Louvain School of Management

Impact Investing: fundamental trend or marginal evolution?

Exploring the potential for banks and digital to address key challenges

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INTRODUCTION

Could solutions to social and environmental challenges faced by our societies lie in reinventing our economic models? Is impact investing the highway to that journey's end?

Traditional finance has shown its limitations. The capitalist model is being questioned by both economists and global consulting firms. The book *Re-Imagining Capitalism (McKinsey, 2017)* reflects this movement. The authors argue that while capitalism has been at the root of the creation of massive wealth and human prosperity in our societies, lifting millions of people out of poverty, the unsustainable level of public and private debt and the rising income inequalities we have reached make the case for its evolution. The idea is not to bring capitalism down, but to question the assumptions behind the model to improve it.

The future of our societies relies on our capacity to transform economic models to achieve convergence between financial and social interests. Public as well as philanthropic resources have proved insufficient to address global social and environmental issues. Effective, scalable solutions need to be based on sustainable models. That is where business comes in. The achievement of the Sustainable Development Goals, set up by the United Nations, requires countries cooperation but also, companies' commitment to serve society and the planet. Time has come for business to become a force for good, as featured in INSEAD's latest capital campaign.

By pursuing a double bottom-line objective, impact investing combines the best of business and philanthropy. What makes it particularly interesting is its innovative investment approach to solving global issues by spinning off financially sustainable business models achieving both a financial return and a measurable social or environmental impact. By succeeding in demonstrating both market-rate financial returns and social and environmental value, it will entail the potential to unlock mainstream capital to scale up solutions to the most pressing societal issues, and eventually transform traditional finance.

This thesis intends to answer the following research question:

Impact investing: fundamental trend or marginal evolution? Exploring the potential for banks and digital to address key challenges

Harnessing the full potential of impact investing will require engaging actors from the traditional finance ecosystem. Nowadays, notably because it has largely been developed by niche players (Drexler & Noble, 2013), this new investment approach often remains perceived as an evolution of venture philanthropy, optimized towards the traditional capital market, but remaining at the margins of it. Scaling up the amounts invested will require to go mainstream and attract institutional investors. Yet, many challenges prevent impact investing to gain wider acceptance and be considered as a real investment product by traditional finance. Reviewing these barriers and discussing possible solutions to overcome them constitutes the initial focus of our research.

Considering the constraints faced by the sector led us to question its development perspectives. Will impact investing gain sufficient momentum to transform traditional finance or will it remain a niche market? Wat are the determining factors for its growth? We chose to further investigate the scale-up potential of the market from two different angles: the catalytic roles of banks and digital.

Exploring the potential for banks to address scale up challenges sounded relevant for several reasons. As staple financial intermediaries, and key players in the structuring and sale of investment products, banks are a natural path to increasing the amount of capital pooled into impact investments. Their access to a large panel of investors, from institutional to retail, constitutes an opportunity to broaden the reach of impact investments, especially as some banks have already started to develop impact offerings to meet the demand of High Net Worth Individuals. Even though they face restrictions in their risk taking, we believe the asset class flexibility of impact investments would allow them to find opportunities suiting the profile of retail investors along the risk return continuum. On the banks’ side, impact investment offerings can confer a competitive advantage, in a context of increasing interest - especially among Millennials - for sustainability and social impact. Leading consultancy firms, such as BCG and McKinsey, have, in their most recent industry reports, set the enhancement of impact investing offerings – and more broadly of ESG considerations – high on the agenda of banks. They stress the urgency to make sustainability an integral part of banks offerings to emphasize their long-term vision for the society and meet the demand of future customers looking for more social and environmental impact (i.e. Millennials).

As digital is radically transforming our societies and considering how disruptive technologies can contribute to the scaling up of this equally disruptive investment approach, it was a pretty obvious research topic. How could digital, which is currently used individually by some impact organizations, be leveraged more collectively to create value, open up new frontiers and attract new investors? Even though some initiatives have been developed, their reach appears rather limited. These questions also arose because digital seemed potentially able to provide solutions to some challenges faced by sector, such as its fragmentation and poor intermediation between investors and impact projects, the lack of investment liquidity and last but not least, the need to aggregate a track record of both financial and non-financial returns to build the case for impact investing towards mainstream investors.

This research was first driven by the desire to investigate the prospects for impact investing to become mainstream. Given the potential of this new investment approach to develop sustainable and scalable solutions to some of the most pressing global challenges, we wanted our findings to contribute to the sector growth by identifying possible ways to unlock more capital.

The lack of literature on the role of banks in impact investing, while as mainstream financial intermediaries, their involvement sounds staple to move away from a niche market, underpins our choice to focus on that angle in our research. Two industry reports account for the majority of the available data and recommendations. Very few information regarding the impact investment offerings of banks is disclosed on their websites. It therefore appeared essential to us to highlight this lack of knowledge and further investigate banks' contribution to the market, with the aim of assessing their potential to address scale-up challenges.

Finally, the contrast between on the one hand, the omnipresence of digital in our societies, its power to harness data, to help decision making and to connect people to opportunities, and on the other hand, its absence from the scientific literature on impact investing and the perceived lack of universally accepted solutions, tools and metrics, led us to consider how digital could be better leveraged to catalyze the growth of impact investing.

The first part of this thesis reviews the existing literature on impact investing to better understand the market context and have an overview of the state of knowledge on the field developed to date. It sets the basis for the qualitative research, based on individual interviews of sector professionals identified for their expertise, insights and vision, aiming at investigating the potential for banks and digital to contribute to the sector development. The results of these interviews are reported in the second part of this report (Chapter 2), they are then analyzed on the background of the literature review and further online research in Chapter 3 and conclusions.

PART I: CONTEXTUALIZING IMPACT INVESTING – LITERATURE REVIEW

The first part of this thesis defines the concept of impact investing based on the analysis of the existing scientific literature. After a review of definitional and historical elements, some key market features will be considered. Financial aspects will be addressed afterward. Finally, the challenges to impact investing development will be tackled.

Chapter 1: Definition

1.1. Impact investing

Overall, few academic works on impact investing have been published (Hebb, 2013; Glänzel & Scheuerle, 2016; Robb & Sattell, 2016). Industry-based reports account for much of the literature available on the subject (Hebb, 2013).

The term *impact investing* is relatively new. According to Harji & Jackson (2012), the word first appeared in 2007 following a meeting held at the Rockefeller Foundation's Bellagio Center in Italy; finance, philanthropy, and development leaders were gathered to discuss the development of a new form of investment combining financial return with positive social and environmental impact.

The Global Impact Investing Network (GIIN), an international membership organization supporting the development of impact investing, defines impact investments as follows:

> Investments made into companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets and target a range of returns from below market to market rate, depending upon the circumstances (GIIN, 2014).

Even though impact investing has gained significance in recent years, a uniform and unanimous definition of the concept is still lacking in the academic literature due, notably, to an absence of consensus among the different actors (Höchstädter & Scheck, 2015). Furthermore, a clear identity is identified by the GIIN in its Roadmap for the Future of Impact Investing (2018), as one of the six major elements essential to a long-term rise of impact investing.

Two core components

In their paper, Höchstädter & Scheck (2015) attempt to clarify the notion of impact investing by conducting an academic review of the existing definitions. Overall, despite the various schools of thought, impact investing is commonly defined around the combination of two core elements: the financial return and the non-financial impact (Höchstädter & Scheck, 2015; Roundy et al., 2017; Evans, 2013; Ragin & Palandjian, 2013).

On one hand, the level of financial return usually stays undetermined – but still intentional (Jones & Turner, 2014), ranging from below to above market rate (Best & Harij, 2013; Drexler & Noble, 2013). The time horizon for returns varies between the medium and long term (Guézennec & Malochet, 2013).

On the other hand, the non-financial impact is commonly required to be both intentional (Addis et al., 2013; O'Donohoe et al., 2010) and measurable (Jones & Turner, 2014), this latter condition being necessary to track the progress made and set future objectives (O'Donohoe et al., 2010). In their report, Dexler & Noble (2013), from the World Economic Forum, define impact investing as follows: "*an investment approach intentionally seeking to create both financial return and positive social impact that is actively measured*." (Drexler & Noble, 2013, p.3). However, Toxopeus et al. (2017), argue that the notion of measurability in the impact investment definition is ambivalent for two reasons. First, it could presuppose the measurement of an output as well as a result (e.g. the number of mosquito nets distributed versus the actual decrease in malaria as a result of nets distribution), yet the impact should be evaluated considering the outcome rather than the output (Jackson, 2013). Second, measuring the impact does not guarantee to achieve the result initially expected. According to the authors, impact investments should rather be defined as such ex post, only if an actual impact has been realized. This way, capital shifted towards impactful projects will be maximized.

Regarding the balance of these two dimensions, some authors point out that impact investments require the investor to be, above all, concerned about the non-financial impact, the financial return being only a secondary consideration (Höchstädter & Scheck, 2015). Nevertheless, the question of predominance is often left open or treated according to the theory developed by Freireich & Fulton (2009) who suggest a division of the investors panel into two categories: those prioritizing the non-financial impact and those favoring the maximization of financial return. In their report, Guézennec & Malochet (2013) indicate that impact-first investors are more likely to be found in Continental Europe while finance-first investors commonly belong to the Anglo-Saxon community.

Various types of impact

Even though the term social investment is often used as a synonym of impact investment, the non-financial impact generated is not necessarily social (Viviani, 2018). It could be of various natures (Kappen & Mitchel, 2019) such as environmental, cultural, financial, governmental, developmental, or social. More usually, social investments are considered as a sub-form of impact investing (Höchstädter & Scheck, 2015). Consequently, the term non-financial impact would be preferable (Viviani, 2018).

A distinct asset class

According to some authors, impact investing is an emerging and distinct asset class (Agrawal & Hockerts, 2019; O'Donohoe, 2010) as it calls for new investment and risk management skills as well as different standardized metrics, benchmarks, and rankings. Additionally, innovative organizational structures are required to accommodate those skillsets. Yet, in its report, the Word Economic Forum emphasizes that:

> "An asset class is traditionally defined as securities or investments that behave similarly under varying market conditions and that are governed by a similar set of rules and regulations. Under this definition, it is clear that impact investing is an investment approach across asset classes, or a lens through which investment decisions are made, and not a stand-alone asset class." (Drexler & Noble, 2013, p.7).

Undefined strategic elements

Regarding the strategic elements of impact investments, no specific requirements seem to be set (Höchstädter & Scheck, 2015). First, the investments are not conditioned to a particular geography or population (Höchstädter & Scheck, 2015). Even though underserved populations are mostly targeted, a broader range of people could be impacted if, for instance, environmental challenges are addressed (O'Donohoe et al., 2010). Besides, O'Donohoe et al. (2010) emphasize that underserved populations can also be found in

developed countries. Second, the impact can be delivered through business operations, either through products and services (Höchstädter & Scheck, 2015). Additionally, many different sectors and objectives can be targeted (e.g., Addis et al., 2013; Philips, 2016). Third, concerning the investees' profile, even if a lot of papers leave the characteristics of the recipient undefined, Höchstädter & Scheck (2015) identified two broad perspectives: some authors limit the scope of eligible organizations to mission-driven firms. However, just as people are never exclusively concerned about pure finance or pure social good, organizations are a combination of financial, social and environmental considerations despite their profit or non-profit status (Bugg-Levine & Emerson, 2011). Others, on the contrary, consider only the impact produced regardless of the organization specificities, broadening the scope of potential investees.
Finally, Höchstädter & Scheck's review (2015) point out the absence of restrictions regarding the financial instruments used in impact investing. Nevertheless, according to the GIIN's 2019 Annual Impact Investor Survey, private equity and debt are the most commonly used financial vehicles.

Absence of definitional clarity

The lack of consensus and definitional clarity led some authors to associate unrelated notions with the term impact investing: "*Impact investing is an umbrella concept encompassing several investment tools, including mission related investments (MRIs), program related investments (PRIs), and screening mechanisms for environmental, social, and governance (ESG) priorities."* (Gripne et al., 2016, p.53). However, according to Bugg-Levine & Emerson (2011), this fuzziness is also the opportunity for a wide range of investors to gather under the same broad concept and capitalize on their similarities to cooperate in the resolution of current societal challenges.

1.2. Blended value

Impact investing is intimately linked to the concept of blended value. According to Hebb (2013), the Blended value proposition developed by Jed Emerson is the framework underpinning the notion of impact investing.

Each organization, regardless of its for profit or non-profit objective, creates value. This value is always threefold: financial, social and environmental. However, we systematically tend to associate for-profit organizations with the sole purpose of financial value creation and the non-profit firms with social value generation.

The concept of blended value refers to the maximization of an organization's value creation by the integration in its strategy of those three dimensions – financial, social and environmental. "*Blended value is the recognition that capital, community, and commerce can create more together than the sum of the three independently*" (Bugg-Levine & Emerson, 2011, p.14).

1.3. Position on the investment spectrum

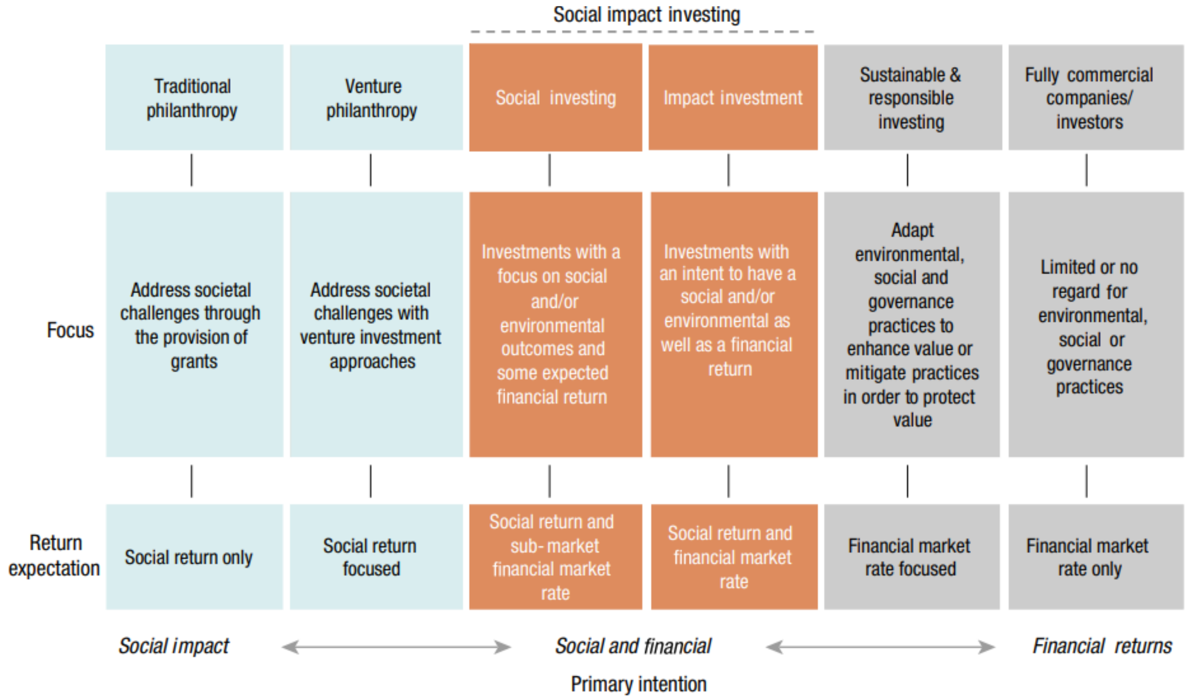
The traditional investment spectrum

The investment spectrum is characterized by a broad set of different expected returns. On one end, the priority is the maximization of the financial return as, for instance, in venture capital. On the other end of the spectrum, the focus is made on social value creation, as in traditional philanthropy. Sometimes, the middle of the spectrum is associated with angel investing since those investors have other motivations than the pursuit of financial return; they support entrepreneurs in the development of their business, occasionally led by the desire to create social good by investing in social mission enterprises (Roundy et al., 2017).

Impact investing within the OECD investment spectrum

The investment spectrum (Figure 1) presented by The Organization for Economic Co-operation and Development (OECD) in its report Social impact investment: the impact imperative for sustainable development (2019) classifies impact investing as one of the intermediate solutions – the other one being sustainable and responsible investing - in-between the two traditional approaches: purely financial or philanthropic. Additionally, it distinguishes between investing 'for impact' (i.e. social investing, where investors prioritize the social or environmental impact) and investing 'with impact' (i.e. impact investment, where investors intend to generate both a financial and a societal return) (OECD, 2019; EVPA, 2019).

Figure 1: investment spectrum



Source : OECD, 2019, p. 9

Impact investing as a sub-form of socially responsible investing

However, some authors consider that impact investing is a sub-set of the broader concept of socially responsible investment (Toxopeus et al., 2017). In his paper, Scholtens (2014), details the seven socially responsible investment strategies identified by Eurosif, which describes itself as "*the leading European association for the promotion and advancement of sustainable and responsible investment across Europe, for the benefit of its members*" (Eurosif, 2020): sustainability theme investment, best in class investment selection, norms-based screening, exclusion of holdings from investment universe, integration of ESG factors in financial analysis, engagement and voting on sustainability matters and impact investment.

Impact investing differentiates itself from the broader concept of socially responsible investment (SRI) by its intention (Hebb, 2013; Tekula & Andersen, 2019) and proactiveness towards impact (O'Donohoe et al., 2010). While SRI is mostly limited to positive or negative screening of firms, impact investing goes a step further (Evenett & Richter 2011, p. 14) and "*[considers] the firm's business model as a source of social or environmental value*" (Barman, 2015, p.16). In sustainable investing, environmental and social considerations are only perceived as a source of risks and opportunities affecting the financial performance of the firm (Bugg-Levine and Emerson, 2011). Even though they have in common the pursuit of non-financial impact, impact investing distinguishes itself from grant funding by its financial return requirement (Addis et al., 2013).

The differentiating factors in Impact investing

As highlighted in the review of Agrawal & Hockerts (2019), impact investing is often associated with various terms such as socially responsible investments, social investing, responsible investing, or microfinance. The more commonly used being social finance. However, many features distinguish those notions from the concept of impact investing, supporting the idea of impact investments being a unique asset class. Overall, six criteria differentiate impact investing from similarly used terms: the amount of capital invested, the degree of engagement with the investee, the process of selection, the social and commercial outcomes, the reporting outcomes, and the government role. Further details are displayed in the figure below.

Figure 2: Factors on which impact investing differs from similar sounding terms

	ImInv Vs Microfinance	ImInv Vs Social responsible investing	ImInv Vs Social impact bonds	ImInv Vs Venture philanthropy
Sum of Capital Invested	Higher	Lower	Equal	Similar
Degree of engagement with the investee	Higher	Higher	Lower	Similar
Process of Selection	Similar to venture capital	Higher	Different	Similar
Social and Commercial Outcome	Depends on the fund mandate	Higher	Depends on the mandate	no commercial outcomes for VP
Reporting of outcomes	Higher	Higher	Similar	Similar
Government role	Depend on stakeholders	Depend on stakeholders	Depends on the stakeholders	Depends on stakeholder

Source : Agrawal & Hockerts, 2019, p.7

Chapter 2: Background

Long-term global trend

According to Addis et al. (2013), impact investing is the result of a long-term global trend.

While the emergence of the term impact investing is commonly associated with a meeting held in 2007 at the Rockefeller Foundation with a group of pioneer investors to envision the development of an alternative form of investment (Bugg-Levine & Emerson 2011; Harji & Jackson, 2012), many reports refer to the 18th century and the religious society Quakers, when addressing the origin of impact investing. The Quaker community managed its investments in line with its values, refusing to finance slavery and other inhumane practices (Tekula & Andersen, 2019; Bugg-Levine & Emerson, 2011; Phillips, 2016). Some even consider that the very first form of ethical investing appeared in the 1500s, when moral and religious beliefs were integrated in the investment process (Deutsche Bank Group, 2012); the Haseki Sultan Imaret, built in Jerusalem in 1552 and established as what we would now call a social enterprise, is an example from the period (Carnie, 2017).

Actually, different manifestations of impact investing have occurred overtime in the history, the term 'impact investing', defined as such in 2007, being the latest combined form of economic and societal considerations (Bugg-Levine & Emerson, 2011).

The "conscious consumer" era

The appearance, in the late 1960s, of the socially responsible investing at the fiduciary-end of the capital spectrum (Trelstad, 2016) is triggered by the rise of conscious investors increasingly aware about environment and sustainability. Initially, the movement was rather passive, excluding controversial activities from possible investments through screening or using shareholder activism to support firms' responsible development. Phillips (2016) suggests that the roots of impact investment date back to global protests and divestment campaigns against the African apartheid regime in the 1980s. Over time, more proactive methods, led by investors willing to use business as a force for good (Tekula & Andersen, 2019) have emerged, such as fair trade, microfinance and corporate social responsibility – several authors mention that the appearance of impact investing is closely related to this movement (e.g. Bugg-Levine & Goldstein, 2009; Phillips, 2016). "*What is new is that impact* *investors are profoundly optimistic about the role business can play in advancing the common good and the leverage social enterprises can achieve by employing financial tools*" (Bugg-Levine & Emerson, 2011, p.11). The rise of responsible investment strategies has therefore also been triggered by the investors themselves – both large institutional and individuals – driving at the same time the "conscious consumer" era. Undoubtedly, the 2008 financial crisis has played a catalytic role in the development of impact investing policies and practices (Phillips, 2016). Globally, this increasing interest towards sustainability led many companies to start reporting on their social responsibility, bringing progressively the whole industry, notably the leading financial data providers such as MSCI, Bloomberg or Sustainalytics, to supply ESG data (Snider, 2015). Berry (2016) explains that the amount of capital required to solve current social and environmental challenges exceeds by far the gift potential of governments and donors, arguing for a financial market intervention, combining the power of social businesses and investors to address those needs.

The role of Foundations

While the evolution of the fiduciary-end of the capital spectrum led to the appearance of socially responsible investing, the philanthropic-end is further developed by the introduction of program related investments (PRIs), firstly introduced by the Ford Foundation during the late 1960s with a view to shift from grants to low-interest loans (Trelstad, 2016). In Trelstad's view, the concept of impact investing results from the intersection between PRIs and sustainable investing. Combs (2014), on the other hand, argues that the arrival of impact investing is related to the foundations' missions related investments (MRIs) which go beyond the PRIs as those investments imply the expectation of a market-like return alongside a societal impact. This means that foundations have been investing for impact for many years.

The role of development finance institutions

Nevertheless, in their paper, Jones & Turner (2014) argue that the modern version of impact investing was initiated after the Second World War, with the appearance of development finance institutions (DFIs) such as the World Bank and the International Finance Corporation, whose mission was primarily to support the reconstruction of Europe. Many other regional and international DFIs have emerged over time to help businesses and development initiatives, acting as impact investors for underdeveloped countries (Littlefield, 2011).

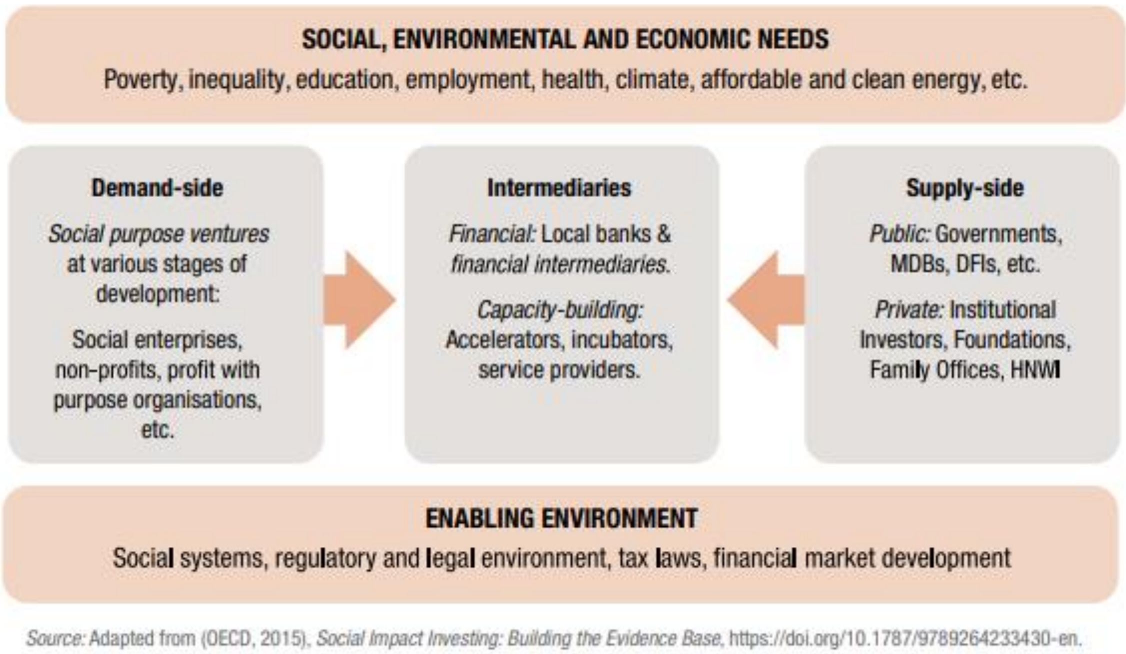
Chapter 3: Market context analysis

As in traditional finance, the impact investing market includes three main categories of actors: the investors, the investees and the intermediaries (Viviani, 2018; J.P. Morgan, 2010; Bugg-Levine & Emerson 2011). In his paper, Viviani (2018) uses the term multidimensional to define these players because of their twofold objective: financial and societal.

A wide variety of players are involved in the impact investing market (Jones & Turner, 2014; Ragin & Palandjian, 2013), offering a broad range of services, and fulfilling various needs. However, Jones & Turner (2014) warn that their roles have to be distinct and well defined otherwise, they could overlap.

The OECD’s Social Impact Investment Market Framework (2019) – see figure below - gives a complete overview of the impact investing ecosystem.

Figure 3: Social impact investment market framework



Source : OECD, 2019, p.8

3.1. Supply overview

3.1.1. Investors' profiles

Investor types

In its paper, Impact Imperatives for Sustainable Development, the OECD (2019), divides the supply-side of the impact investing market into two broad categories: the public and the private investors. An additional distinction can be made between the asset owners and the asset managers (J.P. Morgan, 2010; Bugg-Levine & Emerson, 2011). The public category refers to governments, development finance institutions (DFIs), and multilateral development banks (MDBs) while, the private category includes institutional investors, family offices, foundations and high net worth individuals - playing a critical role in impact investing (Combs, 2014). DFIs raise and manage funds from private and public sources to allocate them where they are most needed, targeting undeserved and disadvantaged populations. They also finance projects that would not otherwise have received support from the traditional banking system or the private sector (Phillips, 2016). Additional players were identified by the Social Impact Investment Taskforce established under the UK's presidency of the G8; social investment wholesalers, charitable trusts, local funds, banks, corporates, and mass retail (G8, 2014). Some pension funds are also starting to invest with a view to have a positive impact on the society (Philips, 2016; Ragin & Palandjian, 2013).

Gender influence

Osili et al. (2018) have studied the gender influence on the impact investing behavior of High Net Worth Individuals (HNWI). Their findings show that there are no significant gender differences in the participation in impact investing. Still, women appear to be more willing to learn about this practice than men. Additionally, the study points out that impact investors tend to be young, wealthy, and educated with at least a bachelor's degree. The same attributes characterized the investors eager to replace their charitable giving by impact investments.

Criticism of impact investors

In Rapaczynski's view (2016), impact investors are not investors as such. He argues that:

> "They are not predicting that the market will move in their direction – but rather want to move the fiduciary corporate decision makers in the direction of certain socially conscious decisions, even at a sacrifice of financial return – they are in fact in a different kind of business: that of corporate lobbying, rather than investing." (p.5)

3.1.2. Investors' expectations and motivations

Expectations setting process

When investing for impact, an investor considers three criteria: his impact preferences, the impact risk/return and his overall impact strategy. The balance of these preferences will determine the kind of impact that the investor desires and for whom. Trelstad (2016) suggests the use of the five "P's" method: determining the place, the type of people, the kind of socially beneficial products, the planet-friendly strategy or the paradigm shifting strategy. Then, the investor looks at the risk he is ready to bear relative to the impact he wants to achieve. Finally, he establishes his impact strategy based on his expectations – which, as has been pointed out above, vary widely among investors.

The motivations of retail investors

Because their investments are usually guided by their own values (Robb & Sattell, 2016; Roundy et al., 2017), the range of motivations amongst impact investors is very broad and complex; it is impossible to classify them using traditional typologies (i.e. purely financial or social).

Furthermore, the emotional factor plays a huge role in the impact investment decisions of retail investors; many invest based on their own life experience (Robb & Sattell, 2016). However, overall, generating both financial and social returns remains their primary motivation. Another motivational aspect frequently mentioned is the belief that market-based solutions are more likely to create sustainable impact. Indeed, unlike grants in traditional philanthropy, the financial return generated by impact investments could be further reinvested to leverage the social impact. Moreover, grant usage being regulated, impact investing constitutes a more flexible source of financing for organizations, assuring the investors to provide the right type of support. However, it should not be considered as a substitute for philanthropy but rather as an additional source of capital (Rangan et al., 2011); as mentioned earlier, grants are necessary to scale up early stage organizations which do not have access to other sources of funding (Tekula & Andersen, 2019). An additional motivation highlighted by Roundy et al. (2017) is the desire to contribute to the development of projects that require longer term loans - often called "patient capital" (p.24) - since traditional finance implies shorter time-horizon.

The motivations of professional investors

According to the 2019 Annual Impact Investor Survey conducted by the GIIN (Mudaliar et al., 2019), the prevailing motivation among professional investors to make impact investments is the organization's commitment to be a responsible investor (85%), closely followed by the integration in the organization's mission of intentional impact seeking through investments (84%). Other motivational factors are the organization impact goal achievement (71%), the contribution to a global agenda such as the SDGs (51%), clients' demand (51%), the financial attractiveness of these investments (30%), the opportunity to engage in growing sectors and geographies (28%), portfolio diversification (23%) and respect of regulatory measures (11%).

Preferred investments areas

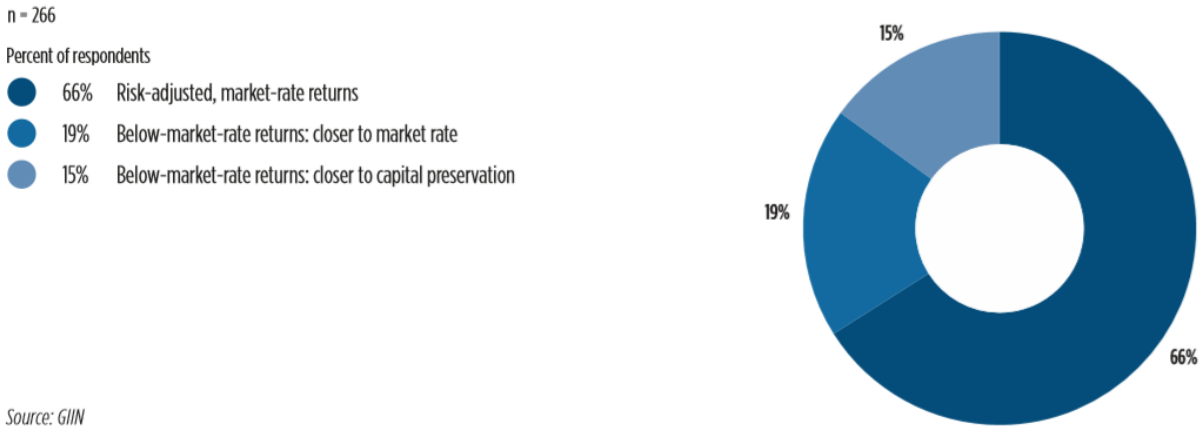
Investors seem to prefer certain sectors: energy is at the top position in terms of asset under management (AUM), followed by microfinance and other financial services. The food and agriculture sector is in fourth position. However, when looking at the number of people investing in those categories, the food and agriculture sector comes first - suggesting smaller investment size than in energy or microfinance - then come energy, healthcare, education and financial services (Mudaliar et al., 2019).

3.1.3. Tradeoff between financial and non-financial return

As explained by Roundy et al. (2017), a disagreement among the impact investing market participants regarding the balance between financial and societal returns still exists. As previously mentioned, a distinction is made between impact-first and finance-first investors (Roundy et al., 2017). While some are ready to accept a lower financial return to reach a specific social or environmental goal, others are not willing to make this sacrifice (Barman, 2015) and claim that some impact investing strategies (e.g. sustainable corporate bonds, sustainable private equity, sustainable real assets) allow the investor to benefit from market-like returns or even, under particular circumstances, above the market return (Snider, 2018). Additionally, Roundy et al. (2017), mention a third standpoint on the question: impact investors can go beyond the consideration of a strict below or above the market return with the creation of a balanced impact investments portfolio, including below, at and above market returns.

According to the 2019 Annual Impact Investor Survey conducted by GIIN, 66% of their 266 respondents target risk-adjusted market-rate returns. Besides, 19% sought below market-rate returns, closer to market rate while 15% expect below market-rate returns but closer to capital preservation (figure 4) (Mudaliar et al., 2019).

Figure 4: Target financial returns principally sought



Source: GIIN, 2019, p.33

3.1.4. Intermediaries' profiles

Intermediaries play a crucial role either by connecting the investors with the investees (e.g. social banks, banks, community development finance institutions, impact investment fund managers, crowd funding platforms), or by building the capacity of the whole ecosystem through, for instance, infrastructure building, consulting, data providing or impact measurement tools development (accelerators, incubators, service providers, consulting firms, associations) (OECD, 2019; G8, 2014; J.P. Morgan, 2010; Bugg-Levine & Emerson, 2011; Jones & Turner, 2014).

The enabling role of donors

In their paper, Tekula & Andersen (2019) provide an exploration of four impact investing market facilitators: governments, charitable foundations, philanthropy, and HNWIs. They first clarify the notion of the facilitator, defined as: "[facilitators are] *those organizations stimulating* [through donations] *the growth of social enterprises and nonprofits and assisting them in attaining scale, such that they are fundable by larger impact investors*" (p.146). Indeed, the 2019 Annual Impact Investor Survey conducted by GIIN displays the percentage of AUM by business stage, amounting to only 3% for seed and start-up stage organizations. Respectively, 3% and 35% of the respondents allocate their capital in seed and start-up stage organizations, highlighting the need to help social enterprises in their early stages of development to scale up and gain access to impact investments (Tekula & Andersen, 2019; G8, 2014). The business stage with the highest amount of AUM is the growth stage, closely followed by the mature private and public companies (Mudaliar et al., 2019).

The authors then identify four courses of action for the facilitators: *enabling, improving, moving, and launching assets to market*. *Enabling* refers to the creation of excellent market infrastructures besides the improvement of productivity through, for instance, grant making, transportation infrastructure building and standardized metrics development. *Improving* mainly concerns the connection between the investors and the investees. The *moving* facilitation type is about helping early stage social enterprises to scale up to have access to larger investors by using patient or first-loss capital. Finally, *launching* relates to the provision of initial capital to yield project growth. The government and the non-profit sector can participate in the four facilitation types, whereas, on one hand, private capital can intervene only in the moving and launching processes and on the other hand, trade associations are only involved in the enabling and improving phases.

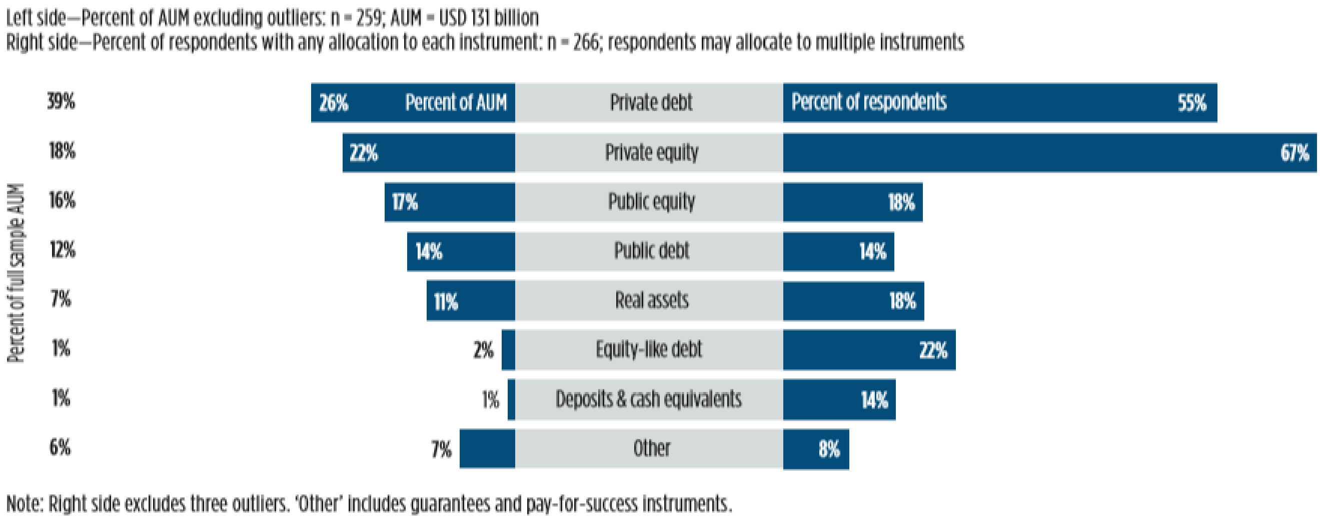
Additionally, in their paper, Institutional Impact Investing: Practice and Policy, Wood et al. (2013) emphasize the importance of coordination between the institutions and the policy makers to allow market growth and development.

3.1.5. Investment offer

As previously mentioned, impact investments encompass a wide range of financial instruments (Tekula & Andersen, 2019): secured and unsecured loans, charity bonds, quasi-equity and equity (G8, 2014). Besides, new vehicles have been set up, such as social impact bonds (SIB), community investment notes and pay-for-success contracts (Tekula & Andersen, 2019).

According to the 2019 Annual Impact Investor Survey conducted by GIIN, the investment vehicle most commonly used by investors is private equity, with 67% of the respondents choosing this investment strategy. Nevertheless, in terms of AUM, private equity accounts for only 22% of the total AUM while private debt amounts to 26% and comes at the second position in terms of investors' preferences with 55% of respondents deploying capital through this asset class; senior, subordinated and mezzanine debt being the most commonly used instruments. The Pay-For-Success contracts and SIBs are the least chosen investment strategies (Mudaliar et al., 2019). The figure below displays the full ranking.

Figure 5: Instrument allocations by AUM and number of respondents



Source : GIIN, 2019, p.22

Social impact bonds

Social impact bonds are a financial instrument by which a bond-issuing organization raises funds from private investors to finance the operating costs of a service provider. If the -predefined- project outcomes are achieved, the government makes a payment to the bond-issuing organization which, in turn, repays the private investors and potentially provides them with a return on their investment (Liebman, 2011).

Social impact bonds are a specific form of pay-for-success (PFS) contracts – "*a contracting mechanism in which government (or another payer) pays service providers after they achieve predefined outcomes"* (Ragin & Palandjian, 2013, p.64). However, while in PFS contracts, the risks are borne by the provider, who supports the loss if the project outcomes are not reached, for social impact bonds, the risk is shifted to private investors. Indeed,

> The SIB structure enables the government (or other payers) to shift program risk to private investors who finance the service delivery upfront, with ultimate payment to the investors based on the achievement of predefined outcomes. If the outcomes are not achieved, the government is not required to repay investors. In other words, the government only pays for results (Ragin & Palandjian, 2013, p.64).

Venture philanthropy

Venture philanthropy, developed by the non-profit sector, is also an impact investing strategy (Tekula & Andersen, 2019). Its objective is to support the growth and scale up social purpose organizations (SPOs) with financial and non-financial assistance - as in traditional venture capital - to maximize social impact (Hehenberger & Alemany, 2017). As explained on the European Venture Philanthropy Association (EVPA) website, venture philanthropy is characterized by three key elements: tailor-made financial instruments suiting the needs of SPOs, non-financial support to assure the maximization of the social impact and the sustainability of the business model, and impact measurement to set objective targets and manage the negative outcomes.

3.2. Demand overview

3.2.1. Investees' profiles

Various forms of impact-driven organizations

The demand-side of the impact investing market gathers various forms of *social-purpose ventures*, also called *impact-driven organizations* such social enterprises, non-profit, profit with purpose organizations, grant reliant organizations, grant-funded organizations with trading activities, profit constrained organizations, profit with purpose businesses, and businesses setting significant outcomes objectives (OECD, 2019; G8, 2014).

Usually, the investees are SMEs. According to Jones & Turner (2014), these are in best position to induce a positive system change and allow development, provided that they benefit from strategic investments.

Value creation within multidimensional enterprises

Viviani (2018) explores the value creation within multidimensional enterprises and concludes that those organizations can benefit from operational – or financial - synergies by combining social and financial activities. Indeed, as the two dimensions leverage each other, the value created is higher than if the two objectives are pursued separately in two different entities. Additionally, social entrepreneurs usually master multidisciplinary skills, enabling them to maximize both the social and the financial value. Nevertheless, regulations, specific costs and conflicts arising from those organizations' hybrid mission undermine value creation.

Chapter 4: Financial analysis

Various impact investing market size estimations

Various estimations of the impact investing market size are proposed by sector organizations.

In its report, Sizing the impact investing market, (2019), the GIIN estimates that the global impact investing market amounted to USD 502 billion AUM in 2018, among which USD 71.9 billion were managed by European investors (Gianoncelli, 2019). While the median level of firms' AUM is USD 29 million, the average is USD 420 million, suggesting that some organizations manage very large portfolios. The survey reveals that 80% of its respondents - who already took part in the survey in 2014 - have experienced a CAGR of 17% in their AUM over the past four years.

Furthermore, most investors are based in developed markets: 58% of the 1102 organizations interviewed were established in the United States and 21% in Europe (Mudaliar & Dithrich, 2019).

The Principles for Responsible Investment Network differentiates between traditional and mainstream impact investing. While the traditional form refers to the theory of change and the concept of purpose driven organizations, the mainstream approach is related to liquid and mature businesses having a positive impact on society. In their Impact investing Market Map, they consider direct and indirect investments in 10 thematic areas and estimate the size of the traditional impact investing market as USD 226 billion and the mainstream impact investing market as USD 1.3 trillion (Morriesen, 2018).

Finally, in its European SRI study 2018, Eurosif concludes that the impact investing market amounted to USD 108 billion AUM in 2017, registering a CAGR of 52% compared to 2013 (USD 20 billion AUM) (Eurosif, 2018).

Those substantial differences in market size estimations highlight the need for a collective and integrated approach allowing for more accurate measurements (Gianoncelli, 2019).

Nevertheless, these organizations agree on the growth experienced by the impact investing sector in recent years. The GIIN has identified three major causes for this development. First, the desire of investors to align their investments with their values, related to the change in their perception of the role of business in society. Second, their increasing awareness about the benefices to align financial and social objectives notably, regarding long-term profitability. Finally, the willingness to align with global frameworks such as the SDGs (Bouri et al., 2018).

The small size of the impact investing market, compared to traditional capital markets, remains a concern. "*Impact investing is increasingly viewed as a tool to encourage investors and enterprises to simultaneously pursue financial and social outcomes, but remains a niche practice relative to the investing industry as a whole*" (The Economist, 2017 cited in Lee et al., 2020, p.103). However, the EVPA argues that impact investors, even though not numerous, set the bases for new business practices. They serve as a 'test' to develop and adjust this new market to further allow mainstream investors to step in (Gianoncelli, 2019).

4.1. Market Liquidity

Impact investments' liquidity is poorly covered by the literature.

Various authors argue that the development of a secondary market is essential to increase the impact investing market liquidity and allow investors to exit more easily, which are necessary conditions to grow a successful investment activity (Harji & Jackson, 2012) and attract large institutional investors (Mendell & Barbosa, 2013). The "*liquidity and exist risk*" was identified as a severe risk by one fifth of the participants to the 2019 Annual Impact Investor Survey conducted by the GIIN (Mudaliar et al., 2019, p.35). Additionally, investors' concerns about exit options are one of the most significant challenges identified by fund managers when raising capital from impact investors (Mudaliar et al., 2019, p.46; Bouri et al., 2018). According to Mendell & Barbosa (2013), "*existing barriers in the market explain the difficulty of developing a secondary market that will generate ongoing capitalization of these [social finance] enterprises and organizations"* (p.114). The two authors envision the creation of a secondary market; on one hand, they point out the predominant role public policies and securitization mechanisms may have in the liquidity creation process. On the other hand, they consider existing exchange platforms enabling investors to channel capital into social enterprises and investigate whether they could support secondary market transactions. Their findings highlight that institutional and structural barriers, related to the variety and hybrid nature of social enterprises, currently prevent the development of a secondary market.

4.2. Financial returns

4.2.1. Investigating the possibility of generating high returns while solving global issues

Opinions on this matter still largely differ (Evans, 2013).

Some argue that social and financial returns "*are not a zero-sum game*" (Jones & Turner, 2014, p.307), meaning that higher financial returns would not necessarily induce lower social benefits and vice versa. Snider (2015), declares that:

> A commonly held belief among investors is that impact investing (…) will require a trade-off in performance. Though this may have been true in the early days of impact investing, the space has evolved significantly in the last decade (p.1).

Others go a step further and suggest that pursuing the two objectives simultaneously should lead to even better results than if each goal is addressed separately (Robb and Sattell, 2016; Viviani, 2018) as the combination of both interests generates additional value (Clarkin & Cangioni, 2016).

> An impact investment should be able to generate both more of a financial return and more social or environmental impact than an investor who pursues a profit maximizing investment strategy and donates a certain portion of the financial returns to achieve social or environmental goals" (Robinson & Nillson, 2012 cited in Trelstad, 2016, p.4).

This theory has already been developed by Emerson & Caba (2000) long before the emergence of formal impact investing (Clarkin & Cangioni, 2016).

Some authors even consider that impact investments are justified only if they generate greater value than a simple portfolio diversification (Viviani, 2018). They argue that long-term sustainability requires both types of returns (Jones & Turner, 2014).

On the contrary, a third category of actors considers that achieving social returns automatically imply to sacrifice a part of financial return (Evans, 2013; Robb & Sattell, 2016).

4.2.2. Investigating the equivalence with financial returns generated by traditional capital markets

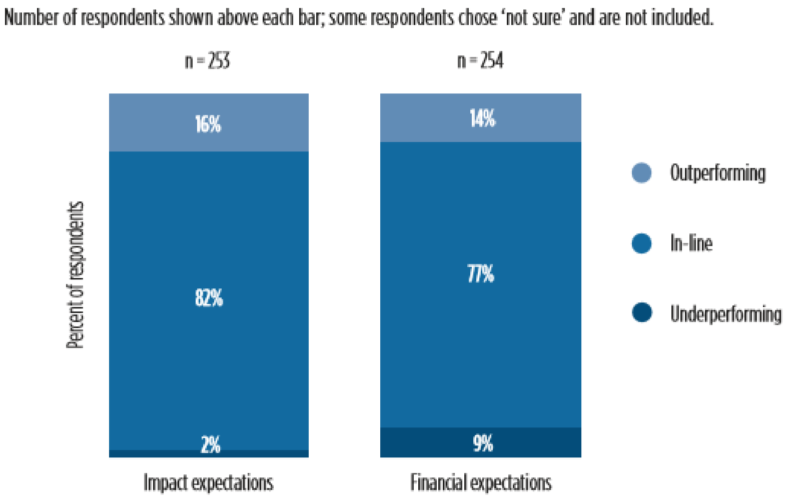
"*The responsible investment literature generally observes that there do not appear to be statistically significant differences in the financial returns of investments that in some ways account for environmental and social dimensions*." (Scholtens, 2014, p.383)

The author based his statement on three different works. First, he cites Cochrane (2001) who argues that the equivalence with the returns generated by traditional capital markets is due to an incomplete asset pricing model omitting, for instance, an unknow sustainability variable. Then, he mentions Boutin-Dufresne & Savaria (2004), explaining that the expectations of market players take time to adapt, the concept of responsible investments being relatively new, market professionals can take advantage of this inefficiency and earn arbitrage profits. Finally, the author argues that according to Sharfman & Fernando (2008), the utility function could be much more complex than commonly presumed; risk aversion -

instead of the traditional risk-neutral supposition – could impact the consideration of social and environmental factors.

In its 2019 Annual Impact Investor Survey, the GIIN investigates the expected and realized gross returns for private markets investments. The results should be analyzed with care considering the relatively small number of respondents. First, it is interesting to observe that 66% of the participants target risk-adjusted market-rate returns whereas 19% sought below market-rate returns – closer to market rate - and 15% below market-rate returns – closer to capital preservation. The organizations targeting market-rate returns are more likely to be for-profit funds while, predictably, below market-rate is acceptable to non-profit funds or foundations. It appears that the majority of respondents have met or even exceeded their financial and impact return expectations since inception (figure 6) (Mudaliar et al., 2019).

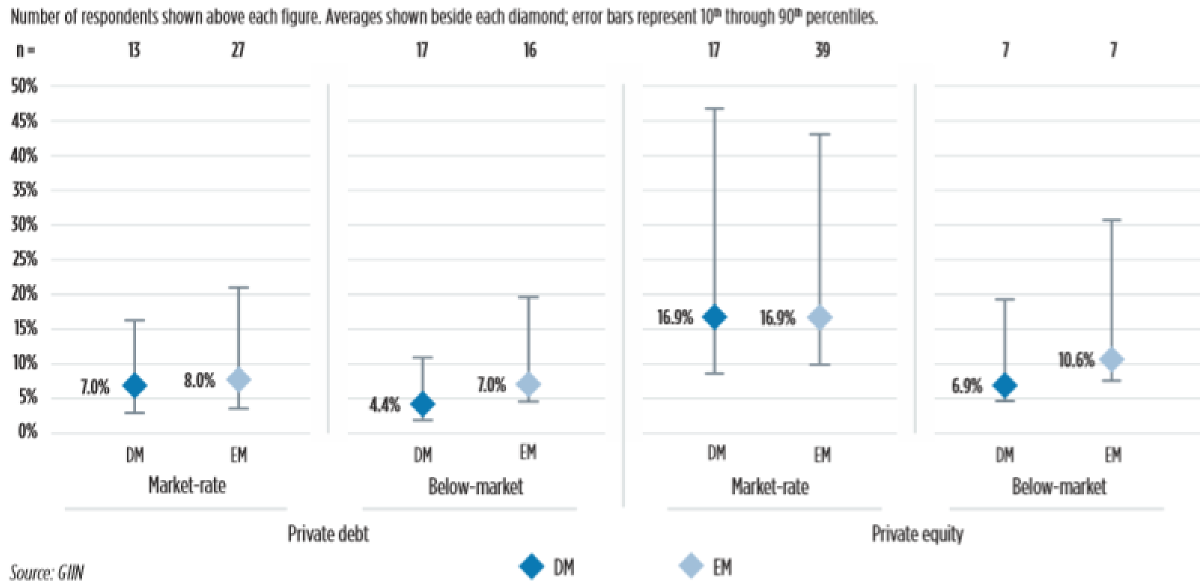
Figure 6: Performance relative to expectations



Source : GIIN, 2019, p.34

The figure below shows the average gross returns realized for private markets investments since inception. As anticipated, investors targeting market-rate performances realized higher returns than below-market seekers and equity investments performed better, on average, than debt did. Additionally, returns have generally been higher for emerging than for developed markets.

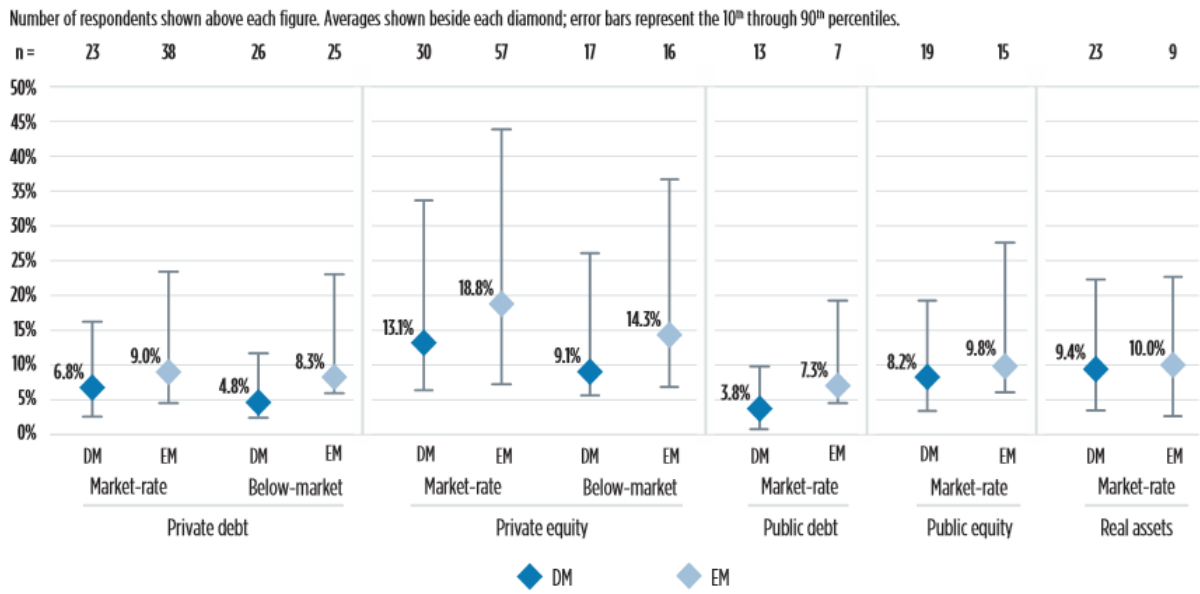
Figure 7: Average gross realized returns for private markets investments since inception



Source : GIIN, 2019, p.35

Finally, the survey displays expected average gross returns for 2018 vintage private markets investments (figure 8). Again, the expectations are higher for investments made in emerging than in developed countries. As would be expected, investors targeting market-rate returns have higher expectations than those seeking below market returns.

Figure 8: Average gross return expectations for 2018 vintage private markets investments



Source : GIIN, 2019, p.34

Sustainability driven organizations: do they perform better?

George Serafeim, assistant professors at Harvard Business School has researched sustainability-driven organizations. His findings show that those firms achieve better performances than their competitors in the long run (Combs, 2014).

4.2.3. Investment time-horizon

The time horizon for impact investing varies between the medium and long-term as investees and intermediaries usually have longer-term needs than in traditional finance (Guézennec & Malochet, 2013). Indeed, the early stage of market development and its poor liquidity require investors to be more tolerant regarding their investment time-horizon (Ormiston et al., 2015).

4.3. Social impact measurement

While the financial performance of impact investments is relatively easy to measure, the quantification of social and environmental impact is much more complex (Hebb, 2013). The lack of universally accepted measurement standards leads in some cases to "*impact washing*" (Verrinder et al., 2018).

In their literature review, Clarkin & Cangioni (2016) observe that social impact measurement and more precisely, the challenges and opportunities it represents, are a heavily covered topic. In fact, the concept of social and environmental impact assessment already emerged during the 1950s with many studies attempting to measure the influence of large infrastructure projects (e.g. highways) on populations and environment (Clarkin & Cangioni, 2016).

IRIS, IRIS + and GIIRS

In the early stage of the impact investing market development, the need for legitimacy led the Rockefeller Foundation, the Acumen fund and B-lab to develop the first impact assessment tool called the Impact Reporting and Investment Standards (IRIS) (Hebb, 2013; Barman, 2015).

> IRIS is a universal language for social, environmental, and financial performance reporting. It was developed as a tool for the impact investing industry to improve

> transparency, increase the credibility of social and environmental performance data, and facilitate investment comparability and performance benchmarking (GIIN, 2011, p.c)

IRIS was designed to be the equivalent of traditional reporting standards - like the GAAP or the IFRS - in impact investing (Barman, 2015). Since 2009, IRIS is managed by the Global Impact Investing Network (GIIN, 2011). In 2019, the GIIN developed the free publicly available resource IRIS +.

> IRIS+ is the generally accepted system for impact investors to measure, manage, and optimize their impact. (…) it combines impact investing's most widely used impact performance metrics with research, evidence, and practical implementation guidance into a single, curated system. (GIIN, 2019)

Simultaneously, in 2008, a second system was conceptualized by the same group of actors: the Global Impact Investing Rating System (GIIRS). Again, the concept was based on existing capital market tools: established rating systems such as Morningstar's or Moody's (Barman 2015; Jackson 2013). In 2011, the independent nonprofit B-Lab developed the GIIRS (Hebb, 2013; Barman, 2015). "*The GIIRS rating system builds on the IRIS Catalog of Metrics in conjunction with additional criteria to come up with an overall fund score for a variety of business models in which the fund invests*." (GIIN, 2019) "*GIIRS Ratings are the gold standard for funds that manage their portfolio's impact with the same rigor as their financial performance*." (B-Analytics, 2020).

The theory of change

According to Jackson (2013), the *theory of change* should be a core element of the impact measurement as it could help achieving better results (Verrinder et al., 2018). The term originally comes from the program evaluation field,

> It refers to the construction of a model that specifies (usually visually) the underlying logic, assumptions, influences, causal linkages and expected outcomes of a development program or project. Through the collection and analysis of performance data, this model can be tested against the actual process experienced, and results attained, by the intervention (Jackson, 2013, p.100).

This evaluation process allows managers to quickly understand how to improve their interventions to maximize societal outcomes. Some actors already use the theory of change, for instance, the Rockefeller foundation built an industry-wide theory of change in 2012 to assess the field building strategy. Other organizations also use this tool but, they are still in the minority.

In their paper, Verrinder et al. (2018) investigate the benefits of implementing the theory of change by conducting case studies across three organizations. Their findings shows that, even though theory of change allows an improved impact communication, a better identification of the measurement indicators and a greater overview of the overall strategy, it is not sufficient to accurately measure impact as it only helps to identify what should be measured and gives no information on how to do it. Yet, this information remains very important as nowadays, many actors still confuse the outputs – being "the activity results" (i.e. the number of people reached) with the outcomes – being "*all the results intended or unintended minus what would have happened without the intervention*". The real impact being measured by aggregating the outcomes rather than the outputs (Jackson, 2013, p.103).

Social return on investment

Social return on investment (SROI) is based on the monetization of social impact, considering the value created and the cost avoided (Guézennec & Malochet, 2013).

Impact measurement statistics

The 2019 Annual Impact Investor Survey conducted by the GIIN reveals that 66% of the 266 participants measure impact through qualitative information, 63% use metrics that are not aligned to any external frameworks or methodologies, 49% work with metrics aligned with IRIS and 39% employ standard frameworks and assessment tools such as GIIRS, SASB (Sustainable Accounting Standards Board). Only 2% do not measure social and environmental impact (Mudaliar et al., 2019).

4.4. Risk assessment

Higher risk tolerance than traditional investors

As in traditional capital markets, the investor's appetite for risk and return depends on his expectations (Ormiston et al., 2015). Arregui & Chu (2013), outline that "*what distinguishes impact investors from traditional investors is that they have a higher tolerance for risks*" (Cited by Brest & Born, 2013, p.29).

Impact investments in early stage organizations are necessarily riskier, especially when those companies target base-of-the-pyramid communities (BOP), requiring massive initial investments in technology or marketing. Investors willing to take that risk are more likely to be part of the "social-first" category (Brest & Born, 2013).

Commonly identified risks

The 2019 Annual Impact Investor Survey conducted by the GIIN reported that respondents perceive 'business model execution and management risk' as the most severe risk to their impact investment. This is followed by 'country and currency risk', then, the 'liquidity and exit risk'. The 'macroeconomic' and 'financing risk' are in fourth and fifth positions, respectively (Mudaliar et al., 2019).

Chapter 5: Challenges to the development of impact investing

The Global Impact Investing Network has established a Roadmap for the future of impact investing. In this report, it notably investigates the six major challenges faced by the sector. Those are detailed below besides other barriers identified by the literature.

5.1. Lack of clear identity

To gain legitimacy, a concept needs definitional clarity. In its Roadmap, the GIIN argues that "*Successful social movements have clear identities and a shared sense of purpose*" (Bouri et al., 2018, p.41). Additionally, to cooperate effectively, the different market players need to share a common ground (Trelstad, 2016). The definition of impact investing is so broad that it is difficult to determine what is an impact investment and what is not (Trelstatd, 2016; Combs, 2014) which constitutes a huge limit to the sector development (Bouri et al., 2018). To engage mainstream investors, the barriers related to the confusion around the concept of impact investing need to be removed by the publication of clear and precise knowledge about the field (Höchstädter & Scheck, 2015; Bouri et al., 2018). However, currently, the number of academic works on impact investing still remains very low (Agrawal & Hockerts, 2019).

Beyond the difficulty in attracting investors and improve the cooperation between the actors, Höchstädter & Scheck (2015) point out another issue: "*without a specific framing of the concept, government actors cannot provide targeted support to build the necessary market ecosystem*" (p.451).

5.2. Lack of market liquidity

As mentioned in the previous chapter, the absence of a secondary market and the medium- or long-term time-horizon of impact investments contribute to a poor impact investing market liquidity (Guézennec & Malochet, 2013). Besides, the lack of exit strategies increases the risk of those investments preventing some investors to step in.

5.3. Lack of policies and regulations

Several papers highlight the lack of supportive policies and regulations in the impact investing industry (Wood et al., 2013; Hebb, 2013; Guézennec & Malochet, 2013).

For instance, the regulations regarding the access to private capital for social companies (i.e. organizations that are not exclusively for-profit) are very restrictive in many countries. The lack of proper status for those enterprises limit seriously their capacity to grow and consequently, hinders the development of the whole impact investing market (Ormiston et al., 2015; Guézennec & Malochet, 2013). Mendell & Barbosa (2013) point out that "*The need for capital is still unmet, largely due to existing structural and/or institutional barriers calling for further innovation*" (p.114).

Policies and regulations could incentivize impact investments, and some argue that tax or financial benefit could catalyze the market development (Bouri et al., 2018).

However, the Roadmap of the GIIN reveals that for some investors, the lack of government regulations is not a barrier to impact investing development since those policies would have, according to them, a limited effect on the market anyway (Bouri et al., 2018).

5.4. Inadequate investment behavior and expectations

A third point raised when addressing the challenges to impact investing development is the paradigm that governs investment behavior and expectations.

Although all organizations are not purely economic nor purely social but rather a combination of financial, social, and environmental considerations, our entire system is built around this mistaken belief. This idea prevented us using business as a force for good to solve global societal challenges and move towards a more sustainable world (Bugg-Levine & Emerson, 2011). Investors mindsets are shaped by this duality. A study has shown that efficient allocation leading to social and financial outcomes optimization is prevented by "categorical cognition" (i.e. "*a natural tendency to view investments in terms of known categories rather than the actual outcomes they produce*" (Lee et al., 2020, p.86)). The findings show that if investments options are not labeled (e.g. "for-profit", "social enterprise", "charity"), the outcome-efficiency improves, suggesting that impact investing development requires a change in the paradigm governing investors decisions. Therefore, business and charity should not be considered as distinct fields anymore (Lee et al., 2020).

Capital owners – retail and HNW individuals but also larger assets managers such as pension funds and foundations – should control the allocation of their funds and set requirements to be sure it will support projects with positive social and environmental impact. By setting such expectations, they will incentivize companies and asset managers to strive for positive societal impact (Bouri et al., 2018).

5.5. Limited range of investment products

The impact investing solutions currently available only meet the expectations of a limited range of investors. Greater scale, liquidity, and diversification are required to reach demand's full potential and cover the preferences of the entire investor's spectrum, from retail to institutional (Bouri et al., 2018). Additionally, the limited track records of impact funds or structured products discourage wealth advisors to recommend them to their clients, further restricting the access to those investments (Ormiston, 2015). To engage mainstream investors, new actors should propose different kind of assets with different levels of performance (Höchstädter & Scheck, 2015).

Furthermore, in Trelstad's (2016) view, the range of asset classes currently proposed should be simplified to help investors discriminate between the different investment opportunities available. In traditional capital markets, it is relatively easy to compare investments based on their risk/return profile. Therefore, an equivalent solution should be found for the impact investing field.

Finally, the limited offer of investment products also restricts the investees access to capital. Their specific needs are not entirely covered by the current range of financing solutions. As for investors, additional products should be developed to cover the full spectrum of investees (Bouri et al., 2018).

5.6. Lack of supportive tools and services

There is a lack of supporting infrastructure (Bouri et al., 2018), and many of the tools used in the traditional capital markets to create, manage and analyze investments are unavailable to the impact investing sector. Mainstream intermediaries need to gain knowledge and expertise in the field. Particularly, there is a need for third party's impact rating, risk/return analysis tools and guarantee mechanisms (Bouri et al., 2018). Additionally, pricing and measurement standards need to be further developed to gain wider acceptance (Ormiston, 2015).

5.7. Lack of education and training

The lack of common knowledge about impact investing is a real problem for its development (Agrawal & Hockerts, 2019). The existing expertise is concentrated among few specialized players. The generalization of impact investing requires the emergence of new actors able to engage mainstream investors (Agrawal & Hockerts, 2019). Besides, it is necessary to educate future financial leaders to integrate societal considerations into the investment process. Too few educational programs are currently proposed (Bouri et al., 2018).

Beyond the education of mainstream investors and students on the core concept of impact investing, specific knowledge, targeting professionals, about the construction and the management of an impact investing portfolio, should be spread (Ormiston et al., 2015; Bouri et al., 2018). Additionally, investees' education is also important to build investment-ready organizations (Bouri et al., 2018). In their Roadmap for the future of impact investing, the

GIIN emphasizes on the fact that: "*Education is needed of both finance professionals (through graduate education and professional training) and business managers (through capacity building)*" (Bouri et al., 2018, p.58).

According to an Accenture survey, Millennials tend to consult various sources besides their financial advisor before making an investment decision while baby boomers are less likely to do it. This is an opportunity for the development of impact investing; open-source research and resources should be made available to share knowledge about those investments' opportunities (Emerson & Norcott, 2016).

5.8. Lack of measurement tools

The measurability of impact investments is one of the challenges highlighted the most by the literature (Clarkin & Cangioni, 2016; Guézennec & Malochet, 2013). Although several techniques for social impact measurement have been developed (e.g. IRIS, GIIRS,…), no universal standard has been generally accepted yet (Snider, 2015; Ormiston et al., 2015). The root of this challenge is subjectivity: people assess a project's social impact in a variety of ways, depending on their point of view (Mulgan, 2010). Impact measurement is essential to gain the confidence of doubtful investors (Emerson & Norcott, 2016). Jones & Turner (2014) argue that IRIS or GIIRS allow the assessment of parameters such as the number of jobs created or the salary increase, that are more outputs than outcomes. They cite a Stanford Social Innovation Review claiming that these evaluation methods give us little insights about the social benefits of such investments, which would be better evaluated by qualitative assessments (p.308).

Clarkin & Cangioni (2016) explain that social enterprises unable to accurately measure their impact have difficulties to access sources of capital. Moreover, the 2019 Annual Impact investor Survey of the GIIN indicates that the biggest challenge faced by the investors is the lack of qualifying investees (Mudaliar et al., 2019).

Beyond the need to measure the results achieved, the measurability would allow the different intermediaries to be sure to attempt to reach the same objective. A sort of 'impact fidelity' would "*allow one another to understand the original impact preferences of their sources of capital, and incentives to try to achieve them*" (Telstad, 2016, p.11).

5.9. Poor connection between the investors and the investees

The intermediation between investors and investees is not efficient (Gripne et al., 2016; Guézennec & Malochet, 2013). The actors do not know each other, so the role played by the intermediaries to connect them is important. Guézennec & Malochet (2013) claim that although the amount of capital in the market is a priori sufficient, social enterprises experience difficulties in accessing this funding. "*To grow beyond the current characterization of micro-finance, a fully coordinated marketplace will be required*" (Hebb, 2013, p.73).

5.10. Lack of transparency

Investees are usually not aware of the business elements they should share to gain credibility. This lack of information leads investors to overrate the projects' risks and diminishes their propension to invest (Guézennec & Malochet, 2013).

5.11. Poor data quality

Even though several sustainable data providers have emerged overtime (e.g. MSCI, Sustainalytics, Bloomberg), there is still a lack of a universal vendor producing comparable data in line with accepted standards (Snider, 2015).

PART II: EXPLORING THE POTENTIAL FOR BANKS AND DIGITAL TO CONTRIBUTE TO THE RESOLUTION OF KEY CHALLENGES

Chapter 1: Methodology

1.1. Qualitative research

Beyond the review of the existing literature, the purpose of this thesis is to bring new perspectives on potential solutions to address the main challenges to the development of impact investing. Therefore, we based our research on the insights of sector professionals with an up-to-the-minute awareness of the market.

As our aim was to explore new possibilities rather than to test an initial hypothesis, a qualitative approach best suited our objective. It allowed us to conduct an in-depth analysis of the viewpoints of industry experts.

However, as the role of digital in impact investing was hardly covered by the literature, we conducted some research on internet beside our interviews to nurture our analysis and spot the initiatives currently developed on the market.

1.2. Sample selection

The objective of our research being to investigate the potential for banks and digital to help overcoming the barriers to the development of impact investing, key market players, with relevant approaches, have been selected for the experience, insights and vision they could bring to the subject.

Financial institutions

Three types of banks, with distinctive customers bases have been consulted. First, it appeared essential to conduct interviews with private banks, who are key players and pioneers in offering responsible investments within the banking sector. Then, the opinion of sustainable retail banks, striving for positive social, cultural, and environmental changes and targeting conscientious customers has been examined. Finally, we selected retail banks, which started to commercialize sustainable investments only a few years ago, their huge number of customers potentially representing an opportunity for the development of the sector. Although this panel of banks gives us a great overview of the growth prospects for impact investing within the banking sector, sustainable investment strategies are specific to each institution, implying that other types of banks (e.g. commercial, investment,…) but also, other banks, part of the three categories selected for this research (i.e. private, sustainable retail and retail), could have been consulted for further insights.

Development finance institutions have a different perspective of impact investing compared to other financial institutions. Consequently, it seemed relevant to get their viewpoint on the topic.

Investment funds

Funds are undoubtedly key market players. It was important for this research to get their insights on the roles banks and digital could play. We selected a fund operating in emerging countries and a cooperative investing in developed countries. The sizes of the funds interviewed are limited; further research could explore the point of view of larger funds.

Consultancy firms

Consultants are in direct contact with investees. They are perfectly aware of their needs and the challenges they face. As field builders, it appeared judicious to question them about the role they see for the banks and digital in the impact investing sector.

Impact finance firms

As both asset managers and financial services provider, those firms have a great overview of the market. They may work with various actors such as banks. Considering their expertise in the creation of innovative financing mechanisms, we estimated they could have an interesting prospective vision on the market evolution.

Participants were chosen according to the relevance of their potential contribution to the subject, that is the reason why other types of market players have not been included in the sample.

A personalized interview request was sent to 21 persons, selectively identified for their experience, insights and vision. A representative of a private bank accepted but then turned down our interview request for confidentiality reasons, as this thesis would be publicly available. Overall, 8 specialists have been interviewed, representing a panel of 9 firms. The table below shows the names and positions of the participants as well as some key features about each company's impact investing offer.

	INTERVIEWEE	POSITION	COMPANY DESCRIPTION
PRIVATE BANK			
Degroof Petercam Asset Management	Catherine Champagne	Group Impact Investing Coordinator	- Belgian private bank - Degroof Petercam Asset Management (wholly owned subsidiary of Degroof Petercam) - EUR 39.2 billion AUM among which EUR 7 billion AUM in sustainable strategies
SUSTAINABLE RETAIL BANK			
Triodos Investment management	Peter Vierbergen	Investor Relationship Manager	- Dutch Sustainable bank - Triodos Investment Management (wholly owned subsidiary of Triodos Bank) - EUR 5 billion AUM
RETAIL BANK			
ING	Caroline De Moor	Sustainability Specialist	- Sustainable investment offering recently developed - Focused on transition - Impact investing offering restricted to private banking customers - EUR 9 billion AUM in sustainable strategies among which EUR 4.6 billion AUM in Belgium
DEVELOPMENT FINANCE			

INSTITUTION			
BIO	Jessica Schicks	Senior Investment Officer Financial Institutions	- Belgian Investment Company for Developing countries - Support the development of the private sector in emerging countries - Invest directly or indirectly in impact related SMEs, infrastructure projects, financial institutions
INVESTMENT FUNDS			
Backbone	Xavier Heude	Co-Founding Partner	- Invest in SMEs striving for a positive societal impact on local populations in emerging countries - Protect human dignity through social inclusion and economic development - Fund size: USD 10 million
ScaleUp	Olivier Van Cauwelaert	CEO	- Cooperative model - Invest in projects striving for a positive impact in developed countries
CONSULTANCY			
L+Impact	Laure Wessemius	Impact Consultant	- Support companies and supervisory board in their transition towards more impact - Specialized in governance and supervision - Advisory, structuring and strategy of impact funds
Shared Values	Olivier Van Cauwelaert	CEO	- Support companies in

			their transition towards more impact coupled with good financial performance
IMPACT FINANCE FIRM			
KOIS	François De Borchgrave	Founder and Managing Partner	- Asset management and financial services - Advisory, structuring and funds management - Create innovative financing mechanisms to turn project with positive social and environmental impact into investment propositions for public and private sector

1.3. Method

Interviews were preferred to questionnaires as our research required nuanced and detailed answered. Besides, we were interested in the breadth of opinions of our interviewees.

As our objective was to collect the analysis of practitioners on the challenges faced by the impact investing sector and to consider how growth might occur, from two specific perspectives: the roles of the banks and digital, we created a semi-direct interview guide around five major axes:

- Their approach of impact investing
- The challenges to impact investing development
- The growth prospects of impact investing
- The potential for banks to contribute to the development of impact investing
- The potential for digital to contribute to the development of impact investing

The guide has been slightly adapted for banks. In their case the topics discussed were:

- The challenges faced by the banking sector in the implementation of an impact investing offer
- The potential for banks to contribute to the development of impact investing
- The growth prospects of impact investing within the banking sector
- The potential for digital to contribute to the development of impact investing

1.4. Execution

Considering the exceptional circumstances arising from the Covid 19 crisis, the interviews were all conducted by phone or videoconference.

Every interview has been transcribed and can be found in the appendix (Appendix A1 to A8). We used codes to organize their content based on the themes discussed and report the main results in chapter 3. An analysis of the results is then developed in chapter 4.

Chapter 2: Results

2.1. Challenges to the development of impact investing

Lack of measurement standards

The challenge most frequently stated is the lack of impact measurement standards and the "impact washing" that may arise from it. One could easily pretend to make "real" impact investments when the impact produced cannot be accurately measured. An interviewee explained that a lot of impact measurement solutions exist, yet, a standard reporting tool, equivalent to the IFRS in traditional capital markets, gathering both the positive and negative impact generated by organizations and therefore, increasing the transparency about their activities is still missing. "*The moment that regulators will make it compulsory to communicate about impact, will be the moment that impact investing will take off*" (Wessemius, L. (cfr appendix 2)).

The difficulty to find qualifying investees

The two funds interviewed agreed on the difficulties in finding reliable investees. One of them, explained that many projects are early-stage and have a high probability of failure. It is challenging to find grow up businesses starting to be profitable. The other fund manager, who mainly invests in developing countries, observed that, in those regions, the creation of impact through the support of SMEs is relatively easy considering their high unemployment rate. However, the lack of local regulations leads some enterprises to run illicit operations, the challenge being then to select trustworthy investees striving for real positive impact.

Gaps between the funding available and the needs of the projects

Another barrier to impact investing development, identified as one of the biggest by the consultancy firm, is the disparity between the funding available and the needs of the recipients. Firstly, while many impact projects require private capital, a lot of investors tend to favor investments in public asset classes (e.g. public debt, listed equity) to limit their risk taking. Secondly, investees are generally early stage organizations. The risk associated with these structures does not fit the expectations of mainstream investors, who prefer follow-up investment in established businesses. Thirdly, an interviewee noted that while the achievement of most of the SDGs will take place in emerging countries, most of the funding available is located in OECD countries. Capital requirements imposed by regulators to cope with the riskiness of those investments prevent the channeling of these funds to the developing world.

Complement the local private sector

For development finance institutions, a major challenge is to work with private sector SMEs in emerging countries at market conditions. They must understand the local commercial environment to provide the same interest rates but, for instance, longer maturities or lower collaterals. Their objective is to support companies rejected by the banking system - without crowding out local players - with a view to help these companies access commercial funds over some years by proving their profitability. "*The point here is really to do something that no one else would do but in the same way that everyone else would do it*" (Schicks, J. (cfr appendix 1).

Tradeoff between financial and non-financial return

One interviewee mentioned the dilemma faced by impact investors when looking for potential investees; the more they maximize their impact - by funding a project that no one else would - the lower the probability that they will recover their funds and earn a return on them.

The lack of investment opportunities for large investors

Institutional investors, like pension funds or insurance companies, prefer to invest large amounts of capital. "*For them, analyzing a EUR 5 million investment or a EUR 100 million investment is the same effort so they focus only on the EUR 100 million investment because they have so much money to deploy*" (De Borchgrave, F. (cfr appendix 4)). However, impact funds are still too small to absorb these amounts, considering that those investors do not want their participation to exceed 10% of the fund's size. As we noted in the literature review (Chapter 4), the median level of impact firms' AUM is USD 29 million.

Lack of incentives for intermediaries

Impact investments are more complicated to manage than traditional investments; they are less liquid and difficult to analyze. Intermediaries, like banks, have therefore few incentives to include those products in their offerings, except to answer their clients' demand.

The belief that market-rate return, and non-financial impact are mutually exclusive

The varying expectations about the level of financial return achieved in impact investing will be addressed later in this thesis. Yet, some investors tend to believe that market-rate return cannot be achieved alongside non-financial impact. "*A Social or environmental impact has a cost*" (Heude, X. (cfr appendix 3)). Convincing them that is it possible was highlighted as a key challenge by one of the research participants.

Lack of public awareness

Usually, it appears that younger people are more concerned about the long-term impact on the society and the environment of their investment decisions than the elderly. However, they express themselves the least when institutional investors consult their constituency to review their strategy. For instance, most of the respondents to pension funds surveys are pre-pensioned customers who care more about the level of their pension than about the way their money in invested. "*That's why public awareness is very important, to make sure* *that people who do care – and that's normally the majority -, so the younger people, will express themselves"* (Wessemius, L. (cfr appendix 2)).

The composition of executive and supervisory boards

In line with the previous challenge, the members of executive and supervisory boards are usually pre-pensioned and, in the view of an interviewee, more reluctant to make changes towards impact than younger people, either because they are conservative, they do not know what their constituency wants, or because the regulations prevent them from realizing these changes - which is an additional challenge.

2.2. Interviewees' contribution to the development of impact investing

An interviewee argued that the mission of impact investors is not only to support companies striving for impact but also to attract new investors and commercial capital by demonstrating the attractiveness of those investments. They help building up the field by proving that it is relatively safe and that earning a return is possible. "*We will contribute to the development of impact investing because we won't remain the only few ones to do it, we will be joined over time by more impact investors and then commercial capital" (Schicks, J. (cfr appendix 1)).*

Consultants help impact driven organizations to develop and consequently act as field builders too.

Other research participants mentioned that they contribute to the development of impact investing by measuring accurately their non-financial impact to prove that "real" impact investing exists.

2.3. Attractiveness of impact investments among investors

There is an overall agreement about the increasing interest for sustainability among investors. "*Nowadays we see that everyone wants to have an impact on the world*" (Vierbergen, P. (cfr appendix 6)). The demand for sustainable investments is growing. Still, some prioritize the non-financial impact while others focus on the financial performance. Even if investors are usually enthusiastic about impact investing, some cannot afford it because of the lack of investment liquidity.

2.4. Prospects for evolution in impact investing

2.4.1. Determining factors in the development of impact investing

The following recommendations to ensure market growth have emerged from our interviews:

- Improve the tools and develop standardized methodologies for impact measurement. The comparability of funds and investments opportunities is seen as essential for further sector development.
- Educate both academics and professionals, not only on impact investing but also on the broader concept of socially responsible investment.
- Create the opportunity for people concerned about non-financial considerations to share their opinion and influence the investment strategies of institutional investors. An interviewee suggested to set up platforms to encourage them to express their views on how their money should be invested.
- Implement supporting measures for small impact funds. A research participant argued that a guarantee mechanism, by which, public authorities would insure part of the capital invested should be introduced. Additionally, public investors could, rather than co-investing in impact projects, invest directly in small funds to add credibility to their approach. "*Knowing that there is a public body by our side, which of course, analyze our governance but also invest with us and take risks in the same way that we do, often reassures investors" (Van Cauwelaert, O. (cfr appendix 5))*. Eventually, the financial support of public authorities could help smaller funds to deal with overheads.
- Set up fund-of-fund vehicles pooling the invested capital of large institutional investors and redistributing smaller amounts to impact funds to cope with their insufficient size to absorb institutional funding.
- Convince intermediaries such as banks and fund managers to sell impact investing products to their clients.
- Soften regulations regarding the riskiness of banks' products to allow the introduction of more complex investment opportunities – if related to impact - such as private equity or impact bonds.

- Explore underserved areas to identify new investment opportunities likely to attract mainstream funding in the future. Impact funds should redirect their investments away from sectors funded by impact investing over many years which have started to attract commercial capital.
- Build partnership with local institutions in emerging countries to spot qualifying investees.

2.5. The potential for banks to contribute to the development of impact investing

2.5.1. The impact investing offer of the interviewees, and their differentiating factors

Our interviews uncover different types of impact investing offerings, each bank having its own specificities. Though we observe a common tendency to target customers with a relatively high risk tolerance. All the banks interviewed propose “home-made” impact funds, and their differentiating features are discussed below.

Private bank

Degroof Petercam has built a partnership with the Swiss Asset Manager Quadia, European leader in impact investing for the management of its Regenero Impact Fund. A team of ten asset managers, dedicated to impact, advise them in the selection of qualifying investees. Their remuneration is based on the impact they generate, and the impact measurement is audited by an independent company.

They are currently setting up an impact fund in listed equities targeting millennials and investors asking for more liquid products.

Sustainable retail bank

The impact funds of Triodos Bank are accessible to its entire customer base. They offer four funds: one fixed income, two equities and one mixed income - pursuing either a defensive, a neutral or a dynamic strategy. Each fund is managed according to the same philosophy: “[We] *strive to select companies which have a positive impact on the society*” (Vierbergen, P. (cfr appendix 6)). They do not just exclude some companies from their investment universe.

Retail bank

The impact investment offerings of ING is restricted to its private banking clients. They collaborate with Funds for Good but also develop their own funds. To maximize their impact as a bank, they give money annually to the Fondation Roi Baudouin to help people better managing their wealth.

2.5.2. Challenges faced by banks when implementing an impact investing offer

The challenges faced in the implementation of an impact investing offer vary depending on the type of bank.

The private bank mentioned the lack of knowledge about impact investing among their clients. However, the recent growth of Socially Responsible Investment has popularized the notion of non-financial impact and facilitated the introduction of impact investments. The second key challenge they face is the lack of liquidity. Some of their funds require investors to lock their money for seven of ten years which prevents many customers to step in.

The sustainable retail bank mentioned its insufficient track record, although this is counterbalanced by its 25 years of experience in the market. Investors know the bank as an expert in sustainability. The second barrier they identified is the performance of impact investments compared to traditional capital markets. In some years, fossil fuel firms, for example, perform very well on the market, but are – like some other top-performing companies - excluded from impact portfolios. Beating the market is then difficult. Additionally, as previously mentioned by fund managers, the size of their funds is often too small to absorb larger investments.

The retail bank explained that its retail clients are not ready yet to sacrifice part of their financial return to have a positive impact on the society. Their impact investing offer is restricted to their private banking customers. They prefer to start educating retail clients about non-financial return with ESG investments before introducing impact funds.

2.5.3. The role of banks in the development of impact investing

Some interviews highlighted that banks have a role to play in supporting the development of impact investing. This standpoint prevails primarily among the representatives of the banking sector whereas other market players are rather pessimistic about their potential contribution.

Channel impact products to retail investors

Some interviewees from the banking sector declared that banks' role is to educate their clients. They must increase awareness around impact investments and engage new investors. By offering impact products and include it into their diversified portfolios, they will allow retail customers to step in. However, a research participant argued that the riskiness of those investments does not suit mainstream investors profile. A financial institution representative thinks that banks should guarantee part of the capital invested in small caps to lower the risks and increase investors' confidence. "*If we guarantee a certain part of the capital, that means* [investors] *will have less return*" (De Moor, C. (cfr appendix 8)). Another interviewee believes that banks could use their influence to convince their clients to step in. Customers generally trust their bank; if its strategy is to move towards more sustainability, they will follow. Eventually, one mentioned that government could have a role to play as well in granting investors a fiscal advantage for investing in sustainable products.

Engage in sustainability and finance impact projects

While a participant form the banking sector estimates that banks – as they choose to whom they grant loans- have a role to play in the financing of sustainable projects but also in divesting from harmful industries, other interviewees believes that sustainability is not the core business of banks and will never be. *"Anyway, all remains a bit reputation focus*" (Schicks, J. (cfr appendix 1)). Banks' interest in sustainable products is guided by the increasing demand of customers for responsible investments. "*Generally speaking, it is all about what clients are asking from their banks*" (Wessemius, L. (cfr appendix 2)).

The banking sector is poorly adapted to the riskiness of impact products. Financing SMEs is difficult and risky, though the impact sector is mainly composed of these firms. Regulations make it difficult for banks to offer complex products such as private equity or impact bonds.

"*An important point is that banks are part of the solution. Banks regulators are also part of the solution because today, banks are very much constrained*." (De Borchgrave, F. (cfr appendix 4)). More sophisticated investment vehicles, if linked to impact, should be authorized by regulators. Some research participants also suggested the introduction of a government guarantee, similar to the interest rate cover in traditional capital markets, to reduce the riskiness of these investments.

Encourage companies to act sustainably

According to an interviewee from the banking sector, by shifting their offerings towards more responsible products, banks will encourage companies to act sustainably. "*I believe that as a bank, by financing sustainability, we encourage companies to go in the right direction*" (De Moor, C. (cfr appendix 8)). If they push big companies like Total to change, the impact will be huge.

Increase the scale of the amounts invested

A bank representative mentioned that the large size of banks could be an advantage; their huge customers base constitutes an opportunity to channel a lot of capital to impact investing. Though, this huge structure also implies difficult and long decisions-taking processes potentially preventing to operate changes in the strategy or to introduce new products. Also, banks are heterogeneous organizations: according to the experience of a research participant, people in charge of developing the impact products are very enthusiastic while those managing the relationship with the clients tend to be more reluctant considering the risk associated with the offering of new opportunities.

2.5.4. Next steps in the development of impact investing within the banking sector

The banks interviewed identified the next steps in the development of impact investing within the banking sector.

Build an impact strategy

Banks need to analyze their activities and elaborate an impact strategy (i.e. the amount of social and environment value targeted and their impact communication).

Make their approach credible

Some market players pretend to make impact investments while they do not. This "impact washing" makes it is essential for banks to capitalize on transparency, demonstrate what they do and how they do it to make their approach credible. "*It is very important to be credible in what you do and what you say for the future of this industry*" (Champagne, C. (cfr appendix 7)).

Raise awareness among their customer base

Interviewees mentioned the need to educate and convince their clients with an adapted strategy and clear predefined messages.

2.5.5. Interviewees' expectations regarding banks' contribution in scaling up impact investing

We investigated whether banks could be a facilitator for different market players interviewed. They have reported limited interactions with banks as part of their impact investing activities. Overall, they do not expect much from the banks in the near future.

The development finance institution believes that, considering the current market state (early-stage investees, level of risk involved, below-market financial returns, etc), banks are not likely to help them, even by channeling their funds.

The representative of the fund investing in emerging countries estimates that private banks could, to a certain extent, leverage their advisory role to high net worth individuals to channel his fund to their client bases. However, "*this is a role that seems less and less relevant to me, because wealthy people tend to turn to independent management companies*" (Heude, X. (cfr appendix 3)). He argued that banks tend to be biased; they offer "home-made" products even though it is not what performs best on the market.

The consultancy firm drawn the same conclusions: banks cannot be a facilitator.

The second fund interviewed suggested, however, that banks could invest in large public funds which in turn, redistribute the capital to smaller impact funds. "*It is more realistic than trying to develop their own early stage impact fund*" (Van Cauwelaert, O. (cfr appendix 5)).

The impact investing firm shared the same standpoint; for now, banks are not really helpful. "*They communicate a lot around their ESG products rather than really doing impact investing. I must say, they do not have an easy job because they are under the constraint of MIFID rules which doesn't make it easy for them to propose private equity products, for example, to their clients.*" (De Borchgrave, F. (cfr appendix 4)).

2.6. The potential for digital to contribute to the development of impact investing

2.6.1. Digital solutions currently set up

The vast majority of the research participants do not use, offer or develop any digital solution. Some do not see the need for it, do not know how to do it or cannot afford it, while others are thinking about developing it in the future. A couple of interviewees shared a few initiatives currently used on the market. It shows that digital could intervene at different levels of the impact investing ecosystem.

Investees level

Some research participants explained they give great importance to the level of digitalization of their investees. In developing countries, it conditions their competitiveness but also the outreach of underserved populations (e.g. mobile banking in Africa). Besides, they tend to finance FinTech that will develop technological solutions for those markets as inclusion multiplies the impact generated. "*High-tech tools, related to FinTech can bring innovative solutions and help open a new market that is, for now very underserved* [e.g. agriculture, as it is a very risky market]*"* (Wessemius, L. (cfr appendix 2)).

Investors level

Others mention crowdfunding platforms as a great approach to connect investors with investees. Though, it is not sufficiently developed yet.

Within the banking sectors, some applications have been developed to allow customers to invest in a digital way.

At the asset management level, some initiatives such as the platform Medirect are emerging. It is a "*funds supermarket*" (Vierbergen, P. (cfr appendix 6)).

2.6.2. The role of digital in the development of impact investing

Even though they do not use much digital solutions at the moment, most of the interviewees acknowledged the potential role digital could play in the development of impact investing. Still, a participant argued that the growth of the sector does not necessarily require the development of new solutions but rather the shift of the whole ecosystem towards impact.

Provide information about investees

Digital could certainly, in addition to providing general information about the impact projects, improve the disclosing of financial and non-financial returns realized by investees. "*This transparency will undoubtedly lead, tomorrow, some investors to step in*" (Van Cauwelaert, O. (cfr appendix 5)).

Improve impact measurement

An interviewee suggested that easy-to-use digital solutions designed for investees could facilitate the impact measurement on the field.

Offer the possibility to invest in impact investing

People rely more and more on the internet, including for banking operations: consult transactions or make a payment. Digital could be an opportunity to invest in impact products more easily.

Raise awareness

Digital could help sharing information and educate people, even though existing solutions, like social media, already perform well.

2.6.3. Interviewees' expectations regarding digital

Our interviews highlighted several expectations regarding the development of digital solutions. Most of the research participants are convinced that digital could help but no-one knows exactly how.

There is an overall agreement around the need for a platform disclosing information about the products available, the non-financial impact generated and the riskiness of the investments.

The notion of comparability, notably in terms of non-financial impact, is frequently highlighted by the interviewees. Digital is expected to improve the transparency regarding the social and environmental impact produced by each investment, allowing investors to discriminate between opportunities. A research participant insisted on the fact that Millennials will invest in a digital way and will need this kind of tools to make investing decisions. "*Millennials have another way to look at investments, they want facts, figures, they want to compare, and this transparency is good*" (Champagne, C. (cfr appendix 7)).

Finally, an interviewee pointed out the need to develop open-source solutions for investment funds to measure and track the performance (both financial and non-financial) of the projects they finance.

Chapter 3: Analysis

3.1. Challenges to the development of impact investing

Our findings primarily show that many challenges to the development of impact investing remain to be addressed.

Additional barriers highlighted by interviewees

Overall, issues reported by our interviewees are convergent with those identified in the literature. They are though described more specifically, with concrete examples derived from their practice on the field. Additional barriers, not mentioned in scientific research, have come out in our interviews. Some of them constitute however a significant challenge to engage mainstream investors to sustain market growth. They relate to the lack of qualifying investees (impact funds), the difficulty to attain performance equivalence with mainstream investment (banks), all the more when averaged in portfolios, and the resistance to change of institutional investors' board members. Broader challenges requiring long term structural changes, regulatory or behavioral, outlined by the literature have not been reported by the interviewed practitioners.

Missing impact measurement standards

The most critical and frequently stated challenge, both in the literature and in the interviews, is the lack of impact measurement standards. While many tools have been developed, reaching a consensus on uniformly used standards is essential to increase the comparability of investment opportunities and attract new investors. Pioneers like the Rockefeller Foundation, Acumen fund and B-Lab are for long convinced of the important role the measurement of non-financial impact has to play in the legitimation of the sector. To that end, they set up the joint IRIS and GIIRS initiatives right after the term impact investing was coined. Yet, 13 years later, measurement standards are still missing. These initiatives have nevertheless been reinstated by the GIIN in IRIS+, which will hopefully bring about concrete results. Some in the industry tend to believe that the introduction of standards falls to the regulators, while others consider that it is a sector's responsibility. Beyond impeding the development of impact investing, the lack of measurement standards increases the risk of jeopardizing the credibility of this investment approach by leaving the ground to "impact washing".

Divergent views on the financial return promise

Another key area lacking consensus is the level of financial return that should and can be achieved. Some participants in our interviews consider that impact investments per se, imply to give up part of the financial return, while others argue that market-rate return can be achieved alongside a positive social or environmental impact. These findings might be related to the lack of "identity" identified as a challenge by the literature. Interestingly, however, none of our participants reported it as an obstacle to the sector development.

Challenges seen from the banks' perspective

Results from our interviews show that the challenges mostly highlighted by banks tend to differ from those outlined by other market players. Banks' main concerns relate to the performance and the liquidity of impact investments, in accordance with their primarily for-profit purpose. It is worthwhile noting though that different obstacles are identified depending on the bank types, i.e. private, retail or sustainable retail. The difficulty to find qualifying investees reported by impact fund managers has not been echoed by banks representatives, even though they also develop and manage own impact funds. An explanation can be that banks come in at a later point in the investment process as they tend to target more mature and sustainable investees with a view to secure financial returns but more importantly to comply with risk management regulations. In line with this observation, we notice that banks representatives surprisingly have not pointed out the lack of measurement tools as an issue. Further research should investigate those divergent perceptions of the challenges to impact investing development.

3.2. Market development perspectives

While remaining marginal compared to mainstream finance, impact investing is one of the fastest growing areas of the investment industry.

Although not precisely quantified, the growing interest in impact investing and rising number of prospect investors is unanimously recognized. This trend has been confirmed by participants in our research interviews as well. Yet, according to a recent survey conducted by McKinsey, "*only 16 percent of participating private banks consider sustainability as a priority driven by client demand, a desire to create positive impact on society, or regulation*" (McKinsey, 2020).

Likewise, some mainstream investors have started to direct part of their asset under management into impact investments, like the Dutch cooperative pension fund service provider PGGM or the global insurance company Zurich, who are among the cases studies featured in the WEF report (Drexler & Noble, 2013). Consumers' increasing attention to the social and environmental impact of companies will likely impulse further involvement of institutional investors into impact investing.

These trends prefigure an expansion of the investors base from niche towards mainstream investors. They will however call for the sector to eventually reach common ground on standardized measurement metrics to bring about sufficient qualifying investment opportunities to absorb new incoming capital.

3.3. The potential for banks to contribute to the development of impact investing

Banks' under-explored role

Overall, there is a lack of literature – both academic and industry based – on the role of banks in impact investing. The subject is wholly absent in scientific papers. We were just able to find two reference reports: one from the European Venture Philanthropy Association and another from the World Economic Forum.

Lack of visibility of banks' impact investing value proposition

While many financial institutions extensively communicate about their sustainable investment products, very few do the same for their impact-investing offerings. Usually, their approach, value proposition and key selling points of impact investment opportunities are not disclosed on their website. We faced the same reluctance share information on impact investing offerings when conducting this research. One private bank who had accepted to participate in our interviews, subsequently declined our request for confidentiality reasons. While we understand they operate in a highly competitive environment, the lack of information and transparency within the banking sector about impact investing does not only contribute to the low knowledge and understanding of their role, but also hinders the creation of a conducive market context.

Perception gap on banks' role between bank's representatives and niche market players

Our interviews reveal a significant disagreement among participants regarding the role of banks in the development of impact investing. While financial institution representatives envision various opportunities for banks to contribute to market growth, none of the niche players, considers that banks could be useful partners to enhance their impact investing activities and help in addressing scale-up challenges as of now. The main reasons they put forward is the lack of compatibility between impact investing current market conditions (early development stage, level of risk involved, below-market financial returns, etc.) and banks' prominent for-profit purpose, their heterogeneous structure, the decreasing relevance of their advisory value to High Net Worth Wndividuals and the risk regulatory framework in which they operate.

Areas of possible banks contribution to scale-up the market

While market players find limited value to banks' involvement in impact investing, some of their recommendations to develop the market could be best addressed by banks. Scaling up impact investing will require intermediaries with sufficient resources and infrastructure. Current sector-specialized intermediaries are small and will likely not be able to reach the size and the visibility necessary to attract mainstream capital. "*Mainstream investors will need mainstream intermediaries. Impact investment products are presently difficult to distribute because investors typically buy products from names they know, not from small specialists*" (Drexler & Noble, 2013, p.23).

Among these recommendations:

- Setting up large intermediary fund-of-fund vehicles pooling capital inflows from institutional investors to overcome the limited absorbing capacity of small-scale individual impact funds. While interviewees primarily underlined the role, public authorities should play in initiating these funds and providing guarantee for impact products, banks could also structure and operate such investment vehicles. Some mainstream investors are already making a play in impact investing. To note a few examples, Credit Suisse raised a US$ 500 million fund of funds that will invest in agricultural opportunities in Africa, JP Morgan established a Social Finance unit in 2007 that actively co-invests in impact investment funds, and UBS developed an internal position dedicated to developing impact investment products for its clients (Drexler & Noble, 2013).
- Raising awareness and knowledge among retail investors about impact investing rationale and investment opportunities.

Conditions to banks' successful involvement in impact investing

Some conditions for banks' involvement in impact investing can be derived from combining the divergent views expressed by the representatives of the banking sector and the specialized market players. The first two conditions rely on banks themselves, and the following ones on impact funds and early stage investors.

- Banks should make their value proposition and engagement in impact investment more visible and credible, not only to customers, but also to other market players. Unless banks demonstrate that the development of impact investing is a key strategic objective, their related services will continue to be perceived as marketing techniques. Banks should engage more with specialized market players.
- Impact investment offerings should be embedded in banks' vision and business strategy, shared by all divisions. As explained by one interviewee, banks are heterogeneous structures, in which departments are guided by different motivations and incentive schemes.
- Developing measurement standards enabling to benchmark investment opportunities and building a track record of financial performance are preconditions to banks' – and other mainstream investors - involvement. Banks are for-profit structures, which will only participate in scaling up impact investing if market-rate return can be achieved alongside demonstrated social and environmental value. Otherwise, impact investing offerings will remain a customer value service to High Net Worth Individuals, close to philanthropic advice. In the conclusion of its 2013 report, From the Margins to the Mainstream, the World Economic Forum announced its plan "*Over the course of the next year it will engage leading mainstream investors in an effort to analyze the competitive advantage that results from an impact investment offering*" (Drexler & Noble, 2013, p.31). We were not able to find track of a report. But the outcomes of such research would likely be highly valuable to lead institutional investors to consider the development of impact investing offerings.
- Banks' involvement will also depend on impact funds' and other market players' capacity to identify enough qualifying investees in a range of investment sectors and bring them to a scalable stage. The constraints imposed by regulators on banks risk taking limit their ability to develop an impact investment offering. Banks are therefore likely to become involved at a later stage, when investees are no longer early birds and risk has been lowered. To reduce the riskiness of these investments, public authorities could set up guarantee mechanism. In its report "15 years of impact", the EVPA points out that the European Union has already set up guarantee schemes to support banks in their impact financing or microcredit initiatives by reducing their risk taking. They notably cite the EaSI guarantee "*through which the*

European Commission via the European Investment Fund (EIF) offers guarantees to financial intermediaries, e.g. banks, providing them with a partial credit risk protection for newly originated loans to social purpose organizations or underbanked individuals." (Gianoncielli, A. et al. (2019), p.73).

3.4. The potential for digital to contribute to the development of impact investing

Existing solutions

Among our interviewees, representatives from the banking sector were the only ones to have developed digital solutions. As of now, however, their digital offerings focus primarily on enabling basic online customer transactions through smartphone applications.

Some digital tools are already available to facilitate impact investments. For instance, LITA is a platform facilitating the intermediation between the investors and the investees. A participant also mentioned Medirect, a platform offering access to various impact funds.

The Impact Finance Network released a review of 150 impact investing platforms around the world (Scholz et al., 2018). Even though the objectives pursued by those platforms are broadly similar: increase innovation, deals liquidity and improve operational effectiveness throughout the sector, their findings uncover a range of shortages:

- The data they disclose is not consistent and consequently not shareable.
- Many platforms are not replicable since they are built on tailor-made proprietary technology.
- Only a few have an Application Programming Interface, limiting the cooperation with other applications. Most of the surveyed participants however expressed their willingness to increase the collaboration between the platforms.
- Most of the platforms are not financially sustainable since the majority cannot cover its operating expenses, whereas 61,5% are funded by grants

The authors of the report advocate for a federated approach "*one would develop a distributed data model that operationalizes ownership of deal data to the venture seeking financing, increasing interoperability of deal data, and fosters the development of* *complementary business models that replace data ownership with other value-added offerings*" (Scholz et al., 2018, p.9).

Leveraging digital potential to address scale up challenges

Digital could be a real field builder. Worthwhile noting that some research participants have mentioned the need to develop digital solutions even before we had brought the subject on the table. They underlined the capacity of digital to facilitate the access to investees' information, notably regarding their financial and non-financial performances but also the investment riskiness, and the comparability of impact products. It is currently extremely difficult to benchmark and compare impact investment opportunities. Improving the transparency in the field will certainly increase investors' confidence and encourage new ones to step in.

CONCLUSION

1. Research summary

This thesis investigates the growth prospects for impact investing on the basis of a review of the existing academic literature and the insights of industry experts. Our research first considers the challenges faced by practitioners in developing the market and then explores the potential for banks and digital to contribute to the overcoming of the identified barriers.

Overall, few academic research are dedicated to impact investing. Industry reports account for most of the available publications. Beside the broadly agreed purpose of combining financial and social returns, our literature review reveals divergent views among actors on almost all aspects of impact investing, from its definition, geographical scope and legal forms of investees to risk perception, and not least financial return expectations.

This lack of identity leads many people to mix up impact investing with other close, yet different, investment approaches, such as social or socially responsible investment, microfinance, or venture philanthropy. The need for a collectively agreed sectorial definition and understanding of impact investing is further illustrated by the lack of common ground regarding the size of the market. Estimations vary from USD 226 billion AUM to USD 502 billion AUM, making it difficult to assess growth potential.

A major disagreement relates to the balance that should be achieved between the financial and the non-financial returns, separating the investors' panel into two sides: the "impact-first" and the "finance-first". In line with this controversial tradeoff, the equivalence of impact investing financial returns with those generated by traditional capital markets is also debated. Yet, according to the 2019 Annual Impact Investor Survey conducted by the Global Impact Investing Network, 66% of the respondents target risk-adjusted market rate returns.

Regarding the social and environmental impact of these investments, a range of measurement tools has been developed, but universally agreed standards allowing to compare investment opportunities are still lacking. This issue emerges as the most quoted barrier to impact investing development, both in our literature review and insiders' interviews.

Financial aspects such as investment liquidity or riskiness are hardly covered by the literature and come out of our study as a priority focus for future research. In general, authors observe a low liquidity and a relatively high level of risk, but concrete analysis or figures are missing.

Overall, the challenges to market growth identified by existing research are quite broad. Next to the issues explained above, the following ones are frequently mentioned: : the lack of policies and regulations, the inadequacy of mainstream investors' behavior and expectations, the limited range of investment products, the lack of supportive tools and services as well as the lack of education and training.

The barriers to impact investing development reported by our interviewees mirror those outlined in the literature. Though, they pointed out some additional obstacles, derived from their hands-on experience. These relate to overall portfolio performance, the limited number of qualifying investees and the resistance to change of institutional investors' boards.

The divergent views of interviewees, notably regarding the level of financial return achieved by impact investments, echo the lack of common ground identified in our literature review.

The contribution of banks to the sector development is hardly covered in academic studies. Apart from two reports form the European Venture Philanthropy Association and the World Economic Forum, the role of banks has not been considered and has never been the subject of a dedicated research. Moreover, the lack of transparency regarding banks' impact investment products hinders the creation of a fostering market context. Our findings show that while banks representatives consider that their institutions have a role to play in the development of impact investment, other actors tend to believe that currently, banks' potential contribution is quite limited. The latter see several hindrances to their involvement. First, the regulatory constraints imposed on banks' risk taking are barely compatible with the riskiness of impact investments. Second, bank's heterogeneous structure, and conflicting incentive scheme between their different divisions, in a context of prevalent business focus, makes the introduction of impact offerings difficult. Finally, interviewees also pointed out the perceived decreasing value of bank's advisory role to High Net Worth Individuals.

Even though most of the interviewees do not resort to digital yet, they unanimously recognize that new technologies will be instrumental in the development of impact investing, especially, in enhancing the comparability of investment opportunities and the disclosing of financial and non-financial information about investees.

2. Research Implications

Implications for academic researchers

This research contributes to the literature on impact investing and opens up new perspectives on two potential levers of future market growth: banks, as a key component of the financial system, and digital, as a powerful means to build the capabilities of the sector and address the challenges it faces. The insights of industry experts, who contributed to the study, on these two subjects provide a basis for future research. Our review highlights the need for the sector to develop common ground on the definition, understanding and measurement of impact investment.

Implications for banks

This research highlights the need for banks to make their engagement in impact investment more visible and credible, not only to customers, but also to other market players. Unless banks demonstrate that the development of impact investing is a key strategic objective, their related services will continue to be perceived as marketing techniques. This starts internally; the development of impact investment vehicles and services should be an integral part of the business strategy, shared by all divisions. In their external relations, banks should engage more with specialized market players. Getting the support of and working in close cooperation with industry actors will be essential if they want to play a key role in the market growth.

Our interviews uncover the lack of education on impact investing as a barrier to the sector development. Given their access to large customer bases, banks surely have a role to play in raising awareness among retail investors. This study calls for their engagement in knowledge sharing. Disclosing more information on their website about their impact investment offerings would be a first step towards that end and towards enhancing the comparability of investment opportunities.

Implications for institutional investors

The growing interest of customers in sustainability, observed by many participants, suggests that large institutional investors should be increasingly prompted by their constituency to develop sustainable investment strategies. One of our interviewees argued that institutional investors, among which banks, should anticipate that trend and consider the creation of platforms allowing customers to express their views on how their money should be invested. As she explained, younger people pay more attention to non-financial impact than older ones, though, respondents to pension funds' surveys are primarily pre-pensioned people, caring more about the amount of their pension than about their impact on the planet. Therefore, there is a need to encourage young people to share their opinions on those large investors' strategy and digital offers a way to reach them.

A recommendation emerging from our interviews was to find solutions to bridge the gap between large institutional investors and small-scale impact projects. An example of such initiative was set up in the United States. The American financial service provider Prudential Finance set up *Active Capital,* one of the largest impact funds worldwide amounting to USD 800 million AUM. "*Prudential's experience is proof that it is possible to incorporate impact strategies within the norms and constraints faced by institutional investors*" (Sathe, n.d). Their portfolio is internally divided into three categories: while 80% of the assets are invested in an *Impact Managed Portfolio,* guaranteeing a market-rate or above market return, the remaining 20% are spread between a catalytic portfolio, financing smaller and riskier projects and a philanthropic portfolio targeting below market rate returns. This hybrid approach, covering the full risk-return impact continuum, allows to finance a wide range of impact projects and demonstrates the capacity to engage institutional investors into impact investing.

Such approach has also been explored by the *Climate Investor One* initiative, developed by the Netherlands Development Finance Company FMO. It combines three investments facilities supporting renewable energy projects in low- and middle-income countries through the different stages of their development. Their approach is threefold; through a development fund, project developers, donors and Private Equity funds support early stage projects, a construction funds, pooling the funding of donors, DFIs, Private Equity funds and commercial investors backs the project evolution. Finally, the re-financing fund, allow institutional investors to refinance up to 50% long-term debts of de-risked projects, the other 50% being funded by external investors and local banks. The fund, which has reached final close at USD 850 million in June 2019, attracts banks and pension funds' investments from all over the word.

Implications for public authorities

Public authorities emerged from our research as having distinct roles to play in facilitating, encouraging, and leveraging more private sector capital in impact funds.

While institutional investors are essential to impact investing growth and market liquidity, our findings outline the gap that currently exists between the size of impact funds and the large amount of capital that these investors are willing to invest. Accordingly, our research identifies the need to create fund-of-fund vehicles to pool together the capital of institutional investors and distribute it to smaller impact funds. The creation of these intermediary funds should be endorsed by a trusted party. Public authorities come first to mind to meet that need, as they would be able to offer the guarantees required by institutional investors. Banks could also do it, possibly as operating partners of these pooled impact investment vehicles that would be backed by a public-private partnership.

As regards to interviewees' recommendation to bridge the gap between large institutional investors and fragmented small-scale impact funds or projects, we discovered meanwhile that a digital platform aiming at engaging institutional investors into impact investing has been launched in June 2020. The so-called *Impact Agora*, sponsored by Barclays, enables accelerators, fund managers, investor networks, corporates, family offices, foundations, and wealth managers to share investment opportunities, improving considerably the intermediation between institutional investors and impact projects. Their ambition is to create a community of member institutions to facilitate impact investment. This platform further illustrates the potential for digital to contribute to the development of impact investing.

Along the same lines, public authorities could contribute to reducing risk associated with impact investing, by exploring the implementation of guarantee mechanisms to secure the capital invested by impact funds, similar to the EaSI guarantee granted by the European Investment funds to banks.

As suggested by an interviewee, public authorities should finally consider the introduction of tax incentives, as a leverage to attract more private funding to public purpose projects.

Implication for banks regulators

This research underlines the possible inadequacy of current bank regulations with the risk profile of impact investing. Some of our interviewees suggested that bank regulators should explore options, results, and possible side-effects of softening restrictions, notably regarding the risk of the products banks can offer, to allow more flexibility for investments generating a social or environmental impact.

Implication for other market players

Our interviews have revealed significant divergences between banks representatives and other market players in their perception of the role of banks in the development of impact investing. This research therefore advocates for the organization of a roundtable at national level, allowing actors to share their experience and views on the potential growth and areas for improvement, with the aim of drawing recommendations and a roadmap on how they could better collaborate to jointly contribute to develop the market.

Implications for digital investments

This research makes the case for the industry to better harness the power of digital to address some of the challenges faced by the sector such as the collection and aggregation of data, the disclosing of financial performance or the assessment of the liquidity and risks. Digital could help creating tools to measure the non-financial impact generated by investees directly on the field, platforms to display standard financial and non-financial information about the projects - allowing comparability between investment opportunities and better informed decisions making-, open source solutions facilitating the performance measurement of funds and opportunities to connect people and set out online marketplaces.

3. Personal view and societal reflection

Making the case for impact investing will definitely require the sector to reach common ground on impact measurement standards. This, in our view, is the first priority to be addressed to ensure that impact investing attracts sizable investments and get a chance of becoming mainstream. Creating the conditions for market transparency, fluidity and growth, by enabling both financial and non-financial performance measurement, risk assessment, and investment opportunities comparison is a prerequisite to open the field to a broader range of investors. But, beyond, the absence of a common vision, approach and understanding of impact investing puts the credibility of the sector at stake. The "impact washing" perception resulting from it can potentially lead industry actors to doubt the reliability of other players' approach, further preventing the market development. Various initiatives have been taken to create such standards - like the IRIS+ of the GIIN - we look forward to seeing one of them succeeding. Indeed, although we acknowledge the complexity of non-financial return measurement, compared to the financial one, the inability of industry actors to agree on common evaluation standards could sound contradictory to the ultimate goal of impact investing: public interest.

We believe digital has a huge role to play in overcoming current challenges. It can be a strong accelerator of market growth, for instance, through data collection and aggregation, enhancing the comparability and transparency regarding the impact and the risks of investments, to open the field to investors with a higher risk aversion. Here, we think about mainstream, but also institutional investors, like pension funds, subjected to regulations limiting their risk taking. Finally, digital could also improve the investments liquidity by enhancing the intermediation between the investors and the investees, through platforms such as LITA.

We are convinced that impact investing is an effective approach to fund and scale up solutions to some of the most pressing social and environmental issues faced by our societies. Though, to become mainstream, a significant increase in the scale of the amounts invested is required. The flow of capital in impact investing market remains marginal compared to traditional markets. Our interviews reveal that market players consider that traditional finance, in particular the banking sector, is not suited to the nature and context of impact investing. Our questions to them are: can impact investing grow substantially outside of the traditional financial system of which banks are a key component? Are not banks key intermediaries to the investors you want to engage? Our standpoint is that building bridges towards traditional capital markets might be more effective to unlock substantial funding capital than developing a sector on its own. For instance, they acknowledge the increasing interest of retail investors for sustainability, but do not quite know how to connect to these prospects since most of them think banks cannot help.

In our opinion, increasing the amounts invested requires channeling the capital of retail and institutional investors into impact investing rather than looking for new sources of funding. This is precisely why, according to us, as major financial intermediaries, banks have a significant role to play in the development of impact investing, especially if they manage to create the pooled-impact investment vehicles previously mentioned, allowing large investors to step in. Besides, developing impact investing solutions is also in their best interest; even though it remains a differentiating strategy as of now, the injection of purpose into investment offerings will become a requirement to answer the growing demand – especially among Millennials – for sustainability and social impact.

Many of the solutions envisioned by the participants to scale the market involve the support of public funding. Though, public funding is already directed at social and environmental needs, and already supports general-purpose projects. Additionally, the Covid 19 crisis will cost billions to the states, potentially limiting their financial support over the coming years. Yet, the aim of impact investing is, according to us, to engage private funding (from both retail and institutional investors) in innovative projects and solutions addressing social and environmental challenges while generating some financial return alongside.

The literature commonly outlines that impact investing development requires long term structural changes such as the evolution of the paradigm governing investment behaviors and expectations, but what if this shift actually depends on the ability of the sector to evolve to meet investors’ expectations regarding performance measurement, risk assessment and market liquidity?

4. Limitations

The limited number of academic works on impact investing has restrained our ability to have a comprehensive overview on all the subjects we wanted to tackle (e.g. the role of the banks). At the moment, the more comprehensive reviews are produced by industry organizations which do not offer the same guarantees as scientific literature.

The lack of figures, notably regarding the size of the market, the liquidity and the risks of impact investment give us a low visibility on the current market state, and size of the issues.

The limited number of respondents to our interview request, especially within the banking sector, did not enable us to draw conclusive recommendations as to the role of banks in the development of impact investing. Besides, the reluctance of banks to share information about their impact investment offering, did not allow us to conduct a comparative review of their services from the information disclosed on their websites.

5. Further research

First, given that the topic has not yet been covered in academic research, a survey across a larger representative panel of interviewees to further analyze standpoints and draw recommendations on the role of banks and the ways to bridge gaps with other market players is needed.

Second, we believe it is essential to investigate the obstacle to the development of impact measurement standards and produce data to inform market players decisions. An increase in the scale of the impact investing market is conditional to the effective measurement of performance indicators.

Third, the lack of clear views among participants about the digital tools to be develop suggests a study to inventory the needs it could answer and how this could be done would be worthwhile.

Finally, the attractiveness of impact investments among investors should be further investigated. Interviewees tend to agree on the increasing interest of customers for sustainability but figures allowing to prospect on market growth are still lacking.

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