



## SDC's Strategy for Engaging with the Private Sector: Concept Note

### 1. Setting the scene – Why do we enter into collaboration

**Engaging with the private sector (EPS) is not a goal in itself, but a means to an end:** sustainable development resp. the SDGs. SDC engages with the private sector only in endeavors that contribute to achieving the SDGs.

Having said that, there are several good reasons for SDC to engage with the private sector in order to reach sustainable impact and scale, as e.g. **mobilizing new sources of funding, developing innovative instruments and approaches, and promoting a transformational agenda for entire sectors of the economy.** For the private sector, and in particular for those actors that are ready to contribute to the SDGs, there are also several reasons to engage with SDC.<sup>1</sup> SDC must take into consideration the different motivations and design projects in a way to create win-win situations, i.e.: how can value creation in a development project contribute at the same time to a business cause. This concept is referred to as **“creating shared value”**. In this context, it is important to notice that the overall agenda of reference might differ: while for a donor it is the Agenda 2030 and the SDGs, for the private sector it is mostly about Responsible Business Conduct (RBC) policies and business results. A general theory of change for engagements with the private sector is provided in Annex IV.

### 2. Defining the scope – What does Engagement with the Private Sector mean

Engaging with the private sector potentially encompasses a **series of ways to engage and a number of different roles for the private sector.** SDC, SECO and other development agencies engage in most of these ways, via bilateral, multi-bi or multilateral projects or in the form of policy dialogue. However, the present strategy refers uniquely to the role of the Private sector as Development Partner and as an Ally of SDC. It is thus about **modalities** that can potentially be used across the portfolio of SDC – in some sectors more, in others less. In this sense, engaging with the private sector is comparable to other working modalities, such as engaging with NGOs and the civil society or using country systems.

1. **Private sector as development partner** refers to a modality where a development agency and a private sector actor jointly engage in a symmetric collaboration for impact along the formula “shared values, shared benefits, shared risks and shared costs” (example: co-funding, together with a large Swiss multinational company, a project aimed at supporting Vietnamese farmers in producing more coffee with less water).
2. **Private sector as ally** refers to situations where development agencies support private sector platforms and engage in policy dialogue with like-minded private actors to promote a common agenda oriented towards sustainable development (example: supporting the Swiss chapter of the UN Global Compact).

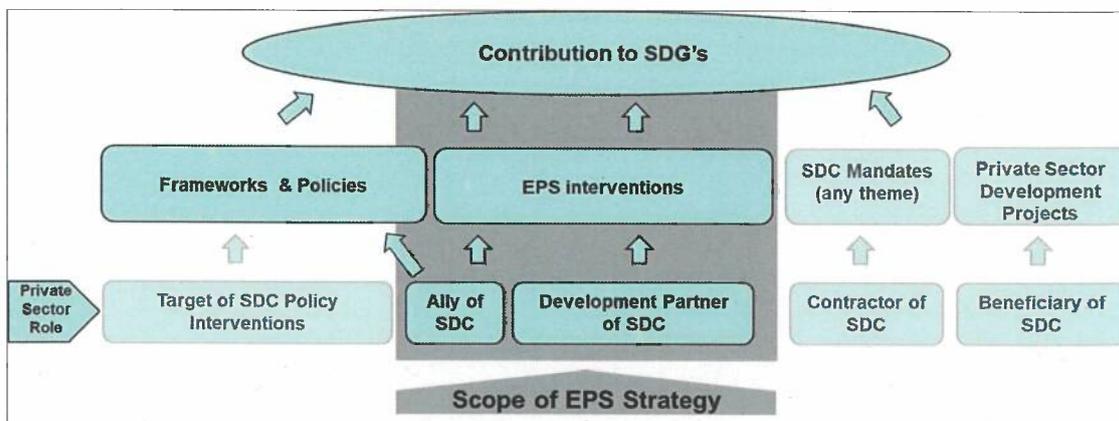


Figure 1: Scope of EPS Strategy with regard to the role of the private sector

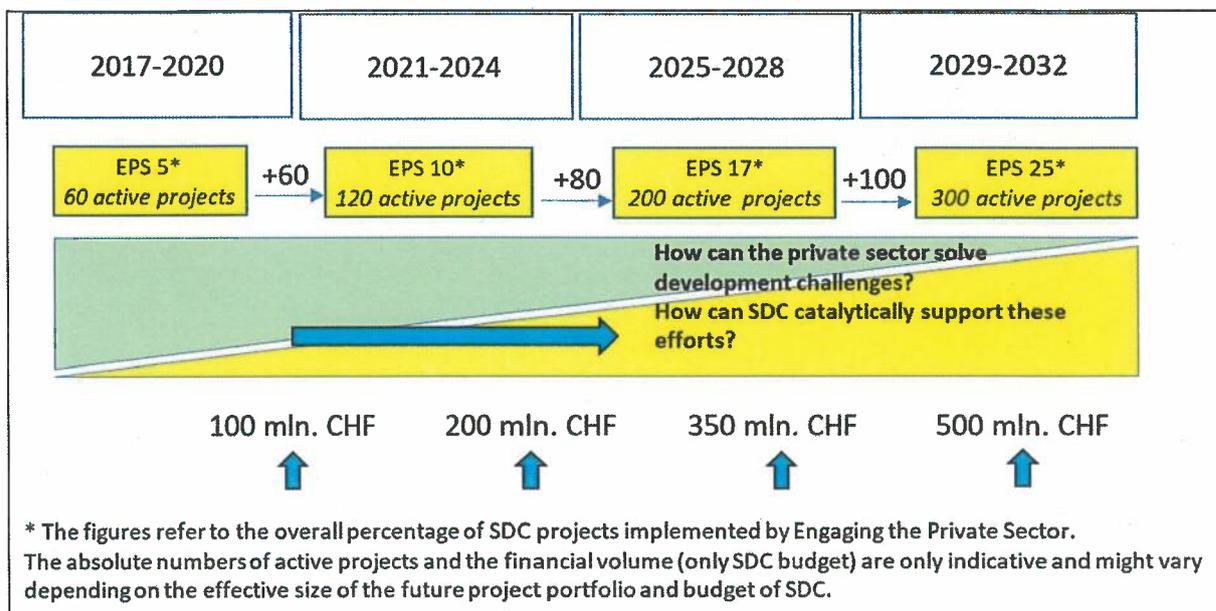
Other roles of the Private Sector outside this strategy are as **beneficiary** in Private Sector Projects; as **implementing partner or contractor** in all kinds of projects; or as **target of SDC Policy**

<sup>1</sup> See Q&As in Annex II A) and B) for an overview on motivations for both SDC and the private sector.

**Interventions** e.g. in international fora and norm-setting processes. It is important to ensure coherence when using the different modalities, both at intra- and inter-agency level. Ch. 10 will further address the issue of political coherence.

### 3. A roadmap for transformation – What do we want to achieve

The **vision** behind this strategy and the proposed roadmap for transformation (see Figure 2) is the following: Acknowledging the necessity of improving framework conditions and mobilizing private sector's resources in order to achieve the SDGs, SDC progressively transforms its way of working and strengthens its engagements with the private sector and its catalytic role within these engagements. In this way, it increases its contribution to a sustainable development.



**Figure 2: Roadmap for transformation – SDC's ambition level**

The proposed roadmap for transformation includes quantitative and qualitative aspects. At the quantitative level, the target is that, by 2032, 25% of all SDC projects are implemented using EPS modalities (current status: ~4%<sup>2</sup>). In this way, it is expected to mobilize substantial additional funds from the private sector for the SDGs – funds that would not be leveraged without SDC catalytic interventions. It is estimated that SDC funds will leverage at least an equal amount of additional private sector's funds.

The quantitative target has to be considered as an average across SDC, with possibly substantial differences across operational units; these shall define and regularly revise their own "EPS targets" based on an analysis of their context.<sup>3</sup> The substantial increase in EPS modalities will require the progressive development of new skills of the staff members throughout the organization as well as the introduction of new policies with regards to communication and funding modalities.

The proposed roadmap for transformation does not intend to reduce the role of the state in partner countries. In many cases, development interventions have to remain within the realm of the public sector. For these cases, development agencies shall support partner countries in adopting sustainable policies and mobilizing local resources.

### 4. The selection of partners – Who does SDC engage with

SDC has a broad understanding of Private sector and aims at a good mix of different categories of partners, e.g. multinational companies and SMEs, Swiss companies and local companies in partner countries, social enterprises, financial institutions, foundations and impact investors.<sup>4</sup>

SDC engages in EPS initiatives with those private sector partners that largely share its commitment towards a sustainable development.<sup>5</sup> Many companies are either genuinely

<sup>2</sup> See Annex I for an overview on the current status of SDC's EPS portfolio.

<sup>3</sup> The objective setting would therefore combine an overall target for the whole SDC with bottom-up targets defined by each operational unit, in the same spirit of the Paris Agreement.

<sup>4</sup> A social enterprise is set up with the primary objective to solve a social or environmental issue in a long-term, sustainable way by using the most adequate financial model. The financial model might range from grants up to generating profits or a mixture of both (hybrid). Impact investors are individuals or institutions making investments into companies, organizations, and funds with the intention to generate a measurable, beneficial social or environmental impact alongside a financial return.

<sup>5</sup> A definition of Private Sector can be found in the Q&As in Annex II F). A list of formal exclusion criteria for EPS projects is provided in the Q&As in Annex II G).

committed to development or have their business interest in areas that favour the SDGs – in many cases, it is a combination of both. SDC aligns shared interests towards a win-win situation.

**SDC needs to manage the risks involved with EPS activities.** Private actors can also do harm to development objectives. They can be involved in activities that run against SDC values, (e.g. violation of human rights, use of child, forced or compulsory labor, systematic corruption). SDC needs to apply its guidelines for risk management and complement them with tools that gear towards the specificity of private sector partners.

**SDC capitalizes on partnerships that work.** Partnerships that go well need a lot of investment in time and relationship management. SDC has an interest to capitalize on these partnerships and systematically scrutinize opportunities to replicate a working EPS with the partner organization, e.g. in other countries, or to broaden a working approach, e.g. to other partners of the same industry.

## 5. The “Content” of EPS – What is the Strategic Profile of SDC

**SDC continues to determine its strategic directions – EPS is a support to achieve them.** The present Strategy will not determine additional content or change any of the existing geographic and thematic strategies of SDC (cooperation strategies, mid-term orientations). It is designed to support and strengthen them by using the specific modality EPS. This said, the EPS modality is apt to support certain crosscutting strategic directions especially well:

**EPS initiatives are well suited to promote “Swissness”.** The understanding of Swissness refers to expertise rather than ownership or geography. Even though SDC does not give automatic priority to Swiss companies, it does acknowledge that Switzerland is highly recognized for specific values, expertise and know-how and the “Swiss Brand” can add value and enhance impact. Therefore, and in line with what has been expressed in the Dispatch 2017-2020, EPS initiatives will be mainly pursued on thematic areas where the Swiss private sector and SDC jointly have a recognized expertise and added value to provide, e.g. Water, Environment, Food Security, Health, Vocational Skills Development, Disaster Risk Reduction, and Financial Services.

**EPS initiatives can also address issues related to public goods.** All global programmes engage already with the private sector. These SDC engagements aim at joining public and private efforts to jointly solve development challenges.<sup>6</sup> They are not about outsourcing certain public tasks to private companies, but about how to ensure the availability of public goods for sustainable development.

## 6. The engagement modalities – How does SDC work with private sector partners

**Shift from an opportunity driven to a systematically proactive approach, the cascading approach.** While SDC has to seize opportunities also in the future, SDC should progressively build EPS into its strategic thinking. A cornerstone of the new strategic thinking is the cascading approach, which aims at maximizing financing for development. In the cascading approach, the universal grant logic is replaced by a step-wise check and the systematic question whether the private sector can solve a development challenge and public funds can be spared for other interventions (see Q&A in Annex II H) for more details). In order to apply such an approach, SDC staff needs to increase awareness through capacity building at all levels.

**SDC’s Principles of engagement with the Private Sector** are additionality, complementarity and commitment to sustainable development. Important aspects of these principles as well as other core attributes of a successful partnership are addressed in the Q&As in Annex II I) - L).

**Formats of engagement:** SDC developed a tool for structuring EPS Projects in different formats. SDC flexibly chooses the specific format to be used in a partnership depending on the development objective, the context and the type and number of actors involved. An important distinction is made between **traditional formats and financial formats<sup>7</sup> of cooperation** with the private sector. SDC’s recent experience shows that in particular the **new financial formats bear a significant potential for mobilizing private funds.**

**Public Procurement regulations apply equally to EPS projects.** However, the relation between SDC and the private sector partner in a EPS project is by definition not one of procurement of goods or services. Procurement can occur within the structure of EPS projects, e.g. if a third party is mandated by SDC to implement an EPS project. The application of relevant regulations has to be assessed in each case and its format.

## 7. Innovative instruments – How to become more strategic and reach scale

SDC has already experience in engaging in innovative platforms that have contributed to mobilize private sector actors and to foster innovation and scale. Examples are the Renewable Energy and

<sup>6</sup> Examples are Product Development Partnerships, where public and private partners join forces to develop new medicines against diseases that over-proportionally affect people living in development countries.

<sup>7</sup> **Traditional formats** include Single Private Partner Projects, Multi-stakeholder Projects and Formalized Multi-stakeholder Consortia, Matching Funds, Secondments and Political Dialogue Alliances. **Financial formats** include Venture Investments (Equity and Debt), Guarantees, Structured Funds, Impact Bonds, Social Impact Incentive and Technical Assistance Facilities to financial vehicles. Further formats could emerge and be used in future.

resource efficiency Promotion in Internal Cooperation (REPIC) platform and the Swiss Capacity Building Facility (SCBF).<sup>8</sup> For the future, the main potential for innovation and scale lies in the **enhanced use of financial formats**. This calls for the creation of a new instrument aimed at using these formats in a more intensive and professional way. To this purpose, a feasibility study has been conducted during 2018, which has provided the following recommendations for SDC:

1. There is **space and need for creating a new vehicle for the use of financial formats in EPS**. While some other donors and development finance institutions have financial vehicles in place, these show certain limitations which make them not suitable for SDC's needs. In particular, these financial vehicles have profitability objectives and therefore tend to invest in promising contexts (middle income, stable countries) and to neglect smaller investments for which the transaction costs would be too high. Moreover, they usually face restrictions, which hinder them to use all financial formats in a flexible way. These considerations apply also to the existing vehicles of SECO (in particular SIFEM).
2. In a first step, it is recommended that **SDC creates an external advisory group** (Innovative Finance Advisory Group – IFAG).
3. In a second step, **SDC shall create a new financial vehicle**, a facility for holding investments and flexibly using other financial formats (the Swiss Social Finance Facility – SSFF). **This financial vehicle would be a real innovation in the way SDC operates**.
4. Finally, if the SSFF proves to be effective, it could in a third step be opened up to other donors. **Various donors have expressed a preliminary interest to join forces**.

The Innovative Finance Advisory Group would have a twofold purpose: to start with, it would provide professional advice to SDC staff in planning and implementing EPS projects in financial formats; and, once the new financial vehicle is created, it would ensure the management of the SSFF and take care of risk management, due diligence, legal issues, impact management, and other challenges related to the financial formats. The proposed format is a stock corporation, which is fully owned by the Swiss Confederation.<sup>9</sup> With regard to the **Swiss Social Finance Facility**, it is important to notice that its **funding would arise from the initiatives developed by SDC's operational units**. This means that the SSFF would professionally manage funds approved (and then transferred to the SSFF) by these units. Legal and administrative aspects related to the creation of the IFAG and the SSFF have still to be analyzed in a follow-up assessment that shall be completed by the end of 2018.

Further information on the IFAG and the SSFF can be found in Annex III.

## **8. Building new mindsets and capacities – How to engage the organization and foster innovation**

A substantial upscaling of SDC's engagement with the private sector requires a change in approaches and mindsets – e.g. from a classical grant-giving to the cascading approach.

This implies **new skills and capabilities for SDC's staff** and will need:

- Top management ownership and deployment of internal and external communication.
- Capacity building and knowledge generation, with different offers targeted at different segments of SDC staff; this will include from short-term trainings in innovative finance instruments up to more in-depth trainings on how to co-create, negotiate and set-up EPS projects.<sup>10</sup>
- Scaling-up strategic advice to SDC operational units, aimed at identifying opportunities for more and better EPS projects.
- A well-developed set of “self-serve” and on-line tools.
- Operational advice combined with on-the-job learning, to be acquired e.g. in co-creation settings.

EPS competences shall be also increasingly valued in hiring processes. Besides that, SDC might also consider introducing some **incentives in view of actively promoting EPS modalities**. These could include financial incentives or personal incentives for staff members who proactively use and promote EPS modalities (e.g. with regards to potential assessment or career development, including possible secondments at private sector partners).

## **9. Strategic Staffing for EPS – How to walk the talk**

A substantial increase of the financial resources for EPS will require also a **progressive increase in capacities and human resources for EPS – both in-house and with external resources**. External resources will include backstopping services for traditional EPS formats (to be in place from December 2018), the external advisory services for financial formats (the IFAG, see above), and establishing

<sup>8</sup> Four Swiss federal offices (SDC, SECO, BAFU/FOEN and BFE/SFOE) cooperates within REPIC and co-finance together with the private sector the testing of promising innovations in renewable energy and energy efficiency. SCBF is a platform that allows SDC to collaborate with impact investors and other financial sector players to co-finance projects promoting responsible financial inclusion in developing countries.

<sup>9</sup> The tasks of the IFAG require very diverse and specialized competences; there is no single actor on the market that can offer these competences in a bundled way. And building these highly specialized competences in-house doesn't seem to be a realistic option due to SDC's rotational system, among others.

<sup>10</sup> There are already plans to develop such training offers in cooperation with the University of St. Gallen.

cooperation with organizations which can provide capacity building for the SDC staff. All these external resources will benefit the entire organization.

As already mentioned in the last Steering Report to SDC's Board of Directors, **there is already now a need to strengthen internal resources for EPS**. The **Competence Center for Engaging with the Private Sector (CEP)**, which is currently understaffed (< 2 Full Time Equivalent - FTE), **shall progressively increase its staffing** to an estimated 4 FTE; these resources will be needed in order to develop and manage the internal demand and the external support for EPS.<sup>11</sup> **Human Resources shall be upgraded also within SDC's operational units**. It is estimated that at least 1 "EPS Peer Advisor" would be needed in every domain (with 0.6 FTE's each). Moreover, regional "EPS champions" could support EPS activities at regional level. Division of roles and modalities of cooperation between all internal and external EPS actors will be defined in the main document of the EPS strategy<sup>12</sup>. Depending on SDC's personnel budget's situation, the newly proposed internal positions could be created as new positions or via internal compensation.

#### 10. Political coherence – How to maximize Swiss impact

While the EPS strategy focuses on the two modalities mentioned at the beginning of this document, SDC shall strive for ensuring coherence and exploiting synergies between its different interventions. As an example, the following paragraph describes how coherence between projects engaging with the private sector as development partner and SDC's multilateral engagements can be reinforced.

**EPS Projects and Multilateral Engagements:** An important share of SDC funds is channeled through contributions to multilateral organizations, which do also engage with the private sector. Therefore, SDC's core contributions to multilateral organizations leverage private sector engagement globally. Moreover, multilateral organizations play an important role in international norm setting (e.g. environmental and social standards). Switzerland is represented in the governing bodies of all its fifteen priority multilateral organizations (according to Dispatch 2017-2020) and can therefore influence these norm-setting processes. In addition, SDC supports several multi-donor trust funds and initiatives, which are linked to or hosted by multilateral institutions, such as trust funds of the World Bank Group (WBG). Finally, EPS in a multilateral setting plays already an important role in the humanitarian aid – important lessons learnt come from there.<sup>13</sup>

**Measures to leverage SDC's multilateral engagement with respect to EPS** shall include:

- Advocate in the governing bodies of multilateral institutions for enhanced EPS operations.
- Support the enhancement of respective institutional policies and reach-out activities.
- Foster multi-bi collaboration in EPS projects.
- Engage in knowledge sharing and learning exchanges on EPS with multilateral institutions.
- Make SDC's private sector partners attentive about EPS opportunities in multilateral and multi-stakeholder fora and platforms.
- Use multilateral/multi-stakeholder fora to enhance SDC's visibility as a donor active in EPS.

#### 11. Coordination with SECO and other Federal Offices

Investing public resources for development requires a good coordination with SECO and other Federal Offices in order to define roles, avoid duplication and ensure synergies for a maximum impact.

**At the level of EPS as a modality of delivering ODA**, comparable to engaging with NGOs and using country systems, there is no specific need for delimitations, all offices can and should use them.

**At the level of thematic topics and strategic orientation**, periodic high-level coordination between offices takes place, e.g. with SECO with regard to geographic focus and thematic division of labor.

**At the level of operational programs or work instruments**, strong interagency coordination needs to take place in order to avoid overlaps and realize synergies. As an example, a good coordination will be needed between SIFEM and the new financial vehicle SSFF. By its design, the SSFF shall become active in areas which are not covered by SIFEM. Nevertheless, a coordination mechanism shall be put in place. Besides that, it will be explored whether a common structure for SIFEM and SSFF, resp. for the management companies Obviam and IFAG, could be feasible and meaningful.

#### 12. Duration of the strategy – Long-term time horizon

In line with the proposed roadmap for transformation, whose time horizon lasts until end of 2032, it is proposed that the EPS strategy has a **validity of 14 years** (2019 – 2032). In order to take into account new developments in the overall context and the strategic orientations of SDC, the EPS strategy shall be revised all four years, i.e. two years before the end date of every Dispatch.

<sup>11</sup> In case the IFAG could not be created, 2 additional FTEs would be needed at the CEP.

<sup>12</sup> Key aspects would be: i) the implementation of the present strategy in line with the subsidiarity principle, i.e. centralized units such as the CEP only do what operational units cannot; ii) strong horizontal learning while maintaining existing reporting lines.

<sup>13</sup> For instance, the insurance industry (Swiss Re and Renaissance Re, amongst others) has created jointly with the WB, UNDP, and UN-OCHA an Insurance Development Forum in order to raise awareness and demand for risk-transfer solutions in partner countries.

## Questions to SDC's Board of Directors

Does the Board of Directors agree with...

1. ...the vision behind this strategy, i.e. that, acknowledging the necessity of improving framework conditions and mobilizing private sector's resources in order to achieve the SDGs, SDC progressively transforms its way of working and strengthens its engagements with the private sector and its catalytic role within these engagements, increasing in this way its contribution to a sustainable development?
2. ...the proposed roadmap for transformation as described in chapter 3?
3. ...the proposed switch from a rather opportunistic to a more strategic approach in EPS as proposed in chapter 6, incl. e.g. the consistent use of the cascading approach in identifying new projects?
4. ...the creation of the proposed Innovative Finance Advisory Group (IFAG) and, in a subsequent step, the creation of a new financial vehicle, i.e. the Swiss Social Finance Facility (SSFF), provided that the still open questions on the legal and administrative aspects related to their creation are satisfactorily clarified?
5. ...the creation of the internal positions needed to implement the proposed strategy?

## Annexes

- I. Current status of SDC's EPS portfolio
- II. Engagement with the Private Sector: some Questions and Answers
  - A) What is the motivation of SDC to enter into cooperation with the Private Sector?
  - B) What is the motivation for the Private Sector to enter into cooperation with SDC?
  - C) Why shall SDC adopt a Roadmap for Transformation with quantitative targets for EPS projects?
  - D) Why does the proposed Roadmap for transformation deviate from the two options proposed in the Note to SDC's Board of Directors of 9<sup>th</sup> May 2018?
  - E) What would be other strategies for SDC in view of engaging with the private sector without transforming its way of working? How do these strategies compare with the proposed Roadmap for Transformation?
  - F) How does SDC define the private sector?
  - G) Are there any exclusion criteria for EPS projects?
  - H) In what consists the cascading approach?
  - I) Which are the basic principles of engagement followed by SDC?
  - J) What are core attributes of a successful partnership?
  - K) Will the current system of strategic partnerships be continued?
  - L) What is the Risk Management approach used by SDC?
- III. Main recommendations of the feasibility study on the creation of an external advisory group and a new financial vehicle
- IV. Theory of Change