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Millennials' Investment Strategy Could Be a Boon for Government.

Their drive to make a meaningful impact could provide the public sector a new pool of investors.

Forty-five years ago, two novice Washington Post reporters unraveled the biggest political scandal in a generation. As depicted in the thriller All the President's Men, a shadowy informant known only as Deep Throat — 30 years later revealed to be longtime civil servant Mark Felt — kept the young Bob Woodward and Carl Bernstein in the game by instructing them to "follow the money."

Today, Deep Throat might instead say, "Follow the millennials." That's because JP Morgan estimates Americans ages 25 to 35 will invest a trillion dollars over the next five years. In the coming three decades baby boomers will turn over $30 trillion in assets to their millennial children and grandchildren, according to an Accenture-CNBC study. And that's just in the U.S.

Even more noteworthy is just how differently millennials think about investing. A survey by Standard Life Investments showed that 65 percent of millennials care more about social and environmental issues than they care about investment returns. That's compared to less than half of 35- to 44-yea--olds and less than one-third of those over 45. Given these trends, it should be no surprise that today every 1 in 5 dollars under professional management is allocated based on the principles of socially responsible investing, according to the Forum for Sustainable and Responsible Investment. "Doing well while doing good" is quickly becoming a mainstream investment strategy.

State and local finance managers have good reason to worry about this trend. Municipal bonds don't offer enticing returns compared to stocks and other investments. But perhaps more pertinent, sewers, roads and tunnels don't have the same exotic appeal as microloans to Indonesian coffee farmers. And Congress is talking openly about ending municipal bonds' cherished federal tax exemption. That last change would make infrastructure projects even more difficult to finance.

But some of the early signs show that "impact investing" is a wave that states and localities can in fact surf. Consider this example. Seattle Northwest Asset Management (SNWAM), a national leader in impact investing, maintains a "gender equity portfolio" product that's popular with its retail clients. Many impact investors want their money to support organizations that offer equal pay for equal work, family-friendly work environments and other policies designed to promote greater gender equity.

One of the bonds issued under the portfolio is from the Oregon Housing and Community Services Department (OHCS). In Oregon, 40 percent of single mothers live below the poverty level. It follows then that investments in affordable housing and other OHCS programs deliver outsized benefits to women. The investment is made more attractive by the fact that the OHCS director and a majority of its governing body are female. Most for-profit entities can't come close to that kind of impact on gender equity, and most nonprofits that do aren't open for investment.

That's just one of the many opportunities SNWAM and other advisers offer their impact investor

clients. New portfolios that cover concerns like climate change, environmental conservation, public education and so on are chock-full of other opportunities to invest in states and localities.

Social impact investing's movement from the fringe to the mainstream has a lot to do with the growth of "impact ratings" as well. Traditional credit rating agencies like Moody's, S&P and Fitch just tell investors the likelihood they'll get their money back, and their ratings are based on a government's financial health, tax base and economic outlook. But impact credit rating agencies tell investors whether an investment is consistent with their social impact objectives. HIP Investor Ratings of San Francisco is one of the largest of these agencies. Its ratings criteria focus on "health, wealth, earth, equality and trust." Many social impact portfolios won't include a government's bonds without a four- or five-star HIP rating. Going forward, this means measurables like public school graduation rates, minority unemployment trends and Environmental Protection Agency water quality scores, among others, might be just as important as tax collections and reserve funds.

Fortunately, most states and localities are good impact investments. If they tell their story correctly, they'll have access to a new and robust pool of potential investors. And perhaps more important, they'll help enlighten a new generation to the essential, often unnoticed high-impact work they perform every day.

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