CONCESSIONAL CAPITAL FOR AGRI-SME FUNDS:

Donor & Investor Guidance Document

MARCH 2025

Photo credit: Jan Kopriva

ISF

ACKNOWLEDGMENTS

This report was authored by ISF Advisors, which included Dan Zook, Craig Courtney, Ana Raviña Eirín, Matthew Newman, and Mathilde Jacquemin.

Key findings of this study were discussed with a dedicated Advisory Committee of external experts including Global Donor Platform for Rural Development (Songbae Lee), Aceli Africa (Brian Milder), Convergence (Safia Gulamani), Collaborative for Frontier Finance (Drew von Glahn) and Catalytic Capital Consortium (Harvey Koh). Thanks also to Heidi Sumser and Hans Muzoora.

Recommended citation

ISF Advisors. Concessional Capital for Agri-SME Funds: Donor & Investor Guidance Document. 2025

TABLE OF CONTENTS

ACRONYMS

AuM	Assets under Management
C3	Catalytic Capital Consortium
CSAF	Council on Smallholder Agriculture Finance
DFI	Development Finance Institution
EA	East Africa
FASA	Financing Agricultural Small-and-Medium Enterprises in Africa
FI	Financial Institutions
FM	Fund Manager
FX	Foreign Exchange
GAIN	Global Alliance for Improved Nutrition
GCF	Green Climate Fund
GDPRD	Global Donor Platform for Rural Development
IRR	Internal Rate of Return
LatAm	Latin America
LDC	Least Developed Country
MEL	Monitoring, Evaluation, and Learnings
MFI	Micro Finance Institutions
NPL	Non-performing Loan
PSD	Private Sector Development
SHF	Smallholder Farmers
SME	Small and Medium Enterprise
SSA	Sub-Saharan Africa
TA	Technical Assistance

EXECUTIVE SUMMARY

ISF Advisors' research highlights a $74.5 billion financing gap for agricultural small and medium enterprises (agri-SMEs) in Sub-Saharan Africa[1]. Agri-SME investment funds are well positioned to help close this gap but often rely heavily on concessional capital, primarily deployed by bilateral agencies, foundations, and Development Finance Institutions (DFIs). **Current approaches to allocating concessional capital lack transparency, hindering the effective optimization of subsidies.**

To address these challenges, ISF Advisors developed an evidence-based report outlining considerations and trade-offs concessional investors face when supporting agri-SME investment funds, with an emphasis on "first-loss" capital. ISF Advisors conducted a literature review, analyzed data from 18 funds active in Sub-Saharan Africa, and interviewed fund managers and investors.

The report finds that the amount of concessional capital in the capital stack has generally been determined based on the risk tolerance of senior investors. In practice, concessional capital is mainly used to reduce senior investors' risk and enhance returns, rather than to pass along some benefits to the underlying investee (i.e., more patient capital, lower collateral requirements). First-loss tranches are sized to cover expected losses and protect against some degree of uncertainty, often with investors pricing in worse-case scenarios rather than just historical or expected loss rates. **This often results in senior investor protections that exceed estimates of portfolio losses by ~15-20x.** The study also confirms that investors often provide concessionality by forgoing risk-adjusted financial returns, rather than through increased risk-taking. High-risk or loss-tolerant capital is hard to raise and is mostly provided by bilateral donors and philanthropies.

The analysis also reveals the critical role of anchor investors in providing high-risk capital early on in the fundraising process. A concessional anchor commitment helps attract other investors due to an improved risk/return profile and because it helps align investment and impact strategies. This report lays out risk mitigation levers used to manage the exposure to high-risk investments, namely intermediation strategies, diversification away from primary production, and blending debt and equity to cover downside or create upside. Technical assistance funding can also be used towards mitigating risk and improving returns; however, along with design grants, it is hard to attract and often takes a backseat during fundraising.

While capital mobilization is often seen as a key success measure in blended finance, concessionality should only be justified if it leads to impact generation. The report explores how concessional investors (e.g., donors, foundations, DFIs) balance the trade-offs between the risk/return profile of an investment and its impact generation potential.

[1] ISF Advisors. "The State of the Agri-SME Sector - Bridging the Finance Gap." FCDO, USAID, March 2022.

These investors typically consider several dimensions: their own value add in a transaction, the pathway to financial sustainability, and the depth and pace of the impact generated. When it comes to agri-SME finance, investment risk is normally at odds with the depth and pace of impact generation; investors need to position themselves on the risk/impact investment continuum accordingly.

Data-driven capital allocation is essential to improving the efficiency of subsidies. Concessional capital helps address market failures and foster new investment vehicles and, importantly, creates the opportunity for public good through shared learning: fund managers benefiting from public capital should be required to contribute to a learning agenda and follow certain transparency requirements.

Performing ex-post evaluations on financial and impact performance and on the actual use of concessional capital in agri-SME funds would help improve understanding of different investment strategies and reduce perceived risk. However, this requires collaboration among investors and fund managers to establish standards and practices on data collection and analysis, something the Agri-SME Learning Collective is currently articulating, and as demonstrated by successful data-sharing initiatives led by the Council on Smallholder Agriculture Finance (CSAF) and Aceli Africa.

Finally, technical assistance, design grants, and post-investment support, when better coordinated and integrated with the provision of investment capital, can be leveraged by fund managers to achieve improved investment outcomes.

1. INTRODUCTION

Small and medium-sized agricultural enterprises (Agri-SMEs) play a vital role in food systems in developing countries and link the farm sector (particularly smallholder farmers) with the final consumer by providing inputs, training, processing, credit, marketing, distribution, and other products and services. However, agri-SMEs are notoriously under-financed. ISF Advisors' research estimates that there is an approximately $74.5 billion gap between the existing supply and demand for finance for agri-SMEs in Sub-Saharan Africa[2]. Multiple financing channels are at stake when it comes to financing agri-businesses, such as banks, MFIs, or investment funds.

The financing gap for agri-SMEs, compounded by the inherent and perceived risks of agriculture in emerging markets, requires the strategic use of concessionality to attract capital. Specifically, subsidy must be efficiently used to address information asymmetries (e.g., through baseline data and learning agendas), mitigate risk, and enhance fund economics, thereby helping mobilize capital and bridge the financing gap.

This document aims to unpack the use of concessional capital by investment funds and investors in the agri-SME financing sector by looking at strategies and structures used by recent blended agri-SME investment funds.

Concessional capital is a form of financial support aimed at incentivizing projects featuring a strong social or environmental impact that may not otherwise be commercially viable, by providing financial instruments (grants, debt, equity, guarantees, and others) at below-market rates. It is typically provided to high-impact areas (climate resilience, economic development) by development banks, governments, or multilateral organizations, aiming to de-risk investments and attract additional private sector funding in high-impact projects. As outlined in the DFI Enhanced Blended Concessional Finance Principles[3], concessionality is justified when in alignment with five key principles:

1. **Contribution is beyond what is available on the market**
2. **Maximum impact for the minimum level of subsidies**
3. **Impact is sustainable and does not compromise commercial viability**
4. **Concessionality addresses market failures while avoiding market distortion**
5. **Concessional funding follows high operating standards**

[2] ISF Advisors. "The State of the Agri-SME Sector - Bridging the Finance Gap." FCDO, USAID, March 2022.

[3] Part of the DFI Working Group on Enhanced Blended Concessional Finance for Private Sector Projects, led by the IFC (more details on IFC website)

Concessional capital is an essential tool to support impact-driven enterprises, organizations, and financial intermediaries, that lack access to capital through the conventional marketplace. While concessional capital is crucial in addressing the financing challenges of agri-SMEs, its allocation generally lacks transparency and standard metrics in blended finance transactions. These gaps make it challenging to quantify the impact of concessionality, and therefore to determine the optimal level of concessionality needed to reach each impact target. Standardized guidelines and methodologies, such as those being established by the Agri-SME Learning Collective, would enable a more efficient practice in assessing, prioritizing, and measuring investments in agriculture-focused investment funds.

2. PURPOSE AND INTENDED AUDIENCE

This document provides concessional investors - such as donors, bilateral agencies, private foundations, family offices, and Development Finance Institutions (DFIs) - guidance on effectively deploying concessional capital into agriculture-focused investment funds, particularly regarding first-loss capital. To note, concessional investors often have a different tolerance for risk, with DFIs generally pursuing more commercial, lower-risk mandates than bilateral agencies, for example. However, these stakeholders often invest alongside each other in blended structures, making the guidance in this document important for improving coordination and adding to the dialogue around the efficient use of subsidy.

This guide outlines the considerations and trade-offs emerging from investing concessional capital into these investment vehicles. Concessional investors can use this report to inform how to balance those trade-offs when evaluating and prioritizing fund investments and setting appropriate impact objectives. While this report is grounded in evidence, the ability to collect data on the deployment of concessional capital remains limited. As such, this report serves as a starting point for understanding the trade-offs associated with deploying concessional capital, which can be refined and expanded with improved data and evidence. To note, throughout the document, the word "impact" is used interchangeably with "additionality" and refers to financial and non-financial additionality. An additionality framework can be found in Annex 4.

While various types of institutions provide below-market concessional capital, all will be referred to as "concessional investors" (or "investors") for the purposes of this report, distinguishing them from "commercial investors", who seek commercial rates of return commensurate with the risks taken.

Additionally, this document was written to help inform the Financing for Agricultural Small-and-Medium Enterprises in Africa (FASA) Fund, a fund of funds that aims to unlock financing for agri-SMEs across Africa by supporting investment funds that are active in the sector[4]. This report is intended to act as an input for FASA's learning agenda, as well as help inform other investors structuring concessional capital for agriculture.

[4] See www.fasafund.com for more information.

3. METHODOLOGY

ISF combined quantitative and qualitative approaches to evaluate the extent, deployment, and impact of concessionality in agriculture-focused investment funds. This analysis began with an extensive literature review - references reviewed in Annex 5. Subsequently, ISF collected and analyzed data from a diverse sample of 18 impact investing funds (fund selection criteria are available in Annex 1). All profiled funds invest in the agrifood sector in Sub-Saharan Africa but feature very different characteristics regarding their approach to additionality. These funds differed in three respects: i) subsidy characteristics (i.e., type of concessional instrument, amount of subsidy), ii) investment strategy (e.g., sector, investment instrument, etc.), and iii) stage of investment cycle (i.e., fundraising, investing, divesting). Also, their degree of exposure to Sub-Saharan Africa – a few have a global portfolio, most are solely focused on the continent but have country diversification, and two are single-country funds – further determine its risk profile, operational characteristics, and in some cases, approach to additionality.

ISF collected more than **30 data points**[5] from fund managers through a questionnaire designed around the following dimensions (Annex 2 provides an overview of the data points included in the questionnaire.)

- **General information**, including information on the fund manager (e.g., AuM, agriculture experience, previous funds managed) and the fund's high-level characteristics such as the fund's size, term structure, return profile, target net IRR, and the date of first close.
- **Fund characteristics**, including the fund's investment strategy (e.g., instrument used, target interest rates, investee characteristics), capital structure and use of concessional capital (i.e. amount, types of instruments, terms, and usage), and pain points faced by the fund manager throughout the fund development lifecycle (i.e., design, launch & strategy validation, and scale up).
- **Impact strategy and additionality**, including impact potential (i.e. theory of change, primary KPIs and targets, assessment of additionality).

To ensure consistency in the data set for drawing insights while maintaining anonymized results, the analyzed sample was broken into four fund archetypes as follows:

Wholesale debt funds (N=5)

- AuM: $100M+
- Ticket: $5M+
- Mostly indirect strategy
- Hard currency

Wholesale debt funds are mainly deploying indirect debt strategies to finance financial intermediaries such as banks, Micro Finance Institutions (MFIs), and other local financial institutions. They are large funds (AuM $100M+) able to blend significant amounts of capital into the agrifood sector by targeting market gaps in the local financial sector. Wholesale debt funds often focus on intermediaries operating in segments that are otherwise overlooked by

[5] The amount of data collected varied across the funds, and ISF was unable to gather all 30 data points for every fund in the sample. Therefore, sample size is mentioned for figures when relevant.

traditional local financial institutions (e.g., staple crops and local currency value chains, rural businesses, innovative models, and early-stage businesses). They normally invest tickets above >$5M, in hard currency in established financial institutions and a few large and well-established (often vertically integrated) agri-businesses. To note, wholesale funds are excluded from FASA's investment strategy.

Niche impact debt funds (N=7)

- AuM: $20M – $100M
- Ticket: $300K – $5M
- Direct strategy
- Local & hard currencies

Niche impact debt funds are intermediate-sized funds (AuM $20M to $100M) providing direct debt investments to agri-SMEs operating in underserved areas with limited access to local financial institutions. Their investment thesis typically targets specific value chains, themes, or geographies, aiming to support small businesses with growth potential and the ability to generate impact. By delivering short to medium-term[6] capital directly to agri-SMEs, these funds have a tangible impact on both capital mobilization and local communities.

Growth equity funds (N=3)

- AuM: $30M – $200M
- Ticket: $3M – $6M
- Direct strategy

Growth equity funds provide equity or mezzanine financing to support the scaling-up of dynamic and high-growth agri-SMEs, such as processors, ag-services, and ag-techs. They are often managed by experienced fund managers, able to raise large funds ($30m-$200m) from a diverse pool of investors (DFI, family offices, foundations, donors). Growth equity funds provide a bridge between small ticket funds and larger funds with tickets > $3M (including DFIs investing directly). Given the inherent high risk of equity strategies in emerging markets, there are relatively few growth equity funds in this market, as reflected in our limited sample size.

Early venture equity/quasi-equity funds (N=3)

- AuM: $2M – $30M
- Ticket: $250K – $3M
- Direct strategy

Early venture equity/quasi-equity funds provide initial seed capital into small and nascent businesses with high growth and impact potential, operating in underserved geographies. Early venture equity/quasi-equity funds often feature high-risk strategies due to the early-stage profiles of their underlying SMEs. They also operate in relatively illiquid markets (i.e., limited exit options), facing greater uncertainty in terms of financial outcomes. However, they can be highly impactful, supporting an under-financed segment with the investment and technical assistance needed to build the market.

While all funds are different, these archetypes generally align with differing levels of commerciality, ranging from wholesale funds as the most commercially driven strategies to early venture equity/quasi-equity funds which tend to be the least commercial.

Data from the following funds (see Table 1 below) were included in the sample used for this guidance document. While most of the funds were able and willing to provide robust data to our team, for two funds (the BUILD fund and African Agriculture Capital Fund) only public information was available. Additionally, while the Mastercard Foundation Africa Growth Fund was included in this report to provide qualitative insights into its investment approach, it was excluded from the quantitative analysis because, as a fund of funds similar to FASA, it is not directly comparable to the other funds in the sample.

[6] For the purposes of this report, short, medium, and long-term capital are defined as loans with tenors of <1 year, 1 – 5 years, and 5+ years respectively.

Table 1: List of funds in the sample

FUND NAME	FUND MANAGER / ADVISOR	CURRENT FUND SIZE (USD)	TERM STRUCTURE	STAGE	INSTRUMENT	INV. STRATEGY	CONCESSIONAL INSTRUMENT	GEOGRAPHY
Wholesale debt funds								
eco.business Fund	Finance in Motion	~$102M	Open-ended	Investing	Debt	Mostly intermediation	First-loss	Global, LDCs
Farmfit Fund	IDH FarmFit	$107M	Closed-ended	Investing	Mostly debt	Mostly direct	First-loss, TA, Guarantee	SSA, LatAm
Huruma Fund	Gawa Capital	~$129M	Closed-ended	Investing	Mostly debt	Mostly intermediation	First-loss, TA	Global
Land Degradation Neutrality Fund I	Mirova	$208M	Closed-ended	Investing	Mostly debt	Direct	First-loss, TA, Guarantee, Design grant	Global
Climate Smart Food Systems	responsAbility	$106M	Closed-ended	Investing	Debt	Direct	First-loss, TA, Guarantee	Global
Niche impact debt funds								
Agri-Business Capital (ABC)	Bamboo Capital	$55M	Open-ended	Investing	Debt	Hybrid	First-loss, TA, Design grant	Global
BUILD Fund*	Bamboo Capital	$50M	Closed-ended	Fundraising	Mostly debt	Direct	First-loss, TA, Guarantee	SSA
Fairtrade Access Fund (FAF)	Incofin	$54M	Open-ended	Investing	Debt	Direct	First-loss, TA	Global
MCE Empowering Sustainable Agriculture	MCE Social Capital	~$42M	Closed-ended	Investing	Debt	Hybrid	First-loss, TA, Design grant	Global
Nutritious Foods Financing Facility	Incofin	~$13M	Open-ended	Fundraising	Debt	Direct	First-loss, TA, Design grant	SSA
SME Impact Fund I	Match Maker Fund Management	~$6M	Closed-ended	Investing/ Fundraising	Debt	Direct	First-loss, TA, Design grant	SSA (EA)
Yield Uganda	Pearl Capital	~$22M	Closed-ended	Divesting	Multiple	Direct	First-loss, TA	Single-country: Uganda
Growth equity funds								
AgDevCo	AgDevCo	$190M	Open-ended	Investing/ Fundraising	Debt	Direct	First-loss, TA	SSA
Acumen Resilient Agriculture Fund	Acumen	$58M	Closed-ended	Investing	Equity, quasi-equity	Direct	First-loss, TA, Design grant	SSA
Fund for Agricultural Finance in Nigeria	Sahel Capital	~$66M	Closed-ended	Divesting	Equity	Direct	First-loss, TA	Nigeria
Early venture equity/quasi-equity funds								
African Agriculture Capital Fund*	Pearl Capital	$25M	Closed-ended	Liquidation	Equity, debt	Direct	First-loss, TA, Guarantee	SSA (EA)
Sinergi Burkina	Sinergi SA	~$3M	Open-ended	Investing/ Fundraising	Equity	Direct	First-loss, TA	Single-country: Burkina Faso
Kampani	Kampani	~$15M	Open-ended	Investing	Mostly debt	Direct	First-loss	Global
Included in the qualitative analysis only								
Mastercard Foundation Africa Growth Fund	Mennonite Economic Development Associates	$150M	Open-ended	Investing	Debt, equity, quasi-equity	Fund of funds	Provides First-loss, TA	SSA

*Funds for which only public data has been collected

ISF expanded the research by conducting a series of **in-depth qualitative interviews** (list of interviewees available in annex 3). ISF spoke to **16 fund managers** to better capture their experience regarding their fund's journey, the intricacies of the fundraising process, investors' preferences regarding the fund's structures, and the funds' impact strategies and approaches to impact outcomes. Additionally, ISF interviewed **7 concessional investors**, including representatives from bilateral agencies, DFIs, family offices, and foundations. These conversations helped validate the research findings, gain insights into the investors' approaches and decision-making processes when allocating concessional capital to agriculture-focused funds, and identify any possible gaps in the available data.

Key findings were discussed and debated with a dedicated Advisory Committee, with representatives from a broad group of stakeholders including Aceli Africa, Convergence, the Collaborative for Frontier Finance, and the Catalytic Capital Consortium.

4. KEY FINDINGS

Findings from the analysis have been organized by the following two dimensions and associated research questions:

- **Concessional investors' approaches to deploying capital:** What are the different strategies of concessional investors and how does their risk/return profile drive their allocation of concessional capital? What risk mitigation strategies are used? How can concessional investors support funds and enhance their performance other than by allocating first-loss capital, using creative or/and alternative forms of support?
- **Concessional investors' approach to additionality/impact:** How do investors define additionality/impact when investing in agri-SME funds? How do they articulate their impact objectives in relation to risk/return profiles?

CONCESSIONAL INVESTORS' APPROACH TO DEPLOYING CAPITAL

4.1 Degree of concessionality is not necessarily tied to fund economics, as numerous factors hamper the application of a consistent approach to subsidy allocation

Generally, the amount of concessionality required in a fund investment depends on two primary factors: i) the expected net financial performance of the fund versus its perceived risk; and ii) the rate of return demanded by senior investors versus their risk appetite. Net fund performance can be broken into the following components, as illustrated in Figure 1:

- **Gross fund income**, driven by the interest charged to the underlying portfolio in debt funds or the investment surplus upon liquidation in equity funds. It depends heavily on the fund manager's ability to generate a strong pipeline and deploy capital effectively. Investors assess this by reviewing the manager's track record and the quality of the investment pipeline.
- **Expected portfolio losses** reflect both the inherent risk of investees and, in debt strategies, the fund manager's ability to recover non-performing loans.

  Risk assessment is complex and subjective, and risk perception varies significantly among investors. In addition to the high inherent risks associated with agriculture in emerging markets, the sector is also significantly exposed to low-probability events with potentially devastating effects (i.e., climate shocks). Misperception of risk can also stem from investors' cognitive biases (i.e., narrative biases or preconceptions) and lack of familiarity, both with the value chains or the specific country contexts.

  To assess real or actual risk, investors can consider historical losses for the asset class, as well as the fund manager's track record; however, historical data is not available for all asset classes. In established asset classes, such as working capital for export commodities, historical series for portfolio risk is available, largely thanks to the collaboration efforts of the members of CSAF[7]. FI financing, one of the pioneering impact investing strategies, is also a mature asset class and benefits from a long historical series of data, helping investors assess the risk of more agri-focused intermediation strategies. On the contrary, other asset classes do not benefit from this shared transparency or are not as established and require investors to rely more heavily on other metrics, such as fund manager track record in other asset classes.

- **Fund manager fees**, set at around 2% per annum, are in line with industry standards for commercial investment funds. However, some funds may require higher fees, particularly those targeting smaller ticket sizes or where significant market development work is needed.

Interviews highlighted that concessional investors often do not have a standardized methodology for prioritizing investments in funds and tend to make relatively opportunistic allocation decisions based on criteria such as the perceived need for subsidy, political priorities, current availability of concessional capital, and existing relationships with fund managers.

In practice, first-loss tranches are sized to cover foreseeable losses and protect against some degree of uncertainty, often with investors looking to price in worse-case scenarios rather than just the historical or expected loss rates for a given asset class. They are calibrated to provide risk protection and expected returns that senior investors find adequate, which is determined by the risk tolerance of the capital that investors manage. Finally, risk appraisal for debt strategies are notably different than for equity strategies, as explored in the subsequent sections.

Debt strategies

Debt investments, especially in well-established asset classes and markets, generate predictable cash flows through contracted interest payments and amortization schedules, which makes the overall risk profile of the fund relatively clear. As such, debt funds can often be quantitatively assessed based on historical data and expected pipeline, and donors can unpack fund economics to support their allocation strategy.

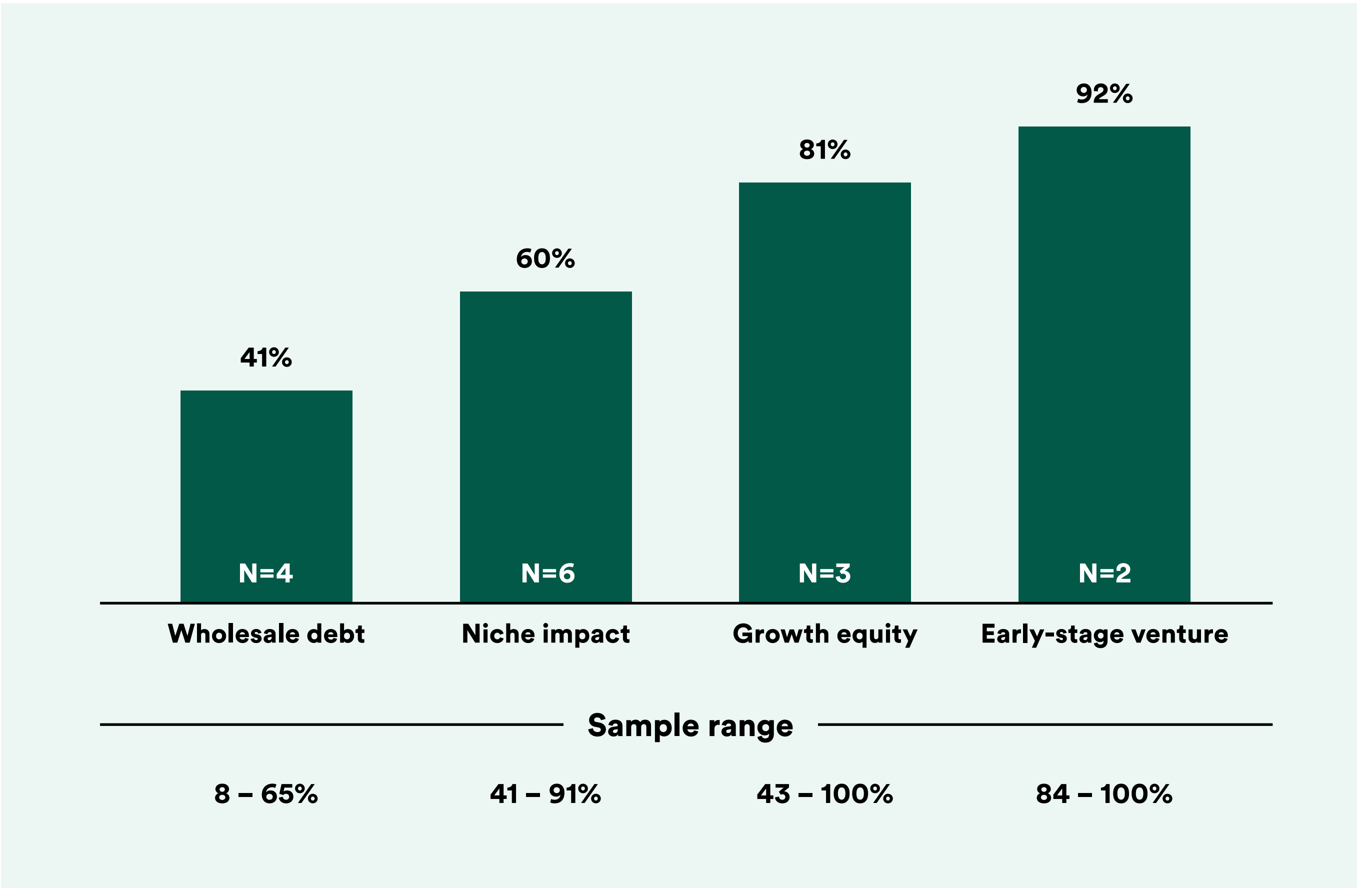
For debt funds, our analysis provides some directional evidence that senior investors may be demanding protection levels that significantly exceed actual risks or the fund manager's expected portfolio losses. Looking at the estimates of portfolio losses in our sample (N=8), it appears that expected losses are notably lower than the funds' junior first-loss tranche. **Estimates of portfolio losses for debt strategies in our sample range from around 2% to 6%**. Fund managers with lower-risk direct lending strategies report expected portfolio losses of around 2-3%, and around 2% or below for intermediated strategies. Meanwhile, estimates for higher-risk strategies, like junior debt, fall on the higher end of the range. To note, a number of funds in the sample are still investing, and definite conclusions about their performance are premature.

Fund managers' expectations of portfolio losses are grounded on their track record and thorough market analysis. However, future performance is not guaranteed and carry inherent high risks and uncertainty, so investors may use more conservative estimates to ensure an additional

[7] CSAF periodically publishes data on the collective lending activities of its members, including loan sizes, crops supported, or size of borrowers.

degree of protection. In our sample, wholesale debt funds had, on average, a first-loss tranche of ~40% of the fund size, and ~60% for niche impact debt funds, reflecting the differences in risk perception of these two strategies.

Figure 1: Total senior investor protection including guarantees (%), by archetype



Our sample data suggests that, even with proven strategies, funds tend to have senior protections that significantly exceed the expected level of risk: wholesale and niche debt funds have junior tranches that covered ~15x and ~20x the estimated fund losses respectively. While applying a multiple to portfolio loss estimates seems to be appropriate to calculate the necessary senior protection, it did not come up as a metric used by either investors or fund managers. **Directly linking the size of the junior tranche to the economics of the fund would reduce the chances of over-committing concessional capital.**

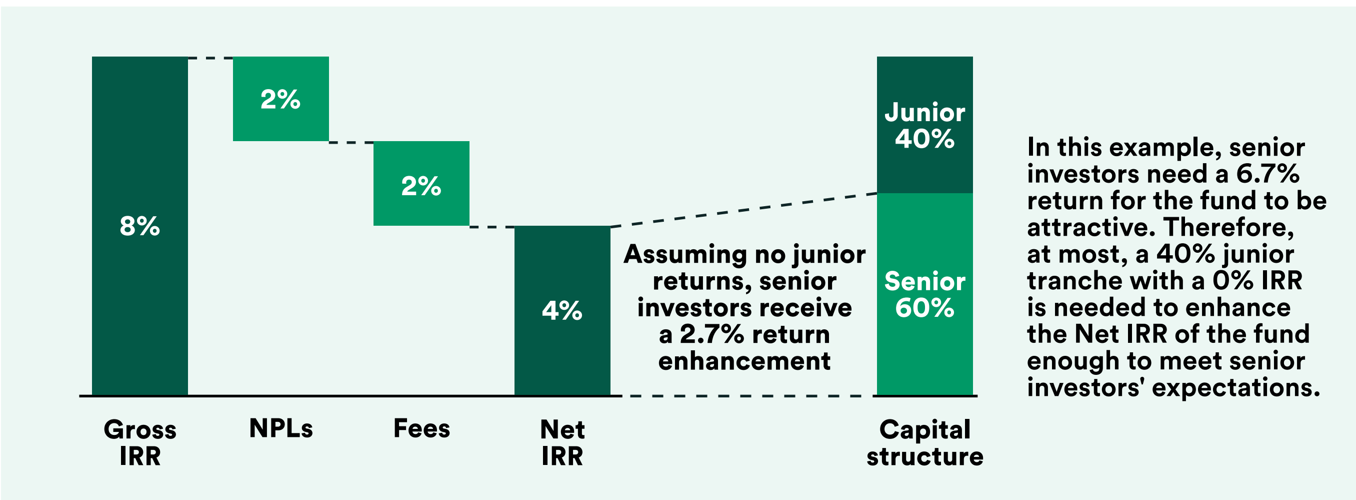
Funds aiming to mobilize more commercially-minded investors and/or investors who are less familiar with the asset class provide not only risk protection but also enhanced returns to senior investors – establishing a cap on financial return on the junior equity tranche and having financial returns accrue in a disproportionate amount to senior investors. In our sample, only three debt funds incorporate return enhancement: two wholesale debt funds and one niche impact fund. All providers of return-enhancing capital in our limited sample are bilateral agencies[8].

[8] In our sample, senior investors benefiting form return-enhancement features were institutional investors with a relatively more commercial profile, and corporate investors.

From a concessional investor perspective, giving up financial returns can be justified by i) the additional capital mobilized from sources that would otherwise not invest in the asset class, and ii) strong impact potential at the beneficiary level.

On average, wholesale debt funds generate net IRRs of approximately 4-5% (N=4); niche impact funds are slightly below at 3-4%. Return-enhancing mechanisms embedded in first-loss capital tranches can significantly boost overall senior returns. As shown in Figure 2, an illustrative fund with a 4% net IRR and a 40% junior equity tranche that forgoes all returns could increase senior investors' returns by over 250 basis points. This scenario is purely illustrative, since junior investors may not forgo 100% of their share of returns, but have them capped. In any case, it highlights the potential significance of return-enhancement features in shaping the risk/return profile.

Figure 2: Illustrative return accrual to senior investors from first-loss capital with return enhancement feature



Equity strategies

Equity funds have higher uncertainty around financial returns, so a different approach is required. The allocation of first-loss capital is linked to senior investors' risk tolerance. This is closely tied to (i) the pipeline's perceived risk and (ii) the fund structure and market liquidity, since equity funds in illiquid markets have additional risks associated with timed exits in closed-ended structures[9], which could result in premature liquidations at sub-optimal returns.

Given higher risks, as seen in Figure 1, junior tranches in equity funds are significantly larger than in debt funds. In our sample, junior tranches represented on average ~80% of the fund's capital structure (vs. 49% in debt funds), with junior investors generally sharing equal upside (only 1 out of 6 minimally remunerates junior investors for extra risk). Given the high-risk profile of some strategies, crowding in private capital, especially from investors providing hard currency, may not be suitable for all funds.

[9] While many traditional equity funds, especially in developed markets, use 10+2 term structures, these timeframes tend to be too short to fully capture value created in agriculture investments in emerging market.

4.2 Concessional investors use risk mitigation strategies to balance concessionality and impact

In order to more efficiently deploy concessionality at the fund-level, certain risk mitigation levers are commonly used.

- **Leveraging intermediation strategies (i.e., investing through financial institutions)** allows concessional investors to deploy capital at scale in the hard-to-serve agri-SME segment. Intermediaries are well positioned to reach SMEs needing smaller ticket sizes and can leverage their deep understanding of local markets, mitigating investment risk. Sample data shows funds with intermediation strategies can attract institutional investors (e.g., pension funds) and use lower senior protection than those using direct strategies. Interviews with FMs operating funds with both strategies confirmed that investors often ask for a higher portfolio allocation in the intermediation strategy to reduce the funds' risk.

- **Incorporating natural hedges into the investment strategy**, such as diversifying the portfolio across the value chain (e.g., upstream, downstream), different crop types, and geographies, while building strong local relationships with key value chain actors, can reduce the fund's overall risk. In particular, diversifying away from primary production helps limit exposure to the more volatile segments of the value chain, favoring more stable areas like agro-processing and logistics, and enhancing portfolio resilience against market fluctuations and climate-related risks. However, this may affect the depth of impact, as discussed later in this document. Furthermore, cultivating strong on-the-ground relationships and partnerships (e.g., with off-takers or providers) improves supply chain visibility, providing a deeper understanding of risks.

- **Using a flexible mandate** mixing debt and equity strategies has proven helpful in decreasing risk or increasing return upside in agri-SME funds in emerging markets in a small number of funds. For debt funds, equity investments provide investors with additional return upside, while controlling for risk; for equity funds, debt helps counterbalance the high perceived risk of an equity strategy, and it can also speed up the pace of deployment, as debt pipeline is more abundant than equity. This strategy is relatively uncommon given the investment skillset required for equity and debt are different, so offering both may increase overall fund management costs.

- **Generating additional revenue streams** can help fund managers cover operational costs when the standard management fee (around 2%) is insufficient, which is often the case for funds targeting smaller segments of the market. In such cases, fund management expenses tend to be drawn from investment capital, reducing overall financial returns. However, fund managers can offset these costs by diversifying their income sources—through activities such as providing technical assistance, market access support, or financial advisory services to agri-SMEs—thereby enhancing the financial sustainability of the fund management firm. While additional revenue streams can generate needed income, these can also cause potential conflicts of interest and should be incorporated by fund managers thoughtfully.

HURUMA FUND

Leveraging risk-mitigation and return-enhancement to attract institutional investors

FUND CHARACTERISTICS			
Fund manager	Gawa Capital	**Impact theme**	Improve the financial inclusion and livelihoods of rural populations, especially farmers' access to tailor-made financial services, by financing and supporting through TA established rural/ agriculture-focused financial institutions and agri-businesses
Archetype	Wholesale debt fund		
Type	Closed-end (10+2 years), launched in 2019		
AUM & Stage	EUR 120m; investing	**Capital structure**	**Equity** **Junior:** EUR 10m Junior equity, funded by the European Union (EU) and managed by Spanish development bank Compañía Española de Financiación del Desarrollo (COFIDES) **Senior:** EUR 90m raised by Spain's CaixaBank from its private banking clients **Debt** EUR 20m concessional debt, funded by the Spanish bilateral agency Agencia Española de Cooperación Internacional para el Desarrollo (AECID)
Instruments	Debt intermediation (~70%) and direct equity (~30%), hard currency (EUR and USD)		
Ticket size	EUR 2m to EUR 10m		
Geography	Latin America and Sub-Saharan Africa (70% min), Asia (30% max)	**Website**	www.fondohuruma.com

Introduction

Thanks to its innovative blended capital structure and investment strategy, Huruma has successfully attracted substantial institutional capital from Caixabank's private banking clients to support its impact goals. This structure has enabled Huruma to raise 3x the amount of commercial capital compared to its concessional capital, engaging investors who might otherwise avoid rural finance. The fund achieves this by integrating a combination of risk mitigation and return enhancement strategies, creating an overall risk/ return profile that appeals to institutional investors.

Risk mitigation and enhancement strategy employed by the Huruma Fund

- **Intermediated investment strategy:** Huruma builds upon GAWA Capital's extensive experience investing in financial intermediaries to help reduce the fund's risk and tap into existing expertise. By investing 70% of the fund in financial intermediaries serving smallholder farmers and agri-SMEs, Huruma can diversify its risk across a broader range of end beneficiaries (i.e. farmers and agri-SMEs) compared to if they were making direct investments. Additionally, by investing in financial intermediaries themselves, Huruma can tap into the institution's local expertise and collection infrastructure further reducing the risk of default.
- **First-loss protection:** In addition to reducing risk through an intermediation strategy, Huruma's capital structure also provides senior investors with significant downside protection, as the fund has a EUR 10m first-loss equity tranche.
- **Mixing debt and equity:** To enhance the overall return of the fund without substantially increasing the risk, Huruma employs a mix of debt and equity instruments. By investing 30% of the fund in equity instruments, Huruma can participate in equity upside, securing higher returns for investors, while still mitigating risk.

Conclusion

By combining de-risking mechanisms with return-enhancing features in a coordinated way, Huruma has been able to mobilize untapped sources of private capital towards improving access to finance for smallholder farmers in Latin America, Sub-Saharan Africa, and Asia. At the time of this study, GAWA Capital had just completed a first close of EUR 140m on a new fund named Kuali, leveraging the same de-risking and return-enhancing features.

Sources: Fund website (Accessed June 2024), Huruma Fund 2021 annual report, and interviews with fund manager

SINERGI BURKINA

Leveraging diverse revenue streams to cross-subsidize concessional investment activity, enabling deep and sustainable impact

FUND CHARACTERISTICS			
Fund manager	Self-managed	**Impact theme**	Support the SME sector, promoting employment, and improving livelihoods in Burkina Faso, while engaging domestic private capital to develop the local business ecosystem.
Archetype	Early-stage venture fund		
Type	Evergreen, launched in 2014		
AUM & Stage	EUR 3m as of June 2024; investing/ fundraising	**Capital structure**	**Equity** EUR 3m as of June 2024
Instruments	Direct equity and quasi-equity		
Ticket size	EUR 30,000 to EUR 300,000		
Geography	Burkina Faso	**Website**	www.sinergiburkina.com

Sinergi Burkina faces significant financial sustainability challenges that are inherent to its impact objectives.

To foster a dynamic SME sector in Burkina Faso, Sinergi Burkina provides local early-stage SMEs with growth equity and support with the aim of developing the SME ecosystem in the country. This focus on local SMEs results in smaller transaction sizes, relatively higher costs, and slower capital deployment. Consequently, the fund relies on a cost-based budget rather than a typical 2% management fee, which does not fully cover operational expenses due to high transaction costs and erodes investors' financial return potential.

To overcome these limitations, Sinergi Burkina leverages diverse revenue streams to cross-subsidize its investment activity, enabling deep impact.

To offset budget constraints inherent in its model, Sinergi Burkina has diversified its revenue streams through impact-aligned activities that cross-subsidize its operations. Specifically, Sinergi Burkina manages donor-funded accelerator programs, which also generates pipeline for the fund, therefore creating meaningful synergies with its investment activities. This is especially relevant for equity fund managers who manage rather illiquid portfolios.

Sinergi Burkina provides a good example of how local teams can monetize their presence and expertise to cross-subsidize investment activities that, while not sustainable on their own, can generate deep systemic impact. However, while this model can ensure sustainable investment operations, upside potential for investors remains constrained.

Sources: Fund website (Accessed June 2024), IPDEV2 2023 Fund evaluation, and interview with fund manager

Interviews with fund managers confirmed the importance of incorporating risk-mitigation considerations into investment strategy design. In some cases, anchor investors influenced the process by pushing for a greater focus on lower-risk strategies, by taking a portfolio approach that balances lower-risk investments with high-risk, higher-impact opportunities. Such a cross-subsidy strategy is particularly relevant for investors with specific financial return requirements. This portfolio-level strategy enables concessional investors to meet their financial goals while maximizing impact across their entire investment portfolio.

MASTERCARD FOUNDATION AFRICA GROWTH FUND

Employing a diversified portfolio to mitigate risk, deliver financial returns, and ensure a high-impact approach

FUND CHARACTERISTICS			
Fund manager	Mennonite Economic Development Associates (MEDA)	**Impact theme**	Supporting early-stage, growth-oriented businesses and fostering the launch of new SME funds across Africa, through investments in female-led, locally-managed investment funds, with a focus on gender-lens investing and job creation.
Archetype	Fund of funds		
Type	Open-ended, launched in 2022		
AUM & Stage	USD 150m; investing		
Instruments	Debt, equity, quasi-equity, both local and hard currencies		
Ticket size	USD 1m to USD 15m		
Geography	Sub-Saharan Africa	**Website**	www.africagrowthfund.org

Early-stage investment funds, especially female-led funds, face difficulties in accessing institutional capital. The Mastercard Foundation Africa Growth Fund (the "Fund") is a catalytic fund of funds that provides access to institutional capital to this class of fund managers to invest in SMEs. Ultimately, the fund aims to improve gender outcomes, SME growth, and job creation for youth and women.

Fund managers often face the challenge of balancing concessional support for investees with generating risk-adjusted returns for investors, which can lead to negative fund economics and the need for subsidies. To navigate this trade-off, the fund employs a diversified fund-of-funds portfolio approach that aligns impact and return goals while managing risk. Catalytic by nature, the fund seeks a modest positive return to cover costs and inflation. The fund achieves this by creating a balanced portfolio of investments across different risk/return profiles and asset classes, including equity, debt, and quasi-equity. Safer investments offset higher risk and/or more catalytic investments, while potential equity upside helps cover any losses or catalytic commitments. The fund supports both first-time and experienced investment vehicles, the majority of which to date are fund managers, fostering local fund development and supporting new, innovative strategies and fund vehicles alongside traditional approaches to fund investments. The fund has also supported local domiciliation of investment vehicles on the African continent, by including this requirement as part of its condition's precedent.

The fund's warehousing facility (USD 7.5m within the USD 150m capital pool) provides essential early-stage capital to investment vehicles and serves as an incubator, enabling them to build a track record and expand their portfolios, thereby de-risking investments and ensuring a sustainable pipeline of projects. Additionally, the USD 25m Business Development Services (BDS) facility offers targeted non-financial support, such as technical assistance, capacity building, and strategic advice, to support portfolio companies, most of which are SMEs, to become investment-ready and scalable. This comprehensive support drives long-term success, fosters job creation, economic empowerment, and sustainable growth across sectors in Africa.

By using a portfolio approach, coupled with technical assistance, the fund supports innovation, nurtures the growth of new investment vehicles, stimulates systemic change, and drives job creation for African youth and women. The fund backs riskier, potentially more impactful investment vehicles while mitigating risk and providing investors with a sustainable modest return.

Sources: Fund website (Accessed June 2024) and interview with fund manager

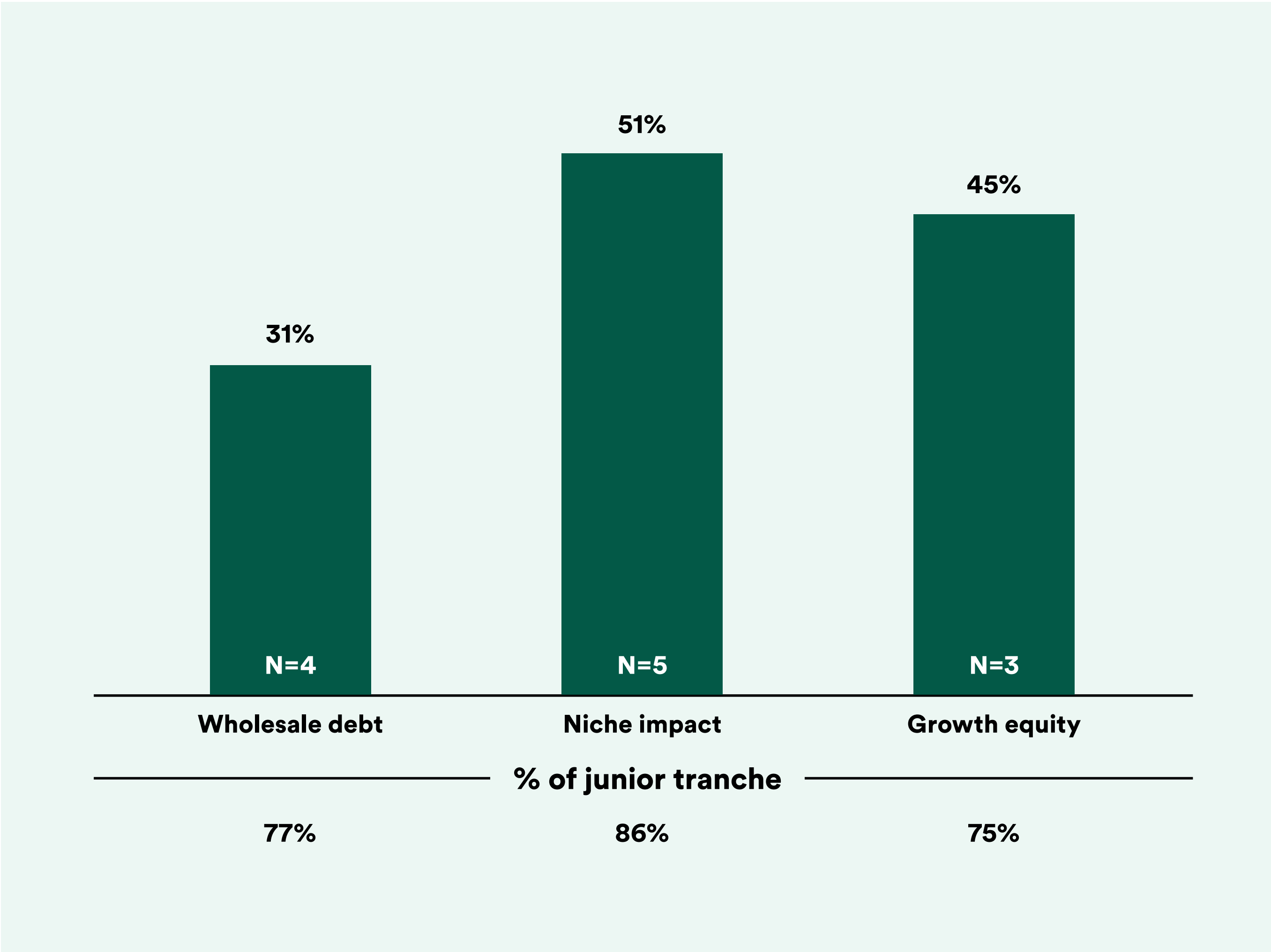
Interviews also revealed that positive track records may pigeonhole fund managers into certain fund structures and investment strategies, limiting opportunities for innovation. When trying to add a layer of innovation (moving from intermediation to direct strategies, providing different asset classes, focusing on an impact theme), fund managers typically require higher levels of concessionality to protect senior investors who prefer that managers stick to proven strengths.

4.3 Anchor investors play an important role in establishing a fund by signaling market confidence and/or reducing risk but may lead to compromises around the fund's purpose and impact

Anchor investors that provide junior capital are crucial for the successful establishment of funds in high-risk market segments, typically providing the initial commitment of high-risk capital. Their initial capital commitment can give confidence to other investors around the fund's viability and can make the risk-return profile more attractive for senior investors. Anchor investors also influence key aspects of the fund, often shaping the investment strategy and the fund's risk-return and impact profiles.

Interviews revealed that access to anchor capital is often erratic, and anchor investors' goals are not often transparent. Fund managers with strong networks and a close understanding of investor priorities are more likely to secure anchor investments. In some cases, bilateral donors have sponsored and fully funded investment funds to address a specific impact objective or support a market solution they strongly believe in. To note, this outcome is not necessarily intentional but often results from a mismatch between the donor's favored investment and impact strategy and the suitability of that approach for other investors. Finally, budget availability and the timing of the fundraising process can also influence these decisions.

Figure 3: Average anchor investor contribution per archetype (% of total fund size)



In our sample, out of 18 funds, 16 had an anchor investor. They provided, on average, ~80% of the junior tranche and ~40% of the total fund. Bilateral agencies and foundations are the most common anchor investors (nine and four funds respectively), and DFIs to a lesser extent (two funds). The sample showed that riskier investment strategies have larger anchor commitments - see Figure 3[10]. Note, that this level of investor concentration is significantly higher than that typically seen with commercial investors or in developed markets, where single investors generally limit their contribution to around 15% of total fund size.

10 Early venture equity/quasi-equity funds were not included in this analysis due to the small sample size.

THE IDH FARMFIT FUND

Leveraging a strong concessional anchor investor to boost market confidence and reduce perceived risk

FUND CHARACTERISTICS			
Fund manager	IDH Investment Management	**Impact theme**	Increase A2F within smallholder value chains by de-risking (senior) investors by taking high-risk positions.
Archetype	Wholesale debt fund		
Type	Closed-end (15 years), launched in 2019		
AUM & Stage	EUR 100m; investing	**Capital structure**	**Equity** EUR 50m junior redeemable grant, committed by Dutch MFA as anchor investor **Debt** EUR 50m senior profit-sharing loans with a concessional return, committed by diverse investors (Unilever, Mondelēz, JDE Peet's, FMO, and Rabobank) **Guarantee** Up to USD 250m guarantee provided by the US DFC, covering 50% of senior co-lenders
Instruments	Guarantees, subordinated loans, and mezzanine debt (jointly 70 %), equity (30%); hard currency (EUR and USD)		
Ticket size	EUR 1m to EUR 10m, with the IDH Farmfit Fund taking up to 50% of a total transaction.		
Geography	DAC Countries; max. 60% Africa, max. 40% LATAM, max. 40% Asia	**Website**	www.idh.org/investment-solutions

The IDH Farmfit Fund uses concessional capital and aims to de-risk (senior) capital in certain smallholder value chains in emerging markets with the purpose of positioning smallholder finance as a viable asset class. By securing initial concessional commitments - EUR 50m first-loss tranche from the Dutch MFA and a second-loss guarantee of up to USD 250 million from the US DFC - the fund has the option to offer senior investors substantial downside protection. This approach enabled IDH Farmfit Fund to raise EUR 50 million from corporate investors, including Rabobank and Mondelēz. The initial support of the Dutch MFA and US DFC was instrumental for the fund to achieve scale. And, by taking subordinated positions up to 50 % in debt transactions, the fund catalyzes other investors on a deal-by-deal basis.

Sources: Fund website (Accessed June 2024) and interview with fund manager

4.4 Other types of concessional capital, namely design grants and technical assistance, are equally crucial for funds' success

Fund managers also face challenges in accessing other types of concessional capital, particularly design grants and technical assistance. These resources can be essential, especially for first-time or small fund managers who lack the capacity to cover initial operational costs and can benefit from support both at fund manager and portfolio levels.

Design and Impact Assessment Grants: Grants covering initial fund design and set-up expenses play an important role in the success of new funds, especially for first-time fund managers or those innovating in their investment strategy. In our sample, around 60% of the funds received a design grant (N=10). Grants ranged from $60,000 to $3,000,000 and were provided mostly by bilateral agencies and foundations. Most often, grants were provided by fund investors to cover initial design but also to support impact monitoring and evaluation efforts. A number of fund managers indicated that design grants were often difficult to access and that the application and reporting processes were onerous.

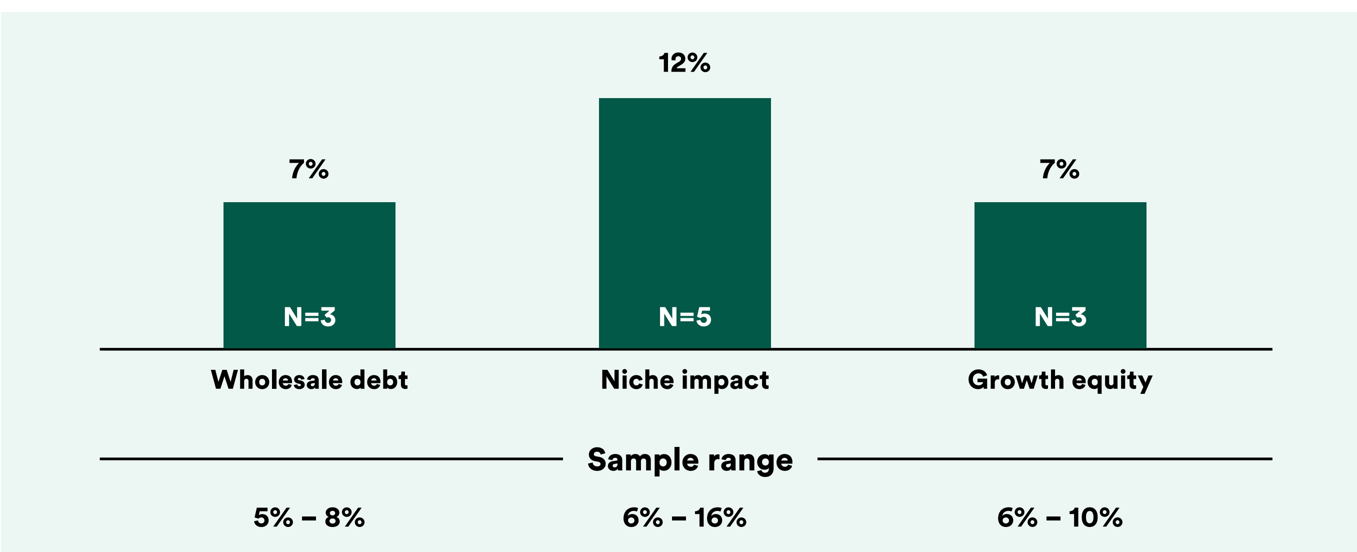
Technical Assistance (TA): Fund managers acknowledge that technical assistance (TA) is crucial at the portfolio level to de-risk their investments and enhance impact. Of the sample, all but one of the 18 funds had dedicated post-investment TA for their portfolio companies. Despite its importance, interviews revealed that raising TA funds often takes a backseat during the fundraising process, becoming a limitation once the fund is active. This de-prioritization of TA can lead to missed opportunities to address portfolio needs, especially long-term ones, by running out of TA funds, while consistently looking to replenish them throughout the life of the fund can be distracting for the fund management team.

All fund managers interviewed mentioned that there is no methodology to determine the ideal size of a TA fund and that the industry uses an indicative ratio of 10% of fund size. However, most fund managers mentioned their TA budgets were insufficient. Many fund managers agree on the need for more capital to document their impact results, and to extract learnings and insights from their investments.

Figure 4 shows the relative size of these TA facilities as a proportion of fund size, by archetype. The graph suggests that while riskier and/or more long-term strategies (i.e., equity) would justify higher TA budgets, in practice, in our sample, they are using smaller budgets. To note, early-stage venture equity funds have been excluded from Figure 4, as they use non-comparable TA models: separate TA budgets, in-house TA covered by fund fees, or opportunistic access to TA facilities independent from the fund.

A promising development in the TA landscape is the recent trend of investment funds partnering with specialized organizations to deliver TA and manage impact. These partnerships are prevalent in funds with a science-based impact theme (i.e., climate adaptation, nutrition, sustainable agriculture). By collaborating with organizations that have deep expertise in these areas, funds tap into specialized knowledge, access cutting-edge research, and implement best practices in impact management, building stronger credibility vis-à-vis investors and stakeholders.

Figure 4: TA facility size per fund archetype



ACUMEN RESILIENT AGRICULTURE FUND (ARAF)

How anchor investors can create outsized impact by providing expertise and technical assistance in addition to capital

<table>
<tr><th colspan="4">FUND CHARACTERISTICS</th></tr>
<tr><td>Fund manager</td><td>Acumen Capital Partners</td><td rowspan="3">Impact theme</td><td rowspan="3">Improving smallholder farmers’ resilience to climate change to ensure long-term sustainable increases in agriculture productivity and incomes</td></tr>
<tr><td>Archetype</td><td>Growth Equity Fund</td></tr>
<tr><td>Type</td><td>Closed-end (10 years with the possibility of two 1-year extensions), launched in 2019</td></tr>
<tr><td>AUM & Stage</td><td>USD 58m; investing</td><td rowspan="3">Capital structure</td><td rowspan="3">Equity
Junior: USD 25m committed by Green Climate Fund (GCF)
Senior: USD 33m committed by FMO, Proparco, Open Society Foundation, Children’s Investment Fund Foundation (CIFF), Global Social Impact and others</td></tr>
<tr><td>Instruments</td><td>Equity & quasi-equity, hard currency (USD)</td></tr>
<tr><td>Ticket size</td><td>USD 300k to USD 4m</td></tr>
<tr><td>Geography</td><td>Uganda, Ghana, Nigeria, Kenya, Tanzania</td><td>Website</td><td>www.arafund.com</td></tr>
</table>

ARAF was launched in 2019 and focuses on investing in early-stage platform businesses that play a pivotal role in overcoming barriers faced by smallholder farmers. The fund operates across key regions, working with companies that empower farmers to access critical information, affordable financing, modern inputs, and formal markets. ARAF’s comprehensive approach involves capital investment, strategic guidance, governance and control structures, and technical assistance to ensure sustainable and impactful interventions.

ARAF is complemented by a $6.0 Million Technical Assistance Facility (TAF) that serves to de-risk investments and enhance impact. The TAF’s four main categories of support include climate adaptation and gender initiatives, business development services, ESG and audit initiatives, and impact measurement support. These categories cater to the diverse needs of investee companies, smallholder farmers, and the broader ecosystem.

To measure the success of this model, a comprehensive Monitoring, Evaluation, and Learning (MEL) framework was essential for assessing climate adaptation outcomes. As ARAF’s anchor investor, the Green Climate Fund (GCF) was instrumental among other experts in co-designing the fund’s impact approach and MEL framework. In addition to providing a 50% first-loss tranche, GCF’s climate expertise helped ARAF’s management team better integrate climate adaptation into the fund’s investment thesis. This collaboration also led to the development of innovative impact metrics now adopted by other stakeholders in the market. Furthermore, GCF supported ARAF in building in-house climate expertise by funding the hiring of a dedicated internal climate expert.

To further enhance the fund’s impact, GCF also provided $2.5 million to support part of the TAF’s climate adaptation and gender initiatives bucket. This bucket equips agribusinesses with the tools and knowledge to manage climate risks, including selecting climate-appropriate crops, adopting adaptation techniques, and diversifying income sources.

Overall, ARAF’s partnership with GCF went beyond the typical concessional capital, with GCF providing valuable expertise, creating a broader and longer-lasting impact than capital alone could achieve. This collaboration not only contributed to ARAF’s success but also developed sector-wide tools and frameworks, paving the way for the success of future climate adaptation funds.

Sources: ARAF funding proposal for the Green Climate Fund, 2018 (available online)

For instance, the Nutritious Food Financing Facility (N3F) benefits from the Global Alliance for Improved Nutrition (GAIN)’s expertise in nutrition. Similarly, ResponsAbility’s Climate Smart Food Systems Fund and the Financing for Agriculture SMEs in Africa (FASA) fund collaborate with the Consultative Group on International Agricultural Research (CGIAR) to benefit from their climate science knowledge, and the Acumen Resilient Agriculture Fund (ARAF) collaborated with the Green Climate Fund (GCF) to design their impact strategy and management tools.

CONCESSIONAL INVESTORS' APPROACH TO ADDITIONALITY/IMPACT

While blended finance discussions often emphasize capital mobilization, as discussed earlier, the DFI Enhanced Blended Concessional Finance Principles emphasize "maximum impact for the minimum level of subsidies." This highlights the need to understand and incorporate an assessment of impact in the evaluation of any investment opportunity. This section explores the trade-offs between financial outcomes and financial and non-financial additionality (economic, social, environmental, and systemic) across dimensions considered by investors. Note that in this report, we use the term "impact" to refer to non-financial additionality.

This framework, detailed in Annex 4, considers the financial and non-financial additionality at the fund level, and at the investee (i.e., agri-SME) level.

Financial additionality refers to the use of concessional capital to (1) address capital scarcity, crowding in capital by protecting or compensating investors, and/or (2) improve the financial product-market fit by making available capital with terms not present in the market (e.g., lower collateral requirements, extended tenors).

Non-financial additionality (i.e., impact) refers to (1) the economic, social, and/or environmental impact an investment has on direct and/or indirect beneficiaries, and (2) the systemic impact of an investment.

Fund level refers to the contribution of investors to the fund capital structure. Concessional investors use their capital to support the fund's viability and capacity to achieve its impact goals. This includes providing investment capital with different risk/return profiles, as well as technical support that improves fund operations and risk management.

Agri-SME level refers to the fund's investment, and how concessional investment ultimately benefits businesses underserved by conventional markets. At this level, concessional capital may help agri-SMEs improve operations, spur growth, and build long-term capacity, which in turn supports local economic development and resilience.

Interviews with investors revealed that most use the following dimensions to assess investments:

Fund level	**Investor value add** refers to the specific outcomes a concessional investment has on the invested fund, which wouldn't have been possible without this investment
	Fund pathway and future need for concessional capital refers to the funds' intrinsic need for concessionality and potential for achieving commercial sustainability
Agri-SME level	**Depth of additionality** refers to the extent and intensity of the impact of an investment
	Pace of impact generation refers to the time frame in which investors expect the funds to generate impact results

The following section explores these attributes and trade-offs.

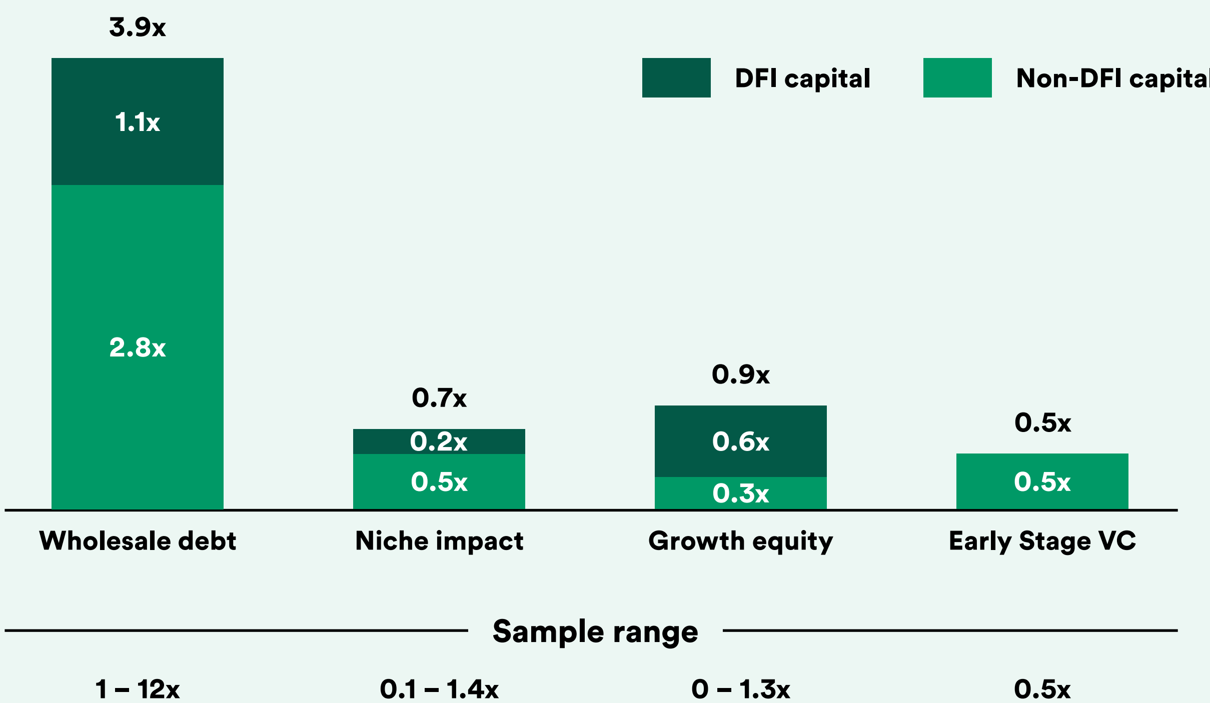
Investor value add

Concessional investors consider not only the impact of the fund at the investee level but also the investors' specific role during the fundraising processes. Priorities depend on investor profile, as they respond to the characteristics and constraints of their capital.

INVESTOR PROFILE	TYPES OF INVESTORS	PRIORITIES
Positive absolute returns	DFIs Commercial investors	DFIs are government-backed financial institutions with both a commercial and development mandate, aiming to generate financial returns with their investments, albeit lower than what institutional investors would demand for that level of risk. They achieve these objectives by managing certain parameters like annual subsidy budgets or risk limits within their portfolio. When supporting agri-SME funds, DFIs often act as senior debt investors and make sizeable contributions. For this reason, their presence is critical for the funds' scale, but their limited appetite for risk often requires protection by junior investors in order to participate. In many cases, their risk tolerance may not be much different than commercial investors. These investors prioritize investments in funds with significant additionality potential at the agri-SME level, as long as the risk of their investment is low and the opportunity generates a positive spread over the rate. They are normally interested in using risk mitigation levers that may compromise the depth of the additionality generated.
Capital preservation	Most philanthropies	Many private endowments of capital (i.e., philanthropies or family offices) look to maximize impact while preserving their capital base. With flexible capital, capital preservation-focused investors seek opportunities to fill critical funding gaps left by other capital types. While they can sometimes forgo upside, they have limited risk appetite – capital losses can diminish their capital base and limit their ability to generate impact in the long run. Ticket sizes are normally smaller than DFIs.
Grant/loss absorption	Bilateral agencies Some philanthropies	Bilateral agencies (or "donors") and some philanthropies provide high-risk capital in the form of grants. By anchoring or sponsoring investment funds, these institutions play a critical role in fundraising efforts. However, they have to weigh the public benefit of grants that could be used for other causes and typically have limited allocations for private sector investment. Thus, it is essential to optimize this scarce capital for maximum impact in an investment setting. Investors in this category typically aim for maximum impact at the agri-SME level and often want capital leverage (i.e., mobilization of additional capital) as well. They often take junior positions with greater risk and sometimes even forgo upside potential to make senior tranches more attractive to investors. Their challenge is to prioritize opportunities to optimize their limited budget for impact generation. Anchor investors normally fall within this category, providing early, high-risk capital to establish fund viability, and attract other investors.

Wholesale debt funds provide the highest financial additionality, both of DFI and non-DFI capital, being the only archetype in which institutional investors participate extensively. In our sample, wholesale debt funds (N=5), have an average size of ~$130m, and a leverage ratio of 3.9x. In other words, $1 of concessional capital unlocked an additional $3.9 of senior capital, of which $2.8 is non-DFI capital (see figure 5).

Figure 5: Capital mobilization of first-loss capital, by archetype (N=15)



Small sample size in equity funds (N=2 for growth equity; N=1 for VC funds) may limit comparability.

Higher-risk strategies find it harder to mobilize and blend capital effectively. In our sample, the average size of growth equity funds is ~$100m, and of niche impact funds is ~$35m, with leverage ratios of 0.7-0.8x (leveraging DFIs and also foundations and other sub-commercial investors). Furthermore, in our sample, 3 out of 6 equity funds do not have a tranched structure because they are 100% concessional. While DFIs have funded growth equity funds often with strong senior protection, they are typically hesitant to support early-stage VC funds due to the small size and high-risk.

This demonstrates the high capital leverage potential of lower-risk strategies on the mobilization of external investment.

ECO.BUSINESS FUND / SUB-SAHARAN AFRICA SUB-FUND*

Using low-risk strategies to drive capital mobilization

<table>
<tr><th colspan="4">FUND CHARACTERISTICS</th></tr>
<tr><td>Fund manager</td><td>Finance in Motion</td><td rowspan="3">Impact theme</td><td rowspan="3">Support business and consumption practices that contribute to biodiversity conservation, to the sustainable use of natural resources, and to mitigate and adapt to climate change.</td></tr>
<tr><td>Archetype</td><td>Wholesale debt fund</td></tr>
<tr><td>Type</td><td>Evergreen, launched in 2020</td></tr>
<tr><td>AUM* & Stage</td><td>USD 129 m as of the end of 2023 for the sub-Saharan Africa sub-fund; investing</td><td rowspan="3">Capital structure*</td><td rowspan="3">Equity
Junior: USD 68m
Senior: USD 30m
Debt
Junior: USD 20m
Senior: USD 6m</td></tr>
<tr><td>Instruments</td><td>Debt, hard currency (USD)
Intermediation strategy (~90%, financial intermediaries) and direct investments (~10%, producers, commodity buyers or aggregators)</td></tr>
<tr><td>Ticket size</td><td>USD 10m to USD 35m</td></tr>
<tr><td>Geography</td><td>Sub-Saharan Africa</td><td>Website</td><td>www.ecobusiness.fund</td></tr>
</table>

The eco.business Fund Sub-Saharan Africa sub-fund was established to promote biodiversity conservation, sustainable resource use, and climate action in key ecological regions across Sub-Saharan Africa. It provides debt financing and technical assistance to financial institutions and businesses in sectors like agriculture, aquaculture and fishery, forestry, and sustainable tourism that are implementing environmentally sustainable practices. Due to the perceived risk of conservation and climate investments in these regions, commercial capital is often scarce. To attract private investors, the eco.business Fund employs a combination of risk mitigation and return-enhancement features to create an appealing risk/return profile.

- **Intermediated investment strategy:** The fund allocates 90% of its investments to financial intermediaries, reserving a portion of its capital for high-impact direct investments. By primarily investing through intermediaries, the eco.business Fund diversifies risk across a broad portfolio while leveraging local expertise and collection infrastructure, reducing default risk. This intermediation strategy not only lowers the fund's overall risk but also demonstrates to local financial institutions that investing in conservation and climate adaptation is feasible and profitable, potentially motivating them to allocate their own capital to such initiatives.
- **First-loss protection:** To further reduce risk for senior investors, the fund employs a substantial ~55% junior equity layer, funded by KFW (on behalf of BMZ) and other concessional investors, offering senior investors significant downside protection against potential losses.
- **Return enhancement:** junior equity investors have their upside capped, with a part of their returns accruing to senior investors.

By employing a lower-risk, intermediated investment strategy alongside robust risk mitigation and return-enhancement features, the eco.business Fund successfully raised over USD 26m* for climate adaptation and conservation from professional commercial investors who might have otherwise felt the sector was too risky.

Notes: *The eco-business Fund is composed of two separate sub-funds: one for Africa and one for LATAM & the Caribbean. The figures provided here are specific to the Africa sub-fund only.

Sources: Fund website (Accessed November 2024), eco.business Fund 2023 impact report, and other public information

Fund pathway and future need for concessional capital

Some fund strategies needing concessional capital have the potential to become commercially sustainable; others, however, will only be viable with extended support from concessional capital. Interviews revealed that understanding the fund strategy pathway is important for investors who view subsidies as temporary support to fix a specific market failure.

Assessing the pathway to financial sustainability should be part of the investors' due diligence process, fund data and interviews show that small agri-SME funds, **typically those under ~$50 million are likely to depend on subsidies indefinitely.** These funds provide direct, hands-on investments to early-stage enterprises with smaller ticket sizes (under $500k). The small size of the fund and its investments make it hard to cover operational costs with a 2% management fee. A higher fee, however, would likely erode the investors' returns potential. Also, the inherent higher risk of the market limits their prospects of profitability. Their high-impact focus makes it difficult for them to transition away from the markets they serve and, thus, may require ongoing concessional support. Only high-yielding strategies with controlled risks could become commercial under this model.

On the other hand, some fund strategies have the potential to reduce their dependency on concessional capital over time. Larger funds, targeting more established companies with bigger ticket sizes, and in the more stable parts of the value chains may eventually attract commercial investors by demonstrating a track record and scaling their operations.

AGDEVCO & SIF 1

Highlighting two distinct pathways for financial sustainability

FUND CHARACTERISTICS			
AGDEVCO		**SIF I**	
Fund manager	AgDevCo	**Fund manager**	Match Maker Fund Management Ltd
Archetype	Growth Equity	**Archetype**	Niche Impact Debt Fund
Type	Evergreen; 1st close in 2010	**Type**	Closed-end (10 years), launched in 2014
AUM & Stage	USD 280m; investing/fundraising	**AUM & Stage**	USD ~5m; investing/fundraising
Instruments	Mostly mezzanine and QE/equity; also, long-term debt and working capital financing	**Instruments**	Debt, local currency (TZS)
Ticket size	USD 3-15m	**Ticket size**	USD 50,000 to USD 500,000
Geography	Sub-Saharan Africa	**Geography**	Tanzania (100%)
Impact theme	Providing growth capital agri-SMEs engaging SHFs to improve livelihoods, promote economic development, and enhance food security	**Impact theme**	Supporting MSMEs that directly benefit SHFs, fostering economic growth and resilience for rural communities
Capital structure	**Equity** **Junior:** USD 313m endowment, akin to 1st loss capital (FCDO) **Senior:** USD 70m preference shares (DFIs) **Debt** USD 20m concessional debt (DFIs) Investment capital not fully drawn	**Capital structure**	**Equity (3 classes)** **Class A:** EUR 680k; 1st Loss Equity (HIVOS) **Class B:** EUR 900k; 2nd Junior Equity (CORDAID and CFC) **Class C:** EUR 2.845M; Senior Equity (private investors) **Debt** EUR 625k; Senior Debt (CORDAID, private investor)
Website	www.agdevco.com	**Website**	www.smeimpactfund.com

Introduction

AgDevCo and the SME Impact Fund (SIF) represent two distinct approaches to generating impact, featuring different structural characteristics in terms of i) target beneficiaries and impact thesis, ii) fund size and ticket sizes, and iii) underlying fund economics. They consequently demonstrate distinct pathways to sustainability, with their concessionality needs determined by their overall role in the market and impact objectives.

About AgDevCo

AgDevCo is a USD 280m investment vehicle established in 2010 by the UK Foreign, Commonwealth and Development Office (FCDO), formerly the UK Department for International Development (DFID), and other development organizations. It was designed to provide long-term, flexible capital to small, early-stage agribusinesses in Sub-Saharan Africa.

What distinguishes AgDevCo is its successful transition from a model requiring significant concessional funding to one reaching financial self-sufficiency.

AgDevCo's pathway to financial sustainability

AgDevCo's initial strategy centered on providing debt (and some equity) to small early-stage agribusinesses. While highly additional, this approach presented inherent challenges to achieve financial sustainability: smaller companies tend to be riskier, and a strategy deploying small ticket sizes has higher transaction costs, on a relative basis, and exits were challenging. Recognizing the need for a more sustainable model, AgDevCo shifted its investment approach in 2017 to deliver impact at scale. This shift involved two key changes: 1) increasing ticket sizes and targeting larger companies, and 2) incorporating mezzanine financing into its portfolio. On the back of this strategic shift, in 2022 AgDevCo raised ~$90m of capital from DFIs (British International Investment, Norfund, and the United States Development Finance Corporation), ranking senior to the original FCDO endowment. AgDevCo is currently raising additional capital on the same terms, with an announcement expected in Q1 2025.

This strategic pivot into a lower-risk strategy allowed AgDevCo to deliver impact at scale, operate more sustainably, and attract capital from commercial DFIs, but limits its ability to provide early-stage capital that nascent SMEs critically need, as it did under its previous strategy, shifting as well the fund's additionality profile. Understanding this need for growth capital, AgDevCo Ventures was recently established with additional first-loss equity capital from FCDO to provide smaller mezzanine investments (£0.75-2.5m) in early-stage agribusinesses, initially in East Africa.

About SME Impact Fund (SIF I)

The SIF is a ~$5 million investment fund designed to provide loans for working capital and capital expenses to MSMEs directly working with smallholder farmers. The fund addresses investment gaps by offering smaller ticket sizes, ranging from $50,000 to $500,000 in local currency. Due to the smaller ticket sizes, the fund's high operating costs make a traditional management fee of around 2% unsustainable. That, coupled with FX losses stemming from local currency lending, limits the fund's financial sustainability and return expectations. Despite these challenges, SIF creates significant impact with strong financial additionality, by providing loans that enable small businesses to grow—an area currently underserved by the market. This impact is crucial for developing a robust ecosystem of agri-MSMEs, driving demand for agriculture in the region, and fostering a thriving economy in many rural areas of Tanzania.

SIF's pathway to financial sustainability

SIF's theory of change centers on providing the small ticket sizes that rural enterprises need to grow and scale. While this strategy generates significant impact and strong additionality, it will most likely always require some level of subsidy, due to the inherent costs of deploying and servicing small ticket sizes. In this case, Aceli Africa is addressing that need and providing the SME Impact Fund with incentives to continue offering sub-commercial loans. Future funds with a similar strategy may be able to achieve greater scale, potentially reducing implementation costs, but the focus on smaller ticket sizes will likely continue to necessitate subsidy. While full financial sustainability is unlikely, the subsidy is justified by the fund's high financial and non-financial additionality.

Sources: Fund websites (Accessed June 2024) and interviews with the fund managers

Depth of impact

Depth of additionality refers to the extent and intensity an investment has on the improvement of financial and non-financial dimensions.

Lower-risk strategies generally attract a broader pool of investors, enabling the mobilization of more capital, particularly from commercially driven and more risk-averse investors. This contributes to 1) bridging the investment gap in aggregate, and 2) creating a track record, potentially reducing perceived risks and further paving the way for future investments in undercapitalized areas. However, lower-risk investment strategies normally prioritize established businesses and markets. While financial additionality may be significant, non-financial additionality can be compromised.

Higher-risk strategies generally mobilize lower amounts of capital, as seen in Figure 4, but they often have the potential to generate outsized impact compared to less risky strategies, by supporting 1) more vulnerable/harder-to-reach populations, 2) riskier segments (e.g., the production end of the value chain), and 3) more uncertain/innovative strategies aimed at seeding longer-term systems change.

The following characteristics of an investment strategy generate risk/impact trade-offs:

Delivery strategy	Direct investments allow the fund manager to select and directly engage with higher-impact enterprises; whereas investing through financial intermediaries makes it more difficult to understand the depth of engagement with enterprises.
Instrument	Equity/quasi-equity investing allows a deeper engagement with companies, allowing fund managers to influence business practices, strategic decisions, and operational improvements.
Market served	Funds targeting underserved or riskier sectors can achieve a deeper, more transformative impact, but normally carry greater investment risk.

KAMPANI

Creating deep impact through a high-risk, patient investment strategy

<table>
<tr><th colspan="4">FUND CHARACTERISTICS</th></tr>
<tr><td>**Fund manager**</td><td>Self-managed</td><td rowspan="3">**Impact theme**</td><td rowspan="3">Provide patient growth capital for small, capex-heavy investments to producer organizations and agri-SMEs in underserved markets (generally called the Missing Middle)</td></tr>
<tr><td>**Archetype**</td><td>Early-stage venture fund</td></tr>
<tr><td>**Type**</td><td>Evergreen, launched in 2015</td></tr>
<tr><td>**AUM* & Stage**</td><td>USD 15m as of December 2023; investing</td><td rowspan="3">**Capital structure**</td><td rowspan="3">**Grant**
USD 1m 1st loss tranche financed by the Belgian Government
Equity
60% Foundations and NGOs (University of Leuven, FTO Foundation, etc.)
40% Private Investors</td></tr>
<tr><td>**Instruments**</td><td>Uncollateralized subordinated debt, both hard and local currencies</td></tr>
<tr><td>**Ticket size**</td><td>USD 100,000 to USD 500,000</td></tr>
<tr><td>**Geography**</td><td>Sub-Saharan Africa and Latin America</td><td>**Website**</td><td>www.kampani.org</td></tr>
</table>

Kampani, an impact-first investor, seeks to improve the livelihoods of smallholder farmers and rural communities by providing patient growth capital to farmer cooperatives and agri-SMEs with capital-intensive financing needs. By providing smaller investments with longer tenors (up to 10 years) and more flexible terms (uncollateralized subordinated debt), Kampani delivers financial products tailored to the unique needs of rural enterprises and cooperatives. This approach enables these organizations to make essential capital investments that they need to grow - opportunities often overlooked by traditional banks due to the perceived risks.

Beyond financing, Kampani actively engages in the governance and operations of its investees, providing targeted in-house technical assistance to strengthen their capacity. By focusing on underserved agri-SMEs and farmer organizations, the fund delivers significant non-financial and financial additionality, fostering sector growth and eventually stimulating demand for larger-scale investments from traditional financiers.

However, to achieve this deep impact, Kampani is prepared to take on considerable risk. However, Kampani has suffered few losses despite a track record of almost 10 years and 30 deals. Kampani relies on its unique multi-stakeholder approach, leveraging a network of mission-aligned partners who reduce risks and costs throughout the investment process. NGO shareholders generate deal flow by combining technical expertise with local knowledge and filter promising deals, significantly lowering Kampani's sourcing costs and risks while enhancing its impact. Kampani aims to preserve investors' capital and may not be suitable for low risk-tolerant investors.

By combining patient, tailored financing with deep engagement, Kampani achieves high-impact attribution, with tangible outcomes such as improved livelihoods, job creation, and community development. Its model not only drives transformative change in underserved communities but also serves as a blueprint for how patient capital can unlock growth and opportunity in high-risk, high-impact sectors.

Sources: Fund website (accessed June 2024) and interview with the fund manager

Pace of impact generation

Investment strategies produce impact over varying timeframes, requiring concessional investors to align their objectives with their chosen timelines. Short-term debt strategies provide quicker, more recognizable impacts as well as continuous visibility on their investment. However, while effective for maintaining operations, these strategies are less conducive to driving transformational change. In contrast, impacts from equity investments unfold over a longer horizon. Though they involve greater risk, these investments can lead to deeper impact outcomes by fostering company growth and sustainable operations.

5. RECOMMENDATIONS

These recommendations are intended to support concessional investors in refining their subsidy allocation process in alignment with their impact goals.

1 To optimize concessionality, investors should integrate learning agendas into their investments and increasingly rely on data-driven methodologies

Subsidies are scarce, drawn from limited taxpayer funds or public budgets, and must therefore be allocated judiciously to ensure they are deployed where they can drive substantial value. As discussed earlier in this report, specific segments of agri-SME-focused funds will need continuous subsidy to operate, given the structural challenges to achieve financial sustainability, and justified by high-impact outcomes on local markets and communities. Concessional capital is also key to bridging market failures, allowing the emergence of new innovative and local investment vehicles, and creates the opportunity for public good through shared learning.

Data-driven capital allocation is the cornerstone of a more efficient use of subsidies. Interviews highlighted that ex-post analysis is typically lacking in concessional investors' processes, and there was limited transparency on the effectiveness of their investments among industry stakeholders. The objective of concessional capital in this context is two-fold: first, to drive systemic change by addressing market failures and information asymmetries that hinder investment in agri-SMEs; and second, to mobilize desperately needed capital for these enterprises. To achieve these objectives, a specific data and learning agenda is crucial – it would generate insights from past investments, allowing for a better understanding of effective and ineffective practices, contributing to reducing information asymmetry.

Systematizing this data-driven approach implies: 1) aligning at the industry level on data collection and generalizing ex-post assessment of the financial and impact performance of funds benefiting from concessional capital, to properly evaluate its effectiveness, and 2) sharing outcomes and insights of ex-post assessment among industry participants.

While it is important to acknowledge the sensitivity of some of the data, fund managers benefiting from public capital should be required to contribute to a learning agenda and follow transparency requirements. By sharing data, they can actively help substantiate the challenges they face, providing evidence that can drive new investment strategies and address the agri-SME market gap. Ultimately, these learnings can enhance investment effectiveness and contribute to more targeted solutions for the agricultural sector.

This is particularly true for debt funds, where increased data sharing can lead to a better understanding of potential risks, reducing information asymmetry, and enabling investors to more effectively link

the size of the junior tranche directly to the fund's economics. In turn, this approach reduces the risk of over-committing and makes deploying concessional capital more efficient.

To this end, building on its long-term perspective and learning agenda, the FASA Fund can be a helpful platform to move the industry knowledge further, by collecting ex-ante and ex-post data, analyzing it, and extracting learnings from a substantial sample of agri-focused investment funds.

Another relevant initiative is the Catalytic Capital Framework by the Agri-SME Learning Collective (ASLC), which aims to help concessional funders investing in agri-SMEs assess capital additionality and impact, and the work of the Global Donor Platform for Rural Development (GDPRD), dedicated to sustainable and blended finance for food systems.

Based on our analysis for this report, we feel a robust learning agenda for the use of concessional capital should focus on the following questions:

i. Unpacking fund economics

- What are the average returns of different fund strategies? How do the different components of fund economics compare across fund strategies (i.e., fund income, operating costs and services provided, portfolio losses)?

- Can other sources of subsidy be levered or aligned to help improve fund operations and economics (i.e., having private sector development programs be more intentional about delivering pre-investment TA)?

- What strategies are (or can be) commercially sustainable and which ones will require sustained subsidy?

- How are FMs being compensated? How is variable compensation being structured? What are the hurdle rates used by investment strategy? What strategies allow FMs to generate carry?

ii. Analyzing additionality

- What are the minimum core impact metrics for agri-SME investing that all funds should report on?

- What are the categories/segments of beneficiaries reached by different funds?

iii. Determining the appropriate level and uses of subsidy

- How much concessionality is required to serve different beneficiaries? It may be necessary to gather a nuanced understanding of: i) the use of funds by the organization, ii) the stage of the organization and its operational capabilities, iii) the organization's capital structure and liquidity position, and iv) the organization's operating environment.

- When sustained subsidy is needed, what form of subsidy is most effective (i.e., first-loss capital, incentive payments)?

- How is the use of concessional capital influencing fund managers in the implementation of their investment strategies?

- What is the relationship between the beneficiary of the concessional capital (e.g., FMs, senior investors, investees) and the outcomes generated?

- To what extent are concessional capital providers influencing the fund's investment strategy, and the fund's risk-return and impact generation profile?

While concessional capital can mitigate perceived risk, it does not inherently improve investors' understanding of underlying risks or address information asymmetry. For that reason, it is also key to work towards addressing information asymmetry and perceived risk of agri-SME investing by establishing a baseline understanding of financial and operational performance for agri-SMEs. Timely and relevant data collection and analysis at the investee level can improve visibility on key metrics and reduce investors' risk perception.

2 Stakeholders across the industry — donors, other investors, and fund managers — would benefit from more transparency to ensure better collaboration

Further transparency around concessional investors' strategies and additionality objectives would facilitate the effective deployment of concessional capital. Interviews revealed that, while many investors have well-defined investment requirements, strategies, and in the case of donors, budget cycles, these are not always clear to other stakeholders. This results in missed opportunities for fund managers and investors. **Interviews revealed that the most effective investors actively signal their role in the market, including their risk/return profile, preferences, and additionality objectives—and seek out partners who can complement their strategy.** This focus on transparency ensures that all parties have a clear understanding of expectations and outcomes, ultimately driving better alignment and accountability across the sector.

Finally, deeper collaboration is crucial for advancing industry knowledge, addressing limited data and fragmented efforts. As mentioned before, transparency is the foundation for better decision-making, but collaboration goes a step further by creating shared spaces for learning and innovation. Industry platforms such as the Agri-SME Learning Collective, Convergence, the Catalytic Capital Consortium, the Collaborative for Frontier Finance, or the GDPRD are encouraging collaborative learning and mobilizing industry participants towards standardizing and sharing data and best practices – however, these are initial steps and more progress is necessary to advance the industry.

3 Concessional investors should further optimize the use of concessional capital by aligning first-loss capital provision with other tools and sources of capital to maximize investment outcomes and reduce risk

Beyond first-loss capital, investors can leverage alternative uses of capital and engage with fund managers to enhance their performance and improve investment outcomes.

Providing design grants to support fund development and learning agendas: by offering design-stage grants, concessional investors can actively shape the creation of investment vehicles that align with their impact objectives. These grants help fund managers develop robust investment strategies, build pipeline, and ensure operational readiness, while concessional investors position themselves to anchor these funds later. This approach increases the likelihood of successful fundraising while ensuring that investors' impact objectives are embedded from the start.

Additionally, and as discussed in the key learnings section, concessional investors can improve the accessibility and inclusiveness of design grants; by lowering entry requirements, streamlining application processes, and reducing administrative burdens. It would make these grants more accessible to a wider range of fund managers, including smaller and first-time managers, enabling them to focus on essential groundwork with less financial constraints.

Systematizing TA at fund manager and agri-SME levels

- **Integrating TA with investment capital:** concessional investors should continue to support fund managers to deliver TA, embedding it within the investment strategy. This strengthens the ability of fund managers to improve the investment readiness of strong prospects and support investees, often mitigating identified risks and improving the organization's operational and financial performance.

- **Supporting impact management and learning:** concessional investors can enhance fund performance by allocating sufficient resources to develop robust MEL systems, enabling fund managers to document investment outcomes and best practices, and to align with investor expectations.

- **Considering fund manager TA:** investors should consider supporting fund managers with TA to improve their deal execution and portfolio management. This is especially important for smaller fund managers aiming to move towards less concessional structures in subsequent funds. Investors, when they have a specific skill set, can support managers in developing specialized analysis and management tools, helping with the execution of the investment strategy.

- **Ensuring sustainability of TA:** access to TA funding needs to be sustainable, especially for open-ended funds. Periodic fundraising distracts fund managers, and the lack of visibility in funding hinders long-term or sizeable projects.

Engaging proactively with fund managers and other investors: concessional investors can generally support the investment community by engaging in coordination and collaboration efforts. For example, concessional investors can leverage their networks and connect fund managers with other investors, TA partners, and/or specialized knowledge professionals. These connections could help de-risk investments by providing valuable resources and insights, ultimately improving investment performance.

Bilateral agencies and other donors have the opportunity to more intentionally leverage the private sector development activities they fund, designing interventions that capitalize on synergies between investment initiatives and direct company support (i.e., on pipeline development, targeted trainings, and investment in human capital).

MCE EMPOWERING SUSTAINABLE AGRICULTURE (MESA) FUND

How design grants are crucial to the success of a new fund concept

FUND CHARACTERISTICS			
Fund manager	MCE Social Capital	**Impact theme**	Focus on sustainable agriculture and farmer organizations, to scale economic opportunities, enhance climate resilience, and support women throughout the agricultural sector.
Archetype	Niche impact debt fund		
Type	Closed-end (9 years), launched in 2023		
AUM*	USD 42m	**Capital structure**	**Debt** **Junior subordinate:** USD 1m committed by MCE Capital, funded by philanthropies **Senior subordinated:** USD 14m committed by Ceniarth, Impact Assets, and others **Senior:** USD 27 committed by DFC, FMO, Visa Foundation, and others
Instruments	Debt, hard currency (USD) Both intermediation and direct investment strategies		
Ticket size	USD 300,000 to 3m		
Geography	Sub-Saharan Africa and Latin America	**Website**	www.mcesocap.org

In 2021, MCE Social Capital (MCE) began the development of the MESA Fund, a debt fund aimed at investing in sustainable agriculture to address the significant financing gap faced by smallholder farmers. Despite its strong track record as an impact investor, MCE had traditionally relied on guarantees from philanthropic organizations to raise capital for on-lending from its balance sheet. The MESA Fund marked a transformative shift in MCE's model - its first effort to create a scalable, closed-end fund structure designed to diversify its funding sources and attract institutional investors.

To achieve this, MCE secured a $200,000 design grant from the United States Agency for International Development (USAID), which played a pivotal role in covering the fund's initial setup costs. These costs—such as fund structuring, legal consultations, and financial modeling—are critical for the fund's development but are rarely covered upfront by investors. This gap in early-stage funding often presents a significant barrier for fund managers, particularly when developing new fund concepts, as they may lack the resources to finance the design phase before raising capital. In addition to capital, USAID provided invaluable non-financial assistance, including introductions to potential investors within its network and sector insights that were instrumental in refining the fund's strategy and execution.

The USAID design grant provided MCE with essential resources to develop the fund concept and served as a credibility signal to attract investors. This "stamp of approval" facilitated early engagement with anchor investors, leading to MESA's successful first close of $20 million, including $10 million in commitments from US DFC, Ceniarth, and others. The MESA fund's development highlights the importance of early-stage catalytic funding in launching innovative investment strategies, mitigating risks, and scaling impact, demonstrating how strategic funding at the design phase can unlock broader investment and create lasting impact.

Sources: Fund website (Accessed June 2024), MCE blog post, and interview with the fund manager

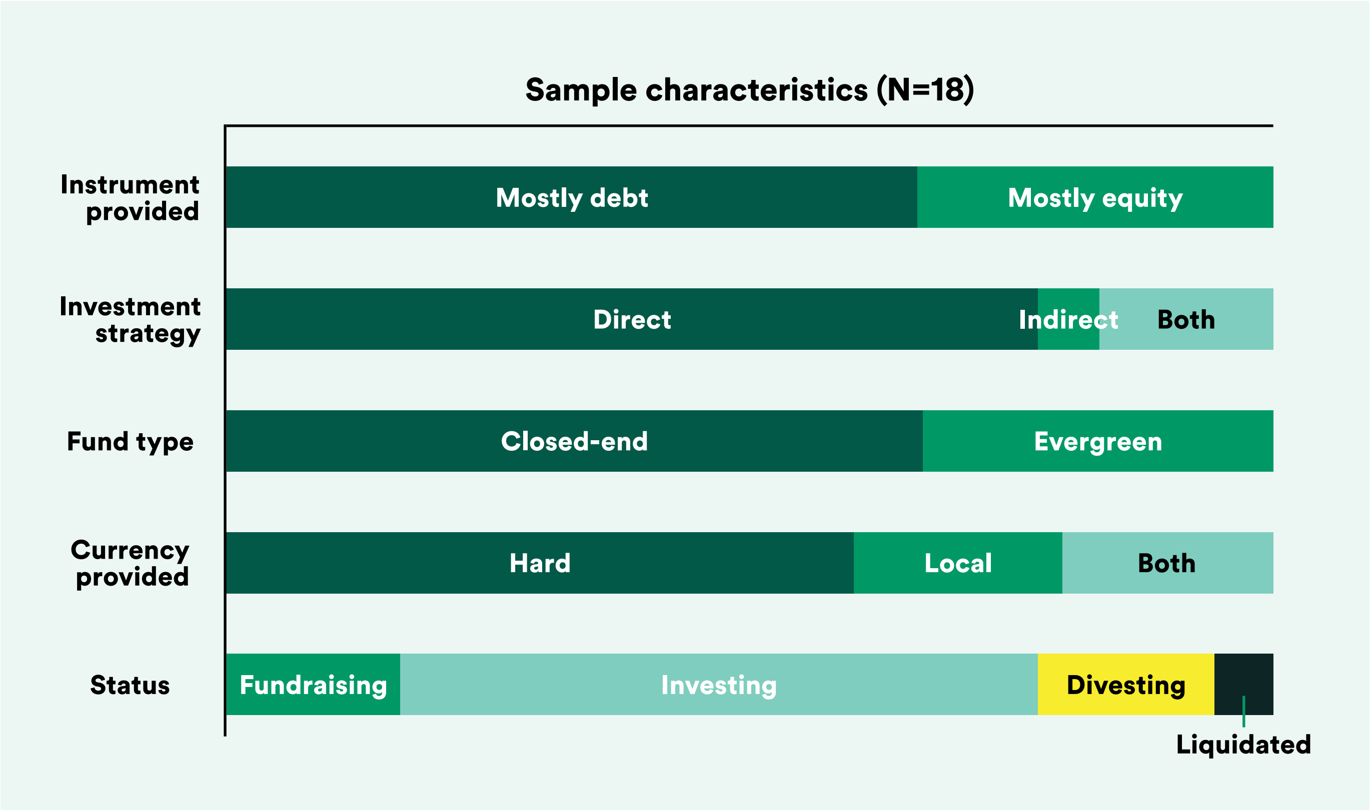
6. ANNEXES

ANNEX 1 – FUND SELECTION CRITERIA

Profiled funds aimed to balance different uses of concessional capital, investment strategies, and cycles. ISF Advisors has applied a set of diversification criteria to ensure the sample was representative of different strategies. Diversification criteria include:

1. **Subsidy characteristics: aim to balance blending archetypes and amount of subsidy used**
2. **Fund characteristics: aim to balance geographic exposure, sector of focus, instruments provided, and market segment served**
3. **Fund design validation: aim to include funds in different stages of the investment cycle in order to allow initial design validation**

Figure 4: Sample distribution across main selection criteria



DIVERSIFICATION CRITERIA		
	CRITERIA	**DEFINITION AND CONSIDERATIONS**
Subsidy characteristics	Blending archetype	Aim to balance representation of the 4 blending archetypes as well as diversity on the resulting bundles
	Amount of subsidy	Aim to include funds using varying amounts of subsidy Aim to include funds that have raised a second fund or additional capital on the back of a successful pilot/1st (smaller) fund, to assess the demonstration effect
Fund characteristics	Geography	Aim to include funds with narrow and broad geographic scopes and investing in markets with varying degrees of development
	Sector	Most funds had a dedicated focus on agriculture; a small number were multisector with significant exposure to agriculture
	Instrument	Aim for diversity on instruments provided, as that speaks to different risk-return profiles
	Market segment	Aim for diversity of strategies serving different market segments, based on company profile (i.e., early-stage, early growth, mature companies), and direct vs. intermediation strategy (or hybrid)
Fund design validation	Stage in investment cycle	To understand performance, funds that have a history of investment (e.g., either have been liquidated or for open-ended funds, that have 5+ years of investing) allow for validation of the design, by looking at the subsidy actually used as well as the impact generated Sample can be complemented with more recent funds, to validate market evolution

ANNEX 2 – DATA POINTS COLLECTED

Answering research questions requires thorough data collection from agri-SME investment funds. The following data points were communicated to the 18 profiled funds for data collection. Due to varying degrees of disclosure by the funds, data collection within the sample is not exhaustive and may present gaps.

GENERAL INFORMATION	EX-ANTE: INITIAL DESIGN		EX-POST: INVESTMENT RESULTS
	FUND DESIGN CHARACTERISTICS	BLENDING APPROACH & IMPACT CASE	
Fund Name Geographic focus Sectoral/ commodity focus Term structure Maturity & investment period Fund size Fund currency Year launched First close timeframe Previous FM's experience in agri-SME investments Target LPs, by type Fund's return profile; target net IRR	**Investment strategy** Instrument(s) provided and portfolio weights Ticket size Currency Interest rate charged Tenor Target investee: size, growth stage, position in value chain Target countries and sectors Partnerships with 3rd parties Cost of delivery Expected loss rates (& net interest income) Management fees, carried interest & impact-linked compensation **Pain points and mitigants** Main risks, and mitigants, as disclosed to investors (i.e., capital loss, deal flow, market, country, liquidity, currency, operational) Other pain points identified Priority pain points requiring concessional capital at each stage of the fund's development (design, launch, scale-up)	**Capital structure and use of concessional capital** Blending archetype(s) used (i.e., subsidy allocation): investment capital, TA, guarantees, design grant Amount of concessional capital in the capital structure Instrument of concessional capital in cap structure (e.g., junior equity, grant) Concessional capital providers (amount and instrument) Amount of TA raised, uses of TA (pre-/post-investment, FM, or investee) Amount of design grants, and uses Characteristics of guarantees used **Impact potential (social/ environmental returns & market impact)** Impact themes Theory of change Primary KPIs and targets Approach and measurement of the fund's additionality Broad market impacts	Actual uses of concessionality (i.e., design grants, TA capital losses absorbed by junior equity) Actual net returns and deviations compared to initial assumptions Actual impact generated and deviations compared to initial assumptions Portfolio data: total amount of capital deployed, portfolio weights of instrument provided, geographical and sectorial breakdown, overhead cost per year

ANNEX 3 – LIST OF INTERVIEWS

INSTITUTION	CONTACT
DFIS	
DFC	Patrick Starr
FMO	Hans Bogaard Robert Darcy
IFC	Amanda Cotterman
KfW	Stefan Hirche
FOUNDATIONS/FAMILY OFFICES	
Ceniarth	Harry Davies
Small Foundation	Karina Wong
FUND MANAGERS	
Acumen (ARAF)	Rebecca Mincy
AgDevCo	Chris Isaacs
Bamboo Capital	Susan Tirop
Finance in Motion	Lachlan Cameron
GAWA Capital (Huruma Fund)	Luca Torre
IDH Investment Management	Roel Messie
Incofin IM	Lia Gonzalez Nury Barreto
I&P	Hugues Vincent Genod
Kampani	Mauricio Barocio
LDNF	Johann Fourgeaud
MCE Social Capital (MESA Fund)	Camilla Nestor
Mennonite Economic Development Associates (Mastercard Foundation Africa Growth Fund)	Samuel Akyianu
Pearl Capital Partners	Wanjohi Ndagu
ResponsAbility (RA Fund)	Harriett Jackson
Sahel Capital	Tosin Ojo
SME Impact Fund	Allert Mentik
Sinergi Burkina	Job Zongo
OTHER KEY INFORMANTS	
Big Valley GmbH	Mauricio M Benitez
Catalytic Capital Consortium (C3)	Harvey Koh

ANNEX 4 – ADDITIONALITY FRAMEWORK

ISF developed a practical framework to further unpack the multi-dimensions of additionality, based on the investors' decision-making process when assessing a fund's additionality. This additionality assessment framework aims to answer some of the key research questions:

- What practical frameworks do concessional investors use during their decision-making process for the allocation of concessional capital?
- How do investors use the different kinds of existing funds/transactions (e.g., direct vs intermediated, equity/debt, fund size, transaction size, etc.) to achieve specific impact objectives?
- How should concessional investors weigh the trade-offs for allocating their concessional capital to investment funds in different ways in order to align with development objectives and/or within different agricultural market contexts?

Additionality assessment framework

ADDITIONALITY		AGRI-SME LEVEL	FUND LEVEL
FINANCIAL	Capital mobilization	Concessional capital unlocks additional resources that are deployed in the system to support company growth **Note: potential for subsequent capital raising has not been considered, neither the quantities of the capital**	Investor provides capital that (i) enables a specific fund to reach its first close, which wouldn't have been possible without the investment, and/or (ii) allows a fund to attract more commercial capital than it otherwise could have
NON-FINANCIAL	**Economic, environmental & social development**	Fund supports company value creation that trickles down to company stakeholders (i.e. employees, clients, suppliers), through the provision of capital and TA	Investor provides specific knowledge & tools that helps the fund achieve a specific objective Investor can connect the fund to the broader ecosystem (i.e., PSD programs)
	System change	Fund (i) promotes knowledge sharing/innovation and/or (ii) supports nascent areas (geography, VCs, etc.) with the aim of building up specific markets. Fund aims to influence policy/regulation	Investor aims to signal to the broader market that a specific impact or objective or innovative model is viable and worth pursuing

METHODOLOGICAL CHALLENGES

1. **Comparability:** comparing depth of impact across funds that can be challenging

   Output vs. outcome: data available is on reach (outputs); outcome data is less standardized or comparable

2. **Sample size:** aggregating impact per archetype can be misleading given limited sample size

Note: throughout the document, the word "impact" is used interchangeably with "additionality" and refers to financial and non-financial additionality.

ANNEX 5 – BIBLIOGRAPHY

AfDB, ADB, AIIB, EEBRD, EDFI, EIB, IDB, ICD, IFC. "DFI Working Group on Blended Concessional Finance for Private Sector Projects, Joint Report March 2023 Update." AfDB, ADB, AIIB, EEBRD, EDFI, EIB, IDB, ICD, IFC, March 2023. https://www.eib.org/attachments/2022-dfi-bcf-working-group-joint-report.pdf.

"DFI Working Group on Working Concessional Finance for Private Sector Projects Summary Report October 2017," October 2017. https://www.eib.org/attachments/mdb_dfi_working_group_blended_concessional_finance_private_sector_summary_2017.pdf.

Catalytic Capital Consortium and Convergence. "How DFIs Deploy Catalytic Capital," March 2022.

Collaborative for Frontier Finance. "Africa Fund of Funds Platforms: Building the Small Business Finance Ecosystem," November 2023. https://static1.squarespace.com/static/59d679428dd0414c16f59855/t/65606aeb6290971bd143efb0/1700817674841/202311+CFF+African+Fund+of+Funds+Platforms+Report.pdf.

"Annual Loan Capital Provider Survey 2023: Small Business Finance in Africa and the Middle East," 2023. https://static1.squarespace.com/static/59d679428dd0414c16f59855/t/6540bc7cf4c8160e5bc97bf0/1698741389546/CFF+Annual+Local+Capital+Provider+Survey+2023.pdf.

Convergence. "Convergence Blended Finance Primer," n.d. https://www.convergence.finance/blended-finance#archetypes.

"Data Brief: Blended Finance & Agriculture." Convergence, May 2021. https://www.convergence.finance/api/file/5e0929743e578795f023c50a636035ba:1066ab014ff53ae3ca3b9056e0fa824ae9d4cb0190144bccda594810c53a219f81a0113b791ae1a8d309f3a7b320cb43fd9c3e03414e654583eca3a9fafde30f74a08e4b93331f2a6013d5a98d1b1f311e13d62a3dacf3d65ce88f8be7ce3b20e4342bc5823c3159ad29e569f251399624de9b27ac4c4137e198dfddc8cc4582dd6f78b8208f259059461fbf01d8b7dcc2dcfaf96c7fbf0f7fe5614f3a9c384de74ae8abb3aa03df3623e0a3c709131968ec8cb07d495c33adceb12d2e6377323290b0d64dbc1d22431e02462d620c1f.

"Data Brief: Blending with Technical Assistance." Convergence, September 2023. https://www.convergence.finance/api/file/44d295e993954fd02ab93c26b4411d19:f53feb69da15295ee1a000f6a56a4e5dbbea2f7bdb6ba052aa3b65b5892bcf2faedc4b5e7f97b86a2871f716f5ab01828c1470914fce826797b764c979046fa435758d6023b243e08301a264751c650d4f8cd658ab44a283ca757409add959b8aa723ad2f6dd74f69d9c080bf6f763a1595838e001988ad079655c45ccb657875e2e5f2f8db35af37446d56b737d95604ce1e748f53d01a7c3586de035c21fc0a7c4dee842d65cf7c8ebba95aac460e52988194d929acf9140b10525ac371afe.

“Evaluating the Impact of Blended Finance: Convergence’s Case Study Portfolio Revisited,” n.d. https://www.convergence.finance/resource/evaluating-the-impact-of-blended-finance-convergences-case-study-portfolio/view.

Convergence Blended Finance. “Best Practices for Donor Governments Engaging in Blended Finance,” 2023. https://www.convergence.finance/api/file/7afe6219c075d598a92b03af94d206dd:5f830bde346e2832e6ac913f75a90d29f4abe3aab256d2d7eec0bd25f76ede150da42f24df6a30063ade5cfc572d27b8758c5d00327dc126abe7e715b56d044405720d56d2d5c9b221f0c2ba91e1e44653ad0b20c9e6a080c145911821266ef09703be1df99125268865eeebde0b0d70046199b24c155a0bd755a40c5b9bccdfd8f42a5d4065375d1cee01ea515fb8a8f24a20ecf69d9536df11611acba4a449b9cf3e8d61cfbd9f19baf339d7ba6294cf3e7e2975929e0d3ff8bb1b47266aa9.

FSG. “Bending the Arc: How the Full Spectrum of Capital Can Enable Inclusive Growth in Agriculture,” January 2020. https://www.fsg.org/wp-content/uploads/2021/08/Bending-the-Arc.pdf.

Impact Investing Ghana, Ashesi University. “Catalytic Capital Investments in Ghanaian SMEs: Strategies, Hurdles and Outcomes,” October 2022. https://impactinvestinggh.org/download/catalytic-capital-investment-in-ghanaian-smes/?wpdmdl=78044&refresh=6595bca5559e51704311973.

I&P. “Using Catalytic Capital to Foster the Emergence of Africa Entrepreneurs in Underserved Markets,” October 2023. https://assets.ctfassets.net/4cgqlwde6qy0/6cHFL462jRhnkPDs7EUAhQ/5be712d5487b38e740f5b7271135223f/IP-C3-Full-Report.pdf.

“IPDEV2 Fund Evaluation”, September 2024, https://www.ietp.com/sites/default/files/IPDEV2%20Evaluation%20Summary%20Report.pdf.

ISF Advisors. “The State of the Agri-SME Sector - Bridging the Finance Gap.” FCDO, USAID, March 2022. https://isfadvisors.org/wp-content/uploads/2022/04/ISF_AgriSME-Finance-state-of-the-sector-report.pdf.

Maoz (Michael) Brown, Riya Kadam, and Katherine Klein. “Catalytic Capital in Impact Investing.” Wharton ESG Initiative, HBS, Chicago Booth, September 1, 2023. https://esg.wharton.upenn.edu/wp-content/uploads/2023/09/Catalytic-Capital-in-Impact-Investing-Forms-Features-and-Functions.pdf.

Matthieu Pegon. “Beyond Leverage Ratios: A Strategic Approach to Blended Finance.” IDB Invest, April 12, 2023. https://idbinvest.org/en/publications/beyond-leverage-ratios-strategic-approach-blended-finance.

OECD. “Blended Finance Principles Guidance,” September 17, 2020. https://one.oecd.org/document/DCD/DAC(2020)42/FINAL/En/pdf.

“Making Blended Finance Work for Agri-SMEs: Lessons Learned from Selected Case Studies,” May 2021. https://www.oecd.org/dac/financing-sustainable-development/blended-finance-principles/documents/Blended-Finance-in-Agriculture.pdf.

“Mobilising Institutional Investors for Financing Sustainable Development in Developing Countries: Emerging Evidence of Opportunities and Challenges,” 2021. https://www.oecd.org/dac/financing-sustainable-development/Mobilising-institutional-investors-for-financing-sustainable-development-final.pdf.

“OECD DAC Blended Finance Principle 2: Design Blended Finance to Increase the Mobilisation of Commercial Finance,” n.d. https://www.oecd.org/dac/financing-sustainable-development/blended-finance-principles/principle-2/Principle_2_Guidance_Note_and_Background.pdf.

Omidyar Network. “Across the Returns Continuum,” n.d. https://omidyar.com/wp-content/uploads/2020/09/Across-the-Returns-Continuum.pdf.

SAFIN. “Landscape Report: Blended Finance for Agriculture,” March 2019. https://www.convergence.finance/api/file/cabe0c781e3f0d0dfe1f1fc59df74b8d:ae29b7e0b507a5772e07209f5c078a00bd4a57b52e3d0059769ae0205ee49800f6c586e99422c7e79d10c93385311a198eb4faef0381cb3c803c6ad73409f885edb5d7ff382b741d4aef59497c1d30e7b01f1bd2dd8e2d556e5082c1ffbada70ed68f21ea091f5f4dc0eb286e94f969ebdadcff7b5d70c12a225847f93288053b2dfabfff7c625b3c47605fde9b043b0b073e00b5f47d4e91a530bd206ae7c02.

The World Bank. “What You Need to Know About Concessional Finance for Climate Action,” September 2021. https://www.worldbank.org/en/news/feature/2021/09/16/what-you-need-to-know-about-concessional-finance-for-climate-action#:~:text=What%20is%20concessional%20finance%3F,countries%20to%20accelerate%20development%20objectives.

Tideline. “Catalytic Capital: Unlocking More Investment and Impact,” 2019. https://tideline.com/wp-content/uploads/2020/11/Tideline_Catalytic-Capital_Unlocking-More-Investment-and-Impact_March-2019.pdf.

ISF