Taylor Vinters*

Impact Investment, Intentionality and Innovation

Unlocking financial, social and environmental value for UK PLC

October 2022

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Foreword

Matt Meyer, CEO, Taylor Vinters

When you start to listen to the conversation about impact investment, a conversation that is increasingly mainstream, you realise something.

It is an imprecise conversation.
It is a conversation without consensus.
It is a movement that lacks data.

Whilst the dominant public conversation is that investment should increasingly be for good, the reality is a more complex one.

In commissioning this report, we wanted to sample a range of informed views from a wide stakeholder group. Our research is based on 36 expert interviews with individuals who operate at the sharp end of impact investment and represent interest groups from investment funds and investee companies to industry bodies, networks and academic institutions. What we found was compelling, but also worrying.

The success of impact investment, we found, requires the conversation and activity to become more precise, to build and share data, and to develop a consensus around what the key components of successful impact investment really are. There is a compelling argument for market innovation.

Equally, impact investment is not an island. It is not a particular type of stock or investment model. Instead, it is about the intentionality of the investment activity. Whilst traditional investment activity is largely focused on financial returns, impact investment has the intention of delivering a more complex set of returns. Yes, economic, but also societal and environmental. Economic returns are relatively straightforward for investors to identify, target and measure. That is not the case with impact returns.

Whilst traditional investment sits in clearly defined markets with mature pathways to return, impact investment inhabits a wider but less precise landscape. In most cases that impact investment landscape is inherently entrepreneurial rather than institutional. It is grounded in problem-solving, and it embraces a wider understanding of value creation. To successfully raise finance or invest in this space requires a broader ambition and a shared sense of intentionality. It is not for the faint-hearted.

ESG compliance, we discovered, is often considered by impact investors as a distraction. It is seen as a license to operate in an increasingly conscious world.

Whereas impact is grounded in intentionality, ESG is rooted in compliance and reporting. That is of course a deliberately provocative interpretation, and for some unfair. ESG compliance has brought global corporate actors to the table, but there is a concern that brand ESG sometimes lacks authenticity, and like emission standards, risks ending up in scandal and cynicism, however good the intentions. ESG has a critical role to play but it is not impact investment.

For some, there will be an enlightenment in the realisation that reputation and the contribution that ESG, when done well, can make to it, is in itself a source of huge value creation. The chances are though, that this applies to the minority. The majority will continue to frame ESG as a compliance obligation unless brand ESG is more courageous.

Our hypothesis is that for impact investment to become a prevailing source of positive economic activity in the UK (and beyond), there needs to be market innovation. The following issues need to be addressed:

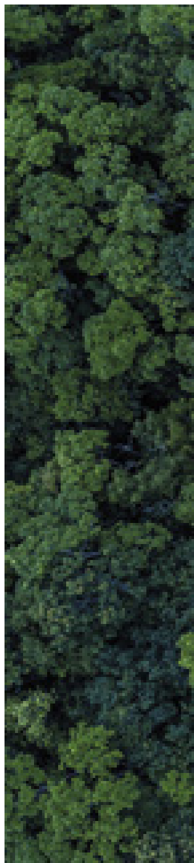
- impact investment needs to be distinguished much more clearly from ESG
- reputational risk and reputational opportunity need to play a more central role in investment decisions
- the science of impact measurement needs to mature, whilst avoiding the ‘analysis paralysis’ that can easily result
- investee companies need to get smarter at demonstrating how impact creates a successful organisation rather than simply how well-funded organisations can create impact
- the impact investment community needs to be better networked.

If we collectively make progress with this agenda, the takeaway from this report is simple. If we can accelerate the rate of innovation in the impact investment ecosystem, we will accelerate the rate of innovation in UK PLC, and possibly beyond.

An investment strategy for UK PLC that fully embraces impact investment could yield extraordinary dividends by delivering innovation, growth and urgently needed solutions to the economic, environmental and social challenges UK PLC faces.

Now is the moment to unlock the potential of impact investment with an exciting set of refreshed possibilities in the investment, entrepreneurial and political communities.

Matt Meyer
CEO
Taylor Vinters



Introduction

The approach and focus of analysis

The intention of this research was to create a state of the nation assessment of impact investment from the perspective of stakeholders operating in the impact space.

By listening to the opinions and experiences of a cross section of experts in impact investment, the report provides a candid and authoritative view of the UK's impact investing ecosystem in 2022, as well as investigating and identifying how the rate of innovation in this ecosystem can be accelerated in the years ahead.

The logic behind the research was simple: the best way to develop an up-to-date understanding of impact investing is to have detailed conversations with a diverse range of experts representing investors, investee companies and well-known public bodies working within the impact sector.

The qualitative information contained within this report has been obtained from 36 video interviews. Each hour-long interview was undertaken by John Knell, a leading business writer and strategy consultant on the changing face of work and organisations, with support from Taylor Vinters' impact lawyers.

John has authored numerous reports on work, the labour market, organisational change, and arts and cultural policy and is co-author (with Richard Reeves) of the international best-selling business book, 'The 80 Minute MBA'.

Chapter One

Impact investment in the entrepreneurial landscape

Section 1.1

How to define an impact venture – intentionality to the fore

The starting point of the research was to establish the definition of an impact venture.

The key feature identified is a clear intentionality to create impact. Impact ventures have founders able to articulate what challenges they are trying to solve, the positive impacts they are seeking to produce on people and/or planet, and how that impact can scale to create meaningful and sustainable impact through a profitable business.

The importance of emphasising ‘intentionality’ was threaded through all interviewee responses to the question, from both founders and investors alike. They expressed an avowedly outcomes-based focus on ‘intended impacts’ in the real world.

Interviewees talked about how impact investors are on the hunt for ‘solution seeking’ investments – i.e., those that support positive, intentional impact from products and services that demonstrably make the world a better place in an environmental and/or social dimension.

For impact investors, the realised impact must be an integral part of the investee’s business model. Specialist impact investors therefore, by definition, seek solutions, intentionality, and measurability as non-negotiable features of their investments.

In addition, whilst traditional investment sits in clearly defined markets with mature pathways to return, by necessity, impact investment is considered to inhabit a wider landscape. In most cases, that landscape is perceived as inherently entrepreneurial, rather than institutional. One that is grounded in problem-solving and embraces a wider understanding of value creation. Therefore, to successfully raise finance or invest in this space, requires a broader ambition and a shared sense of intentionality. But one not without rigour and precision.

Section 1.2

Intentionality facilitates a lock-step investment approach

In the case of the majority of experts interviewed, the way in which they seek to put into practice impact intentionality aligns them with what Bridges Ventures (a privately held, family-owned investment company) has called a lock-step approach to impact investment.

As Bridge Ventures observes in its 2016 Annual Impact report

> *We look for investments where all business success factors are impact success factors. We call this a 'lock-step' business model. When we invest in for-profit businesses, this lock-step is vital to ensure that there is no risk of the company losing its impact focus as it grows, or that its impact focus acts as a barrier to growth.*[1]

The consensus arising from the interviewees is that impact investors are looking for founders who can clearly describe how their business will generate impact. Founders need to show how evidencing impact is core to the venture in terms of driving growth and innovation and influencing key strategic and operational decisions.

Market clarity for these impact investors comes from the clearly expressed intentionality of their investment purpose, operationalised through an impact and finance lens rather than through a badged affinity via generalised compliance activity.

> **I think it is important that we don't lose sight of the fact that we're looking at impact, both because it matters for its own sake, but crucially, it's got to deliver value to the business and be aligned with commercial success.**

Lisa Barclay, Executive Director of Investments at Nesta

1. Bridges Ventures (2016) 'Annual Impact Report' - https://www.bridgesfundmanagement.com/wp-content/uploads/2017/02/Bridges-Ventures-Impact-Report-2016-screen.pdf

Section 1.3

Scalable, long-term value

The research established that some investors have moved to a position in which impact is an essential indicator of sustainable value. At a time of change in an uncertain world, impact has become a long-term indicator of worth.

As Dr Katharina Sommerrock, Head of Investor Relations at Lightrock, explains:

> *“We believe that the companies solving today’s problems will be the most valuable tomorrow. We invest because we want to help solve these problems as an investor.”*

For a growing number of investors, an investable proposition that has a clear, intended positive impact on the environment or people’s lives is a highly relevant proxy indicator of long-term value. In this respect, a number of interviewees talked about new pressures on the investment thesis of fund managers.

They point out that widely recognised influences (such as global warming, Black Lives Matter, MeToo, pandemics and inequality within societies) are creating a strong tail wind for impact investment and inevitably challenge leading VCs to update their thesis of how the world is now, and how it might be in the future. Interviewees suggest that impact considerations will strengthen in the next decade when judged from a consumer perspective, a founder perspective and an investor perspective.

As a result, there is no surprise that the growing influence of impact is already bringing bigger investment fish into impact waters. Many will be familiar with the ‘finance-first’ to ‘impact-first’ spectrum of capital popularised by the Impact Investment Institute,[2] and the experts provided their views from all points across this spectrum. A number of interviewees talked about how the financial return opportunities from highly intentional impact investments are enormous.

As Sam Gill, Co-founder and COO of Sylvera, comments:

> *“Some of the world’s largest, most structurally important businesses will be built in climate. And they will be backable by top tier funds, and top tier funds should be chasing those returns.”*

This challenges any misconception that investors are financing impact ventures for purely philanthropic or altruistic reasons. The return on investment can be financial plus social and/or environmental.

2. https://www.impactinvest.org.uk/wp-content/uploads/2020/11/Spectrum-of-capital-general-version.pdf

Section 1.4

Profit positive: moving the dial on the world's biggest challenges

The research indicates the need to let go of the view that impact investing is, and will remain, the preserve of smaller, boutique and specialised investment houses. This is supported by the fact that heavyweight American private equity investors, including Apollo, KKR, Bain and TPG, have entered the field of impact investing with funds targeting positive social and environmental impact.[3] Angel investors and VCs are also seeing impact as an important driver of commercial potential.

In effect, to use the language of the 'Spectrum of Capital', we are seeing the finance-first and impact-first worlds converging and connecting. As Dougie Sloan, Managing Director of Impact Venture at Big Society Capital, notes:

> *"Looking back a few years, the traditional venture world and the impact venture world were barely connected – but now they are increasingly coming together. We are seeing mainstream, top-tier VCs investing in subsequent rounds of companies that have come out of these highly impact-dedicated early-stage funds. We're also seeing investors from top-tier VCs spin out and launch their own funds with an impact flavour, some of which are entirely dedicated to impact. Those data points suggest the ecosystems are coming together more than before and communities like ImpactVC are helping to broker relationships and accelerate that shift."*

As this happens, impact ventures will be expected to move the dial on the world's biggest challenges through a profit generating business model. The interviewees specified that this approach facilitates sustainable and long-term impact, as well as satisfying the financial expectations of investors.

> **"Most investors care about getting £3 back for every £1 invested – so impact investment has to deliver benchmarkable returns."**

Alex Dunsdon, LP and Board Member at Climate VC

3. 'The billion-dollar funds that have changed impact investing' Environmental Finance, 20th August 2021 - https://www.environmental-finance.com/content/analysis/the-billion-dollar-funds-that-have-changed-impact-investing.html

Chapter Two

The risk in confusing impact investment with ESG

A key finding to emerge from our expert interviews, is that when it comes to understanding impact investment, ESG is considered a distraction. Whereas impact is grounded in intentionality, ESG is rooted in compliance and reporting. This may be a generalisation, and some of the interviewees acknowledged that generalising may to a degree be unfair, but there is broad consensus that the description ‘ESG’ lacks authenticity, and risks ending up in scandal and cynicism whatever the intentions of some.

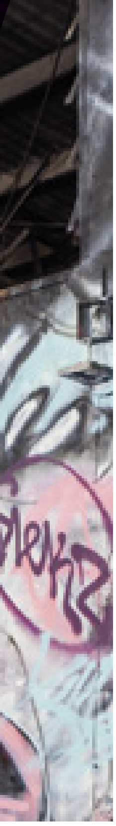
The expert view is that, conceptually, there are a plethora of ‘trade-off’ considerations that haunt ESG judgements.[4] The ability for firms that are doing badly on the ‘E’ of ESG, to balance their ESG ratings by performing well on their ‘S’ and ‘G’ metrics, has fuelled claims of ‘greenwashing’ and ‘impact-washing’. This has led some observers to suggest investors might do better not to use overall ESG metrics and ratings when constructing portfolios, but rather to choose a more customised approach that only takes into account one or two ESG sub-themes. As the authors of a paper for the Bank of International Settlements noted:[5]

> *“Devising investment strategies based on an amalgamation of these fundamentally different topics underpinning ESG investing has been a practical hurdle, especially given the potential for weak scores in one pillar to be offset by strong scores in another pillar.”*

The conclusion, therefore, is that a focus on factors that are most relevant to a particular investor would bring greater intellectual clarity to the use of ESG measures and enable investors to overcome the aggregate confusion created by consolidated ESG scores or ratings. In addition, the interaction between impact investing and ESG needs stronger ground rules, with impact investment distinguished much more clearly from ESG.

4. https://www.ft.com/content/b8df3190-e91e-4138-be00-142b5603eb92

5. Ehlers, T et al (2022.22) ‘Deconstructing ESG Scores: How to invest with your own criteria’ Bank for International Settlements Working Papers, No 1008, March 2022 - https://www.bis.org/publ/work1008.pdf



Section 2.1

Impact investment and ESG - not interchangeable terms

The interviewees believed that definitions of ‘Impact Investment’ and ‘ESG’ can be found if you look hard enough to find them, but the consensus was that they are not used consistently or with sufficient clarity.

There is also a view that this has led to surprisingly careless use of language, with key terms such as Sustainable Investing, Ethical Investing, Responsible Finance, ESG Investment and Impact Investment, continuing to be used interchangeably by investment practitioners and commentators alike.

The research found that this was an obstacle to the ongoing development of impact investment, and that impact investing can only deliver on its full potential if there is a forensic approach to the difference between it and ESG metrics.

As Stephanie Kater, a Partner in The Bridgespan Group, noted in 2021:

> *“…[a] plethora of terms ….[socially responsible investing, ethical investing, ESG, impact investing], and others like them, has blurred the boundaries among different investment products and strategies, causing confusion for many investors. Indeed, a remarkable 96 percent of impact investing professionals consider a lack of clarity about what constitutes an ‘impact investment’ to pose a challenge. And the fact that both ESG investing and impact investing are growing so rapidly – and in tandem, as it were – may lead some to conflate those two terms.[6]”*

Experts consulted were keen to avoid this conflation at all costs, seeing impact investment and ESG as separate concepts and practices. Essentially, they view impact investment and ESG engagement as having entirely different centres of gravity. Impact investment’s centre of gravity is about high levels of intentionality. ESG’s centre of gravity is rooted in compliance and reporting, detailing how and in what ways it needs to respond to new red lines around risk and reputation in the face of sharpening external assessments of purpose, governance and business culture.

Our research also identified the possibility that as impact investing inevitably moves further into the mainstream, it will be less prone to misappropriation in terms of badging in the way that ESG has been plagued by greenwashing. Intentionality is significantly more difficult to fake through virtue signalling than claims of environmental credentials.

6. Kater, S et al (2021) ‘Why the World Needs Both ESG and Impact Investing’ The Bridgespan Group - https://www.bridgespan.org/insights/library/impact-investing/why-the-world-needs-both-esg-and-impact-investing

> "The thing in my experience that gets asset managers and owners moving on sustainability is risk. It's like, oh, sugar. I've suddenly realised I've got massive exposure to the impacts of climate instability, nature loss and societal inequality that aren't priced on my balance sheet, that are now having **real financial impacts.**"

Lucy Auden, Head of Sustainable Investments, C40 Cities

Section 2.2

ESG as a screening and risk management tool

Where ESG helpfully interacts and supports impact investment, it is emerging as a way of 'screening' and a due diligence 'floor' for mainstream investing activity. As several interviewees commented, some impact investment VCs are using ESG screening on an exclusionary basis at due the diligence stage. Sabina Pasha, an Associate at Guinness Ventures, sums up the views of many others:

> *There is definitely a trend from non-impact investors to start changing their processes to be influenced by ESG and impact investing. But you won't necessarily see it being publicised until these funds can use their data to show progression.*

For these reasons, it is possible that in the near future ESG might become a more supportive piece of scaffolding to the impact investment activity.

As Ashley Abrahams, Fund Manager at Guinness Ventures, comments:

> *A strong ESG proposition by itself is not a reason for us to say yes to a deal, but if a company has a negative ESG impact (e.g. fossil fuel extraction) that would be a reason for us to say no to the investment opportunity.*

In a similar vein, Johannes Lenhard, Co-founder and Co-director of VentureESG, notes that:

> *ESG is how you do things – and impact is what you do.*

This potential to keep ESG and impact investing separate, but fashioned into a supportive relationship, is strongly underlined by Lightrock's investment management approach.
What is striking about Lightrock's approach is that ESG and impact are considered as separate, complementary considerations and processes, with both regarded as vital inputs to the investment process. As Lightrock's Dr Katharina Sommerrock observes:

> *At Lightrock, we make a clear distinction between ESG and impact investing. We have separate systems and processes for both. We run an impact assessment and an ESG assessment, and in turn produce separate ESG and Impact reports. ESG is a hygiene criteria for us, so we wouldn't invest in a company that is non-compliant or misaligned on the ESG side. But we invest for impact, we don't invest for ESG. There is a clear difference between the two.*

Section 2.3

ESG needs to mature and grow, but not 'crowd out' impact investment

The interviewees talked about how the ESG 'language jungle' has unfortunately been translated into a measurement and reporting 'jungle' – generating an alphabet soup of acronyms and hundreds of ESG performance indicators.[7]

A clear conclusion is that the science of ESG and of impact measurement needs to mature, and our interviewees are broadly optimistic about the long-term potential of ESG measures to help improve company performance on key indicators, particularly if those measures are more tightly focused.

But for the shorter term, the view is that this proliferation of measures creates the real risk that the progress of early-stage impact ventures could be derailed by applying complex and unachievable ESG reporting and measurement requirements and obligations. The measurement debate also obscures a bigger risk: that ESG investments may be drawing capital that would otherwise be available to impact ventures, when in fact the confusion around ESG measures and reporting could be used as a starting gun for investors to look more concertedly at impact investment opportunities.

A key observation from the interviews was that impact investment is a faster answer compared to slower moving ESG compliance, reporting, and investing. There is a need for an avowedly entrepreneurial and innovation-based approach to current challenges, not a reporting led one.

A further observation was that businesses cannot stand on the same ground they stood on pre-Covid and expect to be able to thrive and create sustainable value in the longer term, due to red lines on a variety of key risks having moved, and all of them demanding a decisive response.

Amongst the various prominent factors named by interviewees, climate was undoubtedly the dominant driver identified in the research, and interviewees talked about the seismic shift in our understanding of the role investment capital has to play in addressing the resulting threats.
As Jamie Broderick, Board Member and Deputy Chair of the Impact Investing Institute, commented:

> *You can't solve this problem without large amounts of capital… So then people start looking at not just government spending, but at pools of managed capital… This is where the momentum is coming from.*

One example cited was the International Energy Agency's estimate that to achieve net zero emissions by 2050, global investment in the energy sector alone will need to grow to approximately $5tn a year in less than a decade. Given significant public-sector indebtedness, the bulk of the required capital will need to come from the private sector.[8]

The urgent challenge then is how to unlock and see more managed capital investing effectively in impact ventures. But this requires capital that is going into generalised ESG-type investments to flow more freely into impact investment, as impact ventures are the businesses that are moving the dial on the world's most pressing social and environmental challenges. For this to happen there is a need to accelerate the rate of innovation in the impact investment ecosystem, both in the UK and beyond.

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7. Lenhard, J. & Lutz, E. (2022) 'What ESG means for venture capital' VentureESG White Paper, No 1

8. https://www.ft.com/content/b6cc17f0-c0c3-476a-bb77-1e7c1e9e946a

"I think with ESG now, it needs to be broken down into some constituent metrics, which we really need to track as a planet. For example, we need more metrics which look at the pace of change. I think essentially the big question for a company is whether the carbon mix of their output is changing? Yes or No. That's the question of whether we, as a species, are going to survive this event. So let's focus on that one for a start."

Sam Gill, Co-Founder and COO, Sylvera

Chapter Three

The opportunity for market innovation

If we are going to make the scale of change we require, we are going to need everybody: authentic impact-dedicated funds who are taking a deep impact lens and pioneering that way of thinking; but also those new to impact – genuine top-tier firms – who are interested in doing more and understanding this better; and then those who are waiting for others to move, and will move as the ecosystem moves.

Dougie Sloan, Managing Director of Impact Venture, Big Society Capital

The consensus among interviewees was that accelerating systemic change in the UK's impact investment ecosystem is going to require market innovation, and that the impact investment community is well prepared for this challenge. Whether investing in highly deployable new solutions to climate change, or in impact ventures, what shone through the interviews was a strong commitment to finding new solutions to the biggest challenges, and to look for entrepreneurial and novel answers.

The expert interviewees identified a range of powerful development areas and themes that they believed need urgent attention to encourage mainstream investors to invest more in impact ventures, and to see impact investment becoming a prevailing source of positive economic activity in the UK.

Section 3.1

Integrating finance and impact by encouraging a lock-step approach

A key conclusion from the interviews is that leading-edge impact investors are actively de-bunking the principle that investment must be finance first and impact second. The lock-step approach ensures that financial returns are not compromised, whilst making certain that impact is front and centre of every decision.

One of the best examples given of the adoption of the lock-step approach was that of Lightrock, a global private equity platform and sister company of the private bank LGT. Its stated mission is to 'back purpose-driven entrepreneurs tackling the world's biggest challenges'.[9]

It describes impact as being core to its strategy, with a commitment to showing how its investments demonstrably contribute to the UN's Sustainable Development Goals and enhance long-term value creation and innovation. It is clear that Lightrock is a highly intentional, 'lock-step' impact investor, with finance and impact seen as integrated when making investment decisions.

As Lightrock's Dr Katharina Sommerrock, Head of Investor Relations, comments:

> *When we do due diligence and select investments, we have thresholds on both impact and finance. We don't compromise between the two. If a company doesn't meet the bar on one of them, we won't invest. We are neither impact first or finance first, we believe they are mutually reinforcing.*

In examining these criteria, Lightrock leverages its own proprietary impact measurement and other frameworks such as the Impact Management Project and GINN's IRIS+. This is an example of why mainstream VCs are starting to see impact as a vital driver of commercial potential. Interviewees commented that the adoption of this kind of lock-step approach will further speed the convergence of finance-first and impact-first ecosystems, encouraging more mainstream investors to cross over to invest in impact ventures, intentionally.

Moreover, interviewees expressed a belief that, in contrast to the often diffuse 'read out' given by ESG metrics, the clarity of demonstrable outcomes being produced by impact ventures, with lock-step business models, makes investing in them a more authentic and powerful way of mitigating the risks their portfolios face from social and/or environmental challenges. Equally, reputational risk and reputational opportunity need to play a more central role in investment decisions, which will further fuel capital flows into impact investment and lock-step models.

9. https://www.lightrock.com

Section 3.2

Encouraging transparency and accountability on the investor side

The quality, appropriateness, and type of data – both measurement and reporting – was identified by interviewees as vitally important to the credibility and growth of impact investment. Requests for more and better data are not seen as novel; a more insightful question is where the greatest information deficits are found.

Johannes Lenhard, Co-founder and Co-director of VentureESG, noted the important role that market researchers such as Pitchbook, Dealroom, CB Insights and Crunchbase perform, and the role they could play in supporting more responsible investment practices by including ESG information in their trends reports.

Interviewees also commented that it would be good to have more information on the performance of impact investors themselves. As Chris Fellingham, Social Sciences and Humanities Lead at Oxford University Innovation and Co-Founder and Director of ARC Accelerator, suggests:

> *Why not have an index of impact investors? And identify those having more impact than others.*

Such an initiative would help prospective investees, and more widely UK PLC, as it would bring transparency and accountability into the marketplace. The view is that, to an extent, this type of impact disclosure is already emerging, but more is needed. Investors are already pushing private equity firms to align impact with their activities. It becomes the natural next step for funders to seek better quality information on the relative performance of different impact investors.

The impact investment ecosystem can take inspiration from related initiatives. One project mentioned was the think tank Influence Map[10] which launched an interactive platform tracking and ranking 70 companies and 30 industry associations headquartered in the EU, based on how they have supported or opposed the advancement of more ambitious climate action. The Corporate Leaders Group, convened by The Cambridge Institute for Sustainability Leadership (CISL), was awarded an 'A' ranking, topping the industrial association list.

An index of impact investors, aimed at showcasing and ranking best in class investment practice, is a potential powerful incentive to encourage improved impact investment practice.

10. https://europe.influencemap.org

Section 3.3

Mapping the impact investment ecosystem

> *Map the system – it is all disjointed – all these ships floating around in the city, going in their own direction, but no sense of how close they are to each other and where they are going.*

Mark Mann, impact focused knowledge transfer consultant

The research has identified a need for the impact investment ecosystem to be mapped in a more sensitive and dynamic way than it currently is. It was the clear view of interviewees that there is a spectrum of returns and types of investment across the impact investment ecosystem.

However, as some experts noted, helpful but simplified explanatory schema, like the aforementioned Impact Investing Institute's 'Spectrum of Capital',[11] inevitably cannot capture the complexity of what is going on in the impact investment ecosystem, and the dynamic movements taking place within it. Investors are moving to their own highly layered 'finance-first – impact-first'-driven spectrum within that impact investor ecosystem.

Not all impact ventures require 'patient capital'. Those ventures with scalable and immediately deployable environmentally-focused impact are capable of achieving substantial and quick returns for investors, and therefore attract significant levels of early-stage investment.[12] However, other impact ventures require different types of capital, for example investment in research and development in intensive renewable energy projects.

Interviewees also pointed to complex areas of public policy such as homelessness and housing/ social care. In these areas, unless the Government or philanthropists use their resources to help create market opportunities and foster an environment where proof of concept pilot solutions can be tested and scaled quickly, private capital is unlikely to be applied in a significant way.

More broadly, as Jamie Broderick comments, with these really difficult problems and challenges, Government should pay more attention to:

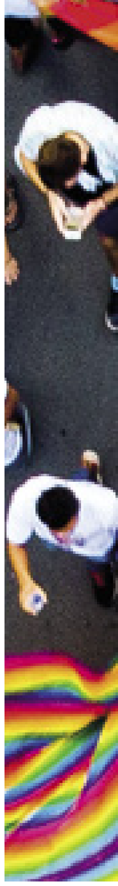
> *catalysing private market capital through various forms of subsidy, whether it's first loss, guarantee or other mechanisms.*

All of this suggests that a new mapping of the impact investment environment is required that allows key stakeholders to develop and determine a more precise spectrum of intentionality (and return) for the impact investment tribe from investors seeking highly scalable, immediately deployable propositions with market rate returns through to 'softer' / patient / market priming / impact venturing activity.

It is believed this type of clarity would help mainstream investors and different types of impact investors to better understand each other, seek collaborative common cause, and learn more quickly from best practice. As growing numbers of mainstream investors enter the world of impact investment, they have the most to learn from sophisticated and experienced impact investors and innovators in this part of the investment sector.

11. https://www.impactinvest.org.uk/wp-content/uploads/2020/11/Spectrum-of-capital-general-version.pdf

12. See for example Sylvera, a carbon credits rating solution, recently raised $32.6M in Series A funding to accelerate its mission to become a source of truth for carbon markets: https://www.sylvera.com/product



Section 3.4

Marketisation

A necessary market innovation theme mentioned by some of the interviewees was the need to build on what we have learned from carbon markets in terms of how best to price externalities and to incentivise investment and corporate behaviours. Charlie Munger, the American investor known as Warren Buffett's right-hand man, has a recognised phrase that was mentioned: 'show me the incentive and I'll show you the outcome'. In other words, if you get the market mechanisms right, then impact investment flows will quickly follow.

So, for example, putting a 'cost' on a negative social outcome, could then be used to create market incentives to drive a response from the impact investment community. As Chris Fellingham comments:

> *There is a limit to how far for-profit investment can go within current market conditions… and it would be good to see some experimentation, taking what we've learnt from carbon markets to other areas.*

Interviewees also discussed possible innovations in shareholder agreements and other legal documents that underpin company formation and incentivisation. For example, they talked about founders getting a bonus if they hit the impact part of their investment agreement, and thereby embedding a drive to impact from the very beginning of a company's growth.

> **I would spend some time finding the incentives that enable the private market and entrepreneurship to help people invest in and build what is needed in the future… Create the right incentives to get the most talented people building the stuff that matters.**

Alex Dunsdon, LP and Board Member, Climate VC

Section 3.5

Supporting networks to accelerate change

One of the key elements to emerge from the research is a real sense among all participants of the dynamism across the impact investment community. They felt change was coming fast, and it was noticeable how many referenced important networks and organisations that are sharing best practice and testing out new ideas.

Networks and organisations frequently named included VentureESG, Diversity ESG, GINN's Gender Lens Investing Hub, Responsible Investment Network – Universities (RINU), the Impact Investing Institute and Big Society Capital. These networks are working concertedly, often together, to drive change, and to encourage more knowledge exchange around innovation and practices. The collective aim must be to generate common purpose around what the constituent parts of impact investment should be, and the operating conditions under which it can flourish.

Networks are vital as they will help ensure a demanding set of lenses (financial, social, environmental, gender) to inform ongoing impact assessment and due diligence in next generation impact investment practices.

Most of our interviewees felt that Government had a role to play as an enabler, but not as the primary leader. It can create the appropriate landscape and incentives for progress, but it cannot - and should not - lead on its own.

Conclusion

Faster impact investment innovation = faster UK PLC innovation

> *Prioritisation is incredibly important for impact investment because the most impactful types of investment can easily be 100x more impactful than average. So we need to ask: what type of impact investments is the UK best placed to lead on? What would updated priorities for 2030 look like?*

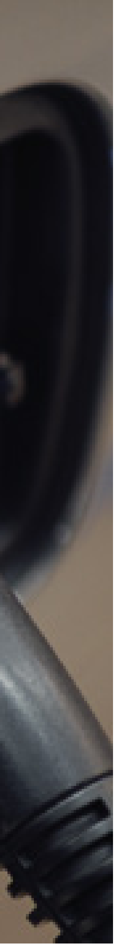
Dr Jonathan Harris, Founder, Total Portfolio Project

If the development themes outlined from the research can be addressed promptly, it will do much to help drive market innovation in the UK impact investment ecosystem, and potentially beyond.

The opportunity costs of inaction are high. The interviewees were enthusiastic supporters of the notion that if innovation can be accelerated in the impact investment sector, it will accelerate the rate of innovation across UK PLC. This would spur the creation of new products and services, productivity improvements, and increases in GDP, as well as creating positive impact.

If we want faster growth in the UK, we need to unlock what could be a big new growth phase for impact investment, seizing this moment with a set of refreshed goals for the investment, entrepreneurial and political communities.

For example, the experts touched upon the role of impact investing in supporting the Government's Levelling Up Agenda (and any successor), through to the need for the Government to carefully consider those areas of economic, social, and cultural activity where a fully catalysed impact investment ecosystem could play a vital role in driving economic growth, and in successfully addressing key societal challenges.



The wider belief demonstrated by the research was that unlocking this potential requires a consolidated vision from Government, developed by working in concert with businesses, the public sector and the third sector. For example, if the Government sought to link greener housing with attempts to tackle the housing shortage and homelessness and set ambitious and stretching targets to be achieved by 2030, systematic consideration could then be given to how impact investors could play a full role in delivering on those ambitions. In light of adopting such an approach, Government would then consider how it would need to act in terms of providing incentives, or seed capital for new innovation.

This raises the broader possibility that in its vision for impact investment, the Government, drawing on key trends shaping our future, could seek to agree key priorities for UK PLC and society, for example, climate and/or homelessness, and structure long-term incentives to help solve these problems by catalysing entrepreneurs and private market capital.

Government has already signalled its interest to sponsor new ideas in impact investment, supporting and endorsing work on 'Growing a culture of social impact investing in the UK'.[13] But the interviewees considered that the scope and ambition needed to be much more expansive, and that the aim should be to make the UK the most innovative environment in the world for impact investment. This raises the question of how else new ideas can best be trialled and tested? And also, what might that look like in terms of incentives, codes, practices, and support?

The challenge then is to capitalise on the resulting potential to amplify the most innovative and distinctive emerging impact investment practices, and to help positively shape the ever more important role impact investment can play in the future fortunes of our planet, our societies, and UK PLC.

An impact investment strategy for UK PLC that fully embraces the important roles that the different impact investment communities can play could yield extraordinary dividends, deliver innovation, growth, and new solutions to the urgent economic, environmental and social challenges.

"We need a vision that says… this is where the puck is going, let's be an innovator in those vital areas for the next 20 years, and put in place the long-term thinking and structures that allows impact investors to make a more profound difference."

Alex Dunsdon, LP and Board member, Climate VC

13. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/811914/Final_report_by_the_Implementation_Taskforce_Growing_a_culture_of_social_impact_investing_in_the_UK_2019.pdf

Appendix: Interviewees


Adam Durant
Satavia


Alex Dunsdon
Climate VC


Alex Egan
Yellow Sub Geo


Ashley Abrahams
Guinness Ventures


Cam Ross
Green Angel Syndicate


Caroline Hyde
Cambridge Enterprise


Catherine Bottrill
Pilio


Cédric Lombard
Impact Finance


Chris Fellingham
Oxford University Innovation


Chris Willis Pickup
Taylor Vinters


Dama Sathianathan
Bethnal Green Ventures


David Bartram
UnLtd


David Ovenden
Bockatech


Douglas Sloan
Big Society Capital


Emma Salgård Cunha
Cambridge Enterprise


Felix Litzkow
Crisis Venture Studio


Francis Wright
Turquoise / Low Carbon Innovation Fund


George Bevis
CanDo


Hayley Cross
Taylor Vinters


Jamie Broderick
Impact Investing Institute


Johannes Lenhard
University of Cambridge / Venture ESG


Dr. Jonathan Harris
Total Portfolio Project


Jonny Page
Esmée Fairbairn Foundation


Dr. Katharina Sommerrock
Lightrock


Katy Brown
Magic Mountain


Kieran John
Taylor Vinters


Lisa Barclay
Nesta


Lowri Hill
Yellow Sub Geo


Lucy Auden
C40 Cities


Maeve O’Hare
Balderton Capital


Mark Mann
Mark Mann OÜ


Nick Temple
Social Investment Business


Nicolas Mathias
Bockatech


Sabina Pasha
Guinness Ventures


Sam Gill
Sylvera


Steve Butterworth
Neighbourly

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For more information on the report and our findings, please contact
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