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CHAPTER 6

Wielding Your Endowment for Good

For many years, philanthropy and investing have been considered separate disciplines—one championing social change, the other financial gain. The idea that the two approaches could be integrated within the same transaction—in essence, delivering a financial return while doing good—has generally struck most philanthropists and investors as far-fetched. Not anymore.

Impact investing, which seeks to generate social or environmental benefits while delivering a financial return, is expanding as a promising tool for investors and philanthropists. Some estimates value the impact investing market at nearly $9 trillion in the U.S. alone. As the problems societies face become more entrenched and complex, it's clear that government and philanthropy can't solve them on their own. A look at the amounts of capital involved bears this out: in the U.S., philanthropy amounts to approximately $390 billion annually, government spending is $3.9 trillion, and capital markets (all debt and equity investments) encompass $65 trillion. On a global scale, total investments are estimated at $300 trillion. Thus, a 1% shift in global capital markets toward impact investing—or investments that work toward social good—could cover the estimated $2.5 trillion annual funding gap to achieve the United Nations' Sustainable Development Goals (SDGs). As this example shows, harnessing capital markets can substantially benefit society.

This kind of investment that works toward social good while seeking financial returns can be a valuable tool for philanthropic organizations to unlock additional avenues for sustainable impact. It offers a way to leverage financial resources for social and economic returns by making investments that align with philanthropic goals and intentionally deploying capital in enterprises, funds, or projects that generate positive social or environmental outcomes while seeking financial sustainability.

The Rockefeller Philanthropy Advisors Impact Investing Handbook

For a deeper dive on starting your impact investing journey, Rockefeller Philanthropy Advisors published the *Impact Investing Handbook: An Implementation Guide for Practitioners* to help asset owners turn interest into action. This practical publication features case studies and detailed guidance for individuals, families, foundations, and corporations. It features input from over 50 experts and practitioners.

The *Handbook* covers:

- *The Why* – Developing a theory of change by merging impact goals with investment goals.
- *The How* – Building or shifting a portfolio using the full range of impact tools and structures.
- *The So What* – Measuring success through leading principles, frameworks, and standards.
- *The Now What* – Crafting a realistic implementation plan by following best practices.

The Growth of Impact Investing and Why it Matters to Philanthropists

Over the past 15-plus years, impact investing has moved from the financial fringes to become an essential part of an equitable philanthropic approach. It is robust, worth trillions of dollars, its staying power is evident, and its potential for driving change is undeniable.

Impact investing provides a tool for achieving social good with a broader array of assets than traditional philanthropy. Private foundations in the U.S., for example, can achieve social good with not only their 5% required annual payout but also the 95% endowment corpus that remains invested. To put this in perspective, U.S. foundations make annual grants totaling $60 billion while holding assets totaling $865 billion.

The Bridgespan Group writes, "Impact investing offers an alternative to philanthropists who reject the notion that there is a binary decision between investing for profit and giving money to a social cause. While traditional grantmaking often overcomes market-based failures, impact investing leverages the power of markets to create change. As you think about the social problems you seek to address, consider impact investing as one of the many tools at your disposal."

- **Market size and staying power.** Impact investing is not a passing trend. In the United States alone, sustainable investing accounted for more than $17 trillion in assets in 2020, a figure expected to grow exponentially.[1] This vast market size has made impact investing an integral part of the global financial landscape.
- **Development of specific tools and approaches.** The evolution of impact investing is marked by the development of unique financial tools. Social impact bonds, green bonds, and ESG funds have multiplied, offering investors diverse ways to align their portfolios with their values. These instruments have expanded the reach of impact investing from

[1] "U.S. Sustainable Investing Tops $17 Trillion, a Third of Assets under Management." ImpactAlpha. November 16, 2020. https://impactalpha.com/u-s-sustainable-investing-tops-17-trillion-a-third-of-assets-under-management/.

institutional investors to individuals.

- **Increasing focus on social challenges.** The popularity of impact investing reflects a broader societal shift toward acknowledging and addressing pressing global issues, such as climate change, income and other types of inequality, and global pandemics which highlight disparities. The impact investment approach offers a way to tackle these challenges head-on, with substantial and sustainable change available to those who leverage their endowments for good.

Aligning Investments with Mission

Many endowed foundations do not use their endowment to fulfill their mission. In the U.S., many private foundations distribute 5% of their assets annually. This means 95% of assets are often not used to further the foundation's mission. With the rise of impact investing, the opportunities for foundations to align their investments with their missions are expanding. There has been a significant push for equity and racial justice equity lens investing, particularly after George Floyd's murder and subsequent world events.

The Benefits of Impact Investing for Philanthropists

- It's a powerful tool for leveraging philanthropic dollars. Investment returns can be reused over and over again to compound the impact.

- It allows donors greater freedom and flexibility to test innovative ways to achieve a financial return as they seek impact.

- Donors use it for breath new life into or complement their philanthropic strategy—many report great satisfaction after incorporating impact investing as a central element in their approach to social change.

- When applied to specific social causes, impact investing also has the potential to bring more capital and fresh approaches to targeted issue areas. For example, efforts are growing to coordinate impact investing with the 17 Sustainable Development Goals (SDGs), 15-year global goals to which all 193 UN member states, along with many businesses and nonprofits, committed themselves, beginning in 2016. The 2017 GIIN Annual Impact Investor Survey found that 60% of investors reported actively (or soon to be) tracking the financial performance of their investments concerning the SDGs.

How does impact investing help advance financial goals in philanthropy?

- Strong environmental, social, and governance (ESG) practices embraced by many social good projects may lead to financial outperformance.
- Merging investment and impact efforts can streamline strategy and help achieve returns (as well as effects) with larger pools of money.
- Investors can bring market-based approaches to bear on the social causes they care about while avoiding making investments that oppose their values.

How can philanthropy help advance impact investing?

- Philanthropy can pave the way for promising investments that don't yet attract pure investment capital due to higher risk, an unproven track record, or an uncertain return timeline. In this case, philanthropy can provide risk, early, or patient capital. One example is a loan guarantee allowing a social enterprise to access credit at a favorable rate.
- Over the past few decades, philanthropy has honed one of the most challenging aspects of impact investing: impact measurement. Philanthropy can coordinate with impact investors to appropriately evaluate impact, which can then be measured along with the desired financial return.
- Philanthropy can help develop, scale, and professionalize the impact investing field through education, training, research, and infrastructure building.
- The combination of impact investing and grants helps catalyze meaningful change, proving that doing good and financial performance are not mutually exclusive but can go hand in hand and benefit and uplift each other. One example is Appalachian radical grantmakers "the Waymakers Collective," who chose a local fiscal sponsor to keep their money in the area and used it to invest in affordable housing alongside annual rounds of trust-based grantmaking.

Guiding Your Impact Investing

There are many opportunities around impact investing and many sources to help guide an organization's thinking. Ranging from environmental, social, and governance (ESG) considerations in investment decisions to mission-related investments (MRIs) and program-related investments (PRIs), each can directly align with and support an organization's mission. Understanding these terms and their implications is the first step in navigating the impact investing landscape. Each type of investment plays a unique role in a diversified portfolio.

- **Environmental, social, and governance (ESG) considerations** have steadily gained traction in the sector. As a means for measuring an investment's sustainability and social impact, ESG has slowly transitioned from the fringes of the responsible business community to being considered by mainstream investors when assessing an organization's financial strength and resiliency. These considerations are increasingly seen as essential for evaluating investment risk and opportunity. A 2017 study by the NYU Stern Center for Business and Human Rights revealed that the measurement of "S" primarily focused on what was "most convenient" rather than what was "most meaningful." Out of convenience, social issues reported in ESG disclosures primarily focus on human rights, labor standards, and gender equality, irrespective of a company's sector or footprint. While the ESG movement has made great strides since that study, and more social considerations, such as data security and employee engagement, are being explored, the challenges remain. Investors implementing ESG considerations into their strategy can potentially improve long-term outcomes by identifying companies that are leaders in their industries, well-managed, and resilient to new regulatory and market challenges.
- **Mission-related investments (MRIs)** can be a valuable tool for impact and take on a variety of shapes and sizes. Still, at their core, they are a financial tool used by foundations to place more—or all—of their assets in service of mission or impact. MRIs are typically risk-adjusted or "prudent" market-rate investments made from the foundation's endowment—or what some affectionately call the other 95%—to advance a foundation's mission across asset class and issue area. Unlike program-

related investments (PRIs), MRIs are not an official IRS designation, and different funders utilize different names to refer to this kind of impact investment.

- **Program-related investments (PRIs)** are mission-driven investments that closely resemble charitable grants and are another tool foundations can use to align their assets in service of their mission. The critical difference between MRIs and PRIs is that PRIs are essentially a program activity for tax and compliance purposes and must primarily be made to advance the foundation's charitable goal, not to achieve an investment return.
- **Fiduciary duty** is a party's obligation to act in another party's best interest. One of the most prevalent myths about impact investing suggests an inherent trade-off between achieving financial returns and impact goals. The argument posits that investors need to pay more attention to their fiduciary duty to seek maximum financial returns rather than focusing on social or environmental returns. A good example of how fiduciary duty can be aligned with equity is Casey Family Programs, which fosters diversity, equity, and inclusion (DEI) at their foundation and in their communities. Their commitment to DEI is underpinned by the "return on investment resulting from greater inclusion, in how we work to improve the well-being of America's children and families, and with our investment partners…. Integrating diversity has added tangible value to Casey in enhancing investment returns and reducing risks; its benefits are irrefutable."
- **Philanthropy can leverage vast resources** to tackle pressing social issues, engaging significant resources for meaningful change. De-risking investment in disadvantaged communities can pave the way for mainstream investors to bring significant capital into underserved areas. By combining impact investing with traditional grantmaking, philanthropy can make a more profound and lasting impact.

Shifting Systems Through Impact Investing

Impact investing and systems change are two concepts that have grown in significance in the philanthropic world, and they are more interconnected than they might first appear. At its core, impact investing seeks to generate both financial return and positive social or environmental impact. It's about leveraging capital to tackle the world's most pressing issues, from climate change to social inequality. Meanwhile, systems change refers to efforts to transform underlying structures and mechanisms perpetuating social problems. It's not about quick fixes but sustainable, long-term change. When we bring these two concepts together, the potential is enormous. Impact investing can serve as a powerful tool for systems change by financing innovative solutions, driving sustainable business practices, and influencing the behavior of other market players. As we move ahead in the 21st century, the convergence of impact investing and systems change will be increasingly critical in our collective pursuit of a more equitable and sustainable world.

Best Practices in Investment Strategy

When venturing into impact investing, taking incremental steps is essential. An organization might start by allocating a small portion of its endowment to impact investments or launching a pilot project in a familiar sector. The incremental steps listed below, when taken in order, allow organizations to gain experience, learn valuable lessons, and make course corrections before scaling up their impact investing activities.

Step 1. Start from Strength

The cornerstone of a successful impact investment strategy lies in leveraging existing knowledge and relationships. Foundations often have deep-rooted connections with a network of nonprofits, government agencies, and other stakeholders. Leveraging these relationships can provide valuable market intelligence, offer insights into potential investment opportunities, and even help mitigate risks associated with impact investments.

- **Identify areas of expertise.** Foundations and philanthropic organizations possess a wealth of knowledge in particular sectors or geographies due to their grantmaking activities. For instance, a foundation with a history of supporting education initiatives may have developed an extensive understanding of the education sector's dynamics, challenges, and opportunities. This knowledge can inform their impact investment strategies, helping them to make more informed and effective investment decisions. Seek input from impact investing experts and practitioners who can provide objective perspectives and insights. Engage external consultants, advisors, or impact investing networks to offer guidance and support.
- **Build consensus.** Building consensus among stakeholders is equally important. This includes board members, senior leaders, staff, donors, and beneficiaries. Everyone should understand and support the organization's impact investing strategy, as this buy-in is critical for long-term success. You might consider moderated focus groups or meetings with stakeholders about the types of organizations they consider essential to invest in. This allows greater transparency about intentions, co-creating the narrative, creating buy-in, and gaining intelligence from impacted populations.
- **Encourage collaboration.** Collaborating can enhance impact and effectiveness, especially with aligned partners such as other foundations, nonprofits, social enterprises, government agencies, or private companies. By pooling resources and expertise, partners can achieve more than any one organization could on its own.

Step 2. Assess and Educate

Offer resources, workshops, webinars, and presentations that explain the concept, known benefits, and potential benefits of impact investing. Share case studies and success stories to illustrate how it aligns with the foundation's mission and can enhance its philanthropic efforts.

- **Engage stakeholders.** Engage foundation stakeholders in open dialogue and discussions about impact investing. Create opportunities to share their perspectives, concerns, and aspirations regarding the foundation's mission and strategies. Encourage active participation and seek input from diverse voices, including board members, staff, donors, and beneficiaries.

- **Audit your portfolio.** Understanding the current portfolio holdings is a critical first step when considering impact investing. These audits involve identifying potentially harmful investments and seeking opportunities to invest in companies and initiatives that actively further the investor's goals. Identifying potential issues and areas of misalignment isn't an end in itself, though. After establishing this baseline, organizations can take action to rectify these issues and better align their portfolio with their mission. This might involve divesting from harmful companies or sectors and investing in those more aligned with the organization's mission.

Step 3. Demonstrate Alignment

Clearly articulate how impact investing aligns with the foundation's mission, values, and long-term goals. Highlight the potential for generating both social impact and financial returns. Illustrate how impact investing can complement existing grantmaking efforts and amplify the foundation's impact.

- **Start small and pilot projects.** Begin with small-scale impact investing initiatives or pilot projects to demonstrate the feasibility and effectiveness of this approach. Implement projects that align closely with the foundation's mission and engage stakeholders. The success of these initial efforts can build confidence and generate momentum for broader engagement in impact investing.

Step 4. Create Clear Policies for Potential Impact Investments

Creating a clear policy for impact investing is another best practice. This policy should articulate the organization's mission and values, define impact investing, set specific goals and metrics for success, and outline the decision-making process for impact investments. It should also be reviewed and updated regularly to reflect changes in the organization's strategy or the broader impact investing landscape.

When establishing criteria for evaluating potential impact investments, foundations may consider various factors aligned with their mission and objectives, such as the following:

- **Start small and pilot projects.** Begin with small-scale impact investing initiatives or pilot projects to demonstrate the feasibility and effectiveness of this approach. Implement projects that align closely with the foundation's mission and engage stakeholders. The success of these initial efforts can build confidence and generate momentum for broader engagement in impact investing.

- **Impact alignment**, to prioritize investments that directly align with their mission and desired social or environmental outcomes. They may evaluate how closely an investment opportunity addresses climate change, poverty alleviation, education, healthcare, gender equality, or sustainable agriculture.

- **Financial viability**, including financial sustainability and potential for reasonable financial returns. They assess revenue generation, profitability, market potential, and risk-adjusted returns. The financial viability of an investment helps ensure the foundation can continue supporting its philanthropic activities.

- **Scalability and replicability**, to assess the potential of whether an investment model can be expanded to reach a larger population or replicated in different regions or sectors, thereby maximizing the impact across multiple geographies or communities.
- **Measurement and evaluation.** Foundations often require investments to have a robust impact measurement and evaluation framework. They assess whether the investment provides clear metrics to track and measure social or environmental outcomes. This includes considering the availability of reliable data, indicators, and reporting mechanisms.
- **Environmental, social, and governance (ESG) factors.** Foundations may consider integrating ESG factors into investment decisions. They assess whether the investment opportunity demonstrates a solid commitment to producing positive returns and/or mitigating negative impacts across the ESG factors.

Engaging More Assets for Good

By engaging more assets for good, foundations can maximize their influence and effectively expedite their missions. While endowment investing often mandates a long-term outlook focused on preserving capital, non-endowment impact investing can afford more flexibility. This allows foundations to experiment with alternative terms, structures, and risk levels to realize their desired impact. Impact investing is not just about deploying capital but also about fostering a shift in mindset. It's about seeing every dollar as an opportunity to create positive change. This broader view of capital can empower foundations to engage more of their assets for good and unlock new possibilities for creating social impact.

"It's about seeing every dollar as an opportunity to create positive change."

Legacy and Innovation in Philanthropy

Today's philanthropy sector increasingly recognizes the role of financial investments as a legacy, in addition to traditional grantmaking. By leveraging financial assets, foundations can catalyze systems change, driving progress on pressing social and environmental issues.

This shift in perspective is ushering in a new era of innovative philanthropy. Foundations use capital to support immediate needs and prove new models for solving societal problems, acting as "innovation capital" for governments and other large-scale actors. This approach, which embraces risk, experimentation, and learning, is crucial to achieving lasting impact in our rapidly changing world.

Conclusion

By aligning investment decisions with mission-driven goals, philanthropic organizations can effect meaningful change while ensuring sustainable growth. Impact investing offers various tools and opportunities, from ESG and MRI to PRI, enabling organizations to tailor their approach to their unique needs and objectives.

Furthermore, impact investing is a powerful movement that's gathering momentum. With an increasing focus on social challenges and a market size that's continually growing, it's clear that impact investing is here to stay, as it is creating a positive impact that resonates far beyond the balance sheet.

Calls to Action for Philanthropy

As we navigate the world of impact investing and philanthropy, there are clear and actionable steps that can guide our journey. These calls to action are not just suggestions but powerful tools to foster a more effective and impactful philanthropic practice. Whether you're a seasoned philanthropist or new to this space, these steps offer a path to enhance your contribution to societal good.

- Champion impact investing. Make impact investing a cornerstone of your philanthropic strategy. Demonstrate that balancing financial returns with impact goals is possible and highly rewarding.
- Collaborate and learn. Seek input from impact investing experts and practitioners who can provide objective perspectives and insights. Engage external consultants, advisors, or impact investing networks to offer guidance and support.
- Embrace innovation. Continually seek improvement and explore new ideas. Learn from successes and failures to adapt your strategy to a changing world. Experiment with alternative terms, structures, and risk levels to realize your desired impact. Remember: Impact investing is not just about deploying capital but also about fostering new ways of thinking.

Additional Resources

Plenty of resources are available to support and guide you on this journey. From platforms that connect like-minded investors to educational materials and professional advisors, there's plenty of help. Here are some of the top resources, with a particular emphasis on those provided by the Rockefeller Philanthropy Advisors, to aid your understanding and implementation of impact investing.

From Rockefeller Philanthropy Advisors:
- *I*mpact Investing: An Introduction
- Solutions for Impact Investors: From Strategy to Implementation

Case Foundation's A Short Guide to Impact Investing

Harvard Kennedy School's Global Philanthropy Report

Global Impact Investing Network: A nonprofit organization dedicated to increasing the scale and effectiveness of impact investing worldwide.

Mission Investors Exchange: A community of foundations committed to advancing the field of mission investing.

SOCAP (Social Capital Markets): A network of investors, entrepreneurs, and social impact leaders addressing the world's toughest challenges through market-based solutions.

Toniic: A global community of asset owners seeking a more profound positive net impact across the spectrum of capital.

Case Study: Dropbox Foundation's Approach to Impact Measurement

Dropbox Foundation, established in 2016 as a corporate philanthropic grant-making vehicle, is committed to supporting global human rights organizations. A central focus is placed on unrestricted grants, skills-based volunteering, and product donations to empower its grantees in the field of human rights.

Trust based philanthropy has become a core pillar of Dropbox Foundation's work. Tina Lee, Head of the Social Impact and Sustainability team at Dropbox, explains that this choice stems from their aspiration "to make the most significant impact with limited resources." This approach reflects their commitment to ensuring that those closest to the problem they are seeking to support can drive solutions effectively.

Hannah Chotiner-Gardner, Chief Development Officer at Kids in Need of Defense (KIND), adds depth to this perspective, describing trust-based philanthropy as "a sophisticated and mature decision" that acknowledges the expertise of grantees and empowers them to lead the way in addressing complex challenges.

An important part of fostering trust is transparency and communication. Lee emphasizes the value of active listening during regular check-ins with grantees. She underlines the authenticity and informality of these interactions by asking that grantees, "don't prepare anything" because she "just wants to have an honest conversation." This approach is designed to foster a deeper understanding of what actual challenges and needs are, instead of adding unnecessary bureaucracy and paperwork.

Chotiner-Gardner explains that these frequent check-ins serve as a meaningful alternative to extensive reporting. The open and trusting dialogue allows her to address challenges and seek solutions effectively. Dropbox Foundation's effort to

Addressing reporting requirements within the context of trust-based philanthropy, Tina Lee emphasizes the need for purposeful reporting. She notes, "I do not want grantees to do anything just because they think a funder wants it," highlighting the foundation's commitment to streamlining reporting to make it more meaningful and efficient.

While unrestricted funding is highly valued by nonprofits, it can pose operational challenges. Tina Lee acknowledges these concerns but assures that they actively work to mitigate risks, stating, "We've been able to mitigate that risk through due diligence and references." This emphasizes their commitment to providing unrestricted support while addressing the associated operational complexities.

Hannah Chotiner-Gardner reinforces the significance of unrestricted support, saying, "Unrestricted support is critical to empowering an organization to make its best decisions." This underscores the flexibility and trust associated with such funding, especially in addressing unpredictable situations. As the world faces escalating and convergent challenges, that empowerment has never been more critical.