ACCELERATING IMPACT WITH GUARANTEES

Another tool in the impact investing toolkit
Kresge’s $350M Impact Investing Commitment

**Existing Investments:** $105M

- **2020 GOALS**
  - Accelerate progress toward Program and Foundation wide strategic objectives
  - Leverage at least $1 billion from other investors
  - Demonstrate “best in class” strategic philanthropy through the use of multiple capital tools
  - Recycle Foundation resources for future use

**To Be Committed:** $100M in cash PRIs

**Guarantees:** $120M

**MRIs:** $25M

**INCREASING CAPITAL SOURCES FOR COMMUNITIES**
- Debt, Deposits, Grants
  - 10-year loans to Community Development Financial Institutions, Development Finance Agencies and Credit Unions working in urban communities in areas of importance to one of Kresge’s Programs.

**PROGRAM RELATED INVESTMENTS**
- Debt, Equity, Guarantees, Grants
  - Investments that target a specific capital barrier in a sector relevant to a Kresge Program.

**INVESTMENT CHANNEL/ THE AMERICAN CITIES PRACTICE**
- Debt, Equity, Guarantees, Grants
  - Initiative to spur the development of mixed income communities and mixed use development in urban markets. Investments will have H.E.A.R.T elements (promote health; preserve equity for low income residents; be adaptive and resilient to climate changes; and have access to transit).

**MISSION RELATED INVESTMENTS**
- Debt, Equity
  - Market rate investments from the endowment that are focused on US urban markets and benefit low income individuals.
WHY DOESN’T CAPITAL FLOW?

- Policy barrier
- High transaction costs
- Market lacks understanding of segment/product
- Cost of capital
- Too much risk
Basic Social Investing Terminology

Social Investing Tools – Everyday Translation

Taking out a car loan

Making a down payment

Debt

Equity

Co-signing a loan

Guarantee
IMPACT INVESTING CONTINUUM

Below-Market Investments (PRIs) → Guarantees → Market-Rate Investments

Higher Risk  Lower Risk  Higher Risk
THE POWER OF THE GUARANTEE

Click [here](https://www.youtube.com/watch?v=x6kBZM7R_Cc&t=26s) to see a 2 min video from Kresge on guarantees and their role in community.
GUARANTEES (AKA CREDIT ENHANCEMENT)

• Credit enhancement is generally used to incentivize the issuance of debt or to obtain better terms for debt instruments. Through credit enhancement, the lender is provided with reassurance that the borrower will honor the obligation.

• Highly effective in crowding in other capital – typically 5x leverage

• Adventagous for foundations (and DAFs) because assets stay fully invested until losses occur in the future. When payments are made they are treated as grants.
MAKING ‘CENTS’ OF GUARANTEES – A CIO’S PERSPECTIVE

“We find ourselves in an investment environment most believe is overvalued, thus making future returns challenging. How can foundations not only continue their level of support but possibly even grow it? One word: guarantees. The balance sheet is one of the most underutilized assets foundations have to support their missions.”

Robert Manilla, Kresge Foundation, CIO
WHAT TOOL DO YOU NEED?

WHEN TO USE A GUARANTEE

- When a transaction can be de-risked so that other capital will flow
- When you want to extend charitable activity without requiring current liquidity
- Perceived risk is higher than actual risk
- When you believe the risk will diminish over time, therefore the guarantee can burn off

Arguably, a guarantee should be considered anytime there is other capital willing to make the investment (at appropriate terms) with some amount of credit protection. As a guarantor your funds to remain fully invested. In the event of future loss, guarantee payments are grants.
## EXAMPLES

<table>
<thead>
<tr>
<th>Entity</th>
<th>MHIC: Healthy Neighborhoods Equity Fund</th>
<th>California Community Foundation</th>
<th>SUN (Boston Community Capital)</th>
<th>Detroit Home Mortgage</th>
<th>Strong Families Fund</th>
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<tbody>
<tr>
<td><strong>Purpose</strong></td>
<td>Mixed Income/Mixed Use Development</td>
<td>Stand by guarantee re: DAF</td>
<td>Credit enhancement for CDFI Bond Guaranty Program</td>
<td>Single family mortgage pool in Detroit</td>
<td>Guaranty on LIHTC properties; release 3 months of Operating Deficit Reserve to establish service coordination function</td>
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<tr>
<td><strong>Structure</strong></td>
<td>Pooled guaranty that cannot be called until the end of the fund term and only after all properties have exited the fund. Guaranty sits behind a publically funded first loss reserve and GP equity</td>
<td>Guaranty to ensure that if CCF is unable to get DAF investors to meet the capital obligation of the SHLF fund Kresge will fund that obligation</td>
<td>Guaranty runs to Aura Mortgage FBO of US Treasury to pay shortfalls to Qualified Issuer if proceeds are insufficient to pay Treasury</td>
<td>Limited credit enhancement for participating banks in the event of a default. Payment on losses are limited to a per loan basis (not pooled) and only in cases of hardship and upon sale of the asset.</td>
<td>Guaranty available to syndicator who can apply it to individual properties. Guaranty is not pooled but at the property level. 1 month of developer ODG must be utilized before Kresge guaranty can be called.</td>
</tr>
<tr>
<td><strong>Pros</strong></td>
<td>Length of term before guaranty can be called; partner (and public funds) at risk before Kresge</td>
<td>If there are any calls on guaranty that amount converts to a note which becomes an obligation of BCC.</td>
<td>Guaranty is called after public funds expended.</td>
<td></td>
<td>Released relatively small dollars; we have to look at every property</td>
</tr>
<tr>
<td><strong>Cons</strong></td>
<td>Uncertainty about when the stand by guaranty may be called</td>
<td></td>
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And other guarantee management practices:

- Working with Finance and auditors
- Asset management
- Projecting future loss
COMMUNITY INVESTMENT GUARANTEE FACILITY
Powerful but less utilized tool by philanthropic investors

Effective in leveraging capital

Keeps assets fully invested
• Increase amount and efficiency of community development investment by centralizing a source of credit enhancement

• Reduce complexity for Guarantors by building intermediary capacity to deploy guarantees and manage them over time

• Accelerate community investment without requiring current endowment liquidity by activating Foundation balance sheets

• Share future losses pro rata

• Seven Foundations have committed to launch the Facility: Kresge, Rockefeller, Dignity Health, Phillips Family Foundation, Gary Community Investment, Weingart Foundation, California Endowment

• First close Q3 2019
CIGF WILL MAKE GUARANTEES IN THREE SECTORS

HOUSING, CLIMATE AND SMALL BUSINESS/JOBS. THE FACILITY IS EXPECTED TO PROVIDE ENTERPRISE LEVEL GUARANTEES TO MEET THE FOLLOWING NEEDS: LIQUIDITY, CREDIT RISK PROTECTION, COLLATERAL/EQUITY SUBSTITUTION.
Community Investment Guarantee Facility – a public charity

Foundation Guarantors

Letter of Credit
Goldman Sachs, Morgan Stanley, Federal Home Loan Bank

Guaranty  Draws on Letter of Credit

Servicer(s)
Enterprise, Community Development Trust, Prudential

Small Business Lenders
Opportunity Fund
Cincinnati Port Authority
Southern Bancorp

Climate Lenders
Nature Vest
Quantified Ventures
Hammon Armstrong

Affordable Housing Lenders
LISC
NY Housing Community Dev. Corporation
Corporation for Supportive Housing

Through CIGF lenders are able to access new capital and/or finance a broader range of transactions

- Organizations in italics are examples of possible participants.

Servicer allocates guaranty capacity to lenders (aka beneficiaries). Lender underwrite projects that meet the approved uses.
A Simple Example

- The Smith Foundation makes a $5MM unfunded guaranty commitment to CIGF which equals 10% of the $50MM CIGF pool
- A lender has a $3,000,000 guarantee allocation from CIGF and experiences a $750,000 loss in Year 5

<table>
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<th>Description</th>
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<tr>
<td>Total Loss</td>
<td>($750,000)</td>
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<tr>
<td>First Loss: Lender</td>
<td>(75,000)</td>
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<tr>
<td>Second Loss: CIGF</td>
<td>($675,000)</td>
</tr>
<tr>
<td>Smith Foundation Loss</td>
<td>(67,500) : 10% of CIGF Pool</td>
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</table>
Scaling the Use of Guarantees in US Community Investing
Global Impact Investing Network
https://thegiin.org/assets/GIIN_Issue_Brief_Guarantees_final%20for%20web.pdf

Making ‘Cents’ of Guarantees: The View From a CIO
Rob Manilla, Chief Investment Officer, The Kresge Foundation
https://kresge.org/content/mission-money-markets-making-cents-guarantees-view-cio

A Needed Piece of Community Investment Infrastructure
Kimberlee Cornett, Director of Social Investment, The Kresge Foundation

Guaranteeing the Goals: Adapting Public Sector Guarantees to Unlock Blended Financing for the UN Sustainable Development Goals
Aron Betru, Chris Lee, Paul Horrocks, Milken Institute