



Impact investing: How private and listed markets offer choice for investors seeking positive change

Key highlights

- There is demand for ESG to go beyond basic integration, towards positive impact
- The rise of sustainability megatrends means it is possible to deliver impact in listed markets as well as private markets
- The UN SDGs provide a very good starting point for identifying areas of significant unmet demand, and demonstrating long-term secular growth opportunities
- In **private markets** investors have more control over operations to deliver targeted impact. Strategies can hold assets for a longer time
- In **listed markets**, investors must deploy capital where they can show impact intentionality, materiality and additionality. Engagement is also used
- Measurement remains a challenge and relies for now on robust frameworks and on verifiable, comparable data at the level of individual assets

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Impact is now a twin-engined vehicle

Impact investing is helping investors tap into key financial markets megatrends while addressing some of our most important sustainability challenges. The sector has been built on powerful private market foundations, but a growing roster of large, listed companies are now providing products and services that can deliver positive and demonstrable effects for people and for the planet. This evolution is offering investors an important choice.

A central idea in the broad responsible investment (RI) marketplace is that long-term investors, regulators and governments share a common goal: To build resilient economies that can thrive in a future that may look very different. The scale of investment required is huge, and by remaining ahead of the curve in policy and consumer behaviour, there should be a clear opportunity set for both small-scale entrepreneurs and for the largest corporations on earth.

For those wishing to deploy capital to such companies, impact investing is a natural

part of call – and it is now a twin-engined vehicle. The sector has always been at the sharp end of strategies that seek to embed environmental, social and governance (ESG) issues, but with private and listed markets both in play it is important to understand how each can help you to meet your investment objectives in different ways.

There are, of course, common threads between the two segments, and this is perhaps most clearly seen in the role of the UN Sustainable Development Goals (SDGs).

The UN SDGs

The United Nations Sustainable Development Goals are a set of 17 targets agreed by all UN member states in 2015 to provide a blueprint for global development. More and more companies and countries are tailoring projects and strategies to specifically address multiple SDGs and as a result, it has become far easier for responsible investors to put their money to work with confidence, and to measure the effect their investments have had.



Drilling down into the SDGs

In the listed market, AXA IM Core offers several impact strategies which reflect broad ESG themes. Amanda O’Toole, who manages Framlington’s Clean Economy strategy, notes the crucial role of the SDGs in articulating secular growth opportunities in this area, and in providing a structure that can guide asset managers and end-investors alike.

“There is an estimated \$5-7trn¹ annual investment need into the themes marked out by the SDGs, and it is clear to us that prices are starting to track that need,” she told investors at a recent AXA IM webinar. “At the same time the SDGs provide the means for verification and measurability of non-financial results. This is utterly crucial for anyone trying to deliver genuine impact.”

For Jonathan Dean, who heads up AXA IM Alts’s ‘traditional’ private market impact investing strategies, the headline SDGs are only half the story. He stresses that the more granular and definitive targets within each goal add heft and detail to the global push to tackle the SDGs – and help identify specific growth paths for portfolio companies.

“The SDGs are more than colourful, attention-grabbing logos, they run deeper and wider in terms of highlighting investability and in terms of delivering genuine financial and impact returns. If you are an investor, in private or listed markets, the SDGs help make impact actionable.”

And so, across private and listed markets, the SDGs offer useful foundations, but

any successful impact strategy must also display some key features:

- ▶ a clear definition of what the strategy seeks to achieve
- ▶ an assessment of the scale of the problem it aims to address
- ▶ an assessment of how capital can be deployed to do that
- ▶ a clear understanding of the route to financial returns alongside impact
- ▶ a path to measuring and verifying impact over time

For now, asset managers need to make sure these factors work individually for each and every impact strategy and for each and every investment. We do not have the luxury of a common set of standards for measuring and reporting impact criteria. In fact, the sharp growth of the industry has expanded the ways in which impact is defined and communicated.

That is a challenge as well as an opportunity – AXA IM has the scale and means to dive deep into each holding, but we also work towards industry standards that will help lift the impact segment as a whole.

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¹ UN Secretary General António Guterres. September 2018. <https://news.un.org/en/story/2018/09/1020372>

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Building a strategy in private and listed markets

For us to deliver measurability and verification for our clients in this environment, it is important to have robust investment frameworks in place that reflect the very different conditions and approaches in private and listed markets.

In private markets, we might have a stake through a fund; we might have a 10-15% stake in a company; or we might have control over an entire project. However an investment is structured, we have the advantage of close involvement with the people delivering both the financial and impact returns. We can set the course of travel – and help define the destination.

At its heart, this is about delivering that change across the life of a private market investment, which could be five to seven years. We want each phase of the process to contribute to the change we seek, from screening to due diligence, from investment to exit. We aim to do that by starting with a four-step framework:

- **Pre-investment analysis.** Bringing impact management and impact targets in at the start of the process
- **Monitoring and Measurement.** Continuous reporting on impact and tracking of performance against targets
- **Industry standards.** External verification and alignment with leading common standards to promote integrity and transparency
- **Impact performance.** Assessments of financial and impact results, with a rigorous examination of the impact delivered

In listed assets, we still tend to be long-term investors but we would have less control over corporate operations. We do not want our holdings to be a drop in the ocean, and so we seek out companies that make a material difference to our defined impact goals.

That means our five-step framework for listed impact has a focus on understanding the nature of potential investments. In putting it to work we seek to deploy capital with impact leaders in a way that sends clear price signals to the market, while using engagement to encourage SDG-aligned corporate behaviour.

- **Intentionality.** Making clear what issues are being addressed by the strategy and by the portfolio companies
- **Materiality.** Is there a significant impact relative to the size of the company or to the scale of the problem being addressed?
- **Additionality.** Do the company's products or services deliver solutions that otherwise might not have come to light?
- **Negative externality.** Ensuring there are not side effects, or other activities at a company which might offset the positive impact sought
- **Measurability.** Is the data attached to the impact, verifiable, repeatable and reliable – and can we compare it to peers?

Case studies in environment and healthcare: A difference in scale

How do these different approaches work in practice? One way of setting the two investment styles in context is to review how each tackles similar themes, and to understand how the direct approach in private markets contrasts with working at scale in listed markets.

The methods, locations, and operations may be a world apart, but these examples also underscore the common thread: Unearth routes to impact; deploy capital; deliver the impact and financial returns.

Environment: Private

Jonathan Dean highlights AXA IM Alts's investment into Komaza, a microforestry-to-wood products company with a stated ambition to become the largest sustainable forestry company in Africa. This allows our private markets team to target SDG 15.1 – to conserve and restore ecosystems.

Delivering impact: Microforestry in Africa

- Komaza has reported planting **five million trees**
- ...Over **5,000 hectares**
- Reported improved financial outcomes for over **20,000 farmers**.
- Ambition to plant **one billion trees** in Sub-Saharan Africa



Source: AXA IM

“We need credible outcomes. Our investors need to know what their capital is being used for,” said Dean. “This investment will aim to contribute to reforestation of degraded lands, mitigate climate change using trees as a natural carbon sequestration solution and build climate-resilience. The idea is to align the financial interest of local communities with conservation.”

To date, Komaza has planted five million trees on 5,000 hectares and reported improved financial outcomes for over 20,000 farmers². Komaza represents what Dean believes is a new, scalable approach to conservation that can potentially put livelihood generation at the centre of environmental restoration. Dean believes this investment is able to provide a clear impact characteristic. “Financial and impact goals are intertwined. This should allow us to embed accountability into the investment, from entry to exit.”

Source: Komaza/AXA IM Alts. Data as of July 2020

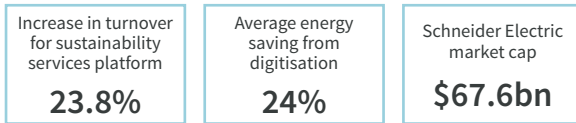
Environment: Listed

You can't get much further from microforests in Africa than the leap to one of Europe's largest companies, but this leap helps to tell the story of how listed and private impact are two sides of the same coin.

Amanda O'Toole has backed Schneider Electric in her clean economy strategy as a key player in the energy transition and one which meets the conditions set out by the investment framework.

"By virtue of its scale and commitment to best-in-class tech, we believe Schneider can potentially offer innovation in energy efficiency, and support the sustainable development of smart grids, renewables etc.

Delivering impact: Schneider Electric and digital services



Source: AXA IM/Schneider Electric annual report 2019/SE Global Digital Transformation Benefits Report 2019/EPA

"This simply can't readily be done on a small scale. Sometimes a company's sheer size can be a key part of materiality." The idea is that a large player should be able to tap more easily into an increasing global commitment to boosting energy efficiency and tackling important SDGs.

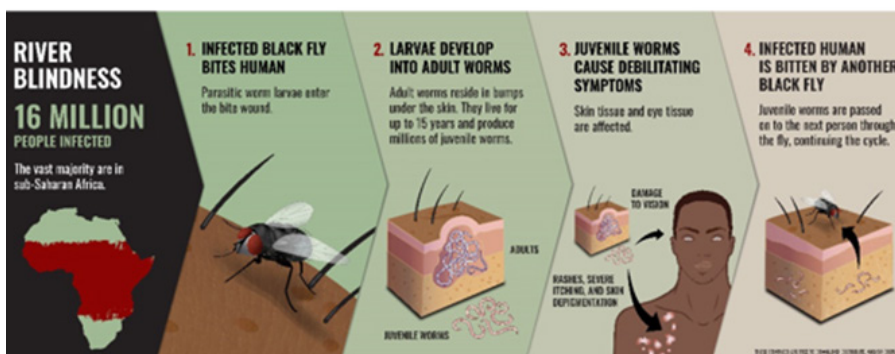
Healthcare: Private

Few things make a more immediate positive impact on people's lives than improvements in health outcomes, and Dean highlights one investment made by AXA IM Alts to address the issue of river blindness, the world's second leading infectious cause of blindness.

The investment backed a drug, moxidectin, as part of a drive to improve treatment activity that has been focused on grant-led work by charities. This was supported by the US Food and Drug Administration (FDA), which wanted to encourage entrepreneurial solutions for neglected

tropical diseases, and which offered Priority Review Vouchers as an incentive to produce new drugs. The allowed the company behind moxidectin, Medicines Development for Global Health, to deliver the first new treatment for river blindness in 20 years, while delivering a financial return through the sale of the voucher to a company eager to get a timing edge on rivals in the cut and thrust of the conventional pharma market.

Delivering impact: The challenge of river blindness



The goal is for impact and financial goals to be intertwined, and to be aligned with SDG 3.3, which calls for an end the epidemics of AIDS, tuberculosis, malaria and neglected tropical diseases and combat hepatitis, water-borne diseases and other communicable diseases.

"Not only that," says Dean, "but we've also recycled some of the capital into a NewCo which is developing this drug for other uses. The 'responsible exit' is potentially continuing."

³ Source: Medicines Development for Global Health. <https://www.medicinesdevelopment.com/development-programs.htm>

Healthcare: Listed

In the health sector, some conditions get less attention than others, often because it can be hard to justify large research and development (R&D) spends, but one portfolio company in AXA IM's listed impact strategies, Alnylam Pharmaceuticals, tries to help fill that gap.

"Their vision is to transform the lives of people living with diseases where there are limited or inadequate treatment options," says O'Toole. "This is a powerful starting point in terms of intentionality from a corporate point of view."

Companies need to back up their ambitions, however, and Alnylam aims to do this with a very large commitment to R&D. One specific breakthrough – delivering that crucial element of additionality – involved an improved understanding of how genes are regulated in cells. That has given the company a way to treat conditions that are not readily addressed with standard drugs, and to put that innovation to work at a growing scale. This is particularly the case for onpattro, designed to treat hereditary transthyretin-mediated (hATTR) amyloidosis, a multisystem disease with a series of unpleasant symptoms.

"This is what we expect from an impact leader," says O'Toole. "It's not only innovation, it is consistent and ongoing innovation and they are trying to build a sustainable business model around that large commitment to R&D to addresses unmet needs, rather than looking to aggressive pricing."

Delivering impact: Ensuring patient access to treatments



Patients worldwide with hATTR amyloidosis
~50,000

Patients on ONPATTRO
>1,050

Alnylam market cap
\$15.7bn



Source: Alnylam annual report 2019/Alnylam corporate presentation Q2 2020



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