

# LEVERAGE FOR GOOD:

## The New World of Social-Purpose Finance

BY LESTER M. SALAMON

**A revolution is underway on the frontiers of philanthropy. New charitable models hold the promise of leveraging for social and environmental purposes not just billions of dollars of charitable grants but hundreds of billions, indeed trillions, of dollars of private investment capital.**

**O**n September 28, 2011, *Microfinance Africa*, a newsletter serving the microfinance industry on the African continent, reported news of an important, if unusual, development designed to help East Africa cope with the region's food shortage and resulting skyrocketing food prices. An unexpected consortium had come together to channel \$25 million to a series of small and medium-sized East African agricultural enterprises whose businesses could help link the region's small-holder farmers to improved production and marketing opportunities. Although the US Agency for International Development (USAID) was a party to this consortium, this was not your normal top-down, government-funded, development project. Rather, USAID had teamed up with three foundations (the UK-based Gatsby Charitable Foundation, and the US-based Rockefeller and Gates foundations), a major US







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investment firm (J.P. Morgan Social Finance), and Pearl Capital Partners – a private, Kampala-based investment company dedicated to channeling private equity of small-holder agricultural enterprises in Africa.

What may be most unusual about this deal in the current climate of development assistance, philanthropy, and finance, however, is that it is no longer unusual at all. Rather, it is an example of what students of the field have begun referring to as “yin-yang” deals, deals that bring together, as in Chinese thought, seemingly contrary forces that turn out to be uniquely capable of producing new life forms when taking advantage of their interdependencies. In the present arrangement, USAID managed to stimulate the investment of \$25 million into building a robust agri-business sector in East Africa with only \$1.5 million of its own money, and all of that in the form of technical assistance to small and medium-sized businesses funded out of President Obama’s flagship Feed the Future initiative. The investment fund itself was assembled by combining this with a USAID guarantee of an \$8 million loan from J.P. Morgan’s Social Finance Unit that was further leveraged by \$17 million in equity investments made by the three foundations, which functioned in this deal as “philanthropic banks” rather than traditional grant-making charities.

Sizable yin-yang deals of this sort are slowly becoming the new normal in efforts to combat the enormous social, economic, and environmental problems that confront our world today. And none too soon. With the resources of both governments and traditional philanthropy barely growing or in decline, yet the problems of poverty, ill-health and environmental degradation ballooning daily, it is increasingly clear that new models for financing and promoting social and environmental objectives are urgently needed.

Fortunately, a significant revolution appears to be underway on the frontiers of philanthropy that is providing at least a partial, though still embryonic, response to this dilemma. The heart of this revolution is a massive explosion in the tools of philanthropy and social investment, in the instruments and institutions being deployed to mobilise private resources in support of social and environmental objectives. Where earlier such support was limited to charitable grants and gifts made available directly by individuals or through charitable foundations and corporate giving programs, now a bewildering array of new instruments and institutions has surfaced – loans, loan guarantees, private equity, barter arrangements, social stock

exchanges, bonds, secondary markets, investment funds, and many more. Indeed, the world of philanthropy seems to be experiencing a Big Bang similar in kind, if not in exact form, to the one thought to have produced the planets and stars of our solar system.

Even a quick glance at the emerging landscape on the frontiers of contemporary philanthropy around the world yields a rich harvest of unfamiliar names and terms: Bovespa in Brazil; Social Capital Partners in Canada; Impact Investment Exchange in Singapore; Acumen Fund, Root Capital, and New Profit in the US; Bridges Ventures, Big Society Capital and NESTA in the UK; Blue Orchard in Switzerland; Aavishkaar International in India; Willow Tree Impact Investors in Dubai; Calvert Foundation; the Schwab Charitable Fund; the Community Reinvestment Fund; Community Development Finance Institutions; TechSoup Global; conversion foundations; and many more.

At the core of this enormous proliferation of entities lie four important processes of change. In particular, contemporary philanthropy is moving:

- **BEYOND GRANTS:** deploying a variety of new financial tools for promoting social purposes – loans, loan guarantees, equity-type investments, securitisation, fixed-income instruments, and, most recently, social impact bonds;
- **BEYOND FOUNDATIONS:** creating a host of new actors as the institutional structures through which social-purpose finance is proceeding – capital aggregators, secondary markets, social stock exchanges, social enterprise brokers, internet portals, to name just a few.
- **BEYOND BEQUESTS:** forming charitable or social-purpose capital pools not simply through the gifts of wealthy individuals, but also from the privatisation of formerly public or quasi-public assets or the establishment of specialised social-purpose investment funds; and
- **BEYOND CASH:** utilising new barter arrangements and internet capabilities to facilitate the giving not just of money, but of a variety of in-kind forms of assistance, whether it be volunteer time or computer hardware and software.

Behind these movements is a common imperative, usefully summarised in a single word: *leverage*. Leverage is the mechanism that allows limited energy to be translated into greater power. It is what allowed Archimedes to claim that, given a lever and a place to stand, he could “move the whole world”. In the philanthropic context it means finding a way to go beyond the limited flow of charitable resources generated by the earnings on foundation assets or the annual contributions of individuals to catalyse for social and environmental purposes some portion of the far more enormous investment assets resident in banks, pension funds, insurance companies, mutual funds, and the accounts of high net-worth individuals.



The upshot is the emergence of a “new frontier” of philanthropy and social investing that differs from twentieth century philanthropy in at least four ways. It is:

- **MORE DIVERSE**, involving a wider variety of institutions, instruments, and sources of support;
- **MORE ENTREPRENEURIAL**, moving beyond “grant-making”, the giving of resources, to capture the possibilities for greater leverage that comes from adopting an investment orientation, focusing more heavily on measurable results, and generating a blend of economic, as well as social, returns;
- **MORE GLOBAL**, engaging problems on an international scale and applying models developed in cross-national settings; and
- **MORE COLLABORATIVE**, interacting explicitly not only with the broader civil society sector, but also with new social ventures serving the “bottom of the pyramid”, as well as with a broad array of private financial institutions and government agencies.

While the changes under way are inspiring and by no means trivial, however, they remain scattered and largely uncharted in any systematic fashion. Individual practitioners typically have a handle on one or another of the relevant innovations, but the full scope of the changes has yet to be visualised, let alone

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pulled together and examined in a systematic way. Even the terminology used to depict these developments is in flux. Established terms such as “program-related investments” (PRIs), “mission investing”, and “market-rate investments”, all of which tended to apply narrowly to foundations, have recently been superseded by the term “impact investing”, which itself covers only a portion of the emerging field and involves its own significant ambiguities.

What is more, much of the extant literature on these developments takes the form of quasi-“grey material”, available only in limited editions to a restricted audience. Largely lacking have been materials that can take the changes under way out to a broader audience and that can penetrate the sizable academic universe training nonprofit managers, social entrepreneurs, business leaders, bankers, investment managers, corporate social responsibility officers, and public policy experts. For the new approaches to philanthropy and social investing

to achieve the impact of which they are capable, it will be necessary for these concepts to make the jump to a broader strata of participants and observers. Even early innovators have come to recognize this point, arguing, as two of them recently put it, that the “challenge now is to bring this [impact investment] perspective from the fringe to the mainstream,” which will require “a new generation of... communicators” who can “absorb the lessons from visionary practice and communicate them effectively to much wider audiences.”

### **New Frontiers of Philanthropy: A Guide to the New Actors and Tools Reshaping Global Philanthropy and Social Investing**

In *New Frontiers of Philanthropy*, published by Oxford University Press, and a companion volume entitled *Leverage for Good*, which carries just the introductory chapter to this larger volume, I have attempted to address this challenge and provide a clear and accessible roadmap to

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the full range of important new developments taking place on the frontiers of philanthropy and social investment. The ultimate goal is to broaden awareness of these significant developments, increase their credence and traction, and make it possible to maximise the benefits they can generate while acknowledging the limitations and challenges they still also face.

The result is the first comprehensive overview of the new actors and tools transforming philanthropy and social investment, the factors giving rise to them, and the steps needed to promote their further development.

### A New Paradigm of Social-Purpose Finance

Viewed through the new frontiers of philanthropy lens, it becomes clear that a new paradigm of social-purpose finance is taking shape:

- Where traditional philanthropy relied chiefly on individuals, foundations, and corporate philanthropy programs, the new frontiers of philanthropy engage a variety of capital aggregators, social secondary markets, social stock exchanges, foundations functioning as philanthropic banks, commercial banks, pension funds, insurance companies and investment advisors;
- Where traditional philanthropy relied almost exclusively on the tool of charitable grants, the new frontiers utilises an array of *financial instruments* – loans, credit enhancements, bonds, securitisation, private equity, quasi-equity, micro-insurance, social impact bonds and more;
- Where traditional philanthropy concentrated mostly on operating income, the new frontiers place their emphasis on *investment capital*; and
- Where traditional philanthropy channels its assistance almost exclusively through nonprofit organisations, the new frontiers support as well a wide assortment of social enterprises, social cooperatives, community interest organisations, and other hybrid entities.

### Why Now?

There is reason to believe that the recent changes taking place on the frontiers of philanthropy are more than a passing fad. Some significant underlying forces have been at work to produce this development at this time. What is more, these forces are operating both on the demand side of this evolving market – creating a strong need for the changes that are underway – and on the supply side – stimulating the availability of both the talents and the resources to meet this need. New players, with new mindsets, and new concepts have come forward, likely spurred in significant part by the psychological shock administered by the 2008 financial crisis and the forced recognition it stimulated that apparent wealth could quickly disappear but that the satisfaction of making a difference in the world offered permanent rewards.


### Remaining Obstacles

But none of this means that the road ahead for these developments is clear of obstacles. To the contrary, significant challenges remain. These obstacles take a number of forms, but five of them seem especially important to acknowledge and confront:

- The pesky dilemma of limited deal flow; and
- The distraction of comforting, but questionable, assumptions regarding likely return rates and the prospects of displacing either government or philanthropy completely.

### Prescription - the Way Forward

Despite the obstacles and limitations, however, there is sufficient promise in the developments taking place on the frontiers of philanthropy to warrant further active encouragement.

Such encouragement could usefully take six major forms designed to: (i) visualise; (ii) publicise; (iii) incentivise, and (iv) legitimise the new actors and tools, and then (v) capacitate those who must make use of them, and (vi) actualise the deals through which these various components can be brought to bear. While hardly a panacea, these developments offer one of the more promising bright spots in an otherwise dismal scenario of lagging resources and resolve. 



This article draws heavily on *Leverage for Good* (Oxford, 2014) and the Introduction to *New Frontiers of Philanthropy* (Oxford, 2014), both by Lester M. Salamon.

### About the Author

**Lester M. Salamon** is a professor at the Johns Hopkins University in the USA, director of the Johns Hopkins Center for Civil Society Studies, and former deputy associate director of the Office of Management and Budget in the Office of the US President. For further information, consult: Lester M. Salamon, *Leverage for Good* (Oxford University Press, 2014) and Lester M. Salamon, (ed.) *New Frontiers of Philanthropy: A Guide to the New Actors and Tools Reshaping Global Philanthropy and Social Investing* (Oxford University Press, 2014). Available at [oup.com](http://oup.com) and from Amazon at [bit.ly/NFPSalomon](http://bit.ly/NFPSalomon) and [bit.ly/LfGSalomon](http://bit.ly/LfGSalomon).