Responsible Impact Investing

SUMMARY

CREATING IMPACT WITH A FOUNDATION'S ASSETS: MISSION (IM)POSSIBLE?

A comprehensive study covering Switzerland and Liechtenstein

Supporters: Swiss Sustainable Finance, Liechtensteinischer Bankenverband, Vereinigung liechtensteinischer gemeinnütziger Stiftungen e.V. vlgs, Basellandschaftliche Kantonalbank

IN BRIEF

- Guidelines, workshops and information events encourage foundations to use their assets to support the foundation's purpose: but what is happening on the ground?
- Through a survey of more than fifty foundations, this study assesses the state of implementation and uses its findings to recommend ways of stimulating further developments.
- The interviews showed that all the foundation representatives questioned are familiar with sustainable and mission-related investments.
- Foremost among the motivations cited are personal values, avoidance of conflict with the foundation's purpose, or the achievement of an impact.
- To date, the implementation mainly takes the form of negative screening, followed by positive sustainability– or ESG–criteria and impact investments.
- The Swiss Foundation Code's recommendations are perceived as helpful, but the follow-through is hampered by a lack of external pressure, ideological reservations and insufficient know-how.

The interviews gave rise to recommendations for action on several levels:

- Increased financial know-how fosters an open attitude, as does the foundation's own modern conception of itself, in which wealth is also perceived as a means of achieving a positive impact.
- The foundations want their financial advisors to be credible partners, who study their individual needs and provide them with choice – also with regard to sustainability. These professionals' expertise in the area of sustainable and mission-related investments should be a core component of the advisory process and accompanied by honest communication and sound reporting.
- Access to sustainable investments can be promoted through greater transparency in the offer and the communication of positive examples or creative solutions, taking account of the foundations' know-how.
- Other factors that could speed up implementation include greater interest or even gentle public pressure, or flexibility and encouragement on the part of the authorities.

Quotes from partners in this study

"The common-benefit foundation should seek to create an impact not only by distributing contributions, but also through the investment of its assets."

– HANS BRUNHART, VLGS

"Mission investing gives foundations the opportunity to increase their impact in a context of declining returns."

– SABINE DÖBELI, SWISS SUSTAINABLE FINANCE

"Sustainable impact investments take centre stage when it comes to investing assets responsibly for the long term. For common-benefit foundations in particular sustainable investments can deliver a double return."

– PATRIK JANOVJAK, BLKB

„Liechtenstein, with its numerous common-benefit foundations and long-standing experience and expertise in wealth management, is almost predestined to play a pivotal role in socially responsible investing."

– SIMON TRIBELHORN, LIECHTENSTEINISCHER BANKENVERBAND

„Over the past twenty years, impact investments have proved remarkably effective in terms of generating risk-adjusted performance while delivering solid social and environmental impacts. While their diversity and quality has been expanding, demand as well has been rising."

– DOMINIQUE HABEGGER, DE PURY PICTET TURRETINI

INTRODUCTION AND STUDY OBJECTIVE

In view of the declining returns on asset management, as well as the budget cuts affecting some foundations' project work, a new point of view is gaining ground. On all sides, foundations[1] are being encouraged to make fuller use of their potential by targeted investment of their assets. Why use just a fraction of their assets, namely the interest and capital income, when they could put their entire assets to work in the service of the foundation's purpose?

Foundation associations in the German-speaking and Anglo-Saxon countries are already issuing copious guidance on this topic. In Switzerland and Liechtenstein the Swiss Foundation Code's explicit recommendations concerning the impact of wealth have triggered a paradigm shift. When it comes to implementing a foundation's purpose, the financial sector is seen as just as important as the grant-making sector to raising the overall impact.

The goal of the present study is to assess the state of implementation of mission-related investing and the corresponding needs of foundations in Switzerland and Liechtenstein. On the basis of the findings, it provides concrete advice as to how the different participants in this field can bring about further progress. Through its facts and insights this study intends to do more than facilitate access to a complex topic. Its proposals should also foster mutual understanding and dialogue between the various parties.

DEFINITIONS

The English terms "mission investing" and "mission-related investing" distinguish between two approaches:

• **Mission-compliant investing**, aimed at aligning the foundation's investment policy with its charitable purpose;

• **Mission-promoting investing**, aimed at participating proactively in achieving the foundation's goals.
Mission-compliant investment is already relatively easy to implement, thanks to the numerous forms of sustainable investment now available. Mission-promoting investments, on the other hand, often entail considerably more individual effort, since there are few standardised ways to participate. One increasingly common form is impact investment.
Several surveys in Switzerland and Germany in recent years have investigated the professionalism of asset management in the foundation sector and the significance of mission-related investing. They came to similar conclusions:

- The foundations spend relatively little time on asset management compared with project work: shortcomings were noted, for example, in the independent performance evaluation of asset management mandates
- The foundations are well acquainted with sustainable and mission-related investments: a good third of those surveyed apply the relevant criteria.

1 This expression will be used for charitable foundations and other non-profit organizations (NPOs)

RESULTS OF THE SURVEY

These findings from earlier surveys are verified by means of the interviews with fifty-one representatives of foundations in Switzerland and Liechtenstein. The areas covered are asset management structure and costs, and particularly, mission-related investing. In addition to questions concerning the state of implementation, the survey places great emphasis on the foundations' preferences and needs. Based on the foundations' concrete wishes and suggestions of necessary measures, we present a catalogue of recommendations, aimed at harnessing more of mission investing's potential.

General questions about the interviewees' approach to asset management

- Many of those interviewed are responsible for foundations whose **assets exceed the average for Swiss foundations**: 25 per cent of the foundations surveyed have assets in excess of CHF 50 million and 25 per cent have more than CHF 150 million.
- Of the Swiss foundations questioned, 80 per cent have **investment regulations** and 90 per cent work to **a written investment strategy**. The degree of organisation rises with increasing wealth. This also applies to the establishment of an investment committee and an independent controlling function. Thus, 68 per cent of the foundations have an investment committee and 72 per cent conduct a neutral review of the investment results.
- Close to three-quarters of the foundations (72 per cent) engage an **external asset manager**; only 15 per cent make their own investment decisions.
- To date, only 9 per cent are fully invested in **passive instruments** while 56 per cent manage their investments actively to a large extent.
- The **investment strategy** (particularly the allocation to shares and bonds) varies considerably: although many foundations (44 per cent) place less than 40 per cent in equities, 22 per cent have more than half their assets in that class. At grant-making organisations the equity portion is significantly lower (maximum 33 per cent);
- For many foundations, asset management is undergoing an upheaval, driven by the low-interest-rate environment, the **professionalisation of the foundation sector,** and **increasing cost-consciousness**. This last includes looking closer at their hidden costs, and economising by pooling their investments with those of other bodies or inviting new tenders for the management mandate.

This synopsis indicates that the foundations in the sample are better organised than the average in terms of their asset management. Furthermore, their readiness to be interviewed on the subject of mission-related investing implies a positive bias in their statements.

Importance of sustainable and mission-related investments

- **All the foundation representatives are familiar with sustainable or mission-related investments, or the requirement to avoid conflict between the foundation's investments and its purpose**. Among them, 84 per cent discuss the subject internally, though Liechtenstein has some catching up to do, since a third of its foundations have not tackled the question.
- As **motivation**, the respondents frequently mention personal values or an ethical stance, or the founders' own values. Avoidance of contradictions plays just as important a role as the desire to achieve a specific impact through the investment. Some foundations also see it as their fiduciary duty to carry out to the full their common-benefit mandate and to develop the assets.
- Three quarters of the foundations now have **sustainability-related objectives in their investor guidelines**. Here too, the aid organisations are in the vanguard (100 per cent) and the Liechtenstein foundations are less systematic.

- Among the **methods** adopted, negative screening takes priority: nineteen foundations exclude firms with controversial business activities, while another five also look into their business processes in relation to issues such as child labour and human rights. Nineteen foundations use positive screening or environmental, social and governance factors. The scope of application varies widely: foundations with small positions in sustainability funds exist alongside others that apply ESG criteria to every mandate. Frequently they use a combination of different practices. A surprisingly high proportion of the foundations have experience of impact investing: sixteen have invested at least a small share of their assets accordingly, often in microfinance. Some are also working in synergy on projects or are planning mission-promoting investments. In many cases, one senses a real energy, aimed at expanding existing mandates or taking further steps.

Influential factors and experience with sustainable and mission-related investments

- More than 80 per cent of the foundation representatives are familiar with the revised **Swiss Foundation Code** (SFC) and its recommendations concerning the impact of assets. The ZEWO quality seal, which also introduces new standards for the establishment of investment regulations and consideration of ESG criteria, is more relevant to the grant-making organisations and is also known to the interviewees. Many foundations have high regard for the SFC as a source of guidance. A few believe that progress can only come with a new generation of board members. The idea of a binding SFC was clearly rejected; at best, self-regulation of large foundations on the principle of "comply or explain" seems realistic.
- On the question of **factors that hinder** greater implementation of mission-related investing, a distinction can be made between lack of incentive and concrete operational problems. **Lack of external pressure** is cited as the reason for not discussing mission-related investing internally, since "nobody cares". Other matters often take priority in the foundation's daily business. In addition, boards of trustees can be sceptical or have ideological reservations, or lack the knowledge or the courage to consider new concepts. And frequently, the founders are not properly informed about the possibilities for achieving an impact through the investment of their assets. In a few cases the old belief is still firmly entrenched that the investment yield must be maximised in order to have sufficient resources for projects.
- As regards **concrete implementation**, the representatives regret the **lack of standards** and the complexity of the subject. Only with the aid of additional expertise (and the higher costs entailed) are they able to reach a final decision. And for quite a few, the reporting is barely satisfactory. In addition, they worry about reducing the investment universe too radically as a result of the criteria, or incurring a cluster risk through the focus on certain sectors. Furthermore, there are few opportunities for foundations in the cultural sector to support their stated purpose through direct investment.
- **Banks and intermediaries also seem to be lagging behind**: not all financial players have the necessary know-how, or perhaps even an interest in acquiring it. Sometimes they are simply not open to including such offers in their product range. Some consultants also lack the knowledge or experience, so that in principle they advise against mission-related investing.

Preferences regarding sustainable and mission-related investments

- In addition to being perceived as highly important to implementation, **negative screening features prominently among the preferences**. The exclusion of companies owing to controversial business activities is seen as more important than exclusion on the grounds of controversial processes or the need to avoid conflict with the foundation's purpose.
- The assessment of approaches based on **positive screening (best-in-class)**, also corresponds to implementation from this perspective.

- **Whether for funds or mandates, the integration of ESG criteria** based on their financial materiality clearly meets with less approval. Nevertheless, a few participants already expect the financially relevant ESG criteria to be integrated.
- As **investments that directly support the foundation's purpose**, the interviewees express a preference for impact investing. Many have concrete experience in the area of microfinance or through their own participation in projects.
- On the subject of **engagement** – the critical dialogue with the managements of controversial companies – it is clear that so far only a few foundations are familiar with the possibilities. This shows that the opportunities for collective engagement through specialised providers or fund solutions are largely unknown.

RECOMMENDED ACTIONS FOR THE PROMOTION OF MISSION-RELATED INVESTING IN SWITZERLAND AND LIECHTENSTEIN

Based on the measures proposed by the foundation representatives to strengthen awareness of this subject, the following ten areas of action are recommended:

1. Modernise the foundations perception of their role

The basic idea that foundations use their resources in conformity with their purpose should also apply to their asset management. This approach focuses on achieving just as much impact with the assets as with the foundation's projects, instead of maximising returns and thereby funding projects. It requires the courage to innovate, as well as collaboration between colleagues on the funding side and the investment professionals. But it promotes shared knowledge and optimal solutions.

2. Improve the foundations' financial know-how

The current environment calls for increasing professionalisation of the foundations with regard to financial investment. The more knowledgeable in this area the foundation boards and management, the easier the integration of mission-related forms of investment. Neutral information and support from the associations is seen as extremely helpful in this respect.

3. Increase the credibility of banks and asset managers on this topic

The foundation representatives demand credibility from their financial partners in relation to mission investing. This includes transparency and honesty about both positive and negative examples, in order to build mutual trust. They also expect financial professionals to propose solutions that go beyond their own product offer and to embrace their social responsibility actively.

4. Promote transparency in the types of sustainable investment

In view of the multiple facets of sustainable and mission-related investment, interviewees frequently expressed a desire for greater transparency: whether through uniform terminology, standardisation and independent labelling or easier access to the relevant offers.

5. Offer the foundations individual solutions

The foundations increasingly expect to receive an individual offer that covers their needs, based on a specific analysis. This is not only a matter of providing more products tailored to the foundation sector. On the one hand, foundations with less financial know-how need more ample basic information. On the other, professionally managed foundations are looking for more creative, possibly unconventional types of investments.

6. Increase financial professionals' expertise with regard to sustainability

Every bank should be capable of making proposals that address sustainability. They should also offer a choice of approaches, some more rigorous than others. The integration of ESG criteria into conventional financial analysis or consulting is perceived as professional and credible. Then again, the banks should enlarge their offer as regards direct implementation of the foundation's purpose in the social or cultural sphere. Intermediaries must also increase their expertise. They are frequently felt to have been a limiting factor.

7. Develop communication and reporting

In their product offer, some banks incorporate sustainability criteria only upon request. A more offensive approach is desirable, starting with making the advisors more sensitive to the subject. Foundations also seek clarity and transparency in the presentation of the offer, which should be easily comprehensible, with no greenwashing. This applies equally to the reporting, which should also contain information about the impact of the investment approaches used.

8. Foster creativity in the investment process by citing good examples

Mission-related investment often requires creative solutions. More positive examples of committed, successful foundations and completely honest accounts of failure can stimulate dynamism and initiate a learning process. The report's case studies also reveal that foundations can contribute their own know-how to developing fund solutions and thus promote innovation.

9. Increase the authorities' openness and flexibility

The authorities must remove the blockades that restrict the foundations' use of mission-related investing. This primarily concerns the tax authorities' stance on impact investment. But the interviewees also wish to see the authorities supporting the process of mission-related investing. In particular, they want the supervisory authorities to play a more active role, by "differentiating, ordering, recommending and stimulating".

10. Strengthen the binding character of the Foundation Code

The Swiss Foundation Code is much appreciated; but so long as there is no pressure to comply, its voluntary nature will not suffice for broader application. This prompts the question of how to create a better incentive system. Greater public interest or even media pressure can help just as much as stimulation from the authorities.

The present study and resulting ten-point plan show that impact investment is on the brink of a breakthrough. Many of the foundations interviewed are familiar with the subject and find this approach increasingly appealing. At the same time, the sector and the market in general have a lot more to do; for example, removing obstacles and building expertise, while, on a broader scale, there still seems to be ample potential for greater collaboration between all the players concerned. That last point is particularly important, since mission-related investing often consists of individual, creative solutions that cannot be obtained "off the peg". However, good approaches and positive energy are evident in many areas, so that the proposals may well contribute to adjustments or acceleration, and therefore more effective use of the opportunities inherent in impact investing.

PRODUCT OVERVIEW

The extended version of the final report includes as an appendix a selection of providers of sustainable mandates and funds in Switzerland and Liechtenstein, together with a list of financial institutions dealing in microfinance and some thematic funds in this segment.

Further information is available on request on the website: www.responsible-impact.com

Responsible Impact Investing

Swiss Sustainable Finance

LIECHTENSTEINISCHER BANKENVERBAND

Vereinigung liechtensteinischer gemeinnütziger Stiftungen e.V. vlgs

Basellandschaftliche Kantonalbank

GlobalanceBank

Enabling Microfinance AG — not for our profit

DE PURY PICTET TURRETTINI & CIE SA

Responsible Impact Investing

Dr. Ingeborg Schumacher-Hummel
Managing Director

Grundwiesstrasse 2
CH-8700 Küsnacht
schumacher@responsible-impact.com
Tel +41-79-309 12 05

www.responsible-impact.com