The Role of PRIs in Creating Scale and Leverage
Presentation to PRI Conference
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I want to thank you all for the opportunity to be here tonight – what a pleasure it is to see so many friends and colleagues in the audience – I am enormously honored that you would ask me to speak to you tonight about future of PRIs and their potential to leverage social benefits. I especially want to thank Asad Mahmood of Deutsche Bank, for personally extending the invitation to me to be with you tonight – Asad has always been a good friend of my organization and I thank him.

I’m honored to follow Frank DeGiovanni – Frank’s overview of the history of PRI making has given us a lot to think about, and is the perfect lead in to my remarks. It’s a challenge to follow someone as smart and eloquent as Frank, so I figured I’d better change the pace of the evening a bit and tell a few stories on Frank. What you probably don’t know is that Frank was my thesis advisor in grad school and was my most thoughtful critic and also my strongest advocate. What I owe him is that – despite a few white-knuckle moments, a few crashing spreadsheets and economic models that didn’t work – he passed me, and I got out of school alive.

Many of you in this room are experienced PRI makers. You have worked hard for the past two decades to build the PRI field. Others have made only a few social investments, and still others have made none at all. Some of you are small foundations, wondering if this tool is relevant to you – others are trying to figure out how to throw more resources into PRIs. Big or small, experienced or inexperienced, what links ALL of us in this room together is a belief in the power of an idea – that capital employed for social purposes can multiply itself many times over. And over the past two decades, that belief has birthed a field in community investing unlike anything else in the world. Especially in my area, community development, you have created an example for others around the globe. The robustness and success of the American community development experience is the direct result of the vision of philanthropists and in many ways, demonstrates the enormous potential of philanthropy when it sticks with its vision.

Let me make this point a little more graphically. If you can, cast back in your mind’s eye to the world of 20 years ago. Twenty years ago, LISC and the Enterprise Foundation were just getting started – small, still finding their way in the world. My organization, the Low Income Investment Fund, had just been incorporated in the State of California and had all of $200,000 in capital under management. The community capital movement was still more idea than reality.

Twenty years ago, I was a young program officer at the Ford Foundation. I made one of my very first PRIs – a $500,000 loan – to the Institute for Community Economics (ICE). As I recommended the investment before the officers of the Foundation, I remember clearly what I said: “ICE is creating network of community-based loan funds and this PRI will be used to seed their creation.” And then, boasting a bit about the scale of this new community loan fund network, I said, “There are 12 of these organizations across the country with $27
million in capital.” At that time, $27 million nationwide seemed like a large and impressive number.

Well, today, we know that there are over 500 community loan funds, with $18 billion in capital nationwide. And my organization, with $200,000 in assets 20 years ago, now manages a quarter of a billion dollars in assets. We have made a half a billion dollars in loans, supporting:

- 50,000 homes for families and kids
- 20,000 safe spaces for children in child care facilities
- and charter schools serving over 20,000 kids of all ages

LIIF has made loans totaling a half a billion dollars, but lost only $192,000 in 20 years.

None of this would have happened without philanthropy – both your vision and resources. Now, we are focused on creating scale in our industry. Now, we are focused on building a bridge between private capital markets and poor communities.

So, the next question is – is there still a role for PRI making? Or, has our field outstripped you? Can you still make a difference, given the magnitude and maturity of the field?

My answer to you is very simple – you are important now for exactly the same reasons you were before. The type of PRIs we will ask you to make will be different, but the reasons are the same. We need you for your vision, your ideas and we need your resources to help us leverage the scale we are poised to reach.

We are confronting a host of new opportunities that come from success, and you are critical to us in getting the ball into the hoop. We will be asking you to be a loss cushion in large scale capital pools that are assembled by multiple organizations, linked together. We will ask you to credit enhance – that’s a fancy word that means guarantee or create a first loss pool – in the sale of our loan portfolios to private investors. We will even ask you to help us open up the cheapest and most robust private capital markets around – those bearing the triple AAA rating of the US government, through Fannie Mae and Freddie Mac.

Even as I speak, a number of CDFIs and non-profit developers have banded together through the Housing Partnership Network to create a $100 million relationship with Freddie Mac, where we can sell our projects. We are looking for PRIs to serve as the first loss cushion – whether we succeed is largely a function of our ability to raise these risk-absorbing funds. Likewise, LIIF is working with Fannie Mae right now on a large scale transaction that does the same thing.

The private sector capital most accessible to us – the banking industry motivated by the Community Reinvestment Act – is regulated. It simply can’t do the types of loans that we do
and still pass muster with its auditors and regulators. So, you have two major trends combining at once:

- We need the scale the private sector offers
- But we are too weird and funky – non-conforming in polite terms – to be accepted by the private sector

This is where you come in. You can help us take the weird, funky, non-conforming community loans that we have proven work and conform this economic flow to terms that match private capital requirements.

Let me explain how this works. I’ll give you a couple of examples, first from the vantage point of a small foundation.

A couple of years ago in New York, LIIF was asked to provide a $2 million loan for a homeless shelter. We could have done this loan on our own by deploying $2 million of our resources. But we had a better idea. We decided to see if we could get State of NY mortgage (SONYMA) insurance for the shelter. This amounts to a guarantee, and if SONYMA guarantees a loan, banks will happily make the loan. So, if we could convince SONYMA to provide a guarantee, LIIF would not need to use its own capital to make the loan. But in this case, the deal was too risky for SONYMA to guarantee. So, we went back and put on our thinking caps. We decided to offer SONYMA a 10 percent guarantee – in other words, we offered to guarantee a guarantee.

That was all SONYMA needed. They provided their guarantee, and LIIF brought in $2 million from the United Methodist Pension fund to build the shelter. At the end of the day, LIIF put up a $216,000 guarantee, but leveraged over $2 million dollars for a project serving very poor, homeless families. That’s 10 to 1 leverage, and a lot of social good.

This is an ideal situation for a small foundation, but it is still investing in individual projects. There is a better way even for small foundations to multiply their dollars many times over.

Imagine the power of several foundations – small and big – joining together to create a guarantee pool. Using the same 10 to 1 leverage ratio, $10 million could leverage a capital pool of $100 million. $10 million is a number that is realistic for philanthropy – $100 million coming solely from philanthropy would be a stretch.

Let me take this example one step further. LIIF is right now assembling a $35 million pool for charter schools. We are using a $1.7 million Department of Education grant (it could easily have been a PRI) as the cushion against losses. That’s more than a 20 to 1 leverage ratio. Citigroup is our lead investor in the pool; Prudential is involved and the Annie E. Casey Foundation is involved. The ultimate result of this will be thousands of low income kids attending high performing schools, receiving a quality education. The financial leverage in this example is huge. The human capital leverage can only be measured in the lives of the kids touched by this opportunity.
And finally, I’ll give you the example of a visionary PRI made by the Packard Foundation to stimulate systems change in child care. Several years ago, LIIF was lucky to receive a sizeable PRI from the Packard Foundation. $1 million of that PRI was to provide a risk cushion to leverage private capital for child care. I’m proud to be able to announce that on January 3, 2006, using the Packard PRI, LIIF closed a $10 million investment from Impact Community Capital – a consortium of insurance companies including Allstate, State Farm, Pacific Life and many others. We combined the Packard Foundation’s leveraging PRI with the New Markets Tax Credit, and I am very pleased to be able to say that this is one of the largest joint commitments by the insurance industry and by philanthropy in child care ever made. And, in part because of this success, today, LIIF is designing a pre-school facilities fund that, assuming the Preschool for All initiative in California passes – as is expected – will leverage nearly $2 billion in public resources.

In this example, Packard provided the spark, Impact provided the fuel, LIIF provided the know-how and, now across the State of California, we are beginning to see change – change in the way that child care is viewed by the private sector, change in the way the child care sector sees itself. But more importantly, this work is changing minds. And after all, changing minds is what causes social systems to change. I predict to you that before too many years go by, we will see this change roll its way through Sacramento and all the way to Washington, DC. The strength of this vision – when philanthropy, the private sector and communities all come together – will change our world as we know it, and change it for the good.

Over the past two decades, we have seen the power of philanthropy when it pursues a vision – in the history of PRIs, as Frank described it – in the history of community capital as I described it. What we need you to do today is to help us step into the next decade for our field. And that means a different vision than in the past – the new vision requires you to accept risk in a different way than before. It is not more risk, but it is risk structured differently. Together, we have proven that the idea of investing capital for social purposes works. We have proven that the idea of investing in communities works. We have taken an idea that started in the 60s with action in the streets and transformed it to capital invested in the creative spirit of neighborhood after neighborhood throughout this country. You have shared our vision and helped us all the way down this path. You have been our prime partners in spirit and commitment. Now, we need your help to take it to the next step: scale and leverage.