<u>**Blended Pool of Capital**</u>

Discussion Summary

<u>**Introduction**</u>

Following an introduction by Harold Rosen, Andrew Fiddaman moderated a discussion on the concept of a pool of capital that invests in social enterprises, and ‘blends’ social and financial returns, grants and loan or equity ‘patient capital.’

Panelists:

- Andrew Fiddaman, IBLF
- Mugo wa Karanja, Uzima Foundation
- Satyan Mishra, Drishtee

<u>**Key Points**</u>

<u>Current challenges faced by GBOs</u>

Uzima:

- *“Adult nature”* of donor money. Donors want to fund specific types of projects, not an organization as a whole, but when dealing with youth, that same youth that needs seed capital to start a business also needs a way to clean and safe fun, and health educations, etc.

Drishtee:

- *Limitations of microfinance*. Microfinance does not work for Drishtee’s model because:
    - It is too region intensive, whereas Drishtee is extremely spread out. Drishtee needs an existing infrastructure that banks can offer, such as ATMs
    - High interest + short maturity. Drishtee’s model should have lower rates than microfinance, since Drishtee developed the model and it believes in its success (rates should reflect this).
- *Linking banks and entrepreneurs directly*. Being the intermediary in the lending is burdensome and unsustainable for Drishtee due to the cost of lending (12%-14%) and the labor requirement, yet banks’ behavior does not allow Drishtee to pass the lending part of its model on to a bank.
- *Banks in India are not prepared for the bottom-of-the-pyramid type clients*: Even ICICI, which is one of the major actors, will not lend directly to Drishtee, but instead will lend to a local bank, at about 12% interest, and this bank in turn will lend at an additional 12%, starting off with an interest rate of 25%!
- Requirements from banks that are not realistic to the reality of rural India, particularly documentation requirements that cannot be fulfilled. Even if there is a proven track record of success, banks are not flexible with their documentation requirements.
- Indian banks will not lend directly to the entrepreneur even with full guarantee from Drishtee; they will still have the same requirements as anyone else.
- Would banks accept equity as an alternative to debt – returns dependent on how the business is doing could prove problematic to attract investment?

<u>**Proposed Solutions**</u>

As banks will not lower their interest rates, Harold noted that the *solution would be in a more equity type instrument***,** without it being traditional equity. There could be a pool that combines equity with grants.

Harold noted that YBI has loans given out to some thousands of young entrepreneurs, and if these loans were in the US, YBI could sell the debt. Why not do something like equity with the grassroots businesses?

Issues

Rigidity of banks in India: BK and Satyan explained that even with a 100% security to the bank, it would not skip the procedures in place. BK suggested that MFIs might be a more appropriate vehicle for this. [This would then not have the infrastructure benefit of banks as Satyan noted earlier].

Businesses, not companies: The group noted that most of these entrepreneurs do not have companies, but proprietary businesses, and therefore equity is not an option.

- It would be "quasi-equity". A hybrid that works like equity, but not in the official sense.

Attractiveness to investors:

Risk: on currency and low return

- The IFC would have to underwrite it, and there could be a senior tranche, for the more risk averse, that would guarantee its return.
- Melinda gave example of SEAF, which works with **hard currency**. She expressed SEAF's interest in doing something in India that reaches further down.
- BK suggested that a pool of debt and equity should mix the debt component in local currency to reduce risk.
- Mugo believed risk should not be viewed as such a problem: these entrepreneurs have succeeded in the most adverse conditions, and should only do better if the conditions improve.

Returns: Would this be attractive to investors?

- It would be aimed at social investors who care about the social benefit

Appropriateness: How to look at double bottom line and take equity where appropriate. There will be limitations – equity will not always be appropriate for the business (not all are ready for it), there is a higher cost involved, etc.

Standards: There will need to be standards for investors. Mugo suggested that it would be positive that the pool/fund set standards that are relevant to the field, as opposed to banks.

Next Steps

- Meeting in India with Banks and Corporate foundations to discuss the idea of more equity than debt type investments for grassroots businesses, and assess possible interest in getting involved in such an initiative for banks and investors.
- Pre-pilot: before putting even an initial $3-5M some kind of trial will be required.
- Pilot with Indian GBOs (BYST, Drishtee…)