New Studies Assess the Risk of Impact Investing and Find It May Help Investors Focus on the Long Term in a Short-Term World

White Papers Call for a Deeper Understanding of Long-Term Investment Risks and Rewards

New York City

Private capital is being called upon to solve some of the world’s most pressing social and environmental issues. At the same time, the business and investment worlds appear to be focused increasingly on the short term. In two new white papers, the Chief Investment Office of Bank of America’s Global Wealth and Investment Management division examines these converging trends and assesses the risks and benefits of impact investing.

*Deconstructing Risks in Impact Portfolios* explores the risk and return characteristics of different impact investment approaches, with the goal of addressing common investor misperceptions that all types of impact investing have a higher investment risk.

The study looks at four distinct categories of impact investing to assess the risk and return profiles of these categories. They include: Socially Responsible; Sustainable; Thematic; and Impact First. The study concludes that the risk is equal to that of traditional (non-impact-oriented) investments, except where completely new business models are being created to effect social or environmental changes. Moreover, the use of environmental, social or governance (ESG) factors within investment analysis can actually help investors identify different types of risk. The study concludes that the major additional risk that impact investment strategies have is that they end up not having the intended positive ESG-based outcomes.

“As more investors use impact investing as a way to achieve their ESG goals alongside their financial goals, it is increasingly important to understand how these investments can help investors better identify risks and opportunities for their portfolios,” said Anna Snider, head of due diligence and co-head of impact investing for Merrill Lynch.
Impact Investing: The Long-Term View further examines the topic of risk as it relates to short-term decision-making and how the use of ESG factors can help investors reorient around a longer investment timeframe to assess both risk and return, with the potential to help better preserve portfolio value.

“Investors should take the time to understand long-term risks and rewards and explore how impact investing can help create portfolio value over an extended period,” said Snider. “With careful evaluation and investment selection, investors can improve their prospects of achieving both their financial and their ESG-based goals.”

With holding times for equity shares at record lows, reduced spending on corporate research and development, and profits going to share buybacks instead of investments in talent, facilities or equipment, corporations and shareholders are focusing on the bottom line short-term, according to the study. This bodes ill for long-term competitive prospects or for shareholder returns, the study found. Additionally, high share turnover can result in adverse tax consequences and higher costs that can erode investor returns.

Impact investing as long-termism

Impact investing may offer an antidote to such short-termism on both the risk side and the return side, according to Impact Investing: The Long-Term View. Taking into account ESG factors while also investing with a longer-term horizon may result in a more holistic approach to investment selection. Risks and opportunities that otherwise might be overlooked can be taken into account and incorporated into investment decisions.

Impact and ESG strategies are growing rapidly and reached $8.72 trillion in 2016, 33 percent more than two years earlier, according to the latest Report on U.S. Sustainable, Responsible and Impact Investing Trends by the U.S. SIF Foundation. The increasing scale of impact investing has brought greater scrutiny of portfolio risks and effects as well as associated societal benefits.

Through its advisors, thought leadership, and investment offerings, Merrill Lynch Wealth Management, Merrill Lynch Private Banking and Investments Group, and U.S. Trust help position clients to invest according to their goals and values.

“We want to encourage investors to think about their long-term goals and invest with purpose, however they define that personally,” said Keith Banks, head of the Global Wealth and Investment Management division’s chief investment office and Investment Solutions Group. “ESG factors can help identify environmental and social risks over time and help clients and advisors integrate them into investment assessments.”

Impactonomics®

Impactonomics® is a thought leadership series published by the Impact Investing Council within the Global Wealth and Investment Management Chief Investment Office (GWIM CIO) of Bank of America. It examines the relationship between economic growth, investing for impact and profit, and the measurable social and environmental change it can bring. This publication is the second of two follow-up papers to the original Performance Realities piece published in 2015. The first paper, “Performance Realities II: Deconstructing Risks in Impact Portfolios,” can be found at ml.com/impactinvesting.
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