Approaches to Assess and Measure Impact
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22 May 2019
ESG and Sustainability
Investing in “green energy” is not sufficient in itself

Our vision:

- Environmental responsibility is consubstantial to energy transition
- The granularity of investments entails a multiplication of players with a wide range of social standards
- The notion of « transition » implies significant social and cultural disruptions, requiring a long term perspective

### Environment

Managing environmental externalities to preserve license to operate and anticipate regulations

Climate change is a game changer in energy investments

Land contamination focuses attention because of impact on human health and remediation costs

Sustainability of supply chain for energy intensive industries and for buildings

### Social, Ethics and Governance

Diversity in the workplace is a clear signal to a company’s insertion in its local environment

A fair split of value creation amongst stakeholders helps tackle rising inequalities

Transparency of decision making fosters stakeholders engagement

Continuous employee development and training is essential to transitioning industry
Climate Change is a Sustainability issue
How the investment sector will tackle the “S” in ESG is critical

‘Yellow vests’ spark EU debate about just transition to clean energy

By Frédéric Simon | EURACTIV.com

27 nov. 2018
ESG and value creation
The focus on correlation fails to see the bigger picture

### HR practices & firm performance

Core HR practices (recruitment, training, development, compensation, etc.)

- **Strong Correlation** \((0.55 \text{ R}^2)\) with

  **Organizational Commitment** = desire to see company succeed\(^3\)
  - Belief in & acceptance of goals & values
  - Willingness to exert efforts (motivation)
  - Unwillingness to withdraw from target (continuance)

- **Strong Correlation** \((0.42 \text{ R}^2)\) with

  **Increased productivity**

### Safety & firm performance

Occupational safety policies & safety management systems

- **Strong Correlation** \((0.55 \text{ R}^2)\) with

  **Competitiveness**
  - Image & reputation
  - Productivity
  - Capacity to innovate

- **Supplemented by empirical studies on links with financial performance**\(^7\):
  - 17% increase in productivity
  - 9% drop in absenteeism & turnover
  - Impact on insurance and claim costs

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Notes 1, 2, 3, 4, 5, 6 and 7: sources available upon request
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EIF Impact strategy & Impact Measurement

Cleantech Forum Europe
May, 22nd 2019
Supporting Impact companies Across the Value Chain

Social Impact Accelerator (SIA)

- Incubator/Accelerator-linked funds
- Technology Transfer
- Microcredit
- Business Angels

Impact Funds

Payment-by-Results investment schemes

VC Early Stage

Portfolio Guarantees & Credit Enhancement

VC Lower Mid-market & Mezzanine Funds

Public Stock Markets

SME Development Stages

PRE-SEED PHASE  SEED PHASE  START-UP PHASE  EMERGING GROWTH  DEVELOPMENT

HIGHER RISK  LOWER RISK
A deliberate pragmatic definition of “impact”, different from ESG-focused funds, or CSR investing

- Intentionality
- Scalability
- Positive correlation between impact and financial performance
Impact metrics: implementation and reporting

**Input GP:**
- Define at least 1 and up to 5 impact indicators per portfolio company
- 1 unique quantifiable target per indicator
- Define a weighting for each indicator, representing the importance of each impact achieved by the business model

**Role of the Advisory Committee (or equivalent Investors’ Committee):**
- Approves indicators
- Approves targets
- Votes upon request of the GP on:
  - Removing indicator
  - Adding indicator
  - Modification of an indicator
  - Modification of a target

**Reporting**
- Annual reporting
- Consolidation of impact multiples at
  - (i) company level and
  - (ii) portfolio level
First and foremost, this mechanism becomes relevant only when the fund is in the financial carry.

<table>
<thead>
<tr>
<th>Portfolio social impact multiple below 0.6</th>
<th>Portfolio social impact multiple between 0.6 and 0.8</th>
<th>Portfolio social impact multiple higher than 0.8</th>
</tr>
</thead>
<tbody>
<tr>
<td>No carry is distributed to the predefined carry recipients.</td>
<td>Between 50% and 100% of the carry is distributed to the predefined carry recipients.</td>
<td>100% of the carry is distributed to the predefined carry recipients</td>
</tr>
<tr>
<td>Carry is donated to a third party foundation/NGO/social enterprise proposed by the team and approved by the Investors’ Committee</td>
<td>The non-distributed part is donated to a third party foundation/NGO/social enterprise proposed by the GP and approved by the Advisory Committee</td>
<td></td>
</tr>
</tbody>
</table>

Portfolio Impact Multiple and Carry distribution
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SET’S IMPACT AND ESG INTEGRATION AND REPORTING
We invest in European early growth-stage companies that impact the future of the global energy system.

We are the only European financial VC purely focused on the Energy System Transition.
IN SHORT

**ESG** – how to build a good and successful company, Internally focused

**Impact** – How to measure the external impact that a company has, we look at Direct Impact only
ESG PRINCIPALS

- SET has long been a leader in ESG in the Venture Capital Community and actively promotes good ESG practice in the industry. We aim to continue to be best in class in ESG performance and implementation.

- We expect all companies we finance to:
  - Impact the energy transition
  - Provide substantive, positive, measurable impact on the environment
  - Compliance with all laws and conventions
  - Provide a positive working environment
  - Constantly report and improve on their own ESG in a transparent manner
  - Engage with customers and suppliers to improve their own ESG systems
  - Apply high ethical standards

We apply these principals to the way we operate and include this as part of our investment process.
WHY IMPLEMENT STRONG ESG POLICIES?

We believe that **ESG excellence** is key to **building successful companies** that can scale, create value and good economic returns to our investors.

Companies that focus on ESG performance are **actively managing** their **internal risks**.
PRACTICAL IMPLEMENTATION AT COMPANIES

We believe a pragmatic approach to ESG implementation at companies

- Talk with management teams – conversations change from “Why should I do this?” to “We should do this to help our business grow.”
- Highlight the key issue areas and work on them – before bringing up more
- Integrate into the company process, identify – assess – improve
- Make things easy for the company – make your required reporting easy
IMPACT

We look at the direct impact that our portfolio companies have - primarily on the benefits to their customers.

Our investment focus means that every portfolio company has an impact on the Energy System Transition.

In practice this means measurable impacts on Energy and CO₂ Emissions.
We believe in a practical approach to impact reporting

We define 1-5 non financial KPIs with the company to derive the impact performance of the company.

We create reasonable targets, calculated using the KPIs, during the investment process.

We report and review the progress annually of each company and the total fund performance.

Any impact metric requiring more than 4 calculation steps is not a sensible metric to use.
WHY IS THIS IMPORTANT TO SET?

We believe in the need to change the way we create value for future generations

Next to financial performance targets we define **impact targets** per individual investment and **link our remuneration** to this performance

This is done in such a way as to not change the financial distribution to the LPs – which is purely based on the fund financial performance and hurdle

50% of the fund manager’s carry is linked to the impact performance of the portfolio

Any carry amount that will not go to the fund manager because environmental impact return has been missed, will be donated to a cause selected by fund manager and accepted by the LPs
INTEGRATION IN TO INVESTMENT PROCESS

Investment process:
- Intake Submission
- Basic Screen
- Further Analysis
- Term Sheet
- Due Diligence
- Inv. Proposal
- Finalize deal

ESG integration:
- Sustainable energy Screening
- ESG Risk Identification
- Management team discussion
- ESG Due Diligence
- ESG mitigation discussion
- Finalize deal

ESG documentation:
- Share ESG principals
- Investment Proposal
- Action Plan
- Shareholder agreement

Impact integration:
- Share Impact Objectives
- Impact KPIs in
- Investment Proposal
- Reporting discussions
- Non financial KPI company reporting
FOR FURTHER INFORMATION:

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Mission Innovation and the 1.5 °C Compatible Solution Framework

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Dennis Pamlin, Lead, Mission Innovation, 1.5 °C Compatible Solution Framework

Accelerate
Reframe
Reprioritize
Financial Sector
Solution Providers
Users of Solutions
Framework for Assessing Avoided Emissions

The Framework is supporting an accelerated uptake of disruptive solutions by supporting increased transparency regarding actual and potential greenhouse gas reductions, making it easier to identify, support and invest in the next generation of solution providers.

Find out more
1. Three-steps towards a solution/innovation agenda

From only:
1. Risk
2. Divestment
To also:
1. Opportunity
2. Impact in society
2. Quantify Avoided Emissions

\[
\sum \left( \begin{array}{c}
\text{Probability of success} \\
\times
\end{array} \right) \times \begin{array}{c}
\text{Probability of adoption} \\
\times
\end{array} \times \begin{array}{c}
\text{Volumes} \\
\times
\end{array} \begin{array}{c}
\text{Carbon Abatement Factor} \\
\end{array} = \begin{array}{c}
\text{Total Carbon Abatement} \\
\pm
\end{array}
\]

\[
\sum \left( \begin{array}{c}
\text{Volumes} \\
\times
\end{array} \begin{array}{c}
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\end{array} = \begin{array}{c}
\text{Total Carbon Abatement} \\
\end{array}
\right)
\]

BAU baseline
Net avoided emissions
3. IPCC based 1.5°C Compatibility Mapping
Shifting the global conversation, focus and action

We will bring >100 solutions with > 2 Gigaton of reduction potential by 2030 to Mission Innovations 4th Ministerial meeting.

We want to support and collaborate with leading stakeholders who can help
1. Gather >1000 solution providers with > 40 Gigaton of reduction potential by 2030.
2. Explore how accelerated uptake and investment in such solitons can be 1.5C compatible

We will launch this at COP25 with an investor challenge for MI5. Please join us https://www.misolutionframework.net/
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