Initiative for Blended Finance at the University of Zurich

University of Zurich[UZH]

What's in it for the Entrepreneur?

An entrepreneurial perspective of catalytic capital and blended finance

Bjoern Struewer
Jed Emerson
Kirsten Andersen

Roots of Impact

BERTHA CENTRE
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Contents

Research Partners:

This report is the result of a collaboration between:

Initiative for Blended Finance at the University of Zurich - Bjoern Struewer, Jed Emerson and Taeun Kwon

Kirsten Andersen, PhD (independent research partner)

The Bertha Centre for Social Innovation and Entrepreneurship at University of Cape Town – Barry Panulo, Rowan Spazzoli and Kirsten Amsterdam.

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Foreword

Over recent years, the fields of impact investing and blended finance (using catalytic capital) have converged, gaining increased interest among a growing number of those providing capital in pursuit of various levels of financial return and diverse types of social and environmental impact. While promising on many fronts, much of the attention has been focused upon the stewards of capital—the impact investor, the public funder, the foundation executive— in various efforts to understand what motivates those providing (catalytic) capital, what metrics and understanding of performance is most relevant and what approaches resonate most with the goals they seek to achieve.

We both have talked many times in the past about how the impact investing scene risks moving away from its intended purpose, focusing too much internally. Maybe that was necessary in the beginning, but now investing with purpose should be focusing on these simple questions:

- What are we trying to achieve?
- Why are we doing all this; who is it all supposed to benefit?

If we prioritize positive impact on people and the planet, this change is not a side effect but the real performance measure. And we can't prioritize impact separately from the entrepreneurs to whom impact capital is deployed. However, the entrepreneur is absent from most discussions of impact investing, which raises some provocative questions:

- What advantages do they see in the practice of catalytic capital and blended finance?
- How do they feel they benefit from the development of this field?
- And what improvements would they like to see in the efforts of those who bring capital to the table in support of their good efforts?

These questions inspired our research with our goal being to learn more about the perspective of the "capital consumer" and the value they find in such structures as well as how the deployment of catalytic capital might be improved. In other words:

- Does catalytic capital deliver on its promise?
- Does it, in fact, catalyze?
- And what exactly makes it useful to help entrepreneurs deliver on their mission?

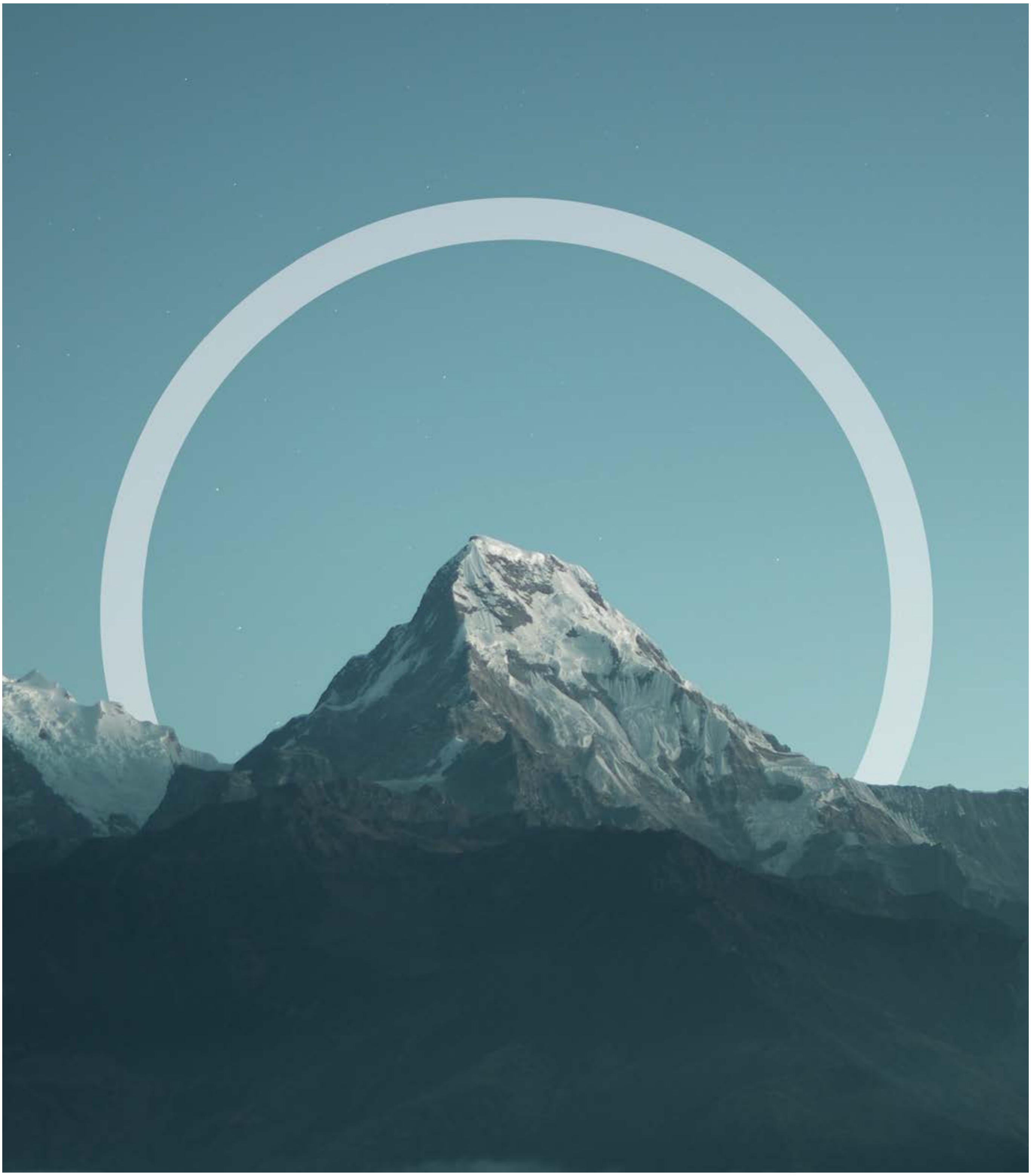
It was very inspiring to have in-depth conversations with entrepreneurs who create positive change with their breakthrough innovations. We learned much more than their perspective on catalytic capital and blended finance alone. We thank them for sharing their experiences, concerns, and courageous plans with us!

The two of us have known each other for many years, but we have never had the opportunity to work together. Collaborating on this research has proven a great pleasure and experience. But it was not just us. Our research was made possible by a global research team led by the incredible Kirsten Andersen, PhD. Everyone on that team did a fantastic job. We offer you our thanks as well.

Please read carefully what the entrepreneurs have to say, because they are the ones who make the difference. And for catalytic capital providers, do not just read what follows; please review our team's findings, draw your conclusions, and put these new insights into practice.

Bjoern Struewer and Jed Emerson

I. Executive Summary



Much research has been undertaken to guide the financing of the Sustainable Development Goals. This has focused heavily on the supply side, developing strategies and structures to guide capital providers as they–in addition to providing much needed investment–leverage limited philanthropic, impact-first, and development capital to generate positive impact and enable third-party investment. One such approach is **catalytic capital** which offers flexible terms (accepting disproportionate risk or concessionary returns, longer time horizons, more innovative investment structures) to create impact and attract additional capital to markets for impact. Catalytic capital can be invested on its own, or within a capital stack in the form of blended finance, which makes use of catalytic capital by structuring it in combination with other capital in funds, projects, and enterprises.

While the design of such strategies has generated guidance for investors, there has been significantly less attention paid to the capital user. The dearth of research means the field knows far less about the experience of catalytic capital and blended finance from the demand side's perspective. Enterprises are the vehicles through which capital is transformed into strategy and impact, and entrepreneurs—as the founders and stewards of these enterprises—represent a key perspective in this investment equation.

This study shifts the gaze on catalytic capital and blended finance, centering the entrepreneurial experience. By asking ***What's in it for the entrepreneur?*** We learn about what capital makes a difference for entrepreneurs, how they blend it with other capitals, and how these compare with providers' intentions for them. Through in-depth interviews with entrepreneurs representing various geographies and sectors, this study conveys what entrepreneurs value most during their financing journeys.

We find that entrepreneurs value the following:

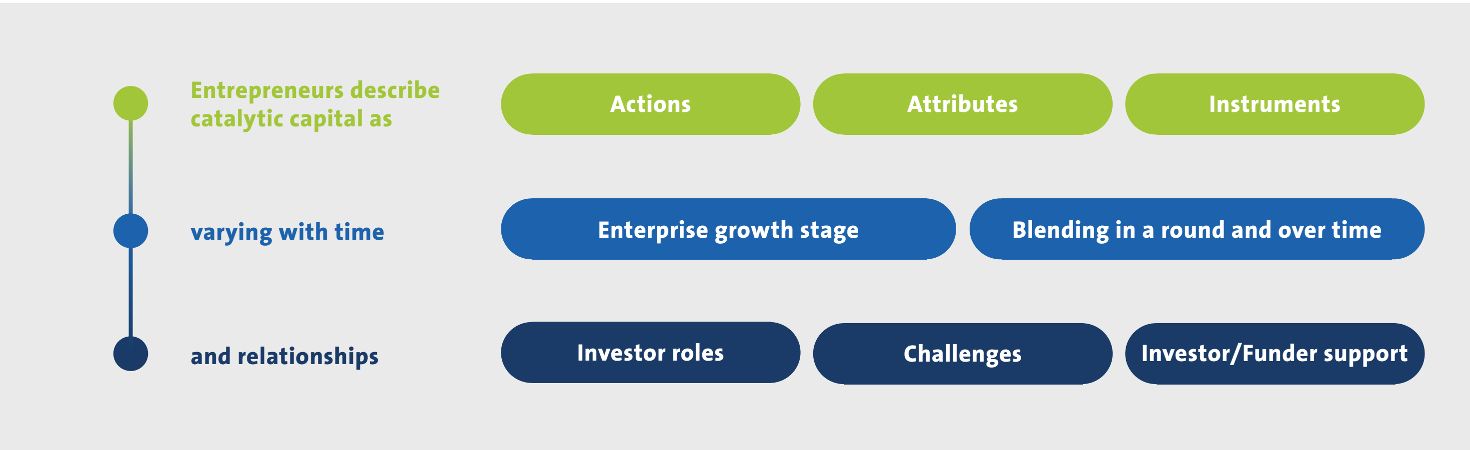
- **Catalytic capital that facilitates experimentation and innovation, leverages additional capital and signals impact potential within markets.** However, entrepreneurs identify further **catalytic actions**, which affect their capital, enterprise and the broader communities. For entrepreneurs, **catalytic capital attributes** are concessionary, flexible, reputable, long-term and risk-tolerant. And while **catalytic instruments** such as convertible notes, loans with concessionary terms and technical assistance are critical, entrepreneurs also claim grants that facilitate innovation are catalytic throughout their enterprise development journey. For entrepreneurs, catalytic capital is not uniform. They see a difference between useful and truly catalytic capital and its characteristics. This distinction relates to the broader context in which entrepreneurs consider capital.
- **A holistic perspective of their financing journey**, influencing what they consider to be catalytic, depending upon the enterprise's stage and broader context. Considering claims about catalytic actions, attributes and instruments in relation to the **enterprise's overall journey** contributes a temporal understanding of catalytic capital. For instance, the grants claimed to be catalytic are thought to be so throughout the entire financing journey, because of their unique support of innovation and experimentation.
- **Blending in rounds, and over time.** Entrepreneurs describe blending grants and concessionary capital with investments from a range of impact investors, development finance institutions and corporate/charitable foundations within a round. Their holistic consideration of financing

indicates they see **various types of capital blending within and between rounds**, both explicitly and through their joint consideration of financing and strategy. Challenges and variations related to the diversity and complexity of entrepreneurial financing journeys are elaborated.

- **A variety of investor roles**, across impact investors, foundations and development finance institutions. Identified **roles reflect the temporary and multiple** ways investors contribute, from impact investors advocating and connecting to foundations acting in a transformational role.

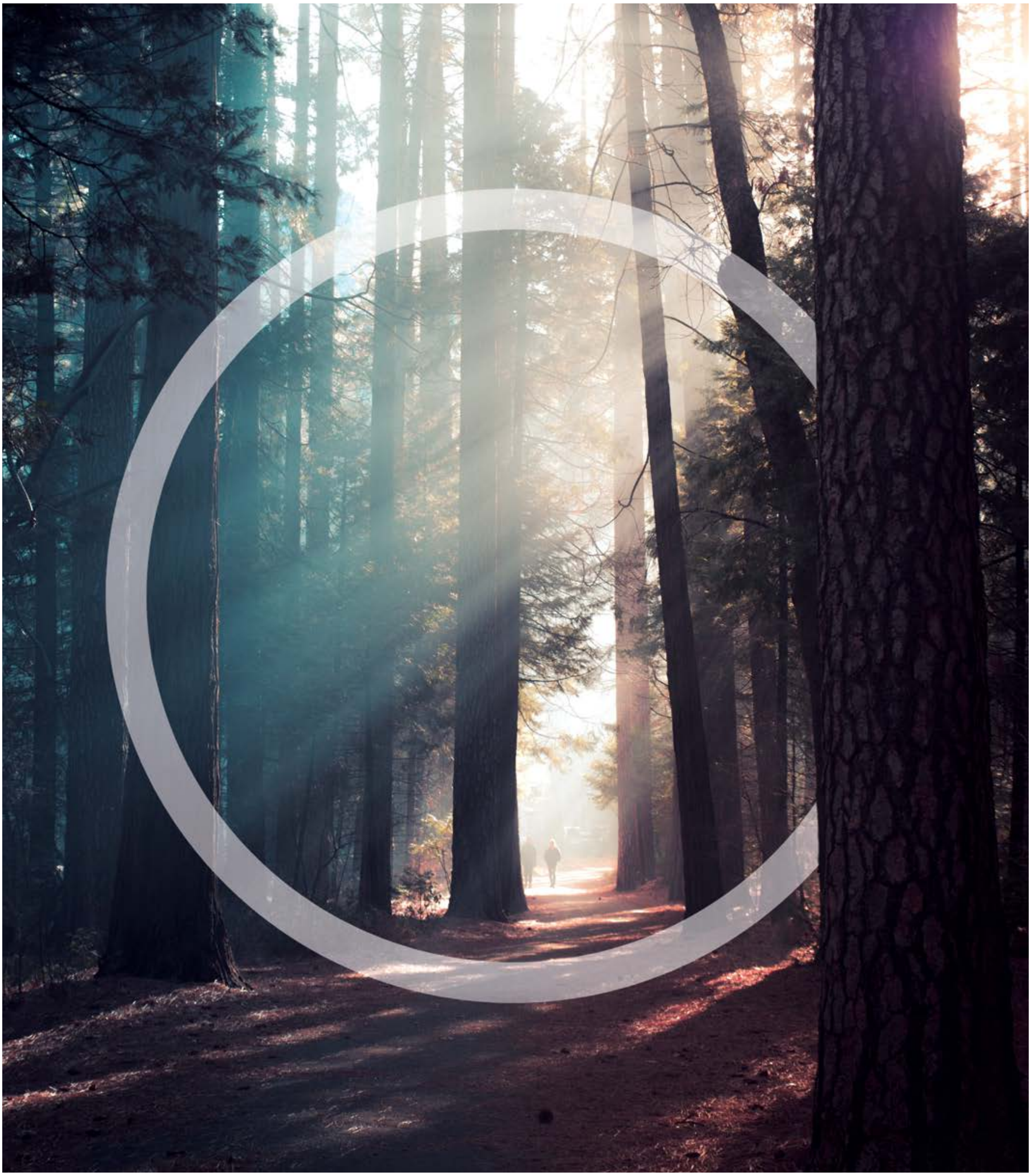
- **Relationships with their investors.** While the focus on catalytic capital often centers the capital itself, entrepreneurial accounts also emphasize the **relationship between the entrepreneur and their investor**. Many mention mentorship, respect for their visions of business and impact objectives and other emotional support. They also mention the value of these relationships for signaling legitimacy, introductions to other investors and as codified in the terms of the capital itself.

Figure 1: Summarized Findings of the Entrepreneurial Perspective



The entrepreneurial perspective contributes a holistic consideration of catalytic capital and blended finance, as these relate to early and growth stage enterprises. In so doing, entrepreneurs connect the structure of impact capital to the broader context in which it can be catalytic. Thus, for entrepreneurs, capital is catalytic when amenable action and terms align with the right moment in the organization's growth, broader financing journey and in partnership with investors/grantors who support the entrepreneur. Such context is often regarded secondarily, but the entrepreneurial perspective makes plain why all of these components ultimately render capital catalytic, useful or otherwise.

II. Introduction & Context



Introduction & Context

An entrepreneur sighs deeply, having just gone public. Despite the pandemic and numerous other challenges, she managed to grow her fintech business to maturity in an emerging market, even managing to expand her impact - educating and serving previously un-bankable customers at affordable rates. She succeeded in building a financially successful and socially impactful business.

How did she do it? Who and what was most supportive? Challenging? There is much we do not know, but we intend to ask...

Since the establishment of the Sustainable Development Goals (SDGs), great attention has been paid to what it will take to achieve such ambitious, global goals. Of major consideration is how to finance efforts to attain the goals and their social and environmental impacts. This challenge is a well-established and elaborated area as of the writing of this report[1]. Early contributors to this conversation include traditional funders of such impact, such as charitable foundations, development agencies, and development finance institutions (DFIs). In addition to their thought leadership, they are critical both as funders/investors as well as enabling the entrance of other private investors into markets they have not entered heretofore. Foundations, development agencies and DFIs wield deep knowledge of impact and are often able to invest on terms that private investors would not consider.

The consulting firm Tideline and the Catalytic Capital Consortium (comprised of the Rockefeller Foundation, the Omidyar Network and the MacArthur Foundation and hereafter referred to as C3) define catalytic capital mobilized toward impact as capital that "accepts disproportionate risk and/or concessionary return to generate positive impact and enable third-party investment that otherwise would not be possible."[2] To date, catalytic capital of this type has come from a small group of funders. As important as these dollars may be, they are a limited resource. While catalytic capital can be deployed on its own, it also plays an important role as an enabler of third-party investment.

Blended finance, "uses catalytic capital from public or philanthropic sources to increase private sector investment in developing countries in order to realize the SDGs", allowing organizations with different objectives to invest alongside each other while achieving their own financial and impact objectives[3]. In so doing, blended finance structures address barriers to private investment including high perceived and real risk, and poor returns for the risk relative to comparable investments. Blended finance structuring approaches generate investable opportunities in developing countries, leading to more development impact[4]. (For more detail on conceptual frameworks for catalytic capital and blended finance, see Appendix 1).

Catalytic capital and blended finance now move significant capital. However, the question of whether volume corresponds to benefit for the organizations that receive them merits investigation. With so much potential impact hanging in the balance, we must keep in mind that intention does not equal additionality, or the beneficial social or environmental outcomes that would not occur but for the investment. Capital’s intention encounters its potential to affect change in the enterprises that put it to use. Therefore, understanding catalytic capital’s impact potential requires investigation into the practices and perspectives of its end users. This research complements design by capital providers with input from capital users.

Enterprises: Where intention meets execution

Whether and how catalytic capital and blended finance structures successfully transform intention into impact hinges largely on which organizations get this capital, when they get it, and what they do with it. Many social enterprises are small and medium-sized enterprises (SMEs, who are arguably in the greatest need of help), driven by the entrepreneur(s) that found them. As the end user of capital, the entrepreneur can speak to the full experience of catalytic capital, from finding these investments to negotiating them, and how these vary over the life cycle of the enterprise. Entrepreneurs may also speak to many non-financial aspects of these investments, ranging from expectations of impact to relationships with and between investors. All of these elements affect the success of a social enterprise, and in turn, its potential for generating meaningful impact.

This leads us to ask, when it comes to catalytic capital, what is in it for the entrepreneur?

In the spirit of centering the entrepreneurial experience of catalytic capital and blended finance, this study gathers data from social entrepreneurs around the world, all of whom have received some type of “catalytic capital” as defined above. However, rather than imposing language and definitions, we listened closely to entrepreneurs’ experiences in their own words. As they explain their financing journeys, they highlight the investors, rounds, instruments and terms they view as most catalytic or pivotal for enterprise success.

Through these conversations, we learned what entrepreneurs value, how this varies throughout the financing journey, and how important qualities of capital and relationships are to entrepreneurs. In so doing, we make it possible to return to the conceptual frameworks of catalytic capital and blended finance, complementing and expanding upon these concepts from the point of view of their end user. It is our hope this research informs capital providers and users alike, helping both groups to collaborate more effectively for deeper impact and the generation of multiple returns—various levels of financial, social and environmental value.

III. Centering the Entrepreneur

A. Entrepreneurial Finance Literature

1. Complexity & Variation

As is true of the design of catalytic capital and blended finance, much of the research in entrepreneurship to date focuses on supply side concerns, and until quite recently, there has been relatively little focus on financing and investment decisions on the part of the entrepreneur[6]. Nevertheless, there are numerous, relevant challenges and concerns for the demand side. These are symptomatic of the complexity of entrepreneurial finance more generally. For instance, entrepreneurial finance encompasses a wide range of financial instruments and approaches, including angel finance, venture capital, private equity, private debt, trade credit, IPOs, and crowdfunding, and usually involves active investors that provide strategic, operational, and networking support. As a result, there are a vast array of issues in entrepreneurial finance when strategy and finance are considered, including fundraising, contracting, syndication, and initial public offerings or acquisitions[7]. This complexity represents opportunity, but also a variety of challenges ranging from access and familiarity to selection and execution.

2. Frequent Challenges

A fundamental challenge for many entrepreneurs is a lack of access to capital, especially in emerging and developing markets[8]. They have no contact with investors or intermediaries, especially if they operate in rural areas. However, those who do manage to get on the radar of investors face various challenges. Some challenges stem from entrepreneurs' lack of knowledge or experience. For instance, some are not familiar with processing financial information[9]. Entrepreneurs may also find it difficult to raise funds as a result of agency problems, information asymmetries, and a lack of internal cash flows or collaterals[10]. Additionally, entrepreneurs may have difficulty identifying the right type of investors to target with their fundraising efforts[11].

Still other challenges arise once entrepreneurs find investors, through negotiations and relationships. For instance, entrepreneurs navigating the impact investing market (which overlaps with blended finance, as impact investors may be involved in blended transactions) indicate they encounter tensions including, mission vs. business, sustainability vs. scalability, outcome vs. process and more, when engaging with the impact investing sector[12]. Such tensions stem from investor relations as much as their structure. Relatedly, while impact investing is meant to be transformational it may also be more transactional, which can be attributed to various factors, including de-coupling ownership of the problem from ownership of the business, investors and entrepreneurs not working in partnership, lack of accountability to impact measurements; and measuring the quantity of investments rather than quality[13].

Research to date demonstrates the importance of the context of capital in the entrepreneur's financing experience. Balancing social or environmental priorities is at the center of various tensions and unexpected experiences, suggesting that for catalytic capital to be successful in the eyes of entrepreneurs, it must not only be present and appropriately sized, but also well-partnered, with a shared understanding of the integration of financial and impact goals.

3. What entrepreneurs value from impact investing

Some of the challenges above relate to navigating within the broader financing ecosystem, while others relate to entrepreneurs' experiences with investors themselves. Relatedly, negotiations and investment terms are codified on paper, but they too are the product of interactions between entrepreneurs and the investors representing capital. As such, the social dynamic between entrepreneurs and investors is an important piece of understanding the entrepreneurial experience of social investment.

More specifically, we know about the social venture capital (SVC) model and how social venture capitalists select investment targets[14], but less is known about entrepreneurs' perspectives of these same investors. While the value of investor capital is seemingly obvious, aforementioned challenges demonstrate the importance of the contextual factors surrounding and imbued in investments[15]. Additional research offers insight into the extra-financial qualities of such social investments. For social entrepreneurs, the most attractive quality of SVC investors is investor reputation. The same study also finds the positive effect of business advisory and network access supports outweighs any negative experience of information and control rights. These findings correspond to broader social support literature, which defines social support as either assistive (relating information, making connections) or appreciative in nature (emotional, help with assessment)[16] demonstrating that entrepreneurs value both types of support during negotiations of impact capital.

Further, entrepreneurs' own experience also affects their opinion of capital. Mayer and Scheck find that more experienced entrepreneurs strongly focus on reputation, whereas more novice entrepreneurs perceive business advisory as most important[17]. This research demonstrates how valuable non-financial benefits like reputation are to entrepreneurs and how what entrepreneurs value changes over time and with experience, from more appreciative to assistive support[18].

4. Addressing the entrepreneurial knowledge gap

The aforementioned research explains challenges for entrepreneurs and what they value, but neither of these literatures offer significant guidance to entrepreneurs. Conversely, a growing body of work has become important to guiding supply side actors, including practitioners, governments, international agencies, and implementing groups on how to design, develop and deploy impact capital. There has been less treatment of the demand side of impact investing and blended finance[19]. As a result, while the field has come a long way in envisioning and moving capital toward impact, it has done so from the perspective of the capital provider, often leaving entrepreneurs – particularly those at SMMEs–arguably those in the greatest need of help--without the knowledge or resources to navigate complex transactions and relationships that catalytic capital and blended finance transactions entail.

To remedy this, we turn an eye and ear toward the entrepreneur, with the intention to suspend supply side knowledge and assumptions about catalytic capital and blended finance, in favor of the entrepreneurial experience. In so doing, we intend to address the demand side knowledge gap by 1) contributing knowledge regarding the entrepreneur's experience of the financing journey and 2) making this knowledge useful to this group of enterprises, as well as capital providers.

B. Methodological Approach

Centering the entrepreneur also informs the methodological approach of this study. We began with a deep dive into the background literature on catalytic capital and blended finance, which orients the study to these concepts as well as project design. Sample selection began by building a database of 90 social enterprises which had received catalytic capital and either had received investor-led blended finance or had sufficient opportunity post-catalytic capital investment to blend at the enterprise level. After narrowing this sample by sector, stage and geography, we recruited participants from 26 enterprises. Data collection comes from in-depth, semi-structured interviews with social entrepreneurs in the early or growth stages of developing their business (Interview Protocol can be found in Appendix 2). Most conversations were conducted with founders or co-founders of the enterprise, while a select few were with chief financial officers or other finance staff.

A relevant note on how entrepreneurs define and identify catalytic capital:

During interviews, we did not define the term "catalytic capital" for entrepreneurs, as this is a supply side term with which entrepreneurs may or may not be familiar. Instead, we asked about one or more specific investments made with terms capital providers which would consider "catalytic". We asked whether this and/or other capital was pivotal for them and whether they blended it with other capitals. In so doing, interviewees were empowered to explain the value of that investment for their enterprises from their perspective. Focusing on what, according to entrepreneurs, is most pivotal, difficult, surprising etc. identifies what capitals are catalyzing (or not) for these enterprises as well as how entrepreneurs consider the relationship between capitals.

Central Research Questions:

- What does it mean for capital to be catalytic, from the perspective of entrepreneurs?
- How do entrepreneurs blend catalytic and other capitals throughout their financing journey?
- What enables and inhibits entrepreneurs during the early and growth stages of their financing journeys?

Figure 2: Enterprise Characteristics

Region	Stage	Sector	Founder
South Asia - 8	Early - 5	Food & Agriculture - 6	Female-Founded - 5
South-East Asia - 4	Growth / Scaling - 18	Financial Services - 3	Male-Founded - 21
Sub-Saharan Africa - 14	N/A (org from change etc.) - 3	Energy - 11	
		Health - 4	
		Other - 2	
Total: 26	Total: 26	Total: 26	Total: 26

Early and growth stage enterprises were selected based upon having at least one investment of "catalytic capital" in the supply side definition, as well as sufficient opportunity post-investment to blend this capital within a round or with other capitals over time. To ensure we were not capturing the experience of a particular geographic location or sector (several findings did, in fact, relate to particular geographic and sectoral particularities), we spoke with entrepreneurs from several regions and sectors. Sectors selected are generally "investable" in order to achieve a degree of comparability without placing too much emphasis on public financing. We selected food and agriculture, financial services, energy and health, with two additional and slightly varied sectoral focuses. Of the enterprises that qualified, several changed organizational form (to a nonprofit or dual business/foundation model, thus the variation in stages) and only 5 of the 26 enterprises were female-founded organizations. The selected sample thus represents the well-documented gender gap in the financing of women-led enterprises[20]. Despite the small sample size, entrepreneurs interviewed represent diverse experiences, yielding deep insights from varied perspectives. Data was coded in MaxQDA software, first through open coding and secondarily through axial coding, examining connections between patterns in the data.

Thus far we have centered the entrepreneur, explaining the lack of research about and for social entrepreneurs and how this gap informs the study's design. Now, we examine catalytic capital more closely, comparing capital providers' design and intentions with the reported entrepreneurial experience of this capital.

IV. Catalytic Capital According to Entrepreneurs

Catalytic Capital According to Entrepreneurs

According to capital providers, catalytic capital:

"accepts disproportionate risk and/or concessionary return to generate positive impact and enable third-party investment that otherwise would not be possible[21]." Thus, catalytic capital is a type of capital, designed to pursue impact at the time of deployment either alone (horizontally) or in combination with other capitals through blending (vertically[22]) to create impact that would not occur in its absence. (More detail can be found in Appendix 1).

The following sections progressively build an understanding of the entrepreneurial definition catalytic capital, which can be compared with the definition offered above. The next section presents entrepreneurs' definitions of what it means for capital to be catalytic. Subsequently, relationships between these elements are outlined, and finally these elements are mapped across the financing journey.

A. Differentiating First and Second Level Catalytic Capital

Conversations with entrepreneurs introduced the qualifying "catalytic capital" investment(s) by the name of the investor associated with it (e.g. the concessionary loan from Example DFI). Entrepreneurs were separately asked what capital was most pivotal for their business. Avoiding the field's term, "catalytic capital", precluded confusion that might stem from a range of entrepreneur familiarity with the term. As a result, conversations yielded clear indications of the experience of "catalytic capital" whether it was or differed from the most useful capital for the enterprise.

In keeping with the language entrepreneurs chose, an important level of distinction emerged: that of first and second level catalytic capitals. It is important to note that because these findings represent a small sample of entrepreneurs, the distinction between first and second level capitals is just as important–if not more so–than the particular actions, attributes and instruments allocated to these categories. A larger sample may affirm, add to, or challenge the contents of first and second level catalytic capitals mentioned here. However, the articulation of useful, if not quite catalytic capitals represents an informative distinction. It demonstrates that entrepreneurs do not think of catalytic capital separately from the other capital they raise, or whether it is intended to be blended formally or not. Additionally, for capital providers, it indicates that there are other very important roles for capital to play even if they do not qualify as catalytic. On the other hand, if investors/funders are intent on being catalytic, they do well to pay attention to the distinction as well.

First level catalytic capital is that which is pivotal for entrepreneurs' financing journeys. It is additional capital with an impact orientation that makes growth or other investments possible that otherwise would not be.
An example identifying first level capital from a respondent:

"I think all of these sorts of experiments take a lot of non-diluted funding. That's the most critical angle."

This entrepreneur identifies non-dilutive funding as unequivocally important in their financing journey.

Second level catalytic capital is that which entrepreneurs claim to be helpful, but for which a clear relationship to growth, accelerated impact, or additional capital is not evident.

An example of second level catalytic capital from a respondent:

"I'm sorry, there's nothing catalytic about coming into a proper normal round...Once they were in, though, they were very good at helping. Any time we didn't have a new infusion of capital, they were very good at saying we're ready to be here to support you. So, if you needed 250k, 300k additional we are happy to put it in as quick as you want. And they were good at driving those terms. They were good at helping get fast feedback"

This quote demonstrates that there may be a difference between what capital providers identify as catalytic, and what entrepreneurs experience as catalytic capital. Further, even though this entrepreneur challenges the definition of catalytic capital, they identify how helpful a related, if different element (follow-on funding) is to their enterprise. The difference and importance of first and second level catalytic capital are apparent in this example.

Examples like these demonstrate the value of considering first and second level catalytic capital separately. For the remainder of this section, catalytic capital is divided into these two groupings, based upon the input of the entrepreneurs interviewed.

B. Catalytic Actions

Entrepreneurs describe capital that is catalytic for their organizations as corresponding to actions, attributes and instruments. As indicated above, these can be separated into first and second level categories, depending on whether they were pivotal or helpful for entrepreneurs.

In this first section, we explore the actions entrepreneurs identify as catalytic.

First Level Catalytic Capital Actions include:

Several of the first level catalytic actions of capital described by entrepreneurs assist them with growing and financing their enterprise internally. Specifically, funding experimentation/innovation is a critical role of catalytic capital, because entrepreneurs claim equity investors want to see a business with multiple products/services, capable of scaling, but they do not want to be the ones to finance the development. Similarly, facilitating financing by bridging financing rounds and sharing due diligence - particularly considering how lengthy due diligence processes (for concessionary terms and/or from impact investors) can be–and signaling legitimacy are identified as catalytic. Further, reducing the cost of capital through lower rates and amenable terms enables entrepreneurs to retain as much ownership as possible. Finally, scaling/expansion of the model and/or to new geographies or products is described as catalytic action.

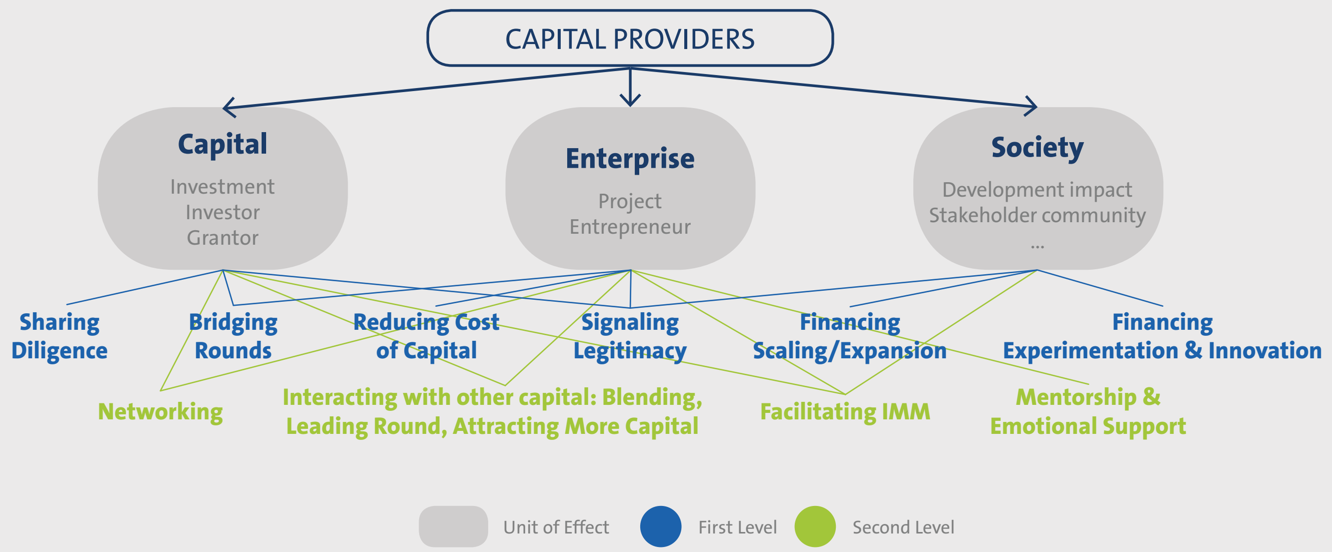
Second Level Catalytic Capital Actions include:

Among the actions claimed to be very useful or helpful, if not pivotal, is networking, particularly introductions from other entrepreneurs or investors to new investors. Similarly, mentorship and other support from investors are extremely important for enterprise growth. Entrepreneurs in early stage enterprises have social or environmental goals but do not necessarily have the experience or capacity to measure impact, so capital that assists in developing IMM practices can, in turn, attract other impact investors. Finally, interacting with capital in a few other ways, including blending (e.g., an accelerator with a grant or concessionary capital) or leading a round are very helpful to entrepreneurs. Interacting with other capitals is perhaps more obviously secondarily catalytic in that none of these are pivotal on their own; they are most effective in partnership with other capitals.

Figure 3: Supporting actions of catalytic capital providers

What actions by capital providers are most catalytic from the perspective of the entrepreneur?

Capital providers can support social entrepreneurship through taking first or second level catalytic actions to have effect on the capital, enterprise, or society level. This version is based on the existing frameworks of classifying ways of being catalytic (such as the Pathways to Impact and AECF framework on additionality). It aggregates the different elements into one consistent framework.



Catalytic actions affecting capital, the enterprise and society

Capital provided by investors may be catalytic in the ways listed above. These actions directly affect other capital invested, the enterprise more broadly and/or Society more generally. Capital itself is affected by catalytic actions, via the investment structure, those interacting with it and how it is assessed. Particular actions including networking, interactions with other investors, blending and leading a round, sharing due diligence, facilitating impact measurement and management of investments, and by signaling legitimacy to other investors are all actions that entrepreneurs identify as either helpful, or pivotal to the structure of the capital.

Enterprises, comprising the project, entrepreneur or other elements of the entity separate from its capital, also benefit greatly from catalytic action, through many of the same actions that benefit the Capital unit of effect, but also through reductions in the cost of capital to the enterprise, mentorship and emotional support, strategic connections and financing experimentation and innovation as well as scaling. This variety of catalytic action demonstrates how broadly catalytic capital providers' actions benefit enterprises, from financial circumstances to relational ones to benefiting the enterprise's strategic development and expansion.

The final unit of effect, broader Society, benefits from catalytic capital providers' actions by virtue of the enterprise's expanded capacity to be strategic, innovate, and to expand and assess its impact.

C. Attributes of Catalytic Capital

Entrepreneurs attribute certain qualities to the capital they deem most catalytic for their financing journey.

"Sometimes...the catalytic approach of investors is getting money in faster, collaborating with each other more effectively--to make sure the pain point of the entrepreneur is out there--and.. endorsing to get you in the right place at the right time."

This statement mixes actions (collaborating, signaling) and qualities (faster, efficiency) to describe what is useful or even catalytic.

First Level Catalytic Attributes

As a group, first level catalytic attributes largely concern the terms that capital is invested on, specifically terms more tolerant of risk and change, and which assist the enterprise through lowered expectations of financial returns, lending for longer terms, and by signaling credibility to the broader ecosystem by virtue of its own reputation.

In keeping with the desire to reflect the language and account of entrepreneurs, it should also be noted there is overlap between first and second level attributes. Particularly, and perhaps surprisingly, regarding concessionary terms. Some say concessionary terms were catalytic, while others indicate they do not qualify.

When asked about a particular investment, one entrepreneur said, "that particular concessionary loan was helpful, but not catalytic" which the respondent attributes to the comparatively greater influence of political and social contexts also influencing the enterprise's growth.

Yet another respondent explains concessionary terms, particularly when paired with an accelerator, are "very helpful". This nuance in language distinguishes the range of ways that entrepreneurs view the role of concessionary capital in their organizations, and reminds that entrepreneurs consider catalytic attributes within the broader context of the financing journey.

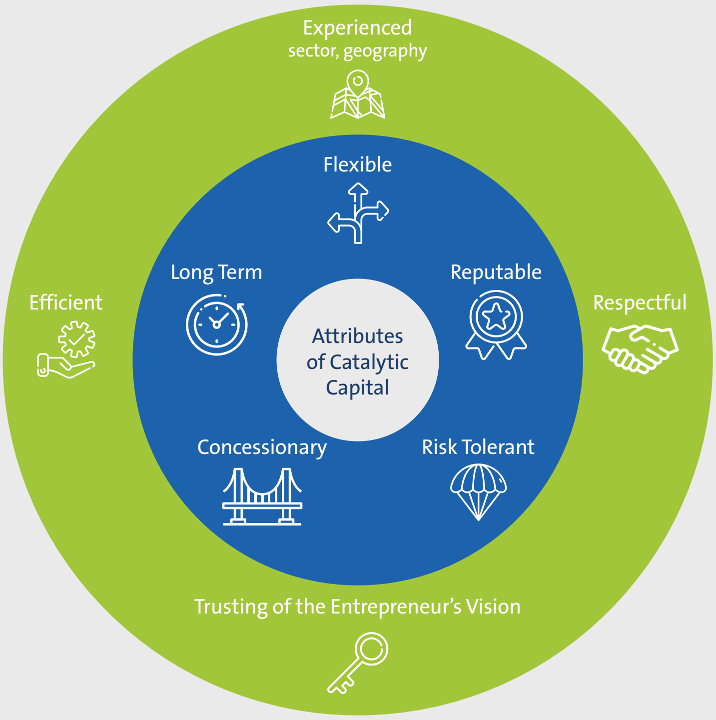
Second Level Catalytic Attributes

Second level attributes are notably different in that, apart from efficiency, these qualities relate more closely to the relational context in which capital is invested. While we often focus on the tangible qualities of capital, according to entrepreneurs, capital that is structured to be respectful and trusting of the entrepreneur's vision for the enterprise, as well as experienced in a particular sector or geography are not only qualities of the relationship but also translate into the very terms of the investment. These findings suggest an entrepreneur-centric approach to catalytic capital must consider both what the terms are and how these terms incorporate the investors' and entrepreneurs' knowledge and experiences.

Figure 4: Attributes of Catalytic Capital

What attributes of catalytic capital are most catalytic from the perspective of the entrepreneur?

This bullseye aligns **first level catalytic attributes** of capital in the inner circle, and **second level attributes** in the outer circle.



D. Catalytic Instruments

In discussing catalytic instruments, entrepreneurs connect qualities and actions, bringing the full picture of catalytic capital into view.

Entrepreneurial explanations of first level catalytic instruments:

Grants

"So I believe a lot of what we are able to do today is just because of the grant funding, and that was the time where we were doing a lot of experiments on the business model itself."

The grant instrument allows for the earlier named catalytic action: funding innovation and experimentation. Still others speak to grants' ability to facilitate other catalytic actions:

"I think the most critical part was especially with [X Foundation and Y Foundation], some of our institutional non-dilutive funders..they thought about scalability."

Often in more traditional contexts, grants are associated with distinct social or environmental projects or goals, as opposed to strategic, long term goals like scalability. However, an important finding of this research is that grants, which some entrepreneurs also refer to as "non-dilutive" capital, are particularly catalytic when they focus on the business's long term strategy and goals for growth. This finding hints at the important role investors play at well (which are described in further detail in Section 7).

Guarantee

An entrepreneur spoke of a guarantee functioning in a catalytic manner when a foundation that previously awarded the enterprise grants previously no longer wanted to make grants that might potentially crowd out other capital. As a result, the foundation made a loan guarantee, inspiring the confidence of commercial capital to invest. This same respondent indicated that the signaling of this guarantee and subsequent successful round of fundraising meant that they did not need guarantees in a following round. However, in an upcoming, and much larger round, a guarantee might be required yet again. This example demonstrates how a guarantee can successfully act catalytically – by signaling legitimacy--and that this may be catalytic both early and later in an enterprise's life cycle.

Concessionary and Convertible Debt

According to one entrepreneur, convertible notes are:

"a really elegant instrument: the investor doesn't have to worry about valuation. It's a really simple investment agreement..., it can be catalytic, it can signal valuation via the valuation cap, and discount."

Here, convertible notes are catalytic through their signaling action regarding the business via the particular terms beyond its nature as preparation for an equity round.

Equity – particularly in combination with other types of capital, can be catalytic. For instance, one entrepreneur said the most catalytic investment they had was a pledge to make an equity investment of a certain amount if the entrepreneur found matching funding.

Yet another entrepreneur differentiates traditionally defined catalytic capital from equity, claiming they are both pivotal, permitting different and equally important actions:

“The catalytic funding has been able to help us test and innovate new services, new business models, and then the equity investments have helped us obviously hire the teams and build.”

Second level catalytic instrument examples:

Working Capital, technical assistance and bridge loans are each mentioned a few times, though not necessarily in a uniform manner. For instance, technical assistance is viewed by some as very helpful, while others find it to be less helpful, because its terms are too restrictive, or the support is not relevant for more experienced entrepreneurs. However, one such claim that technical assistance is very helpful explains:

“[The impact investor was] able to help facilitate technical assistance, grant funding for certain interventions that equity capital wouldn’t necessarily allow...Like leadership development, doing deeper impact assessments, trying to navigate a new strategy.”

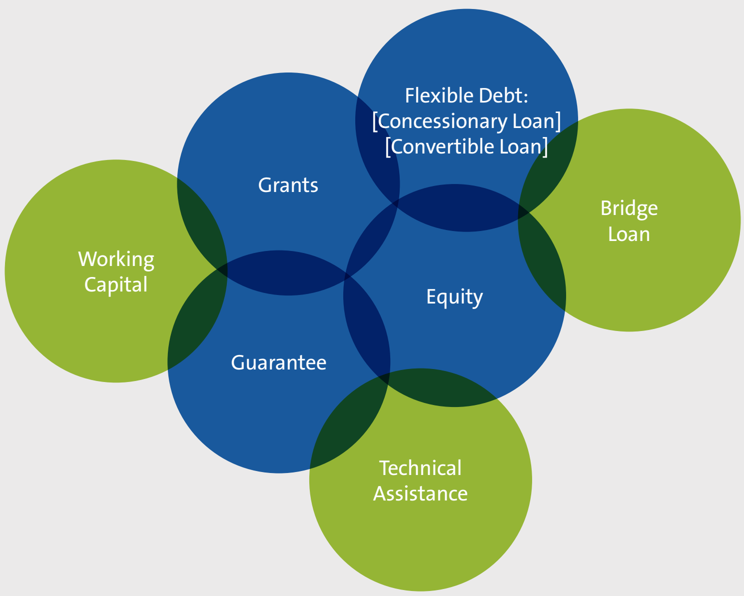
Here, technical assistance enables the helpful, but not necessarily pivotal actions of facilitating impact measurement and management and financing growth and scale.

As the examples of these instruments suggest, they facilitate many of the pivotal and useful actions defined and mapped earlier. The instruments must also be evaluated in terms of when they are provided. Some are more catalytic at certain stages of the entrepreneurial financing journey, while others are claimed to be catalytic further into the financial life cycle.

Figure 5: Catalytic Instruments

What instruments used by capital providers are most catalytic for entrepreneurs?

First level catalytic instruments are in blue, with equity less claimed than grants and various types of debt.
Second level catalytic instruments are in green with technical assistance featuring strongly.



V. A Holistic Approach: the Entrepreneurial Financing Journey

A Holistic Approach: The Entrepreneurial Financing Journey

Thus far, we have categorized entrepreneurs' claims of catalytic capital, dividing them into actions, attributes and instruments. In this section, we align these elements with the timeline of the financing journey, combining entrepreneurial insights about what is catalytic alongside when it is catalytic. We find that time matters to entrepreneurs in two ways:

1. In accordance with financing stages.
2. Situationally, or at a moment in time that coincides with other actors, capitals etc. such that the time is not linear but a catalytic moment in the journey.

We attempt to address both of these in the figures and descriptions below.

Catalytic Actions Throughout the Financing Journey:

Perhaps as notable as the catalytic actions aligned with early and growth stages are those actions entrepreneurs claim to be important over the entire financing journey of the enterprise. For example, entrepreneurs explain that equity investors always want to see new and additional projects, and that grants and long-view non-dilutive funders play a critical role in enabling necessary, continued experimentation. Further, investor types vary and change throughout the financing journey. However, the value of signaling legitimacy from different investors does not cease to be catalytic. For example, entrepreneurs may begin with angel investors, accelerator funding or prize money, which may signal to impact investors or development finance institutions. These examples demonstrate the longevity of some catalytic actions relative to others, as well as how these intersect with financing stage and other factors, such as investor types.

Figure 6: Catalytic Actions throughout the Financing Journey

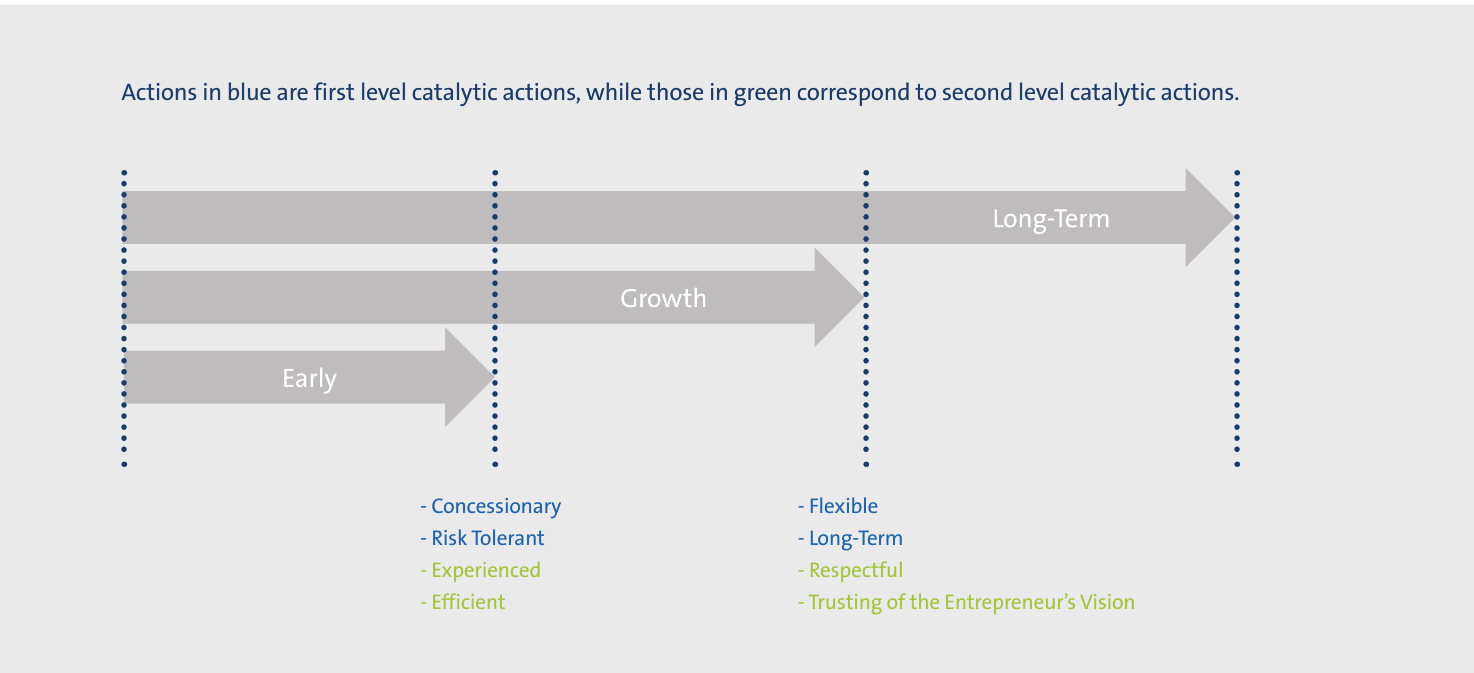
Actions in blue are first level catalytic actions, while those in green correspond to second level catalytic actions.

Catalytic Attributes throughout the Financing Journey:

In both early and scaling stages, capital that is concessionary and risk tolerant is cited as catalytic and experienced and efficient capital is cited as deeply helpful in the early and beginning of the scaling stages of an enterprise.

Similar to catalytic actions, certain attributes are spoken of as catalytic throughout the financing journey, during all stages. Flexibility and long term commitments are claimed to be catalytic throughout the course of the financing journey. For instance, an enterprise named a corporate foundation the most pivotal investor and capital for their journey. They claimed this because they both made grants and investments in the business and made the first grant when they were early in their journey, shifting back and forth to investments and more grants as the needs of the enterprise changed. Respectfulness and trust of the entrepreneurial vision are also noted to be very helpful throughout the life course of the journey, which follows, because capital structured to incorporate these attributes are the result of relationships with grantors or investors that must comport themselves this way and which does not become less critical to an entrepreneur's survival in later stages.

Figure 7: Catalytic Attributes throughout the Financing Journey



Catalytic Instruments throughout the Financing Journey:

At least one entrepreneur indicated that each of: technical assistance, concessionary loans, convertible notes, equity and technical assistance funds are particularly catalytic or useful in early stages. In addition, guarantees and working capital are catalytic or useful tools once the business's operations are established and capital is needed to continue producing and growing, without diluting the entrepreneur's equity excessively.

Similar to catalytic actions and attributes, certain instruments—particularly grants— emerged as catalytic throughout the life cycle of an enterprise. The context for their catalytic capabilities shifts over time, as well. Entrepreneurs may have claimed them as catalytic for being first capital or signaling early on, they claim that the ability grants give to enterprises both early, scaling and nearing maturity, is that they allow enterprises to continue to experiment and innovate. Entrepreneurs claim that innovation and experimentation are always needed, and grants are the only capital that continually allow them to finance risky experiments.

This study's contribution regarding the temporality of catalytic capital is that what is catalytic varies over time and should be considered by capital providers and users alike. Above, we document instances of entrepreneurial claims regarding catalytic elements attached to specific enterprise and financing stages. These should be interpreted as illustrative, as opposed to exhaustive or exclusive. Future research should investigate such allocations in a larger sample.

Figure 8: Catalytic Instruments throughout the Financing Journey

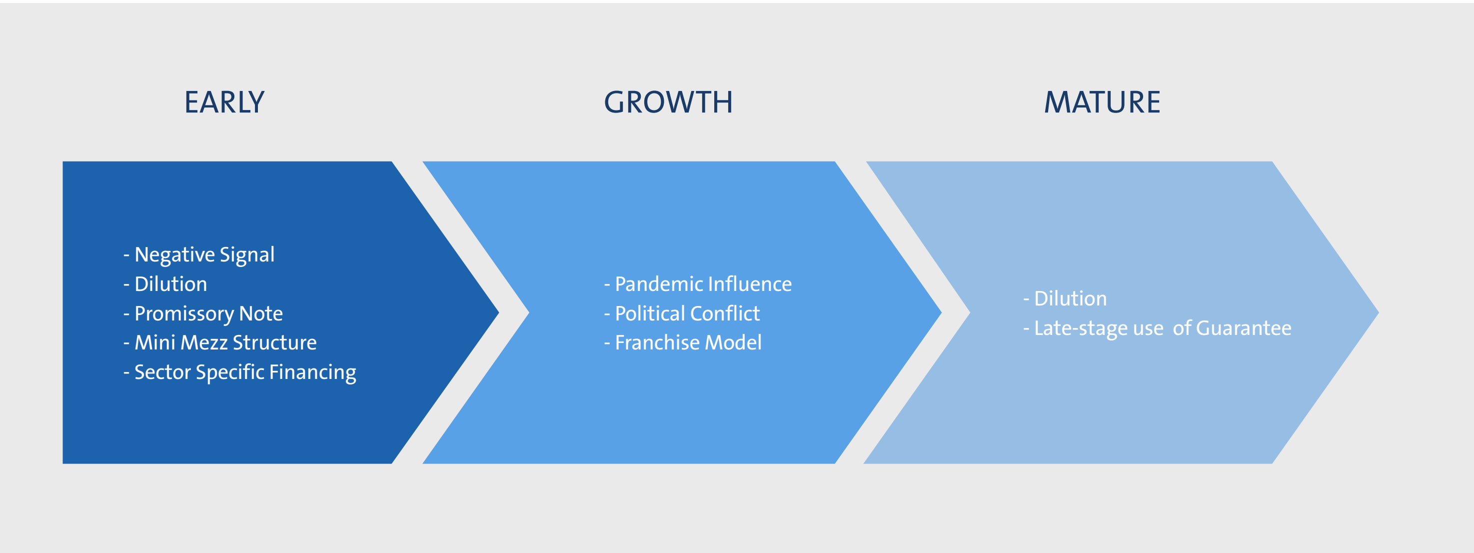
Instruments in blue are first level catalytic, while those in green correspond to mentions of second level catalytic instruments. Multiple listings of the same instrument indicate multiple, different mentions.

A. Variations in the Financing Journey

A number of entrepreneurs described their early and scaling financing journeys as corresponding to a relatively predictable pattern of growth and investor involvement, while some articulated varied circumstances or structures that merit mention. While not catalytic, their influence on the financing journey influences and interacts with catalytic capital and may affect blending. Additionally, these may be more or less common in the broader population of social entrepreneurs.

These circumstances are mapped to the corresponding phase of the financing journey. Corresponding explanations are offered below.

Figure 9: Variations in Financing Journey Stages



Some of these variations were negative experiences for entrepreneurs:

- **Negative Signal** - One entrepreneur’s journey hinged on a large investment from a development finance institution that had not reserved follow-on funding for a subsequent round. When it was time to raise a subsequent round, he says that impact investors found the lack of DFI follow-on funding to be a negative signal.
- **Dilution** - A few entrepreneurs gave away too much equity too early or had either impact investors or commercial investors with whom the deal terms favored the investor excessively (through rates, board appointments/influence, forced executive staff appointments etc.). For two such companies, entrepreneurs were forced to leave or sell the company, leaving with no profit.

- **Pandemic Influence*** - Interviews in 2022 allow entrepreneurs to reflect at this point on the influence of the pandemic. Several entrepreneurs pivoted their business and financing strategies to accommodate for the pandemic. For a few this meant moving more services online, which either helped or hindered obtaining financing, while others were forced to slow production and needed additional capital to stay afloat.
- **Political Conflict*** - Two other entrepreneurs reported stalling in their financing journeys due to political conflict in their region.

* (These two cases are external influences that affected the enterprise at the noted phase of the financing journey, as opposed to others, for which the phase was integral to the variation).

Other variations mentioned were positive in nature, including:

- **Promissory note** - One entrepreneur underwent a long and stringent due diligence process with a development finance institution. However, they provided a note the entrepreneur brought to potential investors after the diligence was sufficiently far along, and before cash had been disbursed, which successfully attracted more investors.
- **Late stage use of guarantee** - One entrepreneur whose business is in lending, said that they believe they will require a guarantee for a third round of funding, after having one for the first but not second round.
- **Mini mezzanine structure** - A two phase loan facility; the first was for a pilot, and the second was tied to an investment round with other investors. The entrepreneur called it a "clever and flexible mini mezz structure." The investor also had warrants they could execute, priced at the next round. This structure offered flexibility, cash needed early on, and helped them to catalyze their next round, all while giving the investor favorable future terms.
- **Sector specific financing** - Two entrepreneurs of health services enterprises noted financing options available to them by virtue of their sector. One such entrepreneur began a franchise model, and another noted being able to get very early financing for medical equipment from the pharmaceutical company that produced it, which a bank would not lend them at the time.
- **Organizational form in female-founded enterprises** - three of the five female founders interviewed make use of a charitable foundation as well as the for-profit enterprise under consideration. Foundation use varies, with one beginning her organization as a foundation and later establishing a social enterprise; another beginning as an enterprise and later creating a foundation; and still another creating both a foundation and for-profit enterprise at once. It is possible that female entrepreneurs maintain connections between social mission and business practice differently than male counterparts, and may use organizational form as a support.

* (Please note this does not appear in the graphic above as it relates to the financing journey but not a particular stage).

B. Challenges in the Financing Journey

In the previous section, entrepreneurs address variations, some of which are challenging. The section below describes more frequently experienced challenges. While these are not always specifically related to catalytic capital or blended finance, they are an important element of the full entrepreneurial experience.

Figure 10: Challenges in the Entrepreneurial Financing Journey

INVESTORS:

- Inexperienced
- Restrictive
- Misaligned or incompatible with other investors

CAPITAL:

- Lengthy and slow approval and payments
- Misaligned to vision causing mission drift
- Restrictive and short-term
- Dilutive

CONTEXT:

- Ecosystem supports unhelpful
- Restricted investment of catalytic capital
- Sector-related

INVESTORS

The most frequently and consistently reported challenges or negative experiences for entrepreneurs relate to their investors. Broadly, these challenges regard a few key categories:

- **Inexperience**
  - In start-ups, to understand how they differ in financing needs or growth trajectory.
  - With finance (e.g., due diligence) when coming from a non-profit or foundation background.
  - With social or environmental impact (e.g., what kind or how much is appropriate, how to assess or balance it with commercial priorities) when coming from a finance background.
  - With the enterprise’s sector (e.g., health, agriculture, financial services, particularly when a social enterprise works in/across two sectors) or geographic location, bringing “Western” expectations not appropriate for local contexts.
- **Restrictive or controlling**
  - Via investment terms (e.g. with requirements to hire executive staff, board seats (both wanting one and pushing others out)).
- **Misaligned or Incompatible**
  - With other investors, such as not accepting a lead investor’s terms or agreeing upon investment terms more generally.

CAPITAL

While challenges most commonly revolve around investors, challenges related to capital are more varied in nature. Capital-related challenges include:

- **Lengthy and Slow**
  - Including a tedious due diligence process, particularly reported for development finance institutions and some impact investors. Investors can be slow to approve and disburse cash, making it difficult for cash-strapped enterprises to stay afloat.
- **Misaligned**
  - To the vision of the organization, either forcing expansion into new markets or geographies or shifting focus away from impact and toward profit, sometimes by making processes more efficient (e.g., reducing training time for employees, which also reduces skill attainment), resulting in mission drift and/or excessive work.
- **Restrictive and short investment terms**
  - That make future negotiations with other investors difficult. Similarly, terms that are too short for enterprises force early stage entrepreneurs to spend more time fundraising than working on their business.
- **Dilutive**
  - Capital that takes too much ownership from entrepreneurs too early, sapping their energy and desire to grow the business.

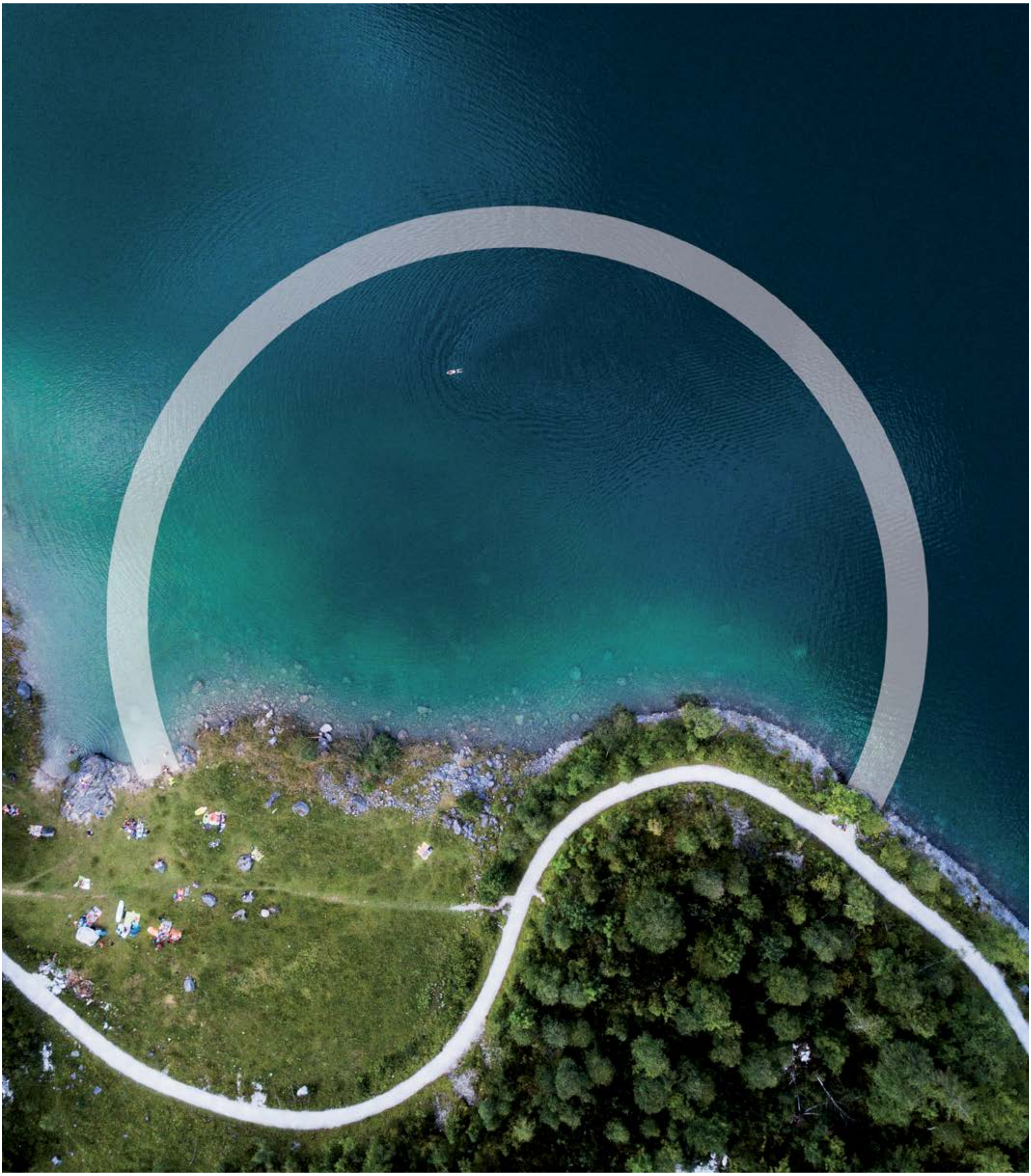
CONTEXT

Relatively few reported challenges related to broader context, but several notable ones included:

- **Ecosystem level resources**
  - Such as accelerators and technical assistance grants that are irrelevant for experienced entrepreneurs (former), and executed by inexperienced and/or slow staff (latter).
- **Restricted catalytic capital**
  - Reported by two entrepreneurs, as flowing from development finance institutions to specific government departments, which deploy to few non-profits/enterprises in emerging markets, thus not reaching its full, catalytic potential.
- **Sector related**
  - Entrepreneurs working at the intersection of two sectors note that this disadvantages them with some impact investors. For instance, an investor may be familiar with one sector but not the other and decide that the enterprise falls outside of their scope because of this.
  - Further, the sector an enterprise works in can affect financing needs. Those extending credit to communities require debt earlier and more consistently, for example, than enterprises in other sectors.

The challenges and negative experiences of financing journeys entrepreneurs report largely regard the 'fit' or suitability of investments to the entrepreneurs' goals and needs. These center on the experience investors bring to negotiations and ongoing relationships, and which are codified in processes, such as long and arduous diligence processes or terms that do not fit entrepreneurial needs, because they redirect focus, take too long or end too quickly. Overall, such challenges might be addressed through investor education, collaboration with other more experienced investors or ecosystem actors, and streamlining and sharing due diligence.

VI. Experiences of Blending:
In a Round and Over Time



Experiences of Blending: In a Round and Over Time

The financing journey is a fitting prior topic to the entrepreneurial view of blended finance. As the variety of actions, attributes and instruments of catalytic capital mapped to the entrepreneurial financing journey demonstrate, there are any number of unexpected sources of support or complication owing to investors, instruments and broader political or global contexts. We now turn to capital provider definitions of blended finance and what entrepreneurs had to say about blending.

According to capital providers and field experts, blended finance:

represents one approach to combining catalytic capital with other capital. The definition of blended finance differs between leading industry actors in international development. While OECD defines it as "the strategic use of development finance for the mobilization of additional finance towards sustainable development in developing countries" the DFI Working Group on Blended Concessional Finance defines blended finance as "combining concessional finance from donors or third parties alongside DFIs' normal own account finance and/or commercial finance from other investors, to develop private sector markets, address the Sustainable Development Goals (SDGs), and mobilize private resources" and for Convergence "blended finance is the use of catalytic capital from public or philanthropic sources to increase private sector investment in sustainable development". (For more background, see Appendix 1).

In the sections that follow, we identify how entrepreneurs think about blending catalytic and other capitals throughout the course of their financing journey. Moran and Ward-Christie (2022) refer to blending in rounds as a "hybrid of hybrids" and the stories entrepreneurs offer about blending capitals support this label. Further, despite a more traditional focus on blending within a round, entrepreneurs reveal that they blend capital both within rounds and over time[23].

A. Blending in a Round

Entrepreneurs discuss blending in a round as pertaining to:

- Investor types blending (Who)
- Design and instruments of blending (How)
- (Challenges) encountered, and
- (Plans) to use blending in the future.

Figure 11: Frequent Topics on Blending in a Round

Impact Investors are the investor type most discussed in relation to blending within a round.

Entrepreneurs cite examples of impact investors blending with other imact investors, following or bringing in development finance institutions, private capital, corporate foundations, and sustainable and commercial banks.

One entrepreneur referred to blending as occuring between a **"coalition" of investors**, including a corporate foundation, a DFI, a national bank and several small impact funds. The entrepreneur said this was helpful in expanding the business.

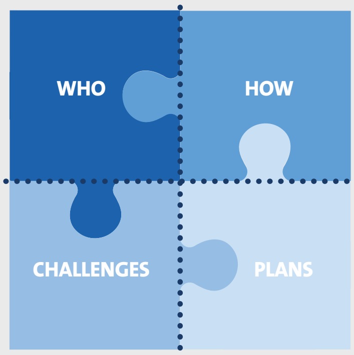
Entrepreneurs discuss elements of the design and execution of blending:

Dilligence - particularly whether or not investors share or "piggy back" due diligence.

Leading an investment round.

Structuring examples - grants with equity, grants with subordinated loans or convertible notes, a loan facility in two tranches with warrants matching incen- tives attracting additional investors to complete a round.

Results based financing/Outcomes Funding - Entrepreneurs explain RBF and outcomes funding ideals that incentivize additional point-in-time investment and motivate the enterprise toward the future incentive.



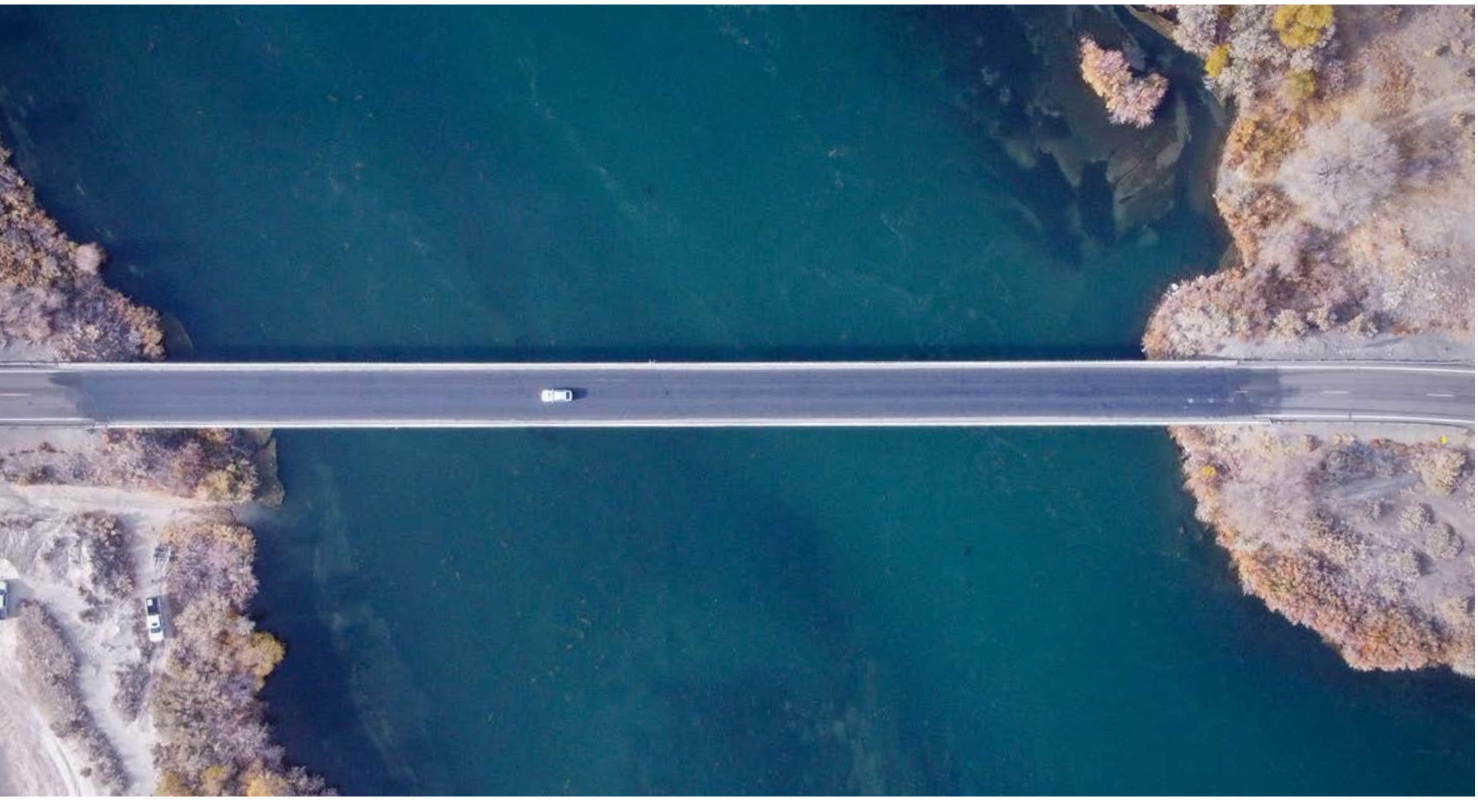
Requirements of blending - One entrepreneur says that the blending requirements of some investments can be difficult.

Grants - Another notes that blending can be thwarted with grant terms. Relatedly, another claims blending failed because funding to date was only grant funding, so investors still saw the enterprise as too risky, despite a large and long-term grant. There is also disagreement between entrepreneurs about whether grants "make a round" or do not really incentivize other investors to join.

One entrepreneur plans to **blend a philanthropic guarantee** in the next and much larger round to encourage commercial banks that might otherwise perceive too much risk in a large round.

Another plans to use "philanthropic money" to **buy back equity**, though it is not certain whether this would take place within a round.

Blending in a round can be very beneficial when there is a clear leader, investors share and streamline due diligence, and they employ a variety of combinations of instruments, including results-based finance. However, blended rounds can also be fragile and challenging, with many investors and requirements to balance. The variety of conversation regarding blending in a round in a sample of just 26 entrepreneurs is a testament to its diversity. These findings shed light on the central role that catalytic impact investors, followed by corporate and charitable foundations and DFIs play in blending, especially in early and growth stage rounds. It also demonstrates the range of views on grants that entrepreneurs bring to blending within a round. This is evident in the variety of design structures involving grants, as well as the challenges that involve them. Finally, this data preliminarily suggests that entrepreneurs with experience blending capital in prior rounds may be able to plan future blending based upon past experience.



B. Blending Over Time

"Sometimes when we talk about blending, we imagine that it's all being blended into one transaction or one moment. But if I think about our history, we get different kinds of capital at different times, because every investor works on their own timescale. It is very difficult to get everybody to move together."

This quote summarizes the way that entrepreneurs often speak about their financing journeys and the relationships they perceive between capital. This is also apparent in noted connections between capitals from different rounds. Even when asked about a particular catalytic or blended investment, entrepreneurs often reference financing that predates that capital or blended round, explaining what allowed them to achieve that investment/round. Often entrepreneurs discuss the relationships they perceive between phases of their financing journey, and the capitals of each, in a holistic manner. Below is an example of such a description:

"It's a constant nudging up the ladder. You started at zero, then you went to a commercial bank with a guarantee. Then you make progress, there's no guarantee required, but then the discount rate is not big enough for you to finance all of your working capital, even though you've given up all of your receivables as security, right? And since then, we've actually now just are doing a debt facility for about [$XXX] million, where the discount rate is finally big enough to finance all of the receivables. But that's a 10 year journey."

The narrative format of blending over time may be due, in part, to the retrospective nature of conversations, and/or due to the interplay of actors, capital and context shaping their journey. Whatever the reason, entrepreneurs discuss grants, investments and rounds in an integrated fashion.

"It's really hard to then separate the catalyst.. the fact that we perform today, we're raising a lot more money. And future grants, actually, now that we've proved what it looks like to open a new office, it's no longer as risky, right? So now, [corporate foundation] catalytic funding can support us in improving our [impact measurement and management], which does have a lot of outlay early on before you're actually getting carbon revenue. So [it].. very clearly sits in a risk thesis. But with a big catalyzing effect, if we can prove the concept."

This quote illustrates how entrepreneurs toggle back and forth between grants, investments, their relation to other capitals and business strategy and growth. This raises a central point for understanding entrepreneurial approaches to blending; blending over time considers not only how blending relates to, enables or incorporates capitals, but how this blending fits within the enterprise's growth, including geographic expansion and expansion of products and services. Thus, entrepreneurial perspectives of blending over time represent entrepreneurs' attempts to merge the financing journey with the evolving commercial and impact goals of the business.

VII. The Capital Provider & Entrepreneur Relationship

A. Capital Provider Roles

Based on the accounts of entrepreneurs, a variety of investors/funders roles are identified below. The roles outlined below are not types, in that they are not fixed or static in their alignment with an investor or funder. An investor may adopt several roles, depending on the investment or the enterprise. This is particularly germane for the varied ways entrepreneurs report that foundations and some impact investors support enterprises. Further, each of these types is neither experienced in a purely positive or negative way, having multiple qualities which also vary in accordance with context.

Capital Provider Type	Capital Provider Role					
Impact Investors / Funds	Commercial with a Twist	Impact Enforcing	Connecting	Advocating	Trend-Setting
Foundations	Transactional	Transformational			
Development Finance Institutions	Wholesaling	Enabling			

Figure 12: Capital Provider Roles by Type

IMPACT INVESTORS

- **Commercial with a Twist** – This role is played by an impact investor that has commercial expectations as well as minimum requirements for social or environmental impact. They may represent greater amounts of money, as well as being more impersonal in relationship to entrepreneurs.

- **Impact Enforcing** – A role that corresponds to specific impact goals and expectations alongside investment. This can be restrictive, difficult and time-consuming for entrepreneurs, although it may also help them to develop IMM practices and standards while still in early stages of business development.

In one scenario, an Impact Enforcing investor was satisfied to see an enterprise sunset, because they were happy with impact attainment, despite financial loss.

- **Connecting** – In this role, impact investors attract other investors to a round or enterprise. They do so through sharing due diligence and at times making introductions to LPs (limited partners). In less favorable instances, they use slow or inexperienced pro-bono resources or collaborate with other investors to establish shared terms that benefit investors disproportionately to entrepreneurs.

- **Advocating** – This role may overlap with the connector role through shared terms, but is more inwardly oriented to the enterprise, providing patient capital, follow-on funding, taking subordinated positions, providing working capital and/or other structures or instruments that support the enterprise.

- **Trend-Setting** – In this capacity, impact investors develop and participate in innovative terms, such as those that include matching incentives, multiple tranches, pairing multiple instruments, such as technical assistance for a particular skill with subordinated debt, for example.

FOUNDATIONS – CORPORATE AND CHARITABLE

- **Transactional** – Associated with the clearly defined parameters of a grant or program-related investment, transactional roles for foundations include grants or investments over a stipulated time in pursuit of specific impact outcomes or business growth. These often one-time transactions can help businesses to center impact, develop a skillset etc. They may cause mission drift without thoughtful consideration of their relationship to the enterprise's overall trajectory.

- **Transformational** – This role highlights changes in the approach of some charitable and particularly a few often-mentioned corporate foundations, that make grants in consideration of and alignment with the company's scalability. As opposed to transactional roles, this role assists enterprises throughout their financing stages. In this role, foundations often pair the grant instrument of a foundation with the long-term perspective of an investor. In this role, foundations may also make subordinated or concessionary investments.

DEVELOPMENT FINANCE INSTITUTIONS

- **Wholesaling** – Entrepreneurs report that development finance institutions provided a large amount of capital to impact funds that invest in social enterprises. The impact fund enables an organization with large amounts of money as a wholesaler to invest in small enterprises, by giving it to smaller funds for the sourcing, diligence and investment processes. Entrepreneurs do not indicate that DFIs' strong reputation and signal regarding reputation reach them via a wholesale role.

- **Enabling** – In this role, direct investments into enterprise–despite long and arduous due diligence processes–are consistently reported to signal an organization's credibility to other investors. Entrepreneurs believe that the reputation of DFIs and their due diligence processes signal their quality to other invesors. DFIs operate in this role more than anticipated, considering the lack of financing for SMMEs.

B. Investor Support for Entrepreneurs

The above section outlines a variety of roles entrepreneurs identify for the investors providing and engaging with catalytic capital in their enterprises. This final section elaborates the type of support capital providers offer to entrepreneurs and connects them to catalytic actions elaborated in prior sections.

Catalytic actions correspond to one of two central types of support- assistive and appreciative[24]. Further, as elaborated in the attributes of catalytic capital, support (or the lack thereof) is codified in the terms of agreement - as flexible, risk tolerant and more. Catalytic capital providers are most often aligned with assistive support to entrepreneurs, with concentration in instrumental support like providing technical assistance. Additional descriptions of support are below:

ASSISTIVE SUPPORT INCLUDES:

- **Informational support** – including concrete information provided to entrepreneurs, which may pertain to investors, impact or business operations, and
- **Instrumental support** – codified in a strategy or instrument, including actions like sharing due diligence and instruments like technical assistance.

APPRECIATIVE SUPPORT INCLUDES:

- **Emotional support** – including respectful communication and guidance, and
- **Appraisal support** – such as assisting an entrepreneur through formal mentorship on business strategy.

While support is evident in catalytic actions and attributes, these qualities also continue to exist in the investor/entrepreneur relationship. While support may be less concrete than actions, attributes or instruments, entrepreneurs' recurrent and varied claims about their relationships with investors–which ranged from challenging to invaluable–indicate the importance of such support throughout their financing journeys. These relationships inform and interact with investment terms, financing rounds and the growth trajectory of enterprises. Findings indicate that the financing experience is optimized for capital users when support is tactical (e.g. helping entrepreneurs to better their practices), as well as considerate of them as humans in need of professional and personal guidance.

VIII. Concluding Remarks

The following questions:

- What does it mean for capital to be catalytic, from the perspective of entrepreneurs?
- How do entrepreneurs blend catalytic and other capitals throughout their financing journey?
- What enables and inhibits entrepreneurs during the early and growth stages of their financing journeys?

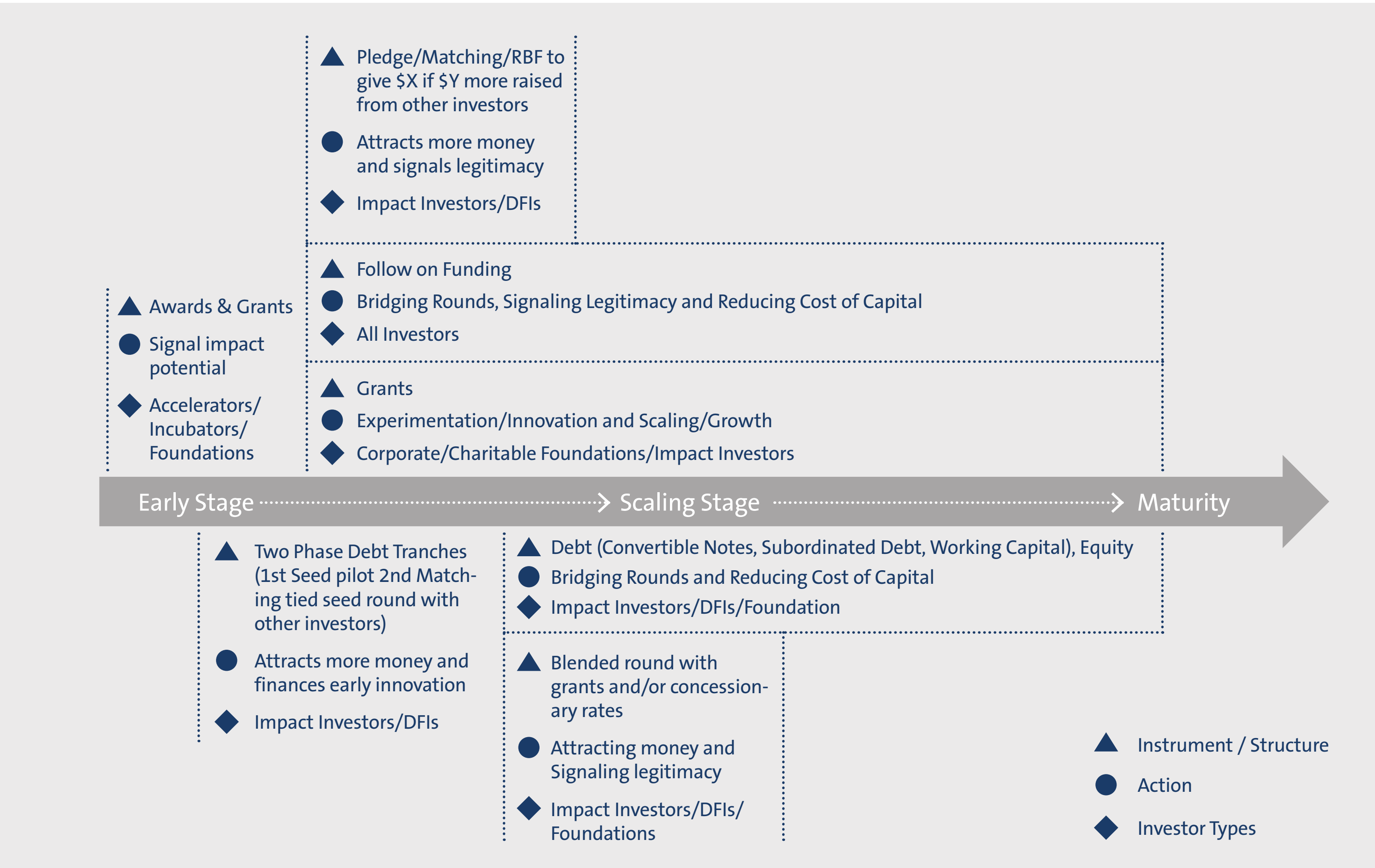
ground this study's approach to the impact entrepreneur's journey. Findings yield support for much of the theory for catalytic capital and blended finance. For instance, of the Catalytic Capital Consortium's articulated uses for catalytic capital, this study particularly corroborates facilitating innovation, leveraging additional capital and signaling impact potential. Further, enabling 'faster' and 'bigger' growth and impact, are qualities of additionality invoked by entrepreneurs. Such alignment suggests that capital providers' intentions for catalytic capital coincide with entrepreneurs' experiences. However, as entrepreneurs indicate, they see a difference between useful and truly catalytic capital and its characteristics and the broader context in which financing occurs requires consideration. For instance, the financing stage, relationships, professional and individual experience, political contexts, impact objectives and more affect the entrepreneurial experience of catalytic capital. It follows that entrepreneurs experience blending capital in rounds and over time in myriad ways that reflect this diversity.

Here is what impact entrepreneurs tell us they value throughout their financing journeys:

- **Introductions** to other field resources and investors
- **Collaborative investors** that lead, share, simplify and/or streamline due diligence processes with other investors
- **Capital structured** to be flexible, efficient, patient, concessionary and reputable for early and growth stage enterprises. Also, capital structured to incentivize additional capital through matching.
- **Blendable capital** in a round and over time more broadly, through reasonable terms, facilitated by grants, concessionary and subordinated positions and using tools like convertible notes. In a round, a clear leader, shared diligence and respect for the entrepreneur, enabling them to continue work on their business.
- **Interconnection between capital and strategy** as evidenced by entrepreneurs' own thinking about blending capital over time. Entrepreneurs think of capital as a tool for developing and growing the business, referencing these simultaneously. Investors who also think long-term and relationally between capital and strategy are key partners.
- **Long-term innovation support** through grants enables entrepreneurs to experiment, innovate and improve, taking risk that equity investors do not want to fund but expect to see from scaled enterprises.
- **Relationships** with investors that respect entrepreneurs' local knowledge of impact, their vision for the enterprise and impact strategy and encapsulate this respect in the terms of the capital itself. The role of the one-on-one relationship is highly influential for entrepreneurs.

With these takeaways in mind, we can begin to imagine some of the ways to assemble catalytic capital in combination with who might provide it and when.While the right combination of these elements will vary in accordance with entrepreneurial need, context, and investor interest and appetite, this diagram below offers several hypothetical combinations of catalytic instruments, corresponding actions and investors that might undertake them. These are loosely mapped to the stages of the entrepreneurial financing journey, but are meant to be interpreted as inspiration. Considering the diversity in catalytic capital and blended finance, there are many more such combinations to identify. Future research can map additional proven or hypothetical cases such as these.

Figure 13: Hypothetical Pairings of Catalytic Instruments, Actions and Investor Types



In closing, this report contributes actionable insight, representing the entrepreneurial voice largely absent in the impact finance space. Though the development of catalytic capital and blended finance supporting social enterprises are still relatively young, there is enough experience to reflect upon and adjust strategy in accordance with the demand side's experience of it. While there are no hard and fast rules to draw from this research, entrepreneurial emphasis on the entire lifecycle of the enterprise, the interconnection of capital and purpose and the central role relationships play remind us that optimizing impact finance is as much the product of experience and context as it is about selecting the right capital at the right time.

A limitation of this study we referred to throughout this paper is the small sample size. While in-depth interviews offer insights into unforeseen topics, uncover important relationships and connections etc. they cannot be generalized as representative. As such, further research into whether these findings hold in larger groups and/or differ by region, sector, or other variable are important next steps in the evolution of thinking about catalytic capital and blended finance.

IX. Appendices

Appendices

Appendix 1:

Conceptual Frameworks for Catalytic Capital and Blended Finance

Catalytic Capital: Investments Prioritizing Impact

The C3's Pathways to Impact framework[25] focuses on structures and actions of such capital, elaborating forms, roles, uses and results of capital. Forms correspond to the structure of the capital, including price, pledge, position, patience and purpose (which briefly overlap with qualities – see patience). Roles relate how catalytic capital can support the investee at different stages of the enterprise's lifecycle. Uses of catalytic capital can facilitate innovation, help build a track record, leverage additional investment, signal impact potential and safeguard mission or articulate a particular action catalytic capital enables. All of these are meant to contribute to enhanced results with amplified social and environmental outcomes.

Figure 14: Existing Frameworks for Catalytic Capital

C3 framework

- Facilitating innovation
- Helping build track record
- Leveraging additional investment
- Signaling impact potential
- Safeguarding mission

CATALYTIC CAPITAL: Pathways to Impact

Catalytic capital accepts disproportionate risk and/or concessionary return to generate positive impact and enable third-party investment that otherwise would not be possible.

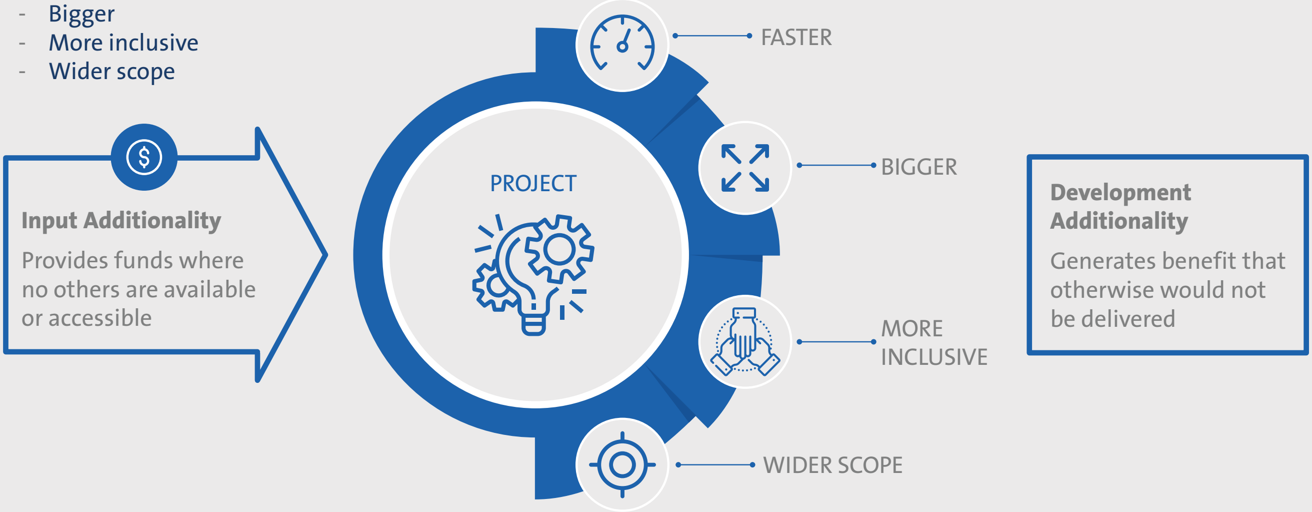
Adapted from Tideline's 'Pathways to Impact' report

Figure 15: Financial (Input) and Development Additionality

Source: AECF (2017): AECF at 8 Impact Report 2016.

AECF framework

- Input additionality – provides funds where no others are available or accessible
- Development additionality – generates benefit that otherwise would not be delivered:
  - Faster
  - Bigger
  - More inclusive
  - Wider scope



While the Pathways to Impact report highlights the importance of the structures and actions of capital, The Africa Enterprise Challenge Fund (AECF)[26] elaborates the relational effect of capital as well as the specific qualities of impact that input additionality (e.g., catalytic capital) enables. AECF describes input additionality –which provides funds where no others are available or accessible—as supporting developmental additionality, or benefits that would not be delivered otherwise. In so doing, the AECF framework demonstrates the relationship, or effect of invested capital and its broader environment. Further, this framework articulates qualities that input additionality enables–a project that is faster, bigger, more inclusive and of wider scope. Such qualities are those we may compare with qualities entrepreneurs report regarding catalytic capital and/or the type of capital that is most fitting for blending.

The AECF framework articulates the relationship between the capital and unit of effect as well as the qualities of impact such investments enable, whereas the Pathways to Impact framework helpfully defines the range of categories for the structures and actions of catalytic capital, complementing. Together, the African Enterprise Challenge and the Tideline and C3 reports offer building blocks for examining the investment of catalytic capital in enterprises, as well as insight into the intention capital providers bring to catalytic capital investments. We will be able to compare the structure, action and qualities of capital explained by entrepreneurs with these frameworks, identifying if, when and how the provider's design and user's experience of catalytic capital align.

Blended Finance: Combining Capitals for Impact

These definitions range in donor/capital sources as well as intended markets and impacts, though they all rely upon concessional capital within blended strategy. Further, while blended finance began by considering blending within a transaction, this is changing. Convergence, the global network for blended finance, for example, lists design-stage grants and pre-investment technical assistance funds as blended finance archetypes, which indicates that blending according to them does not only take place within a single transaction or structure[27]. Additionally, the term "blending over time" is more frequently used[28] indicating a shift in the definitions of blended capital to extend beyond the moment of a transaction.

Despite the variation in structuring approaches and time horizons of blended finance, the collaborative purpose remains largely consistent. As Convergence explains, "blended finance allows organizations with different objectives to invest alongside each other while achieving their own objectives (whether finance return, social impact or a blend of both). Further, the concept addresses the following barriers to private investment: (i) high perceived and real risk, and (ii) poor returns for the risk relative to comparable investments. It generates investable opportunities in developing countries, leading to more development impact."[29]

01. The instruments and approaches of blended finance

Various structuring approaches and types of instruments facilitate the 'blending' of blended finance. In 2020, the proportions of closed transactions by blending approach are structured as follows:

- Concessional capital (85%) - where an investor provides funds on below market terms within a capital structure to lower the overall cost of capital;
- Technical assistance funds (30%) - used to strengthen commercial viability and development impact;
- Risk insurance (19%) - investor provide guarantees or insurance for a transaction at below-market terms and
- Design stage grants (11%) - provided when preparing or designing a project or venture[30].

Instruments may also be considered in relation to their temporality:

Those that blend over time, such as grants or technical assistance, and those that blend within a transaction, such as concessional debt and equity or guarantees. Those that blend over time are utilized with the intention of catalyzing other forms of capital in the future - e.g., technical assistance provided to a social venture so that it is investible for private capital at a later stage. The instruments that blend within a transaction catalyze other forms of finance to join within that transaction - e.g., a guarantee being utilized alongside market rate debt[31].

Blended finance's attention to the financing timeline contextualizes catalytic and blended capitals throughout the financing journey, identifying capitals' structure and role in relation to others as they change over time.

02. Challenges in Blended Finance

Academic research on blended finance confirms the importance of grants and concessionary capital for blended finance deals. However, Moran and Ward-Christie also find the complexity inherent in such combinations problematic. They refer to blended finance deals as "hybrids of hybrids", demonstrating these dual hybrid structures can mask underlying misalignment and conflict with superficial alignment, causing subsequent problems. The study concludes that more research into blended finance and social impact investing is needed, or cautions we will continue to fault those on the demand side rather than the complexity that stems from the hybrid form.[32]

Nevertheless, challenges related to the "hybrid of hybrids" form only exist for those who get blended finance investments. Blended flows averaged approximately $9 billion per year over the past five years, with the greatest volume of deals falling between $100 million and $250 million dollars (approximately 20%). The majority of deals, 51%, fall in the range between $10million and $250million.[33] This suggests blended finance investments are mainly made into infrastructure projects or growth and mature stage companies, capable of absorbing deals of this size and complexity. In fact, Convergence reports only 6% of blended finance deals fall below $5 million, which means many early stage social enterprises are simply too small to absorb a deal such as those counted in the statistic above. However, because Convergence's data comes primarily from blended finance investors, these numbers do not represent transactions occurring at the enterprise level. It should also be noted that some SMMEs may be able to absorb the lower end ($10M) deal sizes.

If blending were to occur in reality only as it is presented in the statistics, it would be particularly problematic because SMMEs requiring smaller deal sizes represent 90% of businesses and 50% of employment worldwide.[34] While the numbers above do not represent all blended finance (blending that happens over time and/or at the enterprise vs. fund level), additional data from the OECD and UNCDF note that there is a significant finance gap in the "missing middle" for smaller sized projects ($50,000 to $1M) in the least developed countries (LDCs). Deals of this size are too small or risky to attract growth capital from conventional investors, and are not supported by DFIs because of the risks or the transaction costs involved. Technical and advisory support are also needed to help strengthen the financial and impact practices of these SMEs. The lack of assistance at this scale means that these organizations struggle to grow and create impact.[35] Such statistics suggest that blended finance ,as orchestrated by investors, is not reaching many of the businesses poised to make contributions to the Sustainable Development Goals.

With insights into the supply side's design of catalytic capital and blended finance, as well as an understanding of how complexity and investor-led deal flow may compromise the potential for effective and impactful investing, we now advance to a discussion of what entrepreneurs had to say about catalytic capital and blended finance.

Appendix 2:
Interview Protocol

The interview protocol was modified for each interviewee. Further, the open-ended format of conversations permitted variation, as some entrepreneurs had more or less to say in response to particular questions.

SECTION 01
Enterprise background and investment context

1. While we have done our homework on _SE NAME_ we would like to hear a bit about the origin and the mission of _SE NAME_.
2. As we mentioned at the outset, we are interested to speak with you today about your experience raising funding. In particular, we are curious to speak with you about your experience with blended finance. For the purposes of this study, we are defining blended finance as raising capital from multiple sources, each of which may have different financial and impact return expectations. These may be structured jointly and intentionally, or separately over time.
   a. If investor known: Specifically, we were hoping to speak with you about _INSERT INVESTOR/FUNDER/YR/_. Could you tell me a bit about the context for that investment? How it came to be?
   b. If investor unknown: Specifically, we were hoping to speak with you about the investment you received for_PURPOSE/YR_. Could you tell me a bit about the context for that investment? How it came to be?
   c. Was this a first, pivotal investment and/or were there others that you think played this role for SE NAME?

Additional Questions:

   d. What was your primary motivation for raising this financing?
   e. If they do not mention attracting additional financing...
      i. Did you hope this investment would attract additional investment?
   f. Were you happy with the negotiation process?

SECTION 02
Deal terms & experience

3. Regarding the deal specifically:
    a. After the terms were agreed upon, did you feel that they fit with the enterprise's needs?
    b. Were there different types of capital blended?
        i. (If no, indicates investor unaware of blending*)
        ii. If so, did these have different purposes and expectations?
            1. Was any of the investment made on concessionary terms?
    c. How specific were investors' expectations regarding impact?
        i. How did they communicate these expectations?
    d. Were the investors' impact and financial expectations realistic?
4. In your experience overall, what are the biggest benefits of this investment?
5. What would you say were or are the biggest challenges regarding this investment?
6. Were you surprised by anything during the course of this investment? Whether about the investment itself, the investors, or other context?

SECTION 03
Experience with the investor(s)

7. How would you characterize the relationship you had/have with the investor(s)?
8. Has your relationship with the investor(s) changed over time?

SECTION 04
Connecting investment to the big picture

9. How could the financing experience be improved for you in the future?
10. Do you have any final thoughts to share about your experience with and opinion of blended finance and catalytic capital investments?

X. Research Team

Bjoern Struewer is founder and CEO at Roots of Impact, a manager of catalytic capital and pioneer in Impact-Linked Finance. After leaving the banking industry he started working closely with public funders, impact investors and philanthropists across the globe to scale high-performing enterprises and innovations with strong potential for impact.

With his team at Roots of Impact he developed pioneering solutions such as Social Impact Incentives (SIINC) and Impact-Linked Finance as well as the Social Finance Academy. He leads the Initiative for Blended Finance at University of Zurich and is Senior Fellow at the Center for Sustainable Finance and Private Wealth as well as mentor at the Harvard Kennedy School’s Impact Investment for the Next Generation Program. He is co-founder of the Financing Agency for Social Entrepreneurship (FASE) and member of various investment committees and advisory boards.

Jed Emerson has authored 8 books on social entrepreneurship and impact investing, including co-authoring the first book on the topic of impact investing. His research while in academic appointments at Harvard and Stanford Business schools (2000-2004) into Blended Value, and what is now called impact investing, has been viewed as seminal in the field.

Jed recently joined Tiedemann as the Global Lead of Impact Investing after serving on the Firm’s Impact Advisory Council. He serves as Senior Fellow at the Center for Sustainable Finance and Private Wealth as well as the Initiative for Blended Finance at the University of Zurich and as Senior Research Fellow at the University of Heidelberg’s Center on Social Investment and serves as Senior Fellow with both ImpactAssets and Toniic.

Kirsten Andersen, PhD is an independent researcher and research partner of Roots of Impact and the Initiative for Blended Finance at the University of Zurich. She is trained as an economic and organizational sociologist and uses qualitative methods to identify valuation and meaning making in impact invest- ing and sustainable finance more broadly. Her recent research projects include interview studies with American foundation impact investors’ assessments of social and financial values, and an examina- tion of impact investors’ perceptions of impact-linked finance and catalytic capital. She is also the Resident Social Scientist at Impacto Consulting. Kirsten has an MA and PhD in Sociology from the University of Illinois at Chicago and a BA from University of Pennsylvania. She worked as a fundrais- ing consultant for non-profit organizations prior to her doctoral work.

Taeun Kwon is the research lead for the Initiative for Blended Finance at the University of Zurich. Her current research projects include innovative financing in water, education, and sustainable landscapes. She was also the lead of the “Sustainable Investing Capabilities of Private Banks” research project and report at the Centre for Sustainable Finance and Private Wealth (CSP). The project investigates the largest wealth managers in Europe in regard to sustainable investing. Before CSP, Taeun had launched her own ethical t-shirt brand and worked in consulting at Boston Consulting Group, TBWA\, and Impact Square.

Barry Panulo is Senior Project Manager at the UCT GSB Bertha Centre for Social Innovation and Entrepreneurship and is active in the Centre’s Innovative Financing initiative. His portfolio of work centers on developing Outcomes-based financing mechanisms and he delivers transaction structuring and advisory support for commissioners exploring Outcomes- based projects across a variety of development sectors. Barry was instrumental in the set-up of the first Social Impact Bond in Southern Africa, and advises to governments on the use of University of Zurich, IBF August 2021 outcomes-based funding. Barry is a CFA Charterholder and earned B.Bus.Sci(Finance) and MCom(Investment Management) degrees from the University of Cape Town.

Rowan Spazzoli is an innovative finance researcher and systems thinking consultant at the Bertha Centre. He runs an economic development consultancy, Accendio, which focuses on entrepreneurial support and small business finance. Rowan is a lecturer at the University of Cape Town in the Department of Management Studies, where he has taught business strategy for 6 years. He is a co-founder of Phaphama SEDI, an NGO that helps micro-entrepreneurs in Cape Town townships, and Loadalot, an innovative logistics company. Rowan is deeply passionate about social entrepreneurship and the financing mechanisms that can enable it, and has developed various business programmes alongside Viridian and Yunus Social Business.

Kirsten Amsterdam is a project manager in the Innovative Finance Team, at the Bertha Centre, with a focus on Early Stage Finance. Previously she worked at UCT’s Research Contracts and Innovation (RC&I) department, TEDI project and IDEA research unit at UCT, Kantar TNS, and the Western Cape Department of Economic Development. She completed her Masters in Development Finance at UCT’s Graduate School of Business with distinction in her dissertation focusing on the effect of financial innovation and it’s effect on economicgrowth in African countries. Kirsten is experienced and skilled in development research, market research and research project management, working on and managing multiple research projects and developing and presenting research, progress and financial reports to both clients and funders.

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What's in it for the Entrepreneur?

An entrepreneurial perspective of catalytic capital and blended finance

Initiative for Blended Finance at the University of Zurich

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