

VIRTUE'S INTERMEDIARIES

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A host of new businesses is trying to make the philanthropic market work better

LEGEND has it that New Philanthropy Capital (NPC) was founded in the Goldman Sachs canteen in London in 2001. After Goldman went public, Gavyn Davies, then its chief economist, and another top banker, Peter Wheeler, had pocketed enough money to enable them to do some serious giving. But when they tried to pin down the best place for their money to create maximum impact, "We found there wasn't enough information produced in a hard-headed, independent, high-quality way, made available to all," recalls Mr Davies. So they decided to create NPC as the equivalent of an equity-research firm for the philanthropic marketplace.

It had the added attraction of providing leverage, the holy grail of the new givers. "We wanted our own charitable donations to be the foundation of a much bigger edifice. This was an investment designed to have a levered effect on other people's giving," says Mr Davies. "We wanted to increase giving by enabling donors to be more confident that they were having an impact on people's lives."

For now, the research effort, headed by Martin Brookes, a former senior economist at Goldman Sachs, is confined to the charity sector in Britain. NPC is not providing ratings at present, but the equivalent of "buy" recommendations through sector reports such as "Grey Matters, Growing Older in Deprived Areas". In preparing these reports, NPC asks the charities seeking funds four simple questions: What is it you do? Why? What is success? And what is evidence of success? The firm also does some secondary research, such as summarising and translating academic work and making it more widely available.

"When you come into this world from Goldman, you realise how screwed up it is as a market," says Mr Brookes. "We are trying to fix the plumbing." They are not alone. Efforts are under way to develop philanthropic versions of most of the main sectors of the capitalist marketplace: social-investment banking, social-investment management, private banking, consulting, data services and research. Though currently the organisations providing these services are relatively small, there appears to be enough demand to enable a successful operation to grow fast.

"The biggest constraint on our growth has been the ability to recruit top talent," says Mr Davies. "Only a few people are willing to come out of a career in banking to do this." An analyst at NPC can expect to earn GBP22,000-48,000 (\$38,000-84,000), a small fraction of what they would make at Goldman.

In any marketplace, knowledge is power. NPC is attracting interest in America, which currently has no direct equivalent. The big foundations,

in particular, do lots of research, but they tend to keep it to themselves. The nearest counterpart to NPC in America is Geneva Global (GG), but it covers only giving opportunities outside America. GG's 140 employees work with a network of over 500 voluntary associates in over 100 countries. It mostly concentrates on small projects, which it thinks have a greater impact.

FAMOUS BRANDS

"In philanthropy, the stuff that will deliver most often gets least," says GG's boss, Eric Thurman. Brands count for a lot in the world of giving, and many people like to give to familiar organisations. For instance, the Red Cross, despite heavy criticism of its handling of donations after September 11th 2001, collected almost 70% of the money given for relief work after Hurricane Katrina wrecked New Orleans.

GG challenges the big charities by finding a small, local group that is doing something well and is ready to scale up its operations. It sends potential donors a monthly catalogue with a choice of evaluated projects, and later provides feedback on what their money has achieved. "We want to be known for making a direct connection between the money you raise and lives changed," says Mr Thurman.

For more comprehensive information about who is doing what in the philanthropic world, there is GuideStar. Nicknamed the "Bloomberg screen of philanthropy", it was founded in America in 1994 by Buzz Schmidt and makes available online, free of charge, the tax-return data filed by 1.5m charitable organisations, together with additional information. It has more than 400,000 registered users, and for a fee it offers detailed analysis of the data--such as which organisations do what in a particular area, how much a charity pays its chief executive relative to the average, and so on.

Mr Schmidt is now busy setting up similar services abroad. Last year GuideStar was launched in Britain, putting data online that had been sitting on paper in Charities Commission and tax-office cabinets, largely unlooked at, says Les Hems of the Institute for Philanthropy, the parent organisation of the British end of GuideStar. The institute was founded in 2000 to help foster charitable giving in Britain, not least by starting, and then spinning off, new organisations that solve particular problems. Britain's Treasury gave it GBP2.9m, topping up GBP1m raised from donors. Now GuideStar is trying to secure continuing public funding, as well as fees from licensing data to organisations such as NPC. Other versions of GuideStar are planned in India, South Africa and Australia.

Not everyone is impressed. Mr Porter, the Harvard strategy guru, thinks that GuideStar's figures are too superficial to be much use in judging, say, the performance of foundations. He helped establish the Centre for Effective Philanthropy, which among other things produces donor perception reports based on confidential surveys of organisations that receive money from foundations. Initially foundations were reluctant to publish the reports, especially the critical ones, but that is starting to change. "Smart non-profits are realising that they can do well by being more transparent, and talking about their successes and failures," says Tony Knerr, a philanthropy consultant.

"The social sectors do not have rational capital markets to channel resources to those who deliver the best results," says Mr Collins. According to a recent article in Stanford's SOCIAL INNOVATION REVIEW, in America raising \$100 can eat up anything from \$22 to \$43. In Britain, the average cost of finance to charities is around 25%, which is very high relative to other industries, notes NPC's Mr Brookes.

The traditional grant-making process is a large part of the problem. Donors would generally rather fund a project than invest in building an organisation. If a charity has money in the bank, they will ask why they should provide any more, and what exactly their donation will be used for.

Not everybody is so short-sighted. For example, the Ford Foundation is encouraging the greater use of debt and debt-like instruments because "there is a growing number of income-generating activities, and donors want to help borrowers to get a credit rating so they can go to the commercial market," says Susan Berresford, the foundation's boss.

In Britain, Venturesome has been arranging unsecured loans for charities, typically bridging finance for those waiting to be paid a promised grant. And in America College Summit, which aims to raise the proportion of young people going to college in low-income areas, recently secured \$15m in growth capital to fund its ambitious expansion plans for the following three years. Previously, it had to raise finance for expansion one project at a time, a costly, time-consuming process.

According to George Overholser of Non-Profit Finance Fund Capital Partners, who helped to raise the money, this is only the first of many private placements of donor capital for non-profits. NFF Capital helps non-profits to raise capital for the organisation as a whole, rather than for an individual project. Mr Overholser claims to have a pipeline of ten charities he considers suitable for similar financing.

A CONFUSION OF CAPITAL

The inadequate accounts of non-profits have proved a big complication. In America at least, all inflows of money are treated as revenue, even if it is really investment capital. Yet to raise growth capital, as College Summit has done, it is crucial to distinguish between money a non-profit receives for services rendered and money it is given to build its organisation. Mr Overholser has devised a common reporting method to track how the money is being spent, to be used both by donors and for internal management purposes. This will introduce concepts from the for-profit world, such as "burn rate" (the rate at which capital is being used), giving all concerned a better idea of how well the expansion is going. Now non-profits can work backwards from their expected long-term sustainable sources of finance to work out their current need for capital, and how to structure it, says Mr Overholser.

In the capital markets, there has been a proliferation of investment opportunities, from mutual funds to complex derivatives. Something similar may be under way in the philanthropic world, ranging from investments that pay a decent return on money put to worthy uses to structures that allow donors to give their money away more effectively.

In America, Google.org has just invested \$5m in the Acumen Fund, which channels donors' money to a portfolio of entrepreneurial poverty-fighting organisations.

In Britain, NPC and the Charities Aid Foundation recently launched a couple of funds that will allocate money to a portfolio of charities, monitor its impact and keep the donors informed about progress. The first two funds concentrate on charities in particular sectors, as their names suggest: the Engaging Young Lives Fund and the Fulfilling Older Lives Fund.

A host of new tax-favoured opportunities have been coming on stream at the same time, guided by Sir Ronald Cohen, a private-equity grandee, philanthropist and chairman of the British government's Social Investment Taskforce. For example, Bridges Community Ventures, which invests in businesses in deprived areas of Britain, has done well with its first fund and is raising another. Charity Bank--"the compassion of a charity and strength of a bank"--has been set up to provide banking services exclusively to charities. Last year, the government launched the Community Interest Company, which engages in commercial activities for community purposes that are not primarily driven by profit. They can pay dividends and borrow, but can be sold for full value only if the money remains in the charitable sector.

Driven by growing demand from wealthy clients, private banks such as Goldman Sachs, HSBC, Coutts and UBS are now scaling up philanthropy advisory services way beyond traditional tax and inheritance advice and asset management. A growing amount of consulting advice, too, is available to philanthropists and those they fund. Rockefeller Philanthropy Advisors is probably the leading consultancy concentrating solely on the giving side.

ADVISE AND CONSULT

Some of the big management consultants are also expanding their non-profit businesses. In 1999, McKinsey created a separate non-profit practice specialising in three main areas: global public health, foundations, and international aid and development. In general, it charges half its regular fee for such work, though for a particularly deserving cause it may drop it even further or forgo it altogether. Its clients include the Gates Foundation and Bono's campaigning organisation, DATA (Debt, AIDS, Trade, Africa).

Bain adopted an even more ambitious strategy. In 2000, it launched Bridgespan, a stand-alone consultancy and executive-search business for non-profits. Run by the former head of Bain, Tom Tierney, Bridgespan aims lower than McKinsey, at mid-sized non-profits. It now employs 75 people who typically earn 30-40% less over a five-year period than they would at Bain. Even so, last year it had 1,700 applications for 18 jobs. Bain would like Bridgespan to spread to other countries, but there is plenty left to do at home, says Mr Tierney: "We are serving only 10% of our demand right now, and turning down the vast majority of approaches from serious clients."

Perhaps the boldest, or craziest, idea is to launch a social stockmarket. Mr Skoll thinks it may happen one day, though no one has any idea what sort of security might trade on the exchange. "Perhaps there could be some sort of system involving social merit points," he

muses; something akin to the recent development of carbon-emissions trading.

"The proliferation of market services is going to be very good for philanthropy," says Mr Myerson of the Philanthropy Roundtable. "There will be more services, more choice, more information, more opportunities to capture people's philanthropic imagination." But in the end, those who are trying to produce a philanthropic version of the capital markets must answer a billion-dollar question: how do you measure success? The original sort has an incontrovertible answer: profits. But a philanthropic equivalent will be nothing like as straightforward.

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