



A LEG UP TO THE NEXT RUNG: Boosting Upward Mobility through Shared Value

Future Finance Series No. 2



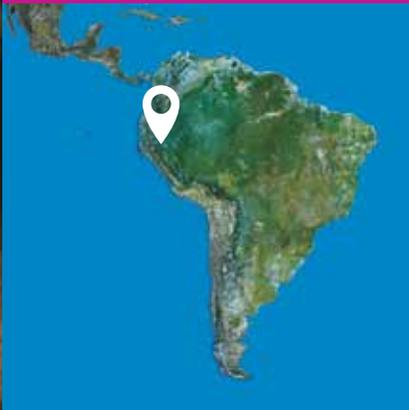


Social Infrastructure

Universidad San Ignacio de Loyola, Peru



CASE STUDY



A Leg Up to the Next Rung: Boosting Upward Mobility through Shared Value

Working with a private university in Peru, the Inter-American Development Bank (IDB) is applying the concept of shared value to higher education, showing that investing in the next generation of students makes sense both for the university and for Peru.

In a country where poverty is still too common and a university education still too exclusive, Peru's Universidad San Ignacio de Loyola (USIL) is acutely aware that access for more students to get a degree means a chance to get ahead in life.

Demand for higher education has taken off in Peru in recent years, as more people join the ranks of the *clase media emergente*, a term that describes the many people—by some estimates, over half the population in the Lima metropolitan area—who have worked their way out of poverty but have yet to gain a solid financial footing.

For the next generation, one of the surest rungs on the ladder of upward mobility is a university degree. Yet that remains out of reach for far too many young people, and not just in Peru. Among 20–24 year old Latin Americans, only 49% of males and 55% of females completed 12 years of education in 2011. The IDB finds a large decrease in high school graduation correlates with lower family income. Poor families are more likely to withdraw students from school so that they may enter the workforce. For those that do graduate from high school, public universities cannot come close to meeting the demand, and many students cannot afford a private alternative. Student loans, meanwhile, are virtually nonexistent for undergraduates, unless their families own property they can put up as collateral.

When the Universidad San Ignacio de Loyola (USIL) approached the IDB to request a sizable financing package for a campus expansion, the Bank saw an opportunity to put a shared value approach to work in the design of the project. Alongside its financing package, the Bank carried out an IDB Shared Value Appraisal to help USIL identify shared value opportunities. The Bank's appraisal is a diagnostic tool based on the premise that a company can best thrive by aligning its core business with pressing socioeconomic needs where it operates.

The challenge for the IDB's shared value team was to identify the business case for USIL to invest greater resources to recruit and retain underexplored segments of academically strong students from socially diverse backgrounds

Writing in the *Harvard Business Review* in 2011, Michael E. Porter and Mark R. Kramer made the case for shared value as an enlightened approach to capitalism:

The concept of shared value can be defined as policies and operating practices that enhance the competitiveness of a company while simultaneously advancing the economic and social conditions in the communities in which it operates. Shared value creation focuses on identifying and expanding the connections between societal and economic progress.

The challenge for the IDB's shared value team was to identify the business case for USIL to invest greater resources to recruit and retain underexplored segments of academically strong students from socially diverse backgrounds.

The idea immediately resonated with USIL's CEO Juan Manuel Ostoja. He described shared value as an "upgrade" of the traditional approach to corporate social responsibility (CSR), which he said can be too dependent on fluctuating budgets and priorities. When social objectives are embedded in the heart of the business, he said in an interview, they add value and are more likely to be sustained over time.

STUDENT GUARANTEE FUND

As a result of the Shared Value Appraisal, \$2 million of the Bank's \$25 million financing package for USIL will be allocated to set up a guarantee fund to provide collateral for student loans and scholarships. The appraisal provided a deep dive into how USIL could structure a solid, sustainable guarantee fund that would benefit the university's bottom line and at the same time put a professional degree within the reach of more students.

As an investment built on the concept of shared value, the guarantee fund is set up to create incentives in different directions, explained Peter Stevenson, the IDB principal investment officer who managed the loan transaction. At the most basic level, the guarantee fund is designed to generate more loans and scholarships in order to get more students in the door of the university, and thus generate financial value to USIL by attracting new students who otherwise might not be able to afford a private school. Since USIL is taking on the cost of borrowing the money for the guarantee fund, it has to take steps to ensure that turns out to be a good investment.

"It's really a tool that motivates the university to encourage success in the students it's guaranteeing," Stevenson said. "If the university doesn't get the job right, they're going to lose money."

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For the guarantee fund to be sustainable, the university must ensure that the beneficiaries can complete their education, find good jobs, and eventually pay back their loans. This will require extensive tutoring and mentoring services, since many of the students would likely be the first in their families to pursue a professional degree and might lack a strong support system to keep them on track.

In 2013, USIL developed and implemented an extensive tutoring program to help several hundred students who had enrolled in the university through a new government-funded scholarship program called “Beca 18”. The university plans to invest greater resources into that tutoring model to optimize the chances for success of the students backed by the guarantee fund.

By combining investment in a guarantee fund to backstop student loans and scholarships, as well as more resources for services aimed at reducing dropouts, the IDB and the university believe they can have an impact well beyond the halls of USIL. “Our main challenge is to create a successful approach so that this model can be replicated,” said Kelle Bevine, who manages the shared value team at the IDB. She said, “By incentivizing the University to invest in lowering dropout rates and catalyzing third-party capital through a guarantee mechanism, this two-pronged approach can improve graduation rates at USIL while kick-starting a broader market for student loans that benefit far more students across the country.”

USIL is preparing to launch the mechanism on a pilot basis in 2014, with the first students arriving in time for the second semester in July. The university itself will not get into the business of student loans, but the guarantee fund will drastically reduce the risk for willing lenders. The initiative will seek out talented students who are at an economic disadvantage and will place an emphasis on promoting cultural diversity and gender equity.

MORE THAN AN ACADEMIC ISSUE

Founded in 1995, the Universidad San Ignacio de Loyola is hardly an ivory tower kind of place; rather, it has set its sights on contributing to a high-quality work force by building the practical skills a fast-growing country requires. Social responsibility is part of the school’s identity. At any given time, USIL students may be teaching crash courses in entrepreneurship in poor neighborhoods of Lima, or professors may be helping local elementary and high school teachers update their computer skills.

USIL’s mission also emphasizes entrepreneurship, a commitment to national development, and a global perspective, reinforced through partnerships with universities in other countries. The curriculum focuses on technical and business-oriented disciplines, and all students must become proficient in English. About 20% of USIL students are young working adults. Tuition is set on a sliding scale, and more than half of the students receive discounts of 50% or more.

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USIL hopes to double the size of its undergraduate student body over the next 10 years, from about 11,000 today to more than 22,000. As part of that effort, it plans to undertake a \$79 million infrastructure expansion and update its equipment and research facilities. (Its main campus is in Lima’s La Molina district, but the school also has campuses in Lima Norte and in the Andean city of Cusco.)

A \$23.5 million loan from the IDB will contribute toward the expansion, help USIL refinance its existing debt, support the university’s plan to achieve international accreditation, and establish the guarantee fund. The financing package includes an additional loan of up to \$1.5 million from the IDB managed Canadian Climate Fund for the Private Sector in the Americas which will enable USIL to upgrade its facilities to meet the highest environmental standards and become the first university in Peru to be LEED-certified (for Leadership in Energy & Environmental Design).

Much of the university’s growth in recent years has come from an increase in students from the emerging middle class. Student enrollment from this socioeconomic group more than doubled in the last few years, jumping from 17% to 37%. In a typical case, a student’s parents or grandparents may have migrated decades ago from a rural area in Peru to the outskirts of Lima, to work at a menial job; now, at great personal sacrifice, they can finally think about sending a member of the family to university as a way to invest in the future.

Although this represents considerable progress—higher education remains out of reach for about 7 in 10 Peruvian young people, according to USIL’s CEO—many of these students struggle financially. If a parent loses a job or an unforeseen expense arises, chances are the student will have to drop out. Ostoja said USIL wanted to be “pioneers in Peru” by investing in helping students afford an education, “not as a bank but by triangulating funds.”

Private institutions now educate a majority of university students in Peru. With a growing number of young people graduating from high school, and more companies demanding a skilled work force, the public university system has been unable to keep up with demand. According to data published by Peru’s National Assembly of University Presidents, in 2010 private universities accounted for around 60% of university students in Peru, up from 40% in 1996. At the undergraduate level, private universities grew three times faster than their public counterparts.

Meanwhile, the quality of education at all levels, and its implications for Peru’s future, has become an area of growing concern for the country’s educators, politicians of all stripes, business leaders, and citizens in general. One trigger for concern has been the poor showing of Peruvian high school students on recent PISA tests—a benchmark called the Programme for International Student Assessment, which measures how well 15-year-olds around the world perform in math, reading, and science. All eight Latin American countries that participated in the test in 2012 ranked among the bottom 25 percent.



TALENT IS
EVERYWHERE

Amid the national conversation on education, the Peruvian government instituted a scholarship program called Beca 18. The program gives top public school students from the most disadvantaged segments of society the chance to receive full university scholarships, along with living expenses, in exchange for a commitment to work in the public sector for three years after graduation. Beca 18 has targeted specific fields, such as engineering, in which the country has the most pressing need for university graduates. In the first year, it provided scholarships to some 5,000 students nationwide.

"This government is making a significant investment in education," said Carmen Blázquez, USIL's vice chancellor for student services. She described Beca 18 as a "light at the end of the tunnel" illuminating the path the country must take to expand opportunities and make higher education more inclusive.

In 2013, the first year the program was in full effect, USIL accepted around 600 scholarship recipients. Blázquez said in an interview that USIL recruiters have traveled to remote reaches of the Amazon and the Andes to identify the most promising students eligible for the Beca 18 program. "Talent is everywhere," she said. "Talent is in the genes."

As a result of the government scholarship program, USIL is welcoming more students from the country's lower economic rungs, including many from rural and indigenous areas—an important step in the university's outreach goals. "This country is multicultural, multilingual, and multiracial. This is a reflection of Peru," said Blázquez, who considers the greater cultural diversity "a source of pride for me as an educator and as a Peruvian."

A STRONG COMMITMENT

In order to maximize the odds for success of the Beca 18 students, USIL contracted dozens of tutors to support the scholarship recipients, academically and in other areas, throughout the school year. Each tutor is responsible for 17 students, providing both group instruction and one-on-one support to supplement the classroom teaching and help bridge some of the gaps in the quality of education the students may have received in elementary and high school. Since many of the students are far away from their families, the tutors also try to ensure that they are in a good housing situation, that they are handling the pressures of city life, and even that they are getting proper nutrition.

By the end of 2013, after the first full year of the program, the number of Beca 18 students at USIL had fallen from 603 to 565; some students dropped out, failed a course, or, in a handful of cases, had to leave for health reasons. While this loss of 6.3 percent is less than half the normal dropout rate for first-year students, Blázquez said she was not satisfied and was in the process of making adjustments to the tutoring program. "It's very painful when a student loses a scholarship," she said.

USIL WILL
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USIL will build upon this existing platform of tutorial support, incorporating lessons it continues to learn from the Beca 18 experience, with an aspirational goal of zero dropouts of students covered by the new guarantee fund. Both the IDB and USIL agree that the key to the success of the new fund will be how well the university is able to manage the dropout rate for the students who receive the guaranteed loans or scholarships.

In Peru, a university education typically lasts five years, with the first two devoted to general studies and the last three to a student's career track. It is in their earliest semesters that students are most vulnerable to dropping out, according to Henry Barclay, who runs USIL's Assessment and Development Center. The center tracks student performance and tries to identify problems early on, so as to provide timely academic guidance or other assistance. For students who reach their third year at USIL, the odds of their dropping out fall significantly, to the low single digits.

The university plans to invest in strengthening the Assessment and Development Center to ensure that the students backed by the guarantee fund receive enough attention and support, according to CEO Juan Manuel Ostoja. Over time, as USIL acquires more experience in lowering dropout rates, it can apply its know-how more broadly, to the benefit of all students and the university itself.

One reason the USIL project is particularly attractive to the IDB is the opportunity to better incorporate more vulnerable students into the university, said Judith Morrison, senior advisor of the IDB Gender and Diversity Division and member of the Bank's shared value team. "We hope that as a result of the IDB's shared value approach, USIL will increase the number of deserving and qualified indigenous, Afro-Peruvian, and female students who would otherwise be unable to attend college due to external financial pressures and social exclusion. We applaud USIL's commitment to incorporating promising first-generation students in challenging academic programs throughout the entire university."

Beyond USIL, the guarantee fund also has the potential to spur a broader market for student loans. Unlike several other countries in Latin America, Peru has had virtually no financing options in place for undergraduates without collateral at their disposal; banks have considered such loans far too risky, said Stevenson, the IDB investment officer. While the Peruvian government is in the process of developing a student loan program, he said, the USIL initiative could have a positive impact in the private-sector lending market. "If this is successful, it could be something that will generate an interest in lending to students," Stevenson said.

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THE APPRAISAL PROCESS

The blueprint for the guarantee fund was the output of the Shared Value Appraisal, IDB's new tool to optimize value creation in its engagement with private-sector clients. To complete the appraisal, the Bank retained the international consulting firm Deloitte to assist the IDB team in carrying out an intensive assessment over several months in 2013. The process included interviews with key university staff, government officials, and other stakeholders, such as potential providers of student loans. The team also met a group of students who currently benefit from Beca 18 or other types of scholarships, to elicit their views about positive aspects of their programs and areas for improvement.

Once the team had the relevant data, the next step in the appraisal process included a detailed cost-benefit analysis, based on different assumptions. The appraisal looked at a range of factors to weigh potential risks and rewards, such as the number of new students the program might attract, the number and costs of tutors and mentors required, and the various scenarios for student dropout rates.

The rigor of the IDB Shared Value Appraisal relies on identifying and structuring investments that are sustainable over the long term, one feature that distinguishes shared value investments from traditional CSR activities. To ensure the guarantee fund was sustainable required keeping the risks manageable: After all, the more students who do not finish school or cannot pay back their loans, the faster the fund will be depleted.

The guarantee fund will therefore be structured conservatively, with a relatively small number of loans backed by the capital of the fund. Commercial lenders tiptoeing into this new market will have the assurance that the fund—which will be held by a trust—can cover the vast majority of their liability. The idea is that over time, once the university builds a track record and demonstrates consistently low dropout and payout rates by the fund, increasing the confidence of guaranteed lenders, the fund can start to leverage funds by mobilizing loans and scholarships in excess of the amount of capital it holds in reserve.

The university's Vice President for Finance, María Julia Garay, said the guarantee fund essentially enables USIL to assure lenders that if they are willing to gamble on a student, "I will guarantee that this student is going to finish school." In the worst-case scenario—maybe the student cannot adapt to life in Lima, or maybe a family crisis intervenes—the lending institution gets most of its money back. Depending on the lender, students will have different grace periods after graduation before they have to start paying back the loans and different time frames for repayment.

For USIL, the Shared Value Appraisal generated benefits beyond the guarantee fund, by helping the university more clearly define its priorities and identify areas for improvement

In addition to the loans, the university is planning to create 20 scholarships per year for talented students from the most vulnerable economic groups. The scholarships will be financed jointly by a nonprofit arm of USIL and private-sector donors, with the private donors' portion backed by the guarantee fund in the event of a default. Eventually, the university hopes to persuade more companies to provide matching grants, backed by the guarantee fund, to help create more scholarships and invest in Peru's talent pool. "We're going to have to knock on doors, because we need more companies to join us in investing in our future workforce," Garay said.

On the loan front, meanwhile, USIL has been negotiating agreements with lenders, including bank-affiliated organizations, to provide educational loans to undergraduates. The value proposition the university is offering is to cover different percentages of the risk, depending on such factors as students' economic situation or whether they have already been in school for a while.

"Institutions obviously want the least risk possible," Garay said. Some will finance a loan only after a student has completed the first few semesters, once the dropout risk has gone down. In some such cases, USIL might provide a scholarship until the student is eligible for a loan.

To reduce risk and protect the guarantee fund from being depleted, the process for selecting students must be rigorous and the support system once they are in school must be strong. Beneficiaries will be selected based on a combination of factors, including academic standing, economic need, and community leadership, and will have to be approved by a committee that includes representatives of the university and the lending institutions.

Like other university officials, Garay hopes that the guarantee fund will lead to more competition among universities, lenders, and public institutions, with the result of more students having a shot at higher education. "What we want as a country is to truly incentivize education," she said.

LESS-TANGIBLE BENEFITS

For USIL, the Shared Value Appraisal generated benefits beyond the guarantee fund, by helping the university more clearly define its priorities and identify areas for improvement, according to Diego Castrillón, who works with an economic forecasting firm affiliated with USIL and served as the university's chief liaison with the IDB-Deloitte team. The appraisal process "helped us bring a lot of this down to earth," he said. "This has been a very enriching subject for us."



I WANT TO
BE THERE

While the university is focused for the moment on making the guarantee fund a success, Castrillón is convinced this won't be its only venture into shared value. As an economist, he appreciates shared value's pragmatic perspective of "aligning incentives," adding that USIL will be looking at other ways to enhance both social and economic benefits.

In recent years, USIL's understanding of social responsibility has been evolving, Castrillón said, and the university has looked for ways to add value to society at a deeper level, building on its particular strengths, instead of simply taking an "assistance-based" approach. The concept of shared value, he said, taps into that desire to effect sustainable change.

Castrillón believes the approach will resonate with students too, adding that young people in Peru today are more attuned than his own generation to the need to contribute in real, lasting ways to society. He said that many students, even those who don't necessarily need a loan or scholarship themselves, will look at what USIL is doing and say, "I want to be there."

A FACE OF PERU'S NEXT GENERATION

Lesli Patricia Pinedo Velásquez is the kind of student any university would love to have. A 17-year-old scholarship recipient at Lima's Universidad San Ignacio de Loyola (USIL), Pinedo has her eyes firmly set on a degree in business engineering, a field that examines how to streamline and improve business operations.

As the oldest child and the first person in her family to attend university, Pinedo realizes that she represents "pride and also hope" for her family. Her mother, "the backbone of our home," always reminds Lesli that she needs to set a good example for her two younger sisters so they can all be professionals someday.

Pinedo started at USIL in 2013, part of the first wave of students under the government's Beca 18 program. She was better prepared for university than many of her peers, having attended the Escuela de Talentos, a public high school designed to provide an enriched, technology-intensive learning experience for top students in Callao, a province in the greater Lima metropolitan area.

Despite her level of preparation, it's not always easy to juggle everything—Pinedo still lives at home with her family, more than two hours by bus from campus—but she is grateful for the opportunity and support she is receiving. Describing herself (with a slightly self-conscious giggle) as a member of Peru's emerging middle class, she is determined to start her own company someday. That goal, she said, will keep her working hard at USIL so she can hold on to her scholarship.

"Not for anything in the world will I let this opportunity slip out of my hands."

Through its Structured and Corporate Finance Department (SCF), the IDB partners with private sector entities to achieve breakthrough financial results with high development impact. The IDB works with large- and medium-sized businesses, including private utilities and infrastructure operators, banks and financial institutions and state-owned enterprises in a broad range of economic sectors.

Acknowledgments

We thank all the people whose efforts helped this project achieve remarkable results. Foremost we thank the Universidad San Ignacio de Loyola for its leadership and for partnering with the IDB to surface shared value opportunities. We also thank Deloitte-Canada and Deloitte-Peru for their role in the design of the shared value appraisal. Special thanks are extended to Kelle Bevine, Bettina Boekle-Giuffrida, Peter Stevenson, Christian Mirabella, Andres Lavarte Judith Morrison, Ana Lucia Escudero and Leonardo Mazzei who provided valuable support in elaborating the case study. Finally, we thank Janelle Conaway for beautifully piecing this story together.



Future Finance Series No. 2

A Leg Up to the Next Rung: Boosting Upward Mobility through Shared Value narrates how a leading private university in Peru is putting shared value into practice through IDB's support.

Coined by Harvard professors Michael E. Porter and Mark R. Kramer in 2011, the concept of shared value is being discussed among businesses, governments and development practitioners alike as a way for businesses to increase financial returns while simultaneously delivering social and climate impact in the community. It is a new way of doing business responsibly.

While many companies in Latin America and the Caribbean appreciate shared value investments, most do not have the capacity, time or resources to identify such opportunities independently. The Inter-American Development Bank (IDB) has created Shared Value Appraisals to assist clients in designing an actionable business strategy to optimize resource allocation that enhances both competitiveness and social value in the community.

This case study discusses how the Universidad San Ignacio de Loyola (USIL), a leading private university in Peru, and the IDB worked together to establish a guarantee fund to recruit and retain academically strong students from socially diverse backgrounds.

USIL's leadership in applying the concept of shared value to higher education, underscores how investing in the next generation of students makes sense both for the university and for Peru.

The case study is also available online at www.iadb.org/sharedvalue

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