CHARTING THE NEXT WAVE OF EQUITABLE FINANCE:

PROCEEDINGS DOCUMENT

Yale SCHOOL OF MANAGEMENT
International Center for Finance

Yale SCHOOL OF MANAGEMENT
Program on Social Enterprise

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Introduction

Finance is the lifeblood of households, organizations, and the economy. It has been the driver to expand economic opportunity and justice, and the cause of countless economic hardships and exploitation. Over the past three decades, a diverse and dynamic field that applies finance to advance the common good and advocate for policies and practices that protect consumers from financial harm has grown exponentially in size, complexity, cross-sectoral partnerships, and impact. It is precisely because of this extraordinary progress in practice and in volume of transactions, dedicated funds, and media awareness that the financial gaps facing nonprofit organizations and social enterprises stand out more vividly.

One of the gaps with the most profound implications for financial health, performance, and impact of the social sector is how we attract, grant, invest, structure, and price equity—the foundation on which both the simplest and most complex debt instruments rest, as well as how the capital markets offer individuals affordable opportunities to build wealth. Equitable finance encompasses a set of financial products that provide nonprofits and social enterprises with flexible capital—both in the form of equity and subsidized debt—that funds the essential organizational infrastructure and finances those activities necessary to achieve their missions. This gap is also one of the most enduring: the philanthropic sector has largely not risen to the visionary call made by Clara Miller (founder of the Nonprofit Finance Fund and former President of the Heron Foundation) in 2003 to provide "philanthropic equity" as a tool to build financial strength and resilience for nonprofits in pursuit of social and economic impact. In addition, the impact investment field has increasingly moved away from offering patient equity to social enterprises in the start-up and scaling stages.

In this time of unprecedented wealth inequality—especially for communities of color—how we structure and invest financial equity also has enormous implications for how we advance economic equity. Private sector financial markets and corporate finance have solutions to offer if we link these solutions with an understanding of how financial tools and practices must be adapted to serve people and places now left of out or behind mainstream markets.

The opportunity is ripe to reflect on what we have accomplished and where we can go together—which is the focus of an initiative that has grown out of my time as an Executive Fellow at the Yale School of Management (SOM). The fellowship is hosted by the International Center for Finance (ICF), led by William Goetzmann, and benefits from a partnership with the Program on Social Enterprise (PSE), led by Tony Sheldon.

On October 4, 2019, ICF and PSE jointly hosted a convening that included philanthropists, impact investors, nonprofit and social venture leaders, and academics to share their perspectives and recommend capital and policy strategies to expand access to philanthropic equity and equitable finance. This proceedings document shares the insights from the participants at the convening with the goal promoting understanding and action. Thank you for joining us!

Andrea Levere
Executive Fellow
International Center for Finance
Yale School of Management

Note on Equitable Finance Convening Report

The International Center for Finance (ICF) at the Yale School of Management fosters leadership in the understanding, practice and management of finance from multiple perspectives in alignment with the Yale School of Management's broader perspective of business for the benefit of society. We are hosting Andrea Levere as an Executive Fellow to inform the design and delivery of products that can meaningfully increase the availability and investment of equitable finance. This project explores how equity investments in both nonprofits and social ventures can build wealth at both the individual and community level, a topic that is a priority at the ICF. We view equity ownership as an essential tool in addressing major social challenges, including inequality and lack of economic mobility. Our future depends on our ability to broaden ownership among the many, not the few. Charting the Next Wave of Equitable Finance offers a major step towards this goal, and we are pleased to be part of this proceedings document.

William N. Goetzmann
Edwin J. Beinecke Professor of Finance and Management Studies
Faculty Director, International Center for Finance
Yale School of Management

Since its founding, the Yale School of Management's mission has been "to educate leaders for business and society." The career of Andrea Levere, Class of 1983, has exemplified this mission. Andrea's work has focused unrelentingly on developing innovative and effective tools to expand economic opportunity for all. In her decades of work at Prosperity Now, she has led the creation a complex and resilient web of bridges across multiple spheres: between communities and banks, between philanthropy and researchers, between grassroots organizations and national institutions, across governments at the local, state and federal levels – all in service of expanding economic opportunities for under-served communities. Andrea's fellowship at Yale SOM has continued this work by exploring new ways to fuel the flow of equity – social and financial – into institutions that build shared prosperity. The October 2019 convening described in this report represents another weaving together of ideas and perspectives across multiple stakeholders committed to this vision. Our hope is that it serves as both a summary of the current state of the field and as a springboard to further and deeper work by us all.

Tony Sheldon
Executive Director, Program on Social Enterprise
Lecturer in the Practice of Management
Yale School of Management

The Convening: Charting the Next Wave of Equitable Finance

Convening Goals

The International Center for Finance (ICF) and the Program on Social Enterprise (PSE) at the Yale School of Management hosted a convening that brought together leading philanthropists, investors, practitioners, and academics to collaboratively explore how we might "chart the next wave of equitable finance" to support strategies to advance social, economic and environmental equity.

The one-day convening sought to accomplish the following goals:

- Craft a shared narrative to advance the case for equitable finance.
- Frame organizing principles and assumptions to define the role of finance in advancing a more equitable economy.
- Assess the current state of the marketplace for philanthropic equity and equitable finance and how these can be a force for constructive change.
- Develop a collective vision to move forward through working groups focused on systems change at various levels.

Convening Design

- **Rules of Engagement:**
    - *Share diverse perspectives:* Participants came from a variety of backgrounds and represented organizations with different objectives, stakeholder expectations, programs, and business lines.
    - *Encourage healthy debate:* Although participants shared a common goal to work towards equitable finance, their approaches differed on how to achieve this goal, sparking spirited conversation and engagement.
    - *Commit to confidentiality:* Participants shared their ideas openly and pledged not to share information or opinions externally that were attributed to specific participants or organizations. Social media was not permitted.
- **Participants:** The 32 participants (List attached in Appendix A) were invited to reflect diversity in practice, commitment to equitable finance, demonstrated innovation in their careers, willingness to share ideas and availability. They represented a range of institutions and sectors, including non-profit social ventures, foundations, community development financial institutions (CDFIs), corporate philanthropy, banking, consulting, impact investing, and academia.

Convening Agenda Structure

The agenda was designed to facilitate reflection, catalyze new ideas, and mobilize participants to action (Agenda attached in Appendix B). To frame the discussion, sessions were structured with opening remarks from participants followed by responses designed to capture a variety of perspectives across diverse stakeholders. Once formal responses were offered, the sessions were opened for a general discussion. Specific readings were suggested as background for the participants to create a shared understanding of the issues to be addressed. (Readings listed in Appendix C).

The agenda included five sessions:

1. Trouble in Paradigm: Let's Put the Equity Back into Finance
2. The View from the Marketplace: The State of Supply and Demand
3. Structuring Equity into the Capital Markets
4. Building Inclusive and Efficient Markets for Equitable Finance
5. Closing Remarks and Next Steps

Trouble in Paradigm: The Case for Equitable Finance

> *"If we want philanthropy to stay relevant in today's 21st century world let alone rise to the level of its soaring rhetoric, we must revolutionize our 19th century business model, operating precepts and conceptual frameworks to be fit for purpose. For owners and investors of significant stores of capital, the changes needed will involve a revolution of capital."*
>
> Clara Miller - *"A Revolution of Capital"*

The conversation opened with a ground rule to "avoid our default mode of good news and positive stories." Our goal for the day was to describe "the nonprofit reality show for the 21st century." The nonprofit and philanthropic sectors alone are inadequate to the task of accomplishing the change we seek, and we should adapt the wisdom of Willie Sutton: pursuit of social and economic justice occurs only when we go "where the money is."

We acknowledged that **the status quo is no longer sufficient.** There is a glaring disconnect between mainstream philanthropy's balance sheet investing and programmatic giving. The disconnect is driven by a siloed mindset that we must protect the "make money" side of the institution from the "do good" side. Marginal improvements are not enough. Instead of simply "planting small seeds of good in seas of bad" we need to rethink the tools and products that shape the status quo in order to address the root causes of the problems we are trying to solve.

We identified **four core principles** that are essential to expanding access to equitable finance:

1. Champion a more integrated approach to the deployment and investment of philanthropic assets, exposing the separation of grant-making from the use of the endowment as a false dichotomy.
2. Discard our field's attachment to the brand of "specialness" which has created a siloed, insular and marginal industry in need of new approaches to consolidation and collaboration. We need to discard "bespoke metrics" that are useful only to a few funders.
3. Adapt the "language" of accounting to reflect the financial realities of our business model in a way that all stakeholders can understand. The field must educate capital providers about real and perceived risk. Even when investments in the social sector can provide risk-commensurate returns, they often struggle to attract balance-sheet capital from banks and philanthropies.
4. Leverage this moment of inflection in the private sector (e.g., the recent Business Roundtable declaration) to influence its investment and partnership practices.

As Paul DiLeo describes in Paved with Good Intentions, the traditional way of thinking - that financial returns and impact must remain separate - gives rise to a *"mindset and a conventional wisdom that justifies waiting to make impact investments, or treating impact as the expendable stepchild of 'real' investing: maybe okay to have around if it doesn't get in the way. However, this inadvertent or deliberate demotion of the impact side of the double bottom line needs to be persistently challenged.*"

View from the Marketplace: The State of Supply and Demand

> *"Without access to some form of equity-like capital, nonprofits are pretty much sentenced to difficult, unhealthy, or slow growth. Beyond money, they lack supporters who take the protective role of the equity holder, even among board members. Everyone wants the nonprofit to do more, especially when opportunity knocks and additional revenue pours in, and the organization struggles with extreme pressure, given a too-small production capacity (think Disney's masterpiece, the cartoon The Sorcerer's Apprentice, where the Sorcerer's broom enacts ever-increasing demand giving rise to out-of-control operations in the hands of an inadequate head count and skill set!). When intractable problems emerge in the face of success, it's confusing to many nonprofits and their supporters, who view increased revenue as growth, and think, "Mission accomplished—we're having more impact."*
>
> Clara Miller - Growth, Equity, and Looking at Nonprofits as Enterprises

State of Supply: The current design of the nonprofit and philanthropic capital markets shapes the opportunities and the barriers that we face. The convening identified **four core characteristics** of the current marketplace:

1. The types of capital available to nonprofits is complex and the **market for this capital is primarily organized by relationships, not public markets**. This creates an uncertain operating environment, which often requires nonprofits to reverse engineer their business models to meet the demands of donors and investors, potentially resulting in perverse incentives that compromise sustainability and impact.
2. Current philanthropic practices **rarely fund the true cost of doing business** or seek to engage the whole enterprise—although there are some promising signs that major foundations are rethinking how they fund "overhead." As organizations without built-in wealth structures, nonprofit operations are too often compromised by the failure to fund them in ways that produce profits. We need to move away from thinking of breaking even as "success" and recognize that **generating surplus drives impact.** This surplus will allow organizations to invest in the talent and technology needed to build resiliency and sustainable results.
3. Nonprofit organizations solve problems that conventional markets cannot or will not solve. This requires capital that understands this reality and prices accordingly in recognition of the need for subsidy. The task is to **mainstream the "but for" argument** by educating financiers to recognize this purpose to bridge market gaps and so better match the structure of their financing to this business model.
4. Nonprofit organizations—as with early stage companies—often operate at a loss in the early years or in periods of dramatic growth. Philanthropic equity is essential at these stages of development. But many social ventures can become profitable over time, opening the doors to investment by dividend-paying equity or other private market instruments. We need the capital markets to **understand that profitability is a multi-stage process** and adapt their products to this business cycle.

"When markets fail to produce a set of broad-based and sustainable public goods, we need a more visible hand: concerted efforts by governments, multilateral agencies, philanthropies, and increasingly, socially minded investors to meet needs and solve problems."

Georgia Levenson Keohane – [Capital and the Common Good]

State of Demand: To change and influence the markets to increase the flow of equitable finance, we must begin by leveraging our own capital to move market perception and expectations, while also engaging with philanthropy and the public sector to target each source of funds to its highest and best use.

Three lessons emerged on how best to advance market change:

1. **Transform our business model from a "storage to a shipping business."** We need to communicate better that we are providers of crucial products and services and not simply custodians of funds. We need to improve how we demonstrate, measure, and communicate that value to donors and investors. Our narrative needs to be tailored in a way that donors and investors can hear so that they will help us develop new financing methods that are better suited for our business models.
2. **Create demand for the change that we produce.** Markets are driven by demand, but we need to illustrate how the "status quo is stupid and expensive" and our strategies are more aligned with the products and services of the future. Instead of spending trillions of dollars trying to address the consequences of poverty, we need to spend money on tackling the root causes. We need to "move from fighting fires to prevention." Too often we fear being perceived as "expensive" by funders, but our work can lead to significant *savings* in the long run. We must coalesce around compelling narratives about the impact and importance of the work we're doing. CDFIs are doing the work that funders seek and have more than 40 years of data demonstrating the strength of their financial performance, yet they still struggle to attract equity. This shouldn't be the case.
3. **Increase our investment in policy change.** To secure the amount and type of funding and investment commensurate with the problems we aim to address, we need to leverage resources of the public sector and direct them to invest where the private sector and philanthropy can't or won't go**.** While there is too often a lack of faith in the government's ability to deliver solutions, our history demonstrates that major initiatives to address poverty often start and end with the public sector. We need to design, advocate and implement policy solutions that accurately address the realities of the 21st century economy.

<u>Structuring Equity into the Capital Markets</u>

William Goetzmann, Edwin J. Beinecke Professor of Finance and Management Studies and Faculty Director of the International Center for Finance at the Yale School of Management, shared highlights from a book he is working on. This book presents an argument for using stock ownership as a mechanism for addressing some of society's fundamental challenges: inequality, the savings crisis, social immobility, slow economic growth, and political partisanship. Widespread equity investment is a way to share the benefits of economic growth. We need to broaden the public stake in the world's productivity by:

1. **Creating a globally available, low-cost diversified world equity portfolio.**
   The cost of U.S. index funds and ETFs has been decreasing for several years and they allow

U.S. investors of comparatively modest means to invest in an incredibly broad portfolio of world equities. A globally diversified portfolio allows investors to participate in company profits and future growth regardless of geography.

2. **Requiring large companies to issue shares in public capital markets.**
   This gives outside investors the same opportunity to benefit from corporate performance as inside owners.
3. **Requiring open access to venture investment opportunities.**
   This would allow all investors access to transformative opportunities by getting in on the ground floor of new ideas, products and technologies. While venture investments are inherently risky, individuals would often be better off being angel investors in speculative new ventures in this era of extraordinary innovation than playing the lottery.
4. **Developing lending programs for long-term equity investors.**
   There are currently government programs that allow low-income families to buy houses using their homes as collateral. Why not create similar lending programs for the stock market?
5. **Creating tools for direct exchange of labor for equity.**
   This would help entrepreneurs and workers directly exchange what they have and what the other needs. It is also a way to reduce costs and create opportunities at an early stage of a startup.
6. **Designing opt-in and opt-out access to equity investment.**
   We should nudge people into making equity investments because investors who keep their money in cash are giving up potential returns. Inertia is one of the biggest mental challenges to overcome in promoting savings. We automate participate in 401(k) savings vehicles. Why not promote other kinds of default equity investments?
7. **Overcoming crash fears.**
   We need to change the narrative on investing so that people are less worried about a market crash. This requires re-focusing investment performance reporting on the economic source of value in the stock market – dividend and earnings growth rather than stock price – and reconfiguring our risk assessment of stock market crashes by understanding the true probability of such an event.
8. **There are many social notions of equity or fairness.**
   In Goetzmann's view, they fall into four broad categories: equal rights, equal access, universal safety net, and equal outcomes. The equitized world envisioned in the book has already been proposed by the Capital Asset Pricing Model, whereby everyone has access to the same set of investments, everyone shares information about them, and everyone has the same "exposure" to them. Equitization, as proposed in the book, puts the economic benefits of the means of production into investment accounts of workers and managers alike. It does not discourage growth and innovation; it simply provides fair, widespread access to it.

Building Inclusive and Efficient Markets for Equitable Finance

> *"Widespread equity investment is a way to share the benefits of economic growth. We typically think of equity as a way of financing an enterprise – a way to raise capital for a business from investors. However, equity investment can also be seen as a tool for spreading the wealth."*
>
> William Goetzmann—*Equity*

Building more inclusive and efficient markets for equitable finance starts with re-thinking how we collaborate. We must consider the incentives to work together and the way we organize around clearer, standardized impact outcomes. The following principles and examples from the field illustrate the elements of a marketplace we aim to create as we journey towards equitable finance:

- **Treat financing as a means to an end.** We must start with programmatic strategies, not capital strategies. Too often, we start with financing strategies, creating a transactional approach to the solution of foundational problems and a disconnect between sources and uses of funds. JPMC Foundation is assessing the continuum of capital needs to determine how to create a product suite that matches capital to purpose and fills gaps in the marketplace through its own investments and by aggregating capital with other funders and investors. The Pittsburgh Capitalization Fund is investing capital to change organizational culture, increase financial resilience, and expand the influencers who can strengthen the flow and use of equitable finance. Their experience underscores the importance of capacity and culture and demonstrates how much time and effort this organizational culture change requires.
- **Highlight the role of philanthropic equity in achieving sustainable organizations and outcomes.** For example, encourage others to adapt the standard of the BUILD Program of the Ford Foundation of devoting 40% of a grant portfolio to operating or flexible, enterprise-level capital, with the goal of aggregating multiple sources of funds.
- **Standardize our products to attract greater supply.** The financial markets need us to simplify our products in ways that increase volume and scale**.** Current efforts to innovate with equity-like instruments has produced added complexity that may be contributing to the challenge of raising adequate amounts of capital by the sector. How can we define our capital needs in ways that better reflect products in the mainstream capital markets?
- **Build champions among the obvious and the unlikely to raise visibility.** Highlight the role of influencers in the market, both those who have been long-time partners and those who might be in the future. Encourage them to influence friends and strangers by focusing on our role in solving the problems that people care about. It's important that people see social sector organizations as agents of change on problems that matter and hear about it from people they trust.
- **Advance public policy.** Connect the grassroots to the grass-tops to build support for policy changes at the local, state and federal levels that provide the unrestricted and catalytic capital necessary to grapple with the full range of problems addressed by the sector.

Closing and Next Steps

During the closing session**,** participants offered a robust set of next steps they believed could expand access to equitable finance and begin to address the insights and recommendations generated during the convening. These included:

- **Research:** Continue research on the design and delivery of products that can meaningfully increase the availability and investment of equitable finance. Invest in outcome and impact measurement that reflects the complexity of the field while creating common messages and metrics.

- **Philanthropic Investments:** Create an Equitable Finance Funding Collaborative in the belief "that philanthropy is impact investing." Reach out to new sources of funds, such as pension funds, to invest in this work.
- **Policy:** Organize a policy working group to discuss how policy change can support innovation.
- **Communications:** Promote narrative change in ways that appeal to friends and strangers. Organize a network of "first movers" able to define our value and create demand building on the belief that we should "never let a good crisis go to waste."
- **Racial Equity:** Integrate a racial equity analysis into everything we do and leverage the analyses and movement within philanthropy and the social sector to target funding in those communities facing the largest wealth gaps.
- **Convene:** Organize a panel on Equitable Finance and a workshop focused on creating a new asset class for philanthropic equity at the Yale Philanthropy Conference, February 14, 2020 at the Yale School of Management.

Ideas, questions or recommendations? Please contact Andrea Levere, Executive Fellow, International Center for Finance at the Yale School of Management, andrea.levere@gmail.com.

Appendix A: Participant List

Paul Bradley
ROC USA, LLC

Colleen Briggs
JPMorgan Chase & Co.

Kathy Buechel
The Benter Foundation

Ellis Carr
Capital Impact Partners

Judy Chevalier
Yale School of Management

Leigh Ann Clark
Yale School of Management

Elizabeth Davidson
Yale School of Management

Frank DeGiovanni
Ford Foundation *(Emeritus)*

David Erickson
Federal Reserve Bank of New York

Joe Evans
The Kresge Foundation

Electra Ferriello
Yale School of Management

Bryan Fike
Yale School of Management

Michelle Gilliard
Venture Philanthropy Partners

William Goetzmann
Yale School of Management

Paul Goldsmith-Pinkham
Yale School of Management

Kathryn Greenberg
KG Consulting

Mary Houghton
Expanding Black Business Credit

Georgia Levenson Keohane
Navab Capital Partners (NCP) Foundation

Amir Kirkwood
Opportunity Finance Network

Anika Singh Lemar
Yale Law School

Andrea Levere
Prosperity Now *(Emerita)*,
Yale School of Management

Clara Miller
Heron Foundation *(Emerita)*

Dan Nissenbaum
Low Income Investment Fund

Neela Pal
Goldman Sachs Foundation

Don Schwarz
Robert Wood Johnson Foundation

Tony Sheldon
Yale School of Management

Alexandra Sing
Yale School of Management

Abigail Suarez
JPMorgan Chase & Co.

Heather Tookes
Yale School of Management

Nate Wong
Beeck Center for Social Impact + Innovation

Vicky Zhang
Yale School of Management

Appendix B: Convening Agenda

Charting the Next Wave of Equitable Finance
A Participatory Convening
Yale School of Management
Evans Hall |165 Whitney Avenue | New Haven, CT
October 3-4, 2019

October 3, 2019

6:30 pm **Drinks and Dinner**
ROÌA Restaurant and Cafe
261 College St, New Haven, CT 06510

October 4, 2019

8:15 am **Shuttle departs The Study Hotel for Yale School of Management**

8:30 am **Registration and Breakfast**
Beinecke Room, Second Floor, Evans Hall, Yale School of Management

9:00 am **Welcome, Goals and Introductions**
William Goetzmann, *Yale School of Management*
Tony Sheldon, *Yale School of Management*
Andrea Levere, *Prosperity Now (Emerita)*, *Yale School of Management*

9:45 am **Trouble in Paradigm: Let's Put the Equity Back into Finance**
Clara Miller, *Heron Foundation (Emerita)*

Respondents: Where is Philanthropy and Investing Today?
Ellis Carr, *Capital Impact Partners*
Joe Evans, *The Kresge Foundation*
Michelle Gilliard, *Venture Philanthropy Partners*

Moderator
Georgia Levenson Keohane, *Navab Capital Partners (NCP) Foundation*

10:50 am **Break**

11:00 am **The View from the Marketplace: The State of Supply and Demand**

The Nonprofit Perspective
Kathryn Greenberg, *KG Consulting*
Neela Pal, *Goldman Sachs Foundation*

CDFI/Social Venture Perspective
Paul Bradley, *ROC USA, LLC*
Dan Nissenbaum, *Low Income Investment Fund*

A View of Systems Change: How to Restructure the Marketplace
David Erickson, *Federal Reserve Bank of New York*
Amir Kirkwood, *Opportunity Finance Network*

Moderator
Judy Chevalier, *Yale School of Management*

12: 15 pm **Lunch**
"Equity"
William Goetzmann, *Yale School of Management*

1:30 pm **Building Inclusive and Efficient Markets for Equitable Finance**

Platforms for Equitable Finance: Continuum of Products for Community Development
Colleen Briggs, *JPMorgan Chase & Co.*

Greater Pittsburgh Small Arts Capitalization Program: Philanthropic Equity in Practice
Kathy Buechel, *The Benter Foundation*

The Lessons from Development Finance: From Shorebank to the Expanding Black Business Credit Initiative (EBBC)
Mary Houghton, *Expanding Black Business Credit*

Respondents
Frank DeGiovanni, *Ford Foundation (Emeritus)*
Paul Goldsmith-Pinkham, *Yale School of Management*
Nate Wong, *Beeck Center for Social Impact + Innovation*

Moderator
Tony Sheldon, *Yale School of Management*

2:50 pm **Break**

3:00 pm **Summary, Next Steps and Commitments**
Andrea Levere, *Prosperity Now (Emerita)*, *Yale School of Management*
Tony Sheldon, *Yale School of Management*
Don Schwarz, *Robert Wood Johnson Foundation*

4:00 pm **Reception**
1st Floor Ligon-Lamsam Student Commons

Appendix C: Background Readings

Readings:

- Clara Miller: Capital, Equity and Looking at Nonprofits as Enterprise
  https://nonprofitquarterly.org/capital-equity-nonprofits-enterprises/
- Paul DiLeo: Paved with Good Intentions
  https://www.grassrootscap.com/paved-with-good-intentions/
- Clara Miller: A Revolution of Capital
  https://www.alliancemagazine.org/analysis/a-revolution-of-capital/
- Georgia Levenson Keohane: Capital and the Common Good