

Foundations Don't Understand What It Means to Take Risks

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People generally want to get the most results with the least risk—at least that is what they tell their investment advisers. In the peculiar world of philanthropy, however, grant makers seem to have it backward. They ignore results by avoiding program evaluations, and constantly talk about needing to take more risks.

To be sure, taking risks can be fun. Climbing mountains or racing cars is exciting. In the sometimes tedious world of grant making, financing a novel and risky project can be a refreshing diversion. But risk, simply put, is the probability of failure: the greater the risk, the lower the likelihood of achieving one's objective. So in spending scarce philanthropic dollars, taking a risk should never be a goal in itself. The goal should be results—producing social benefits at the lowest possible cost.

But many grant makers seem to misunderstand what risk really is. Making a modest grant—often less than 1 percent of the total grants budget—to an uncertain but promising project is not much of a risk, especially if there is no evaluation afterward and if failure has no serious consequences. In percentage terms, it is the equivalent of a minimum-wage worker spending a dollar or two each week on lottery tickets—unwise, perhaps, but hardly what we would describe as taking a big risk.

True risk is frightening—when a program officer bets his or her job on a particular proposal knowing that the outcome will be highly visible, or when the chairman of the board gulps before taking a final vote. Taking a risk is when a foundation decides to focus all its grant making on a single area, declares that it will give away 12 percent of its assets every year, or devotes half of its grants budget to one project. In other words, if you don't feel it in your stomach, you aren't taking a real risk.

Does this mean foundations should only support safe, predictable projects? Not at all.

Foundations can, and should, be willing to take risks that other donors do not. What matters, however, is being able to evaluate the risk correctly, measure it against the potential rewards, and, as in managing an investment portfolio, develop an overall risk profile that serves the foundation's objectives.

Even more important is learning to reduce risk over time. No project or program is entirely risk-free—and conversely, most proposals that survive the grant-selection process have at least some chance of success. But continually making grants that fail is not productive—it is simply a waste of money.

Unless we learn from past mistakes, nothing at all is gained from taking risks. Few foundations today evaluate the effectiveness of their grants, and even fewer systematically incorporate what they have learned into their future grant making. As a result, their next grants are just as likely to succeed—or fail—as those made in the past.

How should one think about risk? In general, risk inheres in three areas, and grant makers should consider each one:

- **Ideas.** The ambition of the idea itself is one form of risk. Expanding or copying an established program is far less risky than financing a new and untested approach. Novelty, however, is not the only factor. The greater the complexity and scale of the project, the greater the risk. Similarly, the less popular the idea, the more difficult it is to carry out. Some new ideas are readily accepted, riding a prevailing trend; others face the more daunting obstacle of trying to change public behavior and market forces, which increases the risk.

- **People.** Any experienced investor will tell you that management is the most important predictor of success. Proven management that has run a similar program successfully probably can do it again. Untested management talent is less reliable. Foundations all too often overlook the level and relevance of experience of the management team that will carry out a particular idea or program—yet it is a crucial risk factor.
- **Location.** Geography carries its own risks. A single-city project close to home is much easier to establish than a national or global endeavor.

Similarly, a project that is geographically remote from the grant maker faces much worse odds. Differences in culture, language, and management style all take a toll. Thus, financing a project in Kosovo or Sierra Leone is inevitably going to be high-risk, though its importance may justify that risk.

Together, those three elements of risk can be used to compare different projects or to consider whether the risk is justified. The goal is not to eliminate risk but to understand it, mitigate it through the grant design where possible, and be certain that the level of risk is justified by the importance of the desired results.

Either way, knowledge, experience, and proximity are the antidotes to risk. The more expertise and prior grant-making experience a foundation has in a particular

field—especially if it has carefully and honestly evaluated its previous grants—the less risk is involved in supporting a novel project.

In other words, the same project represents different levels of risk to different grant makers based on their past experience and the importance of the outcome to their missions. That should produce a nice synergy: The areas in which a foundation has the most knowledge and grant-making experience should be the areas that are most central to its mission. And those are precisely the areas in which it can finance the greatest innovation with the least risk, and where it can make the greatest difference to society.

Without a clear focus and a solid evaluation process, however, foundations cannot learn to judge risk effectively. And they cannot make smart choices about where to direct their money. The challenge for grant makers, then, is not whether to seek or avoid risk, but whether to honestly evaluate results and think about risk in a more disciplined way.

Not only can we look before we leap, we can even measure the distance and velocity. And if grant makers want the excitement of mountain climbing, let it be on their own time.



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