



Deep Dive: Impact-Linked Finance

Better terms for
better impact

Taskforce Finanzierung Soziale
Innovationen in Deutschland

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17 October 2023



**Roots
of Impact**



What kind of finance do high-impact enterprises need to scale and optimize their impact?

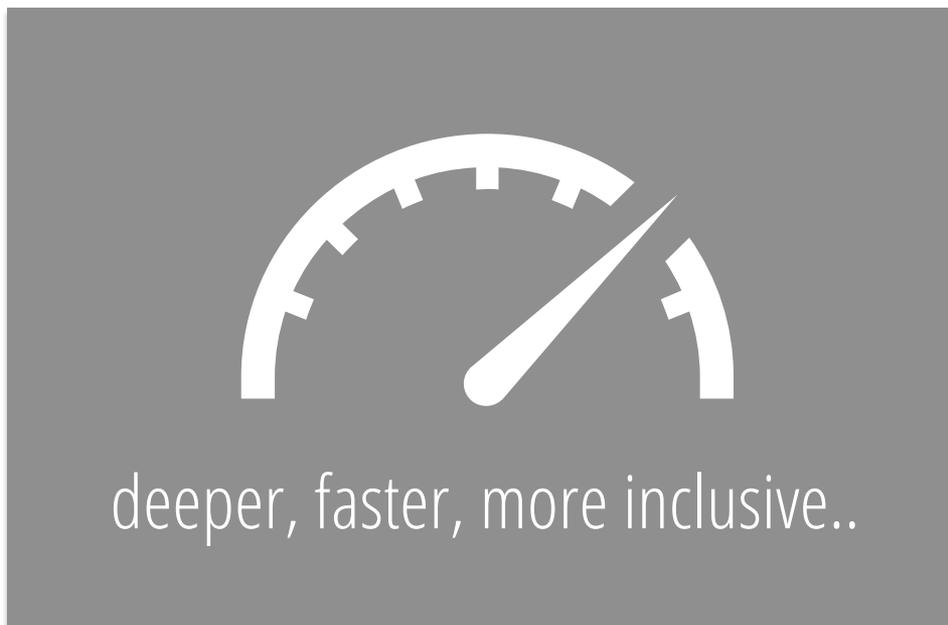


Pictures: Programa Valentina / Novulis



Impact finance can be powerful, but ...

... there are typically no incentives
in place for entrepreneurs and their investors to
optimize for impact





What if social innovators were remunerated for all the value they create?





Impact-Linked Finance is
unleashing the full potential
of impact enterprises by providing
better terms for better impact.





Example: Social Impact Incentives (SIINC)

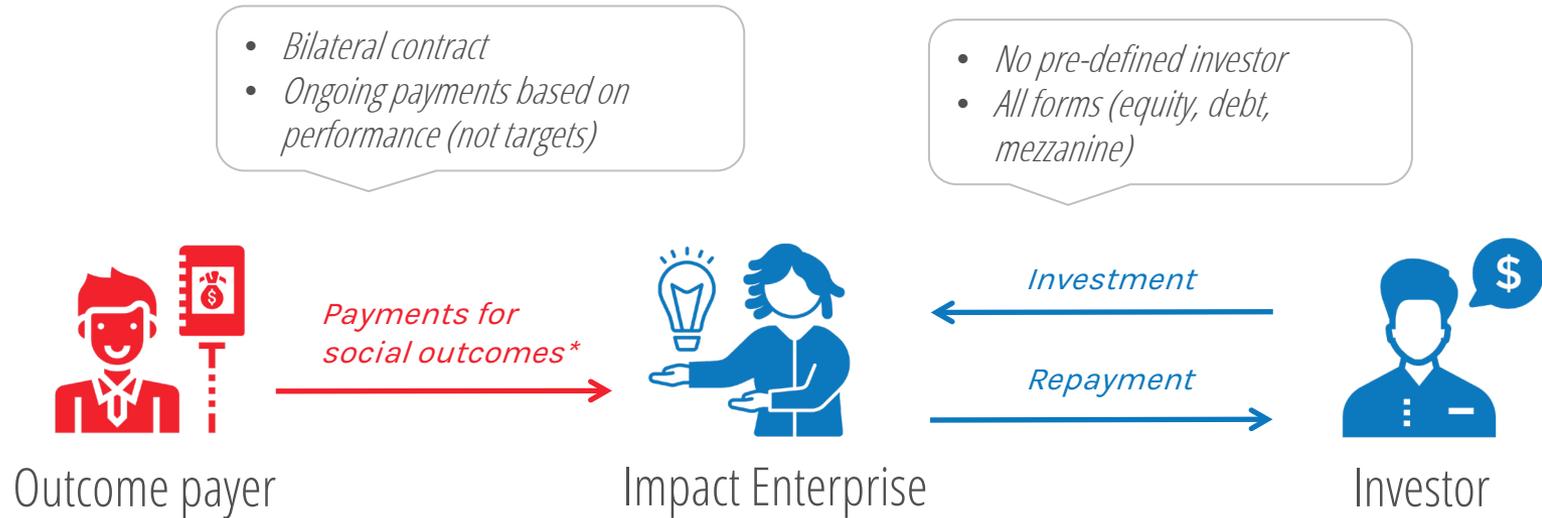


SIINC is a blended finance instrument that provides outcomes-based payments directly to enterprises raising investment.

* upon verification



Example: Social Impact Incentives (SIINC)

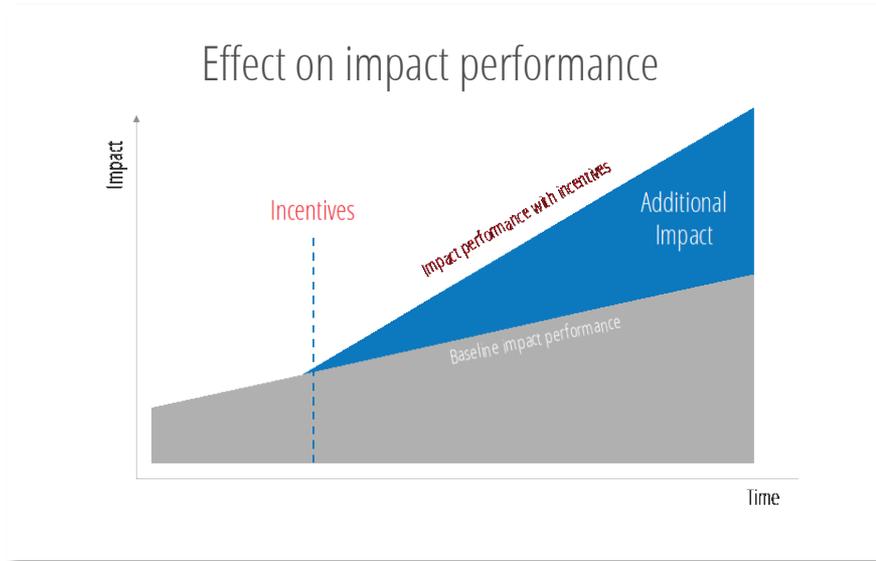


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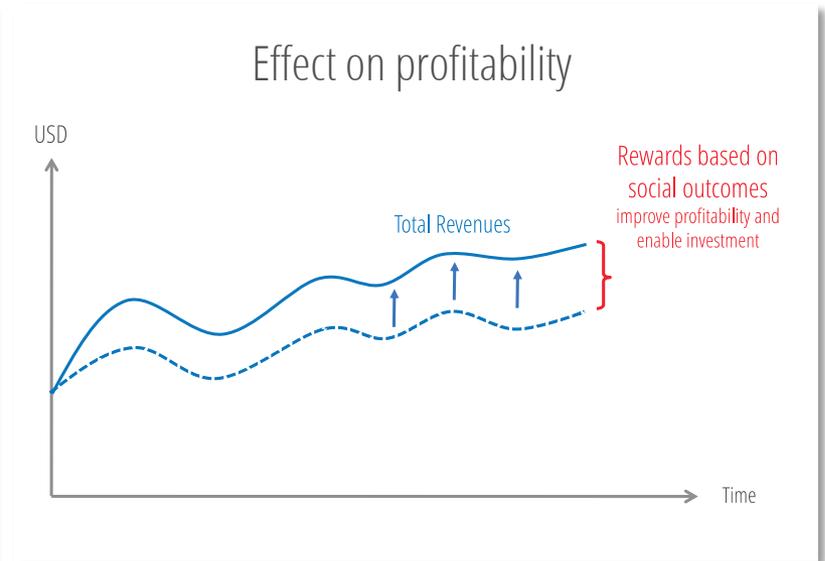
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Effect on profitability and impact performance



Targeted financial rewards deepen and widen positive outcomes...



...while also improving commercial viability and attracting (further) investment



SIINC example: Training and job placement for unemployed youth



1st Metric: # disadvantaged students successfully placed in decent jobs*

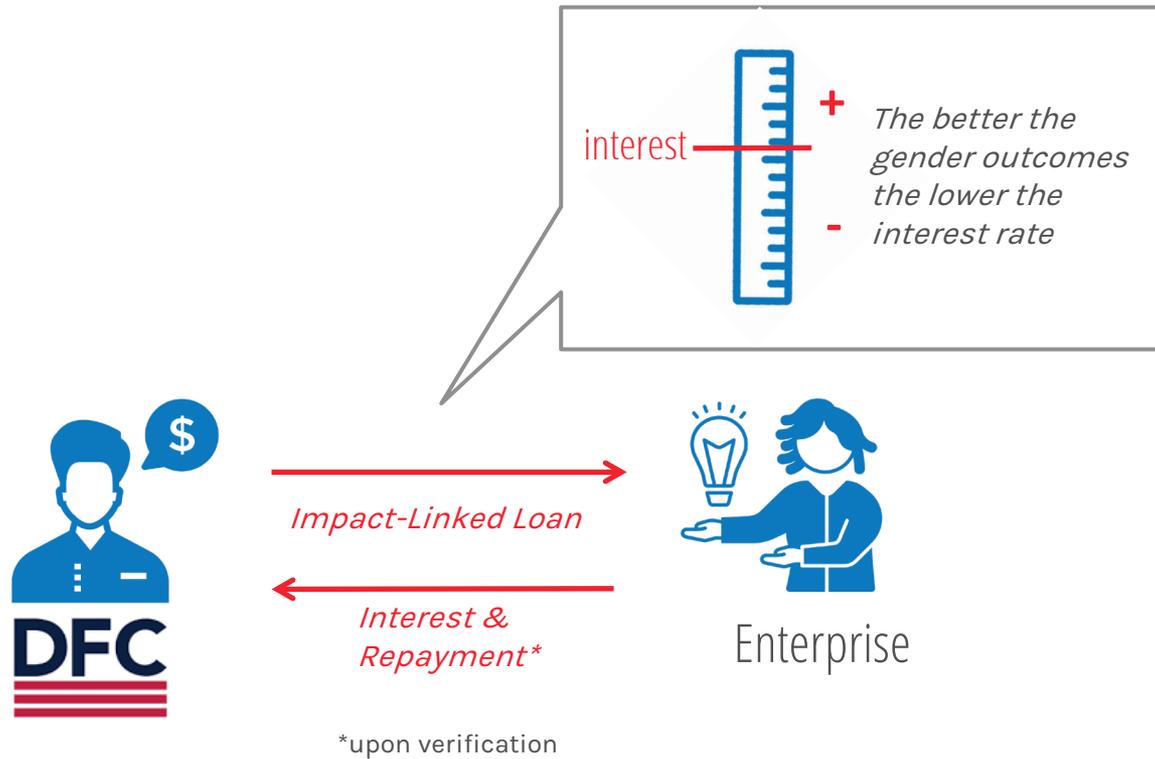


2nd Metric: % placed candidates still employed after 12 months**

* Unemployed youth meeting a pre-defined profile ** or equivalent income-generating activities (e.g. entrepreneurship)



Example: Gender Impact-Linked Loans by DFC



Impact-Linked Loans incorporate rewards in the form of reduced interest rates depending on the achievement of predefined outcomes. DFC focuses on encouraging **better gender outcomes** among their borrowers.



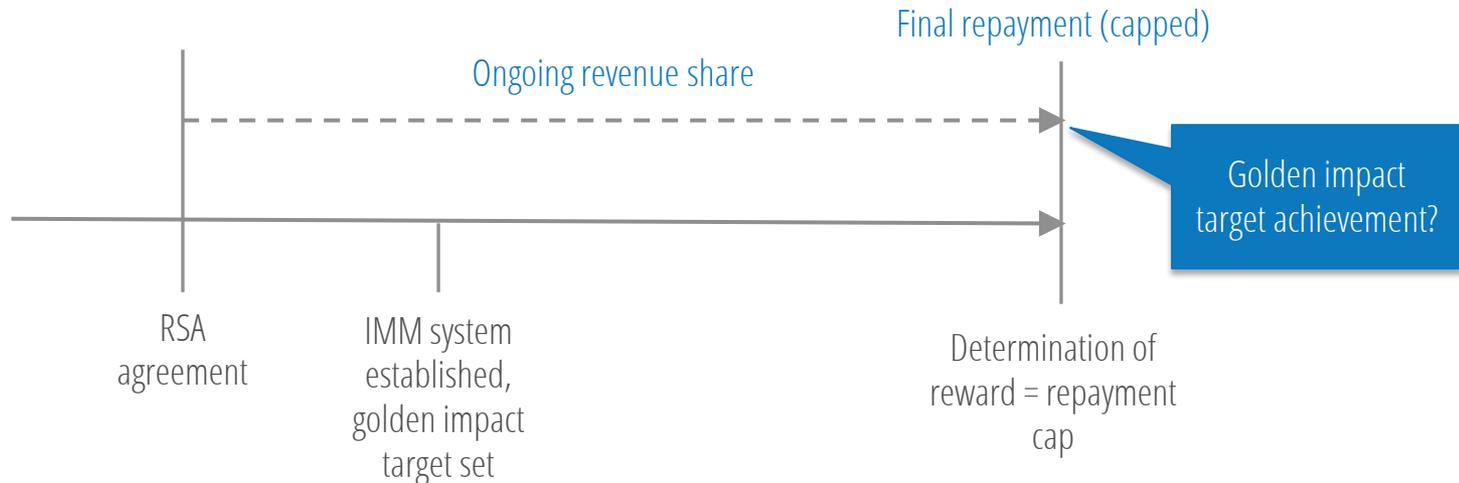
Instruments for impact start-ups and innovators

- **Impact-Ready Matching Fund**
 - Matching private investment 1:1 (capped)
 - Payments linked to milestones for setting up an impact measurement and management system (with quality controls)
- **Impact-Linked Challenge Fund**
 - Selection of supported enterprises based on a competition (challenge fund)
 - One golden impact target
 - Either: (partly) repayment of funding if the impact target is not achieved
 - Or: additional reward for achieving impact target (e.g. 50% premium payment)
- **Impact-Linked Matching Fund**
 - Matching private investment 1:1 (capped)
 - One golden impact target
 - (Partly) repayment of funding if impact target is not achieved

X-Price !



Impact-Linked Revenue Share Agreement (RSA) with impact kicker



Characteristics

- Reduction of repayment cap upon reaching a golden impact target in 5 years (e.g. reduction from 1.8x to 1.3x)
- The enterprise has sufficient time to establish its impact measurement system, which will be used to verify the target achievement (must be accepted by the investor)
- (TA) support for impact measurement and management (IMM)



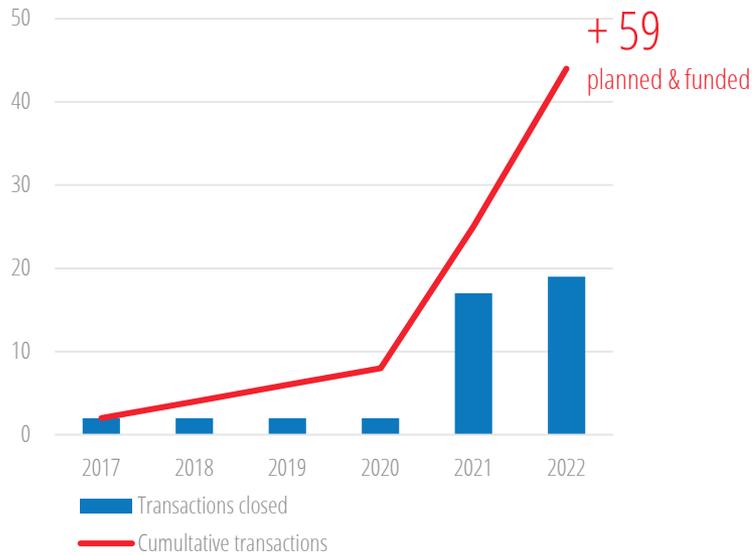
Impact-Linked Finance differs from ...

- ... **Impact Investing**, that seeks positive impact but does not incorporate rewards for achieving it
- ... **Impact Bonds**, that have a strong outcomes-orientation but focus on non-profit interventions
- ... **Carbon Credits**, that are used to monetize a single outcome in a standardized way

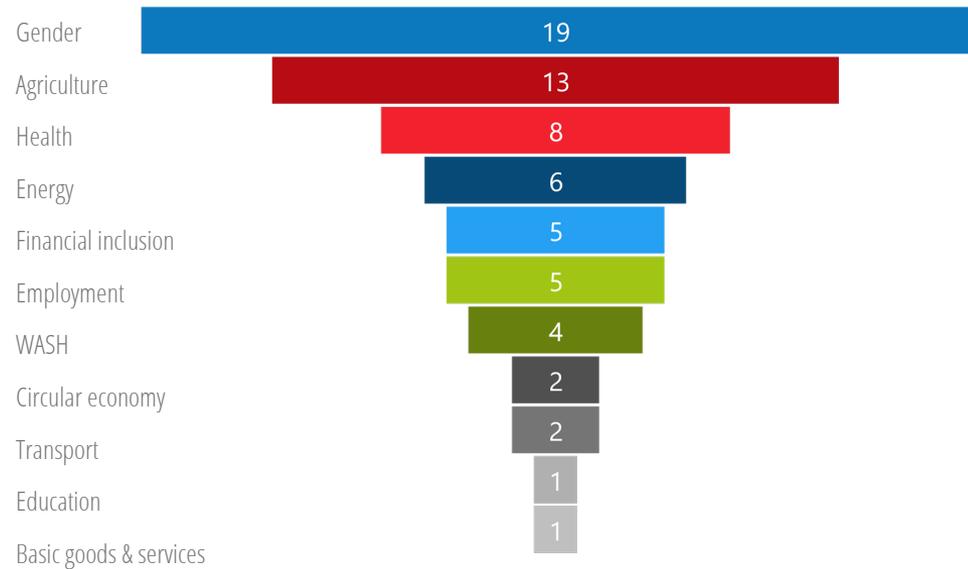


Facts & figures

Number of Impact-Linked Finance transactions by year (44 until end of 2022)



Impact sector focus (on transactions closed until end of 2022, incl. double counts)





Facts and figures

Closed transactions by region
(44 until end of 2022)



Funding partners and collaborators





Impact-Linked Finance has proven to be effective

Independent evaluation examples of our work:



Clínicas del Azúcar: “The SIINC transactions have successfully created additionality.”

Catalyzed growth in the proportion of low-income patients with excellent treatment results. A conservative estimate translates into 4'000 more Bottom-of-the-Pyramid clients each year.



“B-Bridddhi’s Impact-Linked Finance and IMM work is leading-edge in Asia and globally.”

In 2020 and 2021, B-Bridddhi built a portfolio of 15 impact enterprises scaling innovative, tech-enabled business models in a range of sectors



“After just two years, SIINC created measurable impact for [Root Capital](#), its client agri-SMEs, and smallholder farmers.”

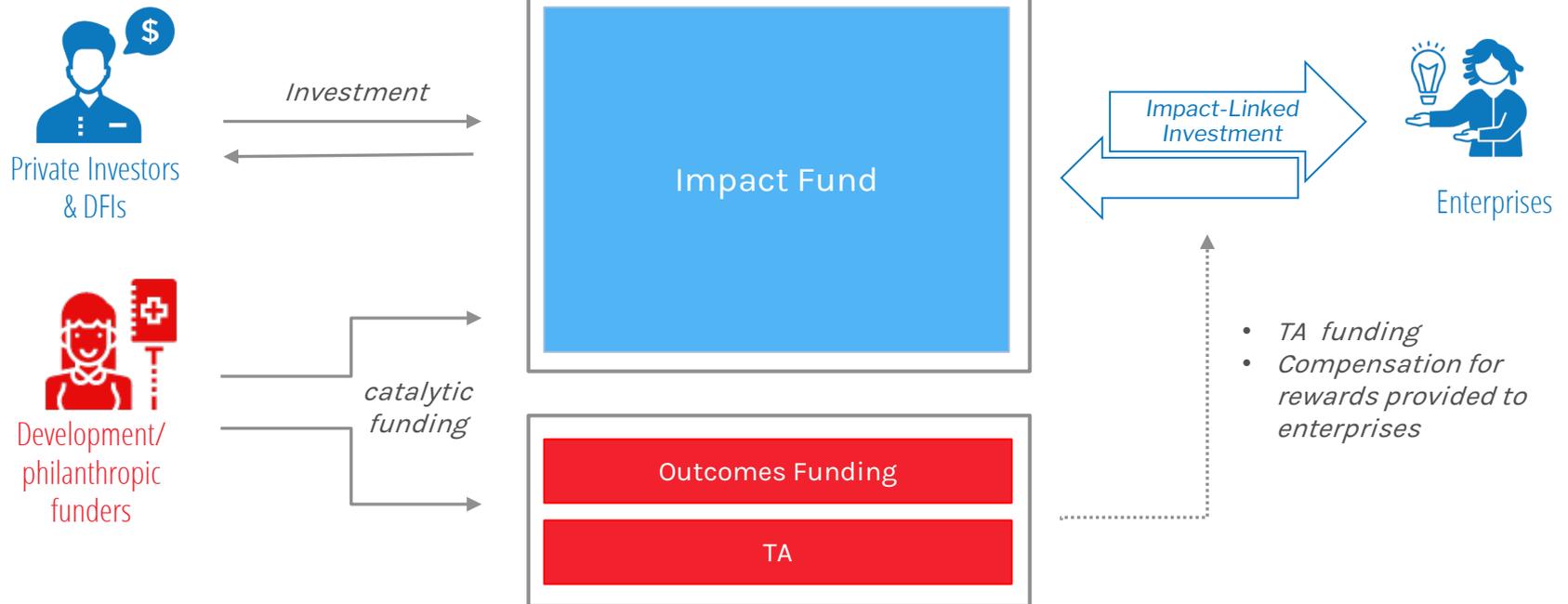
Catalyzed 11.5 million in loans to 32 agricultural businesses reaching about 9000 smallholder farmers

Find more about Roots of Impact's impact and evidence and the individual evaluation report [here](#).



ILF-enhanced funds

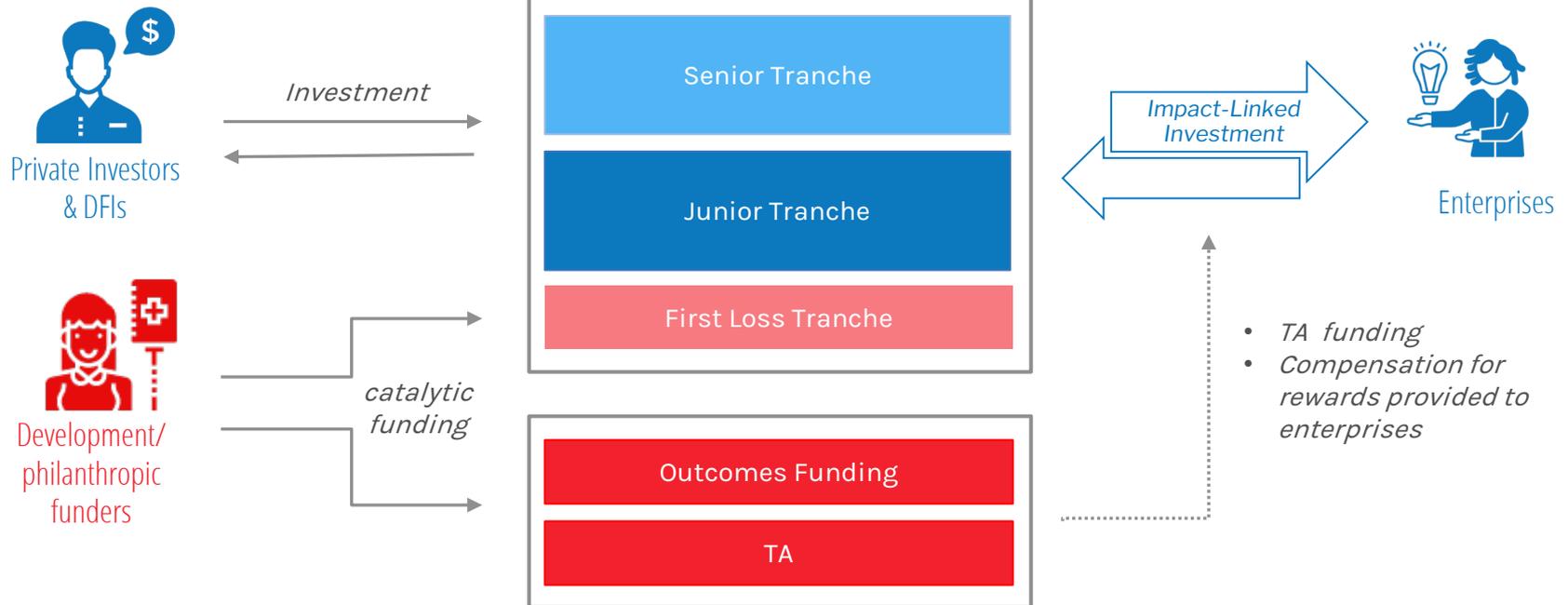
The new normal





ILF-enhanced blended finance fund

The new normal

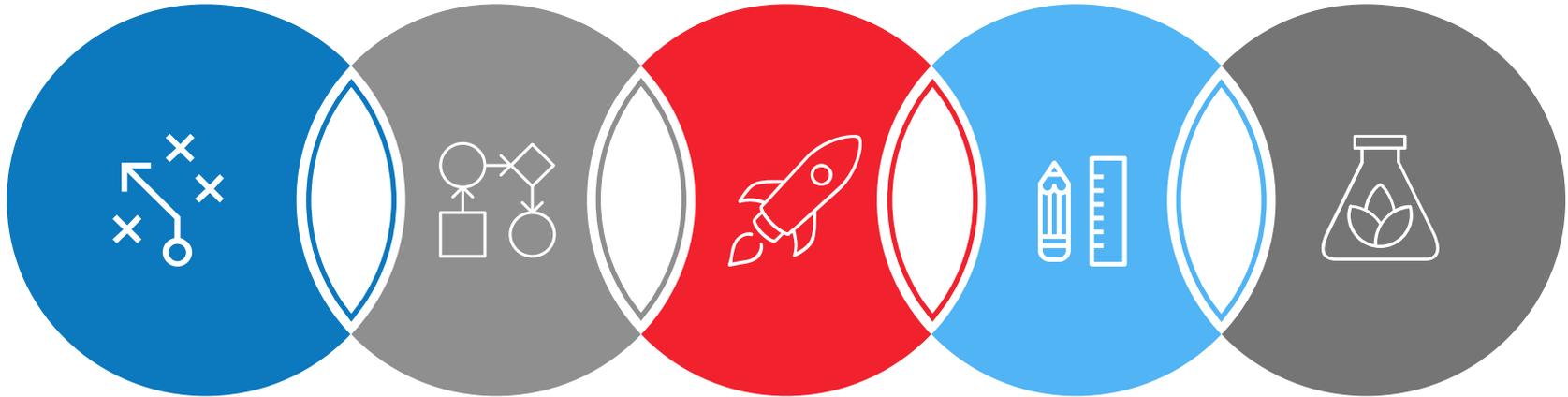


Existing example: Impact-Linked Fund for Gender Inclusive Fintech

Further funds in preparation for off-grid renewable energy, gender and financial inclusion



What have we learned?



Sector- and theme-specific funds enable comparability and learning

Strategic alignment of enterprises to ILF is key

The most effective approach is to unlock the enterprise's untapped potential and enable it to achieve its own objectives sustainably

An appropriate impact measurement system is crucial

Selection and incentive design need to consider sustainability after the "exit"

A young girl is lying on a dental chair, being examined by a dentist wearing full personal protective equipment (PPE), including a blue gown, gloves, a face shield, and a mask. A parent, wearing a pink patterned sweater and a beige knit hat, stands by the girl's side, holding her hand. Another person in a blue gown and gloves is visible in the foreground. The scene is set in a dental clinic with large windows in the background. A sign with the text "Respi" and "Co" is visible on a stand.

We are committed ...

... to unleashing the full impact
potential of high-impact enterprises





Thank you



Appendix



About Roots of Impact

Roots of Impact is a manager of catalytic capital and pioneer in Impact-Linked Finance, enabling fast-scaling impact enterprises to optimize for impact while strengthening their commercial viability.

- Pioneered Social Impact Incentives (SIINC) in partnership with SDC
- Defined the practice of Impact-Linked Finance in partnership with the Boston Consulting Group (BCG)
- Established the Design Principles for Impact-Linked Finance
- Launched the [Impact-Linked Finance Fund](#) in partnership with iGravity
- Closed 44 transactions by end 2022
- Set up three sector-specific Impact-Linked Funds
- Created the [Open Platform](#) for Impact-Linked Finance



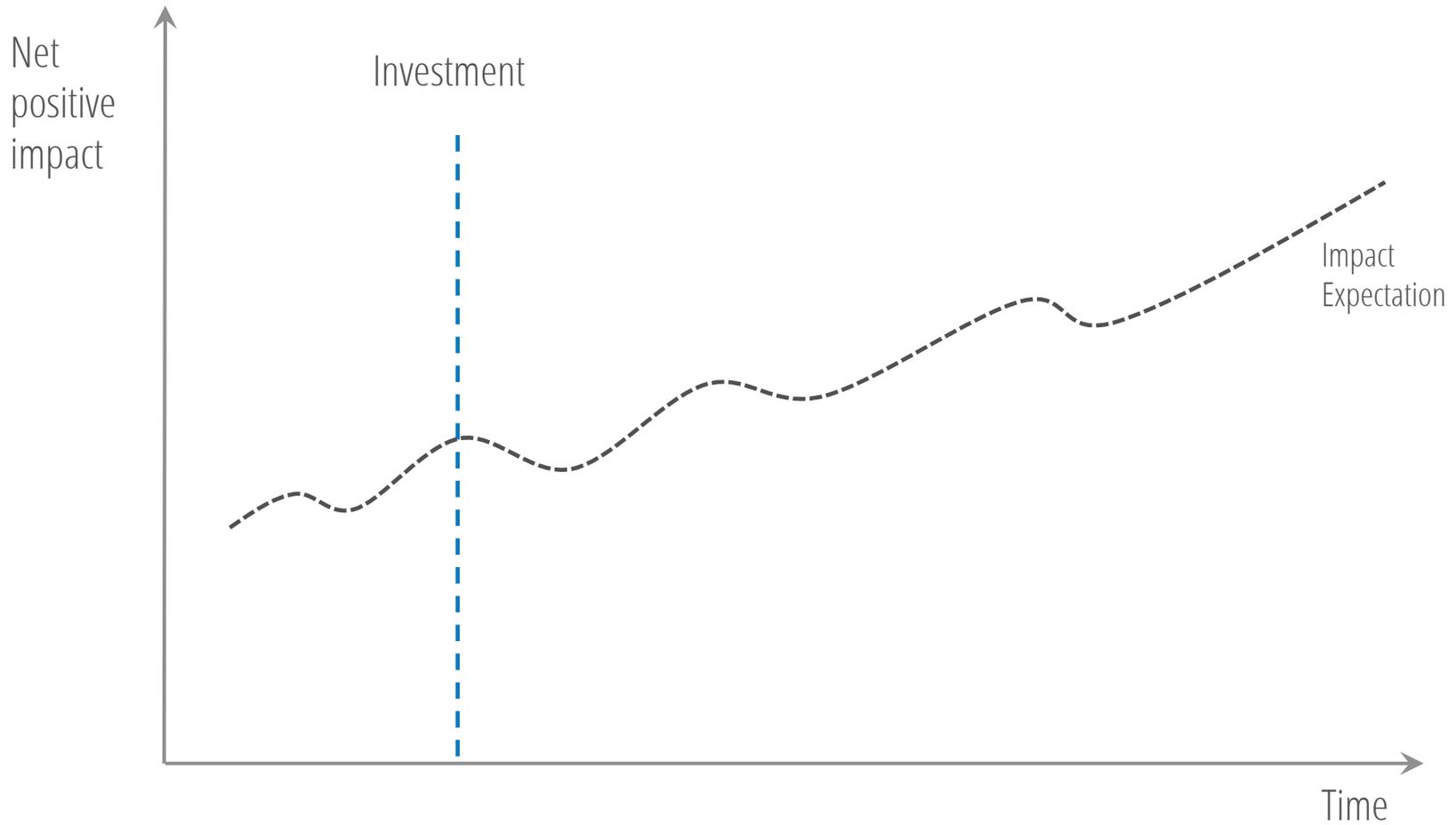
“The key market-builder of impact-linked finance, ... which has most experience of implementing ...”

Investing for Good, 2021



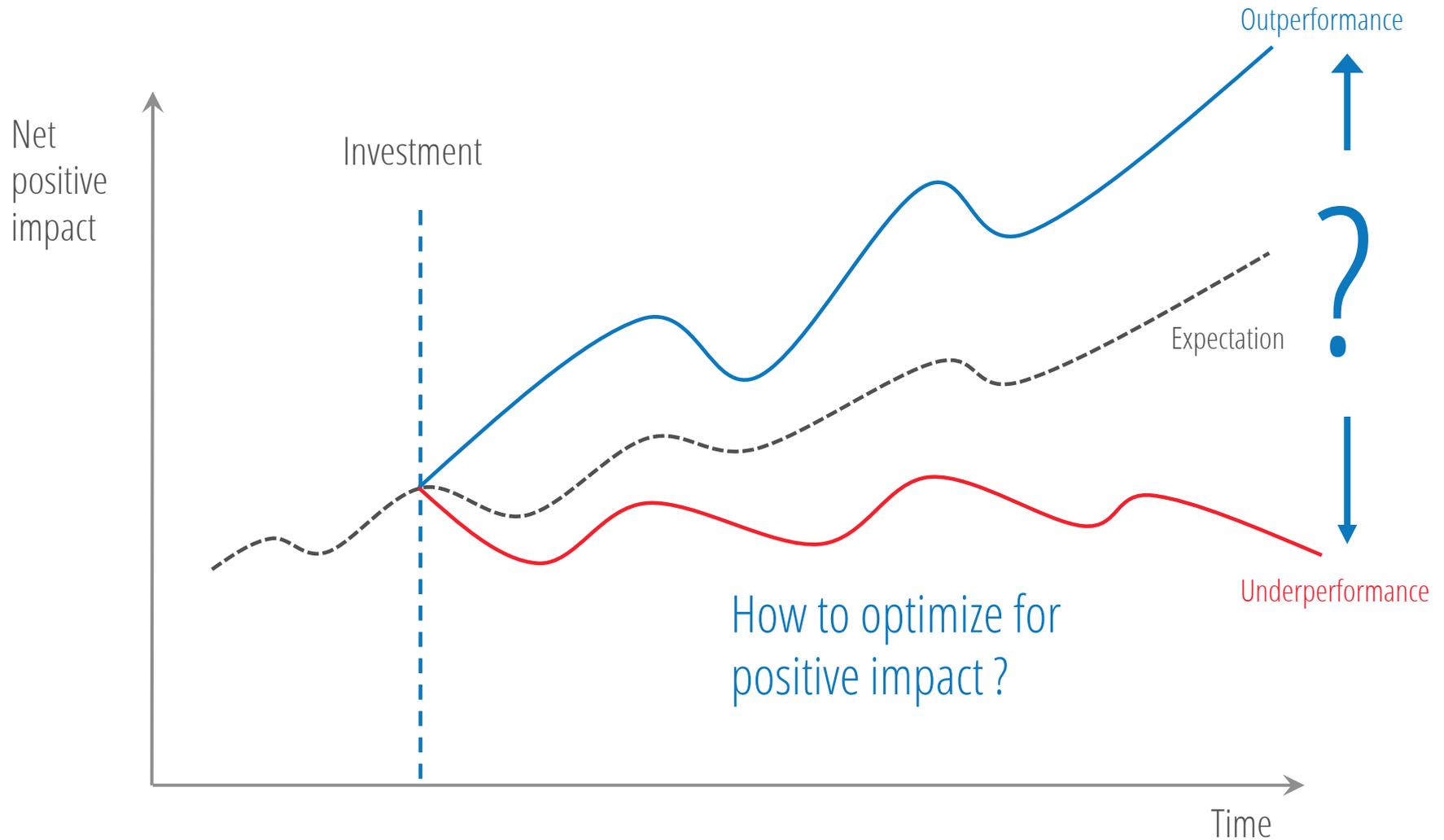


Ex-ante impact expectation





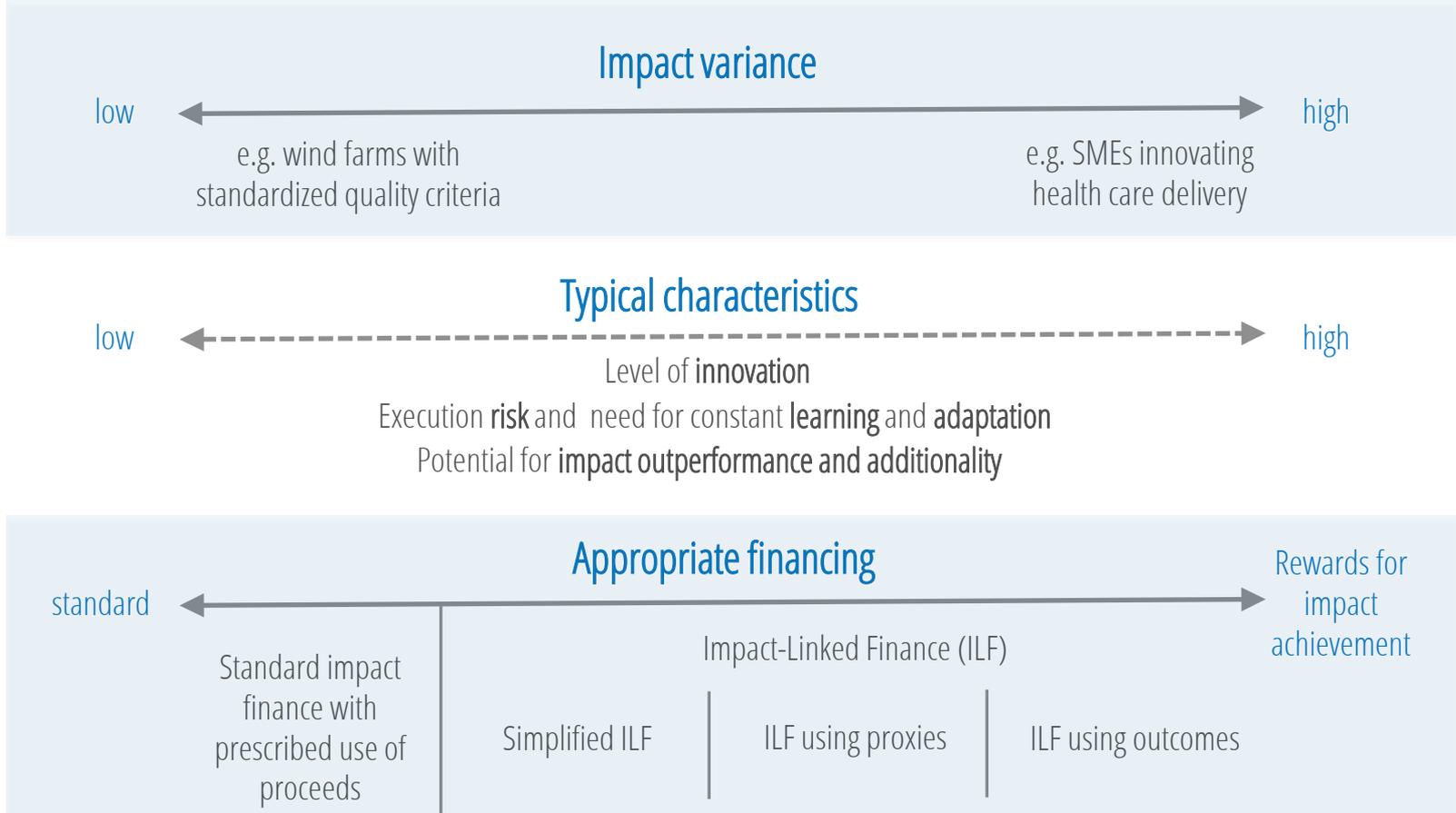
Ex-post impact creation





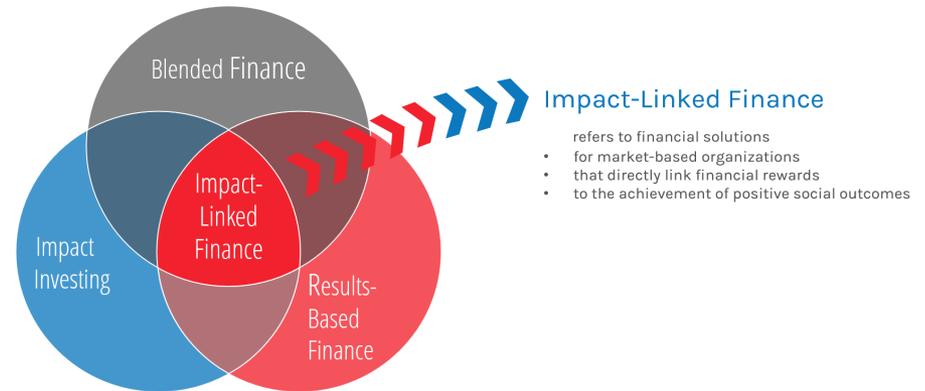
Appropriate financing depending on impact variance

Impact variance: How much actual impact performance may vary (differ from average impact performance or expectations). Covers impact risk and potential for impact outperformance.





Impact-Linked Finance

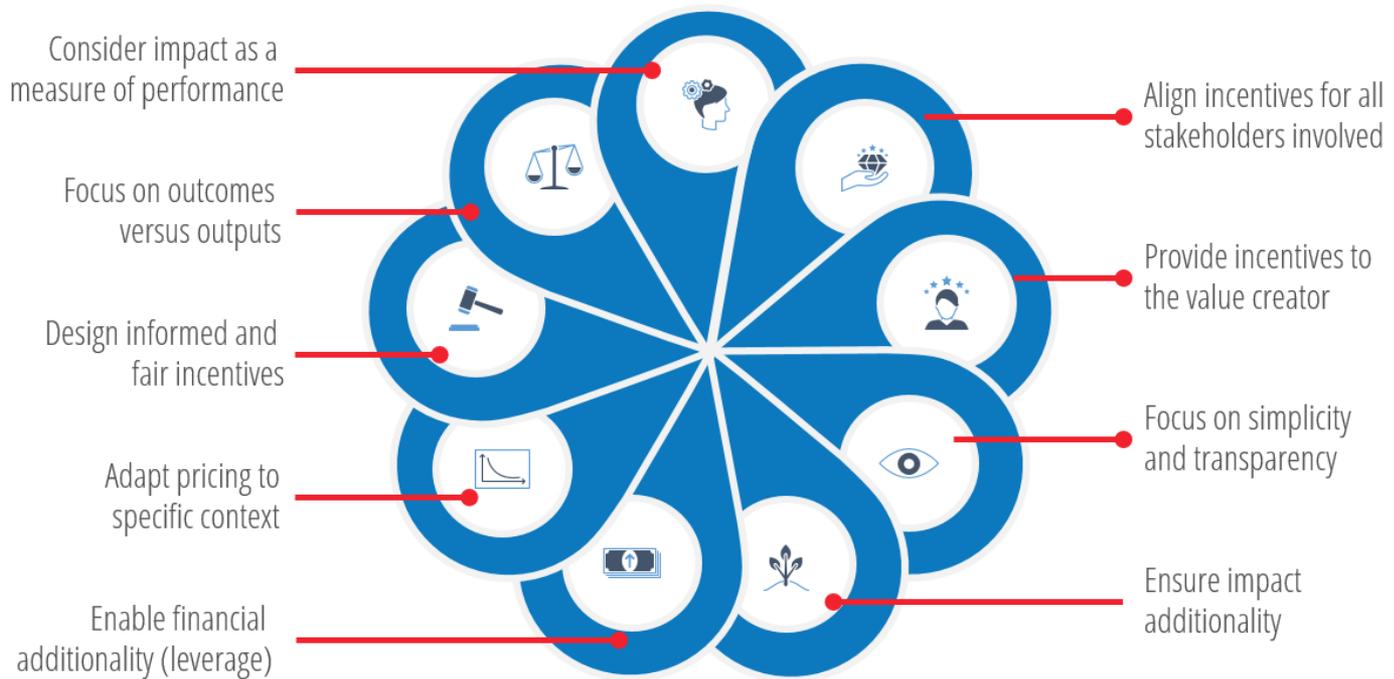


Definition of the practice (incl. design principles) in 2019 based on practical experience with Social Impact Incentives (SIINC) introduced in 2016:

- market-based
- outcomes-based
- catalytic



Design Principles for Impact-Linked Finance





ILF instruments and features

| Products/ Features | IMM build- up phase | Evolving metrics (agreed from the start) | Adaptive performance targets | Golden impact target (impact kicker) | Upfront payment (with repayment option) | Incentive repayment option | Conversion option |
|---------------------------------|------------------------|--|------------------------------------|--|--|----------------------------------|----------------------|
| Impact-Ready Matching Fund | standard | | | | x | | |
| Impact-Linked Challenge Fund | x | | | x | x | x | |
| Impact-Linked Matching Fund | x | | | x | x | x | |
| SIINC | x | x | x | | x | x | x |
| Impact-Linked RSA | x | x | x | x | standard | x | x |
| Impact-Linked SAFE | x | x | x | x | standard | x | standard |
| Impact-Linked Convertible | x | x | x | x | standard | x | standard |
| Impact-Linked Loan | x | x | x | x | standard | x | x |



Impact-Linked Finance - examples from Latin America

Profile



Leading provider of diabetes care in Mexico with more than 100,000 patients, 95% gaining access to specialized treatment for the first time (US\$1.5M equity alongside US\$275k SIINC)



Agricultural business, that creates employment for poor communities through eco-friendly production and export of sphagnum moss in the high Andean areas (US\$620k debt alongside US\$240k SIINC)



Dental health enterprise that provides on-the-job-site health solutions to the working poor in Ecuador (US\$1M debt alongside US\$280k SIINC)



Pioneering impact lender to agricultural SMEs in Latin America and Africa (US\$12M loans alongside US\$1M SIINC)

Effect of Impact-Linked Finance (over three years)

- Increased proportion of low-income patients with sustained good treatment outcomes from initial 32% to 37%
- On the way to 100 clinics across Mexico with further investment
- Expansion from 20 active communities in 2017 to 40 active communities in 2019
- 35% average income increase for harvesters
- Expanded from 550 to nearly 2,500 BoP customers
- Consistent majority (>62%) of low-income customers
- Consistent high patient satisfaction
- Provided high-additionality loans to 32 small, early-stage agricultural enterprises
- These enterprises generated US\$41M in income for 9,300 smallholder farmers



SIINC example: Clínicas del Azúcar



Enterprise profile

Clínicas del Azúcar is a leading provider of diabetes care in Mexico with more than 100,000 patients, 95% gaining access to specialized treatment for the first time.

Dedicated to serving the poor, the enterprise offers its services through a unique one-stop-shop model at about 40% of the average price for private treatment.

Financing

- US\$ 275k SIINC over 2.5 years
- US\$ 1.5M equity investment

Focus of impact incentives

More disadvantaged patients get access to effective, high-quality treatment (many for the first time)

Metrics

1. Ratio of BoP clients among active members
2. Average improvement in HbA1C levels among BoP patients

Results

- Increase in the average proportion of BoP members across all clinics from 32% to 37%
- Improvement of HbA1c levels of BoP clients exceeded those of other income groups
- Clínicas del Azúcar was able to raise an additional US\$6M in debt for its expansion across Mexico



Impact-Linked Finance example: Root Capital



Enterprise profile

Root Capital is a pioneering impact lender to agricultural SMEs in Latin America and Africa. The borrowing SMEs purchase crops such as coffee, cocoa, or grains from smallholder farmers. With growth enabled by access to capital and technical assistance, they become impact engines that can raise incomes, create jobs, empower women, and preserve vulnerable ecosystems.

* Loans are considered “high additionality” if no other lender would make the same loans on the same terms; “medium additionality” if only a social, subsidized or government institution would make the loan; different levels of rewards for high vs medium additionality

Financing

- US\$ 1M SIINC over 2 years
- US\$ 12M debt investment

Focus of impact incentives

Increase lending to agricultural SMEs in Latin America that are unprofitable to serve today, but which demonstrate substantial promise for growth and impact, especially for women

Metrics

1. Number of high- and medium additionality loans* below US\$ 500k
2. Number of loans to gender inclusive businesses (bonus)

Results

- Provided high-additionality loans to 32 small, early-stage agricultural enterprises
- These enterprises generated US\$41M in income for 9,300 smallholder farmers
- Twice as many high-additionality loans than in same period before