for Century Seed could not be undertaken because the country returned to violence. But even if there had been stability, the nascent market for the business model being developed was such that it had to completely change for the company to find an approach that worked. This is perhaps a risk for any innovation scheme and has certainly occurred in other areas of the portfolio and is one of the reasons why the AECF is moving away from these assessment methodologies.

For desk based results measurement, there are generally fewer secondary sources for the business models being implemented to be able to generate an objective estimate of development impact. This includes also the lack of government statistics that support the analysis – market prices are recorded for a range of products throughout Kenya on a weekly basis, but this information is much rarer in Somaliland and Sierra Leone.

It is also more difficult to physically get to project locations to measure or verify benefit. Visas for DRC can take months to arrange and many parts of the country become seasonally impassable for long periods of time due to rain. Female staff find it difficult to work effectively in Somaliland. Security becomes a more pressing issue in many parts of the operational area – KPMG was quoted US$70,000 for protection to visit one grantee in Puntland, hence they have never been visited by a staff member. To address these issues, the Fund Manager has made extensive use of independent consultants to support permanent staff. This can be a pragmatic solution and may bring more technical competence but requires results measurement methodologies to be consistently applied and this can be difficult to achieve.

Results reporting at the AECF relies substantially on the self reporting by grantees and this naturally varies tremendously across the portfolio, including across the PCW. Many investees do not have the technical or language capacity to be able to submit reports with sufficient detail. The emphasis of the Fund Manager on financial performance over results performance is at the heart of this and is reflected in the use of principally financial staff, rather than development professionals, to manage the Fund. The AECF provides guidance and training to companies in results measurement but it remains something of an external skills competency to them. Companies throughout the portfolio are principally interested in their business performance rather than their development performance and it is one of the great weaknesses of the AECF that these two concepts have not been brought closer together – although significant efforts in this regard have been made since 2015.

Where the Fund Manager seeks clarification of key metrics through external research or field surveys, there is frequently only limited capacity locally – although this is in the process of improving due to the presence of aid agencies that have an increasing interest in evidence based measurement. To get around this issue, the Fund Manager seeks proxy indicators from other areas where information may be more available (the use of pastoralist data from northern Kenya or Ethiopia for Somaliland for example) or to sense check information reported by the business.

The light touch reporting of the AECF captures the financial performance of companies and generates an objectively based assessment of the impact on the target populations but does not capture many other qualitative benefits. Especially in a fragile state environment where economic opportunities for investors and potential employees are even more limited than elsewhere in sub Saharan Africa, the contribution of substantial investment in the private sector to regulatory reform, institution building, peace building and community stabilisation and indirect economic and employment effects can be tremendous. Investment in cocoa processing facilities in DRC allowed thousands of people to begin earning incomes within three months of returning from refuge in Uganda. Financing the establishment of micro finance in Somaliland has led to the establishment of a regulatory infrastructure that works towards resolving issues of terrorist financing. Establishing a par boiled rice processing facility in Sierra Leone reduces diabetes in a population that heavily consumes white rice.

## 5 Conclusions from Fund Manager perspectives on managing challenge funds in post conflict and fragile states

- The Fund Manager has implemented projects in post conflict and fragile states both under the specific PCW and also under national Windows (such as Zimbabwe) and within the context of broader geographical windows (such as in Mozambique in the Africa Agribusiness Window). All competitions have followed the same structures and rules, but with an implicit increased flexibility in the quality of deliverables for those under the PCW.
- The key benefits of having a specifically 'post conflict' approach when working in fragile states is that there is a clear inference of higher risk and higher rewards that is accepted by all parties, in particular donors. This may also mean that funding comes from different sources within the donor with different performance and reporting standards that may make it more appropriate to the fragile state environment.
- The Fund Manager has taken on different risks in both grantee selection and programme management to other windows, but has also benefited from a reduced level of competition for funds from the companies that are operating in the target countries. There is a limit to the amount of due diligence that a fund manager can undertake in the context of competitions managed remotely, but recruitment of local knowledge to the process is essential. A fund seeking larger numbers of companies would be much more likely to start encountering more marginal enterprises and individuals that would significantly increase risk.
- The lack of information on companies and systems for generating market intelligence means that the selection process is based more on the individual leading the firm and subjective assessments from the IC. This requires experience of reading people over researching facts and a donor willing to invest based on fewer objective criteria. Despite this, there have been very few instances of companies not performing as expected – although even more broadly across the AECF portfolio fraud is extremely rare.
- Companies even in less developed economic spaces have good ideas and are able to generate credible proposals so whilst the interpretation of rules and conditions may not be as rigorous as with other competitions, the standard approaches of the challenge fund can be applied. However, both the Fund Manager and the IC (and to some extent the donor) need to have the experience to make subjective analysis based on human factors.
- Donors supporting investment in fragile states need to be brave, understanding that risks may be high but the potential upsides in economies almost entirely starved of

investment funds can be considerable. They will frequently need to change their normal risk and performance management procedures and need to have confidence and faith in the Fund Manager's professional capacity to manage risk and make human based assessments. Sida has been an ideal donor in this regard but this may also be due to their change in strategic objectives that left the AECF as something of an institutional orphan. DFID, by contrast, was still following up with the AECF in 2017 on relatively minor financial losses incurred by Century Seed three years before when farms were pillaged by armed militias in South Sudan.

- There was merit in having a PCW to address the issue of creating a more level playing field between applicants by having a specific competition for 'less developed' countries, but it should also be clear that there are differences between these countries. Grouping countries by poverty level does not necessarily group similar countries and so this approach may not be successful in actually levelling the playing field. Competition focus needs to come down to the local level.
- Fragility and the ability for the private sector to function is principally on a sub-national level. Vulnerable groups may not have the same consideration for borders and may continue to use traditional or tribal areas especially for pastoralists. Care must therefore be taken to really understand the specific development issues and challenges in the target areas.
- The wide variations between the countries of the PCW and indeed within the countries meant that there has been no real collaborative or collegiate effort between grantees to exchange information or work together. In those areas such as financial services in Somaliland, this has happened in areas such as the development of industry regulation but it could have been more comprehensive. This might be to do with tribal allegiances or it could be due to the limited management funds available to promote alumni networking.
- In terms of implementation, the PCW/SSW has been substantially affected by external factors – war in the case of South Sudan and DRC, Ebola in the case of Sierra Leone and drought in the case of Somaliland. The fragility of the national institutions, infrastructure and economies of these countries exacerbated the effects of these external factors and as such, managing these projects in the context of a specific window with reduced standards for reporting, greater leeway on operational performance and a brave and resilient donor has been appropriate.
- Success in these areas is hard fought but when it is successful – as in the case of Esco Kivu which is now buying from 35,000 farmers due to AECF investment in processing and storage facilities – it has tremendous impact in changing how market systems work for the poor. Many of the qualitative benefits, such as the peacebuilding effects of incomes and employment are not captured by the results measurement systems.