Sharpe
Strengthening Host and Refugee Populations in Ethiopia

Use of financial subsidies for the private sector in the context of host and refugee communities

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1. Executive summary

Overview of the study

The Strengthening Host and Refugees Populations in Ethiopia programme (SHARPE) is one of a number of innovative programmes working at the intersection of market systems development and humanitarian relief.[1] Through the use of an adapted market systems approach – 'Markets for Resilience' – SHARPE works to strengthen the economies of target populations in three regions in Ethiopia: Dollo Ado, Gambella, and Jijiga.

A recent programme annual review recommended that SHARPE "analyse their use of public subsidy to inform future programmes delivered by FCDO, delivery partners, and others. This will allow decisions to be informed by evidence and is key to understanding how market systems can be best supported in Ethiopia." In response to the review recommendations, SHARPE has commissioned a study to answer the following primary research questions:

1. How has SHARPE used public subsidies for private sector actors?
2. What processes and considerations did SHARPE use in deciding if and how to use public subsidies for private sector actors?
3. How effective has the use of subsidies for private sector actors been, and what lessons can be drawn for SHARPE and for similar programmes operating in host and refugee communities?

To answer these questions, the research team conducted an internal and external document review and conducted interviews with SHARPE staff, advisors, and private sector actors that had received financial support from SHARPE.[2]

Headline findings (1): how SHARPE has used public subsidies for private sector actors

SHARPE has provided grants to over 100 different enterprises, which range significantly in size, sophistication, and ownership-type. Broadly, these enterprises fall into three categories:

- Large, national companies, often headquartered in Addis Ababa;
- Small and medium regional companies, typically host-owned;
- Micro-enterprises, typically refugee-owned but also host-owned, and often informal.

Reflecting the diversity of the enterprises supported, the subsidies provided by SHARPE vary significantly in value, from under £100 to over £200,000. All grants provided by SHARPE have a cost-share element; the average cost-share provided by SHARPE was 70%. The average cost-share was highest for refugee-owned businesses (77%), followed by host-owned enterprises (65%). The average cost-share is also inversely correlated with the size of enterprise: the average cost-share

Box 1: About SHARPE

SHARPE is a 5.5 year, £14.4mn programme funded by FCDO. The programme started in September 2019 and is scheduled to close in March 2025. SHARPE promotes increased refugee self-reliance and generates economic opportunities for host communities through the piloting and scaling of interventions. The approach is based on understanding the economic barriers that refugee and host communities face and working with key stakeholders – including businesses, government, and service providers – to make markets work for target communities. SHARPE expects to benefit up to 125,000 people in the target populations, helping them realize increases in incomes and employment or expand access to assets through private sector-driven changes. As well as targeting hard to reach groups, the operating context for SHARPE has been challenging, including Covid-19, the Tigray civil war, and a worsening macro-economic outlook.

1 For a good summary of other programmes working at the same intersection, see ILO / UNHCR (2023): 'The Humanitarian Development Nexus in Action: A Review and Mapping of Market-Led Approaches in Forced Displacement Contexts'.
2 A full summary of the study methodology is available on request.

provided to large enterprises was 59%, increasing to 73% for micro enterprises. Although comparable data is hard to come by, the cost-shares provided by SHARPE may be higher than other market systems programmes globally, but not for programmes operating in comparable contexts. With a few exceptions, all grants are structured as standard cost-sharing grants and provided on a reimbursable basis. For larger companies, SHARPE grant agreements typically include conditions around the percentage of refugees and women reached. SHARPE also often provides non-financial support alongside grants – mainly market linkages and on-the-ground facilitation support.

Headline findings (2): the processes and considerations used by SHARPE

Before deciding which actors to support, and how, SHARPE undertook a market systems analysis of multiple sectors in order to identify those sectors with the highest potential to integrate host and refugee communities and to understand the key systemic constraints. Within the prioritised sectors and sub-sectors, SHARPE has taken a proactive approach to seeking out private sector actors that are genuinely interested in trying something new (and not just seeking cheap donor money).

Once a high-potential partner has been identified, SHARPE and the partner agree the objectives for the partnership, what practice changes the actor will implement in order to achieve these objectives, and what support SHARPE will provide. SHARPE has a clear policy on what costs it will and will not subsidise – with a clear focus on catalysing 'innovation', not 'more of the same'. SHARPE also has relatively robust processes in-place for assessing the additionality and sustainability of any grant-support.[3] SHARPE also adapted its grant and due-diligence processes and procedures to allow it to provide financial support to refugee and host-owned enterprises.

Once the overall partnership objectives and budget have been agreed, cost-shares for each budget item are negotiated by SHARPE. The SHARPE Partnership Manual provides guidance on the 'expected' cost-share (50:50), but not the factors that might drive an upward or downward deviation from this, and no benchmarks are used by the team when negotiating the cost-share. SHARPE also has a relatively robust system in-place for monitoring grant performance; learning and insights from the monitoring system are used by SHARPE to adapt the support provided and to help grantees themselves to learn and adapt.

Headline findings (3): how effective the use of subsidies for private sector actors has been[4]

Grants, alongside market linkages and on-the-ground facilitation, have been effective in catalysing larger companies to adopt and test practice changes targeting refugee and host communities. Grants have also been made more effective by the ability of SHARPE to generate insights and learning on what is and is not working, and supporting grantees (and SHARPE) to adapt accordingly.

For larger companies, grants have been effective in building the capabilities of grantees to serve host and refugee communities through 'learning-by-doing'. After buying-down the initial risk, SHARPE grants have also been effective at catalysing an underlying shift in motivations in larger companies regarding target markets, suggesting a high degree of sustainability (at least in relation to host markets). Larger companies have naturally been more likely to target host than refugee markets; SHARPE has been able to steer grantees towards the refugee market during the lifetime of the grant, although post-grant, the early evidence as to whether companies will continue to target the refugee market is mixed (especially for national Addis-based companies).

In the case of regional and micro host and refugee-owned businesses, grants or subsidised loans plus market linkages and other support, have been effective in enabling these businesses to upgrade, expand, and integrate into supply-chains. However, in some cases, the use of reimbursable grants has created a barrier for refugee-owned enterprises to make the necessary up-front investments. Many of the refugee-owned businesses have maintained the practice changes post-grant, although the vulnerability of refugees to shocks means some have been unable to sustain their businesses.

3 'Sustainability' here and in the rest of the paper is defined as the likelihood that the practice changes adopted by market actors, to which SHARPE has contributed, are maintained or built-upon by market actors beyond the end of SHARPE support.

4 'Effectiveness' is assessed in terms of the extent to which SHARPE support to private sector actors has led to the adoption of new innovations and practice changes that are both sustainable and impactful (in terms of contributing to improvements in the lives and livelihoods of host and refugee populations).

Recommendations for future programming

Overall programme strategy-setting:

1. Programmes wishing to sustainably improve the livelihoods of host and refugee communities in the context of protracted displacement should combine market systems development principles with direct targeting of large market actors, small and medium regional actors, and micro and host and refugee-owned enterprises.

Identifying private sector actors to support:

2. Programmes should adopt a proactive approach to identifying and engaging private sector partners and test their commitment through cost-sharing, particularly when operating in 'donor-heavy' context. This requires a strong core team with on-the-ground presence in the main economic hubs as well as in the target host and refugee markets.

Designing the package of support:

3. Programmes should co-create ideas with potential partners and undertake a diagnostic of each partner to understand their 'capability', 'opportunity', and 'motivational' constraints to adopting the desired practice changes. Staff should actively consider a wide range of 'facilitation tactics' in developing the support package, which should be designed to tackle the specific constraints facing each partner. The menu of possible facilitation tactics should include cost-share grants, but also other forms of financial support such as risk-guarantee mechanisms, as well as linkages, on-the-ground facilitation, and external Technical Assistance.

Setting the grant policies, processes, and procedures:

4. Programmes should adopt a clear grant policy, with a strong focus on innovation, additionality, and sustainability. The grant process should also consider the 'business case' for targeting hosts, refugees, and women (as appropriate), and potential wider systemic impacts. Programmes should also ensure that their administrative processes allow them to effectively administer a potentially large number of small grants to host and refugee enterprises, potentially including those outside the formal sector, combined with on-the-ground support.

Cost-sharing:

5. Programmes should maintain the principle of cost-sharing, but be willing to provide higher-than-average cost-shares, particularly to host and refugee-owned micro-enterprises. Caution should be maintained when considering high cost-shares for large companies.
6. Programmes should develop guidance and benchmarks to assist staff in the negotiation of cost-shares with grantees.

Monitoring, learning, and adapting:

7. Programmes should adopt a flexible and adaptive approach, underpinned by a robust research and monitoring system. The package of support provided should be adapted as needed based on on-going monitoring of what is and is not working on-the-ground. Programmes should also actively support enterprises to learn and adapt their business models, especially larger companies for whom host and refugee markets are often unknown and untested at the start of the partnership.

The rest of the study is structured as follows. Section 2 presents the main findings from the study. Section 3 summarises the key lessons from SHARPE, combined with lessons from the external literature, and provides a set of recommendations for future programming. The Annex presents a conceptual model of how financial subsidies can be used to catalyse change in private sector actors and how the level of public subsidy necessary may vary depending on a variety of internal and external factors.

2. Study findings

This section presents the main findings for each of the three research questions.

2.1: How SHARPE has used public subsidies for private sector actors

SHARPE has provided grants to over 100 different enterprises, which range significantly in size, sophistication, and ownership-type. Broadly, these enterprises fall into three categories:

- Large, national companies, often headquartered in Addis Ababa. Examples include Shayashone, an Addis-based agro-input supplier with a network of more than 450 vendors and 400 youth resellers across Ethiopia, and Shabelle Bank, the largest bank in the Somali region and one of the leading providers of Digital Financial Services in Ethiopia.
- Small and medium regional companies, typically host-owned. Examples include Shifo, a small, host-owned agro-vet based in Kebribeyah town and serving approximately 3,000 people in the host and refugee community at the time of the first SHARPE grant.
- Micro-enterprises, typically refugee-owned but also host-owned, and often informal. This includes, for example, small-scale poultry farmers and vegetable farmers.

Of the 102 enterprises receiving SHARPE grants to date, 77% were micro-enterprises, 12% were small, 4% were medium, and 7% were large. Nearly half of all grantees (49%) were refugee-owned enterprises (all of which were micro-enterprises). SHARPE also provided subsidised business loans to 17 businesses and 41 Hello Cash agents in the Somali region.

Although the specific objectives of each grant agreement varies, in general the purpose of the grants is to catalyse the integration of host and refugee communities into high-potential supply / value chains. For medium and large companies, grants have been used to incentivise firms to expand into host and refugee markets and 'test the market'. Here the focus has generally been on using grants to buy-down risk. For refugee-owned micro-enterprises, grants have been used to support enterprises to reach a size and sophistication where they can participate effectively in wider supply chains. Given their low levels of income and difficulty accessing finance, grants have generally been used to provide a substantial part of the necessary financing. Host-owned enterprises have also been supported to grow, and to more effectively link large companies in the capital or regional centres with refugees.[5]

Reflecting the diversity of the enterprises supported, the subsidies provided by SHARPE vary significantly in value, from under £100 to over £200,000. The largest single subsidy was for SMFI (now Shabelle Bank), worth £222,000. The smallest subsidy was for £81, given to various refugee vegetable farmers in Gambella. The average value was £15,500.

All grants provided by SHARPE have a cost-share element; the average cost-share provided by SHARPE was 70%. Aside from emergency grants provided to eight poultry farmers who lost their chickens due to an outbreak of Newcastle disease, all SHARPE grants have had a cost-share element. Again, reflecting the diversity of enterprises supported, the cost-share provided by SHARPE varies considerably, from 35% to 88% (based on the commitments set-out in the grant agreements).

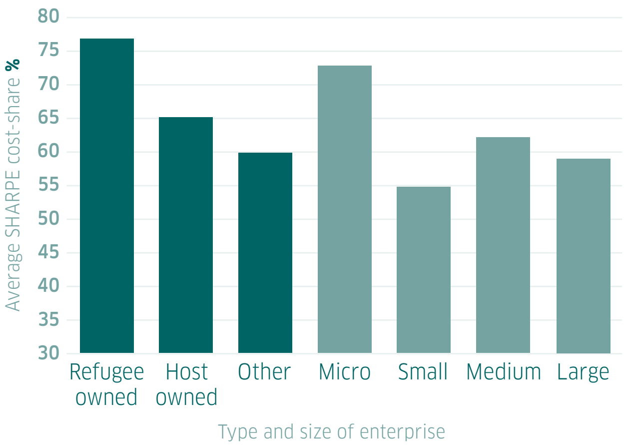
SHARPE does not systematically monitor grantee's actual financial contributions; the ultimate cost-share is therefore unknown, although anecdotal evidence suggests it is close to the committed cost-share. SHARPE closely monitors whether the grantee has met the milestones detailed in the partnership agreement before releasing the grant payment. However, due to various practical difficulties, SHARPE does not systematically track the actual value of grantee resources committed against the commitments made in the grant agreement. Anecdotal evidence suggests that partners' actual contributions closely match or exceed the committed amounts.

The cost-share provided to enterprises is highest for refugee-owned businesses, followed by host-owned enterprises; the average cost-share is also inversely correlated with the size of enterprise. The average cost-share for refugee-owned businesses was 77%, followed by host-owned businesses at 65%, then 'other' businesses at 60%. Given that refugee-

5 A good example is host-owned Shifo Agro-Vet, which was linked with Shayashone and provided with a subsidised loan to enable it to grow and more effectively serve the local host and refugee market.

owned enterprises, followed by host-owned enterprises, are least likely to be able to access internal or external finance to fund investments, this is consistent with the conceptual model presented in the Annex. The average cost-share also falls as the size of the enterprise increases, although with an anomaly for 'small' enterprises (see Figure 1). The average cost-share for micro-enterprises was 73%, falling to 59% for large enterprises – also consistent with the conceptual model.

Figure 1: average cost-share provided by SHARPE, by ownership and size of enterprise



Source: SHARPE grants tracker and study team's calculations.

Although comparable data is hard to come by, the cost-shares provided by SHARPE may be higher than other market systems programmes globally, but not for programmes operating in comparable contexts. Interviews with international consultants familiar with SHARPE suggest that the cost-shares provided by SHARPE are "more generous" than other market systems programmes globally. In terms of the external evidence available, the Investment Manual for one market systems programme in Georgia suggests aiming for a cost-share of 65% – only slightly lower than the average of 70% provided by SHARPE – noting that "50% for an initial investment for most businesses would be too much".[6] Given the context SHARPE is operating in, with both 'thin' markets and a 'donor-heavy' environment, a higher cost-share is to be expected (see the Annex). Anecdotal evidence from several of the SHARPE grantees interviewed also suggests that other donor programmes in Ethiopia are as, if not more, generous than SHARPE.[7]

Within any given grant agreement, the cost-share for individual budget items can vary between 0% and 100%. For example, in the grant agreement with SMFI (now Shabelle Bank), SHARPE agreed to pay 100% of the field team salary and mobile phones (for a time-limited period) while the bank agreed to pay 100% of agent incentives and education and promotion materials, and so on (overall, the cost-share from SHARPE was just under 70%).

SHARPE grants have included cost-shares for 'one-off costs' including buildings or equipment (unlike some other market systems programmes) and time-limited cost-shares for recurrent costs such as staff salaries. For example, SHARPE has cost-shared for one-off costs such as the purchase of imported equipment by Hello Solar and the construction of satellite bank branches in refugee camps by Shabelle Bank. This is in contrast to the guidance provided by some market systems programmes such as KATALYST in Bangladesh or PRISMA in Indonesia.[8] In interviews, SHARPE staff expressed the view that, given the very different and more challenging context, it was important to be able to cost-share infrastructure and hardware if that is what is required to catalyse the desired innovation.

Nearly all grants are structured as standard cost-sharing grants and provided on a reimbursable, milestone basis. There have been some exceptions. For example, for companies struggling to access foreign exchange due to the capital controls imposed by the Government of Ethiopia, such as Hello Solar, SHARPE provided pre-financing (in foreign currency) for the purchase of imported parts and equipment. For a few refugees struggling to raise the finance necessary to make the initial investment, SHARPE also paid its contribution direct to the vendors.

For larger companies, SHARPE grant agreements typically include conditions around the percentage of refugees and women reached. For example, the grant agreement with SMFI / Shabelle Bank designed to support the expansion of their agent network includes the condition that 35% of the agents recruited and trained must be female agents.

SHARPE often provides non-financial support alongside grant support. This typically takes the form of brokering linkages and providing on-the-ground facilitation support and market insights. The SHARPE core team also provide advice and guidance to partners, both at the deal stage and during implementation (e.g. sharing data and insights

6 ALCP Investment Manual, 2022.
7 For example, Shayashone reported receiving a cost-share from two donors of 65% (versus 65% and 58% for the two grants provided by SHARPE).
8 The PRISMA Deal Making Guidelines states that funding equipment or infrastructure should be avoided "as this can give unfair advantages to a firm and reduce potential for replication".

from the monitoring system). Beyond this, SHARPE has made relatively limited use of specialist external Technical Assistance (although through its grants it has supported larger companies to provide training to regional and micro enterprises).

2.2: The processes and considerations SHARPE used

Before deciding which market actors to support, and how, SHARPE undertook a market systems analysis of multiple sectors in order to identify those sectors with the highest potential to integrate host and refugee communities and to understand the key systemic constraints. The original DFID Business Case for SHARPE identified six sectors. During the inception phase, SHARPE undertook a more detailed analysis of these sectors to identify a number of priority sectors and sub-sectors, including: poultry, agri-inputs, Digital Financial Services, and solar. The SHARPE team noted that this process suffered from numerous challenges, including travel restrictions due to Covid and delays to the MoU. During implementation, although SHARPE has considerably deepened its learning around these focal sectors, for example

Box 2: How does the market systems development approach differ from a humanitarian livelihoods approach, and how do the approaches differ in the use of public subsidy?

A recent paper by the ILO and UNHCR* provides a useful summary of the differences between 'market systems' and 'humanitarian livelihoods' approaches:

"The market systems approach... are usually implemented by development practitioners, focused on private sector engagement either to support or change markets. Projects often work to transform the entire system, designing interventions that respond to binding constraints in order to shift systems or markets. Implementers take on the role of a facilitator and work through other market actors. Projects focus on implementing strategies with the private sector, with no push strategies to prepare refugees, IDPs or hosts for the market."

"On the other side of the continuum is livelihoods programming, characterized by direct delivery of services, products or subsidies, usually the emphasis of humanitarian organizations. There is often a focus on handing out productive assets such as seeds or tools, or providing grants for income-generating activities, as well as directly providing extension training, farmer organization, or training on business start-up. Subsidy is often high, programming is narrow and focused on the targeted beneficiaries, and there is typically no systemic analysis, nor interventions targeted to shift the wider systems where displaced peoples are based."

As hinted at above, the use of public subsidy will tend to be very different for programmes at either end of the spectrum. Under the market systems approach, although there are no firm rules, programmes will tend to provide financial (and non-financial) support to larger market actors and not to the ultimate target groups. The aim is to catalyse sustained changes in the practices and behaviours of these larger market actors, thereby delivering lasting impact for large numbers of target individuals. Programmes will deliberately seek out actors that already demonstrate some level of capability and motivation. Typically, high levels of cost-share from grantees are expected in order to test commitment. Conversely, humanitarian livelihoods programmes will typically only provide support direct to end-beneficiaries in the host and refugee community. Subsidies tend to be large, with little or no cost-share expected from grant recipients.

Note that in the case of SHARPE, the programme would fit somewhere in between the two ends of the spectrum presented in the ILO / UNHCR paper. Although SHARPE adheres to all the core principles of the market systems development approach, it does actively provide financial and non-financial support to refugee and host entrepreneurs. This is done in the context of SHARPE's support with larger companies, with a strong focus on also providing linkages between the two (what the ILO / UNHCR paper calls a 'push' and 'pull' strategy).

Notes: * ILO / UNHCR (2023): 'The Humanitarian Development Nexus in Action: A Review and Mapping of Market-Led Approaches in Forced Displacement Contexts'.

through regular technical review sessions, this learning has not been systematically consolidated (e.g. through the periodic updating of the original systems analysis).

Within the prioritised sectors and sub-sectors, SHARPE has taken a proactive approach to seeking out private sector actors that are genuinely interested in trying something new (and not just seeking cheap donor money). According to the SHARPE Partnership Manual: "Starting from the system constraint identified, SHARPE searches for the most incentivised, motivated and able system actor to implement new business models, introduce new products and services (or scale them up) – all of which should be in a manner that is commercially sustainable." To identify potential companies to support, SHARPE has taken a proactive approach. This has included SHARPE head-office staff seeking out and engaging with larger mostly Addis-based companies to gauge their potential interest in expanding to host and refugee communities, and local teams engaging with mid-size regional companies as well as identifying entrepreneurial host and refugee business owners in the priority sectors. Given the 'donor-heavy' context, to avoid attracting 'donor-hunters' SHARPE avoided the use of Challenge Fund-style call for proposals or open applications.

To aid this effort, SHARPE has distinguished itself from other development actors in Ethiopia by presenting itself as a 'business-like' organisation that understands the private sector. This approach appears to have helped SHARPE to attract the 'right' private sector actors in the first place (as well as helping in managing partnerships during implementation). For example, one Addis-based company that has received two grants from SHARPE expressed the view that, for donors wanting to work with the private sector, it is "very important that they understand the dynamics of the private sector". They noted the "good chemistry" with SHARPE, based on a "shared value proposition". The company had rejected offers of support from other donors and NGOs because "they were not commercially minded" and they feared that accepting the support would dilute their commercial identity.

Once a high-potential partner has been identified, SHARPE and the partner agree the objectives for the partnership, what practice changes the actor will implement in order to achieve these objectives, and what support SHARPE will provide. These are documented in a 'deal note', which then forms the basis of the Grant Agreement. For each practice change, the deal note then sets out what support, if any, SHARPE will provide.

SHARPE actively considers the constraints facing each grantee in adopting the desired practice changes, although this appears to focus on financial and incentive constraints (with less active consideration of capacity constraints). SHARPE has a clear understanding that programme support should be tailored to each partner and designed to overcome the specific barriers preventing the partner from adopting the desired practice changes by themselves. However, although SHARPE has a robust due diligence process in-place, it does not appear to undertake a comprehensive analysis of the 'capability', 'opportunity', and 'motivational' constraints within the partner. In practice, support has focused on the provision of grants to buy-down risk of larger companies, or to help refugee-owned enterprises to grow to a sufficient size, plus help to broker linkages and other on-the-ground support; limited use has been made of Technical Assistance to address any 'capability' constraints (see Annex).

SHARPE has a clear policy on what costs it will and will not subsidise – with a clear focus on catalysing 'innovation', not 'more of the same'. As noted in Section 2.1, the SHARPE Partnership Manual has clear guidance on what SHARPE will and will not fund. The Manual also stresses that the role of SHARPE "is not to subsidise 'more of the same', but to allow partners and systems to make incremental steps forward to develop more inclusive and resilient business models".[9] However, the study observed several cases where SHARPE's policies on cost-sharing was not well understood by the partner, resulting in confusion and frustration on both sides.

SHARPE has relatively robust processes in-place for assessing the additionality and sustainability of any grant-support. The DFID policy framework for the provision of subsidies to for-profit firms emphasises the importance of additionality, sustainability, and avoiding market distortions.[10] Through the Deal Note

9 In the case of Shabelle Bank, for example, SHARPE was willing to provide a time-limited cost-share for the salaries of a sales team tasked with raising awareness and registering customers for Hello Cash in target host and refugee communities, and for the construction of satellite bank branches in four refugee camps to provide the necessary liquidity for the agent network – both a first for the bank – but rejected requests from Shabelle Bank to cover core business expenses such as the purchase of additional cash transport trucks.

10 DFID (2011): 'DFID Policy Framework for T DFID policy framework for the provision of grants or concessional finance to for-profit firms the Provision of Grants or Concessional Finance to For-Profit Firms'.

template and the grant approval process, the SHARPE team carefully consider the additionality of the grant – i.e. why the partner is unable or unwilling to make the desired changes without SHARPE support. SHARPE also considers the extent to which a partner could finance the additional investments themselves and, in some cases, will instead try to link the partner with a finance provider instead of providing a grant itself. Sustainability is assessed in the Deal Note through financial analysis of the expected post-partnership revenues and costs of the business model. However, the Deal Notes reviewed by the study team do not always include a clear elaboration of the 'business case' for targeting refugee or host communities, and women, in particular.[11] The potential positive and negative systemic impacts of the grant are also not documented. The SHARPE team were of the view that, in practice, the risk of negative systemic impacts of their grants is low given they support 'first-movers'.

SHARPE adapted its grant and due-diligence processes and procedures to allow it to provide financial support to refugee and host-owned enterprises. At the start of the programme SHARPE developed two different grant agreements: 'standard' and 'micro' (for grants up to £5,000). The micro grant agreement has allowed SHARPE to provide support to refugee-owned enterprises that would otherwise be unable to meet the full grant conditions, while also reducing the administrative burden for both SHARPE and the grantee. According to interviews with the SHARPE team, prior to receiving SHARPE support many of the refugee-owned grantees were informal and did not have a license or bank account. The SHARPE local teams provide facilitation support to grantees to help them obtain the necessary licenses, either as enterprises or cooperatives, and open a bank account.

Once the overall partnership objectives and budget have been agreed, cost-shares for each budget item are negotiated by SHARPE, with mixed evidence from interviewed grantees regarding how 'tough' the negotiations are. SHARPE negotiates the cost-share based on SHARPE's assessment of what the partner can afford to contribute. Within the overall budget, some items SHARPE might offer to fund 100%, some items the partner might be expected to fund 100%, with other items in-between. In interviews, SHARPE staff said that the approach of 'you pay for this, we'll pay for that' was partly to reduce the burden of administering the grant. SHARPE also aims to cost-share items that are easier to verify, and that are more critical for success. SHARPE may also ask the partner to pay 100% of the cost of an earlier budget item in order to demonstrate commitment. One of the partners interviewed described the negotiations as "tough". However, another partner admitted that they would have accepted a 50% cost-share rather than the 58% agreed.

The SHARPE Partnership Manual provides guidance on the 'expected' cost-share (50:50), but not the factors that might drive an upward or downward deviation from this, and no benchmarks are used by the team when negotiating the cost-share. Cost-shares are negotiated on a case-by-case basis. There is a general understanding within SHARPE that cost-shares need to be higher for micro and refugee-owned enterprises. However, beyond this there is no comprehensive guidance for team members regarding the factors that might necessitate or justify a higher or lower cost-share.[12] The cost-shares from previous SHARPE grants have also not been analysed, data which could be used to develop historical benchmarks to guide negotiations. In interviews, several team members noted the uniqueness of each partnership and context, making it difficult to adopt a 'formulaic' or 'rules-based' approach to cost-share negotiations.

The initially short time horizon for the programme and delays to implementation due to Covid, combined with ambitious impact targets, may have contributed to more generous cost-shares. SHARPE was initially contracted for only three years, and the early years of the programme were hampered by Covid. In interviews, several SHARPE team members noted that the need to deliver impact in a relatively short timeframe created a pressure to finalise grant agreements quickly and to speed implementation with grantees. This resulted in more generous cost-shares than might otherwise have been the case.

Learning and insights from the monitoring system are used by SHARPE to adapt the support provided and to help grantees themselves to learn and adapt. As well as tracking milestones in the grant agreement through the finance system, the SHARPE monitoring system tracks: the extent to which grantees adopt and sustain (six-months after the end of the grant) the desired practice changes; how many people are

11 For example, the Deal Note for SMFI (now Shabelle Bank) includes a condition to recruit 35% female mobile money agents, but the Deal Note does not consider the 'business case' for the partner to do so, or how the grant will be used to test the 'business case'.

12 The PRISMA and ALCP partnership guidelines both set out the factors which would justify a higher or lower cost-share, such as: the partner's financial capacity, the risk profile of partner, the perceived risk of the intervention, the anticipated impact, sustainability (higher support can be justified for one-off activities), and whether the intervention has a public-good aspect. See also Table 1 in the Annex.

reached (disaggregated by refugees, hosts, and women); and the ultimate impact for target groups. SHARPE also seeks to generate insights and learning regarding the business models and innovations being tested; if a grant has not delivered the results expected, this can include undertaking additional on-the-ground research to understand why.[13]

2.3: How effective the use of subsidies for private sector actors has been

Grants, alongside market linkages and on-the-ground facilitation, have been effective in catalysing larger companies to adopt and test practice changes targeting refugee and host communities. Of the large companies selected for analysis by the study team, all four had adopted and tested practice changes targeting refugee and host communities. Interviews with grantees suggest strong additionality: without SHARPE support, the companies would not have adopted these changes by themselves. For all four companies (with the possible exception of Ethio-chicken who had undertaken a few small investments in the target markets prior to SHARPE), the host and refugee market represented unknown, 'frontier' markets. As such, the SHARPE grants played a critical role in de-risking the initial investments required to test these new markets. Beyond the grants, several interviewees also stressed the importance and value of the linkages SHARPE was able to broker, with small and medium regional companies who could act as wholesalers or agent hubs and/or with host and refugee-owned micro-enterprises. In several cases, the ability of SHARPE to provide on-the-ground intelligence and facilitation support, particularly around access to refugee camps, also seems to have been vital. Based on an analysis of the partnership status tracker maintained by the SHARPE monitoring team, excluding recently signed grants, 90% of medium and large companies adopted the desired practice changes.

13 For example, in the case of Shabelle Bank, there were initial concerns around the higher number of inactive agents in the host and refugee target markets. Research by SHARPE highlighted a number of issues, such as problems with agent liquidity. These findings were fed back to the SHARPE team (to inform the next round of support), and to the grantee, thereby supporting the partner to adapt the model.

Box 3: examples of the practice changes implemented by SHARPE grantees

Shayashone built-out new supply chains for its agro-input products targeting 'frontier' host and refugee communities in two regions. This included building a network of distributors and undertaking various marketing and demonstration activities to build awareness of their products. In interviews, the CEO stated that SHARPE had reduced the risk of entering these market and that, without SHARPE, they would not have made the changes they did.

Under an initial round of grant support, **Shabelle Bank** "deepen its DFS/Hello Cash network to more distant and scattered refugee hosting woredas in Jijiga and Dollo Ado at an accelerated pace that would have been impossible without SHARPE support".* Under a second round of grant support, Shabelle Bank also opened satellite branches in or adjacent to four refugee camps in order to better serve the host and refugee market and to address liquidity issues for its refugee and host Hello Cash agents. In interviews, senior bank staff stated that they already had plans to expand in the Somali region but that the support from SHARPE added a new focus on host and refugee markets.

Hello Solar expanded its distribution and sales agent networks to cover host communities and refugee camps. The company also adapted its payment terms to allow for a lower upfront cost and longer repayment terms in order to improve affordability for refugees.*

Ethio-chicken has built-out its sales and service model to host and refugee communities in two regions, including the establishment of 32 Mother Units to supply Day Old Chicks (DOCs) to host and refugee poultry farmers.*

Notes: * Bear, M. (2022): 'A Review of SHARPE'.

Grants have been made more effective by the ability of SHARPE to generate insights and learning on what is and is not working, and supporting grantees (and SHARPE itself) to adapt accordingly. As noted above, many of the national and regional companies supported by SHARPE had no experience of serving host and refugee communities. At the start of the programme, SHARPE staff themselves also did not know for certain what innovations would work best and how these might need to be adapted across the three target regions. SHARPE therefore placed a strong emphasis on generating insights and learning on what is and is not working, both through on-the-ground research and through the SHARPE monitoring system. There are multiple examples of the insights generated being fed-back to the grantee, thereby helping them to adapt their business models.

Grants have been effective in building the capabilities of larger companies to serve host and refugee communities through 'learning-by-doing'. Aside from the examples provided above, the grant support from SHARPE has also enabled companies to build their own knowledge of how best to serve host and refugee markets. For example, in interviews Shayashone management cited learning around how to adapt the size and pricing of vegetable seed packets in order to make them more affordable to refugee farmers.

After buying-down the initial risk, SHARPE grants have also been effective a catalysing an underlying shift in motivations in larger companies regarding target markets, suggesting a high degree of sustainability (at least in relation to host markets). For example, in interviews Shayashone management reported being excited by the prospects in Gambella and described the newly expanded supply chain in the region as a "critical cornerstone we will leverage in the future". In interviews, Shabelle Bank appears to be optimistic that the new satellite branches will improve the performance of its host and refugee agent network and has plans to make further investments in these markets. However, in several of these cases SHARPE grantees are more convinced about the case for serving host communities, with the case for serving refugee communities still uncertain or unproven (see below).

Understandably, larger companies have been more likely to target host than refugee markets; SHARPE has been able to steer grantees towards the refugee market during the lifetime of the grant, although post-grant, the early evidence as to whether companies will continue to target the refugee market is mixed (especially for national Addis-based companies). As noted in interviews with SHARPE staff, larger companies are understandably often more drawn to host than refugee markets. Host communities are typically easier to reach, face fewer restrictions or administrative barriers, have higher incomes, and have higher assets. To ensure that grantees reach both host and refugee markets, SHARPE often includes conditions in the grant agreement regarding the inclusion of refugees. The actual levels of inclusion are monitored by SHARPE, which seeks to 'nudge' grantees towards including more refugees if results are less than expected (see Section 2.2). According to one SHARPE interviewee, the actual reach of grantee companies is roughly 25-30% refugees, 70-75% hosts, and a current focus of the programme is to increase this ratio.

Although there are examples of SHARPE successfully nudging grantees to target more refugees during the lifetime of the grant, post-grant the sustainability of these efforts will depend on the 'business case' for firms to continue to target refugees, and the practicalities of doing so when SHARPE is no longer able to provide the on-the-ground facilitation support.[14] As noted in the recent review of SHARPE:

"Ethiopia's private firms will continue to invest in new market expansion and form long term business / trading relationships with businesses in refugee hosting communities with little or no direct SHARPE support... However, far fewer refugee community consumers and suppliers of goods and services have benefitted from SHARPE's private sector partners. This is partly because it takes time to learn and adapt business models to refugee economies but, most importantly, the private sector continues to face access and formalization barriers when partnering with refugee businesses without SHARPE support."

Interviews with SHARPE staff suggest that for medium and large companies, firms based in the region are more likely to sustain the investments in refugee (and host) communities than national, Addis-based companies. Regional companies tend to be more invested in the local economy whereas national companies can easily pause expansion efforts or shift to other markets. SHARPE has sought, where possible, to increase grantees' long-term commitment to the target markets.[15]

In some cases, SHARPE grants and the wider package of support could have been more effective by more clearly targeting the company's underlying 'capability', 'opportunity', and 'motivational' constraints (including more active consideration of external Technical Assistance and alternative forms of public subsidy). As noted above, targeting host and refugee markets was new to many of the larger companies receiving SHARPE support. The general approach employed by SHARPE has been to use grants to buy-down the risk of entering these unknown markets and incentivise firms to 'test the water'. However, as new markets, companies also faced 'capability' constraints in terms of how best to adapt their business models in order to effectively and profitably serve these new markets. As summarised above, firms have been able to build their capabilities themselves through 'learning-by-doing', helped along in many cases by research and insights provided by SHARPE. Aside from this, SHARPE has made relatively limited use of Technical Assistance which is a more direct way of tackling 'capability' constraints in firms. Where financial subsidies have been used by SHARPE, they have been in the form of a cost-share grant. This form of subsidy is well suited to buying-down the risk associated with any sunk-cost investment the firm is required to make in order to enter the target markets (such as building satellite bank branches, or investing resources in developing an adapted product or service offering). However, cost-share grants are a less direct way of tackling 'transaction' risk, which are best tackled through risk-guarantee mechanisms.[16] These alternative forms of public subsidy do not appear to be actively considered by the SHARPE team.

In the case of regional and micro host and refugee-owned businesses, grants or subsidised loans plus market linkages and other support, have been effective in supporting these businesses to upgrade, expand, and integrate into supply-chains. According to an analysis of the partnership status tracker, aside from the 'too early to tell' category, 94% of host and 100% of refugee owned grantees have adopted the practice change (with 8% adopting then later dropping the practice change – see below). As with larger grantees, alongside the grant support

14 For example, while Shayashone management indicated an intention to expand further in Gambella, they are still as yet uncertain about the extent to which they will continue to target refugee communities.
15 Cost-sharing with Shabelle Bank to open satellite branches in refugee camps is a good example.
16 For a good example of a risk-guarantee in-practice, see: FSD Kenya (2016): 'The Growth of M-Shwari in Kenya – A Market Development Story: Going digital and Getting to Scale with Banking Services'.

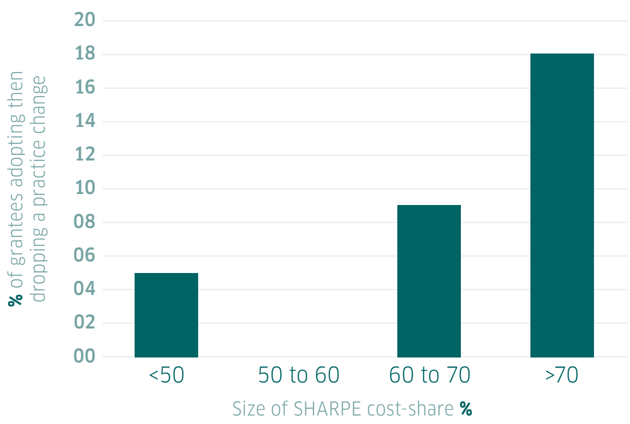
or subsidised loans the market linkages plus other on-the-ground support provided by SHARPE appears to have been particularly valuable for many host and refugee grantees.[17]

In some cases, the use of reimbursable grants has created a barrier for refugee-owned enterprises to make the necessary up-front investments. As noted in Section 2.1, the vast majority of grants have been in the form of reimbursable grants. This requires the grantee to fund 100% of the up-front cost of implementing the practice changes; once the corresponding milestones have been verified, they are then able to claim back the cost-share from SHARPE. In interviews, several SHARPE staff expressed a preference for reimbursable, milestone-based grants, stating that they did not want to give grantees "a blank cheque", and that "making things somewhat difficult" for the partner provides a useful test of commitment. However, given that refugees often face significant constraints in accessing finance – which is often why the grant is justified in the first place – the use of reimbursable grants can mean that refugees are unable to overcome these constraints.[18]

Many of the refugee-owned businesses have been able to maintain the practice changes post-grant, although the vulnerability of refugees to shocks means some refugees have been unable to sustain their businesses. In the case of poultry, the SHARPE annual review found that 16 out of 32 refugee poultry farmers were operating independently of SHARPE.[19] Of the three refugee poultry farmers interviewed by the study team, two out of three were still active, despite the protracted rations crisis. In the one drop-out case, the family had been forced to sell the chickens to a neighbour due to a period of illness for the husband and unexpected medical bills for several of the children (on top of the rations crisis). However, they expressed a desire to re-enter the poultry business once their finances improved – the construction of a poultry shed appears to have created a strong on-going commitment to the business model.

Across the whole portfolio, early evidence suggests that host and refugee-owned enterprises are less likely to adopt then drop practice changes than other firms, and that high costs shares for larger firms increase the likelihood of unsustainable outcomes. By combining data from the grant tracker with data from the monitoring systems it is possible to undertake an analysis of how the rate of adopting and sustaining practice changes varies across the portfolio. Given that many of the grants provided by SHARPE are relatively recent, many of the grantees are classified as 'too early to tell' by the monitoring system. Excluding these, the data suggest that host and refugee-owned enterprises are less likely to adopt then drop a practice change (8% of host and 8% of refugee grantees) than 'other' companies (20%). The data also suggests that grantees receiving a high cost-share are more likely to adopt then drop a practice change: where the cost-share was less than 50%, only 5% of grantees adopted then dropped a practice change, versus 18% of grantees where the cost-share was greater than 70% – see Figure 2. If the analysis is repeated for medium and large enterprises only, two-thirds of the grantees receiving a cost-share of 70% or more adopted then dropped the practice change.

Figure 2: the percentage of grantees adopting and then dropping a practice change, by the size of the cost-share



Notes: excludes grantees classified as 'too early to tell'.
Source: SHARPE grants tracker, partnership status tracker, and study team's calculations.

It is important to note that the size of the cost-share is unlikely to be the main determinant of whether a partnership is successful and sustainable. In interviews, SHARPE staff were of the view that the ethos, spirit, and vision of the company was the most important factor.

Although there is not yet any systematic evidence of wider market-level impacts, in several cases grants from SHARPE have helped to build networks and infrastructure that will benefit other companies in the market – thereby further bolstering the case for public subsidy. In the case of Shayashone, the sales agents in their network are non-exclusive.

17 In the case of the three refugee poultry-farmers interviewed, for example, all three had managed to build a chicken shed (with a SHARPE cost-share) and had also established linkages with Horn Afrique, another SHARPE partner, who supplies them with Day Old Chicks and feed, provides on-hand advice, and has bought-back the chickens to sell for meat once they are no longer productive.

18 For example, in interviews with SHARPE staff, examples were given of poultry farmers in Aw-Barre camp being unable to raise the capital needed to start construction of the poultry shed.

19 FCDO (2023): 'Annual Review: Support to Refugees and Migration in Ethiopia'.

The expansion of Shayashone's agent network to host and refugee markets has therefore potentially benefited other agro-input suppliers and made it easier for them to target the market should they so wish. This already appears to be happening in the case of Shifo Agro-Vet, part of Shayashone's expanded sales network, which has increased its sales of veterinary drugs provided by other agro-input companies. Similarly, Shabelle Bank's Hello Cash agents are non-exclusive, potentially benefiting other DFS providers wishing to target these markets.

3. Key lessons and recommendations

This section summarises the key lessons from SHARPE, combined with lessons from the external literature. The section also includes a set of recommendations for future programming in this area, both in Ethiopia and in comparable contexts.

Overall programme strategy-setting

Grants and other forms of support need to be deployed within an overall strategy for each priority supply / value chain, with support provided to actors along the chain – including large national companies, small and medium regional companies, and refugee-owned micro-enterprises. As noted in Box 2, market systems programmes have typically eschewed working directly with target groups, generally preferring to work with larger actors who can generate the required scale. However, in the case of programmes targeting host and refugee communities, often in very specific geographic areas, this approach may not work. As noted in interviews with one SHARPE team member, one of the key learning from SHARPE has been the need to work along the whole supply chain, including with host and refugee enterprises, otherwise interventions risk not reaching the intended target groups. In terms of the external literature, there is a growing body of evidence that this kind of approach, sometimes referred to as a 'push-pull' strategy, is the best way of generating sustainable impact in the context of protracted displacement (versus 'push-only' market systems programmes or 'pull-only' humanitarian livelihoods programmes):

"Interventions should be aimed at combining 'push' and 'pull' factors. 'Push' factors aim at building the capacities of the target group to engage with the market, for instance through skills development, transfer of assets and/or strengthening social networks, while 'pull' factors focus on developing market systems in such a way as to expand and diversify the market opportunities available to both the target group and the host community." [20]

As noted in the 2017 UNHCR / ILO paper, "to achieve economic inclusion in a sustainable way, interventions should be based on a thorough analysis of the existing demand for labour, products and services, and of market systems in which refugees could make a living."

Recommendation 1: Programmes wishing to sustainably improve the livelihoods of host and refugee communities in the context of protracted displacement should combine market systems development principles with direct targeting of large market actors, small and medium regional actors, and micro and host and refugee-owned enterprises. This should be underpinned by a robust and regularly updated market systems analysis of priority sectors / value-chains.

Identifying private sector actors to support

Given the 'donor-heavy' context, it has been particularly important for SHARPE to proactively seek out genuinely committed larger companies, and entrepreneurial host and refugee business owners, and to test their commitment early on. Through its proactive engagement with Addis-based companies and regional companies, SHARPE has for the most part succeeded in identifying potential partners that are genuinely interested in targeting host and refugee markets (albeit with the need for an initial cost-share to buy-down risk). The ability to 'speak the language of business' was also highlighted as an important factor in deciding whether to partner with SHARPE by several grantees. With regards to identifying host and refugee-owned enterprises to support, SHARPE took a similarly proactive approach, this time through their on-the-ground teams in each of the three target regions. Unlike humanitarian programmes which use a needs-based approach to identify 'beneficiaries', SHARPE actively sought out the more capable and entrepreneurial hosts and refugees who were committed and ready to invest in and upgrade their businesses. SHARPE is unlikely to have achieved the same success if it operated on a Challenge Fund model with a 'lean' Addis-based core team issuing call for proposals. The requirement for cost-sharing and the focus on only funding

20 Nutz, N. (2017): 'A Guide to Market-Based Livelihood Interventions for Refugees', UNHCR / ILO. See also ILO / UNHCR (2023): 'The Humanitarian Development Nexus in Action: A Review and Mapping of Market-Led Approaches in Forced Displacement Contexts'

‘innovation’ (not ‘more of the same’) was also designed to exclude actors not committed to the change process or only looking for cheap donor funding (see below).

Recommendation 2: programmes should adopt a proactive approach to identifying and engaging private sector partners and test their commitment through cost-sharing, particularly when operating in ‘donor-heavy’ context. This requires a strong core team with on-the-ground presence in the main economic hubs as well as in the target host and refugee markets.

Designing the package of support

Grants can be effective in catalysing practice change in private sector actors, large and small, but should be combined with market linkages, on-the-ground facilitation, and external Technical Assistance (as needed). The experience of SHARPE has demonstrated that grants can be an effective way of incentivising larger companies to develop and test new business models targeting host and refugee communities and to ‘test the water’. Given that these markets are often new or untested for these companies, cost-sharing grants are a good way to buy-down the initial risk. This approach to facilitating business expansion of established market players is a common approach among programmes working in ‘thin’ or ‘nascent’ markets:

> **“As nascent markets are characterized by few existing businesses within a given sector, additional emphasis must be placed on encouraging existing entrepreneurs from other regions to expand into ‘new’ markets. For example, in Ethiopia this could mean facilitating the movement of businesses from the highlands to expand their services (i.e. retail outlets for solar products) into the lowlands.”[21]**

Many of the grantees interviewed for the study also highlighted the importance of the market linkages brokered by SHARPE, and the on-the-ground facilitation support provided by the SHARPE regional teams. Again, this chimes with the experiences of other programmes working in ‘thin’ markets:

> **“Besides facilitating the movement of existing businesses from other regions into the thin market region, projects working in nascent markets may also need to emphasize creating linkages between businesses inter-regionally.”[22]**

However, SHARPE has made relatively limited use of specialist external Technical Assistance. Other programmes working in ‘thin’ market contexts emphasise the importance of Technical Assistance as a facilitation tool. For example, the HMG-funded ÉLAN RDC programme in DRC recommends:

> **“Invest[ing] to prepare businesses for growth and innovation. Business, operational and financial management capacities are often limited among actors in thin markets… Recognising limited partner capacity, ÉLAN RDC developed an in-depth business and financial advisory support offering, helping partners to prepare for growth and to systematize innovations. ÉLAN RDC’s support to partners often went above that which would typically be required in other, more mature markets to include strengthening internal management structures, tools and teams that necessarily underpin sustained, commercial growth.”[23]**

Recommendation 3: programmes should co-create ideas with potential partners and undertake a diagnostic of each potential partner to understand their ‘capability’, ‘opportunity’, and ‘motivational’ constraints to adopting the desired practice changes (see Annex). Staff should actively consider a wide range of ‘facilitation tactics’ in developing the package of support, which should be designed to tackle the specific constraints facing each partner. The menu of possible facilitation tactics should include cost-share grants, but also other forms of financial support such as risk-guarantee mechanisms, as well as brokering linkages, on-the-ground facilitation support, and external Technical Assistance.

21 PRIME / Mercy Corp: ‘Facilitative Approach for Nascent Markets’.
22 PRIME / Mercy Corp: ‘Facilitative Approach for Nascent Markets’.
23 Beevers, K.: ‘Market Systems Development in Thin and Crisis-Prone Markets’. See also: PRIME / Mercy Corp: ‘Facilitative Approach for Nascent Markets’, and the ‘thin markets’ guidance on the BEAM Exchange.

Setting the grant policies, processes, and procedures

It is important to have a clear set of grant policies, processes, and procedures, which should be adapted to the context of host and refugee markets. SHARPE has developed a clear policy regarding the use of grant-funding, with a strong focus on catalysing 'innovation' (not 'more of the same'). SHARPE has been more willing than other market systems programmes to cost-share physical assets and infrastructure. This appears to be entirely justified given the 'thin' market context and has been part of a deliberate strategy to increase the long-term commitment of companies to host and refugee markets (the opening of satellite branches in or adjacent to refugee camps by Shabelle Bank is a good example). It is also justified when supporting host and refugee enterprises, which often lack access to external sources of finance to make the necessary upfront investments to upgrade their businesses. The inclusion of conditions for larger grantees regarding the targeting of hosts and refugees also appears to have been useful, although more focus could be given to setting-out the 'business case' for targeting hosts, refugees, and women. SHARPE could also improve the way it communicates its approach and policies to potential partners, to avoid frustrations when negotiating new or follow-on grant agreements.

SHARPE also successfully adapted its administrative and due-diligence processes – for example, through the introduction of 'micro' grant agreements – which has allowed it to provide support to relatively large numbers of refugee grantees while still providing the necessary assurance and oversight. On-the-ground support to potential grantees, such as helping refugee entrepreneurs open bank accounts and obtain the necessary licenses, has also been critical. One area for improvement is perhaps the near-default use of reimbursable grants, which potentially limit the effectiveness of the grant where refugee grantees face insurmountable access to finance constraints (and are therefore unable to fund 100% of the upfront investment).

Recommendation 4: programmes should adopt a clear grant policy, with a strong focus on innovation, additionality, and sustainability. The grant process should also consider the 'business case' for targeting hosts, refugees, and women (as appropriate), and actively consider the potential wider systemic impacts (positive and negative). The programme's approach and policies should be clearly communicated to potential partners. Programmes should also ensure that their administrative processes allow them to effectively administer a potentially large number of small grants to host and refugee enterprises, potentially including those outside the formal sector, and that on-the-ground support is available to potential grantees to pass the necessary due diligence checks. Programmes should also be flexible in how grants are structured, for example by relaxing any requirement for reimbursable grants in cases where host and refugee enterprises face external financing constraints.

Cost-sharing

Cost-sharing is a principle that is equally applicable to large companies and to host and refugee-owned micro-enterprises; although higher cost-shares seem warranted by the context, programmes should be cautious about providing high cost-shares to larger companies. The basic purpose of cost-sharing is to test the commitment of the grantee and increase their sense of ownership. By leveraging private sector investment, cost-shares also increase value for money for the donor. In contrast to humanitarian livelihood approaches, SHARPE has demonstrated that the principle of cost-sharing can be applied to host and refugee entrepreneurs as well as larger companies. The cost-shares provided by SHARPE appear to be higher than other market development programmes, but not higher than other programmes operating in 'thin' markets or in host and refugee contexts. Refugee (and host) enterprises will generally require a high cost-share given the serve access to finance constraints they face. Larger companies may also require a higher cost-share than in other contexts given that host and refugee markets are often unknown and untested. However, early evidence from SHARPE suggests that programmes should remain cautious about providing high cost-shares (above 70%) to larger companies, which are more likely to result in unsustainable outcomes.

The lessons from SHARPE mirrors the emerging external evidence:

"The principle of using 'smart' subsidies should be maintained as much as possible in displacement contexts to achieve sustainability and scale... [However] using higher subsidies with the private sector risks the sustainability of the business model, impacting on the success of the project in its reach and scale."[24]

24 ILO / UNHCR (2023): 'The Humanitarian Development Nexus in Action: A Review and Mapping of Market-Led Approaches in Forced Displacement Contexts'

Recommendation 5: programmes should maintain the principle of cost-sharing, but be willing to provide higher-than-average cost-shares, particularly to host and refugee micro-enterprises. Caution should be maintained when considering high cost-shares for large companies.

Although a fully formulaic or rules-based approach to cost-sharing may not be feasible, programmes should provide staff with guidance on the factors that would justify a higher or lower cost-share and develop benchmarks to guide cost-share negotiations. Evidence from interviews and the external literature suggests that a fully rules-based or formulaic approach to negotiating the cost-share is not possible given the multitude of different businesses, innovations, and contexts supported by a programme like SHARPE. However, it may have been useful to provide SHARPE staff with cost-sharing benchmarks (both from historical SHARPE grants and from comparable projects in Ethiopia and elsewhere) and written guidance on the factors determining why the cost-share might deviate from these benchmarks (see Table 1 in the Annex for an example). The Deal Notes could also provide a clearer justification for the proposed cost-share and any deviation from benchmarks.

Recommendation 6: programmes should develop guidance and benchmarks to assist staff in the negotiation of cost-shares with grantees.

Monitoring, learning, and adapting

A flexible and adaptive approach, underpinned by a robust research and monitoring system, will increase the overall effectiveness of grants and other support to private sector actors. SHARPE has demonstrated the value of building a robust research and monitoring function, combined with an organisational culture of curiosity and proactive problem-solving. There are numerous examples of insights and learning generated by SHARPE being used by grantees to adapt their business models, thereby improving reach as well as the likelihood of sustainable outcomes. Learning is also used by SHARPE to adapt its package of support or when negotiating follow-on grant agreements. This is especially important in the context of host and refugee markets, where there is limited existing evidence on exactly which business models will work best, and how they should be adapted for different geographic contexts.

SHARPE could potentially improve its tracking of actual partner spend. Some market development programmes routinely track and report on private sector investment leveraged,[25] although SHARPE interviewees pointed to the challenges of doing so for the large number of grants administered by SHARPE. One approach might be to focus on larger companies, where it will be easier to obtain the required data and supporting evidence.

Recommendation 7: programmes should adopt a flexible and adaptive approach, underpinned by a robust research and monitoring system and a culture of curiosity and evidence-based decision-making. The package of support provided, including grant and non-grant support, should be adapted as needed based on on-going monitoring of what is and is not working on-the-ground. Programmes should also actively support enterprises to learn and adapt their business models, especially larger companies for whom host and refugee markets are often unknown and untested at the start of the partnership.

25 See, for example, the annual reports produced by the DFAT-funded Market Development Facility (MDF) which operates in Pakistan, Sri Lanka, Timor Leste, Fiji, and Papua New Guinea.

Annex: conceptual framework

The Annex starts with a definition of the key terms used in the study, then presents a conceptual model of how financial subsidies can be used to catalyse change in private sector actors. The Annex ends by looking at how the level of public subsidy necessary may vary depending on a variety of internal and external factors.

Definitions

Following DFID (2011), a 'private sector actor' is defined as: "a business or organisation which is established or operated with the primary intention of making a profit". The term encompasses "for-profit companies, companies, businesses, and firms".[26] For the purpose of this study, this includes both formal and informal enterprises, including refugee-owned micro-enterprises.

'Public subsidies' or 'financial subsidies' are defined as the transfer of financial resources from the public sector (in this case, from FCDO via the SHARPE programme) to private sector actors. This includes all forms of grants, returnable grants, cost-sharing, concessional finance, and risk guarantees. The term excludes the provision of Technical Assistance or other forms of knowledge transfer. Private sector actors that have received financial subsidies from SHARPE are referred to as 'grantees'.

Conceptual model

Following the COM-B model of behaviour change,[27] the practices and behaviours of private sector actors are driven by three factors:

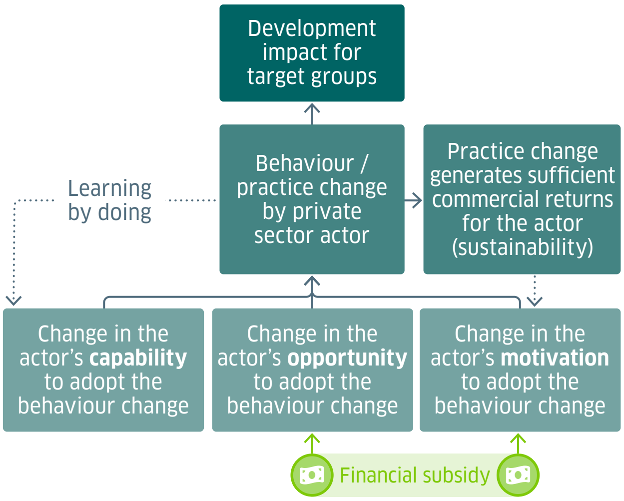
- **Capabilities** (or capacities) – the actor's knowledge, skills, and abilities;
- **Opportunities** – external factors which make the adoption of a given set of practices possible or viable; and
- **Motivations** (or incentives) – the actor's short and long-term goals, appetite for risk, and other decision-making processes, both reflective and automatic (including biases and beliefs).

Market development programmes such as SHAPRE aim to use financial subsidies (and other non-financial types of support) to catalyse the adoption of new or improved practices or behaviours in private sector actors that both: (1) generate a sufficient commercial return, at an acceptable level of risk, for the actor itself, and (2) generates or contributes to development impact for target groups.[28] Condition 1 is necessary if the practice change is to be sustained and scaled-up by the actor beyond the end of programme support. If condition 1 is met, this can also lead to the replication of the practice change by other private sector actors not directly supported by the programme, contributing to wider market-level change.

Financial subsidies can catalyse practice change through two mechanisms – see Figure 3. Firstly, financial subsidies can be used to change the motivations of private sector actors to adopt a given practice change. For example, where a potential practice change is considered too high-risk by the actor, or has unknown or untested returns in the given operating context, financial instruments such as cost-shares or risk guarantees can be used to buy-down risk, thereby removing motivational blockers of change, at least temporarily. For financial subsidies to lead to a permanent shift in an actor's motivations, the practice change, once adopted, must generate a sufficient commercial return (represented by the right-hand dotted arrow in Figure 3).

Secondly, in the context of constrained internal and external sources of finance, financial instruments such as grants can change the opportunity for private sector actors to adopt a given change by providing the necessary financial resources.

Figure 3: conceptual model of using financial subsidy to catalyse behaviour change



26 DFID (2011), 'DFID Policy Framework for the Provision of Grants or Concessional Finance to For-Profit Firms'.
27 Michie, S., van Stralen, M., West, R. (2011): 'The Behaviour Change Wheel: A New Method for Characterising and Designing Behaviour Change Interventions'.
28 In the case of SHARPE, target groups are individuals in host and refugee communities in three regions in Ethiopia: Dollo Ado, Gambella, and Jijiga.

Note that financial subsidies are not primarily designed to address capability blockers of change, which are more directly addressed by Technical Assistance. However, financial instruments may lead to indirect or second-order changes in an actor's capabilities, for example through learning-by-doing (represented by the left-hand dotted arrow in Figure 3), or where some of the subsidy is used to acquire consultancy or advisory services.

Factors influencing the size of the public subsidy

The conceptual model can be used to make predictions regarding how the size of the public subsidy necessary to catalyse the desired practice change will vary depending on different internal and external factors – see Table 1.

Table 1: implications of internal and external factors for the size of the public subsidy

Factors	Implications for the size of the public subsidy
Nature of the behaviour / practice change	
Level of innovation	Practice changes that are more innovative or untested in the market context entail higher risk and uncertainty for the company (motivation), necessitating a higher subsidy
Sunk-cost*	Practice changes with a large sunk-cost component entail higher risk for the company (motivation), necessitating a higher subsidy
Capital requirements	More capital-intensive practice changes have higher initial financing requirements (opportunity), necessitating a higher subsidy
Nature of the actor	
Size of the company	Larger companies are better able to raise the necessary internal and external finance (opportunity) and companies with multiple revenue streams and markets have lower risk (motivation), necessitating a lower subsidy
Risk appetite	More innovative firms with a higher risk appetite (motivation) will require a lower subsidy
Company capabilities	More capable companies will have lower execution risk (motivation), necessitating a lower subsidy
Non-financial motivations	Companies that also have social-impact objectives may require a lower subsidy
Contextual factors	
Macro-economic conditions	In a more unstable or unfavourable macro-economic context, companies will be less willing and able to invest (motivation / opportunity), necessitating a higher subsidy
Financial system	In countries with an undeveloped financial system with low accessibility of affordable and appropriate financial services, companies will be less able to raise the necessary capital (opportunity), necessitating a higher subsidy
Conflict and fragility	In conflict-prone and fragile contexts, companies will be less willing to invest (motivation), necessitating a higher subsidy

Notes: * 'sunk costs' are costs borne by the company that cannot be recovered, for example by selling or repurposing the assets or investments made.

Beyond the factors predicted by the conceptual model, the external literature points to several other factors that may influence the size of the public subsidy. These stem from the recognition that agreeing a financial package with a private sector actor involves a degree of negotiation between the company and the donor programme. Companies are likely to have more negotiating power in the following contexts:

- **'Thin' markets.** In these contexts there may be few or even no private sector actors operating in the target markets that the programme can work with. In these markets, given the limited choices available, actors may be able to negotiate higher subsidies than would otherwise be the case. Programmes may also need to incentivise larger firms to enter the target markets which, as they are untested for the firms in question, may also necessitate a higher subsidy (as per Table 1).

Companies are also likely to have lower capabilities and lower access to finance, again necessitating higher subsidy.[29]

- **'Donor-heavy' markets.** In markets where there are many donors active, chasing relatively few private sector actors, a programme may need to offer a higher subsidy than would otherwise be the case. This will be especially true if companies are used to receiving generous subsidises with low or even no cost-share requirement.[30]

29 This argument is also made in Mercy Corp / PRIME: 'Facilitative Approach for Nascent Markets', and in the guidance on 'thin markets' on the BEAM Exchange.

30 See Helvetas Eastern Europe (2015): 'How to Develop Effective and Realistic Market Systems Strategies in a Donor-Heavy Environment'.

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