

Institutional Capacity Assessment (ICA)

Toolkit for Securities Regulators in Africa

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Dalberg

Key ideas

- Capital market regulators are critical in supporting broader economic growth. A well-regulated market fosters trust and confidence, unlocking capital that is key to economic development.
- Emerging market regulators are very challenged – they play a dual role of regulation and market development yet must do so with limited resources. Unlike more mature markets, these markets are too small and nascent to pay for the regulators they need.
- Institutional capacity assessments (ICA) and institutional capacity strengthening (ICS) programmes are critical tools in this context, providing a means to systematically identify and invest in key regulatory needs.
- ICAs and ICSs for capital market regulators must be managed carefully, with a recognition of the sensitivity of capital markets to signals, the unique contexts of any given country, and the complex dynamics that a regulator must manage.

An effective ICA/ICS for emerging markets follows the DAART approach, aiming carefully and accurately at the right target:

- **D** – Define success tailored to the market’s stage of development, unique needs and context, and the right time horizon.
- **A** – Align with stakeholders, including key decision makers and influencers, on the objectives, process and deliverables.
- **A** – Assemble the right resources, i.e. the advisors, budget and timelines appropriate to a constrained regulator.
- **R** – Respect sensitivities given the role and visibility of the regulator and the risk of inadvertent market signals.
- **T** – Tailor for results so the regulator has the right scope and depth where needed and a clear, actionable plan at the end.



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CONTEXT3
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FRAMEWORKD
DEFINE SUCCESSS
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TAILOR APPROACH

Capital market regulators are mandated to **supervise**, but in emerging markets must also **develop** the markets – all while dealing with resource constraints

Regulators are typically independent public agencies with the mandate to oversee and develop orderly, fair and efficient markets. A well-regulated market builds trust and confidence among those seeking or deploying capital, enabling more efficient, competitive allocation and use of financial resources.

Roles of capital market regulators in emerging markets

Regulation

- **Policy framework:** Ensure a robust policy and regulatory framework is in place.
- **Registration and supervision:** Grant and supervise capital market intermediaries and other capital market businesses and instruments.
- **Competition:** Enforce guidelines that ensure fair competition.
- **Investor protection:** Monitor the disclosure of important information to investors.

Market development

- **Public engagement:** Promote corporate and public awareness of the country/territory's capital market and products.
- **Product development:** Support industry players in launching and trading new products.
- **Industry capacity:** Develop the technical capacity of industry players and investors through training.

Challenges facing regulators in emerging markets

In performing their dual role, many regulators in emerging markets face systemic challenges that adversely affect their capacity. These challenges include:

- Weak and outdated legal frameworks
- Limited financial resources, personnel capacity and technological capabilities
- Mismanagement and public distrust
- Political interference
- Emerging risks in the external environment.

To develop practical solutions for these issues, regulators need a comprehensive assessment which clearly documents the scale of their gaps and outlines solutions in line with their market context

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The ICA and ICS are tools for improving the capacity of a regulator based on an assessment of their challenges and opportunity pathways

Purpose

Institutional capacity assessment (ICA)

An ICA aims to provide a clear picture of an institution's capacity in terms of strengths, weaknesses and available assets. It is a systematic, structured approach to evaluating an organisation's governance, human capital, technology, finances and more.

Institutional capacity strengthening (ICS)

An ICS is a targeted, tailored programme that strengthens a regulator by addressing specific areas. It often follows an ICA and focuses on gaps that the ICA identified, usually through a combination of financial and technical assistance.

Impact

A well resourced and implemented ICA can:

- Provide a regulator with an assessment of issues they had not fully understood or systematically evaluated
- Equip regulators with inputs into a strategic plan, including critical initiatives relevant to market context
- Provide the basis for a regulator to secure resources and political support for key initiatives.

A poorly designed ICA risks:

- Impractical recommendations that are inappropriate to the regulator's current capacity or market context
- Triggering sensitivities that risk damaging the relationship with other ecosystem actors or signaling the market.

This toolkit sources information from: i) insights drawn from FSD Africa's Regulator Support Programme (ARSP) work with multiple regulators in Africa; ii) desk research on global practices and iii) insights drawn from internal and external capital market experts.

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DAART approach to conducting an ICA/ICS for emerging market regulators (II/II)



Target appropriately for the regulator's needs and their particular market context.
Aim the ICA/ICS tools accurately and carefully to maximize the probability of success.

DAART FRAMEWORK



Define success

Clearly articulate a **vision for the capital market** – what it can and should be in the next 3–5 years, and therefore what the regulator must be able to deliver.



Align stakeholders

Identify and build **alignment with the key decision makers** – with the internal team and with external actors (e.g. ministries of finance) who have key resources and relationships.



Assemble resources

Mobilise **fit-for-purpose resources** (adequate funding, time and technical expertise) to deliver results – bearing in mind the constraints facing the regulator itself.



Respect sensitivities

Apply **care and diplomacy** throughout the process, recognising the unique role and visibility of the regulator while balancing this against a thorough and rigorous process.



Tailor for results

Focus on **prioritisation and pragmatism** in both process and deliverables, considering what will help a time and resource-constrained regulator take action.



DEFINE SUCCESS

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DEFINE SUCCESS

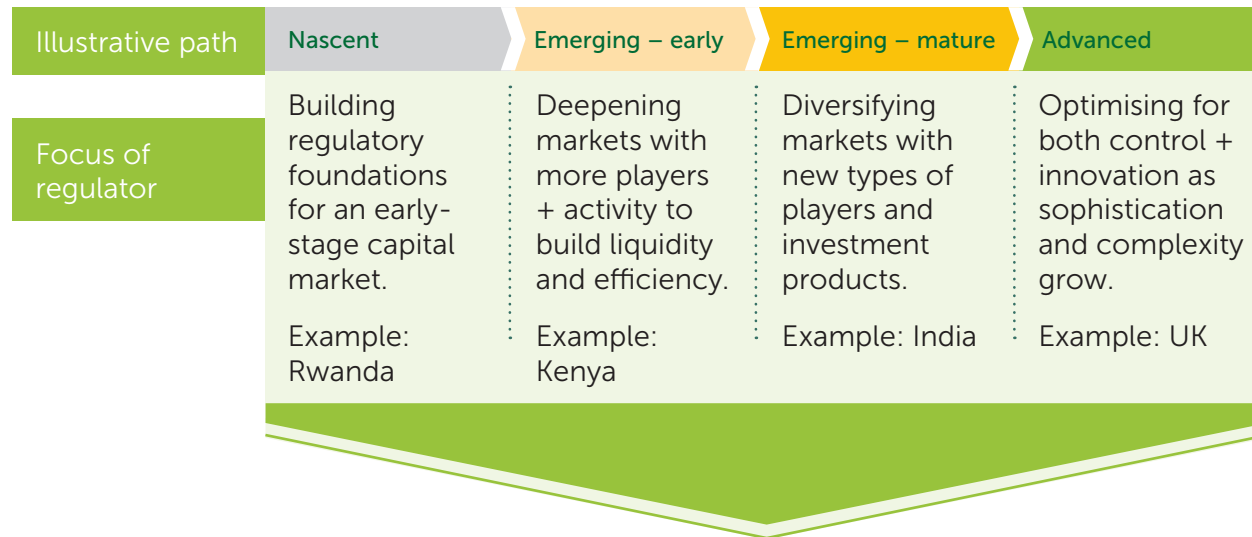
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Definition of success depends on stage of development and achievable medium-term objectives – with implications for what a regulator will need to do



Determining how a capital market can and should realistically evolve over a 3 to 5-year time horizon helps set direction for the role the regulator will play.

This definition of success will in turn **set the parameters for what an ICA and ICS should prioritise** – as well as what can be ‘light touch’.

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With the articulated vision of success, the regulator needs to develop a sense of ownership of the ICA/ICS process within the organisation

Given the long-term and resource-intensive nature of the ICA and ICS, the regulator needs to commit to and drive the process to ensure that its functions are reviewed efficiently, and practical recommendations are implemented. In creating this commitment within the organisation, the regulator could consider the following:

Articulate the definition of success	<ul style="list-style-type: none"> ■ The management needs to articulate two things within the organisation: what the organisation's role is and what success looks like for the capital market. This vision should also explain why the ICA/ICS are critical drivers.
Create buy-in at the board level	<ul style="list-style-type: none"> ■ The management needs to involve the board in the process by conveying the critical ICA objectives. This aims to create a sense of ownership and support at the executive level to drive the process and rapidly adopt the identified action items.
Engage staff	<ul style="list-style-type: none"> ■ The management team can also engage staff to ideate on crucial investigation areas and effective ways of coordinating with the consultants.
Institute open communication	<ul style="list-style-type: none"> ■ The management team needs to institute open channels to share the progress of the ICA/ICS.
Designate internal champions	<ul style="list-style-type: none"> ■ The ICA process needs designated internal champions at the executive, management and technical levels to lead the process and act as point of contact with the consultant.

“

Regulators need to take ownership of the initiative to ensure they completely take into account all the necessary requirements and inputs from them.”

Key voice in Africa capital markets

“

The ICS should be demand driven and not support driven. Donors should articulate the support they will provide, while the regulators need to actualise their commitment to ensure the exercise proceeds well.”

Key voice in Africa capital markets

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The regulator also needs to align with key stakeholders on the ICA process to develop buy-in and consolidate support from the ecosystem

1. Identify key stakeholders¹

The regulator needs to draft a list of key stakeholders to notify and/or engage during the ICA process. These stakeholders can be broadly classified into:

- **Decision makers:** Ministry of Finance; Central Bank; and other financial regulators, e.g. Retirement Benefits Authority and Insurance Regulatory Authority.
- **Resource mobilisers:** FSD Africa; and Donors and NGOs.
- **Key voices:** Member associations, e.g. East Africa Venture Capital Association and ACI Kenya²; market intermediaries, e.g. brokers, investment banks and fund managers; market infrastructure providers, e.g. Central Depository and Settlement Corporation; market professionals, e.g. accountants and legal specialists; and other industry experts.
- **General market participants:** Institutional investors, e.g. pension funds and insurance companies; and retail investors

2. Communicate the ICA process

The regulator can then decide on the level of information on the ICA process that they will share with different sets of stakeholders.

- For example, for the decision markers and resources mobilisers, the regulator can detail the objectives, processes and potential outcomes, such as a strategic plan, in a bid to consolidate buy-in and support.
- For the key voices and participants, the regulator can articulate the objectives of the ICA and how it can transform their capacity and lead to market development and improved efficiencies.



Engaging the Ministry of Finance at the beginning would have made some decisions easier given that it took so long for us to convince them at the end."

Africa-based regulator



With consolidated buy-in, the regulator can mobilise critical resources to drive the ICA process

ICA-relevant resources

Competent consultant	<p>The ICA process requires a competent consultant, who has:</p> <ul style="list-style-type: none"> ■ Expertise in the operational aspects of capital markets and experience working with regulators, thus leveraging existing knowledge when designing tools and processes ■ Local presence and knowledge to establish relationships, capture unique challenges and tailor actionable recommendations ■ Relevant technological, human resource, financial and transformational skills to effectively evaluate the regulator.
Appropriate budget	<ul style="list-style-type: none"> ■ An appropriate budget is required to conduct a comprehensive evaluation of the regulator’s capacity. The budget size needs to be communicated at the onset and revised as needed.
Realistic timelines*	<ul style="list-style-type: none"> ■ The consultant and regulator need to align on realistic timelines, typically 7–9 months, to enable rigorous data collection and analysis of unique market characteristics. ■ After the initial alignment, timely communication and feedback between internal champions and the consultant can enable the assignment to finish within the set timelines.

“Consultants can partner with a local firm, which understands local challenges and can pick up on unspoken aspects.”

Key voice in Africa capital markets

“With more time, the ICA consultants would have engaged more key stakeholders and taken a bit more time with specific ones.”

Africa-based regulator

“With more time budgeted at the beginning, we could have tailored the approach further and assessed more risks.”

Leading ICA consultant

Note: *To ensure that the ICA process is completed within the set timelines, the regulator and consultant can put in place in certain time-saving mechanisms. These include: i) placing clear deadlines for critical deliverables, ii) aligning with the regulator’s internal calendars to avoid scheduling issues, and iii) putting in place risk mitigation strategies at the onset to counter any implementation delays. Source: Dalberg Analysis, 2021



Throughout the evaluation process, the regulator and consultant need to respect internal and external sensitivities that might adversely impact the ICA

Given the unique dual role and visibility of the regulator, any capacity evaluation needs to be communicated tactfully to respect any internal or external sensitivities, and avoid market signalling on the perceived incompetence of the institution.

	Internal	External
Position the evaluation	<ul style="list-style-type: none"> Internally, the regulator needs to affirm that the evaluation does not pose a threat to individuals or departments. Rather, the evaluation is an opportunity to i) document gaps, ii) benchmark leading regulators and iii) build capacity. 	<ul style="list-style-type: none"> Externally, the regulator needs to emphasise the transformative nature of the ICA to the ecosystem. This approach might stop the ecosystem from viewing the regulator as weak, which would potentially impact market confidence
Communicate findings	<ul style="list-style-type: none"> The internal champions need to diplomatically communicate findings without creating adverse attention to departments or individuals identified as the biggest growth areas. 	<ul style="list-style-type: none"> The regulator and consultant need to be mindful of i) the level of output delivered to decision makers vs the general market, ii) how the findings are framed and iii) appropriate timing to avoid raising insensitivities.



The regulator and consultant can host post-ICA workshops with stakeholders and decide on non-sensitive information to share.

Leading development consultant



In particular countries, language can lead to insensitivities, hence the need for tactical wording.

Leading ICA consultant



The consultant can then proceed to tailor data collection and analysis tools to focus on key areas linked to the regulator’s definition of success

Regulator’s evaluation areas/domains (non-exhaustive)*

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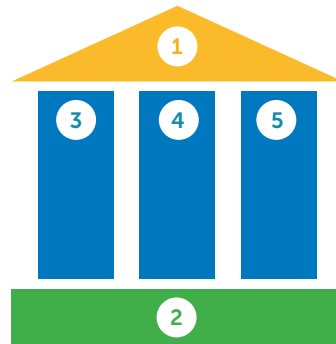
Technical capacity

- Regulatory mandate
- Market development regime
- Enforcement capability
- Vision and mission
- Legal requirements and status

2

Institutional framework

- Organisational structure
- Board and management roles
- Strategic planning processes
- Operational policies
- Internal communication
- External interface: key stakeholder involvement and communication
- Enterprise risk management



3

Human resource

- HR policies and job descriptions
- Staff recruitment and retention procedures
- Staff salaries and benefits
- Staff time management
- Staff supervision and growth opportunities

4

IT and systems capacity

- Technological systems (hardware and software)
- IT governance and policies
- Technological capability (emerging securities expertise and data analytics)
- Information security and business continuity

5

Financial management

- Budgeting and accounting tools
- Financial sustainability and revenue streams
- Internal financial controls
- Financial reporting
- Auditing

Tailor the approach and tools:

For an impactful ICA, the consultant needs to filter through the long list of evaluation areas and allocate more effort to the ones which are linked to the regulator’s definition of success.

The tools should collect quantitative and qualitative data from multiple internal and external sources to validate the insights.

A regulator with well-functioning internal functions leads to:

Reputable perception of the market and the regulator’s capacity

Relatively rapid market response to policy and guideline changes

Proper coordination with key decision makers in the ecosystem

Note: *Based on the market context and ICA focus, the evaluation areas/domains can be broader, covering areas such as programme management, or narrower, focusing only on human resources and technological capacity. Source: ISC, Institutional Capacity Assessment (ICA) of the Ghana SEC, 2019; ISC, Institutional Capacity Assessment of the Nigeria SEC, 2019; A2F Consulting, Institutional Capacity Assessment of the Zimbabwe SEC, 2020; Dalberg Analysis, 2021



The outcome of the internal and external evaluations should include summarised key outputs, clear next steps and practical execution timelines

Process and outcomes

Constant engagement	The regulator and consultant need to establish constant communication channels to counter-check the quality of data analysis and early findings that shape final outcomes.
High-level summaries with clear outputs	The consultant should ideally develop a high-level summary that is easily digestible by stakeholders and points to the specific areas of improvement. Further, the consultant needs to link outputs to the initial objectives and success indicators identified at the onset.
Clear next steps	The outputs should include clear next steps and outline the departments or individuals who should lead the implementation.
Realistic implementation timelines	The consultant should propose realistic and flexible implementation timelines that are suitably linked to the organisation’s operating environment and resource availability.

“The consistent engagement was precise and allowed us to move swiftly on the assignment.”
Africa-based regulator

“We expected the ICA to come out with big four or five areas for focus. Essentially, a strategic plan with details on the gaps and potential competitive advantage.”
Africa-based regulator

“There was no point person for implementation as such. The way we’re structured, implementation lies with the CEO.”
Africa-based regulator



At the end of the ICA, the regulator and consultant can co-prioritise the assessed gaps based on impact and ease of implementation

Impact/importance

The identified gaps can be ranked based on how important the potential resolution is for the regulator. The impact can be on a scale of:

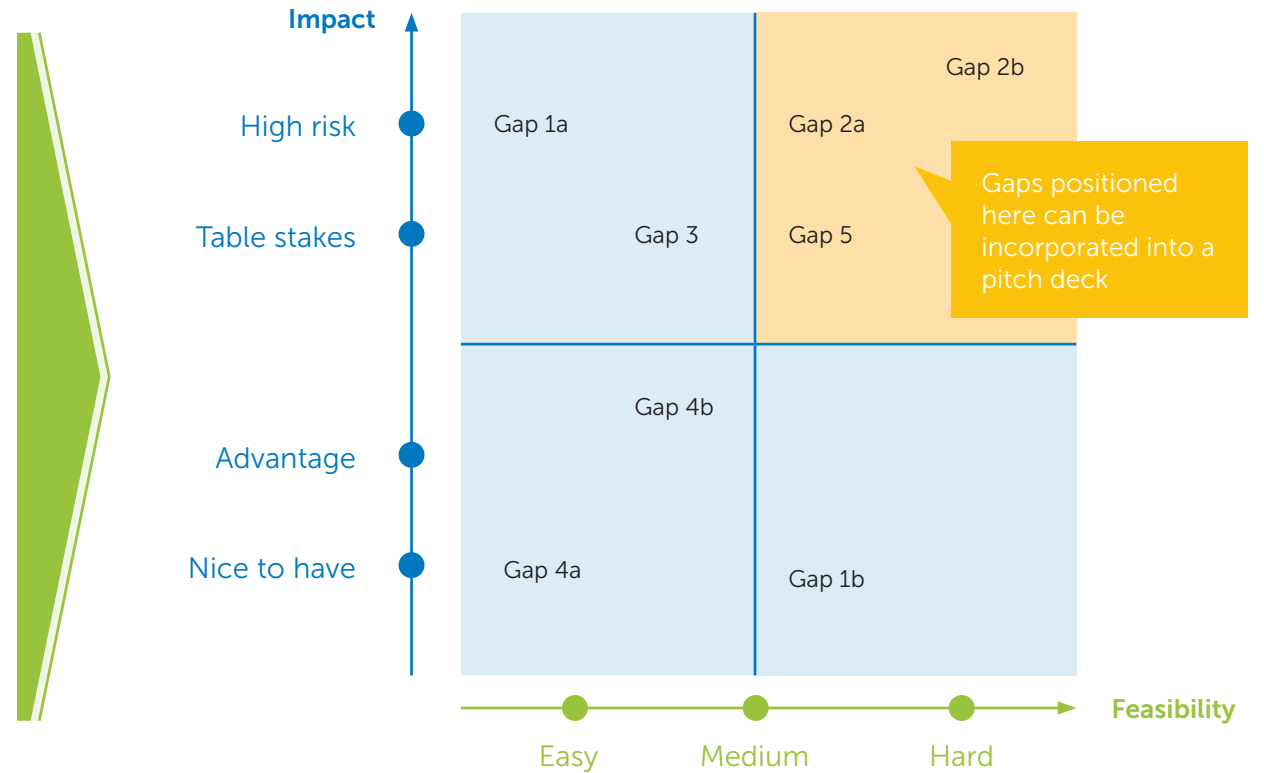
- **High risk** – Ignorance of the gap can lead to adverse implications for the regulator.
- **Table stakes** – Highly impactful and significantly increases the capacity.
- **Advantage** – Moderately impactful and can boost the regulator’s long-term growth.
- **Nice to have** – Least impactful and can be addressed later.

Feasibility/ease of implementation

Within the matrix, the gaps can also be prioritised based on feasibility. The feasibility can be influenced by:

- **Required resources, i.e. financial, personnel capacity and time**
- **Executive and management buy-in**
- **Implementation timelines.**

Prioritisation matrix (illustrative)*



Notes: *Gaps are numbered based on the five evaluation areas, i.e. Gap 1 is linked to the policy framework. Source: Dalberg Analysis, 2021



The prioritised gaps can be synthesised into a pitch deck that outlines support needed from external actors as the regulator proceeds to the ICS

Many emerging market regulators struggle to implement recommendations drawn from the ICA due to limited resources including financial and human resources. In lieu of this, the regulator could develop a pitch deck to source funding and technical assistance from external actors.

Purpose of the pitch deck

- 1 Recognise the regulator’s specific resource constraints, i.e. human resource and funding challenges.
- 2 Persuade potential funders to support the regulator, given the transformative nature of the ICS on the institution and ecosystem.
- 3 Outline the specific actions and timelines of the ICS.



It’s primarily funding that is a challenge. If you have a masterplan to address gaps, then funding is the main challenge.”

Africa-based regulator

Potential storyline of the pitch deck

Gaps	What are the institutional gaps identified by the ICA? Which ones have the regulator and consultant prioritised?
Solutions	For each of the prioritised gaps, what are the practical solutions?
Support	What form of support is needed from external actors?
Implementation timelines and monitoring	Who are the actors who can provide the support?
	Can the support be linked to existing programmes?
	What are the realistic timelines to implement the solution in time to maximise impact?
	What are the specific milestones within the workplan?
	What are the KPI for the process?

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