Impact Consortium Global Advisory Panel Discussion Points

【Date & Time】 Friday, November 1, 2024 22:00–23:30 (JST)
【Venue】 Online
【Agenda】

1. Opening
2. Introduction of Japan's Initiatives "Japan's Current Situation"
3. Panel Discussion "Current Global Status, Challenges and How to Collaborate"
4. Closing

1. Opening

(1) Opening Remarks (Mr. Akitaka Fujii, Co-Chairs, Global Advisory Panel Planning Committee)

- Launched in November 2023, the Impact Consortium is a forum for a wide range of stakeholders to share their experiences and expertise in order to promote and expand impact investing.
- Today's Global Advisory Panel is part of the Impact Consortium's efforts to engage with global leaders in the impact investing community. Through this, it aims to promote impact investment initiatives.

(2) Opening Speech (Professor Tsuyoshi Mizuguchi, Takasaki University of Economics)

- The immediate goal of the Impact Consortium is to promote the concept and practice of impact finance. Expanding impact finance is not the end goal, but a tool for achieving a more sustainable society.
- Challenges such as climate change, biodiversity loss, and Japan's declining birthrate and aging population are caused by economic and social system, and systemic transformation is needed to solve them. The conversation today is a valuable opportunity to hear the opinions and advice of those who have led the impact investing field on an international scale.

2. Introduction of Japan's Initiatives "Japan's Current Situation"

(1) Overview of the Impact Consortium in Japan (Mr. Akitaka Fujii, Co-Chairs, Global Advisory Panel Planning Committee)

- The Impact Consortium aims to push the boundaries of what impact investing can achieve by refining practical solutions for investors and companies.
- The Impact Consortium has four working groups, each focused on addressing unique aspects of impact investing.
  - Data and Indicators Working Group: Aims to make it easier for investors and

companies to collect and analyze impact data and identify practical KPIs.

- Market Research and Formation Working Group: Discusses how to link impact to the enhancement of corporate value and aims to form an impact market, especially targeting listed companies.
- Local Finance and Evaluation Practices Working Group: Shares case studies focused on integrating impact into assessment processes, with the objective of unlocking value in local companies.
- Public-Private Partnership Promotion Working Group: Promotes collaboration between local governments and impact startups to enhance solutions for societal challenges.

(2) Japan's Impact Investment Market and Initiatives (Mr. Ken Shibusawa, Chairman of GSG Impact Japan)

- Impact investing in Japan started gaining traction in 2014, following the work of the UK government the previous year, and was initially spearheaded by the social-sector more than the investor community.
- An import moment for impact investing in Japan was the founding of the "Council of New Form of Capitalism Realization", which sought to achieve "a virtuous cycle of growth and distribution". However, the key turning point was when "New Capitalism" was defined not as rejecting capitalist principles, but rather, enhancing capitalism by incorporating externalities left behind by capitalism. The work of the "Council of New Form of Capitalism Realization" helped position impact investing as a key economic policy on the Japanese government's agenda, sparking Japanese investors interest in impact investing.
- In the West, impact investing is still quite niche, but in Japan, large companies are taking a serious look at it.
- Sir Ronald Cohen has frequently used the term "post-ESG". ESG investing has focused on encouraging the disclosure of the non-financial value of companies, which is what companies now disclose in their sustainability reports. But in a post-ESG world, the emphasis should be on the impact companies are having on society and environment. One way of increasing the transparency of the companies' impacts is through impact accounting, which focuses on monetizing companies' social and environmental values.
- A paradigm shift is necessary for impact to take hold in the economy. Investors initially were the instigators for more sustainability information and companies mostly just disclosed requested information. But companies need to be in the driver's seat because they are the ones creating value. Companies should be proactive in communicating their impact story to investors.
- At the "Council of New Form of Capitalism Realization" held 2 days ago, which was

succeeded by the Ishiba administration, I stated my opinion about enhancement of the quality of engagement between companies and investors and impact is also the key part of this. We aim to transition from an investor-centered impact investment ecosystem to an impact economy, where companies have an intention of solving societal challenges, with investors supporting them, thereby co-creating a better future.

(3) Initiatives by Financial Institutions in Japan (The Japan Impact-Driven Financing Initiative, Deputy Secretary-General, Ms. Yuka Ogasawara)

- The Japan Impact-Driven Financing Initiative (IDFI) is a platform established in November 2021 with the vision of transforming the flow of funds handled by financial institutions to be as impact-oriented as possible and creating a sustainable flow of funds that can solve environmental and social issues.
- IDFI supports both a top-down approach that promotes managing financial organization for impact, as well as a bottom-up approach that advances IMM practices in individual investments and loans.
- IDFI holds monthly steering committee (SC) meetings, where SC members are balanced in asset class, gender, and age. There are six working groups: regional finance, social metrics, venture capital, asset owner and asset management, loans and bonds, and impact driven corporate-value enhancement alliance. Last year, 52 working group meetings and 22 events were held, with more than 2,000 participants in total.
- Recent key discussion points include: (1) the engagement of the entire investment chain, including individuals and asset owners (like pension funds), (2) IMM "Dos and Don'ts" for specific asset classes, and (3) investing for managing systemic risks and system-level impact.

(4) Views on the Impact/Outcomes of PRI (Mr. Tatsuro Yuzawa, Head of Japan, PRI)

- The Principles for Responsible Investment (PRI) is a global initiative supported by the United Nations to implement responsible investment, and there are approximately 5,300 signatories worldwide, 140 in Japan, including asset owners, investment managers, and service providers. In our 2023 reporting, approximately 80% of signatories have identified sustainability outcomes related to their investment activities.
- PRI supports investors across a spectrum of progression pathways. On one end, investors are maximizing financial returns by incorporating ESG factors and on the other end, investors are meeting financial objectives while pursuing positive impact.
- In 2005, UNEP FI and Freshfields found that ESG factors can, and should, be integrated into investment decision-making. In 2015, PRI found that ESG integration was not optional, but rather a requirement of fiduciary duties. Furthermore, in 2023 PRI noted investors should not only consider how ESG risks affect returns but should also

consider how the impacts (externalities) of their investments affect returns through system-level risks.

- Through the "LFI" (A Legal Framework for Impact) project, it has become clear that the pursuit of impact is not limited to the practices of specialized investors (i.e. impact investors). The consideration of impact is consisted with the duties of asset owners under an "instrumental IFSI (Investing for Sustainable Impact)" concept.
- The 2023 LFI Japan Report made five recommendations to help investors position themselves correctly to play a role in achieving Japan's sustainability goals.
- Japanese life insurers have been working on impact investing and system-level investing. As pension investors could consider adopting similar practices, Japan is continuing to define the practices of impact investing with a broad scope, incorporating different actors.

3. Panel Discussion "Current Global Status, Challenges and How to Collaborate"

Moderator: Mr. Masato Nakamura, Co-Chairs, Global Advisory Panel Planning Committee

Panelist

- Mr. Sean Gilbert, Chief Investor Network Officer, Global Impact Investing Network (GIIN)
- Mr. Mike McCreless, Founder and Executive Director, Impact Frontiers
- Mr. Douglas Sloan, Managing Director, Better Society Capital
- Mr. David Freiberg, Impact Investing and Accounting lead, Senior manager, Climate Change and Sustainability Services (CCaSS), EY Japan

(1) Comments on Japan's presentation

- GIIN, Mr. Sean Gilbert
  - GIIN is a network of financial institutions established about 15 years ago with the aim of facilitating the growth of impact investing.
  - In general, investors incorporate environmental and social factors into their investment decisions for a variety of reasons, such as preparing for future risks, aligning with values, addressing specific societal problems, or the belief impact will help achieve better long-term returns. The way Japan is building momentum around impact investing can support the achievement of Japan's long-term social and economic development.
  - In Japan, investors are targeting specific priorities such as the declining birthrate and aging population, eliminating regional disparities, and promoting innovation in environmental technologies. Impact investing can help inform markets about how to most effectively allocate resources to address these challenges.

- Better Society Capital, Mr. Douglas Sloan

- He has dual roles as Managing Director of Better Society Capital, formerly known as Big Society Capital, and as co-founder of Impact VC – global community of VCs coming together to learn from each other and accelerate impact investing efforts.
- Some of the comments in Japan's presentation, such as adopting impact measurement and management practices by asset class and integrating a system-lens for risk and investment outcomes, resonate with what has occurred in the UK over the past decade or so.
- With regards to building an impact ecosystem, Japan has a great opportunity to jump directly to where countries like the UK have taken over a decade to reach.

- Impact Frontiers, Mr. Mike McCreless
  - Impact Frontiers is a not-for-profit field-building organization that helps investors measure and manage the impacts of their investments. Impact Frontiers' work focuses on addressing gaps in existing impact frameworks and tools by bringing together hundreds of investors to create practical solutions.
  - Looking to the future of impact investing in Japan, there are a few possible futures:
    1. The first, impact investing may just be a fad. Investors will use impact for labeling to attract funds, but short-term profits will remain the priority. If this is the case, the assets will likely be gone in 5 years and not much will change.
    2. The second is the possibility of succeeding in using impact investing to drive social change for individual communities and the financial environment. This might be profitable, or it might require support from philanthropy or blended finance. Either outcome would be an overall success, as it would help investors achieve their goals while reducing the burden on governments and society.
    3. The third is impact investing becomes the new way the financial sector operates. This also requires the help of policymakers and outlines the importance of the efforts the FSA is taking.

- EY Japan, Mr. David Freiberg
  - Based in Japan, he leads impact investing and impact accounting at EY.
  - The focus on a paradigm shift and system-level investing is critical if Japan is going to successfully accelerate the growth of impact investing and integrate it into mainstream capital markets.
  - In recent discussions with large institutional investors in New York, a reoccurring theme has been the risks associate with keeping "impact investing" as its own separate practice. We need to focus on how we integrate the principles of impact investing into mainstream investing practices. Japan should continue to nurture and grow impact investing to expand its track record and success stories, but also seek

how to engage non-impact investors. This is how capital markets will really change.

- ■ Japanese investors, financial institutions and corporations are beginning to focus on telling their unique impact stories. They should continue to advance these efforts as it reflects what could be a global competitive advantage. Many are watching to see if Japan can build an effective impact ecosystem embedded in its financial system.

(2) From an impact investing perspective, what issues should we focus on in the future?

- GIIN, Mr. Sean Gilbert
  - ■ The basic idea of impact investing is to understand an environmental or social problem or need, think about solutions, identify the range of investments that could deliver those solutions, and systematically develop an investment strategy that delivers a financial return and a positive impact. It can be applied to any important issue.
  - ■ Our past surveys have shown that many impact investors have chosen to focus on social challenges, such as ensuring access to affordable housing, healthcare, and education. According to GIIN's research (available on GIIN's website), financial inclusion and access to clean energy have been two of the most frequently prioritized areas over many years. This is likely at least partially due to the fact these areas are relatively easily understood by investors and have business models with clear cash-flows and which also can provide goods or services needed by vulnerable or underserved populations.
  - ■ Impact investing is most effective when specific gaps or unmet needs can be clearly identified and described. For example, all medical care is valuable, but focusing on additional medical care facilities for well-supported populations has a different societal impact than, for example, extending primary care coverage to underserved communities and regions.

- Impact Frontiers, Mr. Mike McCreless
  - ■ Next year's themes for Impact Frontiers' programs supporting impact management will be climate change and health equity. These are areas of consistent interest from investors and are pressing environmental and social challenges.
  - ■ As Mr. Shibusawa mentioned, it is companies that create social value, for the most part, and investors provide the necessary capital to these companies. However, when investors declare themselves "impact investors", there is an expectation that they themselves are creating some value. Therefore, Impact Frontiers is focusing on the contribution of investors in how their specific actions drive social change and how their impacts are reported in a meaningful way.

(3) What are the key takeaways for connecting impact to financial returns?

- Better Society Capital, Mr. Douglas Sloan
  - There are places where there is a trade-off between impact and financial return, and places where there is not. Where there is no trade-off is in venture capital (VC). It is important to look at this relationship at the business model-level. A key driver is the trend of people looking to buy, work, and invest in-line with their values. This gives a competitive advantage to companies with impacts imbedded in the heart of the activities, as it affects how they retain investors, retain talent, engage with customers, and engage with regulators.
  - One example of this is a company called Wagestream, which partners with employers to offer financial products that improve employee benefits. If Wagestream can show evidence that workers' lives have improved, there will improve its ability to sell to employers. This creates a clear loop between impact and financial performance, which is the exact type of driver we are looking for to connect impact and returns.

- EY Japan, Mr. David Freiberg
  - Early evidence by Harvard Business School already shows that impact leaders tend to outperform other groups. However, there is still work to be done around establishing the clear pathways by which specific company-level value is being created.
  - Most sustainability reports are "disclosure-oriented" and focus on simply disclosing large amounts of information. This results in companies not prioritizing a clear, quantitative connection between their sustainability performance and their medium- to long-term strategy.
  - Impact accounting is the process of valuing and converting social and environmental impacts into monetary values, thus allowing a direct comparison to financial value. This is one way of establishing a quantitative path between a material, measurable impact and a company's performance. One potential application of impact accounting is that it can allow us to treat impact information in a similar way how we are treating financial information.

(4) What should be done to prevent impact washing?

- Better Society Capital, Mr. Douglas Sloan
  - It is important for impact investors to base their investments on three pillars: Intentionality, Additionality, and Measurability.
  - When it comes to intentionality, it is important to understand where impact is positioned within the investment thesis, as well as the company's culture, incentive structure, and how it operates.

- In terms of additionality, this refers to what was achieved that would not have been possible without the investment. Depth and importance of the impact is more important than just being part of the journey; it's more about making a substantial difference.
- Measuring impact can vary in complexity depending on the stage of the investment, but it is important to understand and prove what changes have been made. In addition, measuring impact is even more important for the internal management of the business than it is for reporting (but is still very important for reporting, as well).

(Mr. Masato Nakamura, Co-Chairs, Global Advisory Panel Planning Committee)
We are pleased to know that these ideas are included in the guidelines published by Japan's Financial Services Agency and align with global standards.

(5) What can the public sector do in public-private partnerships?

- GIIN, Mr. Sean Gilbert
  - From what we see in different parts of the world, and there are three ways the public sector can support impact ecosystems:
    1. The first are policies for the real economy. Policies such as subsidies, taxation, permits, etc. have significant impact on the revenues and costs of running a business. This, in turn, will influence the relative attractiveness of one investment as compared to another and private investors' willingness to deploy their capital.
    2. The second is through providing catalytic funding to support growth. In most markets, it is very important to have some investors that are willing to play a catalytic role (e.g. investors that will take a junior position in blended structures, investors that are willing to place funds with new managers that may lay a track record, etc.) in order to stimulate the flow of capital into segments that are perceived as high risk or complex. In many parts of the world, you can find examples of governments who have created programs that provide catalytic capital in some form.
    3. The third is the supervisory role. This includes rules on product labeling and fiduciary duty among other things. It is important to clarify the role that impact plays within fiduciary duties. Investors need to be free to structure funds and decide the combination of impact-risk-return that they wish to pursue with their capital. There are multiple ways to structure a portfolio to achieve a given set of financial goals in conjunction with meeting impact goals at the same time. Since there are multiple ways to construct portfolios and it is possible to achieve multiple goals in the process, it may not always be necessary to identify

a specific relationship between impact and financial performance.

- Impact Frontiers, Mr. Mike McCreless
  - The biggest risk that impact investing will simply become a trend is the expectation that impact-driven investments will always deliver superior financial outcomes. We need to analyze both impact and financial performance separately to understand both separately and then how they interact. Capital can be allocated confidently and with full understanding after this.
  - Impact analysis and financial analysis are handled by different teams and functions, often creating silos. Breaking down these silos is important to become skilled allocators of capital to the right opportunities. Breaking down these silos is critical for derisking impact investing being a trend.
  - Regulators can play an important role in creating fund labeling clarity. Japan has begun to do great work, first in the paper released by the FSA, and also by examining and incorporating lessons from what is working in the EU.

(6) What actions should Japanese impact investors and startups take to collaborate with global impact investors and startups?

- EY Japan, Mr. David Freiberg
  - The first is international cooperation. Japanese organizations need to build international teams and then actively work to incorporate international norms into their internal and external operations. This will help Japanese investors and startups understand international business practices and foster stronger international relationships.
  - The second is supply chain cooperation. There are a lot of opportunities to collaborate on topics of building climate and socially resilient supply chains. This is also a great way for larger companies for support impact start-ups. By pushing impact considerations into the supply chain, the demand for impact-businesses will increase. Moreover, the need for climate resilient supply chains creates a straightforward way to link impact and financial performance.

- Impact Frontiers, Mr. Mike McCreless
  - The system of measuring and managing impact is still in its infancy, which organizations such as Impact Frontiers and GSG are leading the way in the public exchange of ideas, gathering feedback through public consultation. Japanese investors and companies are encouraged to actively participate in these global exchanges of opinions.
  - It took more than 100 years to establish financial accounting, and it will take time to

build similar system for impact. Joining the discussion now can help shape the future system of impact accounting and measurement that will be relied upon for years to come.

- Better Society Capital, Mr. Douglas Sloan
  - Organizations, such as the GIIN, Impact Frontiers, and Impact VCs, have produced insightful activities and tools for organizations in the impact investing space. Investors and organizations in Japan can gain valuable insights by participating in these communities, through working groups and connecting with other stakeholders. While lessons learned don't always perfectly align with local contexts, there's a lot of value in hearing diverse perspectives and experiences.

- GIIN, Mr. Sean Gilbert
  - It's important to have a cross-cultural team. Overseas Japanese investors can also play an important role in connecting to the global community, but also supporting Japanese investors to be involved in impact investing overseas, not just Japan.
  - In the 1990s, Japan conducted a lot of pioneering work in life cycle assessments and the creation of robust databases for sustainability. However, these were not well known outside of Japan, partially due to language barriers. For Japan to share its own insights and achievements internationally, it is important for Japanese stakeholders to engage actively in and with the international community.

4. Closing

(1) Closing Remarks (Mr. Akitaka Fujii, Co-Chairs, Global Advisory Panel Planning Committee)

- While it is very valuable to learn information from outside Japan, it is also important to disseminate Japan's insights and achievements to the outside world. Together, we want impact investing to be a force that will shape the next generation of the economy.