



A SHORT GUIDE TO **IMPACT** INVESTING



ABOUT THE AUTHOR

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**WELCOME TO THE CASE
FOUNDATION'S "A SHORT
GUIDE TO IMPACT INVESTING"**

—A BASIC PRIMER TO HELP
INDIVIDUALS BETTER
UNDERSTAND HOW BUSINESS
CAN DRIVE SOCIAL CHANGE
AND CREATE SOCIAL IMPACT.



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PREFACE

A movement is afoot that represents a significant opportunity for businesses and markets to drive social value. By allocating assets toward products, services and companies that generate positive social impact, the movement toward “impact investing” has the potential to create real value both for investors and for society.

The term “impact investing” dates only to 2008, but already there has been significant growth in the number of companies, funds and individual efforts created in support of the concept. A cottage industry of associations, conferences, research efforts, advisors, consultants and platforms has grown up around the world.

And yet, many savvy and sophisticated investors remain on the sidelines, looking for ways to invest. Many high net worth individuals, institutional investors, financial and wealth advisors and even philanthropists are anxiously waiting for new opportunities to deploy capital in exciting companies and growing markets with entrepreneurs and managers who are proving they can deliver both financial and social returns.

My colleagues at the Case Foundation and I have had hundreds of conversations over the past year with investors, philanthropists and others experts, some of whom identify with the impact investing movement and many who don't. “What are the bottlenecks?” we wanted to know. “How do we get people to stop kicking the tires and ‘Just Do It’?”

WHAT HAVE WE HEARD?

We heard that a lot of work is still needed:

- A robust pipeline of investable deals;
- Better data on business and fund performance;
- Expanded opportunities for exits and the return of capital;
- Actionable research on impacts and outcomes; and
- More products and easier “on ramps” for people to get started.

We also picked up a recurring theme: many people are confused. What exactly is impact investing? How is it different from what I'm already doing?

“YOU SAY YOU WANT A
REVOLUTION, WELL, YOU KNOW,
WE ALL WANT TO CHANGE THE
WORLD.”

- JOHN LENNON

There are also the pioneers of impact investing who are clamoring for less talk, more action. We agree.

A SHORT GUIDE TO IMPACT INVESTING

This guide is intended to help bring newcomers into the game. We hope it helps high net worth individuals, family offices and others to know some of the questions, if not the answers, to determine what's right for them and what to do next to move toward meaningful, measureable impact.

We kept it short and, we hope, fun to read. We developed a flexible framework and a simple taxonomy to help people get their arms around impact investing. We have also included several profiles of impact ventures, funds and investors that you can see at [ImpactAlpha \(impactalpha.com\)](http://ImpactAlpha.com).

The guide builds on the work of great champions for this movement. The Rockefeller Foundation, Omidyar Network and many others have been pioneers in supporting the development of the field.

We hope that this guide will inform, pose questions, provide some answers and develop a robust conversation. We now invite you to help build the future of impact investing by sharing your experiences and comments to make the guide more helpful.

- Sean Greene, *Entrepreneur in Residence, the Case Foundation*



CHAPTER

01

A CALL TO ACTION

Inner city warehouses hum with production of healthy lunches for schoolchildren. Silicon Valley entrepreneurs ramp up manufacturing of solar lanterns to meet consumer demand for cheap, safe power in the developing world. Credit flows to small businesses and farmers adopting sustainable techniques to feed a hungry world.

A growing number of companies, including Revolution Foods, d.light and TriLinc, are committed to doing well by doing good. They have explicit social goals and strategies and measure their impact. Providing capital to such companies that are aligned with those intentions is what impact investing is all about.

We start with the hypothesis that business and capital markets can be a tremendous force for positive social change.

CONSIDER:

- We face urgent challenges of poverty, inequality, health and climate change, domestically and around the world.
- Neither government, nor philanthropy, even combined, are equipped to solve these problems alone.

- Entrepreneurship unleashed is powerful. We need all hands on deck, all oars in the water.
- Private capital markets reward scalable models that sustain growth, attract talent and drive cash flows.

We know how to make smart investments. We know how to maximize returns. We know how to make money. Now it's time to make money more...

Let's make money more *effective* at creating value, for every shareholder and every stakeholder. Let's make money more *fearless* in delivering on its disruptive potential. Let's make money more *willing* to take real risks for real returns.

In our giving, let's give money more purpose, more power, more impact. It's charitable to donate; it's transformative to invest in the future you want for our children's children.

If the head has been making investments and the heart giving it away, it's time to unite the head and the heart and make money more.

“NOW I’M A BELIEVER... NOT A TRACE OF DOUBT IN MY MIND.”

– THE MONKEES



CHAPTER

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IMPACT INVESTING: A (SHORT!) DEFINITION

“A ROSE BY ANY OTHER NAME WOULD SMELL AS SWEET.”

– WILLIAM SHAKESPEARE

Amid all the excitement about impact investing, we found a fair bit of confusion.

We found that people are confused by similar sounding concepts: venture philanthropy, socially responsible investing, corporate social responsibility, ESG (for environmental, social and governance reporting) and more.

We realized that first impressions matter. People’s perceptions were shaped by their first exposure to an impact investment, be it cook stoves in Africa, clean tech in California or community development in Detroit. “Well, that’s not really right for me,” was a natural reaction to specific opportunities.

So let’s take a step back. The definition developed by the Global Impact Investing Network (GIIN), the closest thing the field has to a trade association, provides a good starting point:

“Impact investments are investments made into companies, organizations, and funds with the intention to generate measurable social and environmental impact alongside a financial return.”

The figure on the following page deconstructs this statement further.

Impact investing focuses on both for-profit companies that have an explicit intent to have social impact via their business model or practices (which we called for-profit “social” enterprises) and nonprofits with revenue and earned income streams (which we called “enterprising nonprofits”).

AN IMPACT INVESTING OVERVIEW

IT'S AN INVESTMENT

Unlike a grant, there's an expectation of a *return* of capital and a range of possible *returns* on capital. Those expended returns could range from concessionary to market rate, or even to "impact alpha."

ACROSS A BROAD RANGE

Impact investments exist across:

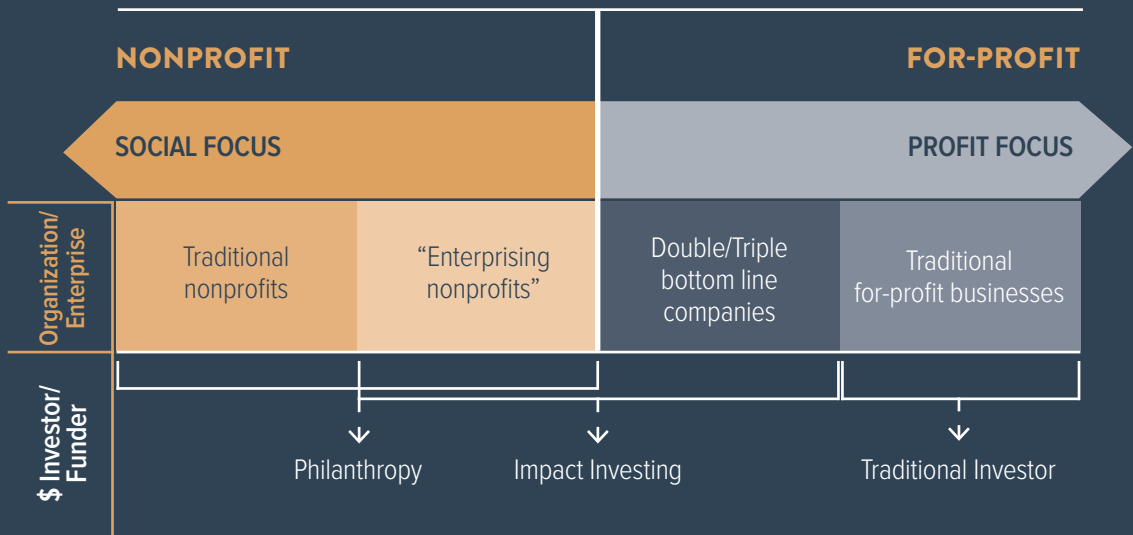
- All asset classes
- Many sectors
- All geographies

WITH A FOCUS ON POSITIVE IMPACT

The intention to generate measureable social or environmental impact puts an explicit focus on positive impact. That distinguishes the practice from "negative screens" used in socially responsible investing (SRI), where investors filter out sectors in which they do not wish to invest, such as tobacco.

ACROSS ORGANIZATIONAL FORMS

Impact companies, organizations and funds can be for-profit or nonprofit entities, which can return capital as simple loan repayments or as shares of revenues.



Certainly, large public companies generate both negative and positive impacts, and it’s possible to steer portfolios away from the former and toward the latter. But the influence of impact investments is generally more directly felt in private companies, and we will focus on small and emerging companies, rather than Fortune 500 corporations.

There are plenty of other nuances and terms to consider. Impact investments, for example, may deliver “blended value” or a “triple bottom line.” They may be mission-driven or program-related. The capital markets are nuanced and dynamic so impact investments will take on many other names. That’s okay: a rose by any other name will smell as sweet.

SPOTLIGHT

REVOLUTION FOODS

Description: Revolution Foods, a B Corp, is disrupting the \$25 billion dollar school lunch market in the United States. It provides more than 1 million healthy, nutritionally-balanced meals with natural ingredients to K-12 schools every week at prices in line with traditional lunch suppliers.

Notable Investors: W.K. Kellogg Foundation, Catamount Ventures, City of Oakland, DBL Investment Partners

Impact Geographies: USA

Social Impact Objectives: Community Development, Food Security, Health Improvement

Data provided by ImpactSpace

Photo credit: Shelly Puri







CHAPTER

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A FLEXIBLE FRAMEWORK

Many people starting to explore impact investing ask a more basic definitional question: what's in and what's out?

Twitter has enabled massive social change, most dramatically during the Arab Spring. Does that count? How about my investment in that educational technology startup? Or in the restaurant that serves local, organic and healthy food? Which of my investments count as impact investments?

SO, WHAT COUNTS?

Some investors argue that much or all of their investing has social impact, and certainly they desire that impact to be positive. The companies they invest in create jobs, provide services and meet needs. Perhaps they even deploy screens to filter out socially negative investments and try to embed their values in their portfolios. Such investments and investors are certainly “Impact Motivated.”

To meet the basic definition of impact investment, we must match intentions for proactive impact with measurement of those results. Many organizations such as B Lab are creating impact certification regimes with third party, objective standards and verification. Such regimes exist in other sectors—USDA standards for organic food,

LEED standards for buildings, Forest Stewardship Council certification for lumber and so on.

Building objective criteria within a single sector, such as organic food or green building, is hard enough; comparing impact across sectors such as education, community development and food security remains very much a work in progress.

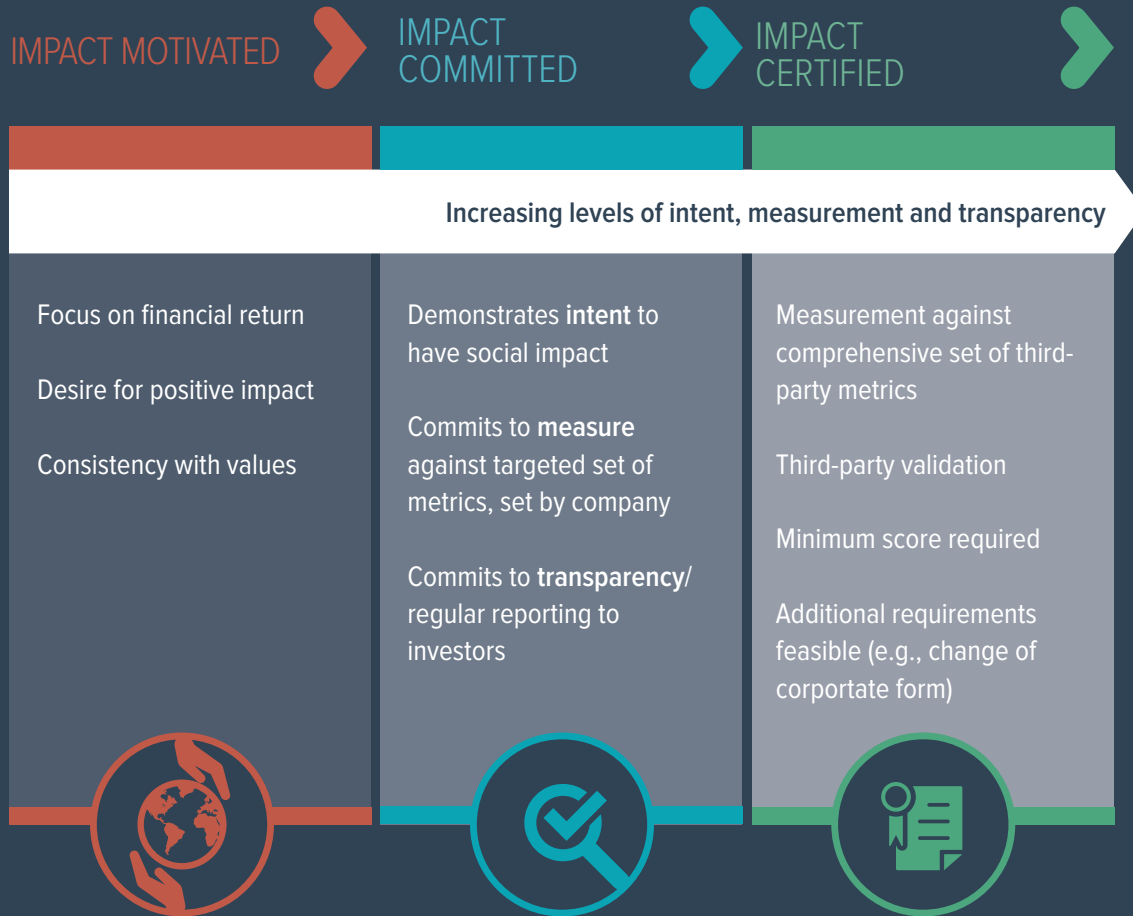
As a general validation of the importance of impact for some investors, nearly two dozen states have adopted legislation to enable the establishment of for-benefit corporations, or Benefit Corps, that commit companies to social benefit goals of their own choosing. Some of the laws require certification by third parties such as the nonprofit B Lab, which certifies B Corps.

Even for-benefit status and B Corp certification can be complex and time-consuming. Some investors worry that the process can distract entrepreneurs, particularly in early-stage companies. Assessments are often not actionable enough for many investors, with too much information in some areas, but not enough to gauge key performance indicators. Investors and companies alike are calling for simpler standards and more targeted metrics.

“WHAT GETS MEASURED, GETS DONE.”

– MICHAEL LEBOEUF

IMPACT INVESTING SPECTRUM



FROM “IMPACT MOTIVATED” TO “IMPACT CERTIFIED”

The spectrum from “Impact Motivated” to “Impact Certified” highlights increasing levels of intent, measurement and transparency. We think it’s helpful to recognize a middle ground that we call “Impact Committed.” The category recognizes that many high-impact companies don’t subscribe to formal assessments of their metrics, and it may help more companies go to “the next level” of impact measurement.

In the Impact Committed category, companies set their own impact goals and metrics, whether they be three or 300. Already, B Lab reports that for every company that seeks certification as a B Corp, another 15 (non-certified) companies make at least some use of their assessment platform. The self-selection of standards and metrics recognizes the breadth and complexity of potential social impacts.

Even without certification, impact assessment is core to companies such as Sanergy, which is improving sanitation in urban slums in Kenya by franchising toilets to microentrepreneurs and repurposing waste as fertilizer. Living Goods, a nonprofit operating in East Africa, distributes products designed to fight poverty and disease. In order to measure their impact, they are performing a randomized clinical trial to determine whether child mortality really falls in their door-to-door sales areas. Warby Parker, the maker of high-fashion eyeglasses that donates frames in developing countries, and Happy Family, with its line of affordable, organic baby food, are both certified B Corps.

Importantly, this spectrum can apply both to companies and investors.

We hope this evolving framework can broaden the impact investing tent by balancing simplicity and complexity. Our intent is to help move forward by:

- Creating a **clear line** for a minimum standard.
- Leveraging the power of **measurement**. As many have observed, what gets measured gets done.
- **Building an on-ramp** that allows individual companies and investors to evolve to higher standards over time.
- Encouraging both **top-down and bottom-up approaches** to metrics
- **Enabling flexibility** so investors can focus on what they care about.
- Responding to the market. Rather than waiting for a perfect system, a **basic framework** will help more people get into the game and evolve over time based on market signals and how investors allocate their dollars.

Over time, the act of committing to measure and reporting outcomes would differentiate companies from “socially neutral” ventures. An ed-tech company that is Impact Committed could, for example, target a handful of metrics around improving learning outcomes in underserved communities. That may not resonate with all investors, but it could make the difference for impact investors.



CHAPTER

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YOUR CENTER OF GRAVITY

A private equity fund targeting microinsurance for African families emerging from poverty. A venture capital “grand slam” in a residential solar installer with a pioneering financing model. Low-cost loans to bring fresh groceries to inner city food deserts in California. A new revenue sharing model to boost the income of small farmers in Belize through exports of sustainable—and delicious—cacao.

The nature of these investments varies tremendously, but they are each targeting and measuring social impacts. Their stories (respectively LeapFrog, SolarCity, California FreshWorks fund and Maya Mountain Cacao) can be found at ImpactAlpha.

There also will be judgment calls. For example, Greyston Bakery in Yonkers, NY, provides employment, skills and resources to lift people out of poverty. “We don’t hire people to bake brownies, we bake brownies to hire people,” is the company’s slogan. At an impact investing conference a few years ago, an attendee recoiled at the idea that making brownies could have a positive social impact, with an obesity epidemic plaguing disadvantaged communities. One

person’s job creation engine is another person’s sugar-laced poison.

YOUR GRAVITATIONAL PULL

Rather than focusing on boundaries, however, we prefer to think about the gravitational pull—the underlying force of attraction that pulls one body to another. The metaphor was suggested by Tim O’Reilly, a leader in the open source, Web 2.0 and Gov 2.0 movements. Gravitational pull keeps it all together, he says, even if sometimes a comet will enter or leave the solar system.

We started out thinking we could create a new kind of Myers-Briggs style personality test that investors could use to create their own profiles and identify the kind of impact investments that are right for them. Instead, we adapted earlier work to create a framework to help investors find their own centers of gravity around a handful of variables that will frame their impact investing decisions.

“DIFFERENT STROKES FOR DIFFERENT FOLKS.”

– SLY AND THE FAMILY STONE

SPOTLIGHT

GREYSTON BAKERY

Description: Greyston Bakery has for 30 years operated a sustainable baked goods business while maintaining a commitment to providing employment, skills and resources to people regardless of educational attainment, work history or past social barriers.

Impact Geographies: USA

Social Impact Objectives: Capacity Building, Community Development, Income/Productivity Growth

Data provided by ImpactSpace





Maria



CHAPTER

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WHY: IMPACT SECTORS

For many people, finding a center of gravity starts with identifying specific social issues about which they are passionate.

We're not talking about tiny niche markets. Impact investing opportunities abound across sectors that together constitute significant percentages of any country's GDP, including:

- Community development
- Small business finance
- Health and wellness
- Education
- Microfinance and financial inclusion
- Sustainable consumer products and fair trade
- Natural resources and conservation
- Renewable energy and climate change
- Sustainable agriculture and development

There is tremendous diversity within each of these sectors and many ventures tick more than one box. Sanergy's Fresh Life toilets improve sanitation in the slums of Nairobi, but also support livelihoods and sustainable agriculture. Happy Family's organic products emphasize healthy babies, but the company is committed to make the products accessible to low-income mothers. AFRIPads adapted a reusable and sustainable menstrual

pad—originally designed for eco-conscious North America women—for African girls, helping them stay in school.

Impact sectors aren't limited to what sometimes are labeled as “progressive” causes (e.g., fair trade) but include more traditional sectors as well. Some areas such as community development are well-established, with many players and billions of dollars of capital committed annually. Other opportunities are still emerging and have newer financial instruments and arrangements.

Many of these impact investment sectors align with ongoing philanthropic efforts, opening the way for layered capital structures and mutual leverage. The W.K. Kellogg Foundation, for example, carved out a \$100 million mission-driven investment fund from its \$8 billion endowment and has made more than 20 impact investments across education, health and financial security in places including Michigan, Mississippi, New Mexico and New Orleans. Foundation leaders say Kellogg's investments in companies like Revolution Foods and Happy Family, and funds such as Core Innovation Capital, an early backer of Progreso Financiero, have made Kellogg a better grantmaker as well.

“WHY NOT INVEST YOUR ASSETS IN THE COMPANIES YOU REALLY LIKE? AS MAE WEST SAID, ‘TOO MUCH OF A GOOD THING... CAN BE WONDERFUL.’”

– WARREN BUFFETT



CHAPTER

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**WHAT: IMPACT ACROSS
ASSET CLASSES**

“IF OPPORTUNITY DOESN’T KNOCK, BUILD A DOOR.”

– MILTON BERLE

Most investors diversify risk and manage their financial portfolio by allocating their assets across distinct asset classes.

Impact investment opportunities exist across asset classes, from cash to fixed income to public equities to private equity, venture capital and real assets. The argument, popular a few years ago, that impact investing constitutes its own asset class has mostly given way to an approach that treats impact as an investment philosophy within existing asset classes.

The matrix on the following page, originally developed with the Rockefeller Philanthropy Advisors and subsequently expanded by ImpactAssets, demonstrates the variety of impact investment opportunities, both between and within sectors. The nature of a loan fund for charter school networks, after all, is very different than a venture investment in an ed-tech startup, though both may produce positive educational outcomes.

Beartooth Capital has taken advantage of investor interest in real assets—western ranches—to raise two funds that have an explicit intention of setting aside large tracts for conservation. SolarCity started out as a

venture capital-backed startup, and a sometimes shaky one at that, before becoming a \$5 billion NASDAQ-listed public company—and an acquirer of other impact startups.

The California FreshWorks fund has raised senior and subordinated debt from major banks and insurance companies, but also functions as a fixed income investment for individuals through the Calvert Foundation’s Community Investment Note (which pays one percent for a three-year note).

There are two fundamentally different ways to approach the matrix. One approach starts with the traditional asset allocation framework (the “columns”) and looks for opportunities to “upgrade” impact within any given asset class.

The other starts with a desired impact in a specific sector/issue area (the “rows”) that you are passionate about and then searches for investment options across asset classes to help you achieve that outcome. You can use the framework to prioritize asset classes and sectors that interest you—and cross off those in which you don’t want to invest.

IMPACT INVESTING FRAMEWORK

KEY VARIABLES FOR EVALUATING IMPACT INVESTMENT OPTIONS

WHY Social Issues	WHAT Asset Classes				
	Fixed Income	Absolute Returns	Private Equity/ Venture	Public Equity	Real Assets
Community Development					
Small Business Finance					
Health and Wellness	Ex.: California FreshWorks				
Education					
Microfinance/ Financial Inclusion			Ex.: Progreso Financiero		
Sustainable Consumer Products and Fair Trade	Ex.: Maya Mountain Cacao				
Natural Resources and Conservation					Ex.: Beartooth Capital
Renewable Energy and Climate Change				Ex.: SolarCity	
Sustainable Agriculture and Development					



SPOTLIGHT

CALIFORNIA FRESHWORKS FUND

Description: The California FreshWorks fund is a public-private partnership loan fund that has raised over \$270 million to bring grocery stores and other healthy food retailers to communities that do not have them.

Notable Investors: Capital Impact Partners, The California Endowment, Citibank

Impact Geographies: USA

Social Impact Objectives: Community Development, Food Security, Health Improvement

Data provided by ImpactSpace

Photo credit: The California Endowment



CHAPTER

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WHERE: EMERGING MARKETS TO DEVELOPED ECONOMIES

“WHAT PEOPLE HAVE THE CAPACITY TO CHOOSE, THEY HAVE THE ABILITY TO CHANGE.”

– MADELEINE ALBRIGHT

Impact investments in emerging markets and developed economies present different kinds of opportunities for impact, as well as different sets of risk. Both involve very different deal structures, intermediaries and legal issues. And within the developing world, no two markets are alike: Latin America is different than Africa; Ghana is different than Tanzania. Investors can obviously take a portfolio approach, making decisions on how much they want to allocate to distinct geographies.

EMERGING MARKETS

Some of the biggest opportunities—and risks—in emerging markets are in providing goods and services to the four billion people at the “base of the pyramid.” These consumers, in total, represent enormous demand and often pay more for sub-standard products and services. Living Goods, for example, empowers Avon-style microentrepreneurs to sell “pro-poor” products to improve health in Uganda and Kenya.

In his day job, venture capitalist Vinod Khosla invests largely in companies focused on the U.S. market. He has created a separate fund, Khosla Impact, to invest in companies meeting base-of-the-pyramid challenges in India and other emerging markets.

DEVELOPED ECONOMIES

In developed economies, impact investing opportunities abound across the full range

of sectors we describe in Chapter 5, such as sustainability and education. Some focus on “Emerging Markets” within the U.S. The approximately 50 million people in this country with income below the poverty line represent a sizeable market for fresh food, fair financial services, preventive health care and other products.

GEOGRAPHIC DIVERSITY ACROSS YOUR PORTFOLIO



For investors who prefer to invest close to home, the California FreshWorks fund finances grocery stores in underserved communities throughout the state. Another example is that of Greyston Bakery, which targets its jobs and services to low-income neighborhoods in Yonkers, NY.

Interestingly, in some sectors like microfinance, “developing” markets are ahead of the “developed” economies.



CHAPTER

108

IMPACT FUNDS AND DIRECT INVESTING

“ALWAYS DO RIGHT. THIS WILL GRATIFY SOME PEOPLE AND ASTONISH THE REST.”

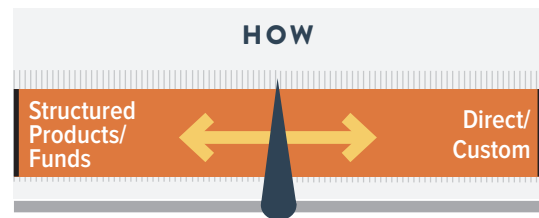
– MARK TWAIN

Like most investing decisions—whether at a large institutional investor or a small family office—there is a fundamental choice between investing into a structured product with a manager (i.e., a fund) or investing directly into deals and companies. The same options exist for impact investing.

The usual pros/cons of the two approaches apply. For some investors there are clear advantages of a structured, pooled investment product like a fund. There is upfront work to evaluate the product and the manager, but lower levels of effort for monitoring. Fund investing generates portfolio diversification within a specific investment strategy. There are additional fees to pay to the manager. Our profiles on ImpactAlpha include examples of funds for accredited and retail investors.

Investing directly avoids those fees, but requires more bandwidth. It also permits the potential for closer involvement with the enterprise. The Cordes Foundation, co-chaired by well-known impact investor Ron Cordes, has taken a combined approach—it currently invests 40 percent of its endowment assets in a balance of companies and

INVESTING YOUR PORTFOLIO



funds that generate social and environmental benefits in addition to financial returns.

Not surprisingly, fund vehicles exist across the spectrum and can provide opportunities within the different asset classes. ImpactAssets has a directory of funds that maps to the matrix, and one differentiated by geography. The GIIN has a database of funds called ImpactBase. There are a limited number of fund vehicles also accessible there as well.

In addition, there are a number of consultants and advisors who can help investors select funds or do direct deals.



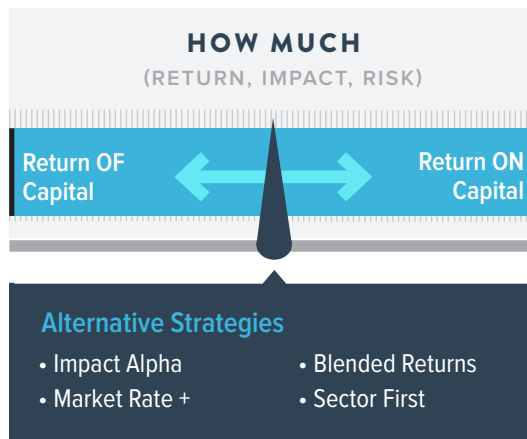
CHAPTER

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CHOOSE YOUR RISKS – AND RETURNS

It's a basic principle of investing that investors balance risks and potential returns in order to maximize risk-adjusted returns. Impact investing adds the additional variable of social impact, requiring investors to think along three dimensions.

A RANGE OF FINANCIAL RETURNS FOR IMPACT INVESTMENTS



Getting your arms around all three variables simultaneously is challenging. As the impact investor, you must answer critical questions on how much financial return you expect, how much social impact you seek and how much risk you will accept in the pursuit of financial and social return.

For a time, some experts differentiated between “impact-first” and “finance-first” investors. We

think this is too limiting—a 2D framing of a 3D problem. While waiting for someone smarter than us to perfect a 3D vision, we have found it most helpful to look at how other investors have actually struck a balance. Certain profiles and strategies emerge:

- **Blended strategies.** Some investors are willing to take lower financial returns, or perhaps higher risks for an expected return, in order to have impact. They consider the “blended” social and financial return. As one investor put it, the “sacrificed” return is equivalent to philanthropy, raising the question of whether you get more impact “bang for your buck” with an investing approach or with pure philanthropy. Another way to put it is that delivering good financial returns along with impact may mean more risk, or at least more patience or more hands-on involvement and support, which may or may not be compensated.
- **Market rate, with impact.** These investors look at these investments like any other, with the expectation of market rate return, but then filter for social impact as well. Ironwood Capital, for example, is a mezzanine fund that invests more than 50 percent of its fund in women- or minority-owned companies or in companies located in low to moderate income areas.

- **Sector-focused.** The Omidyar Network has articulated a compelling strategy of how sector-based investing can be very impactful in “priming the pump” for market-based solutions. Early investments in a targeted sector may yield dramatic innovations that provide benefits to the sector as a whole, rather than the return accruing to one specific company. They are making the early investments in the sector innovators that ultimately may yield market rate opportunities.
- **Impact alpha.** A growing number of investors are making the case that “impact” may represent a fundamental insight that

the rest of the market doesn’t yet fully value, raising the possibility of market beating returns. These investors reject the tradeoff between social impact and financial return—rather than seeing returns or impact they see returns from impact. They target investments with sustainable business models with intrinsic focus on a product or service that delivers social impact. If the businesses succeed they can deliver financial and social returns at scale. Equilibrium Capital is an example of a fund pursuing this strategy in the real assets space.

Other strategies clearly exist, and we welcome input on them.

“THE BIGGEST RISK IS NOT
TAKING ANY RISK.”

– MARK ZUCKERBERG



SPOTLIGHT

PROGRESO FINANCIERO

Description: Progreso Financiero—a CDFI fund—provides credit-building, affordable loans that enable the Hispanic community to build a better future. Progreso has provided more than \$1 billion in loans and aims to bring responsible credit access and savings to a million customers by the end of 2016.

Notable Investors: Greylock Partners, Core Innovation Capital

Impact Geographies: USA

Social Impact Objectives: Access to Financial Services, Community Development, Equality and Empowerment

Data provided by ImpactSpace



CHAPTER

10

SOCIAL RETURNS: MEASURING IMPACT

“THERE’S SOMETHING HAPPENING HERE... WHAT IT IS AIN’T EXACTLY CLEAR.”

– BUFFALO SPRINGFIELD

We all know how to measure one bottom line—but how do you measure and account for the second and third ones?

Generally Accepted Accounting Principles (GAAP) have evolved over the last 70 years or so. Given the newness of impact investing, we can’t expect generally accepted impact measurement overnight.

We must address a few core principles. First, understand the type of outcome you are looking to achieve with your investment. In “When Can Impact Investing Create Real Impact,” Paul Brest, the former president of the Hewlett Foundation and now a professor at Stanford University, and co-author Kelly Born, differentiate between the impact of the product itself and the impact of a company’s operations.

- **Product impact** is the impact of the goods and services produced by the enterprise (such as

providing anti-malaria bed nets or clean water).

- **Operational impact** is the impact of the enterprise’s management practices on its employees’ health and economic security, its effect on jobs or other aspects of the well-being of the community in which it operates, or the environmental effects of its supply chain and operations.

Second, focus on outcomes rather than outputs. For instance, Living Goods sets a specific goal: a 15 percent reduction in deaths of children under five in the communities it serves, compared to similar areas where it does not work. Intermediate outputs are the number of bed nets and malarial medicine it sells.

Some social enterprises focus on both product impact and operational impact; others focus on one or the other. As an investor, you should decide what’s important to you.

PATHS TO ACHIEVING IMPACT

PROCESS	PRODUCT/BUSINESS MODEL
<p>Are you running a business in a way that has a positive impact on your:</p> <ul style="list-style-type: none">• People/Hiring (e.g., % at living wage, diversity of team)• Environment• Community <p><i>(consistent across sectors)</i></p>	<p>Does your product or service have a positive impact?</p> <p>Examples:</p> <ul style="list-style-type: none">• CDFI – # of affordable housing units created• Number of anti-malarial bed nets distributed <p><i>(unique to sector/company)</i></p>

Finally, don't let the perfect be the enemy of the good. Even in social services supported by philanthropy and government, not all areas have developed effective outcomes measurement. In others, good definitions and measurement metrics are available, an example of which is in the definition of low- and moderate-income areas served by community development finance institutions.

For impact investing, we need both a “top-down” and a “bottom-up” approach. One example of a top-down approach is when multiple players in specific sectors agree on standards for increased income for smallholder farmers. In other areas, a bottom-up approach will work, in which individual enterprises define their own impact goals and measure and report their results. Over time, broader sector norms will evolve.



SPOTLIGHT

LIVING GOODS

Description: Living Goods is a social enterprise that empowers microentrepreneurs to educate households on improving health and to sell essential and affordable healthcare, clean energy and clean water products to low-income consumers.

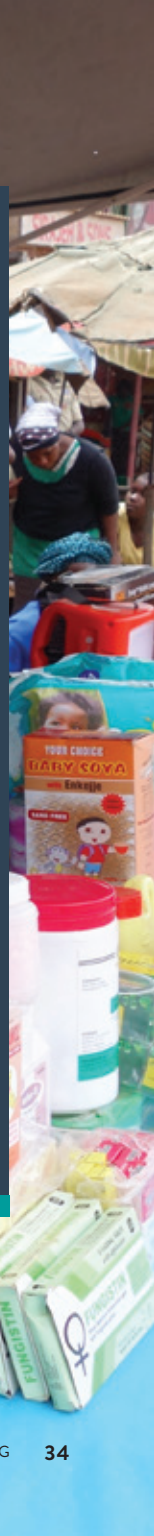
Notable Investors: Mulago Foundation, Pershing Square Foundation, Barr Foundation

Impact Geographies: Africa, Americas

Social Impact Objectives: Community Development, Employment Generation, Health Improvement

Data provided by ImpactSpace

Photo credit: Living Goods





CHAPTER

11

FINANCIAL RETURNS: TRACKING PERFORMANCE

How do impact investments perform on financial terms relative to other investments? Many investors assume they will make a lower return relative to risk-adjusted market rate returns and want to know how much. Others focus on risk and are demanding downside protection for the preservation of their capital.

Given that returns will vary by sector, geography, asset class and indeed the execution by entrepreneurs and fund managers, it may be a fool's errand to try to assess returns from impact investing as a whole. Moreover, there is no central source of data for impact investments, many of which are private. Our guess is that in some sector/asset class combinations, returns will compare favorably with "market" rates. In some cases they may be below market.

PUBLIC EQUITIES VS. PRIVATE MARKETS

In the public equities markets, there has been a significant amount of research on socially responsible investing, across a wide variety of strategies, including both positive and negative screens. According to UBS, which undertook

a comprehensive review of the research, the overall message is very clear—social investing strategies perform pretty closely to the market as a whole.

There is less data and research on private markets, but we have gotten some glimpses. Individual investors such as the Kellogg Foundation and the KL Felicitas Foundation have shed some light on their investments, publishing data on at least a portion of their returns.

KL Felicitas moved from a two percent allocation to impact investments in 2006 to more than 85 percent by 2012. A report last year that covered just over half of the foundation's holdings—in cash, fixed-income, public equities and hedge funds—concluded "impact investments can compete with, and at times outperform, traditional asset class strategies while pursuing meaningful and measurable social and environmental results." (The report did not include results from KL Felicitas' investments in private equity, real assets or so-called "impact first" investments made as Program-Related Investments in the foundation's grant portfolio.)

“GET YOUR FACTS FIRST, AND THEN YOU CAN DISTORT THEM AS YOU PLEASE.”

– MARK TWAIN

NEW DATA ON FINANCIAL RETURNS

Some individual funds have performed well relative to benchmarks, according to the Impact Investing 2.0 report from the Center for the Advancement of Social Entrepreneurship at Duke University, Pacific Community Ventures and ImpactAssets.

- Elevar Equity, for example, in San Francisco, CA, and Bangalore, India, reported a 21 percent internal rate of return (IRR) for its \$24 million Unitus Equity Fund, though much of that came from the controversial IPO of SKS Microfinance in India.
- Huntington Capital Fund II, in San Diego, CA, a growth capital or mezzanine fund, reported a 13.8 percent net IRR on its investments in small and medium businesses in underserved areas of the western U.S.
- The \$9.4 million Aavishkaar India Micro Venture Capital Fund in Mumbai, India, said it achieved a 13 percent IRR net of fees and had six exits and three write-offs.

Some industry-level research exists. For instance, Cambridge Associates has done a comprehensive study on the returns to clean tech investing from 2000 to 2012. Not surprisingly, given the bursting of the clean tech bubble, returns slightly underperformed relative to the venture market as a whole, with gross IRRs of 6.5 percent over the period. There is also significant variation within the data: later stage deals outperformed versus

early stage deals (11.3 vs. 1.5 percent); U.S. clean tech investing underperformed relative to clean tech outside of the U.S. (4.7 vs. 19.2 percent).

IMPACT INVESTMENTS MEETING EXPECTATIONS

An important benchmark may be how actual returns are performing relative to the expectations of investors or fund managers themselves. Research released by J.P. Morgan and GIIN in early 2013 suggested that organizations investing at significant dollar levels are “satisfied” with their financial returns—an important statement on the impact investing sector’s ability to deliver results at scale.

The research tracked the progress of close to 100 investors (public and private), who in aggregate manage over \$35 billion of impact investments, two-thirds of whom were pursuing market rate returns. Of those surveyed, 68 percent said their investments were “meeting their expectations” for both social and financial returns; another 21 percent said their investments were “outperforming.” The majority of investors reported they had at least one “home run”—an investment that significantly outperformed expectations while delivering the intended impact.



SPOTLIGHT

BEARTOOTH CAPITAL

Description: Beartooth Capital, a B Corp, believes that conservation adds value for investors as well as for ecosystems, and it is dedicated to the restoration, enhancement and protection of more than 25,000 acres of land in the American West.

Impact Geographies: USA

Social Impact Objectives: Community Development, Sustainable Land Use, Natural Resources Conservation

Data provided by ImpactSpace

Photo credit: Turner & Fitch



CHAPTER

12

MOVING FORWARD

Many important conversations continue in the impact investing sector. For example, a debate has broken out about “additionality,” that is, whether the same impact would have been achieved even without the presence of an impact investor(s). We have a simple position: If additionality is important to an individual investor, then he/she should factor it into their investment criteria. If not, that’s fine.

Indeed, while these conversations are important, our bias is to be more action-oriented in this emerging industry.

We favor a broad tent in which individual entrepreneurs and investors focus on the segments and areas that they care about and try to attract others to their causes. We favor an entrepreneurial approach in which we learn by doing, iterating and evolving—both as investors and as an industry as a whole. We favor a commitment to sharing lessons learned—the good, the bad and the ugly—with like-minded investors to accelerate that evolution.

WE KNOW WE ALL WANT
TO MAKE MORE MONEY.
BUT TOGETHER, WE CAN
MAKE MONEY MORE...
MORE IMPACTFUL, MORE
PURPOSEFUL AND MORE
POWERFUL IN DRIVING
SOCIAL CHANGE
AROUND THE WORLD.

“IN THEORY, THERE’S NO DIFFERENCE
BETWEEN THEORY AND PRACTICE. IN
PRACTICE THERE IS.”

– YOGI BERRA



APPENDIX

RESOURCES

For complete list of resources, visit: shortguide.org

BOOKS

The Impact Investor: Lessons in Leadership and Strategy for Collaborative Capitalism

October 13, 2014

Cathy Clark, Jed Emerson, and Ben Thornley
Jossey-Bass

New Frontiers of Philanthropy: A Guide to the New Tools and New Actors that are Reshaping Global Philanthropy and Social Investing

July 25, 2014

Lester M. Salamon, Ed.
Oxford University Press

The Power of Impact Investing: Putting Markets to Work for Profit and Global Good

May 6, 2014

Judith Rodin and Margaret Brandenburg
Wharton Digital Press

Impact Investing: Transforming How We Make Money While Making a Difference

September 2011

Antony Bugg-Levine and Jed Emerson
Jossey-Bass

Guide to Impact Investing For Family Offices and High Net Worth Individuals: Managing Wealth for Impact and Profit

Dr. Julia Balandina-Jaquier, CFA

REPORTS AND GUIDES

Private Capital, Public Good

June 2014

US National Advisory Board on Impact Investing

Spotlight on the Market: The Impact Investor Survey

May 1, 2014

Yasemin Saltuk, Ali El Idrissi, Amit Bouri, Abhilash Mudaliar and Hannah Schiff
JP Morgan and Global Impact Investing Network

Impact Investing 2.0: The Way Forward – Insight from 12 Outstanding Funds

November 2013

Cathy Clark, Jed Emerson and Ben Thornley
Pacific Community Ventures, Inc., ImpactAssets and Duke University's Fuqua School of Business

Evolution of an Impact Portfolio: From Investment to Results

October 2013

Justin Lai, Will Morgan, Joshua Newman and Raúl Pomares
Sonen Capital Press and KL Felicitas Foundation

From the Margins to the Mainstream—Assessment of the Impact Investment Sector and Opportunities to Engage Mainstream Investors

September 2013

Michael Drexler and Abigail Noble
World Economic Forum and Deloitte Touche Tohmatsu

Community Foundation Field Guide to Impact Investing: Reflections from the Field and Resources for Moving Forward

September 2013

Mission Investors Exchange

GLOSSARY

ABSOLUTE RETURNS

An absolute returns strategy is one by which a fund invests across a range of different instruments and asset classes in order to hit a specific targeted return.

ADDITIONALITY

Additionality is a term that refers to the additional impact that was achieved by the presence of an impact investor. It prompts the question of whether the same impact would have been achieved even without the presence of an impact investor.

ALPHA AND BETA

Alpha and Beta are both used by investors to determine the risk-reward profile of an investment. Alpha is the return on an investment that is in excess of the compensation for the risk borne by making that investment. Alpha is commonly referred to as the value that a portfolio manager adds beyond a fund's risk/reward profile. Beta is a measure of volatility or risk of an investment or portfolio of investments in comparison to the market as a whole.

BENEFIT CORPORATIONS

A benefit corporation is a class of corporation that voluntarily meets higher standards of corporate purpose, accountability and transparency. The nonprofit B Lab certifies some benefit corporations; a corporation certified by B Lab is called a "B Corp."

BLENDED VALUE

Blended value is a framework that evaluates a business or nonprofit based on the ability to generate financial, social and environmental value. Blended value is sometimes used interchangeably with the terms "triple bottom line" and "social enterprise."

CAPITAL STRUCTURE

The capital structure refers to the composition of funds that a firm uses to finance its operations and growth.

CORPORATE SOCIAL RESPONSIBILITY

Corporate Social Responsibility (CSR) is the commitment by business to behave ethically and contribute to economic development while improving the quality of life of its workforce and their families, as well as of the local community and society at large.

DOUBLE BOTTOM LINE

Double bottom line investments deliver both risk-adjusted market rate financial returns in addition to positive social and/or environmental impact.

ESG (ENVIRONMENTAL, SOCIAL AND GOVERNANCE)

ESG stands for "environmental, social and governance." It is a set of standards for a company's operations that socially conscious investors use to screen investments.

FIXED INCOME

Fixed income is a type of investing or budgeting style for which returns or period income is received at regular intervals and at predictable levels. The most common type of fixed income security is the bond.

IMPACT INVESTING

Impact investing refers to investments made into companies, organizations and funds with the intention to generate measurable social and environmental impact alongside a financial return.

MICROFINANCE

Microfinance refers to a variety of financial services—including loans, insurance and savings products—that target low-income clients.

NEGATIVE SCREEN

A negative screen eliminates from an investment portfolio companies that partake in practices generally deemed detrimental to society, such as arms or cigarette production.

PRIVATE EQUITY

Private equity consists of investors and funds that make investments directly into private companies or conduct buyouts of public companies that result in a delisting of public equity. The majority of private equity consists of institutional investors and accredited investors who can commit large sums of money for long periods of time.

PUBLIC EQUITY

Public equity is an asset class where individuals or organizations can buy ownership in shares or stock of a company through a public market, such as the New York Stock Exchange.

REAL ASSETS

Real assets are physical or tangible assets like land, gold or oil. They have intrinsic value due to their utility.

RISK-ADJUSTED RETURNS

A concept that refines an investment's return by measuring how much risk is involved in producing that return, which is generally expressed as a number or rating. Risk-adjusted returns are applied to individual securities and investment funds and portfolios.

SOCIALLY RESPONSIBLE INVESTING (SRI)

Socially responsible investing (SRI)—also known as sustainable, socially conscious, “green” or ethical investing—is any investment strategy which seeks to consider both financial return and social good. In general, socially responsible investors encourage corporate practices that promote environmental stewardship, consumer protection, human rights and diversity.

TRIPLE BOTTOM LINE

Triple bottom line investments deliver financial, social and environmental returns.

VENTURE PHILANTHROPY

Venture philanthropy works to build support nonprofits by providing them with both financial and non-financial support in order to increase their impact.



SEPTEMBER 2014

CaseFoundation.org