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Targeting your impact investing to benefit your local community could be a good way to deliver visible change



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nvestors face a challenge when trying to apply their sustainable consumer behaviors to their portfolios. Living small – which manifests itself in a number of behaviors and under many labels – basically means shrinking your environmental and societal footprint from a consumption point of view and can also involve localizing and increasing your leverage in terms of positive impact.

The 'eat local' movement is a good example of that. By eating local you encourage and support the farms, delivery companies, stores, kitchens and restaurants in your community, while simultaneously shrinking the carbon footprint of your dinner because the ingredients do not have to travel hundreds or even thousands of miles to your plate, probably wrapped in masses of cardboard and plastic. There is also the notion that staying local keeps you in closer touch with what you put in your body, improving your mindfulness and overall wellbeing. Healthier, more sustainable food leads to a healthier, more sustainable life.

So the question is this: How can investors consume financial services in the same way? Can you invest small? From a traditional asset allocation point of view, that would mean focusing on small allocations, small companies or small countries. Where I am going with this though is what I would describe as 'small-batch capitalism.' There are strategies and financial instruments out there that focus on small, local efforts to put capital to work in a way that has the potential for positive returns and positive impact.

LOCAL HEROES

Community Development Financial Institutions (CDFIs) make it possible to project the

traditional tools of capital formation and economic opportunity into low-income communities that are historically underbanked. CDFIs include loan funds, venture capital funds, credit unions and development banks. For investors who are looking to invest locally, CDFIs offer a number of vehicles including fairly traditional fixed income investments, certificates of deposit and time deposits that pay market yields at a variety of durations – all with the added yield of social impact in the communities where that capital is put to work. From a safety point of view, because CDFIs are local and because positive outcomes are core to their mission, you can make a case that their lending portfolios are robustly underwritten, even when you account for the myriad economic challenges that borrowers face.

The Community Reinvestment Act (CRA) is another engine for the hyperlocal deployment of capital through traditional investment structures. Banks that are insured under the Federal Deposit Insurance Corporation are compelled to extend loans into low- and middle-income communities to provide equivalent economic opportunities to everyone in their local markets. There is no legal requirement for banks to take unwarranted risk in making these loans, nor are they called upon to make unprofitable loans. As such, mortgages issued under the CRA are generally carefully underwritten – particularly following the financial crisis – and collect competitive but not usurious rates of interest. Add robust research and due diligence at the issue level, and building portfolios of these mortgages could be an intelligent way to get asset class exposure with this small-batch mentality.

HOME AND AWAY

To the extent that anyone 'automatically' thinks of an investment strategy when talking about small-batch capitalism, microfinance quickly comes to mind. CDFIs might be a platform for this type of economic empowerment when looking at the US or the UK, but when we look toward emerging and

frontier markets, microfinance institutions (MFIs) are a more realistic option. MFIs are set up to provide some institutionalization and scale to the process of extending finance to communities and individuals beyond the developed West, in what to us would be considered tiny increments. These capital injections can help to build or expand businesses, acquire inventory and equipment, or even hire employees. Not only can these MFIs function hyperlocally, but in a lot of instances they are a direct expression of the drive to empower women as the economic engines of their families and communities.

Certain types of municipal finance might also satisfy the criteria for small-batch investing. Funding a public works project to bring clean water to a community, build a school or preserve a greenway might lift up a specific community and create direct positive impact.

GETTING HANDS-ON

Most of what has been mentioned is easily accessible, even for retail investors of modest means. For gatekeepers, there are strategyoriented solutions that can bundle and diversify exposures. Community investment notes can provide thematic exposure to affordable housing, microfinance, community development projects, minority- and womenowned businesses, healthcare and the environment. These sometimes come as bonds of set durations with yields that are often more modest than traditional issues, but with a heavy orientation to localized impact. ESG-oriented SMAs and mutual funds may contain exposure to sustainable municipal finance, CRA-qualified mortgages, CDFIs and MFIs too.

Like reading the board at the local gastropub or microbrewery, a little research can go a long way toward finding these opportunities to deploy capital into small-batch investments with a local focus. Then you stand a chance of economically empowering communities while providing a compelling return on capital for clients.