Philanthropy Impact

Exploring the role of philanthropy as part of wealth management

Magazine

IN THIS ISSUE

THE CAMPAIGN FOR GROWING MODERN PHILANTHROPY

Impacting investing: trends, issues and capabilities

Impact investing and socially responsible investment strategies pursuing societal impact

PHILANTHROPY	VENTURE PHILANTHROPY	SOCIAL INVESTMENT	IMPACT	SRI – ESG INVESTMENT

The above table from **The Investment-Return Continuum** shows how Impact investing rests between social investment in social enterprises (whose primary purpose is a social return of some type; and only secondarily with some modified form of financial return) and SRI/ESG investing (whose primary purpose is to maximise financial returns to investors whilst achieving some social good which is secondary). Impact investment is where there is an equal emphasis and balance between societal and financial returns on investment.

A need to know for professional advisers

Philanthropy Impact

Vision: A world where individuals and families engage in philanthropy and social investment, supported by advisers.

Mission: Growing modern philanthropy by developing the skills and knowledge of professional advisers about philanthropy and social investment. We deliver our mission by delivering activities to support our members and key stakeholders.

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- Publications and Research: developing our 'body of knowledge'
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- Technical content and analysis
- Case studies
- Philanthropy Impact Magazine
- Market research

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- Advocacy: lobby for policies and regulations that encourage philanthropic giving and social investment
- Policy position submissions and papers
- Engagement with Government and key policy stakeholders

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The purpose of the magazine is to share information about philanthropy in a domestic and international context. We welcome articles, letters and other forms of contribution in Philanthropy Impact Magazine, and we reserve the right to amend them.

Please contact the Editor at editor@philanthropy-impact.org

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Editorial

Rennie Hoare

There has been a vast number of reports and news articles about how professional advisers to ultra high net worth (UHNW) individuals need to adapt to address a younger generation of clients. As a collective of millennial philanthropists brought together by Philanthropy Impact, we believe we can use our voices to say this once again, but also to move this sector towards greater understanding of what they can do as professional advisers to adjust to these trends.

As young philanthropists and investors, we see the role we can play in this world as a crucial form of activism, by using our money as consumers or by investing our money in a thoughtful way.

We understand that it is not always easy for advisers to advise us in a complicated sector where definitions and guidelines are blurry and difficult to distinguish. That is why we, Philanthropy Impact's Millennial Group, have decided to prepare a White Paper, which will be distributed to the sector and can be used as a tool by advisers to navigate the sometimes confusing realm of engaging with younger clients' needs. Addressing the need for more and better impact investing plays an important part in this. Our White Paper will outline case of successful client-advisor relationships as well as some of the dos and don'ts for advisers who are ready to take the steps towards offering these types of advice. It will offer help for advisers working with families where a younger generation might want to step out of the traditional space their parents have been engaged in to do innovative and collaborative work with other young people.

Our White Paper will outline case studies of successful client-advisor relationships as well as some of the dos and don'ts for advisers who are ready to take the steps towards offering these types of advice.

Research[1,2,3] demonstrates that millennials are value-driven consumers who wish to have a positive environmental and social impact as consumers as well as investors. With the great wealth transfer which will be taking place in the coming years, where a large amount of wealth will go to women and millennials, it will be crucial for advisers to understand these value-driven consumers to be able to serve them in the best possible way.

This magazine covers many aspects of impact investing and aims to move the dialogue ahead on what impact investing can mean and what opportunities it brings both for advisers and clients.

We hope that this issue of the Magazine, as well as the White Paper we will prepare, will help advisers to support their clients on this journey.

Rennie Hoare
Chair, Philanthropy Impact's Millennial Group

[1] *Investor motivations for impact (2017), Barclays,* https://www.barclays.co.uk/content/dam/documents/wealth-management/investments/impact-investing-product/investor-motivations-for-impact.pdf

[2] *Supertrends 2017 - Millennials' values (2017), Credit Suisse,* https://www.credit-suisse.com/microsites/private-banking/supertrends/en/supertrends-2017/millennials-values.html

[3] *Sustainable investing: The millennial investor (2017), EY,* https://www.ey.com/Publication/vwLUAssets/ey-sustainable-investing-the-millennial-investor-gl/$FILE/ey-sustainable-investing-the-millennial-investor.pdf

Social investment is not impact investment, let's finally be clear on what we mean

James Perry *www.bcorporation.uk*

James Perry

To understand what social investment is, it's important to go back to its start. In the beginning there was Ronnie (Sir Ronald Cohen), who having masterminded the 2008 Dormant Bank and Building Society Accounts Act, then founded social finance from which social investment was born. Ronnie then made friends with Nick O'Donohoe from JP Morgan, a prince of impact investing. Nick had orchestrated JP Morgan's seminal impact investment report. The two then worked with Nick Hurd, Minister for Civil Society, to create Big Society Capital with the result that social investment took off in the UK. Or is it impact investment?

This question reveals that at the heart of that history is a linguistic fudge that sits atop a conceptual fudge. And if we don't unpick it now, it will fudge up our future. To see ahead, we must (to paraphrase Sir Winston Churchill) first look back.

To understand what social investment is, it's important to go back to its start.

Ronnie set out with the Commission for Unclaimed Assets to understand how repayable capital could be deployed to help to scale social sector organisations (social enterprises and charities). From the outset, the assurance that an intervention was 'social' came from the presence of an asset lock, which was a barrier to distributions. The compelling potential of Ronnie's vision was that charities and social enterprises – should they demonstrate their value – might persuade someone (mostly government) to pay for it. This might enable them to access an almost limitless supply of capital. It explains the associated obsession with social impact bonds, which arises from their promise as an instrument that might become the venture capital industry for social transformation – the vehicle through which much of this capital might pass. By deploying vast sums into actually solving social problems, society is strengthened and the need for government intervention is radically reduced. A virtuous cycle is created that redefines the social contract, with civil society organisations at its heart. This is the powerful idea at the heart of social investment.

Meanwhile, others were making the point that all capital deployments in society have a social impact. Not just the *10%* of the economy that is deployed in the social sector, but also the 90% deployed in the mainstream economy. Understanding and seeking a net positive social and environmental impact from the 90% is at least as important as social investment. But this is a different point, although it is allied and associated. This is impact investment.

Separating social investment from impact investment

So, we have social investment, which aims to enable social sector organisations to access capital. And we have impact investment, which is a movement to reform capitalism by including social impact as a third investment dimension in mainstream capital markets, alongside the classic binary of risk and return.

By deploying vast sums into actually solving social problems, society is strengthened and the need for government intervention is radically reduced. A virtuous cycle is created that redefines the social contract, with civil society organisations at its heart. This is the powerful idea at the heart of social investment.

These two ideas are distinct. Social investment is an asset class – it is, after all, investment capital deployed into a distinct class of assets, be they real assets, private equity, fixed income and so on. The distinguishing feature of these assets is that they have a primary social motivation and they are asset locked structures. The Big Society Capital Governance Agreement formalises this idea and is, in the UK, where the rubber hits the road. Generally, these assets are where positive social impact is most concentrated.

By contrast, impact investment is not an asset class and it is wrong to think of it as such. All investments have an impact. Impact investment strategies can (and should) be deployed in mainstream capital markets in every asset class, whether fixed income, private equity, cash, real assets, social investments and even public equity.

The point is that these two ideas have been allowed to become conflated. The G8 taskforce evolved into the 'Global Social Impact Investment Steering Group' (GSG). Without clearly defining each term, this is risky because these two allied but distinct ideas have different needs. It risks creating confusion, that might set people, who are fundamentally aligned, at odds with one another.

Impact investors and social investors have much in common. They seek the same outcome – a society left fairer, more inclusive, more resilient and more prosperous as a result of investment activities.
This matters, because the quantum of investment

capital deployed for profit by the private sector and foundations dwarfs the quantum of capital deployed by governments and foundations for social outcomes.

But social investments are a brand spanking new, wholly distinct kind of asset. These assets offer the awesome promise of directly solving social problems. The market in them needs a substantial investment in research and development (i.e. subsidy). It also needs a strategic reboot of the government's approach to commissioning – something that sadly seems light years away.

By contrast, whilst impact investment does need policy support, it should not need subsidy. Impact investment is a different vision for capitalism. It is a superior way for the global economy to operate than by pretending that private sector capital deployments have neutral social impact, as it currently does. It offers the promise of a sustainable social contract where business no longer routinely strips value from individuals, families, communities and the environment because 'externalities are nothing to do with me, I'm just doing my fiduciary duty'.

The conflation of social investment and impact investment must stop because it risks creating a mutually assured destruction. There is a fundamental mismatch of expectation – in the risk/return offer of social investments on the one hand, and the risk/return requirements of impact investors on the other. This mismatch results in a logjam, where deals can't be done. Time is wasted and intermediaries – who rely on transactions – go bust.

Social investments as a set of assets (an asset class) within an impact investment portfolio makes much more sense, because those impact investment fund managers can (must) then accept the characteristics that the social investment market can offer.

Conclusion

Both of the allied but distinct industries of social and impact investment have each come an astonishingly long way over the last few years. Bravo to all concerned. Certain tensions should be expected in both fields – growing pains are a necessary part of growing up.

But some tensions are self-inflicted and result from a cross-purpose conversation that's been allowed to go on too long. Impact investment is not an asset class. Social investments are. The time has come for all participants, in both industries, to be clear about what they are doing, and about what they are not doing.

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Defining impact should not be an 'issue'

Bonny Landers *www.bridgesfundmanagement.com*

Bonny Landers

Potential impact investors are being inundated with articles telling them how to define impact in their investment portfolios and philanthropic programmes. This is confusing at best and off-putting at worst. Many potential impact investors are reluctant to consider ways to increase the positive impact of their investment and philanthropic programmes because they don't think they 'fit' these definitions – and some advisers are agreeing with them to avoid getting 'too personal' with their clients or to avoid changing the way they have 'always done things'. For example, they may say that financial returns are all that matter or that measuring impact is too difficult.

Standardisation in the industry may indeed be needed but, until we have that, the lack of one agreed definition of 'impact' should not be used as an excuse for not exploring the many ways to seek more positive impact in our investments and our philanthropic programmes.

In fact, we are finding that investors can and should define 'impact' for themselves – just as philanthropists and donors have done for decades. It is a question of personal values and goals which lead them to their causes and their theories of change. Once they are personally engaged with the goals, they become more connected to their investments and philanthropic efforts.

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Defining impact in a personal way means that everyone, from ultra high net worth individuals (UHNW) to pension plan contributors and smaller donors, is more aware of the positive and negative impacts their money is having on society. This can reduce the negative impacts and increase the positive ones across the entire spectrum, which can range from responsible/ethical, sustainable/environment, social and governance (ESG) through to impact driven and philanthropy, to target intentional social and environmental impact.[1]

Why is this relevant?

The increasing interest in impact is now well-documented. Last year, Morgan Stanley surveyed 118 institutional investors (including philanthropic foundations) and concluded that 70% of investors have already implemented ESG strategies and that 84% of asset owners are either 'pursuing or actively considering ESG integration' in their investment decision-making processes.[2] Cambridge Associates reported that 'a recent survey of Cambridge's endowment & foundation clients shows that 61% of them plan to increase their impact-oriented allocation over the next five years.[3]

In the past, most clients would expect advisers to understand ethical screening; now, they expect them to understand the entire spectrum from traditional investments to all things impact. As wealth transfers to the next generation, the demands change. A 2017 BlackRock survey[4] showed that 67% of millennials expect that their investments should reflect their values and address social and environmental issues, and 76% of women, another large group of inheritors, are focusing on their values as well. Given the increased coverage of these trends in the media, I would wager that the percentages will be even higher in their next survey. Advisers need to get ahead of this curve to remain relevant to the clients (current and future) and to become true trusted advisers who maintain long-term relationships by knowing their clients.

A 2017 BlackRock survey[4] showed that 67% of millennials expect that their investments should reflect their values and address social and environmental issues, and 76% of women, another large group of inheritors, are focusing on their values as well.

Still, what is impact?

There are several accepted definitions which the investment industry has been using for years.

Foremost is the original definition from the GIIN (Global Impact Investing Network): 'Impact investments are investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return' which has been supplemented by their 2019 Core Characteristics.[5]

The Advisory Group to the UK Government issued a report in November 2017 entitled *Growing a Culture of Social Impact Investing in the UK* which set out the definition of impact investing as: 'Investment in the shares or loan capital of companies and enterprises that not only measure and report their wider impact on society – but also hold themselves accountable for delivering and increasing positive impact'. The Implementation Taskforce report of 2019 states this is 'entirely compatible with the GIIN Core Characteristics'.

Yet, these and other definitions have not solved the issue of what is impact. A survey by Barclays showed that '56% of investors express interest in exploring impact investing' but only 15% had made an impact investment at the time of their survey. The report concludes that it is investor (and donor) motivations which are the key to defining and increasing impact.[6]

In other words, impact is personal. Understanding the motivations for this increasing interest is key to defining it. Advisers need to help potential impact investors and donors to explore their motivations for seeking greater positive impact in their investments and philanthropy.

Why?

Based on my personal experience of working with many types of investors and philanthropists, I can say that they can and do list numerous motivations which have brought them towards impact investing. These include:

- **Financial** – some investors are motivated by the financial rewards promised by new technologies which also may be life-changing, thereby 'doing well by doing good'.
- **Legacy** – some philanthropists seek to expand their toolkits with impact investments which can complement their existing philanthropic programmes, thereby increasing the effectiveness of their efforts to achieve positive change whilst solidifying a legacy.
- **Reputation** – some people want to understand impact in order to avoid a risk to their personal reputations. For example, it may prove embarrassing to be invested in certain sectors such as gambling or payday loans, etc.
- **Systemic change** – many others are looking for systemic change. For example, those who are demanding that their service providers publish data on the positive and negative impacts of the companies in which they invest their clients' monies often say they are trying to change behaviours in the financial services industry, thereby changing the world by increasing the overall positive impact – or even the purpose – of each company.
- **Risk management** – most investors are now expecting that ESG risks will be taken into account by asset managers during the investment decision-making process. This is certainly reflected in the exponential increase in funds labelled 'ESG' or 'sustainable' or 'impact' – though these products do need rigorous analysis to understand their true impact profiles. By specifically addressing ESG risks, investors are hoping to protect or enhance their investment returns as well as increase awareness of the impact of the investments.

Advisers need to help potential impact investors to explore their motivations and goals so that they clarify their own definitions of impact and are encouraged to use all of the available tools to achieve their aims. It will also help them to provide appropriate solutions for their clients.

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How can advisers do this?

More than 2,000 practitioners in the field (including the largest asset managers and philanthropic foundations in the world) are building a consensus around a definition of impact and its measurement and management. The Impact Management Project (IMP) defines impact as: 'Impact is a change in an important positive or negative outcome for people or the planet.'

Acknowledging that this is yet another 'definition of impact' with the potential to confuse (or be the proverbial straw breaking the camel's back), it is, nevertheless, a helpfully straightforward definition now being used by a huge number of premier impact investment practitioners and service providers. It therefore can stake a very strong claim to helping to standardise the terminology in the field.

More importantly, this definition also allows for personal interpretation to allow each of us to define impact according to our own criteria, thereby encouraging more people to become impact investors, no matter their resources or their goals.

In view of this, we can help our clients to set their criteria by asking the right questions. For example,

- Why are you interested in impact? (i.e. exploring motivations).
- What are the changes you wish to see? (i.e. exploring goals).
- Over what timeframe are you hoping to achieve these changes? (i.e. exploring the parameters of risk and return).

The answers can help advisers to respond with the appropriate products tailored to the client's motivations and goals whilst incorporating the appropriate risk and return parameters. The more specific you can help the client to be, the more connected to their investment and philanthropic portfolios they will be and the more prudently their financial and human resources can be managed.

The IMP sets out five dimensions of impact which help to clarify clients' answers and set the impact measurement criteria (which is an iterative process):

- *What* tells us what outcomes the enterprise is contributing to and how important the outcomes are to stakeholders.
- *Who* tells us which stakeholders are experiencing the outcome and how underserved they were prior to the enterprise's effect.

- *How much* tells us how many stakeholders experienced the outcome, what degree of change they experienced, and how long they experienced the outcome for.
- *Contribution* tells us whether an enterprise's and/or investor's efforts resulted in outcomes that were likely better than what would have occurred otherwise.
- *Risk* tells us the likelihood that impact will be different than expected[7].

Conclusion

The IMP consensus agreed by the foremost practitioners across the industry can help advisers to help their clients towards understanding and articulating their impact goals. Once they are reassured that their personal definitions and approaches are valid and can encompass a broad spectrum of definitions based on their personal values, motivations and goals for positive impact (including their financial drivers), advisers can then translate them into actionable strategies for increased positive impact in their clients' investment and philanthropic portfolios. Everyone can then define their impact.

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[1] *The Spectrum of Capital, page 9, Final Report of the Implementation Taskforce, "Growing a culture of social impact investing in the UK." (2019.)*

[2] *Morgan Stanley Institute for Sustainable Investing and Morgan Stanley Investment Management (June 2018)*

[3] *Cambridge Associates press release. (May 2018).*

[4] https://www.blackrockblog.com/2017/04/17/millennials-save-world-retirement/

[5] https://thegiin.org/assets/Core%20Characteristics_webfile.pdf

[6] *Barclays Bank UK PLC and its subsidiary Barclays Investment Solutions Limited."Investor motivations for impact: a behavioural examination!". (July 2018).*

[7] https://impactmanagementproject.com/impact-management/what-is-impact

Impact investment in Asia:
rising trend, lagging reality

Mehvesh Mumtaz Ahmed *www.caps.org*

Mehvesh Mumtaz Ahmed

There are three big ways in which private resources can be harnessed for meeting societal needs: through charitable giving and philanthropy, through corporate social responsibility programmes and through the latest arrival in the marketplace for doing good – impact investing. Impact investing is hip, it's cool, it's innovative and it's very, very understudied and misunderstood.

Impact investment is becoming a staple on the speaker circuit. It's sparking much interest from a financial services industry following the lead of wealthy clients. It even has the likes of illustrious institutions such as Harvard University and the University of Oxford offering courses on how to develop 'business solutions to the world's biggest problems'.[1] But impact investing is also bringing some serious financial muscle to the table. There is some US$502 billion allocated to impact investment worldwide, according to the Global Impact Investing Network (GIIN).[2] To put it into context, this is 11 times the foreign aid flowing to the 15 Asian economies covered by the inaugural Doing Good Index and a third of the cost of achieving the Sustainable Development Goals by 2030.[3]

Impact investment's popularity stems from how well it seems to straddle business and philanthropy. By using financial investments as a vehicle for doing good, it comfortably embraces the double bottom line and embodies the concept of blended value.[4] At a time of great wealth creation but also rising inequality and unmet socioeconomic needs, impact investment has the potential to help close the gap in unprecedented ways, potentially at an unprecedented scale.

Impact investment's popularity stems from how well it seems to straddle business and philanthropy.

In Asia, where wealth is growing faster than anywhere else in the world – the growth rate of Asian billionaires will outpace North America and Europe by a solid 10% over the next few years[5] – one would expect to observe a commensurate deployment of resources towards impact investment. And yet, of the half trillion dollars' worth of assets under management in the impact investment industry, Asia accounts for less than 10%. North America and Europe combined account for 79%.[6]

Reasons for lack of interest in impact investment

One reason for impact investment capturing the imagination but not yet wallets of wealthy Asians is that both large-scale wealth and the concept of impact investment are still relatively new to Asia. While almost all (98%) of next generation high net worth (HNW) and ultra high net worth (UHNW) individuals polled by Lombard Odier were looking to increase their portfolio allocations to impact investment, over half (56%) had yet to make a single impact investment, and a quarter (26%) were unfamiliar with the basics.[7]

Asian investors also often cite a lack of an investable pipeline of social enterprises that can absorb private investment. Interviews of Indonesian and Pakistani investors for an upcoming study by the Centre for Asian Philanthropy and Society (CAPS) spanning six Asian economies pointed to the gap between the ticket size that investors are willing to invest given the costs of screening and due diligence, and the needs and absorption capacity of small, mission-oriented startups. A survey of social enterprises averaging more than 100 responses each from Korea, Japan, Indonesia and Pakistan (part of the same study) shows less than a quarter have received any private investment.

It doesn't help that social enterprises in Asia can be business-oriented nonprofits or mission-oriented businesses, with divergent funding needs requiring a diversity of financial instruments which investors are not yet prepared or equipped to offer. This mismatch between the type of financing needed versus what is available is also evidenced in a study of foundations in Singapore and Hong Kong, which found that social enterprises tend to look for uncollateralised loans while impact investors have a preference for equity investment.[8]

And finally, there is no industry standard for what impact investing means. Even GIIN admits that organisations participating in their surveys have different boundaries for their impact investment portfolios, with some counting ESG investing as impact investing, others classifying development finance as impact investment, and yet others selectively including (or not) green investments.

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Our conversations with investors around Asia have yielded wildly different interpretations of impact investing. Some believe investments into businesses which have any degree of social impact is impact investing, others that only investment into businesses driven by a social mission can constitute impact investment. Some attach the impact investment label only to investments with measurable social or environmental impact, others use the length of divestment schedules as the yardstick to distinguish shorter-horizon commercial investments from longer-term patient capital impact investment.

Along the investment-return continuum, impact investment falls squarely to the right of traditional philanthropy which focuses on social impact with no expectation of financial return. It falls left of traditional commercial investment which focuses on maximising financial return, or sustainable/ environment, social and governance (ESG)/responsible investing which weave in varying degrees of purposive social impact or at least screen out negative social or environmental impact. Between these two ends of the spectrum, the boundaries of impact investment are less clear. In our conversations with, and surveys of, investors from across Asia, there is a great desire to engage in impact investment, but indecision on what that implies for the balance between social return and financial return.

In our conversations with, and surveys of, investors from across Asia, there is a great desire to engage in impact investment, but indecision on what that implies for the balance between social return and financial return.

The challenge for advisers

Is it problematic that this confusion exists? Yes and no. Yes, it is true we cannot get accurate estimates of assets under management that are under impact investment and that grey areas abound in even defining what it is. And yes, the social enterprise ecosystem in Asia is still nascent, and the mismatch between social enterprises' needs and investor offerings persists. On the other hand, none of this is preventing interest in impact investment from growing. In fact, this interest is breeding ideas for how to translate will into action. On the investor front, we observe Korean investors advising investees on how to measure social impact, Hong Kong investors offering high-touch mentoring and guidance, and Indonesian and Pakistani investors experimenting with smaller ticket sizes. Philanthropists are making grant funding available to budding, cash-strapped social enterprises. Companies are offering business expertise or incubation support. Governments have made grants available to startups, and are paying heed to calls for creating an enabling regulatory environment for social startups as evidenced by new laws in Thailand and Indonesia.

The lack of clarity creates a challenge for advisers who, need to bridge the gap between how 'thinkers' are defining impact investment and the much wider range of interpretations the 'doers' are experimenting with. Another challenge is that traditional investment advisers may not be trained in identifying dual impact investments, or have the grassroots reach to access social venture startups. But one thing is clear: there is opportunity for functions servicing impact investment to grow if the right combination of reach, knowledge and talent can be nurtured.

Conclusion

Experimentation and innovation using business tools to address social challenges is widespread and exciting. Some of these initiatives will fail, some will succeed but the evolution of thinking around impact investing continues. The present may be marked by unrealised potential, but the future seems bright.

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Bridging the borders between venture philanthropists and impact investors

Julia Oestreich and Joseph Wirthlin *www.widersense.org*

Julia Oestreich

Joseph Wirthlin

In 2013, there were between 80 and 100 venture philanthropy participants in Europe that provided approximately €278 million to increase social impact throughout the world.[1] However, the European Venture Philanthropy Association (EVPA) has reported that that number has risen to €767 million in 2017 and that the average venture philanthropy organisations' budgets have grown by 9% in the last year.[2] Additionally, the 2018 European SRI Study shows that the volume of impact investments has increased from roughly €8 billion in 2011 to €108 billion in 2017.[3,*]

This is incredible growth, but we believe that social enterprises can be even more effective and productive when venture philanthropists and impact investors work together to fund these projects in innovative ways.

Definitions

Venture philanthropy is 'the application or redirection of principles of traditional venture capital financing to achieve philanthropic endeavours'.[4] Often, financing provided by venture philanthropists is less focused on financial returns and profits and more focused on bringing about social and environmental good. Impact investing can be defined as 'investments made into companies, organisations, and funds with the intention to generate social and environmental impact alongside a financial return'.[5,**]

While impact investors often emphasise that financial returns are equally as important as the social or economic impact of their investments, venture philanthropists focus more strongly on impact results and are willing to take greater risks that may result in financial losses. Venture philanthropy is also more focused on general capital building and is frequently carried out by foundations and private equity firms. On the other hand, impact investing is more focused on traditional private equity, and debt models facilitated by impact investing funds.

Our experience

As an integral part of a worldwide network of venture philanthropists, Wider Sense has been able to develop a unique perspective on the issues that surround social business. One trend that we have noticed is that many social enterprises struggle to move past grant-based funding towards professional investments. In order to maximise the potential good that these enterprises are capable of achieving, we believe that they must have access to proper funding that will both incentivise and catalyse various innovative solutions. This can be achieved as venture philanthropists and impact investors work together, uniting their individual strengths.

Challenges

In 2012, Monitor Group published a report entitled *From Blueprint to Scale* outlining a major funding issue for social enterprises which they called 'the pioneer gap'. This gap occurs when organisations have a clear business solution to a social problem but do not have the means to properly develop or validate it in the marketplace. Because of the early and high-risk stage of these social ventures, investors are hesitant to provide the funds that are necessary to test and refine the product or service as well as the organisation and its governance.[6] Venture philanthropy organisations, on the other hand, have the ability to make valuable contributions at this stage, but have historically been focused on dedicating their funds directly to projects and initiatives that have immediate impact. Pioneers of social enterprises are then left suspended between these two sources of funding and are unable to make their desired impact.

Additionally, we have observed that there is a tendency by many philanthropists to ignore impact investing altogether and lay all the responsibility on the shoulders of the financial industry. However, in our experience it is the close collaboration between venture philanthropy and impact investing that leads to real and innovative solutions.

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Solutions

1: Incubators

One solution to bridge the gap between venture philanthropy and impact investing that is growing in popularity is an incubator and accelerator model that is funded by grant money and/or investor's money. These types of companies are purely focused on making organisations investment ready. This intermediary form of involvement allows many venture philanthropists to continue with their main focus of funding on direct impact and allows impact investors to make sound financial investments that are less risky. Often, incubator investors receive priority status for investing in businesses that successfully develop and scale as a result of the incubators.

An example of this type of solution is the Closed Loop Partners Circular Innovation Accelerator. Closed Loop Partners is an investment fund partnered with some of the largest corporations in the world such as Coca-Cola, Johnson & Johnson and Amazon. The investment fund focuses on building circular economies by investing in better recycling and energy-efficient production methods. The winner of the funds NextGen Cup Challenge is admitted into the accelerator and offered 'access to a network of experts, business and technical resources, and testing opportunities to ensure that their innovations can successfully scale to serve the needs of the industry'.[7] These companies turn into investment opportunities for Closed Loop Partners and its investment partners because the accelerator makes them investment ready.

2: Blended finance

Toniic, an international impact investing network organisation, published an article in 2016 that proposed blended financing as a solution. Venture philanthropists can continue funding early-stage, high-risk and high-impact organisations and projects and impact investors can offer additional funds through equity capital. Through collaboration and measurement, the two parties can better organise and plan a funding strategy for social enterprises that would 'generate a forecast return that meets the investors hurdle rate of return for a given risk profile'.[6]

One innovative application of this solution is the German-based Financing Agency for Social Entrepreneurship (FASE). FASE seeks to bridge this gap by bringing together the entire spectrum of financing to fund social enterprises in a way that meets the goals and expectations of all parties. Not only does FASE facilitate collaboration between foundations and impact investors, it also includes private investors, banks and family offices. The organisation focuses on matching funding sources with the appropriate critical growth periods in the development of an enterprise.

For example, when working with SignTime, a business that provides online sign language translation through an avatar, FASE helped secure a €1.1 million grant from the European Commission to cover much of the production and testing phase. Additionally, the Erste Bank provided an overdraft account to cover the company's working capital and a private investor provided a conditional loan based on the achievement of a predetermined impact goal. More funding came through a €100k investment loan with interest rates dependent on the progress of the enterprise.[7] Each funding method met the expectations of the financier and accomplished the overall goal of providing a social service through a for-profit business model.

A slightly different approach was valuable in the development of Justice42, a start-up that provides online divorce services. Justice42 developed as a spin-off of a social enterprise called HiiL (The Hague Institute for Innovation of Law). HiiL sponsored the company with a series of grants that were able to fund many trials with online tools and with interactions with mediators, lawyers and judges. These grants embodied the role of venture philanthropy. They were high-risk but encouraged an innovative solution to a social problem. When Justice42 approached SI², a Belgian-based social venture fund, it had been verified in the marketplace, and had a well-operated organisation to support the innovative product. The SI² Fund was able to make a sound equity investment in Justice42 because of the previous work done through the philanthropic funds of HiiL. SI²'s investment gave Justice42 the means to scale and provided investors with an opportunity for substantial returns.

Conclusion

Fortunately, there has already been improvement in collaboration between venture philanthropy and impact investing. However, there is still a clear gap in the development of companies between the venture philanthropy grant phase and the impact investing phase. In order to continue making progress in working together, clear communication is imperative. By identifying shared impact goals as a basis for a common impact language, organisations would be able to facilitate more effective collaboration. This type of collaboration has the potential to combine financial tools in innovative ways that support the growth of social and environmental business and increase the effectiveness and productivity of social start-ups.

* *These numbers vary depending on the definitions for venture philanthropy and impact investing according to the organisations that performed the research.*

** *The definitions and understanding of these terms vary among organisations and individuals. These definitions are not universally accepted but suffice for the purpose of this article.*

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[9] *Case Study Social Entrepreneurship: SiMAX Scale-up of a Social Innovation Business Plan, Social Impact, Financing. FASE, 2018, pp. 13–16, Case Study Social Entrepreneurship: SiMAX Scale-up of a Social Innovation Business Plan, Social Impact, Financing.*

Julia Oestreich *is a consultant at Wider Sense where she supports foundations, companies and private individuals in their effort to identify tailor-made financial instruments that help to solve social challenges in a sustainable way. With her experience in impact investing, pay-for-success schemes (e.g. Social Impact Bond) and strategic grant giving, she advises clients along the whole investment cycle from project identification and due diligence to the management of the social investments.*

Prior to Wider Sense, Julia worked at Ashoka, an international support network for social enterprises and was the Impact Investment Manager at Scheuch Foundation where she was responsible for the selection and management of the impact investments.

Julia holds a bachelor´s degree in Cultural Anthropology and Political Science from the University of Hamburg as well as a master´s degree in Public Policy from the Willy Brandt School of Public Policy.

Joseph Wirthlin *is an undergraduate student studying economics at Brigham Young University (BYU) in Provo, Utah, USA. His studies have also incorporated area studies of the Middle East, Arabic and German. As a part of the Ballard Center for Economic Self-Reliance at BYU, Joseph has worked for the last two years to better understand social entrepreneurship and impact investing and is on track to receive the Ballard Scholar for Social Innovation award, demonstrating that he has the skills to make a meaningful, sustainable, and impactful difference. Joseph is currently working as an analyst at Wider Sense GmbH in Berlin, Germany.*

A philanthropist's perspective: how to maximise impact using social impact investment

Katie Fulford-Smith *www.bigsocietycapital.com*

Katie Fulford-Smith

A growing number of philanthropists are exploring innovative ways to maximise the value of their donations by making social impact investments from a Donor Advised Fund (DAF) account. A subset of impact investing, social impact investment is 'intentional … and dedicated to delivering a measured, deep and lasting positive social impact, whilst providing financial returns'.[1]

About the donors:

Donor A has been making social investments for over five years and recently set up a DAF account.

Donor B set up his DAF account over a decade ago and is an experienced philanthropist and social impact investor.

Donor C has been making social impact investments through his DAF account for 15 years.

Donor D set up his DAF account nine years ago. He is a dedicated investor and philanthropist.

Donor E has been making social impact investments through her DAF account for two years.

Editor's Note

DAFs are one form of a giving/social impact investment structure. Others include trusts and foundations, dedicated accounts and social investment intermediaries.

Social impact investment opportunities are wide ranging across the return continuum. Some investments have the potential to deliver significant impact at the same time as targeting market rate risk-adjusted returns. Other social impact investments may require more flexible capital to deliver their intended impact, where target return targets are sub-market or unproved. While investing across the return continuum can help philanthropists better align their investments with their charitable objectives, they are particularly well positioned to make the riskier sub-set of social impact investments where financial return targets are either sub-market or unproven.

Philanthropists also recognise that social impact investment can help social enterprises and charities become more sustainable, and in turn deliver better social outcomes. What's particularly compelling for donors making social impact investments from their DAF account, is the opportunity to reinvest their original donation once it's been repaid. This has the effect of multiplying their original investment as well as the potential to deliver impact many times over.

We have spoken to a range of donors making social impact investment from their DAFs so we can gain insights into their motivations and experiences of investing in this way to help increase their impact and support the causes they really care about.

What was your motivation for setting up a DAF account?

Donor A: I set it up as a mechanism to contribute to the Charities Aid Foundation (CAF) Development Fund.

Donor B: At the beginning of the year it forces you to think – how much am I going to give to charity? It's a good mechanism for disciplined giving.

Donor C: I set up a DAF account around 15 years ago primarily to make donations.

Donor D: I was extremely busy with my career, but I knew that one day I would want to focus more on my philanthropic giving. It made sense to set up the account back then as I would benefit from a good level of tax relief and Gift Aid.

Donor E: I am not a millionaire, but I do give regularly. I think a DAF is a cool way to give to charities and can make my money go further.

What was your motivation for making social impact investments?

Donor A: I see it as a part of my philanthropic activities, rather than my investment portfolio. I believe giving people a hand up is better than just donating.

Donor B: I think that social impact investment offers more hope to society than traditional philanthropy. It helps organisations to become more sustainable.

Donor C: I thought it was an interesting way to make my philanthropic funds go further. In the worst case, in the event that some of the loans were not repaid, I would in effect be making a donation to underlying charities.

Donor D: I was attracted to the recycling of funds, amplifying economic reach and social impact.

Donor E: It just so happens that the charities I would like to support were raising social impact investment at the time.

What type of social impact investments have you made so far using your DAF account?

Donor B: My own account has four equity-type investments and four bond investments. They are all interesting investments, doing noticeably useful work in the local community which is what a charity should be trying to do.

Donor C: Over the years, I have invested in a number of different funds through my DAF account, ranging from lower risk working capital lending, to high-risk development loans, and a fund focused on community housing projects.

Donor D: I am quite early in my social investment journey. I have put money into 1to4 GiftVest and I am now considering a development impact bond.

Donor E: I have made one social impact investment through my DAF account into an organisation that invests in microfinance institutions and organisations active in sustainable agriculture.

How would you describe your experiences so far?

Donor A: Being able to recycle my money is a wonderful thing. My initial investment of £2,500 has provided 98 loans to more than 500 individuals and small businesses. After the loans get repaid, I can re-lend to more people.

Donor B: My experience of lending and investing money is much more rewarding than simply giving money away.

Donor C: I initially made a £1.5m allocation for social impact investment through my DAF account. Since then, the funds have been recycled many times, enabling a total commitment of £6.6m in more than 400 deals.

Donor D: The experience has been positive so far; I am learning and I think social impact investing is an exciting field with lots of opportunities.

Donor E: My experience has been positive so far and I hope to make more social impact investments on a more regular basis later in life. I would definitely recommend other donors to consider using a DAF to make social investment.

What would make it easier for donors to make social impact investments via DAFs?

Donor A: Size of investment is still a barrier, as many opportunities have a high minimum investment amount.

Donor B: The single biggest improvement in making it easy for people is to make them more aware of DAFs. In respect to social impact investment, we don't yet have a fully flourishing marketplace, it's quite immature and nascent and needs to mature.

Donor D: I do think the cost of making social impact investment is high in some cases and I always want to make sure the risk-adjusted impact is worthwhile.

Conclusion

The experiences shared on making social impact investment from DAF accounts were overwhelmingly positive. It's helped donors engage with their philanthropy in different and exciting ways and the most rewarding thing of all is the opportunity to help more people through the recycling of their donation many times over.

It's clear that one of the main benefits for philanthropists choosing to set up a DAF account is to help make the process of tax-efficient giving easier. But while the experiences of the donors we've spoken to has been positive, more can be done to help philanthropists make social impact investments, in part by raising awareness of this growing sector.

Surprisingly, most money held in DAFs is invested with little or no consideration at all for impact. Although traditional investments potentially offer better risk-adjusted returns, they don't intentionally further the social objectives of the donor. In some cases, they may even be in direct conflict with their personal ethics or values. If a donor chooses to make social impact investments, they can achieve a financial return whist staying true to their values and philanthropic objectives.

Professional advisers play an important role in helping their clients navigate the wide range of social impact investment opportunities available. They should help clients achieve their social as well as financial objectives by utilising all the tools available, including social impact investing. By building an understanding of the social issues that their clients are trying to address, advisers will be better placed to recommend suitable social impact investments that can help them maximise their impact.

[1] *UK National Advisory Board on Impact Investing*

Katie Fulford-Smith *is Engagement Manager in the Engagement team at Big Society Capital, with a specific focus on investor engagement. Her role is to help increase the amount of private capital invested into funds delivering positive social impact in the UK, working with a range of investor groups from HNW individuals and their professional advisers to university endowments and pension funds. In 2017, Big Society Capital convened a Donor Advised Funds Advisory (DAF) Council, a collaborative partnership for DAFs who share the same vision to reduce barriers to social investments. With the support of the Advisory Council, this year, she co-authored a guide for philanthropists:* Maximising Your Philanthropy: A guide to Social Impact Investment and Donor Advised Funds.
Prior to joining Big Society Capital, Katie worked in mainstream fund management on fundraising initiatives across a range of institutional fund strategies in private markets including: venture, growth capital, renewable energy and real estate. She also spent several years raising investment into tax-efficient venture capital schemes.

Alternative routes to financing bigger impact and better outcomes for vulnerable children: a case history

Katie Fowler *www.chanceforchildhood.org*

Katie Fowler

In 2018, Chance for Childhood, an international children's charity, embarked on a journey to test alternative routes to financing bigger impact and better outcomes for some of the most vulnerable children in Africa, such as street children, children with disabilities and kids behind bars. We work with visionary community leaders and governments to implement locally relevant justice, education and social protection projects that focus on 'hard to reach' children, both in terms of their complex needs e.g. street children with learning difficulties, and location e.g. urban violent slums.

In the last four years, by working with community-based organisations, local NGOs and civil society, we successfully piloted Uganda's first community-led diversion programme for young offenders. This award-winning project, called Right2Change, forms the cornerstone of our zero-tolerance policy towards children and young people being held in adult prisons, or for indefinite periods awaiting sentencing. The results of this pilot across three remote post-conflict districts have been ground breaking. To date 3,200 children have been diverted from detention, 83% of whom are now receiving legal counsel (from 3% prior to our intervention) and the re-offending rate among our Right2Change model is staggeringly low at less than 1%. This is an enormous triumph when compared to the 42% re-offending rate amongst children and young people in the UK in 2017.

Exploring alternative financing routes

Despite seeing huge success at local levels, we face a roadblock to scaling our activities partly due to this area being under-funded in the development sector and particularly due to a lack of political will in the countries we work. This roadblock has been a huge driver of our decision to explore new routes to financing, scaling and sustaining our work.

Social finance is a rapidly growing industry – the number of social investors is fast multiplying while bi-lateral aid stagnates – OECD estimates there is US$228bn of social impact investment under-management. Many international NGOs are now exploring the possibility of moving down the social investment curve, away from traditional philanthropy and towards impact investment. Large international NGOs are working with investment banks to develop social impact bonds for extremely large-scale programmes which is another form of results-based financing. In other cases, traditional philanthropists are finding ways to recycle their donations by offering repayable finance to social enterprises which can design viable business models or to smaller NGOs that require a boost to cashflow for a capital outlay, such as a construction project e.g. CAF Venturesome.

We knew that we were in no position to develop a social impact bond as our need for alternative finance was not significant enough to justify such a model, but we did feel that repayable finance was an option. Spearheaded by our co-CEOs and our Innovation Lead, we set about researching the social investment space, building our knowledge and developing an understanding of what is being tried and tested in the UK – and what models could be applied to international development, specifically the justice sector. Before long, our networking and knowledge gathering were exhausted, and it was time to put our money where our mouth is.

We looked to access investment to scale our Justice for Children work by developing a business model for the Right2Change community-based rehabilitation and diversion programme. After a few months of intense work-scenario planning with different business models and testing the market with some initial research, we were ready to present our business model to an investor in the form of a social franchise. A social franchise model would allow Chance for Childhood to roll out our proven model of support, while maintaining control over some operational elements that we believed to be essential and most importantly to control quality by limiting the extent to which the model could be diluted down. Of course, we would continue to allow innovation within the model and have a built-in system to ensure successful innovations are rolled out across the franchise.

A social franchise model would allow Chance for Childhood to roll out our proven model of support, while maintaining control over some operational elements that we believed to be essential …

As a small organisation, this process has been revolutionary for us. We now understand that there is a place for social investment and traditional philanthropy to exist side by side to prevent undue gaps in funding and create a more holistic approach to solve problems faced by marginalised children across the world. OECD's 2019 report *The Impact Imperative for Sustainable Development* highlights 'social impact investment not only mobilises private financing to contribute to the sustainability development goals but most importantly, it catalyses innovative new approaches to social economic and environmental challenges'. This assertion certainly summarises the case for Chance for Childhood, in that we would not have explored the merits of a social franchise model without the pursuit of a sustainable business model, driven by our need to attract investment.

There are various financing options to share the risks between the investor and investee and we concluded that a blended finance solution with a Revenue Participation Agreement would be the most effective way to ensure that our start-up costs were covered through grant funding and that our repayable finance would be hedged against our future net revenue. Blended finance has been a really important steppingstone for Chance for Childhood, in managing our risk and also in understanding how complementary philanthropy and impact investment can be.

As both a wealth adviser for over 20 years, and a trustee of Chance for Childhood, Tony Wellby explains: "It has been critical for us to appreciate that impact investment will not replace the reliance that we, and many other important actors working in international development, have on the generosity of pure philanthropists, but rather that there is now a new space where investors can make a huge difference. I would urge my fellow wealth advisers to discuss these options with your clients as social investment will become more and more prominent. I would also encourage philanthropists to think seriously about extending the impact of their support by exploring how their current giving can be complemented by future impact investments."

Conclusion

We anticipate receipt of our first social investment in the Autumn of 2019 and are really excited about what we can achieve in the future!

Katie Fowler *has 14 years of international development experience in both the private and not-for-profit sectors. Since joining Chance for Childhood in 2012, Katie has led the charity's transition to an effective, multi-year grantee of institutional donors and has more recently championed the establishment of Chance for Childhood's first regional office in Rwanda.*

The role of philanthropy and impact investing in unlocking the potential of displaced peoples

Justin Sykes *www.innovestadvisory.com*

Justin Sykes

With the largest ever number of forcibly displaced people worldwide, there is a massive and urgent need for private impact capital to help bridge the humanitarian funding gap and support market-based interventions that offer sustainable livelihoods for people on the move.

A total of 13.6 million people were displaced from their homes by conflict and natural disasters in 2018, taking the global total population of forcibly displaced individuals up to 70.8 million – the largest number at any time since World War II.

Contrary to popular perception, 84% of these displaced reside in developing countries, where resource scarcity is even more acute and the ability of governments to effectively address the needs of these people is fundamentally challenged.

Yet while immense capital transfers are required to help developing countries integrate displaced populations with host communities, developed nations continue to shrink away from the global leadership that this challenge requires.

Globally, a US$5 billion funding gap exists between the UN's requirements and available funds to meet the immediate needs of all displaced people while only 1% of UN Sustainable Development Goals (SDG) funds are directed towards displacement. Irrespective of opinions on donor funding effectiveness, it is clear that traditional development assistance alone cannot address this challenge.

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Social impact opportunities

Philanthropic and impact investing institutions are recognising that increasing displacement trends represent an opportunity for social impact. Through catalytic grants and development-focused impact investments provided to social-purpose businesses that serve, employ or are owned by refugees, funders can create sustainable solutions to the global displacement crisis.

Philanthropic and impact investing institutions are recognising that increasing displacement trends represent an opportunity for social impact.

Network facilitators such as *Innovest Advisory*, *Tent Foundation* and the *Refugee Investment Network (RIN)* are spearheading this new frontier in philanthropy and impact investing. They are serving as a bridge between social impact funders including foundations, family offices, impact investment funds, development finance institutions (DFIs), NGOs, government aid agencies and displacement-inclusive enterprises in host and source countries.

Accordingly, private and public capital is now helping to close these huge funding gaps. One high profile example is George Soros' commitment to invest $500 million via his *Open Society Foundations* (OSF) in companies that serve the displaced.

Access to finance

Key thematic trends are emerging. One is the recognition that displaced people require access to finance in order to rebuild assets and foster long-term self-reliance. However, financial institutions in developing countries often view displaced individuals as too risky. Refugees and migrants are less likely to possess identification, collateral or credit history and they are often considered a flight risk.

Yet evidence from the efforts of initiatives such as the Dutch *NPM platform* and *Kiva.org* is disproving these perceptions.

Kiva's *World Refugee Fund*, is a crowd-lending platform that has distributed $12.5 million in microloans from retail social investors to 15,000 displaced entrepreneurs over the last two years, achieving a 95.5% repayment rate across its portfolio. The Kiva is now seeking to increase its fund to $100 million by 2024.

In the private equity space, efforts are also underway. The Global Displacement Fund, an upcoming $50 million private equity strategy by *Developing World Markets* for which Innovest is serving a dedicated impact advisor, will seek to invest in financial institutions and businesses that serve displaced people.

Use of technology

Another key thematic is the use of technology to overcome physical barriers for displaced people that prevent travel for employment opportunities or accessing essential public services.

Migrant Nations, is a new collaboration of UN agencies, refugee hosting nations and private organisations that aims to harness new digital tools to overcome identification and employment access, securing new pathways to livelihood opportunities for displaced people.

One example of such solutions is WorkAround, a social enterprise founded by a refugee entrepreneur Wafaa Arbash that addresses these access barriers by remotely training highly-educated and internet-connected Syrian refugees in 'micro-work'. This provides highly skilled refugees with fair, dignified work while also serving the growing need of global companies to prepare data for machine-learning algorithms.

In a similar vein, *NaTakallam* is an award-winning social enterprise that offers language tutoring and cultural exchange as well as translation services, delivered by displaced persons and refugees.

Financial innovation

Financial innovation to mitigate risk is also a key priority in this space. Network actors such as RIN and the World Bank are building blended-finance platforms which will seek to crowd in private investment by de-risking commercially-orientated capital with grant funding and concessional finance.

The *Development Impact Bond for Syrian Refugees*, backed by the *IKEA Foundation*, is another innovative approach where private funders will be repaid with a return that is conditional on partner NGOs achieving development targets for refugee training and business start-up in Lebanon and Jordan.

In 2018, Business Fights Poverty launched the *Business and Refugees Challenge* with Innovest Advisory to identify ways to mobilise business action for refugees. Meanwhile, the Tent Foundation has galvanised over 70 companies to support the refugee response beyond charitable contributions, by using their core expertise, resources and stakeholder influence for impact.

The number of enterprises in developing countries who have committed to support sustainable livelihoods for the displaced grows:

- *Pawame*, a Kenyan-based social enterprise distributing solar home systems is creating jobs by distributing its systems and empowering the lives of refugees in Kakuma camp.

- *KIMS Microfinance* has provided over $750,000 in financing to support economic integration of 1,000+ refugees and IDPs in Somalia through business loans and training.
- The First Syrian Exporters Group is a consortium of 10 refugee-owned SMEs based in Eastern Turkey in the ready-made garments sector. Starting from scratch in 2012, these businesses now employ over 1,300 staff, 60% of whom are refugees, the rest being Turkish nationals.

Meanwhile, multinational companies are discovering the business case for refugee investment. Vodafone has brought 3G to Nyarugusu refugee camp, Tanzania, which yields higher returns per user than the Tanzanian average. The camp now has access to digital payments, education and healthcare, illustrating the positive externalities of refugee investment.

Conclusion

As RIN's *Paradigm Shift* report attests, 'it is a tragedy that history provides so few examples of humanitarians and investors working together…it is time for history to stop repeating itself.'

Efforts now underway by this consortium of aligned stakeholders is set to change this narrative.

Justin Sykes *is the Founder and Managing Director of Innovest Advisory, a boutique consultancy firm that seeks to unleash the power of public and private capital to address some of the world's most challenging issues.*

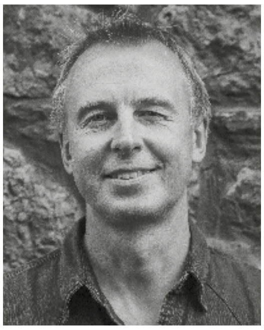
Justin is a social investment specialist with over 18 years' experience in supporting the deployment of private capital to create more and better opportunities for vulnerable populations, often in fragile contexts. These investments have positively impacted hundreds of thousands of lives across a diverse range of countries in Africa and the Middle East. Thematic areas of expertise include financial inclusion, job creation, clean energy access and food security.

His wide-ranging career history has included working for international charities, the United Nations and a major Middle Eastern-focused private foundation. He serves as a board member and advisor to a number of microfinance institutions and international charities engaged in supporting the livelihoods of low-income communities.

He also serves as non-executive director on a developing markets-focused $210-million private equity impact investment fund.

Climate: the defining issue for the next decade

David Hunter *https://bateswells.co.uk/*



David Hunter

Rapid and accelerating change is everywhere – including the investment world. Over the last decade, there has been a steady growth in impact investing, yet it has remained a relatively niche area. As of today that may still be the case, but it is unlikely to be so for long.

Anyone who has not gone cold turkey on the news for the sake of their mental health in the last year will know that, finally, the climate emergency is garnering the attention it demands. Just to recap, in that short time we have had:

- The *IPCC Report* identifying that global warming is likely to reach 1.5 degrees, if we continue to emit carbon at current rates, by 2030
- The UK government legislating to achieve net zero carbon emissions by 2050 and the *report of the UK Climate Change Committee* demonstrating how that might be achieved
- National and local governments, businesses and organisations declaring climate emergencies across the globe
- The Bank of England publishing an *open letter* on climate-related financial risks stating that, "If some companies and industries fail to adjust to this new world, they will fail to exist"
- *Extinction Rebellion* protests and school strikes across the globe demonstrating the scale of public concern around the issue
- Pension trustees being required soon to produce a *Statement of Investment Principles* which sets out financially material considerations (specifically including climate change) over the appropriate time horizons of the investments
- Hot topics for businesses including *'Effective Climate Governance on Corporate Boards'* and '*Managing Transition Risk*'
- The PRA issuing a *Supervisory Statement* for banks and insurers on managing the financial risks of climate change
- *A coalition of charitable foundations* approaching the Charity Commission and Attorney General to seek a ruling on trustees' investment duties in the context of climate change specifically and more broadly in relation to the societal impact of investments by public benefit organisations.

That is a lot happening and is by no means all of it. For the most part, it is not activists, or the left, coming out with this stuff either. This is the political, financial and business worlds beginning to face up to the situation we are in – and doing so because climate is a political risk, a financial risk and a business risk, as identified as long ago as 2006 by *Lord Stern* and by many since from Carbon Tracker and CDP through to the 34 central banks and supervisors comprising the *Network for Greening the Financial System*. It is essential to understand though this is not an issue for the compliance or risk teams to manage in isolation. It must inform attitudes, behaviours and practices across the industry.

For the most part, it is not activists, or the left, coming out with this stuff either. This is the political, financial and business worlds beginning to face up to the situation we are in.

To comply with the Paris Agreement aspiration of limiting warming to 1.5 degrees, fossil fuels have to be left in the ground, while failure to achieve 1.5 degrees will lead to circumstances which will have significant detrimental impact on the value of whole markets and economies. Either way, fossil fuels are no longer a sound long-term investment. The question becomes not if but when to divest, and given the precipitous fall in value when that happens at scale, that is a huge financial risk (regardless of the other consequences of continuing to invest). The 'fail to exist' threat voiced by *Mark Carney* is a real one. In other words, not responding appropriately will not only mean negative social impact, it means negative financial impact too. You cannot disaggregate the social and the financial.

In other words, not responding appropriately will not only mean negative social impact, it means massive negative financial impact too. You cannot disaggregate the social and the financial.

In this context, impact investment begins to seem less of an optional extra – 'the icing on the cake' – and more the means to preserve the cake. It will not be enough to ring-fence a small proportion of a portfolio for social or ethical investment, while continuing business as usual with the vast majority of your funds. It will be necessary to look at all your investments to ensure you are not causing negative climate impact overall.

This is all good news. The regulations and changes in public attitude listed above create an easier environment in which to mainstream impact investing without it seeming peculiar or sacrificial. The opportunities for impact investing are likely to increase too. Much is being made currently of the *Just Transition* and *Green New Deal* which will require lots of capital investment – investment which may bring significant social benefits countrywide and beyond. Already, the cost of renewables infrastructure is coming down significantly, making it an investment free of subsidy dependence. And at the recent Responsible Investor conference in London, there were tales of it being easier to fill a green bond issue than more traditional offerings.

Conclusion

The implications for professional advisers to ultra high-net worth (UHNW) individuals and high-net worth (HNW) individuals are clear. Investment decisions must be viewed through a climate lens. Sometimes this may be directly (i.e. looking to invest actively to reduce carbon emissions), or sometimes indirectly (seeking to ensure investments across a portfolio are not increasing emissions). If advisers do not proactively embrace this change, a combination of clients, regulators and the market will force their hand. It is part opportunity, part threat, and for each adviser to determine how to face this challenge.

David Hunter *is a legal consultant with Bates Wells. His focus is the impact economy, spanning everything from how businesses can flourish whilst acting more responsibly to how the state can improve commissioning of services for the public good; from how investors can achieve social as well as financial returns from their investments to how civil society organisations (whether charities or social enterprises, co-operatives or other forms of social business) can prosper. In the midst of the climate emergency, the sixth extinction and imminent soil and water crises, David is committed to working with organisations actively looking to implement paradigmatic change, not just modest amelioration of the current system.*

What does impact investing really mean?

Alice Millest *https://evpa.eu.com/*

Alice Millest

Impact is a word that has increasingly become part of our professional lexicon, but we still struggle to agree what it means. When developing our understanding of impact investing, we often have lots of questions: Can high social impact go hand in hand with market-level financial returns? What role does philanthropy play in relation to impact investment? Is it possible to robustly and comparably measure the impact of different investments?

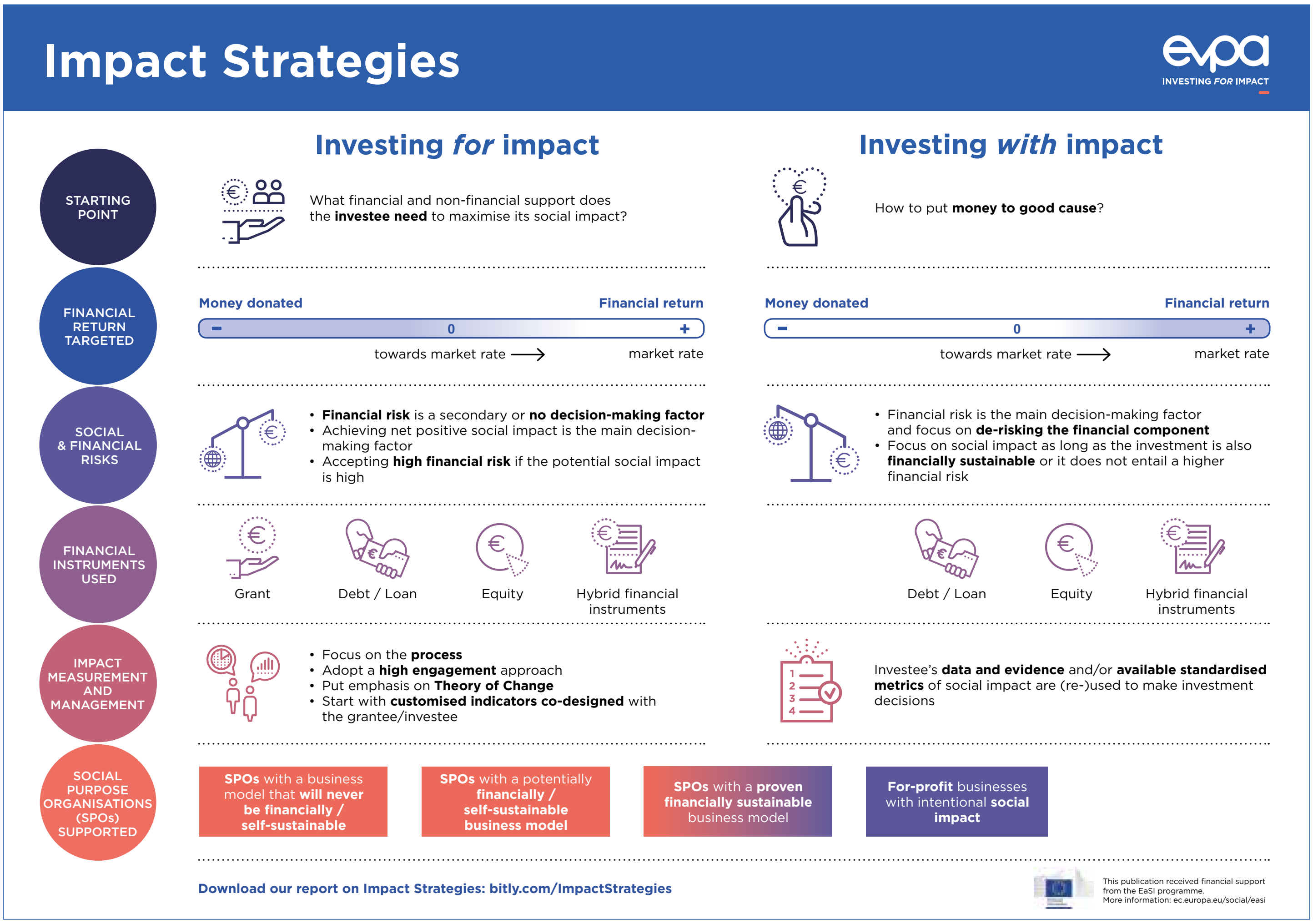
Impact investing has been growing and maturing over the last decade, attracting the attention of an increasing number of people. New resources and capital moving into the sector are great news. The challenge, however, is that the risk-return-impact discussion becomes more blurred, creating confusion amongst both investors and investees and sometimes even disillusions or frustrations due to mismatched expectations and lack of clarity around intention.

The European Venture Philanthropy Association (EVPA) published its *Impact Strategies* report at the end of 2018 as an important step forward in the process of clearing the air around risk, return and impact. It describes in concrete terms the difference between two impact strategies: 'investing for impact' and 'investing with impact'.

Impact investing has been growing and maturing over the last decade, attracting the attention of an increasing number of people. New resources and capital moving into the sector are great news.

What's the difference?

Investing *for* impact means starting with the needs of the social purpose organisation (SPO) and back-engineering which financial instruments are most appropriate to support them. These investors take risks that no other actor (e.g. government, mainstream investors) can take – or is willing to take but are generally deploying relatively small pools of capital. Investors for impact often test – and sometimes scale – new solutions to social issues that have the potential to become financially sustainable. But these investors also have a role to play in supporting SPOs that provide valuable products or services with no commercial market and in building social infrastructures.



Impact Strategies – Visual Overview

(Source: EVPA Knowledge Centre) in Gianoncelli, A. and Bolardi, P., (2018). 'Impact Strategies – How Investors Drive Social Impact'. EVPA.

Investors *with* impact have access to larger pools of capital but need to guarantee a certain financial return on investment alongside the intended positive impact. Investors with impact mainly have a role in scaling proven business models, and in making sure social impact considerations become part of all their investment decisions.

These two strategies commonly interact when investors *for* impact prepare SPOs for investors *with* impact, who can then help them generate impact at scale. Both strategies are valuable and exist alongside one other to support different maturities and types of social purpose organisation. *(See table above)*

Why is clarity important to professional advisers?

We know that ultra high net worth (UHNW) individuals and high net worth (HNW) individuals are increasingly asking their advisers for impact services and products, particularly the rising Women of Wealth and NextGen groups. Although some actors will always look at social impact as a side effect of a financial return, most are increasingly interested in screening investments according to environmental, social and governance (ESG) criteria, assessing the contribution of their investments to the social development goals (SDGs) and in complying with principles of responsible investment (PRIs).

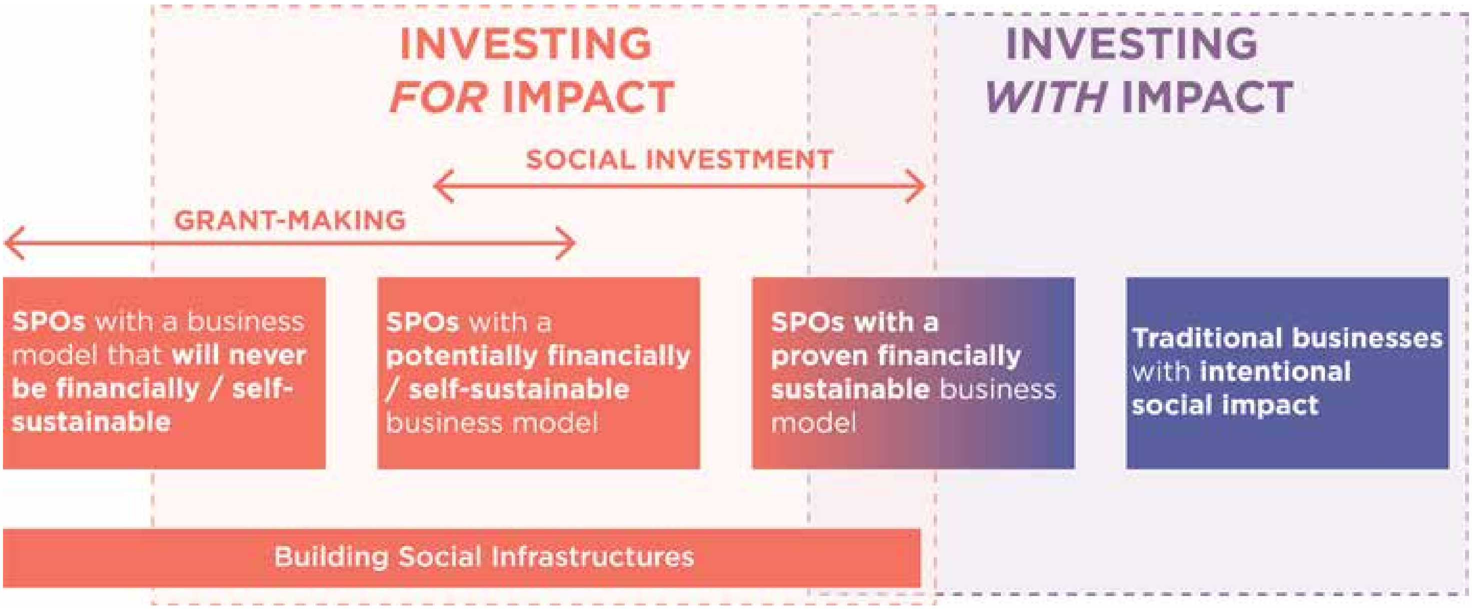


Figure 1
Adapted from: 'Different types of business models for the two impact strategies'
(Source: EVPA Knowledge Centre) in Gianoncelli, A. and Bolardi, P., (2018). 'Impact Strategies – How Investors Drive Social Impact'. EVPA.

Recognising the differences between investors *for* and *with* impact is important to help manage client expectations and clearly articulate their options to them.

How does this fit into the traditional investment-return continuum?

EVPA uses the SPO's potential for financial self-sufficiency to determine the appropriate type of capital and where this activity will fit on the investment-return continuum. An investment being made with the intention of achieving impact, whether as a primary or secondary priority, will be classified as either investing for or with impact. Investments that are ambivalent to their impact will fall outside.

What does the landscape look like today?

The EVPA *Investing for Impact | The EVPA Survey 2017/2018* gathered data from 110 VP/SI organisations across Europe, either focussing exclusively on social return, or seeking a social return alongside a financial one, and adopting the core practices of the venture philanthropy approach (i.e. tailored financing, non-financial support and impact measurement and management). We found that:

- Loans are currently the most deployed financial instrument, followed by grants, equity and hybrid instruments (only 5%).
- The large majority of investors for impact with positive financial return expectations, seek moderated financial returns: respondents deploying equity having expectations not exceeding +10%, and those using debt expecting returns from 0% to +5%.
- Grants are largely preserved to support SPOs at incubation and start-up.

What's next?

Throughout 2019, we will publish case studies, labelled 'investor cards', to show how practitioners have translated their strategies in practice, providing a reality check, showing the elements of their investment activity. Each investor card will be coupled with a success story, featured on *EVPA Success Stories* Website, showcasing practical examples of innovative solutions developed by SPOs, with a specific focus on the way investors for impact contribute to the generation and scale-up of social impact by adopting the venture philanthropy approach.

Conclusion

Let's join forces and build on the momentum in this changing landscape, engaging seasoned players as well as NextGens and all the investors aiming to address and solve pressing social issues.

***Alice Millest** represents the EVPA in the UK & Ireland, and is responsible for building relationships with leaders of foundations and social impact investment funds, philanthropists, advisers and angel investors in this region. Alice began her career in financial services, structuring investments into mid-size European businesses. She transitioned in her mid-twenties to the social investment sector, starting at social finance. She's been working as a freelance consultant across the social enterprise, philanthropy and arts sectors for the last two years with a particular interest in new financial models and venture approaches to social change.*

Join Us

Philanthropy Impact

'I believe Philanthropy Impact has a key contribution to make as a forum to encourage more – and more effective – philanthropy and social investment through the exchange of ideas, spreading knowledge and improving the professional advice available. This is more important than ever.'

LORD JANVRIN Senior Adviser
HSBC Private Bank (UK) Ltd

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- Priority invitation for all Philanthropy Impact events
- Priority for contributing articles for Philanthropy Impact magazine and for speaking at events
- Receive bi-weekly **Philanthropy Impact News** with articles, think pieces and research reports
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- 20% off Alliance subscriptions for Philanthropy Impact members and 10% off individual Philanthropy Impact membership for Alliance subscribers

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- 15% discount on advertising
- 15% discount on event fees for employees and partners who are non-members
- Priority for hosting, chairing, and speaking at events; and for contributing articles for our magazine
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- 20% discount on bespoke training for company employees and partners
- 20% discount on advertising
- 20% discount on event fees for employees and partners who are non-members
- First priority for hosting, chairing and speaking at events; and for contributing articles for our magazine
- Feature the Philanthropy Impact logo in your marketing material

How to *join us*

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