Interview: Jan 2011 for the following book

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PEI: ***Why is responsible investment important to you as a family office investor and how long has it been a consideration?***

Charly Kleissner: Following successful careers in Silicon Valley, my wife Lisa and I created a certain personal wealth. We felt that a combination of circumstances and talent helped us create this wealth so we wanted to do something meaningful with it, something that is value-aligned with what we perceive to be the big challenges of the planet. Lisa was the main driver originally and she encouraged our broker to look at this in 2000. At that stage, we had heard about socially responsible investing, but it was still a very new area so there was limited information. Unfortunately our investment adviser did not think it was a viable strategy and advised us against pursuing this avenue – a common response from many advisers at that time. Consequently, a year later, we changed investment advisers because we felt strongly that this was something we wanted to do. At that time, it was very difficult to find somebody who would support our agenda. We eventually found someone who worked for a boutique wealth management company and he embarked with us on defining a strategy that would ultimately put our foundation's assets into what we refer to as impact investing. The mission of the KL Felicitas Foundation, our family foundation, is two-fold: to enable social entrepreneurs and enterprises worldwide to develop and grow sustainably; and to advocate our Foundation's impact investing strategy. Our family foundation is only part of our overall wealth management strategy and we are currently moving into impact investing in all of our entities, including our family limited partnerships.

PEI: ***Did you hire this new investment adviser solely on the basis of this strategy?***

Kleissner: We decided in 2003 that we would only work with value-aligned partners. Intermediaries with a focus solely on financial return no longer fit our criteria for what we desired in an investment partner. The good news is that there are enough individuals and firms out there who really care about having a positive influence and we have the good fortune of being able to work with them.

PEI: ***Do you think your views are widely shared?***

Kleissner: The short answer is not yet. There are definitely some glimmers of hope within our peer group – high net worth individuals and entrepreneurial enterprises. We are co-founders of a global network of impact investors called Toniic. We are also participating in a couple of smaller networks in Silicon Valley – The Philanthropy Workshop West (TPWW) and the Global Philanthropy Forum. We have been presenting our successes and challenges to these small, but growing, networks and our message has resonated with our peers. We find that there is an increasing number of high net worth individuals who feel the same way we do: they do not want their capital to do damage – knowingly or unknowingly. It is not yet a groundswell, but there is definitely a realisation among our peers that sustainability from an economic, environmental and social perspective needs to be considered. We are the trailblazers and our mission is to inspire others.

PEI: ***You have talked about personal motivations, but obviously different investors have different motivations and, particularly for large institutional investors, they have a duty to maximise returns – can this actually improve returns or is it more of a charitable practice?***

Kleissner: This is definitely not a charitable practice. We believe that best market practices can result in a triple bottom line result. For us, it is about both profit and impact; and, yes, these investments can provide handsome returns. Approximately 95 percent of our investments are 'financial first' – providing competitive returns – and we reserve about 5 percent for subsidy capital, allowing us to nurture small social enterprises to the point where they can accept commercial capital. We call this 5 percent 'impact first', when the investment leads with the social and/or environmental impact and the returns may be below average market returns. We use this subsidy capital to help level the playing field, allowing more socially-focused enterprises to provide services or products which meet a need that could otherwise not be met without this capital.

PEI: ***Is there a risk when talking about 'impact first' and 'financial first' that responsible investment is seen as a charitable or philanthropic movement rather than a financial one?***

Kleissner: Yes, there is a big risk with this, particularly with the established forces that are keen to push this aside. It is not in their interest to create a new way of investing as all the incentives are aligned with the old way. I think the only way that this can change is by showing concrete examples and success stories. We are very transparent about the names and performance of the 29 investments that we have made to date, particularly regarding their successful performance during the economic downturn. We need to have more data like this because institutional capital, due to its limitations and constraints, is unable to adopt such policies until they have been proven. The way we can make a difference is by showing that the funds in which we invest have been successful – our role with our limited capital is to lead the way so that institutional capital can follow.

PEI: ***Is your approach more about screening and thematic investments rather than entering into a dialogue with companies?***

Kleissner: We do not believe that screening is the most impactful methodology for what we want to achieve. Therefore, we are taking a very proactive approach to understanding the social and/or environmental impact of all of our investments, which often requires a dialogue with the companies in which we invest. While we do not focus on thematic investments, clusters of investments have emerged in our portfolio, for example, community development, alternative and renewable energy, land conservation, and water and health. From an asset allocation standpoint, we want to invest in all relevant asset classes including alternative assets and hedge funds. It is harder to find aligned investments in these alternative asset classes and we might make a temporary trade-off until we find the appropriate investments. In the philanthropic world, many investors will only make investments that are fully aligned with their mission. We think more broadly about our mission – sustainability is not that simple, you cannot necessarily demand that the whole supply chain is fully sustainable but you can ensure that the companies or funds in which you invest are at least thinking and hopefully leading in some aspect around these challenges. We will only work with them if they are at least considering these issues.

PEI: ***Are there regional differences when considering responsible investment?***

Kleissner: Regulatory and policy environments make it very challenging depending on which country you are investing in. Regulations create huge opportunities as well as risks. India, for example, or other emerging markets provide huge potential opportunities but also have complex investment rules.

There is also a cultural difference in investor mindsets within specific geographies. I can only comment on the US, European and Indian mindsets as these are the areas we work and invest in. With respect to high net worth individuals, I believe that the US is at the forefront in thinking about impact investing, with Europe running a close second. India has a way to go but is at least beginning to have dialogue in this area.

On the institutional side, I believe it is the reverse. European institutional investors seem to have responsible investment tied into the highest level of governance structure and do not see them as an 'add-on' anymore. They seem to have realised fundamentally that it is in their interest to care about impact investments for a number of reasons. One specific reason that I heard recently from a large investment bank is that in order for them to stay competitive and attract young talent, they need to adopt responsible investment practices within their business.

PEI: ***Are there lessons that private equity can learn from listed equities?***

Kleissner: As society and economists begin to better understand the implications of externalities, there will be more demand to know what companies and funds are doing in this area. Private equity, to some extent, is integrating this thinking from the start. We choose to work with those who integrate this thinking into their products as we see this as a more sustainable long-term investment strategy. Fund managers should understand this is not just about shareholders, but also about stakeholders. In Silicon Valley, this transformation has been going on for years now – there were certain listed organisations that were huge offenders in this area and yet now, although far from perfect, they have changed their practices considerably in order to attract younger consumers who are more likely to care about these issues. Private equity can certainly learn from these types of examples.

PEI: ***What trends are going to impact the private equity world the most?***

Kleissner: The megatrends of population growth and resource scarcity are the ones that will have the most impact. We are soon going to have nine billion people globally and the scarcity of resources is becoming more apparent by the day. To pretend that a system invented 150 years ago when we had just over one billion people and seemingly unlimited resources does not need to be adapted is naïve at best. There are unfortunately still lots of people who perpetuate the myth that we can grow the economy without understanding sustainability constraints; however, there is also an increasing number of people who are working hard to understand and consider sustainability issues on all levels of society.