E&F CIO Corner

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BERT FEUSS, SENIOR VICE PRESIDENT, INVESTMENTS, AT THE SILICON VALLEY COMMUNITY FOUNDATION (SVCF), DISCUSSES THE STEWARDSHIP OF BILLIONS IN HIGHLY UNUSUAL GIFTED ASSETS, WHAT IT TAKES TO IMPLEMENT ASSET MANAGER DIVERSITY, AND INNOVATION FAILURE (AND SUCCESS).

Q: What is the Silicon Valley Community Foundation's investment philosophy?

FEUSS: Overall, our goal is to achieve strong, consistent performance over time, in support of grant spending from our endowment and the charitable funds established by our donors. Unlike most private foundations or college endowments, we're stewards of numerous donor-advised funds and custom portfolios with different objectives and time horizons. Within each portfolio, our philosophy is diversification—across different asset classes, strategies and geographies—and discipline, to stick to our strategic allocation and rebalance regularly. We primarily employ active managers, and we avoid making short-term tactical bets. Last and most importantly, we seek diversity of background, experience, gender, race and ethnicity in the managers we hire, in partnership with our consultant and investment committee.

Q: Do you have a target return?

FEUSS: It would depend on the objective and time horizon of the portfolio. For our endowment, the expected long-term rate of return is about 8% net of fees. The endowment returned an annualized return of 9.1% over the 10-year period ended November 2018. Our Long-Term Growth and Social Impact pools returned 8.6% and 9.5%, respectively.

Q: Can you discuss the foundation's growth? During your 11 years in an investment role there, it's grown to $13.5 billion [as of year end 2017]—the largest U.S. community foundation.

FEUSS: When I assumed responsibility for investments in 2007, total assets were $1.7 billion. The majority were in one of six commingled investment pool options for individuals, corporations and nonprofits establishing funds at SVCF. The pools are overseen by an investment committee and advised by an investment consultant. Over the past eight years, we've experienced significant growth in donor funds with a custom portfolio managed by a trusted investment advisor recommended by the donor, which is vetted and overseen by my team.

Another source of growth has been our ability to accept unusual and complex assets. I think we excel at accepting complex assets and, if necessary, holding and selling them over time. For example, large gifts of public stock sold over a number of years, thinly traded and private stock, cryptocurrencies or, most recently, air quality emission reduction credits.

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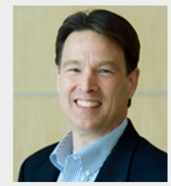
PROFILE



Bert Feuss, Senior Vice President, Investments Silicon Valley Community Foundation

- **Hometown:** I grew up in Santa Clara, California, and live in San Francisco with my wife and two sons.
- **Education:** BS, agricultural science and management, University of California, Davis; MBA, Golden Gate University.
- **Career highlights:** Spent 16 years at Franklin Templeton Investments prior to joining SVCF 14 years ago. A highlight of my career has been building capacity at the foundation and in the field for impact investments from donor-advised funds. I serve as board member, Mission Investors Exchange, and finance and investment committee volunteer, UC Davis Foundation.
- **First job:** Working Saturday mornings sweeping floors and testing television tubes at my dad's TV repair shop.
- **Hobbies:** Remote adventure travel, backpacking, hiking, kayaking, mountain biking, diving, gardening and bonsai.
- **Favorite band:** I love the Americana genre that includes everything from John Prine to all the great new talent played on WUMB-FM, a Boston blues, roots and modern folk station.
- **Last thing you read that made a strong impression?** *Reclaiming the American Dream: Proven Solutions for Creating Economic Opportunity for All* by Ben Hecht, president and CEO of Living Cities.

The tremendous growth in asset value over the last two years is partly due to cryptocurrency donated by various donors, which exploded in value during 2017 and subsequently declined during 2018. We have been steady sellers all along. As a result, we have had to learn how to hold, safeguard and trade this new asset. However, I want to stress that these donated assets are held in individual donor funds. Any gain or loss in the donated assets is isolated to the individual donor fund.

Q: What else about SVCF makes it unique among foundations?

FEUSS: We are seeing growing donor interest in impact investing as a strategy, to amplify their charitable focus and/or to align invested assets with their mission and values. This includes the use of passive ESG [environmental, social, governance] overlays, program- and mission-related investments, and recoverable grants. As a unique fee-for-service offering, we can facilitate impact investments to for-profit and nonprofit entities after conducting a thorough due diligence process. We have made numerous impact investments over a decade structured as debt, convertible debt, equity and simple agreements for future equity [SAFEs].

Q: Has the foundation looked at how the markets, fundraising and budgets work together at an enterprise level?

FEUSS: Certainly. For example, investment and spending policies must work together to support endowment payouts and maintain the purchasing power of future distributions. But keep in mind that our endowment is a very small percentage of our assets and contributes a small percentage to the overall operating budget. The majority of operating revenue comes from support fees on assets held in donor-advised funds. For budgeting purposes, we consider expected inflows from fundraising and outflows from grant distributions, and we factor in current needs. The budget impact from volatile markets is typically minor unless we're talking about the Great Recession of 2008. One challenge we and other community foundations face is that our work is largely tied to the number of grants we process, but our revenue is tied to asset value.

Q: Have you taken a view on the potential end of the business cycle?

FEUSS: We think trying to time business cycles and financial markets over the short term is not a good practice. However, we do adjust the strategic asset allocation of our investment pools every 18 to 24 months, with consideration given to where we are in a business cycle. And within certain asset classes, the committee and the consultant will have a point of view as to the opportunity set relative to other areas. Over the past few years, as the bull market has lengthened and relative valuations have changed, we have gradually reduced exposure to U.S. equity markets in favor of non-U.S. equity markets. We will review again mid-2019. Otherwise, allocations to fixed income and alternatives have stayed relatively the same, to date.

Q: What is your end-of-cycle view in the budgeting process?

FEUSS: With the current cycle being the second-longest period of expansion on record, we are cautious in our budgeting, holding expenses down and assuming flat year-over-year revenue growth.

Q: How much do you allocate to venture capital?

FEUSS: In our endowment and Long-Term Growth investment pools, we allocate a fairly modest 10% to all types of private asset funds—venture, buyout, growth equity, special-situation, credit and real assets—with the majority allocated to venture and largely through a fund-of-funds approach.

Q: The foundation has taken innovation risks. Which have worked and which haven't?

FEUSS: One area of innovation has been impact investing. We were pioneers among community foundations in facilitating direct impact investments from donor-advised funds. While most of these investments have been successful in terms of meeting financial and social return objectives, some have failed. However, some write-offs are expected when providing seed capital to new ventures with the potential to significantly improve social outcomes. One clear success was a program-related investment in the Eye Fund. This fund directly reduced the incidence of blindness in developing countries by financing the expansion of training and treatment at affordable eye care hospitals. All investors were repaid in full, with interest and on time. More recent investments include fisheries management and plant-based meat substitutes.

Another area of innovation is our Social Impact pool, which seeks a competitive rate of return along with intentional social and environmental impact. The pool has outperformed our conventional and much larger Long-Term Growth and Endowment pools over the past three, five and 10 years. We use the 17 United Nations Sustainable Development Goals to frame the social purpose of the portfolio. We're picking active public equity managers that integrate ESG factors into the investment process and also, typically, screen out "sin" stocks such as alcohol or tobacco. Some also include a corporate engagement strategy. The fixed income investments finance green bonds, microfinance, community development and housing. Private asset strategies include investments driving sustainability, health and wellness, and job creation in low-income communities.

Q: Can you describe the foundation's governance structure?

FEUSS: All investments are the responsibility of the board of directors, which delegates policy-setting and oversight of implementation to our investment committee. The investment committee has historically consisted of board members and volunteer advisors, who tend to have deeper expertise in specific asset classes or strategies. For the six investment pools, we outsource manager research and selection to Colonial Consulting. Private asset strategies require committee approval prior to commitment. Colonial is also responsible for advising the committee on policy and asset allocation strategy. For impact investments and externally managed donor-advised funds, my staff vets, hires and monitors these relationships with oversight by the investment committee.

Q: Please tell us about the foundation's work around minority-owned investment management firms.

FEUSS: Diversity and inclusion are core values and ongoing priorities across everything we do at SVCF. In 2013, we noticed that our board was diverse, our staff was diverse, our donors and grantees were diverse, but our list of 50 investment managers only had three women- or minority-owned firms. This was not acceptable, as it wasn't aligned with our values, nor did it represent the best diversity of investment ideas. So we challenged our consultant to demonstrate that it was identifying and engaging with a broad pool of talented and diverse managers, and to report three diversity metrics yearly—the number of diverse managers they met with, recommended and hired, across their client base. It took a while to get traction, but with their partnership we have increased the number of diverse investment managers from three to 15 and have increased assets deployed to these managers from $52 million in 2014 to over $200 million today.

Q: You're a leading voice in impact investing. What's going on that's exciting right now?

FEUSS: We are excited to launch a new place-based investment pool that will be a new investment option for donor-advised funds and provide a new source of capital for local investment. The new pool will serve as a revolving loan fund to nonprofits and fund managers. Unlike our other investment pools, this portfolio is not seeking a market rate of return. Instead, we are looking to fund capital gaps in areas such as affordable housing, transportation, small business lending, education and immigrant integration. A recent Urban Institute report highlighted 12 different place-based investing initiatives across the country, so while innovative, we're not the first. The fund will prioritize lending in Santa Clara and San Mateo counties, with an initial focus on housing and transportation, which are at a crisis level here in the Bay Area.

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