



Why it is important to view impact holistically

This blog reflects on views from the first all-stakeholder event for our new Global Impact Forum, hosted by Charlotte O'Leary and David Brown.

Sponsored by **Aon, Goldman Sachs Asset Management and Tikehau Capital.**

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Views of multiple stakeholders were aired at this event on 16 January 2023. Discussions centred around how impact should be viewed holistically, at systemic, governance and strategy, portfolio, and assessment and measurement levels.

Impact ecosystem

Once pension funds decide to invest with impact, they need support from all stakeholders to act on it. Investment consultants need to rate asset managers on impact and asset managers need to create innovative products. We are in a strange space now, however, where those who are doing nothing get no attention whereas those who are trying often get denounced. Legal firms, asset managers, investment consultants and independent advisers also need to be talking the same

language to ensure a systems-based approach. As well as this, these stakeholders need to provide a minimum level of freely available data.

Communicating impact to pension fund members is also a valuable tool. If members are aware of the positive impact of their pensions, they may be inclined to contribute more money, which, if done earlier and to a greater degree, would have a larger influence on their pension pots than the investment returns.

At a systemic level, it is important to recognise the differences between defined benefit (DB) and defined contribution (DC) in the impact space. In DC, there is a lot of focus on how to minimise costs. Although managers shouldn't use the impact revolution as an unbridled opportunity to increase fees, we must recognise the need for innovation even if it comes with higher charges. Another DC challenge is how asset managers think about

liquidity and how they take high impact investment opportunities in private markets and try to implement them so that they work from a liquidity perspective.

We have heard a lot of noise about DB being 'dead' in the impact space because funds are too close to buyout and we should consider insurers as well. While this is true, we must also look at the liability-driven investment (LDI) crisis and DB schemes' unwinding private markets exposure as potentially creating an opportunity for DC master trusts and local government pension schemes (LGPS) looking for inflation linkage. This, again, highlights the importance of viewing impact investing as an ecosystem.

Impact in governance and strategy

We have had feedback that pension funds are unwilling to say they are – or potentially attempting to – invest

with impact unless they can be confident of positive impact. They want to be sure of the facts first and have a solid framework in place before making any public commitments to stakeholders.

Despite this, there is substantial evidence members want governance owners to implement impact holistically. Research suggests positive impact does not have to be at the detriment of returns.

Although challenges exist with governance budgets, the impact process should integrate trustees, pensions committees, investment committees, third party advisers and asset managers. A suggestion was made that pension funds could even have an impact committee.

Another way impact can be aligned with culture is by ensuring diversity on the trustee board and investment committee.

A successful approach is to embed impact from a



governance perspective and have conversations which change the culture of the organisation. This also translates to how incentives are built. Long-term incentives should match what a fund manager tries to do from an impact perspective and extend beyond the investment management team to business development.

In a more tangible way, impact can be embedded in the pension fund's statement of investment principles (SIP) and through its climate policy. Sustainable development goals (SDGs) or *United Nations* principles for responsible investment (UN PRI) mapping helps with alignment and the *Impact Management Project's* five dimensions of impact can help with execution.

Holistic portfolio impact – public and private markets

Asset owners don't think about boundaries between asset classes in the same way consultants and managers do. So why shouldn't they think about impact holistically, in both public and private markets? After all, every investment they make has impacts, whether positive or negative or both.

The typical DB scheme, because of the LDI crisis, has seen a reduction in allocations to private markets. This is a great reason to start impact investing in public markets. Many investors see private markets as the impact space, and underestimate the power of engagement and stewardship in public markets.

Working with groups like *Share Action*, *Climate 100+* and the LGPS pools, pension funds can leverage collaboration for positive change. For example, through *Share Action*, one pension fund present at this Global Impact Forum event was able to introduce the living wage as a minimum for *Sainsbury's* employees. There are also many examples of pension funds' fruitful individual efforts in stewardship and engagement.

Having said this, when it comes to getting to net-zero, there needs to be £60 trillion of capital allocation to green infrastructure, so we shouldn't underestimate the impact private markets still allow.

The UK pensions industry has assets under management of £3 trillion. With the full scale of that capital and a holistic understanding of the impact investments make, pension funds can move the dial to help address the climate and biodiversity crises.

Holistic impact assessment and measurement

There has been a lot of energy spent on frameworks, regulations, specifications and labelling. This helps when it comes to creating a common language among stakeholders and can assist with measurement. While there needs to be a shared framework for understanding what impact means, frameworks should not stifle innovation. They also don't tell you about organisational alignment or the mission that should permeate all products.

Thinking about impact as a whole – for example not focusing on just intention but positive and negative impact – is paramount to avoid impact-washing. After all, you would get laughed out of the room if you went to talk about financial materiality and only mentioned the positives. To help with this, we must look along the supply chain. It is also important to recognise the potential for investments to deliver positive impact in future.

While understanding climate impact is relatively straightforward, social impact, for example is more complex, and pension funds should work with asset managers and different stakeholders to agree appropriate metrics. We must remain pragmatic and work case-by-case to understand which impacts we want to drive given there is no universal answer.

'It is important to consider, overall, are we making things better or worse? Sometimes we need complexity but it's important not to forget the fundamental objective of impact investing.'

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