

Findings from the second research wave of the Independent Evaluation of the FCDO Development Impact Bonds Pilot Programme

Summary report

February 2021



“We push ourselves to go the extra mile... The fact that fellows, teachers and headmasters all know... what the expected outcomes are, is triggering accountability.”

Service provider



Introduction

The Foreign, Commonwealth & Development Office's (FCDO's) Development Impact Bonds (DIBs) pilot programme runs from June 2017 to March 2023 and funds three DIBs:

- **International Committee of the Red Cross (ICRC): Humanitarian Impact Bond (HIB) for Physical Rehabilitation**, which funds the building and operationalising of three new physical rehabilitation centres in Mali, Nigeria and Democratic Republic of Congo (DRC);
- **Village Enterprise: Micro-Enterprise Poverty Graduation Impact Bond**, which aims to raise the income levels of the extreme poor through Village Enterprise's microenterprise development programme; and
- Support to **British Asian Trust**: to design impact bonds for education and other outcomes in South Asia, including the **Quality Education India (QEI) DIB**, which aims to improve education outcomes for primary school-aged children in India.



What is a DIB?

A DIB is a mechanism for drawing external finance into payment-by-results (PbR) projects. In a DIB a donor commits to paying for development results if and when they are achieved. A service provider steps up to deliver the prescribed results.

The main way a DIB differs from standard PbR is that a DIB brings in third party "investors" who supply the service provider with the investment needed to deliver activities. Under the DIB model, the investor also takes on a portion of the financial risk associated with failing to deliver the prescribed results.

The programme aims to: a) understand the process of agreeing and managing DIBs and implications for FCDO's processes; b) build an understanding of whether DIBs enable efficient and effective delivery of programmes and c) build an understanding of the conditions for DIBs to be an appropriate commissioning tool and the costs and benefits of using them.

The **objective** of the evaluation is to generate learnings and recommendations on the use of DIBs as an instrument for aid delivery. In addition to the three projects funded under the pilot programme, a fourth DIB has been added to the evaluation – the **Cameroon Cataract Bond**, which aims to prevent blindness in Cameroon through the provision of cataract surgeries.

The two **evaluation questions** are:

- 1 How does the DIB model affect the design, delivery, performance and effectiveness of development interventions?
- 2 What improvements can be made to the process of designing and agreeing DIBs to increase the model's benefits and reduce the associated transaction costs?

The evaluation focuses on the use of the DIB funding mechanism and understanding the '**DIB effect**', that is, the effect of using a DIB instead of a grant or other PbR mechanism. The evaluation team developed a DIB Theory of Change (ToC) that outlined anticipated DIB effects (summarised in Table 1), based on wider literature and consultations with stakeholders in these four DIBs. The evaluation seeks to test this ToC.

A key challenge is trying to isolate the effect of the DIB from other factors on the different stakeholders and phases, and from the PbR effect. The evaluation team used a combination of process tracing and comparative analysis to achieve this. The evaluation draws on interviews and programme data, including design documents, cost data, monitoring data and other evaluations and reviews. The evaluation identified 'comparator sites' delivering similar interventions but funded through grants, in order to examine how delivery compares between a DIB and a grant. The evaluation team also interviewed stakeholders working on other DIBs, and reviewed the broader literature on DIBs, social impact bonds (SIBs) and PbR.

This report presents the evaluation's initial findings against the evaluation questions. As the DIBs are part-way through delivery, this report focuses on the DIBs during their delivery stage. It builds on the first report, which focused on the DIBs during their **design** stage.

These findings will continue to be refined and developed based on additional evidence over the remainder of the evaluation. A final evaluation wave in 2022 will assess the achievement of outcomes and explore how the DIB affects the sustainability of the intervention.

Findings

EQ1: How does the DIB model affect the design, delivery, performance and effectiveness of development interventions?

One of the main themes to emerge from the evaluation is that the DIB can be an **effective change management tool**. In all of these DIBs we have seen a greater focus on outcomes. In particular, in QEI and VE, the DIB encouraged a stronger outcomes-focused culture within both the service providers and funders. It provided the impetus to increase performance management activities, thereby improving the capacity to adapt and improve service delivery and manage projects towards the target outcomes. The increased pressure to achieve outcomes had both positive and negative effects – positive in some cases, as staff reported increased motivation, but negative in others, with staff reporting that this affected morale. Collaboration between stakeholders was also strengthened across the DIBs.

We note that these effects are not *exclusively* DIB effects. These effects were also seen in some of the comparator sites, that is, comparable programmes identified for the purposes of the evaluation. However, in some cases, the effects were stronger under the DIB. Also, while these effects were present in some comparator sites, the DIB appeared to be the catalyst for change that set things in motion and sped up changes.

Stakeholders believe that this is leading to the achievement of **more outcomes than would be possible without a DIB**. Early results from VE and QEI suggest elevated outcomes performance in the DIB sites compared to previous delivery. This will be further investigated in the next research wave.

The table opposite summarises the extent to which DIB effects were present across the four DIB projects. In assessing the DIB effect, we considered both whether this was observed in the project, as well as the extent to which this was attributable to the DIB. Each effect is 'RAG' rated¹ on the extent to which it was identified across all projects, followed by individual ratings for each DIB. It should be noted that the rating identifies the extent to which the effect is present, not whether it had a positive effect (i.e. both positive and negative effects would be marked as green if present). It is important to bear in mind that stakeholders decided to use the DIBs for different reasons, and not all DIB effects were anticipated.

¹ Green = effect is present in at least three DIBs; amber = mixed evidence over presence of DIB effect; red = effect is not present in at least three DIBs.

Table 1: Extent to which DIB effects materialised across the four DIBs

| DIB effect | Summary | ICRC | QEI | VE | Cataract |
|--|---------|------|-----|----|----------|
| Positive DIB effects | | | | | |
| 1 Shift focus to outcomes, greater accountability | ● | ● | ● | ● | ● |
| 2 Drives performance management | ● | ● | ● | ● | ● |
| 3 Providers deliver adaptive management and course correction | ● | ● | ● | ● | ● |
| 4 Greater collaboration between stakeholders | ● | ● | ● | ● | ● |
| Negative DIB effects | | | | | |
| 5 Perverse incentives | ● | ● | ● | ● | ● |
| 6 Tunnel vision | ● | ● | ● | ● | ● |
| 7 Lowers staff morale, affecting other DIB effects | ● | ● | ● | ● | ● |
| Greater outcomes | | | | | |
| 8 Increased efficiency and effectiveness, leading to increased number of beneficiaries supported and outcomes achieved | ● | ● | ● | ● | ● |

Key ● Present ● Present to some degree ● Not present ● Too early to tell

The DIB effect described above also includes **wider spillover effects**. There is evidence of service providers and funders strengthening their outcomes focus and data-driven adaptive management in other parts of their organisations. For example, Village Enterprise quickly rolled out the adaptive management techniques developed in

its DIB to its non-DIB delivery because these practices proved to be so effective. Funders in the Cataract Bond have started implementing learning from this DIB in other projects, to monitor the *quality* of surgeries and simplify outcome targets and performance management.

Our analysis across these four DIBs suggests there are four 'key ingredients' within the DIB that have led to increased efficiency and effectiveness of delivery, and consequently increased outcomes:

- **Stronger focus on outcomes:** Tying payments to outcomes in the DIBs led to a clearer articulation of the specific results the project is trying to achieve. Everyone was made aware of priority outcomes and how the project was expected to achieve them.
- **Heightened performance management:** Stronger measurement approaches were introduced in the DIBs to help monitor the projects' progress against their stated outcomes. There was regular scrutiny of performance, which allowed the projects to identify quickly areas of under-performance and respond accordingly. An external performance manager often provided additional expertise, support and pressure.
- **External perspectives and expertise:** Multi-stakeholder partnerships facilitated by impact bonds brought in new perspectives and expertise to support project implementation. The participation of these new partners, such as investors and external technical advisors, helped strengthen project design, supported with problem solving, provided management support and advice, and introduced new tools and methodologies.
- **High-stakes environment:** Attaching payments to outcomes created financial risk for investors and sometimes for service providers. Increased accountability and heightened attention paid to DIBs increased reputational risks for all parties. Both elevated financial and reputational risks prompted rapid responses to challenges when project performance was under great scrutiny, particularly when everyone's attention was focused on the stated outcomes.

These four key ingredients cut across our understanding of how a DIB affects the delivery of development interventions. The figure below sets out our framework for understanding the relationship between DIB *inputs*, DIB *outputs* and DIB *effects*, relevant for the delivery phase. The four key DIB ingredients are boxed. This has been developed based on our analysis.

“We have ... placed emphasis on improving data driven adaptive management capacity specifically because of the DIB.”

Service provider



DIB effects framework – delivery phase



It is important to note that the DIB effects seen are not *exclusively* DIB effects. The implication of this is that a DIB is not always necessary. Some of the desired effects could also be achieved through a well-designed grant or PbR, and it is possible to design these to include many of the features of a DIB (e.g. in the case of the Cataract comparator site). However, the DIB appeared to be the catalyst for change that set things in motion and sped up changes. A key finding is that how the DIB affects delivery depends on how the DIB is structured and the target objectives of using a DIB.

This is starting to shed some light on when a DIB is most applicable. It would suggest a DIB may be most appropriate where:

- performance could be enhanced through a stronger focus on outcomes buttressed by performance management;
- the system/culture needs an external 'disruption' to bring about change;
- service providers would not be able to tolerate high levels of financial risk; and
- providers would benefit from external expertise and support.

EQ2: What improvements can be made to the process of designing and agreeing DIBs to increase the model's benefits and reduce the associated transaction costs?

Reducing transaction costs

The key additional costs during delivery relate to:

- 1 Verification to ascertain the outcome payments.
- 2 Other evaluation costs related to generating learning on the use of the DIB mechanism.
- 3 Investment vehicle/legal costs needed to use the DIB mechanism.
- 4 Governance costs related to coordination and convening the generally larger number of stakeholders under a DIB.
- 5 Performance management costs related to increasing the use of data to deliver adaptive management.

DIB structures and costs vary, as do structures and costs in other funding mechanisms such as grants and PbR. However, generally it seems that verification costs are an additional DIB cost, though they are also required in PbR. Evaluation and performance management costs are not unique to DIBs, but our finding is that these costs represent the higher end of M&E costs seen in grant and PbR projects. Investment vehicle and legal costs are unique to the use of the DIB mechanism, though we note some PbR mechanisms will also require these costs. Governance costs are also higher, but we note that this could be due to the fact that contracting intermediaries to deliver this crystallises and formalises tasks and costs that were previously undertaken by the service provider and/or outcome funder.

Across the DIBs, the highest costs are in the areas of verification, especially the QEI and VE DIBs which involved large RCTs and quasi-experimental approaches. Intermediary costs represent the second highest proportion of costs.

These costs are generally paid for by the outcome funders, as part of the total DIB costs. However, there are also some costs paid for by other funders, such as the separate learning grant paid for by FCDO in the case of the QEI DIB. A number of stakeholders across intermediaries and service providers also mentioned that they are providing in-kind contributions, in terms of staff time.

There is some indication that these costs do lead to additional results, impacts and benefits. These additional costs are critical to the key ingredients and DIB effects described above. For example, verification was noted as a key driver for a stronger focus on outcomes. The external expertise was noted as a key contributor to improved performance management and adaptive management.

Relevance of DIBs and increasing the model's benefits

Generally, stakeholders considered that DIBs were relevant to the sectors involved in the pilot DIBs. For example, QEI and Cataract stakeholders noted that clear outcomes were characteristic of the education and health sectors, which meant they were well suited to DIB funding. The move to multi-year funding offered by the DIB was very relevant in the India context (QEI) and humanitarian sector.

To increase the benefits of the DIB model, the guiding principle should be to design a DIB with a clear understanding of why a DIB is being used, and what the target benefits are. Designers can then consider how to best structure DIB to meet these objectives. This ensures the model can be designed most effectively and efficiently to meet these objectives.

As such, it is difficult to set out general learning across all DIBs. However, we have identified some emerging learning for the key design choices in the DIB:



Role of the intermediary

Most consultees agreed that the intermediary had an important role to play to coordinate stakeholders with different priorities and needs. At the same time, intermediary costs can be high. For the DIB market to grow, the intermediary role needs to be clearly defined and costed effectively. The precise role of the intermediary should be tailored to the specific DIBs, including the mix of stakeholders and skillsets brought by the other stakeholders.



Role of independent evaluation

The role of a rigorous approach to validating impact was noted to be a key contributor to a number of DIB effects. The use of validated administrative data versus experimental approaches should be guided by the target objectives of the DIB and the geographical/sector context. Potentially, there can be greater consideration of synergies between verification and performance management activities, and drawing on existing data, e.g. those collected by government.



Performance management systems

All four DIBs involved significant strengthening of performance management systems, and there are promising indications that this is improving the efficiency and effectiveness of delivery. A key learning, especially given the Covid-19 situation, is the need for real time monitoring to support timely course correction.



Role of collaboration and governance

It is important to clarify roles, responsibilities and decision-making authority and processes across stakeholders in order to maximise collaboration.



Managing communication and learning

To maximise spillover effects, there is a need to focus on external communication and improve the sharing of learning between stakeholders.

To further grow the development impact bond market and engage government stakeholders, standardisation and establishment of 'best practice' are needed to reduce costs. However, more impact bonds and evaluations are needed to develop context-specific learning around the structuring and delivery of DIBs. Stakeholders also agreed on the importance of building service provider capacity in further growing the market.

Areas for consideration and further investigation in the next research wave

There are some themes and questions where there is not enough evidence yet to draw conclusions at this stage of the evaluation, but are nevertheless important to consider in the next research wave:

- 1 Is a DIB necessary to achieve the DIB effects described in this document, or could similar effects be achieved through a well-designed grant or PbR project?** In some instances, it seems possible that the DIB effects could be achieved through a grant with more funding for performance monitoring and technical expertise. However, the DIB's high stakes environment and focus on outcomes can be an important catalyst to drive change.
- 2 To what degree can a DIB be rolled out to the wider landscape of service providers?** The DIBs covered under the evaluation have only involved interventions with a strong evidence base, undertaken by service providers experienced in delivering through an adaptive management approach. It is unclear if the DIB will be as effective with organisations where these characteristics do not already exist.
- 3 Does the idea of a DIB as a change management tool mean it is only needed once in an organisation?** If a DIB shifts the focus and behaviour of a whole organisation, can another add value after the first is completed? Is a DIB a 'one time pivot'? We do not know the answer to this question yet because we do not know a) how far reaching the spillover effects have been; b) how sustainable they are; or c) how this view might change if transaction costs go down over time.
- 4 How appropriate is a DIB in development contexts?** The impacts of Covid-19 are unprecedented, yet large scale shocks are not uncommon in development contexts. Therefore, the ways that DIBs responded to Covid-19 provides a 'litmus test' for the efficacy of the model in development contexts. The DIB model appears to have both helped and hindered the projects' response to Covid-19. There is additional flexibility in some areas, but reduced flexibility in others.
- 5 Does a DIB displace other delivery?** There were some suggestions in the research that a DIB project diverts skilled staff, expertise and resources away from other parts of the organisation. Further consideration is needed in terms of whether the DIB itself is more effective, or if elevated performance is simply the function of more resources and skills.
- 6 Is performance management most effective when provided through a third party?** The DIB effect seemed particularly potent when projects had access to additional resources and technical expertise, which is provided by external third parties. On the other hand, one of the major sources of additional costs of DIBs is external expertise. The best approach to balance cost, effectiveness and sustainability merits additional investigation.

Lessons learned

Below we set out the lessons of potential relevance for others implementing development impact bonds. We caveat that there is still significant variation across existing DIBs and the evaluation sample remains small.

DIB effects on interventions

- 1 The DIB effect varies across DIBs depending on the stakeholders involved, their motivations for using the DIB, and the structure of the DIB.** Hence, when designing a DIB, stakeholders should consider *why* they want to use a DIB. They should then structure the DIB to support these objectives.
- 2 A DIB can be an effective change management tool.** In these pilot DIBs, the DIBs have been a catalyst for change, driving stronger use of data to inform delivery.
- 3 The added advantage of the DIB, in comparison to PbR, is that it brings together different stakeholders, such as outcome funders, investors and intermediaries.** The pilot DIBs have seen more flexibility in terms of the roles played by different stakeholders and more collaboration across stakeholders.

Reducing costs and increasing the model's benefits

- 4 Additional stakeholders require more coordination, resulting in greater costs.** These costs can be managed by having clarity on what added value different stakeholders are bringing and clarifying decision-making processes.
- 5 Transitioning to an outcome-based contracting model requires outcome funders and service providers to shift their perspectives.** To maximise the benefits of the model, it is important to focus on outcomes, rather than inputs.
- 6 Delivery of a DIB requires strong internal and external communication.** The use of a new funding mechanism and involvement of private investors brings potential reputational risks that need to be managed.
- 7 The DIBs have required more time and resources than expected and budgeted for.** To ensure attention is not diverted from other projects, these should be planned and budgeted for.
- 8 The role of the intermediary should be carefully considered, to ensure costs and benefits are proportionate.** A balance is also needed between bringing in external expertise and building the capacity of providers and funders.
- 9 Validation costs can be high – there is a trade-off between rigour and cost.** There are opportunities for synergies between verification and performance activities.

- 10 Measuring cost-effectiveness of the DIB funding mechanism is extremely challenging.** More transparent sharing of data and analysis is needed to assess the value for money of the mechanism.
- 11 Covid-19 has meant changes to targets have been needed.** DIB stakeholders have tried to avoid additional legal costs, by agreeing changes more informally and flexibly. This depends on the existing relationships and levels of trust between stakeholders.


Recommendations

Recommendations to FCDO

- 1 FCDO can support the wider market in collecting more robust cost data.** This would ensure future DIB designers have a good understanding of potential costs and cost drivers and are able to assess these against the expected benefits of using a DIB.
- 2 In designing future DIBs after the pilot programme, FCDO should review the emerging evidence and structure the DIB to maximise the target objectives of using the DIB.**
- 3 FCDO should consider following up with DIBs after the end of delivery (building this into contracts as needed) to test the sustainability of outcomes and spillover effects.**

Recommendations to the wider DIB sector

- 4 Clarify roles and responsibilities upfront.** The many stakeholders involved in a DIB can drain resources and time. To ensure stakeholders are adding value to delivery, roles and responsibilities should be clearly defined and linked to the specific experience and expertise stakeholders are bringing.
- 5 Build in flexibilities into the contract to respond to changing situations without having to substantially change contracts.** It will likely be impossible to incorporate all eventualities into a contract; therefore, building in flexibilities and agreed steps for approving changes will help the DIB mechanism remain relevant in crisis situations. The more that DIB contracts can be made public and learnings captured may help accelerate learnings in this area.
- 6 Be transparent and share lessons learned and key successes and challenges to support the strengthening of the market.** There is a very high level of scrutiny and focus on these early DIBs. It can be difficult to openly share 'failures'. A broader understanding of what 'success' looks like, for instance, including generating learning of what does not work, especially during this pilot phase, will be important for building the wider market.



“ [In a DIB, you are] much more determined to understand how to improve your performance. ”

Outcome funder



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