CDC
Investment works

Research summary

Insight

Making the most effective use of grants and technical assistance to support financial institutions

What's the issue?

In the financial sector, 'impact' historically has been understood as promoting financial inclusion for under-served populations such as rural households, farmers, micro-enterprises, and women. More recently, there has been increasing recognition that to maximise impact on the lives of these target groups, development actors need to think beyond access – for example, the number of bank accounts or e-wallets opened – and also consider quality and usage, such as the appropriateness of financial services for target groups, financial literacy of end-users, and actual usage in terms of regularity and frequency of use.[1]

In low-income countries, financial institutions and other financial sector market actors can be unwilling to take the necessary risks or do not have capacity to deliver these desired outcomes. Technical assistance and grants are often used to overcome these challenges and, in some cases, catalyse wider systemic change. Development finance institutions (DFIs) in particular, may use technical assistance or grants to increase the impact of an investment, particularly where there is overlap between social impact and commercial return. For example, using technical assistance to support a financial institution to develop new products which reach under-served markets can generate both social impact through expanded financial inclusion and commercial impact through customer acquisition and increased revenue. DFIs may also use technical assistance or grants for compliance or risk management purposes, for example to ensure environmental and social standards in investees.

CDC's technical assistance and grant facility, CDC Plus, aims to make a lasting difference to the lives of under-served groups by increasing economic opportunity, improving standards of living and creating a more sustainable environment. We do this by supporting businesses to adapt their operations and pilot new more inclusive business models and help shape markets where we invest.

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1 www.cgap.org/sites/default/files/researches/documents/Consensus-Guidelines-A-Market-Systems-Approach-to-Financial-Inclusion-Sept-2015_0.pdf

Given the number of financial institutions in CDC's portfolio (which make up approximately a third of investments), we commissioned this research to improve our understanding of the opportunities to use technical assistance and grants effectively within the financial sector, with the aim of facilitating inclusive and sustainable business practice change at scale. We were also keen to understand whether, and how, the unique nature of financial institutions and the systemic role they play in national and regional economies changes how technical assistance and grant projects should be designed and delivered. For example, many Tier 1 banks in developing countries are highly profitable, creating a risk that technical assistance or grants simply subsidises projects that the bank would have undertaken anyway, with no additional development impact. Due to the nature of financial services and the high level of supervision and regulation, many banks are also relatively risk-averse, creating challenges for development actors using technical assistance or grants to spur innovation or new business practices. Most financial institutions are also large, complex organisations, making it difficult to find entry-points and support successful change processes.

The full research report seeks to answer two primary questions, each relevant both to our own financial sector technical assistance and grant programming, and to other DFIs and development actors active in the same space:

1. What are relevant examples of technical assistance and grants being used to promote change within financial institutions? What type of support was provided, by whom, and what was the intended outcome?
2. What were the results? What explains the differences in success and failure? What are the relevant lessons for CDC and DFIs more broadly?

The research questions were addressed through a combination of literature review and semi-structured key informant interviews. 34 interviews were conducted in total with a wide range of key informants; nearly 80 documents were reviewed with 41 selected for deeper analysis. This summary presents an overview of the main report findings, which is available at cdcgroup.com/insight

Technical assistance and grants are non-commercial, non-returnable instruments provided to a particular organisation (the 'recipient') in order to induce a change in the organisation's performance, behaviour, or practices ('practice change'). They can be non-financial (such as training or the provision of technical expertise) or financial (such as the provision of non-returnable grant funding).[2]

~$1.6bn

CDC invests ~$1.6bn in financial institutions across Africa and Asia

2. TA/grants are distinct from 'commercial' instruments such as debt and equity investments (even when these are priced at below-market rates), which are outside the scope of this research.

What are the key trends?

1 **Some donors are adopting a systemic approach to financial sector development.** In line with wider trends in private sector development, donors are increasingly adopting a systemic approach to financial sector programming. This approach looks at financial systems holistically, identifying constraints not just on the supply-side (within financial institutions) but also on the demand-side (among customers) and in the wider ecosystem. Technical assistance and grants may be targeted at a wide range of different 'market actors', including financial institutions, regulators, government agencies, industry associations, and service providers.

2 **DFIs remain focused on supply-side interventions.** In contrast, DFIs remain largely focused on direct support to financial institutions. For example, according to a 2017 paper by CGAP, 96 per cent of DFI commitments are dedicated to financing or strengthening the supply side in the financial services market.[3]

3 **A slow convergence between donor programming and DFIs.** There are some examples of DFIs and impact investors engaging in market development and 'market shaping' initiatives, which was traditionally in the domain of donors. Conversely, some donors are moving towards the DFI and impact investing space. For example, FSD-Africa was recently awarded £90m by the Department for International Development (DFID) to scale-up its development capital fund, and DFID's market systems programmes are linking-up with DFIs and impact investors to provide a pipeline of potential investees.

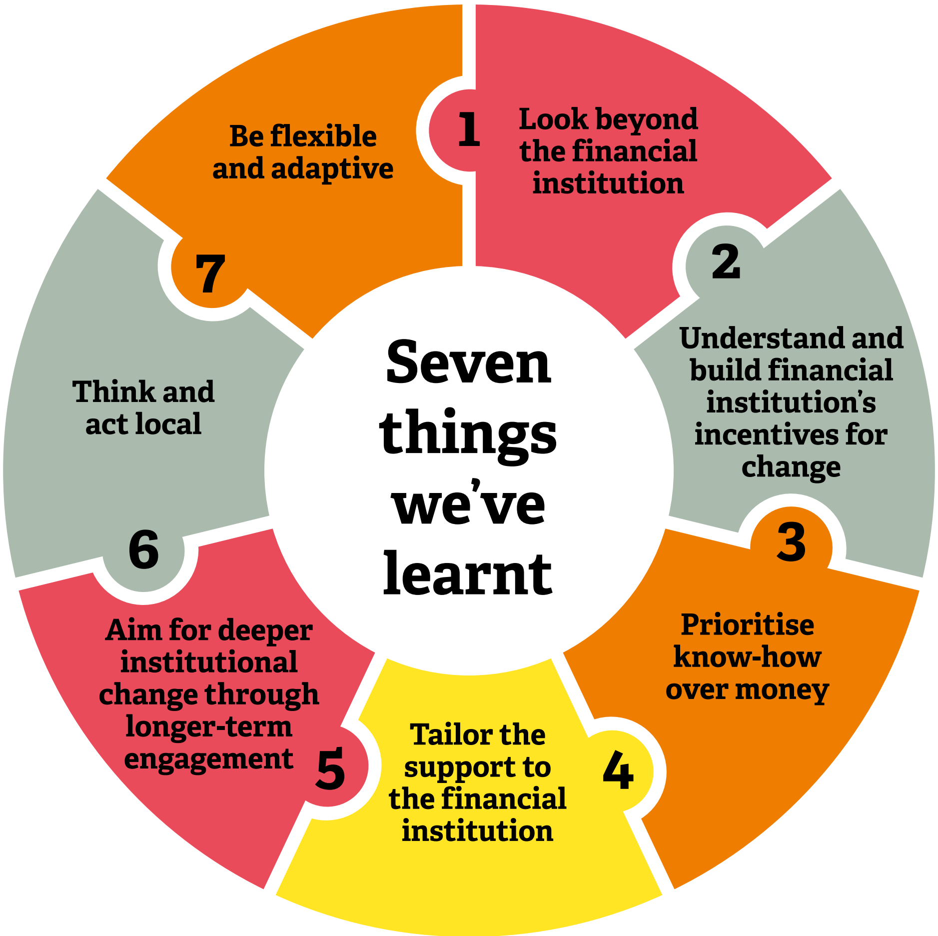
96%

96 per cent of technical assistance/grant commitments by DFIs in the financial services market are dedicated to supply-side interventions.

3 www.cgap.org/sites/default/files/researches/documents/Focus-Note-DFIs-and-Financial-Inclusion-Mar-2017-rev_0.pdf

What did we learn?

The research highlights seven key lessons on the effective use of technical assistance in the financial sector. The findings demonstrate the tangible opportunities to improve the effectiveness of technical assistance and grants to increase the impact of investments in financial institutions. They are relevant for development actors funding and designing financial sector technical assistance or grant projects and for technical assistance service providers implementing and evaluating technical assistance and grant projects on the ground.



1 **Look beyond the financial institution.** Depending on the context, critical barriers to practice change and product innovation can lie outside the financial institution itself. For example, due to high levels of regulation and supervision in the financial sector, the regulatory landscape was commonly cited as a constraint to financial product innovation. Technical assistance/grants programmes that are able to work both at the individual financial institution level and at the wider sector-level are more likely to generate sustainable, transformational impact, particularly in countries with weak or underdeveloped financial sectors. Even if the technical assistance/grant project does not have the scope to work at a sector-level, understanding beyond-the-firm constraints is still important to identify risks and potential barriers to project success.

2 **Understand and build the financial institution's incentives for change.** When selecting technical assistance/grant recipients, one of the most critical success factors is the incentive for change within the financial institution. Due to the critical importance of maintaining a reputation for prudential management and the high levels of regulation and supervision, many retail financial institutions are relatively risk-averse, making it particularly challenging for technical assistance/grant providers to catalyse innovation and change. Different financial institutions have different incentives for change and innovation, with Tier 1 banks seen by key informants as the most resistant to change (although there can be trade-off here between incentives for change and the capacity for change). Technical assistance/grant projects should therefore be prepared to build and reinforce incentives for practice change, based on a well-reasoned business case. CEO buy-in is vital, although given the organisational size and complexity of many financial institutions, buy-in at multiple levels also seems to be important. Use of cost-sharing is also an important tactic for testing recipient buy-in and incentive alignment, and financial technical assistance/grant instruments can be useful for reducing risk for financial institutions during the change or innovation process.[4]

3 **Prioritise know-how over money.** Although it varies by type of financial institution and stage in the business cycle, there is some evidence that knowledge and know-how (as well as organisational structure and processes to put new knowledge into action) limits most financial institution practice change rather than financial constraints. Consequently, providing non-financial support (e.g. advice and expertise) is generally more effective than just providing grant funding, although combining targeted non-financial and financial support in order to buy-down risk can also be effective in catalysing innovation in risk-averse financial institutions. While many Tier 1 banks in developing countries are highly profitable, FinTechs and early-stage FIs are more likely to suffer from financial constraints, particularly when trying to scale-up successful innovations, again providing a potential justification for temporary financial support.

4 **Tailor the technical assistance or grant to the financial institution.** Financial institutions can be complex organisations, offering a range of financial services to a variety of clients, and facing several different constraints and opportunities. Comprehensive and tailored technical assistance, based on detailed understanding of the recipient financial institution, is therefore more likely to promote sustained practice change than short-term, standardised packages of support. Careful consideration must be given to who conducts the diagnostic and identifies the needs of the financial institution. For example, if using self-diagnostic tools or conducting joint diagnostics, financial institution staff can sometimes overestimate their own ability to absorb technical assistance/grant support or to manage multiple change processes.

CEOs and MDs must have the capacity and willingness to absorb the services of TA providers. A client's readiness to absorb technical services has a tremendous impact on the effectiveness of TA... CEOs will be more willing to support the findings and create a conducive environment for staff to implement recommendations if they have been engaged in the process from the outset of the project.

Technical Assistance Delivery to Small Business Banks and MFIs: What Works?', ShoreCap Exchange (2005)

We quickly realised that with the new goals of [helping FIs to] expand markets and enter new markets, the grant approach was going to be a waste of money and instead [FIs] needed a lot of ground building of institutions... Asking [FIs] to do something they haven't done before, don't just give them money – odds are they won't do it, or it won't work. You need to provide the know-how.

Key informant (Technical assistance provider)

5 **Aim for deeper institutional change through long-term engagement.** Given the relative complexity of many financial institutions, promoting a particular practice change is often more effective and sustainable if addressed from a wider institutional perspective. This entails targeting fundamental organisational change rather than a specific single practice change, which requires longer-term engagement that can touch on a range of different functions and departments. For example, within the product innovation space, supporting financial institutions to become customer-centric organisations (which could involve departments from product design, to marketing, to IT) is seen as more effective than narrowly supporting a particular product or technology.

6 **Think and act local.** Due to the complexity of financial systems and their varying levels of development in low-income countries, it is advantageous to have a local presence when designing and delivering technical assistance or grant projects to financial institutions. This allows project teams to build a better understanding of the local market and context (including beyond-the-firm constraints –point 1), maintain good industry networks, and be more responsive and adaptive (point 7). For similar reasons, and given the organisational complexity and risk-aversion of many financial institutions, using local consultants in the project team who can navigate the organisation and build long-term relationships with their financial institution counterparts will also typically deliver better results and value for money.

7 **Be flexible and adaptive.** The organisational complexity of financial institutions and the dynamic nature of financial systems means that being flexible and adaptive is a critical success factor when delivering technical assistance or grant support to financial institutions. This means being prepared to change the technical assistance/grant package over time as needs and opportunities within the financial institution change, and in response to what is working – and not working – on-the-ground. This requires projects to invest in a good monitoring and evaluation system that provides regular feedback and useful insights to project teams and the financial institution itself – however, there is a limit to what financial institutions can be expected to measure (and measure well). It also requires flexibility in project work-plans and budgets.

What technical assistance providers typically do is deliver training. Training is focused on skills and knowledge, passing along knowledge, teaching how to do things. The theory is that once [the financial institution staff] have that information, they know how to do it, they will do it. But this is a flawed assumption! Real change requires a big strategic focus shift. Every aspect of your business gets touched... so requires a wider range of technical assistance.

Key informant (independent consultant / training provider)

[Technical assistance] can unblock processes, build trust, help decision makers priorities, build capacity and strategic focus. However, it will often depend on having the right people at the right time, which can be partly addressed through adaptable designs and rapid response capacity.

Lessons from Donor Support to Technical Assistance Programmes', Knowledge 4 Development (2018)

This summary is a snapshot of the report, Making the most effective use of grants and technical assistance to support financial institutions.

Find the full research on our website: cdcgroup.com/insight

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