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Impact Investing: an Overview

Maria Pinelli, Giuseppe Torluccio

Abstract

Impact Investing is a very promising phenomenon which is gaining always more popularity and importance, drawing the attention of both academics and practitioners. This practice was crucial in the recovery process after the 2008 financial crisis, and it has all the potential to be considered as a critical element to respond to the emergency situation generated by Covid-19 pandemic.
However, since a lot of organisations and investors are now approaching the industry, this risks to incur the "impact washing" phenomenon. In order to avoid this threat, it is important to define the specific characteristics of impact investing, distinguishing it from other forms of sustainable finance, and this is the primary objective of this paper.
Subsequently, this work describes in detail the impact investing ecosystem, composed of supply-side, demand-side, intermediaries and the enabling environment, in order to provide a complete view of the phenomenon. Finally, the main challenges of impact investing are identified, in order to direct the attention of research to them, enabling the phenomenon not to lose its transformative potential.

JEL classification: G21, F61, B55
Keywords: Impact Finance, Social Bond, Financing, Sustainable finance

"The world is on the brink of a revolution in how we solve society's toughest problems. The force capable of driving this revolution is 'social impact investing,' which harnesses entrepreneurship, innovation and capital to power social improvement."

(Impact Investment: The Invisible Heart of Markets,
Social Impact Investment Taskforce, 2014)

University of Bologna; Department of Management - Yunus Social Business Centre - Via Capo di Lucca, 34, 40126 Bologna. E.mail: maria.pinelli@studio.unibo.it; giuseppe.torluccio@unibo.it

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Context

It is universally known that, when there are times of economic and social crisis, there is ground for social and economic revolutions.

At present the world is suffering from the Covid-19 pandemic; as denoted by Roubani (2020), the global economy is going to incur a harder collapse than the one of 2008 financial crisis. However, what could provide a bit of comfort is that human history is characterized by several critical periods, each of them followed by important transformations.

Taking as a reference the financial crisis that arose in 2008 and persisted during these years, economic depression led public judgement to distrust the traditional way of doing business and allocating capital.

Introduction

It was in this context that a contemporarily financial and social revolution took place. In fact, a new approach to financing grew and gained major importance: Impact Investing.

This phenomenon was operational also before, but only in this period it received this name, mostly due to the fact that, as illustrated by Benedikter and Giordano (2011), investors, fostering a great discourage towards the traditional financial practices, began to be involved in socially related projects.

This term was officially used for the first time in 2007 in the meeting of the Rockefeller Foundation at the Italian Bellagio Center dedicated to developmental finance.

Impact investments are defined by the Global Impact Investing Network (GIIN) as "made into companies, organizations, and funds with the intention to generate measurable social and environmental impact alongside a financial return." (GIIN, 2014) To be of extraordinary importance in this sentence is the word "***intention***" to produce both social or environmental benefit and economic return. This was a shocking news for the time: the financial world, which has always been so concentrated only in the maximization of profits, was beginning to nourish an interest for themes associated with the third sector.

After a decade, as indicated by the respondents of the 2020 GIIN survey, the magnitude of the impact investment market corresponds to USD 715 billions. As it results evident, this practice has grown and gained success, but it is important to understand what can be really considered as impact. In fact, along the years, another phenomenon started to take shape; the so-called "impact washing". As explained in their work, Busch and colleagues (2021) define impact washing as the "dilution" of the term impact investing, where the term impact is used as a promotional word to obtain capital, without

the intention to solve social or environmental problems. The authors distinguish between three eras of Sustainable Finance. At the beginning, Sustainable Finance was guided by moral motives and the objective of avoiding unethical attitudes. Then, it became a tool used to regulate financial risks, arriving to be a mainstream practice. Now, with these numbers at hand, the urgent question is: which investments can be defined as impact and which can not?
In order to understand this, it is important to define in an univocal manner what an impact investment is, since, after so many years, there is still terminological and conceptual confusion about this practice.

Objective

The whole world is living in a crisis situation, probably stronger than any other in history. The financial world is struggling, governments are showing their dysfunctions, and social inequality is incredibly highlighted, more than in other periods. Additionally, the phenomenon of digitalization has influenced the entire world in the last decade, and enterprises have undergone strong structural changes. During this pandemic year, digitalization has inevitably become a prerequisite for all to keep up with the rest of society. This phenomenon clearly intensifies the already present problem of social inequality. Alongside these problems that have been intensified by the pandemic, the constant emergency of climate change is becoming more and more urgent. It is not a case that the Italian recovery plan allocates €57 billions to green investments and €42 billions to digital ones.
In a situation like this, it is probably more urgent than after the 2008 financial crisis the presence of impact investments, that embed in their nature the great objective of an inclusive economy.
Governments' actions are fundamental, but, as depicted by Andrikopolous (2020), social finance, intended as impact investing, originates to solve market failures and, logically, to government policies intended at managing social challenges.
The great challenge of impact investing, in this new era, is to distinguish itself from all the other forms of investment that, to obtain popularity, claim to be sustainable and impactful.
This article has the objective to clarify, through a review of the existing literature, what are the main differences between impact investing and other forms of sustainable finance that are often associated with it, to define what can be included in this term. Then, it will proceed illustrating the impact investing ecosystem, composed by which are the suppliers of impact capital and its recipients, intermediaries and the enabling environment. Finally, the main challenges of this approach will be delineated. In this way, having a clearer definition of what is impact investing and its peculiar characteristics, this paper can contribute to the studies in this field, which appears to be still under-investigated.

1.Definitional problem

In this paragraph there will be an analysis of the several practices that have been associated with Impact Investing over the years, in order to clarify its boundaries.

1.1. Social finance

The term that is mostly used indifferently with impact investing is social finance. According to many authors, the two terms can be used to indicate the same process. In the review of Agrawal and Hockerts (2019), the authors found out that the term "social finance" is mostly used by UK and European researchers, while North American ones adopt the term "impact investing", and declare to use them ad synonyms. Andrikopolous, in his review of 2020, states that social finance evaluates the viability of impact investments, conceiving, once more, the two terms as equivalent ones. In "The architecture of Social Finance" by Rexhepi (2016), instead, social finance comprises all the forms of organizations that, besides generating profit to sustain themselves, deal with social or environmental challenges, following, in doing so, the triple-bottom-line (economic, environmental and social objectives). In line with their conception, therefore, impact investing is incorporated in the big umbrella of social finance, that has the purpose to contemporarily create social and financial returns.

1.2. Microfinance

Microfinance is a practice which has been regulated for the first time in 1967, thanks to the actions of Muhammad Yunus, who founded the Grameen Bank in Bangladesh, aiming at providing small loans to poor people excluded by standard operations, without requiring guarantees. Grameen Bank is still the most powerful microfinance organization: total borrowers are 8.93 mln, 97% of which are women and 1.2% are beggars[1].

Yunus, as an economic man, recognized a dysfunction in the economic and social policies and built a new and very effective way to include poor people, believing in their capacity, as it is clear from his words: *"I believe that we can create a poverty-free world because poverty is not created by poor people. It has been created and sustained by the economic and social systems that we have designed for ourselves; the institutions and concepts that make up that system; the policies that we pursue."*

This form of credit became very popular also in Europe, with the formation of banks with the formalized aim of delivering credits to those who are excluded by standardized transactions.

[1] www.grameenbank.com

A great example of microcredit in Italy is the one of PerMicro, born in Turin in 2007; now it counts 17 offices spread across Italy. From its birth, PerMicro supplied 29.329 credits with a value of €220 mln.

To have a global vision of this phenomenon, according to the statistics of Convergences (2019)[2], in 2018, 139.9 million borrowers received the services of microfinance institutions, taking advantage by them, compared to 98 million in 2009. Of the total 139.9 million borrowers, 80% are women and 65% are rural borrowers; the curious part of this story is that these percentages have been the same throughout the past ten years, accompanied by a positive increase in the number of borrowers. The approximate credit portfolio is, following this study, of $124.1 billion in 2018, with good previsions for the future.

Microcredit is, without any doubt, a powerful tool of social finance, but, differently from impact investing, which uses mainly equity-based instruments, it is based on credit, and it is characterised by higher interest rates with respect to debt-based impact investments, as denoted by Agrawal and Hockerts (2019). The authors also express, as the main differences between them, the fact that the amount of capital invested by impact investors is higher than the micro-loans, and that the relationship between investors and investees is much deeper with respect to the one established with micro-lenders. Finally, impact investors can be considered as investors to microfinance institutions.

1.3. Social Impact Bonds

Social Impact Bonds are an example of public-private-partnerships (PPP) instrument. As explained by Andrikopolous (2020), they are loan arrangements in which who provides the capital, which most of the time is the government, will receive the money depending on the effectiveness of the investment. They are established to solve a social problem: the debt capital is handled by an independent organization receiving the money by the government. This organization manages the firms that have the objective to deliver activities aimed at reducing the predetermined social problem. These instruments are pay-for-success models because they are based on a strong measurement of the created impact. In fact, an independent organization is involved to assess if the expected social impact has been reached. On the basis of this, it decides the amount of money that will be received by the initial creditor; the obtained social impact is directly connected to a reduction of government expenses in the resolution of that specific social problem.

[2] https://www.convergences.org/en/119115/#:~:text=In%202018%2C%20139.9%20million%20borrowers,in%20the%20number%20of%20borrowers.

Staying at the numbers, the social impact bonds that can be counted nowadays are roughly 100 worldwide, 40 in the UK and 20 in the USA[3].
The author depicts that the main challenge of these pay-for-success instruments is the difficulty of measuring the social impact delivered; on the other hand, this allows an increase in the transparency in the creation of public goods.
In 2015, the Yunus Social Business presented, together with the Rockefeller Foundation, another pay-for-success instrument, the Social Success Note, defining it as a "blended finance tool for social impact". The concept of blended finance, as illustrated in the SSN Playbook (2020), foresees the employment of public or philanthropic money in projects which have a social or environmental goal and an opportunity to receive economic returns near to market ones.
In the SSN Playbook (2020), the functioning of the Social Success Notes is explained, shading light also on the main differences with Social Impact Bonds.
The objective of Social Success Notes is to enlarge the provision of money for those companies with the aim of producing social change. An investor provides a debt to a social enterprise which demonstrates in a quantifiable way to generate social impact. Once the social enterprise is able to reach the desired social impact, a "philanthropic outcome payer" provides the initial investor with a supplementary incentive, securing in this way an ambitious risk-adjusted rate of return. This philanthropic payer can also provide the social enterprise with an incentive. With respect to social impact bonds, in the Social Success Notes the social enterprises play the key role of repaying the initial loan, and the outcome payer just gives the investor an incentive. In the social impact bond, instead, the outcome payer repays the loan and also the incentives, leaving the social enterprise only the responsibility to deliver the activities and reach the desired social impact.
In this way, it becomes clear how social impact bonds are more suitable for non-profit organisations which cannot repay the debt, while social success notes can be a support for for-profit businesses.

1.4. Socially responsible investments

Since these investments are defined as "socially responsible", they can be confused with impact investing. However, they are positioned almost on the opposite side with respect to this practice. In fact, they comprehend securities of companies that distinguish themselves for the conscientious way in which they produce goods and services. In other words, as denoted by Agrawal and Hockerts (2019), they make investments in organizations that employ ESG procedures, meaning the use of environmental, social and governance reflections in the evaluation of an investment.

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[3] https://www.instiglio.otg/en/sibs-worldwide/.

As denoted by Andrikopolous (2020), they depart from the idea of maximizing value for the shareholders, since they include the possible negative externalities deriving from financial operations. However, as explained by Martin (2016), their objective is to prevent social or environmental damage, so to eliminate the possibility of creating harmful effects or results. In this way, socially responsible investing foresees a negative selection of investments, in the sense that certain industries, like gambling, alcoholic, petroleum and pornography are deliberately excluded by the range of sectors in which investing. The difference with impact investing stays here: as seen before, impact investments are characterised by the intention to generate a positive impact on the society or the environment and doing this they address returns that go from below to market rate, as expressed by the GIIN[4]. Differently from other forms of social finance, impact investing intentionally focuses on enterprises with the dual objectives of generating impact while contemporaneously being economically sustainable (J.P. Morgan and Rockefeller Foundation, 2010). Socially responsible investments, instead, are aimed at mitigating the possible adverse outcomes of their actions while boosting the profit.

A strategy which is connected to Socially Responsible Investments, and still very different from Impact Investing is Corporate Social Responsibility, globally known as ***CSR***. In the last years there has been the general recognition of the fact that organisations negatively affect the environment and the ecosystem, as denoted by Olanipekun and colleagues (2020). This, joined with the expansion of sustainability issues and actions, has brought about the necessity for companies to adopt corporate social responsibility processes. In this way, business can develop projects for the benefit of society and, on the other side, decrease possible damaging consequences. CSR activities usually take shape in altruistic activities or environmental and human rights responsibility projects[5].

1.5. Venture philanthropy

As it has been explained since now, impact investing is strictly connected with ethical and moral concepts. For this reason it is clear how it can be connected, and surely also confused, with philanthropy. A practice that, as it can be intended by the name, stays in the middle between Traditional Philanthropy and Traditional Venture Capital is Venture Philanthropy. This phenomenon arose in the USA at the end of 1980's and now it has become a global phenomenon, as explained by Andrikopolous (2020). As denoted by Phillips et al. (2010), the way in which third sector entities are funded has transformed a lot throughout time. In fact, in the study of Corry (2010) it is clarified that, at the beginning, they received financial aid mainly through grants and donations, included in the

[4] https://thegiin.org/impact-investing/need-to-know/
[5] https://corporatefinanceinstitute.com/resources/knowledge/other/corporate-social-responsibility-csr/

model of Traditional Philanthropy. This kind of philanthropy is based on the idea of the "gift" with the objective of removing the fundamental causes of social challenges and to improve the life of disadvantaged people (Anheier, 2001).
Then, it became urgent to introduce a new, more structured model starting from Traditional Philanthropy with features of Venture Capital. As explicated in the study of Mair and Hehenberger (2014), Venture Philanthropy, in fact, involves direct interventions in the direction of enterprises in which investments are made also in order to increase their effectiveness. On the contrary, traditional Philanthropy is based on the grant-making approach, which does not foresee a concrete engagement with enterprises. Traditional Venture Capital deals are based on the measurement of outcomes, and the research of Andrikopolous (2020) shows that the main criticality about the Venture Philanthropy approach is the measurement of the obtained results. It results evident that this approach is very similar to Impact Investing, since, as it emerges also by the study of Agrawal and Hockerts (2019), both Venture Philanthropy and Impact investors concentrate on the maximization of social impact and its measurement, and are strongly involved with their investees. The main difference between Venture Philanthropy and Impact Investing is the fact that the first aims at the expansion of the social return on investments, without taking into great consideration the economic one, while Impact Investing insists on the dual return.

At this point, the main differences between different streams of what is defined social/sustainable finance and impact investing should result fairly clear.
During the years, many definitions of Impact Investing have been proposed, showing that the concept of **intentionality** have gained always more importance, together with the **creation of contemporaneous financial and social return**.
Hereafter some definitions will be listed in a chronological order, to evidence this evolution:

- *"[Impact investing] helps to address the social or environmental problems while generating financial returns."* (Bugg-Levine and Goldstein, 2009)
- *"Impact investing is a sub-set of responsible investing. Here the investor intentionally invests to achieve positive social and environmental impact in addition to financial return."*(Hebb, 2013)
- *"Impact investing refers to the use of investment capital to help solve social or environmental problems around the world with the expectation of financial returns. Unlike ethical investing or socially responsible investing (SRI), which focuses on the negative screening of alcohol, tobacco, and firearms, and a range of businesses and activities which do not damage society, impact investing is positioned as taking a proactive approach actively identifying businesses*

with the intent to achieve a financial return and create a positive social or environmental impact." (Quinn and Munir, 2017)

- *"Impact investors intentionally contribute to positive social and environmental impact alongside a financial return; use evidence and impact data in investment design; manage impact performance; contribute to the growth of impact investing".* (GIIN, 2019)

With a general vision of the definitions that were given in time regarding impact investing, it is possible to resume its main three characteristics that researchers have used to delineate the phenomenon, forming the so-called *impact triad*. They are summarized in the study of Vecchi and colleagues (2015):

- Intentionality, meaning the *ex-ante* declaration of the proactive search for entities which have the primary objective to generate social or environmental value;
- Measurability: the social outcomes must be declared *ex ante* the employment of capital and measured *ex post* to understand how they have been appropriately and successfully reached (OECD, 2019);
- Additionality, which coincides with the desire of investors to address undercapitalized areas, meaning the ones that are not taken into consideration by traditional investors (Achleitner et al., 2013).

2.Impact Investing Ecosystem

The Impact Investing Ecosystem is formed by a variety of components, which can be divided in four groups, as identified by Mackeciviuté (2020): supply-side, demand-side, intermediaries and the enabling environment.

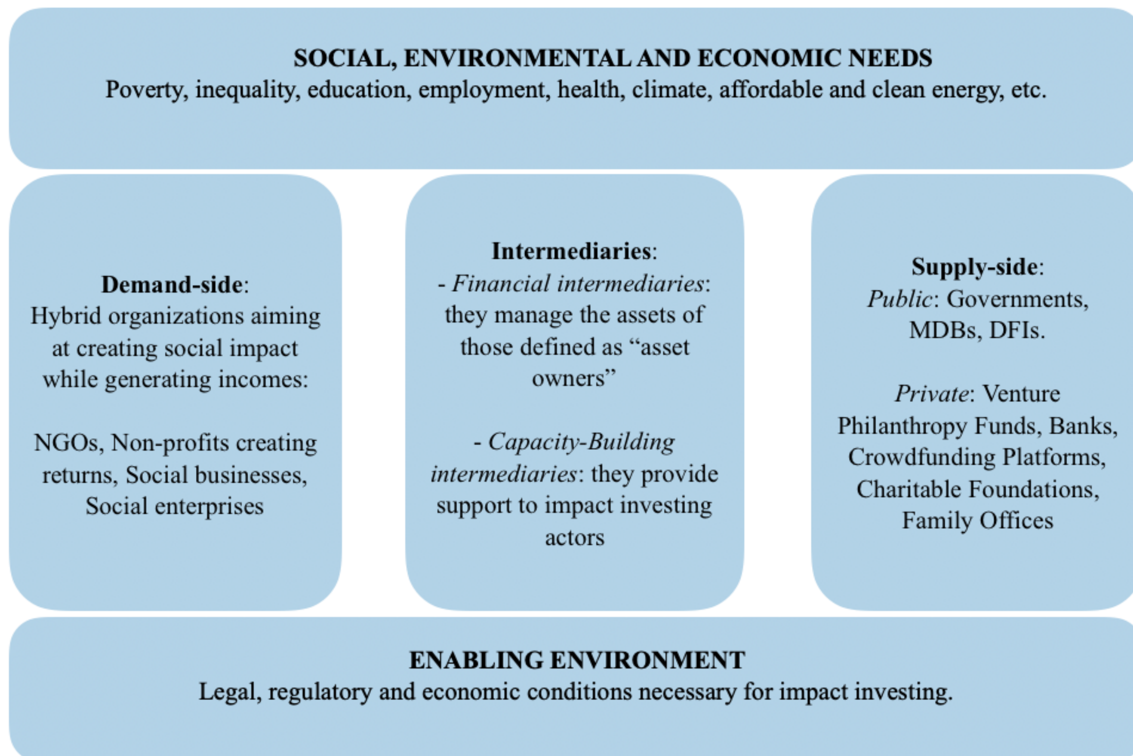

Fig.1: The Impact Investing Ecosystem
Adapted from "The Impact Imperative for Sustainable Development" (OECD, 2019)

2.1. Demand-side

It comprehends all the organisations which are in need of capital in order to create social impact while being financially sustainable.

As it has already been noted, the way in which third sector entities receive funding has been significantly changed.

In fact, as reported by Corry (2010), NGOs have existed for a long time; the oldest is Save The Children, created in 1919. Traditionally they have been supported mainly through donations and grants. Starting from the financial crisis of 2008, however, many governments have not been able to facilitate the access to money for these realities. From these failures, the social entrepreneurship sector had the possibility to grow and gain the interest of governments, bringing to transformations in the social investment sector (Nicholls and Schwartz, 2014).

Social entrepreneurs have as their primary aim the creation of social impact, while preserving a financially viable business model, resulting in this way as “hybrid” entrepreneurs (Douglas and Prentice, 2019).
They differ a lot from traditional businesses; as Gupta and colleagues (2020) assert, it is true that every form of entrepreneurship can have a social task. What differentiates social enterprises by them, indeed, is the fact that the generation of social impact is their principal objective, while conventional firms have their personal profit as a priority.

This innovative manner of doing business required the creation of a lot of new legal forms for hybrid organisations, contributing to structure the demand-side in a better way. However, the study of Main (2020) sheds light on the fact that legal form is not a determining characteristic of social enterprises, since there are a lot of various forms which depend also on the beneficiaries’ capacity to pay and the firm’s possibility to attract funds.
The report of the European Commission (2020) draws a large review about the state of art of social enterprises in Europe. It accounts that sixteen countries have a precise legislation for social enterprises. In particular, the UK government was the first in creating a new legal form ad hoc for social enterprises, the Community Interest Company, deriving from the for-profit company status. They must aim for a social impact by implementing any types of activity with limits on gains distribution. Finally, they must annually communicate the way in which the social purpose has been accomplished. Instead, in four countries comprising Italy, the new legislative model for social enterprises was established starting from the model of cooperatives. In Italy there are two types of cooperatives: type “A” deals with social, health and instruction services, while type “B” with all the other sectors. Social enterprises in Italy have the duty to merge business activity in specific sectors, with the aim of reaching a social impact; beneficiaries and workers are involved in their processes and decisions. Concerning the management of earnings, they cannot distribute them; returns must be used to strengthen the firm’s capital or to boost its activity.
Considering USA, instead, they rely mainly on Low Profit Limited Liability Company (L3C) and Benefit Corporations, which have become popular also in Europe.

Regarding these types of firms, they have to manage relationships with many different stakeholders, having as the main focus their beneficiaries, intending the people who suffer from the societal problems that enterprises aim to address. The study of Mair (2020), dedicated to social entrepreneurship, demonstrates that typically social enterprises do not limit their activities to a singular beneficiary group, rather to many of them contemporaneously. Often it happens that

beneficiaries are directly involved in the development of enterprises' products and services. In this way, they can benefit from the delivered activities while, at the same time, being included in their creation, having the possibility to feel doubly satisfied. This is a clear evidence of the fact that impact investing has the intention to go towards an inclusive economy. In fact, beneficiaries are usually the disadvantaged parts of the society (youth, people with disabilities, women, ancients, migrants, eccetera) that, through an engagement in business activities, contribute to the community.

In literature there is still confusion also about the terms "social enterprise" and "social entrepreneurship". In particular, the phrase "social enterprise" is often used interchangeably with the term "**social business**" by researchers and practitioners. The name "social business" was introduced by Muhammad Yunus, with these 7 precise characteristics:

1. **Business objective will be to overcome poverty**, or one or more problems (such as education, health, technology access, and environment) which threaten people and society; not profit maximization.
2. Financial and **economic sustainability**;
3. Investors get back their investment amount only. **No dividend is given beyond investment money**;
4. When investment amount is paid back, company profit stays with the company for expansion and improvement;
5. **Gender** sensitive and **environmentally** conscious;
6. Workforce gets market wage with **better working conditions**;
7. Do it with **joy**.

In this way, social business has the only objective to find a solution to social or environmental challenges, and the distribution of dividends is not foreseen.

A demonstration of the fact that social entrepreneurship is gaining a lot of attention is, among others, the fact that a company like Ericsson, leader in the ICT sector, has dedicated one report to delineating the main characteristics of social businesses.

In this report, the term is used as a synonym of "social enterprise", as it can be noted by this sentence: *"(...) Social businesses, also known as social enterprises, have emerged and developed in a networked society. Unlike traditional businesses, these companies are driven by a social cause, putting social impact before profit to create a sustainable business model for the greater good."*[6]

[6] https://www.ericsson.com/en/reports-and-papers/networked-society-insights/social-business

The company makes a great distinction between traditional businesses and social businesses, which is summarized with this figure:

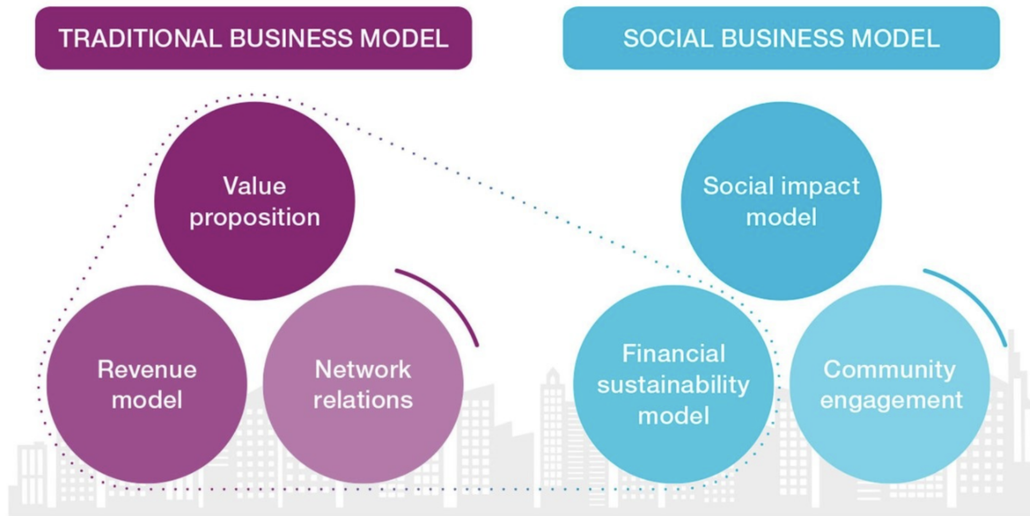

Fig.2: Traditional business model Vs Social business model

Source:https://www.ericsson.com/49eb4c/assets/local/reports-papers/networked-society-insights/doc/social-business-report.pdf#page=7%5D

Describing the social business model in this manner, it is evident that it is conceived as a social enterprise as described before.

The main differences with respect to a traditional business model are:

- The social impact model: differently from traditional businesses, which explain the benefit they create for their customers through the description of their products and services, social businesses describe the value they are able to generate through the expected social impact of their actions;
- The financial sustainability model: while the traditional revenue model aims to maximize profit, the financial sustainability model seeks to produce a sufficient amount of revenues to simultaneously achieve the social impact and be economically viable.
- The community engagement expresses the concept that social businesses are correlated to all the actors that are influenced by their initiatives, while traditional businesses are independent and the relationships they create are all in the direction of boosting their revenues.

On the other hand, there are companies like ClearlySo, an online social market with the objective to support social businesses and social enterprises in increasing their investments, which make a distinction between the two terms. Social businesses are conceived as firms with two objectives, the commercial one and the social, environmental and ethical one. Diversely, social enterprises are economically sustainable organizations with a primary focus on producing a social impact, and so they address the majority of their profits to its creation.

At the end, a clear distinction between the two expressions can be found in the writings of Muhammad Yunus. In fact, in January 2020 he declared that in too many cases they are used indifferently, and it could be dangerous for these approaches.
As it is clear by the 7 properties of a social business, for the author its main aim is to fix a social or environmental failure in which the only dividends that could be distributed are those that allow to recuperate the initial investment. Social entrepreneurship and social enterprises instead, are seen by Yunus as larger concepts; they could be charities or for-profit activities with both commercial and social aims. They could be also individual actions aimed at fixing social or environmental problems. The concept of social business, with this perspective, falls into the broad definition of social entrepreneurship.

This paper, when talking about social enterprises, does not take the perspective proposed by Muhammad Yunus. In fact, as previously seen, social enterprises are conceived as hybrid entities with the main objective of creating social impact while being financially sustainable.

2.2. Supply-side

The supply-side of impact investing comprises different actors who provide capital to organisations aiming at reaching a social impact.
As declared by the report of IFISE (2019), access to economic resources is a crucial problem for social enterprises, since they embed a risk that is higher with respect to the one that traditional investors are willing to take.
Impact investors must, indeed, be ready to bear a high risk with the consciousness that they are creating an impact greater than the initial effort.

Following the article of Spiess-Knafl & Jansen (2013) which enlists the principal capital providers, they are:

- ***Venture Philanthropy Funds***: as seen before, Venture Philanthropy puts together elements of Traditional Philanthropy and Venture Capital. In this way, it is straightforward to understand that these types of funds employ approaches originating from Venture Capital with the objective to provide capital to social enterprises. The EVPA (European Venture Philanthropy Association) defines venture philanthropy as a "*high-engagement and long-term approach whereby an investor for impact supports a social purpose organisation to help it maximise its social impact.*" Investors for impact are conceived as grant-makers or investors willing to take risks that mainstream investors would not be ready to take in order to finance

social enterprises. This high-engagement relationship reflects in a financial and non-financial aid, capacity-building and in performance assessment.

An example of venture philanthropy fund are the Yunus Social Business funds that support social businesses in East Africa, Latin America and India. They utilise the donations they receive into patient and long-term investments in social businesses, together with a direct assistance in the management of their activities.

- ***Banks***: European banks involved with social enterprises are divided into two types. On the one hand there is the Global Alliance of Banking on Values (GABV), including banks giving loans to firms matching their statement of purpose. The number of people who are attracted by these types of banks has been increasing throughout time and for this reason these banks are growing a lot. On the other hand, there are banks with a *charitable agenda* that fall within the social capital market.

- ***Crowdfunding platforms***: they are an attractive financial option for social enterprises, and could be equity-based, lending-based, reward-based or donation-based. They are really useful for social enterprises also considering the fact that when they are in their initial stages they do not have a credit history and so they could not receive attention by traditional capital providers, as denoted by Andrikopolous (2020). Since they work as social networks, they help social enterprises to improve their performance. However, some criticalities can be noted: the study of Bolton and Niehaus (2018) underlines that, most of all, the amount of invested capital is limited while the risk that these investments bring along is quite large.

- ***Charitable Foundations***: they invest their consistent properties in the market and employ the dividends in the social impact activities they want to carry out.

- ***Family offices***: wealthy people are always more interested in investing in social enterprises, and they have the freedom to incorporate social aims in their investing approach.

All these actors can use three types of financing instruments to engage with social enterprises. There is the possibility to use ***donations and grants*** that, as it emerges by the analysis of Andrikopolous (2020), are rarely used for projects that need several years to be carried out. Through the use of donations, the philanthropists fulfil their willingness to generate social impact and the risk is all borne by the social enterprise.

Then, impact investments can be funded through ***bank loans and bonds***, being a favourable choice for social enterprises since they can decrease the part of profit subject to taxes; on the other hand, social enterprises can incur the risk of bankruptcy.

Finally, ***equity*** is an important way of funding for enterprises in general, in fact venture capital is the primary way in which they are financed. Talking about social enterprises, as it has been already reported, the approach is the one of **Venture Philanthropy**. In literature the term Venture Philanthropy is often utilised as a synonym of **Social Venture Capital**. However, here a distinction can be made: in fact, the EVPA clarifies that Venture Philanthropy is the use of capital *for* impact, comprehending also the situations in which social enterprises will never be financially sustainable. Social Venture Capital, instead, is the employment of equity capital in organisations which aim to reach a social impact while managing to be economically independent.
As in traditional Venture Capital, the managers of the investments are generally involved in the ownership and support of organisations for a long time period. In the same way, as traditional venture capital investors require the measurement of the financial performance of firms in which they employ their capital, using it also as an investment criterion, social venture capital ones necessitate, in addition, the measurement of the social performance, which is one of the main challenges of impact investing

2.3. Financial and capacity-building intermediaries

They support the interaction between the supply and the demand side. Talking about financial intermediaries, they are defined by Gutterman (2020) as “asset managers”, since they administer the transactions in order to reach the investment objectives of asset owners. Capacity-building intermediaries, instead, sustain the impact investing ecosystem providing information and useful advice.
These are very important actors mainly for investees; however, what Mackeciviuté (2020) pointes out is that in many cases there is a lack of these figures. Moreover, often social enterprises are not able to pay for their services, and so only privileged ones can benefit from them.

2.4. The enabling environment

The enabling environment is the legal, economic and regulatory conditions in which impact investments can be developed. Since its inception in 2008, impact investing has grown a lot, and also the initiatives actuated by governments. To cite some of the efforts enlisted by the research of

Gutterman (2020), there was the creation of the GIIN in 2019, the willingness of organisations to obtain the certification of Benefit Corporations, the establishment of requisites for financial tools to be defined as “green”, the increase of investments’ reporting in social and environmental terms.

After having described the components of the Impact Investing Ecosystem, it is important to report the main deficiencies that characterize impact investing and prevent its successful development.

3. Main challenges in impact investing

Starting from the problems that concern the enabling environment of impact investing, what the study of Mackeciviuté (2020) and in general researchers in this field recognize is that there is the **lack of a systematized and precise treatment of impact investing**. There are not predetermined rules, regulations and policies. For this reason, there is still a paucity of consciousness and understanding of the impact investing market, tools and advantages.

Furthermore, as it has been already reported, this is connected also to the **absence of an univocal definition of impact investing**. This emphasises the risk that other practices, like Socially Responsible or ESG investments, could be confused with impact investing. The lack of a unique definition renders the effectiveness of impact investing much more labile.

Another action that the governments could do would be to address the provisioning of money towards impact investing initiatives, or to actuate more public-private-partnerships as the ones of social impact bonds or social success notes.

Finally, **normative barriers** connected to the legal status and the characterization of the realities composing the demand side impede the advancement of impact investing ecosystem.

In fact, the definitions given to demand-side realities are really diversified in Europe and, connected to this, some organisations are excluded by the definitions that are given. Moreover, many countries have not defined legislative architectures for demand-side organisations, not aimed at regulating their operations nor their flows of financing.

A strong barrier to the development and the integrity of impact investing is, as it has already been depicted, the **measurement of social impact**. In fact, there are not strict rules about this practice, differently from the measurement of financial results. The OECD (2019) declared that there is not a sufficient number of institutions creating an expertise about the reporting of social impact and this prevents the spread of impact investing. The study of Andrikopolous (2020) declares that the possibility to include the measurement of the social impact reached by organisations depends on the standardization of information regarding social finance, such as reports and measures.

The research of Mackeciviuté (2020) expresses the need to standardize the measurement of social impact. Throughout the years, a lot of efforts have been put in the research of standard metrics for social impact (SROI, IRIS, Acumen Fund's Lean Data methodology). However, the particularity of impact investments stays in the fact that all the realities are different, and the achievement of social impacts depends on a large variety of factors, so standardization is not the optimal way to treat social impact.

It would be interesting to understand how investors, together with investees, can find a way to construct Key Performance Indicators for each specific case.
Together with the measurement of social impact, another key challenge is the assessment of **social risk**. As Andrikopolous (2020) asserts, impact investments are unique and, in this way, it is difficult to assess probabilities as in traditional deals. However, it would be of major importance to find a way of integrating the quantitative evaluation of impact risk and impact measurement in the consideration of investments. In fact, they influence both the foreseen gain of investments and the appraisal of its feasibility.
Moreover, as it has been described there is a large variety of investors involved with social enterprises, and they are inclined to collaborate with firms but also between them. Thus, they could create a large network useful to delineate techniques and methods to measure social impact and risk.

Another challenge that could be addressed is the one of **mission drift**. What it could happen, as explained by the study of Cetindamar and Ozkazanc-Pan (2017), is that the imbalance between economic and social goals of investors, which is not evident in their missions, could bring social enterprises to experience the risk of mission drift, meaning the risk of giving priority to financial results rather than the creation of social impact. This can be correlated to the evaluation of impact risk. In fact, if investors have not clear in mind what could be the returns of their investment and are dissatisfied with the results of social enterprises, the probability that the aim of reaching economic returns would surpass the initial intent of creating social impact can increase.

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