THE IMPACTASSETS HANDBOOK FOR INVESTORS

GENERATING SOCIAL AND ENVIRONMENTAL VALUE THROUGH CAPITAL INVESTING

Edited by
JED EMERSON

7

Assessing Your Opportunities: The Challenge and Key Practices of Engaging in Investor Due Diligence

Sandra Osborne

In this chapter we will review in full the process of performing due diligence on a potential investee. We will walk through the various stages of the diligence process and provide key tips and things to keep in mind along the way. We will provide a framework that an investor can adapt and tailor as necessary for a given investment. Some of the key questions that we will address include:

- What is due diligence?
- What are the basic steps involved in a due diligence process?
- How in depth should my diligence be for a given investment type?
- What are the key types of things to look out for during the course of due diligence?

After reading this chapter, you should have the tools you need to develop your own due diligence process and thoroughly investigate an investment opportunity. Ultimately, the goal is to help you make clear and confident investment decision based on the due diligence findings.

This chapter has been published in 'The ImpactAssets Handbook for Investors' edited by Jed Emerson (Anthem Press, 2017)

What Is Due Diligence?

Due diligence is the comprehensive investigation undertaken on an investment opportunity in order to help the investor assess risk, return and impact as you make your investment decision. Within the impact investing space, this process encompasses both financial and impact analyses. The process begins as early as the first meeting with a fund manager or entrepreneur as any interaction is an opportunity to learn something about the character of the people running the enterprise under evaluation. The process is complete once an investor has thoroughly vetted every relevant aspect of a potential investee and can confidently come to a conclusion about whether or not to make an investment. The purpose of conducting due diligence is to fully understand the business model, identify key strengths and weaknesses and develop a risk-reward analysis, all of which will ultimately inform the final investment decision. Keeping in mind the fact that virtually all investment entails some level of risk, there is no guarantee your investment will perform well with both financial and social returns; but with these key practices in your tool kit, you'll be better prepared to assess the opportunities and understand potential pit falls.

Your due diligence process will vary based on a number of factors including life-stage of a potential investee, type of investment and size of investment. For example, performing a diligence on a start-up enterprise will be very focused on the character of the management team, the quality of the business model and future outlook of the market they are operating within, as very little historical track record will exist. On the other hand, an investor considering an investment in an established enterprise will have much more historical performance available on which to base an investment decision. Furthermore, it is important bear in mind the size and type of investment under consideration when considering the scope of diligence to perform. According to members of Toniic (a leading impact angel network), "due diligence should strike a delicate balance, collecting enough data for rigorous analysis and providing value while not exhausting the entrepreneur in the process. Your due diligence process should focus on information that will get you to a decision and be commensurate to the

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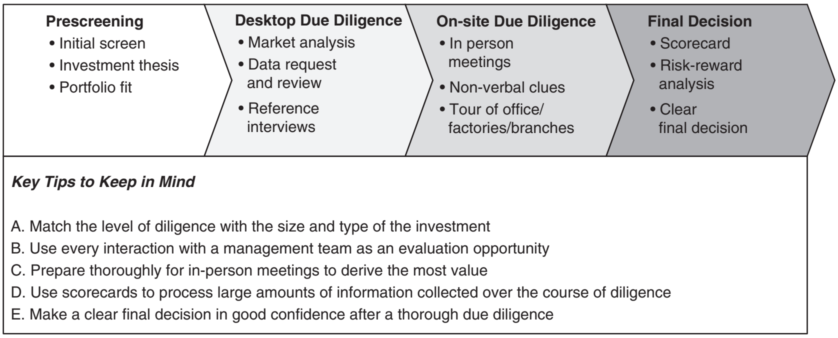
Figure 7.1 Stages of Due Diligence and Key Tips to Keep in Mind.



size and type of capital you are planning to deploy."[1] For example, an investor seeking to take a majority equity stake in a start-up enterprise is likely to spend significantly more time investigating a potential investee than would an investor looking to make a relatively small and short-term loan to a known entity.

At the most in-depth level, due diligence typically consists of four stages:

1. Prescreening,
2. Desktop due diligence,
3. On-site due diligence, and
4. The final decision stage.

We will review each in more detail in the ensuing sections but below is a brief snapshot of the key elements of each stage as well as the five key tips to keep in mind throughout the process:

Due Diligence Process

Pipeline Generation

The due diligence process begins with the first contact an investor has with the management team of a potential investment. As mentioned above, every interaction with the management team is in opportunity to ascertain information around the investment's value proposition. As such, deal sourcing is essentially the first step of deal vetting. Sourcing and identifying high-quality investment options is one of the most challenging steps. An investor looking to place capital is likely to be inundated with options; weeding through these options to identify investments of sufficient quality to move forward is the hard part. One option to help facilitate the sourcing is to invest in a structured product or fund. The choice between investing in a fund or investing directly into deals or companies is equally as relevant for impact investors as it is for conventional investors. While we would encourage investors operating independently to focus on a single category or invest in funds or through intermediaries in order not to have to become an expert in each are of potential interest, we present the pros and cons of both below:

If, after weighing the pros and cons of investing in funds or directly into companies, an investor opts for the direct companies, joining an angel group or network could serve as a beneficial aid in deal sourcing. Toniic, recommends finding "value-aligned networks of investors, impact intermediaries, impact banks, advisory firms, incubators, and fund managers who will allow you to coinvest, or select some of their deals."[2] Toniic members further provide the following recommendations:[3]

Figure 7.2 Pros and Cons of Investing in Funds versus Direct Companies.

Funds		Direct Companies	
Pros (+)	***Cons (–)***	***Pros (+)***	***Cons (–)***
• Portfolio diversification	• Removed from direct impact	• Engaged with direct impact	• Undiversified
• Less ongoing monitoring	• Manager fees can be high	• Avoid manager fees	• Ongoing monitoring required
• Lower risk	• No ability to impact direction of companies	• Ability to influence investment	• Higher risk

Figure 7.3 Options for and Benefits of Angel Groups and Networks.

Type	Description
Incubators and Accelerators	Help socially conscious start-ups refine their business models and prepare to pitch to investors.
Business Plan Competitions	Can help early-stage entrepreneurs connect with mentorship, practice pitching to investors and get their plans ready for first infusions of capital.
Networking Groups	Provide learning and community as well as access to resources for impact investors.
Deal Flow and Investor Networks	Can provide a wide variety of services like capacity building on the deal flow side as well as on the investor side, deal vetting, syndication services and more. Frequently only open to accredited investors.
Key Events and Conferences	Can include multisector events and keep you informed of impact investing trends.
Impact Intermediaries	Developing in regions around the world to support entrepreneurs and investors.
Crowdfunding	Provide opportunities both for “retail” investments (for nonaccredited and accredited investors) and “platform” investments (in crowdfunding platform enterprises for accredited investors).

Prescreening

Once an analyst has identified a potential investment, the formal vetting commences. The prescreening stage can be viewed as a relatively high-level review that confirms an investment meets minimum criteria from an investment standpoint and is a good fit from a portfolio standpoint. At this stage, an investor should seek out necessary documentation to form an initial understanding of the potential investment. These documents may include recent audited financials, a business plan (in the case of direct investment), offering documents and preliminary terms. A high level review of each of these will allow the investor to answer the question of whether the investment meets the initial criteria. In addition, prescreening will frequently bring to the surface questions or concerns to be further investigated once full diligence begins. Questions to keep in mind include:

1. What is the investment thesis from a financial and impact perspective?

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2. Does this investment provide an acceptable financial risk-return profile?
3. Does the impact value proposition align with the investors values?
4. What are the key risks associated with this transaction and what will an investor need to gain comfort with those risks during the diligence process?

As an example, at ImpactAssets, when we assess potential private debt and equity funds for inclusion on our Global Impact Ventures platform (GIV), we apply the criteria below as our first screen. As you develop your own approach, you might consider developing similar criteria that fits within your own investment philosophy.

Once it has been determined that an investment meets your preestablished criteria, it is also wise to consider how the investment will fit within the overall portfolio, prior to proceeding with full due diligence. Some important questions to ask on the portfolio side include:

- Does this investment fall within targeted asset allocation?
- Does this investment offer diversification benefit to the overall portfolio?
- Does this investment introduce concentration risk to the portfolio?

Figure 7.4 Sample First Screen Criteria.

First Screen Criteria for GIV Platform Candidates

- Private debt or equity, no publically traded investments
- Direct positive social and/or environmental impact; approach to measuring impact
- Strong investment thesis; range of financial returns acceptable
- Track record with previous funds or extensive experience with other funds
- First close by the time the investment panel reviews fund
- Open for at least a year between first and last close

- Does this investment have implications on near-term needs for liquidity (i.e., will the funds be locked up in an investment that can't be exited beyond the time an investor would otherwise need access to the funds?
- Does the time horizon of the investment fit within the needs of the overall portfolio?

With your sourcing process in place and these initial questions addressed, you're now ready to move on to your next step in the process.

Desktop Due Diligence

Once an investment has been prescreened and is determined to be a good potential fit for your portfolio overall, intensive due diligence commences with what is referred to as desktop due diligence. In this stage, an investor will gather and review an exhaustive list of documents and materials on both the potential investee and the market in which it operates. The purpose of this stage is to become as familiar as possible with every aspect of a potential investee. This stage also serves as important preparation for the next phase, on-site due diligence, when you will want to be fully prepared to ask the right questions and understand the venture you are touring. During desktop diligence, a number of questions are bound to arise that the investor should flag for further discussion during subsequent in-person meetings. By the end of the desktop due diligence, an investor should have a solid understanding of both the market landscape of a potential investee as well as a thorough grasp of the ins and outs of the business operations, with any outstanding questions organized in preparation for the next phase of engagement.

Market Analysis

Understanding the space within which a potential investee operates is a key component of desktop due diligence. An investor should seek out market reports, association annual assessments and any industry research available. The purpose of this research is to be able to develop an *independent* strategic

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view of where the potential investee sits within the broader market and what the total addressable market may be. While the potential investee is likely to provide an investor with their market perspective, it is important to engage in your own research as well. Internally prepared research by a potential investee is likely to present the investee in the best possible light. It is incumbent on the investor to cross-check and verify the company's purported market position and the opportunity they are promoting to you.

Data Request and Review

After the market assessment, the first step of digging into the potential investee itself is to gather and review the necessary legal, financial and organizational documents. This step can take different forms depending on the life-stage or sophistication of a potential investee. An established company or fund will likely have a number of relevant documents available on their website, or be able to provide access to a secure online data room. A virtual data room is an online space dedicated to housing documents and file sharing. If that is not the case, or if the website or data room does not contain everything necessary to complete desktop diligence, it is perfectly acceptable to send an exhaustive diligence request to the potential investee. A responsible investor mindful of the potential investee's time will first identify what information can be sourced independently and then pare down the diligence request to reflect only those items that are still outstanding. It is also important to keep in mind at this stage that the level of diligence undertaken should be proportionate to the size of the investment. A relatively small and shorter-term debt investment may not require the same level of information as a majority equity stake would entail. Below, we present sample documents to request from an investor that assumes a relatively large and high risk investment but should be pared back in the case of smaller, lower risk investments.

The topics that the diligence request will cover include specific documents on recent performance and projections, organizational structure and team, and operations and legal. Specific documents on recent performance and projections are the ones most likely to be found in a potential investee's data room. You should review these documents with a fine-tooth comb looking for any anomalies in the financials or projections or any other red flags, especially any qualified opinions by an auditor. The existence of red flags does not necessarily preclude investing. The purpose of this review is to first identify all red flags in order to prepare follow-up questions with the potential investee in determining whether there are sufficient mitigating factors to offset the red flags and move forward with the investment. The top 10 list of key documents to request that will help facilitate a thorough financial and business analysis in this category are listed below:

1. Articles of incorporation
2. Employee handbook or similar policy documents
3. Audited financial statements for past three years
4. Most recent unaudited financial statements
5. Five-year proforma financial projections
6. Any available third party reports
7. Two most recent annual reports to investors
8. Two most recent quarterly reports to investors
9. Two most recent impact reports
10. Sample of any other reports provided to investors

On the organizational side, an investor should look to gain a deeper understanding of the structure of the organization and key people involved. An investor should seek to learn who reports to whom, how long key team members have been working together and what is the pedigree and experience of the management team and staff. You should also be assessing the fundamental operating and governance systems of the organization. Are appropriate checks and balances embedded in the organizational structure? Does the team seem to chafe at getting you the information you request or in working with each other? In addition, information about the Board of Directors and any advisory positions will help you form an opinion regarding the quality of influential people involved. How often do they meet? How much do they really understand about the venture and its operating practices? Are they individuals with specific industry

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expertise or more general knowledge? A top 10 list of items to request in this category include:

1. Organizational structure chart with reporting structure chart for management and staff
2. Role, responsibilities and biographies of the board of directors, advisory board, management team and staff
3. Changes in the past 18 months and changes expected in the next 18 months among the board of directors, advisory board, management team and staff
4. Past working relationships among members of board of directors, advisory board, management team and staff
5. Conflict of interest policy and explanation and mitigation of any current potential conflicts of interest
6. Names, titles, tenure, experience, education and responsibilities of management and all staff members
7. Stakeholder diversity: percentage of female and percentage of underrepresented groups (e.g., ethnicities or other minority groups) for (separately) board of directors, management and staff
8. Annual board, management and staff compensation
9. Firm compensation structure, including any performance-based compensation and employee benefits packages
10. List of any significant compensation middle- to senior-level staff receive outside of the firm compensation

On the operations and legal side, an investor should look into the third party associations a potential investee has, including service providers and industry affiliations, and any legal issues they may be facing. Key questions to keep in mind include:

- What key functions have been outsourced?
- Is the investee using "best-in-class" service providers?
- Has there been any legal action taken against the potential investee or is there a risk of any?

The top 10 list of items to request in this category include:

1. List of all firm offices and associated personnel
2. List of any significant parent/subsidiary/joint venture agreements

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3. List of any key loans, contracts, conflicts or interrelations
4. List of any current or past legal actions taken against the firm or its funds and outcomes
5. Overview of any third party providers of firm's management information systems, including firm financial management
6. Overview of any other third party service providers, including legal services, tax, auditors and any other service providers
7. List and details of all banking relationships and credit availability
8. List of and documentation for any external regulations complied with or recognitions received
9. List and description of any participation in industry initiatives
10. List of any intrafirm social or environmental policies or initiatives

Recall that every interaction you have with a potential investee is an opportunity to assess something relevant to the due diligence process. In the case of the desktop diligence data request, the pace at which the potential investee is able to provide the requested documents and materials may be informative. Fulfilling an exhaustive data request within 24–48 hours likely indicates a high degree of organization and efficiency. On the contrary, if a potential investee is unable to fulfill a request within one to two weeks, it could be an indication that the organization has poor internal processes in place—which may not bode well for the future! That said, it could also be an indication that the management team is assiduously working to successfully execute on their business plan. Whichever conclusion you reach, it is important to keep in mind this is just one piece of the puzzle that forms the bigger picture you are attempting to sketch out through your due diligence process.

Reference Interviews

The final stage of desktop due diligence is to interview third party references. These are people that are independent from the day to day of the company but have sufficient involvement to be able to provide insights into its future prospects. Key people to consider for a reference interview would be people such as an independent board member, an advisory board member and/or a current investor. As the Bridgespan Group recommends in their blog entitled "Effective Philanthropy, Seven Questions to Ask a Member of a Nonprofit Board in Your Due Diligence," some important questions to ask, which also apply to for-profit investment opportunities, include:[4]

1. Why did you become involved in the organization, and what has your involvement looked like over time?
2. How would you characterize the role of the board of directors/advisory board/investors in the organization?
3. How would you describe the goals of the organization, and how does the organization achieve these goals?
4. How focused on results do you believe the organization is?
5. What attributes does the CEO have that will enable him or her to accomplish the company's goals?

On-site Due Diligence

After desktop due diligence is complete and an investor has gone through all of the necessary documentation, the next step is to pay the potential investee an in-person visit known as on-site due diligence. On-site due diligence is crucial for verifying everything learned thus far. There is no substitute for meeting a management team in person, on their turf, and witnessing firsthand their interactions with one another. In fact, you may well want to have multiple engagements with the management team over several months, depending upon the size and nature of the investment you are considering.

In addition, an investor should want to see for themselves "how the sausage gets made." Whether performing diligence on a company producing a physical product, or a fund or financial institution, a potential investor should take the opportunity to observe the ins and outs of how the business is run and how well processes are followed. During all of the meetings and visits throughout the on-site due diligence, keeping an eye out for staff members putting policies into practice; verifying that behavior aligns with previously reviewed handbooks or manuals is advisable. The bottom-line is that during the on-site visit you want to ensure, to the greatest degree possible, that what they say is what they do!

Similar to the size of the data request for desktop diligence, the amount of time an investor spends performing on-site diligence should vary depending on the size and type of investment under consideration. An afternoon spent discussing repayment capacity and cash flows with the most senior members of the management team could be sufficient for a relatively small or short-term debt investment. On the other hand, an investor contemplating a major equity stake in a company is likely to spend days, possibly over the course of multiple visits, performing on-site diligence. During that time, an investor should make it a point to sit down and meet with each member of the senior management team and each department head on a one-on-one basis. If possible, it is helpful to send a request to the management team in advance of your visit and schedule each meeting. An investor may refer to the organizational chart to determine the list of people who are most important to meet. This list will vary widely depending on the type of company or fund under consideration. As an example, an investor performing diligence on a microfinance institution might ask for the following meetings:

- Chief Executive Officer
- Chief Financial Officer
- Chief Operations Officer
- Head of Risk Department
- Head of Credit Department
- Head of Treasury
- Head of Internal Audit
- Head of Human Resources
- Head of MIS/IT
- Head of Marketing

A well-prepared investor will have a set of questions unique to each of these business heads that relate directly to the function

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of their departments. Some standard questions that an investor could ask in each interview include:

1. What are some of the key initiatives your department has undertaken in the past 12–18 months?
2. How do you measure success for yourself and your team?
3. What do you view as the three major risks facing your department and the company overall?

While *what* the interviewees say during the interviews is important, *how* they say it can be equally enlightening to a potential investor. Take note of body language during the meeting for clues that an interviewee is holding something back or avoiding an uncomfortable topic. Is the interviewee maintaining good eye contact or constantly averting the investor's gaze? Does the interviewee have their arms crossed in a defensive position? Excessive fidgeting could also indicate nervousness. Also take note of how the team interacts as a group. Do they joke? Is there a comfortable dynamic? It is not at all unreasonable to ask to meet individually as well as with the staff and/or operating managers as a group. A lot of information can be gleaned from these conversations regarding the quality and competency of the interviewee by observing visual clues in addition to the verbal responses.

Another important thing to observe during the interviews is the degree of faith a CEO has in his staff. If the CEO insists on being present for each of the meetings, or send in an observer, this could indicate that the CEO has micromanagement tendencies and may present key man risk, not to mention inefficiencies in running the business. In an ideal scenario, a CEO will grant an investor all of the interviews requested with complete autonomy.

Getting out of the office and "into the field" is also a key component of on-site diligence. An investor should request visits to nearby factories or outposts, as applicable for a given potential investee. This specific request will again vary depending on the type of company or fund under consideration. Going back to the microfinance institution example, an investor would want to go to one or two of the branches for a tour and additional interviews. During the tour, an investor would look to see how the branch is organized, how the tellers interact with customers, how secure the

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vault is and so on. In terms of meetings, an investor would ideally sit down with:

- branch manager,
- loan officer, and
- teller/cashier

An investor in this scenario should also review loan files at random and request the loan officer walk through the process involved in assessing the credit worthiness of a given client. Through desktop diligence, an investor should have gained a thorough understanding of the lending policy that will come in handy to compare written policies with those actually applied by the loan officer in a specific case. Take note of any discrepancies observed during the review. In this case, the final step of this “in the field” example is to meet with actual clients of the microfinance institutions. During this visit, an investor will have the opportunity to assess the level of client satisfaction and the relationship between the loan officer and this client. Of course, an investor should take everything the client says with a grain of salt as the loan officer is likely to only bring an investor around to meet with star clients. That said, it is possible to catch a lucky break and hear something unexpected. Once on a diligence trip in Laos, I had a client who was presented to me as being a good representative of the types of clients the institution served. When I asked her what purposes she put her loan toward, she essentially confessed to being a loan shark, on lending her loan to friends and neighbors. She was clearly not a star client and we ultimately ended up not making an investment in the microfinance institution.

Final Decision

Once the on-site diligence is complete, an investor should have sufficient materials to make a clear final decision on whether or not to make an investment. Digesting and processing all of the evidence collected and reviewed over the course of the diligence process can be overwhelming. Scorecards can be useful to help evaluate the wide array of factors that play into the final decision. While an investor should determine the specific elements to

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include in a scorecard depending on the type of investment being considered, the structure should seek to capture the risk and reward profile, both in terms of financial and impact. In order to assess potential private debt and equity fund options for inclusion on the Global Impact Ventures platform, the ImpactAssets Investments team, consisting at the time of Fran Seegull and Joann Chen, developed Quattro, a proprietary scorecard that considers all four key categories: impact risk, impact return, financial risk and financial return. The scorecard contemplates a weighted aggregate of over 80 specific criteria to help map a given fund on the below webs.

The financial return score is calculated through a combination of targeted returns, return benchmarks and historical returns. On the financial risk side, the scorecard contemplates a weighted aggregate of 35 specific criteria across six key categories. Impact return considers the impact generated within the firm such as staff diversity and the impact generated through the firm's investment practices and portfolio. The scorecard aggregates 11 criteria across three categories for a weighted total impact return score. Impact risk is also a weighted score and includes 13 criteria across three categories.

While the ImpactAssets' Quattro scorecard is unique to rating fund managers, many of the elements are relevant to developing a

Figure 7.5 Quattro Risk and Return Webs.

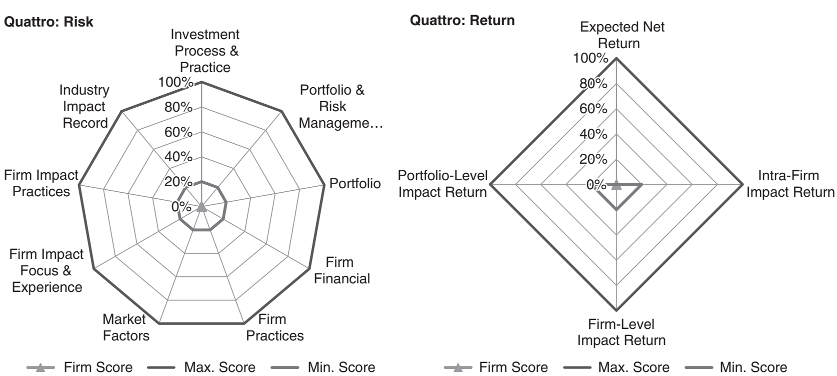

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Figure 7.6 Categories to Consider When Developing a Scorecard.

RISK	RETURN
• Firm Financial • Firm Practices • Market Factors • Firm Impact Focus & Experience • Firm Impact Practices • Industry Impact Record	• Expected Net Financial Return • Firm-level Impact Return • Intra-Firm Impact Return

scorecard for any type of potential investee. To develop your own scorecard, consider using the below general categories within risk and return and identify specific ways of measuring and weighting subcategories within. The subcategories should be specific to the potential investee's business line and market within which it operates. Combining the scored results with the overall impression gleaned during the course of the extensive due diligence process will help inform a clear final investment decision. Readers can refer to the chapter on impact metrics and measurements for additional information on how to approach measuring impact risk and return.

Conclusion

In ultimately making the decision of whether or not to make an investment, there is simply no substitute to a thorough due diligence. Rolling up one's sleeves and digging into the nitty gritty of a company is the only sure way to feel confident and comfortable in the analysis and, ultimately, the investment decision. While consulting other investors is wise and could provide important insights, nothing compares to the knowledge gained from doing the research and hard work yourself. An investor undergoing a first due diligence can use the framework laid out in this chapter as an outline and tailor it to the specifics of the type of investment under consideration. As we wrap up this chapter, we would leave you with the key tips we recommend keeping in mind when

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Figure 7.7 Key Tips to Keep in Mind during Due Diligence.

Key Tips to Keep in Mind

- ✓ Match the level of diligence with the size and type of the investment
- ✓ Use every interaction with a management team as an evaluation opportunity
- ✓ Prepare thoroughly for in-person meetings to derive the most value
- ✓ Use scorecards to process large amounts of information collected over the course of diligence
- ✓ Make a clear final decision in good confidence after a thorough due diligence

developing the due diligence process appropriate for a given potential investee:

One final word to the wise:

In general, always remember that the folks you are assessing for a possible investment are usually working hard to keep their venture moving forward while at the same time giving you the time and attention they feel you deserve as a potential investor. Be sure to respect their time and energies as you go through you due diligence process. Remember, as a general rule, it is always good to say "No" fast and "Yes" slowly. You don't want to be the person who leads an entrepreneur on well after you could have informed them that you didn't feel it to be a good fit for you and your portfolio! With the framework laid out in this chapter, tailored to suit the investment at hand, you are well prepared to perform your first due diligence with confidence and, ultimately, make a clear investment decision.

Notes

1 "The 7-Step Framework," Toniic, Accessed April 7, 2017, http://www.toniic.com/the-7-step-framework/.
2 "The 7-Step Framework," Toniic, Accessed April 7, 2017, http://www.toniic.com/the-7-step-framework/.
3 "The 7-Step Framework," Toniic, Accessed April 7, 2017, http://www.toniic.com/the-7-step-framework/.
4 The Bridgespan Group, "Seven Questions to Ask a Member of a Nonprofit Board in Your Nonprofit Due Diligence," June 26, 2012, https://www.bridgespan.org/insights/blog/give-smart/seven-questions-to-ask-a-nonprofit-board-member.

Case Study 3

IMPACT INVESTOR CASE STUDY: "LINDA SHORELY"

Year Started Impact Investing: 2010

Primary Focus: Private equity, debt and venture capital impact funds

Background: Linda is an accredited investor who seeks out professionally managed funds that do seed, early stage venture, later stage venture and private equity investments in mission-driven businesses. The impact funds that Linda invests in generally have minimums starting at $250,000. When Linda invests in impact funds through his donor advised fund (DAF), minimums start at $25,000.

Impact Trigger

Linda's background is in law and during her career she's had the opportunity to work with some of the most disruptive game changers in technology. In 2010, she began to understand that the "real deal" entrepreneurs were those moved by something other than making money. They had a bigger mission. Their satisfaction came from using their creativity and energy toward solving an identified problem as opposed to simply making money. She also started to notice the growing success of companies that are creatively solving for social and environmental challenges, whether in Clean Technology or Fintech (financial technology). It deeply

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resonated with Linda when she saw that an innovative and sustainable business model could do “financially well while doing good.” This intersection of mission and financial return had staying power. It just made sense and Linda began to revise her worldview on the meaning of money. This awareness began to reshape a vision for a future that she wanted for her family and that she wanted to participate in.

Investment Approach

Linda now believes there is no better opportunity than the present to use private capital to solve massive global problems. And she believes impact can actually be the key to finding growth and value in an increasingly crowded marketplace. It’s become clear that there is exciting and real potential with companies seeking to solve social and environmental problems. For example, there are more than 2,000 certified B Corps companies globally, redefining success in business because of having a social and environmental mission and not despite it.* Some of the fastest growing and most recognizable companies in the United States are B Corps, such as Warby Parker and Toms Footwear.

Rather than seeking individual investment deals herself, Linda prefers to work with fund managers who have the expertise, focus and passion in finding suitable portfolio bets and appropriately diversifying. There still aren’t as many fund managers with a track record of making money in the impact space. There aren’t many second- or third-time impact investing funds in the United States. But venture capital pioneers bumped into this same thing 30 years ago. As soon as she hears the old adage that “you can’t make money doing this because no one has ever made money doing this,” her interest peaks. She focuses instead on her set intentions as an impact investor and to work with funds that are demonstrating the attractiveness of investing for social and environmental impact. At times, she invests in newer or more risky funds using philanthropic capital through her DAF. Doing

* https://www.bcorporation.net/.

so allows her greater flexibility around minimums, risk and return expectations and avoids that annoying K1 reporting.

The risk aspect was a question Linda explored extensively. Are impact fund managers able to consistently deliver both market-rate returns and social or environmental benefit? Are mission-driven businesses different than non–mission-driven businesses? Are they slower growing? Are their margins less attractive? Are they more costly to invest in? Are their exits harder to find? Are their valuations lower? And just like traditional investing, Linda discovered, it all depends on what the investment is. Some investors do prioritize impact returns over financial returns, like those financing social impact bonds to support innovative public sector programs, or those investing with the economic base of the pyramid in emerging markets. And for many impact investors, including Linda, those types of investments play a role in her investment mission. Given the growing number of mission-driven companies that are proving that there doesn't have to be a trade-off, any skepticism should be rethought. There is no doubt that impact investing is an important new force in private capital investing.

Linda believes we've reached a place where most fund managers now recognize strong environmental, social and governance programs can drive real bottom-line value. But she's interested in those that go even further. They see impact as a lens that can help them spot underserved markets where others aren't looking; to work with mission-driven management teams who would otherwise be wary of private equity; and to build economic value by thinking deeply about, and measuring clearly, the social or environmental returns that move in lock-step with earnings growth.

A few examples of funds she has invested in include:

- DBL Investors, which raised over $350 million for its second fund, which invests in high-growth companies that are located in underserved communities or have strong environmental, community or workforce practices.
- Elevar Equity, which raised $78 million for its third fund, focused on commercial investments in early stage companies providing financial services, education, housing and health

care to low-income communities primarily in India and Latin America.

- Better Ventures, which recently closed a $21 million dollar fund focused on start-ups focused on closing opportunity gaps in society in everything from clean tech to health, HR and financial services focused on closing opportunity gaps in society.