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Venture Philanthropy – a good idea at the right time

Philanthropy – practical benevolence

Charity – liberality to the poor

Source: Oxford English Dictionary

In the New Year my intention is to return to the subject of private equity, but as financial markets start to slow down in the run up to Christmas it seems more appropriate to comment on developments in philanthropy and the way in which private equity skills are being put to work for charitable purposes. It is, after all, the season of goodwill.

Without wishing to overstate the case, there is evidence of changing attitudes to philanthropy. A number of factors such as generational change have an influence, but perhaps most importantly it is clear that donors are looking to retain greater control by self management of their philanthropic activities rather than subcontracting to traditional charities. Governments are also interested in this trend as they try to reduce the role of the state in paying to solve social problems.

I have been following venture philanthropy developments since 2006 and so have seen the way in which this concept has evolved to meet the demands of the post credit crunch world. According to the Charity Commission for England and Wales there are 162,440 registered charities at present with annual income of £52.86bn. In contrast there are only 10 venture philanthropy funds accounting for 0.172% of total income.

On the assumption that venture philanthropy may be a new concept I turned to Chris Carnie, founder of Factary, a European consultant in the field of philanthropy since 1990, for some background;

> *Venture philanthropy (VP) is not the new kid on the financial block – it originated in 1997 in a Harvard University paper and in a Silicon Valley community foundation. But it is adolescent, noisy, opinionated and keen to turn over the old ways of doing things. We calculate that the total assets of the UK's ten leading VP funds reached £2 billion in 2010 with income, in 2009, of £91m.*
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> *Venture philanthropy is like venture capital (VC) from which it was born; in its purest form it is a specialist activity, undertaken by a few. It is defined by the leverage it seeks, as it aims to build stronger social purpose organisations using a mix of financial and non-financial support. VP is not about "giving money away" to needy causes. A VP approach would be to find an organisation that meets a social or environmental need (anything from an educational charity to a community transport service) and then to strengthen the organisation, so that it can do more. Just like venture capital, this means high engagement with the cause (many VP funds insist on a seat on the nonprofit's board), tailored finance over a number of years, non-financial support – often in the form of advice and training - and performance measurement.*
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> *Each of these areas has meant throwing out the old model and trying something new. The simple idea that a funder should insist on a seat on the board has meant that many potential partnerships never got past the first meeting between VP and nonprofit. The tailored finance area has been the source of some clever financial architecture, including organisations that link philanthropy, investment in social enterprises and pure VC, in order to generate profits from the latter to feed the former. It has also been the source of a dizzying new vocabulary, from "soft equity" through "Impact Investing" to "patient capital."*

The VP community has pushed performance measurement to new levels with the development of tools for measuring "Social Return On Investment" (SROI.) The idea that you can measure the social benefits of a philanthropic investment has been around since the 1970s. But it is only in the last couple of years that we have seen charitable foundations in the UK really take it seriously.

The funds vary widely in their philanthropic investment model – some going for grants, attached to strict structural change and SROI measures, others, such as Venturesome, providing loans and soft equity. Venturesome is a scion of the long-established Charities Aid Foundation – just as Inspiring Scotland was floated out of the Lloyds TSB Foundation. This is a feature that is becoming increasingly common in Europe, with some of the very largest foundations creating VP funds, or at least subsidiary foundations with many VP characteristics. We will see more of these subsidiary foundations in the future.

VP blurs the lines between what is philanthropic and what is for-profit. This trend will strengthen over the next few years, with the old battle-lines between "charity" and "business" falling away and new mixed entities appearing, using the best of both worlds to solve social problems and provide financial returns to their investors. There is a developing spectrum of financial products, ranging from (social) "impact-only" investments such as grants, through "impact-first" investments such as an investment in a social enterprise, to "profit-first" investments, such as traditional private equity. As this spectrum of investment opportunities develops, we can expect to see more and better data on social, and financial, risks and returns.

It certainly seems to me that venture philanthropy is an idea that has found it's time. Just as the decline in bank lending has presented exceptional opportunities for private equity investors, venture philanthropy is growing as wealthy individuals adopt a more business like approach. It is also interesting to look at the way in which philanthropy is being interpreted in both India and China where the expertise and wealth of entrepreneurs is being mobilised in similar ways.

Individuals rather than institutions drive innovation and there is a growing trend in the charity sector towards making both money and skills work harder. In any fast changing sector there are bound to be challenges. The most obvious one is that the boundary between philanthropy and commercial funding may become blurred. However, at present it seems unlikely that banks will prioritise funding business plans that are unusual or difficult to assess and this opens the door to venture philanthropists who will have different priorities.

For those of us involved in advising and managing the wealth of individuals it is clear that an increasing number of our clients are looking for more imaginative ways to recycle some of their wealth and are prepared to play a far more active role than has been the case in the past. Practical benevolence in action for the post credit crunch world.

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