

Private Sector Development Synthesis Note

Matching Grant Schemes & Systemic Approaches for Private Sector Development: Differences & Complementarities

Introduction

Matching Grant Schemes and Systemic Approaches are both used increasingly in private sector development; the DCED is an umbrella organisation for both. **They can look similar on the ground, where both use ‘partnerships’ in the form of a matching grant** to an individual company to stimulate investment and change. Yet practitioners of the two approaches generally have **different world views**. This Note explores the implications, covering both differences and complementarities.

Definitions

- The Matching Grant Schemes referred to in this Note include challenge funds and other mechanisms that have clearly defined strategies for sharing the costs and risks of private investments in a developing country, based on proposals from businesses. They are a **common form of initiating partnerships** with the private sector, and are frequently referred to as ‘*Partnership Mechanisms*’.
- In the PSD community, Systemic Approaches or *Market System Development programmes* aim for sustainable improvements in the systems in which the poor live, through catalytic interventions. **Market Development interventions can include a wide range of activities**, based on a thorough analysis of market failures and weaknesses. For example, they may combine technical assistance, brokering, business environment reforms and a matching grant.

World Views

- Matching Grant Schemes use partnerships as a **strategy** – partly to enhance efficiency by topping up aid budgets with matching funds from business. Building on business initiative is further justified by the argument that businesses know their markets best, and are most creative in coming up with new ideas; they can “get things done” in settings where implementation partners are hard to find.
- Systemic Approaches use partnerships as a **tactic or tool**, among many other options to address the underlying causes of underdeveloped markets. They assume that development workers are best placed to understand the market and to develop an over-arching strategy to enhance its working. The end-game is generally to crowd in competition so that poor consumers and producers get a better deal.

Starting points

- Matching Grant Schemes **invite businesses to submit their new business ideas** to a ‘window’ that is receptive - within some defined filters. The design of the individual partnership depends largely on the market knowledge of the proposing business. The public partner performs due diligence on the business and its business plan – but **does not conduct its own market research** in each case to understand the logic, or to develop its own, wider strategy.

- Systemic Approaches start differently; the publicly-funded agency carries out its own **ex-ante analysis of a market or sector**, and uses it to develop its strategy. This strategy defines the roles and activities of the public sector; it **may or may not show that the tactic of a partnership is likely to address a binding constraint in the market**. If it does, the agency then **searches pro-actively for the right private partner** to stimulate change, e.g. introducing a new business model that could ultimately be copied by other companies. If it can, it persuades the private partner to collaborate.

Partner companies

- Matching Grant Schemes frequently **limit their flexibility in terms of possible partner companies ex-ante**, e.g. through rules regarding their size and origin; in some cases the criteria are at least in part politically influenced and not only driven by effectiveness considerations: Out of 14 centrally-funded mechanisms reviewed, 5 are officially tied, at least partially, to partner companies from the donor country. They may thereby **lower their chances of finding the most suitable partners to stimulate systemic change**.
- Systemic Approaches are **flexible in this regard**; partner companies can be local or international, small or large, depending on an analysis of suitable partners to address identified market weaknesses.

Implementation and Management

- **Implementation often looks similar**, with a legally-binding agreement up-front, usually involving a matching grant or cost-sharing. That cost-sharing may be 50% or more; even in Systemic Approaches. Their share may be higher especially when working in shallow, early or fragile markets – although always with the justification that it may trigger wider change.
- Systemic Approaches, however, would also often involve **complementary activities** outside the collaboration, such as advocacy for improving the business environment through other partners, etc. whereas partnerships supported by Matching Grant Schemes are usually free-standing.
- Both approaches are subject to competing pressures: to achieve rapid, large-scale and predictable change with high additionality (implying a large public contribution) while at the same time achieving a high degree of leverage (implying a small public contribution).
- **Management by the implementing organisation looks very different**; in a Matching Grant Scheme, it is typically light-touch, arms-length, and primarily about the performance of the business. In a Systemic Approach, management is hands-on and responsive to performance data. The implementing agency often conducts research around the activity to understand the development implications and thinks continually about how to go beyond the immediate context, to leverage wider change and consider how the experience of one business can be used by others.
- All of this implies that **staffing costs** of the implementing agency are generally **higher in Systemic Approaches** than in Matching Grant Schemes

Finishing Points

- The different starting points mean that, by the end of the collaboration, the public partner is in a **very different position in the two approaches**.
- In a Matching Grant Scheme, the public partner concludes the partnership, measures and reports the results, and moves on. There is usually no agreement within the partnership that the intellectual property produced can be shared more widely; there are also not enough staff in the implementing agency to stimulate the replication.
- In a Systemic Approach, on the other hand, the implementing agency already has a plan to assess and adapt the experience, and to expand and replicate it with other companies in the market.

What is the potential for the two approaches to converge?

The review of similarities and differences between the two approaches indicate that there is probably room for greater synergies. The following actions could allow donors and implementers to achieve these.

For Matching Grant Schemes, enhancing the ability to achieve systemic change seems to depend to a large extent on their **capacity to undertake analysis and other Market Development activities**.

However, even within the current capacities of Matching Grant Schemes, some relatively **modest changes could already help them exert more influence on market systems**. These include:

- Paying attention to the appropriate wording of partnership agreements, and what that allows in terms of the use of Intellectual Property; this is not always easy, as businesses normally prefer a contract preventing the public partner from crowding-in competition, even in the medium term.
- Documenting successful business models in a systematic way, that enables other companies to copy the approach (if the original contract allowed that), and raising awareness through outreach events, company visits etc.
- Encouraging and supporting partner companies to engage in national Public Private Dialogue around reforms to the business environment
- Using a Matching Grant Scheme to catalyse growth and mitigate binding constraints to private sector activity in a specific sector or cluster (e.g. through technology transfer, new infrastructure, or positive effects on supporting industries). This can be facilitated by working through specialised funding windows or calls for applications.
- Exploring ways in which centrally-funded schemes could be used to respond flexibly to the needs identified by Market Development programmes.

At the field level, **additional activities could focus on**

- training implementing staff of Matching Grant Schemes in Market Development
- establishing regional/ local Matching Grant Schemes where these would be useful to complement sector strategies which follow a Market Development approach
- using Market Development programmes to complement existing partnerships in ways that would also benefit other companies in the market, e.g. by developing support services, promoting demand for a specific product, or supporting business environment reform efforts by partner companies
- bringing together practitioners of matching grant schemes and market development programmes to exchange on effective practices in due diligence and business plan assessments, partner negotiations etc

Conclusion

Although Matching Grant Mechanisms and Systemic Approaches look very similar on the ground, they start and end in very different ways. Given that both approaches are supported by donor agencies, sometimes even in parallel by the same agency, there seems to be **clear scope for enhancing their complementarity** as well as **incorporating the lessons of systemic approaches into the design of matching grant mechanisms**.