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SOCIAL ENTREPRENEURSHIP & IMPACT INVESTING REPORT

RESEARCH CONDUCTED BY UTS FOR INNOVATIONXCHANGE: DEPARTMENT OF FOREIGN AFFAIRS AND TRADE

2017

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FROM INNOVATIONXCHANGE

The innovationXchange was launched in 2015 to tackle intractable problems in development – finding solutions by embracing collaboration, partnership and bold new perspectives. A key part of iXc's mandate is to increase the impact of Australian aid through finding and testing new ways to address long held problems. This might be new technologies, the application of new scientific findings, or new ways to influence behaviours to improve development outcomes.

Part of iXc's work has been to understand how to amplify the development impact of social entrepreneurs in our region. The untapped potential of social entrepreneurs remains enormous. Innovative, market based solutions have the potential to deliver sustainable, effective and scalable solutions to development challenges which complement traditional aid efforts.

Our initial research demonstrated that there is demand and need for investment at all stages of the social entrepreneurship value chain in the Asia-Pacific region.

Entrepreneur Support	Encourage entrepreneurs to start and grow businesses that have the potential to deliver region-wide social impact
Enabling Services	Support early stage business to become investable
Marketplace	Connect social entrepreneurs to impact investors
Capital	Encourage impact investment funds to move into underserviced regional markets

iXc engaged UTS to investigate the viability of these portfolio interventions, contributing to a greater understanding of social innovation and insights into how to strengthen regional innovation eco-systems.

This research forms part of a scoping phase that will help iXc deliver targeted programs that make it easier for social entrepreneurs to connect with impact investors from our region and drive innovation to scale.

We thank participants who contributed their insights to this research program, and welcome the opportunity to share the findings of this research with the wider community.

Lisa Rauter, First Assistant Secretary, iXc
Matt Steine, Director, iXc

FROM UTS

The genesis of this research collaboration and program emerged from contributions to the 2015 Senate Inquiry on 'Partnering for the greater good: The role of the private sector in promoting economic growth and reducing poverty in the Indo-Pacific region'[1]. In this submission and final report, I raised ideas around building impact investing markets via mechanisms such as social stock exchanges.

We welcomed the opportunity to take these ideas further in collaboration with iXc and the Department of Foreign Affairs and Trade, examining the entrepreneurial journey in the region and how we could better connect (social) enterprises with investors. This included everything from platforms, exchanges, incubators and accelerators, to education programs and networks, and all types of financing mechanisms to support entrepreneurship in the region.

Fundamentally, I approached this study as an economic sociologist, with the understanding that markets are not naturally occurring - they are built. If we are to develop an impact focussed marketplace, what are the 'rules of the game' regarding access and participation? How is existing market infrastructure working (or not)? How do we decide upon measures and what counts as 'impact'? How will we create common systems of meaning and language, and build expectations and norms around investment deals and returns?

As we worked our way through the various interventions and ideas, it was important for us to consider: who wins and who loses in any such proposed arrangements? And what is the role of the State in market building?

In the field of social entrepreneurship and impact investing, nascent markets demand large-scale qualitative work. As such, we had the privilege of talking to over 110 experts across the region, in addition to analysing secondary materials, and attending international and national events to identify the debates and tensions in this global market building effort. For our work on social stock exchanges I particularly thank our collaborators Dr Hokyu Hwang (UNSW), Dr Kyoung-Hee Yu (UNSW), Mel Dunn (AECOM), Steven Baker (AECOM) and Daniel Madhaven (Impact Investing Australia), and for their contribution to our work on regional incubators, I thank Tamsin Jones and Pip Wheaton (Mosaic Africa Strategy Advisory). Sincere thanks to my UTS colleagues Senior Researcher Dr Gillian McAllister, and Co-Investigator (Part 2), Dr Jochen Schweitzer, and research assistance provided by Alexandra Pitsis, Krithika Randhawa and Martijn Boersma.

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1 http://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Foreign_Affairs_Defence_and_Trade/Indo-Pacfic_Economic_Growth/Report

OVERVIEW

Scope of the research

UTS was engaged by iXc to investigate the viability of a range of portfolio interventions designed to leverage new sources of investment finance and to support the growth and investability of new businesses in the Indo-Pacific region, with a particular focus on the development of social enterprises. Some of these interventions were relatively new within the aid sector while others were designed to take a fresh perspective on an existing activity. This report sets out our findings for each of the interventions examined.

While the interventions we investigated were wide ranging, they are all key components of the entrepreneur's journey and their ultimate participation in an impact investing marketplace. Given that our brief focused on the development of new businesses in the region, we considered how early stage enterprises could be funded; how entrepreneurs (and particularly social entrepreneurs) could be incubated and supported to develop their business skills; how new financing structures could be deployed by government to attract more private investment into the sector; and the role of platforms in connecting enterprises and sources of capital in brokering deals. The scheme below sets out the scope of our research program, mapped against iXc's social entrepreneurship value chain.

Entrepreneur Support	> Crowdfunding platforms > Microfinance
Enabling Services	> A regional network of incubators
Marketplace	> Social stock exchanges
Capital	> Blended finance > Pay by results

Key themes from the research

In spite of the broad scope of our inquiry, some overarching themes emerged that will be important for any future entrepreneur support programs in the region, particularly as they relate to social enterprises and impact investing.

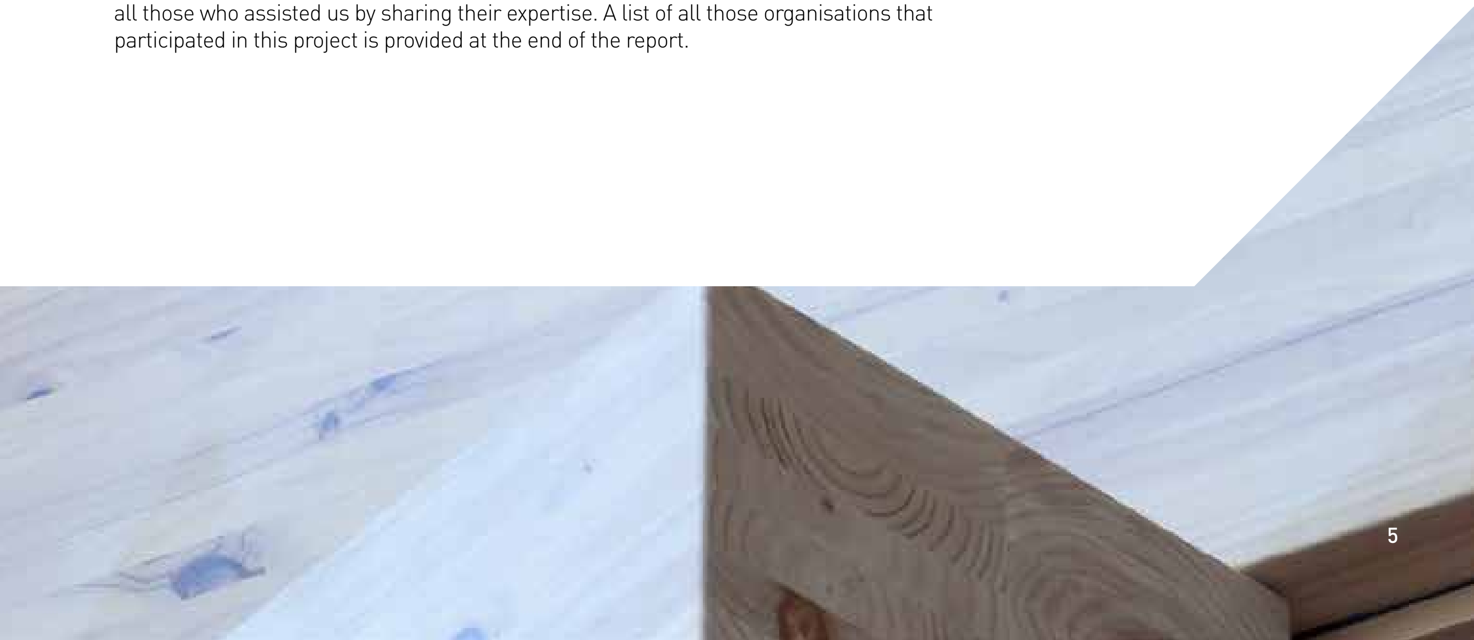
1. There is an inherent difficulty in measuring impact and an associated challenge for diverse stakeholders to agree on measures to understand (social) entrepreneurial performance and the viability of impact investing deals.

2. Given the diversity of the region, specialisation in support programs may be a more efficient approach, with specialisation based on stage of business, sector/industry, or business type (e.g. impact business).

3. In this eco-system, market infrastructure is necessary but also struggles to sustain itself at this nascent stage, and we see a clear role for government in supporting such infrastructure.

Acknowledgements

We were privileged to speak with more than 110 people across the region in the course of working on this project and we undertook a broad-ranging review of research papers and secondary reports. We also built a database of incubators and accelerators, crowdfunding platforms and microfinance organisations relevant to the region. We are very grateful to all those who assisted us by sharing their expertise. A list of all those organisations that participated in this project is provided at the end of the report.



ENTREPRENEUR SUPPORT

When examining entrepreneurship across the Asia-Pacific region, one of the most striking features is its diversity. The region includes some of the world's leading entrepreneurial economies, such as Australia, Taiwan and Singapore, but also some of its least developed, such as Myanmar and Bangladesh.[2]

As part of its survey of entrepreneurship, the ASEAN Regional Entrepreneurship Report 2015/16[3] analysed the key constraints to entrepreneurial activity in the region. Across the region, the leading barrier for entrepreneurs was lack of access to finance. Also important was the capacity for entrepreneurship, which is a combination of attitudes and aspirations, skills and capabilities.

In this section we explore two opportunities for iXc to support entrepreneurs in the region:

> Crowdfunding platforms, that can assist entrepreneurs to test their ideas as well as to source finance; and

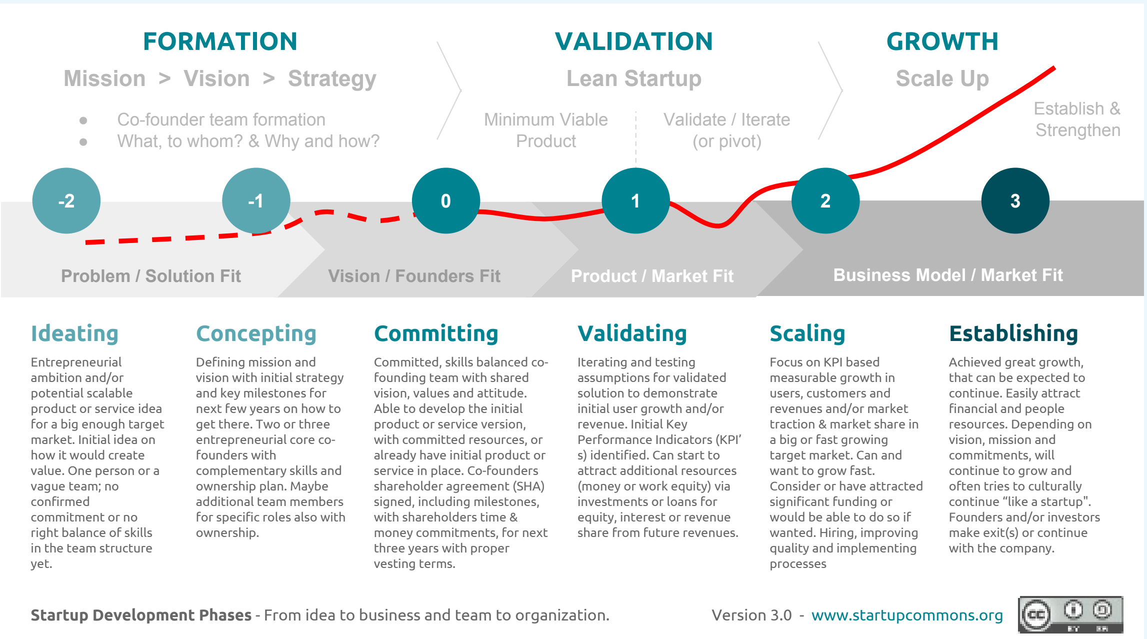
> Microfinance, which has a long history of supporting micro, small and medium size enterprises but may also represent a pipeline for impact investors.

The research considered the viability of interventions in these areas and how they might address the challenges faced by entrepreneurs in the early stages of their business journey.

2 Acs, Z., Szerb, L., and Autio, E. (2016). Global Entrepreneurship Index 2016. The Global Entrepreneurship and Development Institute, Washington, D.C., USA.

3 Xavier, S.R., Sidin, S., Guelich, U., and Nawangpalupi, C. (2016). ASEAN Regional Entrepreneurship Report 2015-2016. International Development Research Centre. file:///C:/Users/130239/Downloads/2015-2016%20GEM%20ASEAN%20Report.pdf

FIGURE 1: Start-up development phases[4]



4 This diagram was developed by startup commons: http://www.startupcommons.org/download-documents.html

Crowdfunding platforms

Focus of the research

This phase of the research program assessed the potential role of crowdfunding platforms in providing support for start-ups and early stage businesses. It also considered whether there are opportunities for iXc to support these platforms as a strategy for connecting entrepreneurs in emerging markets with the capital they need to grow their businesses.

Background to the issue

Crowdfunding is a method of collecting many small contributions from a large number of people, via an online platform, to fund a project or venture. In this research, we assessed crowdfunding for its potential to provide funding support for start-ups and early stage businesses in the Indo-Pacific, and particularly social enterprises.

Crowdfunding has emerged as an alternative to traditional finance and philanthropic giving.

- It enables individual crowdfunders to direct their contributions to specific campaigns. In the traditional charitable model, an individual contributes money to support the general purposes of a benevolent organisation which then decides how to apply that money.
- Minimum threshold amounts for investment are kept low in order to allow ordinary funders or investors to take part in the process.
- The role of 'the crowd' is to assess the merits of the projects put forward. Crowdfunding is built on the proposition that the crowd can efficiently choose legitimate projects by aggregating the knowledge and expertise of a large and diverse group of people.

For those who are seeking funding, crowdfunding platforms offer two different approaches. Projects or campaigns all need to set a target amount to be raised. Some platforms then take an **'all or nothing' approach**, so that if a project or campaign does not achieve its target, the proposer receives none of the funds pledged. Other platforms offer a more flexible **'keep what you raise'** model, where the proposer receives any funds that are pledged even if the project target is not met. Some platforms allow proposers to choose between these approaches.

There are several different types of crowdfunding platforms.

> "It is still early days for crowdfunding. Despite all the euphoria about ecommerce, there are still significant challenges [in developing markets], the first one being that not many people have their own bank accounts or credit cards."
> Business incubator manager

TABLE 1: Taxonomy of crowdfunding platforms[5]

Category	Nature of the exchange	Examples
Donations	Philanthropic donation or gift, no return expected	> GoFundMe
Rewards/pre-purchase	Contribution in exchange for a perk (such as t-shirt, thank you card, production credit, meeting with artist or performer) or a pre-order of a product	> ArtistShare > Chuffed > IndieGoGo > Kickstarter > Pozible > StartSomeGood
Lending	Capital repayment, most often with interest	> Funding Circle > Kiva > Lending Club > One Acre Fund > Prosper > United Prosperity > Zidisha
Equity	Investment for an ownership stake in the business	> Crowdcube > Microventures (also working in partnership with IndieGoGo) > Seedrs
Royalty	Crowdfunders invest in campaign owners and receive a share of (future) revenue earned in return for the investment	> AppsFunder > Quirky

Our research focussed on three of these streams - rewards/pre-purchase, lending and equity - as these were most relevant to early stage businesses.

Crowdfunding offers a range of benefits and risks for both the funder ('the crowd') and the proposer (the individual or enterprise seeking to raise funds). These advantages and disadvantages can vary according to the type of platform. The table below provides a summary assessment.

5 Massolution (2015). 2015CF. The Crowdfunding Industry Report. http:// www.crowdsourcing.org/research.

TABLE 2: Benefits and risks of crowdfunding[6]

	Benefits	Risks
For 'the crowd' (funders)	Fundraising is a much more engaging and interactive experience than typical giving or investing. Funders 'go on the journey' with the project.	Fraud: there is opportunity for proposers to put forward projects with no intention of delivering.
	Funders can influence the design of new products to better serve their needs.	Crowdfunders are not specialist investors and will have access to less information about the past performance of the entrepreneur (proposer) or about the industry than is typical when investing in a business.
	Funders obtain early access to new products and new companies.	
	An investment portfolio can be diversified across sectors or platforms at very low cost.	
	Minimum investment thresholds are low so individual contributions can be relatively small. As a result, risk remains low.	
	Individual funders can choose projects that are of direct interest to them, so have greater control over how their funding is applied. This is of particular relevance to social purpose projects or enterprises and can make crowdfunding more attractive than philanthropic giving through an established charity.	
	Funders have access to a wide range of funding choices from across the globe.	

[6] Agrawal, A., Catalini, C., and Goldfarb, A. (2013). Some simple economics of crowdfunding. Cambridge, MA: National Bureau of Economic Research. Working Paper 19133. http://www.nber.org/papers/w19133; Gajda, O., and Mason, N. (2013). Crowdfunding for Impact in Europe and the USA. Toniic Network. http://www.toniic.com/wp-content/uploads/2013/12/CrowdfundingForImpact.pdf; Lehner, O. M., Grabmann, E. and Ennsgraberb, C. (2015) Entrepreneurial implications of crowdfunding as alternative funding source for innovations. Venture Capital. 17 (1–2): 171–189; Schwienbacher, A. & Larralde, B. (2010). Crowdfunding of Small Entrepreneurial Ventures. Final draft of book chapter forthcoming in Cumming, D. (Ed.), The Oxford Handbook of Entrepreneurial Finance. Oxford University Press. http://www.em-a.eu/fileadmin/content/REALISE_IT_2/REALISE_IT_3/CROWD_OUP_Final_Version.pdf; Vitins, M. (2013). Crowdfunding and Securities Laws: What the Americans Are Doing and the Case for an Australian Crowdfunding Exemption. Journal of Law, Information and Science. 22(2): 92.

	Benefits	Risks
For the proposer (enterprises and individuals seeking funds)	Crowdfunding can offer a source of funding when there are few funding sources available, other than the individual or entrepreneur's own resources. Early stage businesses in general find it difficult to attract funding from banks or mainstream investors; this issue is magnified for early stage businesses in emerging markets.	To be successful, a proposer needs to invest considerable time in developing a campaign, designing campaign materials and (where relevant) perks and keeping in touch with supporters through updates and feedback.
	The online call-out provides a form of marketing for the project and its products, at very low cost.	A proposer needs to be skilled in using online tools and managing social media channels to run their campaign.
	Due to the online and interactive nature of funding campaigns, the crowd can be involved in development of a product or project and can contribute ideas and feedback. This provides a form of consumer product testing, again at low cost.	If a project is highly successful and attracts many funders, the proposer may be overwhelmed and unable to deliver, resulting in loss of reputation. This applies particularly to reward-based platforms.
	A successful campaign provides valuable signals as to the market potential of a product. This demonstration of demand can be used to support later stage capital raising.	There is a greater risk of ideas for new products and businesses being stolen as they need to be shared with a much wider audience than is typical for traditional forms of fundraising.
	Transaction costs (and therefore the cost of capital) are lower due to platforms using business models based on margins from a high number of transactions. Processes are often automated, which also contributes to lower costs.	A great deal of information about the business trying to raise capital becomes public knowledge, including plans for their enterprise and the amount of money actually raised. This can impact on the business's capacity to negotiate with future suppliers and customers.
		In the case of crowdfunded equity investments, investor management may be significantly more costly due to the sheer number of funders who need to be managed.

Insights and findings

Experience from crowdfunding platforms operating in the developed world shows that platforms can potentially be successful vehicles for:

- Testing the viability of products and business models; and
- Providing early stage financing and assisting small businesses to scale.

However, our research revealed a range of challenges for the operation of crowdfunding platforms in developing economies:

- Low e-commerce penetration which impacts on the ability of platforms to attract funders;
- Lack of online banking infrastructure, which hinders financial transactions from platforms to businesses;
- Difficulty of developing an adequate revenue stream so that platforms can remain financially viable. The revenue model for most crowdfunding platforms is based on a transaction fee for successful projects, usually 4-5% of the total funding amount. Given the small amounts of money requested by projects in developing countries, the actual amount of revenue generated can fall short of the resourcing required to support the platform

Platforms based in developed economies can provide support to businesses in emerging markets but to do so successfully the platform needs to:

- Work with effective and reliable local intermediaries;
- As an alternative, focus on project proponents with developed world connections;
- Connect projects back to funders in the developed world, including diaspora communities.

"There are definitely ways to engage donors and continue to excite donors or funders to projects and teams and maybe create longer term relationships through a platform."
Platform operator

Regardless of where the platform is based, start-ups and small businesses will only be able to benefit from crowdfunding if they can undertake the online marketing campaigns required of crowdfunding. While crowdfunding is seen as a channel for those who have traditionally lacked access to capital, running a successful crowdfunding campaign still requires certain skills, including:

- Skills in using social media;
- Capacity to market and engage the 'crowd';
- Planning and preparation.

We found some platforms have responded to this challenge by providing quite intensive support to entrepreneurs in relation to their campaigns while others offer more standardised tools and guidelines. These approaches each have cost and resourcing implications for platforms and flow through to the business models adopted.

While some studies have confirmed that crowdfunding can be a useful path to creating ongoing businesses,[7] both the available research and interview feedback provided to this project suggests that entrepreneurs need to have some fundamental business skills if they are to take their business forward and achieve the goals set, post-funding. Business education and training programs may therefore need to sit alongside crowdfunding platforms if businesses using the platforms are to successfully obtain funds and scale.

In spite of these challenges, the World Bank[8] has concluded that **crowdfunding models have potential for the developing world.** They put forward the following models as suitable for exploration in the developing world:

- Rewards/pre-sale models (where less than $US 100,000 was sought) for projects and products would be suitable and could function as a testing ground for proof of concepts for high growth, innovative start-ups;
- Investing or equity platforms (where less than $US 250,000 was sought) would be suitable for technology innovation and for high growth, innovative start-ups.

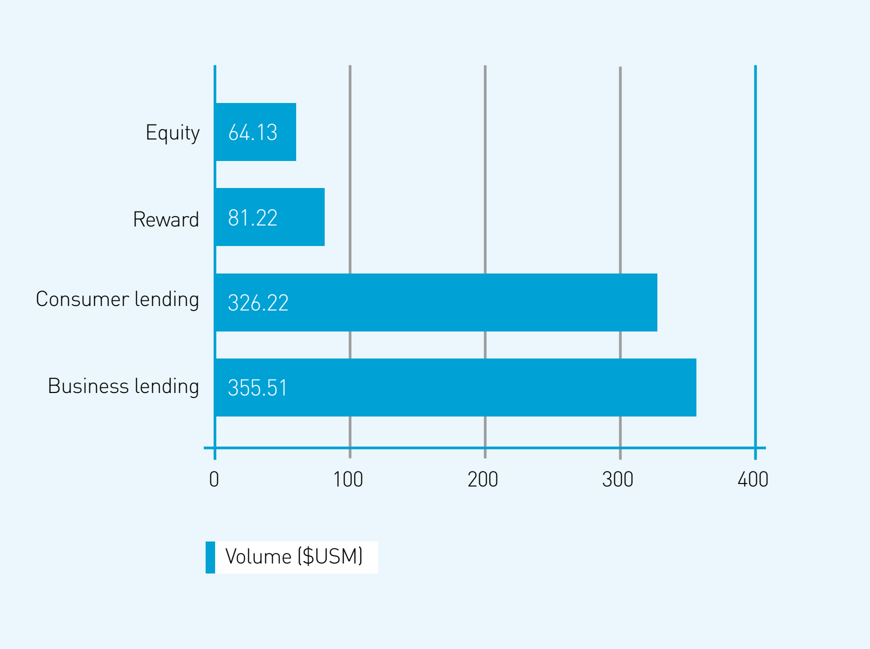
7 See, for example, Mollick, E., and Kuppuswamy, V. (2014). After the campaign: outcomes of crowdfunding. UNC Kenan-Flagler Research Paper No. 2376997. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2376997.

8 infoDev, Finance and Private Sector Development Department. (2013). Crowdfunding's Potential for the Developing World. Washington, DC: World Bank. http://www.infodev.org/infodev-files/wb_crowdfundingreport-v12.pdf

How to strengthen the eco-system in this area

- Support crowdfunding platforms that work in developing markets. Platforms need assistance and resources for:
  - Outreach and promotion;
  - Establishment of sound policies and practices;
  - Coaching and support for projects that have potential for high impact;
  - Activities to build a pipeline of projects and links with funding communities.
- Develop programs for matching grants, to support projects likely to have high social impact.

FIGURE 2: Market volumes by model in the Asia-Pacific (excluding China), 2015[9]



[9] Zhang, B., et al. (2016). Harnessing Potential. The Asia-Pacific Alternative Finance Benchmarking Report. Cambridge Centre for Alternative Finance. https://www.jbs.cam.ac.uk/fileadmin/user_upload/research/centres/alternative-finance/downloads/harnessing-potential.pdf

CASE STUDY: Cropital[10]

Platform category	Lending
Established	2014
Focus of fundraising	Smallhold farmers in the Philippines
Business model	> Lenders provide money to assist farmers through the farming cycle. Once the crop has been sold, lenders receive their capital plus a share of profit. > Lenders can choose a specific farmer to support, although they are encouraged to spread risk across several farmers. > Farmers are grouped into clusters and are managed by one local community partner. The local community partner visits the farms regularly and monitors the progress of each farmer against the farm plan they have submitted. > Selling of produce is coordinated by the local community partner and the farmer. The buyer is authorised by Cropital and pays directly through Cropital > Cropital's revenue source is not set out on the website but they do receive support from a number of partners.
Observations	> Cropital assists farmers with techniques to improve yield, with insurance and with links to buyers. > Cropital sends farm backers monthly updates about the status of the farms. This report will include the status, detailed progress and pictures of the farm > Cropital's website not only seeks support from investors but also calls for applications from people who are interested in becoming buyers or distributors of produce > The website also encourages people with ideas for improving farm profitability or introducing new technologies to contribute to the overall project
Sample campaign	Mario Walang's farm in Benguet produces carrots. The farm sought a loan of approximately $AU 1,800 dollars to enable them to continue farming. This amount was raised from 8 investors who will receive a 20% profit share when the crop is sold.

10 www.cropital.com (at November 2016)

CASE STUDY: Chuffed[11]

Platform category	Reward/pre-purchase/donation
Established	2013
Focus of fundraising	Socially conscious projects within one of the following categories: > Social Enterprise > Refugees and Asylum Seekers > Health and Disability > Community > Environment > International Development > Animal Welfare > Social Welfare
Business model	> Chuffed offers a 'keep what you raise' funding model > Chuffed does not deduct fees from campaigns. However, it offers donors the option of contributing money towards its costs
Observations	Chuffed is supported by the Telstra Foundation. In January 2016 it incorporated in Australia as a 'social benefit corporation' in order to raise equity and scale. This model is new to Australia but based on the US social benefit corporation.
Sample campaign	Cassava Project is seeking €5,000 to develop a sustainable weather station to provide better seasonal climate predictions and other early warnings to help Indonesian farmers better manage their crops. The campaign is offering the following perks: > Donation of €25 – personal thank you card (digital) with a picture of a local farmer > Donation of €50 - personal thank you card (digital and printed) with a picture of a local farmer plus a typical Indonesian Wayang bookmark In addition, a video will be made in Indonesia that will feature the names of all donors. All donors will receive a copy.

[11] www.chuffed.org (at November 2016)

Microfinance

Focus of the research

The modern microfinance industry has its roots in the 1970s when organizations such as the Grameen Bank of Bangladesh, with the microfinance pioneer Mohammad Yunus, began implementing innovative approaches to lending to the very poor. iXc was interested to understand whether it could work with this well-established industry but from a different perspective. The research investigated a specific question: could microfinance providers (and particularly those that operate through a network model) provide a pipeline of investable businesses that have the potential to scale beyond their immediate community?

Background to the issue

Microfinance has been growing rapidly over the last decade. It has been estimated that, from 2002 to 2013, the total loan portfolio of microfinance institutions (MFIs) in all developing countries increased from $US 4.95B to $US 144.70B.[12]

TABLE 3: MIX survey 2014: World portfolio of loans[13]

Region	Borrowers (N)	Annual growth (%)	Rural borrowers (%)	Portfolio size ($US B)	MFIs in survey (N)
Latin America and Caribbean	21.6M	14.2	29.9	40.6	349
Africa	5.3M	11.3	59.2	8.2	219
Middle East and North Africa	2.1M	8.3	43	1.2	31
Eastern Europe and Central Asia	3.5M	11.6	57.8	11.3	143
South Asia	64.1M	19.7	58.4	12.8	165
East Asia and Pacific	15.1M	7.6	80.2	12.9	138
Total	111.7M	14.2	57.3	87.1	1,045

While total portfolio size of MFIs can be very large, the loans disbursed are very small.

12 Donou-Adonsou, F., and Sylwester, K. (2016). Growth effects of banks and microfinance: Evidence from developing countries. The Quarterly Review of Economics and Finance. Article in press. Available online at: http://dx.doi.org?10.1016/j.qref.2016.11.001.

13 Convergences (2016). Microfinance Barometer 2016. http://www.convergences.org/wp-content/uploads/2016/09/BMF-EN-FINAL-2016-Version-web.pdf.

TABLE 4: Average microfinance loan size: December 2015[14]

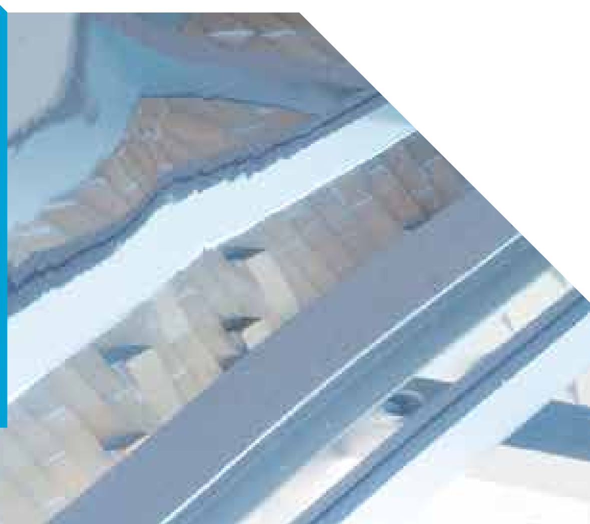
MFI	Country	Active Borrowers	Average Loan size ($ US)
ASA International	Bangladesh, Philippines, India, Pakistan, Nigeria, Ghana, Kenya and Uganda	1.38M	151
Bank Rakyat Indonesia	Indonesia	N/A (RBI has approx. 45% market share)	1,610
DAWN Microfinance	Myanmar	53,835	87
IFMR Holdings	India	265,693	228
Saija Finance	India	145,757	182
Swadhaar FinServ	India	243,842	175

The Asia-Pacific region is generally seen as having strong prospects for growth in the microfinance sector. The responsAbility Microfinance Market Outlook 2016 predicted a growth rate of around 30% in the region for 2016 compared to a global rate of 10-15%.[15]

14 https://www.accion.org/global-impact; http://www.asa-international.com/at-a-glance; The Asian Banker (2015). Bank Rakyat Indonesia wins Best Microfinance Business award for 2015. Press release. 19 March. http://www.asianbankerawards.com/retailfinancial/press/2015/Press%20Release%20-%20Bank%20Rakyat%20Indonesia%20wins%20Best%20Microfinance%20Business%20award%20for%202015-final.pdf

15 responsAbility (2015). Microfinance market outlook: Developments, forecasts, trends 2016. http://www.responsability.com/investing/data/docs/en/17813/Microfinance-Outlook-2016-EN.pdf.

> "A proportion of our micro-enterprises do grow. Less than 10% are superstars; about a third would grow; but two-thirds are people who ... are not looking to build big businesses – they just want to get out of debt and earn enough money to support their family and educate their children."
> Microfinance adviser



Insights and findings

There were no clear statistical findings – through either the literature or the consultation program – to indicate the volume of microfinance clients that had the potential to scale. Several stakeholders consulted for this research were of the view that microfinance will not provide a pipeline for investors as microfinance clients tend to be found in sectors where there is limited scope to scale. These enterprises are often small traders who may need capital to buy assets (such as chairs and tables for a food stall) but are not scalable businesses. Other sources were more optimistic, though, and in some cases estimated that 10-15% of enterprises that receive micro-loans have potential to scale.[16] One stakeholder cited the example of a microfinance client who was struggling to feed her family five years ago but has now won a significant business award for ready-to-wear garments and employs 27 people. Other organisations, such as World Vision and South Pacific Business Development, are working to develop the business skills of microfinance clients through training programs.[17]

Even if a very conservative, 2% estimate is taken, this still represents a large number of potential, investable businesses. Based on the 2014 MIX Survey, which estimated that there were 15.1 million microfinance clients in East Asia and the Pacific (see Table 3), this would still provide an investment pipeline of over 300,000 small businesses in the region.

A potential barrier to the microfinance industry supporting businesses to scale is that the practices of MFIs generally do not permit them to identify and tailor services for high potential microenterprises. Managing operating costs is a key consideration for MFIs, so the traditional MFI business model emphasises standardised products and group lending. However, our research has suggested several strategies that MFIs could adopt which would address the issue of operating costs while enabling the delivery of more targeted services. These include:

> Development of smart selection tools, that enable the MFI to undertake reliable business and credit assessments at low cost;[18]

> Vertical or sectoral specialisation so that MFIs can develop standard products tailored to particular areas of economic activity;[19]

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16 CGAP (2011). MFI Level Challenges to Serving Enterprises. http://www.cgap.org/data/mfi-level-challenges-serving-enterprises; Women's World Banking (2015). Individual Lending for Low-Income Women Entrepreneurs: An Inclusive Approach. http://www.womensworldbanking.org/publications/individual-lending-for-low-income-women-entrepreneurs-inclusive-approach/.

17 See South Pacific Business Development website: http://www.spbdmicrofinance.com/what-we-do/our-impact; World Vision website: http://www.wvi.org/sri-lanka/article/moo-moo-here-and-moo-moo-there.

18 Larson, G. (2012). Needles in the Haystack: How a New Tool is Unlocking Entrepreneurship in Africa. Kennedy School Review. http://harvardkennedyschoolreview.com/needles-in-the-haystack-how-a-new-tool-is-unlocking-entrepreneurship-in-africa/.

19 Women's World Banking (2015). Individual Lending for Low-Income Women Entrepreneurs: An Inclusive Approach. http://www.womensworldbanking.org/publications/individual-lending-for-low-income-women-entrepreneurs-inclusive-approach/.

TABLE 5: MFI networks

Model type	Features	Examples
Network of direct lending organisations	This is an MFI which provides loans to customers across multiple locations through a network of branches or affiliates. These networks deal directly with enterprises so will have some visibility of their activities.	> Bank Rakyat Indonesia > BRAC > FINCA > South Pacific Business Development
Network of investor organisations	These are investment funds, international NGOs or international development agencies which invest in, and provide business development assistance, to MFIs. These organisations tend to be closely involved in the activities of multiple MFIs so constitute networks at the level of the MFI. Their involvement can include sitting on the board of an MFI and/or providing business advisory services. They have limited visibility of enterprises.	> Accion > Opportunity International Australia > Triodos > Unitus Equity Fund
Industry organisations	These are industry or professional associations that operate across the microfinance sector. In some cases, these organisations are national, self-regulatory bodies; in other cases they operate globally and work to improve skills within the sector and/or to promote values of global inclusion.	> Microfinance Institutions Network (MFIN), an industry self-regulatory organisation in India > SEEP, a global organisation for the microfinance industry dedicated to promoting financial inclusion > The Microfinance Association, a global body for professionals working in the microfinance sector

Networks of investor organisations (Model 2) and industry organisations (Model 3) might be an appropriate and effective intervention point to introduce new business practices to MFIs and assist them to develop systems for identifying and supporting high potential microenterprises. At these levels, existing organisations are working to build capacity within MFIs by:

- Providing strategic and operational business advice and technical assistance;
- Investing in MFIs and providing general purpose loans;
- Undertaking research and sharing knowledge about effective business practices.

However, it is important to understand that there are differences in the structure of the microfinance industry across the Indo-Pacific, with varying approaches to regulation and delivery of microfinance. Any interventions designed for this industry will need to be sensitive to these differences.

> "Vertical specialisation is the key to working in the SME area. We need to understand specific client segments – better than we do at present – and build special products."
> Microfinance adviser

How to strengthen the eco-system in this area

- Support the design and development of:
  - Smart assessment tools that MFIs can use to improve their capacity to identify and provide loans for high potential microenterprises.
  - Specialised financial products, tailored to particular sectors.
- Promote collaboration between MFIs and entities such as incubators and accelerators.

Examples of MFIs in the Indo-Pacific

MFI	Location	Year launched	Details
1st Valley Bank[20]	Philippines	1956	The Company has its roots as the Rural Bank of Kapatagan Valley, Inc., a stock corporation founded in 1956. After its consolidation with the Rural Bank of Sinacaban in 2005, the Company became the 1st Valley Bank. As at 2015, the bank had 43 offices.
ASA International[21]	Bangladesh, Philippines, India, Pakistan, Nigeria, Ghana, Kenya and Uganda	1978	ASA commenced operations in Bangladesh and its operating model has spread to other developing nations. Across the group there are currently 1.38 million borrowers and a loan portfolio of $US 209M.
Bank Rakyat Indonesia[22]	Indonesia	1984	BRI is a commercial bank that started its microfinance business in 1984. BRI is the oldest bank in Indonesia and is 70% government-owned. BRI has 45% of the microfinance market.
BRAC[23]	Bangladesh	1972	BRAC is an international development organisation with programs across several areas including microfinance. It provides collateral-free micro-loans to mostly poor, landless, rural women, to enable them to generate income.
DAWN Microfinance[24]	Myanmar	2002	DAWN was founded by the Save the Children Fund in 2002 to support poor families around Yangon. It is now supported by a consortium of partners (Accion, Triodos and FMO).
ESAF Microfinance[25]	India	1995	ESAF Microfinance has a membership base of over one million and a network of 264 branches. In 2015, ESAF received approval from the Reserve Bank of India to operate as a Small Finance Bank.

20 http://1stvalleybank.com
21 http://www.asa-international.com
22 http://www.asianbankerawards.com/retailfinancial/press/2015/Press%20Release%20-%20Bank%20Rakyat%20Indonesia%20wins%20Best%20Microfinance%20Business%20award%20for%202015-final.pdf
23 http://www.brac.net
24 https://myanmar.savethechildren.net/our-consortiums/dawn-microfinance
25 http://emfil.org

ENABLING SERVICES

Enabling services are essential to the growth of social enterprises. Intermediaries build the business skills of entrepreneurs by providing training and mentoring and support the development of business models through the provision of technical advisory services such as legal, accounting and marketing services. Intermediaries also establish connections between investors and enterprises, and design and fund deals.

In this section of the report, we explore the role of a specific type of intermediary - incubators and accelerators – in the Indo-Pacific region, with a particular focus on programs designed for social enterprises.

"We are eager to increase this network or accreditation, that entrepreneurs can look back and say: is this accelerator worth my while? Particularly if I am going to give up 80% of my company, or 20% or 40%. I see a lot of entrepreneurs being saddled with really silly equity decisions and getting nothing from programs."

Manager of an incubator program

A regional network of incubators

Focus of the research

Early stage support for social enterprises has been identified as a gap in the market in the Indo-Pacific region.[26] iXc wanted to investigate this issue in more depth, to understand whether creation of a regional network of incubators could:

> Reach out to entrepreneurs and bring more new businesses into the (impact) investment eco-system;

> Improve the quality of early-stage business support services; and

> Help entrepreneurs to land the business/investment deals that will put them on the path to success.

Background to the issue

Incubators and accelerators are both programs aimed at very early stage or start-up businesses.

> An **incubator** is a central work space where a new business is physically located with many other start-up companies. In many cases, the start-ups are all venture funded by the same investor group and offered support to improve the commercial viability of the business from advice to shared services. Mentorship is typically provided by proven entrepreneurial investors, and by shared learnings of peers.

> An **accelerator** is similar to an incubator except that the entrepreneur is typically limited to an intensive three to four month mentorship program intended to jump-start a business. This method allows a venture capitalist to manage risk across a portfolio of companies by gaining exposure to a number of businesses for a limited cash and time investment. Although originally a concept of the venture community, accelerators are now found in other spheres such as for use in driving corporate innovation.

As part of this research, we developed a database of incubators and accelerators operating across the region. To date, this database has identified 39 programs operating in the Indo-Pacific and 55 in Australia.

While incubators and accelerators can be differentiated in theory, it is often difficult to clearly categorise programs in practice. For ease of reference, we have used the term 'incubator' in this report.

[26] Report prepared for iXc by Results for Development in 2016 (unpublished).

Insights and findings

Three principal challenges for entrepreneurs in the region were identified through the research:

- **Funding channels for early stage businesses are limited (the 'pioneer gap')**
  - Early stage entrepreneurs have difficulty obtaining seed funding ($25,000 to $250,000) and lack connections to potential investors.
- **There are not enough business training opportunities in the Indo-Pacific region**
  - The ASEAN Regional Entrepreneurship Report 2014/15[27] drew attention to this issue. It identified a gap in entrepreneurship in the region and recommended increasing the number of accelerators, incubators and coaching agencies.
  - Our consultation program revealed that:
    - More incubator programs are required;
    - Programs are needed in local languages as well as English;
    - In many countries, there is an absence of programs outside major cities.
- **Entrepreneurs are looking for opportunities to connect with their peers**
  - Entrepreneurs benefit from peer networks but peer networks tend to close when training and incubator programs come to an end. Supporting structured regional networks for entrepreneurs could contribute to the growth and development of their businesses.

High quality incubator programs can assist to meet these challenges and support the growth of businesses across the region. In this context, project participants identified a range of benefits that could flow from the establishment of a regional network of incubators, including:

- Providing a resource for newer programs;
- Sharing of experience among program managers;
- Access to investor lists;
- Shared costs for program activities;
- Sharing of mentors;
- Development of standards and quality benchmarks;
- Awards and accreditation as a guide for entrepreneurs when choosing a program.

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27 Xavier, S.R., Guelich, U., Kew, P., Nawangpalupi, C. and Velasco, A. (2015). ASEAN Regional Entrepreneurship Report 2014-2015. International Development Research Centre. https://www.idrc.ca/sites/default/files/sp/Images/Articles/gem-asean-regional-report-2014-2015.pdf

However, participants also cautioned that an incubator network has to be able to offer tangible benefits to encourage and retain members. These could include:

> Peer support (as between incubator managers);
> Incubator management tools and resources;
> Structured training programs;
> Measurement and evaluation tools;
> Fundraising support and funding opportunities.

There was a clear message from participants that a network that only offers 'light touch' networking opportunities will not meet the needs of the region.

An analysis of the database of incubators developed for this research identified three possible models for a regional incubator network.

Model type	Features	Examples
Network of program providers	This model only accepts intermediary organisations as members. It is similar to an industry association. The goal of this model is typically to share expertise and experience at the program level, and to support members to deliver high quality services.	> Aspen Network of Development Entrepreneurs (ANDE) > Global Social Entrepreneurship Network > InBIA
Information platform/forum	A connection point open to all members of the eco-system. It offers online directories and resources and may also convene in-person events. This model aims to facilitate connections across the eco-system.	> f6s.com > Sankalp Forum > Conveners.org
Replication of programs across sites	A defined incubator or accelerator program is rolled out across multiple sites. This can be implemented through a type of franchising arrangement or through a head office/branch structure. This enables programs to be established quickly at new sites as they draw on existing methodologies and resources.	> Founder Institute > Spark > Village Capital

How to strengthen the eco-system in this area

- Establish a network of incubators in the region which would support impact programs through activities such as:
  - Development of a regional training and education program, and a peer learning network, for incubator managers.
  - Development of an incubator performance and accreditation system for impact programs.
- Establish a funding stream with the capacity to:
  - Support impact incubators in the region through funding of operational costs or funding of specialist programs in priority areas;
  - Provide seed grants or small loans to entrepreneurs participating in incubator programs.

> "[A network] would really really help. When we first started there were so many questions...you just had to run it and learn from that. But there were quite a significant amount of things we did that could have been improved."
> Manager of an incubator program

CASE STUDY: Spark*[28]

Establishment	> Spark* is the impact arm of YGAP > Spark* has been operating since 2011. It has offices in Kenya, South Africa, Australia and Bangladesh. > The focus is on enterprises that improve the lives of people living in poverty.
Programs and services	> There are 12 participants selected for each Spark* entrepreneur support program > The programs cover three phases over 12 months: - Accelerate – a one week intensive program; - Support – 12 months of rapid support, including business mentoring, technical services and small grants; - Growth – 1 in 25 participants are selected for this phase. They receive intensive support to help them grow their model and have access to larger loans ($AU 25,000) and investor partners.
Business model	> Spark* operates with support from partners. > They also run their own companies in Australia that bring in revenue and enable Spark* to provide their programs without charge.
Outcomes	> Spark* selects two IRIS metrics for each participant to track against. > SInce 2011: - 267 entrepreneurs have come through programs; - 90% of entrepreneurs have doubled their impact and revenue; - These enterprises have improved the lives of 237,035 people.

CASE STUDY: iHub Kenya[29]

Establishment	Founded in 2010, iHub is a multi-use start up location for technology firms located in Nairobi.
Programs and services	> Co-working space. > Events to build skills and knowledge. > Networking events. > User experience lab. > Maker space.
Business model	> iHub was established with grants from donors. > It is now self-funding through: - Research services; - Consultation services (eg UX lab); - Membership fees; - Corporate partnerships.
Outcomes	> There are now approximately 17,000 iHub members. > The iHub neighbourhood has grown organically to become a place that technology companies choose to locate, thereby strengthening links within the ecosystem.

[28] http://www.sparkinternational.org/
[29] https://ihub.co.ke/about; interview with a representative of iHub Kenya.

MARKETPLACE

Given the nascent stage of the impact investing market, much of the market infrastructure that supports more mature sectors is yet to be built. This includes channels for connecting supply and demand, standards for impact measurement and shared knowledge of deals and opportunities.

This section looks at the role of social stock exchanges in providing this market infrastructure.

Social stock exchanges

Focus of the research

Drawing from the Senate Inquiry in 2015 on how to mobilise private sector capital into impact investing in the region, iXc was also interested in examining how platforms such as social stock exchanges could assist in connecting enterprises with impact investors.

Social stock exchanges are platforms that connect the supply and demand sides of the emerging impact investing market. While private placement platforms also exist to assist impact investors find deals, platforms such as those established in London and Toronto are more focused on catalysing market development.

Some of the initial findings from this project are set out here, as a social stock exchange could form an important part of the social entrepreneurship eco-system across the region, enabling private capital to be mobilised for development purposes.

Background to the issue

The impact investing market is at a nascent stage globally, with market participants often struggling to find one another, communicate or agree on measures of impact and return.

Platforms such as social stock exchanges are one mechanism that contributes to alleviating these difficulties in the early stages of this market. Although the label 'social stock exchange' is used, at this early stage these existing mechanisms are essentially platforms that connect supply and demand. It is a medium to longer-term market-building aim to provide secondary liquidity and trading as per mainstream stock exchanges.

Other mechanisms are private placement platforms and private funding networks, that work to identify impact investment opportunities, including Enable Impact, Tonnic and the recently established ImpactUS. There is also increasing attention from mainstream stock exchanges in this market development, such as the collaboration between the Stock Exchange of Mauritius and IIX Singapore, that may offer future opportunities for liquidity.

For social stock exchanges to generate deals (listings and interest of investors), much time, effort and funding is invested in enterprise education programs (getting them investor ready), investor meetings and education, and often providing high-touch, personal connections between listed enterprises and suitable impact investors, that then go on to interact via the platform.

Most platforms are nationally focused, and in order to transact online require approval from the appropriate national securities regulator or need to meet formal listing requirements.

Examples of platforms that have substantial and active membership listings include:

- **London (http://socialstockexchange.com)**
  - The Social Stock Exchange (SSX) is a public trading platform that was initially established as an information and advertising portal, providing consistent layers of impact measurement, promoting 'investor ready' social enterprises to enable capital raising with impact investors. It is a standalone for-profit entity.
  - It has successfully expanded with currently over 50 enterprise members, and a growing number of professional service firms that it certifies to work with members ('Social Company Advisers')
  - SSX is establishing a network of local offices (including in Liverpool and Edinburgh) to help with origination and deal flow
  - SSX's partnership with NEX Exchange in 2015 (formerly ISDX) provides the formal trading mechanism. NEX Exchange is a Recognised Investment Exchange under the UK Financial Services and Markets Act 2000
  - The London Social Stock Exchange recently executed a crowd funding campaign for its own business model as it expands and establishes a network of local offices across the UK
- **Toronto (http://www.svx.ca)**
  - Social Venture Connection (SVX) is an impact investment platform for impact ventures, funds and investors seeking social and/or environmental impact alongside the potential for financial return via debt and equity investments. SVX is the first North American impact investing portal and functions as a full-service intermediary for the local impact investing market.
  - SVX was developed by MaRS Discovery District with the support of the TMX Group Inc. and the Government of Ontario. Although it is a separately incorporated not-for-profit entity, MaRS Discovery District has been the institutional home for the SVX, providing a connection to highly motivated investors and entrepreneurs.
  - SVX is registered as an Exempt Market Dealer (EMD) with the Ontario Securities Commission (OSC), as well as regulators in Québec, BC, and Alberta, and complies with applicable securities legislation set by provincial regulators. Accredited investors (as defined and approved by the OSC) and retail investors can access SVX.
  - SVX has partner platforms in the United States and Mexico, and is exploring partnerships to facilitate more investment activity in other regions.

Insights and findings

Existing platforms all operate using different business models, with revenue drawn from transaction fees, membership fees, impact assessments and some support services.

Existing platforms use different impact measures for enterprises wishing to list, including social return on investment (SROI), B Corporation certification and other proprietary methods.

Significantly, most platforms rely on donor/philanthropic/government activity to develop deal flow through educational events and training for both enterprises and investors. These activities are essential in supporting the platform in these early stages.

These platforms are very successful in providing tangible and intangible market infrastructure for impact investing, providing a necessary role in coordinating and convening actors, matching supply and demand, and establishing norms and understandings around returns and liquidity.

How to strengthen the eco-system in this area

> Build an understanding of the existing key brokers in the region, their business models, reach and specialisation (country or focus).

> Consider how existing platforms could be translated into a regional context, within the constraints of national regulatory systems.

> In addition to any technology platform solution, consider traditional financing for necessary offline capacity building of both enterprises and education of investors.

CAPITAL

In the social entrepreneurship value chain, capital is the final, critical component. Social enterprises need access to appropriate capital, including from impact investment funds, to enable them to scale. This section explores a relatively new financial tool – blended capital – and considers how it might be used to support social enterprises within the Indo-Pacific region. Within this section, we also report our findings on the role of pay by results funding mechanisms.

Blended finance

Focus of the research

This phase of the project sought to understand the effectiveness of various types of blended finance deals and investment stacks being used in impact investing in relation to their ability to leverage private capital and make capital more available to entrepreneurs in the 'pioneer gap'. This directly related to iXc's interest in identifying new sources of investment finance to support the growth of businesses in the Indo-Pacific region.

Background to the issue

Blended finance is a relatively new type of investment activity. It involves the strategic use of development finance and philanthropic resources to mobilise private capital so as to deliver risk-adjusted returns on investments while also ensuring significant development outcomes. Interest in blended finance as a vehicle for international development has intensified following the establishment of the UN's Sustainable Development Goals (SDGs) in 2015.

The basic blended finance instruments are set out below.

TABLE 6: Blended finance instruments used to leverage private capital[30]

Instrument	Description
Grants	A financial award provided for the express purpose of covering a set amount of first-loss. There is no expected repayment or compensation.
Guarantees	Protection against capital losses for investors due to commercial and political risks. A guarantee will cover a set amount of loss.
Debt	Money lent for repayment at a later date, usually with interest. > Market Rate Debt, when rates and terms are determined based on capital markets prices and tenors, but can be subordinate to senior debt (i.e. mezzanine) > Flexible (Concessional) Debt, with favourable terms or rates for the borrower relative to market pricing.
Equity	Ownership in a company, with value determined at time of investment. By taking the most junior equity position in the overall capital structure, the provider takes first losses (but perhaps also seeks risk-adjusted returns); this includes common equity in structures that include preferred equity classes.

As blended finance is a relatively recent addition to the field of development finance, there is only limited data available on the volume of deals being closed across the world. In 2016, the OECD and World Economic Forum published the results of a survey of 74 blended finance funds and facilities. This showed that:

- The 74 funds and facilities within the survey accounted for $US 25.4B in assets.
- Looking at those funds and facilities that are region-specific (as opposed to global), there were capital commitments of $US 2B within the **East and South-East Asia and South Asia regions**, across 10 funds. This represented 22% of all region-specific investments and 8% of all funds committed globally.[31]

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30 OECD/WEF (2015). Blended finance Vol. 1: A primer for development finance and philanthropic funders. OECD, Paris and World Economic Forum, Geneva; GIIN (2013). Catalytic First-Loss Capital. Global Impact Investing Network. https://thegiin.org/assets/documents/pub/CatalyticFirstLossCapital.pdf.

31 OECD/WEF (2016). Insights from Blended Finance Investment Vehicles & Facilities. OECD, Paris and World Economic Forum, Geneva.

Insights and findings

While there is substantial global interest in blended finance, particularly since the establishment of the SDGs, blended finance is an evolving approach and published evaluations of deals are limited. Available evidence from several case studies shows that public investment can catalyse private sector investment. However, there is no definitive view on the most effective way to structure these deals.

- **Guarantees** have been shown to be effective in mobilising private sector investment and these can be deployed at low cost to government.
- Public agencies can manage risks associated with early-stage investments by providing **technical assistance** to investees to support their success.
- There are also several existing deals which show that the level of public sector investment (through guarantees, subordinated debt or equity) need not be high: the involvement of a public agency on its own can be sufficient to provide credibility for a deal.
- Creating a layer of **first-loss capital** has also been a successful strategy for mitigating risk and leveraging private sector investment. However, there are currently no benchmarks or guidelines to assist development agencies to determine the appropriate level of concessional capital. Processes need to be put in place to understand the appropriate level of risk reduction and avoid providing an excessive subsidy to private investors.

But blended finance deals are currently limited by the cost and length of time involved in establishing deals. As an indication:

- The African Agricultural Capital Fund ($US 25M deal) took 12 months to structure at a cost of $US 300,000; and
- The Global Health Investment Fund ($US 55M deal) took 18 months to structure at a cost of $US 1M.[32]

Prima facie, this limits the use of blended finance as an instrument for bridging the 'pioneer gap' and providing funding for early-stage enterprises: the amounts required by these enterprises are generally too small to justify the creation of a blended finance deal. However, in some areas this hurdle is being overcome through the creation of investment funds which then on-lend to small and medium enterprises. In future, blended finance deals might be available for direct investment in smaller firms if deal structures can be standardised and made scalable.

"Guarantees can be a really powerful option where the amount of capital required is reasonably heavy and the risk isn't overly strong."
Impact investment adviser

32 UK Cabinet Office (2013). Achieving social impact at scale: Case studies of seven pioneering co-mingling social investment funds. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/193697/2900897_HMGCO_Co-mingling_acc.pdf.

How to strengthen the eco-system in this area

- Support the development of:
  - Standardised and scalable blended finance products;
  - Standard metrics to measure the effectiveness and performance of blended finance deals.
- Build an understanding of blended finance within both the public sector and private sector. Blended finance is at an early stage of development and calls for new types of skills and expertise.

CASE STUDY: Sarona Frontier Markets Fund 2[33]

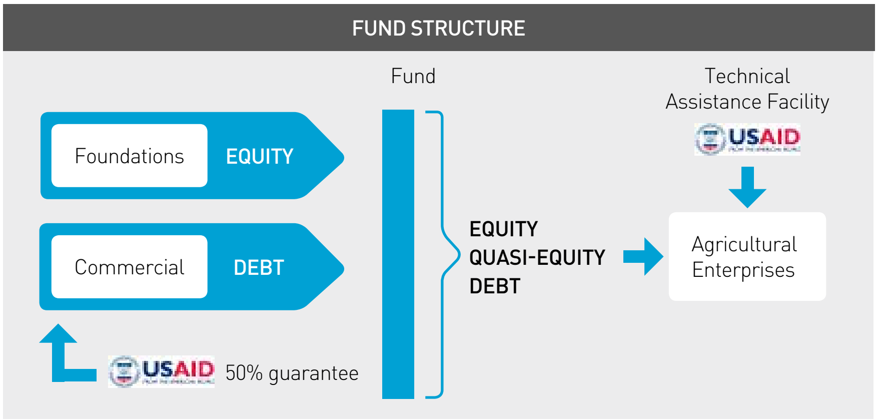
Establishment	2014
Development focus	> Sarona Frontier Markets Fund 2 (SFMF2) is a 'fund of funds' that invests in frontier and emerging markets private equity funds, which in turn invest in small and medium enterprises. SFMF2 targets strong financial returns for investors and positive ethical, social and environmental outcomes for investees. > To date, investments have been made in funds that invest across 20 countries, including Peru, Ecuador, Nigeria, Egypt, Vietnam and Indonesia.
Deal size	$US 150M
Deal partners	**Anchor partners** > OPIC > DFATD **Other investors** > There are 117 private sector investors, including individuals, corporations, foundations, non-profits, pension funds and endowments. **Fund manager** > Sarona Asset Management
Deal structure	> The most senior layer in the fund is a debt layer of $US 50M contributed by OPIC. > The senior equity layer in the fund amounts to $US 85M and has been contributed by a range of investors, as noted above. > The junior equity layer (first-loss capital) is $US 15M contributed by DFATD, now Global Affairs Canada. The layer is charged organisational costs, management fees and fund expenses in proportion to other investors but does not accrue gains or profits.

33 Convergence (2016) Case Study: Sarona Frontier Markets Fund 2. https://convergence.finance/knowledge-detail/5v2MUKquHYuoI2u6GG0wow

CASE STUDY: Crossboundary Energy[34]

Establishment	2015
Development focus	> On-site solar generation for commercial and industrial businesses in Sub-Saharan Africa. > CBE finances the construction, operations and maintenance of solar projects, and is repaid through the sale of electricity to businesses or through lease arrangements.
Deal size	Up to $US 30M
Deal partners	> USAID > Private investors, primarily impact-oriented family offices such as the Blue Haven Institute, Treehouse Investments and Ceniarth. > Manager of the fund is CrossBoundary Energy
Deal structure	> Class A equity ($US 7.5M) is the senior tier in the fund. This is owned by private investors and CrossBoundary management. > Class B equity ($US 1.3M) is the junior tier, subject to first losses. This has been contributed by USAID. > CBE invests its equity through special purpose vehicles (SPVs) that can also raise debt to increase total capital available to the project. It is expected that the SPVs will raise approx. $US 20M debt.

FIGURE 3: Structure of the African Agricultural Capital Fund[35]



"Organisations where they have blended deals are very high impact. But the deals are hard to put together and take a lot of time. There are so many cooks in the kitchen."
Impact investment adviser

34 Convergence (2016) Case Study: CrossBoundary Energy. https://convergence.finance/knowledge-detail/3nqBaWj2PKES22swss2KeS

35 UK Cabinet Office (2013). Achieving social impact at scale: Case studies of seven pioneering co-mingling social investment funds. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/193697/2900897_HMGCO_Co-mingling_acc.pdf

Pay by results

Focus of the research

In this phase of the research, we explored whether 'pay by results' or success-based payments could provide a mechanism to stimulate impact investing in a development context. Our research reviewed the status of this approach in the global development market. In this phase of the research program, iXc was also interested to explore the role of social procurement.

Background to the issue

Pay by results

In traditional aid interventions, development funding is directed to financing specific inputs to aid activities: for example, purchasing medical equipment to improve the health of a population. Results-based approaches differ significantly in that the implementing organisations need to deliver the required results before funds are disbursed to them. Under these interventions:

> The focus is on the outcomes to be achieved rather than the activities undertaken; and

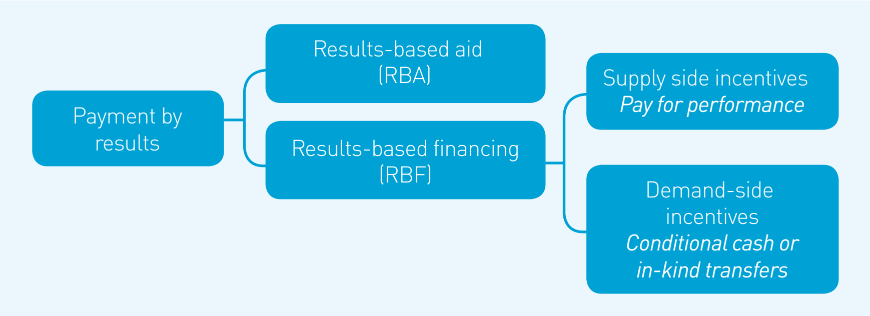
> Risk of delivery is transferred to the implementing organisation.

In the literature, pay by results (PBR) mechanisms are categorised according to who **receives** the payments:

> PBR mechanisms targeting national governments are often labelled **'results-based aid' (RBA)**;

> Mechanisms targeting sub-national service providers or individuals are called **'results-based financing' (RBF)**.

FIGURE 4: Results-based payments[36]



[36] Helland, J. and Maestad, O. (2015). Experiences with Results-Based Payments in Norwegian Development Aid. Norwegian Agency for Development Cooperation. . https://www.norad.no/en/toolspublications/publications/2015/experiences-with-results-based-payments-in-norwegian-development-aid/.

Some writers add a further category to this listing: challenge-linked financing. This category comprises awards and prizes and includes funds that offer rewards for solutions to development problems.[37] Examples include the Grand Challenge programs, the Small Medium Enterprise Innovation Trust Fund and iXc's Blue Economy Aquaculture Challenge.

The 2016 Annual Report for the Global Partnership on Output-Based Aid (GPOBA), a program in the World Bank Group, provides an indication of the size and distribution of this market. As at June 2016:

> GPOBA's cumulative subsidy portfolio consisted of 46 grant agreements in seven sectors, totalling $US 234 million;

> In FY16:

- Energy remained the largest sector in the portfolio at 44%; and
- Water the second largest sector at 24%;

> Sub-Saharan Africa has the highest percentage of GPOBA funding by region, at 52%, followed by:

- South Asia at 20%; and
- East Asia at 12%.

Social procurement

Social procurement, in the aid context, is a strategy for maximising the effectiveness of aid disbursements by ensuring that, wherever possible, the goods and services required for aid projects are purchased in aid recipient countries. The logic of this approach is that the aid dollar could 'go further' if businesses in recipient countries were given the opportunity to tender for contracts to supply goods and services related to aid projects.

Insights and findings

Pay by results

While PBR is a relatively new approach to aid, there has been discussion and analysis of its strengths and limitations. The table below summarises these arguments.

[37] Bhushan, A. and Calleja, R. (2015). Paying for Impact: Results-based Approaches in Development Finance, Situating Canada's Efforts in a Global Context. Canadian International Development Platform. http://cidpnsi.ca/wp-content/uploads/2015/05/ResearchReport_PayingforImpact_v21.pdf.

TABLE 7: Benefits and limitations of results-based approaches[38]

Benefits	Limitations
Linking payments to results encourages recipients to improve efforts to achieve targets due to their need for funding.	RBA assumes that partner countries political systems are open to incentives to achieve better outcomes. However, in some cases, pre-existing governance capacity may be too low for recipients to actively lead implementation.
Program risk is shifted to implementing agencies rather than being borne by taxpayers in the donor country (in the case of official development assistance) or by donor organisations. This encourages implementing agencies to undertake more thorough risk assessments before proposing projects to donors.	PBR may prioritise projects with easy to measure outputs over more systemic and harder to measure reforms.
Measuring results shifts the focus of policy makers and aid organisations to outcomes, rather than limiting their focus to inputs.	The costs of measuring and verifying results can be so high as to outweigh any benefits when compared to traditional grant funding
With its emphasis on outcomes rather than inputs, PBR allows for much more precise targeting of aid projects to specific communities or populations.	PBR cannot be implemented equally well in all contexts. For some programs, outcomes are not easily measureable.
In the case of RBA, there is strengthened ownership on the part of partner governments: the task of achieving goals lies with the partner government rather than with the donor organisation. This can strengthen accountability to local populations.	There is a danger of setting adverse incentives or encouraging people to game the system. The pressure to achieve certain goals can lead to the neglect of other priorities in the same sector.
PBR increases recipient discretion over spending so creates opportunities for adaptation and learning, thereby increasing capacity.	Development partners can be forced to pay partner governments for results, even in the face of governance problems such as serious human rights abuses. Results-based aid is not an instrument for expanding opportunities for policy dialogue.
	PBR can create a short-term perspective, because it might cause a focus on results that can be achieved quickly.
	Aid disbursements are not tied to specific activities or procurement procedures, only to outcomes. This raises the possibility of fiduciary risk.
	Aid may be withdrawn if results are not achieved. This has implications for developing countries that rely on continued and relatively stable levels of aid funding.
	Project goals might be set that are unambitious, because partner countries and donor agencies would prefer to disburse aid funding.

[38] Barder, O. and Talbot. T. (2015). Guarantees, Subsidies, or Paying for Success? Choosing the Right Instrument to Catalyze Private Investment in Developing Countries. CGD Working Paper 402. Washington, DC: Center for Global Development. http://www.cgdev.org/publication/guarantees-subsidies-or-paying-success-choosing-rightinstrument-catalyze-private; Bhushan, A. and Calleja, R. (2015). Paying for Impact: Results-based Approaches in Development Finance, Situating Canada's Efforts in a Global Context. Canadian International Development Platform. http://cidpnsi.ca/wp-content/uploads/2015/05/ResearchReport_PayingforImpact_v21.pdf; Klingebiel, S. and Janus, H. (2014) Results-Based Aid: Potential and Limits of an Innovative Modality in Development Cooperation. International Development Policy. 5.2. http://poldev.revues.orgbcrfj.revues.org/1746; Perakis, R., and Savedoff, W. (2015). Does results-based aid change anything? Pecuniary interests, attention, accountability and discretion in four case studies. Centre for Global Development. http://www.cgdev.org/sites/default/files/CGD-Policy-Paper-52-Perakis-Savedoff-Does-Results-Based-Aid-Change-Anything.pdf.

While there is only limited evaluation data available, it would seem that PBR is best suited to projects with the following features:

> It is easy to identify development results;

> These results are measureable;

> Data and baseline information is often available or easy to collect; and

> Intense disputes between the different parties around the definition of results, the indicators, the applied methods and data are not expected.

Projects that are **not** suitable for PBR approaches would include:

> Projects that require a significant investment of upfront capital;

> Projects with a long timeframe, where actual outcomes will not be produced for several decades;

> Projects where there is insufficient capacity on the part of the recipient government or service provider.

Social procurement

It has been estimated that, of the overall aid spend in 2010 of $US 129B, over 53% ($US 69B) related to procurement.[39] This is a significant funding pool available to be spent with enterprises in developing economies.

However, to increase the level of purchasing from aid recipient countries will require work to be packaged in a way that suits local markets and the capacities of local businesses. Another approach is to use in-country procurement systems for the tendering of goods and services.

How to strengthen the eco-system in this area

> Test and refine results-based approaches by:

  - Piloting results-based finance projects in sectors such as health and sanitation where results are more readily measureable;

  - Creating pay by results components within larger aid programs, to introduce a hybrid approach to aid funding.

> Support the design and implementation of cost-effective approaches to measuring and verifying the outcomes of results-based aid projects.

[39] Ellmers, B. (2011). How to spend it: Smart procurement for more effective aid. Eurodad. file:///C:/Users/130239/Dropbox/DFAT%20iXc/Previous%20reports/Payment%20by%20results/Social%20procurement/eurodad-how_to_spend_it.pdf.

CASE STUDY: SWIFT Consortium for Sustainable Water, Sanitation and Hygiene in Fragile Contexts[40]

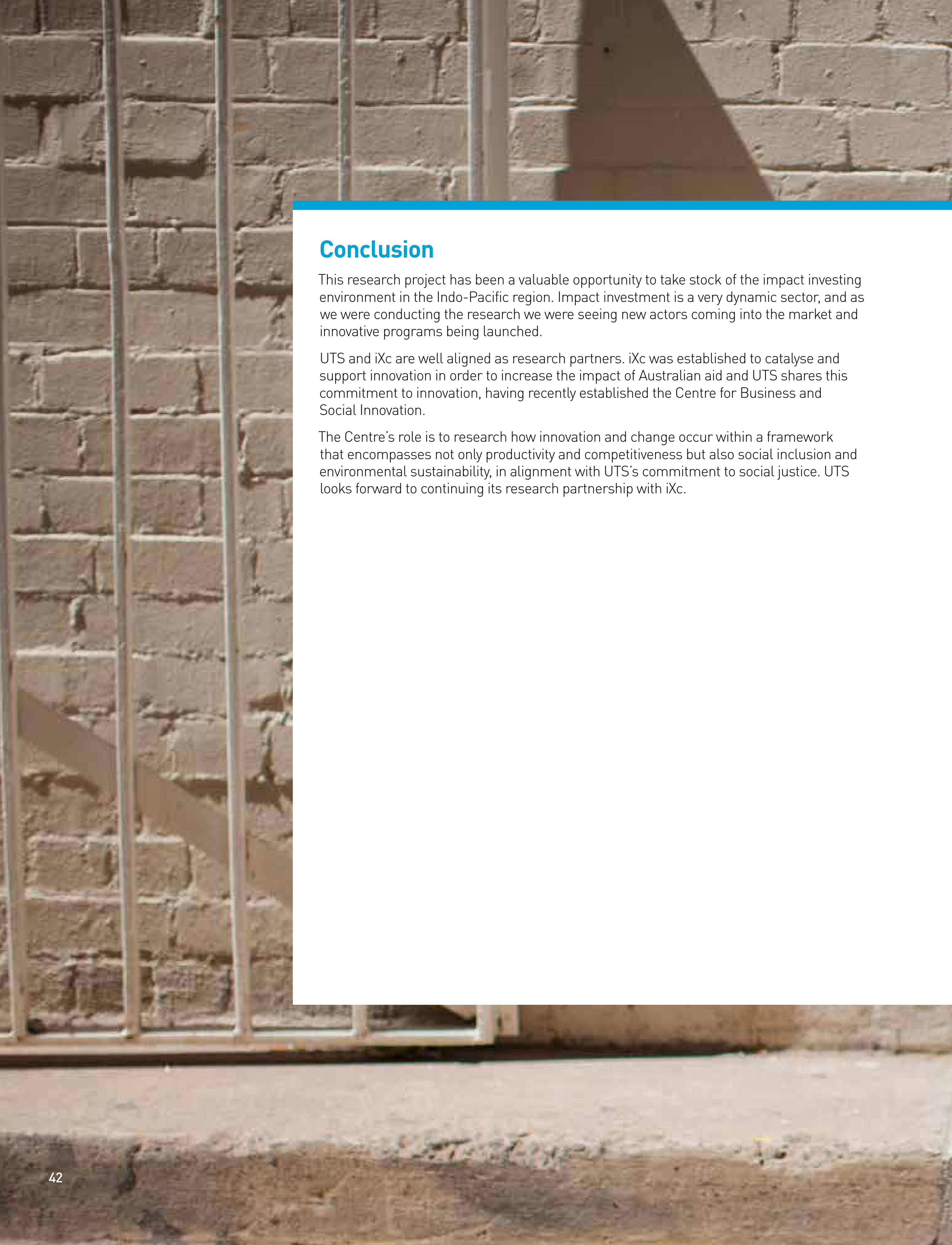
Establishment	2014
Overview	Since 2014, the SWIFT Consortium has provided access to water and sanitation and encouraged the adoption of basic hygiene practices in the Democratic Republic of Congo and Kenya.
Structure	The consortium is led by Oxfam and includes global members Tearfund and ODI, and global associate Water and Sanitation for the Urban Poor (WSUP). The SWIFT Consortium is funded with UK aid under a 'Payment by Results' contract.
Outcomes	It reached nearly 850,000 people with at least two of the three services (hygiene, sanitation, water) by the end of March 2016, which triggered payment by the UK Department for International Development. Results must also be sustainable if SWIFT is to receive payment in full. The consortium has two years to follow up activities and continue to engage with communities and local government. Checks will be carried out in 2017 and 2018.

CASE STUDY: (Proposed) Development Impact Bond for Syrian Refugees[41]

Establishment	In design stage with funding from Convergence. The bond could be ready for deployment from January 2018.
Overview	KOIS Invest is looking to create a $US 20-50M development impact bond that will fund a program to provide Syrian refugees with vocational training and other career skills in countries such as Lebanon, Jordan and Turkey.
Structure	The proposed structure is for private investors to pay the up-front costs of a project and donors to the project (usually governments) will provide reimbursement to the bondholders if the program's objectives are achieved.
Performance	If the objectives of the bond are met, it is anticipated that investors will receive a return of 9-10%.

40 Feeny, E. (2014). Implementing WASH programmes in a Payment by Results context. SWIFT Consortium Learning Brief. http://swiftconsortium.org/resources/

41 Rumney, E. (2016). First multi-country development impact bond targets Syrian refugees. Public Finance International News, 3 October. www.publicfinanceinternational.org/news/2016/10/first-multi-country-development-impact-bond-targets-syrian-refugees; Wagner, S. (2016). Impact Bond Targets Employment for Syrian Refugees. Bloomberg Briefs. 20 October.



Conclusion

This research project has been a valuable opportunity to take stock of the impact investing environment in the Indo-Pacific region. Impact investment is a very dynamic sector, and as we were conducting the research we were seeing new actors coming into the market and innovative programs being launched.

UTS and iXc are well aligned as research partners. iXc was established to catalyse and support innovation in order to increase the impact of Australian aid and UTS shares this commitment to innovation, having recently established the Centre for Business and Social Innovation.

The Centre's role is to research how innovation and change occur within a framework that encompasses not only productivity and competitiveness but also social inclusion and environmental sustainability, in alignment with UTS's commitment to social justice. UTS looks forward to continuing its research partnership with iXc.

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