ADRIENNE ARSHT
LATIN AMERICA CENTER

Harnessing Social Impact Investing in Latin America:

Private Capital for the Public Good

By Gabriel Sánchez Zinny

Atlantic Council

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Foreword

The core of our mission at the Atlantic Council's Adrienne Arsht Latin America Center is to show that Latin America is no longer about the subjects that tend to dominate policy discussions about the region: transnational crime, terrorism, corruption, violence, and drugs. Rather, Latin America is about game changing, global trends. Social impact investment and entrepreneurship is one of these areas. Business leaders and policymakers are at the forefront of working to make financially sound investments to transform their societies' ability to confront important social challenges, such as opening access to education, improving health care, and reducing inequality.

Social impact investing offers alternatives to the policy community that shift development away from traditional, often unsustainable models. Development assistance to Latin America from wealthy countries is at a historical low, while government support for domestic social programs is in jeopardy in many countries because of falling economic growth rates and political constraints. But where governments hit roadblocks, the private sector can step in to make important quality-of-life changes for millions of people, with innovations ranging from pay-as-you-go solar power to fresh farming practices.

Supporting these social innovators is important. They can help citizens and create jobs while generating profits at the same time. But these innovators also have the potential to spur systematic change.

In Latin America, social impact investment holds great promise. Over the past decade, innovative government programs lifted millions out of poverty and into the middle class. These programs are slowing down at the very moment that a new, burgeoning middle class is demanding higher quality services. This is where the private sector can offer a unique solution: integrating private capital with public good through targeted impact investments.

Though social enterprise is driven by the private sector, policymakers also have an essential role to play. Supportive regulatory frameworks that foster competitiveness while also developing tomorrow's entrepreneurs are tasks that require enlightened federal and local government action. Governments can also act as important risk-bearers, supporting promising, early-stage initiatives through training and catalytic capital.

Important players extend far beyond the typical public- and private-sector actors. Multilateral agencies such as the Inter-American Development Bank and the World Bank support social entrepreneurs by providing seed funding when no one else will take a chance. Many philanthropic organizations allocate a portion of grants to support for-profit models that contain social development goals. They are also establishing much-needed networks to connect diverse stakeholders.

Latin America is a vastly different region from a decade ago. Societies are largely rising to respond to the new, more sophisticated demands that come along with more prosperous societies. But governments increasingly don't have all the answers. Social impact investing offers some of the best hope for addressing what's needed for the next stage of development, with governments approaching it in different ways. Some openly embrace the private-sector-for-social-good model as a national priority while others take a more local, incubator-focused approached.

This publication provides a snapshot of how successful models are working, and also offers much-needed recommendations of how to build on the region's early successes. Policymakers and business leaders should take heed of what more needs to be done so momentum is not lost.

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Executive Summary

Social impact investing is on the upswing. Already an established practice of many US-based investment funds, the use of private capital for public good is quickly gaining momentum across developing countries.

The increase in global volume is impressive. By 2020, global impact investments are expected to reach $500 billion, with $120 billion of investments originating in the United States.[1] And while North America and Western Europe are the home bases for much of this activity, more than 70 percent of current investments flowing from the developed world end up in emerging markets.[2]

Latin America is quickly becoming a top destination for investment; still, regional economies struggle to generate domestic social impact investments. While only 4 percent of global impact investors are based in the region, a full 19 percent—and growing—of total global social impact funds are put to work in Latin America.[3]

Why Social Impact Investment Matters for Latin America

Despite Latin America's robust growth over the past decade—and the investments in conditional cash transfer programs—4.6 percent of people live on less than $1.25 a day, making it the world's most economically unequal region. Low levels of productivity, struggles with competitiveness, and educational systems that inadequately prepare Latin American youth for today's labor market threaten to stagnate, or even reverse, the gains made in the past few years.[4]

Reaching the next level of development requires greater competitiveness. But accomplishing this means increasing productivity, boosting innovation, bolstering investment in research, and developing human capital.

Here, social impact investment plays a unique role. As David Brooks wrote in the *New York Times*, "Impact investing is not going to replace government or be a panacea, but it's one of a number of new tools to address social problems."[5] Governments are increasing expenditures in social progress but finding it difficult to implement sustainable, impactful policies.

Social impact investors and entrepreneurs are uniquely positioned to complement public investments through innovations that reduce poverty, protect the environment, and improve healthcare and education. This could bring much-needed capital into the region, with the corresponding ideas that trigger a new wave of competitiveness. For both the public and private sector, social innovators can also help to unleash new products, processes, and technologies—all critically important for a region with low innovation rates.

Laying the Groundwork for Latin America's Social Innovation Sector

This publication provides a roadmap for understanding the state of impact investing in Latin America with recommendations of what more needs to be done to boost the sector's growth. Governments, for example, must have clear rules of the game to attract investment. While civil society and multilateral institutions should be even better conduits for sharing what models work and what have failed. And additional incentives should be put forward to generate public-private partnerships.

Beyond the typical private or public sector actors, this publication also explores the role of multilateral agencies in creating social impact. Credit granting organizations such as the Multilateral Investment Fund have found ways to support social entrepreneurs when neither the private sector nor governments would take the risk to provide seed funding. These organizations have helped to define the framework for impact investing, connect first-time investors with first-time entrepreneurs, and establish networks to support entrepreneurs. What are the lessons learned, an what may be the future trends?

Why Latin America?

A number of factors are motivating social impact investors to increasingly invest in developing markets. As of 2013, 19 percent of impact investments were directed toward firms and organizations in Latin America and the Caribbean. Though Sub-Saharan Africa remains the most popular destination for impact investments, Latin American investments and regional-based funds are both quickly accelerating.[6]

Young and Upwardly Mobile

One reason for this shift is the unprecedented growth of the region's middle class, with more than seventy million new entrants since 2000. This has opened up new market opportunities with increased demand for better services.

While the rise of a more robust middle class is a welcome development, it also puts additional pressure on governments to perform at a higher level. New middle-class citizens can afford—and have come to expect—access to a greater range and quality of social services, from education and housing to healthcare.

Yet improvements in the quality of state services have, for the most part, failed to keep pace with the rate of economic expansion. For example, though the vast majority of young people in Latin America have access to education, curriculums often inadequately prepare students to enter the existing job market. In education and other areas, increasingly frustrated citizens are turning to nonstate solutions. These solutions include services by the private sector or by the steadily growing number of philanthropic foundations, multilateral projects, and nongovernmental organizations (NGOs).

> **The rise of a more robust middle class puts additional pressure on governments to perform at a higher level.**

Latin America's youth bulge makes finding sustainable solutions even more important. Twenty percent of the population is between fifteen and twenty-four years old. Many of these young people are better educated than previous generations.[7] This means they use less state services but also have higher expectations of what the state should deliver. But a larger number of youth, known as "NiNis" (neither employed nor in school), have few opportunities for economic advancement in the formal labor market. Impact investing can provide new avenues for education, training, and employment.

Technology is a primary driver for the region's youth having a largely nontraditional attitude toward public service. They grew up as "digital natives" in a region where Internet penetration rates are growing fast and are expected to surpass 54 percent by 2015.[8] Regionwide, millennials and post millennials account for an estimated 32 percent of total Internet users, 6 percentage points higher than the global average.[9] They exhibit a strong entrepreneurial spirit, a deep concern for social good, and are positioned for success given the right resources and support.

These youth do not necessarily look to the state for answers. Instead, they try to solve problems on their own or in collaboration with their tech-savvy and socially engaged peers. For these innovators, the chance to make an impact on their communities is as important as the prospect of financial success. This creates a new class of entrepreneurs ripe for social impact investment.

A Team Sport: Catalyzing Social Impact

Government remains a key part of the equation. In many cases, social impact investing has taken root in response to a

lapse in government capacity, whether in terms of building schools, providing housing, or ensuring clean water. Social investors can and do help to compensate for these gaps, but governments remain critical partners for impact investors. Only the public sector can provide the enabling regulatory framework necessary for private capital to support new ventures and scale-up successful projects.

Governments are often incapable of taking direct investment risks, but they can create the foundation for innovation by developing startup accelerators or business incubators that seek out impactful enterprises. National and local governments in Argentina, Brazil, Chile, Colombia, and Mexico have all begun implementing models to kickstart social enterprise.

The case studies that follow highlight efforts in Buenos Aires, Argentina, which created two distinct incubators—one of which is tech-focused—to enable the city's socially minded entrepreneurs to learn and create new companies. Likewise, Brazil's federal government recently created Start-Up Brazil (similar to the internationally acclaimed Start-Up Chile program) to both attract tech entrepreneurs to Brazil and enable young entrepreneurs at home to start their own companies.

Another important government role is investment in core infrastructure, such as broadband Internet. High-speed Internet is crucial for entrepreneurs' success; it enables them to pursue source funding and share best practices and information with other entrepreneurs. Governments can also issue "social impact bonds" that use public authority to raise private funding for social projects.

With or without this initial "push" on the part of governments, the private sector remains the driving force behind these investments.

Many firms, under the motto of "doing good while doing well," are already investing successfully. These include both for-profit entities such as JPMorgan Chase & Co. and nonprofits like the Calvert Foundation, which is trying to align its endowment with a social mission. What JPMorgan labels as "socially responsible investment assets" have increased exponentially, with the global market expanding from $639 billion in 1995 to $2.7 trillion by 2007—and continuing to rise.[10] In the United States alone, sustainable, responsible and impact investing (SRI) reached $6.6 trillion at the start of 2014, a 76 percent increase from 2012.[11]

The Calvert Foundation speaks of "aligning values with profits" and has turned its endowment into a portfolio of affordable loans to nonprofit organizations and social enterprises in the areas of affordable housing, microfinance, and agriculture. It has invested more than $1 billion in 240 local community development financial institutions.[12] The W.K. Kellogg Foundation has directed a major slice of its endowment—$100 million since 2007—into "mission-driven" private-sector investments.[13] Numerous other foundations are following their lead.

The US government has also sought to bolster this growing market, paralleling initiatives by Latin American and European governments. It contributes funding directly through Overseas Private Investment Corporation (OPIC) investments and the domestic Community Development Financial Institutions Fund. The Obama administration has also created a National Advisory Board on Impact Investing in an attempt to catalyze investors.

Latin American efforts in this direction have the

High-speed Internet enables entrepreneurs to pursue source funding and share best practices with others.

The Calvert Foundation has invested more than $1 billion in 240 local community development financial institutions.

opportunity to both draw on the success of the US impact investing model as well as push the envelope on how the public and private sectors can work together to address diverse social challenges. With over 3 percent of the working population in Latin America reportedly engaged in social entrepreneurship, the timing is right to build on the number of "social entrepreneurs" who conceive, launch, and manage social impact projects.[14]

While the Latin American social entrepreneurship market has not yet reached the size of its US counterpart (3 percent versus 5 percent social entrepreneurship prevalence rates), its popularity is growing with investors from the United States, Europe, and the region itself.[15] Some of the most successful private funds include Brazil's Gera Venture Capital, Mexico's IGNIA fund, and the regional Elevar Equity fund, as well as efforts by Adobe Capital. Each uses market-based financing methods to help correct persistent gaps in social services, including microfinance, affordable housing, environmental protections, healthcare services, and education.

Using a series of case studies, the following section identifies of firms engaged in impact investing, identifying key lessons from the successes and failures of firms engaged in impact investing in Latin America. The wildly successful Grupo Compartamos in Mexico, for example, lends to low-income entrepreneurs while still posting above-market rate returns. FINAE (also in Mexico) is another, lesser-known example of a successful firm using new funding mechanisms while tackling long-standing public issues. Specifically, FINAE is making affordable student loans for college available to wider segments of the population while maintaining a profit.

Case Studies

The diversity of Latin America's impact investing experience—ranging from markets as big as Brazil or as small as Honduras—provides useful cross-national comparisons and gives crucial insight into how the impact investment model fares in different contexts.

A new generation of middle class, tech savvy, and engaged citizens both drives and feeds off of the spread of social entrepreneurship and impact investing. But the next phase of impact investing requires taking stock of where we are today and charting a course forward based on what has and hasn't worked.

The following case studies are divided into private sector, government, and multilateral organization efforts so as to better address questions relevant to their unique roles in this sector. Will these models continue gaining traction in Latin America? Where is the practice successful and why, and how will it change and progress in the future? The answers to these questions will shape the decisions of investors, entrepreneurs, and policymakers moving forward.

Private Funds Take the Lead

The public sector and numerous multilateral or quasi-governmental agencies play a key supporting role in impact investing, but private-sector investors are the major driving force. They supply the majority of funding and thus shoulder most of the risk. For them, success or failure depends on the profitability and sustainability of any given social project.

Adobe Capital: Adobe targets a number of high-impact investments in Mexico—including organic agribusiness, recycling and waste management, clean energy, and tourism—with funding that ranges from $100,000 to $3 million.[16] Erik Wallsten, Cofounder and Managing Partner at Mexico's Adobe Capital, is one of the leading investors in this space. Impact investing "is on the cusp of where the world is going," he argues, "and it requires changing business mindsets because the companies we are investing in have a strategic advantage."[17]

Adobe also provides various forms of assistance to its investees through its offshoot organization, New Ventures Mexico. New Ventures has been investing in growth stage, socially conscious small- and medium-size firms (SMEs) since 2004—and not just with money from Adobe. It sits at the center of a web of public-private partnerships, receiving funding from the World Resources Institute, which funds similar organizations from Brazil to Indonesia, as well as from the Mexican government. FINAE and SalaUno, described below in greater detail, are each successful investments of the Adobe universe.

Adobe started with one fund worth $20 million in 2012, which it then invested in three companies. Initial positive signs from the companies pushed the founders to create a new fund, worth $15 to $20 million, which will focus on investing in higher-risk early stage ventures. Adobe is unique among the private-sector funds surveyed for this publication for its willingness to take a risk on early-stage ventures (with investments alongside institutional investors such as the Inter-American Development Bank and International Finance Corporation), and for its provision of various forms of assistance to investees. Among other things, this enables clients to source other outside funding.

Adobe has yet to exit an investment (its projected average time period between entry and exit is eight years), but it has invested in firms that survived and thrived during their first few years of existence. One reason for the viability of its investments is a policy of co-investing alongside institutional partners, which allows multiple entities to share risk at the earlier stage of projects. Also important to the model's success is the ability of investees to secure outside support. Though this

may not work for every fund, Adobe has set an example for how to maximize investment with sustained success.

The Elevar Equity II fund has averaged 78 percent cumulative asset growth since the initial investments.

Elevar Equity: In Latin America, Elevar provides funding for housing, healthcare, and financial services with a focus on early and growth stage companies. It is based in Seattle but runs the majority of its investments out of offices in Bangalore, India, and Bogotá, Colombia. Elevar is built around the theory that disconnected groups, such as migrants, can be brought into the global fold when granted access through customer-based models. These include microcredit, remote payment services, and low-income housing services that enable migrants to use remittances to purchase homes for their families in their home countries.

Between its two major funding vehicles, the Elevar Equity II fund (EEII) and the Unitus Equity Fund (UEF), Elevar has distributed $94 million to more than eleven million households for services that include microcredit, rural health, and home improvement loans.[18] Both funds deliver significant value for investors. The UEF's return on investment stands, as of 2013, at over 21 percent, while the EEII portfolio has averaged 78 percent cumulative asset growth since the initial investments.

Elevar currently has investments in five Latin American companies, which are largely focused on microfinance, and it also invests in FINAE [see p. 9 for more on FINAE]. One of its more innovative investments is in Unión Andina, a company that allows migrants to channel remittances sent to Latin America from the United States and Europe into affordable home mortgages in their home countries.[19]

Mexico's IGNIA: In Mexico, the IGNIA fund draws its $102 million in capital from an array of sources, including: institutional investors, investment banks such as JPMorgan Chase & Co.; multilateral organizations, such as the IDB; high-net-worth individuals; and groups such as the Omidyar Network and the Rockefeller Foundation. IGNIA focuses primarily on housing. In 2008, the fund made its first investment—$2 million in the Jardines del Grijalva affordable housing development in Chiapas for families who earn less than $10,000 a year.

The Grijalva effort formed a major part of IGNIA's strategy for addressing southern Mexico's structural shortage of housing. (This phenomenon results from large developers seeing no profit in developing the region while smaller developers often lack access to well-developed credit markets that enable financing of housing construction.) The company is on track to earn above-market rates of return while giving 1,800 families access to affordable mortgages. "We are big believers in finding business solutions to social problems," says IGNIA's Álvaro Rodríguez Arregui, Managing Director and Cofounder.[20]

IGNIA is particularly revolutionary for its aggressive focus on market-based solutions to base-of-the-pyramid problems. The firm's other Cofounder, Michael Chu consistently emphasizes he does not believe in concessionary lending—where impact investors accept a lower financial return in the interest of impact. He firmly believes that to incentivize people to invest in the base-of-the-pyramid, they need to enjoy market-rate or above-market-rate returns. Though this mindset is somewhat shared by other funds, INGIA seems to be the most intent on consistently pushing this message. So far the strategy seems to be working. IGNIA currently has nine companies in its

portfolio, proving that social impact is possible while still expecting returns of 20 to 30 percent.

In Summary: These three case studies all have elements in common, but each holds a distinct lesson. Adobe co-invests with institutional partners and mentors investees to mitigate the risk of failure. Elevar focuses on enabling disconnected groups to enter the global market, engaging a new part of the population that is typically overlooked. IGNIA seeks out social investments that can grant it the most return on investment, holding greater incentives for partners. Their success will inspire future investors and entrepreneurs in the region and will hopefully prove to institutional investors—who are more focused on returns—that a profit can be made when investing in impact-oriented projects.

Entrepreneurship Gaining Ground

Private funds such as Elevar and IGNIA are increasingly providing the funding, or the access to networks of venture capital, that social entrepreneurs desperately need to implement new initiatives. But Latin America's weak culture of entrepreneurship has led to few startups for socially conscious investors to invest in. That is now changing.

A new generation of Latin Americans, raised with higher expectations, less patience for the status quo, and unprecedented technological connectedness with innovators around the world, are increasingly launching their own ventures.

A newfound culture of entrepreneurship is taking hold, intensified with the support of government policies and multilateral financing. Some of the most notable examples are in Mexico and include FINAE, Grupo Compartamos, NatGas, and SalaUno. PicoBonito from Honduras and Caja Rural Los Andes and Unión Andina from Peru are all ventures spanning multiple sectors, countries, and financing models.

These companies are grappling with enormous development challenges on the most grassroots level. Their groundbreaking work will carry important implications for whether the startup mentality can continue to expand throughout Latin America.

IGNIA is on track to earn above-market rates of return while giving 1,800 families access to affordable mortgages.

FINAE: A private Mexican company, FINAE offers low-cost loans for students pursuing higher education. The loans, covering up to the full cost of tuition, have supported six thousand Mexican students. Forty-sixty percent are women. Seventy percent are the first in their family to go to college, and 25 percent have parents who didn't finish primary school. These loans are critical to the recipients: 71 percent wouldn't have been able to enroll in college without financial support.[21] FINAE Founder and CEO Francisco Vizcaya explains that "students have extremely limited options if they want to pursue higher education . . . they either have to receive admission to one of the free but extremely competitive state schools, or receive scholarships to private universities—leading many to withdraw altogether."[22]

Launched in 2006, Vizcaya argues that FINAE's system, which shares the risk of the loans through partnerships with the IDB and ten private universities, is now proven to be profitable and sustainable. Forming partnerships with universities is critical because the universities select the students, create the loan packages, and subsequently mentor the students who take out the loans. When selecting

Forming partnerships is critical; universities select the students, create the loan packages, and subsequently mentor the students who take out the loans.

university partners, it was important to only select reputable institutions where students had a strong probability of employment post-graduation and could thus have the means to pay back their loans. The initial loan from the IDB was critical because traditional banks would not provide credit in a country where no other entity like FINAE existed.

Contrary to some expectations, students from the first wave of loans are repaying as expected, and FINAE has secured a fourth round of investor funding (of which two of the investors are IGNIA and Adobe Capital). The lesson here is that multi-sector partnerships—in this case including academia, the private sector, and multilateral organizations—can make a huge difference in ensuring a business model's success. And given its focus on giving opportunities to underserved young people, this model will likely have effects far beyond what can be measured through investment returns.

Grupo Compartamos: A wholly Mexican venture, Grupo Compartamos is the largest and best-known microfinance group in Latin America with nearly 2.4 million clients region-wide.[23] Both its client base and its profitability have continually risen since its founding in 1990. In 2012, the most recent fully recorded year, the number of participants grew by 9 percent, while interest income increased by nearly 26 percent.[24] The Guatemala portfolio grew by 145 percent while the number of branches more than quadrupled from four to eighteen. And in its original market, Mexico, the group opened seventy-two new branches.

Compartamos' success is based on its regional growth strategy as well as its innovative approach to social loan-making. Its Peruvian credit portfolio, for instance, grew 24 percent in 2012 thanks to the introduction of a new loan focused on low-income women, the "Crédito Súper Mujer" (Superwoman Credit). The Crédito Súper Mujer system is unique and bills itself as the first "group" credit in Latin America. Groups of twelve or more women involved in small businesses, who can work together or separately, jointly seek out the loan from Compartamos. Different rates or "preferences" are offered depending on the size of the group. This system does have detractors who point out that if one person fails to pay her portion of the loan, the others have to account for it; but it nonetheless seems very popular and helps mitigate the risk of the investor, hopefully providing a more sustainable model. It also shows the potential benefit to the investor and to the beneficiaries when risk is spread among a group with a common purpose.

Compartamos has proven that well-executed, socially-targeted microfinance can bring very significant returns—the group's 2007 initial public offering (IPO) raised $467 million and still counts as one of the most oversubscribed public offerings in Mexican history.[25]

NatGas: A Mexican company that converts traditional vehicles to ones that use cleaner natural gas engines, NatGas is at the forefront of developing a sustainable model for partnerships between local governments and socially oriented private companies.

Founded in 2012, NatGas leverages the fact that natural gas is, on average, 50 percent cheaper than conventional fossil fuels and significantly cleaner when burning. NatGas specializes in retrofitting cars, buses, taxis, and other vehicles to become "bi-combustible," or capable of burning

both natural gas and traditional gas, and has successfully partnered with the local Querétaro authorities to convert nearly one-fifth of the state's public transportation fleet. Bolstered by public subsidies, more than 750 Querétaro taxis and twelve microbuses have been converted to natural gas, with plans underway to replace 150 vehicles in the state bus fleet.

The company, inspired by similar efforts in Argentina, Colombia, and Peru, is already pursuing collaborative efforts with the governments of San Luis Potosí, Guadalajara, and Mexico City. The question ahead will be whether local government support, as well as the funding achieved through subsequent investment rounds with both the private sector and Mexico's development bank, will be enough to continue scaling up NatGas' operations and fundamentally shift Mexico's energy use to a cleaner, more affordable footing.[26] For now, it seems that NatGas' ability to form mutually beneficial partnerships with local governments could provide a sustainable model for similar companies. Josué Hernández, the entrepreneur behind NatGas' swift growth, notes that the Querétaro government is known for being innovative and environmentally conscious, and that the city's size (population of three million) makes it optimal for an exportable pilot program.

Pico Bonito: Pico Bonito demonstrates the unique promise of for-profit management in another sector: sustainable forestry. The company, founded in 2006, applies a business model to environmental restoration with projects like the Honduras program to plant more than one million trees in Pico Bonito National Park. More than five hundred thousand trees have already been planted, and the project employs more than 150 people.

Pico Bonito raised its current operational fund of $5 million through a mix of philanthropic and innovative market-based mechanisms. Support comes from groups like the KL Felicitas Foundation and the US-based EcoLogic Development Fund. But the company also makes its own sales. Pico Bonito sells carbon offsets for investments in forestry carbon sequestration efforts and also engages in the environmentally sustainable sale of timber from the forests under its cultivation. So far, Pico Bonito's return on investment is 20 percent, easily above the risk-adjusted market rate for the timber sector. With this, the company provides agro-forestry training for local communities that then benefit from the increased sales of staple crops such as beans and corn.[27]

Pico Bonito's business strategy, which uses financing from a combination of donations and sales, is a model for the sustainable forestry world. The involvement of the local community is also unique and critical to its success. Engaging local stakeholders prevents illegal logging (previously an issue) while the company's efforts also increase local employment and food availability.

SalaUno: SalaUno is a successful example of impact investing in the healthcare sector, where far too many low- and middle-income citizens have poor or nonexistent access. Since 2011, SalaUno has provided more than eight thousand cataract surgeries and performed more than seventy-five thousand eye exams, based on a sliding fee scale for patients. The company, led by former investment bankers Javier Okhuysen and Carlos Orellana, is still small, with one surgical clinic in Mexico City. However, it is quickly expanding the number of vision centers that provide diagnostic consultations and other nonsurgical eye care.[28]

SalaUno reinforces a repeated theme among social entrepreneurs: the need to cultivate a diverse network of funding sources, which often includes both for-profit mechanisms as well as donor funding. The company was launched, for instance, in collaboration with Seguro Popular, a Mexican government health program, but quickly added private investment and a $250,000 grant from the IDB to scale up operations. Subsequently, it attracted equity from private investors, including

from Adobe Capital and from Fundación Cinépolis—a foundation financed by the Mexican movie theater chain. Like many other impact investors, SalaUno embodies the ingenuity and flexibility needed to implement a social impact venture. Future efforts in this space should take note of its resourcefulness.

SalaUno has provided more than eight thousand cataract surgeries and performed more than seventy-five thousand eye exams, based on a sliding fee scale for patients.

In Summary: These case studies—FINAE, Grupo Compartamos, NatGas, Pico Bonito, and SalaUno—are all from different sectors and at different stages in their development, but all provide important lessons. One commonality is that each organization received the first round of financing from public sector or not-for-profit actors; however, since that initial round, each has scaled up and is now receiving private financing. This demonstrates the critical role that public sector actors play in sparking new growth in the impact investing sphere.

The Growing Public Sector Role

Social entrepreneurs must look to a wide array of funding sources in both the private and public sectors. And it is here that governments, with their relatively large budgets and their mandate to operate in the name of the public good, can have a tremendous impact on the trajectory of impact investing. Even seemingly modest sums of money or other, nonmonetary forms of support—if applied to programs or incubators that have proven success and that reach promising projects in the crucial, early stages—can have a ripple effect throughout society.

This is a lesson being learned even among the perennially cash-strapped public sectors of Latin America. Mexico, Brazil, Chile, and Argentina have recognized the enormous benefits of creating platforms from which impact investment ventures can spring. While these efforts are in their infancy, they hold the promise of developing a more robust, better-funded, and better-connected generation of social entrepreneurs.

INADEM: Mexico launched its National Institute for Entrepreneurship (INADEM) in 2013 to foment the country's nascent startup culture. In 2014, INADEM examined and cleared more than seven thousand projects seeking investments through its SME fund. The Institute has begun serving as a central clearinghouse for guidance as well as a network for connecting potential investors to information and to social entrepreneurs.

For the firms that INADEM deems viable, the government will directly invest federal resources while also working to incentivize funding from private investors, thus serving in a much-needed accelerator capacity. The goal this year is to invest in sixty firms.[29] In addition, INADEM has created separate special programs, one for women SME owners and one for SME owners who live in the Mexican states most impacted by violence, where the goal is to "revitalize" local economies. INADEM hopes to invest in at least one hundred businesses this year.

It's difficult to evaluate INADEM's effectiveness given its relatively recent launch. However, the organization is moving to begin disbursal of funds to some of the initially approved projects. It has also created incubators in each Mexican state to enable the dispersion of information and funds to approved entrepreneurs.

> **Even seemingly modest sums of public money or other, nonmonetary forms of support can have a ripple effect throughout society.**

Start-Up Chile: Chile's state-organized and funded accelerator program aims to support early-stage entrepreneurs, but Start-Up Chile has several more years of experience, as well as a broader focus. Created in 2010, the program brought twenty-two startups in its first year from fourteen countries to work in Chile with local entrepreneurs. Each company was given a seed capital grant of $40,000 and a one-year visa.[30] Start-Up Chile has rapidly expanded. It is now accepting more than 250 companies a year and puts new participants through a rigorous, multi-week training process that culminates in a public "demonstration day" for the fifteen most successful projects.

One criticism is that many of the start-ups were unable to source local funding after graduating from the program, and many graduates then returned to the United States or Europe. In response, Start-Up Chile recently announced that it will begin providing more financing through its SCALE program. This program will give $100,000 to the three best projects of every thirty graduates after they commit to incorporating in Chile and raise an additional $30,000.[31]

Start-Up Chile is still relatively new and is adjusting the program to be more effective, aiming to incentivize the start-ups to stay and succeed in Chile and thereby inspire innovators across the country. This model has already sparked a following in other countries—most notably Brazil and Peru, which have implemented programs similar to Start-Up Chile.

City of Buenos Aires: In Argentina, the mandate to spur entrepreneurship has fallen to local governments, and the City of Buenos Aires has sought to do so by launching its own Bureau of Entrepreneurship (Dirección General de Emprendedores). The Bureau, led by Director Mariano Mayer, is divided into two incubators that provide physical operating space and financing for startups: Baitec, which focuses on technology-based projects; and IncuBA, which has a broader mandate to support all forms of innovative initiatives.

Since 2009, IncuBA has offered its services—and nearly $2 million in financing—to more than thirty thousand entrepreneurs; one result is the creation of ten thousand jobs. Mayer is a recent convert to government and comes from a private sector and academic background, but he is convinced that public investment is an "essential spoke" connecting investors, entrepreneurs, and universities.[32]

The dual incubator system is unique in an area where many programs (such as Start-Up Chile, Brazil, and Peru) are entirely focused on technology. The same is true of the local Bureau of Entrepreneurship. With youth unemployment hovering around 21 percent in Argentina, the training and jobs created by the program can have a real impact on both entrepreneurs and the wider society. Mayer emphasizes that even though the program was started by Buenos Aires for its city dwellers, the city is sharing the knowledge, programs, and data with other cities across Argentina that are interested in replicating the program.

In Summary: This series of cases represents diverse ways in which Latin American governments are spurring entrepreneurship and provides important models for how governments across the region, and even the world, can effectively create new innovation ecosystems that achieve social

progress. Some of the programs, namely INADEM and Start-Up Brazil, are very young and therefore lack sufficient data, but they nonetheless represent genuine and substantial attempts by governments to enable entrepreneurship and create new forms of employment for their citizens.

Initiatives with longer histories such as Start-Up Chile and Buenos Aires' Bureau of Entrepreneurship hold important lessons that can help cut down the experimentation phase and accelerate gains in this sector. Start-Up Chile, for example, discovered the natural difficulty of keeping firms rooted in Chile and carved out new policies to incentivize entrepreneurs to build locally. Buenos Aires recognized that products and services beyond technology can have a major impact on people's lives and thus created an effective two-pronged structure to ensure that non-tech entrepreneurs have access to specialized training and resources.

Multilaterals and Nonprofits Offer Support

The last "spoke" in the wheel of social impact investment includes institutional efforts by multilateral investment banks and nonprofit organizations that straddle the line between being privately run and seeking to serve the public good. These groups marshal both grant-based funding as well as private financing and technical support.

Two major examples of these organizations' hybrid approach are the Inter-American Development Bank and the New York-based Acumen Fund, both of which are sharpening their focus on impact investment in Latin America.

Since 2009, IncuBA has offered its services to more than thirty thousand entrepreneurs; one result is the creation of ten thousand jobs.

Inter-American Development Bank: The IDB is the largest, most heavily engaged investment bank in Latin America and, in many ways, one of the most innovative. Its Multilateral Investment Fund (MIF), launched in 1993 and currently under the direction of Fernando Jimenez-Ontiveros, was one of the first organizations to systematically support the then-undefined impact investment sector.

The MIF invests its grants, which range from $1 to $5 million, in microfinance and venture capital funds, most notably the Latin American Venture Capital Association (LAVCA).

Through the Opportunities for the Majority program, in operation since 2007, the IDB has targeted projects for the specific benefit of communities at the base of the pyramid, in sectors including agriculture, education, financial services, health, housing, and infrastructure. One such program is the $10 million given to the Nicaraguan bank Banco de Finanzas S.A. in 2012, which funded an affordable mortgage program for low-income citizens. Under the rent-to-own program, Nicaraguans are eligible for a fraction of their monthly rent to go toward a down payment on a reduced-price mortgage.[33]

In 2014, the MIF announced its first social impact bond offer, which will raise $5.3 million for an as-yet-undisclosed project. Under the "Pay for Success" model first applied in the United Kingdom and the United States, private investors who fund the project will be reimbursed, with interest, only if the social goals of the initiative are reached to the satisfaction of an independent evaluator.[34] As MIF principal investment officer Susana García Robles notes, "It is not only about investing, but also about creating the ecosystem: bringing other investors to the region, as well as other important financial stakeholders."[35]

Acumen: Major nonprofits like Acumen are among the important financial stakeholders that García Robles says must be engaged. Acumen's model mixes philanthropy with market forces, beginning by developing a fund through donations and then achieving sustainability by investing in profitable social projects and reinvesting the returns.

The IDB's Multilateral Investment Fund was one of the first organizations to systematically support the then-undefined impact investment sector.

One of the fund's notable successes was its investment in Tanzania's A-Z Textiles Ltd., now the largest anti-malaria bed net producer in Africa. An initial Acumen investment in 2002 allowed the small firm to scale up quickly, expanding its operations, attracting more private investment, and repaying Acumen while keeping the bed nets extremely low cost for the populations that need them the most.[36]

But Acumen's recent shift toward Latin America, in addition to its traditional focus on Africa and South Asia, demonstrates the region's growing role in the impact investment movement. Acumen opened a new office in Bogotá, Colombia, led by Latin America Director Virgilio Barco, based on its evaluation that the region is on the cusp of major start-up financing opportunities for socially conscious companies.

For Barco, Latin America has untapped potential because the market is "less developed than in other parts of the world, for various reasons—including an overreliance on the state, poorly developed entrepreneurial cultures, and the lack of role models."[37] In other words, Acumen, and other mission-driven nonprofits like it, wants to make sure that a newly resurgent Latin America doesn't miss its moment.

In Summary: The Inter-American Development Bank's Multilateral Investment Fund and Acumen's philanthropy-driven investment and reinvestment models show the role that non-government institutions can play in growing the impact investment sector. The IDB has carved out its role in providing critical catalytic capitol for numerous socially minded entrepreneurs, including FINAE and SalaUno. Acumen provides an interesting example of actors abroad who sense the enormous opportunities in Latin America and are making strategic decisions to enter the market.

Challenges Ahead for the Impact Investing Sector

The case studies demonstrate a number of commonalities for successful impact investment ventures. The "mainstreaming" or systematization of the sector is well underway, as groups such as university endowments and pension funds are beginning to diversify portfolios to include mission-driven investments.

At the same time, the very growth of impact investing has revealed a number of persistent challenges that must be overcome if the goal is to influence social outcomes on a broader scale. These challenges include a persistent lack of applicable metrics and meaningful standards to measure success, a dearth of data to measure program effectiveness, immense difficulty finding and securing the initial catalytic capital to get initiatives off the ground, and the fundamental challenge of becoming revenue-positive while serving the poorest communities.

Measuring Success

The lack of standardized metrics for impact investment proposals and a general failure to collect comprehensive data on the outcomes of existing projects are both linked with many of the other challenges facing the sector today.

The Global Impact Investing Network (GIIN) and other groups like the nonprofit advocacy organization B Lab are trying to address this shortfall by helping investors to set performance targets that will allow them to rigorously monitor and manage their investments. The GIIN created, for example, a tool known as the Impact Reporting and Investment Standards (IRIS) evaluation. IRIS, a "set of metrics that can be used to measure and describe an organization's social, environmental, and financial performance," is now the primary reference for both private sector impact investors and multilateral organizations such as the World Bank.[38]

Unlike most measures of financial success, however, these metrics are often largely based on qualitative indicators: organizational description, product description, financial performance, operational impact, and product impact. In addition to cross-sector indicators, IRIS uses sector-specific metric sets for areas such as housing, agriculture, and financial services.

Project length is another important factor to consider when determining the effectiveness of reporting metrics. Few investments have moved completely through their typical ten-year implementation window, and as more ventures reach maturity, measuring their social and environmental impacts will become easier. Already some of the pioneering projects are producing data on the number of jobs created, total populations served, products or services sold, and estimations of environmental impact. It is critical to develop at least a minimally unified set of standards for measuring these outcomes, as well as an effective way for collecting the data and making it accessible to current and future investors.

This sort of transparency will help grow the sector by legitimizing its efforts and mitigating concerns over the model's effectiveness. In particular, the perennial challenge of finding that first chunk of seed, or "catalytic," investment capital would be eased if prospective funders, especially those interested in making more and larger investments, can receive assurance of the quality and track record of socially-oriented projects.

Accessing Catalytic Capital

A common refrain across the case studies—even for those that have achieved significant success—is the persistent inability to access startup capital. A study by Pacific Community Ventures, "Impact Investing

2.0," identifies the bandwagon effect as a major challenge: investors are willing to enter a market only once it has proven successful.[39] JPMorgan corroborates this study with findings that show late stage investments making up 89 percent of their respondents' commitments, while the venture stage attracted just 8 percent.[40]

National, or even regional, systems of metrics would encourage entrepreneurs to conform to a set of best practices.

Difficulty in sourcing catalytic capital particularly impacts the groups that would benefit from it the most—the younger entrepreneurs and those from marginalized communities or informal industries. They lack the personal funds or family connections needed to move ideas forward from the planning stage. Governments and nonprofits can play a bigger role in serving these groups, while demanding and facilitating more transparency to attract private capital.

Here, policymakers can follow the examples of Chile, Brazil, Mexico, and Argentina, which utilize accelerators and joint university programs to provide grants and networking opportunities to underprivileged entrepreneurs.

The type of public-private partnerships currently led by quasi-governmental and multilateral entities like OPIC and the IDB is playing a critical role in connecting low-income communities with access to capital, loans, and information. Companies like NatGas demonstrate the potential of public funds to buoy a project in its earliest, riskiest stage, support its expansion and scaling up operations, and then allow it to attract private investment and expand as it becomes self-sustainable.

Many of these initiatives are full of promise, but are too young to bear concrete results. Mexico's INADEM is still reaching out to low-income entrepreneurs and recruiting them for its first programs. Start-Up Chile, with several more years of experience, is fostering more entrepreneurship, but it could also recruit young talent from impoverished communities more aggressively by offering "need-based scholarships."

The public sector can also step in to improve transparency and create more reliable evaluation tools. National, or even regional, systems of metrics would encourage entrepreneurs to conform to a set of best practices while creating a vetting process that will reassure potential investors. The efforts of groups like GIIN, and those of social entrepreneurs themselves, are pushing the sector toward greater accountability. Nevertheless, coordinated, country-level impact metrics could provide a gold standard and spur greater activity without incurring much additional budgetary cost.

So far, the experience of social impact investing indicates that the potential is real: well-managed projects, such as Pico Bonito or SalaUno, can have significant environmental and social impacts while also enjoying financial returns that rival any other sector. The challenge ahead is in finding ways to systematize this potential—to identify entrepreneurs who are at the most precarious stage of development and connect them to capital and business networks. Public sector and multilateral actors should be mobilized to help scale up, expand, and rigorously evaluate socially-oriented investment projects.

A Roadmap: Opening a New Era of Innovation in Latin America

Latin America is facing a decisive moment in impact investing. A sector still in its infancy, Latin America's impact investment market has nonetheless begun to grow rapidly. The next few years are critical to building the foundations for both a sustainable and inclusive innovation ecosystem.

Given the region's history of weak entrepreneurship and underdeveloped capital markets, the practice will undoubtedly encounter significant challenges to maintaining the positive momentum that it has so far generated. Expansion of Latin America's impact investment sector must focus on incentives that can attract a greater quantity of investors and entrepreneurs. This ecosystem must work in such a way that entrepreneurs, investors, and government all have complementary roles and naturally empower each other.

The key takeaways from the case studies can help guide impact investors in the next decade. The six policy recommendations below will be more relevant in certain contexts, but codifying a general set of principles can help clarify and offer solutions for the tradeoffs that policymakers and entrepreneurs will face as they seek to build more sustainable, equitable societies.

Six Recommendations to Boost Impact Investing

1 A clear, market-based legal system enforced by a solid judiciary branch is fundamental to attracting impact investments. In a free (or relatively free) market system, economic stability and a solid rule-enforcing foundation will incentivize the arrival of more investors.

The World Bank's *Doing Business Report* and the World Economic Forum's *Global Competitiveness Report* are guides for investors and governments. To be even more useful, these organizations should also include sections in each report detailing the impact of closed markets and weak judiciary branches on the potential for socially-minded investors to finance new projects. This would encourage national governments to tackle these issues with more vigor.

2 More networks and experience-sharing platforms between entrepreneurs and investors should be created. Conferences like FLII, MIF one, and others help to promote new ideas and highlight this sector's importance for societies. But more platforms for information sharing must be developed.

Here, think tanks, universities, investors associations like LAVCA, and multilateral organizations can play an important role. Investor family forums such as the Padres e Hijos conference (organized for families who own large corporations in Latin America) should be expanded to bring more players into the fold.

Many associations, organizations, and entrepreneurial networks already exist and are working on these issues in Latin America. For example, the Global Impact Investing Network (GIIN), Endeavor, Ashoka, and Red Innovada, or accelerators such as NXTPLabs and Social Lab, play a unique role in enabling and expanding these networks. The creation of new entrepreneurial accelerators and the expansion of existing ones are critical to the growth of impact investing.

Public and private universities must also provide the tools that entrepreneurs need to succeed. They

are the training grounds for the next generation of social impact investors and entrepreneurs but are often one-step removed from the real world experience of how to generate successful, socially-conscious investments. Universities can also be catalysts for producing public-private partnerships. They can serve as hubs for sharing experiences through conferences and digital platforms.

> **Governments should help the growth of impact investing by subsidizing a measure of the often-lacking venture-stage capital for projects.**

3 More attention should be placed on disseminating success stories and communicating the importance of social impact investing as a tool for improving economic and social well-being. One of the biggest challenges for such a new sector is getting the word out on its effectiveness. Multilateral organizations, including the IDB, the OAS, the CAF Development Bank of Latin America, and the Central American Bank for Economic Integration, as well as existing networks and accelerators should build platforms to diffuse these lessons. In the same way, US and regional think tanks can encourage governments to invest in the future of this sector.

4 Governments should help the growth of impact investing by subsidizing a measure of the often-lacking venture-stage capital for projects, especially when the entrepreneurs come from less affluent communities. This could be achieved through a number of programs, including accelerators and incubators, social impact bonds, government grants, and agencies such as OPIC. Problems accessing capital require two solutions: increasing and facilitating the availability of capital itself and overcoming a general lack of information and connectivity.

Initially, multilateral organizations such as the MIF have pioneered programs to correct this market failure, whether through financing entrepreneurs or enabling the creation of private impact investment funds. But governments are uniquely positioned to fulfill this role. In this way, governments can target young and low-income entrepreneurs who may have actionable ideas but who lack access to capital, thereby adding new and innovative actors to the social impact sphere. For example, while continuing to market Start-Up Chile to non-Chileans, the government can also encourage the program to recruit Chileans from a diversity of backgrounds and potentially offer a needs-based scholarship to enable their participation.

5 Tax incentives for for-profit companies with social impact missions should be put in place to encourage investments and entrepreneurship. In March 2014, Great Britain implemented the Social Investment Tax Relief (SITR) program, a 30 percent tax break for UK investors who invest in a variety of government-accredited organizations. According to the UK National Advisory Board's 2014 report, SITR has the potential to provide over $700 million of new capital to small social sector organizations.[41] This policy could be replicated throughout Latin America, particularly in countries like Mexico, which has a dense network of entrepreneurs and a pre-existing public agency (INADEM) to support startups. Multilateral organizations such as the IDB and the IMF could play a role in this process by advising governments that take out loans to change the tax code and providing technical support for doing so.

6 Local governments should be viewed as public sector partners as they often have more flexibility to spur private social enterprise. Querétaro state's green transportation program in Mexico

Tax incentives for for-profit companies with social impact missions should be put in place to encourage investments and entrepreneurship.

could be an effective and scalable model to follow. Alignment between the state government goals and NatGas operations demonstrates how state policies can use a combination of tax incentives and public subsidies to get a good idea off the ground until it becomes profitable.

Impact investing is growing at a rapid rate in Latin America. It has begun affecting communities from the bottom of the socioeconomic pyramid to the expanding middle classes. But it still faces many challenges. The top issues among them are access to catalytic capital and the need to create standardized measurements for impact that can parallel existing financial measurements. The case studies in this paper offer a glimpse into how investors, governments, entrepreneurs, and nongovernmental entities should think about addressing some of these systemic barriers.

But these challenges also present state and local governments and multilateral and nonprofit organizations with opportunities to get involved by providing catalytic capital and enabling standards settings. Their involvement could help more entrepreneurs to start-up and grow their businesses to the tipping point where they attract private capital. It would accomplish one of impact investing's end goals: private sector investment in companies that provide social or environmental goods and services.

As these case studies demonstrate, successful social entrepreneurs often work with a combination of actors in the impact investing ecosystem. This collaboration allows them to source the funding and knowledge necessary to get their companies off the ground. This also allows entrepreneurs to provide critical goods and services to previously underserved populations as well as to Latin America's rising middle class, which expects higher-quality goods, services, and opportunities.

The goal of this paper is to draw more attention to some of the actors already in the field and to energize and contribute to the discussion on social impact investing. It is also important to encourage young people to follow career paths that enable them to "do good" while also being successful. We look at Latin America as a global leader and believe the time is ripe for more people to continue exploring impact investing as an opportunity to solve critical global issues.

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