

Impact Investing*

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December 2019

JEL classification: G11, G21, G22, G23, G24, G28, H41, M14

Keywords: Impact investing; venture capital; private equity; socially responsible investment; United Nations Principles of Responsible Investment (UNPRI); sustainable investing; public pension funds; willingness to pay; random utility discrete choice models

*We are grateful for Philip Bond, Magnus Dalquist, Lisa Goldberg, Will Gornall, Tim Jenkinson, Oğuzhan Karakaş, Hideo Owan, Ludovic Phalippou, Elena Pikulina, Josh Rauh, Berk Sensoy, Laura Starks, Annette Vissing-Jorgensen and the comments of seminar and conference participants at AFA Annual Meetings (Chicago), Caltech/USC 2016 PE Conference, European Commission Promoting Sustainable Investment Conference, the Fifth International Conference on Financial Frictions in Copenhagen, LBS 9th Private Equity Symposium, 2017 LSE-Chicago Booth Economics of Social Sector Organizations Conference, Masahiko Aoki memorial academic conference, 2016 PERC Conference (Chapel Hill), Sustainable Finance Conference at Swedish House of Finance/ Stockholm School of Economics, 2016 WFA Annual Meetings (Park City), UW 2016 Summer Finance Conference, Cambridge University, Lancaster University, Maastricht University, New York Fed, Oxford University Saïd Business School, Tuck (Dartmouth), UC Berkeley (Law), University of Massachusetts, University of Warwick, University of Porto, University of Tilburg, and Yale School of Management. Radin Ahmadian, Christina Chew, and Derek Lou provided valuable research assistance. All errors are our own.

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Abstract

We document that investors derive nonpecuniary utility from investing in dual-objective VC funds, thus sacrificing returns. Impact funds earn 4.7 percentage points (ppts) lower IRRs ex post than traditional VC funds. In random utility/willingness-to-pay (WTP) models investors accept 2.5-3.7 ppts lower IRRs ex ante for impact funds. The positive WTP result is robust to fund access rationing and investor heterogeneity in fund expected returns. Development organizations, foundations, financial institutions, public pensions, Europeans, and UNPRI signatories have high WTP. Investors with mission objectives and/or facing political pressure exhibit high WTP; those subject to legal restrictions (e.g., ERISA) exhibit low WTP.

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I. Introduction

Do investors knowingly accept lower expected financial returns in exchange for nonpecuniary benefits from investing in assets with both social and financial objectives? Classic asset pricing models generally define an investor's objective function using utility over wealth or consumption. While there have been innovations in the form of these utility functions (Epstein and Zin 1989; Laibson 1997), wealth generation is the common goal of investors. Economists are now taking seriously the possibility that investors might value positive societal externalities in utility in addition to wealth. Theoretical models consider the implications of these nonpecuniary preferences in a variety of settings (e.g., Andreoni, 1989; 1990; Fama and French 2007; Hart and Zingales 2017; Niehaus 2014), yet, these models start from a relatively untested assumption that nonpecuniary motives affect the allocation of capital in a way that reflects an intentional willingness to pay for impact.

A natural starting point is to look for indications of demand for nonpecuniary benefits by the sources of capital themselves. As of April 2019, 2,372 organizations representing \$86 trillion in asset under management have become signatories to the United Nations Principles of Responsible Investment (UNPRI). Virtually all major consulting groups have implemented a social impact practice, and all major investment banks have an impact division to meet corporate, institutional, and private wealth demands for impact considerations in investment. These indications of demand for investing with a social conscience do not imply that investors readily accept a tradeoff between financial returns and nonpecuniary benefits. For instance, the signing of the UNPRI accords does not imply that a holder of capital necessarily must tilt investment toward impact. Rather, UNPRI investors can comply by adhering to principles of governance within their investing entity.

An important, recent empirical literature on SRI (socially responsible investment) mutual funds shows that the demand for responsibility is growing rapidly (Bialkowski and Starks, 2016), reflecting both preferences and social signaling (Riedl and Smeets, 2017). However, performance in public market SRI has not been statistically different from other mutual funds in this period (see the amalgamation of evidence in Bialkowski and Starks, 2016). Hence, the tilt toward SRI need not reflect a willingness to pay in wealth for nonpecuniary benefits.

Thus, we study a different asset market – impact investing – to ask whether the theoretical assumption that investors are willing to pay for impact holds. Two primary instrument types that

receive the largest capital allocation among impact investors are private debt and private equity.¹ While private debt is the largest category, we are not aware of any data sources for private debt impact investments. Instead, we focus on impact funds, which are predominantly VC and growth equity funds that are structured as traditional private equity funds but with the intentionality that is the hallmark of impact investing. The Global Impact Investing Network (GIIN) defines impact investing as “investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return.”² Thus, an impact investor exhibits an intention to generate both positive social or environmental returns and positive financial returns. Green washing investments, which is branding for an appearance of impact intentionality (Starks, Venkat and Zhu, 2017) and purely for-profit investment in sectors that associate with positive externalities (e.g., health, education, clean energy) do not meet the *intentionality* criteria. In our data collection, we ensure that we only choose impact VC funds that explicitly market a dual agenda.

Besides the data availability, the VC institutional setting brings an additional advantage. Because VC funds only fundraise at the inception of the fund and investors contractually commit their capital for the duration of the fund (typically 10 years), the timing of capital flowing in and out of funds is not a concern in our setting. This institutional feature allows us to focus on the investors’ discrete choice to invest in traditional VC funds versus impact VC funds among the observable choice set at a given point in time.

These advantages in the impact-versus-traditional VC market provide us with an ideal setting to identify any *ex ante* willingness-to-pay for impact that investors may exhibit. We ask: (a) whether investors are intentionally willing to forego expected financial returns in exchange for expectation of impact, (b) whether this willingness to pay depends on the source of the capital (e.g., pension fund, bank, or development organization), and (c) whether the evidence points to any attributes (e.g., mission objectives, household versus institutional ownership, the legal or regulatory framework governing the allocation of capital) that explain heterogeneity in investor willing to pay for impact?

Using Preqin data, we construct a sample of 24,000 VC and growth equity (to which we refer together as VC for simplicity) investments by about 3,500 investors over the period 1995-2014. These investments reflect 4,659 funds – the combination of traditional VC and impact VC

¹ GIIN Annual Impact Investor Survey 2016.

² <https://thegiin.org/impact-investing/need-to-know/#what-is-impact-investing>

funds. We manually isolate 159 of these funds as being impact funds using a strict criterion that the fund must state dual objectives in its motivation. Investors are not all alike in their portfolio choice decisions; thus, we also manually look up the ultimate source of capital for each of the 3,500 investors and code them into ten investor types. Our final piece of data coding is to codify the impact agenda themselves in more detail. The impact agenda of impact VCs are quite broad, including funds that seek to reduce greenhouse gas emissions, encourage the development of women and minority-owned firms, alleviate poverty in developing countries, or develop local business communities.

Our primary analysis estimates the willingness to pay (WTP) for impact across investor types and attributes. To set the stage for this analysis, we estimate reduced form regressions of impact fund performance compared to that of traditional VC funds. We document that the annualized internal rate of return (IRR) on impact funds is 4.7 percentage points (ppts) lower than traditional VC funds, after controlling for industry, vintage year, fund sequence, and geography.

Reduced form estimations suggest investors may be willing to forego returns, but this evidence is not sufficient. Selection in observability of VC fund returns may affect this analysis, and, more fundamentally, ex post performance estimations do not necessarily reveal ex ante decisions to invest as a function of expected returns.

To investigate whether investors willingly forego expected return at the time of their investment decision, our primary empirics employ a discrete choice methodology using investors' observed choices of investments (yes/no decisions in a random utility framework) among a large set of VC funds fundraising in a year as the dependent variable. This approach builds on a large literature on hedonic pricing techniques, which provide tools for estimating implicit prices of attributes that a good possesses (e.g., Court, 1939; Griliches, 1961; Rosen, 1974; McFadden, 1974, 1986). Cameron and James (1987) introduce the idea that willingness to pay can be estimated in discrete choices over alternatives. In discrete choice models, the choices made by agents over alternatives can be used to infer the sensitivity of the choice probability to price and other attributes (McFadden, 1974). Cameron and James (1987) note that if one re-parameterizes the sensitivity of choice to an attribute by scaling it relative to the sensitivity of choice to price, the result is an estimate of the individual's willingness to pay for that attribute.

A relevant example of the method is Huber and Train (2001), who study households who choose among a set of electricity providers. They are interested in the tradeoffs in price households

make when choosing characteristics of the provider (e.g., local utility vs. conglomerate), making inference as to people's willingness to pay to do business with a more expensive local provider. Analogously, we study the choice of alternatives of funds and ask whether investors exhibit a willingness to pay for the impact characteristic of a fund.

Our empirical analysis relies on two key independent variables: an impact fund dummy variable (the hedonic variable) and an ex-ante estimate of expected return for each fund (the price variable in a hedonic model), which we model using historic data on a fund's characteristics that investors would observe at the time of fundraising. From investors' choices, we find that both the ex-ante expected returns and the impact fund designation positively relate to the probability of investing in a fund. We estimate a logit model over the choice of funds fundraising in a given vintage, including investor fixed effects (i.e., a conditional logit model) or similar-investor dynamic groupings (to capture time-varying investor demand for the asset class). Our specifications include a rich array of fund and investor characteristics to model dimensions of portfolio choice preference. Measuring how sensitive the investment rate is to a fund's expected return allows us then to convert the desirability of impact into a willingness to pay for impact via standard hedonic methodologies.

We address two main methodological concerns with respect to the estimation and inference in our VC setting. First, unlike traditional hedonic models, our price variable is an estimate – the forecast expected returns – and thus has measurement error. This likely induces over dispersion in expected return forecasts and attenuation bias in the expected return coefficient in the logit model. Since WTP has the expected return coefficient in the denominator, attenuation does not affect the sign of the estimated WTP but increases its magnitude. To address the magnitude issue, we apply a shrinkage estimator, which provides an asymptotic correction for the attenuation bias in the expected return coefficient.

Second, investors may have differential exposure or access to opportunity sets of funds to invest in, thus inducing them to have different expected return forecasts for the same fund. Misspecifying this heterogeneity may induce a bias in the expected return coefficient, thus affecting the magnitude of our WTP estimates. Heterogeneities in expected returns is plausible in our private investment setting, but the exact mechanism is difficult to pin down with precision given the limitation in our private equity data. As empiricists we are agnostic as to whether parsimony vs. specificity in the expected return model brings us closer to the true expected return used by each

investor. Thus, we use both a parsimonious homogenous expected return model and a heterogenous expected return model to estimate expected returns and report WTP estimates based on both models to generate a range of plausible WTP estimates. Furthermore, we estimate the model under both rationed and expanded opportunity set assumptions and find that our impact coefficient and WTP estimates consistently positive and stable. Overall, we report that the aggregate willingness to pay for impact is between 2.5 percent to 3.7 percent in expected IRR.

Willingness-to-pay (WTP) for impact is not in equal magnitude across investor types. Five noteworthy investor groups exhibit a positive WTP for impact. (i) Development organizations have a high WTP for impact, presumably reflecting their direct impact mission. (ii) Foundations also have a small but positive WTP for impact in some specifications, again reflecting their mission orientation. (iii) Financial institutions – banks and insurance companies – have high WTPs, likely reflecting their incentives to invest in local communities either to comply with the Community Reinvestment Act (CRA) and/or to garner goodwill from the community or politicians/regulators. (iv) Public pension funds have a high WTP for impact, in line with the tendency for state pensions in the U.S. to prefer investments within their home state (Hochberg and Rauh, 2013) to bring spillover economic benefits, nonpecuniary political benefits, and direct social objective benefits. (v) Investors in Europe, Latin America, and Africa have a higher WTP.

We then explore six investor attributes that might capture differential utility from investing in impact across investors; namely, whether the capital is (1) held by households (as opposed to an organization), (2) intermediated by an asset manager, (3) held by an organization with a mission objective, (4) held by an organization facing regulatory or political pressure to invest in impact, (5) held by an organization subject to laws restricting investments in impact, or (6) held by an organization (e.g., corporation) with charters that restrict investments in impact.

We find that mission-focus (i.e., development organizations and foundations) is associated with a positive WTP of 3.4 to 6.2 ppts in expected excess IRR. This result is robust to including the LP geography fixed effects interacted with impact (i.e., within each geography, investor mission orientation is positively related to WTP for impact). Likewise, organizations expressing their mission by signing the UNPRI have a similarly higher WTP, especially after their signing. These UNPRI results are robust to including either LP geography fixed effects interacted with impact or LP Type fixed effects interacted with impact.

Next, we find that political or regulatory pressure is associated with a positive WTP. In our most conservative models, WTP for impact associated with pressure is 2.3-3.3 ppts in expected excess IRR. Legal restrictions against investments for non-financial motives (e.g., ERISA and UPMIFA) are associated with a lower WTP for impact. In contrast, we find no evidence that organizational charters that require a focus on financial returns (e.g., corporate charters that require shareholder wealth maximization) lower the WTP for impact. In addition to the LP geography-impact interaction, these estimates for attributes (4)-(6) are further robust to including the LP Type fixed effects interacted with impact, thus exploiting international (e.g., U.S. vs. non-U.S.) differences in laws for a given LP type governing attributes (4)-(6).

Finally, we provide evidence on whether investors' WTP varies across the different types of impact, though we characterize this evidence as preliminary given the small sample sizes in each type. Impact funds focused on environmental impact, poverty alleviation, and women or minorities generate the highest WTP estimates. In contrast, impact funds focused on small and medium-sized enterprises (SMEs) and social infrastructure (e.g. health, education, and mainstream infrastructure) funds do not generate investment rates that reliably differ from those of traditional VC funds. These preliminary findings, which we hope provides fodder for future research, suggest that the internalization of utility from public good investing depends on how much the good is viewed as a public good versus an endeavor that could be profitable.

There is little prior academic work on impact investing by private investment vehicles. Kovner and Lerner (2015) study 28 community development venture capital funds in the U.S., finding that these funds tend to invest in companies at an earlier stage, in industries outside the VC mainstream, and with fewer successful exits. Geczy, Jeffers, Musto, and Tucker (2018) analyze contracts of impact funds and document that these contracts provide specific impact goals, indicating that investors intentionally seek impact when investing in these funds.

Our work relates to the broader literature on socially responsible investing (SRI) that dates back as far as Milton Friedman's 1970 doctrine on responsible investing.³ A survey by Renneboog, Ter Horst, and Zhang (2008) highlights the tension of SRI investing, concluding that investors in SRI funds may (but not with certainty) be willing to knowingly forego some expected financial returns for social or moral considerations. Consistent with the idea that investors in SRI funds

³ "The Social Responsibility of Business is to Increase Its Profits," The New York Times Magazine, September 13, 1970. Also see Geczy et al. (2003).

value attributes other than performance, Benson and Humphrey (2008), Renneboog, Ter Horst, and Zhang (2011) and Bialkowski and Starks (2016) show that SRI fund flows are less sensitive to performance than non-SRI flows while Bollen (2007) documents SRI funds have less volatile flows. Hartzmark and Sussman (2019) document Morningstar sustainability ratings introduced in 2016 resulted in large reallocations of capital toward funds with high sustainability ratings. Similarly, one strand of the SRI literature argues the nonpecuniary interests of investors affect the expected returns of investors; stocks preferred for nonfinancial reasons earn lower returns than spurned stocks. Building on this idea, Hong and Kacperczyk (2009) find that stocks subject to widespread negative investment screens earn strong returns (also see Chava 2014). In other work, Dimson et al. (2015) provide evidence that investor engagement with the management of publicly traded firms on a collection of environmental, social, and governance issues is associated with positive abnormal returns. The above studies highlight the potential importance of nonpecuniary motives when investing, which dovetails with our analysis of the performance of impact funds and investors' willingness to pay for impact.

Our paper also relates to a strand of the private equity literature that focuses on understanding demand. For example, Lerner, Schoar and Wongsunwai (2007) and Sensoy, Wang and Weisbach (2014) compare returns earned by different types of LPs. Our findings complement those of Lerner, Schoar and Wongsunwai (2007), Hochberg, Ljungqvist, and Vissing-Jørgensen (2014), and Hochberg and Rauh (2013) in finding the importance of relationship and geography in understanding investment patterns in private equity.

II. Data and Statistics

II.a. Data and Impact Funds Designation

Our data on funds, investors, and performance come from Preqin's Investor Intelligence and Performance Analyst datasets. We initially search all private equity funds (which include buyout, balanced, and various types of funds of funds) for impact funds. However, the majority of impact funds we identify are venture or growth oriented. Impact buyout funds are a relatively recent phenomenon and was quite rare during much of our sample period. For example, Bain Capital raised its first "Double Impact Fund" only in 2017, and KKR did not set up its impact-investing unit until 2018. Thus, we restrict our study to one of VC and growth equity, which we loosely refer to as VC.

Our first task is to designate funds as being impact or traditional VC, using the criterion that an impact fund must state the dual objectives of generating a positive externality in addition to earning financial returns. To identify such funds, we proceed in the following three steps.

1. We form an impact potentials list, combining (i) text search of articles in Factiva using a list of impact-related keywords⁴ to describe funds, (ii) four third-party lists of impact funds and managers (ImpactBase (www.impactbase.org), Impact50 list in ImpactAssets (www.impactassets.org), ethos funds in Preqin (www.preqin.com), and MRI Manager Database in Cambridge Associates (www.cambridgeassociates.com)), and (iii) list of funds with majority geographic focus on countries with GDP per capita less than \$1400.⁵ Our potentials list consists of 323 VC and growth impact funds, once we impose the further restriction that the fund appears in the Preqin Performance Analyst database.
2. We manually read descriptions and online resources about funds and fund families, and screen out funds that do not explicitly aim to be double bottom-line, or state a dual objective. This results in the elimination of 146 funds from the sample (e.g., some large traditional global fund of funds like one managed by HarbourVest Partners that do not bear any resemblance to impact investing).
3. We further restrict the sample to funds with vintage years between 1995 and 2014 and investor information exists for at least one LP per fund in Preqin's Investor Intelligence database. This results in the elimination of 18 funds.

The screening process above results in our final sample of 159 impact funds. Note that we likely fail to designate some funds as impact (false negatives) due to a lack of detailed information, but our approach yields a clean sample of impact funds (i.e., false positives are unlikely).

Impact funds have diverse goals, so it is useful to consider specific examples of impact funds in our final sample. Bridges Ventures is a London-based family of funds "...dedicated to sustainable and impact investment..." that uses an "...impact-driven approach to create returns for both investors and society at-large." Bridges has several funds in our sample including the CarePlaces Fund, which builds care homes for the elderly. Its limited partners include university endowments, banks, pension funds, and high-net-worth investors. NGEN Partners is a Manhattan-

⁴ See Table A1 for the list of keywords.

⁵ See Table A2 for the list of low GDP per capita countries.

based family of funds that “...invests in companies that positively improve the environment and human wellness” and manages three funds in our impact dataset (NGEN Partners I and II, and NextGen Enabling Technologies Fund). The North Texas Opportunity Fund “...seeks to invest in companies located in or willing to expand operations to underserved North Texas region markets, with a special emphasis on the southern sector of Dallas. The firm invests in minority or women owned or managed companies located anywhere in North Texas.”

To parsimoniously categorize these diverse impact goals, we construct six impact categories: environmental impact, minority and women funding, poverty alleviation, social infrastructure development (e.g., health, education, and mainstream infrastructure), small and medium-sized enterprise (SME) funding, and focused regional development (jobs creation and economic development funds in a specific region). For each impact fund, we read fund descriptions in three databases (Prequin, Capital IQ, and ThomsonOne) as well as in the fund’s own marketing materials on their websites and code the impact objectives of the fund using these six categories, allowing funds to have multiple objectives.

Figure 1 depicts the percentage of the 159 impact funds for each of stated impact goals. The smallest impact categories are minority and women funding (11% of funds) and social infrastructure development, which includes health and education as well as other social or physical infrastructure (16%). The remaining impact categories are more common with the most prevalent being poverty alleviation (43%) and SME funding (42%), followed by focused regional development (33%), and environmental impact (28%).

We augment our Prequin data with the list of UNPRI signatories and signing years, which we obtain from UNPRI. As of November 16, 2015, there were 1,422 signatories (297 asset owners, 931 investment managers, and 194 professional service managers) who collectively manage \$59 trillion. We match UNPRI signatories to our dataset using investor names. Investors that are subsidiaries of a UNPRI signatory are also coded as signatories, but not investors who are parents of UNPRI signatory subsidiaries.

II.b. Fund Statistics

Our analysis focuses on 4,659 funds with vintage years from 1995 to 2014. Table 1 presents descriptive statistics for the 4,500 traditional VC funds on the left and the 159 impact funds on the right.

Although traditional VC funds are larger than impact funds (\$204.6 million v. \$129.6 million at the mean and \$102 million versus \$83 million at the median), the mean commitment size does not differ by impact versus traditional VC. When we average across investors in a fund and then calculating the mean of this average across funds, we find that the mean commitment size for impact funds is \$27.1 million, which is not significantly different from the mean commitment size of \$22.2 million for traditional VC funds. One might wonder if the difference arises because we are more likely to observe commitment size for traditional funds and thus are more likely to observe smaller capital commitments. This does not appear to be the case as we observe proportionately more investment amounts for impact investments (38.0%) than for traditional funds (32.6%). Note that the motivation for our decision to use discrete choice of investments rather than commitments in dollars as the outcome variable is transparent in Table 1; of the 23,986 investments we observe only 7,867 (32.8%) have data on commitment size.

In terms of realized performance, traditional funds have a mean (median) IRR of 11.6% (7.4%), while impact funds have mean (median) IRR of 3.7% (6.4%). The same pattern emerges for value multiples (VMs) and imputed public market equivalents (PMEs). (Note that we do not observe fund cash flows for our sample funds; thus, the imputed PMEs were calculated using regression coefficients from Table IA.IV of Harris et al. (2014), which use the S&P 500 as a benchmark, and observed IRRs and value multiples for our sample funds.) The imputed PMEs for impact funds suggest that they do not beat the public market on average, while traditional VC funds do (albeit with significant time variation).

Our preferred measure of performance, percentile rank, is based on a fund's performance ranking (either IRR or VM, based on data availability) relative to cohort funds of the same vintage and geography (five regions). Percentile ranks adjust for the large temporal and geographic variation that trouble any inference using the other performance measures, which are notoriously difficult to risk adjust (Korteweg and Sorensen, 2010; Sorensen, Wang, and Yang, 2014; Korteweg and Nagel, 2016). In particular, VC funds of vintages from the mid- to late-1990's realized very right-skewed IRRs, when impact funds were relatively rare (only 14 of our sample funds have vintage years between 1995 and 1999).

Table 1 reports that traditional funds have a mean (median) percentile rank of 0.49 (0.50), while impact funds have mean (median) rank of 0.34 (0.28). The difference of 0.15 (0.22) in percentile rank translates to a difference of about 3.0% (4.7%) in excess IRR centered at the median

in historical returns. Appendix Table A3 provides the mapping of percentile ranks to excess IRRs, which are calculated as a fund IRR less the median IRR for the fund's vintage year and geography cohort. Although this mapping includes the strong VC return years of the late-1990s, the post-2000 sample yields estimates that are within 1.2 ppts of the full sample mapping for percentile rank differences 0.40 or less.

Table 1 reports a large difference in the standard deviation of IRRs for traditional funds versus impact funds (32.06% versus 15.17%). This difference is not statistically significant, but the magnitude of the difference triggers concern about risk differences. When we look into the source of these standard deviation differences, we find that the difference in return dispersion is again due to the lack of impact funds during the dot.com boom in the 1990s together with the highly right-skewed performance of traditional VCs during this period. Among traditional funds of late-1990s vintage, 22 earned IRRs greater than 100%. From 2000 onwards, the standard deviation of IRRs for traditional and impact funds are similar (16.8% versus 14.7%). Likewise, even in the full sample, the downside risk (measured as the standard deviation of funds with IRRs less than 50%) is statistically and economically the same across traditional (14.3%) and impact (15.2%) funds. Furthermore, our results are quantitatively similar if we restrict our sample to funds from 2000 onwards.

Another potential data concern is the observability of returns among VC funds. Prequin data are similar to other databases in return statistics (Harris, Jenkinson, and Kaplan, 2014), but the observability of returns may vary depending on a fund's impact status. In unreported tests, we use the fact that public pensions are often required to disclose their holdings and returns (Metrick and Yasuda, 2010) to ensure robustness of our results to a setting unlikely to be affected by selection in observability.

Panel B of Table 1 reports the geography of impact-versus-traditional funds. We collapse Prequin codes of the geographic focus of fund investments to eight regions and designate a fund to have a geographic focus if more than a third of all geographic descriptors are concentrated in a given region. Most funds (84%) focus on only one of the eight global regions and a small percentage have no geographic focus (3.5%). Impact funds tilt more toward developing countries including Africa, Latin America, and Emerging Europe than traditional funds.

Panel C of Table 1 reports the industry foci of impact-versus-traditional funds. We collapse the Prequin codes to 11 different industries (business services, energy, consumer, diversified,

industrials, information technology, health care, infrastructure, food and agriculture, real estate, and media/communications) and code a fund as having an industry focus if more than a third of industry sector descriptors are concentrated in a given industry. Both self-described diversified funds and funds that lack any focus on particular industries (according to our coding method) are categorized as “diversified.” Impact funds are more likely to be energy or diversified funds, and less likely to be IT, health care, or media and communication funds than traditional VC.

II.c. Investor (LP) Statistics

We categorize investors into nine types by doing manual web searches for each investor in our sample. We refer to these groupings as LP types, reflecting the limited partner designation of investors in private equity. Our goal is to attribute the investing to the source of capital (rather than the intermediary). Thus, for asset managers, we search each manager to uncover whether the asset manager specializes in serving a particular constituent (e.g., public pensions).

Development Organizations include multinational, national, and regional organizations that invest with development purposes in mind (e.g., International Finance Corporation, Ireland Strategic Investment Fund, and New Mexico State Investment Council). *Financial Institutions* include banks and insurance companies. (When we separately analyze banks and insurance companies, we obtain similar results for each group.) *Corporation & Government Portfolios* include corporations who invest in VC (e.g., Cisco and Siemens), state-owned corporations (e.g., China Steel and China Oceanwide Holdings), and sovereign wealth funds that are not development-oriented (e.g., Abu Dhabi Investment Authority).⁶ *Wealth Managers* include family offices (e.g., Merrion Family Trust) and advisers who serve retail or high net worth clients (e.g., BNY Mellon Wealth Management). *Private Pensions* are primarily corporate pensions, but also include multiemployer retirement funds (e.g., Carpenters’ Pension Fund of Illinois).⁷ *Foundations, Endowments, and Public Pensions* are self-explanatory. Finally, *Institutional Asset Managers*, a residual category, include LPs who manage money for a diverse institutional client base (e.g., Adams Street Partners), where the capital appears to be primarily institutional capital with a mixture of constituents.

⁶ We sort sovereign wealth funds into development organization and government portfolios following Dyck and Morse (2011).

⁷ There are 81 multiemployer pension funds and the majority are union-backed. Our results by LP type and LP attributes are qualitatively similar if we group these multiemployer pension funds with public pensions.

In Table 2, Panel A, we provide descriptive statistics on LPs. The smallest categories in terms of LP counts are endowments and wealth managers, but even these have close to 200 distinct LPs participating in the market. The total number of investments by LP type generally mirrors the patterns of LP numbers. The average LP makes 6.9 fund investments. The most active investors are public pensions (15.4 funds per investor), private pensions (8.9 funds) and development organizations (8.3 funds). The average LP has 4.3 years of experience as an LP, though this number is positively skewed. Public pensions, private pensions, and endowments are the most experienced LPs. Overall, 9% of LPs are UNPRI signatories. Institutional asset managers are the most likely to sign the UNPRI (17.9%), followed by wealth manager (14.4%) and public pensions (13.4%). Foundations, corporations, and endowments are extremely unlikely to be UNPRI signatories.

The last two rows of panel A present statistics across the 23,986 investments made by the 3,460 LPs. The penultimate row of Panel A, last column, reports that for 33.4% of investments, there is a prior investment relationship between the LP and fund family. The last row of Panel A, last column, reports the home bias rate, which is strikingly large with 75.8% of investments made into funds focusing on the home region of the LP headquarters.

In Table 2, Panel B, we present the regional distribution of LP headquarters. Focusing on all LPs (last column of Table 2), nearly half of all LPs are in North America, while another 29% are in Developed Europe. However, the regional distribution of LPs varies by LP type. For example, 82% of endowment LPs are in North America, while only 34% of financial institution LPs are in North America. Relative to other LPs, development organization LPs have greater presence in Emerging Europe, Africa, Central and South America, and Emerging Asia-Pacific.

III. Realized Performance Results

Our starting point, and the topic of this section, is reduced form regressions of fund performance. An economic conjecture is that impact funds will earn below average returns because they impose a constraint (the generation of positive externalities) on the investment opportunity set, which hurts performance. Alternatively, it is possible that the market fails to fully price the opportunities in the sectors that impact funds target (e.g., natural resources, infrastructure development), thus resulting in above-market opportunities for impact funds (though this argument requires a friction in pricing). We consider both possibilities and test for performance differences between impact and traditional VC funds.

We analyze the realized (or last reported) performance of funds in our sample: internal rate of return (*IRR*), value multiple (*VM*), and the average percentile rank of a fund relative to its vintage year and region cohort (*Rank*). We include funds with vintage years 1995 through 2012 in this analysis and use last reported performance for funds with later vintage years that are not yet completely liquidated. We regress a fund's *IRR* on a key impact dummy variable (IMP_j) that equals one for impact funds and step in control variables (denoted by the matrix X) in estimating six variations of the following regression:

$$IRR_j = \alpha + \beta IMP_j + X\Gamma + \varepsilon_j. \quad (1)$$

In model (1), we estimate a univariate regression with only the key impact dummy, which recovers the average difference in *IRR* between traditional VC funds and impact funds from Table 1. In model (2), we add controls for fund size, fund sequence number, and vintage year. In model (3), we add controls for fund industry and fund geography.

In the remaining model variations, we introduce time-varying controls for fund industry and geography. Ideally, we would like to include vintage-geography-industry fixed effects, but we lack degrees of freedom to do so (since some geographies and industries have few funds). As a compromise, we consider models with vintage-geography and static industry fixed effects (Model 4), vintage-industry and static geography fixed effects (Model 5), and fixed effects for 60 clusters of vintage year, industry and geography (Model 6). In the last model, we cluster funds into six three-year vintage groups (1995-1997 to 2010-2012), two geographies (North America/Europe versus the rest of world), and five industry groups (Information Technology and Business Services, Diversified and Consumer Discretionary, Health Care, Media and Communications, and Other Industries in Table 1, Panel C).

In each regression, we estimate robust standard errors clustered by vintage year and geography. The six regressions are also estimated using either a fund's *VM* as the dependent variable or a fund's percentile rank as the dependent variable.

Table 3 reports the coefficient estimates on the key impact dummy variable. We find that impact funds reliably underperform traditional VC funds. Focusing first on *IRR* results in columns (1) to (3) of Panel A, the univariate regression of column (1) reveals that impact funds underperform traditional VC funds by 7.89 ppts ($p < .01$). When we add controls for fund size, sequence number, and vintage year in column (2), the performance spread grows to 9.94 ppts ($p < .01$). Finally, in column (3) we add controls for fund geography and industry. While fund

geography and industry explain some of the performance variation, the performance spread of 4.70 ppts remains reliably negative. Models (4) to (6) introduce finer controls on industry and geography as discussed above and yield results similar to those of model (3). Thus, industry and geography explain some of the variation in performance between impact and other funds. However, models with industry and geography controls may underestimate the differences between impact and traditional funds if we misclassify some impact funds as traditional funds and impact funds are more prevalent in some industries and geographies.

The analysis of value multiples (Panel B) and percentile ranks (Panel C) are qualitatively similar to the analysis of IRRs. Value multiples for impact funds are reliably less than those of traditional VC funds, ranging from 0.194 to 0.465 depending on model specification. Percentile ranks for impact fund are also reliably less than those of traditional VC funds, ranging from 7.8 to 15.8 ppts depending on model specification.

These performance results represent one contribution of our analysis as we document impact funds underperform traditional VC funds. However, this fund level analysis of realized returns is not immune from concerns of selection in observability of VC fund returns. More fundamentally, ex post performance estimations do not necessarily reveal ex ante decisions to invest as a function of expected returns. As motivated in the introduction, we are interested in an *intentional* willingness to pay for impact if any, and its variation across different investors. Thus, we now turn to a willingness to pay model of this ex ante choice, which builds on the hedonic pricing and resource choice literatures.

IV. Willingness to Pay Methodology

This section presents the discrete-choice hedonic model for estimating investors' willingness to pay (WTP) for impact funds, closely following Cameron and James (1987) and Huber and Train (2001). In the original applications of these models WTP might be, for example, a homebuyer's willingness to pay for a porch, estimated from homebuyers' purchase choices among the houses for sale at a cross-section in time. Analogously, WTP in our context is the hedonic value of investing in impact, estimated from investors' choices of investments from investment opportunities available at a cross-section in time.⁸ Our WTP model is different from

⁸ VC fund structures only allow investments at fund formation. Thus, the choice of a VC investment is considered relative to other funds of the same vintage.

the housing example in that the price variable in our setting is an unobserved expected return, requiring an additional layer of estimation that we discuss in detail below.

IV.a. Random Utility Model of Willingness to Pay

Consider investor i facing a binary choice of whether to invest in fund j . A random utility model of latent utility U_{ij}^* from such an investment is given by:

$$U_{ij}^* = \beta \mathbb{E}[r_j] + \Gamma_1' X_{1,j} + \Gamma_2' X_{2,ij} + \mu_i + \delta_i \text{IMPACT}_j + e_{ij}. \quad (2)$$

The first terms $\{\mathbb{E}[r_j], X_{1,j}, X_{2,ij}\}$ and the four parameters $\{\beta, \Gamma_1, \Gamma_2, \mu_i\}$ govern the creation of utility from an investor's portfolio choice. $\mathbb{E}[r_j]$ is the expected return for fund j . $X_{1,j}$ is a matrix of non-price fund characteristics that enter the portfolio choice preference for the investment (e.g., geography, sector, fund size). $X_{2,ij}$ is a matrix of investor characteristics governing investor preferences, including the investors' recent intensity of investing in the asset class, the proximity to the investment, and the prior relationship with the VC firm. Beyond these investor-specific variables, investors may differentially value exposure to the asset class within the larger portfolio choice of all of their capital, which we cannot see. Thus, we allow for investor fixed effects, μ_i , as a heterogeneous baseline utility of investing in VC. Investors' VC investment portfolio size may grow or shrink over time, and their baseline utility may fluctuate. Therefore, we also introduce time-varying investment intensity bins, described more fully in the results section *V.a*.

The final term in equation (2), IMPACT_j , is a dummy variable equal to one if fund j is an impact fund (and 0 otherwise). Investors may have specific utility for impact; therefore, we index δ_i by i . To make this investor heterogeneity operational, we cluster investors by investor types.⁹

Omitted from equation (2) are explicit risk variables that might enter into a standard portfolio choice decision. Differences in liquidity, which might generally carry return implications, are not relevant in our context, since investing in the VC asset class – whether traditional or impact – involves liquidity lock-up and no trading. Differences in fund-specific risk might be a concern. We control for the portfolio choice variables $X_{1,j}$ to absorb risk differences as they relate to the industry sectors, geography, and size of funds chosen. Yet, residual risk differences could be

⁹ An alternative is to estimate a random effects logit (mixed logit) model of investor choice (Revelt and Train 1998); however, we found the computation to be prohibitive costly given the very extreme choice (1 fund chosen out of about 100) in VC selection. Also, given that many investors only invest in a few funds, the model was not precisely estimable.

correlated with a fund being IMPACT. If so, we would expect the ex post standard deviation of impact VC performance to be different from traditional VC. As discussed in Section II.b in conjunction with Table 1, Panel A, we find no such difference except in the dot.com period when some traditional VC funds had outside IRRs of 100% or more and drove up the skewness of return distribution for traditional funds. In contrast, downside risk is not statistically and economically different between traditional and impact funds. Finally, our results are robust to restricting our sample to 2000 onwards.

IV.b. Logit Specification and Willingness to Pay

Random utility U_{ij}^* is not directly observable to the econometrician, who instead only observes the investor's choice to invest or not. The observable, discretized investment decision U_{ij} corresponds to the latent utility U_{ij}^* as follows:

$$\begin{aligned} U_{ij}=1 & \text{ iff } U_{ij}^* > 0 \\ U_{ij}=0 & \text{ iff } U_{ij}^* \leq 0. \end{aligned} \quad (3)$$

Under the assumption that the error term ε_{ij} is distributed *iid* extreme value, this form of random utility can map to a logistic distribution with a mean 0 and variance $\pi^{2/3}$; thus, a logit estimation can uncover the parameters of equation (2):

$$\text{Logit}(\text{invest}_{ij}) = \beta E[r_j] + \Gamma_1' X_{1,j} + \Gamma_2' X_{2,ij} + \mu_i + \delta_i \text{IMPACT}_j + e_{ij} \quad (4)$$

Following Cameron and James (1987) and Huber and Train (2001), the willingness to pay for impact (*WTP*) for investor i is:¹⁰

$$\text{WTP}_i = \frac{\partial E[r_j]}{(\partial \text{IMPACT}_j)_i} = \frac{\left(\frac{\partial U_{ij}}{\partial \text{IMPACT}_j} \right)_i}{\frac{\partial U_{.j}}{\partial E[r_j]}} = \frac{\delta_i}{\beta}. \quad (5)$$

IV.c. Expected Returns Formation

Estimation of a discrete choice hedonic model requires a price variable, which in our context is the expected return for each fund, $E[r_j]$. As motivated by the literature on the

¹⁰ Technically, IMPACT is a discrete choice variable; thus the correct form is:

$$\text{WTP}_i = \frac{u_i(\cdot | \text{IMPACT}_j = 1) - u_i(\cdot | \text{IMPACT}_j = 0)}{\frac{\partial u}{\partial E[r_j]}}$$

The continuous time version is provided above for readability.

determinants of fund performance (Kaplan and Schoar, 2005; Sorensen 2007), we estimate expected returns, with estimates denoted $\widehat{\mathbb{E}}[r_j]$, based on fund characteristics observable at the time of investment. We start with the assumption that all investors have the same model for predicting fund returns and later relax this assumption. We begin by considering an investor who is making decisions about VC investments offered in the market in a particular vintage year, say 1995, as an example. The investor forms return expectations based on the information set available for the VC asset class at that point in time. The information set consists of the average asset class return observed recently and a fund-specific skill adjustment. Skill in the VC asset class shows up to the econometrician as persistence in fund series performance. To estimate the strength of persistence and the average observed asset class return, 1995 investors would use data covering vintage funds 1983 to 1990 (because of the time lag in realizing returns in VC).¹¹ Denoting these 1983 to 1990 vintage years as being in set v , we assume the 1995 investors use the following simple linear model to gauge parameters:

$$r_{jv} = \alpha_0^{1995} + \alpha_1^{1995} r_{jv}^{prior} + \varepsilon_{jv}. \quad (6)$$

The return r_{jv} of fund j in these look-back vintage years v is a function of the performance of the prior funds managed by the same VC firm (r_{jv}^{prior}) and the overall asset class performance for funds in vintage pool v (the constant).

Using the coefficients from the estimation of (6), we apply them to funds which are raising capital in 1995 to forecast expected returns for any 1995 fund j as:

$$\widehat{\mathbb{E}}[r_{j \in 1995}] = \hat{\alpha}_0^{1995} + \hat{\alpha}_1^{1995} r_{j \in 1995}^{prior}. \quad (7)$$

We roll forward this process to the remaining vintage years, until we have an estimate of expected returns for each fund j with vintage years from 1995-2014.

By definition, these forecast expected returns have measurement error since we do not observe the actual expected returns.¹² In our context, this measurement error is a common problem of over-dispersion in expected return forecasts, given by the simple relation:

¹¹ The typical private equity fund invests in companies during years 1 to 5 of the fund's life and liquidates those investments after year 5. It is during this liquidation phase that the fund's performance becomes clear to investors. Thus, a 1995 investor would have a good indication regarding the performance of funds with vintage years 1983 to 1990 because these funds would be 6 to 13 years old in 1995. In contrast, funds with vintage years 1991 to 1994 would still be in their investment phase with no or limited liquidations.

¹² Our forecast model uses fully realized fund percentile rank as dependent variables in Equation (6), while as of 1995, some of the 1983-1990 vintage funds are yet fully realized (assuming 10-year fund life, 1983-1985 funds are at least 10 years old, whereas 1986-1990 funds are still less than 10 years old). This may introduce measurement errors to our

$$\widehat{\mathbb{E}}[r_j] = \mathbb{E}[r_j] + u, \quad (8)$$

where $\mathbb{E}[r_j]$ is the true but unobservable expected return, and u is measurement error that is uncorrelated with $\mathbb{E}[r_j]$. The importance of this over-dispersion comes when we turn to estimating WTP in the logit formation. Over-dispersion in $\widehat{\mathbb{E}}[r_j]$ may cause attenuation bias in the $\widehat{\beta}$ coefficient on $\widehat{\mathbb{E}}[r_j]$ when we estimate the logit equation (4), relative to the true β if we had the precise $\mathbb{E}[r_j]$. Because $WTP_i = \frac{\delta_i}{\beta}$, attenuation in $\widehat{\beta}$ implies an over-estimate of WTP .

We take two steps to correct the bias. First, we seek to remedy a source of error, which is our inability to observe the soft information entering the assessment of skill. We augment equation (6) to include indicator variables as to whether the fund is missing prior fund performance information ($Miss_j^{prior}$), is a first-time fund ($First_j$), and/or is an impact fund ($IMPACT_j$). This augmented model, dropping the vintage subscripts to reduce equation clutter, is given by:

$$\begin{aligned} r_j = & a_0 + a_1 r_j^{prior} + a_2 Miss_j^{prior} + a_3 First_j + a_4 IMPACT_j \\ & + a_5 (Miss_j^{prior} * IMPACT_j) \\ & + a_6 (First_j * IMPACT_j) + \varepsilon_j. \end{aligned} \quad (9)$$

In estimating these regressions, we use percentile ranks as the performance measure. Table 4 reports a summary of estimates from the 20 rolling regressions estimating equation (9), corresponding to fund expectations formed from 1995 to 2014. In Panel A, we summarize the coefficient estimates and associated t-statistics on the model's independent variables across the set of rolling estimations. Consistent with the literature, prior fund performance carries the vast majority of the explained variation. The only other reliable relationship is that that first-time funds tend to have subpar performance.¹³

model in one or more ways. For example, if investors apply interim-to-final rank transition in their true expected return formation using their soft information, our model approximates that with some measurement errors. Alternatively, investors may attempt to isolate the component of performance persistence that is due to skill (and investable) from spurious correlation due to contemporaneous exposures (Korteweg and Sorensen, 2017), in which case our naive model also produces forecast expected return with measurement errors. Furthermore, investors may be heterogeneous in their soft information possessed to form their expected returns. We present our expected return model that incorporates investor heterogeneity in the next section.

¹³ We consider a number of robustness checks to ensure our results are not driven by the specific model that we use to predict expected returns. First, our results are robust to alternative specifications of the expected return model of equation (5). For example, we add additional lags of past fund performance, fund industry fixed effects, and fund geography fixed effects. These additional variables are not consistently related to fund performance nor does their inclusion materially affect the WTP estimates. Consequently, we opt for the more parsimonious model.

Second, we employ a correction for the logit estimates attenuation by applying a shrinkage procedure used in practice. Because over-dispersion is a common issue in portfolio choice, investors knowingly shrink extreme forecasts toward a global mean, as in the seminal portfolio optimization models of Jorion (1986) and as applied in expected returns or cost of capital estimations in Fama and French (1997).

The shrinkage procedure begins with regressing realized fund return (r_j) on the estimated expected returns $\widehat{\mathbb{E}}[r_j]$:

$$r_j = \gamma_0 + \gamma_1 \widehat{\mathbb{E}}[r_j] + e_j. \quad (10)$$

Our estimates are $\gamma_0 = \underbrace{0.25}_{p < 0.001}$ and $\gamma_1 = \underbrace{0.50}_{p < 0.001}$. The γ estimates imply that our $\widehat{\mathbb{E}}[r_j]$ has some information about future returns ($\gamma_1 \neq 0$), but that $\widehat{\mathbb{E}}[r_j]$ is imprecise ($\gamma_1 \neq 1$ and $\gamma_0 \neq 0$). Then, following standard shrinkage procedure, we calculate the shrinkage estimate of expected returns $\widehat{\mathbb{E}}_{shrink}[r_j]$, as the prediction from equation (10):

$$\widehat{\mathbb{E}}_{shrink}[r_j] = 0.25 + 0.50 \widehat{\mathbb{E}}[r_j]. \quad (11)$$

Whereas $\widehat{\mathbb{E}}[r_j]$ has a ranking range of 0.16 to 0.72 (on a natural percentile rankings range of 0 to 1), $\widehat{\mathbb{E}}_{shrink}[r_j]$ has a range of only 0.28 to 0.61, reflecting the shrinkage to address imprecision. We use $\widehat{\mathbb{E}}_{shrink}[r_j]$ to estimate Equation (4).

Importantly, using the true realized returns to shrink the dispersion in estimated expected returns asymptotically eliminates attenuation bias in the logit *WTP* estimation when the following two key assumptions are added to a classic errors-in-variable analysis:

- (i) The ex post residual of realized fund returns relative to true expected returns is uncorrelated with $\mathbb{E}[r_j]$. Specifically, $\text{cov}(\mathbb{E}[r_j], \xi) = 0$, where this residual is given by:

$$r_j = \mathbb{E}[r_j] + \xi \quad (12)$$

This condition assumes that the unexpected part of realized returns is not systematically higher [or lower] for funds with high expected returns and is the implicit assumption made in the asset pricing literature, which uses realized returns to understand temporal and cross-sectional variation in unobserved expected returns.

In venture capital, returns are highly nonlinear and positively skewed. To deal with this issue, our empirical analysis uses percentile ranks relative to cohort funds, which are bounded between 0 and 1. In theory, these bounds could generate $\text{cov}(\mathbb{E}[r_j], \xi) < 0$, since an

expected percentile rank near one (zero) will have negative (positive) estimation error because of the boundary. In practice, we do not believe these boundary conditions are binding on errors since true expectations of percentile ranks would not approach the boundary; stated differently, investors do not expect to be able to pick the top and bottom performing funds from a cohort. The actual range of percentile ranks that we estimate after shrinkage is 0.28 and 0.61, with a standard deviation of 0.035. This range is a reasonable estimate of the range of ex-ante expected percentile ranks and they are far from the boundary conditions.

- (ii) Measurement error u in forecast expected returns, $\widehat{\mathbb{E}}[r_j] = \mathbb{E}[r_j] + u$ from equation (8), is uncorrelated with the residual in the realized return relative to the true expected return, $cov(u, \xi) = 0$. We can think of no reason why errors in our forecast returns would be correlated with errors in realized returns.

In Appendix B, we show that the bias in our WTP estimates is positively related to the two covariance terms and is positive if $(cov(\mathbb{E}[r_j], \xi) + cov(u, \xi) > 0)$. To simplify the analysis below, we also assume the measurement error u in forecast expected returns, $\widehat{\mathbb{E}}[r_j] = \mathbb{E}[r_j] + u$ from equation (8), is uncorrelated to the true expected returns, $cov(\mathbb{E}[r_j], u) = 0$; this assumption only affects the absolute magnitude of the attenuation bias if the two assumptions above are violated.

To show how shrinkage with realized returns removes attenuation under (i) and (ii) from above, imagine a simple model of an outcome variable y (investment in a private equity fund in our case) such that $y = a + b\mathbb{E}[r_j] + e$, where the econometrician must estimate with $\widehat{\mathbb{E}}[r_j]$ instead of $\mathbb{E}[r_j]$. The standard estimate of the slope coefficient in the classic errors-in-variable analysis is:

$$\text{plim}(\widehat{b}) = \frac{b\sigma_{\mathbb{E}[r_j]}^2}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2} = \lambda b, \quad (13)$$

where $\lambda < 1$ is the attenuation bias. Note that the slope parameter (γ_1) of the shrinkage regression of equation (10) yields an estimate of this attenuation bias:

$$\gamma_1 = \frac{cov(\widehat{\mathbb{E}}[r_j], r_j)}{\sigma_{\widehat{\mathbb{E}}[r_j]}^2} = \frac{cov(\mathbb{E}[r_j] + u, \mathbb{E}[r_j] + \xi)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2} = \frac{\sigma_{\mathbb{E}[r_j]}^2}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2} = \lambda. \quad (14)$$

Thus, the shrinkage regression provides a valid correction for the attenuation bias.

IV.d. Heterogeneity in Expected Returns Forecast and Use

The logit model described in Eq. (4) assumes that investors are homogenous in their forecast of expected returns. In practice, investors may exhibit heterogeneity in their forecast of expected returns because of different forecast mechanisms or because of interest in only a subset of funds (Hochberg et al. 2014; Cavagnaro et al. 2019). The dimension of concern to us is bias at the LP investor type level. Thus, we estimate $\widehat{\mathbb{E}}_{type,shrink}[r_j]$ uniquely for each investor type as a robustness check on our results. To implement these expected return forecasts, we limit the set of funds in which an investor has an interest to those funds with investment by investors of the same type (e.g., financial institutions, development organizations, foundations, etc.).¹⁴ Estimating by LP type also allows us to incorporate prior relationships as part of the forecast. Different investor types have different propensities to have a prior relationship with a fund in question, which will provide heterogeneity in the use of soft information.¹⁵ These heterogeneous expected return estimates are correlated with the homogeneous expected returns (with a correlation coefficient of 0.76), but as anticipated have more variation (a standard deviation of 0.042 versus 0.035).

Having estimated LP type-specific expected returns for each fund, we then estimate:

$$Logit(Invest_i) = \beta \widehat{\mathbb{E}}_{type,shrink}[r_j] + \Gamma_1' [X_{1,j}] + \Gamma_2' X_{2,ij} + \mu_i + \delta_{type} IMPACT_j + \varepsilon_{ij}. \quad (15)$$

We are agnostic about which estimates are superior and report estimates from both the homogenous and heterogenous expected return models to generate a range of reasonable WTP estimates. While the heterogenous model is theoretically appealing, as empiricists we are not confident that the introduction of heterogeneity *necessarily* improves the precision of our estimates and are concerned that it might introduce unintended bias in our estimate due to the quality of our LP holdings data. For instance, there are some unobserved LP investments due to data limitations, but the heterogenous model draws a bright line between funds in which we observe at least one investment from a given LP type vs. funds with no observed investments by the LP type. The

¹⁴ The forecast $\widehat{\mathbb{E}}_{type,shrink}[r_j]$ will only be defined over a subset of funds. Because we are interested in how our estimate of WTP varies when allowing $\widehat{\mathbb{E}}_{shrink}[r_j]$ to be instead unique to an investor type, $\widehat{\mathbb{E}}_{type,shrink}[r_j]$, we want to reproduce the full dataset of funds as the opportunity set for investment. Thus, we fill in $\widehat{\mathbb{E}}_{type,shrink}[r_j] = \widehat{\mathbb{E}}_{shrink}[r_j]$ for the funds j not estimated by a particular investor type.

¹⁵ For each fund in a given LP type sample, we calculate the average of the relationship dummy variable across all LPs who invested in that fund and add this relationship propensity as an additional independent variable to Equation (9) when estimating LP type-specific expected returns.

introduction of this type I error may more than offset the theoretical benefit of heterogenous expected return model.

As a final robustness check in our analysis of WTP patterns across LP types, we allow for the possibility that investors are heterogeneous in their use of expected returns because they face different portfolio choice considerations. The model described in Eq. (15) assumes that investors are homogenous in their use of forecast expected returns, though forecasts vary across LP types. Yet, investors may exhibit heterogeneity in their portfolio diversification model (e.g., preferring investments in a particular industry or geography). Thus, in our analysis of WTP across LP types we allow heterogeneous expected returns forecasts to interact with the industry and geography.

We amend equation (15) to allow for these heterogeneities by investor type:

$$\begin{aligned} \text{Logit}(\text{Invest}_i) = & \beta \hat{\mathbb{E}}_{\text{type}, \text{shrink}}[r_j] + \mathbf{B}'_1[X_{1,j} \cdot \hat{\mathbb{E}}_{\text{type}, \text{shrink}}[r_j]'] + \Gamma'_1[X_{1,j}] + \\ & \Gamma'_2 X_{2,ij} + \mu_i + \delta_{\text{type}} \text{IMPACT}_j + \varepsilon_{ij}. \end{aligned} \quad (16)$$

The resulting WTP for impact embeds a richer investor type-level application of the role of returns in the portfolio choice model while maintaining a baseline property of hedonic discrete choice models that heterogeneities in the magnitude of the coefficient on the hedonic variable (impact designation in our case) be calculated relative to common coefficients on the price variable (representing the change in utility per unit of price) that are fixed across the choice agents. This WTP calculation is:

$$WTP_{\text{type}} = \frac{\hat{\delta}_{\text{type}}}{\left(\hat{\beta} + \hat{\mathbf{B}}'_1[\bar{X}_{1,j}]_{\text{type}} \right)}, \quad (17)$$

where $[\bar{X}_{1,j}]_{\text{type}}$ is the average of exposures to the industry, geography and discretized fund size buckets by investor type.

V. Willingness to Pay Results

V.a. Aggregate WTP Results

Table 5, reports coefficient estimates from the logit model of investment choice, akin to those used in the discrete choice implementations in venture capital (Ljungqvist et al., 2006; Bottazzi et al., 2016). Panel A presents the results using homogenous expected returns (corresponding to Eq. (4)); Panel B uses heterogenous expected returns (Eq. (15) but with a single impact coefficient). The dependent variable is an investment indicator variable. The set of observations are all potential investments into the funds that close in a given year by all of the

active LPs with at least one fund investment in that vintage year. This crossing of all LPs and all VC funds active in each vintage year yields over 3 million fund-LP observations, pooled across years. Our main independent variables of interest are *Expected Returns* (forecasted and shrunk per the methodology section) and *Impact*. To prevent the impact coefficient from picking up LPs' portfolio choice demand for particular investment characteristics, we include fixed effects for fund vintage, geography and industry. We also include two variables capturing paired characteristics between the investor and the fund. First, following Hochberg and Rauh (2013), we include a home bias variable, defined as whether fund j focuses its investments on the home region of investor i , where we consider eight major regions globally. Second, because the prior relationship between an investor and a particular VC fund manager matters (Lerner, Schoar and Wongsunwai 2007; Hochberg, Ljungqvist, and Vissing-Jørgensen 2014), we include an indicator variable for a prior investment relationship between investor i and any prior fund managed by fund j 's fund manager. We measure expected fund size as the 3-year prior average of the median fund size in the vintage and market (U.S. or non-U.S.).

We first show our aggregate WTP result with two models of investor heterogeneity in terms of their preferences for the VC asset class. In column (1), we absorb investment rate heterogeneities with 368 dynamic (i.e., time-varying) buckets of LP type crossed with the discrete number of prior investments in the previous 3 years. Each investor group consists of investors of same LP type (e.g., development organization, foundation, pension, etc.) and the same average number of investments per year made in the prior three years. In column (2), the model is conditional logit at the individual LP investor level. The conditional logit levels LPs according to their average likelihood of investing in a VC fund. We prefer the dynamic LP investment groups of column (1). The benefit is in allowing for dynamic appetite for the VC asset class, since we cluster together, for example, all foundations which have 5 total investments in the prior 3 years or public pension funds with 20 investments in the VC asset class in the prior 3 years, etc.¹⁶

In Panel A, column (1), the coefficient on impact is 0.591, and the coefficient on expected returns is 3.354 ($p < .01$ for both coefficients). The WTP estimate is reported as the ratio of these estimates. We find that investors are willing to pay 18 percentile ranks ($0.18 = 0.591/3.354$) for impact, where a percentile rank runs from 0 (0th percentile) to 100 (100th percentile). In column (2), estimates from the conditional logit model imply a similar WTP of 17 percentile ranks. A

¹⁶ In earlier drafts of the paper, we estimated linear probability models and obtain similar results.

WTP of 18 percentile implies that the average investor is indifferent (obtains identical utility) between investing in an impact fund at the 41 percentile rank of its vintage-geography cohort and investing in a traditional VC fund at the 59 percentile rank. In terms of the expected excess IRR of the fund, this suggests that investors who invest in impact funds are willing to give up 3.7 ppts in expected excess IRR (see Appendix Table A3 for the mapping of percentiles to excess IRRs). This 3.7 ppts is 11% of a cross-sectional standard deviation of IRRs (0.32).

In Panel B, column (1), the estimated impact coefficient and expected return coefficient are 0.613 and 4.655, which yields a $WTP = 0.13 = .613/4.655$. A WTP of 13 percentile rank suggests that investors are willing to give up 2.5 ppts in expected excess IRR, which is lower than the estimate in Panel A. In Panel B, column (2), conditional logit estimates yield a similar WTP estimate. Overall, our WTP framework suggests that an investor willingness to pay lies between 2.5% to 3.7% in IRR. These WTP estimates are smaller, but within one standard error of the performance shortfall that we estimate in the reduced-form regressions of Table 3.

In columns 1 and 2, we assume that the investment opportunity set for all LPs in a given year is the set of funds completing fundraising that year. In practice, opportunity sets may be either more restrictive or more expansive.

One story is that some LPs are more likely to invest in high-performing funds, either due to LP skill differential or assortative matching between elite VC firms and elite LPs (Cavagnaro et al. 2019; Lerner et al. 2019). Sensoy, Wang and Weisbach (2014) document that access disparities between LP types (e.g., endowments vs. pensions), as well as returns to such access disparities, largely dissipated in the 1999-2006 period. Yet the possibility remains that some specific LPs continue to enjoy exclusive access to top-performing VC firms that is denied to the rest, and that this in turn makes investors who invest in (less exclusive) impact funds appear to accept lower financial returns.

Another possibility is that fundraising campaigns may last longer than a year for some funds. In such cases, funds with vintage year y were *effectively* fundraising in year $y-1$, and LPs who were in the market in year $y-1$ had the opportunity to invest in that fund. Yet another possibility is that for some LPs the fund selection/due diligence may take more than a year. In those cases, LPs who did not pull the trigger till year $y+1$ were *effectively* looking to invest in year y , and had the opportunity to invest in vintage y funds.

Columns (3)-(6) report results of tests where LPs are designed to have either more restricted or expanded opportunity sets. In column (3) and (4), we present estimates using the same empirical model as column (1), except we restrict the possibility of investing in funds managed by elite VC firms only to a subset of LPs who have already invested in the VC firms' previous funds. The two columns differ in the way we define an elite VC firm. In column (3), elite VC firms are those with at least one fund with top-quartile performance (ranked against its vintage cohorts) among the three previous funds. In column (4), we define elite VCs as the 15 VC firms that are chosen as "Best VCs" in Metrick and Yasuda (2010). We find that our impact coefficient and WTP estimates are quite robust to these rationed opportunities sets, with only slight variation across columns.

In columns (5) and (6), we turn to considering an expansion of opportunity sets, rather than a rationing. In column (5), we assume that the fund raised in year y was also fundraising in year $y-1$ if more than 5 years had lapsed between the vintage years of the current fund and the previous fund. Operationally, we treat these funds as being in the market in both $y-1$ and y . In column (6), we assume that LPs who made no investments in year y but invested in $y+1$ were in fact already looking to invest in year y but passed. Alternatively, some of those LPs with investments in year $y+1$ actually made the commitments into the funds in year y , but the funds did not close until $y+1$. Either way, operationally we treat these LPs as being in the market in both y and $y+1$. In both columns (5) and (6), the sample size expands because either the set of funds (column (5)) or the set of LPs (column (6)) in a given year is greater than in our baseline sample. Again we find that our aggregate WTP estimates are very robust to the expanded opportunity sets, as the results in columns (5) and (6) are very similar to those in column (1).

Before proceeding to the analysis of WTP across different LP types, we estimate the WTP across five geographic regions using the model of column (1), but interacting impact with five regions. We summarize the WTP by region in Figure 2. Circumstantial evidence suggests that demand for impact should be higher for investors domiciled in Europe. In their 2014 report, the Global Sustainable Investment Alliance (GSIA) reported that 59% of total managed assets in Europe are in SRI strategies compared to only 18% of assets in the US, 17% of assets in Australia, and 1% of assets in Asia. This suggests that Europeans value positive externalities more than others. Our results strongly confirm the circumstantial evidence. North Americans have a positive and significant WTP for impact, but it is smaller than the baseline estimate (10-12 percentile ranks

or 1.6-2.2 ppts in expected excess IRR). In contrast, investors from Developed Europe and from Africa, Latin America, and Eastern Europe have much higher WTP of 20-28 percentile ranks and 25-35 percentile ranks, respectively, corresponding to an expected excess IRR WTP of 4.2 to 8.7 ppts.

V.b. WTP by LP Type

In this section, we estimate variation in WTP across LP types. The WTP estimate of 13-18 percentile ranks as reported in Table 5, column (1), is an average effect among all investors in our sample. It does not imply that all investors exhibit the same willingness to pay. In practice, investors are likely to be heterogeneous in their taste for impact with some investors valuing the attribute more than others for social, institutional, legal or regulatory reasons.

Table 6 presents the results. In all columns we allow investors' taste for impact to vary across nine LP types and five geographic regions. In column (1), we estimate the logit model using homogenous expected returns corresponding to Eq. (4). In column (2), we use heterogeneous expected returns corresponding to Eq. (15).

Figure 3 summarizes the WTP results by LP type. We find that development organizations, financial institutions and public pensions have large positive WTP for impact with estimates ranging from 13-27 percentile ranks (2.5-6.2 ppts in excess IRR). In contrast, endowments, corporations, institutional managers, wealth managers, and private pensions have negligible WTP for impact, as their impact coefficients in the logit model are not significantly different from zero. Foundations have a small positive and statistically significant WTP (6 percentile ranks) in column (2). Although the WTP magnitudes fluctuate across models, the patterns across LP types are very robust.

In addition to testing the null that the individual WTPs are equal to zero, we also test the null hypothesis that LP types have equal WTP; we can easily reject the null hypothesis that the WTP is equal across LP types ($p < .001$). In pairwise tests of the null hypothesis of equal WTP, we cannot reject the null in pairwise tests for Development Organizations, Financial Institutions, and Public Pensions. These are the same LP types who exhibit a robustly positive WTP for impact throughout our analysis. We always reject the null that these three LP types' WTPs are equal pairwise to WTPs of the other six LP types.

One explanation for our results might be that investors look as if they are willing to pay for impact, but in reality they erroneously expect returns on impact funds to be comparable to those earned on other VC funds. Because this story would be applicable to investors new to impact investing but not for investors repeatedly choosing impact VC funds, we can test this prediction. In untabulated results, we re-estimate the specification of Table 5 column (1) modified to include the impact dummy interacted with an indicator for an LP having prior impact investing experience. We find that both the impact indicator and the interaction term are positive and significant, with the interaction term coefficient being twice as large as the impact coefficient. Put simply, investors with prior investments in impact funds are much more likely to invest in impact. This result combined with the PME result that impact funds on average do not beat the market ex post (Table 1) suggests that our main results are capturing investors' preferences rather than inaccurate beliefs.

As a robustness check of observed variation in WTP across LP types, we allow for variation in the portfolio choice considerations of LPs as described in Eq. (16) with results summarized in column (3). The general pattern of WTP across LP types is quite similar with the exception of institutional LPs who have a greater WTP when we consider portfolio choice considerations.

Finally, column (4) of Table 6 reports a model where we exclude the forecast expected returns. Forecasted expected returns, from our main specification, are lower for impact funds. Thus, we expect that, by excluding these forecasts, the coefficients on impact interacted with the investor types should be lower as this variable is picking up a lower desirability for the fund associated with missing variable of expected returns. Indeed, this is what we find. The coefficients on all the impact interactions with investor type shift negatively, while the patterns of relative magnitudes of impact coefficients across investor types align exactly with our previous specifications.

V.c. Attributes

V.c.1. Discussion of Investor Attributes

In this section, we analyze the origins of varying utility over impact by studying attributes of investors that could motivate WTP. Table 7 presents six investor attributes (across columns) and their mapping to the ten LP types (rows). The first three attributes characterize inherent LP features. *Household* categorizes investors based on the constituents of the capital (organizations or households). *Intermediated* classifies the LP types based on whether the capital is intermediated

through an asset manager, with an observation that intermediation creates distance between the ultimate owner of capital and those who facilitate capital allocations. *Mission* identifies investors (development organizations and foundations) that have an impact mission as a primary goal.

The last three attributes (*Pressure*, *Laws*, and *Charters*) characterize the implicit or explicit rules governing different investors' ability and desire to invest in impact funds. For these attributes, we exploit the fact that laws governing these rules vary by geography, thereby allowing us to estimate the WTP associated with these rules within an LP type fixed effect model. Although we do not claim causal identification, this within-LP-type estimation strategy offers suggestive evidence that rules may directly affect WTP for impact.

Pressure (column 4) identifies regulatory or political pressures that encourage impact investment. Worldwide, public pensions, despite commonly being subject to a fiduciary duty standard, may face political pressure to increase the (perceived or real) welfare of voting populations.¹⁷ Likewise, financial institutions worldwide may have incentives to invest in impact funds that serve low- to moderate-income communities if such investments garner goodwill from customers or regulators. However, in the U.S., additional regulations (or the threat to regulate) are imposed on financial institutions in a way not operative in other countries. Specifically, U.S. commercial banks are subject to investment obligations to serve their local low- and moderate-income communities under the Community Reinvestment Act (CRA) (CRA Investment Handbook, 2010, p.24). Likewise, insurance companies in some of the large U.S. states (e.g., Texas, New York, and California) must comply with state-level insurance regulations akin to the CRA that require them to invest in local communities. Even outside of those states, insurance companies in the U.S may face pressure to invest in impact locally in order to preempt passage of a federal CRA-like regulation for insurance (Gainer 2009). We exploit this geographic variation by coding Pressure equal to one for U.S. financial institutions (banks and insurance companies), as well as for public pensions worldwide, and zero for others.

Laws (column 5) identifies investors facing fiduciary duty legal restrictions *against* impact investing. While most public pensions worldwide face formal (legal or regulatory) restrictions to act solely for the benefit of pension recipients by achieving target investment returns and providing

¹⁷ Public pensions may also face pressure to serve the political interests of their boards, which are often pro-labor and consider local job creation as an important policy goal. Consistent with this idea, Dyck, Manoel, Morse, and Pomorski (2016) and Andonov, Hochberg, and Rauh (2018) both document that the investments of public pensions are affected by the degree to which the boards governing the pensions are appointed by government officials.

liquidity while minimizing risks and costs, regulations concerning investing principles of other entities such as endowments, foundations, and private pensions are typically less restrictive. However, in the U.S., foundations, endowments, and private pensions face more restrictive fiduciary standards than their non-U.S. counterparts. U.S. private pensions are subject to the 1974 Employee Retirement Income Security Act (ERISA), which states that a pension plan fiduciary could consider non-financial factors (such as environmental or social impact) only if doing so would result in the same level of return at the same level of risk as comparable investment alternatives.¹⁸ Likewise, the Uniform Prudent Management of Institutional Funds Act (UPMIFA), which governs the management of U.S. foundations and university endowments, imposes fiduciary standards similar to those of ERISA (see Geczy, Jeffers, Musto and Tucker, 2015). However, unlike ERISA, UPMIFA provides an additional duty of obedience to the unique charitable mission of the organization. Furthermore, tax laws in the U.S. create an additional hurdle on foundations. The U.S. tax authority requires foundations to maintain a 5% annual payout rate to keep their tax-exempt status; impact investments in the form of program-related investments (PRIs) can count if certain eligibility tests are met.¹⁹ While the policy may have been intended to encourage PRIs, the ambiguity around the test outcome and the perceived threat of tax-exempt status loss may subdue foundations' WTP for impact in their investment portfolio.

Charters (column 6) identifies restrictions against impact investment in the form of organizational charters, excluding investors already covered by legal restrictions (column five) under the assumption that legal restrictions are more binding. Charters require organizations to maximize value for shareholders, which may constrain investments into impact funds. The list of organizations bound by charters includes financial institutions, corporations, non-U.S. private

¹⁸ U.S. NAB (2014). The ERISA guideline issued in 2008 and in effect until 2015 went even further, stating that pensions "... may never subordinate the economic interests of the plan to unrelated objectives, and may not select investments on the basis of any factor outside the economic interest of the plan" (Johnson (2014)) and that those who consider noneconomic factors could be challenged later for noncompliance with ERISA absent a written record demonstrating no financial sacrifice was made. The new ERISA guideline issued in 2015 withdraws this language and reverts to the original ERISA restrictions. See: <https://www.dol.gov/opa/media/press/ebsa/ebsa20152045.htm>.

¹⁹ Specifically, the PRIs must further the foundation's organization mission, and the financial returns cannot be a primary purpose of the investment. In practice, PRI investors are required to demonstrate that conventional investors maximizing returns would not invest at the same term as their investment terms. This is simple if the financial instrument used is a below-market return debt security. Precisely for this reason, below-market-return loans are popular vehicles for PRIs. In contrast, equity vehicles are relatively rare, possibly because of the perceived risk of violating the PRI eligibility requirement if it makes too much profit ex post.

pensions (subject to fiduciary responsibility via their parent corporate charters), and institutional asset managers (subject to fiduciary standards of the institutional sources of capital).

Finally, as we noted in the introduction, both the number of and the dollar amount of assets managed by organizations that are UNPRI signatories have sharply increased in the recent years. Since investors signing the UNPRI are doing so with a cost of compliance, it is plausible that they also have higher willingness to pay for impact compared to non-signatories because of a mission objective. This mission objective may be a fixed attribute for the investor or may reflect some time-varying interest in generation of non-pecuniary benefits from their portfolios. Thus, we introduce two final variables – an indicator variable that takes a value of one if the investor is a UNPRI signatory and an indicator variable that takes a value of one for UNPRI signatories in the years after signing.

V.e.2. WTP Results by Attribute

Table 8 reports the role of investor attributes in generating WTP for impact. The specification is again the logit estimation with dynamic LP investment groups. Columns (1)-(3) present the results using homogenous expected returns; columns (4)-(6) are for heterogenous expected returns. The columns differ as follows. Column (1) and (4) provides the baseline logits. Column (2) and (5) includes fixed effects for LP geography interacted with impact. This forces the estimation to identify attributes' effects beyond regional preferences for impact. Column (3) and (6) includes LP type interacted with impact fixed effects. The inherent LP type attributes – *Mission*, *Household*, and *Intermediated* – do not vary by geography and thus drop in this specification.

We report three main attributes results that inform our understanding of investors' WTP for impact. First, having a mission objective increases investors' WTP for impact. Investors with *Mission* objectives have a WTP for impact of 17-27 percentile ranks (3.4-6.2 ppts in expected excess IRR). We also find evidence supporting a mission objective in considering the coefficients on UNPRI variables. Both the *UNPRI Signatory* and the *UNPRI Post-Signing* variables have positive and significant coefficient across columns. The WTP of being a *Signatory* type is 6-12 percentile ranks, while that for a *Post-Signing* dummy is additional 17-22 percentile ranks. UNPRI signing captures both temporal *and* cross-sectional differences in investors' willingness to pay for impact.

Second, investors facing *Pressure* from political or regulatory institutions exhibit a high WTP. In the saturated model of columns (3) and (6), the estimated WTPs for *Pressure* are 12-16 percentile ranks (2.3-3.3 ppts in excess IRR). This evidence is consistent with the interpretation that investors facing *Pressure* returns to satisfy the pressure they face from constituents or to comply with regulators to allocate capital to investments that generate positive externalities.

In auxiliary analyses, we find the effect of *Pressure* can be linked to a preference for local investments by investors who face pressure to invest with impact. We previously noted that financial institutions within the U.S. are subject to regulatory pressure to invest locally, while public pensions funds worldwide are subject to political pressure to do so. In both of these scenarios, the mechanism of pressure acts locally. We test whether pressure is a local concept and find that indeed this is the case: investors subject to pressure are much more likely to invest in impact funds that are focused on generating externalities at home than abroad or in another unrelated region (see Appendix Table A4).

Third, we find that *Laws* of fiduciary duty against dual-agenda impact investing have a significantly negative effect on decisions to invest in impact. In the saturated model of columns (3) and (6), the estimated WTPs for *Laws* are -20 to -28 percentile ranks (-4.2 to -6.7 ppts in excess IRR). Laws like ERISA and UPMIFA matter. In contrast, we find that having *Charter* restrictions against impact alone does not materially affect their demand for impact on average; shareholders' recourses (e.g., lawsuits and management turnover) do not seem to bind against impact investing in a way that we can identify.

Note that our results are a mixture of utility from regulatory compliance, social signaling and preferences as underlying investor motivations. We do not attempt to disentangle the sources of utility across different investors, but our results have some counterparts in the literature. Akin to our *Mission* result, Riedl and Smeets (2017) document that both signaling and preferences explain investors' SRI decisions. Yet, in our data, investors that are subject to regulatory *Pressure* may be more driven by the signaling benefits or regulatory compliance. For example, financial institutions may be interested in impact investing as a method of complying with regulator or fostering local goodwill (a form of social signaling). Likewise, pension managers may have signaling incentives over the distilling perception of local job creation that drives portfolio decisions (Dyck et al., 2016; Andonov et al., 2018). As a counterpoint, Bauer et al. (2019) find in an experiment using a Dutch pension program that retirees themselves support allocating more of

their retirement portfolios to sustainable investments even when they expect financial returns to be lower. Disentangling between these underlying mechanisms is an important question that we leave for future research.

V.f. WTP by Impact Category

In this section we examine whether investors' willingness to pay for impact varies by the impact category (e.g., the environment, women and minority businesses, poverty). Figure 4 presents the results of the logit model estimation of Table 5, column (1), but interacts the impact dummy with each of the six impact categories we describe in Section II.a. Note that these categories are not mutually exclusive, as a given fund can meet the criteria of more than one impact category.

The results indicate that investors exhibit a positive willingness to pay when considering investing in impact funds focusing on environment, poverty, and women or minority issues. Investors are willing to forego 15-22 percentile ranks (3.0-4.7 pts in excess IRR) in performance when investing in these impact categories. Notably, these are all arguably categories with high public good or externality content. In contrast, investors do not exhibit significantly higher WTP when considering investing in impact funds focusing on SME funding relative to nonimpact funds. However, 57% of impact funds in the SME category also have a poverty focus and are thus captured by the poverty category. SME funds without a poverty focus often target particular geographic areas (e.g. Oregon Investment Fund) and are unlikely to attract interest from investors other than local financial institutions and pensions.

VI. Conclusion

Our goal has been to understand whether investors are willing to accept lower financial returns for nonpecuniary benefits of intentional impact investing. We document that ex post financial returns earned by impact funds are 4.7 pts lower than those earned by traditional VC funds, even after controlling for a host of fund characteristics. To examine whether investors in impact funds willingly trade off *expected* financial returns at the time of investment decisions, we use a hedonic pricing framework of willingness to pay for impact. We find that impact investors

are on average willing to forgo 13 to 18 percentile ranks of vintage-geography benchmarked performance or about 2.5 to 3.7 ppts in expected excess IRR.

Willingness to pay varies considerably over who controls the capital. To unpack the heterogeneity across investors, we categorize investors into nine broad categories. Investors in three of the nine categories – development organizations, financial institutions, and public pensions – exhibit reliably positive willingness to pay for impact. We then delve into what attributes of investors affect investors’ willingness to pay for impact. Not surprisingly, investors with organizational missions and investors who are PRI signatories (especially post-signing) have high WTP. In addition, we find that investors facing political and/or regulatory pressure (e.g., banks and insurance companies in the U.S. that face CRA and other equivalent requirements) and those benefiting from political or local goodwill exhibit a higher willingness to pay for impact. In contrast, laws restricting financial return-sacrificing investment (e.g., ERISA and UPMIFA in the U.S.) may hinder WTP for impact. Since the number of high-fiduciary LPs affected by such legal restrictions is large (1,258 out of 3,504 in our sample), this finding has important implications for how subtle shifts in legal interpretations of institutions’ fiduciary duty may affect investors’ willingness to pay for impact. For example, in the U.S., the IRS and Treasury issued guidance on mission-related investments in September 2015, assuring that it is possible for private foundations to make a prudent investment using the foundation’s assets that advances the foundation’s charitable purpose, even if the investment offers a lower rate of return, higher risk, or lower liquidity than alternative investments that do not further charitable purposes. To the extent that (either real or perceived) risk of a tax penalty from making impact investments had a negative effect on their WTP prior to this ruling, this regulatory shift may affect foundations’ WTP in the future years. Moreover, recent growth in fundraising by impact buyout and impact infrastructure funds by mainstream GPs like KKR and Bain Capital is consistent with asset managers meeting investors’ demand for dual-bottom-line funds. Since a positive loading on the impact implies lower performance-sensitivity in fundraising, these GPs may find the impact designation valuable for their objective of maximizing NPV of future fee revenues (Chung et al. 2012).

In combination, our results provide compelling evidence that investors are willing to pay for nonpecuniary characteristics of investments. This result indicates that the capital allocation decisions, though certainly governed by the linchpin risk-return tradeoff of wealth maximization in standard utility models, are also shaped by the real-world consequences of the investments that

people make. The willingness to pay for impact varies considerably across legal and regulatory environments, investor geography, and time. This variation opens up a number of avenues for future research that explores the factors that govern the variation that we document.

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Appendix A

Table A1 contains a list of search terms used to identify impact funds.

Table A2 contains the list of countries with GDP per capita less than \$1400.

Table A3 presents the mapping of percentile ranks to excess IRR.

In Table A4, we test the home bias argument for the pressure result in Section *V.e.2* by adding a triple interaction of *Impact*, *Pressure*, and *Homebias*, a dummy variable that equals one if the fund is in the same region as the LP. Table A4 reports logit estimates with dynamic LP investment groups akin to the attribute table (Table 8), where we add fixed effects for the interaction of impact and LP geography (column 1 and 4), the interaction of impact and LP type (column 2 and 5), or both interactions (columns 3 and 6). In columns (1) to (3), we show the *Pressure* WTP results of Table A5 are qualitatively unchanged from Table 8 when we pare down the model to focus only on *Impact* and *Pressure* (Table A5, column 2, is akin to Table 8, column 3). The key result is the economically large effect of the triple interaction of *Impact*, *Pressure*, and *Homebias* in columns (4) to (6). Investors subject to pressure are much more likely to invest in impact funds that are close to home. The double interaction of *Pressure* and *Homebias* is also consistently positive, though the economic magnitude is relatively small; LPs subject to political pressure prefer local nonimpact investments, but not to the same extent that they prefer local impact funds. The double interaction of *Impact* and *Pressure* is reliably negative in two model specifications, which suggests that LPs subject to political pressure do not have a general preference for impact funds (and might actually spurn impact funds when they are not locally focused).

Table A1: Impact Investment Search Phrases

base of the pyramid	greenhouse	social objectives
bottom of the pyramid	impact investing	social responsible
clean air	impoverished	socially conscious
clean water	indigenous	socially motivated
community invest	invest ethical	socially responsible
disadvantaged	investing ethical	socially-motivated
double bottom line	low carbon	SRI
dual bottom-line	low-carbon	sustainable agriculture
environmental impact	lower-carbon	sustainable development
environmental objective	minority community	sustainable economic development
environmentally clean	minority-owned	sustainable farming
environmentally conscious	missing middle	sustainable forestry
environmentally motivated	mission driven	sustainable investment
environmentally sustainable	mission investing	sustainable property
ethical invest	mission related	sustainable water
ethical objectives	mission-driven	tribe
ethically conscious	mission-related	triple bottom line
ethically motivated	poverty	triple bottom-line
ethically-conscious	S.R.I.	women owned
ethically-motivated	social finance	women-owned
green energy	social good	
green focused	social impact	

Table A2: Countries with GDP Per Capital less than \$1400

Country	GDP per capita	Country	GDP per capita	Country	GDP per capita
Pakistan	1,343	Haiti	833	Guinea-Bissau	589
Kyrgyzstan	1,299	Benin	822	North Korea	583
Chad	1,236	Sierra Leone	808	Ethiopia	575
Burma	1,221	Mali	754	Guinea	573
Bangladesh	1,172	Uganda	726	Liberia	484
Lesotho	1,130	Rwanda	722	Niger	469
South Sudan	1,127	Burkina Faso	717	Madagascar	449
Tajikistan	1,113	Nepal	699	Congo	437
Cambodia	1,081	Togo	658	Gambia	428
Senegal	1,072	Afghanistan	649	Central African Republic	380
Zimbabwe	1,031	Mozambique	630	Burundi	336
Tanzania	1,006	Eritrea	590	Malawi	242
Comoros	923				

Source: IMF World Economic Outlook 2014

Table A3. Distribution of IRR and VM for VC Funds, 2000 to 2012

The table reports the distribution of funds' final (or last reported) internal rate of return (IRR) or value multiple (VM). Excess IRR (or VM) is the fund's IRR less the median IRR (or VM) for cohort funds. Cohorts are defined by vintage year and geography. Panel A presents percentiles of the distribution. Panel B translates percentile rank spreads centered on the median performance measure to a performance spread for each of the performance variable.

Percentile	Excess		Excess		Percentile Rank	Excess		Excess	
	IRR	IRR	VM	VM		IRR	IRR	VM	VM
<i>Panel A: Percentiles of Performance Measures</i>					<i>Panel B: Mapping of Percentile Rank Spread to Performance</i>				
5th	-14.1	-18.8	0.40	-0.81	1	0.3	0.0	0.02	0.00
10th	-7.9	-14.2	0.59	-0.60	2	0.4	0.0	0.03	0.00
15th	-4.9	-10.9	0.71	-0.49	3	0.6	0.2	0.05	0.02
20th	-2.7	-8.6	0.82	-0.40	4	0.8	0.4	0.06	0.02
25th	-0.5	-6.1	0.92	-0.30	5	1.0	0.4	0.07	0.03
30th	1.2	-4.8	1.00	-0.23	6	1.5	0.6	0.07	0.03
35th	3.0	-3.4	1.06	-0.15	7	1.7	0.9	0.09	0.04
40th	4.5	-1.9	1.12	-0.09	8	2.0	1.1	0.09	0.05
45th	5.9	-0.7	1.18	-0.04	9	2.2	1.1	0.11	0.05
50th	7.2	0.0	1.24	0.00	10	2.5	1.3	0.12	0.07
55th	8.4	0.6	1.30	0.03	11	2.6	1.6	0.13	0.07
60th	9.5	1.7	1.38	0.09	12	2.9	1.8	0.14	0.09
65th	10.8	3.1	1.45	0.15	13	3.2	2.0	0.15	0.09
70th	12.4	4.3	1.52	0.22	14	3.5	2.2	0.17	0.11
75th	14.4	6.0	1.61	0.32	15	3.7	2.6	0.18	0.12
80th	16.8	8.0	1.73	0.42	16	3.9	2.8	0.19	0.14
85th	19.9	11.1	1.87	0.56	17	4.2	3.0	0.21	0.14
90th	24.7	15.1	2.10	0.80	18	4.5	3.3	0.22	0.17
95th	35.0	24.0	2.50	1.25	19	4.8	3.5	0.24	0.18
Interquartile	14.9	12.1	0.69	0.62	20	5.0	3.6	0.26	0.18
N	1,036	1,036	1,177	1,176	21	5.4	3.9	0.26	0.20
					22	5.7	4.1	0.28	0.21
					23	6.0	4.4	0.29	0.23
					24	6.2	4.5	0.31	0.23
					25	6.5	4.7	0.31	0.24
					26	6.8	5.1	0.33	0.25
					27	7.0	5.4	0.35	0.26
					28	7.3	5.8	0.35	0.28
					29	7.5	6.1	0.37	0.29
					30	7.8	6.5	0.39	0.30
					31	8.3	6.8	0.40	0.31
					32	8.6	7.1	0.41	0.33
					33	8.8	7.3	0.43	0.34
					34	9.3	7.8	0.46	0.36
					35	9.7	8.0	0.46	0.38
					36	9.9	8.2	0.48	0.40
					37	10.4	8.4	0.49	0.41
					38	10.7	8.6	0.51	0.42
					39	11.0	8.8	0.51	0.44
					40	11.2	9.1	0.52	0.45

Appendix B
Attenuation Bias and Shrinkage Regression

In the main text, we argue the WTP estimates are reasonable if $\text{cov}(\mathbb{E}[r_j], \xi) + \text{cov}(\xi, u) = 0$. In the analysis that follows, we outline the bias that would occur if this summation is nonzero.

The standard slope coefficient from the regression $y = a + b\widehat{\mathbb{E}}[r_j] + e$, where $\widehat{\mathbb{E}}[r_j] = \mathbb{E}[r_j] + u$ yields:

$$\begin{aligned} \text{plim}(\hat{b}) &= \frac{\text{cov}(\mathbb{E}[r_j] + u, a + b\mathbb{E}[r_j] + e)}{\sigma^2(\mathbb{E}[r_j] + u)} \\ &= \frac{b \left(\sigma_{\mathbb{E}[r_j]}^2 + \text{cov}(\mathbb{E}[r_j], u) \right) + \text{cov}(\mathbb{E}[r_j], e) + \text{cov}(e, u)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2\text{cov}(\mathbb{E}[r_j], u)} \\ &= \lambda b + \frac{\text{cov}(\mathbb{E}[r_j], e) + \text{cov}(e, u)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2\text{cov}(\mathbb{E}[r_j], u)} \end{aligned} \quad (\text{A1})$$

Taking the classic errors-in-variable framework where $\text{cov}(\mathbb{E}[r_j], e) = \text{cov}(\xi, e) = \text{cov}(e, u) = 0$, the attenuation bias is measured by λ :

$$\lambda = \frac{\left(\sigma_{\mathbb{E}[r_j]}^2 + \text{cov}(\mathbb{E}[r_j], u) \right)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2\text{cov}(\mathbb{E}[r_j], u)}. \quad (\text{A2})$$

The slope parameter (γ_1) of the shrinkage regression of equation (10) from the main text can be written as:

$$\begin{aligned} \gamma_1 &= \frac{\text{cov}(\widehat{\mathbb{E}}[r_j], r_j)}{\sigma_{\widehat{\mathbb{E}}[r_j]}^2} = \frac{\text{cov}(\mathbb{E}[r_j] + u, \mathbb{E}[r_j] + \xi)}{\sigma^2(\mathbb{E}[r_j] + u)} \\ &= \frac{\sigma_{\mathbb{E}[r_j]}^2 + \text{cov}(\mathbb{E}[r_j], u) + \text{cov}(\mathbb{E}[r_j], \xi) + \text{cov}(u, \xi)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2\text{cov}(\mathbb{E}[r_j], u)}. \end{aligned} \quad (\text{A3})$$

To sign the bias, we can analyze the difference between the attenuation bias (λ) and the slope coefficient from the shrinkage regression (γ_1):

$$\begin{aligned} \gamma_1 - \lambda &= \frac{\sigma_{\mathbb{E}[r_j]}^2 + \text{cov}(\mathbb{E}[r_j], u) + \text{cov}(\mathbb{E}[r_j], \xi) + \text{cov}(u, \xi) - \sigma_{\mathbb{E}[r_j]}^2 - \text{cov}(\mathbb{E}[r_j], u)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2\text{cov}(\mathbb{E}[r_j], u)} \\ &= \frac{\text{cov}(\mathbb{E}[r_j], \xi) + \text{cov}(u, \xi)}{\sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2\text{cov}(\mathbb{E}[r_j], u)}. \end{aligned} \quad (\text{A4})$$

Consider the effect of the bias, ($\gamma_1 - \lambda$), on our estimates of the WTP for impact, which is estimated as the ratio of coefficient on impact divided by coefficient on expected return. When we shrink the expected return, we obtain a larger coefficient on expected return and thus a smaller WTP. As a result,

WTP is increasing in the shrinkage parameter, $\frac{\partial WTP}{\partial \gamma_1} > 0$. This is an appropriate adjustment if the shrinkage parameter is an unbiased estimate of the attenuation bias (λ). It will lead to bias in the WTP estimates if the assumptions in the main text are violated as follows.

1. The bias, $\gamma_1 - \lambda$, is increasing in $cov(\mathbb{E}[r_j], \xi)$. Thus, the bias in WTP is positively related to $cov(\mathbb{E}[r_j], \xi)$.
2. The bias, $\gamma_1 - \lambda$, is increasing in $cov(u, \xi)$. Thus, the bias in WTP is positively related to $cov(u, \xi)$.
3. The absolute magnitude of the bias, $|\gamma_1 - \lambda|$, is decreasing in $cov(\mathbb{E}[r_j], u)$. Note that $cov(\mathbb{E}[r_j], u)$ only appears in the denominator of the bias measure and thus only affects the absolute magnitude of the attenuation bias since the denominator is strictly nonnegative. The denominator is strictly nonnegative because it represents the variance of forecast expected returns, $\sigma_{\mathbb{E}[r_j]}^2 = \sigma_{\mathbb{E}[r_j]}^2 + \sigma_u^2 + 2cov(\mathbb{E}[r_j], u)$.

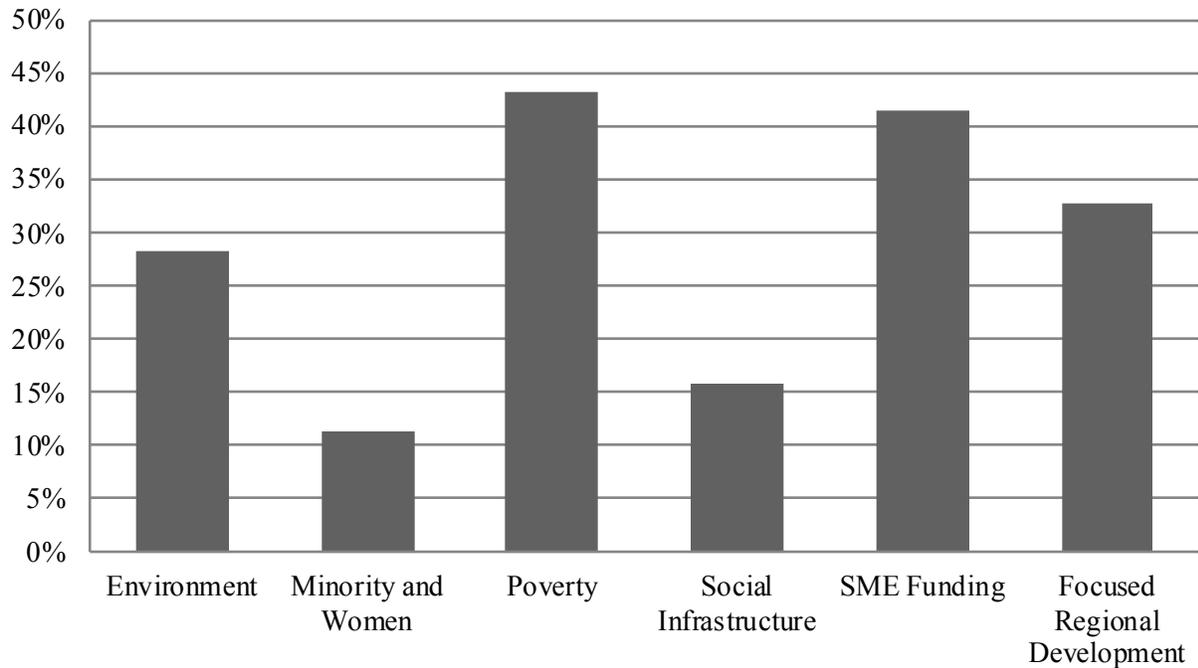


Figure 1. Distribution of Impact Categories that Impact Funds Target

For the sample of 159 impact funds, we identify the impact categories targeted by each impact fund. The figure presents the percentage of sample funds that target each category. Funds can have multiple impact categories. The categories are as follows:

Environment - delivers positive environmental impact (e.g., agriculture, energy, water, and forestry).

Minorities and Women - funds firms run by minorities or women.

Poverty - funds firms in impoverished areas.

Social Infrastructure - develops infrastructure for societal benefit (e.g., microfinance, health care, schools, and housing).

SME Funding - provides capital to SMEs and undercapitalized markets.

Focused Regional Development - imposes a material geographic constraint on investment.

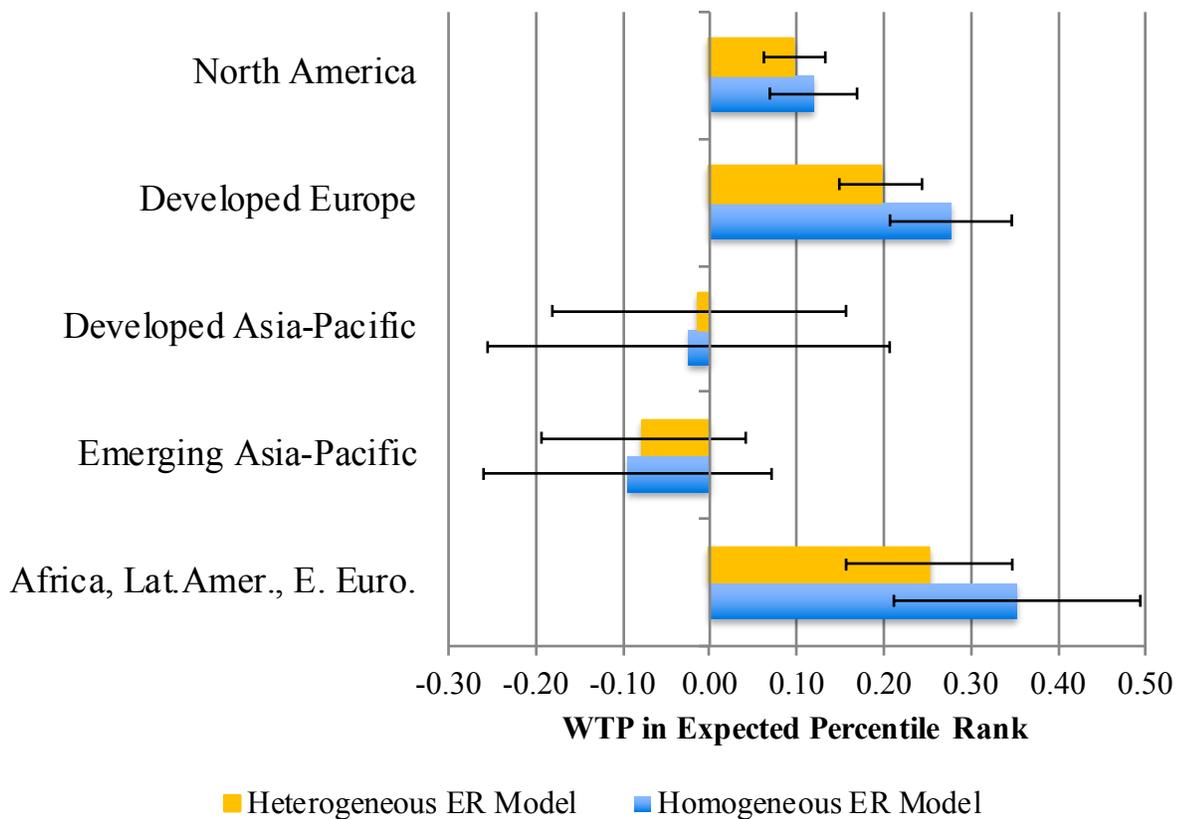


Figure 2. Willingness to Pay (WTP) for Impact by Geography

The figure presents estimates of the willingness to pay for impact based on the logit model including the impact coefficient and the impact coefficient interacted with geography using either homogeneous or heterogeneous expected return models. (Geography is not mutually exclusive.) The WTP is the sum of the impact coefficient plus the impact*geography coefficient, all divided by the expected returns coefficient expressed in percentile ranks. Percentiles are based on performance relative to cohort funds. Cohorts are defined by fund vintage year and region. Black bands represent 95% confidence intervals on WTP estimates.

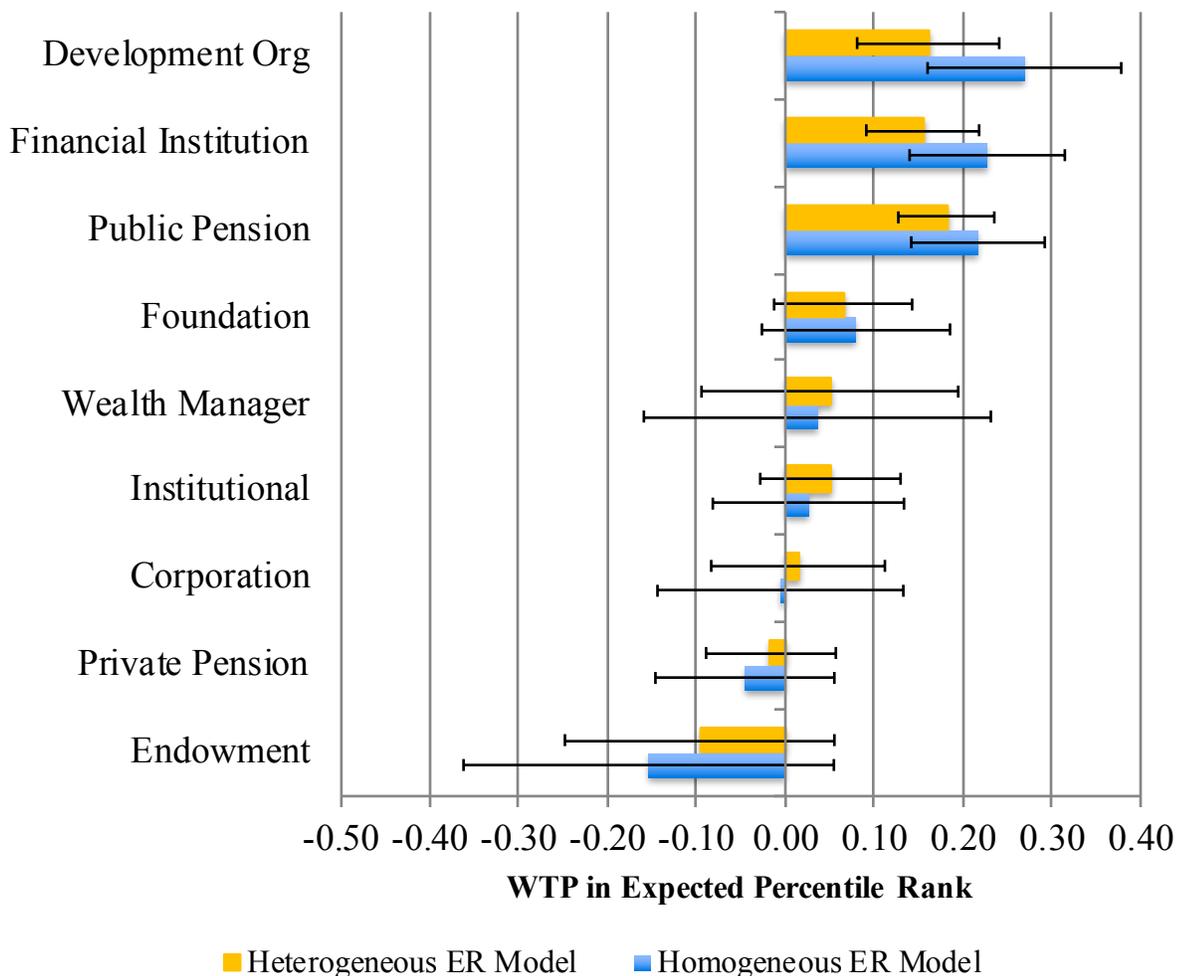


Figure 3. Willingness to Pay (WTP) for Impact by Investor Type

The figure presents estimates of the willingness to pay for impact derived from the logit estimation of Table 6, column 1 (homogeneous expected return model) and column 3 (heterogeneous expected return model). The WTP magnitude is the ratio of the impact coefficient for the LP type divided by the expected returns coefficient expressed in percentile ranks. Percentiles are based on performance relative to cohort funds, where cohorts are defined by fund vintage year and region. Black bands represent 95% confidence intervals on WTP estimates.

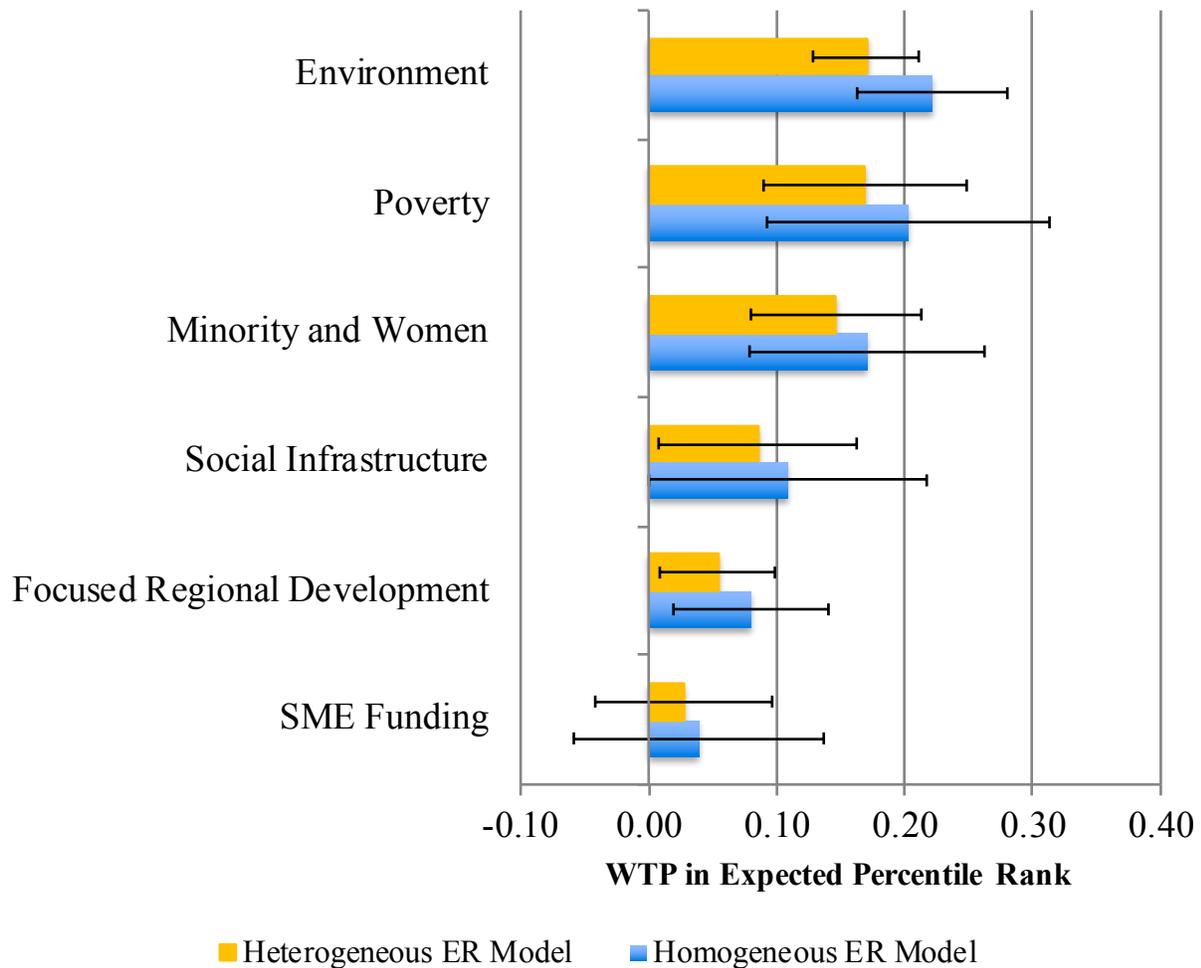


Figure 4. Willingness to Pay (WTP) by Impact Category

The figure presents estimates of the willingness to pay for impact by impact category using either homogeneous or heterogeneous expected return models. Estimates are based on a variation of Table 5, column (1), but include an interaction of impact with the impact type category. The WTP is calculated as the sum of the coefficient on impact and the coefficient on impact*category, all divided by the coefficient on expected returns (expressed in percentile ranks). Percentiles are based on performance relative to cohort funds, defined by fund vintage year and region. Black bands represent 95% confidence intervals on WTP estimates.

Table 1. Fund Descriptive Statistics, 1995 to 2014

This table presents fund summary statistics for traditional funds (left columns) and impact funds (right columns). Capital Commitment is the average capital commitment across investors within a fund. IRR is the final or last observed internal rate of return for the fund. VM is the fund's value multiple. Imputed PME (Public Market Equivalent) is the fund's PME imputed using regression coefficients in Table IA.IV in Harris et al. (2014) and the fund's available IRR and VM. Percentile Rank is the fund's percentile rank relative to similar cohort funds (year, region, and fund type). In Panel B, we present the geography focus of fund investments. In Panel C, we present the industry focus of fund investments. Funds can have multiple geography and industry focuses.

	Traditional VC Funds				Impact Funds			
	N	Mean	Median	Std. Dev.	N	Mean	Median	Std. Dev.
<i>Panel A: Descriptive Statistics</i>								
Vintage Year	4500	2005.4	2006.0	5.26	159	2006.7	2008.0	4.44
Fund Size (\$mil)	4000	204.6	102.0	300.2	147	129.6	83.00	147.3
Capital Commitment (\$mil)	2717	22.21	14.60	33.85	125	27.09	15.00	32.88
IRR (%)	1207	11.59	7.40	32.06	76	3.70	6.35	15.17
VM - Value Multiple	1484	1.51	1.22	1.94	91	1.17	1.10	0.56
Imputed PME	1147	1.29	1.09	1.29	65	1.00	0.97	0.42
Percentile Rank	1530	0.49	0.50	0.30	94	0.34	0.28	0.30
Fund Sequence Number	4500	3.95	2.00	5.63	159	3.88	2.00	5.91
<i>Panel B: Geography Focus of Fund Investments</i>								
North America	4500	0.50			159	0.33		
Developed Europe	4500	0.23			159	0.18		
Emerging Europe	4500	0.06			159	0.09		
Africa	4500	0.02			159	0.23		
Central and South America	4500	0.03			159	0.12		
Developed Asia-Pacific	4500	0.07			159	0.01		
Emerging Asia-Pacific	4500	0.17			159	0.14		
Middle East	4500	0.03			159	0.00		
All Regions	4500	1.10			159	1.09		
<i>Panel C: Industry Focus of Fund Investments</i>								
Business Services	4500	0.03			159	0.03		
Energy	4500	0.06			159	0.19		
Consumer Discretionary	4500	0.05			159	0.03		
Diversified	4500	0.27			159	0.48		
Industrials	4500	0.04			159	0.06		
Information Technology	4500	0.45			159	0.06		
Health Care	4500	0.22			159	0.06		
Infrastructure	4500	0.01			159	0.05		
Food and Agriculture	4500	0.01			159	0.04		
Materials	4500	0.01			159	0.04		
Real Estate	4500	0.00			159	0.04		
Media and Communications	4500	0.12			159	0.03		
All Industries	4500	1.27			159	1.12		

Table 2. Limited Partner (LP) Descriptive Statistics

For each of the LP types and all LPs, we present descriptive statistics by first averaging all observations for a unique LP and then calculating the mean (standard deviation) for each variable across N LPs. Funds per LP are the total number of unique fund investments by an LP. Vintage Year is the average vintage year of fund investments. Years of Experience is the number of years since the LPs' first fund commitment (measured at the time of each investment and averaged across all investments for a given LP). The % Prior Relationship is the percent of capital commitments where the LP and fund's general partner (GP) had a prior investment relationship. The % Home Bias is the percent of capital commitments by the LP type where the region of the LP and fund are the same (using the eight major global regions of Panel B). In Panel B, we present the regional distribution of LPs by LP type. For development organizations, we manually coded geographic foci of their missions and used them instead of the actual headquarters location. For example, Inter-American Development Bank is headquartered in the U.S., but its mission is focused on South and Central America. Standard deviations are in parentheses.

	Dev. Org.	Found- ation	Financial Institutions	Endow- ment	Corp. & Gov't	Institu- tional	Wealth Manager	Private Pension	Public Pension	Total
<i>Panel A: LP Descriptive Statistics</i>										
# of LPs	258	453	572	196	404	591	174	440	372	3,460
% of Total	7.5	13.1	16.5	5.7	11.7	17.1	5.0	12.7	10.8	100.0
# of Capital Commitments	2,147	2,770	2,473	1,287	1,513	3,541	635	3,893	5,727	23,986
% of Total	9.0	11.5	10.3	5.4	6.3	14.8	2.6	16.2	23.9	100.0
Funds per LP	8.32 (16.70)	6.11 (13.61)	4.32 (8.85)	6.57 (15.72)	3.75 (16.58)	5.99 (14.82)	3.65 (6.54)	8.85 (19.80)	15.40 (30.43)	6.93 (17.43)
Vintage Year	2007.2 (3.79)	2005.8 (3.66)	2005.7 (4.33)	2004.8 (4.15)	2006.6 (5.09)	2005.7 (4.48)	2005.9 (4.36)	2004.7 (4.09)	2005.5 (3.67)	2005.7 (4.28)
Years of Experience	4.39 (4.47)	4.13 (4.69)	3.77 (4.38)	4.64 (5.39)	2.70 (3.46)	3.54 (4.30)	3.67 (4.58)	5.08 (5.23)	7.76 (7.52)	4.34 (5.11)
% UNPRI Signatories	5.4	2.2	11.0	1.5	1.0	17.9	14.4	8.4	13.4	9.0
% Prior Relationship	23.7	41.7	22.7	38.8	23.3	25.0	24.6	38.3	41.1	33.4
% Home Bias	59.4	78.2	82.4	82.0	72.1	61.5	68.5	78.3	84.5	75.8
<i>Panel B: Regional Distribution of LPs by LP Type (%)</i>										
North America	19	83	34	82	21	32	34	72	62	48
Developed Europe	28	15	36	16	28	40	39	20	29	29
Emerging Europe	5	0	2	0	2	1	2	1	0	1
Africa	5	0	3	1	1	2	1	1	2	2
Central and South America	6	0	1	1	2	1	0	3	2	2
Developed Asia-Pacific	8	1	10	0	20	9	20	2	3	8
Emerging Asia-Pacific	25	0	10	1	24	11	4	0	1	9
Middle East	4	1	4	0	3	5	2	1	1	3

Table 3. The Performance of Impact Funds, Vintage Year 1995-2012

Fund performance (Panel A, IRR; Panel B, VM; Panel C, percentile rank) is regressed on a dummy variable for impact funds and controls. Controls include vintage year, log of fund size, log of fund sequence number, fund geography, and fund industry. Models (1) to (3) step in controls without interactions using 5 geographies and 12 industries. Model (4) creates fund group dummy variables based on 6 three-year vintage groups (1995-97 through 2010-12) and 5 fund geographies in place of vintage year and geography FEs of Model (3). Model (5) creates fund group dummy variables based on 6 three-year vintage groups and 12 fund industries in place of vintage year and industry FEs of Model (3). Model (6) creates fund group dummy variables based on 6 three-year vintage groups, 5 fund industries, and North America/Europe v. other funds. The 5 fund industries include (1) Information Technology and Business Services, (2) Diversified and Consumer Discretionary, (3) Health Care, (4) Media and Communications (5) Others (Energy, Industrials, Infrastructure, Food and Ag., Materials, Real Estate). Models that include fund size in the regression lose observations of traditional VC funds with missing fund size. Robust standard errors (in brackets) are calculated by clustering on vintage years and fund geography. *** p<0.01, ** p<0.05, * p<0.1

	(1)	(2)	(3)	(4)	(5)	(6)
<i>Panel A: IRR</i>						
Impact	-7.890*** [2.548]	-9.937*** [2.386]	-4.701** [2.282]	-4.898** [2.440]	-4.652* [2.555]	-5.359** [2.520]
Observations	1,283	1,252	1,252	1,252	1,252	1,252
R-squared	0.004	0.146	0.166	0.288	0.19	0.274
<i>Panel B: Value Multiple</i>						
Impact	-0.403*** [0.124]	-0.465*** [0.107]	-0.361*** [0.137]	-0.265* [0.141]	-0.228* [0.122]	-0.194* [0.103]
Observations	1,456	1,417	1,417	1,417	1,417	1,417
R-squared	0.002	0.117	0.125	0.184	0.122	0.204
<i>Panel C: Percentile Rank</i>						
Impact	-0.149*** [0.037]	-0.158*** [0.037]	-0.089** [0.040]	-0.093** [0.045]	-0.083** [0.040]	-0.078* [0.040]
<i>Controls for all Panels in Column</i>						
Vintage Year FE	NO	YES	YES	NO	NO	NO
Log(Fund Size)	NO	YES	YES	YES	YES	YES
Log(Fund Sequence)	NO	YES	YES	YES	YES	YES
Fund Geography FE	NO	NO	YES	NO	YES	NO
Fund Industry FE	NO	NO	YES	YES	NO	NO
Vintage Group*Geography	NO	NO	NO	YES	NO	NO
Vintage Group*Industry	NO	NO	NO	NO	YES	NO
Vintage Grp.*Industry*Geograp	NO	NO	NO	NO	NO	YES
Observations	1,505	1,465	1,465	1,465	1,465	1,465
R-squared	0.014	0.027	0.068	0.17	0.121	0.164

Table 4. Summary of Expected Return Regression Models

In each of 20 forecast years, 1995 to 2014, we estimate a regression of realized fund performance (using percentile ranks) on fund attributes as described in the main text. For example, in the 1995 forecast year we estimate relations between fund attributes and performance using data on 1983-1990 vintage-year funds since the performance and attributes of these funds would be observed by an investor looking to invest in 1995. Panel A summarizes the distribution of the 20 coefficient estimates and associated t-statistics across the 20 regressions; Panel B summarizes number of observations and R-squareds across regressions. The interaction terms are only estimated for the last 12 of the 20 year rolling window regressions because there are a small number of impact funds in the early part of the sample.

	Mean [t-stat.]	% of t-stats > 1.96	% of Coef. > 0	25th Percentile [t-stat]	Median [t-stat.]	75th Percentile [t-stat]
<i>Panel A: Coefficients</i>						
R_j^{prior}	0.217 [3.12]	85.0%	100.0%	0.167 [2.93]	0.222 [3.23]	0.280 [3.95]
$Miss_j^{prior}$	-0.052 [-0.94]	15.0%	20.0%	-0.079 [-1.49]	-0.051 [-1.00]	-0.014 [-0.42]
$First_j^{prior}$	-0.076 [-1.97]	45.0%	10.0%	-0.146 [-3.63]	-0.054 [-1.67]	-0.019 [-0.64]
$Impact_j$	-0.203 [-1.15]	0.0%	0.0%	-0.292 [-1.35]	-0.186 [-1.08]	-0.139 [-0.88]
$Impact_j * Miss_j^{prior}$	-0.033 [-0.38]	0.0%	33.3%	-0.160 [-0.92]	-0.069 [-0.31]	0.067 [0.24]
$Impact_j * First_j^{prior}$	0.068 [0.31]	0.0%	75.0%	0.004 [0.04]	0.062 [0.31]	0.147 [0.79]
<i>Panel B: Regression Statistics</i>						
Observations	459.4	n.a	n.a	240.0	446.0	649.0
R-squared	6.50%	n.a.	n.a.	3.00%	4.50%	10.20%

Table 5. The Willingness-to-Pay for Impact

The dependent variable is a dummy variable that equals one if an LP invests in a fund. Observations are determined by crossing all vintage year funds with LPs that make an investment in that year. All columns except column (2) are a logit model with LP investment group controls. LPs are dynamically placed in one of 368 groups according to how many prior three-year investments they make in VC by LP Type. Column (2) is a conditional logit model (LP fixed effects). Columns (3) and (4) drop ex ante top-quartile VC fund and Top15 VCs, respectively, investment opportunities for LPs that have no prior relation with the VC fund families. Column (5) creates an opportunity set assuming that a GP was fundraising in year t (and thus included in the fund opportunity set for LPs investing in year t) if it closed a fund in year t+1 and its predecessor fund was raised in t-5 or older. Column (5) creates an opportunity set assuming that an LP considers investments in year t but does not realize investments until t+1. Impact equals one for impact funds. Expected Returns are expressed as percentile ranks relative to vintage year cohort funds and are modeled based on known fund characteristics at the time of investment and adjusted for shrinkage. In Panel A, a fund's expected return forecast is homogenous across all investors. Panel B allows heterogeneous forecast for each fund by LP type. The WTP estimate is the ratio of the Impact coefficient divided by the Expected Return coefficient. Standard controls included in all columns are: LP experience (log of years since first fund investment plus one), LP-GP relationship (we analyze five regions rather than eight by combining Emerging Europe, Africa, and Central and South America into "Rest of the World", and Emerging Asia-Pacific and Middle East into "Emerging Asia-Pacific"; however, to establish an LP-fund geography match we continue to employ the eight-region code first and then combine the eight home-bias dummies into five), fund-LP geography match (five dummy variables for five regions that equal one if the fund and LP are in the same region), expected fund size, and fixed effects for fund geography (five regions), industry (12 industries), and vintage year. Standard errors in brackets are clustered at the LP level, except for the conditional logit. *** p<0.01, ** p<0.05, * p<0.1.

	(1)	(2)	(3)	(4)	(5)	(6)
<i>Panel A: Homogeneous Expected Returns Forecast</i>						
Expected Returns	3.354*** [0.276]	3.426*** [0.210]	3.248*** [0.363]	2.833*** [0.354]	3.146*** [0.270]	3.307*** [0.275]
Impact	0.591*** [0.0599]	0.585*** [0.0443]	0.599*** [0.0645]	0.567*** [0.0643]	0.590*** [0.0599]	0.580*** [0.0595]
WTP Estimate	0.176	0.171	0.184	0.200	0.188	0.175
Pseudo R-Squared	0.261	0.237	0.264	0.269	0.258	0.263
Observations	3,047,430	3,047,430	2,780,390	2,944,643	3,301,101	3,873,720
<i>Panel B: Heterogeneous Expected Returns Forecast</i>						
Expected Returns	4.655*** [0.225]	4.725*** [0.140]	5.072*** [0.253]	5.022*** [0.262]	4.622*** [0.227]	4.655*** [0.225]
Impact	0.613*** [0.0577]	0.602*** [0.0422]	0.650*** [0.0589]	0.645*** [0.0588]	0.618*** [0.0579]	0.613*** [0.0577]
WTP Estimate	0.132	0.127	0.128	0.128	0.134	0.132
Pseudo R-Squared	0.263	0.240	0.267	0.272	0.259	0.263
Observations	3,047,430	3,047,430	2,780,390	2,704,939	3,159,087	3,047,430
Model:						
Logit with Dynamic LP Invest. Groups	Yes	--	Yes	Yes	Yes	Yes
Conditional Logit Model	--	Yes	--	--	--	--
# F.E. (LP or Dynamic LP Groups)	368	3,460	368	368	368	368
Sample Restrictions:						
Drop Top Quartile unless Prior Relation	--	--	Yes	--	--	--
Drop Top15 VCs unless Prior Relation	--	--	--	Yes	--	--
Expanded Fundraising Years	--	--	--	--	Yes	--
Expanded LP Investor Set	--	--	--	--	--	Yes

Table 6. Willingness-to-Pay for Impact by Investor Type

Presented are coefficients and willingness-to-pay estimates from investment choice logit models. The columns vary in their estimation or use of the expected return forecast. Column (1) implements a homogenous model to forecast expected returns, where we estimate a single estimate of the forecast expected returns by fund using all funds in the dataset. Columns (2) and (3) use LP-type specific expected return forecasts, but forecasting with a smaller set of information in numbers of fund which are invested by the investor type. Column (3) uses the same forecast as column (2) and also interacts these forecasts with fund characteristics (industry, geography and size). Column (4) drops the expected return forecast variable altogether. Note that WTP is reported only for columns (1)-(3). Standard errors clustered at the LP level are in brackets. *** p<0.01, ** p<0.05, * p<0.1.

<i>Expected returns forecast:</i>	(1) Homogenous ER Forecast		(2) Heterogenous ER Forecast by LP Type		(3) Heterogenous ER Forecast by LP Type		(4) No Forecast
	Estimates	WTP	Estimates	WTP	Estimates	WTP	Estimates
Expected Return	3.364*** [0.275]		4.591*** [0.223]		5.568*** [1.584]	Note: Not comparable to columns (1) and (2).	
Impact Estimates by LP Type:							
Development Org.	0.906*** [0.180]	0.27***	0.738*** [0.183]	0.16***	0.980*** [0.155]	0.14***	0.595*** [0.180]
Foundation	0.267 [0.179]	--	0.299* [0.179]	0.06*	0.469*** [0.178]	0.07***	0.00261 [0.178]
Financial Institution	0.765*** [0.144]	0.23***	0.710*** [0.144]	0.15***	0.852*** [0.122]	0.13***	0.483*** [0.141]
Endowment	-0.518 [0.346]	--	-0.443 [0.346]	--	-0.300 [0.360]	--	-0.802** [0.343]
Corporation	-0.0188 [0.233]	--	0.0655 [0.224]	--	0.238 [0.194]	--	-0.316 [0.232]
Institutional	0.0872 [0.182]	--	0.233 [0.182]	--	0.501*** [0.157]	0.08***	-0.187 [0.181]
Wealth Manager	0.121 [0.329]	--	0.23 [0.332]	--	0.449 [0.335]	--	-0.142 [0.325]
Private Pension	-0.153 [0.168]	--	-0.0746 [0.168]	--	0.0834 [0.174]	--	-0.440*** [0.165]
Public Pension	0.730*** [0.121]	0.22***	0.832*** [0.119]	0.18***	1.028*** [0.107]	0.16***	0.430*** [0.121]
Region*Impact F.E.	YES		YES		YES		YES
ER interacts with portfolio choice	NO		NO		YES		NO
Standard Controls	YES		YES		YES		YES
Pseudo R-squared	0.261		0.264		0.276		0.260
Observations	3,047,430		3,047,430		3,047,430		3,047,430

Table 7. Limited Partner (LP) Types and Attributes related to Impact Motives

The table summarizes investor attributes by LP Type (column (1)) and region. Column (2) indicates whether the primary constituents of the capital are households (v. organization). Column (3) indicates whether the constituent capital is intermediated as opposed to directly invested by the constituent or an administrator (e.g., foundations and pensions). Column (4) indicates whether impact is a primary goal of the constituent. Column (5) identifies legal and political pressure to invest with impact. The last two columns identify laws (e.g., ERISA) and charters (e.g., corporate charters) that restrict impact investment.

Limited Partner	Household	Intermediated	Mission	Pressure toward Impact	Laws Restricting Impact	Charters Restricting Impact
Development Organizations	--	--	yes	--	--	--
Foundations	--	--	yes	--	yes UPMIFA and PRI (U.S.)	--
Financial Institutions	--	--	--	yes Community Reinvestment Act & State regulation modeled after CRA (U.S.)	--	yes
Endowments	--	--	--	--	yes UPMIFA (U.S.)	--
Corporate & Government Portfolios	--	--	--	--	--	yes
Institutional Asset Managers	--	yes	--	--	--	yes
Wealth Managers	yes	yes	--	--	--	--
Private Pensions	yes	--	--	--	yes ERISA (U.S.)	yes (non-US)
Public Pensions	yes	--	--	yes Political pressure	yes State & National Laws	--

