IMPACT INVESTING

A CASE FOR CLARITY

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In 2007, the Rockefeller Foundation convened a group of investors with a common interest in achieving social change, to think through better ways of measuring social intervention activities. This period is marked by popular consensus as the inception of major global activity on Impact Investing. Prior to this, institutional investments for social and environmental returns were generally measured using anecdotal evidence. In recent times however, there has been a ground swell of activities focused on quantitative evaluation, thereby causing the Impact Investing space to grow steadily into a coherent body of professional and academic discipline. Notwithstanding this remarkable global development in Impact Investing, the concept is yet to gain mainstream attention in many sub-Saharan countries, Ghana included. The risk of delayed adoption at the regulatory level and by mainstream private actors may manifest in weak supply-side support hence moderating the potential influence of social entrepreneurship in addressing social and environmental gaps. A second challenge is the lack of clarity on what Impact Investing really is, with implications for policy design and institutional systems alignment. The import of achieving clarity in terms of definition has more to do with the organizational form and level of activity than on

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nature of activity, particularly on the demand side of the Impact Investing market. In other words, the concern is not just whether or not an organization is achieving measureable social and/or environmental impact but the degree of change realized. It is no brainer that the word “Impact” really means impact and not some minute changes within a local area of operation. The significance of this difference plays out in who qualifies to receive impact capital and support, in order to achieve measureable social and environmental outcomes that transforms an entire value ecosystem.

So What Is Impact Investing?

Global Impact Investing Network (GIIN) a Rockefeller organization dedicated to promoting Impact Investing, defines it as “ investments made into companies, organizations, and funds with the intention to generate measurable social and environmental impact without compromising financial return. Such investments may take the form of debts, equity, mezzanine facilities, project finance or even working capital support. Impact Investing has therefore been classified as an emerging asset class that balances social and environmental returns with financial viability of the investee organization. Like every economic market, there are two sides to it, the supply side and the demand side. Supply-side actors include organizations that play either a primary role or intermediary role. A limited partner, say a hedge fund, that places funds with a venture capital operator for Impact Investing purposes may be classified as a primary supply-side actor or primary Impact Investor whiles the venture capital operator, albeit an intermediary, is also an Impact Investor. Other organizations are foundations, finance institutions, philanthropies and government agencies. The common denominator is the emphasis on measureable social and environmental outcomes as well as financial returns as a basis for capital allocation decisions.

There is usually little controversy in terms of understanding the organizational types that constitutes, actually or potentially, impact investors. This clarity increasingly becomes a luxury when one attempts to define the type of organizations and level of activity, from the perspective on the impact investee organization. From the perspective of an untrained analyst, it may seem intuitive that a typical Non-governmental Organization (NGO), for instance, could be classified as a social entrepreneurship organization within the context of Impact Investing. Nonetheless, it is erroneous to engage in such classification for the simple reason that, a typical NGO business model lacks one key qualification required under Impact Investing; financial viability.

The mere focus on social and/or environmental outcomes is insufficient. An organization must demonstrate commercial viability in order to qualify for impact capital. In Ghana, the main organizational vehicle for achieving social and environmental change is through NGOs that are registered as companies limited by guarantee. In terms of sector distribution, Poverty Reduction and Health/Sanitation seem to top the list, arguably, in terms NGO presence across the ten regions of Ghana. The significance of drawing attention to organization form, relates to the nature of action usually taken by social entrepreneurs to address market gaps, the reason for which they may qualify for impact investment. The implication for an organization's business model in taking direct action to address a market gap spells the difference between commercial viability and financial/philanthropic dependence or between an NGO and a social venture. The entrepreneurial response to a market disequilibria and the potential impact created as a result is determined by the nature of action taken by such entrepreneur. An illustration should clear the fog. Let us suppose three scenarios:

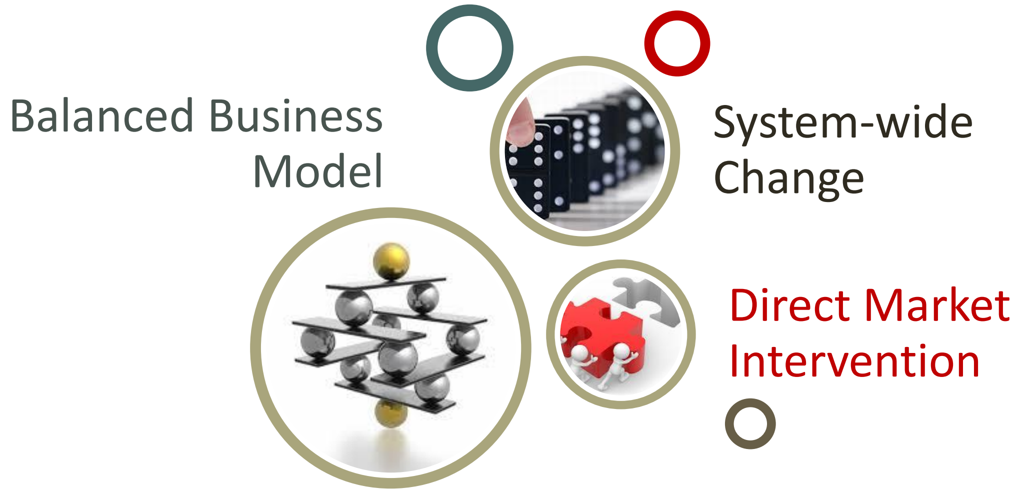
1. Suppose a market in a health sector has achieved equilibrium at a point where patients still feel short-changed due to poor care, unaccountable management systems and apathetic nursing.
2. Suppose one entrepreneur designs a tech-driven solution that can demonstrate measureable reduction in consultation time, improve doctor accountability and provide feedback data on service quality at Out-Patient Departments. Let us suppose further that this entrepreneur is able to market and sell this solution to all the hospitals in Ghana. Clearly, the potential for changing the health care ecosystem and spawning new value chains is tremendous. And all this can be achieved with a significant financial return to sustain operation of this solution.
3. Then, let us suppose that another private actor with good intentions and tons of empathy, decides to set up an NGO in order to train nurses on customer service or maybe advocate for a new law that would hold doctors accountable. Arguably this entrepreneur does not address the problem directly, but seeks to use indirect approach to solve the problem. Now the nature of action will no doubt influence the degree of change achieved, as in the case of the first social entrepreneur.

Impact Investing seeks to align investment capital with the activity of the first social entrepreneur in order to achieve measureable and significant social outcomes. Now there may be other actors that may use indirect action but achieve system-wide change in a manner that rivals that social entrepreneur.

Social and/or policy advocacy groups may be found under this category. Indeed there are examples in Ghana such as IMANI Ghana, Centre for Policy Analysis (CEPA), Institute of Democratic Governance (IDEG) and the like, who take an indirect advocacy approach yet have demonstrable records of social change achieved. Of this category as well, Impact Investing is not concerned. The reason being that their revenue model lacks the principle of independence and sustainability. Another category of organization that may be misclassified as social entrepreneur within the context of Impact investing is what I have termed “The Limited Visionary”. Such organizations have built business models that clearly demonstrates the balance between financial viability and social returns but have been unable to cross the critical volume threshold or lacks scaleability due to its limited area of operation. Solving a fundamental social need that is limited to a particular local or geographical area may achieve limited impact without the benefit of achieving an evolved ecosystem.

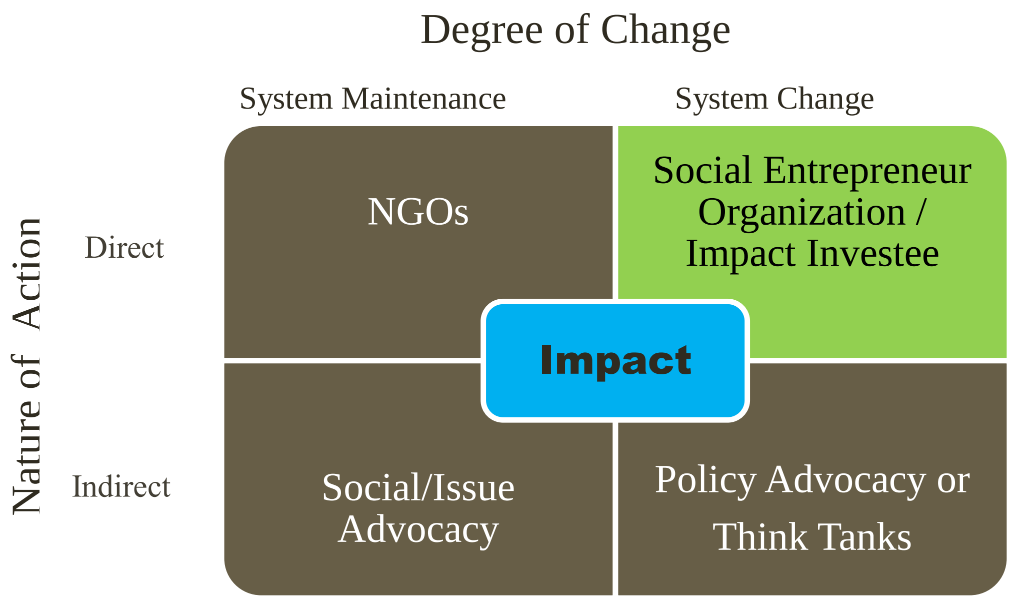
So essentially, the basis of including a private actor into the category of social entrepreneurial organizations, within the context of impact investing, must be done on the basis of three variables; nature of action, degree of change and balanced/sustainable business model.

Fig.1 Key features of a typical social entrepreneur/impact investee



Using this approach for purposes of defining clearly what impact investing is and is not, places all other social interventionists into appropriate categories that helps avoid the temptation to dissipate impact capital on organizations that are neither intervening directly nor achieving system-wide change with their well-intended but limited actions. For such organizations, other funds are available from donor institutions that deal in grants.

Fig.2 - The Social Impact Space



Conclusion and Recommendations

Impact investing as an emerging asset class has come to stay. The increasing committal of funds by international donor institutions to local efforts in Ghana is clearly indicative of growth potential. There are specific issues nonetheless, that must be addressed to remove obstacles to growth. Issues related to conceptual clarity, business model rationalization and outcome evaluations are few of the building blocks that must be iterated in order to improve portfolio quality for impact investors.

Recommendation for Government of Ghana:

1. Public Private Partnerships must be structured to give preferential consideration to social impact actors by emphasizing demonstrable social and environmental benefits as bid requirement for public contracts.
2. Social Investment Fund must re-orient activities to encourage social innovation by partnering with impact investors at institutional level.