Understanding the Destination of Venture Philanthropy and Impact Investment

An Institutional Theory Perspective

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Abstract

The paper investigates the factors that determine the attractiveness of different social sectors for venture philanthropy and impact investment in Europe. A better understanding of investor choices and decisions is particularly important for resolving significant social problems where the interest from philanthropic investors remains limited. Accounting for investment characteristics; including the length of commitment, investment strategy and the financing instruments, the paper explores the circumstances under which a certain social project is more likely to receive philanthropic investment. The paper uses data from a unique survey of venture philanthropy and social investment organizations (VPOs) based in Europe, conducted on an annual basis by the European Venture Philanthropy Association in the period between 2011 and 2016. The preliminary results suggest that factors such as geographical focus, country of origin and organizational structure are largely irrelevant when it comes to social sector targeted. However, our study allows us to better define so-called "impact areas" that impact investors are targeting. Beyond the traditional social sectors, we develop a two-dimensional approach of combining social sector and beneficiary groups, thus contributing to a refinement of impact investing strategies. From an institutional theory perspective, our initial findings indicate that it is normative characteristics that are more likely to affect the investment decisions made by VPOs. For example, certain social issues such as children's education are perceived as more appropriate and thus an "easier sell" than others that are more controversial.

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Introduction

The paper investigates the factors that determine the attractiveness of different social sectors for venture philanthropy and impact investment in Europe. Impact investing and venture philanthropy are investment approaches that seek a societal impact combined with different degrees of financial return by investing in social enterprise. Impact investing uses innovative financing mechanisms, capacity-building support and impact measurement and management. Impact investing is also characterized by a long-term and high-engagement/hands-on approach to investees and an intentionality in producing positive and measurable societal impact at both investor and investee levels (Hehenberger, Mair & Seganti, forthcoming). From a policy perspective, the European Commission has identified access to funding as one of the key barriers to growth for social enterprises in Europe[1]. Hence, a better understanding of investor choices and decisions is particularly important for resolving significant social problems where the interest from philanthropic investors remains limited.

The paper explores data from a unique survey of venture philanthropy and impact investment organizations (VPOs) based in Europe, conducted on an annual basis by the European Venture Philanthropy Association in the period between 2011 and 2016. The survey provides data on demographics and positioning of VPOs, their sources of finance and profile of human resources, as well as their investment processes and strategies. The data set provides a unique insight into the investment strategies of European-based impact investors.

The paper is embedded within the institutional theory discourse to systematically highlight the underlying regulatory, normative and cognitive factors that are likely to affect investment decisions related to social projects. While an institutional theory perspective is increasingly used in qualitative studies on social entrepreneurship and venture creation, it often proves challenging to operationalize in quantitative empirical studies due to limited data availability, which adds further academic value to our analysis.

The preliminary results suggest that factors such as geographical focus, country of origin and organizational structure are largely irrelevant when it comes to social sector targeted. However, our study allows us to better define so-called "impact areas" that impact investors are targeting. We show that investors that target a specific beneficiary group are more likely to invest in particular social sectors. Our findings allow us to develop a two-dimensional approach of combining social sector and beneficiary groups, thus contributing to a refinement of impact investing strategies. From an institutional theory perspective, our initial findings indicate that it is normative characteristics that are more likely to affect the investment decisions made by VPOs. For example, certain social issues such as children's education are perceived as more appropriate and thus an "easier sell" than others such as human trafficking or prostitution that are more controversial, and largely absent from our results. The study contributes to the field of practice as well as to our conceptual understanding of the institutional context within which impact investing is emerging.

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[1] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52011DC0682

Background

We study a field - a constantly in-flux (Fligstein & McAdam 2012) community of "frequent and faithful" interaction organized around a common issue (Scott, 2001; Hoffman 1999). We use the term impact investing in Europe to label the field whose actors work to generate a positive social impact through investing in social enterprises – either directly or through funds and other vehicles such as social impact bonds. The main types of actors in the field are investors, including mainly financial institutions, investment funds and grant-making foundations, who deploy capital, and investees, the social enterprises and non-profit organizations that are the investment targets and who receive capital. Venture philanthropy is a practice that some consider a subset of impact investing whereas others view the practice as outside the boundaries of the field due to its primary focus on social impact over financial return, and the prevalent use of grants as a financing instrument. In this study, we use venture philanthropy and impact investing interchangeably, and refer to the organizations practicing venture philanthropy and impact investing as venture philanthropy organizations (VPOs). Impact investing in Europe is clearly an emerging field for which boundaries and defining practices and principles are yet to be established. The coexistence of new and old models has been investigated (Mair & Hehenberger, 2014), but the factors that determine the social sectors targeted by VPOs have yet to be studied.

According to institutional theory, organizations within the same social structure, such as an organizational field, that are exposed to similar institutional forces tend to resemble each other, adopting homogenous structures, practices and procedures. The main motivation for organizations to seek homogeneity is to increase their legitimacy rather than for immediate efficiency reasons (Powell & DiMaggio, 1991). Institutions are multifaceted, durable social structures, made up of symbolic elements, social activities, and material resources (Scott, 2001). They both enable and constrain organizations; those who adhere to institutional rules gain legitimacy and thus access to resources, while those who do not conform to the rules are sanctioned (Scott, 2001; Washington & Ventresca, 2004; Zuckerman, 1999). Early institutionalists stress how isomorphism leads to increased organizational homogeneity (DiMaggio and Powell, 1983). Isomorphism is a process by which organizations in the same field, that are facing the same set of environmental conditions, tend to resemble each other. DiMaggio and Powell (1983) identified three mechanisms of isomorphic change, through which institutions diffuse through an organizational field; coercive, mimetic and normative. Scott extended the analysis by classifying institutions as resting on three pillars: regulative, normative and cultural-cognitive; each with its underlying assumptions, mechanisms and indicators (Scott, 2001).

In this study, we explore whether the underlying regulatory, normative and cognitive factors are most likely to affect investment decisions related to social sector targeted by impact investors.

Methods

We compiled the data set from a survey conducted by the European Venture Philanthropy Association (EVPA). EVPA started collecting data on the European venture philanthropy and social (impact) investment sector as early as 2011, with data from 2010. Since 2011, data has been collected through an annual survey, with the exception of year 2015 – thus the data set lacks data for fiscal year 2014. The EVPA survey aims to capture the activity of Venture

Philanthropy Organizations (VPOs) based in Europe, although their investment activity may take place in other continents. As a way of illustration of survey procedure, for the latest survey conducted in 2016, the survey was first sent to a total of 119 organizations investing using the VP approach in March 2016 and closed in June of the same year. Follow-up phone calls and emails were conducted between April and June in order to reach the final response rate of 64%. The response rate for the EVPA survey is exceptionally high, reflecting the close relationship between EVPA's Knowledge Centre and its members. However, EVPA also reaches out to non-members. EVPA does not claim to have captured the entire venture philanthropy and impact investing "industry" in Europe; however they believe the sample to be highly representative (Boiardi & Gianoncelli, 2016).

The database we have constructed reflects the emerging nature of the sector and the practices and organizations involved. Hence, some of the survey questions have changed over time, and the pool of respondents has evolved. For the latest survey, out of 108 respondents, 56 respondents also completed the previous year's survey and 52 were new respondents. A total of 24 respondents completed all five of the surveys (for fiscal years 2010, 2011, 2012, 2013 and 2015). Table 1 shows response statistics from the EVPA surveys.

Table 1 Statistics on surveys conducted by EVPA

Fiscal year	*2010*	*2011*	*2012*	*2013*	*2015*
EVPA members surveyed (full members and members with VP/SI activity)	55	74	71	89	119
EVPA members completed surveys	46	53	55	72	75
EVPA member response rate	84%	72%	77%	81%	63%
Total surveys sent (including non-EVPA members)	65	102	134	140	168
Total completed surveys	50	61	75	95	108
Total response rate	77%	60%	56%	68%	64%

Considering that the first survey conducted was largely a pilot survey that included several questions that needed to be altered in subsequent surveys, we omitted 2010 data from our data analysis.

We developed a model to test which factors affect the destination of funds from VPOs. The dependent variable was the social sector invested in. The EVPA survey asked VPOs which social sectors they invested in, based on the social sector classification that follows the International Classification of Non-profit Organizations (ICNO), first introduced by Salamon and Anheier (1992), which has since become a standard in research of the non-profit sector. Table 2 provides an overview of the classification.

Table 2 The International Classification of Non-Profit Organizations

1. Culture and Recreation (culture, arts, sports, other recreation and social clubs)
2. Education (primary, secondary, higher, other)
3. Research
4. Health (hospitals, rehabilitation, nursing homes, mental health/crisis intervention)

5. Social services (emergency, relief, income support/maintenance)
6. Environment (organic, cleantech, animal protection)
7. Development and Housing (economic, social, community development, fair trade, ethical clothing, employment and training)
8. Law, Advocacy and Politics (civic/advocacy organisation, law/legal services, political orgs)
9. Philanthropic intermediaries and Voluntarism promotion
10. International (intercultural understanding/development and welfare abroad/providing relief during emergencies)
11. Religion
12. Business and Professional associations, Unions
13. Other
14. No focus

Respondents were asked to indicate the value of the investments made in the last fiscal year in one or more social sectors from the list above, or to specify other social sectors if not included in the list. Alternatively, respondents could report not having any sector focus.

Our independent variables included various dimensions of organizational structure, target beneficiary groups, number of years of experience in VP, organizational size and geographic focus.

Results

Table 3 reports descriptive data for the investment made by VPOs in the social sectors outlined above. The top three sectors are consistently Economic and social development, Education and Health, during the time period from 2011-2015, although no clear trends can be discerned.

Table 3 Venture Philanthropy investors by sector of investment (% of all investors)

Economic and social development	40.7	49.3	59.6	41.6
Education	44.1	43.7	42.7	31.0
Health	28.8	39.4	39.3	29.0
Environment	13.6	23.9	21.3	25.7
Financial inclusion	18.6	22.5	29.2	19.8
Culture & recreation	11.9	19.7	22.5	14.9
Social services	20.3	15.5	22.5	11.1
Housing	11.9	11.3	14.6	10.9
Research & VP promotion	18.6	29.6	24.7	12.9

Table 4 shows the results of our Probit models for investment activities.

Table 4 Factors of VP investment by sector

	Economic and social development		Education		Health		Environment		Financial inclusion		Social Services		Housing		Culture		Research and VP promotion	
Org structure: Company	-0.042		-0.086		0.195		0.107		0.189		-0.203	**	0.304	**	0.008		0.157	
Org structure: Company with CS	-0.061		-0.041		-0.036		0.350	**	0.293		-0.013		-0.001		0.294	*	0.243	
Org structure: Corporate foundation	0.130		0.393	*	0.037		0.008		0.046		0.259		0.019		0.262		0.736	***
Org structure: Independent Foundation	-0.438	***	-0.325	*	-0.406	**	0.539	***	0.035		-0.148		0.043		0.308	*	0.579	***
Org structure: Non profit/Charity	-0.249		-0.061		0.150		0.027		0.018		-0.134		-0.089		0.397	**	0.264	
Experience with VP (years)	-0.006		0.039	***	0.066	***	0.001		0.011		0.014	*	0.006		0.005		0.019	**
Target: Children	-0.495	***	0.499	***	0.673	***	-0.067		-0.069		0.107		-0.173	**	-0.045		0.034	
Target: Youth	0.286	*	-0.289	**	-0.375	**	-0.077		-0.228	**	-0.170	*	-0.083		0.023		0.129	
Target: Poverty and Unemployment	0.193		-0.217	*	-0.095		-0.203	***	0.097		-0.248	***	0.105	*	-0.134	*	-0.428	***
Target: Elderly	-0.444	**	-0.115		-0.222		-0.095		-0.116		-0.055		0.185		-0.124	*	0.226	
Target: Women	-0.137		-0.142		-0.384	***	0.166		0.348	***	0.141		0.009		0.017		0.010	
Target: Disabled and sickness	0.478	***	0.075		0.713	***	0.051		0.237	*	0.243	*	0.065		-0.056		-0.088	
Target: Reoffenders	0.232		0.308	*	-0.039		0.027		0.347	**	0.073		0.006		0.418	***	0.058	
Target: ethic minorities and immigrants	-0.272		0.302	*	-0.331	**	0.577	**	-0.113		0.077		-0.017		0.129		0.340	*
Organisanional size (employees)	-0.027		-0.047		-0.003		-0.019		-0.064	**	-0.069	***	-0.027		0.011		-0.017	
Investment in Europe	-0.001		0.277	**	0.295	***	0.001		0.198	***	-0.026		0.157	***	0.103	*	-0.067	
Geographic focus: International	0.299		-0.249		-0.446	**	0.066		-0.015				-0.119		-0.154		-0.197	
Geographic focus: Local	0.160		0.101		-0.297		-0.015		-0.106		0.171		-0.091		0.004		-0.043	
Geographic focus: National	0.123		-0.090		-0.496	**	0.027		-0.183		0.084		-0.150		-0.026		-0.311	**
Country of origin	YES		YES		YES		YES		YES		YES				YES		YES	
Year	YES		YES		YES		YES		YES		YES				YES		YES	
Observations	178		183.000		176		164		174		162		142		163		172	

Note: Probit models for investment activities, reporting marginal effects, so that the coefficients can be interpreted as the change in the probability that an individual venture philanthropy investor is involved in a given sector as a result of a unit change in each independent, continuous variable. For discrete explanatory variables the coefficients report the discrete change in the probability as the variable changes from zero to one.

The omitted category for Org structure is "Fund management companies and Trusts"; the omitted category for geographic focus is "no set criteria". *** significant at 1% level, ** significant at 5% level, * significant at 10% level.

In what follows, we provide a preliminary interpretation of the results.

Organizational structure matters to a certain extent. Independent foundations are less likely to invest in Socio-economic development, Education and Health, but more likely in Environment, Culture and Research & VP promotion. Companies with charitable status are more likely to invest in Environment and Culture, and Companies are more likely invest in Housing but less likely to invest in Social services.

Experience with VP activities matters too. VPOs that have existed for a longer time are more likely to invest in Education, Health, Research & VP Promotion and Social services.

In terms of the *size of the VPO*, larger organizations (in terms of staff involved) are less likely to invest in financial inclusion and social services.

Although having a certain *geographic focus* (local, national and international) appears to be irrelevant, having Europe as an investment destination is associated with more investment in Education, Health, Financial inclusion, housing and culture.

The most interesting results appear when connecting beneficiary groups with social sector focus. Indeed, our study allows us to better define so-called "impact areas" that impact investors are targeting. Beyond the traditional social sectors, our results allow us to develop a two-dimensional approach of combining social sector and beneficiary groups. The following are the main results:

- A focus on *Children* is likely to trigger investment in *Education* and *Health*, but discourages investment in *Economic and Social Development* and *Housing*. This result makes sense considering that children's welfare can be strongly enhanced through better education and health.

- A focus on *Youth* is likely to encourage investment in *Economic and Social Development*, but discourages investment in many other activities. This result may be interpreted as a focus on developing employment and a healthy economic climate as part of building a future for young people. Investors may underestimate the issues/problems facing youth in other sectors.

- A focus on *Poverty and Unemployment* is likely to encourage one type of investment only such as Housing, but discourages many others.

- A focus on the *Disabled and Sick* is likely to encourage investment in development, health, financial inclusion, and social services, as one might expect.

- A focus on *Reoffenders* is likely to encourage investment in *Education*, *Financial inclusion* and *Culture*. Connecting reoffending with a need for education and financial inclusion makes sense, but the connection with culture is less obvious.

- A focus on *Women* encourages investment in *Financial inclusion*, but discourages investment in *Health*. There is a strong link between women and microfinance, which makes up the majority of financial inclusion efforts. However, it is worrying to see that investors focusing on women are less likely to invest in Health.

- A focus on *Ethnic minorities and Immigrants* encourages investment in education, which sounds fairly expected. However, that such a focus also encourages investment in the *Environment* and *Research & VP Promotion* is not as easy to explain.

- A focus on the Elderly as a beneficiary group has largely no effect, but is likely to discourage investment in development and culture. Some further interpretation is needed.

Discussion

This study is still at a preliminary stage and the results are difficult to interpret fully without having finalized the analysis. What we can observe is that coercive mechanisms are still fairly absent from the impact investing sector. The sector is still relatively unregulated - policymakers at European and national level are only recently devising new regulation and directives for the field – an example is the European Social Entrepreneurship Fund regulation of 2013 that was designed as a voluntary label to allow investors and social enterprises to better identify European funds investing in social businesses throughout Europe.[†] Furthermore, there is little room for mimetic mechanisms as few organizations have been present long enough to have established themselves as successful. Therefore, considering the emerging nature of the impact investing field, impact investors seem to be mostly driven by normative mechanisms, conditioned by values and norms. The normative pillar (Scott, 2001) extends DiMaggio and Powell's (1983) definition of normative mechanisms to include a notion of moral obligation within a society or social system.

The preliminary results suggest that factors such as geographical focus, country of origin and organizational structure are largely irrelevant when it comes to social sector targeted. It is difficult to predict which social sector an impact investor will target based on these factors. However, the beneficiary group seems to determine to some extent the social sector that the impact investor is likely to target. The moral obligation of helping specific groups of people in need seems to drive the subsequent choice of social sector. However, the beneficiary groups themselves constitute a limiting constraint for European impact investors as they are also likely to focus on types of beneficiaries that are considered an "easy sell". It is difficult to argue that there is a need to invest in children and youth – but perhaps the additionality of impact investing should rather focus on marginalized groups that are fall outside the safety net of European welfare states, such as the victims of human trafficking and prostitution?

Furthermore, our study allows us to better define so-called "impact areas" that impact investors are targeting. We show that investors that target a specific beneficiary group are more likely to invest in particular social sectors. Our findings allow us to develop a two-dimensional approach of combining social sector and beneficiary groups, thus contributing to a refinement of impact investing strategies. We believe that our study may help VPOs (and policy makers) assess which are the areas that are underserved by current investments and that need patient capital to explore possible new solutions. The

[†] http://europa.eu/rapid/press-release_IP-17-1477_en.htm

study contributes to the field of practice as well as to our conceptual understanding of the institutional context within which impact investing is emerging.

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