Social Finance and Social Enterprises: A New Frontier for Development in Indonesia

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Abstract

The number of social finances and social enterprises are steadily growing in Indonesia. However, there is yet to be a comprehensive research in this context. The objective of this study is to explore and identify the unique challenges of social investment in Indonesia. There are three key players in social investment ecosystem in Indonesia. Social enterprises, which aim to solve social or environmental problems, are mostly at their early stage and not investment ready. Meanwhile, many investors, with or without intention to invest for social mission, are not willing to fund early-stage enterprises. There are also challenges or false perceptions from traditional financial institutions in giving external funding to social enterprises. Enablers act as catalysts for the growth of social enterprises; however, their presence in Indonesia received an equivocal review, as many of them are lacking instruments as a social enterprise enabler. Blended finance is explored to be the solution to the unmet demand and supply of funding. There are two tools to implement blended finance model. With direct funding scheme, investors are given guarantees in exchange for the higher risks to investing in seed- and growth-stage social enterprises. Alternatively, support mechanisms acknowledge and address different issues in every lifecycle through various building capacity and programs.

Keywords: Social Enterprises, Impact Investment, Social Finance, Blended Finance, Sustainable Development Goals (SDGs), Indonesian Development

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I. Introduction

Social finance encompassed the deployment of financial resources principally for social and environmental returns, and in some cases, an economic return (Hangl, 2014). Although the idea has been lingering for over a century (European Commission, 2016), the concrete concept of social finance as a development tool has been relatively newly understood in the international banking and finance sector (Benedikter, 2011; Lehner et al., 2014). Particularly in Indonesia, social finance gained a lot of support and attention after the economic turmoil in 2009 and after the push from government and foundations to provide more sustainable financing for social initiatives (Angin, 2016). The number of active organization in social financing, therefore, grew from only a handful to double-digit, coming from both Indonesia and overseas.

Nevertheless, the research on this area is scarce, particularly in high-impact countries such as Indonesia. The currently available study explores the topic of social finance from the perspective of general micro-market; how specific mechanism can best fund social enterprises (Cooch and Kramer, 2006; Griffith, 2006; Emerson, 2006). While these studies provide a fresh insight on the area, the mechanisms are not easily applied to an individual country without first knowing the outlook.

The pressing need to understand the landscape of social finance in Indonesia is also aggravated due to the growing number of social enterprises in Indonesia. There are more than 300 social enterprises from different background, maturity level, and operation in different sectors. The identified catalysts for the increasing number are the growing interest of younger generations, as well as returning Indonesians who have studied abroad (Angin, 2016). The rising demand side is also helped by the existence of some startup accelerators programs and active government programs.

This research addresses the current literature gap in Indonesian social finance and social enterprise. To date, there is yet have been any robust collection of data, no recorded figure on existing ecosystem players, no information on what's currently going on, and what are current main challenges. The study was initiated by the UNDP (United Nations Development Programme), through its works with Otoritas Jasa Keuangan (OJK), Badan Perencanaan Pembangunan Nasional (Bappenas), and Kementerian Koordinator Bidang Perekonomian (Kemenko), where they wanted to understand better the social finance landscape and potentially start to take actions to play an active role in the Indonesian social finance scene. It is challenging yet imperative to understand what is the best social finance tool to use to address the needs.

Against this background, the purpose of this research is to answer the overarching question: "What is the latest outlook of social finance activities in Indonesia?". More specifically, the research questions driving this study are as follows:

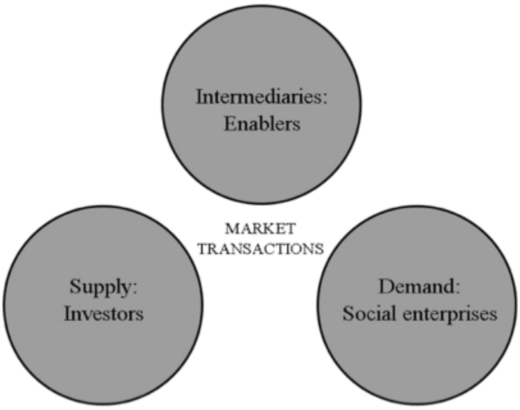
1. Who are the key players in the social finance landscape in Indonesia?
2. What is the current state of each of the Indonesia's social finance key players?
3. What are the challenges faced by each of the stakeholders in achieving their objectives?

The rest of the paper is outlined as follows: the next chapter provides a context for understanding the role of respective stakeholders in the social finance and social enterprise. Chapter 3 describes the methodology. Chapter 4 discusses the trends, further exposing current problems challenges. Lastly, drawing from previous two chapters, Chapter 5 will conclude the research with suggestions and best approach for both public and private sector to address the issues.

II. Literature Review

To holistically framing the landscape of social finance, one must set out the key players within the rudimentary market framework: the demand side, the supply side, and the intermediaries/enablers.

Figure 1. *The key stakeholders in social finance landscape*



2.1 Demand Side: Social enterprises

Social entrepreneurship is a practice that amalgamates economic and social value creation in its mission (Mair and Marti, 2006). While there is a varying definition of a social enterprise; it can be shortly defined as an 'entrepreneurial activity with an embedded social purpose' (Austin et al., 2006). They are financially sustainable businesses that are intentionally solving a social or environmental problem awhile having an entrepreneurial mindset to grow their business and impact.

2.2 Supply Side: Investors

Investors are defined as being either natural persons (individuals) or legal persons (companies/businesses) that injects capital or money into financial schemes with an expectation of economic return (Nikièma, 2012). An investor is considered as a socially responsible investor if he/she integrates the financial consideration with non-financial aspects, including personal values, societal demands, and environmental concerns. (Scholtens, 2006). Several types of investor fall into this category, including but not limited to non-profit organization, foundation, and impact investors. However, other investors who do not have a primary interest in making a social change can also invest in an enterprise with a social mission.

2.3 Intermediaries: Enablers

Social enterprises often require the assistance from intermediary organizations to grow and become investment ready (Dey, Schneider, Maier, 2016). In other words, intermediaries or enablers in social entrepreneurship context are agents that act as catalysts to support the social enterprise ecosystem. These intermediaries can be either a financial or non-financial intermediaries. A financial intermediary organization links the capital providers with social investment opportunities, while a non-financial one influences a more significant area of the social enterprise through capacity building, developing the market framework, and collaboration.

III. Methodology

To give a perspective to the topic, the paper dissects the social finance ecosystem in a broad approach, by looking at different layers of the ecosystem: the buy-side (investor), sale-side (social enterprise) and support-side (enablers) which comprise the social finance ecosystem.

3.1 Data Collection

Data on social entrepreneurs was collected in a month period from November 15th, 2016 to December 12th, 2016 via surveys, individual interviews and focus group discussions. The research focused its analysis on social enterprises in the process of raising funds that raised funds or that failed in their fundraising efforts.

Desk research identified 324 social enterprises, 108 investors (including 12 impact investors), and 62 enablers as potential research participants. Surveys and initiation to participate in interviews and discussions were sent, resulting in 26 responses for social enterprises, 53 investors (including four impact investors), and 11 enablers. The analysis was conducted based on 90 valid responses.

3.2 Measures

Aligned with the research questions, there are several qualitative measures in analyzing the key stakeholders.

Table 1. *Measures of the Qualitative Research*

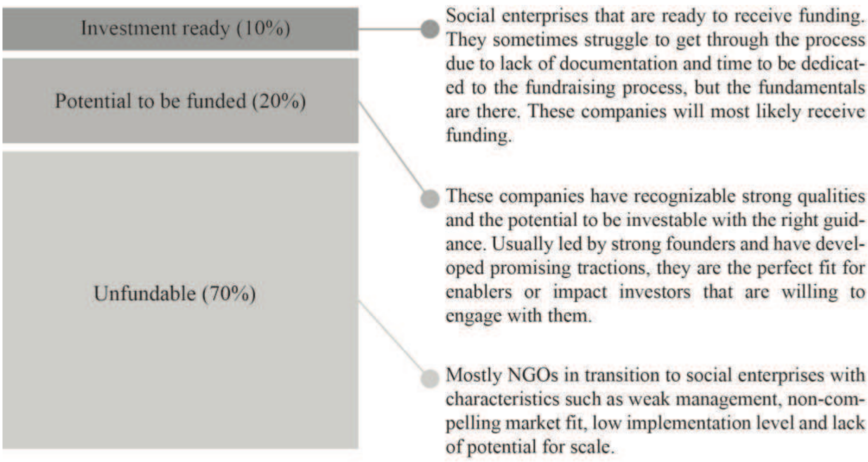
Stakeholders	Measures
Demand-side: Social enterprises	• Enterprise sector • State of investment readiness • Quality of the founders
Supply-side: Investors	• Taxonomy of investors • Investment instruments • Ticket size of investment • Challenges and limitations
Intermediaries: Enablers	• State of enablers in Indonesia • Effectiveness • Challenges and limitations

IV. Results and Discussion

4.1 Demand Side: Social Entrepreneurship in Indonesia

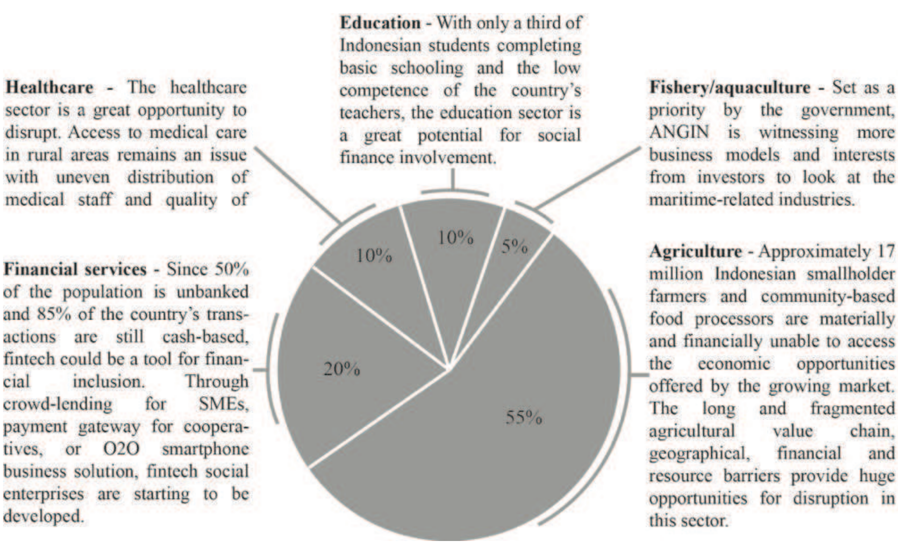
From the analysis, the authors categorize Indonesia's social enterprises into three states of investment readiness:

Figure 2. *Categories of social enterprises' investment readiness*



As shown in Figure 2, the issues on the number of social enterprises that have potential and ready to be funded need to be addressed, because the acceleration of social investment depends heavily on the investment readiness of the social enterprises (Gregory et al., 2012). Furthermore, around 70% of the social enterprises in Indonesia are in pre-seed and seed-stage and around 80% of the social enterprises are five years old or younger as most of them were founded following the emergence of the startup trend in 2012. On average, they would require funding from IDR 130 million up to approximately IDR 1.3 billion. Most of these enterprises are still trying to validate their business model and fine-tuning the right product-market fit, and have yet to plan for expansion that will require a larger amount of capital. On another aspect, Figure 3 represents the areas of opportunity for impact (relating to UNDP's Social Development Goals) and social finance's proof of concept. In addition, many of the sectors are heavily shaped by geographic and demographic, as well as infrastructure profile in Indonesia.

Figure 3. *Indonesian Social Enterprise's Sector Domination*



This research also identified some key trends in Indonesian social enterprise. Firstly, there is an **incline in numbers of technology-based social enterprises**, compared to 2014. Secondly, several social enterprises that successfully raised capital have grown with the **support of larger corporations**. The role of corporations had been key in providing early funding, key operational expertise and the human resources to early-stage ventures. Regarding gender approach, 25% of the social enterprises encountered are led by **female entrepreneurs**.

From the founder's side, there are three types of successful Indonesian social enterprises that have received external funding. The first type is associated with educational background. Many of successful entrepreneurs were educated abroad and decided to bring home the learning curve and set up their own venture in observance of the social issue in Indonesia. Most of them have a certain form of safety nets, such as the familial support or professional career. These groups attract investors not only because of their strong education pedigrees, but also their family or professional associations. The second type is social enterprises owned by foreign nationals. Most of them have a development background such as working with Peace Corps or UN Agencies. The decision to live in Indonesia is driven by their social mission and personal willingness to create change in the community. As a result of being an expatriate with previous work in development space, most of them have the right connections to foreign investors, media and other networks of support that may be inaccessible to Indonesians. The last type is called 'hyperlocal'; Indonesians who were educated in Indonesia, observed social issues in their own community, and build mostly local solution. They may have challenges at first in building their credentials with foreign investors and thus, most of the investment come from local investors.

4.2 Supply side: investors in Indonesia

4.2.1 Types of Investors

There are various types of investors identified in Indonesia' social finance landscape:

Friends and family financing is commonly used by social entrepreneurs as their first source of capital. It is usually the easiest to obtain as it involves very light documentation (sometimes social entrepreneurs do not even record this investment accurately on their balance sheet) and it often takes less than a month to close this funding. From the analysis, friends and family rounds are usually in the IDR 65,000 to IDR 325 million range, rarely going over IDR 390 million.

Bootstrapping/internal funding is not an external funding source per se; some social entrepreneurs opt to focus on revenue generation and to find a shorter path to break-even to grow their company organically. This decision is usually taken after an extended period of unsuccessful fundraising process, or based on the desire to avoid dilution and to not have any external parties to report to.

Crowdfunding is a growing topic in Indonesia. Crowd or Peer-to-Peer (P2P) platform allows social enterprises to raise capital from a large crowd of retail individual investors with the platform serving as the facilitator of the transaction. The capital raised could be structured as donation, equity or debt. Through this mechanism, social enterprises would have access to capital below IDR 260 million. However, the regulation on peer-to-peer licensing has yet to be fully clarified by the OJK and thus, it is still considered a grey zone.

Angel investors are individuals with disposable capital and the intention to mentor and invest in early-stage companies. They can act individually or jointly with other angel investors to form a network or a group, thus mutualizing resources and expertise. The angel investors have the decision power to invest (different from being a Limited Partner with a Venture Capital), and their investment decisions are usually based on a combination of rationality and a sense of passion. Typical ticket size in Indonesia would be IDR 650 million, but angel investors are flexible by nature and would be able to start funding social enterprises with a ticket size as low as IDR 65 million.

While not used by many social entrepreneurs, the government is running several initiatives aiming to finance SMEs (Small and Medium Sized Enterprises) which most social enterprises are categorized into. The range of funds distributed per organization varies but can be up to IDR 5 million for micro businesses, IDR 50 million for small businesses, and IDR 100 million for medium enterprises and cooperatives. Repayment period is between five to eight years. The main requirements for prospective recipients are: (1) The organization must have been running for at least two years, (2) It should have legal entity, and (3) It should have profitable for at least two years.

A **venture capital** invests funds in early-stage companies on behalf of the investors. In general, a VC consists of two main components: Limited Partner (LP) and General Partner (GP). LPs are the fund investors in the VC funds, while GPs consists of a partner(s), principal(s), associate(s) and an analyst team. While VC firms are not tied to financing social enterprises and do not have the primary intention of generating impact (double or triple bottom line), some traditional VCs play a significant role in funding early-stage impactful businesses. They take risk in investing smaller ticket size (~IDR 650 million to IDR 2.95 billion) in social enterprises with a low traction level and business models that still need to be proven.

Impact investor is engaged in investments that are being made into companies, organizations, and funds with the intention to generate social and environmental impact along with a compelling financial return. There are two types of impact investors: equity-focused and debt-focused with an appetite to do equity investments.

Banks are financial institutions licensed by the Bank Indonesia (the Indonesian central bank) to receive deposits and issue loans. Banks may also provide financial services, such as stock trading, wealth management and currency exchange. There are two types of banks: commercial/retail banks and investment banks. Most of the interviewed banks do not have exposure to social enterprises. They lack understanding of the concept and do not have any special financial products for social enterprises. Only companies with collaterals, mainly fixed assets, are proposed loans. The company would be able to offer collateral to the bank and thus would be able to secure a loan between 10% to 15% p.a. interest rate.

International multilateral organizations such as Asian Development Bank (ADB), International Finance Corporation (IFC), and the World Economic Forum (WEF) are playing a role in supporting social enterprises at a later stage and inclusive businesses. They are directly investing in social enterprises or are providing capital to existing funds through their funds activities.

4.2.2 Social finance instrument in Indonesia

Various financial instrument options are available to social entrepreneurs in Indonesia, depending on their type of proceeds, stage of the company, profitability and legal incorporation. Most social entrepreneurs are not savvy with or even aware of the various financing structures available to them. Below are the most common instruments encountered in Indonesia from the lowest to highest return expectations.

4.2.2.1 Grant

Traditional donations are commonly considered as a gift, as it does not involve a counterpart such as an interest or shares, given by individuals or legal entities to organizations with a social or environmental mission. Most Indonesian social enterprises receive the donation through their legal entity (i.e. PT) when the donor can disburse the donation to such a legal entity or through a foundation (seen as the ideal recipient of donation for most donors). Donation in Indonesia is broadly available to social enterprises through social enterprise competitions and awards in the form of cash or in kind (e.g. equipment, hours of services).

Venture philanthropy is a hybrid between traditional grant-making and venture capital's best practices. It finances social enterprises through a donation, but it is treated as a venture capital investment both in terms of the selection process, proceeds, reporting, objectives and hands-on support such as capacity building attached to the funding. The grant would fund high-risk social enterprises' early operations, typically made together with an impact investment. It is meant to prevent the entrepreneurs from having to source the fund for its costly operational expansion from its balance sheets in a market with various frictions.

4.2.2.2 Debt

A collateralized loan is a loan in which the borrower has pledged some of its assets (e.g. land, equipment, buildings) to get the debt line issued. Collateral serves as a guarantee in case of non-repayment of the installments and interest as stated in the loan agreement. This is the most common instrument provided by commercial banks and impact investors. Early-stage social enterprises usually obtain a loan at 10-15% p.a.

A non-collateralized loan is the riskiest type of loan for the lender as it is not guaranteed by any assets, leaving the borrower's signature and law enforcement options as the only securities for loan repayment. This type of loan typically has higher interest rates than collateralized loan in consideration of the risk, usually above 15% p.a.

Trade financing is a short-term loan financing trade or export transaction. In a broad definition, trade financing includes lending facilities, letter of credit issuance, export factoring, and export credits. It usually involves a triangulation between the buyer, seller and the investor.

While a traditional loan involves a negotiated fixed coupon interest rate as well as fixed installment periods and maturity, **revenue share loan** is proportioned to the performance of the company. The interest is a variable of the company's future metrics (revenue, profit or even net cash flow). It is still technically a loan, but there are no fixed payments, no set time for repayment, and no set interest rate. The investor and the company share both the upside and the downside embedded in the transaction. This is typically the type of financing considered by impact investors when equity investment is not feasible, and the expected upside justifies a revenue share. Sharia-banking imposes this type of risk-shared scheme.

Account receivable/invoice financing is a means to finance the time that a company needs to collect payments from customers and the time required to pay its suppliers. Typically, modern retailers (such as Ranch Market or Kem-Chicks) will pay within 60 days while a social enterprise must pay its supplying smallholder farmers upfront at delivery of the supply (could even be ahead of the harvest). It is a short-term debt financing that takes accounts receivables (invoices) as collateral. This type of financing is gaining popularity among the Indonesian technology peer-to-peer lending platforms. Online financial technology platforms such as Investree, Modalku, Kredivest are offering account receivable financing to SMEs.

4.2.2.3 Grant Equity/Quasi Equity

A **convertible note (CN)** is a form of debt that can be converted into equity at a discount (~5-20% in Indonesia), and the conversion is typically triggered by a future financing rounds (called a qualified financing). In Indonesia, most of the investments by VC firm in the technology industry and foreign-based investors are executed in the form of a CN for two main reasons: 1) it is too early for the company to be valued, so a CN is used to bypass/postpone the valuation process, 2) the investor is foreign-based and will not be able to inject equity into the company directly. A CN allows the investor to carry out investment while avoiding the PMA structure (which is usually impossible for ticket size below IDR 6.5 billion).

An **equity** investment is a means of financing that takes shares/ownership in exchange for the capital invested. The number of shares taken will be based on a valuation agreed upon with the entrepreneur. The equity rounds are usually labelled from pre-seed to Series A/B/C, depending on the stage of the company's ticket size and the use of proceeds. A typical seed equity investment in Indonesia will finance the early go-to-market expansion of a company and will amount between IDR 600 million and IDR 6.5 billion for 10-30% ownership of the company. This is the tool usually used by venture capitals, impact investors and angel investors as it provides the potential financial gain to balance the risk of the investment.

4.2.3 A Focus on Impact Investing

There are four kinds of impact investors operation implementation in Indonesia identified: fully foreign-based who are operating remotely from overseas, foreign-based with a local partner or team, purely domestic-based, and foreign-based but pulling out the operations from Indonesia. Having been underestimated as a potential economic force among its more well-known Asian peers in the past, Indonesia is deemed by the investors ANGIN interviewed as one of the strongest potential markets for social finance. This is driven by the size of the demography, increasing internet/mobile penetration and agrarian/maritime potential, among other factors. Impact investors remain confident in the Indonesian economic fundamentals and ANGIN sees more players are willing to engage resources in the country.

Between 2014 and 2016, the number of identified active impact investors in the country has not increased significantly and remains at an estimated number of 30 investors. Some investors have started to invest and several ceased operations in Indonesia. Currently, the total AUM is difficult to assess as organizations rarely report their entire AUM. ANGIN estimates that IDR 265 billion of impact investment capital has been invested over the last two years.

The research identifies 25 **new impact investors looking for prospects in Indonesia**. Some of them are actively looking to hire a full-time investment manager or country head, while others are currently in due diligence on several deals, inferring that they will become active in 2017.

Between 2014 and 2016, at least four **impact investors left Indonesia** (i.e. withdrew the local staff and ceased investment). The most common reasons were the lack of investable pipeline fitting their investment mandate, geographical focus on other regions, the lack of capital to continue investing, and internal governance issues.

There is a **silent but dynamic activity** of the trade finance impact investors: Several impact investors are active in funding the trade financing needs of social enterprises. As an example, Root Capital claimed to have disbursed several million dollars in over a portfolio of seven companies, mostly coffee businesses or cooperatives. Similarly, ResponsAbility has worked with several organizations such as Big Tree Farms. Except for direct investments in equity, these investments do not get any exposure and are not published by either the companies or the investors. ANGIN anticipates for several agriculture-related businesses in their growth stage to export.

From our research, Indonesia **still lacks domestic capital providers**. Most of the capital providers identified have their investment arm (i.e. the actual fund) abroad.

Only Unitus Impact seems to have a small pool of capital incorporated in Indonesia aside from their largest fund based overseas. ANGIN, YCAB Ventures and Kinara are among the only investment structures operating with funds from Indonesia.

4.2.4 Deal Transactions

While the Indonesian social finance scene has grown in terms of exposure and media attention, **the authors are yet to see a clear proof of concept that more funding is being deployed**. In 2014 and 2015, impact investors in Indonesia made around 15 new investments although the total amount is difficult to measure, with a rough estimation of IDR 260 billion. This amount is below the regular technology VC space which brought IDR 11.2 trillion of investment in more than 60 companies in 2015, which is dominated by e-commerce and consumer internet companies.

The analysis estimates that the ticket size of 60% of the transactions (in number) were done in the IDR 1.3 billion to IDR 6.5 billion range, 35% in the IDR 13 billion to IDR 26 billion range, and 5% beyond IDR 26 billion. **Equity and trade financing as the commonly used financial instrument**. From our research, equity represents 30% of the transactions, followed by quasi equity at 30%, debt at 30%, and other types of investments at 10%.

4.2.5 Common Barriers to social invest in indonesia

The legal environment is seen as a barrier to investing, and there is a low understanding of how to invest in Indonesia. From our interview with impact investors, mostly foreign-based ones, very few managers have a full understanding of the legal framework to disburse capital in Indonesia, from issuing a loan to injecting equity. Their market prospecting time has been focused on building a pipeline of companies, and the legal side has been postponed to later stages when the actual transaction occurs (learning by doing). The lack of comprehensive platform and access to reliable legal/notary services were among the issues pointed out.

There is a **lack of the quality pipeline of investable companies**: 80% of the impact investors interviewed acknowledge the lack of the quality pipeline. Some of the common gaps mentioned: 1) quality of the solution/less innovation in the business model versus other regions (80%), 2) low potential for scalability (70%), 3) low level of tractions validating the model (60%), 4) low IRR/exit expectation (40%), and 5) lack of documentation readiness (e.g. financials, contracts) (35%).

Some social entrepreneurs with minimum business background face **challenges in bookkeeping and financial projections**, which are critical for fundraising. This is for companies that provide debt instruments to social entrepreneurs. Debt requires clear four-to- five-year projections on the three (3) fundamental financial documents: Profit and Loss, Balance Sheet and Cash Flow. Most of the social entrepreneurs are not able to comply with this exercise and impact investors do not have the internal resources to support the pipeline in doing so.

4.3 Intermediaries/enablers

In a relatively nascent ecosystem, social enterprise enablers have aimed to fill the funding and support gaps between investors and social enterprises in Indonesia. Regarding capacity building, the enablers target early-stage companies, typically in their first to the third year of operation. They provide different sources of support such as business canvas preparation, monthly mentoring, pitch deck presentation or access to the network. Enablers are aiming to address the “pioneer gap”, referring to the frictions borne by companies pioneering new implementation and business models targeting social or environmental impact. This gap usually occurs before the companies are ready to be qualified for impact investors (transitioning to the growth stage).

The research sees a growing trend of social enterprise enablers. Social enterprise enablers have been around for several years in Indonesia with Ashoka being the first one to enter in 1983 before the concept of social entrepreneurship was even popularized. Ashoka is a network of global social entrepreneurs that provides financial, professional and network support to social enterprises. In its 33 years of activities in Indonesia, Ashoka has selected 180 social entrepreneurs such as Ashoka Fellows — social enterprises that aim to provide innovative solutions to social problems and potential impact on the society.

Meanwhile, the growth in technology startups and venture capital since 2012 has coincided with the emergence of more enablers supporting the social enterprise ecosystem. In 2012, LGT VP entered Indonesia in partnership with GEPI (Global Entrepreneurship Program Indonesia) to launch its Smiling World Accelerator Program (SWAP) dedicated to early-stage social enterprises. This program aimed to help early-stage enterprises develop and scale up by providing financial, network and mentorship support. LGT VP made its first investment in Indonesia to Krakakoa in 2015. The investment was in the form of a 3-year loan, used to finance processing equipment that would help improve workflow. Krakakoa also received support in the form of network and mentorship from LGT VP's ICats Accelerator and Investment Manager for Indonesia.

In 2014, UnLtd Indonesia launched another accelerator program dedicated to social enterprises. Supported by the Rockefeller Foundation, UnLtd is now operating its fifth cohort of incubation. One of the last initiatives in 2016 is the Kinara impact accelerator that has selected ten companies working in the field of food security and agriculture for a three-month curriculum program bringing them to a better investment readiness.

The research identified that 62 enablers had been running programs in Indonesia throughout 2016. Non-monetary type of support increased by more than 300% compared to 2015. Last year has brought in more varying schemes of enablers, compared to the early 2010s where social enterprise enablers consisted only of workshop and support groups.

4.3.1 Challenges and Limitations

Although the quality of certain enablers has improved regarding selection process and curriculum, as well as providing wider access to grants funded from competition and awards, improvements are still needed to be made based on below key findings.

Enablers could be a distraction for social entrepreneurs: A couple of companies encountered still rely on these donations to cover their early-stage activities, while this should be done from market-based streams of revenue. Several companies are spending a significant amount of time applying to capacity building programs without assessing whether the programs are relevant to their needs and business.

Lack of sector-specific focus enablers: Most of the enablers that are dedicated to social enterprises are sector/industry agnostic and do not customize their capacity building curriculum to the industry in which the social enterprises are operating in. In most programs, the only segmentation is done based on the stage of the companies and the maturity of the operations. Enablers lack the specialization and expertise in their domains. On the technology side, some enablers have managed to propose laser-focused on verticals.

Lack of mentors with the right expertise: Most of the enablers are limited regarding access to a pool of industry veterans and experts. Most of the human resources used to nurture the social enterprises come from the NGO space (low experience in running businesses) or are of generalist profiles. The mentors operate on a pro bono basis, which also limits the time involvement.

Limited connections to social finance: Most of the enablers are not integrated with an investment arm and still rely on pitching session and investor forum to bridge incubates/accelerates with social financiers. Most of the enablers involve the investors too late in their programs.

Lack of impact Metrics: Most of the enablers measure the operational (e.g. a number of teams, outlets) and financial performance (e.g. GMV, Revenue, EBIT, Net Profit) of their incubatees, but none of them collects social performance and impact evaluation data beyond the information provided by the companies. There is no third- party assessment as such resource is not available in Indonesia.

Lack of KPI and difficulty to measure the added value of the enablers: Most of the enablers interviewed do not understand the endgame of their capacity building. There is no research available to help understand the impact of the accelerators by, for example, matching a comparable group of social enterprises that do not participate in capacity building programs and those graduating from the programs: do we see an acceleration in reaching key operational and impact milestones, do they raise venture capital/angel investment or impact investor funding faster and do they provide faster exit by acquisition.

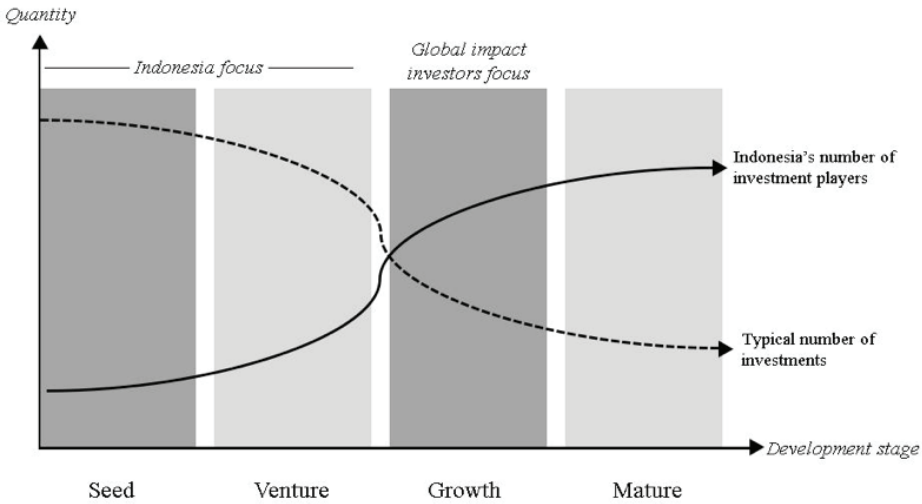
Social enterprise enablers in Indonesia have gained popularity and grown in numbers, but the quality and content relevancy of the enablers to the social enterprises is to be challenged. Even with a growing number of enablers, Indonesia still proves to be far from being able to provide social enterprises with the necessary means for development (e.g. advice, access to mentorship, coaching and network). Moreover, 80% of social enterprise socializing efforts are still concentrated in the Java islands (mostly Jakarta), leaving a lot of areas untouched. There is still space for social enterprises and its enablers to grow in Indonesia. If properly socialized and managed, Indonesia will see the emergence of more successful social enterprise cases in the future.

4.4 Social Finance Landscape in Indonesia: The Missing Middle Gap

By and large, the social financing landscape in Indonesia remains juvenile, although it is currently transitioning. The volume of funds disbursed is low and the financial instruments used does not vary compared to the more mature markets such as India and the United Kingdom. Regionally, Indonesia remains in the top three of impact investment destinations together with the Philippines and Vietnam. What sets Indonesia apart from its counterparts in Southeast Asia is its promising landscape: 1) the population boom will bring 90 million people into the consumer class by 2030, 2) currently, 90% of Indonesia's workforce relies on small medium enterprises, in which 79% of them still encounter challenge to access financing. However, complicated regulatory and bureaucracy make it difficult for foreign investors to enter the market. Meanwhile, the number of local investors is too low to finance them.

Concerning the supply and demand of funding, Indonesia is facing a typical "missing middle gap" where there are very few social enterprises that are investment ready, while there are a large number of investors who are willing to put capital in the growth and mature stages. Conversely, there are many early-stage social enterprises that require more funding, while there are very few of investors who are willing to invest.

__Figure 4.__ Investment vs. social enterprise distribution across lifecycle



V. Conclusion and Recommendation

5.1 Conclusion

The research has helped in understanding better the needs and barriers of several players involved in the social entrepreneurship ecosystem. Problems occur differently for each key players. Below is the summary:

__Table 2.__ Summary of problems in social entrepreneurship ecosystem based on each player

Ecosystem Players	Problems identified
Social enterprise	• Many are not investment ready
Investors	• Legal barrier and low understanding of investing in Indonesia
Enablers	• Can be a distraction for certain social entrepreneurs • Lack of sector specific focus • Lack of mentors • Difficulty to measure KPI and added value • Lack of impact metrics • Limited connections to social finance

5.2 Recommendation

Acknowledging that there is a missing middle gap in the distribution of investment across social enterprises, there has been a consensus about blended finance as a solution. It is the combination of public and private capital to finance social enterprises, achieve SDGs, and increase the effects of international development agency funding. According to the World Economic Forum (2015), blended finance is an approach to a development finance that employs the "strategic use of development finance and philanthropic funds to mobilize private capital flows to emerging and frontier markets". Furthermore, the characteristics of blended finance are defined as first, to leverage the use of development finance (e.g. IFC, ADB) and philanthropic funds (family foundations and NGOs) to attract private capital. Second, blended finance prioritizes all aspects of impacts (social, environmental, and economic). Third, the returns for private investors are in line with market expectations based on perceived risk.

Different tools are available to implement blended finance approaches; this paper will focus on supporting mechanisms and direct funding schemes.

Table 3. *Supporting mechanism and direct funding approaches on each level of social enterprise lifecycle*

Life Cycle	Pre-Seed	Seed	Seed/growth	Growth
Objectives	***Preparing***	***Pioneering***	***Facilitating***	***Anchoring***
Issues	High upfront costs to start social enterprise; high risk that a project will not be launched	High business model risk; high transaction costs	Sectoral or project risks; returns below commercial rates	Macro or sectoral risks; liquidity, refinancing and inefficient markets
Supporting Mechanism	Replication model (Sharing local and global market knowledge and experience)	Corporation involvement (incubator grant) Domestic impact evaluation entity (building local capacity)	Domestic impact evaluation entity (building local capacity) Financial literacy training for social enterprises (building local capacity)	Risk underwriting with hedging facilities (forex risk) Advocacy/training for local banks (building local capacity)
Direct Funding	First loss pioneer fund			

5.2.1 Support Mechanisms

Every life cycle in social enterprises have different objectives: as for pre-seed stage, the main issue faced is the high upfront costs to start and also higher risk of failure. Especially in Indonesia, there is a lack of compelling capacity building programs. As a result, social entrepreneurs and enablers spend significant time and capital to develop and establish new business models that capture value and impact, with a lower chance of success due to the lack of support for capacity building.

The recommended supporting mechanism for pre-seed enterprises is the replication model. The replicator's business model is to copy overseas proven social venture's and execute these models effectively in Indonesia. The replicator will capture the learning curve by partnering with the successful social enterprises across the region or worldwide and will recruit similar-minded entrepreneurs and talents to execute the venture development. The funding will be injected by different parties (e.g. corporates, impact investors, angel investors, etc.) and the incubation will be done by a local company builder or investor.

After reaching seeding stage, the enterprises would have high business models risks and also transaction costs. One of the supporting mechanisms is to involve large corporations through incubation grants. They already have the existing scales and assets; large corporations have tremendous potential coverage across Indonesia. They also have a deeper understanding of the value chain; which can benefit newer enterprises. The scheme would usually involve a matching between corporations and existing social enterprises that share the same objectives and missions. The social enterprise may grow organically in partnership with the corporation or through a joint venture. Another alternative is where the corporation may eventually choose to acquire the social enterprise.

Impact measurement is difficult for seed or growth stage due to the lack of domestic knowledge and trained staffs, and as a result, the evaluation is done using overseas resources which will increase the cost. The issue can be remedied by piloting a domestic impact evaluation entity that can provide services to local social enterprises and even overseas players. The Acumen's lean methodology could be one option to pilot. It will involve having the Acumen's team to come to Indonesia and train local staffs who could highly leverage on performing local participants (like hand-picked students) to do the impact evaluation assessment (on the model of the BCG giving back program).

Another issue identified for these stages is the lack of financial literacy of social enterprises. A proposed supporting mechanism is building a training facility designed to help selected social enterprises in the preparation to generate financial statements such as accurate profit and loss, balance sheet and cash flow statements. The training would be done on companies with the potential to export and raise debt from trade financiers such as Oikoscredit, Root Capital and ResponsAbility.

On the other hand, the cost of hedging the Indonesian rupiah is an issue for several impact investors lending from overseas. Several impact investors mentioned a cost of 7.0 to 9.0 % p.a. to hedge the principal amount. This can be addressed by setting up a hedging product, alternatively in the form of an independent financial technology company, to offer affordable currency options to impact investors. The form and implementation would need further research.

Lastly, there is an insufficient understanding from local banks in social enterprise model, which refrain them from investing. For instance, banks are comfortable with simple agriculture models rather than more complex models for other crops. This issue can be amended by designing a training or workshop targeting local banks in meeting and understanding social enterprises model. A facilitator will train the bank relationship managers and financial product design teams in understanding the risk and its mitigation tools. A pilot in the agriculture supply chain could also be considered.

5.2.2 Direct funding scheme

Another tool in the application of blended finance is direct funding scheme. As discussed in the previous chapter, there is a lack of seed funding as banks and impact investors think that there is a higher risk in investing in early-stage enterprises. A catalytic or 'first loss capital' structure would encourage the flow of capital to Indonesian social enterprises by improving their risk-return or by providing an incentive for other capital providers to invest. The structure of first loss capital could take several forms, such as credit guarantee, subordinated debt, matching grants and most junior equity positions. As an example, Panin Bank's top executive expressed that they would be interested to consider a loan to smaller enterprises and social enterprises if there was an institution willing to provide a guarantee.

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