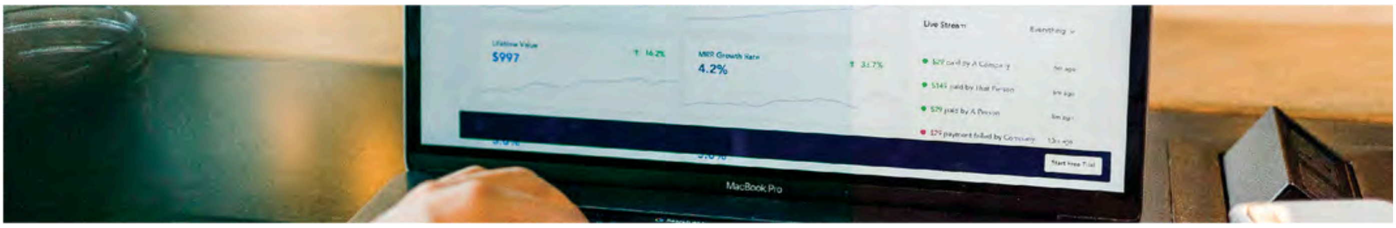
REDEX

Making an Impact: Delivering Social, Environmental and Financial Dividends



REC

Trace, Trade, Trust
www.redex.eco

What is impact investing?

The term 'impact investing' was coined in 2007[1]. Impact investing refers to the strategy and practice of making investments to generate positive social and environmental impact in addition to financial returns. As impact investing balances business with compassion, it appeals to many potential investors[2].

To be characterized as an impact investment, the investment must be measured and reported against the impacts. This is to demonstrate the intentionality and contributions of investors[3]. Other elements of impact investing include expectation of returns, a range of return expectations and impact measurement.

[1] Mudaliar & Dithrich, "Sizing the Impact Investment Market", 11
[2] Rockefeller Philanthropy Advisors, "Impact Investing: An Introduction", 3
[3] Global Sustainable Investment Alliance, "Global Sustainable Investment Review 2020", 7

Characteristics of impact investing[4]

Intentionality:
The investor possesses the intent for the investment to further a positive social or environmental impact.

Investment with return expectations:
There is an expectation for the impact investment to generate a financial return on capital or a return of capital at the very least.

Varying return expectations and diverse asset classes:
Impact investments may aim for below market to risk-adjusted market rates and can comprise various asset classes.

Impact measurement:
The social and environmental impact and financial return of these investments must be measurable for transparency and accountability purposes.

Contribution[5]:
The investor follows a credible narrative, or thesis, which describes how the investment contributes to achievement of the intended goal—that is, how the actions of the impact investor will help achieve the goal. In this case, contribution is considered atthe level
of the impact investor and can take financial or non-financial forms.

[4] Global Impact Investment Network, "What You Need to Know About Impact Investing"
[5] International Finance Corporate, "Creating Impact: The Promise of Impact Investing", xi

Why make impact investments?

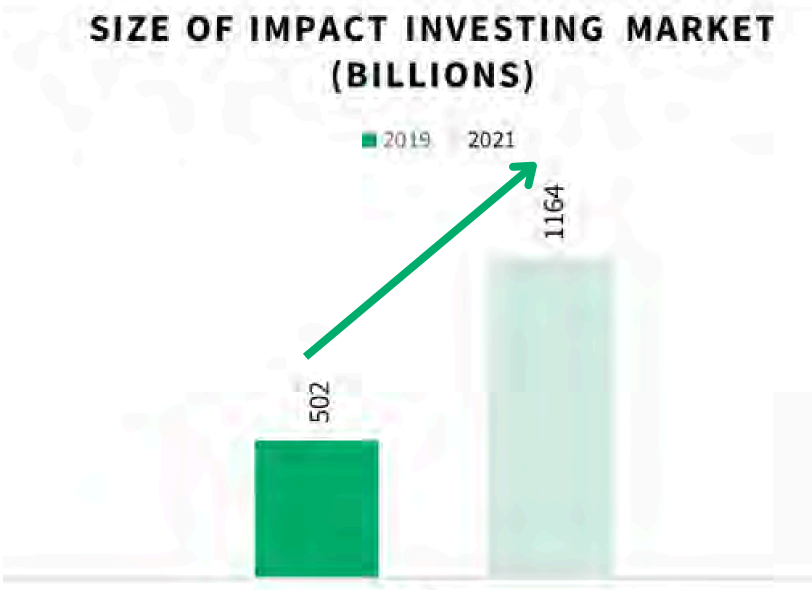
Traditionally, market investments are seen as distinct from social and environmental causes. The former is concerned with financial returns while the latter supports social and environmental goals and are funded by philanthropic donations without the expectation of financial returns.

Impact investing, however, offers opportunities for investors to invest in projects and causes that not only support social and environmental goals, but also earn financial returns. It allows corporates to make holistic use of capital – to advance sustainable development and make a positive difference to their stakeholders while reaping reputational and economic benefits at the same time.

Market and demand for impact investing

Depending on their objectives, investors may make impact investments in both developed and developing countries across a variety of assets and initiatives to achieve social, environmental and financial targets.

According to an estimate by the Global Impact Investing Network (GIIN), an international think tank on impact investing, the assets under management (AUM) of the impact investing market grew by more than 100%, increasing in value to USD1.164 trillion[6] in 2021 from USD502 billion[7] in 2019.



However, this is just a fraction of the market potential and there is much room for growth. The International Finance Corporation estimates that the potential market for impact investing could be worth as much as USD26 trillion[8].

USD26 TRILLION

POTENTIAL IMPACT INVESTING MARKET SIZE

Due to growing awareness of the need to address social and environmental challenges, impact investing has gradually entered the mainstream. It is not unusual for businesses to actively invest in initiatives that tackle sustainability-related challenges not just for financial, but for holistic returns. In an article published in 2022, Forbes shared that “over 50% of active impact investing organizations made their first investment in the past decade[9]”.

[6] Global Impact Investment Network, “What You Need to Know About Impact Investing”
[7] Global Impact Investment Network, “Sizing the Impact Investment Market”, 6
[8] International Finance Corporate, “Creating Impact: The Promise of Impact Investing”, vii
[9] Laker, “Demand For Impact Investing Is Rising. Here’s Why”

A 2020 survey by GIIN indicated that 85 percent of asset managers made impact investments due to client demand[10]. This was backed up in a 2022 study by Bank of America which suggests that demand for sustainable or impact investing is driven, especially by younger people, with 73 percent of those aged 21-42 holding sustainable investments as part of their portfolio (Bank of America 2022)[11]. This was nearly double the rate of 37 percent in 2018. Thus, with appropriate tools and platforms in place, private investors can potentially be major financers of the transition to a sustainable economy.

The increasing emphasis on social and environmental factors in investing connotes a broader transition in the global financial markets — more and more people are cognizant that their funds should be used in a way that transcends monetary gains. Their investments may potentially be used to spark sustainable development that benefits the disadvantaged and the world-at-large, in line with the United Nations (UN) Sustainable Development Goals (SDGs).

[10] Hand et al., “2020 Annual Impact Investor Survey”, 20
[11] Bank of America, “Starkly shifting attitudes amid a historic wealth transfer”

United Nations SDGs

The United Nations adopted the Sustainable Development Goals in 2015 as a universal call to action to end poverty, protect the planet, and ensure that all people enjoy peace and prosperity by 2030[12]. There are 17 inter-connected goals which aim to provide a blueprint to achieve a better and more sustainable future for all[13]. They address global challenges, including poverty, inequality, climate change, environmental degradation, peace and justice.

The UN SDGs are as follows:

Image source: https://commons.wikimedia.org/wiki/File:1._TIMES_17_UN_SDG1.png

More information on the SDGs can be found at https://sdgs.un.org/goals .

The SDGs raise awareness of these global challenges and have advanced the growth of the impact investment market. They also provide context and a useful framework for investors to think about how they can "avoid harm, benefit stakeholders and contribute to solutions"[14], enabling alignment of investment strategies and broader sustainable development goals. According to a 2018 GIIN publication, 42% of impact investors used the SDGs as a barometer for measuring their investment impact[15].

[12] United Nations Development Programme, "Sustainable Development Goals"
[13] United Nations, "Sustainable Development Goals"
[14] https://www.bvca.co.uk/Our-Industry/Impact-Investment/What-Is-Impact-Investment
[15] Global Impact Investing Network, "Roadmap for the Future of Impact Investing: Reshaping Financial Markets", 19

Another useful approach to thinking about the SDGs include their role in boosting impact investing to become a mainstream investment standard instead of a niche market[16]. The SDGs could be a rallying call and catalyze large-scale impact investments by corporates, allowing the market to reach its potential.

The SDGs also serve as a communications framework to describe the relationship between investments and impact goals[17]. Using the SDGs as a framework has enhanced communications with diverse stakeholders, including regulators, clients, and investees, The SDGs articulate goals that are relatable and allow investors to better communicate their contributions to stakeholders.

[16] Global Impact Investing Network,"Achieving The Sustainable Development Goals: The Role of Impact Investing", 9
[17] Global Impact Investing Network,"Achieving The Sustainable Development Goals: The Role of Impact Investing", 1

Impact investing challenges

Despite vast support for the SDGs and strong demand for impact investments, the market is yet to fulfil its potential as several challenges are hampering its development. The challenges include:

Uncertainty of financial returns[18]:
During the infancy of impact investing, investors were less concerned with financial returns. However, as the market grew, new potential investors were also more focused on commercial returns. The potential market is thus discouraged by the belief that impact investments pay sub-par returns.

Impact washing[19]:
Potential investors could be deterred by accusations of "impact washing". Similar to greenwashing, businesses may avoid impact investments due to reputational risks of investing in projects that have difficulty providing measurable and tangible social and environmental benefits. This issue is exacerbated by the absence of a global common standard that encapsulates impact investing.

Absence of common standard for assessing impact:
The lack of common yardsticks for measuring impact made it challenging for investors to make informed investment decisions across projects and allocate funds. This is unlike financial return, which has common accounting standards and practices.

Constraints due to fiduciary duty:
Investors, especially institutional, may be constrained by fiduciary duty which is often consigned to maximizing financial returns. While fiduciary duty is important in protecting capital from reckless or underperforming investment, it potentially discourages investors from considering impact goals.

Lack of impact investment expertise and tools:
Impact investment is relatively new and hence, may face a shortage of expertise and talent, which is exacerbated by a lack of impact investment specific tools and frameworks.

Paucity of investment options and platforms for retail investors:
Now, the bulk of impact investments are made by institutional investors who have the means and resources to conduct due diligence, measure and assess risk and provide capital. Retail investors are left out of the pie due to the absence of suitable products and challenges in accessing this type of investment.

[18] International Finance Corporate, "Creating Impact: The Promise of Impact Investing", 31
[19] International Finance Corporate, "Creating Impact: The Promise of Impact Investing", 14

Solutions to impact investing challenges

So what can be done to mitigate the challenges preventing the growth of impact investing? Potential solutions proposed by the IFC[20] and GIIN[21] include:

Providing evidence that financial returns from impact investing is not inferior to conventional investing:
According a 2017 study by GIIN, impact investors who seek market returns can achieve them[22]. Their analysis reveals that impact investment funds performed similarly to conventional funds. Another similarity between both types was that the choice of fund manager was crucial in determining returns.

Standardising operating principles for managing impact investments:
With standardised operating principles, stakeholders will have a common understanding of the key aspects of how to integrate impact considerations with financial returns during the investment process. A common standard is likely to result in greater transparency in the investments, build trust in the market, and help investors to identify the funds, institutions, and asset managers that pursue impact in a disciplined way.

Developing uniform standards of measuring impact:
Increased transparency is fostered by adopting and utilising a uniform standard for measuring frameworks and tools for impact investments. Impact reporting is thus strengthened, enabling the industry to gain mainstream acceptance and attract more capital. With greater transparency and rigorous standards of measurement, the likelihood impact washing is also reduced.

Regulatory reforms:
Regulatory reforms pertaining to investment policy, and rules related to disclosure and reporting could potentially enable investment managers to consider impact goals in addition to financial returns, while protecting fiduciary duty. Furthermore, to spur investment, tax incentives could be given for impact investments.

[20] International Finance Corporate, “Creating Impact: The Promise of Impact Investing”, 31-63
[21] Global Impact Investing Network, “Roadmap for the Future of Impact Investing: Reshaping Financial Markets”, 38-66
[22] Muduliar & Bass, “GIIN Perspectives: Evidence on the Financial Performance of Impact Investments”, 26

Increasing education and training:
As the impact investment market grows, the need for talent with expertise in this area will grow significantly. To prevent bottlenecks arising from talent shortages that curb growth, tertiary institutions, training institutes and professional organisations should start developing a talent pipeline for impact investment.

Innovating new tools and frameworks:
Modern investment analysis tools primarily focus on financial returns. There is a need for these tools and frameworks to be updated by incorporating impact performance as well.

Developing new products and platforms:
To tap the retail market, new products and platforms must be developed, providing ease of entry for retail investors. In recent years, the explosive growth of digital technology has accelerated the development of fintech and democratisation of data[23]. Riding on this wave of development, new financial products and platforms have sprouted, providing opportunities for investors previously unavailable. For instance, REDEX developed Asia's leading trading platform for renewable energy certificates (RECs).

[23] Global Impact Investing Network, "Roadmap for the Future of Impact Investing: Reshaping Financial Markets", 21

REDEX and impact investing

REDEX developed and operates ***REHash***, Asia's leading trading platform for renewable energy certificates (RECs). It offers a one-stop ecosystem for RECs, supporting clients through the full REC lifecycle – asset registration, verification, marketplace and retirement.

Continuously innovating, REDEX has incorporated an impact investment marketplace on ***REHash***. Through ***REHash***, investors may conveniently select and invest in high quality impact projects that contribute to the sustainable development of communities.

The impact projects on REHash undergo a rigorous assessment process and chosen for potential impact and returns. They allow impact investors to invest in solar projects with strong social impacts. Many times, in geographies or locations where solar projects are developed for energy access, the beneficiaries have no means to make payments for the electricity consumed, resulting in the failure to meet even low internal rate of return requirements of Impact funds. REDEX has developed a novel solution, to use RECs as the main source of long-term returns to support the IRR hurdle of such funds. On the buy side, green corporates may make sustainable claims by offtaking the RECs generated from these projects.

REDEX for your impact investment needs

Leveraging on new technologies and our innovative capabilities, REDEX is providing a new avenue for investors to make impact investments with convenience and confidence.

Contact our representatives for more information on our platform and impact investment projects.

Email:
enquiry@redex.eco

Website:
www.redex.eco