



*Photo Credit: Leocadio Sebastian*

# IIX Women's Livelihood Bond

IIX SUSTAINABILITY BONDS: CHANGING FINANCE, FINANCING CHANGE



The  
**ROCKEFELLER  
FOUNDATION**

*shujog*

*Opportunity for Impact™*

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## ACRONYMS

<b>DSRA</b>	Debt Service Reserve Account
<b>IE</b>	Impact Enterprise
<b>ISB</b>	IIX Sustainability Bond
<b>MFI</b>	Microfinance Institution
<b>SME</b>	Small-Medium Enterprise
<b>SPV</b>	Special Purpose Vehicle
<b>USAID</b>	United States Agency for International Development
<b>WLB</b>	Women's Livelihood Bond





## EXECUTIVE SUMMARY

Impact investing has been revolutionary in the history of capital markets. The concept refers to investments with the intention of generating positive social impact over and above financial returns. Over the last six years, impact investing has moved from the margins to the mainstream with an estimated market size of \$46 billion in 2014 (World Economic Forum, 2014), shifting the paradigm on how the world blends impact with financial returns.

But there is more to be achieved. A 55% annual growth rate would be required to reach the target market size of \$1 trillion by 2020 (J.P. Morgan, 2010). This exponential growth can be achieved only by unlocking mission-oriented capital at scale, by bringing in new actors from the private sector to support sustainable development and by developing innovative financial products that can channelize resources to high impact entities – which in turn can deliver scalable and sustainable market-based solutions.

Leveraging its expertise in innovative finance, Impact Investment Exchange Asia (IIX) sets out to achieve this by developing a new financial product that seeks to bridge the current gap between development and finance: the IIX Sustainability Bond (ISB). ISBs are debt securities that pool together in a single portfolio, a group of high-impact entities that have undergone a rigorous due diligence process based on both social and financial criteria. This unique pooled structure allows underlying borrowers to access large amounts of capital that they would not otherwise have been able to raise individually. ISBs are designed to be sustainable instruments, offering attractive rates of risk-adjusted returns to impact investors who are interested in a double bottom line. ISBs will be listed on the Stock Exchange of Mauritius, adding an additional layer of secondary liquidity, mission protection and transparency.

IIX's commitment-to-action to the Clinton Global Initiative, the first ISB, is the Women's Livelihood Bond (WLB), a \$20 million debt security designed to unlock capital for Impact Enterprises (IEs) and Microfinance Institutions (MFIs) that are part of the sustainable livelihoods spectrum for women in South-East Asia. The WLB is projected to empower over half a million women with access to credit, to market linkages, to natural resources and to affordable goods and services. This will, in turn, help them transition from subsistence to sustainable livelihoods and redefine the dominant narrative from viewing women as victims to recognizing them as solutions to development, change and progress.

This Blueprint Paper, developed by IIX's sister non-profit entity Shujog, aims to provide an overview of the bond mechanics by outlining the key steps involved in the bond structuring process. Supported by the Rockefeller Foundation, a visionary catalyst in the impact investing space, this preliminary paper will capture the progress made to date by IIX on product, pipeline and partnership development. A subsequent paper will be published post bond issuance which will capture the key steps involved in selling the bond to investors and listing it on the Stock Exchange of Mauritius.

Shujog hopes this paper will act as a roadmap for other stakeholders in the space to create similar instruments that are designed to change finance and finance change.

# SECTION 1: IIX SUSTAINABILITY BONDS



## IIX SUSTAINABILITY BONDS

### CHANGING FINANCE AND FINANCING CHANGE

#### IIX SUSTAINABILITY BONDS: OVERVIEW

IIX Sustainability Bonds (ISBs) are innovative financial instruments that effectively mobilize large scale private sector capital by pooling together a basket of Impact Enterprises – defined as revenue generating non-profits or mission driven for-profits, and Microfinance Institutions. Both IEs and MFIs are key drivers of change owing to their ability to create scalable impact in a financially sustainable manner. ISBs are debt securities that pool together this group of underlying borrowers (IEs and MFIs), depending on their financial needs, repayment abilities, risk profiles and impact potential. ISBs are replicable instruments that can be structured and issued around different themes – depending on the target beneficiary (low income women, at-risk youth, among others) – or sectors (livelihoods, energy, education, among others).

#### KEY OBJECTIVES OF IIX SUSTAINABILITY BONDS:

ISBs are designed to finance change and change finance via three overarching objectives:

- **Availability of mission-oriented capital:** To open the floodgates of mission-oriented investment capital available to high-impact organizations that are equipped to create sustainable impact
- **Accessibility of mission-oriented capital:** To bring together capital supply from investors with demand from high-impact organizations through an innovative, replicable financial instrument
- **Affordability of mission-oriented capital:** To provide high-impact organizations access to relatively low-cost capital that is more affordable than capital available from public debt markets

#### BOND MECHANISM

This section provides a brief overview of the bond mechanism [Figure 1] and how ISBs coalesce diverse stakeholders from both the public and private sectors to create an innovative new instrument that effectively unlocks private capital and redirects it towards achieving development outcomes.

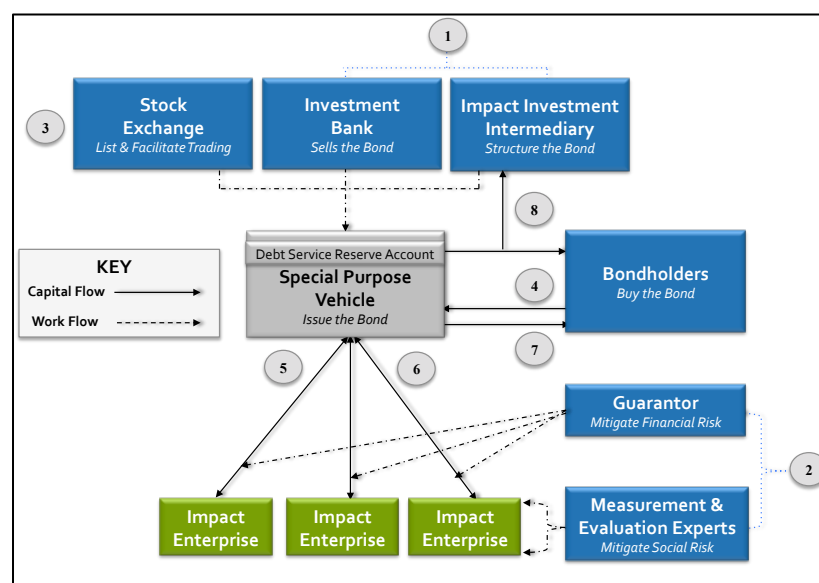


FIGURE 1: OVERVIEW OF ISB MECHANISM

## IIX SUSTAINABILITY BONDS

Following are the steps to creating an IIX Sustainability Bond:

- 1a The first step is for the **Impact Investment Intermediary**, promoter of the bond, to structure the bond by designing the mechanism and key risk mitigation factors, developing the pipeline of underlying borrowers, and coalescing partners (banking, legal, academic, measurement and evaluation, etc.)
- 1b Simultaneously, the **Investment Bank Partner** provides strategic input on the product based on investor preferences, including bond size, coupon rate and maturity, among other key security features. The investment bank also takes the responsibility of bond placement (unless the impact investment intermediary has a license to sell securities) and sells the bond to investors.
- 2a To mitigate social risk, **Measurement and Evaluation experts** conduct preliminary screening on potential underlying borrowers to measure and project impact before they are selected. Ongoing monitoring and evaluation as well as regular reporting of impact will also be done to ensure transparency of results.
- 2b **The Guarantor** (government, donor agency or foundation) provides added risk mitigation by guaranteeing either whole or part of the bond. There is a trade-off between the coupon rate that can be offered to investors and the amount of the portfolio that can be covered by the guarantee. A ceiling can be applied to reduce the total cost of the guarantee and protect only the riskiest assets in the portfolio.
- 3 The bond is listed on **Stock Exchange of Mauritius** to provide secondary liquidity. This entails ongoing monitoring and evaluation on impact metrics as well as regular reporting from a financial (risk-return) perspective to ensure transparency of results.
- 4 **Bondholders** (accredited investors) purchase the bond, which is issued by the Special Purpose Vehicle (SPV). The bondholders may trade the bond on the **stock exchange** during the life of the bond, if either the impact or the financial returns do not meet expectations, among other potential reasons. This layer of secondary liquidity provides an exit option and added comfort to the investor.
- 5 The amount raised is lent by the SPV to the pre-selected group of underlying borrowers – **Impact Enterprises**. Over the life of the bond, the **Impact Enterprises** use this capital to magnify their impact and scale their operations.
- 6 The **Impact Enterprises** pay the SPV back the principal amount borrowed plus interest over the life of the bond. Part of the interest earned from **Impact Enterprises** is held back to build up a Debt Service Reserve Account (DSRA) that acts as an inbuilt cushion or first-loss reserve account. If one of the borrowers defaults, the guarantee and the DSRA protect the investors up to a certain extent.
- 7 The **bondholders** are paid a coupon on a semi-annual basis and are repaid the principal amount at bond maturity. They also receive regular updates on the bond's performance on both financial and social criteria.
- 8 Upon bond maturity, if there is any unutilized amount left as part of the DSRA, the amount is split evenly between the **bondholders** (as a reward for taking on the risk) and the **impact investment intermediary** (as a reward for conducting a sound due diligence).

## IIX SUSTAINABILITY BONDS

### THE FIRST IIX SUSTAINABILITY BOND: WOMEN'S LIVELIHOOD BOND

The first ISB will be the Women's Livelihood Bond (WLB) that aims to empower women to make the transition toward sustainable livelihoods. Many organizations – IEs and MFIs – recognize the importance of focusing on women in development, but alarmingly, existing funding channels fall drastically short of development goals focused on women.

The WLB sets out boldly to change this, providing high-impact entities with the capital they need to support women in the most vulnerable communities today. The proceeds of the bond will be used to make loans to IEs and MFIs that are part of the sustainable livelihoods spectrum. Underlying borrowers will have a proven revenue generating, high-impact business model.

Officially launched at the 2014 Clinton Global Initiative (CGI) annual meeting, the WLB represents IIX's commitment to the CGI. The structuring of the WLB was funded with support from the Rockefeller Foundation and Japan Research Institute. The WLB focus countries are in South-East Asia, namely Cambodia, Indonesia, the Philippines and Vietnam.

IIX is anticipating a bond size of \$20 million, a tenor of four years and a target coupon rate of between 6% and 7% that will be paid to impact investors who buy the bond. The WLB mitigates risk via credit enhancement features including a guarantee facility and an inbuilt DSRA, to reduce financial risk and protect investors. **More details on the WLB are provided in the next section of the paper.**

### CUSTOMIZATION AND REPLICABILITY

ISBs are replicable instruments that can be customized to suit different geographic contexts from both a regulatory and a needs-based standpoint. Although the first bond is focused on women's livelihoods in South-East Asia, ISBs can be replicated in different geographies, sectors or focus areas. For instance, ISBs can be customized to address a region's most pressing development issues in high-impact sectors such as sustainable agriculture, clean energy, access to education, affordable healthcare, water and sanitation, among others.

Prior to structuring an ISB, the impact investment intermediary structuring the bond will have to diagnose the market need and relevant value chain to assess key gaps that can be addressed by the ISB, estimate the profile of potential pipeline of underlying borrowers and identify regulatory constraints that need to be considered while designing the mechanism. This would ensure the ISB is aligned to address local needs, designed to bring in private sector investors from both within and beyond the region and well positioned to mobilize large-scale capital to accelerate the region's development agenda.



## IIX SUSTAINABILITY BONDS

### DISTINGUISHING BETWEEN IIX SUSTAINABILITY BONDS AND PAY-FOR-SUCCESS MECHANISMS

IIX Sustainability Bonds are very different in structure from pay-for-success mechanisms, such as Social Impact Bonds (SIBs) or Development Impact Bonds (DIBs). While pay-for-success mechanisms have been able to advance in developed markets they may struggle in a developing context and are not designed to support IEs. The five main points of differentiation are outlined below:

	Pay for Success Mechanisms	IIX Sustainability Bonds
<b>Impact – Measurement and Assessment</b>	Impact is assessed after the instrument is issued/sold to investors	Social due diligence done prior to the entity being selected, as well as during the life of the bond
<b>Returns – Payment Terms</b>	Investors get financial returns based on the achievement of pre-determined social outcomes	Investors are paid risk-adjusted returns (principal + coupon) regardless of achievement of anticipated social outcomes
<b>Risk – Stakeholder that assumes the Risk</b>	Entire risk is shifted to investors	Risk is shared between investors and other partners (example: guarantor)
<b>Borrowers – Legal Structure and Repayment Ability</b>	Usually an NGO or Non-Profit – this mandates a third party payback investors (usually a government or donor agency)	IEs and MFIs – borrowers themselves pay back investors over time
<b>Liquidity – Exit Opportunity Available to Investors</b>	Investors don't have any clear exit opportunity; full repayment is received upon bond maturity	Investors have the option to trade the Bond on the stock exchange; in case of ISBs as well, full repayment is received upon bond maturity

While both instruments are highly innovative, ISBs have been designed to address the specific nuances and challenges that arise in a developing country:

- In regions such as Asia and Africa where multiple factors could play into the achievement of social outcomes, it becomes difficult to measure impact and validate results based on a single intervention. This is further complicated by the fact that pay-for-success mechanisms mandate expensive M&E measures that put further pressure in an already resource-constrained environment. ISBs take this into consideration by ensuring bondholders get paid regardless of social outcomes. Instead, the social impact is ensured in three ways: (i) conducting a rigorous pre-selection process that assesses the impact prospect and projects potential impact trajectory; (ii) entering into contractual obligations with borrowers which restricts use of loan proceeds to ensure social objectives are achieved as part of a loan agreements; and (iii) ongoing reporting to ensure complete transparency of social performance.
- On the demand side, the capital recipients of pay-for-success mechanisms (such as NGOs) usually have limited scale and are financially unsustainable, resulting in limited deal sizes and reduced appeal to private sector investors. IEs and MFIs tend to be better equipped to absorb and deploy

## IIX SUSTAINABILITY BONDS

capital effectively to not only create scalable impact but also to repay bondholders over time. Thus, pay-for-success mechanisms tend to be limited in the amount of capital they are able to absorb whereas the entities that are part of the ISB portfolio are able to absorb capital more effectively.

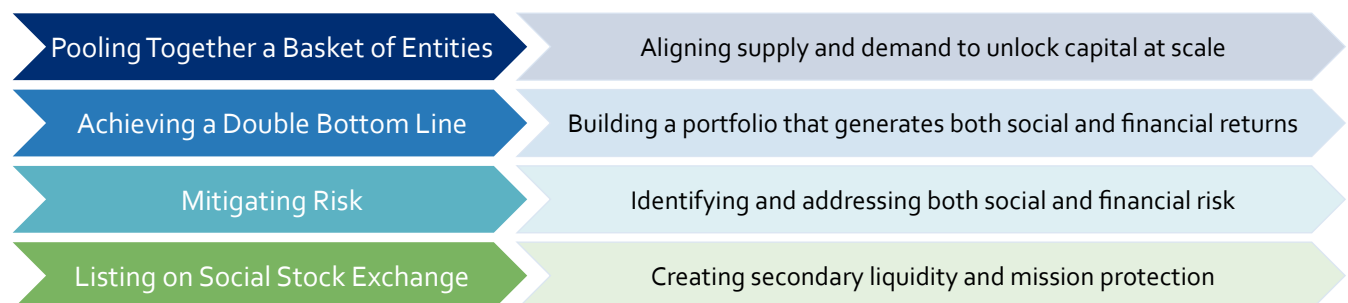
- On the supply side, ISBs do not have any dependency on a third party (donor or government) to pay the bondholders, unlike pay-for-success instruments. ISBs are financially sustainable which allows them to be easily replicated and improves the chances of using the same structure to unlock capital in the future. With a pay-for-success instrument, the mechanism can be replicated only if the third party agrees to remain a part of the equation. In an increasingly resource-constrained environment, ISBs are well equipped to tap into private sector capital and unlock the potential of capital markets to accelerate the global development agenda.

### HOW IIX SUSTAINABILITY BONDS ARE INNOVATIVE

Access to capital is a perennial challenge for IEs. As introduced by Monitor and Acumen in 2012, the 'pioneer gap' highlights the difficulty for IEs to gain access to growth capital. Many of these IEs face various problems that inevitably arise from implementing innovative business models in developing countries, including "poor infrastructure, customers with limited ability to pay, the challenges of attracting talented managers, and nonexistent supply chains".<sup>1</sup> As a result, these IEs present significant risks that investors are unwilling to take on at projected rates of financial returns.

ISBs aim to address this very issue and unlock greater amounts of investment capital for these IEs. By pooling high-impact enterprises into a basket of entities and incorporating various mechanisms to alleviate risk for investors, ISBs present a groundbreaking solution that overturns conventional investment approaches toward IEs.

There are four innovative aspects of ISBs that, upon replication and scale, promise to bridge the 'pioneer gap' that IEs face [Figure 2]:



**FIGURE 2: INNOVATION AT EVERY STAGE OF ISB DEVELOPMENT**

The following section describes each of these four dimensions.

<sup>1</sup> Closing the pioneer gap, SSIR 2013 [http://ssir.org/articles/entry/closing\\_the\\_pioneer\\_gap](http://ssir.org/articles/entry/closing_the_pioneer_gap)



## Pooling together a basket of entities

### Aligning Supply and Demand to Unlock Capital at Scale

In the 2015 Global Impact Investing Network (GIIN) and J.P. Morgan survey for impact investors, two key issues were highlighted as the most pressing challenges for the industry: (i) lack of appropriate capital across the risk-return spectrum; and (ii) shortage of high quality investment opportunities with a good track record. The usual issue with lending to IEs is the relatively low confidence in their ability to pay back risk-adjusted returns and small average deal size, which discourages commercial investors.

WLB will pioneer bringing the IEs and Microfinance Institutions (MFIs) together in a single structure to allow impact investors to leverage on the strengths of both entities to mitigate risk, maximize returns and catalyze impact. A separate set of due diligence questions has been prepared for both the MFIs and IEs that will help in the screening and selection of the final portfolio of entities. IIX and Shujog conducted a site visit to (i) validate the results of the initial selection process; (ii) assess the financial strength of the entity; and (iii) quantify and project impact potential of the borrower. By pooling a group of underlying IEs and MFIs together, ISBs open up investment opportunities that were previously excluded and provide a channel to attract greater amounts of impact investment capital than these entities could have otherwise accessed on their own. Additionally, the basket of borrowers are all financially sustainable entities that are able to repay the loan amount along with interest by using market-based solutions to address development issues.

Ability to attract private sector capital can be further enhanced by including MFIs with a stronger track record in the portfolio, thereby lowering the overall risk. Relatively higher impact and financial return by IEs and MFIs with relatively lower risk-profile allows the portfolio to be optimized for investor's risk-return-impact requirements. Bringing both types of entities together then creates a basket of borrowers with varying risk-return profiles. By pooling younger enterprises with mature MFIs, ISBs will be able to leverage on the MFIs' better risk-return profiles to provide loans to relatively riskier IEs, at a rate that is still attractive to impact investors. At the same time, the Bond also benefits Tier 2 and Tier 3 MFIs that generally have limited access to foreign investment and require capital to scale their impact.

**Outcome:** Pooling together a group of borrowers into a basket allows the overall portfolio to diversify away part of the risk and enhances the opportunity for entities to attract private sector investors.



## Achieving a double bottom line

### Building a Portfolio that Generates Both Social and Financial Returns

The ISBs focus on not only unlocking large amounts of capital from new participants, but also effectively utilizing this capital to create scalable and sustainable impact. This mandates balancing social impact with financial returns throughout the bond structuring process, starting with pipeline development and continuing on an ongoing basis through the life of the bond. IIX’s approach to achieving a double bottom line via ISBs is outlined below:

- Pre-Bond Issuance Dual Due Diligence on Underlying Borrowers:** The first step towards creating an effective ISB is deciding the appropriate risk-return-impact targets of the instrument. This framework will act as a guideline for the impact investment intermediary to build a portfolio. The impact investment intermediary and the Measurement & Evaluation (M&E) partners should coordinate to conduct a rigorous due diligence on potential borrowers ahead of finalizing the portfolio, to assess performance on both business and impact related criteria. The broad dimensions that should be assessed as part of the due diligence process include:

BUSINESS-RELATED CRITERIA	IMPACT- RELATED CRITERIA
Regulatory Environment	Mission Prioritization
Competition and Market Positioning	Corporate Governance
Shareholders and Organizational Structure	Environmental Impact
Audit and Control Systems	Social Performance Management
Liquidity and Capital Structure	Poverty Targeting
Material Contracts and Business Strategy	Client Satisfaction and Responsible Pricing
Legal Proceedings and Disputes	Employee / Supply Chain Actor Protection





# Mitigating Risk

## Identifying and addressing both social and financial risk

ISBs view risk from a dual perspective – financial risk and mission failure or social risk. This section outlines how ISBs leverage the strength of partnerships with diverse stakeholders to adequately alleviate such perils:

- Mitigating Financial Risk through Guarantee Facility Provided by Donor or Government Partner:** ISBs should include a guarantee aspect, where the partnering government or donor agencies will cover a portion of the losses in case of default. This guarantee effectively improves the risk-return profiles of IEs and compensates for the operational challenges that young IEs have to overcome. By incorporating aspects of blended finance, the ISBs aim to leverage on public funds from donor agencies to trigger and unlock larger amounts of private capital into the impact investment space. If borrowers do not default, the funds allocated by the guarantor can potentially be redirected for subsequent bond issues or other projects, allowing for a more efficient use of donor funding.
- Mitigating Social Risk and Linking it to Financial risk:** The Measurements and Evaluation experts should focus on pre-empting and addressing social risks during the social due diligence process by proactively identifying and finding solutions to issues that could create negative externalities, cause mission drift or in any way compromise the impact potential of the Bond. This includes governance related issues, negative environmental impact and social issues faced by beneficiaries or employees, among other risks [more details provided in Section 4]. The ability of borrowers to use social outcomes as a way to diminish long-term financial risk deepens the sustainability of the instrument and increases the probability of success. The Measurement and Evaluation experts should preemptively take into account a variety of social impact related factors that could bring about financial stability in the long run. Some of these factors are listed below:

SOCIAL IMPACT CRITERIA	LONG-TERM EFFECT ON FINANCIAL STABILITY
Corporate Governance	Reduction of Reputational Risk
Positive Impact on Environment	Reduction of Regulatory Risk or Legal Issues
Employee Benefits	Improved Employee Retention and Productivity
Focus on End Beneficiaries	Improved Customer Retention and Earning Ability
Affordability and Accessibility of Products	Higher Growth Potential and Market Penetration



## Listing the Bond

### Creating Secondary Liquidity and Mission Protection

ISBs will be listed on the the Stock Exchange of Mauritius (SEM). Initially, ISBs will be listed on Impact DEM, a compartment within the SEM’s Development and Enterprise Market Platform. Once there is a critical mass of ISBs or other socially-oriented instruments on the platform, these instruments will be migrated to Impact Exchange, a platform operated by the SEM in cooperation with IIX, regulated by the Financial Services Commission, Mauritius. Impact Exchange devoted to listing shares and bonds issued by impact enterprises, NGOs and social impact funds (impact entities) that meet stringent listing criteria relating to social and environmental impact. Listing on an exchange provides a unique opportunity for high-impact entities to raise investment capital to scale and deepen their social and environmental commitments while offering investors a means to invest in and trade securities issued by organizations that reflect their values. It should be noted that ISBs are listed on Impact DEM before migrating on to Impact Exchange for two reasons: (i) it is more cost effect to list on an existing platform than to list on a platform with only one security; and (ii) the investors are still subject to the same benefits of secondary liquidity and will still receive ongoing reporting on both financial and social performance.

The following section explains the key benefits of listing on Stock Exchange of Mauritius (Figure 3):

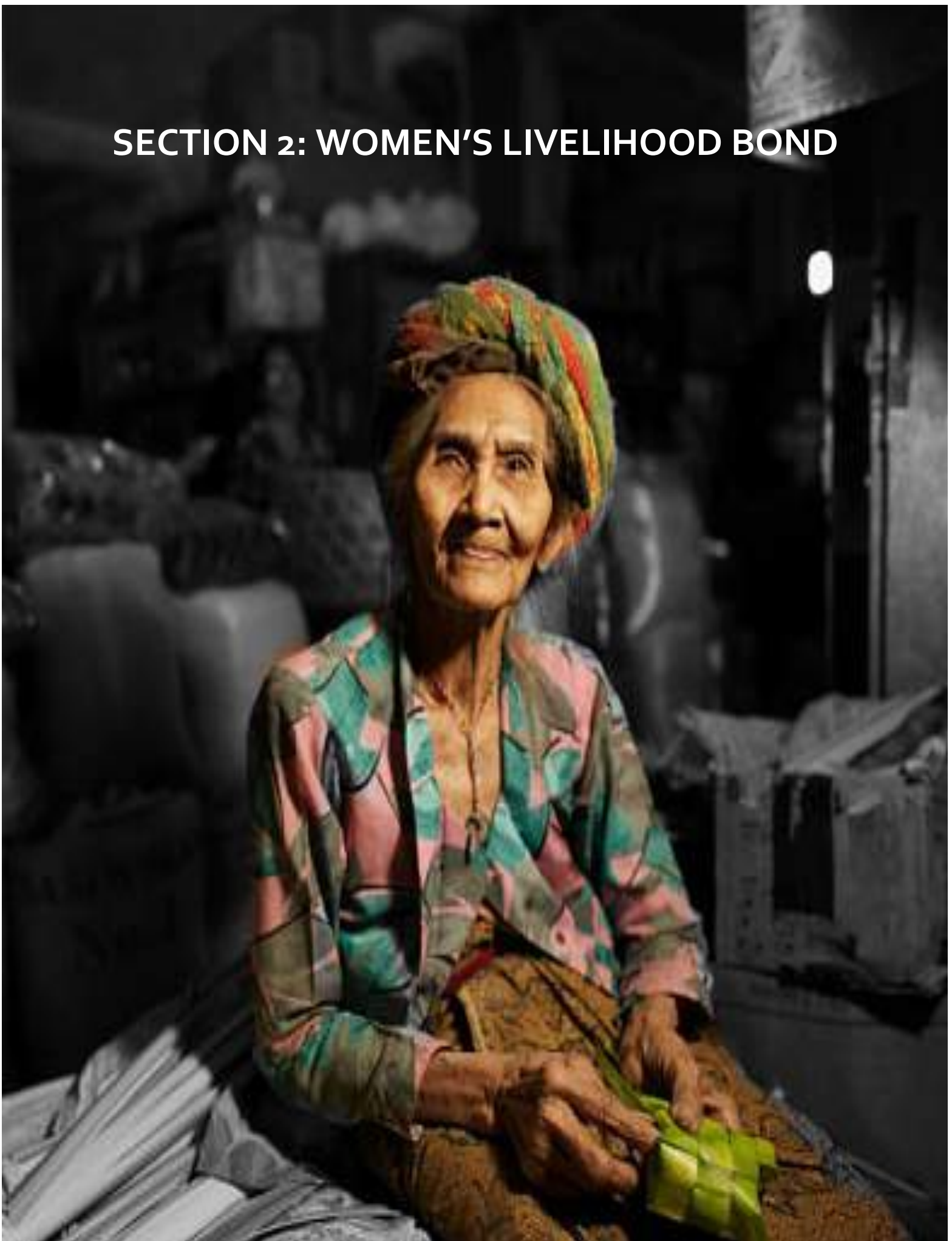


**FIGURE 3: BENEFITS OF LISITING ON IMPACT EXCHANGE**

- **Secondary liquidity** – Being a listed entity establishes a market for the issuer’s securities, providing investors with a well-organized, transparent and regulated market to trade these securities in. Liquidity offers early investors in impact entities the opportunity to exit their investments. If investors are not satisfied with the impact being created they could potentially sell the bond on the exchange. Analyzing trading activity will serve as a good ‘litmus test’ on investor preferences and response to social performance.
- **Mission protection** - Listing demonstrates an organization’s commitment to its social and/or environmental mission as all listed entities must meet rigorous impact criteria and commit to ongoing impact reporting. The transparency provided by the dual reporting of financial results and social and/or environmental impact will publicly raise the issuer’s profile and will draw more potential investors. This will lead to a more diversified group of investors, which may increase the demand for the issuer’s securities and increase their value. It may also increase the availability of capital supply should an issuer need additional capital in the future.
- **Access to Global Investors** – Listing on an exchange will provide the issuer greater exposure to retail and institutional impact investors, the media and the general public. Many Institutional investors and fund managers are subjected to restrictions; for instance, institutional investors are typically barred from investing in securities that are not listed on a regulated stock exchange. Fund managers are often restricted from investing in securities that do not have a publicly-quoted price. International investors account for over 35% of the SEM’s daily turnover.
- **Real Time Information Efficiency** – The SEM website provides daily information about prices and listed issuers. In addition, the SEM is connected live to a top bracket of global platforms, including Thompson Reuters, Interactive Data, Financial Times, Factset, Bloomberg and I-Net Bridge, enabling both retail and institutional investors worldwide to follow its markets real time. The coverage of the SEM’s data by global data platforms is a powerful marketing tool to put the Exchange on the radar of a wider spectrum of institutional investors, thus attracting more foreign investor interest on the market.
- **Accountability and Efficiency** - The requirements for rigorous disclosure will lead to better systems and controls, improved management accountability and greater operating efficiency within the organizations – in particular among these IEs which are usually not subjected to extensive due diligence. Credibility in listed companies is reinforced by the existence of the stock exchange’s regulatory framework. Having a number of institutional investors can bring with it increased business credibility, stability and wider business networks for an issuer as well.
- **Priority Alignment** – Bond financing allows issuers to focus on their core mission of serving society and/or the environment, unhindered by the pull on resources typical of traditional donor fundraising activities.
- **Highly Attractive Tax Regime** – Mauritius has a highly attractive tax regime. Foreign investors investing on the SEM can benefit from no withholding tax on dividends; no capital gains tax; free repatriation of profits, capital and interest; and Double Taxation Avoidance Treaties and Investment Promotion and Protection Agreements with multiple countries.



## SECTION 2: WOMEN'S LIVELIHOOD BOND





## THE NEED: WOMEN ARE AT THE HEART OF DEVELOPMENT

Human capital is a core driver of sustainable, long-term economic growth. If half of the population is underdeveloped or underutilized, an economy will never reach its full potential. Discrimination against women can hinder economic growth by essentially cutting out half the population from contributing to a country's demographic dividend. There is a bidirectional relationship between economic development and women's empowerment, defined as improving the ability of women to access the constituents of development, including the resources and opportunities to participate in the labour force. Women are at the heart of development in Asia, playing a pivotal role in supporting their households and communities in achieving food security and overall natural resource management. They are the backbone of rural enterprises, fuelling local and global economies. Research reveals economically secure women are more likely to have healthier and better-educated children, creating a positive, virtuous cycle for the broader population.

As such, providing sustainable livelihood opportunities for women is essential to drive forward the global development agenda and to reinforce economic growth. Yet, in many countries across Asia, women and girls face persistent structural constraints that keep them trapped in subsistence livelihoods, reduce their resilience to economic and environmental downturns and have severe negative repercussions on their political participation which compromises holistic economic development. Four key issues are listed below:

- **Poor access to credit and finance** resulting in vulnerability to economic shocks and stresses
- **Absence of market linkages** restricting women to the informal workforce
- **Limited availability of affordable goods** constraining ability of women to maximize productivity
- **Lack of reliable power supply** that is cost-effective and accessible in remote or rural locations

IIx acknowledges the dire need to empower women by supporting and expanding the sustainable livelihoods spectrum [Figure 4]. To achieve this, a comprehensive multi-dimensional strategy that includes providing women with access to capital, markets, essential goods and natural resources, is required. There are many IEs and MFIs that focus on empowering women to overcome gender-based constraints and socio-economic barriers to achieve a sustainable livelihood.



**FIGURE 4: SUSTAINABLE LIVELIHOODS SPECTRUM**

However, lack of access to funding is a major barrier to growth, preventing IEs and MFIs from reaching a greater number of women beneficiaries. It is essential to address this funding gap by unlocking additional sources of capital from new players (from the private sector) to complement the efforts of traditional players that focus on gender issues (governments, donors, foundations, NGOs).

## THE SOLUTION: ANATOMY OF THE WOMEN'S LIVELIHOOD BOND

The IIX Women's Livelihood Bond (WLB) is the first instrument in the ISB series and is designed to bring in fresh private sector capital for IEs and MFIs focused on women's livelihoods to scale operations, deepen impact and sustain results. A \$20 million debt security, the bond pools together a basket of these high-impact entities. A Special Purpose Vehicle (SPV) based in Singapore will issue the bonds that will be sold via IIX's investment banking partners to accredited and institutional investors. The bond proceeds will then be lent to the underlying entities.

This will be the first impact investing instrument to be listed on a stock exchange, thereby providing an additional layer of secondary liquidity, ensure transparency of results and mitigate risk of mission-drift. Figure 5 outlines the key partners that are supporting different parts of the mechanism.

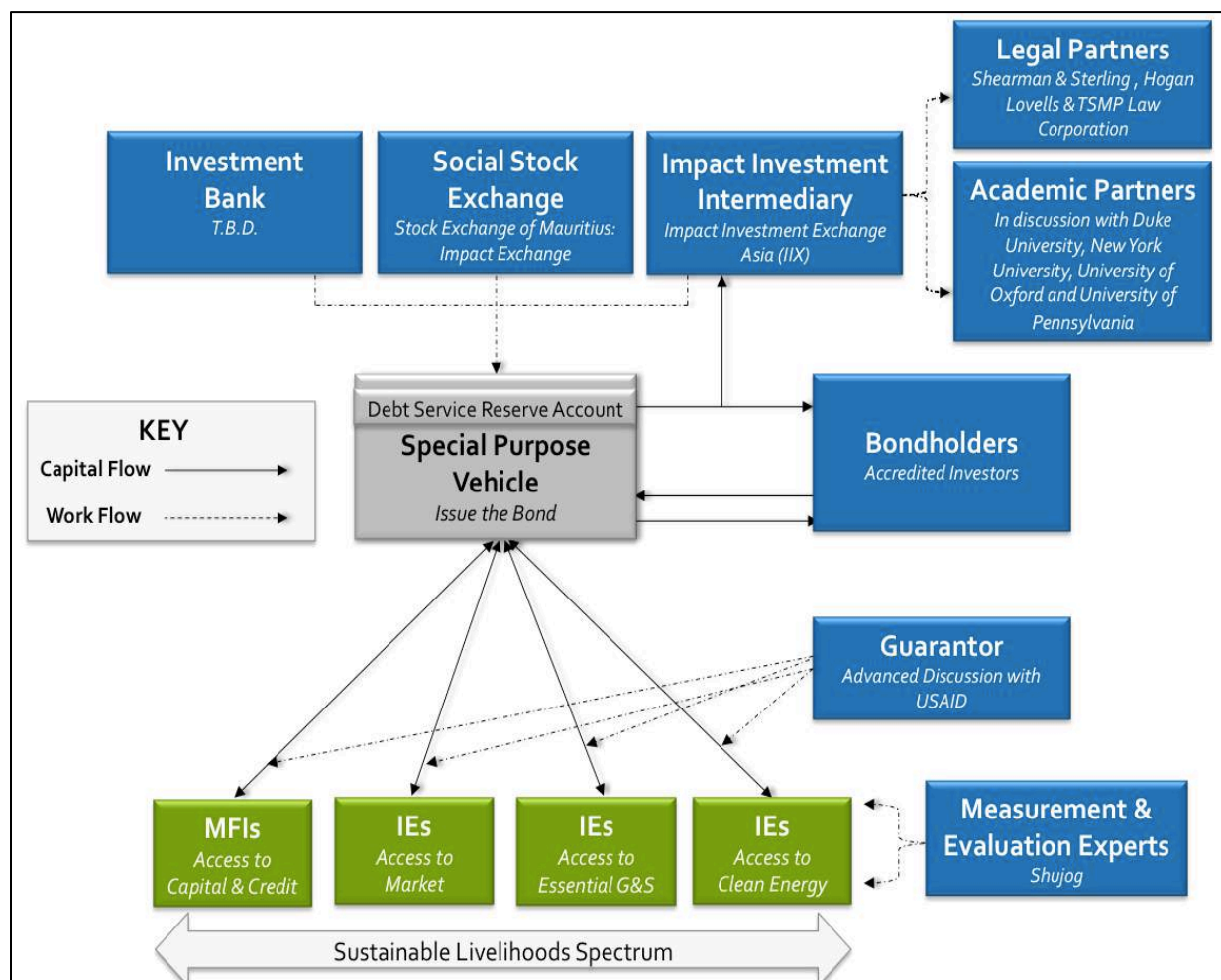


FIGURE 5: WOMEN'S LIVELIHOOD BOND MECHANISM

Figure 6 provides an overview of the underlying borrowers in the SPV 'basket' that focus on different aspects of the sustainable livelihoods spectrum in Asia (exact figures are subject to change):

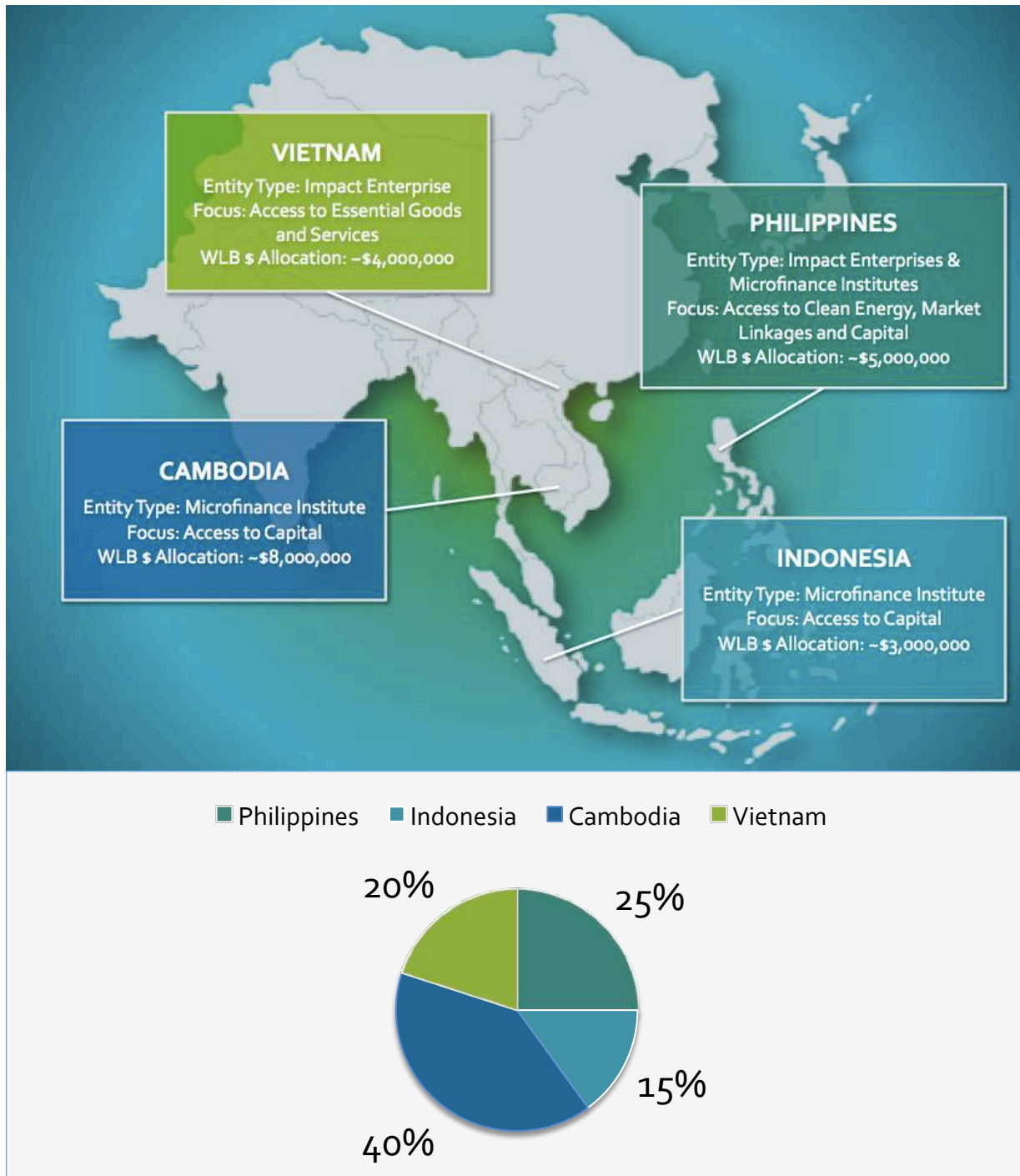
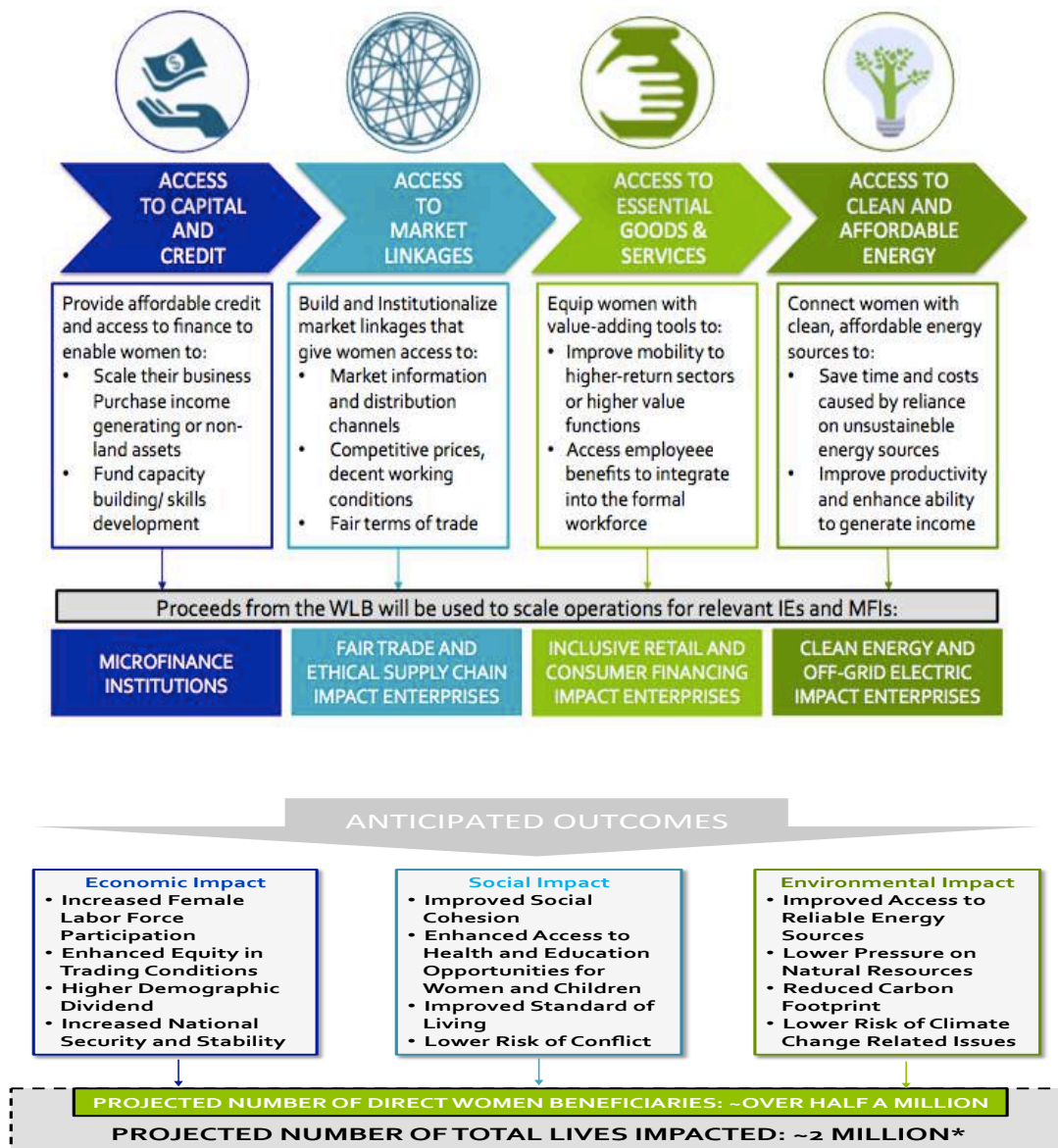


FIGURE 6: WOMEN'S LIVELIHOOD BOND PORTFOLIO MAP AND CAPITAL ALLOCATION PIE CHART

## SUSTAINABLE LIVELIHOODS SPECTRUM

*A livelihood is sustainable when it can cope with and recover from stress and shocks, maintain or enhance its capabilities and assets, provide earning opportunities for the next generation and contribute to wider development goals.*

IIX has taken a holistic approach to assessing the sustainable livelihoods spectrum that enables women to transition from subsistence to sustainable livelihoods. The underlying borrowers of the WLB will focus on the spectrum of factors that play a role in redefining the dominant narrative to view women as solutions to economic growth instead of victims of social inequality [Figure 7]. The following sections outline each of these dimensions in depth, also highlighting the type of entities that would be potential underlying borrowers for the bond and the anticipated outcomes on women, the wider community, the economy and the environment.



**FIGURE 7: SUSTAINABLE LIVELIHOODS SPECTRUM**

\*Projected number of total lives impacted includes both: (i) male and female direct beneficiaries; and (ii) indirect beneficiaries



## WOMEN'S LIVELIHOOD BOND: ACCESS TO CAPITAL AND CREDIT



Women in Asia face a multitude of challenges, both financial and non-financial, that prevent them from obtaining the same levels of access to capital that men enjoy. Generally, creditors might be reluctant to lend to women-run enterprises if they have the perception that such projects tend to have poorer risk-return profiles as compared to those run by men. This could be because of the propensity for women to run small, informal micro enterprises or because women entrepreneurs tend to have lower education levels than their male counterparts.<sup>2</sup> As for non-financial barriers, women in some countries face challenges such as a lack of credit bureaus, tedious application procedures (for women), among others – factors, which make it even harder to women to get credit.<sup>3</sup>

By unlocking women's access to capital, the WLB will make significant progress in creating positive impact on women's ability to obtain financing. Women will be able to take control of their immediate borrowing and consumption, allowing them to invest in income-generating activities or household assets. More importantly, with this initial access to credit and financial services, women will be able to start building credit histories that can help them borrow larger amounts of capital to expand their businesses in future. There is great potential for successful women-run enterprises to create follow-on impact through employment and expanded supply chains, further providing sustainable livelihoods for more women.

### ANTICIPATED OUTCOMES



<sup>2</sup> [http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/02/13/000333037\\_20120213000822/Rendered/PDF/667610WP00PUBL065805BoStrengthening.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/02/13/000333037_20120213000822/Rendered/PDF/667610WP00PUBL065805BoStrengthening.pdf) 8-9

<sup>3</sup> [http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/02/13/000333037\\_20120213000822/Rendered/PDF/667610WP00PUBL065805BoStrengthening.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/02/13/000333037_20120213000822/Rendered/PDF/667610WP00PUBL065805BoStrengthening.pdf) 7

## WOMEN'S LIVELIHOOD BOND: ACCESS TO MARKET LINKAGES



Market linkages are essential in order to improve incomes and help women progress beyond rural poor and low-income levels. The development of markets over the years has given rise to today's system where rural women and smallholder producers in general have to negotiate complex relationships with market intermediaries. Many of these are heavily inequitable at the expense of the women producers. Also, smallholder producers generally lack market understanding and price information and are, therefore, forced to negotiate from a position of weakness.<sup>4</sup> These disadvantages are generally exacerbated for women as compared to men.<sup>5</sup>

By strengthening women's access to market linkages and educating them on available opportunities in the market, WLB borrowers can empower women to negotiate for more equitable market relations. Besides strengthening women's bargaining positions, exposure to and integration with market-oriented models, it will also enable them to identify niche areas in the market where they can capture opportunities to earn higher incomes.<sup>6</sup> The Fair Trade model is one such example, where women producers can manufacture value-added products and receive a premium above available market prices. The evolving market for agricultural products presents significant opportunities for women to identify sustainable livelihoods and the WLB will help women benefit from these linkages. Ultimately, women producers will be equipped with economic control over their returns, enhanced social status and greater household-decision making authority. This will result in substantial improvement in living standards for themselves and their families.

### ANTICIPATED OUTCOMES



<sup>4</sup> <http://www.ifad.org/igbdocs/gc/26/e/markets.pdf> 9-10

<sup>5</sup> <http://siteresources.worldbank.org/INTGENAGRLIVSOUBOOK/Resources/Module5.pdf> 173

<sup>6</sup> <http://www.ifad.org/pr2013/report/e/pr2013.pdf> 139



## WOMEN'S LIVELIHOOD BOND: ACCESS TO ESSENTIAL GOODS



Women employed at the lower end of the wage scale in the formal workforce in developing economies often have access to basic employment benefits including job stability and a minimal income that enables them to provide for their families and meet basic living standards. However, they have limited purchasing power to access certain essential goods and services that can (i) enhance well-being (household goods, loan products and financial services); (ii) enhance earning capacity (training to improve vocational skills, education, financial literacy); and (iii) improve resilience to economic shocks and stresses (access to affordable healthcare products and medical services).

With access to broad-based skills development, women can enhance their productivity for various aspects of their livelihoods, achieve financial security and improve their ability to support their families. Further, it has been shown that empowering women leads to amplified multi-generational impact, as mothers usually reinvest their money in their children's health, nutrition and education.<sup>7</sup>

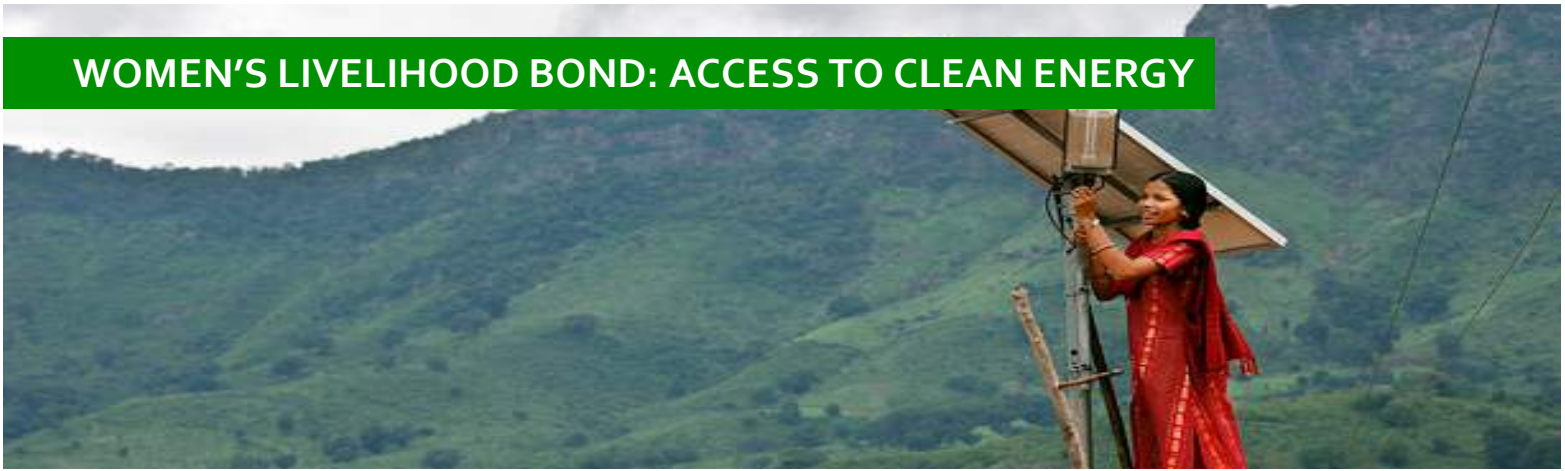
By providing access to these goods and services through low-cost installment finance, WLB borrowers can effectively unlock purchasing power and bridge the affordability gap for women workers in developing economies. Access to this market platform can also lead to improved spending behavior – engineering a shift away from informal borrowing facilitating greater savings. Through the WLB, women workers will be provided with access to affordable life-enhancing products and services that can help them transition to a more economically secure and socially stable life.

### ANTICIPATED OUTCOMES



<sup>7</sup> [http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/02/13/000133037\\_20120213000822/Rendered/PDF/667610WP00PUBL06805Bo5Strengthening.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/02/13/000133037_20120213000822/Rendered/PDF/667610WP00PUBL06805Bo5Strengthening.pdf)

## WOMEN'S LIVELIHOOD BOND: ACCESS TO CLEAN ENERGY



Poor access to rural infrastructure, in particular energy and technology, disproportionately affects women in developing countries. They usually face more difficulties obtaining energy supplies, which means, women have less time to devote to other daily activities. Progress has been made in terms of rural electrification efforts, but there is still widespread use of hazardous and unhealthy energy sources like kerosene lamps in developing countries. Besides the risk of burns, prolonged exposure to fumes from kerosene lamps and stoves have significant costs on human health.<sup>8</sup> As the main users of such energy sources, women bear the majority of these negative impacts.

Technological advancements can solve many of these problems for women who lack access to reliable alternatives in the absence of grid electrification. Off-grid solutions such as solar home systems can help save time and raise productivity levels.<sup>9</sup> Considering the long hours that women typically spend on household activities, such as cooking and running home-based micro-enterprises, such improvements to their productivity and livelihoods can immensely empower them. Besides the direct benefits from improved health and increased disposable incomes, women will be able to ensure a stable and sustainable environment for their families, the wider community and future generations. On a macro level, sustainable energy focused IEs can also help economies strengthen national security in conflict-prone areas where resource constraints are often the root cause for violence and social unrest. Through the WLB, IIX will support Impact Enterprises to ignite development in some of the most rural and remote locations in Asia, by providing access to off-grid energy supply.

### ANTICIPATED OUTCOMES



<sup>8</sup> <http://www.unep.org/ccac/Media/PressReleases/KeroseneLampsImportantTargetforReducingPollu/tabid/794525/Default.aspx>  
<sup>9</sup> <ftp://ftp.fao.org/docrep/fao/010/a1021e/a1021e00.pdf> 17-18



# SECTION 3: BOND STRUCTURING PROCESS

BOND STRUCTURING PROCESS



## Overview

The WLB structuring process is broken down into four key work streams [Figure 8]:

- **Product Development:** Developing the WLB mechanism by defining overarching risk-return-impact parameters, building the financial model and designing key risk mitigation features.
- **Pipeline Development:** Identifying and screening potential underlying borrowers – IEs and MFIs – which share the overarching social mission of the bond and are also financially sustainable and able to repay the loans.
- **Partnership Development:** Coalescing diverse stakeholders that can play a role in developing the bond by leveraging their resources, expertise and networks.
- **Bond Issuance:** Selling the bond to impact investors, listing the bond on the Impact Exchange to facilitate trading and continuing with knowledge management and monitoring, evaluation and reporting.

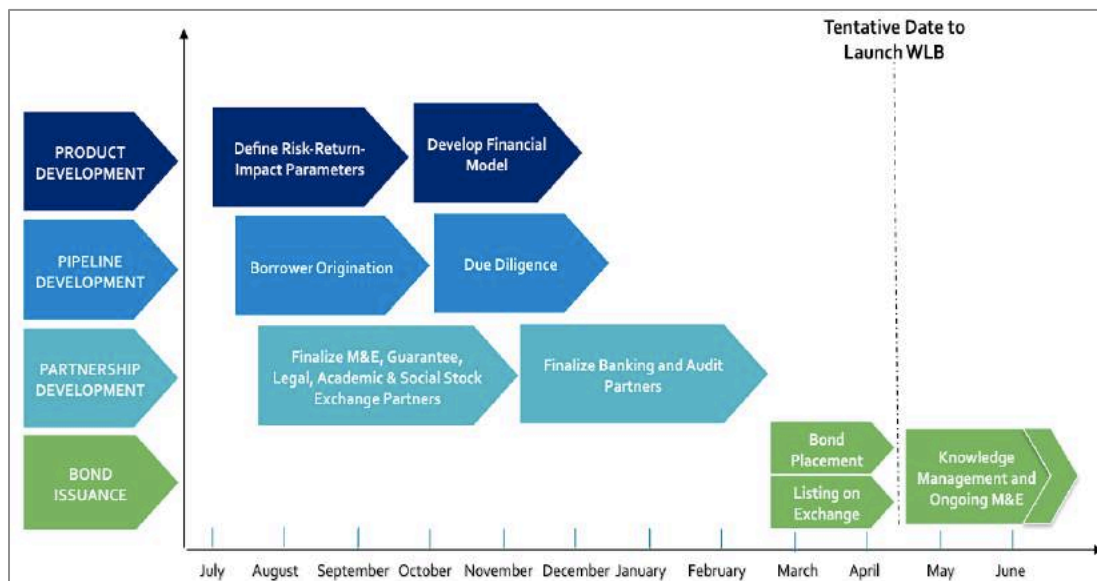


FIGURE 8: WLB BOND STRUCTURING TIMELINE

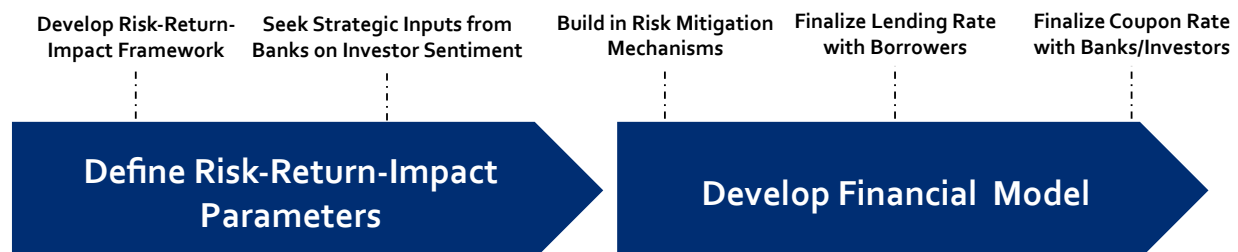


# BOND STRUCTURING: PRODUCT DEVELOPMENT



## Product Development

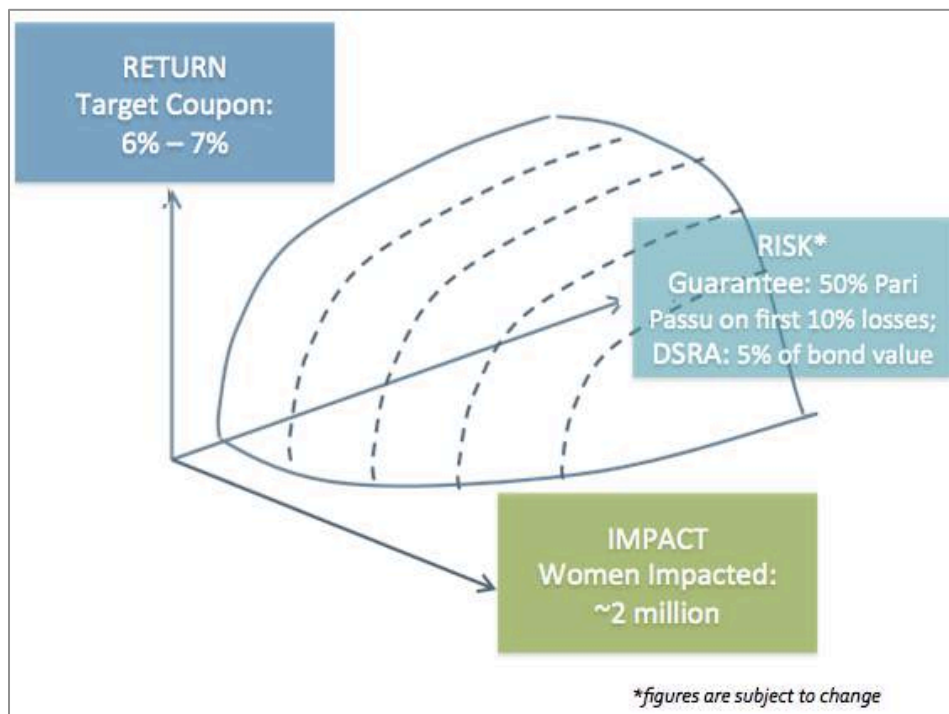
Product development involves designing the financial instrument that is customized to the geographic context, taking into consideration the target risk-return-impact parameters, and effectively mobilizes funds such that the instrument itself is sustainable. This process involves two key phases as detailed in the following section:



## PHASE 1: FINALIZE RISK-RETURN-IMPACT PARAMETERS

The first step in product development for an ISB involved laying out the parameters that will govern the bond structuring process. Traditional metrics considered were target rate of return and commensurate level of risk that bondholders would find acceptable.

In addition, IIX took a 3-D investing approach by introducing a third parameter: target impact. This entailed creating a framework (Figure 9 below) that estimated ranges of each of the three parameters that are acceptable to investors and other stakeholders. This framework guided pipeline development as well as the subsequent steps of product development.



**FIGURE 9: WLB 3-D RISK-RETURN-IMPACT FRAMEWORK**

This was a critical part of the product development process because it allowed the bond mechanics to be completely aligned with key constraints from the onset, enabling bond structures to ensure alignment with market preferences on risk and return.

At the same time, investor interest in catalyzing impact and the consequent trade-off with risk and return were also kept in mind. This mandated alignment and a constant dialogue with partners – in particular with investment banks that can provide insights on market sentiments and investor preferences regarding factors such as the geographic scope, guarantee structure, bond tenor and coupon.



## PHASE 2: DEVELOP FINANCIAL MODEL

Once a range of risk-return-impact parameters are defined, the financial model helped the bond issuer narrow down on the specifics. ISBs are designed to be sustainable instruments that generate sufficient cash flow streams to both cover ongoing costs and payments to bondholders. This mandated a structured approach that takes into consideration certain financial criteria [Figure 10], as detailed in the following section:

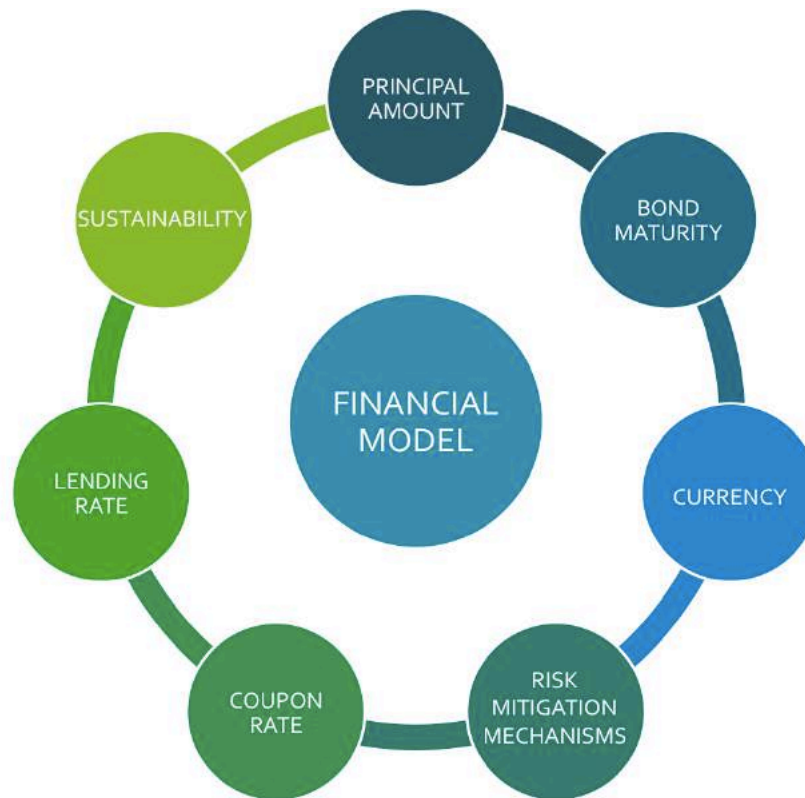
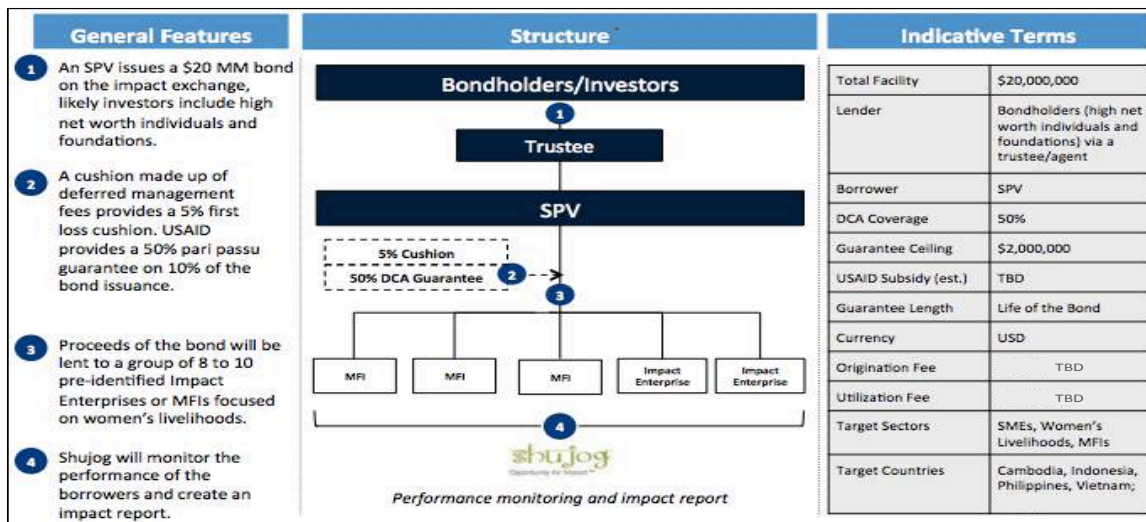


FIGURE 10: FINANCIAL CRITERIA CONSIDERED

- (i) **Principal Amount and Maturity:** The financial model for the WLB went through several iterations testing out different bond sizes and maturities. A sensitivity analysis that calculated the different risk and return implications resulted in increasing the bond size to \$20 million and reducing the tenor to four years. The initial anticipated bond size was \$10 million over a five-year period. It was imperative to constantly tweak the financial model to align supply of capital with demand and ability of borrowers to absorb, deploy and repay capital. This is done by ensuring that the amount lent to borrowers is based not only on their need for capital but also their ability to utilize it effectively to create intended impact and their ability to pay investors back both periodic interest and principal upon maturity.

- (i) **Currency:** Given that the WLB is a multi-country bond, macro level analysis informs key decisions that need to be integrated into the financial model such as the currency denomination. The bond must be issued in a currency that is suitable for both investors and borrowers. If it is not possible to lend to borrowers in certain countries in the same currency in which the bond is denominated, the bond issuer may consider (i) hedging the loan to mitigate currency risk; (ii) limiting the total amount lent to entities in that country; or (iii) lending to these entities through a sister entity incorporated in another country to which it will be possible to lend in hard currency. For the WLB, IIX will issue the bond in USD. All repayment will be in USD with the potential exception of one entity, which will be hedged as required.
  
- (ii) **Risk Mitigation:** Apart from hedging the currency risk, IIX also factored in a guarantee mechanism and a DSRA to provide investors with protection. When building this into the model, there were certain cost implications that will reduce the returns available for investors – for instance, guarantees usually have an upfront cost and an ongoing cost. In case of the WLB, IIX is in advanced discussion with USAID to provide a 50% pari passu guarantee to protect upto 10% of the portfolio. Although the key features of the guarantee facility are still being finalized, a tentative structure is detailed below in Figure 11:



\*The above structure is under consideration

**FIGURE 11: GUARANTEE FACILITY PROVIDED BY USAID FOR THE WLB**

Using funds from donors and governments to provide additional financial security allows the WLB to unlock capital for high-impact entities that otherwise struggle to tap into capital markets. The guarantee mechanism is designed to leverage 10 times more funding from investors. This epitomizes an ideal way to use grant or philanthropic capital that effectively unlocks new sources of funding, enables participation from new mainstream participants and allows creation of impact at scale.

- (iii) **Coupon Rate and Lending Rate:** It was necessary for IIX to have a good sense of both investor preferences and a strong understanding of borrower limitations to ensure the WLB is an attractive product for both. It is vital that the portfolio is a good investment opportunity and simultaneously, is mobilizing capital for entities that can create demonstrable outcomes, have scalable business models and a need for capital.

Striking the right balance between the lending rate and coupon rate can be achieved by having parallel conversations with the banks and the borrowers and working iteratively on the financial model to ensure optimization on the three-dimensional efficiency frontier. The coupon rate the WLB will be offering is between 6% and 7%. The average lending rate for the portfolio of borrowers will be approximately 2.5% higher than the coupon after accounting for cost of the guarantee, the DSRA and other upfront costs.

- (iv) **Sustainability:** The overarching objective for IIX was to design a sustainable instrument. An overview of the cost centers and revenue streams IIX factored into the WLB model is given below:

COST CENTERS	
UPFRONT COSTS	ONGOING COSTS
SELLING COMMISSION	SERVICING AND ADMINISTRATIVE COSTS
LEGAL FEE	M&E COSTS
GUARANTEE UPFRONT FEE	GUARANTEE ONGOING FEE
LISTING COSTS	CURRENCY HEDGING COSTS
AUDIT COSTS	PAYING AGENT AND TRUSTEE COSTS

The bond will generate revenue streams in the form of a structuring fee and a monitoring and management fee that that will allow IIX to cover key costs ongoing costs.

REVENUE STREAMS (FOR IIX)
STRUCTURING FEE
MONITORING AND MANAGEMENT FEE

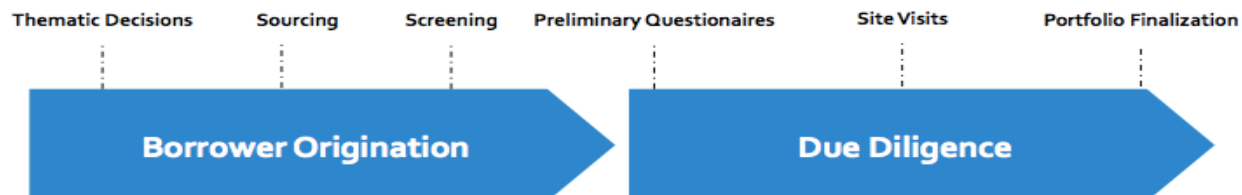
## BOND STRUCTURING: PIPELINE DEVELOPMENT



### Pipeline Development

The key objective of the pipeline development phase is to identify a group of underlying borrowers and pool them together in a basket based on their risk-return-impact profiles. For the WLB, these entities – IEs and MFIs – are the underlying borrowers that will use the capital raised by the bond to empower the lives of over half a million women to transition from subsistence to sustainable livelihoods and over two million lives in total, including both direct and indirect beneficiaries. Pipeline Development is an intensive process, which entails rigorous assessment of social and business criteria of the portfolio to ensure both impact and financial returns are generated and that risk is identified and preemptively mitigated.

To create this basket of entities for the WLB, IIX assumed a structured, two-phase process spanning over a six-month duration: (i) Borrower Origination (ii) Due Diligence. The following section outlines these two phases:





## PHASE 1: BORROWER ORIGATION

### 1. THEMATIC DECISIONS

The first step of the borrower origination process is to clarify the objectives of the bond in terms of risk-return-impact. It is imperative to formulate clear investment policies to express risk preferences and ensure well-informed return expectations to guide product development. It is equally important to define impact goals upfront to enable the bond issuer to build a portfolio that is focused on target outcomes. Articulating the mission of the instrument at the onset lays the foundation for pipeline development and helps tighten the link between investment decisions and impact creation. For the WLB, the mission was to empower women in Asia, recognizing they are at the heart of development and must be viewed as solutions instead of victims.

The next step is to identify the best approach to achieve this mission within the target risk-return-impact parameters, by assessing an array of high-impact sectors. IIX researched and assessed multiple high-impact sectors before designing the women's livelihoods spectrum and finalizing the bond's focus areas: access to capital and credit, access to market linkages, access to essential goods and services, and access to clean energy (as described in detail in the previous section).

**RESULT: Clearly defined investment objectives and thematic focus**

### 2a. SOURCING: DEFINING TARGET BORROWER PROFILE

The next phase in borrower origination is to identify potential borrowers in these sectors that are able to meet certain preliminary criteria that will allow payment of risk-adjusted returns to investors on one hand and creation of scalable impact on the other. The legal structures of target borrowers should be conducive to borrowing and repaying debt capital. Bond issuers must consider whether this mandates inclusion of MFIs in the basket – a decision that will be contingent on the thematic decisions outlined above. For the WLB, it was critical to have both MFIs and IEs as part of the portfolio for three key reasons:

- **Impact:** MFIs address a core aspect of the sustainable livelihood spectrum – access to capital.
- **Returns:** MFIs have consistent need for capital and stable cash flow streams from repayment of loans – this allows them to easily absorb capital and to pay investors back the principal amount plus a return.
- **Risk:** MFIs have a longer track record and are the pioneering impact investment vehicles – they significantly limit the total risk of the portfolio.

### 2b. SOURCING: ACTIVE OUTREACH

The next step in the sourcing phase involves doing strategic outreach to potential borrowers, tapping into existing databases and partner networks to identify new leads and initiating contact with entities that require capital to magnify their impact. It is critical to use this as a litmus test to see if the market is ready for a bond and whether target borrowers have interest in and appetite for using debt securities to unlock capital at scale.

**RESULT: Broad list of potential entities aligned with investment objectives and theme**

## 3a. NEGATIVE SCREENING

This phase begins first with negative screening or avoidance screening – ensuring entities meet certain initial criteria and do not violate any core values of the investment philosophy that is being followed. Key considerations at this point include:

- **Mission Orientation and Prioritization** – The entity must have an impact-first approach so borrowers are mission-driven sustainable entities pursuing a double bottom line. This means that strategic decisions will be guided by impact on target beneficiaries/clients as opposed to being focused solely on profit maximization.
- **Financial Sustainability and Capital Absorption Capacity** – The entity must have positive, stable cash flow that will allow it to absorb and repay debt. If it is a non-profit, it must be revenue generating.
- **No Environmental Externalities** – The entity must not have any spillover negative impact on the environment that contributes to degradation or instability in any form. This is particularly critical for energy, water or agriculture related entities.
- **No Governance or Legal Issues** – The entities must not have any track record that raises red flags in terms of corporate governance, conflict of interest or negative impact on either immediate beneficiaries or the wider community in which the enterprise operates.

## 3b. POSITIVE SCREENING – MACRO INDICATORS

Positive or affirmative screening goes beyond negative screening. Rather than merely excluding entities which create negative impact or do not meet basic financial criteria (as detailed above), positive screening involves proactively seeking effective social outcomes that investors would like to create with their capital, as well as a target rate of return that would be acceptable. This mandates doing a preliminary assessment of the list of potential borrowers based on the factors outlined below; first, at a macro level for target geographies and next, at a micro level for MFIs and IEs:

### MACRO INDICATORS: COUNTRY SELECTION

Poverty Level

Gender Inequality Level

Country Economic Outlook

Regulatory Barriers

Local Market Potential

Ability to Absorb External Financing

Local Currency Volatility

For the WLB, IIX used the above framework to narrow down four target geographies: Cambodia, Indonesia, the Philippines and Vietnam. As a multi-country bond, the WLB adequately balances the trade-off between two factors: (i) controlling costs by narrowing down the scope from entire South-East Asia; and (ii) diversifying risk by distributing the capital raised across four different countries thereby lowering the correlation between the borrowers in the portfolio.

### RESULT: Country Selection

## 3c. POSITIVE SCREENING – MICRO INDICATORS

### IMPACT ENTERPRISE SELECTION: FINANCIAL CRITERIA

Financial Stability	Operational Maturity
(i) Turnover > USD 1 million	(i) Years of Operation
(ii) Significant/International Shareholders	(ii) Total Staff
(iii) Net Profit Last 3 Years (USD) (needs defining?)	(iii) International Financing
(iv) External Audit Report Last 3 Years	(iv) International Partners
(v) ROE	(v) Proven Business Model
(vi) ROA	(vi) Number of Customers / Beneficiaries

### IMPACT ENTERPRISE SELECTION: SOCIAL CRITERIA

Gender Lens (Either one of the two)	Social Mission
(i) Owned or run by women	(i) Clear intent to create social impact
(ii) Low-income marginalized women as main target beneficiaries (empowering them, improving their lives, creating opportunities for them)	(ii) Social mission taken into account in all key decisions (partnerships, branch opening, product launch); social mission integrated in the planning process with achievable goals and good identification of the challenges and constraints
Livelihoods Focus	(iii) Low probability of risk of mission drift
(i) Clear commitment to expanding women's livelihoods efforts or financial independence and security	(iv) Vision and mission shared among shareholders and key stakeholders who may have an influence on decision making
(ii) The ripple effect of women's livelihood opportunity can be positively felt by the family members	Social Performance Management
(iii) Enterprise addresses one of the sustainable livelihoods value chain focus areas: access to capital/credit, market linkages, essential goods & services, clean energy	(i) Adequate tools and systems in place to measure and track social performance - if not, willing to put in place

### MFI SELECTION: FINANCIAL CRITERIA

Financial Stability	Operational Maturity
(i) Net Profit Last 3 Years (USD) (needs defining?)	(i) Years of Operation
(ii) Financial Rating	(ii) OSS
(iii) External Audit Report (Last 3 Years)	(iii) Number of Customers
(iv) Size of Loan Portfolio (USD)	(iv) Number of Branches
(v) Level of Deposit	(v) Total Staff
(vi) Average Size of Loan (USD)	(vi) Foreign Investment
(vii) Key Ratios: ROE, ROA, FSS, PAR (30 Days)	(vii) International Partners

### MFI SELECTION: SOCIAL CRITERIA

Gender Lens	Client Protection
(i) Low-income or marginalized women as main target customers (share of women in portfolio (%))	(i) Transparency of services: loans conditions fully disclosed and clearly communicated
Livelihoods Focus	Responsible Pricing
(i) Clear commitment of lending specifically to improve women's livelihoods and financial independence	(i) Effective interest rate within international benchmarks (or national benchmarks if they exist); effective interest rate compared to what is generally charged for the same services in the country/region (commercial lending rate)
Social Performance Management	
(i) Adequate tools and systems in place to measure and track its social performance	

**RESULTS: Selection of list of entities for due diligence**

**Final Selection of Entities for Due Diligence:** This preliminary assessment helps to narrow down IEs and MFIs that can go to the next level of analysis via an in-depth due diligence based on: (i) a comparative analysis on the impact front; (ii) lending rates each entity is willing to borrow at and consequent implications on the model; and (iii) the trade-off between risk diversification (by adding more entities to the portfolio) and cost implications (not just for upfront due diligence but more critically for the ongoing M&E work that each entity will require over the life of the bond). Entities that are interested to move forward with the due diligence process sign a Memorandum of Understanding (MOU) stating their intent to be a part of the bond.

**Three other components of the origination process are briefly discussed below:** (i) Assessing whether to include for profit MFIs or non-profit MFIs; (ii) Creating an impact assessment framework using Shujog's proprietary methodology (iii) Analyzing the correlation between risk-return-impact to optimize the portfolio

## ASSESSING WHETHER TO INCLUDE FOR PROFIT MFIS OR NON-PROFIT MFIS IN THE WLB PORTFOLIO

At this juncture, IIX also debated whether to include for-profit or non-profit MFIs in the portfolio – a concern highlighted by certain banking partners that IIX was in conversation with. The usual 'higher-social impact' argument commonly used in favor of non-profit MFIs is based on the below hypotheses:

- i. Non-profit MFIs have a higher portion of women borrowers
- ii. Non-profit MFIs make many smaller loans reaching a larger number of the poor
- iii. Non-profit MFIs charge lower interest rates; for-profit MFIs have higher margins
- iv. Non-profit MFIs have lower margins

There is research<sup>10</sup> available to negate all the above points. On average, non-profits do not charge lower interest rates to their clients and have similar margins as for-profit MFIs. A study<sup>11</sup> shows there is a slight tendency for more profit-oriented MFIs to avoid targeting rural clients ( $q = 0.14$ ). However, they seem to offer similar average loan sizes ( $q = 0.04$ ), are slightly more inclined to target women borrowers, ( $q = 0.09$ ) and about as likely to emphasize poverty in their mission statements ( $q = 0.04$ ).

The usual arguments in favor of for-profit MFIs are:

- i. For-profit MFIs have lower number of risky loans
- ii. For-profit MFIs achieve greater operational efficiency
- iii. For-profit MFIs tend to be large in size (a study<sup>12</sup> shows the correlation between the profit-orientation index and the MFI size variable is 0.31 and its correlation with country population variable is 0.20. This indicates the ability of for-profit enterprises to scale their impact – and our aim with the bond is to impact over half a million women.)

As such, this has not been marked as one of the criteria for selecting the MFIs to be part of the WLB portfolio.

<sup>10</sup> <http://www.econ-jobs.com/research/35795-Microfinance--The-Impact-of-Nonprofit-and-For-Profit-Status-on-Financial-Performance-and-Outreach.pdf>

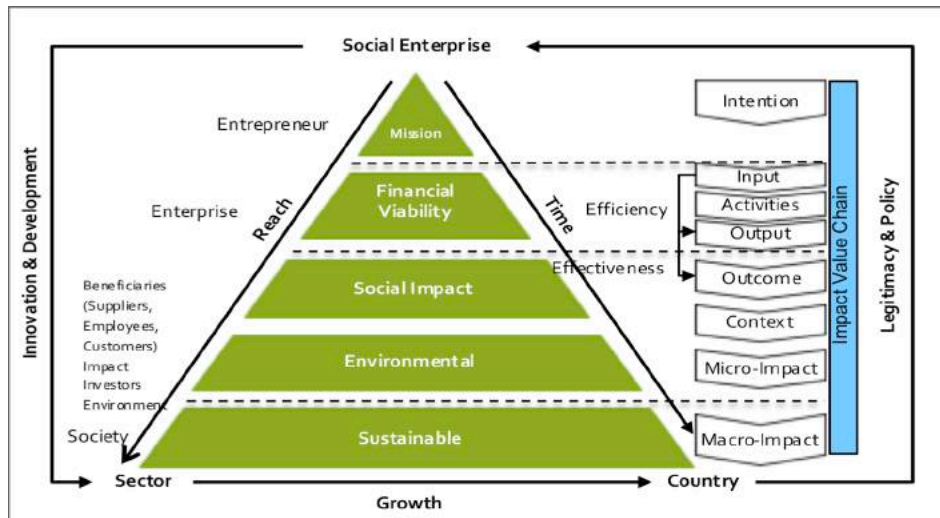
<sup>11</sup> [http://goizueta.emory.edu/faculty/socialenterprise/documents/profit\\_orientation\\_of\\_microfinance.pdf](http://goizueta.emory.edu/faculty/socialenterprise/documents/profit_orientation_of_microfinance.pdf)

<sup>12</sup> [http://goizueta.emory.edu/faculty/socialenterprise/documents/profit\\_orientation\\_of\\_microfinance.pdf](http://goizueta.emory.edu/faculty/socialenterprise/documents/profit_orientation_of_microfinance.pdf)



## CREATING AN IMPACT ASSESSMENT FRAMEWORK USING SHUJOG'S PROPRIETARY METHODOLOGY

The core of Shujog's work involves measuring and communicating the social and environmental impact of IEs and other inclusive organizations. Impact assessments entail a comprehensive, bottom-up evaluation that utilizes industry best practices and taxonomy to develop a Social Impact Framework and projections. These Impact Assessments follow Shujog's proprietary methodology, which incorporates industry tools such as the Impact Reporting and Investment Standards (IRIS) and the SROI (Social Return on Investment) calculations. This methodology marries impact creation with the financial health of the company and assesses outcomes based on the foundational framework of the Shujog Sustainability Pyramid [Figure 12]. The impact pyramid below applies a broad set of sector, country and mission specific indicators to assess the sustainability, scalability and impact of the portfolio of borrowers.



**FIGURE 12: SHUJOG'S SUSTAINABILITY PYRAMID**

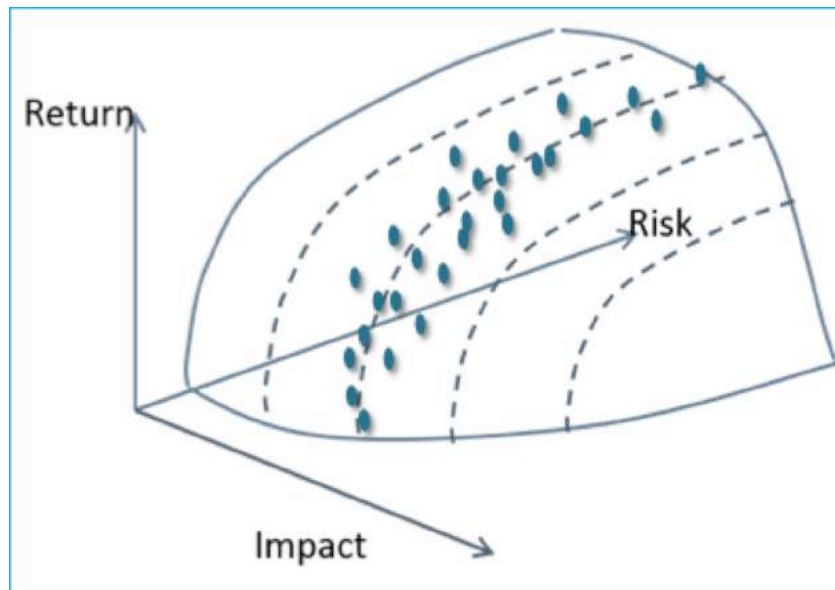
To evaluate the social performance of the bond, Shujog designed an overarching social impact measurement framework to: (a) clearly map out how the basket of entities achieve the expected social outcomes, (b) track the actual performance of the basket in empowering women, and (c) identify any deviations against targeted performance. On a conceptual level, the measurement also seeks to encourage maximum mission-alignment between the portfolio companies and the expected social outcomes of the WLB. This performance will be reported on a regular basis to investor and other stakeholders as part of the listing process.

Shujog conducted the impact assessments on two levels – first, at the entity-level by evaluating the performance of each portfolio company and second, at the bond-level by evaluating the overall pro-rated social performance of all portfolio companies in empowering women. Shujog assesses the performance of the portfolio and its individual entities vis-à-vis a stipulated set of outcomes and outputs, with the greatest emphasis placed on three overarching indicators: (a) the Social Return on Investment (SROI) generated, which tabulates the total net impact generated (monetized) per dollar of investment across the life of the bond, (b) the number and percentage of female beneficiaries, and (c) the number of households positively impacted.

## BOND STRUCTURING: PIPELINE DEVELOPMENT

### ANALYZING THE CORRELATION BETWEEN ASSESS RISK-RETURN-IMPACT TO OPTIMIZE THE PORTFOLIO

As part of the due diligence process for the ISB, the findings allowed IIX and Shujog to analyze the correlation between social impact and financial risk, and start to understand the optimal ways to adjust the equation. This correlation analysis based on the three-dimensional risk-return-impact framework will potentially lay the foundations for an eventual credit rating for high-impact entities – a significant step toward establishing a risk-return-impact approach toward evaluating impact assessments [Figure 13]. In particular, IIX and Shujog seek to identify how entities that have stronger social impact can mitigate future financial risk and long-term financial sustainability. More details on mitigating risks are outlined in Section 5 (Page 52).



**FIGURE 13: CORRELATION BETWEEN RISK-RETURN-IMPACT**

Additionally, portfolio optimization is governed by three overarching considerations of risk, return and impact (different from the traditional two-dimensional risk-return paradigm). MFIs lower risk of the portfolio but also demand a lower interest rate as compared to IEs. Thus, higher burden on MFIs reduces the coupon paid to investors and hence, the financial return that investors can expect. Similarly, IEs can have greater impact on women’s livelihoods through access to market but can only absorb a limited amount of capital as compared to MFIs, which are larger in size and have more regular, stable capital requirements due to the nature of their operations. Total amount lent to each entity is capped at ~25% of annual turnover to further reduce financial risk. The WLB portfolio has been carefully constructed based on the collective ability of underlying borrowers to balance risk, generate reasonable financial returns and create demonstrable social impact.

## PHASE 2: DUE DILIGENCE

### 4. PRELIMINARY QUESTIONNAIRES

The due diligence process is initiated by crafting a set of pre-due diligence questionnaires that are sent to potential underlying borrowers in advance. These questionnaires are a more in-depth version of the initial screening criteria and delve further into aspects that can either trigger financial instability or compromise the organization's social mission. For the WLB, IIX's in-house experts developed these questionnaires separately for MFIs and IEs.

### 5. SITE VISIT

The next step in the due diligence process is to synthesize the responses to the due diligence questions and identify any gaps in the information, potential discrepancies, or aspects that require verification. This is followed up by a site visit to the entities with the purpose of validating the information, addressing any red flags and identifying any nuances in the organization's operations, finances or impact strategy that would need special attention post bond issuance during the ongoing monitoring and evaluation process.

For the WLB, both IIX financial experts and Shujog impact experts were present during the due diligence field visits and separately analyzed the potential borrowers from a dual lens perspective before approving them for the portfolio. This process is guided by the initial risk-return-impact parameters that were established at the beginning of the process.

### 6. PORTFOLIO FINALIZATION

The last step in the pipeline development phase is the finalization of the basket. Based on the information collected during the site visit, the bond issuer will conduct a thorough review of the pre-selected basket to determine whether or not to go ahead with each of the borrowers. For the WLB, a Credit Committee approved the final portfolio of entities, allocation amount and lending rates.

An important factor to keep in mind is the number of entities that can realistically be included in the portfolio given the trade-off between risk and cost. The inclusion of more entities, sectors and geographies can significantly diversify part of the portfolio risk. However, at the same time this increases the ongoing M&E costs and consequently reduces the coupon rate that can be paid to investors.

Finalizing the basket mandates buy in from all stakeholders to ensure incentives are aligned and that trade-offs between risk-return-impact are adequately weighed. Reaching this final consensus involves coalescing all partners involved to opine on the selection and raise any concerns. For instance, the lead investment bank provides insight on market sentiment to assess whether they can sell the bond with the given weightage across countries and sectors; M&E experts quantify the net impact of the portfolio and give strategic advice on anticipated social outcomes that can be achieved by the basket of entities; and auditors do a final assessment on any potential final irregularities.

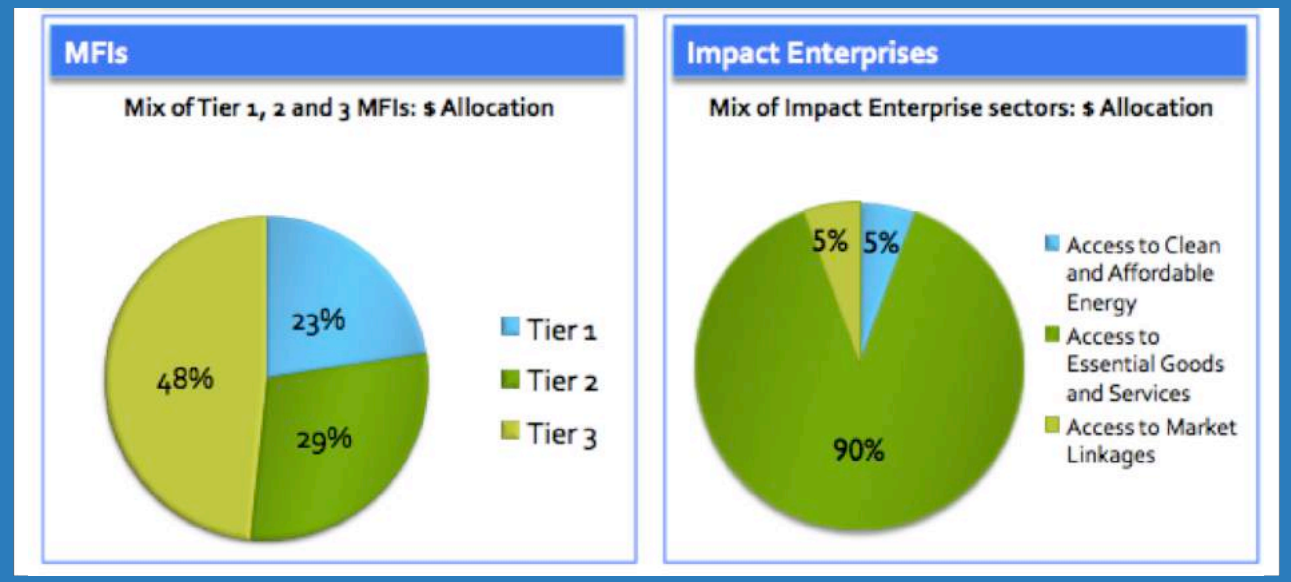


FIGURE 14: WLB PORTFOLIO BREAKDOWN

The tentative portfolio selected for the WLB is outlined above in Figure 14 (exact figures are subject to change). There is higher weightage on MFIs to ensure supply of capital is aligned with demand (the ability of the entity to absorb and deploy capital effectively). MFIs have longer track record, larger operations, stable capital requirements and regular repayment ability relative to IEs, which are less mature. However, IIX has included in the portfolio a greater concentration of Tier 2 and 3 MFIs, which have lower access to affordable financing. This is in line with the mission of the bond to mobilize capital for high impact entities that need funds to scale their operations, deepen their impact and sustain results over the long term. Once the basket has been finalized, the underlying borrowers are sent the loan agreements and term sheets drafted by the lawyers to duly sign and send back to IIX.





## Partnership Development

What makes ISBs distinctive is that they are focused on creating financial incentives for IEs to produce better outcomes. However, more broadly, they coalesce diverse stakeholders to overcome the wider set of barriers hindering the pace of social innovation. These barriers include a lack of holistic risk mitigation, measurement and evaluation that are either too expensive or lack depth, the inability of IEs to access the capital needed to scale impact and regulatory constraints that prevent traditional development players from investing in prevention.

IIX has followed a two-phased process for on-boarding key stakeholders as detailed below:

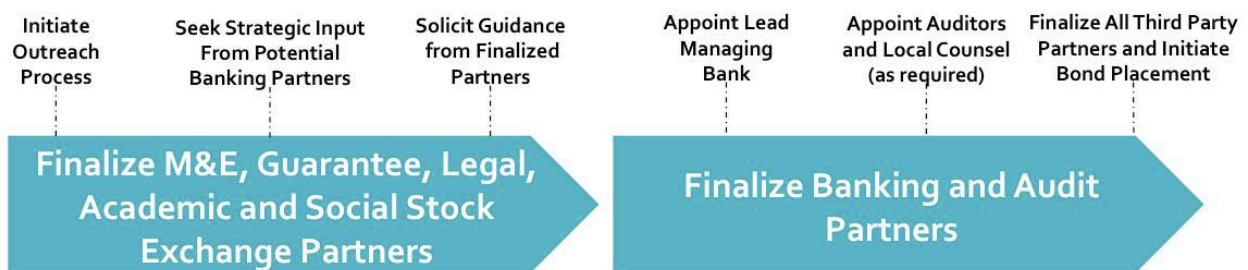
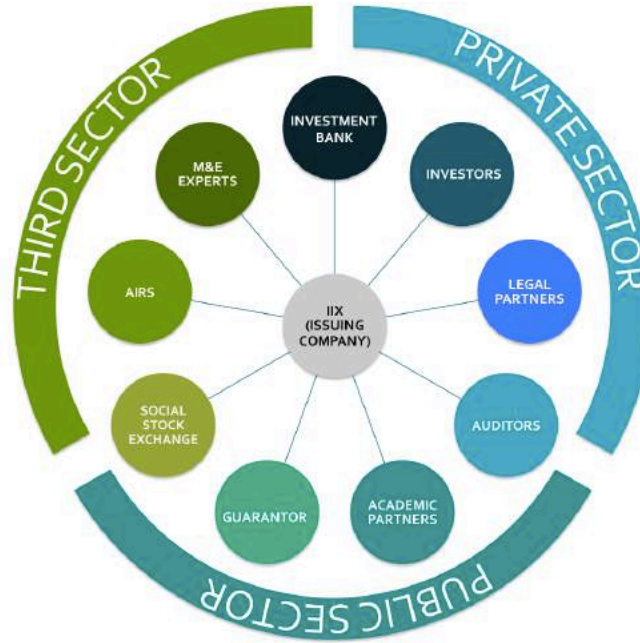


Figure 15 briefly outlines how diverse stakeholders play a role in developing the WLB and the sections below describe their role in detail.



**FIGURE 15: OVERVIEW OF KEY PARTNERS**

## INVESTMENT BANKS

Investment banks play an integral role in the bond issuance process, performing two key functions:

(i) **Providing strategic input during the structuring process:** After the bond issuer has appointed the investment bank and discussed with it the terms of the issue, the issuer then provides the bank a formal mandate letter (or term sheet). It helps set out the basic terms of the issue, based on the potential demand of the bond, and authorizes the bank as lead manager. The lead manager is responsible for arranging the bond issue and managing the entire issue process, advising the issuer on the structure and timing of the issue. It is imperative for the investment bankers to begin assisting the impact investing Intermediary well before the ISB is actually issued, taking into account the current investment climate and advising the bond issuer on how best to raise funds. The investment bank provides advice on the market and other factors that guide the bond structuring process as listed below:

- **Borrowers Origination:**
  - Providing inputs regarding client preferences on underlying borrowers
  - Advise on geographic diversification based on investor preferences
- **Product Structuring:**
  - Defining coupon rate and bond tenor in line with client requirements
  - Finalizing key documentation regarding investment terms

**(ii) Placing the bond with investors:** The second role of the Investment Banks is to serve as an intermediary between the bond issuer and the investors. The investment banks possess a broad investor network among which to sell the bond as well as the necessary licensing to deal in securities. Their involvement in the placement process is therefore critical.

A bank may commit only to use best efforts to sell the bonds or it may underwrite the whole bond issue, making a firm commitment to buy any bonds unsold to investors. Bonds can either be sold to the banks' clientele or bought directly by the bank by investing off their balance sheet.

### INVESTORS

Investors buy the ISB on the premise of regular coupon payments during the tenor of the bond and return of the principal amount invested upon maturity of the bond. Investors also are promised a certain amount of social return, although bond payments are not linked to the same. ISBs are designed to unlock capital at scale from the private sector and direct it towards development issues. Thus, the target bondholders are investors who are interested in creating impact over and above financial returns.

For the WLB, the investors that the bank will be targeting are limited to accredited investors and institutions. The banks will target those investors that are keen to participate in the impact investing market, and still receive a reasonable rate of returns relative to the risk they bear.

It is also important to consider the geographic location of investors to ensure compliance with necessary country-level regulatory procedures. This will impact the costs involved in issuing the Bond, associated reporting requirements and, consequently, may put pressure on the amount of coupon that will be paid to investors.

There is potential for subsequent ISBs to be issued to retail investors once the WLB sets precedent and acts as a litmus test for investor preferences as well as regulatory constraints. Issuing ISBs to retail investors will act as the final frontier for truly democratizing capital markets and bringing the impact investment space from the margins to the mainstream. However, being the first of its kind, the WLB will be sold only to accredited investors, who typically have lower regulatory restrictions and larger risk appetite. For the Women's Livelihood Bond, target geographies for investors are likely to include Hong Kong, Singapore and the United Kingdom.

## LEGAL PARTNERS

The legal partners assisting in the process provide counsel to the bond issuer on the legal aspects of the structuring, placement and listing of the Bond. This includes drafting term sheets, ensuring alignment with international and local regulations, and facilitating the listing process. The bond counsel collaborates with the issuer, the impact investment intermediary (IIX), and the investment bank in structuring the transaction. For the WLB, Shearman & Sterling, Hogan Lovells and TSMP Law Corporation are the legal firms that are providing *pro-bono* support for the process.

## AUDITORS

Auditors would assist in preparing and reviewing the financial information included in the offering circular. They would also issue a comfort letter to the issuer and the lead arrangers. The comfort letter is an integral part of the due diligence process and declares that there are no indications of false or misleading information in the financial statements and that the offering circular follows the prevailing accounting standards. Given that there are multiple borrowers under the WLB, each of the borrowers' auditors is involved in reviewing and issuing a comfort letter for the transaction.

## ACADEMIC PARTNERS

Academic partners play an essential role in educating interested parties on the benefits, opportunities and challenges of structuring mission-focused bonds. Knowledge sharing and management is a critical component for IIX and Shujog considering the WLB is the first security in the ISB series and has the potential to open up the floodgates of private capital for development. For the WLB, IIX is in discussions with Duke University, New York University, University of Oxford and University of Pennsylvania.

## GUARANTOR

The guarantor play a key role in mitigating risk of the instrument and provide investors with a certain degree of comfort. The guarantor can be a donor, a government or even a foundation that is interested in achieving a certain developmental outcome in a scalable and sustainable way. By providing a guarantee, these traditional development players are able to use their funds to leverage a much larger amount of capital from private sector investors, given the extra layer of security to investors.

The presence of a guarantee from a credible third party can induce investors to accept a lower coupon rate on the bonds. The third-party guarantor receives a fee for incurring the risk that comes with guaranteeing the debt should any of the borrowers default. The guarantors need not guarantee the entire amount of the ISB. IIX is in advanced discussions with USAID to provide a 50% *pari passu* guarantee for the bond.



## SOCIAL STOCK EXCHANGE

Initially, the WLB will be listed on Impact DEM. Strategically located in Mauritius, Impact DEM is operated by the Stock Exchange of Mauritius and is regulated by the Financial Services Commission, Mauritius. Upon reaching critical mass, the WLB and other ISBs (or other innovative financial instruments that create dual social and financial returns) will be migrated to Impact Exchange, which is the world's first dedicated board of an established, regulated stock exchange devoted solely to listing securities issued by impact entities. It provides a unique opportunity for impact entities to raise funds that will allow them to scale and deepen their social and/or environmental impact. Impact Exchange allows both the general public and professional impact investors the opportunity to invest in and trade securities issued by impact entities which reflect these investors' own values. Impact Exchange provides all the same advantages as any other global public trading platform – transparency, efficiency and liquidity – while also ensuring that the social and/or environmental mission and impact of the issuers are both safeguarded and showcased. In addition to the usual listing requirements, Impact Exchange requires that all issuers demonstrate positive social and/or environmental impact, and IIX provides oversight of these impact requirements. Shujog will provide ongoing social reporting even while the bond is listed on Impact DEM.

## AUTHORIZED IMPACT REPRESENTATIVES

Issuers must satisfy impact reporting requirements in order to list, and remain listed, on Impact Exchange. Each issuer must appoint an Authorized Impact Representative (AIR) to support it through the listing process and ensure compliance with its listing requirements (a Nominated Impact Advisor) as well as to verify impact reports at the end of each financial year (an Impact Verification Agent). All AIRs, including both Nominated Impact Advisors (NIA) and Impact Verification Agents (IVA) are social advisors who must be accredited and registered with the SEM. The assistance of the AIRs is intended to ease the listing process for impact entities and to bolster investor confidence – through independent verification of the social and environmental impact of the issuer. For the WLB, Shujog will act as the AIR. Shujog is a listed AIR on SEM.

## MEASUREMENT AND EVALUATION EXPERTS

Measurement and Evaluation (M&E) experts have two key objectives as partners:

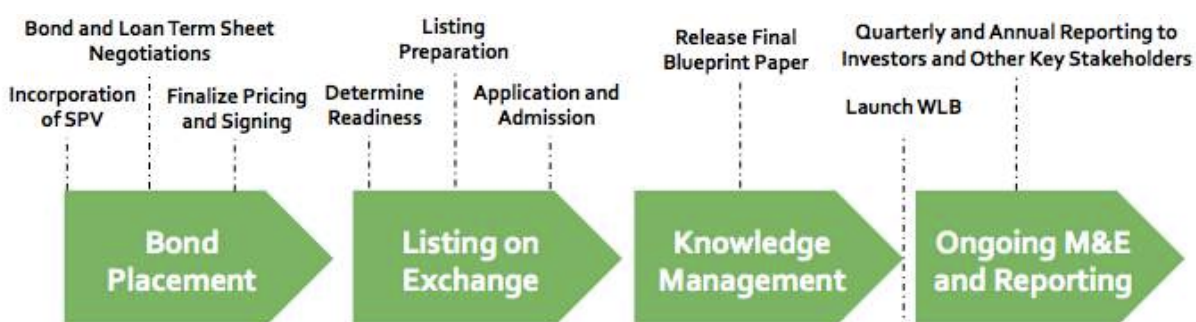
- Ensuring the ISB has a strong focus on impact and achieving target social outcomes
- Ensuring social risk of the underlying borrowers is adequately mitigated

These objectives are achieved by conducting preliminary impact assessment on the portfolio of borrowers during the pipeline development process and by conducting an ongoing impact assessment drill during the life of the bond to take preemptive measures to identify and mitigate risk of mission drift. This mandates the partners have expertise in articulating theory of change, data collection, quantification of social outcomes, calculation of Social Return on Investment (SROI) and impact reporting. Shujog is the M&E partner for the WLB and has been involved through the entire bond structuring process, leveraging its expertise in quantifying social outcomes; to ensure over half a million women and an estimated two million lives in total are impacted by the operations of the portfolio of IEs and MFIs that form part of the bond portfolio.



## Bond Issuance

To date, IIX has made significant progress on developing the WLB. The final phase of work to be initiated is the actual bond issuance. This phase includes the placement of the bond and listing on the Stock Exchange of Mauritius, as well as ongoing monitoring and evaluation (M&E) throughout the term of the bond as detailed in the following section:



## BOND PLACEMENT

Following the due diligence process and the final selection of companies, IIX is working in tandem with selected investment banking partners to define a capital raising approach and market the bond to a broad base of global investors.

IIX's banking partners will take ownership of selling the bond to accredited investors and institutions in their networks. This also mandates developing the market and educating the investors about both the impact investing space and the dual social and financial benefits of the WLB.

Key tasks that investment banks perform to facilitate and execute bond placement are outlined below:

- **Market Development:**
  - Host a series of training workshops to address the current knowledge gap
  - Target investors or bank clients that would be interested in learning about the impact investing space and the WLB
- **Selling the Bond:**
  - Active investor outreach
  - Lead working group on capital raise
  - Deal closing and signing of subscription agreements

## BOND LISTING

As the final step in the bond structuring process, the WLB will be listed on the Stock Exchange of Mauritius's Impact DEM platform. There are three stages in the bond listing process:

- Listing Preparation
- Listing Application and Admission
- Post-Listing

The following section provides an overview of these three stages

### **STAGE 1: LISTING PREPARATION**

In the first stage, IIX will appoint and consult with legal and administrative advisors in order to meet the preparatory requirements for listing. This stage encompasses all internal preparations, including reviewing of financial documents (tax structures, due diligence), assembling social impact reports and certifications, and compiling legal, financial and impact due diligence documents. In accordance with

Impact DEM regulations, IIX will work with legal partners to draft the necessary listing documents and provide support during the application process. The listing preparation process will build on the work required for bond placement.

### STAGE 2: LISTING APPLICATION AND ADMISSION

At this stage, IIX will submit the finalized listing circular for the WLB to Stock Exchange of Mauritius as part of an official application for bond listing. On receiving conditional approval from the Listing Executive Committee (LEC), IIX will register the final Listing Document with the Financial Services Commission, Mauritius. Once the bond receives final approval from the LEC for admission to Impact DEM, the WLB will be admitted to listing and available for trading.

### STAGE 3: POST LISTING

Once the bond is listed on Stock Exchange of Mauritius, the SPV will disburse the loans to the underlying borrowers, which will use the proceeds to scale their organizations. Operating as a listed entity brings with it increased obligations. Stock Exchange of Mauritius sets out requirements – such as periodic disclosures – that must be met by listed entities in order to maintain their status. This ongoing monitoring and evaluation throughout the life of the bond will ensure continuous risk mitigation and a focus on measuring and demonstrating social outcomes achieved.

## MONITORING AND EVALUATION

Entities listed on Stock Exchange of Mauritius have a general obligation to disclose performance information on a continuous basis. In particular, listed entities should immediately release to the market any information which a reasonable person would expect to have a material effect on the price or value of its listed securities.

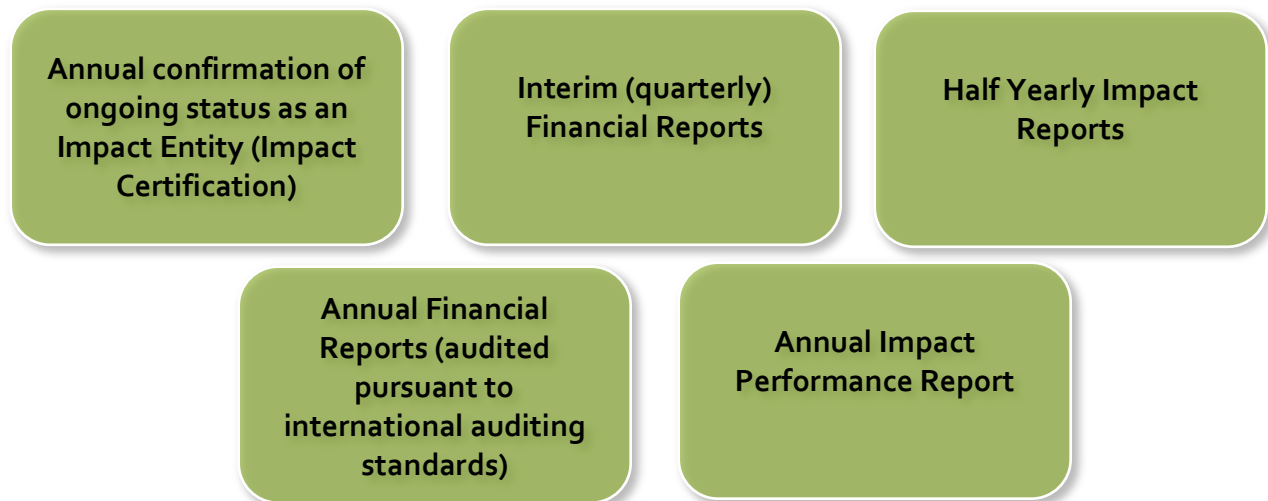
The due diligence will be further strengthened by a strict ongoing M&E process to ensure both the above objectives – impact creation and financial stability – are met. Investing in strong monitoring and evaluation procedures will ensure three key outcomes:

- **Improved Transparency:** IIX will be able to track and assess borrower performance and share accurate results and frequent progress updates with investors and partners.
- **Demonstrable Social Impact:** The WLB will set a precedent for similar instruments to be created that effectively mobilize private sector capital to invest in change, with a focus on gender-based outcomes. It is crucial that the impact on women is quantified, analyzed and shared with stakeholders to benchmark performance and provide opportunities to structure similar instruments in future.
- **Mitigated Financial Risks:** The M&E process will, as outlined above, play a key role in mitigating financial risks both by taking preemptive action when required and providing data collection opportunity – the results will be used to analyze the correlation between social impact created by



borrowers and corresponding financial risk that was reduced. Findings from this analysis can be potentially game-changing and capable of unlocking large-scale capital for entities that seek a double bottom line.

In addition, IIX and Shujog will prepare and submit certain reports at regular intervals as detailed below:



### FINANCIAL PERFORMANCE MONITORED AND REPORTED BY IIX

IIX will conduct monitoring and evaluation of the financial performance of the underlying borrowers. The Capital Markets Director will lead program management oversight and facilitate communication, monitoring, evaluation and real-time learning. IIX will monitor the entities that are part of the WLB portfolio and prepare reports for the SPV to release to the Exchange on a regular basis.

### IMPACT-RELATED PERFORMANCE MONITORED AND REPORTED BY SHUJOG

Shujog's expertise in conducting impact assessments will be leveraged to provide monitoring and evaluation services, to determine the impact delivered by the WLB. For evaluation of activities and collection of output and outcome indicators, Shujog will build on the respective impact assessments conducted for the IEs, using the data collected during these enterprise-level assessments for the establishment of a baseline. This will include understanding the expansion in the number of beneficiaries, growth in business size and use of impact investment for the designated purpose.

## KNOWLEDGE MANAGEMENT

The overarching aim of the WLB project is to create a series of ISBs that effectively mobilize private sector capital to address development challenges. As the WLB is designed to be a replicable model, IIX will monitor project deliverables from this first bond to identify best practices plus risk mitigation strategies; and translate the same into organizational learning for future bond issuances. This information will be shared in two ways:

- (i) Via this initial Blueprint Paper and, subsequently, via the Final Blueprint Paper that will be published post bond issuance. These papers will be submitted to the Rockefeller Foundation and made publicly available.
- (ii) Via other public platforms for which IIX has developed a structured knowledge management approach to share learnings and outcomes of the WLB project with external parties as described below:
  - **Clinton Global Initiative (CGI)**: CGI convenes global leaders to create and implement innovative solutions to the world's most pressing challenges. Because CGI has worked with thousands of organizations since it was founded in 2005, CGI has an unrivaled ability to connect members engaged in similar work through one-on-one introductions, large events, and focused networking opportunities. The robust and active CGI community allows members to share best practices, forge partnerships, and leverage resources to effect measurable change. As a member of CGI, IIX will be able to share key lessons learnt with a variety of different stakeholders – NGOs, donors, foundations, corporate sustainability programs, Impact Enterprises – who are also part of the CGI community and would be interested in learning more about the bond.
  - **Impact Academy**: Impact Academy is a joint product of IIX and Shujog, which has contributed significantly towards broadening knowledge about the emerging paradigm of impact investing. These two entities have conducted over **60 Impact Academies and Impact Chats** across South-East Asia, exposing **300,000 individuals** to the IE landscape and introducing over **26,000 professionals** to the impact investing ecosystem through education and training. IIX will use this as a platform to connect with interested external parties – impact investing professionals, traditional investors, M&E experts, HNIs, private bank relationship managers, social entrepreneurs and NGOs – to share key learnings, showcase outcomes achieved and debate alternative approaches to overcome challenges faced while structuring and implementing the WLB.
  - **Academic Partners**: IIX's academic partners will be engaged to do independent reports and case studies on the WLB that will be a key part of the WLB's knowledge management strategy.
  - **Online Engagement – Webinars, Impact Quarterly and IIX official website**: Additionally, IIX will also host frequent webinars during the life of the project open to the general public, to discuss the program's progress and solicit opinions. The organization's quarterly online newsletter, Impact Investing Newsletter, with a readership of +30,000, will be an additional platform that will feature program results. There will be a progress report specifically on the program's impact, developed by IIX's impact assessment partners Shujog, that will be made available on IIX's official website.

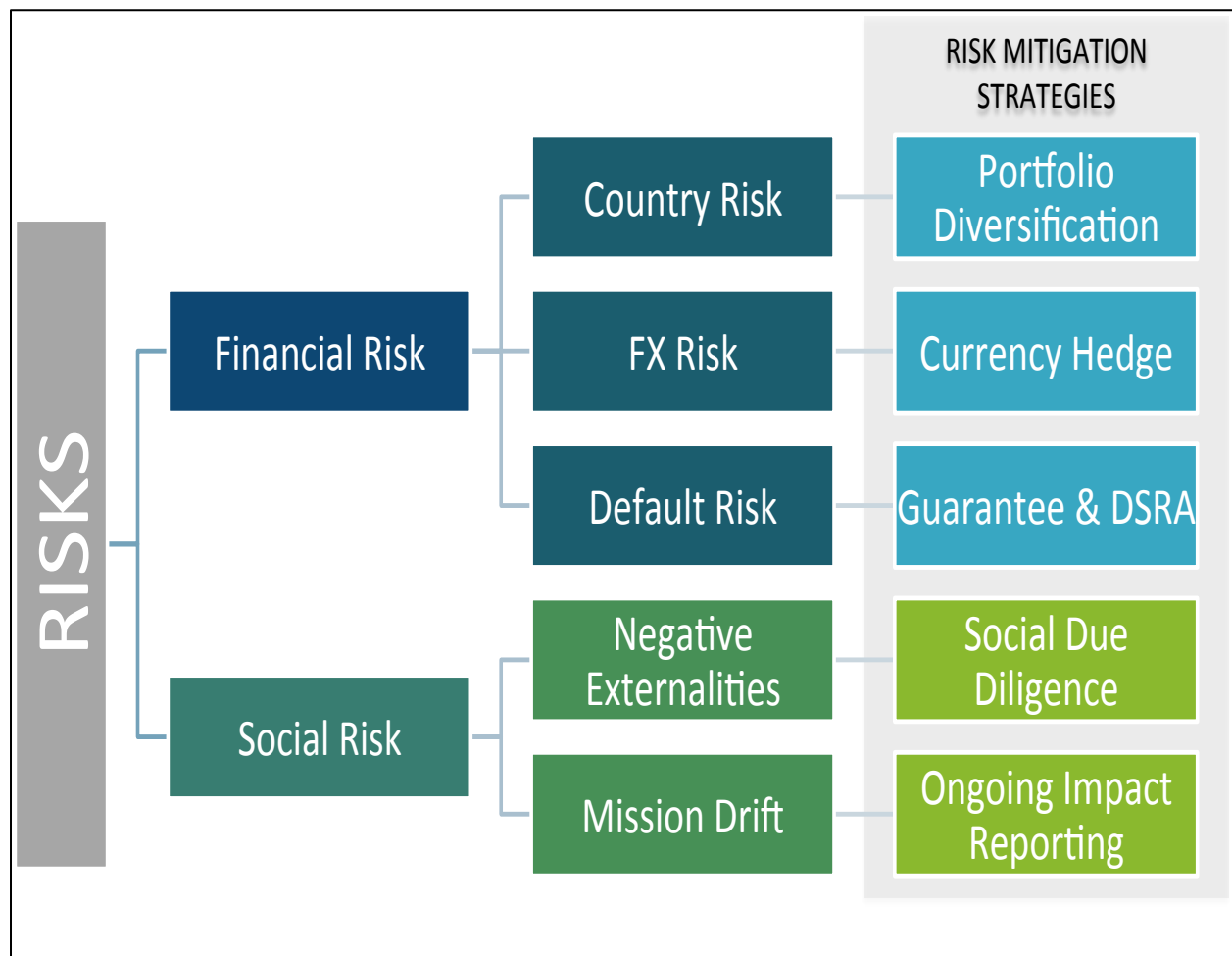


## SECTION 4: RISKS



## Anticipated Risks

IIX views risk through the dual lens of financial and social risk [Figure 16]. The purpose of this section is to outline anticipated risks for the WLB that IIX has identified and taken preemptive steps to mitigate during the process of structuring the WLB.



**FIGURE 16: ANTICIPATED RISKS AND PROPOSED RISK MITIGATION STRATEGIES**

### FINANCIAL RISKS

There are three key financial risks identified by IIX:

- **Country Risk:** Country risk refers to the risk of investing or lending in a country, arising from possible changes (1) in the business environment that may adversely affect operating profits or the value of assets in the country; or (2) the regulatory environment which may adversely affect the ability of entities operating in the country to make payments and interest to foreign lenders.



**RISK MITIGATION STRATEGY:** IIX assessed country risk of each of the countries in which potential borrowers operate, based on the credit rating of the countries (shown in the table below), which follows quantitative econometric models and financial analysis as well as qualitative methods and policy analysis.

COUNTRY	Moody's	Standard & Poor's	Fitch	COFACE Country Risk
Cambodia	B2 / Stable	N/A	N/A	C
Indonesia	Baa3 / Stable	BB+ / Positive	BBB- / Stable	A4
Philippines	Baa2 / Stable	BBB / Stable	BBB- / Positive	A4
Vietnam	B1 / Stable	BB- / Stable	BB- / Stable	B

- FX Risk:** The WLB is a US Dollar-denominated bond. The majority of loans to the underlying borrowers will be denominated in US dollars to match this. However, ~10% of the total amount is tentatively allocated towards an Indonesian entity and may be lent out in Indonesian Rupiah (IDR). As a consequence, investors could be exposed to risk that stems from potential changes in the valuation of IDR. These fluctuations may result from the unpredictable gains and losses incurred when repayment of interest and principal received from the Indonesian entities are converted from the IDR to USD.

**RISK MITIGATION STRATEGY:** To mitigate currency risk, the bond issuer intends to enter into a hedge transaction to neutralize the effect of the fluctuations in the IDR:USD exchange rate. In this case, the borrower bears the cost of risk mitigation.

- Bad Debts:** The third financial risk investors are exposed to is payment default by the underlying borrowers. This refers to potential deficiency arising on account of failure to make repayment by IEs and MFIs that are part of the WLB portfolio. A default indicates the borrower may be in financial trouble and thus cannot fulfill the agreed upon debt obligations.

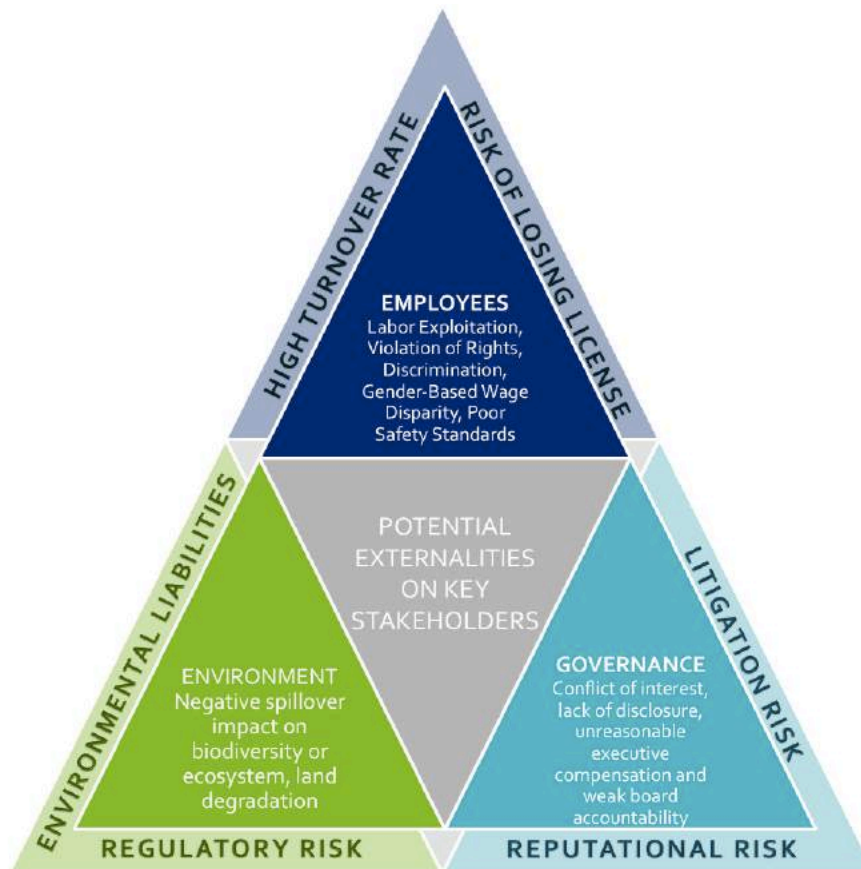
**RISK MITIGATION STRATEGY:** To mitigate the default risks, IIX performed extensive financial due diligence on the proposed borrowers in addition to providing the guarantee and DSRA to cover a portion of the potential losses.

## SOCIAL RISKS

The potential social risks identified and addressed by IIX and Shujog are outlined below:

- Negative Externalities:** While projecting the positive impact of underlying borrowers, it is critical for the bond issuer and the M&E partner to be cognizant of the potential spillover effect operations may have on the surrounding environment or community that may cause negative impact or externalities. These externalities must be preempted, mitigated or removed all together.

Although the by-products of an entity's activities vary on a case-by-case basis based on key stakeholders [Figure 17], potential risks relevant to the WLB portfolio are outlined below:



**FIGURE 17: EXTERNALITIES FACED BY STAKEHOLDER TRIAD**

- **Employees:** Potential issues that employees may be subjected to include exploitative labor practices that are often heightened by asymmetric power relationships and are highly prevalent in developing countries. The moral framing of exploitation extends to violation of human rights, gender-based wage discrimination and non-conducive working conditions that pose safety or health risks. Although these practices are against the mission of IEs, latent or hidden challenges must be preempted and addressed by rigorously assessing not just the direct workers and employees but also across the supply chain.

There is a strong business case for addressing these issues early using a proactive and preventative strategy. In the immediate term, the company will be affected by high turnover that negatively impacts productivity; in the medium term the entity may run into issues with local authorities, face push-back from the local community (thereby losing potential employee base) and result in loss of license to operate, if reformative measures are not taken; and in the long term, the cumulative impact of these externalities can put financial stability of the entity at risk.

- **Environment:** Entities that have high reliance on natural resources, dangerous by-products and inefficiently manage their usage of energy and water supply, can have spillover effects on the surrounding ecosystem. On a global level, this heightens the risks of issues such as climate change; and at a local level this could impact land-degradation and natural habitat loss. Both issues have long term trickle down effects on the community and can result in environmental liabilities and regulatory risks that could have high cost implications on the organization.

Additionally, unsustainable practices present a lost opportunity in terms of cost saving on energy and other natural resources. This makes it imperative for the due diligence team to critically assess IEs that are part of the ISB on spillover aspects that are not immediately obvious but could pose serious long term financial and social risks that could jeopardize future operational efficiency and stability.

- **Corporate Governance:** The internal management team of any entity does not operate in isolation – the entrepreneur/founder, executive management and board of directors are accountable to other stakeholder groups besides shareholders. This includes beneficiaries/customers, employees and the broader supply chain, the local community and the environment. Transparency in management and reporting, and a strong code of ethics to guide internal policies and governance are essential tenants that must be assessed to avoid conflict of interest, poor disclosure of material information, unreasonable executive compensation levels and weak board accountability.

Besides obvious litigation risks that could arise from discrepancies in corporate governance, there is also a reputational risk that the brand faces – both factors that could cost the organization massive financial losses. Although this has low probability for most impact entities, the high cost involved in case an issue arises mandates a rigorous focus on pre-identifying and addressing these risks.

**RISK MITIGATION STRATEGY:** The key risk mitigation measure for the above is the rigorous social due diligence performed by Shujog and ongoing reporting done to ensure transparency of impact results to all stakeholders involved in the WLB.

- **Mission Drift:** The inherent challenge of operating an Impact Enterprise is managing the dual objectives of generating both financial and social returns. This often translates to conflict between decisions and actions thereby mandating calculated trade-offs. For instance, the situation may demand forsaking social impact in order to capture market share or improve profit margins; or conversely, expanding the scope of positive outcomes on target beneficiaries at a financial cost. Problems occur when an entity's efforts to meet its financial goals start taking precedence over its social mandate, threatening to swing the pendulum too far in the other direction. Although market-based solutions are essential to ensure sustainability, the feared result of this mission drift is that the organization will lose focus and stray too far into the commercial realm, compromising its social mission.

It is critical to set parameters on 'how far is too far' on the mission-money spectrum. MFIs accomplish this by quantifying loan sizes, duration of client relationships and fixing interest rates before arriving at a model that is financially viable and at the same time, well positioned to create scalable impact. IIX recognizes the need for vigilance of these parameters at a portfolio level and a clear understanding of purpose and priorities at an individual borrower level. This requires strong market discipline, an equally strict sense of ethics and integrity, along with a leadership consensus on limits of factors that dictate 'how far is too far' in any direction.

**RISK MITIGATION STRATEGY:** The key risk mitigation measure, apart from the social due diligence, is ongoing monitoring and reporting of social performance that will be done by Shujog to further enhance transparency and encourage the IE to remain on track to achieve the intended mission.





Since the inception of the WLB project, IIX has already taken several positive strides in developing it from a concept into a reality. Progress to date has been briefly summarized below:

- **Product Development:** IIX's capital markets team and Shujog's impact assessments team have designed a robust mechanism that effectively introduces the new dimension of IMPACT into the traditional risk-return paradigm which forms the basis of commercial investment products. At the same time, the WLB is a high-yield bond with a sustainable model, generating its own cash flow streams to support expenses. Finally, the WLB is designed to provide impact investors who buy the bond with an attractive coupon rate, which will amount to returns between 6% and 7%.
- **Pipeline Development:** The WLB will lend capital at an affordable rate to underlying borrowers – Impact Enterprises (IEs) and Microfinance Institutions (MFIs) that are financially stable and making visible impacts on the lives of women across South-East Asia. IIX has finalized the basket of entities and created a multi-sector, multi-country bond with an inbuilt risk mitigation mechanism that is well positioned to impact the lives of over half a million women by empowering them to transition from subsistence to sustainable livelihoods and an estimated two million lives in total.
- **Partnership Development:** IIX's partners have played a pivotal role in accelerating the bond development process. The Clinton Global Initiative provided a global platform for IIX to launch the bond and build momentum; Rockefeller Foundation and Japan Research Institute provided upfront support to develop the mechanism and build a robust portfolio; Shearman & Sterling and Hogan Lovells have provided *pro-bono* legal services to ensure the instrument is in compliance with local and regional regulations; and Shujog has played an instrumental role in quantifying the social impact and highlighting potential outcomes of the portfolio.

Before the bond is issued, a final version of this Blueprint Paper will be released that will list more details about the final phases of the bond, including the role of the banking partners in marketing the bond to accredited investors and that of the Stock Exchange of Mauritius in listing the WLB. IIX and Shujog hope this paper will serve as a blueprint to open the floodgates of private capital that is earmarked for creating large-scale impact; it could also be a catalyst in the impact investing space in Asia by bringing in new private sector players and using the power of capital markets to transform the lives of women across the region.

