STANFORD SOCIAL INNOVATION *review*

Blog : Constructing the Case for Impact Investment

This post is one of a two-part series.

It is nothing new to say that the Internet is a tremendous resource for gathering information. However, when it comes to starting a business, entrepreneurs in particular have the benefit of digging up a wealth of articles and blog postings from a vital audience: investors. Interestingly, investors seem to be a fairly vocal class of Internet participants whether it comes to formal articles, blog posts, or even tweeting on Twitter. Seems investors love giving unsolicited advice.

As an early-stage investor, I enjoy reading what other investors have to say on topics from valuation to deal terms to the state of a particular sector. Some of the angel investors who keep blogs have a knack for writing such excellent, insightful pieces on early stage investing that the posts could just as easily be required reading in any business school course on entrepreneurship. However, in the impact space, there isn't much information applying general startup topics to the unique challenges and idiosyncrasies of investing in the developing world and, especially, for the benefit of bottom of the pyramid consumers (the three billion people who live on less than **$2.50 per day**).

With that in mind, here is a pair of questions that all social entrepreneurs need to be thinking about when approaching impact investors and making the pitch for investment capital. I have singled out these questions because of the frequency at which they arise in our discussions as we screen potential BoP-focused investment opportunities. Bear in mind, these are not the *only* questions social entrepreneurs need to think about, but simply important ones that have special complexities in relation to the BoP marketplace.

Question #1: What is the management team's commitment to the target (geographic) market? As with any investment, impact or otherwise, the analysis starts and ends with the management team. Outside of social enterprises, an investor wants to see an entrepreneur go all in. Usually, that comes in the form of a financial commitment and time commitment. "Quit your job, mortgage your house"—that's the level of commitment some (perhaps, many) traditional investors want to see.

Social entrepreneurs focusing on the developing world need to show this level of commitment—and more. We tend to see a lot of US-based companies that operate (or will operate) in developing nations. That is certainly all right, but there are a number of questions that arise out of situations like this one. If the entire management team is located in the US, who is on the ground overseeing operations? Furthermore, if the going gets tough, how do we know they will stay? What partners do they have in the region? What ties do they have to the geography, and how strong and/or permanent are those ties? Social entrepreneurs have to answer these questions. However, I can count on one hand the number of business plans and presentations that offer a thoughtful discussion to address these issues. Instead, the focus is on items of traditional significance, such as management's pedigree. Bottom line is that when it comes to evaluating a management team in the impact space, I say this: pedigree is actually far less compelling than relevance. The question of commitment to the target (geographic) market gets to the core of a management team's relevance.

Question #2: Will consumers accept the product or service being offered? Obvious, right? After all, customer acceptance is part of any good business model. Actually, when the focus is on the BoP consumer, this question rises in importance and therefore requires far more consideration than the standard business strategy might require.

There is plenty of literature out there about **design theory** for products and services aimed at BoP consumers. If you are a social entrepreneur focusing on the BoP audience, get familiar with this issue and, importantly, how it applies to your social enterprise. Again, the bottom line is this: BoP consumers in the developing world will not simply buy a better mousetrap just because it's better. In most cases, the majority of your target audience is not using the current mousetrap, and conventional notions of value propositions and payback periods won't sway those who are. Explaining why BoP consumers will accept your product or service in the unique context you are providing it is crucial.

Linking Questions #1 and #2. When it comes to customer acceptance, nothing beats field trials and seeing the product in action. Successful or not, meeting the market, learning what it has to say, and using that information to refine everything from the product's core features to the overall business model is part of building a viable enterprise. This is true in any sense, but given the nature of the customer acceptance issue with BoP consumers, it is of the utmost importance. We will always want to know about your beta customers, what they have to say, and whether any of them were so pleased with your product that they became evangelists for you and helped sell others during the field trial or initial launch period.

Naturally, the commitment of the management team is key to this process. In order to feel the full effect of meeting the market, the management team has to be there, on the ground, learning and gathering feedback first-hand. Not only do we have suspicions about the veracity of field trial results not conducted by the management team, but we have doubts about whether the feedback from it will be incorporated as it should be. As you can tell, social entrepreneurs who successfully answer question #2 will be able to support and back up their answer to question #1. When you have done your homework on the customer and show how your design will resonate with the target audience, you can construct a compelling narrative that not only articulates your commitment to the audience, but resonates with impact investors as well.

Read part two of this series, "**Investing Beyond Exit**."

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