Aspects considered by investors when evaluating the impact of startup companies

A cross-sectional study of the criteria investors consider when evaluating the impact and sustainability status of target companies in the screening process

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Abstract

Background

To attain the objectives set for the sustainable development goals within the Agenda 2030 the SFDR regulations were created as part of the EU taxonomy. The new incentives have caused many investors to cope with the new regulations which have pushed startups to not only achieve profitability, but also achieve it in a way that considers different ESG factors. The recent evolvement of sustainability in the screening process has led to a need for an understanding of what factors investors consider when evaluating the impact of target start-up companies.

Purpose

The purpose of this research is to investigate and create an understanding of the different factors and aspects that different types of investors consider when evaluating a target companies level of sustainability and impact. This would potentially benefit investors wanting to improve the incorporation of ESG factors in the screening process, but also the companies intending to achieve sustainability status among investors.

Method

To answer the research question and its sub-questions a cross-sectional research method was chosen to analyse the results of the 18 interviewees which were conducted using a generic purposive sampling technique. The data were analysed thematically, and the themes were compared with the relevant theoretical concepts obtained from a literature review.

Conclusion

The research shows that the area of impact evaluation from an investor perspective is a relatively unexplored area where a lot of development will occur in the coming years as the evaluation understanding matures. The aim of this research was to make the area of sustainability evaluation clearer, both from a startup perspective that intends to raise capital, but also to extend the knowledge of how investors are working practically with ESG questions, especially in the screening process.

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Key Terms and Abbreviations

ESG: Environmental, Social and Governance.
SFDR: Sustainable Finance Disclosure Regulation
GHG: Greenhouse Gas Emissions
WACC: weighted average cost of capital
DCF: Discounted Cashflow

1. Introduction

The initial section of the research will provide an overview of the theoretical frameworks for the research objective, which aims to explore what factors investors consider when evaluating the impact of a target company at the startup level. To contextualize the background and introduce the study's objectives and research questions, a problematization section will be included.

Companies intervene with sustainability in multiple dimensions, such as environmental, social, and financial ones. 1987 the United Nations Brundtland Commission defined sustainability as “meeting the needs of the present without compromising the ability of future generations to meet their own needs” (Brundtland et al., 1987). However, the commission acknowledged that achieving this goal is challenging since economic and social development often conflicts with environmental objectives. Griffin (2017) discovered that 100 of the largest companies in the world are accountable for 71% of the worldwide green-house gas emissions. Sustainability, however, does not only include environmental dimensions, but also social and governance aspects that need to be addressed. Raworth (2017) acknowledges this and argues that the perpetual pursuit of growth in businesses and the economy should not only consider the depletion of natural resources, but also the exacerbation of social and financial inequality and injustice. Companies must take a role in a much needed comprehensive and large-scale transformation towards sustainability.

Incorporating sustainability into the fundamental structure of a company already from its start can facilitate the transition towards a more sustainable society. Since some of today's early-stage startups will become tomorrow’s largest corporations, incorporating sustainability into their early stages of development will contribute on a massive scale to the sustainability of the society and world we´re living in. Thus, to improve the level of sustainability among companies and the overall society, sustainability should be a primary focus already from the very birth of a company.
The need for change has resulted in a push from regulators, putting pressure on investors by incentivizing them to invest in companies that can solve the challenges the world is facing (The Economist, 2017; Geczy et al., 2015). The idea of impact investment is that the focus not only

is on and not only the financial return on investment, but also on enabling a positive environmental and social impact with the investment.
This global movement has incentivized startups at all stages on a to adapt to the new focus of the investors, which intends to not only achieve profits for its shareholders, but also to create a positive impact on the society on environmental, social and governance aspects. As sustainability investment still is a relatively new phenomenon, there is no specific consensus of exactly what factors the different investors look at when evaluating ESG aspects of a target startup company. Without the clarity of what investors evaluate, the accuracy of the startups that focus on intending to achieve the sustainability status in the eyes of the investors might get affected. This results in startups focusing on the wrong aspects.
This chapter will introduce the study by first discussing the context of the research, followed by a presentation of the research questions, the research strategy, research design and overall thesis structure.

1.1 Background

The world is currently confronted with considerable ecological, social, governance, and economic difficulties, and the time limit for the Sustainable Development Goals (SDGs) set forth in the Agenda 2030 is approaching at an alarming pace. To attain these objectives and advance sustainable companies, great investments in sustainable enterprises that contribute to positive change are required (Bocken, 2015). Venture capital (VC) investments play a crucial role in enabling startups to evolve into established firms capable of making a substantial positive impact (UN PRI, 2022).
In order for startups to stay relevant and attract investment capital they therefore need to consider not only metrics such as profitability or turnover but also aspects that investors prioritize when evaluating whether a company is “good enough” to be passed on in the screening process.
The assessment of startups in the screening process of traditional investors who only consider the financial return on investment has been studied for many decades (Poindexter, 1976). The criteria considered by investors evaluating social aspects do have a lot in common with regular investors, but there is also some aspect that differs between the two (Miller & Wesley, 2010). Except for the traditional goals of regular venture capital firms, such as financial viability, scalability, and the background of the founders, they also consider social goals. The selection process and its criteria are therefore different for investors with social goals. As social

objectives, or ESG goals is a wide and complex area, different investors focus on different aspects. Assessments of environmental, social, and governance factors remain subjective to a certain extent. The year of 2018, over 600 ESG ratings were used by investors, each one slightly or drastically different from the other one (Fish et al., 2019). As the selection criteria for investors considering social goals as well as financial goals make an already complex area even more sophisticated, Lee et al. (2020) prove that investors considering social aspects have challenges in the screening process. Consequently, Lee et al. (2020) suggest that the area is in need for more empirical research within to support and improve the selection process of investors considering social aspects in the investment process.

1.2 Problematization

VCs are often considered and required to be skilful in identifying potential prospects that could yield promising financial returns while also contributing to societal benefits. Many researchers have therefore opted to analyse the decision-making process for investors with the aim of investigating the different factors considered among investors in the investment process. The topic of aspects considered among investors within the social investment area is, however, as mentioned by Gompers et al. (2021) and Lin (2022). relatively new and unresearched so far as it until recently have not been more than an investment area in the periphery (Pitchbook. 2022).

1.3 Purpose of research

The purpose of this research is to investigate and create an understanding of the different factors and aspects that different types of investors consider when evaluating a target companies level of sustainability and impact. This would potentially benefit investors wanting to improve the incorporation of ESG factors in the screening process, but also the companies intending to achieve the sustainability status among investors.

1.4 Research questions

The research questions will act as a catalyst to set a focus of and the scope of the study to uncover crucial aspects within the identified gap of the topic. To reach the goal of the study, the following questions are formulated:

RQ: What factors are investors evaluating when considering the impact of target start-up companies?

Sub-questions 1: How does the 'Sustainability label" affect the valuation of a startup?

Sub-questions 2: How do these factors affect the decision of investors when evaluating potential investment cases?

1.5 Delimitations

The definition of "investors" stretches throughout an extensive array of different types of investors, at different locations around the globe. As such, due to limited time and resources it would not be possible to investigate all markets and all types of investors. For this reason, a few chosen investors within the Nordic countries, and mostly Swedish market has been interviewed. The logic behind this choice is that the Nordic countries investors have come relatively far regarding sustainability incorporated within the investments industry (Sustainable development report, 2020), but also as the researchers are based in Sweden the availability of interviewees within the same region was better than other continents.

Further the authors have chosen to only interview one person per investment company, where all of them had a position that´s involved in the screening process and investment decision making process. This choice was an important one as it´s necessary that the interviewee has full insight in the factors that are considered in the screening process to be able to provide useful insights for the research questions. Further the study will not investigate the impact on valuation in relation to the sustainability level of the target company, even though this was initially planned. This eventually became a delimitation as there would be a risk that the research would lack depth within that area as it would intend to answer questions in multiple different areas.

The analysis and conclusion will mainly focus on the most frequently mentioned and highest prioritized aspects mentioned by the investors.

1.6 Disposition of the paper

This paper is structured into six main chapters. The first chapter introduces the thesis and its background and context to motivate the research and contain the research questions and the and its scope. The literature review starts in the second chapter where relevant literature, theories and frameworks linked to the research topic are summarized and brought. It will

function as the foundation of the research and contains literature related to the screening process of investors, start-ups, but also has a focus on how sustainability plays a key role in the screening process of many investors. The third chapter describes the chosen methodology as well as research strategy and design, how the data was analysed as well as aspects that´s relevant for the research quality.

The fourth chapter presents the primary data gathered through interviews and highlights the main themes and significant aspects of the findings. The empirical results are analysed, interpreted, and compared to the existing literature in the field in chapter five. Chapter six answers the research question and summarizes the most significant contributions of this research, highlighting its relevance to the existing literature.

2. Literature review

The literature review chapter will examine previous research and literature within the impact investments field to summarize and provide an understanding of the research that has already been done on the subject. The section will also go through what´s missing, where consensus has not yet been reached among researchers, and where the gap will be filled in with data presented from interviews performed within this research.

The chapter start with presenting literature stating that investors consider ESG factors in the screening process, but also why and how they do so. This is followed by a section about different methods and metrics that can be used from the startups perspective to support statements about its impact and ESG focus.

2.1 Start-ups

To gain an understanding of sustainability within the business arena, and more specifically startups, it is important to have an understanding of startup businesses in general. As the startup businesses are in focus of the study the startup phenomenon and the startup process will therefore be defined in the coming section.

In the early stages of a startup, securing investment from investors is often crucial for the success of the venture. To gain investors, trust, startups must deliver an effective pitch. The pitch generally lasts between five to twenty minutes and consists of approximately seven to sixteen slides. The limited time and number of slides make it essential to present information

efficiently. The startup pitch serves as the initial point of contact between the investor and the startup where the investor determines whether to explore the business further or to decline it. Thus, it is a critical event in the startup journey, and often the first opportunity for investors to learn about the startup. The pitch ultimately determines whether the investor proceeds with additional investigation of the business to potentially receive funding. However, only a small percentage of startups seeking funding are successful in doing so. Usually, a pitch includes elements such as the future vision of the company, its value proposition, defining the problem it intends to solve, the solution, target market, specific numbers of the opportunity and competitors. These elements are usually complemented with a financial forecast and budget as well as financial statements. As the startup is heavily dependent on the founding team, they will also present themselves and their background (Cremades 2016).

Investors seek as high a degree of financial safety as possible, while also keeping the potential upside high when making early-stage investments. Startup investments are associated with potentially great return on investment, but also with high risk of failures, and thereby risking erasing the whole investment. Hence, startups face significant odds against them progressing to the next phases within the investment process, and thereby receiving funding.

The pitch is not only significant for entrepreneurs, but also for investors, as it lays the fundamentals to their decision-making process of what investment opportunity to proceed with (Maxwell et al., 2011). Beyond financial feasibility, some investors consider not only financial potential of the investment, but also social aspects of the startup's business model. Sustainability and other social aspects is becoming increasingly considered among investors as regulators and investors themselves set up incentives for investments of such types (Pitchbook. 2022).

2.2 Defining different types of investing

The terminology used to describe sustainable investments is diverse, and there is no universally accepted definition or terminology for investments that aim to generate financial returns while having a net positive impact on the environment and society. This has led to a many different terms that often are used interchangeably, as they rarely overlap with each other. Some of the common investment approaches that consider sustainability factors include Socially Responsible Investing, Impact Investing, Ethical Investing, Thematic Investing, SDG Investing and ESG Investing (Hill, 2020). In this study, an attempt to clarify the key definitions of the most prominent sustainable investing styles is being made. After doing so, a more thorough

description of ESG investing will be made as it is one of the wider terms, covering most aspects of the sustainability investing spectrum.
Socially Responsible Investing involves investing in companies that meet specific social and environmental standards or avoiding companies that do not meet such criteria. Impact Investing aims to generate positive social and environmental impact alongside financial returns by investing in companies that are committed to addressing specific social or environmental issues. Ethical Investing refers to investing in companies that align with the investor's values and beliefs, such as avoiding investments in tobacco or weapons. Thematic Investing is focused on investing in companies that are aligned with a particular theme, such as renewable energy or water conservation. SDG Investing seeks to invest in companies that are contributing to achieving the Sustainable Development Goals set by the United Nations.

2.2.1 Traditional investing

Traditionally, investors have prioritized financial returns over sustainability considerations in their investment decisions (McLachlan & Gardner, 2004). However, this approach is becoming increasingly outdated. Despite this, there are still investors who do not factor in sustainability considerations in the screening process.

2.2.2 ESG Investing

Environmental, social, and governance (ESG) investing, is a type of investing where ESG aspects are considered along with traditional investment criteria. To understand what aspects startups should focus on to achieve the sustainability stamp from the investors, it´s crucial to understand what ESG investing means. ESG investing directly relates to the perspective of the investors. The ESG investing phenomenon also shows how sustainability aspects can be accounted for in the screening process.
When deciding what type of investor to target when raising capital, and thereby adapting the company's general approach and business model, it would be beneficial to know how large part of the investors that are considering ESG factors in the screening process.
ESG investing in on a rapid growth trend, making it hard to ignore by companies seeking capital from investors. Over the last 10 years, a shift has taken place towards increased attention

to sustainability in the screening process made by investors. On a global scale, asset managers are expected to increase their ESG-related assets under management to US$33.9tn by 2026, from the levels of 2021 at US$18.4tn. With a projected compound annual growth rate (CAGR) of 12.9%, ESG assets are on pace to constitute 21.5% of total global assets under management in less than 5 years, with 8 of 10 investors planning to increase their allocation to ESG products within the two coming years (PWC, 2022). The same questions were researched Pitchbook (2022). After interviewing 522 Investors on a global scale, Pitchbook (2022) concluded that 81% of the investors are considering ESG factors in the screening process and 90% are planning to increase the attention on ESG factors in the coming year, or "are already fully implemented on a ESG factor program".

The major issues that ESG investing is taking into consideration when measuring impact on the society as a whole are environmental, social, and governance factors. These aspects are in particular relevant for investors that are focusing on socially responsible investments. Socially responsible investors take their values into consideration in the screening process instead of purely focusing on financial return on investment. ESG investing or socially responsible investing may also be referred to mission-related investing, impact investing, or sustainable investing in another research (Syed, 2017).

2.2.3 Environmental aspects for ESG investing

The environmental criteria within ESG investing include criteria that consider environmental sustainability in different contexts. Pollution, emissions, energy as well as waste-related aspects are all examples of criteria that are included within the environmental criteria. The pollution and emission-related aspects are mainly focused on use of fossil fuels, resulting in primarily CO2 gas emissions. The energy aspect is related to the target companies use of renewable energy sources, while the material criteria apply to the raw material that´s being used, but also weather it´s being recycled or not. The environmental considerations correspond to concerns about air and water pollution as a consequence of the company's activities. Theirs also aspects in addition to these, there are other environmental factors to consider, including deforestation, biodiversity, and other potential issues caused from the company's operations. The company's stance and actions towards climate change are also considered as part of the evaluation (Syed, 2017).

2.2.4 Social aspects for ESG investing

The social criteria of ESG investing examine the internal and external activities of a company and cover a wide range of aspects relating to workers' rights, ethics at the workplace, and the company's mission statement. The criteria aim to evaluate whether the business is adhering to fair compensation practices. (Syed, 2017).

Fair salary practices are a significant focus area of the social criteria of ESG investing. The criteria examine whether the compensation that employees receive is associated with industry standards and whether there are any additional benefits outside of the original salary, such as retirement plans or employer contributions. The social criteria also evaluate development programs offered by the business, as well as working hours and how long the employee stay at the company (Syed, 2017).

The social aspects of ESG investing also encompass workplace ethics, with an emphasis on policies related to diversity, inclusion, as well as the prevention of sexual harassment. Additionally, the aspects evaluate the company's mission statement and employee engagement, considering factors such as how much input employees have in determining operational procedures within their respective departments. The criteria also examine the relevance and benefits of the mission statement to society as a whole. Other factors considered include the company's attitude and public or political stance on human rights, as well as any charitable donations made (Syed, 2017).

2.2.5 Governance aspects in ESG investing

In the ESG context, governance pertains to how a company is managed and encompasses not only the executive management but also the board of directors' capacity to serve the interests of various stakeholders, such as workers, suppliers, and the company's customers. The governance aspect also evaluates the company's contribution to the society where it operates (Syed, 2017).

Governance involves a broader range of activities beyond traditional management tasks. It also encompasses the board of directors' diversity and independence, adherence to ethical principles, optimization of long- and short-term strategic goals, and accurate measurement and reporting practices. The governance criteria of ESG investing also includes financial transparency and reporting, which are essential elements of a company's governance. This involves not only avoiding conflicts of interest but also promoting diversity and inclusivity

among the top management within the company, as well as providing full and honest financial reporting (Syed 2017).
The main criteria that the E, S and G within ESG investing are presented here:

Environmental	Social	Governance
• Energy usage • Materials • Pollution • Emissions • Climate change effects	• Workers' rights • Workplace ethics • Mission statements	• Top management and board members • Stakeholders impact • Financial transparency and reporting

Figure 1- ESG Classification

In summary, ESG investing criteria assess sustainability from multiple angles, including environmental, social, and governance-related factors, which investors can make use of to evaluate a company's overall sustainability. The width of the different aspects does, however, raise the question of which of all these aspects an early-stage start-up should focus on, as being perfect in all the criteria from the very start will be hard. Understanding what aspects and areas that investors prioritize therefore becomes crucial in order to match the investors increased requirements towards sustainability impact of their invested capital.

2.3 Different investment styles

An important aspect to understand when discussing the criteria that investors consider when evaluating the impact of start-ups is the different investment styles used by the investors. There are several investment styles described in the literature when it comes to the investors' perception of the corporate social responsibility of target companies. One of the most widely accepted ones is the negative screening method which excludes certain sectors or businesses based on specific criteria related to ESG. The positive screening style instead is the inclusion of certain sectors or businesses based on some specific ESG criteria. There's also the "best-in-class investment style" that targets the best performing companies in terms of certain ESG aspects compared to peers. The thematic investment style focuses on investments related to specific ESG factors that the investors consider highly prioritized or where they think they can

achieve a high impact due to for example contacts or experience within the area (Amir El Zadeh & George Safreim, 2018). By understanding which one of these different styles the investors are making use of, and what aspects some investors make us of for the different styles, the startups can save time and effort of not applying to investors that are prioritizing aspects that the specific startup will not be able to keep up with. Or he opposite, where the startup can focus on labelling itself and proving that it belongs to the group of companies that the investor is prioritizing in their positive screening style.

2.4 Investors increased attention towards sustainability

While less than 20 companies used to report on ESG data in the 1990s, the number has increased to more than 9000 by 2016 with more and more investors joining as signatories of the UN principles for responsible investment (Amir Zadeh & George Serafeim, 2018). According to a report by the Global Sustainable Investment Alliance (2021), the global sustainable investment market grew by 15% between 2018 and 2020, reaching a total of $35.3 trillion in assets under management. Suggesting that there is an increasing interest among investors in sustainability and that many are willing to put their money into companies that are making positive environmental and social impacts.

Investors interviewed by Pitchbook (2022) responded that the top three challenges of sustainable investing are the difficulty of benchmarking non-financial goals, hard to define and measure impact outcomes, and the fact that the understanding of sustainable investing varies widely across investors. Meaning that the investors themselves think it´s hard to decide whether a target company should be considered sustainable, or should be ESG-friendly enough to be invested in. Therefore it´s not a surprise that startups struggle to know what to prioritize to become sustainable in the eyes of the investors. This does, however, open for some subjective interpretation in the judging of the ESG aspects of a startup, as many investors struggle with judging these aspects by themselves. Therefore, this suggests that startups that have clear numbers and measurable metrics on the targeted ESG aspects that the startup is focusing on could benefit from directing the investors in the preferred direction when deciding whether the company can be categorized as ESG-friendly or not.

43% of the investors interviewed by Pitchbook (2022) measure the impact that the portfolio companies generate, where 27% are using customized frameworks, and 16% are using frameworks created by external organizations. The target companies therefore often not only

need to prove it´s sustainable at the point of the screening process but also need to keep reporting on specific metrics along the growth journey of the company.

When the investors were asked what categories of impact investing, they are focusing on, 45% responded that they focus on energy and climate, 32% responded agriculture, and 29% mentioned water, health, and waste. 27% mentioned diversity and inclusion, and 25% mentioned infrastructure. Other categories were only mentioned by less than 25% of the investors (Pitchbook. 2022). These numbers help to create a picture for answering the main research question as it provides an understanding of what areas the startups should focus on as well. As if the startup would focus on ESG areas that are not prioritized by the investors, they would be less likely in receiving investments as they risk talking for death ears when bragging about their impact in areas that are not considered by the investors. These numbers does however not go into detail in why the investors are prioritizing ESG aspects in the screening process, or in detail specific aspects, such as what environmental aspects they consider of extra importance. Pitchbook (2022) as well as PWC (2022) rather focus on E, S or G as well as the percentages of the investors that consider these factors at all.

The drastic increase in ESG-focused capital presented by Pitchbook (2022) and PWC (2022) has resulted in an increased demand for ESG-friendly target companies to invest Investor But in order for startups to attract sustainability focused investors capital they need to prove their level of impact, by the natural reason that the investors want to know that capital that should achieve a certain impact also succeed in doing so. Therefore, it´s in both the investors as well as the startups interest that the startups have a clear understanding of exactly what the investors are prioritizing and considering in the screening process when evaluating ESG aspects and the impact it intends to achieve.

Block et al. (2021) aimed to answer a similar question as the one asked in this article, namely "what criteria matter when impact investors screen social enterprises?". After analysing the 179 investors that participated in their survey, they conclude that the three most common criteria considered are the authenticity of the founding team, the Importance of the societal problem, and the venture's financial sustainability. The research also compares the prioritization of these three criteria between different types of impact investors. After doing this Block et al. (2021) conclude that donors consider the importance of the societal problem being more important than the financial sustainability, in contrast to equity and debt investors. However, equity investors prioritize the large-scale implementation of the social project than higher than the debt investors do. The result´s derived from Block et al. (2021) does however

only scratch the surface of the topic as it does not mention more than three aspects, and do not go into detail in whether some aspects are more of "nice to haves" or are considered "must haves" by some categories of investors.

2.5 SFDR Regulated funds

The Sustainable Finance Disclosure Regulation (SFDR) is a regulation imposed by the EU to put pressure on funds transparency within the area of sustainable investing, mainly to prevent greenwashing. Under the SFDR regulations there are three different funds, article 6, 8 and 9 funds, each one with their own different angles of sustainability focus. The main differences between article 6, 8, and 9 funds are the different sustainability aims of the fund (Eurosif, 2022). Article 6 funds are funds that do not have any sustainability scope and therefore cannot label themselves as impact funds. They do, however, still must disclose the sustainability risks associated with their investments (European Securities and Markets Authority, 2020). Article 8 funds promote environmental and social criteria, but do not have the sustainable investment objective as their primary aim (European Union, 2019). Article 9 funds have a sustainable investment objective and mainly aim to have a positive impact on the environment or society (European Securities and Markets Authority, 2020). The level of disclosure and the investment strategy were also identified as differences between each type of these funds with article 9 funds having the highest level of disclosure requirements, as they are designed for impact investing and are intended to have a positive social or environmental impact. (Eurosif, 2022).

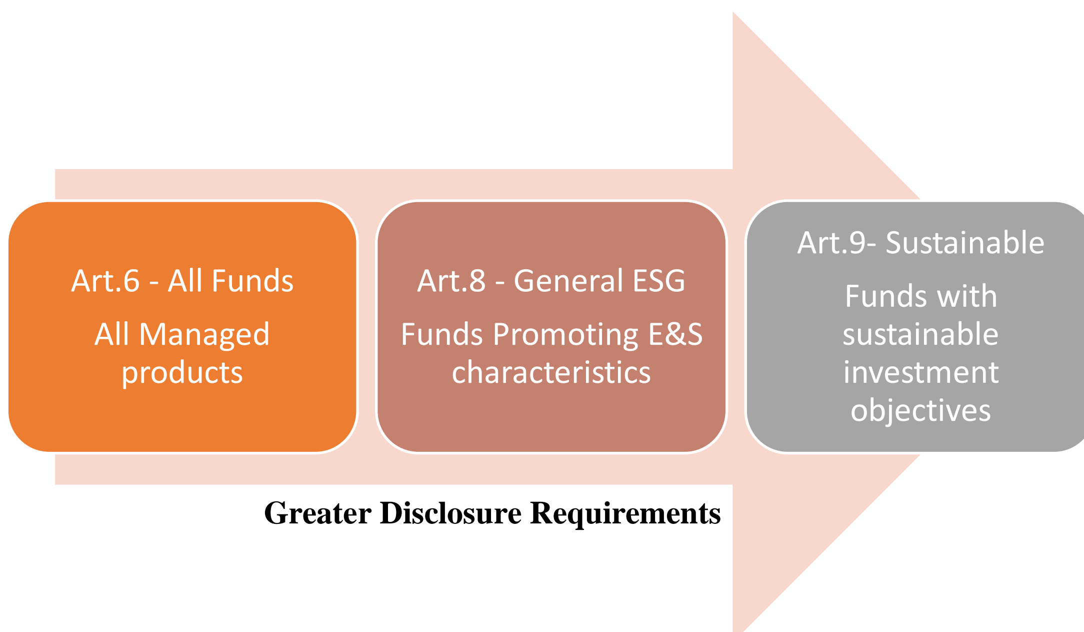

Figure 2- SFDR Fund Classification

Source: Eurosif (2022)

2.6 Measuring impact

Ebrahim and Rangan (2014) conclude in their research that start-ups should clarify their operational mission, as well as specify the scale of the problem it intends to solve, and how much of that problem they intend to solve. The scale and scope. This gives the investor a precise understanding of the impact that it can achieve by investing in the target company. There are however many different theoretical models that aim to quantify or measure the social impact of a company. These models measure different aspects and types of social impact, as well different types of measures such as numerical ones where the dollars spent in relation to CO2 reduction is measured, to more subjective alternatives. If the founders of a start-up intend to prove it´s sustainable for potential investors, they need to understand how impact investors measure impact when they decide whether a target company is beneficial to invest in or not, from an impact standpoint. So and Staskevicius (2015) has divided the impact investment measurement into four phases. These phases are illustrated in Figure 3 below. The first phase, estimating impact, is associated with the investor's due diligence phase where the investors attempt to estimate the expected impact return, benefit-cost ratio, or the social return on investment. So and Staskevicus (2015) suggests that early-stage impact investors that focus on smaller start-ups should develop a simple screening methodology when it comes to impact due diligence, what they refer to as the Logic model. The second phase, planning impact, focuses on what tools and frameworks the investor should make use of to measure the impact. The third phase refers to following up and monitoring the impact that has been achieved so far while the fourth and last phase refers to looking backward and evaluating the impact achieved after the investment is excited by the investor. Since startups that are applying for capital are being screened in the first phase of the impact evaluation model presented by So and Staskevicius (2015), this should also be the phase they should study the closest. This will enable the founders to understand what the investors are considering when evaluating whether the target company can be categorized as an impact company or not. There are several aspects that So and Staskevicius (2015) suggest that investors should consider within the Estimating impact phase. These include evaluating the expected return to estimate the anticipated social benefits against the costs of investing in the target company discounted to today's value. To estimate the impact, the investor needs to define the scope of the analysis by describing the issues and stakeholders that the target company is addressing. Once this is done, specific indicators and measurable inputs and outputs need to be identified to quantify the impact achieved from the target

company. The first phase also includes the theory of change and logic model, which explains the process and linkage from the input to activities to the outcome and the actual impact of the investment.

Figure 3- Impact investment measurement

Source*: So and Staskevicius (2015)*

Another model that rather intends to specify the current sustainability of a start-up is the Impact compass (Malhotra et al. 2019). At the Stanford Graduate School of Business, the impact compass was created for evaluating sustainability in nascent start-ups. The impact compass is well-suited for early-stage businesses due to its user-friendly nature, web-based functionality, and rapid applicability. The compass has six dimensions; value to society, efficacy, impact magnitude, scalability, mission alignment, and ESG, each of which is leveraged by the platform to generate a visual representation of sustainability impacts within the different dimensions.

The United Nations global compact, established in 2000, serves as a practical framework for businesses that are committed to sustainability and ethical business practices. It is a multi-stakeholder initiative that aims to align business operations and strategies with 10 generally recognized principles in the areas of human rights, labour, the environment, and anti-corruption while also serving as a catalyst for actions in support of the UN objectives at a general level. It is the largest voluntary business sustainability project in the world, with 7,000 corporate signatories across 135 nations (UN PRI, 2023).
MSCI, a prominent financial services firm, has developed a range of instruments to facilitate the incorporation of environmental, social, and governance (ESG) objectives into investment screening process. The tools developed by MSCI might however be inappropriate to apply to startups as they are adapted for mature companies and therefore rarely suitable to the startup context where human and financial resources are scarce (Julianto, 2023).

Another aspect that could be considered by investors in the screening process for evaluating the impact of a startup is certifications. Research by Cañón-de-Francia and Garcés-Ayerbe (2009) examined how an ISO 14001 certification could affect the market value of a company by proving to be an environmentally responsible company. The research concluded that ISO 14001 had a negative effect on the market value of many firms due to the signalling of the resources allocated to such certification instead of other activities, at least in the case of less polluting firms. Investors perceived the profit expectations from ISO 14001 to be less than the implementation cost of such a standard. This suggests that a startup needs to carefully evaluate what tools to make use of, and how they are presented for the investors, as focusing on the wrong ones might even harm the valuation of the company.

Tools and frameworks as the ones mentioned can be helpful for startups to communicate it´s level of impact and sustainability, as well as for investors to get an understanding of the impact it will generate for by investing in the target companies. But what aspects the investors are focusing on, and what the start-ups therefore should prioritize still is an area that´s relatively unexplored. The ones mentioned are rather examples of what could be used, or that some make use of, or numbers describing what wide areas that some investors prioritize, but without specifying the specific factors and aspects that the investors are considering of extra importance.

2.7 Challenges

Measuring on sustainability is just one of many challenges that startups and investors face when it comes to the area of ESG investing or raising capital with a focus on sustainability. As many of the difficulties are related to the diffuseness of the area, clear indications for what investors are prioritizing, would help the startups with what to focus on. This would also make it easier for the investors in the screening process as the target companies already will be able to have the right aspects in mind, making the startups more comparable with each other.

2.7.1 Challenges for Investors

Due to the lack of data and accuracy of the available data, especially at the level of start-ups, the screening process becomes challenging for investors that intend to incorporate the impact aspect when evaluating startups (Wang. C. et al, 2022). Audit requirements and the lack of reliability on ESG aspects makes it extra challenging for larger institutional investors. Also, the lack of comparability of reported information across firms becomes a challenge for the investors (Amel-Zadeh & Serafeim, 2018).

Due to the lack of standardization in ESG reporting frameworks and metrics investors often are left relying on their own judgment to determine which companies meet the criteria that they intend to impact. Causing the screening process to be more subjective and time-consuming. Additionally, investors may face challenges in verifying the accuracy and transparency of the ESG reporting data provided by startups, particularly if the startups lack a dedicated sustainability team or personnel with expertise in ESG reporting. Moreover, there is a risk of greenwashing, where companies may pretentiously market themselves as sustainable or environmentally responsible, making it difficult for investors to distinguish between honest sustainability efforts and mere rhetorical ones. leading to reputational damage and loss of trust with stakeholders (Wu et al. 2020).

Another challenge mentioned by Eurosif (2020) is the perceived trade-off between financial returns and ESG considerations, as some investors mean that focusing on ESG aspects may negatively impact financial performance. However, recent studies have shown that ESG investing can deliver competitive financial returns, and companies with strong ESG performance are better positioned to mitigate risks and capitalize on opportunities in the long term (Eurosif, 2020).

2.7.2 Challenges for Start-ups

Startups face a range of challenges when it comes to implementing efficient ESG (environmental, social, and governance) and sustainability reporting practices. Limited resources, including limited financial and human resources, can make it difficult for startups to devote time and money to ESG and sustainability reporting, resulting in limited capacity to collect, track, and analyse ESG data and report on it (Robinson, 2020). In addition, many startups lack dedicated sustainability teams or personnel with expertise in ESG reporting, making it challenging to navigate the complex landscape of ESG frameworks and standards. This can lead to incomplete or inaccurate reporting, which can result in a loss of credibility with investors and other stakeholders (Dornbach-Bender & Jacobsen, 2021).

ESG reporting standards and frameworks are constantly evolving, and there is no consensus on a universal reporting framework for startups. This can lead to confusion and inconsistency in reporting, making it difficult for stakeholders to compare ESG performance across companies (Jalili, 2021). Furthermore, startups often have multiple competing priorities, including product development, customer acquisition, and fundraising, which can make it difficult to prioritize ESG and sustainability reporting, especially in the early stages of the company's development. This can result in limited attention and resources being devoted to ESG reporting, which can impact the quality and comprehensiveness of the reporting (Robinson, 2020).

Startups may face the risk of greenwashing, which refers to the practice of making false or misleading claims about a company's environmental or social impact. This can result in reputational damage and a loss of trust with stakeholders. Therefore, startups must ensure that their ESG reporting is accurate, transparent, and supported by concrete actions (Jalili, 2021).

2.7 Impact of a start-up’s Sustainability on its valuation

One of the reasons why startups should consider ESG criteria when raising capital is because the focus on ESG from investors leads to higher competition among the sustainable companies, which provide better bargaining power in the negotiation phase for the startup founders. Which results in higher valuation and better conditions for the founders (Mansouri & Momtaz, 2022). The conventional method for valuing a company is based on financial projections and present value of future potential cashflows and earnings (Brealey, Myers and Allen 2007). This is

measured through valuation techniques that focus on future earnings and current assets. Examples are the discounted cash-flow method, the earnings multiple, or the net asset value methods. Methods which are rarely accurate, available, or relevant at the level of early-stage startups (Miloud et al., 2012). Thus, the pricing mechanism is heavily influenced by the bargaining power between the entrepreneur and investor as future earnings are based on projections and parameters that come subjective to a certain degree (Emir Hidayat, S. et al., 2022).
Sustainable business valuation is however looked at not only from a strictly financial perspective but rather from a triple bottom line perspective where financial, environmental, and social benefits are considered along with each other. Sustainable business valuation is thus combining the traditional financial valuation with the value of the impact made by the start-up on specific ESG criteria. (Soans, F, & Kostadinovic, B, 2022).

If a start-up can prove it is impacting these criteria in a positive direction, it can therefore also increase its valuation, as it´s not only the financial projections that are encountered when finalizing the valuation of the company (Mansouri & Momtaz 2021). Thus, taking the sustainability aspect into consideration can increase the entrepreneurs bargaining power. Zein Et. Al (2020) recommends start-ups to disclose their degree of ESG compliance and use it for brand promotion, not only towards their customers, but also investors. It is also shown that being open with ESG criteria have been linked to lower capital constraints and lower costs of capital for companies raising capital (Amel-Zadeh & Serafeim, 2018). Mansouri and Momtaz (2022) found that a one-standard-deviation increase in ESG measurement is associated with a 28 % increase in the funding amount. However, it is also associated with decreased returns of 16 % in the first 12 months.

3. Methodology

The primary objective of this chapter is to describe the research methodology that was used for the study. The chapter starts with a presentation of the research philosophy that underlies the relevant theoretical concepts. Subsequently, *the research design, data collection methods, and data analysis techniques* are derived from the research philosophy. Finally, the chapter discusses qualitative and ethical considerations that were considered during the study. In summary, the present study follows an inductive and qualitative approach. The primary data collection method employed was semi-structured interviews, which were conducted using a

generic purposive sampling technique. The interview data was analysed thematically, and the themes were compared with the relevant theoretical concepts obtained from a literature review.

3.1 Research Strategy

As the research intends to discover what factors and aspects different types of investors are looking at when evaluating a startup's level of sustainability, and therefore what startups should focus on to become sustainable in the eyes of investors, the focus will be on the interviewees' reasoning and ways of working with these questions. As the qualitative research method has its focuses on words, behaviour, reasoning, experiences, and perspectives of the interviewees, the qualitative method will be suitable. A quantitative method would instead be suitable if the research would focus on a larger data set, with numbers or quantifications (Bell et al., 2022).

Bell et al. (2022) identified two main ontological approaches, objectivism, and constructionism. Objectivism assumes that organizations and phenomena possess the attributes of an object and should be understood as an objective. However, as sustainability-related theories are indeterminate and subjective in nature, rather than objective, the constructionism approach, which considers reality as socially constructed by human perceptions and understandings, was deemed more suitable for this research. The study explores sustainability definitions, theoretical concepts related to venture capital investments, and subjective views on investors perception on the aspects that investors are considering. Therefore, when researching on investors within the area of sustainability, adopting a constructionist ontological stance is deemed appropriate.

Given that the study adopts a constructionist ontological stance, an interpretivist epistemological position is considered to be most suitable (Bell et al., 2022). The interpretive approach primarily relates to understanding human behaviour, processes, and how people understand their surroundings. This approach is therefore relevant as this study aims to understand how investors create their own perceptions of target companies' sustainability level. Since the research questions are mainly empirical and are based on the investors' understandings, the data gathered is highly subjective, without any objective truths resulting from it. Meaning that the study aims to understand different views and ways of working with questions related to ESG and sustainability based on investors' views.

Furthermore, as noted by Bell et al. (2022), making use of a "double interpretation" approach to gather data is optimal for some research. This approach involves the researchers making

their own understanding of how interviewees perceive some questions and topics. The circumstances of this study are similar to the ones of the described approach, as the conclusions are derived from investors' views, understandings, and ways of working with sustainability-related factors in the screening process. Due to the multiple levels of interpretations that are involved, an inductive strategy should be used (Bell et al., 2022).

As the authors explored the research subject, the theories used have been adapted and adjusted to be able to iterate on the gathered information and theories, based on interviews, literature review, as well as information from secondary data sources. See figure 4. This follows the abductive approach, which is a mix of the inductive and deductive theories, allowing the researchers to go back and forth to iterate on the gathered information and data (Bryman & Bell, 2022). The flexibility that the abductive approach has is exploratory, that comes suitable when studying a subject that yet is relatively unsearched, as the sustainability investing criteria considered for startups. Case studies within the abductive approach therefore comes suitable when the aim mainly is to generate theories rather than testing already existing ones, but rather complement them, and is thus suitable for this research.

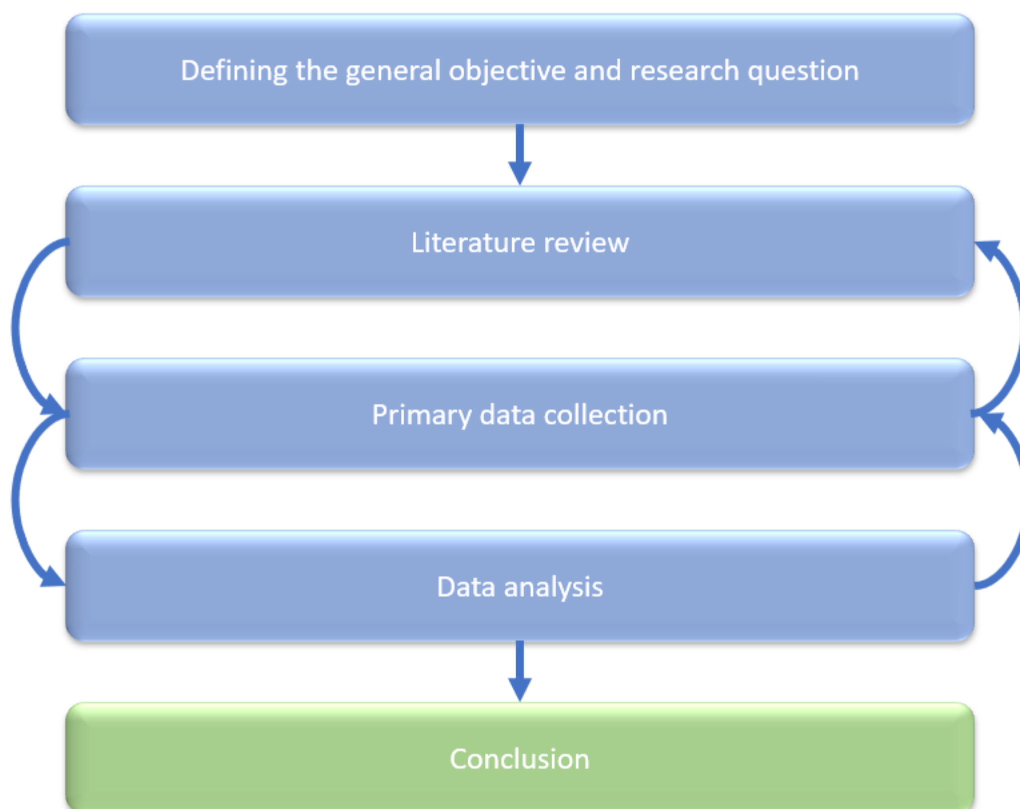

Figure 4- The research process

Source*: Made by the researchers*

3.2 Research Design

Following the literature review, it is clear that the topic of sustainability evaluations of start-ups is a relatively unsearched topic, as also have been stated by Gompers et al. (2021) and Lin (2022). As found from the literature review, the extent and focus of the sustainability assessments of investment opportunities within the screening process highly vary from one investor to another. Furthermore, existing sustainability assessment methods have largely focused on larger institutions that invest significant sums of capital in prospects at later stages of maturity. The area of what aspects investors that focus on start-ups, in general, prioritize, therefore remain relatively unexplored ground.

The research makes use of a cross-sectional design since the research intends to investigate several investors views and ways of working with sustainability related questions. The intention is to get an understanding of the investors views on the topic as a whole, rather than looking at the unique outliers, even though those will be taken into consideration during the process as well. Bell. et. al (2022) state that the cross-sectional design focuses on the sample of the cases, to produce generalizable findings, with little regard to the special and unique context of the interviewees. Therefore, cross-sectional design was used in the study. e

A pure multiple case study, without interaction from the cross-sectional method could also have been suitable for the study. It can be explained as a comparative design, where multiple cases will be studied, to be able to contrast the different investors responses with each other. As this study however intended to find themes across the different interviewees instead of the unique cases, the cross-sectional method was considered most relevant.

The aim is to perform interviews with investors to understand their perception of the startups reported data and how it would affect their valuation of the firm. The point of this data collected and analysed is to identify connections between the ESG data reported and the improved perception of the investors towards the company studied and to identify any patterns of association that might be applied in other startup contexts.

3.3 Data Collection

The collected data for this study consists of both primary as well as secondary data. The primary data have been collected from semi structured interviews from interviewees considered suitable for answering sustainability related questions from an investor perspective. The

secondary data are based on statistics and reports from well-known, trusted sources such as Pitchbook or Eurosif. The method used for collecting the data is well associated with the purpose of the research, which Bell. et. al (2022) state is of high importance.

3.3.1 Primary data collection

The primary data was gathered from interviews as it´s a qualitative study that will collect information from investors that should not be influenced from each other. Based on the chosen research approach, semi-structured interviews are considered to be the most suitable method for the primary data collection. This will enable to answer the research question, as well as sub questions that are set in advance of the interviews.

3.3.1.1 Semi structured interviews

Bell. et. al (2022) states that the cross-sectional design in a qualitative study that´s been chosen for the research makes a semi structured interviews optimal as it offers the researchers to find themes and contrast multiple interviews in parallel. The semi structured interviews enabled a more enhanced insight of the interviewees priorities in terms of sustainability and ESG criteria by providing structure to the process of collection data. Semi structured interviews provide the structure needed when interviewing several cases and thereby provide cross case compatibility. The semi structured interviewing technique also enable the comparison of differences and similarities that´s been detected within the gathered data (Bell. et. Al. 2022).

The semi structures interview is a combination of structured interviews where the interviewer follows a pre-set scheme of questions, but at the same time has the opportunity of asking follow up questions and let the interviewee freely spin off within the relevant area if it would intend to do so. Therefore, the semi structured interview style offers the advantages of both the structured as well as the unstructured technique. When using the semi structured interview technique, a preset list of questions will be set, called the interview guide. These questions include the topics or questions that the interviewer intends to receive responses on during the data collection, and interviews. These questions are, however, set so the interviewee could answer in the format it's comfortable with. The semi structured interviews have the ability to also include topics and questions outside of the area and questions intentionally listed within the interview guide. This makes the semi structured interview method preferable as it enable the researcher the opportunity to go deeper into areas that we´re not set up previously within the interview guide, perhaps because they weren't known of before the actual interview. The chosen method was hence crucial for enabling the researchers to be open for unexpected new

areas of data and to deepen the primary data collection that will lay the foundation for the final analysis and conclusion of the research.
The interview guide had a total of 10 preset questions that also was followed by 5 pre-set follow up questions. The interview guide did however offer space for topics and question outside the preset agenda, which often resulted in many questions not being asked as the interviewee already answered them within previous questions as the interview often ended up close to a conversational context instead. This suggests that the interview process had a relatively flexible approach (Bell. et. Al. 2022).

3.3.1.2 Selection of interviewees

As the gathering of data is a crucial part of the research, and there's multiple different approaches for the task, the choice of method is of high importance (Bell. et. Al. 2022). In a cross-sectional study, all the investors, i.e., interviewees, need to be carefully selected to be relevant to answer the research question. Each individual investor, or investment company needs to be chosen either because it is expected to provide similar results, or contrasting ones (Yin, 2018). This is why the different investors selected for this research were chosen within different categories of the investment industry. A purposive sampling has thus been used when sampling the interviewees for this research. The selection of interviewees is therefore not random, but rather based on strategically set criteria to enable answering the research questions and get a deep understanding of the studied subject (Bell. et. Al. 2022). A positive sample is however not necessarily representative for the whole population according to Yin (2018) and can therefore not be used for generalization for the whole population (Bell. et. Al. 2022). Since this qualitative research is intended to understand what factors investors consider when deciding if a target company is sustainable or not in the screening process, generalizing the findings to the whole population therefore is not needed (Yin, 2018).

3.3.1.3 Participants

Out of the 18 interviewees that were interviewed 7 individuals were representatives from VC funds, three were from government-backed institutions, 2 consultancy firms with a focus on VC, 5 investment funds, and one angel investor. The investors interviewed in this study are all located within the Nordic region. This decision was taken mainly as the Nordic countries investors have come relatively far regarding sustainability incorporated within the investments industry, but also as the researchers are based in Sweden (Sustainable development report, 2020). As the aim is to understand what factors investors consider when evaluating the impact

of target startup companies, interviewing investors that do not consider factors related to impact or sustainability at all would not be helpful for answering the question. Therefore, the interviewees are skewed towards caring more about sustainability and impact than the general investor. But as the research intends to support startups that intend to secure the impact stamp from the investors in the fund-raising process, the skewness of the report does not impact the relevance of the study.
The interviewee´s was initially reached by e-mail, where time was spent to find specific personal e-mail addresses to people working either with sustainability-related issues, or as a high-level decision maker such as partner, investment manager, CFO, or similar. This ensures that the interviewee has the information necessary to answer the questions. Out of the initial 87 people or organizations that were contacted, 7 responded to the first e-mail. After waiting another week, a second mail was sent to all the ones that didn't respond to the first mail. These mail conversations resulted in a total of 17 meetings held via teams as many of the interviewees still did not answer, did not have time, or said they would not be suitable for answering the questions. One of the interviewees responded only by e-mail, without providing the opportunity to be interviewed digitally.

Below a table categorizing the investors surveyed based on their private Vs Public funding and the level of regulation they are subject to according to their SFDR classification providing readers with a clearer understanding of the research sample and contextualizing the insights gathered. This categorization helps to highlight the individual characteristics of the investment firms interviewed and how to interpret the statements of the investors.

Tableau 1- List of Participants

Investor	AUM	Position of the Interviewee	Interview Duration	Sector Focus	Type of organisation	SFDR Regulation Applicable
Investor 1	NA	Program manager	20min	All	Public Institution	NA
Investor 2	Non Available	Investment Analyst	30min	Cryptofinance	Private VC	No
Investor 3	SEK 2Bn	Investment Manager	40min	All	Private VC	NA
Investor 4	NA	Regional Developer & Team Leader	20min	All	Public Institution	No

Investor 5	123B	CEO	30min	Heavy Industries	Private investment company	NA
Investor 6	650m	Fund Manager	20min	Green Tech	Public investor	NA
Investor 7	Non applicable	Investment manager	30min		Private VC	NA
Investor 8	Non applicable	Associate	40min	NA	Private Consultancy	NA
Investor 9	NA	Angel Investor	60min	Life Science	Private – Angel Investor	NA
Investor 10	Non available	Investment Analyst	40min	All	Private VC	Article 8
Investor 11	Non available	Co-founding Partner & Head of Investments	30min	Tech	Private VC	NA
Investor 12	€250m	Investment analyst	30min	Healthcare & Life Science	Private VC	NA
Investor 13	NA	General Counsel and Head of Sustainability	30min	Technology	Private VC	NA
Investor 14	600m	Investment Manager	30min	GHG Emissions and boundaries tra nsgression	Private – Bank	NA
Investor 15	300m	Co-founder and CEO	30min	Greentech	Private Investment Company	NA
Investor 16	770m	Principal	40min	Science based deep Tech and Hardware	Private VC	Article 8
Investor 17	NA	Principal	40min	Healthcare	Private VC	Article 8
Investor 18	SEK 5Bn	Head of Sustainable Investments & Senior Investment Director	By Email	Life science and deeptech	Private investment company	NA

3.3.1.4 Interview setting

As the study intends to interview Nordic investors, and the researchers' location is Gothenburg, all interviews were decided to take place through the digital meetings platform Microsoft Teams. This enabled more interviews to be performed as the time that otherwise would have been spent traveling could be spent on interviewing and contacting interviewees. Having interviews digitally, however, risk limiting the influences such as body language or eye contact

that physical interviews otherwise can provide. Although due to time and financial constraints, digital interviews were chosen for interviewing all the investors. Digital interviews can however limit the researcher bias as the presence of the interviewer can affect the responses of the person being interviewed (Bell. et. Al., 2022). Also, the fact that digital interviews allow both the interviewee as well as the interviewee to feel more relaxed as they have the opportunity to take the meeting from home (Saunders. Et. Al., 2009). The interviews lasted on average for 30 minutes, with a minimum of 20 minutes, and maximum of 40 minutes.

After receiving permission to record the interview, they were recorded to be able to go back and listen to it if anything would be unclear afterwards. As transcribing all the interviews would take an extensive amount of time, the decision was taken not to transcribe all the interviews, but rather immediately take notes. One of the researchers was the one talking and asking questions, while the other one was responsible for taking notes. This ensured that the ones taking notes would not be distracted by trying to keep the conversation going or asking to follow up questions when needed.

3.4 Data Analysis

According to Bell et al. (2019), data analysis requires going through the collected data with an analytical eye and reducing it to identify patterns and make to be able to find patterns within it. Thematic analysis, one of the most used approaches for analysing qualitative data, is being employed for this study. This approach involves identifying patterns in the data, such as recurring phrases or themes related to a particular question. When using thematic analysis, the researchers looked for patterns such as recurring topics, analogies, similarities, differences, and theory-related material (Bell et al., 2019). However, a potential limitation of thematic analysis is the lack of clear guidelines, which can result in a variety of different approaches and make it hard to pursue all the generated themes (Castleberry & Nolen, 2018). It is therefore important to keep the balance between exploring new themes emerging from the analysis and relating them back to the research questions that are the foundation for the investigation and literature review (Bell et al., 2019).

The primary data was obtained through semi-structured interviews, which were recorded using phones, as described in chapter 3.3 Data collection. These interviews were noted manually in English for most of the cases and Swedish in some specific cases, depending on the language used during the interview. The content generated from the interviews was analysed and

summarized in a new document where answers to each question were grouped together under the question to have a clearer visibility of the potential patterns, similarities or differences in the investors opinions with regards to that specific question. and relevant quotes were highlighted in order to be added to the relevant section of thematic analysis. Further filtration of the data took place through the pairs discussions to confirm the data interpretation and the potential contribution of each quote to the analysis. Although the coding procedure has not been conducted in a systematic conventional way, it became increasingly apparent which potential themes that could roughly be constructed based on the several analysis iterations.

3.5 Research Quality

To evaluate the quality of the research, reliability and validity are two important criteria to consider (Bell et al., 2019) especially for qualitative research that often risks being associated with subjectivity. Validity is mainly about the appropriateness of the means or tools used to conduct the study and collect the data required for the specific research question (Leung, 2015). Reliability however is about the consistency of the research results. In other terms, a study is considered reliable if it results in consistent results every time it is conducted in the same conditions (Leung 2015). Reliability and validity can both be split into external and internal reliability which we will discuss and clarify in the context of this research (Leung, 2015).

3.6.1 Validity

A research's internal validity is mainly about the confidence of the researcher that the drawn conclusions from the study findings are not affected by other factors (Bell et al, 2019). To ensure the validity of the study, various principles and methods have been followed during the research process in the context of this research. Collecting primary data through semi-structured interviews, the authors carefully selected the participants in a way to interview people with extensive knowledge in the investment world. The positions of the interviewed people within the investment firms are detailed in the participants' section.

One of the validity risks that could be mentioned is the possible bias to be aware of when collecting data and drawing conclusions. Even though the agreement was that the interviewees would be anonymous, it is probable that they wanted to present their organizations as forward-thinking in some way especially as we are talking about sustainability practices in the investment field, a topic that sometimes can be sensitive. Unfortunately, it was deemed tricky to address this concern as it is out of the researchers' control. To prevent the risk of drawing

conclusions based on misleading information from the interviews the researchers made use of triangulation. That way the claims made by the interviewees could be controlled by checking different other sources such as webpages or other publicly available material.

3.6.3 Ethical considerations

Numerous ethical considerations should be considered in a thesis writing process. These include being transparent in the writing process, following the research established rules and showing respect to all those involved. During the interviews conducted for this study, the goal was to maintain transparency throughout the process. This was achieved by informing the participants about the study's purpose by email and at the start of the interview, asked for their permission to record, and informed them how the collected data would be used in the thesis. Participants were also aware that participation was entirely voluntary, and they could end the interview at any time for any reason. To encourage candid responses, participants were informed that their answers would be anonymized and treated with care.

3.6.2 Reliability

External reliability as defined by Bell et al (2019), is the extent to which the research results are generalizable and applicable to other cases. This issue was addressed by providing a detailed picture of the steps taken during the study throughout the document. An extensive description of the decision-making process throughout the research is also provided in various sections of the paper. Additionally, a transparent approach has been deployed to enhance the reproducibility of the study. The sampling method, however, used in this study may limit the possibility of replicating the results. Given the rapidly changing landscape of impact investing and investment regulations, it is less probable that the same observations would be observed if the study were to be conducted again in the future.

Internal reliability however pertains to how the data is interpreted by the members of the research team, and most importantly, the level of consensus on the interpreted data (Bell et al, 2019). In quantitative research context there is a higher risk of subjective interpretation of things. Therefore, the researchers used the response validation technique for every time there was an ambiguity in the answers provided by the interviewee to make sure that the interpreted meaning is the same one conveyed by the respondent. Additionally, working in pairs on this research allowed for both an independent analysis of the data as well as a collaborative one afterwards. This approach has several benefits, including enhancing the dependability of the

findings and identifying any discrepancies in the results. The authors of the study worked closely together, examining inconsistencies within the findings, and sometimes revisiting the original material by recalling the interviewees answers together again to clarify the respondent's intended meaning. As a result of these efforts, the internal reliability of the study was deemed to be high.

4. Empirical findings

This chapter presents the main findings obtained from the conducted semi structures interviews in relation to the research questions. The chapter has been organized based on the themes that emerged from the interviews, using a thematic analysis approach. The presented findings will serve as the foundation for the analysis and discussion in the next chapters. The main findings derived from the interviews divided into themes that relate to the research question, which will be answered in the discussion chapter. The themes are highlighted and supported with the use of quotes from the interviewees to provide the reader with deeper insight into the interviews. The full interviews records are accessible upon demand the investors categorization is described in detail in the participants' section in previous chapter.

4.1 Business feasibility is a deal breaker

The focus on the business model's feasibility and how suitable is it for solving a sustainability related issue while operating profitable and efficiently was a main criterion that all the investors pointed out. An entrepreneur can't bring a weak, non-scalable, or non-profitable business model with the aim to address an environmental or social issue and hope to be able to succeed with fundraising. It is safe to presume that potential financial scalability is a must have for investors to consider investing in start-ups that intends to prove its impact for the investors.

"We are more interested if the business idea works, best workplace rewards and similar doesn't really matter that much. Impacting ESG factors is considered positive, but we put more focus on making money, so it doesn´t matter that much. As long as the business is not bad for the environment, and they have plans that they report on progress we are ok. Businesses in sectors such as oil, gas and tobacco however wouldn't be so attractive" – *Investor 3, Private VC*

Investor 3, a VC that reports on sustainability factors clearly states the importance of the companies they invest in making money. Without making money, or at least having the potential and intention to do so, they would not consider the investment. The same goes for investor 5. That means that the times when it was enough for a company to affecting the environment positively is past, now there is a larger focus on profitability.

"We don´t look at any specific boxes or frameworks, rather common sense. We do however want to be able to quantify the progress as it´s linked to the financial targets. For example, reduced C02, amount of energy produced, consumed or such. Times when companies only can be sustainable without making profit is bye. It is however still a focus on sustainability, as it can drive profit in the long run. They focus on changing something bad to something that´s better. Not like investing in a better oil company that the ones existing, but solutions that improve society when they sell more. Such as wind turbines". – Investor 5 (investment company).

The investors prioritization of companies' ability to scale its business can also be tied the capabilities of the team and their willingness to make their vision a reality.

"*We do not invest without thinking that the team has the ability to scale the idea, which will thereby enable a larger impact in itself. The strategy and the future intentions of the team are something we look into as the startups has no history of ESG actions yet"- Investor1 (Public Investor).*

"The most important aspect is the founders' or boards reliability, and trustworthiness that they will succeed with the development of their vision and business."- Investor 15 (Private Investor).

4.2 Gender balance in management is prioritized

The gender balance within the founding team or management was considered by 12 out of the 18 interviewees. All the government-backed institutions considered this to be important.
Investor 11, a government backed institution explain that they do so for business reasons, more specifically because they consider companies with a diverse set of managers or founders to be more ready for offering a diverse set of customers their services.

"We don´t use any specific metrics to measure for gender diversity, but it´s something we always consider when evaluating potential investments. It can however be okey to not have a diverse team from the very beginning of the startup, as long as there is a clear strategy and plan for achieving this gender diversity, especially at the management level, in the future. The reason why we target start-ups with diverse team members is because you must have a diverse broad team to be able to target a broad audience of customers. This is the reason why we include the diversity aspect in the term sheet for every investment we proceed with." - Investor 11 (private VC).

"*Gender and carbon footprint most prioritized, most important is to measure this and record it"*. Investor 3 (private VC).

Investor 3 even prioritize the gender balance aspect among the most important aspects related to ESG within the screening process. While investor 10 consider it, and intends to set up policies for their portfolio companies to make sure that they are considering these factors even after the investment has been done.

"We are trying to onboard our portfolio-companies on these types of regulation with metrics that handles policies for gender and diversification." – Investor 10 (private VC).

Investor 9 however insisted on not exaggerating the gender-balance aspect in a way to just tick boxes and instead highlight the importance of doing the right things for the right purposes instead of just ticking boxes to look try to give the impression of being sustainable and impactful.

"Make sure to not exaggerate some aspects like "number of women" just to tick some boxes" – Investor 9 (angel investor).

In contrary to this quote, however, this does not mean the gender equality aspect isn´t considered important from investor 9, just that the company should focus on scaling it´s business and not exaggerate certain aspects to look good when contacting investors, because it will eventually shine through.
Investor 15 was the only one of the investors interviewed who expressively said they don´t consider the gender diversity aspect at all. The board members of Investor 15 are 6 males,

everyone being over 60 years old, and they admit that having more diversity could be better, even it´s not on the agenda for the moment.

"*Don´t consider other aspects related to governance, such as diversity on the team. Even though it would be positive with diversity." – Investor 15 (private investment company).*

4.3 Greenhouse gas emission is a common metric for investors

A great focus is put on emission reduction as it is a common metric and businesses are getting familiar with it. Investors are therefore often demanding their portfolio companies to work proactively with emissions reduction. When asked about frameworks or metrics for evaluating sustainability aspects of a target company, investor 15 said that they exclusively measure greenhouse gas emissions, but nothing else.

"We don't, expect from CO2 impact measurement" Investor 15 (Private Investor).

One of our interviewees, who was part of an investment directive of a bank, confirmed that they have a strong focus on emission reduction through their investment.

"Especially one of our funds has a focus on greenhouse gas emissions and boundaries transgression." - Investor 14 (Private Bank Fund).

Another example of this theme is Almi invest greentech fund (2023) that describes themselves on their webpage as

"*Almi Invest GreenTech Fund backs Swedish early-stage startups that significantly reduce greenhouse gas emissions*".

4.4 SFDR regulation and reporting awareness is positively viewed from investors

SFDR regulations, while they exist to regulate investment funds, a start-ups familiarity with them is considered to be a plus among investors. Investor 17 mentioned that a start-ups familiarity with SFDR regulations and reporting requirements is a good sign for them as it

signals that the company has knowledge within the area. It also comforts the investor as it lifts off some of the reporting and compliance work among SFDR compliant funds. (i.e. Article 8 or 9 funds). This is of extra high importance due to the increase in the funds claiming to be SFDR compliant.

"Knowledge about SFDR is a good sign as for us it is a bit of a pressure as VCs to report on that. If a company can show familiarity with this kind of reporting and comfort with reporting on that, that can comfort us as investors"- Investor 17 (Private, Health-tech)

"The sustainable finance disclosure regulation (SFDR) is quickly becoming the most common approach to measure sustainability metrics of a portfolio. It includes several indicators for adverse sustainability impacts" – Interviewee 8 (Management Consultant with focus on VC).

The intention of the team to work on ESG aspect is considered by most investors. The team must showcase their intention to prove that ESG is well integrated to the company. Concretely this could be achieved by having relevant policies in place, a future ESG plan and preferably a person who oversees the execution of this plan. The sustainability effort will not be enough for a company to grow.

"The early-stage VC funds that do not extensively work with sustainability may be aware that sustainability will become important at the stage of exit, or an IPO. Some aspects may signal to an investor that the company is managing their sustainability risks and impacts: A sustainability strategy which considers negative impacts, material risks, coping with sustainability reporting metrics such as SFDR, and having a person responsible for the sustainability strategy" - Interviewee 8 (Management Consultant with focus on VC).

"During the initial workshop we set goals and then we follow up. We try to make them understand that if they don't start from the beginning it would be difficult to start later" – Investor 11 (Private VC)

4.5 Focus on one specific impact goal

One aspect that was mentioned by several investors was the fact that the start-up founders should be focused and specific about the environmental or social aspect(s) that they are

targeting. To achieve this, they need to have a clear strategy of how they would do that. A general approach where the company tries to target many impact goals would not be appreciated by investors as it shows non-cantered efforts and potentially greenwashing to some extent.

"What we evaluate is the quality and strategy to go towards that specific goal. We evaluate the application forms: Does the company really know what they are doing and do they have the intention to execute the plan?" – Investor 1 (Government Backed Institution)

"I prefer to see the focus on the ones where we really make an impact instead of talking about all the SDG goals." – Investor 9 (Angel Investor)

Investor 1 is clearly stating that it is not enough to just talk widely and diffusely about different ESG goals and expect the investors to just check that "sustainability box" to then move on to other aspects considered in the screening process. The start-up has to be specific and clear on how much impact the investor can expect for the money they're investing in the start-up. Investor 13 further states the importance about having measurable targets to prove the progress along the journey of the start-up.

"Focus on specific questions, not everything. Have a clear story that´s backed by data that you also clearly can measure so you can prove and support how much good you´re saying that you are doing. This way you show that you´re not just pretending, but that you genuinely care. And not just that the impact aspect is for example 5% of the business". – investor 13

As a founder it might be tempting to mention and market all different types of ways that the start-up would be sustainable or working towards different ESG goals. The quotes from investors 1 and 13 however suggest that the start-ups that does so, rather harms itself as it might send the wrong signals to the investors. By focusing on one specific goal, where the historical or potential progress can be backed up by data, the founder signals to the investor that the start-up is being serious about the impact it intends to generate, rather than just intending to label itself as impactful and sustainable, without really caring.

4.6 Sustainability does not determine the valuation

The answer on whether the environmental and social sustainability of a start-up provides a higher valuation did not have a one straightforward answer from all investors. None of the investors were able to say that they put a valuation premium to companies that prioritize environmental and/or social sustainability aspects. The takeaway from the answers to this question is that the impact aspect of a start-up would improve the investors evaluation of it, but no conclusions can be drawn regarding it´s valuation impact.

"It should be real. It will not impact my valuation of it but my evaluation of it. I don't like greenwashing'' – Investor 9 (Angel Investor)

The increasing regulations related to the environmental/social aspects of businesses can act as a catalyser for the transition towards incorporating sustainability related numbers to the valuations process. For the moment however the interviews performed don´t suggest that any link can be drawn between the valuation and sustainability of a business.

"As all companies we invest in have a positive impact by default it is difficult to answer this." - Investor 16 (Private Investor)

"It's difficult to say what impacts the holistic value of the valuation of a company. But if a company is doing bad we would of course not consider it." – Investor 17 (Private Health-tech Investor)

It is worth mentioning that only five of the investors were able to answer this question. Of those, only one stated that sustainability factors have a positive influence on a start-up's valuation. However, the others were hesitant to make a definitive assessment, stating that they needed to consider the full picture before deciding to proceed with the investment or not. Another reason why this question was not answered by all interviewees is because some of the governmentally backed institutions rather work with grants and therefore do not involve any valuation matters. The main issue with the question is however that the investors either consider the company to be sustainable enough to be investable, or it's not. Therefore, they were not able to for example answer that the sustainability of a start-up improves the valuation with x % for example.

4.7 ESG due diligence exist, but rarely strict and quantitative

Investors, go through a due diligence process before making investments. This process often involves questionnaires that intend to understand the company's sustainability practices. Some investors also had, in addition to the general DD questionnaires, some industry or sector-specific questions that they ask, such as the number of customers helped, or the total loan amount granted to companies within the emerging market fintech sector.

"Every year we follow up on sustainability aspects. And for the ones categorized as "impact companies" we follow up on metrics such as number of customers helped or loan amount provided to people in a developing country ". – Investor 13 (private VC).

Investor 13 however is an investor especially focused on companies that in one way or another support developing countries. Therefore, it´s not a surprise that this company has relatively specific criteria when following up on ESG aspects. A majority of the investors however had a more diffuse way of working with these criteria, like Investor 5.

"We have no specific boxes or frameworks; we use rather common sense" - Investor 5 (Investment Company).

Additionally, one investor came up with a distinction between hard and soft metrics, meaning with hard metrics being specific, measurable numbers related to ESG aspects, and soft metrics such as the team's knowledge and willingness to implement sustainability within the business context. Some investors, like Investor 10, are still working to come up with metrics that are suitable and applicable to their portfolio companies to ensure progress is measurable also after the investment has been made.

"We try to evaluate the business in the due diligence process and identify the red flags but we have been looking into more metrics that could be used according to the company's field. Like energy use or water use" – Investor 10 (Private VC).

Especially the governmental investors were relatively loose when it came to ESG expectations in the screening process. The aspect they prioritized the most was that they should by "common

sense" judge whether the company has a good impact on the society or not. After considering the target company being a company that has positive impact, they don´t prioritize the ESG aspects that high as they think they can be dealt with later in the companies' growth journey.

"We highly consider the willingness of the team and the strategy towards making more ESG impact in the future and it doesn't matter if they haven't started at the moment of the investment due to the often times small size of the company"- Investor 1 (Public Investor).

Once the investment had been made, 3 out of the 18 interviewees used a data-driven tool to measure ESG aspects of their portfolio companies. One of them employs a platform for ESG reporting called "Worldfavor" (2023), while another uses "Upright Project" (2023) a similar platform. The third investor uses an SFDR-based template to report on specific metrics. The Upright Project (2023) assessment considers positive and negative impact in four dimensions; environmental, health, society, and knowledge. It also considers the EU SFDR principals of adverse impacts such as greenhouse gas emissions, energy consumption, EU Taxonomy alignment, and UN SDG alignment. The evaluation covers the entire value chain, including upstream, downstream, and internal aspects.

VCs that have committed to the SFDR as an article 8 or 9 funds on the other hand are required to make their portfolio companies report on ESG metrics at a post-investment stage. Ultimately, there are no standard metrics or frameworks used by all investors. Each investor rather has their own way of evaluating sustainability aspects in potential investments.

4.8 Environmental aspects are given priority over social and governance aspects

The investors interviewed generally prioritized environmental and governance aspects higher than social aspects within the ESG spectra.

"We focus on truly positive impact on the environment rather than just ESG reporting requirements that some institutions might push for. In terms of social and governance impact, we look at these aspects, but we don't really measure specific progress and we don´t prioritize it." – Investor 14 (Private- Bank fund).

Investor 14 clearly has a focus on environmental aspects prior to governance and social aspects. Even though they do have social aspects in mind both prior and after the investment decision has been made. Interviewee 8, a management consultancy firm specialised on venture capital agrees to the conclusion that most investors focus on especially the environmental aspects among the ESG criteria.

"The investors mostly focus on the environmental aspect among the ESG spectra. But gender diversity is also a thing. In terms of social impact, every investor has their own way of measuring and tackling that. They sometimes work on the social aspect by encouraging the companies on certain aspects or sharing inspirational speakers that inspires the start-ups to take governance friendly decisions. They do stuff that is not necessarily measurable, but that still is not yet a common practice." - Interviewee 8 (Management Consultant with focus on VC).

Most investors showed a keen interest in reducing CO2 emissions, nevertheless, two investors stood out for prioritizing social aspects in front of sustainability and governance. Investor 17 (Private, Health-tech) invest only in clinical-stage med-tech companies, and therefore consider themselves as a company strongly focused on the social impact rather than environmental aspects for their investments.

"We try to minimize air travel and minimize the negative environmental impact but we also know that our impact in this area is limited so our focus is the social aspect through the number of lives saved or number of people who will get access to specific medicine or medical equipment through the potential investment. We do have scientific metrics like the potential number of patients that we can help or how are we saving the patient's life through the technology we invest in, but we also include other metrics that are more company specific, like equality" – Investor 17 (Private Health-tech Investor)

Investor 17 is however not a regular investor as they focus specifically on medtech companies, and by nature therefore has a unique focus set from the beginning.

"We focus on the social aspect. The E&G are the sort of things we want to tick the boxes on so that we are not the negative side."- Investor 11 (Private VC)

Investor 11 also prioritizes the social aspect, while acknowledging that the environmental and governance aspects are mandatory steps that they consider by default. Overall, while most investors emphasize environmental and governance sustainability, some are slowly recognizing the importance of the social aspect in their investment decisions.

5. Analysis

In this chapter the the empirical findings are being analysed through the methods of choice, and anchored within the theoretical framework that is presented in chapter 2. The chapter is structured around the same themes presented in the previous chapter to provide the reader with a relatable and easy to read structure.

5.1 Business feasibility is a deal breaker

Hill (2020) describes some of the common investment approaches that consider sustainability factors, such as socially responsible investing, impact investing, ethical investing, thematic investing, SDG Investing and ESG Investing. These different investment approaches all have their own angle of prioritization of sustainability goals. What´s common for all these however is that to achieve the impact, they consider business feasibility, scalability, and financial viability in parallel with their individual ESG angel. This was something that all the interviewees could agree to as well. That no matter of their own unique angle of impact focus, they considered the viability of the business, its scalability and opportunity to eventually make money a crucial aspect to proceed with the investment. Investor 1 and 3 for example say specifically that they would not consider the target company interesting unless they think that the team would be able to and intends to scale the business to a larger corporation. Perhaps the biggest explanation for this is because without the start-ups ability to financially stand on its own, it would struggle to scale and thereby create a large impact within the ESG area it is focusing on. In this sense, McLachlan and Gardners (2004) definition of traditional investing, where financial viability is the only criteria for the investment, can be seen as the foundation for all types of investments. The other investment models described by Hill (2020), that to a high degree are adapted by the investors interviewed within this research, have all the traditional investment criteria in mind, but add other aspects to the screening process as well. When evaluating whether the business would be financially viable and scalable the investors highlight the importance of the founding team. As the early-stage start-ups evaluated in the

screening process are often more dependent of the founders than the business itself. The same conclusion was drawn from Block et al. (2021) who intended to answer the question of “what criteria matter when impact investors screen social enterprises?”. The result from the 179 participants was, except for the importance of the societal problem also the authenticity of the founding team, and the venture’s financial sustainability. While the authenticity is more indirectly linked to the business feasibility, the venture´s financial sustainability can me directly linked to this theme.

5.2 Gender balance in management is prioritized

Among the social aspects considered within the ESG spectra displayed by Syed (2017), diversity, with an extra focus of gender balance at management level was the most prioritized one among the interviewees. Pitchbook (2022) discovered that 27% of the 522 investors that they interviewed globally mentioned diversity and inclusion when asked about what categories of impact investing, they focus on. The same theme could be found from the interviews performed within this research where especially all the governmentally backed investors displayed a strict attitude towards the gender balance at the level of the board or team of the company. Even though it´s positive with gender balance among the founders at the time when the screening is being performed, a non-diverse team can be overseen if there is a clear strategy for how the gender balance at the management level should be achieved in the future.

There was a slight difference between governmental backed investors and the private ones where the governmental backed investors had a stronger focus on the governance aspect by putting an emphasis on the gender balance at the level of the team and/or board from a regulatory perspective. Private investors, however, focused on the governance aspect more on the added value that gender balance at management level could bring. The private investors do however not just require a gender balance at the level of the board/team to “tick a box”. They are more into finding the right people for the team while ensuring that the gender balance is there. For the private investors the diversity and gender balance are being implemented to improve the management of the company by bringing different perspectives to the table when evaluating different options in the decision-making.

5.3 Greenhouse gas emission is a common metric for investors

Wang. C. et al (2022) pointed out the lack of accurate data at the start-up level as a challenge

for investors that through data driven methods screen for companies positively contributing on ESG factors. This was confirmed through the interviews as some investors said that they are not being strict with metrics due to the lack of comparable data. Some also mentioned that they are still searching for the right metrics to use as their isn´t any clear consensus of what to measure and compare between the different target companies. This challenge however wasn´t as applicable in the case of greenhouse gas emissions. Most investors interviewed look both at the pre and post investment stage in the screening process when evaluating greenhouse gas emissions. Some investors even had specific funds especially focused on companies that intend to reduce greenhouse gas emission, where CO2 was the most common metric to use. Measurement and reporting of greenhouse gas emissions is a well-established practice in environmental management and sustainability with standards and guidelines for measuring emissions. This incentivises companies to report on their emissions as part of their sustainability strategy. Therefore, it´s not surprising that investors focus on the metric of reducing greenhouse gas emissions when evaluating the impact of their investments.

5.4 SFDR regulation and reporting awareness is positively viewed from investors

To prevent investment funds from labelling themselves as “green funds”, EU set up the SFDR regulation as part of the EU Taxonomy act where strict rules apply to companies claiming to be “green”. This has incentivised many investors to report on different sustainability metrics, partly because raising capital can become easier once the fund is labelled as “sustainable” or “green” (Eurosif, 2022). The result of this is that the investors that cope with the SFDR regulations must consider a wide range of ESG related reporting areas when investing in companies, but also after the investment has been made. To make the screening process of the ESG criteria easier, but also the potential ownership of the target company more seamless, the investors are considering companies that have the knowledge and expertise of SFDR. That way they save time and effort that otherwise would have been spent on asking for the numbers from the company that is needed for the reports. Another reason for targeting companies that have expertise in sustainability reporting is that at a future state, when the investor intends to exit the company to another investor or an IPO, those investors will be just as, or even more demanding in terms of sustainability reporting.

5.5 Focus on one specific impact goal

Ebrahim and Rangan (2014) suggest that start-ups should clarify their operational mission, as well as specify the scale of the problem it intends to solve, and how much of that problem they intend to solve. That precisely matches what the investors interviewed pointed out. More specifically investor 1 and 13 highlighted the importance of start-ups to be specific regarding the impact it intends to generate by setting up quantifiable targets and measurable progression on that specific main goal. Ebrahim and Rangan (2014) further suggest that the start-up needs to understand what measures the investors they intend to pitch for are considering when evaluating the impact of target companies. This not only makes it easier for the investor in the screening process to evaluate the impact it generates with its invested capital, but also sends signals from the start-up to the investor that the funds are taking impact and sustainability seriously.

So and Staskevicius (2015) means that start-ups should focus on the aspects considered by investors in the first phase of the model the impact evaluation model they've presented in their research. This includes evaluating the expected return in terms of impact that the investor can expect in contrast to the costs of investing in the target company discounted to today's value. To be able to do so, So and Staskevicius (2015) suggest that the investor need to define the scope of the impact it wants to achieve by describing the issues and stakeholders that the target company is addressing. This goes hand in hand with the interviewed investors suggestion that start-ups should focus on one specific impact goal and be clear with how they will reach it. For the investors to be able to achieve So and Staskevicius (2015) definition of a measurable scope they need to gather these numbers and goals from the target companies to be able to compare and contrast them. When this is done they will be able to make a well-informed and rational decision regarding what target company to proceed with along the investment process.

5.6 Sustainability does not determine the valuation

Mansouri and Momtaz (2022) conclude that the investors prioritization of sustainable companies creates competition among investors to acquire impactful companies, which eventually creates a better negotiation situation for the startups. This higher demand then pushes the price of sustainable companies up. Amel-Zadeh and Serafeim (2018) furthermore found that being transparent with ESG criteria and following up on sustainability metrics lower costs of capital for companies raising capital. Which is also associated with higher valuation of the company as the cost of capital is an important aspect when valuing a company based on

WACC (weighted average cost of capital) (Brealey, Myers and Allen 2007). Mansouri and Momtaz (2022) research concluded that a one-standard-deviation increase in ESG measurement according to their study is associated with a 28 % increase in the funding amount.

Another aspect that pushes the valuation of sustainable companies is the EU Taxonomy regulation that potentially shifts the valuation of ESG compliant businesses by raising the investment interest in specific sectors through tax advantages and labelling of certain companies and investors as "green" (Upright Project 2023).

Considering the previously mentioned aspects, it might have been expected that the interviewees would have responded that a sustainable startup, that keep track of ESG related metrics, and has a positive impact on the society would be higher valued than a company that does not tick these boxes. The results from the interviews was however not aligned with each other. Many investors said that the sustainability status of a target company does not affect the valuation of it at all, while others did not want to answer the related question as they thought it was irrelevant. The majority of the interviewees said that they can´t say specifically how the sustainability status impact a company's valuation, since it´s rather a yes or no for them when investing where they consider the company being sustainable enough or not. If the company furthermore is sustainable enough, they do a valuation of the company, but if it does not meet the investors requirements, they don´t proceed with the valuation of the company.

While sustainability is an increasingly important consideration for investors, its impact on the valuation is not yet be fully understood. As the focus on sustainability continues to grow, it is likely that investors will pay closer attention to sustainability metrics and their relationship to start-up valuation.

5.7 ESG Due Diligence exist, but rarely strict and quantitative

All the investors interviewed, public as well as private, have integrated ESG into their due diligence process. Most of the investors based the ESG, or impact aspect, on common sense where they made their own judgement using common sense when evaluating a target companies impact. A company that provides micro loans to poor families in a developing country would for example be considered having a positive impact.

The investors that didn´t consider themselves as impact investors, that rather purely focused on the profitability aspect still cared about ESG aspects, but rather made use of the negative screening method (Amir El Zadeh & George Safreim, 2018). This resulted in the investor

excluding certain areas such as coal, tobacco, and oil due to its negative impact as a result of its business. This was for example investor 5 and 15. The governmental institutions interviewed, however, were not as strict about the current situation regarding measuring the sustainability. They rather prioritised and valued the intention of the team and their strategy towards making the change in the future when larger scale is achieved.
In terms of metrics, except from the gender balance or emissions reduction impact, most investors did not have specific numbers they looked at when making the investment. This implies that investors consider more of the general picture of the company and the feasibility of the business model and its impact evaluated by common sense rather than evaluating it using specific metrics.

The time dimension, of the investment process was discovered to play an important role for what types of aspects that were considered by the investors. Some aspects are considered at some stages of the investment process but not at others (i.e Pre-Investment Stage Vs. Post Investment Stage). The empirical findings resulted in a model divided between the different investment stages. Under each investment stage a list of aspects considered within the specific investment stage are being listed. Aspects that are considered within both investment stages are also listed in between. The business idea, making use of negative screening and evaluating the intention and strategy of the team were often mentioned at the stage of pre-investment. Setting sustainability goals, reporting on progress as well as reporting on measurable hard metrics was mostly discussed during the post-investment stage where investors expected the company to report on their progress.

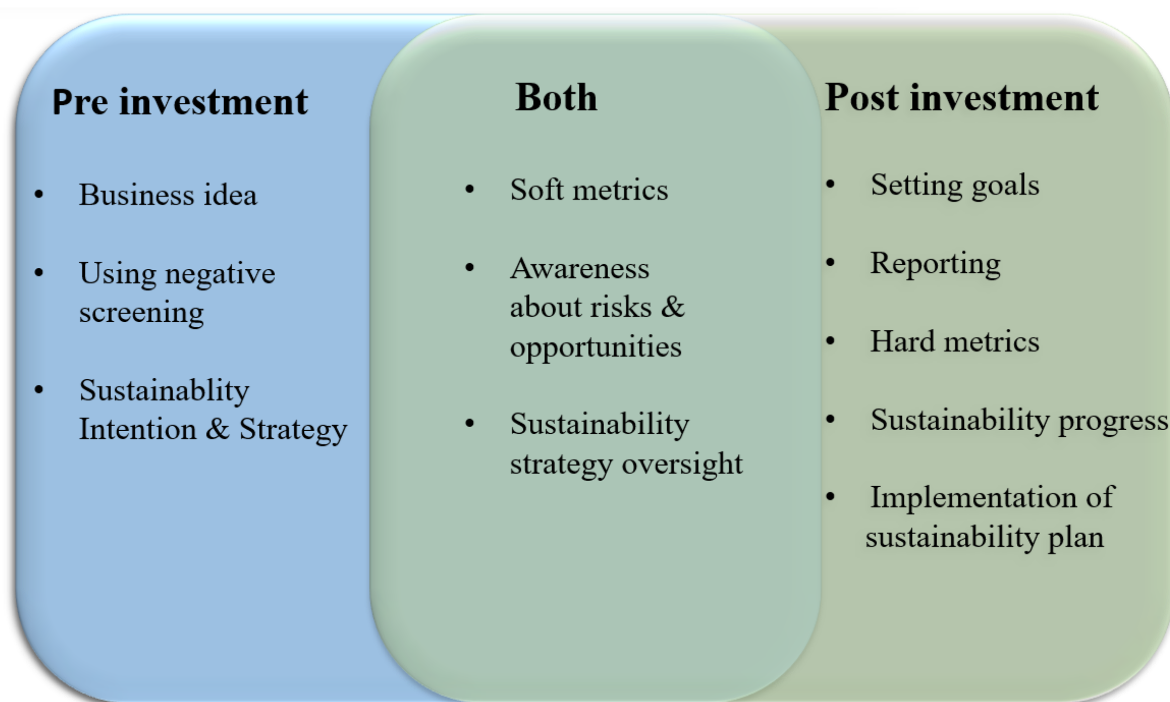

Figure 5- Due Diligence requirements per investment stage

Source*: Made by the researchers*

5.8 Environmental aspects are given priority over the social and governance aspects.

The higher focus on environmental rather than social and governance impact might be related to the lack of clear and quantifiable ways of measuring the social and governance factors. This was also indicated Wang. C. et al (2022) that described the challenges investors face related to investing in impactful startups. It was primarily the social aspect that was confirmed to be difficult to measure, and therefore resulting in less available data and thus comparability challenges amongst firms. Environmental factors such as carbon emissions and water usage can be easily tracked, while social factors such as employee satisfaction and customer loyalty are more subjectively quantified. This leads to relatively undeveloped reporting obligations and restrictions within the area, resulting in the investors not being as eager to target companies based on those criteria.

While most investors emphasize on environmental aspects, some are beginning to recognize the importance of social and governance aspect in the screening process of new investments as the area matures over time.

6. Discussion

The objective of this chapter is to provide a summary of the theoretical and empirical findings and to analyse their interconnections. The results of the research will be examined in relation to the research questions, with a structure that mirrors the research questions order. This ensures a well-organized presentation of how each question is handled and responded to.

RQ1 What factors are investors evaluating when considering the impact of target start-up companies?

The investors highlighted several factors considered when evaluating a start-ups impact on environmental, social or governance aspects. Great focus was put on the target companies' way of working with impact and the risks and opportunities associated with it. Due to the SFDR regulations set up as part of the EU taxonomy, many investors want the target companies to have knowledge about these reporting methods because it enables report on specific metrics if demanded from the investors. From an environmental perspective, focus was mainly put on greenhouse gas emissions and the judgement by common sense of the business impact on the environment, without the need for certain quantitative measurements. From a governance perspective, gender balance at management within the target company was often highly prioritized. The social aspects, however, did not receive as much attention except from a developing country-focused investor and one med-tech-oriented investor which by natural reasons has a large social impact due to the investment focus.

Sub-question 1: How do these factors affect the decision of investors when evaluating potential investment cases?

The empirical findings revealed a few key aspects commonly considered by investors that together create an image of a target companies impact and sustainability. Start-ups that attempt to tackle many different impact areas at the same time are often being judged for greenwashing. It might also result in the investors thinking that the resources could have been spent more

wisely by prioritizing one specific area of impact. To focus on a specific impact area demonstrates a real intention and determination of the team to make an actual impact. Having awareness of risks and opportunities and readiness to take action to mitigate these risks or exploit the opportunities associated with ESG aspects is highly evaluated from the investors.

Many investors showed interest in seeing the measured impact of the start-ups through specific metrics, especially the ones related to CO2 emissions reduction or the gender balance within the team. They explained however that not being perfectly sustainable now is not a deal breaker. Showing future intentions supported with a clear strategy and the right people that are responsible of the oversight of the set plan is of higher importance.
The main reason why the investors showed an interest for ESG impact is because of regulatory risks, tax advantages and future shareholders demands.

Sub-question 2: How does the 'Sustainability label" affect the valuation of a start-up?
When it comes to the valuation of a startup, investors were not able to directly link sustainability aspects of the startup to the valuation. The general perception of investors regarding this question was that it a startup demonstrating positive impact might have influence the valuation positively as it is an indication of the team's thoughtfulness and awareness of the general benefits of being sustainable as well as the financial benefits associated with it. No conclusion could however bee drawn on this question as the investors were not able to link the valuation directly to sustainability without the full picture of the companies other aspects.

6.1 Limitations

The time constraint for this study caused not more than 18 interviewees to respond to to the questions set up by the researchers. As such, the validity of the conclusions drawn from this research can be questioned. The aspects presented in the conclusion should therefore rather be seen as material that can be used by scholars for future studies within the topic. In addition, such a study should also research investors outside of the Scandinavian borders and investigate the investors views on the questions in another market. An interesting study would be to compare the Scandinavian investors views with the ones on another market, something that was not possible within this study to the time constraints.

6.2 Directions for further research

Since this research focused mainly on Scandinavian investors and specifically Swedish ones, future research could explore other regions and discover if there are differences among different regions and how startups can make use of these differences for an easier fundraising. There is also potential to use the results of this research in further developments of sustainability assessment methodologies where one would discover how investors can make better use of existing sustainability evaluation methods and measurement tools to make more data driven and less subjective decisions when evaluating the impact of a target company. Another topic for potential research would be to discover what would be smart from a founders perspective to focus on. As resources are often scarce, one must take the financial and time aspects in consideration when deciding what to prioritize. Also constructing quantitative research would be suitable as that would complement the finding of this qualitative research.

7. Conclusion

This research shows that the area of impact evaluation from an investor perspective is a relatively unexplored area where a lot of development will occur in the coming years as the regulations change and the area matures. The aim of this research was to make the area of sustainability evaluation clearer, both from a startup perspective that intends to raise capital, but also to extend the knowledge of how investors are working practically with ESG questions while making investment decisions, especially in the screening process. The key findings of this research are the following themes, all considered among investors in the screening process: Business feasibility is a deal breaker for investors,
gender balance in management is prioritized, greenhouse gas emission is a common metric for investors, SFDR regulation and reporting awareness is positively viewed from investors, focus on one specific impact goal, sustainability does not determine the valuation, ESG due diligence exists but r arely strict and quantitative and lastly, that environmental aspects are given priority over social and governance aspects. A more detailed description of these aspects can be found in the empirical findings and analysis section.

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9 Appendix

8.1 Interview Guideline

Interview Guideline	
Main Questions	**Sub / Follow up-Questions**
What is an Impact fund for you?	Would you consider your fund being one?
What sustainability aspects do you evaluate in the screening process?	How? How Important would you consider these ones being? Why do you consider sustainability aspects when taking investment decisions?
Any special frameworks or metrics you look at when evaluating the sustainability aspects of a target company?	
Do you follow up on any sustainability metrics for your portfolio companies?	Any framework that you use for that?
If you would be a founder of a startup that intends to motivate it´s sustainable, how would you motivate this for potential investors?	
How does a startup's sustainability status impact your valuation of it?	
How do the following aspects affect your perception in the screening process?	- Sustainability rewards - The product/service affecting "ESG-factors" positively. - The product/service is in a less "responsible/ESG-friendly" industry such as oil, but does it in a better way than the competitors. Or are highly prioritizing "Social/Governance" aspects as they lack environmental ones? - The founding team has a background of sustainability-related experiences and expertise. - E,S or G highest priority?
Anything else you´d like to add?	
Is there anyone you know that you think we should interview?	- Anyone you would be able to refer us to?

8.1 Thematic Analysis

Thematic Analysis		
Interviewee	**Quote**	**Theme**
Investor 3 (Private VC)	*We are more interested if the business idea works, best workplace rewards and similar doesn't really matter that much. Impacting ESG factors is considered positive, but we put more focus on making money, so it doesn´t matter that much. As long as the business is not bad for the environment, and they have plans that they report on progress we are ok. Businesses in sectors such as oil, gas and tobacco however wouldn't be so attractive*	**Theme 1: Business feasibility is a deal breaker for investors**
Investor 5 (Investment company)	*We don´t look at any specific boxes or frameworks, rather common sense. We do however want to be able to quantify the progress as it´s linked to the financial targets. For example, reduced C02, amount of energy produced, consumed or such. Times when companies only can be sustainable without making profit is bye. It is however still a focus on sustainability, as it can drive profit in the long run. They focus on changing something bad to something that´s better. Not like investing in a better oil company that the ones existing, but solutions that improve society when they sell more. Such as wind turbines.*	
Investor1 (Public Investor)	*We do not invest without thinking that the team has the ability to scale the idea, which will thereby enable a larger impact in itself. The strategy and the future intentions of the team are something we look into as the startups has no history of ESG actions yet".*	
Investor 15 (Private Investor)	*The most important aspect is the founders' or boards reliability, and trustworthiness that they will succeed with the development of their vision and business.*	

Investor 11 (Private VC).	*We don´t use any specific metrics to measure for gender diversity, but it´s something we always consider when evaluating potential investments. It can however be okey to not have a diverse team from the very beginning of the startup, as long as there is a clear strategy and plan for achieving this gender diversity, especially at the management level, in the future. The reason why we target start-ups with diverse team members is because you must have a diverse broad team to be able to target a broad audience of customers. This is the reason why we include the diversity aspect in the term sheet for every investment we proceed with.*	**Theme 2: Gender balance in management is prioritized**
Investor 3 (Private VC)	*Gender and carbon footprint most prioritized, most important is to measure this and record it.*	
Investor 10 (Private VC)	*We are trying to onboard our portfolio-companies on these types of regulation with metrics that handles policies for gender and diversification.*	
Investor 9 (Angel Investor)	*Make sure to not exaggerate some aspects like "number of women" just to tick some boxes.*	
Investor 15 (Private Investment Company)	*Don´t consider other aspects related to governance, such as diversity on the team. Even though it would be positive with diversity.*	
Investor 15 (Private Investor)	*We don't, expect from CO2 impact measurement.*	**Theme 3: Greenhouse gas emission is a common metric for investors**
Investor 14 (Private Bank Fund)	*Especially one of our funds has a focus on greenhouse gas emissions and boundaries transgression.*	
Investor 17 (Private, Health-tech Investor)	*Knowledge about SFDR is a good sign as for us it is a bit of a pressure as VCs to report on that. If a company can show familiarity with this kind of reporting and comfort with reporting on that, that can comfort us as investors.*	**Theme 4: SFDR regulation and reporting awareness is positively viewed from investors**
Interviewee 8 (Management Consultant with focus on VC)	*The sustainable finance disclosure regulation (SFDR) is quickly becoming the most common approach to measure sustainability metrics of a portfolio. It includes several indicators for adverse sustainability impacts.*	

Interviewee 8 (Management Consultant with focus on VC)	*The early-stage VC funds that do not extensively work with sustainability may be aware that sustainability will become important at the stage of exit, or an IPO. Some aspects may signal to an investor that the company is managing their sustainability risks and impacts: A sustainability strategy which considers negative impacts, material risks, coping with sustainability reporting metrics such as SFDR, and having a person responsible for the sustainability strategy.*	
Investor 11 (Private VC)	*During the initial workshop we set goals and then we follow up. We try to make them understand that if they don't start from the beginning it would be difficult to start later.*	
Investor 1 (Public Institution)	*What we evaluate is the quality and strategy to go towards that specific goal. We evaluate the application forms: Does the company really know what they are doing, and do they have the intention to execute the plan?*	**Theme 5: Focus on one specific impact goal**
Investor 9 (Angel Investor)	*I prefer to see the focus on the ones where we really make an impact instead of talking about all the SDG goals.*	
Investor 13 (Private VC)	*Focus on specific questions, not everything. Have a clear story that´s backed by data that you also clearly can measure so you can prove and support how much good you´re saying that you are doing. This way you show that you´re not just pretending, but that you genuinely care. And not just that the impact aspect is for example 5% of the business.*	
Investor 9 (Angel Investor)	*The impact should be real. It will not impact my valuation of it but my evaluation of it. I don't like greenwashing.*	**Theme 6: Sustainability does not determine the valuation**
Investor 16 (Private Investor)	*As all companies we invest in have a positive impact by default it is difficult to answer this.*	
Investor 17 (Private Health-tech Investor)	*It's difficult to say what impacts the holistic value of the valuation of a company. But if a company is doing bad we would of course not consider it.*	

Investor 13 (Private VC)	*Every year we follow up on sustainability aspects. And for the ones categorized as "impact companies" we follow up on metrics such as number of customers helped or loan amount provided to people in a developing country.*	**Theme 7: ESG due diligence exists but rarely strict and quantitative**
Investor 5 (Investment Company)	*We have no specific boxes or frameworks; we use rather common sense.*	
Investor 10 (Private VC)	*We try to evaluate the business in the due diligence process and identify the red flags but we have been looking into more metrics that could be used according to the company's field. Like energy use or water use.*	
Investor 1 (Public Institution)	*We highly consider the willingness of the team and the strategy towards making more ESG impact in the future and it doesn't matter if they haven't started at the moment of the investment due to the often times small size of the company.*	
Investor 14 (Private-Bank Fund)	*We focus on truly positive impact on the environment rather than just ESG reporting requirements that some institutions might push for. In terms of social and governance impact, we look at these aspects, but we don't really measure specific progress and we don´t prioritize it.*	**Theme 8: Environmental aspects are given priority over social and governance aspects**
Interviewee 8 (Management Consultant with focus on VC)	*The investors mostly focus on the environmental aspect among the ESG spectra. But gender diversity is also a thing. In terms of social impact, every investor has their own way of measuring and tackling that. They sometimes work on the social aspect by encouraging the companies on certain aspects or sharing inspirational speakers that inspires the start-ups to take governance friendly decisions. They do stuff that is not necessarily measurable, but that still is not yet a common practice.*	
Investor 17 (Private Health-tech Investor)	*We try to minimize air travel and minimize the negative environmental impact but we also know that our impact in this area is limited so our focus is the social aspect through the number of lives saved or number of people who will get access to specific medicine or medical equipment through the potential investment. We do have scientific metrics like the potential number of patients that we can help or how are we saving the patient's life through the technology we invest in, but we also include other metrics that are more company specific, like equality.*	

Investor 11 (Private VC)	*We focus on the social aspect. The E&G are the sort of things we want to tick the boxes on so that we are not the negative side.*	