GENEROUS PROFITS

Social enterprise investing blurs traditional lines between business and charity

By Peter Shadbolt

It's not necessary to travel all the way to Kenya, Tanzania, or Malawi to visit the frontiers of the global economy. A quick trip to the neon world of Chungking Mansions in downtown Kowloon, a stone's throw from Hong Kong's financial center, provides an unparalleled petri dish of the global economy in action.

Inside the infamous 1950s tenement building—a fabled flophouse for backpackers and down-at-heel business travelers—scores of African traders are cutting deals with wholesalers for thousands of knockoff Chinese mobile phones.

Amid the squeal of packing tape coming off reels, shipping cartons are wrapped in China's ubiquitous striped woven plastic fabric, known simply as red-white-blue, and their destinations are hastily scribbled in marker pen: Abidjan, Lagos, Nairobi.

Hundreds more phones are de-boxed on the spot and stuffed into sports bags as carryon luggage. Traders—often arriving with empty bags and carrying nothing apart from the clothes they are standing in—can make upwards of dozens of trips a year between Africa and Hong Kong.

With a baggage allowance of around 23 kg and a carryon allowance of 7 kg, as many as 600 phones can go back on each trip, but traders often use the extra baggage allowed with frequent-flyer points to shoehorn even more handsets into every trip.

If there were any doubt that mobile telephony is a game changer for Africa, then a quick trip to Chungking Mansions would immediately lay it to rest.

For Dambisa Moyo, a Zambian-born economist and vocal critic of African dependence on Western aid, the humble Chinese knockoff mobile phone represents a quantum leap in the motor forces of Africa's economies.

"What is happening in Africa with the mobile phone is nothing short of amazing. It's being used to trade everything—even livestock. It's being used for the transportation of money from one city to another," Moyo says on the sidelines of an emerging markets conference in Singapore.

Its applications are now so ingenious, she says, that Western financial companies are borrowing technologies and applications from Africa.

"It is revolutionary," Moyo explains. "People that have traditionally been locked out of the financial system are being brought in."

It is in exactly this space that social enterprise development—where companies nurture micro-, small-, and medium-size businesses with a view to making a socially positive impact as well as a profit—is targeting investments.

The M-Pesa money transfer system devised by Vodafone and Kenya-based Safaricom, the country's largest mobile operator, is one of the best illustrations of a system in which aid, development, and profit find common cause.

Initially launched as an experiment in creating a development impact through a private sector solution—and seeded with as little as £2 million in competition money—the system was designed to aid Kenya's millions of citizens without bank accounts in transferring cash, obviating the need for bank accounts, bureaucracy, and sometimes long journeys to settle accounts.

Safaricom launched the service in 2007 after partnering with Vodafone on initial concept development. For the two mobile operators, the synergies were obvious; in exchange for Vodafone's strong technology solutions, Safaricom allowed Vodafone a strong presence in one of the world's fastest-growing markets.

What happened next surpassed even the most optimistic expectations.

The unmet need in the market was massive: M-Pesa now has 18 million customers and almost 80,000 retail agents throughout the country, constituting a previously untapped revenue source and providing a way for Safaricom to retain its mainstream mobile customers.

With it, account holders can transfer funds, pay bills, purchase goods and services, and make bank transactions.

"Its [success] was unexpected, but the origin of the product really came from Vodafone, who had some kind of big idea about how we could use the mobile phone for deepening financial inclusion," explains Bob Collymore, chief executive officer at Safaricom. "I think at the time, they didn't really quite know what that meant."

Originally, he says, the intention had been to develop a system for women, usually the recipients of microfinance, to repay micro-loans cheaply and quickly. But when Safaricom's management team looked at the application, they saw it had the potential to meet a broader need.

"Many people move money from urban to rural districts in Kenya, and the way to do that traditionally was simply to give somebody cash and to take it back home to the family," he said.

"Effectively, it's a mobile money transfer system, but it's developed a hell of a lot since then.

"People are now using it to pay school fees, to pay taxes, traffic fines, and more recently, in the past year, we have extended it to give people the ability to save and to borrow," says Collymore.

Other uses have also penetrated the service in a country where just over 50% have bank accounts but 68% have used a mobile phone to make a monetary transaction, according to World Bank data.

"It's being used for microinsurance. People are paid their salaries with M-Pesa. Distributors like Diageo, who need to deliver beer to bars, are taking M-Pesa payments rather than have the delivery lorry go around with cash," says Collymore.

Recently, it's even extended into Kenya's burgeoning real estate and rental market with a service called Lipa Kodi—Swahili for "pay your rent."

Kenya's rental market is a large and growing segment (the latest census estimated there were 6.5 million rental households) as the country rapidly urbanizes. Valued at around 17.2 billion Kenyan shillings (US$200 million), it represents a fifth of the total value of the real estate market in Kenya.

Little wonder that M-Pesa, after a short five years, contributes almost 20% of Safaricom's total revenue.

"The other side effect of all this is that it's created 79,000 agents. And while they're small—they're just kiosks really and it might not be the kiosk holder's exclusive job—we estimate it has created half as many jobs as that," says Collymore.

"It was originally designed for or aimed at those at the bottom of the pyramid, but the fact that we now have about 18 million users says everything about it. I use M-Pesa pretty much all the time," he says.

"You can transfer as much as 140,000 Kenyan, which is about US$1,500–US$1,600 per day, which for many people in Kenya are pretty large chunks."

For Collymore, M-Pesa is an example of social enterprise done properly—a system that not only has a clear social benefit but returns a profit as well. For detractors of Africa's dependence on foreign aid, such as Moyo, applications like M-Pesa are the way forward.

"It's very rational for African governments to take the aid; I would take the aid too if I were them," Moyo says. "The reason I am critical is because it's eroding the political infrastructure."

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"I had one African person say to me," she adds, "that taking aid was the choice between traveling around the world to be abused by hedge fund managers and pension fund managers asking uncomfortable questions about why they should invest in my country or sitting back with my wife and kids in sunny Africa and having aid organisations come in making promises."

Ironically, even as systems like M-Pesa undermine the old aid models, aid organisations are using M-Pesa themselves to direct cash payments.

"When it was started, it wasn't even conceived as a social enterprise; I don't think it was even a popular term at the time," says Collymore. "But now, USAID, which distributes aid—and often this aid evaporates; it's stolen—these guys use M-Pesa to get the benefit directly to the person who is receiving it."

The Vodafone and Safaricom experience in Kenya highlights one of the key concepts of social enterprise investment: that low-income populations in emerging markets offer high-volume, low-margin profits in the short term and a significant consumer and supplier base in the long run.

Corporations are learning that not only do investments made today have the potential for high returns in the future but also operating in low-income markets helps them to innovate to create low-cost products, create new business models, and develop supply chains that work well.

Such investments also allow companies to try out new approaches in relatively untested markets, improving risk management in their core business.

Managing social enterprise activity provides businesses with the means to look closely at new operating environments and to build relationships within that region.

Ashwin Subramaniam, typical of the new breed of social entrepreneurs, ditched a stable job at RBS (Royal Bank of Scotland) to create Gone Adventurin', a Singapore-based social enterprise that works with companies in low-income markets.

Its business model is simple: Take the employees of a well-known company or brand, put them on bicycles, and then take them on a long journey through the base of the pyramid.

The company then films the trip, creating documentaries that reach out to larger audiences.

Last year, B.P. de Silva Holdings, Singapore's oldest family-run business, approached Gone Adventurin' with the idea of marking its 140th anniversary by supporting communities in Sri Lanka, a country critical to its heritage, and maximizing return on investment in brand marketing.

The result was Cycle on Ceylon, a custom-branded project based on the cycling adventure of B.P. de Silva Holdings' employees and directors through Sri Lanka, which took them from misty mountains and sandy beaches to battle-scarred towns.

"Gone Adventurin' is a social enterprise that helps companies create projects that take people into an immersion experience into a country or a community where the company can then make an impact," Subramaniam says.

"Back in the day, corporate social responsibility was very much about just writing the cheque, giving it to charity, or taking a group of employees on a once-a-year event like visiting an orphanage," he says.

"We believe that's outdated and CSR needs to be embedded in the business. We don't want to be a consultancy that just gives reports to people; we actually want to help them implement it as well."

His group has just completed an 800-km bicycle journey with Standard Chartered Bank, which took 15 bankers, including the CEO for the Mekong region, on a journey across Indochina.

"This helps them to understand what's happening on the ground in terms of business and to get a sense of how, as a business, they can create social impact."

He said the biggest motivation for companies was often to raise awareness about what they were already doing to create a social impact. Standard Chartered, for instance, already has a well-established project combating avoidable blindness around the world.

"When people on the ground see the work, there's a greater chance of them buying that product. A huge part of people's buying decision is the perception they have about the company," says Subramaniam. "If someone in a small family in Indonesia perceives the company as something that does good for the local community, there's a higher chance of the person buying that product."

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Hong Kong–based SOW Asia Foundation makes investments in individuals and enterprises that it believes will make a sustainable social and environmental impact.

"By 'sustainable,' we mean commercially self-sustaining," says Scott Lawson, chief executive officer at SOW Asia, a hybrid charity that invests donations in private sector operations that are likely to have the greatest impact.

"It's a big space that's growing bigger all the time," he explains. "Once upon a time not too long ago, there was either profit maximising or the charitable world and a wall between them.

What we've seen in the past generation—and even in the past 10 years—is really more diversity and different ideas coming in between these two polar positions."

The convergence has come about, he says, as companies—once hell-bent on maximising shareholder value at all costs—begin to take stakeholder value seriously.

"Some of the early examples of that are what we would call socially responsible investing; this was initially a negative screen where shareholders refused to invest in tobacco or gun manufacturers or gambling," says Lawson.

"Now it's evolved into the next space, where there is a positive screen and investors are looking at for-profit organisations that have prioritised impact and want to do it on a sustainable basis."

In many respects, he says, this generational shift has reversed the roles of traditional charities and businesses.

"Traditional charities are increasingly being asked by their donors to account for the difference they're making," Lawson says. "They're being asked to measure the outputs and outcomes they're creating.

"What you're seeing," he continues, "is traditional charities being asked to function more like traditional businesses and businesses being asked to be more like traditional charities. It's quite an interesting time."

Measuring these outcomes is still far from an exact science, and Lawson says that data are still being assessed as the sector continues to mature.

"This is something that we and others are spending a lot of time on," Lawson says. "I would say that we're getting better at understanding the data and how to aggregate it. We're still at the point where it's difficult to compare social investment across the sector.

"It's still subject to a lot of interpretation. We need to work more on the quant side, and we also have to be careful how we use those numbers because a lot of it is context specific and context driven."

SOW Asia has just closed a deal investing in a Hong Kong–based recycling company (recycling being a pressing environmental issue in a densely populated area where landfill capacity is expected to be exhausted within a few years) but is strategically placed to take advantage of new markets in the region.

"We are extremely interested in what's happening in mainland China, but there are many challenges around transparency and governance. The social-impact space is still quite nascent in China," Lawson says.

"China is extremely fragmented, but there's a lot of interest in this space among investors. The other positive is that the Xi government seems more receptive to looking at innovative solutions to some of the challenges that China faces, especially on the environmental side."

From the point of view of large financial institutions, impact investing—defined as the placement of capital into social enterprises and other structures, such as loan, equity, or infrastructure projects, with the intention of creating benefits that go beyond financial return—is still a relatively small segment but one that is growing.

According to Yasmine Saltuk, director of research for J.P. Morgan Social Finance, the past 18 months have seen a shift in the pattern of interest in impact investing.

"There's been more interest from mainstream institutional investors," says Saltuk. "Prior to that, there was much more outreach from us to the client base. That flow of inquiry has reversed, so we're getting more inbound requests."

She said perceptions have changed as impact investing has become increasingly mainstream—a factor she attributes to wider media coverage, a greater awareness among governments eager to find private sector solutions to problems that previously had strained public budgets, and shareholder pressure.

"Probably at the beginning of the market, it was more in the blogosphere, whereas now, it's being covered by the *New York Times*, the *FT*, *Institutional Investor* magazine, *Forbes*—these are mainstream media outlets.

"In terms of government attention, this has changed over the past couple of years," she says. "We actually published something in 2011 which was just recognizing that governments among the G–8 were beginning to support the impact investment market; we noticed that as a trend among individual governments."

"This year," Saltuk continues, "there was a formal launch of the G–8 Social Investment Taskforce, so across these governments, they're now working together to try and promote the development of the market.

Thirdly, and most importantly, the shareholders or stakeholders in pension funds or asset managers are getting increased inquiries from their client base, so it's just getting harder to ignore."

A J.P. Morgan survey in early 2012 titled "Perspectives on Progress," which consisted of interviews of some 99 impact investors, found that respondents planned to invest US$9 billion in the sector in 2013, up from US$8 billion in 2012.

Investors surveyed for the report included fund managers, development finance institutions, foundations, diversified financial institutions, and other investors with at least US$10 million committed to impact investment. Two-thirds of respondents were pursuing market-rate financial returns.

"The question on returns is a challenging one simply because of the newness of the market," Saltuk says.

"The oldest investments for the majority of the market are maybe just four, five, or six years in—and these tend to be 10-year funds—so the realized return data that we have is really minimal because there are only a handful of investors who have been doing it longer than that."

At the moment, the expectations of respondents for returns are as strong a guide as any to the relative strength of the sector.

"A significant portion of the market does expect their investments can be competitive to a similar nonimpact investment," Saltuk says, adding that investors need to be clear on what impact they want to have and then determine whether there is a revenue-generating business model that can deliver that impact.

Moreover, she points out, investors are becoming increasingly knowledgeable about working in such a diverse marketplace.

"We just marketed a health fund, for example, and our fund focused on malaria, tuberculosis, and HIV—problems endemic to Africa. And we had responses from investors who were interested in health saying, 'I'm interested in health and maybe even health in Africa but just not those diseases,'" Saltuk says. "It can get to that level of granularity."

The best business models, in her opinion, are those that are scalable and that can deliver products and services to customer bases where there is not a lot of competition.

Under this definition, M-Pesa stands out as a stellar example of social enterprise investment—a product that helps meet a strong social need but isn't inimical to profits.

"M-Pesa is a flying success. It's an exceptional business model," Saltuk says, adding that Kenya's low technological base allowed it to leapfrog technologies to deliver the very latest systems to some of the world's poorest people. "Because it was a blank slate, they had the opportunity to jump straight in, and there was a lot of demand straight away."

Peter Shadbolt is a freelance journalist and writer based in Hong Kong.

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"Impact Investing: How Do You Measure Social and Environmental Impact?" *Enterprising Investor* (23 September 2013) [blogs.cfainstitute.org/investor]

"Has the Climate for Climate Bonds Changed?" *Enterprising Investor* (18 November 2013) [blogs.cfainstitute.org/investor]

"New Frontiers," *CFA Institute Magazine* (July/August 2013) [www.cfapubs.org]