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Short Article: More VCs Invest in Companies With Social Impact

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Fast growth attracts the socially conscious (and profit-minded)

Executive Summary

More than 300 venture capital funds are investing in double bottom-line businesses—companies with both bottom-line profit and social impact. This growing interest is being partly driven by a rethinking of the role of business in the developing world.

Full Article

Venture capital (VC) is about as pure a form of capitalism as you can get. VCs either perform or they don't get to raise a new fund. Performance means profit.

But there's rising interest in businesses that are also socially conscious. The Global Impact Investing Network (GIIN) estimates that more than 300 VC funds are pursuing investments in what are known as double bottom-line businesses—companies with both bottom-line profit and social impact. A GIIN survey of 125 such funds found that, depending on their year of founding, between 25 and 50 percent of them follow a venture capital or private equity model. These funds fall into three broad categories: environmental, social focus and triple bottom line (profit, social impact and environmental impact). [1]

The rise of socially oriented capital is being partly driven by a rethinking of the role of business in the developing world, which has a history of exploitation both of resources and of the poorest members of society. It's also being driven by the failure of massive amounts of aid to create notable change. [2] The success of microfinance, which provides small loans to the poor, sparked interest in alternative models of investment, as did the desire of wealthy venture capitalists to apply high-tech-style innovation to their philanthropy. [3] "Impact investing is poised to change the trajectory of poverty, crime, homelessness, for education, green energy and much more," wrote Sir Ronald Cohen, chairman of British social investment firm Big Society Capital, and Matt Bannick, managing partner of the Omidyar Network, a large impact investor started by the founder of eBay, in a call to governments to create better regulatory conditions for such investing. [4]


Nancy Pfund

The best-known socially conscious venture firm is DBL Investors (double bottom line), a partnership headed by Nancy Pfund, who has also run JPMorgan Chase's social capital fund. [5] Among DBL's investments are SolarCity (power systems), Tesla Motors (batteries and electric cars), Pandora Media (Internet radio), Revolution Foods (healthy food) and EcoLogic (food packaging).

Other funds that have formed and drawn institutional money are Equilibrium Capital, Village Capital and Leapfrog Investments, which specializes in companies that provide financial services such as insurance in emerging markets. [6]

Although social venture capital funds have emerged, traditional VCs are getting involved, too. Warby Parker, a for-profit eyeglass maker that donates glasses to entrepreneurs to resell in emerging markets, has drawn more than $100 million in venture capital from Tiger Global Management, General Catalyst, Spark Capital and others. [7] VCs are making smaller investments as well: Cotopaxi, an outdoor gear firm organized as a public benefit corporation (for-profit companies with social missions that are also known as B corporations), drew $3 million from New Enterprise Associates and several other investors. It has raised $9.5 million overall, a record for benefit corporations, signaling that Silicon Valley sees profit potential in such companies. [8] VCs are drawn by the fast growth of these businesses, which can be popular with socially conscious consumers. [9]

Still, "the general perception is that it has not grown as fast as people thought three or four years ago," says David Bank, a former Wall Street Journal writer who founded ImpactAlpha to cover the market for impact investing.

Bank says the institutional money that has fueled social venture capital is looking at markets such as sustainable agriculture, sustainable timber and green real estate. These hold enough long-term promise for institutional investors to see potential returns.

Social venture capital isn't yet a proven vehicle for creating large returns, but neither were the early venture capital funds. "This is a young and growing market. Things aren't always growing at the exact same rate and in perfect alignment," said Amit Bouri, CEO of GIIN. [10]

Cohen and Bannick argue that venture capital had almost evaporated in the late 1970s before the U.S. government made some regulatory changes that opened the industry again. [11]

Social venture capital isn't in danger of disappearing. It may have already had its Intel moment, when a pioneering company in an untested market has a defining milestone, such as going public. For social capital, that company may be SolarCity: It took solar power and devised a low-cost way for consumers to adopt it, installing panels upfront and then securitizing the cash flow from generating power. SolarCity went public in 2012, raising $92 million, with market capitalization of about $600 million. [12] In mid-May 2015, it was worth $6 billion. [13]

About the Author

Michael Fitzgerald is an award-winning freelance writer from Boston whose work has appeared in The Boston Globe, The Economist, MIT Sloan Management and other publications. He has written on a variety of business topics, including innovation and the digital transformation. He also has made numerous appearances on CNN, Bloomberg TV and CNBC.

Notes

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[4] Ronald Cohen and Matt Bannick, "Is Social Impact Investing The Next Venture Capital?" Capital Flows blog, Forbes.com, Sept. 20, 2014, http://tinyurl.com/pycplvr.

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[8] Lizette Chapman, "Cotopaxi Raises $3M for Do-Good Outdoor Company," Venture Capital Dispatch, The Wall Street Journal, July 22, 2014, http://tinyurl.com/pvrpa3l; Tom Foremski, "Cotopaxi raises record $9.5M, breaks through 'B Corp' stigma," ZDNet, April 21, 2015, http://tinyurl.com/og23ejw.

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[11] Cohen and Bannick, op. cit.

[12] Maureen Farrell, "SolarCity IPO shines," CNNMoney, Dec. 13, 2012, http://tinyurl.com/qz3t5tx.

[13] "SolarCity Market Cap," YCharts, accessed May 13, 2015, http://tinyurl.com/nqu56wk.