SPECIAL REPORT

What Role Does Germany Play in the Impact Investment World?

In this article, Dr Andrij Fetsun (pictured), CEO of Agents for Impact GmbH & Co. KG (AFI), a burgeoning impact investment company in Germany, addresses the topic of Germany's role in impact investing. Andrij has lived in Germany since 2008. Prior to co-founding AFI, Andrij was a Senior Portfolio Manager at Invest in Visions GmbH, where he built the portfolio management division of the company from scratch. Within four years, Andrij managed to grow the IIV Microfinance Fund portfolio from EUR 98 million to over EUR 661 million without any defaults. His 10 years of professional experience in impact finance include engagements with KfW and the Frankfurt School of Finance & Management, where he promoted SME finance as well as microfinance. Andrij started his career in portfolio management in the private banking department of BHF-Bank, Frankfurt. Andrij also published several articles on quantitative approaches in portfolio management and on environmental, social and governance (ESG) integration in portfolio management when he was at Veritas.

Impact investing and sustainable finance as a personal choice

My interest in impact investing has its roots in my personal belief in living and working in a manner that is environmentally and socially sustainable and responsible. For instance, on a day-to-day basis, I come to the office by city scooter regardless of the weather. I don't own a car as a matter of principle. Throughout my professional experience with Frankfurt School and IIV, I built my knowledge and capacity in the sector and finally decided to venture out and start a business that combined sustainability with finance. And that's how AFI was born in 2018. I co-founded the firm and have been its managing director since then. I find it very satisfying to be associated with an impact investing company that seeks to help impact investors in Germany find stellar opportunities for sustainable investing around the world.

Impact investing and sustainable finance as a growing sector in Europe

Impact investing in Germany is on its way to becoming mainstream in all segments of the economy. When I talk about impact investing, I do not mean ESG or sustainable funds in general, but investments with an intentional, measurable social and environmental impact alongside a financial return, for example as defined by GIIN. According to the FNG market report, the share of sustainable funds and mandates, including impact investments, in the German fund market is only 9.4 percent as of December 2021.

It is always interesting to compare the figures, especially for me as a mathematician: In contrast to Germany, the FNG market report states that in Austria during 2021, sustainable funds and mandates grew to account for 28 percent of the total fund market for the first time. The volume of sustainable funds in Switzerland accounted for 53 percent of the total Swiss market in 2021 (compared to 38 percent in 2019). Thus, funds using sustainable approaches are outcompeting conventional investment funds in Switzerland. This all serves as proof that Germany still has some catching up to do in the field of impact investing.

Current trends in impact investing

Green bonds and other sustainability-linked bonds are currently a very popular and widely used product across the globe, with local governments getting in on the trend as well. It all began with the European Investment Bank's issuance of the first green bond in 2007. The popularity of sustainability-linked bonds also has driven the growth of other fixed-income ESG and impact investments such as microfinance, supply-chain loans and blended finance products (to name a few).

AFI has been serving as investment manager to IIV for its microfinance funds for three years. During this time, AFI-IIV generated more than EUR 200 million in microfinance loan transactions. Moreover, AFI has been analyzing ESG plausibility for capital management companies, including HANSAINVEST, which has been an AFI client for three years.

But aside from impact investing advisory and transactional support, AFI has also developed a tool - AFISAR - that helps to rate and rank companies on their contributions to the UN Sustainable Development Goals (SDGs). The microfinance sector, for example, is very relevant to the following SDGs: SDG 1, No poverty; SDG 5, Gender equality; SDG 8, Decent work and economic growth; and SDG 10, Reduced inequalities. With governments imposing strict ESG requirements, investment companies will only need more help with SDG and ESG ratings and sustainability advisory services going forward.

The importance of impact investing for regulated investors

Interest in and demand for products with measurable, positive social and/or environmental impact are growing in the German financial market. Many investors will therefore become much more involved in the sub-sector, and the market for impact investments will continue to grow.

The compliance and regulatory requirements in Europe have become more complex, for example with the introduction of the EU Sustainable Finance Disclosure Regulation. While these regulations contribute to transparency, they also pose a great challenge for the market to ensure compliance. This is where AFI's ESG and SDG rating teams can be of great help for investors! When our rating team analyses a company's SDG alignment, for example, this helps us guide the company to become more sustainable.

The role of AFI in the impact investing sector

As an impact investing company, AFI can serve a range of different institutional investors: such as family offices and asset managers that invest in non-liquid assets. Our investment approach is top-down. We start by analysing macroeconomic and country risks. Then we look at the regulatory environment and only afterwards at credit risk, of which ESG is one part. But before we even start, we use our SDG rating to measure whether the investees sufficiently align with the UN SDGs. Our team - including investment officers, the SDG rating team, the ESG team and the legal team - participate in each due diligence process. Of course, we need to understand the varying legal aspects in different regions, and we already have demonstrated this expertise in 11 countries.

In total, we have generated more than USD 217 million worth of transactions since receiving regulatory authorization in October 2019. It is also extremely noteworthy that our loan default rate has been zero. We have agents on the ground in various regions like Central and South Asia, Africa, and Eastern Europe. This is how we were able to work smoothly - including conducting due diligence on potential investees - even during the worst days of the COVID-19 pandemic. Meanwhile, it is always my goal to get to know our clients personally. As examples, I spent a month in Cambodia and two and a half months in India to better assess the situations on the ground.

Expectations for the field of impact investing in 3 to 5 years

More funds in Germany need to get into the impact investing space in Germany, and the government can help by ramping up incentives for the sector. Increasing the volume of sustainable funds in Germany would not only help us keep up with neighbouring countries, but would also help emerging markets to achieve the SDGs.

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