



Frequently Asked Questions

Multi-Input Area Development Global Development Alliance Initiatives in Afghanistan and Tajikistan

TERMS:

MIAD: MULTI-INPUT AREA DEVELOPMENT

GDA: GLOBAL DEVELOPMENT ALLIANCE

In this document, we use MIAD GDA to refer generally to the hybrid vehicle.

1. HOW DOES THE MIAD GDA PARTNERSHIP APPROACH DIFFER FROM USAID'S TRADITIONAL APPROACH TO FOREIGN AID?

Like many development and philanthropic organizations, USAID sees itself primarily as a grant maker—it is in the business of providing money to achieve beneficial ends. While it does not expect to make any financial return, it nevertheless has high expectations for its capital. It makes grants to advance US development and political objectives, always with an eye toward making the world a better place. As USAID puts it, “The purpose of foreign aid should be ending the need for its existence, and we provide development assistance to help partner countries on their own development journey to self-reliance—looking at ways to help lift lives, build communities, and establish self-sufficiency.”¹

The two hallmark innovations of the MIAD GDA were to (1) find a way for USAID capital to catalyze true investments into business enterprises, and (2) to take a portion of the hoped-for ensuing profit stream and place them into a social grant-making foundation. This was done with the intent of making the capital “the gift that keeps on giving” for the localities in Afghanistan and Tajikistan (the first two pilot countries).

¹ <https://www.usaid.gov/what-we-do>



USAID is traditionally seen as barred from investing in private enterprise. In the MIAD GDA, USAID grant money supported common development programs managed by the AKDN, and this was used to free up capital by AKDN to invest in social enterprises identified as appropriate by the two agencies. There was an additional commitment that the pro rata portion of the profits from the investment that could be assigned to USAID capital would flow not to USAID but rather into a “trust” mechanism in country to make further grants in country.

The benefits over traditional “-100% return” aid grants include the following:

- USAID capital would indirectly capitalize real enterprises to hire workers, generate income, and create wealth, prosperity, and stability in the locality;
- The profit stream would be evergreen and therefore, the long-term trust mechanism would have a permanent and sustainable source of capital to fund future social programs, meaning USAID’s capital would be recycled productively; and
- Both the enterprises and the trust would exist within a region whereby the local residents would see their own communities growing and profiting from the new enterprises, as opposed to so many businesses that take from communities without giving back.
- In sum, the MIAD GDA was a novel approach to fulfilling USAID’s mission to “lift lives, build communities, and establish self-sufficiency.”

2. HOW DOES THE MIAD GDA DIFFER FROM THE AGA KHAN’S LONGSTANDING MIAD DOCTRINE?

The Aga Khan Development Network has a rich tradition of utilizing its “multi-input area development” approach in the regions where it works. The MIAD doctrine intentionally uses social and cultural programs alongside investments to support one another and to create synergies. The novelty in the MIAD GDA mechanism was combining this development approach with a major international development agency in partnership, and establishing a trust fund to hold and disperse investment returns back into social development activities within specific geographic regions. The MIAD GDA married AKDN’s capital and social programming and USAID’s, leveraging both parties’ capital and development expertise.

3. ARE THERE NECESSARY OR HELPFUL PRE-CONDITIONS TO CONSIDER WHEN DEVELOPING SIMILAR, BLENDED FINANCE PARTNERSHIPS IN THE FUTURE?

The Implementation Guide that accompanies this document goes into findings from the study. In sum, the authors suggest the following as sine qua non conditions for an innovative partnership like this to succeed in the future:

1. Ensure buy-in across participating stakeholders at both the senior and working levels. Trust built at one level and not at both results in slowdowns and hold-ups.



2. Provide a robust pipeline of investable opportunities at the outset of the partnership. This is challenging since staff need to do the front-end work to identify potential investments and do preliminary “due diligence” even before there is an agreement in place. However, launching an agreement and not having good opportunities to put money to work can lead to frustration and second thoughts by capital holders.
 3. Ensure the investment decision process is streamlined to the greatest extent possible and also flexible enough to ensure adaptability to changing socioeconomic and political contexts.
 4. There are various styles of private company investment: early stage, growth stage, buy outs, utilities and infrastructure development, etc. It is important to match the investment skills of the agents with the investment opportunities in the target country. For example, it makes no sense to have electric power development experts on staff if the investment pipeline comprises mainly small social enterprise startups.
 5. Remember that even the most successful, profit-oriented private investment firms will invest in companies that fail. Investing in frontier markets (especially) or the developing world (generally) will likewise have a share of failed investments, perhaps even a high share. The key to this is to make sure that taking sensible risk is tolerated, even encouraged. Failure may be an outcome on a given project, but overall the successes should outweigh the failures. This is classic “portfolio theory.” In sum, if the investment agents fear to fail, then they will never invest at all. Senior leadership has to make it acceptable to fail on individual investments, provided the portfolio succeeds overall.
4. THE TAJIKISTAN ESCOMIAD CAME AFTER THE AFGHAN MIAD GDA. DID IT DIFFER AND IF SO, HOW? WHAT WERE THE LESSONS LEARNED IN THE AFGHAN MIAD GDA THAT WERE APPLIED TO ESCOMIAD?

Both AKDN and USAID learned from the Afghanistan MIAD GDA experience that it was beneficial to launch these agreements with an investment already identified within the collaboration agreement. This made approval processes for USAID much easier during the project period. Therefore, the ESCoMIAD was launched with an investment already agreed; it was an investment into the First Microfinance Bank of Tajikistan (FMFB-T).

Of course, Tajikistan does not have the ongoing security and stability issues that Afghanistan has, and that has made collaboration and investment sourcing more straightforward.

That said, it must be noted that neither country has many extant opportunities for private investment, FMFB-T is an arm of the AKDN; this made due diligence much simpler and more reliable. It may be difficult to identify with certainty an investment in the agreement itself in future iterations. This reinforces the point made above that it is critical to have a pipeline of potential opportunities identified by the investment team as the agreement is taking shape.



5. WAS SPECIAL LEGISLATION REQUIRED FOR THE US GOVERNMENT TO EXECUTE THIS TYPE OF PARTNERSHIP?

No special legislation was required.

6. DOES THIS APPROACH ONLY WORK FOR FRONTIER MARKETS? WHAT MAKES A SUITABLE POTENTIAL TARGET COUNTRY FOR THIS KIND OF AGREEMENT?

In theory, the MIAD GDA joint venture concept could be applied to any country or region in which USAID or other bilateral or donor groups work. As with any investment-led vehicle, of course, the underlying economy needs to be robust enough to enable sufficient deal flow and then cash flow to make enterprises successful. One of the takeaway lessons from the first two MIAD GDAs is that the group may have chosen regions where there are insufficient volumes of enterprises (or profits) to meet the ambitions of the trust mechanism. This needs to be monitored in the go-forward period. A concentration of actors that can and will implement multi-sector and place-based social development must also be considered.

7. WHAT ARE POTENTIAL CRITERIA FOR SOURCING INVESTMENTS?

Within MIAD GDA and ESCoMIAD, AKDN officers in the field, especially AKFED, sourced deals. USAID was very clear throughout that it did not see itself as an investment expert. AKDN, chiefly AKFED, sourced deals through meetings with international and local business people, bankers, and entrepreneurs both within and external to the AKDN. In future MIAD GDAs and other public-private partnership arrangements, and as noted prior, it is important that investment managers be knowledgeable of the local economy and also familiar with the appropriate style of investment within that country (early stage, late stage, infrastructure, etc.). The creation of accelerators and the pipeline of entrepreneurs who tap into microfinance networks also create excellent potential sources of investable opportunities.

8. SHOULD INVESTMENTS BE DESIGNED TO GENERATE A FINANCIAL RETURN WITH A LITTLE SOCIAL UPSIDE OR A SOCIAL RETURN WITH A LITTLE FINANCIAL UPSIDE, OR ARE BOTH EQUALLY WEIGHTED?

The MIAD GDA and ESCoMIAD were conceived to put equal weight on financial returns and social benefits. The social benefits were forecast to flow both from the direct enterprise investment (leading to jobs and outputs) and from the later Trust-funded grants to social programs. In practice, very few investments have been concluded, in part perhaps because the financial screen was too tight.

In future iterations of MIAD GDAs, the parties ought to consider the trade-off between investing in smaller social enterprises, where the financial returns may be weaker or farther into the future, with consequent negative implications for the Trust but potentially greater impact to local job and wealth creation; or



investing in larger scale, more mature opportunities that may not require the capital as much but that are more likely to provide dividends and financial returns.

9. HOW ARE THE INVESTMENTS MANAGED?

MIAD GDA and ESCoMIAD investments were overseen by AKFED and AKF Impact Investing staff in Washington DC. In the single investment done to date and the investment in the pipeline, AK staff have board seats on the enterprise. As a matter of general policy, AKDN officers try to meet with relevant entrepreneurs at least once a month and insist on quarterly financial reporting. Depending on the size of the investment and the stage of the enterprise, more frequent interactions with the entrepreneurs are often necessary.

At some point, it will come time for the ownership to “seek liquidity,” meaning a payback on their investment. This can occur in many different ways, including dividends, having their shares bought out, interest payments (if the capital was injected as a loan), or in a very few instances, taking the company public in a share offering. The process of generating liquidity is a crucial one for the successful investor to manage with his/her fellow board members, shareholders, and management.

10. HOW CAN INVESTMENT IMPACT BE MEASURED?

The two classic measurements for financial success in investment are Internal Rate of Return (IRR) or Return on Investment (ROI, also called cash-on-cash returns). IRR is highly sensitive to the holding time for the investment; the longer the hold period, the harder it is to hit a high IRR unless there is an opportunity for a massive uptick in valuation over the years, which is unusual though not impossible in the developing world. In our judgment, ROI is a better financial metric for frontier investment.

The phrase “risk-adjusted rates of return” is a shorthand way of saying that investors expect a higher potential return for taking more risk. That is because if they take higher risk, then across the portfolio a greater number of their investments will fail, which means they have to earn more from the ones that succeed. Investing in frontier markets is perceived as being among the riskiest investment markets in the world. Since returns are not likely to be as robust in frontier markets as in developed markets, there are often very few and often no “investable opportunities” for pure market-oriented investors. This is precisely why MIAD GDA type vehicles that bring investors together who are not simply profit-oriented are so valuable. USAID and AKDN can have much higher risk tolerance than ordinary financial investors, which means they can find many more investment opportunities in the frontier markets that meet their risk/reward targets.

11. WHAT CONDITIONS SHOULD BE CONSIDERED WHEN ESTABLISHING A TRUST?

Returns generated by the investments must be administered through a mechanism established either internally or, if and when an independent structure is merited, externally.



Until they are substantial enough to warrant external oversight, these funds will likely be “incubated” internally, in this case by AKF USA. Once a substantial pool of funds has been generated, the funds should be managed by an entity governed by a body that represents the stakeholders, including the communities that the Partnership is designed to support. That entity must have investment and disbursement policies that will ensure that the principal is maintained and grows over time so as to be able to effectively fund social programs after the end of the partnership.

AKF engaged the international law firm White and Case LLC to help determine the most appropriate structure and location for such an entity for the MIAD GDA, based on the following criteria:

- Its ability to provide legal stewardship for the investment proceeds under local governance laws;
- Its ability to invest proceeds and to make grants (legally and practically);
- A reasonable and predictable tax regime;
- Its ability to interact easily with AKDN entities in Switzerland, the Netherlands, and in the United States and with USAID;
- Low risk of political disruption or appropriation;
- Its ability to support the MIAD activities in Afghanistan and Tajikistan;
- A governance structure that would reflect the different stakeholders in the project (AKF, AKDN, USAID, and regional/community representatives); and
- Self-sustainability;

White and Case evaluated the following options based on those criteria:

- A separate restricted endowment fund within AKF USA with its own investment and advisory committees
- An independent US nonprofit organization
- An independent Swiss nonprofit organization
- An independent UK nonprofit organization
- An independent Tajik nonprofit organization – for Tajikistan only
- An independent Afghan nonprofit organization – for Afghanistan only

With input from the law firms Froriep (Switzerland), GRATA International (Tajikistan), and RIAA Barker Gillette Afg (Afghanistan), White and Case concluded that a US endowment fund within AKF USA would be best suited as the eventual trust vehicle. Each of the other options presented issues relating to one or more of the criteria that would make them difficult to implement effectively.

Their reasoning was that creating an endowment fund within AKF USA would not affect AKF USA’s tax-exempt status and, unlike an independent US nonprofit, an endowment fund within AKF USA would not need to manage around private foundation rules. The AKF USA Board of Directors would exercise oversight over the restricted fund, with AKF USA’s Directors’ ordinary fiduciary responsibilities extending to the endowment fund. The AKF USA endowment fund structure also



provides administrative and operational advantages: using the existing AKF USA structure would eliminate the need to create a new entity and would avoid the duplication of personnel and other resources that would be required to manage an independent entity. Finally, because of AKF USA's preexisting relationship and proximity with USAID, this structure is a practical means of implementing the MIAD GDAs.

Others considering such an entity for future partnerships of this kind would need to assess the options in the context of their specific situation, including locations, objectives, and legal framework.

Other potential considerations might include:

- **SIZE:** A large fund might require outside investment management expertise and dedicated staff;
- **COMPLEXITY:** An agreement with multiple partners might require the fund to have particular governance, accounting, and reporting considerations;
- **EXPENSE MANAGEMENT:** Each structure will have different requirements to ensure that staffing and management expenses are managed appropriately.

12. COULD PARTNERSHIPS LIKE MIAD GDA BE CONSTRUCTED BY PARTIES OTHER THAN THE AKDN AND USAID? IF SO, WHAT WOULD MAKE FOR GOOD POTENTIAL PARTNERS?

Absolutely, the hybrid investment/grant vehicle is one that was intended from the outset to be applicable to any country where USAID or other bilateral or private donors are present, and it was never envisioned that only AKDN could be the other implementing partner. Indeed, while AKDN's reach is wide, there are many markets in which it simply does not operate.

That said, one of the reasons USAID chose to work with AKDN was because of the longstanding investment success that the AKDN, most especially the Aga Khan Fund for Economic Development (AKFED), has had in investing in frontier or under-developed economies. AKFED has built some of the most successful enterprises and chains in the developing world, including hotel chains, telecom networks, and power plants. In terms of social programming, and depending on the geography, AKDN is able to bring a breadth of agencies focused on health, education, the built environment, culture, civil society, and economic outcomes to implement programming in close collaboration with public and private actors.

If another party wants to promote a "MIAD GDA" or similar blended finance agreements in a new area, then the implementer will need to have demonstrated expertise in the region across public, social, and private sectors including investment execution. Alternatively, impact investment groups with experience and expertise could also partner with AKDN and leverage its development experience to achieve more sustainable investments and greater social impact.