

June 11, 2010

Nonprofits eye private investments as donations dwindle

PUGET SOUND BUSINESS JOURNAL (SEATTLE)

The deep recession and a growing desire to align investments with social missions is prompting nonprofit organizations to look to a new source of funding — social venture capital.

Although nonprofit organizations and private businesses have been overlapping in recent years, the participation of private investment with positive returns has remained one of the few ways to distinguish between the two.

But even that line between business and nonprofits is blurring as new financial options become available to the nonprofit sector.

“This is the thing that everybody is thinking about,” said Bookda Gheisar, executive director of Global Washington, a consortium of organizations focused on international development that will convene a forum later this month on using commercial strategies to advance development goals. “Funding is shifting, and nonprofits have been really forced to think about new sources of revenues.”

While tax-exempt organizations are prohibited from returning profits to directors, they are familiar with generating returns. Nonprofit groups must report to donors or funding partners on how their donations achieved mission results, which is commonly called impact.

But the recession is prompting fundraisers to rethink their capital sources. In 2009, giving by foundations, corporations and foundations fell 3.2 percent, the largest reduction ever recorded, according to the June 9 report of Giving USA, a clearinghouse for national data.

The potential to tap into the trillions of dollars controlled by credit and equity markets — some with social missions — has nonprofit organizations dreaming of breakthrough possibilities to accomplish their own goals. But investment capital is limited to opportunities that meet specific risk and return criteria, and some wonder if nonprofit organizations can secure, put to work and then repay these private investments.

To be sure, microfinance groups are among the most successful segment of the nonprofit sector to tap investor capital. But Rick Beckett, CEO of Seattle-based microfinance group Global Partnerships, says any nonprofit that generates a cash return, whether it is in health, environment, education or conservation, could potentially tap investor dollars.

Several nonprofits and socially motivated businesses have secured investor funding, including:

— Seattle-based nonprofit VillageReach formed a joint venture called VidaGas to distribute propane in Africa and ensure a reliable energy source for refrigerators to cool vaccines. VidaGas was started with a \$1.4 million investment by a Luxembourg-based venture fund.

— Everett-based EarthWise, a for-profit venture, is raising \$2.4 million to build ferries to service African commuters. Rob Smith, the venture’s founder, expects a return of 7 percent for investors, according to reports.

— Trilogy, the cellular phone company founded by wireless executive John Stanton, has received an undisclosed amount of funding to build out a network in Haiti.

Nonprofits are finding ways to make their tax-exempt status mesh with private investors. Some nonprofit groups form separate limited liability corporations or joint ventures that are subject to tax laws and distribute returns to investors or back to the nonprofit, which then plows that money back into its mission-related work. Other investors are directing their donor advised funds, typically held by a community foundation, to be invested with socially responsible businesses, organizations or funds.

Powering the trend is a growing desire by investors to use their money to earn social returns.

continued on next page

Nonprofits eye private investments as donations dwindle *continued*

The Bill & Melinda Gates Foundation joined many other charitable foundations earlier this year when it announced it would invest a portion of its \$35 billion endowment in so-called “program related investments” that generate a financial and social return.

“That is one of the things I have been pushing on for a while,” said Jeff Keenan, an investor who has put \$100,000 of his own portfolio into Global Partnerships funds.

Experts say nonprofits and socially motivated businesses must offer market competitive products to investors before they can count on collecting investment dollars.

Global Partnerships, for example, designed its latest fund to offer four “tranches” or segments that deliver different levels of risk and reward. The first tranche in the \$20 million fund is worth \$1.5 million and was largely given by donors to serve as a loss cushion for more senior investors who expect a 3 percent and 4 percent return.

“What you do by creating a fund structure this way is you create an opportunity to absorb all the risk at the bottom (donated funds that serve as a loss reserve) and create very low risk and very well managed and diversified investments for the investors at the top of the fund. What that creates is a variety of ways for people to invest depending on what their objectives are,” Beckett said.