Impact investing: If Oxfam did hedge funds...

Meet the most improbable new entrant to the financial services arena this year: Oxfam.

As one of the world's leading anti-poverty charities, Oxfam has spent much of its illustrious campaigning history trying to defend the poor from the worst excesses of big corporates. But for its latest venture, it's actually working in tandem with the private sector: it has teamed up with fund manager Symbiotics to launch the Small Enterprise Impact Investment Fund, which will support financial intermediaries in developing countries.

The fund only launched in July, but it has already done its first deal, providing $1 million in senior debt to Mongolian company XacLeasing. The plan is that Oxfam and Symbiotics will raise up to $100 million over the next three years, which they'll pass on via a range of financial instruments (to include both debt and equity) to lenders, leasing companies, investment funds and so on.

So why is a third sector organisation suddenly trying to get into the investment business?

It's important to note that Oxfam won't actually be managing the fund; it will leave that to Symbiotics. Instead, its role will be to act as an 'impact adviser', measuring the effectiveness of its investments. What's more, this fund can be seen as a natural extension of Oxfam's previous work on sustainable livelihoods – which in recent years, has focused heavily on enterprise development.

"The small business sector is very important for economic development," says Alan Doran, Oxfam's Business and Finance Adviser. "In developed countries, SMEs [small and medium sized enterprises] contribute a very large chunk of GDP. But in developing countries, it's much weaker." Much of the focus lately has been on micro-lending; but according to Doran, SMEs are actually a better route to job creation and possibly even poverty alleviation. What's more, poor people often value banking services like savings accounts and so on more than the ability to borrow money.

However, there's a credit issue here, he says. Big companies can get credit easily enough, and these days, thanks to micro-lenders, so can very small enterprises. But for SMEs, 'the missing middle', it's a different story.
As a result, there's been a "seismic shift" in thinking within development finance area, he suggests: rather than trying to help everyone become an entrepreneur, the priority now has become getting credit to SMEs. This is the gap the SEIIF hopes to fill.

BEYOND THE USUAL SUSPECTS

Of course, identifying the problem is one thing; trying to fix it by branching out into financial services is quite another. But Doran says Oxfam decided it would have "much more credibility" in the enterprise discussion if it was an active player on the scene, rather than commentating from the sidelines.

And there's a bigger prize at stake here – which explains Oxfam's evolving relationship with the world of finance. "In the last five to ten years, we've had a much more complex engagement with the private sector; we recognise that it can be part of the solution, not just part of problem," he says. "We want to be part of a movement that harnesses private capital to work for pro-poor development. We recognise donations and government funding will both always be heavily constrained, so the prize of liberating a chunk of capital markets to move in this direction is a huge and worthwhile one."

Part of this plan involves trying to attract investors who would not typically invest in a fund like this (i.e. not just the development finance institutions). "We're keen to raise awareness and extend our range of investors beyond the usual suspects," says Doran. "We want to bring in different classes of investors – foundations, high-net-worth individuals, family offices…"

To this end, SEIIF is structured in a pretty investor-friendly way. It's open-ended, so investors can get out at the end of any quarter (given sufficient notice). It will contain a mixture of debt and equity; Doran expects the deals to be largely debt-focused to begin with, to give greater certainty on returns and rolling yields (an essential part of the liquidity offering), but in time there will be some mezzanine and equity investments in there too.

So while SEIIF is currently offering investors a "five percent plus" return – which Doran admits is not high enough for some of the institutions the fund manager talks to – he expects that to look more like six to eight percent towards the end of that three-year period. "As the fund gets bigger and matures, we'll add some higher risk/higher return instruments. So we think the profile of the return will rise."

THE HARD SELL

Getting up towards eight percent should certainly make SEIIF easier to sell to a broader range of investors. However, it is likely to run into the same issue that many impact investors continue to face, i.e. how it should fit into a standard LP portfolio. In fact, it might even have a harder time than most, purely because of its structure: it actually looks much more like a hedge fund than a standard private equity fund, which could make it harder to slot into a 'private equity' bucket.

Nonetheless, for those LPs with an active interest in impact investment, SEIIF will no doubt be an attractive concept. For one thing, some of them may have no other way of backing the sort of intermediaries the fund is targeting, because the companies concerned will be too small to meet their minimum investment threshold level.

Equally, given how long Oxfam has been on the ground in these countries, it has better credentials than most to throw light on an area that remains difficult for impact investors: how to measure specific impact. Interestingly, despite the huge amount of theoretical work that is going into developing common standards within this burgeoning asset class, Oxfam says it will focus on one very simple, very measurable statistic: quarterly (or possibly bi-annual) job creation.

This will no doubt be easier said than done, depending on the intermediary concerned (an investment fund will be much closer to its portfolio companies than a lending bank, for instance). But it should at least act as a decent proxy for economic development; and in time, it should also encourage the intermediaries to channel their lending to those SMEs with the best employment growth prospects.

SEIIF will be holding its next close in late September / early October, by which point it is hoping to have accumulated around $2 million. To date, its money has come from its core sponsors, Oxfam, Symbiotics and the City of London Corporation, plus a small number of high-net-worth individuals and a “small charitable foundation”. A private client and a pension fund may also be in the next close.

So there’s a long way to go to get to that $100 million – and many investors will clearly want to wait and see whether SEIIF can deliver proof of concept before they even think about putting money in. “We’ve discovered that a lot of people are waiting in the wings; they want to know if these guys are serious, if they can make an investment successfully, if can they do what they say they’re going to do,” says Doran. That may take a while yet.