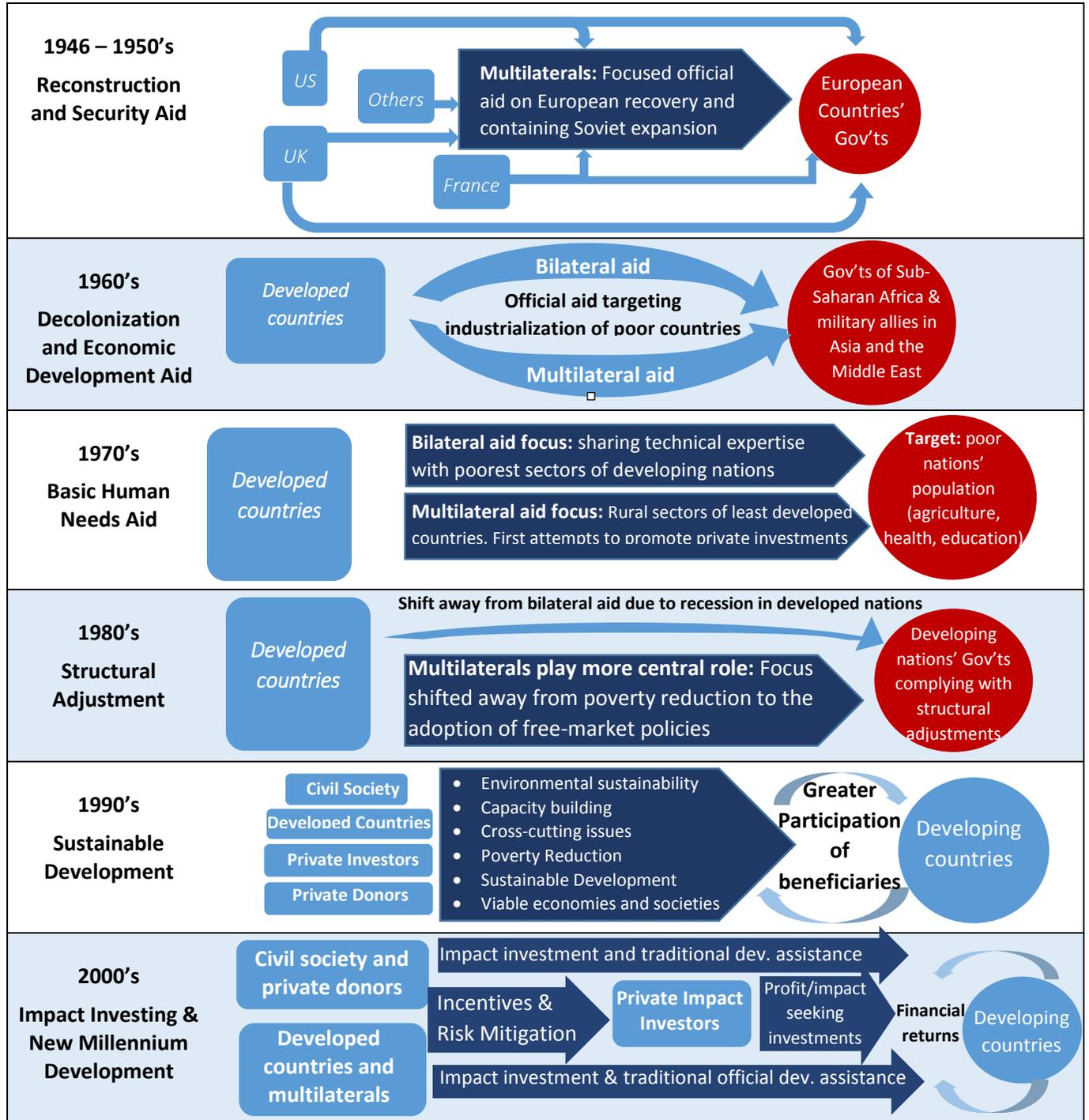


## Chapter 1. THE INTERSECTION OF IMPACT INVESTING AND INTERNATIONAL DEVELOPMENT

As sustainability and scalability continue to gain precedence in the context of international development, impact investing has become particularly well positioned to deliver solutions to some of the toughest, cross-cutting socioeconomic challenges facing developing countries across the globe.

In this section, we explore the potential and challenges associated with leveraging impact investing as a catalyst for international development. We begin by offering a visual review of the post-war transformation of international development, leading to the current focus on market-driven development solutions. We provide an overview of the key players in impact investing as well as a comparison with other international development mechanisms. This leads to a video-based exhibit on some of the current thought leaders in the field of international development and the points of view that are shaping the debate, followed by an analysis of the most important challenges that impact investing faces in the international development arena. Finally, we introduce some of the most innovative and successful initiatives that the field has seen in the last few years and we identify some of the leading organizations in international development and impact investing.

1. The Post-War Evolution of International Development Financing



## 2. Key Players in Impact Investing for International Development

KEY PLAYERS	ROLE
<b>Government/ Regulators</b>	<ul style="list-style-type: none"> <li>• Establish regulations that both protect consumers (especially within vulnerable sectors of society) and encourage investment and innovation</li> <li>• Promote and protect fair and strong competition</li> <li>• Maintain strong diplomatic relationships with other governments</li> <li>• Foster entrepreneurship</li> <li>• Ensure political stability and access to robust infrastructure</li> </ul>
<b>Practitioners (fund managers, investors, entrepreneurs, advisors)</b>	<ul style="list-style-type: none"> <li>• Identify opportunities for impact investing</li> <li>• Generate and circulate data and information on the financial and social performance of impact investments</li> <li>• Identify and disseminate best practices</li> <li>• Shape and define the language and meaning of impact investment</li> <li>• Scale up impact investing models and capabilities</li> </ul>
<b>Corporations</b>	<ul style="list-style-type: none"> <li>• Incorporate impacting investing models in their corporate social responsibility programs</li> <li>• Contribute to the scalability of proven impact investments by serving as later-stage investors</li> <li>• Leverage their technology and expertise to lead entrepreneurial initiatives that target development challenges</li> </ul>
<b>Accelerators (philanthropists, non-profits, and specialized gov't agencies)</b>	<ul style="list-style-type: none"> <li>• Provide business development support to early-stage social enterprises</li> <li>• Connect social entrepreneurs with investors</li> <li>• Often provide direct early-stage funding</li> <li>• Develop partnerships with commercial and impact investors, governments, corporations, and other key players.</li> </ul>
<b>Development Finance Institutions</b>	<ul style="list-style-type: none"> <li>• Provide seed funds for social entrepreneurship as well as larger scale growth capital</li> <li>• Offer technical assistance to social entrepreneurs</li> <li>• Support host governments in the creation of impact investment ecosystems</li> <li>• Contribute to the development of industry-specific infrastructure</li> </ul>
<b>Private Banks</b>	<ul style="list-style-type: none"> <li>• Enable the scaling of social enterprises that have proven financially sound and, potentially, drive large transactions for high-risk, high-impact investment.</li> <li>• Incorporate impact investing as part of their sustainability and corporate social responsibility efforts.</li> </ul>

### 3. Differences between Foreign Direct Investment, Development Aid, and Impact Investing

Foreign Direct Investment (FDI), Official Development Assistance (ODA), and Impact Investment are all mechanisms that promote international economic development. However, there are important differences between these three mechanisms that international development policymakers and practitioners should understand and take into account when designing and implementing development initiatives.

#### Official Development Assistance (ODA):

- **The source** of ODA are the governments of industrialized nations
- **The objective** is to support development initiatives in poor and emerging countries, fund basic needs such as education, health and security, and contribute to long term economic development and the eradication of poverty
- **Takes the form of** money and technical assistance. According to the Organization for Economic Co-operation and Development (OECD), ODA must be concessional in character and convey a grant element of at least 25 percent.<sup>1</sup>

#### Foreign Direct Investment (FDI):

- **The source** of FDI are private companies from developed countries
- **The objective** of FDI is to profit from the growth opportunities, natural resources, new markets, and low production costs that developing countries offer
- **Takes the form of** capital, infrastructure development, human resources, and skill transfers. “The investing company may make its overseas investment in a number of ways—either by setting up a subsidiary or associate company in a foreign country, by acquiring shares of an overseas company, or through a merger or joint venture”<sup>2</sup>

#### Impact Investing:

- **The source** of impact investment funds includes commercial banks, individual investors, entrepreneurs, non-profits, foundations, governments, corporations, and development finance institutions.
- **The objective** of impact investing is to generate financial returns as well as positive social impact on a broad range of socioeconomic sectors including energy, healthcare, housing, water, etc. International impact investments tend to flow to regions that attract more ODA but less FDI.<sup>3</sup>
- **Takes the form of** loans or equity to finance high impact businesses. Early stage social enterprises also benefit from grants, seed capital, and technical assistance from foundations, philanthropists, governments, and development finance institutions.

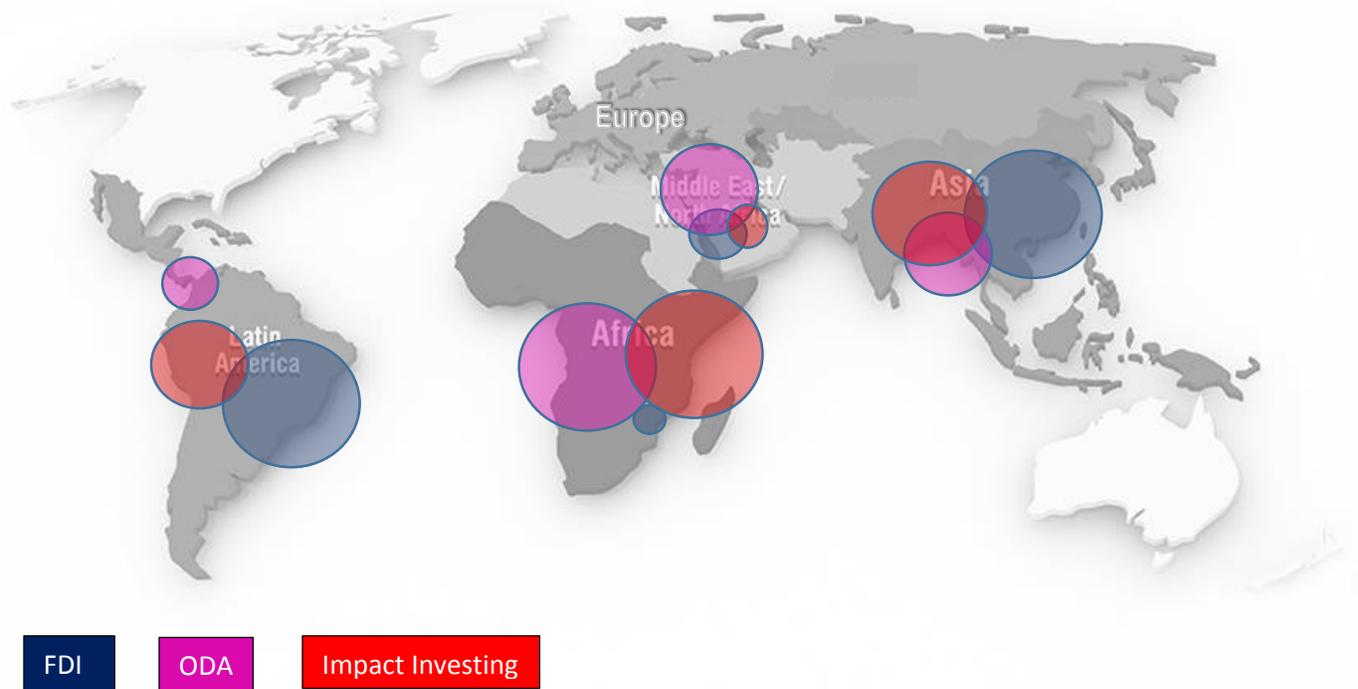
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<sup>1</sup> [www.oecd.org](http://www.oecd.org) (2013). *Official development assistance—definition and coverage*. Retrieved on Sunday, November 30, 013 from [www.oecd.org/dac/stats/officialdevelopmentassistancedefinitionandcoverage.htm](http://www.oecd.org/dac/stats/officialdevelopmentassistancedefinitionandcoverage.htm).

<sup>2</sup> [www.investopedia.com](http://www.investopedia.com) (2013). *Foreign Direct Investment—FDI*. Retrieved on Sunday, November 30, 013 from [www.investopedia.com/terms/f/fdi.asp](http://www.investopedia.com/terms/f/fdi.asp)

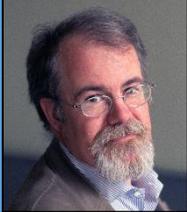
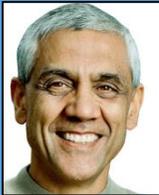
<sup>3</sup> Simon, John and Julia Barmeier. *More than Money: Impact Investing for Development*. Center for Global Development. 2009.

**General flow trends of Official Development Assistance (ODA), Foreign Direct Investment (FDI), and Impact Investing:**



<sup>1</sup> Based on the research results of the Center for Global Development as presented in "More than Money: Impact Investing for Development" by John Simon and Julia Barmeier (2010).

#### 4. Different Perspectives on Foreign Aid and Investing

WHO?	PERSPECTIVES/VIDEO	MORE INFO/QUESTIONS TO CONSIDER
<p>Jeffrey Sachs</p> 	<p><a href="#">Jeffrey Sachs on CBC</a> (2009, 9:52)</p> <p>- Sachs is a proponent of collaborative foreign aid programs and advocates for increasing foreign aid commitments.</p>	<ul style="list-style-type: none"> <li>- What are some of the foreign aid successes Sachs references?</li> <li>- According to Sachs, what is the main problem as to why problems in Africa persist?</li> </ul>
<p>William Easterly</p> 	<p><a href="#">Authors@Google: William Easterly</a> (2006, 56:42)</p> <p>- Easterly opposes Sachs view on foreign aid. He advocates for more feedback and accountability in foreign aid programs.</p>	<ul style="list-style-type: none"> <li>- What are the two tragedies of the world's poor?</li> <li>- What is the "scandal of our generation"?</li> <li>- Explain Easterly's idea of "lack of CIAO" in international aid</li> <li>- What is the basic philosophy of those that back the "planners"? And those that back the "searchers"?</li> </ul>
<p>Dambisa Moyo</p> 	<p><a href="#">On why aid to Africa has been a disaster</a> (2010, 27:13)</p> <p>- Moyo claims that foreign aid creates perverse incentives and does more harm than good.</p>	<ul style="list-style-type: none"> <li>- How did the concept of foreign aid begin?</li> <li>- What is the "reverse Boston Tea Party"?</li> <li>- Why do you think South Africa and Botswana have turned down foreign aid?</li> <li>- Moyo acknowledges progress on HIV/AIDS thanks to NGOs supplying ARV drugs, but what is the problem she sees with that system?</li> </ul>
<p>Esther Duflo</p> 	<p><a href="#">Social experiments to fight poverty</a> (2010, 17:17)</p> <p>- Duflo advocates for a scientific approach to measuring the value of development programs.</p>	<ul style="list-style-type: none"> <li>- What is a randomized controlled trial (RCT)?</li> <li>- What are the pros and cons of RCTs?</li> <li><a href="#">Duflo's Radical Anti-Poverty Fight</a> (7:20)</li> <li>- What is Duflo's view on the debate between Sachs and Easterly?</li> <li>- What is Duflo's view on microcredit?</li> </ul>
<p>Vinod Khosla</p> 	<p><a href="#">Khosla on Green Investing</a> (2007, starts @ 6:35)</p> <p>- Khosla, billionaire venture capitalist, insists capitalism is and should be the key driver of social change.</p>	<p>Watch more: <a href="#">Black Swans in Energy</a> (3:26)</p> <ul style="list-style-type: none"> <li>- How does he see transformative change happening in the world?</li> </ul> <p>Audio: <a href="#">The Black Swans of Energy Invention</a> (58:13) - start @ 18:15</p> <ul style="list-style-type: none"> <li>- What are some ways "black swans" could spur development? Why microcredit as a black swan?</li> <li>- How do his ideas parallel w/the evolution concept of "punctuated equilibrium?"</li> </ul>
<p>Ha-Joon Chang</p> 	<p><a href="#">On Free Markets</a> (2:09)</p> <p><a href="#">On Trickle Down Economics</a> (1:58)</p> <p><a href="#">On Free Trade</a> (3:29)</p> <p>- Chang advocates for interventionist policies to help countries develop.</p>	<ul style="list-style-type: none"> <li>- What does Chang posit about the development of the U.S. and other developed countries?</li> <li>- What is the hypocrisy that he implies regarding developed nations treatment of developing nations?</li> </ul>

## 5. Potential Challenges in International Impact Investing

CHALLENGES	SOLUTIONS IN PROGRESS	MORE TO READ/WATCH
<p><b>Establishing effective cross-sector partnerships.</b> Across sectors there are different types of actors including governments, development agencies, private companies, NGOs, foundations, and banks—all with different structures, policies, and incentives. Subjectivity in investors' goals creates challenges for collaborating and deciding what is most important to invest in.<sup>4</sup></p>	<ul style="list-style-type: none"> <li>- <a href="#">CGAP</a> and <a href="#">CFSI</a> provide market intelligence and advisory services to governments, financial service providers, donors, and investors.<sup>4</sup></li> <li>- <a href="#">The Impact Investing Policy Collaborative (IIPC)</a> is building a network of stakeholders and helping identify and support policies improve impact investing markets.</li> </ul>	<p><a href="#">Impact Investing 2.0: Policy Symbiosis</a></p> <ul style="list-style-type: none"> <li>- How can investors effectively collaborate with governments?</li> </ul> <p><a href="#">The Systemic Barriers of Impact Investing – Will the Sector Fail to Keep its Promises?</a></p> <ul style="list-style-type: none"> <li>- What specifically is lacking in order to create effective collaboration within impact investing?</li> </ul>
<p><b>Governance problems.</b> Investors must navigate policies of local governments. There may be uncertainties around property rights or contracts, for example, that require local expertise that is hard for investors to find.</p>	<ul style="list-style-type: none"> <li>- Many public-private partnerships (PPPs) are successfully creating positive impact economies. Read about Manila Water—a successful PPP <a href="#">HERE</a>.</li> </ul>	<p><a href="#">Priming The Pump, p. 20 – V. Government Matters</a></p> <ul style="list-style-type: none"> <li>- Where are governments facilitating impact investing around the world?</li> <li>- How are they doing it?</li> </ul>
<p><b>Risk tolerance of investment firms.</b> Different institutions have different levels of risk tolerance. Risk is generally higher when working in emerging markets. Risks may include: political instability, economic instability, corruption, natural disasters, and conflict.</p>	<ul style="list-style-type: none"> <li>- <a href="#">OPIC</a> provides financing, political risk insurance and support for private equity investment funds</li> <li>- USAID provides loan guarantees to encourage banks in poor countries to lend to targeted groups. Learn about DCA program and watch video <a href="#">HERE</a>.</li> </ul>	<p>2 Microfinance Crises in Nicaragua and India: What were the causes and what can we learn?</p> <ul style="list-style-type: none"> <li>- <a href="#">Nicaragua's Microfinance Crisis: Looking Back, What Did We Learn? (2011)</a></li> <li>- <a href="#">Andhra Pradesh 2010: Global Implications of the Crisis in Indian Microfinance</a></li> </ul>
<p><b>Working in informal markets.</b> At the base of the economic pyramid there are either no functioning markets or very informal markets with informal workforces. To attain success, it is crucial for investors to understand these environments.</p>	<p><a href="#">Segmenting the Base of the Pyramid</a></p> <ul style="list-style-type: none"> <li>- How have some companies found success in creating commercial and social value at each segment at the base of the pyramid?</li> </ul>	<p><a href="#">Financial-first Impact Investing</a></p> <ul style="list-style-type: none"> <li>- What is the contradiction in impact investing literature identified by the authors?</li> <li>- According to the authors, where is it impractical for return-oriented impact investors to invest?</li> </ul>
<p><b>Measuring impact.</b> Measuring impact is particularly difficult in emerging markets.</p>	<p>Initiatives building infrastructure to measure impact:</p> <p><a href="#">GIIRS</a>, <a href="#">IRIS</a>, <a href="#">SROI Network</a></p>	<p><a href="#">Unpacking the Impact in Impact Investing</a></p> <ul style="list-style-type: none"> <li>- What is <i>additionality</i> and <i>counterfactual analysis</i>?</li> <li>- What are the 3 parameters of impact and ways to measure each?</li> </ul>

<sup>4</sup>Born, Kelly and Paul Brest. *Unpacking the Impact in Impact Investing*. Stanford Social Innovation Review. 2013. Retrieved on Sunday, December 1, 2013 from [http://www.ssireview.org/articles/entry/unpacking\\_the\\_impact\\_in\\_impact\\_investing](http://www.ssireview.org/articles/entry/unpacking_the_impact_in_impact_investing).

## 6. Unorthodox Innovations: the Black Swans in Economic Development

Nassim Nicholas Taleb, a famed essayist and statistician, focuses his work on problems of randomness, uncertainty and probability. He developed the concept of the Black Swan which refers to the rare, unforeseen, random and improbable events that have significant historical consequences. This theory can be applied to innovative advances in economic development that have had high social and financial impacts. But first, listen to Professor Taleb's brief overview on the concept: [What is a "Black Swan"?](#)

### Black Swans in International Development (examples)

1. **Micro-credit:** Refers to the extension of small loans (microloans) to borrowers who would otherwise be unable to borrow money from a bank due to their lack of credit history, steady employment or collateral. The concept was developed by Muhammad Yunus who started Grameen Bank in 1976 (see below). Microcredit strives to motivate entrepreneurs, bring people out of poverty, and empower women; it has the potential to change entire communities.<sup>5</sup>

**Considered a Black Swan because...** Micro-credit shifted the way people thought about development financing. Traditionally development was structured in the form of aid; microcredit empowered people through self-employment and made them accountable for their success.

- **Micro-credit beginnings:** [Grameen Bank](#), Bangladesh
- **Micro-credit challenges:** [Access, capacity building, regulations](#)
- **Micro-credit innovations:** [Janalakshmi](#), India

2. **Treadle pumps:** a [treadle pump](#) is a human-powered irrigation device positioned on top of a well; it is activated by pumping one's foot up and down on the treadle to draw groundwater to the surface. A treadle pump frees farmers from dependence on rain for irrigation.

**Considered a Black Swan because...** Treadle pumps have increased the labor productivity of farmers and enabled them to step out of subsistence farming. With the pumps, farmers can produce more crops which they can use to sell in order to make an income.

- [iDE](#) has popularized treadle pump technology in Bangladesh through focused value chain and social marketing interventions - 84 manufacturers now produce treadle pumps and 1.4 million treadle pumps have been sold to small plot Bangladeshi farmers since 1985. Success in [Zambia](#) has brought farmers out of subsistence farming.

3. **Satellite Technology used to track rainforest deforestation** is providing people with a way to accurately monitor the destruction of forest in Latin America and detect the towns or other protected areas that are affected by deforestation.

**Considered a Black Swan because...** satellite systems can now monitor deforestation in real time. Having a visual image of forest loss is much more impactful than hearing statistics; it brings heightened awareness of illegal deforestation leading people to change the way they do business.<sup>6</sup>

- USAID has partnered with the Skoll Foundation to launch the [Innovation Investment Alliance](#). Their first investment will be in [Imazon](#), an organization that works with the Brazilian government and farmers to reduce deforestation through satellite technology.

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<sup>5</sup> <http://en.wikipedia.org/wiki/Microcredit>

<sup>6</sup> <http://green.blogs.nytimes.com/2012/06/25/a-new-satellite-tool-tracks-deforestation/>

## 7 Impact Investing: Success Stories

### **Anudip** – *Investment Decision-Making*

Anudip creates opportunities for impoverished people in rural areas and urban slums of India by bridging the gap between traditional schooling and achieving a sustainable livelihood. Through vertically integrated model of training, job placement, and entrepreneurship, it creates opportunities for communities to improve social and economic conditions on a broader scale. Since beginning operations in 2006, Anudip has trained more than 15,000 students and successfully placed 80% of them in jobs across a variety of sectors.

When deciding whether or not to invest in Anudip, the Omidyar Network (ON) had to consider a number of questions including: Did Anudip have a scalable model? What type of capital should ON commit? How would the deal be structured to measure success? The decision-making process requires in-depth organizational due diligence and extensive review of financial statements. Investors often find the process challenging especially when trying to make from abroad. *Read about how ON came to the decision to invest in Anudip.*

**CASE STUDY:** [Investing in Anudip](#)

#### **INVESTORS:**

- [Omidyar Network](#)
- [Accenture](#)

### **Bridge International Academies** – *Scalable Opportunities*

Bridge International Academies extends access to primary education in Africa, demonstrating the power of for-profit innovation to transform lives. Its mission is *Knowledge for all*. By employing key characteristics of successful franchises, Bridge's vertically integrated *Academy-in-a-Box* approach has reengineered the entire lifecycle of basic education, leveraging data, technology, and scale in order to keep quality up and prices as low as \$5 a month (on average). Investors find Bridge attractive because it offers an alternative solution to education with a likelihood of a financial return.<sup>7</sup>

**CASE STUDY:** [Background, challenges, scalability](#)

#### **INVESTORS:**

- [NEA](#)
- [OMIDYAR NETWORK](#)
- [LearnCapital](#)
- [khosla ventures](#)
- [Pearson Education](#)
- [Mulago Foundation](#)
- [Jasmine Social Investments](#)
- [Deutsche Bank Americas Foundation](#)
- [DOB: equity for Africa](#)

#### **IN THE NEWS**

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<sup>7</sup> <http://www.bridgeinternationalacademies.com/>

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