



GRAYGHOSTfund

BUSINESSWEEK.COM

Tiny Investments, Big Changes

By Robert Hof

November 4, 2005

eBay founder Pierre Omidyar and his wife are donating \$100 million to create a microfinancing fund to help Third World entrepreneurs

When Pierre Omidyar started eBay 10 years ago, he aimed to help individuals create online businesses that could compete on a level playing field with corporate giants. Today, some 750,000 people make a full- or part-time living by selling on eBay (EBAY). Now, the eBay chairman and wife Pamela are turning their sights to a much bigger group of people — 500 million would-be entrepreneurs in developing countries.

On Nov. 4, the Omidyars are announcing that they're donating \$100 million to Tufts University to create a new fund for microfinance lending initiatives. Microfinance groups typically lend what in the developed world are tiny amounts of money — as little as \$40 — typically to women creating crafts, selling vegetables, and the like. But often, that's enough to get the businesses rolling. Microfinance initiatives now serve some 80 million poor people worldwide, with more than \$7 billion in current loans.

“VIABLE INVESTMENT PRODUCTS.” But while a few microfinance lending organizations are profitable enterprises, such as the Grameen Bank in Bangladesh, most such loans have been funded with philanthropic donations. The problem with that, according to Pierre Omidyar: “If you want to reach global scale — and we're talking about hundreds of millions of people who need this — you can't do it with philanthropy capital. There's not enough charity capital out there.”

The Omidyar-Tufts Microfinance Fund will invest in microfinance banks and possibly in related lending initiatives, such as ratings agencies. The Omidyars hope they can prove that the sector can produce profits while it helps lift people from poverty, thereby making microfinance self-sustaining.

“By connecting with an institutional investor like a university, we would like to increase the level of professional investor involvement in this sector to try to stimulate more commercially viable investment products,” Omidyar says.

LOANS TO LENDERS. The Omidyars' interest in microfinance isn't new. Their philanthropic organization, the Omidyar Network, had made some \$15 million in microfinance investments to date (see BW Online, 3/25/04, “A Bid for More Accountable Nonprofits”).

The network, which started investing its \$400 million early in 2004 in for-profit enterprises in addition to nonprofits, has put money into such microfinance pioneers as Unitus, a Redmond (Wash.)-based group that tries to accelerate microfinance investment, and the Grameen Foundation USA.

The fund won't directly lend directly to borrowers in developing countries. Instead, it will invest in lenders, so they can grow fast enough to reach economies of scale. Tufts will keep half the fund's income to invest in its own programs, and half will be reinvested in more microfinance initiatives.

TREND OF THE DECADE? Omidyar hopes the fund will spur at least \$1 billion in loans as they're continually repaid and recycled into more loans. It's all intended to help spur the creation of new investment products attractive to traditional investors (see BW Online, 11/4/05, "A Major Push for Microphilanthropy").

Indeed, Tufts President Lawrence Bacow sees microfinance potentially offering an entirely new investment vehicle for investors. He thinks the fund could help spur the creation of new investment opportunities similar to the rise of venture capital in the 1960s, mortgaged-backed securities in the '70s, and emerging-markets funds in the '80s and '90s. Says Bacow: "If people can earn significant returns from microfinance, investment will flow to it."

How significant? Tufts Chief Investment Office Sally Dungan says a good target will be the same average that Tufts has for its endowment overall: 9%. "We hope this will be a proof statement," she says.

STIFF RATES. Remarkably, the history of microfinance indicates that doing well by doing good isn't just a nice slogan. Typically, say microfinance experts, repayment rates on microloans top 98%. That's partly because interest rates are relatively high — often well over 20% annually. Indeed, some microfinance veterans worry that a profit-making motive could squeeze out some of the truly needy by excluding people or charging even higher interest rates.

Others say the evidence suggests otherwise. Grameen, for instance, has gradually lowered interest rates over time, as it has reached economies of scale, notes Geoff Davis, chief executive of Unitus. The entry of new investor capital through initiatives such as the Omidyar-Tufts fund, he says, should help accelerate that process.