Managing and Measuring Impact in Social Infrastructure

FRANKLIN TEMPLETON INVESTMENTS



JOHN G. LEVY, CFA, CAIA, Director of Impact

RAYMOND J. JACOBS, Managing Director

RICCARDO ABELLO, Senior Vice President

Franklin Real Asset Advisors

Investing in social infrastructure in Europe can lead to positive impact-based outcomes for communities and the environment. By bringing impact-focused private capital to the social infrastructure space, the community and environmental performance of these assets can be markedly improved. Our Real Assets team proposes a three-step framework that allow not just measurement, but management of impact from social infrastructures.

SOCIAL INFRASTRUCTURE DEFINED

Social infrastructure is defined as the physical assets that facilitate social services. Examples include healthcare and education facilities, social and affordable housing, and buildings related to justice, emergency and civic services. One recently published report by the European Long-Term Investors Association (ELTI) highlights the importance of social infrastructure: "High-quality social infrastructure provides benefits to individuals and communities and improves social cohesion..."[1]

IMPACT IN SOCIAL INFRASTRUCTURE

Impact investing is investing with the explicit intention to generate financial returns alongside measureable and positive social and environmental impact. It can be thought of as investing with a dual-return approach: impact return is targeted in addition to an at-least market-rate financial return. Not all impact investments seek market-rate returns, but for the sake of our approach to impact measurement we will only be referring to those that do.

Impact investing is a natural strategy to pursue within social infrastructure. In many instances, there is a natural alignment between impact return and financial return, as each can reinforce the other. Renovations that improve the utility of the space for tenants and visitors can both improve the quality of services and increase the value of the asset. Investing in social infrastructure with a focus on impact can not only yield market-rate returns, it can also create financial resiliency that improves financial results.

THE OPPORTUNITY FOR IMPACT

We believe that investors and managers should frame the impact opportunity into three main buckets: challenges, contributions and impact.

CHALLENGE

The core societal challenge we seek to address

CONTRIBUTION

The value-add of investors & managers in addressing the challenge and achieving impact

IMPACT

The social and environmental outcomes that result from investments

Challenges

Our approach begins with identifying the challenges that we are seeking to address. We believe it is important for investors to align these challenges with the United Nation's Sustainable Development Goals (SDGs). For that reason we've identified those SDGs goals that can be directly addressed through investments in Social Infrastructure, including health, education, sustainable cities and communities and climate. Let's take goal 13 "Climate Action" as an example.

Source: United Nations, Sustainable Development Goals (SDG). For illustrative purposes

Parties to the UN Climate Change Conference in Paris in 2015 agreed to target keeping global average temperatures from rising 2°C from pre-industrial revolution levels. **The battle against climate change is being waged not only in the fields of manufacturing and transportation, but also in real estate.** In fact, by many measures, buildings use more energy than either industry or transportation and will contribute more to CO_2 emissions between now and 2030. (See exhibit 1)

Our climate change challenge is that buildings today are contributing to a 2°C rise in global temperatures.

Investor & Manager Contributions

Once we have identified the challenges, we look to the ways we can contribute to solutions. Our Real Assets team has developed a set of five categories that describe the ways we contribute to and create positive impacts. Let's focus on one of this categories: Environmental Upgrades.

We can create positive environmental impact through actions that reduce pollution, reduce net water and material use, and support biodiversity and clean transportation. Examples of upgrades could include installing energy efficient systems, creating more green space, improving recycling and waste disposal polices.

By ensuring that each of our investments includes one or more of the established contribution categories, we can more confidently speak to how investments lead to positive community and environmental outcomes.

Exhibit 1. The Real Estate Sector (as a % of total)

Global energy use	40%
Global greenhouse gas emissions	20%
Global usage of raw materials	40%
Total waste generated in the EU	30%

Source: "Environmental Sustainability Principles for the Real Estate Industry" World Economic Forum, World Economic Forum Industry Agenda Council on the Future of Real Estate & Urbanisation, January 2016

Impact

Our approach is grounded on one principle: impact should not simply be measured, it should be managed.

By identifying and addressing challenges, we can increase access to quality social infrastructures with enhanced resource efficiency and conservation. These positive outcomes require fully integrated impact management into our entire investment process.

Impact Management

We integrate impact into each stage of the investment process through proprietary tools and frameworks that ensure continued prioritisation and reassessment of our impact objectives. By integrating impact we, as managers, and also investors can form a more holistic process that aligns investment and impact considerations at every step.

Throughout our Impact management process we stress the terms "authenticity" and "transparency" to acknowledge that with a dual-return objective, we will not be able to pursue all possible avenues of impact, since some may not be economically viable. To this end, we created an **internal impact rating system** that measures the current and projected state of each asset's community and environmental performance. This system allows us to speak authentically to each investment's impact thesis, whether it be to buy and lease-back already high performing assets, or to significantly improve the performance of old or underutilised buildings.

FOOTNOTES

1 Source: Boosting Investment in Social Infrastructure in Europe. Report of the High-Level Task Force on Investing in Social Infrastructure in Europe. Lieve Fransen, Gino del Bufalo and Edoardo Reviglio. January 2018.