Family Office Insights
Impact Investing for Family Offices

Introduction

Since our previous piece discussing what at the time appeared to us to be an emerging investment theme for family offices, we have seen widespread evidence of increasing interest and awareness levels around impact investing in numerous sectors, both amongst our clients or contacts and more generally.

Whilst it is difficult to track the extent to which proclaimed interest is being converted into executed investments, and it is likely that the volumes of capital remain relatively insignificant, the appetite amongst investors for stakes in impactful businesses looks to be fairly well established and on an upwards trajectory.

We thought, therefore, that a fresh look at what might be driving this from the perspective of the family office was merited and why this may be an increasing area of focus.

Why Might This Be Happening?

Many wealthy families have of course long been associated with philanthropy, often seeking a social impact via purpose-specific donations or endowments. Under a traditional model, these philanthropic endeavours may be undertaken entirely independently of the family's commercial and investment activities. Successful execution of the latter generates the funds required to engage in the former, but there might otherwise be very little overlap or connection between the two concerns.

What appears to be happening more frequently, however, is that family office investors are targeting assets through which they can simultaneously make a positive social impact and achieve market rates of return. In the family office space, one of the most oft-cited explanations for this shift is that we are going through an era of significant wealth transfer and, as a consequence, the next generation of younger family members, who may be more socially conscious than their predecessors, are taking up decision-making positions and demanding that their family's wealth be deployed in a way that benefits a broader group of stakeholders.

Another factor to consider is that there are undoubtedly more and more for-profit businesses that are developing innovative ways to tackle specific social and environmental problems (think of renewable energy, healthcare and financial services and the technological developments in those sectors). In some jurisdictions, we are also seeing innovative legal structures encouraging this approach, including the development and growth of the "benefit corporation", or "B Corp", in the US and elsewhere, which seek to enable directors to move away from a "shareholders first" fiduciary model. These developments are influenced by more than just a strengthening of social conscience, with advances in technology or perceived failings by the non-profit or public sector also catalysts, but no matter the cause, the result is that it seems increasingly the case that for-profit enterprises are finding market-oriented solutions to issues that historically may have been the preserve of governments and non-profit organisations.

These sorts of businesses are, therefore, presenting investors with opportunities to invest capital for growth and profit, as well as social impact. Supporting such businesses so they can continue to grow and innovate may also be better for the overall ecosystem as, whilst some will undoubtedly succumb to market pressures and fail, the wider effect should be the promotion of self-sustaining, scalable enterprises with greater potential to make lasting social impact.

Family Offices Are Well Positioned…but There Remain Challenges

Given its innate flexibility, family capital seems very well placed for allocation to impact investments, especially those early-stage, higher-risk undertakings that might not otherwise be in a position to take investment from more mainstream investors. Un-restricted by investment mandates, return targets and fund life spans, wealthy families generally have the freedom to determine their own requirements as far as the ROI is concerned, both economic and social.

On the other hand, family offices will not always have the resources or expertise to identify, monitor and support these businesses in perhaps the same way that more sophisticated or institutional investors would. Whilst there may be approaches to mitigate this, by co-investing, for example, this may preclude some family offices from investing in higher risk enterprises. Complexity relating to structuring and/or challenges relating to certain geographic locations can also present significant obstacles, making investments prohibitively inefficient in terms of the execution time/cost required.

An impact investor will, of course, also need to find a way to measure and assess the impact and value the business has for society or the environment. This may not be straightforward, as in many instances, the impact may be intangible and difficult to quantify so investors will need to put considerable thought into what the most appropriate methodology or units of measurement are and how accurate data can be obtained and then purposefully interpreted.

Being able to assess and monitor impact in a meaningful way will also be important for governance and accountability purposes, both for investors and investees, whilst effective monitoring will help the investor with managing reputational risk/benefit. Having the data to demonstrate clear and positive outcomes may also facilitate public reporting, which in turn has the potential to improve the overall environment for and narrative around impact investing, setting off the virtuous circle.

Looking Forward

Greater transparency from investors about their impact investments, raising awareness about impact investing and the emergence of common standards and analytical tools may assist with some of these difficulties, though assessing impact is likely to remain quite a subjective and imprecise exercise. However, with regulatory mandated reporting in some jurisdictions, classification systems such as the UN's Sustainable Development Goals and the rise of "benefit corporation" or "B Corps" systems, there has been significant progress in these areas and as a result of legislative changes and work by various organisations, frameworks of standardised metrics that can be used to assess social and environmental impact are becoming more widely adopted and understood.

Notwithstanding the difficulties around defining and measuring the concept of impact, given the recent progress and the wider social forces at play, it seems likely that we are going to hear much more from the businesses and investors involved in this space and can expect to see family offices playing a part in this story.

Contact

Robert J. Shakespeare
Of Counsel, Singapore
T +65 6922 8674
E robert.shakespeare@squirepb.com