CHB 5130

Youth Bonds
A Proposal for funding the initiative of young people

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Youth Bonds need to be designed to be a partnership, a walking with the young people so funded. They also need to be such that individuals compete against themselves, rather than against one another; that they are 'stretched' and learn to know themselves and their worth in society through the way they serve other people by what they bring to the table. The basic idea is as follows:

1) Municipal governments issue the Youth Bonds in order to raise capital to finance the initiative of young people (so that they become entrepreneurs, not dependants).

2) The Youth Bonds are bought and held by institutional, governmental and private investors. The bonds are tradable.

3) The interest on the bonds is met out of the 'misplaced youth' budget, meaning the funds the municipal government would otherwise spend in order to meet the costs of drug addiction, criminality, re-education and other aspects of misplaced youth. Whether they should or not, insofar as these costs fall to its account, the municipal government stands surety for the bondholders in the event of partial or total default.

4) The bond market prices the Youth Bonds on the basis of risk and term structures that reflect (a) the use the funds will be put to, and (b) the importance the market gives, and therefore the value it accords, to funding young people in this way.

5) The money is used to fund the initiatives of young people on the following basis:
   i) the money is advanced in the context of a specific financial plan (see *Financial Literacy*) which is used by lender and borrower-entrepreneur alike to navigate the project to fulfilment. The financial plan identifies the amount and term of the capital needed by the borrower-entrepreneur;
   ii) because the interest on the bond is met out of the 'misplaced youth' budget, there is no interest charged to the borrower-entrepreneurs. They are, however, required to refund the principal at the agreed term, so that other young people may use the money, and so that the bond can be repaid (in the event that it cannot be rolled on or replaced at term).[1]

6) The fact that no interest is charged to the young borrower-entrepreneurs is intended to do two things:
   i) provide a psychological fillip because it expresses confidence in the borrower-entrepreneur;
   ii) maximise the borrower-entrepreneur's pathway to profitability.

7) As well as acting as a navigation instrument, the purpose of the financial plan is to provide collateral based on shared awareness of a project's circumstances (instead of the usual 'blind' risk-reward considerations when lending at a remove).

8) The financial plan has three components: Income and Expenditure Accounts, Balance Sheet, and the Cashflow Monitor. All are tracked in terms of budget, actual, variance and explanatory narrative, reviewable at least quarterly, but preferably monthly. This means:
   i) the project is accounted for on a detailed basis, using standard accounting software;
   ii) the borrower-entrepreneur is financially literate (see *Financial Literacy*), meaning able to keep accurate, up-to-date accounts and to create and work within a financial plan. But also cognisant of broader economic and monetary affairs.

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[1] An added feature, but not necessary, would be to add a repayment supplement, freely contributed by the borrowers, which could be used to create a fund to displace the original bonds.

Technical Aspects

Purpose:	To provide capital for investment in the initiative and projects of young people, so that they discover themselves and take charge of their own lives.
Type:	*To be defined.*
Features:	*To be identified.*
Nickname:	A nickname needs to reflect the social and financial effect of the bond. Suggestions sought.
Denomination:	Should this be a national, international (e.g. SDRs or USD) or local currency?
Issuer:	A municipal rather than national government (because of proximity to the problem).
Dealer:	A municipal rather than national, in order to promote solidarity with the community.
Holders:	Institutional, Governmental, Private individuals. Local, national or international.
Term:	*n* years. The term would be a function of the proposed use of the funds
Interest Rate:	It would be interesting to see how markets priced such a bond. Any thoughts?
Yield to Maturity:	It would be interesting to see how markets priced such a bond. Any thoughts?
Risk:	Covered by financial literacy on the part of the borrower-entrepreneurs, by 'walking with' on the part of the lender, and by not seeking automatic exit.

Initial Amount:

50	x	1,000	=	50,000
20	x	10,000	=	200,000
10	x	20,000	=	200,000
1	x	50,000	=	50,000
(81	x	6,175)	=	500,000 USD

Financial Literacy

Whether they have in mind first, second or third sector businesses, governments or charities, for-profits or not-for-profits, serious commentators are increasingly pointing to the need for financial literacy on the part of all economic agents if they are to be able to operate effectively in today's circumstances. In my book, *Finance at the Threshold*[2], I argue that there is an urgent need to find ways that connect today's excess liquidity to young people especially by, in this case, creating bonds with which to fund their initiative and creativity. In this way, money can be made available for them to undertake tasks that are meaningful for themselves, their communities and socio-economic life generally.

Such funding is and should be kept apolitical. The borrowed capital will appear as a liability on the borrowers' balance sheets; the corresponding asset will be the 'cash' with which they are able to give expression to their intentions. More importantly, as befits entrepreneurs, the income individuals then derive from their activities is treated as a reduction or withdrawal of capital, not as a wage or salary. That is to say, from a taxation point of view they are self-employed or own proprietors. Put another way, their income derives from the profitability (i.e. success) of their venture.

A key aspect of the Youth Bonds, therefore, is the financial literacy of the borrowers, the young entrepreneurs. In that sense, the Youth Bond's foundation (and collateral) is an awakening to financial literacy on the part of borrowers so that they, in effect, also act as their own financiers and auditors.

Financial literacy can be of a narrow, unquestioning kind that merely reiterates existing assumptions and practices, many of which are becoming out-dated by events. Or it can be thorough-going, based on an awareness of the wider history of monetary and financial affairs and, in particular, the role of accounting as an instrument for goal achievement and effective organisational management.

Financial literacy can also be top-down, theoretical and remote, or grounded in the up-to-date accounts, financial planning and cash-flow realities of an existing business. Best of all is a business that one either owns or in some other way has a direct connection with, so that one can effect change by doing, especially by doing with regard to one's own activities.

It is financial literacy in this wider sense that is meant here. Financial literacy of this kind is also a powerful learning path, teaching one to be the author rather than victim of one's circumstances. Indeed, it is often the lack of financial literacy and its corollaries, long-term profitability and effective cash-flow management, that prevent goal achievement.

[2] Gower, London, 2011.

Outline of Financial Literacy Courses

The financial literacy courses implicit in this proposal would have two main components:

1) understanding the big picture (the history of economic thought, economic history, macro economic policy, and so on);

2) effective day-to-day financial management of one's own affairs, since what is done in an individual economic activity can be a microcosm of the world economy as a whole. This approach has two important consequences. Firstly, the big picture problems of our time can become tractable through the way one conducts one's own business. Secondly, the relation to the big picture can give larger meaning to the chores of day-to-day financial management.

The courses would need to cover various aspects of entrepreneurial activity:

1) the way an activity is constituted (sole proprietor, cooperative, limited company, etc.)
2) book-keeping (balance sheet and income & expenditure account)
3) financial planning (including cash flow management) for a period of, say, 5 years.

The intended outcomes as regards finance would be the ability:

a) to understand double entry bookkeeping
b) to read a set of accounts
c) to identify and propose remedies to capitalisation and other financial problems
d) to pre-audit one's own business.

At a minimum, the courses would need to be accompanied by workbooks detailing the borrower-entrepreneur's progress. But these could also provide a context for essays, presentations and other means of sharing their projects as they unfold. These assignments could also be marked to the standards of a mainstream, prestigious university, adding the possibility of borrowers also getting educational credits.