

Open Standards support for the Impact Investing market

An outline of a significant new funding source, showing how use of the Open Standards can position organisations to access it

Purpose	This report outlines the emerging Environmental Impact Investing market, a potential future source of funding at the scale required to effectively protect global biodiversity. It illustrates how use of the Open Standards positions projects to access this market. It also outlines the IRIS Metrics, which provide an industry standard for reporting the impact of projects, helping investors to compare performance of various organisations.
Who should use this, and with whom?	Integrators / M&E staff, with organisation leadership, particularly Finance and fundraising executives
When	When discussing high-level organisation strategy and options for funding it; and in reviewing options for assess and report project and organisational performance
How	Demonstrate the core capabilities required to tap into the market (particularly project management, impact measurement, and scaling up of projects) and how adoption and institutionalisation of the Open Standards provides these capabilities. For use of IRIS metrics, potentially start with a few of the existing metrics that are relevant and use those in external reports. Collaborate with other conservation groups to build a broader range of metrics more relevant to the sector.

Annette Stewart - Fulbright Scholarship 2016

**Improving the *practice* of conservation
by improving the *management* of conservation**

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Open Standards support for the Impact Investing market

The Impact Investing market offers a potential new source of significant funding to protect global biodiversity. Several recent reports have analysed this market and concluded that “*there is no shortage of investment funds; there is a shortage of investable projects*”. They also conclude that the conservation sector is around 10 years behind other social sectors in being able to leverage this market.

Adoption and institutionalisation of the Open Standards creates the capabilities required to tap into this market - particularly for project management, impact measurement, and scaling up of projects.

This document provides a summary of some recent reports on the Impact Investing market, along with the connections to Open Standards and some exhibits that might aid communication.

Refer also to these related tools -

- [Positioning Open Standards within business performance & reporting frameworks](#)
- [Open Standards and Collective Impact](#)
- [Conservation Capability Maturity Model](#)

The Impact Investing market

Efforts to improve the *practice* of conservation are clearly targeted at achieving greater conservation impact with the resources available. Improving the *management* of conservation is aimed at using these resources as efficiently as possible. While both of these improvements are critical, global conservation efforts continue to be constrained by the resources available to undertake conservation work.

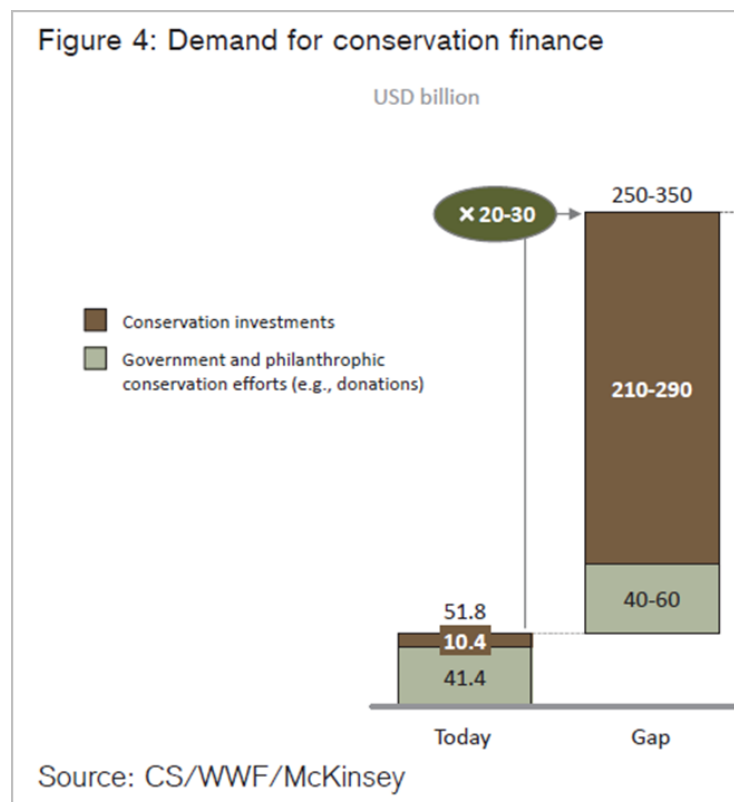
Several recent reports¹ have investigated alternative models for funding the effort required to adequately protect the world’s biodiversity. These reports analyse the supply-side options for “conservation finance” which can be defined as - “*Investment mechanisms that activate one or more cash flows generated by the sustainable management of an ecosystem, which in part remain within the ecosystem to enable its conservation and in part are returned to investors*”. Examples include service payments, compensation payments or fees, permit trading, offsets, and certified natural commodity markets like the Forest Stewardship Council. These options form part of the broader Impact Investing market which is growing rapidly in other social sectors.

The key findings from the original thought-leadership report (by Credit Suisse, WWF, & McKinsey) include –

- The current global spend on biodiversity protection (including all government and philanthropic funding) is estimated at around \$50bn per annum.

¹ For example, see [Conservation Finance - Moving beyond donor funding toward an investor-driven approach](#), 2014 co-authored by Credit Suisse, WWF, and McKinsey & Company; and [Investing in Conservation - A landscape assessment of an emerging market](#), co-authored by TNC’s NatureVest, and EKO Asset Management Partners

- Recognising the challenges of sizing the cost of adequately protecting biodiversity at a global scale, their research concluded “an estimate of US\$300-400 billion as a reasonable working figure of the projected annual costs for global biodiversity protection”.
- To meet that gap in demand, “investable cash flows from conservation projects need to be at least 20-30 times greater than they are today, reaching USD 200-300 billion per year, if we assume that current government and philanthropic funding at least doubles”
- While this seems like a huge amount, “There would be sufficient financial capital available to meet conservation investment needs if the main investor segments (i.e., high-net-worth individuals, retail and institutional investors) globally allocated 1% of their new & reinvested capital to conservation”.



The key conclusion (from this and other similar reports) is that **there is no shortage of investable funds, but there is a shortage of investable projects**. The report described the conservation sector as “moving from infancy to young adulthood” and that “conservation finance is 10-15 years behind social impact investment”.

The authors’ hypothesis is that a concerted, systematic effort focused on structuring investment products that provide a conservation and a financial bottom line would be the best way to overcome the current gap between conservation project funding requirements and the capital available to cover these needs.

The report outlines some key steps that conservation NGOs should take, including –

- provide a sufficient supply of large-scale conservation projects that have clearly defined environmental and financial benefits
- act as verifiers of conservation project impact, and
- further develop conservation impact measurement techniques

The Open Standards is mentioned as a potential means to this end – “To ensure that a conservation project is worth investing in, its impact needs to be measured”. Further “We believe many of the above elements can be achieved by increasing the professionalism along the stages of the life cycles of conservation projects.”

A follow-up report has recently been published², showing the growth in the market in the intervening two years. The report is *“targeted at those who are willing to take the plunge into the “financialization” of conservation finance projects in order to try to tap into these deeper capital pools”*.

"Nature must not be turned into a commodity, but rather into an asset treasured by the mainstream investment market"
Credit Suisse CEO Tidjane Thiam

The report notes that the current low-interest environment is prompting investors to turn to new investment opportunities, seeking financial returns but also *“looking for a nonfinancial impact from their capital through direct or indirect investments in environmental conservation”*. The report also notes the number of "value projects" available in the conservation space is rapidly growing as illustrated by:- *“demand for sustainable agriculture or FSC-certified forest products now exceeds the traditional non-conservation segments of their markets”*.

The report outlines three major shifts required along the project maturity lifecycle that could unleash the next period of growth in the conservation finance field –

- **Incubating** - addresses how a project moves from a conceptual idea to a commercial business model. *“Setting up an incubator would provide an opportunity for key stakeholders interested in furthering this field – investors, NGOs, foundations, and other conservation finance actors – to bring their respective strengths to the table and collaborate in establishing a pipeline for the conservation finance market”*.
- **Scaling** - the issue of moving from small-scale to proven projects
- **Mainstreaming** - taking tested, medium-scale projects to the next level, developing large-scale and established conservation finance products attractive to mainstream investors.

If these shifts can be achieved, the report states:- *“they have the potential to create a conservation finance investment market of USD 200 billion to 400 billion between now and 2020”*.

The report identifies five key barriers on the project side of the market –

- Search costs to identify conservation projects with good risk-return profiles remain high. The authors observe that conservation financing is rarely integral to the concept and design of projects, and call for project developers (often NGOs) to apply a rigorous and standardized identification and evaluation process based on predefined impact and investability criteria.
- Few project developers have a track record in developing cash-flow generating conservation projects.
- Adequate collateral, which can be used to reduce financing costs and lower the risk of investors, is often missing as many project developers are unaware of what could be used as collateral.
- Scalability remains an issue, as most projects are not replicable beyond a 5-million-dollar threshold yet. This leads to high transaction costs.
- Monitoring - the lack of tested and agreed upon standardized frameworks for monitoring conservation impact. This is seen as essential to ensure that financing is not being directed at programs that yield little or no conservation benefits.

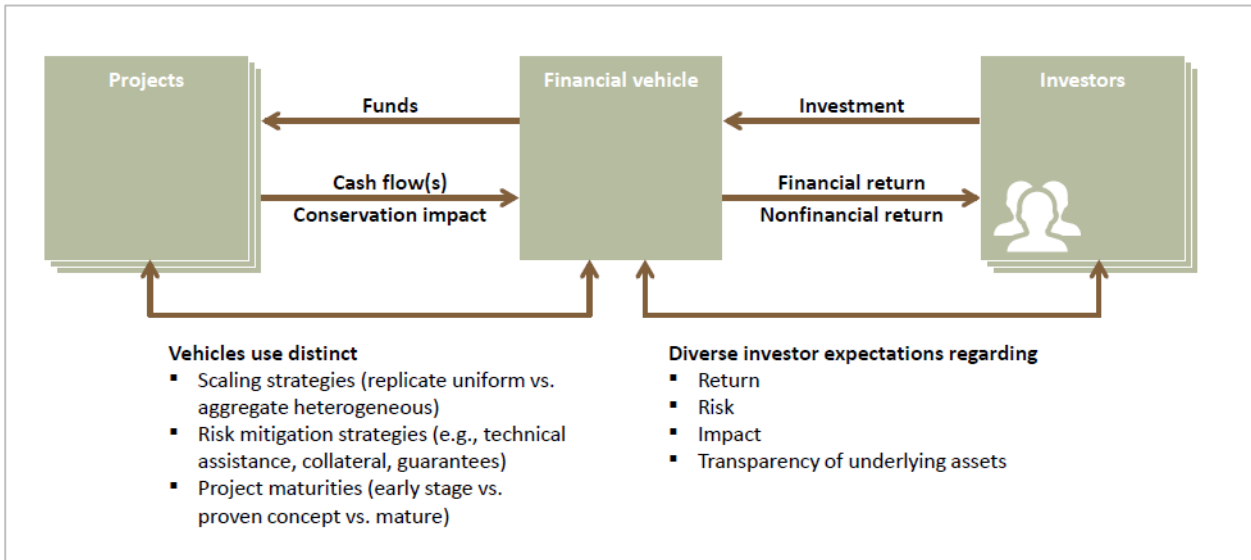
Actions proposed in the report to overcome these barriers include –

- a more systematic approach to scaling and replicating projects; replicating homogenous project types and financing these through equity and/or debt, or structuring multiple heterogeneous projects and then bundling them into a single financial product

² ; [Conservation Finance - From Niche to Mainstream: The Building of an Institutional Asset Class](#), 2016, Credit Suisse and McKinsey & Company

- a standardized project evaluation process to further reduce transaction costs; the report proposes a “project investability funnel” to evaluate the investment potential of proposed projects, and notes that “a similar funnel is being developed by the IUCN to evaluate and assess projects from a conservation impact perspective”
- options to mitigate risks need to be created, for example through operational assistance or guarantees.

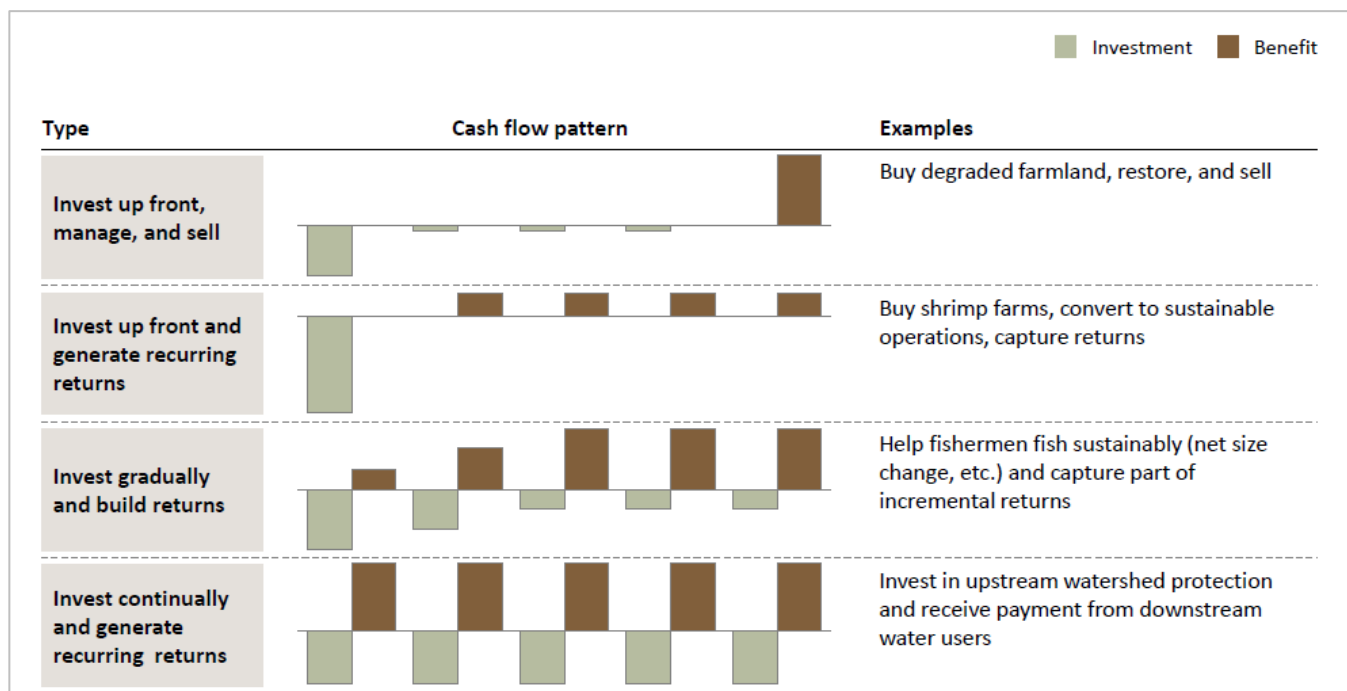
This diagram illustrates the link between the project (demand) and investor (supply) sides of the market.



“On one side there are project developers – most often NGOs – that have financing demands (e.g., large up-front investment required to acquire land or working capital demand to buy seeds or machines) and require capital to be able to generate or augment cash flows. Such cash flows can be generated, for example, by investment in the restoration of large landscapes, watershed protection, or ecotourism. On the other side, more and more investors seek new opportunities to invest their capital in a way that generates both a market-rate financial return and a nonfinancial impact (i.e. environmental and/or social).”

The report looks at the market from many points of view and suggests that there are some “natural starting points” - areas such as sustainable forestry, agriculture, or fisheries related activities offer sustainable cash flows and a comparatively larger number of risk mitigation techniques; while from the perspective of market maturity and scale, sustainable forestry, agriculture, and ecotourism stand out.

The diagram below illustrates several different forms of project funding and financial flows.



Some of the key entities in this market are listed below.

- [The Global Impact Investing Network](#) (the GIIN) is “a non-profit organization dedicated to increasing the scale and effectiveness of impact investing”. The network members include investors from commercial and philanthropic fields. The GIIN “addresses systemic barriers to effective impact investing by building critical infrastructure and developing activities, education, and research that attract more investment capital to poverty alleviation and environmental solutions.”
- [IRIS](#) is a catalogue of standard metrics commonly used by Impact Investment funds to measure and report results (see later in this document). IRIS is developed and managed by the GIIN.
- [Impact Base](#) is a searchable on-line database of Impact Investment funds. Currently there are over 100 funds categorised under the theme of “environmental markets”, targeting a total assets under management of over US\$182bn.
- [Conservation Finance Alliance](#) (CFA) develops publications and organises meetings to build and distribute knowledge and best practices in conservation finance.

For many conservation NGOs, tapping into the impact investing market requires new skills and knowledge, and a scaling-up of projects. Adoption and institutionalisation of the Open Standards can be seen as a necessary first step to developing a track record of organisational capabilities in project management and impact measurement – the basic building blocks expected for entry into this market. It also provides a common language for organisations to collaborate and scale up their efforts to create project at sufficient size to attract financial interest. See the supporting document **“Open Standards and Collective Impact”** for one model that helps to scale up projects.

Impact Investment Fund example

Althelia Madagascar Conservation and Climate Fund

Fund/Product Overview	
Fund Manager/Firm Name	Althelia ecosphere
Fund/Product Name	Althelia Madagascar Conservation and Climate Fund
Fund/Product Track Record	Fund has 3+ years of track record
Fund/Product Description	<p>The Althelia Madagascar Conservation and Climate Fund makes investments in sustainable environmental activities which reduce deforestation, facilitate the acquisition of carbon credits, and provide access to renewable energy in Madagascar.</p> <p>The fund focuses on 3 complementary set of activities to achieve landscape conservation, at scale:</p> <ol style="list-style-type: none"> 1. Conservation investments, through the improved management of High Conservation Value areas in Madagascar, with revenues in the form of Payment for Ecosystem Services (including carbon) that will reward successful operations (results-based payments); 2. Agroforestry and sustainable production, through the improvement of existing plantations (vanilla, cloves, cardamom etc.) by agroforestry techniques, improved logistics and direct route to markets, generating revenues from increased volumes and improved prices of certified commodities; and 3. Access to energy, by providing access to electricity, enabling reduction in deforestation (less slash and burn and firewood) and improvement of livelihoods, with revenues in the form of sale of power. <p>The fund is a 10 years closed ended fund, which deliver environmental, climate, social impacts in one of the most biodiversity-rich and economically-poor country in the World.</p>
Fund/Product Status	Open - committed capital
Target Close Date	Dec-16
Fund/Product Term	10 years
Impact	
Impact Description	Madagascar offers unparalleled opportunities for investing into conservation, sustainable production and clean infrastructure. In a country where ~80% of the population work in agriculture, and where rural electrification reaches only 5% of the population, appropriate and targeted investment can transform livelihoods and reverse long-term trends of environmental degradation.
Financial	
Financial Description	<p>The Fund invests into medium-term loans in 3 sets of activities: conservation, sustainable agriculture and rural electrification. Overall, USD45m is to be invested in a portfolio of c.10 investments: c. 40% conservation; c. 30% agroforestry; c. 30% access to energy/ agri-energy;</p> <p>Capital is drawn down as required across a blended portfolio creating strong and predictable cashflows. Conservation investments are made on a payment for performance basis. Agroforestry and access to energy investments are made as equity or loan investments.</p>
Currency for Fund/Product Figures	US Dollar - USD
Target Assets Under Management (AUM)	45,000,000
Minimum Investment Required	5,000,000
Target Return Category	Risk-adjusted market-rate of return

IRIS Metrics for reporting impact

External reporting is increasingly using standard metrics to help stakeholders gauge and compare performance. Of all the options available, [IRIS](#), managed by the [Global Impact Investing Network \(GIIN\)](#), is the one that seems to be gaining most traction, particularly in the Impact Investing market. IRIS is the catalogue of generally-accepted performance metrics that impact investors use to measure the social, environmental, and financial performance of their investments.

The IRIS catalogue includes a range of quantitative and qualitative metrics for:

- Financial performance (standard financial metrics such as assets and liabilities)
- Operational performance (governance policies, employment practices, social and environmental impact of their day-to-day business activities)
- Product performance (the social and environmental benefits of the products, services)
- Sector performance (impact in sectors such as agriculture, financial services, healthcare)
- Social and environmental objective performance (metrics of progress towards specific impact objectives such as employment generation or sustainable land use.)

IRIS guidance talks of developing an “impact measurement program” – which includes activities such as “determining what to measure, collecting and analysing the related information, and using the results in decision-making and reporting”. Sounds much like Open Standards. [Guidelines](#) are provided for organisations to develop a metrics program – from both the investor and investee perspectives.

A “Land Conservation” subset was developed a few years ago as one of a number of aligned catalogues. The latest version of IRIS (v4) now incorporates the [Land Conservation](#) subset into the core metric set. These metrics, along with the Environment set, provide a useful coverage for many types of conservation work.

It is difficult to develop standard metrics to cover the breadth of work undertaken by the conservation sector; in contrast it seems relatively easier to develop metrics for other social sectors, such as education rates etc. As metrics start to get used more broadly by philanthropists and impact investors, it can be expected that these other sectors will increase their “slice of the pie” of available funding unless the conservation sector collaborates to improve capabilities in this area.