

IMPACT INVESTING AS THE NEXT NORMAL

By Wouter Koelewijn and Dean Hand

Over the last decade, the annual surveys of impact investors by the Global Impact Investing Network (GIIN) have identified inspiring signs of progress. Going forward, scaling with integrity must be a priority for the industry.

United Nations Secretary-General António Guterres remarked at this year's Nelson Mandela Annual Lecture that all of us should work together to integrate the principles of sustainable development into financial decision-making. He laid out the challenge that the financial system is not working for all and that 'financial markets must be full partners in shifting the flow of resources to the green, the sustainable and the equitable.'

This is what impact investing is about. The focus of the GIIN and its more than

300 member organizations around the world is to build an impact investing ecosystem which fosters strong communities, a healthy environment, and a sustainable future for all people. In this future, the GIIN envisages financial markets that are inclusive and where impact is integrated into all financial decision making, simply by default.

A DECADE OF PROGRESS

The growth and increasing sophistication of impact investing over the past decade give reason for optimism. In 2010, the GIIN launched its first survey of impact investors. Each year since, we have seen impact investors doing more of what they do best: leveraging the power of finance to tackle our biggest social and environmental challenges.

This year, the 2020 Annual Impact Investor Survey¹ provided insights from nearly 300 of the world's leading impact investors. The respondents represent a variety of organizations, from asset managers, foundations, DFIs, to pension funds and insurers. The impact investing industry is very diverse in geography, asset class, and approach. From the respondents, headquartered in 46 countries, 67% seek risk-adjusted market rate returns. Moreover, 63% of all capital invested in 2019 was in private markets, with the remainder in public markets.

Similar to past years, 88% indicated that they were meeting or exceeding their financial performance targets and an impressive 99% were achieving their impact performance targets. The compound annual growth rate for impact investing AUM among repeat respondents is 17%. Despite the headwinds from the COVID-19 crisis, most respondents to the survey plan to maintain or increase their capital commitments to impact investing in these difficult times.

CHALLENGES AHEAD

There are also challenges, however. Over the next five years, respondents indicate that they are most concerned about impact washing: 66% perceive impact washing among the top threats to the industry. How to address this challenge? The survey offers some insights as to how we could proceed. It starts with the core characteristics of impact investing.²

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A core tenet of impact investing is to allocate capital with the intention to create positive impact and to measure and manage these impact results. This ex-ante intention to allocate capital to positive impact is what distinguishes impact investing from other forms of sustainability investing or responsible investing. But intention alone is insufficient. Essentially, investors should know the actual results, positive and negative, of their investments' performance.

What they need are the systems and practices that facilitate this knowing, so they can integrate this knowledge into the investment process. With this integration, both financial and impact returns can be optimized for the benefit of all stakeholders. The survey found that 84% of impact investors are unable to compare their impact results to market performance and 89% cite the lack of transparency on impact performance as a challenge. Without the ability to compare performance to that of peers and to the very problems that investments seek to address, there is a risk that impact investment will become nothing more than an unfulfilled promise.

INDUSTRY INNOVATION NEEDED TO SCALE WITH INTEGRITY

To address these challenges, an infrastructure of systems is needed so that investors can analyze and compare impact performance data. The risk of impact washing can be mitigated by

transparency and facilitated by standardization, comparability and impact data sharing at scale.

Focus to date has been on the harmonization, standardization and adoption of a shared language: impact metrics. IRIS+ is now the generally accepted system for measuring, managing, and optimizing impact.³ The next frontier is to develop impact benchmarks, indices, and rating systems. These crucial pieces of the impact investment infrastructure will enable comparability of impact investments across portfolios on the basis of impact results and comparison to overall market performance. But the infrastructure is only a start. It requires strong adoption by asset owners and asset managers.

ACTION NEEDED TO ENSURE IMPACT INVESTING IS THE NEW NORMAL

The challenge to investors is to translate noble motivations into actual impact results that make a positive, measurable difference. The call to action is straightforward:

- Adopt impact goals for your assets and commit to measuring your progress.
- Use impact data to inform your investment decisions across asset classes.
- Subject your impact claims to the same rigor as your financial statements.
- Account for your results to your stakeholders.

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Join an ever-growing cohort of investors committed to using the generally accepted common language for impact, IRIS+, to measure and manage your impact.

We encourage you, asset owners and managers, to take these steps, not because they are required by compliance or statutory requirement or a legal prescription, but because they are needed. We cannot afford the financial sector to underperform on its social and environmental impact. As investors and financiers, your bold action matters to make a just and sustainable future a reality. The impact investing infrastructure, together with your resolve, can lead us to the next normal: a financial system that truly serves our planet and our society. «

1 Available for free at www.thegiin.com/research

2 See www.thegiin.com/characteristics

3 Free use of IRIS+ is available at www.iris.thegiin.com

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