

Journey into Brazil's Social Sector

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The founder of the first social fund in Brazil tells his story

BY LEONARDO LETELIER

OVER THE PAST DECADE, the social sector in Brazil has undergone a growth spurt. In 2002, the Instituto Brasileiro de Geografia e Estatística, the government-led national statistics bureau, counted 276,000 NGOs. By 2005, there were 338,000, a quarter of which were religious organizations. The current estimate is that Brazil is home to more than 400,000 nonprofits, excluding religious ones.

According to the same census, however, 74 percent of nonprofits, including hospitals and universities, have no paid employees and only 6 percent have more than 10 staff. In 2009, the Brazilian Association of NGOs (ABONG) polled its members and found that only 20 percent have annual budgets of more than \$1 million. In addition, the foundation sector in Brazil is weak. Most foundations are corporate foundations, with no endowment and strong ties to the original businesses—and offer very little support to social enterprises.

So there is good news about civil society activity in my country, but there is also concern about how sustainable and effective the social sector really is. Can several hundred thousand organizations with no paid staff and little funding provide the support and services that many of Brazil's 190 million citizens desperately need?

I have always been interested in the public good. During college, at the Industrial Engineering School in São Paulo, I worked for Brazil's antitrust agency. As an analyst at McKinsey & Company, I discovered Ashoka and did pro bono projects for several social entrepreneurs. At Harvard Business School, I enrolled in every possible social enterprise course and then returned to McKinsey, where I continued to consult for social businesses in my spare time.

If you ask Brazilian executives what they want to do when they retire, many will say "Open an inn at the beach." The social sector was my eventual inn at the beach. But that plan changed in 2005 when a friend asked, "If you were offered a job at the Clinton Foundation at your current salary, would you take it?" I replied with a resounding "Yes!" What startled me was how instinctively I answered. It wasn't until I was considering two equally appealing but different job offers—at a European private bank establishing operations in Rio and at a digital-inclusion nonprofit with more than 900 schools—that I realized everybody would be better off, especially me, if my business skills were used for social impact. It was then I decided that social entrepreneurship, and more specifically social finance, was my calling.

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FOUNDING SITAWI

Three insights helped me define what I wanted to do: 1) advice is not enough—many consulting projects for for-profit or nonprofit clients don't yield impact; 2) capital is not enough—many grants do not generate impact either; and 3) more types of capital equals much more capital—there are about 200 times more funds in traditional markets (debt and equity) than in grants in Brazil.

Before I took the plunge I asked myself: What is the worst that can happen? If sitawi fails, I will spend the next two years doing something I love and go back to the corporate world.

The development process took about one year. At the end of 2006, I started the first social fund in Brazil, sitawi, which means to flourish or develop in Swahili. My colleagues and I faced three immediate questions: Who are our target clients? Should sitawi itself be structured as for-profit or nonprofit? And how would we pay the bills?

First of all, we decided that our focus was to provide midsized loans (\$50,000 to \$250,000) to organizations for which social

impact is a core mission and business is the supportive engine. Such organizations don't have access to capital and will be the last to be served by banks. Because most of these social enterprises are non-profits and are less comfortable working with a for-profit fund or bank, we decided to structure the fund as a nonprofit. That would also allow us to receive foundation and donor support.

We aimed to position ourselves somewhere between a foundation and a bank. Whereas a foundation provides grants and other support, a bank provides loans at market-based interest rates. We decided to provide some strategic support—much more than a bank but less than many foundations' capacity-building programs—and integrate this support through the provision of below-market loans. The latter decision was especially important, because market-rate loans in Brazil

fund sitawi were withdrawn. Finally, the Avina Foundation granted us \$250,000, enabling sitawi to formally start the fund.

Since then, we have provided close to \$1 million in loans to eight social enterprises, a mix of nonprofits with business units and for-profits with a clear social mission that promote civil rights and provide health care, social services, and income opportunities benefiting more than 10,000 people. That has been accomplished with a fund turnover of 2.5 times and no default or restructuring of loans. Today, we have much more demand from deserving social enterprises than we can serve.

The other enterprises we have funded are microcredit institution ICC/Banco do Povo (\$250,000), to allow it to expand its reach to more people developing small businesses; community bank

Banco Palmas (\$140,000), to enable it to fund new loans to its best customers; fair marketing handmade product coalition Tekoha (\$65,000), to finance the purchase of raw materials to meet its largest order to date; social investment organization IDIS (\$90,000), to improve the company's

debt structure; and São Paulo poverty alleviation and social service agency Caspiedade (\$330,000 in two separate loans), to make up for delays in payments from government contracts.

The need for our services has been obvious. Davida had a hard time opening a bank account; its crime was to have the word prostitute in its legal name. Banco Palmas uses an official line of credit that has harsh restrictions on late payments, punishing its portfolio as a whole, especially the best customers. Local governments expect Caspiedade to pay taxes on time—even when they don't reimburse the services provided—and otherwise will freeze payments of money owed. It's definitely not easy to run a social enterprise in Brazil!

There is so much to be done to improve the social sector. Nonprofits, especially ones linked to politicians, are repeatedly involved in corruption scandals. The country's tax and legal infrastructure in this area is weak. Although there are several laws that provide tax benefits for donations to arts and sports projects, there is very little incentive for giving to social organizations—and none to help foster social enterprises. Unfortunately, I see more talk than action in those directions.

Sitawi's current focus is on the estimated 20,000 social enterprises and nonprofits for which sales of products or services generate more than 20 percent of income. As the fund grows and we attract more support for operations, the need for consulting, which represented 52 percent of revenues in 2010, decreases.

Over the next five to 10 years, we believe our market-building efforts will have created enough demand to launch a for-profit fund with the same strong social mission focus, one that will attract more capital and visibility to the social impact market. Over time, I see sitawi pioneering new financial products tailored to the social sector, such as loan guarantees, performance contracts, and hybrid products. But, just as in the United States and Europe, there is a long road ahead.

On a personal note, a few years ago I did receive a call from the Clinton Foundation to apply for a position. I respectfully declined, and smiled inside. ■

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have interest rates of 35 to 50 percent, loans that our target clients likely could not get because they lack collateral (a must in Brazil) and banks don't have incentives to understand or support the social sector.

We were joining several other funders that support social enterprises and nonprofits: Acumen Fund, based in New York City, which provides loans and equity; Charity Bank, headquartered in Kent, England, which is a fully regulated bank targeting the social sector; and the pioneer Nonprofit Finance Fund, in New York City, which also provides loans. The difference between sitawi and these funders is that we're creating infrastructure for the social sector specifically in Brazil and for Brazilian social enterprises.

But before sitawi had any funds to lend (or lending revenue to book), we had costs. In 2006, I had recruited two people to help me start sitawi: an entrepreneurial college dropout and a Boston Consulting Group consultant. For the first year and a half, we provided strategic consulting services to companies, foundations, and larger nonprofits, offering advice on "social impact with a business mindset" to make payroll. We talked about social loans as if we did one loan a day. But we hadn't made a single loan: Social entrepreneurs had a hard time thinking about loans, and funders had a hard time considering support of intermediaries like sitawi.

FIRST LOANS

At the end of 2008, we still had no money in the fund, but we had two potential recipients: Daspu, a clothing brand owned by Davida, a prostitute rights association that needed to finance its winter 2009 collection; and Solidarium, a social enterprise connected to Aliança Empreendedora, an organization that provides business support and market access to small artisan associations, which had a large order from Wal-Mart Stores. So I did what entrepreneurs typically do: I put my money where my mouth was and extended the loans myself—credit lines of \$30,000 and \$90,000, respectively. These were simple working capital loans at rates of 1 percent a month (similar to Brazil's central bank base rate) and were repaid within three months.

In 2009, as the financial crisis hit Brazil, several commitments to