INSTITUTIONAL INTENTIONALITY | Aligning institutional investors with the global SDG agenda

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ABOUT 17 ASSET MANAGEMENT
17 Asset Management (17AM) is a privately-owned, global asset management company that designs, implements, and manages investments for a broad spectrum of clients. We specialize in blended finance and other innovative financing methods in order to lower risk and increase returns for our customers. Our mission is to align our clients’ financial objectives with the advancement of the United Nations’ Sustainable Development Goals (SDGs). We believe achieving these Global Goals will result in superior long-term returns, while also contributing to a world that is economically prosperous, environmentally secure, and more inclusive. 17AM works with both global asset owners and local stakeholders, to match our clients’ financial interests with SDG needs across our countries of operation. We work in both developed and emerging markets, and have a presence in New York City, Cape Town, and Amman.

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EXECUTIVE SUMMARY

In the new impact economy, investors are increasingly demanding financial products that drive financial returns through creating social and environmental value. To this end, the Sustainable Development Goals (SDGs) are a powerful framework to guide structured investments towards long-term financial value and impact. In this paper, we begin a dialogue on practical applications of the SDGs into portfolio management. Institutional asset owners have tremendous power to shift development pathways, and it is a power that should be embraced to build a sustainable and equitable future.

THE SUSTAINABLE DEVELOPMENT GOALS PROVIDE A HISTORIC GLOBAL OPPORTUNITY.
If the SDGs can be achieved by the United Nations’ target date of 2030, the global economy will grow by an estimated $12 trillion, with the potential for 2-3 times that. Commitment to the SDGs is only growing - 373 asset owners with $19 trillion in assets under management (AUM) have signed on to the Principles for Responsible Investment (PRI), an initiative that closely maps to the SDGs. The opportunity and commitment are apparent; the missing piece is a coherent guide to translate the SDGs into an actionable investment strategy that incorporates the motivations and constraints of asset owners and institutional investors. 17 Asset Management, along with other actors in the impact economy, is facilitating asset owners’ connection with SDG business opportunities in order to make SDG-investing actionable.

THE SDGS CAN ALSO GUIDE INSTITUTIONAL INVESTORS WHEN INVESTING IN NON-LISTED ASSETS.
The SDGs help institutional investors transition from an investment approach rooted in “cause no harm” to actively driving long-term value through structured investments that drive long-term development impact. To date, the environmental, social, and governance (ESG) structure has been a powerful tool in creating public acceptance and demand for impact-driven investments. However, there are asset classes, such as direct equity investment, where ESG investing may provide minimal direction for investors, given its focus on public markets. Evolving from ESG investing towards SDG-aligned investing offers a fundamental opportunity for greater financial return on investment (ROI) thanks to the improved social ROI.

THERE ARE AMPLE REASONS INVESTORS ARE ADOPTING THE SDGS.
A mixture of ethical, commercial, strategic, and policy-related factors all motivate investors to tailor their investments to the SDGs. The SDGs can also help investors align their investments with their stakeholders, who are increasingly impact-oriented consumers, beneficiaries, and internal leadership among fund managers and trustees. Investors are also looking to the SDGs to align with predicted shifts in government policy, including taxes and regulations. Furthermore, some development finance institutions (DFIs) and national governments are de-risking investments with a first-loss facility, and other blended finance facilities, providing financial incentive and creating new markets for SDG investing.

THE SDGS PROVIDE A GUIDE TO EVALUATING RISK AND OPPORTUNITY WHEN CONSTRUCTING AN OPTIMAL PORTFOLIO.
The SDGs can play a significant role in the portfolio planning process, due to their inherent risk
characteristics and presence across asset classes, styles, market capitalizations and locations. Their social, environmental, and economically inclusive dimensions in the underlying investments increase stability, robustness, and indicate better preparedness for a world that demands sustainability, as seen through increasing regulations and consumer preferences.

**ANALYZING FIRST MOVERS CAN HELP OTHER LARGE ASSET OWNERS REFINE THEIR OWN SDG-INVESTING STRATEGIES.**
Select pension funds, insurance companies, sovereign wealth funds, and endowments and foundations have dedicated a portion of their assets to support the SDGs. Analyzing these first movers’ experiences can fill the knowledge gap other institutional investors need to build an SDG strategy with reduced uncertainty. Collectively these institutional investors own over $60 trillion, and while some of them have prioritized SDG investment, there is room for many more to enter and benefit from the space.

**INVESTMENT STRATEGY DEVELOPMENT AND PORTFOLIO CONSTRUCTION ARE CRITICAL PHASES TO ENSURING SDG ALIGNMENT.**
To integrate the SDGs in the investment policy statement, the investment team needs to know SDG achievement gaps in portfolio markets to determine the depth of impact the investment can have, and understand how to examine investments’ anticipated positive and negative effects.

**THE WORLD IS SHIFTING TOWARDS AN IMPACT ECONOMY, IN WHICH SUSTAINABILITY AND SOCIAL IMPACT ARE FUNDAMENTALLY INCORPORATED ACROSS INVESTMENT DECISIONS.**
The SDGs provide a moonshot opportunity for asset owners, managers, and advisers to channel capital towards impact-focused opportunities. Consumers are rapidly demanding both impact and financial return from the capital markets, and the industry is on the cusp of disruption. Improving the capital markets for better outcomes will hinge on asset owners, managers, and advisers embracing the role of intentionality in making investment decisions. Contributing to the SDGs may indeed unlock some of the greatest long-term investments. Institutional asset owners have tremendous power to shift development pathways, contribute to building a sustainable and equitable future, and achieve the SDGs. Our ability to convert those 17 Goals to investment opportunities lies in the partnership between asset owners and intermediaries.
INTRODUCTION - THE SDG OPPORTUNITY

Institutional investors must embrace a sense of intentionality and leverage the SDGs as an investment framework for portfolio strategy.

Both investors and consumers can embrace intentionality to channel capital towards impact-focused investment opportunities. The SDGs are framed as “goals,” to be achieved by 2030, set to hold institutions responsible and to create a shared framework for governments, civil society, and the private sector to work together on agreed-upon standards of action. Investments aligned with the Sustainable Development Goals are defined by their effective allocation of capital that delivers the development of impact economy. In this paper, we hope to stimulate a deeper dialogue on practical applications of the SDGs into portfolio management. Institutional asset owners have tremendous power to shift development pathways, and it is a power that should be embraced to build a sustainable and equitable future.

The Sustainable Development Goals have received an unprecedented level of global buy-in. All 193 member countries of the United Nations have signed on to the 2030 Agenda for Sustainable Development that announced the SDGs. Subsequently, 13,000 companies signed the Global Compact, committing to adopting sustainable and socially-responsible practices. Additionally, 373 asset owners with $19 trillion in assets under management (AUM), have signed the Principles for Responsible Investment (PRI), as well as asset managers with $82 trillion in total AUM.

One main reason behind this large scale of asset owner commitment is the tremendous business opportunity posed by the SDGs. If the SDGs can be achieved by the United Nations’ target date of 2030, the global economy will gain an estimated minimum of $12 trillion, with the potential for 2-3 times more. The achievement of the SDGs by 2030 will also mean the creation of more than 380 million jobs, with almost 90 percent of them in developing countries. The Better Business Better World report has categorized the 60 largest market opportunities of achieving the SDGs into what they define as four economic systems: food and agriculture, cities, energy and materials, and health and well-being. Over half of these opportunities are in the developing world (Figure 1).

Given the large scale of SDG-aligned investment opportunity, and the subsequent scale of commitment to the SDGs by asset owners, what the field needs now is a guide for action on a massive scale.
WHAT ARE THE SDG\text{s}\text{?}

The SDGs are an articulation of the world’s most pressing development challenges, framed by the United Nations as those facing people, planet, and prosperity. In short, the Goals encompass a determination to end poverty, ensure human dignity and equality, protect the planet, and guarantee that all people can have opportunities for decent work and acceptable living conditions.

There are in total 17 Goals, covering the breadth of social, environmental, and economic outcomes. This can be seen in the wide ranging Goals, which include those such as SDG 2: Zero Hunger, SDG 9: Industry, Innovation, and Infrastructure, and SDG 13: Climate Change. The overall framework places special emphasis on the most vulnerable populations and the Goals are designed to be viewed inclusively rather than in silos, partially due to their high correlation with one another. For example, progress on SDG 4: Quality Education, typically means progress on SDG 8: Decent Work and Economic Growth and SDG 10: Reduced Inequalities.
SDG BUSINESS OPPORTUNITIES

Developing countries hold more than half the value of the business opportunities arising from the SDGs

Figure 1

Total opportunity share, %

- Food and Agriculture
- Cities
- Energy and Materials
- Health and Well-being

Developing

Food and Agriculture: 71%
Cities: 55%
Energy and Materials: 50%
Health and Well-being: 50%

Developed

Food and Agriculture: 25%
Cities: 48%
Energy and Materials: 50%
Health and Well-being: 50%

MAINSTREAMING THE SDGs INTO THE INSTITUTIONAL INVESTMENT WORLD

In the past 25 years, the number of companies that measure and report ESG data has sharply increased. Whereas fewer than 20 companies disclosed ESG data in the early 1990s, the number of companies issuing sustainability or integrated reports had increased to nearly 9,000 by 2016. Many ESG indicators map to SDG indicators, and this existing ESG framework will be helpful to investors to draw from in the development of an SDG strategy.

Creating and enabling viable investment opportunities that support the SDGs hinges on disrupting capital markets. This process will hinge on asset owners, managers, and advisers embracing the role of intentionality in making investment decisions. For institutional investors, incorporating the SDGs will not mean remaining highly profitable despite incorporating a “collective benefit” dimension, indeed intentionally targeting the SDGs may be a prerequisite to making more effective long-term investments.

One obstacle to scaling SDG engagement to an even wider investment audience is the tendency to associate the SDGs with “justice” or “charity” mindsets: we owe it to one another, as fellow human beings, to work towards improving the quality of life for all peoples everywhere. It is natural that this mindset prevails, as the SDGs are a vision of a more ideal world, and in a more ideal world all individuals and institutions would work towards, or at minimum not against, the greater social good. The second mindset is that of individual benefit, that which drives people towards efficiency, survival, and profitability.

The mistake is in thinking that the two mindsets are mutually exclusive. The most forward thinking and innovative individuals and institutions will move beyond the false tradeoff between collective and individual benefit. In fact, the investment community is increasingly embedding social and environmental goals into its mandate. The 2018 Preqin Fund Manager Survey identified six key reasons fund managers have begun to incorporate ESG into their investment strategies (Figure 2).1 As the field evolves, they predict “Demand from LPs,” “Competitive Advantage,” and “Value Creation” to rise sharply as motivating factors. This indicates that best practices of incorporating ESG criteria will become more advanced in creating value and real returns for investors. “Regulation” is predicted to have the sharpest increase, indicating how the field expects legal regulation around ESG to evolve as governments hold investors increasingly responsible for the social and environmental effects of their investments.

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Impact-focused investments are no longer going to be solely about “doing the right thing,” but in fact doing what is required in order to stay relevant and competitive. For investors, SDG-investing provides a critical commitment to intentionality towards goals. It supplements the value of ESG as a tool for measuring current activity or historically-focused measurement. Whereas ESG investments are often rooted in “cause no harm,” the SDGs drive long-term value by structuring investments to actively create long-term change in social, environmental, and economic systems.

The ESG and SDG frameworks work largely hand-in-hand: The rise of the SDGs complements and bolsters the growth of ESG investing, and the groundwork laid by evolving ESG criteria helps investors incorporate SDG strategies. While using ESG criteria is more tangible to an investment’s material returns, the SDGs provide more direction and intentionality, and greater long-term benefit. In some asset classes, like direct equity investment, ESG investing may not provide as much functionality, as it is mostly used for public markets. As such, the SDGs and the translation of their targets and indicators can play an important role.

A key advantage of the SDGs is that they create a standard and language for areas of impact. According to the Principles for Responsible Investment (PRI), a United Nations-sponsored international network of investors working towards implementing responsible investment standards, investors and clients do not always agree on which investment decisions and financial products are deemed sustainable. The Goals create a global standard for sustainability and impact. Additionally, investors can use many of the Goals’ 232 detailed indicators to more easily compare progress on gender equality, or reducing hunger, or combatting climate change, or any of the many other issues encompassed by the SDGs. An agreed-upon global standard for sustainability and impact can help investors make ESG-minded investment decisions, and communicate those areas of impact to others.

The work of the PRI and other bodies, such as the Global Compact, to translate the SDGs into business standards and an investment language furthers this effort. The SDGs offer a comparable when evaluating firm performance, and also evaluating new markets. When undergoing market entry analysis, potential regions, countries, or cities to invest in can be compared based on their SDG scores thanks to indexing efforts from the development community. This methodology is leading to more and more countries, cities, and industries incorporating the SDGs as a variable in their investment decisions.

The list below details why institutional investors may adopt an SDG framework in making investment decisions.

**ALIGNING WITH STAKEHOLDERS: INTERNAL LEADERSHIP, CONSUMER PRESSURE, EXTERNAL POLICY**

• **ETHICS OR FIRM VALUES:** An investor may use the SDGs to shape an ethical position, which could lead to them divesting from funds or companies that do not align with those values. A notable example of this is high net worth individuals (HNWIs) and family offices who align their investments with personal and family values. Another common example is firms divesting from “sin” industries, such as tobacco and alcohol.

• **STAKEHOLDER ACTIVISM:** Shareholders, like those who benefit from the proceeds of the investment fund, may advocate for more ethical action or projects that have tangible benefit for stakeholders beyond financial return. For example, corporate shareholders or board members may call for the creation of gender equity policies, or the divestment of funds from certain industries deemed injurious to the environment or society.

• **ALIGNMENT WITH A SHIFTING MARKET OF BENEFICIARIES AND CONSUMERS:** According to a survey by Fidelity Charitable, more than 70% of affluent millennials and Generation Xers have made some form of impact investment, compared with 30% of baby boomers and older generations. Similarly, Natixis Global Asset Management found that 81% of women surveyed believe it is important to invest in ethical companies.

• **ALIGNING WITH GOVERNMENT POLICY:** Governments around the world are considering structuring tax obligations around impact, with the most common example being a carbon tax. The PRI predicts that “a significant proportion of current external costs, such as environmental damage or social upheaval, might be forced into companies’ accounts. The uncertainty surrounding the timing and extent of this internalization is a critical component of the overall risk landscape facing investors.”

“The SDGs drive long-term value by structuring investments to actively create long-term change in social, environmental, and economic systems.”

**PUBLIC-PRIVATE PARTNERSHIPS AND FINANCIAL INCENTIVES:** Some DFIs and national governments are establishing low-cost mechanisms for investors to contribute to SDG-aligned development projects, providing a financial incentive for SDG investing. One example of a blended finance (use of public or philanthropic capital to catalyze for-profit private sector investment in projects that advance environmental, social, and economic well being) initiative is the Triodos Sustainable Trade and Agriculture Fund. The fund provides trade finance and term loans to SMEs that source sustainably produced crops from smallholder farmers and export to world markets with a particular focus on enterprises based in Africa, Asia and Latin America. The fund manages $30 million, and provides first-loss capital accompanied by mezzanine funding.

**AUGMENTING INVESTMENT STRATEGY AND LONG-TERM FINANCIAL RETURNS**

• **FIDUCIARY DUTY:** Investors must consider all financially material factors when acting in the best interests of beneficiaries, which includes activities that aim to prevent or even combat the root causes

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Footnotes 3-7 are missing?  

of systemic risks. Fulfilling fiduciary duty can involve incorporating SDG data that is financially material to investment performance. SDG adoption benefits from the groundwork done regarding ESG factors, which overlap with SDG priorities and can generate returns over the short and long term.

- **UNIVERSAL OWNERSHIP**: Universal owners, by virtue of their size, own a broad range of investments across a national, regional, or global market. Institutional asset owners that invest in a wide range of asset classes, styles and geographical regions, may inevitably be exposed to risks stemming from the development challenges that the SDGs represent. Actively engaging with the SDGs, therefore, contributes to critical risk mitigation.

- **MACRO-LEVEL ECONOMIC GROWTH OPPORTUNITIES**: The SDGs should be a consideration for institutional investors relying on the Modern Portfolio Theory (MPT), or mean-variance analysis. The MPT is built on the concept that greater diversification will result in lowering the overall risk of an investment portfolio. The portfolios of institutional asset owners generally reflect the holdings of the global capital markets. Because of this, the investment returns of an institutional investor become dependent on the continuing good health of the global economy, which could be jeopardized by companies that are not aligned with the SDGs. Thus, institutional investors could take an active role signaling to companies that they will only deploy capital to SDG-focused investments.

- **DEFENSIVE INVESTMENT**: Investors seek high quality investments with good fundamentals during a capital markets’ downturn. When investors are looking for downside protection, they tend to tilt their investment holdings to areas that are larger in capitalization and higher in dividend payments. In volatile times, investors also shift to the defensive sectors for investment, which typically include the healthcare, consumer staples, and utility industries, among others. These sectors can map well to the SDGs: access to water and clean electricity; access to nutritious, affordable food; and healthcare.

- **DECREASING RISK**: Ninety percent of bankruptcies that occurred in the S&P 500 could have been avoided if positive impact investment screening was used. Environmental, social and governance scores have been strongly correlated with companies’ future earnings volatility, both at a market level and within sectors. Moreover, companies with two or more downgrades on S&P common stock rankings had average environmental and social scores in the 40th percentile or lower (weak), whereas those with two or more upgrades had ranks in the 70th percentile or higher (strong). Allocating capital to companies with high external environmental and social costs can lead to a long-term decrease in cash flows and dividends and a lowering of asset valuations. A business with strong fundamentals that internalizes ESG costs is better equipped to protect its cash-flow and competitive advantage from the effects of a catastrophic scenario. Moreover, interest in mitigating systems-level risks can help explain why investors have gravitated towards the SDGs.

“While there is abundant discussion of why the SDGs require substantial support from private investors, there is little information regarding how private investors can engage with the SDGs.”

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8 EY. (2017). Why Sustainable Development Goals should be in your business plan
13 Ibid.
CONVERTING THE SDGs INTO VIABLE INVESTMENT OPPORTUNITIES

Leading organizations like Calvert, Domini, Parnassus, Pax World, and Trillium have been investing in a socially responsible way for over ten years. The impact investment movement has also attracted some of the largest investment banks and money managers, including BlackRock, Goldman Sachs, and UBS. Furthermore, the Rise Fund and Bain Capital Double Impact Fund, and long-time players in the impact space, like Bamboo Capital, Bridges Ventures, LeapFrog Investments, MicroVest Capital, and SEAF, have also increased their private equity activity with a focus on achieving social and environmental impact. In the United States domestic market alone, there were 72 listed Opportunity Zone projects amounting to $16 billion in deal flow as of November 2018. In the impact fixed income product space, there have been 79 Green Bond issues totaling $29.7 billion. In 2018, the major Green Bond underwriters included such names as Bank of America Merrill Lynch, Citi, Crédit Agricole, Goldman Sachs, HSBC, JP Morgan, Mitsubishi, Natixis, SEB, RBC, and UBS.

Beyond these examples, SDG-linked investment instruments and products are gradually coming to market. Global financial institutions, predominantly European based firms, are using the SDGs as a framework for evaluation and measurement. When reviewing SDG-related funds currently in the market, the most evident characteristics are their recent inception dates and relatively modest assets under management (Table 1).

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### Table 1
**SAMPLE SDG-RELATED PRODUCTS**

<table>
<thead>
<tr>
<th>Product Name</th>
<th>Type</th>
<th>Size (USD)</th>
<th>Inception</th>
<th>SDG Focus</th>
<th>Firm Location</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calvert Impact Capital Community Investment Note</td>
<td>Private Equity</td>
<td>410 MM</td>
<td>1995</td>
<td>1, 8, 10, 11</td>
<td>United States</td>
</tr>
<tr>
<td>SEAF Sichuan SME Investment Fund</td>
<td>Private Equity</td>
<td>23 MM</td>
<td>2000</td>
<td>8, 10</td>
<td>United States</td>
</tr>
<tr>
<td>RobecoSAM Sustainable Food Equities</td>
<td>Global Equity</td>
<td>46 MM</td>
<td>2008</td>
<td>2, 3, 10, 12, 13</td>
<td>Switzerland</td>
</tr>
<tr>
<td>Pax Ellevate Global Women’s Leadership Fund</td>
<td>Global Equity</td>
<td>304 MM</td>
<td>2009</td>
<td>5</td>
<td>United States</td>
</tr>
<tr>
<td>Bridges Sustainable Growth Fund III</td>
<td>Private Equity</td>
<td>125 MM</td>
<td>2013</td>
<td>3, 4, 13</td>
<td>United States</td>
</tr>
<tr>
<td>Triodos Multi Impact Fund</td>
<td>Fixed income</td>
<td>30 MM</td>
<td>2015</td>
<td>1, 5, 7, 10, 13</td>
<td>Netherlands</td>
</tr>
<tr>
<td>DBL Partners III</td>
<td>Global Equity</td>
<td>400 MM</td>
<td>2015</td>
<td>3, 7, 8, 10</td>
<td>United States</td>
</tr>
<tr>
<td>Encourage Pescador Holdings</td>
<td>Private Equity</td>
<td>NA</td>
<td>2017</td>
<td>10, 14</td>
<td>United States</td>
</tr>
<tr>
<td>HSBC UN SDG Bond</td>
<td>Fixed Income</td>
<td>1 BN</td>
<td>2017</td>
<td>7, 9, 11</td>
<td>United States</td>
</tr>
<tr>
<td>Union Investment Uninstitutional SDG Equities Fund</td>
<td>Global Equity</td>
<td>32 MM</td>
<td>2017</td>
<td>4, 6, 7, 9, 13</td>
<td>Germany</td>
</tr>
<tr>
<td>Creation Investments Social Ventures Fund I</td>
<td>Global Equity</td>
<td>32 MM</td>
<td>2018</td>
<td>1, 10</td>
<td>United States</td>
</tr>
<tr>
<td>IFU Danish SDG Investment Fund</td>
<td>Global Equity</td>
<td>620 MM</td>
<td>2018</td>
<td>1, 2, 6, 7, 9</td>
<td>Denmark</td>
</tr>
<tr>
<td>Impact Shares SDG ETF</td>
<td>Global Equity</td>
<td>2 MM</td>
<td>2018</td>
<td>5, 13, 15</td>
<td>United States</td>
</tr>
<tr>
<td>ING 7-year green bond</td>
<td>Fixed Income</td>
<td>1.25 BN</td>
<td>2018</td>
<td>13, 15</td>
<td>Netherlands</td>
</tr>
<tr>
<td>World Bank sustainable cities bond</td>
<td>Fixed Income</td>
<td>270 MM</td>
<td>2018</td>
<td>11</td>
<td>United States</td>
</tr>
<tr>
<td>BlueOrchard UCITS Emerging Markets SDG Impact Bond Fund</td>
<td>Microfinance</td>
<td>NA</td>
<td>2018</td>
<td>1, 7, 8, 9, 10</td>
<td>Switzerland</td>
</tr>
<tr>
<td>Bamboo Finance BLOC Fund</td>
<td>Private Equity</td>
<td>113 MM</td>
<td>2019</td>
<td>1, 3, 4, 7</td>
<td>Switzerland</td>
</tr>
</tbody>
</table>

Source: 17 Asset Management research
Within the SDG product space, many funds that specifically target the SDGs have very broad impact mandates, and include a large number of SDGs. Currently, funds are initially drawn to the SDGs as a way to communicate their values to investors. As this space evolves, expertise will develop in parallel to find and focus on assets within a single SDG. Already, products exist across asset classes, styles, and geographies, and as product supply and investor knowledge increase, SDG investing will be more easily institutionalized.

While there is a large business opportunity for SDG-investing, the lack of proper investment vehicles has resulted in limited action in the SDG-investment space. Although there is no shortage of asset owners who have conveyed their interest in investing in the SDGs, a few key obstacles have led to limited action:

• **STANDARDIZING RISK / RETURN / IMPACT TRADEOFFS** and the alignment between the SDGs, fiduciary duty, and financial returns can reduce uncertainty to create asset owner demand.

• **INCREASING PRODUCT SUPPLY** by filling the gap of sustainable institutional investment instruments and products, especially those achieving liquidity.

• **ADVISING FINANCIAL INTERMEDIARIES** and developing frameworks and training workshops to create a class of effective intermediaries who can align sources and uses of capital to the SDGs. Part of the problem intermediaries face is a lack of systems and platforms to facilitate broker deal-making, including exchanges.

To enable more asset owners and institutional investors to enter this field, the above challenges must be overcome in a way that is replicable across investor types. The first step is finding first movers and learning from their experiences.
FINDING FIRST MOVERS - EXAMPLES OF SDG INVESTMENTS AND PRODUCTS

Highlighting, understanding, and replicating the larger asset owners that are making their way into this space can help in identifying SDG investment opportunities. In particular, pension funds, insurance companies, sovereign wealth funds, and endowments and foundations can all align their investment agendas with the SDGs. Collectively, these institutions have over $60 trillion AUM, and the table below provides some insight into the role that each of these institutions can play in the larger field of SDG investment.
Table 2
EXAMPLES OF INSTITUTIONAL ASSET OWNERS FOCUSING ON SDGs

<table>
<thead>
<tr>
<th>ROLE</th>
<th>FIRST MOVER</th>
<th>PENSION</th>
<th>INSURANCE</th>
<th>SOVEREIGN WEALTH FUNDS (SWF)</th>
<th>ENDOWMENTS AND FOUNDATIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>PENSION</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The second largest group of asset owners globally are</td>
<td>APG and PGGM, the two major Dutch pension funds, have defined</td>
<td>Pension funds globally hold over $36 trillion AUM, and</td>
<td>British insurance group, Aviva, is a strong advocate for the SDGs.</td>
<td>Sovereign Wealth Funds (SWFs) collectively hold $7 trillion and</td>
<td>Endowments and foundations hold $1.4 trillion in combined</td>
</tr>
<tr>
<td>insurance companies, with over $23 trillion of assets. These</td>
<td>a comprehensive decision tree mapped to the SDGs to find</td>
<td>often rely on liability-driven investment strategies. They are</td>
<td>Aviva boasts “we see ourselves as a 320-year-old disruptor” and</td>
<td>are players in the SDG and impact investment space. SWFs are</td>
<td>assets. Endowments tend to serve educational institutions while</td>
</tr>
<tr>
<td>companies are significant players in the responsible</td>
<td>“Sustainable Development Investments” that meet financial risk</td>
<td>in a position to be at the forefront in the integration of</td>
<td>“since issuing our first insurance policy over 300 years ago, we’ve</td>
<td>inherently invested in their respective country’s domestic</td>
<td>foundations seek alignment between their missions and the</td>
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<td>investment space, investing with a returns-based mentality</td>
<td>and return requirements and support positive social and environ-</td>
<td>responsible investing, yet are often hesitant to allocate</td>
<td>never been afraid to tackle the big issues” like climate change</td>
<td>policy priorities as well as foreign interests. Domestic projects</td>
<td>companies they invest in.</td>
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<td>that is tied to matching their assets to their current and</td>
<td>mental impact through their products and services. These global</td>
<td>greater dollars to the SDG and impact spaces, due to a lack</td>
<td>and an aging population. As an insurance firm looking at the long-</td>
<td>could include national infrastructure projects, and foreign</td>
<td>The second largest group of asset owners globally are</td>
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<td>future liabilities. Insurance companies readily invest in a</td>
<td>leaders have published their decision tree online, to assist others</td>
<td>of understanding of driving returns with impact-aligned</td>
<td>term, Aviva is invested in the health and well-being of individual</td>
<td>investments could contribute to the SDGs, aligned with the</td>
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<td>socially and environmentally impactful way, primarily</td>
<td>in making capital allocation decisions aligned with the SDGs.</td>
<td>investments.</td>
<td>people and the overall economy, making it a natural fit to incorpo-</td>
<td>country’s provision of Official Development Assistance (ODA).</td>
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<td>through the debt markets, and also look at developing future</td>
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<td>rate the SDGs into its core strategy. The Reinvestment Fund (TRF),</td>
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<td>insurance markets when investing in economically challenged</td>
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<td>is a Community Development Financial Institution (CDFI), based in</td>
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<td>areas.</td>
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<td>the United States, with more than 800 investors and $1 billion in</td>
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<td>managed assets. TRFConnects mainstream capital to the financial</td>
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<td>needs of low-income communities across the United States, using</td>
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<td>investment grade (AA - by Standard &amp; Poors) bond issues. The</td>
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<td>proceeds of these bonds support small businesses, grocery stores,</td>
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<td>childcare centers and affordable housing in struggling communi-</td>
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<td>ties, thus touching more than half of the 17 SDGs. Demand for</td>
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<td>these general obligation bonds have far exceeded their initial</td>
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<td>expectations, leading to oversubscriptions.</td>
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Building an investment strategy

Developing an investment strategy aligned with the SDGs is predicated on including the Goals within each step of the strategy planning process. Typically, institutional investors follow a three-step portfolio management process:

**STEP 1: PLANNING**

- **KEY ACTIVITIES**: Objectives and constraint determination, investment policy statement creation, capital market expectation formation, and strategic asset allocation creation.

- **DESCRIPTION**: With the help of investment professionals, institutional fund trustees formulate and adopt a written investment policy that is used as a blueprint to manage the fund’s assets. If an investment type or mandate is not written in the Investment Policy Statement (IPS), it will not appear in an institutional investor’s portfolio. The IPS sets forth the fund’s investment objectives, asset allocation guidelines, manager selection process, fund and manager evaluation methods, investment restrictions and guidelines, and other matters concerning in-house investment. The IPS also delineates the fund’s needs (e.g., stated annual performance goal), desires (e.g., limiting losses in a down capital market) and restrictions (e.g., limiting the exposure to certain companies and industries).

- **SDG INTEGRATION**: SDG mandates are created based on desired social outcomes (the target level of the SDGs), how SDG-alignment can drive financial outcomes based on the sociopolitical context the fund’s assets will operate in, and how assets can drive systems-level solutions to the SDGs. This information is typically derived from intensive research processes. These considerations need to be incorporated into the fund’s objectives, and investment restrictions and guidelines.

**STEP 2: EXECUTION**

- **KEY ACTIVITIES**: Portfolio selection, composition, and implementation.

- **DESCRIPTION**: In order to fill the asset classes stated in the IPS, asset sub-classes and investment styles are defined and a request for individual investment managers is made. The purpose of the refinement of the IPS is to arrive at an optimal portfolio combination that will maximize its investment returns while minimizing its risk. The money managers that are interviewed and eventually selected are evaluated on their individual risk and return profiles along with their fit within the fund’s written objectives.

- **SDG INTEGRATION**: The SDG outcomes selected in Step 1 of the process inform portfolio selection and due diligence. Money managers are also selected based on their knowledge of SDG investing.

**STEP 3: FEEDBACK**

- **KEY ACTIVITIES**: Performance evaluation and portfolio monitoring and rebalancing.

- **DESCRIPTION**: All aspects of the investment portfolio must be measured against the standards set forth in the IPS. After an optimal portfolio is adopted, the fund trustees have the responsibility to monitor the qualitative and quantitative changes that will occur in both the individual holdings and the overall portfolio. Measuring the performance of the assets, in terms of risk, return, and impact, must be completed on an ongoing basis.

- **SDG INTEGRATION**: Developing robust processes for SDG monitoring and evaluation is integral to the ongoing monitoring of the portfolio’s performance. The ability to guide portfolio companies in their SDG-alignment and operations that achieve social and environmental impact can assist in augmenting this step.

Adhering to this process enables asset owner to build an investment strategy. Integrating the SDGs into the language of the IPS, due diligence, and portfolio management is vital groundwork to creating a working SDG investment strategy. Adopting IPS language, meeting risk-return profile, and implementing measurements are fundamental to institutional asset owners’ agendas. Asset owners can use the SDGs as a tool to build an investment framework, but only if they achieve this alignment.

The inclusion of the SDGs in the planning process can play a significant role in building an optimal portfolio, due to the Goals’ inherent risk characteristics and the
fact that they exist in all of the broad asset classes (e.g. stocks, bonds, cash, commodities, alternatives), styles (e.g. stocks - value, growth), market capitalizations (e.g. stocks – large, mid, small, micro) and locations (domestic, foreign developed, foreign emerging).

Incorporating the SDGs into a coherent investment strategy requires the investment team to develop an understanding of the SDGs as a framework, and particularly the Goals targeted by the firm. Next, the investment team needs to understand the key factors that determine if the chosen Goals will be accomplished and the role of institutional investors in contributing to, and partnering with other actors to contribute to reaching that Goal. It also requires research into the SDG achievement gaps in portfolio markets to determine the depth of impact the investment can have. To stay true to the nature of the Goals, impact reports should examine both positive and negative effects of investments.

CONSTRUCTING AN SDG PORTFOLIO:

Once asset owners have included SDG language in their written IPS, they can build an investment portfolio. To do so, it is helpful to examine how other institutional investors have incorporated sustainable investments into their investment process. Institutional investors have typically adopted one of three recognized impact investment strategies (Table 3).

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Process</th>
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<tr>
<td>Portfolio Overlay (Holistic)</td>
<td>A Total Portfolio Management (TPM) impact investing lens can be used to view the entire portfolio. Portfolio design, construction, and reporting is completed by using the SDGs and the framework’s three dimensions (social, economic, and environmental) of sustainable development as an impact investment tool.</td>
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<tr>
<td>Balanced Sleeve (Carve-Out)</td>
<td>Balanced Sleeve is a staged approach to impact investing that takes a portion of the total portfolio, creating a balanced impact sleeve by using the same portfolio design, construction, and reporting tools utilized in the portfolio overlay strategy. The remainder of the total portfolio is invested in a traditional investment format.</td>
</tr>
<tr>
<td>Theme Specific Sleeve (Carve-Out)</td>
<td>An impact themed approach takes a portion of the total portfolio creating a theme-specific sleeve, by using the SDGs as the guide for the portfolio design, construction, and reporting tools. The remainder of the total portfolio is invested in a traditional investment format.</td>
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</table>

Taking a portfolio approach to SDG investing is critical, not only for private sector investors but also for international financial institutions like the European Investment Bank, and development finance institutions, such as CDFI Banks, that seek to contribute to development outcomes. Notably, different types of asset owners will opt for different portfolio approaches. For instance, institutional asset owners in the United States have tended to use the theme specific sleeve strategy to address shareholder, participant, and mission and impact-related concerns. To date, the least used of the three strategies is the portfolio overlay. Although this holistic approach has been embraced by a few endowments and foundations in the United States, it has been more widely used by European asset owners. The balanced sleeve method is currently underutilized, and could be incorporated into situations where fund trustees cannot currently commit to the portfolio overlay approach but can break off a portion of their portfolio to enter the SDG investment space.
DEALING WITH RISK

Investors’ perceptions of risk have impinged on their willingness to adopt an SDG lens. One de-risking tool is blended finance, the use of public or philanthropic capital to catalyze for-profit private sector investment in projects that advance environmental, social, and economic well-being. This process increases funding for public-benefit projects and works by using concessionary capital to incentivize return-oriented investments. It is a structuring approach, not an investment approach. As blended finance gains traction and popularity in the market, it will pave the way for the private sector to increase SDG-aligned investment, and investments in developing markets that are traditionally seen as too risky.

IMPACT MEASUREMENT: Thorough impact measurement is critical to SDG-aligned investing. As Peter Drucker, influential thinker on management strategy, is often quoted as saying, “you can’t manage what you can’t measure.” Without proper impact measurement, it becomes impossible to monitor a portfolio company’s positive impact on the community within which it operates, to guard against negative impacts, to measure the additionality the investor has in claiming a portion of that impact, and to gather information about best practices to use in future investments. Additionally, a well-defined impact thesis, incorporated into the IPS, and well-executed impact measurement creates transparency, which is vital to attracting investors to a fund, as well as solidifying community engagement and partnerships which can augment the social return on investment (SROI) of a fund.

The SDGs, by design, provide a definitive framework for measuring impact. If these measurement tools are adopted by institutional investment committees, the SDGs can be the standardization that the industry has been looking for in building impact protocols and benchmarks. While tremendous effort has gone into the standardization of ESG criteria, definitive standards around this set of indicators has not yet been accomplished. The opportunity of the SDGs to be adopted as a framework is amplified by their alignment with government priorities, company priorities, and the needs of long-term institutional investors.

The Impact Measurement Project (IMP) has created a framework to propose actions investors can take to move them along the impact spectrum, from avoiding harm to contributing to systemic solutions. In tangent, the group has also created a spectrum of the depth of an investor’s contribution, from signaling that impact matters to growing new capital markets and providing flexible or patient capital. IMP proposes five areas in which an investor can measure impact: 1) what outcomes people and the planet experience and how important those outcomes are to those experiencing...
them, 2) who experiences the outcomes and how underserved they were previously, 3) how much of the outcomes occur, in terms of what degree of change they experience, and how long they experience the outcome for, 4) the contribution that enterprises and investors make to the outcomes, relative to what would likely not have occurred otherwise, and 5) the risk that impact is not as expected. IMP is seen as a “revolutionizing factor” for the impact investing industry given its broad applicability across asset classes and impact themes. Its traction is growing as a tool to plan and communicate impact measurement.

The industry also has other tools that can guide the impact measurement process. For instance, SEAF’s Gender Equality Scorecard is a proprietary methodology used to assess women’s economic empowerment and gender equality within the fund’s investment portfolios. Additionally, the Refugee Investment Network’s (RIN) refugee lens for investment focuses on refugee ownership, leadership, and potential for catalytic change within refugee communities. The RIN methodology helps to identify activities that are refugee-supporting, or refugee-host-community-supporting. Drawing from these organizations’ impact measurement frameworks can assist in constructing an overall SDG-aligned risk, return, and impact measurement strategy.

Furthermore, investors developed a shared language to communicate impact before the SDGs were created, and adapting the SDGs to existing frameworks can facilitate alignment across the industry. The Global Impact Investment Network’s IRIS is a catalog of performance metrics that impact investors use to measure the social, environmental, and financial performance of their investments. Additionally, Toniic21, a network of high net worth individuals and family offices working together to build the ecosystem of impact investing, has developed the Impact Theme Framework, which highlights the alignment between and IRIS indicators and the SDGs.

Part and parcel of developing an impact measurement strategy is communicating that strategy’s robustness. In this vein, the Impact Measurement Project is assisting the United Nations Development Programme (UNDP) to create an “SDG certification” to provide an official verification of SDG-aligned investing. Third-party validation of SDG-alignment, particularly from an entity as universally recognized as the United Nations will help reduce uncertainty among investors wary of SDG washing.

This certification will be part of the UNDP’s SDG Impact. Overall, SDG Impact is also one of several programs empowering investors and businesses to contribute to the SDGs by creating investor-friendly knowledge of the SDGs. Specifically, the SDG Impact initiative aids investors and portfolio companies to adapt and transform their core business strategies to deliver financial, social and environmental performance, and to use the SDGs as the basis for engaging in untapped markets, including by providing country-level data and SDG investment roadmaps. Another leader in this effort is the Swedish Investors for Sustainable Development network. The group is comprised of 18 institutional investors, pension companies, investment companies and the Swedish International Development Cooperation Agency (SIDA) to explore the role of investors in achieving the SDGs, potential investment opportunities, and jointly overcoming obstacles. Similar groups based on the Swedes’ example are also starting to form, such as a new global group being formed by the United Nations Department of Economic and Social Affairs, based on SIDA’s experience.22 Efforts to include and clarify the role of institutional investors in the achievement of the SDGs can help integrate the goals into investors’ strategies, and make those strategies more successful.

This can stimulate a deeper dialogue on practical applications of the SDGs for portfolio management. We urge asset owners and financial consumers of all sizes to push their advisors and vendors to integrate the SDGs, and the corresponding intentionality it brings, to their portfolios.

Recruiting the investment community as allies in this movement hinges on clearly and effectively spelling out tangible opportunities. To do so, the investment and development communities must work hand-in-hand to build viable financial products that can channel capital towards the SDGs, thereby crafting a new investment paradigm in global capital markets. Applying innovative finance techniques such as blended finance, pay for success bonds, loan guarantees, political insurance, first loss equity, concessionary loans, and others, can usher in a new mindset amongst investment bankers, financial intermediaries, and asset owners.

The SDGs offer investors a historic opportunity, as well as a foundation on which we can build towards an impact economy — a system in which financial and social returns are complementary and help to ensure a sustainable and prosperous future. The major advances of our time have come from audacious vision from leaders and a herculean cooperative effort to achieve that vision. With 193 countries agreeing to 17 Goals with 169 targets and 232 indicators to solve the world’s problems by 2030, have any considered the profound affect it may have on the capital markets? Just like putting a man on the moon and looking at the earth from space, or seeing how human’s genes map together, understanding our investments and business practices through the SDGs can advance society in ways we have only begun to imagine.