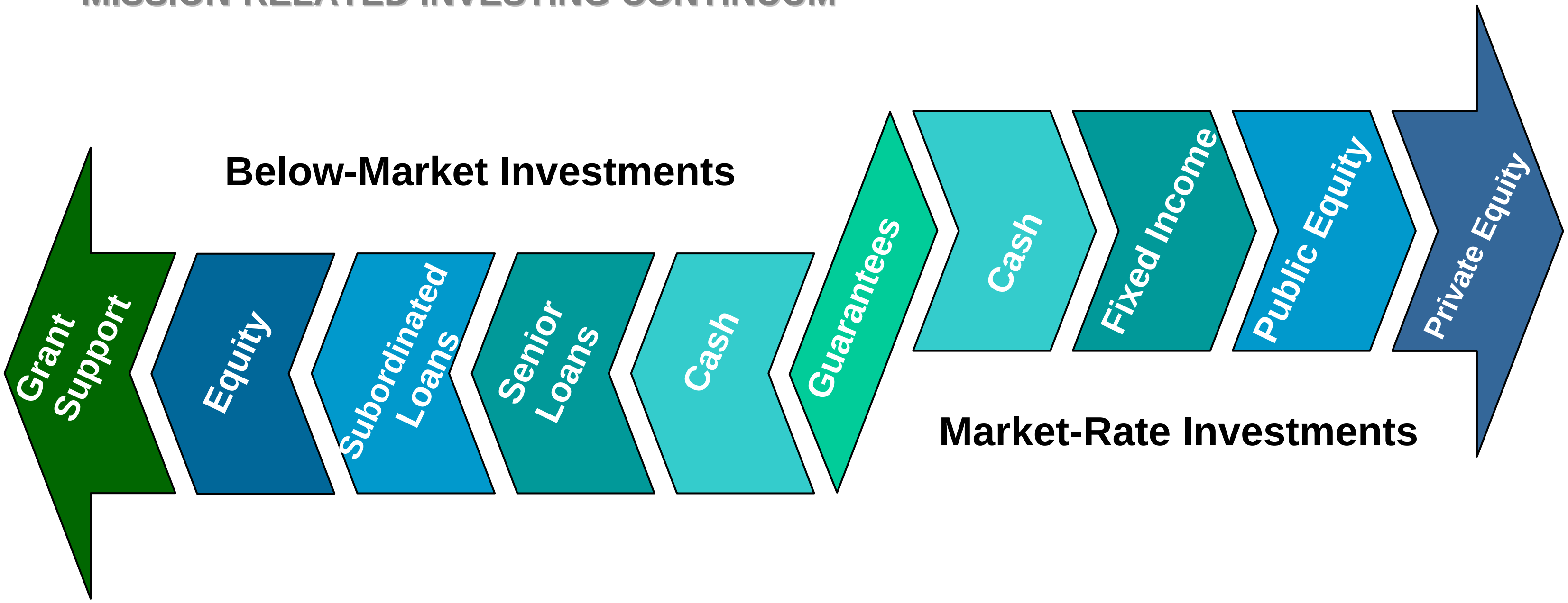
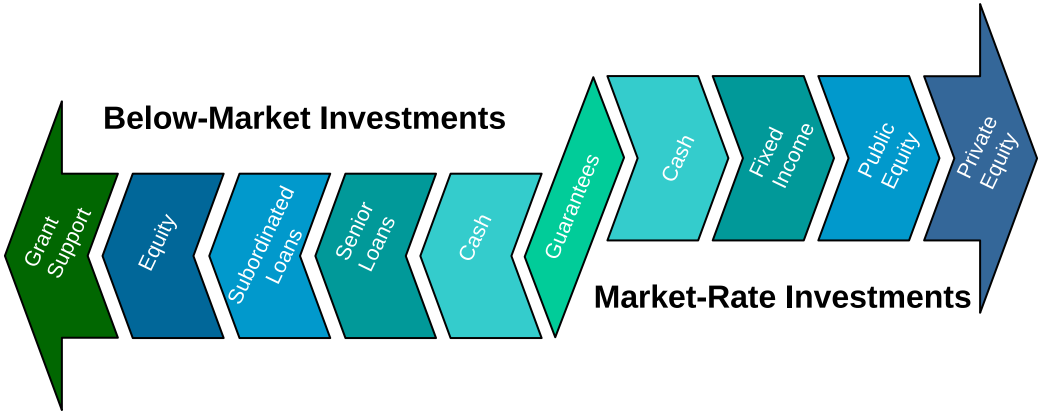
THE F.B. HERON FOUNDATION

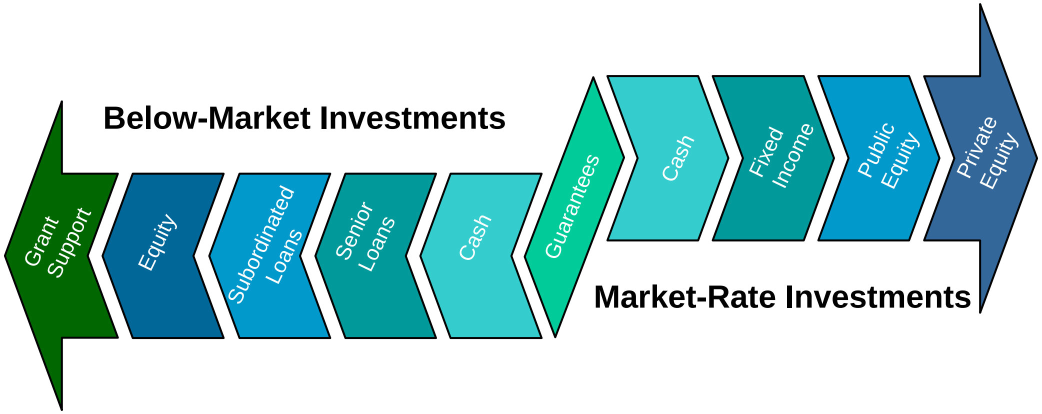
MISSION-RELATED INVESTING CONTINUUM




**"Should a private foundation be more than a private investment company that uses some of its excess cash flow for charitable purposes?"**

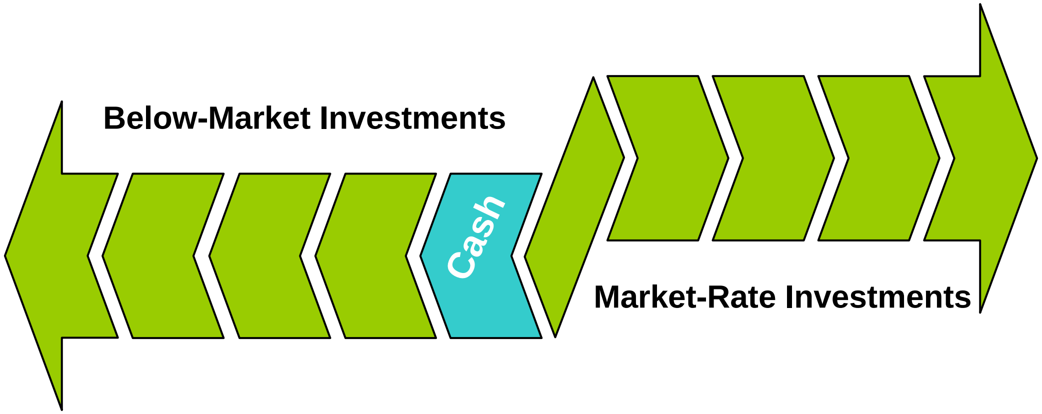



- Using assets to support mission
  - $35 billion in grants; $600 billion in assets
- Expanding the ‘Philanthropic Toolbox’
  - Grants & PRIs as part of a spectrum of tools
- Maintaining investment discipline
  - The value of incrementalism
  - Conforming with asset allocation policy
  - Use of benchmarks and prudent underwriting practices (including third-party reviews)
- Partnering with others to increase impact
  - Co-investing, joint underwriting, syndications



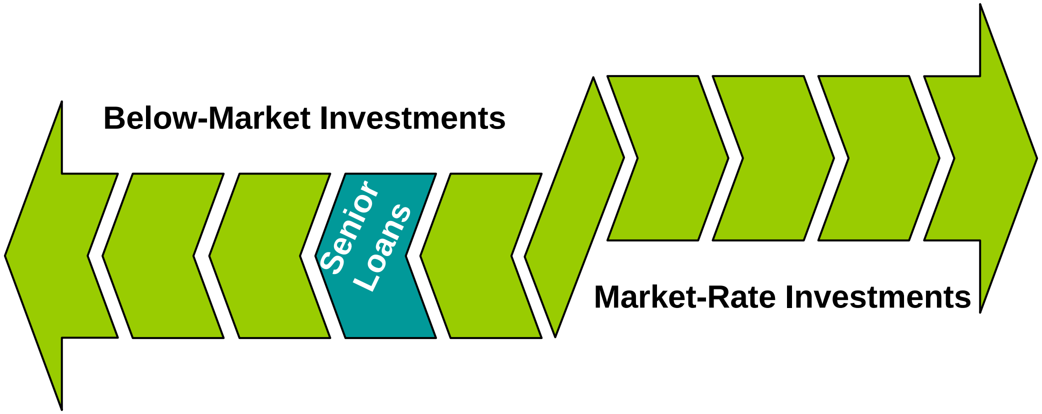

# Why make PRIs?

- Can achieve greater impact than with grants alone
- Promotes better management
- Places organizations on a more sustainable path
- Hastens convergence
- Improves a foundation’s asset management

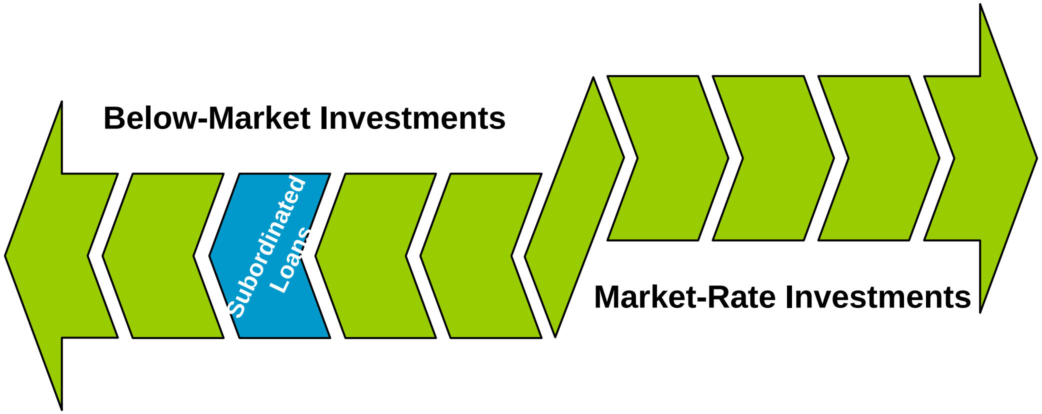



- Below-market deposits in “low-income designated” credit unions (n=1046) to increase the capacity of these member-owned institutions to provide financial services to members.

- Direct placement vs. placement through intermediaries.



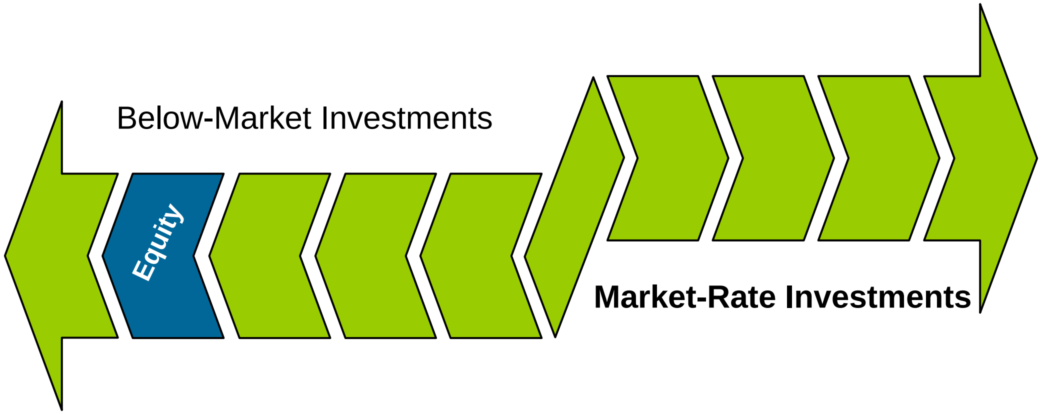

- “Typical” program-related investments made to non-profit CDFIs, CDCs or others for a term of up to 10 years at interest rates of 1% to 8%.
- PRIs support affordable housing and homeownership, enterprise development, child care and community facilities, and other strategies.
- Often “signal” other investors and lenders.




- Subordinated debt (with respect to right of repayment) may include secondary capital to a credit union, trust preferred securities to a community development bank, or so-called “equity-equivalent debt” to a CDFI.

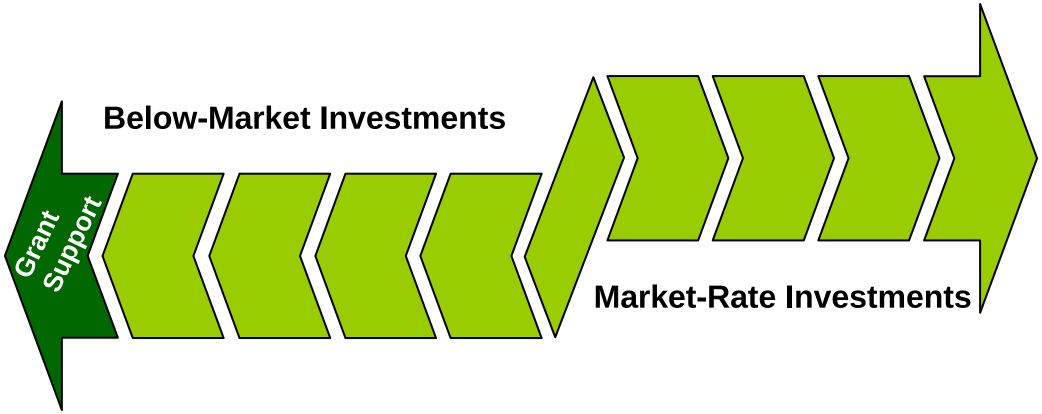
- Terms are generally longer than senior debt and pricing may be higher.

- Key rationale for subordinated debt is *leverage*.




- Includes limited partnership interests in community development venture funds (including New Market Venture Capital Companies and Rural Business Investment Companies), preferred or common stock investments in community development banks, and land purchase for conservation or other purposes.

- Often assumed (incorrectly) that equity investments cannot be PRIs. What is "charitable" and "concessionary" in the context of an investment in a for-profit?
  - Strategies to limit return

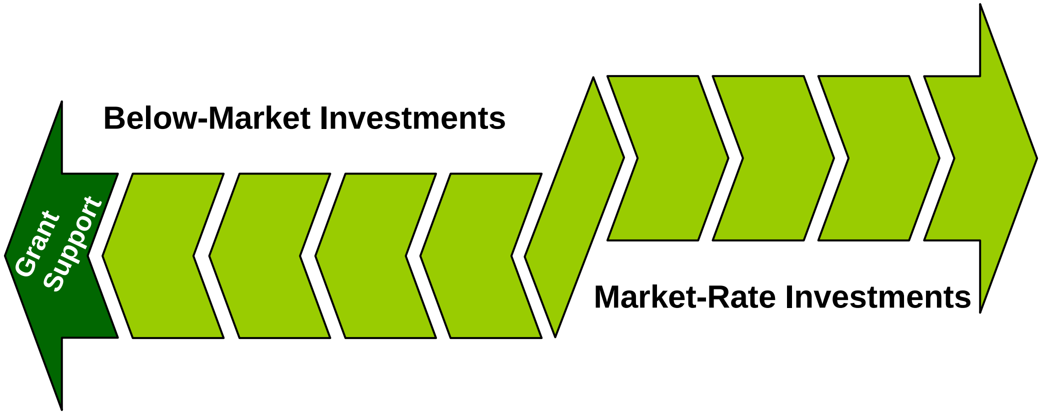



- Relationship of PRIs to grantmaking.
    - Programmatic alignment

- Differences between PRI-making and grantmaking.
    - Focus on financial capacity
    - Management & “bench strength”

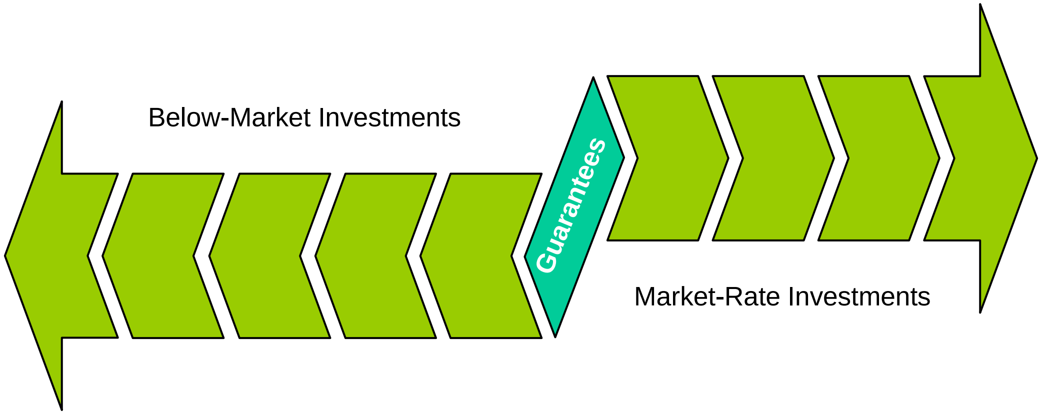
- Are PRIs always part of the “grants budget”?

- The dual character of PRIs: charitable distributions <u>and</u> asset management tool




Some key learnings from PRI-making:

- Be serious about being repaid (“moral hazard” issue)
- Invest with those you know
- Consider intermediaries versus direct investments
- Use third-party reviews to increase quality of underwriting and build capacity
- The process doesn’t end at the closing
- You don’t have to do it alone

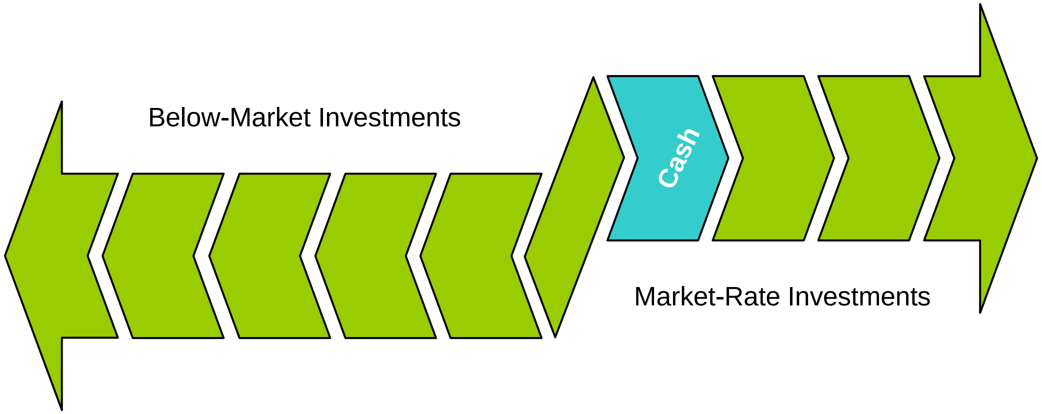



• Guarantees can enhance access to capital by lowering the actual or perceived risk of lending by conventional lenders.

• Connects groups to the larger capital markets, building networks and credit histories.

• Current IRS rules do not encourage guarantees as PRIs.  Linked deposits may be an alternative.

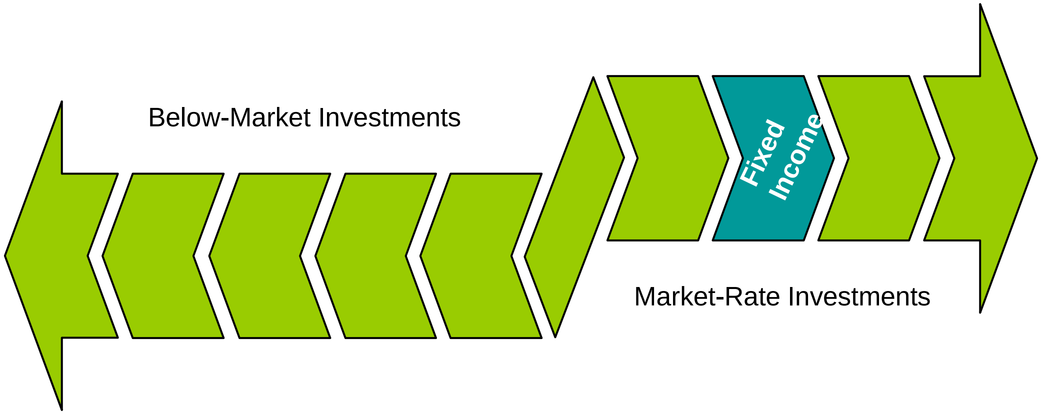
• Direct guarantee vs. Standby Letter of Credit.




• Market-rate deposits in community development credit unions and community development banks.

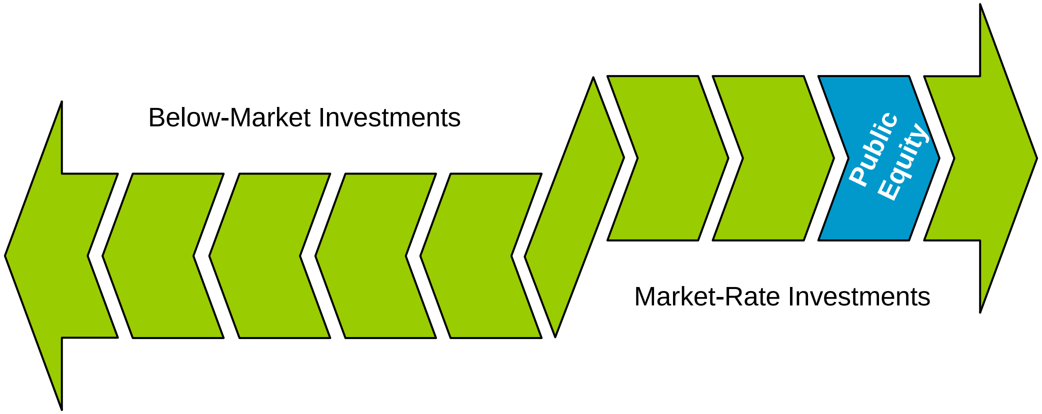
• Term: one to three years.

• Certificate of Deposit Account Registry Service (CDARS) permits insured deposits up to $50MM in certain community development banks.




• Separate bond account managed by Community Capital Management consists of fixed-income securities aligned with the Foundation's programmatic interests. Includes taxable municipal securities, targeted mortgage-backed securities, and asset-backed securities. Since inception (6/15/01) gross return is 5.92% vs. 5.69% for the Lehman Brothers Aggregate Index. R-Squared=.86.

• Mutual fund products also available and have attracted nearly $2 billion in institutional capital to date.

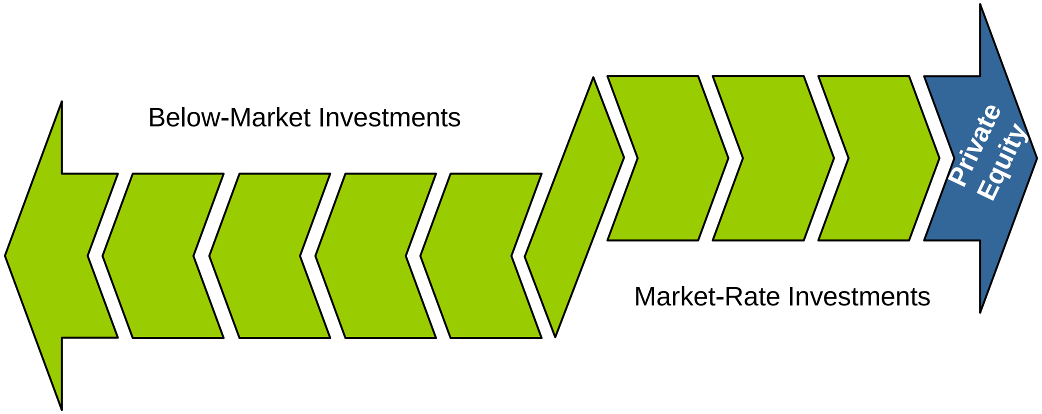



• Long history of “socially-screened” stock investments and proxy activity.  More than $2 trillion of such assets in the United States.  But how tight is the fit with mission?

• Negative vs. positive screening.

• Community investing has not been a significant screen.

•US Community Investing Index (CMTYIDX) developed in conjunction with Innovest Strategic Value Advisors to identify S&P 900 companies that outperform their peers on core community investing metrics.




• Real estate has been particularly promising (e.g., UrbanAmerica I & II, Bay Area Smart Growth, Canyon-Johnson Urban Funds I & II, Genesis Workforce Housing).

•Since 1999, there has been a significant increase in community development venture funds, as well as clean tech and so-called “green funds” and those that target women- and minority-owned businesses.  Key differentiators:  size, management and market-rate returns.

•Importance of due diligence on social benefits as well as financial performance.