

# »» Materials on Development Financing



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## Results-based approaches

### An innovative modality becomes more significant in Financial Cooperation

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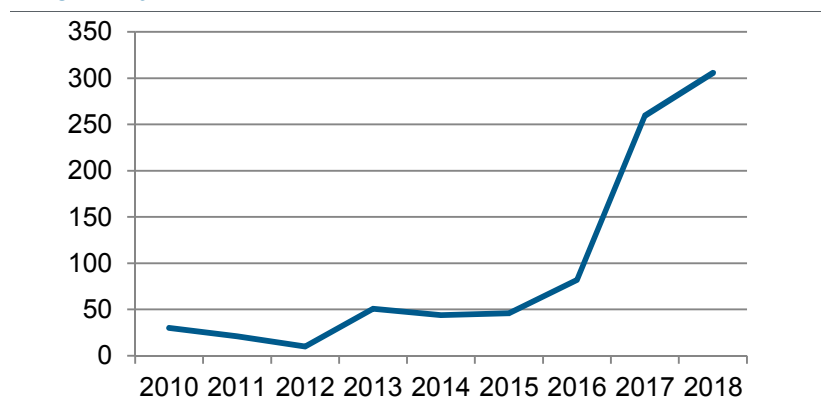
The discussion about more results-based approaches in international development cooperation (DC) has led to the development and implementation of new approaches since the beginning of the new millennium. These approaches place a much stronger focus on results. These so-called results-based approaches (RBAs) are characterised by the fact that financing is linked to the achievement of previously agreed results that are relevant for development. Unlike traditional investment projects, costs are not reimbursed; instead, results and impacts are rewarded. This modality is increasingly gaining importance in Financial Cooperation.

#### Basic principles of results-based approaches

RBAs are characterised by the fact that donors tie payments to evidence of achieved outputs, outcomes or impacts. To do this, donors and recipients agree to the sum that will be paid per achieved result unit before the

project is implemented. In contrast to traditional development projects, in which payments are usually made when there is progress during implementation (cost reimbursement logic), in RBAs, payments are only dependent upon verifiably achieved results.

**Graph 1: KfW commitments for RBAs 2010-2018**  
 In EUR million



Source: own data

The responsibility for achieving the results, and thus for selecting the measures required to achieve them, is borne solely by the partner (who also must ensure that the relevant environmental and social compatibility standards are complied with). The partner must pay the costs for implementing these measures in advance and also bears full responsibility for their success: if the results are not or are only partially achieved, or if the constraints were violated, the partner receives no payment (or only reduced payments). This set-up creates a clear incentive for the partner not only to completely achieve results (effective-

ness), but also to do so in the most cost-effective way (efficiency) because the partner has to pay for any partial achievement and all additional costs.

The donors have the advantage that they only need to pay for results that were truly achieved.

### Payment based on indicators

So-called disbursement-linked indicators (DLI) are used to measure the degree to which previously agreed results have been achieved. The indicators can be at different levels of the impact matrix. It is thus possible to reward the immediate outputs of a measure (e.g. the number of vaccinations performed or schools built) and outcomes (e.g. the number of qualified graduates or rainforest area that was protected from deforestation). The indicators can also be based on the longer-term development policy impacts from a certain project, e.g. progress made towards sustainable transformation of the economy or achieving individual SDGs.

Because the agreed result indicators are fundamentally important for RBA project disbursement decisions, they have to meet certain quality criteria. These include that the indicators have to be clearly defined, transparent and also plausibly quantifiable. The period in which the agreed results need to be achieved must also be clearly specified. The higher the level of impact of the results indicators is, the more complex it usually becomes to measure them, and verification of the results also tends to be more costly.

Furthermore, the timing and methods for checking the achieved results must be defined before project implementation. It is also necessary to clarify who is responsible for verifying the agreed results and thus creating the basis for making decisions about the related disbursements.

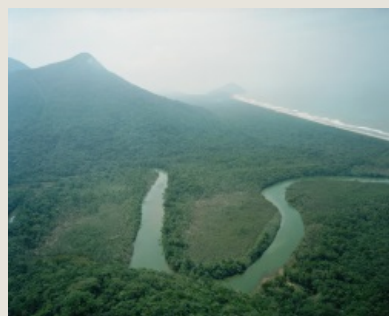
### What types of countries and results are suited to results-based approaches?

Whether a results-based approach is suitable for a certain project in certain countries and sectors depends on various factors: first, strong commitment on the recipient side is important as the full responsibility for project implementation and thus for its success is with the party executing the project. The capacity of the partners executing the project also has to be accurately assessed. Ideally, partners should demonstrate that they have sufficient capacity to also achieve the results independently. Otherwise, technical support measures are necessary. However, these should also be completely within the partner's scope of responsibility so as not to undermine the results-based approach.

Other important criteria are the availability of suitable indicators that can be used to measure achievement of the results independently, without doubt, promptly and at reasonable expense, and a chain of effects that is as simple and clear as possible so that achieving the results is not a gamble for the partners and, instead, can be substantially influenced.

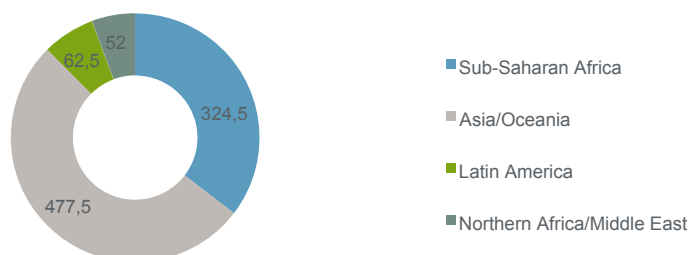


#### Example 1: REM – Country component Acre, Brazil / results-based financing for climate protection measures



One of the greatest sources of emissions worldwide comes from the greenhouse gases released through deforestation. Deforestation, particularly in tropical regions, releases large amounts of CO<sub>2</sub> in a very short time. This is why forest preservation is key to protecting the climate. To advance climate protection through forest preservation, the United Nations anchored the REDD concept (Reducing Emissions from Deforestation and Forest Degradation) in its Framework Convention on Climate Change. With the REDD Early Movers (REM) programme, Germany supports REDD pioneers who are already independently making moves towards climate protection. Climate protection efforts made by Early Movers are remunerated with compensation payments for measurable and independently verifiable CO<sub>2</sub> emission reductions. Fair distribution of the funds (benefit sharing) favours sustainable development in support of smallholders and populations living in and from the forest. In the Brazilian state of Acre, KfW remunerates lowered emissions based on a historic deforestation baseline. To do this, data from the Brazilian monitoring system PRODES are consulted and regularly evaluated by an independent scientific committee. CO<sub>2</sub> savings are then remunerated based on an agreed lump sum.

Graph 2: KfW commitment volume for RBA per region In EUR million



Source: own data



**Example 2: Educational SWAp ESP-FASE – Mozambique**



Despite considerable progress, Mozambique remains one of the poorest countries in the world. Measured in the context of the Human Development Index, Mozambique is towards the bottom of the list. The illiteracy rate is high. Women are disproportionately affected. KfW supports the Ministry of Education as it implements reforms in line with the Sustainable Development Goals (SDG), pursues inclusive and equitable education (SDG 4), and achieves gender equality and autonomy for all women and girls (SDG 5). Donor financing is tied to verified results to some extent. This includes completion of classrooms, hiring additional personnel and the implementation of recommendations from strategic sector studies. KfW thus contributes to expanding the capacities and improving the quality of Mozambique's primary education capabilities. In addition to school-age children and young people, the measures also benefit teachers and employees in the Ministry of Education.

Results-based approaches can be used very flexibly. In poorer developing countries, they should primarily target the output level (outputs that can be achieved with simple and highly standardised

measures) to ensure that local implementation capacity is not overburdened and that the financial risks for the partner country are bearable. More complex measures should only be implemented with partner countries that have more capacity and are able to bear more risk.

**Different kinds of results-based approaches**

An increasing number of development actors are concerned with the development and application of RBAs leading to the development of different forms of RBAs. Their primary difference is the level on the impact chain related to the disbursement-linked indicators. So-called output-based aid approaches are on the lower end (e.g. reimbursement and coupon systems for vaccinations performed or births assisted). At the other extreme there are the development or social impact bonds, where only the actual long-term development policy effects achieved are rewarded (such as the reduced prevalence of diseases or lower infant and maternal mortality rates). Between these two extremes is a broad spectrum of approaches that follow a similar principle and bear a wide range of monikers, such as results-/performance-based financing, cash-/aid-on-delivery or the World Bank's "Program-for-Results" financing. The REDD (Reducing Emissions from Deforestation and Forest Degradation) programmes also qualify as RBAs because their financing is linked to the

avoidance of CO<sub>2</sub> emissions.

**Results-based approaches in KfW's portfolio**

KfW Development Bank is currently supporting 40 ongoing RBA projects on behalf of the German federal government, 13 of which are purely results-based and 27 contain one or more results-based components.

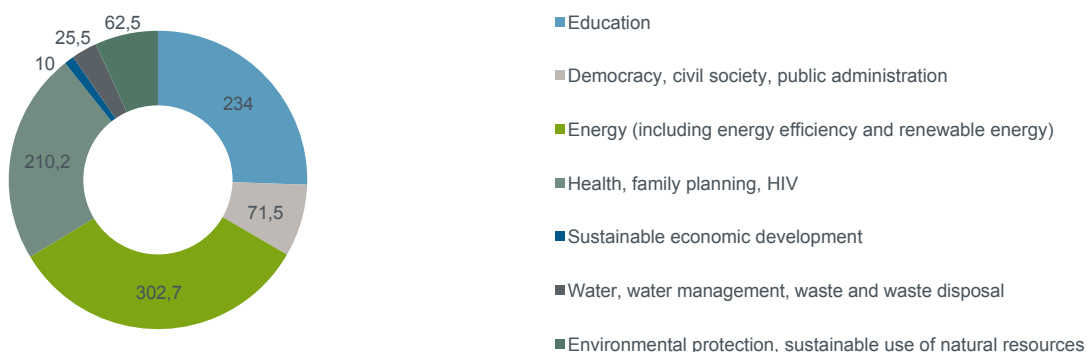
Overall, these projects amount to around EUR 916 million, EUR 735 million of which is disbursed based on results.

The volume of new commitments for this type of financing and the financing volume have increased quite dynamically in the last few years (see Graph 1).

The RBA projects are spread across four regions of the world and 20 countries (see Graph 2). The geographic focus areas are in Asia and sub-Saharan Africa; 85 per cent of the promotional portfolio commitments are in these areas. The remaining commitments are spread across Latin America and the Middle East / North Africa.

Around EUR 494 million of the EUR 916 million total promotional volume are from the federal budget, while EUR 423 million are financed using funds that KfW has raised on the capital market. Market funds are mainly used in Asia and make up close to 90 per cent of the promotional commitments for results-based projects.

**Graph 3: KfW commitment volume for RBAs by priority area**  
In EUR million



Source: own data



With the exception of three projects, all RBA-projects contain the alleviation of poverty as a primary or secondary objective. Furthermore, around three quarters also contribute to gender equality.



### Example 3: Water Services Trust Fund – Kenya



Residents of poorer areas in Kenyan cities often have no access to adequate drinking water supplies or sanitation facilities. On the one hand, Kenyan water suppliers lack the financial funds and expertise. On the other hand, there are hardly any incentives to supply these often unofficial settlements. For this reason, the Kenyan government started the Water Services Trust Fund (WSTF). Together with other donors, Germany has supported the WSTF from the start. In addition to traditional investment projects and accompanying awareness campaigns, demand-oriented, results-based components from the WSTF have recently been piloted. Here, water suppliers first pre-finance investments using equity and bank loans. Only after successful execution does the WSTF reimburse a part of the investment costs, thus reducing the debt. The water suppliers usually take out a private bank loan for the first time. This is an important step on the path to financial independence, and the trust fund works closely with them on that path.

With around 17 ongoing projects, the numbers suggest that the majority of the projects are in the health sector. However, judged by the promotional volume, the health sector is only in third place behind the energy and education sectors (compare with Graph 3).

The sectoral focus areas of results-based projects differ according to the regions. In Latin America, RBA projects focus on environmental and climate protection. In sub-Saharan Africa and Asia, the main projects implemented are projects in the health sector. In North Africa and the Middle

East, the focus is both on health and on decentralisation/municipal development.

### Opportunities and challenges

Several typical opportunities and challenges can be derived from KfW's and other donors' previous implementation experience with results-based projects:

- The willingness to use results-based financing modalities is a good proxy indicator for a partner's motivation and will to reform.
- Transparency during evaluation of the projects' success can reinforce the target groups' trust in the partner groups' institutions.
- Indicators at the output or outcome levels are usually easier to achieve than those at the impact level due to a shorter chain of effects.
- When designing programmes, it is important to pay attention to simplicity and clarity from the very beginning so that the potential efficiency gains of RBA are not relativised due to complex structures and lengthy discussions.
- Defining an appropriate incentive payment (per achieved results unit) in advance that offers sufficient financial incentives for partners on the one hand and also ensures the efficient use of resources on the other is no simple task.
- The mechanism is particularly well suited for advanced and productive developing countries. Poorer countries often have difficulties pre-financing the necessary measures and also bear a greater risk of failure due to weaker implementation structures. Poorer countries can obtain support for pre-financing from the donor through various vehicles.
- Uncertainty surrounding the amount (and possibly the timing) of the payments is a significant challenge for budget planning of the donors and the recipients alike.
- From the perspective of the donors, the modality is also appealing because the donors only have to pay for the results that were realised (no risk of failure) and they already know exactly how many funds they need to raise for each result unit before implementation begins (the

financial risk and also the financial opportunities are borne solely by the partner).

### Conclusion: potential for more widespread use in DC

In summary, results-based approaches fundamentally offer a useful and interesting addition to the financing instruments traditionally used in DC. RBAs facilitate very extensive execution of the principles from the Paris Declaration for improving the effectiveness of development aid (ownership, managing for results, alignment, harmonisation, mutual accountability).



### Example 4: District Development Fund – Ghana



In Ghana, provision of donor funds for poverty- and development-oriented municipal services (for example in the areas of education, health and transport) are result-based to some extent. All local authorities are annually evaluated based on defined indicators (based on their transparency, openness and accountability to citizens, the quality of their planning systems, etc.). Achievement of certain performance target values is rewarded with disbursements from a multi-donor basket fund (responsiveness factor grant). If performance is bad in areas relevant for disbursements, capacity building measures are implemented (compulsory). The efforts of municipal administrations are thus not only noticeably improved with regard to provision of basic services, but also in terms of efficiency and accountability. Based on the positive experiences, Ghana has now decided to integrate this financing modality into the national fiscal transfer mechanism.

They can be used very flexibly (from the simple financing of performed vaccinations through to anti-corruption initiatives and entire sustainability strategies). Results-based approaches are not all-purpose tools; certain pre-requisites must be in place if they are to be useful and meet expectations. However, the potential of using this financing modality is still largely untapped in international development cooperation.



#### Example 5: results-oriented financing of maternal and infant health – Malawi



Deliveries in hospitals or health stations used to be rather rare in Malawi. To increase the number of safe births and improve the quality of health services for maternal and infant health, KfW financed a project that used performance-based payments on both the demand and the supply sides. This meant that health facilities received financial "rewards" when they achieved certain targets or services. These services or targets were linked to both improved quality and an increase in the amount of services rendered. This was evaluated quarterly. Furthermore, annual adjustments were made for targets/services relevant for disbursement.

On the demand side, so-called cash transfer cards were distributed to pregnant women who came to a registered facility. This enabled the women to claim a share of the transport costs and a lump sum for the time that they spent in the facility due to the birth and follow-up care. Patient costs that are pre-financed by the health providers using the cash transfer cards are only reimbursed after the treatment and disbursement depends on the number of treatments performed.



#### Photos

KfW photo archive: photographer: p. 01: v.l.t.r.: photothek.net, Dawin Meckel, Rendel Freude; p. 02: Rüdiger Nehmzow; p. 03: auslöser-photographie; p. 04: Rolf Obertreis, Bernhard Schurian; p. 05: Jonas Wresch



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