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''Strategy Paper for Impact Driven Investments and Business Models

Abstract: The first part of this paper investigates the relation between business model innovation and current approaches with sustainability. The second part focuses more on the new impact valuation models as well as impact investment space with its newly emerging concepts and players.

THE CHALLENGE

There is growing interest and debate on how to DEFINE value, in our future economic realities. Forward looking companies started to work on their authentic impact models, defining their unique KPİ's based on their strategy in order to integrate sustainability into their core business.

The BİG question private sector is asking and trying to answer is

How to ensure growth or optimise growth and at the same time balance profit and purpose ?

THE CONTEXT

Recent research and practice have shown that business model innovation can be one way to create and capture **new value** and drive production and consumption toward sustainability. **However**, business model tools typically do not create a space to consider **how sustainability concerns may be integrated into the innovation process.**

In addition to that, a typical approach of a company/organisation to sustainability is to follow he ESG space to adress issues and overcome mismanagement and risk related challenges. This might have been enough until the beginning of 21th century.

Today, - we need to find or create new ways to close the gaps in value creation and distribution

The real opportunity lies in leapfrogging into a technology-driven approach to sustainability. This will help make faster progress. For that companies will need to find a way to measure their maturity levels not only in term of carbon emissions but also about their capacity to leverage technology for that transformation. Once we accept sustainability as a competitive advantage we realise its strategy should be designed by taking into consideration all strategic functions of an organisation.

The reason why many organisations are reluctant to to change their business models or shift to better greener or more inclusive ones is basicly because they don't know how to use sustainability as a strong stimulating factor for their business. **Sustainability should be aligned with your corporate business strategy. The key to that is creating your own authentic impact models.**

We all know that, a good corporate business strategy involves factors or insights that will differentiate the company's value proposition and so it is about what you do different than your competitiors – **its about your competitive advantage**. Today, smart organisations are the ones who are playing a different kind of game. Some are using technology to solve enviromental and social problems; I call it the ''Gap Business ''

And some are thinking hard to design new products and services for the BOP- which is called ''Inclusive Business''.

And both attempts are very much linked to the capacity of an organisation to innovate its business model. So, the real challenge of the business world is to integrate sustainability in all functions of its organisation and if possible with an appropriate culture to imprint the impact to its DNA.

PART I

While business model innovation has been the subject of much discussion and research, very few tools have been developed to help companies integrate sustainability into the business model innovation process.

Existing tools for business model innovation either do not consider sustainability (Business Model Canvas) or do not address all of the elements of the business model (for example, lifecycle assessment tools). Thus, sustainability considerations and business model innovation are often not well integrated, with sustainability being treated as an add-on rather than as a core source of value.

Considering sustainability in the process of business model innovation can provide entirely new ways to create and capture value, beyond those offered by merely developing greener technology or cleaner production systems, by making sustainability a central element not only of the product but of the business itself.

New tools that help companies integrate sustainability concerns and opportunities into the design of new business models can uncover new approaches that yield new sources of value, making sustainability an opportunity for growth rather than a challenge to be overcome.

IT IS IMPORTANT TO DISCOVER THOSE NEW TOOLS OR CREATE AND DESIGN UNIQUE IMPACT MODELS

In the literature, the concept of the business model is closely linked to the concept of value; the business model explains how a company creates, delivers, and captures value . Thus, business model innovation is the process of identifying new ways to create, deliver, and capture value. Several tools have been developed to help companies improve value creation.

Value Network Analysis maps the tangible and intangible value exchanges within internal networks (between individuals and groups within a firm) and external networks (between organizations); the method has achieved practical results (Allee 2011).

Osterwalder and Pigneur's (2010) **Business Model Canvas**, specifically intended to help companies design business models, has become the dominant tool in industry. This tool breaks the business model down into nine elements—value proposition, customer segments, channels, customer relationships, revenue streams, key resources, activities, partnerships, and cost structure—and provides a framework for understanding the relationships among these elements.

A more recent entrant, **the Value Mapping Tool** (Bocken et al. 2013; Evans, Rana, and Short 2014), also focuses on relationships, analyzing value exchanges from the perspective of multiple stakeholders to identify value creation opportunities.

Den Ouden's (2012) **Value Framework**, which approaches business model design by developing value propositions for all stakeholders, is alone among the major tools in explicitly considering larger impacts; the framework aims to create shared value concepts for four levels of value—**user, organization, ecosystem, and society**—and considers value from four perspectives: the economy, psychology, sociology, and ecology.

However, the framework remains largely conceptual and is difficult to apply in industry.

None of the other major tools specifically includes sustainability considerations in the construction of the business model or the mapping of value relationships.

The Business Model Canvas, for example, focuses on economic value, and the Value Network Analysis, while it may include larger networks beyond the organization, is not specifically intended to be used in the context of sustainability. The Value Mapping Tool includes sustainability issues by considering the environment and society as key stakeholders, but it still does not offer an adequate approach to address the concept of value related to sustainability.

Focusing business model innovation on sustainability requires a framework for understanding how sustainability may generate opportunities for value creation.

It requires **innovation not only on technologies, but across the entire system, including design, processes, and operating procedures. This holistic systems view can be based on four key concepts.**

- Lifecycle thinking,
- Multiple stakeholders,
- Value uncaptured, and
- Economic, social, and environmental value.

Lifecycle thinking.

Lifecycle thinking is about considering the economic, environmental, and social impacts of a product across its entire life cycle—not just in manufacturing or disposal, but from materials sourcing through manufacturing and use to disposal or recycling. A product's life cycle begins when the product is designed and manufactured, extends through its life in use and to its recycling, reuse, remanufacture, and disposal (end of life).

Many manufacturers expend great energy creating value from sustainability in design and production, but miss opportunities to create and capture value while products are in use or even at the end of the life cycle, when they are recycled or discarded. Lifecycle thinking can help companies to discover sustainability-focused value opportunities across the entire product life cycle, and perhaps identify new ways to both maximize value and minimize environmental and social impacts.

Multiple stakeholders. The manufacture, marketing, and recycling of any product involves multiple stakeholders at various levels, from company shareholders to employees, customers, end users, and communities. Building business models focused on sustainability requires companies to link resources and outcomes across all of these multiple stakeholders as sustainability efforts must contribute to the creation of shareholder value at the same time as they satisfy customer needs and make positive contributions to the environment and society. Engaging with multiple stakeholders can help managers identify the key players at each stage of the product life cycle, understand the value exchanges between stakeholders, and keep all stakeholder interests aligned.

Value uncaptured. The concepts of value captured and value uncaptured offer a way to think about where and how value is captured in the business model and where additional value might be created and captured. Recognizing value captured and value uncaptured and identifying the opportunities represented by value uncaptured is an effective approach to sustainability-focused business model innovation. Value captured is the benefit delivered to the company and its stakeholders; it includes not only monetary value, but also the wider value provided to the environment and society. Improved energy efficiency, zero emissions, and clean production are all elements of value captured for the environment. Value uncaptured is potential value that is not captured in the current business model.

Some value uncaptured is visible, for example, in waste streams in production and in reusable components of broken products that are discarded. Some is invisible, for example, workforce overcapacity or underutilization of available expertise and knowledge.

Value uncaptured may come in any of four forms—value surplus, value absence, value missed, and value destroyed Value uncaptured has some similarity with the Lean concept of waste, for instance the seven wastes of lean production but value uncaptured is broader than Lean's wastes, both in the kinds of value it considers and in its coverage of the entire product life cycle, beyond production.

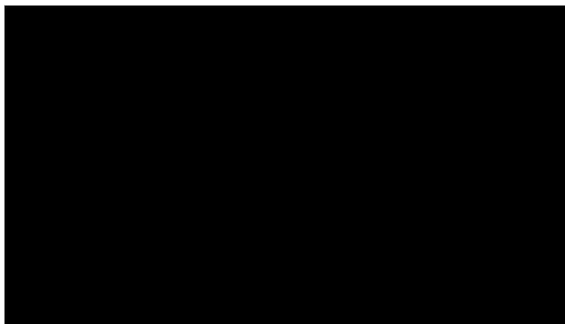
These four concepts—lifecycle thinking (where to look for value opportunities), multiple stakeholders (who to identify opportunities for), value uncaptured (how to identify value opportunities), and economic, social, and environmental value (what value consists of) can be synthesized to provide a conceptual framework for value analysis focused on sustainability. By analyzing value captured and value uncaptured for all stakeholders across the product life cycle, companies can identify opportunities to create sustainable value that yield economic benefit and contribute to the environment and society.

Economic, social, and environmental value.

Value is commonly understood as monetary value; however, sustainability requires a more comprehensive view of value that includes social and environmental benefits. This is what we mean by sustain- able value.

Sustainable value includes economic, social, and environmental value, and all of the considerations particular to each of those domains. To effectively integrate sustainability into their business models, companies must consider benefits to the environment and to society as valuable—that is, they must integrate sustain- able value into the other sources of value they consider.

PART II



What is Impact Investing ? (please double click on the black box to activate the video)

ESG investing is part of a group of approaches collectively referred to as **responsible investment.**

While ESG investing is concerned with how ESG issues can impact the long-term return of assets and securities, other responsible investment approaches can also take into account non-financial value creation and reflects stakeholder values in an investment strategy. While there is no standard set of criteria for identifying responsible investment, the main investment approaches are presented in this section to demonstrate the wide spectrum of different types of responsible investment. Responsible investment is an umbrella term for the various ways in which investors can consider ESG within security selection and portfolio construction. As such, it may combine financial with non-financial outcomes and complements traditional financial analysis and portfolio construction techniques.

RESPONSIBLE INVESTMENT TYPES

Figure 1.2 **A SPECTRUM OF CAPITAL**

	PHILANTHROPY		SOCIAL IMPACT INVESTING		SUSTAINABLE AND RESPONSIBLE INVESTING	CONVENTIONAL FINANCIAL INVESTING
	Traditional philanthropy	Venture philanthropy	Social investing	Impact investment	ESG investing	Fully commercial investment
Focus	Address societal challenges through the provision of grants	Address societal challenges with venture investment approaches	Investment with a focus on social and/or environmental outcome and some expected financial return	Investment with an intent to have a measurable environmental and/or social return	Enhance long-term value by using ESG factors to mitigate risks and identify growth opportunities	Limited or no regard for ESG practices
			Use of ESG metrics and methodologies			
Return expectation	Social return only	Social return focused	Social return and sub-market financial return	Social return and adequate financial market rate	Financial market return focused on long-term value	Financial market return only
	Social impact	⟵⟶	Social and financial		⟵⟶	Financial returns

Source: Stylised adaptation from Organisation for Economic Co-operation and Development (OECD),[6] based on earlier versions from various organisations. For illustrative purposes only.

Responsible investment

Responsible investment is a strategy and practice to incorporate ESG factors into investment decisions and active ownership.[2] It is sometimes used as an umbrella term for some (or all) of the investment approaches mentioned in the following sub-sections.

At a minimum, responsible investment consists of mitigating risky ESG practices in order to protect value. To this end, it considers both how ESG might influence the risk-adjusted return of an asset and the stability of an economy, as well as how investment in, and engagement with, assets and investees can impact society and the environment.

Socially responsible investment

(SRI) refers to approaches that apply social and environmental criteria in evaluating companies.

SRI ranking can be used in combination with best-in-class investment, thematic funds, high-conviction funds or quantitative investment strategies.

Best-in-class investment involves selecting only the companies that overcome a defined ranking hurdle, established using ESG criteria within each sector or industry.

Typically, companies are scored on a variety of factors that are weighted according to the sector. The portfolio is then assembled from the list of qualified companies.

Bear in mind, though, that not all best-in-class funds are considered to be 'responsible investments'.

Due to its all-sector approach, best-in-class investment is commonly used in investment strategies that try to maintain certain characteristics of an index. In these cases, security selection seeks to maintain regional and sectorial diversification along with a similar profile to the parent market cap index while targeting companies with higher ESG rating. The tracking error for **MSCI World SRI**, which is designed to represent the performance of companies with high ESG rating and employs a best-in-class selection approach to target the top 25% companies in each sector, is only 1.79%

Sustainable investment refers to the selection of assets that contribute in some way to a sustainable economy, i.e. an asset that minimises natural and social resource depletion.

It is a broad term, with a broad range of interpretations that may be used for the consideration of typical ESG issues. It is further used to describe companies with positive impact or companies that will benefit from sustainable macro-trends. The term 'sustainable investment' can also be employed to mean a strategy that screens out activities considered contrary to long-term environmental and social sustainability, such as coal mining or exploring for oil in the Arctic regions.

Thematic investment refers to selecting companies that fall under a sustainability-related theme, such as clean-tech, sustainable agriculture, healthcare or climate change mitigation. Thematic funds pick companies within various sectors that are relevant to the theme. A smart city fund, for example, might invest in companies offering activities or products related to electric vehicles, public transportation, smart grid technology, renewable energy and/or green buildings.

Bear in mind, though, that not all thematic funds are considered to be responsible investments or best-in-class. Becoming one not only depends on the theme of the fund, but also on the ESG characteristics of the investee companies.

Green investment refers to allocating capital to assets that mitigate:

- climate change;
- biodiversity loss;
- resource inefficiency; and
- other environmental challenges.

These can include:

- low-carbon power generation and vehicles;
- smart grids;
- energy effciency;
- pollution control;
- recycling;
- waste management and waste of energy; and

Green investment can thus be considered a broad sub-category of thematic investing and/or impact investing. Green bonds, a type of fixed-income instrument that is specifically earmarked to raise money for climate and environmental projects, are commonly used in green investing.

Social investment refers to allocating capital to assets that address social challenges. These can be products that address the **bottom of the pyramid (BOP)**.

BOP refers to the poorest two-thirds of the economic human pyramid, a group of more than four billion people living in poverty. More broadly, BOP refers to a market-based model of economic development that seeks to simultaneously alleviate poverty while providing growth and profits for businesses serving these communities. Examples include:

- micro-finance and micro-insurance;
- access to basic telecommunication;
- access to improved nutrition and healthcare; and
- access to (clean) energy.

Social investing can also include social impact bonds, which are a mechanism to contract with the public sector. This sector pays for better social outcomes in certain services and passes on part of the savings achieved to investors.

Impact investment refers to investments made with the specific intent of generating positive, measurable social and/or environmental impact alongside a financial return (which differentiates it from philanthropy). These are usually associated with direct investments, such as in private debt, private equity and real estate. However, in recent years, impact investing has increasingly mainstreamed into the public markets.

Impact investments can be made in both emerging and developed markets. They provide capital to address the world's most pressing challenges by investing in projects and companies that may, for example:

- offer access to basic services, including housing, healthcare and education;
- promote availability of low-carbon energy;
- support minority-owned businesses; and
- conserve natural resources.

Measurement and tracking of the agreed-upon impact generally lies at the heart of the investment proposition. Impact investors have diverse financial return expectations. Some intentionally invest for below-market-rate returns in line with their strategic objectives. Others pursue market-competitive and market-beating returns, sometimes required by fiduciary responsibility. The **Global Impact Investing Network (GIIN)** estimated the size of the global impact investing market to be US$502 billion (£361bn); its 2019 annual survey indicated that 66% of investors in impact investing pursue competitive, market-rate returns.[8]

The IMPACT UNIVERSE

The spectrum of capital

		THE IMPACT ECONOMY			
INVESTMENT APPROACH	TRADITIONAL	RESPONSIBLE	SUSTAINABLE	IMPACT DRIVEN →	
RISK RETURN PERSPECTIVES	Only financial returns	ESG risk management	ESG opportunities	Impact solutions	
	Seek financial returns regardless of ESG factors	Investments are screened out based on ESG risks	Sustainability factors and financial returns drive investment selection	Targeted themes and financial returns drive investment selection	Social and environmental considerations take precedence over financial returns
	Accept competitive risk-adjusted financial returns				Accept lower risk-adjusted returns
IMPACT GOALS		AVOID HARM AND MITIGATE ESG RISKS Mitigate or reduce negative outcomes for people and planet			
			BENEFIT STAKEHOLDERS Generate positive outcomes for people or the planet		
				CONTRIBUTE TO SOLUTIONS Generate real positive change for otherwise underserved people or the planet	
PERSONAL INTENTIONS	"I am aware of potential negative impact but do not try to mitigate it"	"I want to behave responsibly" "I have regulatory requirements to meet, e.g. cutting CO_2 emissions"	"I want to have positive effects on the world and help sustain long-term financial performance"	"I want to help tackle climate change" "I want to help tackle the education gap" "I want to support solutions at the core of the problems of our planet"	

There is a continuum of investment approaches ranging from traditional investment management to the integration of ESG factors to impact investing. While ESG investments primarily intend to minimize negative externalities and financial risks, impact investing rather focuses on investment opportunities which generate positive outcomes for underserved people and the planet and contribute to solve current global challenges.

Global Impact Investing Network (GIIN) focuses on reducing barriers to impact investment by building critical infrastructure and developing activities, education and research that help accelerate the development of a coherent impact investing industry. Of note are its databases IRIS+ (of metrics for measuring and managing impact) and ImpactBase (of impact investing funds).

CASE STUDY – BMW FOUNDATION FUND

BMW Foundation helped build consensus with the Impact Management Project (IMP) and many other initiatives. Impact measurement and management is all about making better decisions with the information we have regarding what people and the planet are experiencing. This isn't easy, and requires judgment. How do we compare x with y? What level of detail can or should I share? Luckily, the IMP helped us use a common language, with the five dimensions and the "ABC" impact classification, that allows us to be more transparent than ever. It's on us, as practitioners, to continue to push the boundary and make sure data is stakeholder- driven and decision-useful.

What are currently core challenges of impact measurement and management?
Comparability of impact, and a deeper understanding of the role of our investment structures, are our greatest challenge and opportunity. We are just scratching the surface here.

While there has been great progress on IMM in the last couple of years, driven by a range of organizations including the IMP, International Finance Cooperation, Global Impact Investing Network, UNDP and others, the onus is on us and our organizations to provide the data necessary to understand impact in context. No one else can do the homework for us, and we can't be lazy. It will require some resourcing, flexibility, learning and nuance, combining all of the tools we have available to us – and asking better questions to challenge each other and raise the bar.

Do you think a standard approach to IMM will emerge in the foreseeable future?
Currently, there are different approaches and methodologies in place. However, tools are improving, metrics will be refined and standards will emerge. We have used tools and approaches that we considered to be the most promising. This process requires a willingness from investors, intermediaries and impact businesses to test, refine and adjust their approaches and share their learnings with the community.

What else is needed to develop the impact investing field?

The BMW Foundation is dedicated to promoting responsible leadership and inspiring leaders worldwide to work towards a peaceful, just and sustainable future. We're convinced that every human being can make a crucial contribution to positive social and sustainable change. That approach also shapes the way we invest our endowment, driven by a dedication to support economic and financial system transformation within the framework of the UN Sustainable Development Goals. This, however, goes way beyond the investment of our endowment and contains a whole set of partnerships, initiatives and projects, from cofounding a platform of competence for impact investing in Germany and a BMW Foundation research fellowship at the University of Zurich, to an accelerator program for young impact entrepreneurs.

What will impact investing be like in 2050?
All investments will be recognized for the impact they have on people and the planet. That data will be as commonly available as financial data, and equally incorporated into decision-making. This won't just be a focus on "impact investing" in a niche of the market... it will be a revolution around the impact of investing.