

Impact Investing Redefined: Launch of the MDI Justice Bonds Initiative

Impact Investing Primer



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National Bankers
Association Foundation

Section 1:

Overview of the Types of Impact Investors





Financial Institutions

Large pools of financial resources presents an opportunity for MDIs

CRA requirements incentivizes participations with MDIs and CDFIs, in addition to mission driven endeavors

In 2022, \$151 billion in community development lending and \$299 billion in small business lending was purchased or facilitated through CRA

Capital Types:

- Racial-equity loans, term loans, syndication
- Corporate foundation lending
- Tier 1 capital: Large cash deposits to enhance liquidity

Example



Citi Collaborations with MDIs

Citi has a multi-tiered approach to working with MDIs, including up to \$50 million in equity investments, working with MDIs on project based lending opportunities and gaining access to new revenue opportunities, and providing technical and scaling assistance to improve capacity.

Example



Netflix: The 2% Solution

Netflix pledged to move 2% of its cash holdings, \$100 million in 2020, to black owned banks and institutions through deposits or investments.

This includes commitments to OneUnited Bank, LISC's Black Economic Development Fund, the Change Company, and Calvert's Community Investment Note.

Corporates



Size of financial resources presents an opportunity for MDIs

US companies have an estimated \$5.8 trillion in cash reserves as of 2022

Equity-driven capacity building to complement capital injection that includes education and mentoring

Capital Types:

- Racial-equity loans, term loans, syndication
- Corporate foundation lending
- Tier 1 capital: Large cash deposits to enhance liquidity



Foundations

Charitable organizations (501(c)(3)) established by an individual, family, or corporation

Total Assets of US Foundations: \$1.5 Trillion (2024)

5% minimum annual disbursement (est. \$75Bn), through grants or PRI, requirements to maintain charitable status

Philanthropic priorities, award cycles, and investment/grant sizes will vary depending on each organization

Possible Investment Types:

- Program Related Investments (PRI)
- Mission Related Investments (MRI)
- Grants

Example

MacArthur
Foundation

MacArthur - \$22.5 million in PRI and \$16.5 million in grants to Self-Help from 1988 to 2018

MacArthur has helped the NC based MDI and CDFI:

- acquire struggling branches of other MDIs,
- create affordable housing mortgage products, and
- provide financial and technical assistance to their communities

Example



Impact Assets DAF platform:

A donor-advised investment platform, specifically dedicated to private impact investments and grants. Impact Assets provide recommendations for vetted grants, debt, and equity funds.

Note: little information about investments and size are publicly available.

Donor Advised Funds (DAFs)



Non-profit funds of donated assets that allows individuals to emulate a foundation without an annual disbursement requirement

Philanthropic donation of assets or funds at the advice of the individual donors

Many DAF platforms partner with specialized advisors to source impact investing opportunities

Total Assets of US DAFs: \$228.9 Bn (2022)

DAF types of Investments

- Impact investments - similar to a foundations PRI instruments
- Grants



Impact Investing Funds

Manage 3rd party investment capital to deliver both financial returns and social/environmental Impact

Estimated AuM of US Impact Funds: \$271.3 Bn (2022)

Pools funds and invests into a portfolio of assets

Frequently works with investees to provide technical assistance or other services

Depending on the investment strategy of the fund, capital can have multiple objectives:

- Catalytic or gap financing
- Can be below market rate and/or longer-term

Example



West Potomac Capital WPC
Impact\$ Cash Investments

A joint project between West Potomac Capital and Ampersand to provide investment and operational cash management services to depositors in the MDI industry

Section 2:

Overview of the types of Impact investment instruments



Program Related Investments (PRIs)

- PRIs are considered similarly to grants for regulatory purposes and counts toward the 5% minimum distribution requirement of foundations
- Range of returns must be below market rate to qualify
 - Typically between 0-3%
- Generally in the form of:
 - Deposits
 - Low-Interest Loans
 - Equity Investments
 - Loan Guarantees
- 3 criteria from treasury regulations
 - Primary purpose is to accomplish a charitable purpose
 - No significant purpose is the production of income
 - No purpose is for political lobbying
- No term restrictions, typically longer term than market rate capital
- Examples:
 - Low interest loans to low-income students
 - High-risk investments in nonprofit LMI housing projects

Mission Related Investments (MRIs)

- An MRI is an investment that is made by a foundation with an **intention to create impact while also achieving a financial return** that is above the PRI level
- No legal definition for MRI - does **not** count toward a foundation's 5% disbursement requirements
- Generally made in the form of
 - Loans
 - Equity Investments
- Can also be more diversified, including subordinated loans, revolving funds, and purchasing of securitized loans
- No term restrictions
- Example:
 - Market rate investment into an affordable housing fund

Grants

- Any investment made by a foundation with **no expected financial return**
- Defined as a financial donation given to an organization that may or may not require repayment - does count toward the 5% distribution requirements
- Generally in the form of:
 - Interest Free Loans
 - Non-Recoverable Financial Donations
- Typically have generous or no term restrictions, can be restricted or unrestricted
- Barriers: Can have onerous reporting requirements, which add a burden to beneficiaries and entail additional operational costs
- Examples:
 - Interest free loans to update the technology infrastructure of a bank and expand capacity
 - In-kind donations of time through no-charge technical assistance or services

Section 3:

Impact Investments in the MDI sector



Investments into MDIs

Equity Investments

Patient, non-dilutive shares either common or preferred

Impact Deposits

Long-term, sticky deposits at below market rate

Subordinated Debt

For expanding lending operations or improving capacity

Emerging Opportunity:

MDI Justice Bonds

A potential financial instrument that aims to bridge investors and communities to advance justice and foster collaboration between MDIs Foundations and impact investors

Partnership opportunities w/ Impact Investing sector

Loan Portfolio Securitization

Purchase or facilitate the purchase of MDI loans, improving liquidity

Co-Lending Facility

Participation in MDI lending activities, via other lenders, to scale lending for underserved borrowers

Section 4:

Preliminary Feedback from Impact Investors



Impact Investor Feedback

1

Importance of place based investments

Investors recommend that MDI leverage their local/regional connections to promote investments for foundations (e.g. local community foundations) that benefit local communities.

2

Focus on impact metrics

Investors recommend that MDI leverage their local/regional connections to promote investments for foundations (e.g. local community foundations) that benefit local communities.

3

Pooling assets to achieve the requisite scale for institutional investors

Investors recommend that MDI leverage their local/regional connections to promote investments for foundations (e.g. local community foundations) that benefit local communities.

Impact Investor Feedback

4

Leveraging partnerships to reach scale, especially in regard to climate aligned lending

Investors would be more aligned to participate in a co-lending facility in the green financing space if there is the presence of a sectoral specialist, like a green bank.

5

De-risk deposits to facilitate investments from Impact Investors

MDIs should aim to leverage deposit sharing platforms (ex:IntraFi) to increase the coverage of FDIC insurance on deposits and de-risk one of the main concerns highlighted by investors

6

Demonstrate additionality

Some impact investors may prefer investing equity into MDI rather than deposits to show that their capital is leveraging additional resources. MDIs should explore options to demonstrate how impact capital is leading to scale and impact on the ground (See impact metrics)

Impact Investor Feedback

7

Core output and outcome metrics

Current metrics reflect a fragmented MDI sector and lacks focus on mission. The creation of a core set of metrics can communicate performance differentiators among banks.

Creating a collaborative process among member MDIs to develop measurable outcomes to unlock/expedite investment capital, e.g., facilitate a secondary market for commercial loans

8

Define the MDI's mission and social objectives

Investors want to see greater clarity from MDIs on:

- what is their mission
- Who are their target beneficiaries
- What tools are used to reach communities and
- How success is defined

Section 5:

Recommendations & Next Steps



Interim Recommendations

Creating an impact framework for the MDI sector

The NBAF's goal is for impact investors scale their investment activities in the MDI sector, this will ultimately result in MDIs having to report on impact metrics to these investors. Creating an industry wide impact framework, specifically tailored to the MDI space, should therefore be a priority.

Packaging due diligence materials to facilitate impact investments

To facilitate impact investments for MDIs, the NBAF could look to create a standardized due diligence package/check list whereby MDIs would have a starting point to prepare in advance of engaging with impact investors. Being prepared, and knowing what impact investors would look for, would provide MDIs with a leg up in respect to engaging with impact investors

Generating and distribution standardized documentation

Similarly to the point above, in the aim to facilitate investments into the MDI space the NBAF could lead out on creating standardized term sheets and documentation to provide MDIs with a strong starting point when negotiating with impact investors.

Next Steps

Create a community of practice for MDI green lending

Such a group would promote knowledge transfer from MDIs with experience in green lending and lead to generating pipeline opportunities for loan participations.

Organize regional networking opportunities to promote connection between local/regional impact investors and MDIs

One of the primary takeaways from our interviews with both MDIs and Impact investors is the lack of knowledge of their respective sectors with few connection points (primarily focusing on larger MDI institutions). As such, creating such connections, particularly for smaller community foundations and small MDIs, should be a priority.

Eliminate barriers for investments in MDIs

Reducing the reporting and application requirements for funding, and investing in improvements to MDI capacity and technology, will enable MDIs to access capital sources more efficiently and allow them to expand their community lending operations

Participate in the study:

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If you would like to share your thoughts and insight on how impact capital can scale and strengthen the MDI sector please reach out and get in touch!

