For Investment Professionals only

Investing for Impact

A guide to positive impact through listed equities

M&G INVESTMENTS

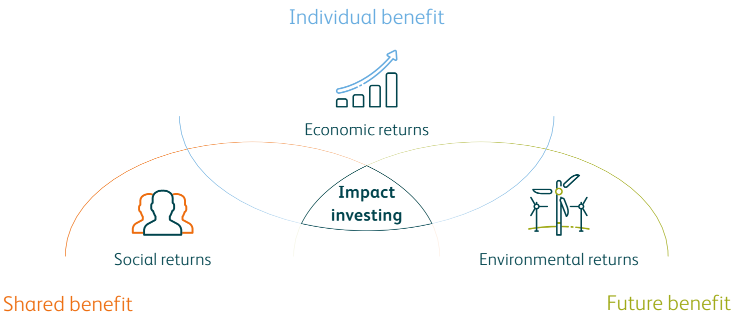
The value of investments will fluctuate, which will cause prices to fall as well as rise and you may not get back the original amount you invested.

What is impact investing?

Listed equity impact investment has the purpose of investing in companies aiming to achieve measurable positive societal impact through addressing the world's major social and environmental challenges, while at the same time producing a financial return. These investments can be made in both emerging and developed markets and target a wide range of impact areas.

The growing impact investment market provides capital to address the world's most pressing challenges in sectors such as sustainable agriculture, renewable energy, conservation and microfinance, as well as affordable and accessible basic services including housing, healthcare, and education. These impact investment areas are increasingly being mapped to the United Nations Sustainable Development Goals (SDGs), which provide a framework against which impact can be assessed and measured.

Figure 1. Aiming for societal and economic returns

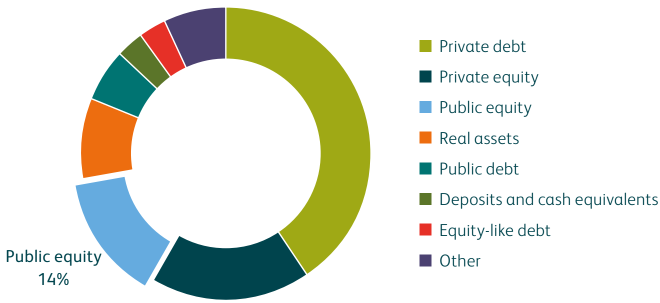


The democratisation of impact investing

Historically, impact investing consisted primarily of private finance to fund specific, impactful projects. Because of this, it has chiefly sat within the sphere of institutional or high net worth investors, with little access for the general public. But that is not to say the demand isn't there. While traditionally impact investment has largely been the reserve of private equity and debt, the impact universe has now extended to include listed equity funds, allowing much greater access for wider categories of investors. Liquid, open-ended investment vehicles can effectively allow for the 'democratisation of impact investing', giving ordinary people a stake in the game.

This is a relatively new development, and listed equity impact investment currently represents a fraction of the overall impact investment universe. However, this is only set to grow, as investors increasingly expect a societal, as well as an economic, return on their investments.

Figure 2. Historically the remit of private equity and debt



Source: GIIN, Annual Investor Survey 2018, total AUMs USD 141bn.

Is impact investing the same as ethical or ESG investing?

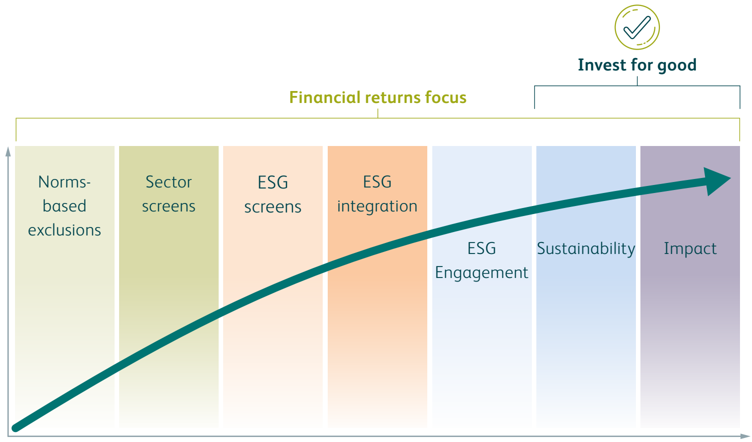
Impact investing is fundamentally different from traditional ethical investing or environmental, social and governance (ESG) investing – even if the difference may seem subtle on the surface.

Ethical investing has been with us for decades, and some would say longer. It had its origins in the Quaker movement and was originally a matter of negative screening, put in place to match the values of individuals or the public institutions and foundations representing them. 'Ethical' funds tended to exclude sectors like tobacco, alcohol, weapons, gambling, pornography, and these days also tend to avoid sectors such as thermal coal, nuclear power or even fossil fuels in general.

ESG investing takes a broader approach and incorporates environmental, social and governance considerations alongside – or within – financial analysis. It looks to integrate such issues as shareholder rights, stakeholder considerations and reputational risk into the investment framework. Often, these strategies still have some basic exclusions, but the focus is on identifying the 'extra-financial' risks and opportunities a company is facing within the more traditional financial analysis.

Impact funds in the listed equities space, meanwhile, need to invest in companies that have the explicit intention of addressing a range of societal and environmental issues the world is facing, again, increasingly framed by the SDGs. Along those lines, there are several areas that Impact investors have to consider, beyond the financial investment case for a business.

Figure 3. A spectrum of responsible investment



Source: M&G, November 2018.

Impact considerations

Intentionality

One element that investors need to consider is the idea of 'intentionality'. This is when a company specifically sets out to deliver a particular impact, with that goal being part of the company's mission statement, strategy and actual day-to-day operations (inadvertent impact doesn't count).

There is also intentionality from the investor's viewpoint; that is, the intention to generate positive social or environmental impact through an investment. To achieve this, investors must actively pick stocks because of their positive impact, rather than screening out companies or picking the least bad from each sector.

Additionality

In traditional impact investing, the 'additionality' of the investment is also considered — identifying and reporting the resultant impact of every pound, euro or dollar invested in a project. For example, a specific amount invested allowed a company to build social housing for 10,000 people, which otherwise would not have been built. This is the additionality of the investment.

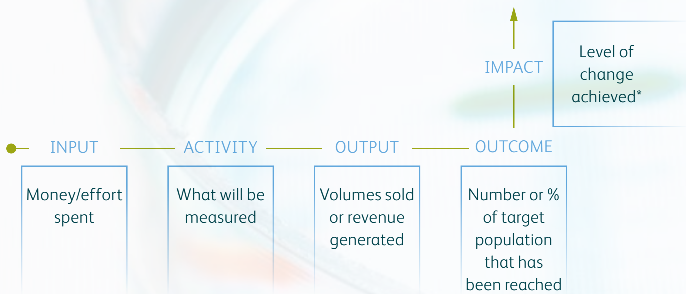
As listed equity impact funds are generally dealing in secondary markets, and the directing of that funding is often not possible, additionality is considered in other ways, generally focused on understanding the additionality of the company. To do that, we might ask how the world would be different if that particular company did not exist or if it were not adequately funded, or how replicable its products or services are.

Measurability

Another key differentiator between impact and other forms of responsible investment is 'measurability'. This is one of the central tenets of impact investing, and also one of its most challenging aspects, especially so for investors in public equity markets where measurement can be less clear. Quality of data and measurability of intangibles are key challenges here, but they need to be overcome for public market impact investors to be effective.

One method to help measure impact at a company level involves feeding analysis into a 'results chain' (figure 4). This framework is used by organisations including the World Health Organisation and the Gates Foundation, allowing the route to impact, and the results achieved, to be mapped from A to Z. This achieved impact can also be mapped against the SDGs, to gain greater insight into its materiality.

Figure 4. The results chain: company specific impact measurement



* Number of people successfully treated or cured, etc.
Source: M&G, November 2018.

Sustainable Development Goals

The United Nations Sustainable Development Goals (SDGs) are a universal call to action to end poverty, protect the planet and ensure that all people enjoy peace and prosperity – its timeframe runs to 2030.

The 17 Goals (with 169 key performance indicators, or sub-goals) build on the Millennium Development Goals, while including new areas such as climate change, economic inequality, innovation and sustainable consumption among other priorities. The goals are interconnected – often, the key to success on one will involve tackling issues more commonly associated with another.

The SDGs also provide a framework for delivering sustainable outcomes, and are increasingly being adopted by both investors and companies as a means of framing their sustainable, or Impact, activities. It is also possible to create specific impact targets focused on key investible impact areas, which can also be mapped against the SDGs. This provides a robust investment and measurement framework, and help impact investors to stay focused on the most pressing issues facing society and the planet we live on.

Figure 5. The UN Sustainable Development Goals (SDGs) framework

Source: United Nations, Department of Public Information.

Figure 6. Mapping investments against the SDGs

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