# Impact Investing – Can We Make Returns and Reduce Inequality?

*Rahul Kapur is a student member of the IFoA working for E&Y in Delhi, India. He believes that Impact Investing provides a win-win for investors and society and that it's worth a closer look by the actuarial profession. In this article, the first of a 3-part series, Rahul introduces Impact Investing and explains how historical returns are higher than you might think.*

Why do we invest? To meet our current and future needs. What if we could use our investments to generate returns and at the same time achieve positive synergies by building a better world?

**The Pandemic and Inequality**

The COVID-19 pandemic has highlighted widespread inequality across a range of factors, from ethnicity to income, around issues such as access to healthcare, employment, technology and health outcome.[1] There are concerns that the pandemic will exacerbate inequality. As a result of national lockdowns around the world, drop-out rates of children from low income families are expected to increase, causing the educational divide to widen.[2] In the USA, black, indigenous and Latino Americans are dying from the virus at a rate at least triple that of whites, according to Amp Research Lab's Color of Coronavirus project.[3] In India, at the beginning of the outbreak, migrant workers, the lowest paid in society, were forced to return to their villages leading to immediate mass unemployment. In many cases, the wealth of affluent people has increased or been preserved by being able to work remotely while their ability to spend was curtailed by lockdowns. According to the Bank of England[4], during the pandemic, 42% of high income employed households in Britain were able to increase their savings whereas only 22% of low income employed households were able to achieve the same. Households that experienced increased savings had 45% more reported income than those that experienced a reduction in savings. Lower-income groups or those working in the gig economy are much more likely to have lost their source of income and rely on government support, charitable organisations and their savings, if any.

**Changing Attitudes**

Across the globe the COVID-19 crisis has forced us to re-evaluate how we live and work and to reconsider our impact on one another and the planet. Many believe that our consumer behaviour will be reset as a result of the pandemic. This may lead to a greater appreciation of the power behind where we invest and save. Is it possible that we may pivot towards more socially and environmentally responsible choices?[5] Now that the fragility of our health and that of the planet is being laid bare, it may be the right time for ***Impact Investing*** to come into the mainstream.

**What is Impact Investing?**

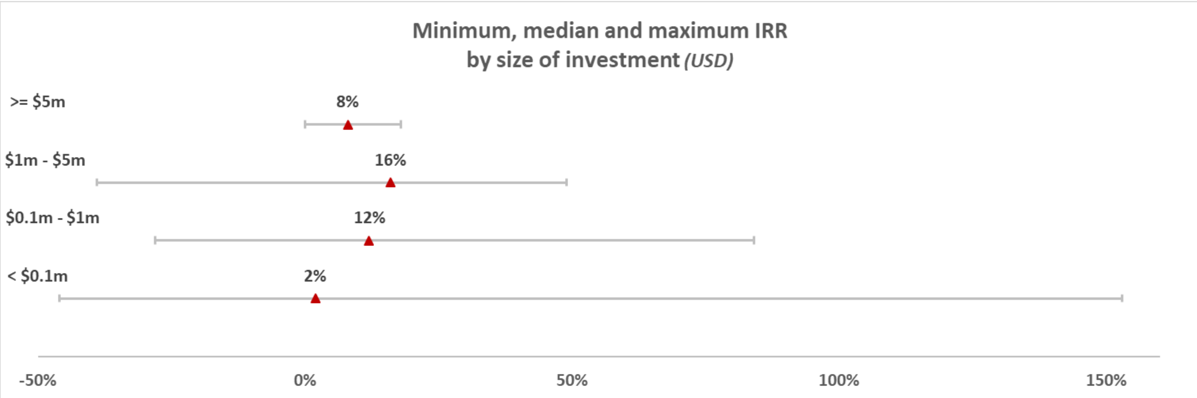
Impact Investing can be defined as investing in the shares or loan capital of companies and enterprises that not only measure and report their wider impact on society — but also hold themselves accountable for delivering and increasing positive impact.[6] Measurement of impact is often performed by reference to the UN's Sustainable Development Goals. The objective is not solely to maximise returns but to make investments in certain sectors which will be beneficial for society and have long term positive impacts. According to the firm Leapfrog Investments, it can be defined as 'Profit with Purpose'.

Investments can be made across various sectors ranging from clean energy, agriculture, financial inclusion, healthcare, microinsurance, affordable housing and education.

Impact investing is not a new concept, but it is often confused with its better-known counterpart focused on environment, social and governance (ESG) factors. The difference comes down to intention; impact investing specifically targets enterprises that intentionally create a positive social benefit, either as a primary or secondary purpose.

**What about Returns?**

According to a McKinsey report[7] 48 impact investor exits between 2010 and 2015 in India produced a median IRR of about 10%. The top one-third of the deals yielded a median IRR of 34%, thus defying views that the returns generated by such social enterprises are not enough to meet the needs of investors or shareholders. It is a myth that such investments generate lower returns. The same report found that those impact investments touched the lives of 60 million to 80 million people in India.




*Source: Impact Investors Council (IIC) survey; VCCEdge; McKinsey Analysis*

**Who invests in Impact Investments?**

Impact investors include pension funds, venture capitalists, NGOs and individuals. Pension funds have found a compelling argument for impact investing, as a means to access diverse opportunities uncorrelated to other assets and generate positive returns in a low yield environment, while also delivering measurable societal benefits in their local area.[8]

Mainstream and bespoke investment managers offer a variety of investments across a range of asset classes including equity, debt, property and other real assets. For example, in November BlueOrchard Finance, a member of the Schroders Group, launched a COVID-19 microfinance impact fund to support micro, small and medium enterprises. The fund is expected to finance 20 institutions, three million micro-entrepreneurs and maintain 60 million jobs per USD 100 million.[9]

**A Case for Balance Sheet Investments**

The evidence highlights that returns do not need to be sacrificed when choosing investments that have a social impact. We know that there are large amounts of capital looking for productive investment opportunities. Impact investment can also bring much needed diversification to a portfolio. Furthermore it may help to win and attract talent, as more and more young professionals choose to work for employers who share their values. All of these realities will endure in a post-pandemic world.

If companies incorporated impact investing into BAU and made the practice mainstream, the effect could be transformational for the impact investment industry. Even if the investment was modest at the company level, the cumulative effect could transform impact investing and the scale of social benefits it could bring.

Quite apart from the scale of the funds in question, their corporate expertise, experience and influence would be brought to bear on the impact initiatives, thus engendering increased confidence of the stakeholders and improving the probability of success. This would help to boost long-term resilience and enable efficient systematic expansion and scalability for these companies and organisations.

If they are investing to have an impact, they will have a long-term commitment that could be beneficial for all the stakeholders involved and for the world as a whole.

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*Footnotes / Bibliography:*


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