FINANCING FOR SOCIAL ENTREPRENEURSHIP IN PERU

CARL BLACK

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TABLE OF CONTENTS

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EXECUTIVE SUMMARY

A SCAN OF THE LITERATURE on social entrepreneurship in Peru presents a paradox: higher-than-average levels of entrepreneurship and yet a comparatively underdeveloped social entrepreneurship and impact investing ecosystem. In recent survey data, 70% of a cross-section of entrepreneurs in Peru cite access to financing as a leading challenge for their business. At the same time, approximately 40% cite financial problems as a reason for business failure.

This study explores the obstacles and opportunities in financing social entrepreneurship in Peru using a combination of structured interviews, case studies, and secondary research. This combination of research methods was preferred due to the paucity of on-the-ground research on the subject in Peru. It was critical that the voices of entrepreneurs and investors be heard to complement existing, albeit limited, survey data.

The study finds that social enterprises in Peru have to a large extent relied on their founders, friends, and family to finance their businesses. Although many interviewees had approached banks and other formal financial institutions in Peru for financing, few have successfully received such financing. Access to finance for social enterprises from formal financial institutions in Peru is particularly limited for early-stage companies.

Access to finance for social enterprises from international impact funds has also been limited by a demonstrated preference of such funds for growth stage and mature companies with a positive financial track record. Investments by impact investors in Peru have focused on financial services. However, in recent years, while investments in this sector have remained steady, investments have been increasing in agriculture and other sectors.

Globally, the sustainable development goals provide an overarching framework through which to understand social entrepreneurship ecosystems. The goals link social entrepreneurs with impact investing, drawing attention to their similar mandates. To fulfil their missions, social entrepreneurs must be integrated into a broader ecosystem that includes government, investors, incubators, accelerators, and knowledge networks. Against that backdrop, the social entrepreneurship ecosystem in Peru is nascent. Important private and public sector programs and organizations are all relatively new, including Startup Peru, Innovate, Concytec, Kunan, and UPC's Protagonistas del Cambio.

The research highlights that many social enterprises in Peru are early-stage companies that impact investors perceive to not yet be ready for investment. This suggests a role for blended finance. Indeed, through Innovate, the Ministry of Production is already providing technical assistance-based grants with matching financing to support innovation and technology within the private sector throughout Peru. The public sector in Peru, potentially with international partners, could consider several other types of blended finance structures to catalyze impact investment for social entrepreneurship in Peru. Three types of financing structures are considered in the study: performance-based payments; contingent recoverable grants; and first-loss capital. More broadly, the report makes three recommendations to improve access to financing for social enterprises in Peru:

1. Bolster support for the development and promotion of viable social enterprises;

2. Consider fiscal policy incentives to promote social entrepreneurship; and

3. Create new public sector funding mechanisms for social enterprises.

In short, the challenge for social enterprises in Peru is that the social entrepreneurship ecosystem in Peru is nascent with a lack of flexible, patient, catalytic, and risk-tolerant funding sources, particularly for early-stage enterprises outside of the financial services and agriculture sectors. The opportunity is for the government and the impact investment community to collaborate to implement innovative approaches to impact investing, and to catalyze the emerging social entrepreneurship ecosystem in Peru.

INTRODUCTION AND BACKGROUND

ENTREPRENEURSHIP IS DEEPLY INGRAINED in Peruvian culture. Forty percent of the population say they would try to start a business within the next three years, compared to the Latin American average of 31.9%, and a global average of 21%.[1] Further, the Global Entrepreneurship Monitor (GEM) has ranked Peru as one of the countries with the highest levels of entrepreneurial activity in the world.[2] One theory is that this is a result of decades-long economic instability, which has resulted – among other things – in a highly informal workforce. Nevertheless, high rates of entrepreneurship have persisted over recent decades of higher growth and increased economic opportunity in Peru.

Social entrepreneurs focus on creating social value and generating positive social change. The way of doing business is often similar between traditional and social entrepreneurs, but their objectives differ; maximizing profits for the former and sustainably solving social challenges for the latter. Many definitions of social entrepreneurship emphasize that it focuses on innovative, sustainable (often market-based) solutions to pressing social challenges.[3]

Despite a culture of entrepreneurship, recent analysis suggests that social entrepreneurship is underdeveloped in Peru. In an IDB study on "Social Entrepreneurship and Innovation Ecosystems," the authors argue that despite having an innate entrepreneurial culture, "Peru has the least developed social intermediary support system and social impact investment scene" among five focus countries (Colombia, Mexico, Chile, Costa Rica, and Peru). They claim that "social solutions have not been supported by public institutions, as is the case in the other countries."[4]

Meanwhile, in recent survey data, 70% of a cross-section of entrepreneurs in Peru cite access to financing as a leading challenge for their business.[5] At the same time, approximately 40% cite financial problems as a reason for business failure, the reason selected with higher frequency than any other option.[6] The results were similar for both women and men in the survey.

A potential source of financing for social entrepreneurs in Peru is impact investment. Like social entrepreneurs, impact investors seek both social and financial returns. Like social entrepreneurs, some impact investors put more emphasis on social over financial outcomes, and vice versa. But for both social enterprises and impact investors, both types of returns are essential. Impact investors in Peru have to date focused predominantly on the financial services sector, with over 70% of total impact investments focused in the microfinance sector, according to the survey presented in the 2018 "Impact Investing Landscape in Latin America."[7]

The purpose of this study is to explore the synergies between social enterprise and impact investing in Peru. Two research questions guided the study:

1. What obstacles do social enterprises face when financing their companies?

2. What alternative sources of finance could help social enterprises overcome these obstacles?

POLICY CONTEXT

THE FOCUS ON PROMOTING ENTREPRENEURSHIP in public policy in Peru is relatively new. In 2012, the Ministry of Production launched Startup Peru to promote Peruvian startups and innovation. The program is modelled after Startup Chile and makes grants between S/.50,000 and S/.140,000 as seed capital to innovative and dynamic startups. Since it was founded, hundreds of startups have received millions of soles in funding. In 2014 the government of Peru established Innovate Peru (El Programa Nacional de Innovación para la Competitividad) to increase innovation and facilitate adoption of new technologies by entrepreneurs and business. Managed by the Ministry of Production (PRODUCE), Innovate provides non-reimbursable grants through co-financing for projects focused on innovation and entrepreneurship to increase productivity. The goal is to strengthen companies, entrepreneurs, and support systems within the Peruvian ecosystem, and facilitate collaboration between them through dozens of specific funds. For example, recently PRODUCE announced the launch of Reto Bio, a program that promotes innovative projects linked to making the most out of Peru's abundant natural resources and that will provide US$3.4M to fund startups and projects linked to biotech, agritech, and foodtech.[8]

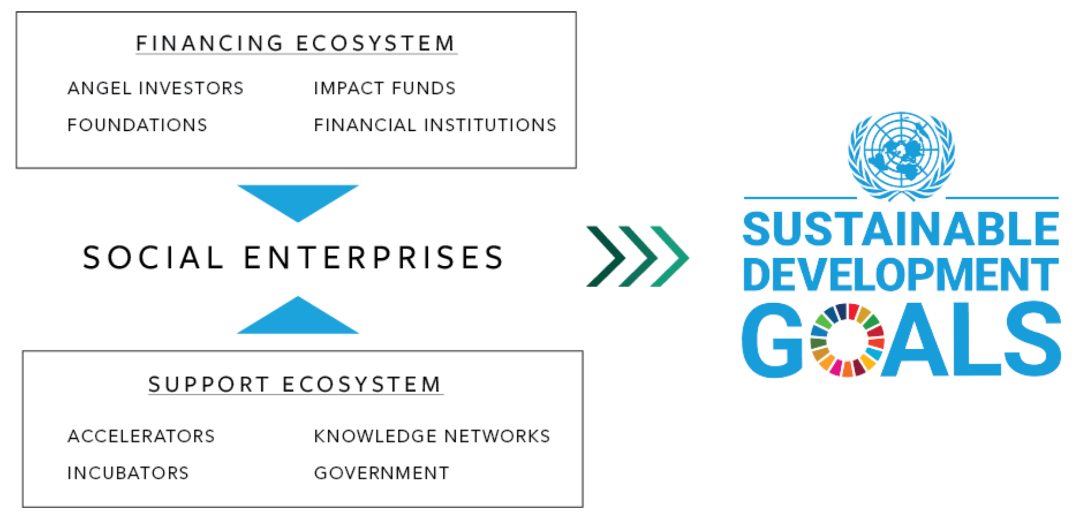
In addition to the direct provision of financing through Innovate (including Startup Peru), the government of Peru has provided three years of financing for angel investor networks. The Asociación Peruana de Capital Semilla y Emprendedor (PECAP), launched in 2017 by a group of five[9] angel investor[10] networks representing approximately 150 angel investors, invested US$9.1M in startups in 2018. The Universidad de Piura (PAD) investor forums have been particularly successful at facilitating investment in startups, usually for five-to-seven-year investments in early-stage equity. However, it is important to note that very few, if any, of this investment was allocated to social enterprises. This effort has been an important small step to the promotion of private finance of entrepreneurship in Peru.[11] The government of Peru has also supported over a dozen incubators to promote entrepreneurship, including Kaman in Arequipa and Startup UPC.

Other public sector participants in the ecosystem include COFIDE, Concytec, and PAME. COFIDE is Peru's development bank that provides credit to support development through financial intermediaries (IFIs). Concytec (including Cienciactiva) promotes science and innovation and has provided funding to several social enterprises interviewed for this study. The Programa de Apoyo a la Pequeña y Microempresa (PAME) of the Ministry of Development and Social Inclusion provides funding administered in a trust by Banco de la Nación since 2007. The credit fund provides lines of credit in rural and marginal urban areas of Peru for training and technical assistance to strengthen microenterprises.

The increasing public support for innovation and entrepreneurship is important in the context of a country where such support has been comparatively low.[12] Another important development in the social entrepreneurship ecosystem in Peru is the 2014 founding of Kunan,[13] a platform to inspire social entrepreneurship in Peru, through the facilitation of networking and collaboration. Meanwhile the Universidad Peruana de Ciencias has been promoting social entrepreneurship by awarding its Protagonists for Change award for nearly a decade. Finally, another important development has been the regionalization of international business accelerators, which has seen the entrance in Peru of, among others, Endeavor,[14] Wayra,[15] and Fledge.[16]

Globally, the sustainable development goals (SDGs) provide an overarching framework through which to understand social entrepreneurship ecosystems. The goals link social entrepreneurs with impact investing, drawing attention to their similar mandates. To fulfil their missions, social entrepreneurs must be integrated into a broader ecosystem that includes government, investors, incubators, accelerators, and knowledge networks. Our study was mindful of this broader context as we more narrowly focused on answering the research questions set out above.

FIGURE 1
Social entrepreneurship ecosystem



METHODOLOGY

DEFINITIONS

Two definitions served as important guides during the study, including during interviewee selection: social enterprises and impact investment.

For **social enterprise**, the definition we use in our study is:

"Any organization that, through its core mission or business strategy, intentionally and sustainably solves social and environmental issues that affect vulnerable populations."

The definition encompasses for-profit and not-for-profit entities. The words "or business strategy" broaden the definition to encompass for-profit companies whose core objective is profitability but who are nevertheless dedicated to inclusive value chains or business models that deliberately emphasize the provision of quality jobs in low-opportunity communities.

The inclusion of "sustainability" in the definition is intended to be broad. It includes the notion of financial sustainability through own income generation to cover costs. However, the study also includes business models that leverage stable partnerships to sustainably solve problems. Many social enterprises in Peru are not yet at financial breakeven, so the trajectory of the business is also an important consideration.

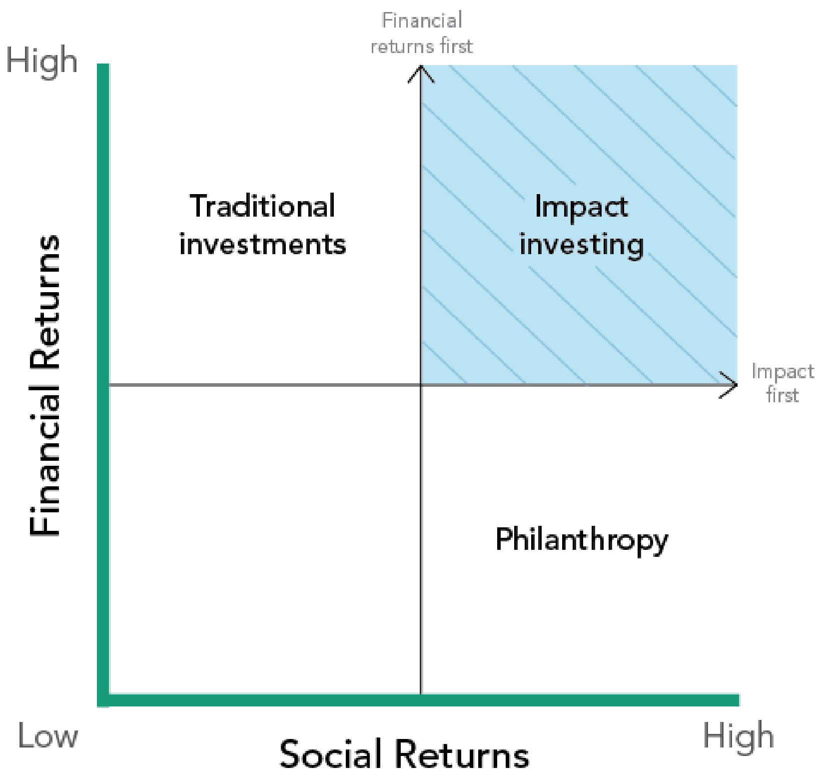
By including the words "that affect vulnerable populations," we follow Kunan,[17] a Peruvian platform and network for social and environmental entrepreneurship. Without that emphasis, a much larger subset of business could be considered a social enterprise, since most business are providing benefits to their communities.

Meanwhile, impact investing as an investment strategy has been around for over a decade and is defined differently by organizations in different contexts and with different goals. For this study we adopt the broad definition from the Global Impact Investment Network (GIIN), whereby impact investments are:

"investments made to companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return."[18]

In its report, "The Second Wave: Promoting a second decade of impact investing in frontier markets in Latin America," the authors explain that within impact investing there is a diversity of expectations with respect to social and financial returns. Graphic 5 from that report is adapted below. It helpfully contrasts impact investing with traditional investments on the one hand, and philanthropy on the other.

FIGURE 2
Defining impact investing



RESEARCH METHODS

The study pursued three lines of investigation to answer the research questions:

• A literature review of existing research;

• Semi-structured interviews with investors, entrepreneurs, and participants in the social entrepreneurship support ecosystem in Peru; and

• Case studies with social enterprises.

This combination of research methods was preferred due to the paucity of on-the-ground research on the subject in Peru. In our view, it was critical that the voices of entrepreneurs and investors be heard to complement existing broad survey data. The scope of the methodology is summarized in Figure 3.

Literature review: Our review of previous research pursued several lines of inquiry. First, we used the review to situate the study in the context of existing research about social entrepreneurship and supporting policy in Peru. Second, our review was data-centric, focusing particularly on previous research that used survey and

FIGURE 3
Summary of research methodology[19]

other quantitative methods to understand the experience of entrepreneurs in Peru in obtaining financing, and of impact investors in providing it. Third, the scope of the review included consideration of relevant best practices and trends in the other Pacific Alliance countries: Mexico, Chile, and Colombia. This research is summarized in the next section, but the secondary research more broadly informs and is reflected throughout this report.

Semi-structured interviews: Semi-structured interviews feature a combination of structured question and answer interactions and open-ended questions. This type of interview was used to collect both quantifiable data and qualitative explanations to provide the interpretive lens. The objective was for the voices of social entrepreneurs and impact investors in Peru to be heard. Three sets of interview questions were used, one each for social enterprises, impact investors, and support ecosystem participants. The interview questions were the same for the 21 social enterprises interviewed. Likewise, a different set of questions was used consistently for the 18 impact investors. A third base set of questions for support ecosystem participants was adapted depending on the interviewee. Interviews were held in either English or Spanish.

Case studies: Two case studies provided an opportunity to study the financial situations of two social enterprises in more depth. The two companies, PISCIS and CEDHI, were chosen to represent social enterprises with very different business models. PISCIS is a for-profit company whose core business strategy includes the employment of hundreds of women in Puno. Meanwhile, CEDHI is a not-for-profit technical education school in Yura near Arequipa that was founded by the Archbishop of Arequipa and relies on strong cross-sector partnerships for sustainability. To undertake the case studies, we held multiple interviews with the founders and management of both enterprises and conducted site visits.

LITERATURE REVIEW

FINANCING FOR ENTREPRENEURSHIP IN PERU

Peru has consistently scored high on the Economist Intelligence Unit (EIU)'s annual Global Microscope ranking for financial inclusion in emerging economies. As of June 2017, 60% of all credit in Peru was disbursed by microfinance institutions.[20] However, the 2016-2017 Global Entrepreneurship Monitor (GEM) cites a survey of entrepreneurs that suggests that profitability and difficulties obtaining financing are among the top reasons for entrepreneurs discontinuing their projects in Peru. It also undertook a survey of Peruvian experts who emphasized the need to increase access to finance to support innovative projects. Similarly, the 2018 study "Brechas para el Emprendimiento en la Alianza Pacifica" presents survey data that shows that difficultly accessing financing is a leading challenge and reason for business failure among entrepreneurs in Peru. Despite support for MSMEs from microfinance institutions providing finance where banks traditionally have not, social entrepreneurs continue to need alternative sources of financing in Peru. The GEM study suggests that Peruvian entrepreneurs continue to rely heavily on their own savings, personal consumer credit, and informal loans from friends and family to support their projects. In the Brechas survey, respondents in the Pacific Alliance countries (Colombia, Chile, Peru, Mexico) selected own resources and friends and family as principal sources of finance far more frequently than the financial system, public funds, angel investors, investment funds, and crowdfunding.[21]

IMPACT INVESTING IN PERU

Impact investing is a global industry that has grown exponentially over the last decade. According to GIIN's recent "Sizing the Impact Investment Market" report, which collected data from over 1,340 impact investors, the market is now over half a trillion US dollars worldwide.[22] However, the study shows that just 4% of impact investors have their headquarters in Latin America and the Caribbean, and those are mostly in Brazil and Mexico.[23] The Impact Investing Landscape 2016 study shows that impact investors headquartered and investing in Mexico manage at least US$392M (US$311 of which corresponds to non-microfinance institution (MFI) investors). In addition, international firms that invest in Mexico manage US$6.3B.[24] The report also emphasizes the role the government of Mexico has played in encouraging the development of venture capital funds, incubators, and accelerators following the creation in 2012 of the National Institute of the Entrepreneur (INADEM).

In contrast, there are no impact investors headquartered in Peru. This is important because risk perceptions are often elevated for international investors, and local investors may be more likely to invest in early-stage enterprises. Two perspectives on impact investing in Peru appear in the literature. On the one hand, ImpactAlpha, Syminvest, and other publications claimed that "Peru tops Latin America in impact investments" based on their reading of the 2018 and 2016 LAVCA/ANDE "Impact Investing Landscape in Latin America" studies.[25] On the other hand, researchers have argued that "Peru has the least developed social intermediary support system and social impact investment scene" of Pacific Alliance countries.[26]

A closer reading of the LAVCA/ANDE study[27] is instructive. Based on a survey of impact investors, the study shows that:

• 55 surveyed investors reported a combined investment in Latin America and the Caribbean (LAC) of US$1.4B through 860 investments in 2016-2017 (up from US$1.0B in the 2016 study);

• There is a global network of impact investors actively looking for and managing investments in Peru. There was at least US$200M of impact investments in Peru in 2016-2017; and

• In Peru, impact investors are heavily concentrated in the financial services sector with a focus on microfinance and financial inclusion. Only about $60M of $220M of impact investment in Peru was allocated outside of the financial services sector (25% to the total).

Figures 4 and 5 demonstrated some of these points and are adapted from data presented in the LAVCA/ANDE study.

FIGURE 4

All impact investments

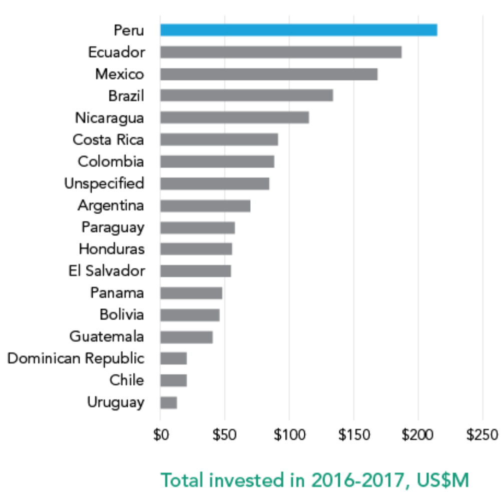


FIGURE 5

Non-MFI impact investments

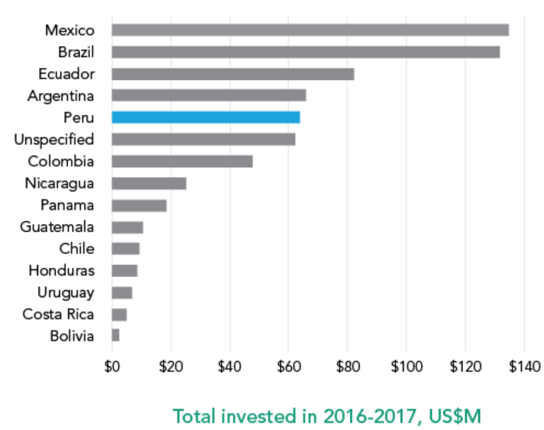
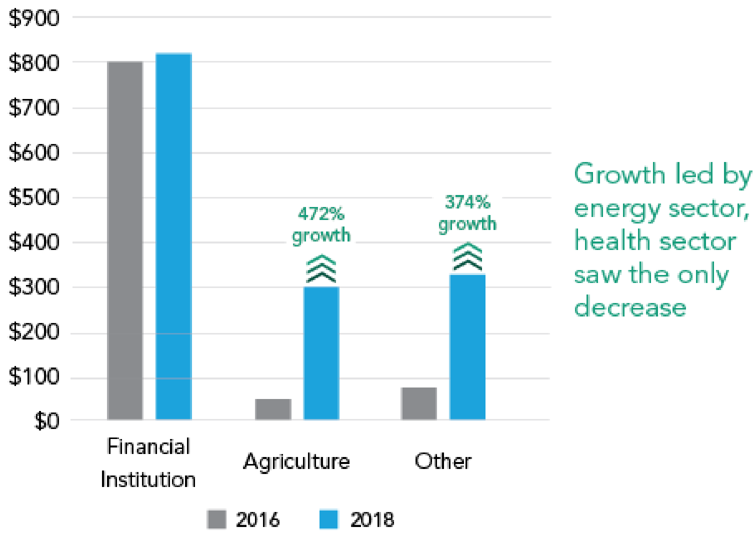


Figure 6[28] adapts the sector-disaggregated data for the LAC region and shows that impact investors in LAC have begun to diversify across sectors.

FIGURE 6

Impact investments by sector in LAC



Reasons for this diversification into other sectors may include the fact that the microfinance market is now mature, and senior debt has become a commodity in the sector with competition leading to declining yields. In Peru, the financial sector for microfinance is led by the CMACs, deposit-taking institutions with less need for senior debt to begin with. Secondly, the publication of the SDGs in 2015, and the increasingly broad interest in impact investing to support their achievement, is driving diversification. Thirdly, the evolving focus of the multilaterals will increasingly orient investment to other sectors. For example, the multilateral investment fund was recently rebranded as the IDB Lab and is now much more focused on innovation than on microfinance. The funding goals of the multilaterals will affect the focus of the private sector impact funds going forward, not least because they are an important source of funding for them.

The data in Figure 6 shows that investments by impact investors have remained steady in financial services but have increased, particularly in agriculture, in recent years. This trend may accelerate as the microfinance market continues to mature if yields decline on private debt in the sector. Meanwhile, agricultural co-operatives are a natural fit for impact investors accustomed to investing in intermediaries for the benefit of producers or microentrepreneurs down the value chain. The intermediary structure of the sector in Peru also facilitates certification (organic, fair trade, etc.) that helps impact investors support their impact theses. Lastly, the higher risk associated with the sector concentration can be offset when lending to co-operatives with international sales through trade finance factoring.

Investors in the region continue to worry about the shortage of options to exit their investments and get their capital back. While funds seeking market-rate returns are increasingly active, early-stage and risk-tolerant "patient" capital is in short supply. According to the GIIN 2018 "Annual Impact Investor Survey," the highest share of investment is allocated to growth stage and mature companies. The Impact Investing Landscape survey likewise shows less investment in seed-stage (US$2M of US$1.4B) and early-stage opportunities (US$140M of US$1.4B). Few funds are pursuing innovative deal structures to accommodate investors' and investees' needs, according to the GIIN survey. In the IDB "Study of Social Entrepreneurship and Innovation Ecosystems in the Latin American Pacific Alliance Countries," the authors observe that "there is a growing landscape of international impact funds seeking sustainable, proven, scalable and profitable social enterprises to support. However, many of these funds are seeking to invest at least 1 million USD and there are far fewer funding opportunities for those organizations who are at an earlier stage in their growth."[29]

ADDRESSING CHALLENGES FOR SOCIAL ENTREPRENEURSHIP

In addition to helping to frame the challenges in marrying impact investors with social enterprises, the literature also points to some solutions. These potential solutions include promotion of a healthy social entrepreneurship ecosystem, promotion of regionalization to address the small-market challenge, and the need for innovative financing solutions, including from the public sector.

First, for social enterprises to successfully attract impact capital, they will need to be embedded and supported by a healthy entrepreneurship ecosystem. In the IDB impact investing in Latin America study, "The Second Wave," the authors argue that "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." The study argues that the key challenges in Latin America include scaling in small markets, lack of early-stage finance, regulatory barriers and taxes, and a lack of financial innovations.

Second, to address the small-market challenge, there is a need to encourage regionalization. Latin America is a region of small-market countries; 29 of 33 countries (including Peru) in the region have populations smaller than that of Canada. There is a need to think big with regional and global models and "solving big problems, not small markets."[30] Co-investing approaches, networks, and accelerators can all promote regional growth. As discussed below in our research findings, promotion of regional approaches is happening increasingly in Peru with the entrance of global accelerators such as Fledge, Agora, and Endeavor.

Thirdly, there is a need for innovative financial solutions and for increased public sector finance. In "The Second Wave," the authors argue that "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." Grants don't always incentivize growth and the development of a financial track record;

debt is often impossible for early-stage companies without the revenues to service it, or the collateral to obtain it; and equity investors often expect rapid scale, high returns, and quick profitable exits. “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.”[31]

Several studies point to the need for greater public sector engagement to address challenges. In “Brechas para el Emprendimiento,” the authors discuss existing public sector financing instruments for SMEs in Peru, including Innovate, and observe that they are still insufficient and that financing for high-risk activities is fundamental in order to attract debt or other financing. They suggest that public sector organizations could bring concessionary financing instruments to address this challenge in Peru.[32] Meanwhile, in the 2016 LAVCA/ANDE Impact Investing Landscape survey, the authors observe that “among impact investors, there is a general consensus that the government should take a more active role in supporting impact enterprises and impact investing…reducing legal and regulatory challenges for impact-oriented firms, creating tax incentives for impact investment, and supporting the development of the entrepreneurial ecosystem.”[33] Similarly, in the IDB’s “Study of Social Entrepreneurship and Innovation Ecosystems in the Latin American Pacific Alliance Countries,” the authors argue that “while Peru has an innate entrepreneurial culture, social solutions have not been supported by public institutions, as is the case in other countries.”[34] They go on to argue for “creating a public fund for social entrepreneurship and innovation, as well as a social innovation lab,” and to learn from neighbours such as Colombia and Chile to replicate programs and fast track progress.[35]

Beyond a need for direct funding, the survey analysis in the Brechas report shows that when entrepreneurs in Peru are asked to rank public policy priorities, tax policy is ranked first, creation of entrepreneurship development centres is number two, and a need for public sector finance comes in fifth. In the Global Entrepreneurship Monitor, survey data shows that respondents select with the highest frequency that government policy had the largest positive or negative effect on the entrepreneurship ecosystem in Peru.[36]

GAPS IN THE LITERATURE

This brief scan of the literature on social entrepreneurship and impact investing in Peru highlights the entrepreneurial culture of Peru, challenges financing entrepreneurial activity, recent growth of impact investment funds in sectors other than financial services, and the need for regionalization, development of healthy entrepreneurship ecosystems, and public sector engagement to address challenges.

Our scan of the literature uncovered a lack of on-the-ground primary research in Peru with social entrepreneurs and financial sector participants to develop a more specific understanding of impact investing and alternative sources of financing for social entrepreneurs. Our study aims to start to fill that gap. The findings from our case studies and interviews are described in the next section.

ANALYSIS OF FINDINGS

SUMMARY STATISTICS

Before discussing the key findings of the interviews with social enterprises, we contextualize them with a summary of the interviewees. Figures 7 to 12 show that:

- Most interviewees were founders and CEOs from companies founded after 2010;
- Most interviewees had male founders between the ages of 31 and 40; and
- Most social enterprises interviewed were early stage, and micro or small.

The figures also show that feedback was collected from a variety of perspectives, from new and older companies at different stages in their life cycle, and with founders from different walks of life. These different perspectives are aggregated and distilled in a summary of key findings in the following sections.

FIGURE 7
Title of interviewee

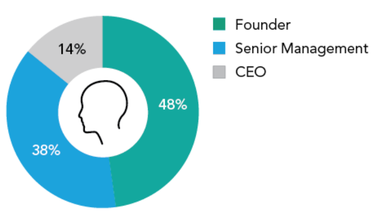


FIGURE 8
Interviewees by year founded

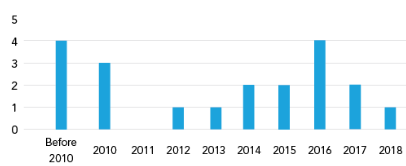


FIGURE 9
Gender of founders

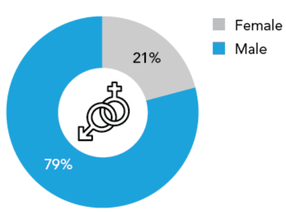


FIGURE 10
Age of founders

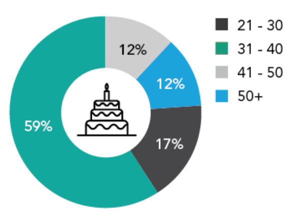


FIGURE 11
Interviewees by company stage

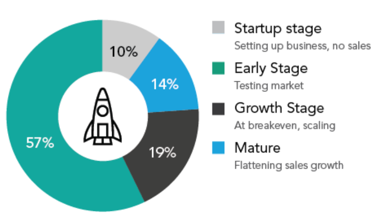
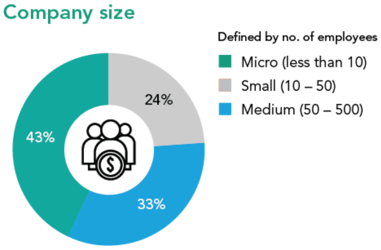


FIGURE 12
Company size



As mentioned during discussion of the methodology, our aim was to include a broad cross-section of sectors in the study. We also considered the alignment of interviewees with the sustainable development goals as we sought to ensure the inclusion of diverse perspectives. Based on our own understanding of the objectives and business models of the social enterprises interviewed, we determined that they could be aligned with 7 of the 17 SDGs. We assigned the enterprises based on the SDG we felt best aligned with their social mission.

Figure 13 summarizes the 21 social enterprises interviewed for the study according to SDG and sector.

FIGURE 13

Social enterprises interviewed sorted by SDG and sector[37]

Sustainable Development Goal	Sector	Social enterprise	Total
3 GOOD HEALTH AND WELL-BEING	Healthcare	Doktuz	1
4 QUALITY EDUCATION	Education	CEDHI	2
		Laboratoria	
6 CLEAN WATER AND SANITATION	Sanitation	X-Runner	2
	Water	Yaqua	
8 DECENT WORK WITH ECONOMIC GROWTH	Financial services	Edpyme Alternativa	7
		Fondesurco	
		ONG Progressa	
	Consulting	Humaniza RSE	
	Agriculture	Elemental Chocolates	
		Inka Moss	
		Cacao de Aroma	
12 RESPONSIBLE CONSUMPTION AND PRODUCTION	Fashion	Estrafalario	5
		Hoseg	
	Waste disposal	Sinba	
		CICLO	
	Tourism	Pausa	
14 LIFE BELOW WATER	Aquaculture	PISCIS	2
		SFT (Sustainable Fisheries Trade)	
15 LIFE ON LAND	Forestry	Patrulla Ecologica	2
		Reforesta	
		Total	21

In addition to 21 social enterprises, the study included interviews with 18 investors and 13 institutions in the support ecosystem. The investors included institutions from eight countries, including Peru. International investors represented over US$320M in impact investments in Peru. These interviewees included: Kandeo, Oikocredit, Incofin, Frankfurt School, Global Partnerships, MCE Social Capital, Desjardins, NESsT, Grassroots Business Fund, Acumen, Rabobank, Peru Opportunity Fund, ResponsAbility, Deetken Impact, and Fundación Wiese (Fondo Emprendedor). Interviews also included Peruvian financial institutions such as Caja Arequipa and Cooperativa Abaco.

Meanwhile, the support ecosystem was represented in interviews by incubators, accelerators, knowledge networks/academia, and government, including Kunan, Peruvian Ministry of Economy and Finance, Universidad Pacifico (Impact Investing Taskforce), Protagonistas del Cambio (Universidad Privada de Ciencias Aplicadas), Universidad Católica San Pablo (Kaman), Federación Peruana de Cajas Municipales de Ahorro y Crédito, Red de Inversionistas Angeles de PAD (Universidad de Piura), Agora, Angel Ventures Network, Fledge, and Endeavor Peru.

SUMMARY STATISTICS

Social enterprises in Peru have to a large extent relied on their founders, friends, and families to start their businesses. Although many interviewees had approached banks and other formal financial institutions in Peru for financing, few have successfully received such financing. Meanwhile, about one-third of interviewees had received funding from the government of Peru through either Innovate, Startup Peru, or Concytec. Finally, Figure 14 also shows that an important share of our sample had received financing from international impact funds.

FIGURE 14
Financing by source

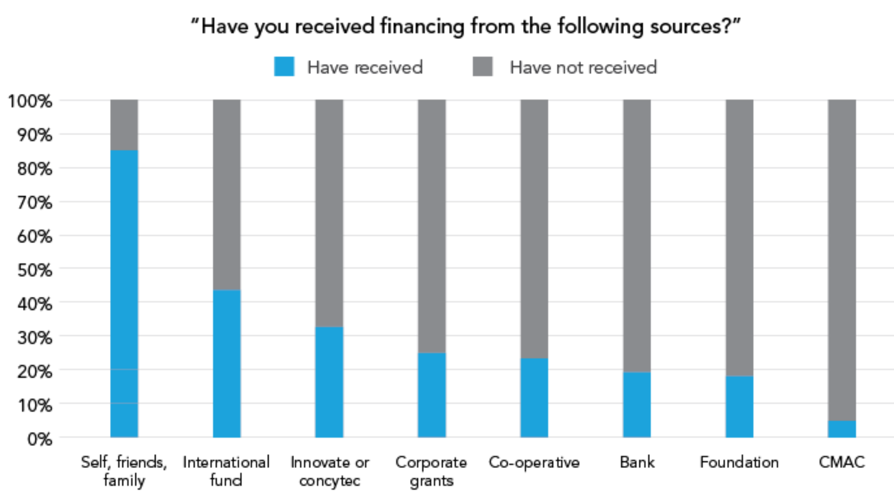
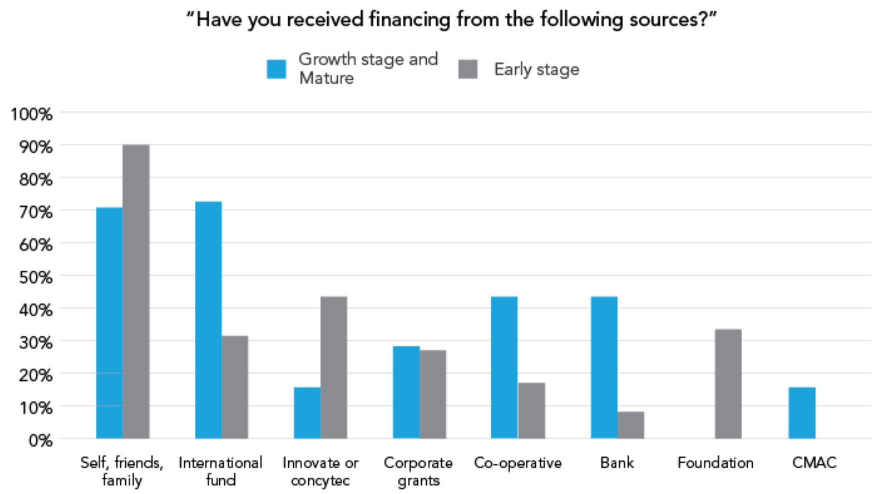


Figure 15 shows that access to financing for social enterprises from formal financial institutions in Peru is particularly limited for early-stage companies. It also highlights the preference historically of international impact funds for growth stage and mature companies.

FIGURE 15

Financing by source and company stage



CHALLENGES RELATED TO FINANCING

During interviews, several common challenges related to financing for social enterprises were uncovered. These include:

• Lack of access to bank financing because of high interest rates,[38] guarantee requirements,[39] uneven cash flows (particularly in agriculture), and costs of formalization (e.g. the need for audited financial statements);

• Lack of access to financing from international lenders because of their inability to lend in local currency;

• Lack of access to equity and quasi-equity financing from international investors who tend to be focused on debt, near-market returns, and are often risk-intolerant;[40]

• Exacerbated working capital financing needs caused by sales on credit by smaller social enterprises to larger buyers. Related, several interviewees discussed payment of value-added tax in advance of receipt of payment from customers as an additional challenge; and

• Challenges for social enterprises in urban areas providing services usually delivered by the public sector (including healthcare, education, sanitation, and waste disposal).

PERU'S SOCIAL ENTREPRENEURSHIP ECOSYSTEM

Interviews also uncovered the following gaps in Peru's social entrepreneurship and impact investment ecosystem:

• The social entrepreneurship ecosystem in Peru is nascent. Important private and public sector programs and organizations are all relatively new, including Startup Peru, Innovate, Kunan, and UPC's Protagonistas del Cambio.[41]

• There is very little specific focus on social entrepreneurship among the existing actors, including public sector funding programs such as Innovate, angel investor networks, and incubators/accelerators. These initiatives tend to be focused on startups and innovation. Further, while the number of organizations in the ecosystem is growing, there is limited co-ordination and interactions among them.

• There are few mature and growth stage social enterprises ready to receive available impact investor debt. Interviewees from global accelerators, angel investors, and academia observed that there is a lack of traction in the business models of social enterprises in Peru, leading to a lack of a clear path to profitability and scalability. Enterprises need clear and simple business models with specific growth strategies.

• Peruvian fund managers focused on impact investments and raising capital in Peru are almost non-existent. While there are several international funds that invest in social enterprises with a strong presence in Peru, they represent relatively small investment portfolios. These include NESsT,[42] Grassroots Business Fund, and the Peru Opportunity Fund. NESsT is currently partnering with Fundación Wiese on Fondo Emprendedor, through which they will invest US$2.0M in four companies while also providing incubation. The fund was created in November 2018 and received over 100 applications for funding on its first round, demonstrating the need for early-stage capital for social enterprises in Peru. Meanwhile. NESsT is partnering with the Grassroots Business Fund on the US$20M SELF fund through which they will invest between US$200,000 and US$500,000 – the "missing middle" in Chile, Peru, Colombia, and Brazil.

• Most impact investors in Peru remain focused on the financial services and agricultural sectors. Indeed, only 3 of 18 investors interviewed had at least one impact investment in another sector. As seen in the literature review, interviews suggest that the focus by impact investors on agri-business in Peru has been increasing in recent years as international funds have joined local financial institutions in investing in that sector. Trade finance is a common investment strategy in the sector. Café and cacao co-operatives have been conduits through which impact investors have sought to implement rural development impact strategies in Peru.

CASE STUDIES

In this section we turn to a more detailed consideration of two social enterprises interviewed for this study. The enterprises were chosen to showcase two very different business models through which social enterprises in Peru are achieving sustainable positive social impacts in their communities. The case studies are based on separate interviews with the founders, managers, and owners of the two social enterprises as well as on-site visits in Arequipa and Puno. A snapshot overview of each of the two social enterprises is followed by a discussion of the history, business model, social impact, financing, public sector interactions, and key lessons for the two enterprises. Our goal with the case studies is to better understand the challenges related to financing that were discussed above and to pave the way for a consideration of solutions in the following section.

CASE STUDY 1

PISCIS

Year founded	**1978**
Location	**Tacna and Puno**
# Active employees	**260**
SDGs impacted	

Piscis provides sustainable livelihoods in the southern Andean community of Puno.

DESCRIPTION	A social enterprise producing trout at its aquaculture farms in Lake Titicaca and processing the fish for export and local sales.
BUSINESS MODEL	A for-profit corporation. Exports through international buyers to Canada, Chile, Argentina, and Northern Europe.
SUSTAINABILITY	The company aims to cover all of its costs through revenue from sales. Core to the company's business model is the sustainable employment of 260 community members, 70% of whom are women.
KEY PARTNERSHIPS	Cooperativa Abaco, PROMPeru
FINANCING	Shareholder loans, international impact investor, Banco de Credito
WEBSITE	https://www.piscisperu.com.pe

HISTORY

PISCIS was founded in 1978 as one of the first aquaculture companies in Peru by the Familia de la Piedra when they acquired well and tank infrastructure from the government in Huancayo to raise trout on farms. The company began by producing and selling trout locally, and later in Lima. In 1982, PISCIS began to export to Sweden. Rural terrorism in the 1980s threatened the business model with attacks on electrical infrastructure and threats against workers. Nevertheless, PISCIS continued its small production and sales.

As the company passed from father to son in the second half of the 1990s, PISCIS began to increase sales and export to other markets. With support from PROMPERU, a state institution promoting exports, PISCIS began to promote its products at international festivals in Boston and Brussels. The company began operations in Puno in 2004 in floating cages in Lake Titicaca, where the company holds a 14.4-hectare 30-year concession.

PISCIS was sold in 2008 to a businessman connected with el Banco de Crédito in Peru, and again in 2014 when it was acquired by the current owner, Cooperativa de Ahorro y Crédito Abaco, through Efis Consulting Group.

BUSINESS MODEL

PISCIS is a for-profit company focused on the production and processing of trout in Lake Titicaca in Puno in Southern Peru. It operates fish farms on the lake, manages a rented processing factory in Puno, and has trout processed by a third party in Tacna. PISCIS purchases juvenile fish from suppliers (including Acuisolutions, a sister company) and raises them in 5×5 and 10×10 floating cages 50 metres offshore at one location on the lake. The fish are moved between cages as they grow in size. There are three main production phases:

• Infant fish (fish up to 40 grams, 90 days);

• Juvenile fish (from 40 grams to 100 grams, 90 days); and

• Adult fish (from 100 grams to 500 grams, 90 days).

PISCIS completes one harvest daily. Harvested fish are transported in its two trucks or by a third party to the rented processing plant in Puno or to the third-party plant in Tacna to be filleted and prepared for sale. Over 70% of PISCIS's costs are for fish feed, most of which is purchased from Salmofood Vitapro in Chile. PISCIS uses cameras to view and monitor its cages. Access to inputs has not been a significant challenge for PISCIS. The key challenges have been accessing finance and strong professional management and monitoring. These are discussed in subsequent sections.

Initially, the company relied predominantly on sales in local markets. While local market sales of fresh, deboned, and frozen fish have increased, today more than

60% of sales are through exports. Buyers in Peru include supermarkets such as Vivanda, Cencosud, Wong, Tottus, and Makro. Meanwhile, exports of frozen fish are undertaken through container shipments with over 10 clients, including Aquastar (Canada), High Liner (Canada), Oceanic (Canada), Citylight (USA/Canada), Kohyo (Holland), Ultra Fish (Russia), Top Intertrade (Japan), Beaver Street Fisheries (USA), Lobster Seafood (Sweden), Cosmos (France), Yens Brothers (China), and Frescopez (Argentina). Approximately 70% of all exports are to Canada.

SOCIAL IMPACT

As the company evolved from a small producer of ~300 tonnes/year on farms in Huancayo, to producing and selling over 2,200 tonnes of trout per year, its core business strategy also became more focused on social impact. PISCIS's social and environmental impact has three elements: care of the lake ecosystem, dignified and equal employment, and strengthening value chains.

First, with respect to the ecosystem of Lake Titicaca, PISCIS uses best practices to mitigate ecosystem impacts from its operations, including:

• Use of sterile female fish only;

• Efforts to mitigate fish escapes;

• Addition of fish feed in accordance with the biomass of each cage;

• Use of high-quality fish feed to avoid excessive discharges of nitrogen and phosphorous;

• Periodic monitoring of the water to control levels of nitrogen, ammonium, and oxygen; and

• Use of the Hazard Analysis and Critical Control Point (HACCP) system for all its plants as required by SANIPES, the Peruvian fisheries and aquaculture sanitation authority, and an essential requirement for exports to the European Union.

Since 2016, PISCIS has been certified with Best Aquaculture Practices (BAP), which covers best practices in the environment, community relationships, animal well-being, and safety and security for workers.

Second, core to PISCIS's business strategy is the provision of dignified and equal employment. There are approximately 6,000 families living alongside the lake who are dedicated to small-scale fishing. PISCIS has close to 40 employees at the fish farm, 180 in processing plants, and a total of 260 once logistics and administrative staff are counted. The fish farm mainly has male workers, where the work consists of transporting fish from cage to cage, feeding fish, monitoring fish health and growth, and harvesting fish. Meanwhile, the processing plants are staffed almost entirely by women, such that over 70% of all employees are women. The women who work at the processing plants are provided with equal pay with the men who work at the farms. Older generations of workers migrated from artisanal sewing to fish filleting, bringing with them transferrable skills from the long textile tradition in southern Andean Peru. Workers are from nearby communities including Huencalla for the farm and Salcedo and Chucuito for the processing plant in Puno. They are paid more than the minimum monthly wage of US$284 in Peru.

Thirdly, PISCIS promotes strong and inclusive value chains. In addition to producing trout on its own farms, PISCIS provides market access for smaller producers by providing training to small volume fishers to help improve the quality of their products. Through this process, PISCIS is helping to formalize the local economy, and provides advice on feed management (the largest cost for fishers) and business administration. PISCIS provides periodic monitoring of small producer farms to ensure quality and alignment with environmental best practices. Small producers are paid within seven days of delivery to PISCIS. PISCIS also promotes nutrition through consumption of protein in the community.

FINANCING

PISCIS has a high demand for working capital to cover its 8-to-10-month production process from acquisition of juvenile fish to harvest and sale. The company also has periodic capital requirements to maintain and improve its farm, logistics, and production plants.

Core to the success and longevity of PISCIS has been strong equity partners, from the founders to the current owners. The Cooperativa Abaco is a financial institution that was founded in 1981 and regulated by la Superintendencia de Banca, Seguros y AFP (SBS). The mission of the institution is to contribute to the improvement in the well-being of its partners with agile and adaptable financial solutions, working for the common good, and a focus on sustainable development.

After purchasing 100% of the company in 2014, Abaco has financed PISCIS with lines of credit for working capital and capital costs, as well as with long term (5+ years) loans. In addition, PISCIS has an international factoring operation for exports and line of credit from Banco de Crédito del Peru (BCP), and a term loan from an international impact investor.

Nevertheless, access to finance has been a leading challenge for PISCIS. Periods of negative earnings before interest, tax, depreciation, and amortization (EBITDA) (now positive) and a limited number of guarantees available to offer has made it difficult for PISCIS to access financing from banks in Peru. Funds have also sought guarantees. This response from the banks resulted in Abaco directly providing debt financing. However, regulation limits the extent to which such financing can be provided. As of January 1, 2019, law N° 30822 established a new direct regulation of co-operatives by the SBS. As one of the larger co-operatives in the country, Abaco qualifies as a Level 3 co-operative under the law, which limits related-party loans. Another challenge is that Abaco does not qualify as an international financial institution (IFI) eligible to serve as an intermediary for loans from Peru's development bank, COFIDE.

PISCIS has never received donations. The financing obtained by PISCIS to date has been secured using a number of approaches. Past loans from Banco Continental and Banco de Crédito were secured with land where the production plant was located plus a bank deposit. Most debt has been in soles; however, US dollar loans have also been obtained when used for US dollar purchases from international suppliers. International factoring based on sales with international buyers is another approach used by PISCIS to obtain bank financing, an approach common across the agricultural co-operatives interviewed for this study. Stand-by letters of credit have also been used to secure financing.

PUBLIC SECTOR INTERACTIONS

PISCIS has interacted with the public sector in Peru and international multilateral institutions in several ways to support its business. First, PROMPERU provides support by organizing opportunities to exhibit and hold meetings at international conferences. Second, Abaco, the IDB, and Umitron (a company in Japan) are partnering to provide US$2M to test new sensor technology to monitor water conditions (oxygen level, pH, etc.) and fish before, during, and after the feeding process. The project is aimed at addressing a key challenge for any aquaculture company, fish mortality. The goal of the project is to use technology to:

- Reduce fish stress, which can cause fish to eat less, get sick, and lose weight;
- Maintain adequate levels of oxygen (at least 5 mg/L);
- Monitor the water quality and chemical composition;
- Ensure appropriate feeding programs for fish of various sizes; and
- Ensure compliance with best practices for aquaculture (GAP) and hygiene (PHS).

The objective of the two-year project is to reduce overfeeding and the resulting negative financial and environmental impacts. After implementation, the technology could be shared with PISCIS's value chain.

While aware of Concytec, Programa Nacional de Innovación en Pesca y Agricultura (PNIPA), the Fondo de Desarrollo Pesquero, Sierra Exportadora, and Innovate, PISCIS has yet to work with those public sector programs in Peru. PISCIS does not qualify for tax incentives under the Ley de promoción de empresas agriculturas.

KEY LESSONS

The literature review highlighted that access to finance is a leading challenge and cause for business failure in Latin America and in Peru. The data was for all businesses, not just social enterprises. With annual revenues in excess of S/.40M, PISCIS is one of the larger social enterprises included in this study. Yet access to finance continues to be a challenge. The barriers to bank financing identified in this case study were similar to those named by early-stage enterprises in interviews: lack of a consistently positive financial track record, limited ability to offer collateral, and high interest rates.

Historically, PISCIS has not benefited from direct financial support from public sector institutions. The recent technical assistance initiative is an exception. The keys to PISCIS's longevity have been strong equity partnerships and a stable management team focused on stabilizing the company's business model and integrating social and environmental objectives into the company's core business strategy. Together, these factors have begun to attract international impact investment as a viable alternative to local financial institutions.

CASE STUDY 2

CEDHI

Year founded	**2010**
Location	**Yura, Arequipa**
# Active students	**400**
SDGs impacted	4 QUALITY EDUCATION

The school offers scholarships such that students pay just 20% of the tuition costs and feeds are adjusted according to the financial situation of the student.

DESCRIPTION	Founded by the Archbishop of Arequipa, the Centro de Estudios y Desarrollo Humano Integral is an education institution offering courses in business administration, gastronomy, soldering, cosmetology, and computing. The school places students in jobs post-graduation with a 92% rate of success.
BUSINESS MODEL	Not-for-profit foundation, offering subsidized education to vulnerable communities through long-term partnerships.
SUSTAINABILITY	The school covers 20% of its costs through tuition fees, and 25% of its costs through soldering and metal craft production and sales. Grants from long-term partners cover remaining costs.
KEY PARTNERSHIPS	Caritas Diocesana, Universidad Católica San Pablo, Caja Arequipa, among others.
FINANCING	Self-generated income, grants
WEBSITE	https://www.facebook.com/CEDHINuevaArequipaOficial

HISTORY

The Centro de Estudios y Desarrollo Humano Integral (CEDHI) was founded by the Archbishop of Arequipa, Javier del Rio, through Caritas Diocesana, a Catholic social service and development organization, in 2010. It is located in the Cono Norte of the Yura District of Arequipa. Initial construction of the school took four years and classes began in 2014.

The genesis for the idea of CEDHI was born in the year 2000 when the Archbishop was then bishop of Callao. In that capacity, he founded the Centro de Estudios y Desarrollo Comunitario de Pachacútec (CEDEC) in Ventanilla in the district of Callao, north of Lima. That school began operations in 2004 and now hosts 2,200 students, most of whom come from nearby communities.

Both schools are premised on the notion that there is a lack of education opportunities matched with market demand for labour and an over-supply for certain jobs. On that basis, the schools are focused on technical professions, including business administration, computing, and gastronomy, with additional courses offered based on the specific needs of the two communities. For example, CEDEC also includes a 450-student nursery, primary and secondary school, and five specialized courses, such as a three-year power-line technician program. Meanwhile, CEDHI has a soldering and metalworks program. Partnerships with the public and private sectors are at the heart of the business model and sustainability of both schools. In Arequipa, the Archbishop approached the Chamber of Commerce (Cámara de Comercio) to gather initial support for the school in Yura. He also leveraged contacts with the Fundación Santos Toledano in Spain. Land was provided at no cost from the government. While CEDEC has now evolved into an independent foundation, CEDHI continues to operate as part of Caritas Diocesana. To date, CEDHI has three classes of graduated alumni.

BUSINESS MODEL

CEDHI is located in one of the poorest areas on the periphery of the city of Arequipa in Southern Peru. The population of Yura includes migrants from Puno and Moquegua, attracted by the expectation of finding opportunity in the city. Currently, 400 students are studying at the school, taking courses of four months to up to three and a half years, including computing, business administration, home gas service installers, soldering, cosmetology, and gastronomy. In addition to offering these core courses, CEDHI has a personal development module that integrates psychology, sport, and art to reduce stress and promote broader personal development. All students are also paired with private tutors who serve the dual role of providing academic support and acting as life coaches to help students navigate personal and professional challenges.

Most students are 18 to 20 years old, but students can begin studies up to the age of 25. In some careers it is not necessary to have finished secondary school to attend, but students do have to pass a written exam demonstrating essential skills, including reading and writing. Students attend class for four to six and a half hours per day and are taught by professors who work part-time, some of whom volunteer or come from partner companies such as Caja Arequipa, Universidad Católica San Pablo, and Repsol. Students help with school maintenance and cleaning under the co-ordination of tutors.

To facilitate access to its courses, CEDHI offers scholarships to all students, who are only required to cover 20% of the cost of their studies. Further, tuition rates are adjusted based on the economic situation of the student. Typically, courses cost students on average S./160 per month. Students are not required to repay the scholarship following graduation, as in other education-focused social enterprise business models.

An essential aspect of the business model is a focus on teaching practical skills to students to provide them with a base of skills to support themselves and their families after graduating. All graduates are provided with work placement support, and 92% of students have successfully found employment to date. Recent changes at the Ministry of Education in Peru have facilitated the school's provision of competency-based education programs rather than programs based on set curriculums. For example, the business administration program has two tracks. The first is the SME track focused on helping students start and successfully manage their own businesses. The second is the office track, focused on providing students with the accounting and other skills needed to support office management. There is a heavy emphasis on English and Microsoft Excel skills for business administration students considering working in the tourism sector, including hotels. Another good example of the school's responsiveness to local labour market needs is its four-month soldering program. Unique to CEDHI (relative to CEDEC), the program addresses a deficit of skilled metalwork labourers in the region. Not only that, students generate income for the school by selling products to businesses in the region. The cooking program is another example. While Arequipa does not boast the same reputation as Lima for high-quality restaurants, the region has proud culinary traditions. At the behest of some students in the program, a traditional oven is being adding to promote traditional cooking methods.

Another core aspect of the business model of CEDHI is its use of partnerships to provide wrap-around services to students, based on the holistic, integral philosophy of the school. Since many students are young parents, free high-quality child care is offered on the school site. A community library is available to students. Health and nutrition campaigns are undertaken. Meanwhile, through an agreement with the Universidad Católica de San Pablo in Arequipa, communications courses are offered to teach students skills to help them express themselves in different academic, business, and social situations. As another example of an important partnership for CEDHI, the Caja Arequipa evaluates the business plans prepared by students for their thesis as part of the business administration program, and it finances the top three.

CEDHI promotes its programs through visiting high schools in the region, presenting the opportunity to students. Directors of the school estimate that it has land to expand to three times its current size. CEDHI is in the midst of adding a roofed sports stadium and is also considering the addition of a small microenterprise centre in partnership with Caja Arequipa.

SOCIAL IMPACT

At the entrance to CEDEC there is a Latin phrase written on an archway that reads: "Duc In Altum," in Spanish "remar mar adentro,"[43] which in English is literally, "row the sea within." The quote captures the education philosophy of CEDHI, where scholarships to support practical job training and placement along with broader holistic human development are at the heart of its social impact. It would be difficult to overstate the impact of making education accessible and providing it in a clean, safe environment for the communities of Yura and Ventanilla.

At CEDEC, students are offered free breakfast through Convida every day in an effort to combat anemia. The school is currently contemplating a similar lunch program. In addition, there is also a medical centre on site.

All students for both schools come from communities on the periphery of Peru's two largest cities. Many are young parents. Many come from conflict situations in their homes and arrive at the school with low self-esteem. Seventy percent of CEDHI's students are women. To sit and listen to thesis presentations by students during site visits is to see first-hand the profound impact of the education offered by CEDHI on the lives of its students.

FINANCING

Unlike in our first case study, CEDHI is a not-for-profit organization integrated with Caritas Diocesana. While it is not sustainable in the sense of operating self-sufficiently through the self-generation of income to cover all its costs, it is also not a charity in the sense of being entirely reliant on donations. CEDHI is a social enterprise navigating a hybrid approach to sustainability.

CEDHI's costs are covered through three sources: one-fifth of CEDHI's costs are covered through income from student tuition; one-quarter of costs are covered with income from sales from the soldering and metal craft program; and the remaining 55% are covered through a variety of in-kind and cash donations and contributions. These include, for example:

• Contributions from Caritas, including through income generated from management of land in the centre of Arequipa;

• Desks and boards from BanBIF;

• Land (20 hectares) owned by the state and provided free of charge for use by the school;

• Contributions from Caja Arequipa and la Universidad Católica San Pablo;

• Contributions from Michell & Cía S.A. (Industria lanera arequipeña);

• Direct project financing by the Catholic Cross USA and la Fundación Santos Toledano de España; and

• Direct operating cost coverage by la Fundación Ntra. Sra. del Perpetuo Socorro.

The directors of CEDHI continue to explore potential new lines of income to increase its self-generated income cost coverage from the current 45%.

At its root, the business and financial model of CEDHI and CEDEC is simple, aligned, and can be summarized in one sentence: Ask companies what education programs they need, create and offer those programs, and ask companies for support, financial and otherwise, in exchange. To date, this model has been easier to implement at CEDEC, since in Lima there is a larger business community from which to draw. There, the business model has also had more time to be refined. For each program, the school works with a strategic partner who provides four things:

• Market knowledge to create courses;

• 80% of the cost of tuition for students;

• Professors; and

• A network of industry contacts for job placements.

Perhaps pointing to the next evolution of CEDHI, CEDEC is operated by a foundation independent of Caritas and generates income to cover upwards of 60% of its costs from private partners and tuition fees. No financing is provided by Caritas.

PUBLIC SECTOR INTERACTIONS

CEDHI has not benefited from the public sector programs in Peru discussed elsewhere in this study aimed at innovation and entrepreneurship. Instead, it is an example of what is possible when someone with a vision brings together public and private stakeholders around an idea and a goal. CEDHI continues to be administered by Caritas. The original financing (cash and in-kind) for the school was provided by a broad array of public and private organizations: International Cooperation from Spain, Repsol, Comunidad Autónoma de Madrid, Junta de Castilla Leon, Fundación Entre Canales, among others, and from Peruvian companies including Minera Cerro Verde (a mining company), Cemento Yura and the Familia Tetino. Meanwhile, the government provides 20 hectares of land for use by the school free of cost. A final example of partnership not previously mentioned is an alliance with the Sociedad Picantera de Arequipa to provide a workshop to promote regional dishes and culture.

KEY LESSONS

CEDHI is an example of the power of partnership for sustainability. Through tuition and sales of products produced by students, the school now generates income sufficient to cover 45% of its annual costs. Over the long term, this percentage may increase through new initiatives. But to date, the school has sustained its positive social impact through its first half-decade, following the lead of its predecessor CEDEC, through partnerships. The collaboration of the church, state, private sector, foundations, and academia is forging a legacy and setting an example on the coast north of Lima and in the dry hot Cono Norte of Arequipa.

POLICY OPTIONS AND RECOMMENDATIONS

1. TAXATION

First, one set of policy options to support social entrepreneurship in Peru relates to taxation. Social enterprises are often providing goods and services traditionally funded by taxpayers and provided by the public sector, such as waste disposal, education, and healthcare, among others. Consequently, a compelling case could be made for differentiated tax treatment for these companies. This could include support for social enterprises with carefully designed income tax exemptions based on defined criteria. Alternatively, to attract difficult to find early-stage equity investment, consideration might be given to how dividends from social enterprises or investment funds domiciled in Peru are taxed.

Early-stage enterprises in Peru could also benefit from changes to value-added tax (VAT) rules, not least because at 18%, the VAT in Peru is among the highest in the LAC region.[44] When social enterprises make sales on credit but are required to pay value-added tax in advance of receipt of payment from customers, already acute working capital needs are exacerbated. Two potential solutions could be to align VAT payments with customer payments or to regulate the extent to which larger companies can buy from smaller companies on credit. For recent precedent, at the end of 2018, Chile passed Ley Pago a 30 días/Ley de Pago Oportuno, which limits invoice payments to 30 days for certain sales and imposes interest payments for late payments. Some have argued that this law could be further improved in Chile if the 30-day count started at sale rather than invoicing, and if the rules were differentiated by sector and size of business.[45]

2. PARTNERSHIP

Secondly, as seen in our case studies, partnerships between different participants in the social entrepreneurship ecosystem, including between the public and private sectors, can be an important component of sustainability. There are several important areas that don't have to do with the direct provision of funding where government can partner with social enterprises, including regulation, promotion and awareness, and business incubation.

Social enterprises in urban areas that focus on delivery of services usually delivered by the public sector may be in particular need of partnership with government. One example of how government might partner with social enterprises is through open communication channels to facilitate the adaptation of regulatory environments to make room for social enterprise provision of traditionally public services in areas where there are service gaps. For example, with respect to waste disposal and recycling, government is an important partner through the government's management of environmental impact studies, and through the issuance of operating licences by the

Ministry of the Environment.

Ultimately, to attract financing, social enterprises need creative and scalable business ideas. Facilitating generation of these ideas through business incubation and an open and transparent regulatory process and then promoting the ideas and increasing awareness among impact investors and other ecosystem members could be a highly beneficial role for the public sector.

CEDHI is an example of the power of partnership for sustainability. Through tuition and sales of products produced by students, the school now generates income sufficient to cover 45% of its annual costs. Over the long term, this percentage may increase through new initiatives. But to date, the school has sustained its positive social impact through its first half-decade, following the lead of its predecessor CEDEC, through partnerships. The collaboration of the church, state, private sector, foundations, and academia is forging a legacy and setting an example on the coast north of Lima and in the dry hot Cono Norte of Arequipa.

3.1 BLENDED FINANCE

Blended finance brings together concessional finance (usually public) with private for-profit finance in ways that share risks and sometimes returns as well. It leverages the fact that private and public sector investors have different incentive structures and perceptions of risk. A key objective can be to catalyze or "crowd-in" private sector investment where it otherwise would not be forthcoming. Convergence, a global network for blended finance focused on making the SDGs investable, describes it as a financial structuring approach that makes transactions investable, rather than an investment approach (like impact investing). Using a database[46] of blended capital transactions, Convergence estimates that every dollar of concessional capital brings in on average three dollars of private investment. Convergence defines blended finance as having three characteristics:

• Transaction expects to achieve a positive financial return;

• Transaction contributes to achievement of the SDGs; and

• The public/philanthropic party is catalytic and crowds in other private sector investment.

Our research highlights that many social enterprises in Peru are early-stage companies that impact investors perceive to not yet be ready for investment. This suggests a role for blended finance. Indeed, through Innovate, the Ministry of Production is already providing technical assistance-based grants with matching financing to support innovation and technology within the private sector throughout Peru.[47] This non-reimbursable grant financing supports specific projects and objectives and can also be complementary to direct private sector investment.

The public sector in Peru, potentially with international partners, could consider several other types of blended finance to catalyze impact investment for social entrepreneurship in Peru. In the following, three types are mentioned: performance-based payments, contingent recoverable grants, and first-loss capital.

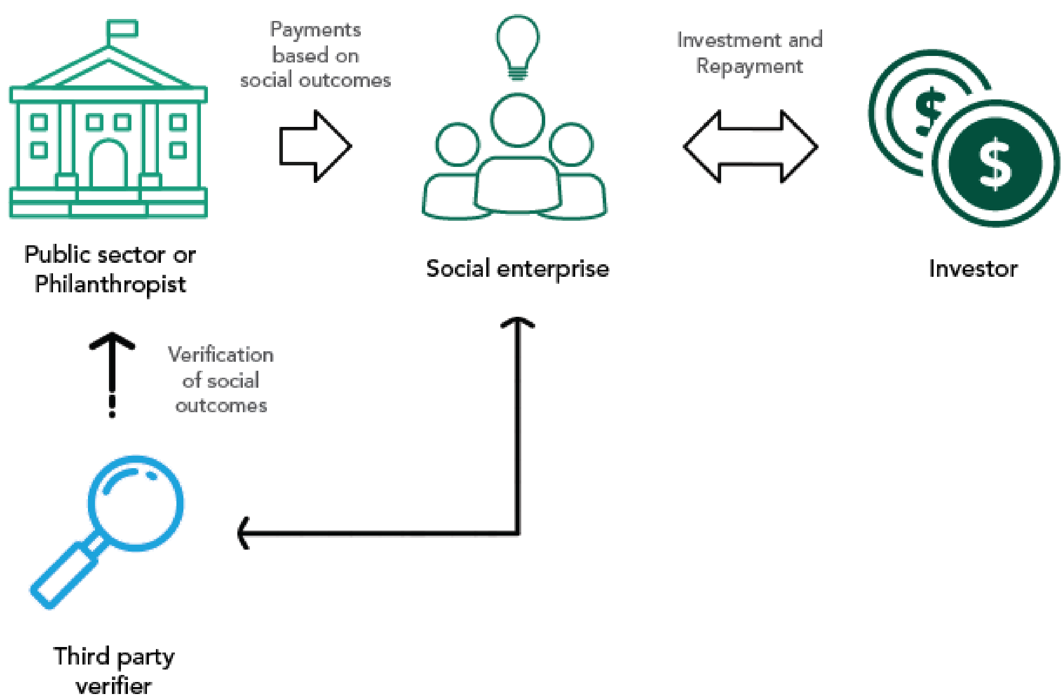
3.1.1. PERFORMANCE-BASED PAYMENTS

During interviews, several social enterprises discussed their interest in social impact incentives (SIINCs). The concept is explained in a 2016 white paper published by the Swiss Agency for Development and Cooperation (SDC) and Roots of Impact. A SIINC is a performance-based payment to a company based on achievement of specific measurable and verifiable social impacts. The grant funding becomes revenues to the company that are earned when the company delivers specific impacts. It awards a company for social performance (like a grant), immediately improves financial projections, and thereby could catalyze impact investment, which seeks both financial and measurable social returns. As the diagram below illustrates, there are three main players in the structure: the social enterprise, the impact investor, and the SIINC provider (likely a public sector institution).

FIGURE 16

Social impact incentives (SIINCs)

Source: Adapted from the Roots of Impact SIINC White Paper



SDC and Roots of Impact have been collaborating with the IDB Lab on a pilot of SIINC structures in Latin America. In 2016, two SIINC agreements were signed:

• For up to US$275,000 over two and a half years with Clínicas de Azúcar in Mexico to prevent diabetes through payments linked to decreasing sugar levels in low-income patients and an increase in low-income patients; and

• For US$195,000 over four years with Village Infrastructure Angels in Honduras to incentivize solar-powered agro-processing mills through payments linked to the number of milling hours saved by using electric grain mills.[48]

Inka Moss is a Peruvian social enterprise founded in 2010 that will also be participating in the pilot. Inka Moss sells sphagnum moss, which grows in the Andes, has an impressive absorption capacity, no market in Peru, and a high demand for fertilizer in Asia.

3.1.2. CONTINGENT RECOVERABLE GRANTS

A second option would be the development of financing buckets that provide market incentives to social enterprises by triggering repayment of grants once an enterprise achieves scale and is capable of repaying. Unlike traditional grants, this blended finance structure tries to incentive performance through market mechanisms. These grants could be based on a minimum commercial viability (MCV) level that is agreed upfront and measured with revenues or another metric, which would then trigger repayment within a defined time frame. Repayment could be made proportional to revenues beyond the MCV threshold. The contract could also include an equity conversion clause as additional security.

3.1.3 FIRST-LOSS CAPITAL

While a SIINC would make a social enterprise more investable by increasing revenues, guarantees reduce the downside risk by shielding investors from losses. Typically, in this structure a public sector institution will commit to absorbing initial losses from a company or a fund under defined circumstances. The circumstances could, for example, be specified adverse events or for investments (from a fund) in particular countries, technologies, or sectors. The Climate Investment Funds, including the Scaling Up Renewable Energy Program in Low Income Countries (SREP), is a prominent example where this investment structure has been used. In addition, in Chile, the Corporación de Fomento de la Producción (CORFO) offers guarantees for both fund administrators and companies.

3.2 FUNDING MECHANISMS

Blended finance structures could be implemented through direct contracts between the public sector with social enterprises or by working through private sector intermediaries. As discussed in the research findings, the absence of impact investment funds in Peru is conspicuous when comparing the country with its Pacific Alliance neighbours.

In Mexico there are several impact funds owned by Mexicans that are operating and raising capital in Mexico. One such fund is Adobe Capital, an impact investment and acceleration platform with more than 12 years of on-the-ground experience in the country, which recently raised close to US$30M for its second Mexico-only impact investment fund. The investment thesis for the funds is to "fill the gap of adequate growth capital ("missing middle") holding back promising SMEs with built-in impact potential." The fund provides tailored mezzanine structures and has focused on healthcare, education, housing, energy, and sustainable consumer products. This is the type of fund that could be promoted through public policy in Peru. In other cases in Mexico, INADEM has participated as a co-investor in investment funds.

Meanwhile, in 2018, fund manager Sudamerik launched the US$26M Impact Investment Chile with support from CORFO.[49] Also in Chile, Ameris, a financial services company, manages the US$4.5M Social Investment Fund launched in 2010 as the "first impact investment fund in Chile."

POLICY RECOMMENDATIONS

On the basis of the evidence and policy considerations discussed above, three policy recommendations are proposed in this section.

1. BOLSTER SUPPORT FOR THE DEVELOPMENT AND PROMOTION OF VIABLE SOCIAL ENTERPRISES. Impact investors perceive there to be a lack of opportunities for investment in viable social enterprises in Peru. To the extent this perception is reality, public sector policy could support the development of sustainable and scalable business models through the ongoing promotion of incubators, accelerators, and angel investor networks that invest much needed capital in early-stage companies. Public funding has supported these initiatives in recent years. An evaluation of the progress and impact of organizations that have received funding in support of such initiatives could inform how to target future support. Consideration could also be given to orient some of these efforts toward social entrepreneurship. Meanwhile, since regionalization and exports are often important to scale social enterprises in Peru, public sector support for networking platforms is also recommended.

2. CONSIDER FISCAL POLICY INCENTIVES TO PROMOTE SOCIAL ENTREPRENEURSHIP. Financing challenges for social enterprises are most acute for early-stage companies that are no longer startups but are not yet ready to scale with debt. Bank financing is risk averse and profitability is an important consideration. In this regard, consideration could be given to corporate income tax exemptions or other incentives for social enterprises (a term that would also need to be legally defined). The case for differentiated tax treatment is compelling in cases where social enterprises are filling public service provision gaps. In addition, rules could be established to mitigate the exacerbating impact on working capital needs of payment of value-added tax in advance of receipt of payment by clients.

3. CREATE NEW PUBLIC SECTOR FUNDING MECHANISMS FOR SOCIAL ENTERPRISES. Social enterprises in Peru receive public sector support during the startup phase and have started to attract international impact debt during the growth phase. However, there is a “missing middle” of early-stage companies that lack financing options. Angel investor networks in Peru are not focused on social enterprises to meet this need. The public sector could consider new funding mechanisms to meet this need, including direct financing of social enterprises and indirect financing through investment in funds or fund managers in Peru. Blended finance investment structures that include first-loss capital or pay-for-performance could be incorporated into the new instruments.

CONCLUSION AND NEXT STEPS

THE PURPOSE OF THIS STUDY was to explore the synergies between social enterprise and impact investing in Peru. Three types of evidence were examined: secondary research that made use of surveys and other quantitative data; interviews with social enterprises, impact investors, and other social entrepreneurship ecosystem participants; and two detailed case studies with social enterprises in Peru. Consideration of the evidence was guided by two questions, which are re-introduced below along with our conclusions.

THE CHALLENGE: WHAT OBSTACLES DO SOCIAL ENTERPRISES FACE WHEN FINANCING THEIR COMPANIES?

• *There is a high degree of reliance for funding on bootstrapping and friends and family;*

• *There is some government support for startups and innovation in Peru; and*

• *Access to finance is limited, particularly for early-stage social enterprises, due to high interest rates, guarantee requirements, and limited financial track records.*

THE OPPORTUNITY: WHAT ALTERNATIVE SOURCES OF FINANCE COULD HELP SOCIAL ENTERPRISES OVERCOME THESE OBSTACLES?

• *Blended finance with public funding mechanisms to catalyze impact investment; and*

• *Alternative impact-linked financing instruments.*

The challenge for social enterprises in Peru is that the social entrepreneurship ecosystem in Peru is nascent with a lack of funding sources, particularly for early-stage enterprises outside of the financial services and agriculture sectors. The opportunity is for government and the impact investment community to collaborate to implement innovative approaches to impact investing and to catalyze the emerging social entrepreneurship ecosystem in Peru.

ENDNOTES

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2. Global Entrepreneurship Monitor Peru 2016–2017.
3. Fostering social entrepreneurship for development. 2016.The case of Kunan: innovation that creates value. International Conference on Sustainable Development submission.
4. Study of Social Entrepreneurship and Innovation Ecosystems in the Latin American Pacific Alliance Countries. 2016. IDB.
5. Observatorio Estratégico de la Alianza del Pacifico (OEAP). 2018. Brechas para el Emprendimiento en la Alianza del Pacifico. Results are for all types of entrepreneurs.
6. Ibid.
7. LAVCA/ANDE 2018 Impact Investing Landscape in Latin America based on a survey of 67 impact investors with portfolio investments in Latin America conducted between February and May 2018.
8. http://www.produce.gob.pe/landing/retobio/index.html
9. PAD Escuela de Dirección de la Universidad de Piura; Ángel Ventures Peru, BBCS Capital, UTEC Ventures, and UP4angels (composed of graduates from the Universidad Pacifico).
10. Angel investors typically invest in high-risk enterprises with early-stage venture capital equity, while also providing mentorship and access to networks. Investments are typically high-risk and illiquid.
11. A similar view is expressed in “Brechas para emprendimiento,” page 93.
12. Public spending on research and development (R&D) as a percentage of GDP of 2.4% in OECD countries, 0.75% on average in Latin America, and 0.12% in Peru. https://peru21.pe/economia/peru-invierte-0-12-pbi-investigacion-desarrollo-193008
13. http://www.kunan.com.pe/

14 A global organization promoting high-impact entrepreneurs.

15 Part of Telefonica, they make small investments in startups in exchange for equity ownership shares.

16 An international accelerator program.

17 Kunan defines Social enterrases as: "Negocios, con o sin fines de lucro, que nacen con el propósito de atender desafíos sociales y/o ambientales que afectan a poblaciones vulnerables actuales y futuras. Son o están en el camino a ser auto sostenibles, generando sus propios ingresos y midiendo su impacto. Creen en el cambio sistémico y están transformando la manera de hacer negocios en el mundo." http://www.kunan.com.pe/

18 GIIN. Annual Impact Investor Survey 2018.

19 Graphic presentation of methodology adapted from "The Second Wave: Promoting a second decade of impact investing in frontier markets in Latin America."

20 Análisis del Sistema Microfinanciera Peruano. 2017. Equilibrium Clasificadora de Riesgo S.A.

21 OEAP op. cit. p. 65.

22 Global Impact Investor Network (GIIN). Sizing the Impact Investing Network.

23 In addition, the Impact Investing Landscape survey includes 11 funds in Brazil and 7 in Mexico.

24 Impact Investing Landscape. 2016. Based on data from the National Institute for Entrepreneurship (INADEM).

25 https://impactalpha.com/peru-tops-latin-america-in-impact-investments/; https://www.syminvest.com/news/peru-tops-latin-america-in-impact-investments/2018/10/16/7725

26 Study of Social Entrepreneurship and Innovation Ecosystems in the Latin American Pacific Alliance Countries.

27 Data from LAVCA/ANDE 2018 Impact Investing Landscape in Latin America, based on a survey of 67 impact investors with portfolio investments in Latin America conducted between February and May 2018. ANDE is the Aspen Network of Development Entrepreneurs, a global network of 200+ organizations that propel entrepreneurship in emerging markets. LAVCA is the Association of Private Capital Investment in Latin America.

28 Data from the LAVCA/ANDE 2018 Impact Investing Landscape in Latin America, based on a survey of 67 impact investors with portfolio investments in Latin America conducted between February and May 2018. Data is in millions of USD. “Other” includes energy, health, housing, education, sanitation, waste disposal, forestation, and water.

29 Refer to the “Final Reflections,” p. 17.

30 IDB. 2018. The Second Wave: Promoting a second decade of impact investing in frontier markets in Latin America.

31 Ibid., p. 35.

32 OEAP op. cit. p. 159.

33 ASPEN/LAVCA. 2016. The Impact Investing Landscape in Latin America. p. 131.

34 Refer to the “Regional Analysis: Chile, Colombia, Costa Rica, Mexico & Peru,” p. 8.

35 Ibid., p. 9.

36 Based on the GEM Perú 2016-2017, Encuesta Nacional a Expertos (NES), p. 61.

37 Categorization based on views of the author. Does not reflect the opinion of social enterprises.

38 Recent research shows that real lending rates in Peru are among the highest in the region. In 2016, Peru had rates lower than only Honduras and the Dominican Republic. The study states that “a number of countries in the region with low investment rates have high real interest rates and high banking spreads suggesting that in those cases, low savings and poor domestic financial intermediation may well be critical constraints.” Review of the study further suggests that the high rates appear to be driven by a large spread over the bank rate. Please refer to Caballo and Powell. 2018. A Mandate to Grow: Latin American and Caribbean Macroeconomic Report. IDB.

39 Several social enterprises commented that they resorted to taking personal loans and then on lending to their companies in order to obtain financing.

40 This finding is corroborated in the broader region in the 2018 GIIN Annual Impact Investor Survey.

41 An annual prize awarded to social enterprises.

42 NESsT was founded in 1997 and arrived in Peru in 2007 and has now fully invested its first US$7.0M fund in social enterprises. Its mission is to empower social enterprises to combat poverty through dignified job creation for vulnerable populations. NESsT has focused to date on investing between US$50,000 and US$500,000 in companies in Latin America that are not yet ready for commercial funding.

43 This is a quote from the Bible, specifically the Gospel of Luke 5:4.

44 Caballo and Powell. 2018. A Mandate to Grow: Latin American and Caribbean Macroeconomic Report. IDB. p. 51.

45 OEAP op. cit. p. 138.

46 Convergence has 1,055 investors in its database, over 50% of which are private. https://www.convergence.finance/blended-finance

47 Convergence estimates that 26% of all blended finance transactions are types of technical assistance, including grants before, during, and after private sector investment.

48 Innovations in Financing Structures for Impact Investors: Spotlight on Latin America. https://nextbillion.net/social-impact-incentives-a-new-solution-for-blended-finance/

49 Corporación de Fomento de la Producción - La agencia del Gobierno de Chile, dependiente del Ministerio de Economía, Fomento y Turismo a cargo de apoyar el emprendimiento, la innovación y la competitividad en el país junto con fortalecer el capital humano y las capacidades tecnológicas.

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