08

Maximum impact

10 TRENDS FOR 2023

In the aftermath of the Covid-19 pandemic, many of our towns and cities face an unprecedented crisis. Cities have found themselves in the front line, as policymakers and businesses face up to the multiple challenges of climate change, energy costs, inflationary pressures and a slowing global economy. The good news is that we are also seeing a sea-change in the attitude of the private sector in helping to tackle this urban crisis, embracing the role that it can play in driving transformational urban regeneration. The focus on what makes a successful place is growing as the public and private sectors partner to drive local growth.

The pandemic has accentuated the difficulties faced by many urban neighborhoods. Retail activity has declined in the face of a rise in online shopping. Employees have been slow to return to the office, particularly in areas that lack the vitality and amenities that cater to the social element of going to work. A lack of affordable housing makes it hard for key workers to find decent quality accommodation within an acceptable commuting distance. Crime levels have risen, even in some of our largest and most prosperous inner cities. Inequality has increased, as many segments of society hardest hit by Covid-19 restrictions are those most affected by rising inflation and a weakening economy. For communities that were struggling before, the challenges have become greater.

While city governments have long been at the forefront of tackling these problems, the private sector is increasingly deploying its skills and capital to help. The real estate community is typically quick to respond to redevelopment opportunities where the commercial and financial case for investment is straightforward; there are now signs of increased private engagement where problems are more entrenched and projects are more complex.

The private sector is increasingly deploying its skills and capital to help tackle local problems.

There is increasing interest in public-private partnerships (PPP) which unlock access to large-scale development and investment projects that are simply not possible without public authority involvement. The perception can sometimes be that such partnerships are simply about persuading the private sector to pay for public works, but this overlooks what government involvement brings to the table. The public sector often contributes land or other assets to the partnership and can sometimes borrow at advantageous rates to increase the funding available. As well as often contributing equally to the financing of projects, public involvement helps de-risk projects and can stimulate additional private sector investment from sources beyond the principal development partner. It is the combination of public and private sector expertise that is particularly powerful.

Public-private partnerships can unlock access to large-scale development.

The growing focus on place and social value

The private sector is now meaningfully embracing the wider ESG – environmental, social and governance – agenda. Decarbonization and strategies for addressing the “E” may be attracting most of the headlines, but the “S” – Social Value – is rapidly coming to the fore. The increasing prominence of social value considerations in corporate thinking is changing the way that institutional investors approach real estate investing. There is a focus on developing a sense of place and interest in harnessing relationships with people to produce long-term, real impact on people and communities. Successful place-based impact investing (PBII) addresses local problems and involves the community in determining the definition of success[1], altering the viability equation for capital investments and introducing new considerations into discussions around “return on investment” (ROI).

The private sector is now explicitly targeting opportunities for impact investing. The Global Impact Investing Network (GIIN) sized the market at $1.164 trillion in 2022, up from their $502 billion market estimate in 2019.[2] Nuveen Real Estate recently announced the establishment of a global impact investing program that will aim to see $15 billion in real estate AUM across the U.S., Europe and Asia Pacific by 2026.

In the U.K., Schroders Capital recently launched a place-based impact investment strategy with the specific objective of addressing social deprivation and inequality as well as delivering a financial return, with investments targeted at affordable homes, workplaces and mixed-use town center re-purposing projects. Similarly, financial services group Legal & General will invest £4 billion into urban regeneration and housing development in the U.K.’s West Midlands region by 2031.

Government actions and regulations will also drive the expansion of the impact investing market. In 2022, the U.K. government’s Levelling Up white paper announced that all local government pension funds would target 5% of investment of assets into projects that support local areas.[3] This policy could increase the U.K. impact investing market by £16 billion. The Canadian Social Finance Fund will inject the market with $755 million in funding towards social initiatives.[4] In the U.S., the introduction of the Social Innovation Fund has increased investment into the social market and helped to develop structures for later impact investing.[5]

There is a focus on developing a sense of place.

Mobilising capital investment to do good

Private sector interest in place-based impact investing will be driven by the desire to leverage capital for the direct benefit of people and place. Companies can also demonstrate community involvement in projects and help build relationships with local groups, boosting the chances of commercial success as well as enhancing the reputation of the investor. At a time when ESG performance is seeing increasing focus from multiple stakeholders, place-based impact investing is set to become increasingly prominent.

A broader array of tools is becoming available to help finance these new initiatives, illustrated by the proliferation of Social Impact Bonds and Green Bonds. The GIIN reported that the issuance of green bonds grew at an annual rate of 43% since their inception in 2008, reaching $578 billion in 2021.[6] They are used to support projects that mitigate climate change and provide environmental improvements. While they address the "E" in ESG, not every green bond-financed project contributes to social value outcomes. Social impact bonds use the same tools to pool capital from various investors to fund efforts towards social value outcomes.

These investments are then repaid by the government if the social outcomes are achieved. As of 2020, over 190 impact bonds had been contracted in 33 countries across the globe.[7] The growth of social impact bonds – or social outcome contracts – in the U.K. began in 2010 following the introduction of the world's first social impact bond in Peterborough.[8] In the subsequent decade, they have been utilized in place-based solutions such as the Life Chances Fund, which uses them to provide funding for locally driven projects targeted at social outcomes.[9] Most importantly – these funding mechanisms allow public and private capital to be harnessed together for social value development.

Accounting for the social as well as the financial benefits of a project can further help bridge the divide between public and private sectors and can go some way to enhancing the viability of a project. But even with increased willingness to collaborate on both sides, three key challenges remain.

Place-based impact investing is set to become increasingly prominent.

Several challenges remain

The first is that transformational place-based impact investment takes time.[10] Unlike the sometimes-instant results generated from environmental impact, changes and improvements in social value will strengthen over the long-term. Social value is generated through collaborating with communities – places and people – throughout the length of a project. In our experience, successful impact comes from early engagement to understand the community coupled with ongoing communication to check, challenge and discuss investment outcomes. However, maintaining consistent engagement with local interests can prove difficult for the private sector, as an ever-changing political landscape and periodic elections for local leadership could hinder long-lasting relationships. Place-based impact investments will maintain that commitment to a community, even as their needs and interests develop.

The second challenge in impact investing lies in the decision to act early and take on risk. In 2021, the Federal Reserve by of New York commissioned a report from the U.S. Impact Investing Alliance which concluded that financial risk is the key factor preventing companies from acting earlier and more decisively. Even if wider social benefits are part of the overall “accounting” of the project, private companies still need a commercial return for the partnership to be viable from their perspective. Unlike governments, they exist to take risk – but they need to be rewarded for doing so. Identifying and documenting the respective risks and returns to be borne, including what happens if the results are not what’s expected and how disputes will be resolved, are often major sticking points. Luckily these risks can be approached by linking impact investing to market returns. Schroder’s cites the improved prime office capital values in the King’s Cross area of London as a concrete example of the connection between social value and market returns.[11] The investors who committed to this project early – and championed social value creation – reaped the most benefit from these returns.

The third issue is adequately identifying and capturing the non-financial (and often difficult to quantify) social value benefits from place-based impact investment. In a typical investment, potential ROI and risk-adjustments are used to determine the viability of a project, however, this is much harder to achieve in the case of a longer-term project where the ultimate aim is to improve health and living standards, employment opportunities and social integration within the wider community. Developing ways to effectively monitor and reward these fundamental objectives of urban transformation projects – and incorporating these metrics into partnership agreements - is key to unlocking the potential for wider private investment in such projects. The development of non-financial return metrics such as the social return on investment (SROI) and impact multiple of money (IMM) is providing methods to compare impact investing outcomes to similar traditional investments. However, these metrics needs to be adjusted based on the desired outcomes for each project to reflect bespoke, place-based outcomes.

The road ahead

The impact investing market is growing, and companies will look to tie these investments to the places and people that relate to the interests of their client and corporate missions. Partnerships between the public and private sectors will increasingly be used to deliver the social value outcomes that are key to tackling the challenges faced by our towns, cities and communities.

Would you like to discuss this trend?

Get in touch

Don’t miss our webinar with Nick Axford

Subscribe

AVISON YOUNG

[1] PBII Quarterly
[2] The Global Impact Investing Network - https://thegiin.org/research/publication/impact-investing-market-size-2022/
[3] https://forecast.citywire.com/articles/the-new-kid-on-the-block-place-based-impact-investing
[4] https://www.canada.ca/en/employment-social-development/programs/social-innovation-social-finance/social-finance-fund.html
[5] The Brookings Institute - https://www.brookings.edu/wp-content/uploads/2020/09/Impact_Bonds-Brief_1-FINAL-1.pdf
[6] The Global Impact Investing Network - https://thegiin.org/research/publication/impact-investing-market-size-2022/
[7] https://www.brookings.edu/wp-content/uploads/2020/09/Impact_Bonds-Brief_1-FINAL-1.pdf
[8] https://www.rand.org/randeurope/research/projects/social-impact-bonds.html
[9] https://www.gov.uk/guidance/social-impact-bonds
[10] https://www.newyorkfed.org/medialibrary/media/outreach-and-education/community-development/emerging-sources-of-community-investment/community-investing-bank-report-final-20210518
[11] https://www.schroders.com/en/uk/tp/markets2/markets/can-social-impact-investing-actually-increase-real-estate-returns