Case Study

Lumni Income Share Agreement

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Introduction

Lumni was founded in 2002 in Colombia with the objective to finance students' university fees using an income share agreement (ISA) financial instrument. By means of an ISA, a private investor or investing organization provides a student with up-front capital for financing higher education. In exchange, the student pays back a percentage of their future income for a defined period of time after they finish their studies. Unlike a loan, there is no principal balance to repay with an ISA, and depending on employment success and earning level after school, the student may ultimately pay more or less than the amount initially financed (Palacios et al., 2014).

In 2011, Lumni raised a total sum of USD 17 million to finance the education of students in Colombia, U.S.A., México, Chile, and Peru (Bornstein, 2011). By 2016, Lumni had supported 8,000 students and experienced 800% growth (Dinero, 2016). In 2019, Lumni raised USD 1.5 million as investment for 360 students with its newest branch based in Peru (Global Innovation Exchange, 2019).

Higher Education Financing Problem

The global economy demands an increasing knowledge-based labor force; therefore, the im-portance of a university education is dramatically rising worldwide. However, only 7% of the world's population currently has a college degree (Bornstein, 2011). The United Nations Education-al, Scientific and Cultural Organisation (UNESCO) reported that access to higher education in the Latin American region was uneven and highly concentrated in high-income areas and cities. There-fore, the overall accelerated increase in access to higher education was leaving rural areas disad-vantaged (UNESCO, 2013). A study conducted in 2009 revealed that a prevalent reason limiting ac-cess to higher education in Latin America was of the financial nature. In Colombia, 73% of youth between 18 and 24 years of age who did not study reported the reasons of financial inability, the need to work, and family responsibilities. In Mexico, only 2% of college students had access to stu-dent loans (Téllez, 2009).

Student loans are the most prominent financing mechanisms attempting to reduce the financial burden for students in accessing higher education. However, in countries where student loans have been implemented, they have shown to be problematic because the investment has not always translated into successful careers, as some students did not complete their studies or secure a job with salaries commensurate with the loan amount. Without securing a job that guarantees an income that enables to repay the debt, loans can have damaging consequences for students. For example, in the United States, a country where student loans have been widely implemented, in 2012, more than 40% of students who started a degree did not complete it within six years of starting it, and many graduates found themselves unable to get a job that pays enough to justify the investment. Nearly 45% of the students who did graduate were working in jobs that did not require a degree. More importantly, it is concerning that the delinquency rates on student loans reached 12% in 2013. This rate is higher than the roughly 10% delinquency rate on mortgages during the housing crisis in 2008–2009 (Palacios & Kelly, 2014).

Considering the negative effects of student loans, traditional capital investments have been considered as viable alternatives to financing higher education costs. Venture capital's established practice splits the risk of the investment between the investor and the entrepreneur. ISAs are considered "equity instruments for human capital," where both students and investors share the risk of a successful career as a result of investment in higher education (Palacios & Kelly, 2014).

Lumni's Mechanism design

Lumni's approach involves students, universities, and investors that are interconnected by Lumni, an independent organization that coordinates the ISA financing mechanism.

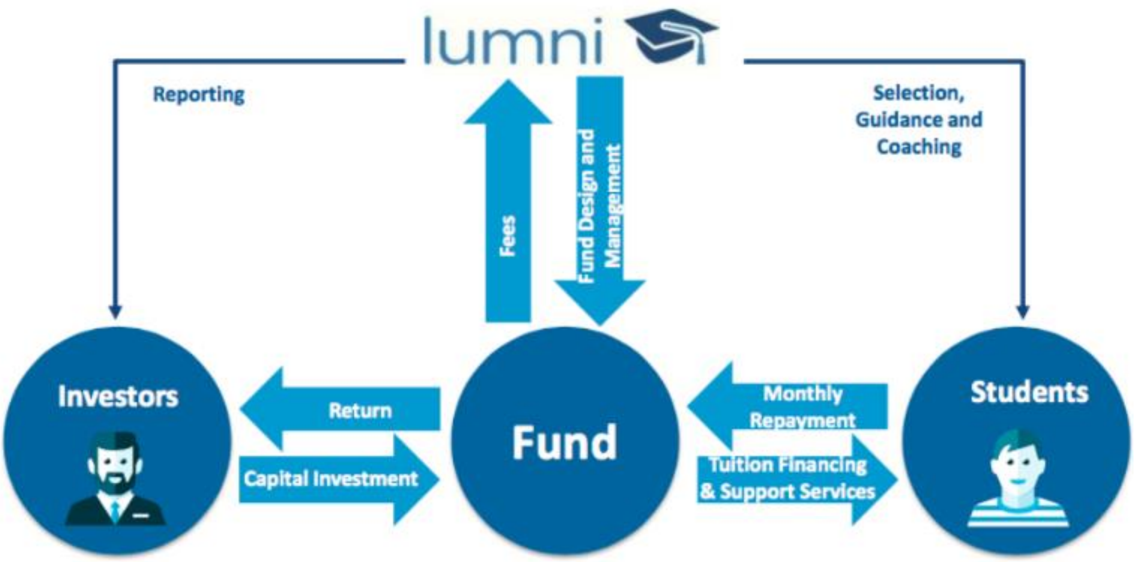

Figure 1. Lumni's income share agreement approach.
Source: Castizo, R., & Buckland, H., (2016). Study of social entrepreneurship and innovation ecosystems in the Latin American Pacific Alliance countries: Case study of Lumni, Colombia. Inter-American Bank of Development Technical Note IDB-TN-1205.

In this case study, the students who seek financing are selected by means of a rigorous evaluation process, involving the submission of various application information, a personalized examination, the financial evaluation of the projected future payments, and personalized contracts fit to the individual and their country-specific circumstances.

Students are accompanied during and after their studies by volunteer mentors who are recruited by Lumni, who seek to ensure the students' academic and professional success. In addition, students can benefit from free courses and trainings depending on the conditions of their contract.
Lumni funds are provided by private and institutional investors who, like in traditional capital ventures, expect a return on investment. Lumni's investors range from private investors, government funds, international funds, private companies, and foundations, who seek to benefit a specific community; there is also a considerable group of individual investors who aim to benefit the society at large in the countries Lumni operates in. Lumni also partners with non-profit organizations to distribute the funds among students of vulnerable populations (Bornstein, 2011).
The personal contracts signed between Lumni and the students detail the payment period after graduation as well as the amount of funding offered to the student, which is individually defined for each student. The general rule applied by Lumni is that every student pays 14% of their salary for a predetermined period of time after their graduation. After completing the contractual period, the students are debt-free independently of the payments made. Principally, students pay back the investment to Lumni on securing their first employment. However, they are also asked to maintain a "payment culture" during their studies, for which payment rates vary by country. In 2016, according to a case study in Colombia, only 2% of students defaulted on their repayment (Castizo & Buckland, 2016).

An ISA is neither a sole profit increasing scheme nor a publicly financed subsidy. Investors potentially benefit from investing in Lumni by receiving financial profit while having high social impact (Lumni, 2019). ISA's proponents claim that they create more educational opportunities and reduce the investment risk for students pursuing higher education and argue that Lumni makes financing available to students based on their potential and regardless of their economic background.

To date, the following illustrative examples of investors have partnered with Lumni to invest in students' higher education:

- *Chile:* FAB1, Fondo Inversión Social, BHP
- *Colombia:* Bancolombia, Fundación Bavaria, Postobon, Fundación Terpel, Equion, Grupo Nutresa, Philip Morris, Alqueria, Cerrejón
- *Mexico:* Teletón Fundación, Promotora Social Mexico
- *Peru:* Grupo ACP, Montpellier Foundation, Hampshire Foundation

Lumni has also partnered with the Universidad Sebastian in Chile and considers the following factors to motivate educational institutions to adopt ISAs in a partnership with them: "reduce the student dropout rate; attract and retain a diverse student body; promote educational access to less favoured populations, strengthen and complement the integral training of students" (Lumni, 2019). Regarding the motivations and alleged benefits for students, Lumni highlights the sense of responsibility students feel to return the investment in them by paying the monthly fees as well as their aim to succeed in their careers after graduating. According to Lumni's website, students report feeling supported by their mentors in balancing academic achievement and their workload to pay the monthly fees.

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