ICAI Independent Commission for Aid Impact

Business in Development:

DFID's work to stimulate private sector contributions in development

Terms of Reference

1. Introduction

1.1 The Independent Commission for Aid Impact (ICAI) is the independent body responsible for scrutinising UK aid. We focus on maximising the effectiveness of the UK aid budget for intended beneficiaries and on delivering value for money for UK taxpayers. We carry out independent reviews of aid programmes and of issues affecting the delivery of UK aid. We publish transparent, impartial and objective reports to provide evidence and clear recommendations to support UK Government decision-making and to strengthen the accountability of the aid programme. Our reports are written to be accessible to a general readership and we use a simple 'traffic light' system to report our judgement on each programme or topic we review.

1.2 In May 2014, we published a review of the Department for International Development's (DFID's) private sector development (PSD) work.[1] The report focussed on DFID's efforts to stimulate the growth of the private sector in developing countries.

1.3 In this review, we will examine how DFID is working with and through the private sector to achieve a range of development objectives that deliver a positive impact on the poor. We will consider how DFID engages with both UK and foreign firms at the global and country levels.

1.4 These terms of reference outline the purpose and nature of the review and identify the main themes that it will investigate. A detailed methodology will be developed during an inception phase.

2. Background

2.1 Businesses can have an impact on the poorest people in developing countries in a number of ways. They can act as employers of the poor or purchase the goods the poor produce. They can also supply basic goods and services which meet the needs of the poor. There may be spill-over effects, both positive (such as through the dissemination of knowledge and technology) or negative (including through environmental degradation or competitive pressures on enterprises owned by the poor). Many larger firms have corporate social responsibility (CSR) programmes which aim to help the poor.

2.2 DFID has placed increasing emphasis in recent years on the importance of PSD for human, economic and environmental development and humanitarian assistance. In 2008, partly in response to a report issued by the International Development Committee of the House of Commons, DFID published its strategy for PSD, *Prosperity for All: Making Markets Work*.[2] In

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1 *DFID's Private Sector Development Work,* ICAI, May 2014, http://icai.independent.gov.uk/wp-content/uploads/2014/05/ICAI-PSD-report-FINAL.pdf.

2 *Private Sector Development Strategy: Prosperity for all: making markets work*, DFID, 2008, http://www.enterprise-development.org/page/download?id=1727

The Engine of Development,[3] published in 2011, DFID reaffirmed the importance of working with the private sector:

- 'We know that there are investment opportunities in the poorest countries and that there are returns to be made.
- Driving up investment opportunities in the poorest countries is a crucial part of delivering poverty reduction.
- By catalysing more private investment and deepening private sector links into communities we can multiply the reach of the private sector and increase opportunities for poor people.'

2.3 DFID went on to state that its own work on PSD would follow two main approaches:

- engaging with firms directly and indirectly; and
- transforming the environment in which firms operate.

2.4 *The Engine of Development* gave a number of examples of how DFID was working with the private sector, including: training small farmers to use fertiliser products produced by a Nigerian company; working with farmers to enable Diageo to start sourcing locally in Cameroon; collaborating with Unilever and others to design and market portable toilets in Ghana; and training Rwandan farmers to deliver tea of the right quality for Betty's of Harrogate.

2.5 In 2011, DFID also created the Private Sector Department in order to help raise the level, extent and effectiveness of DFID's engagement with the private sector. Its purpose is to 'help increase awareness and capability across DFID's country offices and other departments on how to work with the private sector to build prosperity and eradicate extreme poverty'.[4] DFID's focus on PSD has continued to increase. In March 2013, the Secretary of State gave a speech at the London Stock Exchange, in which she set out her vision for an increased emphasis on economic development within DFID. In particular she stressed the importance of:

- 'Firstly, reducing overall barriers to trade and investment – whether regulatory, infrastructure, legal or institutional;
- Secondly, unlocking the ability of entrepreneurs and business people in developing countries to themselves drive economic growth through their own businesses being more and more successful;
- Thirdly and critically, I believe it also means greater investment by business and I want to see UK companies joining the development push.'[5]

2.6 In January 2014, DFID published its Economic Development Strategic Framework.[6] The Framework is designed to give new impetus to DFID's ambition to promote economic development as a key mechanism for delivering growth and poverty reduction in the developing world. It sees private sector investment and growth as central to success and is built around five pillars. Pillars 3 and 4 are directly relevant to this review, while Pillar 5 is a key cross-cutting priority:

- Pillar 3: catalysing capital flows and trade in frontier markets;
- Pillar 4: engaging with businesses to help their investments contribute to development; and
- Pillar 5: ensuring growth is inclusive and benefits girls and women.

2.7 Under Pillar 3, DFID includes 'increasing private investment into poor countries, regions and sectors, with a focus on high growth sectors to support economic transformation' including 'impact investment'.

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[3] *The Engine of Development: The private sector and prosperity for poor people*, DFID, 2011, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/67490/Private-sector-approach-paper-May2011.pdf.
[4] *The Engine of Development: The private sector and prosperity for poor people*, DFID, 2011, page 4, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/67490/Private-sector-approach-paper-May2011.pdf.
[5] *Investing in growth: How DFID works in new and emerging markets*, Justine Greening, March 2013, https://www.gov.uk/government/speeches/investing-in-growth-how-dfid-works-in-new-and-emerging-markets.
[6] *Economic development for a shared prosperity and poverty reduction: a strategic framework*, DFID, January 2014, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/276859/Econ-development-strategic-framework_.pdf.

2.8 Under Pillar 4, DFID spells out specifically how it would work with businesses to promote development. In summary, this includes:

- encouraging and supporting businesses to invest more and more responsibly in poor countries as part of their core business strategy and specifically:
  - helping companies looking to invest in frontier markets, by providing information and advice, for example, through support for International Finance Corporation (IFC) Foreign Investment Advisory Services; and
  - pushing for businesses to be more accountable to the people whose lives are affected by their decisions, for example, through the adoption of responsible business practices.
- promoting business investment in upgrading supply chains to benefit the poor through:
  - local sourcing;
  - improving local working conditions, for example, through the Trade in Global Value Chains Initiative;[7] and
  - improving skills and health.
- supporting business innovation to develop solutions to development challenges, such as products and services for the poor;
- initiatives to crowd in solutions to development challenges using technology, for example through the Amplify programme;[8]
- encouraging businesses to apply better standards in their work, through:
  - voluntary standards systems; and
  - alliances of businesses.
- involving businesses in policy debates and strategic partnerships, for example, Unilever, the G8 Nutrition for Growth and the London Stock Exchange.[9]

3. Purpose of the review

3.1 The purpose of this review is to assess how DFID engages with businesses to achieve its objectives and to benefit the poor. We will consider DFID's objectives in engaging and partnering with businesses, the ways in which it is seeking to achieve those objectives, what impact it is having on the poor and how well DFID is learning through its interactions with business and disseminating good practice.

3.2 The review will focus on five core questions. More detailed questions relating to the four core ICAI themes of objectives, delivery, impact and learning are outlined in Section 6. The core questions are:

- What opportunities exist for DFID to work through private businesses to achieve pro-poor developmental benefits while also being of commercial benefit to businesses?
- To what extent do DFID's strategy and objectives demonstrate an understanding of these opportunities?
- How effectively is DFID seizing opportunities to engage with businesses, including catalysing additional private investment?
- What is the incremental impact on the poor that DFID is able to achieve through working with businesses?
- What is DFID doing to learn more about the potential for working with businesses?

[7] This initiative works with businesses to improve the skills, health and working conditions of workers and smallholder farmers.
[8] Amplify is an online innovation platform designed to 'crowd in' solutions to development challenges from around the world.
[9] *Economic development for a shared prosperity and poverty reduction: a strategic framework*, DFID, January 2014, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/276859/Econ-development-strategic-framework.pdf.

4. Relationship to other reviews

4.1 This review will examine how DFID works directly with individual businesses and through private sector partnerships, both internationally and at the country level, to achieve development outcomes which benefit the poor. This includes both UK and foreign owned businesses.

4.2 This compares with our earlier review of DFID's PSD work, published in May 2014, in which we examined 'the rationale for, viability of and coherence of DFID's PSD approach and portfolio'.[10] That report focussed on DFID's efforts to stimulate the growth of the private sector in developing countries. It recommended that DFID should clearly articulate where it can add most value in PSD relative to other stakeholders. There is some potential overlap with this report, specifically where DFID seeks to use its influence with businesses to stimulate wider private sector growth. Our earlier report also recommended that DFID needs to work harder to understand the barriers and business imperatives faced by the private sector in developing countries; so opportunities for DFID to learn through its interaction with businesses, in order to guide its PSD approach, are also relevant to both reviews.

4.3 ICAI's first review of DFID's PSD work also touched on DFID's support for 'patient' or 'returnable' capital, which covers lending to or investment in private enterprises at concessional rates. A significant part of DFID's engagement with the private sector is undertaken indirectly by development finance institutions (DFIs), such as the Commonwealth Development Corporation (CDC), funded in part by DFID. The National Audit Office (NAO) plans to review CDC during 2015. DFID also invests in the Private Infrastructure Development Group (PIDG), which was the subject of a recent review by the NAO.[11] We will, therefore, not cover the operations of CDC or PIDG in our review in detail, except insofar as they manage funds on behalf of DFID, such as the Impact Investment Fund, or otherwise act as a conduit for DFID business engagement initiatives.[12] Other impact investment funds managed by country offices, such as the Delhi office, may form part of the current review.

4.4 ICAI will also be reviewing DFID's engagement with multilaterals more broadly as part of a separate review due to be published in the second quarter of 2015. Much of DFID's work with the private sector is undertaken through the IFC, which is part of the World Bank Group. We will, therefore, coordinate our review with this review to avoid overlap or omissions.

4.5 The IDC has announced an inquiry into jobs and livelihoods.[13] Some aspects of the inquiry cover similar ground to the areas outlined above. For example, the inquiry intends to establish: 'whether DFID has sufficient engagement with the private sector in developing countries and elsewhere to understand its priorities and its views on the role of development agencies in creating sustainable jobs and improving livelihoods'. We will, therefore, coordinate with the IDC to minimise any potential overlap.

5. Analytical approach

5.1 This review will look across funding streams at the way in which DFID and the UK Government work with businesses to leverage greater development impact. We will adopt a cross-cutting approach, rather than focussing on a particular portfolio of DFID programmes or funding allocations. We will be looking at the various mechanisms through which DFID engages with businesses, including:

[10] *DFID's Private Sector Development Work*, ICAI, May 2014, http://icai.independent.gov.uk/wp-content/uploads/2014/05/ICAI-PSD-report-FINAL.pdf.
[11] *Oversight of the Private Sector Infrastructure Development Group,* NAO, July 2014, http://www.nao.org.uk/wp-content/uploads/2014/07/Oversight-of-the-private-infrastructure-development-group.pdf.
[12] A major review of DFID's financing of private sector development work was undertaken by the House of Commons International Development Committee and published in February 2014. The report requested further information on DFID's Impact Investment Fund, managed on its behalf by the CDC. According to the Government's response to the IDC's question, 'CDC will invest up to £75 million of DFID capital into up to seven impact investment Funds over 13 years. Investments to the Funds can be made in the form of debt or equity. In turn, these Funds will invest into transformative enterprises that directly target the poor as consumers, workers or suppliers. The DFID Impact Fund aims to reach at least five million poor people in Sub Saharan Africa and South Asia.'
[13] http://www.parliament.uk/business/committees/committees-a-z/commons-select/international-development-committee/news/jobs-and-livelihoods-tor/

- loans, equity, guarantees and hybrid investment into businesses (known as returnable capital) including funds managed by DFID's Delhi office and PIDG;
- challenge funds (including RAGS, FRICH and Girls Education Challenge Fund); and
- other business engagement (including multi-stakeholder partnerships, such as the New Alliance for Food Security and Nutrition, but also bilateral relationships with individual businesses).

5.2 In each instance, we will be assessing the degree to which DFID is able to achieve pro-poor development outcomes through businesses' direct impact, including, for example:

- as an employer;
- as a purchaser of goods and services supplied by the poor (for example, agricultural products);
- the provision of goods and services to the poor; and
- CSR programmes which benefit the poor.

5.3 We will also examine how DFID increases the indirect benefits to and minimises the negative consequences for the poor of business activities and investment, for example through:

- pro-poor competition;
- knowledge and technological spillovers; and
- good governance.

5.4 We will be looking both at how well DFID currently recognises and takes advantage of these opportunities and how it could do more in the future. The focus on what else DFID could do, as well as on private sector leverage, are the main elements that will distinguish this review from other ICAI reviews and, in particular, from the previous review of DFID's PSD work.

6. Indicative questions

6.1 This review will follow the standard ICAI assessment of four key areas: objectives, delivery, impact and learning. A detailed methodology will be developed during the inception phase, which will give further detail on assessment questions and the methods that we will use to answer them. Questions will be applied, however, to each of the three core mechanisms outlined in Section 5 and may include the following:

6.2 Objectives

6.2.1 Are DFID's objectives in working through the private sector:

- relevant in the light of its broader objectives; and
- consistent with wider portfolio and national objectives?

6.2.2 Are DFID's business engagement and private sector leverage objectives:

- underpinned by evidence;
- responsive to the business context; and
- based on consultation with the poor?

6.2.3 Is it clear:

- how the achievement of DFID's objectives will ultimately have a positive impact on poor people; and
- whether the assumptions have been articulated and/or any prejudicial impact for the poor mitigated against?

6.2.4 Should DFID have additional objectives in this area which it has not articulated?

6.3 **Delivery**

6.3.1 Have DFID's objectives been translated into actionable plans?

6.3.2 Are there better ways of achieving DFID's objectives than the ones which it is implementing?

6.3.3 How well does DFID engage with the private sector to support pro-poor development?

6.3.4 How effectively is DFID working with UK Trade and Investment (UKTI), the Foreign and Commonwealth Office (FCO) and other departments in the area of corporate engagement?

6.3.5 How effective is DFID as a Board member or shareholder in intermediary funds or other organisations that seek to leverage pro-poor private investment?

6.4 **Impact**

6.4.1 Where and how has the UK Government's work with the private sector had a positive impact on the poorest people?

6.4.2 Is DFID maximising the positive impact it is having on the poor?

6.4.3 How much additional private investment by beneficiary firms is DFID leveraging as a result of its work with those businesses?

6.4.4 How much additional pro-poor finance is DFID leveraging as a result of demonstrating the success of its returnable capital to other investors?

6.4.5 What are the barriers to achieving greater impact?

6.4.6 Has DFID effectively mitigated against any potential negative impacts on the poor as a result of businesses' activities?

6.5 **Learning**

6.5.1 Has DFID commissioned evidence on what works in this area and then translated that into action?

6.5.2 How well is DFID listening to and learning from businesses?

6.5.3 How effectively is DFID weighing the possible negative impacts of engaging businesses in pro-poor development (for example crowding out, conflict of interest and market distortions) against the positives?

6.5.4 How does DFID assess whether the steps it has taken are resulting or are likely to result in benefits for the poor?

6.5.5 Is there evidence of real learning and sharing of insights internally within DFID and dissemination of good practice across the private sector?

7. Methodology

7.1 The methodology will consist of the following elements:

- a contextual review of business practices and other donor approaches;
- a strategic assessment of each of the engagement mechanisms employed by DFID;
- a desk review of a selected number of initiatives under different engagement mechanisms;
- an assessment of DFID's collaboration with other UK departments; and
- case studies of DFID's activities in two countries: India and Ghana.

7.2 As part of the contextual review, we will approach relevant business organisations, such as the Corporation of London, the Confederation of British Industry, the International Business Forum, Business fights Poverty, Business Action for Africa and others to gain their feedback and facilitate events. We will refine the exact modality as part of the inception phase but one possibility would be to engage businesses at two tiers: a working level group and a chief executive officer (CEO) level group. The purpose of this split tier approach would be to ensure a suitable blend of detailed, technical discussion with higher-level strategic insight.

7.3 In India and Ghana, we will assess the opportunities DFID does and could take advantage of to engage with businesses to maximise development outcomes on the ground. This will be focussed around an in-depth review of up to eight case studies. We will:

- speak to local businesses about their agendas for development and what role they see DFID taking or potentially taking;
- speak to local stakeholders and beneficiaries (such as employers, employees and suppliers) to assess what impact has been achieved on the ground;
- assess the impact of a number of DFID investment funds (returnable capital);
- speak to DFID country offices about how they view the private sector and whether they are identifying and taking full advantage of the opportunities to work alongside business and maximise their impact in terms of development outcomes; and
- look at how DFID works with bodies such as UKTI and the FCO, for example as part of the High Level Partnership for Prosperity.

8. Timing and deliverables

8.1 The review will be undertaken by a small team which brings together public sector, private sector and development experience. The work will be overseen by the Commissioners. The Lead Commissioner for this review will be Graham Ward. The review will commence in July 2014, with a final report ready for publication in the first half of 2015.