



# MAKING AN IMPACT

Lee Qian, Investment Manager. First Quarter 2018



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## LEE QIAN

### *Investment Manager*

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Lee grew up in China during a period of incredible economic and social progress, when hundreds of millions of people were lifted out of poverty and the standard of living improved for the majority of the population. Witnessing that has influenced Lee deeply about the role of businesses in society.

Lee graduated BA (Hons) in Economics and Management from Oxford University in 2012. Lee joined Baillie Gifford in 2012 and is an Investment Manager for the Positive Change strategy and a member of the Positive Change Portfolio Construction Group.



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*Living standards have risen steadily across the globe over recent centuries. But the future trajectory looks less certain. Humanity needs to find ways in which to address the social and environmental challenges it faces. Back in 1930, the economist John Maynard Keynes recognised how significant the accumulation of capital was in driving progress. But the world has moved on and the recent evolution of impact investing – which has the dual objectives of achieving positive social and environmental outcomes as well as good financial performance – brings even greater potential for the investment community to deliver a more sustainable future for all.*

Traditionally, impact investing was confined to the private market, with initiatives, such as the Ford Foundation's Program Related Investments in the 1960s, often investing directly in targeted projects in local communities. More recently, it has broadened out and is being adopted by investors in the public market. The Dutch pension manager PGGM, for example, has committed to investing at least €20 billion into companies that have a positive impact on areas such as the climate, environment, water, food and health.



## OPPORTUNITIES ABOUND

The World Bank estimated in 2016 that the total market capitalisation of listed companies was US\$65 trillion. Hence, the public equity market offers a larger and more liquid universe in which to find impact investment opportunities than elsewhere. That is not to say that all listed companies are suitable bedfellows for impact investors. However, many do have the potential to make significant inroads into solving some of the issues that are of global impact – companies such as the electric vehicle manufacturer, Tesla, which is driving the adoption of eco-friendly cars, and Safaricom, a telecoms operator that is bringing mobile banking to the masses across Africa.

By investing in the public equity market, investors are increasing the amount of capital that is being funnelled into solving social and environmental challenges. But it is not as simple as finding the ‘right’ companies to invest in. Those who trade regularly in and out of companies in their portfolio have little claim to making an impact through their investments. It takes the patient mind-set and the capital of the long-term equity investor to give companies the freedom and focus they need to deliver on their long-term growth plans and ambitions.

## BRIDGING THE GAP

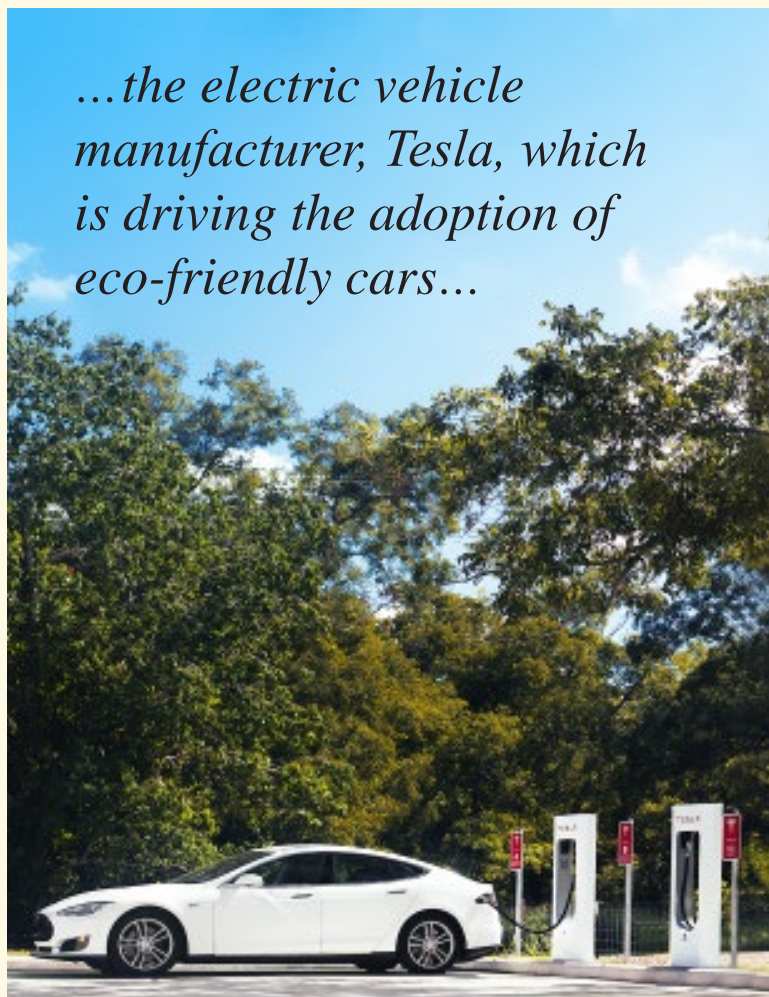
There is a big gap to plug in financing sustainable development. The Brookings Institution – an influential American research group – has estimated that between US\$5 trillion and \$7 trillion of investments are required annually to finance the United Nations Sustainable Development Goals. The good news is that it is not necessarily a one-way flow. The UN’s Business and Sustainable Development Commission has estimated that addressing these goals could open up US\$12 trillion of economic opportunities for the private sector by 2030, with more than half of that in developing countries. This ties in with what the respected scholars, CK Prahalad and Stuart Hart, see as the ‘prodigious opportunity’ to provide solutions and services to the bottom tier of the world economic pyramid – that is, those with an annual per capita income of less than US\$1,500, the minimum considered necessary to sustain a decent life.

In addition, focusing on sustainability issues can help companies to improve their competitiveness through better customer loyalty, lower operating costs and higher employee motivation. Mozaffar Khan and his colleagues at the Harvard Business School found that “firms with good performance on material sustainability issues significantly outperform firms with poor performance on these issues.”

## MEASURING OUTPUTS

Analysing the social and environmental impact of listed companies is a challenge. But it is necessary if impact investing in listed equities is to be seen as a credible and socially acceptable way of allocating capital. Although there are many companies providing data on economic,

*...the electric vehicle manufacturer, Tesla, which is driving the adoption of eco-friendly cars...*



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social and governance (ESG) issues, they capture only part of the picture, especially when it comes to assessing more nuanced areas such as corporate culture and management intent. Reporting companies' impact is also difficult: not all impacts can be quantified and even those that can be are not always disclosed.

For this reason, Baillie Gifford's Positive Change strategy uses in-house fundamental research to examine a company's impact on society, focusing on both quantitative and qualitative aspects. Before making an investment, we conduct an impact analysis which looks at management intent, product impact and business practices. Doing this helps to build a fuller picture of a company's ability to deliver on the dual objectives of achieving positive social

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and environmental outcomes as well as strong financial performance. Likewise, having a long-term investment horizon builds rapport with management teams over time, making it easier for us to engage with them on matters such as impact and disclosures.

## A BRIGHTER FUTURE

Impact investing in listed equities is a new and exciting area for those wishing to contribute their capital to shape a better world. Although there are many challenges ahead for this sector of the market, not least measuring impacts, the long-term benefits for companies, investors and society could be significant. This is neatly summed up by a quote from a piece of work by Michael Porter and Mark Kramer at Harvard Business School, "When a well-run business applies its vast resources, expertise and management talent to problems that it understands and in which it has a stake, it can have a greater impact on social good than any other institution or philanthropic organisation."







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