Cost-Sharing Grants

By

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Pro-Market Aid

- Why do we put aid money into private sector development? Because it delivers development benefits.
- How come? Because of the relative efficiency of the market allocation process.
- So, *if* we want to build up "an effective business development services industry," we should do so in a manner that *supports and strengthens* the market allocation process.
- "Pro-Market Aid" defined - *An aid intervention which, when completed, will leave the market allocation process better able to serve the country's development objectives than before.*

Gosplan Aid

- If it's not "Pro-Market Aid," it must be "Gosplan Aid"!
- 90% of aid to governments is Gosplan Aid.
- In social security, tax administration, etc., this is probably as it should be. *But in private sector development, we should be aiming for something different.*

Grant Schemes in Aid Projects started with Exports

- The previous history of aid interventions aimed at supporting exports is a sorry tale.
- During the 1950's, LDC exports fell behind badly. [Share of world imports in 1950 - 32%; by 1962 - 21%.]
- Big UNCTAD meeting in 1964 recommended "a permanent centre in each LDC for trade information and market research." The concept of the centralised "Trade Promotion Office" [or TPO] was born. In same year, UNCTAD set up the International Trade Centre [ITC].
- Since then, over 70 TPO's set up in LDC's, mostly in the sixties & seventies. Almost every LDC has one. Most followed the standard ITC model - set up as a single central service provider, within a ministry or a public agency - providing services free of charge.

The Two World Bank Papers of 1991

- This was the first big research project to look at how that approach had worked.

- By Prof. Don Keesing & Andrew Singer - "Development Assistance Gone Wrong," and "Assisting Manufactured Exports through Services: New Methods and Improved Policies."
- Broad finding - *the TPO approach that had dominated aid support for exports over three decades had been a disaster.*
  - They had rarely, if ever, demonstrated a measurable impact on export performance.
  - In the survey, only three of the seventy were cited by more than one respondent as being "relatively effective."
  - The report listed 28 typical negative characteristics of ineffective TPO's, and estimated that over half were to be found in the great majority of LDC TPO's.
  - Most have never been weaned off continuing aid support. They continue to absorb aid money ten or twenty years after being set up, the justification being "institutional strengthening."

Why the TPO Concept was Fundamentally Flawed

- Central provision of export development services was Gosplan Aid at its worst.
- Where export development services work well, the reason is that there exists a plurality of many different specialised service providers, most of them private and commercial.
- *The very idea that one single central service provider could ever meet the diverse needs of a whole national population of exporters was fundamentally flawed from the outset.*
- Placing this single service provider in the public service merely succeeded in making a fundamentally bad model even worse.
- Hence the challenge - how could aid money help to stimulate and expand the required *marketplace* in export development services?

The Pro-Market Approach in Action : Cost-Sharing Grant Schemes

- I have designed export grant schemes within World Bank aid projects that have already been completed in India, Indonesia, and Kenya. I have designed grant schemes that are ongoing in Mauritius, Uganda and South Africa. I was part of the design team for a further scheme in Argentina, that is now almost complete.
- What lessons do I draw from this experience so far?
  - *Compared to what happened before - the TPO model - the grant scheme model has been nothing less than a roaring success!*
  - Direct impact, in terms of additional exports generated per $ of grant support, has been way above expectations - 48 times within five years in India; 36 times within just one year in Indonesia; 30 times in just one year in Kenya; 160 times within one year in Mauritius. [These are figures reported by recipients. So far, no full control-group studies have been done.]

- Indirect impact has been just as exciting. Grant schemes in India promoted what has become a national wave of enthusiasm about ISO 9000 as a tool of export development. In Indonesia, "the assistance has definitely contributed to a change in the attitude of Indonesian entrepreneurs … they have become more active and assertive in marketing." In Mauritius, the scheme stimulated a shift in technology level within the dominant export business of woollen garments.

How does it Work - Key Characteristics of an Export Cost-Sharing Grant Scheme

- The concept is deceptively simple. "You draw up a basic plan, showing how you intend to improve export competitiveness. Within that plan, basically any usage you make of outside services will be supported with a 50% non-refundable grant."
- The concept is at heart "pro-market." At all stages, the service purchaser stays in control of the transaction. *He* chooses what the plan is to look like. *He* chooses what services he will buy, and in what order. *He* chooses which provider he will buy these services from. *He* decides whether he's satisfied with the result, and thus whether to pay. [All radically different from the TPO/Gosplan approach.]
- The concept is biased in favour of success. Grants are allocated on a "first-come, first-serve" basis. In a sense, *recipients select themselves*. Those that are most confident about risking their own 50% come forward first. That's how you get impact. [Again, a radical departure.]

Other Characteristics

- Typically, a grant scheme will consist of a mix of three complementary interventions, all directed to a common goal:
  - *Active promotion* to potential users of the benefits of utilising export development services to build competitiveness.
  - On-going *handholding advice* on the process [not on content] - eg. how to select a provider - how to draw up a contract - how to use the results of a consultancy report.
  - 50% cost-sharing *grants*.
- This is not about "institution-building" at the centre. Schemes are *deliberately temporary*. Most last three to four years. The message is "This subsidy will not be available for long. Make use of it now!" [Schemes set up with their own institutions run the risk of encouraging a "grant culture."]
- This is not about subsidy levels based on assessed neediness, or being deserving. This is not aid as a form of charity. Cost-sharing grants are *deliberately partial*. The firm's contribution is set deliberately high! [We want firms to graduate.]
- There are built-in safeguards against misuse. Grants are paid after the event, on basis of proof of payments made. Deliverables are specified in advance. If need be, grants can be made conditional on competitive bidding. Also, there is the personal relationship built up.

What have we Learned from the Experience so far?

- In export work, this concept has already broken the thirty-year-old TPO/Gosplan mould. The World Bank has virtually stopped that type of help. IDB too, apparently. The EU is starting to use grant schemes. USAID has been using grant schemes.
- Over these early years, from each scheme, we have learned something:
  - From India, we learned the importance of "pro-active selling."
  - From Indonesia, we learned not to set up a new institution. Since then, management contractors have worked particularly well. Public agency management has not worked well.
  - From Mauritius, we learned that this approach could extend from exports to technological development.
  - From Kenya, we learned that we could even give money away efficiently and safely in a very corrupt environment.
- The big challenge right now is whether the concept can transfer well from export/technology to private sector development.
  - The first experiment, Uganda, indicates that the usual grant scheme approach doesn't work with very small firms.
  - So, what I am trying next, in Mozambique, is a modified approach for very small firms, based on grants to training providers.

To Sum Up

- In export aid, the old approach didn't work.
- What was needed was a viable "pro-market" aid mechanism.
- The cost-sharing grant mechanism has met that challenge. It works. It is clearly the way forward in export aid.
- What next? How useful will it be in PSD? Can it be modified to extend its usefulness - particularly down to small/micro firms?