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An Assessment Framework for Social Risk in Impact Investing

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ABSTRACT (English version)

Social impact investing has grown in recognition and adoption on a global scale in the last few years. However, due to its recent history there is still a lack of adequate discussion about many aspects such as a standard investment process, impact metrics and transparency of results. In fact, the addition of the impact lens generated the need of new tools and procedures besides the traditional ones in order to capture not only the financial perspective, but also the social benefits that these investments produce. The investment paradigm has shifted from a bi-dimensional structure, in which only financial risk and return were encountered, to a tri-dimensional one in which social impact is added.
Nevertheless, it has been recently discovered that these three variables are not sufficient to adequately assess the potential of the social organizations asking for impact funds. As a matter of fact, new types of risk are deterring asset owners from investing into impact projects. Among them, **social risk** emerges and needs to be included in the investment paradigm. Through an intensive review of the literature, it is clear that some authors have tried to design a definition of this concept, but most of them still do not know how to assess its value. Nonetheless, important insights can be drawn from social risk evaluation: above all, it allows to allocate capital to the most prominent initiatives that can truly deliver impact in the long term. This research has thus the objective of better classifying this new type of risk, analyzing through semi-structured interviews the experiences and actual approaches of impact investors and investees within the Italian ecosystem. Here follow the main contributions obtained both through the literature review and this empirical study. Firstly, a new definition of social risk is developed which integrates all the key elements highlighted by the academics. Then, a structured approach for social risk evaluation is set up, designing a qualitative framework comprehensive of all the variables that influence social risk and, thus, need to be monitored. These variables mostly concern the investee organization internal managerial system, skills and intents. Finally, some practical suggestions are provided to the investor in order to mitigate impact risk.

KEY WORDS: Impact Investing, Social Risk, Social Risk Evaluation, Social Risk Framework, Social Impact

ABSTRACT (Versione Italiana)

Gli investimenti a impatto sociale sono cresciuti notevolmente in termini di riconoscimento e adozione a livello globale negli ultimi anni. Ciononostante, data la novità di questa tipologia di investimento, manca un dibattito accurato su diversi aspetti quali il processo di investimento, gli approcci alla misurazione di impatto e la trasparenza dei risultati. Infatti, l'introduzione del concetto di impatto ha portato all'esigenza di nuovi strumenti e procedure in aggiunta a quelli tradizionali, cosicché possa essere inclusa non solo la prospettiva finanziaria, ma anche i benefici sociali che l'investimento genera. Il paradigma dell'investimento si trasforma così da struttura bidimensionale, comprendente solo rischio e ritorno finanziario, in tridimensionale, includendo l'impatto sociale. Tuttavia, è di recente sviluppo l'idea che queste tre variabili non siano sufficienti a valutare adeguatamente il potenziale delle organizzazioni sociali che richiedono capitale. Nuove tipologie di rischio scoraggiano gli investitori che continuano a focalizzarsi su ordinari investimenti volti solamente a generare profitti. Spicca fra queste il **rischio sociale,** che deve essere incluso nel paradigma di investimento. Attraverso una intensiva revisione della letteratura esistente, è apparso come alcuni autori abbiano tentato di definire questo rischio senza, però, arrivare ad una risolutiva definizione. Nondimeno, importanti conclusioni possono essere tratte da una corretta valutazione del rischio sociale: infatti, uno degli aspetti fondamentali è la possibilità di allocare il capitale in quelle iniziative che possano produrre un impatto significativo nel lungo termine.

Questa ricerca si pone quindi l'obiettivo di migliorare la classificazione di questo nuovo tipo di rischio, analizzando attraverso interviste semi-strutturate le esperienze e gli approcci pratici degli agenti che operano nell'ecosistema italiano. I risultati ottenuti attraverso questo studio empirico e l'analisi della letteratura sono i seguenti: in primis, viene sviluppata una definizione di rischio sociale comprensiva di tutti gli elementi chiave già proposti nella letteratura esistente. In seguito, viene proposto un approccio strutturato per la valutazione del rischio sociale, presentando un framework qualitativo che include tutte le variabili che influiscono su questo rischio e che quindi necessitano di essere monitorate. Esse riguardano prevalentemente il sistema manageriale interno, competenze e intenti delle organizzazioni investite. Infine, vengono introdotte proposte pratiche per l'investitore al fine di mitigare il rischio di impatto.

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EXECUTIVE SUMMARY

It was just ten years ago that the term "**impact investing**" was coined at The Rockefeller Foundation's Bellagio Center in Italy. Since that time, an unprecedented growth of social businesses has marked the economy of both developed and developing countries. Powerful in its simplicity, the idea of impact investing for blended value – that is, investment strategies that generate financial returns while intentionally improving social and environmental conditions – is disrupting a world organized around the competing beliefs that for-profit investments should only produce financial returns, while people who care about social problems should donate money in an attempt to solve these issues, or wait for government to step in.

Over the years, we have seen international organizations emerging to support impact investors through new infrastructures, tools and procedures that standardized and simplified certain activities.

Despite the great effort made so far to create an efficient and effective investment paradigm, several challenges continue to afflict the market. In particular, social measurement remains one of the most arduous tasks, given the qualitative nature of the impact sought. For this reason, it is not unusual for investors to simply define the target outputs, namely products/ services offered, neglecting the positive outcomes that the funded initiative could create on beneficiaries.

In addition, the primary goal of some investors is far from contributing for a sustainable society, but rather it is the exploitation of a common trend that prevent those who do not comply with social standards to access business opportunities. This behavior is also known as "impact washing".

However, international institutions, such as The GIIN or EVPA, are trying to solve these issues. Firstly, different measurement methods and social KPIs have been developed for capturing the impact created by social organizations; many practitioners are adopting them entirely, while others take inspiration for then developing ad-hoc systems that better serve their needs.

On the other hand, to avoid the misuse of the impact investing concept for marketing purposes and to preserve the integrity of social impact, some rules have been established. Three essential characteristics emerged when shaping the "good" impact investor:

“intentionality”, namely a declared, ex-ante intention to tackle a social problem; “measurability”, meaning the possibility to demonstrate and measure the social impact generated; “additionality”, that is investing in undercapitalized markets.

Furthermore, a new issue recently arose: impact investors are struggling with different types of risk, with **social risk** being the most relevant.

Social risk is anything but a new concept, however it has been always applied to the social science context and until some years ago it has never been adopted within the financial sphere. In particular, it started gaining importance with the rise of social finance practices and, in particular, with socially responsible investments and the latest impact investments. However, this concept assumes different meanings and weights depending on the field of interest: while in the case of impact investing social risk questions the capacity of the investee to create positive impact, in the other it investigates on whether the investee is able to avoid negative impacts on environment and society.

Although in the first case social risk is a central issue because it concerns the additional mission that marks impact investments (the impact mission), it has been little investigated. In the case of responsible investments, instead, some procedures and models to assess social and environmental risks of investments have been designed and are already utilized by investors.

As a matter of fact, impact investors still lack a clear interpretation of social risk but, especially, they are not provided with any tool that helps them to assess the level of impact risk related to funded projects.

From 2009, 13 diverse definitions of social risk have been provided by academics, each of them highlighting different aspects, or underlining the same ones in different ways, thus confusing the reader.

An even lower number of authors committed to find a way to address social risk during investment due-diligence: only four models aimed at social risk assessment have been developed; however, each of these tools remains an isolated reality.

All of them are organized as a checklist of variables that influence social risk: in particular, they regard the organization impact plan characteristics, the skills and main intents of the project team. The authors are convinced that social risk evaluation should be carried out ex-ante and its value balanced with the other three relevant parameters –

financial risk, financial return and social impact – in order to allocate resources into the most promising organizations on a blended perspective.
In order to concretize the assumptions posed by the writers about what is social risk and how it should be materialized into the investment path, the present research had the **objective** to investigate how Italian impact investors are currently conducting the investment process and, in particular, whether they are taking into consideration social risk. Then, leveraging on the main insights retrieved from the Italian case study examination and the precedent literature review, the next intent was to better frame social risk within the impact investment context: first to provide a unique and comprehensive definition of social risk and then to develop a structured approach for assessing the level of social risk applied to any type of investment.

To complete the first objective a qualitative **methodology** was followed: semi-structured interviews were organized with the actors forming the Italian impact investing ecosystem. The subsequent steps implemented are the following.

1) Research sample selection: To define the population of Italian **impact investors**, a desk analysis of Italian media press releases concerning news about impact investors was conducted. In this way, 50 financial operators were identified and only 38 selected according to precise criteria, which analyze their true intents and strategies adopted. To define the population of **investees**, the investing portfolios of those financial organizations previously defined were scrutinized. In this way, it was found that, until today, 40 different Italian companies have been financed with impact instruments. Among them, only 20 decided to take part to the interviews. At the end, the entire population was composed of 58 different subjects.
2) Data collection: Two interviews protocols were built, one for investors and one for investees, with some questions in common. The interviews were performed between June and October 2019 both face-to-face and via Skype. For this study only some of the issues that were addressed during the interviews were selected: the impact due-diligence approach, the social risk concept and its concretization into the investment process.
3) Data analysis: The information retrieved from the interviews were analyzed through a **thematic analysis**. The main categories exploited for the research were derived

from the literature review. Then, for the social risk topic a further investigation was conducted: given the limited amount of information that we had, the responses of each interviewee were reviewed in details.

The **results** gathered through the literature review and the empirical study have led to important conclusions which constituted the starting point for the framing and assessment of social risk.

First of all, it was found no convergence about the notion of social risk among investors and investees. This confirmed the assumption made after the literature review: there is an urgent need to better define social risk related to impact investments.

Furthermore, there are investors who do not consider this type of risk in the investment process, while others are still figuring out how to properly manage it.

This led to the conclusion that it is necessary to design a structured approach for social risk evaluation that can be exploited by all investors during impact due-diligence.

In particular, an ex-ante evaluation of social risk is fundamental, since, as it is shown in the literature, the social risk parameter helps to understand whether the project under analysis has more or less possibilities to reach the intended impact.

Even if they do not assess social risk of prospect clients, all the interviewed investors are adopting certain criteria for investment screening. These criteria affect the project future performance, namely both financial and social outcomes.

Indeed, they concern the risk that the funded company would not deliver on the impact promised and they should be included into the social risk framework.

It was also discovered that both investors and investees prefer to have a direct relationship and communicate with each other's since the first stages of the investment process.

This, in particular, allows to better align their interests and objectives.

For instance, a participatory due-diligence can help the investor, on one hand, to understand the real risk of the investees' lower social performances and, on the other, to set up customized services to support them.

Moreover, the interviewees think that non-financial assistance is crucial for the investees to reach the financial and social goals.

The social organizations financed often lack essential managerial knowledge, the instruments for social impact measurement, or even access to important business networks that can be easily provided by the investor.

As a matter of fact, non-financial support can be seen as mitigation instrument exploited by the investor to reduce the probability of negative impact, namely social risk.
There are some investors who, for prevention, apply some rules in the investment contract that establish the possibility to exit the deal in case the investee drifts away from the social mission.
Some others have even started to link social returns to financial benefits, such as discounts in the interest rates, as a way to incentivize the investee organization not to lose the focus on the impact mission.

Starting from these results the following outcomes were obtained.
To develop a unique and comprehensive **definition of social risk**, an accurate analysis was performed by revealing interpretative patterns among the definitions of academics and practitioners retrieved in the literature. In particular, three key expressions were identified: “likelihood”, “expected social outcomes”, “negative social impact”. They are integrated in the resulting statement:
“Social risk is defined as the likelihood that the social outcomes of a financed project are lower than expected, null or even negative, therefore worsening the actual social conditions”.

Then, the attention moved to the development of a framework for assessing social risk associated to any impact investment.
Initially, the main drivers of social risk were investigated through a desktop review of the literature. For each risk factor, some mitigating conditions were determined, which constituted the macro-categories of the model.
Then, these categories were further split into several sub-categories that more evidently affect social risk.
Starting from seven different macro-categories we obtained thirteen different variables. They regard mostly the organization mission, resources, activities, processes, outputs, measurement systems and past performance.
All the variables were organized into a framework that the investor could use when carrying out the impact due-diligence.

Subsequently, the evaluation approach was determined. Due to the lack of real cases to analyze, it is difficult to evaluate which variables are more relevant for risk mitigation; therefore, all of them were considered with the same importance.
Moreover, given the qualitative nature of social impact, a qualitative analysis was preferred. For each variable it was provided a thorough explanation that helps the investor to understand whether the investigated company/ project satisfies the requirements.
In case the latter are accomplished, the investor attributes a low risk, while on the contrary a high risk is assigned.
The lower is the number of mitigation variables satisfied, the higher is the risk that the organization would not reach the agreed social outcomes and the investor should be less willing to finance the project.

A short version of the resulting framework is provided in Table a, which, however, does not include the explanation of how each category affects social risk.

Macro-categories	**Sub-categories**
1. Mission alignment	1.1 Balance between social and financial mission
	1.2 Legal and governance structures
2. Clarity of outcomes	2.1 Quantitative/ Qualitative target results
3. Reasoned TOC	3.1 The organizational mission responds to a market problem
	3.2 Direct link between the project's outputs and outcomes
4. Key resources	4.1 Motivated personnel
	4.2 Experience in the social sector
	4.3 Financial sustainability
5. Stakeholder management	5.1 Stakeholder engagement
	5.2 Include marginal stakeholders
6. Social impact measurement	6.1 Adoption of a structured approach for impact measurement
7. Project readiness	7.1 Pilot phase
	7.2 Short-time duration

Table a: Short version of the social risk framework

Once the investment decision has been taken – finance the project or abandon it – this model can also help the investor to understand which are the weaker aspects that characterize the investee organizations. In this way, the investor can establish proper **mitigation measures** to help them improve those aspects.
The most important ones are here presented:

- Make use of intermediaries to manage investments on-the-ground (especially when allocating capital in markets outside the investor control);
- Set up a direct relationship with the customers, for instance by allowing them to participate in the due-diligence process and, then, discuss about the target financial and social performances;
- Provide managerial knowledge, access to important networks, or support with social performance measurement (non-financial services);
- Link target social outcomes to financial incentives (payment-by-result deal structures);
- Set up proper rules that give freedom to the investor to exit the deal whenever the investee is drifting away from the agreed social goals.

In **conclusion**, the social risk framework designed represents a significant step towards the integration of social risk evaluation in the impact investment due-diligence.
In the latest interpretations of the impact finance paradigm social risk constitutes the fourth variable that, beyond financial risk, financial return and social impact, needs to be taken into account for investment selection. The social risk analysis is not only important for investment selection, but also for understanding which are the main problems that can negatively affect the project's social outcomes and that need to be addressed through proper mitigation measures.
The lack of a standardized approach for social risk evaluation, however, does not facilitate investors to integrate the new parameter in the investment process.
The proposed framework aims at solving this gap and support investors with the social risk analysis, providing a simple checklist of variables that need to be examined.
Nevertheless, the research needs to be completed once more evidence will be gained and the first impact deals will reach some results. These results could highlight other social risk factors and new variables will be added into the framework.

Empirical evidence from impact deals could also help to understand which variables in the risk framework are more relevant and to which a higher weight needs to be assigned. All these new elements would make the evaluation more concrete and accurate.

An additional, but more difficult, long-term evolution of the model is the shift from a qualitative to a quantitative evaluation.

The framework, in particular, could become a sort of "social score system": the investor assigns to each variable a numerical value that represents the level of social risk connected to it and, then, computes a weighted average of all the risk values assigned.

A quantitative evaluation of social risk would allow to make easier comparisons among different projects and would simplify the investment decision-making.

It would allow to make a more rational selection of the social projects to finance, balancing the target financial and social returns and the risk that these would not be reached, without leaving anything to chance.

INTRODUCTION

In the last decades, profound challenges have started to afflict the so-called developed economies while the new developing economies are still lacking access to basic goods and services.
These have been reflected in a shrinking welfare system and an increase of social risks afflicting more and more of the world's population.

Up to the middle of the 20th century, social assistance organized by civil society, be it the church, self-help movements or philanthropic institutions, was the main form of welfare provisioning, aimed at the marginalized population (Oosterlynck, Kazepov, Novy, Cools, Barberis, Wukovitsch, Sarius, & Leubolt 2013).
Only after the traumatic experiences of the Great Depression, Fascism and World War II, post-war development became a period of unprecedented progress in social welfare (Oosterlynck et al. 2013), the so called "golden age".
In this era of welfare capitalism (Esping-Andersen, Gallie, Hemerijck, & Myles 2002), the welfare state was not limited to cash transfers, but the public provisioning of a wide variety of social services, from housing to education and health.
Then, in the late 1970s, profound changes in the socio-economic context marked the beginning of a long and deep crisis of the European social model, even more intensified during the financial crisis in 2008.
The crisis resulted from the development of more open, globalized and competitive markets coupled with technological changes and the transition to a knowledge-based service economy, the demographic shifts and changes in family patterns and the entry of a large number of women into full-time employment (Taylor-Gooby 2004).
In this panorama, a series of new social risks, apart from the old social ones, emerged.
In relation to work, secure employment and decent wage, especially for low-skilled work force, became increasingly difficult (Esping-Andersen et al. 2002).
In relation to women and family life, issues of gender equality and discrimination appeared, together with pressures to provide child and elder care services as private households found it increasingly difficult to meet these needs (Taylor-Gooby 2004).

In relation to poverty, the emergence of new sub-groups of the poor, such as the homeless (Fabricant and Burghardt 2016).
In parallel, the situation did not improve for developing countries, that still face huge social problems such as poverty, hunger, unsafe water supplies, poor education systems and poor sanitation (Brinkman, De Pee, Sanogo, Subran, & Bloem 2009).

For years government aid agencies have launched programs and implemented interventions to help impoverished and marginalized groups (Alvord, Brown, & Letts 2004). But all too often, the results of these initiatives have been disappointing in terms of both effectiveness and sustainability, let alone their capacity to scale up their impacts into significant social changes (Alvord et al. 2004).
In addition to this, the lack of financial resources and adequate public policy schemes to tackle the increasing exclusion of some groups from the labor market or more generally from society (Defourny and Nyssen 2010) and the gap between welfare and new risk profiles rose (Ranci 2010).
Therefore, in an environment where traditional providers including charitable and voluntary sector organizations have been criticized as resistant to change and the public sector has become overstretched, social entrepreneurship has been identified as an innovative way of tackling unmet socio-economic needs (Leadbeater 1997).

Social activity, as previously seen, is anything but a new concept.
However, social enterprises are built upon innovative business models that leverage on a dual mission of generating positive social impact as well as financial return, solving the traditional dichotomy between social and financial good.
More specifically, "a social enterprise operates by providing goods and services for the market in an entrepreneurial fashion and uses its profits primarily to achieve social objectives; it is managed in an open and responsible manner and, in particular, involves employees, consumers and stakeholders affected by its commercial activities" (European Commission 2011). Hence it is at the crossroads of the traditional ''business'' and ''charity'' model (Battilana and Lee 2014)
At present, the degree of development of these new organizational forms varies significantly across EU member states. In some countries, like Italy, France and the

United Kingdom, social enterprises are already well integrated in both the welfare system and market; while other countries, like CEE countries, are still at an early stage of development (OECD 2016).

On the other hand, both profit and not-for-profit organizations have started to make their part for a more socially and environmentally sustainable society, so that boundaries across these two traditionally separated sectors are increasingly becoming blurred and a new scenario of hybrid organizations is taking place, represented in Figure1.

The former, in fact, saw the opportunity to invest in social business, as a possible way to exploit new synergies between social and financial performances and to redefine their corporate social responsibility strategies (Sinkovics, Sinkovics, & Jamin 2014).

The latter are sobering to the reality that traditional streams of income, like grants and government contracts, are dying up and, therefore, re-evaluating their financial management practices, becoming partners in business venture or directly managing profit-generating activities (Clark and Brennan 2012).

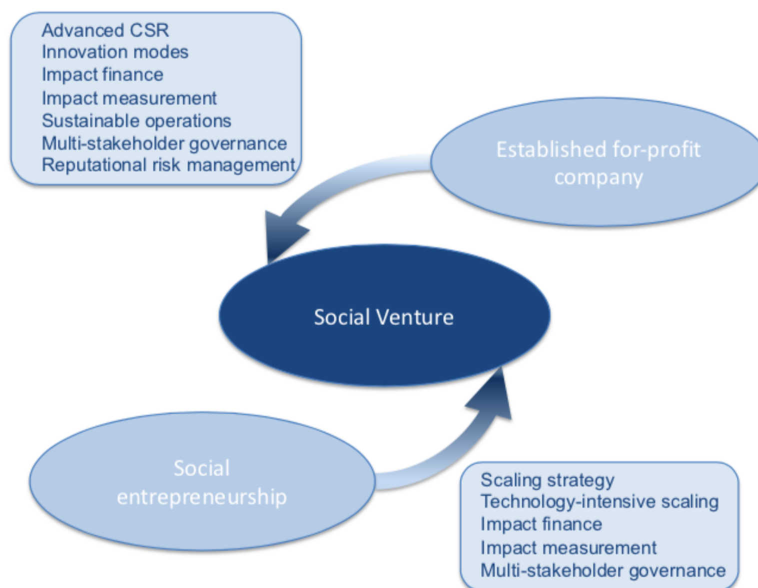

Figure 1: Hybridization process, Tiresia (2017)

Furthermore, public institutions are trying to foster the growth of the social business ecosystem. The "Social Business Initiative" launched in 2011 by the European Commission constitutes a perfect example of supranational effort towards the construction of a more favorable environment for social enterprises to flourish, by

improving their access to finance, giving them more visibility and optimizing the legal environment in which they play. The new "Big Society" strategy of the UK government, as well, is based on the ideology that government alone cannot solve the complex challenges of society but can help to bring together the resources, policies and people, who, between them, can do so. Then, the United Nations (UN) 2030 Agenda for Sustainable Development, adopted by all UN member states in 2015, provides a shared blueprint for peace and prosperity in the forthcoming future.

Despite the impressive increment in number of social enterprises, in which 13.6 million Europeans work today (Borzaga, Galera, Franchini, Chiomento, Nogales, & Chiarini 2020), these new organizational hybrids still face several hurdles to scale up their mission. In this respect, capital represents the key driver for further expanding the social business sector, laying the groundwork for sustainable business growth.

Similar to traditional enterprises, capital fuels the engines of social venture launch and development (Kickul and Lyons 2015) but traditional sources of capital such as government or charitable foundation grants, and individual or corporate donations (Clarkin and Cangioni 2015) are becoming scarce.

To respond to the rising demand of capital and to the changing financial needs of the emerging social market, a new type of financial instrument is born, called "impact investing".

LITERATURE REVIEW

This chapter aims at providing the reader first with the basic concepts regarding the nascent field of impact investing and then goes deeper into its actual stage of development, explaining which are the major challenges that still need to find a solution. Among them one is selected and further investigated: Social Risk.

Social Finance and Impact Investing Overview

The term "Impact Investing" was coined in 2007, when the Rockefeller Foundation invited leaders in finance, philanthropy, and development to its Bellagio Center in Italy to discuss the need for and means of building a global industry striving for investments with a positive social and environmental impact (Harji and Jackson, 2012).

Like conventional investing, impact investing involves the provision of financial resources for a financial return (The GIIN 2013; Louche, Arenas, & Cranenburgh 2012); but the financial return is not the sole objective; impact investing also aims to have social and environmental impact (The GIIN 2013; Louche et al. 2012).

As such, it stands in the middle of an impact continuum between traditional philanthropy on one side and, on the other, mainstream financial organizations, which is called "**Social Finance Spectrum**". In particular, the Social Finance cluster embraces the diverse social investment practices represented in Figure 2.

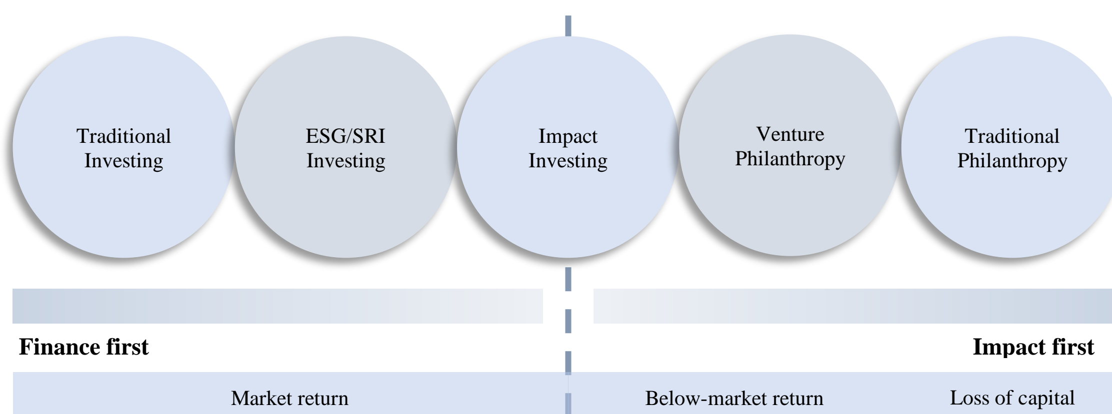

Figure 2: "Impact Investing is catching fire", adapted from Forbes (2018)

Venture Philanthropy occupies the right end of the spectrum and opts for impact-first strategies applying below-market rate interests. In particular, it takes processes and management techniques from venture capital finance and applies them to achieving philanthropic goals (Forbes 2018).
On the other end, immediately after traditional finance, socially responsible investing (SRI) takes its place. Socially responsible investors align ethical and financial concerns in their portfolio strategy, through the traditional practice of excluding stocks of companies involved in harmful and controversial activities, called "negative screening", or adopt more innovative strategies such as "best-in-class" investing and ESG integration (Renneboog, Horst, & Zhang 2007; Eurosif 2014).

Impact investing then lies in the middle between venture philanthropy and SRI since the heart of the movement is the reorientation around blended value.
The Global Impact Investing Network (2018), most known research organization and accelerator within the impact investing industry, has accurately defined impact investments as "investments made into companies, organizations, and funds with the intention to generate measurable social and environmental impact alongside a financial return".
The word "intention" differentiates these investments from socially responsible investments, which instead, aim to avoid social or environmental harm, while still pursuing a single bottom line: profit (Maximilian 2013).
A second adjective used in the upward definition is "measurable", that constitutes the second critical element to recognize true impact.
Indeed, many academics have traduced the impact finance concept into three main pillars:

- **Intentionality** (O' Donohoe, Leijonhufvud, & Saltuk et al., 2010; Harji and Jackson 2012; Brandstetter and Lehner 2015; The GIIN 2018; Tiresia 2019): the impact should be decided ex-ante and the investor must show clear ambition to achieve social or environmental goals (Brest and Born 2013). Positive externalities arising from traditional investments are not considered as intended impact.

- **Measurability** (O' Donohoe et al. 2010; Hebb 2013; Tiresia 2019): the investor should always be able to monitor and measure the social impact of a client company in qualitative or quantitative terms.
- **Additionality** (Brest and Born 2013; So and Staskevicius 2015; Tiresia 2019): the investment must increase the quantity or quality of the social or environmental outcome beyond what would otherwise have occurred (Brest and Born 2013) or, in more radical terms, it means to invest in undercapitalized, risky markets.

As long as impact investments respect these three requirements, they can be made in both emerging and developed markets and target a range of returns from below market to market rate, depending on investors' strategic goals (The GIIN 2018).

Impact Investing Marketplace

The impact investing ecosystem involves three main actors: demand, supply and intermediaries intended to connect them, all presented in Figure 3.

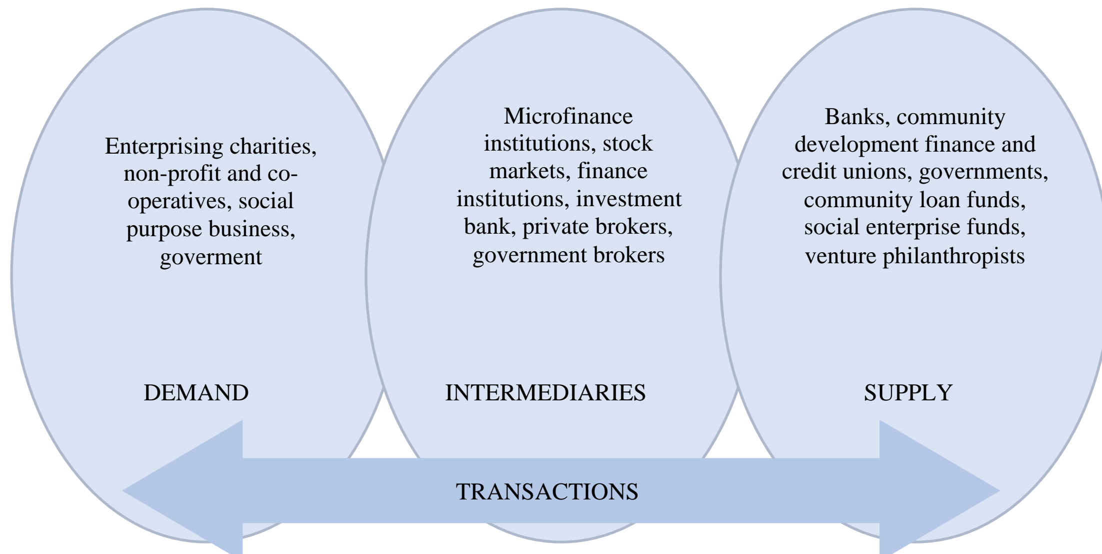

Figure 3: Overview of impact investing marketplace, adapted from Myers and Conte (2013)

On the **demand side** there are organizations such as charities, not-for-profit organizations, social enterprises, profit with purpose businesses, that most often are located on early stages of business lifecycle, meaning that their entrepreneurial idea has

still been not implemented or, alternatively, they have tested the model on a small target of beneficiaries and they need capital to make them grow and scale up the impact.

The central feature of impact investees, however, is that they are double and can be even triple bottom-lined, achieving both a social and/or environmental aim alongside a financial return (Millar and Hall 2013), since they have to repay at least the principal at maturity. Therefore, even not-for-profit organizations might have some sources of revenues.

According to The GIIN (2017) the sectors in which they usually operate are: sustainable agriculture, renewable energy, conservation, microfinance, and affordable and accessible basic services including housing, healthcare, and education.

A spectrum of potential investees has been defined; in particular, the version provided by Wilson (2014) is shown in Figure 4.

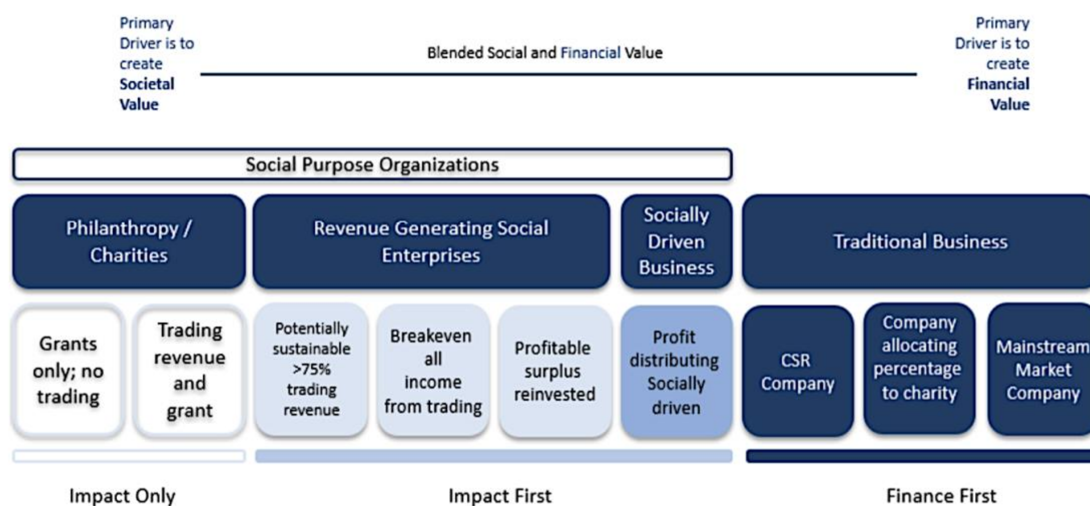

Figure 4: Social Purpose Organizations Spectrum, Wilson K. E. (2014)

In general, the organizations that stand in the central part of the spectrum are the most suitable for impact deals, nevertheless some distinctions can be made.

In particular, “impact first” investors, who are particularly seeking to optimize social and environmental impact with a secondary goal of financial return (Margiono, Zolin, Chang 2017), will favor social enterprises.

In fact, as it has been said before, contrary to market-based organizations, they consider social value creation as central (Battilana and Lee 2014).

On the other hand, “finance first” investors, who generally want to optimize financial returns with social or environmental impact as secondary goal (Wilson 2014), will focus on the right side of the spectrum including traditional businesses somehow intended to enact socially oriented activities.
As a matter of fact, corporate socially responsibility practices are still growing: Mohin (2019), Chief Executive of the Global Reporting Index (GRI), has shown that over 90% of the largest companies are actually filling sustainability reports.

The **supply side** includes in the same way a wide variety of investors, from individuals to institutions across sectors. The main actors currently making impact investments are banks and other financial institutions, public institutions such as pension funds, insurance companies, high net worth individuals and angel investors, community development funds, private foundations and a nascent mass retail market, for example, through crowdsourcing (Hinings, Logue, & Zietsma 2017; The GIIN 2018).
As said before, these investors can range from “impact first” to “finance first” logic, which reflects their strategic goals and investment selection approach that can either prioritize the reliability of investees to return the loan or their capacity to generate true impact. Consequently, investors can have different financial return expectations.
According to The GIIN 2019 Annual Impact Investor Survey, most of them are pursuing market-competitive and market-beating returns, while just a few are investing for below-market-rate returns.

The connections between investors and investees are made through **intermediaries**, who accomplish different tasks.
Firstly, they aim at providing proper investment infrastructures and building market readiness, sharing knowledge and best practices at disposal of actors from both supply and demand side. Most often social organizations do not have the proper managerial skills to compete in the market and make their business sustainable while investors are not even aware of the potential and mechanisms of this emerging sector.
Then, intermediaries commit to aligning capital with projects by matching investors with trustworthy investees; for instance, crowdfunding platforms are becoming more and more utilized.

They also engage to develop commonly accepted metrics and standards enabling communication among different stakeholders. In this way they can both help investees to track and manage their results and reduce due-diligence costs and time for investors (World Economic Forum 2013).

Financial Instruments

Since current financing methods have proven to be inefficient with such peculiar types of investees (Bugg-Levine, Kogut, & Kulatilaka 2012), new financial instruments have been developed to better serve their needs.
Besides well-known financing tools such as grants, debt, equity, mezzanine and hybrid capital (The Schwab Foundation and Technische Universität München 2011), in fact, impact investors are favoring more innovative tools.

Social Impact Bonds

The first and probably the one with the most peculiar structure, is called "Social Impact Bond". It is based on a "payment-by-result" logic which means that money is disbursed just in case the pre-agreed objectives are achieved.
In particular, four types of actors are involved: the government or public entity that commission the impact investor to deploy capital for tackling a specific social challenge, who in turn finances the social project that, more likely, can reach the target objectives. To establish if the social outcomes are achieved or not, an external evaluator is involved, accountable for assessing and reporting results; just in case these are achieved, the government will repay the intermediary, namely the impact investor.
With this system, all risks linked to the failure of program are transferred to the investors, thus encouraging governments, traditionally risk-adverse, to invest their capital and contribute to the social development of communities.

Microcredit

The second innovative instrument called "Microcredit" belongs to the debt category and has a less recent history.

It was utilized for the first time in 1976 in Bangladesh, when professor Muhammad Yunus founding Grameen Bank pioneered the idea of giving out micro-loans to poor people so they can start or expand small businesses in their villages and pull themselves out of poverty. The Grameen Bank and its concept of inclusive finance received worldwide attention and was soon replicated both in developing and developed countries.
The World Bank (2018) emphasized that the progress has been uneven: nearly 1.1 billion people moved out of extreme poverty since 1990.
In this effort, the European Commission has founded the "European Progress Microfinance Facility" followed by the "European Programme for Employment and Social Innovation", managed by the European Investment Fund, intended to deploy financial resources through selected intermediaries across the EU, providing micro-loans, below EUR 25.000, to micro-entrepreneurs.

Crowdfunding

The crowdfunding category has instead become important in the last few years. It implies raising financial resources from a large number of capital providers, the "crowd", usually through funding platforms.
Crowdfunding is seen as a way to reduce the funding gap in the early stages of new ventures (Hemer 2011; Röthler and Wenzlaff 2011).
In fact, funding from venture capitalists and banks is usually available only in the later development phases of start-ups (Robb and Robinson 2014) while during pre-seed and seed stages, funding is typically provided by the founder himself, his friend and family and, if possible, by business angels.
Crowdfunding encompasses several strategies such as donation-based, reward-based, lending-based and equity-based crowdfunding.
In 2018, the global crowdfunding market was valued at 10.2 billion U.S. dollars and was forecast to almost triple by 2025 (Szmigiera 2019).

Now that the major concepts, mechanisms and actors related to impact investing have been clarified, the research moved to the investigation of its actual stage of development and major issues.

Impact Investing actual stage and major challenges

2019 has been a period of significant growth for the impact finance market and someone even defined it as the "golden year" of sustainability and impact (Tiresia Impact Outlook 2019).

This refers not much to the explosion of popular and media attention regarding the new trend but rather to the fact that the economic system has finally start proposing itself as a proactive actor for answering to the actual greatest environmental and social challenges (Tiresia Impact Outlook 2019).

In April, The Global Impact Investing Network (The GIIN) released a new report "Sizing the Impact Investing Market" that estimates the current size of the global impact investing market to be $502 billion, that is over 50 times bigger than its 2013 estimation of $9 billion.

Nevertheless, common concerns arose as financial organizations continue to explore how to implement impact investing strategies.

In particular, the actual major challenges are:

- The lack of a unique and standardized **impact measurement system** that reduces costs and time spent in setting up ad-hoc measurement approaches for each investment deal and encourages benchmarking, thus allowing to channel capital into the most promising social businesses.
- The necessity to clarify what is impact and distinguish between those investors who are really creating positive social impact and those who instead make misuse of the term for marketing purposes and with the ultimate goal of generating profits: this increasing trend is called "**impact washing**". Preserving the integrity of impact investing concept is fundamental in order not to lose its transformative force (Tiresia 2019).
- **New risks** have emerged, besides the traditional ones, that are deterring asset owners to invest in social initiatives through impact investing instruments, and that need to be appropriately defined and taken into consideration (Barby and Gan 2014).

Measurement Problem and Impact Washing

The "readiness" of a social entity to receive impact funds is proportional to its ability to track and account for the social impact created. Impact investors, in fact, are not only interested in monitoring the financial returns but also the social results attributable to the organization activities.

Nevertheless, attempting to assess the impact created – in ways that best capture the whole effect on the enterprise, its employees and society – is a notoriously difficult challenge (O'Flynn and Barnett, 2017) due to multiple reasons.

- Social impact is often difficult to quantify; especially because of its **qualitative nature**, which makes hard to attach an objective value to it.
- Social impact includes short term as well as long term effects on society, very hard to predict.
- Many elements can contribute to environmental and social impact. Consequently, it is often hard to link activities and impact because of difficulties with attribution and causality questions (Maas and Liket 2011).
- The business model of impact investees is often new; that makes it difficult for investors to apply statistical tools and traditional financial analysis (Chell 2007).

In the last years, however, many progresses have been done toward the standardization of impact measurement by several exponents within the social finance field.

In particular, at the heart of social evaluation it has been located the "**Impact value chain**", which describes the causal pathway that starting from long-term goals brings backward to identify changes that need to happen earlier (Clark, Rosenzweig, Long, & Olsen 2004). Its structure is represented in Figure 5.

The inputs exploited and activities implemented can lead to outputs, outcomes and impact, which need to be properly differentiated.

"Outputs" are the tangible products and services that result from an organization's activities, "outcomes" refer to the changes resulting from the activity on the group of beneficiaries while "social impact" means long-term effects on the wider society, adjusted for what would have happened anyway, action of others and unintended consequences (EVPA 2013).

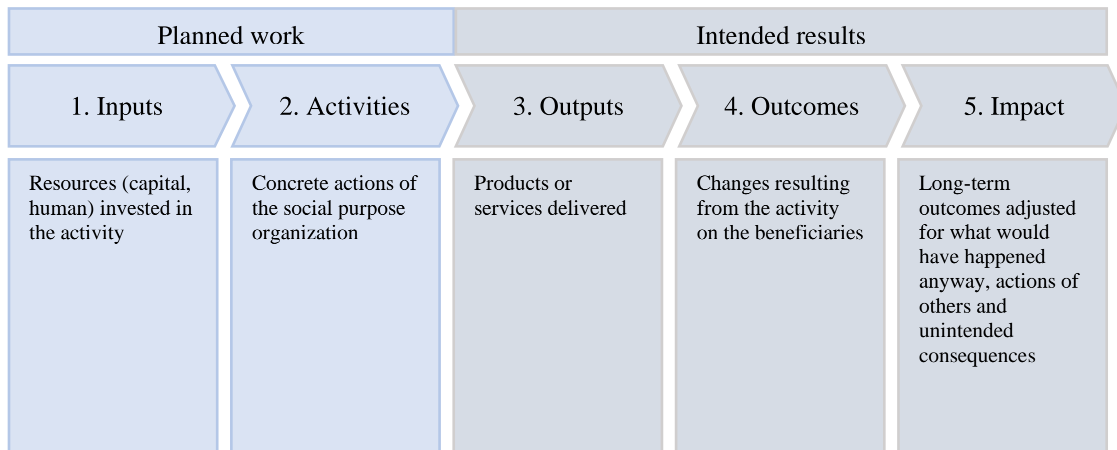

Figure 5: Social Impact Value Chain, adapted from EVPA (2013)

Furthermore, some tools have been developed for the measurement of social and environmental outcomes accompanying impact investors with their due-diligence process.

Among them, the most well-known and used is IRIS, a catalogue of generally accepted metrics to measure social, environmental and financial performances, developed by the Global Impact Investing Network (The GIIN).

IRIS metrics are also exploited by GIIRS (Global Impact Investing Ratings System), an impact rating platform that facilitates funds to manage their investment portfolios. Other certifications are promoted by B-Lab, the SASB (Sustainable Accounting Standard Board) and the GRI (the Global Reporting Initiative), which claims to be the first, since 1997, and most comprehensive sustainable reporting standard in the world.

These approaches aimed at simplifying impact measurement have given substantial advantages to the industry, making it easier for investors to forgo the labor-intensive process of comparing, contrasting and ultimately investing in products on the basis of their potential impact (The GIIN 2018), therefore enhancing deal flow and improving market credibility (O'Flynn and Barnett 2017).

Although the existing systems such as GIIRS and IRIS provide the first steps toward assessing the outcomes of a social initiative, they fall short of capturing the whole range of impacts that can be generated (Brest and Born 2013) and are not suitable for all types of social organizations (Maas and Liket 2011).

The investors still lack a unique and standardized tool for assessing social results which can allow for benchmarking and thus help them to distinguish between those who are really committed to the social cause and that can create positive impact.
The GIIN 2018 Annual Impact Investor Survey, shows that respondents are also looking for some form of third-party certification or shared principles in the attempt to standardize the industry and counteract the risks of impact washing.
One recent effort, in particular, comes from the International Finance Corporation (IFC), part of the World Bank Group, who in the new report "Investing for Impact: Operating Principles for Impact Management" (2019) provides a reference point against which the impact management systems of funds and institutions may be assessed.
The report breaks nine fundamental principles to be satisfied into a five-element end-to-end process, including:
1. Strategic intent: Defining impact objectives in alignment with investment strategy (principle 1) and managing impact and returns at the portfolio level (2);
2. Origination and structuring: Establishing the investor role in creating impact (3), as well as assessing each investment expected impact (4) and managing the risks of each investment possible negative effects (5);
3. Portfolio management: Overseeing each investment impact performance against planned objectives, intervening as necessary (6);
4. Impact at exit: Both conducting thoughtful exits (7) and articulating newly learned best practices and takeaways (8);
5. Independent verification: Disclosing and verifying alignment with the principles (9) (IFC 2019).

Although a definitive answer to these gaps, impact measurement and impact washing, has not yet been given, many academics and practitioners have yet conducted in-depth analysis and proposed some possible solutions.
On the contrary, for what concerns the third issue upwards introduced, it has been found a lack of interest and effort towards the investigation of other potential risks, besides traditional financial ones, associated to impact investing deals.
In this thesis, instead, the risk problem was prioritized in order to understand how the concept of risk evolves with impact investments.

New Risks associated with Impact Investments

From an intensive review of the literature, it came out that impact investors are still struggling with traditional financial and non-financial risks, such as operational risk, market risk or currency risk; but at the same new types of risk arose, that need to be taken into consideration during investment due-diligence.
A list of the most recurrent ones is provided here to the lector:

- **Exit risk**: it is related to the difficulties for the investor to sell or transfer the asset. Although the principle of "patient capital" characterizing impact investments is critical to achieve certain forms of impact, it can make the investors to wait longer to realize their returns and threaten his/her ability to sell the security (Barby and Gan 2014). Exit risk represents a huge barrier for market growth since without liquidity, or the perception of liquidity, huge sections of the investment community will not be able to participate in the impact investing market (SIIT 2014). Barby and Gan (2014) in their study on the new forms of risk connected to impact investments have identified for each risk type one or more de-risking feature. For exit risk the mitigation method identified is "liquidity": a liquid impact investment is defined as any product tradeable on a platform, where the platform may be a widely used exchange or a smaller listing that matches buyers with sellers by providing detailed product information. Liquidity can be influenced by a range of factors including the quality and type of legal documentation, the number of trading platforms and market-makers, transaction costs and overall market transparency (Barby and Gan 2014).
- **Transaction cost risk**: investors usually incur transaction costs, namely time and cost spent on due-diligence, deal structuring and the ongoing monitoring of the asset, and the smaller the transaction the greater the risk that the costs will be out of proportion with potential returns and therefore prohibit the investment (Barby and Gan 2014).

  As an institutional investor explained: "the due-diligence time required for a US$ 10 million investment is the same as the time required for a US$ 100 million investment, therefore resources are best spent on the larger deal" (World Economic Forum 2013). However, impact investment deal sizes are comparably

smaller than traditional investments and therefore impact investors should be higher concerned with this type of risk.

To mitigate transaction cost risk, in this case, Barby and Gan (2014) describe two different features: "bundling" and "track record". Bundled products offer asset owners the opportunity to buy a single product that comprises two or more different underlying investments, allowing also to spread risk: traditional fund structures are based on this logic (Barby and Gan 2014).

The definition given by the two authors, however, go further than this, defining "bundled" as the deliberate aggregation of investments dissimilar in profile, which means belonging to different sectors and geographies or even to different asset classes, to provide diversification. Instead, the second feature presented, "track record", is probably the most inherent and difficult to build in the impact investing industry, given its recent history, but also fragmentated and small-scale configuration.

- **Unquantifiable risk**: the economist Frank Knight defined risk as "quantifiable"; in other words risk is something that can be measured.

  When asset owners consider an investment product, they look at a variety of data, such as historical performance of both product and team, regulation, current and forecasted events and human behavior in order to estimate how an investment will perform over time (Barby and Gan 2014). What an asset owner cannot quantify, however, is the probability of risk factors occurring which they do not necessarily know are relevant or even exist (Barby and Gan 2014). This is called "unquantifiable risk".

  In this respect, unquantifiable risk applies to situations which are not well-charted, such as impact investing, which is not yet a mainstream strategy and whose market mechanisms are still obscure. To avoid these types of risk, Barby and Gan (2014) suggest two de-risking features: "technical assistance" and "placement and distribution". Technical assistance addresses the complexity or performance gaps that an impact lens might add to an investment strategy (Barby and Gan 2014). There can be many forms of technical assistance: the most common is to provide non-financial support to the investee, such as managerial support and impact measurement trainings. Then, a product with placement and distribution is backed

by an advisor who can communicate and demystify the product to unfamiliar audiences, for instance by providing useful comparators (Barby and Gan 2014).

- **Reputational risk**: this risk refers to the probability that an entity ruins its reputation which normally leads to losing clients and reducing revenues.
  For this reason, it is of remarkable importance both for traditional financial institutions and impact investors to manage reputational risk.
  However, since the latter are intentionally pursuing social good, usually customers expect more from them; therefore, in case of negative events the damage to their reputation could be even worse than the one of traditional investors facing similar issues.
  Moreover, impact investors are constantly balancing the dual imperative of generating social impact and profit and some tension can occur between these two. For instance, in pursuit of more profit a business may be inclined to target relatively better-off customers, raise prices to take advantage of the lack of competition or take cash out of the business rather than invest in innovation to enable even broader customer reach (Saltuk 2012; O' Donohoe et al. 2010).
- **Legal risk**: when setting up a new business, there are always legal and regulatory hurdles that can be amplified for impact investments, especially when operating in emerging markets.
  Particularly if the scale of the business is small, the time and resources required to obtain approvals and secure legitimacy for the business can be very onerous (Saltuk 2012; O' Donohoe et al. 2010).
  In addition to legal and regulatory challenges upon inception of the business, there may also be changes to legal and regulatory regimes over time, or challenges to transitioning the business as it grows or changes ownership (Saltuk 2012; O' Donohoe et al. 2010).
- **Social risk/ Impact risk**: this type of risk is particularly important to define and manage since it refers to the social results of the investment. As a matter of fact, impact investments entail two types of performance: financial returns and social returns. As the financial payback of an investment is aleatory and should be accompanied with the risk of default, so it is the social return that the investment could generate and should be accompanied with the risk that the impact fails,

namely “social risk”. Although the concept of financial risk has a long-standing history and relative measurement methods are already well-established, the concept of social risk applied to the investment sphere has not been scrutinized so far in depth. The main feature proposed by Barby and Gan (2014) for preventing social risk is “impact evidence”, a concept that will recur frequently in this thesis. In general, impact evidence is brought by several factors including: a reasoned impact strategy defined together with all the stakeholders, a measurement system to track progress against the expectation set, causal links between the investment’s outputs and target social outcomes, a cost-effective approach, wider stakeholder impacts management, etc.

The achievement of the social objectives is the hardest part to accomplish that characterizes investments with impact. This is why probably among all the new risks connected to social finance, social risk deserves greater attention. Despite the research attention in the last years has been concentrated on the evaluation of social returns – for instance developing for qualitative or quantitative social impact evaluation – the part related to social risk has been mostly neglected.
Few researchers in the field, in fact, have tried to attach a definition to social risk and most asset owners don’t even know how to take it into consideration during an investment process. However, by assessing social risk connected to any social organization the investors are enabled to understand which projects have higher possibility to reach positive impacts in the long term and can allocate financial resources into them.
For all these reasons, from the next paragraph the focus will be on the social risk analysis within the impact finance literature.

Social Risk Definition

Despite the concept of “social risk” is still little known and used within the impact investing sphere, the term is not novel if applied to other contexts.
Indeed, social risk firstly appeared in the social science field where its prevailing definition is “the likelihood that an undesirable state of reality (adverse effects) may occur as a result of natural events or human activities” (Renn 2008).

According to this interpretation, the major social risk types that have been faced in the last decades are unemployment, precarization, gender inequality, weak-family balance, global warming and poverty, which has become a huge problem not only for developing countries but also for developed ones (Leoni 2016).

The social risk term has been later applied to the financial context, where it assumes a rather different meaning, however maintaining its negative connotation.
Firstly, the concept was introduced within socially responsible investments, whose main purpose is to avoid negative impacts by integrating environmental and social (E&S) criteria in the investment strategy.
For this type of investments, it is in fact recommended to carry out an E&S due-diligence immediately after or in conjunction with the financial due-diligence (OECD 2018). In this occasion social risk is assessed. In particular, the "OECD Guidelines for Responsible Business Conduct" attempt to support investors in carrying out the risk analysis. This document also provides a shared definition of E&S risk, reported in Table b.

Definition	**Author/s**	**Year**	**Source**
"E&S risk refers to the likelihood of adverse impacts on people, the environment and society that enterprises cause, contribute to or to which they are directly linked"	OECD	2018	OECD Due-diligence guidance for responsible business conduct

Table b: E&S Risk definition, OECD (2018)

For socially responsible investors the investment decision is still based on searching for the optimal combination of financial parameters. Instead, assessing E&S risks is an activity to exclude those investments that could generate adverse impacts.
The OECD (2018) designed how the investment process should take place which is represented in the flow diagram, shown in Figure 6.

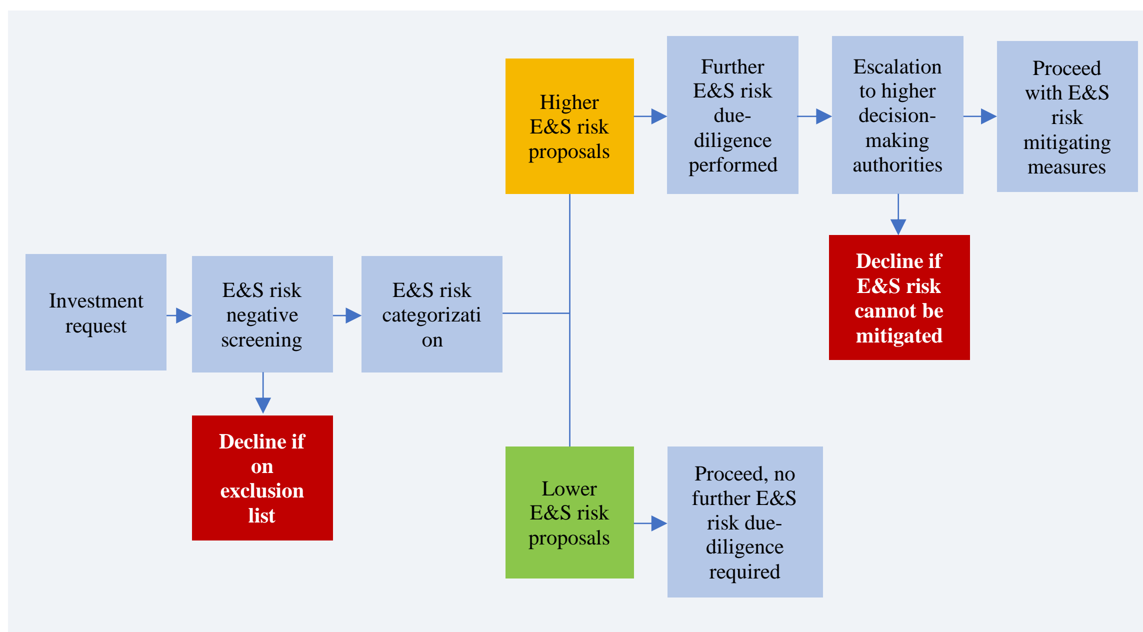

Figure 6: E&S Due-diligence process, OECD (2018)

After the investment request, the company directly undergoes negative screening analysis and in case it operates in those sectors present on exclusion lists – such as tobacco, gambling, drugs, etc. – the offer is declined.

In case, instead, the organization succeeds this phase, it goes through further examination and, if it presents significant probability of adverse impacts (orange box), the judgement is escalated to higher decision-making authorities, who decide if to proceed and develop risk mitigation measures or decline.

Theoretically, the projects that present lower E&S risks, belonging to the green box, should be preferred, even if their financial returns are lower than the ones of those organizations that fall in the orange box (OECD 2018).

In general, financial institutions show different approaches to addressing the E&S risks to which they may potentially be linked through the provision of financial products and services. According to an OECD study on current approaches and practices in the financial sector (2018), there are several factors that influence E&S risk due-diligence: the most relevant are reported in the diagram below.

The percentages are calculated on the basis of the responses to a survey conducted on a sample of financial institutions selected for the research.

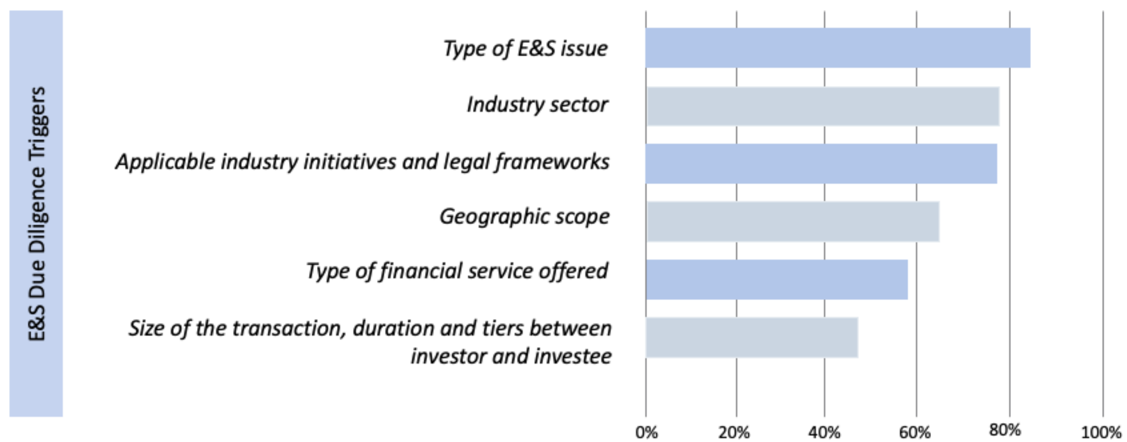

Figure 7: E&S Due-diligence triggers, OECD (2018)

Figure 7 shows that the type of E&S issue and the industry sector, to which the potential client belongs, represent the main concerns and the first things to consider during negative screening analysis.

The same study reveals also that, for the assessment of E&S risks, a consistent number of international frameworks are available for financial institutions, among them are the United Nations backed principles for responsible investment (UN PRI), the Millennium development goals and the Banking environment initiative (OECD 2018).

Most of these risk tools are based on qualitative evaluations that categorize the alternative investments as low/medium/high E&S risk.

After having understood how social risk is taken into account by socially responsible investors, the attention shifts to its conceptualization within the impact finance field.

In particular, thirteen diverse definitions of social risk were found in the literature, the first among them dates back to 2009.

All the definitions are listed in Table c with their respective authors, date and titles of the articles in which they were published.

After having analyzed them, some differences regarding the concept of social risk applied to the impact investing sphere and to socially responsible investments (SRI) were identified.

While in the case of impact investing social risk questions the capacity of the investee to generate additional positive impact, in the other, it questions whether the investee is able to avoid negative impacts on the environment and society.

For these reasons, social risk has different meanings and weights within the two diverse financial fields and for this reason it is better to keep them separated.
Although a clear definition of E&S risks and numerous frameworks to assess them have been designed within the SRI context, there is still not a common understanding of the concept of social risk in the impact investing literature (Lehrer 2016).
However, some famous academics and practitioners have underlined that social risk evaluation should occupy a central position in the impact investing process, since it can tell whether a certain business could really create positive impact.
In the next paragraph it is better investigated the structure of an impact investment process, analyzing also in which stage of the process the social risk assessment should be added.

#	Definition	Author/s	Year	Source
1	"The uncertainty of generating the intended impact"	S. Godeke and R. Pomares	2009	Solutions for impact investors: From strategy to implementation
2	"Social impact risk refers to difficulties regarding standardized performance measurement and reporting"	N. O' Donohoe, C. Leijonhufvud, and Y. Saltuk	2010	Impact investing: An emergent asset class
3	"Impact risk is a concept we have developed to give an indication of the certainty that an output will lead to the stated impact"	R. Puttick and J. Ludlow	2012	Standards of evidence for impact investing
4	"The possibility that what may be first viewed as a "good thing" may actually end up being not so good"	J. Emerson	2012	Risk, return and impact: understanding diversification and performance within an impact investing portfolio
5	"How interventions and investment practices might have negative social returns"	S. Geobey, R. Westley et Al.	2012	Enabling social innovation through developmental social finance
6	"Social risk refers to the risk that an institution' investments might alienate key stakeholders and/or compromise the values of an organization"	N. Laing, C. Long et Al.	2012	The U.K. Social Investment Market: The current landscape and a framework for investor decision making
7	"Impact risk is a measure of the certainty that an organization will deliver on its proposed impact (as detailed in the impact plan). The question is: How sure is the impact plan to work and what is the risk that the impact won't be generated?"	A. Hornsby and G. Blumberg	2013	The good investor. A book of best impact practice

8	"Social risk refers to the uncertainty about and severity of the events and consequences of an activity with respect to something that human value"	H. Mahmoudi, O. Renn, F. Vanclay, V. Hoffmann, & E. Karami	2013	A framework for combining social impact assessment and risk assessment
9	"While some authors interpret social risk solely as the risk of not reaching the intended impact, others apply a broader lens including for example exit risk, liquidity risk, measurement risk or unquantifiable risks"	L. Brandstetter and M. Lehrer	2014	Impact investment portfolios: including social risks and returns
10	"Impact risks can take various forms. For example, there may be a lack of evidence that an intervention will lead to the desired outcome. Even if the intervention is successful, the investment could cause displacement, leading to reduced or no net benefit"	C. Barby and J. Gan	2014	Shifting the lens: a de-risking toolkit for social impact investments
11	"The social risk can be defined as the likelihood that a given allocation of capital will generate the expected social outcomes irrespective of any financial returns or losses"	A. Nicholls	2015	Social Finance. Designing Effective Outcome Metrics and Measurement Systems
12	"Social risk has not been fully conceptualized at present; it ranges from negative social impact despite the well-intended investment motives, to opportunity costs because of an adverse selection of impact projects that fail to deliver"	M. Lehrer	2016	An epiphany of social and sustainable finance (Routledge Handbook of social and sustainable finance)
13	"Social risk is used to identify the possibility that the expected social outcome is not achieved due to unpredictable events"	H. Chiappini	2017	An introduction to social impact investing

Table c: Social Risk definitions in the Impact Investing Literature

The Impact Investment Process

Horsnby and Blumberg (2013) have accurately defined how a "good investor" should act by providing a list of the essential stages of an impact investment process and highlighting which are the key activities carried out in each stage.
In particular, the process should be divided into five stages:

1. Screening and mapping
2. Analysis
3. Investment Decision and Deal-Making
4. Monitoring and Evaluation
5. Reporting

In reality, the first phase is the planning phase which, however, takes place only one time, more specifically when the impact investment fund is set up or when an existing financial institution decides to enter into the impact investment market. In both cases, the prior thing to do is outlining the investment strategy, which means establishing:

- What sectors, outcome areas and geographic locations to be active in;
- What beneficiary groups to reach out;
- The direct impact on beneficiaries, the wider impact on communities and the impact on the financed social purpose organizations;
- Which methods to use (e.g. for measuring financial returns and impact) and the overall appetite for impact risk (Horsnby and Blumberg 2013).

As it can be noticed, impact risk firstly appears in the planning phase when the investor has to decide the maximum amount of social risk that is going to be accepted.

Screening and Mapping

The number of potential investee organizations and investment opportunities for impact investors is growing. In fact, the market continues to expand and so the range of social and environmental issues that need to be tackled.

In order to manage this increasing flow, it is useful for investors to pursue a preliminary screening, that allows to check the fit of any potential investee with the impact investor strategic goals prior to entering into the much lengthier analysis required to make an investment decision (Hornby and Blumberg 2013).
In particular, this preliminary analysis focuses on two aspects:

- Eligibility: it means that the impact investor needs to assure that the prospect investment really support impact and that the underlying organisation is committed to its social or environmental aims;
- Suitability: it means that the impact investor should check if the underlying organization corresponds to the targeted sectors, issues, beneficiaries, geographic area of operations and legal structure chosen during the planning phase (Hornby and Blumberg 2013).

During the screening process, five main topics should be covered:

- mission
- use of investment capital
- governance
- profits and assets
- impact evidence and transparency

When analyzing the mission of an organization, the investor should check if there is a good balance between the financial and impact mission and that the latter is concrete and attainable. It is also important to clarify how the investee will use the investment capital and how this would ultimately support the impact generation.
Then, the governance system should support the investee organization mission and activities and the internal processes which need to be consistent with sustainability principles. It should be also verified that the organization has the resources needed for running the business.
Last check regards the transparency in sharing information, for instance regarding the company financial and social performances.

After or in conjunction with the screening, the mapping process takes place in order to define the pipeline of potential investments down to those that meet whatever conditions or requirements the investor may have.

Analysis

The impact analysis is probably the cornerstone of the investment process, since it is critical to making good investment decisions.
At this point, the investors can adopt their own methodologies but always referring to two main key areas: impact risk and impact generation. The questions that they should asked to themselves are:

- What is the risk that impact will not be achieved?
- What is the impact that the investee organization would generate?

Therefore, it is in this phase that the investor needs to assess the social risk value connected to the investment under analysis. This value together with the amount of expected impact constitute the inputs of the next stage: the investment decision.

Investment decision and Deal-making

Typically, the investment decision is made by an investment committee, starting from the results of the impact and financial due-diligence which are conducted in parallel (Hornsby and Blumberg 2013).
In fact, according to Hornsby and Blumberg (2013) to select one investment the investor should look at its future performances described through four different parameters: impact risk, impact return, financial risk and financial return.
In particular, trade-offs between each couple of the four variables should be conducted. The most well-known relationship is between impact generation and financial return, represented in Figure 8.
In this case, the optimal solution depends on the investor's social and financial return appetites. In particular, the utility function of an outcome-maximizing investor is built assuming that the investor prefers an increase in either financial payback or social benefit that comes without a decrease along the other dimension, that is any Pareto improvement

in the two-dimensional outcomes (Lee, Adbi, & Singh 2020). In this case, the utility function increases monotonically in terms of both financial return and impact generation. Instead, when the investor would rather give up to a portion of profits for achieving a greater social impact, its utility function has a concave shape. On the contrary, a profit seeking investor utility function is convex (Hornsby and Blumberg 2013).

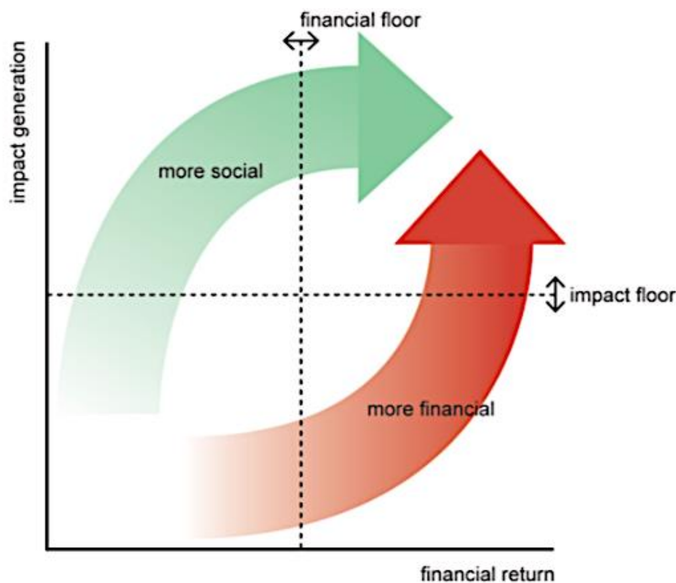

Figure 8: Trade-off between impact generation and financial return, Hornsby and Blumberg (2013)

The other noteworthy trade-off is between social risk and return. In this case controversial opinions exist. Someone considers social risk as an "uncompensated risk" as there is no increased expected impact when exposed to this type of risk, differently from financial risk, which is considered a "compensated risk" as investors seek compensation for higher levels of financial risk with higher levels of profit generation and vice versa (Laing, Long, Marcandalli, Matthews, Grahovac, & Featherby 2012). When comparing two alternative investments with similar business model and impact objectives, normally, the one that offers a higher financial payback is also the riskiest and the choice depends on the risk appetite of the investor. On the contrary, not necessarily the one that proposes a bigger social return entails a higher impact risk, maybe because the social business strategy is better executed or the external environment more favorable.

On the other hand, some authors look at social risk as a "compensated risk" and in this case the trade-off between impact generation and impact risk suggests an upward sloping indifference curve, as shown in Figure 9.

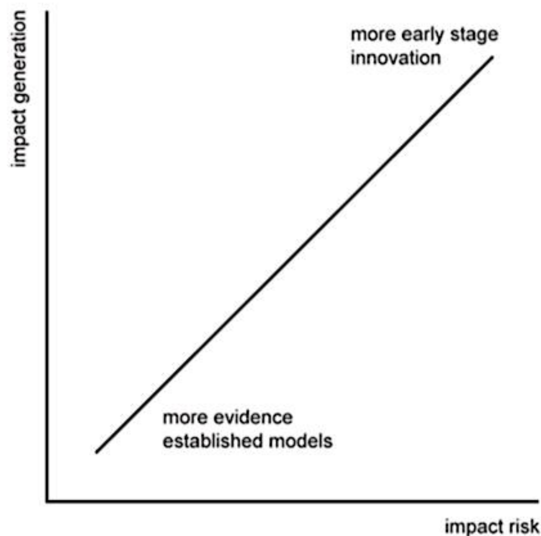

Figure 9: Trade-off between impact generation and impact risk, Hornsby and Blumberg (2013)

Investments that lie on the higher section of the curve are likely to be characterized by less well-tested and evidenced approaches, but due to the fact that they usually target more innovative markets, their potential of impact generation is higher (Hornsby and Blumberg 2013).

On the contrary, investments that lie on the lower section of the curve are more likely to work with standard approaches and in common fields of operation, but the impact that they will generate is comparatively modest (Hornsby and Blumberg 2013).

Therefore, investments that sit above the curve in the graph will be preferable, while investments that sit below the curve, which present a higher social risk and the same level of expected impact, will be less attractive (Hornsby and Blumberg 2013).

Besides the two trade-offs discussed above, others occur between each pair of the four parameters, which however are not highlighted in this study.

While traditional investors are quite simply used to think in bi-dimensional terms (Emerson 2012), impact investors have to deal with four different variables and therefore six trade-offs have to be conducted. Therefore, the investment decision becomes longer and difficult for them.

After the investor decides to proceed with a client, the investment deal should be prepared. Alongside the financial constraints and the repayment structures, an impact investment deal considers also how the organisation will deliver on its proposed impact (Horsnby and Blumberg 2013).

In particular, in the investment contract three main things are established:

- Impact objectives are agreed between the investor and the investee and arranged in the form of key performance indicators (KPIs) with related targets;
- Social reporting requirements are established: typically, these include specifics regarding when and how frequently the organization needs to share its performances with the investor;
- Protection measures are determined. These can involve covenants related to reporting requirements, the application of credit penalties according to the investee social performances (i.e. higher levels of impact generated are rewarded with favorable credit treatment, lower levels of impact incur higher credit rates or other forms of financial penalty), exit restrictions which stipulate a mission-aligned exit, otherwise, the investor could also take a position in the organizational board being able to influence managerial decisions (Horsnby and Blumberg 2013).

Monitoring and Evaluation

The purpose of monitoring and evaluating impact is to determine whether the investment is having the intended effect (Horsnby and Blumberg 2013). It usually takes place over the course of the investment but, in some cases, especially when the investment is short-term, it may be necessary to continue monitoring the organisation and its beneficiaries beyond the investment term, to establish if the impact has been generated and if it is sustainable (Horsnby and Blumberg 2013).

In this phase social risk evaluation needs to be included again. During the whole investment lifetime both the impact generation and impact risk continue to be evaluated. In fact, as the organization goes on with the implementation, social risk could gradually decrease – when the first positive results are achieved – or alternatively it can increase due to different reasons. It could be, for instance, that the approach is not effective and some improvements need to be made. In any case, failure is a considerably better result than continuing ignorance (Hornsby and Blumberg 2013). Therefore, it is important to

monitor the social results during the whole investment lifecycle and sometimes even beyond the investment maturity.

Reporting

The last step of the investment process is reporting. As monitoring and evaluation entail transparency of results reached by the investee organizations, in the same way investors need to account for their performances.
The financial institution impact reports should explain in this respect the use of capital, the portfolio distribution among different activities and areas of focus, the impact risk that the overall portfolio is exposed to, and the impact generation that the investments have facilitated (Hornsby and Blumberg 2013).

This paragraph has shown why and when social risk needs to be included in the impact investing process. However, it is still not clear how social risk should be assessed. In this regard, the last part of the literature review is dedicated to the review of the existing methodologies developed so far for evaluating social risk associated to any impact investment deal.

Social Risk Models

Although some effort has been put by the authors within the impact finance literature in order to define social risk, less attention has been dedicated to develop a proper approach for assessing its value.
In particular, only four models for evaluating social risk have been found.
All start from the assumption that impact investors should separately evaluate impact risk and financial risk. On the contrary, there are some authors that think this new type of risk should be combined with the financial one.
On one hand, the second approach simplifies the investment decision-making process, since it decreases the number of variables that need to be balanced but, on the other, the combination of financial and social risk into one figure could be difficult, since social risk is not easily quantifiable. Laing (2012), who agrees with the second methodology,

recommended to increase the combined risk value only when a relevant social risk is identified, otherwise just keep the financial risk value.

In Table d it is provided a list of the four models that have been found in the literature with a short description that highlights their logic and main characteristics. Afterwards a more in-depth analysis for each of them is conducted.

#	**Framework**	**Author/s**	**Year**	**Description**
1	Standards of evidence	R. Puttick and J. Ludlow (Nesta)	2012	This model starts from the assumption that social risk is indirectly proportional to the level of evidence that the investees will generate impact. In particular, it identifies 5 levels of evidence that the impact project can reach. The higher the level of evidence, the lower the risk that the project's social outcomes would not be reached.
2	Six key qualities of an impact plan	A. Hornsby and G. Blumberg	2013	This framework helps to assess social risk by considering six key qualities of an investee's impact plan – that is: explicit, reasoned, integral, feasible, evidenced, evidenceable. The more the qualities an organization's impact plan fulfils, the lower the risk that it will not reach the proposed impact.
3	Bridges Impact Radar	Bridges Venture	2013	This scoring framework is based on four key criteria: target outcomes, additionality, ESG, alignment. For each criterion it gives a score, from 1 (low) to three (high), both to the impact return and to the impact risk associated to the investment under analysis. This helps to build a risk/return profile for each investment.
4	Social Risk Scoring Model	E. Scognamiglio, A. Rizzello, & H. Chiappini	2018	This framework applies to social impact bonds. It split social risk into three main categories: program process, contractual condition and evaluation methodology. For each category different risk factors are shown and for some of them also the related sub-factors. Then, for each variable it is specified a key question and some alternative responses

				that correspond to a specific risk score, which in this case range from 1 to 4; the smaller the number the lower is the risk level. Then, a mathematical methodology is adopted to integrate all the scores into one numerical value that represents the overall social risk connected to the project.

Table d: Social Risk Evaluation Frameworks retrieved in the Impact Investing Literature

Standards of Evidence

The "Standards of Evidence" framework has been developed by Puttick and Ludlow (2012) for Nesta Foundation to help guide their impact investments decisions.
As already explained in Table d, any investee can reach different levels of impact evidence which determines the amount of social risk connected to the project.
Moreover, whatever the level of evidence shown at investment proposal, the investee will be expected to move towards the levels over the investment lifetime that provide higher certainty of expected outcomes (Puttick and Ludlow 2012).
The higher the level the more in-depth evaluation techniques are required, that probably would need the support of specialists (Puttick and Ludlow 2012).
A summary of the subsequent levels of evidence that can be reached by an organization is provided in Table e.
For each level, in particular, it is described which are the expectations of the investor and it is explained how the investee can demonstrate that evidence.

Level	Expectation	How the evidence can be generated
1	The organization should give an account of impact by providing a logical reason, or set of reasons, for why its products/services could have impact on one of our outcomes[1], and why that would be an improvement on the current situation.	The organization should be able to do this by drawing upon existing data and research from other sources, for instance giving evidence of similar initiatives being developed or providing data about the problem to be tackled, etc.
2	The organization should present some data that show some change among those using its product/service.	At this stage, there will we some evidence of the results but still not evidence of direct causality. The organization can consider methods such as: pre and post survey evaluation; cohort/panel study, regular interval surveying.
3	The organization should demonstrate that its product/service is causing the impact, by showing less impact amongst those who didn't receive the product/service.	At this stage robust methods need to be used such as control groups that allow to isolate the impact of the product/ service. Random selection of participants strengthens evidence but the organization needs to have a sufficiently large sample at hand (scale is important in this case).
4	The organization should be able to explain why and how its product/service is having the impact observed and evidenced so far.	At this stage, a robust evaluation that investigates and validates the nature of the impact is needed. This might include endorsement via commercial standards, industry kitemarks etc.
5	The organization should show that its product/ service could be operated up by someone else, somewhere else and scaled–up, whilst continuing to have positive and direct impacts and remaining a financially viable proposition.	It is expected that the organization will use methods like multiple replication evaluations; future scenario analysis; fidelity evaluation.

Table e: Standards of Evidence of Impact Investing, Puttick and Ludlow (2012)

[1] It refers to the target outcomes of Nesta Investment Fund which refers to three main areas: Ageing, Children and young people, Community sustainability.

Six Key Qualities of an Impact Plan

Hornsby and Blumberg (2013) proposed an impact risk assessment tool that looks at the impact plan for six key qualities, all mentioned in Table f. To build this model, the two authors leveraged on a research made on nine of the UK leading impact investors[2].
In particular, the study analyzed their current activities, the problems that they face, where they demonstrate best impact practices, and where instead there are realistic and tangible improvements to be made. This resulted in a list of key features that a good impact plan should satisfy and that decreases the level of social risk. The more the qualities that the organization impact plan has, the lower the probability that the company will not reach the expected social impact.

#	Six key qualities	Sub-factors
1	1)Impact plan **explicit** in all particulars	1.1) Clarity
		1.2) Concreteness
		1.3) Completeness
2	2)How well-**reasoned** and compelling the theory of change is	2.1) Mission and activities coherent with the context
		2.2) Link between outputs and outcomes
		2.3) Context of change
3	3)Impact plan **integral** to the organization's business strategy	3.1) The business plan clearly supports the impact plan
4	4)**Feasibility** of the impact plan	4.1) Key personnel
		4.2) Operational processes
		4.3) Capacity
		4.4) Conditions for change
5	5)**Evidence** of impact generation	5.1) Track record
		5.2) Precedents
		5.3) Research
		5.4) Control groups
6	6)**Evidenceable** impact plan	6.1) Measurement systems in place

Table f: Six key qualities of an impact plan, Hornsby and Blumberg (2013)

[2] The consultation group consisted of: Big Issue Invest, Bridges Ventures, Big Society Capital, CAF Venturesome, Deutsche Bank, Esmee Fairbairn Foundation, Nesta, Social Investment Business, Triodos Bank as well as discussions with the Cabinet Office.

1)Explicit:

It means that the impact plan should articulate clearly the processes followed and how the activities will bring about the desired change.

It has to be concrete about the resources needed to realize the plan, the target beneficiaries and the context in which it exists; then it should specify exactly what is to be achieved and the time required for reaching the stated results.

The plan should also consider a broader picture and understand how its activities influence other people or relates to the surrounding environment.

Since a full address of the context is difficult to accomplish, it could help to conduct before an assessment of materiality which determines the bounds of what is relevant to include in the analysis, because it determines or compromises the expected impact (Hornsby and Blumberg 2013).

2)Reasoned:

A crucial factor for the success of an impact plan is having a well-structured and reasonable theory of change.

This implies that the organizational mission and activities respond coherently to a market problem, a direct link exists between the project outputs and expected outcomes, the plan addresses the context in which it is located.

3)Integral:

Social impact is at risk in case the company financial and social interests are not well-aligned. On the contrary, if the impact plan is integral to the organization business strategy, which means that the business plan is supporting the impact plan, the social risk is lowered and the financial and social return go hand in hand.

Where there is tension regarding the integration of impact return into the business model, the investor may look for some forms of “mission lock” or protection via the governance or legal structure of the organisation.

4)Feasible:

An impact plan is valid if it is feasible. A significant aspect of the overall feasibility of the plan relates to the financial and operational strength of the organization, which is generally questioned during financial due-diligence.

However, some aspects remain uncovered by the financial analysis such as skills and experience of the personnel or projections around contextual factors beyond the organizational control (e.g. conditions in the local economy, supports or services to be delivered by other organizations), which the impact is reliant upon.

These elements need to be tackled during social due-diligence and influence the level of social risk.

5)Evidence:

This is a key quality that indicates whether the plan would generate the expected results. Evidence serves to promote confidence in the impact plan, reassuring the investor that planned activities will lead to the agreed social results.

According to Hornsby and Blumberg (2013), the best ways to prove evidence of results include track records of past performances.

In case the company has never carried out a similar project before, precedent experience of other organizations in the same sector can be exploited.

In addition to that, research and knowledge of experts may be used to support the strategy adopted and the assumptions made about the contextual factors that can affect final impact.

The gold standard for showing evidence of results is to use control groups; however, they are expensive to carry out and, above all, they are applicable only when the intervention takes place at a relatively large scale.

The availability of track record, precedent experience, extensive research, control groups depends on the organization and the overall market stage of development.

For an organisation proposing a completely new idea, for instance, it is difficult to show evidence that the business approach will lead to the stated social impact; in that case, it is better to show how the different approaches have failed in the past and how this one has learned from them (Hornsby and Blumberg 2013).

Nevertheless, excessive investor demand for high levels of evidence could lead to prioritize mature organizations working with tried and tested methods, at the expense of investing in innovative and in some cases even more effective forms of intervention (Hornsby and Blumberg 2013).
Therefore, a good balance between innovation and certainty of results should be identified.

6)Evidenceable:
When there is less evidence available, it becomes increasingly important for the impact plan to be evidenceable (Hornsby and Blumberg 2013). This requires that a robust impact measurement system is in place to track outputs and outcomes.
Then, as the organisation carries out its plan, it is expected that its impact will become more evident and the social risk will diminish.
Alternatively, if the approach is failing, the presence of monitoring systems will be able to show this, giving the organization and the investor the opportunity to change the course of action (Hornsby and Blumberg 2013).

Bridges Impact Radar

The Bridges Ventures impact framework is based on a scoring approach which allows to assess the potential impact return and the related social risk of prospect investments.
In particular, it evaluates these two variables along four different dimensions: target outcomes, additionality, ESG, alignment.
For each dimension it is provided a question with three possible answers, each corresponding to a certain level of risk/ return, that goes from 1 to 3. The lower the score is, the lower the level of impact risk/ return.
A summary of the Bridges Impact Radar is reported in Table g; but only the part of the model that regards impact risk assessment is included.

Dimension	Key questions	Score	Scoring guide
Target outcomes	How well tested are the causal links in the logic model?	3 High	Credible secondary research evidences causality (in a different but comparable context)
		2 Medium	Credible secondary research evidences causality (in a different but comparable context), plus primary research supports causality (i.e. the organization own quantitative and qualitative assessment)
		1 Low	A scientific study (e.g. control trial or longitudinal study) evidences causality, demonstrating that the investment is generating impact
Additionality	Does the investment lead to outcomes which would not otherwise occur?	3 High	Likely displacement of comparable societal benefits (e.g. simply stealing market share with no impact value-add)
		2 Medium	Unlikely displacement of other comparable societal benefits due to increased quantity or quality addressing current market failure
		1 Low	Very unlikely displacement of comparable societal benefits due to increased quantity or quality addressing current market failure
ESG	Can any ESG risks be mitigated?	3 High	ESG risks cannot be mitigated
		2 Medium	ESG risks can be mitigated
		1 Low	Minimal ESG risk
Alignment	How fundamentally aligned is the business model with its generation of impact?	3 High	Many business success factors are not aligned with impact success factors
		2 Medium	Some business success factors are not aligned with impact success factors
		1 Low	All/most business success factors are aligned with impact success factors

Table g: Bridges Impact Radar, Bridges Ventures (2013)

The results of the above analysis are used to build the risk/return profile of each impact investment, as shown in Figure 10, which allows for easier comparisons among alternative investments.

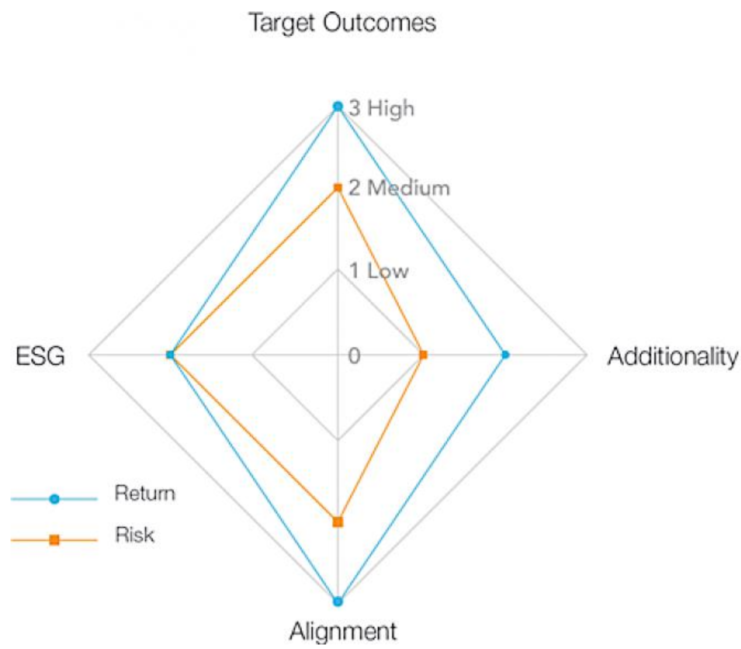

Figure 10: Risk/ Return profile, Bridges Ventures (2013)

SIB Scoring Model

The social risk evaluation system developed by Scognamiglio (2018) leverages on a credit scoring approach which is similar to one used for the evaluation of microcredit assets (Serrano-Cinca, Gutiérrez-Nieto, & Reyes 2013).
The model was built by choosing the criteria that could affect the results of a social initiative; these criteria were found through an intensive literature review and an analysis of the social impact bonds issued during last years.
The whole framework is represented in Table h.
As it is possible to observe, the factors used for the evaluation of social risk are divided in three main categories: program process, contractual conditions and evaluation methodology.
All the risk factors are then further split into relative sub-factors.
For any sub-factor it is specified a key question to which alternative responses are provided. To any response it is associated a certain social risk score, that ranges from 1 to 4. In general, the smaller is the number the lower is the risk level.
In order to get a unique value that represents the overall level of social risk connected to the program, a mathematical function is exploited.
The underlying idea is that the final score should include both objective and subjective factors.
The objective aspects are evidenced through the risk score assigned to any of the factors, since they only refer to the initiative under analysis and should not be influenced by subjective considerations of the evaluator.
The subjective aspect, instead, is included in the final score through the weights assigned to each risk factor. These weights, in fact, are determined by the evaluator.
According to the model, the importance of each risk factor and consequently its weight depends on the peculiarities of the project and the subjective opinion of the evaluator.
Once the weights are assigned, a weighted average is computed to get the final score that represents the overall social risk related to the program.

Risk category	Risk factor	Sub-factor	Key question	Options	Risk level
Program process	Program features	Duration of the program	How long is the project?	Less than 3 years	1
				From 3 to 5 years	2
				More than 5 years	3
		Pilot phase	Is present a pilot phase?	Yes	1
				No	2
		Empirical evidence	Is an evidence-based program? On which scale?	Evidence on large scale	1
				Evidence on small scale	2
				No evidence	3
	Service provider	Worker/target number relation	How many workers are present for each target group?	One-to-one	1
				No more than one to ten	2
				More than one to ten	3
		Number of service providers	How many service providers are involved?	From 3 to 5	1
				From 1 to 3	2
				More than 5	3
		Number of similar projects developed	How many similar projects had developed the service provider involved in this program that present more experience in the same area of intervention?	More than 10	1
				From 5 to 10	2
				Not more than 5	3
		Years of experience of service provider	How many years of experience have the older service provider involved in the program?	More than 10	1
				From 5 to 10	2
				Not more than 5	3
	Intermediary	Years of experience	How many years of experience has the intermediary?	More than 10	1
				From 5 to 10	2
				Not more than 5	3
		Skills relative to the program	Has the intermediary social, political and legislative skill relative to the program analyzed?	Yes	1
				No	2
Contractual conditions	Target variation	Variation of dimension	Does the contract permit the ongoing variation of target dimension?	Yes	1
				No	2
		Variation of typology	Does the contract permit the ongoing	Yes	1

			variation of target typology?	No	2
	Contest variation	Operative variation	Does the contract permit ongoing operative variation?	Yes	1
				No	2
		Governate variation	Does the contract permit the ongoing variation consequent to a policy change?	Yes	1
				No	2
		Social/ Local variation	The program is implemented in the same social and local contest?	Yes	1
				No	2
Evaluation methodology	Number of outcomes		How many outcomes are measured?	From 1 to 3	1
				From 3 to 5	2
				More than 5	3
	Evaluation methodology		Which methodology is used?	Experimental design that controls for both observed and unobserved variables	1
				Live but non-experimental counterfactual	2
				“Constructed” counterfactual with no live control	3
				No counterfactual	4

Table h: SIB Risk Scoring System, Sconamiglio et Al. (2018)

Highlights on Literature Analysis

A short recap of the major insights gathered through the literature review is here presented.

- The impact investing sector is becoming increasingly integrated into traditional financial markets and it is also receiving greater attention by big institutional investors, in 2019 The GIIN estimated the current size of the global impact investing market to be $502 billion;
- International institutions are fostering the growth of the social sector trough proper infrastructures – such as social impact measurement systems, standard financial products, reference frameworks regarding sectors of interest etc. – that simplify the impact investing process for asset managers, but still there are some issues that need to be solved;
- Impact investments have brought, for instance, to new types of risk that should be assessed: among them "social risk" has recently start being discussed among academics, but so far it is still a vague concept and few practitioners take it into consideration;
- Even biggest international institutions such as The GIIN or EVPA, which are committed to enable and align structures and processes used by impact investors worldwide, still do not provide any indication about how to consider social risk during the impact investing process;
- However, according to the latest interpretation of the impact investment paradigm social risk is considered as the fourth factor that, beyond financial risk, financial return and social impact, should likewise affect the investment selection; in particular, social risk evaluation allows to allocate resources into the most promising organizations;
- Only four different frameworks for assessing social risk have been developed so far; however, any of these tools remains an isolated reality, either because they are too restrictive or because the authors do not provide sufficient explanation on how to use them, thus remaining unappreciated by the vast majority of impact investors.

To sum up, the literature analysis has been useful to define the state-of-the-art of the impact investing ecosystem and in particular of the related social risk concept, considered one of the major gaps that need to be solved and that can bring social investors to invest in those projects that can be really transformative. This would also help not to lose the authentic mission of impact investments to “do good” and not just “feel good”.

OBJECTIVES

The addition of the impact purpose to traditional investments generated the need to include in the investment process a further analysis, beyond the financial one, aimed at evaluating the social performances that the investee organization can generate.

Social impact is difficult to quantify because of its qualitative nature and, in this regard, some methodologies have been designed by international institutions to support investors with the social due-diligence process.

Nevertheless, it is not enough to determine the expected impact of a social project but it is also important to assess its likelihood to happen, namely social risk.

In a market where demand of capital is high and resources are scarce, it is necessary to allocate them into those projects that could more likely generate positive outcomes on society.

The most recent studies on impact investing have shown that four different variables need to be examined during investment due-diligence: financial return, financial risk, social return and social risk.

While the first two – financial risk and financial return – are entrenched concepts and do not need further explanation, the social ones are not clear.

There are still diverse interpretations of the impact concept; for instance, controversial opinions exist about the additionality of green investing.

Some effort, however, has been given to define the boundaries of what is impact and what is not. In particular, this study refers to three different categories which allow to recognize true impact: intentionality (O' Donohoe et al. 2010; Harji and Jackson 2012; Brandstetter and Lehner 2015; The GIIN 2018; Tiresia 2019), additionality (O' Donohoe et al. 2010; Hebb 2013; Tiresia 2019) and measurability (Brest and Born 2013; So and Staskevicius 2015; Tiresia 2019).

Furthermore, even if a standardized impact measurement system has not been yet recognized, almost all impact investors and respective investee organizations are either adopting one of the impact frameworks proposed by big international institutions or have developed ad-hoc measurement solutions that better serve their needs.

On the contrary, the review of the literature reveals that few authors have tried to define social risk and, above that, find a way to assess its value; this explain why many investors focus the investment decisions only on the first three variables, neglecting social risk. However, social risk is important to monitor because sometimes it happens that the social project is not well-executed or that some unexpected events ruin or displace the impact.

Until now, no geographical distinction has been made. In order to concretize the assumptions made after the literature analysis about social risk, it was decided to deep dive on the Italian context, which still lacks adequate discussion.

In fact, as emerged in the literature, the majority of the case studies already addressed by scholars focus on US and UK contexts (Rizzello, Migliazza, Carè, & Trotta 2016; Agrawal and Hockerts 2019).

Nevertheless, since 2013 when the Italian Impact Investing Taskforce was established, a growing number of investors were attracted into the new market field – investment funds, pension funds, banks, venture capitalists, etc. – and an increased request from traditional social organizations as well as "profit with purpose" organizations was registered.

According to the analysis conducted by Tiresia in 2019, in Italy the total amount of assets under management considered "strictly impact", meaning that adhere to the three previously mentioned pillars that characterize impact investments – intentionality, measurability and additionality – is actually 210.5 million.

Although the Italian market is still small, especially in relation to its competitors in UK and US, it is rapidly evolving and the financial operators[3] are adapting tools and processes accordingly. For all these reasons, the Italian case should not be ignored.

The first objective of the study is therefore to examine the current Italian situation, in order to understand how impact investors are carrying out the investment activities and if they are taking into consideration "social risk" in the due-diligence process.

This would allow to verify if there is a correspondence between the academic definitions of social risk and its actual interpretation and operationalization within real investment cases.

[3] The term "operators" will be used in the text to indicate investors

Then, leveraging on the main insights gathered from the Italian case examination and from the literature review, the next intent is to *design a unique and comprehensive definition of the social risk concept applied to the impact investing context.*

After having clarified how social risk should be operationalized into the impact investment process, *we want also to provide the investor with a qualitative framework that can be used to assess the social risk level associated to any investment.*
This framework helps the investor to carry out the social risk analysis and further supports a common procedure for analyzing different organizations, allowing for meaningful comparison to feed into the investment decision.
In the following chapter it is explained how all these objectives have been met.

METHODOLOGY

Here the overall process followed in order to accomplish the objectives of the thesis is presented. First it is explained how the literature review was carried out, after that the Italian case study is outlined and, at the end, the procedures pursued for social risk definition and for the social risk framework design are clarified.

Literature Review

The starting point of this study was an in-depth literature review about how the impact investing field was born, its main features and actual issues to make it grow.

Among the major challenges identified, it was decided to focus the analysis on the least known and investigated concept, "social risk", which, however, is considered an important driver for impact investment decision making.

Two main sources were used to conduct the research: Google Scholar and Scopus, which are the most important online bibliographic databases where scientific works are stored. In addition, the websites of the most famous practitioners in the field were explored; in particular, The Global Impact Investing Network (The GIIN), the European Venture Philanthropy Association (EVPA), the Organization for Economic Cooperation and Development (OECD), the United Nations Global Compact, the Global Reporting Initiative (GRI), the Bridges Fund Management and Acumen Fund.

The same criteria were utilized for the research on the two databases.

At the beginning, to review the general context of impact finance, the following search strings were used: "welfare state crisis", "social enterprise", "social finance" and "impact investing". This analysis led to frame the main elements, mechanisms and infrastructures that actually characterize the impact investing market.

Then, new search strings were added to the group – "main challenges", "problems", "issues" – in order to investigate the actual concerns impact investors have to deal with. Through this analysis, different issues emerged: above all it was discovered that besides financial risks, the addition of the impact lens to investments has brought out new types of risk, among which social risk stands out.

From this point, the attention moved solely towards the social risk topic.

In order to gather a complete overview of its meaning, the term was initially separated from the context of interest, impact finance. The intent was to reveal if and how this concept has been used so far in other research fields.
To do that, only the string "social risk" was digited in the databases.
Immediately a correspondence with the social science field appeared and a first definition of social risk was discovered.
Then, the boundaries of the research were gradually restricted. The goal was to find out when this concept emerged within the financial landscape and how it has been defined.
In this case, search strings were built by matching couple of keywords, one linked to the research content and one to the context of analysis. The group of keywords regarding the content includes "Social risk", "Impact risk", "Risk" while the codes exploited for the context are "Finance", "Social finance", "Socially responsible investing", "Impact investing", "Impact investment", "Social impact bonds".
The abstract of any paper found with this method was analyzed in order to understand whether the report could be relevant for the study. In particular, only the papers that at least mention social risk/ impact risk within the selected context were used.
Once composed the dataset, the keywords "social risk" and "impact risk" were used to search in the articles the correlated definitions, where present.
Through this research, it has been discovered that the term has been defined both within the socially responsible investing literature and the impact finance literature but in different ways.

After having investigated the concept of social risk within the financial literature, the next step was to look when and how social risk should be taken into consideration by investors during the due-diligence process.
The methodology adopted for the research was the following.
The same sample of papers that were used for defining social risk was exploited.
Among these sources, only one was found that accurately describes all the phases of the impact investing process by integrating also social risk analysis into it – "The Good Investor" written by Hornsby and Blumberg in 2013.
The last part of the literature review was then dedicated to search for existing methods to assess the social risk associated to impact investments.

Once again, the dataset analyzed is composed of those reports previously examined because they aim at defining the social risk concept applied to the impact finance context. In particular, four different models were discovered:

- Standards of evidence, developed by Puttick and Ludlow for Nesta Foundation in 2012
- Six key qualities of an impact plan, developed by Hornsby and Blumberg in 2013
- The Bridges Impact Radar Methodology, developed by Bridges Ventures in 2013
- The Social Impact Bond Scoring Model, developed by Scognamiglio in 2018.

The literature review led to determine the objectives of the study whose methodology is presented in the next paragraphs.
The literature analysis also helped to build some assumptions regarding the definition of social risk and its operationalization into the investment process that were exploited together with the results gathered through the Italian case study to accomplish the objectives.

Italian Case Study

The first objective was to discover how those actors forming the Italian impact investing ecosystem define social risk and whether they consider it during the due-diligence process. In order to do that, a qualitative methodology has been exploited through **semi-structured interviews**. The conducted interviews were part of a much broader study regarding the current Italian impact investing situation, which covered several topics apart from social risk, on which this thesis concentrates.
The study was initiated by the Research Center Tiresia, whose major results are reflected in the Tiresia Impact Outlook 2019.
This report describes the current state-of-the-art of impact finance within the Italian landscape and offers some reflections on its possible future configuration.
The research was designed to read the entire ecosystem, analyzing the point of view of both the demand and supply side. In the following paragraph it is described how the research population was created.

Research sample selection

In order to constitute the research population, a twofold analysis was conducted.
First of all, to define the cluster of Italian impact investors, a desk analysis was conducted using the LexisNexis database, which allows to analyze the media exposure of specific topical themes.
In particular, some of the most common keywords in the impact investing literature were used for the research.
In this way, all press releases of Italian media concerning news about impact investors were collected in a database. Each press release was triangulated with the stakeholders' websites and official documents.
At the end of the screening process, 50 organizations were recognized as impact investors according to precise criteria which analyze their true intents, tools and strategies adopted.
In particular, it was decided to exclude those actors that are only devoted to advisory or that adopt an ESG/SRI perspective.
The resulting operators were contacted by e-mails and informed about the purpose of the research, in order to understand their willingness to take part in the project.
At the end 38, out of 50, were selected as sample for the study. A list of all the participants is provided in the Annex, Table p.
For privacy compliance the company names were transformed into codes which refer to the organization typology. For each one it is reported the legal residence, the geographical area of operations, the type of business meaning if it is specialized in impact investments or if it is of general interest but with some activities dedicated to impact, the entry year in the industry and the type of financing system: debt-base or equity-based.
Moreover, in Figure 11 the participants are graphically distributed by type of organization.
The main typologies identified are insurance companies, banks, family offices, foundations, SGR/venture capital and public financial institutions.

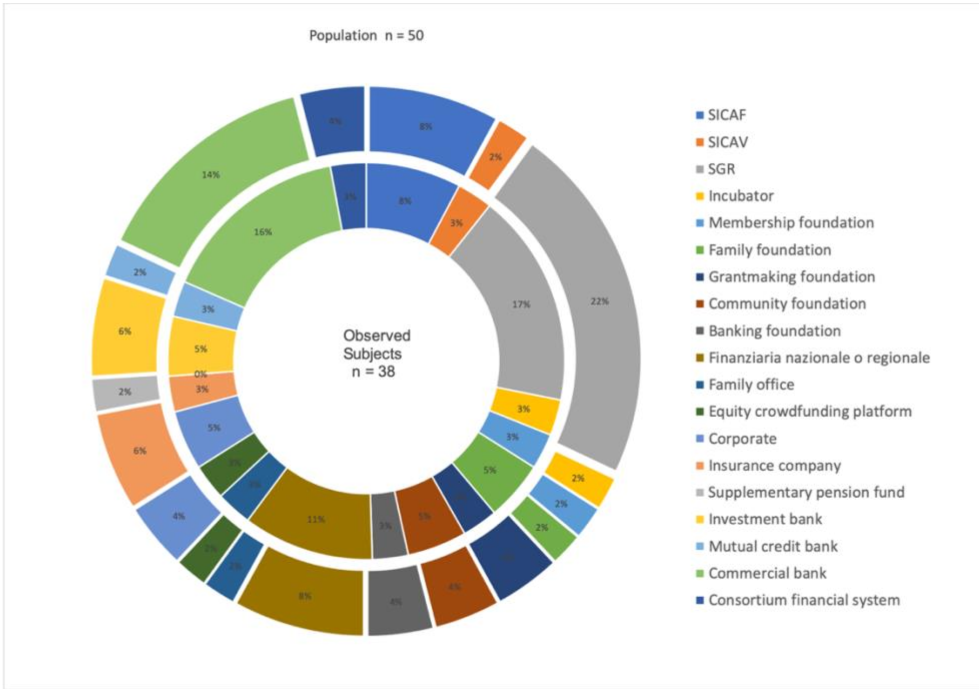

Figure 11: Target organizations typology, adapted from Tiresia (2019)

In order to create the population of investees, the following methodology was used.
The investing portfolios of those financial operators considered as "strictly impact", that constitute the supply sample, were mapped through an accurate desk research.
In this way, it was found that until today 40 different Italian organizations have been funded with impact finance instruments. In particular, these entities received investments from 2012 to 2019 as detailed in Figure 12.

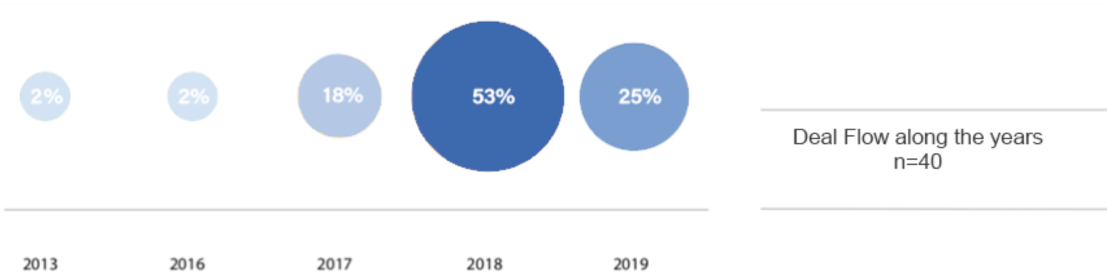

Figure 12: Impact Deal flow over the years, adapted from Tiresia (2019)

The organizations were contacted and only 20 of them agreed to take part to the study and be interviewed. A list with all the participants from the demand side is provided in the Annex, Table q. For each one it is reported the company typology, the legal residence, the sector of operations and the year in which it received the impact capital.
The main organization typologies identified are S.r.l., Social Ventures and Social Cooperatives; while regarding the sectors of operation the most common are culture and free time, healthcare, social housing, education and technology.
In conclusion, the total research sample, including both impact investors and investees, is made of 68 different actors.
In the next paragraph it is explained how the interviews were organized.

Data collection

Two interview protocols were built, one for investors and the other for investees.
It was asked to both group of actors a brief introduction regarding the company history and its approach to the social business. Then, it was asked their opinion about the impact investing main characteristics, its actual challenges and possible future developments of the phenomenon.
Some questions instead were personalized according to the type of actor; in particular, the main topics covered with the financial operators were: the impact strategy adopted, the volumes of impact capital provided until now and the investment process pursued.
On the other hand, with the investees it was discussed about their relationship with the investors in terms of influence in governance, negotiation process and monitoring of social objectives. One issue analyzed both with impact investors and investees is “social risk”, which is the focus of this study. In particular, it was asked to both how do they interpret social risk, providing three alternative definitions, that are diffused in the impact investing literature: a) the probability of generating a negative impact b) the probability of not reaching the social objectives set in the ex-ante phase c) the probability that the profit purpose will dominate on the social mission, thus undermining it, namely "mission drift". In addition to this, it was also investigated whether Italian investors are currently operationalizing social risk into their investment processes and if the financed organizations are considering it while setting their impact strategies.

Analyzing the point of view of both parties, supply and demand, was crucial to gather a complete picture of the impact investing ecosystem and to understand if they are aligned with each other's.

The interviews were performed between June and October 2019, each lasted from 30 to 80 minutes. They were conducted both face-to-face or via Skype/phone.

When allowed, the interviews were recorded and subsequently transcribed; when it was not possible to record them, notes were taken and subsequently enriched after the discussion. Among all the responses, only those that are related to the topic of this thesis were extracted from the transcriptions.

In the following paragraph it is presented how data analysis was handled.

Data analysis

The information retrieved with the semi-structured interviews were analyzed through a thematic analysis. The thematic analysis is the structuring and interpretation of collected data through the identification of recurrent themes. A theme represents a pattern or meaning, which captures something important in relation to the research question (Dixon-Woods, Agarwal, Jones, Young and Sutton, 2005).

In this case, the main categories were developed using a deductive approach, deriving them from the literature review.

For the whole research a qualitative data analysis software NVivo was exploited and findings were validated through a joined discussion.

Then, a further analysis of the information gathered about the social risk topic was conducted. Given the limited amount of information that we have, the responses of each interviewee were reviewed in details and, at the end, combined together, in order to reveal the common opinion about social risk definition and the current social risk evaluation practices within the Italian impact investing ecosystem.

The results gathered through the literature review and the empirical study have led to important conclusions which constituted the starting point for the framing and assessment of social risk, whose process is described in the following paragraphs.

The links between the interviews' outputs and the framework for social risk evaluation, instead, are explained in details in the Results chapter.

Social Risk Definition

After the empirical study of the Italian situation, the second objective of the thesis was to develop a unique definition of social risk applied to the impact investing context. This was done by revealing interpretative patterns among the definitions given by famous academics and practitioners, which are reported in the Literature Review chapter.
Due to the fact that impact risk is quite a new concept within impact finance and not many definitions have been found – thirteen in total – it was possible to determine a limited number of keywords, frequently repeated by the authors. These codes were then integrated together in a unique statement, which is presented in the Results chapter.

Framing social Risk

Once having clarified its concept, the following step was to investigate the main drivers of social risk that can jeopardize a project's expected social outcomes. To do that, a desktop analysis of the already utilized sources for social risk definition and social risk modeling was carried out. In fact, most of these factors populate the impact risk frameworks that have been presented in the last part of the Literature Review chapter.
A list of all the relevant risk categories was built, which has been the baseline for the social risk framework generation, explained as follows.

The first thing to do was modeling, which means deciding which structure the evaluation system has to assume.
The decision in this case was driven by the aim to provide a methodology suitable for all types of investors and therefore well-comprehensible and easy-to-use.
In particular, the model is organized in two levels: a first level made of aggregated macro-categories and a second made of more explicit variables derived from them.
The process to determine the macro-categories and related variables was the following. For each risk factor in the list it was determined one or more conditions that help to reduce the probability that the financed organization would not reach the expected social outcomes or, in other words, that mitigate the project's social risk.
These categories constitute the first level of our model. However, they are not enough specific and it is difficult for investors to understand what they need to check when

analyzing each category. For this reason, they were further split into several sub-categories that more evidently show a relationship with social risk. In particular, starting from seven different macro-categories the model explodes into thirteen variables.

They regard mostly the organization internal configuration: its mission, resources, activities, processes, outputs, measurement systems and past performance.

To evaluate the risk that a project deviates from expected outcomes, it is essential for the investor to "get inside" the investee organisation, including getting to know the management or entrepreneur in question, the vision and strategy that is driving operations. While for carrying out financial due-diligence it is investigated the organization business plan, in the case of social due-diligence the impact plan should drive the analysis to determine the potential impact and related social risk of a project.

For instance, any component of the impact value chain is included in the model: resources, activities, outputs and outcomes.

The social risk macro-categories are briefly displayed in Figure 13, but the complete framework will be presented and explained in the Results chapter.

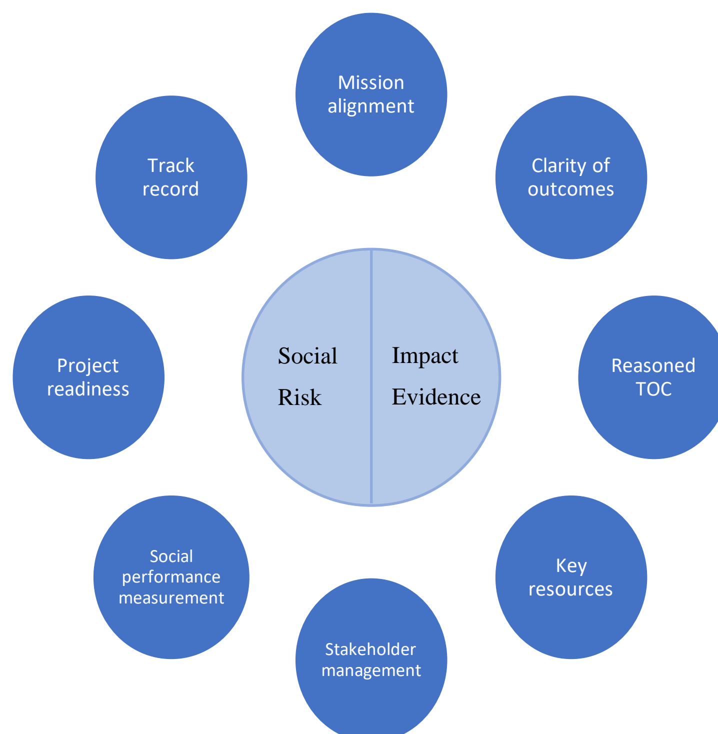

Figure 13: Social Risk Evaluation Framework macro-categories

To summarize, the social risk evaluation framework is organized as a checklist of variables, which mostly regard the investee organization’s strategy and internal management. These variables are crucial for the achievement of the social purpose and thus determine a lower impact risk.
In particular, the framework leverages on two main levels: one higher level composed of aggregated macro-categories which identify the specific aspects that needs to be considered and a lower one made of more concrete variables to monitor.
The investor needs to examine all these variables which all contribute to the social risk level connected to the investment under analysis.

After the modeling stage, the next step was to organize the evaluation approach.
Given the qualitative nature of social impact and due to the lack of real cases to analyze, it is difficult to estimate which variables are more relevant for risk mitigation and diversify their weights accordingly. Similarly, it was not possible to reasonably attribute a quantitative value that identifies the risk connected to each variable.
For these reasons, the score system methodology adopted in the recent model developed by the researcher Scognamiglio and in the one used by Bridges Ventures was excluded.
Despite these methodologies seem more precise and allow for easy comparisons among alternative investments, they were tested only on a limited number of cases and applied to restricted impact investment fields – this is the case of the Social Risk score system developed by Scognamiglio, which focus only on Social Impact Bonds.
On the contrary, our model was designed to be applicable to each type of impact investment, and the value-added lies in the fact that it integrates all the information included in the existing frameworks together with the most relevant findings gathered through the interviews.
A qualitative evaluation was designed. For each variable it was provided a thorough explanation that helps the investor to understand if the company/ project under analysis satisfies the requirements or not. In case these are accomplished, the investor attributes a low risk, while in the other case a high risk is assigned.

Of course, the lower is the number of mitigation variables satisfied by the organization the higher is the risk that the investee would not reach the intended social outcomes and, consequently, the financial operator should be less willing to invest in that project.
This model is also useful to discover which are the main problems that can make the social organizations to deviated from expected results. This would help investors to support their clients in the weaker aspects of their strategy and execution, that need to be improved in order to increase evidence of future impact.
Further explanations regarding the framework's characteristics and logic will be provided in the following chapter.
Due to the fact that impact investing has just few years of history but usually these types of investment have a long-term maturity, it is not possible to find a sample of cases sufficiently big for conducting an empirical analysis to validate the model.
However, it is worth highlighting that all the variables included in the framework result from an accurate desk research about the major issues spotted by academics and practitioners with long experience in the field.
Their concepts in some cases have been reworked and further analyzed, but nothing has been invented.

RESULTS

This chapter aims first to present all the insights gathered from the semi-structured interviews conducted both with the Italian investors and the investee organizations who received impact funds from them in the last few years. Among the topics covered during the interviews the social risk issue, which is the focus of this study, is selected and discusses in details. The Italian case analysis is fundamental both because it shows which are the major gaps that need to be addressed to smooth and make the investment process more efficient but it also gives some hints on how to build the social risk assessment framework.

Leveraging on the findings gathered from the empirical case study, the attention moves to the framing and assessment of social risk.

In order to assess social risk a standard framework is designed, which includes all the variables that are affecting impact risk and thus need to be monitored during impact investment due-diligence.

Italian Case Study

As introduced in the methodology, the interviews have covered different topics regarding both the investors and investees' strategies and activities.

The main intent was to clarify how the former are carrying out the investment process, in particular how they build their pipeline of customers, how they conduct the screening activities, which criteria they utilize to select the investees, which types of additional services they offer to their clients and how they keep track of the social results obtained with the investment.

Similar issues were discussed also with the investee organizations, in order to understand their opinion and experience with impact investments and in order to look whether the two parties, demand and supply, are aligned with each other's.

The first issue here discussed regards the methodology followed by financial operators to build their own pipeline of customers. In particular, three main behaviors were identified through the interviews:

- **Proactive**: the investor looks for potential target customers
- **Reactive**: the investor is contacted by potential customers
- **Ecosystem**: the investor and potential client know each other's through a network of shared relationships

It came out that the preferred behaviors by impact investors are the first and the third one. A proactive behavior entails setting up more structured screening procedures, for instance, leveraging on intermediaries. On the other hand, many think to have more probability to find the right client through the consolidated networks of relationships that they have established over the years. This opinion is also shared by the investees, who believe that systemic relationships are the best way to attract investors.
The reactive behavior, instead, is less used. To this cluster belongs one participant that declared to "have put in place a website, on which there is an online form, accessible by anyone, where the investment proposals are collected" (S-SGR3, Table p).
This alternative for sure would reduce the time spent by financial operators at the beginning to search for potential customers; but since anyone could apply, there are often many applicants who are not in line with the investor preferences and expectations and therefore the following screening process will be more time consuming.

Both for investors and for investees it was built a graph that catches their preferences regarding how to attract prospect investees/ investors reported in Figure 14 and 15.

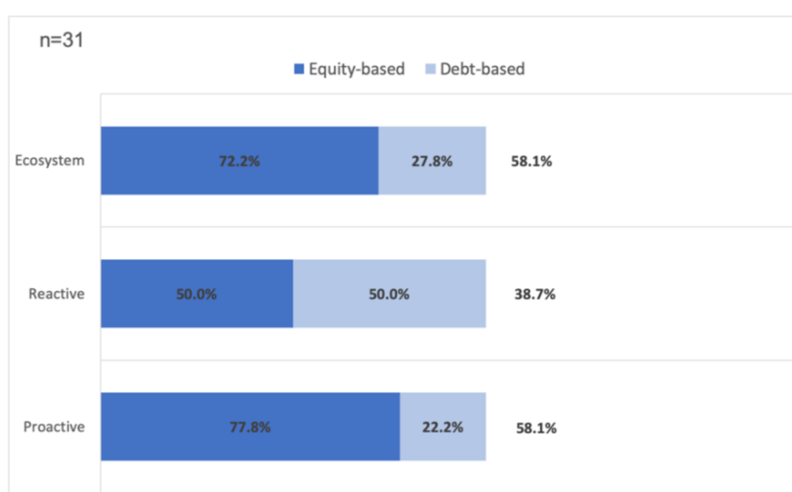

Figure 14: Scouting behavior of impact investors, adapted from Tiresia (2019)

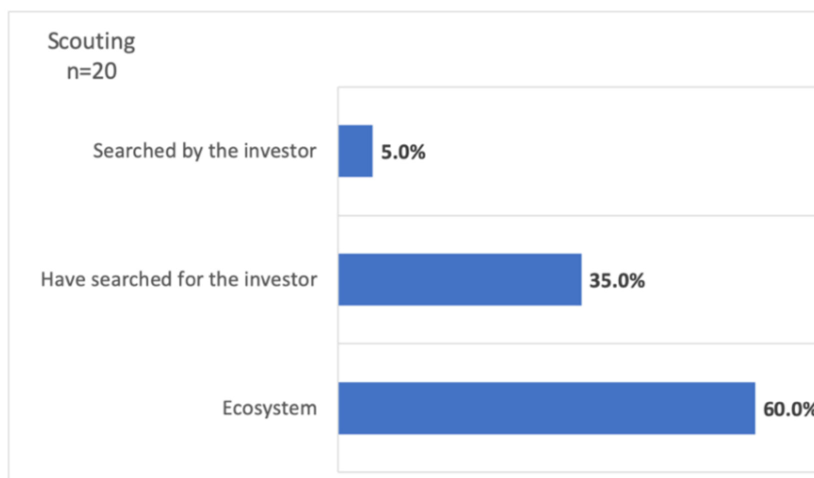

Figure 15: Investee approach to attract investors, adapted from Tiresia (2019)

Once clarified how the pipeline of potential clients is built, it was investigated the screening process followed by investors.

In particular, it was asked to them which are the main criteria that they consider in order to understand if a project could be successful and therefore allocate resources into it.

The most common criteria with the respective percentage of adoption are shown in Figure 16. It came out that the characteristics of the business model in terms of credibility of the business plan, financial sustainability and presence of subjects offering comparable products/services are the elements that matter most for investors.

One operator, for instance, highlighted that "the self-sustainability that emerges from an organization business plan needs to be assessed, because if that is missing it will be difficult also to reach and scale up the social results" (S-CF2, Table p).

Moreover, almost 67% of operators thinks that the expected social impact or the capacity of the entrepreneurial project to respond to a social problem need to be assessed.

In this regard, the investor should look at the organization impact mission and the context in which the project is inserted. There is one respondent who declared that "the analysis of the territory is very important because most of the times social problems are peculiar to the geographical area served by the organization, who has to focus on the most urgent customer needs" (S-SGR4, Table p).

The team is another important category that emerged from the interviews. In particular, it refers to the managerial and technical skills of employees and the team social commitment and internal cohesion. Many of the investors agree that intentionality is a key criterion for the success of a social project. In particular, one of them explained that

"making early-stage investments (during organization seed and pre-seed phase) implies that very often no track record exists and the team becomes a fundamental factor that demonstrates the ability to produce social benefits" (S-SICAV1, Table p).
Other criteria utilized by impact investors are the governance structure, personnel management policies and the state of progress of the project. Regarding the last issue, one of the respondents affirmed that "social risk changes according to the level of maturity of the organization" (S-SGR7, Table p). For instance, start-ups have no track record and usually less experience and resources and bigger is the risk for them to deviate from expected outcomes. For these reasons, "It can happen that they realize on the go that their business idea is not applicable and they need to change their scope or even close the business" (S-SGR7, Table p).

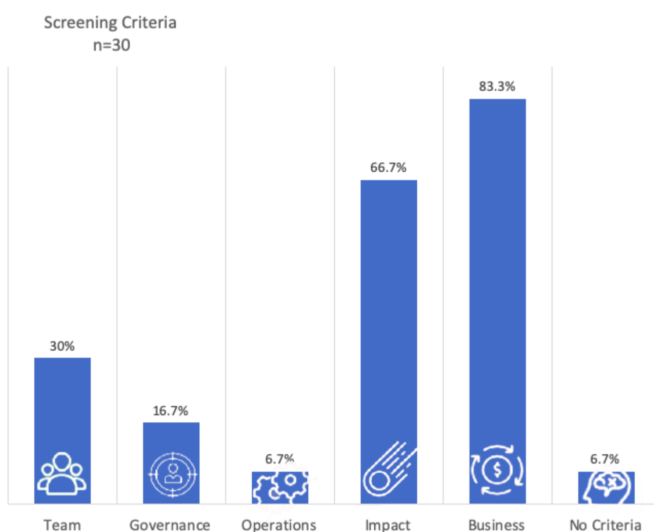

Figure 16: Screening Criteria, adapted from Tiresia (2019)

Besides the main criteria utilized for investment screening, it was also discovered that the process is carried out in different ways: there are financial operators that prefer to conduct an internal analysis by reviewing the company's financial and social documents, while others prefer to establish a direct contact with the organizations by organizing meetings from the first stages of the process or, in case this is not possible, through questionnaires. One interviewee explained that "the screening process output is an evaluation form which describes the company in details, in particular focusing on the pre-established selection criteria" (S-CB4, Table p).

One topic covered during the interviews with both parties, investors and investees, is the social performance monitoring.

In particular, it was asked to them whether any target result has been set in the deal contract and which types of social dimensions are monitored.

Both the investors and respective investees declared that project outputs are always taken into consideration, while only in the 25 % of the cases monitoring and evaluation also include social outcomes and impact. This is shown in Figure 17.

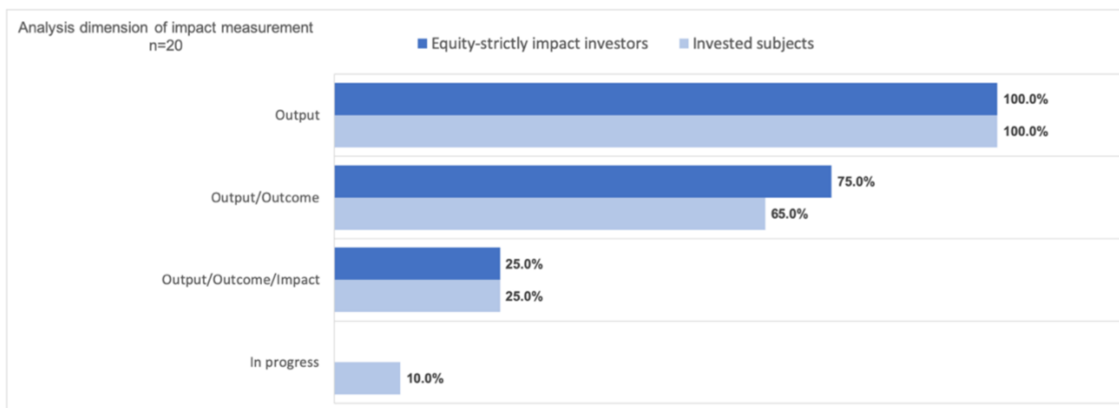

Figure 17: Social measurement dimensions, adapted from Tiresia (2019)

Regarding measurement systems adopted by investors, the use of proprietary methods prevails (57.1%) and sometimes they even develop ad-hoc measures for each investee organization.

The other group of investors instead makes use of internationally recognized methodologies, among which the most common are IRIS set of indicators, the Theory of Change with related KPIs and the Social Return on Investment (SROI), represented in Figure 18 with the respective percentage of usage[4].

[4] The operators who declared to be still in the development phase did not answer to the question about the social measurement system utilized

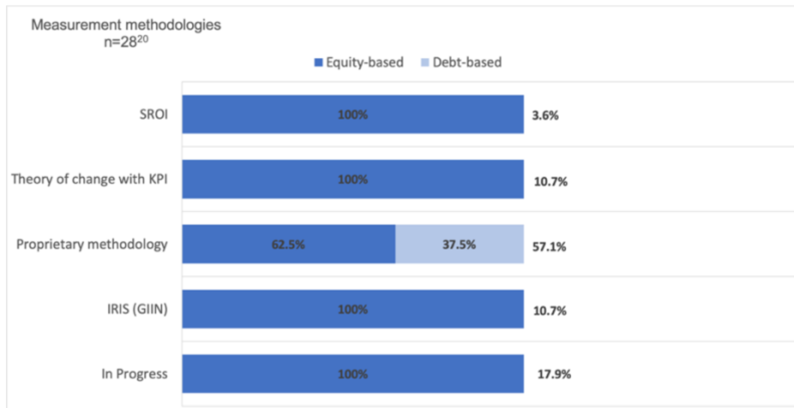

Figure 18: Measurement methodologies, adapted from Tiresia (2019)

Regarding the implementation phase of the social evaluation, not all the financial operators are implementing it ex-ante; instead, ongoing monitoring and ex-post verification of social results are more common, as shown in Figure 19[5].

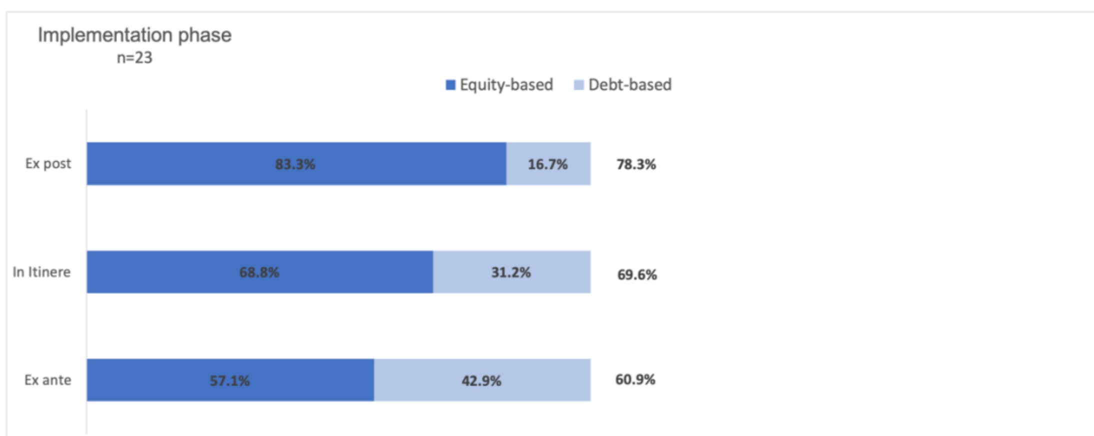

Figure 19: Social Impact measurement implementation phase, adapted from Tiresia (2019)

The financial operators that set up specific target outcomes in the investment contract sometimes link the achievement of these with financial benefits, for example, through a discount in the interest rates. In this respect, there was one respondent who said that "The

[5] The question regarding the social measurement implementation phase was asked only to the operators who declared to measure impact

achievement of social results must be recognize and recognition could be traduced in a financial reward through a discount in the in the loan rates" (S-CB5, Table p).

Another topic that was analyzed regards the additional services which normally are added to the financial resources.

Not all investors provide the same kinds of services to their investees. It was discovered that, both according to the investors and investees' opinion, the most common one is the introduction into relevant networks. Partnerships, in fact, often facilitate the organization activities and allow them to discover best practices to apply in their business processes. Furthermore, capacity building, trainings and incubation programs are common and in the same way help social organizations to improve their managerial and social skills, increasing the probability to reach the expected social impact.

All the types of non-financial support with the respective percentages of utilization, according to investors and investees, are provided in Figure 20 and 21.

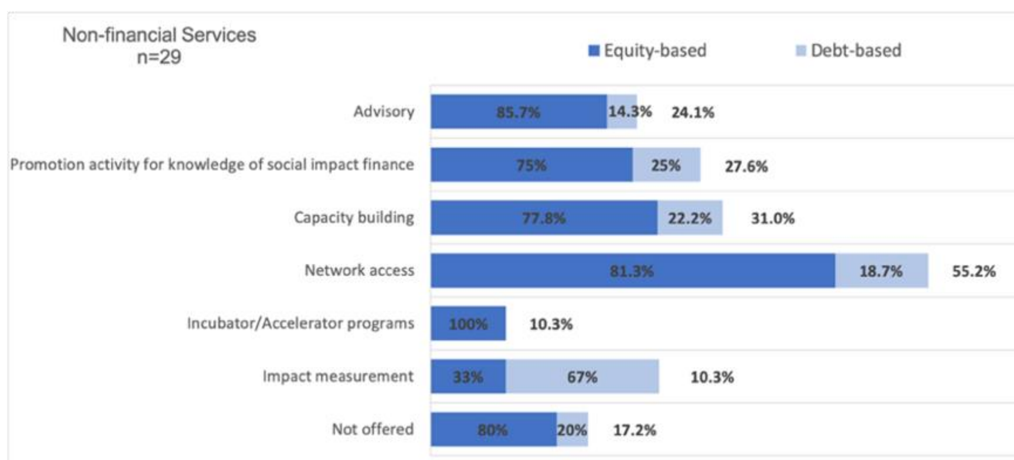

Figure 20: Non-financial services provided according to investors, adapted from Tiresia (2019)

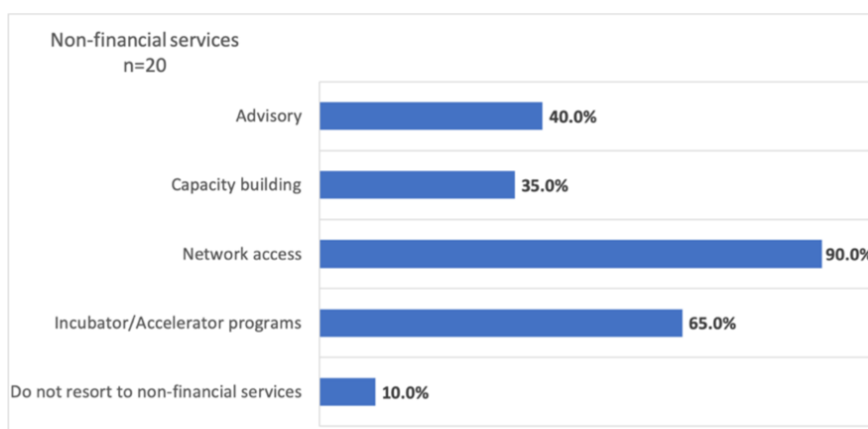

Figure 21: Non-financial services provided according to investees, adapted from Tiresia (2019)

Moving to the central topic of this study, social risk, these were the major insights gathered from the interviews. Regarding the interviewees' opinion about social risk definition, it was determined a unique figure by putting together all the responses given by investors and investees. In particular, 67.7% of the respondents agreed with the second definition, while 45.2% were in accordance with the first and 41.9% with the third, as represented in Figure 22.

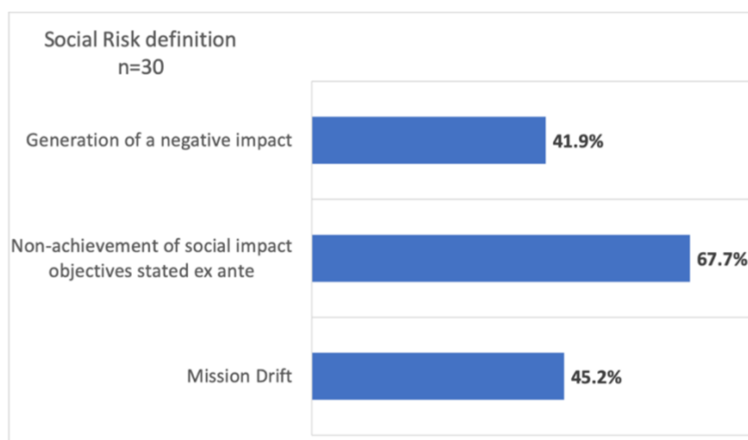

Figure 22: Social Risk definition, adapted from Tiresia (2019)

From the interviewees' responses it came out that, at the moment, social risk evaluation is not organized in a structured way neither by investors in their due-diligence activities nor by investees when setting up their impact strategy.

The majority of the investees have shown to be skeptical about the benefits obtained from assessing social risk.

One participant said "to have never thought about the possibility of not reaching the intended social returns because impact is always the first concern in all the decisions and activities carried out" (D-SRL4, Table q).

This means that anything that can make the project to deviate from expected performances is proactively managed by the team and resources allocated for solving the problem. Another investee stated that "negative externalities of course can happen and some are difficult to prevent and mitigate, but since the project's social results are constantly monitored, they can understand when something goes wrong and need to be adjusted" (D-SRL4, Table q).

On the other hand, 45.1 % of the investors declared that they are currently addressing social risk in their investment process. In particular, these subjects interpret the impact risk as shown in Figure 23.

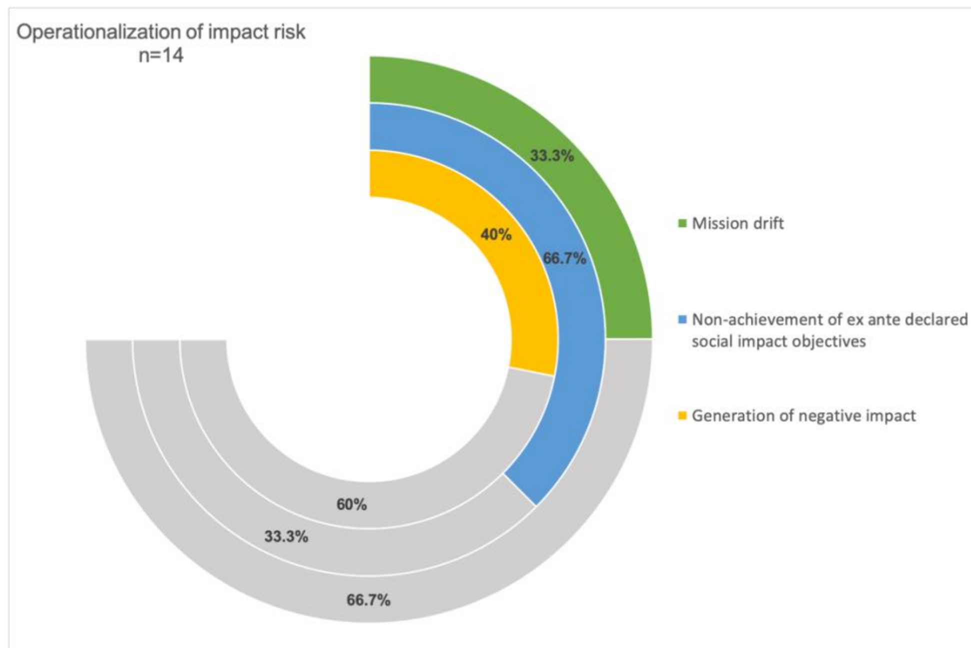

Figure 23: Operationalization of impact risk, adapted from Tiresia (2019)

All the investors exclude an ex-ante evaluation of social risk, meaning that they do not consider it as a critical variable for investment decision-making. The ongoing measurement of social results, instead, is the method by which investors manage to control impact risk, ensuring that there are not excessive deviations with respect to the impact objectives agreed in the investment contract. Only few respondents, in particular, are defining standard procedures for managing social risk.

For instance, there is one investor which is trying to build a sort of "Impact Appetite Framework", that for how it is structured is similar to the Risk Appetite Framework used by banks to monitor financial risks. "It is made of 20 indicators related to different aspects of the investee organization – such as the governance systems and the sector of interest – whose value cannot go below certain levels, in order to ensure that its activities continue to be impactful" (S-IB1, Table p).

Another relevant response comes from a banking foundation saying that "they are currently taking into consideration social risk but in a very informal way, in the sense that while doing the screening process they evaluate also the possibility that the social impact would be not enough significant; however, there is not a structured approach and the evaluation is linked to the sensitivity of the individual" (S-BF2, Table p).
One declared "to take into consideration social risk when the project is ongoing and the first results occur. Then, when a deviation from target outcomes appears, sometimes the contract allows them to exit the investment or alternatively, in case of equity investments, to remove and substitute the management of the organization" (S-GF1, Table p).
Similarly, one advisor that is supporting local territory infrastructures, admitted that "they haven't planned to assess social risk of the financed projects; however, they think that in large part this risk is mitigated with an intensive monitoring during the whole duration of the investment" (S-SICAV, Table p).

In summary, these are the most relevant results that came out from the interviews with impact investors and investee forming the Italian ecosystem.
The investment process is not equal for all the investors: some diversities have been found in the construction of the pipeline of customers, in the screening process carried out and the selection criteria utilized for the investment decision.
The approaches to social evaluation still poorly reflect the notion of impact sought and often limit the measurement to goods and services produced, leaving out the related social outcomes created on beneficiaries.
There is no convergence on the notion of impact risk among investees and investors.
The latter are still in the first stages of the process to concretize social risk evaluation in the investment approach, while the others are even not sure about the benefits of considering it in their impact strategies.
These results show a difference between how social risk is managed by Italian impact operators and how those pioneers in the impact investing industry, most of them based in UK (e.g. Bridges Ventures, Nesta Foundation, etc.), handle it.
In fact, the latter are convinced that social risk evaluation should be carried out ex-ante, and its value balanced with the other three variables – financial risk, return and social impact – relevant for investment decision-making.

The empirical study was fundamental to discover the state-of-the-art of the Italian impact investing ecosystem and the main gaps with regard to the investment process.
In particular, regarding social risk there is still not a structured approach for taking it into consideration from the first phases of the investment process, when the investee social potential is questioned. Nevertheless, all investors are adopting certain criteria for customer screening which mostly regard the company's internal structure, strategy and main intents. These elements affect the capacity of the investee to reach its objectives, both from a financial and social standpoint.
Therefore, they are connected in a certain sense to the risk that the company would not deliver on its proposed impact. They also remind to the main drivers of risk that populate the models presented in the Literature Review chapter.
For these reasons, the screening criteria identified have been crucial for the design of the social risk evaluation framework. In the next paragraphs, we are going to see that most of them constitute the variables included in the model for mitigating social risk.
In addition to this, the empirical study also led to interesting intuitions to be exploited in the framework. First of all, it came out that both for investors and investees it is important to set up a direct relationship. This helps investors to capture the needs of the customers and shape the investment contract accordingly but also to have a more complete understanding of their potential.
Furthermore, it was shown that those services provided in addition to financial resources – such as managerial support or access to important networks – are key drivers for the success of the investee's social businesses.
Last evidence from the empirical study is that there are investors that have put in practice some forms of "mission lock" or financial incentives to make their customers to stick to the social mission. For instance, payment-by-results structures are exploited but also contracts that allow the investor to exit the deal in case the customer is not adhering to the pre-agreed conditions. All these expedients are exploited in the approach to social risk mitigation that is explained in the next paragraphs.
The relevant findings gathered from the Italian case study analysis are summarized in Table i.

Main Findings	**Conclusions**
There is no convergence on the definition of social risk among investors and investees.	This confirmed the assumption made after the literature review: there is the need to better define social risk applied to the impact investment context.
Some investors do not include social risk in the investment process while others are organizing structured approach in order to manage it. Nevertheless, in most cases the evaluation is not carried out ex-ante but rather when the project is ongoing.	It is necessary to design a standard system for social risk evaluation to be used by investors during impact due-diligence.
The majority of the investors adopts similar criteria for investment screening. These criteria mostly regard the organization's managerial process, resources, activities and main intents and affect the project performances, that means both financial and social returns. Indeed they influence the social risk of the project. However, there is not a structured approach to evaluate them.	These criteria need to be included in a standard framework for social risk evaluation, where their relationship with social risk is also explained.
Both investors and investees are favorable to set up a direct relationship with each other's. This in fact helps them to align their interests and objectives.	A participatory due-diligence can be crucial for social risk evaluation, since it helps investors to gather more concrete evidence about the real intentions and capacity of the investees. It can also help investors to understand which are the main problems that affect the performances of the clients and that need to be solved through proper mitigation measures.
Investors often provide other services in addition to the financial resources aimed at supporting the investees with the implementation of the business idea. The most frequent ones are: providing access to important networks, managerial support, incubation programs, support with social impact measurement. These additional services are important means to avoid project failure.	Non-financial services provided by impact investors can be seen as mitigation activities that can be used to reduce the social risk connected to a certain investment.
There are investors that set up some rules that guarantee the possibility to exit the deal should the investee deviate from the social mission. To avoid this event to happen, others instead link social returns to financial benefits.	These two strategies can be exploited for mitigating social risk when setting up the investment contract.

Table i: Relevant findings from the Italian case study

Social Risk Definition

The first thing that was done after the literature review and the Italian case study analysis was to better define the social risk concept applied to the impact investing context. In particular, it was formulated a unique definition of social risk by extrapolating the most relevant information retrieved from the literature review.

In the social risk definitions provided by scholars three main key expressions have been identified. The first keyword is **"uncertainty"**, which is a common term used in relation to risk. Risk in fact refers to something that is not sure to happen due to contingent factors. In particular, if applied to a business context, it means that not always planned actions lead to the expected results due to internal causes, that are for instance under the manager or employees' control, or to external ones that cannot be foreseen. In fact, even if the business strategy is well executed and the entrepreneur is devoted to the social purpose, it can happen that, either the market response deviates from predictions or unexpected accidents raise some problems that can affect the project's performance. To express the same thing, it is also adopted the word **"likelihood"**. All the definitions in which compares these two alternative words are reported in Table j.

Definition	Author/s
"The uncertainty of generating the intended impact"	S. Godeke and R. Pomares
"Impact risk is a concept we have developed to give an indication of the certainty that an output will lead to the stated impact"	R. Puttick and J. Ludlow
"Impact risk is a measure of the certainty that an organization will deliver on its proposed impact (as detailed in the impact plan). The question is: How sure is the impact plan to work and what is the risk that the impact won't be generated?"	A. Hornsby and G. Blumberg
"Social risk refers to the uncertainty about and severity of the events and consequences of an activity with respect to something that human value"	H. Mahmoudi, O. Renn, F. Vanclay, V. Hoffmann, & E. Karami
"The social risk can be defined as the likelihood that a given allocation of capital will generate the expected social outcomes irrespective of any financial returns or losses"	A. Nicholls

Table j: Social Risk definitions that include the keyword "uncertainty"/ "likelihood"

Uncertainty of results is very generic and can be referred to any type of risk. This is why in the definitions it is underlined the kind of performances we have to look at when addressing social risk. The authors connect social risk to the uncertainty of **"expected social outcomes"** or alternatively of **"intended impact"**.

For instance, Nicholls (2015) wrote that "*Social risk can be defined as the likelihood that a given allocation of capital will generate the expected social outcomes irrespective of any financial returns or losses*".

All the definitions that adopt these expressions are listed in the Table k.

Definition	**Author/s**
"The uncertainty of generating the intended impact"	S. Godeke and R. Pomares
"Impact risk is a concept we have developed to give an indication of the certainty that an output will lead to the stated impact"	R. Puttick and J. Ludlow
"Impact risk is a measure of the certainty that an organization will deliver on its proposed impact (as detailed in the impact plan). The question is: How sure is the impact plan to work and what is the risk that the impact won't be generated?"	A. Hornsby and G. Blumberg
"While some authors interpret social risk solely as the risk of not reaching the intended impact, others apply a broader lens including for example exit risk, liquidity risk, measurement risk or unquantifiable risks"	L. Brandstetter and M. Lehrer
"Impact risks can take various forms. For example, there may be a lack of evidence that an intervention will lead to the desired outcome. Even if the intervention is successful, the investment could cause displacement, leading to reduced or no net benefit"	C. Barby and J. Gan
"The social risk can be defined as the likelihood that a given allocation of capital will generate the expected social outcomes irrespective of any financial returns or losses"	A. Nicholls
"Social risk is used to identify the possibility that the expected social outcome is not achieved due to unpredictable events"	H. Chiappini

Table k: Social Risk definitions that include the key expression "expected social outcomes"

Indeed, a deviation between expected and actual social results can occur and the probability of these event to happen is also called social risk.
Of course, deviations can be slightly or huge, sometimes even reaching *"negative social impact despite the well-intended investment motives"* as stated by Lehrer (2016).
This definition introduces the third element that helps to delineate social risk which is **"negative social impact"**, probably the worst thing that can happen when investing in an organization aimed at creating social value.
However, just few authors include this aspect into their social risk definitions, mentioned in Table l.

Definition	Author/s
"How interventions and investment practices might have negative social returns"	S. Geobey, R. Westley, & Weber
"Social risk has not been fully conceptualized at present; it ranges from negative social impact despite the well-intended investment motives, to opportunity costs because of an adverse selection of impact projects that fail to deliver"	M. Lehrer

Table l: Social Risk definitions that include the key expression "negative outcomes"

By putting together the main elements found in the different definitions of social risk – "uncertainty"/ "likelihood", "expected social outcomes"/ "intended impact", "negative social impact" – a unique and clear definition has been developed.
"Social risk is defined as the ***likelihood*** *that the* ***social outcome*** *of a financed project is* ***lower*** *than expected,* ***null*** *or even* ***negative****, therefore worsening the actual social conditions".*

In the definitions found in the literature two further keywords appeared – "displacement" and "mission drift" – but it has been decided not to include them in the above statement. This because they are rather interpreted as risk factors that can lead the investee to deviate from expected outcomes.
Therefore, they will be discussed in the next paragraph as main drivers for social risk.

Framing Social Risk

As it was described in the methodology chapter, the first step for the development of the social risk framework was to discover the main factors that, according to academics and practitioners, affect the risk to generate a reduced, null or even negative impact.

As Lehrer stated (2016) *"Risk is multi-factored, meaning that it can be driven by a set of different factors that combined together could lead project's outcomes to deviate from expectations."*

There is never one reason for why plans go wrong. Usually, the negative outcomes of a project trace back to a set of different causes; and this is true also for social outcomes.

In Table m, all the social risk categories identified through the desktop review are listed. For each factor the respective author/s, source, definition and date are provided.

Author/s	**Source**	**Risk Factor Definition**	**Year**
Y. Saltuk	A portfolio approach to impact investments	**Early stage of the market**: *Risk might arise from the market's small size, the short track record of performance and the fund managers inexperience at delivering on dual-return objectives.* **Ecosystem**: *The impact investment market is largely dependent on ecosystem components such as policy support and impact measurement infrastructure under development.* **Mission drift**: *The risk that investees drift away from the intended mission without the approval of the investors or that investors nudge investees prior towards commercial goals.*	2012
J. Emerson	Risk, return and impact: understanding diversification and performance within an impact investing portfolio	**Measurement and reporting:** *Given the challenges and difficulties in measuring social and environmental impact, investors may be exposed to inaccurate assessment of outcomes.*	2012

R. Puttick and J. Ludlow	Standards of evidence for impact investing	**Impact evidence**: *Impact risk can be reduced by strengthening the evidence that helps to demonstrate investees will reach intended impact.*	2013
A. Hornsby and G. Blumberg	The good investor. A book of best impact practice	**Validity of the impact plan**: *The assessment of impact risk appraises the plan for its validity, and for the confidence it inspires that the organisation, through carrying out its activities and delivering its outputs, will achieve the intended outcomes, and generate real positive change.*	2013
C. Barby and J. Gan	Shifting the lens: A de-risking toolkit for impact investment	**Displacement**: It *occurs when the positive outcomes experienced by beneficiaries of a product or service are offset by negative outcomes experienced by another group elsewhere, this will lead to reduced or no net benefits.*	2014
E. Sconamiglio, A. Rizzello, & H. Chiappini	Evaluation of social risk in the social impact investing	**Program process:** *The duration of a program, the presence of a pilot phase and the experience of operators can influence the social outcomes of a project.* **Contractual conditions:** *The possibility to change outcomes and conditions established at the beginning can influence the social outcomes of a project.* **Evaluation methodology:** *Higher is the number of different outcomes planned higher is the social risk of the project, the type of measurement methodology adopted can influence the social risk of the project.*	2018

Table m: Social Risk factors retrieved from the Impact Investing Literature

Furthermore, this reflection was done: the social risk factors can be attributable to different actors within the impact investing model – the investor, the investee or the external context.

Social risk can depend on the investee organization’s fault; for instance, it can happen that the impact plan and underlying theory of change are not well-structured due to a lack of management expertise. It depends also on the investor’s defect; for example, when he prioritizes financial results and brings the financed organization to give up a portion of social outcomes in favor of higher profits, drifting away from the impact mission. In this

regard, one issue that was discussed during the Tiresia Impact Outlook 2019 is that, at present, many investors are either doing impact investments only for marketing reasons or are still inexperienced at delivering on dual return objectives since they have just entered the social sector. This could lead to wrongly select the organizations with high risk of impact failure or sometimes to draw up contractual terms that prioritize financial returns.

Then, social risk can hinge on the context in which the social business is operated, which can change casually its configurations due to contingent factors, such as natural hazards, or economic and legal factors that are not under the organization control and could damage the project's expected results. However, these contingent risks, which affect also traditional investments, are difficult to be foreseen; this is why they have been excluded from the social risk framework that has been designed.

Furthermore, social risk does not only derive from one of the three agents, but also depends on the interactions among them. For instance, interorganizational misalignment between the investor's goals and the investee's mission and actions could potentially undermine the social performances of the investee and damage the reputation of the impact investor (Agrawal and Hockerts 2019).

It is clear that the failure of the investment's social goals is caused not only by a poor management or feeble social intents of the financed organization but also by the investor himself and the surrounding context. However, the social risk framework that is described in the next paragraph was meant to be used by impact investors for identifying the social risk level connected to each prospect client. This is why the contextual factors and those problems connected to investors' inexperience or bad intentions are left out from the scope of the model. In particular, the risk factors that are mostly related to the context and investors' faults and thus excluded from the framework are ecosystem risk, early stage of the market and contractual conditions.

Social Risk Evaluation Framework

In this paragraph the social risk framework that has been designed is exhibited and explained in details. As it was prior clarified in the methodology, the model is composed of two levels, a higher level made of more general macro-categories and a lower one

made of more specific variables. The higher level is represented in Figure 24, which includes the risk factors with the derived mitigation categories.

All the categories included in the model were found in the literature and sometimes reworked. Many of them also remind to the screening criteria that have been discovered through the empirical study.

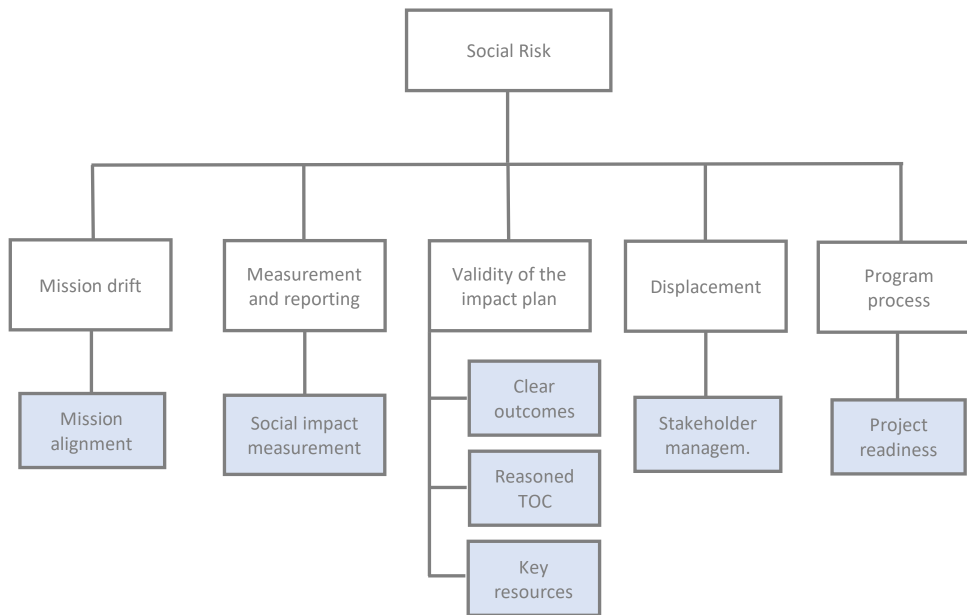

Figure 24: Social Risk factors and derived mitigation categories

Impact evidence, which is in the list of social risk factors provided before, is excluded from this scheme. The reason is that impact evidence comprehends all the others factors and can be seen as a transversal category. For instance, an early stage of the market equals saying that there are few comparable products/services in the market or even none showing evidence that the business idea could work and generate positive outcomes.

Similarly, a social measurement and reporting system helps entrepreneurs to track their daily project performances: this allows to increase evidence of future impact.

Impact evidence is also one of the key features, according to Horsnby and Blumberg (2013), that prove the validity of an impact plan. Furthermore, program process, which is one of the risk categories in the model developed by the researcher Scognamiglio (2018), refers to the current stage of the project, meaning early-stage, growth or maturity; in general, the more advanced is the project phase the higher is the evidence of future impact.

Impact Evidence is inversely proportional to social risk, meaning that when the first is

increasing the latter is decreasing, and both are influenced by the variables that populate the social risk framework developed.

The complete framework with the macro-categories and related sub-categories is presented in Table n. It is also included a short explanation of how each variable affects social risk.

Macro-category	**Sub-category**	**Short Explanation**
1.Mission Alignment	**1.1**Balance between social and financial mission	If financial objectives are aligned with impact outcomes it means that the achievement of the former would also encourage the realization of the latter, therefore decreasing the probability of mission drift.
	1.2 Legal and Governance structures	Legal restrictions and governance rules that drive the entrepreneur and employees to stick to the social mission are useful means to avoid prioritizing financial returns and thus decreasing the probability of mission drift.
2.Clarity of outcomes	**2.1**Quantitative/Qualitative target results	If a project's social objectives are not vague and rather translated into specific targets, using quantitative or qualitative indicators, it is simpler for the organizations and also for the investor to monitor results. This would allow to increase evidence of prospect impact and, on the other hand, to decrease social risk.
3.Reasoned Theory of Change	**3.1**The organizational mission responds to a market problem	The social risk of a project could also derive from a lack of additionality, which means that the output provided is not solving any market problem. For this reason, it should be checked that the organizational mission of the investee responds to an urgent need and provides a coherent solution that could improve the current situation of the beneficiaries.
	3.2 Direct link between project's outputs and outcomes	A well-structured theory of change which explains how the project's outputs can lead to the stated outcomes increases evidence of future impact and decreases the level of social risk connected to the project.

4.Key resources	**4.1**Motivated personnel	If the project team is characterized by a strong shared vision that highlights the intentionality to generate positive impact on society, the social risk level is diminished.
	4.2 Experience in the social sector	If the project team is formed by people with some experience in the sector of interest, it means that they are aware of the market mechanisms and needs of the beneficiaries: this can help them to set up a more effective impact plan and reduce the social risk level.
	4.3 Financial sustainability	To reach the impact mission and expand it in the long-term, it is not sufficient to propose a positive solution but it should also be sustainable, otherwise the project fails as the provided financial resources are exhausted. Moreover, more the project is profitable higher is the possibility to scale up the impact, and lower is the social risk related.
5.Stakeholder management	**5.1**Stakeholder engagement	Through the engagement of direct beneficiaries the organization can better understand if they will appreciate the solution offered and, in case of negative response, they can easily adapt their products/services to the stakeholder needs. Indeed, stakeholder engagement reduce the level of social risk connected to the project.
	5.2 Include marginal stakeholders	The higher the number of stakeholder groups the organization takes into account in its theory of change – even when they seem marginal to the project influence – the lower the probability that its activities would cause displacement on secondary actors, thus undermining the positive impact created. For this reason, a thorough stakeholder analysis can reduce the level of social risk.
6.Social impact measurement	**6.1**Adoption of a structured approach for impact measurement	Through a standard impact measurement system, the organization can easily track the results and understand when the project is deviating from expected outcomes, taking then corrective measures. For these reasons, the adoption of a structured approach for measuring social impact allows to

		increase evidence of future impact and reduces the social risk of the project.
7.Project readiness	**7.1**Pilot phase	The presence of a pilot phase allows to test the effectiveness of the impact plan on a restricted sample of beneficiaries. For this reason, it increases the evidence of impact and decreases the project's social risk.
	7.2 Short-term duration	A long-term duration of the project reduces evidence of expected impact due to the fact that in long time periods the context can change and so the problems, needs and expectations of the society. On the contrary, a short-term duration increases evidence of impact generation and decreases social risk.

Table n: Social Risk Evaluation Framework

Now for each of the variables included in the model some suggestions are given to the investor in order to understand whether the requirements are satisfied by the investee organization under analysis.

1.1 Balance between social and financial mission

To verify that the social objectives are not in contrast with the financial objectives, the investor should investigate whether the business success factors are aligned with the impact success factors, looking in parallel at the business and impact plans. This check would require less time if the organization provides a clear explanation in the impact plan of how the profits would support the impact mission.

1.2 Legal and Governance structures

To understand if the legal and governance structures support the organization social mission, an investor should pay attention to the organization rules and procedures, for instance, in the use of profits. Sometimes there are explicit governance policies that regulate the use of profits, allocating a certain percentage of them to support the social mission. This may include reinvestment in impact-generating activities or donations. Alternatively, there can be some rules that limit the portion of profits that can be distributed to shareholders.

Moreover, the investor should check if there are some forms of assets lock, meaning that, in case some assets are sold, the money earned will remain within the organization.

2.1 Quantitative/ Qualitative target results

To investigate how much the social outcomes are clear, the investor should check if the organization has established specific indicators, quantitative or qualitative, and the respective target values that they aim to achieve. Probably the investor can find them in the impact plan and for sure these targets are included in the social measurement system, in case the company adopts one.

3.1 The organizational mission responds to a market problem

To check if the project output responds to an existent market problem, the investor should look for alternative products/ services in the market which answer to the same needs; this would help to understand if the project is coherent to the context of operations.

In case the organization operates in an innovative market, where no competitors are present, it would be more difficult to understand whether the business idea is in line with the market expectations; the only way is to prove it through a pilot phase, where the product/service is tested on small samples of beneficiaries.

3.2 Direct link between project's outputs and outcomes

To understand whether there is a direct relation between the outputs and social outcomes of a project, the investor should verify if there is any track record of past performances, which means similar initiatives carried out in the past years which have proved the validity and effectiveness of the approach.

In absence of these, precedent experience of other organizations working with similar methods and assumptions can be exploited, that show how a certain approach has been successful to deliver a specific outcome. But the most conclusive evidence of the effectiveness of an intervention can be reached through the use of control groups, which reveal the difference between the outcomes achieved when the organisation is active and when it is not.

However, these are rarely used because too expensive and, above all, meaningful only when sample sizes are large and the intervention leads to easily isolated, testable and relatively short-term outcomes.

For an organisation proposing a completely new idea, it is more difficult to show evidence that the approach can work. In this case the investor can check if the organization impact plan, instead of proving the approach used, rather shows how different approaches have failed in the past, and how the new one learned from them.

Although an organisation working with well-established methods can better prove that planned outputs will lead to the stated outcomes, excessive investor demand for high levels of evidence would lead to prioritize more mature organizations working with tried and tested methods, at the expense of innovative, and in some cases more effective, forms of intervention.

Therefore, it is important that the investor balances these conflicting desires: on one hand, give priority to a more evidenced approach and on the other to innovation.

These considerations will play an important role into the investment decision when weighing impact risk against other criteria.

4.1 Motivated personnel

To look if the project team is unified and motivated towards the social mission, the investor should check if, for instance, these people have worked together before and if they are driven by a strong impact vision and leadership.

4.2 Experience in the social sector

To look if the team members have some experience in the social market, the investor should check again if there is any track record of past performances. Alternatively, he could also check if the organization is engaged in other not-for-profit activities or donations to charities.

4.3 Financial sustainability

To check if the plan is financially sustainable, the investor should look simply at the organization business plan, which usually provides the necessary information about the company's profitability and financial reliability. Economic sustainability is the central issue in the financial due-diligence, however, it also impacts on social results and needs to be included in the framework.

5.1 Stakeholder engagement

To verify that the product/service offered respond effectively to the customer needs, the investor should check if the company has organized any kind of interaction with the direct beneficiaries, such as questionnaires, direct interviews or other methods that have led them to understand the preferences of the clients.

5.2 Include marginal stakeholders in the theory of change

To check the probability of displacement, the investor should check how the stakeholder analysis was carried out. Normally, an analysis of materiality is a good practice since it useful to understand the bounds of what is relevant to include in the theory of change, in particular which are the actors that, even if they seem marginal to the project boundaries, can determine or compromise the expected impact.

6.1 Adoption of a structured approach for impact measurement

The investor should check if the organization adopts a structured system with clear indicators that track social outcomes during the whole duration of the project and potentially even once the project has been concluded. If the organization has already put in place a structured method for social performance monitoring, this would also help the investor not to spend a lot of time in the social evaluation of the projects financed.

7.1 Pilot phase

The projects financed with impact products are very often in the early stages of the lifecycle, probably when the business idea has been neither implemented and they are still searching for the resources necessary to launch the business.

In order to check whether the impact plan is reasonable the investor should check if the organization has at least tried to test the solution on a small sample of beneficiaries through a pilot phase.

7.2 Short-term duration

This social risk level connected to this variable is more difficult to determine. In fact, the variability of the context is related to the particular industry in which the organization operates: some market needs are more constant while others can change rapidly.

In addition, the project duration depends on the type of results that the company wants to achieve. Usually those projects that lead to long-term impacts need also long time to reach their goals. Therefore, the investor needs to balance the time period with the amount of impact that the project can generate.

Once the social risk profile of the investment is determined, the investor can decide whether to proceed with the investment, balancing this value with the other critical variables: financial risk, return and potential impact.

When the decision is taken, the investor can also utilize the framework to highlight the main problems that can affect the social performance of the investment. This will help him to set up coherent mitigation measures to reduce the social risk connected to the funded project.

For investors allocating capital in markets outside those in which they operate, for instance, it may make sense to utilize fund intermediaries to manage the investments on-the-ground. Fund intermediaries can also relieve some of the burden of managing the investments post-commitment, which can often require a high level of engagement due to the early nature of many impact businesses.

Furthermore, the set-up of a direct relationship with the customers can help to avoid misalignments between investors' expectations and investees' actual results.

Another expedient which is currently adopted by investors is to provide additional support to clients such as trainings, advisory, incubation programs or help them to join important business networks. These can facilitate the investees, for instance, with managerial activities that are necessary to run a business.

The investor can also introduce some forms of "mission lock" to the investment, for instance, linking financial compensations to impact targets through discounts in the interest rates and payment-by-result schemes. Alternatively, they can adopt protection measures in the investment contract. These can involve covenants related to reporting requirements, a position in the organizational board so that the investor could be able to influence managerial decisions, certain rules that guarantee the possibility to exit the deals when the investee drifts away from the social mission. All these expedients would incentivize the customer to stick to the social purpose without looking only at financial returns. The mitigation activities identified are summarized in Table o.

Mitigation activities	**Comments**
Participatory due-diligence	This would allow to better understand strengths and weaknesses of the investee and organize supporting activities accordingly.
Direct relationship with the customer	This would help to avoid misalignment between investors' expectation and investees' intentions. It will also facilitate the investor to monitor the ongoing project results and support the investee if it is necessary.
Intermediaries	Make use of intermediaries that manage the investment on-the-ground is useful when the investors are allocating capital in markets outside those in which they usually operate and they do not have the needed competences or instruments to support the clients.
Managerial support, advisory, incubation programs	These activities would help the investee organizations, especially those in the first stages of the lifecycle (e.g. startups), to carry out managerial activities and other processes, such as impact measurement, that are critical for the business success.
Provide access to business networks	Many times partnerships with important people in the sector are essential but sometimes the social entrepreneurs do not have access to these networks. This is why the investor should help them to provide access to business networks. Relevant partners could be organizations working in the same industry, from which the newcomer can leverage on or organizations providing consultancy regarding new processes such as social impact measurement.
Link social objectives to financial compensations	This would incentivize the investee to do their best for delivering the agreed social outcomes and do not only focus on financial results.
Set up protective rules in the contract (e.g. rules that allow the investor to exit the deal if the investee drifts away from the agreed social mission)	This would incentivize the investee to stick to the social mission not to lose the investor financial support.

Table 0: Social Risk Mitigation measures

The social risk framework designed constitutes a practical guide for impact investors to assess the social risk connected to any type of investment. All the variables that reasonably affect social risk are included in the framework and explained.
Its **simplicity** is the key driver for allowing also the new comers in the industry to carry out the impact risk analysis, which so far has been ignored.
In this regard, some suggestions are provided to the investor in order to verify whether the conditions determining a lower social risk are satisfied.
Moreover, it is also useful to identify the organization main weaknesses; this helps the investor to prepare some expedients to avoid a reduced or even negative social impact. In particular a list with the most significant mitigation measures is provided.
As a matter of fact, the investor can exploit the framework both during the investment due-diligence for estimating the social risk level and once the investment decision is taken to reveal the main problems that need to be tackled with proper mitigation activities.
Nevertheless, this framework presents some limitations that need to be overcome through additional research and empirical evidence. The possible evolution of the model is going to be discussed later.

CONCLUSIONS

This conclusive chapter aims to summarize all the insights gathered from the literature review and from the interviews that have been conducted with the main exponents of the Italian impact investing ecosystem. The results have driven the formulation of the social risk definition and, later, the design of the social risk framework which determines a more structured approach for impact risk evaluation.

Starting from the findings related to **social risk definition**, it was discovered that some differences exist in how this concept is used within the financial field.
While within traditional finance this term is rarely present and taken into account in the investment strategies, it started to receive greater attention with the emergence of social finance; in particular, impact risk is used within two specific investment contexts: socially responsible investments and impact investments.
However, its meaning and weight change when applied to the two diverse financial fields.
For responsible investors social risk represents the possibility that the investee would generate negative impacts on society and the main variables that determine the risk extent are the sector of operations and the type of environmental, or social issue entailed.
In this respect, some procedures have been established by big international institutions, such as the GIIN, that help investors to carry out the investment due-diligence, in particular, supporting them with the environmental and social risk analysis.
On the other hand, for impact investors social risk relates to the failure of the impact mission of the project financed. In this case, the investment purpose is double, meaning that social returns assume the same relevance of financial returns.
There are some pioneers in the field who think that social risk together with social impact should play a central role in the impact investment process and should be balanced with the other variables that are critical for investment decision-making, financial risk and return. Others, instead, are more conservative and believe that it is important to monitor social risk because it allows to foreshadow negative events and prepare corrective actions to avoid that the project fails in delivering social impact, but for them the investment decision is still based on financial parameters.

Regardless the adherence to the innovative or conservative school of thought, several authors in the impact investing field have tried to attach a definition to social risk. Through an accurate analysis of these definitions, it was developed a unique and comprehensive statement as follows:
"Social risk is defined as the likelihood that the social outcome of a financed project is lower than expected, null or even negative, therefore worsening the actual social conditions".

Regarding the **"operationalization" of social risk** in the impact investment process, instead, it was found a lack of information in the literature, especially among the main representatives of the impact investing network, such as the GIIN and EVPA, that do not provide any suggestion for social risk evaluation.
Only four systems for impact risk assessment were developed so far which, however, remain circumscribed to the experience of the authors who developed them and are ignored by the other practitioners in the field, who do not have the proper instruments to carry out this analysis.
The lack of a standard approach for social risk evaluation has been also confirmed through the **interviews** that were carried out with the exponents of the Italian impact investing ecosystem. There are investors who do not even consider social risk in the investment process, while others are still in the first phases of setting up some procedures in order to monitor it.
On the other hand, the interviews provided interesting information that were exploited in the design of the **social risk framework**, which represents the completion of the study conducted on impact risk both through desktop review and on the field. In particular, the criteria used by Italian investors during customer screening turned out to affect social risk and were included in the framework. The latter is modeled as a checklist of variables, which determine a higher evidence of impact and, at the same time, a lower level of social risk. These variables are mostly related to the organization internal mechanisms that drive operations: intents, competences, past experience, tools and processes.
The social risk analysis in not only important for investment selection, but also for the understanding of the main weaknesses that characterize the investee organization, e.g.

inadequate managerial competences, which need to be addressed through proper **mitigation measures**.

The most relevant are the provision of managerial support, the establishment of effective relations with the investee organizations, the adoption of monetary incentives linked to the social target outcomes, and the set-up of protective rules in the investment contract that avoid the investee to drift away from the impact mission.

The monitoring of social risk could help investors to select the projects that can more likely generate positive impact, but it could also be useful to understand the reasons why a certain project did not work. This allows the investors and the social organizations to become more conscious about which strategies and approaches work better in certain sectors of operations. The social risk analysis represents also an opportunity for recognizing those entities who are not truly committed to the impact purpose, but rather use the social matter as a way to attract customers and reach higher profits ("impact washing").

In summary, these are the most important **contributions** that this research has provided. From a **theoretical** point of view, this study offers a critical overview of the new types of risks associated to impact investments beyond the traditional ones, deep diving on the least investigated, but also very relevant one: social risk. It integrates all the information provided so far by academics and practitioners, who committed to define and better classify social risk within impact finance. In particular, all the social risk definitions found in the literature are presented in this thesis together with the main drivers of impact risk identified by the authors. Despite other scholars have performed an analysis of the social risk issue in the impact investing literature, nobody has yet conducted a proper review of the social risk evaluation issue and the related measurement frameworks that have been developed so far.

Then, in addition to the desktop analysis, this thesis also provides an empirical analysis aimed at reaching more **practical insights** regarding social risk definition and evaluation, by interviewing individuals working in the Italian field. From the interview with impact investor and investees, in particular, it was discovered how the impact investment process is carried out and the current approaches to social risk analysis. At the end, leveraging both on the desktop review and the real case study, a practical approach for the integration of social risk into the investment process is provided.

In particular, a simple framework for social risk evaluation is designed, which can be applied to any sector of operations and any type of social organization, and whose point of strength lies in its simplicity and clear structure.

Limits and Future steps

The practical framework that has been provided in this thesis offers a qualitative method for evaluating social risk associated to any project aimed at generating positive impact. However, further research can be performed to improve the social risk framework.
Firstly, as the market will become more mature, more evidence will be gained through the investments' results, which could lead to the emersion of new **variables** affecting the social outcomes of a project and that would need to be added into the framework. Moreover, the context is continuously changing and new types of social risks, which will need to be taken into account in the model, can transpire. For these reasons the actual version of the social risk framework should not be considered as definitive.

Moreover, a future step that should follow is to assign to each variable in the framework a certain **weight** that represents the extent to which the variables affects the social risk level of the investment. This should be done through an accurate analysis of the financed projects that have already reached some results. In particular, for each project it should be investigated whether its social outcomes deviate from the targets that were established and the causes for this deviation. Through this analysis, it could be determined which social risk factors are more relevant and which, instead, are less impactful.

Nevertheless, the biggest limitation of the model is related to its qualitative nature, that makes it difficult to perform benchmarks among different projects.
To facilitate the comparison among alternative initiatives it could be helpful to measure social risk in quantitative terms. To shift from a qualitative to a **quantitative evaluation**, it is necessary to find an objective function that associates certain events/conditions to a quantitative value of risk. To be more specific, for each variable in the model different alternatives should be identified, each of which corresponds to a specific score that represents the level of social risk associated. Then, a weighted average of all the single risk scores will be computed to find a unique number that identifies the overall social risk value. However, this could be realized only through a deep analysis of a big sample of investment cases that for the moment is not available.

ANNEX

Name	Organization Typology	Legal Residence	Geographical Location	Impact specialized / General-interest	Entry year in the industry	Equity/Debt-based
S-SGR1	SGR	Milano	National	General-interest	2019	Equity-based
S-IC1	Insurance Company	Trieste	National	General-interest	2019	Equity-based
S-SICAF1	SICAF	Milano	National/ International	Impact specialized	2019	Equity-based
S-SGR2	SGR	Milano	Regional	General-interest	2020	Equity-based
S-CB1	Commercial Bank	Padova	National	General-interest	2017	Debt-based
S-CB2	Commercial Bank	Verona	National	General-interest	2010	Debt-based
S-CB3	Commercial Bank	Roma	National	General-interest	2013	Debt-based
S-BF1	Banking Foundation	Torino	Regional	General-interest	2013	Equity-based
S-C1	Corporate	Torino	National	General-interest	2017	Equity-based
S-SGR3	SGR	Milano	National	Impact specialized	2015	Equity-based
S-FO1	Family Office	Torino	Regional	General-interest	/	Equity-based
S-MF1	Membership Foundation	Padova	National/ International	Impact specialized	2009	Equity-based
S-FRN1	Finanziaria regionale o nazionale	Milano	Regional	General-interest	2020	Equity-based
S-FRN2	Finanziaria regionale o nazionale	Torino	Regional	General-interest	2019	Equity-based
S-CF1	Community Foundation	Roma	National	General-interest	2018	Equity-based
S-CF2	Community Foundation	Milano	National	Impact specialized	2017	Debt-based
S-BF2	Banking Foundation	Cuneo	Regional	General-interest	2011	Equity-based
S-GF1	Grant making Foundation	Milano	National	Impact specialized	2017	Equity-based
S-GF2	Grant making Foundation	Torino	Regional	Impact specialized	2007	Equity-based
S-SGR4	SGR	Milano	National	General-interest	2017	Equity-based
S-SGR5	SGR	Estero	National/ International	Impact specialized	2020	Equity-based
S-I1	Incubator	Milano	National	Impact specialized	2015	Equity-based
S-CB4	Commercial Bank	Torino	National	General-interest	2007	Debt-based
S-FRN3	Finanziaria regionale o nazionale	Roma	National	General-interest	2015	Equity-based
S-C2	Corporate	Estero	National	General-interest	2017	Equity-based
S-ECP1	Equity crowdfunding platform	Torino	National	Impact specialized	2018	Equity-based
S-SICAV1	SICAV	Milano	National	Impact specialized	2006	Equity-based
S-SICAV2	SICAV	Milano	National	Impact specialized	2013	Equity-based
S-FO2	Family Office	Milano	National/ International	General-interest	2013	Equity-based

S-SGR6	SGR	Padova	National	Impact specialized	2016	Equity-based
S-SICAV3	SICAV	Estero	National/ International	General-interest	2015	Equity-based
S-SGR7	SGR	Milano	National/ International	General-interest	2015	Equity-based
S-SGR8	SGR	Torino	National	Impact specialized	2017	Equity-based
S-IB1	Investment Bank	Estero	National/ International	General-interest	2012	Equity-based
S-CB5	Commercial Bank	Bergamo	National	General-interest	2011	Debt-based
S-SGR9	SGR	Milano	National/ International	General-interest	2018	Equity-based
S-CB6	Commercial Bank	Roma	National	General-interest	2018	Debt-based
S-IC2	Insurance Company	Bologna	National	General-interest	2018	Equity-based

Table p: List of interviewees-Supply side, adapted from Tiresia (2019)

Name	Organization Typology	Legal Residence	Sector of operations	Investment Year
D-SRL1	S.r.l.	Roma	Culture, creativity and free time	2018
D-SRL2	S.r.l.	Torino	Technology	2017
D-SRL3	S.r.l.	Palermo	Healthcare	2018
D-SV1	Social Venture	Cuneo	Culture, creativity and free time	2018
D-SV2	Social Venture	Milano	Culture, creativity and free time	2018
D-SRL4	S.r.l.	Milano	Culture, creativity and free time	2018
D-SC1	Social Cooperative	Verona	Manufacture	2018
D-SRL5	S.r.l.	Bari	Education	2018
D-SRL6	S.r.l.	Ginevra	Manufacture	2018
D-SB1	Società Benefit Srl	Rimini	Welfare	2017
D-SRL7	S.r.l.	Milano	Education	2019
D-SRL8	S.r.l.	Milano	Healthcare	2018
D-SRL9	S.r.l.	Torino	Technology	2017
D-SRL10	S.r.l.	Siracusa	Education	2018
D-SC2	Social Cooperative	Brescia	Social housing	2018
D-SRL11	S.r.l.	Milano	Healthcare	2019
D-SRL12	S.r.l.	Milano	Culture, creativity and free time	2017
D-SV3	Social Venture	Torino	Social housing	2019
D-SRL13	S.r.l.	Milano	Healthcare	2019
D-SRL14	S.r.l.	Milano	Distribution	2018

Table q: List of interviewees-Demand side, adapted from Tiresia (2019)

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