Dalberg

FMO
Entrepreneurial
Development
Bank

Evaluation of Progression Model

2024

FINAL REPORT (SHORT)

Executive summary

Objective, Approach and Methodology

- This evaluation study aims to **better evidence how successful or not FMO's progression model has been** - specifically, how customers starting with public funding move to FMO-A and further commercial mobilization. In the process, it also **establishes a baseline for progression**
- We collated and analyzed **quantitative and qualitative inputs from diverse sources** to define the scope of our evaluation and answer the key evaluation questions

Key progression trends and contributors

- **Of the 230 customers in scope of our study**, over **62 customers progressed to receive FMO-A** investment (L2), while a further **18 progressed to also receive commercial funding (L3)** [1]
- Relatively **higher levels of progression were observed in Asian countries and among banks**. Customers from Building Prospects (BP) saw lower progression vs those from other funds
- Progression is **influenced by market stability (economic and socio-political), alongside customer factors** like track-record, governance quality, and green operations
- Evidence suggests that **FMO's investment strategy and various forms of financial or non-financial support aid progression** when tailored to customer's market and customer context. Within the confines of limited available evidence, **FMO engagement is also linked to improved SDG impact contribution by stagnated customers**

Learnings and recommendations

- Our evaluation of FMO's progression model uncovered a **few key challenges** which limit its efficacy and operationalization
- To overcome these challenges and collectively unlock the potential of the progression model at scale, we propose that FMO
  - **Clearly articulate contribution of progression** to FMO business priorities
  - **Specify how** progression **steers fund-level** action
  - Determine **progression Monitoring Evaluation Learning (MEL) strategy**
  - Build awareness of and advocate for progression
  - Broaden FMO's role in driving and leveraging progression
- Additionally, **enhancements to people and data processes & systems** will be essential to execute the proposed strategic refinements
- Implementing these proposed recommendations would require additional time, resource, and effort investment. **Starting small**, retaining avenues for **flexibility**, and **rationalizing priorities** will help mitigate against this risk

Note: (1) There were an additional 37 customers who originated at L2 blend with public funds, who were also in the scope of our study.
Evaluation of FMO's impact or additionality is not in the scope for this engagement. Further, 'market creation' is not in the scope for this engagement

Project context and objectives

CONTEXT OF THE PROJECT

- The **‘progression model’**, a cornerstone of FMO's 2030 strategy, **‘Pioneer-Develop-Scale’**, aims to graduate portfolio customers from pre-bankability to commercial viability
- The **four stages of the progression model** are (1) market creation, (2) public funding, (3) FMO-A, and (4) commercial mobilization
- However, there is a lac**k of aggregate quantitative and qualitative evidence** on whether and why customers financed by public funds are progressing (or stagnating) in the ‘progression model’
- This **evaluation study aims to better evidence the ‘progression model’**, from public funding (2) through to commercial mobilization (4) without accounting for market creation interventions[1]. The study will also serve **accountability purposes to the Dutch Ministry of Foreign Affairs**
- Additionally, conventional beliefs suggest that efforts to drive progression also benefit customers in ways beyond explicit progression. FMO is hence keen to understand the **value of its efforts in driving positive momentum/ growth for customers** originating in stage (2), public funding

OBJECTIVES OF THE PROJECT[2]

- Assess **progression at a customer level** (not at a sector or country level), by quantifying **the extent to which customers** in FMO’s portfolio have progressed. This excludes the quantification of other types of progression such as sector-level, transaction-level, etc.
- Report the **average time for progression** for customers, nuanced by differences in sectors, sub-sectors, countries, etc.
- Identify the **factors that contribute to the progression or non-progression** of a customer
- Develop **in-depth case studies** for customers that successfully progressed versus those that stagnated
- Unpack what other intended and unintended **positive developments, apart from progression**, can be realized by investment of public funds even if customers stagnate (and how).
- Identify **areas for refinement** of the progression model

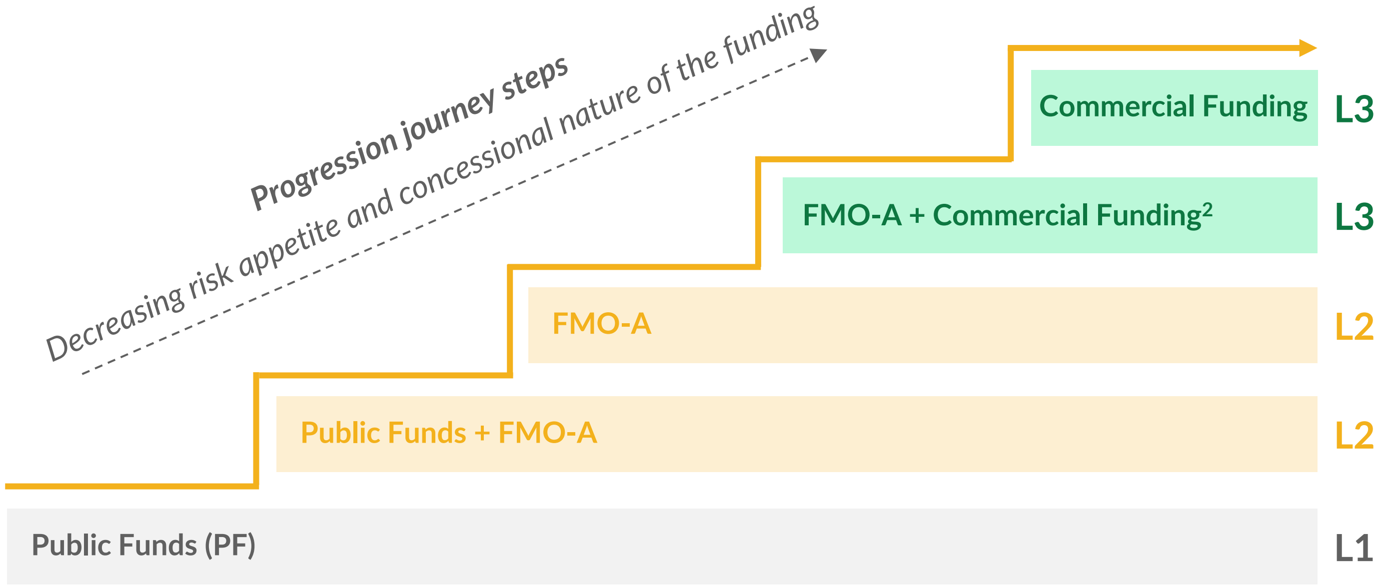
Notes: (1) Market creation was not explicitly covered in the scope of this evaluation, even as some market creation efforts may be underway in parallel that support an investment (2) Evaluation of FMO’s impact or additionality is not in the scope for this engagement. Further, ‘market creation’ is not in the scope for this engagement

Through key stakeholder conversations, we aligned on a common definition of progression, spanning 3 distinct levels, for the purpose of this study

Definition of Progression

For this study, progression is defined[1] as the **participation by more risk-averse or non-concessional investors** in companies that originally received investments from FMO public funds or FMO's own balance sheet (FMO-A), as a consequence of an **improvement in the financial risk profile of the company**

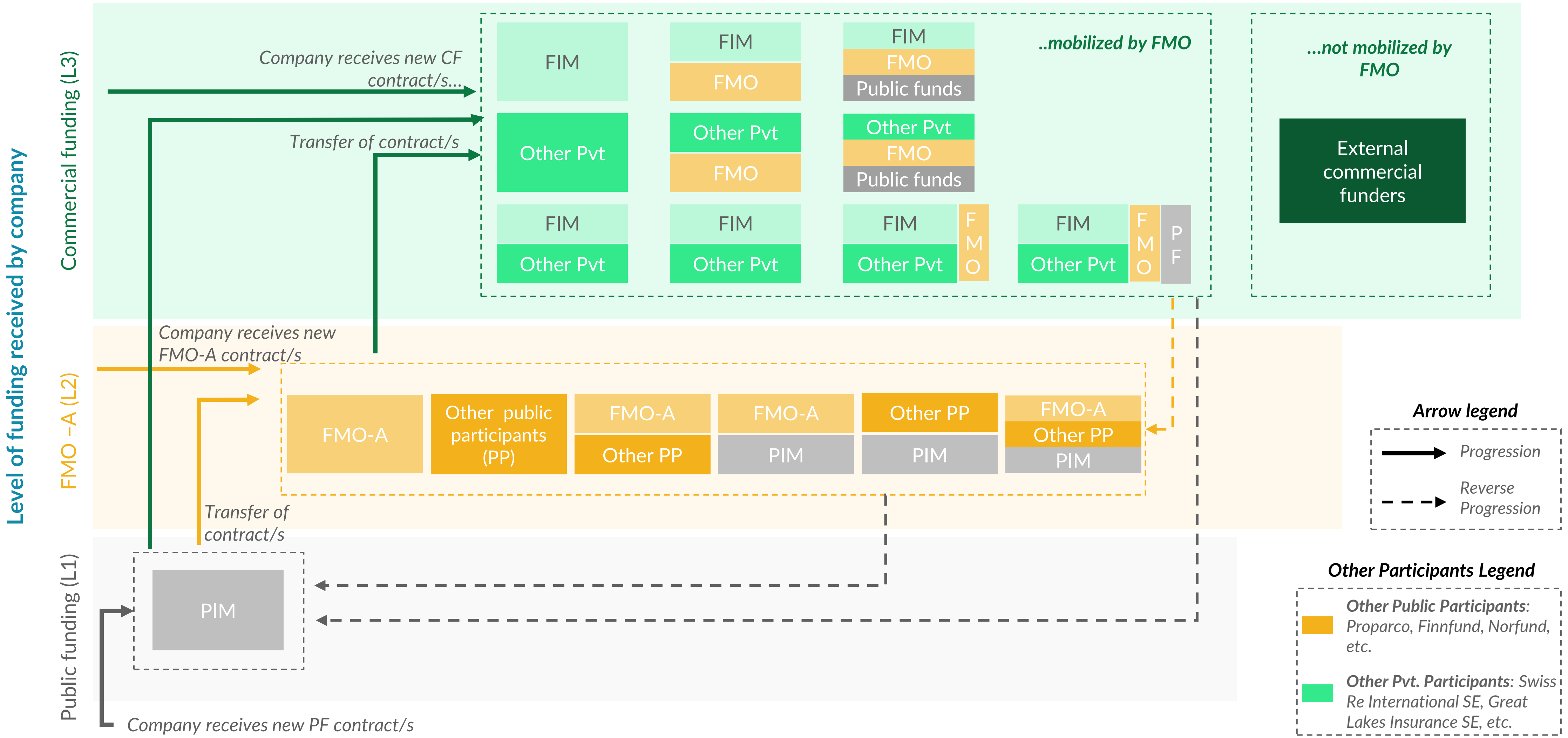
The potential stepping stones in a customer's journey towards progression



Legend
L1: Level-1; **L2**: Level-2; **L3**: Level-3 (assigned by Dalberg for this study)

Notes: (1) This scope of this definition is limited to the current engagement; (2) In addition to the progression ladder represented here, we also noticed a few scenarios with blended financing from all 3 levels - Public Funds, FMO-A and Commercial Investors

The conversations also clarified to us that a company's path to progression, between the three levels, could be varied and diverse



Out of scope: (1) Companies directly originating from FMO-A are not in our scope; (2) FMO Subsidiaries are out of scope and have not been included in the above flowchart (3) The FMO Ventures Program is not considered in our scope; (4) Due to lack of data, external commercial funders who aren't mobilized by FMO are not in our scope (5) Due to lack of data, other public participants financing without FMO's involvement is not in our scope

Abbreviations used: PIM = Public Investment Management, Other PP = Other Public Participants, Other Pvt = Other Private Participants

Scope | Our evaluation tracks FMO-enabled progression among customers that originated with MASSIF/ AEF/ BP participation from 2006-15

	Scope	Nuance/ Limitation
L1 Participants considered	Our evaluation only focuses on customer-level progression for those who originated from the following three public funds: **MASSIF, Building Prospects (BP), and Access to Energy Fund (AEF)**	This includes customers that (i) originated from either of these funds; (ii) originated with a blend of L1 (Public Funds) and L2 funding; (iii) originated directly at L2 but reversed[1] to L1
L2 Participants considered	In addition to **FMO-A,** our study considers **other public participants** such as Proparco, Finnfund, Norfund, etc. when co-financing with FMO as L2 participants	• While FMO's subsidiary entities are positioned at the same level as FMO-A, they will not be in scope for this study • Data limitations prevent us from tracking the other public participants' financing without FMO's involvement
L3 Participants considered	Our evaluation considers **FIM and other private participants mobilized by FMO** such as Swiss Re International SE, Great Lakes Insurance SE, etc. as L3 participants	While other commercial investors (not mobilized by FMO) technically qualify as L3 participants, data limitations prevent us from tracking them within this study, which has resulted in **underreporting of L3** status for customers, particularly those likely to have secured non-concessional financing independently
Originating Year	Our evaluation only includes customers that were on the balance sheets of MASSIF, BP, and AEF **from 2006-2015**	For contributor analysis, we have considered customers onboarded beyond 2015 to increase our sample size (from 265 customers till 2015 to 368 customers across all cohorts) and improve statistical confidence in the contributors to progression

Notes: (1) For the purposes of this study, reverse progression is defined as the complete withdrawal of a higher-level participant from a customer while a lower-level participant continues its exposure with the customer.

Approach I We used both quantitative and qualitative methods to answer 4 key questions

This study attempted to answer four key questions...

1. To what extent have customers in FMO's portfolio progressed?
2. Which factors have contributed to the progression or stagnation of a customer?
3. How has FMO's support helped a customer's progression and development
4. What are areas for refinement of the progression model?

... by conducting a quantitative portfolio analyses of FMO customers in scope...

- We followed a **three-step process build a progression database:**
  - **Developed a customer level summary** for **1720 customers** using **400k data points** that covered data on participants, instruments used, and time
  - **Traced customer's progression journey** from 2006 till present to identify key transition instances
  - **Collated information from various internal and external sources** that can provide additional context which could help explain progression journey
- We then **analyzed progression, contributors and development indicators**

... and nuancing our understanding with stakeholder interviews, qualitative case studies

1 

Gather key perspectives on progression and create initial contributor list

2

Validate and contextualize findings from quantitative analyses

3 

Build additional nuance into understanding progression through 10 case studies[1]

Question 1 |
To what extent have customers in FMO's portfolio progressed?

Quantum of progression I ~20-30% progression seen between stages; higher share of companies starting with L2 blend (vs only L1) progressed to L3

L1

230

L1 companies were a part of BP, MASSIF and AEF as of 2015

L2

62 (~27%)

companies from this sample progressed to L2

L3

18 (29%)

companies from this sample progressed to L3

~7% of companies that started at L1 progressed all the way to L3

37

companies joined at L2 in or before 2015 as a blend of BP/MASSIF/AEF, and FMO-A and/or Other PP[2]

7 (~18%)

companies from this sample progressed to L3

Reverse progression[2] was observed mostly from L2 to L1 - 15 cases of reverse progression were customers losing FMO-A participation. 33% of customers that underwent reverse progression, made subsequent advancements to L2/L3

1. Companies excluded from the median calculation: (A) 30 companies originating pre-Oct 2006, as the data export lacks monthly balances pre-Oct 2006 for confident progression duration estimation. (B) 3 companies that started at L1 and progressed to receiving L2 and L3 funding within the same month. 2. Companies joined at L2 in or before 2015 as a blend of BP/MASSIF/AEF, and FMO-A and/or Other Public Participants. Some of these companies that originated as an L1|L2 blend but were part of one of the big 3 funds subsequently as a standalone investor have also been included in the 230 list; (2) Reverse progression occurs when a higher-level participant completely withdraws its risk exposure, while a lower-level participant maintains its exposure to the customer

Time to progression I Median time to L3 progression was ~35-60 months; first transition took 40+ months for both L1 and L2-blend origin

L1

230

L1 customers were a part of BP, MASSIF and AEF as of 2015

47 months (median)

L2

62 (~27%)

customers from this sample progressed to L2

15 months (median)[1]

L3

18 (29%)

customers from this sample progressed to L3

- PIM origin customers that have already reached L2, usually make the jump to L3 faster than PIM + FMO-A origin customers
- However, on including the duration at Level 1 (L1) for PIM origin customers, the total time to reach L3 is actually shorter for customers originating from both PIM and FMO-A.
- This suggests that FMO's **familiarity with a customer** (gained through experience) and the **customer's initial risk profile** play a role in the progression timeline

37

customers joined at L2 in or before 2015 as a blend of BP/MASSIF/AEF, and FMO-A and/or Other PP[2]

43 months (median)

7 (~18%)

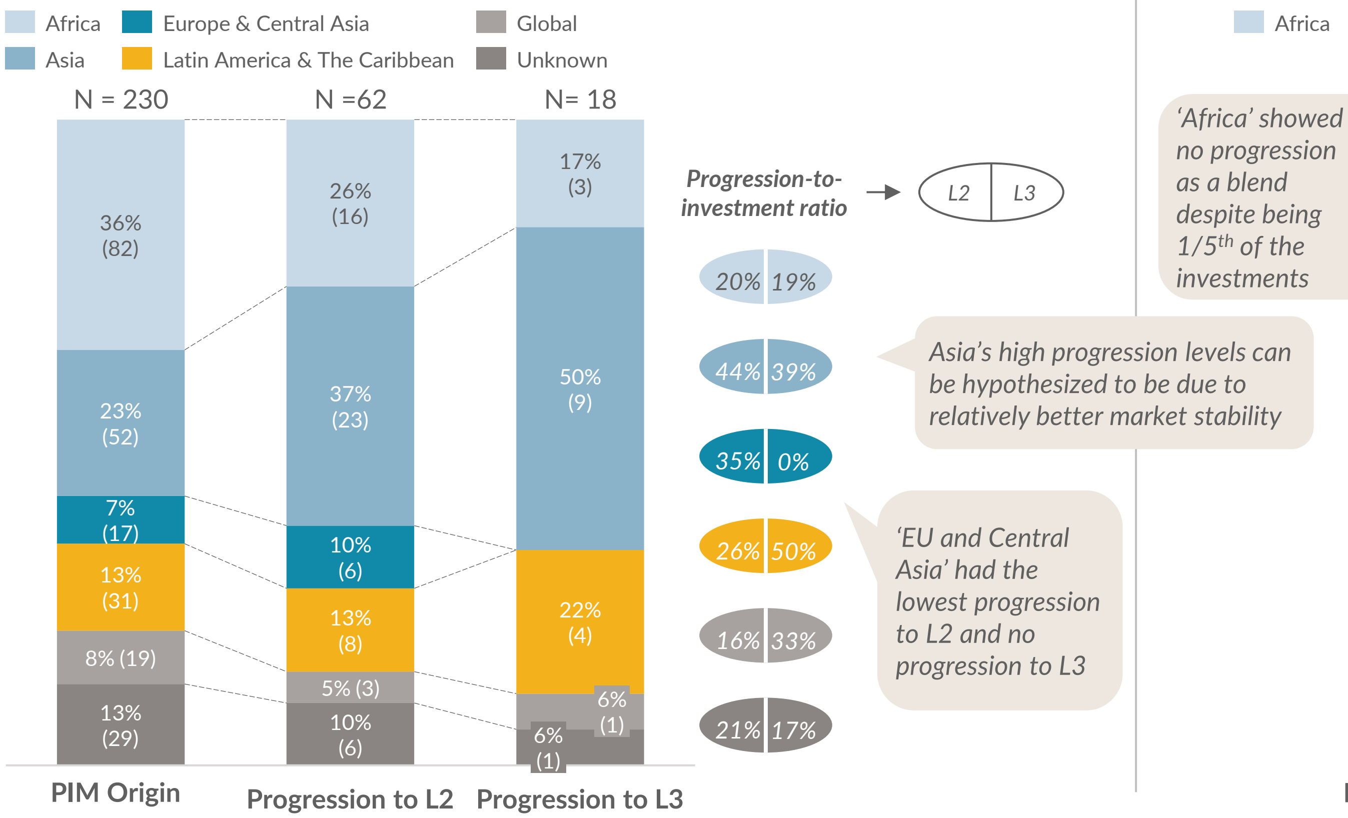
customers from this sample progressed to L3

Notes: (1) The median months are calculated based on the time taken for progressed companies to transition. Since this is an analysis of transition time and not the duration within each specific stage, companies that did not progress are not included in this calculation; (2). customers excluded from the median calculation: (A) 30 customers originating pre-Oct 2006, as the data export lacks monthly balances pre-Oct 2006 for confident progression duration estimation. (B) 3 customers that started at L1 and progressed to receiving L2 and L3 funding within the same month. 2. customers with PIM + FMO-A origin, but were part of one of the big 3 funds as a standalone investor has also been included in the 230 list

Region | Despite highest share of investment in Africa, Asia exhibited the best progression-to-investment ratio and speed of progression

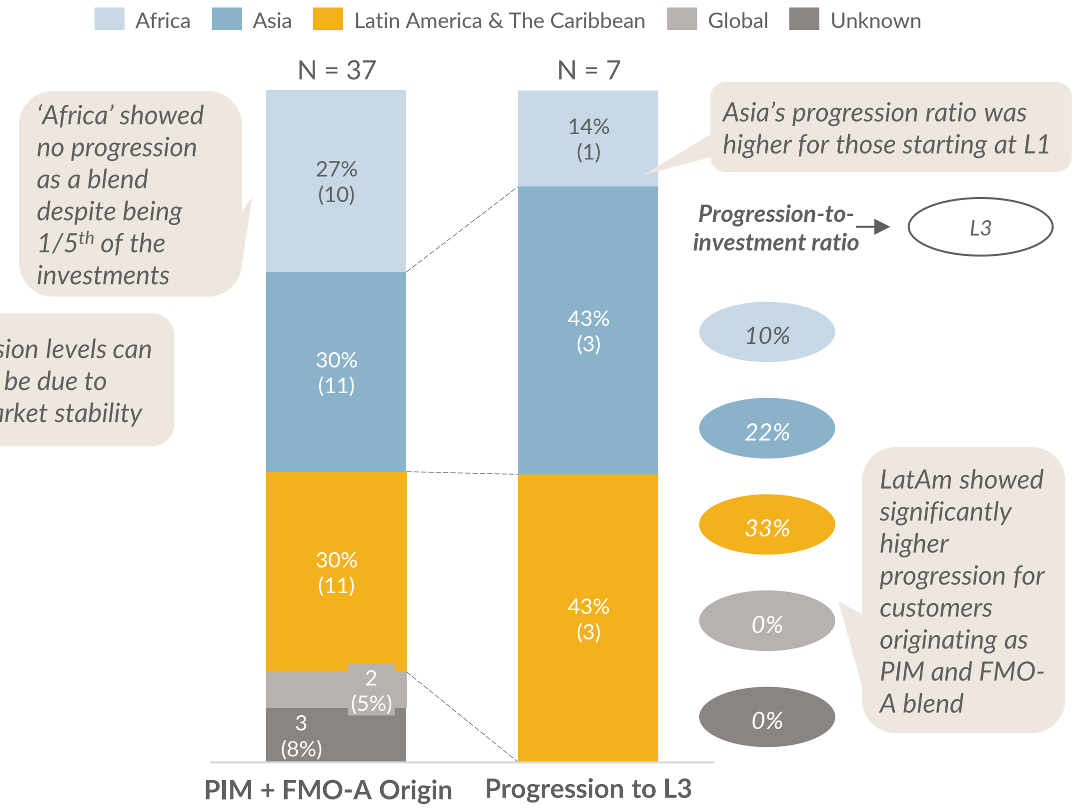
L1 Origin = 230 → L2 = 62 → L3 = 18

Share of customers by region at PIM Origin, L2 and L3 stages



PIM + FMO-A origin = 37 → L3 = 7

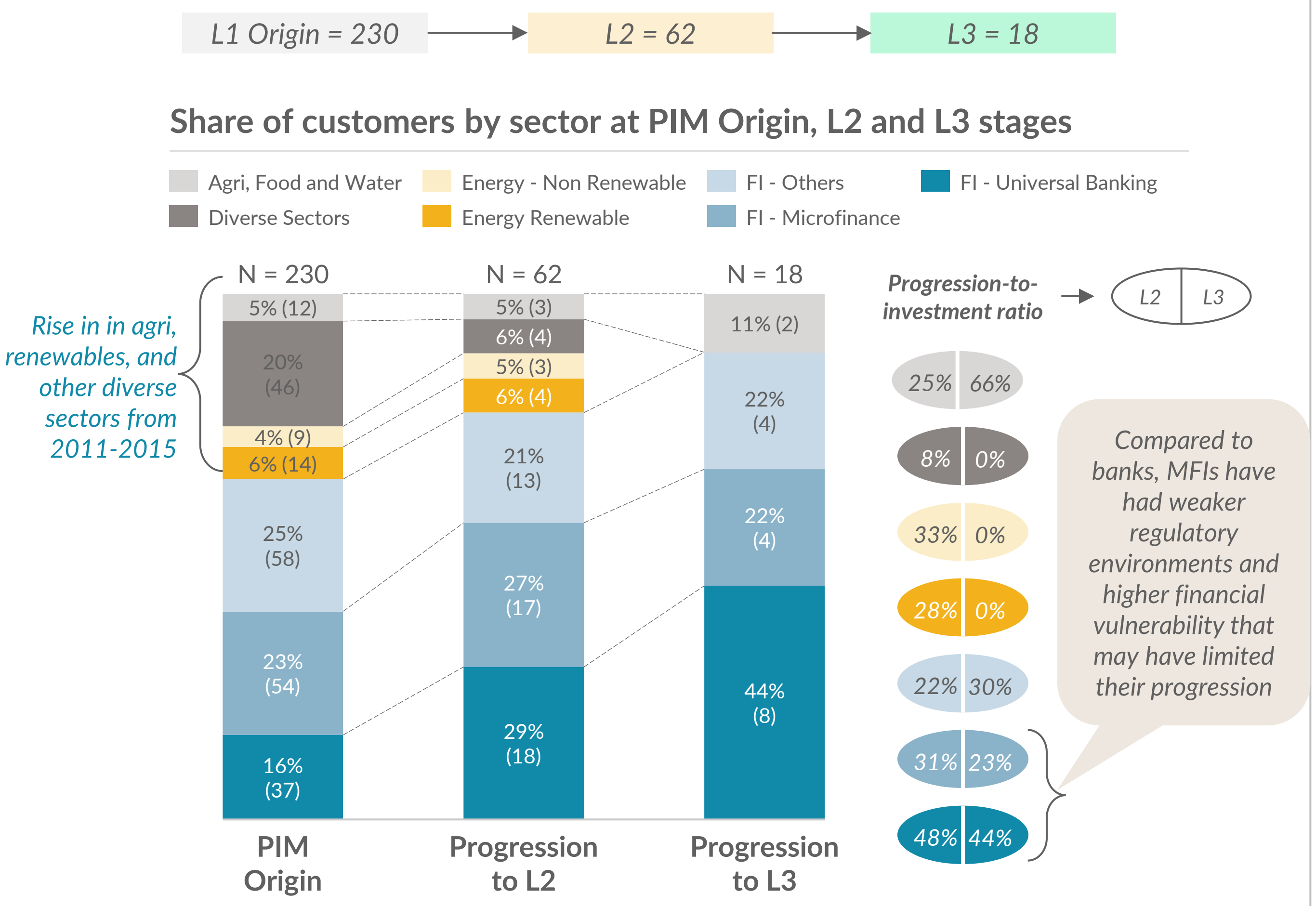
Share of customers by region at PIM + FMO-A Origin and L3



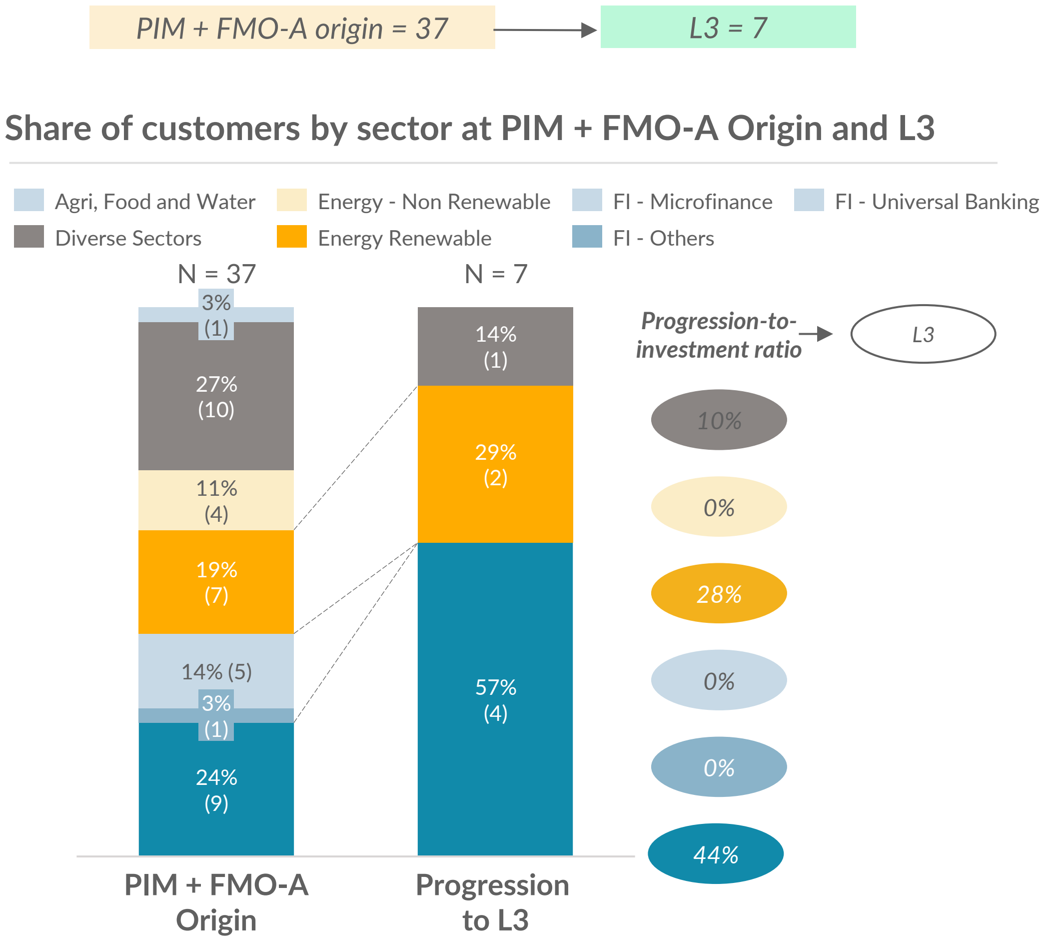
Despite higher Africa investment share, Asia saw higher progression ratio (likely due to better macro-economic and political conditions in countries making up FMO's Asian portfolio). Asia also had the fastest progression to L2 and L3.

Note: In each stacked bar chart, the first bar showcases the number of customers invested in at the PIM stage, the second and third bar chart shows the number that progressed to L2 and L3 respectively. E.g., on the LHS, 82 African customers were invested in, of which 16 progressed to L2, and 3 further progressed to L3.

Sector | Universal banking saw highest progression, while diverse sectors – spanning infra, telecom, mining, etc, witnessed the least



Time to progression: *Non-renewable energy and agri sectors progresses the slowest (~96 and 104 months medians respectively), much slower than FI benchmark (45-70 months)*

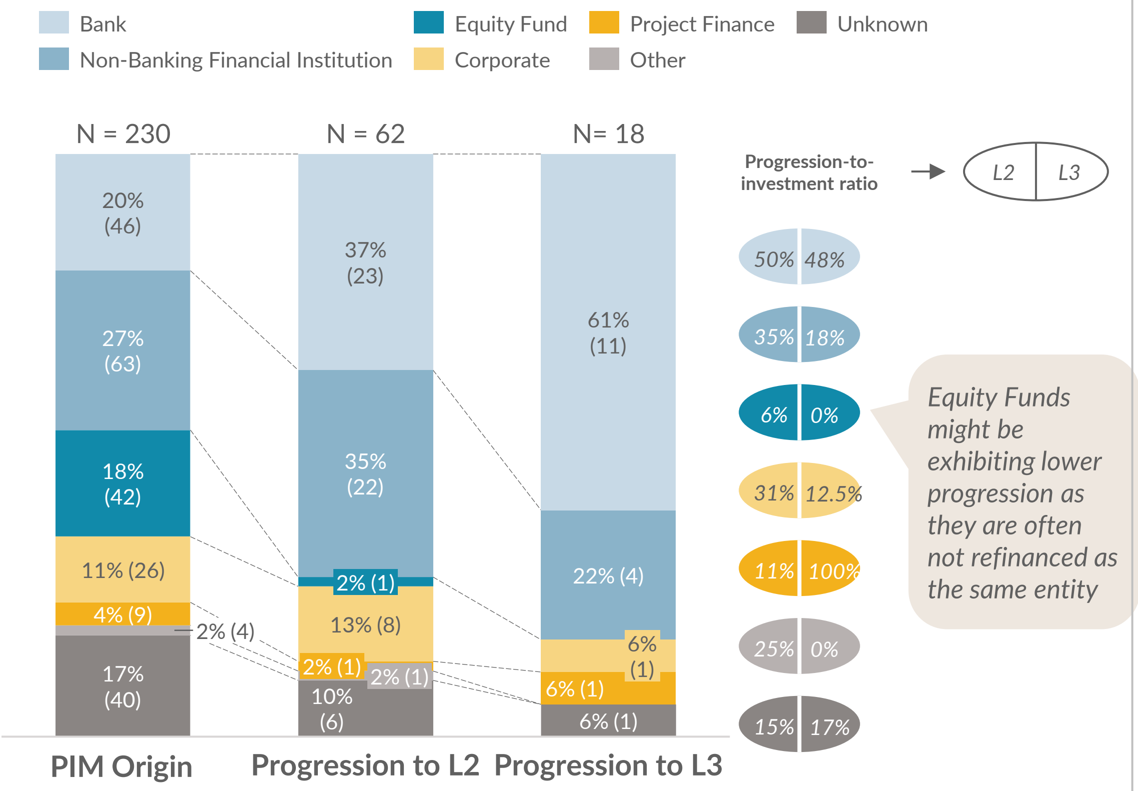


Note: (1) FI stands for Financial Institutions (2) FI – Others includes the industries 'leasing'. 'mortgage finance', 'insurance' and 'other FIs' (3) Energy Renewable includes the industries 'hydro energy', 'solar energy', 'wind energy', and 'other/mixed renewables' (4) All other classifications are consistent with FMO industry classifications (4) Diverse sectors spans 5 industries – 'infrastructure', 'manufacturing', ' 'hotels, hospitals and education', 'mining', 'telecom', 'other diverse sectors';
(4) In each stacked bar chart, the first bar showcases the number of customers invested in at the PIM stage, the second and third bar chart shows the number that progressed to L2 and L3 respectively. E.g., on the LHS, 37 'FI-Universal Banking' customers were invested in, of which 18 progressed to L2, and 8 further progressed to L3.

Customer type | Banks and project finance customers show highest progression, while equity funds exhibit the least

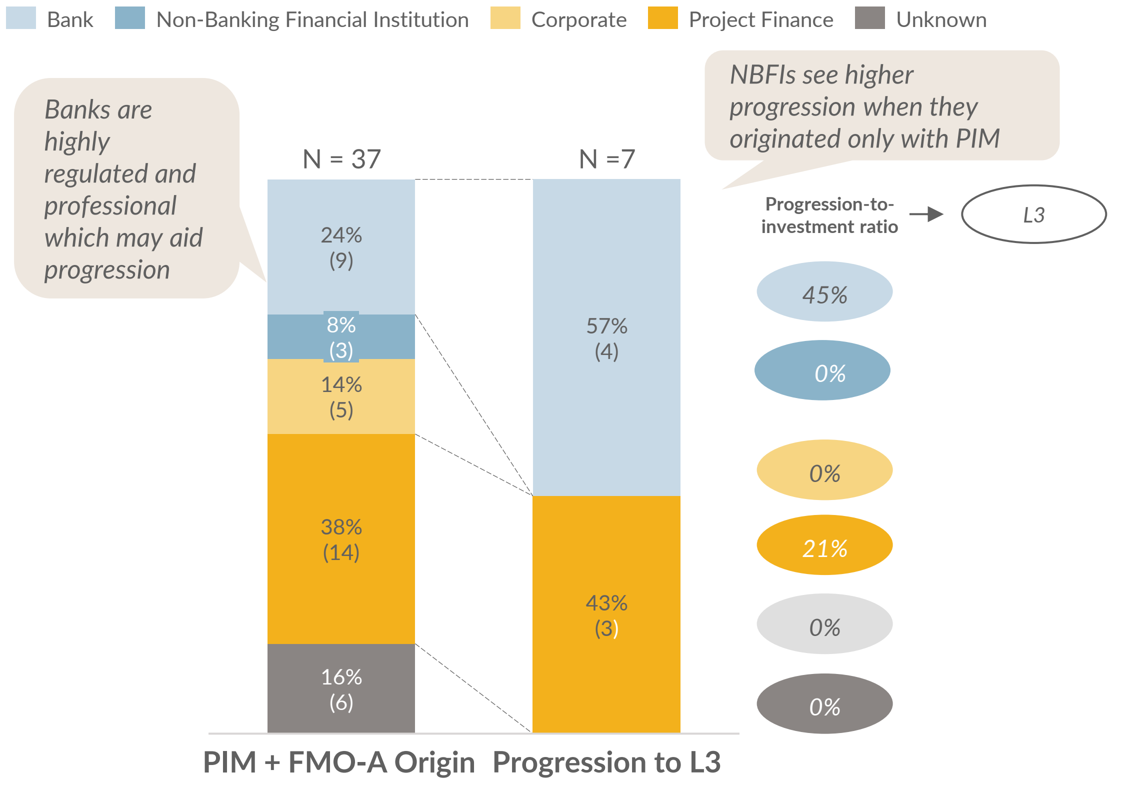
L1 Origin = 230 → *L2 = 62* → *L3 = 18*

Share of customers by customer type at PIM Origin, L2 and L3 stages



PIM + FMO-A origin = 37 → *L3 = 7*

Share of customers by customer type at PIM + FMO-A Origin and L3



***Time to progression:** All customer types take roughly the same time to progress*

Note: In each stacked bar chart, the first bar showcases the number of customers invested in at the PIM stage, the second and third bar chart shows the number that progressed to L2 and L3 respectively. E.g., on the LHS, 46 banks were invested in, of which 23 progressed to L2, and 11 further progressed to L3.

Based on FMO stakeholder inputs, we identified four key investment characteristics that influence variations in progression within the portfolio

Year of progression

Year in which companies progressed to L2 and L3

- **Half of the progressions to FMO-A and other DFIs (L2) occurred before 2008** and dipped during the financial crisis when investors' interest in emerging markets reduced.
- **Huge sustained spike in commercial mobilization (L3) occurred after 2013** after FMO's allocation policy shift to prioritize FIM funding and syndication with private participants

Region

The geographical region in which the investment has been made (e.g., Asia)

- FMO's public funds are most heavily invested in Africa, yet **Asian investees show better performance** with highest progression-to-investment ratio and fastest progression times. This could be attributed to more favorable macroeconomic and political conditions in Asian region

Sector and industry

The pre-defined strategic sector of investment (E.g., Energy)

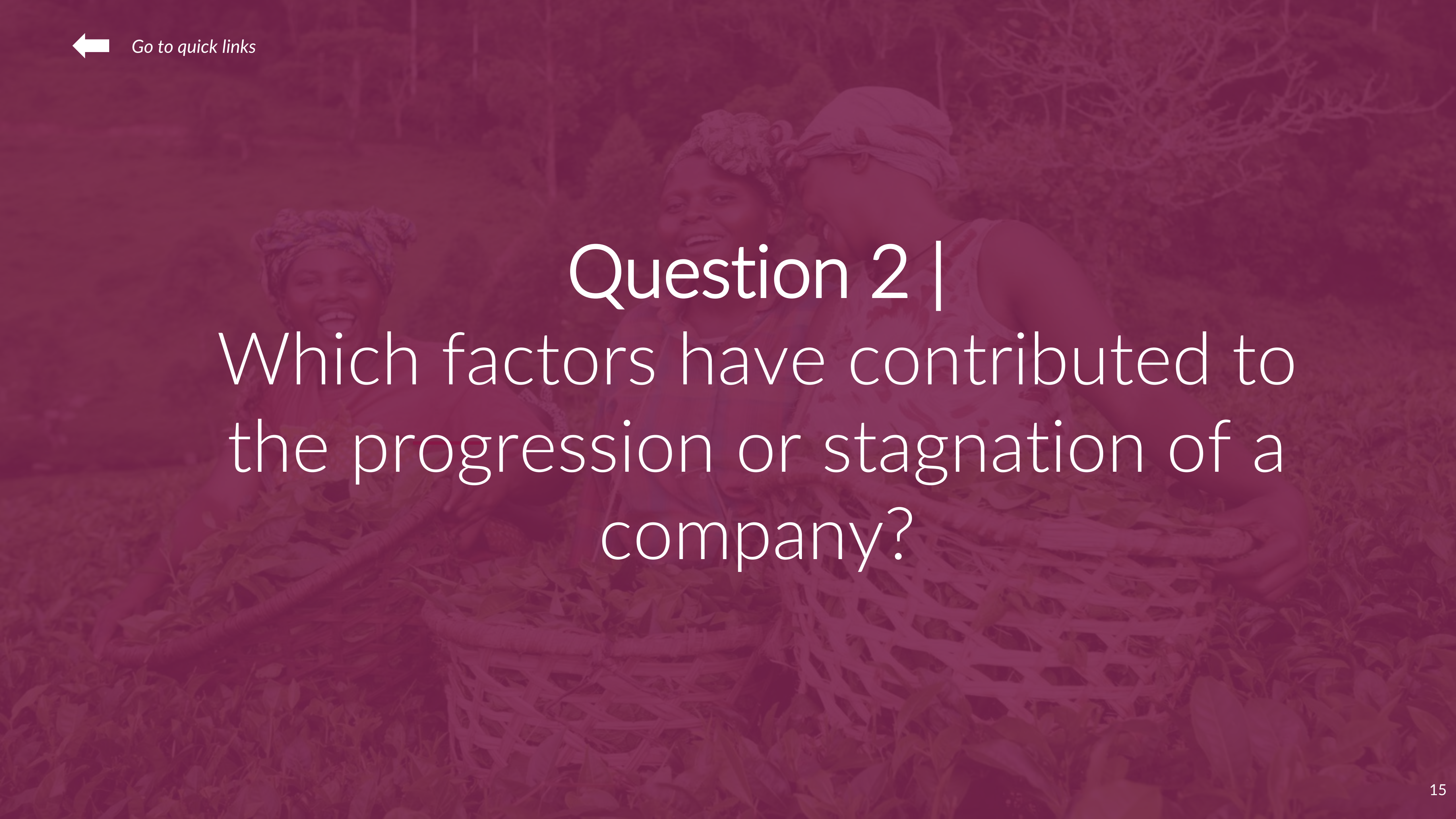
- **Universal banks** exhibit **highest progression –to- investment ratio**, ~1.5-1.6X higher than peers (microfinance, other Financial institutions, energy), potentially aided by greater sector maturity and stability.
- **Other "Diverse sectors" – spanning riskier fields** like infra, telecom, mining - **reported lowest** progression.
- **Non-renewable energy and agriculture sectors are** among the slowest to progress.

Customer type[1]

The pre-defined company archetype (e.g., corporate, banks, project fin etc.)

- **Banks have shown highest progression to L2 and L3**, likely benefiting from favorable regulatory environments and lower financial vulnerability, followed by **NBFIs and corporates. Equity funds**, display **negligible** progression.
- In contrast to steady progression among others, project finance has one of the lowest L2 conversions and the best L3 progression conversion.
- Despite the variability in quantum, **all customer types take approximately the same time to progress.**

Note: (1) Customer types refers to the Customer Risk Rating (CRR) type classification followed within FMO. Each customer is tagged as either a 'Bank', 'Non-Banking Financial Institution', 'Equity Fund', 'Corporate', 'Project Finance', 'Other', or 'Unknown'.



Question 2 |

Which factors have contributed to the progression or stagnation of a company?

FMO stakeholder inputs and outside-in research suggested that progression trends are influenced by market and company specific factors

Focus of this section

Market-based contributing factors

Factors stemming from external factors beyond the company's control, which influence progression.

Company-specific contributing factors

Factors stemming from the structure, composition, and processes of the investee

FMO-driven contributing factors

Many tools within FMO's control help mitigate against or leverage market/ customer contributors to progression

Note: We understand that FMO's choice of markets and companies to invest in will also determine what market/company-based factors contribute to progression at the overall portfolio level. In the bucket "FMO Driven contributing factors", however, we shall focus primarily on tools and support FMO offers, once the decision on where to invest has been made

Market factors | Stability in a market's socio-political-economic environment aids progression while conflict, shocks, and other risks hinder it

Enablers

Stable economic growth

Countries with stable GDP growth rates and fewer dips have higher progression

Sector maturity and stability

Sectors with strong regulation, operational stability, and good growth exhibit stronger progression

Barriers

Poor country risk rating

Countries with lower eco-political-social risk ratings show less & slower progression

History of conflict

Countries with history of or ongoing conflict saw less progression than those without

Black swan events ★

Negative macro-economic events inhibit progression and even contribute to reverse progression

No Conclusive Evidence

Presence in 55 poorest countries

Progression does not show correlation with investments being in a 'poorest 55' country

Ease of Doing Business

Most countries have a low score below 80, with no strong progression correlation

Backed by quantitative and qualitative evidence (solid box)

Backed by qualitative evidence (dashed box)

★ *More relevant for L1 to L2 progression* (yellow star)

★ *More relevant for L2 to L3 progression* (green star)

Please note that no star indicates that the factor contributes to both L2 and L3 progression comparably

Note: For contributory analysis in particular, we have also considered customers that were onboarded beyond 2010 as a part of our sample. This was done to achieve a reasonable sample size (from 170 customers till 2010 to 368 customers overall) necessary for this type of analysis

Company factors like business track record, governance quality, and green operations contribute to progression; impact of others remains uncertain

Enablers

Corporate Governance (CG)

Companies with better CG (Management and governance quality) have demonstrated higher progression

E&S compliance

Companies with strong E&S frameworks and management systems (especially in sectors with high E&S risk) exhibit better progression

Impact labels – green financing

Companies that have green labels[2] associated with FMO's financing have much higher progression

Barriers

Poor business model and financial health

Companies with poor track record of financials and/or market positioning struggle to progress to FMO-A and beyond

No Conclusive Evidence

Company size (assets, revenue)

Does not impact progression; investors might see smaller companies as having higher growth potential

Impact labels – reducing inequalities

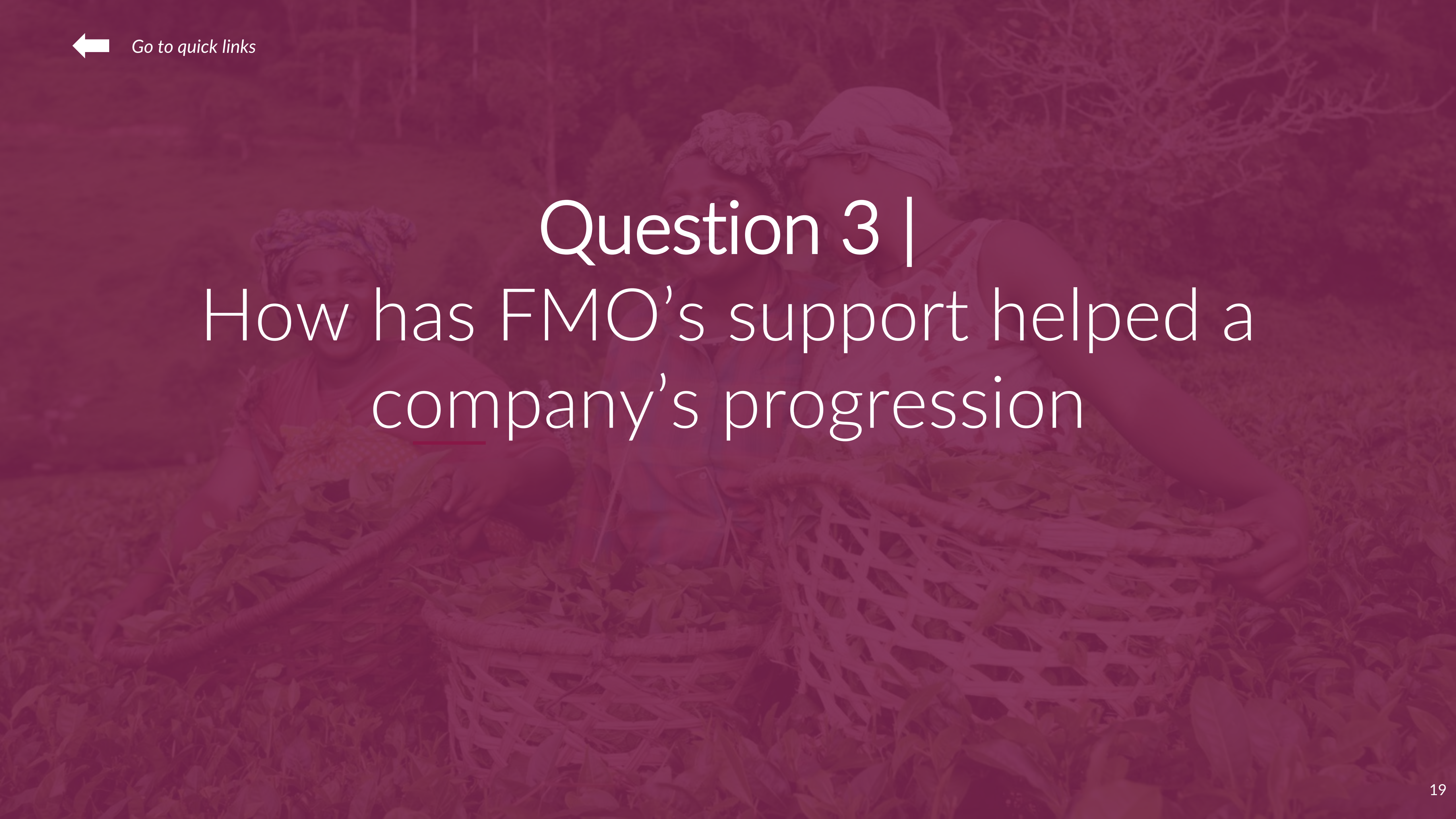
Impact metrics tagged to RI label (e.g. gender) did not have sufficient datapoints to establish correlation

Backed by quantitative and qualitative evidence
Backed by qualitative evidence

More relevant for L1 to L2 progression
More relevant for L2 to L3 progression

Please note that no star indicates that the factor contributes to both L2 and L3 progression comparably

Note: (1) For contributory analysis in particular, we have also considered customers that were onboarded beyond 2010 as a part of our sample. This was done to achieve a reasonable sample size (from 170 customers till 2010 to 368 customers overall) necessary for this type of analysis; (2) FMO looks for investments in the following three Green categories: Climate Change Mitigation, Climate Change Adaptation and Other Footprint reduction.



Question 3 |
How has FMO's support helped a company's progression

FMO has several tools which mitigate or leverage market and customer factors such as investee selection and financial and non-financial support

Company selection criteria	**Country/sector-level strategy** *Developing country/sector-specific plans/strategies can focus efforts and drive higher progression rates*	**Companies with strong competitive advantage** *Investing in top companies in each country and sector helps balance market-level risks*	
Financial support tools	**Concessional finance terms** *FMO offers financial additionality (e.g. longer tenor loans, local currency financing, unsecured debt) which aids progression*	**Mix of debt, equity, guarantees** *By deploying an appropriate mix of instruments, FMO can offer necessary leverage and/ or support to aid progression*	**Risk sharing mechanisms** *Through syndication and subordination, FMO facilitates participation of more risk averse investors (in turn aiding progression)*
Non-Financial support tools	**Technical assistance/capacity development** *Interventions or grants to strengthen operations like E&S and CG aid progression* **Market-level action** *Focused market action leads to sector-wide improvements, eventually leading to company-level progression*	**Strategic support and networks** *Guidance to mitigate market or business risks, and opportunity to network with other relevant actors helps aids progression*	**Conditional financing** *Requirements that come as part of FMO's financing help increased company standards, in turn aiding progression*

Company selection criteria · Financial support tools · Non-Financial support tools

In high market risk situations, key FMO tools are likely to support company resilience to macro chances and crowd in L3 funding

High market risk

Situation	Complication	FMO tools that are likely to be effective
Investees in **high economic-political risk geographies**	• Socio-political turmoil and (consequent) economic instability often affect investees operations and financial performance • Other investors are also often hesitant to participate in these markets	• Significantly **factor company's financial and market position** into investment decision • **Maintain risk exposure via FMO-A** funding to crowd in private investors in a risky sector • **Work closely with the companies' management** to assess resilience and drive growth during challenges
Investees in **high risk, unstable sectors**	• In nascent, volatile or unregulated sectors, company-level progression may be inhibited by market risk which complicates business operations and dissuades other investors • Often these sectors also have high E&S risk, which limits participation from even DFIs and impact investors	• **Diversify investment** either across multiple companies or geographies to reduce risk • Offer **TA/ CD to build E&S and CG** processes; and provide **advisory support** • Engage in **holistic market-building efforts** to grow the sector, and eventually the companies

● Company selection criteria ● Financial support tools ● Non-Financial support tools

For high-risk companies, FMO's focus on selecting high-potential investees and investing in their capacity building aids progression

High company risk

Situation	Complication	FMO tools that are likely to be effective
Early-stage or nascent of investees	• Companies lack a financial track record which deters other DFIs and commercial funders from investment • Companies do not have well-defined internal processes and structures, further limiting growth	● **Factor country/ sector risk profile** during investment decision to offset company risk ● **Ownership via equity** allows FMO to direct internal process building and larger strategic trajectory ● Supports investees **explore and identify their niche within green products** and provides relevant support
Investees **piloting new innovations**	• Companies are piloting new innovations, with no proof of success at scale, which inhibits DFI and commercial funding • Such projects, if in sectors like energy, could be of a big-ticket size, and hence bear higher risk	● Invest in pilots backe**d by rigorous research and experts**, and in **topics within FMO expertise** ● Ensure that there is **strong leadership with skin in the game,** to minimize accountability and non-performance risk ● Given the steep scale up/ pay-off potential, maintain **willingness to provide follow-on funding**

● Company selection criteria ● Financial support tools ● Non-Financial support tools

Question 4 |
What are areas for refinement of the progression model?

Our evaluation of the Progression Model surfaces 5 strategic priorities and supporting process enhancements for FMO to consider

FMO can explore 4 shorter term and 1 longer term strategic priorities to refine its current 'Progression Model'

Longer term consideration

1 Clearly articulate contribution of progression to FMO business priorities/ activities

Articulate the progression model within the context of FMO's Strategy 2030,and other public/ commercial funding priorities, including additionality

2 Specify how progression model framework can steer fund level actions and priorities

Clarify how progression will be used to set and achieve fund level investment, and establish supporting accountability measures

3 Build a future looking progression Measurement, Evaluation, and Learning (MEL) strategy

Leverage results of the current evaluation as a baseline. Use them to determine FMO's approach to progression MEL strategy the future

4 Build awareness of and advocate for progression/ progression supporting initiatives in FMO

Build key stakeholder awareness of progression and undertake advocacy efforts to directly promote progression or opportunities which can unlock it further

5 Broaden FMO's role in driving and leveraging progression

Develop sector-level strategies in target countries, design responsible exits to commercial investors and anchor thought leadership on progression in the broader DFI ecosystem

To support these strategic priorities, we recommend implementing essential systems & process enhancements

6 Streamline processes and systems spanning across the following categories

People and Organization

Modify people processes to clarify and incentivize progression targets, set up knowledge management systems, and facilitate coordination across teams

Specialized skills and tools

Invest in developing specialized skills and toolkits to aid progression, including local market syndication, special operations and TA (post public finding stage)

Data Systems

Improve data systems from expanding the scope and quality of data collection efforts to facilitating easier real-time review of progression

Thank you!

Please feel free to reach out to us in case of any questions