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Positive impact finance

The UN is working with financial institutions to close the SDGs funding gap by generating much-needed private sector finance

By **Eric Usher**, Head, UN Environment Programme Finance Initiative (UNEP FI)

With the 2017 launch of the Principles for Positive Impact Finance, UNEP FI has proposed a framework to help financial institutions adopt a holistic, impact-based approach to their commercial financing activities. In 2018, we're making it a reality. Sounds fancy? Don't get us wrong: there's no such thing as altruistic finance. Or rather, there is something called philanthropy, but philanthropy alone will not close the Sustainable Development Goal (SDG) funding gap. Some estimates put the shortfall at $2.5 trillion a year – an amount the public sector can't afford and must hope that the private sector, somehow, will handle.

On the surface, this looks like an ominous, intractable challenge. Existing solutions – such as green bonds or blended finance – are growing, but have yet to make their mark at scale. What else is possible?

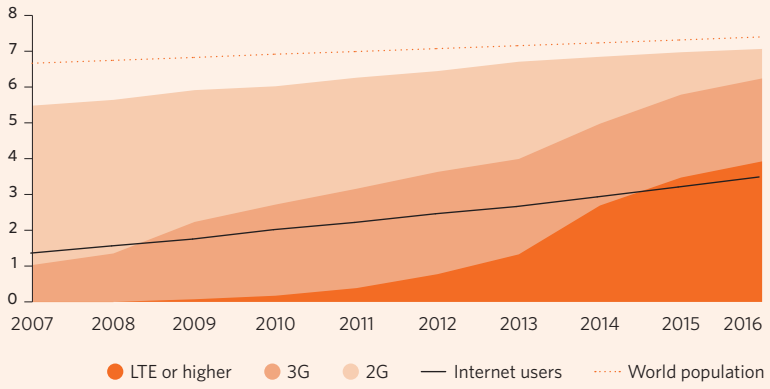
Let's remind ourselves of some facts and figures. First, the largest part of this financing gap comes in emerging markets. In Africa, the gap is estimated at an annual $1.3 trillion, or about 90 per

▲ **Bridge under construction in the port of Maputo, Mozambique. Africa needs an estimated extra $1.3 trillion per year in funding to be able to meet the SDGs**

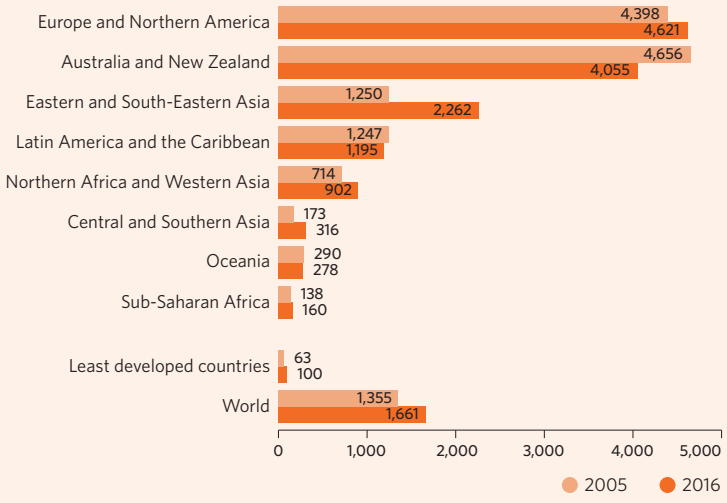
9 INDUSTRY, INNOVATION AND INFRASTRUCTURE

Build resilient infrastructure, promote inclusive and sustainable industrialisation and foster innovation

Number of people covered by a mobile network, by technology, 2007-2016 (billions)



Manufacturing value added per capita, 2005 and 2016 (constant 2010 US dollars)



Infrastructure, industrialisation and innovation are three drivers of economic growth. When inclusivity, resilience and sustainability are factored into the implementation of these driving forces, economic growth can support sustainable development

Source: The Sustainable Development Goals Report 2017, United Nations

cent of financing needs. Might one see the makings of a huge opportunity?

Second, while many of us have been concerned about the SDG financing gap, what we see is first and foremost a solutions gap. Think about frontier and emerging markets. These regions and populations have very little in the way of infrastructure – from energy to healthcare, education to mobility. It's often less of a gap and more of a void. Here, again, are the makings of an unparalleled opportunity.

This is how it works: the public sector is frequently tasked with providing essential services such as energy, mobility, healthcare or education to citizens. This involves public planning and tendering chief mechanisms. Public authorities may choose to contract out these services in the form of projects to specialist suppliers. Companies, governments and development institutions will turn to banks to secure financing for the projects – such as loans, project finance or trade finance. The banks will then sell the financing instruments onwards to institutional investors – for example by aggregating them, and offering the package in the form of bonds or other investment products.

What we see here is a mechanism by which a macroeconomic policy objective is turned into a string of microeconomic business solutions. For example, a city's goal to educate its children translates into schools and school financing. But there is a risk. The schools' walls may be built, but there is no guarantee that the public sector's initial goal of education will be met.

Consider how local authorities tend to approach service provision. Typically, they provide services in a discrete way, by which individual public services or contractors are called on to meet one social or environmental objective or another – street lighting, air quality monitoring, public transportation, and so on. This multiplicity of solution providers results in a very high cost-to-impact ratio.

Instead, governments can challenge the private sector to develop solutions by issuing impact-based requests for proposals. In response, companies, in association with the finance sector, would compete on designing business and financing solutions to the

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SDGs, with the best cost-to-impact and public-to-private financing ratios.

With such an impact-based approach, integrated solutions addressing multiple needs can help to reduce costs. For instance, public lamp posts can be fitted with technology and used in many different ways: to monitor air quality, to provide video surveillance, or to serve as a charging station for electric cars or other appliances. Some of these services can generate revenues and sustain private sector interest in the business.

This shows the need for the private sector to innovate based on an impact analysis of the market. So, what are the impact value chains contained in the SDGs, and what role might the private sector play in that chain?

The finance sector for its part needs to become actively involved in developing such business models with its clients and investee companies. This is key if we want to realise the big business opportunity of the SDGs and, indeed, achieve the SDGs themselves. To play this role, finance needs to equip itself with the means to understand impact in the first place.

Principles for Impact Finance

What positive impacts can be generated and what negative impacts can result from a given activity and hence through a given investment? What risks are inherent to financing certain activities where negative impacts cannot be addressed? What business opportunities reside in the positive impact – or potential for positive impact – linked to a company's activities and profile?

How can this potential be developed so that the investable SDG market can grow?

This is where the Principles for Impact Finance kick in, to help financial institutions adopt a holistic, impact-based approach: from the very first stages of identification and analysis, to those of product structuring, distribution and, finally, monitoring and reporting.

In doing so, the principles prepare financial institutions for an economy where impacts will become more central. They offer a common language to all actors, public and private, that need to engage with each other in this transition.

UNEP FI is drawing on its deep expertise of collaboration with the financial sector to lay the groundwork for Positive Impact Finance. We have been working in partnership with leading global banks, investors and markets to develop solutions.

In 2018 we will be exploring how different financing solutions, debt, equity or notes can adopt a positive impact approach. We will use real-life examples and case studies, and develop guidance notes. We are exploring impact-based tendering through concrete partnerships with municipalities. A new research paper will provide deeper insights into the solutions we propose.

At its heart, Positive Impact Finance proposes we start with objectives front and centre in mind. It builds on the knowledge that public sector engagement of the private and finance sectors at the planning stages is a necessary evolution. As the Carillion story shows in the UK, there is no shortage of business risks to public–private partnerships. But the numbers don't lie: private finance and business are the core force underpinning the realisation of the SDGs.

To 2030 and beyond, Positive Impact Finance will reconcile economic opportunities with people's basic needs and respect for the environment. ●

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► Geothermal power plant near the Blue Lagoon hot springs in Iceland. A 500MW geothermal project has recently commenced in the Corbetti caldera in Ethiopia. The project, which brings together technology from Iceland and private equity finance, supported by core finance from MDBs, is a good template for bridging the SDG funding gap