CONCEPT NOTE FOR UNECE MINISTERIAL BREAKFAST – ANNUAL MINISTERIAL REVIEW 2013

Making a difference: impact investment and the financing of innovation

Innovation provides an answer to social and environmental problems through the introduction of new products, production processes and business models that promote positive change. The mobilization of appropriate financing that is aligned with the risk profile of innovative companies is a major hurdle that needs to be overcome in order to unleash this transformative potential.

The key challenge for public policy is to attract private financing to support goals that are of public interest. Private and public assessments of costs and benefits may differ and risks may be perceived as too high by the private sector to provide the necessary financing.

There are multiple types of risk influencing investment decisions (technological, market, regulatory…). **Collaborative arrangements between public and private stakeholders can contribute to reducing or sharing risks and, therefore, facilitate financing**. Public policy can positively affect perceived risks (which may be higher than actual risks), thus creating a barrier to investment. Public policies impacting the business environment can also improve the risk/return ratio for private investors, thus encouraging larger investments, including through the creation of favourable investment framework conditions that facilitate the transformation dynamic.

A relatively recent approach to investment which could be of particular interest to policy makers is impact investment. These are investments made with the intention to obtain, in addition to financial returns, concrete social and environmental outcomes. Thus, they can serve to enhance the achievement of development goals. Impact investments are often structured in a similar way to traditional venture capital financing, as investors take an active role in nurturing the development of the project and provide not only financial resources but also managerial and technical support. **Public policies can promote the emergence of specialized financial intermediaries who bring particular skills to the investment process** and provide financing which is attuned to the particular needs of innovative companies.

Public development financial institutions can behave as impact investors, as their provision of resources is linked to achieving particular social and environmental goals while paying attention to the sustainability of interventions and the economic rationale of the investments undertaken. **Seeking a financial return on investments opens access to larger pools of capital than simple reliance on aid.**

In the current economic climate, where risk aversion has increased, a major concern is to ensure that the available capital for innovative projects with a social or environmental impact does not shrink and that investors operating in this field have the continued ability to raise funds. Policy needs to pay attention to the role of institutional investors as a source of capital for impact investments and innovation financing, creating an appropriate regulatory environment and raising awareness about potential opportunities.

Increasing the availability of finance should not be an overriding policy concern that neglects other factors that may be constraining innovation. Sometimes, the reluctance of private investors to provide financing reflects the absence of investable opportunities rather than problems in raising funding. Attempting to correct this only through measures to increase the supply of financing can distort market conditions without addressing the absence of a sufficiently robust supply of financeable projects. An important policy consideration is how to effectively combine interventions to mobilize financing with actions to increase the "investment readiness" of projects seeking finance.

Key questions to guide the discussion:

1. How can collaboration between the public and the private sector be structured to raise financing for innovative projects with positive social and environmental outcomes? What are the factors that explain the success of this public-private collaboration and the pitfalls that need to be avoided?
2. How can international cooperation support the emergence of effective innovation financing models? What mechanisms can be put in place to facilitate policy learning?
3. How can the contribution of impact investments to development goals be increased?
4. How can obstacles to cross-border fundraising and investment be eased?
5. How can innovation and impact investment projects be structured in order to better reduce investment risks (thus increasing financing opportunities) -- and what role could the public sector play in this?