Positive Impact Investment

A journey from Global Administrative Law to Positive Impact Investing

Karen Wendt- Responsible Investmentbanking, Germany

Positive Impact Investing (PII)
Going Beyond Risk-Liquidity-Return

- Nascent Field of Research.
- World Economic Forum (2013) acknowledged role of investment sector in creating solutions to global challenges: “Given the nature of how resources are distributed in the world, private investors may have a special role and responsibility in addressing social challenges”. challchchallengeschallenges.” (World Economic Forum 2013).

How to circumscribe PII

- Field occupied and developed by practitioners.
- Encompasses Responsible Investment or Socially Responsible Investments (SRI), Sustainable Investment, Thematic Investment and Impact First Investments (Cambridge Associates 2015).
- Many researchers recognize this journey.

Positive Impact Investing Defined by Practitioners (GIIN,EMPEA et.al)

- ” Impact investing is a lens through which investors consider investment options across asset classes, such as bonds, listed equities, and private equity.” ”Impact investors pro-actively invest with intention to generate measurable benefits to society or environ-ment alongside with financial performance.“

Positive Impact Investing Core Caracteristics (according to GIIN)

- Intentionality;
- Financial Return Expectations;
- Measurement and Report Eco-Social (E&S) Performance alongside Financial Performance (setting metrics for dual objective);
- Stakeholder Engagement (SMART Objectives):

Positive Impact Investing Distinct from SRI

- Whereas Responsible Investment or Socially Responsible Investment (SRI) screens to avoid portfolio exposure to socially or environ-mentally harmful investments, impact investing actively & intentionally seeks to create a positive, measurable impact through profitable business (extends invest universe).

Developing Best Practice:

Bridges Ventures (2013)

- Developed a four-dimensional Bridges IMPACT Radar, which plots impact risk and impact return of each of the four criteria: "Target outcome," "Additionality," "Alignment" and "ESG," which are evaluated from a return as well as a risk perspective based on a scoring model.

Developing Best Practice: KL Felicitas Foundation (2015)

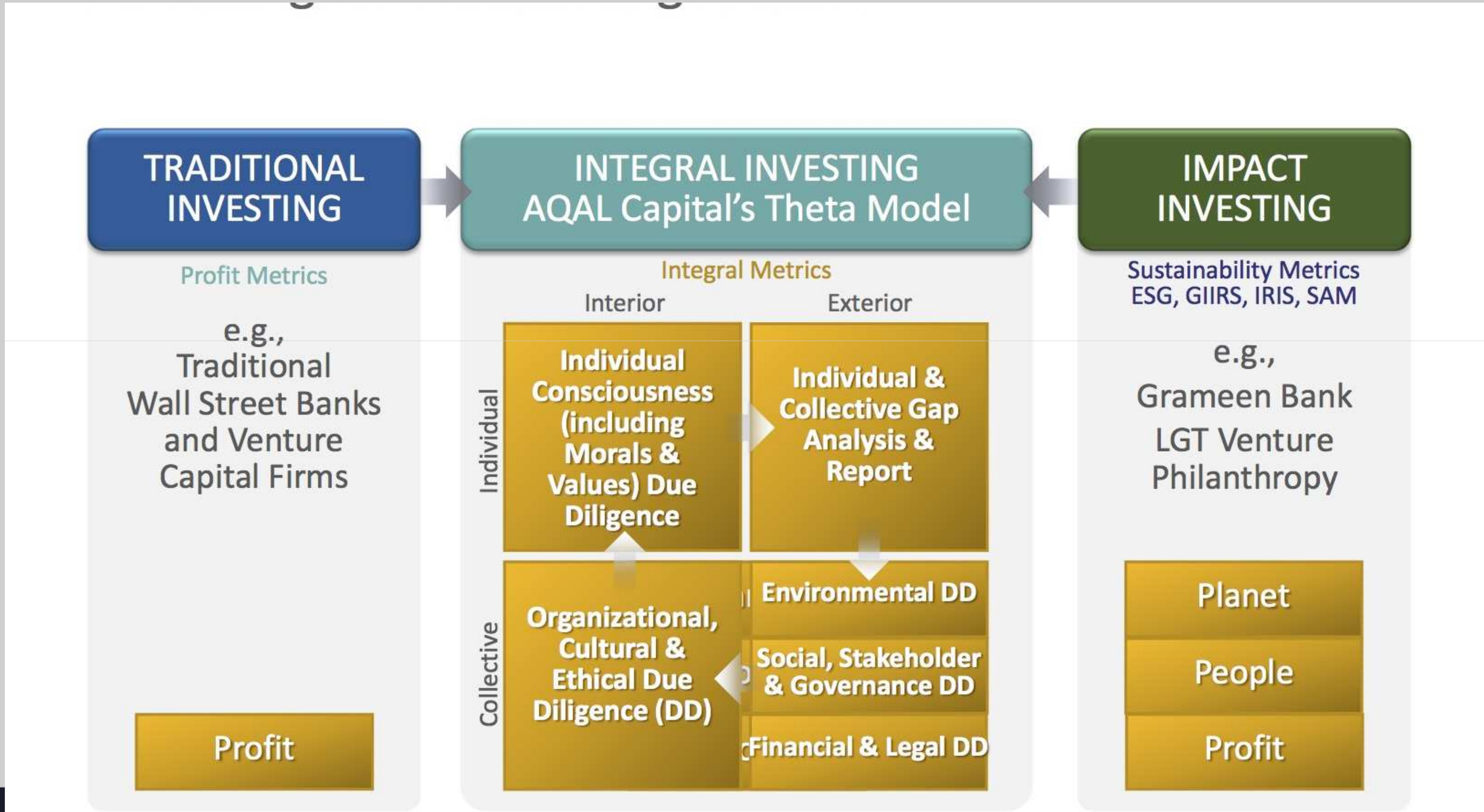
- Developed a Theory of Change to influence the market (investors, investees and intermediaries) alongside with creating an own impact investing portfolio whereimpact is measured alongside return

Theory of Change

Theory of change

Investment Portfolio	Movement Building Work
Impact achieved by Individual Assets/ Investments	Impact on investees
Impact achieved by Theme	Impact achieved on Intermediaries
Impact achieved by Responsible and Sustainable Investments	Impact achieved on investors

From Traditional to Impact Investing AQAL



Learning Enablers: The Emergence of Global Administrative Law

– Emerging patterns of global governance are being shaped by a little-noticed but important and growing body of global administrative law. This body of law includes Soft Law Standards with quasi legal status.

– Equator Principles, OECD Common Approaches, OECD MNE Guidelines, IFC Standards, ILO, Aarhus Convention and UN Guiding Principles for Human Rights show patterns of commonality & connection.

• Devel opment in emerging markets is often in the

Framework for Project Finance

Management Systems and Governance

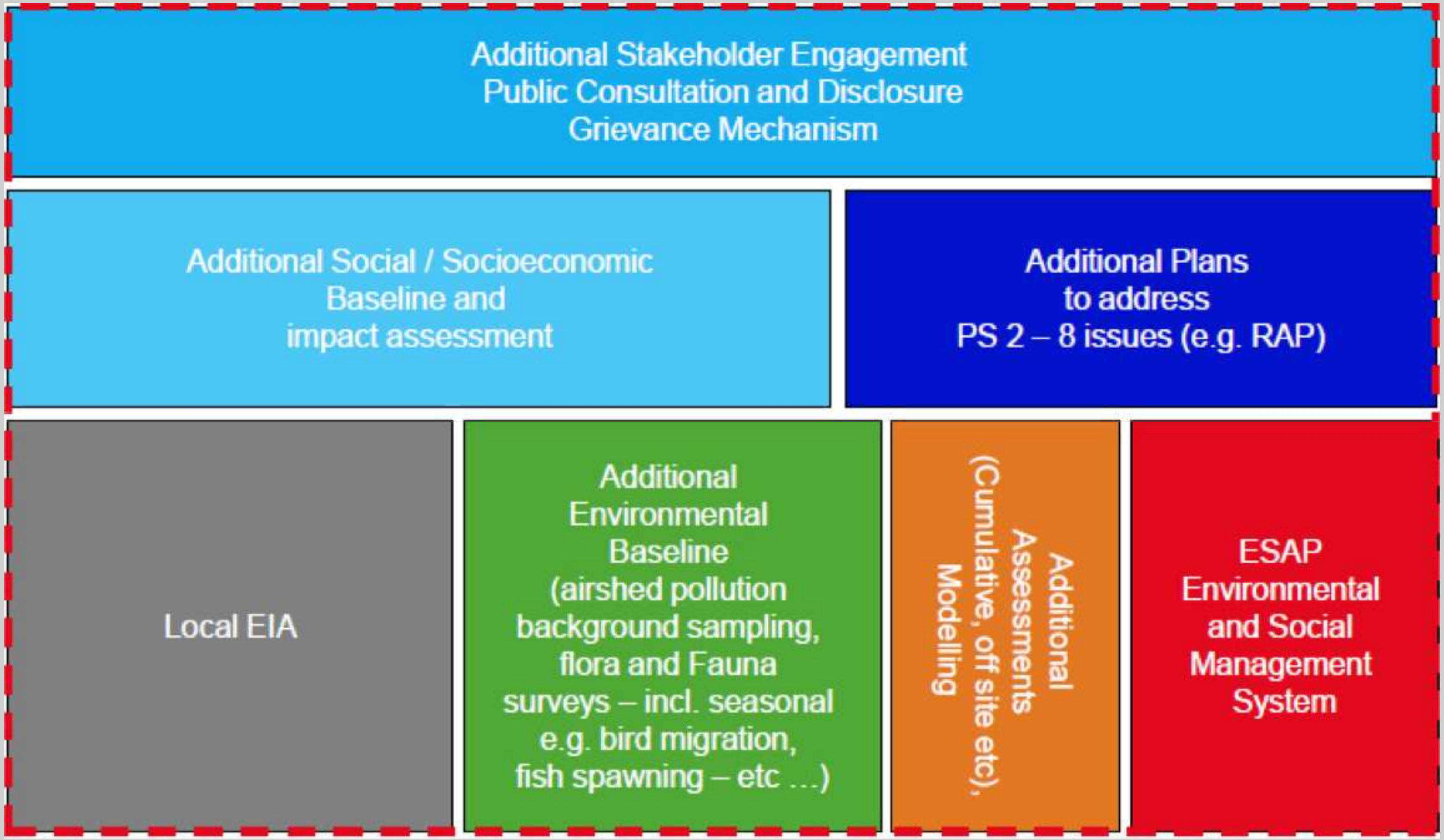
Stakeholder Engagement Consultation Grievance

EquatorPrinciples in Project Finance and Project Related Loans

EIA

Additional Assessments

(Social, cumulative impacts)


Additional Stakeholder Engagement
Public Consultation and Disclosure
Grievance Mechanism
Additional Social / Socioeconomic
Baseline and
impact assessment
Additional Plans
to address
PS 2 – 8 issues (e.g. RAP)
Local EIA
Additional
Environmental
Baseline
(airshed pollution
background sampling,
flora and Fauna
surveys – incl. seasonal
e.g. bird migration,
fish spawning – etc …)
Additional
Assessments
(Cumulative, off site etc),
Modelling
ESAP
Environmental
and Social
Management
System

From Impact Risk to Impact Return

- Reputation Risk,Legitimacy/ InstitutionTheory;
- Governance and Compliance including ESG;
- Fiduciary Duties;
- Extra-Financial Risk & PESTO Analysis in Portfolio Theory
- Role of Leadership, Brands, ESG in Goodwill;
- Disruptive Innovation;

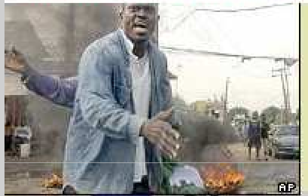
Development of Impact Risk Story

- Consistent Environmental, Social & Governance standards developed by Worldbank, IFC, Mulilaterals, DFIs, UNEPFI often referred to as “Global Administrative Law “ (Mc Intyre 2015). Governance & Reputation is seen a necessary corrective in an industry governed by principal-agent theory.

Impact of Extrafinancial (ExF) Risks

risks in project financing.

Community protests cause project shutdowns and infrastructure damage



Dead vultures cause energy production loss

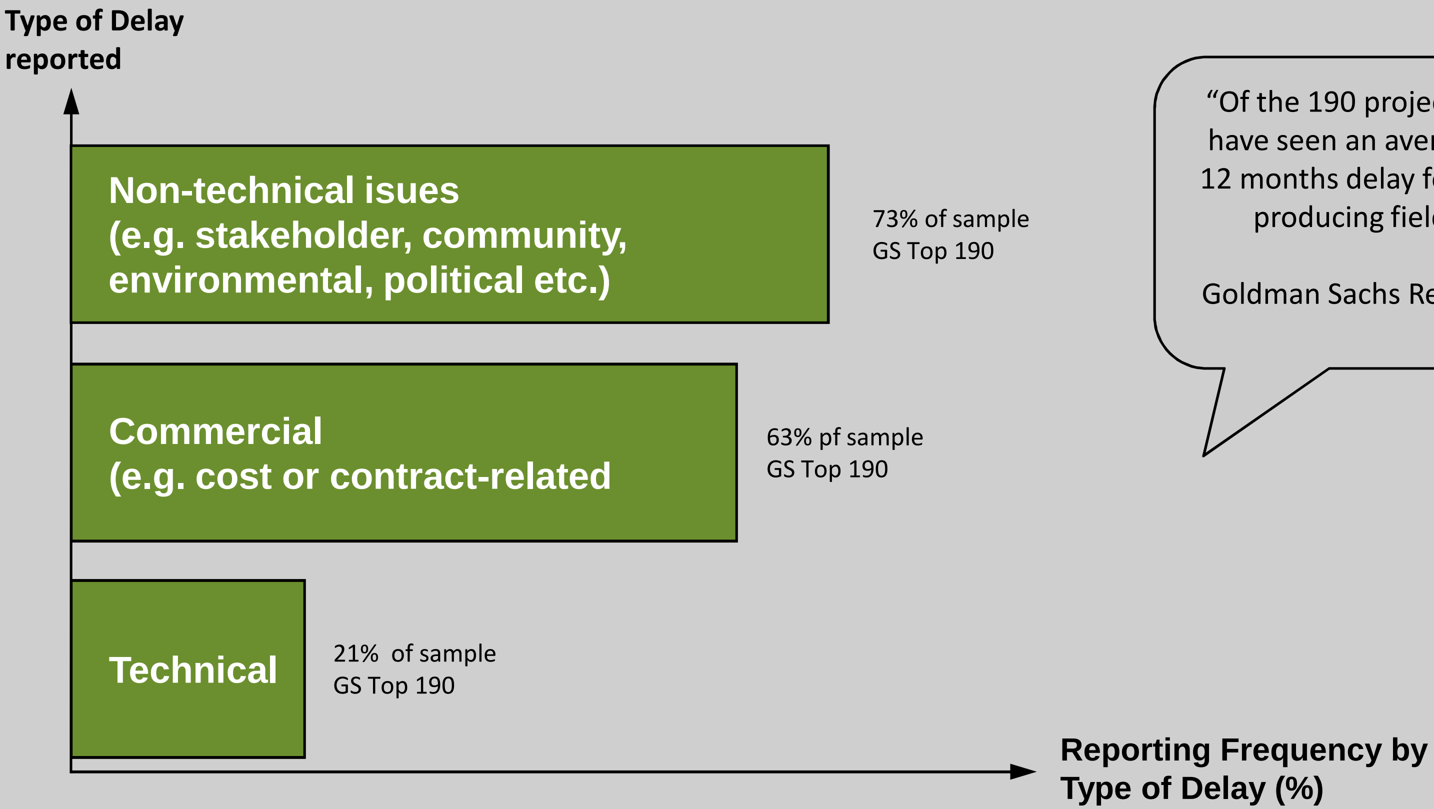
Toxic waste dumping by third party supplier results in $250m fine

Asia-Pacific:
Project finance – Gunning for Gunns
Australian bank ANZ is having second thoughts about financing the controversial Gunns pulp mill in Tasmania.
Now institutional investors are reported to be unhappy with the project, while its primary banker, ANZ, has stated its determination to finish an independent technical review before agreeing to arrange vital project financing.
12 Nov 07

Poor management of extra-financial risks results in financing difficulty

Not just best practice, but part of a robust risk management approach

Impact Risk Quantification by GS



"Of the 190 projects, we have seen an average of 12 months delay for non-producing fields"

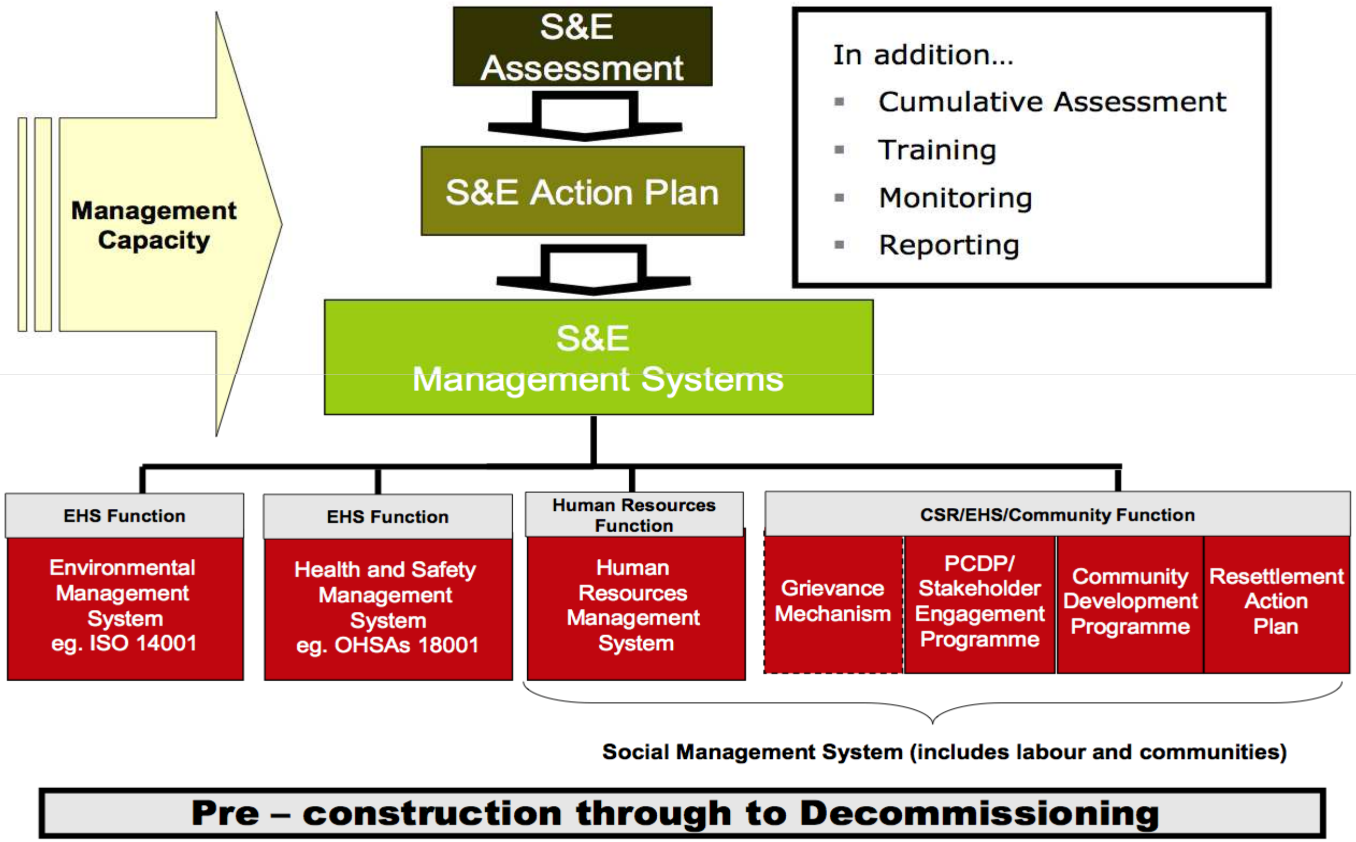
Goldman Sachs Research

Going Beyond Apparent Financials

- Political
- Environmental
- Social
- Technological
- Organizational

→ Risks stemming from PESTO Factors

PS1: Social and Environmental Assessment and Management S Karen n

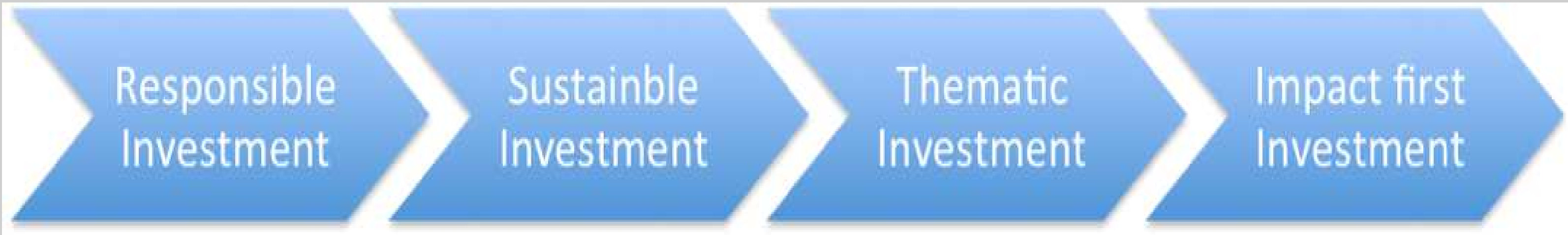


46

SRI Basic Elements

- Eurosif Transparency Code Certification;
- Asset Filtering: Exclusion List /Assets from certain industries;
- Adoption of ISO Certifications, EMAS etc.;
- Best in Class Selection Process;
- Screening on Institutional Legitimacy.

Market History of Impact Investing



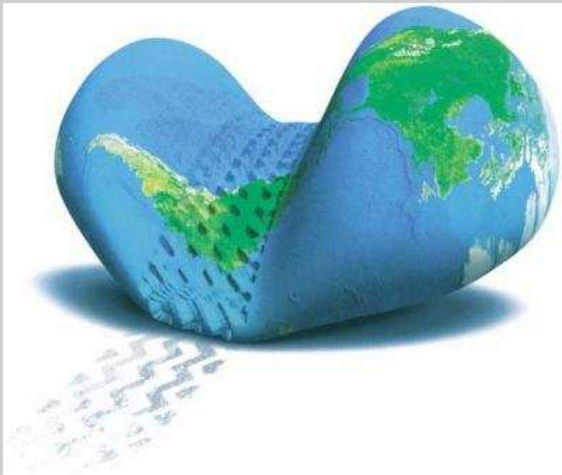
- Figure 1: The Impact Investment Journey; Source: Cambridge Associates and New Philanthropic Capital NPC. 2015

Context Factors and Investment

Climate Change and Climate Adaptation Risk

Energy Crisis

- **Increasing Energy Price**
- **Electricity access to billion of people**



Increasing Consumer Society:

- **New Economic Giants (BRIC)**
- **Consumers at the bottom of the pyramid**
- **Incresing population and urbanisation**

Scarcity of Natural Resources

Impact Return – Finding Answers to Global Challenges

- Political
- Environmental
- Social
- Technological
- Organizational

→ Opportunities stemming from PESTO Factors

Impact Return

- Green Bonds and Social Bonds
- Pay for Performance Schemes
- Financed CO2 Emissions
- Addressing poverty at the bottom of the pyramid with market driven solutions like Leapfrog, Memphis Meat etc.

Conventional versus Impact Investing

- **Intermediation: Find, match, price capital moves from Suppliers to Users**
  - Ultimately involves the creation and transition of real assets in real economy
  - Paid on fee basis by clients
- **Market Innovation: Additionality and Alignment of Interest – allows deals to happen which would not have happened under pure FINANCIAL intermediation**

1. Investment Finances creation of new assets often based on disruptive innovation
2. Enables capital constrained good ideas and projects to be commercialized
3. Promotes adoption of innovations for producers Helps creation of infrastructure & Public Goods
4. Enables development in face of Political Risk

Main Hurdles to Impact Investing

- Compatibility: Applied logic constructs incompatible to each other. Compatibility, however, is a pre-requisite for the inclusion of impact investments into the portfolios of traditional institutional investors.
- BUT: Low correlation of impact investments to traditional markets reduces portfolio risk increases sustainability

Main Hurdles to Impact Investing

- Attracting Institutional Capital is a significant constrain to the development of impact investing. Private equity-style impact investing remains "niche" according to Bridges Ventures;
- BUT: Establish Evidence that no trade of between impact and financial return (see IRIS) impainvestments to traditional markets reduces portfolio risk increases sustainability

Main Hurdles to Impact Investing

- Mismatch between investors' preferences and absorptive capacity: Institutional Investors need significant size (e.g. US$500 million), have minimum commitment sizes (e.g. US$100 million) and maximum ownership limits;
- BUT:Social Stock Exchange, Impact Exchange help go market to 650 bn USD.

The Business of Business is Business ?