Catalytic Capital Case Study

KAYA IMPACTO Mexico

This case was prepared by Latimpacto and the Catalytic Capital Consortium

EXECUTIVE SUMMARY

Kaya Impacto is a B Corp organization thathas the purpose of strengthening the impact investment ecosystem in Latin America. In 2020, it played a key role in the development of the PES LATAM Emergency Fund created to assist, through financial and technical support, 14 social ventures in response to the effects of the COVID-19 pandemic.

The program was designed with a particular interest in amplifying impact through two instruments: impact-linked loans (Impact-Linked Loans) and impact-linked grants (Impact-linked grants). In the first one, $1.4 million were disbursed in 8 loans, which were 80% focused on companies in growth stages and 20% on companies that required support to survive. In the second, $103,500 were disbursed in 7 grants.

In order to ensure proper impact measurement and verify compliance with metrics, Roots of Impact's role was critical. However, the Swiss Agency for Development and Cooperation (SDC) played a major role as a financial catalyst by providing guarantees to cover potential losses and bond capital for impact payments. Thanks to its role, Open Road (USA) and Viwala (Mexico) were successfully engaged.

In addition, the program was notable due to its four catalytic aspects: (1) price, where impact-linked loans not only accepted lower yields due to terms favorable to ventures, with interest rates between 5% and 10%, (2) patient capital, with a payment term of three years (3) a focus on purpose, delivering up to a 35% discount on the total debt for meeting the impact goals (4) as a portion of the technical support, entrepreneurs acquired capabilities related to strategy, finance and impact measurement, which facilitated their access to new loans and new commercial agreements.

PES LATAM_Emergency COVID 19 Fund

Scope: Latin America
Ventures Supported: 14
Duration: 14 months (Round 1: July 2020 to December 2020; Round 2: April 2021 to September 2021)

SDGs:

Vehicle: Impact-Linked Loans and Grants and Technical Assistance

Loans: $1,400,000
Grants: $103,500
Linked to impact metrics: $400,000

Type: scaling (Expand capacity and impact of entrepreneurs)

Use: survive, facilitating innovation, leveraging additional investment

Role of catalytic capital:
price, patience, purpose

Actors:
- **Founder:** Swiss Development and Cooperation Agency
- **Investors:** Viwala, Open Road
- **Impact Incentive Structurer:** Roots of Impact
- **Structurers:** Kaya, PES LATAM

KAYA IMPACT: STRENGTHENING THE IMPACT INVESTMENT ECOSYSTEM

Kaya impacto is a B Corp financial consultancy which was founded in the transition between 2016 and 2017 with the purpose of strengthening the impact investment ecosystem in Latin America, betting on catalyzing capital and ensuring that entrepreneurs can access it in order to achieve their objectives.

As it began its journey, it identified low levels of professionalism and sophistication in the impact sector, and took on this challenge as an opportunity to improve processes, initially from investment funds. It focused on systematizing internal functions and processes so that funds could focus on attracting more capital to the social impact sector and on achieving their goals. So far, it has worked with more than 10 funds to define their methodologies in a structured manner, sharing lessons among them and working as ambassadors or experts in order to catalyze capital for social impact in the region.

Because of these needs, Kaya offers a wide range of services that span the various ecosystem players. For investors, it focuses on designing their investment thesis, conducting due diligence processes, and managing their portfolio so they can make more informed investment decisions and expand their impact. For entrepreneurs, it has diagnostic services and strategy and finance consulting, in addition to the ability to accompany them during the capital raising process. Finally, for other ecosystem organizations, it has tailored services for training, workshops and project management in impact investment.

Through these services, alliances and other strategies, Kaya has been an intermediary in raising $36 million, strengthening ninety-five organizations in seventeen countries and achieving a 90% success rate at raising capital.

In 2020, it was part of the PES LATAM Covid-19 emergency fund, playing two main roles. First, it co-designed and coordinated a program with Impact-Linked Loans and Impact-Linked Grants. Second, it provided technical assistance in strategy and financial management to entrepreneurs.

PES LATAM EMERGENCY FUND

PES Latam is a program designed to accelerate the growth of social enterprises in Latin America and the Caribbean, regardless of their sector or stage of development. In recognition of the complexity of this objective, it has a comprehensive portfolio of programs implemented in conjunction with specialized organizations which strengthen entrepreneurs through financial and non-financial support.

The entities which comprise PES LATAM (Social Entrepreneurship Promotion in Latin America and the Caribbean)

Ashoka: The largest global network of systemic change for social entrepreneurs.

Bridge for Billions: Create, design and manage innovation programs around the world.

LeFil Consulting: consulting firm specializing in inclusive businesses.

New Ventures: organization dedicated to catalyzing companies with Latin American social and environmental impact.

Swiss Agency for Development and Cooperation (SDC): Agency for international cooperation of the Swiss Federal Foreign Affairs Department.

VC4A: Global virtual community for startups, mentors and investors.

Source: https://vc4a.com/pes-latam/?lang=es

In 2020, PES LATAM designed and implemented the Covid-19 Emergency Response Program with the objective of providing financial and/or technical support to social companies in Latin America based on analyses of their situations:

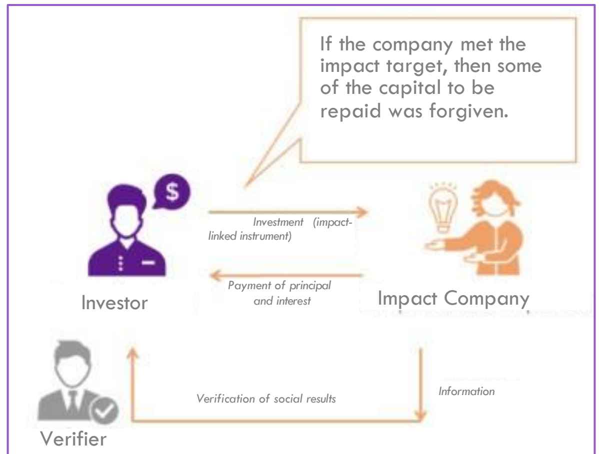
- 54% were affected by reduced income and lack of liquidity.
- 60% would face the decision to close the organization within four months.
- 80% would access low-interest money loans.
- 67% said their country's government had no measures for impact organizations.
- 97% do not have insurance to cover a critical situation.

Source: Community ES2 Latam VC4A

The information gathered showed the importance of creating a program to facilitate the survival of some businesses and the growth of others to counteract the effects of the pandemic. Additionally, a high percentage of entrepreneurs were found to be willing to access loans as long as they had low interest rates.

In response to these needs, PES Latam launched emergency funds with the Swiss Agency for Development and Cooperation (SDC) in July 2020, which provided guarantees to cover potential losses, as well as bond principal for impact payments. Thanks to this catalyst role, a combination funding fund alliance is created with Open Road (US), that offers quick, flexible and short-term debt to keep growth and impact going during critical "step-up" moments for impact-driven businesses, and Viwala (Mexico), a debt fund that uses blended finance models to close the financing gap for marginalized groups such as Women, LGBTQ+ communities, young opportunity and, in general, companies that have a positive impact on society or the environment.

In addition, Roots of Impact was responsible for designing enterprise metrics and impact assessment, LeFil Consulting participated in the selection and implementation of entrepreneurship grants, and Kaya Impacto co-designed and coordinated the secured debt program with Impact-Linked Loans, Impact-Linked Grants, and financial management Technical Assistance. Its roles included selecting entrepreneurs and coordinating the various players involved in the program.



Source: finanzasinnovadoras.org reference image

A fundamental aspect of these loans and grants was that the selection and disbursement criteria were primarily based on the impact generated by the venture. In the case of loans, payment obligations were linked to the achievement of social results, which were established with and verified by Roots of Impact. That is, if the venture achieved the impact objectives set forth, then a portion of the capital to be repaid was to be forgiven.

This approach sought to promote the maximizing of impact in vulnerable communities, putting this result above financial return.

The catalytic nature of this program is evident due to the increased risk assumed by SDC to leverage the participation of other investors. In addition, impact-linked loans not only accepted lower yields due to terms favorable for entrepreneurs, but are also patient capital with below-market rates and long-term return.

Terms and Conditions

	PES_ Covid-19 emergency	Traditional banking
Loan interest rate	5%	> 10%
Discount on debt due to goal fulfillment	Up to 35% of total debt	Not applicable
Term of Loan	3 years	> 3 years
Non-financial support	Strategy, Financial, Measurement	Not applicable

Source: Based on interviews

DUE DILIGENCE PROCESS FOR LOANS

Kaya played a critical role in meeting project objectives by being an enabling actor with respect to enabling both investors and entrepreneurs to achieve their purposes. Through advisory services, Kaya was a "translator" between two worlds with varying levels of understanding and different languages. Its experience was essential to strengthen entrepreneurs' financial knowledge and procedures. In addition, it played a crucial role in building proposals that met all investor and impact incentive structuring requirements, with some being novel and very sophisticated for the ventures.

The due diligence process for loans was conducted in fifteen steps, organized into three phases and a time (Phase 0) of program preparation and design under Kaya's coordination and in accordance with the Latam PES guidelines.

In Phase 1, the selection of ventures was sought, with these having been analyzed through an initial assessment, supplemented with interviews and a triage process. This rigorous process was designed to select the entrepreneurs that were prepared to properly use resources.

It is important to note that the fund selection and disbursement criteria were based directly on the impact generated by the ventures, and not just on the numbers presented at the beginning of the program.

Selection Criteria	Grants	Loans
Additionality and Use of Funds	a) Plan clear on use of funds, b) Alternative source of funding, c) Additionality	Not applicable
Financial Sustainability	Not applicable	a) Revenue growth, b) Clear unit economy, c) Solvency, d) Use of funds
Business Model	a) Articulation of the problem, b) Clear solution, c) Market size and trend, d) Scalability and growth potential	
Impact	a) Impact on the base of the pyramid and women, b) Additionality, c) Transferability and potential impact, e) Impact measurement	
Team	a) Quality of leadership, b) Commitment, c) Presence of women in leadership	
Potential to Survive	a) Impact of Covid-19, b) Risk management	

Source: Based on the case presented by KAYA at the Catalytic Capital Latimpacto bootcamp

In Phase 2, while eligible ventures were performing investor due diligence, Kaya performed independent technical assistance on ventures that applied for loans and grants but were not eligible according to predefined criteria. This process was coordinated by LeFil Consulting and Kaya took care of the financial advisories through weekly meetings in which it delivered:

- **Limited strategic advice**
- **Development of fundraising strategy and material**
- **Development of pricing strategy and financial model**
- **Technical Support**

Finally, in Phase 3, although the selected companies had gone through the funders' due diligence process, Kaya advised all companies on topics such as strategy, financial and capital management. Establishing the methodology and monitoring tools was part of the non-financial accompaniment that complemented the delivery of capital and which sought to generate long-term utility, by leaving behind installed capabilities to make decisions based on data.

ALTITUD'S BACKGROUND: FUNDING RECIPIENT

Altitud accessed the Impact-Linked Loans line and received a $250,000 loan with a 5% interest rate and a three-year term for repayment. This company was founded in 2011 and operates in the northeastern part of Mexico, specifically in Nuevo León. Its primary objective is to improve the economic opportunities of women heads of household, allowing them to increase their income while continuing to play their role as caregivers in the household.

Gabriel, the founder of Altitud, learned the stories of single mothers who were forced to leave their children home alone, often tied up, to go to work in textile factories. Although at first he thought they were isolated cases, his experience showed that this was a common situation, leading him to design a strategy to address this problem. After several visits and dialogues with these women, he identified that the main difficulty was the lack of productive assets to start working from home. That's why Altitud was established as a financial model for women, providing credits for the purchase of sewing machines that are then paid with the income generated from the work performed.

To generate more opportunities for its customers, Altitud became a sewing machine distributor, allowing it to provide better pricing, technical support and warranty. Additionally, it identified the possibility of providing technical advice (sewing, use of machines), such that it generated a line of productive courses and workshops to improve the textile production skills of its customers. With this knowledge and their own experiences and skills, some customers create small businesses with daughters, neighbors and/or their husbands, thus expanding their response capacity and income.

A more recent model that complements these services is Cricket textile (www.crickettextile.com) focused on removing intermediaries by taking on the role of facilitators in order to connect the supply (the designers) and the demand (national and international companies with social focus).

During the pandemic, the Altitud and Cricket model was very convenient, since women could work from home. While textile factories adapted to new ways of working, Altitud had more than 750 working workshops, primarily dedicated to the production of masks and other medical products.

Despite the adversity of the environment, the business model coupled with access to the PES LATAM Emergency Fund meant a growth opportunity for Altitud. Before accessing this fund, Altitud's main challenge was finding funding. On the one hand, traditional banking did not provide financing due to its business model. On the other hand, it had participated in accelerators, but annual interest rates were very high, they even turned to the search for investors to lower these rates, which amounted to 35% per year, a little bit. According to Altitud's multiple capital access experiences, Gabriel notes that the PES LATAM Emergency Fund has been the program with the best interest rate and the broadest payment term, allowing him to focus on defining a strategy and long-term planning.

Additionally, he emphasizes that the payment for impact was a very important incentive for him, because unlike loans focused on return, this modality allows for total concentration in the organizational mission and in amplifying positive impacts. He also highlights the importance of the non-financial support received from Kaya and Roots of Impact, since it enabled him to have a clear financial model and measurement system to challenge himself and to maintain focus on social impact generation.

RESULTS
AND IMPACT

SDC's catalyst role facilitated the participation of market-recognized investors and technical advisors due to its experience, enabling its contribution to impact ventures.

This experience served as proof of the viability of deploying capital quickly to address emergencies and the specific needs of entrepreneurs, provided there is a clear and structured governance process from the outset, as well as flexibility on the part of the stakeholders to address the challenges that arise along the way.

Below are some management data that quantify the scope of this project.

Results	
Loans	$1,400,000 distributed spread across 8 loans
Use of Loans Disbursed	Growth: 80% Surviving: 20%
Grants	$103,500 distributed spread across 7 grants
Social Entrepreneurships strengthened with technical assistance	20 Fourteen companies in Round 1 (9 companies to receive loans, 5 companies only received technical assistance), and 6 in round 2 in 2021 received technical assistance in order to potentially receive loans
Triage-assessed Social Businesses	36

Source: Based on interviews

For Altitud, the Latam PES program made a number of fundamental changes possible:

- It provided evidence of the need to separate Altitud from Cricket and create strategically differentiated business models.
- With Kaya's advice on financial education, Altitud left with an established financial model and the capabilities to properly analyze accounts.
- Payment terms reduced the pressure to source resources on a monthly basis in order to solve immediate problems, allowing the organization to focus, with the help of Kaya, on strengthening its portfolio, defining a long-term strategy, and creating a stronger portfolio.
- Without the financial pressure of short-term loans, Altitud was able to consolidate a business strategy that would drive growth by strengthening alliances and acquiring new customers.
- Participation in the program allowed access to new foreign credits and investments with more favorable interest rates.
- The increase in opportunities has also created better conditions for Altitud's clients, since by having lower interest from investors and lenders, it can offer better rates to its clients.

The above shows that in this program the catalyst effect is not limited to only low interest rates and the term of payments, but also it validates the potentiality of engaging with the ecosystem. Access to new investors has allowed Altitud to participate in events and projects that have a snowball effect, whereby new opportunities gradually add up.

The results obtained in PES Latam's Covid-19 Emergency Fund have positioned Altitud in the impact investment ecosystem and have provided credibility for new investors, many of whom contact program implementers, primarily Roots of Impact, to verify the information provided by Altitud.

FINAL COMMENTS

- **The Swiss Development and Cooperation Agency's guarantee was critical with respect to the attracting of other investors to the program.** Not only did their participation bring credibility and trust, but it also generated a multiplier effect by attracting the attention of other potential investors and key players in the entrepreneurial ecosystem, facilitating the generation of strong strategic partnerships and the support of recognized institutions that served as a determining factor for the program's success and scalability.

- **Technical support strengthens entrepreneurs' business capabilities, reduces their risks and facilitates access to financing.** This allows them to improve business management, understand key financial concepts and adopt good business practices. Additionally, clearly identify their capital needs and adopt appropriate financial practices to approach new investors and financial institutions; in addition to having a greater understanding of the risks associated with their businesses, identifying opportunities to mitigate them and developing sound risk management strategies, which can decrease the likelihood of business failure and increase resilience in the face of adverse situations.

- **There is a gap between investor requirements and the capabilities and/or knowledge of entrepreneurs.** The lack of financial knowledge and the terminology used by investors can create a barrier for entrepreneurs, rendering investor requirements and expectations difficult to understand . As a result, some entrepreneurs may feel overwhelmed and discouraged from seeking investment, especially those who do not have access to networks or resources that allow them to bridge this gap. That's why programs such as PES Latam's Covid-19 Emergency Fund are relevant. By providing not only funding, but also guidance, advice and support to entrepreneurs, they help close the gap between entrepreneur needs and investor requirements.

- **Patient capital programs allow entrepreneurs time to focus on strategy.** By accessing patient capital, entrepreneurs can spend more time and resources developing a strong strategy for their businesses. This allows them to analyze the market, identify opportunities, establish long-term goals, and plan more effectively. By having long-term financing, entrepreneurs are not pressured by short-term results, which encourages more thoughtful and well-informed strategic decision-making.

- **Lack of capital for impactful investment in Latin America is a barrier to developing catalytic capital programs.** Available capital from family offices, the financial sector and governments is primarily invested in the traditional high-yield sector. In this regard, available capital is not directed to impact projects and high-risk projects, although these could potentially generate even higher returns.

  For this reason, for Catalytic Capital programs, Latin American depends, in most cases, on foreign government capital and multilateral funds. While this is a breakthrough because it allows for greater coverage and impact on programs, it continues to face a huge challenge for local actors to act as catalysts in their own region.

- **It is important to encourage the participation of actors willing to take risks in impact projects in Latin America.** One way to do this is to replicate learnings and best practices from programs such as PES LATAM's Covid-19 Emergency Fund. It is crucial to overcome the perception that social and environmental impact projects are less profitable than investments in traditional sectors.

  In this regard, it is essential to promote education and awareness about the potential for the financial performance of impact projects, as well as their social and environmental benefits, in order to attract more investors that willing to assume these risks and strengthen the impact investment ecosystem in Latin America.

Latimpacto

2023