



The
Economist

The business of giving

A survey of wealth and philanthropy
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The business of giving

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Philanthropy is flourishing as the number of super-rich people keeps growing. But the new donors are becoming much more businesslike about the way their money is used, says Matthew Bishop

GIVING away money has never been so fashionable among the rich and famous. Bill Gates, today's pre-eminent philanthropist, has already handed over an unprecedented \$31 billion to the Bill and Melinda Gates Foundation, mostly to tackle the health problems of the world's poor. Its generosity has earned the couple *Time* magazine's nomination as 2005's "people of the year", along with Bono, an activist rock star.

The next generation of technology leaders are already embracing the same ethos. Pierre Omidyar, the founder of eBay, and Jeff Skoll, the auction site's first chief executive, are each putting their billions to work to "make the world a better place". And when the founders of Google, Sergey Brin and Larry Page, took their company public, they announced that a slice of the search engine's equity and profits would go to Google.org, a philanthropic arm that they hope will one day "eclipse Google itself in overall world impact by ambitiously applying innovation and significant resources to the largest of the world's problems".

The new enthusiasm for philanthropy is in large part a consequence of the rapid wealth-creation of recent years, and of its uneven distribution. The world now boasts 691 billionaires, 388 of them "self-made", compared with 423 in 1996, according to *Forbes* magazine's "rich list" for 2005. Not all of these newly wealthy people are

turning to philanthropy—and of those that do, many continue to give in unimaginative ways, say to support an institution such as their *alma mater*. But the extra wealth is creating huge new opportunities. "This is a historic moment in the evolution of philanthropy," says Katherine Fulton, co-author of a recent report on the industry, "Looking out for the Future". "If only 5-10% of the new billionaires are imaginative in their giving, they will transform philanthropy over the next 20 years."

For now, it does look as though everyone, from Michael Bloomberg, the billionaire mayor of New York, to hedge-fund tycoons and film stars, is opening their wallet for a good cause. In Manhattan these days, a table for ten at the best charitable fund-raising dinners can cost \$1m. Celebrities are increasingly putting their own money into good works, as well as playing their time-honoured role of using their fame to raise money from others. The film star Angelina Jolie, for example, has backed up her public advocacy of the cause of refugees with substantial gifts to refugee organisations.

The media, which used to take little notice of charitable donations, now eagerly rank the super-rich by their munificence and berate those they regard as tight-fisted. The latest *Business Week* list, which ranks giving in the latest five years, is topped by Intel's co-founder, Gordon Moore, and his wife Betty, pushing Mr and Mrs Gates into

Acknowledgments

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A list of sources can be found online

www.economist.com/surveys

An audio interview with the author is at

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▶ second place. Among America's super-wealthy, it seems that only Warren Buffett, the world's second-richest man, still dedicates all his energies to making more money rather than giving away some of what he already has. But even he says it will all go to charity when he dies.

Nor is the fashion for giving limited to America, where philanthropists have long played a particularly prominent role. In Europe, too, entrepreneurs who have made a lot of money are starting to hand some of it to charitable causes. Examples include Britain's Dame Anita Roddick, founder of the Body Shop, and Arpad Busson, a colourful French hedge-fund boss. India's new wealthy, such as Azim Premji and Nandan Nilekani, two Bangalore technology-firm bosses, are also becoming keen philanthropists; and even the new rich of China and Russia are catching the bug. Roman Abramovich, a Russian oil-garch who became famous for buying Chelsea Football Club, has given away many millions to improve living conditions in the Kamchatka region of Russia. And so the list goes on.

The whys and wherefores

Why are they doing it? Many people are wary of rich folk bearing gifts, suspecting them of having hidden business or political motives, or feeling guilty about how they have made their pile, or simply enjoying an ego trip fuelled by generous tax breaks. But there could also be plenty of innocent and admirable reasons why the rich have become so much more open-handed. Never mind the motives: the important thing is to ensure that this largesse is put to good use.

Done well, philanthropy can have a hugely beneficial effect—witness the achievements of past giants such as An-

drew Carnegie, John D. Rockefeller, Joseph Rowntree and William Wilberforce. This survey will argue that if the new generation of philanthropists get it right, they too can make a real difference to the world. But for that to happen, philanthropy will have to shed the amateurism that still pervades much of it and become a modern, efficient, global industry.

For much of the past half-century, America seemed exceptional in its enthusiasm for philanthropy. Claire Gaudiani, in her book, "The Greater Good: How Philanthropy Drives the American Economy and Can Save Capitalism", makes a distinction between charity, which is about easing symptoms of distress, and philanthropy, which is about investing in solutions to the underlying problems. The "investment approach distinguishes the most significant kind of American generosity from the 'poorhouse and soup line' method and expresses our values of freedom, the individual, and entrepreneurialism," she says. In practice, though, the borderline between the two is often blurred.

Over the years, many wealthy Americans have broadly followed the blueprint laid out by Andrew Carnegie in his 1889 essay, "Wealth". The steel tycoon believed that growing inequality was the inescapable price of the wealth-creation that made social progress possible. To prevent this inequality undoing the "ties of brotherhood" that "bind together the rich and poor in harmonious relationship", he argued that the wealthy had a duty to devote their fortunes to philanthropy. Not to do so was the worst sort of personal failure: "The man who dies thus rich dies disgraced."

As a result, a far higher proportion of hospitals, libraries, universities and welfare services in America is funded by private donations than in other rich countries, where governments are spending proportionately more yet are still struggling to meet growing public expectations. Still, the differences can be exaggerated. America's basic health research is largely funded by the government, whereas in Britain much of it is paid for by the Wellcome Trust, a charitable foundation based in London, albeit set up by an American.

Britain's government has recently been trying to foster the philanthropic spirit, and other European countries are starting to follow suit. Even in China, the government seems keen to build up a non-profit sector that caters to social needs, and appears to be relaxing some of its rules to allow philanthropy to play a bigger role. The exception is Russia, where President Vladi-

mir Putin, averse to concentrations of power outside his government, has cracked down on non-governmental organisations (NGOs) and their backers. Mikhail Khodorkovsky, the former boss of Yukos, a big oil company, was reportedly Russia's leading philanthropist before he was jailed after a show trial.

But just as the world's wealthy and powerful are discovering the joys of giving, students of the American model of philanthropy are becoming increasingly critical of its flaws. This is not just a private concern for the donors: because of America's huge tax breaks for charitable donations, it is a matter for public scrutiny too. The cover story of a recent issue of Stanford University's *Social Innovation Review* is entitled "A Failure of Philanthropy". It argues that those American tax breaks are of most benefit to things like elite schools, concert halls and religious groups. "We should stop kidding ourselves that charity and philanthropy do much to help the poor," says the author, Rob Reich.

A series of scandals at charitable foundations—mostly over excessive pay, jobs for family members and other extravagances—has attracted the ire of Congress, which is threatening tough new legislation. State attorneys-general are taking a greater interest, too.

Mainstream charities that rely largely on donations from the general public have also come under fire. The American Red Cross was exposed for diverting money raised for the families of victims of the September 11th 2001 terrorist attacks to other purposes. And after the Asian tsunami and Hurricane Katrina, two fundraising former presidents, Bill Clinton and George Bush senior, found themselves having to reassure the public that they would monitor how the money was used.

One of the many things exposed by the collapse of Enron was that corporate philanthropy is often pretty sleazy too. A firm's executives can ingratiate themselves with business partners, and even with their own board members, by supporting their pet causes with funds from the company's charitable foundation, without breaking the law.

Wasting a fortune

But the problem lies far deeper. "Foundation scandals tend to be about pay and perks, but the real scandal is how much money is pissed away on activities that have no impact. Billions are wasted on ineffective philanthropy," says Michael Porter, a management guru at the Harvard ▶▶



► Business School. “Philanthropy is decades behind business in applying rigorous thinking to the use of money.” Mr Porter believes that the world of giving can be transformed by learning from the world of business. Many of the leaders of the new generation of philanthropists agree with him, so “there is a big opportunity over the next 20 years to figure out how to make philanthropy effective.”

Many of the new philanthropists are well aware that traditional philanthropy is not sufficiently businesslike. They want to bring about a productivity revolution in the industry by applying the best elements of the for-profit business world they know. That has prompted the industry to adopt (and adapt) some of the jargon familiar from the world of business. Philanthropists now talk about “social investing”, “venture philanthropy”, “social entrepreneurship” and the “triple bottom line”. The new approach to philanthropy is “strategic”, “market-conscious”, “knowledge-based” and often “high-engagement”, and always involves maximising the “leverage” of the donor’s money.

Leverage is particularly important to the new philanthropists. They know that however large their personal fortunes, they are dwarfed by the financial resources at the disposal of governments and in the for-profit marketplace. So to make a real difference, they need to concentrate their resources on problems that are not being dealt with by governments or for-profit organisations. Being constrained by neither voters nor shareholders, they can take risks to find pioneering new solutions that can then be adopted on a larger scale by governments or for-profit firms.

But not everyone is convinced that philanthropists must become more business-minded. “We must reject the idea—well-intentioned, but dead wrong—that the primary path to greatness in the social sectors is to become ‘more like a business,’” wrote Jim Collins, a bestselling management author, in a recent monograph, “Good to Great and the Social Sectors”. His reason is disarmingly simple: “Most businesses are mediocre.”

Still, even Mr Collins agrees that the way in which money passes from philanthropists to the organisations that put it to work leaves much to be desired. Here there is some reason for hope. In recent years, a host of new firms and institutions have been created that, with luck and good management, will provide the infrastructure and intermediaries of a philanthropic capital market, an efficient way for philanthropists to get their money to those “social entrepreneurs” and others who need it. These newcomers include management consultants, research firms and a philanthropic investment bank of sorts.

Plenty can still go wrong. There is no market discipline to force philanthropists to adopt innovations, however desirable. And the new philanthropists, along with the innovators who are trying to help them become more efficient, may find the going harder than expected. “The new rich have often made their money very fast, and get intoxicated with their own brilliance into thinking they can quickly achieve results in the non-profit sector. They forget that their success may have been due to luck, and that the non-profit sector may be far more complex than where they have come from,” says Mario Morino of Venture Phi-

lanthropy Partners, one of America’s leading venture philanthropists.

One obvious risk is of a political reaction against the philanthropic rich. The new philanthropists are not just into spending money. According to Greg Dees of Duke University, today’s philanthropy is best defined as “mobilising and deploying private resources, including money, time, social capital and expertise, to improve the world in which we live.”

Peggy Rockefeller Dulany, who runs the Global Philanthropists Circle, makes a similar point. “With wealth comes education, decision-making power, links to elites in other countries and enormous convening power,” she says. “We are helping philanthropists to make use of all these advantages. It is using money and connections—whether personal, family or business—to create public benefit.”

A global elite, seeking to change the world by combining lots of money with new ideas, cutting-edge business techniques, media and marketing savvy, the mobilisation of citizens and helpful political connections: all this is bound to set alarm bells ringing in some quarters even as it spreads hope in others. Already George Soros, a famous hedge-fund philanthropist, has become embroiled in controversy over the role of some of the organisations he funds in various former communist countries as well as in America itself. And last year Bob Geldof, Bono’s philanthropist partner in rock activism, provoked demonstrations in Uganda when he suggested that the country’s president should not stand for re-election. Philanthropy seems sure to become an increasingly hot political potato. ■

To have, not to hold

The rise of the new philanthropist

BILL GATES is much the most generous philanthropist since records began. The \$31 billion he has donated so far is already many times the \$6 billion (in 2005 dollars) given away by a previous giant of American philanthropy, John D. Rockefeller. And Microsoft’s founder is only just getting started. By the end of his life, he intends to have handed over most of the rest of his fortune—put at \$46.5 billion in *Forbes* magazine’s latest “rich list”—to the Bill and Melinda Gates Foundation.

Mr Gates is given much of the credit for the rise in giving among today’s super-rich. He seems to have discovered his generous streak relatively recently: in 1998, *The Economist* was still criticising him for sitting on his fortune. But since then “Bill Gates has made philanthropy the norm” among the super-rich of the world, says Vartan Gregorian, who runs the charitable foundation set up by Carnegie. “Giving is now what you are expected to do.”

The power of Mr Gates’s example is

one reason why Mr Gregorian—who is a mentor to many of the new philanthropists around the world—is no fan of the secretive approach to giving. “I like people to be public about their philanthropy; it makes it more competitive if we can see who is doing what.”

In order to give money away, you first have to have it. The past two decades have seen vast global wealth-creation, but the “winner-takes-all” aspect of many of today’s fastest-growing markets, and the ►►

▶ sharp reductions in top marginal income-tax rates and profit and capital taxes almost everywhere, have caused a rapid increase in inequality between the very rich and the rest. The number of billionaires is growing fast, and not just in America: of the 691 billionaires listed by *Forbes*, 350 live outside America, with Lakshmi Mittal, an Anglo-Indian steel tycoon, coming third overall. According to the latest annual survey by Cap Gemini and Merrill Lynch, the number of families with over \$30m in investable assets has also risen rapidly, to 77,500, as has that of millionaires (defined as people with investable assets of at least \$1m, not including their main home), now 8.3m worldwide against 7m in 1997.

In the technology industry, there are now several generations of newly wealthy people who are actively giving—the Hewlett and Packard families, Intel's Mr Moore,



Mr Gates, eBay's Messrs Omidyar and Skoll and the newest billionaires on the block, Google's Messrs Page and Brin. Likewise, in the financial industry newly super-rich hedge-fund stars are following in the philanthropic footsteps of Mr Soros. Performance-based donations to charity are now sometimes built into a hedge fund's structure. For example, one-third of all the fees earned by the Children's Investment Fund, one of Europe's leading hedge funds, goes to a foundation that helps children in the developing world.

In Europe, following in America's footsteps, the gradual emergence of an equity culture has generated serious wealth for owners selling their business in an initial public offering. A fair amount of this money is going into charitable foundations. In Germany, for instance, their number has increased from 4,000 in 1997 to over 13,000 now. Germany's best-known charitable foundation, Bertelsmann, which is now mentoring some of these newcomers, says that half the founders are actively involved in their foundations, which for many have become a second career. In America, the number of private charitable foundations has soared from about 22,000 in the early 1980s to over 65,000 today, according to the Centre on Philanthropy at Indiana University.

In India, where traditional charitable giving within communities has dwindled because of urbanisation, those newly enriched by the country's technology boom are starting to fill the void. The wealthy bosses of Infosys, Wipro and Dr Reddy are becoming big philanthropists, joining more established Indian business philanthropists such as the Tata, Birla and Bajaj families.

In Latin America and Asia, "whoever has got wealthy...has now got an agenda to give," says Martin Liechti of UBS, a Swiss bank. He points out that a generational shift is under way from the old wealthy, who tended to practise traditional charity, to the new wealthy, who are open to more entrepreneurial approaches.

Although in many countries the poor give away a higher proportion of their total income than do the rich, it is the wealthy who dominate charitable giving. In America, for instance, families with a net worth of \$1m or more accounted for 4.9% of the total number of all donations to charitable organisations in 1997, but as much as 42% of the value, according to a study by Paul Schervish of Boston College. The concentration in bequests is also striking: estates worth \$20m or more made up 0.4% of their total number but 58% of their value.

In most countries, total giving has been rising slowly, although the outpouring of public sympathy after a series of natural disasters made 2005 a bumper year for donations. Surveys show that in many countries the public's trust in charitable organisations is falling, and there are growing worries that donations will not be put to good use.

According to an annual survey, Giving USA, total charitable giving in America in 2004 rose by 5% to a record \$249 billion, over 2% of GDP. That was more than in any other big country, both in absolute terms and as a proportion of GDP. And even if you ignore donations to religious congregations and add in the value of volunteering, America is still a global leader in giving. A study led by Lester Salamon of Johns Hopkins University of charitable giving in 36 countries, excluding donations to religious congregations, showed that in the seven years to 2002 such giving in developed countries ranged from around 1.85% of GDP in America to 0.11% in Italy.

Mr Salamon also notes that measured against state spending on welfare, charitable spending is tiny everywhere. In America, such welfare spending equals 18% of GDP; in Britain, 28%. This shows just how hard it will be for the new philanthropists to ensure that their money makes a real impact, especially in rich countries.

According to an adviser to a leading Swiss private bank, around one-quarter of its super-rich clients are already committed to philanthropy. A further 40% are ac- ▶▶

Generosity writ large

America's top 20 philanthropists

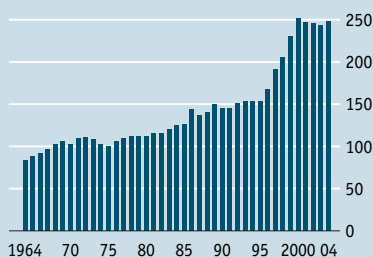
	Background	Amount, \$bn*
Gordon & Betty Moore	Intel co-founder	7.05
Bill & Melinda Gates	Microsoft co-founder	5.46
Warren Buffett	Berkshire Hathaway CEO	2.62 [†]
George Soros	Investor	2.37
Eli & Edythe Broad	SunAmerica, KB Home founder	1.48
James & Virginia Stowers	American Century founder	1.21
Walton family	Family of Wal-Mart founder	1.10
Alfred Mann	Medical devices	0.99
Michael & Susan Dell	Dell founder	0.93
George Kaiser	Oil & gas, banking, real estate	0.62
John Templeton	Investor	0.56
Ruth Lilly	Eli Lilly heiress	0.56
Michael Bloomberg	Bloomberg founder, NYC mayor	0.53
Veronica Atkins	Widow of Robert Atkins	0.50
Jeff Skoll	Founding president of eBay	0.49
Ted Turner	CNN founder	0.46
Kirk Kerkorian	Investor	0.45
Donald Bren	Real estate	0.45
Pierre & Pam Omidyar	eBay chairman, founder	0.43
Patrick & Lore Harp McGovern	IDG founder	0.37

*Given or pledged during 2001-05

[†]Includes a \$2.5bn bequest by his deceased wife Susan Buffett
Source: *Business Week*

A fashion for giving

Total giving* in the US, \$bn
2004 prices



*By individuals, bequests, foundations and corporations
Sources: Giving USA Foundation; The Foundation Centre

▶ tively thinking about it, and another 15% are just starting to put it on their agenda. What motivates them?

Religion has always played a big part in giving (Christians, Jews, Muslims and Sikhs all traditionally aim to give away a set proportion of their income). In America, religious giving accounts for a staggering 62% of total donations, according to Indiana University's Centre on Philanthropy Panel Study, and donations to religious causes outweigh those to non-religious ones in every income group. In Europe, religious giving is generally lower. In Britain, a recent study by the Charities Aid Foundation, a non-profit body, found that faith-based organisations accounted for 10% of the 500 largest charities' income. Among the super-rich of the Muslim world, the Islamic prohibition of things such as alcohol, pork, gambling and conventional financial services has opened up a role for philanthropy: those whose portfolios include such activities can "purify" them by giving the resulting profits away.

"The rich are trying to figure out a moral biography of wealth, and philanthropy can provide part of the purpose side of living the good life," even if you are not religious, reckons Mr Schervish. Becoming very rich can rob you of your old ambitions and give you a need for new ones. Why did Sir Tom Hunter, a Scottish retail entrepreneur, become a philanthropist? "Aged 37, I got a massive cheque. I had achieved all my goals at that time. So I started to think, what shall I do now?"

"There is a search for a narrative, about making a difference with your life, which is vaguely religious and gives you a buzz," says Charles Handy, a management guru who is putting the finishing touches to a book about philanthropy in Britain, "Beyond Success: The New Philanthropists". Mr Handy points to Abraham Maslow's

hierarchy of needs, and suggests that nowadays more people are getting to the stage Maslow described as "the highest need, for a purpose beyond ourselves. They want to make a difference—it used to happen in their 60s and 70s, now it is in their 30s and 40s."

Faced with the world's many and urgent problems, a lot of wealthy people are asking themselves: if I can help, why not? Mr Gates read a World Bank *World Development Report* and realised he could do something to improve public health in the world's poorest countries. That made it seem absurd to leave his philanthropy until old age, as he had previously intended.

A lot of giving is stimulated by personal experience. Wealthy people often want to show gratitude for something that helped them succeed, such as a school or a supportive community. Similarly, they may want to support a life-saving hospital or play a part in finding a cure for a disease that has afflicted someone close to them, or help a poor country they have visited. Indeed, newly wealthy Americans often give to causes abroad, says Mary Duke of HSBC, a bank. Promoting education and fighting disease and poverty in Africa are now high priorities. The Middle East too is rising up the agenda, in hopes of improving America's battered image in much of the region. So-called "diaspora philanthropy"—where people from, say, Mexico or India who have prospered abroad, send gifts home—is also increasingly popular.

Many rich people feel that they have been fortunate and want to "give something back". But eBay's founder, Mr Omidyar, dislikes the phrase. "The classic business executive reaches his late 40s and says I want to give back. But what does that mean he has been doing? Taking away? What a sorry way to think about your career," he says. It is hard to tell whether some of the new wealthy feel guilty, but certainly many of them think, like Carnegie, that philanthropy is part of a social contract: both a duty and an insurance policy against populist redistribution.

Social norms and peer pressure clearly play a part. The fund-raising events in London laid on by Mr Busson for his charitable foundation, Absolute Return for Kids (ARK), seem to be prising open the wallets of many people in hedge funds who would not have contributed otherwise. And not everybody's motives are lofty: Ms Fulton, the co-author of a new report on philanthropy, argues that "a lot of philanthropy is motivated by pleasure—ego gratification and reputation enhancement."

Good examples can help to stimulate largesse. In Britain, the Beacon Prize, launched in 2003 to celebrate philanthropists, was an attempt to reverse a long stagnation in giving. There are signs that, slowly, British culture may be changing. "There is a mood now in Britain that there are niches that the government doesn't fill, and that if you have talent, money and time you should get into these gaps. Thirty years ago, a businessman would have said, 'I pay my taxes, the government should do it,'" says Mr Handy, the management guru. "It is getting like America—if you are wealthy, you want to be on the giving list as well as the rich list."

In continental Europe, a tradition of giving anonymously (not least to avoid the taxman's attention) has meant there is less peer pressure to give, and few role models for would-be new philanthropists. To help change that, Ise Bosch, a member of the family behind the eponymous electronics company, is now writing a "how-to" book on philanthropy. She has also formed a network called Pecunia for wealthy German women interested in giving.

Transcendental meditation

Many baby-boomers, with their children through college, their houses paid for and plenty of money tucked away for retirement, are now beginning to think about their legacy, which often involves philanthropy. "In an age where everything is up for sale, transcendence can be bought through philanthropic giving," argued a working paper, "Strategic Legacy Creation: Toward a Novel Private Banking Proposition", published by the University of St Gallen, Switzerland, in 2004. "While a bank cannot make people literally immortal, it can...create legacies for its clients that satisfy their need for transcendence," ac- ▶▶

International benefactors

The largest foundations in America and Europe

	Assets, \$bn*
Bill & Melinda Gates Foundation (US)	28.80
The Wellcome Trust (Britain)	18.82
The Ford Foundation (US)	10.69
J. Paul Getty Trust (US)	9.64
The Robert Wood Johnson Foundation (US)	8.98
Lilly Endowment (US)	8.59
Fondazione Cariplo (Italy)	8.27
Fondazione Monte dei Paschi di Siena (Italy)	7.13
W.K. Kellogg Foundation (US)	6.80
The William & Flora Hewlett Foundation (US)	6.49

*Financial years ending 2004
Sources: The Foundation Centre; foundation reports

According to the author, Maximilian Martin, now a philanthropy adviser at UBS.

Certainly, people tend to become more generous as they grow richer, both in life and in death. Mr Schervish points out that between 1992 and 1997 the value of final estates in America rose by 65%, but charitable bequests went up by 110%. For the largest estates, the shift was even greater. One possible explanation is the growing concern of wealthy parents that if they leave too much to their kids, they will give them a nasty dose of “affluenza”, also known as “trust-fund baby syndrome”. “A lot of people say they are not going to pass on much of their wealth to their kids, for fear of spoiling them,” says Joe Toce of HSBC. “But as they get older, and grandchildren come along, they often end up passing on a lot to their descendants.”

Nevertheless, when the baby-boom generation dies, vast amounts of money will be passed on, and a large chunk of that seems destined for philanthropic purposes—not least because involving children and grandchildren in the running of a foundation is increasingly seen as a way to give them a sense of purpose and to pass on family values.

Self-interest

A secondary motive may be the desire to take advantage of the many tax incentives and other fixes that can make a wealthy person look virtuous at an appealingly low cost. America has the most generous treatment of charitable giving, allowing



taxpayers to deduct their donations from their taxable income.

In Britain, too, the tax system has become much more philanthropy-friendly. Other parts of Europe are following slowly. The European Foundation Centre is lobbying for better tax treatment throughout the European Union. A particular concern is the harsh tax regime that some countries apply to giving abroad.

The recent tax reforms in Britain have not changed the tendency to give out of income rather than assets, in sharp contrast to the Americans, says Les Hems of the Institute for Philanthropy in London. There is currently no British version of America’s popular “charitable remainder trust”—a device that allows a donor, say, to give away his house, claim an immediate tax

break and then continue to live in it until his death, when the remaining value of the asset goes to the designated charity.

One of the strongest trends in American philanthropy in recent years has been the rapid growth of donor-advised funds, offered by money management companies such as Fidelity, whose fund is now America’s fifth-biggest charity. These funds allow individuals to commit themselves to a donation and claim their tax deduction, but defer nominating a beneficiary and actually paying out the money until a later date. This has led Congress to suspect foul play—though not by Fidelity, which has a decent average pay-out rate of 25% of donated money each year.

Would scrapping inheritance tax, as President George Bush wants to do, hit charitable giving in America by removing one of the main penalties for not giving? Judging by how vigorously charities have been lobbying against the move, they clearly fear that they would lose out. But John Whitehead, a former boss of Goldman Sachs and now the *eminence grise* of New York philanthropy, believes that even if giving carried fewer tax advantages, it would not fall by as much as people fear, for “most of it is from the heart, not the pocketbook.”

At any rate, many people reckon that philanthropists’ motives are beside the point. As Mr Gregorian of the Carnegie Corporation says, “Why they give is not important; the act of giving, and how effectively they give, is what matters.” ■

The birth of philanthrocapitalism

The leading new philanthropists see themselves as social investors

“RELATIVE to the corporate environment, we are in the 1870s. But philanthropy will increasingly come to resemble the capitalist economy,” predicts Uday Khemka, a young Indian philanthropist and a director of the SUN Group investment company owned by his family. Like many of the new generation of philanthropists, he has big but well-defined ambitions. “I want to help develop the infrastructure of philanthropy,” he says.

The need for philanthropy to become more like the for-profit capital markets is a common theme among the new philanthropists, especially those who have made their fortune in finance. As they see it,

three things are needed for such a philanthropic marketplace to work.

First, there must be something for philanthropists to “invest” in—something that, ideally, will be created by “social entrepreneurs”, just as in the for-profit world entrepreneurs create companies that end up traded on the stockmarket.

Second, the market requires an infrastructure, the philanthropic equivalent of stockmarkets, investment banks, research houses, management consultants and so on. This is what Mr Khemka wants to concentrate on.

Third, philanthropists themselves need to behave more like investors. That means

allocating their money to make the greatest possible difference to society’s problems: in other words, to maximise their “social return”. Some might operate as relatively hands-off, diversified “social investors” and some as hands-on, engaged “venture philanthropists”, the counterparts of mainstream venture capitalists.

All this may sound fine in theory. However, the history of philanthropy suggests that there are many potential pitfalls.

America’s early charitable foundations were built by entrepreneurs. Carnegie and Rockefeller would have understood the new investment-oriented model. “Having seen their own economic activity trans-

The good company

CORPORATE giving has long had a reputation as the sleaziest corner of philanthropy. Although usually nominally independent of the companies whose names they take, corporate foundations in practice are often treated as a sort of slush fund into which the chief executive can dip to help a pet cause, enhance his status in the community or even cement a business relationship with a donation to a cause close to a business partner's heart. Corporate philanthropy has been coming under greater scrutiny since the collapse of Enron, because many people believed that donations to various Enron board members' good causes may have made them less willing to hold the firm's top executives to account. Companies are now having to work harder to justify their philanthropy on strategic grounds.

The best justification, and perhaps the only intellectually rigorous one, is that philanthropy is in the enlightened long-term interest of shareholders. This is a key argument in a new book, "Compassionate Capitalists: How the Leading CEOs are Doing Well by Doing Good", by Marc Benioff, the boss of salesforce.com. The book contains two dozen articles by captains of industry, including Alan Hassenfeld of Hasbro, Jeffrey Swartz of Timberland, Steve Case of AOL, Michael Dell of

the eponymous computer-maker and Jean-Pierre Garnier of GlaxoSmithKline. All of them argue—some more convincingly than others—that their philanthropy is good for shareholders, at least in the long run. Mr Benioff argues that giving his staff time to volunteer in the community improves his company's ability to recruit top talent.

Corporate philanthropy is also becoming more important in developing countries, where firms may feel the need to support local communities by contributing through their foundations to health care, education and so on. In an article in a new book, "The Accountable Corpora-



Is corporate philanthropy worthwhile?

tion", Messrs Porter and Kramer note that Nestlé, for example, now invests a lot in what it calls "milk-production systems" in developing countries, realising that a decent infrastructure is needed to ensure a reliable supply.

"The dominant trend in corporate philanthropy is to do giving that reinforces a firm's core strategy," argues Trevor Neilson of the Global Business Coalition on HIV/AIDS. Thanks to shareholder pressure, increasingly the only acceptable philanthropy is the sort that enhances profits. Mr Neilson is a keen advocate of "cause-related government relations", which means that a firm will help a government to deal with a social problem in the hope of getting favourable treatment in the future. For example, 26 companies so far have made commitments to help the Chinese government with its AIDS strategy, which Mr Neilson says will allow them to form a valuable relationship with the government. Perhaps.

Some of the new philanthropists believe that they are doing good simply by running their business. Thus, Mr Omidyar argues that eBay does its bit by empowering people and promoting trust between strangers. Most importantly, it is creating wealth to be shared around. After all, without wealth-creation there would be no chance of philanthropy.

form the world, they thought that the foundations they left behind would be transformative organisations," says Carl Schramm, head of the Ewing Marion Kauffman Foundation. Those foundations did remarkable things. Set up as conduits for making grants as well as running the programmes that would benefit from the money, they thought big, concentrated on clear goals and were willing to invest heavily for long periods to achieve them, says Mr Schramm. The Rockefeller Foundation, for example, found a cure for yellow fever and drove the "green revolution" in agriculture. Carnegie, among other things, built thousands of public libraries.

Yet this long-term investment ethos has proved to be the exception, not the rule. In a landmark article, "Philanthropy's New

Agenda: Creating Value", published in the *Harvard Business Review* in 1999, Michael Porter and Mark Kramer described widespread flaws in America's foundations that mostly remain to this day. For instance, little effort is devoted to measuring results, and foundations have unjustifiably high administration costs.

Michael Bailin, head of the Edna McConnell Clark Foundation, has described the typical foundation as "autocratic, ineffective and wilful, elitist, cloistered, arrogant and pampered". There are "chronic problems in the way foundations operate", says Joel Fleischman, former head of the unusually impressive Atlantic Philanthropies, who is writing a book on the successes and failures of foundations. He says that most of them provide little in-

formation about what they do, and are particularly secretive about their failures. As a result, says Mr Fleischman, "foundations keep reinventing the wheel."

As for foundation governance, it is a nightmare, says Robert Monks, a veteran campaigner for better corporate governance: "Perpetual existence, no need to conform to competitive standards, it is all too much for human nature. Hence the palatial offices, fancy conferences and increasingly lavish pay for the professional philanthrocrats."

Arguably the biggest problem is the way that foundations make grants to organisations they support. Whereas Carnegie was willing to invest for the long term, more recently foundations have tended to chop and change, says Mr Fleischman. Me- ➤

► lissa Berman of Rockefeller Philanthropy Advisors argues that there is too much emphasis on funding individual programmes and too little on the sustainability of the non-profit organisation running the programme. Overheads are seen as a bad thing, and grants tend to be short-term.

Should the new generation of philanthropists try something different from the traditional foundation? Ebay's Mr Omidyar thinks so. He has folded his Omidyar Foundation into Omidyar Network, which is free to make for-profit investments as well as philanthropic donations to pursue its mission of "individual self-empowerment". "After a few years trying to be a traditional philanthropist, I asked myself, if you are doing good, trying to make the world a better place, why limit yourself to non-profit?" he explains. Although there is a separate chequebook for the foundation, his "investment team" is free to put his money in either for-profit or non-profit projects. The team's main criterion is whether the investment will further the social mission.

Similarly, the Google Foundation is part of Google.org, which can mix for-profit and non-profit investments. However, unlike Omidyar Network, Google.org is an arm of Google, so this is corporate philanthropy—which raises a further series of difficult questions (see box, previous page).

In principle, large foundations should be the most effective vehicle for philanthropy, argue Messrs Porter and Kramer. Not only are they free from both political and commercial pressures, they also employ professional staff that smaller outfits would not be able to afford. But the staff often become the biggest problem, especially in foundations whose founder has long been dead.

The new philanthropists are mostly young enough to be able to keep an eye on their foundations for many years to come. Nonetheless, says Mr Fleischman, they might consider setting a closing date for their foundation. For instance, the John M. Olin Foundation, a big source of finance for conservative organisations, recently shut itself down. As John Miller recounts in his new book, "A Gift of Freedom", Olin had stipulated that all of his legacy should be spent within a generation of his death, a sunset model that kept it nimble, unburdened and true to its founder's ideas.

The new philanthropists also need to be clear what they want to do, and stick with it. That is one lesson from the Gates Foundation, which has already notched up some remarkable achievements—



helped by its huge size, which allows it to do things that are beyond everyone else. Its clear mission is to tackle global health inequalities in six main areas: infectious disease, HIV/AIDS, tuberculosis, reproductive health, global health strategies and global health technologies.

Leverage is all

Crucially, it has found ways of using its money to the greatest effect. Mr Gates's big idea is to overcome the market failure afflicting poor consumers of health care by deploying his money on behalf of the poor to generate the supply of drugs and treatments they need. For instance, the money provides market incentives for drug companies to put some of their resources to work for the needy.

The Gates Foundation also favours partnerships, even though it is big enough to pursue many projects on its own. Again, it is looking for maximum effectiveness. Other philanthropists are following similar strategies. For instance, Britain's Dame Stephanie Shirley wanted to fund research into an autism gene, the total cost of which she reckoned would be £1 billion (\$1.7 billion). She stumped up £50m herself and is raising similar sums from other donors around the world. Another "hot" idea at the moment, championed by the x-Prize Foundation, is to donate large cash prizes that will generate lots of further spending from those competing to win them.

Mr Omidyar recently donated \$100m to Tufts University to invest profitably in providers of microfinance to the poor. He hopes to attract private capital to turn what has largely been a subsidised business into a profitable one, operating on a far bigger scale than today.

Other new philanthropists are piloting new models for welfare provision that, once they have proved themselves, can be taken up by governments and made available much more widely. Governments tend to be risk-averse, whereas philanthropists are free to take whatever risks they

like with their money, so they can play a useful role as providers of start-up risk capital for government services.

Networks, too, are an increasingly popular way of leveraging money and experience. Peggy Rockefeller Dulany's Global Philanthropists Circle brings together about 50 super-rich families from 20 countries to exchange ideas and experiences, mainly with a view to finding solutions to international poverty and inequality. Often this will involve the use of connections and influence as well as money.

However, there is still a lack of global giving consortiums that take on single issues, says Mr Khemka. He hopes to bring together philanthropists from around the world who want to tackle climate change.

Some foundations are now exploring new ways of funding organisations. Mr Salamon of Johns Hopkins University thinks that they should start to behave more like philanthropic banks, offering a range of financial products such as loans and loan guarantees as well as grants.

Some philanthropists are also beginning to think about how best to harness all their assets to the causes they support, rather than just concentrating on the money they are currently giving away. This point was brought home recently to Jeff Skoll, one of whose philanthropic missions is to make films with a social message. His latest film is based on the book "Fast-Food Nation"—yet he had not checked his investment portfolio to see if he owned shares in food companies such as McDonald's that are attacked in the film.

Over the past year or so, many of the super-rich have started to ask themselves what exactly their assets are doing, says D.K. Matai, an Indian-born software entrepreneur who runs the Philanthropia Trinity, another international network of philanthropists. "What is the point of earning a high return in China if my money is helping to build Dickensian working conditions? If I have \$5 billion, and am giving \$4 billion away, do I really want a 17% return ►►

► on activities that are wrecking the world?" To deal with that problem, the investment industry will need to improve on the strategies and products it currently offers for "ethical" or "socially responsible" investment, which often amount to little more than avoiding shares in, say, tobacco, arms manufacturing or oil.

The phrase most often used to describe the new approach to giving is "venture philanthropy". This was first used in the 1960s by one of the Rockefellers, but is still practised relatively rarely. Perhaps the best example is a firm called Venture Philanthropy Partners. Run by Mario Morino, who made his fortune in software, it specialises in mid-sized non-profit organisations in the Washington, DC, area that work well enough, but lack the capital and talent to expand. With a \$30m fund raised through a community foundation, Mr Morino behaves much like a venture capitalist. He is working intensively with 12 non-profit organisations, helping them to develop a business plan for growth and to recruit managers and board members.

Old dogs, new tricks

New foundations may be learning from the mistakes of the old ones; but what can be done to reform established foundations that are underperforming? With America's Congress showing increased interest in foundations, Senator Charles Grassley has proposed tough new laws. His reforms would "dramatically transform the relationship between the federal government and foundations", says Adam Meyerson of the Philanthropy Roundtable, an industry body. Among other things, Senator

Grassley is proposing a five-yearly review of foundations' charitable status and a formal government ratification regime. But Mr Meyerson thinks it would be far better for the government properly to enforce the laws that are already in place.

Better regulation is on the agenda in Britain, too, where charity is still governed by an act passed in 1601. "The governance of charities and non-profits is generally poor," says Geraldine Peacock of Britain's Charity Commission, which under new legislation due to take effect this year will become much more independent of government. Like Senator Grassley, Ms Peacock thinks that a charity should be licensed for a limited time—say five years—and then have to reapply.

Encouragingly, many of the older foundations themselves are becoming more concerned about effectiveness, and have started demanding more information on how the money they provide is spent, says Mr Fleischman. The recent transformation of the Edna McConnell Clark Foundation shows that an inefficient old organisation can turn itself into a cutting-edge operation. It used to hand out grants in the traditional manner for a wide range of good causes. But in the late 1990s, a new head, Mr Bailin, decided to concentrate its activities in a single field, youth development. Working closely with its chosen organisations, notably Harlem Children's Zone, it has helped them become more effective and serve many more people.

The biggest question of all is how to measure the performance of a philanthropic organisation. A huge amount of work is going on in this field, but it is still

more art than science—particularly when it comes to the fuzzier goals of some philanthropists, such as "empowering people", "increasing the effectiveness of civil society" or "fighting climate change".

Measures involving the so-called double bottom line (financial plus social performance) or triple bottom line (financial, social and environmental) are readily susceptible to statistical manipulation. So are popular concepts such as "changed life"—a combination of the number of people affected by an initiative and the extent to which it improves their lives.

One danger is to pay too much attention to managing inputs, which are easier to measure than output. Another is to concentrate donations on those activities that can be easily measured, such as the number of vaccinations given, even where that may not be the most effective way of tackling a problem.

Donors also need to strike the right balance, so that on one hand they ask for enough information to be able to monitor the effectiveness of the organisations they fund but on the other they do not bog them down in form-filling bureaucracy. The Gates Foundation has a good reputation for getting the mix right and tailoring it to individual circumstances.

"The risk with any metric is that people will come to see it as a description of reality, rather than a tool for a conversation about that reality," says Rowena Young of the Skoll Foundation. "One metric or another can function well only when managers know why they are measuring and for whom...In the world of social value-creation, context is king." ■

The rise of the social entrepreneur

Whatever he may be

UBS, a Swiss private bank that counts many of the world's richest people among its clients, is conducting an interesting experiment in Brazil, Mexico and Argentina. It has formed an alliance with Ashoka, a global organisation that identifies and invests in leading "social entrepreneurs". The alliance is offering a new prize for social entrepreneurship, which UBS's Martin Liechti admits is an excuse to bring together two groups of people who might otherwise never meet. "As the biggest wealth manager in the region, we are at the

crossroads between capital and ideas—so why not bring the people with capital together with the people who have ideas?"

The social entrepreneurs that are short-listed must have been working successfully with Ashoka for at least three years. Winning the prize is not really the point. Simply being selected to be in the room with a bunch of wealthy people gives the social entrepreneurs great credibility with potential donors, and even runners-up have a good chance of coming away with a new financial backer or some other form

of help. Héctor Castillo Berthier, who runs an innovative project for troubled Mexican teenagers, came third in last year's Mexican prize, but still got a crucial donation and free use of office space.

Ashoka is not alone in bringing social entrepreneurs together with the wealthy and powerful. Social entrepreneurs now rub shoulders with the world's business and political elite at the World Economic Forum in Davos, under the auspices of a sister organisation to WEF, the Schwab Foundation for Social Entrepreneurship. ►►

Shining examples

Leading social entrepreneurs

5

	Organisation	Nationality	Background
Jeroo Billimoria	ChildLine India Foundation	India	Children's rights
Somsook Boonyabancha	Community Development Institution	Thailand	Land rights
Peter Eigen	Transparency International	Germany	Anti-corruption
Oded Grajew	Instituto Ethos	Brazil	Citizen sector
David Green	Project Impact	United States	Public health
Alice Tepper Marlin	Social Accountability International	United States	Labour
Pearl Nwashili	StopAIDS Organisation	Nigeria	Public health
Fabio Rosa	IDEAAS	Brazil	Renewable energy
Orri Vigfusson	North Atlantic Salmon Fund	Iceland	Environment
Muhammad Yunus	Grameen Bank	Bangladesh	Microfinance

Source: Ashoka

▶ This year, the people selected included Rory Stear, founder of Freeplay, a company dedicated to the spread of cheap, sustainable energy for all; Jim Fruchterman of the Benetech Initiative, a non-profit organisation that makes technology available to disadvantaged communities; and Victoria Hale, founder of OneWorld Health, which works with the Gates Foundation (among others) to make low-cost drugs available in poor countries.

Waiting for a productivity miracle

Ashoka was founded in 1980 by Bill Drayton, a former McKinsey consultant, who expects the rise of social entrepreneurship to generate huge benefits. He says it is now helping to bring about a productivity miracle in what he calls the "citizen half of the world" (education, welfare and so on), a sector that for three centuries has lagged behind the "business half of the world", where productivity has soared and vast amounts of wealth have been created thanks to its competitive, entrepreneurial culture. The emergence of more social entrepreneurs, and their improved access to growth capital as they get better connected to philanthropists, is creating enormous productivity opportunities for the citizen sector, argues Mr Drayton.

The citizen sector is defined somewhat loosely, but is largely made up of government plus the non-profit sector. Both government and non-profits have traditionally been run inefficiently. The productivity miracle detected by Mr Drayton is due both to a shift from government provision to more efficient private provision (by both for-profit and non-profit organisations) and by an increase in the efficiency of the non-profit sector.

The improvement in non-profit organisations' efficiency may still have some

way to go. In 2004, Bill Bradley, a former presidential hopeful for the Democrats, and two McKinsey consultants claimed in an article in the *Harvard Business Review* that, in America alone, there was a "\$100 billion opportunity" for the non-profit sector to improve its efficiency through better management. But is social entrepreneurship the best way to achieve that?

There is no easy answer, not least because nobody is sure what exactly the term means. In a book charting the rise of social entrepreneurship, "How to Change the World: Social Entrepreneurs and the Power of New Ideas", David Bornstein notes that most discussion of social entrepreneurship tends to revolve around "how business and management skills can be applied to achieve social ends". He himself sees social entrepreneurs as "transformative forces: people with new ideas to address major problems who are relentless in the pursuit of their visions". The late management guru Peter Drucker, typically quick to spot the trend, defined social entrepreneurs as people who raise the "performance capacity of society".

Mr Schramm of the Kauffman Foundation, which promotes a better understanding of entrepreneurship, says that being an entrepreneur means being a risk-taker, but a high risk of failure may be the last thing that many non-profits need. And, surely, "every entrepreneur is a social entrepreneur," says Mr Schramm. "A successful entrepreneur...creates wealth—and without wealth there is no surplus capital to turn over to charitable activity."

Mr Omidyar, too, is uncomfortable with the label, which he feels implies a disapproval of profits that he does not share. "I think of myself as an entrepreneur, and I have a social view, but I don't call myself a social entrepreneur," he says. But his fel-

low philanthropist from eBay, Mr Skoll, thinks social entrepreneurship has something going for it. The mission of his eponymous foundation is "to advance systemic change to benefit communities around the world by investing in, connecting and celebrating social entrepreneurs".

Among other things, Mr Skoll has endowed the Skoll Centre for Social Entrepreneurship at Oxford University's Saïd Business School. This is part of a growing trend for academic institutions, including nowadays most business schools, to take the phenomenon seriously. Harvard Business School started teaching a course on social enterprise 12 years ago.

Mr Schramm worries that some of these courses are more likely to turn students against capitalism. But Mr Whitehead, a former Goldman Sachs boss who is the driving force behind the HBS course, sees it as part of a trend among the elite in many countries who increasingly want to make not just money but "a difference". The money may not be as good as in business, but "a bright young person can have more of an impact on any non-profit in his first five years than on Goldman Sachs, which is full of bright young people. In their first year they could make ten suggestions that would improve the non-profit operation because they have been trained in practical business ways of thinking."

People like you and me

Certainly the number of business-school graduates going into the non-profit sector has increased. That appeals to the new philanthropists, who want to see people like themselves in charge of the non-profit organisations they support. But these new professionals may achieve as much by using the latest management techniques to improve the performance of existing non-profit organisations than by creating new ones through social entrepreneurship.

Mr Collins, the management guru, says getting the right people is arguably even more important in the non-profit world than it is in business, because it is often harder for non-profits to get rid of employees once they are "on the bus". Business leaders can fire people more easily and can spend money on buying talent. But some social entrepreneurs have found their own ways of securing top talent. Wendy Kopp, who in 1989 founded Teach for America—a non-profit organisation that gets graduates from top universities to spend the first two years of their careers teaching children from low-income families—made it clear from the start that only the best would do. ▶▶

► By last year, over 97,000 people had applied to work for her organisation, but only 14,000 had been accepted. Ms Kopp's ability to pick and choose boosted her credibility with her philanthropic backers and enabled her to raise more money.

A growing number of non-profits now have state-of-the-art marketing departments. Indeed, it can sometimes seem that the marketing has become more important than the mission. One technique is to use "charity muggers" on commission to collar people in the street and get them to sign a standing order. For a while this was used in Britain by Oxfam, but the development charity now thinks that raising money this way does not pay. Far better to tap into the public's concern about where its charitable donations are going, as Oxfam has done with its hugely successful Christmas gift catalogue, offering gifts such as sponsoring a goat in an African village for £24 or providing safe water for 1,000 people for £720. "The public want to be transactional, to have a more direct relationship with where their money is going," says Barbara Stocking, Oxfam's boss.

Many non-profit organisations have been wary of working with big donors because their money can come with too many strings attached. But that is starting to change. Oxfam now wants to raise more money from the sort of wealthy philanthropists it has not targeted in the past—only because in Britain there haven't been many of them, says Ms Stocking. "I'm not sure we have been asking for enough money," she muses.

But the main problem for many non-profit organisations is how to get bigger. "One of the problems is that well-run non-profits don't necessarily grow," says Nigel Morris, the co-founder of Capital One, a credit-card company. True, growth isn't everything. Indeed, Mr Collins worries that non-profits will put scale before genuine effectiveness: "One of the markers of mediocre companies is that they become obsessed with scale and growth," he says. But donors need to decide if they simply want to buy services from a non-profit, or whether they want to invest in helping the organisation grow. If growth is important to them, they need to become a lot less squeamish about overheads.

The virtue of overheads

"In the business sector, people are very comfortable with the idea of investing in an organisation, and the need to build up its infrastructure. In the social sector, the tendency is to invest only in a programme; there is very little investment in building organisations," says Mr Collins. Yet often, in yielding to public pressure to keep down overheads, "non-profits sacrifice efficiency for virtue," says Carnegie's Mr Gregorian.

There is no merger-and-acquisition market in the non-profit world. And for all sorts of reasons, there are far too many non-profits. Philanthropists could help by encouraging consolidation, says John Studzinski, co-head of HSBC's investment bank and an active philanthropist. "In homelessness work, I'm a great advocate

of consolidation. There are about 40 homelessness projects in London; only eight are any good," he says.

There is also a role to be played by philanthropists in encouraging non-profits to develop other sources of finance, to reduce their dependence on the goodwill of donors. Providing fee-generating services is one strategy. Doing work for the government is another. Many non-profits have long generated revenues in this way.

Philanthropists can even encourage non-profits to move towards becoming for-profits, able to stand entirely on their own feet. This is what Mr Omidyar hopes to achieve with his \$100m donation to Tufts University to invest profitably in microfinance. But the idea may face a lot of cultural resistance. "How do you get the citizen sector to change its attitudes so that it allows institutions to have incomes that are at least equal to outgoings?" asks Ashoka's Mr Drayton.

He is now trying to promote for-profit partnerships between big companies and community groups in some of the most impoverished parts of the world. "Working with both sides, we map a new value-added chain, ranging from product design to production to distribution to servicing; that delivers a far better service to the ultimate customer faster, better and more economically. Ending centuries of non-communication brings so much value that both business and citizen groups emerge as huge winners as well," he says.

For example, community groups in Mexico's slums now work with Cemex, a huge cement firm, to create a market for its cement among the slum dwellers, greatly reducing the cost of adding extra rooms to their dwellings, providing funds for the non-profit groups and turning a (still small) profit for Cemex. The social entrepreneurs running the community group have the trust of the locals without which the big company would never be able to enter the market, says Mr Drayton. Other similar "hybrid value-added chains" that combine business and social purposes are being developed between groups of forest-dwellers and forestry firms, and small farmers and irrigation companies.

Meanwhile, Ashoka hopes that its relationship with UBS will flourish, and that prizes will soon be awarded across Latin America and Asia. But as well as highlighting the growing role of social entrepreneurs, this experiment also points to another new trend: a more active role for intermediaries in the emerging philanthropic capital market. ■



Virtue's intermediaries

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 en-

able 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 £22,000-48,000 (\$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 £2.9m, topping up £1m 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.

The man responsible for the capital injection, George Overholser of Non-Profit Finance Fund Capital Partners, reckons 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 Family 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. ■

Faith, hope and philanthropy

What the new breed of donors can do—and what it can't

THE growing enthusiasm of the rich for philanthropy, together with their determination to see their money used to better effect, has prompted talk of a new “golden age of philanthropy”. But much remains to be done before today's beneficent billionaires can claim to follow in the footsteps of such giants of giving as Carnegie, Rockefeller and Rowntree.

The willingness of so many of the new wealthy to apply part of their fortune to “making the world a better place” is certainly welcome. True, there are questions to be asked about what exactly is motivating them, and whether they are doing the right things to tackle society's problems. Yet philanthropy, free of the short-term pressures from voters and shareholders that constrain governments and for-profit companies, may be one of the best hopes for solving problems such as the spread of AIDS, poverty and climate change.

The new philanthropists rightly insist on making their money go further, because in the past a lot of donors' cash has been wasted. One way of introducing more leverage is to adapt elements of the capital markets for use in this sector. Many innovative businesses have sprung up to provide some of the infrastructure of this new philanthrocapitalism. But in the absence of market forces, much giving remains less effective than it should be.

To-do list

To improve matters, the first thing that is needed is better measurement of the impact of philanthropy. When Carnegie built libraries, or the Rowntrees and Cadburys built social housing, it was easy to see the benefits with your own eyes. But how do you know whether Omidyar Network is achieving its goal of helping “more and more people discover their own power to make good things happen”? Mr Davies, the co-founder of New Philanthropy Capital, concedes that measurement is difficult, but insists it is not impossible: “Some of these things from an economic point of view are unmeasurable, but no more so than measuring GDP in the service sector, which we do, though it is very hard.”

The second requirement is greater transparency. There are still far too many

philanthropists trying to do the same thing, often unaware that they are duplicating each other's good works. More transparency would help to avoid wasting scarce resources and promote consolidation in parts of the sector. Failures also need to be more frankly acknowledged, so that philanthropists can learn from each other's mistakes.

Compared with the resources of governments and businesses, philanthropic capital is still tiny, so it needs to be used with the utmost care to ensure that it will make a real difference. Yet many of the activities funded by philanthropy do not add much value and could be funded by more risk-averse investors, such as the state.

That said, some of the new philanthropists are doing their best to use their money in innovative ways which, if successful, could then quickly be scaled up by government or business. Indeed, a growing number of them recognise that the best way to attract the capital needed to achieve scale quickly is to find potentially profitable ways of solving problems.

The third thing that is needed to make philanthropy better is greater accountability. Democracy and plutocracy do not sit comfortably together, and even when donors' money is being spent in non-democracies, the democratic world is likely to take a growing interest in what is being

done. The new philanthropists will have to get used to public scrutiny, cynicism and even active hostility—together with a good dose of *Schadenfreude* if and when their schemes fail.

This should not surprise them. They are, after all, making increasing use of mass-marketing and public campaigns to support their causes, as Bono did with his initiatives “Make Poverty History” and “One” around last year's G8 summit, seed-financed by Mr Gates and Mr Soros. The flip side of that is the risk of an equally high-profile public backlash if they do not deliver. But they should persevere, not least because they are far likelier to make an impact if they can get the public on their side. And even if some of their projects do not come off, many will.

One way in which these new philanthropists are already making a difference is by improving the running of a big chunk of society—charities, non-profits, non-governmental organisations and the social sector—where amateurishness and inefficiency used to be the norm. They are introducing the best techniques from business and ensuring that market forces are being given a much bigger role. This amounts to an industrial revolution in what Rockefeller called the “business of beneficence”. It has only just started, but rich and poor alike should hope that it succeeds. ■

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