

# LEVEL EEI

## WORKSHOP 1: GENERATING MORE IMPACT IN PUBLIC MARKETS

BY NICOLA KOCH (2DII)



# Workshop agenda

**Phase 1:** introducing impact mechanisms in public markets and (15 min)

**Phase 2:** collective work on minimum requirements for impact mechanisms in public markets (full group, 30 min)

**Phase 3:** presentation of an impact assessment framework for financial products (15 min)

**Phase 4:** improving the impact potential of specific products (small groups, 55 min)



# Phase 1: introducing impact mechanisms in public markets

Investor Impact Mechanism		Type of change	Evidence Level	Requirements	Limitations	Typical asset classes
Grow new/undersupplied capital markets		Enabling growth	B	<ul style="list-style-type: none"> <li>Investment in companies with net positive impact</li> <li>Companies growth is limited by external financing conditions</li> </ul>	<ul style="list-style-type: none"> <li>Not suited for investments in large, established companies, which have sufficient access to external financing</li> </ul>	Private markets
Provide flexible capital			B		<ul style="list-style-type: none"> <li>Not suited for companies that have sufficient access to philanthropic or commercial capital</li> </ul>	
Engage actively	Provide non-financial support		B	<ul style="list-style-type: none"> <li>Investment in companies with net positive impact</li> <li>Investors with know-how, reputation or network that helps companies grow faster</li> </ul>	<ul style="list-style-type: none"> <li>Only suited for early-stage investments, where investors can directly influence the company</li> </ul>	
	Shareholder engagement	Encouraging improvements	B	<ul style="list-style-type: none"> <li>Focus on meaningful improvements that companies can achieve at a reasonable cost</li> <li>Investor with strong influence on a company</li> </ul>	<ul style="list-style-type: none"> <li>Limited to incremental improvements; unlikely to transform industries</li> </ul>	Public markets
Signal that impact matter			C	<ul style="list-style-type: none"> <li>Transparent ESG criteria that companies can meet at reasonable cost</li> <li>Substantial portion of the market screening out or underweighting firms that don't meet the criteria</li> </ul>	<ul style="list-style-type: none"> <li>Effect unlikely for industry exclusion</li> <li>Disagreement on how to measure ESG criteria</li> </ul>	
	Non-market signals	Growth or improvement	D	<ul style="list-style-type: none"> <li>High level of public visibility of the signal</li> </ul>	<ul style="list-style-type: none"> <li>Impact is difficult to evaluate as it is indirect and depends on political action or cultural change</li> </ul>	

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Phase 2: collective work on definitions /  
minimum requirements for impact mechanisms  
in private markets

# Shareholder engagement/stewardship

## Strategies:

- Engagement
- Voting

## Examples:

- Hermes EOS
- Engine No 1

# Shareholder engagement/stewardship

## Definition:

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- Voting

## Examples:

- Hermes EOS
- Engine No 1

## Impact moderators:

- Size
- Access to management/board
- Specific objectives and clear milestones
- Detailed escalation policy
- Full use of shareholder authority
- Coordinated engagement



# Shareholder engagement

## Impact moderators:

- Size
- Access to management/board
- Specific objectives and clear milestones
- Detailed escalation policy
- Full use of shareholder authority
- Coordinated engagement

## Questions:

- Which best-practices do you know ?
- Are impact moderators missing?
- What are important KPIs to watch?
- How would you define relevant thresholds for those KPIs?

# Market/price signalling

## Strategies:

- Positive screening
- Negative screening
- Thematic screening
- Tilting

## Examples:

- Taxonomy aligned Art 9 funds

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## Impact moderators:

- The deviation from conventional index of the sustainable allocations
- The elasticity of stocks
- the fraction of wealth commanded by sustainable investors
- the size of the sustainable inflows or outflows vs the investment universe
- the concentration of trades by sustainable investment funds
- the similarity of screening filters across sustainable funds

# Market/price signalling

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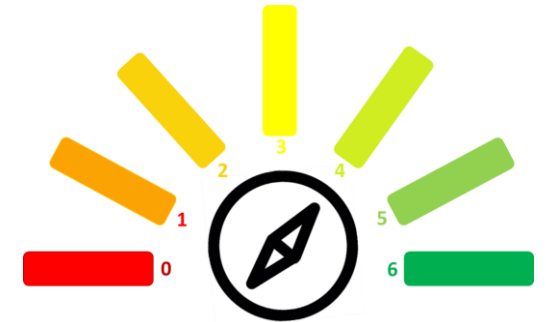
## Questions:

- Which best-practices do you know ?
- Are impact moderators missing?
- What are important KPIs to watch?
- How would you define relevant thresholds for those KPIs?

# Phase 3: presentation of an impact assessment framework for financial products

# Description of the two-step methodology

1. Attributing an average impact potential rating to each product category, based on IMP's investor contribution categories
  - From 0 to 6
2. Attributing an impact exploitation score for specific products within a category
  - Each product receives a rating (0, +, ++ or +++) based on its ability to exploit the full impact potential of its product category



Rating	Total score (as % of maximum score for the product category)
0	0
"+"	$0 < x < 33\%$
"++"	$33\% < x < 66\%$
"+++"	$x > 66\%$

# “Climate impact potential synthetic rating” methodology

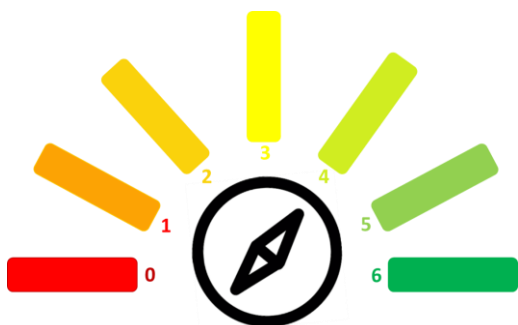
1. Synthetic score = Category Impact Potential Score \* Product Exploitation Score
2. The synthetic score is transformed into a synthetic rating
  - 0 => G
  - ]0;1] => F
  - ]1;2] => E
  - ]2;3] => D
  - ]3;4] => C
  - ]4;5] => B
  - ]5;6] => A



Product  
XXX

### Category impact potential

*How high is the impact potential of the product category?  
From 0 to 6*



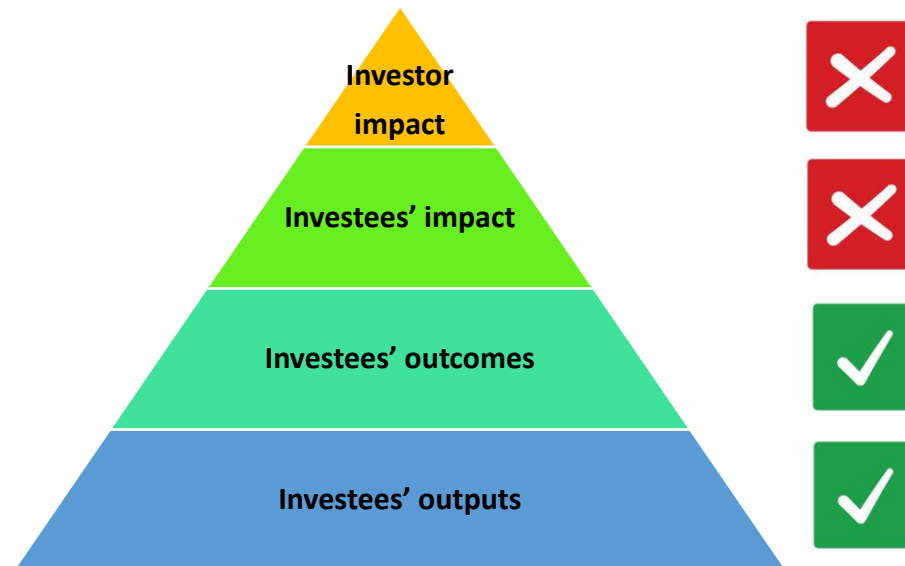
### Potential exploitation (of the product)

*How much does the product exploit the impact potential of its category?  
From 0 to +++*

++

### Impact evaluation (by the product)

*Which effects on the real economy does the product carefully evaluate (quantitatively or qualitatively)?*



## Product's Climate Impact Potential Synthetic Rating

*(based on category impact potential and potential exploitation scores)*



Highest impact potential

Lowest impact potential



		No impact potential	Low impact potential	Median impact potential		High impact potential		
IMP Investor contribution categories		0	1	2	3	4	5	6
Applied impact mechanisms		None	S	SE	SG/SF	SEG/SEF	SGF	SEGF
Product categories	Green impact investing funds				X	X	X	X
	Thematic VC/PE funds		X	X	X	X	X	X
	Thematic private debt funds		X	X	X	X	X	X
	Sustainability-linked loan funds				X	X	X	X
	Sustainability loan funds		X	X	X	X	X	X
	Thematic infrastructure funds				X	X	X	X
	SIB funds				X		X	X
	Microfinance / Solidarity funds				X		X	X
	Thematic crowdfunding				X		X	X
	Thematic PtoP				X		X	X
	Sustainable saving accounts				X		X	X
	SDG Engagement funds			X				
	ESG Engagement funds			X				
	Best-in-class equity funds		X	X				
	Exclusion equity funds		X	X				
Thematic equity funds		X	X					
Low-carbon equity funds		X	X					
Sustainability bond funds		X						
Sustainability-linked bond funds		X						

S = Signalling

E = Engage actively

G = Grow undersupplied markets

F = Provide flexible capital

## In need for qualifying questions for each product category

Which questions to ask for assessing the exploitation score of specific products in each product category ?

Ex: Green public equity funds

Ex: Green public bond funds

Ex: Green engagement funds



## Phase 4: improving the impact potential of specific products

# Improving the impact potential of specific product categories

## Product categories

Choose one product category among the following ones:

- Green public equity funds
- Green public bond funds
- Green engagement funds

## Questions to answer

- Can you formulate minimum requirements for the impact moderators for your specific product (focus on one or more sub-categories)?
- Are there existing guidelines for designing minimum requirements for your moderators?
- What would be your strategy to maximally exploit the impact potential of your products category?
- List specific questions to ask for assessing impact potential of products in your category

# Improving the impact potential of specific product categories

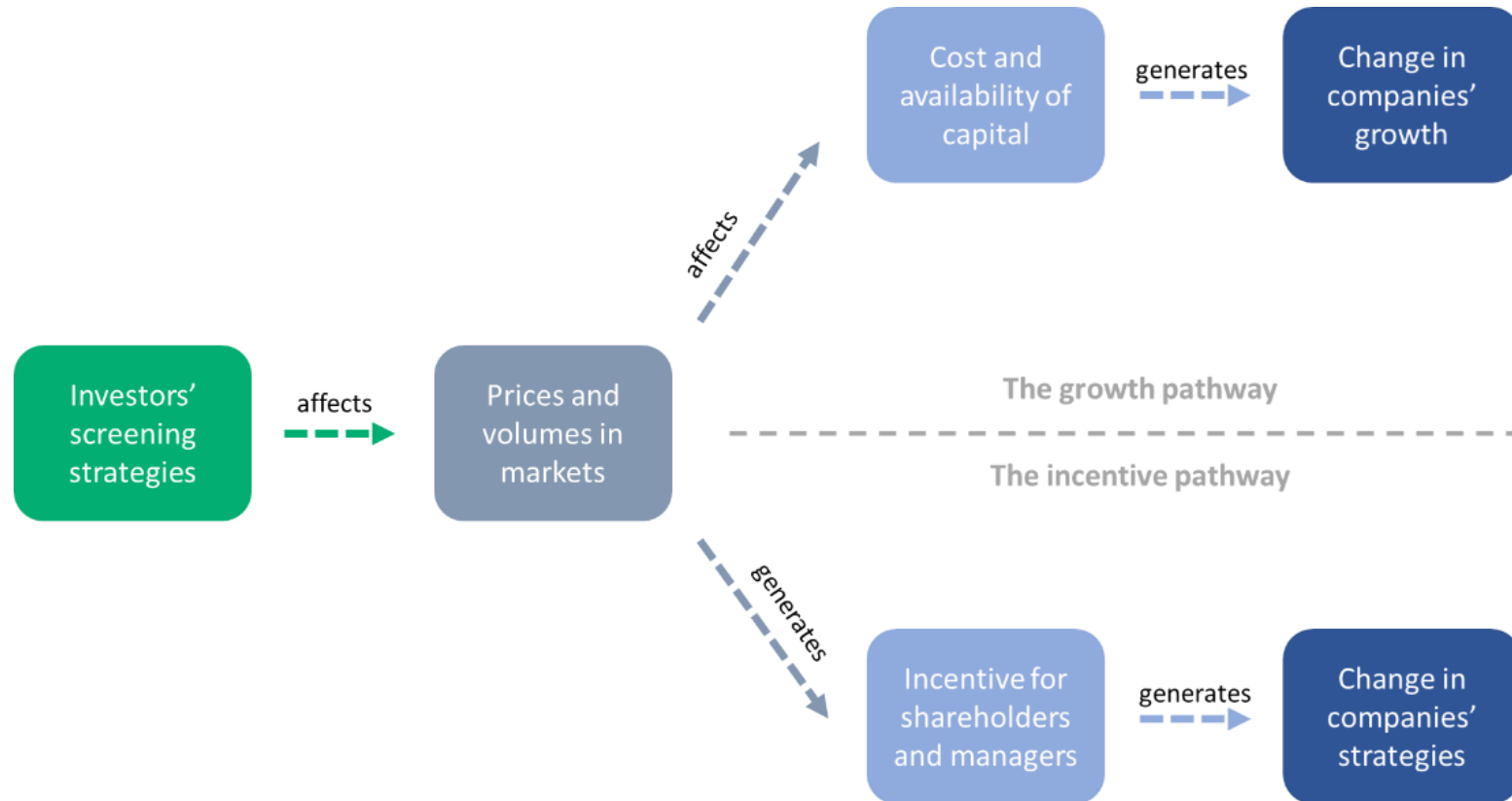
## Impact moderators for stewardship:

- **Size**
- **Access to management/board**
- **Specific objectives and clear milestones**
- **Detailed escalation policy**
- **Full use of shareholder authority**
- **Coordinated engagement**

## Impact moderators for market signalling:

- **Deviation from conventional index of the sustainable allocations**
- **Elasticity of stocks**
- **Fraction of wealth commanded by sustainable investors**
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- **Similarity of screening filters across sustainable funds**

# Annex



# Annex

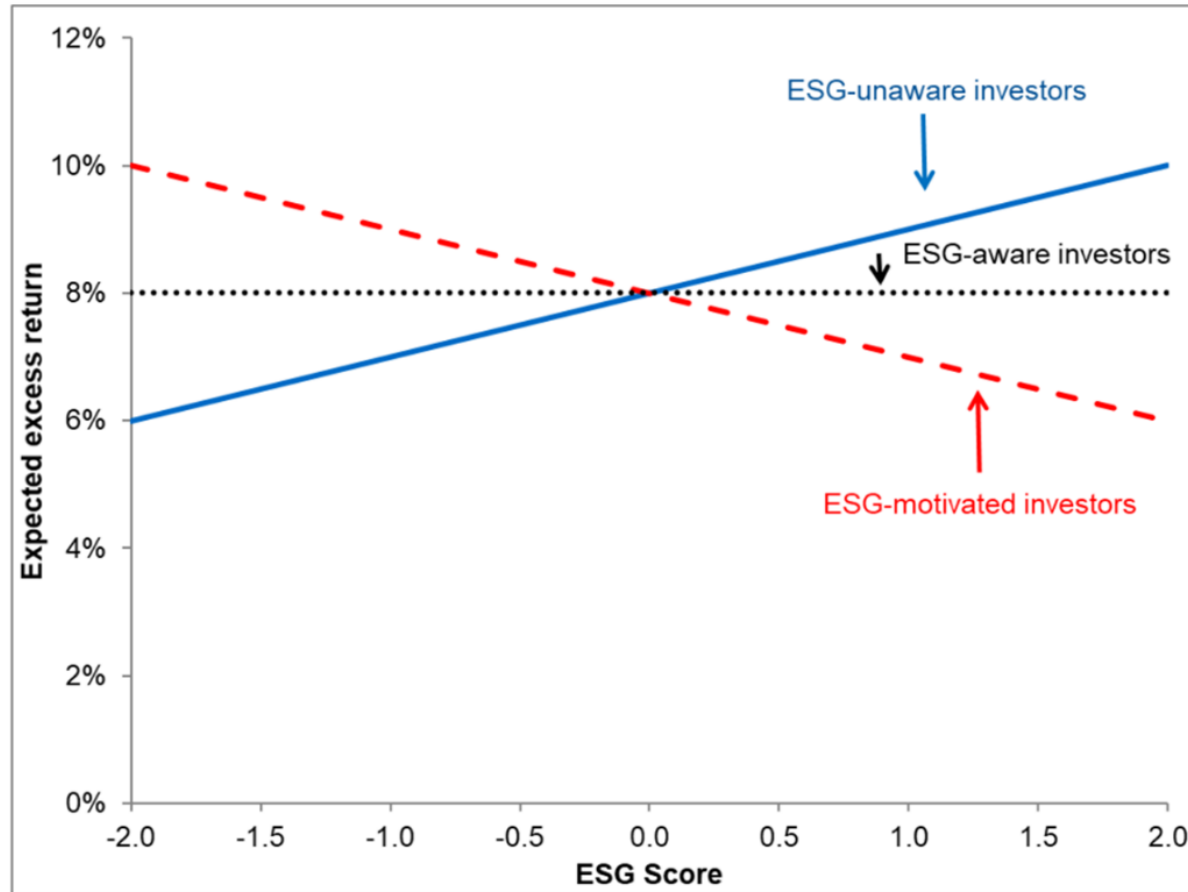


Fig. 2. ESG-CAPM

Figure 1 | The Impact Classes available

**IMPACT OF UNDERLYING ASSETS / ENTERPRISES**

		<b>A</b>	<b>B</b>	<b>C</b>	
		<b>Act to avoid harm</b>	<b>Benefit stakeholders</b>	<b>Contribute to solutions</b>	
<b>INVESTOR'S CONTRIBUTION</b>	<b>1</b>	Signal that impact matters + Engage actively + Grow new/undersupplied capital markets + Provide flexible capital	E.g. Ethical bond fund	E.g. Positively-screened / best-in-class ESG fund	E.g. Sovereign-backed bonds (secondary market) funding vaccine delivery to understand people or renewable energy projects
	<b>2</b>	Signal that impact matters + Engage actively + Grow new/undersupplied capital markets + Provide flexible capital	E.g. Shareholder activist fund	E.g. Positively-screened / best-in-class ESG fund using deep shareholder engagement to improve performance	E.g. Public or private equity fund selecting and engaging with businesses that have a significant effect on education and health for underserved people
	<b>3</b>	Signal that impact matters + Engage actively + Grow new/undersupplied capital markets + Provide flexible capital	E.g. Anchor investment in a negatively-screened real estate fund in a frontier market	E.g. Positively-screened infrastructure fund in a frontier market	E.g. Bond fund anchoring primary issuances by businesses that have a significant effect on environmental sustainability, access to clean water and sanitation
	<b>4</b>	Signal that impact matters + Engage actively + Grow new/undersupplied capital markets + Provide flexible capital	<i>Investment archetypes not yet defined</i>	E.g. Positively-screened private equity fund making anchor investments in frontier markets	E.g. Private equity fund making anchor investments in businesses that have a significant effect on income and employment for underserved people
	<b>5</b>	Signal that impact matters + Engage actively + Grow new/undersupplied capital markets + Provide flexible capital	<i>Investment archetypes not yet defined</i>	<i>Investment archetypes not yet defined</i>	E.g. Below-market charity bonds, or an unsecured debt fund focused on businesses that have a significant effect on employment for underserved people
	<b>6</b>	Signal that impact matters + Engage actively + Grow new/undersupplied capital markets + Provide flexible capital	<i>Investment archetypes not yet defined</i>	<i>Investment archetypes not yet defined</i>	E.g. Patient VC fund providing anchor investment and active engagement to businesses that have a significant effect on energy access for underserved people



# Impact scoring

- Caldecott et al. (2022) argue that, in order to have a positive environmental impact, investors or financial institutions must make a clear and measurable difference in one or more of the following ways:
  - reducing (increasing) the cost of capital for (un)sustainable activities;
  - increasing (reducing) access to capital for (un)sustainable activities;
  - encouraging or enabling sustainable practices by counterparties, such as companies, sovereigns, and individuals.

**Table 3: Potential Impact Rating Scorecard**

	Public equity	Fixed Income (bonds)	Fixed Income (loans)	Private Equity	Real Assets	Hedge Funds
Cost of capital	1 / 3	2 / 4	3 / 5	2 / 3	2 / 3	2 / 4
Access to liquidity	1 / 3	2 / 3	3 / 5	2 / 4	1 / 3	1 / 4
Adoption of practices	2 / 4	1 / 3	3 / 5	3 / 5	2 / 4	1 / 4