



HONEYBEE CAPITAL

**HONEYBEE PUBLICATION #7 – BOXES AND BRIDGES ISSUE
FEBRUARY 2010
(ABRIDGED WEB VERSION)**

MAIN TOPICS FOR THIS PUBLICATION:

- **Idea of the month:** expanded thinking about developing markets
- **Boxes and bridges:** update on issues in investing
- **Books, arts, music ideas**
- **Bonus publication:** Divinity School, what the heck??

QUOTES OF THE MONTH:

“Talking about below-market return is basically saying, ‘give me your subsidy’... it is not efficient allocation of capital.”

- Jayant Sinha, Omidyar Network

“It’s more important to loving than to be right.”

- Raymond Chambers, UN Envoy for Malaria, private equity pioneer

“It is possible to be completely certain of the truth, and completely wrong.”

- Madeleine Albright

“Trust is built through relationships, not through providing capital.”

- Bob Pattillo, Gray Ghost Ventures

“Dude, you know he’s legit, ‘cuz there’s a lot of old people here.”

- Undergraduate attendee at CHK campus presentation
(where security was later called to handle hecklers)

“Character is nature in its highest form.”

- Ralph Waldo Emerson

“When it’s raining gold, reach for a bucket, not a thimble.”

- Warren Buffett, 2009 annual report

HOW ARE YOU THINKING ABOUT DEVELOPING MARKETS?
Or, is “Serving the Bottom of the Pyramid” already passé?

These thoughts came together in bits and pieces, mainly through discussions at the recent Harvard Social Enterprise Conference.

Here is an interesting notion – how are you, and the companies in which you invest, thinking of the developing markets? (All of these phases can coexist, of course, but they represent fairly distinct mindsets, and so are presented separately here).

- **STUFF - phase one:** in many cases developing markets are still seen mainly as a **source of resources** and raw materials, approached with an extraction mentality (many firms’ presences in Africa would seem to reflect this mindset). In this phase most attention is paid to efficient resource extraction – which, unfortunately, has historically proved that there is a fine line between extraction and exploitation.
- **PEOPLE - phase two:** increasingly popular in recent years has been the goal of “serving the bottom of the pyramid”, viewing people in the developing markets as **customers** and not just labor. Ten years ago few US fund managers knew what a sachet of shampoo was – now, it would be surprising if they did not. I vividly recall a GE aircraft engines presentation from years ago when every single customer was a non-US carrier, and many were brand new entities – it was startling then, but would not be so now. In this phase most of the focus is on repurposing “developed” products for “developing” markets – often with smaller packages, simpler design, lower price, etc.
- **IDEAS - phase three:** this is still pretty early, it involves viewing the developing markets as a **source of innovation** and new business opportunity. We are seeing some great innovations in local, scalable solar and water technologies in India and Africa, for example – this seems obvious, that innovation would come from the places with a great need for the new product – indeed, it is pretty arrogant to think that such ideas can or should be imposed from elsewhere. But most companies are not structured to find (or fund) local innovation, nor is this the way most business leaders are thinking. The VC community, especially those focused on impact investing and social enterprise, already regularly expresses this point of view, but it is still rare in other groups. *We think this will prove to be a great long term investment theme for both individuals and companies - seeking out local innovation outside of the traditional centralized hubs. How do we need to re-think our information sources, our business structures, and the use of our own time, in order to be more informed about these developments?*

THEMES TO CONSIDER IN IMPACT INVESTING – NO, MAKE THAT ALL INVESTING

We present these themes partly because they have been top of mind as we've been working more actively in the impact investment world, but also because, upon closer examination, they are actually universal themes, applicable to all forms of investing, and really all forms of analysis and decision-making. Therefore we hope this discussion is helpful to all Honeybee readers.

These thoughts have been gathered from many conferences, conversations, and publications, most notably the Take Action conference, the Harvard Social Enterprise Conference, and recent reports by Rockefeller Philanthropy Advisors, Parthenon Group, and Baldwin Brothers/Highwater Global Fund.

- **Theme #1: BAN THE EITHER/OR! UP WITH AND!**

In impact investing, countless discussions begin with the question, “where do you fall on the spectrum of maximizing social benefit vs. maximizing investment return?” The appeal of this question is clear – it is analogous to the risk/return discussions in all forms of investment. But the premise is false – there is NOT automatically an either/or tradeoff between social and economic return, and to frame our discussions as if there is (and even worse, as if it is scientific and decide-able beforehand) does a dis-service to the whole field. Sure, there are plenty of times when there is a tradeoff, but what about the times when you have a genuine win-win, or when you *could* have a win-win with just a little more creativity? We at Honeybee are in pursuit of high return AND high social impact, and when this is not possible... well, in the words of an early mentor, “Move on! The greatest thing about investing is, you get to choose!”

The greatest flaw in this either/or thinking seems to be assuming a finite (and usually short) time horizon. Take a concrete example – selling solar lamps to individual consumers who will use them instead of dangerous and costly kerosene lamps. The product is great, the manufacturing is responsible and efficient, the price is fair. Sure, you could maximize social benefit this year by giving the lamps away for free – but you would not be around next year, so the long term social benefit would end up being awfully small. Likewise, you could maximize profit by only selling to wealthier customers who could pay 10x as much – but if those customers are living in a well-ventilated home that maybe even has electric service already, the benefits to them would be much lower and so the lamps would actually be LESS valuable to them, not more. Your market would be constrained and again, your longer-term profits would be dinky compared to those from offering a fair price to the customers who'd benefit most. Yes, this is an oversimplified example, but by just extending the time horizon (something many investors say they are keen to do anyway), a lot of the noise falls away.

*This theme is more clearly and elegantly elaborated upon in the Rockefeller Philanthropy Advisors report, *Solutions for Impact Investors* – the authors, Raul Pomares and Steven Godeke, discuss the “tyranny of the OR” and “genius of the AND” in their introductory chapter ([link below](#)).*

<http://rockpa.org/pdfs/impactinvesting.pdf>

- **Theme #2: BOXES VS. BRIDGES: WHY DO WE ALL LIKE BOXES SO MUCH?**

If someone said, hey, get in this box! What would you do? Well, if it was a roomy box, with an open top, paved with stacks of hundred dollar bills, we'll all be inclined to try it out. But then next year, they say, welcome to your new box! And it's a little smaller, with dimes instead of dollars... but still, okay. But then one day you wake up and realize you are trapped in an airless 2 foot cube like David Blaine and there is one scuffed-up penny in the corner, and you are saying, how did I get here???

I will pause here to emphasize, I like consultants. I like them personally (usually), and their work often provides a useful framework for thinking through investment decisions. But, as with all frameworks, this with some limitations, and one of those limitations is the tendency to define fields more and more narrowly, until there are boxes within boxes within boxes. This is not a problem with consultants, it is a problem with human nature – faced with uncertainty and newness, we rush to define it, to quite literally box it in. It's more comfortable that way – we can examine it, and compare it to other stuff, in other boxes. Some level of this is healthy analysis, of course - so long as the boxes have enough air holes and flexibility to allow for growth and change over time.

We prefer the metaphor of a bridge to a box – while it can be helpful to have boxes to characterize different products, or different approaches, it can be even more helpful to have some way of comparing or contrasting or connecting them. This is hard enough when thinking about stocks vs. bonds, but even more difficult when bridging industries, or disciplines, or philosophies. Yet, opportunity lives in-between! Bridges (be they bridging ideas, or people, or organizations) can help to capture all that can't be neatly boxed-up.

Again, this is not specific to impact investing – think of “old media” companies who were willing to think creatively about the internet. Think of the number of times you've asked a research analyst what they thought of a big company's entry into 'their' industry, or a cool new product, only to hear “I don't cover them”. Well, that wasn't the question, was it?

- **Theme #3: LET'S MAKE SOME MONEY!**

In part due to all of the above, our discussions often end up being “defense” as opposed to “offense” (this, too, does not seem to be limited to the impact investment community; the consult-ification of financial markets plus awful turmoil of the last few years have put most discussions firmly –and perhaps even appropriately - in the 'defense' camp). But, that is exactly the point – if the whole world is scared and looking to be completely risk averse, it's time to make some money! Much like the time horizon issue in theme #1, when impact investing just shows some eye-popping

returns, a lot of the concern over terminology and fake tradeoffs will magically fall away (this might not be warranted, but it is true). What concerns us most is that it is difficult even in the best of times to generate returns like that – and when your mind is occupied with tradeoffs, lawyers, paperwork, and ever-shrinking boxes, it is almost impossible. Several years ago we heard a legendary investor voice his concern that his “profession had become a business”. It is time to re-focus on the profession, the reason that all good investors have entered the field in the first place – the art, the messy and profitable in-between, the bridges, not the boxes. It’s time to make some money for our shareholders, to find those great opportunities that are going to change the world. After several years of investment drought, you know there is a great backlog of worthy ideas and amazing businesses-to-be out there. Let’s talk just a little less about tracking error and a little more about upside potential.

BOOKS, ARTS, MUSIC - MEDIA OF ALL SORTS:

- **UNCHARITABLE, Dan Pallotta.** What I like best about this book is that it challenges those notions of boxes we talked about above – why is there such a vast gap between for-profit and non-profit enterprises in the US? Are the structures we’ve designed for each really helping to further our goals, or are they creating barriers that make effectiveness more elusive? (Pallotta’s for-profit company put together some of the biggest nonprofit fundraising events ever). Reactions to Pallotta’s arguments are often quite emotional, which perhaps indicates that the dysfunction he describes is real.

http://www.amazon.com/Uncharitable-Restraints-Nonprofits-Contemporary-Perspectives/dp/1584657235/ref=sr_1_1?ie=UTF8&s=books&qid=1267547237&sr=8-1

- **ZEITOUN, Dave Eggers.** This non-fiction account of a New Orleans family during the Katrina era is a compelling narrative, and also raises some important questions about our society and the structures we’ve created for our own protection (without beating you over the head with moralizing).

http://www.amazon.com/Zeitoun-Dave-Eggers/dp/1934781630/ref=sr_1_1?ie=UTF8&s=books&qid=1267500442&sr=1-1

- **GO TELL IT ON THE MOUNTAIN, James Baldwin.** Oh my! This is not a happy-go-lucky book. But it IS a passion-filled account of one man’s experience with faith -- and without it. The role that faith serves for each of the characters is a fascinating stew of need and want, of weakness and strength, of loss and (maybe) salvation. Even better when read in conjunction with Baldwin’s Notes of a Native Son. And while you’re at it, take another look at Richard Wright’s Native Son too.

http://www.amazon.com/Go-Tell-Mountain-James-Baldwin/dp/0385334575/ref=sr_1_3?ie=UTF8&s=books&qid=1267499421&sr=1-3

http://www.amazon.com/Notes-Native-Son-Beacon-Paperback/dp/0807064319/ref=sr_1_7?ie=UTF8&s=books&qid=1267499488&sr=1-7

http://www.amazon.com/Native-Blooms-Modern-Critical-Interpretations/dp/0791096254/ref=ntt_at_ep_dpi_3

- **THE RED BOOK, Carl Jung. (Sonu Shamdasani, Editor/Translator).**

There are several reasons to check out this (gigantic, costly) book. First, it is physically beautiful, resembling a 15th century illuminated Bible more than a philosopher's journal. Second, it is a rare chance to see the source material of a great thinker's work. Jung himself said of this period and these writings (1914-1930, when he was 38-54 years old): *"The years of which I have spoken to you, when I pursued the inner images, were the most important time of my life. Everything else is to be derived from this... the later details hardly matter anymore. My entire life consisted in elaborating what had burst forth from the unconscious and flooded me like an enigmatic stream ad threatened to break me... everything later was merely the outer classification, the scientific elaboration, and the integration into life. BUT THE NUMINOUS BEGINNING, WHICH CONTAINED EVERYTHING, WAS THEN."*

Just in case you are an 'executive summary' kind of person, here is Jung's own conclusion: *"I came to my self, a giddy and pitiful figure. My I! I didn't want this fellow as my companion... I want to live with you, therefore I will carry you through an utterly medieval Hell, until you are capable of making living with you bearable. You should be the vessel and womb of life, therefore I shall purify you. The touchstone is being alone with oneself. This is the way."* Interestingly, though the entire book is thick with religious and spiritual discussion and imagery, Jung's final words are about the self, alone. "My I" ! Isn't that a beautiful expression, and haunting? Caring and in opposition, all at once.

There has been a lot of press coverage of this book, as it has never been published before, and it was the center of an exhibit at the Rubin Museum this fall – some of the better articles are bundled together at the NY Times link below.

http://www.amazon.com/Red-Book-C-G-Jung/dp/0393065677/ref=sr_1_1?ie=UTF8&s=books&qid=1267499720&sr=1-1

http://topics.nytimes.com/top/reference/timestopics/people/j/carl_gustav_jung/ind ex.html?scp=1&sq=jung red book&st=cse

- **WEBSITE OF THE MONTH: KICKSTARTER.COM**

This is a fundraising platform for quirky creative types – you can help to sponsor films, new products, books, art of all sorts. If the project is fully funded it goes

ahead, and you often get some sort of participation (like a copy of the book). But if it's not fully funded you keep your money, and it's back to the drawing board for the creator. If you are sitting in your cubicle dreaming of your artsy hip Brooklyn-dwelling alter ego's life, this site makes a great coffee break.

<http://www.kickstarter.com/>

- **VIDEO OF THE MONTH: SHIRTLESS DANCING LEADERSHIP?**

Really, this is a lesson in following, not leading: *"There is no movement without the first follower – leadership is over-rated. Without followers, leaders are just lone nuts. So when you find a lone nut doing something great, have the courage to be the first to join in."* - Premal Shah, Kiva.org

<http://www.youtube.com/watch?v=GA8z7f7a2Pk>

BONUS PUBLICATION:

Can Divinity School help you to better understand investment risk?

Many have asked about our recent studies at Divinity School – generally, with a slightly wary tone: "what do you DO over there, anyway?" One of the most surprising and encouraging elements so far has been the discovery that most of the material studied is quite directly relevant to Honeybee's more capitalist-minded interests. (And, importantly, the two are not very often at odds!). The easiest way to demonstrate this is to just share some of the work we've done so far... so, as a supplement to our regular publication, we've included in a separate attachment a SHORT paper written for a class last fall. The paper compares two sets of parallel concepts around risk and uncertainty, translating from the financial literature to the philosophical, and vice versa, and then using the recent financial crisis as a sort of case study for these concepts. Though written in more academic style, it is a SHORT paper and we hope it helps to show the relevance of the academic to the applied, and vice versa. Did we mention it is SHORT? Five minutes, see what you think!

COMING ATTRACTIONS:

Honeybee's next issue will have an eco-focus, as we will be attending several events focused on energy and the environment in the coming weeks.