

SEEDING THE FUTURE

Challenge and Opportunity in Early Stage Impact Investing

An ImpactAssets issue brief exploring critical concepts in impact investing

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PRÉCIS

To meet a promising entrepreneur, be convinced that their venture will thrive in the market, and subsequently invest at the ground floor leading to outsized returns; this is the exciting vision of seed stage investing. Although a risky proposition, it has nonetheless attracted many investors who want to take those bets realizing that their capital may be the only chance these ventures have to build and grow a potentially great solution. An entire ecosystem of venture capital and angel investing has been developed to support seed stage technology startups and other companies with large scale potential. As the market for impact investing has grown, however, seed stage investing has not kept apace, consequently limiting the deal pipeline.

By taking a closer look at the landscape of seed stage investing as perceived by the diverse players involved, this Issue Brief aims to unpack the layers of complication around seed stage investing and illuminate opportunities to close the gap between early opportunity and investor appetite. Interviews were conducted in early 2013 with entrepreneurs, accelerator leaders, seed stage funders, and foundations that are committed to the continued development of the seed stage ecosystem of impact investing. Supporting a robust pipeline of social ventures is critical to the growth of impact investing and social entrepreneurship, and the challenges that currently exist in seed stage financing present opportunities for innovation.

INTRODUCTION

The assessment that there is a gap in impact investing at the seed stage¹ has been made by many leaders within the field² who have suggested a range of possible causes. Interviews were conducted in early 2013 with entrepreneurs, accelerator leaders, seed stage funders, and foundations that are committed to the continued development of the seed stage ecosystem of impact investing. Some believe social entrepreneurs need capacity building support to make their ventures “investment-ready” and point to accelerators or incubators as a solution. Others advocate for philanthropic dollars to fill the funding gap while an organization tests its product and establishes a customer base. On the capital side, many interpret the seed stage gap as an investor issue; the economics of investing in a round of \$500,000 or less in an early stage social

venture just don't make sense considering the extensive due diligence, term sheet negotiation, and ongoing monitoring of investments as needed. In addition, it can be very difficult to generate the deal flow to match an investor's financial and impact-based expectations as well as their geographic or issue area focus.

Compounding these issues, the whole discussion can be somewhat opaque, with little visibility into funds, investors, ventures, and deals within the seed stage landscape. This creates a level of uncertainty and reluctance to invest in the absence of such transparency and data. Each of these factors contributes to the frustration experienced by both investors and entrepreneurs trying to increase funding flows between impact investors and promising social entrepreneurs.

CHALLENGES IN SEED STAGE IMPACT INVESTING

There are a multitude of sound reasons why many investors have not pursued seed stage investing in the impact space. By taking a closer look at those reasons, this daunting gap can be broken into specific obstacles so that the needs and concerns of investors can be more directly addressed.

Risk Return Profile

Any early stage investment, especially seed

funding, is a fundamentally risky investment. The way this type of risk has traditionally been managed is by making many “tiny bets” and thereby playing the odds that, through wide diversification, one of those bets will result in generating the exponential returns that more than compensate for any lost investment in the other investments of an angel portfolio. For this approach to make sense, all of the initial investments must have the potential

¹ For the purposes of this paper, we will consider seed stage to be a venture that is raising an amount of capital less than \$500,000 with little to no revenue recognition.

² The seed stage investment gap has been raised in reports including *Blueprint to Scale* (2012) by Acumen Fund and Monitor Group and *Accelerating Impact* (2012) by The Rockefeller Foundation and E.T. Jackson Associates

to scale up and produce a return of multiple times the invested seed capital, although only a small percentage will actually do so.

This presents a challenge for seed stage impact investing because the return on the investment is not purely financial. Both the social and environmental impact of social ventures may dramatically outperform previous solutions, but many of these ventures will still have fairly slow and steady financial growth; many more will sputter out, as is true of their conventional counterparts. In fact, the slow and steady growth pattern is a commendable outcome that produces financial return and sustainable impact. These are great impact investments, but someone still has to take the risk of the seed stage investment, before the model is proven and financial returns generated. There are investors who are willing to take that chance, but it is with full recognition they are taking on high risk that may not have correspondingly high financial return.

There are, thus far, few social ventures that have produced the kinds of multiples of financial return on investment that the venture capital industry has experienced in traditional sectors, especially technology and web-based business models. And more importantly, the objective of impact investing is different from traditional investing at its core in that it seeks both financial and social or environmental returns. Impact investors are accepting both

impact risk and financial risk, and should subsequently evaluate return with a blended value³ approach. These investors may also have good reason for ignoring traditional investment guidelines, as it's unlikely that modern portfolio theory is going to solve our global challenges.

The long term outcomes and risk-return profile of seed stage impact investing are still somewhat of an experiment at a cultural and market level, with each funded venture providing a new data point. As part of the enthusiasm for social entrepreneurship and impact investing, more and more individuals are being drawn to early-stage solutions that have the potential to build a better world. However, they want some benchmarks around risk and return. Better market-wide data on the aggregate return profile of seed investing will allow investors to make informed decisions regarding the risks they must be willing to take to realize future impact.

Investment Size and the Realities of Allocation

As a risky investment, the allocation to seed stage investing is typically a small percentage of an investor's portfolio. Within that limited allocation, a common way to decrease the risk is to diversify with multiple small investments, as mentioned previously. An investor with \$1M might reasonably allocate \$200,000 to alternative investments (a healthy percentage). Even if all of that is allocated to impact invest-

³ Blended Value is the idea that the value created by an organization is fundamentally indivisible. Thus, one cannot speak of simply "economic value", "social value" or "environmental value"--these quantities are simply parts of one essential value. This term was coined by Jed Emerson and additional work related to the topic is available at blendedvalue.org

ing likely no more than 25% would be for early stage seed stage investing, or \$50,000. With reasonable practicalities related to transaction size, this would yield investment in at most one to two ventures, which does not provide sufficient diversification. This inability to diversify risk may decrease investor appetite for such an allocation.



Excerpt from *Mission in a Bottle*, by Seth Goldman & Barry Nalebuff. *Crown Business*, September 2013.

For an entrepreneur trying to raise a seed round, a significant amount of time goes into cultivating each investor. The relatively small

amount that they are trying to raise (average range of \$250k – \$500k) falls below the range of consideration for large investors, and raising money from individuals results in piecemeal investments requiring significant time of both entrepreneur and investor. Identifying an investor who can make a sizable contribution of capital out of a diversified impact portfolio is a clear challenge for seed stage ventures.

Expense to Source, Analyze, Monitor Deals

Closely tied to the challenges of investment size, there is often a disproportionate expense associated with making seed stage investments. Regardless of size, these investments must be sourced, undergo thorough due diligence, be negotiated on various terms and be continuously monitored after the initial investment. The process is very time consuming and requires special expertise; this level of work could be a part- to full-time job. The expense of a single deal is potentially even greater for seed stage investments because the business models are less developed, often requiring additional research and conversations to establish confidence in the investments.

These costs do not scale in relation to the size of the investment, which makes seed stage investments very expensive relative to the capital that is being put to work. One of the key reasons that large investors do not consider investments below \$500,000 is that the economics of those deals don't make sense, whereas the same costs are easily accommodated for a multi-million dollar investment. There is a clear need to streamline seed stage

The concept of Village Capital was a response to the prohibitive expense of sourcing and vetting early stage deals. Peer selection as a way of awarding capital, which has had promising results in micro-finance, was identified as a process innovation that could reduce some of the administrative cost of seed stage funding.

— Ross Baird, Village Capital

investing; to shrink the hurdles between an investor who believes in the potential of a social venture and their ability to make and monitor an investment.

Lack of Information

One of the most time-consuming aspects of being a seed stage investor is the amount of hunting, gathering, and reinventing the wheel that is done because of a lack of transparency and compiled information. The information gap starts with sourcing investments: while platforms where entrepreneurs can post their ventures and seek financing do exist, many entrepreneurs don't know about this fundraising option. For example, an entrepreneur in education technology may not even know of the field of impact investing, much less think of posting a profile on the Gust platform⁴ as a necessary step in raising capital. Additionally, many investors don't find the level of detail that they need through those sites and are unlikely to be inspired by or spend the time required for sifting through online profiles;

they want to simply and easily connect to a story that aligns with their values and interests.

Once a connection is made between an entrepreneur and an investor, there is likely a lack of information about the venture, due to its early stage. Such is the nature of the seed stage game, but it requires that investors seek analogous sources of information about the founder, the team, the product viability, the market, which requires quite a bit of research and creative analysis. Many investors simply do not feel comfortable investing in businesses that don't have robust information supporting their model, which will be an ongoing limitation in recruiting seed stage investors.

And even if the courtship between entrepreneur and investor makes it all the way to a proposed investment, both parties can experience some trepidation upon realizing that they don't know what the "norm" is in early stage impact investing deals. Lack of transparency

For the early-stage social entrepreneurs that we select for the Echoing Green fellowship, we have found that a track record of leadership, resilience, passion, and the ability to attract resources are very reliable indicators of an individual's potential. Identifying high impact seed stage social ventures requires a creative approach to connect to the entrepreneur and share their vision.

— Lara Galinsky, Echoing Green

⁴ Gust (<http://gust.com/>) provides a global platform for the sourcing and management of early-stage investments.

For both the entrepreneur and the investor, resources are lacking to guide the process of making a deal; there just isn't the volume or history of deals that exists in traditional angel investing. Every impact venture is unique in its geography, issue area, business plan, and fundraising needs, which makes it challenging for entrepreneurs to find aligned investors and then to figure out terms that work for both sides.

— Tyler Hartung, Unreasonable Institute

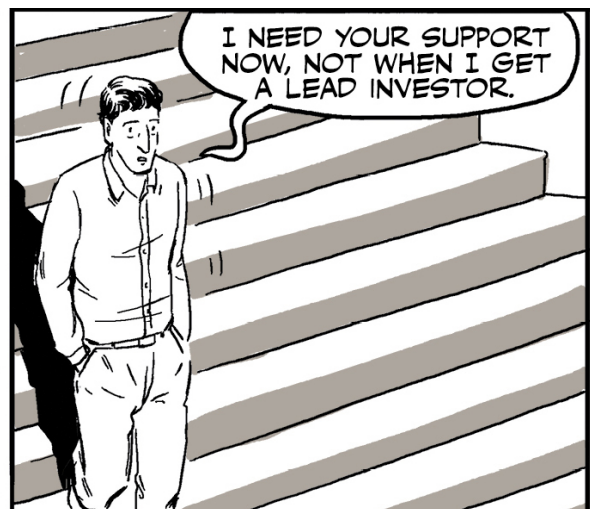
into what deals are being done within impact investing has left both investors and entrepreneurs without a benchmark or range of outcomes to orient themselves in a negotiation. Especially in the challenging effort to evaluate blended value, guidance and additional data is needed to strengthen the field.

Investment Readiness

The cause most often cited for the gap in seed stage impact investing is lack of investment

readiness by social ventures. This has prompted the rise of accelerators and incubators tailored to social enterprises, to fortify their business plans, make their financials presentable and polish their pitches. We have only seen the beginning of a wave of social enterprises that will require extensive mentoring and support to develop into viable impact investments. The efficiency with which high-potential ventures and strong leaders can become investment ready is what will set the pace of deal flow. Many investors feel that current demand is outpacing the supply of investable companies.

To be fair, investment readiness also applies to investors. One of the strengths of the venture capital industry is that practitioners are quite ready to invest when an opportunity presents itself and are unabashed in turning away ventures that do not meet their criteria. When an investor makes a personal connection to a social enterprise based on its impact, however, they may extend the conversation with an entrepreneur even if an investment is not on the horizon. This is wasted time that the entrepreneur could spend cultivating other seed stage



Excerpt from *Mission in a Bottle*, by Seth Goldman & Barry Nalebuff. Crown Business, September 2013.

capital and muddles expectations and relationships within the market.

Lack of Scalability

Without the infrastructure to reduce the friction and widen the margins, the gap in seed stage investing will remain. Each deal faces all of the challenges explained above, and the next deal doesn't get any easier for either the entrepreneur or the investor. For the best

impact ventures to have a chance at success, dramatically more seed stage companies need to be given a chance, which will not happen with the lack of scalability of the current process. Innovations in how to seed many diversified early stage ventures at low cost and with a sustainable return on the portfolio are needed to catalyze a steady flow of capital to potentially powerful solutions.

INSIGHTS FROM THE FIELD

There is an ecosystem in development to support the growth of early stage social ventures. This network of players is deeply familiar with the challenges described above and is on the front lines of addressing the gap in seed stage investing.

Entrepreneurs

The hallmark quality of entrepreneurs (dogged perseverance!) is at the core of their experience raising capital. Speaking to entrepreneurs who have raised seed stage capital, many feel they have collectively taken every feasible path to find those funds. Support from bootstrapping, family and friends, crowdfunding campaigns, fast pitch competitions, charitable contributions through a fiscal sponsor and personally secured credit cards and bank loans are all pursued and strung together until the entrepreneur can raise funds from a well-matched set of investors.

Entrepreneurs are willing to admit that it can be more challenging to communicate

the competitive advantage and exit strategy of a social venture. However, they also feel many investors are unprepared to evaluate a blended value proposition. Somewhat surprisingly, some social entrepreneurs find raising capital to be more efficient through traditional capital sources than through impact investing networks, because the feedback and decision-making is faster and more direct. In our interviews, entrepreneurs generally felt that raising money from impact investors was hard to do,

My partner and I have had to roll with the punches and track down every source of capital available to us. Sometimes a really promising investor disappears without explanation, and other times we have been surprised by a much larger investment than was anticipated. We've learned a lot, but securing funding has been a roller coaster.

— Carrie Ferrence, Stockbox Grocers

both in identifying aligned investors and having to reach a higher bar for demonstrating both financial and impact potential.

As critical as passion and vision are to any social enterprise, they don't pay the bills. Entrepreneurs are forced to perform a harrowing juggling act in which they try to balance customers, vendors, employees and (occasionally) life, on little more than fumes. A significant and respected funding partner who can provide an early stage mission-driven venture with the capital and the resources to break through could make the difference between liftoff and letdown.

— Seth Goldman, TeaEO, HonestTea

As for business plan contests or fast pitch competitions as a way of attracting investors, the evaluation is that these are helpful for building awareness of the brand, but don't often lead to meaningful investor relationships.

Entrepreneurs are scrappy and resourceful and many are finding ways to bridge the seed stage investment gap. Even the most experienced entrepreneurs, however, are having trouble raising money from impact investors for a multitude of reasons as articulated above. Although it is important for an investor to understand the risk that they are taking with their capital, investors would also be wise to respect the huge risks that each entrepreneur

takes to pursue their impact venture, truly leveraging every resource they have to affect change.

Seed Funders

Not surprisingly, those running seed investment funds are passionate about channeling capital to early stage ventures. They emphasize that this is exciting and important work which too few investors have committed to, and that even those who are already doing seed stage investing should be placing more capital faster. Seed funds anticipate that many of their investments will fail, they know that the ventures will require extensive mentoring and support, and they are willing to accept proxies as evidence of an entrepreneur's capability and potential. This is not the right business for anyone who is looking for a sure bet or a detailed plan; it is a game of diversification and faith. Although seed funds build their portfolio by approaching each deal with investment integrity, they are consciously providing the risk capital that precedes market validation of any given business model or idea.

Of course seed stage investing is risky, but it can also be the most catalytic. We won't always pick winners, but we are learning by doing and helping important social ventures get the early support that they need.

— Andy Lower, Eleos Foundation

Seed funders have found that their best investments are often sourced by referrals from prior investees. Many of the strongest prospects don't identify as social entrepreneurs or even realize that there are investors specifically seeking social or environmental return. An entrepreneur getting a new business off the ground oftentimes looks to his or her peers for actionable business advice rather than spending time to understand the landscape of investors. For this reason, established entrepreneurs

often have the first glimpse into the next great businesses. To identify promising early stage deals, seed funds have built field networks, in addition to their portfolio companies, to gather this street level intelligence.

Some seed funders are foundations that make debt and equity investments in social enterprises as a way of putting more than just grants to work to pursue the change they seek in the world. Other seed funders raise capital from outside investors to build a fund. The investors in a fund are generally interested in supporting seed stage impact ventures but would rather pay a fund manager to do the sourcing, vetting, and monitoring of the investments. Fund managers have found that for many of the investors in these seed funds, this is their first impact investment and often comes out of their philanthropic capital allocation.⁵ While they are still taking on the risk that an early stage investment carries, a fund manager serves as both an efficient way to gain diversity and a trusted filter for promising ventures.

While sourcing potential investments in India, we have found that many of our best leads are referrals from other entrepreneurs. They are businesses that we never would have found through an accelerator program or other networks in the impact community; many of the best impact investments don't even think of themselves as social entrepreneurs.
— Dave Richards, Unitus Seed Fund

⁵ This refers to the common practice of separating out capital that is intended for philanthropic use from investment capital. Although impact investments are made for financial return, many individuals new to impact investing make these investments out of their philanthropic capital because it is in service of social or environmental impact — and they are unsure how best to manage their investments for serious financial performance.

Coming from Experience: An Investor Perspective

Jed Emerson has long been in conversations with entrepreneurs and impact fund managers trying to match capital to ventures to execute their respective strategies. As a founding board member of Pacific Community Ventures, a past advisor to sustainable private equity investment funds, convener of ImpactAssets' IA50 and now senior advisor to three family offices — each of which is executing significant, multi-million dollar impact investment strategies — he has had many discussions on the complicated dance between impact investor and social entrepreneur. From an investor perspective, the challenges are often due to Capital Mismatch, Moving Targets, or Limited Capacity.

Capital Mismatch: Right Deals to Wrong Capital

Too much time is spent by entrepreneurs pitching the right deal to the wrong capital. Some of this challenge is simply a function of bad information in a fragmented market that is still being formed, but sometimes an investor doesn't know until sitting down with an entrepreneur that the money they have to allocate (and more importantly, the terms of investment that capital carries) simply doesn't fit the deal being presented. Just as often, however, entrepreneurs seeking capital have not done their homework to try to understand what the asset owner's strategy is or what kind of capital they have to invest at that time. Often times entrepreneurs don't even bother to ask what the specific investment strategy or appetite of an investor is before launching into a pitch or positioning for a meeting that wastes time and causes frustration on both sides of the check book.

Moving Targets: Investors' Evolving Strategies

Compounding the complications of an effective capital raise is the reality that many investors are on a journey, exploring investment strategies and thematic areas. As interests and focus areas are refined, ventures that investors may have initially been interested in no longer fit upon further inquiry. Investors develop greater expertise and understanding of what they can and cannot manage as a portfolio evolves, and subsequently adjust their practices. While investors do owe it to those seeking capital to be as transparent as possible with regard to where they are in their evolution, it is often in the actual deliberations of investment committees that impact investors realize why a specific deal either is or is not a fit for them. The development of an investor's strategy over time, as they make investments and learn more about the market of investment opportunities as well as their own abilities and interest to invest, makes for a moving target to be hit by the entrepreneur hunting for capital. While this is frustrating, it is also the sign of an evolving market place that ultimately bodes well for the field.

Limited Capacity: The Need for Smart Money

While many entrepreneurs feel themselves to be simply in need of cash, that is rarely the case. Especially at the very early stage, what is required is a strong, engaged anchor investor and a prospective investor may decline because she or he simply does not have the skills, time or expertise to act in that role. As an early stage entrepreneur, it is short-sighted to take money from investors who are not in a sound position to contribute their talents to making the venture a success, leveraging their experience and networks. If an investor says that they will only consider investing once an experienced anchor has signed on, they are often times communicating something about themselves and their ability to contribute and support the greatest chance of success. It is frustrating to hear, but good entrepreneurs know it is not simply a question of finding money, but rather the need to find smart money!

Ecosystem Funders

There are major funders behind the growth of impact investing, and they have been thoughtful about the various components that need to be developed to create sustainable social capital markets. In preparation for a rapidly growing capital base, a continued focus is placed on building metrics, measurement and infrastructure to support institutional investment in impact, but it has become increasingly

It is widely agreed that there will always be a role to play for philanthropy in bridging the seed stage gap for social ventures. For example, in areas with entrenched poverty and/or hard-to-reach populations, the returns will rarely compensate for the time and risk of those market-leading investments, and philanthropists can serve a critical role in supporting early stage ventures with high potential for impact at scale.

Rockefeller Foundation is devoted to impact investing as a driver for global change, but we feel just as strongly that philanthropy will always have a role to play in supporting seed stage social entrepreneurs. Many of these ventures address market failures or function in parts of the world where markets are undeveloped. There is an ongoing need for philanthropic capital to sustain social ventures that are having impact, but may not have a clear financial return.

—Brinda Ganguly, Rockefeller Foundation

Another response from ecosystem funders, however, is that the seed stage gap is largely a perceptual problem, caused by definitional issues around impact investing, lack of transparency, and a shortage of resources to connect entrepreneurs to investors. Funders with this point of view support infrastructure investments in mapping seed stage deals, increasing accessibility for individual investors, and innovative products and services that give both entrepreneurs and investors a wider range of options for the flow of capital.

I don't think that we fully know if there is a gap in seed stage funding for social enterprise until there is more visibility into the deals that are happening, regardless of whether they define themselves as impact investors or not. Mapping the space and promoting information sharing to create additional transparency for those interested in these markets is a critical step to alleviate the perceived seed stage investing gap.

—Sonal Shah, Senior Fellow, Case Foundation

obvious that resources need to be directed towards the gap in seed stage investing, as well. Funders of the impact investing ecosystem are aware of this gap, but they have differing opinions regarding the causes. Each funder's respective point of view informs their funding in this area.

Accelerators

Social entrepreneurship continues to attract more individuals across the world that see a need in their communities or in larger systems and feel empowered to respond. Many of these individuals have not run companies or received any business training. Those who followed the rise of early social entrepreneurs quickly realized that mentorship, introductions to key contacts, and basic management training would accelerate the growth and impact of these ventures. Venture philanthropy has been accompanied by capacity-building services and strategic consulting and continues to accelerate the growth of many scalable, high-impact social ventures.

As for-profit social ventures have become more prolific, the accelerator model that has been celebrated in the venture capital community (prime examples being Techstars and Y Combinator), is being adapted to social enterprise. The model of an accelerator is to accept a high-potential cohort of start-ups into the program, power through early stages of business development, connect the ventures with expert mentors in their industry, and gather investors for a rigorous pitch event at the end of the program. For the value they provide during the program, the accelerator receives a relatively large equity stake for a small investment.

The research for this Brief revealed a variety of philosophies behind social impact accelerator programs. One was designed as a process innovation for identifying and vetting early stage

The primary focus for Agora is supporting early stage entrepreneurs because that is where we believe we can have the biggest impact, and frankly, it's in the very young companies where the most innovative multi-stakeholder business models are being created. These entrepreneurs are passionate and innovative but they are still small; the right mix of knowledge, networks, and capital can significantly accelerate this critical group.
— Ben Powell, Agora Partnerships

investments at a lower cost, another one is taking a whole systems approach in a particular industry to spark innovation at critical gaps, and a third is primarily seeking equity return with a strong impact filter. Terms vary widely as well, with one accelerator basing its investment on future revenues rather than an equity stake, due to a perception that exits may be uncommon for social ventures. Many have a blend of these philosophies and they are all trying to support social entrepreneurs to establish a more solid footing and connected network to increase their impact.

Entrepreneurs come into these programs with a wide variety of strengths and weaknesses. Both selection and curriculum have evolved to tailor the accelerator training towards investment readiness. All of the accelerators described a clear need for training entrepreneurs about different types of capital, the pros

and cons of each, and how to put together a pitch that speaks the language of investors. Even with a clear ask and solid pitch, however, identifying high potential matches of investors to ventures is challenging because there is so much diversity in investor focus—across geography, issue area, asset class, stage, investment type. Accelerator leaders see a need

As the market has developed for impact investing, there has been an over-investment in helping big investors and an under-investment in helping small investors, and critically, entrepreneurs. The future of the impact investing movement is in the hands of entrepreneurs, not investors, and the sooner we can inspire, support, and finance the next generation of entrepreneurs, the better.
— Ben Powell, Agora Partnerships

for investor training as clearly as the need for enterprise development, and have cultivated the investors in their network over time to build confidence in the accelerator, adding a layer of familiarity and due diligence to ease the investment process.

Many entrepreneurs perceive accelerators as an expensive service. Although accelerator programs generally provide an investment along with technical assistance, introductions, and relationships that come out of their networks, that is in exchange for a relatively large equity stake. Although entrepreneurs generally agree that they could use training and mentorship to refine their pitch, get their financials in order, and evaluate various funding options, some believe the 5-8% of equity stake taken by an accelerator program in exchange for an investment of \$25,000 is prohibitive.

(See table page 13)

SEED STAGE CAPACITY BUILDING*

ORGANIZATION	WEBSITE	HQ LOCATION	ANNUAL COHORT SIZE	CUMULATIVE VENTURES SUPPORTED	PROVIDES EARLY STAGE CAPITAL
Agora Partnerships	agorapartnerships.org	Nicaragua	30+	50	
Artemesia Social Business	artemesia.org.br/eng/	Sao Paulo, Brazil	6 - 8	15	X
Ashoka	ashoka.org	Washington, DC		3000	X
Civic Accelerator/ Points of Light	pointsoflight.org/civic-incubator/programs/civic-accelerator	Atlanta, GA	10	10	X
Code for America	codeforamerica.org	San Francisco, CA	28	74	X
Dasra	dasra.org	Mumbai, India	50	132	X
Echoing Green	echoinggreen.org	New York, NY	20+	500	X
Ecsel	ecselfellows.org/en/	China	30	100	
Fledge	fledge.co/	Seattle, WA	7 - 10	14	
Future of Fish	futureoffish.org		4 - 5	11	
Global Social Benefit Incubator	scu.edu/socialbenefit/entrepreneurship/gsbi/	Santa Clara, CA	20	180	
GoodCompany Ventures	goodcompanygroup.org/residency/program	Philadelphia, PA	12	45	
Greenstart	greenstart.com	San Francisco, CA		17	X
HUB Ventures	hub-ventures.com	San Francisco, CA	8 - 10	23	X
Ideaccelerator/ Idea Village	ideavillage.org	New Orleans, LA	15 - 20	60	
Impact Engine	theimpactengine.com	Chicago, IL	8	8	X
NESsT	nesst.org	San Francisco, CA		58	X
New Ventures	new-ventures.org/	Washington, DC	25+	367	
Rainer Arnhold Fellows	rainerfellows.org	San Francisco, CA	8 - 10	71	X
Rock Health	rockhealth.com/	San Francisco, CA	14	49	X
Unreasonable Institute	unreasonableinstitute.org	Boulder, CO	22 - 26	70	
Venture Greenhouse	venturegreenhouse.org/	San Rafael, CA	12	35	
VentureWell	venturewell.org	Boston, MA	16	16	X
Village Capital	vilcap.com	Atlanta, GA	15 - 17	300	X
Villgro	villgro.org	Chennai, India	12	29	X
William James Foundation	williamjamesfoundation.org	Washington, DC	15 - 20	200	

* This table is not exhaustive but represents the majority of accelerators for social entrepreneurs as well as other organizations that are focused on building capacity for early stage social ventures. This table does not include seed stage investment funds.

OPPORTUNITY

While the gap in seed stage investing is frustrating to entrepreneurs and impact investors alike, this challenge does not require a large shift of capital to move towards resolution. A rough analysis indicates that allocating \$60MM — less than one percent of impact investing assets — to seed stage investing would significantly reduce the gap.

How can we estimate the capital needed to advance promising seed stage social ventures to the next level? There are about 30 established social venture accelerator programs that receive a few hundred applications for each cohort. There is overlap between these application numbers as well as other ventures that have decided against applying to these programs, but it would be reasonable to estimate

the number of early stage social ventures at around 6,000 annually. Out of their applicants, accelerators end up with cohorts of around 8-20 ventures. Some of these programs accept non-profit ventures, which are looking for grant funding but not an equity-like investment, so an estimate of ten for-profit ventures per cohort from 30 accelerators results in about 300 investable companies annually that are vetted by and accepted into these programs. Most seed stage ventures are seeking funding in the range of \$50k - \$400k, so if we estimate the average at \$200k each the total capital needed to give all of these 300 ventures the funding to fuel them to the next stage is only \$60MM per year.

POTENTIAL SOLUTIONS

After taking a closer look at the barriers to seed stage investing, gaining insight into the way various players in the ecosystem see the issues, and understanding the relatively small amount of capital that could dramatically alleviate the seed stage impact investment gap, it is clear that this is an area ripe for creative approaches. There is not one solution to the seed stage investing gap; there are many tactics that will come together to enhance the landscape.

- ***Improve the economics of seed stage investing*** by decreasing the time and expense of due diligence. Collaborative angel groups and investment platforms such as Investors' Circle and TONIIC have made an effort at sharing information among investors but there need to be other ways to outsource due diligence or streamline the process through intermediaries.
- ***Enable investors to make tiny bets, facilitate diversification and increase the number of investments*** by leveraging the energy around crowdfunding, new accredited angel

investor online platforms and donor advised funds. Additionally, the JOBS Act⁶ has the potential to open up the retail investor market to seed stage impact investing.

- **Address concerns about risk and return with financial product innovation.** For example, donor advised funds (DAFs), a \$30B capital pool, could be a source of seed investing capital, as well as private foundations with more than \$600B in assets. Since investors receive a tax deduction when they open a DAF or fund a private foundation, they could view the tax benefit as an initial “return” of sorts at the point of investment.

Seed stage social venture funds are springing up from new places, such as non-profits, traditional venture capitalists, and accelerators. This may attract new investors who are willing to pay a management fee rather than spend the time and effort to source their own seed stage deals. Each will bring a different lens to their investment approach and will diversify the capital available to entrepreneurs. Accelerators are iterating their models to more acutely match entrepreneurs with investors and providing ongoing services to support

follow-on financing. Additionally, relationships between seed funds and accelerators are being developed which will provide a more immediate and ongoing feedback loop between entrepreneurs and investors, in addition to the more efficient vetting resulting from accelerators sharing experiential knowledge of the founding teams and their ventures.

Creative thinking around intermediaries, platforms and products will provide ways for investors to come in at lower levels and at enhanced levels of diversification and subsequently unlock a new group of investors who may also have a more flexible view of investment readiness. There are also unexplored areas of improvement that could reveal powerful solutions in sourcing, vetting, monitoring, mapping, reporting, networking, entrepreneur capacity-building, investor training, and many other areas of this ecosystem. Identifying and developing those solutions will close the seed stage investing gap and strengthen the deal flow across impact investing by providing a more efficient way for promising social ventures to move from concept to market.

CONCLUSION

Going a layer deeper into the widely perceived seed stage impact investing gap to look at its component parts reveals that the dysfunction comes not from any deeply rooted misalign-

ment but from surface level friction. Both building and investing in blended value business models require a new kind of expertise that is being developed with each impact

⁶ The Jumpstart Our Business Startups Act, or JOBS Act, was signed into law by President Obama on April 5 of 2012. The Act requires the Securities and Exchange Commission to adopt rules to implement a new exemption that will allow for crowdfunding, so entrepreneurs can raise equity capital from a large pool of small investors who may or may not be considered “accredited” by the SEC.

investment, but there are still many areas of uncertainty and a lack of resources to provide guidance.

Impact investing is not an off-the-shelf practice proven out over decades of experience and portfolio management; it is a market of innovation and evolution and development. The very nature and purpose of early stage investing is to work out the kinks and take proof of concept to the next stage of dependable deliverables where other investors can more easily come in, assess the opportunity and invest. While it is a source of frustration for both investors and entrepreneurs, the struggle to place capital in early stage social ventures is a challenge worth embracing as it strengthens the field for ongoing success.

Those who are already entrenched in the seed stage landscape have laid the groundwork that further innovations can be built upon to invite new investors to early stage investing and more effectively connect entrepreneurs to capital.

The next stage of innovation:

- **Simplify** sourcing of high quality and assisted ventures, both to build comfort and

organize the landscape of investment deals, through the leverage of accelerators and other deal sources like seed funds.

- **Reduce** transaction friction and requirements through the use of technology and platform plays so that investors can concentrate on the positive value without getting lost in the operational details.
- **Decrease** investment size requirements to facilitate flow and diversification.
- **Develop** new models of crowd-sourcing, donor advised and philanthropic sourced investment, while leveraging the emergence of platforms for accredited and JOBS Act-enabled retail opportunities.

There remains a tremendous opportunity for innovation and for intermediaries to alleviate the friction in seed stage impact investing. A small shift in the allocation of capital can make a significant difference, and it is our hope that a handful of new products and services will be developed to support that reallocation in response to the challenges outlined in this brief. Directing a steady flow of capital towards promising early stage ventures is critical to the growth of social entrepreneurship and impact investing, and the solutions are within reach.

RELATED RESOURCES

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