Cornerstone Capital Group

Global Thematic Research

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Exploring the Nexus of Philanthropy and Market-Based Solutions


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Erika Karp, founder and CEO of Cornerstone Capital Group, was interviewed by Charities Aid Foundation (CAF) America to explore the intersection between market-based solutions and philanthropies, particularly as it relates to investment. We used the request by CAF America to conduct interviews internally and externally with thought leaders in the finance and foundation fields to gather opinions about the nexus of market-based solutions (i.e., traditional for-profit investment via the capital markets) and philanthropy (i.e. foundations and other tax-advantaged giving vehicles). Topics included:

- Areas of collaboration between philanthropy and capital markets,
- Donor Advised Funds (DAFs), and
- Evolution of corporate philanthropy.

Collaboration between philanthropy and capital markets

Interviewees cited collaboration between traditional investors and philanthropies as a key to solving the world's most pressing issues. Philanthropies bring issue-specific expertise and willingness experiment, while market-based solutions bring scalability and financial sustainability.

Our interviews identified three areas of collaboration:

1) **Partnerships between philanthropies and investors** can bring scalability to projects. Market-based solutions provide financial returns that can be recycled for further impact while philanthropies typically have deep knowledge of specific social and environmental issues.

2) Philanthropies can amplify the impact of their capital by **aligning investment of their endowments to their mission.**

3) Collaboration between philanthropies and capital markets **can increase the attractiveness of certain investments**, as philanthropies that focus on social impact can act as a guarantor for part of the investment and entice more capital to projects.

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List of interviewees

- Jenny Chan, Senior Investment Officer, Doris Duke Charitable Foundation
- Clara Miller, President, Heron Foundation
- Katherine Pease, Principal, KP Advisors
- Jennifer Pryce, President and CEO, Calvert Foundation
- Bruce DeBoskey, founder, The DeBoskey Group
- Cornerstone Capital Group staff

A key opportunity for partnerships is to **share expertise and knowledge.** Investors are often in positions to interact with companies to address concerns about the social and environmental impact of business activity. Philanthropies have specific expertise and understanding of issues that may not be clear to mainstream investors. Therefore, philanthropies can facilitate the exploration by more mainstream investors of innovative approaches to critical issues.

While partnerships between capital market players and philanthropies are powerful, **there are often roadblocks in collaborating**. Differences in investment jargon and perspective can present operational difficulties. For instance, the concept of scale can differ between philanthropies and mainstream investors: A $10 million project may represent significant outlay for a foundation, while a mainstream institutional investor might require a much higher minimum investment to justify the time and effort of becoming involved.

Yet, in our view the potential of partnerships far outweighs the difficulties posed by the hurdles, and the desire for perfection should not override the need for good. By leveraging the expertise of both types of organizations and increasing the capital available for social impact, partnerships can integrate sustainability into mainstream financial markets and create impactful investments.

Examples of Philanthropy and Market-Based Partnerships

Age Strong is an impact investing collaboration with AARP, AARP Foundation, Calvert Foundation, and Capital Impact Partners. Through Age Strong these organizations work to channel capital to critical services for the aging, including healthcare, long-term care, access to healthy foods, and affordable housing. AARP Foundation has invested $70 million of its own assets in Age Strong. Calvert Foundation offers the note through which investors can invest in Age Strong, and Capital Impact Partners, a nonprofit Community Development Finance Institution (CDFI) with a national presence, is deploying this money.

Greyston Bakery is certified B Corporation bakery located in Yonkers, New York. Started in 1982, Greyton focuses on employment as the key to eliminating poverty. The company's Open Hiring policy employs a range of difficult-to-employ people and also provides a range of services to the community. The business is funded through a mix of sales revenue, grants and donations. Major recent donors include the Kresge Foundation and the Gary Saltz Foundation. Greyston is an example of foundations and market-based solutions developing innovative and sustainable business models to address systemic issues.

Benefit Chicago is an impact investing collaboration with MacArthur Foundation, Chicago Community Trust, and Calvert Foundation. Benefit Chicago aims to channel $100 million to nonprofits and social enterprises working to develop and support Chicago. MacArthur Foundation has invested $50 million of its own assets in Benefit Chicago, alongside a $15 million commitment from the Trust, which is a Chicago-based DAF. As with Age Strong, Calvert Foundation offers the note through which investors can invest in Benefit Chicago. MacArthur Foundation, with its strong local knowledge and relationships in Chicago, is deploying this money.

Leading philanthropies are increasingly becoming more transparent in delineating their investments in target programs. This transparency is key to fulfilling their mission: Philanthropies can use transparency to find the environmental and social issues that most need attention and then to demand and assess the effectiveness of interventions.

Aligning financial investments with mission allows for the holistic evaluation of social and financial objectives

Historically, a disconnect has existed between the philanthropic mission and the investments made in their endowments. This pattern has begun to change in recent years (see our 2015 report The Future of Foundations: Impact at Scale). Interviewees for this report noted that aligning financial investments with mission allows for a more holistic evaluation of social and financial objectives, and increases the likelihood that management is accountable both for financial performance and managing conflicts of interest between financial objectives and mission-related goals.

Funders can enhance mission and avoid headline risk if the funds are invested in a way that aligns with their mission

Sustainable finance including Environmental, Social and Governance (ESG) analysis is one natural extension of the transparency that funders seek as they incorporate a greater focus on governance, which includes transparency. Philanthropies can leverage ESG as a market-driven approach that incorporates an awareness of governance to amplify the social and financial returns of their investments.

Donor Advised Funds

DAFs enable donors set aside funds that are invested in the market for the time being but are paid out for charitable purposes in the future. The benefits go beyond the tax benefit in the year in which the donations are made into the fund as DAFs have lower minimum contributions and lower setup costs than other tax-advantaged giving vehicles. More importantly, DAFs enable legacy-building gifts over longer periods on issues that are dear to the donors. Since their introduction, amount of assets in DAFs have grown substantially.

The tax-advantaged nature of DAFs creates a responsibility for DAF investments to have positive impact.

Interviewees expressed a view that the tax-advantaged nature of DAFs, like all tax-advantage structures, do create a responsibility for the funds donated to have a positive impact even before being paid out as charitable contributions. DAFs can incorporate mission into the investing process across all asset classes through social screens, ESG integration and traditional impact investments. This leverages the capital invested and increases the scale of mission-related impact.

The best way to maximize the value of this tool for addressing issues is a hotly debated topic. The smaller scale nature of DAFs means that these vehicles can target smaller, local issues. Conversely, interviewees stated that DAFs, on a larger scale, hold huge potential as a tool to combine philanthropy and investing. DAFs, like any pool of capital, could be pooled with like-minded donors and managers for specific projects to increase the scale and scope of impact. The range of possibilities for mission-aligned DAFs to address issues of all shapes and sizes is an important and worthwhile discussion.

The Benefits and Pitfalls of Corporate Philanthropy

Well-crafted sustainable business practices contribute to the advancement of a company's long-term performance and should be focused for the company's strategy.

Finally, interviewees recognized that companies have traditionally optimized their businesses for economic returns and engaged in philanthropy separately from their strategies. By integrating philanthropy, business strategy and investment, however, companies can reach a wider range of stakeholders than they can through a discrete focus on philanthropy. Aligning philanthropic and business strategies can also deepen a company's impact by concentrating a greater absolute amount of capital can flow into similar thematic areas.

However, if moving to integrate philanthropy throughout the business model, companies risk stakeholder frustration if they don't communicate effectively. If stakeholders expect explicit philanthropic efforts and don't understand companies' sustainability strategies, the credibility of corporate efforts can suffer.

Conclusions

Interviewees agreed that capital markets and philanthropies working together offer a good opportunity to introduce sustainability into mainstream business. While the process of collaboration is far from straightforward, it is key to solving the world's largest issues. Partnerships, integration of philanthropy into business strategies, and innovative types of investments, including impact-focused investments, can transform the traditional economy to be more inclusive and environmentally friendly. In doing so**, philanthropies and capital markets can help achieve a new form of regenerative and sustainable capitalism.**

Cornerstone Capital, as an investment advisor, helps its clients navigate the intersection of philanthropy and investment. As a purpose-built, research-driven, sustainable finance firm, Cornerstone works to systematically incorporate sustainability into mainstream capital markets and assist foundations to integrate sustainable investment into their portfolios.

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