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Bridging the Social Investment Divide: How Can We Generate More Investments in Social Ventures?

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New social ventures are often shunned for training and network reasons.

Social Ventures Fail to Raise Sufficient Funds:

While social ventures make up only 3% of all startups, they are crucial for the global economy and sustainable business development: social ventures employ more than 200 million people with social missions, are a crucial driver of female business ownership, and the top 500 social ventures alone have improved more than a billion lives over the past 25 years (World Economic Forum, 2024). However, despite their relevance for solving the world's grand challenges, social ventures face a funding gap of more than $1 trillion in 2024 alone. This gap is particularly problematic for early-stage ventures, as only 2% of the already limited social funding goes to new ventures (Hand et al., 2023).

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The social venture funding gap is commonly blamed on financially motivated investors who refuse to accept the typically lower financial returns of social ventures. However, new research on the topic (Wesemann & Antretter, 2023), based on a quantitative analysis of

19,757 early-stage investment decisions and interviews with private investors and entrepreneurs, suggests that greed for financial returns is not the main reason for the lack of social investments. In fact, most early-stage investors will accept lower investment returns from social ventures, but do not invest in them because they struggle to assess their impact and goal hierarchy. One investor told us:

> *"I understand the business side; that's easy. When I built my company, I was the CFO. But I struggle to understand the true social impact of a venture when I invest in it. Like, does it really work? How much good can I buy for a dollar?"*

The difficulty of communicating social missions is also visible on the entrepreneurs' side, where the CFO of a clean water venture from Uganda told us about his struggle:

> *"With the rather intangible focus [...], it is quite challenging to convey our message effectively."*

This company only managed to get fundraising off the ground once they adopted an integrated Enterprise Resource Planning (ERP) approach that also quantified the social bottom line.

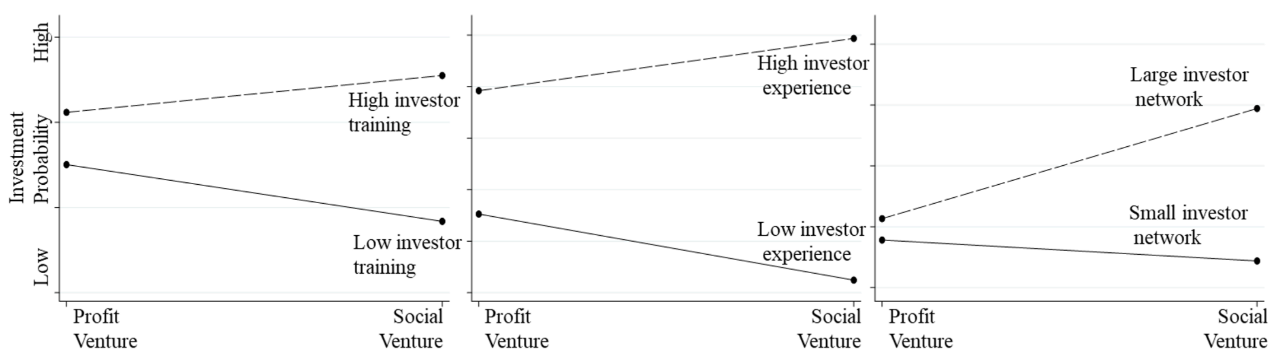
Factors that Limit Social Investments:

Overall, our research identified three factors that are associated with low social investment rates.

1. **Lack of investor training.** Most investors have made their money in for-profit businesses and lack experience in the social sector. While the processes seem similar at first, management and investment processes often cannot be transferred. As a result, angels lack relevant investment training and a solid understanding of double-

bottom lines. On average, a one standard deviation increase in investor training was associated with a 12.0% increase in their social venture investment probability.

2. **Lack of prior social investment experience.** Before their first social investment, most investors are somewhat apprehensive about the sector but warm up quickly once they made their first deal. However, the sector is still so small that it can be difficult to find initial experiences with which to gain experience. Getting angels' feet wet is important, though: an increase of one standard deviation in social investment experience increases the investment likelihood on additional social opportunities by 13.1%.
3. **Lack of professional networks.** While early-stage investments are becoming increasingly social activities (e.g., Wesemann & Antretter, 2022), investor collaboration is still rare. However, teaming up increases the likelihood of social investments: according to our research, broadening the breadth of investors' networks by one standard deviation increases the average social venture investment probability by 15.1%.



Social ventures do not have to offer higher returns to investors; they must communicate their purpose better and integrate investors in the impact space.

Three Strategies Help Social Ventures Attract More Social Angel Investments:

Ventures can take several steps to improve their chances of investment:

1. **Get your finances right.** Understand how important financial metrics are to investors. Most have a better understanding of finances than social targets, so expect deeper questions on the finance front. Even entrepreneurs with untested business models must be prepared to engage in hard conversations about cash flows and unit economics.
2. **Simplify social metrics.** Devote extra time to explaining your social goals; early-stage investors are often puzzled by the mechanisms behind social goals. Use frameworks like the Theory of Change to outline causal effects that connect your actions to broader societal goals. Also clarify the hierarchy between potentially competing goals explicit. What will be prioritized in tradeoff situations?
3. **Word-of-mouth referrals.** Use existing investor networks to recruit additional ones. Since many investors who want to get involved want to feel a sense of belonging and often even status, making word-of-mouth referrals far superior to cold calls in social investment contexts.

Two steps can help investors get started with social investments:

For investors, it is perfectly normal to be hesitant to start with social investments. The underlying logics are different, the goals are hard to quantify, and prioritization between social and financial goals is unclear. While social ventures really tend to have more complex and ambiguous goals, uncertainty can still be reduced through mentoring and the use of proven frameworks.

1. **Get mentoring.** When presented with potentially interesting social venture investment opportunities, use more experienced impact investors as a sounding board and mentors. Ideally, you even make your first social investment in collaboration with other investors. Guidance from more experienced social investors can help you avoid most of the usual pitfalls. The first social investment is the hardest. Initial guidance ensures clarity at the start; experience ensures clarity in later investment evaluations.
2. **Learn about frameworks.** Familiarize yourself with the most common frameworks (that best align with your approach to impact) of social ventures like the Theory of Change or the Balanced Scorecard Model. There are rich online resources on websites and YouTube that can help you get started.

Collectively, our research shows that low social investment rates by angel investors are not due because they demand impossible profits but because of communication issues. Fixing this can help us close the social venturing gap and get investor money where it is most needed.

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