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Is India Impact Investment Ready? Drivers and Constraints

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ABSTRACT

India being one of the most promising emerging economies has to rethink the way businesses contribute to the nation. Impact Investment provides a wonderful way to reconfigure the business to enhance their impact. Impact Investment has become a slow and steady movement which is touching millions of life in its wake. India also has started benefitting from social and environmental improvements these investments are providing. Much of these investments though making a dent in the huge background of societal issues ailing our nation, are slow in coming and insufficient. The purpose of the paper is to examine the extent of the drivers and constraints and consider some of the most important elements of an effective Impact Investment strategy at the Country level. Some recommendations have been suggested to achieve long term success in an overcoming these problems.

Keywords: *Impact investment, Drivers, Constraints, India, Emerging Economies, Social*

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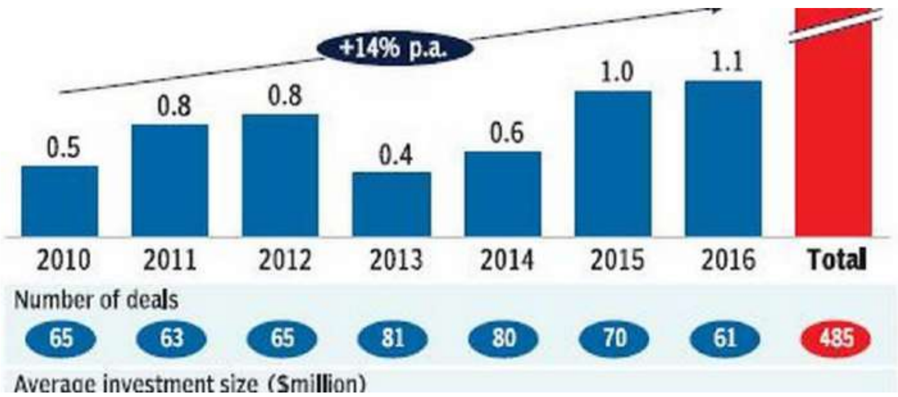
INTRODUCTION

Impact Investment, the term which has been around for a long time now, has gained more popularity in this decade. The OECD (Organisation for Economic Co-operation and Development) defines Impact Investment as 'the provision of finance to organisations addressing social needs with the explicit expectation of a measurable social, as well as financial return'.[1]Michael Drexler and Abigail Noble of the World Economic Forum have defined it as "an investment approach intentionally seeking to create both financial return and positive social impact that is actively measured."[2] Impact investment is soon turning out to be a solution for many issues plaguing the underdeveloped countries. It has the potential to initiate growth spiral at the very grass root level. This movement is touching millions of lives region, state and country level. It has created long-term employment, solved social issues like poverty and hunger and giving dignity of life on its way.The Global Social Impact Investment Steering Group, a taskforce set up by the G8 in 2015, predicts that the 20th-century approach to investing, based on risk and return, will be replaced by a new model built on risk, return, and impact.[3]

In India, Impact Investment has come a long way. Moving away from the charity and philonthropical way of fulfilling their Corporate Social Responsibilities, the businesses are looking ways to bring social and ecological change with financial returns. Impact investment provides them their answer. This way of Socially Responsible Business is changing the very way in which we look at CSR.

'Impact investing can be a vehicle to fund, catalyse, and scale approaches that improve millions of lives. India is an opportunity-rich environment and is emerging as one of the most attractive markets for impact investing worldwide. High demand for investments is likely to continue as a result of a growing population, underlying economic growth, stable financial markets with a strong rule of law, combined with large unmet social needs. Cumulative investment in impact investments in India since 2010 has been US $5.2 billion. In many ways, 2015 was a turning point, as investments crossed US $1 billion (Exhibit 1). Much of the growth has come from a doubling or more of average deal size, which rose to US $17.6 million in 2016, from US $7.6 million in 2010. The volume of deals has remained stable at about 60 to 80 a year, demonstrating the emphasis on scaling new models of impact.'[4]



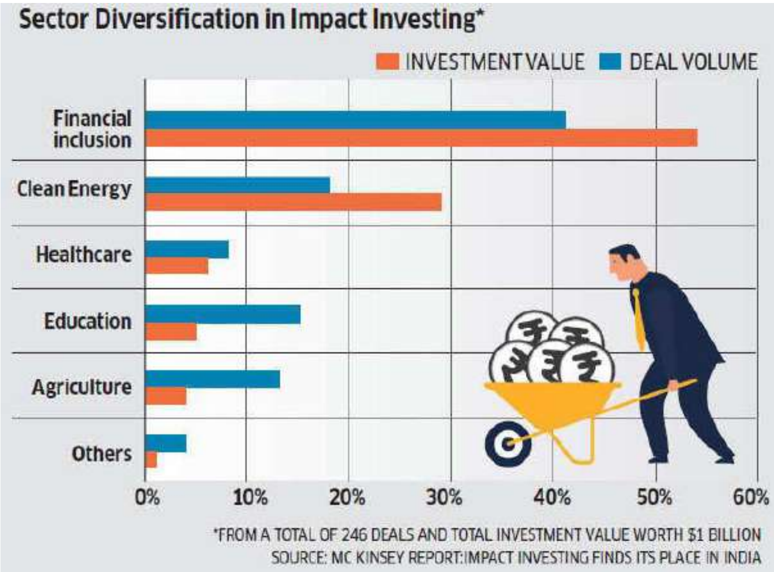
SOURCE: IIC members' survey; VCC Edge; McKinsey analysis

According to the report, impact investments – that meet the needs of the base of the pyramid population in a range of sectors such as healthcare, education, financial inclusion, agriculture and clean energy – cumulatively totalled $5.2 billion since 2010, with 2015 being the turning point, when that year alone the investments touched the $1-billion-mark. In 2016, the investments totalled $1.1 billion in India; the value of annual global impact investments topped $22 billion that year.[5]

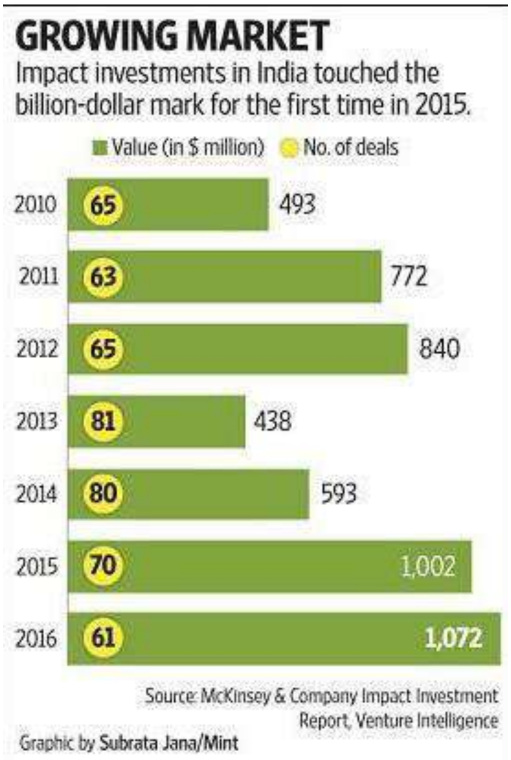
Most of the investments are coming from financial sector followed by Energy i.e. clean energy initiative and Healthcare. India being a developing economy is in dire need of such initiatives which can help solve the myriad social issues ailing the country.

Social Diversification: New forms of Investment in different sector

The key findings from the report suggest that Impact investing in India is estimated at a US$4.1bn market in terms of cumulative investments from 2010 to 2015. The sector is growing at about 15% annually. Current beneficiaries include at least 60 million Indians each year who are seeing advances in clean technology, financial inclusion, agriculture, healthcare and education.



Impact investments in India are focused on: clean-tech, financial inclusion, agriculture, healthcare and education. Conventional private equity and venture capitalists have contributed over 44% of the impact investment capital in India, while the rest comes from specialized impact investors. Impact investors have played a vital role in seeding.



LITERATURE REVIEW

There have been multiple attempts at providing a clear definition of Impact Investment. Impact investing at country level is a process of capacity building for the creation, managing and scaling-up of successful inclusive businesses (Koh et al., 2012) Inclusive businesses are facing lots of constraints in this very process. (Koh et al., 2012).The academic research on the subject is very limited.

This being a nascent issue, most of the research is focused on providing a clear definition of the subject. Impact Investment has become a wonderful tool of societal upliftment. This societal upliftment can take many forms depending on the requirements of the developing countries. It can be either ecological, financial or social changes which solve basic issues crippling these economies. (Dalberg, 2011; 2012; Koh et al., 2012; 2014; Brest and Born, 2013).

It is attracting high levels of interest in financial circles and it is claimed that it could become a new asset class worth more than USD 1 trillion globally by 2020 (Martin, 2013; 2013a)There has been lots of work done by independent agencies which provide consultancy and measure profitability of Impact Investment. Financial Institutions are partnering with mainstream private investors (e.g. asset owners and asset managers) to create impact funds aimed at solving the most pressing social problems through funding and technical assistance to improve society at Bottom of Pyramid (GIIN, 2011; WEC, 2013).

Most of the research in this field deals with Socially Responsible Investment strategy. A SRI strategy on impact investing refers to an 'explicit aspiration to generate exceptional social impact and a financial return by investing in enterprises that benefit the poor' and focuses on measurement metrics and assessment of Impact. (McCreless and Trelstad, 2012: 21). Impact investment companies differ on the basis of sizes of investment flows (e.g. Dalberg, 2011), motive and justification of investment strategies and sourcing behaviour (e.g. Banerjee and Duflo, 2011; Myers and Majluf, 1984.GIIN, 2011; Dalberg, 2011have created a data base of country and motive wise Impact investment which is very useful for further research in the field.

These research are also focussed on impact created and measurability of the social and ecological impact (Dalberg, 2011, 2012).Academic research, however is more interested in comparison of socially responsible investment with traditional tools of investment. Apart from quantitative side there is a need to understand the motivations and hurdles for the same.

SCOPE OF THE STUDY:

This study explores the field of Impact Investment. Most of the research in this field has been focused on innovation, definition and motive of Impact Investment. This paper attempts to identify the drivers and constraints which the Impact Investors in India face. This paper proposes the ways in which Indian Government could primarily support social impact investing by creating an enabling environment for private sector-led social impact investing and by funding (or co-funding with State Governments) investments. The field of Impact Investments has many attractive motives or drivers, which can bring the private capital, which so far has been underutilized in our country. The path to Impact Investment led social transformation path is also filled with hurdles. This paper attempts to identify and understand the same to come up with suggestions.

RESEARCH METHODOLOGY:

The aim of the paper is to examine how the impact investment are connected in Indian market. The objective of research was twofold. First it sought to understand the impact investment. Second, it derived and document the forces behind impact investment from varying referred sources. The objectives are framed on the basis of mentioned aims.

1. To understand the concept of Impact Investment
2. To analyze the drivers behind Impact Investment in India
3. To identify the constraints these investment are facing in Indian market
4. To provide some suggestions for boosting Impact Investment in India

Keeping in view of the set objectives, this research design was adopted to have greater accuracy and in depth analysis of the research study. Looking into requirements of the objectives of the study the research design employed for the study is of descriptive type.

SOURCES OF DATA:

The sources of data utilized in this research are multiple journalistic articles about impact investment and the private sector, and articles from academic journals that discusses the concept in perspective to globalization, development and public/private sector. These sources are secondary data, which the researchers have used to gather an overall understanding and knowledge about the concepts and tendencies in question.

LIMITATIONS

The research have few limitations as:

- One basic limitation of the researchers plan to remove in the future is lack of primary Data. Lack of time and resources have created this limitation.
- The other limitation arise from not being able to assess more aspects of Impact investment.

DATA ANALYSIS:

In a world where government resources and charitable donations are insufficient to address the world's social problems, impact investing offers a new alternative for channelling large-scale private capital for social benefit. [6] Businesses are looking for Impact investment as an opportunity to effectively contribute to approach key social challenges through leveraging their domains of expertise, resources, and people; and create solutions for long-lasting impact on the three pillars namely People, Planet and Profit.The research identified drivers and constraints in sustaining impact investment. The impact investment scenario, seen from the traditional viewpoint, presents a dismal picture. Research derive major drivers and constraints which are as follows:

DRIVERS

The main drivers which come in front after the analysis are:

- **Increase in Capital movement towards Underdeveloped Economies**: Impact Investment has the pull to bring additional much-needed money to these countries. This is definitely a great opportunity for investors who are looking forward to added social returns along with the financial ones. The add-on benefit of ecological and societal benefits. Impact Investment has the potential to harness the under-utilized capital in the developed countries and shift the flow to these developing economies. The myth of Impact investment avenues being less profitable is now swiftly being shattered by the gains earned by such investments.
- **Scalability of Impact Investment**: One more misconception which is very common is the dearth of measurement tools for such investments. The major driver which is steering the plethora of Impact Investment across the globe is the multiple tools which number of companies have come up with. There are lots of tools available online for self-assessment like GIRI, Inclusive Business Challenge, Social E-Valuator, Social Business Scorecard (SBS) etc. There are also lots of consultant companies and NGOs involved with impact assessment work.
- **Boost to Social and Ecological Innovations**: Impact investment has become the harbinger of innovations across products, services and processes for corporates across the world. There are multiple examples strewn across the industries where the motive of doing good has driven the companies and entrepreneurs to be creative with the way they do things. Embracing social impact with financial sustainability helps the prospects of bringing products and services which are welcome and easily acceptable by the society.
- **A helping hand to Governments**: The Private sector is joining hands with the Local, State and Central governments to solve the maladies faced by the society. This brings the added financial and human resources to the Governments much-needed aid. The Governments of

developing countries are struggling to solve the myriad issues faced by these societies. The main drivers of Impact investment is the much required collaboration between Government and the private investors. The Government funds usually fall short for tackling ecological and societal issues. The inclusion of private investment with a promise of returns enhances the viability and sustainability of such ventures.

- **A step-up from Traditional Investment Avenues:** This platform is turning out to be more profitable and sustainable in the long-term. Most of the start-ups are finding it easier to enter and sustain in the market with such investments. The customers and other stakeholders are supporting the ventures which have social responsibility entwined with the financial returns. These avenues are now preferred over traditional asset class.
- **Enhanced Human Resource Sourcing:** The promise of societal change through is very lucrative for the talent pool.The younger generation is now-a-days more interested in combining their passion of social cause and environmental issues with their job. It is easier to attract loyal, talented employees by associating work with a social or environmental issue.
- **Stronger Supply Chains:** Aligning environmental concerns with their business values helps in developing stronger and sustainable supply chains. The inclusion of eco-friendly inputs and search for suitable supplier many a times improves the value chains of suppliers for these investments.
- **Increased Visibility-** Integrating social impacts from day one and interweaving social value into their products can help these ventures to achieve increased visibility amongst competitors. Adoption of societal and ecological targets can provide a USP (Unique Selling Proposal) in face of tough competition prevailing in the industry**.**
- **Other Benefits:** The otherbenefits which accrue to the economy areIncreased transparency, accountability and performance, possibility of collaborations and building stronger partnerships with service providers, investors and State and National Governments

Constraints

The constraints which are faced by these Impact Investments in India are:

- **Gaps between target and achieved Impact:** The major constraint which is faced by Impact Investment in India is enhanced expectations of social changes. Any social or ecological impact is slow and time-taking. Heightened expectations might result in disappointments or demotivation of people involved. Investors face challenges in fulfilling social and personal ambitions in the short-term.
- **Confusion with Charity and CSR**: Impact investment which have the onus of delicately balancing financial returns with societal gains are not to be confused with Charity/philanthropy and Corporate Social Responsibilities. These investments though having one of the objective of environmental and social value creation have their eye focussed on profitability and sustainability in the market. There is still lot of confusion in the market with their primary objective and also with the very definition of Impact investment.

- **Dearth of commonly acceptable social metrics**: One major constraints faced by these investors is measurements tools which are acceptable everywhere and are standardized.
- **Cultural Barriers**: Some of the constraints and challenges of any social project accrue to these investments too. Crossing the hurdle of cultural and social barrier is usually having a dampening impact on the results.
- **High Costs**: Like all social ventures a vast majority of these investments face the high transactional costs which result in added risk to the project. Addressing complex societal challenges brings with it many additional costs.
- **Less Credibility**: Lack of good risk evaluation parameters and measurement tools, especially in India brings loss of credibility to such projects. This results in such ventures losing their appeal to the stakeholders.
- **Infrastructure Bottlenecks**: Shortage of infrastructure physical as well as financial create a huge constraint for any Investors. India as an emerging economy presents wonderful opportunity for such investments. An underdeveloped physical and financial infrastructure brings down the impact created by such investments.
- **Lack of dependable Data**: A lack of Dependable and accessible data to measure outcomes to determine the impact of such investment projects creates one more constraint
- **Narrow Application fields**: One more basic limitation of the field of Impact Investment in India is that not all social problems could or should be targeted through social impact investment and it takes time to identify opportunities for social impact investing.

SUGGESTIONS and RECOMMENDATIONS

The suggestions to the policy makers/ Government are as follows:

- **Access to reliable Data**: Most of the capital flows from developed countries are deflected towards other developing economies which have more accurate and reliable data. The Government should ensure access to data related to ecological and social parameters.
- **Robust and Transparent Measurement Metrics**: One more hurdle which can be mitigated in this field is lack of easily applicable evaluation metrics and methods.
- **Progress Measurement**: One more initiative can be to provide help or government intervention in measuring progress of these investments by creation of milestones.
- **Reduction of Transactional Costs**: One major Government intervention can be with reduction of transaction costs which usually are a deterrent to such investments.
- **Removal of Infrastructural Barriers**: The major role of Indian Government in attracting Impact Investment can be through provision of strong and stable financial and physical infrastructure to the investors.
- **Provision of Consultancy**: There are lots of constraints which limit the amount of capital flow to Impact Investment field. The Government should provide Technical and financial consultancy to reduce the impact of difference in regulatory, legal and cultural sectors.

CONCLUSION

Addressing successful Impact Investment in India requires a comprehensive and multifaceted strategy, which includes effort aimed at the different reintegration of several sectors. Otherwise, the strategy forces will not be successful in the long run. In essence, India being an emerging economy, has a lot to offer to the world. The investors across the globe are looking for the opportunities to deliver some social good with the money inputs they are making in these economies. It is the right time to harness such potential. The government should refabricate and reinforce its strategic intent on this subject. There is an urgent need to bring this huge untapped capital resource to India. Benefits of this definitely outweigh the challenges.Without any commitment of developing the financial infrastructure to the lowest part of the pyramid would not strengthened to deliver the fruitful results. India has to be Impact Investment ready in all perspectives.

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