Thought Leadership

Beyond giving

New ways to channel philanthropic funding that drive increased investment into the Sustainable Development Goals

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Authors:
Nalini Tarakeshwar
Karin Tang

Editor:
Richard Morrow

Reviewers:
Maya Ziswiler
Mike Ryan
Grégorie Muhr
William Nicole
Jackie Bauer

Project Management:
Jackie Bauer

Executive Summary

Philanthropic efforts have long helped to alleviate poverty and direct funds into areas that are left behind by profit-oriented forms of investment. However, philanthropic capital is also well placed to play a unique and potentially vital role as the world looks to adapt its output-focused economy to become more sustainable, evolving to the impact economy.

Mounting concerns about climate change, biodiversity loss and social inequity are putting pressure on countries to shift their economic focus from solely looking at maximizing production levels to also considering the inherent value of natural capital, biodiversity, and the ecological health of the planet. This requires a shift to the impact economy, which would place quantifiable values on natural resources and social equality.

Philanthropy can play an important role in this adjustment. Funds used for philanthropic purposes are, by definition, not concerned about investment returns, but their capital is carefully monitored for real-world value, or impact. These funds can be utilized with the larger pool of profit-oriented private capital to support the many investment projects that are urgently required to combat climate change and biodiversity loss.

The idea would be to combine public finance, philanthropic capital, and private capital in varying forms of blended finance. The philanthropic element would be integral to this, as it can act as a catalyst to support relatively risky projects and help to ensure funds are employed effectively so as to maximize impact.

For example, philanthropic capital can potentially work with public or multilateral funds to act as first-loss absorbers when it comes to financing emerging technologies or to support investments into infrastructure projects in emerging countries. This blended finance approach should help to persuade major asset owners such as pension funds, sovereign wealth funds and major asset management companies to use some of their investment capital to support these projects.

1. From philanthropy to impact

At a glance

- The rise of the impact economy brings an opportunity for philanthropy to do more with its resources and to have greater impact.
- In doing so, philanthropy can help demonstrate the viability of the impact economy and create the conditions for it to flourish.

In our May 2023 paper, The Rise of the Impact Economy[1], we highlighted the need for the world economy to shift away from a sole focus on one-dimensional output measures such as gross domestic product and toward a broader set of socioeconomic outcomes and impacts that would enable people and planet to thrive, simultaneously and sustainably, long into the future.

> "An impact economy is one that balances people, profit and planet, and it understands the interconnection between them." Fiona Reynolds, CEO of Conexus Financial, speaking to Monocle's Bulletin with UBS

The paper introduced the potential of philanthropy to catalyze investment into impact by brokering social investments such as those that use blended finance approaches. In this follow-on analysis, we delve deeper into how philanthropy can support the rise of the impact economy. It is an opportunity that is already crystallizing as societal norms, financial innovation, data revolutions and strategic alliances align to support more impactful philanthropy, in service of a fairer economic system.

The promise of philanthropy for the impact economy of tomorrow

Global philanthropy today stands at about USD 1.2 trillion, but it is expected to grow tenfold over the next 20 years to reach nearly USD 12 trillion. As the scale of philanthropy continues to grow, so does its scope. Increasingly, philanthropists focus less on "how much" has been spent (which tells us nothing about the outcomes and impact philanthropy generates for people and planet) than "how" funds are spent, and whether they are being allocated equitably and sustainably.

One way that philanthropists can have a bigger impact is by putting funds to work through social investments that combine philanthropic with other forms of capital. Philanthropic capital can bridge the gap between public finance that targets the common good and private finance that targets individual returns. Used thoughtfully, it can be flexible and nimble, responding quickly to needs as

[1] https://www.ubs.com/impact-economy

they arise; or it can support long-term results that are more systemic[2] and more sustainable. Philanthropic capital can take greater risks without requiring higher returns.

This approach fits neatly in an impact economy, where the lines begin to blur between private finance, impact investing and philanthropy, and where silos between different forms of capital—public and private, catalytic, and commercial—start to blur.

This provides an unprecedented opportunity for philanthropy to do more: to play an essential role, alongside governments, businesses, and the financial sector, in demonstrating the viability of the impact economy and creating the conditions for it to flourish.

[2] A systemic change is a modification to how a system works, and what happens as a result. It should be sustainable, scalable and resilient. See DCED (2021) 'Assessing Systemic Change. Implementation Guidelines for the DCED Standard'

2. Recognizing what matters

At a glance

- Philanthropy and the impact economy share an understanding of "value" which recognizes the importance of natural, social, and human capital, and not just produced capital.
- Value is vested in the impacts and outcomes—the real-world change—that economic activities generate, and not just the outputs.

Impact economics resets our approach to economic thinking by broadening our mindset as to what we value and how we measure that value. First, it redefines "value" to encompass assets such as natural, social, and human capital, in addition to produced capital. That value, once known, can then be accounted for in financial markets, enabling investment that is based on "impact-adjusted" returns.

The carbon markets have demonstrated, albeit imperfectly, how an intangible good (the absence of or reduction in carbon emissions) can be priced and traded in order to bring about a positive result, namely less CO2 in the atmosphere. Such models can deliver other positive results, including financial and non-financial benefits for communities whose activities, such as protecting mangroves, contribute to the reduction of carbon emissions. Similarly, "outcomes-based" contracts reward providers for delivering social and environmental outcomes. For example, a development impact bond (DIB) such as the Quality Education India DIB, charges a lower interest rate if borrowers achieve above-target results—in this case increased levels of learning among primary school children in India.

As natural, social, and human capital become more integrated in financial markets, the social and environmental agenda of philanthropy will become increasingly aligned with that of the main economy. Second, the impact economy considers all the impacts and outcomes of economic activities when calculating their value, rather than focusing on their outputs alone (box 1). For example, an education program designed to address child labor in coffee plantations may have the output of training a set of teachers; but its full value lies in medium-term outcomes such as improvements in literacy skills, and in long-term impact such as a measurable reduction in child labor. These achievements may take several years to materialize, but they hold considerable value for any society.

Box 1: Outputs, outcomes, and impact—what's the difference?

The Organisation for Economic Co-operation and Development (OECD) defines the results of development interventions as follows:

- **Outputs:** The products, capital goods, and services which result from development interventions.
- **Outcomes:** The likely or achieved short-term and medium-term change and effects of intervention outputs.
- **Impact:** Positive and negative, primary, and secondary, long-term effects produced by development interventions.

Third, the impact economy depends on the ability to be able to measure and verify impacts and outcomes, and this aligns well with the evolution of development assistance. For more than three decades the global development agenda has increasingly sought to establish the principle that development assistance should do more than just give money to good causes, and that this money should demonstrably help to create the outcomes and impacts that funders, sovereign governments, and communities want to see.

This trend was crystallized in 2005 with the Paris Declaration on Aid Effectiveness and then further reinforced in 2011 by the Global Partnership for Effective Development Cooperation, which had been established in Busan, South Korea. These agreements are designed to enhance the effectiveness of development cooperation and they have been reflected in the evolving agendas of foundations and organizations such as the Center for Effective Philanthropy.

The focus on outcomes has been equally important for private philanthropy. As philanthropic funding for social and environmental causes has grown, so has research and advice on "good donorship" that ensures funding delivers genuine change[3].

[3] https://pacscenter.stanford.edu/research/effective-philanthropy-learning-initiative/

3. Data for transparent impact

At a glance

- Harmonized standards and benchmarks for measurement of impact are the bedrock on which a mature impact economy rests.
- Impact evaluation to assess the change—the impacts and outcomes—of funded interventions has transformative power to shine a light on what works.
- Philanthropy brings a long track record of monitoring and evaluation to support the task of developing robust standards and benchmarks that could be game-changing.

The full introduction of the impact economy will take time. As of today, there is no general agreement about how to value impact in a way that allows for meaningful comparisons between various social and environmental impacts. The impact economy can only be realized by creating credible standards for what to measure and how to measure it, how to judge what level of impact is "good enough", and, finally, equitable methods to value these impacts.

Philanthropy can play an important role in this process. The industry has a long track record of accounting (to donors, implementing organizations, and communities) for the results of philanthropic funding. One established best practice is that of impact evaluation, which assesses the change caused by an intervention, before and after, or over time. Impact evaluations are now routinely conducted and have contributed to a global evidence base of what works, for whom, and in which contexts. Box 2 illustrates how impact evaluation has demonstrated the effectiveness of a primary school teaching approach, helping to promote its wider adoption and replication.

The transformative power of rigorous impact evaluation was internationally recognized in 2019 when the Nobel Prize for Economics was awarded to Esther Duflo, Abhijit Banerjee, and Michael Kremer. Their innovative work demonstrated how experimental impact evaluation methods can provide reliable answers about the best ways to fight global poverty, covering topics such as health, education, agriculture, and gender.

Once they have been shown to work, social and environmental programs need to scale with public and/or private sources of funding. In place of impact evaluations, we need simpler and standardized metrics, tools, and benchmarks to indicate if a program is on track to achieve its desired impact.

The Global Impact Investment Network (GIIN) offers one example. It has developed the "IRIS+" system for measuring and managing impact based on core metric sets, which are designed to be consistent with other frameworks. Another possibility would be to create a single, composite rating for certain forms of investments which, like a bond rating, provides an at-a-glance indicator of how impactful they are. This is important if philanthropists and investors are to continue to invest in these programs.

Box 2: The role of impact evaluation in knowing what works: Teaching at the Right Level

Traditionally, school children are grouped based on age. Indian NGO Pratham, however, aims to build foundational reading and math skills by grouping primary school children based on learning levels instead, using an approach called Teaching at the Right Level (TaRL).

The approach assesses children's learning levels using a simple tool and works with each group using a range of engaging teaching and learning activities. It focuses on foundational skills rather than solely on the curriculum, and tracks children's progress.

Rigorous impact evaluations across several countries have proven TaRL to be highly cost-effective in improving learning outcomes. In India, for instance, various versions of TaRL have been shown to produce large gains in numeracy and literacy. Before a 50-day supplemental school program was implemented, 39 percent of children could not recognize letters and 85 percent could not read a paragraph or story. Children who did not receive TaRL instructions made little improvement. But for children who participated in the program, assessment evidence showed 92 percent could recognize letters and 49 percent could read a paragraph or story. The evaluations also find that the method has the best results when teachers are mentored in the approach and when governments have strong ownership of the program and data on children's learning.

Based on this evidence, TaRL is considered a "smart buy" in improving learning in low- and middle-income countries. According to the Global Education Evidence Advisory Panel, public and private investment in proven approaches such as TaRL are urgently needed to address the learning loss due to COVID-19.

There are risks to overly simplifying and standardizing such measurement. Moreover, seeing philanthropic giving as a for-profit investment—philanthrocapitalism—has been criticized for the power it gives to those who have benefited from the inequities perpetuated by the global economic system. In addition, there is skepticism about the benefits of a focus on efficiency, measurement, and management for those affected by these inequities. Issues resulting from gender-based power imbalance, for example, are harder to "quantify" and will take time to change.

An impact economy with a standardized and transparent measurement and management approach provides an opportunity to build trust among all the stakeholders involved. Frameworks and metrics such as those of the Sustainable Development Goals, the Impact Management Project, and IRIS+ have contributed to a common understanding and taxonomy around impact and which metrics are to be used. What is currently missing are the standards around how to track these metrics and performance benchmarks.

The creation of a standard impact rating methodology could be game-changing in helping to bring this about, especially when complemented by an "impact marketplace" (learning from the carbon markets) where such ratings are verified by independent parties and shared with donors for investment.

4. Joining forces for greater good

At a glance

- Philanthropic partnerships provide a platform for advocating for action to achieve the objectives of the impact economy.
- They can use their influence to help facilitate new kinds of alliances, focused on addressing intractable challenges.
- And they can be a force for ensuring equal and inclusive partnerships, in which all stakeholders have voice and representation.

Philanthropic partnerships are important channels for amplifying reach and impact. They serve three important and interrelated objectives that, taken together, can help develop the institutional capacity that would be needed for a robust and fair impact economy:

1. Advocacy and influence

Philanthropists have platforms and resources that enable them to advocate for positive social and environmental change. They can work through their networks to raise awareness among diverse stakeholders, build coalitions and consensus, mobilize resources, and help change mindsets.

This provides philanthropists with a lever to help move the agenda from debate to action at a global scale, to help embed the impact economy. Amazon founder Jeff Bezos announced his Climate Pledge to reach net zero carbon emissions 10 years ahead of the 2050 Paris Agreement deadline; so far more than 400 companies have signed up to the pledge. Companies that do so have to make tangible commitments to regularly report greenhouse gas emissions, implement real business changes that eliminate carbon, and credibly offset any remaining emissions.

2. Convening diverse stakeholders around critical issues

Catalytic collaborations with partners and leaders in the impact space will be needed to bring together commitment, assets, and expertise from across different stakeholder groups to address difficult challenges more effectively and build a broad coalition around the goals of the impact economy. The philanthropic sector is key in this stakeholder universe, alongside governments, business, and civil society.

Landmark examples include the Bill & Melinda Gates Foundation which, in the late 1990s, successfully moved the topic of immunization up the global agenda and spearheaded a partnership with the World Health Organization, UNICEF, and the World Bank to establish Gavi, the Vaccine Alliance.

Today, Gavi vaccinates almost half of the world's children and has been central to the COVAX program to guarantee fair and equitable access to COVID-19 vaccines.

An impact economy will require innovative types of partnership that can unlock entrenched technical, social, or political positions and provide new ways of tackling stubborn problems. It will be important to be open to evolving types of partnership and the potential for innovation that they offer.

An example of this is Project Last Mile, which brought together the Coca-Cola Company, the Bill & Melinda Gates Foundation, USAID, and the Global Fund to Fight AIDS, Tuberculosis and Malaria to help provide access to essential medicines. This innovative, cross-sectoral partnership applies Coca-Cola's supply chain intelligence and networks to improve the functioning of medical supply chains in countries such as Mozambique, Tanzania, and Nigeria, and ensure that essential medicines get to the last mile in a sustainable and scalable way.

3. Ensuring just transitions for all

At the heart of all philanthropy are the many different communities that the funding is intended to serve. These are often communities that are marginalized economically, politically, and socially, through unequal growth, undemocratic systems and practices, or denial of their basic human rights.

A fundamental principle of impact partnerships should be to ensure communities have a voice and representation in decision-making that affects their assets and resources, their lives and livelihoods. The Agency Fund[4] is a good example of a multi-donor collaborative that was established to change the funding ecosystem and expand people's agency and self-determination; and the Child Learning and Education Facility (CLEF) illustrates how multi-sector partnerships can bring together public, private, and civil society actors, to ensure voice and representation for all stakeholders (box 3).

Box 3: Working through partnerships for scale, sustainability and effective collaboration

Children in poor households in Côte d'Ivoire are at high risk of being recruited for child labor, including in the harvesting of cocoa and coffee. There have been several projects run by different ministries within government, bilateral donors, and cocoa industry partners to improve farmer livelihoods, increase access to education, and provide poverty relief to these households.

In February 2023, the Child Learning and Education Facility was launched, a USD 77 million public-private partnership between the Government of Côte d'Ivoire, cocoa and chocolate companies and philanthropic organizations (including UBS Optimus Foundation and the Jacobs Foundation), to support access to quality education as an essential tool to promote children's rights and fight child labor in Côte d'Ivoire. This multi-stakeholder partnership works in alignment with the National Sustainable Cocoa Strategy and the Ivorian Education Sector Plan to support the scaling of evidence-based interventions, sustainability, and inclusive decision-making.

[4] https://www.agency.fund/

5. Leveraging all forms of capital

At a glance

- Philanthropic capital can be the "bridge" that enables both public and private capital to participate in the same impact-aligned investment.
- "Blended finance" refers to a range of financing arrangements that combine philanthropic, public and private risk appetites and return expectations.
- Philanthropy can provide the visionary risk tolerance that promising new ventures need.

A growing number of philanthropists consider themselves to be "investors" in social and environmental impact, seeking to stimulate a culture of risk and innovation. There are two important ways in which such philanthropic investment can support an impact economy:

1. Philanthropy can be a bridge that brings together different forms of capital in a single investment.

Successful innovations require size and scale if they are to gain traction and bring about embedded, sustainable change at a systems level. Social finance offers various mechanisms and instruments to leverage investments to achieve scale of financing as well as of impact—and it is continuously evolving to meet the needs and expectations of a variety of problems, contexts, and investors.

The ability of philanthropists to collaborate and take long-term risks is likely to prove vital to this process and their entrepreneurship can help to drive the commercialization of innovation at scale. This is particularly the case with blended finance (box 4), where philanthropic and public funding can improve the risk-return profile of projects and catalyze increased investment into blended finance transactions that offer impact and positive financial returns.

The ability to "recycle" funding is another important strategy for scaling finance. There are several mechanisms through which philanthropic funding can be recycled. For instance, outcomes-based financing can use philanthropic capital to fund the implementation of a project, and this is then reimbursed by an "outcomes payer" (usually a government or development finance institution) once the expected outcomes have been delivered and confirmed. In this way, philanthropic funding can be used many times over, multiplying its impact.

Box 4: Blended finance: using philanthropic capital to catalyze commercial capital at scale

Within the broader field of social finance, blended finance is a powerful key to "unlock" large volumes of funding for the impact economy that might not normally be invested.

It uses philanthropic and public funding—which typically has higher risk tolerance and/or lower return expectations than private investment capital—to de-risk investments sufficiently that they become "bankable" for private investors and thus attract commercial investment. Once an investment has developed a track record, enabling it to operate on commercial terms, the de-risking function of philanthropic and public funding is no longer needed.

A blended finance structure comprises different tranches of capital, with each tranche tailored to the risk and reward expectations of a different group of investors, to attract more private investment to projects.

This can work through a variety of mechanisms—individually and in combination. For instance:

- The **SDG Outcomes Initiative** is a pioneering USD 100 million blended finance initiative focused on delivering SDG-aligned outcomes, investing alongside private investors. In the blended finance structure, UBS Optimus, funded by donations from over 30 UBS clients, provides 20% first-loss capital to unlock additional impact aligned commercial capital.
- The **Swedish International Development Cooperation Agency** (Sida) uses a guarantee instrument, backed by the Swedish government, to enhance lending to promote sustainable development, inclusive economic growth and poverty reduction. By issuing a guarantee Sida can take a share of the underlying risk in order to unlock financing and investments to serve development purposes.
- The **Blue Alliance**, a network of marine protected areas in the Philippines, is financed through a USD 50 million blended finance facility which combines grants, returnable grants and different debt tranches including an impact-linked loan from the UBS Optimus Foundation.

2. Philanthropy can use its risk tolerance to support new ventures in the early stages.

New businesses responding to opportunities in the impact economy, as well as social enterprises and impact-oriented organizations, require considerable early-stage, risk-tolerant capital to establish enterprises on a stable footing. However, they face several barriers in securing finance, with access to investors being the most frequent. While venture capital can provide early-stage investment, it typically focuses on minimizing risk and maximizing return. Philanthropy, in contrast, has the potential to help meet the need for visionary funders with the patience to wait for longer-term returns and the risk appetite to put their money behind innovation and diversity at an early stage.

Initiatives such as the RS Group's Terratai are designed to meet these needs. Terratai is a "venture builder" for nature that provides resources, expertise, and early-stage investment to foster the growth of nature-based companies until they can reach scale and attract institutional capital.

Philanthropy can draw on its funding flexibility to catalyze investment and facilitate access to expertise across the development finance spectrum, from early project development to early-stage finance, to risk sharing and mitigation. It can underpin this financial support by engaging networks and convening power to mobilize actors around important challenges and issue areas, and to promote and advocate for the expansion of successful approaches.

In practical terms, this might involve:

- **Pipeline strengthening.** Identifying ventures with the greatest potential to build a pipeline of good ideas and impactful investments. This could be by awarding prizes or competitive challenge funds that focus on priority needs.
- **Keeping frontline issues in focus.** Focusing support on those actors tackling intractable, frontline issues, for example interventions in fragile states or innovation in difficult sectors facing structural obstacles to private investment. The impact economy should enable risk capital to go where the mainstream won't.
- **Building scale.** Supporting ventures with grants, patient investments, and innovative impact finance to help them scale. For example, facilitating access to investors through impact accelerators or incubators.
- **Promoting good ideas.** Celebrating ventures that emerge as leaders to provide inspiration and ideas in breakthrough areas.

6. Summing up

Philanthropy combines financial flexibility and risk appetite with resources—financial, social, and political capital—that can help foster the change needed for an impact economy to flourish. Current economic and financial trends are bringing impact to the fore, making data more and more accessible, emphasizing partnership, and opening up new forms of investment. As all these factors converge, we believe philanthropy can bring its resources, skills, and influence to bear to help:

1. change the focus from outputs to outcomes and impacts;
2. change accounting practices around how we value people, planet, and profit;
3. change mindsets to form inclusive and fair partnerships, so all voices are heard; and
4. change investment to leverage all forms of capital into impact solutions.

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The UBS Sustainability and Impact Institute was founded in 2021 to contribute to the sustainability debate, with a focus on actionable and timely contributions. The Institute is a collaborative effort with sustainability experts from across UBS's business divisions. We strive to encourage objective and fact-based debate, provide new impulses for action, and identify innovations that will help shape our collective efforts and awareness about sustainability and impact.

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