The Portland Trust

BUILDING AN IMPACT INVESTMENT MARKET IN PALESTINE

It is becoming ever clearer that there is an increasing need for innovative and effective solutions to society's problems. For instance, the UN's Sustainable Development Goals (SDGs) which target significant progress by 2030 on the most critical economic and social challenges facing developing countries, require between $3.3 and $4.5 trillion of investment each year. In addition to the need to mobilise additional financial resources, there is a growing recognition that meeting the SDGs will require effective public, public-private, and civil society partnerships as well as better measurements of progress[1].

Social impact investment, which has been growing globally over the last decade, could help tackle some of these long standing development challenges. Social impact investments, known as impact investments for short, are those that intentionally target specific social objectives along with a financial return and measure the achievement of both. They are already playing an important role alongside the existing financial flows to emerging economies.

Impact investment supports the growing number of impact driven organisations that are finding innovative and sustainable ways to address social problems. Impact-driven organisations, whether they be social sector organisations or businesses, have a long-term social mission, set outcome objectives and measure their achievement. By incorporating social motivations into investment decisions impact investment can provide capital to impact driven organisations that are not yet targeted by mainstream markets and provide longer-term more sustainable capital.

Impact investment provides an opportunity to bring new capital to Palestine and improve the effectiveness with which that capital is deployed. Palestine is a prime example of an environment where billions of dollars of donor aid have been deployed over the last decade. While some important results have been achieved, sustainable long-term progress remains elusive. Numerous development projects – estimated to have cost over $2bn since 2006[2] – have been implemented in the country over the last decade, but there is little robust evidence that traditional donor approaches have yielded desired outcomes. In many cases, the impact of an intervention, positive or negative, is unknown as it has not been measured. With a mounting public sector financing gap, declining donor assistance, and rising unemployment, a new approach is needed to mobilise and deploy funding.

In the light of significant global momentum, this report seeks to highlight how an impact investment market could work in Palestine and the opportunities that it could create. The report is structured as follows:

1. The Global Impact Investment Market
2. The Impact Investment Market in Palestine
3. A Framework for Growing the Impact Investment Market In Palestine

THE GLOBAL IMPACT INVESTMENT MARKET

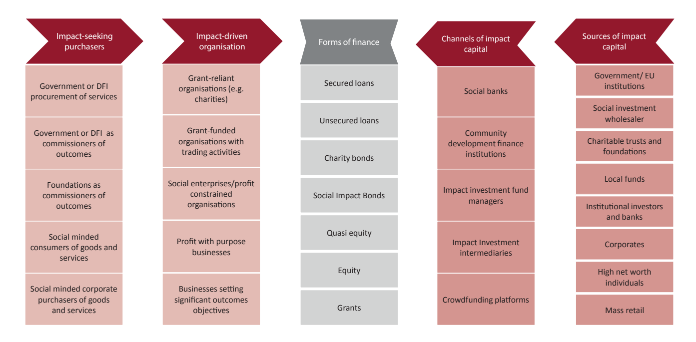
It is difficult to assess the size of the impact investment market, particularly in the context of international development, due to the lack of common definitions and reporting. However, the recent J.P. Morgan-Global Impact Investing Survey, reports that $10.6 billion in impact investments were committed in 2014[3]. Capital is diversified across regions with about half invested in emerging markets[4]. Development Finance Institutions (DFIs) – which include the private sector investment arms of bilateral governments, multilateral development banks, regional development banks and bilateral aid agencies – provide 74 percent of the total capital to impact fund managers based in emerging markets.[5]

This is just the beginning. The Social Investment Taskforce, established in 2013 under the UK's presidency of the G8, estimated that there is the potential to unleash up to $1 trillion of new investment to tackle social problems more innovatively and effectively.[6]

Impact investment, like any market, is a combination of demand (for capital to finance impact-driven organisations), supply (of impact capital) and intermediaries (helping to connect supply and demand).

1 https://sustainabledevelopment.un.org/focussdgs.html [see goal 17]
2 PMA data – development expenditure financed from grants and donations.
3 https://thegiin.org/assets/documents/pub/2015.04%20Eyes%20on%20the%20Horizon.pdf
4 https://thegiin.org/assets/documents/pub/2015.04%20Eyes%20on%20the%20Horizon.pdf
5 https://thegiin.org/assets/documents/pub/2015.04%20Eyes%20on%20the%20Horizon.pdf
6 Impact Investments: An Emerging Asset Class, J.P. Morgan and the Rockefeller Foundation, November 2010, pp. 6 and 11

Social Impact Investment Ecosystem[7]



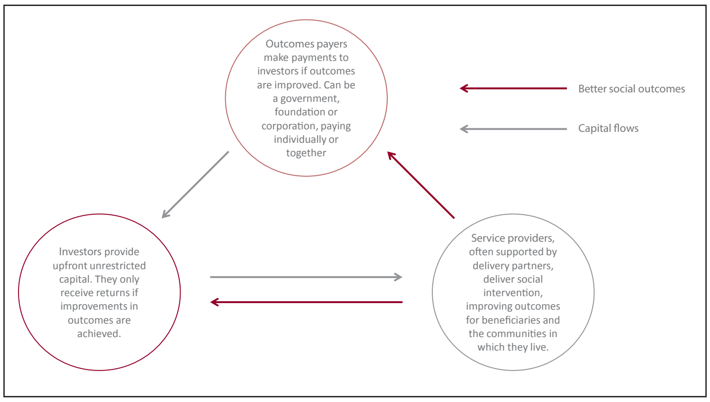
There exist a range of funds that have been making impact investments in emerging economies. For instance, Acumen Fund raises charitable donations and investment capital to make early stage investments in small businesses that are solving some of the world's toughest social problems.[8] Grassroots Business Fund combines investment capital and business advisory services to support income-generating businesses in low-income communities.[9]

Impact investment can also help catalyse other sources of funding. As an example, in September 2013, The Gates Foundation with the help of JP Morgan, launched the Global Health Investment Fund, which has raised over $100 million from impact and commercial investors to develop drugs that are in the late stages of testing, as well as new technologies, that can help improve health in the developing world. The Gates Foundation has guaranteed to cover losses made by the fund, up to the first 20%, although Bill Gates says he expects it to eventually make a good profit while at the same time helping save tens of thousands of lives.[10]

One way that impact investments can have greatest impact for development is through the linking of funding to outcomes. There is a growing movement among DFIs toward funding approaches that pay on the basis of outcomes (e.g. reduced unemployment) rather than activities (e.g. sessions for people who are unemployed).[11] A key benefit of this approach is that recipients of funding can focus on the strategies that are needed to achieve results, rather than focusing on reporting on how donor-funded inputs are spent.[12] This creates the space for innovation and learning to take place and, through that process, for longer-term development impact. At the same time, outcome-based approaches require that data is collected on the impact of the programme.

As with results-based contracting approaches, impact investment requires setting objectives and clear results metrics. Impact investment comes in many different forms and some models yield financial returns only when some social objective has been met. For example, the model of social impact bonds (SIBs) is that impact investors provide investment capital to service providers – which can be any combination of public agencies, private companies and non-profits – and are repaid by public sector agencies (and/or possibly foundations or corporations) if programmes lead to the expected results, with levels of returns commensurate to success. This approach thereby directly links social impact with financial returns. The market for SIBs is growing. Over 50 SIB contracts have been signed globally and dozens of SIBs are being developed across the world[13]. The first SIB was launched in the UK in 2010 and that is where the highest number can be found with 33 SIBs launched to date.

Social Impact Bond structure[14]



The Development Impact Bond (DIB) is an innovative idea that has much in common with the SIB, but with the crucial difference that bilateral aid agencies, foreign aid ministries, multilateral institutions and philanthropists pay for the outcomes delivered instead of the local government. DIBs are still in their infancy. The first was announced in June 2014 by the Children's Investment Fund Foundation and UBS's Optimus Foundation to improve the quality of girls' primary education in Rajasthan, India[15].

THE IMPACT INVESTMENT MARKET IN PALESTINE

Impact investment could harness the existing entrepreneurial nature of the Palestinian economy for social good. With its focus on achieving demonstrably improved outcomes, impact investing has the potential to give organisations with a social mission a better chance of success. This includes social sector organisations that want other sources of capital besides traditional grants from charitable donors or government, and businesses that decide to put a social mission at the core of their business model.

Local entrepreneurs, businesses and foundations have expressed an interest in impact investment. Paltel Foundation – one of the largest philanthropic foundations in the country – is interested in how to incorporate impact investment into

7 Schematic from Impact Investment: The Invisible Heart of Markets Report of the Social Impact Investment Taskforce 2014
8 http://acumen.org/
9 http://www.gbfund.org/
10 Cited in Impact Investment: The Invisible Heart of Markets Harnessing the power of entrepreneurship, innovation and capital for public good, Report of the Social Impact Investment Taskforce Established under the UK's presidency of the G8
11 The Center for Global Development-Social Finance Development Impact Bond Working Group report reviews the landscape of results-based contracting for development (CGD 2013). The working paper Incentive Proliferation? Making Sense of a New Wave of Development Programs discusses in more detail the ways in which results-based funding programs for development can be classified (Savedoff, 2011).
12 Birdsall and Savedoff, 2010, Cash on Delivery Aid

13 Brookings, Potential and Limitations of Social Impact Bonds, July 2015
14 Schematic from Choosing Social Impact Bonds by Bridges Impact Plus and Bank of America Merrill Lynch 2015
15 https://ciff.org/grant-portfolio/education-development-impact-bond/

its strategy. A number of leading Palestinian corporates have expressed an interest in being one of the first investors in a Palestinian DIB.

Impact investment could build on the existing entrepreneurship scene that has emerged and the different initiatives which have been put in place to help launch and support innovation. Dr Abdulmalek Al-Jaber, CEO & Chairman of Arabreneur, told the Bulletin that "We are seeing a growing number of entrepreneurs that want to create products and services that help communities grow and prosper. Over the last three years, we have invested in start-ups of impact at different levels and stages of development. For instance, in our first round of investments, we invested in Edunation, which is improving the education system in a social and digitalized way. Today they help more than 80,000 students from the MENA region and outside."

Shadi Atshan, Director of Leaders Organization, believes having some sort of impact investment mechanism could help solve some of the problems that exist in Palestinian society. "Leaders would be most interested in establishing an impact investment fund that invests in technology start-ups that solve a social or environmental problem specific to Palestine or the region." He believes that equity rather than loans or loan guarantee funds would be the most useful financial products for social entrepreneurs. "Loans structure and procedures are highly complicated in Palestine, also they require a high level of insurance. This limits risk taking by any entrepreneur. Equity investments not only provide the cash, they also provide the experience and connections provided by the equity fund or venture capitalist."

Impact investing is happening now. Ambar Amleh, COO of Ibtikar Fund sees Ibtikar Fund as a prime example of impact investing. "First, most of our investors are wealthy individuals, the vast majority from the diaspora, investing for the first time in Palestine (they are used to donating, but not to expect returns). All of them are doing this looking for a dual bottom line, not only expecting profits but also a positive social and economic impact. As a fund, we also expect to have a strong social impact in job creation and the training and development of CEOs and CTOs, for example. I think this should be the way forward for Palestine, moving away from aid and towards a more private-sector-led economy."

The Portland Trust has taken a market building role for the promotion of social impact investing initiatives in Palestine. It has sponsored a number of workshops in Ramallah and Jerusalem, bringing together Palestinian businesses and international organisations with leading impact investing practitioners from the UK, including Social Finance UK (SFUK) and Bridges Ventures.

Bridges Ventures is a specialist fund manager dedicated to sustainable and impact investment, set up in 2002. Following her visit to Palestine in September 2015, Emilie Goodall, Director at Bridges Ventures Impact+ reported that "Impact investing could play an important role in Palestine, as a mechanism to bring together different actors (private, public and social sectors) to deliver not just jobs but also progress in fields as diverse as agriculture, energy, housing, healthcare and education. There is a clear need for capital, particularly of the innovative, risk-taking kind that impact investment so often provides."

There are a growing number of intermediaries globally, such as Bridges Ventures and SFUK, who can support the use of impact investment. These organisations could help local investment funds measure impact, support corporates or foundations seeking to develop impact investment strategies, and enable international donors to integrate impact investment into their private sector development initiatives.

As a result, momentum is building and some corporates and development finance institutions are exploring the development of impact investing mechanisms. The World Bank, as part of a recently launched private sector development programme aims to create a DIB, to support private sector focused skills development in Palestine. This would be the World Bank's first DIB worldwide.

Stefanie Ridenour, Private Sector Development Specialist at the World Bank, announced that "The DIB aims to enhance employment outcomes and skill development amongst youth and women in Palestine. One of the key reasons a DIB model is exciting and promising is that it more actively involves the private sector. There is a clear need to better link the demands of the private sector with the skills of the labour market in a more market-driven way. The DIB will focus on people aged 18 to 29 years old with a targeted share of 30% women. The DIB is designed to catalyse the role of the private sector by crowding in both private sector capital and expertise to better incentivise employment outcomes".

The Portland Trust is also working on two DIBs to help tackle pressing social issues in Palestine. First, in close cooperation with SFUK, The Portland Trust has prepared an initial programme design for a DIB to address the growing Type II diabetes epidemic in Palestine by focusing on prevention through an intensive lifestyle intervention. Second, The Portland Trust, in partnership with Palestine Technical University in the West Bank, is working to establish an integrated agricultural centre that would serve as an enabling platform for Palestinian farming communities and funded through a DIB.

Peter Nicholas, Director at Social Finance UK, has worked closely with development partners and sees a significant potential for impact investing in Palestine. According to Nicholas, "there's a particular opportunity for Development Impact Bonds in Palestine, given the need for a clear focus on verifiable results and working capital to finance investment to achieve those results". He identified significant opportunities for improved service delivery in a range of areas including health, vocational education and extension services.

FRAMEWORK FOR GROWING THE IMPACT INVESTMENT MARKET IN PALESTINE

A bigger, more dynamic impact investment market would have important benefits. While the first components of a market have been emerging in Palestine, it is embryonic and needs support.

To help the impact investment market reach its potential, this report sets out five priority actions that could accelerate the rate of market development.

1. Support coordination and collaboration between DFIs. At this early stage of development, improved coordination and strengthened collaboration in the area of impact investment by DFIs would do much to help increase capital flows to the social sector. In particular, shared efforts to issue pay-for-success securities such as DIBs and SIBs, impact evaluation, and co-financing could accelerate the application of outcome-based impact approaches. Lessons from the World Bank's DIB could help prime and test the market for the introduction of additional impact investment initiatives by other DFIs.

2. Explore the creation of an Impact Finance Facility to provide early-stage risk capital. DFIs could create an Impact Finance Facility (IFF) that would proactively support the development of the impact investing market by encouraging testing of diverse investment models and instruments and stimulating an ongoing flow of potential impact investing transactions. An IFF including grant funding to boost capacity-building, would bolster the demand side of the market and better connect supply of investment with demand from impact-driven organisations. To address current shortcomings in the impact investing market, the IFF would help match needs for capital for early stage business development with technical assistance, and it would also share information and best practice publicly.

3. Encourage DFIs and government to explore how SIBs and DIBs might contribute to greater efficiency in the delivery of services. Development agencies, impact investors, philanthropic foundations, and other interested players could support the testing of DIBs and SIBs in emerging markets. SIBs and DIBs are a new model for public private partnerships that attract private investment and align incentives toward achieving social outcomes. DFIs could accelerate experimentation and learning about DIBs by contributing to an independent DIB Outcomes Fund which would make funding available to pay for the results of successful DIB-financed programmes, and stimulate the development of transactions. In addition to funding from official donors, the Outcomes Fund could seek grant financing from foundations that want to catalyse the development of pilots to test the concept. The UK Cabinet Office's Social Outcomes Fund and the Big Lottery Fund's Commissioning Better Outcomes provide a blueprint for how this could work in practice.[16] These funds pay a proportion of outcomes payments for SIBs in complex policy areas, as well as support to develop robust proposals.

4. Improve metrics and increase transparency. There is a need for clear definitions and comparable, accessible data for the growth of the impact investing market. All participants in the impact investment market could clearly distinguish between indicators that measure commercial performance and those measuring social outcomes, and could use harmonised standards for outcome and impact metrics, both social and financial, across different sectors. A range of impact measurement tools are now available including the Portfolio Risk, Impact and Sustainability Measurement (PRISM), Impact Reporting and Investment Standards (IRIS), the Global Impact Investing Rating System (GIIRS), and the Global Reporting Initiative (GRI). DFIs could identify impact objectives across their portfolios and more clearly and intentionally "tag" those projects or portfolios that constitute impact investments, building on the work of OPIC and the Inter-American Development Bank in this area. Locally, the Palestinian Central Bureau of Statistics could play a pivotal role in providing evaluations of new and existing impact investment programmes and supporting the development of better metrics.

5. Support research, knowledge sharing and awareness raising to help the market mature. This could build on the work of The Portland Trust and others to build knowledge-sharing platforms to raise awareness of impact investment in Palestine. Potential initiatives could include providing grant support for the sharing of knowledge and best practices amongst government, enterprises, and investors as well as strengthening platforms for dialogue. International examples of these platforms include the SANKALP FORUM in Asia and Africa, SOCAP in the USA, global and local investor platforms such as GIIN and Indian Impact Investor Network.

It is clear that there is much more that impact investment can do for development in Palestine and globally. There is an important role for DFIs such as the World Bank and others. The impact investment market is already gathering momentum but without leadership from government and the DFIs, its development will be slow and its impact more limited. Implementation is a matter of urgency.

16 http://bit.ly/1PZaTM5

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The Palestinian Economic Bulletin is prepared and edited by The Portland Trust. Please send any comments suggestions or complaints to feedback@portlandtrust.org