impact investing institute

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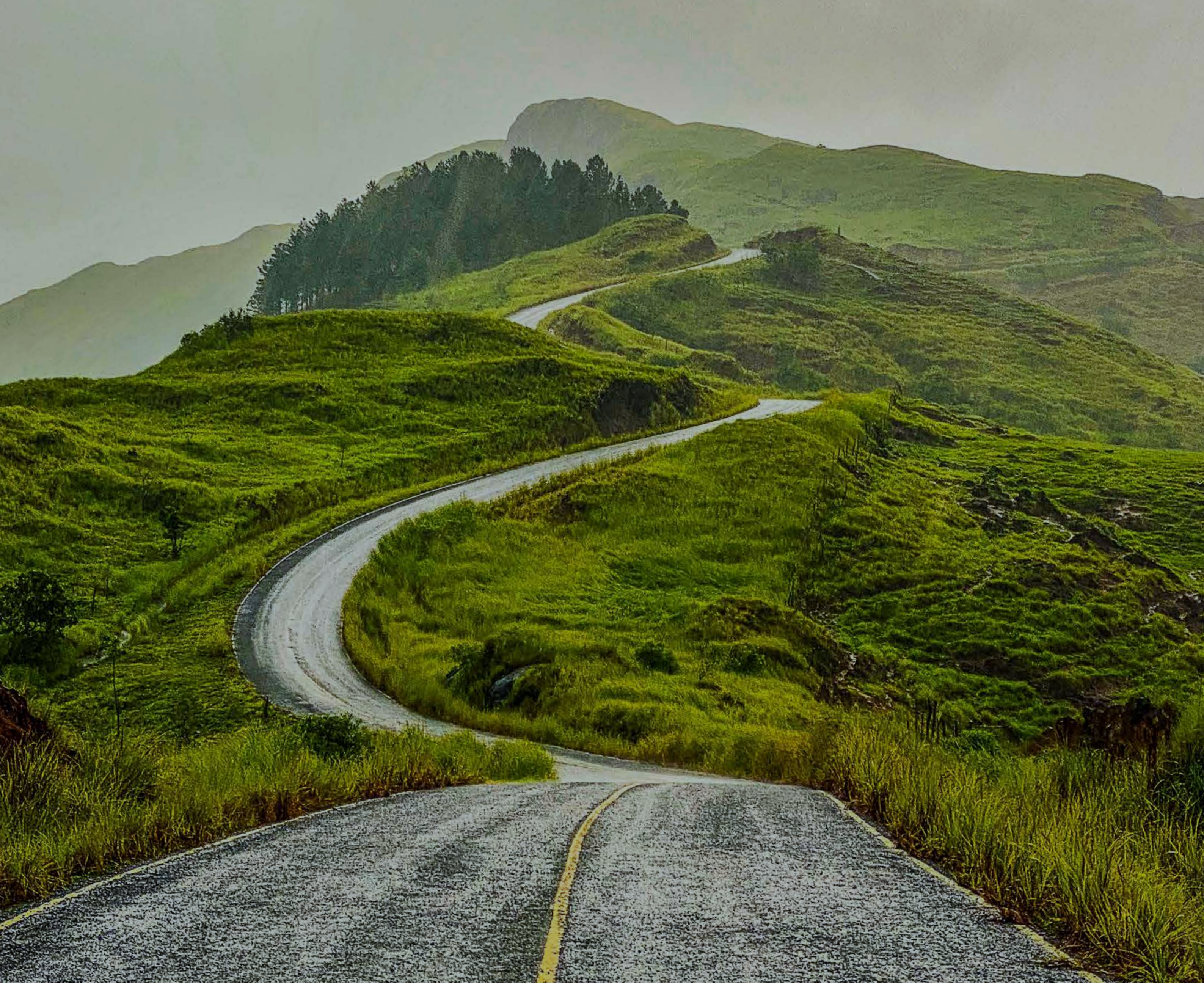
Investing with impact in the endowment: Why do it and how to get started



Esmée Fairbairn Foundation

Department for Digital, Culture, Media & Sport

About the Impact Investing Institute

The Impact Investing Institute was launched in 2019 with the goal of changing capital markets to be fairer and work better for people and the planet. We are an independent, non-profit organisation created out of two initiatives: the Government's Taskforce for Growing a Culture of Social Impact Investing in the UK and the UK National Advisory Board on Impact Investing.

We seek to create thriving capital markets where impact investment plays a central role within the financial system, enabling both private individuals and institutional investors to use their capital to target positive social and environmental impact, alongside a financial return. To do this we raise awareness of the value of impact investing, deliver research, co-create tools to help facilitate informed and targeted investment, and advocate to government for a policy environment in which investing for impact can thrive.

Everything we do is collaborative and guided by our values of inclusiveness, independence, and integrity. Our ability to deliver impact is supported by our strong networks and partnerships across the financial services industry, the social sector, and with policy makers. This project has manifested that spirit of collaboration and would not have been possible without the support and guidance of the following individuals and organisations:

Our Funders

Department for Digital Culture Media and Sports (DCMS)
Esmée Fairbairn Foundation

Our Endowments Expert Panel

Colin Baines, Investment Engagement Manager, Friends Provident Foundation
Kieron Boyle, CEO, Guy's & St Thomas' Foundation
Dame Caroline Mason, CEO, Esmée Fairbairn Foundation
Barnaby Wiener, Founder and Trustee, Treebeard Trust

Sector individuals who gave us their advice and insights

Seb Elsworth, Chief Executive, Access - The Foundation for Social Investment
Chris Coghlan, Director of Finance and Operations, Access - The Foundation for Social Investment
Chloe Stables, Director of Partnerships and Advocacy, Access - The Foundation for Social Investment
Gail Cunningham, Head, Investment Learning Programme, Association of Charitable Foundations
Luke Fletcher, Partner, Bates Wells
Oliver Hunt, Senior Associate, Bates Wells
Jonathan Brinsden, Partner, BDB Pitmans
Katie Fulford-Smith, Investor Relationships Director, Big Society Capital
Joanna Heywood, Relationships Director, Big Society Capital
Amir Rizwan, Relationships Director, Big Society Capital
Kate Rogers, Head of Sustainability, Cazenove Capital
Harry Davies, Manager, PRI Investments, Ceniarth
Greg Neichin, Director, Ceniarth
Helen McDonald, UK Head of Foundations and Impact Advisory Services, Credit Suisse
James Gifford, Head of Sustainable and Impact Advisory and Thought Leadership, Credit Suisse
Richard Bettermann, Sustainable and Impact Advisor, Credit Suisse
Peter Webster, CEO, EIRIS Foundation
Lisa Stonestreet, Head of Communications and Charity Impact, EIRIS Foundation
Georgina James, Partner, Farrer & Co
James Maloney, Partner, Farrer & Co
Danielle Walker Palmour, Director, Friends Provident Foundation
Ethan Hall, Chief Investment Officer, Guy's & St Thomas' Foundation
Matteo Yoon, Associate, Herbert Smith Freehills
Tracey Preece, Director of Finance, Joseph Rowntree Foundation
Jonathan Levy, Investment Portfolio Manager, Joseph Rowntree Foundation
Dominic Burke, Investment Director, Lankelly Chase Foundation
Carolina Minio Paluello, Global Head of Product, Solutions and Quant, Schroders
Lily Tomson, Head of Networks, ShareAction
Laura Boyle, Head of Stakeholder Engagement, Snowball
Nick Temple, CEO, Social Investment Business
Dave Gorman, Director of Social Responsibility and Sustainability, The University of Edinburgh
Shishir Malhotra, Impact Investment Advisor, Treebeard Trust
Rebecca Garrod-Waters, CEO, Ufi VocTech Trust

Executive summary

Introduction

- The largest 300 endowed charitable foundations in the UK have over £72bn in total assets – the bulk of this is invested in mainstream capital markets without impact considerations.
- A number of pioneers are seeking to deliver impact via the choice of investments in their endowments as well as through grant-making.
- However, ongoing perceptions that impact investing means concessionary returns, is expensive and complex to deliver and lacks suitable choice have deterred wider adoption.
- The Impact Investing Institute in partnership with the charitable foundation sector is seeking to change that - aiming to educate and motivate more foundations to increase the volume of charitable endowment assets invested for positive social and environmental impact as well as financial return.

Defining impact investing

- Impact investing is defined by the Global Impact Investing Network as 'investments made with an explicit intention to generate positive, measurable social and environmental impact alongside a financial return'.
- In this way, it goes beyond responsible and sustainable investment approaches and is ultimately about contributing solutions to environmental and social problems – not just managing the risks associated with them.

Legality and financial returns

- Endowed charities are legally permitted to make impact investments. Charity Commission guidance states that trustees must be able to justify why it is in the charity's best interests to invest in this way.
- There are strong legal grounds for trustees to conclude that the best way to advance their foundation's charitable purposes is to adopt an investment strategy which, alongside financial return, seeks to mitigate/avoid impacts that can undermine those purposes and mission – but also target positive impacts that support or advance the purposes and mission.
- In terms of financial return, there is a growing evidence base (much of which can be accessed via the Impact Investing Institute's Learning Hub) that risk-adjusted market rate return and impact can co-exist.
- Additionally, a wide variety of sustainability issues have been shown to be material to financial performance, including climate change, supply chain practices, diversity and inclusion, and farm animal welfare as well as having a direct bearing on a charity's purposes, mission and work.

Why should endowments invest for impact?

- There are five central arguments why it is valuable for foundations to pursue impact investing in their endowments:
  - It increases the volume of assets seeking to deliver mission and public benefit outcomes. Financial return also enables the same capital to be reapplied for social purpose, meaning the same quantum of money can be recycled to deliver more impact;
  - It can unlock new impact strategies by delivering investment activity that influences private sector practices;
  - There are growing expectations that charitable endowments will be invested in a way that is aligned with their mission and public benefit, with potential reputational danger for those that do not do so;
  - Impact investment at significant scale will drive change in the capital markets as foundations role model making market rate return and delivering positive impacts, and advocate for private sector change alongside other institutional investors, catalyzing systemic impacts; and
  - It can support prudent, long-term management of risks that can arise from sustainability issues.

Products and tools for investing for impact

- Today there is an array of products spanning public equity and debt, multi-asset strategies, private markets and real assets that are seeking to deliver both market-rate return and positive impact.
- The buy-in thresholds for investment into private markets (e.g. $250,000 for a private equity or venture capital fund) can make it hard for smaller endowments to achieve sufficient diversification in this key asset class for the impact market.
- For larger endowments, conversely, the perceived challenge is that the market may not offer investments at sufficient scale for the capital available.
- However, funds-of-funds can provide a solution for smaller investors – and as more asset allocation in impact occurs so more fund and asset class options (e.g green bonds) are coming onto the market to support scale players too.
- It is also important for public equity investors to recognise that shareholder engagement is an important impact investing tool, enabling foundations to use their voting power to drive specific outcomes and change company behaviour.

Practical steps to becoming an impact investing endowment

- Although there is no single way into impact investing, there are five domains of activity that all the practitioners consulted for this report say they have had to address in order to deliver their approach:
  - Obtain an internal mandate for impact investing
  - Establish financial and impact requirements for the endowment
  - Update the Investment Policy Statement
  - Integrate impact and investment at board and staff level to deliver the strategy
  - Work with investment advisors, investment managers and asset managers with skills and experience in impact.
- In other words – and unsurprisingly – a process of consulting with and educating all stakeholders, embedding support into all levels of the organisation and drawing on specialist expertise are all essential to delivering an impact investment approach in a sustained and effective way.

Impact in action: case studies of impact investing endowments

- The journey to become an impact investing endowment has been taken by pioneers around the world. These can be categorised into:
  - 'Carve outs' in which a proportion of the endowment's AUM is committed to impact investing opportunities with a view to experimenting with and growing the allocation over time – e.g. Esmée Fairbairn Foundation in the UK and the Ford Foundation in the US.
  - 'Total impact' approaches in which all foundation assets are managed with an intention to generate a positive impact across a broad range of asset classes – e.g. the FB Heron and KL Felicitas Foundations in the US, and Access – the Foundation for Social Investment, Ufi VocTech Trust and Guy's & St Thomas' Foundation in the UK.
  - 'Catalytic capital' which seeks to deliver capital that is patient, risk-tolerant and flexible in order to provide impact investment that may not otherwise be possible to find – e.g. US-based family office Ceniarth.

Contents

1. Introduction

In the UK, the largest 300 endowed charitable foundations have over £72bn in total assets.[1] Despite the impact investing field originating from the foundation community, the bulk of this £72bn is invested in mainstream capital markets without impact considerations, and the returns generated are distributed as grants to charities. As Danielle Walker Palmour, CEO of Friends Provident Foundation, has put it: "the reality is [for UK foundations] that most of our assets are invisible, even to us": staff tasked with the delivery of impact are sometimes focused on as little as 4% of the foundation's assets, while the remaining 96% is outsourced to external non-impact specialist investment managers.[2]

A few pioneers globally have sought to challenge this norm and deliver impact via the investments in their endowments as well as through their grant-making. In the UK, Access – the Foundation for Social Investment, Esmée Fairbairn Foundation, Friends Provident Foundation, Guy's & St Thomas' Foundation, Treebeard Trust, and Ufi VocTech Trust are notable examples; in the US FB Heron and the KL Felicitas Foundation are leaders in their field. Despite these pathfinders and several high-quality interventions by key bodies[3] there remains a lack of impact investing endowments in the UK foundation sector. Ongoing perceptions that impact investing means accepting concessionary (i.e lower) financial returns, that it is too expensive and complex to deliver, and lacks suitable products and third-party managers, have held the approach back.

However, at the Impact Investing Institute we believe that the time is ripe for change. The impact investing market itself is reaching maturity: today, evidence abounds that impact investment can deliver market-competitive financial returns alongside positive social and environmental impact across a range of investable asset classes, both public and private. Awareness of the shifts in the market are growing, with more and more charitable trustees interested to understand what a more mature impact market might deliver for their organisation. This is particularly the case given the net-zero carbon emissions agenda, and the economic shock of Covid-19, both of which have brought home the need for a massive increase in investment to help address the scale of environmental and social problems the world faces. Many within the foundation community are looking once more at their investments and re-evaluating the role they could play to deliver public benefits. As Darren Walker, President of the Ford Foundation put it: "If the last 50 years of philanthropy were defined by grant-making budgets, the next 50 must be about directing the other 95% of our assets toward justice." [4]

The Impact Investing Institute, with its focus on mobilising big pools of capital into impact, has partnered with the charitable foundation sector to help drive that change. With support from the Department of Digital, Culture, Media and Sport and Esmée Fairbairn Foundation, and working in partnership with other key players in the sector, we aim to increase the volume of charitable endowment assets invested for positive social and environmental impact as well as financial return. We believe that with the right combination of myth-busting introductory materials to impact investing, case studies of those foundations leading the way, and highly tailored stakeholder engagement, more foundations would deploy impact investing in their endowments. This practical guide to getting started is a key element of that process, helping foundation leaders and the constellation of professionals that surround them, make their first moves into impact investing. We hope that this guide helps many more institutions unlock the potential of their endowment to deliver positive impact in the UK and beyond.

1 Foundations Giving Trend 2021: https://www.acf.org.uk/common/Uploaded%20files/Research%20and%20resources/Research/Foundation%20Giving%20Trends/ACF179%20Foundation%20Giving%20Trends%202021_Design_DigitalVersion_v3.pdf

2 The pillars of stronger foundation practice: https://www.acf.org.uk/common/Uploaded%20files/Research%20and%20resources/Stronger%20foundations/ACF_investment_pillars_FINALv3.pdf

3 The Association of Charitable Foundations (ACF), ShareAction and EIRIS in particular have all created helpful resources to charities on their investment approach.

4 Darren Walker, Scaling Capital for Good: How the Ford Foundation is leveraging its endowment to finance more social good than ever before (2018) https://beyondtradeoffs.economist.com/scaling-capital-for-good-leveraging-endowment

> If the last 50 years of philanthropy were defined by grant-making budgets, the next 50 must be about directing the other 95% of our assets toward justice.
>
> **Darren Walker, President - Ford Foundation**

Who is this guide for?

This guide should be helpful to the full range of individuals and organisations that need to work together to deliver an impact investing strategy:

- Foundation trustees and their investment committees, taking the strategic decision to allocate for impact in their endowment;
- Foundation leaders, CEOs and their teams, implementing endowment strategies in step with their board, investment advisors and managers;
- Investment advisors, working closely with foundation leadership to recommend investment strategies for the portfolio;
- Investment managers, partnering with foundations and investment advisors to deliver impact investing strategies; and
- Impact investing asset managers, seeking to raise capital from foundation endowments and deliver impact through their investments.

Please note that within this guide, the terms 'trust' and 'foundation' are used interchangeably to refer to charities that have "private, independent and sustainable income that fulfils their charitable goals mainly by funding and supporting individuals or other organisations"[5]. These are endowed bodies that have the majority of their assets invested in capital markets, and a portion of the returns generated distributed as grants or applied for service delivery. This guide particularly speaks to the grant-making foundations that dominate the UK philanthropic sector, but the approaches are relevant for endowed bodies such as universities too.

What impact investing approach does the guide advocate?

Our vision at the Impact Investing Institute is for capital markets that are fairer and work better for people and the planet. We see impact-led investment by charitable endowments as integral to that transformation: although the assets under management (AUM) of the charitable endowment sector are small relative to other asset owners like pension funds, foundations can role-model new practices and exert moral pressure on other investors. Ultimately the Institute would like to see foundations acknowledge and deliver impact through their entire portfolio of endowment investments and treat the impact of those capital market strategies as assiduously as they do their grants and programmatic work.

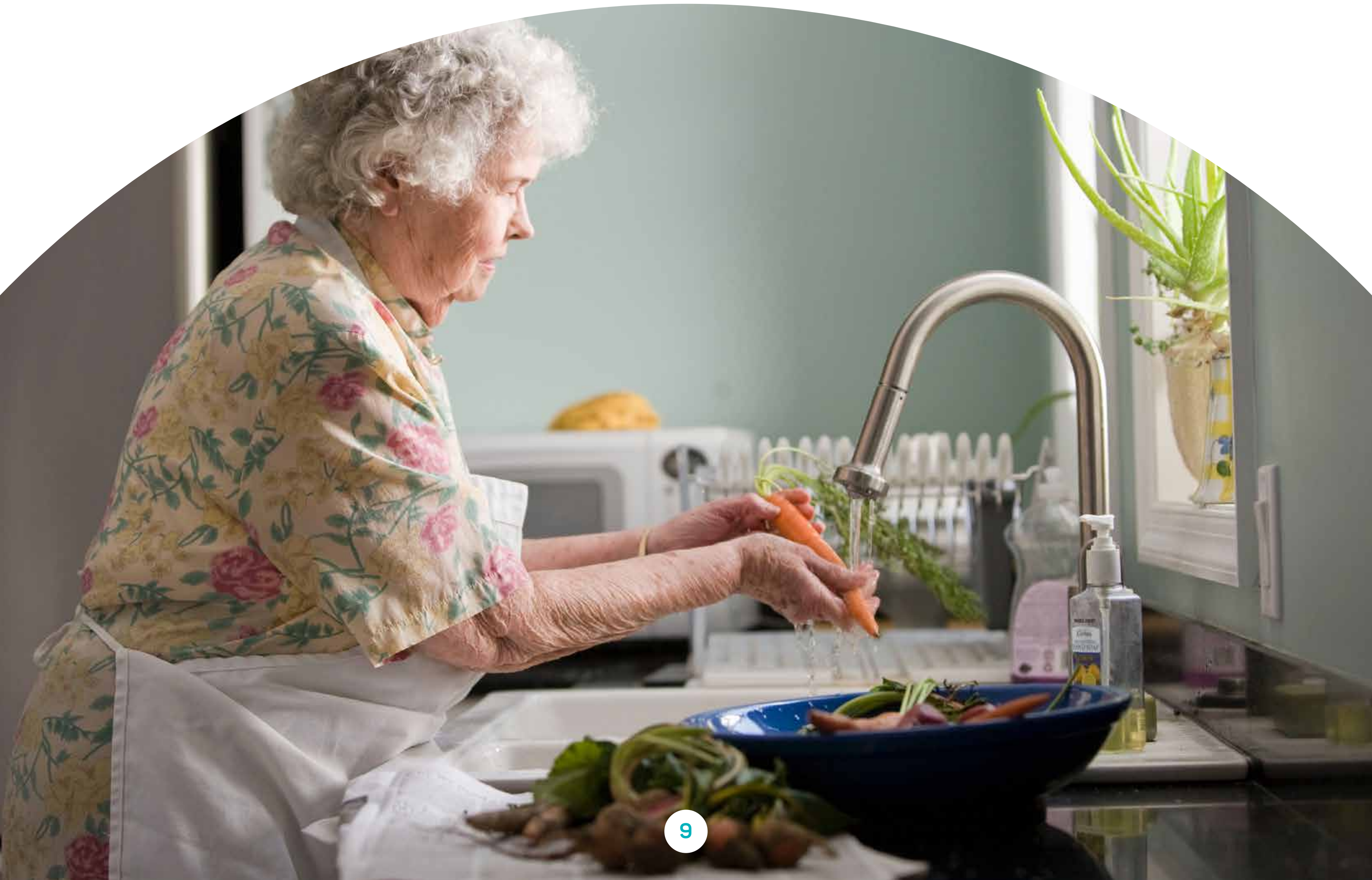
5 https://www.acf.org.uk/common/Uploaded%20files/Research%20and%20resources/Research/Foundation%20Giving%20Trends/ACF_Foundation_Giving_Trends_2019.pdf

This approach, which would steer all of a charitable foundation's investments, grants, and programmes towards delivering impact, has been described as a 'total impact approach'[6] and is associated with UK foundations already mentioned above like Access – the Foundation for Social Investment,[7] Ufi VocTech Trust[8] and Guy's & St Thomas' Foundation[9].

However, given the stage of the market's development as at late-2021, 'total impact' for the charitable foundation sector may be some way off. Part of the purpose of this project therefore is to encourage the initial foundation experimentation and exposure that might support a longer-term and more significant allocation to impact investing. To help, this guide highlights case studies and examples such as Esmée Fairbairn Foundation that has decided to allocate £10m of the endowment to market rate impact investing to experiment with it, learn from it and, over time, increase their allocation.

This guide also recognises that the scale of possible impact investing allocation will be contingent on the history and culture of a foundation as well as its size: larger-scale institutional foundations with assets of £1bn or more will have very different challenges and opportunities compared to a smaller founder-led charitable foundation with, say, £20m under management. Where appropriate, we try to identify and address those different challenges, particularly in section 5.

6 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/386335/2903051_ImpactFoundations_acc.pdf
7 https://access-socialinvestment.org.uk/blog/total-impact-blog-creation-and-crisis
8 https://ufi.co.uk/latest/investing-for-impact-how-we-transformed-our-investment-portfolio
9 https://gsttfoundation.org.uk

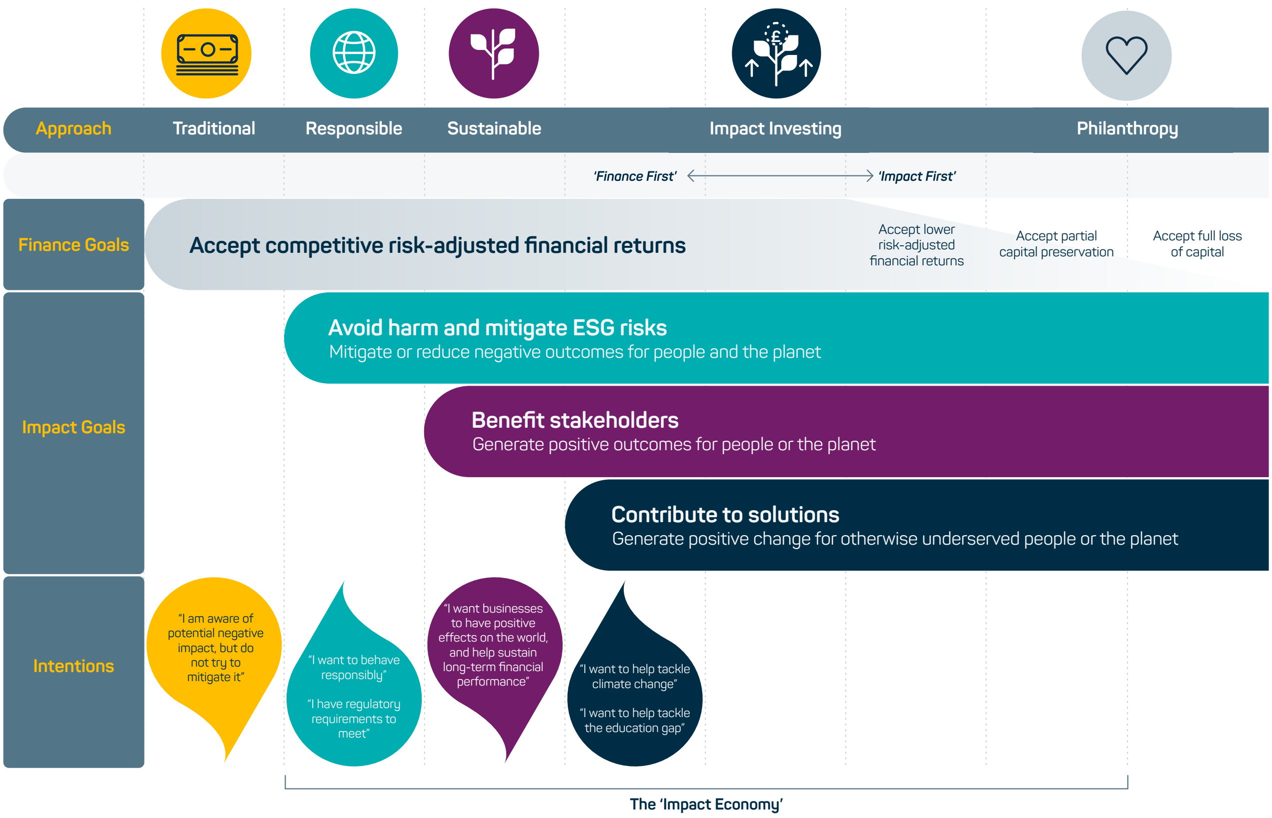


2. Defining what we mean by 'impact investing'

'Impact investing' is the original term formalised in 2007/08 by a cluster of foundations gathered under the aegis of the Rockefeller Foundation for seeking to combine financial return with delivering public benefit. Today the impact investing field has largely coalesced around the Global Impact Investing Network (GIIN)'s, definition of impact investments as "investments made with an explicit intention to generate positive, measurable social and environmental impact alongside a financial return."[10]

Impact investment sits at the middle/higher end of a spectrum of investment approaches where the balance between targeting financial goals and outcome goals progressively shifts. This spectrum ranges from traditional investing that focuses purely on financial return, through to responsible and sustainable investing (the world of environmental, social and governance, or ESG, investing) and on to impact investing, social investment and philanthropy. Bridges Fund Management detailed this spectrum in a short paper in 2017, graphically plotting the different categories of investment approach in a visual that we've included here in Figure 1.[11][12]

Figure 1: Spectrum of investment approach by financial and impact goals



Source: Bridges Fund Management and Impact Management Project.

10 https://thegiin.org/impact-investing/need-to-know/#what-is-impact-investing
11 https://www.bridgesfundmanagement.com/wp-content/uploads/2017/08/Bridges-Spectrum-of-Capital-print.pdf
12 Other credible categorisations of investment include that developed by ShareAction: https://api.shareaction.org/resources/reports/Definitions.pdf

Let's look at each of these categories in a bit more detail:

Traditional investment is only interested in maximising financial return and does not concern itself with the environmental and social impacts that that investment causes. The majority of both retail and institutional assets in the world continue to be invested in this way.

Responsible investment emerged in the anti-apartheid divest movements of the 1960s and became more formalised into "Socially Responsible Investing" (SRI) in the 1980s with a focus on 'screening out' harmful products and practices (such as tobacco or firearms). Over time, many investors have also recognised that factoring ESG risks into their investment decisions helps to protect value. This has given rise to a broad universe of 'responsible investors', ranging from those who 'negatively screen' for ESG risks, to those who actively work to mitigate them through ownership.

In the UK charitable foundation sector two leading organisations support charitable endowments seeking to act as responsible investors:

- ShareAction's Charities Responsible Investment Network (CRIN) has 20 member organisations that collectively represent more than £6bn of responsible investment assets. CRIN sees responsible investments as a way for charities to align their money with their mission and further their charitable objectives. Typically, members of this body focus on ESG strategies in the endowment. CRIN as a network engages on ESG issues such as the living wage, workers' rights in supply chains, executive pay, corporate lobbying and investment managers' voting records.[13] ShareAction is also home to a sister body: the Responsible Investment Network for Universities (RINU).[14] Currently RINU has nine colleges and universities as members. The network supports these universities to "develop and share knowledge, build a community or practice, and work together to champion social and responsible investment."
- The EIRIS Foundation[15] provides advice, support and resources to help charities and their trustees develop an ethical, sustainable and socially responsible investment approach. Responsible investment is seen as "aligning investments with mission and incorporating social, environmental and ethical issues into investments". Negative screening is considered a good first step into responsible investment. However, EIRIS also emphasises the potential for foundations to use positive screening, engagement and voting to drive positive change, as well as collaboration with other investors to pursue mission and public benefit objectives.

13 https://share-action-site.vercel.app/investor-networks/charities-responsible-investment-network
14 https://shareaction.org/investor-networks/responsible-investment-network-universities
15 https://eirisfoundation.org

Sustainable investment is described by Bridges Fund Management as 'best-in-class' socially-responsible investment: "An approach to investment where investors have deeply integrated social and environmental factors into their investment analysis and start proactively looking for ESG opportunities, selecting companies that they believe will outperform the market because they operate (or have the potential to operate) in a more sustainable way than their peers over time".[16]

Impact investment goes beyond responsible and sustainable approaches and is ultimately about contributing solutions.[17] It provides capital to help solve social and environmental problems rather than just manage the risks associated with those problems. Impact investing builds on sustainable investing in three ways:

1. **Intentionality:** Investors seek to contribute to the well-being of people and the planet while receiving a financial return. Their approach is not just about risk mitigation, it is the investor seeking a specified social or environmental outcome, which can range from decreasing carbon emissions to increasing decent local jobs in a given place. Impact intentionality means establishing an impact goal for an investment before it is made, including how its relative success or failure will be measured.
2. **Measurability:** Impact investing seeks to manage, measure and report on social and environmental outcomes with rigor and consistency. Measurement holds the investor accountable to their impact intention. Transparent and comparable measurement and reporting is also key to assessing the effectiveness of a strategy relative to its peers.
3. **Additionality:** Additionality asks that a given impact investment makes more of a difference than a "business-as-usual" approach. An impact investment should be additive: ideally, it should make an impact occur that wouldn't have happened had the investment not been made.

Impact investing is therefore an approach, not an asset class, and is a broad church too: it can be delivered in both public and private markets; it may aim for risk-adjusted market rate returns or have a concessionary target (i.e where financial return is potentially sacrificed to achieve a social or environmental benefit); and be applied to the majority of impact goals that a foundation might seek to deliver against.

Impact-driven investment is a description used by the Association of Charitable Foundations (ACF) to describe the risk-adjusted market rate return wing of the impact investing market – the kind of activity that would be most fitting for the endowment. ACF defines "impact-driven investment" as aiming to "balance financial returns with strong positive outcomes for marginalised people and/or the planet".[18]

Social investment or impact-first investment (as it is termed by ACF), referenced in Figure 2 below, is an integral part of impact investing's broad church. Within the UK sector, when the returns targeted are below market return the approach is typically described as social investment. This might comprise loans to charities and social enterprises for example, where repayable finance is central but seeking a market rate return could undermine the creation of impact.

- In the UK charitable foundation sector, the ACF's Social Impact Investors Group (SIIG) is particularly supportive and helpful of foundations delivering this approach. SIIG is a membership network for foundations that are starting or undertaking social investment.[19] Typically, members will focus on social investment strategies using funds that have been carved out from the endowment and are now allocated to support charities and social enterprises with repayable finance.

16 https://www.bridgesfundmanagement.com/wp-content/uploads/2017/08/Bridges-Spectrum-of-Capital-print.pdf
17 https://impactmanagementproject.com/impact-management/how-investors-manage-impact
18 https://www.acf.org.uk/common/Uploaded%20files/Research%20and%20resources/Stronger%20foundations/ACF_investment_pillars_FINALv3.pdf
19 https://www.acf.org.uk

UK / US distinctions in impact investing terminology

When defining impact investing it is important to detail some of the differences between how UK and US foundations discuss impact investing and why. In the US, while 'impact investing' is a term in common use, two others are often referred to that are less frequently deployed in the UK: Programme Related-Investing (PRI) and Mission Related Investing (MRI). These two categories roughly equate to social investment / or impact-first investment and impact-driven investment. The PRI and MRI categories however exist in the US because of how they are recognised by the US Internal Revenue Service (IRS). In short, the majority of US foundations are required by law to distribute 5 % of their investment assets annually for charitable purposes or face penalties from the IRS. Charitable purposes can comprise grants to non-profits and programme support costs, as well as Programme Related Investments (PRI's). MRI however do not count towards the foundation's annual 5% pay-out requirement. MRIs have been little used to date, with the notable exception of the Ford Foundation (a case study referred to throughout this study). It is important to note that in the UK there is no mandated grant-making spend by charitable foundations unlike the US. UK foundations generally use a total return approach with most aiming to maintain the real value of their endowment over time, allocating 4% towards spending on grants on top of that total (in practice, a 100% + 4% split). It has become a habit however even within the UK sector to speak of a 95%/5% or 96%/4% division between invested assets and grant-making spend: when quoting others in this guide, that rhetorical norm may be reflected in their remarks.

Figure 2: Esmée Fairbairn Foundation and Guy's & St Thomas' Foundation: a portion of their invested assets and grant-making mapped against the impact investment spectrum.[20]

Esmée Fairbairn Foundation:

	Responsible	Sustainable	Impact-driven (Market rate return impact investing)	Impact first / Social investment	Philanthropy
Amount invested		£25m	£10m	£45m	£53m
General goal of investment approach	Promoting corporate and investment behaviour that is in the interests of long-term shareholders, and will have a real world impact.	Mitigating ESG risks and benefiting stakeholders.	Delivering positive impact innovation and market return.	Supporting organisations that will contribute towards their impact goals in line with their mission, helping them to achieve financial sustainability, and helping to build a more innovative social investment market.	Supporting organisations that will contribute towards their impact goals in line with their mission.
Example activity	Becoming joint signatories with other investors to an initiative asking global food producers to focus on sustainability in their sourcing practices.	Investing in funds looking to achieve enhanced ESG impact alongside financial return.	Investments to be allocated in 2022.	Think for the Future (£515,000): Bridging finance for the purchase of an education hub building.	Grant to Asylum Support Appeals Project: aims to reduce destitution amongst asylum seekers by protecting their legal rights to food and shelter.

20 https://esmeefairbairn.org.uk/latest-news/new-10m-allocation-for-impact-investing/ https://esmeefairbairn.org.uk/about-esmee/investments

Guys' & St Thomas' Foundation:

	Responsible	Sustainable	Impact-driven (Market rate return impact investing)	Impact first / Social investment	Philanthropy
Amount invested	~£650m	~£235m	£100m target (£31m already committed)	~£20m	~£40m p/a
General goal of investment approach	The endowment has a dual mandate: financial return and health impact			Driving more equitable health	
	All investments are expected to meet recognised ethical, environmental and governance standards and be consistent with the foundation's values and need to generate financial returns.	Investment in funds and projects creating health benefits for stakeholders and contributing to health solutions.	The foundation has applied a carve in approach in order to explore how impact can be embedded in the main endowment.	Direct and indirect Investments as part of a test & learn approach to understanding what works in addressing health inequalities.	Grants to organisations that will contribute to driving more equitable health, and to support staff wellbeing and patient experience at Guy's and St Thomas' NHS Foundation Trust.
Example activity	Part of several responsible investing networks including a ShareAction investor coalition for better health, that is pushing (for example) for the government to introduce new legislation for mandatory reporting of nutrition sales-weighted metrics.[21]	£120m invested in healthcare and biotechnology. £50m targeted to climate solutions Investments. Further targets for Investment In funds active in promoting better ESG performance at companies and fund managers from diverse backgrounds. Development of select properties targeting positive health impact through market leading schemes to lower emissions, limit environmental impact and support health & wellbeing in local communities.	This is spread across 9 funds in focus sectors such as healthcare innovation, healthcare service delivery and social determinants of health including housing for vulnerable people, social outcomes contracts, and technology supporting health access.[22]	£4m in venture funds and direct investments focused on improving commercial determinants of health (e.g. disrupter brands in healthier fast food and snacking). £2m investments in black and minority ethnic owned research and design intermediaries. £2m in medical technology spinouts from Guy's and St Thomas' NHS Foundation Trust. £12m of mission related property including housing for families of paediatric patients at St. Thomas' and co-working space for digital health start-ups.	Deployment of c.£20m in charitable expenditure to improve urban health of which £6.4m was deployed to support local recovery activity from COVID-19. c.£15m provided to Guy's & St Thomas' NHS Foundation Trust for patient and staff wellbeing.

These types of approach are not mutually exclusive: a foundation's endowment might, for example, be active in traditional, responsible, sustainable and impact investment all at the same time. As Esmée Fairbairn Foundation and Guy's & St Thomas' Foundation examples detail in Figure 2, foundation funds are being managed under mandates that have differing impact and return expectations. It is the middle domain – "impact driven" investing – where both impact and a risk-adjusted market rate return are sought that is the focus of this guide. This area is the least explored in charitable foundation practice. At the Impact Investing Institute, we hope this project supports a change to this status quo, motivating and helping foundations to apply their impact expertise to a new canvas of their own endowment investments.

21 https://esmeefairbairn.org.uk/latest-news/new-10m-allocation-for-impact-investing; https://esmeefairbairn.org.uk/about-esmee/investments; and https://gsttfoundation.org.uk/our-work

22 https://gsttfoundation.org.uk/our-work/investment/investment-portfolio-impact-investments

3. Myth busting: legality and financial returns

The legality of impact investing

In considering the legal case for impact investing by charitable endowments we are grateful for the support of the following lawyers who have drafted (Bates Wells and Herbert Smith Freehills) and reviewed, (Farrar & Co. and BDB Pitmans), this guidance. The section below is a precis from a longer-form paper on the legal position of charitable endowments on impact investing. For further detail of this work please look to https://www.impactinvest.org.uk/publications/can-charities-invest-their-endowment-with-impact

Endowed charities are legally permitted to make impact investments. Charities exist by definition for exclusively charitable purposes. Unlike pension funds or private trusts, charities do not exist to meet defined liabilities or to benefit specified individuals.

The Charity Commission has provided guidance with respect to the duties of charity trustees when investing in *Charities and investment matters: a guide for trustees*, known as CC14. At paragraph 3.3 of CC14, under the heading "Can a charity decide to make ethical investments?", the Commission states that: "Trustees of any charity can decide to invest ethically, even if the investment might provide a lower rate of return than an alternative investment. Ethical investment means investing in a way that reflects a charity's value and ethos and does not run counter to its aims. However, a charity's trustees must be able to justify why it is in the charity's best interests to invest in this way."

The Commission therefore sees the question of whether ethical investment (which would include impact investment) is in a charity's interests, as a matter for trustees to determine acting reasonably.

The Commission goes on to say in CC14 that: "Trustees should also evaluate the effect of any proposed policy on investment returns and balance any risk of lower returns against the risk of alienating support or damage to reputation." The Commission therefore seems to take the view that trustees ought to look at financial factors and relevant non-financial factors when deciding how to approach investments. The category of relevant non-financial factors includes impact factors and other non-financial factors that relate to the charitable purposes or the ability of the charity to advance its mission and work.

The duty of a charitable trustee is to act in the way they consider, in good faith, is most likely to advance the charitable purposes.[23] When applied to investing, trustees need to assess which approach is most likely to achieve this goal. There are strong legal grounds for trustees to conclude that the best way to advance the charitable purposes will be to adopt an investment strategy which, alongside seeking good financial returns, seeks to (a) mitigate or avoid negative impacts that threaten to undermine the charitable purposes and mission of the foundation and, in addition, (b) achieve positive impacts that are aligned with and support or advance the charitable purposes and mission. How best to go about this in practice will be a matter of judgement for trustees, acting reasonably, based on available evidence and information. It is to be expected that the boards of different foundations will adopt different approaches that reflect their particular circumstances.

23 https://www.gov.uk/government/publications/the-essential-trustee-what-you-need-to-know-cc3

Both the financial case and mission case is strong for impact investing as a means to help advance charitable purpose over time. Financially, evidence indicates that taking account of the wider social and environmental impacts of an investment can also have a material impact on performance. A range of well-regarded studies have shown that a wide variety of sustainability issues are financially material, be it, climate change[24], poor supply chain practices[25], diversity and inclusion[26], and farm animal welfare.[27] These same financially material issues may also have a direct and sometimes significant bearing on a charity's purposes, mission and work, which can be positive or negative. Compared to other institutional investors, foundations therefore have additional reasons to invest for impact, as well as a unique legal mandate to do so.

Regulatory changes and legal challenges have brought the legality of impact investing by charitable endowments to the fore. In summer 2021, the Charity Commission consulted on its existing CC14 investment advice[28]. Concurrently the law firm Bates Wells is acting for two charitable foundation clients, in the case of Buttler-Sloss v Charity Commission, who are seeking a ruling on whether and how the charities should align their investments with their objects. This case will be heard in March 2022, which we anticipate will drive a wave of coverage and interest. The Charity Commission has indicated that it will publish any changes to its CC14 guidance following the ruling.

Notwithstanding the fact that new information pertaining to the legal and regulatory context is expected in the near future, the law already permits charities to invest in line with their mission. Charities are not under obligation to only seek financial returns from their investments, instead they can seek an overall return that comprises both financial as well as mission-aligned social or environmental returns.

Risk-adjusted market rate return and impact

A significant obstacle to impact investing for foundation trustees, and particularly those charged with investment committee responsibilities, is the misperception that developing an impact investing strategy means sacrificing financial returns. Today that need not be the case: impact investing is wholly able to deliver risk-adjusted market rate returns: the global impact investing market is estimated at over $2trn[29]; there is a good evidence base to demonstrate that risk-adjusted market rate return and impact co-exist; product selection is growing year on year; and institutional investors – including local government pension schemes – are now allocating to impact.

24 https://www.ifc.org/wps/wcm/connect/news_ext_content/ifc_external_corporate_site/news+and+events/news/climate-change-to-affect-investment-returns
25 https://www.ft.com/content/afa784ee-7b32-477f-a52d-1e8609ddedc1
26 https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters
27 https://www.fairr.org
28 https://www.gov.uk/government/consultations/charity-responsible-investment-guidance/public-feedback/summary-of-consultation-responses
29 https://www.ifc.org/wps/wcm/connect/publications_ext_content/ifc_external_publication_site/publications_listing_page/impact-investing-market-2020

Impact investor's perspective

Investment committees tend to be conservative and seek a balanced portfolio approach... They want to see the financial side of the argument. The point for them is there should be no detriment/ trade-off to financial return. The argument that if you have slightly less return in [the] endowment but more impact, then ultimately you will have greater impact, doesn't land!

The Impact Investing Institute has built a growing evidence base of sector insights and case studies that show impact investment across a range of sectors and asset classes can provide capital growth, income, and portfolio risk diversification as well as positive outcomes for people or planet. In a recent market sizing survey by the Impact Investing Institute, the majority of the respondents stated that the financial returns from their impact portfolio have either been in line with or outperformed their targets.[30] Those stepping into impact investing can use the Institute's Learning Hub[31] to explore some of this evidence. Recent thematic sector research that may assist those seeking to understand the potential universe of impact investments and their financial return potential includes:

Evidence base: UK

Is there an investment case for social and affordable housing? (October 2021)[32]
A comprehensive insight into the investment characteristics of investing in social and affordable housing which evidences that:

- Debt and/or equity investment in social and affordable housing is likely to increase the risk-adjusted return of both multi-asset and real estate portfolios with the greatest impact evident for lower-risk portfolios.
- Strong credit fundamentals and low correlation with other real estate sectors and the broader economy support an argument that social and affordable housing provides resilient, stable and diversified cashflows and presents a strong case to be an increasing proportion of institutional investment portfolios.

Big Society Capital, Mapping the market of social and affordable housing funds (2021)[33]
In addition to the investment case for social and affordable housing, Big Society Capital has created a helpful overview of investment in the sector. The sector, historically funded by debt, is increasingly attracting equity, such as investment from social and affordable housing funds that typically retain ownership of the property and lease it to housing providers in return for a portion of rental income. This market has grown from virtually zero in 2012 to an estimated £2.9bn at the end of 2020. Five new funds under development in 2021 are aiming to raise £8.2bn. Big Society Capital has mapped the funds' strategies into three overarching categories depending on the type of housing, the people (residents/ tenants), and the level of support provided:

- Specialist housing: supplying suitable homes (bespoke/ adapted new builds) for people with specific needs such as older people, people with learning disabilities or mental health needs.
- Transitional supported housing: refurbished homes (acquired from existing stock) for people with vulnerability or in crisis, such as those at risk of homelessness or survivors of domestic abuse.
- General needs social and affordable housing: new builds for people who cannot afford to rent or buy on the open market such as low-income families.

Scaling up institutional investment for place-based impact (May 2021)[34]
Together with The Good Economy and Pensions for Purpose, the Institute published a white paper that lays out a detailed case for institutional investors to adopt a "place-based lens" that delivers positive impact for communities and underinvested places. The report shows that there are real opportunities for investors to secure financial returns while addressing place-based inequalities and supporting more inclusive and sustainable development across the UK. Ten case studies of investments made are available on the Institute's website[35] that underscore the potential to create risk-adjusted market rate return in affordable housing, urban regeneration, renewable energy, infrastructure and SME financing.

30 https://www.impactinvest.org.uk/project/sizing-the-uks-impact-investing-market
31 https://www.impactinvest.org.uk/learning-hub
32 https://www.impactinvest.org.uk/publications/is-there-an-investment-case-for-social-and-affordable-housing-in-the-uk
33 https://bigsocietycapital.com/latest/mapping-the-market-uk-social-and-affordable-housing-funds
34 https://www.impactinvest.org.uk/publications/report-scaling-up-institutional-investment-for-place-based-impact
35 https://www.impactinvest.org.uk/our-case-studies/place-based-impact-investing

The British Private Equity and Venture Capital Association (BVCA) focus on impact investment
Working with its Impact Investment Advisory Group the BVCA has pulled together a set of case studies that explore private equity investment for market-rate return and impact.[36] Examples include investments in the food waste technology company Winnow, the training technology provider Estio and the sustainable food retail business Farmdrop.

Evidence base: Emerging and frontier markets

Opportunities for impact investing in emerging markets: evidence for institutional investors[37]
We have detailed 16 studies of impact investments in emerging and frontier markets made by institutional investors including pension funds, providing concrete examples of impact investments that meet the specific needs of UK institutional investors. The case studies cover multiple asset classes, themes and geographies, including emerging and frontier markets in Africa, Asia and other global regions. They are accompanied by asset class profiles that summarise key trends and opportunities in emerging and frontier markets from the perspective of institutional investors. Our evidence shows that significant and measurable impact can be achieved while delivering a risk-adjusted financial return that is suitable for these investors.

36 https://www.bvca.co.uk/Our-Industry/Impact-Investment/Case-Studies
37 https://www.impactinvest.org.uk/our-case-studies/

Impact investor's perspective
The argument is simple: there is now a track record in the impact investing world. It's the responsible thing to do to align with your values. You can do that and stop your endowment working against your mission.

4. Why do it? Helping meet your mission, drive broader public benefits and manage risks

There are five central arguments why it is valuable for foundations to pursue impact investing in their endowments:

- **a.** It increases the volume of assets seeking to deliver mission and public benefit outcomes. Financial return also enables the same capital to be reapplied for social purpose, meaning the same quantum of money can be recycled to deliver more impact.
- **b.** It can unlock new strategies for impact by delivering investment activity that influences private sector practices.
- **c.** There are growing expectations that charitable endowments will be invested in a way that is aligned with their mission, with potential reputational danger for those that do not do so.
- **d.** Impact investment at significant scale will drive change in the capital markets as foundations role model making market rate return and delivering positive impacts, and advocate for private sector change alongside other institutional investors, catalyzing systemic impacts.
- **e.** It can support prudent, long-term management of risks that can arise from sustainability issues.

Below we'll explore these arguments in detail:

a. More capital driving positive impacts and public benefit outcomes

Endowments have rightly been called a foundation's 'super power'[38]: they provide financial independence and enable foundations to consider activity with much longer timelines than in the private or public sectors. The returns realised enable the foundation's grant-making and work programme expenditure, and as a result help meet the charity's mission and achieve public benefit. Current norms of practice however have yet to unlock the potential of the endowment investments themselves to deliver positive social and environmental impacts, alongside a risk-adjusted market rate return. However, as the profiles below show, choosing to allocate a proportion of an endowment to carefully chosen impact investments can significantly increase the amount of assets being used to meet the charity's purpose and mission compared to grant-making alone.

As well as increasing the volume of assets that the foundation can use to deliver positive impacts, over time, impact investing enables the possible reuse of the same funds for social purpose. Financial return means that once one deal is done and the capital returned, that original sum can be reapplied to social purpose, compounding the impact that any one pound can have over time, hypothetically ad infinitum. In a market rate return context the approach also yields more resources that could thereafter compound to create positive impacts. Whereas with a grant, any given pound can only be used once, with an investment mindset it can be used multiple times.

38 https://www.acf.org.uk/common/Uploaded%20files/Research%20and%20resources/Stronger%20foundations/ACF_investment_pillars_FINALv3.pdf

Impact investor's perspective

We think of the size differential between grant-making and the assets invested in the capital markets as a planet orbiting the sun. If you're just focused on the impact of the planet, and ignoring the impact of the sun, you are missing a huge opportunity.

Impact in action: Guy's & St Thomas' Foundation

In 2018, Guy's & St Thomas' Foundation decided to allocate 5% of its (then £600m, now) £1bn in endowment assets towards impact investing. Prior to this, the endowment was invested in mainstream products and directly-held property without consideration of impact. About 4% of the net assets were disbursed as grants, social investments and fund-raising, meaning about £40m is directly mobilised towards its mission. The allocation of 5% of the endowment to impact investing, particularly towards health benefits, meant that an additional £30m to £50m could be mobilised in alignment with the mission. By the end of 2021, £30m or 3% of the total endowment had been committed on top of the grant-making expenditure. In total then, and within three years, the foundation had increased the amount of its assets explicitly delivering public benefits from £40m to £70m, without spending down its principal. Recently securing its board's approval for a dual mandate across the entire portfolio, Guy's and St Thomas' now target a £100m allocation to impact investments in the next five years and intends ultimately to align its entire £1bn endowment with the delivery of positive impact. [39]

Impact in action: Treebeard Trust

For Treebeard Trust, a family foundation with £18.7m (as at April 2021) of assets under management, impact investing has enabled it to use many more of its assets to target positive outcomes. The foundation has built up over time with a mission to create a fairer society and healthier planet by backing entrepreneurs and ideas both with grants and investments. Every year the foundation gives away the equivalent of 5% of its endowment as grants, i.e. approximately £900,000. The rest of the assets are invested as impactfully as possible. This has resulted in 50% of the endowment being allocated to responsible investment in public markets. The other 50% is intended to be allocated into direct impact investments covering equity (in mission-driven, for-profit businesses), property and debt. Currently the trust is investing over £5m in this way. Through this approach, therefore, Treebeard has activated over five times the amount of assets targeting positive impact than it would have, had it remained solely a grant-maker.

39 https://gsttfoundation.org.uk/our-work/investment

b. Unlock new strategies to help meet your mission

The power of investment to deliver impact in the endowment is not just restricted to the amount of funds it adds to creating public benefit. It also enables new strategies to effect changes that are not possible through grant-making. As Danielle Walker Palmour, CEO of Friends Provident Foundation put it: "Not every problem is grant shaped".[40] For most issues that foundations care about there are private sector dimensions that have a material influence on whether those issues are positively resolved or not. Using the United Nations Sustainable Development Goals (SDGs) as a filter – see Figure 3 – it is clear that across a multitude of social and environmental problems there are an array of investable opportunities that can contribute to solutions.[41]

Figure 3: Investable opportunities to support the UN Sustainable Development Goals

UN Sustainable Development Goal	Potential private sector interactions that foundations can support/ influence via investments[42]
1 NO POVERTY	• Investing in products and services tailored for poor customers (e.g. mobile-based money transfer services for unbanked consumers). • Investing in businesses that pay workers a living wage.
2 ZERO HUNGER	• Investing in solutions providing access to affordable, healthy and nutritious food. • Investing in sustainable agriculture business models and supporting small-scale producers. • Improving sustainable sourcing practices, enhancing traceability of commodities and demonstrating transparency in agricultural supply chains.
3 GOOD HEALTH AND WELL-BEING	• Investing in affordable medicine and health care, including for low-income and other target populations.
4 QUALITY EDUCATION	• Investing in facilities, technology and services that provide affordable access to quality education and workforce training for underserved populations and improve the quality of learning, including IT solutions.
5 GENDER EQUALITY	• Encouraging and enabling participation of women in decision-making and governance at all levels and across all business areas (30% or greater). • Expanding business relationships with women-owned enterprises, including small businesses and women entrepreneurs.
6 CLEAN WATER AND SANITATION	• Investing in best practice technologies for water conservation. • Investing in water and sanitation projects or infrastructure in underserved regions. • Engaging with investee companies, especially in water-intensive industries or ones operating in regions under high water stress, to become net-zero user of water.
7 AFFORDABLE AND CLEAN ENERGY	• Investing in local renewable infrastructure to establish accessible energy services.

40 Ufi event, November 2021
41 https://thegiin.org/assets/Financing%20the%20SDGs_Impact%20Investing%20in%20Action_Final%20Webfile.pdf
42 Broadly based on SDG compass (https://sdgcompass.org/sdgs/)

UN Sustainable Development Goal	Potential private sector interactions that foundations can support/ influence via investments[42]
8 DECENT WORK AND ECONOMIC GROWTH	• Investing in businesses with strong apprenticeship opportunities, skills development programmes and fair wage practices.
9 INDUSTRY, INNOVATION AND INFRASTRUCTURE	• Investing in new, resilient infrastructure or retrofitting existing infrastructure to make it more sustainable.
10 REDUCED INEQUALITIES	• Investing in businesses led by under-represented and minority leaders. • Investing in Community Development Finance Institutions (CDFIs) that in turn are investing in small and medium-sized enterprises (SMEs) in left-behind areas.
11 SUSTAINABLE CITIES AND COMMUNITIES	• Investing in low-carbon transport solutions. • Investing in affordable housing.
12 RESPONSIBLE CONSUMPTION AND PRODUCTION	• Investing in innovative closed-loop business models.
13 CLIMATE ACTION	• Investing in enterprises or encouraging investees to source from renewable sources of energy (e.g. wind, solar or hydro). • Investing in retrofitting. • Understanding climate risk and building resilience into assets and supply chains.
14 LIFE BELOW WATER	• Discouraging/ prohibiting practices that put marine species and resources at further risk of harm, exploitation or depletion.
15 LIFE ON LAND	• Measuring, managing and mitigating impacts on ecosystems and natural resources. • Investing in sustainable forestry.
16 PEACE, JUSTICE AND STRONG INSTITUTIONS	• Complying with laws and seeking to meet international standards and requiring partners, managers, advisers, investees etc. to do the same.
17 PARTNERSHIPS FOR THE GOALS	• Investing in emerging/ developing markets to promote/ increase the exports of developing countries.

For example, if a foundation has a mission focused on oceans, an endowment investment strategy that seeks to improve fishing practices could complement an advocacy campaign funded by grants. Or take foundations targeting climate change mitigation as an impact goal. Although grants to non-profit organisations delivering advocacy to government and behaviour change to citizens can deliver positive impacts, much of the activity that needs to be shifted to a low-carbon future is in the private sector. The example of Engine No.1 is instructive here. The 2021 shareholder activism campaign by the $240m impact investing hedge fund targeted the $250bn ExxonMobil, pushing it to chart a low-carbon course. Exxon capitulated to the campaign and appointed three new board members committed to changing the business.[43] This was a positive climate outcome that could not have been achieved through grants or social investment: it was only made possible through investors marrying their interest in delivering a market return and a climate-specific outcome.

Social impact outcomes have also been achieved through active shareholder engagement by foundations. Guy's & St Thomas' Foundation has worked on its obesity agenda through its public markets' investments. Through ShareAction the foundation successfully campaigned to secure a Tesco commitment that 60% of their sales of food would be healthier, affecting every £1 in £5 spent on food in the UK.[44]. Another example is a £4tn investor campaign that Guy's & St Thomas' Foundation is participating in,[45] engaging government on mandatory reporting from food retailers on nutrition and sustainability of their sales.

Tackling rising social inequality is a key mission focus for a number of foundations. Many have provided funding to support racial justice and racial equity through their grant-making and programme-related activities. Examples of this include the allocation of $180m by the Ford Foundation for racial justice efforts in the US, including support to advocacy and activists groups.[46] There has also been support from multiple UK foundations to launch The Baobab Foundation, which aims to raise over £1bn in endowments and build long-term funding solutions to tackle the problems of racism, poverty and disadvantage.[47] But going beyond grant-making and programme-related investments, impact investing can unlock opportunities for advancing racial equity. Investment themes that support solutions to racial justice include: venture capital funds like Impact X[48] investing in businesses led by people of colour; private equity funds investing in small businesses owned by people in underserved communities; CDFI's supporting small business in low-income communities; and investment in technologies that, for example, enable employers to identify diverse talent.[49]

43 https://www.ft.com/content/ebfdf67d-cbce-40a5-bb29-d361377dea7a
44 https://shareaction.org/news/tesco-sets-health-target-in-response-to-shareholder-challenge
45 https://citywire.com/wealth-manager/news/eighteen-fund-firms-join-forces-to-launch-sustainable-food-campaign/a1596430
46 https://www.fordfoundation.org/the-latest/news/ford-foundation-announces-180-million-in-new-funding-for-us-racial-justice-efforts/
47 https://www.baobabfoundation.org.uk/funders
48 https://www.theguardian.com/business/2020/jun/08/use-your-money-to-support-racial-equality-says-head-of-impact-x
49 https://cornerstonecapinc.com/wp-content/uploads/Investing-to-Advance-Racial-Equity_Second-Edition.pdf [note: adapted to UK case]
50 https://gsttfoundation.org.uk
51 https://urbanhealth.org.uk/partnerships/current-partnerships

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Impact in action: Investing in better health outcomes

Guy's & St Thomas' Foundation[50] also provides a good example of how applying an impact investment approach can uncover new ways to help deliver a foundation's core goals. Its mission 'to build the foundations of a healthier society' seeks to deliver positive health outcomes in Lambeth and Southwark.[51] Health outcomes are driven by a whole range of factors, many of which can be hard to target with grant-making programmes, such as the local food retail context and inadequate housing. The Guy's & St Thomas' endowment has opened up new routes to tackle these issues. For example, it is investing in food businesses that manifest good practices compatible with the reduction of childhood obesity, has committed significant monies to funds providing affordable housing to vulnerable populations and has a long-term property portfolio with a focus on health and wellbeing.

A key concern more broadly for foundations in their grant-making is the notion of how to ensure the financial sustainability of their investments after the foundation exits. For those foundations that have incubated ideas through grant-making and have potentially supported that organisation to become income-generating through social investment, the next step to attracting more capital is to demonstrate their readiness to take on commercial investment. Foundations can use the reputational badge of their endowment investment, just as they often do their grant-making badge, to highlight to the market that this initiative has their commercial and impact approval.

Impact in action: Friends Provident and Riding Sunbeams

Friends Provident Foundation's involvement with Riding Sunbeams is a good example of a foundation progressing from grant-making to commercial investment. Friends Provident started supporting Riding Sunbeams, a BCorp aiming to enable local cooperatives and social enterprises to supply renewable energy to public transport networks, in 2019. The Foundation gave a grant of £100,000 for business development and to help the organisation become investment ready.[52] In 2020, when the business development work was completed and following the closing of the 12-month grant timeframe, Friends Provident Foundation, along with Thrive Renewables (which is also a portfolio investment of Friends Provident Foundation through its investment in Snowball), became the first commercial investors in Riding Sunbeams.[53] This injection of working capital will enable Riding Sunbeams to develop a new pipeline of renewable energy projects supporting efforts to decarbonise the rail system.

Impact in action: Treebeard Trust and Lighthouse

Treebeard Trust is another organisation with a philanthropic grant that has ultimately become an impact investment in the endowment. The foundation funded Lighthouse,[54] an organisation pioneering a new approach to looking after children in care. Treebeard were initially a grant-maker to the organisation giving them £40-60,000 early on their development. Then Lighthouse faced a conundrum: it couldn't find investment without a contract from a local authority, and the local authority wouldn't give it a contract until it had its first care home up and running. Treebeard solved the issue by providing £2m to fund the purchase of the first home, thus enabling Lighthouse to start providing a safe place for looked-after children, while still expecting to generate a satisfactory return on its investment.

c. Reputational considerations

Alongside the positive spurs to deliver impact in the endowment, given climate and biodiversity crises, major inequalities in the world, and racial injustices, there are "pull" drivers too for foundations. Expectations on all organisations are changing with respect to the delivery of social and environmental impacts. Even in 2007 the Gates Foundation was castigated for its investment practices jarring with its public health mission,[55] and the clarion call for foundations to consider the impact of their investments has only become louder. For the average citizen there is a perception gap between what they would assume the majority of a foundation's assets are delivering, and the reality of them being invested without impact considerations. In a response to a presentation of the US foundation FB Heron's total impact approach, an audience member asked: "But what were you doing before?"[56] The general expectation was that as impact organisations, impact would be a consideration in the totality of the organisation as a norm of practice, not the opposite.

52 https://www.friendsprovidentfoundation.org/grants/projects/riding-sunbeams-riding-sunbeams-business-development
53 https://www.ridingsunbeams.org/17062020-green-tech-startup-riding-sunbeams-wins-innovation-funding-for-solar-rail-demonstrator
54 https://lighthousechildrenshomes.org.uk
55 https://www.latimes.com/news/la-na-gatesx07jan07-story.html
56 https://nonprofitquarterly.org/trouble-in-paradigm-foundations-bargain-with-the-devil

Impact investor's perspective:

The main question to ask is what is the money for? What is the point of a foundation? Was it set up to grow or to actually do something?

Today, many in society, and particularly those closely involved in the philanthropic and foundation worlds, expect organisations to contribute to achieving net zero carbon emissions and creating a more sustainable world. Particularly for foundations, which are built as social purpose vehicles, or for endowed bodies like universities, which have a naturally activist set of stakeholders in their student body, there can be reputational risks from not contributing to these goals. As Darren Walker, President of the Ford Foundation, put it: "I no longer find it defensible to say that our investment strategy is only to maximize the value of our endowment—just as it's no longer defensible for a corporation to say its only responsibility is to maximize shareholder value."[57]

For some this is a question of what can be described as a foundation's 'net impact': if 5% of your total distributable assets are used as grants and are building a better world, but 95% are unwittingly exacerbating environmental degradation, social unrest and inequality – then you may still be broadly 'net-negative'. The hope is that by approaching their entire investment portfolio with an impact perspective, foundations can not only ensure that the positive impact created by their grants are not diminished by any of their investment activities, they can also make investments that can provide comparable risk-adjusted financial returns while increasing the total positive impact created by the foundation.

d. Catalysing change in other investors and in the capital markets more broadly

Capital markets have a clear and important role to play in delivering progress on key sustainability issues like climate and inequality. But they are slow to change. Foundations have an opportunity to be role models for other less mission-driven capital market actors. By demonstrating that foundations can engage in positive impact investment whilst delivering on their commercial goals, foundations can inspire others to help drive a broader capital markets transition.

57 https://www.fordfoundation.org/media/4565/transformative_capital_booklet.pdf
58 https://www.cop26declaration.uk

Impact in action: Tackling climate commitment variance

Friends Provident is working with asset owners to counteract green-washing by asset managers. Organised by Friends Provident grantee Students Organising for Sustainability (SOS-UK), and in partnership with ShareAction's Charities Responsible Investment Network (CRIN) and Responsible Investment Network for Universities (RINU), 25 asset owners have come together as founding signatories of the 'COP26 declaration: asset owner climate expectations of asset management'.[58] The coalition currently comprises asset owners with over £6bn of AUM, who are seeking to tackle the variance in standards from asset managers making similar climate commitments. Amongst the 25 signatories are WWF UK and Jesus College Cambridge.

Additionally, taking the decision to engage in impact investment in the endowment opens up the prospect of more actively influencing other private sector investors to deliver mission-aligned investment. Alignment, coordination and even blending funds with other investors in the service of social and environmental outcomes becomes more possible in a space where impact is part of the discussion within the endowment. Foundations have an independence and reputational heft that enable them to convene investors that might not normally connect. Deploying that convening power in step with the weight of the endowment is likely to encourage private sector capital flows into foundation priorities.

A great example of investors influencing broader markets is one cited by systems change expert William Buckhart.[59] In an article for Pioneers Post Buckhart outlines the systems change aspects of the investment strategy of institutional investor, the Australian Constructions and Buildings Union Superannuation Fund (Cbus). He details, "Cbus has a responsible investment policy that states its commitment not only to integrate environmental, social, and governance (ESG) considerations into security selection and portfolio construction, but also to use its "strategic activities" to influence "the shift towards a sustainable financial system." Its partnership with the New South Wales government promotes investments in low-income and affordable housing, leading to an initial $10m investment. Cbus believes that further collaborations with other state governments "will provide a pathway for greater institutional investment into much needed social and affordable housing, not only providing capital for the building of housing stock, but creating and maintaining jobs in building construction".[60]

Finally, the largest 300 foundations are investing over £72bn in the UK. So if only 5% more endowment assets were allocated by UK charities to impact, a further £3.6bn would be targeting positive social and environmental impact. This increase in AUM delivered under impact mandates would incentivise the financial services industry to better deliver for this client base and drive change in capital markets more broadly.

59 https://www.tiiproject.com/21st-century-investing
60 https://www.pioneerspost.com/news-views/20210715/healthier-society-we-need-more-system-level-investing

Impact investor's perspective:

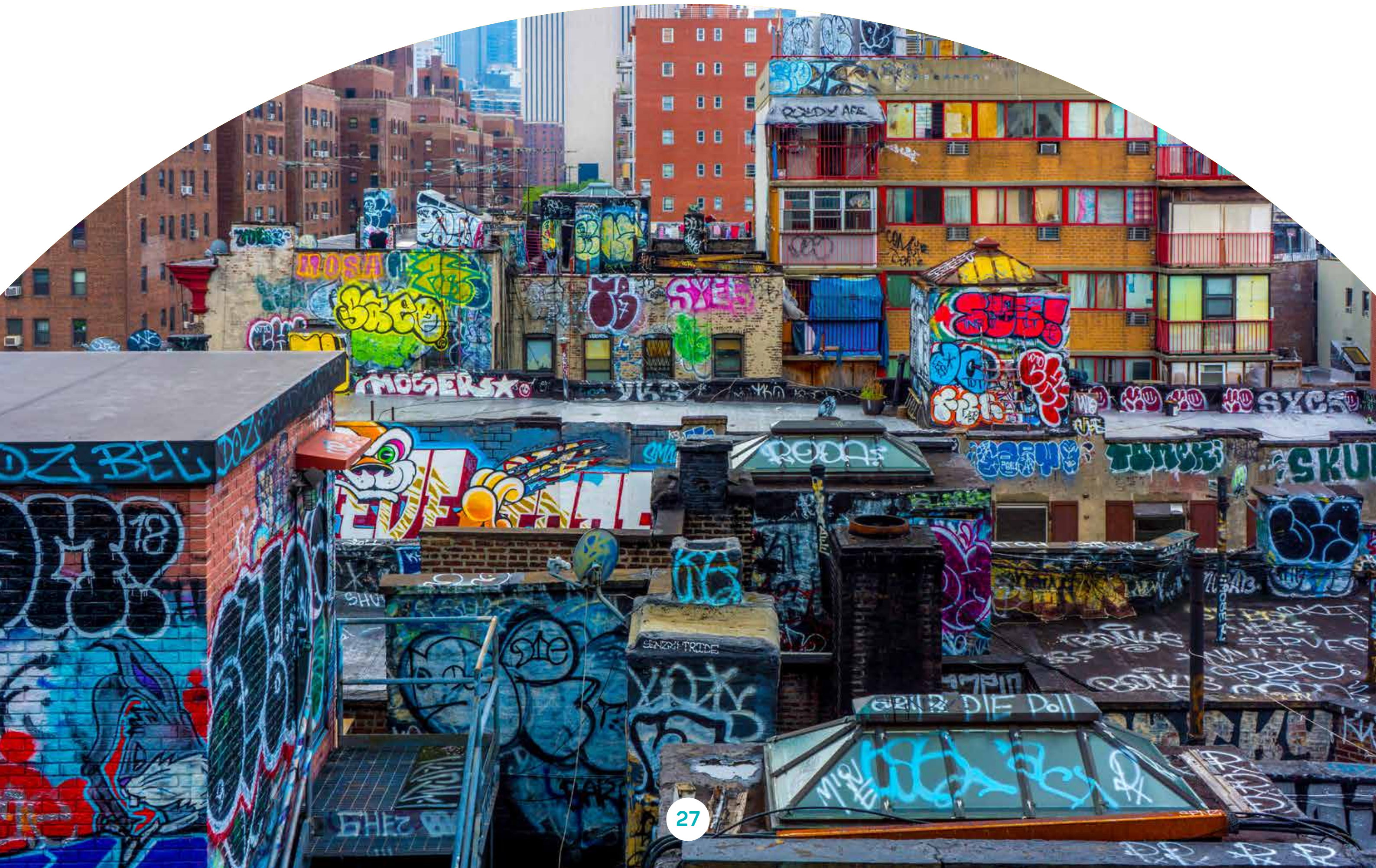
Social investment stuff isn't cutting edge anymore: it was, but now it's not. Today there are huge pools of capital deployed thinking about impact and foundations need to be a part of that. Foundations should be active in shaping the game – we know what it is to deliver impact, so it's important we are part of this discussion in capital markets.

e. Improving the long-term effectiveness and accountability of capital

Foundations generally have a long-term time horizon, with most seeking to exist in perpetuity, and only a few spending down their endowments. This focus on the long term means foundations increasingly must grapple with the systemic risks posed by factors such as climate change and social inequality.[61] Today these risks are not only known but are also financially material with well-documented evidence that social and environmental issues including climate change[62], poor supply chain practices[63], diversity and inclusion[64], farm animal welfare[65] and human health[66] can have adverse financial impacts. The regulatory environment is responding to these risks, for example through the Taskforce for Climate-related Financial Disclosure (TCFD) and the Modern Slavery Act.[67]

Measurement and reporting practices are core to impact investing. By definition then, delivering an impact investment approach in the endowment will help foundations better understand the extent of their negative and positive impact on people and the planet, anticipate regulatory change and proactively tackle the financial risks presented by the climate and environmental issues mentioned above. In other words, impact investing in the endowment gets investment managers on the front foot: spotting negative social and environmental issues before they arise and being on the right side of regulatory development.

61 https://www.impactinvest.org.uk/wp-content/uploads/2020/11/Impact-Investing-Principles-for-Pensions.pdf
62 https://www.ifc.org/wps/wcm/connect/news_ext_content/ifc_external_corporate_site/news+and+events/news/climate-change-to-affect-investment-returns
63 https://www.ft.com/content/afa784ee-7b32-477f-a52d-1e8609ddedc1
64 https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters
65 https://www.fairr.org
66 https://shareaction.org/news/a-healthier-society-leads-to-healthier-returns
67 https://www.legislation.gov.uk/ukpga/2015/30/contents/enacted



Impact investor's perspective:

Investment managers should be presenting impact investing as a part of what a professional asset manager in 2021 should have in their product range – and not wait for the endowment to ask for it.

5. Product availability, product access and tools for impact investing in the endowment

Today there are a range of products from leading and specialist managers that could fit comfortably into an impact investing endowment portfolio, examples of which are detailed below. **Please note, these examples do not constitute investment advice or endorsement but highlight a selection of the market that is seeking to deliver market-rate return and positive impact with their approaches.**

Illustrative Products

Multi-asset

Launch Date: 2020
Fund Size: c. £90m
Investor Type: Institutional and Retail investors

Schroder BSC Social Impact Trust[68]
Launched in December 2020, the Schroder BSC Social Impact Trust is a London Stock Exchange listed investment trust, with a market capitalisation of c.£90m, that enables a wide range of investors to access "a diversified portfolio of high-impact private market investments". The portfolio spans the UK, includes both private market funds and direct investments, and focuses on three primary areas:

- High impact housing: investment to increase the number of safe, secure and genuinely affordable homes for more disadvantaged groups, diversified across: transitional supported housing, general needs social and affordable housing, and specialist supported housing.
- Debt for social enterprises: lending and some preference shares to typically large and well-established charities and social enterprises to help fund expansion projects to scale operations and impact.
- Social outcomes contracts: contracts where private capital enables a consortium of expert charities and social enterprises to deliver outcomes for Government commissioned contracts.

The trust is aimed at investors seeking high quality, deep impact, social investments and a sustainable, inflation-linked return with a low correlation to mainstream asset classes. It is open to both institutional and retail investors.

68 https://www.schroders.com/en/uk/private-investor/fund-centre/funds-in-focus/investment-trusts/schroders-investment-trusts/schroder-bsc-social-impact-trust/

Launch Date: 2016
Fund Size: £24m
Investor Type: Professional investors

Snowball[69]

Snowball is a diversified, multi-asset fund of funds manager that invests in a range of public and private funds to create positive social and environmental outcomes alongside a financial return. It holds a "portfolio of highly impactful public and private market funds across asset classes and impact themes" targeting a risk-adjusted annualised return of 6-7% above inflation and have a five-year track record investing with this strategy. Snowball actively engages with fund managers and measures its impact both at enterprise and fund manager level. Launched in 2016, Snowball has an AUM of £24m. Currently, Snowball accepts investments from professional investors only, but its ambition is to make impact investing accessible to retail investors and "break down the invisible wall between the investment industry and retail investors". Snowball is in the top 5% of B Corporations globally for the governance which protects its mission.

Launch Date: 2018
Fund Size: £750m
Investor Type: Charities with £10,000< investable assets

SUTL Cazenove Charity Responsible Multi-Asset Fund[70]

The Charity Responsible Multi-Asset Fund is a long-term Charity Authorised Investment Fund, regulated by the Charity Commission and the Financial Conduct Authority. It has a diversified strategy targeting financial returns of inflation plus 4% and invests in equities, bonds, property, and alternative assets. It supports what Cazenove terms "a whole portfolio impact approach" for the charities that invest in it and is designed to enable charities to invest in line with their charitable mission and public benefit. Using the Impact Management Project's ABC framework (referenced in Figure 1 and Figure 4 of this report) it focuses on: acting to avoid harm by screening, integrating ESG factors into investment decisions and reducing carbon emissions; benefiting stakeholders through investing in leading sustainable businesses; and contributing to solutions through influencing, via engagement and voting, and by investing for impact. At the end of last year 27% of the portfolio was invested in enterprises that they defined as 'contributing to solutions'. The focus on influencing through engagement and voting includes both environmental and social themes, with recent examples including:

- Pushing the big tech sector to take on greater responsibility for its impact on society
- Driving carbon reductions from high emitters
- Promoting racial equity, human rights and diversity and inclusion.

To promote transparency, the fund publishes a standalone impact report.[71] The fund was launched in June 2018, and currently has investment from over 160 charities. It has been the fastest growing Charity fund In the UK over the last 3 years and has assets of over £750m by December 2021.[72] Investors can access the fund with £10,000 or more of investable assets.

69 https://www.snowball.im
70 https://www.cazenovecapital.com/uk/charities/our-funds/sutlc-crmaf-fund
71 https://library.cazenovecapital.com/view/869139937
72 https://www.cazenovecapital.com/uk/charities/insights/charity-investment/responsible-multi-asset-fund-annoucement

Public markets

Launch Date: 2020
Fund Size: $630m
Investor Type: Retail and Institutional investors

Public equity: Credit Suisse Rockefeller Ocean Engagement Fund[73]

The Credit Suisse Rockefeller Ocean Engagement Fund was launched in 2020, with a focus on UN SDG 14 – Conserve and sustainably use the oceans, seas and marine resources for sustainable development. It is a listed equities (UCITS) fund, in which both retail and institutional investors can invest. The fund is currently sized at $630m (as at November 2021). A feature of the fund is engagement through active representation of shareholders' rights. The fund engages and invests in three ocean themes: pollution prevention, carbon transition, and ocean conservation. The objective of the fund is to seek higher financial returns alongside creating positive impact by, for example, pressing companies to transition away from plastic pollution and improve sustainable fishing practices.

Public debt

A key area of growth and an important option for impact investors is the emergence of green, social, sustainable and sustainability-linked (GSSS) bonds. In 2020 according to figures from the Environmental Finance Bond Database, total GSSS issuance crossed $600bn – nearly double the $326bn issued in 2019. Growth in the GSSS bond market in 2020 accelerated on the 53% year-on-year growth reported in 2019 compared to the $214bn issued in 2018.[74] Sustainable finance bonds had a record first half of 2021 too, accounting for a remarkable 10.4% of the market, almost double the proportion a year earlier.[75] Although the sector still represents a very small slice of the total bond market of $128.3tn[76] overall, it is quickly gaining ground.

73 https://www.credit-suisse.com/about-us-news/en/articles/media-releases/credit-suisse-raises-usd-212-million-for-the-first-impact-fund-d-202009.html?t=290_0.0666357693494517
74 https://www.environmental-finance.com/assets/files/research/sustainable-bonds-insight-2021.pdf
75 https://www.refinitiv.com/perspectives/market-insights/sustainable-finance-surges-in-popularity-during-h1-2021
76 https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Secondary-Markets/bond-market-size

Launch Date: 2013
Fund Size: £400m
Investor Type: Retail and Professional investors, with some Institutional investments from local authority and charity investors

Public debt: Threadneedle UK Social Bond Fund[77]

Launched in December 2013, with $5m seed capital from Ameriprise and £10m from Big Society Capital, the Threadneedle UK Social Bond Fund is the first UK public bond fund to target social impact as well as deliver financial return. This c.£400m fund invests in bonds, primarily in the UK, issued by international, public, private or voluntary and/or charitable sector organisations. Investments are assessed against the Social Assessment Methodology, developed by The Big Issue Group and Columbia Threadneedle Investments, to ensure that social impact is integrated into investment decision-making. These bonds can target particular social outcomes while seeking to generate financial returns in line with UK corporate bonds. The fund focuses on eight social outcome areas: housing and property; community services; education, learning and skills; employment and training; financial inclusion; health and social care; transport and communications infrastructure, utilities and the environment. The fund is primarily aimed at retail and professional investors and eligible counterparties but it includes some institutional investments from local authority and charity investors. As the social partner for the fund, the Big Issue Group sits on a social oversight committee and produces an Independent Annual Impact Report. Each bond is mapped both to a primary UN SDG and also to the IMP ABC classifications (i.e. 'Act to avoid or reduce harm', 'Benefit stakeholders' and 'Contribute to solutions').

Launch Date: 2021
Fund Size: £10bn (first tranche)

Sovereign debt: UK Green Gilts[78]

In 2020, the Impact Investing Institute, together with the Green Finance Institute and LSE's Grantham Research Institute on Climate Change and the Environment, engaged with the UK government on the need to issue £15bn of green gilts with reported social co-benefits.[79] The UK issued a first £10bn tranche of the gilts in September 2021. The 12-year inaugural gilt, priced at a yield of 0.87%, was met with significant demand with investors placing bids of more than £100bn. The proceeds will finance projects in line with the government's Green Financing Framework, to tackle climate change, biodiversity loss and other environmental challenges while addressing social challenges and creating jobs across the UK.

77 https://www.columbiathreadneedle.co.uk/en/retl/fund-details/threadneedle-uk-social-bond-fund-z-income-gbp_t9uksb_gb00bf233915
78 https://www.gov.uk/government/publications/uk-government-green-financing
79 https://www.impactinvest.org.uk/publications/the-green-gilt-how-the-uk-could-issue-sovereign-bonds-that-deliver-climate-action-and-social-renewal

Private markets

BRIDGES
Fund Management

Launch Date: 2002 (launch of Fund I)
Fund Size: £370m

Private equity: Bridges Sustainable Growth Funds[80]

The Bridges Sustainable Growth Funds have collectively raised £370m in capital and have invested in 57 companies that help accelerate the transition to a more sustainable and inclusive economy. They invest in "companies of the future that people want to buy from, work for and invest in over the next decade and beyond," in order to tackle the challenges of our generation whilst delivering lasting economic value. The Bridges Sustainable Growth Funds are traditional close-ended private equity funds where the returns are 'because of impact and not in spite of it'. The businesses backed by Bridges Sustainable Growth Fund III have reported an EBITDA[81] compound annual growth rate of 40% since 2016. Some examples of these investments include World of Books, a circular economy technology business that enables the reuse of books which has contributed to the aversion of over 23,000 tonnes of CO2e emissions whilst delivering a 49% IRR and 6.2x money multiple for investors upon exit in 2021; and Impact Food Group, an educational caterer which aims to change the eating habits of a generation by providing delicious, nutritionally-balanced school lunches, which has grown its contract book by over 70% despite Covid, with its strong focus on nutrition.

Real Assets

resonance

St Mungo's
Ending homelessness
Rebuilding lives

Launch Date: 2013
Fund Size: £70m

Real Lettings Property Fund[82]

The Real Lettings Property Fund, developed by fund manager Resonance and homelessness charity St Mungo's, is a good example of a fund driving solid returns and impact. The £57m fund (now valued at over £70m) is managed by Resonance, and investors in the fund include Big Society Capital, City Bridge Trust, Esmée Fairbairn Foundation, Lankelly Chase Foundation, London Borough of Croydon, and L&Q Foundation. The fund was launched in 2013, to help address the issue of access to affordable accommodation in London. It provides affordable accommodation and light touch 'coaching and support' for a minimum of two years to homeless families and individuals facing homelessness typically stuck in temporary Local Authority accommodation. The focus of this intervention is to evidence how families can become more independent, more resilient and move away from crisis by giving them a safe, secure affordable home with a supportive landlord. The fund leases properties to Real Lettings, the social lettings agency arm of St Mungo's who take referrals from Local Authorities across the Capital. The rental income, largely coming from housing benefits, is used to pay a yield to investors, but capital gain can also be realised by investors once the fund matures. The fund has 259 homes and since launch has housed over 950 individuals, including 525 children. The fund currently supports over 600 adults and children in its properties.

80 https://www.bridgesfundmanagement.com/sustainable-growth
81 EBITDA: Earnings before interest, taxes, depreciation, and amortization (generally used as an indicator of the overall profitability of a business)
82 https://bigsocietycapital.com/portfolio/real-lettings-property-fund-lp/ ; and; https://bigsocietycapital.com/impact-stories/real-lettings-property-fund

Product access and endowment size

A commonly cited obstacle for charitable foundations seeking to deliver impact investing is access to product, and the interplay that has with the size of their investable assets. Central to this problem is the important role that private markets play in impact investing. Although public equity and debt markets are important in delivering impact investment, private markets are widely seen to be the most effective platform for achieving measurable, additional positive impact.

Buy-in thresholds for private markets can, however, look prohibitive - especially for smaller endowments. Typically, $250,000[83] is the minimum ticket size for investment in a private equity or venture capital fund if investing through a wealth manager that is aggregating tickets. This means that a foundation that has, for example, $10m in total AUM and seeks to experiment with 5% or $500,000 of its endowment to deliver impact, can only secure exposure to a smaller number of single funds through its wealth manager, limiting its diversification (and that is if the wealth manager in question has a private equity offering at all). Some wealth managers can navigate around these issues with fund-of-funds products that allow clients to buy into one product that aggregates multiple high impact funds, allowing smaller investors to access the diversification benefits enjoyed by larger foundations. This underscores the need for foundations that want to deliver impact in their endowment to be partnered with wealth managers who can respond to their impact needs and offer products that can accept lower ticket sizes.

For larger foundations however a more frequently cited obstacle is typically around product volume and diversity rather than product access. The market is growing, but for significant allocators the complaint is that the market does not offer investments at sufficient scale for the capital available.

As more institutional investors come into the market however there are ever-increasing opportunities for scale players: the growth of the green bond market is one key point of evidence of this. Another example is the growth of pooled fund products in the market: the Cazenove Charity Responsible Multi-Asset Fund for example, launched in 2018 now has £750m AUM. The market is developing apace, and as more asset allocation occurs in impact, so too will the opportunities. Again, this underlines the vital role played by investment advisors and managers: to deliver this work effectively, foundations require that their investment partners are following the rapid developments in the market and can help them access suitable opportunities.

Using public market engagement to deliver impact

For smaller foundations, public market assets may be the most accessible form of investment. So it is worth highlighting that there are products and approaches in public markets that can be classed as impact investment activity. Shareholder engagement in publicly-listed companies, for example, is typically associated with the responsible investment movement. However, engagement is a tool that, if used intentionally to drive specific outcomes by changing company practice or policy, can be classed as impact investing – especially if there is a commitment to measure robustly the success or failure of that activity,

83 Please note that these observations were detailed to the Institute in dollars by a specific asset manager, hence their indicative use here instead of pounds.

In short, it is important for charity trustees to recognise that public market engagement can change investee company behaviour and deliver positive impact. One example of this is the role that a group like Climate Action 100+ plays, which includes more than 615 investors representing $60tn in AUM. This group persuades investors to vote, or its members themselves vote, on relevant resolutions at AGMs driving the largest greenhouse gas emitters to address climate change at board level and set targets to cut emissions.[84] One successful campaign included mobilising sufficient investor engagement to push BP to broaden its corporate reporting to describe how its strategy is consistent with the goals of the Paris Agreement.[85] Today public markets asset managers are creating products (like the Credit Suisse Ocean Fund detailed above) that explicitly hold stocks and advocate around them in order to drive a specified societal outcome. Rigorous due diligence on such public markets propositions will be key in distinguishing between those managers that are delivering impact, and those merely saying they are, but at least impact products based around corporate engagement are now starting to appear in the market.

Investor tools for impact in the endowment

There are a variety of impact investment strategies available to the endowment investor. It is likely that any endowment committed to delivering impact as well as financial return will enter into a range of funds and products, so it may be useful to look at some of the approaches that have been developed to consider overall portfolio impact.

84 https://hbr.org/2019/05/the-investor-revolution
85 BP example: https://www.bp.com/en/global/corporate/news-and-insights/press-releases/bp-to-support-investor-groups-call-for-greater-reporting-around-paris-goals.html
86 https://www.friendsprovidentfoundation.org/news/applause-for-sses-sector-first-just-transition-strategy

Shareholder engagement: Friends Provident

Friends Provident has a major focus on shareholder engagement in its public markets' investments. Working with Royal London Asset Management, they have been undertaking a programme of investor engagement with large UK energy utility companies on the trends disrupting markets and business models, from decarbonisation to increasing democratisation, and covering issues such as business model resilience, net-zero and just transition strategy, lobbying alignment, and appetite to partner with community energy. They have been actively engaged in driving a specified outcome – a just transition to a low-carbon world – through their public market holdings. This work resulted in, for example, energy utility company SSE publishing the sector's first Just Transition strategy, which details how SSE will seek to mitigate the negative impacts of the transition away from fossil fuels for workers and communities, such as prioritising worker retraining and redeployment, and site redevelopment. The strategy also embraces the transition's opportunities, such as the provision of good quality green jobs, supporting domestic supply chains, and sharing economic value with local communities, including devising the option of a simple shared ownership structure for onshore renewables.[86]

The Impact Management Project (IMP)[87] which created the spectrum of investment approach shown in Figure 1 in collaboration with Bridges Fund Management has a helpful categorisation of how impact investors can think about the impact they are delivering through their investments. IMP distils this into four core 'investor contributions' that can be delivered in combination (as shown in Figure 4).

- **Signal that measurable impact matters:** A commitment to factoring in the impact an enterprise has, such that – if all investors did the same – it would lead to a 'pricing in' of social and environmental effects by the capital markets. Often referred to as values alignment, this strategy expresses the investor's values and is an important baseline. But alone, it is not likely to advance progress on social or environmental issues when compared to other forms of contribution.
- **Engage actively:** Investors can use expertise, networks and influence to improve the environmental/social performance of businesses. Engagement can include a wide spectrum of approaches from dialogue with companies, to creation of industry standards, to investors taking board seats and using their own team or consultants to provide hands-on management support (as often seen in private equity). This strategy should involve, at a minimum, significant proactive efforts to improve impact.
- **Grow new or undersupplied capital markets:** This can be done by anchoring or participating in new or previously overlooked opportunities. This may involve more complex or less liquid investments, or investments in which some perceive risk to be disproportionate to return. Investments "grow new or undersupplied capital markets" if they directly cause or are expected to cause:
    - A change in the amount, cost or terms of capital available to an enterprise that enables it to deliver impact that would likely not otherwise occur, or;
    - A change in the price of the enterprise's securities, which in turn pressurises the enterprise to increase its social and/or environmental impact and/or rewards it for doing so.
- **Provide flexibility on the risk-adjusted return:** By recognizing that certain types of enterprises do require acceptance of lower risk-adjusted financial return to generate certain kinds of impact.

87 https://impactmanagementproject.com/impact-management/how-investors-manage-impact

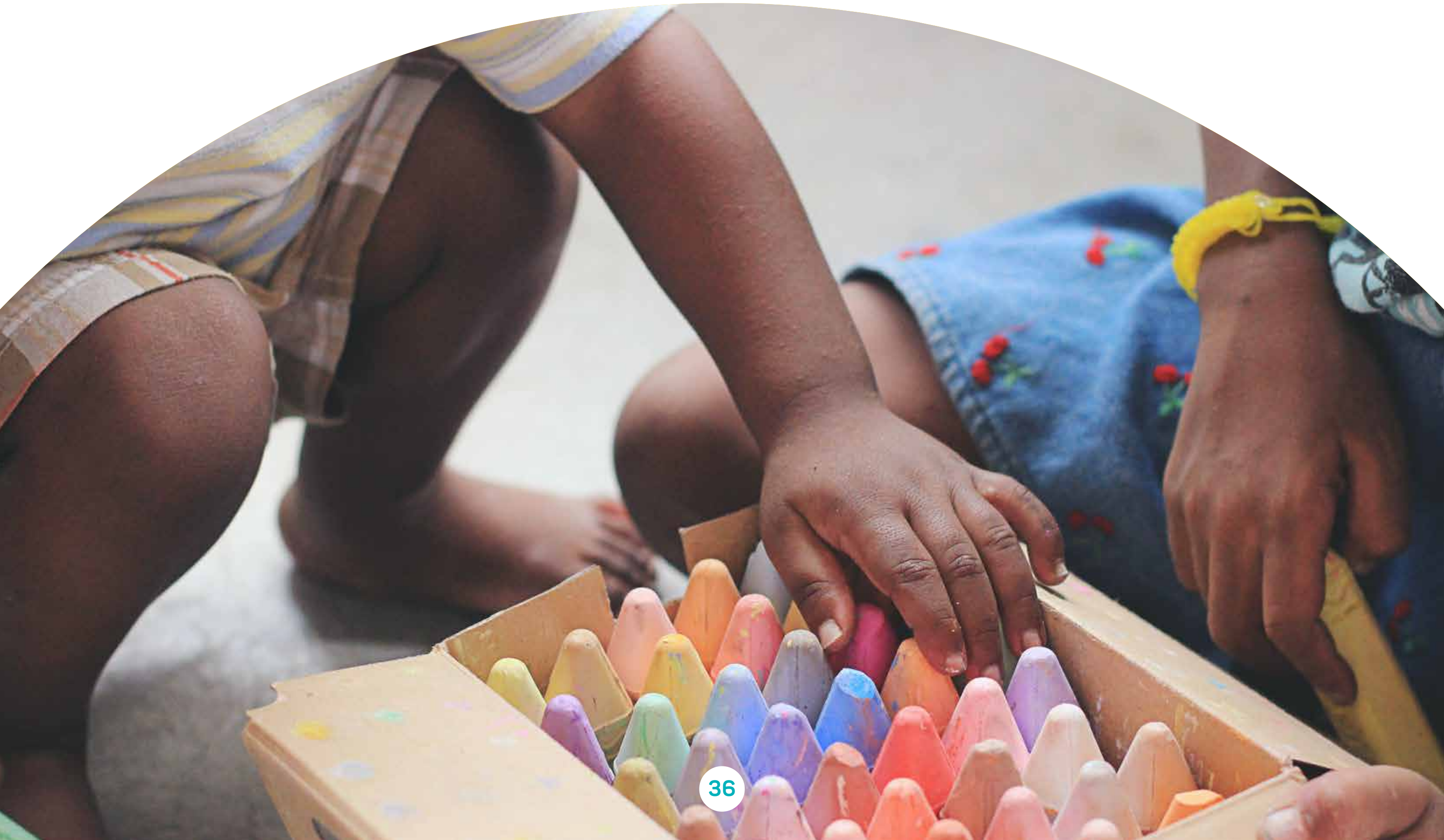


Figure 4 below illustrates a few examples of how investors' choice of impact contribution results in different types of investment decision.

Figure 4: The Impact Classes Matrix: Mapping an investment by its impact on people and planet

The Impact Classes Matrix: Mapping an investment by its impact on people and planet

Impact of underlying assets / enterprises

	Act to avoid harm		
		Benefit stakeholders	
Investors contribution			Contribute to solutions
Signal that impact matters 1 • Engage actively • Grow new/undersupplied capital markets • Provide flexibility on risk-adjusted return	E.g. Ethical bond fund	E.g. Positively-screened/ best-in-class ESG fund	E.g. Sovereign-backed bonds (secondary market) funding vaccine delivery to underserved people or renewable energy projects
Signal that impact matters 2 • **Engage actively** • Grow new/undersupplied capital markets • Provide flexibility on risk-adjusted return	E.g. Shareholder activist fund	E.g. Positively-screened/ best-in-class ESG fund using deep shareholder engagement to improve performance	E.g. Public or private equity fund selecting and engaging with businesses that have a significant effect on education and health for underserved people
Signal that impact matters 3 • Engage actively • **Grow new/undersupplied capital markets** • Provide flexibility on risk-adjusted return	E.g. Anchor investment in a negatively-screened real estate fund in a frontier market	E.g. Positively-screened infrastructure fund in a frontier market	E.g. Bond fund anchoring primary issuances by businesses that have a significant effect on environmental sustainability, access to clean water and sanitation
Signal that impact matters 4 • **Engage actively** • **Grow new/undersupplied capital markets** • Provide flexibility on risk-adiusted return	Investment archetype not widely observed	E.g. Positively-screened private equity fund making anchor investments in frontier markets	E.g. Private equity fund making anchor investments in businesses that have a significant effect on income and employment for underserved people
Signal that impact matters 5 • Engage actively • **Grow new/undersupplied capital markets** • **Provide flexibility on risk-adjusted return**	Investment archetype not widely observed	Investment archetype not widely observed	E.g. Below market charity bonds, or an unsecured debt fund focused on businesses that have a significant effect on employment for underserved people
Signal that impact matters 6 • **Engage actively** • **Grow new/undersupplied capital markets** • **Provide flexibility on risk-adjusted return**	Investment archetype not widely observed	Investment archetype not widely observed	E.g. Patient VC fund providing anchor investment and active engagement to businesses that have a significant effect on energy access for underserved people

As the table In Figure 4 details, any of these four different types of contribution can be targeting a range of asset classes, using both public and private market investment and in most combinations in order to contribute solutions. For impact investing seeking a risk-adjusted market rate return, it is likely that the first three will be most common to any endowment: signalling that impact matters; engaging actively; and growing new or undersupplied capital markets.

6. Practical steps to becoming an impact investing endowment

This section of the guide focuses on the practical steps that a foundation can take to start on the impact investing journey. Although there is no single way into impact, and for many the trajectory is non-linear, there are five domains of activity that all the practitioners consulted for this report say they have had to address in order to deliver their approach – namely:

a. Obtain an internal mandate for impact investing
b. Establish financial and impact requirements for the endowment
c. Update the Investment Policy Statement
d. Integrate impact and investment at board and staff level to deliver the strategy
e. Work with investment advisors, investment managers and asset managers with skills and experience in impact

In other words – and unsurprisingly – a process of consulting with and educating all stakeholders, embedding support into all levels of the organisation and drawing on specialist expertise are all essential to delivering an impact investment approach in a sustained and effective way.

We'll now look at each of these five steps in detail.

a. Obtain an internal mandate for impact investing

The impact investing agenda in any given foundation might start in a variety of places: the CEO or professional staff of a foundation; a trustee curious about whether the foundation could do more; an investment manager or advisor encouraged to bring a new range of investment opportunities to the board; or in the sharing of best practices with peers in the sector. For the impact investing approach to be taken up by the foundation more broadly requires expanding the group of stakeholders committed to explore the approach. This can be achieved through an exercise of information sharing, education and consultation.

As part of the Endowments with Impact project the Impact Investing Institute is making available a downloadable Powerpoint presentation to assist those leading the consultation process. It includes concepts and arguments from this guide including:

- Impact investing definitions
- Myth-busting around financial returns, product availability and legality
- Five key arguments for delivering impact investing
- Product availability and access
- And concludes with tailorable sections:
    - What could impact investing mean for us?
    - How could impact investing positively help us meet our mission?
    - What kind of opportunities are out there that directly speak to our mission?
    - What might we be investing in / are we investing in that could be undermining our mission?

Impact investor's perspective:

We got our advisors to speak separately with each of the trustees… they said that if you are not taking climate risk seriously, you are being a negligent investor. That was really helpful.

The process of obtaining a mandate to explore impact investing is often iterative and may need to be repeated and reinforced by multiple sources from inside and outside the foundation in order to be recognised and accepted. The Impact Investing Institute is comfortable supporting any foundation that might appreciate an external stakeholder presentation on this theme. Additionally, as part of the Endowments with Impact project the Impact Investing Institute has an Endowments with Impact Expert Panel made up of foundation leaders themselves who are going through the process of delivering impact investing in their organisation. Speaking from first-hand experience, they can attest to the lessons they have learned shifting into this practice. Please get in touch with the Institute if you might welcome their contribution.

Impact investor's perspective:

We found Client Earth, ShareAction and the Carbon Disclosure Project useful in us understanding where we should be investing our money.

Hopefully the result of conversations with a broad array of stakeholders will be a mandate from the board to explore impact investing. A typical approach to this area is experimentation and learning through doing. Impact investing is a new approach for most, and thus obtaining a mandate for a small percentage of the endowment to be invested under impact principles, or a specified quantum with which to do deals is advised. This is how leading UK foundations have embarked on the area: Esmée Fairbairn Foundation is delivering £10m of endowment capital for impact seeking a risk-adjusted market rate return on a £1.17 bn portfolio.[88] Guy's and St Thomas' Foundation started its journey into impact in 2018 with a £30m-£50m or 5% endowment allocation to impact investing. Having tested and learnt through that process and been satisfied with the results, it has now obtained a dual mandate from the board to deliver positive health impacts and a financial return for the full £1bn endowment.

88 https://Esméefairbairn.org.uk/latest-news/new-10m-allocation-for-impact-investing
89 https://panahpur.files.wordpress.com/2012/03/the-return-of-capital_final_low-res.pdf

Impact investor's perspective:

I went to a social investment seminar organised by ACF, listened to Danyal Sattar, read a piece by James Perry of Panahpur called The Return of Capital[89] and also read something from FB Heron by Clara Miller. I saw a slight crack in the door and pushed it: it became obvious that impact investing was a huge opportunity.

Impact investor's perspective:

We allocated a small proportion [to impact investing] a few years ago and said we will do this differently. Just that experience of having to think about the impact and ESG bits of it - tipped the investment committee into having to think about it and discuss it: once you have opened that door it doesn't close again.

b. Establish financial and impact requirements for the endowment

Having achieved a mandate to do this work it is important to be clear on both the financial and impact requirements under consideration.

Many would advise starting with financial needs. Grant-making foundations are making money to serve the ultimate goals of the organisation to make grants to other charities. An intent to pursue those goals will ladder back to establishing the amount of money needed each year to fund grant-making and other activities, combined with whatever the aspiration is for the endowment itself (i.e. without reducing total investable assets or having an interest in growing the endowment or spending down the endowment over a particular length of time).

There are different ways to consider establishing both your financial and impact approach. Credit Suisse shared a specific roadmap with the Institute that it uses:

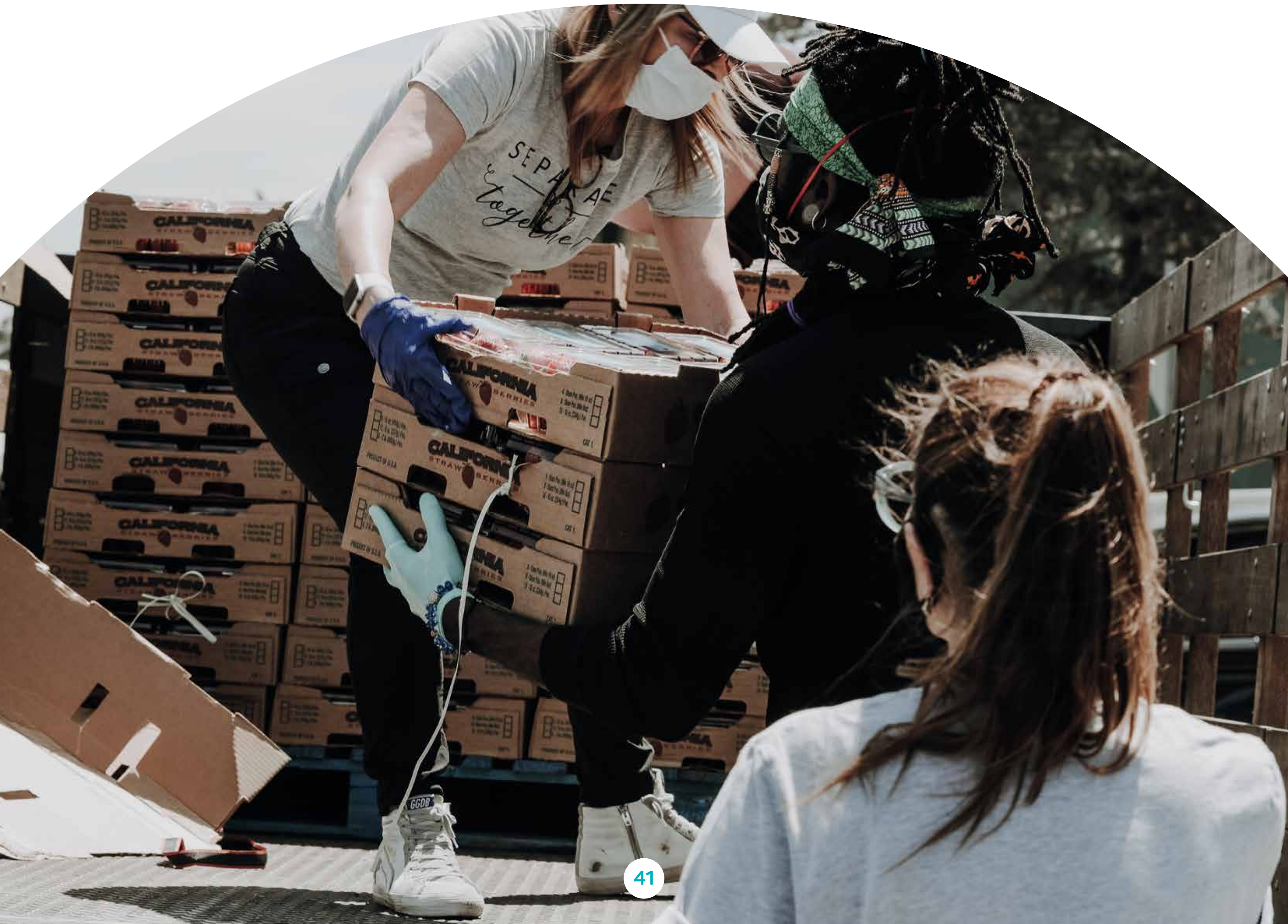
1. **Set a financial goal tied to the foundation's cashflow:** What are the financial needs the foundation has, and how does the endowment need to serve them? A foundation might be happy with 3% + inflation (e.g CPI) to fund 2% grant-making and grow an evergreen asset base for example, but that investment goal needs to be made explicit from the start.
2. **Determine the foundation's liquidity needs:** Most endowments default to a liquid portfolio out of habit and norm, investing predominantly in public securities. Delivering an impact investing approach is strengthened by being open to private markets opportunities as that expands the investable universe. To counter this, foundations can flip the liquidity onus, that is, be comfortable that anything that it doesn't explicitly need to be liquid can be invested in illiquid assets.
3. **Allocate to the spectrum of capital:** Once the cash flow and liquidity needs have been established for the foundation, Credit Suisse creates a tiered asset allocation approach of 1-5 which broadly correlates with the spectrum of capital shown in Figure 1 earlier in the guide. In essence they start to populate portfolios seeking to target as much of a portfolio as possible (given liquidity and return needs) in bucket five, flowing back across from 4 through to 1 to build the portfolio as a whole - see Figure 5.

Figure 5: Credit Suisse's five tiers of capital allocation

1	2	3	4	5
Traditional	Exclusion	ESG integration funds	Sustainable thematic funds: liquid, sustainable impact funds	Impact investing: investing in impact companies (often in private markets) and growing them; or funds with strong shareholder engagement and activism

After this broad conceptualisation of the financial goals of the charity and how they might interact with portfolio construction at a general level, the focus can critically return to mission. The impact investing market is growing year by year, and overall – contingent on the breadth of the foundation mission – there is likely to be some impact approach or product that is suitable. That said, as with any investment strategy, the more restrictions placed on managers the harder it will be to find mission-aligned investments. There are enough impact investment products available to diversify a portfolio, but if a foundation is too strict on theme (except, currently for climate change) the product selection is likely to be too small. Thematic mission-aligned preferences can be included where available and possible, and thereafter the creation of a more generalised public benefit can be a helpful way of thinking about the impacts created. For example, for a foundation with an environmental mission, investments in affordable housing may not directly deliver on its stated mission objective; however, including affordable housing debt in the portfolio would likely be of more public benefit than investing in UK sovereign debt with a similar risk/return profile. If the choice is between mission alignment and no impact investments, or public benefit alignment and some impact investments, the latter strategy clearly generates more positive 'net-impact' overall.

When selecting impact goals, common frameworks can be helpful. The UN SDGs are now in common use in the investment community: locating a foundation's mission among these goals can be a helpful communication bridge between the investment and foundation worlds. Inspiration can also be sought by looking at major trends in sustainable finance – for example natural capital or climate change – to understand the different opportunities in the private sector where finance touches the issues a foundation cares about.



Determining suitable impact categories

The Ufi VocTech Trust, a £50m foundation and client of Credit Suisse that seeks to advance vocational learning, is a useful example of how an organisation has sought to align impact investing with its mission. In each of the five buckets detailed in the model shown in Figure 5, the foundation first sought to find opportunities that delivered on its vocational training mission: it used the UN SDGs as a communication tool to achieve a common language to discuss different impact themes. Ufi also adopted the IMP's ABC Impact Framework and developed a matrix that referenced the A, B and C with different types of investor additionality. This matrix (see Figure 6 below), helped identify categories of preferred investments, accepted investments, and areas from which Ufi wished to divest and make no further investments. Of the 11 themes under which Ufi invests, four themes (38.5% of the equity portfolio) match with Avoiding Harm, one (7.5% of equity portfolio) with Benefiting Stakeholders, and six (54% of equity portfolio) align with Contributing to Solutions.

Figure 6: Mapping investment preferences against impact and investor contribution

		Impact of enterprises			
		May Cause Harm	**Act to Avoid Harm**	**Benefit Stakeholders**	**Contribute to Solutions**
Investor additionality	**Purely Financial**	(Not permitted / for progressive divestment)	Only if necessary for risk hedging or liquidity purposes		(Unlikely to exist)
	Signaling that Impact Matters	(Unlikely to exist)			
	Engage Actively	(Only purposefully and with strong proof of engagement)			
	Provide undersupplied and/ or flexible capital	(Not appropriate)	(Not appropriate)		

Legend:

- Adapted from Impact Management Project Investor Impact Classes Matrix link
- **Impact of Enterprises: A** - act to avoid harm; **B** - benefits stakeholders; **C** - contributes to solutions
- **Investor additionality:** Purely Financial; Signaling that Impact Matters; Engage Actively; Provides Undersupplied and/ or flexible capital
- **Colour coding: Turquoise** - prefer investments in these categories; **Purple** - we accept investments in these categories subject to the notes in the table; **Navy** - we wish to disinvest from these categories and will not make new investments here.

Impact investor's perspective:

[Updating the IPS] was the first thing we did. It was handy to get it all down, secure full board approval and then can get on with it. Governance can be slow with foundations – if you have to go back to them with everything you want to do, you will only achieve a quarter of what you want to get done. Having that document is really useful – a clear steer from trustees that enables to get your priorities done in any given year.

c. Update the Investment Policy Statement

The Investment Policy Statement (IPS) is a key document likely requiring change to support the process of shifting towards impact investing. The role of the IPS generally is to communicate the foundation's parameters on investment performance - risk, return and liquidity – to the professionals that manage these investments. A 'classic' IPS will cover all of a foundation's assets, and thus be drawn on (especially in larger foundations) to create specific mandates for multiple investment managers. This general statement will often make high level statements about ESG aspects - typically exclusions – but seldom details a foundation's underpinning values and what it is seeking to achieve on impact. As a result, if the IPS is not updated or created to be mindful that a foundation might be interested to deliver impact, creating an impact investing allocation can be an uphill battle, chafing against the mandate that the foundation is issuing to its investment advisors and investment managers. However, good practice in this area is starting to grow – with helpful examples detailed below from Access and Friends Provident in particular.

90 https://access-socialinvestment.org.uk/wp-content/uploads/2019/11/Investment-Policy-Statement-Endowment-Fund.pdf

Access and its Investment Policy Statement

Access's Investment Policy Statement[90] was originally adopted by the board of trustees in April 2018 and revised in June 2019. The statement defines the investment objectives and constraints, including both financial and impact objectives, as per the time horizon of the endowment, alongside clarifying the liquidity requirements and the expected withdrawals from the portfolio to fund the foundation's spending. The statement includes a list of criteria regarding investment types and asset classes that the investment manager is mandated to follow in their investment decisions, as well as mandates on risk management, benchmarking, ESG policy and reporting. The investment manager is required to share monthly reports with the Access management team, quarterly reports with the endowment investment committee, and annual reports with the board. These three stakeholder groups review the reports received respectively on a monthly, quarterly and annual basis. The endowment investment committee also reviews an annual report by the investment manager against relevant responsible investment reporting frameworks, e.g. the UN-supported Principles for Responsible Investment.

d. Integrate impact and investment at board and staff level to deliver the strategy

The division between endowment management and grants management in a foundation is often evident in the administrative, governance and human resourcing structures that serve the organisation. Despite the organisation as a whole being a combination of both finance and impact, in practice the different domains of the foundation are often managed as if they were two separate entities. At the board level it is common, and understandable, to appoint trustees with experience in investment as the core of a foundation's investment committee, but often those individuals may have limited knowledge of impact or impact investing. That impact voice is then absent from overarching governance of the investment strategy and can go unheard by the investment advisors and investment managers commonly tasked with managing the money. A few of the larger foundations have internal investment teams (the Wellcome Trust for example) but most foundations work through investment advisors and multi-asset managers. The financial director would commonly be the point person for interacting with managers on the endowment, but on a day-to-day level few of those individuals are charged with supporting and challenging their endowment investment partners on impact.

91 http://www.friendsprovidentfoundation.org/wp-content/uploads/2019/09/Investment-Principles-and-Policy_new-sept-2019.pdf

Friends Provident Foundation and its Investment Policy Statement[91]

Friends Provident Foundation seeks to leverage all its capital to maximise impact. The foundation's investment policy stipulates that 90% of the endowment shall be allocated to generate income for grant making by supporting investments in line with its investment policy. That policy seeks to direct capital to socially and environmentally useful activity to create social and economic value and address societal challenges, with less of a focus on creating short-term financial returns. However, these investments are still expected to generate competitive market-rate returns. The policy also articulates that a further 10% carve-out of the endowment shall be invested to generate strong social benefits that further the charitable objectives of the foundation; for this carve-out the foundation is willing to accept higher risks or lower financial returns. On specific environmental and social issues, the policy clearly defines:

- Specific areas that the endowment will particularly favour: renewable energy, companies supporting local economies and/or offering decent work and fair pay, and banks with a strong approach to addressing financial inclusion.
- Specific areas where the foundation will use its influence as a shareholder: promoting just and net-zero carbon transition, supporting local economies, fair pay, decent work, diversity, responsible payment of tax and responsible corporate lobbying.
- Specific areas and practices where the endowment will not invest: weapons, arms, fossil fuel and high-carbon fuels, nuclear power, unsustainable harvesting, intensive farming that degrades the environment or has poor animal welfare standards, companies with issues around serious pollution incidents and sub-standard governance practices.

Impact investor's perspective:

When we started on this journey, it was like two separate companies. The endowment didn't even have exclusions. Our advisors had never even presented to the full board, just to the investment committee. The rest of the trustees didn't really have full oversight or understand their role/responsibilities in relation to this.

To deliver an impact investing strategy therefore requires changing this separation of investment and impact and bringing the two worlds together in practical terms. At the board level it might require challenging the norm around the trustees that are members of the investment committee: diversifying those investment professionals on the committee to include impact specialists who can help the foundation investment team look at the impact picture. At the team level, new personnel may be required beyond the financial director of the foundation, who are specifically charged with driving engagement and impact in the endowment. In all of the foundations featured as case studies in this guide, from Treebeard at £20m to Esmée Fairbairn at over £1bn, there was a key individual hired to challenge, provoke and oversee the impact side of the investment strategy. For those however that are resource constrained and can't add headcount to deliver this strategy, a good investment manager, adept at impact and with a strong client ethos, can be sufficient to support a strategy.

Impact investor's perspective:

You do have to resource this: currently this agenda falls on [the] finance director's desks, and they do what they can with it, but they don't have the time to do it. There might be a lack of in-house expertise. They see something with ESG and green on the label and have the conversation, but actually they don't know whether it's quality or not; or they go to existing managers with questions and don't know how to judge the response.

92 https://www.fordfoundation.org/media/4565/transformative_capital_booklet.pdf

Ford Foundation: Creating a team for mission-related investing

Ford Foundation's shift to deliver its $1bn impact investing carve-out exemplifies the internal integration necessary to deliver a move to impact. For Ford's shift to mission-related investing (MRI) both a new committee at the board, and a new team were started. The board committee enforces tight risk management guardrails for MRI activities and approves all investments. The committee also monitors social and financial returns performance, and has set criteria, including trigger events, that allow it to suspend MRI investment activity if the foundation's objectives are not met, or if material adverse conditions affect the overall endowment. The new team manages all MRI and programme-related investment activity (concessionary / capital preservation work). The team includes four investment professionals, a senior programme officer—who does grant-making to build the field – and one professional dedicated to portfolio management. Team members' backgrounds include investments, corporate finance, investment banking, law, general management, SEC reporting, information technology, and real estate.[92]

Impact investor's perspective:

Those who push back and say we don't have resources to do this – you may as well say you don't have the resources to do grant making. A foundation is a pot of money that exists for public benefit – it is the responsibility of the trustees/directors to use that money well. The idea that you focus all your internal expertise to handle 5% and handover the 95% to another party with no oversight is absurd. You need to build that in-house capacity and also if you outsource the function, you need to have some oversight and expertise on this

e. Appoint investment advisors, managers and asset managers with expertise in impact

Central to delivering an impact investing strategy with the endowment is a strong working relationship between a foundation and the constellation of financial professionals managing the money. It is often in the relationship between the foundation and manager that an impact investing strategy lives or dies. If a foundation is convinced on the approach, but their investment manager or advisor is not well-versed in impact investing, it will not fly. Consulting on this guide, the Impact Investing Institute has interviewed mainstream managers with strong impact practices as well as specialist asset managers with a deep understanding of the field. Presented with an investment manager partner that doesn't understand the field as adeptly as these players, a foundation is likely presented with one main course of action: run a selection process to obtain new management that can help to invest for impact.

Both Ufi VocTech Trust and Access have run and publicly documented the process they went through to appoint an investment manager that could support impact investing. Ultimately Ufi decided to partner with Credit Suisse, and Access with Rathbones. The selection criteria they used to choose their partners may well be of value to other foundations seeking to tender for new management – see Figure 7.

Impact investor's perspective:

One of the key challenges is financial advisors dismissing [impact investing] and peddling myths that this approach can't be done. They're saying that because they don't know. If you hear that you have to find someone else [to help you].

Figure 7: Two foundations and their investment manager selection criteria

Ufi VocTech Trust	Access – the Foundation for Social Investment
Manager selection criteria: • Understanding Ufi's mission, strategy, investment policy and current fund investments and the ability to translate this into appropriate investment solutions • Positive working relationship with comparable clients, demonstrating a proactive and engaged approach • Excellent track record of supporting clients to achieve or exceed their investment objectives • Expert knowledge and experience of best practice in ESG and of advising on impact investing • High quality reporting with deep transparency over underlying assets including ESG/impact performance • Robust and stable business and team • Value for money.	Manager selection criteria: • Willingness to engage and likelihood of being a good partner to work with • Experience in the impact sector • Ability to deliver required products/asset classes • Plausibility of suggested investments • Market changing/leading • Transparency and costs.

Another interesting approach taken by Friends Provident Foundation, Blagrave Trust and Joffe Trust[93] in 2020, and Eiris[94] in 2021 is to go yet further on transparency, running an open tender process for new investment managers. This process, where investment managers pitch publicly to win a mandate while the foundation in question considers their responses but also invites others to hear the presentations, is a very powerful approach. It raises awareness of investment management that delivers impact, and enables comparison between different providers, accelerating the number of managers competing on impact as well as fees and returns.

93 https://www.friendsprovidentfoundation.org/news/charities-launch-esg-investing-olympics The winners of the mandate were Cazenove
94 https://eirisfoundation.org/investmentwinners The winners of the mandate were Castlefield Investment Partners and Snowball Impact Management

7. Conclusion

We hope that this guide has provided a persuasive case for impact investing in the endowment and shared a pathway for charitable foundation endowments to get started on delivering the investment approach. Today's impact investing market can deliver the risk-adjusted market rate return and positive impacts that investment committees are increasingly seeking. Through delivering impact investing strategies they will:

- Increase the volume of assets delivering both for their mission and for broader public benefit outcomes.
- Get more from their money, with financial return enabling the same capital to be reapplied for social purpose, ultimately delivering more impact.
- Unlock new impact strategies by delivering investment activity that influences private sector practices.
- Meet growing expectations that charitable endowments will be invested in a way that is aligned with their mission and public benefit, and avert the reputational danger of not doing so.
- Open up the possibility of driving change in the capital markets as foundations role model making market rate return and delivering positive impacts, and advocate for private sector change alongside other institutional investors, catalyzing systemic impacts.
- Have anticipated and be managing prudently the long-term risks that arise from sustainability issues.

Few foundations have fully embraced the journey to deliver positive impacts and compelling returns in their endowment, but through taking the five steps outlined below, can readily do so, starting small and building confidence in the approach over time:

1. Obtain an internal mandate for impact investing;
2. Establish financial and impact requirements for the endowment;
3. Update the Investment Policy Statement;
4. Integrate impact and investment at board and staff level to deliver the strategy; and
5. Appoint investment advisors, managers and asset managers with expertise in impact.

Importantly, any foundation interested to embark on this approach can do so in-step with, and supported by, their peers. Throughout this paper, in the case studies featured in the appendix, and the standalone case studies created by the Impact Investing Institute, there is an emerging UK community of practice of impact investing endowments. Through the Endowments with Impact programme, the Impact Investing Institute will be expanding this collaborative community of peers, convening on the themes featured in this guide, creating a peer network that spreads knowledge, good practice, advice and guidance on delivering positive impact and risk adjusted market rate return in the endowment. We hope that working together, more foundations can unlock the engine of their endowment to deliver further positive impacts for their work, and move capital into delivering the environmental and social outcomes that matter.

8. Appendix: Impact in action - case studies of impact investing endowments

The journey to become an impact investing endowment has been taken by pioneers around the world: in this guide we include inspiring examples from both the US and the UK. There are three main approaches that these case studies illustrate. First is a 'carve out' in which a percentage or set amount of the endowment's AUM is committed to impact investing opportunities with a view to experimenting with and growing the allocation over time. Second are those who have gone further with a commitment to deliver 'total impact' in which all foundation assets are managed under an impact mandate. Finally, some foundations have gone further still delivering a total impact approach that they see as catalytic in the market, using the concessionary/capital preservation strategies of social investment, but deploying them on a much more significant scale.

In the course of creating this report a general trend has been noted:

- Newer foundations, presented with an opportunity to build a foundation from scratch are, to some extent, freer to bake in a 'total impact' approach. Unconstrained by their own history they can chart this innovative course and respond to the market as it is today.
- For older foundations – some hundreds of years old – the approach is necessarily more experimental and incremental. These foundations have been extremely successful over a long period delivering work under longstanding norms of practice. To be convinced that impact activity in the endowment is worth exploring and will not compromise financial performance, requires experimentation and a 'seeing is believing' approach.

Carve out case studies

Most foundations start on the journey to impact investing in their endowment through experimental and gradual allocations. This approach makes sense for those looking to get a feel for the impact investing market and how it can work for their requirements.

Esmée Fairbairn

Esmée Fairbairn Foundation aims to align its investments with its charitable objectives and use all the tools available across the board, including grants, social investments, investments and influence/ engagement, to further its impact objective and catalyse change. As part of this aim, Esmée Fairbairn Foundation is reviewing its investment strategy and transitioning through responsible, sustainable and impact investing with its £1.17bn endowment.[95] In 2021 the foundation allocated £10m to impact investing, to bridge the gap between their £25m ESG carve-out, where investments are made with the primary objective of achieving risk-adjusted market rate financial returns in line with the foundation's mainstream investment strategy alongside ESG impact, and their £45m allocation to social investing, which has an impact-first approach and accepts concessionary returns.[96] This carve-out will be invested in funds that target and report not only on financial performance but also social or environmental performance. The impact investing decisions will be made based on the intentionality of generating social and environmental outcomes, the measurability of such outcomes, and the expected financial return. The fundamental transition in this approach has been to start by thinking about the outcomes that the foundation wants to achieve and approach investment structures and decisions based on the outcome objective. The foundation is using this allocation to experiment with impact investing opportunities and to test the potential to achieve financial returns by aligning the investments with impact goals. This experiment will inform the foundation's long-term investment strategy.

95 https://Esméefairbairn.org.uk/about-Esmée/investments
96 https://Esméefairbairn.org.uk/latest-news/new-10m-allocation-for-impact-investing

The Ford Foundation

In the US, the Ford Foundation is a good example of a foundation that has shifted to deliver a step change in its investment practices, expanding its programme related investments (equating to the UK's conceptualisation of social investment) in 2018 to include a major new impact investing strategy. It allocated 8% of its endowment – at that point $1bn of AUM – over 10 years into two main domains: investment in affordable housing, and into financial inclusion. The strategy was signed off by the board on the grounds that it will:

1. Achieve a total return consistent with prudent risk while taking into account the relationship between particular investments and the foundation's charitable purposes, and
2. Eventually contribute to foundation spending over time.

Although the board did not set a minimum financial return target, in practice the foundation used a 7% hurdle rate as an important consideration in its portfolio construction. The 'mission-related investing' (MRI) programme's purpose was "to make investments that generate positive social returns and commercially appropriate risk-adjusted returns on capital". For high-impact investments where the foundation feels it might not be fully compensated for the level of risk assumed, Ford will re-focus on programme-related investment (PRI) capital.[97]

Total impact case studies

A working paper on total impact[98] by the Cabinet Office defines a total impact approach as "when a foundation considers the social impact of all of its resources and assets before settling on the strategy that will enable it to best meet its charitable objects". This approach requires the foundation to articulate the positive impact they want to create, measure the impact their activities do create, and redirect resources to maximise this impact. An important aspect of a total impact approach is to see if any negative impact contributed by their traditional investments is reducing the positive impacts created by their grant making or other investment activities.

Total impact in the US

Two influential examples from the US of foundations aligning the totality of their endowment with their philanthropic mission are the FB Heron Foundation and the KL Felicitas Foundation.

FB Heron

Founded in 1992, the FB Heron Foundation[99] has a mission to "help people and communities help themselves". Heron had an initial mandate to mobilise its 5% pay-out (the minimum US foundations are required to distribute by law each year towards charitable expenditure) towards mission-aligned grants. However in 1996, the board started viewing this as, "the narrowest expression of the foundation's philanthropic goals," and began looking at a "toolbox" that could mobilise the other 95% of Heron's assets. This gave rise to a strategy that combined grants with 'mission-related' investments. The foundation implemented this strategy incrementally, and within a decade, approximately 40% of the overall endowment was mobilised in mission-related activities/investments.

97 https://www.fordfoundation.org/media/4565/transformative_capital_booklet.pdf
98 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/386335/2903051_ImpactFoundations_acc.pdf
99 https://www.heron.org

In 2012, Heron decided to increase this activity and invest 100% of its assets for mission but wasn't able to find a fully mission aligned investment manager in the market. Considering impact-screened products as better aligned to its mission than its 2012 portfolio, the foundation worked with investment managers to move its entire investment approach to impact-screened products. By the end of 2016, Heron moved its last unscreened piece of the endowment to impact-screened products. This strategic change moved over $150m, of the foundation's (now) $275m endowment, to impact-screened products. Going forward the foundation is committed to continue pivoting its portfolio to better align with its mission. The purpose of Heron, that of furthering the ability of people and communities to move out of poverty and thrive, continues to guide the use of all its resources, including its investments. In December 2017, Heron affirmed its investment policy statement to reflect the foundation's intent to select opportunities, for both grants and investments, whereby both social and financial returns can be maximised. The investment policy statement acknowledges that all investments are impact investments in a spectrum of impact, prioritises maximising both social and financial performance, and is driven by fundamentals – which means analysing an enterprise's broad social contribution, market opportunity, management team, business model and other factors, compared to peers and the industry/sector/market. Furthermore, the policy statement also calls for collective action and seeks for Heron to align with like-minded investors and enterprises to enable system change and leverage capital together.

KL Felicitas

KL Felicitas Foundation[100] was founded in 2000 by Silicon Valley veterans Charly and Lisa Kleissner with the mission to "enable social entrepreneurs and enterprises worldwide to develop and grow sustainably". KL Felicitas pursues a strategy to achieve targeted social and environmental returns as well as financial returns. Of its $10m endowment, 99.5% is committed to impact investment.

The KL Felicitas Foundation pursues both impact-first and finance-first investment types, and has divided its investments in five categories:

- **Programme-related investments** that primarily aim to advance the foundation's charitable objectives and are paid out from the foundation's annual 5% pay-out.
- **Thematic investments** that support the mission of the foundation and seek risk-adjusted returns comparable to investments made without regard to the mission.
- **Sustainable investments** or investments made into companies or funds focused on environmental, social or financial sustainability.
- **Responsible investments**, that are not necessarily aligned to the mission of the foundation but that directly or indirectly support social beneficiaries.
- **Corpus impact first investments**, similar to programme-related investments but that originate from the foundation's endowment and are thus part of the portfolio with an expected financial return and related risk.

Beyond these investment categories, the foundation provides grants that are aligned with the impact investment portfolio.

Total impact in the UK

Within the UK there have also been some notable examples of total impact. The work of both Access and Ufi is illustrative here. Below we draw extensively on two very good existing case studies publicly available online[101] that give a deeper view of how these two foundations shifted to impact.

100 https://klfelicitasfoundation.org
101 Case study references are found in Access and Ufi footnotes

Access – the Foundation for Social Investment[102]

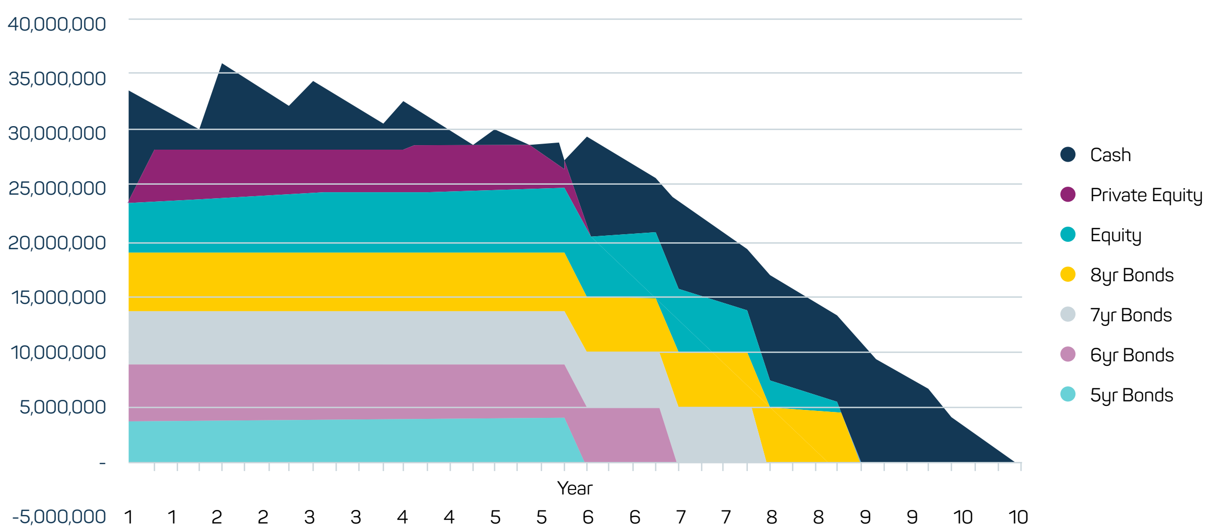
Access received a £60m endowment commitment from the Cabinet Office in 2015 (released in multiple tranches over time) along with two specific mandates:

- To spend the endowment over 10 years to support charities and social enterprises become investment ready so they can access capital from the social investment market.
- To apply a total impact approach in allocating its resources "including in its investment strategy" alongside evaluating and reporting its total impact across all its activities.

With its mission to support charities and to help social enterprises access capital from the social investment market, it was seen as appropriate that the endowment capital was allocated to the same market. A vital question for Access in applying a total impact approach to investment strategy was how to ensure funds from the endowment were available for programmes throughout the 10 years.

Four factors were seen as critical in the decision-making process of allocating endowed capital: risk, return, impact and liquidity (i.e length of investment). The financial and impact models that were developed reflect the mission alignment alongside the flexibility that Access needed in designing its investment process. The financial model, developed initially for a capital size of £36m (see Figure 8 below), was to primarily invest in social and ethical fixed income investments such as charity bonds, with some cash reserves for programmes.

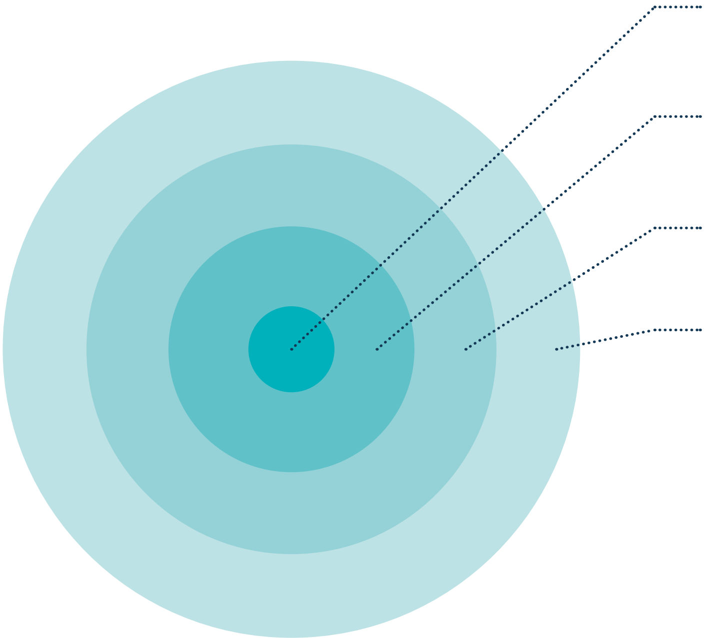
Figure 8: Access financial model showing the projected spenddown as designed



The impact model was perceived as a spectrum varying from low-impact to high-impact investments and was designed as a bullseye with full mission alignment (see Figure 9 below), i.e. 'charities and social enterprises delivering social impact in the UK', at the core, and consecutive rings which respectively included 'charities and social enterprises delivering social impact elsewhere', 'other organisations delivering social impact', and 'other organisations that have best in class ESG indicators (priority on S&G)'. This model has enabled Access not to have to wait for all its allocation to be fully deep impact (i.e. at the centre of the bullseye), but instead given it the flexibility to allocate capital in ways that are close to total mission alignment while retaining the intention to invest more at the centre over time.

102 https://access-socialinvestment.org.uk

Figure 9: The Access 'bullseye' impact model



As of 30 June 2019, 45% of Access's portfolio was invested in the centre of the bullseye. As per the 2019 impact report[103], the endowment's 2018 investments have supported the management of 80 social housing properties, the generation of renewable energy for 206 UK homes, and the provision of water and wastewater for 605 customers. In January 2019, with a fresh tranche of £10.3m of endowment money (released as part of the original commitment of £60m to Access) and £3.7m of interest, Access's total impact capital was £52m. Of this £300,000 is spent on management fees and £7.8m is withdrawn for programme funding, leading to an invested amount of £43m along with a cash reserve of £900,000.

At a portfolio level, Access has been able to implement the total impact approach, channelling funding to the core of its impact model. It has achieved good impact and financial performance, outperforming its target benchmarks. However, Access has also faced some challenges. For example, it had invested £440,000 in Our Power, a not-for-profit energy supplier that collapsed in January 2019. In investment terms the loss was manageable, as a default risk of 1% was accounted for, however the loss of capital in a time-bound endowment meant that funding for grants decreased.

Access had also originally calculated its programme demand at £6.6m per year evenly spread out until the end of 2024. However, actual demand was found to be about £8m per year which would require faster exits, potentially at a lower price, to maintain cashflow. These experiences of Access have given rise to some important questions on the impact of loss of capital or loss of expected profit, on achieving the foundation's mission. A particularly interesting issue is how liquidating assets early and subsequently channelling funds to programmes affects the total impact of the foundation.

103 https://access-socialinvestment.org.uk/wp-content/uploads/2020/01/Access-annual-impact-report-MAIN-Jun-19-FINAL.pdf

Ufi VocTech Trust[104]

The Ufi VocTech Trust was set up in 2010 with an initial fund of £50m to "champion the power of technology to improve skills for work". Ufi's initial investment model focused on investing a majority of its endowment with the primary purpose of achieving financial returns to fund its charitable activities. In 2019, Ufi began to consider how its financial assets could be better aligned with its mission, and thus developed a new five-year strategy (2019-2024) along with a new investment policy and a new investment strategy. An important milestone for this exercise was learning that it was possible to invest its endowment both to meet its financial needs and to further its mission, from a legal and fiduciary responsibility perspective. Ufi plans to transform its portfolio over ten years, transitioning towards greater liquidity and lower risk over time, starting with a balanced allocation of c.50% equity and c.50% fixed income. To achieve this transition, Ufi appointed a new investment service provider in autumn 2020.

Catalytic capital case studies

Finally a catalytic capital approach takes the total impact concept even further, seeking to deliver capital that is patient, risk-tolerant, and flexible in order to provide impact investment that may not otherwise be possible to find. This type of capital may better serve the impact need itself, enabling an enterprise to thrive given the better terms that it is partnering on. Such catalytic capital can also support crowding in other mainstream/ commercial/ private capital into opportunities, by either lowering the risk and / or improving the return profile for others.

Ceniarth[105]

Ceniarth is a family office headquartered in the US with a total impact approach, focused on improving the livelihoods of marginalised and vulnerable communities globally, but it has gone a step further than the other approaches detailed to be completely catalytic in its approach. Using its $500m+ AUM, it seeks to achieve capital preservation in real terms in its endowment investments. Ceniarth is active in a space where commercial (impact) investors are not willing or not able to invest as the rate of return is not attractive to commercial capital. Realising that conventional finance-first approaches were not able to mobilise capital into the marginalised and vulnerable communities it wanted to help, Ceniarth made a declaration in 2018 to move assets to impact-first investments. That year, it moved $30m, or 7% of its assets, into impact-first investments. This allocation had grown to $174m, or 39%, by 2020. Ceniarth's ambition is to be fully impact-first and in 2020, 100% of its new commitments, i.e. $31m, were impact-first investments. As a provider of patient and catalytic capital, Ceniarth seeks below-market return rates. Opportunistically it may also invest in companies with good impact alongside market rate return but its focus remains on supporting funds and enterprise that are unable to access capital. Through its catalytic capital approach, Ceniarth aims to:

- Lower the cost of capital for impact gains;
- Unlock capital by taking a subordinate, impact-first position;
- Seek specialist, high-impact fund mandates, including those offered by first-time fund managers;
- Provide early, pilot debt; and
- Support impact-first investing and impact measurement.

104 https://ufi.co.uk
105 Impact-First: Before, During and After COVID-19, Ceniarth Annual Report 2020: http://ceniarthllc.com/wp-content/uploads/2021/04/Ceniarth_AnnualReport-2020.pdf