



ESG

Impact Investing: Seeing The Change



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With walk-outs from Australian school students, climate change protests across the country and a no-nonsense address to the UN by Greta Thunberg - there was plenty of publicity over the quarter surrounding humans' impact on the environment. The actions also mirror a strong and growing interest among our clients and the broader community for investments that make a positive contribution to both the environment and society. This is one of the key objectives of impact investing and the focus for this quarter's ESG update.

What is impact investing?

First some groundwork before we delve deeper into the details of impact investing. An ESG approach to investing would typically consider Environment, Social and Governance factors when assessing opportunities. This could be through screening out harmful areas (a negative screen) such as tobacco and firearms. It could also assign each investment a score that would help rank different options. Impact investing takes this approach a step further and actively seeks investments that make a positive impact on the world and include a financial return.

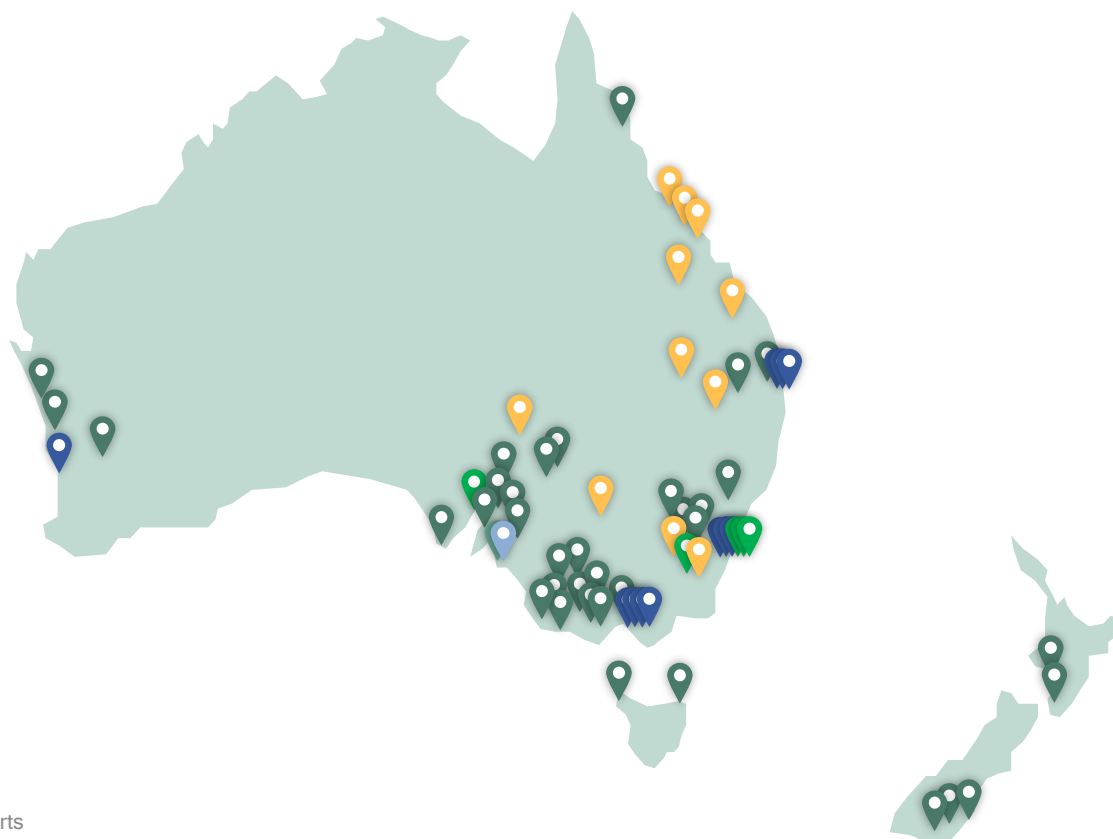
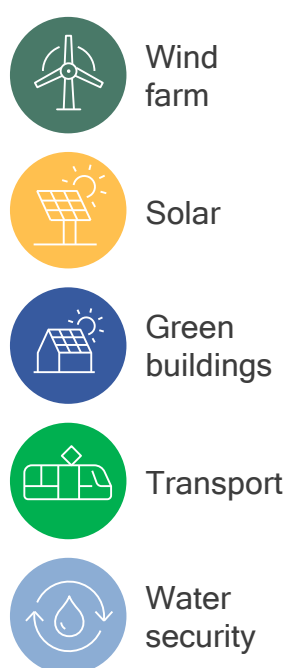
Impact bonds have been a rapidly growing area of the domestic and global bond universe over the past decade and we have provided a breakdown and overview of the different categories in the [Q3 2018 update](#). Delving deeper into these bonds, there is much more detail on the nature of their impact.

The money raised from a climate bond will be ring-fenced and can only be used for predetermined projects and not for general corporate activity. Green bonds for example finance a range of projects such as wind farms, solar panels and low carbon buildings. Similarly, the proceeds of social bonds can vary greatly and could be used provide loans to small business owners from disadvantaged backgrounds or social housing.

In turn, these projects will typically report a range of impact measures depending on their nature. For green bonds this may include the amount of renewable energy generated, carbon emissions avoided and water usage saved. For social bonds, the impacts could include the number of homeless or victims of domestic abuse housed, or underprivileged students educated. We highlighted a powerful social bond case study focused on social housing in [last quarter's update](#).

Visualising impact

Given the diversity and scale of the underlying projects for each bond, assessing and aggregating the impacts is not an easy task. This is illustrated in the map below, which highlights a range of the green projects in Australia and New Zealand that are financed in part by climate bonds within one of our portfolios.



Source: Pental, issuer impact reports

Most of the projects financed will report impact measures, such as carbon emissions avoided, which can then be aggregated by the bond issuer. These will be provided to investors in periodic impact reports. Among the large list of projects financed we have chosen our own example to highlight as a case study. The Coopers Gap Wind Farm, north-west of Brisbane, is expected to become Australia's largest when construction is completed in 2020. It will have a capacity of 453 MW of energy and produce roughly 1,510,000 MWh of renewable energy.¹



Photo: Coopers Gap, supplied by AGL

¹ AGL

Accountability

Given the importance of these outcomes, we need to hold issuers accountable for reporting impact measures and closely scrutinising the results. Some accountability is also shared with auditors who conduct annual reviews of the proceeds to ensure they are being used for their intended purpose. This forms part of the larger process from the identification of eligible projects to their ongoing monitoring as outlined below.



Source: NAB annual green bond report FY 17

One example that reflects the growing importance of accountability and transparency was a green bond issue during the quarter by European utilities provider, Enel. It became the first bond to link its coupon payments to hitting predetermined impact targets. If it does not meet its objectives then the coupon is raised, penalising the issuer. Closer to home, Sydney Airport conducted a similar style sustainability-linked loan earlier in the year.

Looking ahead

As the importance of impact investing receives greater recognition we expect the outcomes for investors to continue to improve. There are several challenges that still exist within the area where we expect further progress. This includes greater standardisation and transparency of impact reporting. We note some strides have been made to utilise some best practice, but that there is room to improve further. There is also room for greater consideration of the range of benefits produced by projects. For example, this could extend beyond measures like electricity produced to encompass the number of jobs created by a project and other benefits for a local community.

Overall with further evolution expected we are excited to lead the way by delivering impact investing strategies that best meet the needs of our clients. This includes assessing the best opportunities in the area and providing our investors with the comfort that their investment is having a positive impact on the world around them whilst still delivering a financial return.

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