IMPACT

The growing popularity of impact investing

Impact investing is an investment strategy which has grown dramatically since its infancy. Its objective is to make a positive difference and target progress on environmental, social and governance (ESG) matters. Whilst still in the initial stages of development, impact investing continues to grow and mature. Here Samantha Steele outlines what impact investing is and how we are seeing increased momentum around its incorporation into private market investment plans.

What is impact investing? Why now?

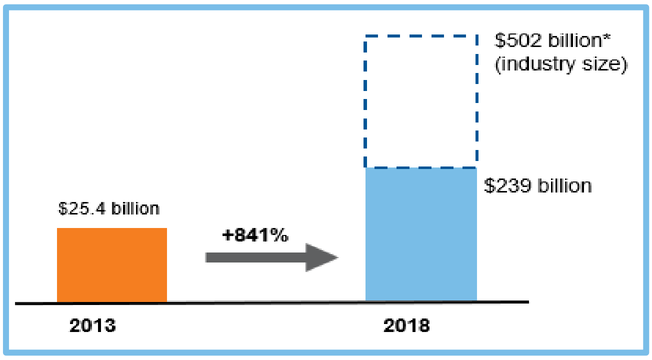
The growth rate of the impact investing industry has ratcheted up following the publication of the United Nations' 17 Sustainable Development Goals (SDGs) in 2016. Indeed, there is now a rising contingent of global investors who are seeking to make a direct impact on the world by means of impact investing. They seek the dual objective of producing both financial and social/environmental measurable returns, i.e. profit with purpose. A key example of this could be investing in a wind farm: impact is achieved through the carbon offset the wind energy provides, plus a strong financial return is achieved through the income streams that the asset creates – just like an investor would with a typical infrastructure exposure.

The popularity of impacting investing appears to be growing, but is capital being raised for this strategy?

The past few years have seen capital flow into impact investments from a widening variety of sources. For example, funding that comes from pension funds and insurance companies has increased significantly (as a share of the total) over the past three years.

Overall, impact fund managers have amassed record quantities of assets under management (AUM): an estimated $502* billion by 2018, according to the Global Impact Investing Network (GIIN) Annual Impact Investment Survey. Since 2013, AUM of respondents to the GIIN Annual Survey have increased significantly from $25.4bn to $239bn in 2018. [1]

Assets Under Management

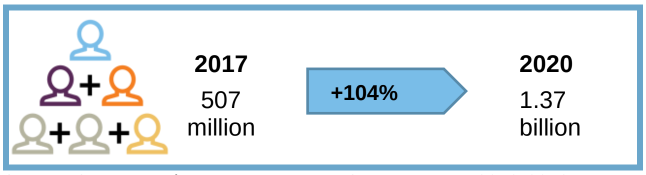


Source: GIIN Annual Impact Investment Survey reports 2013-2019, KPMG India Analysis

Yet even this amount of money is small compared with the annual capital outlay - estimated at $1.4 trillion to $2.5 trillion of additional spending - required to achieve the SDGs set by the United Nations by 2030.[2] Fortunately, investment trends appear to be moving in that direction. Surveys are showing that a substantial number of investors, including 'mainstream' investors, are seeking impact investment products. As the impact economy matures, we would expect to see more asset owners prioritizing the financing of solutions to environmental and social challenges, and a major increase in commitments of capital to impact-seeking investment vehicles.

Since 2017, it is estimated that the number of beneficiaries from impact investing will increase by 104% by 2020.[3]

Beneficiaries



Source: GIIN Annual Impact Investment Survey reports 2013-2019, KPMG India Analysis

What kind of areas does impact investing cover?

As the market matures, the opportunity set is expanding. Areas where we have seen impact investing are:

- Healthcare
- Clean energy
- Education
- Financial inclusion
- Affordable housing
- Strategies around clean water/plastic
- Food security

[1] Source: GIIN Annual Impact Investment Survey reports 2013-2019, KPMG India Analysis
[2] Source: GIIN Annual Impact Investment Survey reports 2013-2019, KPMG India Analysis
[3] Source: GIIN Annual Impact Investment Survey reports 2013-2019, KPMG India Analysis

It is also possible to invest both in an equity and debt instruments. Although we believe that it would be worth questioning debt for impact investing, as there is a chance that the management influence may dilute the true 'impact' of this type of investment.

How big is the fund manager universe for impact investing?

According to the survey by GIIN, fund managers raised $13.6 billion during 2018 and plan to raise $23.9 billion during 2019, a 76% increase.[4] However, all data surrounding impact is very difficult to access as the market is still very immature. So, we are hoping that over time, there will be more transparency surrounding that number i.e. what percentage are first-time funds.

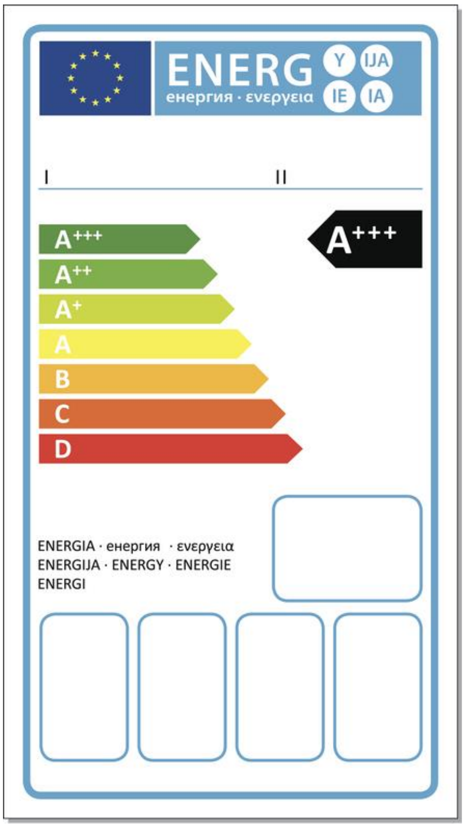
One of the main observations we've made is that there are a significant number of first-time funds and emerging managers that have a limited (or no) track record. In our view, successful impact investing requires either previous experience investing in private market funds or specialist advice.

There are three categories of impact managers currently in the market:

- Diversified large-cap: launched by private market managers, provides benefits to smaller clients as a one-stop-shop but impact is diluted
- Concentrated single strategy experienced: strategy dedicated managers with proven fund experience
- Concentrated single strategy inexperienced: strategy dedicated but with limited fund track record

By definition, impact investing is active. How can impact be measured?

Measurement is a constantly evolving and GIIN have tried to pave the way launching an impact benchmark. However, in our view, there is a lot more development required before we would consider using it. In an ideal world, we would like to see something similar to the energy efficient labels used for electronic goods such as fridges, dishwashers and televisions, which help consumers make like-for-like comparisons of a goods' energy consumption. Cambridge University have been working with many of the listed funds in the UK to do something along these lines, with the aim to roll out across all funds (not just impact funds).



Source: Getty Images.

We believe that the listed market will pave the way with metrics, and private markets will shortly follow

In summary, what are the three biggest challenges for impact investing?

1. **Research expertise is critical** – there is a limited pool of experienced managers and a significant amount of first-time funds. Strategies can be niche with steep learning curves and often exposure to more challenging markets such as emerging markets e.g. renewable energy infrastructure. It is for these reasons we suggest that investors seek specialist advice in underwriting these strategies.
2. **Impact measurements are still evolving** - Accounting standards for measuring impact do not yet exist and the measures in use are still evolving. Greater clarity on measurement is slowly emerging with academic researchers studying impact assessment, and organisations such as the Global Impact Investing Network, GIIRS, and Principles for Responsible Investment are seeking to develop standards for the industry. We're also seeing more developments in the listed space which will trickle down to private markets, e.g. Cambridge University's benchmark tool.
3. **Transparency needs improvement.** To reduce the potential risk of 'impact washing' (as compared to green washing), investors are beginning to emphasise the importance of greater transparency around impact investing when underwriting a commitment.

[4] Source: GIIN Annual Impact Investment Survey reports 2013-2019, KPMG India Analysis

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