Impact Investing 101

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The Terminology of Responsible Investing

* **Traditional Investing:** Investing to maximize risk-adjusted returns indifferent to the social/environmental impact of the investment or investee activities (‘Amoral’ Investing)

* **Socially Responsible Investing (‘SRI’):** Investing in stocks, bonds of public companies, choosing those that are best with regard to Environmental, Social and Governance (‘ESG’) practices
  * Highly liquid, public securities investing, low intentionality

* **Impact Investing:** seeks to generate measurable positive social or environmental impact along side a financial return. Seeking profit-making commercial solutions to social and/or environmental challenges
  * Illiquid, private investment (direct or fund manager), high intentionality
Liquidity/Intentionality Continuum

- Very Liquid investment in equities/bonds
- Low Intentionality (hard to influence, Impact not likely part of mandate)

**ESG**

Screen broadly for Environmental, Social and Governance policies

**Impact Investing**

Select investments that have a direct impact on positive social change

- Very illiquid investment direct in Cos, or in Funds
- High Intentionality (wired into purpose)
**Responsible Investing, Impact Investing Will be Transformative**

* 83 million Millennials in the US. 76% of Millennials said they consider their investment decisions to be a way to express their social, political and environmental values, and 88% said that a company’s impact in these areas is an important
* They inherit $68 Trillion near term
* $1 in every $4 invested worldwide, is via an ESG framework

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**$68 Trillion Assets in Motion.**

Cerulli Associates projects that nearly 45 million U.S. households will transfer a total of $68.4 trillion in wealth to heirs and charity over the course of the next 25 years.
Seeking Purpose in Your Work, Asserting Purpose with YOUR Money Makes for Harmony

* **Old Approach:** Make money in my job, indifferent to impact, and offset this with Philanthropy – Gifts to address pressing problems that matter to me
  * Discordant - Human Bias of Mental Accounting, Al Capone Example

* **New Approach:** Make money in purposeful work, make purpose-driven consumption decisions and banking/investing decisions
  * Harmony

* **Philanthropy vs Impact:** Do you address the problem once, or in perpetuity?
  * Impact Investing redefines Philanthropy (those situations where money is the only way)
  * Impact Investing allows recurring effort to address a problem
Impact Investing Sits in the Middle of a Continuum

- Impact Investing seeks to generate measurable positive social or environmental impact along with a financial return.
- Seeks profit-making commercial solutions to social and/or environmental challenges.

Source: Case Foundation
Due Diligence - Is the business sound, is the fund manager effective?

Are there competitive advantages, and foreseeable highly probable returns in line with expectations?

What macro forces support or weigh on this investment thesis?

What Impact objectives of mine are met by investing in this business or fund?
The Social/Environmental Menu

Sustainable Development Goals

1. NO POVERTY
2. ZERO HUNGER
3. GOOD HEALTH AND WELL-BEING
4. QUALITY EDUCATION
5. GENDER EQUALITY
6. CLEAN WATER AND SANITATION
7. AFFORDABLE AND CLEAN ENERGY
8. DECENT WORK AND ECONOMIC GROWTH
9. INDUSTRY, INNOVATION AND INFRASTRUCTURE
10. REDUCED INEQUALITIES
11. SUSTAINABLE CITIES AND COMMUNITIES
12. RESPONSIBLE CONSUMPTION AND PRODUCTION
13. CLIMATE ACTION
14. LIFE BELOW WATER
15. LIFE ON LAND
16. PEACE, JUSTICE AND STRONG INSTITUTIONS
17. PARTNERSHIPS FOR THE GOALS
Diversity of Goals – What are Yours?

- Finance First, or Impact First?
- Market Returns or Reduced Economic Returns?
- What Impact Matters to You?
- How Do we Dial In the “Impact” part of Return?
  - How do we measure?
- Passive vs Active?
  - Equity/Debt Public Markets, Funds, Direct (Private Equity/Debt), Deals
  - What are Your Time/Bandwidth Limitations?
Impact Investment Opportunities and Structures

- Impact Enterprises (often “B-Corps”)
  - Companies pursuing social impact and profit by creating jobs, essential goods and services or environmental benefit
  - Can be seed to growth to scale stage of investment
    - With accordant risks
- Sought Outcomes of Impact Enterprises (“Theory of Change”)
  - Creating High Quality Jobs
  - Providing Products or Services that Improve Lives
  - Providing Products or Services that have a Positive Impact on the Environment
  - Generating an Impact Through Supply Chains
  - Creating Replicable Models

A collaborative ethos often distinguishes social enterprises from other for-profit companies.
Impact Investment Opportunities and Structures

* **Impact Funds**

  - Passive investment in a portfolio of businesses. Leveraging the Fund manager to do the due diligence, negotiate terms with Impact Investment prospects, manage and create portfolio diversification

  - Typically LP (Limited Partnership) structure distinguished by:
    - Mission – impact, sector, geography (“Theory of Change”)
    - Stage of Company, Type of Asset Invested in, Type of Capital (debt and/or equity)
    - Targeted Financial Returns
    - Socio-Economic Group/Beneficiary Target
    - Risk/Return Criteria and “Financial vs Impact Return First”

  - Conflicts in Traditional Fee Arrangements Call for Innovation in Structure
Impact Investment Opportunities and Structures

* **Real Assets**
  * Forest, Farmland, Affordable Residential Developments
  * More likely candidates for Foundations and other Institutions
  * Well-suited to sustainability, environmental and affordable housing objectives

* **Pay for Performance Models; Social Impact Bonds ("SIBs")**
  * Improving lives while saving governments’ money
  * Portion of savings returned to investors
  * Objectives include: unemployment, poor student performance, recidivism
  * Also frees up tax dollars for other needs

Ex/Peterborough Bond Deal with Short Sentence Inmates

Reduction in re-offender rate increases payout
We Are at a Tipping Point

- Investment Capital is Part of an the Formula
- Responsible and Collaborative Businesses
- Civic Engagement and Functional Governments
- Social Contract

- Generational Differences Between Current Decision Makers and Future Stewards of Capital, Corporate Leaders, Inheritors/Creators of Wealth

- Additional innovation – This is a Frontier!!
- Where the jobs should/will be
Sausage-Making Issues

* **Measurement of Impact**
  * Is uniformity important, if so, how to do?
  * ie, “how many points of ‘impact’ return”?
  * How do you evaluate across sector, ie, how do you evaluate a Green Energy project in Iowa vs Financial Inclusion project in Kenya?

* **Equitable Return Models**
  * Nothing about us without us
  * ‘Beneficiary’ groups still deal with ‘extraction’

* **Do Market Returns Really Matter?**
  * What are we really solving for, attempting to accomplish?