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First Person

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Effective Funding

How foundations can best support social innovators

By Steven Lawry

When he was an economics professor at Chittagong University in the 1970s, it occurred to Muhammad Yunus that commercial banks could successfully lend money to poor Bangladeshis even if they lacked the traditional assets, such as titled land and houses, typically needed to collateralize loans. The banks could make loans to small groups of peers and neighbors, and the mutual support and social pressure that occur naturally in such groups would ensure that banks got their money back. Still, in 1981, when Yunus asked commercial bank managers in Bangladesh to capitalize his new Grameen Bank's five-year expansion plan, they all said no. They simply could not get past poor people's lack of collateral.

Yunus realized that he had to reduce the risk to commercial banks of investing in Grameen. So he went to the Ford Foundation's office in Dhaka and asked for an $800,000 loan guarantee fund as security against commercial bank lending. The foundation would never have to dip into the fund, Yunus assured senior staff members. "The fact that it is there will do the magic," he explained. Happily, after careful appraisal by senior staff, Ford agreed to the request, and Bangladeshi banks provided the capital to finance Grameen's expansion to five previously unserved rural districts. Grameen's borrowers repaid their loans in full, the commercial banks got their money back with interest, and the rest, as it were, is history.

I tell this story because I find the partnership between Yunus and the Ford Foundation deeply compelling. First, it demonstrates how private foundations can support risky new approaches to poverty reduction in ways that other institutions—including commercial banks and publicly financed donors such as the U.S. Agency for International Development (USAID)—often cannot. What's more, once these foundation-funded ideas and practices become proven, then banks, governments, and other kinds of donors are more likely to incorporate them into their own work, and to do so in ways that may have far-reaching impact on poor people's lives.

Of course, foundations for which poverty reduction is a priority don't always take advantage of this distinctive ability to support innovative work. But if foundations embrace the following three precepts—which go against their predilections to shape and manage social change themselves—I believe they can successfully invest in social innovation.

Powerful Ideas Come From Outside

First, foundations should open their doors wide to the potentially powerful ideas of people like Yunus—entrepreneurs who come from outside of philanthropy and can test and champion their ideas in the complex social, economic, and political environments in which they live and work. Foundation program staff should constantly search for people distinguished for their powerful ideas and their practical understanding of what it takes to bring about meaningful change in their societies—and then fund their work with the fewest possible constraints. Yunus, for instance, as well as Sheela Patel, the founding chairperson of Shack Dwellers International, and Wangari Maathai, the founder of the Green Belt Movement in Kenya, did not submit funding applications in response to foundation requests for proposals. Rather, they and their colleagues defined the interventions that were most needed and asked foundations and other donors to fund them.

The three innovators' subsequent success suggests that to find good ideas in the outside world, foundation staff should not shape highly specific program strategies. By doing so, they may prematurely reject potentially powerful ideas because they "don't fit" their program. Sometimes the staff's experience itself is the problem. If a foundation commits to supporting microfinance institutions and staffs its poverty division mainly with micro-

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finance specialists, it increases the possibility that future breakthrough ideas for reducing poverty not related to microfinance will get overlooked. A better option: Staff that division with people who have broad knowledge of the country's economy and social relations and who are skilled at tracking trends that may be creating new opportunities for reducing poverty.

Board members, meanwhile, can encourage the foundations they steward to welcome social innovators' ideas. They can convey a passion for innovation and share their knowledge that successful innovations typically emerge only after prolonged periods of trial and error. M.S. Swaminathan, a Ford Foundation trustee from 1989 to 1997, consistently spoke in support of Ford's flexible funding for leaders of women's rights movements when this kind of activism was still controversial and unfamiliar to many large foundations. Among the scientists whose research helped launch the Green Revolution, Swaminathan felt strongly that women's participation in managing farming and other rural enterprises was essential for rural wealth to be equitably distributed. He also saw women's marginalization as a disturbing loss of talent and freedom.

MEASURING IMPACT SHOULD NOT SLOW INNOVATION

In an effort to improve their accountability, some foundations have clarified and tightened internal decision-making processes to reduce the danger of trustee conflicts of interest; set aside resources to support evaluations and impact assessments; and invited beneficiary communities and grantees into discussions about strategy and impact. These efforts are good things: They might give the public greater overall confidence in foundation governance and management, and therefore in foundations' decisions to take risks.

Nevertheless, the growing emphasis on quantitative measures of short-term impact can distract foundation program officers and grantees from fostering the deep, systemic changes often needed to improve poor people's lives. Even though the effectiveness of microlending in helping reduce poverty was measurable, Yunus's greater contribution was in creating a new kind of banking institution dedicated to serving borrowers who had historically been denied banking services, and in convincing banking regulators of its viability. And that took time. Yunus made the first experimental microloans out of his own pocket in 1976, and Grameen was not registered as an independent bank until October 1983.

Evaluations should also assess whether new institutions responsive to the needs of poor people have been successfully established, or if government agencies, companies, and banks have changed their policies and practices in ways that are likely to reduce inequality and neutralize the systemic causes of poverty.

LET GRANTEES TAKE THE LEAD

Much is made of the convening power of foundations. Many in the philanthropic sector believe that foundations' money, independence, and moral authority can bring diverse and sometimes competing institutions to the table on behalf of a larger public purpose. Although this may be true, it is also true that foundations are not in a position to implement systemic change themselves. The heavy lifting is ultimately done by grantees like Yunus, who often work through setbacks and diversions to convince major funders, private investors, policymakers, and regulators of their ideas' merits.

Yunus suffered considerable frustration as a result of his early engagement with the Central Bank of Bangladesh and a number of commercial banks, as some officials of these institutions were endlessly skeptical of his plans' viability. But these encounters deepened his understanding of the obstacles he had to overcome to fundamentally change the banking system. The Ford Foundation would not have been capable of sustaining a comparable effort or of wielding comparable influence. Its contribution lay in providing Yunus the resources to shape a rigorous and ultimately persuasive test of his ideas.

> Few foundations have the resources and the staying power to fund a complex process of social and policy change on their own.

Innovative grantees, who have the advantages of local knowledge, intuitive insights into local social and institutional dynamics, and social and professional standing in their communities, are in a better position than foundations to push and pull the levers that move other essential institutions toward adopting the kinds of pro-poor policies necessary for their ideas to work. Few foundations have the resources and the staying power to fund a complex process of social and policy change on their own. Indeed, Grameen Bank had many funders in addition to Ford in its early years, and Yunus directed donors toward activities he thought they could best support, given their particular program goals and restrictions. Individual foundations, therefore, should cooperate with grantee efforts to package and phase funding, and not complicate it by insisting on "owning" discrete pieces of what are ultimately complicated and highly integrated endeavors. If the larger program proves successful, there will be plenty of credit to go around.

In 1986, Ford's Dhaka office commissioned an evaluation of the foundation's early support for Grameen Bank. In his report, the evaluator, Ken Marshall, analyzed what unexpected challenges and opportunities presented themselves, if objectives were achieved, how many people benefited from the new loan opportunities, and what the effects on poverty reduction were. But in a break with convention, Marshall also commented on how the adaptive and supportive terms of the foundation's support for Yunus might have contributed to Grameen Bank's ultimate success. He wrote, "The foundation's own contribution has been its flexible and timely support that proved critical in enabling Grameen Bank to keep up momentum and to maintain the supportive environment in which creative individuals like Dr. Yunus best flourish."

The terms of a foundation's support for grantees matter. The kinds of far-reaching breakthroughs in practice and policy needed to reduce poverty will more likely happen if foundations provide funding in ways that give fullest possible rein to the ideas and leadership of social innovators like Muhammad Yunus. ■