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IFC at an Inflection Point: Time for a New Business Delivery Model?

As IFC continues to further scale up its operations, seeking to deliver more development impact, could it be in danger of inadvertently becoming an increasingly slower and higher-cost delivery mechanism, and thus a less relevant change agent? This SmartLesson—growing out of the author's observations during 32 years with IFC—proposes an alternative business delivery model with particular relevance to fragile states and frontier regions in middle income countries, in hopes of sparking a lively and productive debate around how IFC defines, delivers and measures success in its poverty reduction effort.

Background

The world has changed dramatically since 1957, when IFC was promoting half a dozen private sector investments annually and hoping the world would notice. Following the largely disappointing outcome of the postcolonial public sector investment wave, many governments and societies increasingly came to recognize the private sector as a primary engine of economic growth and efficient delivery of goods and services. However, egregious instances of environmental depredation and corporate greed cast a major shadow on capitalism. Not until relatively recently has a redefinition of capitalism's ultimate purpose through an emphasis on corporate social responsibility began to emerge. And the latest development is the emergence of a new class of social entrepreneurs eager to bridge the delivery gap between public sector institutions and private sector corporations.

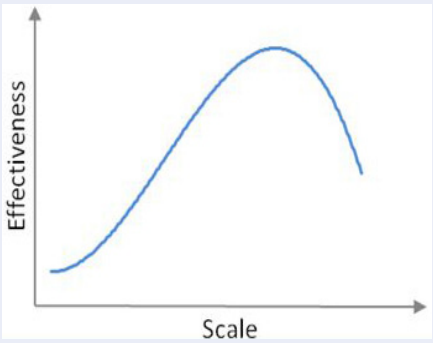
In its response to these different phases, IFC found itself gradually morphing from the world's leading private sector "development finance corporation" into the world's leading "socially responsible and environmentally sustainable development finance corporation." Recognized worldwide for its remarkably thorough financial due diligence, structuring expertise, and risk mitigation, IFC has sought to develop the same capabilities and brand in its environmental and social due diligence. Having introduced with authority and success its Equator Principles and its Performance Standards, IFC is now recognized as a leader in these key domains of corporate social responsibility.

At present, IFC heroically, proudly -and at times, miraculously- delivers its annual commitment targets every year!

But if we were to step back and contemplate our annual achievements, what does IFC actually deliver in terms of development impact through its annual commitment volumes and, given its tremendous delivery effort, where does IFC lie on the relevance curve (defined as effectiveness on the y axis and scale on the x axis, see Figure 1). Furthermore, is the current IFC business model scalable as currently structured and executed?

To answer this fundamental question we must (a) revisit how IFC defines, delivers and measures its development impact and (b) step back from our business as usual and ask:

Figure 1: The Relevance Curve



• Is the current emphasis on DOTS and IDG attribution factors leading project teams to substitute documentation and reporting tools for an actual operational strategy to deliver development impact and poverty reduction on the ground?

• Is IFC on the positive segment of the curve? That is, can IFC deliver more development impact through linear growth, relying primarily on scaling up commitment volume through continued streamlining and decentralization of its current business model?

• Is IFC on the flat side of the curve, simply stuck in its attempt to deliver more?

• Or is IFC on the negative side of the curve, actually fraying at the seams, absorbing its energy and resources in largely internal debates and laborious decision–making? Is IFC thus in danger of poor delivery, decreasing impact and ultimate irrelevance?

While an objective debate about the exact position of IFC on the relevance curve is a welcome opportunity for renewed focus on productivity and effectiveness, it is even more pertinent from a strategic perspective to ask the following question:

Should IFC revisit its development impact definition and delivery and accordingly restructure its business delivery model to engineer an inflection point to scale up its development impact?

In concrete operational terms, would IFC benefit from taking a step back from its annual performance scorecards to consider whether an alternative business model could position it as a key player in a new development strategy partnership model? Could IFC thus become an even more effective delivery vehicle for the ultimate objective of development impact and poverty alleviation on the ground?

This is a highly opportune moment, given both external and internal factors, to confront this fundamental question with leadership and lucidity.

External factors include the growing complexities and challenges of the world around us: the increasingly strained financial capability of our shareholder governments, the potential role of an increasingly active civil society, and the emergence of a new class of social entrepreneurs with innovative approaches and technologies.

Internally, new leadership at the helm of IFC and the WBG means high expectations. But challenges also remain, particularly the increasing strain at all levels as the WBG attempts to deliver more every year in the face of ever-increasing and often contradictory demands while grappling with constrained budgets, internal rigidities, and ever greater pressure to actually prove development impact.

An Alternative Strategy

In contrast with conventional budget-oriented strategy presentations which often make a pitch for additional resources, this strategy exercise considers whether a reconfiguration of the way current resources are deployed and used could yield to a new growth phase, without the current bottlenecks of a linear expansion.

In essence, this is an attempt to break the mold, disassemble the delivery machinery's gears, and re-assemble them differently to allow IFC to engineer an inflection point on the relevance curve:

1) It posits that a carefully executed decoupling of IFC investment processing activities from current IDG/DOTS driven processing activities would free IFC core staff to devote its investment skills to the structuring and delivery of a larger universe of financially and economically sustainable projects. This core effort would be leveraged, in parallel, by special purpose partnerships to effectively deliver development impact, guided by IDGs and focused on targeted delivery on the ground, with better results through enhanced knowledge management and quality assurance.

2) This attempt deliberately suspends the urgency of Board-oriented do-or-die delivery of the commitment volume and its consequent attitude of maximum focus on annual corporate and departmental performance scorecards, in favor of a long-term perspective of development effectiveness.

3) It deliberately posits that IFC and IBRD Boards and Senior Management will overcome the challenges posed by the short- to medium-term internal rigidities and constraints that discourage consideration of an alternative business model.

4) It reduces the current emphasis placed on the DOTS reporting system and IDG attribution factors in favor of a field-based development of infrastructure and supply chain linkages and delivery of bottom-of-the-pyramid (BOP) goods and services. This would be achieved through operational partnerships between IFC, private corporations, civil society organizations (CSO), and public institutions. Such private/civil/public partnerships, defined hereafter as PCPs, would be constituted for the specific purpose of leveraging the beneficial impact of the cash flow and payroll generated by the project supported by an IFC investment.

5) It posits that, in parallel to the already significant challenge of structuring resilient and growing cash flows, the optimal use of IFC's current expertise in social, environmental and advisory services is through quality control and knowledge management focused exclusively on the delivery of the PCPs' objectives (see Box 1 on the next page for an alternative model).

Operational Relevance

Although they may appear idealistic or aspirational, the suggested components of the model in Box 1 are actually derived from experience in the field and—whether based on success or lessons derived from failure—merit further consideration.
The three examples below illustrate the potential of this alternative model, which can be particularly relevant to fragile states and frontier regions in middle income countries, and more broadly, wherever the following circumstances apply:

• civil society is motivated to bridge the gap between the private sector impact and the public sector capabilities;

Box 1: What Might an Alternative Delivery Model Look Like?

The proposed model is driven by the ultimate objective of defining, delivering, and monitoring development impact through the upfront identification and coordination of PCPs to deliver a package of mutually supportive and coordinated investments, direct and ancillary, that will have maximum impact on reducing poverty and improving development impact.

First Component: engaging partners from public and private sectors, plus civil society—an externally-oriented collaboration based on partnerships between the client, civil society, the municipality, and provincial and sovereign governments (as applicable), wherein IFC and IBRD play an incubator role in the identification and coordination of such PCPs.

Second Component: a governance framework for PCPs—a clearly bounded, upfront partnership predicated on the following: 1) an upfront and collective sharing of the overall desired outcome in development impact, 2) an upfront specialization in which each party brings to the table its own area of strength and expertise and recognizes candidly where it can leverage its impact through the expertise of its carefully selected partners, and 3) an upfront policy to launch such PCPs only after the creditworthiness of the IFC investment is ascertained.

Third Component: programmatic complementarities between IFC, WBG, and CSOs—The challenge is two-fold:

1. To find the right balance between collaboration and integration. Despite daily progress, the current state of collaboration leaves too much discretion to each institution to actually harness or reallocate resources in a targeted and timely manner to support the objective of the other institution. Similarly, full integration is likely to dilute the intrinsic character and culture of each institution and absorb too much energy internally, whereas the priority is to harness and deliver more energy externally.

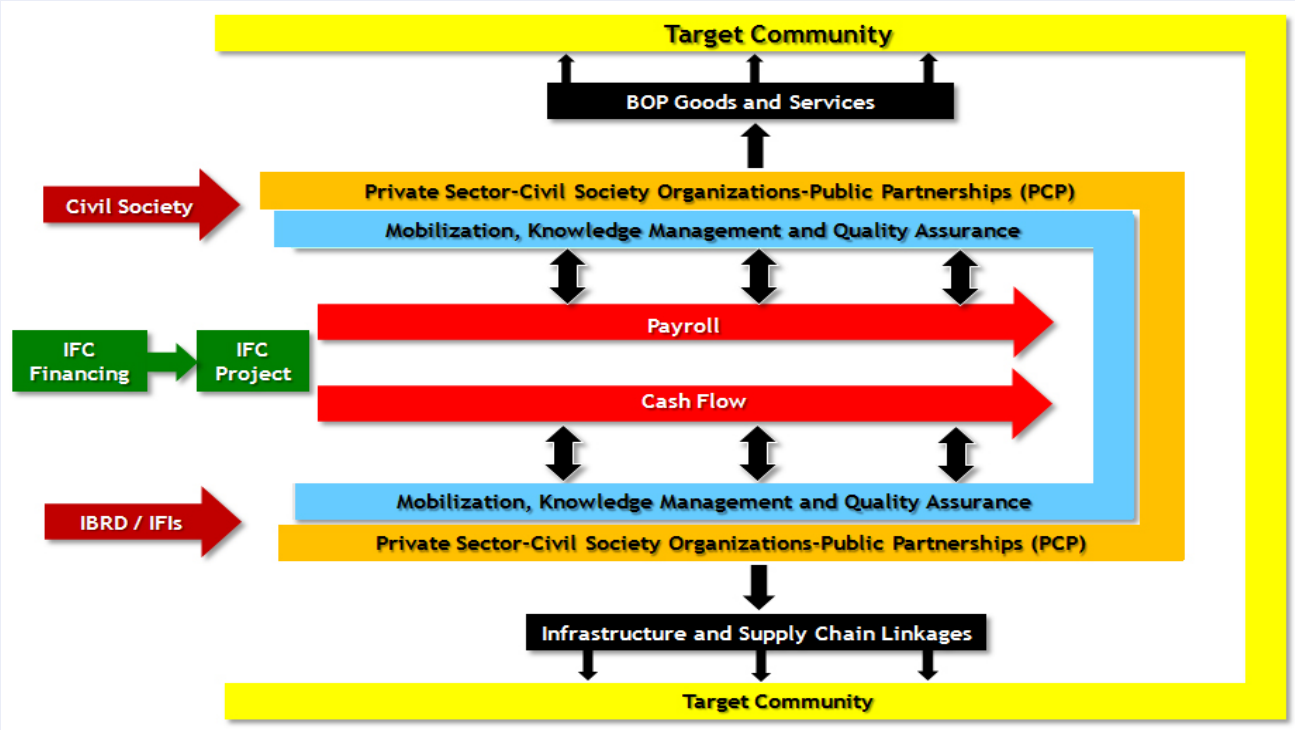
2. To astutely choose development clusters that lend themselves to such programmatic complementarities. The PCP approach must also be fully mapped and articulated from the outset in terms of key partnerships.

Guiding Principles: The objective is to respect the independence and specialized expertise of all parties involved but enter into programmatic agreements that 1) embrace the emerging role of the CSO in filling the delivery gap between private and public sector institutions and 2) adopt PCPs as an organizational tool for the delivery of development impact through targeted poverty reduction. Such programmatic agreements would be made, on a country-specific basis, by main sectors of emphasis, and would serve to establish the governance framework of a fully identified and structured partnership involving, as appropriate, other parties tapped to contribute their expertise and policy actions.

For these components to yield operationally relevant results, IFC and its prospective partners must accept that no partner can be the *primus inter pares*—in setting priorities, allocating financial resources, or delivering expertise.

The idea is to let the ultimate objective of reducing targeted poverty determine the upfront structure of a partnership in which an IFC investment is contemplated with identified government institutions and CSOs, within a clearly established PCP with a fully articulated governance mechanism.

A Development Partnership Model



- social entrepreneurs have stepped in to fill the gap, supported by IFC and WBG programmatic complementarities; and

- a political/strategic agreement exists around a desired outcome to structure a PCP with clearly defined objectives and the appropriate governance structure.

1. Brazil—Missing link in transport for unleashing export potential of agricultural cooperatives: The Valley of Sao Francisco in the Northeast of Brazil, a frontier region, is potentially one of the most competitive regions in the world in high-value horticulture, with significant promise of job creation in production, post-harvest, cold storage, and logistics activities. However, a 200-mile railroad gap inhibited the transportation of fruit to the coast, thereby frustrating the Brazilian government's ability to reap an adequate return on the significant irrigation investment it had made in the region.

A few years ago, an IFC Agribusiness mission identified this need but could not find a willing godfather for this project within the WBG. The IFC Agribusiness and Infrastructure Departments could not get any traction with the corresponding IBRD departments and the IBRD Brazil Country program, which invoked a "completed" CAS (country assistance strategy) process as a rationale for not promoting the project. Yet, completion of these 200 miles of railroad track might have been one of the key success factors in the take-off phase of large-scale high-value horticulture, with all the multiplier effects of generating businesses and jobs all along the value chain, from R&D activities, to irrigation and green houses, to post-harvest activities, to cold storage chains and inter-modal logistics, etc.

In this case, the construction of the missing railway link, either through a public sector project or a private sector concession, which could have been delivered through a PCP, did not materialize.

2. Haiti—Private sector investment in an isolated area that needs basic service provision to stop the propagation of and reverse slum conditions: IFC financed Codevi, a garment manufacturing project in an isolated area in Ouanaminthe, northern Haiti. Today, Codevi is one of the largest employers in Haiti, having grown from 600 jobs in 2000 to 6,500 jobs in 2012. Employees are fully trained, receive adequate pay under unionized conditions, and their working conditions are in compliance with IFC's performance standards. Development results, as measured by DOTS, would suggest that development impact has been achieved. Yet, the migration of 6,500 workers and their families away from the devastated earthquake areas of Port-au-Prince, without accompanying investments in basic infrastructure and services, has resulted in a slum area without drinking water, sewage treatment, roads, basic health and education, and other social services. However, to date, Government of Haiti (GOH) and IBRD attention is largely absorbed by the challenges of rebuilding Port-au-Prince. So far, CSO partnerships have filled the gap (see Figure 2), but further delivery from such community efforts also depends critically on further physical and social infrastructure investments.

The expectation that IFC can set up the investment and "things will eventually happen" in the community and that IFC can demonstrate development impact through DOTS champions chasing investment officers and clients to produce reports, must be replaced by the upfront mapping and structuring of PCPs to ensure that actual development impact is achieved and that mid-course corrections are implemented as necessary once the project is under portfolio supervision.

To address this specific situation, IFC is working on a pilot phase of a consortium established in partnership with Ashoka, a highly reputable CSO, to leverage the payroll generated by IFC's client to deliver infrastructure and supply chain linkages as well as BOP goods and services to the Ouanaminthe community, since the provision of adequate infrastructure and affordable BOP goods and services have the largest impact in boosting disposable income for the poor. The pilot phase (please refer to www.osiic.org) has already been launched with IFC support and if successful, will be scaled up into a full-blown PCP model, deploying social entrepreneurs and engaging the GOH and the IBRD/IDB to deliver basic road, water and lighting infrastructure to Ouanaminthe.

Without the multi-pronged contributions of the PCP partners, stand-alone projects may simply contribute, despite their best positive intent, to the creation or persistence of slums, as happened already in Cité Soleil, near Port-au-Prince.

3. Argentina—IFC 1991 investment in Argentine dairy company benefits 100,000 farmers: Several lessons of experience could be drawn from this specific investment, in contrast with how IFC would approach it today and could approach it under a PCP.

(a) First, IFC would probably have to overcome its reflexive reservations about investing in a first tier $1 billion turnover company. Yet, given its sheer capillarity and cashflow, it is precisely this profile of company that an IFC investment, if financially and economically viable, which could deliver maximum development impact and poverty alleviation, if a PCP is structured.

(b) Were IFC to proceed currently with such investment, a DOTS-driven approach or an IDG attribution factor would only provide a statistic of "100,000 farmers reached" without actually providing insight into whether these farmers and their farming communities were able to leverage the relationship with the dairy company or remained confined to an essentially dependent and limited buyer-seller relationship.

(c) Even in middle-income countries such as Argentina and Brazil, a cash flow and a payroll from a first or second tier company can be effectively leveraged through PCPs to deliver development impact wherever CSOs are already quite active and local government institutions can be expected to be reasonably effective. IBRD studies have shown that poverty in middle income countries can still be substantial in absolute terms and that poverty alleviation efforts need not be confined to IDA countries. IFC role and additionality should not be defined narrowly in terms of what IFC can bring in financing and/or advisory services, but more broadly in PCP terms, where role and additionality are based on the ability of the PCP partners to leverage the cashflow generated by the IFC transaction and deliver actual impact on th ground as opposed to an ex-ante and ex-post DOTS report.

Such approach would allow IFC to have a more neutral approach to the origin of the cashflow (first tear vs second tier) and to the ultimate destination (MICs or IDA countries).

Operationally, PCP would be considered essential in IDA countries and still highly desirable in MICs.

Lessons Learned:

Lesson 1: We need to take a fresh look at the way we define, plan, and measure development impact.

IFC's strategy should no longer confine itself to an ex-ante and ex-post DOTS accounting and documentation approach (intended as a tracking system for reporting to the Board) as a proxy for an effective IDG-guided strategy to deliver development impact and reduce poverty. Instead, IFC must identify the largest possible set of partnerships that will ensure or improve the actual delivery of the IFC-supported project's development impact, with targeted on-the-ground delivery.

For the IFC project development impact to be truly effective, we must structure it upfront in partnership with all parties involved. At the outset, we need to identify each potential partner's mandate, interest, and expertise—and then select the best partners to work with to deliver effective and targeted development impact where it is intended.

Lesson 2: From the outset, the strategy should take full advantage of the capabilities offered by partners to assure delivery of development impact.

IFC should be prepared to embrace, depend on, and learn from more specialized partners—primarily social entrepreneurs and carefully selected CSOs—to shoulder the task of structuring, implementing, and reporting on their specific contributions to the partnership that has been formed around the IFC-supported project, subject to a pre-agreed governance mechanism, anchored in poverty reduction objectives and WBG environment and social Performance Standards.

Lesson 3: We need to seriously consider decoupling investment activities from development impact activities by conducting them on mutually supportive parallel tracks and leveraging the expertise of investment, E&S and advisory staff to its maximum extent.

Decoupling would free up and refocus investment and operations staff to deliver what they were trained and hired to do—structure and promote financially and economically sustainable investments—while refocusing support departments with environmental and social expertise to perform the critical quality assurance and knowledge management functions. Also, this would help focus Partnerships and Advisory Operations on the specific task of identifying, developing and monitoring the main partnerships engaged with IFC to ensure the delivery of development impact.

For full benefit, special focus should be given to the leveraging of such specialized expertise, internally and externally, through an enhanced knowledge management function in PCP activities.

Lesson 4: IFC and IBRD should be ready to support PCPs wherever a development cluster in a client country is identified, whether requested by a client government or suggested by a private sector client.

The PCP approach toward a development cluster is particularly suitable to fragile countries and frontier countries but clearly could be applied to any development cluster that is the focus of the client government in agreement with the WBG.

Conclusion

Operational experience in the examples above suggests that the only viable way forward to actually deliver development impact is to decouple the processing of our core investment activity from the design and implementation of our development impact work, and to deliver both through a new business model.

This alternative delivery model is predicated on a PCP approach focused on field-oriented delivery of infrastructure and supply chain linkages as well as BOP services and goods to the community, through effective partnerships with IBRD (and other international financial institutions) and local and foreign CSOs. Under such a model, IFC would focus its investment staff (and related budgets) on core investment tasks, while carefully identifying its PCP partners and entrusting them with their areas of specialization and related reporting, thus leveraging the development impact of IFC projects with the parallel and mutual support of IFC mobilization, quality assurance, and knowledge management functions (see also Box 2 for further thoughts of the implications of such model at the IFC organizational level).

Using PCPs, IFC could indeed scale up its overall operations while delivering its maximum development impact in terms of job creation and poverty alleviation through partnerships that can deliver BOP goods and services and develop supply linkages through IFC's financially and economically viable projects.

Box 2: Further Thoughts at the IFC Organizational Level

The IFC Financial Markets Department appears to have successfully cracked the nut: its business model and organizational structure currently allow it to scale up its operations without the challenge of documenting its development impact. By contrast, the real sectors of IFC are still, by and large, struggling to scale up without getting bogged down in proving their development impact, resulting in sub-optimal and slow decision making due to the laborious, internally-oriented task of describing and documenting potential development impact.

The resulting strains on the IFC delivery machinery are likely to reach critical levels as we try to crank up the speed in response to reasonable and not so reasonable expectations. The recommended decoupling, which delivers an effective poverty reduction effort (as contrasted with the current emphasis on DOTS capture and documentation), is therefore also an internal organizational necessity and not just an option.

While several organizational realignments can be envisaged to implement such decoupling, it is crucial that the fundamental concept is internalized and assessed in terms of functional workflow with the configuration and creation/elimination of organizational "boxes" only decided in a subsequent phase.

Assuming the decoupling process is adopted, systematically for IDG countries, fragile economies and frontier regions, and desirably and opportunistically in all other instances, the functional workflow would be as as follows and in the following sequence:

Business Promotion and Client Relationship development - (in broad alignment with IFC's overarching strategic objectives)

Investment Phase - (Structuring, Business Risk Assessment and Mitigation)

Development Impact Delivery - PCP Structuring for IDA countries, Fragile Economies, Frontier Regions in MICs and wherever opportune. Otherwise: Focus on company job creation and consumer surplus in broad alignment with IFC IDGs. IFC could broaden the current remit of its pioneering Inclusive Business Department to leverage operationally the Partnerships and Advisory Operations department in the development, governance and syndication of PCPs, through regional divisions that ensure the delivery of BOP goods and services and supply linkages.

Quality Assurance and Knowledge Management - IFC's significant capabilities and expertise in E&S and Advisory would provide the crucial tasks of quality assurance and knowledge management that are vital to guide staff as they structure PCS, leverage stakeholders and reassure shareholders, as to the ultimate delivery of devlopment impact.

A significant operational gain derived from the specific workflow sequence suggested above that it would help expedite decision making and scale up further delivery by freeing IFC management and staff from the need to establish role and additionality, in the current sense of the terms, while still exercising efficient selectiveness at entry point, in terms of broad strategic fit with IDGs.

Having adopted a modulated PCP delivery approach to planning, organizing, delivering, and reporting on its development impact, IFC would gain significant degrees of operational freedom, having clarified and justified how and why it is dealing with any private sector company.