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2018 Sneak Peek: What to Expect of Impact Investing

By Abby Schultz • Dec. 29, 2017 9:17 a.m. ET

Impact investing — the strategy of investing in companies with the intent of bettering the environment and society while still earning a market rate-of-return — gained momentum in 2017 amid rising investor interest and high-profile opportunities from the likes of alternative-investment firms TPG and Bain Capital Management.

TPG raised $2 billion for The Rise Fund, a social impact private-equity fund, while Bain launched its $390 million Bain Capital Double Impact fund. Of course there were dozens of less prominent efforts as well, mostly direct investing by wealthy families and increasingly by institutions into small companies tackling specific issues, such as managing forests for sustainable timberland or improving access to healthcare for low-income communities.

There are no hard figures on the total size of the largely privately held market, but last May, the Global Impact Investing Network gave $114 billion as a “reasonable floor”, based on a survey of 209 of the “world’s leading impact investors.” These investors expected to boost the amount of their investments by 17% to nearly $26 billion in 2017, GIIN reported.

So what’s in store for 2018? Penta asked executives at four leading institutions for their thoughts:

Matt Christensen, Global Head of Responsible Investment, AXA Investment Managers:

Matt Christensen, Global Head of Responsible Investment, AXA Investment Managers. *ILLUSTRATION: AXA INVESTMENT MANAGEMENT*

From AXA's offices in Paris, Christensen oversees responsible investing, which includes environmental, social and governance (ESG) strategies as well as €1.2 billion (US$1.4 billion) in impact investments. In 2018, Christensen expects better data on existing impact investments, as well as "better ways to calibrate and present that information" to help educate and inform more investors about the sector. Today, impact investing depends on wealthy investors to share their experiences. Next year, interest from institutional investors will move the sector beyond private equity and into the public markets, Christensen says.

He also expects fund managers to focus on specific impact investment themes in 2018, like gender equality. Some may also take a quantitative approach to selecting public securities. For example, it's possible to measure how a given company is preparing for a low-carbon world. By quantifying these efforts, "we can push that as a key lever in how we construct a portfolio, which will therefore make the portfolio look different," Christensen says. "It's really exciting because it really starts to open up the area of impact investment to take off where ESG has been."

Hugh Lawson, head of ESG & Impact Investing, Goldman Sachs Asset Management:

Hugh Lawson, head of ESG & Impact Investing, Goldman Sachs Asset Management.
ILLUSTRATION: GOLDMAN SACHS ASSET MANAGEMENT

Even as investors increasingly turn to passive investing strategies, many others are beginning to say, "I'd really like to understand more about the kinds of enterprises my capital is supporting," Lawson says. Asking this question, "is a trend that will only continue and asset managers need to be prepared to answer it," he says. "Companies need to be prepared to answer it too," Lawson adds. "A given company makes a product: but customers may want to know how did it make it, where did it make it, how does it treat people who are making it?"

Lawson expects impact investing to grow next year as investors recognize that the "impact edge," is integral to the financial returns they can receive (an edge they can't achieve through passive investing). "You'll see more demand and potentially more supply," Lawson says. The environment will remain a popular investing theme next year, "because people see there's a clear opportunity to make money and have a beneficial effect," he says. In addition to renewable energy projects, investors are showing interest in water efficiency, waste-water treatment, infrastructure and building efficiency.

Andrew Lee, head of Americas sustainable and impact Investing at UBS Wealth Management's chief investment office:

Andrew Lee, head of Americas sustainable and impact Investing at UBS Wealth Management's chief investment office. *ILLUSTRATION: UBS WEALTH MANAGEMENT*

Individual and institutional interest in impact investing will only accelerate in 2018, Lee says. “The challenges that are out there remain just as significant as they were at the end of last year,” he says, citing climate change, health care, education, food security and energy as a particular focus at UBS. “Those are really critical challenges that we think we can address, that private capital can play a role in addressing and where we’re seeing client demand and interest,” Lee says. He expects the real acceleration in the market will be in the solutions asset managers devise to address these issues. “There will be more vehicles, larger vehicles, where specific focus is on addressing these opportunities and achieving returns,” Lee says.

He also expects investors to use their role as shareholders “to really drive change” at companies. “That’s something that has a lot of promise for the coming year,” he says. Hand-and-hand with driving this change will be an effort to improve impact measurement and management data gathering, “not just for reporting issues, but to increase our knowledge about where the gaps lie — to tell us what companies are doing and can do to actively address those gaps.”

Jonathan Firestein, managing director, impact investing, Ascent Private Capital Management, U.S. Bank Wealth Management:

Jonathan Firestein, managing director, impact investing, Ascent Private Capital Management, U.S. Bank Wealth Management *ILLUSTRATION: ASCENT PRIVATE CAPITAL MANAGEMENT, U.S. BANK WEALTH MANAGEMENT*

"Freedom," is Firestein's word for 2018. By that he means freedom for his clients to not compare impact opportunities to financial opportunities elsewhere in the market, and freedom from the judgment of family members who might not understand what investing for social and environmental impact is about. That's a particular worry for younger family members trying to justify their desire to parents and grandparents to improve the environment or alleviate hunger, he says. (U.S. Bank's Ascent unit manages money for clients with at least $75 million in assets). "It doesn't matter what somebody else thinks about your achieved or expected financial returns — it's your money, do what you want to do," Firestein will tell them.

Too often discussions on impact investing center on whether or not you can make money while helping people and the planet. Instead, investors should think about how they want to spend their wealth. Many impact investments earn market rates of return, but investments that earn less yet directly address an issue an investor cares about, are worth considering, he says. That's especially true for clients who know they have enough funds to maintain their lifestyle and to buffer them in the event of another financial crisis. "After you have security and lifestyle taken care of, think about wealth expansion and impact," Firestein says.

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