Enterprise Solutions to Scale

Lessons learned in catalysing sustainable solutions to global development challenges

SHELL FOUNDATION

2010

This report was written by members of the Shell Foundation team: Chris West and Clare Woodcraft.

Our sincere thanks go to David Carrington for his guidance on structure and content, Chris Logan for his editorial input, and Richard Gomes and Shell's Creative Services team for the design and production of this report.

Copies of this report and more information are available to download at www.shellfoundation.org

Shell Foundation is a UK registered charity (no. 1080999)

Contents

Executive Summary	II
Introduction	1
Evolving our Strategy	4
"Spray and Pray" is Not Scaleable	7
Strategic Partnerships	9
Lesson One: Catalysing Disruptive Change: Angel Philanthropy	17
Lesson Two: Building Sectoral Pioneers	24
Lesson Three: From Subsidy to Earned Income	30
Lesson Four: Scale is Not Enough	35
Conclusion	37
Looking to the Future	39
Appendix 1: Enterprise-Based Approach	40
Appendix 2: Performance Assessment Methodology	42
Appendix 3: Overview of Grants	44

Executive Summary

When Shell Foundation (SF) was established in 2000[1], we had ambitious objectives to catalyse scaleable and sustainable solutions to global development challenges. We set about doing this in ways that were new at the time by pioneering an enterprise-based[2] approach. We concentrated our efforts on tackling social and environmental issues in which the energy industry has a particular responsibility. We also sought to test whether we could harness value-adding links to our corporate parent to maximise charitable benefit.

We have learned a lot about trying to achieve scale and sustainability over the past decade. In keeping with our business principles that enshrine transparency we feel it of value to share our experience. This report highlights, therefore, not only our success stories but also the lessons learned from failure.

Scale means different things to different people. For us, scale is about delivering cost-efficient solutions that impact large numbers of beneficiaries in multiple locations in ways that are ultimately financially viable and self-sustaining. To try and ensure we do not over-report success, only those initiatives that meet all of the following criteria are judged to have achieved the goal of scale:

- Large-scale development outcomes (measurable)
- Multiple country and/or regional operations (measurable)
- Earned income derived from the market (measurable)
- Leverage that matches or exceeds our grant contribution (measurable)
- Management team has competence to execute the venture (subjective)

SF has committed almost US$111.9 million since inception (see Appendices for further details). To ensure we assess our performance most accurately, this report only covers the US$78 million committed to initiatives that targeted achieving scale from the outset and which were completed by end 2008. Of this total, 65% achieved scale according to our evaluation criteria, 19% was implemented successfully but showed no evidence of going to scale, and 16% failed to achieve intended outcomes. But underlying these percentages are considerable changes in performance over time that resulted from us adapting our strategy in response to the lessons we learned.

In our inception phase (from 2000 to end 2002) – where we largely provided short-term project-based support to multiple not-for-profit organisations – 80% of the initiatives we supported failed to achieve scale or sustainability. This reflected

1 Royal Dutch Shell PLC established Shell Foundation (SF) as a UK charity in June 2000 with the objective of protecting and preserving the environment and public health by means of education and research into the provision and use of energy in ways that reduce or eliminate harmful emissions.

2 By enterprise-based we mean a solution that treats the poor as customers not beneficiaries, is based on a viable business model implemented by a committed, competent and disciplined management team, and which from the outset is designed to achieve long-term financial viability that is the basis for scale-up and an exit from subsidy dependence.

Lima Feeds is a Kenyan business supported by GroFin.

either poor execution or lack of market demand for the proffered products and services. Having changed our strategy to focus on co-developing and implementing new business models with a few carefully selected strategic partners, we now find that 80% of our grants meet our criteria for having achieved scale or sustainability.

Today, two of our strategic partners (EMBARQ[3] and GroFin[4]) have achieved verifiable global scale and sustainability and two others (Envirofit[5] and The Better Trading Company[6]) are well advanced in this respect. While we are proud of their progress, we believe we can still do more to enhance our overall performance and create more scaleable and sustainable pioneers. Our success to date reinforces our view that while scale can be achieved through public sector programmes and community-based initiatives, the greatest untapped opportunity lies in developing more enterprise-based solutions.

We certainly do not claim that everything we have done has been successful or that we have all the answers. But we have identified some common features underpinning the success of some of our partnerships which we hope may be of interest to others seeking to achieve scale and sustainability.

In our inception phase – where we largely provided short-term project-based support to multiple not-for-profit organisations – 80% of the initiatives we supported failed to achieve scale or sustainability.

3 **EMBARQ** aims to improve the quality of life of people living and working in mega-cities in developing countries through the implementation of sustainable solutions to urban mobility.

4 **GroFin** supports the start-up and growth of viable small and medium sized enterprises (SMEs) in emerging economies as a means of enhancing sustainable employment and livelihoods.

5 **Envirofit** aims to achieve a significant long-term reduction in the incidence of Indoor Air Pollution (IAP) at the global level through the market-based development, production and sale of high-quality, durable and affordable improved cookstoves.

6 **The Better Trading Company** acts as an ethical intermediary to help build sustainable supply chains that are both good for business and help to eradicate poverty.

Catalysing Disruptive Change Through Angel Philanthropy

The importance of "new"...

We find it striking that in every instance where partnerships achieved scale and measurable social impact it has been with newly created entities that we helped co-found using new business models we co-developed. In all cases we were also the sole partner and subsidy [7] provider during the development and testing of these business models. By contrast, despite our various efforts, we have never succeeded in helping an existing organisation go to scale. We believe that angel philanthropy[8] has significant potential to catalyse scaleable solutions to global development challenges.

...and getting the right entrepreneur as a partner...

Testing new solutions with new partners in new markets is inevitably risky. Where we chose the wrong partner with insufficient business acumen, we failed. Our partner selection process has thus evolved considerably such that now we look for entrepreneurial partners who focus entirely on the venture and share the start-up risk by investing their own resources in it. We no longer encourage unsolicited proposals but instead proactively use our networks to identify the best people to partner with – although we admit we still have much to learn about the art of partner selection.

...who shares an aligned vision of scale

It is hugely important to have an aligned vision with partners, from the outset, with respect to achieving scale and sustainability. This means having a plan to achieve both social impact and financial viability from inception and which is subject to regular measurement and reporting. It is also based on recruiting the best staff and developing the most efficient operating systems essential for managing the complex multiple location operations that scale entails. Where we have partnered with individuals or organisations who did not share this early ambition to achieve scale, we found it virtually impossible to "retrofit" the subsequent capacity needed to achieve it.

Building Sectoral Pioneers

Supporting the building of a sustainable enterprise...

We believe there is a need to deploy resources to build a sustainable enterprise rather than simply provide grants to subsidise the short-term provision of products or services. Building sustainable enterprises means investing in core capacity and systems as a pre-requisite for scale. It also requires additional input over and above grant finance in the form of business advice, market access and appropriate governance support. This means that large amounts of up-front subsidy as well as

We find it striking that in every instance where partnerships achieved scale and measurable social impact it has been with newly created entities that we helped co-found using new business models we co-developed.

7 Our use of the term subsidy refers to the provision of grants (our primary financial instrument) but could equally refer to "patient capital" as deployed by others.

8 We define Angel Philanthropy as: Investing in a new venture without a proven track record or documented impact but with a new business-based concept, a new product in a new market which has the intrinsic goal of going to scale, achieving measurable social impact and becoming financially viable. By implication, this means investing considerable subsidy – including both grant finance and technical expertise – to prove the concept and that the market exists before the venture is then able to access second stage finance from the emerging class of impact investors.

A Bus Rapid Transit system in Mexico City established by EMBARQ.

dedicated staff resources must be committed before verifiable developmental benefits start to materialise in the longer-term.

…takes time, patience and considerable investment…

Building sustainable enterprises that can effectively address global development challenges takes time, patience and considerable investment. We have invested between US$10 million and US$15 million of grant support over five to seven years to help our strategic partners achieve scale and sustainability. Testing new partners to provide new services in new markets will always be difficult and a high risk approach. It requires our staff to understand fully not only our partners' business models but also the risks they face. Only then can we have the capacity to respond to changing circumstances and business challenges.

…and more than money

SF has invested considerable time in providing a range of expertise, business advice and skills-based support to our partners. We believe that this "more than money" approach forms a critical part of our differentiated business model and serves to significantly reduce the risk of working in a start-up environment. We have also sought to apply the same approach to harnessing our "independent yet linked" relationship with Shell. Our shared branding has been of tremendous value to our partners in leveraging support from others and opening doors. But we have also drawn on other Shell support including *pro bono* provision of skills, tools, market knowledge and networks. While this form of leverage has been far lower than originally expected – less than 17% of the projects that we funded over the past decade have drawn on such support – we hope to further exploit this opportunity in the future to support our partners.

Building sustainable enterprises means investing in core capacity and systems as a pre-requisite for scale. It also requires additional input over and above grant finance in the form of business advice, market access and appropriate governance support.

Local trader sells Envirofit cookstoves in India.

A strong market-based and value-chain approach underpins all the ventures we have supported that have gone to scale.

From Subsidy to Earned Income

Adopting a market-based approach...

A strong market-based and value-chain approach underpins all the ventures we have supported that have gone to scale. This has reinforced our belief that only by offering good quality products or services to the poor that they value and can afford, can the financial viability that is essential for lasting and scaleable solutions be achieved. While our strategic partners comprise both not-for-profits and for-profits, they all share a common mindset around cost-efficiency, customer service and revenue generation.

...and targeting financial viability is paramount

We have found that a disciplined focus on financial returns and earned income is critical to ensure sustainability and an end to depending on subsidies. This shared commitment to financial viability has enabled our strategic partners to leverage investment from other parties. Over the past decade we have helped partners leverage over US$1.2 billion of funding – with the majority of this for sustainable mobility initiatives (EMBARQ) or SME funds in Africa (managed by GroFin). In the latter case, this leverage has allowed us to exit as a subsidy provider entirely.

Scale Is Not Enough

We now realise that achieving scale alone is not enough. No matter how successful our partners are at pioneering new business based solutions to development challenges, they alone will never fully address the un-served needs of the millions of poor people around the world. There is a need for wider system change. We have made some

While our strategic partners comprise both not-for-profits and for-profits, they all share a common mindset around cost-efficiency, customer service and revenue generation.

tentative steps in this direction, but recognise that more effort will be required by us and others to promote replication and overcome market barriers.

In summary, we believe that foundations have a hugely important role to play in supporting efforts to resolve global development challenges. We equally believe the current debate around the importance of "impact investing" will help mobilise capital from other sources towards these shared goals. But a very significant gap still remains between those organisations that give project-based subsidy to not-for-profit entities and those social investors that seek returns that are both developmental and financial. It is in this space that we see a vital role for angel philanthropy that is based on:

- Catalysing new enterprise-based solutions with new partners
- Deploying significant subsidy and "more than money" to achieve scale
- Adopting market-based approaches that aim for financial viability

We accept that angel philanthropy requires focus, patience and flexibility. We also acknowledge that it represents a high risk approach given the time needed to achieve developmental returns. But we believe that more angel philanthropists are needed to catalyse and support the growing number of social entrepreneurs until they are ready to source second stage finance from others. Opportunities exist for syndication between angel philanthropists and such impact investors.

When we undertook this exercise of documenting our experience we were unable to answer the simple question "is our performance over the past decade good, average or poor in comparison to others?" We have found no widely accepted performance benchmarks for foundations or for programmes with common objectives. Equally we have found very few evaluations by other foundations that report both their successes *and* failures. While tackling global development challenges is hugely rewarding, we equally know it is not easy and our collective chances of success will increase if we share learning. We stand ready to work with others interested in developing, testing and deploying such comparative performance metrics.

We have learned a lot over the past decade that has helped us chart our journey for the next one:

- We will retain our enterprise-based approach and our focus on building strategic partnerships
- We will endeavour to do more to incubate, scale-up and spin-off strategic partnerships by enhancing our networks, facilitating dialogue between our partners and allocating time and effort to critical self-analysis
- We will seek to leverage greater value-adding support from Shell to achieve our mission

And we will continue to share our success and failure along the way.

Workers in South Africa packing wild flowers for export thanks to ethical intermediary The Better Flower Company.

No matter how successful our partners are at pioneering new business based solutions to development challenges, they alone will never fully address the un-served needs of the millions of poor people around the world. There is a need for wider system change.

Introduction

When Shell Foundation (SF)[9] was established in 2000, we had ambitious objectives to catalyse[10] scaleable and sustainable solutions to key global development challenges. We set about doing this in ways that were new at the time: by pioneering an enterprise-based approach[11] and by focusing on a range of social and environmental issues in which the energy industry has a particular responsibility. We also sought to harness links to our corporate parent Shell, for the purpose of delivering greater charitable benefit.

Since our inception, we have committed almost US$111.9 million towards meeting this mission and have learned a lot about how to achieve scale and sustainability. Some of what we have learned is no doubt familiar to other foundations with a longer track record than ours. However, in keeping with our business principles[12] that enshrine commitments to transparency, we feel it is of wider value to share our progress. As such, this report highlights not only our successes but also the lessons learned from failure.

Much thought has been dedicated to the subject of how foundations and social investors can be more effective in scaling up the solutions they support in order to increase the impact of their work. We remain convinced that going to scale is an important objective not just because it can increase impact but also because it avoids creating isolated "islands of excellence".[13]

Kestrel Wind Turbines in South Africa supported by GroFin.

9 Royal Dutch Shell PLC established Shell Foundation (SF) as a UK charity in June 2000 with the objective of protecting and preserving the environment and public health by means of education and research into the provision and use of energy in ways that reduce or eliminate harmful emissions.

10 "Catalyse" in this case is appropriately defined by Jeff Raikes, CEO of the Bill and Melinda Gates Foundation in his article in Alliance Magazine, Vol 15, 2 June, 2010 where he says it is the means by which effective identification of new solutions can trigger "an innovation, or new intervention that can drive sustainable change."

11 See Appendix 1, for an explanation of enterprise-based and *Enterprise Solutions to Poverty*, Shell Foundation, 2005.

12 For further information www.shellfoundation.org

13 "…so many good ideas either wither and die or get stuck as isolated 'islands of excellence'"…Specialised consulting firms such as Bridgespan and non-profit arms of mainstream consultancies such as McKinsey and Monitor have emerged in recent years to tackle these new problems of successful, but not successful enough, organisations." (Bishop and Green 2010, p 26).

Metrobus reduces commute times of 500,000 suburban passengers a day in Mexico City.

We fully acknowledge that scale can be achieved nationally through effective public sector programmes, or locally through a multitude of community-based initiatives. Equally, voluntary charitable contributions can provide valuable emergency disaster response where immediate funds are required and capacity is insufficient. But we believe that the greatest global opportunity to achieve scale is through the deployment of enterprise-based solutions. These solutions, in turn, should be implemented with discipline and focus against agreed key performance indicators (KPIs) that measure progress in terms of social impact and financial viability. This approach has allowed us to achieve scale of impact with some of the development challenges that we are currently addressing.

The difficulties in achieving the Millennium Development Goals[14] have highlighted the sheer size of the problem. Some argue that if current population and consumption trends continue, by the middle of the next decade we will need the equivalent of three Earths to provide the resource base to support the human race.[15] Finding effective solutions to large-scale development issues will inevitably require scaleable solutions. But scale is neither quick[16] nor easy to achieve.

---

14 The Millennium Development Goals (MDGs) are eight time-bound development goals adopted by world leaders in the year 2000 and set to be achieved by 2015. They provide concrete, numerical benchmarks for tackling extreme poverty in its many dimensions and include targets on income poverty, hunger, maternal and child mortality, disease, inadequate shelter, gender inequality, environmental degradation and the Global Partnership for Development.

15 Jonathan Maxwell, Proposal for a Climate Public-Private Partnership Fund, Sustainable Development Capital, 2010. The World Wildlife Fund argues that "If everyone in the world consumed natural resources and generated carbon dioxide at the rate we do in the UK, we'd need three planets – not just one – to support us.": www.wwf.org.uk/what_we_do/about_us/building_a_one_planet_future.cfm.

16 ...as Bill Clinton noted, in reviewing school reform initiatives during his presidency, "Nearly every problem has been solved by someone, somewhere." The frustration is that "we can't seem to replicate [those solutions] anywhere else." With a few exceptions, the non-profit sector in the United States is comprised of cottage enterprises – thousands upon thousands of programmes, each operating in a single neighbourhood, in a single city or town. Often, this may be the most appropriate form of organisation, but in some – perhaps many – cases, it represents a substantial loss to society overall. Time, funds, and imagination are poured into new programmes that at best reinvent the wheel, while the potential of programmes that have already proven their effectiveness remains sadly underdeveloped. Going To Scale, Jeffrey L. Bradach Stanford Social Innovation Review, Spring 2003.

Peter Frumkin points out that: "Only around 200,000 nonprofits out of some 1.5 million have revenues above US$25,000. The number of very large and successful nonprofits is considerably smaller than 100,000 and probably closer to 10,000, the majority of which are universities and hospitals." Frumkin On Philanthropy, http://www.socialedge.org/blogs/frumkin-on-philanthropy 10 April 2007.

The idea for this report was triggered by a simple question: "Has our performance to date in achieving scale been good, average or poor when compared with our peers?"

The idea for this report was triggered by a simple question: "Has our performance to date in achieving scale been good, average or poor when compared with our peers?" Given the lack of other published information around performance – including both success and failure – from peer organisations, this proved to be a very difficult question to answer. That is surprising given the billions of dollars managed by foundations (totalling over US$580 billion for US foundations alone[17]) reflecting the emergence of a new capital market.[18]

So rather than attempt any comparative assessment, we decided to share our own process of performance assessments and our perceived successes and failures. We also discuss how these experiences impacted our strategy during three distinct operational phases.

We certainly do not claim that we have all the answers. However, based on our experience over ten years we have identified some core lessons about how to deliver development results most effectively. These reflect our varying degrees of success in trying to achieve scale and sustainability through an enterprise-based approach. We also draw a few key conclusions that we feel have wider relevance and which we expect to help shape our own approach over the next decade.

Envirofit's cookstoves help reduce emissions, fuel consumption and cooking time.

Ultimately, we hope that our report stimulates thought and debate among our peers – other donors, foundations and social investors interested in scale – about reporting success and sharing lessons. Tackling global development challenges is not easy. Finding lasting solutions is even harder. Greater transparency about not just success but also the lessons learned from failure may help all those involved in this area achieve a much greater impact.[19]

17 Presentation to Aspen Philanthropy Group, 30 July 2010, by Jackie Khor of Impact Capital Advisors.

18 The Economist's article on "Non-Profit Capitalism" of 11 September 2008, noted the huge global capital market of the non-profit sector and how some were using IPOs to raise funds and offer their investors instead of simply a cash return, a 'perpetual interest in the organization seeking funds." (Cited in 'Knowledge Connect' published by the Centre for Social Impact, Edition 1, Spring 2008, page 1.) Susan Wolf Ditkoff and Susan J Colby argue that prior to the global recession foundation assets topped US$680 billion although have subsequently by 20% to 40% from their highs in 2007. Galvanizing Philanthropy, the Bridgespan Group, (2009)

19 In an inaugural speech delivered in June 2010, the new UK Secretary of State for International Development, Andrew Mitchell, made numerous calls for greater transparency in the development sector, announced a change at the UK's Department for International Development that would focus on 'transparency, accountability, responsibility and fairness' and announced the creation of an independent aid watchdog called the UK Aid Transparency Guarantee.

Evolving our Strategy

Shell Foundation was established in 2000 as an independent charitable foundation with a mission to catalyse sustainable and scaleable enterprise-based solutions to global development challenges. But unlike many corporate foundations at that time, we chose to pursue this mission using three specific approaches:

- **Focus:** We chose to focus on development challenges arising from the links between energy, poverty and the environment and the impact of globalisation on vulnerable communities
- **Business-based:** We started with the belief that the application of business thinking was essential to delivering solutions that were both sustainable and scaleable. As such, we have sought to deploy "more than money" when working with our partners extending our support to business strategy and implementation
- **Linkages to Shell:** We sought to explore whether we could add value to achieving our charitable mission by drawing on the skills, tools and market knowledge embedded in Shell businesses across the world

Over the past decade we have not deviated significantly from our mission or these three approaches. As described in Appendix 2, the **global development challenges** we have sought to focus on over the past decade comprise:

- Supporting the start-up and growth of small and medium-sized enterprises (SMEs) that represent the **Missing Middle** in emerging economies;
- Reducing the incidence of **Indoor Air Pollution (IAP)** that kills two million women and children each year in developing countries;
- Implementing sustainable solutions to **Urban Mobility** in the growing number of mega-cities in developing countries;
- Facilitating **Pro-poor Ethical Trade** by unlocking markets for developing country producers;
- Enhancing **Access to Modern Energy Services** for the poor in ways that are financially viable.

What has changed, over the past decade, however, is our strategy towards tackling these challenges. In this report we will share the lessons learned in relation to the three phases of our operations:

- **2000-2002:** Our inception phase during which an open Request for Proposals (RFP) process was used as the main way of selecting grantees;
- **2003-2005:** The period during which we shifted to piloting a number of strategic partnerships, either as the sole investor or together with other investors; and
- **2006 to date:** The period during which we focused our resources on the scale-up of a few partnerships.

What has changed, over the past decade, however, is our strategy towards tackling these challenges.

In 2006, we focused our resources on a few strategic partners with a view to helping them go to scale and achieve sustainability. This focus was rewarded by a significant improvement in our performance, with over 60% of all our initiatives (and 80% of the total value) having met our criteria for achieving scale and sustainability. This is illustrated in figures 1-6 on page 6. These charts reflect the percentage of our total grants that achieved scale according to our traffic light scoring system of red, amber, green for each different phase of our operations (see Appendix 2). They show the incremental reduction in the failure rate both in terms of the total amount awarded in grant finance (Figs 1-3) and the number of initiatives implemented (Figs 4-6). Our performance assessment confirms that our change in strategy and focus has contributed to an increase in the success of our grants.

In summary, we found that our initial reactive and open strategy to support multiple projects with NGOs alone did not yield much success with regard to achieving our intended goals of scale of impact or sustainability. By contrast, our shift to a more proactive and closed approach was far more successful. Today we focus on working directly, very closely and over the long-term with a strategic group of carefully selected partners. We believe these partners have the ability to co-catalyse sustainable new enterprise based solutions to development.

What do we mean by scale?

As in the traditional sense, we believe scale is first and foremost a question of simple economics. As scaleable enterprises grow, the average production cost per unit declines along with the marginal cost of adding another customer. But more important is the arithmetic. The magnitude of global poverty requires solutions that reach billions of people. For that to happen, solutions must be replicable in more than one country or region and able to generate sufficient earned income to sustain their growth. **For us, therefore, scale is about delivering cost-efficient solutions that benefit large numbers of poor people in multiple locations in ways that are ultimately financially viable.**

Scale is not a goal in itself. It is, however, in our experience, a critical component of achieving a long-term sustainable outcome. It is important not just because it allows for the efficient transfer of successful ideas and knowledge but also because it removes the need for perhaps hundreds of parallel efforts to solve essentially the same problem.

In the absence of agreed definitions, we set our own set of strict criteria to measure whether scale had been achieved. They were purposely conservative in order to avoid over reporting success. We adopted a simple traffic light system for scoring success against these criteria and sought wherever possible to agree these with our partners. Of the US$78 million we have committed as grants since inception, that specifically targeted scale and sustainability, 65% (approx. US$51 million) achieved scale according to our evaluation criteria, 19% (approx. US$15 million) were implemented successfully but showed no evidence of going to scale, and 16% (approx. US$12 million) failed to achieve intended outcomes.

Figures 1-3: Performance by Amount*:

Fig 1. Phase 1: 2000-2002

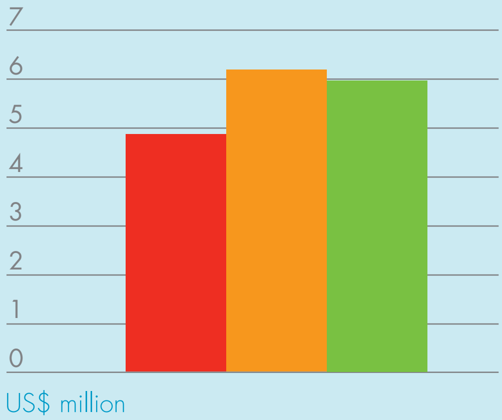


Fig 2. Phase 2: 2003-2005

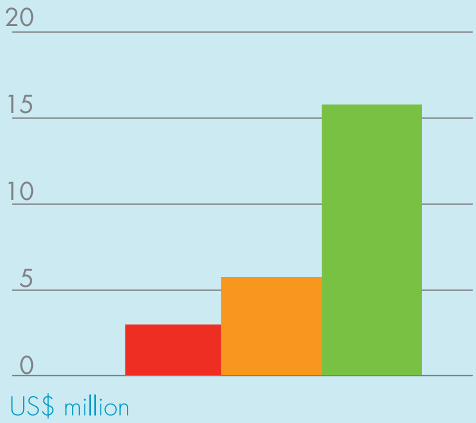
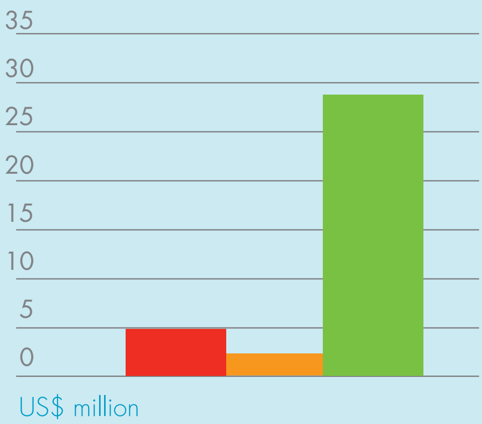


Fig 3. Phase 3: 2006-2008



Figures 4-6: Performance by Count:

Fig 4. Phase 1: 2000-2002

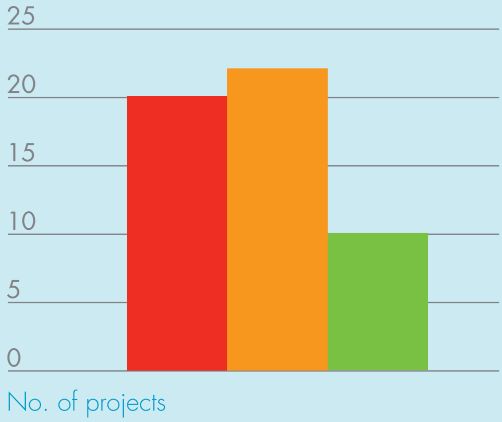


Fig 5. Phase 2: 2003-2005

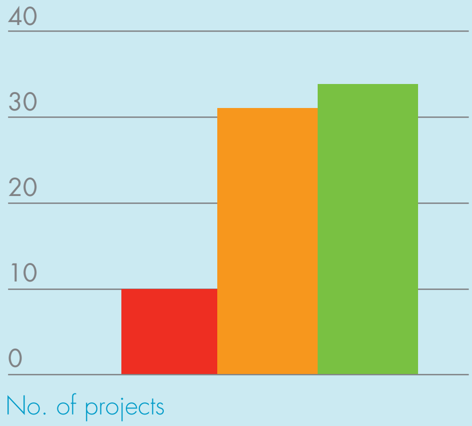
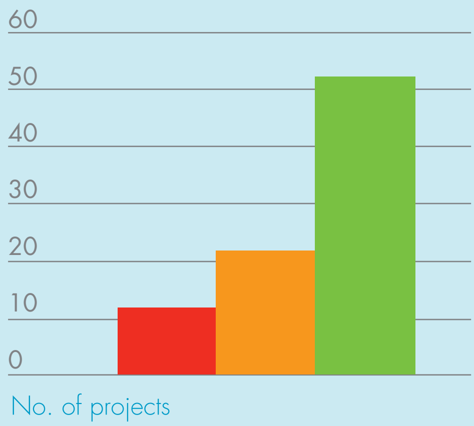


Fig 6. Phase 3: 2006-2008



***N.B. Performance in Phase 1 was positively skewed by the success of a single grant awarded to WRI/ EMBARQ of US$3.75 million in 2002.**

Grants/investments were judged to be green if they met our criteria for scale and sustainability (see Appendix 2). Large-scale development outcomes were measured by evaluating results against pre-agreed performance benchmarks.

Green Achieved scale/sustainability
Orange Achieved intended project objectives but no evidence of scale
Red Failed to meet intended project objectives

"Spray and Pray" is Not Scaleable

Since our inception we understood the need to keep our operations as focused as possible around a specific set of global development challenges. However, in the early stages of our operations we did this by consulting widely, publicising our areas of interest and then reviewing multiple proposals submitted by prospective grantees. It was the classic RFP methodology based on offering short-term (i.e. less than three years) grants of less than US$300,000 to not-for-profit organisations.

At the time, we believed it was the fairest and most transparent way to achieve our goals quickly and that the NGO sector was the right one to target given their knowledge and experience. During our inception phase (2000-2002), we received more than 840 applications in response to RFPs. Although we were very specific about our selection criteria, the overall quality of applications received was generally poor. After rigorous internal and external review, we ended up supporting just 35 projects (4% of those received) across multiple countries.

While lacking comparative data, we have no reason to believe that our selection process was any more or less efficient or effective than that applied by others adopting this approach. But our impact was poor. Of all the projects we supported in our inception phase, 80% failed to achieve any evidence of scale or sustainability. Of the 38% of projects that failed to even achieve their basic stated objectives, almost half (45%) did so due to poor execution by the partner (see Appendix 2).

The other main reason for failure was the inability of partners to meet the needs of their customers and market: in other words, the inability to ascertain whether people either wanted or valued a particular service or product. This issue, rather than the nature of the product or service, was often behind the failure of several of our energy projects in being able to scale-up. We learned to appreciate early on the importance of understanding the needs of the poor and of avoiding eternal dependency on subsidy.[20] Others share our experience.[21]

Of all the projects we supported in our inception phase, 80% failed to achieve any evidence of scale or sustainability.

20 Our use of the term subsidy refers to the provision of grants (our primary financial instrument) but could equally refer to "patient capital" as deployed by others.

21 "KickStart, offering a one-year guarantee, underwrites the risk of the up-front capital for small-scale farmers to buy foot pumps for irrigation. Fisher and Moon anticipate that the market will eventually grow to the point where the industry will be profitable, attracting the private sector, without the need for any subsidy" Skoll Social Entrepreneur, Martin Fisher, Design to Kickstart Incomes, 2007. http://www.socialedge.org/blogs/civic-entrepreneurship/archive/2010/03/02/skoll-social-entrepreneur-martin-fisher2019s-kickstart.

The conclusion we reached at the end of our inception phase was that backing a multitude of short-term, solely NGO-run projects that were not market-based was not likely to generate scale of impact or lasting change without a continued need for subsidy. By contrast, we had far greater success in our inception phase when we focused our resources – time and money – on developing new approaches with a few carefully selected partners or by supporting organisations with a clear market demand for the products or services they offered.

This experience taught us a lot and guided not only our renewed focus on scale and sustainability but led us quickly to evolve our strategy. As of 2003 we decided to cease RFPs and focus instead on working with strategic partners with a commitment to scale and sustainability. We greatly reduced the number of unsolicited proposals that we received and we declined submissions that were short-term or project in nature. As a result, our overall performance increased significantly: 41% of our grants (and 65% total commitments) made during the period 2003-2005 achieved scale and sustainability. Of the 22% of all initiatives we supported during this period that failed to achieve their intended objective, the main reason was the lack of business viability of the solution (44%) followed by poor execution (33%).

We have restructured our operations and now recruit staff with entrepreneurial flair, business acumen and the skills and ability to work collaboratively in joint-venture type relationships with partners. In addition we shifted our financial management systems to be able to report the deployment of all our resources – staff and financial – and not simply grant expenditure.

Two of our strategic partners – GroFin and EMBARQ – have achieved measurable scale, impact and sustainability. Two others – The Better Trading Company and Envirofit – are in the advanced stages of scale-up. Overviews of these partnerships are presented in the next section. We have other successful strategic partners that are in earlier stages of scale-up with respect to tackling other global development challenges, but we believe it premature to draw conclusions as to their success in this report.

Strategic Partnerships

Since our establishment we have worked with a wide range of organisations to tackle different development challenges. Today, however, our efforts are focused on a small select group of strategic partners and a limited number of development issues for the reasons outlined in the previous section. For the purpose of this report, we discuss primarily our four core partners with whom we have had a long-term relationship (i.e. for more than five years) and who have achieved scale and sustainability in their operations, or are clearly on the path to doing so.

While these four partnerships address four very different development challenges – the Missing Middle, IAP, Urban Mobility and Pro-poor Trade (see *Evolving Our Strategy* on page 4 for details) – our experience of working with them over time has highlighted strong structural and strategic commonalities. These commonalities form the basis of the four key lessons that we share in this report.

EMBARQ®
The WRI Center for Sustainable Transport

Sustainable solutions to urban mobility problems in developing mega-cities

Shell Foundation Strategy

40% of the world's population now live in mega-cities with populations over ten million. Poor people in the developing world suffer particularly from the economic impact of traffic congestion which causes pollution and lengthy commutes to work where public transport is inadequate. Transport is responsible for 25% of global green house gas (GHG) emissions with road transport the most significant cause. SF recognised that transport problems in cities are essentially a result of market failures: transport decision-making is too often supply rather than demand-driven leading to sub-optimal solutions. Having market tested the idea of creating a global centre for sustainable transport we collaborated with leading planning experts to identify a specialist partner that could deliver practical action-oriented solutions to city authorities.

Partnership

In 2002, following a restricted tender, we selected the World Resources Institute (WRI) as a strategic partner. WRI is an internationally respected environmental NGO who shared our desire to build a sustainable transport network that focused on in-country expertise and multiple stakeholder engagement. SF worked closely with WRI to co-create EMBARQ (www.embarq.org) and helped recruit a core team of multiple disciplinary experts (including engineers, policy advisers, health and safety experts and environmental specialists) headed by Director Nancy Kete, herself previously a senior environmental and trade adviser to the US government. Together we developed a plan for scale-up based on the creation of sustainable regional centres of excellence.

The Solution

EMBARQ acts as an independent broker and fosters government-business-civil society partnerships whose members are committed to finding solutions to the transportation-related problems in their cities. Within the framework of these partnerships, EMBARQ is empowered to identify, test, evaluate and implement comprehensive solutions to local transport problems within a three to five year time horizon. These include Bus Rapid Transit (BRT) systems, bus retrofits, cycling and pedestrian infrastructure, improved public spaces and transport safety measures. The goal is to establish a locally-run transport centre in each city that can expand its remit to exert increasing influence over transport policy in the country as a whole. By working in this way, EMBARQ aims to deliver measurable improvements in transport including fuel use, air pollution, quality and cost-effectiveness, public health impact, accessibility and road safety.

Investment

Since 2002, SF has invested US$13.5 million as grant subsidy towards establishing and building EMBARQ. In 2006 The Caterpillar Foundation (www.cat.com) became a global strategic partner through a contribution of US$7.5 million. On the back of this support, EMBARQ has leveraged additional funds from other regional and national supporters, increasing year on year to over US$2 million in 2009 when it also secured a five-year, US$30 million commitment from Bloomberg Philanthropies.

Development Outcomes

EMBARQ's team of experts now provides support for sustainable transport projects in 22 cities across the world, having leveraged over US$880 million to date into these projects. In Mexico City EMBARQ developed Metrobus, a 20 km long BRT corridor serviced by 97 articulated buses that carries more than 500,000 people each day, cutting travel times by 50% and reducing CO_2 by 80,000 tonnes a year. In 2007, EMBARQ played a key role in establishing the world's first inter-continental BRT corridor across the Bosphorus Bridge in Istanbul linking Europe with Asia. This 41 km route serves 800,000 people a day, saving each commuter an average two hours in travel and some 100,000 tonnes of CO_2 per year. EMBARQ's outcomes helped secure WRI's recognition as one of the top 50 pioneers of social and entrepreneurial innovation in the Phoenix economy by Volans.[22]

Istanbul's Bus Rapid Transit system saves 100,000 tonnes of CO_2 entering the atmosphere per year.

Scale and Sustainability

EMBARQ now operates in multiple locations with a focus on Latin America and South-East Asia through five regional centres in five different countries. The organisation has been hugely successful in leveraging SF involvement to secure further grant funding to cover medium-term expansion. With support from a team of *pro bono* Shell consultants, SF is now helping EMBARQ to move towards an earned income funding model based on a focused portfolio of products and several new revenue streams for services provided to cities. These include charging for transport policy and planning advice, technical consultancy, or brokering investment into transport infrastructure projects and will help provide revenue that can be deployed in poorer areas where urgent action is required.

Future Plans

SF will maintain its close relationship with EMBARQ by providing funding, strategic advice, performance analysis and governance as they continue to deepen their impact in Latin America, invest in growth in Turkey and India, and – when financially viable – expand into China. We will also help EMBARQ to set new standards for the measurement of air quality, health and road safety impacts of their urban mobility projects and to build the case for future large-scale investment to achieve these benefits across the transport sector by harnessing institutional investor interest in good quality clean projects at city-level.

22 The Phoenix Economy: 50 Pioneers in the Business of Social Innovation, Volans, 2009. www.volans.com

Market demonstration of Envirofit's clean cookstoves in India.

ENVIROFIT
making the world fit for humanity

Reducing Indoor Air Pollution (IAP) through the sale of improved cookstoves

Shell Foundation Strategy

IAP is the toxic smoke created by using wood, charcoal or other biomass to cook on open fires or with inefficient stoves in poorly ventilated homes. It is arguably the greatest energy-poverty issue impacting the lives of over three billion people and leading to the premature death of over 1.5 million people every year. It is widely acknowledged that the most viable way to reduce IAP at scale is for people to use clean cookstoves or clean fuels that reduce both emissions and fuel use. By 2007, SF had invested over US$4 million in nine pilots with a range of IAP-specialist NGO partners across the globe. While this resulted in significant sales of improved cookstoves, no pilot showed the potential for scale-up or sustainability.

As a result, we changed strategy and sought a global strategic partner with a proven track record in product design coupled with commercial experience in the marketing, distribution and sale of consumer durables.

Partnership

Envirofit International (www.envirofit.org) – a US-based non-profit organisation – was selected as our global strategic partner following a restricted tender in 2007. While Envirofit had no prior experience in producing clean cookstoves, they had a strong track record in engineering environmental solutions for application in developing countries (enhanced by their close links to Colorado State University) and their Chairman and CEO, Ron Bills, had managed several for-profit companies involved in product development, distribution and sales.

The Solution

To achieve the desired global health, environmental, social and economic impact of tackling IAP, hundreds of millions of clean cookstoves need to be sold. From the outset, SF and Envirofit worked together to develop a viable business model, conduct in-depth consumer market research, undertake ground-breaking R&D in product development and establish distribution and sales networks with an initial focus on southern India. Envirofit has subsequently produced a line of durable clean cookstoves that currently retail for between US$15-US$30 in India. Compared to traditional cooking fires, these reduce emissions, improve fuel efficiency, and are perceived to reduce cooking time significantly. A recent independent study in India has rated the stove as the preferred one as it is modern looking, has high fuel efficiency, uses traditional fuel and is portable and smokeless.

Envirofit has recently produced a clean charcoal burning stove which is now being sold in Africa and other developing countries. As part of wider efforts to enhance sales of clean cookstoves, SF developed and implemented local and national IAP awareness-raising campaigns ("Room to Breathe"), and established a range of effective distribution channels through partnerships with microfinance institutions and NGOs. It has also supported Berkeley Air Monitoring Group (www.berkeleyair.com) to conduct independent monitoring of the performance of the stoves. Recent field work in India concluded that the Envirofit stoves showed statistically significant reductions of PM2.5, CO_2 and fuel use. Additionally, 78% of users reported that cooking time was reduced compared to their traditional stove, 89% reported that the improved stove saved fuel and 97% found the improved stove easier to use.

Investment

Over the period 2007 to date, Shell Foundation has committed US$12.3 million as grant funding towards the development of a range of clean cookstoves as well as building up the capacity and operational systems of both Envirofit International and Envirofit India. In 2010 Envirofit started expanding into Africa and is expected to scale-up further in 2011.

Development Outcomes

Since early 2008, Envirofit has evolved into the market leader in sales of clean cookstoves across India. Aggregate sales to date of more than 150,000 stoves benefit an estimated 600,000 IAP affected people. With a durability of three to five years depending on the model, stoves sold to date are predicted to save over US$30 million for India's lowest-income consumers through fuel-saving of over 600,000 tonnes of wood and preventing one million tonnes of carbon from entering the atmosphere. The business has also created over 500 local jobs through the growth of its 400-strong network of manufacturing, sales and distribution channel partners.

Scale and Sustainability

Envirofit has succeeded in creating a sustained and growing market for its clean cookstove products in India. As market growth continues, Envirofit will shift further towards localised assembly and manufacture so as to continue efforts to lower end-user costs. As with many other types of consumer durable products aimed at the Bottom of the Pyramid, it takes a long time for this high volume, low margin business to reach the tipping point whereby sales growth is generated largely through brand awareness. Despite increasing earned income and improving gross margins, Envirofit will rely upon grant funding in its continuing efforts to both develop and market better performing and cheaper stoves until it achieves financial break even expected in 2014.

Future Plans

In line with meeting agreed Key Performance Indicators, SF will continue to support Envirofit with regards to its own global scale-up plans for clean cookstoves. SF is also a founding partner in the Global Alliance for Clean Cookstoves, hosted by the UN Foundation (www.unfoundation.org) to establish international standards and testing protocols for clean cookstoves, fund related health and climate research, and develop innovative financing mechanisms that aim to create a thriving global market for clean and efficient cooking solutions such as clean cookstoves and fuels. Their "100 by 20" goal is: 100 million households to have adopted clean and efficient cooking solutions by 2020.

GroFin has enabled Sebbagala & Sons to develop their electrical centre in Uganda.

GroFin

Sustainable job creation through supporting SME sector development in Africa

Shell Foundation Strategy

We, like many others, recognised how the Missing Middle in emerging economies was frustrating pro-poor economic growth and job creation. In view of our own experience in starting and growing small enterprises, we believed that the solution to this problem lay in the integrated provision of both business development assistance and risk capital to viable start-up and growing enterprises. We chose to test two approaches – one based on partnering with a financial institution and one based on partnering with a specialist intermediary. Based upon both performance and ability to go to scale, we subsequently focused all our efforts on the latter approach.

Partnership

In 2001 there were very few organisations providing both business development assistance and risk capital to small enterprises. We met Jurie Willemse, a serial entrepreneur and founder of Rural Area Power Solutions (RAPS – a South African energy, finance and development company). Building on both his track record and through co-developing a business model that was designed from the outset to achieve scale and long-term financial viability, we co-established a pilot SME fund in South Africa (the Empowerment through Energy Fund). Drawing on the early success of this Fund, and after refining the business model, other larger SME funds were co-established across Africa. In 2004 GroFin (www.GroFin.com) was established as a specialist finance company providing both business development assistance and risk capital to viable start-up or growing businesses.

The Integrated Solution

Pre-investment business development assistance is provided by GroFin's local teams of investment professionals to start-up and growing enterprises. Those judged to be capable of viable growth – as opposed to having collateral available – are then provided with mezzanine finance of between US$100,000 and US$1 million typically in the form of medium-term loans and cash-flow based performance incentives. During the financing term, mentoring support is provided by GroFin to help enterprises achieve their growth objectives.

Investment

Over the period 2002-2007, SF committed US$11.5 million as grant funding towards recruiting and training GroFin staff, establishing operational systems and setting up local offices across Africa. GroFin was a significant co-contributor towards all these set-up costs. Through acting as an anchor investor, SF committed US$8 million in the form of risk capital contributions to GroFin managed funds over this period (with all returns to be reinvested in scale-up) and in 2008 invested US$15 million in the GroFin Africa Fund. GroFin currently has a total of US$245 million under management for SME funds in Africa based on investments by a wide range of development finance institutions (including the International Finance Corporation, the African Development Bank, CDC and FMO) as well as African banks.

Development Outcomes

The average size of investment in the 188 enterprises financed as of July 2010 (of which 28% are start-ups) is US$389,000 over an average term period of 51 months. These enterprises have to date generated 2,664 new sustainable jobs and have maintained a further 3,016 jobs. It is estimated that a further 41,958 people have benefitted through impacts on households and indirect employment.

Scale and Sustainability

GroFin now has over 100 staff working in local offices in South Africa, Kenya, Tanzania, Uganda, Ghana, Rwanda and Nigeria. The US$160 million GroFin Africa Fund is the world's largest fund targeting the sub US$1 million SME sector. GroFin's performance to date demonstrates both the strong market demand from local SMEs for integrated skills support and finance, as well as robustness of the business model under different market conditions. Based on the scale of leveraged funds, GroFin has not required further grant support from SF since 2007.

Future Plans

GroFin has a vision to have US$1 billion under management and to be operating in over 25 emerging economies worldwide by 2020. But even if this vision is achieved, it will still mean that the SME sector is woefully under-served across the world. To encourage greater investment, both SF and GroFin are promoting Growth Finance as a new commercially viable asset class, targeting start-up and growing enterprises, that has the potential to rival the growth and global impact of micro-finance. As part of our efforts to build the emerging Growth Finance sector, in 2008 SF helped establish Optima (www.optima.mu) as a specialist provider of skills and support to SME fund managers and investors.

Small holder farmers in Zimbabwe now supply chillies to McIllenny Company in the US for use in Tabasco sauce.

THE BETTER TRADING CO

THE BETTER FLOWER CO

Pro-poor ethical trade: unlocking markets for developing country producers

Shell Foundation Strategy

Connecting international retailers with producers in developing countries to supply goods to international markets can positively impact the livelihoods of rural communities. However, small-scale producers often lack the skills, capital and business expertise to deal with the demands of sophisticated export markets. International retailers, for their part, often struggle to reliably source from the developing world despite growing demand for high quality products with ethical credentials. SF's initial three year collaboration with UK retailer Marks & Spencer (M&S) showed that it is possible to create new value chains that both alleviate poverty at the farm level and deliver commercial returns to retailers through the creation of an intermediary that could represent both producers and retailers. To do this at scale, we have created ethical agents to bridge the gap between developing country producers and the mature retail markets.

Partnership

Our work with M&S helped us understand how to unlock markets for developing country producers by providing seed capital, business mentoring and strategic partnerships with major retailers to create sustainable supply chains. Based on our early experience and a strategic review of the development challenge, in late 2007, we created a strategic scale-up partner, the ethical agent, The Better Trading Company (TBTC) (www.thebettertradingcompany.com) linking retailers with a range of small agricultural producers. In 2008, TBTC established a specialised subsidiary, The Better Flower Company (TBFC) (www.thebetterflowercompany.com) focusing specifically on new and value-added niche products in the cut flowers sector. UK retailers Waitrose and Tesco now source directly from TBFC benefitting struggling rural communities in South Africa and contributing to greater transparency in the supply chain by building direct relationships.

The Solution

Ethical agents help developing world agricultural producers form partnerships with retailers and understand the product development challenges of accessing highly competitive international retail markets. Retailers demand innovative products of consistently high quality, at the right time, in the right quantity. Our ethical agents provide market intelligence, business skills, technical skills and training to help producers deliver the right product and meet retail requirements. Retailers get access to exciting new products that respond to the growing demands of ethical consumers. They also improve their supply chain management through better knowledge of possible product ranges and seasonality in the developing world, and tailored engagement programmes with workers (following baseline studies to identify the key issues affecting them and opportunities for improvement). Ethical agents facilitate transparency in trading relationships by encouraging fairer information flow around costs and margins and add a human factor by connecting producers face-to-face with retailers – a practice that is not commonplace in this fast-paced market sector.

Investment

Since 2007, SF has invested nearly US$5.7 million in developing a range of ethical intermediaries to suit different and various aspects of the supply chain. SF has provided US$3.9 million in grant subsidy to TBTC and TBFC, and a bank guarantee of US$480,000 for TBFC.

Development Outcomes

Ethical agents created by SF have improved the livelihoods of thousands of producers in rural communities in Africa. SF's work with TBTC and TBFC has created a new model that has helped small businesses sell niche agricultural and horticultural products such as wild flowers, Rooibos tea, chillies, tea tree oil and honey. Their clients include Waitrose, Woolworths South Africa, The Body Shop and the McIlhenny Company (maker of *Tabasco* sauce). This effort has helped create over 492 new jobs, directly increased 2,150 incomes and improved 8,600 livelihoods and has led to growing retailer interest to work with ethical agents.

Scale and Sustainability

SF's ethical agents have proved the size of the market, the market need and the business case. With all our pilots still in their early stages, we have been able to identify the elements of scaleability by proving the market demand and showing that retailers are increasingly willing to address some of the issues arising from global supply chain management and the growing demand for ethical products. These models can now be used to influence the supermarket sector and other retailers to support development rather than cause social and environmental damage. Ethical agents will demonstrate real scale once they have secured a range of international retailers as clients. TBTC and TBFC are now witnessing more demand from international retailers who in turn are increasingly recognising that sustainability is key to competitiveness and has a commercial value. Producers are also acknowledging the value of better resource management with ethical agents working to help them understand the benefits of sustainable farming with an increased focus on both addressing social issues and taking advantage of opportunities to empower their workers.

Future Plans

SF will remain an energetic champion of the creation of specialist agents capable of catalysing the mutually beneficial relationships of retailers and developing world producers. Only through the network expansion of such agents can industry significantly impact both economic growth and quality of life in low income countries. Recognising the need for distinct types of intermediaries for different markets, SF has pioneered an additional two models, one focusing on small holder producers of commodity crops and the other in high value, complex agricultural product markets. Both have completed successful pilots. Much progress has been made to consolidate the case for change. The next challenge for SF and the organisations who share our approach is to encourage big business, governments and other retail industry stakeholders to pick up the baton.

Lesson One: Catalysing Disruptive Change: Angel Philanthropy

The Importance of "New"

One of the most illuminating and surprising lessons that we have learned is that our greatest success in achieving scale of impact and sustainability is associated with newly created entities (as opposed to traditional, well-established ones with an existing track record) that have all pioneered new solutions to old challenges. While we never set out with this specific intent, we also find it revealing that we played a pivotal role in co-founding all of these ventures and sharing their risk, much as an angel investor would in a purely commercial investment.

1

For example, during our inception phase we market tested the idea of creating a sustainable transport centre as opposed to a strategy based on funding a number of sustainable transport-related projects. We concluded that an intermediary was required to run such a centre both for credibility as well as to enable scale. We then launched a limited tender, following which the World Resources Institute (WRI) was selected to host EMBARQ. Together with WRI we established the first regional centre in Mexico to pilot this new partnership. The disruptive approach to creating a new intermediary was the key starting point to the eventual scale-up and success of EMBARQ.

Similarly, during our inception phase we piloted two approaches to support the SME energy sector in Africa. The first involved collaboration with a reputable bank in Uganda (DFCU) to extend advice and finance to local enterprises. While the scheme successfully met its intended objectives, we concluded that it did not provide an appropriate institutional platform for scale without continued subsidy. It also wasn't able to address the vital business skills needs of SMEs. By contrast, our initial partnership with RAPS in South Africa led us to realise that a specialised intermediary providing both business skills and finance to start-up and growing enterprises was the most effective way to pioneer a sustainable and scaleable solution to the Missing Middle. Out of this partnership emerged GroFin, created in 2004. Again, a disruptive approach based on testing a new business model with a new intermediary partner was the key to the eventual success of GroFin.

Our other successful partners were equally a result of catalysing disruptive change. TBTC, which was founded in 2007, emerged from prior collaboration between us, three African entrepreneurs and a three year partnership with M&S. We jointly recognised that a business-based solution was the most scaleable and sustainable solution for the value chain since it linked producers to markets. This realisation was the forerunner of this new ethical agent.

During our early phases of operation we failed to achieve scale or sustainability in the production and distribution of good quality, durable and affordable improved cookstoves. We therefore shifted strategy and sought a new global strategic partner that had no previous experience of tackling IAP but had good product design experience and a commercial mindset. We considered these as key to delivering a market-based scaleable solution to the mass sale of clean cookstoves. This led us to partner with Envirofit, an NGO with an established track record in the development of well-engineered energy products coupled with commercial experience in the sale of consumer durables. This disruptive approach has resulted in Envirofit quickly becoming the market leader in sales of improved cookstoves in India.

We have been able to foster innovation and incubate new and successful approaches by being able to work closely together with a selected partner in testing a new business model, and absorbing the associated initial costs through subsidy provision. In essence we applied angel investment thinking to philanthropy.

While we appreciate that this is a small sample size on which to base more generalised conclusions, we are struck by the consistency with which all our success can be attributed to newly established ventures – be they for-profits or not-for-profits. To this end we share the viewpoint offered by Volans that: "...disproportionate effort continues to be lavished on shoring up the dinosaurs of the old order, rather than investing in the new pioneers, who are working hard – and often against the odds – to incubate and scale market solutions essential for a sustainable future."[23] Our own

23 The Phoenix Economy: 50 Pioneers in the Business of Social Innovation, Volans – the Business of Social Innovation. The Volans 'Pathways to Scale' model of change: "Each new business model will typically begin at Stage 1, with the early recognition of an opportunity for a new solution; the 'Eureka' moment. In Stage 2, that initial idea is put to the test, with prototypes and experimentation. Over time, successful experiments evolve into solutions around which new, Stage 3 business models and enterprises are created. Stage 4 sees the focus shift to the evolution of broader ecosystems of change agents – involving a growing number of public, private and citizen sector partnerships, followed by secondary waves of imitation. Ultimately if anything like a truly sustainable and equitable future is to be achieved entrepreneurial initiatives will need to scale-up further to Stage 5, system change – typified by broad-based market and societal adoption of new mindsets, models and technologies. Success in moving from Stage 4 to 5 will involve the transformation of political priorities, governance process, market rules and cultures."

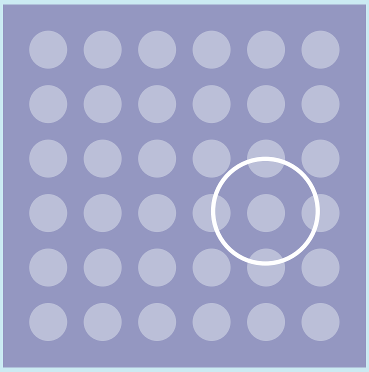
Fig 7: Volans 'Pathways to Scale' model of change

Stage 1

Eureka!

Opportunity is revealed via the growing dysfunctions of the existing order

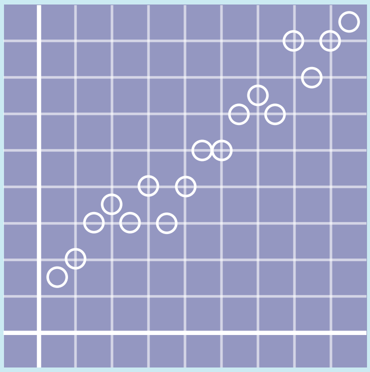
Stage 2



Experiment

Innovators and entrepreneurs begin to experiment – a period of trial-and-error

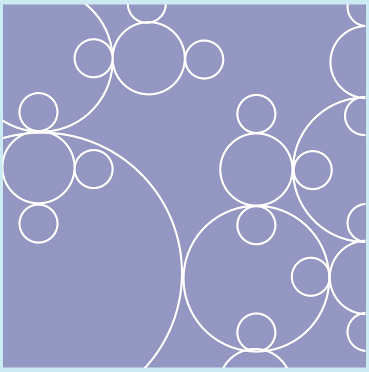
Stage 3



Enterprise

Investors and managers build new business models – creating new forms of value

Stage 4



Ecosystem

Critical mass is achieved through alliances and imitation

Stage 5

Economy

The economic system flips to a more sustainable state – driving market and institutional transformations

experience testifies to the eureka moment identified in the Pathways to Scale model of Volans (which identified EMBARQ as one of the 50 pioneers illustrating this thinking – see Fig 7 above).

Supporting a new partner to catalyse a new solution to a specific development challenge requires us to focus our efforts and resources. In consequence we accept a high degree of risk before these partnerships and models are proven in the market. It also requires us to work closely with our partners so that we can truly understand their business, set appropriate performance targets and be flexible in considering how best to address the inevitable challenges that emerge. By contrast, our early experience of allocating grants to multiple partners for short-term projects did not allow for sufficient engagement with our partners to understand their operations. As a result we struggled to support them with their challenges and weren't able to transfer "more than money". Our experience as angel philanthropists leads us, therefore, to conclude that developing new concepts and disrupting the status quo, has proven the most effective way to achieve scale and sustainability.

We recognise there are certain constraints to replicating this approach. It requires broad networks. Our own personal networks – generated through work in both the private sector and development sector – were key to our ability to identify potential partners. It also requires an acceptance of a high level of performance risk. Testing new solutions with new partners in new markets, with the potential downside that a small number of failures in a small portfolio can have a far higher impact than one spread across numerous investments, is a high risk approach. We were fortunate in that our Trustees both fully endorsed our angel philanthropy approach and encouraged and advised us on the implementation of a robust and disciplined risk management process.

Our experience suggests that catalytic angel philanthropy offers the most effective route for creating pioneers capable of going to scale. And we believe, as others working in the same sector testify[24], that innovative pioneers are critical to addressing global development challenges at scale.

Get the right entrepreneur

When reviewing our performance, it is clear that a commonality underpinning our most successful partnerships is that the senior executive is either someone with prior commercial experience (e.g. GroFin, Envirofit, The Better Flower Company) or with a history of innovative thinking and practice in the social sector (e.g. EMBARQ). Conversely where we have witnessed poor execution we have found this to be correlated to leaders that lack either entrepreneurial flair or business acumen.[25]

Again, this conclusion will not necessarily come as a surprise to others. But of potentially wider interest are the lessons we have learned – and continue to learn – with respect to identifying and selecting entrepreneurial partners. Despite the recognition and emergence of a new class of social entrepreneur[26] finding quality partners is hard and unlikely to occur through an open reactive process of soliciting applications. This is partly because such entrepreneurs, especially those coming from the private sector, are not naturally attuned to seeking support from foundations and other donors. It is also because such essential networks that might connect them are still maturing.

Over time we have implemented ever more rigorous partner selection criteria. Rather than simply assessing a written proposal or plan, we now give greater emphasis to assessing the lead people involved, using the following core criteria:

- Personal alignment around the importance of achieving verifiable social benefit through solutions that can be delivered at scale and sustainably;
- Evidence of being able to execute a venture both at the start-up and during its growth stages (substantiated by prior personal track record);
- Commitment to focusing 100% on the venture and sharing risks in trying to achieve success; and
- Understanding of and acceptance of the need to comply with our Business Principles.

We recognise that selecting the right person is more of an art than a science and that we still have much to learn in this respect (notably from venture capitalists and other angel investors).

24 Richard Branson, the founder of the Virgin Group notes that the most important lesson that he has learned is "to get the right people in key positions." (p40) Alliance Magazine, Vol 15, 2 June, 2010

25 Ibid, p35. "We can succeed only if we have picked the right partners." (p35) Alliance Magazine, Vol 15, 2 June, 2010.

26 The Skoll Foundation which is dedicated to connecting and supporting social entrepreneurs, defines them as: "the change agents for society, seizing opportunities others miss by improving systems, inventing new approaches and creating sustainable solutions to change society for the better. However, unlike business entrepreneurs who are motivated by profits, social entrepreneurs are motivated to improve society. Despite this difference, social entrepreneurs are just as innovative and change oriented as their business counterparts, searching for new and better ways to solve the problems that plague society." http://www.skollfoundation.org/skollawards/glossary.asp

"A scaleable and commercially viable model is the basis for delivering the greatest developmental impact over the long-term."

Jurie Willemse, GroFin, Managing Director

However, we are pleased to note that the number and proportion of our co-founded ventures that fail due to poor execution has fallen considerably.

But starting up and growing *any* new venture is hard. There will always be associated partner risks that often only emerge when ventures are on the point of being successful whereby the venture itself is overly-reliant on a single (often the founder) individual. We have indeed encountered such risks and have worked closely with partners to resolve them. However, no matter how good the identification process and selection criteria, the success of any start-up is fragile, hard to maintain and vulnerable to changes in key staff. This is why we now reserve the right to include reference to any change in pre-determined key individuals as one of our standard event-of-default clauses in agreements we sign with partners.

Start-up risks in tackling global development challenges are likely to be greater than those in the traditional commercial sector. Even when a new solution is successful, it will probably deliver lower financial returns. In essence, it's "really hard… Venturing out on your own. No steady stream of income. No way to know that your idea will be the one that works, not the one that fails. No stability. No demarcation between life and work. People constantly questioning your progress…"[27] Shore *et al* agree, noting that "only a tiny fraction of successful companies ever scale [so be] … careful not to be too glib about scaling as if in fact it is an everyday occurrence."[28]

Sharing the Vision

A key lesson we have learned in achieving lasting scale of impact is the essential prerequisite to select a partner who shares an aligned vision. This means having a plan to achieve both social impact and financial viability from inception and which is subject to regular measurement and reporting. While this seems so obvious that it does not merit stating, our experience has repeatedly proven that only through investing time in early open and honest face-to-face discussions can one develop a shared vision, mission and approach. Aligned vision is hard to assess through a desk-based review of a short-term project.

Our strategic partnership with GroFin was based on a clear understanding of our shared goal to achieve scale and sustainability. "For us it was always about developing a business model that you can scale-up and replicate in numerous countries and regions and which sustainably addresses the needs of start-up and growing businesses – a solution of global value for emerging economies rather than just a few countries in Africa. A scaleable and commercially viable model is the basis for delivering the greatest developmental impact over the long term," says Jurie Willemse, GroFin's managing director.

27 Adrienne Villani, Romanticising Social Entrepreneurship, 12 April, 2010, www.beyondprofit.com. Villani goes on to add: "Everyone wants a piece of the action. What is cooler than chasing your dreams and having a social impact? No one is ever going to accuse you of selling out to the machine, of being a slave to the man. Instead, you are going to sit with your MacBook in your Ray-Bans and Birkenstocks, eating organic dried fruit and bring affordable drip irrigation to five million Indian farmers in the next three years. Yep, that is what you are going to accomplish. No sweat."

28 Bill Shore Jennifer Vanica, Mario Morino, Sean Closkey, Clara Miller, Julius Walls, and George Gendron, Achieving Impact and Sustainability through Market-Based Approaches: Discussion Highlights, A convening sponsored by Community Wealth Ventures, 27 October 2007, Washington, DC: Community Wealth Ventures, March 2008.

> "The world is a big place and there are hundreds of cities that require sustainable transport solutions. By starting in Mexico City and demonstrating success we were able to generate sufficient traction to replicate these solutions in other places."
>
> Nancy Kete, EMBARQ, former Managing Director

EMBARQ is also a good example of strong mutual understanding of the desire to achieve scale. As Nancy Kete, EMBARQ's former managing director notes: "We understood early on that we needed to achieve significant change in at least three to five developing countries as this was required to create a multiplier effect. The world is a big place and there are hundreds of cities that require sustainable transport solutions. By starting in Mexico City and demonstrating success we were able to generate sufficient traction to replicate these solutions in other places." She concludes: "That was always the golden apple – achieving success in iconic places so that we could trigger replication in other places. Now we see many more cities in Mexico and other countries around the world wanting to work with EMBARQ."

By contrast, we embarked on several partnerships where it later became clear that where we thought we shared an aligned vision, in reality we didn't. For example, we failed to achieve scale with one specific partner in part because we disagreed on the route to it. While we advocated for several years the need to focus resources on replicating successful initiatives and building local capacity, our partner was adamant that success lay in testing a large and growing number of different solutions. Similarly, other ventures failed because we had different perspectives from our partners about the importance of securing earned income rather than relying purely on subsidy. Again, it took time to discover this discrepancy.

Over the past five years we have modified our approach to maximise the likelihood of identifying a partner with an aligned vision. We now focus on reviewing or co-developing business plans instead of simply reviewing project proposals. We recognise the need to assign a staff member to work closely with each partner during the design and testing of any new initiative. Such intimate understanding of the challenges our partners face enables us to structure and deliver value-adding support more effectively.

Success is not secured just by agreeing a vision. It's also about resourcing accordingly. We have learned that it is exceedingly difficult to retrofit a venture to achieve scale and sustainability. "If you build small it's difficult to upscale. You have to have devised a plan from day one that provides the platform for going to scale notably by recruiting the best staff and developing robust operating systems even before the market is fully tested", says Willemse. "Everyone wants to solve a couple of billion-dollar problems with a few thousand dollars," he adds. Industry commentators make similar points about the challenge of building capacity for the sheer size of scale.[29]

29 "Scaling Impact: How to get 100x the results with 2x the organisation", Jeffrey Bradach, Stanford Social Innovation Review, Summer 2010. "Finding ways to scale an organisation's impact without scaling its size is the new frontier in the field of social innovation."

"You can't solve a problem that affects half the world's population one village at a time."

Ron Bills, Envirofit, Managing Director

While all new solutions start off small – both in terms of finance and number of partners – we have learned that there must be sufficient investment upfront to allow for planned scale-up. As David Carrington, a development consultant with specific expertise in the foundation sector, notes: "Some of the most important lessons are learned at the level of small-scale intervention – small incremental things such as serendipity, getting the right people in the right room at the right time. But to achieve longer-term success and size, the systems and people invested in, in the beginning need to have the potential for much larger more complex operations."[30]

This perspective is shared by others working in the same sector. The joint work done by the UK government's Department for International Development and the Swiss Agency for Development and Cooperation makes the point that "starting small to achieve ambitious objectives may be a perfectly valid strategy but small "pilot" projects, if they are to achieve larger-scale impact, need to be grounded in the incentives of players, the transactions between them and the supporting functions required for growth. Small that can only ever be small – the worthy tokenism of some development efforts – is not consistent with [making markets work for the poor]."[31] Equally Kramer *et al* note that "... we have to say out loud: The end goal of this work is to solve the world's most intractable problems. We have to be bold enough to say: Let's end poverty, let's cure disease. If we're not that bold, we don't need to change what we're doing – but we won't solve these problems either."[32]

Our experience with Envirofit reiterates this point. "You can't solve a problem that affects half the world's population one village at a time," notes Ron Bills, Envirofit's Managing Director. "We had a ramp up plan from focusing on the lowest hanging fruit in India and Africa to moving to a sustainable business model, with in-country business opportunities and local staff."[33]

30 Interview by Shell Foundation with David Carrington, 27 April, 2010. http://www.davidcarrington.net.

31 *A Synthesis of the Making Markets Work for the Poor (M4P) Approach*, financed by the UK Department for International Development (DFID) and the Swiss Agency for Development and Cooperation (SDC), p29-30.

32 FSG's report on Breakthrough in Shared Measurement and Social Impact by Mark Kramer, Marcie Parkhurst and Lalitha Vaidyanathan, 2009.

33 Skype's co-founder Niklas Zennstrom, agrees with this point having produced a highly successful product used by millions of people globally. He acknowledges that the size of the challenge was too big to think small: "From the beginning, we saw it as something that could be used by hundreds of millions of people and make a big difference in how people communicate." Interview with Niklas Zennstrom, Focus on Rethinking Scale, Alliance magazine, Vol 15, No 2, June 2010.

Lesson Two: Building Sectoral Pioneers

Building Sustainable Enterprise

Creating scaleable and sustainable enterprises requires building core capacity, slick operational systems and a robust infrastructure early on. This means recruiting the best staff and developing efficient operating systems from the start. Without these, being able to manage complex multiple location operations, as scale requires, becomes extremely difficult. Equally, the early adoption of efficient systems and procedures (e.g. IT, MIS, HR, communications) that automate and reduce the cost of day-to-day operations, significantly enhances the potential for scale.

2

Our early experience was that short-term project based funding neither helped us nor our partners achieve these objectives. Indeed it led us to believe that to achieve scale and sustainability, we needed to change strategy and move away from supporting time-limited activities, which we see as akin to buying services from a partner to deliver pre-agreed outputs. Instead, we have shifted towards building viability through the provision of long-term core funding and support to our partners that can build capacity for business plan-related milestones.

We discovered – retroactively – that these views were shared by others. For example, Overholser's building vs. buying argument proposes that only once an enterprise is built can it move on to other initiatives: "Indeed, it is precisely by dismantling their growth capital "scaffolding" that they prove they have built an enterprise that can stand on its own. Buying from the enterprise…isn't about changing what the enterprise does; it's about asking the enterprise to do more of what it already knows how to do. So it's not about risk, or about shifts in strategy." [34]

We believe our operational experience with our partners reflects this. Only through providing long-term core funding support to EMBARQ was it possible for them to recruit quality staff, develop a network of regional centres, and have the staying power necessary to build trusted relations with city partners. All of these were essential to their longer-term expansion and scale-up. As Nancy Kete explains, "You have to use initial grant finance to build capacity. Only once we had a credible, established business model and were recognised in a number of key markets as an independent entity could we really deliver a customer value proposition." She also points out that, "Only through this could we ultimately begin to think about how to diversify EMBARQ's revenue by developing some earned income streams that would enable the business to progressively move away from grant dependency."

There are of course risks associated with our approach. The first and most obvious is that considerable investment of time and money is required before the partner is able to demonstrate a market for their products or services or realise significant developmental benefits. So trying to select the right partners and being patient are critical to reduce risk.

However, even with the right partners, things can go wrong in unexpected ways. Given that our focused approach means we tend to have just five to seven strategic partners in the scale-up phase at any one time, the proportional impact of failure is high. Indeed, this realisation lies behind our aversion to applying the word "project" to our investments. We firmly believe that we need to focus on building institutions and not time-limited projects.

We have also had to develop a more rigorous approach towards terminating partnerships, wherever possible by mutual agreement. This relies on our ability to identify quickly and accurately signs of whether that they can or can't achieve scale. While we recognise we have more to learn, we believe an approach based on taking bold risks must be balanced by a robust process of taking tough and early exit decisions.

Considerable investment of time and money is required before the partner is able to demonstrate a market for their products or services or realise significant developmental benefits.

34 Overholser explains: "Building the Enterprise (e.g. investing capital towards the creation of a tutoring outfit) requires growth capital and close stewardship. It requires a patient process of trial and error. It is highly technical and has a high risk of failure. More often than not, it requires major shifts in strategic direction, and major shifts in personnel…It's about "show me what you do, and how you stack up so I can decide whether I should buy here or go elsewhere." Finally, unlike building, buying is an ongoing thing, in the sense that if you buy something once and like it, then you might as well come back for more." Defining, Measuring and Managing Growth Capital in Nonprofit Enterprises. Part One: Building is not Buying By George M. Overholser, 1 January, 2006.

Despite the emergence of a growing class of social entrepreneurs and impact investors, our experience and that of many of our strategic partners is that there are still very few foundations or donors willing or able to provide the level and duration of subsidy required to build the core capacity of such organisations – and in particular for-profits – that aim to pilot and scale-up solutions to development challenges. All too often, our experience and that of our partners, has been that such concessional funding is drip-fed into the venture with significant restrictions, delays and conditions. Such behaviour can frustrate the chances of a partner achieving scale and sustainability since it may prevent the recipient from investing in high quality institutional infrastructure that can support taking a solution to scale and creating a much broader impact. Without effective angel philanthropy to test new solutions and build the upfront capacity of partners, we see a risk that the growing number of social investors or impact investors may not be able to help their investees fully achieve their scale-up potential.

Time, Patience and Investment

Our experience has shown that the complexity of catalysing enterprise-based solutions to development challenges requires a lot of time, patience and money – often substantially more than is initially foreseen. Achieving scale and sustainability is not a linear progression. In our experience, while it takes a good three to five years to reach the tipping point for delivering significant development returns it can take up to seven to ten years to achieve real scale and sustainability. We believe it's very difficult to fast-track scale and it's not for the faint-hearted. But it is where significant opportunity lies.

> We believe it's very difficult to fast-track scale and it's not for the faint-hearted. But it is where significant opportunity lies.

> In our experience, while it takes a good three to five years to reach the tipping point for delivering significant development returns it can take up to seven to ten years to achieve real scale and sustainability.

Scale also takes very significant investment. Our experience with three very different partners showed that it took some US$10-15 million of grant support to achieve a tangible impact. With GroFin, for example, we provided US$11.5 million in grant funding over seven years, with most of this being invested before a significant increase in developmental impact could be verified.

We provided a founding five year contribution of US$7.5 million to EMBARQ in 2002 and a subsequent five year grant of US$7.5 million in 2007. It was only towards the end of the first funding period that significant development outcomes were recorded by EMBARQ in Mexico City, and it was only in 2008 that EMBARQ was able to demonstrate multiple country success, secure major leverage and increase impact.

With our partner Envirofit we have invested similar time and money – US$12.3 million over four years, and we have witnessed a similar pattern. As Envirofit's Managing Director Ron Bills acknowledges, "Success in mass production takes time. It's complicated and requires a robust understanding of many different processes – the purchase of raw materials, production and manufacture, shipping and transportation, distribution and the entire value chain. You don't do it with an Excel spreadsheet. It takes an advanced system like SAP where we use expensive software and detailed order management systems to track from orders to accounts payable, and inventory management. So it also takes significant money."

It's not just the operational building process that takes time. Building brand equity also requires significant patience. Ron Bills points out that processes alone don't sell products. Brand visibility is critical but cannot be built overnight. SF is now working with Envirofit on raising brand awareness based on market research and structured marketing and sales and follow up. "But it's not easy," says Bills. "There are multiple value propositions to be articulated – why buying an improved cookstove is good for health reasons, financial reasons, fuel saving and so on."

The replication of innovative solutions is neither quick nor easy.

"The driving factors for success are almost always idiosyncratic, often dependent on the efforts of one or more champions, and closely linked to the particular circumstances of time and place...There is a view that a few processes or techniques that worked successfully in one setting can be disseminated in an almost uniform and self-contained package, a view that often underestimates or ignores the complex human, organisational and other context-specific issues."[35]

With a pro-poor enterprise, where the route to market doesn't already exist and where you still need to show bottom line impact, commercial success can take much longer than a traditional for-profit initiative. Envirofit works with a highly inefficient supply chain that doesn't exist for the "last mile". As a result, the programme is effectively trying to create a supply chain infrastructure from scratch for a single product category in some very untested space. Patience is of the essence and the jump from pilot to enterprise is usually a considerable step change with some rather steep learning curves.[36]

Conventional businesses struggle with numerous common start-up challenges but when there is also a development impact goal, these are compounded. We have learned that we need to be flexible. If things don't go as planned but are clearly heading towards the agreed end-point (scale) there has to be flexibility on how and when to get there. It takes a long time to secure tangible development results and commercial viability in a high-risk space.

And finally, undertaking initiatives that require a committed long-term focus before financial *and* developmental outcomes can be secured, requires SF to have a governing body that understands this principle. In our case our Board of Trustees (comprising three senior executives from Shell and three eminent external trustees) have been of fundamental importance.

More than Money

Building viable partners takes "more than money". We first acknowledged this in *Enterprise Solutions to Poverty*, and our experience since 2005 has simply reinforced this belief. Few development problems of any kind are solved permanently by simply giving money alone. While all of our partners have had their own key strengths, all have equally testified to the benefit received from some form of business support or advice from staff in SF. This could be broad business planning, participation at the governance level, specific support on issues such as product marketing, strategy review exercises or enhancing communications.

Other forms of additionality we have provided involve using our networks to facilitate market access, delivering training and guidance with respect to understanding and managing risk, and actively working with partners to leverage support from other investors. All this active participation means that we essentially work in

35 *Building on Success – Replication vs Propagation*', James Posner, 1 March 2009, *Alliance* magazine.

36 Patient Capital: The Next Step Forward? Why nonprofit capital funding often backfires, and how we can adapt traditional capital campaigns to fix the problem, by George Overholser, Founder and Managing Director, NFF Capital Partners, p5, 2010 "... replication...was not simply a question of rote repetition – it took tinkering...This knowledge took decades to amass – it took a lot of trial and error and a lot of money. In other words, it took a lot of exceedingly patient growth capital.

joint-venture relationships with the benefit to us that we fully understand the challenges faced by any business and are able to restructure our support accordingly. This has proven far more effective than sticking rigidly to monitoring progress against pre-agreed short-term objectives.

Since our establishment we sought to leverage our "independent yet linked" relationship with our corporate parent. We have tried to test whether we could harness – where appropriate – links with Shell that add value either to us directly or our partners in achieving our charitable objectives[37]. This was a radically new approach back in 2000 and one based on the premise that as a multinational company with over 100,000 employees in over 150 countries our corporate founder offered a potentially rich and diverse range of resources for us to tap into. Our success to date has been mixed, however.

Our common brand has been of tremendous and consistent value in leveraging support from others. It has been recognised by our partners as having the ability to convene power and facilitate access. GroFin's Jurie Willemse acknowledges that the brand facilitated access to financing institutions that may not otherwise have been receptive. "We used the Shell brand a lot to get introduced to other investors. It's very different when they know you have the backing of the corporate. It gave us credibility and leveraged access."

In terms of other linkages, only a total of 17% of the initiatives we supported over the past decade harnessed any non-financial *pro bono* support from Shell. This non-brand support was most commonly provided in the form of business skills provision by Shell staff (50%), followed by local market knowledge (24%) physical infrastructure (11%) and access to Shell business tools (6%).

Given that we explicitly sought from the outset to leverage our non-brand links with Shell, we find this level of engagement somewhat disappointing and far lower than we expected. We think there are several reasons for this. First is the unsurprising mutual anxiety about respecting our charitable independence. In our early years this served to isolate us from potentially value-adding support. We believe we are the first corporate foundation to have developed and published our own Business Principles (in 2007) that enshrine our "independent yet linked" relationship with Shell, and we have systems to ensure compliance with these. Second is the fact that senior executives of SF were all externally recruited, and thus it took time to develop all-important internal relationships.

Our strategic partners have benefited from non-brand support from Shell. By way of just one example, EMBARQ benefited from *pro bono* advice in 2003 from Shell staff on how to apply business-framing tools when dealing with cities and again in 2009 when Shell consultants gave *pro bono* support to developing a new business plan and strategy. In the main, the quality of the non-brand support to partners has been good as verified through our own annual customer surveys (which report an 80% satisfaction rate notably with respect to advice on specific issues such as marketing, finance and HSSE).

But sometimes we have experienced qualitative issues. On the rare occasions (three out of 44 initiatives) where our partners judged the support received from Shell to be less effective than expected, it was mainly because the large company and systems-based experience of Shell employees was less relevant to the flexible and entrepreneurial needs of start-up ventures tackling social challenges. We are now working to make sure that Shell employees supporting our partners are carefully selected and well briefed in advance to adapt to the working environment of a small-scale start-up.

We have always sought to recruit staff from Shell on the assumption that they would bring business skills and networks of value to our partners. Of our current staff of 14, 11 were recruited internally.

---

37 CAN argue in their Breakthrough, Scaling Up Social Enterprises, (2010) report that "Corporate skill and involvement can have powerful impact on social enterprise when it *is structured, focused and results orientated.*"

Of the 28 staff working for the Foundation since inception, only seven were hired externally. We believe that our choice to recruit internally has played a major part is us being able to deliver "more than money" support to our partners. But at the same time, we recognise the importance of having staff with a background in the development sector. We believe this combination of both business DNA and development DNA is a huge factor underpinning the success of our efforts to achieve scale and sustainability.

Being able to leverage Shell resources has proven to be a significant advantage to our partners and us on various occasions. However, we still believe that we have underused our links to our corporate founders and that this is an area where we can improve our collective performance. We see opportunity to further mine our links to Shell and draw more upon the skills, tools and market presence of the company. Equally we see an opportunity to further align our enterprise-based model focused on scale with the corporation's social investment programmes and approach to achieving sustainable development.

Lesson Three: From Subsidy to Earned Income

Market-Based Approach

We have consistently maintained that scaleable and lasting solutions to global development challenges could best be achieved through developing and offering good-quality products and services to the poor. This means providing products and services that they both valued and could afford. It also means delivering them in ways that can become financially viable so as to avoid donor dependency. In a nutshell this was our starting point in defining a market-based approach which essentially means one that treats the poor as customers and not as beneficiaries.

3

Over the past decade our experiences – good and bad – have reinforced our view that market-based approaches offer the greatest hope in tackling global market failures that impact the lives of the poor. The failure of many of our grantees in the inception phase to provide products or services that addressed the needs of their real customers (as opposed to the aspirations of their funders and donors) was highlighted in our 2005 *Enterprise Solutions to Poverty* Report.[38]

An example that captures this learning is the evolution of our Breathing Space programme that seeks to reduce IAP through the sale of improved cookstoves (ICS). The majority of the early pilot projects we supported were unsuccessful as they were based on the limited and inefficient production of often poor quality non-durable products that generated no real consumer demand. By contrast, Envirofit was able to rapidly become the market leader in the sale of ICS in southern India because they design and manufacture high quality and durable cookstoves at prices poor people can afford. They also take a commercial approach to sales and distribution.[39]

The "Voice of the Customer" (VOC) approach adopted by Envirofit was a key differentiator from other stove producers we encountered and continues to be core to their ongoing scale-up. As Ron Bills of Envirofit notes, "You really need to understand your customers and then develop products that are VOC driven and based on local market knowledge". Our experience is that the poor are no different to any other type of consumer. They want and value good quality, attractive, durable products that meet their needs are well designed and sold at prices they can afford.

We have learned exactly the same lesson with service provision. Together with GroFin we developed a new service offering a new business model to address a market failure, the Missing Middle. GroFin is a commercially based model that provides integrated business skills and risk capital for start-up and growing enterprises in Africa at a price they can afford. As Willemse says: "You always need to be customer centric and focus on what the end user needs[40] and develop a business model from that perspective. Understanding the client and building a business model around that is key." Willemse points out that GroFin's mid-term reviews of their first funds show quite clearly that they achieved very strong social economic development as well as acceptable financial returns to their investors.[41] He notes, however: "A key factor in our success was being able to take a market-based approach to creating a new business model for an un-serviced segment. Several years later, with operations in multiple countries and regions, we can clearly show that this approach worked."

But over the past decade we have learned that there are some inherent challenges in adopting a market-based approach to global development challenges. While none of them change our continued fundamental belief that this is the best way forward, we share these as we think they will offer a degree of realism to others seeking to replicate such market-based approaches.

---

38 Richard Branson concurs with this point in an interview with the *Alliance* magazine, Vol 15, Number 2, p40, June 2010 when he says: "Think about investing in solutions with a business approach so that your social investment is maximised."

39 "Correct pricing will be a critical issue for sustainability and requires an investment in the analysis of delivery costs, value proposition to customers and cost and pricing position relative to competitors," Breakthrough, Scaling Up Social Enterprises, CAN, 2010.

40 Both GroFin and Envirofit due to the commoditised product nature of their ventures regularly undertake consumer surveys and have built infrastructures that can process customer satisfaction data.

41 The Triple Value CDC report that provides a mid-point report on GroFin evaluates performance according to five key criteria: development outcome; financial performance; economic performance; ESG performance and private sector development. It assesses that only financial performance was "below expectations" with all four other metrics "successful" with the exception of Private Sector Development which was categorised as "excellent". Financial performance the report acknowledges was affected by the economic downturn, political crisis in Kenya and the considerable devaluation of local currencies (about 10-15%) in which the fund lends. (Triple Value Strategy Consulting, CDC, GroFin East Africa Fund Mid-Point Evaluation, 10 December 2009).

Firstly, bringing a new product or service to market requires considerable investment in building consumer understanding and stimulating demand. With EMBARQ, considerable time and effort was required to establish the best options for enhancing sustainable transport while also navigating the political complexities of cities and gaining the trust and confidence of multiple stakeholders. But once this tipping point was reached – through the perseverance of EMBARQ staff coupled with our flexibility and patient subsidy – it was demonstrated that urban poor were willing and able to pay a higher price to use a new Bus Rapid Transit system than alternative modes of transport. Customer surveys proved that this was because the urban poor placed a value on the enhanced quality of life associated with using faster, safer, more reliable and cleaner bus services.

Secondly, it is essential to place early emphasis on the marketing and pricing of new products or services. Our experience with GroFin illustrates this. Ask any entrepreneur in any country what they need to grow their business and they will respond "finance." But in reality, the vital service that most entrepreneurs need is targeted business development assistance (BDA) to ensure that their growth plans are both viable and sustainable. Yet traditionally this need was either not recognised or, if it was, it was typically provided as a free service through donor-funded consultant support. We always believed that BDA was an essential support service like any other to a business (e.g. water, electricity, IT) and as such should be marketed and priced to reflect its value. After adopting different approaches, we find that entrepreneurs in multiple countries are not only willing and able to pay BDA fees, but that this approach allows us to attract the best quality enterprises.

Thirdly, is the recognition that achieving scale is based upon addressing the entire value chain rather than just one component such as producers in developing countries. Many of our pilot projects that only gave support to pro-poor agriculture

> A key factor in our success was being able to take a market-based approach to creating a new business model for an un-serviced segment.

production failed either because there was no understanding of what consumers wanted to buy or any market linkages to buyers or retailers. Once we changed approach, and focused on understanding consumer demand and establishing linkages to retailers, we succeeded in helping producers gain fairer and sustainable access to value chains.

But through this process, we equally had to pioneer the creation of new ethical agents such as TBTC who not only provide support to producers but also establish market linkages with retailers. Such a value chain approach has triggered a change in behaviour of global retailers such as M&S. M&S acknowledged that the approach we adopted worked well and was commercially sound, and "opened our eyes to a whole range of different things that a retailer can do to get involved in development…it really stimulated our thinking in terms of working with small businesses and small holder farmers all across the developing world."[42] Similarly, C&A's Phil Chamberlain acknowledges that co-establishing CottonConnect, a new ethical intermediary, with SF has created a partnership that is "good for our business development, enabling us to meet the expectation of our consumers [while]… also creating something, which will have a beneficial effect on thousands of farmers and their families."

42 Katie Stafford, former Sustainable Development Manager, Marks & Spencer, p28, Fresh: Critical New Pathways to Ethical Sourcing," Shell Foundation report, 2008.

Finally we must acknowledge some limitations to market-based approaches. They require an appropriate enabling environment, which is still lacking in many emerging economies, and where there is a vital need for donor support. Our partnerships have improved access by the poor to various new products and services. However, issues of affordability, high transaction costs and risk mean that we have yet to see a systematic trickle down impact on the very poorest people.

Financial Viability

We argued extensively in our *Enterprise Solutions to Poverty* report the need for financial viability. Five years later our experience serves to reiterate the same point. The prime concern of all actors involved in the venture must be the long-term financial viability of the enterprises being assisted. Socially or environmentally sound enterprises that remain permanently dependent on subsidy are not sustainable.

The ability to achieve financial viability and the importance attached to it is critical when we look at new investment opportunities. As we have argued before: "The reasoning is simple. Achieving financial viability is not just about making a profit. Many things happen as pro-poor enterprises become financially viable. First, they rely less and less on relatively scarce aid money, which is a good thing. Secondly, achieving financial viability usually means they can start to grow, thus impacting more poor people directly or through their suppliers. Thirdly, through the ongoing process of innovation and problem-solving that accompanies growing financial viability, they are able to provide more of their customers – poor people – with more appropriate and more affordable goods and services."[43]

We fully acknowledge the fundamental need for upfront grants – or subsidy – to test new solutions. However, going to scale requires a disciplined focus with our partners on how to move away from grants and maximise financial returns through earned income from poor customers. And indeed, where our partners have embraced this concept, we have seen considerable success in being able to leverage capital from other investors with a similar interest in both financial and development returns.

With our partner GroFin, we aimed to develop a financially viable model based on the integrated provision of skills and finance to African start-up and growing enterprises. This approach clearly set us apart from the majority of other organisations who supported SME funds targeting these businesses. We found that others typically either had an investment strategy that was weighted in favour of developmental rather than financial returns or an operational model that was only sustainable through the continued provision of subsidy. GroFin set out to be self-sustaining through being cost-efficient and financially disciplined.

By becoming cost-efficient and financially disciplined GroFin were able to leverage over US$200 million from development finance institutions, international finance institutions and African banks, making it the largest financier of small enterprises in Africa today. To date, every grant dollar that we invested into building GroFin's operations in Africa has leveraged over US$20

The prime concern of all actors involved in the venture must be the long-term financial viability of the enterprises being assisted. Socially or environmentally sound enterprises that remain permanently dependent on subsidy are not sustainable.

43 *Enterprise Solutions to Poverty*, Shell Foundation, 2005.

> There is a critical difference between an investment that takes a business-like approach to achieving a specific objective and a long-term partnership that is designed to exit from subsidy completely, secure earned income from the poor and achieve scale.

in capital from others, and enabled us to end our role as a subsidy provider after six years. Having achieved scale, GroFin can now strengthen further its financial model by increasing the level of management fees payable by investors. Thus a virtuous circle is born whereby financial viability leads to scale, scale allows for leverage and leverage can help secure financial viability.

Similarly, EMBARQ has been able to leverage US$880 million from public and private investors into new Bus Rapid Transit systems based on its financial strength. For example Bloomberg Philanthropies joined SF and Caterpillar Foundation as a new global strategic partner of EMBARQ in January 2010 with a five year commitment of US$30 million. This will allow EMBARQ not only to fund their existing solutions-based approach to urban mobility but also to scale-up their activities. It also allows for relationship leverage by connecting EMBARQ with the other grantees of Bloomberg's US$125 million global road safety initiative (including the World Health Organisation, the World Bank, the Global Road Safety Partnership and Johns Hopkins Bloomberg School of Public Health). EMBARQ will now lead work to measure the air quality, health and road safety impacts of urban mobility projects and build the case for future large-scale investment to achieve these benefits across the transport sector. Nancy Kete recognises the importance of early business-based advice from SF: "We would not have seen such strong appetite from the likes of Bloomberg Philanthropies if it wasn't for our clear business-based model, our robust financials and KPI reporting, all of which were driven by Shell Foundation."

As a result of TBFC having the capacity, track record and secured orders with major retailers, we were able to facilitate a three year loan of US$700,000 from the UK Charity Bank. This is a major step forward for them in that they can now exit subsidy dependence and shift to growth based on support from the financial sector.

Our successful partnerships have demonstrated that scale and sustainability are critically dependent upon financial viability and its associated linkage to securing investment from the financial sector. Demonstrating the acumen to be able to render development solutions commercially viable has also proven critical in establishing the credibility of the solution, the venture and the management team.

Over the past five years we have seen increasing reference in the development sector to the importance of promoting an enterprise-based approach. However, there is a critical difference between an investment that takes a business-like approach to achieving a specific objective and a long-term partnership that is designed to exit from subsidy completely, secure earned income from the poor and achieve scale. This is why we believe the skill set of the development sector should more equitably balance development DNA with business DNA. This hybrid of skills is essential to developing lasting solutions of benefit to the poor.

Lesson Four: Scale is Not Enough

After 10 years we have come to realise that while assisting any one partner to achieve scale and sustainability is a hard but necessary task, it is not enough by itself. No matter how successful pioneers such as GroFin, EMBARQ, The Better Flower Company or Envirofit are, they will never fully solve any one global development challenge. The world is too big, the numbers of poor affected too large and the need for constant innovation too pervasive. To have a real impact on world poverty an even greater ambition is needed.

4

As Pamela Hartigan, Director, Skoll Centre for Social Entrepreneurship argues: "For social entrepreneurs there has come a realisation that one can scale a social venture to huge size and not make a dent in the issue: the central unit of analysis is not the organisation but the *sustainable solution and its underlying business model*."[44] New Philanthropy Capital makes the same point in its analysis: "...to scale-up an approach requires both a good model of working and a sound organisation."[45]

If we return to the Volans[46] "Pathways to Scale" model (see page 19) of change, it is only at stage 4 that the model shifts to the evolution of broader ecosystems of change agents. These involve a growing number of public, private and citizen sector partnerships followed by secondary waves of imitation. As Litovsky clearly states: "Ultimately if anything like a truly sustainable and equitable future is to be achieved entrepreneurial initiatives will need to scale-up further to…system change – typified by broad-based market and societal adoption of new mindsets, models and technologies. Success… will involve the transformation of political priorities, governance process, market rules and cultures." Equally, he points out that getting stuck at the earlier stages does not allow for the catalysis from a market pioneer to market reform.

We have made some tentative steps towards market reform. For example, we are promoting the concept of Growth Finance. We want to capture the integrated and commercially viable provision of skills and finance to small businesses so as to differentiate Growth Finance from recognised asset classes like microfinance and private equity. Growth Finance is a solution to the Missing Middle that has huge opportunity for development, replication and innovation across emerging economies. It also has the potential to create millions of sustainable jobs and livelihood benefits for the poor. In addition to promoting Growth Finance, we were one of the co-founders of the Aspen Institute for Development Entrepreneurs (ANDE). We also helped establish a new venture – Optima – that specifically targets ways to enhance the professional competence of organisations operating in the growth finance sector. However, there is clearly still a long way to go before Growth Finance achieves its potential.

Similarly we are working to promote the role of ethical agents as part of a wider system change to promote fairer trade, and together with other partners we are supporting a global alliance to tackle IAP through the market-based sale of improved cookstoves.[47]

As Kete confirms: "Sometimes when I think about the scale of the impact we have had it is really amazing. When we started I don't think many people thought we would be successful." Kete notes that EMBARQ "now see systems that we stimulated or catalysed in the multiple of millions and in each of those cases we are shortening people's commute by thousands of hours a day – for all kinds of people – but many of whom live close to the minimum wage. This is a large impact in terms of quality of life." Kete concludes that if EMBARQ had "started too modestly and not started at a high scale – which was actually a Shell Foundation decision – I don't think we could have achieved this impact."

We are only starting our efforts to address wider ecosystem change. It will require us to adopt new approaches and new partnerships. Doubtless we will learn more through our successes and failures. But fundamentally we feel that organisations that are close to market and have practical experience of tackling real barriers to growth must be positioned at the heart of any effort to effect wider sector reform.

---

44 *Reflections on the meaning of scale*, by Pamela Hartigan, Alliance magazine, Vol 15, No 2, June 2010.

45 *Scaling up for the Big Society*, Martin Brookes et al, New Philanthropy Capital Perspectives, 28 May 2010.

46 *Pathways to Scale*, Alejandro Litovsky, Volans, 2009, which explores how to accelerate the impact of solutions to major economic, social, environmental and governance challenges, in order to reboot markets, institutions and the economy.

47 The Global Alliance for Clean Cookstoves is a new public-private partnership that aims to save lives, empower women, improve livelihoods, and combat climate change by creating a thriving global market for clean and efficient household cooking solutions. The Alliance's "100 by 20" goal calls for 100 million homes to adopt clean and efficient stoves and fuels by 2020. The Alliance will work with public, private, and non-profit partners to help overcome the market barriers that currently impede the production and use of clean cookstoves in the developing world. See "Strategic Partners: Envirofit" for further information, p 11.

Conclusion

As a relatively young organisation we have been on a steep learning curve. Our journey has allowed us to capture not just the lessons we learned but also to fortify our institutional strength by recording our experience. Indeed, the process of collating the information for and writing this report has helped us create knowledge and a learning platform that we can build upon in future.

Our performance assessment leads us to believe that achieving scale and sustainability is fostered by an ability to:

- Catalyse disruptive change through angel philanthropy
- Build sectoral pioneers that can create new solutions to old problems
- Ensure an exit from subsidy and a transition to earned income

But pioneers that go to scale, while critical to demonstrating that enterprise-based solutions to global development challenges, are on their own never sufficient to resolve such large market failures.

We recognise the long history of thought-leadership, innovation and self-analysis among our peers. While these factors make us wary about offering recommendations, we believe that we have identified three specific challenges where additional focus from all working in the philanthropic sector, could generate tangible systemic change and much greater returns of scale and sustainability:

More Angel Philanthropy

We have been struck by the paucity of foundations and donors willing to provide all-important flexible and long-term subsidy support to start-up and growing for-profit social enterprises.

All too often we have been something of a rarity in our ability to act in this way. Even when such funding is available from others, we have seldom encountered grant-giving that enables an enterprise to build core capacity and establish core operational systems. By contrast, subsidy is often provided at levels insufficient to build core capacity, or in the form of technical assistance where skills are provided by an external consultant rather than by creating internal capacity. Or it is conditioned such that it cannot be used to support essential infrastructure costs (e.g. developing or upgrading IT systems). We believe that more foundations need to be willing to give flexible subsidy support to for-profit organisations to enable them to achieve social change rather than just restrict their giving to not-for-profits.

More foundations need to be willing to give flexible subsidy support to for-profit organisations to enable them to achieve social change rather than just restrict their giving to not-for-profits.

More Syndication with More Impact Investors

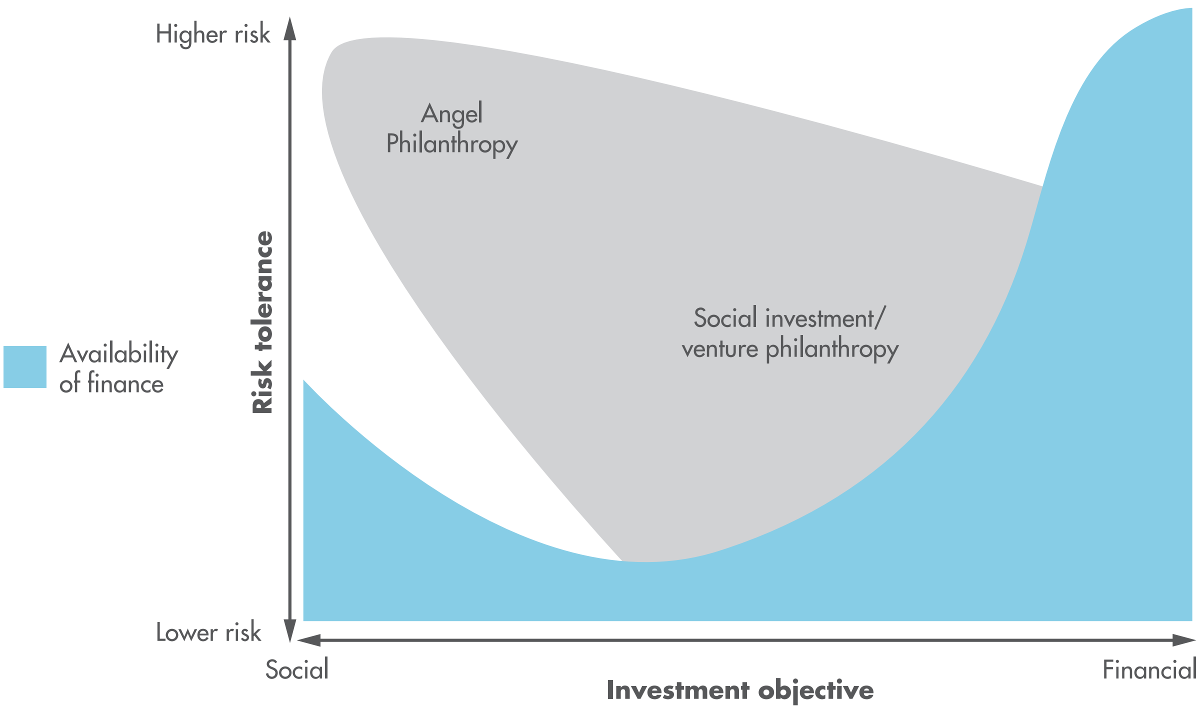
There remains a huge gulf between funders that provide subsidy in the form of grants and those providing commercial finance. We applaud and encourage the growing number of social investors that are willing and able to achieve blended financial and developmental returns. But our own strategic partners have all struggled to secure such second stage social investment on their path towards scale-up and sustainability. Our experience is that there still remains a "valley of death" facing successful pioneers in their search for second stage finance, as we illustrate in Figure 8.

We believe there are new and important opportunities for alliances or syndicates to be established that link angel philanthropists with impact investors, as well as opportunities for greater use of certain social investments (such as partial risk guarantees) that can be deployed by angel philanthropists to leverage greater second stage finance.

More Benchmarking on Performance

The concept for writing this report came from asking the question: "Are we a good, average or poor foundation?" Yet we have found no widely accepted or used performance benchmarking of foundations or for comparing the effectiveness of different programmes with common objectives. Equally we have found very few evaluations by other foundations that report both their successes and failures. While tackling global development challenges is hugely rewarding, we equally know it is not easy and our collective chances of success will increase if we share learning. For our part we stand ready to work with others interested in developing, testing, deploying and reporting such comparative performance metrics.

Figure 8 – The Valley of Death Funding Gap



Adapted from the Said Business School, Oxford University.

Looking to the Future

The Next Ten Years

Our learning to date, and a significant amount of critical strategic thinking that the production of this report has engendered, leads us to adopt the following strategy for the next decade.

- We will **retain** our mission, our enterprise-based approach and our focus on building strategic partnerships for achieving scale and sustainability.
- We will **do more** to incubate, scale-up and spin-off strategic partnerships by:
  - enhancing our networks
  - facilitating dialogue between our partners
  - leveraging added-value from our links to Shell
  - using more non-grant funding as appropriate
  - forming alliances with a few social investors, and
  - allocating time and effort to critical self-analysis and learning.
- We will seek to **continuously improve** our partner selection processes in order to enhance:
  - our (co-)development of new business models
  - our ability to effect wider market reform
  - the transparency with which we report our comparative success
  - our ability to encourage others to be enterprise-based.
- We will avoid exiting too early from a strategic partnership during the critical scale-up phase or spreading our resources too thinly among strategic partners or geographic regions.

Appendix 1: Enterprise-Based Approach

We believe an enterprise-based approach has relevance across all sectors when tackling market failures that are typically the prime cause of many global development challenges. We believe that an enterprise-based approach can be applied not only to for-profit organisations but also to not-for-profits and public sector organisations. Being enterprise-based is about adopting a mindset and process of thinking rather than an expectation of delivering solely financial return in a way typified by most commercial enterprises. When we talk about an enterprise-based approach, we mean addressing what we believe are the prerequisites for achieving scale and sustainability.

Focus: As in business, we believe the starting point is for an organisation to focus on doing a few things well. This translates both to the focus of the Shell Foundation on tackling a few key development challenges, as well as selecting a few strategic partners who then fully focus their skills and resources on tackling specific issues.

Customer Based: We believe it is important to treat the poor as customers and not beneficiaries. This mindset helps focus on delivering products and services that are demand-driven and valued by the real market (i.e. the intended recipient) rather than being supply-led and based on the needs perceived by others (often those who provide funds to the organisation or intermediary). Such a market-based approach enshrines the general principles of Know Your Customer and Customer Value Proposition that are key to understanding needs, as well as customer feedback to ensure products and services are appropriate, affordable and performing to desired standards. It also ensures that constant attention is paid to improving product or service quality, effective marketing and pricing, as well as fostering a need for continual innovation. We find this customer-based approach is just as relevant when working with a for-profit organisation like GroFin to support African small enterprises as it is with working with our not-for-profit partner EMBARQ that helps city authorities in developing countries implement sustainable transport solutions.

Disciplined Implementation: This has many dimensions all related to enhancing performance of the organisation. This includes not just having the right blend of skills, management capability and incentives to achieve performance targets, but also a range of effective systems (e.g. management information systems, IT, training and recruitment, communications, financial management and reporting) that are essential to tracking and enhancing the efficient and effective use of resources. It also means understanding, monitoring and reporting key risks on a regular basis and taking action as appropriate to mitigate these risks.

Performance and Accountability: We have always sought to agree a few (usually three to five) Key Performance Indicators (KPIs) with each of our strategic partners. Core to an enterprise-based approach is selecting KPIs that make sense for the organisation itself to collect in order to measure its own progress towards achieving its goals. Typically KPIs cover both financial and developmental measures that are specific to each organisation. Wherever possible, we try and agree smart ratios that can be tracked over time (e.g. cost per job created, ratio of fixed overhead to service delivery cost, cumulative subsidy per clean cookstove sold). Because they make sense to the organisation, they tend to be tracked and reported on a monthly or bi-monthly basis. They equally serve as shared metrics used by other funders. Performance against agreed KPIs is measured, documented and reported on a regular basis to ensure an accountability mindset from the outset. Equally we believe that performance and accountability is enhanced by organisations developing, implementing and monitoring adherence to a set of business principles that define their ethics and core practices.

Financial Viability: Our definition of an enterprise-based approach enshrines varying types of financial viability. At one end of the spectrum is the concept of commercial viability whereby an organisation generates profit and will no longer require subsidy for growth. Moving along this continuum we look for our partner organisation to eventually become capable of securing sufficient earned income to meet ongoing operational costs (though without repaying start-up capital). Finally we might support organisations whose long-term operation and scale-up depends on securing significant and lasting subsidies, grants or deal flow. This, however, is our least favourite end of the spectrum to work in and the persistence of subsidy would have to be offset by considerable scale effects. These could include the amount of leverage that our subsidy could secure from other significant donors. Whether grant-based or revenue-based, deployment of income must be as cost-efficient and effective as possible, using agreed indicators of evaluation.

Appendix 2: Performance Assessment Methodology

We found no widely used or accepted criteria for assessing the impact of grants or performance with respect to achieving scale and sustainability. As such we devised our own criteria that we believe are both simple to use and do not risk over-reporting success. All completed grants were classified using a traffic light system (with scoring agreed whenever possible with our partners – see page 6).

Green	Achieved scale/sustainability
Orange	Achieved intended project objectives but no evidence of scale
Red	Failed to meet intended project objectives

Defining Scale

We choose to define scale as meaning the delivery of cost-efficient solutions that benefit large numbers of people in multiple locations in ways that are financially viable. Grants scored as **green** were judged to have achieved scale and sustainability if they met the following criteria:

- Large-scale development outcomes met/exceeded (measurable).
- Leverage met/exceeded SF grant contribution (measurable).
- Earned income being derived from intended market (measurable).
- Multiple country and/or regional operations (measurable).
- Management team has competence to execute the business (subjective).

Defining Failure

We have deliberately chosen not to name the partners involved in projects we judged to have failed to meet their intended objectives. This is not because we believe our judgement may be contested, but because we recognise that we must accept varying degrees of responsibility for such outcomes and because our experience was often based on a single grant relationship with a partner.

For all those grants that were scored as **red**, we found in hindsight that we could classify reasons for failure in three main ways:

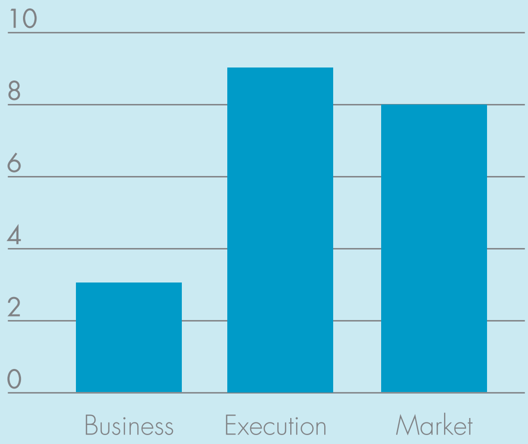
- **Execution:** Partner lacked competence/ability to manage the project. For example, several partners lacked a combination of technical skills, management resources, operational systems and financial controls essential for the effective implementation of pro-poor energy projects in Africa.
- **Market:** No observable market/customer demand for product/service offered. For example, we helped create a new business to unlock the flow of carbon credits to projects in

Africa, but subsequently found a lack of local capacity to develop and assess such projects as well as a lack of interest by banks – triggered by the global financial crisis – to invest in such an enterprise.

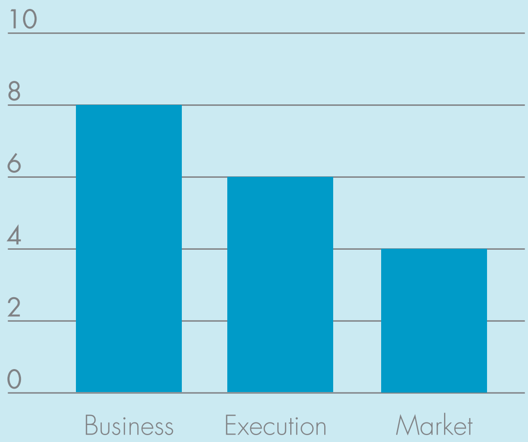
- **Business:** No evidence for financial viability without permanent subsidy. For example, several partners in Asia were distributing pro-poor energy products and services at prices well below production costs and were either unwilling or unable to shift from a subsidy mindset or focus their efforts on where they could best contribute to the value chain.

The following figures depict the numbers of projects whose failure was attributed to one of these three reasons in each of our operational phases.

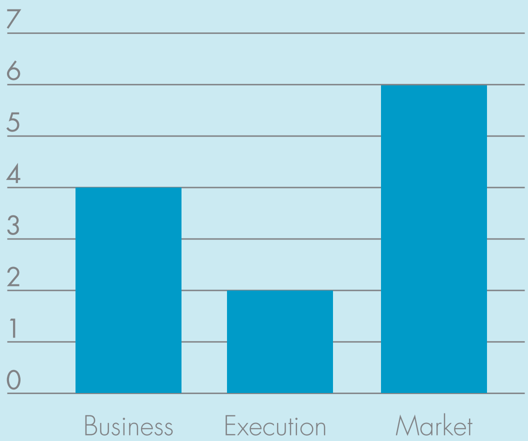
Reasons for Failure
Phase 1: 2000-2002



Reasons for Failure
Phase 2: 2003-2005



Reasons for Failure
Phase 3: 2006-2008



Appendix 3: Overview of Grants

Shell Foundation has committed total funds of US$111.9 million since our inception in June 2000 to June 2010. Of these, US$93.9 million were awarded as grants, the remaining US$18 million relates to amounts committed but not yet awarded as grants to EMBARQ (US$3 million) and amounts committed as programme related investment under ASPIRE (US$15 million).

We have chosen to report only on the performance of initiatives funded by SF over the period from 2000 to end 2008, as this allows us to objectively assess the realised impact of completed grants as opposed to those still ongoing.

The total committed by SF over the period from 2000 to end 2008 was US$80.2 million. Of the 296 grants awarded by SF during this period, 221 grants – with a total value of US$78 million – aimed from the outset to achieve scale and sustainability (the other 75 grants largely representing support to one-off initiatives or specific time-bound activities such as conferences and workshops). We focus our performance assessment solely on those grants designed from the outset to achieve scale and sustainability during the period 2000 to end 2008.

Operating Strategies

Over the past decade we have adopted different operating strategies during three discernible phases:

2000-2002: Our inception phase (Phase 1) during which an open Request for Proposals (RFP) process was used as the main way of selecting project proposals from NGOs of less than US$300,000 and three years duration.

2003-2005: The period (Phase 2) during which we shifted to piloting a number of strategic partnerships, either as the sole investor or together with other investors.

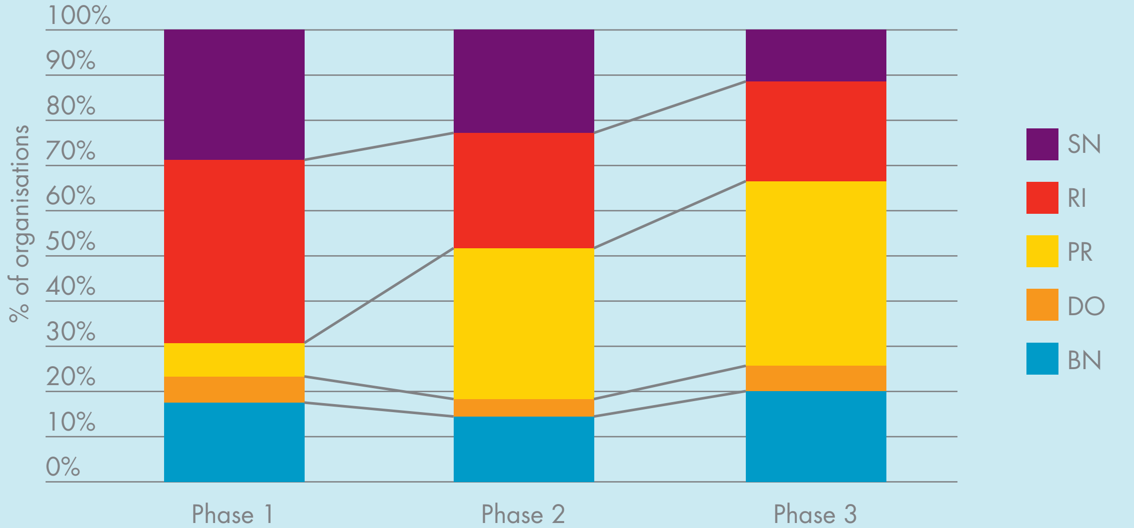
2006 to date: The period (Phase 3) during which we focused our resources on the scale-up of a few strategic partnerships.

We choose to define scale as meaning the delivery of cost-efficient solutions that benefit large numbers of people in multiple locations in ways that are financially viable

Overview of SF Investments

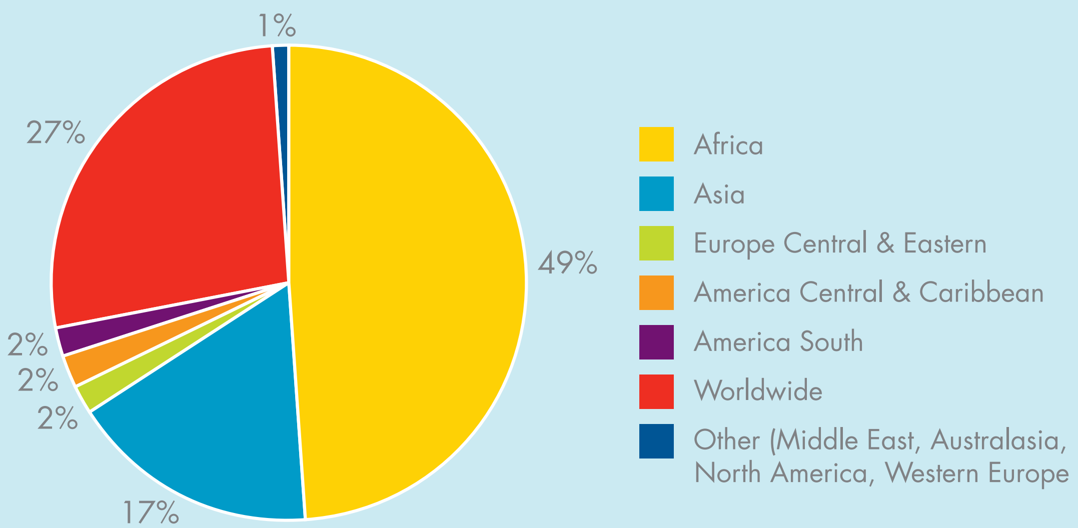
The following information provides an overview of our commitments during the reporting period.

Mix of organisation type by phase



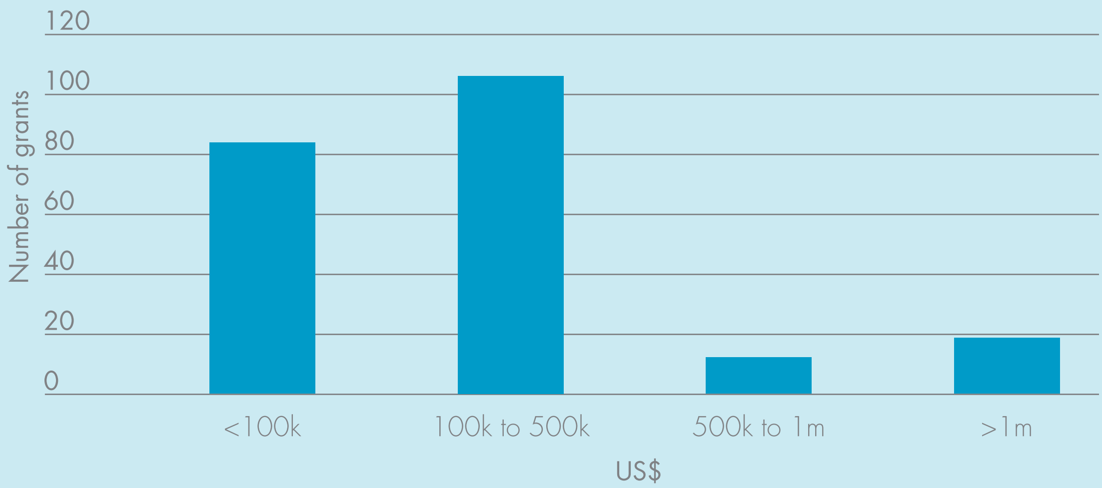
SN = Local NGO; RI = Research Institute; PR = Private Company; DO = Development Organisation; BN = International NGO

Geographical split of grants 2000–2008*



*Includes initiatives that were not specifically intended to go to scale.

Grant amounts*



*Includes initiatives that were not specifically intended to go to scale.

SF Programme Focus

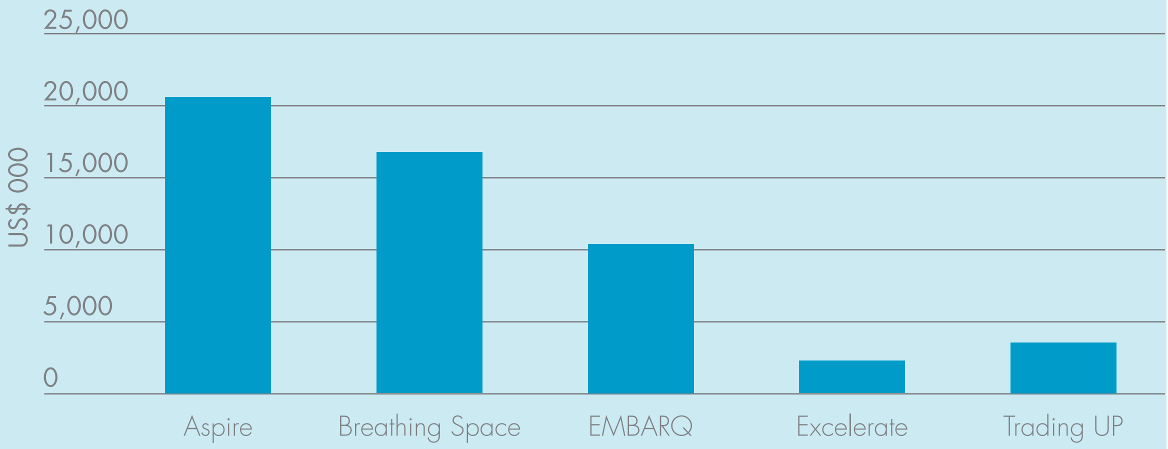
When SF was launched in 2000 it had three main broad programmes – Sustainable Energy, Sustainable Communities and Youth Enterprise. By 2004, our focus had evolved to tackle five different global development challenges through five branded programmes:

- **Aspire** supports the start-up and growth of viable small and medium sized enterprises (SMEs) in emerging economies as a means of enhancing sustainable employment and livelihoods. While in OECD countries SMEs typically account for over half of annual contributions to GDP and nearly two thirds of all employment, in Africa the contribution by SMEs to national GDP can be as low as 10%. SMEs – which we define as being those viable start-up and growing businesses having less than 100 employees – frequently require access to capital in the range of US$100,000 to US$1 million (in local currency). Investment of this size is too large for microfinance and perceived as too risky for banks (due to lack of collateral, track record or audited financials). This market failure is commonly referred to as the Missing Middle.

- **Breathing Space** aims to achieve a significant long-term reduction in the incidence of Indoor Air Pollution (IAP) at the global level through the market-based development, production and sale of high quality, durable and affordable improved cookstoves. IAP is the toxic smoke created by cooking on open fires and inefficient stoves burning wood, dung, coal, straw and charcoal in poorly ventilated homes. IAP impacts some three billion people and is estimated to kill 1.5 million people each year in developing countries, mostly as victims of childhood pneumonia. It is widely accepted that the best method for tackling IAP is for people to use improved cookstoves which reduce both toxic emissions and fuel use.

- **EMBARQ** aims to improve the quality of life of people living and working in mega-cities in developing countries through the implementation of sustainable solutions to urban mobility. Over the past two decades, the urban population of the developing world has grown by an average of three million people per week, with the result that more than half the world's population live in cities. By 2050 it is predicted that 70% of the world's population (6.4 billion) will be urban, with 5.3 billion in developing countries.

Grants given to core programmes*



*Excludes initiatives that were not specifically intended to go to scale.

- **Trading UP** facilitates pro-poor ethical trade by building sustainable supply chains that are both good for business and help to eradicate poverty. Despite growing consumer awareness in the concept of fair trade, producers of sustainable products and commodities from developing countries lack access to the skills, capital and markets that enable them to gain access to value chains sustainable jobs.
- **Excelerate** aims to enhance access by the poor to modern energy services in ways that are financially viable and scaleable. There are significant gaps in many developing countries between the growing demand for modern energy services – especially from rural and peri-urban communities that lack access to the electricity grid – and the supply of appropriate technology and enterprise capable of delivering these at reliable and affordable prices. For example over 500 million people in India – representing 30% of the world's estimated 1.6 billion "energy poor" – have no access to electricity.

672408–CSL–09/2010