Impact investing in social sector organizations: A systematic review and research agenda

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Abstract

Impact investing has great potential to contribute to achieving the Sustainable Development Goals by financing the growth of social sector organizations. This paper conducts a systematic literature review to develop cumulative insights into impact investing in social sector organizations. It identifies four streams of impact investing research – impact investment decision making, impact evaluation in impact investing, behavioral issues in impact investing, and impact investing ecosystem. This paper also identifies nine main research focus areas within these research streams and discusses key insights into each of them. Finally, building on prior research, this article offers a comprehensive future research agenda.

Keywords: Impact investing; Investment decision making; Impact evaluation; Behavioral issues; Impact investing ecosystem

1. Introduction

Impact investing has received increasing attention from both scholars and practitioners around the world over the last decade. Generally, impact investing refers to investments made into organizations, funds, and/or projects with the intention to generate measurable social impact alongside financial returns (Nicholls, 2010; Hehenberger *et al.*, 2019). Unlike other investment vehicles (e.g., responsible investing and environmental, social, and governance investing) that mainly invest in publicly listed companies, impact investing primarily invests in impact-driven, unlisted organizations in the form of private equity, debt, and/or guarantees (Höchstädter and Scheck, 2015; Brest and Born, 2013).

In impact investing, a primary target group of investee organizations is social sector organizations (Bolis *et al.*, 2017). Broadly, social sector organizations are those organizations whose primary aim is to address social and environmental problems (e.g., youth unemployment, deforestation), which can take several forms such as social enterprises, benefit corporations, charities, not-for-profits, cooperatives, and community interest companies (Ebrahim and Rangan, 2014; Powell *et al.*, 2019).[1] While scaling their social impact (Islam, 2020a), one of the major challenges faced by most social sector organizations is the difficulty of obtaining appropriate finance (Lyon and Owen, 2019; Arena *et al.*, 2018). Indeed, the lack of access to finance is considered the single most significant factor inhibiting the growth of social sector organizations (Castellas *et al.*, 2018; Bhatt and Ahmad, 2017). As social organizations play a vital role in most economies worldwide, and as their development is strongly linked with the achievement of the United Nations Sustainable Development Goals (SDGs), impact investing has great potential to contribute to achieving SDGs through financing the growth of social organizations (OECD, 2019; International Finance Corporation, 2019).

[1] Throughout this paper, the terms *social sector organizations, social organizations, social enterprises, cooperatives,* etc. are used interchangeably.

Indeed, because impact investing primarily aims to invest in tackling pressing global problems underlying SDGs, it is considered a promising investment vehicle to effectively address the $2.5 trillion annual SDG investment gap (Pineiro *et al.*, 2018; United Nations, 2020).

Given the importance of impact investing, it is no surprise that research in this area is proliferating. However, little cumulative knowledge exists in this regard. The objective of this paper is to provide a comprehensive understanding of impact investing in social sector organizations. To accomplish this objective, this paper conducts a systematic review of 114 articles drawn from a wide range of journals. The review identifies four research streams in impact investing: 1) impact investment decision making, 2) impact evaluation in impact investing, 3) behavioral issues in impact investing, and 4) impact investing ecosystem. It also identifies nine main research focus areas within these research streams and discusses key insights into each of them. In doing so, this paper responds to the call of researchers to provide a finer understanding of the issues underlying impact investing, without which the impact investing field risks advancing in a fragmented way (Nicholls, 2010; Höchstädter and Scheck, 2015).

Furthermore, by analyzing selected articles, the current paper identifies gaps in the existing research and offers a comprehensive research agenda, thus providing clear directions to researchers interested in impact investing research. More specifically, this paper identifies six promising future research avenues: 1) interrelationship between criteria used in impact investment decision making, 2) a lifecycle perspective in impact investing, 3) navigating conflicting requirements in impact evaluation, 4) understanding behavioral factors from the perspective of both impact investors and social entrepreneurs, 5) facilitating balanced growth in impact investment markets, and 6) unintended consequences of impact investing.

The remainder of the paper is structured as follows. Section 2 details the research method, including data collection and analysis procedures. Section 3 critically reviews the main streams of impact investing research. Section 4 provides an overall discussion of the review findings. Section 5 presents promising avenues for future research. Section 6 concludes the paper.

2. Review method

2.1 Data collection and cleaning

This review draws on several prior review articles, as will be discussed later. To locate relevant articles, two sets of keywords were developed. First, to develop suitable keywords for the term "impact investing", we followed a systematic procedure. More specifically, to gain an initial understanding of various terms that are used interchangeably with the term "impact investing", we consulted a few prominent articles on impact investing (e.g., Höchstädter and Scheck, 2015; Nicholls, 2010; Phillips and Johnson, 2019; Hehenberger *et al.*, 2019). Based on our reading of these articles, we drafted an initial list of more than 20 keywords. To assess the suitability of these keywords, we searched them in several combinations in the Scopus database by using its article title, abstract, or keywords feature. Gradually, it was clear that many of these initially drafted keywords were causing unnecessary duplication of effort. As a result, to ensure the focus of the search while minimizing unnecessary duplication, the following keywords were finalized: "impact invest*", "impact financ*", "social invest*", "social financ*", "philanthrop* invest*", "philanthrop* financ*", "responsible invest*", "responsible financ*", "venture capital*", "ethical invest*", and "ethical financ*".[2]

[2] While conducting a preliminary review of literature, we noticed that terms such as "developmental venture capital", "social venture capital", and "philanthropic venture capital" are also used to refer to the phenomenon of impact investing. Instead of using all these terms as separate keywords, we used the common term "venture capital*". Later, in the data cleaning stage, we excluded articles containing more discussion on "traditional venture capital".

Second, the keywords for "social sector organizations" were also selected following a systematic procedure. Initially, we drafted a list of more than 20 keywords after reviewing several prior articles (e.g., Doherty *et al.*, 2014; Saebi *et al.*, 2019; Ebrahim and Rangan, 2014; Powell *et al.*, 2019). We searched these keywords in the Scopus database, but found that many of them were not adding any extra value in terms of search results. Consequently, we dropped them and finalized the following list of keywords: "social enterprise", "social business", "social ventur*", "social entrepreneur*", "social innovat*", "cooperative", "community enterprise", "social sector", "third sector", "non profit", "not for profit", and "hybrid organi*ation". The wildcard (*) was mainly used to locate different variants of a keyword, going beyond its plural form.

The above keywords were searched in the following way: *any of the words from the first set of keywords AND any of the words from the second set of keywords*. The search was conducted in the Scopus database by using its article title, abstract, or keywords feature. No limitations were placed on the time period. This search generated a list of 253 peer-reviewed articles (in English), which belonged to multiple academic disciplines, including business, management, accounting, finance, and economics. The same search was also carried out in the Web of Science database, which resulted in 135 articles.

Next, following Saebi *et al.* (2019) and Shepherd *et al.* (2015), data were manually cleaned by excluding articles that i) were duplicated between the two databases; ii) were editorials, book reviews, and summaries of articles published elsewhere; and iii) treated impact investing trivially (e.g., contained little discussion on impact investing but more discussion on donation and grant-giving and traditional investments). This resulted in 80 articles.

Furthermore, following Linnenluecke *et al.* (2020) and Doherty *et al.* (2014), we employed a reverse search or snowballing technique to source additional articles from the citations in these

80 articles. This generated a further 34 articles. It should be noted that these additional articles were not detected in the initial search because the journal titles (e.g., *Stanford Social Innovation Review*) were not included in the databases employed and/or search terms were missing in the article title, abstract, and keywords. Overall, the final list contains 114 articles (cut-off: 5 January 2021). A complete list of articles reviewed is presented in the Appendix.

2.2 Data analysis

We used a qualitative data analysis technique by drawing on Foss and Saebi (2017) and Shepherd *et al.* (2015).[3] This involved reading and re-reading selected articles and manually coding them according to the main research focus. As an example of the coding process, the paper of Phillips and Johnson (2019) was coded as "issues around investment readiness" since its main focus was to examine the demand-side factors that contributed to the lack of investment readiness in the Canadian impact investment market. As another example of the coding process used in this review, the article of Achleitner *et al.* (2013) was coded as "criteria used in decision making" by impact investors since its primary focus was to understand how impact investors evaluate the integrity of social entrepreneurs while making investment decisions. Overall, the coding process resulted in the identification of the following nine main research focus areas in impact investing: 1) criteria used in decision making, 2) design of decision-making systems, 3) roles of impact evaluation, 4) impact evaluation approaches, 5) influence of characteristics of investors and investment products, 6) influence of cognitive factors, 7) issues around market growth, 8) issues around capital supply, and 9) issues around investment readiness. Table 1 presents examples of articles concerning each of these research focus areas.

[3] See Linnenluecke *et al.* (2017) for an alternative literature assessment technique, namely bibliographic mapping, which can be used to quantitatively analyze the sample articles. However, conducting such an assessment of literature is beyond the scope of the current review.

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Furthermore, these nine research focus areas were assembled into different research streams according to their similarity. For example, because the following two research areas – criteria used in decision making and the design of decision-making systems – mainly focus on decision-making issues in impact investing, they were assembled into a single research stream, namely "impact investment decision making" (see Table 1). Overall, the following four research streams were identified: 1) impact investment decision making, 2) impact evaluation in impact investing, 3) behavioral issues in impact investing, and 4) impact investing ecosystem. Table 1 shows which research focus areas were assembled into which research streams.

3. Research streams in impact investing

This section discusses the main streams of impact investing research and their underlying key focus areas, as presented in Table 1.

3.1 Impact investment decision making

3.1.1 Criteria used in decision making

While making investment decisions, a fundamental task of impact investors is to evaluate investment projects (Scarlata *et al.*, 2012). Research shows that impact investors use both individual- and organizational-level criteria while evaluating investment projects. At the individual level, impact investors assess the personal characteristics of social entrepreneurs. In this regard, a major evaluation criterion used is the integrity of social entrepreneurs (Drayton, 2002; Mogapi *et al.*, 2019; Block *et al.*, 2021). Research shows that social entrepreneurs having either high voluntary accountability efforts (e.g., voluntary disclosure of organizational reports) or high reputation are more likely to receive an overall positive judgment of integrity

from potential impact investors (Achleitner *et al.*, 2013). Research also shows that, at the individual level, impact investors positively evaluate social entrepreneurs who have i) strong passion for social change, ii) high professionalism, iii) clear vision and ambition, and iv) strong community-based social networks (Miller and Wesley, 2010; Bhatt and Ahmad, 2017; Hazenberg *et al.*, 2015).

At the organizational level, impact investors assess several dimensions of social organizations. One such dimension is the specific sector in which the social organizations operate. Research shows that impact investors often have their preferred investment sectors, which are mostly determined by socio-economic and contextual realities as well as their passion (Mogapi *et al.*, 2019; Jayashankar *et al.*, 2015). As a result, they favorably judge social organizations that operate in their preferred investment sectors. For example, solidarity mutual funds in Spain evaluate social organizations in the health and social services sectors more favorably than those who operate in other sectors (López-Arceiz *et al.*, 2017). Although impact investors are heterogeneous in their preferred investment sectors, on a global level, their preference falls within a few sectors such as financial services, clean energy and technology, health, agriculture, and housing (Mudaliar *et al.*, 2018; Phillips and Johnson, 2019). Consequently, these sectors have become more developed in terms of infrastructure availability, profitability, and scalability, which provide private investors with a relatively safer launching pad into the impact investing markets (Bolis *et al.*, 2017). That said, this practice is also hampering the balanced growth of the impact investment markets by significantly underserving other important sectors such as the creative sector (i.e., arts and culture) (Callanan, 2017).

Another important organizational-level variable that impact investors consider while evaluating investment projects is the geographic location of investment projects (Murray, 2018; Castellas *et al.*, 2019; Gasparro and Weinberger, 2019). At a national level, impact investors favorably evaluate investment projects that are located in more populous and advanced

economic regions of a country. For example, researchers show how investment projects located in more developed cities, such as Delhi and Bangalore in India, Madrid and Catalonia in Spain, and Sao Paulo in Brazil, are assessed more positively by impact investors than those located in less developed cities in the respective countries (Rajan *et al.*, 2014; López-Arceiz *et al.*, 2017; Andion *et al.*, 2012). The same trend can also be observed at an international level. Drawing on 41 North American and European impact investing organizations, Mersland *et al.* (2020) show that while selecting investment projects in developing countries, these investors choose projects located in countries with relatively stronger economies and institutions, and avoid the ones located in countries with the weakest economies and institutions (see also Larcom *et al.*, 2015).

Research also shows that ideologies and values of social organizations play a vital role in impact investors' investment project evaluation. For example, many impact investing organizations across Europe and North America tend to favorably judge investment projects located in emerging countries whose religious values are more aligned to their home countries' religious values (Mersland *et al.*, 2020). Furthermore, research shows that certain ideologies and values appear to be more compatible with impact investing, leading to more effective addressing of targeted social problems. For example, Di Lorenzo and Scarlata (2019) show that impact investing in social enterprises with a dominant collectivist ideology (rather than a utilitarian ideology) has more potential to alleviate income inequality, since such an ideology facilitates greater cooperation between impact investors and investees, better mobilization of a wider network of experts, and augmented learning.

As part of their investment decision-making, impact investors also assess social organizations' mission and the competence of their leadership team (Ingstad *et al.*, 2014; Roundy *et al.*, 2017). However, research shows that impact investors are heterogeneous in how they assess these organizational variables. Some impact investors favorably judge social organizations whose

mission primarily focuses on social goals (Leborgne-Bonassié *et al.*, 2019; Miller and Wesley, 2010), while others favor social organizations with a balanced focus on both social and commercial goals (Apostolakis *et al.*, 2016; McWade, 2012). Similarly, research shows that some impact investors positively assess the higher commercial experience of the leadership team of social organizations by perceiving such experience as necessary to attain financial sustainability (Mogapi *et al.*, 2019). In contrast, some other impact investors negatively judge the higher commercial experience of social organizations' leadership team by recognizing such experience as a major driver of mission drift (i.e., focusing more on profit at the expense of social impact) (Miller and Wesley, 2010; see also Scarlata *et al.*, 2016; Scarlata *et al.*, 2017; Lim *et al.*, 2020).

3.1.2 Design of decision-making systems

Generally, research is limited on what systems impact investors use in practice to prioritize different investment projects. However, scholars have addressed several design-related issues underlying an impact investment decision-making system. While designing a system to prioritize impact investment projects, a major challenge is to effectively deal with social impact and financial return dimensions of impact investments (Brest, 2016; O'Donohoe, 2016). In this regard, some scholars suggest deriving a single measure by integrating the social impact dimension with the financial return dimension. For example, Viviani and Maurel (2019) offer a quantitative measure of multidimensional value creation in impact investing by taking into account both the financial and social impact performance of a social enterprise, which could be used by impact investors to estimate which investment projects would create the highest value in terms of impact and return (see also Emerson, 2003).

Going one step further, some researchers suggest that designing an impact investment decision-making system should consider several other important dimensions (e.g., risks and stakeholders) in addition to considering financial return and social impact dimensions, without

which impact investments may not achieve the intended results (Geobey *et al.*, 2012; Serrano-Cinca and Gutiérrez-Nieto, 2013; Muñoz and Kimmitt, 2019; Gregory, 2016). For example, Brandstetter and Lehner (2015) present an econometric model for optimizing impact investment decision making, which incorporates not only financial and social returns but also financial and social risks.

Although investment decision-making systems based on quantitative methods help to ensure rigor and objectivity in the investment decision-making process by quantifying an investment project's value, too much emphasis on the quantification of a project's value by ignoring its qualitative aspect may result in misleading decisions. King (2017) shows how the evaluation of an investment project in a social enterprise, based on quantitative methods only, could provide a one-sided, biased picture, and how using both quantitative and qualitative methods in evaluating the project could provide a more holistic picture of the project's worth. Indeed, qualitative data about an investment project may reveal some subtle yet significant insights, which usually remain beyond the realm of quantitative evaluation methods (Roundy *et al.*, 2017). This suggests that to increase the chance of optimal investment decision making, impact investors need to use qualitative insights/data to supplement investment decision-making systems that are primarily built on quantitative methods.

3.2 Impact evaluation in impact investing

3.2.1 Roles of impact evaluation

Impact evaluation is a fundamental aspect of impact investing, since it is one of the few key features that differentiates impact investing from traditional investing (Höchstädter and Scheck, 2015; International Finance Corporation, 2019). Research shows that in the impact investing industry, impact evaluation is mainly driven by impact investors who hold social organizations accountable for achieving social impact (Bolis and West, 2017; Ebrahim and

Rangan, 2014). Here, impact evaluation mainly serves as an accountability mechanism. However, researchers observe that, at times, impact investors' obsession with the expectation of accountability can demand burdensome impact evaluations and reports from social organizations without giving extra resources, leading social organizations to divert precious resources away from serving beneficiaries (Phillips and Johnson, 2019; Jackson, 2013).

Research also shows that impact evaluation plays a legitimacy-building role in impact investing. For impact investing organizations, impact evaluation helps to legitimize their investment decisions to key stakeholders, such as their own funders, peers, and other industry networks (Urban and George, 2018; Glänzel and Scheuerle, 2016). In contrast, for social organizations, impact evaluation assists in establishing legitimacy with both existing and potential investors to receive future investments (O'Leary and Brennan, 2017).

Furthermore, research shows that in an impact investor–investee relationship, the specific role of impact evaluation may change over time. At the early stage of the relationship between impact investors and social organizations, impact evaluation mainly serves as an accountability mechanism (Lall, 2019). However, as their relationship matures over time, both impact investors and social organizations adopt a more collaborative practice regarding impact evaluation, leading to the use of impact evaluation as an organizational learning mechanism to better manage their social and business objectives (Lall, 2019; Mayer and Scheck, 2018).

Recent research depicts a more comprehensive picture of the role of impact evaluation in impact investing. Drawing on 78 organizations representing investors, intermediaries, investees, regulators, and consultants in the Australian and UK impact investing markets, Ormiston (2019) shows that the role that impact evaluation plays in impact investing is more complex and transdisciplinary in nature, involving elements of accounting, strategy, operations, marketing, and organizational learning. Although the multiple roles of impact

evaluation help to advance impact investing markets, at times, clashes can occur among different roles, which could be counterproductive to the sound development of the markets. For example, the marketing role of impact evaluation (i.e., highlighting positive impact data) may overshadow its organizational learning role (i.e., learning from failure or negative impact data) (Ormiston, 2019).

3.2.2 Impact evaluation approaches

Research shows that impact investors are heterogeneous in their use of impact evaluation approaches (Chen and Harrison, 2020). For example, drawing on 16 impact investing organizations across Europe, Reeder *et al.* (2015) show that impact investors follow three broader approaches while evaluating their investments' impact. The first group of investors (e.g., Big Issue Invest, UK) follows a case-by-case approach, where they select both output and outcome metrics based on the unique context of a specific investment portfolio. The second group of investors (e.g., Nesta Impact Investments, UK) follows a system-building approach, where they adopt a more systematic and standardized approach in evaluating impact by testing and modifying their theory of change, building upon their past results, and developing a transparent impact database. The third group of investors follows an intermediate approach, where they focus on short-term outputs rather than long-term outcomes. These findings also echo other research that shows how some impact investors mainly focus on measuring activities and outputs on an ad hoc basis (Adams *et al.*, 2017; Castro and Ripley, 2019), while others focus on outcome measurement following a systematic method (Bank, 2016; Buckland *et al.*, 2013; So and Capanyola, 2016).

Although outcome measurement is desirable in impact investing, scholars recognize the complexity and significant costs associated with such an endeavor, especially if impact investor/investee organizations carry out outcome measurement for the first time or they are in the early stage of their operations (Dufour, 2019; Muers, 2017; Andrikopoulos, 2020). Even

for mature and resourceful investor/investee organizations, designing and implementing an outcome evaluation program is not an easy task. Indeed, Pradhan *et al.* (1998) show how the outcome evaluation of the Bolivian Social Investment Fund was full of complexity resulting from issues surrounding the availability of pre-intervention data, the appropriateness of matched-comparison design versus randomized control trials, and the difficulties in identifying valid instruments.

However, researchers note that not all impact investor/investee organizations may need to measure their outcomes; rather, some organizations may be better off measuring their outputs, thus realizing cost savings in impact evaluation. For example, drawing on a number of impact investor and investee organizations in India and the US, Ebrahim and Rangan (2014) suggest that organizations should measure outcomes under two conditions: when there is a well-established cause-and-effect linkage between outputs and outcomes, or when the organizations can control the range of interventions needed to achieve outcomes. That said, scholars acknowledge that these conditions are unlikely to be met in most cases in the social sector due to the existence of complex, non-linear relationships in this sector (Ebrahim and Rangan, 2014; Brest and Born, 2013). Therefore, when outcome measurement is impossible or impractical in impact investing, organizations are encouraged to continuously measure outputs and use existing research evidence, where available, to make credible claims about the linkage between their actual outputs and potential outcomes — an approach that some leading impact investors and intermediaries follow (e.g., Rise Fund and Bridgespan Group) (Addy *et al.*, 2019; International Finance Corporation, 2019).

3.3 Behavioral issues in impact investing

3.3.1 Influence of characteristics of investors and investment products

Understanding the factors affecting impact investment behavior is an emerging research area. Research shows that individual investors' age has an influence on their impact investment behavior. In an online survey experiment of 145 wealthy, private investors in Germany, Schrötgens and Boenigk (2017) find that younger investors, as opposed to their older counterparts, are more likely to contribute part of their overall investments to impact investments. This finding also echoes Apostolakis van Dijk Blomme *et al.* (2018), who show that among 637 individual investors in Netherland, older investors (rather than younger ones) are less likely to invest in an investment portfolio that has a more social focus. This indicates that younger investors are relatively more interested in impact investing, and that it may be relatively easier for social organizations to persuade younger, private investors to allocate funds to impact investments.

Attributes of impact investment products also influence impact investment behavior. A common attribute of many impact investment products is the trade-off between financial return and social impact – that is, the extent to which investors need to accept lower financial returns than the market rate to attain the desired social impact (Brest *et al.*, 2018; Bannick *et al.*, 2017). Research shows that private investors exhibit a positive attitude towards impact investment products as long as the products do not require them to sacrifice financial returns beyond a certain level. In an experiment based on 334 Dutch individual investors, Apostolakis van Dijk Kraanen *et al.* (2018) find that investors are willing to sacrifice some financial efficiency of their investments to participate in investments that have more socially oriented features. Similarly, in another experimental study, Schrötgens and Boenigk (2017) show that private investors are willing to sacrifice up to 1% of financial returns to participate in impact investing (see also Barber *et al.*, 2021). This suggests that social sector organizations or financial

intermediaries may still attract impact investors by designing impact investment products that offer financial returns 1% below the market rate.

Furthermore, research shows that the perceived innovativeness of impact investment products is positively related to private investors' willingness to participate in impact investing (Schrötgens and Boenigk, 2017). Indeed, individual investors are more inclined to allocate funds to impact investment products when they have higher confidence in the products' claims about their effectiveness in addressing targeted social problems (Apostolakis van Dijk Blomme *et al.*, 2018). However, individual investors who have less confidence in the impact investment products' claims are more guided by social norms in deciding whether to participate in impact investing or not (Apostolakis van Dijk Blomme *et al.*, 2018). Overall, this indicates that better marketing and communication of impact investment products by clearly articulating their innovativeness and effectiveness may attract more private investors to impact investing.

3.3.2 Influence of cognitive factors

More recent research explores cognitive factors that may limit the outcome efficiency of impact investment decisions. In a laboratory and online experiment, Lee *et al.* (2020) find that individuals systematically fail to identify investment portfolios that optimize both financial and social outcomes. This is due to a behavioral factor, namely, categorical cognition — the tendency of people to make investment decisions based on known categories rather than actual results they generate. Lee *et al.* (2020) further observe that limiting the effect of categorical cognition by removing the labels (e.g., for-profit company, charity, and social enterprise) from investment options leads to more outcome-efficient investment allocations (i.e., optimizing both financial and social results). This suggests that to realize the full potential of their investments, impact investors need to focus on investment portfolios based on their potential financial and social outcomes rather than purely on the social organizations' structures and/or legal forms.

3.4 Impact investing ecosystem

3.4.1 Issues around market growth

Impact investment markets are rapidly growing in a few countries such as the UK, the US, Australia, and Canada. Research shows that two key enablers of the rapid growth of impact investment markets in these countries are active government support and the catalyzing role of large foundations (Tekula and Andersen, 2019; Qu and Osili, 2017; Buckland *et al.*, 2013). For example, the UK government is actively supporting impact investing by creating large impact investment funds (e.g., Big Society Capital), introducing innovative impact investment products (e.g., social impact bonds), developing infrastructure for impact investment intermediaries, and creating new legal structures (e.g., Community Interest Company) for social sector organizations to increase their transparency and tradability in impact investment markets (Ridley-Duff, 2009; O'Donohoe, 2016).

Research shows that, due to the lack of these market enablers, impact investment markets are making only little progress in many countries, including both developing and developed countries. For example, although there is considerable interest among Ukrainian business communities and private investors about impact investing, the country's impact investment market lacks much progress because of significant uncertainty about the "rules of the game" at the legislative level (Bukharina and Onyshchenko, 2019). Similarly, the German impact investment market shows little progress due to the lack of much government support to develop intermediary infrastructure for impact investments as well as government initiatives to address the country's complex welfare system (Glänzel and Scheuerle, 2016).

However, although typical market enablers (e.g., strong government support and heavy involvement of large foundations) are important for the growth of impact investment markets, a country's impact investment market can also grow in their absence by forming a strong cross-sector network, characterized by a higher level of deliberate engagement of various actors to

support one another (see Roundy, 2019). For example, Michelucci (2017) shows how the Italian impact investment market is demonstrating considerable progress despite the absence of government-initiated large impact funds and infrastructure and heavy involvement of large foundations. The main driver of the growth of the Italian impact investment market is the high level of collaboration between for-profit and non-profit sectors, comprising banks, advisors, associations, and smaller foundations, who play several roles such as booster, backer, instigator, engineer, assessor, social accountant, and tutor (Michelucci, 2017).

Recent research also highlights the critical role that rhetoric plays in the growth of impact investment markets. Scholars show that to build the legitimacy of impact investment markets by overcoming the liability of their newness, various actors (e.g., impact investors, intermediaries, investees, and other investment platforms) pursue several rhetorical strategies through their financial and nonfinancial communication (Lehner *et al.*, 2019; Meyer, 2019; Ryder and Vogeley, 2018; Lehner and Nicholls, 2014). However, at times, rhetoric may be counterproductive to the sound development of impact investment markets. For example, Mollinger-Sahba *et al.* (2020b) note how the current pervasive rhetoric around impact investing, which is rooted in the neoclassical assumption that market discipline in impact investing is the only effective way to address social problems, has left little room for alternative ways to conceptualize the effectiveness of impact investing (see also Bolis and West, 2017).

Furthermore, although the growth of impact investment markets is laudable, not all types of market growth may deliver the intended results, especially in the long term (Nwankwo *et al.*, 2007; Clyde and Karnani, 2015). Indeed, research shows that impact investment markets in many places are growing but systematically failing to serve the communities who deserve the service most (Mollinger-Sahba *et al.*, 2020a). For example, Castellas *et al.* (2018) show how the rapidly growing Australian impact investment market is mainly dominated by an investment logic (i.e., a higher focus on financial returns rather than social impact) and how

the market is predominantly targeting mature social enterprises, with little or no investment support for early-stage social enterprises. Along the same lines, other researchers observe how impact investment markets in several other countries across Europe, North America, and South America are increasingly bypassing social logic – that is, developing investment products that are most profitable by neglecting the needs of marginalized communities (Cetindamar and Ozkazanc-Pan, 2017; Barbu and Boitan, 2019; Andion *et al.*, 2012). This highlights the case of potential "impact wash" in impact investing.

3.4.2 Issues around capital supply

To ensure a smooth flow of capital in impact investment markets, scholars suggest developing an integrative financial system by adopting a multi-stakeholder approach, thus making a bridge between mainstream financial markets and impact investment intermediaries. For example, research shows how the national and local government institutions, impact investment intermediaries, foundations, private investors, and mainstream financial institutions can work in a collaborative way to provide much-needed capital to fight for major social problems, such as recidivism (Pandey *et al.*, 2018; Alijani and Karyotis, 2019).

Research also highlights the importance of having a formal and specialized financing platform such as social stock exchanges (SSEs). By offering a dedicated platform to connect impact investors and social sector organizations, SSEs have the potential to address the seeming mismatch between the supply and demand for impact investments (Walker, 2012). Furthermore, because of their regulatory authority, SSEs can ensure that the "right" kinds of investors access the platform and that the platform upholds the goal of social welfare in the first place (Chhichhia, 2015). That said, SSEs that exist in a few countries (e.g., UK, Canada, South Africa, Singapore, and Mauritius) are operating on a limited basis only, mainly experimenting with different types of rules and regulations (e.g., listing and de-listing requirements and mandatory and voluntary reporting requirements) (Mendell and Barbosa,

2013; Dadush, 2015). Also, existing SSEs tend to emphasize developing investor protection mechanisms more, with little consideration for developing beneficiary protection mechanisms (Dadush, 2015).

Beside formal, regulatory financing platforms such as SSEs, researchers show how the emergence of alternative, less formal financing platforms such as Kiva, MicroPlace, and Kickstarter is bringing together individual impact investors and investees around the world in innovative ways and helping them to find the right match, whilst measuring and communicating impact data to demonstrate investments' impact on the lives of investees/beneficiaries (Parhankangas and Renko, 2017; Gajjala and Birzescu, 2011; Meyskens and Bird, 2015; Cortese, 2017; Jones, 2010; Martin, 2016). However, researchers observe the presence of regulatory uncertainties/bottlenecks as well as public misconceptions about the operations of this type of alternative financing platform, which are detracting from their true potential for capital supply in impact investment markets (Broccardo *et al.*, 2019; Lehner and Nicholls, 2014).

In addition to platform-based financing arrangements, innovative non-platform-based financing arrangements (e.g., slow money and pooling) are also emerging around the world to address the issue of financial inclusion of social entrepreneurs in marginalized communities (Rubin, 2009; Storton and Astone, 2019). Two factors critical to the success of creating such innovative financing arrangements are the formulation of wide-ranging partnerships with actors from multiple sectors based on equality and trust, as well as the adaptation of tools and practices used in mainstream investment markets (Bhatt and Ahmad, 2017; Vézina *et al.*, 2017; Sonne, 2012).

Although the availability of multiple financing arrangements provides more flexibility to social organizations while making financing decisions, it also creates a significant challenge for them

in terms of choosing the right financing option. This is because while some impact financing options may be relatively straightforward (e.g., microloans), others may be more complex, combining debt and equity in different arrangements (e.g., mezzanine capital, subordinated debt, and social impact bonds (Nicholls, 2010; Bugg-Levine *et al.*, 2012). Scholars warn that before accepting impact finance, social organizations should carefully assess the pros and cons of different impact financing options by considering multiple factors such as levels of risk, time horizon, liquidity, cost, and ease of deployment (Jayashankar *et al.*, 2015; Martin, 2015; Scarlata and Alemany, 2010; Bank and Price, 2016). Indeed, Islam (2020b) shows how accepting equity capital from several private equity firms, which demanded higher financial returns, resulted in an apparent mission drift in SKS Microfinance in India, and how it caused suffering to the ultimate beneficiaries. That is, as social organizations primarily aim for value creation and value devolution (Agafonow, 2015), to prevent mission drift, they need to avoid accepting impact investments that mainly aim for value capture.

3.4.3 Issues around investment readiness

Although the supply of capital is essential in impact investing, it is only one part of the equation. The impact investment markets also need to have enough capacity to absorb the available capital, which is commonly known as investment readiness (Mogapi *et al.*, 2019; Giloth, 2019). More specifically, investment readiness is the perception that investee organizations possess appropriate attributes to attract investment capital (Hazenberg *et al.*, 2015). Research shows that impact investors generally perceive social organizations as investment ready when they have high financial sustainability, good governance structure, proven business models, and demonstrated or potential ability to achieve higher social impact (Hazenberg *et al.*, 2015; Glänzel and Scheuerle, 2016; Gregory *et al.*, 2012).

From the demand-side perspective, research identifies several factors that contribute to the lack of investment readiness in impact investment markets, such as social organizations' lack of

knowledge about how impact investment markets work, their insufficient financial literacy, and their lack of awareness of investment capital (Phillips and Johnson, 2019; Gregory *et al.*, 2012). Furthermore, research shows that a large number of social organizations do not actively seek impact investments due to the fear of potential mission drift, thus relying mostly on grants and donations (Sunley and Pinch, 2012; Tirumalsety and Gurtoo, 2019; Lin *et al.*, 2011). That is, from a demand-side perspective, the lack of investment readiness in impact investment markets mainly results from the lack of sufficient demand for investment capital from social organizations and, where such demand exists, their inability to navigate through impact investment markets.

However, supply-side factors are also partly responsible for the lack of enough investment deals in impact investment markets. Research shows that repayable finance is mostly available to social organizations that have a proven history of profit-making (Ademola *et al.*, 2019; Lyon and Owen, 2019). Furthermore, many impact investors avoid making equity investments in early-stage social organizations because they are perceived as too risky (Arena *et al.*, 2018; Walker, 2012). Also, many impact investors are only interested in large investment deals (e.g., over $1 million) that would generate a large amount of profit at their required rate of return (Hazenberg *et al.*, 2015). Unfortunately, none of the above features that many impact investors are searching for in their investment deals are representative of most social organizations. Rather, some of the common features of social organizations are that they are in their early stages of operation, they aim for break-even or modest profit, and they can absorb smaller deals (e.g., under $200,000; (Social Enterprise UK, 2017; British Council, 2016). Thus, it appears that many impact investors' expectations of investment deals may be primarily informed by the investment deals available in mainstream investment markets, ignoring the realities of social sector organizations.

4. Discussion

The objective of this paper is to provide a comprehensive picture of impact investing in social sector organizations. The review shows that while making investment decisions, impact investors use both individual- and organizational-level criteria to evaluate investment projects. At the individual level, impact investors favorably assess social entrepreneurs who have high integrity, strong passion for social change, clear vision and ambition, high professionalism, and strong networks. At the organizational level, impact investors positively evaluate social organizations that operate in their preferred investment sectors (e.g., clean energy and technology and health), are located in relatively advanced/developed economic regions/countries, and possess ideologies and values similar to their own. However, impact investors are heterogeneous in assessing social organizations' mission and the competence of their leadership team.

An important aspect of impact investing is to evaluate whether and to what extent investments are creating social impact. In impact investing, impact evaluation plays multiple roles related to several key organizational phenomena, including strategy, accountability, legitimacy, marketing, operations, and organizational learning. Although the multiple roles that impact evaluation plays in impact investing are laudable, at times, clashes could occur between different roles, leading to counterproductive results. Furthermore, impact investors are heterogeneous in their use of impact evaluation approaches, ranging from using a case-by-case approach to using a more systematic and standardized approach, to using a mix of them. Regardless of the impact evaluation approaches chosen, a focus on outcome measurement is desirable in impact investing. That said, measuring the outcome of impact investments in the social sector is always neither possible nor practical.

Exploring behavioral issues in impact investing is another emerging research area. Individual investors' age has a significant influence on their impact investment behavior, with younger

investors being more likely to participate in impact investing than their older counterparts. Attributes of impact investment products also influence impact investment behavior. Impact investment products with high perceived innovativeness and effectiveness, as well as up to 1% sacrifice of financial returns, appear to have a positive effect on private investors' willingness to participate in impact investing. In contrast, some cognitive factors (e.g., categorical cognition) have a negative effect on impact investing by limiting the outcome efficiency of impact investment decisions.

The review also shows that impact investment markets are rapidly growing in places where typical market enablers (e.g., active government support) are present. Although the growth of impact investment markets across the world is praiseworthy, in many places, they increasingly resemble mainstream investment markets, thus signaling the possibility of impact wash in impact investing. Furthermore, the review shows that to ensure a smooth flow of capital in impact investment markets, several innovative platform-based and non-platform-based financing arrangements are emerging worldwide. However, while the availability of capital supply is important, in many places, impact investment markets lack investment readiness, leading to a shortage of investment deals.

5. Future research opportunities

While prior research has significantly advanced our knowledge on the phenomenon of impact investing in social sector organizations, several areas have remained largely underexplored. Building on prior research, this paper now presents six promising future research avenues.

5.1 Interrelationship between criteria used in impact investment decision making

Although existing research provides useful insights into the criteria used in impact investment decision making (e.g., Achleitner *et al.*, 2013; Mersland *et al.*, 2020), we need more research

in this area. For example, we know little about the interrelationship between different individual-level criteria that impact investors use to assess social entrepreneurs: Does a social entrepreneur's high level of integrity compensate for their lack of a strong network? Similarly, our knowledge is limited about the interrelationship between different organizational-level criteria used in impact investment decision making. Furthermore, future research could investigate these issues from the perspective of social organizations: How do social organizations decide which impact investments to accept? What individual- and organizational-level criteria do they use to assess individual impact investors and impact investing organizations?

5.2 A lifecycle perspective in impact investing

A promising future research opportunity is to investigate issues around impact investing by adopting a lifecycle perspective. To date, most impact investing research has focused on investment deal evaluation (e.g., López-Arceiz *et al.*, 2017; Miller and Wesley, 2010), which is just one phase of an impact investment lifecycle. Our knowledge is limited about other phases of an impact investment lifecycle, such as deal sourcing, deal negotiation, and deal structuring. Therefore, future research could address, for example, how impact investors source investment deals in the first place, what challenges they face while sourcing investment deals, and how they address those challenges. Similarly, what the key issues are that impact investors and social organizations face while negotiating and structuring investment deals, and how they address those issues.

5.3 Navigating conflicting requirements in impact evaluation

Although existing literature has shed light on several aspects of impact evaluation in impact investing (e.g., Glänzel and Scheuerle, 2016; Lall, 2019), several other important areas have remained largely underexplored. For example, when social organizations receive impact investments from different investors who have varying requirements regarding impact

evaluation and reporting, how do they navigate these multiple requirements? Do they prioritize one impact investor's requirements over another? If yes, on what basis do they do so? What happens when different impact investors have conflicting requirements regarding impact evaluation and reporting? How do impact investors and social organizations overcome this issue?

5.4 Understanding behavioral factors from the perspective of both impact investors and social entrepreneurs

A fruitful area for future research is to conduct in-depth investigations into behavioral issues in impact investing. Although existing research (e.g., Schrötgens and Boenigk, 2017) shows that private investors' age has a significant influence on their willingness to participate in impact investing, we know little about the influence of their other personal characteristics (e.g., educational background, and commercial and social experience) on their impact investment behavior. Furthermore, existing research identifies categorical cognition as a behavioral factor that limits impact investors' ability to make outcome-efficient decisions (Lee *et al.*, 2020). We need more research to identify what other behavioral/cognitive factors could potentially limit outcome-efficient decision making in impact investing, and what strategies could be taken to effectively address them? What behavioral/cognitive factors could potentially improve impact investors' ability to make optimum investment decisions? Also, existing research has mainly addressed the behavioral issues in impact investing from the impact investors' perspective. Our knowledge is limited on the behavioral issues in impact investing from the social entrepreneurs' perspective. For example, which factors have a positive and negative effect on social entrepreneurs' willingness to participate in impact investing?

5.5 Facilitating balanced growth of impact investment markets

Existing research shows that in several places, impact investment markets are growing in an unbalanced way by systematically failing to cater to the needs of, for example, early-stage

social organizations and marginalized communities (e.g., Castellas *et al.*, 2018; Mollinger-Sahba *et al.*, 2020a). Future research could investigate what market incentives could be created to facilitate balanced growth of impact investment markets, and what roles private and public actors could play therein. Furthermore, although existing research (e.g., Phillips and Johnson, 2019) has highlighted the lack of investment readiness in impact investment markets, little research exists on how to address this issue.

5.6 Unintended consequences of impact investing

Finally, little research exists on what could go wrong in impact investing, and what we could learn from that. Therefore, future research could investigate the dark side of impact investing by exploring the potential unintended consequences (e.g., impact washing) of specific practices underlying impact investing. Such research could help impact investors, social organizations, and other stakeholders to avoid or minimize the unintended consequences of impact investing by raising greater awareness about them as well as developing relevant tools to better address them.

6. Conclusion

This paper conducts a systematic review to provide a comprehensive understanding of impact investing in social sector organizations. The review identifies four research streams in impact investing: 1) impact investment decision making, 2) impact evaluation in impact investing, 3) behavioral issues in impact investing, and 4) impact investing ecosystem. It also identifies nine research focus areas within these research streams and discusses key insights into each of them.

Building on prior research, this review also identifies six promising future research areas. These research areas are 1) interrelationship between criteria used in impact investment decision making, 2) a lifecycle perspective in impact investing, 3) navigating conflicting requirements

in impact evaluation, 4) understanding behavioral factors from the perspective of both impact investors and social entrepreneurs, 5) facilitating balanced growth in impact investment markets, and 6) unintended consequences of impact investing. This paper encourages researchers to investigate these issues in greater detail, which could significantly advance the theory and practice of impact investing.

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Table 1. Research streams in impact investing

Research streams	Research focus	Examples of articles
1. Impact investment decision making	1. Criteria used in decision making	Achleitner *et al.* (2013); Miller and Wesley (2010); López-Arceiz *et al.* (2017); Mersland *et al.* (2020); Mogapi *et al.* (2019)
	2. Design of decision-making systems	Viviani and Maurel (2019); Emerson (2003); Serrano-Cinca and Gutiérrez-Nieto (2013); Brandstetter and Lehner (2015); Muñoz and Kimmitt (2019)
2. Impact evaluation in impact investing	3. Roles of impact evaluation	Glänzel and Scheuerle (2016); Urban and George (2018); Lall (2019); Mayer and Scheck (2018); Ormiston (2019)
	4. Impact evaluation approaches	Reeder *et al.* (2015); So and Capanyola (2016); Ebrahim and Rangan (2014); Addy *et al.* (2019); Dufour (2019)
3. Behavioral issues in impact investing	5. Influence of characteristics of investors and investment products	Schrötgens and Boenigk (2017); Apostolakis van Dijk Blomme *et al.* (2018); Apostolakis van Dijk Kraanen *et al.* (2018)
	6. Influence of cognitive factors	Lee *et al.* (2020)
4. Impact investing ecosystem	7. Issues around market growth	Tekula and Andersen (2019); Qu and Osili (2017); Bukharina and Onyshchenko (2019); Michelucci (2017); Mollinger-Sahba *et al.* (2020)
	8. Issues around capital supply	Alijani and Karyotis (2019); Dadush (2015); Sonne (2012); Meyskens and Bird (2015); Bhatt and Ahmad (2017)
	9. Issues around investment readiness	Phillips and Johnson (2019); Hazenberg *et al.* (2015); Lyon and Owen (2019); Arena *et al.* (2018); Sunley and Pinch (2012)

Appendix: List of articles reviewed

Articles		
Achleitner *et al.* (2013)	Dufour (2019)	Murray (2018)
Adams *et al.* (2017)	Ebrahim and Rangan (2014)	Nicholls (2010)
(2019)	Emerson (2003)	Nwankwo *et al.* (2007)
Ademola *et al.* (2019)	Gajjala and Birzescu (2011)	O'Donohoe (2016)
Agafonow (2015)	Gasparro and Weinberger (2019)	O'Leary and Brennan (2017)
Alijani and Karyotis (2019)	Geobey *et al.* (2012)	Ormiston (2019)
Andion *et al.* (2012)	Giloth (2019)	Pandey *et al.* (2018)
Andrikopoulos (2020)	Glänzel and Scheuerle (2016)	Parhankangas and Renko (2017)
Apostolakis *et al.* (2016)	Gregory (2016)	Phillips and Johnson (2019)
Apostolakis van Dijk Blomme *et al.* (2018)	Hazenberg *et al.* (2015)	Pradhan *et al.* (1998)
Apostolakis van Dijk Kraanen *et al.* (2018)	Ingstad *et al.* (2014)	Qu and Osili (2017)
Arena *et al.* (2018)	Jackson (2013)	Rajan *et al.* (2014)
Bank (2016)	Jayashankar *et al.* (2015)	Reeder *et al.* (2015)
Bank and Price (2016)	Jones (2010)	Ridley-Duff (2009)
(2017)	King (2017)	Roundy (2019)
Barber *et al.* (2021)	Lall (2019)	Roundy *et al.* (2017)
Barbu and Boitan (2019)	Larcom *et al.* (2015)	Rubin (2009)
Bhatt and Ahmad (2017)	Leborgne-Bonassié *et al.* (2019)	Ryder and Vogeley (2018)
Block *et al.* (2021)	Lee *et al.* (2020)	Scarlata and Alemany (2010)
Bolis and West (2017)	Lehner *et al.* (2019)	Scarlata *et al.* (2012)
Brandstetter and Lehner (2015)	Lehner and Nicholls (2014)	Scarlata *et al.* (2017)
Brest (2016)	Lim *et al.* (2020)	Scarlata *et al.* (2016)
Brest and Born (2013)	Lin *et al.* (2011)	Schrötgens and Boenigk (2017)
Brest *et al.* (2018)	López-Arceiz *et al.* (2017)	Serrano-Cinca and Gutiérrez-Nieto (2013)
Broccardo *et al.* (2019)	Lyon and Owen (2019)	So and Capanyola (2016)
Buckland *et al.* (2013)	Martin (2015)	Sonne (2012)
Bugg-Levine *et al.* (2012)	Martin (2016)	Storton and Astone (2019)
Bukharina and Onyshchenko (2019)	Mayer and Scheck (2018)	Sunley and Pinch (2012)
Callanan (2017)	McWade (2012)	Tekula and Andersen (2019)
Castellas *et al.* (2019)	Mendell and Barbosa (2013)	Tirumalsety and Gurtoo (2019)
(2018)	Mersland *et al.* (2020).	Urban and George (2018)
Castro and Ripley (2019)	Meyer (2019)	Vézina *et al.* (2017)
Cetindamar and Ozkazanc-Pan (2017)	Meyskens and Bird (2015)	Viviani and Maurel (2019)
Chen and Harrison (2020)	Michelucci (2017)	Walker (2012)
Chhichhia (2015)	Miller and Wesley (2010)	
Clyde and Karnani (2015)	Mogapi *et al.* (2019)	
Cortese (2017)	Mollinger-Sahba *et al.* (2020a)	
Dadush (2015)	Mollinger-Sahba *et al.* (2020b)	
Di Lorenzo and Scarlata (2019)	Muers (2017)	
Drayton (2002)	Muñoz and Kimmitt (2019)	