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Impact Investing Landscape Scan

Syntrinsic Social Capital

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Context

The Gates Family Foundation, a $500M private family foundation based in Denver, Colorado, commissioned Syntrinsic to conduct a landscape scan of the foundation community's engagement in impact investing. This scan represents one of the tools that the Foundation's Board will consider as it crafts its strategic plan.

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Defining Impact Investing

To provide consistency and clarity through this project, it is helpful to appreciate the spectrum of tools and strategies that comprise "impact investing." The framework below provides a high-level context for defining the impact investing space that sits between classic investing and traditional philanthropy. Classic investing emphasizes optimizing risk adjusted returns while philanthropy involves distributing capital toward mission without any expectation for a financial return.

Impact investing describes the array of strategies that strive to integrate financial and social objectives. As the graphic below highlights, many impact investing options (e.g., Responsible, Sustainable, Thematic) strive to achieve competitive returns. There are some impact investing options (i.e., Impact First) that prioritize the depth of impact over financial return.

While the framework below serves as a helpful guide, impact investing is not a rigid concept. For example, some investors might focus on classic investing and yet strive intentionally to include investment managers from underrepresented groups such as women or people of color and/or leverage the power of their stock ownership through shareholder advocacy to promote environmental, social, and governance factors. Most importantly, each foundation needs to clarify what impact investing means for their organization.

Classic Investing	Responsible	Sustainable	Thematic	Impact First	Philanthropy
Competitive Returns	Competitive Returns	Competitive Returns	Competitive Returns		
	ESG Risk Management	ESG Risk Management	ESG Risk Management		
	Sustainable Investment Opportunity	Sustainable Investment Opportunity	Sustainable Investment Opportunity	Sustainable Investment Opportunity	
			Higher Impact Solutions	Higher Impact Solutions	Higher Impact Solutions
Emphasis on profit maximization without regard for Environmental, Social, and Governance (ESG) factors or personal values	Consideration of values and/or ESG risk to screen out investments	Targeting investments positioned to benefit from the integration of ESG factors and broad based macro trends	Focus on where social or environmental needs offer commercial growth opportunities for market rate return	Emphasis on the optimization of social or environmental needs (e.g. PRI) which may result in financial trade off	Where social and/or environmental needs outweigh any consideration for financial return

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Methodology

This scan is not intended to be all-inclusive; as such, we have not attempted to survey all foundations of comparable size and/or intent. Rather, we have focused on developing a deeper understanding of the broad spectrum of types of impact investing engagement—including little or no such engagement—by identifying and conducting in-depth interviews with 20 foundations from Colorado, the Western US, and the United States more broadly. Characteristics of the subject group include:

Formal Interview Subjects	
Total Number	20
Colorado Foundations	4
Private Foundations	15
Family Foundations	5
Largest	$12.5b
Smallest	$10m
Primary Range	$200-600m

To gain a candid perspective from representatives of these foundations of both achievements and challenges, we committed to maintaining confidentiality. Still, occasionally in this white paper we may reference specific sources with their explicit permission.

In addition to the 20 in-depth interviews, we held conversations with ten foundation and sector leaders though more informal interviews. These discussions offered additional insights regarding trends and opportunities in impact investing across the region and around the country.

We also gleaned information from publicly available foundation white papers, websites, blogs, and other publications. Since many foundations that are engaging in impact investing seek to share their learnings with the field, several such foundations provide publicly available documentation of their process.

Importantly, almost all the foundations considered in this landscape scan have a perpetual time horizon and seek to outpace inflation net of their distributions. We did not interview subjects intentionally spending down their corpus or explicitly seeking to accept what would be considered a concessionary return on their investments.

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Key Themes

The interviews surfaced several key themes relevant to foundations in general, regardless of how they approach impact investing specifically. While each interviewee offered unique, insightful perspectives, we only defined as "themes" those observations that emerged from multiple subjects. While not all these themes are actionable, they provide insight into the challenges and opportunities that many foundations are confronting.

Recognizing that foundations generally include the diverse perspectives and authority of multiple stakeholders and decision-makers, the themes tend to highlight topics around which there was some degree of disagreement and debate amongst foundation decision-makers as well as between foundations.

We have loosely grouped these Key Themes around six primary topics.

1. Impact investing: trend or fad?

Some perceive that all investing has societal impact, or framed another way, that impact is inevitable. For those investors, the primary question is what type of impact they want to have on the world and their role of ensuring the world is left a healthier, better place because of the investments that they have made. The key decision points for investors committed to impact revolve around how one measures that impact, how intentional one wants to be or even can be regarding the nature of that impact, and then, what that intentionality would inspire one to do differently.

Others do not look at investing through that same lens, focusing instead on investing as means to an end with purely financial purposes to maximize charitable giving over time. Some subscribe to the notion that traditional investing's societal benefits occur through its allocation of capital to well-run companies meeting society's needs and the good that comes from the charitable distributions made from a growing corpus. They might even argue that the increased awareness of investors' Environmental, Social, and Governance concerns is already changing how companies behave and thus is being incorporated into market behavior anyway.

While these views continue to inform foundation decision-making, even impact investing's critics acknowledge that there is broad-based, growing interest in impact investing, particularly amongst foundation staff and younger board and investment committee members.

Despite growing interest in impact investing, there are those who see the growing interest in and utilization of impact investing as a short-term "fad" that has been accelerated recently by Wall Street's marketing machine. They do not see the movement of assets toward impact

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investing as a sustainable trend. This thinking tends to be most prevalent amongst older and wealthier foundation stakeholders who are white.

Interestingly, many people who have been active in impact investing for several years would not describe Wall Street as an ally or advocate for authentic impact investing. Some see that the broader consumer demand for investments that align with their values incentivizes the industry to create or rebrand products designed to meet that demand but only superficially "greenwashing." For example, a traditional investment manager can suddenly claim that it uses Environmental, Social, and Governance factors in its stock-picking without changing its methodology. Similarly, a traditional utilities fund can be rebranded to appear as a socially aware renewable energy fund without materially changing the portfolio development process or holdings.

In a sense, both critics and advocates of impact investing are cautious about how quickly the field is evolving, though for very different reasons. Many critics of impact investing see impact investing as a fad that runs the risk of hampering a foundation's ability to meet its long-term financial objectives. Meanwhile, many advocates of impact investing are concerned that inauthentic actors will only make it harder for well-intentioned investors to increase the positive social impact of their investments.

2. Mission + Values

Foundations that have started exploring in statements and/or actions how their investments might align (or not) with their mission and values often find themselves needing to explore more deeply what is meant by the mission and values. While many foundations now have mission statements, sometimes those statements do not provide sufficient guidance for decision-making related to investing. And while most foundations are guided by values, many times those values are not explicitly defined, especially as those values relate to investments.

Making decisions around impact investing compels many foundations to call out shared values in a way that other foundation activities may not. This step can take time, surface uncomfortable topics, cause conflict, and otherwise become a frustrating experience. Concurrently, the process can be stimulating and generative, particularly for foundations seeking to engage younger generations in the foundation's activities and governance. It can help everyone get on the same page and move forward with greater intentionality.

These discussions compel many foundations to wrestle with what a foundation's role in society should be. That role is defined in part by law and the tax code, in part by donor intent, and in part by how the various decision-makers approach the foundation's social responsibility. It is important to note that there are a growing number of outspoken foundation leaders strongly advocating that foundations must be 100% impact oriented. In

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their minds, there is simply no excuse for a foundation to do anything less. While that view is perceived as too extreme by some, with more and more foundations moving in that direction,[1] and given anticipated generational shifts in governance, that approach could shift from fringe to mainstream relatively quickly.

Similarly, impact investing raises differing perspectives around what it means to be good stewards of a foundation's financial resources. Whether family members or independent stakeholders, most foundation trustees, committee members, and professional staff have a shared commitment to being good fiduciaries. For some, that fiduciary responsibility points away from investing for any reason other than financial return; for others, that same fiduciary responsibility points toward the need to maximize the societal impact of all financial resources. At both extremes, decision makers can assume that those who have differing views do not take their fiduciary responsibility seriously, which often is inaccurate and can make these discussions more fraught than they need to be.

3. Decision-Makers and Influencers

Given all the issues surfaced above, it is no surprise that many interviewees highlighted complexities related to the board, investment committee, staff, and outside advisors. Specifically, several noted that organizations seeking to move along the impact investing journey needed to have an internal champion with real power and influence driving the process. That champion could not be an outside advisor or consultant, though those outside colleagues could be resources and partners. Many (including key staff) noted that even key staff could not carry the torch effectively in the face of board resistance.

Several staff-level champions of impact investing expressed frustration at the slow pace of progress their organizations were making, particularly at the board level. For some senior foundation staff, the lack of progress with engaging in impact investing is a major source of job dissatisfaction. Some staff interviewed for this project sought express assurances that their comments to that effect would be confidential.

While such dynamics can be present in any organization and can affect other elements of foundation decision-making, the tension that can emerge around impact investing can be particularly acute. For example, for organizations explicitly committed to climate change, health care access, or social justice, events in 2020 highlighted the intensity and time-sensitive nature of addressing those issues. If one agrees that we must make material progress on climate in the next decade or if one sees a need for immediate progress on social justice or immediate access to health care, the often-plodding decision-making timeline of foundations can be immensely frustrating.

[1] US SIF Repost on US Sustainable and Impact Investing Trends 2020 and 2018

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Investment advisors, consultants, and Outsourced Chief Investment Officers (OCIOs) were mentioned by several interviewees. In some case, those outside advisors brought substantial impact related resources in terms of education, research, access to investments, and impact investing experience. In other cases, these outside advisors—sometimes referred to as "Gate Keepers"—were staunchly opposed to impact investing conceptually, lacked the tools and/or willingness to engage on the topic, and did not serve as a resource for meaningfully exploring the possibility of moving in that direction. Anecdotally, some subjects referenced that the inability to be thought partners with foundations learning about impact investing was creating strain in the relationship with outside advisors. While some foundations mentioned advisors that only work with investors committed to impact investing, others work with advisors who can engage at different points along the spectrum.

4. Process

Consistently throughout the interviews, foundations used the metaphor of a journey to describe their engagement with impact investing. Even though we sought out foundations that have totally rejected the idea of impact investing, we generally found that even the most skeptical foundations are at least testing the waters with PRIs or creative tools for supporting their mission. At some level, all the foundations we interviewed are at least discussing impact investing and considering how it might be or become a part of their strategic plan. The journey metaphor recognizes that there is not an obvious linear path that would apply to all foundations moving from traditional to holistic impact investing. While on one hand, this flexibility enables each foundation to chart their own path, it can also enable foundations to avoid hard conversations or put off making concrete decisions with regards to how they want to approach impact investing, if at all.

Given the metaphor of a journey, each foundation's experience is quite different. And given that the field of impact investing—the advisors, the investment managers, the evaluation and measurement tools—is rapidly evolving, the pacing and intensity of these journeys can vary wildly. A committed board chair or well-regarded CEO can move a foundation toward holistic impact investing in just a year or two. In contrast, a board can learn about and even verbally commit to impact investing for several years and yet fail to make any meaningful progress in that direction.

5. Defining Success

Across the board, the foundations we interviewed reaffirmed a commitment to maintaining spending power in perpetuity. While some foundations—impact oriented or not—have sunset provisions or a willingness to wind down over time, the subjects in our data set were all committed to financial longevity. We had expected that at least a few of the foundations engaged in impact investing would have been planning on some financial tradeoff in the

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portfolio target return; we did not find any subjects willing to sacrifice portfolio level return for increased social impact.

Even as all the foundations we interviewed remain focused on investing for financial longevity, some remain willing to make targeted individual investments with a concessionary return to achieve an impact-first objective. In these situations, the foundations need to carefully balance the size of that concessionary component of the portfolio to ensure that the rest of the portfolio can carry the burden of its financial objectives. Several foundations that focus on impact do so without using concessionary return investments as one of the tools.

While traditional measurements of financial success remain a top priority and are closely tracked, most organizations are still working out how they will define their impact objectives and measure their success against those objectives. To some degree, the reporting and evaluation gap reflects the youth[2] of the impact investing field and its fragmentation. That said, there are some common impact research providers and measurement tools (i.e., SDGs, Impact Management Project, Standards of Evidence) gaining traction within the sector[3].

While some foundations strive to craft their own measurement tools, many in the field recognize the need for commonly accepted metrics that can allow for more peer level comparisons and can help the field mature. Traditional institutional portfolio measurement went through that process with the development and evolution of Modern Portfolio Theory in the second half of the 20th century and then the increased computing power that allowed many of today's commonly used risk and return metrics to become commonplace. The impact investing space is early in that process.

[2] Global Impact Investing Network (GIIN), Bass, Dithrich, Sunderji, and Nova, *The State of Impact Measurement and Management Practice*, 2020
[3] Rockefeller Philanthropy Advisors, Godeke and Briaud, *An Implementation Guide for Practitioners*

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Approaches to Deploying Capital for Impact

Through these interviews, we have identified four general approaches to deploying capital for impact.

Grantmaking	Grantmaking Plus	Integrating Impact	Holistic Impact

1. Grantmaking

Mindset (*“We’ve always done it this way. If it ain’t broke, don’t fix it.”)*

Many foundations remain focused on maximizing their impact through the grant dollars that they distribute. Most private foundations remain focused on the IRS-mandated 5% distribution rate, though from time to time, some foundations might briefly exceed that required distribution. For example, in 2020 some foundations temporarily increased their distributions due to COVID-19 and/or society’s growing awareness of social justice issues. Additionally, some foundations increased their grantmaking portfolio in 2020 based on recent higher-than-expected returns from their investments. For example, a few private foundations we interviewed increased their charitable distributions from 5% up to 10% for at least one year due to heightened concern about social, economic, climate, or health issues and/or because their portfolios had exceeded return expectations significantly.

Highlights

Traditional Grantmaking

While many foundations are devoting considerable energy to new and different ways of deploying capital, all grant makers acknowledged that grantmaking remains the most flexible tool for impact. Because no financial return is expected, grant makers can deploy capital with only impact objectives in mind. Of course, that does not mean that every grant is impactful; still, as a tool, it remains the central—and for some foundations, only—means of generating impact.

Tools Within Grantmaking Budget

Within their grant making budget of roughly 5%, some foundations deploy part of that capital in the form of low interest loans and/or recoverable grants without necessarily structuring such commitments as PRIs. These options allow the foundation to adapt to help solve

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problems in a manner that traditional grantmaking may not address as effectively or in a manner that better meets the foundation's needs.

Balance Sheet

While not very common, some foundations leverage their balance sheet to provide guarantees that enable nonprofit organizations to secure capital from other sources. For example, one family foundation uses its balance sheet to help guarantee loans to nonprofits for capital projects. In this case, the foundation is not actually deploying capital, but its guarantee attracts capital that otherwise would avoid making the loans given the risk.

Strategic Increases to Grantmaking

While it is not uncommon for a foundation to tactically make grant distributions above the required 5% of assets, some foundations have elected to materially increase their distributions for a longer period to increase near-term impact on the problems they strive to address. In our survey, three foundations stated that they increased their grant spending to address emergency needs due to COVID and social justice issues.

For example, one private foundation elected to raise their grant distributions to 10% of corpus for three years (2020-2022), with the additional 5% going to specifically fund issues related to equity and social justice. It is important to note that the private foundation in question already viewed equity and social justice as central to its mission; thus, this was not a situation of mission expansion. In addition, this foundation only made this decision after analyzing the likely impact on long-term growth of the corpus, recognizing that it would be highly unlikely that the foundation could earn enough to cover the increased distribution. This foundation is less concerned with perpetuity than most of the other private foundations in our sample, making the strategic shift easier for them to adopt.

2. Grantmaking Plus

Mindset (*"Impact is nice, but we need to make money."*)

Some foundations are willing to use investment capital in a more impactful manner, but primarily on the margins and with considerable risk-aversion. They generally are concerned that focusing on impact inherently undermines the primary objective of maximizing risk-appropriate financial return. Some of these Foundations are well-aware of expanded efforts in impact investing, but do not have confidence in its efficacy.

Most often, these foundations are using Program Related Investments (PRIs) to complement their traditional grantmaking, giving them a more flexible way to structure their financial support of nonprofit organizations. Generally, PRIs are debt or equity investments made into

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a nonprofit or nonprofit venture with the potential for investment return, albeit often concessionary (i.e., below market rate) in nature.

In some cases, PRIs are made from the grantmaking portion of the portfolio. Some foundations treat their PRI dollars as if they were grants, with little expectation that the capital (or any associated interest payments) will be returned. Foundations that make PRIs from their grantmaking portfolio are not really increasing the amount of dollars going to impact, just attaching strings to the way they make distributions.

Several of the foundations we surveyed make PRIs above and beyond the grantmaking portion of their portfolio. Some include those PRIs as part of their total investment allocation when setting asset allocation policy and evaluating performance, while others view the PRIs as sitting outside their investment portfolio in a sort-of limbo between investments and grants.

Highlights

PRI (Debt)

Many interviewees noted that their foundations primarily use PRIs as debt capital, providing short-term financing to nonprofits for capital projects and/or to launch or expand programs. In some cases, PRIs can serve as a bridge loan during a capital campaign or while awaiting government reimbursement. Many foundations structure PRIs with a high likelihood that a material amount of capital will be returned and potentially "recycled" for use with other beneficiaries.

PRI (Equity)

Some interviewees expressed frustration that most foundations use PRIs primarily as a debt/lending tool rather than as an equity tool. They argue that using a PRI to take an equity stake in an initiative can be a more meaningful way to support the foundation's mission and the financial needs of their grantees. That said, the interviewees focused on equity investments tended to not structure such investments as PRIs, but as direct equity investments. That private equity-like approach requires a mindset that we tend to see amongst foundations taking a more holistic approach to impact investing.

Market-Based ESG and/or MRI Integration

One of the most common approaches to low-risk impact investing involves the integration of Environmental, Social, and Governance (ESG) factors or other Mission Related Investment (MRI) criteria into the portfolio, usually in the public market equity and debt allocations. The majority of the 20 foundations we interviewed use at least some ESG integration.

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For example, one foundation integrates ESG investments as a way of addressing their mission around climate change. In their case, they started with a goal of having 50% of the assets integrate such ESG screens; recently, they increased that goal to 90% of their assets. In addition, they are starting to explore next steps beyond ESG integration. Even in doing so, however, they noted that they are not sure how much of an environmental impact they are having with this decision. Both advocates and critics of impact investing are struggling with this question.

In general, several foundations have used ESG or MRI integration into public market portions of the portfolio as an entry point into impact investing. Given the many tools available for doing so, ESG or MRI integration can be incorporated with relatively modest workload and at essentially no financial cost, making it a relatively low-risk way to strive to increase impact and mission alignment.

De Minimus (<2%) Carveout

One foundation we spoke with has committed to exploring different impact investing tools with 1% of their assets. They are educating themselves on different possibilities for how to utilize that 1%, including the possibility of adding PRIs. While some impact investing advocates are quick to downplay the value of such efforts, we have seen this initial step transition to much bigger commitments over time. One of the organizations in our scan started with a 2% commitment to impact investing in 2014 and has since grown that commitment to over 60% of the portfolio. Still, it took a few years with that more modest allocation before that foundation got comfortable considering broader and deeper commitments. Most of that move happened from 2018 – 2021 after the board set a quantifiable target and made a more holistic commitment to impact investing.

Limited Partner Co-Investing

Two foundations specifically referenced investing in impact related opportunities initiated and led by other foundation partners, though again on the margins. For these foundations, making modest commitments as limited partners to impact specific deals created an opportunity to mitigate risk in several ways:

1. Using relatively small dollar amounts
2. Deferring to the General Partner for structuring and leading the deal
3. Reducing headline risk by investing alongside several other foundations

This type of co-investment also provides the non-financial benefit of sharing ideas and learning. Even limited partners become part of the knowledge-sharing and reflection that can emerged from co-investing, enabling them to become more experienced funders in their areas of interest.

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We have witnessed considerable growth in this type of impact co-investing in the family office space, so it is natural that it would be expanding into the foundation sector as well.

3. Integrating Impact

Mindset (*"We use multiple impact tools but we're not ready to go all in."*)

As foundations start to prioritize impact investing objectives alongside their financial objectives and grain greater confidence in the potential ability of impact investing to meet both objectives, we start to see more significant integration of impact investing tools.

Frequently, such foundations identify a portion of their investment portfolio with which they try to achieve both financial and social impact. While their colleagues earlier in the process (i.e., Grantmaking Plus) might dip their toes in the waters of impact investing with 1-2% of the portfolio, foundations that are integrating impact are making more meaningful commitments in terms of both the tools they are willing to use and the relative size of those allocations.

Foundations in this category often use the tools referenced above while starting to integrate more creative and/or complicated tools as well. As the notes below highlight, this stage can lead to much more complicated leadership and governance challenges.

Highlights

Decision-Making

While some organizations have made a commitment to move toward integrating impact investing more meaningfully into their investment strategy, several pointed out that there can be complications that arise along the way that create a gap between intention and implementation. Of course, this situation is true of traditional investing as well, though impact investing adds new dimensions to the challenge.

For example, one foundation spoke to their ten-year journey of moving toward integrating impact, a journey complicated by family dynamics, challenges with attracting and retaining capable outside advisors and consultants, and prioritizing impact tools. While they are now starting conversations about integrating impact across most of their investment portfolio, in many regards they are still figuring out how to successfully implement the tools and allocations to which they have already agreed.

Venture Funds

Two of the foundations in our sample have launched separate venture funds. While still a part of the parent entity, these venture funds are dedicated to making high impact direct investments that are strongly mission-aligned. Though the parent entities still use other impact tools in other parts of the portfolio, the venture funds are designed to be 100%

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committed to impact related risk-taking, though still with the potential for market rate returns.

Carve Out Allocation

Some foundations have identified a targeted allocation within which they are implementing impact investing tools, leaving most of the portfolio invested in a more traditional manner. For example, one large foundation ($1B) has created a meaningful "carve out" allocation that they are using intentionally to test out impact related concepts with the idea of transitioning those concepts across the entire portfolio. For this foundation, the partial commitment enables them to build experience, knowledge, and confidence as they move through the journey.

Foundations this size and larger often express concern that they are too big to holistically approach impact investing. Some argue that there simply is not enough worthwhile impact investing product available yet; as a result, they have decided that they must maintain a large traditional investment portfolio until the market adjusts to accommodate their need for more impact investments. Thus, while some are using the carve out as a step toward a more holistic approach, for others, this may be as far as they want to go with impact investing for a longer period.

Diverse Managers

Some foundations—and what seems to be a growing number—are extending their impact investing to include more intentional consideration of investment managers led and/or owned by women and people of color.[4] Their commitment tends to extend from recognition that investment management firms owned and/or led by women and people of color manage a de minimus amount of the assets under institutional management. For some, intentionally seeking out investment managers from groups underrepresented in the investment industry is part of promoting equity and wealth building. For others, seeking out diverse managers is an effort to access skilled managers who might have been overlooked by the industry not because of ability, but because their demographic profile is inconsistent with what the industry expects.

Some nonprofit organizations have instituted a policy like the "Rooney Rule," a guideline named after a former owner of the NFL's Pittsburgh Steelers whereby every NFL team with a head coaching, general manager, or other senior front office vacancy must interview at least one diverse candidate. These foundations are challenging themselves and their advisors to bring forward more diverse investment managers. We do not have data on the degree to which this policy ultimately leads to the inclusion of more diverse managers in portfolios.

[4] Knight Foundation, *Diversity of Asset Managers in Philanthropy*, February 2020

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Other foundations have quantified their commitment to diverse managers. For example, a few have made a "25% by 2025" commitment (i.e., Kresge Foundation Pledge)[5,6]. Some—including a few in the scan—define this as allocating 25% of total Assets Under Management to diverse managers. Others have caveats that focus on specific asset classes (e.g., 25% of the US equity assets). Interestingly, some have noted that it can be easier to identify diverse managers in the private investment space due to barriers to entry in the traditional asset classes.

Local Private Investment Focus

Given the ability to target impact more precisely, some foundations focus their impact investment efforts in private rather than public markets.

One foundation takes a particularly rigorous localized approach. This foundation is strongly committed to its local urban community, one that has long struggled with disproportionate poverty and inequity. The foundation makes private equity investments in companies that are willing to move their operations to their local community, creating jobs and economic activity that can be a significant multiplier of the foundation's impact and economic investment. These investments in private companies are not concessionary and are not structured as Program Related Investments.

General Partner Co-Investing

While we referenced Limited Partner Co-Investing in Grantmaking Plus as a lower risk way to engage in impact investing, General Partners of impact-oriented co-investments generally take more risk and are more deeply engaged because they are initiating and structuring the deal, leveraging their reputation and networks to secure support from the limited partners, and often dedicating personnel and other resources to administration, reporting, and monitoring of the investment. While sizing remains a variable that can help foundations manage their risk in such endeavors, the GP bears meaningful responsibility regardless of the dollars involved in the deal.

The development over the past decade of social impact or pay-for-success bonds has created a mechanism through which foundations can activate not only their own capital and capital from other foundations, but also capital from government and private sources. For example, one foundation in our survey is developing a social impact bond related to workforce development. By the time they introduce the opportunity to potential financial partners, the lead foundation will have invested considerable time and money in structuring the deal. Still, assuming the deal moves forward and achieves most of its aims, the foundation will be able

[5] Kresge Foundation, *Kresge Foundation Launches "25% by 25" Pledge*, April 2, 2019
[6] Association for Black Philanthropic Executives, *The Investment Manager Diversity Pledge*, 2019

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to point to an impressive multiple of financial impact given their ability to leverage other dollars and hopefully improve community economic activity. While that financial multiple would not be captured on a portfolio performance report, it could be captured on a report that measures impact.

Shareholder Advocacy

Some foundations take the concept of integrating ESG or MRI factors one step further by advocating as shareholders for policies aligned with their mission and/or values. Most of the foundations that are incorporating shareholder advocacy are doing so via investment managers that they are using to get access to parts of the portfolio. For example, some ESG oriented investment managers actively engage with management of their portfolio companies to help drive policies that support that managers' values-based mandate and ideally can unlock additional financial value. Some foundations engage with third party partners like As You Sow to vote proxies on the foundation's behalf. Still others delegate proxy voting to their advisors. While it is certainly possible for a foundation to rely on its own staff or board members to vote its proxies, doing so can be a laborious task. None of the foundations in our survey indicated that they vote proxies themselves.

4. Holistic

Mindset (*"We want to maximize the impact of every investment decision."*)

In a holistic approach, a foundation has embraced the concept of activating essentially all its capital to maximize its impact and values alignment. Foundations that have come to this place generally have determined that doing anything less than activating the entire portfolio for impact is not enough to address the social issues of greatest concern.

Foundations with a Holistic Impact mindset approach portfolio construction with a dual mandate of meeting the foundation's financial goals and its social goals throughout the portfolio development process. For example, a few foundations noted that they now look at the role impact plays in every investment decision—the asset allocation strategy, the selection of investment managers, the definitions of success.

Even when making this commitment, foundations still must make several decisions:

- How is the foundation defining "impact?"
- Which investment tools is the foundation willing and/or able to use?
- How will the foundation select its investments?
- How will the foundation evaluate, measure, and report upon the impact of its investments?
- How public does the foundation want to be about its stewardship efforts?

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- To what degree, if any, does the foundation want to share its experiences with other investors, particularly other foundations?

This holistic approach should not be defined solely by measuring assets currently allocated to impact-specific strategies. Given the ongoing evolution of impact investing tools, differing definitions of impact, and the deliberate (if not slow) nature of change in the foundation and investment communities, some organizations may have adopted a holistic impact mindset while still being only part-way through the journey in terms of how their assets are invested today. For example, it can take many years to unwind a traditional private equity portfolio and transition those assets to more intentional impact-oriented private equity.

Highlights

Values Clarification

Foundations that are starting to explore impact investing can use some of the tools without necessarily clarifying their values or long-term impact objectives. However, many of the foundations that have embraced a more holistic approach have some process of defining and regularly re-evaluating their values and mission. Because a holistic approach represents a more significant commitment to integrating impact across the portfolio, it requires a foundation to really know what it is trying to accomplish. Only then can the foundation align its board, committees, staff, outside advisors, and investment managers toward those impact goals.

Impact Evaluation

Generally, impact evaluation remains in its early stages. Foundations along the spectrum of impact investing sometimes dabble in different ways of measuring or evaluating impact, such as reviewing impact reports from the handful of investment managers that prepare them. In practice, however, many foundations that are in the first stages of integrating impact investing still focus their evaluation practices on purely financial metrics, for example, comparing the performance of an ESG oriented active manager to a traditional market index like the S&P 500.

Many of the foundations that have adopted a more holistic approach to impact also are adopting tools for evaluating their impact in a more disciplined, consistent manner. Some foundations are developing their own frameworks for this evaluation process, whether by retaining outside consultants or doing the work in-house. Other foundations are using tools that are gaining greater adoption across the impact investing sector. For example, many advisors and foundations are starting to rely more heavily on the Impact Management Project (IMP) evaluation framework, a forum for building consensus on measuring, managing, and reporting impacts on sustainability.

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As a part of their evaluation strategy, some foundations use data from database providers such as MSCI or Sustainalytics to score publicly traded companies. While critics of impact investing point out that the differences in these databases highlight inconsistency in how impact is measured, others point out that its natural—and even healthy—to have some variance in the frameworks to keep pushing the field forward in quality and accuracy.

Foundations with a holistic approach to impact investing will need to adopt some manner of disciplined evaluation to hold themselves accountable to their impact objectives. We have seen tremendous growth over the past few decades in how foundations evaluate the impact of their grantmaking specifically; we expect the sector will even more quickly adopt and improve tools for evaluating their overall impact.

Place-Based Impact

Some foundations focus on how they use their location to leverage impact. As mentioned earlier, one foundation in our survey is deeply dedicated to investing in companies that they then help move to their economically distressed city. Another foundation concentrates its impact investing efforts in the county in which they are located, which is generally underserved by philanthropy. While most foundations continue to locate their offices in city centers alongside banks and other financial institutions, some taking a more holistic approach are at least discussing how they can use their location to better leverage their social impact.

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Next Steps

Foundations have an opportunity to optimize their portfolios to strive to meet both financial and impact objectives. A steadily growing number of foundations are participating actively in developing impact-oriented investment policies, become early adopters of impact-oriented investment products, convening with other funders, and participating in the development of impact measurement tools. Others like the concept but are watching from the sidelines, waiting for the field to mature or for their decision-makers to evolve. Still others are not sure if this impact investing trend has legs or substance; they need to see even more hard evidence of its dual success before they make any changes to their investment philosophy. And still others are simply going to stay focused on maximizing financial objectives so they can grow the roughly 5% that they distribute each year.

Neither the capital markets nor the social challenges we face will be getting any easier in the decades ahead. More than ever before, however, foundations have a wide array of tools for determining the impact they want to have on the world. We anticipate that in the next few years, many foundations will be asking themselves to what degree they want to:

- Convene and educate other funders on their mission-alignment journey
- Invest in mission-aligned field building through grantmaking and investments
- Help structure sustainable investment ideas that make capital more productive and attract capital from private, public, and nonprofit sectors alike
- Broaden stakeholder engagement so the future foundation incorporates diverse voices and perspectives

The energy around impact investing is growing and we anticipate that such growth will only intensify in the years ahead. Still, as with any movement, there can be peer pressure to delve in before one really knows what one wants to accomplish. We encourage foundations to approach their deliberations about impact investing strategically and intentionally while remembering that innovation and entrepreneurship created much of the wealth that foundations steward. In its best light, impact investing can empower foundations to return to their roots in innovation and entrepreneurship.

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