

THE LANDSCAPE FOR IMPACT INVESTING IN EAST AFRICA



WITH SUPPORT FROM



**THE
IMPACT
PROGRAMME**

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GIIN Advisory Team

Amit Bouri, abouri@thegiin.org

Abhilash Mudaliar, amudaliar@thegiin.org

Hannah Schiff, hschiff@thegiin.org

Laura Gustafson, lgustafson@thegiin.org

Open Capital Advisors

Annie Roberts, aroberts@opencapitaladvisors.com

David Loew, dloew@opencapitaladvisors.com

Neal Desai, ndesai@opencapitaladvisors.com



LIST OF COMMON TERMS AND ACRONYMS

AFD | Agence Française de Développement (French Development Agency)

AfDB | African Development Bank

BIF | Burundian Franc

BIO | Belgian Investment Company for Developing Countries

BoP | Base of the Pyramid

CEPGL | Communauté Économique des Pays des Grand Lacs (Economic Community of the Great Lakes Countries)

COMESA | The Common Market for Eastern and Southern Africa

CSR | Corporate Social Responsibility

DFI | Development Finance Institution

DFID | The Department for International Development (United Kingdom)

DRC | Democratic Republic of the Congo

EAC | East African Community

Early-stage business | Business that has begun operations but has most likely not begun commercial manufacture and sales

EIB | European Investment Bank

ESG | Environmental, Social, and Governance

ETB | Ethiopian Birr

FDI | Foreign Direct Investment

FMCG | Fast-Moving Consumer Goods

FMO | Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (Netherlands Development Finance Company)

Focus countries | Countries under the study where non-DFI impact investors are most active in. Namely Ethiopia, Kenya, Rwanda, Tanzania, and Uganda

GDP | Gross Domestic Product

GEMS | Growth Enterprise Market Segment

GIIRS | Global Impact Investing Ratings System

GIZ | Gesellschaft für Internationale Zusammenarbeit (German Agency for International Cooperation)

Growth-stage business | Company has a functioning business model and its current focus is developing new products / services or expanding into new markets

HDI | Human Development Index

ICC | International Criminal Court

ICT | Information and Communication Technology

IFAD | International Fund for Agricultural Development

IFC | International Finance Corporation

IMF | International Monetary Fund

IRIS | Impact Investing and Reporting Standards

KES | Kenyan Shilling

LP | Limited Partner

Mature business | Profitable company with a developed and recognizable brand

MDG | Millennium Development Goal

MFI | Microfinance Institution

MSME | Micro, Small and Medium Enterprise

NGO | Non-Governmental Organization

Non-focus countries | Countries covered in the study but have limited non-DFI impact investor activity. Namely Burundi, Djibouti, Eritrea, Somalia, South Sudan, and Sudan

OFID | OPEC Fund for International Development

OPIC | Overseas Private Investment Corporation

PE | Private Equity

PPA | Power Purchasing Agreement

PPP | Purchasing Power Parity

PPP | Public-Private Partnership

PTA | Preferential Trade Area Bank

RDB | Rwanda Development Board

RFP | Request for Proposal

RWF | Rwandan Franc

SACCO | Savings and Credit Co-operative

SAGCOT | Southern Agricultural Corridor of Tanzania

SDG | Sudanese Pound

SGB | Small and Growing Business

SME | Small and Medium-Sized Enterprises

SOE | State-Owned Enterprises

SOS | Somali Shilling

SSP | South Sudanese Pound

TA | Technical Assistance

TIC | Tanzania Investment Centre

TZS | Tanzanian Shilling

UGX | Ugandan Shilling

UN DESA | United Nations - Department of Economic and Social Affairs

UNCTAD | United Nations Conference on Trade and Development

USAID | The United States Agency for International Development

VAT | Value-Added Tax

VC | Venture Capital

Venture-stage business | Sales have begun but cannot sustain the company's operations. The business model is still being aligned with the realities on the ground

WASH | Water, Sanitation, and Hygiene

WHO | World Health Organization

EXECUTIVE SUMMARY



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INTRODUCTION

East Africa is one of the centers of global impact investing, as activity has grown strongly throughout the region over the past five years. More than USD 9.3 billion has been disbursed in the region through by more than 1,000 direct deals by development finance institutions (DFIs) and other impact investors active in East Africa today (Figure 1).¹ In total, 155 impact investors currently manage 203 active investment vehicles in the region, and many more are considering the region for future commitments.²

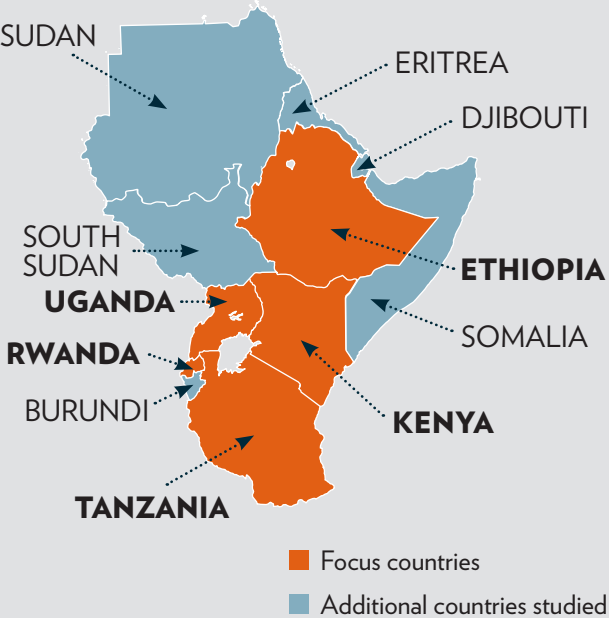
Kenya and its capital city Nairobi are the regional hub of East African impact investing. At least 48 impact fund managers have staff placed in Nairobi, which is more than three times as many local offices as in any other country in the region.

Almost half of the USD 9.3 billion in impact capital disbursed in East Africa has been in Kenya—more than triple the amount deployed in each of Uganda and Tanzania, the countries with the next highest amounts at around 13% and 12% respectively. Despite having the largest economy in the region (in PPP terms), Ethiopia has received only around 7% of disbursements to date. Rwanda, with an economy just one-eighth the size of Ethiopia’s, has received half as much impact capital, or 4% of all disbursements in the region.

ABOUT THIS REPORT

This report presents a detailed analysis of impact investing activity in East Africa, examining the supply of global impact investment capital as well as the demand for investment resources from small and medium enterprises (SMEs), social enterprises, and others who aim to drive social and environmental impact through the private sector. The report covers five “focus countries” in depth: Kenya, Uganda, Tanzania, Ethiopia, and Rwanda; and six additional countries in the region in less depth: Burundi, Sudan, South Sudan, Djibouti, Eritrea, and Somalia.

For the purpose of this report, impact investors are defined as those who invest with the intention to generate a beneficial social or environmental impact alongside a financial return—and who seek to measure the social or environmental returns generated by their investments.



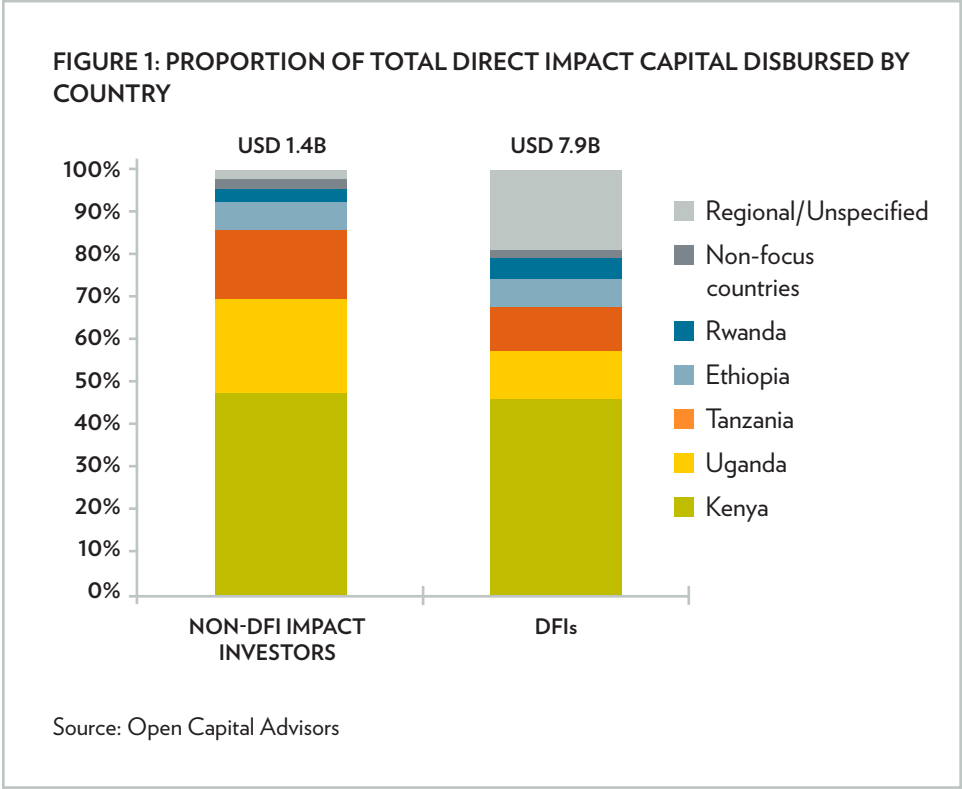
1 Open Capital Research. Based on primary and/or secondary research conducted during this study. Please see Introduction and Methodology chapter of this report for details.

2 Throughout the report, DFI investors are analyzed separately from non-DFI investors, to highlight the differences between these two categories. See the Introduction and Methodology section of this report for further information.

Notably, the research team was unable to find any evidence of impact investment activity in Eritrea or Somalia, and only minimal activity in Burundi, Sudan, South Sudan and Djibouti. Though development finance institutions (DFIs) are often active in these countries, the majority of support provided is through bi-lateral or multi-lateral government loans.

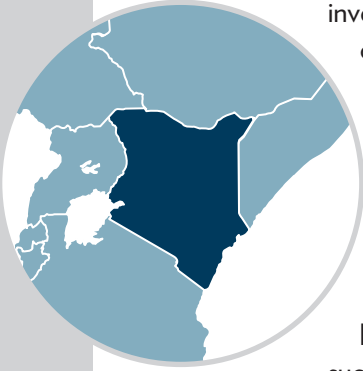
Throughout the region, DFIs have provided the vast majority of impact capital to date, accounting for more than 85% of disbursements. As shown in Figure 1, Kenya receives almost 50% of the regional disbursements for both DFIs and non-DFI impact investors, but DFIs have generally spread investments more evenly throughout the rest of the region. In the focus countries, there are fewer deals made by DFIs than by other impact investors, along with a higher average deal size for DFIs. The regional and country chapters explore the nature of these disbursements in depth.

Most East African impact investors work across the region, and many look beyond East Africa to Sub-Saharan Africa and other regions of the world to deploy capital. In practice, these impact investors do not typically divide their capital to country-specific pools, but rather invest opportunistically across the markets they cover. This means available capital could be deployed elsewhere if sufficient investment opportunities are not found in East Africa, or the funding could grow rapidly if impact investors see more promising opportunities inside East Africa.



COUNTRY SUMMARY: KENYA

Kenya is the heart of East African impact investing. It represents nearly half of impact capital disbursed in East Africa—more than USD 650 million by non-DFI impact investors and more than USD 3 billion by DFIs. Nairobi is the physical hub for impact investing in the region, where 48 impact investors have local offices, and is often the first port of call for impact investors operating in the region, even if they look for opportunities beyond Kenya.

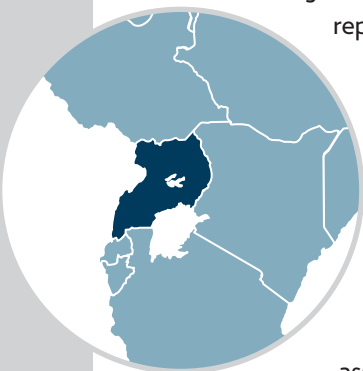


Kenya is so dominant that some impact investors express concern that the Kenyan impact investing landscape is already saturated. However, ongoing security concerns as well as challenges common to the region have kept impact investing activity in Kenya from reaching its potential. Kenya offers the advantage of more readily available human capital compared to other countries in the region. But like other countries in the region, the informal nature of many businesses poses challenges for investors, and there have been few examples of successful exits.

Impact investors expect Kenya to offer strong investment opportunities in the future and to retain its central position in the region. Rapid economic growth, a growing middle class, and an increasingly robust business ecosystem drive this optimism. The Kenyan banking sector has been moving aggressively to expand SME lending, and SMEs increasingly gain access to financing through both impact and conventional sources. Impact investors are actively looking for deals in Kenya's fast-growing second-tier cities, highlighting opportunities in agricultural aggregation, renewable energy, and mass market consumer goods.

COUNTRY SUMMARY: UGANDA

After Kenya, Uganda is the second most active country in East Africa's impact investing landscape, attracting approximately 13% of capital disbursed by impact investors. Impact investors appreciate Uganda's generally favorable business climate and regulatory environment, and do not report any significant country-specific challenges to investment.

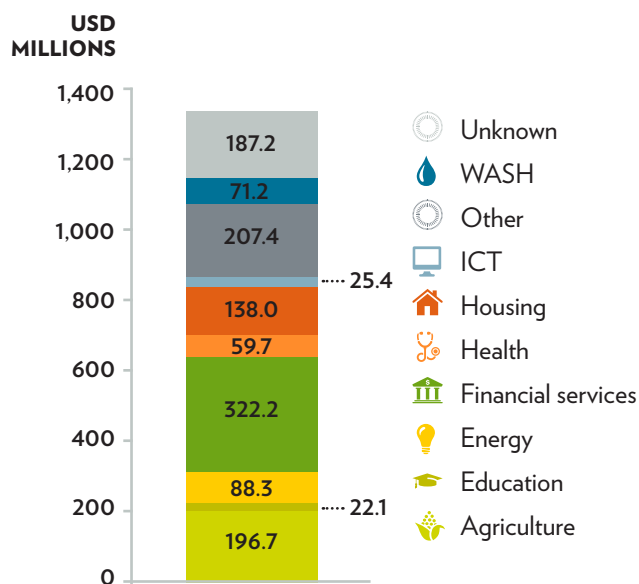


Nevertheless, Uganda's investment climate has not yet reached the maturity of Kenya's, and investors in Uganda face many challenges common to the region—difficulties in acquiring talent for middle management, managing informally operated businesses, and few examples of successful exits have kept deal flows below potential.

At the same time, Uganda's growing economy is expected to offer opportunities to impact investors in the future, particularly those able to draw on technical assistance facilities for pipeline building and able to look for deals outside of the capital city of Kampala. Uganda is one of the most fertile countries in the region, but its agricultural sector lacks organization and technological sophistication. Investors therefore particularly highlight businesses that build agricultural value chain efficiency as attractive opportunities, along with renewable energy and water and sanitation to serve Uganda's large off-grid and urban populations.

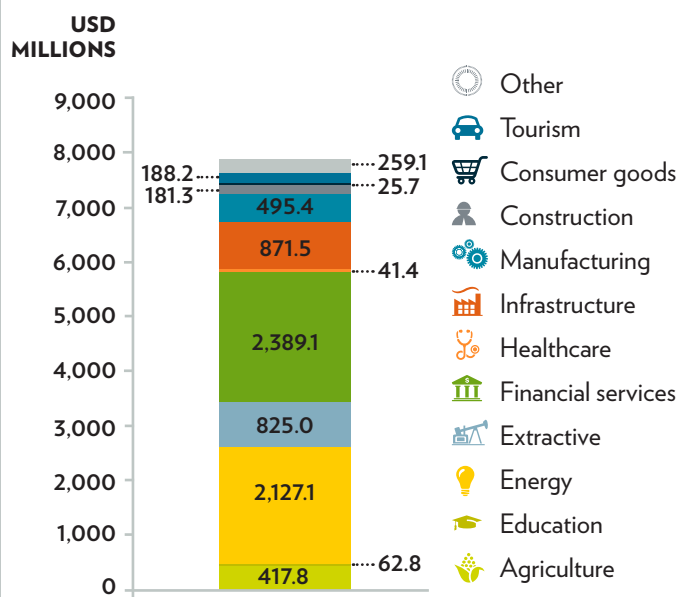
Both DFIs and non-DFI impact investors have disbursed more capital in financial services than in any other sector, accounting for nearly 30% of overall capital disbursed. The sector is attractive to many different impact investors as it offers an opportunity to reach large customer bases through well-established local businesses with many years of operational experience. Preferences between DFI and non-DFI investors diverge for other sectors. DFIs typically favor large deal sizes and government backing available in energy, infrastructure, mining, and manufacturing projects, while non-DFI impact investors have been particularly active in agriculture and affordable housing. Despite their compelling impact narratives, impact disbursements into basic services such as education and healthcare have been relatively limited to date.

FIGURE 2: NON-DFI IMPACT CAPITAL DISBURSED BY SECTOR



Source: Open Capital Advisors

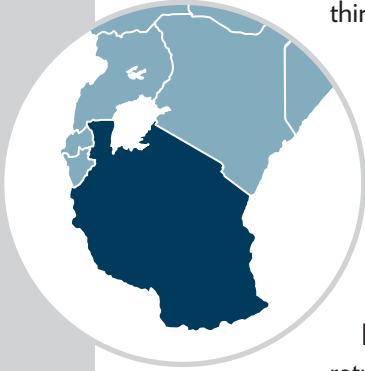
FIGURE 3: DIRECT DFI IMPACT CAPITAL DISBURSED BY SECTOR



Source: Open Capital Advisors

COUNTRY SUMMARY: TANZANIA

Tanzania is an increasingly attractive destination for impact investors active in East Africa, particularly those looking to avoid comparatively competitive markets in Uganda and Kenya. Having received close to 12% of deals and capital disbursed by impact investors, Tanzania has become the third largest market for impact capital in the region.



Despite having a GDP that is approximately 50% higher than Uganda's, impact investing in Tanzania remains below its potential as investors continue to face several challenges. Tanzania's large land area, comparatively low population density, and weak road infrastructure hamper efficient distribution and logistics. Government intervention can be severe and unpredictable, triggering sudden changes in the business environment. Investors also face many of the same challenges in Tanzania as in the rest of the region, such as highly informal record-keeping and limited human capital, exacerbated in Tanzania by very low levels of returning diaspora.

Investors with flexible investment criteria, local presence, and technical assistance facilities for pipeline building should be well-positioned to tap Tanzania's large markets. Investors overwhelmingly highlight agriculture as a high-potential sector, particularly processing and post-harvest infrastructure.

COUNTRY SUMMARY: ETHIOPIA

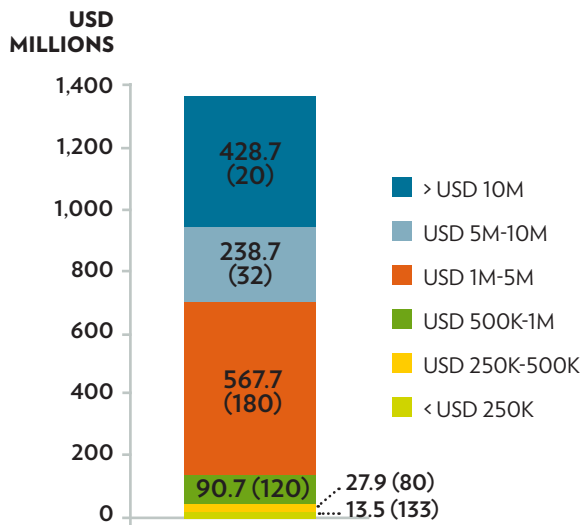
Despite its position as East Africa's largest country by population (around 90 million) and largest economy by GDP (over USD 120 billion in PPP terms), Ethiopia has received relatively little capital from impact investors to date. Only 4% of deals completed in the region have been in Ethiopia, accounting for around 7% of impact capital disbursed. Ethiopia's complex regulatory system severely restricts business ownership and profit repatriation by foreigners, who often struggle to overcome significant linguistic and cultural barriers. As is common in the entire region, low levels of human capital, highly informal record-keeping, and lack of experience with private investment among entrepreneurs have further impeded investment-ready deal flow. Consequently, only three impact investors have offices in Ethiopia, and the number of intermediaries is similarly low.



Nonetheless, Ethiopia's vast but underdeveloped market presents significant opportunities to impact investors, particularly those able to increase local decision-making, build portfolio company management teams that combine foreign and local talent, draw on technical assistance providers with local experience to provide pre-investment support, and source opportunities outside of Addis Ababa. Investors and entrepreneurs highlight agriculture, renewable energy, and mass-market consumer goods as particularly promising sectors.

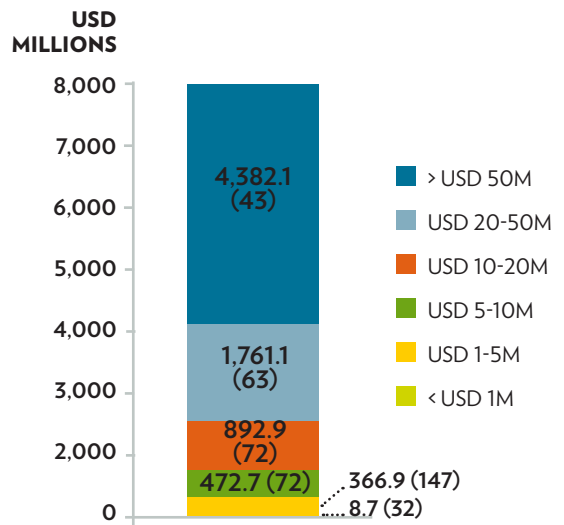
As shown in Figure 5, DFIs prefer large deals; over 50% of DFI capital has been disbursed in deals over USD 50 million, while only 5% of capital has been disbursed in deals under USD 5 million. By contrast, as Figure 4 shows, deals under USD 5 million account for 50% of capital disbursed by non-DFI impact investors, who are able to invest in smaller businesses. Overall, the average deal size for DFIs is USD 17 million, while it is USD 2.4 million for non-DFI impact investors.

FIGURE 4: NON-DFI IMPACT CAPITAL DISBURSED BY DEAL SIZE (NUMBER OF DEALS DENOTED IN PARENTHESES)



Source: Open Capital Advisors

FIGURE 5: DIRECT DFI IMPACT CAPITAL DISBURSED BY DEAL SIZE (NUMBER OF DEALS DENOTED IN PARENTHESES)

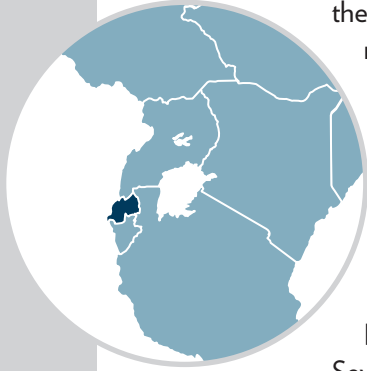


Source: Open Capital Advisors

DFIs' focus on large projects and more mature businesses is also reflected in the investment instruments they use. As shown in Figure 6, the majority of DFI investments are through debt, while non-DFI impact investors invest mainly through equity (for deals where the instrument is known). The large number of deals with unknown instruments, however, prevents definitive conclusions on non-DFI impact investors' instrument use.

COUNTRY SUMMARY: RWANDA

Rwanda's favorable business climate and strong governance track record have made it an attractive destination for impact investors. The World Bank, local entrepreneurs and investors view it as the easiest country to do business in across the region, and more than half of investors active in the region include Rwanda in their target geographies. However, deal flow to date has not matched this enthusiasm. Rwanda accounts for around 7% of deals and 4% of disbursements in East Africa, in line with its 4% share of regional GDP. Investors cite small markets, high input costs, a weak culture of entrepreneurship, and government interference as obstacles, along with the lack of human capital and formal record-keeping (as are common in the rest of the region).

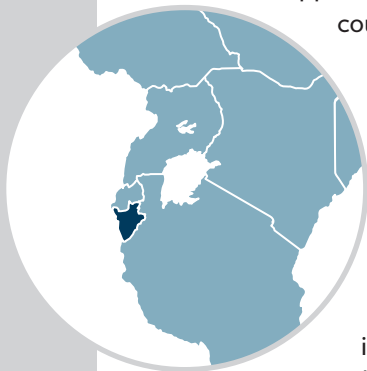


Investors able to mitigate these challenges are likely to enjoy significant opportunities in Rwanda. The neighboring countries of Burundi and the eastern DRC in particular offer large but untapped markets for Rwandan businesses.

Several investors have successfully addressed Rwanda's immature investing landscape by taking majority stakes or playing more active roles on investee boards than they might in more developed markets.

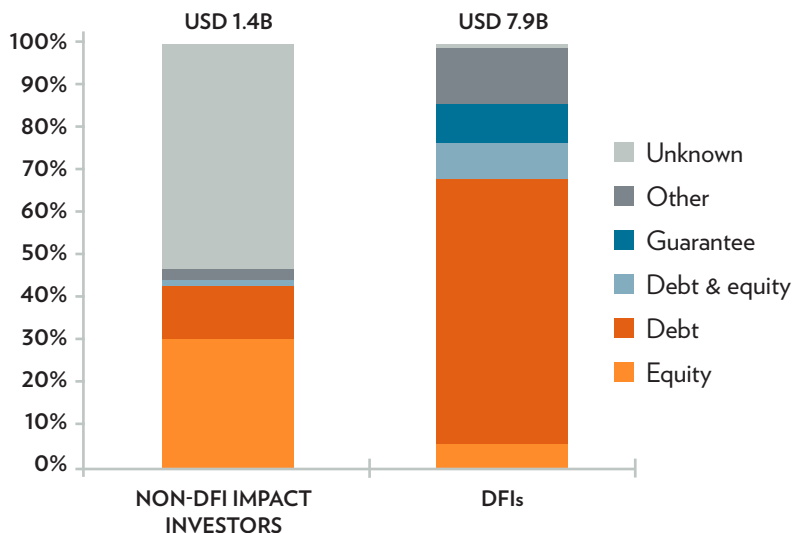
COUNTRY SUMMARY: BURUNDI

With a small market and economy, Burundi has seen limited impact investing activity. Few non-DFI impact investors operate in Burundi and there have only been a total of eight known deals worth approximately USD 1.4 million among these investors. DFIs have been more active in the country, closing 15 known deals totaling nearly USD 65 million in agriculture, financial services, and infrastructure.



Burundi's private sector is small, constrained by numerous factors including unreliable energy provision, political instability, limited human capital, and underdeveloped regulatory frameworks. Investors cite concerns such as corruption and a lack of political stability, though the government of Burundi has begun introducing regulatory reforms in an attempt to foster private sector development. Despite these challenges, Burundi offers an increasingly interesting proposition to impact investors, particularly in agriculture, sanitation, and renewable energy.

FIGURE 6: DIRECT IMPACT CAPITAL DISBURSED BY INSTRUMENT



Source: Open Capital Advisors

As seen in Figure 7, there are a variety of different impact investors for enterprises looking to raise various amounts of impact capital. Depending on the deal size, these investments often have different structures and are appropriate for different sectors, though all investment types and sectors are seen at all sizes.

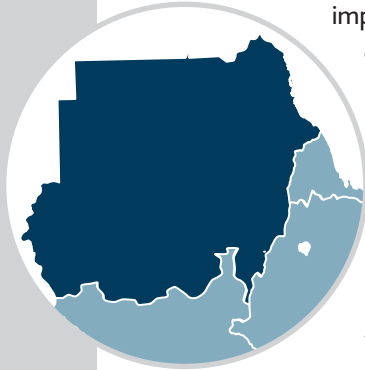
FIGURE 7: TYPICAL STRUCTURES, SECTORS, AND IMPACT INVESTORS BY DEAL SIZE

Deal size range	Typical financial products	Typical sectors	Example providers in East Africa
Less than USD 500K	Debt, convertibles	ICT, Agriculture, Health, Energy	Small social VC and debt-finance funds targeting early-stage businesses
USD 500K - 1M	Equity, debt, quasi-equity, convertibles	Agriculture, Financial Services, Health, Energy	Private equity funds, VC funds and foundations targeting social businesses with some track record
USD 1M - 5M	Equity, debt, quasi-equity, convertibles	Agriculture, Financial Services, Health, Energy	Larger impact funds and foundations
USD 5M - 10M	Equity, debt, quasi-equity, guarantees	Financial Services, Energy	Smaller national DFIs and large impact funds
USD 10M - 50M	Equity, debt, quasi-equity, guarantees	Financial Services, Infrastructure, Manufacturing	Regional and national DFIs
Over USD 50M	Debt, guarantees	Financial Services, Infrastructure, Energy	Large regional and national DFIs

Source: Open Capital, GIIN, interviews

COUNTRY SUMMARY: SUDAN

Although Sudan is East Africa's second largest economy in PPP terms, the country has received little impact capital. Most has been placed by DFIs into projects in oil, infrastructure, and agricultural processing. Non-DFI investors have been reluctant to invest in Sudan due to sanctions imposed by the United States and the United Nations, as well as Sudan's history of conflict and a challenging regulatory environment.



Following the loss of oil reserves and revenues with South Sudan's secession in 2011, Sudan has sought to increase investments into other sectors such as mining and agriculture. To promote investment, the government has offered tax incentives and prioritized access to foreign exchange to investors. Although Sudan's business environment remains challenging, the country's economic growth and human development indicators show opportunities to seek social and financial returns.

COUNTRY SUMMARY: SOUTH SUDAN

As the world's youngest country as of early 2015, South Sudan has seen very little impact investment. Investing and working in South Sudan continue to be challenging due to ongoing conflict, a poor regulatory environment, and economic concentration in oil. Although 50 impact capital vehicles list South Sudan in their list of target geographies, these vehicles typically have broad geographic mandates and are, for the most part, not actively looking for deals in South Sudan. Only one impact investor has staff based in the country. DFIs have deployed significantly more capital, disbursing approximately USD 17 million across six known deals.



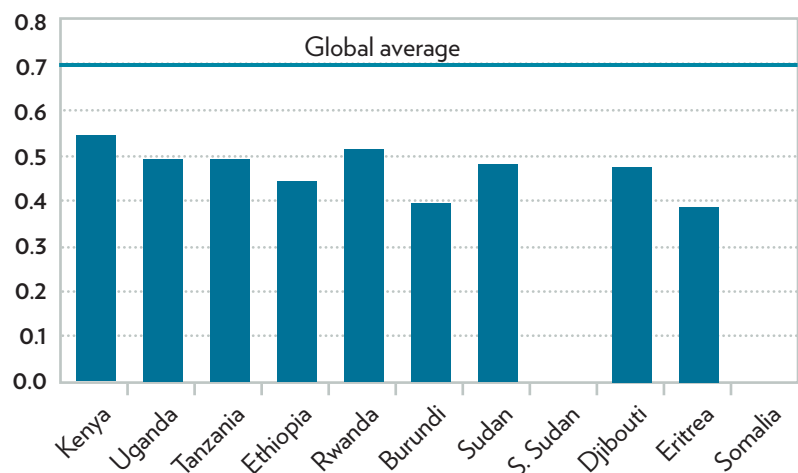
The government has acknowledged the importance of private sector development and diversification, and has begun streamlining the regulatory environment and investment process. With continued development of the enabling environment and technical assistance, there are opportunities for impact investors, particularly in agriculture, renewable energy and telecom.

SECTOR OPPORTUNITIES ACROSS EAST AFRICA

All East African countries share a need for capital to create social and environmental impact, with populations well below global averages for human development indicators despite robust recent economic growth, averaging a combined 7% annual GDP (PPP) growth for the last eight years. The following sectors present particularly notable opportunities in East Africa:

- **Agriculture:** Throughout East Africa, agriculture contributes more than 30% of GDP, employs most of the population, and is an important sector to increase incomes and improve food security. Given the predominance of smallholder farming, there are opportunities to aggregate production and create consistent, high-quality supply. In addition, there are opportunities to connect directly with export markets. There is also significant potential in agricultural processing across a range of crops and in agricultural sub-sectors such as horticulture, livestock, and dairy.
- **Renewable energy:** All countries in East Africa are looking to expand power generation capacity in the coming decades, with strong government support. This opens the door for large-scale projects and creates the potential for improved power purchase agreements and cross-border trade. At the same time, there are large segments of the population that lack reliable access to grid power, opening opportunities for micro-grid and off-grid solutions.
- **Aquaculture:** Fisheries and fish processing also show high potential, with the export of fish and fishmeal becoming an increasingly significant part of the East African economy. Sustainable fisheries can provide a critical source of protein and have the potential to reduce increasing pressure on important coastal areas.
- **Tourism:** Given the variety of attractions available in East Africa, from beautiful coasts to vibrant safari parks, there is high potential for tourism, although countries will need to be conscious of addressing security concerns to attract tourists. Governments across the region have started encouraging foreign investors and the returning diaspora to invest in the sector with some encouraging results. Tourism presents a particular opportunity for the non-focus countries in this report as a near-term potential employment source.

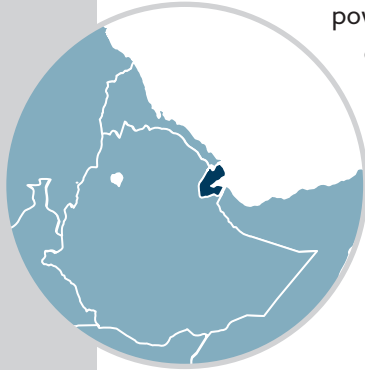
FIGURE 8: UN HDI SCORE BY COUNTRY, 2013



Source: UN Human Development Index. Note: South Sudan and Somalia not included in latest report

COUNTRY SUMMARY: DJIBOUTI

The smallest country in East Africa, Djibouti has received no known non-DFI impact capital to date, and DFIs have completed only two recorded investments. Impact investors face a number of challenges, including cumbersome bureaucratic processes, high costs for water and power, corruption, a weak legal system, and unfavorable labor laws. The Djiboutian government is working to improve the country's business and regulatory environment in order to attract more foreign investment.



With its coastal location, entrepreneurs and investors see high potential in the tourism, logistics, and fishing industries. The country also has an underdeveloped agriculture sector, importing 97% of its food. Supporting the agriculture sector could offer a high-impact opportunity for investors willing to work in Djibouti's challenging, arid environment.

COUNTRY SUMMARY: ERITREA

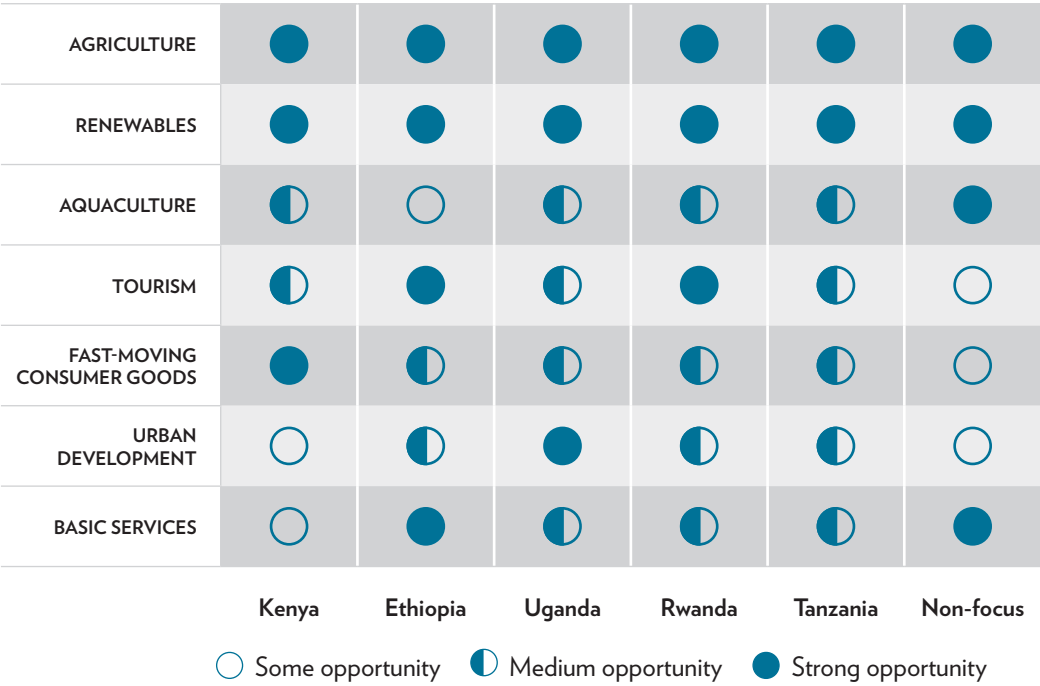
Eritrea is one of the world's most closed economies. Due to its isolation, difficult regulatory environment, and small private sector, there has been no known impact investing to date. The government has established a policy of "self-reliance" that restricts foreign investment and aid from foreign organizations, while operating without a constitution, functioning legislature, independent judiciary, or elections. Eritrea's private sector is also underdeveloped, meaning there are few investible opportunities. Private sector development has been severely limited by lack of capital, restrictive government policies, and a shortage of talent. Consequently, Eritrea ranks last in the World Bank's Ease of Doing Business survey.



However, there are signs that the economy is liberalizing. These trends include increasing privatization of state-owned enterprises, a gradual opening of the economy to foreign investors, and an increase in private investment. Although most foreign investment thus far has been in mining, there are opportunities for impact investors as well. Other promising sectors of the Eritrean economy include agriculture, aquaculture, and tourism.

- **Consumer goods for the mass market:** With East Africa’s rapidly growing middle class, impact investors report seeing increasingly attractive opportunities to supply goods and services to consumers with rising disposable incomes. These businesses often create substantial employment opportunities, which may align with impact criteria for some impact investors.
- **Urban development:** Non-DFI impact investors also note rapid urbanization and growing demand for businesses to serve expanding cities as an area of opportunity. Service sectors cited by impact investors include affordable housing, water, and sanitation.
- **Basic services distribution:** Throughout the region, increasing incomes and populations put growing pressure on the provision of basic services, including healthcare, education, water and sanitation, energy access, and financial services. Across these sectors, social enterprises struggle to distribute products and services across urban, peri-urban, and rural areas. Providing distribution as a basic service could have an exponential effect in driving growth for social enterprises and their investors.

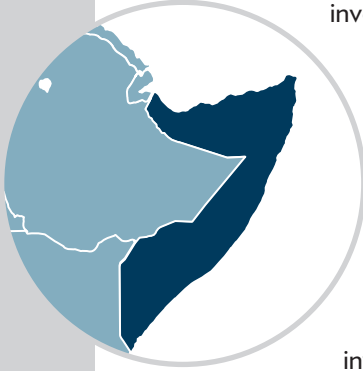
FIGURE 9: SECTOR OPPORTUNITIES ACROSS THE REGION



Source: Open Capital Research

COUNTRY SUMMARY: SOMALIA

No known impact investments have been made in Somalia to date. The country has been plagued by decades of conflict, insecurity, and a lack of central government, leading investors to hesitate. Without a strong government, the country suffers from a weak regulatory environment and lack of investor protection.



Despite these uncertainties, a growing private sector has flourished. In many cases, the private sector has filled roles typically held by public institutions, such as financial services, security, and education. With a new, internationally backed government in power and Al-Shabaab expelled from all urban centers, there is hope for a new era of stability to establish the regulatory and legal systems necessary to encourage foreign investment and formalize the private sector.

If this takes place, Somalia will likely receive increasing attention from impact investors looking to support Somalia's burgeoning private sector. Entrepreneurs, including members of the diaspora returning to their home country, see high-potential opportunities in agribusiness, fishing, and basic services.

CHALLENGES AND OPPORTUNITIES FOR IMPACT INVESTORS

Despite dramatically increasing interest in deploying impact capital in East Africa, impact investors face a variety of challenges in raising and deploying capital. These include challenges at both the investor and investee levels, as well as some more broadly present in the ecosystem. On the other hand, these challenges also present opportunities for current impact investors, new entrants, and other eco-system players to support rapidly growing, high-potential enterprises and the development of the regional impact investing industry.

Common Challenges

- **Insufficient investment-ready opportunities:** Despite robust market activity to date, many non-DFI impact investors still struggle to place the capital they have raised. Though investors acknowledge that there are many businesses with exciting potential, investors encounter few companies that they believe are truly investment ready. Early-stage businesses, which are the primary target for impact investors, face certain common challenges that constrain them from being fully prepared for investment, including unproven operations, an unclear strategy to scale, informal financial and corporate records, and a lack of realistic forward-looking projections.
- **Insufficient human capital:** Talent is the key constraint for many East African businesses. Companies struggle to find the talented, reliable management needed to plan for and reach scale. Though true for all skilled positions, this shortage is particularly acute for finance professionals with 5-15 years of experience who can serve as a company CFO. Even when talented, experienced professionals can be found, they often command high wages that can be challenging for SMEs or social enterprises to support, especially in their early years.
- **International decision makers:** Many non-DFI impact investors have investment committees based abroad and whose members may not have on-the-ground experience with investments in East Africa.³ These remote investment committees often interpret risk differently than their investment teams operating on the ground, which can cause due diligence and deal closing timelines to stretch to 12 to 18 months for both debt and equity investments.⁴ This can frustrate entrepreneurs, and put additional pressure on businesses as they must survive without needed capital.
- **Difficulty accessing bank financing:** Though entrepreneurs are sometimes able to source capital to begin operations from friends, family, and various community

³ Open Capital interviews with entrepreneurs, intermediaries, and investors.

⁴ Open Capital interviews with entrepreneurs, intermediaries, and investors.

financing organizations, they struggle to find the next round of capital to test and pilot their ideas in the market. In particular, conventional bank financing is difficult to access for early-stage businesses, as conventional banks in the region are very risk averse. Even if willing to lend, they require high collateral ratios (often in excess of 100% of the loan amount), which few entrepreneurs are able to meet.

- **Limited local currency financing:** Many impact businesses earn the majority of their revenues in local currencies. However, most impact investors track returns in international hard currencies and have little ability to invest in local currencies. This is especially challenging for long-term debt instruments, which require repayment in hard currencies that can appreciate 5-10% per year. Hedging options are typically prohibitively expensive, though some impact investors with large funds report effectively using fund-level hedges to minimize risk.
- **Few exit examples:** For new funds looking to raise capital, the relative youth of the impact investment industry means there are few examples of successful exits. As more impact portfolios in East Africa near the end of their tenors, there will be significant pressure on funds to exit investments, though it is not yet clear how this will develop in coming years. Without a successful track record of exits, it can be difficult for impact investors to raise additional funding or a second investment fund. Some fund managers interviewed for this report believe it may be easier for a new impact investor to raise funds than for an experienced one, as the latter are expected to demonstrate a track record before raising a second fund.

Common Opportunities

Each country in East Africa is unique. As a result, impact investors must learn about each country individually; strategies and solutions that are effective in one East African country will not necessarily work in another. Nevertheless, there are some high-level recommendations for investors that apply to the region as a whole:

- **Leverage technical assistance (TA) facilities for pre-investment pipeline building:** More pre-investment support for businesses is needed to develop a strong pipeline of investible opportunities. Increasingly, TA funders (e.g. USAID, DFID) recognize the importance of pre-investment support to get companies to the point where they can successfully raise capital. Several impact investors have successfully developed TA facilities for portfolio companies. Kenya in particular offers a robust intermediary ecosystem, and many of these players operate across the region. Such support can also significantly reduce diligence timelines if the investor is able to increase familiarity and visibility into the business pre-investment.
- **Develop sector expertise:** Beyond bringing capital to portfolio companies, impact investors can drive performance by understanding the specific sectors where their portfolio companies operate. For some investors, this sector focus has allowed them to identify exciting, less well-known opportunities earlier, and reduce their diligence timelines by leveraging existing knowledge. Sectors such as agriculture, energy, and financial services present large opportunities where companies often face consistent challenges across portfolio companies.

- **Source opportunities outside capital cities:** Many impact investors with staff on the ground in East Africa report finding investments more easily than those based abroad. However, many entrepreneurs operate in rural areas or smaller cities, instead of the capital cities or regional hubs where investment staff are based. For investors who see these entrepreneurs' businesses as attractive impact investment opportunities, it will be increasingly necessary to build relationships beyond those made in major cities.
- **Expand investment instruments:** With the variety of early-stage businesses in East Africa, creative investment structures—such as milestone-based conversion and profit-sharing debt—can help to fill a significant gap that straight equity and debt deals do not. Such structures can help entrepreneurs meet ongoing cash flow requirements while delivering long-term returns in line with investor expectations. There is also an opportunity to expand sharia-compliant investments to support Muslim entrepreneurs, using Murabaha and Ijara methods to help align impact investor goals with sharia law in areas with large Muslim populations in the region.
- **Increase local decision-making:** Impact investors have cited significant improvements in their portfolio from increased local decision-making and local support. This allows investment officers to form meaningful relationships with portfolio companies, where they are empowered to respond to changing realities on the ground. Placing staff and investment committees locally can also reduce diligence timelines, as these individuals are more familiar with local trends and norms. In an environment of increasing competition between impact investors for high-potential deals, designing effective diligence procedures aligned to the region could be a key differentiator for successful impact investors.

RECOMMENDATIONS FOR FUTURE STUDY

This report presents the most comprehensive study of impact investing in East Africa to date. Given its broad mandate, its findings raise several additional questions for future research:

- **What types of support effectively prepare businesses for investment?** Several organizations in East Africa provide pre-investment and post-investment support. Which are the most effective in developing investment-ready businesses? How does this vary by the stage of businesses? What role can mentoring, acceleration, classroom lectures, tailored business support, outsourcing, and other services play in helping businesses attract the capital they require to grow?
- **How can appropriate investment structures catalyze additional impact capital?** This report raised a key challenge for Islamic businesses that require sharia-compliant investment structures. But beyond this need, all impact investors face a tension to drive for both social and financial returns. What types of structures can help an impact investor achieve these dual goals, and what protections are required for foundations and others who may have specific impact requirements?
- **How can social enterprises and impact investors attract, build, and retain top talent?** Talent is one of the most frequently cited challenges in East Africa. What can the social enterprise sector learn from top corporations in attracting, building, and retaining talent at all levels? What monetary and non-monetary compensation is expected by professionals considering a career path in East Africa? How can social enterprises and impact investors leverage non-monetary compensation to compete with top international firms for talent? What value do social enterprises realize when they hire talent to help drive to scale?
- **What viable exit mechanisms can impact investors consider in East Africa?** Beyond thinking through the impact implications an exit may have, how can impact investors consider exits more broadly in the region? How could a secondary market improve deal flow, and incorporate learnings from prior attempts to create impact exchanges, dedicated secondary markets, and strategic acquisitions?



ABOUT THE GLOBAL IMPACT INVESTING NETWORK

The Global Impact Investing Network (GIIN®) is a nonprofit organization dedicated to increasing the scale and effectiveness of impact investing. The GIIN builds critical infrastructure and supports activities, education, and research that help accelerate the development of a coherent impact investing industry. For more information, see www.thegiin.org.

30 Broad Street, 38th Floor, New York, NY 10004
+1.646.837.7430 | info@thegiin.org | www.thegiin.org