Improving the Social Utility of Philanthropic Investments

By David C. Wood

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Despite the attention and increasing use it has seen over the past decade or so, mission investing – the practice of investing foundation endowment capital in funds and projects that are intended to yield social as well as financial returns – remains a fundamental challenge to traditional foundation practice.

Those of us who advocate for increased mission investing tend to make a blend of both moral and practical points to encourage uptake, including: 1) mission investing is an imperative, as foundations are public purpose entities and favored with tax exempt status because they turn financial resources into social benefit; and 2) mission investing is useful because it expands the resources traditionally considered available to foundations to achieve their organizational goals. If these claims are true, then foundations that do not engage in mission investing are underperforming on the terms under which society has granted them special tax-exempt status.

I think that these are powerful arguments, and to some extent, the fact that mission investing remains relatively underemployed among U.S. foundations is as much a matter of dissociation – a cultural predisposition to divorce endowment management from the purpose of the foundation – as it is a rational response to the challenge.

The most common response from skeptics to mission investing is that foundations should concentrate on growing their endowments as much as possible, so as to have more money to give in grants. This isn't much more than a dodge. It assumes both that there is a non-mission investing strategy that necessarily outperforms a mission-investing counterpart, and, perhaps more importantly, that investment strategy itself should be determined without regard to the ultimate goals of the organization.

But this does not mean that hard questions about the practicability of mission investing – the costs involved in developing and managing strategies; engaging consultants, lawyers and fund managers; and identifying opportunities that create real impact – don't need answers. Indeed, one of the heartening aspects of the mission investing conversation in recent years is the turn from existential questions of whether it is possible to much more useful questions about how it can be done.

In what follows, I will outline a few of the ways in which foundation investors and related parties are thinking about mission investment in practice. I concentrate on barriers to entry for foundations considering the field, at the expense of exciting (often sector-specific) developments in strategic innovation among the more experienced mission investment community, which brings a different though related set of issues worth exploring another time. This article draws on our experience at the Initiative for Responsible Investment working with foundations and other stakeholders on the More for Mission Campaign – now with 96 foundations representing more than $38 billion in assets – as well as complementary investment organizations in the foundation and responsible investment community.

We have a window of opportunity to turn interest and excitement in mission investing into action that improves the social utility of foundation investments. If mission investing is a challenge to conventional investment practice, we in the mission investing community face a challenge in building a healthier, sustainable and resilient investment marketplace.

BUILDING INTERNAL CAPACITY

For new entrants into the field, the first step in mission investing is achieving board-level consensus on investment strategy. For these discussions to proceed beyond the level of whether mission investing is possible, board members must be convinced that: 1) mission investing will not compromise the financial integrity of the foundation; 2) mission investments have the potential to create positive social impact in line with a foundation's objectives; 3) there is a robust enough market in mission investing vehicles to commit to the practice; and 4) foundation board and staff will have the resources and expertise to oversee strategic implementation.

In our own interaction with foundation boards and individual trustees at IRI, we have found trustees who generally are open to mission investing but remain particularly concerned about the depth of the market and internal oversight capacity. Mission investing as a topic is more familiar now than it has been in the past, but the actual state of the market is much less so. The recent growth of peer networks, proliferation of publicly available investment policy statements and case studies, and easier access to reports on and databases of investable opportunities have created momentum in favor of mission investing in large part by convincing trustees that it is a world worth exploring.

Staffing and oversight remain important considerations. Foundation board members and staff rarely are chosen for mission investing expertise, though there are heartening examples where this has happened. For many board and staff members, investment is a foreign topic, removed from daily considerations and job descriptions by design, and mission investing requires education and active engagement on top of already busy schedules. A number of resources have been developed in recent years that are intended to lower the burden of mission investing adoption, but there must be an internal institutional commitment to use or develop proper resources for successful implementation.

Internal capacity can mean many things. Few foundations take on resource-intensive mission investments; most have tended to work with established investment intermediaries that they or their investment consultants underwrite for both financial and social performance. Again, peer networks have served to reduce transaction costs to some extent, as foundations and advocates share information. In recent years, more "traditional" investment consultants who work with foundations have built their own capacity in mission investing, which has significantly expanded foundations' ability to enter the market.

ENGAGING WITH INVESTMENT SERVICE PROVIDERS

Most foundations do not manage their investments themselves, but rather engage investment consultants and managers. Even those (typically large) foundations with substantial internal investment capacity have extensive interaction with the broader investment community practice. Internal capacity most often means mediating mission investment through financial intermediaries.

Though the investment consultant community is more engaged than in the past, mission investing remains a relatively small slice of the foundation investment universe, and this can pose challenges for those foundations that want to engage. Too often, one still hears stories from foundations that ask their consultants about mission investing, only to hear that it is not practical, or that it will necessarily reduce returns. In many cases, these answers reflect an unfamiliarity in the consultant community with the mission investing market, as well as an institutional bias toward conventional investment styles for which consultants already have capacity.

The relationship with consultants is complicated by the internal cultural resistance at many foundations to challenging the consultant community. To the extent that investment is seen as an external mechanism that enables a foundation's "proper" work, investment intermediaries will be deferred to as much as engaged on mission investing in particular, as well as investment strategy more generally. But recent years have seen movement. I've had more than one investment consultant say to me over the last few months that foundations are coming in to say they want to do mission investing, rather than seeing if it is possible.

The relative (or perceived) newness of the field also can complicate relationships with investment fund managers. Foundations must find ways to identify appropriate products, communicate their mission objectives and concerns to fund managers and develop oversight systems that fund managers can report to on mission impact.

The growth of and attention to mission investing (and its siblings responsible and impact investing) raises two specific concerns. First, as fund managers come to see potential in the space, they increasingly lay claim to mission impacts, raising concerns about greenwashing or ineffective delivery of social benefits. Second, mission investing, by its very nature, encourages innovative integration of financial and social objectives, and so can help encourage the development of products with idiosyncratic value propositions without substantial track records. This can be challenging for both investment service providers and foundations, as institutional investment strategies tend to favor investment vehicles with track records and readily comparable peers.

WHERE MIGHT THE FIELD GO?

As noted, the field has received a great deal of concerted attention recently, which has increased acceptance of mission investing as a practice and is, we hope, laying the groundwork for significant new pools of capital coming into the field.

Groups such as More for Mission, PRI Makers Network and Confluence Philanthropy for mission investing; the Global Impact Investing Network for impact investing, US SIF and the United Nations Principles for Responsible Investment for responsible investing, all have played a role in building legitimacy for the broader field, and in creating networks of shared information and best practices that make it easier to engage in socially and environmentally focused investing. There remains a great deal of hard organizing work to build internal capacity and expand the range of opportunities among service providers, all of which can leverage on what these advocacy networks have done to date.

Less attention has been paid to the role of foundations in shaping the structure of markets themselves. There are ways that the conversation around mission investing might inform broader discussion over the role of markets in society. Indeed, many of us think that mission investing has gained attention in part because of the weaknesses in conventional financial practice revealed by the global financial crisis. To date, this has been a missed opportunity. Mission investors have focused largely on building capacity within the constraints of conventional investment paradigms. But the very existence of the field does call into question how we can measure and improve how financial systems serve the public good. Indeed, one measure of success in mission investing is how much foundation investments can leverage other sources of capital.

Over time, I hope we find the mission investing conversation turning to public policies and investment structures that move entire markets toward more socially beneficial allocation of capital. ■

For more on the IRI, see www.hauser-center.org/iri. For More for Mission and additional resources, see www.moreformission.org. Relevant peer networks can be found at www.primakers.org, thegiin.org and confluencephilanthropy.org. For responsible investing more generally, see ussif.org and unpri.org.

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