Building back better: Evaluation insights on reconstructing the private sector in fragile and conflict-affected contexts

The European Bank of Reconstruction and Development (EBRD) is working in nearly 40 economies across three continents, many of which are affected by conflict and fragility. Since Russia invaded Ukraine in February 2022, the EBRD has been working in a dramatically challenging and rapidly evolving operational context. Large-scale war and destruction in Ukraine, its significant negative effects for neighbouring countries, and its disruptions for the supply chains and markets are particularly damaging for the private sector. Bank's clients, facing relocations, loss of assets, partial curtailment of operations and dramatic market changes, require bespoke type of financing and advice, often packaged together with the emergency support and subsidies.

Eight lessons that emerged from evaluative evidence:

1. Knowledge of context and accessible data are key for successful interventions
2. Presence and continuous engagement on the ground secures relevance in the peace settlement phase, while partnership approach is crucial for sharing risk and adding value
3. Absorptive capacity of recipients is a risk that can and should be mitigated
4. Effectiveness of recovery stage investments is the highest when they are sequenced based on clear prioritisation criteria, with consideration of specific sectors
5. Trust Funds are an effective mechanism for supporting planning, co-ordination and delivery of technical assistance
6. Identification and application of specific products should be flexible
7. Gender inequalities must be factored into any investments in conflict and post conflict contexts
8. Improved assessment of the impact of interventions is crucial for enhancing the effectiveness in FCC
This fifth issue of the “Connecting the Dots” series proposes independent evaluation insights from EBRD as well as from 18 International Financial Institutions (IFIs) and Development Financial institutions (DFIs). It covers a range of important elements of reconstruction efforts in conflict-affected countries regarding private sector support, ranging from strategic approach to practical toolkit of Recovery and Reconstruction.

**Strategic Approach to Conflict and Fragility**

At present, almost a quarter of the world’s population – 1.8 billion – live in fragile contexts. By 2030, this figure is set to rise to 2.2 billion. There is unanimity amongst IFIs/DFIs that economic development can be achieved by enabling recovery and growth of the private sector in fragile and conflict-affected contexts (FCCs), simultaneously addressing drivers of fragility and conflict and state-building and peacebuilding efforts.

The need for a dedicated approach to investment in FCCs and directly affected countries is recognised by IFIs. Most of these institutions have produced a strategy or ‘approach’ in recent years or updated a previous strategy (the World Bank and the African Development Bank). These documents explain the position of their institution vis-a-vis FCC, the areas of focus, comparative advantages, capacities and mandates. These approaches are rooted in an analysis of what works in FCC and evaluations of IFI past interventions, although those are not numerous.

Currently the EBRD does not have a dedicated policy or strategy in FCC, nor has it undertaken any targeted/dedicated evaluations or assessments of its own substantial engagement and experience with fragility and conflict. The EBRD has a unique offering in support for the private sector, extensive experience in conflict-affected countries, specifically Western Balkans, Caucasus, and Central Asia, and capable staff in the field. The EBRD’s six key transition qualities may have specific meaning in a particular context and will require calibrating against recovery and reconstruction objectives in coordination and collaboration with other IFIs and partners. EBRD will benefit from the recently launched real-time evaluation of ongoing crisis response to war on Ukraine and offer to its internal stakeholders, as well as international partners, the insights that are so essential for designing and implementing private sector investments in FCC.

Lessons from other institutions can offer a useful building block for EBRD’s own actions.

**1 Knowledge of context and accessible data are key for successful interventions**

Private sector development in FCC is more effective when it is guided by the ‘do no harm’ principle rooted in a deep understanding of local context, targeted diagnostics and accurate analytics. Evaluative evidence emphasises that detailed context-specific analysis is needed for a comprehensive understanding of fragility and conflict dynamics; their implications for socio-economic development, inclusive growth, sustainable development and good governance. For example, the EU Delegations now routinely advocate for in-depth Conflict Screening Analysis (CSA) for their countries of operation. Experience of other organisations suggests that one-off assessments are insufficient in the dynamic and complex situations. A real-time impact analysis is useful in identifying, at an early stage, both negative and positive effects, including any unintended results. Another opportunity is to use local actors to validate diagnostics of IFIs/DFIs to ensure context clarity. Open data, when available, is essential for understanding the impact of conflict in country affected by war, such as Ukraine.

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1 Previous CtD include: IFIs Operations in Egypt; MDBs in Sub-Saharan Africa; Climate Finance; Gender mainstreaming
2 IFIs include the African Development Bank (AfDB), the European Investment Bank (EIB), the International Finance Corporation (IFC), the World Bank (WB), the International Monetary Fund (IMF). DFIs included BII (British International Investment formerly CDC; Proparco a subsidiary of Agence Française de Développement (AFD) focused on private sector development; KfW (the German Development Bank) and FMO The Netherlands Development Bank
3 These institutions include, inter alia the OECD; Overseas Development Institute (ODI); the Brookings Institution; Clingendael; NYU Centre on International Cooperation (CIC); Stockholm International Peace Research Institute (SIPRI); Centre for Global Development; IRC; Mercy Corps.
Evidence also shows that the private sector cannot be assumed to be an always-positive participant in FCC. Private companies can be part of the conflict system, supporting one conflict actor or another and directly benefiting from the conflict. That’s why some DFIs, like Dutch Entrepreneurial Development Bank (FMO), recommend developing fragility maps and conflict actors mapping to feed into investment and monitoring process. IFIs may use tools such as a Conflict Sensitivity Helpdesk as a resource for staff, or “fragility lens” for appraisal to identify the context, potential impacts of the conflict on investments, and vice versa, the impact that investments could have on conflict.

Linked to the importance of understanding context is the issue of working with good data. The evidence shows that the least context knowledge is typical for the earliest phases of recovery, when organisation is under the most pressure to deliver quickly and decisively. Easy access to country diagnostics from other IFIs, DFIs, and donors offers potential solution, and there is well-stocked database launched by a group of international actors, including EBRD, in 2017.8

Working in partnership with local expert networks can mitigate the risks of poor data. The findings from the WBG’s experience with Post Conflict Needs Assessments (PCNAs) reflect the need for joint assessments which, when effectively designed, managed, and supported by senior leadership from the partner organisations and national stakeholders, are efficient response to crisis and post-crisis situations.9 Another opportunity is conducting Joint Country Diagnostics, such as one recently conducted by EIB and EBRD in Georgia.10 The UN, inter alia, is pursuing the potential for exploiting complex risk analytics.11

A real-time impact analysis is useful in identifying, at an early stage, both negative and positive effects, including any unintended results.

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7 TrustWorks Global and NIRAS for FMO (2021) Conditions for Successful Investment in fragile and conflict-affected states
8 https://www.countrydiagnostics.com/
10 EBRD EIB (2021) Georgia Country Diagnostic. This joint publication between the EBRD and the EIB aimed to identify the key challenges and opportunities for promoting private sector development as well as public and private sector investment in Georgia
11 The UN’s Complex Risk Analytics Fund established in 2021 is a unique multi-partner trust fund (MPTF) that will pool investments in critical data and analytics capabilities to help partners better anticipate, prevent, and respond to complex risks in fragile and crisis settings. It will also utilise AI and innovation in the analysis of social media, geospatial, video, audio, image, sensor, and other data.
12 EBRD EvD (2022c) Evaluation of EBRD’s investments in the West Bank & Gaza.
14 EBRD EvD (2020) EBRD-Ukraine Stabilisation and Sustainable Growth Multi-Donor Account. Interim Evaluation
15 EBRD EvD (2022c) Evaluation of EBRD’s investments in the West Bank & Gaza.
16 The EU Delegation in Palestine in 2021 supported IFI partnership working and coordination through establishment of the EU – Palestine Investment Platform in an effort to foster policy dialogue on investment and to help better identify, prioritise, coordinate and promote investment opportunities
Absorptive capacity of recipients is a risk that can and should be mitigated

Past evaluations across the MDB system indicate that in an active conflict situation there are few realistic prospects for investment other than emergency works to safeguard vital infrastructure due to the limited absorption capacity of the recipients. Factors that have affected IFIs’ ability to scale up support to FCC include: (i) availability and quality of clients, (ii) upstream engagement, (iii) cost of doing business, (iv) risk management, (v) collaboration, and (vi) incentives.27

Evaluation reports often indicate that the risk linked to the absorptive capacity of recipients can be ameliorated through training, for example with Partner Financial Intermediaries (PFIs).28 The Asian Development Bank (ADB)’s experience suggests that technical assistance (TA) can help PFIs to improve product development, lending policies and procedures, risk management procedures, management information systems and IT infrastructure. Evaluations of the IFIs’ activities suggest the need for more upstream and policy work to contribute to developing the pipeline of projects needed to keep the recovery moving and then complimentary TA to build local capacity. In addition, mechanisms to track effectiveness of project work for real-time learning are beneficial.

The Evaluation of Western Balkans Investment Framework (WBIF) commissioned by the EU has found that country stakeholders looked at the “single sector projects pipeline” as an opportunity for the development of their strategic projects, thus increasing ownership of investments.29 Furthermore, the pipeline was seen in some countries not only as an opportunity to engage in a genuine prioritisation exercise but also to avoid duplication of effort and unnecessary discussions and negotiations about projects that are not considered a priority by the country.

Experience of IFIs’ and DFIs’ engagement in FCC clearly indicate the need to stay engaged on the ground and over time.

Effectiveness of recovery stage investments is the highest when they are sequenced based on clear prioritisation criteria, with consideration of specific sectors

Evidence shows that the sequenced strategy of private sector reconstruction in FCC must be customised and owned by local stakeholders. Also strategic partnerships can be a way to overcome resource limitations. All IFIs/DFIs recognise that supporting the private sector requires backing from the government, as it plays an important enabling role. Political instability is often the biggest constraint to private sector development in FCC, though in some instances, such as Ukraine, political cohesion may be a positive factor in private sector development.30 The sequencing can be influenced by the perception of risks. Despite ‘no regrets’ approach to rapid response in Ukraine, erring on the side of moving aid as quickly as possible and keeping fiscal compliance standards too rigid might be counter-productive to rapid response.

Physical reconstruction priorities need to be identified in a plan that meets competing demands and allocates appropriate resources. Sequencing is a challenge and priority sectors defined by respective government agencies and international partners might differ, as they are aligned with institutions’ own mandates, focusing on their own areas of interest, e.g., health, education, agriculture, and using their own proprietary methodologies for assessing damages and loss.31 The principle of ‘programme criticality’32 holds that aid providers should be prepared to accept higher levels of risk when needs are critical. For example the World Bank Group in Yemen has focused on private enterprise in sectors that are key to resilience and recovery: trade, construction, finance, and agriculture. The focus is on immediate and short-term investment and policy recommendations to support the recovery and stabilization needs of private sector operations during and following the end of the conflict. It follows that engagement with private sector stakeholders is a pre-requisite and that coordination is key to success (see lesson 2).

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27 Ibid.
30 IFC (2014) The Private Sector in Fragile and Conflict-Affected States. IEG Insights
32 UN CEB (2013) United Nations System Programme Criticality Framework. Chief Executives Board for Coordination, CEB/2013/HLCM/
Analysis of past Reconstruction and Recovery Plans reveal a focus on the following sectors in the immediate aftermath of a crisis, which are linked to ongoing humanitarian operations:

1. security of civilians, food and medicine supplies
2. security of energy and water supplies, provision of emergency fuel supplies
3. support for re-establishing vital infrastructure; road infrastructure, ports, airports, rail networks
4. financing for local government to manage local services, including waste collection and rubble removal
5. food security including support to maintain agricultural production and open ports. Noting that the relationships between food security and violent conflicts are conditioned, mediated and influenced by the specific context in which they take place
6. availability of construction materials
7. private sector support for the pharmaceutical industry and related supply chains

Independent evaluation of Western Balkans Investment Framework (WBIF), which is also implemented by the EBRD, suggests three relevant lessons for efficient process and meaningful results: (i) importance of solid and high-quality pipeline of projects owned and prioritised in accordance with the real needs of key country stakeholders, such as Ministry of Finance; (ii) flexibility and responsiveness of Bank processes for preparation and implementation stages; (iii) transparency in decision making during the programming phase to ensure deep and productive engagement with the country stakeholders.

Recent lessons gained through addressing the COVID-19 pandemic are also relevant to support for private sector reconstruction. During the pandemic the private sector received life-saving support, targeting short-term liquidity needs created by the crisis; helping firms preserve their investment plans. The policy was to sustain the provision of services and safeguard business activities with the goal of preserving livelihoods. One unfortunate outcome of emergency support for the private sector during the pandemic was the heightened risk of corruption in the use of funds, as highlighted by the UK Government’s National Audit Office. Evidence alludes to cybersecurity as another risk. It is critically important to engage the public and private sector in cybersecurity. Discussions of the cyber-threats to critical infrastructure have become more frequent in the wake of the cyberattacks against Ukraine’s power grid in 2015.

Trust Funds are an effective mechanism for supporting planning, co-ordination and delivery of technical assistance

Trust Funds used by most IFIs are a financing arrangement set up with contributions from one or more development partners, sometimes referred to as Multi-donor Trust Fund (MDTF). The funds are held in trust by a third-party (administrative agent), for allocation across an extended or unspecified time period in fulfilment of priorities of the recipient nation. EBRD refers to Trust Funds as a Multi Donor Account (MDA).

EBRD has extensive experience of Trust Fund management, including a single country MDA for Ukraine. It was established in 2014 as part of a multilateral urgent crisis-response measures to support Ukraine in the wake of major crisis. Evaluation findings suggest that the MDA’s scope is in line with the EBRD’s mandate and core capabilities, and has proven to be strategically relevant, operationally efficient and effective, and enabled key institutional changes in Ukraine. It also found that EBRD’s engagement has supported economic recovery and growth. Another EBRD Trust fund utilised in the West Bank & Gaza has funded TA as well as SME investments, demonstrating the flexibility and utility of TFs. EBRD independent evaluations emphasise the importance of maintaining flexibility of fund allocations, recommending against the earmarking of individual funding streams.

26 IFC has acknowledged that its emergency response to Ukraine is modelled on its COVID-19 response, which included a fast-track facility to provide liquidity and a global health platform to accelerate health-related investments. See also https://www.consilium.europa.eu/en/documents-publications/library/library-blog/posts/think-tanks-reports-on-covid-19-and-the-recovery-fund/
27 See also NAO (2020) Investigation into the Bounce Back Loan Scheme. HM Treasury, Department for Business, Energy & Industrial Strategy, British Business Bank plc
29 The EBRD Ukraine Stabilisation and Sustainable Growth Multi-Donor Account (Ukraine MDA) was launched in 2014 as part of a multilateral crisis-response measures to provide urgent support to Ukraine in the wake of major political, security, economic and humanitarian crises. A total of fourteen donors contributed €53.5 million to the Ukraine MDA. The TF has been extended until July 2024.
30 The EBRD (2022c)
A review of MDTFs in relation to improving aid effectiveness highlighted the significance of impact the political contexts have on their success or failure.36 Too often MDTFs are designed and implemented without considering the political environment or security concerns; and with unrealistic expectations. It suggested that in FCCs, the IFIs should have a common purpose of creating decent jobs and economic opportunities, while also focusing on improving regulatory frameworks for trade, finance, and business.

Overall Trust Funds, established with a clear set of objectives, can underpin the provision of TA and support for essential policy reform to improve the investment climate. TA and grant funding are critical in the early project development stage and support development of a pipeline of bankable projects. However, TF design must contain the requisite clarity over objectives and management sufficient to guide collaboration and to consider the differing institutional mandates, priorities, and budget cycles of partners.

Identification and application of specific products should be flexible

Recovery and reconstruction in Ukraine will be a steep learning curve. Evidence suggests that experimentation and innovation should inform the development of collaborative financing frameworks and allow the development of new products that enable IFIs/DFIs to assume greater risks in fragile environments.37 Due to the extreme and persistent uncertainty experienced in FCC, identifying what works requires “sustained, iterative experimentation and active inter-institutional learning and lesson-sharing”.38 In this case, the EU candidate status received by Ukraine in June 2022 might potentially work as an anchor and help knowledge-sharing around the EU’s drive for conditionalities and gradual milestones.

In many situations of conflict IFIs/DFIs need to tackle the uncertainty that private sector investors experience in investment decisions. Evidence shows that this can be partly achieved through de-risking private sector investment e.g., through blending arrangements, guarantees, subsidies, currency management arrangements, etc.39 Even more important is to ensure that private investors can rely on ‘anchor investments’ essential for making their investments productive and profitable, e.g., the transport and telecom infrastructure, the banking sector, the local service sector, etc.

An important lesson from the WBG is the need to develop financial mechanisms or fast-response facilities in FCCs, as well as use its global convening power more effectively.40 As an example, in June 2022 the World Bank’s Board approved the establishment of a financial intermediary fund (FIF) that will finance critical investments to strengthen pandemic Prevention, Preparedness and Response (PPR) capacities at national, regional, and global levels, with a focus on low- and middle-income countries.

The evaluation shows that there are tried and tested tools and products to bring to bear in FCC. Based on these findings, IFIs and DFIs can develop a new generation of innovative financing tools to manage risk and improve financial flows to fragile contexts. These tools include:

- **Blended Finance**, that helps reduce the risk to investment in fragile contexts and bring in private capital, promoting collaboration across diverse stakeholders, and taking a holistic approach to private sector and socio-economic development. Lessons from evaluations have been captured to help guide the diverse stakeholders supporting blended finance. From an implementation perspective, enhanced principles have been developed by the DFIs to guide using Blended Finance.41 The OECD has also developed principles for blended finance focusing on SDG financing. Blended finance targets projects that are smaller and riskier, which is typical for firms in FCC. In 2018 blended finance supported over 40 percent of IFC’s FCC/Low Income IDA commitments, and over the last five years, nearly half of investments in the financial and agribusiness sectors of FCC. A risk-sharing agreement between IFC, the European Investment Bank, and Ecobank (a pan-African commercial and investment group) illustrates the potential for blended finance.

- **Innovative Concessional Financing Facilities**, where donor contributions can be used to reduce

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32 Notwithstanding some donor preferences
38 Collier et al., “Strengthening Development Finance in Fragile Contexts.” Pg 28
39 Barder, Owen and Talbot, Theodorem (2015) “guarantees, Subsidies, or Paying for Success? Choosing the right instrument to catalyse private investment in developing countries”, Centre for Global Development
the cost of borrowing for development projects that can benefit target communities.

- **Guarantees**, that can be powerful catalysts to attract private-sector investments and commercial financing for increasing development impact to support economic growth and improving public services. Although, Banks such as FMO recognise they need to do more to measure the success and impact of portfolio guarantees.

- **Social Impact Bonds**, which are public-private partnerships whereby investors fund interventions that improve social outcomes that are of interest to a government and the private sector. The investors are paid a return if the interventions successfully demonstrate a social impact.

- **Political Risk Insurance**, aimed at reducing the barriers to investing in fragile contexts, including breaches of contract, export prohibition, political risk, war, asset dispossession, etc. In FCC political risk insurance is often only available to foreign investors due to the high cost. MDBs could support efforts to make political risk insurance available to local investors to promote their investment in fragile markets.

- **Currency Management Instruments**, which address currency risk needs. Local currency financing significantly reduces risk of foreign exchange for investors. This can be achieved through currency management instruments, such as the IFC's Local Currency Facility, which provides long-term local currency in IDA countries where market solutions are not available, or capital markets are not sufficiently developed.

At the same time the evaluations teach that having the tools ready to bring to the market does not mean they will be used. The Evaluation of EBRD’s Ukraine MDA found some elements of the General Conditions that were not utilised, for example the use of funds by other IFIs or the financing of investment grants, concessional funding and first-loss guarantees. EvD advised management to investigate the reasons behind the lack of demand for these instruments.

Past experiences suggest that investing in and developing markets in FCC takes more than money. Financial support should be accompanied by advice, regulatory reforms, staff presence on the ground, capable intermediary organizations, capacity building, management of complex environmental and social issues, and recruitment of strong lead investors. The IFC's evaluation suggests avoiding the dilemma of choosing between short-term and long-term impact.42 Both approaches are valid in FCC. In all cases, evaluations suggest that IFIs/DFIs should also make more explicit the risk-reward trade-offs and implications for investments in FCC in the context of their portfolios.

### Gender inequalities must be factored into any investments in conflict and post-conflict contexts

Women are disproportionately affected by conflict, violence and natural disasters. None of the fragile contexts, for which data is available, are on track to achieve Sustainable Development Goal 5 on Gender Equality. The UN Security Council has adopted 10 resolutions related to Women, Peace and Security (WPS), which guide work to protect and promote the rights of girls and women in conflict and post-conflict contexts and to ensure their participation in peace processes and negotiations.44

**Accordingly, IFIs and DFIs seek to support projects that promote social cohesion, gender equality, women’s economic empowerment and social inclusion, and peaceful community relationships.** Reflecting the rise in non-financial additionality in recent years, the Banks ensure the application of their Environmental and Social Standards and a strong commitment to equality and inclusion are important elements of the investments, regardless of the sector in which they take place. Some DFIs, like FMO, are advised to extend their investment-specific due diligence to include potential impact of the project on gender dynamic.45

**FMO has doubled its lending practices via financial institutions to vulnerable groups between 2014 and 2019.** Especially loans targeting women-owned enterprises increased sharply in the last five years, but FMO also reached more young entrepreneurs and micro-enterprises (microfinance). The positive development impact of these microfinance and gender-financed deals was confirmed in other FMO studies.46 FMO has also found that earmarking loans to financial institutions (FI) clients for use towards vulnerable groups has helped the FI sector create a significant impact on SDG10, in particular on reducing within country inequalities.

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There remains a paucity of evaluations that focus on fragile context amongst IFI; and there are many institutions whose evaluation policies lack reference to fragility or conflict. At the same time, there are signs of increased recognition of their value and recommendations for change in this regard.

- FMO has scant data available on jobs, growth, and other fund development impacts.\(^47\)
- The UK Government’s National Audit Office (NAO) has advised that CDC (now BII) to do more to capture its development impact in FCCs. It should build a measure of attribution to help make investment decisions and to improve accountability for its performance. CDC should incorporate a broader range of development impact criteria and indicators into its assessment of investment opportunities and ensure these are systematically considered in the selection process.\(^48\) ICAI, The UK’s Independent Commission for Aid Impact, observed that “CDC should strengthen the monitoring and evaluation of the development impact of its investments in low-income and fragile states, and the learning from this, working with DFID to accelerate their joint evaluation and learning programme”.
- In the Annual Review of UK support to MIGA’s ‘Conflict Affected and Fragile Economies Facility (CAFEF)’, evidence on ways to encourage increased private sector investment in fragile and conflict-affected states was assessed as weak at the time of programme design and remains weak. For this reason, evidence building was incorporated into the programme design.
- The World Bank has suggested it needs to rethink what success looks like in FCCs. This will require moving away from an over-reliance on quantitative metrics, attribution, and short time frames that do not suit the nature of these country programs and their contribution to higher-order outcomes.\(^49\)

All IFIs including EBRD would benefit from considering how they can improve their assessment of impact in FCCs. Ongoing real-time evaluation of EBRD’s Resilience Package for Ukraine could help fill this gap.

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