

THE SECOND WAVE:

Promoting a second decade of impact investing in frontier markets in Latin America

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A report by:



With the support of:



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In memory of Fernando Sierra Maya who always followed one simple rule: ***“in the end, the important thing is how many people you have helped.”*** His vision and passion for creating change in Latin America will continue to inspire the work of many. How he lived his life is his legacy to us all.

Dear reader,

My co-founders and I started IMPAQTO in Ecuador to harness the power of entrepreneurs in solving our country's biggest challenges. I was inspired by the incredible impact of entrepreneurs around the world and knew in my heart that Ecuador could benefit from this approach. After four years of helping change makers onto the path of impact entrepreneurship, I was inspired by their potential but also worried that the funding these companies need to grow is not present locally. So, I began to look abroad to the region and globally. What I found was a funding and capital market that doesn't see Ecuador and other countries similar to it. In the reports and global meetings I attended, Latin America was represented primarily by our colleagues from Mexico and Brazil, and - while I applaud and hope for continued advancement of the Mexican and Brazilian ecosystems - Latin America is more than just the large markets that serve as reference points in the impact investing world.

In fact, the majority of countries in Latin America face challenges more similar to those of Ecuador and other countries in the Andean region and beyond. We have smaller populations, smaller markets, but face the same socio-economic and environmental challenges and inequalities that entrepreneurs can solve. On the demand side of capital, we have early stage companies that require support and investment, and on the supply side, we have little even traditional investment dollars available, much less triple bottom line financing, with the intention of positive financial as well as social and environmental return. Thus, what can be done in these smaller, yet viable markets?

Our hypothesis in putting together this report is that, over the past decade, when impact investing was still new in the Latin America region, it was natural to start with the "low-hanging fruit" of larger markets. But I believe it is time to start pushing the envelope again, to ensure that impact investing is advancing within smaller markets as well - **a second wave of impact investing over the next decade** that ensures funding and investment is funneled to high-impact entrepreneurs in smaller markets such as those of the Andean region - as well as outside of the urban centers of larger markets.

Amazing innovations can come from unsuspected places. As a region we lose a huge opportunity by not tapping this potential in smaller markets in a more concerted way. Thank you for your interest in this report, and I look forward to working with you to activate high impact enterprise and early-stage impact investing in the region.



Michelle Arevalo-Carpenter
Chief Executive Officer
IMPAQTO

Dear reader,

At the InterAmerican Development Bank, we have a regional perspective. We understand that it takes many players to make an ecosystem work. In order to scale, a company needs various types of support and needs to understand how to get the help it needs, both internally - from the talent it hires to grow - and externally - from the mentors, sector expertise, and funding and finance it must attract. Entrepreneurs are continually piecing together this complicated puzzle of resources it requires. And ideally, all of these resources are located locally, wherever the entrepreneur happens to be active. However, we know that this is, unfortunately, not the case yet in most countries in Latin America and the Caribbean.

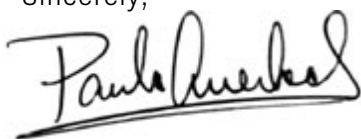
With this report, we are supporting a focus on the early-stage funding and investment pieces of the puzzle. We know that healthy investment ecosystems and the entrepreneurs that create new, scalable businesses that drive these ecosystems, need various types of funding and capital - from technical assistance grants to debt to seed and growth investment. We need not only a healthy ecosystem of entrepreneurs and entrepreneur support intermediaries, but also a healthy ecosystem of diverse types, sources and amounts of funding and investment.

As well, IADB supports this report's focus on highlighting innovators in the supply of funding and investment focused on triple impact - seeking high growth financially, socially, environmentally - in emerging and intermediate markets in Latin America, in particular the Andean region, but being open to cases and inspiration from other intermediate and emerging markets in other parts of Latin America, such as Central America, where early-stage impact investors have been active. With a clear vision of the barriers faced by those creating high impact companies and those investing in these companies, we can also begin thinking, discussing and collaborating to address these barriers together.

To stimulate action, we include inspirational examples of those that have created funds and other funding and financing vehicles in these challenging, intermediate markets. We can learn from these pioneers, be inspired by their words, and realize that these types of financing vehicles can be started up and grown in our own countries, helping to power the vibrant economies we envision in all countries in the region.

Thank you for your attention to this report.

Sincerely,

A handwritten signature in black ink, reading "Paula Auerbach". The signature is fluid and cursive, with a horizontal line underneath the name.

Paula Auerbach
Senior Specialist
Inter-American Development Bank
Multilateral Investment Fund

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EXECUTIVE SUMMARY

Impact investing is growing in Latin America. Seventy-eight impact investment firms reported investing into Latin America between 1997-2016¹. Nearly 80% of these impact investors made their first investment in the region after 2007, with 14-15 new entrants every two years, representing an important **first wave of impact investment in the Latin America region, mostly into large market countries**. Impact investors in the region have been most active over the past decade in Brazil, Mexico, and, more recently, Colombia². However, Latin America & the Caribbean is a region of small market countries. Twenty nine of the thirty - three countries and territories in Latin America and the Caribbean have populations of 32M people or less. So what can be done to promote a second wave of impact investing in these markets? This is one question this report aims to answer.

OBJECTIVES

With that background, the objectives of this report are three-fold:



1

to add the voices of **smaller markets** in the region to challenge our region's entrepreneurs and investors to revisit their assumptions for why these frontier markets are not a higher priority for impact investment



2

to highlight, via the words and **stories of** actual companies and investors, the **challenges** encountered and innovative **solutions** that exist in small markets



3

to inspire local and regional **action and collaboration** leading to a **second wave of impact investing** over the next decade in these relatively untapped markets

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SCOPE

Given the focus and objectives of this study, the scope of this report is limited to:



1

Impact. companies and investors that seek triple bottom line growth: social, environmental and financial, and aim to serve the needs of the region's growing vulnerable populations³



2

Small markets. ideas and action to apply within small market countries and regions, which are early stage



3

Early-stage. funding and investment under US\$500K,

CHALLENGES



1 .....
WE ARE SMALL:
the small market
challenge

From the entrepreneur perspective: It is difficult, when living in a small country to think past one's own national borders. Entrepreneurs in the region, in general, aren't thinking strategically about scale from the inception of their enterprises. Even if they do have ambitions to scale nationally, in a small country, for example, like Ecuador, where 100% market saturation represents just 16M people, often that's still not enough of a potential market to entice regional or global investors. To read more about the need to think globally to have greater impact locally, [see page 32](#) Spotlight on Waku in Ecuador.

From the investor perspective: Investors typically want rapid growth. Thus, in part because of the perceived lack of deal flow, assumptions of scale limitations and limited capital, investors simply aren't inspired to invest heavily in getting to know frontier markets. This is a critical barrier, as without that local knowledge and trusted networks, investors are unlikely to invest. To read more about the entrepreneur-investor disconnect, [see page 33](#) Spotlight on Kirah Design in Bolivia.



2 .....

WE ARE EARLY STAGE

our companies,
investors and
networks

“Investors want two things: a [robust] pipeline **[of enterprises]** in terms of scalability and size; and other investors to co-invest with.”⁴ Most early stage ecosystems have neither. Enterprises are often simply not ready for investment, lacking understanding of what it takes to grow their business and their impact, attract capital and innovate. Investor ecosystems lack diverse sources of early-stage capital, with an appetite for risk and an impact focus. To read more about how the dearth of capital is leading to a lost generation of high impact enterprises, [see page 35](#), Spotlight on Agruppa in Colombia.

Finally, networks for both entrepreneurs and investors are fragmented, lack coordination and knowledge of impact. To read more about the importance of networks to coordinate links to international capital, [see page 37](#), Spotlight on InkaMoss in Peru.



3 .....

WE FACE REGULATORY BARRIERS

when investing
or receiving
investment

Entrepreneurs need to raise funds - donations, loans or investment - to grow. However, interviewees, both entrepreneurs and investors alike, expressed frustration at the practical challenges faced when attempting to raise investment for their companies or funds within existing regulatory frameworks. Interviewees noted several challenges that, while legally feasible, are difficult in practice, including, but not limited to: comparatively **high taxes**, the ability to fundraise via inclusion of **third party investment**, such as shareholders or other investors, (to read more about the practical regulatory barriers to stock options, [see page 38](#), Spotlight on Cuestionarix in Ecuador), **investment fund regulation** (To read more about the challenges to investment fund creation and operations, [see page 33](#), Spotlight on Fondo Progreso in Bolivia, [and page 40](#), Spotlight on Invictum in Colombia).



4 .....

WE NEED FINANCIAL INNOVATIONS

Traditional financial instruments that fund entrepreneurs - such as grants, debt, and equity - do not always meet the financial needs of early-stage, high-impact enterprises or the investors who want to support them. **Grants** are suitable for early stage companies at proof of concept stage, but aren't always structured to ensure funding is well spent or to incentivize growth, don't help a company build a financial track record to attract downstream investment, and are limited because grants aren't paid back to support additional companies. **Debt** is often difficult for early stage companies to access as they often don't have the minimum revenues, collateral, tangible assets, or ability to repay in periods required by traditional lenders. **Equity** investors typically expect rapid scale and high returns, and exit expectations that do not often align with realities of early stage companies, as exit or may not even be a priority or part of the enterprise's vision.

OPPORTUNITIES



1

WE CAN
THINK BIG

From the entrepreneur perspective, though all businesses start small, they will only attract investment with a big vision and the operational plan behind it to scale. Entrepreneurs must envision growth through their cities, their countries, Latin America and beyond, and build the right skills, networks and teams to power this growth. To read more about using global models and tech for big impact, [see page 47](#), Spotlight on TPAGA in Colombia. Entrepreneurs and investors both can focus on **solving big problems, not small markets**, to define market opportunities for high growth enterprises and investment. For example, rather than focusing on Bolivia's small market population of 11M people, focus on its US\$500B market opportunity for safe drinking water technology. To read more about the success story of a high impact company and one of its early investors, [see page 48](#), Spotlight on TerraFertil in Ecuador & the EcoEnterprise Fund.

From the investor perspective - on the supply side of capital - investors interested the under US\$500K ticket size might consider **co-investing regionally** and in neighboring small markets, to build their early stage pipeline and learn more about neighboring frontier markets. To read more about one early stage funds' regional approach, [see page 49](#) Spotlight Pomona Impact / Open up to a regional pipeline.

From the intermediary perspective - on the demand side of capital - enterprise support programs like networks or accelerators, based in small countries, can join forces regionally to promote regional and even global growth within its pipeline, such as impact-focused regional soft landings programs.



2

WE ARE
BUILDING
A MOMENTUM

Enterprises may be early stage but are growing. At the regional level, impact investors recorded 52 exits and investors are optimistic about the prospects for impact investing in the region.⁵ Perhaps the most promising development is an increasing awareness of and demand from underserved market⁶ that can inspire new entrepreneurs and talent to the space. For example, recent data indicates that in Latin America and the Caribbean homes with incomes of up to US\$10 / day (representing 70% of the region's population) are a steadily growing market currently valued at US\$750B.

Public and private **investors** are becoming more engaged in investing locally and taking risks, and new models are evolving that address risks to investing at the early stage. To read more about an impact company builder-fund taking risk head-on, [see page 52](#), Spotlight on Connovo in Mexico.

Networks in the region are also gaining momentum as well, with new, professional players in entrepreneurship, investment and impact coming online. Existing players can leverage this momentum to attract others to by highlighting the strengths of frontier markets, such as: Geographic location and **environmental** biodiversity; **Innovation labs**, as small markets are compact, thus impact and validation of models to expand into other countries in the region is easier; Greenfields investing, as small markets are **less crowded**. Thus, it may be easier to find overlooked high-value companies and validate talent. Finally, we can highlight stories of success at impact-focused fora, such as the Latin American Impact Investment Forum (FLII) in Mexico and Guatemala, the Latin American Impact Investment Summit in Quito, and the global Social Capital Markets (SOCAP), as well as, perhaps more importantly, those fora that are not exclusively impact focused such as the Latin American Venture Capital Association (LAVCA), to raise awareness of impact investing, combat the small market myth and encourage potential investors to take a closer look at frontier markets. To read more about pioneer early stage impact funds in frontier markets, [see page 55](#), Spotlight on NESsT Fund in Peru.



3 ..... WE CAN PROMOTE LEGAL AND REGULATORY INNOVATIONS

Two types of solutions arose from our interviews to address legal barriers faced in the region: long term policy change processes and short term practical workarounds. **Long term** can be drawn inspiration and policy reform supported to remove barriers to and create incentives for impact investment, as well as leveraging existing movements to promote legal structures that make sense for high impact companies and their investors, such as the benefit corporation in the USA or similar initiatives in Colombia. **Short-term**, practical workarounds our interviewees are using in practice mostly focused on making it easier and cheaper to establish entities in more entrepreneur and investment friendly environments, such as the USA. To read about two companies making it their business to make doing business easier through addressing legal barriers, [see page 57](#), Spotlight on Westaway in the USA, offering flat-fee, impact entrepreneur-friendly legal services; and [see page 57](#), Spotlight on Stripe Atlas in the USA, making the establishment of US entities quick and easy.



4 ..... WE CAN APPLY FINANCIAL INNOVATIONS IN OUR WORK

In early stage impact investing, “innovation comes from the outside. We can’t wait for banks to develop innovative financial products for entrepreneurs. We need actors that are close to entrepreneurs and that have access to investors to create that bridge.” Innovators in the field have become that bridge and developed new grant, debt and equity models that better address the needs of early-stage high impact companies.

Examples of grant alternative structures & models

Grant alternative structures, in some cases, better support high impact startups. For example with contingent **recoverable grants**, while grant funds are usually given away, recoverable grants can be repaid, if the enterprise achieves a certain level of sales or secures additional financing. To read more about contingent recoverable grants, [see page 58](#), Spotlight on Topa.uy & IADB in Paraguay.

In the case of **social impact incentives** or SIINC, while grants don't necessarily help a company build a financial track record to attract downstream investment, SIINC directly help a company improve its financial track record by directly linking grant funding as revenue to the company, triggered when the company delivers specific impacts, and involving debt providers or investors in SIINC structuring. To read more about SIINC, [see page 59](#) Spotlight: Roots of Impact & SADC / Social Impact Incentives (SIINC),

Examples of debt alternative structures & models

Alternative debt structures have more flexible repayments, longer time horizons of repayment, grace periods and prepayment discounts that better address the financial needs of early stage companies, compared with traditional debt. To read more about three debt alternative examples, [see page 61](#), Spotlight: Adobe Capital - New Ventures on **Revenue Financing**; [page 62](#), Spotlight on Beneficial Returns in the USA on **first-loss, guarantees** and, finally, [see page 62](#), Spotlight on Kiva in the USA, an **online crowdlending** platform where many individuals lend small amounts to early stage companies.

Examples of equity alternative structures & models

Alternatives now exist to the traditional equity model that, instead of depending on a traditional exit event, such as acquisition by another company or a public offering, provide investors a structured exit and a liquidation mechanism. These structures can be suitable for early stage impact enterprises that are too small for traditional equity investors.

To learn more about one example of an alternative equity structure, see page 63, Spotlight on NXTP Labs and its use of a **Simple Agreement for Future Equity (SAFE)** agreement. To learn more about a **syndicate platform** model, enabling aggregation and coordination of early-stage investment into companies, [see page 64](#), Spotlight on Founderlist in Chile.

CONCLUSIONS

We believe in the entrepreneurial power and potential of all Latin Americans, those in both large and small population markets.

We know that understanding the challenges we face is key to designing solutions that work, and there are many challenges. Despite these somewhat inhospitable conditions in frontier markets, innovations always find a way to come to light. As Buckminster Fuller once said, “you never change things by fighting the existing reality. To change something, build a new model that makes the existing model obsolete...”

This report has been an effort to highlight those brave individuals and institutions that are building a new model for Latin America, these rare sprouts growing in unforeseen places. And by highlighting their struggles and their successes, through their own words, we hope to promote learning and collaboration amongst those who, like them, also see the opportunities in the challenges around us. We draw inspiration from those who have already successfully “hacked the system” - who have transcended the generally held assumptions about small markets and their challenges and found a way to make the system work for impact entrepreneurs and the investors that seek to support them.

In conclusion, there are more than enough challenges to be solved. But the building blocks and examples exist to experiment with potential solutions. Whether you are an entrepreneur or an investor, a public servant or a titan of industry, we all can play a role. Think big. Leverage the momentum of a growing movement. Learn from others. Promote regulatory reform. Experiment with financial innovations. We each can take individual actions that, collectively, will get the right kind of funding into companies that are solving our world’s biggest challenges.

---

¹ ANDE/LAVCA/LGT, 2016, p.7-8.

² The top three countries for impact investment, based on the number of firms that invest there are: Mexico, Brazil and Colombia.” ANDE/LAVCA/LGT, 2016, p. 8.

³ For this study, in Latin America “**poor populations**” are defined as those households making US\$4 / day or less, and cannot satisfy their current basic needs. “**Vulnerable populations**” are those that make ~US\$10 / day and though they can satisfy current basic needs, they are at high risk - after one small event like a car breaking down, getting sick or losing a job - of falling into poverty. (Acevedo, 2015).

⁴ Rann, T. of Mercy Corps Social Venture Fund (2018 May 21). Telephone interview.

⁵ ANDE/LAVCA/LGT Ventures, 2016.

⁶ In the region, “poor populations” are defined as those households making US\$4 a day or less, and cannot satisfy their current basic needs. “Vulnerable populations” are those that make ~US\$10 a day and though they can satisfy their current basic needs, they are at high risk - one small event like a car breaking down or getting sick or losing a job - of falling into poverty. (Acevedo, 2015).

SPONSORS & ACKNOWLEDGEMENTS

About the Study Sponsors

IMPAQTO is a B-Corps with the mission of supporting change agents in transforming their ideas into scalable triple bottom line companies with impact in Ecuador. IMPAQTO has three business arms: IMPAQTO Coworking Spaces, IMPAQTO Labs Incubation and IMPAQTO Consulting which provides social innovation services to private industry and the public sector.

Inter American Development Bank - Multilateral Investment Fund (IADB-MIF) serves as the innovation laboratory of the IADB to promote development through the private sector by identifying, supporting, testing and piloting new solutions to development challenges and seeking to create opportunities for the poor and vulnerable populations in the Latin America and Caribbean region.

Acknowledgement of Study Participants

We wish to thank the 68 study participants interviewed - investors, entrepreneurs and intermediaries in the impact entrepreneurship and investment sector - representing experience from Argentina, Bolivia, Chile, Colombia, Costa Rica, Ecuador, Guatemala, México, Paraguay, Peru and the United States - for their contribution and support to this research project.

ORGANIZATION	COUNTRY	NAME
593 Capital Partners	 Ecuador	José Villareal
AEI	 Ecuador	Luis Marriot
Agora Partnerships	 USA	Brian Bell, Michael Hayes & Jesse Grainger
AlkuPets	 Ecuador	Juan Sebastian Espin
Aló Maestro	 Ecuador	Juan Carlos Rivadeneira
Alpha Mundi Group	 Colombia	Mauricio Preciado
Alterna	 Guatemala	Daniel Buchbinder
Ángeles EC	 Ecuador	Eduardo Quincoces
Banco del Pacífico	 Ecuador	Maria Susana Castro
Beneficial Returns	 USA	Ted Levinson
InterAmerican Development Bank - Multilateral Investment Fund	 Ecuador	Paula Auerbach
	 USA	Micaela Cordero, Oscar Hugo Farfán, Susana Garcia-Robles & Tetsuro Narita
BuenTrip	 Ecuador	Felipe Chediak
Capitalize Impact	 México	Anastasiya Litvinova
Cuestionarix	 Ecuador	Guillermo Zarate
DevEquity	 USA	Dan MacCombie
EcoEnterprises Fund	 Colombia	Jullia Santander
Fundación Bolívar Davivienda - Fondo Inversor	 Colombia	Fernando Cortés

ORGANIZATION		COUNTRY	NAME & LASTNAME
FounderList		Chile	Pedro Varas
Fundación Crisfe		Ecuador	Veronica Juna
Fundación Emprender Futuro		Bolivia	Allison Silva
Fundación Progreso - BILD		Bolivia	Daniel Andrade
Fundación Nobis		Ecuador	Claudia Rodriguez
Google.org		USA	Hector Mujica
Grupo Faro		Ecuador	Ana Patricia Muñoz
Grupo KFC		Ecuador	Xavier Ponce
Humboldt Management		Ecuador	Thierry Benoit
Idukay		Ecuador	Ignacio Freire
Private Individual		Ecuador	Corinne Lebrun
InkaMoss		Perú	Marco Piñatelli
Invictum Capital		Colombia	Fernando Sierra
Kirah Design		Bolivia	Gabriela Flores
Kiva		USA	Nicolas Lafaye
LexValor		Ecuador	Victor Chiriboga, Marcelo Mora- bowen & María Pía Rivadeneira
McKinsey		USA	Sara Boettiger
Mensajea		Ecuador	Jurgen Schuldt
Mercy Corps Social Venture Fund		Colombia	Tim Rann
Morrison Foerster		USA	Shannen L. Naegel
Multidoctores		Ecuador	David Borja
Nanay		Bolivia	Patricia Soria
NESsT		USA, Perú, Chile	Nicole Etchart
New Ventures / Adobe Capital		México	Rafael Alonso
Novulis		Ecuador	Greg Krupa
NXTP Labs		Argentina	Marta Cruz
Peru Opportunity Fund		Perú	Bruno Rath
Pomona Impact Fund		Guatemala	Rich Ambrose
Rokk3r Labs		Ecuador	Ernesto Noboa
Root Capital		USA	Brian Milder
Secretary of Productive Development and Competitivity, Municipality of Quito		Ecuador	Paola Ramon

ORGANIZATION	COUNTRY		NAME & LASTNAME
Secretary of Higher Education, Science, Technology and Innovation (SENESCYT) - Banco de Ideas		Ecuador	Gabriel Bermeo
Startups Ventures		Ecuador	Marlen Rueda
Sudamerik		Chile	Andres Baehr
Topa		Paraguay	Juan Puerto
Vamos Ventures		USA	Pedro Arce
VIVA Idea		Costa Rica	Bryan Bejarano & Lianna Mora
VSC		Ecuador	Vicente Servigón
Waku		Ecuador	Nicolas Estrella
Waykana		Ecuador	Demetrio Santander
Westaway Partners		USA	Kyle Westaway
Yaesta.com		Ecuador	Alejandro Freund

1

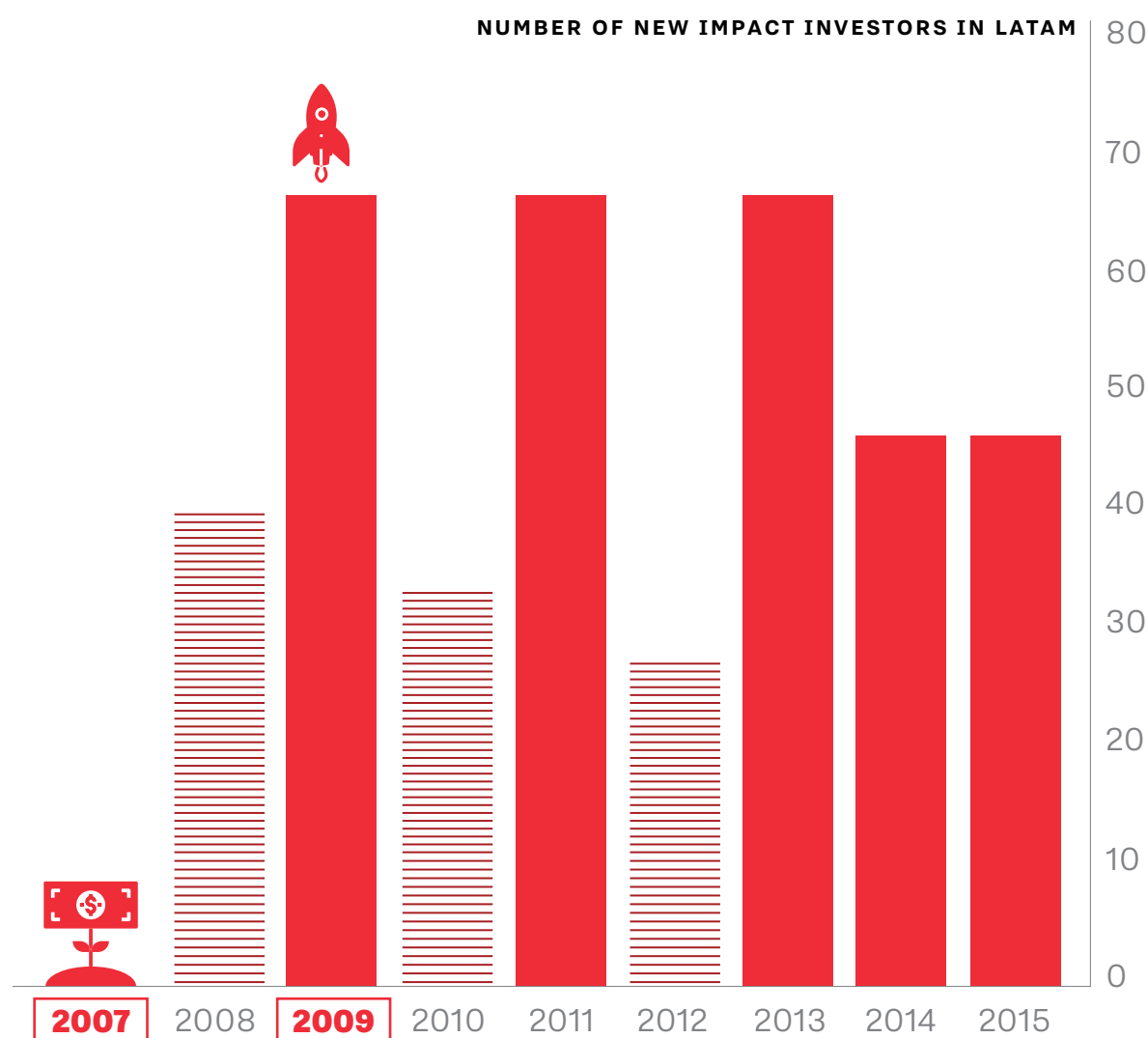
INTRODUCTION

Impact investing is growing in Latin America. Seventy-eight impact investment firms reported investing into Latin America between 1997-2016¹. Twenty-eight of these firms are headquartered in Latin America and manage US\$1.2B in assets. Thirty-one of these firms are headquartered outside of Latin America and manage a total of US\$7.2B² in assets. Nearly 80% of these impact investors made their first investment in the region after 2007, with 14-15 new entrants every two years thereafter, representing an important **first wave of impact investment in the Latin America region** (See Graphic 1).



OVERVIEW

78 impact investors firms reported investing into Latin America between 1997 - 2016, **80% of which made their first investment after 2007** when the term “impact investing” was coined.¹



GRAPHIC 1, The First Wave of Impact Investment in the Latin America Region³

¹ ANDE/LAVCA/LGT, 2016, p.7-8.

² Includes assets allocated to both Latin America and other regions. ANDE/LAVCA/LGT, 2016, p. 20.

³ ANDE/LAVCA/LGT, 2016, p.30.

Much of that investment appears to be in big market countries. Information, data and inspirational examples of impact investment in Latin America remain scarce. But where data does exist, it more often reflects the realities of larger population markets in the region where impact investors have been most active⁴ over the past decade: Brazil (205M), Mexico (121M) and more recently, Colombia (48M). Given that market size and opportunity are key drivers of investment, this trend makes sense. **However, Latin America & the Caribbean is a region of small market countries.** Of the thirty - three countries located in Latin America and the Caribbean, twenty nine have populations under 32M⁵ (See Graphic 2). What can be done to promote the Information, **second wave of impact investing in these frontier markets of the region?**



GRAPHIC 2 Latin America and the Caribbean: A region of small markets. 33 of the 29 countries and territories of the region have populations under 32M.

⁴ The top three countries for impact investment, based on the number of firms that invest there are: Mexico, Brazil and Colombia." ANDE/LAVCA/ LGT, 2016, p. 8.

⁵ Wikipedia: List of Latin American countries by population, Populations current as of 2015.

OBJECTIVES

With that background, the objectives of this report are three-fold:



1

to add the voices of **smaller markets** in the region to challenge our region's entrepreneurs and investors to revisit their assumptions for why these frontier markets are not a higher priority for impact investment

---



2

to highlight, via the words and **stories of** actual companies and investors, the **challenges** encountered and innovative **solutions** that exist in small markets

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3

to inspire local and regional **action and collaboration** leading to a **second wave of impact investing** over the next decade in these relatively untapped markets

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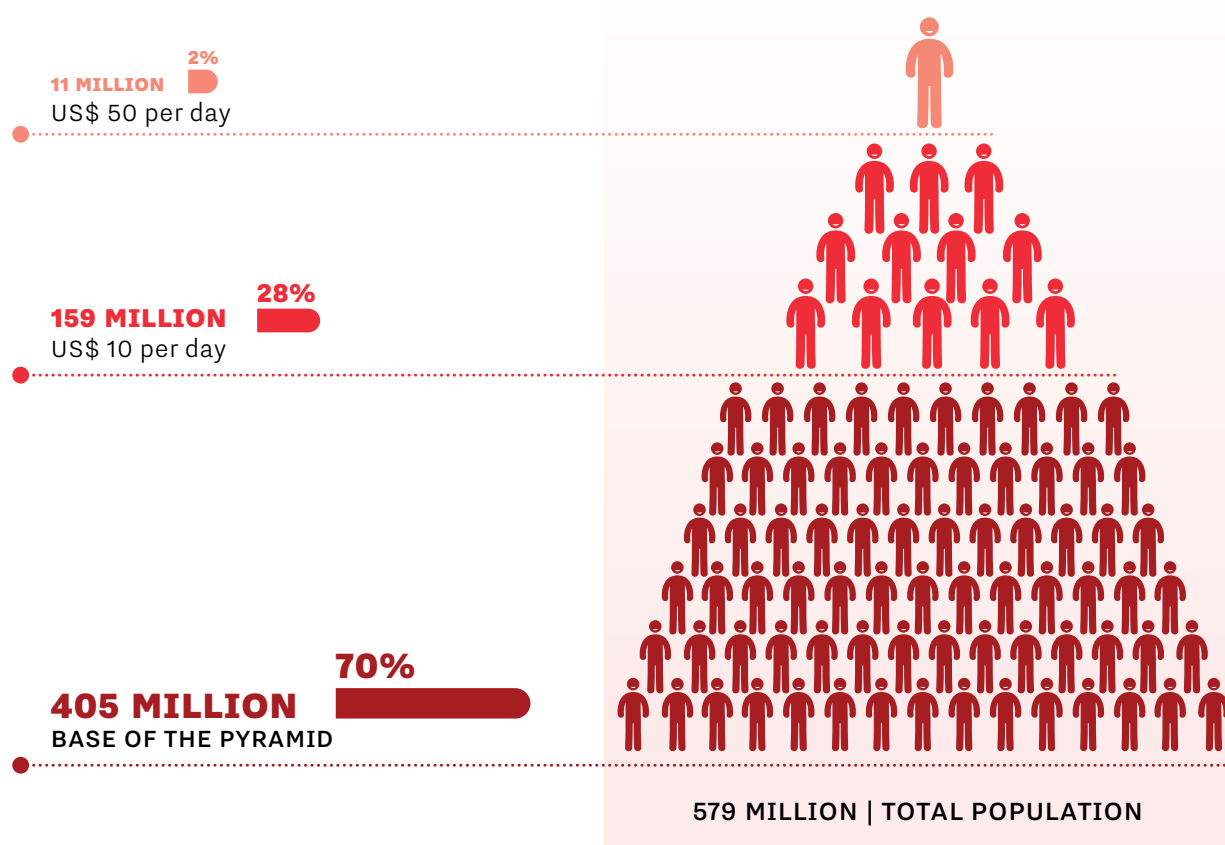
The primary audience for this report is anyone interested in early stage impact funding and investment in the region and specifically, those entrepreneurs, funders, investors and intermediaries that are new or considering entering this space. We want to do all we can to facilitate new actors or entice existing ones to dedicate more resources to promoting this second wave of impact investing. In this report, you will find not just a sanitized synthesis of findings from our interviews, but also the extensive use of quotes and “Spotlights” - the actual words and stories of active investors and entrepreneurs - that, hopefully, will bring to life the challenges and potential of the region.

SCOPE

As an intermediary promoting the start-up and scale of triple bottom line companies in Ecuador, IMPAQTO has, over the last four years, supported more than 134⁶ companies. These companies need smart money⁷ to grow, which, unfortunately, is currently rare in our context. With the support of the InterAmerican Development Bank (IADB) - Multilateral Investment Fund (MIF), the innovation lab of IADB, we developed this study to explore the context, viability and potential design of financial mechanisms for meeting the needs of early stage triple bottom line companies in Ecuador, the Andean region more broadly and other small markets. Given the focus and objectives of this study, the scope of this report is limited to **impact, small markets and early stage funding**.

1. Impact

We envision a world where all companies work not just for their own bottom line but also for people and planet. We also want to see more high-growth companies serving the needs of poor and vulnerable populations that represent 70% of the population in Latin America (See Graphic 3)⁸. There are so few early stage institutional investors in the region focused on high impact companies, that we found it important to interview and learn from active financial-only investors and models to inspire the current and future impact investing community.



GRAPHIC 3 Latin America is a region of underserved populations, with 70% of its population considered poor or vulnerable (Acevedo, 2015)

⁶ Number of companies supported by IMPAQTO to date, as of August, 2018.

⁷ "Smart money" - money from donors and investors that bring not just funding, but networks, influence and knowledge: the power to open doors, raise funds, influence regulators and other gatekeepers, and/or bring deep sectoral, or technical understanding critical to a company's business.

⁸ For this study, in Latin America "**poor populations**" are defined as those households making US\$4 / day or less, and cannot satisfy their current basic needs. "**Vulnerable populations**" are those that make ~US\$10 / day and though they can satisfy current basic needs, they are at high risk - after one small event like a car breaking down, getting sick or losing a job - of falling into poverty. (Acevedo, 2015).

2. Small Markets

We are interested in experiences that can apply to countries with small population markets, such as Ecuador, Paraguay or Guatemala, or to underserved regions typically outside of the large urban centers. Study sponsors are located in Ecuador and, thus, had easy access to experts in Ecuador and the Andean region, and as such, the study has a particular focus on perspectives from this region.

3. Early stage

As we are focused on small markets that are typically early stage ecosystems, we also limited our scope to “early stage finance,” or the “missing middle of finance,” defined for this study as between the range of US\$1,000 - US\$500,000. This is the financial need IMPAQTO sees within its pipeline of enterprises, and our interviews corroborated this funding gap exists. Funding before and after this range is more available. For example, micro-finance and government funding in the under US\$1,000 range is more common, typically supporting micro- and small enterprises or smallholder farmers, that, while important to local economies, are typically not interested in scaling regionally or globally; and institutional funding in the US\$1M to US\$2M+ range⁹ is, in general, more plentiful because at these amounts, the traditional closed fund model¹⁰ is more financially viable. (See Graphic 4: Missing Middle of Finance)



GRAPHIC 4. Missing Middle of Finance. As defined by Cheetah Development.

⁹ For example, in Colombia, investors report the average deal size is US\$2.2M, much more than small and growing high-impact businesses can absorb. ANDE/LAVCA/LGT, 2016, p10.

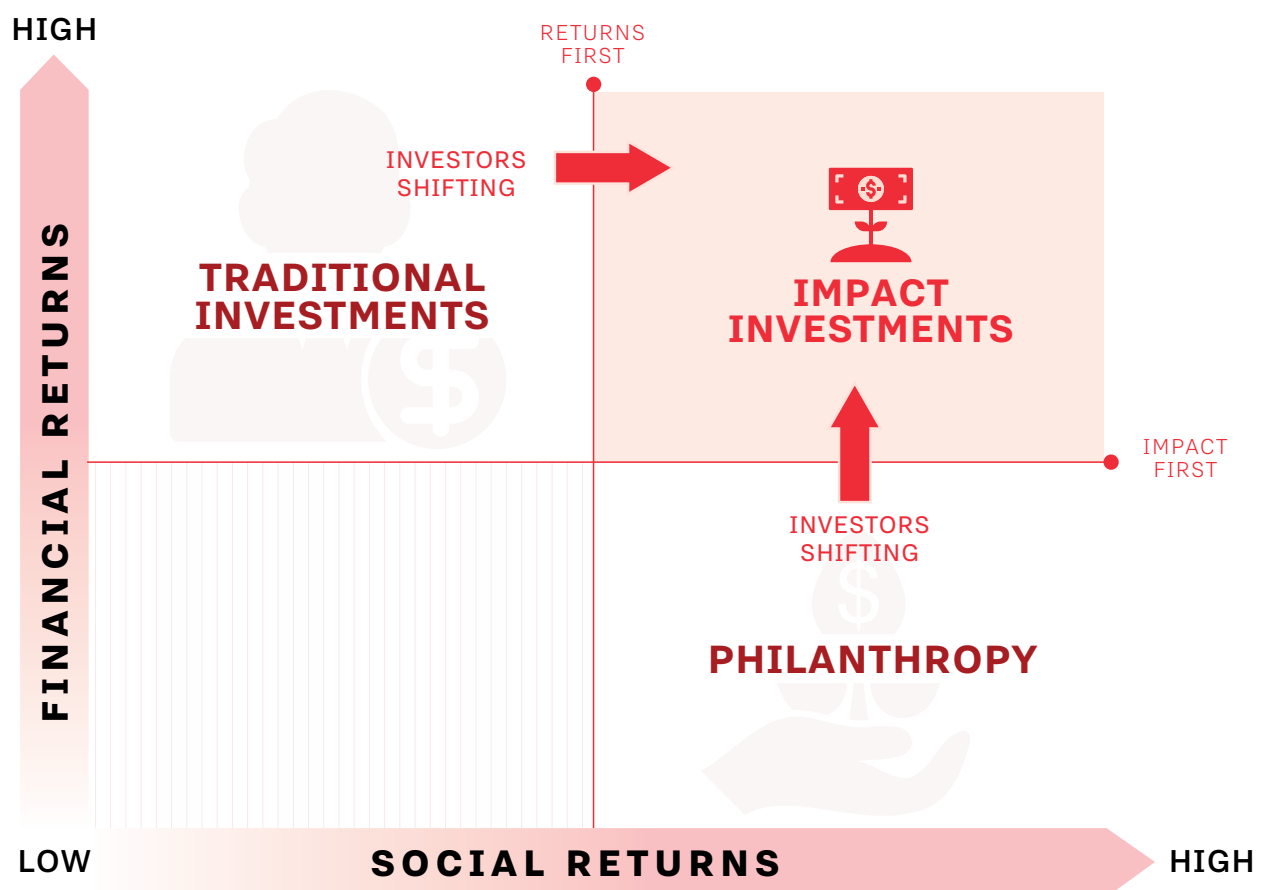
¹⁰ A traditional closed fund model might have an expected life span of ten years, five years to find and invest in companies, and five years to exit companies in order get your investment out with a significant return.

DEFINING IMPACT INVESTMENT

For the purposes of this report, we follow generally accepted definitions by entrepreneurial and impact investment networks¹¹ regionally and globally, and consider impact investors as those individuals or firms that:

- **MAKE** investments of US\$500Kk or less directly into companies using any financial instrument¹²
- **INTEND TO** create positive social or environmental impact
- **HAVE AN EXPECTATION OF** a financial return
- **FOCUS ON** small and growing businesses¹³

Within this sub-group of investors, there is a broad and diverse spectrum of expectations related to impact, financial return¹⁴, types of asset classes and financial instruments deployed. We also broadly include funders and investors often referred to as 4x4 investors (see Graphic 5), impact-first or finance-first investors, and venture philanthropists¹⁵



GRAPHIC 5. Impact investments are defined as those investments that seek both high social and financial returns.

¹¹ ANDE/LAVCA/LGT, 2016, p17.

¹² For example, grants, debt, equity, quasi-equity, guarantees, inter alia.

¹³ Small and Growing Businesses (SGBs) are defined as commercially viable businesses with five to 250 employees that have significant potential, and ambition, for growth. Typically, SGBs seek growth capital from US\$20,000 to US\$2 million. SGBs differ from the more traditional characterization of small and medium enterprises (SMEs) in two fundamental ways. First, SGBs are different from livelihood-sustaining small businesses, which start small and are designed to stay that way. Second, unlike many medium-sized companies, SGBs often lack access to the financial and knowledge resources required for growth. ("What is a small and growing business?", ANDE)

¹⁴ 46% of impact investors target a return of 10% and lower, 56% target a return of 11%+. ANDE/LAVCA/LGT, 2016, p.7-8.

¹⁵ Venture philanthropy is a type of impact investment that takes concepts and techniques from venture capital finance and business management and applies them to achieving philanthropic goals. More at "What is venture philanthropy," European Venture Philanthropy Association). Also see the International Venture Philanthropy Association.

METHODOLOGY

The research team undertook this project between March to August 2018. We developed and invited an initial list¹⁶ of organizations that the research team identified as active traditional and impact investors in the early stage (under US\$500,000) with interest in company growth and impact in Latin America, with an emphasis on Ecuador, the Andean region more broadly and other frontier countries where impact investing pioneers¹⁷ have successfully launched and actively invest. The choice to prioritize traditional, financial-only investors or experts was made depending on how active the investor is in our target countries and whether something might be learned from the interviewees' experience or model of early stage financing in Latin America to apply to the impact investment context. Ultimately, the research team consulted with **sixty-seven (67) investors and entrepreneurs in total**, through **sixty-two (62) semi-structured interviews with fifty-eight (58) organizations in eleven (11) countries**: 1 in Argentina, 4 in Bolivia, 2 in Chile, 5 in Colombia, 1 in Costa Rica, 28 in Ecuador, 2 in Guatemala, 2 in Mexico, 1 in Paraguay, 3 in Peru and 11 in the United States. Thirty (30) of the interviewed organizations are actively investing in the region. The team also facilitated one (1) focus group between legal experts and high impact entrepreneurs in Ecuador to delve more deeply into and regulatory challenges and opportunities section of this report. See pages 17, 18 and 19 for a full list of participants of this study.

The research team consulted:



67
investors and
entrepreneurs in total



62
semi-structured
interviews



58
organizations
participated in the study



11
countries in the region

NUMBER OF INTERVIEWS PER COUNTRY



¹⁶ Throughout these initial interviews, the list of impact investors of interest grew and the research team interviewed additional experts, as time and resources permitted.

¹⁷ Etchart, Nicole and Loic Comolli. "Betting on Higher Social Returns—Pioneer Donors Show the Way." *Social Enterprise in Emerging Market Countries: No Free Ride*. Palgrave Macmillan US, 2013. p. 113-131.

2 CHALLENGES

“

“Across Latin America, common challenges to entrepreneurial development include the lack of entrepreneurs with growth ambitions, lack of early stage funding, and weak networks.”

ANDE/Lavca/LGT, 2016, p.22

”

In particular in the Andean region and in Ecuador, interviewees highlighted four types of challenges to impact investing. The region:

**1**

is primarily represented by **small population markets**, which is challenging for entrepreneurs and investors

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**2**

is **early stage** (our entrepreneurs, investors and ecosystems)

**3**

faces regulatory barriers that inhibit entrepreneurial growth and investment

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**4**

is in **need of financial innovations** that serve the needs of both early stage entrepreneurs and investors

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1. WE ARE SMALL: The small market challenge

It is difficult for **entrepreneurs** living in small countries to think past their own national borders, and **investors** - who want rapid growth - often dismiss opportunities in small countries as limited in scale, or simply aren't aware of what's going on in small markets.

Entrepreneur Perspective

Entrepreneurs need to think bigger

“Across Latin America, common challenges to entrepreneurial development include the lack of entrepreneurs with growth ambitions, lack of early stage funding, and weak networks.”¹

Entrepreneurs in the region, in general, aren't thinking about scale from the inception of their enterprises. Even if they do have ambitions to scale nationally, in a country like Ecuador, where 100% market saturation represents just 16M people, often that's still not enough of a potential market to entice regional or global investors. Ecuadorian experts agreed, stating, “we need to consolidate quality enterprises with the vision to grow.”² Ecuadorian entrepreneurs, who have knocked on the doors of many funders and investors locally and abroad, stated, “Foreign funds aren't attracted to companies that only operate in Ecuador. You need to prove that the model works in other markets.”³



SPOTLIGHT



Waku in Ecuador | Global Reach, Local Impact

Waku was created in 2017 to distribute healthy food and drinks, made with Ecuadorian ingredients and traditions. Its first product is “horchata”, a typical Ecuadorian tea using more than twenty Andean plants that supports a healthy digestive system. “Our goal always was to create a company with global reach that generates impact in Ecuador. We want to motivate and open paths for other Ecuadorian products and brands to compete at the global level.”⁴

Ecuador has a well-developed local market for selling horchata. The founders believe that thinking no further than the national level is one of the biggest limiting factors for attracting investment. “The only way to grow...is to have companies win in international markets. Ecuador's market is very small.” Waku also increases its social impact by competing at a global level. For example, it purchases its plants directly from independent farmers in Ecuador, pays more than 10% over local prices, thanks to margins earned in the international market. Though based in Boston, Waku has achieved distribution in more than eighty shops in less than one year. In spite of that, one of its biggest challenges has been finding funding. “We haven't found alternatives [in Ecuador] like convertible notes, that allow postponement of valuation of the company until we have generated sufficient sales.” For this reason, its current investment round is made up exclusively of US investors, who require the company be constituted in the USA. (Read more on regulatory barriers to investment on p 37).

¹ ANDE/Lavca/LGT, 2016, p.22

² Ramón, P. of the Secretaría de Desarrollo Productivo y Competitividad. (2018 June 20). Personal interview.

³ Zarate, G. of Cuestionarix (2018 July). Personal interview.

⁴ Estrella, N. of Waku. (2018 July). Telephone interview.

Investor Perspective

Investors dismiss opportunities in small countries as limited in scale.

Interviews corroborate findings of other regional impact investing reports that cite key small country challenges as “sourcing quality deals, [and] achieving expected returns.”⁵ Investors interviewed noted the lack of a healthy pipeline of profitable, scalable companies as a serious impediment to growth of early stage impact investment in the region. For example, Tim Rann at the Mercy Corps Social Venture Fund (MCSVF) looks at, on average, 200 companies to every one company he finds investable within MCSVF’s criteria⁶. Some interviewees highlight that this is not just a problem of triple bottom line companies, [but] that it is, in fact, a “horizontal problem....Even [traditional companies] are not scaling in the region.”⁷

Investors don’t have the opportunities to get to know smaller markets.

Finally, in part because of the perceived lack of deal flow, assumptions of scale limitations and limited capital, investors simply aren’t inspired to invest heavily in getting to know frontier markets, and there is, as one expert put it, “simply a lack of regional and global investor knowledge of these [less well-known country] contexts”⁸. This is a critical barrier, because without local knowledge and trusted networks, investors, unlikely to seek and close deals.



SPOTLIGHT

Kirah Design in Bolivia | Entrepreneur - Investor Disconnect.

Kirah Design transforms recycled wood into high quality, unique items while creating jobs for talented artisans in Bolivia. Gabriela Flores, founder, launched the company in 2008 and to date, has trained 700 artisans and employs thirty artisans in its supply chain. In 2014, Kirah Design received a US\$100,000 investment from the Corporación Andina de Fomento (CAF), which was critical in turning the enterprise into a company. However, it is not easy to find follow-on funding that understands her company’s full value. “We are past the ‘Valley of Death’...but it took us a lot of time educating clients, artisans and investors on the impact we are trying to create.” Gabriela is sure financing options exist for her company, but there is a disconnect between investors and entrepreneurs. “The entrepreneur has no way of accessing financing,”⁹ especially in a market like Bolivia, that is off the investor map.

⁵ ANDE/LAVCA/LGT Ventures, 2016, p8.

⁶ Rann, T. of Mercy Corps Social Venture Fund (2018 May 21). Telephone interview.

⁷ Baehr, A. of Sudamerik. (2018 April 20). Telephone interview.

⁸ Naegle, S. of Morrison Foerster. (2018, April 19). Telephone interview.

⁹ Flores, G. of Kirah Design. (2018 July 23). Telephone interview.

2. WE ARE EARLY STAGE: Our companies, investors, networks

“Investors want two things: a [robust] pipeline [of entrepreneurs and enterprises] in terms of scalability and size; and other investors to co-invest with.”¹⁰

Most early stage ecosystems have neither. “[There is a] lack of an ecosystem of strong players, industry, universities, government, investors, angels, etc.” And for places where those do exist, their networks are fragmented, lack coordination and knowledge of impact.

Entrepreneurs

Our entrepreneurs, companies and talent pools are early stage.

Consistently, interviewees noted entrepreneurs in the region **lack the skills** and understanding of what it takes **to grow**, attract (by good self-marketing and promotion) and comply with requirements of future investment. Furthermore, companies that do exist have low growth expectations, for example, of 54 countries surveyed for expectations of high volume job creation over the next five years, Ecuador ranks quite low at 48th..¹² **Even fewer understand innovation**, which is critical for success of triple bottom line companies that have non-traditional business models. As one interviewee noted, “Ecuador is a very entrepreneurial country, but...it’s at the tail end of innovation.”¹³

Regional experts and investors also consistently highlighted the lack of local talent in the form of quality technical advisors, mentors and middle management - the people hired by founder entrepreneurs - in particular in back-end operations expertise and skills, such as human resources, finance, and marketing. This impression is reflected in the latest data. **“In the Global Talent Competitiveness Index¹⁴ - the annual [global] ranking of countries based on their ability to develop, attract and retain talent - the highest Latin American country featured is in 34th position (Chile).”¹⁵** Entrepreneurs also see this challenge. Founding entrepreneurs are forced to learn essential business skills themselves, but to scale, all companies require skilled middle management at “a price point that works for startups, but this is difficult to find and retain locally.”¹⁶

¹⁰ Rann, T. of Mercy Corps Social Venture Fund (2018 May 21). Telephone interview.

¹¹ Garcia-Robles, S. of the InterAmerican Development Bank (2018 April 11). Telephone interview.

¹² Global Entrepreneurship Monitor Global Report 2017/18. Global Entrepreneurship Research Association (GERA). 2018.

¹³ Ernesto Noboa, Rokk3r Labs. (2018 June 21).

¹⁴ Lanvin, Bruno and Paul Evans (Editors). The Global Talent Competitiveness Index 2017: Talent and Technology. INSEAD, The Adecco Group and the Human Capital Leadership Institute. 2017.

¹⁵ Acebuche, David Herranz. “Latin America has the world’s biggest skills gap. Apprenticeships could close it.” World Economic Forum on Latin America. 31 Mar 2017.

¹⁶ Bell, B. of Agora Partnerships. (2018 May 11). Telephone interview.

Investors

Our investor ecosystems lack diverse sources of early-stage capital, with an appetite for risk and an impact focus.

Interviewees consistently noted the lack of capital as “an important restriction in Latin America.”¹⁷ In Ecuador, for example, the Association of Entrepreneurship and Innovation in Ecuador reported just eleven institutional investors, of which only six were actively investing, and only seven were interested in the seed stage¹⁸. The missing middle is even more restricted because it is hard for traditional closed fund models to be profitable at small ticket sizes. “There are many more investors in the....\$US1M+ range where the fund economics make more sense. There aren’t that many funders in the under \$500K stage.”¹⁹

Daniel Andrade, President of Fundacion Progreso, and founder of the Fondo de Inversión de Impacto Progreso, recalled trying to structure and fundraise for what was to be the first impact investment vehicle of Bolivia, “Investors were puzzled and found the idea of an initial fund of under US\$1M almost laughable... [believing] ticket sizes of under US\$1M were a waste of time, since getting US\$3M out the door would have the same internal costs as US\$1M. So they preferred that. Further advice that he received, which, according to Andrade, clearly reflect the traditional for-profit investment mentality that permeates...the impact investment community, was that a standard 2% fund management fee wouldn’t cover himself or keep the lights on. “But that shows you how little they understood the context of Bolivia. US\$20K in Bolivia goes a long way,” Andrade says. “But the real...concern is that being pushed to take larger ticket sizes blurs past the issue that even US\$1M would have been insanely hard to deploy in Bolivia, given the specific type of social enterprises we sought.”²⁰



SPOTLIGHT



Agruppa in Colombia | No Capital, A Lost Generation of Companies.

Agruppa, in Colombia, was one of the most celebrated high impact enterprises in past years. It had a clear value proposition for its core customers, neighborhood mom and pop shops: lower cost fruits and vegetables, and time and money saved on transportation.²¹ The company demonstrated its impact in a World Bank study showing that Agruppa’s clients saw a 10% reduction in produce costs and a 50% reduction of transportation costs. However, despite this impact, Agruppa’s client retention was low. Why? Shopkeepers want to negotiate their own prices and socialize with other shopkeepers, so they only occasionally used Agruppa’s services. “Unfortunately, we didn’t have enough cash flow to pivot to a service that...[was]...more attractive for our clients while maintaining our social impact²².” Agruppa’s investors believe the company would have been able to grow past the “valley of death” if it had received appropriate financing when it needed it most. “Agruppa failed, in part, because of lack of early stage, risk taking capital. Even for a business that has exit / acquisition potential.” The dearth of early stage, risk-tolerant capital for high impact companies, even in a more active, diverse impact investing ecosystems, such as Colombia, demonstrates the acute need the region faces.

Not only do the countries in the region lack sources of funding and investment, another critical **challenge is the lack of diverse types**, amounts and stages of funding. “In healthy ecosystems [you] have sources of early stage, for example, grant capital in the **50-100k range for companies. This doesn’t exist at a sufficient level in many countries....**”²⁴



Moreover, the capital that does exist is often risk-averse. As one interviewee noted, “there is money in the ecosystem, but not much, and... what there is prefers traditional sectors that...have less risk. But as Mike Bannick of the Omidyar Foundation writes, high impact companies in emerging markets “require highly risk-tolerant capital.”

After all, *[these]... entrepreneurs...are often attempting to build entirely new business models, to serve consumers coming into the formal economy for the first time, and to do so under variable and sometimes volatile macro-conditions. Not surprisingly, there is far too little such capital currently available....*” Finally, few companies and investors focus on impact, products and services for vulnerable populations.²⁷ As one Ecuadorian funder noted, “existing initiatives don’t...respond to...needs of vulnerable communities that have a different reality.”²⁸

Thus, the concept of impact investing is still very new. As one impact investor in Chile remarked, “you might see [impact investing] every so often in the newspaper here and there, but [in general] most investors are new to the concept.”²⁹

¹⁷ Sierra, F. of Invictum. (2018 June 26). Telephone interview.

¹⁸ Alianza para el Emprendimiento e Innovación (AEI). “La Industria de Capital Emprendedor en Ecuador: 2016-2017.” Con el apoyo de CAF y COLCAPITAL.

¹⁹ Litvinova, A. of Capitalize Impact. (2018 June 19). Telephone interview.

²⁰ Andrade, D of Fundación Progreso - BILD. (2018 August 7). Telephone interview.

²¹ Liedgens, Verena and Carolina Medina. “Cuando una buena propuesta de valor no es suficiente”. www.carolinamedina.co/blog. July 17, 2018.

²² ibid

²³ Rann, T. of Mercy Corps Social Venture Fund (2018 May 21). Telephone interview.

²⁴ Bell, B. of Agora Partnerships. (2018 May 11). Telephone interview.

²⁵ Varas, P. of FounderList. (2018 June 20); Telephone interview.

²⁶ Bannick, Matt, Paul Goldman and Michael Kubransky. “Frontier Capital: Early Stage Investing for Financial Returns and Social Impact in Emerging Markets.” Omidyar Network. 2017.

²⁷ footnote definition of vulnerable populations (take from note in opportunities section).

²⁸ Bermeo, G. of SENESCYT. (2018 July 9). Personal interview.

²⁹ Baehr, A. of Sudamerik. (2018 April 20). Telephone interview.

Networks

Our entrepreneurial and investment networks are dispersed and lack coordination.

Recognizing this challenge, over the past decade, key impact investing industry events have emerged, through leaders such as New Ventures and the Latin American Impact Investing Forum (FLII), Alterna and the FLII in Central America and IMPAQTO and NEXUS and the Latin American Summit on Impact Investment in the Andean region. However, locally in frontier markets, there is a lack of awareness of these regional impact investment networks, and a “lack of coordination to understand objectives and collaborate.”³⁰

Finally, there are very few channels for connecting demand (entrepreneurs) and supply (investors) of capital.



SPOTLIGHT ■ ■ ■

InkaMoss in Peru | Coordinating Links to International Capital (Ale)

InkaMoss, founded in Peru in 2010, sells Sphagnum Moss, a naturally antibacterial moss with great absorption capacity, that is common in the Andean region. Through export of this product, InkaMoss generates jobs and increased income for 2,800 families in the high Andes. Marco Piñatelli, founder of InkaMoss highlighted that Sphagnum Moss has “no national market in Peru. In fact, demand for it comes entirely from abroad,” mostly, Asia. Despite its global vision, the company’s growth trajectory has not been easy, due to the “lack of a solid network and risk capital in the region.”³¹ However, support from the Peruvian government and international organizations has been critical, in particular to linking to other sources of capital. InkaMoss received mentoring and financial support from NESsT (See NESsT Spotlight p 55.) who referred them to Kiva (see Kiva Spotlight p. 62) from which it received a US\$49,925 loan at 4% over a period of forty-two months. With this fundraising track record, InkaMoss was able to approach others like the Peru Opportunity Fund and other larger international funds. In 2017, InkaMoss secured a SIINC (Social Impact Incentive) as part of a pilot with Roots of Impact and the IADB to test this financial innovation in supporting early stage entrepreneurs (See Spotlight SIINC, page 59).

3. WE FACE PRACTICAL REGULATORY BARRIERS WHEN INVESTING OR RECEIVING INVESTMENT

Entrepreneurs need to raise funds - donations, loans or investment - to grow. However, interviewees, both entrepreneurs and investors alike, expressed frustration at the practical challenges faced when attempting to run and raise investment for their companies or funds within existing regulatory frameworks. This section synthesizes the opinions expressed by interviewees on the barriers they believe they see and is not a formal legal or regulatory analysis. Founders and investors should ground truth the situations faced by their own companies by directly seeking legal and regulatory expertise in their country(ies) of operations. Interviewees noted several challenges that, while legally feasible, are difficult in practice, including, but not limited to: comparatively **high taxes**, the ability to fundraise via inclusion of **third party investment**, and investment **fund regulation**.

³⁰ Silva, A. of Fundación Emprender Futuro. (2018 May 30). Telephone interview.

³¹ Piñatelli, M. of InkaMoss (2018 July 24). Telephone interview.

Taxes

Comparatively high local taxes in the region can inhibit entrepreneurship and investment. For example, until recently³², “when an investor sells a company in Ecuador, (s)he pays [up to] 35% capital gains tax, the highest in the world.”³³ These costs decrease the profitability of Ecuadorian-based companies that might otherwise be quite attractive investments. As Julia Santander of EcoEnterprises Fund noted, “because of tax regulations, doing transactions in Ecuador comes at a higher cost and it is difficult to find investment structures that are attractive to investees and investors. Over the past years, we therefore stopped actively looking for opportunities in Ecuador.”³⁴ This hinders growth of the entrepreneurship ecosystem, which would benefit from foreign investment in the country. At least one Ecuadorian expert agreed, “[Foreign] investors don’t want to figure it out and bring cash to Ecuador.”³⁵

**SPOTLIGHT****Cuestionarix in Ecuador | Few options on stock options**

To go to college, all students in Ecuador must pass a National Education Evaluation Exam. More than 700,000 Ecuadorian students are not adequately prepared for this exam. Programs exist in urban centers, but are expensive and difficult to get to for students in peri-urban and rural areas. Cuestionarix is an online academic platform that prepares students in an interactive, personalized and flexible way, at an accessible price. Their success has led to the largest online community in the country with 360,000 students as of June 2018. The vision of Cuestionarix is to reach the other 12M underserved students in Latin America that face this same problem. The company wants to incentivize its employees to have a stake in this growth by providing stock options, but has found this to be challenging within existing local regulations where inclusion of third party shareholders is legally possible but practically difficult and time-consuming. The founders, thus, decided to establish a US entity and structure this third party partnership agreement through it, despite the extra time, cost and regulation, in the establishment and maintenance of a binational structure. As the company’s leadership put it, “investment is easier and more viable through a company registered in the USA.”⁴³

³² Legislation in Ecuador was recently been approved which may address these challenges and other regulatory barriers, the Law to Promote Productivity, Attract Investment, Create Jobs.

³³ Redacción Desde Cero. “La AEI destinará \$ 42 millones en 2018 para impulsar ideas innovadoras” in Diario EL TELÉGRAFO. 18 January 2018.

³⁴ Santander, J. of EcoEnterprises Fund. (2018 July 12). Telephone interview.

³⁵ Ernesto Noboa, Rokk3r Labs. (2018 June 21). Telephone interview.

Fund Regulation

Investors interested in creating funds to supporting ticket sizes of US\$500K or less, often find that, while legally feasible, it is more complicated in ongoing practice. For example, as one potential investor noted, in Ecuador, “it is difficult and expensive to create an [early stage] investment fund. The costs of the trust³⁶ eat up the fund itself....”³⁷ There are advantages to creation of a formal fund especially if the leaders of a new fund have a long-term goal of influencing the regulatory framework to pave the way for future interested investors, in which case “you want to be present formally as a fund”³⁸, but not all funders and investors have the time and resources to take on this challenge.



SPOTLIGHT



Fondo de Inversión de Impacto Progreso in Bolivia | Soccer referees using basketball rules.

Legal barriers exist for investors exist, too, in various shapes and forms in other small, less active investment markets. Daniel Andrade, founder of Fundacion Progreso and impact investing pioneer in Bolivia, manage to secure clear intents from potential U.S. investors to fund what was to be one of the first impact investment vehicles in Latin America and the Andes. However, the financial oversight, regulation and the costs incurred by cumbersome rules in Bolivia, compounded by the need for new and appropriate rules, would prove to be too high. Bolivia is a global micro-credit pioneer, with penetration rates as high as every 1 in 3 potential clients accessing credit³⁹. Thus, Bolivia’s regulatory environment is geared towards supporting micro-finance and debt, but lacks appropriate regulation for an impact investment fund hoping to issue equity. Additional barriers related to reporting, accounting, and currency made the operations of a longer-horizon equity fund, bureaucratic and inefficient.

Daniel recalled, “when we approached the Bolivian banking authority to ask for new rules appropriate to an investment fund...we thought they’d be thrilled to have someone come forward and ask to be better regulated. They were NOT thrilled to see me. They said, ‘These are the rules in place. You’re welcome to follow them or be subject to penalties for not...’”⁴⁰ Over the next year, while juggling the expectations... [of] several potential investors...Daniel and his team became lobbyists, trying to influence regulators with the realities of an impact investing fund attempting to do good for the Bolivian poor, “This is a new type of fund,” they explained. “Regulating us with current rules is like trying to referee a soccer match with basketball rules!”

Andrade and his team explored creative structures in Uruguay, Panama. “We were grasping at straws, trying to keep things afloat....We spent a ton of money and time lobbying in Bolivia. Ultimately, we could never focus on the actual fund....After almost two painful years, we decided to stop pursuing the fund launch and pivoted towards something else”.

³⁶ A Trust or “fideicomiso” is a typical fund structure.

³⁷ Lebrun, C. (2018 July 5). Personal interview.

³⁸ Cortes, F. of Fundacion Bolivar Davivenda / Fondo Inversor. (2018 July 16). Telephone interview.

³⁹ Pedroza, Paola A. “Microfinance in Latin America and the Caribbean: the sector in numbers.” InterAmerican Development Bank - Multilateral Investment Fund. 2010.

⁴⁰ Andrade, D of Fundación Progreso - BILD. (2018 August 7). Telephone interview.



SPOTLIGHT



Invictum in Colombia | Regulations trump success.

Invictum Capital is a Colombian boutique venture capital firm that operates through a fiduciary trust. Created in 2016 to provide capital to early stage entrepreneurs and to develop the risk capital industry in Latin America, it aims to promote development of the entrepreneurship ecosystem. "You just need one success for more traditional investors to begin seeing the value of this type of investment."⁴¹ However, after two years of successfully investing into high performing companies such as Ofi.com and Tpage, Invictum faces regulatory barriers limiting its growth. Invictum wants to raise additional capital for the fund, but as a trust established in Colombia, it is subject to strict regulations by financial regulators, and the process of fundraising and sale of fiduciary rights has become inefficient and costly. "The lack of knowledge about the benefits of alternative financing is tremendous and the lack of understanding from the fiduciary leaders of what this means in terms of economic development is very limited. As Daniel Blandon, co-founder of Invictum Capital states, "each time the fund wishes to bring on new investors, it will need regulatory approval. Now, Invictum faces the challenge of looking for viable alternatives that will allow it to scale and continue to generate impact. Interviews indicate that investors in other countries, such as Ecuador and Bolivia (See Spotlight Bolivia Fund, page 39), face similar barriers that impede creation of new investment actors.

A regional or foreign investor face with the challenges above, might. The bureaucracy and time required to figure out and conform to existing regulation ends up not being worth it, especially when, as one entrepreneur put it, "Fast response time of the entrepreneur when he or she receives an investment offer is key."⁴² One unintended result, as found in several interviews, has been that entrepreneurs and investors sometimes resort to opening binational structures, finding it less costly in time and resources to open, for example, a limited liability corporation (LLC) in the United States, along with another entity in Ecuador, and pay taxes and other operations costs in two countries, rather than simply opening one company in their own country of operations. Finally, related to all of the above challenges, the "constant changes in the law [and regulations] over the past decade...create uncertainty for investors."⁴⁴ All of which inhibits investment of all kinds, impact-focused or not. These frameworks form the ecosystem in which existing and future entrepreneurs and investors live and work. According to our several interviewees, that environment does not appear to be a hospitable one. So much so that the impact entrepreneur and investment pioneers who braved this difficult path are considering - or already have - resorted to costly and complicated structures to do what they need to do to be competitive. Unless regulatory frameworks are addressed over the long term, or alternatives are found in the short term, we risk missing the second wave of impact investing in the region.

⁴¹ Sierra, F. of Invictum. (2018 June 26). Telephone interview.

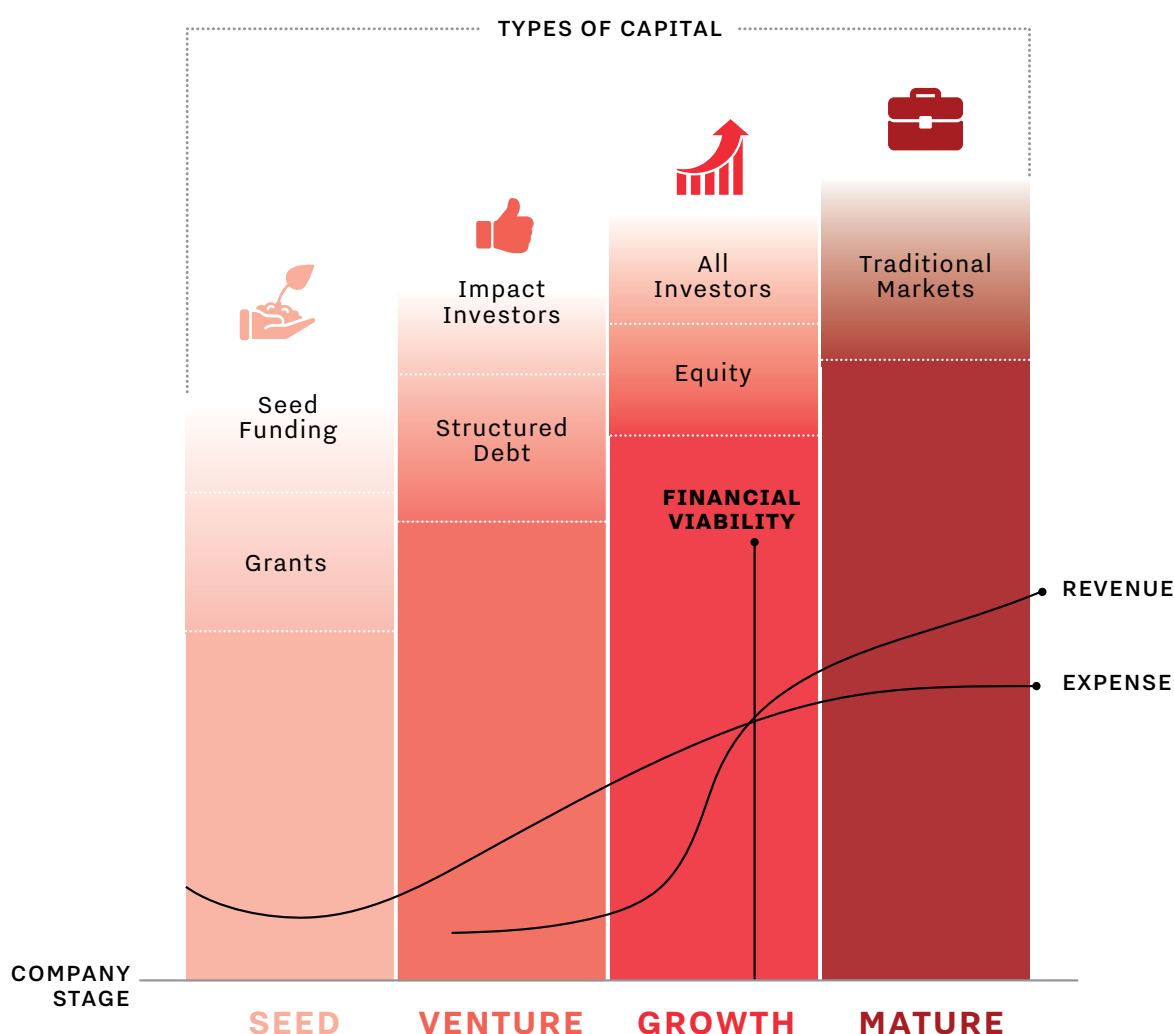
⁴² Lexvalor and entrepreneurs. (2018 June 26). Focus Group.

⁴³ Zarate, G. of Cuestionarix (2018 July 16). Personal interview.

⁴⁴ Lexvalor and entrepreneurs. (2018 June 26). Focus Group.

4. WE NEED FINANCIAL INNOVATIONS

As Nathalie Molina Niño, CEO of Brava Ventures has stated, "[Venture capital (equity)] dominates the headlines...you don't get a whole lot of press when you secure a line of credit or a loan. It's just not perceived as sexy." And, she goes on to caution, "Do not take venture capital...unless you're willing to be fired from your own company. There are many different sources of capital."⁴⁵ Founders of early stage companies should be looking for sources of capital that do not require giving away ownership in their companies. And while all of these traditional financial instruments exist - **such as grant, debt, and equity - exist**⁴⁶ they do not always meet the financial needs of early-stage, high-impact enterprises⁴⁷ or the investors who want to support them (See Graphic 6: Types of capital by stage).



GRAPHIC 6: Types of capital generally appropriate by company stage, income and expenses.

⁴⁵ Molina Niño, Nathalie. "Why venture capital can be a trap for entrepreneurs." The Big Think: Smarter Faster Blog. <https://bigthink.com/videos/nathalie-molina-nino-why-venture-capital-can-be-a-trap-for-entrepreneurs>

⁴⁶ Grants or donations are financial rewards, given by an individual or entity (typically a company, foundation, or government) to another - could be an individual or a company - to facilitate a goal, incentivize performance or create social or environmental impact. Grants are not typically paid back. Debt gives the borrower permission to borrow money under the condition that it is paid back at a later date, usually with interest. Equity refers to the sale of ownership interest to raise funds for business purposes.

⁴⁷ Armeni, Andrea and Miguel Ferreyra de Bone. "Innovations in Financing Structures for Impact Enterprises: Spotlight on Latin America." InterAmerican Development Bank (IADB) / Multilateral Investment Fund (MIF), The Rockefeller Foundation, Transform Finance. 2017. pg 4-5.

Grants

Grant capital is limited and typically lacks appropriate incentives for enterprise growth.

Grants are suitable for innovative companies at early and proof-of concept stage with high potential impact. For example, throughout the region, the InterAmerican Development Bank - Multilateral Innovation Fund has been a key player in providing technical assistance grants to support to high impact startups such as SocialLab in Chile, Novulis and Poliestudios in Ecuador, as well as intermediaries, like IMPAQTO in Ecuador and Koga in Paraguay, that support these kinds of companies. However, without follow-up, mentoring and advisory, post-grant, companies don't always use these funds effectively. In addition, enterprises that receive non-reimbursable funds don't build a track record to demonstrate financial viability of their businesses that would attract downstream debt or investment. In Ecuador, "in general, seed funds or risk funds are not provided in a way that allows adequate technical follow up enabling companies to succeed. There is a lack of operators providing entrepreneurs adequate mentoring, post-evaluation and help in creating networks to scale."⁴⁸

Finally, from the investor's perspective, philanthropic capital doesn't capture the potential gains or recover the capital of companies that succeed and, therefore, loses the opportunity to participate in the profitability of an enterprise that becomes commercially viable.⁴⁹ This affects the sustainability of impact funds and limits the impact to a certain number of enterprises because the capital is given away and isn't recouped to reinvest in a new batch of companies.

Debt

Debt instruments don't always fit the needs and characteristics of early-stage, high impact enterprises.

Loans for startups are limited, unattractive or do not exist. High impact enterprises usually have innovative business models that are unfamiliar to banks. They're startups so they don't have a financial track record. They often lack collateral or the tangible assets often required to offset a higher risk loan, and they often don't have cash flows that match a bank's typical repayment schedules. For example, in Ecuador, financing available from one entity supporting small enterprise requires at least US\$100,000 in annual sales, a loan minimum of US\$30,000 over two years maximum, with quarterly adjustable interest rates of 16%.⁵⁰ These terms are simply inaccessible for typical early-stage, high impact companies in most small markets.

Idukay is an example of this challenge. Idukay is an education management platform, founded by Ecuadorian entrepreneurs to automate and improve communication and interaction within high schools between professors, students, parents and administrators. As it is a software company, Idukay has no tangible assets and it was very difficult to attain financing. "We tried approaching various financial institutions until we finally got a loan for 5 years at 9%, but the process took six months."⁵¹ Idukay is not alone. Other entrepreneurs have noted, "There are no options for credit without collateral. There is...one...exception in the country, but they have lots of requirements and there are limits to early-stage entrepreneurs. It's not efficient and the process takes a long time."⁵²

Equity

Equity investors' expectations of rapid scale, high returns and quick exits do not always align to the reality of impact enterprises.

Early stage, high impact companies usually have slower growth rates. As one investor noted “the majority of companies that we see are... “zebras” (companies growing 2x or 4x) in place of “unicorns” (10x growth of capital). Moreover, [certain impact sectors like] health... companies [with their long growth timelines, e.g. sometimes a decade or more]...do not adapt well to the timelines of a closed fund.”⁵³

It is difficult for early stage companies in frontier markets to envision what their exit opportunities are, since the general ecosystem is still developing. For example, in Ecuador, “the equity market still needs development. There are few venture capital firms and we lack clear exit strategies for the investor.”⁵⁴

This is doubly true for high impact companies, which are so new that traditional mergers and acquisitions are virtually non-existent. As one interviewee put it, “there aren’t as many exits as we would like, even less so in social and environmental companies.”⁵⁵

Finally, exit may not currently be a priority or even part of the enterprise’s vision. Impact entrepreneurs often prefer to maintain control of their business to preserve the impact focus in their business model. As Greg Krupa, entrepreneur active in Ecuador explained, “we have had interest on the part of investment funds...US\$1M in exchange for equity..., but we declined...because we were too early to sell equity. We’d like to prove our product and impact first.”⁵⁶

⁴⁸ Ramón, P. of the Secretaría de Desarrollo Productivo y Competitividad. (2018 June 20). Personal interview.

⁴⁹ Armeni et al, pg. 17.

⁵⁰ Castro, M. of Banco del Pacifico. (2018 June 28). Personal interview.

⁵¹ Freile, I. of Idukay. (2018 June 19). Personal interview.

⁵² Santander, D of Waykana. (2018 July 23). Telephone Interview.

⁵³ Alonso, R. of New Ventures. (2018 July 31). Telephone interview.

⁵⁴ Ernesto Noboa, Rokk3r Labs. (2018 June 21). Telephone interview.

⁵⁵ Alonso, R. of New Ventures. (2018 July 31). Telephone interview.

⁵⁶ Krupa, G. of Novulismed. (2018 July 5). Personal interview.

3 OPPORTUNITIES

“

We can't wait for banks to develop innovative financial products for entrepreneurs. We need actors that are close to entrepreneurs and that have access to investors to create that bridge.

Alonso, R. of New Ventures.

”

We saw through the eyes of interviewees that small markets have a lot to offer entrepreneurs and impact investors - especially if we can turn the region's perceived weaknesses into opportunities.



1

Though small, **WE CAN THINK BIG.**



2

Though our ecosystems are early stage, there is **POSITIVE MOMENTUM** we can leverage and grow.



3

Though we face **REGULATORY BARRIERS**, we can promote legal and regulatory innovations

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4

Though we need **FINANCIAL INNOVATIONS**, examples exist **TO INSPIRE US.**

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1. TOUGH SMALL, WE CAN THING BIG

Entrepreneurs Perspective

Entrepreneurs can envision and plan for scale earlier.

Though all businesses start small, they will only attract investment with a big vision and the operational plan behind it to scale. Impact investors can and do play a role in providing feedback to entrepreneurs that they need to think big. For example, Ecuadorian investors we interviewed want to know, “how scalable is a business? do they have growth projections? Can they open operations in or export to other countries? Because the local market is...small.”¹ Entrepreneurs seeking investment must internalize this message, envision their businesses and impact growing past their city, their country and Latin America, and build the right skills, networks and teams to create this growth. Entrepreneurs seeking investment must internalize this message, envision their businesses and impact growing past their city, their country and Latin America, and build the right skills, networks and teams to create this growth.



SPOTLIGHT



TPAGA in Colombia | Using global models and tech for big impact

Invictum Capital's portfolio company, TPAGA, is bringing mobile payments to Colombia's unbanked.² Inspired by companies in India and China, TPAGA adapted technology to the realities of Colombia's taxi drivers, enabling them to take online payments for their taxi services. In addition to this service that makes transactions easier for both the customer and the taxi driver, TPAGA also collects the drivers' financial data which allows traditional banks to provide loans to this previously unbanked population. 95% of TPAGA's core users - truck drivers, domestic workers, couriers, and taxi drivers - are unbanked, so estimates over 900K people without a bank account who they can serve. This level of scale, use technology and global potential, make TPAGA attractive to investors.

¹ Benoit, T of Humboldt Management. (2018 July 3). Personal interview.

² LAVCA Venture Investors Blog. "TPAGA Co-Founder André Guitiérrez on Bringing Mobile Payments to Colombia's Unbanked." 6 February 2018.

Entrepreneurs Perspective

Entrepreneurs and investors can focus on big problems, not small markets.

According to Daniel Andrade, current Chief Social Entrepreneur at an impact company builder BILD in Bolivia, and former fund manager of Fondo Progreso, using population size as an indicator for market opportunity is short-sighted. He uses the example of potable water access and a high potential technology solution his current company is promoting in Bolivia. "Bolivia's current population is over +10M people. Assuming around five people per family, that's around 2M families in the country. We know that at least 60% of Bolivian families have limited or no access to clean, potable water, but even if we round down to 50%, that's about 1M Bolivian families in need of safe drinking water. We have a product that provides families 2L of clean, maintenance-free potable water per person, US\$100 per family per year (about ~US\$20 per person per year). So if we reached that total market, with a US\$500 dollar solution for a family of 5, that's a half billion dollar market opportunity. Size of population is a ridiculous metric."³ Need' should be the driver for the impact opportunities investors should seek. Solving a big problem should be the goal.



SPOTLIGHT



TerraFertil in Ecuador & EcoEnterprises Fund | We don't see a pipeline gap

TerraFertil provides a wide range of organic dried fruits from our highly biodiverse region - such as uvilla or golden berries, an Andean fruit rare in other parts of the world - and natural superfoods for nutritious snacks and beverages. TerraFertil began in 2005 as a small family business with an aggressive growth strategy. As a result, today, it operates in Mexico, Colombia, Peru, Chile, the United Kingdom and the USA and its products are sold in twenty countries. TerraFertil has received international recognition for its positive social impact, as it provides technical assistance, opens markets and creates jobs for hundreds of small farmers, especially women, in Ecuador and Colombia. In 2018, Nestlé acquired a majority stake in TerraFertil, a strategic partner that will position the company to achieve global scale. TerraFertil is a successful example of a profitable business model that, as it scales, continues to increase its impact, its financial returns and maintain its mission.

Behind this success story is the EcoEnterprises Fund. Originally spun out of The Nature Conservancy in 2008, EcoEnterprises has twenty years experience investing in companies with high environmental conservation impact in Latin America, and was one of the first institutional investors in TerraFertil. Julia Santander of EcoEnterprises fund has learned that having strong, hands-on involvement with the companies they invest in makes all the difference. "Having a full-time team on the ground in the region is key, making regular visits and building relationships early to provide support and assistance when problems arise". As a result, Julia notes, "We don't have a pipeline issue. There is a lot of talk about a pipeline gap, but we don't see it." Pipeline, connections and co-investors come with deep engagement in a country or region.

³ Andrade, D of Fundación Progreso - BILD. (2018 August 7). Telephone interview.

⁴ Santander, J. of EcoEnterprises Fund. (2018 July 12). Telephone interview.

Investors Perspective

Early-stage investors on the supply side of capital can consider co-investing regionally and in neighboring small markets.

One trend in the interviews was that fewer early-stage impact investing funds are investing exclusively in one market, instead tending to invest regionally, perhaps in response to the perceived lack of pipeline locally (see case Pomona Impact, p 49). In addition, if an investor is currently focused in a large market, he/she might consider exploring neighboring small markets. For example, if in Mexico, consider Guatemala, or if in Colombia, consider Ecuador. If in Quito, explore Cumbaya or Tababela⁵. Some funds in small market countries, such as Guatemala, are considering investing into underserved sub-regions in larger country neighbors, such as southern Mexico (see Pomona spotlight p 49.)



SPOTLIGHT

Pomona Impact | Open up to a regional pipeline

It is difficult for a traditional closed fund of under US\$20M to be financially viable.⁶ Add to that the transaction costs implied by ticket sizes of under US\$500K, and most investors don't think it's worth it. However, Pomona Impact is finding it worth it at this stage, as it is open to a broader regional pipeline. Pomona began investing from Guatemala in 2011 and supports early-stage entrepreneurs with technical assistance and financing in the US\$250-500K range. The fund has invested in more than twenty companies in Central America, Mexico, Colombia and Ecuador, in the sectors of agriculture, agricultural technology and basic services. Pomona aims to invest in companies that will create 15,000 jobs and improve lives of 500,000 people in the next five years. Rich Ambrose, a managing partner of Pomona states, "we have ambitious impact goals...and want...a healthy return....We structure investments with a minimum base return of between 18-30%, depending on the stage and risk profile of the enterprise."⁷

However, Rich affirms that his team needs to think regionally, to increase his chances of finding high impact entrepreneurs. "If I only focused on Ecuador, that [would be] an uphill challenge: how to put a US\$20M fund to work in tickets sizes of US\$500K, I'd have to find forty companies in less than five years. Not that that's impossible, but that's the line of questioning".

⁵ Neighboring communities of Ecuador's capital city.

⁶ Cruz, M. of NXT. (2018 July 23). Telephone interview.

⁷ Ambrose, R. of Pomona Impact Fund. (2018 April 23). Telephone interview.

Intermediary Perspective

Intermediaries on the demand side of capital can join forces regionally to promote regional and even global growth within its pipeline.

The idea of a **regional program to help companies startup and scaled in other neighboring countries**, perhaps via collaboration across programs that support high impact companies in, for example, Bolivia, Colombia, Ecuador and Peru. Each partner would pool its top three companies that would be required to bring along at least one interested investor. Interviewees also raised the idea of promoting **regional private industry partnerships. “We can align our efforts with opportunities that...industry...presents us.”**⁸ This might manifest as a partnerships with potential industry partners already present regionally. For example, Nestle working across the region in cacao and chocolate, might partners with intermediaries locally and regionally to solve challenges they see in their bean to customer value chains. Intermediaries might raise awareness around these challenges, identify entrepreneurs with ideas to solve these industrial challenges, provide technical assistance and seed capital to the best companies, which would be mentored within the partner industry player(s) to test and scale throughout the region.

2. THOUGH EARLY STAGE, WE ARE BUILDING MOMENTUM.

ENTERPRISES

Entrepreneurs are advancing and the growth of the underserved market can inspire new enterprises and attract new talent.

While the region needs more founding entrepreneurs, companies are growing. At the regional level, impact investors recorded 52 exits and investors are optimistic about the prospects for impact investing in the region⁹. Moreover, perhaps the most promising development is an increasing awareness of and demand from underserved¹⁰ markets that can inspire new companies and new talent to serve this growing market. For example, recent data indicates that homes with incomes of up to \$10 / day¹¹ (70% of the population in the Latin America and the Caribbean) is a steadily growing market currently valued at US\$750B in sectors such as Food (\$209B), Housing (\$184B), Transport (\$82B). Moreover, 75% of this population is in urban areas, with access to basic services such as water and electricity.¹²

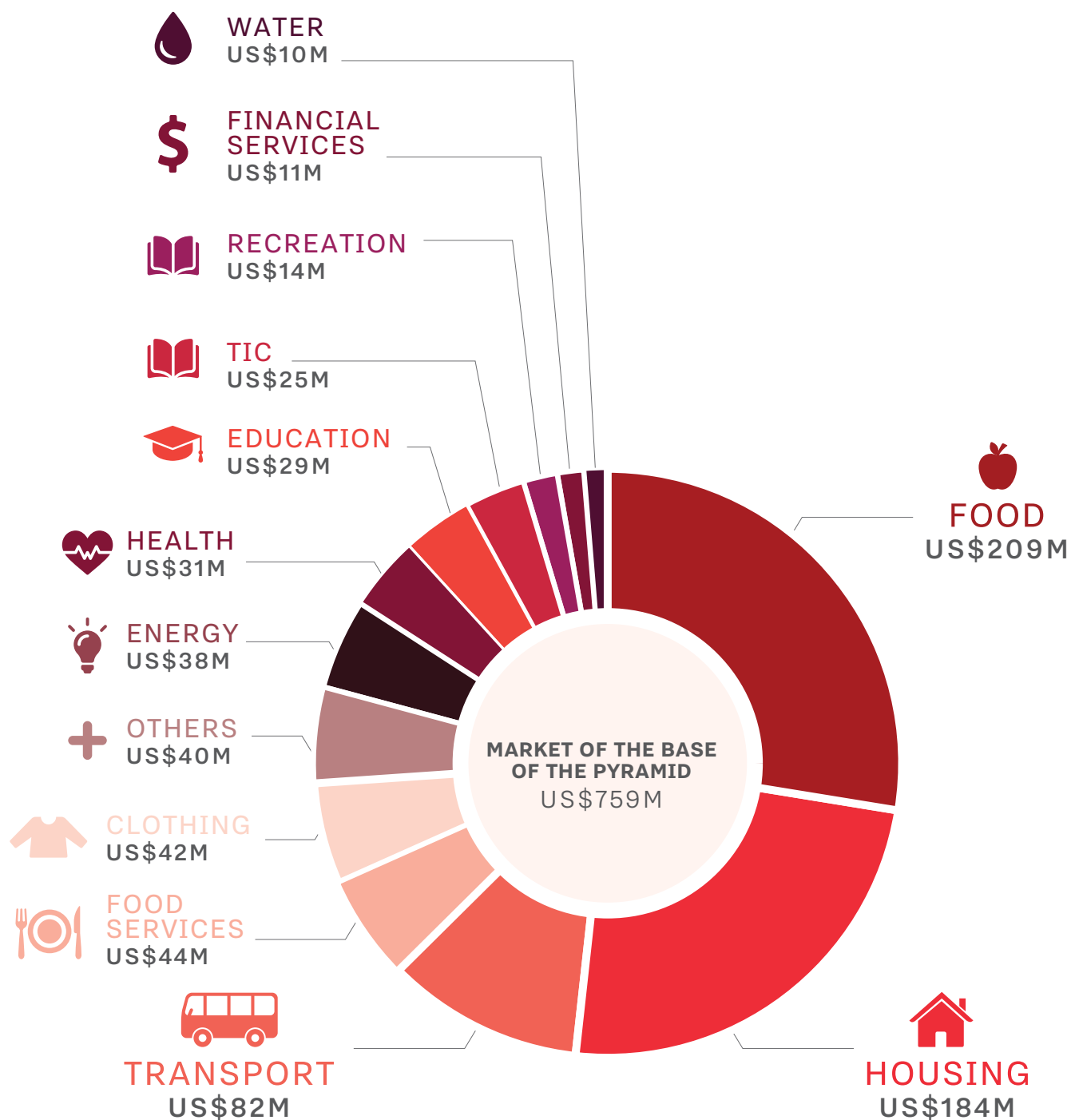
⁸ Silva, A. of Fundación Emprender Futuro. (2018 May 30). Telephone interview.

⁹ ANDE/LAVCA/LGT Ventures, 2016.

¹⁰ In the region, “poor populations” are defined as those households making US\$4 a day or less, and cannot satisfy their current basic needs. “Vulnerable populations” are those that make ~US\$10 a day and though they can satisfy their current basic needs, they are at high risk - one small event like a car breaking down or getting sick or losing a job - of falling into poverty. (Acevedo, 2015).

¹¹ Acevedo, Viviane M.R, Alejandra Baigun, Cesar Patricio Bouillon Bendia, Duncan Duke and Maria Lourdes Gallardo Montoya. “A Growing Market of US\$750B” InterAmerican Development Bank”

¹² Acevedo, 2015



GRAPHIC 7 Underserved markets (households making \$10 or less) represent 70% of Latin America and the Caribbean and a US\$750B...and they are growing. The region needs companies to serve this growing market. (Acevedo, 2015)

INVESTORS

New public and private sector actors are **becoming more engaged, and new models are evolving that address risks to early-stage investors.**

While risk tolerant investors are still rare in the region, interviewees such as those in Ecuador noted “an increased interest on the part of investors to invest in the development of the country.”¹³ Also, while institutional **risk capital is rare**, funding does exist in the region. Locally, it is typically held by families that are deeply personally invested in a country and want to invest locally. Thus, while institutional funding may be lacking, in small countries, high net worth families represent a powerful lever for catalyzing impact investment in countries like Ecuador. For example, the country’s largest retailer, a family business, has invested in Pacari, one of Ecuador’s most successful fair trade chocolate companies. In addition, new models are being created that address the risks to early stage investment ([see Spotlight Connovo p.52](#))



SPOTLIGHT



Connovo in Mexico | the impact company builder-fund taking risk head-on

Connovo focuses on building education companies in Mexico, specifically, early childhood development and training for employability. Connovo, as a company-builder, becomes part of the companies that it takes on or launches, by taking board seats and working alongside founders to advance the company. Connovo aims to build up to four companies in the next three years, and currently has three in its portfolio. It’s companies need early-stage growth capital, so they tried to launch an early stage fund. They “couldn’t find any LP’s [lead partners or first investors]....The hardest part about attracting people to a new model is...it doesn’t have a name, doesn’t have a team and is focused on impact. Risk, risk, risk!”¹⁴. So the design parameters for Connovo were clear. They had to develop a model that “de-risked” the things that scared investors away.

Connovo pulled from various models to create something that works for them: a holding company providing preferred returns to investors and seed capital to its companies. 1) Like a **holding company**, Connovo holds its portfolio companies within an umbrella entity and offer investors 30% equity in Connovo itself, a board seat and a vote on which companies to build, so they are supporting names, teams, and impact they believe in; 2) Like private equity, **preferred returns**, 100% of Connovo’s profits are paid first to investors up to 1x their original capital investment; 3) **Like a seed capital fund**, Connovo also provides US\$150K in seed capital per company to get the companies started fast, and demonstrate value over 18 months to attract another round of investors. They are diversifying risk across seven companies with the goal of three, ideally four of the companies scaling. **They invite their investors to own 30% of the three companies currently in the company builder**, which helps new investors really understand what impact investing is, and how Connovo and its companies work. As Connovo notes, “We have been more successful with this model. Investors say, ‘I own equity in the umbrella company. I decide what models are the best. I get returns first. I’m diversifying risk between seven companies. Now the package is...more attractive to certain types of investors.’”

The experience of Connovo indicates that, even in Mexico, where the impact investing ecosystem is relatively strong in comparison in the rest of the region, models still need to be adjusted to fit local realities. “Typical models like venture capital funds or traditional company builders, are not matched to underdeveloped economies, and even more so if you’re focused on creating social and environmental impact.”

NETWORKS

Our entrepreneur and investor networks are gaining momentum.

Interviewees have seen a growth in the number of actors in the last several years, creating positive momentum. For example, in Ecuador, our interviewees noted increased involvement of different types of public and private sector actors in different initiatives, of “increased professionalism and knowledge of other actors” in the ecosystem¹⁵, for example, in entrepreneurship and investment with AEI, Crisfe, Innobis, and SENESCYT Banco de Ideas, and in impact entrepreneurship and investment with Fundación Nobis, the Hult Prize and IMPAQTO. Building on this momentum locally and regionally, as one interviewee noted, “we can also promote initiatives to map and identify potential areas of collaboration.”¹⁶

We can attract others to our networks by leveraging our strengths.

Interviewees noted that while there is much to be inspired by us in the region and globally, local actors, of course, need to “adapt models to the realities of our countries,”¹⁷ and we need to leverage our strengths. For example, interviewees noted that strengths of small countries like Ecuador¹⁸ - and in particular the Andean countries - include:



1. Geographic location and environmental biodiversity.

The region’s natural resources and biodiversity is a competitive advantage which lends itself to the creation of unique companies in the impact investing space which promote and ensure environmental sustainability, and can manifest in many different types of companies such as Waku (p. X), InkaMoss (p. Y) and TerraFertil (P. Z).



2. Innovation labs.

“[Ecuador] is compact, but big enough that if you have impact, it’s meaningful.”¹⁹ As another interviewee noted, “in a small market, you can validate ideas and models more quickly to expand into other markets in the region”.²⁰



3. Greenfields investing.

Small markets aren’t crowded like other ecosystems. Investors can find more low-hanging fruit: high value companies that have been overlooked. Also practically, as one investor put it, “it’s relatively easy to see if an entrepreneur is legit, which is harder in more crowded markets.”²¹

¹³ Juna, V. of Crisfe. (2018 July 5). Personal interview.

¹⁴ Ordas, J. of Connovo. (2018 August 3). Telephone interview.

¹⁵ Marriot, L. of AEI. (2018 July 6). Personal interview.

¹⁶ Silva, A. of Fundación Futuro Emprender. (2018 May 30). Telephone interview.

¹⁷ Silva, A. of Fundación Futuro Emprender. (2018 May 30). Telephone interview.

¹⁸ Additional strengths particular to Ecuador mentioned by interviewees included: entrepreneurial spirit, a dollarized economy which decreases currency risk, good infrastructure.

¹⁹ MacCombie, D. of DevEquity. (2018 July 18). Telephone interview.

²⁰ Sierra, F. of Invictum. (2018 June 26). Telephone interview.

²¹ MacCombie, D. of DevEquity. (2018 July 18). Telephone interview.

NETWORKS

We can **highlight stories of success** in high leverage fora.

The above framing of the strengths of frontier markets to build awareness and momentum in countries in the region can be used to attract investment. Success stories need to be highlighted of entrepreneurs and investors in small markets, especially at existing regional and global impact investment fora, such as the Latin American Impact Investment Fora (FLII) in Mexico and in Guatemala, at the Latin American Summit on Impact Investing in Quito (CLIIQ) in Ecuador and at the global Social Capital Markets (SOCAP) meeting in the USA. "Stories of exits need to be told"²² at traditional investment networks, such as the Latin American Association of Venture Capital Association (LAVCA) that raise awareness of impact investing, combat the small market myth and encourage potential investors to take a closer look at frontier markets.

Be smart about **impact investing:** heart and head.

Seasoned impact **investors reminded us to Invest with both heart and head**²³ For the legitimacy of the field, **funders need to “ensure financial rigor”²⁴ while investing for impact.** There is a lot of interest right now in impact investing, and while this is a positive trend, at least some investors worried that new investors are coming in with incorrect assumptions, in particular related to return and levels of social impact.

In many deals, “There is a reason there are not a lot of investors focused on these smaller businesses given the challenging financial returns in this market segment.”²⁵ “For a....traditional investor, the idea of making money and doing good feels like an oxymoron. They tend to put their pure profit maximization head on when making investments. When thinking about doing good, they just put their philanthropic head on and check out.”²⁶

Impact investors really must do both. Impact investing is an important tool in the sustainable development toolkit, but it is investment, which always has some element of risk. As one investor observed, “you expect losses, in some cases,”²⁷ especially in those cases where companies are addressing the most challenging problems with the poorest populations.

As in traditional investment, it is just as important in impact investing for both sides - investors and entrepreneurs - to understand, clearly articulate and align around the investor’s risk tolerance and goals for financial and impact returns.

²² Fernando Cortes, F. of Fundaciona Bolivar Davivienda / Fondo Inversor. (2018 July 16). Telephone interview.

²³ Kyle Westaway of Westaway. (2018 June 6). Telephone interview.

²⁴ Ambrose, R. of Pomona Impact Fund. (2018 April 23). Telephone interview.

²⁵ Milder, B. of Root Capital. (2018 July 12). Telephone interview.

²⁶ Kyle Westaway of Westaway. (2018 June 6). Telephone interview.

²⁷ Ambrose, R. of Pomona Impact Fund. (2018 April 23). Telephone interview.



SPOTLIGHT ■ ■

NESsT in Peru | Global funds with local partners for local impact

NESsT was founded in 1997 and its mission is to empower social enterprises to combat poverty through dignified job creation for the most vulnerable. NESsT raises grants, donations and patient capital and invests in social enterprises to help them validate and grow their business and impact.

To date, NESsT has invested US\$5.8M in 68 enterprises that have improved the lives of more than 196,000 people in Chile, Ecuador and Peru. To scale its work, NESsT has created a loan fund, a LLC in the United States, which is wholly owned by NESsT the non-profit. The fund provides patient debt in the range of US\$50K-US\$500K to companies in Latin America that are not yet ready for commercial loans, plus mentoring and technical assistance for a period of 5-7 years to help a company onto the path to scale.

The US\$20M Loan Fund will invest in 80 enterprises creating 30,000 dignified jobs in the next ten years. NESsT's success is due, in part, to the development of strategic partnerships with philanthropy globally and with experienced loan and investment funds in the Andean region such as local Peruvian financial institutions, and the Grassroots Business Fund.²⁸

We can draw inspiration and learn from existing pioneers locally and regionally.

While impact investing is early stage in most frontier markets, there are early movers in the impact investment space in similar countries in the region that can be learned from, several of which are highlighted in this report. Motivated actors don't need to wait until traditional financial-only investment works in the region.

The field can draw inspiration from those in other countries and use those lessons to innovate locally. Those interested in growing the ecosystem are encouraged to find out more about other initiatives working on early stage finance into high impact companies, such as the Fondo Inversor and AlphaMundi Foundation/ SocialAlpha Investment Fund in Colombia investing regionally, Peru Opportunity Fund in Peru, Root Capital in the United States investing regionally, Sudamerik in Chile, and other pioneers in the space.

²⁸ Etchart, N. of NESsT. (2018 April 12). Telephone interview.

3. WE CAN PROMOTE LEGAL AND REGULATORY INNOVATIONS.

We earlier described five legal barriers raised by our interviewers. Two types of solutions also arose from our interviews: **long term policy change and processes; and short-term**, practical workarounds for today that our interviewees are using in practice.

LONG TERM REGULATORY AND POLICY REFORM

Promote policy to remove barriers to and create incentives for impact investment and entrepreneurship.

Development of relevant policy and regulations would incentivize the creation of impact investment funds in the region over the long term. For example, at the national level, as one interviewee noted “several venture capital funds in Chile, use a line of credit offered by the Chilean government.”²⁹ In Ecuador, The Entrepreneurship Law, shepherded by the the Asociación de Emprendimiento e Innovación (AEI), focuses on removing barriers and creating incentives in four areas: legal framework and process, entrepreneurs support, financing and innovation. In addition to the aforementioned, it is important to consider a reform of the company law that contemplates new types of companies adapted to the current needs of entrepreneurs. Interviewees in Ecuador also proposed **that local governments could have a positive influence on the industry**. “For example, the Guayaquil City Council has introduced a tax deduction - up to 50% off annual municipal taxes for a maximum period of ten years - to electric vehicle factories in Guayaquil.”³⁰ These kinds of policies would promote investment by working on the demand side of capital - supporting the start-up and growth of strong companies with high social and environmental impact.

Leverage existing movements to promote legal structures and regulation that make sense for high impact companies and their investors.

The Abogados B initiative within the B-Corps / Sistema B movement is one example of a global movement that is beginning to address legal and regulatory barriers in specific countries in the region. LexMundi Probono Foundation is a global network of law firms that provides pro bono services to high impact entrepreneurs with staff dedicated to brokering connections between companies and legal experts in their particular jurisdiction. In the United States, Canada, the United Kingdom and Colombia, specific legislation and legal structures have been created for companies with social and environmental impact, such as the Public Benefit Corporation in the USA. These efforts can be leveraged to address specific legal challenges within each country in the region.

SHORT TERM PRACTICAL WORKAROUNDS

Over the long term, the world should be a place where every country has the legal and regulatory frameworks that make it easy to do good through good business, but turning that vision into reality is going to take a while. So what is an entrepreneur or a new impact investor to do right now? Our interviews raised several cases of entrepreneurs and investors who are “hacking the system”, mostly through making it easier and cheaper to establish entities in more entrepreneur and investment friendly environments, such as the USA. We highlight two examples below.

²⁹ Baehr, A. of Sudamerik. (2018 April 20). Telephone

³⁰ Servigón, V of VSC. (2018 May 18). Telephone interview.



SPOTLIGHT

Westaway in the USA | Impact entrepreneur-friendly legal offerings

Several years ago, Kyle Westaway and a few friends started up a social enterprise and found no legal advice that fit their needs. So he started Westaway, a boutique law firm specializing in “lean law” for high impact entrepreneurs. Entrepreneurs often avoid seeking legal advice in the early stage because they see firms as corporate, slow, expensive and with opaque pricing. However, avoiding legal advice can lead to costly mistakes such as not being registered properly, or not understanding the full recurring costs of a particular legal structure. Westaway prides itself on being fast, professional with a personal touch and transparent with its up-front, reasonable flat fees for the most common things an entrepreneur needs to do like incorporate, protect intellectual property, labor contracts, structuring investments, even impact evaluation. In particular, providing upfront flat fees for legal services makes it easier for entrepreneurs to seek appropriate legal advice from the beginning. Unfortunately, in the region, like, for example, “in Ecuador, there are few lawyers oriented to startup needs, not just in knowledge but also in budget.”³¹ However, models such as Westaway can inspire innovations in the legal field to increase the pipeline of entrepreneurs.

Stripe Atlas in the USA | Establishing US entities quickly and easily

As we have seen, companies attempting to grow and raise capital in small markets find few local sources, so may attract foreign investors who prefer or even require investments go into structures they are more familiar with, such as a US LLC. Recognizing the global demand for establishing US business structures, companies like Stripe Atlas allow global, online startups to establish a US business entity in just a couple of days. Their service also includes free templates for common legal needs after company formation, a bank account and debit card, ability to accept payments online in 100+ currencies, and issue stock to founders or a team. Businesses like these facilitate processes that can be overwhelming and time-consuming for an entrepreneur, and quickly and easily remove one complication, at least, to investors that prefer to invest into structures like a U.S. LLC.

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³¹ Alonso, R. of New Ventures. (2018 July 31). Telephone interview.

4. WE CAN LEARN FROM AND APPLY FINANCIAL INNOVATIONS

As Rafael Alonso of New Ventures in Mexico suggested in his interview, *“innovation comes from the outside. We can’t wait for banks to develop innovative financial products for entrepreneurs. We need actors that are close to entrepreneurs and that have access to investors to create that bridge.”*³² Pioneers in financial innovation are using and raising awareness of new structures that exist to meet the needs of innovative, high-impact companies and the investors who seek to support them. We outline just a few of these alternative financial structures relative to their closest equivalent traditional mechanism: alternatives to grants, debt and equity.

GRANTS: examples of alternative structures & models

Grants are suitable for early stage companies at proof of concept stage, but aren’t always structured to ensure funding is well spent, don’t help a company build a financial track record to attract downstream investment, and aren’t recycled to support additional companies. However, alternatives have been developed that address some of these challenges. Two examples are **recoverable grants, and social impact incentives.**



SPOTLIGHT



Topa.uy & IADB in Paraguay | Recoverable Grants.

Topa is addressing the challenge of traffic and access to safe, quality public transportation by developing Paraguay’s first collaborative online platform for users, transport providers (like bus drivers) and the Paraguayan Transit and Transport Information System. Topa offers real time transit information to make public transport safe, easy, quick and pleasant. Topa.uy offers technologically advanced transit stops - with security cameras, a panic/emergency button, real time traffic conditions, bus location and arrival times, free wifi, usb chargers, and buttons for riders with visual or learning disabilities. It also informs what amenities are available on oncoming buses such as wifi, A/C or an onboarding ramp for riders with disabilities. Topa.uy also helps transport companies and the municipal government analyze its data to improve the city’s transit system. Topa, is a promising smart transport / big data tech company with significant social impact in terms of decreasing traffic and increasing safety, efficiency and accessibility of public transport in cities. It seeks to expand to six Latin American countries, but needs financing to do so.

Topa is working with the IADB - MIF to experiment with a recoverable grants as a new instrument to reach high-impact startups. "The recoverable grant works as a risk-sharing mechanism that provides the entrepreneur with...flexibility during the most difficult stages of project development and launch. First, a Minimum Commercial Viability (MCV) level is agreed upfront in terms of accumulated sales or revenues. If the product does not reach such a level within a defined timeframe, then it is deemed unsuccessful and the grant does not need to be reimbursed. If the product however reaches and surpasses the MCV level, the entrepreneur begins repaying the grant gradually and proportionally to its revenues. The reimbursable grant contains a clause that allows the investor to convert the outstanding balances into equity if the company reaches a high level of revenues or receives an equity round."³³ As Oscar Farfan of the IADB recalled, "We are still testing this new mechanism on a few promising companies that are at very early stages of development....These companies do not qualify for traditional sources of financing given their risk level but are developing products that can have a disproportionate impact. The recoverable grant is a viable instrument for such businesses as it helps to share the risks of product launching, limits early dilution for the founders, and still provides an upside for the investor in successful cases."



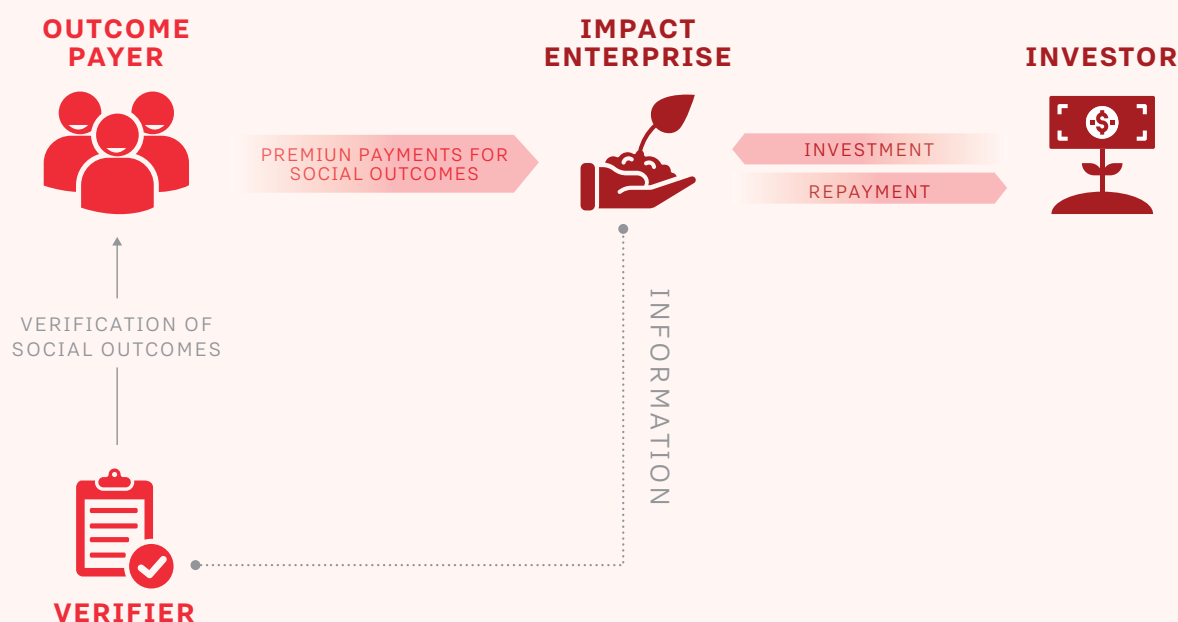
SPOTLIGHT

Roots of Impact & SADC | Social Impact Incentives (SIINC)s

Grantmakers, like governments or foundations, make grants to maximize impact. Investors want to maximize profitability. High impact enterprises want to maximize both, but typically, a company needs to choose: increase impact or increase income? A SIINC helps the entrepreneur choose both. A social impact incentive or SIINC is like a grant in that it rewards a company for its impact performance, but in addition, it also aligns to profitability goals of investors as funding is tied to the enterprise meeting specific impact goals. As the company increases its impact - by, for example, serving poorer customers with health care services, a move that may not be aligned with increasing profitability of the company - they receive SIINC payments or premiums which increase its revenues. A SIINC “boosts the viability of businesses serving the poor by aligning impact with profitability.”³⁴

A SIINC involves three players: **an early stage high impact company with funding needs**, an impact investor (provides loans or investment) **an outcome payer** (a grantmaker) that agrees to pay premiums to the company based on its achievement on predefined social performance indicators. Measurement that the company is meeting its impact indicators that trigger the SIINC payments are verified by a third party. The investor will receive a return based on impact achieved. The premiums received by the company increases its revenues, and, thus, its profitability, becoming more attractive for other investors. Funds are often coupled with financial management training to improve the company’s growth and capacity.

MAKE POSITIVE IMPACT A CHOICE THAT PAYS OFF



BOX 7 SIINC structures include an impact enterprise that needs funding, an outcome payer (a grant funder that provides premiums for social impact achieved), and an investor (providing debt or investment) that is attracted to the investment because of the improved risk/return profile provided by the SIINC funding.³⁵

³² Alonso, R. of New Ventures. (2018 July 31). Telephone interview.

³³ Farfan, O. of IADB. (2018 July 12) Telephone interview.

³⁴ Roots of Impact. Social Impact Incentives (SIINC White Paper). Swiss Agency for Development and Cooperation. September, 2016.

³⁵ Roots of Impact and the Swiss Agency for Development and Cooperation (SADC) Website: <https://www.roots-of-impact.org/siinc/>



In Ecuador, Novulismed is a candidate in the pipeline to receive SIINC funds upon completion of the first milestones of a current technical assistance grant agreement with the IADB-MIF. Novulismed brings quality dental and other health services to underserved workers and their families in Ecuador, by partnering with employers - such as flower growers in the Andean mountains - who facilitate these service for their workers. As Greg Krupa, CEO of Novulis, said “SIINC funds are intended to make your social enterprise more attractive to investors. And for the entrepreneur it is a very attractive mechanism because fund disbursement is linked to pre-established impact goals.”³⁶

Finally, these alternatives to grants, in some cases, better support high impact startups because:



While grants are given away, recoverable grants can be repaid, if the enterprise achieves a certain level of sales or secures additional financing.



Grants don’t necessarily help a company build a financial track record to attract downstream investment, but, for example, **SIINC help the company improve its financial track record by directly linking grant funding as revenue for delivering specific impacts, and involving debt providers or investors in the structuring.**



Early stage risk of the startup is still shared between the company and the grant funder, while enabling the funder some potential “upside” if the company does well and returns the funds, which can then be reused to support other high impact, early stage enterprises.

³⁶ Krupa, G. of Novulismed. (2018 July 5). Personal interview.

DEBT: examples of alternative structures & models

Debt is often impossible for early stage companies to access as they often don't have the minimum revenues, collateral, tangible assets, or ability to repay in periods required by traditional lenders. Alternative debt structures have more flexible repayments, longer time horizons of repayment, grace periods and prepayment discounts that better address the financial needs of early stage companies. Two examples are highlighted below: revenue based financing and loan guarantees.



SPOTLIGHT

Adobe Capital - New Ventures in Mexico | Revenue Financing

Adobe Capital, affiliated with New Ventures is a triple bottom line fund providing growth capital in amounts significantly higher than US\$500K. However, it is currently the only Latin American fund offering alternative financing structures. In 2018, New Ventures is creating another financial mechanism: an open fund providing debt in the amounts of US\$50-US\$150K for impact enterprises in Mexico. This mechanism will use revenue-based debt, where repayments are based on a fixed percentage of revenues, with flexible repayment schedules. In some cases, at the end of the period, there is a conversion equity option for a pre-established percentage. "It is a more viable framework that implies no dilution of shares for owners of the company and has an incorporated exit....For this reason...revenue based lending...[has] such traction, especially in markets where there isn't an equity culture, no venture capital...and no exit alternative."³⁷

Staff at New Ventures agree. "In México, entrepreneurs are so grateful for debt paid with a percentage of sales because it's...easier to legally register and entrepreneurs maintain control of their enterprise."³⁸

Adobe's has extensive experience over six years using revenue-based debt. Its investments are doubly useful as the capital is accompanied by technical assistance. The instrument adjusts to a company's timing and amount of cash flow, and as it requires repayment, funds comes back to support more entrepreneurs and increase overall capital impact. Other examples of investment that do not depend on collateral, but lend based on cash flow, include Variable Payment Obligations (VPOs), currently being tested by Agora Partnerships, Enclude, The Miller Center at Santa Clara University funded by USAID.³⁹

³⁷ Farfan, O. of IADB. (2018 July 12) Telephone interview.

³⁸ Alonso, R. of New Ventures. (2018 July 31). Telephone interview.

³⁹ USAID Partnering to Accelerate Entrepreneurship (PACE): Catalyzing Investment in Latin America. CE and Kohler, J. of Santa Clara University, The Miller Center. "Variable Payment Obligations and Structured Exits". (2018 July 13). Impact Capital Presentation for the Global Social Benefit Institute (GSBI) Accelerator.



SPOTLIGHT

Beneficial Returns in the USA | First-loss, loan guarantees = high leverage

Ted Levinson of Beneficial Returns provides loans of US\$50K - US\$500K for revenue-producing and cost-saving equipment to social enterprise eliminating poverty in Latin America and Southeast Asia. Ted is also on a mission to increase the use of first loss reserves and loan guarantees as one of the easiest, highest leverage instruments donors and investors can use to support high impact enterprises. A loan guarantee is the promise of the guarantor to assume a debt obligation if the borrower defaults. So first of all, because this is a guarantee, and not an actual loan, no money changes hands initially, so the transaction is easy. “You sign this paper and you’re done. The guarantor says to an enterprise, I will offer you a 30% loss guarantee on any investment made into your company, up to, say US\$1M.”⁴⁰

This guarantee, then allows the entrepreneur to more easily attract other investors as the company has effectively been de-risked. First loss capital is a “catalytic credit enhancement tool... [that] can encourage the flow of capital to these [high impact, early stage companies] by improving their risk-return profiles and, thus, incenting others to invest.”⁴¹

What’s even more interesting is the potential leverage. Because with that guaranteed US\$1M for a ⅓ loans loss reserve, an entrepreneur could unlock millions more in funding, and ultimately the guarantor “may only write a US\$200K check, and [as] it might be years until...a loss, in the meantime, whatever money the investor has put aside for the reserve can continue to grow wherever it happens to be.” MCE Social Capital is another fund using the guarantee mechanism in an interesting way for impact in frontier markets.

SPOTLIGHT

Kiva in the USA | Online Crowdlending Platform Many lend to one

Kiva is a U.S. non-profit organization founded in 2005 that provides provides loans to entrepreneurs from vulnerable communities through crowdfunding or collective financing. Kiva’s online platform connects micro-entrepreneurs that would not otherwise be able to access working capital with investors or individuals that provide a small amount of money (US\$25 and up) to help companies on the platform operate and scale.

In the last five years, Kiva has helped impact enterprise in Latin America via strategic partners such as NESsT Peru, which supported InkaMoss in accessing a Kiva loan (see Spotlight page 37). In 2017, Kiva launched an initiative to directly extend interest-free loans to companies without the need for an intermediary. The Ecuadorian chocolate company, Pacari, received a US\$49,925 loan financed by 1549 lenders on the Kiva platform at 0% interest for a period of six months. This direct lending benefits not just the company, but the agricultural families that grow and provide Pacari its high quality as well.

⁴⁰ Levinson, T. of Beneficial Returns. (2018 August 21). Telephone interview.

⁴¹ Global Impact Investing Network (GIIN). Catalytic First Loss Capital. GIIN Issue Brief. October 2015. <https://thegiin.org/assets/documents/pub/CatalyticFirstLossCapital.pdf>

EQUITY: examples of alternative structures & models

The expectations of equity of rapid scale and high returns, such as 3x at a minimum for some impact investors, and clear exit expectations do not often align with realities of early stage companies. As Nathalie Molina Niño, CEO of Brava Investments, states, However, alternatives now exist that, instead of depending on a traditional exit event, such as an acquisition by another company or a public offering, provide investors a structured exit and a liquidation mechanism. These structures can be suitable for early stage impact enterprises that are too small for traditional equity investors.



SPOTLIGHT



NXTP Labs in Argentina | Simple Agreement for Future Equity (SAFE)

A SAFE is an alternative to convertible notes.⁴² Convertible notes have become more complex due to the inclusion of complicated conversion scenarios and features which increases the legal costs and the time spent closing deals. A SAFE, on the other hand, is a more flexible instrument, including a one-document security without numerous terms to negotiate, saving money in legal fees and reducing the time of negotiation of the investment. A SAFE is not a loan, therefore, it will not accrue interest. This is particularly beneficial for startups, that do not have the cash flow to service debt, but also better for some investors, who never intended to be lenders.⁴³

The other advantage of a SAFE, for entrepreneurs is that “it does not appear as a financial obligation unlike convertible debt [that does] appear on your balance sheet as a financial obligation. Moreover, for the investor, it is an agile and simple way to provide financing to entrepreneurs, especially in the early stages where it is difficult, if not impossible, to value your idea so that when someone makes a valuation of the company in subsequent rounds, it can be converted into equity.”⁴⁴

NXTP labs, is a fund that finances and supports innovative technology enterprise to scale in Latin America. It combines finance (principally via SAFES) with enterprise acceleration. “When the future of the startup is uncertain, it isn’t worth investing equity immediately, but to provide the option of obtaining participation in the future, if it meets certain requirements. A SAFE has no expiration date [and] is executed [when]...the startup has a financing event (in general more than US\$500K), or a liquidation event.”⁴⁵

⁴³ <https://www.ycombinator.com/documents/>

⁴⁴ Tetsuro N. of IADB. (2018 July 17). Telephone interview.

⁴⁵ Cruz, M. of NXTP. (2018 July 23). Telephone interview.



SPOTLIGHT



Founderlist in Chile | Online investor syndicate platform, many invest in one

FounderList is an online investment platform for high impact Latin American startups. It has around 500 investors registered, many of which are investment funds, and 4,000 startups registered. Founderlist permits the creation of online groups of investors called syndicates, that group their capital to invest between US\$30K-US\$200K in early stage startups based in Latin America valued at between US\$200K and US\$1.5M. A lead investor within the syndicate takes on the role of “fund manager” and is in charge of selecting the startup into which the group will invest, has a track record of startup investment, is experienced in the industry of the investee, and searches for “backer investors,” that do not necessarily have experience in investment or in startups. This online platform, while not impact-focused, is an interesting model to explore for application in the impact investing space.

While by no means an exhaustive list, hopefully the themes and spotlights we have highlighted from interviews in the region inspire readers to learn more about the innovations one can apply, either in an investor’s next early stage impact investment deal, or in an entrepreneur’s next negotiation with investors interested in the company. However, no matter what financial instruments employed, experts recommend keeping it simple. **Try to make investment documents as simple and standard as possible.** As one intermediary in the design phase of an early stage fund declared, “all the kids get vanilla ice cream.”⁴⁶

For small amounts and small companies, the legal revision for complex terms can become burdensome very quickly, negating the benefit of using these financial mechanisms.⁴⁷

⁴⁶ Hayes, M of Agora Partners. (2018 August 21). Telephone interview.

⁴⁷ Farfan, O. of IADB. (2018 July 12) Telephone interview.

4

CONCLUSION

We believe in the entrepreneurial power and potential of all Latin Americans, those in both large and small population markets.

We know that understanding the challenges we face is key to designing solutions that work, and we face many challenges. But innovations always find a way to come to light. As Buckminster Fuller once said, "You never change things by fighting the existing reality. To change something, build a new model that makes the existing model obsolete."

With this report, we have highlighted those brave individuals and institutions that, despite the inhospitable conditions of many of the markets in which we work, are building a new model for Latin America. We are inspired by those that have transcended the generally held assumptions about small markets and their challenges and found a way to make the system work for high impact entrepreneurs and the investors that seek to support them. And by highlighting their struggles and their successes, through their own words, we hope to promote learning and collaboration amongst those who, like them, also see the opportunities in the challenges around us.

Therefore, no matter who you are, whether an investor interested in taking a leap into impact investing or an entrepreneur looking to attract impact investment, there are actions we all can take, individually, that collectively will create the change locally that is needed to move the right kind of funding into companies solving our world's biggest challenges.

In conclusion, there are more than enough challenges to be solved. But the building blocks and examples exist to experiment with potential solutions. Whether you are an entrepreneur or an investor, a public servant or a titan of industry, we all can play a role. Think big. Leverage the momentum of a growing movement. Learn from others. Promote regulatory reform. Experiment with financial innovations. We each can take individual actions that, collectively, will get the right kind of funding into companies that are solving our world's biggest challenges.

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