NEGATIVE RETURNS: THE IMPACT OF IMPACT INVESTING ON EMPOWERMENT AND ADVOCACY

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In the long history of American foundations, these institutions have continually sought to maximize the impact of their gifts. Early leaders in the foundation world, such as Carnegie and Rockefeller, tried to apply a scientific method to grantmaking, emphasizing their own strategic approach to taking on selected problems (Fleishman 2007, 59). Specific orientations have changed over time but the central question remains the same: "given limited resources, how can our philanthropy be most effective?" Moreover, "how is the effectiveness of grants to be measured?" In recent years foundations have turned toward a new rigorous means of trying to understand how to increase the impact of dollars spent (Salamon 2014; Brest and Harvey 2008). In this regard the movement toward "impact investing" appears to hold out great promise for the foundation world. Unfortunately, however, a side effect of impact investing may be to reduce the impact of nonprofits on grassroots empowerment and advocacy.

Reducing the political effectiveness of nonprofits and their ability to represent the most marginalized in American society is not the intent of U.S. foundations. As some of the articles in this symposium make clear, there are foundations actively working to drive policy change through their donations. But impact investing does not reflect political or policy concerns. Rather, this emerging strain of thought in contemporary philanthropy is focused on increasing the effectiveness of foundation giving through new means of financing charitable projects, prioritizing capacity building, and more accurately measuring what grantees are actually accomplishing. These goals are complex but the strategy is built on the simple financial concept of leverage: using one dollar to generate more dollars. Leverage offers a way around an enduring problem: each foundation can only spend what the return of their endowment (or other money it has raised) allows them. Conceiving of grants as *investments* and becoming more disciplined

about maximizing leverage with their funds, gives foundations the opportunity to move beyond the previous limits of their resources.

This paper explores this trend with a close examination of three interrelated aspects of impact investing. The first step is to look at the conceptual base of this movement, the business yardstick of return on investment (ROI). A common assumption is that if foundations are to maximize leverage, they must be more businesslike. When they invest money, private sector enterprises make a crucial calculation: over a given time period, for each dollar invested, how much return do they anticipate? For foundations the return on investment has traditionally relied on a qualitative assessment of whether they're doing good with their grants to nonprofits. Second, we'll look at capacity building. Leverage can be obtained by giving grants to nonprofits for building up the organizations themselves. If a grant helps a recipient organization become more efficient or effective (or both), then the foundation gains a greater return on its money. Third, a foundation can only know if it is receiving a satisfactory return on investment if it can measure outcomes. Careful and valid measurements must be taken if foundations are serious about understanding the efficacy of their grants.

Yet if a foundation is to truly maximize its impact, advocacy may be the ultimate leverage that allows it to accomplish its goals (Berry 2015). By "advocacy" I'm referring to efforts to influence government at any level. Advocacy includes direct lobbying of legislative or administrative officials, litigation and other legal stratagies, grassroots mobilization, and efforts aimed at influencing public opinion. Nonprofits vary greatly in the degree to which they engage in these activities and, similarly, foundations vary greatly in the degree they are willing to support advocacy.[1]

This paper builds on recent literature on impact investing, examination of evaluation reports on such practices, and upon interviews with foundation executives, consultants in the field, and leaders of nonprofits. These interviews utilized a modest number of open-ended questions while relying on probes and follow-ups to extend discussion and explore additional topics. The interviews were done on a not-for-attribution basis.[2]

Return on Investment

In India the government provides limited financial assistance for maternity care for low-income families (those with $2 to $5 a day in daily household income). This hardly seems like a lucrative market but, nevertheless, LifeSpring, a partnership between Acumen, a U.S. based nonprofit global investor and a corporate entity created by the Ministry of Health in India, set out to try to turn a profit in this sector. LifeSpring now has six 20-bed hospitals that operate "as high volume, low cost businesses [targeting] high occupancy, utilization and turnover rates in order to ensure profitability." Remarkably, it reached the break-even point after only 18 months (O'Donohoe 2010, 53).

LifeSpring represents the ethos of impact investing: *doing well by doing good*. It combines financial rewards with societal benefit, achieving a "double bottom line." In the case of LifeSpring, profit offers the opportunity to expand maternity care or provide additional services. In other cases social benefits are combined with monetary returns to private investors. In a concise way social impact investing can be described as "the use of multiple instruments in addition to grants in order to leverage available resources to maximize social or environmental impact" (Salamon and Burckart, 2014, 169). The focus of such investments are "bottom of the pyramid" populations—those at the lowest level of the income scale who need health and welfare services (Saltuk, 2011, 10). Investors, including individuals, for-profit institutions, and

foundations and other nonprofits, can access such projects through both middlemen—dedicated financial institutions specializing in this sector—and investment banks offering impact investing funds.

This may all seem far afield from foundation practices. Yet foundations are being drawn into impact investing by the seductive appeal of investing as an alternative to traditional grants. Some foundations, like F.B. Heron, now operate as foundation banks, making investments rather than grants, through loans, loan guarantees, fixed-income instruments, and equity (Salamon and Burckart, 2014, 165). A fundamental attraction of impact investing to foundations is that it fits very well with their orientation toward initiating something new; foundations want to be able to take credit for facilitating or catalyzing innovation without assuming long-term financial responsibilities. Impact investing by foundations can be similar to venture capital support of for-profit start-ups. The Omidyar Network works "across the social and business sectors, operating both a Limited Liability Company (LLC) and a 501(c)(3) foundation." Its mission is to "invest in entrepreneurs and their visionary ideas that create opportunities for people to improve their lives."[3] Omidyar's investees include Change.org and NationBuilder, nonprofits that provide software for social action and community organizing, as well as HealthKart and Quikr, electronic marketplaces for consumers in India. The massive Chan Zuckerberg Initiative appears to embrace a LLC impact investment structure as well. Foundations, of course, have long helped to start new nonprofits but this recent impetus is aimed at developing dedicated arms devoted to funding start-ups with investment support rather than outright grants.

It is not clear how much foundation money is being spent this way as opposed to traditional grants but what is clear is that impact investing is receiving a lot of attention in the foundation world. There is no shortage of evangelism pushing foundations and other potential

investors toward a double bottom line strategy. Matthew Bishop and Michael Green preach the divinity of “philanthrocapitalism,” arguing that impact investing is much more than an alternative means of doing good. Rather, “philanthrocapitalists see a world full of big problems that they, and perhaps only they, can and must put right” (2008, 3). Evangelism for impact investing and the pursuit of ROI also comes from business firms and nonprofits that act as middlemen. Capital aggregators assemble investors who pool funds into investment levels appropriate for a variety of projects and organizations. Another set of middlemen are enterprise brokers. They directly link investors with interests in promoting social and environmental goals to specific projects offering market-level returns (Salamon 2014, *passim*).

Individual consultants have built specializations in various niches in this complex array of financial instruments. In one interview I asked a nonprofit director if she ever focused on ROI in her grant applications. Since most of her agency’s clientele are abjectly poor she said she “didn’t know how to think about ROI.” But she then added that a consultant she used to help her agency raise money from foundations was always asking her, “what about return on investment?” When I asked why the consultant was focused on ROI, she responded, “Because she’s very creative and she’s looking for fame and glory. She’s trying to carve out a niche.”

Unfortunately, empowerment and advocacy fit very poorly into an ROI framework. Problems of measurement are discussed more fully toward the end of this essay but at a conceptual level, it’s difficult to define what constitutes advocacy return. An executive with a health-related nonprofit explained that “it’s been difficult for me to make [my board] understand that empowerment is a deliverable.”

At the heart of this problem is a mismatch between the way foundations distribute their available funds and the very nature of advocacy. Affecting change in public policies is a long-

term process. The president of a foundation noted the disjunction: “foundations fund grants in the range of one to three years. That doesn’t square with the realities of how long it takes to achieve social change.” Foundation officers need to show impact, whether it be ROI or a more traditional conception of impact. The time horizon for achieving change in the political world means that those foundation officers would have to tell their management or board that the grants they’ve awarded for advocacy may not show a payoff for years to come. That’s a tough sell and such grants may be seen as unlikely to help one climb the ladder of success in the foundation world.

Capacity Building

If foundations and other institutions are to maximize leverage with their dollars, they need to invest in those nonprofits that have the capacity to effectively implement programs, grow in revenue, and achieve results that influence the broader field. Thus, capacity building is directly tied to return on investment as high capacity organizations are, understandably, seen as more likely to deliver the goods.

“Capacity building” is an inherently ambiguous term. In his book on the subject Paul Light defines it “as any effort to increase, replenish, or improve an organization’s capacity” (2004, 53). This non-definition definition perfectly captures the all-encompassing nature of capacity building—it’s what anyone says it is. Still, practitioners, especially consulting firms, do identify the qualities they regard as most important. For example, Grantmakers for Effective Organizations, list eight areas as key to building capacity: leadership, vision and strategy, program delivery, fundraising, financial management, communications, technology, and strategic relationships.[4]

The emphasis on capacity building derives in large part of the stereotypical image of small and medium-sized nonprofits as being run on a shoestring, managed by a few overtaxed individuals whose training did not prepare them for all that is required to run an organization. Christine Letts and her colleagues write in the *Harvard Business Review* that nonprofits "often lack the organizational resources to carry out the programs they have so carefully designed and tested." They also scold foundations as well because "in the process of making a grant, foundations often overlook the organizational issues that could make or break the nonprofit" (1997, 36).

These long-standing critiques have led to a greater weighting of capacity building in foundation grant making. As contradictory as it may seem, one reason why nonprofits may lack sufficient capacity to excel is because they are expected to be lean, no-frills, low salary, low overhead organizations (Pallotta, 2008). Once the concept of investing began to take hold in philanthropy, though, business practices from the private sector became more relevant in foundation strategizing. A consultant specializing in capacity building said in an interview, "Who in the private sector asks, 'does it [pay] to train our people?'"

Since foundation grants continue for only a limited time and are often awarded to a nonprofit so that it can start up a new initiative, there is always the question of the "exit strategy." Foundations want to know "how does the nonprofit keep the new initiative going after we've stopped funding it?" It is in this context that impact investing offers a solution. If money is leveraged through an investment rather a traditional grant, the enhanced economic activity can lead to sustainability. This is the Holy Grail of foundation giving: a grant that doesn't need to be renewed but will, nevertheless, have a lasting impact. In the words of one foundation officer,

"This is a funder's dream, because you won't feel guilty after you stop funding" (Seedco Policy Center, 2007).

This focus on capacity building in the nonprofit world is pushed forward not only by foundations but also by an extensive infrastructure of consulting firms marketing their expertise in this area. The large roster of consultants includes national firms like McKinsey which, in addition to its private sector work, operates a robust nonprofit practice. There are also many firms that specialize in nonprofit consulting, some of which are nonprofits themselves. Bridgespan is one of the best known and says its goal with clients is to strengthen "the ability of mission-driven organizations and philanthropists to achieve *breakthrough results*."[5] The private sector TCC Group has a strong nonprofit practice with a particular focus on capacity building. One of its products, the Core Capacity Assessment Tool (CCAT), priced at $350, is a 146 item online questionnaire that measures a nonprofit's capacity along four dimensions. The firm also offers more direct consulting with an emphasis on leadership and what it calls "adaptive capacity"[6]

What is perhaps most surprising about capacity building is that despite its centrality to foundations, nonprofits, and consulting firms, there is a great deal of uncertainty about whether it achieves anything significant (Light 2004, 44). Melinda Tuan, a leading consultant on nonprofit capacity building, concludes that there is a "lack of meaningful, practical, and consistent methods of evaluating the effectiveness and impact of organizational capacity building" (2014, 233). But it is far more than the absence of consistent measures that is the problem. More essentially, it's difficult to operationally define what is to be measured. In all the various schemes for building nonprofit capacity that I examined, improving organizational leadership was at very core of strategies to improve performance. Is there anything more elusive than

measuring the impact of leadership? And what does improved leadership bring to a nonprofit? A study of “high impact” nonprofits by Grant and Crutchfield (2007) found that internal management capabilities were not related to these organizations’ success. The Center for Effective Philanthropy concluded that capacity building had little chance of working unless it was comprehensive: “Providing just two or three types of assistance to grantees appears to be ineffective” (Buteau *et al* 2008, 5). More than a few forms of assistance are, however, very expensive and beyond what most foundations are willing to support in their capacity-building grants.

A clearer case can be made as to the relationship between capacity building and any emphasis on strengthening nonprofit advocacy. Building up the capacity of nonprofits to improve their efforts in community organizing, lobbying, or other forms of advocacy, doesn’t appear to fall into foundations’ conceptions of what constitutes capacity building. In a survey the Center for Effective Philanthropy asked foundation grantees about fourteen different types of capacity building (Buteau *et al* 2008, 8). Not one of the fourteen capacities had anything to do with advocacy. More broadly, in reading through the literature on nonprofit capacity building, there is scant mention of the subject.

Interviewees confirmed that foundations do not see a link between building capacity and advocacy. As one consultant who works with foundations put it, “the resistance comes largely from foundation people’s level of comfort with advocacy.” An executive with a nonprofit infrastructure group noted that “Foundations don’t understand what they can do in terms of advocacy. A lot of them think that advocacy is what Saul Alinsky did. . . We need to educate foundations on this.” Yet there is no reason to believe foundations want to be educated on how advocacy is part of organizational capacity.

Measuring Outcomes

In an era where statistics and analytics are of paramount value, there is a strong imperative to quantify the true impact of impact investing. This pressure comes from foundations that make such investments, from donors and investors who want evidence that their money is doing what was promised, from consulting firms that want to win contracts to conduct the measurements, from the boards of directors of nonprofits who want the best tools at their disposal to oversee the work of their professional staffs, and from the staff of nonprofits themselves (Schambra 2013). Although the need for evidence creates additional work and internal challenges for the management of nonprofits, these individuals want to be able to show that their work is effective. The CEO of a community development nonprofit said that while it gathered the numbers at the request of the foundations that fund the organization, “It’s important to have these numbers for ourselves. We have to ask ourselves if what we are doing is working.”

Although foundations frequently ask for evaluations and may favor quantitative scoring of program impact, they actually seem of two minds as to the value of rigorous analysis of their grants and investments. For those adopting an investment strategy, the obvious incentive is to validate their efforts by demonstrating the effectiveness of leveraging the dollars they distribute. Even for those foundations operating through a traditional grantmaking structure, there are reasons to pursue exacting measurement. Foundations may feel that they need to keep up with the trends in their field when they believe other foundations have adopted these oversight processes.

There are also reasons why foundation executives and program managers may want to avoid independent, statistical assessments. The reality of program evaluations is that they create considerable risk to all those who have supported the program being measured. If the numbers

come back as negative, that may not only reflect badly on the nonprofit carrying out the mission, but also upon those foundation officers who greenlighted the grant. The nonprofit, Evidence Action, dewormed 17 million children in India but somewhat surprisingly didn't evaluate whether these treatments improved school attendance, school performance, or graduation rates (Hobbs 2014). One of the interviews I conducted was with the head of program evaluation for a large foundation that is quite forceful in claiming that it makes "investments" with its funds. When I asked him whether they were earning a discernible ROI in the nonprofits they invested in, he confessed that they don't actually do research that could show that. Instead, he offered me anecdotal evidence as to what works with its grantees.

For a foundation officer a qualitative self-assessment conducted by a nonprofit grantee, which is much more likely to downplay program shortcomings and to accentuate the positive, is a safer alternative to more rigorous evaluation. Foundations may not have professional staffers qualified to prepare statistical analyses and, thus, they would need to outsource such studies to a consulting firm. This reduces a foundation's control over the way that a given program is to be judged. Joel Fleishman notes that "Foundations usually shy away from empirical measurements of the extent of their impact. They are wary about sharing information about their choice of goals and the strategies they employ to achieve them" (2007, 96).

Whatever the reasons, the feedback loop on program performance seems tenuous. Based on its surveys, the Center for Effective Philanthropy found that foundation officers "know little about the actual results of the assistance they provide." Of the minority of foundation officers that do follow up with their grant recipients, "nearly 90 percent indicated that they do not look for changes in grantees' work or organizations related to the assistance they provide" (Buteau *et al* 2008, 5-6). I asked the CEO of a health-related nonprofit if foundations ever came back to

determine if new programs initiated through their grants were, in fact, sustained by the nonprofit when those grants expired. She replied simply, “No, that’s never happened.”

Beyond these concerns are real methodological issues involved in measuring social impact investing. There is no one generally accepted method to measure social and environmental impact and as a consequence, there is a great diversity of both approaches and levels of rigor in evaluations. The National Committee for Responsive Philanthropy (NCRP) calculates that for every dollar that a foundation or other donor provides to a nonprofit, the community benefit (ROI) amounts to $115 (Ranghelli 2012, 1). As one might suspect this sensational 115-1 return on investment is built on a rather expansive notion as to what constitutes “return.” For example, increased funding for public schools is counted by the NCRP as a return, even though increases in such spending can be the product of multiple advocates and might have nothing really to do with the work of a grantee in that community (Ranghelli 2012, 3). Nonprofits themselves are not terribly rigorous in the way they determine key indicators. An Urban Institute study found that of those nonprofits with at least $50,000 in annual revenue, 37 percent indicated on their 990 tax return that they spend absolutely nothing on fundraising (Light 2004, 49).

Since it’s difficult to quantify real impact, measurement of advocacy effectiveness tends to focus on rather mundane and minor program qualities. One community development director I spoke with told me that his reports to foundations about the impact of his organization’s community organizing were composed of measurements such as:

The number of people who show up for an event
The number of people who take on leadership roles
The number of people who speak at a hearing or meeting
How many people who participate are “not the usual suspects,” such as non-English speakers.

I asked other nonprofit directors the same question and received much the same answer: the metrics focused on participation, things that could be counted. The shortcomings of such advocacy metrics was amply illustrated by the head of a disease-related nonprofit. His statewide chapter was part of a federated structure and he had to report advocacy metrics along with all the other indicators of chapter performance to national headquarters. The national office had a point system and he explained that "You get three points if you actually speak with a member of Congress. You get fewer points for a letter or email to a legislator." Remarkably, what isn't covered under this point system is actually influencing public policy.

Conclusion

Impact investing holds out great promise but it's important to recognize its limitations. Some investments have been remarkably imaginative and brought together impressive partnerships among foundations, private sector and hybrid financial institutions, nonprofit service providers, and government agencies. By bringing in additional dollars beyond what government and conventional philanthropy normally generate, there is more being done to alleviate the ills that plague societies, particularly those in underdeveloped countries.

How much impact investing is taking place is not evident as there is no clearinghouse to monitor it and no any consistent way that has been utilized to measure it. Optimally, it will be used in targeted ways where the business model can entice new investment. But if impact investing grows considerably, it could produce winners and losers, a problematic outcome for philanthropy (Edwards 2008).

Foundations and nonprofits should be very precise in the way they use the language and business frameworks of impact investing. It is not a positive development for grants to be called investments when the change in the underlying financial instrument is superficial. New jargon

does not make foundations any more effective nor give them any more leverage. Much of what I came across in my research was old wine in new bottles.

There is reason to be concerned about how philanthropy focused on ROI, capacity building, and program measurement can affect the political system, including advocacy by nonprofits. All three of these interrelated set of goals have worrisome implications for advocacy. Advocacy by nonprofits is crucial to the representation of the interests of the most marginal, most disadvantaged sectors of society (Berry and Arons 2003). Despite the huge numbers of nonprofits in America there is far too little advocacy and impact investing will not remedy this inequality in our political system. Instead, it will likely make it worse.

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NOTES

[1] The legal context for foundation support of advocacy can be confusing but without going into the details of nonprofit law, it should be noted that it is perfectly legal for foundations to make general grants to nonprofits who, in turn, can use the funds for lobbying and other forms of advocacy (Berry and Arons 2003).

[2] Fourteen interviews were conducted for this study and the subjects were selected on the basis of their prominence in the field. Most interviews were carried out over the phone and lasted around 45 minutes each.

[3] Http://www.omidyar.com/.

[4] Http://www.geofunders.org/smarter-grantmaking/nonprofit-resilience/capacity-building.

[5] Emphasis in the original. Http://www.bridgespan.org/about/Our-Mission.aspx.

[6] Http://www.tccccat.com/; and Raynor *et al*., n.d.