Investors’ appetite towards Impact Investing continues to rise, so is their selectivity

A global survey from Vontobel shows that nearly three-quarters of global institutional investors are set to increase allocations to impact investing over the next three years, but “greenwashing” and measurability remain key concerns. Vontobel’s Head of UK and Ireland Sheridan Bowers explains.

Although 2022 was a challenging year for sustainable equity investors due to the market rotation from growth to value that took place, impact investing has continued to rise in popularity among investors in the UK and other markets.

As the sector continues to evolve and mature, investors are increasingly allocating assets to impact and exploring approaches to manage their portfolios toward greater impact. According to the industry body Global Impact Investing Network (GIIN), the global impact investing market is now worth approximately £1tn.

We expect this trend to continue in the coming decades. The intensification of the pursuit of “net zero” emissions economies and the implementation of the UN Sustainable Development Goals (SDGs), among other things, are likely to accelerate this. Our recent impact investing survey of institutional investors in Europe, Asia Pacific and North America shows that seven out of ten respondents are set to increase impact allocations to both public and private markets over the next three years.

Investors increasingly discerning and selective

Impact investors seek to deploy their wealth in a way that benefits the environment and the society, whilst also generating a financial return. Being impact investors for the last 15 years we have seen clients becoming more sophisticated and savvier in terms of sustainability.

Our survey revealed that investors are looking to gain exposure to areas that will last beyond short-term and macro-economic cycles; these are areas that are benefitting from secular structural shifts, such as population growth and technological innovation. We share this long termism as we believe that by investing in companies benefiting from these secular structural shifts creates long-term growth opportunities and strong financial returns, while driving positive change for people and the planet and delivering tangible benefits.

We also believe that impact investing should follow a holistic approach. For example, since energy accounts for most greenhouse gas emissions, clean energy is key to addressing climate change and represents a significant component to reduce the human impact. The overall focus lies on emission reduction with, electricity, hydrogen and heat generated from renewable resources, and technologies enabling a reliable, as well as smarter and greener, grid. In this area, there are six pillars we consider interesting, clean energy infrastructure, clean water, building technology, low emissions transportation, resource efficient industry and life cycle management. We clearly see a growing need for investments in these areas and believe that a “green” transition supported by environmental technologies will benefit the whole society, including investors.

Measuring impact is key for investors

Our survey also revealed that investors want to make sure that they are investing in strategies that do what they say and that enable them to improve the impact they are trying to achieve. They are not only concerned with "greenwashing", but also want to allocate to investment strategies, which are better aligned to their objectives and values.

Measuring the real-world impact is one of the main challenges that clients are facing when choosing such an investment strategy. Our survey indicates that the biggest factor preventing investors from using or recommending impact strategies is the challenge of accurately measuring non-financial performance (54%).

On the one hand, the lack of (quality) data of investee companies makes it difficult to quantifying the impact; on the other, the measurements and their underlying methodologies are still relatively new and are constantly evolving as the industry continues to grow.

Given that measurements are still evolving, in our view, it is also important to apply a wide range of metrics rather than relying on a limited number. For example, to measure the impact of our investments, we provide various quantitative impact indicators. We started with CO_2 as a key metric to measure climate impact. Since 2016 we have further developed that approach and focus on the CO_2 emissions avoided through the use of the company's products and services. Measuring the emissions of the entire value chain allows assessing a potential contribution to achieve the climate goals. To this purpose, we quantify - in cooperation with ISS ESG - the portfolio companies' impact by estimating Potential Avoided Emissions (PAE) from energy efficient products or services. For example, consider a wind turbine; Whereas the carbon footprint during manufacturing (scope 1&2) is significant, over its lifetime a wind turbine helps to avoid approximately 50x more CO_2 that were emitted during the production. To assess such an ability to contribute to climate transition, a holistic approach considering PAE is essential.

As the impact investing sector continues to grow, more players and products will enter the market. Investors can play an important role in steering the industry toward better practices, ultimately resulting in a greater and better impact for our planet. They can do this by partnering with those asset managers who have a proven long-standing experience in the field and that put transparency at the heart of their investment process.