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The A-Z of Impact Investing

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KEYNOTE INTERVIEW

Why metrics matter for impact investors

Tania Carnegie, leader of the Impact Venture practice at KPMG, on the power of positive impact measurement to drive opportunity

Q What does impact mean for KPMG and why is it important for you as a business?

As a firm, we have been focused on impact investing for almost a decade. We started to see our clients becoming interested in this investment approach in the wake of the financial crisis. They were looking for a deeper sense of accountability, a higher utility to the capital that was being deployed and a greater sense of purpose as to what companies actually stand for.

We saw a movement emerging and we wanted to be sure that, as a business, we were contributing our time, resource and expertise to helping that movement develop.

We also, of course, wanted to help our clients embrace impact with an approach that was appropriate for them.

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Q How much has this movement grown over the past 10 years and how much further do you believe it can grow?

I think the potential is enormous. The impact investment industry is estimated to be worth around $502 billion with more than 1,340 organisations participating around the world. That is clearly still a small proportion of overall invested assets, but – over the past five years in particular – we have seen a tremendous evolution. In fact, the IFC estimates the appetite and opportunity for impact investment to be around $26 trillion, which equates to 10 percent of financial assets globally. Over the past few years, we have seen mainstream finance players getting increasingly involved, from private equity firms launching impact funds to large global financial institutions, banks and wealth managers, specifically tailoring impact products and services for their clients. Now, of course, we are seeing a momentum build around the development of retail products as well. I really think we are just scratching the surface and clients certainly are starting to see this as far more than a niche opportunity. They view impact as transformational and as where the future of investing is heading. That makes this an incredibly exciting space.

Q What – or who – is driving this transformation?

Younger people certainly have a tremendous amount of interest and influence.

That is abundantly clear. But impact isn't exclusively for the younger generation. For example, we see a real interest among the boom generation, matriarchs and patriarchs within our family office clients. This is particularly true for entrepreneurial families who tend to welcome new ideas and opportunities.

From a fiduciary perspective, our institutional clients are keen to capture and enhance returns on their capital, beyond the purely financial. And a lot of experienced company executives are thinking hard about how they invest their money and create a broader sense of purpose within their businesses. The younger generation has a loud voice, but they are not the only ones embracing impact.

Q To what extent are we seeing an advisory ecosystem grow up around the impact investment community?

We are seeing a growing number of boutique impact advisory firms. And then, of course, there are multi-disciplinary firms like KPMG, which are supporting their audit, tax and advisory clients, while also providing an additional impact lens.

One of the things we have really focused on as a firm, is how we can provide our clients with the advice they need to have a rigorous, authentic and credible approach that stands up to the scepticism that is natural in any new and evolving space. We take a lot of pride in helping our clients build trust around their impact approach.

Q Where do the big impact opportunities lie? Is the major focus environmental or are social challenges equally well represented?

I definitely think it's both. I would add that we see an increasing recognition of the link between social and environmental issues. Environmental challenges often influence the social challenges that a community may face. In geographical terms, the spectrum of opportunities is also broad, taking in North America and Western Europe as much as developing markets.

Q Which asset classes are proving most effective for impact investment?

One of the most exciting things about impact investment is that it is an approach that is applicable across all asset classes. In

Private equity turns to impact investment

The ability to measure, monitor and communicate outcomes will prove key, says Tania Carnegie

There has been a significant increase in impact investment activity in the private equity industry in recent years. A number of traditional private equity firms have launched dedicated funds, injecting billions of new capital and drawing in institutional investors that haven't historically been attracted to this area.

According to KPMG's *Enlightened Capital* report, which is based on extensive interviews with both GPs and LPs, many private equity firms are pursuing impact strategies in response to investor interest. Furthermore, this interest is not only coming from obvious prospects such as foundations and health or faith-based organisations, with a natural inclination to consider impact. Mainstream institutional investors including pension funds and corporations are also demonstrating real appetite.

Private equity firms are attracted to impact investment because of an unmet demand for financing solutions to the big problems facing society as well. That presents unique opportunities for both impact and financial returns, and many GPs are using the UN SDGs as a road map.

But there are nonetheless challenges that remain for private equity investors interested in embracing the impact opportunity, not least countering scepticism regarding the legitimacy of the investment approach and concerns about a trade off with returns. Authenticity, transparency and the genuine integration of impact throughout the investment life cycle are critical, and the ability to measure, manage and communicate impact is therefore key.

GPs active in impact investment acknowledge the importance of leveraging existing methodologies for measurement, while still developing their own unique approach aligned to their view of the market, culture and investment expertise.

They are also focused on balancing the ability to measure impact with the additional burden on portfolio company management and internal resource. However, the *Enlightened Capital* report also shows that many are willing to learn together, leveraging the experiences of others to contribute towards a broader impact ecosystem.

addition to private equity, we are also seeing activity in real estate, infrastructure and in the public markets. I think that is very encouraging.

Q What are the big challenges associated with impact investing?

I think the first big challenge is to build an awareness and understanding about what impact investing actually is. As much as it has been growing in popularity as an investment approach, it is still a relatively new concept for the majority of investors.

Of course, that means it represents a tremendous opportunity, but it also means there is a lack of common understanding. People will often have preconceived ideas and I think that is a barrier that we need to address in order to channel as much capital as possible.

There are misconceptions, for example, about whether there is a trade off between impact and financial returns, or sometimes people think that impact investment is only an early-stage opportunity, or is restricted to certain asset classes. And then, of course, there is the challenge of measuring impact.

Q What stage have we reached in terms of the ability to measure impact?

There are a number of approaches that are beginning to be adopted around measurement and management and that is helping to form the basis of a common understanding. But we haven't yet got to the point where we have a widely accepted framework such as GAAP in the accounting world. It is really important, therefore, for fund managers to be clear about their investment thesis and transparent about what they are trying to accomplish and also for investors to be clear about what they are looking for in terms of returns and outcomes.

Q Why is the ability to measure impact so important?

In short, accountability. If you are an impact investor, you are not only interested in making money but also seeing that your invested dollars are helping to influence positive change. That means the ability to demonstrate returns in both financial and impact terms is critical. Certainly, the clients we work with take the view that they are equally important.

There is a heightened expectation of trust associated with impact investing. So, being able to deliver on the promise in your investment thesis, being able to live up to that expectation of trust, is essential. Measuring outcomes is a part of that process.

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Q How important have the UN's SDGs proved in terms of metrics?

The SDGs are incredibly important. They are commonly featured as part of the impact frameworks that our clients are developing. Many are adopting them as a roadmap to help them understand where investment opportunities lie or how their current investment approach aligns. It helps them articulate what contribution they are making to solving the bigger picture challenges that society is facing. The SDGs are really proving unifying.

Q What are the obstacles to a greater ability to measure impact?

I think one of the key obstacles is a lack of expertise. Impact measurement is not new. The public sector and social sector have been measuring impact for many years and there's a great depth of expertise there. But this is still new for the financial community and bringing in some of that expertise is a priority. This is an area where KPMG's experience can really add value.

Q Given the ability to measure and benchmark that we have today, how is impact investment delivering in terms of both returns and impact outcomes?

It is still early days. A lot of the investment activity is taking place in the private markets and so there is not a lot of public disclosure of results. However, there is a great deal of interest from all parties in the ability to be transparent, to be collaborative and to really learn from one another. And while we are not quite there on the benchmarking of specific results, there are other ways to express the results being achieved.

One way impact investment is being assessed right now is through a number of different investor surveys. A key question being asked is whether impact investments are meeting expectations in terms of financial returns and impact.

Those surveys are generally indicating that the answer is yes, those expectations are being met. It is not clear what those expectations are to begin with, of course, but that is one way to get a sense of what is happening.

Q How do you think impact investment is likely to evolve going forward? Can it deliver the impact required fast enough given the urgency of the global challenges it is aiming to address?

I think we will continue to see more and more capital targeting impact investments. There will continue to be an evolution of next generation products looking to satisfy the weight of investor demand out there. With the urgency around climate change and social issues that are being articulated will come real opportunity for investors and for business leaders. It's that articulation of opportunity that will continue to drive the evolution and scale of impact investment. ■