Paul Breloff

Accion Venture Lab

Case Narrative

Accion Venture Lab, launched in 2012, is a seed-stage impact investment initiative that provides small amounts of capital (up to $500,000) and management support to jump-start game-changing financial inclusion startups around the world, promoting better financial services to more people at the base of the pyramid (BOP).

Lack of financial access is a massive global problem. At Accion we believe, and the research shows, that the right financial tools can make or break whether someone will be able to take advantage of an opportunity (e.g., invest at the right time to grow a business) or absorb a financial shock (e.g., pay for an emergency medical procedure without spiraling into debt). According to the World Bank's Global Findex Database 2014, roughly two billion people around the world lack access to formal financial services. Our efforts address this widespread issue by helping to provide access to financial tools that help underserved customers—particularly low-income customers and small business owners—improve their lives. A reliable place to borrow and save, for example, can help a household manage uneven cash flow, smooth consumption, and build working capital; insurance can help mitigate risk and manage shocks; new types of payment services can help reduce transaction costs and keep money with families, rather than big money transfer organizations. Evidence also shows that financial inclusion is positively correlated with growth and employment at the macro level.

Venture Lab is an in-house, strategic venture capital arm of Accion, a financial inclusion nonprofit organization headquartered in the United States, with offices in Colombia, Ghana, and India, and with 200 staff members around the globe. Although this strategic, in-house venture capital model is common among mainstream banks (e.g., Citi Ventures, American Express Ventures), it remains uncommon among nonprofits, which rarely have the resources to foot the bill for exploratory investment arms. Venture Lab's purpose is to spur innovation in financial inclusion, specifically innovation led by the earliest and most unproven startups. We believe that market incumbents—the big banks, credit card companies, and remittance players—need a healthy dose of inspiration or perhaps fear from a new breed of entrepreneurs poised to shake up the status quo in global finance.

Paul Breloff is the founding Managing Director of the Accion Venture Lab.

Accion has been a leader in commercial microfinance, advocating that the best way to reach the greatest number of customers with high-quality services is by building strong institutions that leverage best-in-class talent, technology, business principles, and capital. To reach the billions of people who remain financially excluded and in need of access, we believe we must mobilize the capital markets, and capital markets are only drawn to sectors promising strong risk-adjusted returns and high profits—just covering costs won't cut it. This commercialized approach, once seen as controversial by some, is now prevalent in social enterprise, impact investing, philanthropy, and even government aid programs.

The success of microfinance as a tool of economic development and a returns-generating business model inspires our work at Venture Lab. Much as microfinance pioneers paved the way and de-risked the basic business model for later entrants, we view a next generation of financial inclusion startups as inspiration for a broader sector. These startups are taking advantage of the increasing ubiquity of technology (e.g., spread of smartphones, Internet and social media, big data, the cloud) and riding market forces (e.g., the unbundling of banks and traditional financial service value chains, global policy support for financial inclusion) to deliver services in ways that weren't possible in the past. We want to see more startups make bigger splashes in their markets, creating positive ripples that extend far beyond a company's immediate operations.

But can a $10 million investment initiative make much of a difference in an investing world in which venture capital funds raise hundreds of millions? Now more than ever, as impact investing goes mainstream—note Goldman Sachs' recent acquisition of Imprint Capital—the push is for scale, big funds, and big investments. In this push to be big, how can we hope to change the world with small investments in pure startups? In this article, I share the story of how Venture Lab started, why we do what we're doing, what we're learning from the more than 1,000 startups we've talked to and the more than 20 we've invested in, and where we might go from here.

ACCION MOVING INTO THE "FRONTIER"

Accion's vision is to build a financially inclusive world, where everyone has access to high-quality, affordable financial services. For the most part, Accion has focused on building sustainable, scalable MFIs that share our commitment to the double bottom line: maximizing both financial and social impact. Accion works with those MFIs by providing capital, management services, technical assistance, and governance. With more than 50 years of experience building more than 60 MFIs in more than 30 countries that today serve millions, Accion has long stood for the idea that it's possible to have a greater social and economic impact by working with markets rather than against them. Accion has been doing this since long before terms like "social enterprise" and "impact investing" became fashionable, and it has been doing it by harnessing best business practices and best-in-class technology and talent to tackle big problems. As an example, Accion was instrumental in helping establish, invest in, and support BancoSol in Bolivia, making an initial investment in 1992. BancoSol was the first regulated for-profit bank for the poor, and when it launched and succeeded with its new model, it ultimately changed the way microfinance was done not only in Bolivia but across the region and the world. BancoSol is a very early embodiment of “double bottom line” ideals.

Through the 1990s and early 2000s, Accion pushed the industry to be more commercial, away from its traditional philanthropic approach. This meant leveraging a range of financial tools to bring money into the sector: equity, debt, credit enhancements, and specialized investment vehicles to deliver them. Having launched the first credit guarantee program in microfinance in 1984, Accion participated in the creation of ProFund, the first private equity fund in microfinance, to help capitalize these growing MFIs. Later, Accion launched Accion Investments (AINV), led by Enrique Ferraro and now-chief investment officer John Fischer. AINV helped build great MFIs across Latin America and Africa from 2003 to 2012. Beyond the social impact of these investments, AINV successfully delivered net annualized returns of 15.6 percent to its investors (returns that do not include the windfall from the Compartamos IPO discussed below), a true accomplishment and a milestone for the microfinance and impact investing industry.

During this time, Accion was also providing operating support to its MFI partners to expand their product offerings and grow in a more customer-centric manner. The basic microcredit product—typically a working capital term loan—gave people access to credit, letting them invest in livelihoods and often increasing household incomes, but loans alone wouldn’t generate the impact Accion wanted. Accion began to explore ways to generate impact beyond microcredit, and it launched a product innovation area to help MFIs diversify beyond microcredit.

The years around 2005–2006 also became a seminal moment for BOP-focused financial services, changing forever how MFIs and other enterprises focused financial inclusions could access capital and capital markets to fuel their growth and outreach. Compartamos, an MFI in Mexico in which Accion had invested, needed to find significant new sources of capital to maintain growth and serve the large client demand of the Mexican microfinance market. After considering multiple alternatives, Compartamos eventually decided that a public offering would best meet its long-term capital needs and serve the market demand, while allowing the institution to retain its mission. The resulting IPO far exceeded everyone’s expectations: it was the first ever in microfinance and a huge financial success. The offering was 13 times oversubscribed. It was also a watershed moment for Accion, which realized windfall returns on its investment.

These record returns generated global attention on both microfinance and interest rates: Compartamos had been charging rates near 100 percent, which many have questioned and criticized as too high, prompting many to ask whether Compartamos and Accion had become “too” commercial. For Accion, Compartamos’ success was at once a validation of its hopes for microfinance but also a call to evaluate whether it could do even better. Compartamos also importantly showed Accion and the world the power of harnessing the capital markets for social change, a lesson that continues to guide

Accion's work today. Over time, the IPO led to a much more competitive microfinance market in Mexico and beyond. Interest rates locally dropped by as much as 20 percent, and many MFIs started to find it easier to raise capital.

The challenge was clear: how could Accion use its IPO proceeds to help radically improve the cost and quality of financial services to the underbanked? Accion committed to several initiatives, including an expansion of microfinance to large unserved markets (such as China), creating the Center for Financial Inclusion to help build a strong industry with high standards, and exploring new investment vehicles to push the frontiers of financial inclusion beyond microfinance.

As the first step of this third prong, Accion established a small experimental portfolio within its in-house Gateway Fund. The portfolio, called the Gateway Microfinance Innovation Fund (GMIF) would eventually be led by Monica Brand, currently managing director of Accion's Frontier Investments Group. Monica had been hired years earlier to develop new products for Accion and its partners and had seen first hand the challenges of getting MFIs to innovate and change in her product development role. Even when her group tried to partner with different types of organizations like CEMEX and Visa, the pilots were rarely fully implemented at scale. Monica and others at Accion wondered what the best approach would be to push innovation beyond microfinance. Instead of changing big institutions, would it be easier to invest in and support companies more naturally suited to innovation, such as earlier stage, stand-alone companies?

Monica focused GMIF's investments in three core areas: enabling technologies (to improve the efficiency of existing MFI processes), distribution channels (to improve financial service convenience and access), and new financial products beyond working capital (e.g., insurance, housing finance, and remittances). Eventually, the Gateway Microfinance Innovation Fund was renamed Frontier Investments Group (FIG), reflecting its ambition to push the boundaries of financial inclusion beyond what microfinance had so far achieved.

FIG made four investments in its first 18 months of operation, all directly from Accion's balance sheet. Once Monica became FIG's managing director she began to focus more on growth-stage investments, rather than seed, because these companies typically involve lower risk and a greater probability of generating returns more quickly. FIG soon amassed a database of roughly 100 companies that it had turned down for being too early—including companies with very strong teams and innovative business models. Even if FIG wasn't going to make these investments, Accion wanted to ensure that it could still partner with and learn from these startup-phase innovations as well. Accion began exploring the best way to partner with these even earlier innovators, planting the initial seeds of Venture Lab.

INDUSTRY IN TRANSITION

It was—and still is—an exciting time for financial inclusion. Since the Compartamos IPO and throughout the early days of FIG, converging forces have begun reshaping how customers access financial services, and the market itself. In the last ten years, the global financial inclusion community identified the deepening penetration of mobile phones and the possibility of agent-based financial services as ways to extend financial service access to underserved customers, riding a digital distribution network and a dramatically lower and variable cost structure, without high-cost brick-and-mortar branches.

More recently, we've been experiencing a proliferation of mobile, broadband, and digital technology, and an accompanying explosion of social media, including widespread usage among low- and moderate-income families in both developed and developing markets. We've also seen a rise of alternative and big data, including those not traditionally used to analyze financial services, such as mobile phone usage and social network footprints. The customers themselves have also begun changing, expecting better banking experiences and simpler products, more responsive service, and more enjoyable mobile and online interfaces.

> The customers themselves also began changing, expecting better banking experiences and simpler products, more responsive service, and more enjoyable mobile and online interfaces.

The industry had begun changing too, with increasing recognition among governments, policymakers, and financial institutions that financial inclusion is critical for long-term global prosperity and growth. Today there also is greater transparency than ever, with many new ways for customers to educate themselves through social media, comparison shopping, and review portals. Moreover, our understanding of human behavior has revealed a tangle of behavioral patterns and "irrationalities" that can nudge people to make better financial decisions.

All of these changes have led to cutting-edge trends, such as the recent push to "unbundle banks" —the idea that banks are evolving from vertically integrated financial providers to utility financial institutions, with regulated banks providing the backbone and compliance for startups that offer deposit-taking and lending services. The financial world also is getting flatter, with services extending beyond single countries in terms of the flow of funds (cross-border e-commerce, with remittance growth of 6 percent per year since the financial crisis, is growing twice as fast as domestic e-commerce) and ideas ("frugal innovations" coming to the United States from developing countries, regulators working together across borders).

Both FIG and Venture Lab have presented a modest challenge to Accion's core MFI business. After literally decades of Accion promoting the investment in and potential impact of delivering financial services to the poorest billions through microfinance, the market had suddenly woken up, and all sorts of new players—some big, some small—were figuring out how to chase their own fortune at the BOP. Our current CEO Michael Schlein and current COO Esteban Altschul understood that we could either continue to focus only on microfinance, which might promise ongoing significant impact but perhaps less sector relevance over time, or we could embrace and learn from this new world, and in fact lead the sector at the cutting edge of this potential transformation. The institutional form must serve the desired impact, and the other way around, while we all believe that MFIs play a very important role in a healthy financial system, we also agree that if we can achieve our mission more effectively using new institutional forms, technologies, or partnerships, then we have a moral imperative to do that. In fact, unlike the majority of corporate venture capitalists whose primary purpose is to serve the core—investing in technology only when it can directly support other existing core products or needs of the company—Accion explicitly supports FIG's and Venture Lab's experiments with new business models and technology that, in time, could threaten the role and identity of Accion's microfinance work. This "mission over model" approach and openness to reinvention lets us do things that most corporate venture capitalists wouldn't dare.

If we can achieve our mission more effectively using new institutional forms, technologies, or partnerships, then we have a moral imperative to do that.

SEEDING VENTURE LAB

My own personal journey from microfinance to financial inclusion innovation to Venture Lab reflects a trajectory similar to Accion's organizational evolution. I was initially exposed to community development finance in a law school class that let us students help design and prepare to launch a community development bank focused on underserved customers in New Haven. This experience sparked my imagination about how financial services could be used as a tool of economic development, and it led me to microfinance. At about that time, microfinance was getting hot: 2005 was the UN International Year of Microcredit, and other publications were hailing microfinance as a silver bullet to cure poverty. I landed a role at SKS Microfinance in India, initially as an unpaid intern but eventually assuming control of the business development and strategic initiatives team. SKS offered a rich and eye-opening opportunity to experiment with nearly every interesting happening in global social enterprise at that time. SKS's customer base was growing rapidly, from around 100,000 customers when I first joined in 2006 to more than six million when I left in 2009. My team's task was to turn SKS into a distribution channel to the BOP for all sorts of products, a one-stop shop for rural India. In addition to financial products like credit and insurance, we provided solar lights, water purifiers, cell phones, lower-priced fast-moving consumer goods, and even primary school education. We thought we could take advantage of our institutional relationship to help customers access these life-enhancing products and services at scale, thereby benefiting customers while also building SKS's business.

We had some success, but we soon realized that creating a "distribution channel to the BOP" was easier said than done. What looked simple on a PowerPoint slide gave way to innumerable real-life challenges, and we realized that even world-class MFIs like SKS have a hard time innovating and launching new products (a similar realization Monica had at about the same time at Accion). It's challenging to train staff accustomed to a cookie-cutter loan product; to integrate with legacy technology systems not designed for new products; to deal with logistics of poor roads, limited electricity, no cell coverage; to get buy-in and work across differently incentivized departments in a big institution. It became clear to me that MFIs could not be the complete answer to the financial needs of the poor, much less their non-financial needs. To reach the BOP effectively, we'd need new entrants with new ideas and new technology.

> Startups … can stretch small amounts of money much farther than incumbents by existing on shoestring salaries and spare budgets, motivated not by an annual bonus but by outsized fame and fortune if they change the world.

From SKS, I consulted with the Consultative Group to Assist the Poor (CGAP), a financial inclusion think tank housed at the World Bank. CGAP had become a leading voice on the power of commercial microfinance and a lead evangelist for "branchless banking," the idea that we could financially reach dramatically more customers at lower costs by using cell phone and bank-appointed agents instead of expensive bank branches. Those same technological and industry forces were shaping Accion's work and identity, and they were also shifting the market as a whole. CGAP was helping to harness these forces to expand financial services massively and cheaply, and was rolling out initiatives to fund big banks, retailers, and mobile operators through sizable grants to sponsor new product or business model pilots. At the time, CGAP hoped to nurture "intrapreneurship" at these large corporations, thinking these would be the best situated groups to develop and scale new products and technology to the masses. We were, in essence, paying the people we thought were the likeliest sources of innovation.

In general, however, many big financial players are not the best innovators; in fact, many aren't even good innovators. They often employ world-class people, but as organizations they tend to be bureaucratic and slow, have legacy tech systems that make it challenging to leverage the newest innovations, and their managers are typically incentivized by an annual bonus rather than a long-term home run. Plus, these companies run on expensive budgets, with highly paid executives, belled-and-whistled technology, and five-star travel.

Startups are the inverse of all of this. Small standalone companies are usually more nimble and less saddled by a complex hierarchy or red tape, and they're building from scratch, rather than trying to integrate into existing tech systems. These features enable startups to correct their course and adapt to market realities more quickly and to pursue niche markets, products, and strategies that would not satisfy the investment criteria of bigger players. These niche strategies have the potential to mature into disruptive innovations that can steal market share from established players, or they can show incumbents how to take an idea to scale. Startups also can stretch small amounts of money much further than incumbents by existing on shoestring salaries and spare budgets, motivated not by an annual bonus but by outsized fame and fortune if they change the world.

The startups were out there, as FIG's experience showed. However, they needed some help, as many weren't getting funding or were wasting too much time chasing it. They also generally weren't able to access the other forms of capital they needed to scale, particularly human capital. It seemed to me that if we (as an organization and industry) cared about innovation, speed, and industry-level experimentation and learning, we had to support startups.

While grants from big donors like CGAP could be one way to provide this support, these donors face many challenges when they try to support startups directly. Procurement and granting policies often make it difficult for big donors to support for-profit companies, and startups often find it challenging to respond to administrative and reporting demands without experienced and dedicated personnel. Most big grantmakers also expect recipients to present a detailed operating plan, budget, and impact or "results framework" years into the future, which is impossible in the fast-changing world of a startup.

In 2011, while still working part-time with CGAP, I joined Accion as a consultant to help further define a strategy to support financial inclusion "beyond microfinance," addressing how we could better work with early-stage innovators. Based on Accion's record of building MFIs and FIG's newer investments, we all believed that venture capital was a much better model for supporting startups than was traditional grantmaking. "Impact investing" was on the rise, and a new breed of investors was looking to solve social problems by making return-seeking investments, and applying venture capital and private equity principles to supporting and building businesses that promised a scalable impact. However, most of these investors didn't want to be troubled with the very early, very risky companies that might be the most interesting and potentially game changing. Accion wanted to change that, and we began creating a solution that could get right-sized capital and support to the earliest and riskiest innovators. This solution eventually became Venture Lab.

Designing the Lab

From late 2011 into early 2012, we had a large number of conversations at Accion to define specific general focus areas and operating modes. We formed hypotheses to determine which markets to focus on and how to engage in the market. I made numerous trips to India, Kenya, Tanzania, Mexico, Indonesia, Colombia, and San Francisco, meeting with every investor and entrepreneur I could. We also met with banks, funders, and others who could give us their perspective on what was happening at the ground level in these markets, what customers needed, and where entrepreneurs were focused. They gave us the details on investment and entrepreneurial ecosystems, maps of the various nodes of influence, and connectors and aggregation points for startups.

At the time, we were struggling with a handful of structural and design questions:

- Should we be located in-country versus having a U.S. headquarters? Having had an operating role in India, I believe in being close to the action. We initially went with a lean staffing model, consisting of one analyst in the D.C. headquarters and regional directors in Latin America, East Africa, and India. However, we underestimated the need for a shared team DNA and the challenges in creating this shared team culture, trust, and communication without working in the same place. When you work in the same place, investing is more fun and also leads to better outcomes—ideas and decisions get stronger when discussed and challenged in informal conversations. Thus, when colleagues decided to move back to the United States, we chose not to replace them in-market immediately. Going forward, I imagine we'll continue to have waves of centralization and decentralization, and we're now considering a program to give our team opportunities to spend longer periods of time based in certain markets. We also aim to leverage Accion's global footprint and staff to be "local."

- How do we determine our investment size and parameters? Accion board members pushed us to make very small investments in pure startups ($100,000–$200,000), whereas we were hearing the need in the market for modestly larger investments ($400,000–$500,000). We initially settled on $100,000–$300,000, but when appropriate we have upped the initial sum to as much as $500,000.

- How should we approach our team, budget, and sustainability? We had big questions about the size of our team and how we'd pay for it. Today, Venture Lab, as a department within Accion, invests funds from Accion's balance sheet and receives operating funding from Accion like any other department. We also get generous pro bono legal support from a number of leading law firms as well as support from like-minded partners, such as Credit Suisse and MasterCard's Center for Inclusive Growth, which fund in-house management consulting and knowledge sharing, respectively. This support has allowed us to be well-staffed to deliver on our mission, although we also acknowledge the long-term need to be thoughtful and disciplined about tying our expenses to the assets we manage.

The Accion board was a supportive force throughout the planning phase for Venture Lab: the board offered great input and perspective on various design decisions, supported a risk-taking approach, and provided (and continues to provide) unwavering support to Accion as it tests new territory in pursuit of its financial inclusion mission. Ultimately, the board approved the launch of Venture Lab in March 2012, initially committing $10 million to the effort. We were officially in business.

Building the Team

The first step was to hire the people we'd need to get the job done. We knew it would be hard to find the right fit: we were looking for people who were passionate about financial inclusion and market-driven development solutions, and who exhibited of strong technical skills honed in the crucible of a management consulting or investment banking firm. We also needed deep expertise related to financial services, technology, and/or microfinance; and we sought great operational instincts gained by living and doing business in the chaos of emerging markets. Finally, we wanted people who were adept at building relationships and who would enjoy the heady enterprise of building a "startup to help startups" on a global scale. Few candidates meet these requirements, and those who do often aren't willing to work for a nonprofit salary, so staffing wasn't easy.

After hiring Nate Gonzalez as our initial analyst based in Washington, D.C., we looked to hire within the emerging markets where we wanted to focus, knowing it wouldn't work long term to do business overseas via Skype. We identified a few key markets—India, Kenya, and Mexico—that seemed to have the right ingredients for success and were leading the way in innovation. We initially focused on one hire in Kenya and one in India. One of our first hires was Vikas Raj, someone with whom I had crossed paths while we were both working in India. I knew he was the person for the India role, but that meant convincing him to leave a lucrative investment banking job and his home in New York City, and to move with his fiancée (now wife) to Bangalore. After about a year of deliberation, he finally agreed to make the jump. Vikas has since been promoted to lead our global investments activity and has been a huge part of our growth and success.

Hunting for Startups

When we started Venture Lab, we didn't know how many companies we'd find to invest in. While at SKS and CGAP, I'd encountered dozens of startups in Asia, Africa, and Latin America, but I knew we would need far greater numbers to build the kind of portfolio we were aiming at. After all, we were targeting nearly 30 investments over four to five years—if it was true that many venture capitalists invest in far less than 10 percent of the companies they speak to, then we'd need to find hundreds of companies. And I'm happy to say we found them. In fact, we've looked at about 1,000 companies in just three years.

So far we've invested in 22, which means that for every deal we make we turn down more than 40 prospects. I find myself wanting to invest in many more companies than we possibly can, but our biggest obligation is to promote ideas that can have a positive impact for the poor at scale, and not all ideas can. We also want to focus on the companies in which we believe we can meaningfully influence the outcome—where we can help achieve scale, or scale more quickly, or scale in a way that maximizes positive social/economic impact. To this end, we go into every investment with a clear sense of fit with Accion, both what we can give (e.g., experience, brand, networks) as well as what we can receive (e.g., insights, exposure). That said, we'd like to find ways to help a broader swathe of entrepreneurs, perhaps by partnering with accelerators in more meaningful ways (which we've done recently with Village Capital financial inclusion-focused programs in Mexico and India), creating open source tools for entrepreneurs or holding more peer learning events for those outside our portfolio.

In our early days of hunting for investments, we faced a pesky problem: we had little experience as principal investors, and we had a lot to learn. I had been exposed to investing at SKS and briefly as a lawyer, but I had never actually been an investor. Vikas' investment experience was with bigger private equity transactions. We consumed books and blogs, and we begged experts to speak with us, but we also messed up lots of little things in those early days. We hadn't yet learned the coded language of venture capitalists and entrepreneurs, and we mismanaged some investment processes by failing to communicate properly with the entrepreneurs. At the time, I knew we'd make mistakes that we wouldn't recognize until later; I just hoped that we'd laugh at those mistakes in time, and that they wouldn't do lasting harm to Venture Lab or Accion. I'm now much more confident that we know what we're doing.

Investing in startups is more art than science, as we quickly learned when dealing with companies without audited financials (or financials, period). We certainly employ hard analysis on unit economics, market sizing, and basic cash flow analysis, but much of the decision of whether to invest is based on a qualitative analysis of the management team, customers' likely reaction to a new value proposition, and the interplay of hard-to-quantify market forces. We try to imagine and make decisions on the basis of what could be, and not necessarily on what is today. There are so many "known unknowns" and "unknown unknowns" that it doesn't do much good to fixate on particular details, unless you're confident that they are the central make-or-break issues of the deal. It comes down to asking the right questions and creating data inputs when nothing is handed to you.

We also learned how much value and goodwill can be created and lost in how the deal process is managed. In one early deal, we thought we could manage without a term sheet. We agreed to "normal" terms and jotted down a few ideas in an email, and then we let the lawyers craft long-form documents. Big mistake! When their lawyers came back with the final documents, we realized that their notion of "normal" was quite different from ours, and thus began several frustrating weeks of backtracking and redoing documents. If we had presented a clear term sheet up front, we could have saved weeks of time and avoided a near collapse of the deal.

In another situation, we tried to build safeguards into a shareholders agreement, specifically a redemption right we could trigger if the company veered off mission. This seemed simple enough, until we got into the legal details of that mission—that is, who would determine whether the company was veering off, what would happen if we disagreed, what price would we be able to "put" our shares at, in what time frame, and so on. Long story short: it was a good idea that I'll never try again. While we now push to maintain some level of contractual control and influence, we focus on the more informal means of influence to guide companies toward pro-customer and pro-social strategies, which we find to be more effective than consent and veto privileges. We also have learned that when negotiating a deal, we're also laying the groundwork for and hoping to facilitate future rounds of investment; thus we aim for the simplest, most market-based deal structures we can to make it as easy as possible to raise money in the future.

Much of our early effort was aimed at letting the world know we existed and were open for business. We traveled globally and spent time in Nairobi, Mumbai, Bangalore, and Mexico City, meeting with entrepreneurs, investors, bankers, social entrepreneurs from other industries, and people in-market I thought would know the kinds of people we wanted to do business with. At that stage, our general goal was to make sure people knew us (including what we were looking for and what we would invest in), and that we stayed top-of-mind so that we'd get access to the most exciting deals. It helped significantly that we were part of Accion, whose strong brand stands for market-based development and impact investing, and that we were so focused on seed-stage financial inclusion opportunities, which made us stand out from investors who were more agnostic on sector, geography, and even stage.

We also began developing more proactive sourcing strategies—forming viewpoints about particular business models we wanted to see, and then going out to hunt for opportunities. For example, we learned early on that almost no merchants in Mexico accepted credit cards, which made sense when accepting cards meant having to buy expensive point-of-sale terminals. But companies like Square were demonstrating that merchants could accept credit cards with only a smartphone and a cheap plug-in "dongle," and we figured this would work in Mexico. After finding and speaking with a half-dozen similar teams with the same idea, we decided to back a company called Clip, which continues to expand across Mexico.

Another challenge for us was determining which customer segment to focus on, and how this would relate to our view on how we could best achieve positive social and economic impact. Since we invest in business models that depend on access to technology—for example, smartphones, Internet social media—we know many rural and poor people may not be our companies' initial customers. But we don't see this as mission creep. Instead, we are betting that the future won't look like the present—adoption curves for these new technologies are steep, even among the poorest and most remote customers—and we believe that certain innovations adopted today by the wired middle class will soon be disproportionately relevant to those at the BOP, once infrastructure catches up. We believe many technologies, such as mobile-based payments, can especially benefit low-income customers lacking traditional payment instruments like credit cards, even if current leading-edge users for these services are more mainstream.

One example is Coda Payments, our very first investment, which initially offered a form of direct-carrier billing that let people buy e-content with value already on their phone. We knew the early adopters would be well-off Indonesians looking to buy games and apps on their phones, but we also knew that if Coda took off, the ability to engage in the e-commerce universe without a credit card or bank account would be enormously valuable to the unbanked. Likewise, we knew that giving the BOP the ability to make remote payments was a precondition to creating digital content tailored to the unique needs of the poor. Was this a good bet? The business is doing well, but we are still waiting to see how our impact thesis plays out.

> The level of total commitment shown by the best entrepreneurs is inspiring, even frightening… The best entrepreneurs have an uncanny ability to hear [harsh] feedback, mine it for wisdom, and still maintain a deep belief that success is the only possible outcome

Over the past few years, we've learned a lot. First, it's clear that entrepreneurs and their teams are the true heroes of this field. Investing can be very challenging and we certainly work hard, but the level of total commitment shown by the best entrepreneurs is inspiring. These people often work for years at sub-market rate salaries, risking their careers and reputations for an idea that they are told by many will almost certainly fail. The best entrepreneurs have an uncanny ability to hear this feedback, mine it for wisdom, and still maintain a deep belief that success is the only possible outcome. It's a privilege to talk and work with these trailblazers every day, and to help turn their visions into reality. There's no doubt that the worst part of our job is having to say "no" to such passionate entrepreneurs so much more often that we get to say "yes."

We've also gained insight as to what makes a company work and how to spot it early. We learned the difference between a good idea, a good business, and a good deal. We have seen a huge number of good ideas and many good businesses, but good deals in which the idea meets profit potential meets the right price, structure, and terms are few and far between. We also have learned to look more closely at the value proposition for our customers. As an industry, we often convince ourselves that customers need products they don't really want and are shocked when no one uses them. Many solutions are at best ten percent better than what exists, and thus aren't "better enough" to prompt customers to adopt them. In his blog, venture capitalist king Ben Horowitz writes that any tech startup must build a product that's at least ten times better at doing something than the prevailing method, that two times better won't be good enough to get people to switch. Whether or not 10 times is the standard, I firmly believe that people only change behaviors to avoid great pain or to experience great pleasure, and very little in between. How many financial inclusion offerings meet this standard? When we invest, we look for painkillers—not vitamins.

We've also improved our ability to figure out when something just will not work. We see many ideas that make sense in theory, or look good in PowerPoint, but are simply implausible given the realities of infinite changing variables, fickle customers, partners and politicians, infuriating infrastructure, and insufficient talent in the market. That's why I try to hire people who have spent significant time in emerging markets and with the customers we focus on, because firsthand experience in market radically accelerates and enriches one's sense of concept plausibility: perhaps one can develop pattern recognition skills with a large number of "reps" as an investor, but this takes time and may never instill the same bone-deep instinct.

The flip side is that we've said "no" to some companies we probably shouldn't have. There are some great entrepreneurs and companies we've turned down that we're still kicking ourselves over. (You know who you are.) We loosely track these companies in an "anti-portfolio" to see what we can learn from our decisions—why did we say no, was it the right decision at the time, and if not, what can we learn to avoid making the same mistake in the future. Hopefully these regrets won't be for naught.

So where are we today? As of September 2015, we have a full-time team of seven, with 22 investments across North and Latin America, sub-Saharan Africa, and South and Southeast Asia. In 20 of these 22 investments, we were the first institutional investor or at least part of the first institutional investment round. Nearly ten of our portfolio companies have raised additional financing at increased valuations. Most of our startups leverage technology as a key element of their business formula, and there are a number of themes we've been particularly excited about: financing small businesses with new digital and data-driven lending models; leveraging new data sources for better credit assessments that allow us to say "yes" to more underserved customers; building out new products and services that can be offered on top of mobile payments platforms; and using technology to engage and empower customers, particularly as they learn about new products and how to use them, improve their credit profile, and take charge of their financial health.

A number businesses we've invested in and are excited about embody these themes:

- Varthana in India uses a unique customer acquisition and credit assessment approach to provide loans to owners of "affordable private schools" for investments in better classrooms and content, as well as expanding educational quality and access.
- RevolutionCredit in the United States offers a digital platform for consumers to watch short educational videos to improve financial behaviors, allowing financial institutions to identify more creditworthy customers, improve engagement, and extend access to a wider range of financial services at better prices.
- CreditMantri in India provides a web-based financial advisory service that helps

consumers who are underbanked, have bad credit, or are new to formal financial services learn about their credit scores and improve their financial health.
- DemystData uses a proprietary technology platform to help financial institutions tap into the explosive growth of online, social, and internal data to improve financial institutions' decisions and more responsibly lend to "thin-file" and underbanked customers.

DELIVERING VALUE BEYOND THE MONEY

As we made our first few investments, we began to give more thought to the type of investor we wanted to be. We strongly believe that investing, particularly at the seed stage, is not just about making smart bets but about adding value post-investment to support the growth and success of our companies. Getting actively involved pays dividends by not only making our companies more successful (we hope), but also by ensuring that companies see value in choosing us as a partner and by making us smarter investors.

Like many investors, we often seek board seats when we invest, which helps us stay close to the business and contribute, but we also have seen an opportunity to go beyond this level of support. Accion is usually deeply involved with its MFI investments, bringing managerial capacity and technical expertise to its partners, so a value-adding approach is in our DNA. We therefore look for any possible way to leverage our Accion brand, our MFI relationships, and our technical expertise to help our portfolio. However, seeing the bandwidth constraints our companies faced and the power of targeted, short-term support to unlock key growth constraints, we saw an opportunity to go even deeper. To build out this capability, we brought Tahira Dosani on board as our director of portfolio engagement. Her background in management consulting, operating in emerging markets, and investing in financial services made her ideally suited to this role. She joined the team in 2013 with a mandate to build out a platform to support our companies "beyond capital."

At that time, we looked around the impact investing community and didn't see any early stage investors who had really fleshed out a portfolio support function. We then looked to the commercial venture capital world and identified an emerging group of venture capitalists who were investing heavily in operating teams—experts in sales, marketing, technology, human resources, and more—to support their investees. These models guided us as we sought the right approach to portfolio engagement for Venture Lab.

Learning from the lean and agile approach of the startup world, we jumped right in with a small team, knowing that we would learn best by doing. In 2014, we worked with a handful of companies that asked for our support. Surprisingly, despite the diverse business models and geographic spread in our portfolio, their needs were largely consistent. Most requests related to customer strategy—segmentation/targeting, defining/communicating value proposition, product development, and channel strategy. We executed a number of projects focused on these issues, each lasting at most several weeks. Each business needed a dedicated team for the duration of the project—certainly more effort than we could have provided through our roles as board members.

An example is our work with Konfio, a Mexico City-based portfolio company that provides Mexico's small and micro enterprises with business loans. Konfio uses a digital platform and unique underwriting approach that allows it to quickly assess credit and provide reasonably priced loans to small businesses. We helped Konfio segment its customers, which allowed the company to identify and prioritize key customer clusters and deprioritize low-value segments. This work helped Konfio clarify its value proposition and messaging to different segments and focus its marketing on the best channels, while also identifying key issues and variables for its managers to track.

To date, we've done projects with 16 companies—a significant number for a staff that includes just one full-time member and an assortment of part-timers or short-termers (including a series of fantastic externs from Bain & Company, which has been an amazing partner to us). We don't charge companies for our time, but companies do cover any travel costs associated with the project, in part to show they have "skin in the game."

As we reflected on our experiences in the first year of portfolio engagement, we saw a number of benefits in our lean, in-house approach. We could be extremely nimble and start projects in a matter of hours after initially spotting a need, and we could be responsive to the changing demands of early stage startups. Moreover, the lessons we learned could be shared with other companies in the portfolio, making us better investors. We've also extracted some of these lessons to develop materials on governance and board management, compensation, stock option plans, and other resources that could be used beyond our portfolio. Just having this internal function has helped us differentiate ourselves as we compete for the best entrepreneurs and deals, and funding support we received from the Rockefeller Foundation and Credit Suisse has been instrumental in enabling us to expand this function.

But we think we can do more, particularly to connect our entrepreneurs to the right expertise and talent to take their businesses to the next level. We've seen that a lack of human capital—the ability to identify, recruit, develop, and retain the right talent—is often the major barrier to growth for early stage startups, and we're drawing up a solution that we think can help. We also see a growing cadre of global experts who are eager to lend their insights to support startups doing work they believe in, and we're hoping to mobilize a network of advisors we and our companies can draw on to make the best decisions on technology, data, customer acquisition, enterprise sales strategy, design, and more. We believe there's a real need and an opportunity to set the standard and help proliferate a model of support that goes beyond capital in the impact investing and financial inclusion worlds.

ACHIEVING THE MANY-SPLENDORED IMPACT

We have been developing our impact thesis and "theory of change," and we are increasingly focused on how we can use startups to catalyze innovation within the industry at large—to move the overall market and not just support interesting startups. We recently established a "knowledge and industry engagement" function for this purpose. This is based on our belief that there are both direct and indirect pathways for a company to achieve impact at scale: direct pathways like organic growth and strategic acquisition, but also indirect pathways like inspiring copycats and competitive responses that build on and respond to the work of pioneers and ultimately benefit end customers. We are working to identify systemic-level ripples or "pinballs" sparked by innovators that lead to the creation or growth of new markets and actors. Consider how Grameen Bank and BancoSol showed the way for future MFIs, or Jipange Kusave served as inspiration for M-Shwari, or new remittance companies forced incumbents to lower prices and open more convenient digital channels. Our aim is to capture, analyze, and articulate key trends and lessons emerging from our portfolio, and to share these insights with providers, entrepreneurs, investors, funders, and policymakers. By doing so, we hope to inspire new products and processes, and to shape policy that enables innovation—all in the service of providing more and better financial services for customers at the BOP.

All that said, we still have more to figure out. First, we are realizing the complexity of articulating and measuring impact. It's not just about giving someone a loan or account and checking them off as "included." It's about ensuring that every person, household, and business has access to the financial tools they need to improve their lives; ensuring that these tools are of the highest quality; and ensuring that customers know enough to make use of these tools in responsible, healthy ways. This requires more than just looking at what products are being supplied, it necessitates a more textured understanding of how products are being used and understood by households and small businesses, a steeper measurement challenge.

It's also a challenge for us to account for the indirect impact we hope to achieve. We believe that the value of a market innovator lies not just in the first customers it reaches but in the ways it enables others to serve millions more. Each time a startup offers something new to customers, it learns a little more about what works and what doesn't, and these learning cycles can immensely benefit the industry at large, if there is a way to share them. However, most market innovators can't readily explain or prove the indirect impact they're having (nor can their investors), thus leading to systemic underinvestment. This is a big challenge, for a number of reasons. It's hard to define impact trajectories early in the life of a startup, or to attribute quantifiable impact to the activities of a single company within a sector. This inability to attribute positive impacts to the acts of an early pioneer is particularly troublesome and calls for a framework more oriented to "contribution" than "attribution." Even when indirect impacts occur, the timeframe over which the impacts become visible, may take years—long enough to outlast the patience and "results frameworks" of most funds and donors. And it's acutely difficult to make apples-to-apples comparisons at the indirect impact level.

As a first step toward identifying this impact, we create an "impact one-pager" for each investment. This document articulates our hypothesis of how a company can expand product access and quality, move markets, and make the world a better place.

Some of these metrics are clear and hard, such as the number of accounts opened or loans made, while others are fuzzy, long term, and hopelessly un-attributable, such as an overall shift in industry best practices. We also use the one-pagers as a frame to encourage our startups to think about their impact beyond traditional business metrics.

THE ROAD AHEAD

It's been an exciting three years since we launched Venture Lab, and we feel we're just getting started. We have a lot of plans and issues to consider, some of which we've noted, such as how to structure our team and define investment theses. Going forward we intend to enhance our capacity to support our entrepreneurs by investing in our "portfolio engagement" function. We also plan to expand our engagement with the industry at large to promote innovation ripples and pinballs, as our pioneering startups experiment with ideas and technology at the cutting edge of the financial inclusion frontier. While we decidely want our companies and entrepreneurs to "win" in the market—grow their companies and eventually generate returns for shareholders—we see more chances to enlarge the pie rather than to fight over slices, more chances to collaborate and share experiences, which we believe also yields the biggest dividends for customers.

We are in the early days of exploring alternatives to our current in-house, on-balance-sheet model that could allow us to broaden our funding base and bring in more investors to support seed-stage enterprises. We realize that our portfolio companies need more money as they grow: leveraging third-party capital, particularly from strategic partners who add value beyond just money, could be one way for us to help provide that. However, there are big questions about whether and how we might pursue this goal. Perhaps most importantly, we're still proving that our investment model can deliver returns—both financial and social—that would be attractive to outside partners. Since the start of Venture Lab, we've focused on supporting and proving scalable business models, but we have yet to prove whether our investment model can be scalable itself—that is, whether it can deliver attractive risk-adjusted returns, given our unique dimensions of deal size, stage risk, and high expense base as a percentage of funds managed. We're still figuring this out.

We also will continually be looking for avenues to extend our work to influence the financial services sector at large. We see a chance to promote a convergence of mainstream profit-makers and impact do-gooders to tackle specific problems or sectoral opportunities globally and across industries. The real momentum in financial inclusion will only come as the mainstream players start to see the opportunity to engage, whether as funders, partners, or competitors. As the mainstream banking world starts seeing BOP customers as a tremendous business opportunity rather than a corporate social responsibility side project, we can bring a new level of expertise, capital, and reach to the project of financial inclusion.

We also see the work of Venture Lab as part of a broader Accion effort to show the way toward a more financially inclusive world. Venture Lab is just a small part of

Accion, but we hope we can have outsized influence in how Accion evolves—what sorts of institutional models, technologies, and markets it invests in, not simply its startup investments through Venture Lab but perhaps even more importantly its "core" work of building leading emerging market financial institutions. We believe Venture Lab can help spur and direct some of these new efforts at Accion by proving what works and exposing what doesn't. We may invest small sums in early and unproven companies, but we believe this can be a strategy that produces a big impact.