

ALTERNATIVES

The Five Building Blocks of Effective Impact Management

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No single, unified best practice has yet emerged for impact investing, and a proliferation of methodologies and metrics has introduced an element of confusion. Simply navigating through all the resources available to impact investors can be a challenge. In the second post in this three-part series, our Franklin Real Asset Advisors team, in collaboration with consulting firm Tideline, help guide us through what they call the “five building blocks” of effective impact management.

As impact investing gathers pace, investors are refining their approach from an early emphasis on impact *measurement*—the practice of quantifying impact outputs and outcomes—to focus on impact *management*, a forward-looking approach that integrates impact considerations into each stage of the investment process. This new focus aims to understand an investment’s impact more fully and improve social and environmental performance throughout the lifetime of an asset.

The different frameworks and tools available to impact investors can be classified into five broad categories: objectives, standards, certifications, methodologies and metrics. These building blocks come into play at different stages of the impact management process. The table below illustrates a selection of the most prominent and widely accepted examples in each category.

Taxonomy of Impact Investment Management Tools and Frameworks

Category	Description	Examples
Objectives	Common language around social and environmental objectives for aligning the supply of and demand for impact capital.	UN Sustainable Development Goals
Standards	Broad guidelines that provide a common basis for evaluating investor practices.	International Finance Corporation's Operating Principles for Impact Management
Certifications	Standardized, third-party analyses for concisely communicating social and/or environmental performance.	Aeris Impact Management Ratings, BREEAM
Methodologies	Instruments for facilitating the diligence, assessment, monitoring, and reporting of impact.	Impact Management Project, bespoke methodologies
Metrics	Standardized definitions for measuring impact and comparing investments.	Global Reporting Initiative (GRI), IRIS (e.g., PI5501: # students per classroom)

Source: Franklin Real Asset Advisors and Tideline. For illustrative purposes only.

Objectives

The numerous interpretations of impact objectives have posed a challenge to investors and entrepreneurs seeking to align around a shared set of goals. As an extension of the [Millennium Development Goals](#) launched in 2000, the creation of the [UN Sustainable Development Goals](#) (SDGs) was a significant step forward in the pursuit of a universal framework. These goals have helped align the public, private and philanthropic sectors around 17 broadly recognized social and environmental priorities.

Many asset owners and managers are either designing new investment strategies to support the SDGs or highlighting how existing strategies are aligned with the goals. Of investors who responded to Global Impact Investing Network's (GIIN's) 2019 survey, 60% track the performance of at least some of their impact investments to the SDGs.¹ Another 15% plan to do so in the future.²

However, a challenge for investors is the lack of clarity on what precisely it means to be "aligned with" or to "advance" the SDGs. Several efforts are underway to spell out what this means in practice, including the United Nations' Principles for Responsible Investment (UNPRI) market map, the Dutch SDG Investing Initiative and the United Nation's Development Program's (UNDP's) SDG Impact, among others. A more precise definition will help impact investors communicate more clearly about their goals, better set expectations and strengthen accountability.

Standards

In light of unsubstantiated impact claims, or “greenwashing,” standards can help investors be more confident about what social and environmental practices are expected of them, and inform society of what to expect of impact investors.

The market has been eager for a set of industry-wide best practices, and in 2018, the International Finance Corporation (IFC) released the Operating Principles for Impact Management. The principles were developed in partnership with more than 15 organizations to encourage authenticity and transparency on the part of investors. By following the IFC’s principles, investors can more readily assess the impact of their strategies. However, as no specific practices are prescribed, this can present some challenges for investors.

Certifications

Impact investing is still a burgeoning space where identifying impactful companies, assets or fund managers can be challenging. Certifications can be used by investors as valuable indicators in screening and due diligence, as well as to demonstrate and report impact performance. They help to verify the quality and validity of impact approaches and build trust between parties.

Third-party certifications range from sector-specific ratings to much broader multi-sector benchmarks. They include standards for particular industries, such as the Building Research Establishment Environmental Assessment Method (BREEAM) for sustainable real estate and Aeris Impact Management Ratings in US community development, as well as broad ratings such as the Global Impact Investing Rating System (GIIRS) for the fund management industry and the B Impact Assessment to certify B Corporations, a class of impact-seeking enterprises.

Despite the proliferation of certifications, many asset owners are still not armed with enough nuanced data to gain comfort in asset managers and their impact management processes. In the coming years, more flexible and robust certifications need to be created to better and more precisely assess impact management strategies across asset classes.

Methodologies

Universal methodologies like the Impact Management Project’s dimensions of impact (What, Who, How Much, Contribution, and Risk) are emerging as best practice for the industry and have been adopted by a diverse group of investors and entrepreneurs. However, it is still common for investors to customize the Impact Management Project’s methodology or develop their own to fit their unique priorities and needs.

Metrics

Before the development and adoption of standard metric sets like the Global Impact Investing Network’s (GIIN) Impact Reporting Investment Standards (IRIS) and the sustainability metrics developed by the Global Reporting Initiative (GRI), some companies and investors measured social and environmental impacts, but it was impossible to compare performance.

Approaches for what to measure and how to report on impact varied widely. The credibility of impact measurement suffered as a result, causing some to be skeptical of impact investing more broadly.

Benefitting from nearly a decade of use and refinement since it was first introduced, IRIS has emerged as the most widely recognized and applied framework for metrics among impact investors. IRIS combines metrics from different industries into one central system.

According to the 2018 GIIN survey, 59% of respondents use IRIS metrics in their impact management practice.³ While often a core resource, many investors have found it beneficial to supplement IRIS metrics with proprietary metrics, qualitative information, and/or additional external frameworks and standards. As such, the most common approach for investors surveyed by the GIIN is to use a combination of select standard, portfolio-wide metrics with other indicators as appropriate.

These five building blocks enable the practice of impact management to be more efficient, robust and consistently implemented. To understand how the tools are used in practice, we will explore their use in a particular strategy in part three of this series.

Robust systems for impact management that are embedded end-to-end in the investment process have come to play a central role in the maturing impact investing market. Drawing on a suite of tools and frameworks—ranging from broad objectives to precise impact metrics—investors are increasingly empowered to understand, manage, and improve the social and environmental outcomes of their investments.

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[1.](#) Source: Global Impact Investing Network (GIIN) Annual Impact Investor Survey 2019. This report captures data from 266 impact investors collected via a survey distributed during January and February 2019.

[2.](#) Ibid.

[3.](#) Ibid.