Soundbites

Impact Investing:

the new paradigm for poverty reduction?

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Impact Investing: the new paradigm for poverty reduction?

There is considerable interest in impact investing from a wide range of stakeholders, yet impact investment means different things to different people and this can lead to confusion and misunderstanding. The Global Impact Investing Network defines impact investment as investments made with the intention of achieving positive impact.

> ***"Impact investments are investments made into companies, organisations, and funds with the intention to generate social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets, and target a range of returns from below market to market rate, depending upon the circumstances."***
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> The Global Impact Investing Network

There is a growing recognition that traditional sources of development financing such as official aid and philanthropic grants are not enough to address the scale and complexity of today's global development challenges. Impact investment is becoming a potent, if only partially understood tool in international development.

The amount of money devoted to impact investment is rising. The G8 Social Impact Investment Taskforce reports that "impact investment in international development may turn out to be one of the fastest growing segments of a global impact investment market"[1]. In 2013, about $10.6 billion in impact investments were made and investors intend to commit a further $12.7 billion or 19% more this year. About 70% of the total money is invested in emerging markets with most investors planning to increase their allocation in Sub-Saharan Africa.[2]

But the field is still evolving and little information is available about what can be expected and/or achieved both in terms of commercial returns and development impacts. Although interest is rising, there is still a need to reach a greater common understanding around a number of issues, including the diversity of investment opportunities and investor interest and the significant gaps that persist in terms of demand meeting supply, the challenges of capturing appropriate impact data, and the need to define a clear role for governments/donors.

Matching supply and demand

Committed investment capital is growing. However, a mismatch seems to exist in the market between capital supply and demand. Investors – the majority of whom are looking to invest in growth or mature stage enterprises – report a lack of quality scalable enterprises and a shortage of quality investment opportunities with a proven track record as their key constraint.[3] Yet one of the main barriers to growth for start-up and small and growing businesses is access to finance.

A report published by the Business Call to Action (BCtA) for the United Nations Development Programme (UNDP) states that some of their 94 member companies have "found the promise of impact investment difficult to capture. They have found their innovative models do not always 'tick the right boxes'" and the availability of impact capital is patchy.[4] For example, Abellon Clean Energy, a BCtA member company promoting sustainable energy access in Ghana, has found that "investors are not ready to finance in Ghana what they finance in India."[5]

Some people argue that the success and size of the market do not currently match expectations and levels of excitement.[6] Indeed, little information is available about businesses that reach true scale or evidence about development impact and poverty reduction.

1 Social Impact Investment Taskforce (2014): Impact Investment: The invisible heart of markets, Report of the Social Impact Investment Taskforce http://www.socialimpactinvestment.org/
2 JP Morgan & The GIIN (2014): Spotlight on the Market: the Impact Investor Survey, available at http://www.thegiin.org/binary-data/2014MarketSpotlight.PDF
3 Monitor Institute (2012): From Blueprint to Scale: The Case for Philanthropy in Impact Investing http://monitorinstitute.com/downloads/what-we-think/blueprint-to-scale/Blueprint_to_Scale.pdf
4 Business Call to Action (2014): Breaking Through: Inclusive Business and the Business Call to Action Today – Mapping Challenges, Progress and the Way Ahead http://www.businesscalltoaction.org/wp-content/uploads/2014/09/BCtAImpactReport_BreakingThrough.pdf
5 Ibid
6 Devex Impact (2014): What's next for impact investing: Definitions, measurement and rising expectations https://www.devex.com/news/what-s-next-for-impact-investing-definitions-measurement-and-rising-expectations-83781

Key questions

- Does impact investment have the capacity to reach the poor in developing countries, and in particular in hard to reach areas and sectors?
- What type of returns can be expected for impact investments focused on poverty reduction/bottom of the pyramid market segments and are these in line with investor needs?
- Are there clear gaps in the availability of impact capital in some markets/ geographies and how should these gaps be addressed?
- Can more investors be encouraged to take the 'pioneering risk', i.e. increase investments in early stage, growing businesses? If so, how?
- What other types of market building initiatives are needed to create a strong pipeline of investment-ready businesses?
- What can we learn from existing experience in the UK and other developed economies for investment in emerging markets?

The role of impact measurement to increase transparency

The lack of information and evidence of impact increases uncertainty and risk, and so decreases investor confidence and capital. Improved impact measurement is therefore not a nice-to-have, but is critical for market growth. However, in developing countries, data is less available and there is generally weaker capacity for planning and monitoring.

Investment made by donors or development finance institutions are often tied to specific poverty targets. Poverty levels are complex to measure, so capacity building for those who are responsible for data measurement has to be considered alongside investments made. The need for better and more comparable measures of outcomes, impact and transparency to ensure the sharing of knowledge and best practice that will accelerate the growth of the market, is one of the key recommendations made by the G8 Social Impact Investment Taskforce International Development Working Group.[7]

Key questions

- Who should drive measurement efforts and should businesses that generate social impact be expected to also take on the burden of tracking and reporting that impact?
- What capacity building and market development is needed to support measurement and knowledge sharing?

7 Social Impact Investment Taskforce (2014): International Development, Subject Paper of the International Development Working Group, http://www.socialimpactinvestment.org/reports/International%20Development%20WG%20paper%20FINAL.pdf

The role of government and development finance institutions to catalyse investment and market infrastructure

An increasing number of multilateral and bilateral agencies are committed to the use of private sector capital and innovation to end poverty and boost prosperity in developing countries. And many development agencies are supporting impact investing to drive development outcomes. The UK Department for International Development (DFID) for example, is providing over £100 million over the next decade to foster the development of the market for impact investment in Sub-Saharan Africa and South Asia under the Impact Programme.[8] The Impact Programme (and many other donor initiatives) is offering grant funding alongside investment capital to achieve development goals. And often public sector initiatives are set up to achieve demonstration effects for private sector investments, and partnerships are emerging between development agencies, large multinationals and local companies.

Key questions

- What role does/should government play to catalyse impact investments for poverty reduction?
- What role does grant funding play alongside investment?
- What policy actions are needed to advance the impact investing market?
- Does public sector investment have positive demonstration effects for private sector investments?

Conclusion

Impact investing alone is not a panacea for poverty reduction, and many questions and issues need to be further explored. But it offers great potential for collaboration and partnership between public sector and private sector stakeholders. Alongside activities aimed to improve the business environment in developing countries, impact investing has huge potential to help address development challenges, at a time when it is critical to evolve models further, answer questions and increase transparency and evidence.

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