CONVERGENCE
BLENDING GLOBAL FINANCE

GLOBAL PARTNERSHIPS

CASE STUDY

GLOBAL PARTNERSHIPS' INVESTMENT FUNDS

MARCH 2017

EXECUTIVE SUMMARY

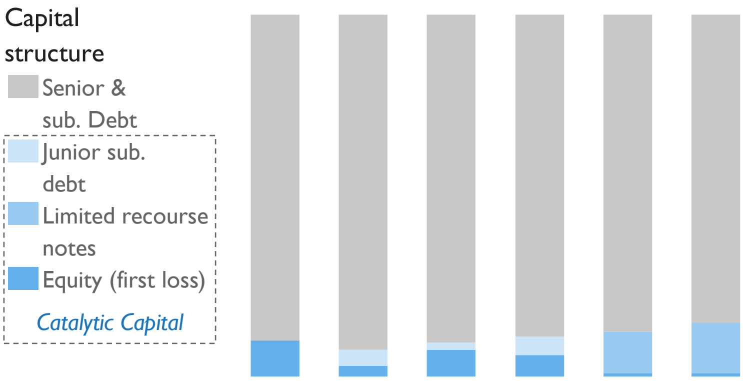
Global Partnerships (GP) is a non-profit impact-led investor whose mission is to expand opportunity for people living in poverty. In 2005, building from a decade of grant-based programming, GP launched its first investment fund. Since 2005, GP has designed, launched, and managed six debt funds. Through these funds, GP has extended USD 232M of loans to over 100 social enterprises across 14 developing countries.

To define the investment strategy for each fund, GP deploys a research team (funded by philanthropic capital) to identify promising, high-impact products and services to families living in poverty in Latin America and Sub-Saharan Africa. For its first four funds, GP raised subordinated philanthropic funding to attract private investment and development finance in the form of senior debt. After demonstrating proof of concept, GP's two most recent funds rely less on philanthropic funding in first-loss or subordinated positions to attract additional investment. GP targets impact-first investors who are also seeking stable financial returns. GP's investors include development finance institutions (DFIs), foundations, religious pension funds, and accredited individual investors.

GP demonstrates that philanthropic capital can be deployed strategically to attract additional investment and demonstrate proof of concept. GP also demonstrates the value of leveraging philanthropic capital to fund impact research and partner identification, costs that are traditionally borne by the fund. GP shows the value of carefully building a track record over time in order to drive more impact and raise more capital. This case study also highlights some ongoing challenges for impact-first funds, including dependence on socially-driven investors rather than financially-driven investors, and avoiding market distortion.

SYNOPSIS

Manager	GP Fund Management, LLC					
Mandate	Expand opportunity for people living in poverty while delivering fixed income-level financial returns					
Legal structure	Each fund is a limited liability corporation					
	MFF '05	MFF '06	MFF '08	SIF '10	SIF 5.0	SIF 6.0
Fund vintage	2005	2006	2008	2010	2012	2015
Size (M, USD)	2	8.5	20	25	50	75



Fund term (yrs)	5	5	6	6	10	10
Investment instruments	Debt (both USD and local currency denominated)					
Investment size	Average size: USD 1M Minimum size: USD 250K					
Target return	Stable, fixed income-level returns, around 3%-4%					
Fundraising status	MFF '05 to SIF '10 closed; SIF 5.0 fully subscribed and deployed; SIF 6.0 fundraising as of Feb 2017, SIF 6.0 reached first close in Oct 2016					
Example impact metrics	Number of solar lamps sold; tons of agricultural products sold; number of women trained					

INTRODUCTION

Global Partnerships (GP) launched in 1994 to provide grant capital to pioneering microfinance institutions (MFIs) in Central America. Established as a family foundation and driven by the impact of early microcredit programs, GP developed a strong reputation for impact and learning. After a decade of success, GP launched its first investment fund in 2005 to further scale its impact.

Since 2005, GP has launched and managed six debt funds. Each fund builds on the success and learning of the last, with each fund growing in total capital raised, number of investors, and impact. To date, GP has deployed USD 232M to over 100 partners across 14 countries. The first four funds have repaid all investors—senior and subordinated—in full, contributing to GP's reputation for predictable financial returns alongside growing impact for people living in poverty.

GP uses blended finance to promote research and learning and to bolster impact and financial success. GP raises donations to identify and research products and services that have the potential to have outsized impact for families living in poverty. GP leveraged junior subordinated funding for MFF '05 through SIF '10 and limited recourse notes for SIF 5.0 and SIF 6.0 to attract private investment and development finance in the form of senior debt. The level of impact and steady returns are evidence of the success of GP's model.

This case study focuses on the evolution of GP's debt funds, from the first investment fund launched in 2005 (MFF '05) to the sixth fund, the Social Investment Fund 6.0 (SIF 6.0) launched in 2015. Each fund shares a similar purpose and structure, and aims to leverage philanthropic capital to attract private and development finance investors.

DESIGN AND FUNDRAISING

EVOLUTION OF FUND DESIGN

GP's funds have evolved in size and maturity, sector and geography focus, and capital structure. The first fund took nearly three years to structure, fundraise, and reach financial close. GP has since streamlined the process, particularly for sourcing capital, producing the offering memorandum, and corporate registration. The design, fundraising, and documentation process now takes 12-18 months, depending on the complexity and novelty of the fund.

GP has taken an "edging out" approach to growing its funds. The first four funds had five to six-year maturities, with growing capitalization of USD 2M, USD 8.5M, USD 20M and then USD 25M. The last two funds have 10-year maturities, with growing capitalization of USD 50M and USD 75M.

The first four funds extended loans to MFIs, and later cooperatives, in Latin America and the Caribbean. Given GP's early success investing in MFIs, GP expanded the sectoral focus in 2012. Under SIF 5.0 and SIF 6.0, GP extends loans to social enterprises mainly in the microfinance, agriculture, and energy sectors. Building on financial and social impact success, GP expanded into East Africa with SIF 6.0—the first time GP's mandate expanded beyond Latin America and the Caribbean.

A key aspect of GP's funds is the use of catalytic capital to attract private investors. For each fund, GP has targeted between 7.5-15% in catalytic capital. The exact level of catalytic capital varies according to the risk perception of current and potential senior investors. The highest levels of catalytic capital have been for the two recent funds, which explore new sectors and new geographies.

The most notable evolution in GP's funds has been the mechanism through which catalytic capital has been raised. For MFF '05, the first fund, GP relied only on donations as equity (first-loss capital) for catalytic capital. As the size of subsequent funds grew, GP could not provide the required first-loss capital through donations alone.

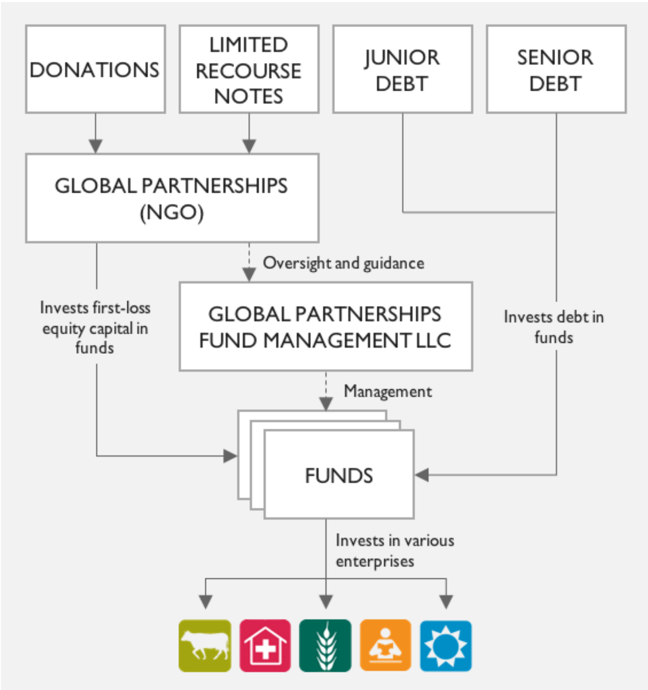


Figure 1: Financial flows of GP debt funds

For MFF '06, MFF '08, and SIF '10, GP introduced a junior subordinated tranche to raise capital from development finance and impact investors. For these funds, GP provided the sole equity contribution, sourced through donations, as first-loss and used the junior tranche—"second-loss" capital—to make up the catalytic capital target.

Given the size of the two latest funds (USD 50M and USD 75M), GP was not able to meet the targeted minimum equity contribution. GP replaced the junior subordinated debt with limited recourse notes in order to raise the additional capital for the equity contribution to each fund. Limited recourse notes allow GP to lower the cost of capital while increasing the size of the funds. The holders of the notes have recourse only to cash flows coming back to GP from that specific fund, hence the term "limited recourse." The limited recourse notes serve the same "second-loss" role as the junior subordinated tranche.

FUNDRAISING APPROACH

New investors are sourced from existing donors and investors, network engagement (ANDE, Interfaith Center for Corporate Responsibility, Mission Investors Exchange, GIIN, Confluence Philanthropy), wealth advisory platforms, and prospect research.

GP targets investors looking for high social impact and stable financial returns. GP funds have a diverse group of investors, including DFIs, foundations, religious pension funds, and accredited individual investors. Fund investors include OPIC, FMO, The Rockefeller Foundation, Ceniarth LLC, and Bon Secours Health System. 81% of current investors have invested in two or more of GP funds and 54% of investors in SIF 6.0 are new to GP.

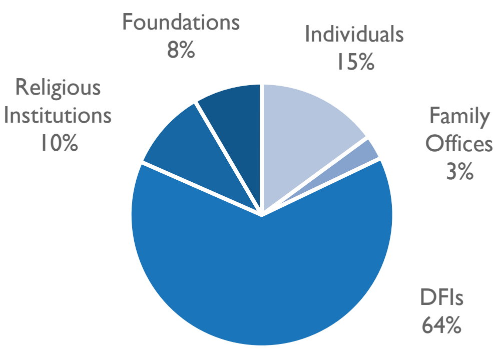


Figure 2: Profile of investors in GP debt funds

DFIs represent 64% of aggregate capital across the six funds, which reflects the funds' alignment with socially-minded investors looking for steady, fixed-income level returns. Nonetheless, GP continues to attract new investors who are increasingly commercially-driven. The small ticket size continues to be a barrier for many institutional investors.

STRUCTURE AND GOVERNANCE

LEGAL STRUCTURE AND GOVERNANCE

To transition from a grant-making institution to a fund manager, GP transformed to a 501(c)(3) non-profit organization and established a separate entity, called Global Partnerships Fund Management LLC, as a wholly-owned subsidiary. Global Partnerships Fund Management LLC manages all of GP's funds.

Each fund is established as a limited liability corporation. As a non-profit, GP is required be the sole equity holder. Equity is sourced through a combination of donations to GP, earned revenue, and limited recourse notes.

CAPITAL STRUCTURE

GP uses a blended capital structure in all its funds. The majority of each fund is senior and/or subordinated debt:

- Senior Debt, 56-88% of fund corpus: GP offers two forms of senior debt—senior notes and senior debt obligations. Both are pari passu and unsecured, with maturities of 1-10 years. Senior notes are offered to accredited investors and bear annual interest payable quarterly in arrears. Senior debt obligations are offered to DFIs and also bear annual interest payable quarterly in arrears at a date determined upon the fund's close.

- Subordinated Debt, 10-34% of fund corpus: GP offered a subordinated debt tranche for the first four funds. Subordinated debt obligations have a five to six-year maturity and bear an annual interest payable quarterly in arrears. Past funds have relied more heavily on subordinated debt, while current funds have more senior debt.

Catalytic capital has been funded through a variety of mechanisms, including (i) junior subordinated debt, (ii) GP's equity contribution, and (iii) limited recourse notes.

- Junior Subordinated Debt, 2-5% of fund corpus: GP offered a junior subordinated debt tranche for three funds—MFF '06, MFF '08, and SIF '10. Junior debt obligations have a five to six-year maturity and bear an annual interest payable quarterly in arrears.

- Equity, 3-15% of fund corpus: GP's equity contributions are raised through donations, which contribute approximately 45% of GP's total revenues, as well as earned revenue from previous funds.

- **Limited Recourse Notes:** To meet the equity contribution requirement for larger funds, GP introduced limited recourse notes. Limited recourse notes are offered by GP (the NGO) rather than the specific fund. Limited recourse notes have an end-of-fund maturity and are paid in a single installment, principal plus interest, at maturity.

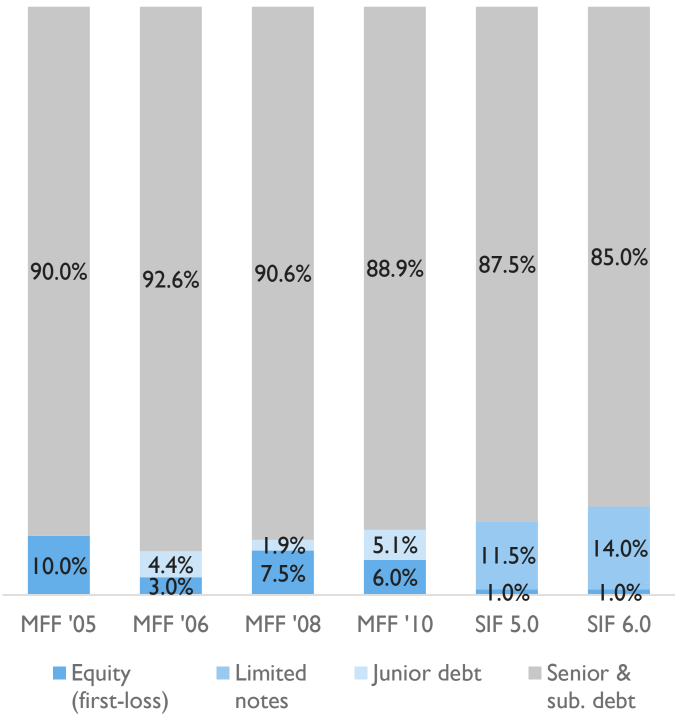


Figure 3: Capital structure of debt funds

OPERATIONS

INVESTMENT CRITERIA

GP's first investment criterion is impact alignment. GP looks for credible evidence of a focus on poor and marginalized clients; outreach to under-served markets, including the very poor, women, and rural populations; and delivery of high-impact goods and services. Once impact alignment has been determined, GP completes financial due diligence. Top candidates are growth-stage enterprises that are not reached or underserved by traditional markets. GP's goal is to identify mission-driven businesses with a clear and compelling strategy for achieving long-term sustainability, scale, and competitiveness.

INVESTMENT PROCESS

GP employs a unique approach to determine the investment priorities of each fund, deploying NGO resources to support fund-based activities. The investment process is a collaboration between GP's Social Investment Team and the Impact and Research Team. Established just over three years ago, GPs Impact and Research Team does extensive legwork, identifying promising products, services, and intervention models by initiative focus. Then the Social Investment Team identifies and screens potential partners, negotiates partnership contracts, and monitors and evaluates outcomes.

The investment process can be understood as follows:

1. Ongoing Research: The Impact and Research Team conducts research on high-potential products, services, and intervention models, as well as impact measurement.

2. Partner Identification: The Social Investment Team scans target geographies and sectors for partners aligned with identified investment initiatives. GP seeks out nearly all partnerships.

3. Partner Screening: The Impact and Research Team and the Social Investment Team screen potential partners for impact alignment and portfolio fit. If sufficient initiative alignment is found, the Social Investment Team negotiates a preliminary term sheet and formal due diligence is scheduled.

4. Due Diligence: The Social Investment Team completes a formal due diligence process, including financial analysis, site visits, and information verification.

5. Final Decision: The Board Investment Committee is ultimately responsible for the final decision on the credit-worthiness, and portfolio fit of the proposed partner. The Fund Manager presents a makes a recommendation to the Investment Committee on the terms and structure of proposed loans.

The partnerships established between GP and social enterprises are multi-year and multi-fund. Social enterprises often take multiple, growing loans from GP funds, both over the course of a single fund and over multiple funds. GP is careful to offer competitive and unique products and terms as additionality and market distortion are an important consideration.

INVESTMENT ACTIVITY TO-DATE

Since 2005, GP has lent USD 232M to over 100 social enterprises across 14 countries. GP has repaid 100% of investors on time and in full for 46 consecutive quarters, including successful wind-downs of the first four funds—MFF '05, MFF '06, MFF '08, and SIF '10. Most recently, SIF '10 fully matured in June 2016. At liquidation, SIF '10 had provided 122 loans to 42 partners.

GP's active funds continue to perform well. In fiscal year 2016, GP deployed USD 47M, a 33% increase over the previous fiscal year, through SIF '10, SIF 5.0, and SIF 6.0. SIF 5.0 is fully invested across Latin America and the Caribbean and is performing well. SIF 6.0 launched in October 2015 and has made 27 investments through December 2016, including GP's first investments in East Africa (Kenya).

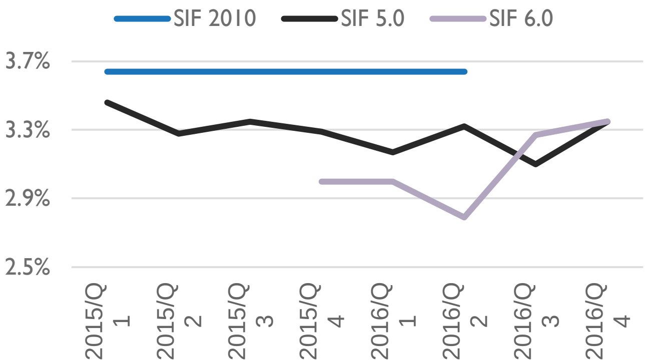


Figure 4: Fund return rates

GP's funds are listed on several impact investment databases, including GIIN ImpactBase and MIX Market, and have been recognized through multiple awards, including the OPIC Impact Award in the "Access to Finance" category (2014) and the ImpactAssets 50 list for six years running.

LOCAL CURRENCY LENDING

GP offers local currency loans to select social enterprises, determined by partner demand and risk rating, for MFF '08, SIF '10, SIF 5.0 and SIF 6.0. Each fund has a maximum local currency allotment—30% for MFF '08, 50% for SIF '10, and 60% for SIF 5.0 and SIF 6.0.

Local currency loans are hedged through the purchase of currency hedging products from MFX Solutions, which provides hedging products to impact investors. MFX offers several hedging products, which are offset by commercial banks or The Currency Exchange Fund (TCX).

Total loans issued in local currency have been well below allocated limits (11% of the portfolio for MFF '08, 24% for SIF '10, 21% for SIF 5.0 and 17% for SIF 6.0). Local currency loans remain prohibitively expensive as the price of hedging is passed on to the loan recipient. This is particularly acute in markets with higher currency volatility, like Argentina.

IMPACT METRICS

GP has a strong track record of reporting on financial and impact metrics, particularly since the establishment of the Impact and Research Team. GP designs impact metrics by first establishing theories of change for each of GP's five investment fund initiatives. GP then works with financial performance data collected quarterly from investees, applying an initiative-lens (see figure 5) and aligning the data points to its evidence base to provide insights.

GP's focus on impact measurement and learning differentiates it from its competitors. The Impact and Research Team is funded primarily through donations and grants, rather than fund management fees. GP consults an investor council semi-annually to discuss findings and areas for model improvement.

Initiative	Initiative-Specific Metric
Women-Centered Finance with Education	Individuals trained
Rural-Centered Finance with Education	Individuals trained
Smallholder Farmer Access with TA	Tons of crops purchased from farmers
Solar Lights	Units sold
Women-Centered Finance with Health	Instances of medical attention

Figure 5: Initiative-specific metrics

IMPACT TO-DATE

GP's debt funds invest across five initiatives. While its focus on microfinance is the longest standing, GP has already accomplished notable progress in the areas of solar energy and extension services.

1. Women-Centered Finance with Education: GP lends to MFIs that deliver credit and savings plus education. In 2015, GP reached 825K clients through investees, of which 88% were female. In total, 1.79M lives have been impacted by GP's investment funds.

2. Rural-Centered Finance with Education: GP lends to financial institutions that deliver tailored credit and education to rural, smallholder households. In 2015, GP reached 219K clients through investees, of which 47% were female and 69% were rural. In total, 545K lives have been impacted under this initiative by GP's investment funds.

3. Smallholder Farmer Access with TA: GP lends to agricultural businesses that provide improved market access and technical assistance to smallholder farmers. In 2015, GP reached 68K farmers, of which 21% were female, who sold 93K tons of chia, coffee, and sesame. In total, 74K lives have been impacted under this initiative by GP's investment funds.

4. **Solar Lights:** GP lends to manufacturers and distributors that provide households living beyond the grid with access to solar lights and small solar home systems. In 2015, GP deployed USD 500K in new loans across 7 investees supporting sales of over USD 1M. In total, over 2M solar units have been sold by GP investees.

5. **Women-Centered Finance with Health:** GP lends to MFIs that deliver credit and savings plus access to basic health services. In 2015, GP reached 514K clients, 82% female, and recorded 299K instances of medical support. In total, 1.3M lives have been impacted under this initiative by GP's investment funds.

NEW FUNDS

In the short-term, GP is focusing on sustaining SIF 5.0, scaling SIF 6.0, and managing a new fund structure, called the Social Venture Fund (SVF). SVF targets early stage social enterprises in East Africa. This represents both a new target market, geography, and financial tool for GP.

In the long-term, GP will look to establish more social investment funds, explore vehicles that allow for participation of retail investors, continue geographic expansion, and explore evergreen fund models.

KEY INSIGHTS

GP presents several insights useful for others looking to create or invest in similar blended debt funds:

- **Philanthropic capital can be leveraged for research as well as first-loss capital.** GP uses philanthropic capital to fund impact research and catalytically to attract fund investment. The use of philanthropic capital for research and impact measurement is unique and represents a replicable model for other impact funds.

- **Catalytic capital can take multiple forms, according to the needs of the vehicle and investor(s).** Over the course of six funds, GP leveraged donations, a junior debt tranche, and limited recourse notes to raise catalytic capital. This reflected the growing needs of each successively larger fund and also feedback from current and potential investors.

- **A track record is invaluable for attracting funds even as activities expand to new regions and sectors.** GP established a strong reputation as an NGO, which was leveraged in establishing and growing its investment funds. Over the last several years, GP has demonstrated the value of investing in impact measurement that quantifies the social impact of the funds, which gives investors tangible reasons to invest and stay invested.

- **Taking an "edging out" approach to growth and not committing to a long-term structure from the outset can allow time to refine and improve.** GP has reached operational efficiency, increasing scale while maintaining strong financial controls. Expenses have grown only modestly despite the tremendous growth of GP's portfolio. Incremental growth allowed GP to identify aligned investors, establish a strong theory of change, and build out a strong pipeline of partners.

- **Impact-first funds like GP are more likely to attract socially-driven investors than commercially-driven investors.** GP's funds are a "typical" investment for its investors. While GP has achieved its goal of scaling its work through blended finance, the small ticket size continues to be a barrier for institutional investors and other commercial investors. Further, GP funds have predictable and steady returns, but not at the level expected by purely commercial investors.

- **Balancing market distortion and long-term partnerships is an important consideration.** Fund investees often take multiple loans with GP rather than graduating to commercial sources of capital. On one hand, social enterprises need to access flexible (e.g. collateral-free,) and socially-minded capital. On the other hand, investors must be careful not to distort local capital markets by ensuring terms are competitive and fair.

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