Federal Reserve Bank of Chicago

Fifth Annual Summit on Regional Competitiveness

October 16, 2017

Sustainable Investing

MS. KELLY O'BRIEN: I know that that panel obviously has created a lot of good buzz. We do want to keep the panel moving forward, and I want to stay on time with the agenda. If I could ask everyone to please take their seats, we're going to start the next panel.

I appreciate that so much of today is about being able to network, and I know again that we cram so much into this. So I appreciate your energy. We do have a reception happening at the end of today, and hopefully a lot of our speakers will be there for you to continue these important questions.

But we want to get on to the next panel, and it is my pleasure to introduce Greg Hummel. Greg is one of the co-founders of the Alliance and is a partner at the law firm, Bryan Cave. Bryan Cave really provides office space and administrative support to the Alliance, and for that we are profoundly grateful. It is a wonderful place to go to work every day.

As you can imagine, I approach Greg kind of constantly with tasks and favors, and he always responds. He is very committed to making a difference. One of the best things about my job is working under such inspiring, accomplished leaders.

In his day job, Greg focuses on complex projects and transactions, including finding the gap funding necessary to make deals feasible, identifying sources of recurring revenue to anchor a project's development and ultimate operation, achieving regulatory relief, or acquiring the necessary permits to allow a project to proceed.

He's a master at driving consensus among parties to achieve critical agreements. Ladies and gentlemen, this panel, Sustaining Investing; The Evolving Landscape Of The Future, will open your eyes to making things happen that you probably aren't sure how to tackle. So with that, Greg.

MR. GREG HUMMEL: Thank you, Kelly. If we look at the last five summits and we look at the OECD report, we focused on workforce development, transportation infrastructure, water as a critical resource and opportunity for the region, innovation, and the green economy. Each one of those project areas needs capital.

What today's panel is about is how we might create a new asset class around sustainable investing. And that goes by different names. It also can be social-impact investing. I want to tell you about the three panelists because they are unusual in their approach to this subject.

Roberta Gordon, my colleague from New York, is an excellent environmental lawyer. She won a gold medal for her service to the Office of General Counsel of the U.S. EPA.

But what I want to highlight about her is that she's the president of a foundation focused on responsible and impact investment, and is a member of Investors Circle, an organization that works with innovators and entrepreneurs to scale solutions to the world's pressing challenges.

As one of Yale's distinguished alumnus, she sits on the Board of Advisors of its Initiative for Sustainable Finance and for the Yale Center of Environmental Law and Policy.

Next, we have Lyneir Richardson. He's the CEO of Chicago Trend, the social enterprise aiming to catalyze retail development to strengthen commercial corridors in urban neighborhoods. Before he had that job, he worked first at General Growth as their Vice President for Urban Redevelopment. And then he joined Cory Booker as the head of their community development arena in Newark.

Finally, Tom Middleton is the founder of Nobadeer Partners, which focuses on urban redevelopment projects. He was recently a fellow at the Advanced Institute at Harvard in 2015 and 2016. Before that, he was a partner at Blackstone. And before that, he led the communications investing group at Merrill Lynch.

Moreover, as a board member of the Innovation Lab at the University of Southern California's Annenberg School, as well as the Institute for Creative Entrepreneurship at the Berkley College of Music, Tom has worked extensively as a mentor to both graduate and undergraduate entrepreneurs. From 2009 in 2016, he was a global trustee for the Nature Conservancy.

So what distinguishes these people? They are actually acting out in their day jobs their philanthropy and trying to create an impact that helps address some of the issues that we've been struggling with over these five years at our Summit deliberations. And so to set the stage, I invite Roberta with opening remarks.

MS. ROBERTA GORDON: Thank you, Greg, for that introduction. I am so happy to be here today visiting you from New York, as Greg said, but my father was born in Michigan City, Indiana. So I do have a connection. I mean, Greg did a lot of introducing that I was going to do about myself. The issue really for me is that I have been an environmental lawyer for 30 years. And then I formed a family foundation three years ago, and now I invest in startups that are doing -- I happen to invest in the environmental area because that's what I know and that's what I care deeply about.

And so I do a lot of investing in new technologies and new ways to deal with environmental issues in the hopes that we look to the future to solve some of our problems. So these terms, responsible investing, impact investing, sustainable investing, they all are very similar terms and they really kind of translate into one goal, which is to place money in such a way as to further an individual investor’s values while also seeking a return on that investment.

And I call it investing with a conscience, and it's not really a new thing. I know somebody who was doing it 30 years ago, but then it was really like a rogue kind of thing to do. And it was not on my agenda three years ago when I started this foundation. But when the idea came up with the managers of my foundation, they said, “Do you want to invest your foundation consistently with your values?” And it was an obvious answer to me.

I had known before that there are certain industries that I had problems with investing in because I didn't like their practices or their products. But basically, through this foundation I found a systematic way to find companies that were doing the right thing in different areas. So right now even though it's a growing area, it's still like 10 to 20 percent, depending how you count it, of the $41 trillion dollars under management in the U.S., 10 percent to 20 percent that's invested in this sustainable fashion. So it has a long way to grow as a movement.

And so let's get to the fundamental questions. What is sustainable investing and who are the sustainable invested people who do this work? It's really the application of social, environmental and governance factors, which we call ESG factors into selection and management portfolio.

So these things can include such things as protections for employees, environmental protection, diversity on boards and other factors that are important in the management of a company. So sustainability can be both how it is a company is affected by these factors, such as a plant that may be subject to rising tides because it has seaside operations. And that also can be what that same plant affects in the outside world. So it could be the greenhouse gas emissions that that plant is producing.

So it’s both ways. But fundamentally, and I look around the room as I say this, it's a very individualized issue, what a sustainable investment is, because people are so diverse in their own desires and ethics and what is important to them. So what I think is important may not be important to you.

Some portfolios, for instance, are made up to cater to a particular value of a particular religious institution, while another one may be geared at energy conservation. So speaking the language of the SEC, which is often used to describe when one decides that something is important when you're looking at investments, you have to look at what is material to your individual investment decision. And so in the end, each person has to define sustainability for themselves.

Who are these investors? First of all, I will start with the future, and that's our millennials. According to 2017 survey conducted by the consulting firm Deloitte, three-quarters of the millennials believe businesses have the power to make social impact.

And also, the 2016 Economist Intelligence Unit research revealed that 93 percent think that social impact is key to their investment decisions, describing that they are blurring the boundaries between investment and philanthropy, pursuing investments that go beyond delivering a profit to having a new measurable social impact as well.

So that's the future. And if you see the graphs of these millennials, it's amazing how much growth there is just within an interest in this area. But turning to ourselves, I guess we're all around the same generation.

There are proponents of the idea that you can effect corporate change in a positive way by working on the inside, for instance, and through shareholder activism. And in my state, we have a Comptroller named Tom DiNapoli, who is an environmentalist, and he's also the trustee of a $192.4 billion dollar pension plan for the workers of New York State.

And he posits that as a fiduciary, he has a duty not to divest from petroleum because he thinks it would hurt his pensioners, and that advocacy from the inside is a good way to transform corporate behavior. But the true fact of it is that most of us don't have that kind of power, that kind of financial power to yield on the inside.

So Professors Dan Esty and Todd Cort recently published an article in the Yale Journal of Environmental Investing, and they classified sustainability investors into several categories ranging from those who are least concerned about the value of their portfolios to those seeking the highest returns.

And this is my take on those categories. I'm actually going to ask you people to think about this as I speak and raise your hands if you think you're the type of investor that I'm describing. The first is the socially responsible investor, what they call a value investor, and that's an investor who wants to exclude what they think are bad actor companies from their portfolio, regardless of the effect on their returns.

So this involves pulling a negative screen. Like somebody might say, “I don't like petroleum. I don't like cigarettes. I don’t like firearms.” And they won’t invest in those things. And those people care least about the value of their portfolio.

Would any of you think you fall in that category? Maybe? Thank you, okay. So the second category are the impact investors who may or may not care about their returns. And what they do is they think that they can use their capital, they can deploy it in order to effect positive change with companies they think are capable of doing that. And so they will look for particular kinds of companies to invest in. Does anybody do that here?

The third one are more the mainstream who perceive sustainability as becoming more salient and want to mitigate their losses by steering clear of certain industries. They are not looking at it so much as a value issue in terms of their value values. They are looking at it because they think they are not going to make money investing in those kinds of companies. Does anybody here have that view?

And then the fourth are those who bounce. I think this is most people, to be honest with you. Mainstream investors bounce their portfolios between sustainable and unsustainable investments. Frankly, they don't know what's sustainable and what's not. And so some of the companies have good bent tricks and some have bad, and I think that's most investors. I was that person until three years ago. Anybody else that person?

So there's one final category and those are the green alpha investors, and they really believe that the companies that are doing good environmental, social and governance are going to outperform the other companies. And they're not so much doing it on basis of their values, but because they think they're going to get rich investing in those kinds of companies. Anybody like that here? No one, well that's interesting, and I'll tell you why.

I'm going to present with you some of the challenges that sustainable investing movement is going through. It's going to be what I conclude with. And going back to the beginning of my presentation, when I said why aren't sustainable investment practices by mainstream investors not more widespread? There are a number of reasons for it, but the first one is a measurement problem.

If an investor wants to figure out where to devote their funds, how do they measure how well the companies are performing? The fact is there are many different methods and standards for assessing the sustainability of a company, which are not clearly or consistently articulated. So under one standard, one particular company might get a really good rating and under another standard, they get a really poor rating.

So it's very hard for the consumer to know what to do with that. Even though there's an effort underway to try to make this more consistent, there are a lot of challenges and really academic research is now focused on this issue. Another big problem is that the mainstream investment advisors are largely uneducated about sustainable investing and, in my experience and many others, often resist engaging in this area. So why are advisors not taking advantage of the available resources to become more proficient? That's one of the issues.

And lastly, there actually remains some doubt about whether sustainable practices does lead to financial outperformance, which is a very controversial issue because some studies would say, “Yes, definitely there's a correlation between good corporate practice and profitability.” But others find that's not the case.

And if you actually isolate specific factors, you can find some correlation that's supposed to like the whole, can. Let's say you take companies that actually are conserving water. Those companies are found by researchers to actually underperform. But if you look at companies that have women on the boards, diversity of women, those companies do outperform.

But people don't know whether that's because women are on the board, or because that's just good management overall. So I leave you with a question that as you map the future of this region, how does sustainable investing fit within your vision?

And this is actually a good segue to our next speaker, Lyneir Richardson, who has launched a social enterprise that's been funded by the MacArthur Foundation and Chicago Community Trust. He will speak and he will share with you his social impact strategy and how an entrepreneur is doing this, and dealing with the goal is strengthening underserved neighborhoods.

MR. LYNEIR RICHARDSON: Good afternoon. You know, I when I got out of law school, I practiced law at a firm. One of the early projects that I had to do at the bank was to do a pro bono project in neighborhoods. And it was Commercial Corridor on Austin, a small business lending organization working on revitalizing the corridor by making loans to small businesses.

It was at that moment that I really knew what I wanted to do with my career, and I subsequently found out that I really wanted not just to be a lawyer, but I want to be an entrepreneur. And I knew I didn’t want to do the -- my brother is venture capitalist. He wanted to make a hundred million dollars. For me, I just wanted to make neighborhoods better and earn a comfortable living.

So it’s odd or fortuitous to have this opportunity 25 years after I graduated from law school to lead a social enterprise that’s focused on catalyzing and transforming commercial corridors in neighborhoods. And to do it in a venture that's been funded by two very prestigious foundations that really allowed us to launch our operations to make impact investment.

I'll tell you just a little bit about our strategy and view my presentation as one side of it is people talking about why social impact investment is important and how to do it. I'm on the other side, the entrepreneur, who's looking for social impact investors to be able to actually be on the ground, doing deals, carrying out that work.

So Chicago Trend started as a really a consulting project with my co-founder, Robert Weissbourd, Bob Weissbourd, and working on our project with the MacArthur Foundation, where the foundation had a specific question. Neighborhoods are coming to us, requesting support, grant and PRI support, to get retail in their neighborhoods. Every neighborhood wants a grocery store, a sit-down restaurant.

And the foundation’s question they were pondering at the time was, how do we decide which neighborhoods? We don't want to pick the winners and losers. We don't want to put a grocery store in a neighborhood where a grocery store won't be successful or a coffee shop where we'll fail. And we don't want to use our precious grant dollars to support retail where retail will grow on its own, you know, market demand.

The question was: Where will retail strengthen neighborhoods? Where will it be impactful to neighborhoods that we care about? And this chart really is this sort of strategic retail development which is really at the core of our mission. Retail development that capitalizes on where a neighborhood is going, its trends, its history, its future that's aligned with what the market demand. And that if we brought retail amenities, it will accelerate neighborhood transformation. So our mission really is strengthen our neighborhoods by catalyzing retail development.

At the same time, the social impact objective is to understand where the retail will be successful, and then ultimately to generate capital to allow our businesses to be sustainable. We have three tools in our toolbox just broadly defined, a market data and analytics, predictive analytics really formed by an 8000-person survey. We now have conducted it twice, that shopper survey about where people shop, how they shop, where they go, how many stores they visit, how they got their income and other demographics.

And then models that stimulate sort of how retail and how neighborhoods are changing. Our real estate deal making, which is our relationships with retailers. We created something we call the Retailer Coalition of the Willing, retailers who are looking at neighborhoods and understanding opportunity, and then financing to get the right retailer at the right place at the right moment in time. It’s really incentive financing to make that happen.

Our services, just quickly, using the predictive analytics connecting the developer to a property owner, working with the retailer and developer, ultimately getting the site under control and entitled, getting the retail to actually sign a lease and commit to a transaction, using our capital, along with leveraging every other source of capital out there to get financing done, and then ultimately expediting the process to get it to the deal to the finish line.

We work with a variety of retailers. The big boxes, Target, to the local restaurant, to some of the local favorite chains, grocers, service. And our retail is broadly defined. We all have read the stories about retail apocalypse by retailers about amenities that will make neighborhoods, neighborhoods of choice where people can rationally decide to live.

There were so many neighborhoods in Chicago where over the last decade there's been depopulation, and the question is: What amenities are necessary or attractive to get folks to choose to live back in some of the neighborhoods on the south and west sides of the City, for example?

We measure our impact, I think broadly, you know, five years or 10 years down the road. Has the population increased? As I said, many of the neighborhoods have been having population decrease. Is there a diversification of income, or race, of educational level? Has crime gone down? Property values, other investment, both public and private.   Are there new businesses being formed? Both different types, you know, are the businesses that open, are they surviving?

Our investment capital, again, the MacArthur Foundation has made what they call a program-related investment to our firm, which allows us to be this sort of flexible financing source. We're putting in capital, we created this vehicle I'm calling “dequity” with Greg’s help.

It’s sort of debt that converts or has some conversion features related to equities. So it goes in as a subordinate nonrecourse loan, it’s flexible, it’s subordinate, it’s interest-only for a period of time. It has a contingent compensation portion contingent upon success. So it's like equity. If it doesn't work, it is in the nature it could be a grant, you know. But if it really works as we expect it to be, it should have a return that exceeds 10 percent, is really our goal. It’s patient up to 10 years.

Right now we're investing a million dollars per project. But what's really interesting is we formed our venture as an entity that we hope, and our projections are in four to five years, once we have about $27 to $30 million dollars invested, we will be able to be self-sustaining.

Right now, I have identified the projects and committed the capital in Chicago. And so we're now evaluating how do we continue to grow this? You know, we need a place where there's economic and political commitment around neighborhoods, an on-the-ground partner and a local CDFI who can do loan underwriting and loan administration. That typically has some period of grant funding for a year or two as we get off the ground. And then the PRI capital to actually invest in the deal.

What I tell our foundation partners all the time is our goal is, we'll be able to give you your money back to give you a return. Then you will have this long list of impact. Neighborhoods are better, more people are choosing to live there, crime reduction, and things of that sort.

So we're looking now at expansion around Chicago Metro. Right now, we've been investing just in the city of Chicago. We looked at opportunities in sort of the suburbs surrounding Chicago. We've had conversations about the Midwest region, you know, Milwaukee, St. Louis, Indiana, and folks in this room, and/or select East Coast cities where we believe are sort of like Chicago from our data and analytic work that might have the opportunity to be successful.

So that's our strategy. I wanted to just put that on the table as an organization that's out here trying to figure out in an entrepreneurial way how to change neighborhoods, how to have impact, how to deploy impact investment capital, and ultimately how to be an entrepreneur and do this as well.

So our next speaker is Tom. Tom, I want you to come up. Tom has spent 30 years, as you heard Greg say, as an investment banker, structuring impact investment, structuring infrastructure investment, and now is doing a great public/private partnership work in Tennessee.

MR. TOM MIDDLETON: Thank you. I think I've sort of come to the same place, to some degree, that Lyneir has from a very different route. I spent most of my career trying to attract capital to build companies, for-profit companies, either through IPO, early-stage financing, mezzanine financing, M&A. And I also worked a lot -- because I was in the communications business on infrastructure, so I worked a lot on public and private partnerships, both here in the States and overseas.

And what I saw as I started to get interested in the impact world was a lot of projects that I thought were being done, but were being done at a smaller scale, and how do you scale up this idea? How do you go beyond getting not-for-profits like MacArthur and Ford and Rockefeller? And all the same people that we hear about who are all doing fantastic work, but how do we start attracting, not only individual impact capital, but institutional impact capital? Because the pools of capital that are forming out there right now for these kind of investments are huge.

Whether its donor-advised funds, insurance companies' pension funds, more and more individuals who make up all those funds are checking a box that I want to have, to Roberta's point, I want to have a piece of my portfolio be for social impact. So when you aggregate all that money, think about how much money that is, even if it's only 5 or 10 percent of what people are checking off.

And they're going to keep checking that off, and they are going to check it off higher and higher. So I wanted to find a way to go sort of beyond a lot of the debate and discussion around impact investing, which has a lot to do with metrics. And how do we know what the impact is? Lyneir addressed that well.

And say, you know, at the end of the day we have to just create a project. We have to find a place where importantly we also recognize that the cities and the economic development corporations of these cities are your first and foremost, your first partner, and they are an investor. And in my case, looking at working with them to transform underutilized assets, i.e., land or buildings, as their initial investment, what they contribute to a project.

And to address, again in my case specifically, whether you're a hot city or a city that's trying to get back on its feet, affordability. And it's an issue that we've gone around and spoken to a lot of mayors, NEDCs and everybody's talking about whether or not, again, people are being pushed out through the Brooklyn effect of gentrification and displacement, or people trying to reinvigorate places like Buffalo and Rochester where I'm from, and St. Louis, which you've heard some about today; sort of reinvigorate the downtown core.

So I had done a lot of work in the music business and seen how the music business was just imploding, coming back now to some degree. And took a look at Nashville, which interestingly is a boom city, but at the same time it's a city that's losing a lot of its talent, and a lot of the people, they're moving on because it's too expensive.

And we went to the city, they have a 21-acre site, which was an abandoned Triple-A baseball field that they were going to RFP. And we put together a plan and said, "Look, here's a way to create green space and public amenities, affordable housing. We have 300 housing units, commercial retail, all around sort of a music cultural generator. And in a way that's completely financially self-sustaining. It won't cost the taxpayers one dollar for all the affordable housing and amenities." And we were awarded the RFP.

We're working now with the city on sort of the final contractors. Obviously, a lot of political negotiation going on, and some pushback. But to me, it's an opportunity to now go out to those pockets and pools that I've seen of impact capital, and so far our reception has been incredible from institutions and individuals. Bigger and bigger impact firms that want to get into this.

And I'll just shoot through, just give you at least a sense of that it's actually real. This is the site over the years, what it was, what it's going to become. A lot of emphasis on park land and open space because it was a public asset, and we wanted to make people to feel it was. And this was in a community that was a maker of music, and a poor community in Nashville. It abuts a Civil War fort, which nobody ever goes to. We're going to help renovate that.

It's got all these different uses below that you can see; education, incubation, studio, and, importantly, stuff that makes money and stuff that costs money because we have to get the model to work right, so we're not relying on tax credits and handouts from the government.

That's right near downtown Nashville. Nashville’s not a walking city yet, a big issue for them. They need more. Sort of a common denominator of all these cities, I think, is health and wellness.

When you put all this together and this is trying to connect green spaces, and this is just some renderings of a sense of what we can we can make it.

Both buildings, yes, but outside in a very vibrant, culturally diverse environment. Something that surprisingly Nashville really needs and something, as I say, I think mayors and economic development corporations throughout the country that we've talked to are very excited about.

MR. HUMMEL: Thank you, Tom. What strikes me -- I met him at Harvard when we were judging a jury of students who were studying Goose Island. And then I found out he was a musician, as I’m a musician. And then I remember stories about a development near Hyde Park where University of Chicago folks created affinities by doing music together in the community.

So there is powerful ideas at work here, and Sam, a shout out to you, it’s (inaudible), you know, the fine arts and how we bring some of this together through the stem. And you add the art piece to it, these developers that you heard are creating art, if you will, in a sense of creative development.

Roberta, you've talked about your foundation being invested in a responsible fashion. Tell us about some of your investments and why you made them?

MS. GORDON: Okay. Interestingly, my investments would span from large public companies to, as I say, the very small startups. And I'm not going to name any names of companies because I don't want to be promoting anything, but I'll just describe to you some of them.

One of them is a nonprofit financial institution that is dedicated to transforming the way that money works, and it's providing capital to more than 2000 social enterprises nationally. Now, I'm not getting market rate of return on that, but I'm getting an emotional high rate of return. So I'm invested in companies like that, even though I know I'm not getting the return.

I have a group of companies that they are funding commercial solar installations, and they have created carbon offsets of more than 1400 metric tons, annually. So my interest in climate is very, very deep and they are fulfilling that.

I have a public company, which is a global leader in sustainability policies. They are one of the Fortune 100 companies, but they stand out in all the areas. They use so much product that they have to set the stage and be leaders.

Then I have another financial services company that give billions away to people who are underserved in the financial sense and try to make it available. And then I have like a pharmaceutical that has been ranked near the top of an index for low and middle income communities, including making key drugs available for $1 per month in low income communities. And so they stand out in an industry that we normally think of as maybe not the greatest in terms of sustainability.

Now I have these little companies, one that makes an alternative insulation from cardboard because cardboard is on the rise, recycled cardboard and papers, I’m going down. I've got a company that makes alternative protein for fish feed. So instead did denuding the oceans, they take bacteria, they grow it in mothball methanol plants, and it actually results in healthier fish.

And I have several other companies like that. And that's some of the reasons -- when I talk to my investment advisor, I sort of -- let's talk about what my most impactful companies are.

And she started laughing because impact can be measured in so many ways. And so that's why I told you I have all these diverse companies.

My question for Lyneir, thank you. So Lyneir’s company is a benefit corporation under Illinois law. And it's a for-profit company, as opposed to a 501(c)(3), which is a not-for-profit. And so, I would like to understand, why it is that you formed it in that fashion?

MR. RICHARDSON: Great question. We spent a lot of time and we were intentional about evaluating how to structure the organization. At the time, this feeling that there are some business solutions -- there can be business solutions to, you know, profits. That, you know, every time you think of making a neighborhood better or having an impact, the first thought doesn't have to be, well let's form another nonprofit.

And so the question for us strategically was, could we form a venture that would have the impacts that we wanted and that ultimately could be self-sustaining with a little bit of a runway? And so the social venture or social enterprise nature of our work is there is a short period in Chicago and other cities as well, where there's some grant funding that allows you to sort of ramp up.

But that goal is if you ramp up and if your business model is right and your investment thesis proves up, that in as soon as three or four years thereafter, you won't need additional grant funding.

And that's the impact that is sustainable in the true definition of it’s enduring, it’s profitable, it's scalable. And so that's our aim with it being a for-profit organization. Again, it wasn't that we tried to create this billion-dollar entity. It was that we figure out a way to be able to fund our operations to make a living and to be unapologetic about being entrepreneurial in making a living, but also to be able to, in three or five years, not be back at the Foundation's table or doing annual galas to fund our work.

And so, Tom, you chose the hardest part. You've got multi-year, multi-phase work project. You have a project that has a very sophisticated and complicated capital stand.

MR. MIDDLETON: Yes.

MR. RICHARDSON: How do you do all of that and still look beyond it?

MR. MIDDLETON: Still make it work, right?

MR. RICHARDSON: Yes.

MR. MIDDLETON: Well, the proof will be in the pudding. It’s about $120 million, roughly right now, penciling out. And it’s probably three or four years, three major phases to do it. I think one of the biggest issues is the -- two main things that we're looking at, debating about.

One is, how much, what I would call horizontal financing, do we do? People who are investing across the whole project. To your point, people who have patient capital who want 10-year, 15-, 20-year money at a reasonable rate, which in today's world is a pretty good investment, versus people who want verticals, which is I just want to invest in affordable housing or I can only invest in affordable housing.

And we have to figure out how to mix those two things together. and those lines are blurring a little bit more and more even through the organizations. And then in terms of the phasing, the hardest thing is, what does the community want and need right away? What does the city want? What does the mayor want to be able to say? “Hey, look, I put in three hundred new affordable housing units.”

But is that the right way? Is that the right thing to build all of that first? How do you build them? That's a typical construction issue, but it's even more under the microscope now because of the public/private nature of it. And so, the city will be held to getting good stuff done quickly.

But there's no question that everybody understands that the key has to be “It's got to work.” You know, it's got to work financially. We're going to attract not-for-profit dollars, for-profit dollars at market, and the impact dollars will be kind of what I call the mezzanine in between layer, and we'll have to keep testing.

But as I said before, right now there seems to be quite a bit of flexibility because quite honestly, there's just a lot of supply, that money looking for projects. Deval Patrick just started the Bain Social Capital Fund at Bain Capital. He went out to raise $250 million and he got oversubscribed $400 million. The biggest issue that he encountered when he went out to institutions was, “You're only giving me a $25 million slice, I need more than that. I need to put more to work.”

So I’m not saying it's falling off the trees. You have to be rigorous just like for-profit deals. You have to have a deal that works. But if you can have a deal that works at scale, there's substantial capital out there.

MR. HUMMEL: Questions from the floor.

FEMALE SPEAKER: To the last point about having rigor and guidelines, I guess, for the investments. I wonder, Lyneir, do you have the latitude to make the decisions or are your funders involved in the selection process?

MR. RICHARDSON: Great question. So our funders initially were very involved in sort of setting up the parameters of what we were to invest in. We were able to structure our company in a way that the funders wouldn't be into the details of every transaction that we would select, so we could be entrepreneurial.

In fact, the entrepreneurial nature is one of the things we sold, and one of the things that they wanted, quite frankly. You know, you get to choose what's good and what’s bad, you know, once they believed in our business model.

One thing that we found strategic was we entered what we called a loan program management agreement with the local CDFI, which does loan underwriting, management administration, so it took a year off of our fundraising effort. And it really allows us to be sort of lean and mean and doing what we do best. This is just the analytic part, dealing with the retailers and understanding the entrepreneurs and the opportunities in neighborhoods.

And so we've adopted that, at least for now, as an ongoing part of our business model is that where we go, we will try to identify a CDFI that impact investors will feel comfortable in. And it's sort of a check. As long as our projects are what I call "commercially reasonable," I am not loaning money to my brother.

But if they are riskier or our analytics are leading us to investing in a business where the neighborhood is not there yet, or the projections may seem rosy, our CDFI partner, in theory, should approve that because it is not a commercially unreasonable transaction.

So we are in our pilot phase and we are going to continue to figure out how that relationship works out, but our early first $4 or $5 million of transactions, we are walking down that path without micromanagement from our investors.

MR. HUMMEL: Other questions?

MALE SPEAKER: Who has the final say, you or the CDFI?

MR. RICHARDSON: So it's interesting. In theory, the CDFI has the final, final say. But we have the say of firing the CDFI. So if there's a -- we will go back and say, "This is not working for the impact investors."

The capital is on the balance sheet of the CDFI. We earn our impact above -- you know, when I talk about the "dequity" piece, if it's performing, we earn our share of cash flow, of profit participation above it.

MALE SPEAKER: Is the CDFI regulated?

MR. RICHARDSON: The CDFI in this instance is not regulated.

MR. HUMMEL: Other questions. We have a little time left. While you are honing those, I've got a question for Tom. What are the commercial and investment banks doing to help develop and create this market?

MR. MIDDLETON: Yeah, I think surprisingly a lot less than they should be. It's actually a great entrepreneurial opportunity for people because you really need -- what's missing here to connect all these huge pools of capital to more and more projects of scale are –- it's sort of a connectivity mechanism, and there's a lot of people who are doing it to some degree. But you really need a firm that can go out and do what we used to do when you would IPO a company and say, "Here's a great idea. Here's a great group of people. How do we kind of get you ready for prime time?"

And understand what the investors want, create products around what they want, and get ready to attract larger scale capital. There is really nobody doing that. And the investment banks and the commercial banks are still putting their impact investing up on their philanthropy floors, as opposed to bringing it down to whether it's municipal or government, finance or utilities, or all the other types of industry groups that they've made tons of money, giving them across the board, products and services to, and they're not doing it here, yet.

MS. GORDON: I'd like to add to that. A lot of the big banks aren’t believers. And if you talk to one of the highest people in those banks, they don’t think that this is workable. They don’t think it is profitable.

And so mostly when these large institutions get involved, they get involved in the negative screens that I talked about before. Like, they will cater to classes of investors that don't like X, Y and Z. But they're not really engaged in proactive behavior yet.

MALE SPEAKER: So Roberta, you mentioned during your presentation that the millennials are very active as far as they want to be involved. They want to solve problems, all those things. You look at that and then you look at business startups right now, and there seems to be a disconnect. There seems to be a lot less startups now then there were even ten years ago. Are you investing in, say, recent graduates or even college students?

MS. GORDON: Almost every single investor that I'm involved in on impact investing are young people. It's amazing to me. There's one exception, he has been for a while, but all -- I see pictures from companies, at least two a month and sometimes 12 in one sitting. And I would say 90 percent of them are young.

MALE SPEAKER: How young have you got to be?

MS. GORDON: They've got to be pretty young.

MALE SPEAKER: I'm joking.

MS. GORDON: They are older than 21, okay. But that's what we see. They are often doing it and they are not getting paid. It's a labor of love and the hope that in ten years or something it will pay off. And those of us who do it are also in that vein. I mean, you know, there's something called slow money. That's what we do. We don't go in there and try to make a killing. We go in there and we want these things to succeed, and hopefully we'll make a return.

MR. MIDDLETON: I would just add, maybe quickly, Greg, to that, that I've had the good fortune of mentoring a lot of people over the years. And in the last two or three years, it's just been a rapid shift to this sort of category called "social entrepreneur" where people would have gone to tech or they might have gone to healthcare or they might have gone to a MGO.

But now this category has evolved, which is, “Hey, I can still, not only quite frankly, make a living, but make a very good living.” And I can be an entrepreneur whether it is through an app or it’s through another kind of thing. And it is an army of highly talented people coming out.

MS. GORDON: There are two things. I think that this up-and-coming generation is really scared about their future. And I think that they have to become more think out of the box in order to deal with it. And I think also it starts right here. I know with my own grown kids, you know, you teach them values. And it is up to us to teach these young people about what we need to do for the world. That’s my view.

MR. HUMMEL: Last question.

FEMALE SPEAKER: I guess I am just curious because I work in government, you know, what do you feel government’s role in the work that you’re doing is or should or could be.

MR. MIDDLETON: I think in my case it is and should be a real partnership. I mean, we are looking at these decisions together. We are looking at what needs to happen. There are really -- almost on the same vein as the last question, some very entrepreneurial, bright people in government.

We've got all these cities have new groups that are doing technology-related stuff, and I am finding I am really encouraged. I mean, there is always the issue of things taking a little bit longer in any government process. But generally, I found them to be incredibly good partners.

MS. GORDON: And I can say that people who are really smart in this area of sustainable investing, some of them at least take the position that the government must get involved in standard setting. Because there are a million standards, they are all different. You can’t understand what company is -- whether they are performing sustainably or not.

And some of these people, academics, take the position that government has to step in and try to help make this more uniform. Sometimes they say it should be governments and sometimes they say it should be stock exchanges. But the question is with reality and the current administration, is that going to happen? And when is it going to happen? And so you have to look at reality. I think states and cities have to take a lead role, too.

MR. HUMMEL: Thank you, panelists.

(END)