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SDG 17: PARTNERSHIPS FOR THE GOALS

ACHIEVING THE SDGs THROUGH INNOVATIVE FINANCE: THE ROLE OF IMPACT INVESTMENT

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Project Overview:
This paper identifies approaches to impact investment that best optimize compatibility between impact investors and investees. Additionally, this paper seeks to identify how impact investors can best identify SDG targets that align with their priorities and available resources.

Keywords:
Impact Investment, Sustainable Development Goals (SDGs), Global Impact Investing Network (GIIN)

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Introduction

The Global Impact Investing Network (GIIN) defines impact investments as "investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return."[1] A relatively new but growing practice, impact investment shows promise as a vehicle to help drive achievement of the United Nations Sustainable Development Goals (SDGs) by 2030 through the targeted mobilization of private capital. Accordingly, an examination of impact investment is necessary to ensure its effects are truly intentional and measurable, as well as to identify areas for improvement and best practices that maximize social and environmental good. This paper explores essential elements of the investment process and the compatibility of investors and investees, using existing literature on impact investment and case studies to demonstrate how impact investments can successfully benefit any of the SDGs.

Since the early 2000s, literature on sustainable investment practices and impact investment has slowly developed. This paper builds on work that addresses the defining characteristics of impact investment and the relationship between investors and investees. To begin, this paper solidifies the theoretical framework for impact investment and the definition of impact investment from major industry leaders.[2] This literature also identifies gaps in impact investment practice.[3] Impact investment is executed by a wide spectrum of impact investors,

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[1] "What You Need to Know about Impact Investing," *The GIIN*, Accessed 16 Aug. 2020.
[2] John E. Clarkin and Carole L. Cangioni, "Impact Investing: A Primer and Review of the Literature," Enterprise Research Journal 6, no. 2 (Sep 2015): 135-173, DOI 10.1515/erj-2014-0011.; Organisation for Economic Co-operation and Development, *Social Impact Investment: Building the Evidence Base*, (Paris: OECD Publishing, 2015), http://dx.doi.org/10.1787/9789264233430-en.; Karen Wendt, *Positive Impact Investing: A sustainable bridge between strategy, innovation, change and learning* (Springer International Publishing, 2018).
[3] Jarrod Ormiston, Kylie Charlton, M. Scott Donald, and Richard G. Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," Journal of Social Entrepreneurship 6, no. 3 (2015): 352-378, DOI: 10.1080/19420676.2015.1049285.

therefore this paper pulls both from the business case for impact investment[4] and the development perspective.[5] This research also draws from analyses of the various types of impact investment and the conflicts between investors and investees.[6] Lastly, case studies from development institutions, financiers, and academics provide a space to test the thesis and compare real world examples.[7]

Through the case studies and literature analysis, this paper demonstrates that within the implementation stages, impact investors can employ innovative strategies that ensure consistent intentionality through the pursuit of any SDG. However, individual investors are better suited to pursue specific SDGs depending on compatibility factors between the particular investor and investee. Some of these factors include prioritization, financial mechanisms, specialization, and scalability. This is important because it rebuts the contention that financial-first and impact-first investments are incongruous. Furthermore, this paper identifies nuances within the investor-investee relationship that can help maximize positive impact, minimize negative externalities, and promote sustainable and inclusive development.

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[4] Antony Bugg-Levine and Jed Emerson, *Impact investing: Transforming how we make money while making a difference,* San Francisco, CA: Jossey-Bass, 2011.

[5] UNCTAD, "Chapter IV: An Action Plan for promoting private sector contributions," in *World Investment Report 2014: Investing in the SDGs: An Action Plan* (United Nations Publication, 2014).; Social Impact Investment Taskforce, *Impact Investments: The Invisible Heart of Markets* (G8, 2014).; Shelagh Whitley, Emily Darko and Grace Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets* (London: Overseas Development Institute, 2013), https://www.cbd.int/financial/privatesector/g-datasocialinvest-odi.pdf.; Cristina Garmendia and Annie Olszewski, *Impact Investing in Development Finance* (Impact Investing Policy Collaborative, 2014).; Organisation for Economic Co-operation and Development, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*, (Paris: OECD Publishing, 2019), https://doi.org/10.1787/9789264311299-en.

[6] Philip Roundy, Hunter Holzhauer and Ye Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors," Social Responsibility Journal 13, no. 3 (2017): 491–512, https://doi.org/10.1108/SRJ-08-2016-0135.; Anirudh Agrawal and Kai Hockerts, "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise," Sustainability 11, no. 15 (2019): https://doi.org/10.3390/su11154117.

[7] Cathy Clark, Jed Emerson, and Ben Thornley, *Impact Investing 2.0: The Way Forward - Insight from 12 Outstanding Funds*, (Pacific Community Ventures, Inc., 2013).; Bridges Ventures, The Parthenon Group and Global Impact Investing Network, *Investing for Impact: Case Studies Across Asset Classes* (Creative Commons, 2010).; John Simon and Julia Barmeier, *More than Money Impact Investing for Development* (The Center for Global Development, 2010).

Importance of this Research

While impact investment remains relatively young—the term was coined in 2007—in recent years it has expanded and matured significantly. In 2020, the Global Impact Investing Network (GIIN) estimated the total size of the impact investment market to be $715 billion.[8] The impact investment industry is growing steadily, and is extremely diverse.[9] Impact investors vary in size, targeted markets, and targeted rates of return and can range from institutional investors such as pension funds, insurance companies, development finance institutions, and foundations to high net worth individuals, and family offices.[10] While room for improvement remains, industry leaders such as the Global Impact Investing Network (GIIN) and Principles of Responsible Investing (PRI) have begun to establish consistent, broadly agreed-upon methods and standards for impact management, and metrics for monitoring investments. As the industry grows, these standards will become increasingly significant and will require the consensus of all participants. One way to help accomplish this convergence is by aligning impact investment with the SDGs, as the goals have already gained a broad international consensus.

Achieving the Sustainable Development Goals by 2030 requires a vast amount of capital. To reach this level of capital and help counteract risk, a broader range of investors, including institutional investors, must be involved in funding more wide-ranging development aims. In addition to capital, meeting the SDGs requires support of innovative approaches and solutions.[11] Thus, mobilizing and maximizing the power of private financing through impact investment

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[8] Dean Hand, Hannah Dithrich, Sophia Sundreji, and Noshin Nova, *2020 Annual Impact Investor Survey*, (GIIN, 2020), xiii.
[9] Hand, Dithrich, Sundreji, and Nova, *2020 Annual Impact Investor Sur*vey, xiii-xvii.; Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors."
[10] Hand, Dithrich, Sundreji, and Nova, *2020 Annual Impact Investor Sur*vey.; Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 353-355.
[11] OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*.

could be transformative. Aligning impact investment with the SDGs is one way to ensure that financing goes to areas of greatest need.[12] Already, many impact investors use the SDGs to choose social targets or measure impact. For instance, the 2020 GIIN survey found that 73% of respondents used one or more SDGs for at least one measurement and management purpose.[13] Further research informing impact investors on the process of matching SDGs with their risk and return profiles could help accelerate this trend. With less than a decade left to achieve the SDGs, it is essential to assess how effective impact investment is, as well as to identify ways for impact to be scaled.

Additionally, as with all sustainable development-oriented efforts, the practice of impact investment must be thoroughly examined to ensure that it truly produces positive impact without unintended negative consequences. Clarkin and Cangioni warn that impact investment "is not a panacea and is inappropriate for many social enterprises," so there needs to be "studies that rigorously examine the applicability and efficacy of [impact investment] initiatives."[14] A related concern is that of "impact washing," which can occur when focus is placed on the amount of financing instead of the methods and effects.[15] This insistence on the specifics and the implementation of impact investment speaks to the need for critical examination of relationships and methods within the impact investment space.

Another key concern in impact investment is confusion resulting from inconsistent terminology and ambiguous classification. Impact investment is an intentionally broad term, as a result of intentional efforts to unite a variety of actors under one big tent. Yet as impact

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[12] UNCTAD, "Chapter IV: An Action Plan for promoting private sector contributions," 136.
[13] Hand, Dithrich, Sundreji, and Nova, *2020 Annual Impact Investor Sur*vey, 44-46.
[14] Clarkin and Cangioni, "Impact Investing: A Primer and Review of the Literature," 135.
[15] OECD, *Social Impact Investment 2019.*

investment grows, Goldman and Booker noted that the lack of classification makes navigating the industry difficult for newcomers, and entrenches the industry "in an unrelenting and unproductive ideological debate about whether or not there is a trade-off between financial return and social impact."[16] Thus, it is critical that we clarify language, and enhance understanding of the impact investment.

Since the investee is the primary instrument of both value creation and value capture, the investee and its relationship with the investor merits scholarly attention.[17] Yet, there is a large gap in the literature regarding investees, especially in their most common form, the social enterprise. This gap is the result of a perceived lack of data and ambiguity around the definition of the social enterprise.[18] Some research within the impact investment space attempts to create methods of aligning investors and investees, but there is no concrete framework that can be actively applied by investors.[19]

Paper Outline

This paper begins by providing further background on impact investment, with a focus on contextualization, clarification of terminology around actors, and outlining the majors trends in the impact investment space. Following this background, a brief methodology section outlines our framework of analysis, which demonstrates the nuances of prioritization, financial mechanisms, specialization, and scalability in relation to compatibility between investors and

[16] Paula Goldman and Lauren Booker, "Parsing Impact Investing's Big Tent," Stanford Social Innovation Review, Stanford University, June 10, 2015, https://ssir.org/articles/entry/parsing_impact_investings_big_tent#.
[17] Agrawal and Hockerts, "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise," 2.; OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*.
[18] Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors."; Whitley, Darko, and Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets*.
[19] Agrawal and Hockerts, "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."

investees. Once this methodology is established, the paper presents case studies on Prudential Financial and BlueOrchard, an impact investment firm and impact investment fund manager, respectively, as well as current investees of each organization. Utilizing the framework, each case is reviewed to highlight the effective approaches of both organizations. Finally, the paper concludes that the pursuit of any SDG target through impact investment is possible, but an individual investor is better suited to pursue specific SDGs depending on compatibility factors between the investor and the relevant investee.

Background

Impact Investment in the Sustainable Development Context

Impact investments fit within the broader trend of what the Social Impact Investment Taskforce, established by the intergovernmental economic organization known as the G8, calls a "generational shift."[20] Sustainable development is seen as the shared responsibility of all members of society. Today, consumers and employees increasingly demand that businesses commit to social good, and businesses increasingly desire to produce a social and environmental benefit along with a profit. Involving the private sector in global change-making unlocks plentiful resources and funds to accelerate innovation and progress.

Private sector involvement is fundamental to the United Nations' Sustainable Development Goals (SDGs), which emphasize cooperation between actors from governments, non-governmental organizations (NGO), and the private sector.[21] When the SDGs were formulated in 2014, the World Investment Report by the UN Conference on Trade and Development (UNCTAD) noted that achieving the wide-reaching, ambitious goals could not be

[20] Social Impact Investment Taskforce, *Impact Investments: The Invisible Heart of Markets*, 1.
[21] UNCTAD, "Chapter IV: An Action Plan for promoting private sector contributions," 136.

achieved without private sector buy-in. It states, “a major escalation in the financing effort for investment in broad-based economic transformation” is necessary.[22] While public financing is essential and should not be replaced by private investment, government and NGO budgets are simply not large enough to meet the massive demand.[23] Companies are pursuing a spectrum of strategies with regard to sustainable development. As a starting point, many companies have taken a “do no harm” approach, including good governance to promote transparency and sustainable business practices that minimize negative externalities.[24] This involves what the UNCTAD calls “responsible investments” that use negative screening, integration of standards for environmental, social and governance (ESG) factors and other practices to avoid undesirable consequences.[25] Yet UNCTAD argues that doing no harm is not enough: The private sector must also make use of its abundant finances to actively invest in sustainable development.

Various approaches to mobilizing private funds for sustainable development exist, including impact investment, social or environmental bonds, and corporate sustainability efforts. What differentiates “sustainability-dedicated investments”—those targeting ESG or SDG-related themes or sectors—from merely responsible strategies is that they actively aim to produce positive effects, not just avoid negative ones.[26] One step further, impact investments harness the plentiful resources of financial markets to fund social enterprises with innovative solutions to complex problems.[27] It is important to note that while impact investment is an attractive vehicle for private financing, public and social-sector actors such as DFIs can also be impact investors.

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[22] UNCTAD, “Chapter IV: An Action Plan for promoting private sector contributions,” 136.
[23] Clarkin and Cangioni, “Impact Investing: A Primer and Review of the Literature,” 144.
[24] UNCTAD, “Chapter IV: An Action Plan for promoting private sector contributions,” 137.
[25] UNCTAD, *World Investment Report 2020*, 187-188.
[26] Ibid.; Clarkin and Cangioni, “Impact Investing: A Primer and Review of the Literature,” 138.; Ormiston, Charlton, Donald, and Seymour, “Overcoming the Challenges of Impact Investing: Insights from Leading Investors,” 353.
[27] Clarkin and Cangioni, “Impact Investing: A Primer and Review of the Literature,” 135.

Defining Impact Investment

In its 2019 report, *The Impact Imperative for Sustainable Development*, the OECD outlines the essential characteristics of impact investment as follows:

- A *social target area* or areas of need such as "inequality, poverty, education, disability, health, affordable housing, unemployment, etc."
- A *"beneficiary context"* consisting of a "population at risk by social demographics, location or income"
- A *good or service* that is "neither fully public nor fully private"
- A *delivery organization* that involves "compulsory reporting, external certification or label or legally binding constraints"
- An *investor* intent solidified in "compulsory reporting or legally binding constraints"
- An *expectation of financial return*[28]

The OECD report emphasizes not only the need for increased funding sources, but also for innovation and accountability.[29] In other words, impact investment in the SDGs should intentionally pursue more than the bare minimum of social impact. To accomplish this, investments must be inclusive, equitable, and sustainable, while including focused, localized engagement. Furthermore, impact investment should promote creation of new, innovative solutions to development problems.[30]

What further distinguishes impact investment from both traditional finance and merely responsible investment is intentionality and measurability. Impact investments are made with the express intention of producing a specific, measurable social or environmental impact.[31] This is achieved by making investments that seek not to simply capture value (gain for themselves the net financial return on investment) but to create value (produce positive externalities for society

[28] OECD. *Social Impact Investment 2019*, 26.
[29] Ibid., 20-21.
[30] Ibid.
[31] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 353.

through investment).[32] The pursuit of value creation in the form of social impact is what differentiates impact investors from traditional entrepreneurs, whereas efforts to create social value while also capturing pecuniary value, is what differentiates them from traditional philanthropists.[33]

In some cases, impact investments can actually be more efficient and effective than philanthropy because investors are, by definition, invested in the cause.[34] Whereas charitable giving ends with the giving, impact investors are incentivized to ensure that impact goals are met, since their financial earnings depend on it. A common sentiment expressed by those promoting impact investment is that "doing good and doing well are no longer seen as incompatible."[35] Serving the greater good and turning a profit do not have to be mutually exclusive. For instance, GIIN's 2020 Survey noted the difference a decade made in respondents' expectations regarding rate of return, stating that findings implied "a shift from the increasingly outdated perception of an inherent tradeoff between impact and financial performance."[36]

Yet at the same time, whether impact and financial return are mutually reinforcing is up for debate. The GIIN's 2018 Roadmap for the Future of Impact Investing specifically identified a need "to reshape the paradigm that governs investment behavior and expectations about the role of finance and society."[37] Impact investors are often designated as either financial-first or impact-first depending on whether they prioritize financial returns or social/environmental

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[32] Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors," 505.
[33] Ibid., 500-505.
[34] Social Impact Investment Taskforce, *Impact Investments: The Invisible Heart of Markets*, 1.
[35] Ibid.
[36] Hand, Dithrich, Sundreji, and Nova, *2020 Annual Impact Investor Survey*, xv.
[37] Amit Bouri, Abhilash Mudaliar, Hannah Schiff, Rachel Bass, and Hannah Dithrich, "Roadmap for the Future of Impact Investing: Reshaping Financial Markets" (GIIN, March 2018), 5.

impact, suggesting that there still exists some trade-off between the two.[38] This is not always the case, however, as Debra Schwartz argued in her call to reject the all-or-nothing view of impact investing for one that considers the flexibility and diversity of impact investment forms. While there is increasingly in-depth discussion surrounding how risk, return, and impact can interact, Schwartz noted the need to "translate this dialogue into new products, and practices."[39] This research contributes to this dialogue by exploring specific practices that can successfully navigate the complex space of impact investment.

The Impact Investment Market: Investors, Investees, and More

One dilemma within the impact investment space is the use of the term as a catch-all across asset classes, investors, investees, geographies, methodologies and scales. The process of impact investment is typically not as simple as a single investor directly funding a social enterprise. Oftentimes, it involves complex relationships within a web of stakeholders.[40] The figure below (fig. 1), produced by the OECD, clearly depicts the various actors and the relationships between them involved in the investment process. In addition to actors, the figure identifies the most common social, environmental, and economic needs targeted by impact investment: poverty, inequality, education, employment, health, climate, and affordable and clean energy. Lastly, it spotlights the key conditions that enable the market to function: social systems, regulatory and legal environment, tax laws, and financial market development.[41]

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[38] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 355-356.; Goldman and Booker, "Parsing Impact Investing's Big Tent."
[39] Debra Schwartz, "Rethinking an All-or-Nothing View of Impact Investing," MacArthur Foundation, Dec 17, 2018, https://www.macfound.org/press/perspectives/re-thinking-all-or-nothing-view-impact-investing/.
[40] Social Impact Investment Taskforce, *Impact Investments: The Invisible Heart of Markets*, 3.
[41] OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*, (Paris: OECD Publishing, 2019), 72, https://doi.org/10.1787/9789264311299-en.

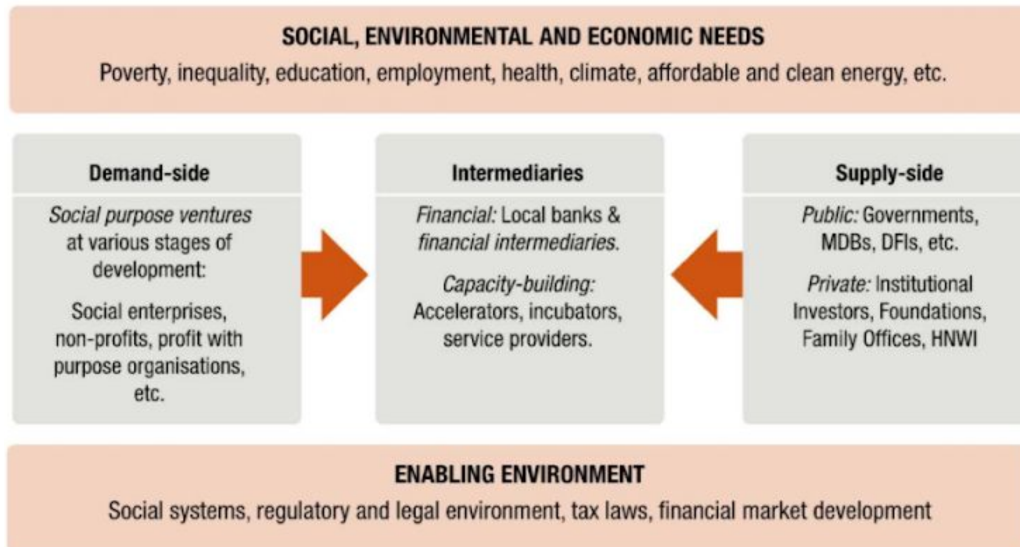

Figure 1: OECD Social Impact Investment Market Framework (OECD,2019)[42]

For the purposes of discussing impact investment in the SDGs, this paper utilizes the term "impact investor to refer to the organizations and individuals acting as the supplier of capital in impact investment, or the funders. These impact-seeking investors span from large financial institutions, pension funds, development finance institutions, and foundations to high net worth individuals and family offices.[43] Thusthis includes both public and private sources of funding. Impact investors vary in size, although the majority are of limited size. 53% of impact investors that responded to a 2020 survey by the GIIN were considered "small" for having total impact investment assets under management (AUM) less than or equal to $100 million.[44] Meanwhile, only about a quarter of respondents qualified as "large" investors, with total impact investment AUM greater than $500 million.[45]

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[42] OECD, "Social Impact Investment 2019: The Impact Imperative for Sustainable Development," Paris: OECD Publishing, 2019, 72, https://doi.org/10.1787/9789264311299-en.
[43] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 355-356.
[44] Hand, Dithrich, Sundreji, and Nova, *2020 Annual Impact Investor Survey*, 2.
[45]Ibid.

Intermediaries help to connect supply and demand through the provision of services and solutions that facilitate the investment process.[46] Intermediaries can include both financial intermediaries such as local banks and financial intermediaries and capacity-building organizations such as accelerators, incubators, and service providers.[47]

The demand side of the impact investment market comes from impact-driven investees.[48] In this paper, the recipients of capital investment are referred to as "investees," and can include intermediary banks, governments, or social ventures, ranging from social enterprises and non-profits to purpose driven for-profit organizations. Investees are the primary instrument through which impact and profit are generated.[49] The most common type of investee is often called a "social enterprise," although exact terminology and definitions vary; for instance, they are sometimes referred to as social purpose organizations.[50] The Overseas Development Institute (ODI) defines a social enterprise as "an organisation committed to social and/or environmental returns as part of its core business while seeking profit or return on investment. The legal structure of the organisation may be for-profit or non-profit, but it must aspire to financial sustainability."[51] Clarkin and Cangioni note that insufficient access to capital is one of the

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[46] UNDP: Financing Solutions for Sustainable Development. "Impact Investment," 2020. https://www.sdfinance.undp.org/content/sdfinance/en/home/solutions/impact-investment.html.
[47] OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*, 72.
[48] Social Impact Investment Taskforce, *Impact Investments: The Invisible Heart of Markets*, 3.
[49] Agrawal and Hockerts, "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."; OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*.
[50] Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors."; Shelagh Whitley, Emily Darko and Grace Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets*.; Agrawal and Hockerts, "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."; OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*.
[51] Shelagh Whitley, Emily Darko and Grace Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets*, 11.

greatest challenges facing social enterprises, a challenge that properly applied impact investment can help a social enterprise to overcome.[52]

Investment Typology

Impact investments vary greatly across a variety of characteristics, including asset class, financial instruments, stages of development, thematic area/sector, legal ownership, and geographic area. These characteristics make up the six categories used to analyze impact investment market activity in a framework created by the OECD Social Impact Investment Initiative, depicted below (fig. 2).[53] Recognizing the vast diversity of impact investments across these categories, it is important that implementation accounts for specific factors within each category.

[52] Clarkin and Cangioni, “Impact Investing: A Primer and Review of the Literature,” 136.
[53] OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*, 40.

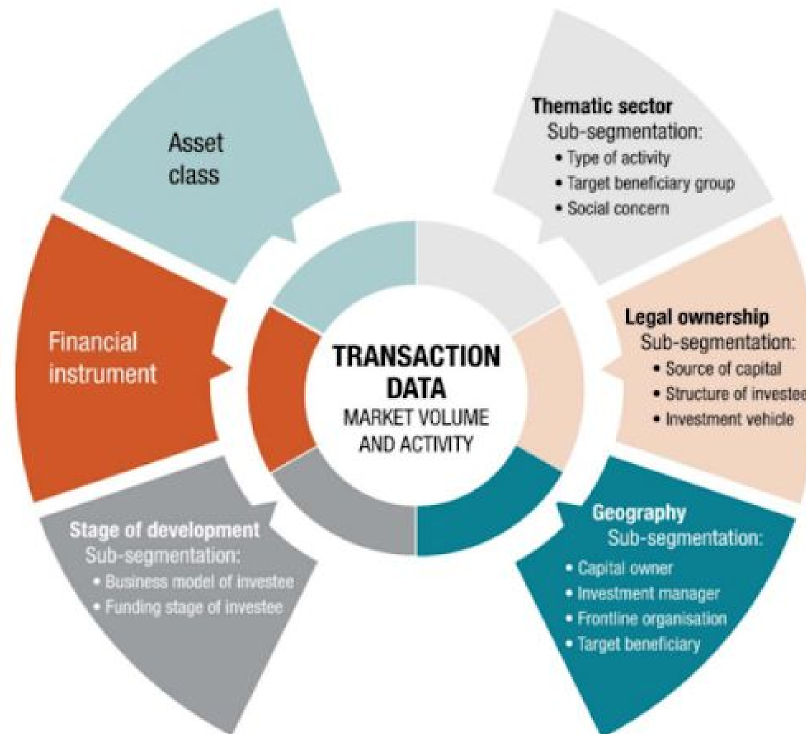

Figure 2: Reporting Framework for Sustainable Impact Investment [54]

Methodology

The methodology of this research is to use an analytical framework that clarifies what is needed to optimize investor-investee compatibility for positive impact maximization, negative externality minimization, and sustainable and inclusive development. Based on analysis of previous literature, the research framework was developed to formulate a common approach to the case studies. The goal of this framework is to demonstrate the attainability of any type of SDGs investment, depending on investor-investee compatibility determined by nuances related to prioritization, financial mechanisms, specialization, and scalability. In addition, this

[54] OECD, "Social Impact Investment 2019: The Impact Imperative for Sustainable Development," 40.

framework is used to highlight the importance of creating sustainable growth while minimizing externalities.

Prior academic studies and their methodologies for analyzing impact investment support the methodology advanced by this paper. First, the work of Agrawal and Hockerts develops the theoretical background for the interorganizational relationship between an impact investor and investee.[55] The authors emphasize the importance of commonality, in both social mission and expected returns. Additionally, they call for due diligence, sector specialization and communication while consistently measuring impact.

Metrics similar to Agrawal and Hockerts' for goals and investor-investee alignment are found throughout the literature (Roundy, Holzhauer, and Dai; Höchstädter and Scheck; Huybrechts and Nicholls; Bugg-Levine and Emerson). Roundy, Holzhauer, and Dai examined investors' criteria for investee selection and also generated foundational insights into the motivations of impact investors.[56] Similar to Agrawal and Hockerts, these authors point out that the limited amount of text discussing the different classes of investors constitutes a barrier for the growth of the field. According to the paper, consensus exists that both financial and social return are needed to qualify as an impact investment. Conflict and ambiguity remains among impact investors regarding the degree of weight that should be given to each component. Höchstädter and Scheck's research acknowledges these differences in priorities among investors and highlights that even what is classified as an impact investment can vary.[57] As this paper also

[55] Agrawal and Hockerts. "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."
[56] Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors."; Huybrechts and Nicholls, "The Role of Legitimacy in Social Enterprise-Corporate Collaboration," *Social Enterprise Journal* 9, no. 2 (2013): 130–146.
[57] Anna Katharina Höchstädter, and Barbara Scheck, "What's in a Name: An Analysis of Impact Investing Understandings by Academics and Practitioners,"*Journal of Business Ethics* 132, no. 2 (2015): 449-475, DOI:

states, ambiguity around the balance between impact and financial return in implementation limits growth within the impact investment space.[58]

Effective management of this balance is essential for successful impact investments that satisfy both the investor and investee. Investors need a financial incentive to continue investing, while investees need to achieve their professed mission of social or environmental impact to continue engaging with investors.[59] Thus, for the sake of positive impact maximization, negative externality minimization, and sustainable and inclusive development, compatibility between the investor and investee must be maximized.

Investor/Investee Compatibility Framework

As opposed to discussing specific typologies or SDGs that directly 'match' with certain types of investors, this methodology can be considered a plan to meet investment goals. Originally, this research intended to designate simple "matches" between impact investors and specific SDGs targeted by investee organizations. The reasoning was that by helping impact investors choose which SDGs to target, effective impact investment in SDGs could be expanded. However, it soon became apparent that such simplified matchmaking was not realistic, nor productive. As demonstrated by UNCTAD's diagram of the SDG investment chain (fig. 3), there is no one link between the funders and recipients of impact investment.[60] In many case studies, numerous funders of impact investment are tied together through an intermediary or advisor that

10.1007/s10551-014-2327-0. Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors,"; Antony Bugg-Levine and Jedy Emerson, *Impact Investing: Transforming How We Make Money While Making a Difference,* San Francisco, CA: Jossey-Bass, 2011.

[58] Anna Katharina Höchstädter and Barbara Scheck, "What's in a Name: An Analysis of Impact Investing Understandings by Academics and Practitioners."

[59] Agrawal and Hockerts. "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise," 2.

[60] UNCTAD, "Chapter IV: An Action Plan for promoting private sector contributions," 154.

in turn invests in SDGs targets. It takes an even further step to reach the actual recipient of funds, or where the impact occurs. Due to this web of investors, managers, and recipient organizations, funding origins can be convoluted and difficult to analyze. With these challenges in mind, this methodology provides a framework of analysis that allows for a broader understanding of the nuances within impact investment. A key component of this is the question not simply of *which* investments are made, but *how* they are made.

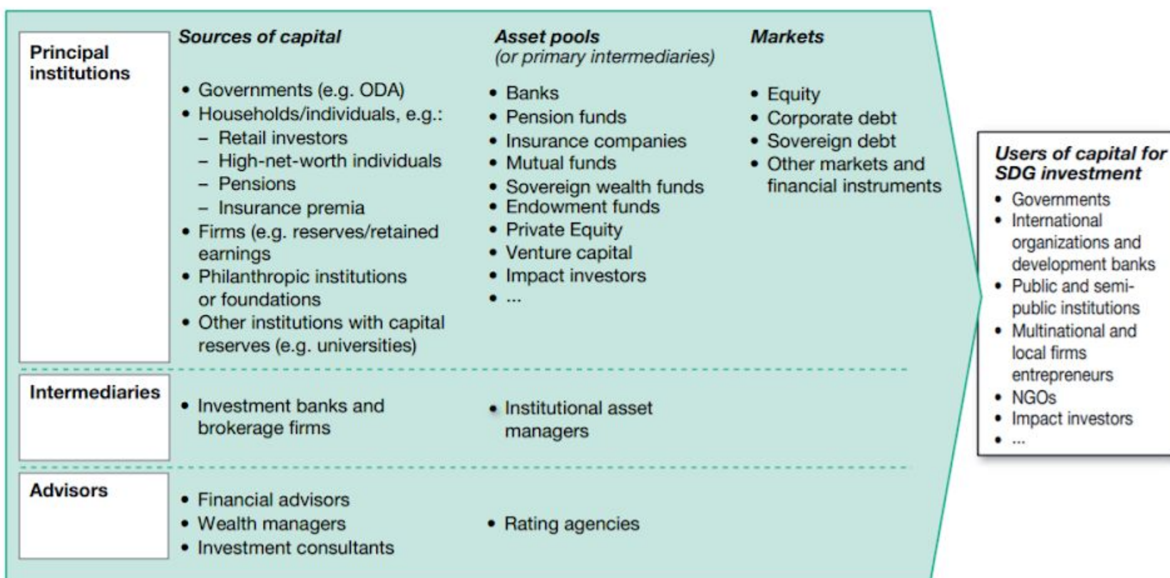

Figure 3: SDG Investment Chain and Key Actors Involved (UNCTAD, 154)[61]

This paper proposes that impact investments are successful if they produce sustainable, measurable results and minimize externalities, while also reasonably scaling value creation in both socioeconomic and fiscal outcomes. The achievement of such successful impact investment can only occur if the investor and investee work well together. Thus, this framework seeks to optimize investor-investee compatibility through consideration of four influential factors: prioritization; financial mechanisms; specialization; and scalability. These four factors in relation to investor-investee compatibility compose this paper's framework for analysis of impact

[61] UNCTAD, "Chapter IV: An Action Plan for promoting private sector contributions," 154.

investment practices. The remainder of the methodology section will describe each factor in detail, which will then in turn be applied to the case studies.

Prioritization

"Investors' expectations regarding risk, return, and impact vary according to their intentions."[62]

The first component of the framework focuses on the priorities of both the funding organizations and recipient organizations, or the investor and investee. Depending on an institutions' priorities, the minimum acceptable returns in both social impact and financial return differ vastly.[63] What determines priorities is based on both an investor's and investee's purpose and motivation for pursuing a particular impact investment. To be an impact investment, the investment must intentionally produce a social or environmental impact, as well as a financial return. Yet in implementation, investors and investees must negotiate their individual motivations, as these motives can in turn affect the weight each actor places on impact versus financial return.[64] When the two are imbalanced, prioritization of social impact or financial return can result. One of the main drivers of investors' motivations and priorities are the perceived risks of the investment. Priorities and specific goals of all organizational actors within impact investment will determine willingness to accept risk.

Looking specifically at investors, some impact investment literature categorizes them into two groups, based on prioritization and willingness to accept risk. Investors that seek to maximize impact with a baseline level of return are called impact-first investors, while those

[62] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 355.
[63] Roundy, Holzhauer, and Dai, "Finance Or Philanthropy? Exploring The Motivations and Criteria of Impact Investors," 498.
[64] Ibid.

who seek to maximize return with a baseline level of impact are called financial-first investors.[65] As Goldman and Booker pointed out, this terminology of impact-first versus financial-first reinforces the idea that there must be a trade-off, and that accordingly, investors must choose where to compromise.[66] Prevailing wisdom asserts that mainstream investors prefer financial-first investments, not wanting to sacrifice returns or take on excessive risk.[67] For instance the 2018 GIIN Annual Impact Investor Survey found that 64% of all impact investors surveyed expected non concessionary, risk-adjusted market-rate returns.[68]

Ormiston, Charlton, Donal,d and Seymour found from interviews with ten leading institutions investors and charitable foundations engaging in impact investment that the investors chose to focus on financial-first investments to minimize risk.[69] In order to attract mainstream capital in the near term, by that logic, there must be impact investment opportunities that generate market rates of return and have reasonable amounts of risk. That said, different types of investments might be appropriate for different types of investors. Some investors are willing to accept reduced returns for the sake of impact.[70] For example, a foundation focusing on *SDG 5: Gender Equality* may be more willing to take on higher-risk or accept lower-than-market-rate returns. This would be because they are motivated to invest primarily in areas such as girls' education, or reduction of legal barriers for women. Their priorities then are first to generate

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[65] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 355-356.; Goldman and Booker, "Parsing Impact Investing's Big Tent."; Karen Wendt, *Positive Impact Investing: A sustainable bridge between strategy, innovation, change and learning*, 218.
[66] Paula Goldman and Lauren Booker, "Parsing Impact Investing's Big Tent," Stanford Social Innovation Review, Stanford University, June 10, 2015, https://ssir.org/articles/entry/parsing_impact_investings_big_tent#.
[67] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 365-367.
[68] Abhilash Mudaliar, Rachel Bass, and Hannah Dithrich, *2018 Annual Impact Investor Survey* (GIIN, 2018): x.
[69] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 365-367.
[70] Ibid., 353.

social impact, and second to create financial return. Some types, locations, or themes of investment may safely provide satisfactory financial return on investment. However, some SDG areas may provide a lower return on investment, as there is perceived higher risk and lower bankability. For instance, an investor whose floor is higher for fiscal returns than for social returns (i.e. is more profit-oriented or "financial-first"), may also be more risk averse. Risk aversion connects directly to perceived feasibility of potential investment opportunities.

Even so, investors' priorities do not necessarily have to limit the thematic goals or potential investment projects they pursue. Not only that, but innovative strategies can enable investors to transcend the binary of impact or financial-first priorities. What changes with differing priorities is the types of investment mechanisms that function best for the institution, with consideration to the types of tools accessible to the investor.

In this sense, a few of the questions asked to determine prioritization include:

- What does the mission statement of the investment fund prioritize?
- What are the stated goals of impact (in regard to investor/investee relationship, development or profitability)?
- What degree of risk is acceptable for this specific project? What degree of risk is acceptable across the portfolio?

Financial Mechanisms

Investors and investees can engage with each other through the utilization of diverse financial mechanisms that best maneuver their particular priorities, circumstances, and financial position. If one thinks of impact investment as a theory for investment, financial mechanisms are the ways in which this theory can be implemented.[71] Financial mechanisms can include the

[71] *The State of Blended Finance* (Convergence, 2018), 23, [online] available at: https://www.convergence.finance/knowledge/7LEqTu0YeceaQugSWaSKSk/view [Accessed 2 Nov. 2018].

specific asset class of investments made and received, as well as the use of innovative investment management approaches or financing tools.

Impact investment is best thought of not as its own asset class, but an approach that can involve investment across a varied range of asset classes including debt, equity, and more.[72] Not only does impact investment span across asset classes, but it also varies in its rates of return, from below-market to market-rate and everything in between.[73] The type of financing required for a particular investment, be it equity or debt, depends on conditions such as the investment's sector type or activity and the social enterprise's phase of development.[74] The process of choosing the most suitable financial instrument to support a social purpose organization is called "tailored financing."[75] While there is clearly reason to tailor financing to specific investments, there is also value in maintaining a diverse portfolio that incorporates these different kinds of financing.

As mentioned previously, certain types of investments may be more conducive to achieving social-impact or financial-return. However, there exists a narrow space in which certain impact investments may achieve both high social and fiscal returns. This requires targeted financial mechanisms that take into account the financial position and priorities of the investor as well as the condition and needs of the recipient investee.

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[72] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 357.
[73] Ibid., 353.
[74] Sujata Gupta, Jochen Harnisch, Dipal Chandra Barua, Lloyd Chingambo, et. al, "Cross-cutting Investment and Finance Issues," in *Climate Change 2014: Mitigation of Climate Change. Contribution of Working Group III to the Fifth Assessment Report of the Intergovernmental Panel on Climate Change* (Cambridge and New York: Cambridge University Press, 2014).
[75] Alessia Gianoncelli and Priscilla Boiardi, *The Key Role of Tailored Financing and Hybrid Finance*, (EVPA, November 9, 2017): 6, https://evpa.eu.com/knowledge-centre/publications/financing-for-social-impact.

One financial mechanism that can achieve both high social and fiscal returns is catalytic capital. Also referred to as concessional or patient capital, it involves granting greater flexibility and assuming greater risk. Social enterprises require different levels and types of capital depending on their stage of development. The literature suggests that the area of greatest need, the initial stages of business development, is also the area in which impact investors are least willing to invest.[76] Social enterprises that are just starting out require "patient capital" that is willing to take on substantial risk and be flexible. But, most impact investors prefer to invest at later stages, once the business model is established and risk has decreased.[77] For instance, a 2013 survey by the Overseas Development Institute showed that the majority of respondents provided their support at enterprises' "Grow" stage, meaning the first two to three years of operation in which the business is building capacity and demand.[78] In order to promote the development of new social enterprises that take innovative approaches to solving complex problems, social enterprises need greater access to flexible capital in their early stages.

The second financial mechanism this paper examines is blended financing. *The State of Blended Finance 2018* describes blended finance as a mechanism that allows opportunities that may not have a sufficient risk adjusted rate of return to become more tenable for various types of commercial investors.[79] Blended finance requires a variety of organizations with different priorities to collaborate on an impact investment. impact investors who utilize blended finance

[76] Whitley, Darko, and Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets.*

[77] OECD, *Social Impact Investment 2019: The Impact Imperative for Sustainable Development*.; Social Impact Investment Taskforce, *Impact Investments: The Invisible Heart of Markets*.; Whitley, Darko, and Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets.*

[78] Whitley, Darko, and Howells, *Impact investing and beyond: Mapping support to social enterprises in emerging markets.*

[79] *The State of Blended Finance*, 2.

are important for their capacity to "bridge the gap between fully concessional and fully commercial returns."[80] Blended finance would be one example of what is considered hybrid financing, which entails "combining different types of financial instruments and different types of risk/return/impact profiles of capital providers."[81] The goal being to reduce risk for traditional capital and therefore increase funds to investees.[82]

In addition to specific financial instruments, the approach investors take in engaging with investees and managing investments matters. Agrawal and Hockerts argued that greater interaction between the investor and investee helps to ensure goal alignment and sustain the relationship between them.[83] For instance, the due diligence process offers an opportunity to "transparently communicate" expectations on issues such as scalability in advance, decreasing the chances of breakdown within the relationship. Additionally, an investor can in some cases provide additional resources to the investee, aside from capital, such as providing technical assistance to enhance the use of a loan. Through engagement with the investee social enterprise, an investor can provide valuable knowledge and business skills that the social entrepreneurs might lack.[84] The funder must answer the question of what degree of due diligence or consultation is appropriate for their specific mission and priorities. This involves the level of involvement that either investors or fund managers are willing to contribute as well as the needs of the recipient.

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[80] *The State of Blended Finance*, 2.
[81] Gianoncelli, Alessia, and Priscilla Boiardi, *The Key Role of Tailored Financing and Hybrid Finance*, 10.
[82] Ibid., 11.
[83] Agrawal and Hockerts. "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."
[84] Ibid.

The case studies section of this paper focuses on cases in which funds and investors are able to achieve both high social and fiscal returns. Financial-first investors and their inclination for immediate market-rate investment that is conventionally used can be limiting, looking at ways financial mechanisms can be used to diversify risk so that they are able to integrate more types of capital. This creates the space for greater flexibility and early stage investment as well. This is possible for them to accomplish because of tools such as Prudential's balancing of multiple distinct portfolios containing a diverse array of asset classes, or Blue Orchard's use of blended financing.

A few of the questions asked to determine appropriate financial mechanisms include:

- What are the main priorities of both the investor and investee?
- At which stage of business growth is an investee, and which stage is an investor willing to pursue?
- How much access does the investor or investee have to a range of types of partners, and can a variety of actors all contribute to the same project?
- How much involvement in a project is an investor or fund willing to have, and how much involvement does an investee want?

Specialization

The next portion of the framework involves specialization of the investor. Specialization allows for funders to meet their priorities, impact focuses, and implementation mechanisms successfully. The first degree of specialization is topical, whether that be by product type, sector, geography, thematic goals, the investee's stage of business development, or political/economic situations. This form of specialization provides the space for an investor fund to develop strong relationships that cultivate longer lasting success. Networks and collaboration are crucial for the

knowledge sharing and opportunity promotion that innovative impact investment requires.[85] Investors and investees with consistent, shared specializations are better positioned to collaborate.[86] Specialization solidifies intentionality through commitment to those relationships as well as to a topical area.

Similarly, an investment fund or investor may specialize in a type of investment mechanism. Possessing experience with specific tools and instruments, whether that be legal and policy tools or financing structures, increases the chances of long term sustainability. In addition to specializing along topical lines, having a structured and consistent management approach allows for investment funds to not only fund investees, but to create greater value. That said, this does not require that investors use only one type of investment or approach; in fact this paper discusses how combining a variety of investment types can help to diversify risk and increase value creation. Some level of focus though can be needed to develop sufficient expertise. Enhancing expertise throughout the impact investment process is crucial; some impact investors accomplish this by building in-house capacity, whereas others consult outside intermediaries.[87] In all of its forms, specialization allows for deepened sector knowledge and development of critical expertise.[88]

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[85] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 356.
[86]Agrawal and Hockerts. "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."; Ormiston, Charlton, Donald and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors."
[87] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors," 359.
[88] Agrawal and Hockerts. "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise."

.A few of the questions asked to determine appropriate specialization include:

- What is an impact investor's capacity level?
- What are the stated impact goals, and are they directed at specific themes of investment?
- If not focusing on a topical area of investment, in what other ways (management, financial) could an investor specialize?

Scalability

The final area of the framework speaks to the scalability of an investment. Scalability is important for attracting investors because many investors prefer or even require investments to be scalable. This is especially true with investors that prioritize financial returns, as larger scale generates greater profit.[89] One of the major challenges within the impact investment space is that the size of investee organizations is not compatible with the scale of investment larger funds pursue. This may be a major limiting factor for impact investment in certain SDG targets, as investees which pursue these targets are too small of a scale for certain investors. The other facet of scalability is the scalability of impact, along with financial return.[90] Morgan Simon argued in her 2018 Harvard Business Review article, "Can Impact Investing Avoid the Failures of Microfinance?", that a focus on scaling profit without equally considering impact is harmful, as demonstrated by the experience of the microfinance market. Thus, efforts to expand the impact investment market should use mechanisms that "ensure we scale impact alongside financial return."[91] Failure to do so can lead to impact-washing and deterioration of the social mission.

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[89] Agrawal and Hockerts. "Impact Investing Strategy: Managing Conflicts between Impact Investor and Investee Social Enterprise," 122-123.
[90] Ibid.
[91] Morgan Simon, "Can Impact Investing Avoid the Failures of Microfinance?" Harvard Business Review, June 8, 2018. https://hbr.org/2018/06/can-impact-investing-avoid-the-failures-of-microfinance.

A closely related concept to scalability is bankability. Bankability indicates the basket of criteria investors consider in approving a project.[92] This basket includes, among other indicators, the political and economic environment, the financial market, the legal system, the reliability of the public sector, and regulatory frameworks.[93] Combined, these factors determine whether the investment can be trusted to succeed and generate a profit. In other words, as the name suggests, projects are bankable if lenders would be willing to fund them.

A few of the questions asked around scalability include:

- Is the investee (or will they ever be) at a scale to accept larger scale investments?
- Will an investment be able to scale in both impact and financial profit? If so, will they scale at the same rate?

Case Studies

This section reviews two cases of impact investment funders, managers, and recipient organizations using innovative techniques to reach sustainable development goals that are sometimes deemed less feasible as targets for impact investment. These case studies highlight the breadth of “impact investors,” as well as variations in geography and targeted social themes.

Prudential Financial and AeroFarms

Prudential Financial is a financial institution and global investment manager that offers a variety of products and services, including life insurance, annuities, retirement-related services, mutual funds and investment management. Headquartered in Newark, New Jersey, it serves over forty countries worldwide through its subsidiaries. With $1.481 trillion in assets under management as of May 5, 2020, Prudential is the 7th-largest asset manager in the world. In the

[92] Lei Zhu and David Kim Huat Chua. “Identifying Critical Bankability Criteria for PPP Projects: The Case of China.” Advances in Civil Engineering 2018 (October 17, 2018): 1–11. https://doi.org/10.1155/2018/7860717.
[93] Ibid.

United States, it is the largest insurer of health and life combined (based on total admitted assets), the third-largest seller of individual life insurance (based on new recurring premiums) and the second-largest insurer based on net premiums written.[94]

In short, Prudential is a large, mainstream, overall traditional financial institution. The institution also prides itself on a long history of using capital for generating social good as well as profit, long before impact investment was a defined term.[95] Accordingly, Prudential is a leader in the impact investment space, formalizing its program in 1976 to identify "communities and individuals whose needs are underserved by traditional capital markets" and "craft investment solutions that generate an appropriate risk-adjusted return while driving social change."[96] Since then, Prudential invested over $2 billion worth of impact investments, including a $1 billion portfolio the company pledged in 2014 to have built by 2020.[97] Hence, its total assets under management (AUM) for impact investments is $962 million, as of March 2020.[98]

Prudential's leadership in impact investment is attributed to its strong impact management strategy and its "80/20" approach. This strategy provides a valuable blueprint for other traditional institutional investors to engage in truly impactful investment while sacrificing only a small fraction of returns.[99] This 80/20 approach means that approximately 80% of their impact investments, in the "Impact Managed Portfolio", target market-rate or greater returns.[100] The other 20% lies within Prudential's catalytic and concessional loans portfolios. Both these

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[94] "Prudential Financial Fact Sheet | Prudential." Accessed August 16, 2020. https://bit.ly/38brfyV.
[95] "Impact Investments," Prudential, Prudential Financial, Inc., Accessed August 22, 2020.
[96] Ibid.
[97] Ibid.
[98] "Impact and Responsible Investments (I&RI) Impact Management Policies (IMP) Operating Principles Disclosure Statement." Prudential, July 2020.
[99] ImpactAlpha. "Prudential's $1 Billion Portfolio of Impact Investments Offers a Blueprint for Institutional Investors," February 27, 2020.
[100] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist, accessed August 16, 2020.

portfolios entail greater flexibility through either higher preliminary risk (in the case of catalytic) or intentionally concessional loans (mainly used within the Philanthropic Portfolio).

One of the beneficiaries of this unique and innovative approach for financing is AeroFarms, a certified B corporation focusing on *SDG 2: Zero Hunger* in Newark, New Jersey. The organization is working to cultivate a new method of farming. Founded in 2004, they began as a start-up specializing in aeroponics, or indoor farming with reduced water usage and no soil. Prudential Financial worked with AeroFarms to offer professional assistance that allowed the idea to be more bankable.[101] Through the further development of the concept and procurement of funding by Prudential's Impact Investing Team, the farm was able to develop from concept to reality. Today, the farm's 100,000 square-foot home spans three facilities, and produces greens for customers in Newark and New York City.[102] AeroFarms has recently grown to 10 facilities, driven through public-private partnerships across U.S. states.[103] It was also awarded the 2018 Global SDG Award for Sustainability Leadership in *Goal 2: Zero Hunger*.[104]

Prioritization

Prudential does not fit within the binary of impact-first and financial first investors, nor does it fulfill the expectation that mainstream investors consistently prioritize returns. This is clearly exemplified by Vice President of Impact Investing, Ommeed Sathe's explanation, "we believe that the best solutions to the challenges we face today will come from investors who can

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[101] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[102] "Positive Change with Impact Investing | Prudential Financial." Accessed August 17, 2020.
[103]AeroFarms. "AeroFarms Announces Build-out of Largest Farm of Its Kind in the World in Danville, Virginia," December 11, 2019.
[104] "The Global SDG Awards Announces Winners of its 2018 Sustainability Leadership Competition," The Global SDG Awards, March 25, 2019, https://globalsdgawards.com/media-and-publications/the-global-sdg-awards-announces-winners-of-2018-sustainability-leadership-competition/.

engage across a spectrum of strategies ranging from concessionary to market-rate and have the commitment to focus on 'Impact Value Add,' not just counting impact assets under management (AUM)."[105] Prudential's first priority is "Impact Value Add", or value creation. According to Sathe, such value creation is sometimes possible "while achieving strong, market-rate or better returns" but that in other cases "investors with flexible capital will be a necessary and vital part of the ecosystem."[106] Through its 80/20 approach, Prudential takes on both investments that might be considered impact-first and others that could be called financial-first, all balanced together for the same purpose of value creation. The "steady outperformance" of the 80% within the Impact Managed Portfolio allows for greater flexibility, risk, and even concessions in the 20% percent so that neither impact nor the company's financial health have to be sacrificed.[107]

Financial Mechanisms

Within Prudential's established goal of value creation, its achievement is not about *which* investments are made, but *how* they are made. Prudential's approach can be characterized as tailored financing. According to the Vice President of its impact investment group, Ommeed Sathe, the *how* involves three key mechanisms. The first of these are "fundamentally active management strategies" that consist of five core practices: *intentional impact sourcing*, *impact diligence*, *impact value-add*, *mission safeguard*, and *impact reporting*.[108] These management strategies most importantly function to generate positive impact, but also help bolster profitability. With this in mind, Prudential believes these active management strategies must be carried out even if they do not directly improve profits; in fact, the use of these strategies can

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[105] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[106] Ibid.
[107] Ibid.
[108] Ibid.

help to promote social impact without decreasing profits either.[109] In this way, he argues, "additionality," or value creation, does not always require financial concessions.[110] Therefore, this method of investment allows Prudential to transcend the binary of financial- vs impact-first investments. However, this does not mean that Prudential never makes financial concessions. In fact, Sathe explains that Prudentials sees "great potential in layering impact management practices with concessionary capital."[111] This use of concessionary capital is accounted for Prudential's the other two impact investment mechanisms.

The second mechanism is asset class flexibility. Prudential seeks to have impact investment across asset classes, to best fit the impact sectors.[112] Their "portfolio currently includes both direct and indirect investments, debt and equity, real assets and operating businesses, mortgages, securitizations, [and] private placements" for the purposes of providing "a sensible combination of risk, return, and impact."[113] Sathe explains that this diversity within the portfolio means they can pick the specific asset class best suited for a specific investment area. For example, Prudential Financial may see strong opportunities in affordable housing equity (but less so in debt).[114]

The third element is the division of impact investments into three distinct portfolios: the Impact Managed Portfolio, which targets market-rate or greater returns; the Catalytic Portfolio, which accepts higher risk; and the Philanthropic Portfolio, which explicitly provides below-market, concessional loans to nonprofits. As mentioned previously, Prudential takes an

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[109] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[110] Ibid.
[111] Ibid.
[112] Ibid.
[113] Ibid.
[114] Ibid.

80/20 approach in which approximately 80% of its impact investments belong to the Impact Managed Portfolio, while the remaining 20% are found in either the Catalytic or Philanthropic Portfolios.[115] While a different ratio might be more appropriate for other investors, in Prudential's case the 80/20 ratio ensures strong returns from the Impact Managed Portfolio compensate increased risk and concessionality in the other two portfolios. This flexibility is what makes space for innovative investments that generate value creation, as demonstrated by the experience of the Catalytic Portfolio.

Prudential's Catalytic Portfolio takes on additional risk and includes smaller investments of one to five million, with the understanding that the portfolio will have more volatile returns.[116] This type of investment tool broadly is called catalytic development, due to its R&D value and ability to jumpstart opportunities that may still be too risky or underprepared for market-rate impact investments. In general, Prudential's Catalytic Portfolio tended to be around 150 to 250 basis points lower than that of similar assets in the Impact Managed Portfolio.[117] This reduction in basis points refers to a range of concessionary outcomes of individual investments, from returns that are slightly lower than market-rate to a loss of all capital. Prudential's management team however finds that "in exchange for this concession, we have received … dramatic examples of social impact and created pipelines … which will typically lead to larger future opportunities, that can be included in the Impact Managed Portfolio."[118]

To contextualize, Naturevest falls within Prudential's Catalytic Portfolio. Based in Washington, DC, the organization's goal was to address stormwater runoff through a

[115] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[116] Ibid.
[117] Ibid.
[118] Ibid.

cap-and-trade marketplace. As stated by Prudential's Impact Investing team, "our initial investment was high risk since there was not yet an established market price for stormwater credits. After using our capital to initiate the first major stormwater runoff mitigation project, the market for credits has become far more predictable and subsequent investments will be made through our Impact Managed Portfolio."[119]

Similar to Naturevest, Aerofarms utilized an initial investment and advice from Prudential and other early stage investor Goldman Sachs to jumpstart their enterprise.[120] Prudential utilized their 80/20 approach, which allows for 20% of impact investments to fall within the catalytic or concessional space. In this example, Prudential served in a catalytic role, offering advice that allowed AeroFarms to become market ready for other investors. Today, AeroFarms has over 10 financial partners, ranging from those who took a concessional/catalytic approach, to companies seeking market-rate returns of their impact investments.[121] What is also important to note is the investor and investee relationship, drawn together through a common goal: commitment to making a difference in their home community of Newark, New Jersey.[122] The alignment of goals and experience in catalytic development created an environment where the relationship was well positioned to thrive.

Specialization

Prudential specializes through their distinct, in-house team of investing professionals, the Impact & Responsible Investments team (IRI) dedicated exclusively to Impact Investments at

[119] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[120] AeroFarms. "AeroFarms Is on a Mission to Transform Agriculture." Accessed August 5, 2020. https://aerofarms.com/.
[121] Ibid.
[122] Devin Thorpe, "Prudential Working To Double Impact Investing Portfolio Focuses On Newark" Forbes, accessed August 16, 2020.

Prudential.[123] This senior team has "deep experience and an ability to constructively engage with investees."[124] Specialization in impact investment ensures strong expertise and focus; to narrow the specialization further, the IRI team focuses on Prudential's specific impact themes and goals, which are a portion of their impact framework. Impact objectives are "designated ex ante rather than ex post and reflect an intentional approach to finding and creating impact as opposed to measuring the impact of pre-existing investments".[125] These themes are maintained over several years, allowing for consistency and specialization but, more precisely, demonstrating a commitment to patient capital.[126]

Prudential also specializes in the sense that it employs a narrow definition of impact investment. Ommeed Sathe states that Prudential believes "the key purpose of impact investment is to solve the social and environmental problems that aren't already being effectively addressed by government, philanthropy or traditional investors."[127] He acknowledges that the private sector role in problem-solving and development is not to replace government or philanthropy (after all, some areas of need simply cannot and/or should not generate a profit). Therefore, Prudential's impact investment efforts focus on communities underserved by traditional markets to create new space within markets.[128]

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[123] "Impact and Responsible Investments (I&RI) Impact Management Policies (IMP) Operating Principles Disclosure Statement." Prudential, July 2020.
[124] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[125] "Impact and Responsible Investments (I&RI) Impact Management Policies (IMP) Operating Principles Disclosure Statement." Prudential, July 2020.
[126] Ibid.
[127] Ommeed Sathe, "Active Capital: Implementing a Billion Dollar Mandate," The Economist.
[128] Ibid.

Scalability

While Prudential's experience suggests most impact-oriented investments can become profitable in the long-run, Sathe recognizes that “scalable for-profit businesses may not be the right vector to derive” impacts which are not conducive to long-term financial performance.[129] This means that the impact investor should specialize within the sweet spot where impact can be driven, without being compromised by for-profit vehicles. Prudential also urges its institutional peers to “avoid the trap of mistaking scale for impact.”[130] This nuanced understanding of value creation acknowledges that scaling does not necessarily equate greater value creation; sometimes impact value-add exists best on a smaller, more local scale. On the other hand, Prudential’s use of active management strategies and catalytic capital is what enables many of its investments to be scaled up. Therefore, scalability is not simply a static condition of an investee, but is influenced by the mechanisms used to scale a specific social enterprise.

Blue Orchard’s Regional Education Finance Fund for Africa

BlueOrchard lies on the other end of the impact investment spectrum from Prudential Financial. Originating in 2001 as a small advisor to a microfinance fund, BlueOrchard has emerged as a large impact investment manager of numerous funds in frontier and emerging markets.[131] Primarily notable in the microfinance field, BlueOrchard was the first commercial manager of microfinance debt investment.[132] The organization operated as a Microfinance Investment Vehicle, connecting financial markets and microfinance institutions.[133] Today, the

[129] Ommeed Sathe, “Active Capital: Implementing a Billion Dollar Mandate,” The Economist.
[130] Ibid.
[131] BlueOrchard. “BlueOrchard Vision and Mission.” Accessed August 16, 2020.
[132] Henry Oguine, “A Sustainability Case Study: BlueOrchard,” Business School Lausanne, n.d, 4, https://www.bsl-lausanne.ch/wp-content/uploads/2017/01/BlueOrchard-Case-Study-Final-Version.pdf.
[133] Ibid., 7.

organization leads in impact investment management for Development Finance Institutions, tracking investments of 6.8 billion USD over their 19 year history. As an industry leader, they've become a convener of public-private partnerships, intentionally implementing projects that create value through both public and private funds.[134] These projects span topical areas from infrastructure and microfinance to climate and education. Though touching on many of the SDGs, BlueOrchard, like many others within the impact investment space, finds commonality through their specific impact themes and prioritization.They focus on thirteen of the SDGs through the pursuit of four core impact areas: governance and capacity building, financial inclusion, education, and climate.[135]

Across BlueOrchard's portfolio, the organization functions as a connector between financial markets and local institutions.[136] This remains the case for the Regional Education Finance Fund for Africa (REFFA), which was formed in 2014 as a thematic fund focusing on education in Africa. REFFA recognized the growing demand for access to schools, which put physical and financial strains on educational systems in African countries. The fund seeks to provide financial services and to supply technical assistance to financial institutions providing education finance products.[137] This is implemented via nine financial intermediaries across eight African countries, in which BlueOrchard takes senior debt positions.[138] In turn these intermediaries fund educational organizations that need capital to achieve their social enterprise. In implementation, this may be a loan for infrastructure improvements (school expansion) or a medium-term loan that permits an educational fee to be dispersed throughout the year, as

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[134] Henry Oguine, "A Sustainability Case Study: BlueOrchard," 34.
[135] BlueOrchard, "BlueOrchard Vision and Mission."
[136] Henry Oguine, "A Sustainability Case Study: BlueOrchard," 7.
[137] REFFA Fund, "REFFA Fund: Education and Finance," accessed August 16, 2020.
[138] "Regional Education Finance Fund For Africa (REFFA) Investor Update," BlueOrchard, March 31, 2020.

demonstrated in *Figure 4*.[139] The fund now reaches nearly 150,000 students and 90 educational providers.

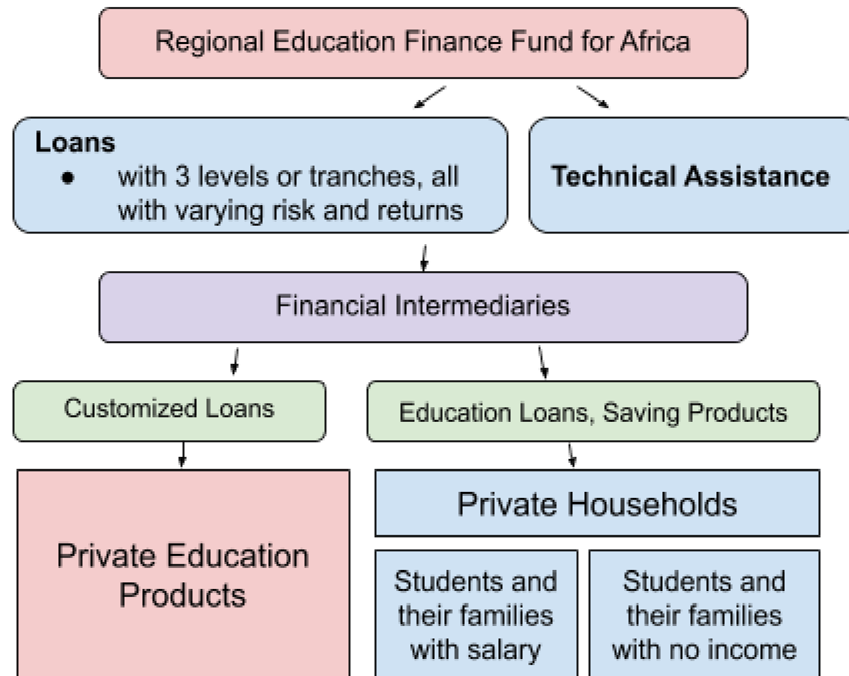

Figure 4: Overview of REFFA Implementation Structure. Made by the Authors.[140]

An important component in the chain of impact investment is the financier of the project. BlueOrchard is the fund manager and technical assistance coordinator, however REFFA is funded by the German Federal Ministry for Economic Cooperation and Development (BMZ) and KfW Development Bank. KfW Development Bank is a Development Finance Institution, which are crucial players within the space, as they manage nearly 27% of all impact investment (according to the GIIN 2018 respondents).[141] In just 2017 alone, DFIs contributed $87 billion in annual investments across their portfolios.[142] Development Finance Institutions tend to prioritize

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[139] REFFA Fund, "REFFA Fund: Financial Institutions," accessed August 16, 2020.
[140] "How Financial Institutions can Access Capital for Education Lending," Opportunity International and BlueOrchard, June 19, 2019, https://edufinance.org/content/edufinance/Ghost%20conference%20page/Session%208.pdf
[141] "Sizing the Impact Investing Market," GIIN.
[142] Daniel Runde, and Aaron Milner, "Development Finance Institutions: Plateaued Growth, Increasing Need," Center for Strategic and International Studies, February 13, 2019.

social impact within impact investment, as their broad motives are to improve economic conditions for developing countries. Conventionally within the international development arena, DFIs are major funders of grants, concessional loans and other forms of financing within Sustainable Development Goals, especially for targets that might be deemed less feasible for commercial investors due to increased risk or lower profitability. As witnessed through this example, the initial investments made by DFIs have the potential to spawn future impact investments by more commercial actors, or create environments for growth.

The German Federal Ministry for Economic Cooperation and Development (BMZ) and KfW Development Bank's initial investment in the Regional Finance Fund for Africa created the opportunity for a blended investment structure, in which public funding sources and Development Finance Institutions offer concessional loans. This generated a more feasible investment environment for private sector investors, who were able to achieve market-rate returns in what is known as the senior tranche.[143] As other blended finance situations, the organizations are able to achieve profit for mezzanine and senior tranches of investment.[144] This is demonstrated through BlueOrchard's track record, in which the fund manager has consistently met and actually outperformed benchmarks. In a 2015 study, it was shown that the fund returned an annualized 4.29% since inception.[145]

Prioritization

BlueOrchard as an organization has evolved in its priorities and purpose. The company's original purpose was around addressing issues such as "poverty, unemployment, and financial

[143] REFFA Fund, "REFFA Fund: Education and Finance," accessed August 16, 2020.
[144] Lei Zhu and David Kim Huat Chua. "Identifying Critical Bankability Criteria for PPP Projects: The Case of China."
[145] Henry Oguine, "A Sustainability Case Study: BlueOrchard," Business School Lausanne, n.d, 14.

exclusion using the tools of microfinance."[146] Their beginning was therefore focused on social-impact, but over the next 15 years, BlueOrchard turned to products that could also mobilize private capital in a profitable manner. This successful business model drew in further investment partners whom they replicated and scaled funds with. After 2006, BlueOrchard began to collaborate with governments and Development Finance Institutions. Between these organizations and BlueOrchard, there was strong alignment between their stated goals of value creation and improving socioeconomic conditions.

The involvement of DFIs, government agencies, and other philanthropic agencies opened up the opportunity to pursue innovative products, such as a blended finance approach with varying tranches (or levels) of returns. These innovative funds were able to then have investors who may be considered financial-first impact investors. In the case of the Blue Orchard Microfinance Fund, it provided a return of over 68% in its 10 year period and an annualized return of 6% USD.[147] The fund manager was able to produce such financial returns as in this case through using this blended finance approach. Like Prudential, this allowed BlueOrchard's funds to include both market-rate returns and concessional returns, used in tandem to increase the level of investment and therefore value creation.

Financial Mechanisms

BlueOrchard was driven by 'pull' factors and gaps in loan options for education in the direction of blended finance. BlueOrchard defines this as "the strategic use of development finance for the mobilization of additional finance towards sustainable development in developing

[146] Henry Oguine, "A Sustainability Case Study: BlueOrchard," 7.
[147] *Investing For Impact: Case Studies Across Asset Classes*, 18.

countries."[148] The organization's expansive network of Development Finance Institutions, international organizations, and private investors provides a diverse mix of capital sources, which creates the space for this mechanism.

In the case of the Regional Education Finance Fund for Africa, BlueOrchard utilized this blended product to achieve its main socially-focused goal. Through public private partnerships, bilateral donors played a catalytic role by investing at concessional terms and taking on the highest degree of risk. This method generated space for a variety of risk-return profiles, and allowed investors whose priorities may be financial-first to still invest. Private investors, such as pension funds and family foundations, were encouraged by the investments of public investors and DFIs, such as the German Development Bank and the CDC Group (UK's DFI).[149] Through this mix of priorities and funding sources, a fund of 100 million USD for a conventionally less financial-feasible SDG of education was possible.

This mechanism is conventionally known as subordination for a fund. Subordination entails using a special purpose vehicle in which any cash flow created would first be used to pay institutional investors within the highest level of security (lowest risk bracket), otherwise known as the senior tranche.[150] Development Finance Institutions and governmental organizations in turn may take the first loss in mezzanine or junior tranche positions, in which they accept below market rate or minimal return on their investment.

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[148] "When Blended Finance Meets Impact Investing – OECD Showcases BlueOrchard Managed MIFA-Fund," BlueOrchard, February 19, 2018.
[149] REFFA Fund, "REFFA Fund: Education and Finance," accessed August 16, 2020, https://www.reffa.org/education-and-finance.
[150] OECD, ed. Making Blended Finance Work for the Sustainable Development Goals, 86.

For REFFA, subordination is possible through the German Development Bank. It serves as an extra layer of “cushion” to prevent losses from institutional or private investors involved.[151] Subordination may best be visualized as a waterfall.[152] Institutional or private investors receive their returns first, and then whatever is left trickles down to the next level (in this case first the mezzanine level of investors like the CDC Group, and then lastly the German Development Bank in the junior tranche.[153] This process decouples the notion that there must be high risk for any return in developing economy context, and again draws in further capital.

Specialization

BlueOrchard’s commitment to inclusive finance, innovative financial mechanisms, and public-private partnerships has allowed them to specialize in blended financing for microfinance. BlueOrchard has worked for the past 19 years with microfinance institutions, allowing them to provide hybrid finance to meet financial needs and to understand the technical assistance needs of these institutions. One of their first initiatives, BlueOrchard Microfinance Securities (BOMS1), was founded in 2004 and provided loans to retail microlenders.[154] Utilizing tranches similar to those discussed earlier, BlueOrchard offered a hybrid finance model while offering investees technical assistance as well. In this sense, specialization in the microfinance space, permitted BlueOrchard to further scale impact and value creation to other funds in their portfolio. Using a similar model, BlueOrchard expanded to other thematic areas. This includes the Regional Education Finance Fund for Africa, in which BlueOrchard is a manager.

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[151] OECD, ed. Making Blended Finance Work for the Sustainable Development Goals, 124.
[152] Ibid.
[153] REFFA Fund, “REFFA Fund: Education and Finance,” accessed August 16, 2020.
[154] Kenny Kline, “Know a Microfinance Fund: BlueOrchard Microfinance Securities (BOMS 1),” MicroCapital, December 2, 2009.

BlueOrchard also has specialized through their impact themes. The fund manager focuses on financial inclusion, education, climate, governance and capacity building. As mentioned before, Blue Orchard first specialized in financial inclusion, beginning as solely a management fund for microfinance. Using this background, BlueOrchard began to look to apply financial inclusion in other SDG target areas, such as SDG 4: Education in the Regional Education Finance Fund for Africa and SDG 13: Climate Action in the InsuResilience Investment Fund (IIF). Both funds lend to financial institutions which provide education financial products and climate insurance respectively.[155] Their success in microfinance specialization is in part what allowed for further scale of other impact theme investment funds.

Scalability

BlueOrchard valued the development of not only funds that provided necessary financial assistance to areas which lacked capital, but also worked to ensure that impact was able to be scaled alongside financial return. Within the realm of investment in developing countries, there have been countless instances of financial scaling without impact scaling.[156]

To counter this, BlueOrchard developed a proprietary tool, Social Performance Impact Reporting and Intelligence Tool (SPIRIT) which they evaluate ESGs and impact (value creation).[157] This model is used to evaluate possible investees through analysis of metrics around employee protection, environmental issues, and over-indebtedness.[158] Through working directly with financial institutions receiving investments and consistently monitoring through SPIRIT,

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[155] InsuResilience Investment Fund, "About Insuresilience Investment Fund – Main Characteristics and Objectives."
[156] Pablo Antón Díaz, "Growing Concerns about Overindebtedness in Mexico's Microfinance Sector." Center for Financial Inclusion. January 9, 2017.
[157] "Social Performance Report 15 Years of Impact," Switzerland: BlueOrchard Finance Ltd, n.d. https://www.blueorchard.com/emags/spr2015/files/assets/common/downloads/social-performance-report.pdf, 17.
[158] Henry Oguine, "A Sustainability Case Study: BlueOrchard," Business School Lausanne, n.d., 16.

BlueOrchard successfully scaled both impact and financial return. This way, focus remains on the end client, where impact actually occurs, while also meeting the fund's financial requirements.[159] In the case of the Regional Education Finance Fund for Africa, BlueOrchard has been able to scale the financial model so that today the fund reaches across eight countries throughout the African continent, from Ghana to Tanzania.

Table 1: Overview of Case Study Results
Made by the Authors

Framework	**Prudential Financial's AeroFarm Investment**	**BlueOrchard's Regional Education Finance Fund for Africa**
Prioritization	Prudential's priorities do not fit within the binary of impact-first and financial-first investors, nor do they fulfill the expectation that mainstream investors consistently prioritize financial returns. Instead, Prudential emphasizes value creation, or "Impact Value Add," Prudential accomplishes this through mechanisms such as active management strategies and its "80/20" investment approach.	As they were funded through DFIs, BlueOrchard was focused on generating social-impact, and therefore mostly concessional rates of return. But over the next 15 years, BlueOrchard turned to products that could also mobilize private capital in a profitable manner. This allowed them to attract investors with all different types of priorities and willingness to accept risk.
Financial Mechanisms	Prudential uses a variety of financial mechanisms within their Impact Investment Portfolio. Aapproximately 80% of their impact investments, in the "Impact Managed Portfolio", target market-rate or greater returns. The other 20% lies within Prudential's catalytic and concessional loans portfolios. Both these portfolios entail greater flexibility, taking higher preliminary risk (in the case of the catalytic portfolio) or intentionally concessional loans (mainly used within the Philanthropic Portfolio).	BlueOrchard uses innovative financial mechanisms and many different funders all with different priorities. The fund utilizes a tranche structure that allows for some funders to receive below market rate returns, while other received market rate returns.
Specialization	Prudential specializes through their distinct, in-house team of investing professionals, called the Impact & Responsible Investments team (IRI) dedicated exclusively to Impact Investing at Prudential. This senior team allows for them to work effectively with their investees.	BlueOrchard's specialization in the microfinance industry allowed for the development of effective financing mechanisms that were transferable to other funds. Their use of a tranche investment structure for microfinance investments was transferred on to later funds, including the Regional Education Finance Fund for Africa.
Scalability	Prudential exhibits a nuanced understanding of value creation which acknowledges that scaling does not necessarily equate greater value creation; sometimes impact value-add exists best on a smaller, more local scale. At the same time, the use of catalytic funds and active management often helps to promote scalability of investments, such as in the case of AeroFarms. Prudential Financial worked with AeroFarms in its early stages, offering professional assistance to allow for the idea to be more bankable.	They have become specialists within this space, which has allowed them to apply, and in turn, scale the financial model - so that it could reach across eight countries throughout the African continent, from Ghana to Tanzania.

[159] "Social Performance Report 15 Years of Impact," Switzerland: BlueOrchard Finance Ltd, n.d., 17.

Analysis

The Prudential Financial and BlueOrchard case studies can be viewed as two different actors along the impact investor spectrum, but they cannot encompass all the variations of impact investment. Still, several key points that can be drawn from both using the framework.

1. ***Mainstream investors can (and should) engage in impact investment***

Through both case studies, it is clear that a wide range of investors with varying priorities can all pursue impact investment. On one end of the spectrum, Prudential Financial is primarily an institutional investor, but has found a space within impact investment to meet risk-adjusted market- or above-market rate of returns for 80% of its impact investments, enabling more concessions in the remaining 20%. On the other end of the spectrum, BlueOrchard demonstrates the capacity for foundations and Development Finance Institutions to mobilize capital in impact investment from other private and institutional investors through blended capital.

2. ***Losing impact to increase profit does not always need to be the case (and vice versa).***

An investor may not need to 'choose' between impact and profit, nor do they have to choose a single type of investment, whether in terms of rate of return, asset class, etc. In Prudential and BlueOrchards' cases, it is possible to achieve investments on typically less 'bankable' SDG topical areas, such as education. This is made possible through innovative financing mechanisms, including tailored finance and hybrid financing.

3. ***Flexibility and willingness to take on risk is essential for value-creation, and can result in greater profit in the long-run.***

BlueOrchard and Prudential Financial both demonstrate the importance of flexibility as investors. Flexibility speaks to the ability to adjust financial mechanisms or priorities depending on the goal or priorities of the investor. Both also took on greater risk as one part of their portfolio or fund, in order to produce further value creation. In both instances, having a diversified portfolio with varying investments or types of investors is key to being able to fund more flexible, risky ventures.

4. ***Additionality is key. This includes scaling both in financial return and impact.***

Impact Investment is about more than simply generating social value, as there are traditional sectors that do that (e.g. renewable energy). It is specifically adding value by creating new markets or opportunities that did not traditionally exist. The Vice President of Impact Investing at Prudential, Ommeed Sathe, summarizes the process of value creation with this analogy:

> ESG is like choosing the best dish on a restaurant menu and impact investing is like going into the kitchen and cooking a great dish. If you do both well, you will come up with a great investment that tastes good, yet it's a process distinction.

This encapsulates the unique role of impact investment, which is to produce social and environmental benefit by creating space in markets for non-traditional investments and underserved communities.

5. ***Successful implementation of impact investment requires paying attention to the specifics, especially within the relationship between investor and investee.***

Impact investment is an extremely broad term that spans a diverse array of actors, geographies, sectors, asset classes, stages of development, and more. What works for one investor, one investee, or for meeting one SDG target may not work for another. Since impact

investment is not a monolith, approaches to impact investment must be equally varied so they can meet differing circumstances. This is especially important within the relationship between investor and investee. This relationship is the vehicle through which capital is funneled to impact-oriented projects. However, there is also space for conflict with this relationship if the investor and investee do not align their prioritization, financial mechanisms, specialization, and scalability appropriately. Paying attention to these specifics in implementation helps to successfully manage conflict between the investor and investee and to optimize the particular resources and circumstances of the investor and investee.

6. ***In the development space, intentionality is important. But ultimately results, not intentions, matter.***

One of the defining characteristics of impact investment is intentionally pursuing positive social or environmental impact. Therefore, concrete, measurable impact is necessary, and should be more important than profit scalability, and scaling must occur in both impact and profit to be sustainable. Preoccupation with profit without sufficient focus on impact, with regard to both intended goals and unintended outcomes, can limit the positive social or environmental impact or even lead to harmful negative externalities. Implementation of impact investment must be careful and smart to ensure good intentions reap actual results.

Limitations

As mentioned in the paper's analysis section, the framework and case studies do not represent an all encompassing review of impact investment implementation. There are plenty of other possible scenarios within the impact investment space that do not fall within the scope of this paper, including ways in which things can go wrong. If implemented incorrectly or

incompletely, an impact investment project can struggle to be truly sustainable and impactful; in fact, poorly implemented impact investments could even potentially cause harm.

While this research focuses primarily on the investor and investee and how they engage with each other, there is another stakeholder that merits attention: the intended beneficiaries. Recently, some have pointed out that the people who impact investments aim to benefit rarely have any part in the decision making process of impact investment. Fearing the results of an undemocratic form of development finance that is disconnected from those it claims to serve, O'Flynn, Higdon, Besamusca, and Shetty, as well as Gaventa and Hinton, argue for a revised impact investment process that incorporates participation from members of the targeted community.[160] Although this concern falls beyond the scope of this research, it is of high importance and should be the subject of future research.

Future Steps

This paper aims to contribute to scholarship on implementation of impact investment by focusing on investor/investee compatibility and how it relates to targeting SDGs. However, further research is needed to promote deep understanding and expertise in every nuanced aspect of the impact investment market and process. Given the interdisciplinary nature of impact investment, combining financial, entrepreneurial, legal, and development concepts, there is great demand for professionals who can understand and navigate these various disciplines.[161] Education can help to close the gap between development practitioners, finance professionals,

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[160] Peter O'Flynn, Grace Lyn Higdon, Daan Besamusca and Anuradha Shetty, "Deepening Impact through a Participatory Due Diligence Process," *Economic Participation Brief*, no. 1 (Jun 2019), https://opendocs.ids.ac.uk/opendocs/bitstream/handle/20.500.12413/14536/OSF_Brief_1_FINAL.pdf?sequence=21&isAllowed=y.; John Gaventa and Sean Hinton, "Participatory Design Approaches to Impact Investing," PND, Candid, August, 2020, http://philanthropynewsdigest.org/commentary-and-opinion/participatory-design-approaches-to-impact-investing.

[161] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors."; Clarkin and Cangioni, "Impact Investing: A Primer and Review of the Literature," 147.

social entrepreneurs, and other related actors by incorporating elements of each discipline into curriculums.[162]

Conclusion

As our analysis of the case studies demonstrates, implementation strategies that optimize the compatibility of investors and investees through prioritization, financial mechanisms, specialization, and scalability increase the chances of successful impact investments. This understanding of the nuances within impact investment implementation can enhance the capacity of investors to genuinely and positively promote any SDG.

Essentially, it is not about picking the right Sustainable Development Goal that would be most successful, but about establishing an investor-investee relationship that is appropriate in light of the value creation and impact generation profiles of the parties. In other words, it is the *how* that matters as opposed to the *what*. With that, it becomes clear that mainstream investors and other capital sources can (and should) engage in impact investment. In conclusion, the pursuit of any SDG target through impact investment is possible, but an individual investor is better suited to pursue specific SDGs depending on compatibility factors between the investor and the relevant investee. Accordingly, impact investors must focus on value creation through fostering strong relationships with their investees. Additionally, funneling capital to traditional, market-rate investments alone will not foster the new, creative solutions required to drive change. Impact investors should be flexible and willing to take on financial risk. Greater

[162] Ormiston, Charlton, Donald, and Seymour, "Overcoming the Challenges of Impact Investing: Insights from Leading Investors."; Clarkin and Cangioni, "Impact Investing: A Primer and Review of the Literature," 147.

flexibility in the short-run supports the development of innovative social enterprises that can achieve sustainable, inclusive impact, while still generating satisfactory profit in the long-run.

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