Reimagine the Purpose of Capital – An Open-source Impact Database for Impact Investment
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1. Introduction

Milton Friedman, a Nobel winning economist, once said ‘The only social responsibility of business is to increase its profits.’ (Friedman, 1970) It has long been assumed that the pursuit of economic growth through profit maximization would spillover to greater social and environmental development.

The 2008 Financial Crisis, however, shows us that the blind pursuit of capital accumulation with no regard to the social and environmental consequences in the long run has traumatizing consequences. Mass unemployment, real estate closures and bankruptcies are just a few examples that impacted billions around the world. As a graduate student in social policy, I have always wondered: Can capital ever achieve a greater purpose?

2. Impact investment – A Game-changer on Wall Street

Having spent years conducting research on sustainable financing and development, I witnessed a potential game-changer in the financial industry, known as ‘Impact Investment’ – an investment strategy that seeks to achieve measurable social and environmental outcomes alongside competitive financial returns (Bugg-Levine & Emerson, 2011). The perfect combination of both financial and social considerations makes impact investment the fastest growing trend on Wall Street.

According to the Annual Impact Investor Survey conducted by the Global Impact Investing Network (GIIN), the impact investing assets under management (AUM) skyrocketed from mere USD 8 billion in 2012 to USD 228 billion in 2018, representing a 2,750% increase in just 6 years! Most of the capital (46%) is invested in emerging markets such as Sub-Saharan Africa, Central Asia and Latin America for better financial access, clean energy and affordable housing. (GIIN, 2018)

The multi-faceted and dynamic market attracts not only the largest development organizations, asset managers, national governments and even social enterprises begin to take interest in this new frontier of investment. For example, in 2017, UBS raised USD 110 million for a venture-capital fund that focuses on gender diverse technology companies. But what are the driving forces behind this game-changing movement?

A few months ago, the Chairman and CEO of Blackrock Larry Fink said that ‘Purpose is not the sole pursuit of profits but the animating force for achieving them.’ (Fink, 2019)

Since the signatory of the Paris Agreement, investors and corporate leaders begin to realize how imminent the threat of climate change is towards business operations and sustainability. With a USD 1.6 to 3 trillion funding gap for carbon reduction, it is of both investors’ and corporate leaders’ interest to consider the impact of their investment (Clark et al., 2018). To this end, they start to wield the power of capital to right the wrong – not just from a social justice perspective but also from a sustainability and forward-looking...
counterpart.

Apart from global challenges, millennial wealth owners, who are expected to own more than USD 24 trillion worth of assets by 2020, plays a crucial role in driving capital towards a more purposeful path (UBS, 2017). According to a recent survey conducted by Deloitte (2016), almost 90% of the millennials believe that corporate success is not only about financial performance. Another survey conducted by the Bank of America (2016) shows that 85% of the millennial wealth owners expressed great interest in impact investing. The growing demand from clients forces conventional financial institutions to look into the ‘impact’ of their investments.

3. The “End of History” Moment for Investment?

Impact investment certainly serves as an exciting turning point for the financial industry. However, we have encountered a major stumbling block that prevents the industry from growing further, which brings us to the problem statement of this paper – the difficulties in impact measurement.

To capture the ‘impact’ part of the investment, rigorous data collection and analysis is required. Yet, the impact measurement practice is still at its nascent stage with several structural problems. Before we dive into the solution for the impact investment industry, we must tackle the following challenges:

3.1. Lack of Common Understanding of Impact

Unlike traditional investment deals with established metrics, such as debt-to-equity ratio, to evaluate asset performance, there is yet a common definition and data points for social and environmental impacts. According to the first-ever Impact Measurement and Management Survey published by GIIN (2017), 58% of the participating asset managers believe that a common set of impact investing principles or guidelines is an important factor in advancing the industry (p.32). Without an objective or standardized data frame, impact investment might risk being a short-term fad that fades away in the next few years.

3.2. Fragmentation of Impact Measurement Industry

The impact measurement industry is also largely fragmented. Because of the long-standing history of environmental sustainability, there is a clear division between environmental and social impact evaluation. Sustainability consultants might be experienced in carbon emission data and social impact professionals might specialize in assessing social intervention – the lack of convergence makes it difficult for impact investors to cohesively evaluate the objectives and outcomes of their investments. In the same survey by GIIN (2017), 50% of the asset managers see the fragmented approach to impact measurement as a significant challenge in the industry.

3.3. Lack of Data and Transparency

While these prevailing measurement frameworks have done a tremendous job in aligning financial and social impacts, the lack of data transparency makes it one of the biggest challenges faced by impact investors. Considered the novelty of impact measurements, it is no surprise that they might not have the resources or manpower to undergo a rigorous data collection and data analysis. Not to mention the fact that a lot of impact investments do not report the impact data of their investments (McCrealess, 2017).

4. Reimagine the Purpose of Capital – An Open-source Impact Database for Impact Investment

Against this backdrop, I would like to put forth a bold yet much needed solution to catalyze not only the impact investment field, but, potentially, the entire investment industry - an open source impact database that transcends geographical boundaries and impact dimensions.

The database is a one-stop shop for investors and impact analyst to get access to metrics and data for social and environmental impacts. With greater impact data availability and quality, impact investment could serve as an opportunity to revolutionize the purpose of capital itself. In response to the aforementioned challenges, I have come up with three essential ideas for the database, including (i) a global impact taxonomy, (ii) an impact baseline and benchmark and (iii) a deal share platform. In the following section, I would discuss the details of each component and how it can unleash the potential of impact capital:

4.1. Global Impact Taxonomy

Giving meaning to capital requires that we understand what the meaning is. The lack of consistency and fragmentation of the impact measurement practice prevents investors from understanding their contribution in a holistic perspective. To solve this problem, I am proposing an impact taxonomy for nation and city-wide investment projects, covering both the environmental and social issues.

The purpose of the taxonomy not only sets a clear direction for impact analysts to identify the impacts of their investments, it also allows asset managers to understand the portfolio and investment products in a more consistent way. With a common understanding of how impact is traced and measured, it is more likely to scale up the industry.

To this end, international organizations like World Bank and United Nations could take reference from the SDGs and the prevailing measurement frameworks to come up with issue-specific metrics, com-
bining both social and environmental indicators that could be easily and directly measured across geographical boundaries.

4.2. Impact Baseline and Benchmark

Now that we understand what the purpose of the capital is, we must consider the impact contributions of investments. After all, impact investment is not just about reporting the metrics, it is about bringing positive changes to the community. The concept of ‘contribution’ is first brought up by the Impact Management Project, a global alliance that seeks to identify the contribution of the investor i.e. the extent to which their activities are responsible for the realized outcomes (Impact Management Project, 2018).

To incorporate this idea into the database, we could leverage national and city-level administrative data to construct a comprehensive baseline and benchmark for each impact metric in the taxonomy. Similar to the approach of global carbon reduction targets, the impact baseline represents the ‘business as usual’ or ‘year zero’ impact performance whereas the benchmark serves as a comparison across taxonomies or geographical locations (Dembek et al. 2017).

With sufficient data, we could estimate the average impact performance of each taxonomy or region and develop an objective benchmark, allowing social businesses to align their impact trajectory along the benchmark, as well as portfolio managers and impact investors to understand and identify investment opportunities along the impact spectrum.

4.3. Deal Share Platform

Setting standards and guideline are not enough – they simply serve as an architecture and foundation of impact investment where investors and asset managers understand the changes that could be attributed to the capital. To grow the impact investment industry, it is equally important to increase the deal flow through information circulation, which brings us to the final component of the database - a deal share platform.

As discussed, data transparency remains a challenge for a lot of investors. With no evidence or track record demonstrating the impact of an investment, the impact investment industry would be nothing more than a marketing campaign (McCreless, 2017). A deal share platform where portfolio managers disclose the impact data of investment deals would then be a great way to solve the challenge. Like stock exchange or data portals, a deal share platform not only holds portfolio companies accountable to their impacts, the information and performance of portfolio companies would also attract more capital and co-investment opportunities between different investors.

5. Challenges Ahead

Cracking the global open-source database is, of course, easier said than done. Our pathway to revolutionize investment not only takes time but also a lot of political will from decision makers, which brings us to the implementation challenges:

- The biggest challenge is the number of stakeholders involved in this proposal. To implement such bold yet much-needed idea, it requires the tenacity and devotion from international organizations like the United Nations, national and city-level governments, scholars and impact investors. Considered the number of stakeholders involved, the consensus regarding what impacts and metrics to be placed in the taxonomy, along with the extent of the benchmark, requires lengthy discussion amongst the actors.

Another foreseeable challenge is the difficulty in information disclosure. Considered the importance of impact data in driving investors’ decisions, businesses might not be willing to consent portfolio managers in releasing impact data. Unlike listed companies that have legal obligations to disclose their ESG performance as an accountability to shareholders, we might face difficulties incentivizing businesses, especially those in the emerging markets, to disclose information.

6. Conclusion: Impact Capital for Collective Prosperity

In the face of threatening global challenges like climate change and food insecurity, impact investment serves as a new wave of capitalism that devotes private capital into socially and environmentally impactful solutions, alongside a favorable financial return.

Despite the 2000% increase in the impact investment volume in the past 6 years, the lack of common understanding of impact, along with the fragmentation of impact measurement practices, prevents the game-changing industry from going further. As a strong proponent of data-driven solutions, I believe that an open-source impact database, composing (i) a global impact taxonomy, (ii) an impact baseline and benchmark as well as (iii) a deal share platform, would be a powerful tool to connect intergovernmental organizations, state governments, private investors and impact analysts for the greater good. Through cross-sector collaboration and commitment to evidence, I believe we could overcome the challenges and unlock the potential of private capital.

As former UN Secretary-General Ban Ki-moon said “We don’t have plan B because there is no planet B” – it is more important now than ever to rewire the purpose of capital for the sake of collective prosperity.
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