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Preliminary insights from interviews with impact investors

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1. INTRODUCTION

1.1 Objectives and background

With €9 billion of invested assets in Europe in 2012, the impact investment market can no longer be described as in its infancy¹. It is a burgeoning sector of the financial markets and gaining in recognition as well as scale. With such promise for achieving social returns, now is an appropriate time to consider how these impact investors are approaching impact measurement. How much impact is actually being achieved, and what effects can we really expect to be assessed?

This paper is the second in a series of LSE publications on measuring non-financial returns to impact investing, as part of a project supported by the European Investment Bank University Research Sponsorship (EIBURS) Programme. Its aim is to draw out points of convergence and divergence in approaches to impact measurement, based on information derived from a series of interviews with impact investors conducted between July and November 2013.

Our starting point for analysis is set out in the first paper in this series entitled 'Measuring impact and non-financial returns in impact investing: a critical overview of concepts and practice' (Reeder and Colantonio, 2013). This emphasised how impact investing involves the combination of social, environmental, governance and financial goals in the application of [financial] capital, underpinned by the measurement of the impact generated by the actual investment process. The paper put forward six key propositions which the interviews set out to test and explore. These included:

- There are two different forms of measurement practice culture, with 'system builders' aiming for assessments that are as objective, robust and quantified as possible, and 'case by case' advocates wishing to produce assessments focused on the specific 'here and now';
- Concepts of what should be measured and covered within 'impact' and 'non-financial return' or 'wider value' are far from settled;

¹ page 23 of European SRI study 2012 (2012), Eurosif

- The conceptual case for creating a single metric of value is highly contested;
- Conceptual frameworks have often downplayed the category of risk;
- Some influential systems of measurement impact have a mixture of 'subjective' as well as 'objective' measures;
- There are observable tensions between an organisation wishing to tailor its measurement to its own situation, and the constraints imposed by a standardised framework.

A further issue raised in the initial working paper was that of divergent practice between pre- and post- investment assessment of social and environmental returns.

1.2 Interviews with impact investors

In order to explore and address these propositions further, we conducted a series of interviews of investors in the fields of the environment; social enterprise; microfinance; and social impact bonds financing (some investors covered more than one category). The sample of interviewees was based on recommendations for well-established impact investors who:

- (i) Manage investment funds with the explicit aim of generating both a financial and social return. The level of financial returns varied significantly across investors, though none saw any necessary conflict between seeking to generate both a social and financial return;
- (ii) Are based in the European Union; and
- (iii) Are active contributors to the impact investing debate.

In addition, our sample was chosen to incorporate investors with a blend of motivations. Some impact funds were backed by public sector funds, charitable foundations or high net worth individuals and philanthropists, and tended to be more willing to take a lower financial return.

Others were backed by institutional investors, corporates or pension funds, and tended to seek a higher financial return. We also included two venture philanthropy organisations who share a focus on supporting sustainable organisations to achieve social return but whose ‘investments’ are in the form of non-repayable grants.

The chosen investors were asked to explain the social and financial goals of their organisations, explain the role of impact measurement in their investment process, discuss their measurement methodology, and recommend ways to improve the state of impact measurement. In total, interviews were held with 15 organisations – Alterfin, Ashoka, Bank of America Merrill Lynch, Big Issue Invest, Big Society Capital, Bridges Ventures, DOB Foundation, Impetus – Private Equity Foundation, Phi Trust Partenaires, Quadia, responsAbility, Social Finance, Social Venture Fund, Triodos Investment Management, and Triple Jump.

1.3 Structure of report

The remainder of this report has been structured into two main parts. Section 2 discusses the approaches taken to impact measurement, drawing on evidence gathered through the interviews; and Section 3 draws conclusions on the propositions set out above.

2. APPROACHES TO IMPACT MEASUREMENT

Impact measurement can take place within different stages of the investment process, as shown in figure 1 below.

Figure 1 Stages involved in the investment and impact measurement process



This section considers a number of questions on impact measurement throughout these stages in relation to the following specific propositions:

- What forms of impact measurement terminology were used by the interviewees?
- What were the main dimensions of ‘impact’, from their perspective?
- How were the ‘impact’ themes and domains conceptualised as a preliminary to undertaking measurement?
- What were the views on forming a single metric of impact and/or integrating financial and non-financial return?
- To what extent were ‘causal links’ between the investment activity and its impact examined?
- What group and network arrangements to build up and share knowledge or other resources are most useful?
- What different ‘mind-sets’ were observed in respect of measurement?
- To what extent is pre- and post-investment impact assessment carried out effectively?

These issues are considered in the remainder of this section in turn.

2.1 Terminology used - outputs, outcomes and impact

An important distinction in impact measurement is between the outputs² ; outcomes³ ; and impact (changes in outcomes)⁴ that result from actions funded by the investment.

Outputs tend to be easier to measure, but neglect the value to the beneficiary. And outcomes are generally easier to assess than the change in outcomes that is due to the value creator, with the task of assessing attribution to a reasonable standard of robustness often being difficult.

All of those impact investors interviewed for this paper were content to use a terminology of outputs, outcomes and impact. It is worth noting that there is the same consistency does not exist in the frontline field of impact measurement. Social analysts and researchers often use a broader range of terminology. For example, advocates of the Outcome Star measurement tool prefer an alternative terminology of ‘end outcomes’ (the

2 The relevant activities completed as part of the intervention (for example, the number of loans approved, service users who complete a training course, counselling sessions completed, sales made etc.).

3 The direct change in the beneficiary that has been caused by the intervention (for example, a would-be entrepreneur obtains access to finance).

4 The change in those outcomes (for example, an entrepreneur given additional loan financing is able to expand their business and move out of poverty).

final outcomes that the beneficiary receives), and ‘distance travelled’ (which relates to the change in outcomes) (MacKeith, 2012).

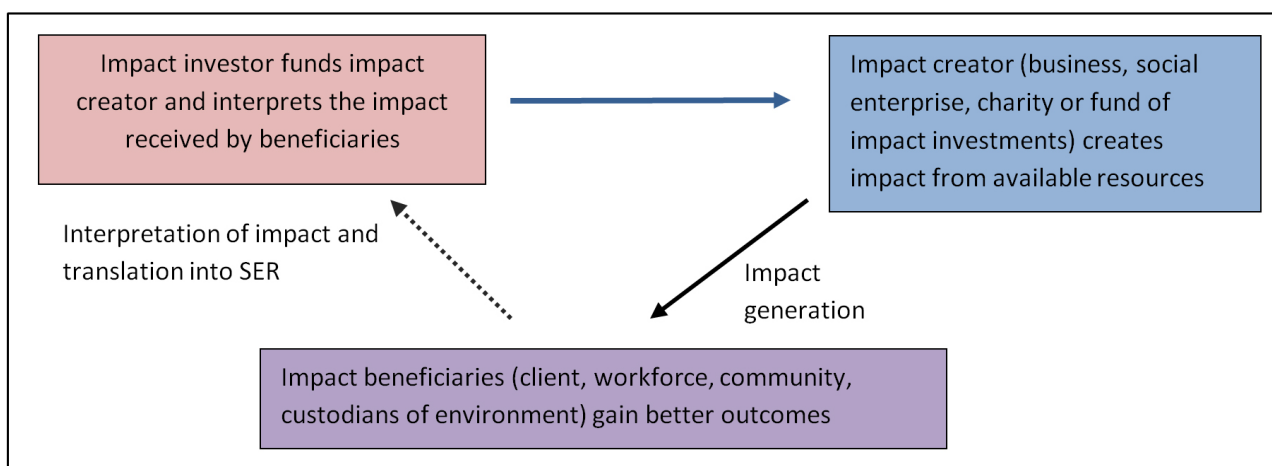
The distinction between outputs and outcomes raises two themes which are central to understanding an investor’s approach to impact measurement. Firstly, a preference for judging performance in terms of outcomes, not outputs. Secondly, an attempt to assess impact (also known as distance travelled, or value added), in terms of changes in outcomes. The extent to which they have and have not been assessed by the various impact investors is covered in more depth in the discussion on causal links between activity and outcomes in section 2.7 of this paper.

2.2. Dimensions of impact

Bridges Ventures has an approach to outlining the elements that comprise impact as follows:

1. Scale – broadly the number of people affected (rated on a scale from 1 to 3);
2. Depth – a subjective assessment of the degree of impact on their lives (rated from 1 to 3);
3. Systemic impact – the wider effects that the scheme may have, such as whether the basic ideas are picked up by entrepreneurs in other countries (also rated on a scale from 1 to 3).

Figure 2 Three main roles within impact investing



Many other interviewees had similar distinctions. Big Society Capital, for instance, currently assesses the extent to which change will be delivered according to the 'Depth' of impact; the 'Breadth' of impact; the extent to which 'Systemic impacts' will be delivered; and the effect on frontline capability. AUM microfinance considers impact in terms of 'Reach', 'Efficiency and Effectiveness' and 'Client protection'.

Ashoka take a slightly different but related perspective, looking for social entrepreneurs that have a systems-changing new idea; that are highly creative in goal setting and problem solving; that have high entrepreneurial skills; and that have 'ethical fibre'.

A number of investors often argued that assessing scale involves not just counting the number of people supported, but also whether they are the 'right' (or suitable) target group for the activity funded by the investment. For example, several microfinance investors valued the PPI (progress out of poverty index) to assist in effective targeting.

The dimensions of 'Scale' and 'Depth' relate to direct effects on beneficiaries; 'Systemic Impact' relates to wider, indirect effects. Although only four interviewees explicitly mentioned systemic effects, all others touched upon it in discussion in some way or other.

Discussions on the concept of 'wider, indirect effects' included suggestions that it relates to such themes as demonstrating the effectiveness of a broad category of idea; outlining new forms of organisation; showing new types of relationship between elements of a system; and challenging widely held norms and prejudices. Especially for an intervention which is not yet mainstreamed, some investors seemed willing in certain circumstances to trade off measurable direct impact against immeasurable long term wider effects.

One investor saw systemic change as coming through such factors as empowerment (proof of the effectiveness of changing the balance of power between client and enterprise); and prevention (evidence of the effectiveness of a long term preventative approach). They cited Shared

Lives Plus (an enterprise supporting people with learning difficulties to be cared for in the homes of local families, rather than in institutions) as a project that is having the effect of changing mindsets as to whether safe and effective care can be delivered to vulnerable people in a non-institutional context.

Similarly, Ashoka also see a crucial role of changing mindsets within their work. As they put it, in tackling a major social problem such as malaria, "it's not about how many mosquito nets you sell". Instead, for this illustrative issue, Ashoka would look for such factors as whether the fight against the disease is being enhanced more generally by new affordable approaches being promoted by markets; whether public policy and industrial norms are being reshaped; whether marginalised populations are being integrated into activities; or whether more people are being enabled to become social problem solvers.

Time scales are also seen as an important dimension. In particular, the majority of investors interviewed were interested in ensuring that impact was sustained beyond the period of their investment - as often the bulk of the social value of an intervention comes not from the direct beneficiaries this year or next, but the stream of beneficiaries that will come as the intervention reaches greater scale.

While most social enterprise investors were hopeful of such diffusion possibilities, microfinance investors had widely different perspectives. Those with socially minded underlying clients were keen to explore the boundaries of the intervention, experimenting with microfinance in more unexpected situations, such as rural environments. For others, the purpose of measurement was to help scaling as much as to understand direct impact; investors in this category were interested in finding out what measures would most help their attempts to scale their interventions.

2.3 Developing strategic impact goals

Largely, although investors focused on small number of social goals, these tend to be broad reaching (for example children and youth, environment) - few investors in our sample have defined specific indicators for impact within each goal. One exception is NESTA Investment Management. Although its fund targets impact in three areas – ageing well, children and young people and sustainable communities – it has clearly defined indicators within each area. For example, within ‘ageing well’ they employ three key indicators: ‘reduction in avoidable injury and premature deaths of older people’, ‘increase in the number of older people ‘enjoying a high quality of life’ and ‘participating in social, cultural and economic life’.

At a fund level, most investors either generated their own specific objectives for social impact, or had them provided for them by their clients - the ultimate source of funds. Only one interviewee mentioned any systematic attempt to seek guidance on what their impact goals should be, in this case from sector experts.

Smaller organisations we spoke to, who had closer relationships with private clients, were able to comment on what these clients found most appealing; one mentioned clean energy, sustainable consumption, green housing and food and nutrition in particular. Private clients tended to be attracted by a narrative that appealed to

their individual interests rather than impact data. None of the investors we spoke to consulted with beneficiaries in order to decide on or refine their goals. Two interviewees suggested that they picked some of their goals precisely because they were measurable, and therefore they believed that it would be easier to track progress against them.

2.4 Conceptualising and identifying impact themes and domains

For all interviewees, an essential step was to determine whether a possible investment was eligible to be included in their portfolio, as determined by adherence to a list of set criteria, which tends to cover such topics as geographical area where investments could be made, required size of investment, likely liquidity of the investment, and the mission of the potential investee. The latter aspect of mission (for example, financial inclusion, education or the environment) was a determining factor for qualification.

The question of confirming that the potential investee was aligned to the social mission of the fund was taken seriously, though such social missions can be defined in both specific and broad terms:

- Impetus-PEF concentrate wholly on getting young people from disadvantaged backgrounds into education, training and employment;

Figure 3 Different scenarios for different types of outcomes

	‘Core outcome’ required by those paying for goods and services	Not a ‘core outcome’ required by those paying for goods and services
Intrinsic to what the enterprise does	Impact - Government pays social enterprise for reducing reoffending in ex-prisoners	Impact - Social enterprise running a bakery provides job opportunity to ex-prisoners
Add-on activity for the enterprise		Law firm makes a charitable donation to a local free advisory service

- NESTA’s Investment Management’s policy is to focus on solutions to three key challenges – meeting the problems of an aging population; meeting the needs of children and young people; and enhancing the social and environmental sustainability of communities;
- Ashoka look to strengthen citizens’ abilities to solve problems, building a ‘everyone a change maker’ world;
- Big Issue Invest’s mission is to back sustainable social enterprises that help tackle poverty and inequality.

As consideration evolves into the due diligence phase, there continues to be emphasis on the organisation, management, process and mission of the investee. Particular attention is paid by most to the extent to which the investor would adhere to its social mission, reassurance that this mission is working well currently, and reassurance that this can be successfully delivered in the future. Most of our interviewees undertake consultation with local stakeholders, including the beneficiaries of the programme, in order to understand if a particular intervention works for them.

Several investors, among them Impetus-PEF and Bridges Ventures, generally create a logic model that specifies the impact to be expected from the activities funded by the investment; as well as a

conceptual model outlining the mechanism by which that impact will be achieved.

Big Issue Invest employs a scorecard approach with 16 criteria to assess a prospective investee. Understanding the potential for scaling the depth and breadth of social impact is a key factor in this assessment. However, so too is a consideration of how embedded the impact is into the organisation’s legal structure and underlying business model. This is considered critical for identifying the risk of future mission drift – an issue that is taken seriously; Big Issue Invest made a decision in one case not to continue with an investment where they felt the risk of mission drift as the organisation grew commercially would be too great.

In the interviews, Impetus-PEF highlighted a role for greater understanding of the ‘user journey’ towards better outcomes; while Bridges outlined their preference for a logic model that had the links between activities and outcomes supported by evidence, with the strength of these links evaluated in order to understand impact risk (as well as potential impact).

There was, however, a wide variety of approaches undertaken; some, such as NESTA Investment Management, rely upon a ‘narrative’ that described the key outcomes and how they would be obtained. By contrast, Social Finance has an inclination to utilise pre-existing quantitative

Figure 4 Two different forms of measurement practice culture

	Central task	Forms of human relationships
System builders	Produce a system that is as objective, robust, and quantified as possible	Expert to expert interactions designed to build up a body of knowledge Expert to audience communications designed to disseminate knowledge
Case by case	Produce an assessment that informs stakeholders of the full social value	Facilitator role played to draw out stakeholder views on key outcomes Focus is on the ‘here and now’, not on what other assessors have done in the past

modelling that showed statistical linkages, and statistical effects, upon outcomes that already had traction within a given sector.

Whichever process was used to conceptualise impact, the sets of measures used to determine progress on impact tends to be a mixture of measures of ‘ethical behaviour’ combined with achievement of hard-edged outcomes. One important instance for this is the set of key principles advocated by the ‘Social Performance Taskforce’ in respect of microfinance⁵:

- Employment creation and enterprises financed;
- Avoiding levels of too much debt;
- Social responsibility to the environment;
- Transparent and responsible pricing;
- Poverty outreach;

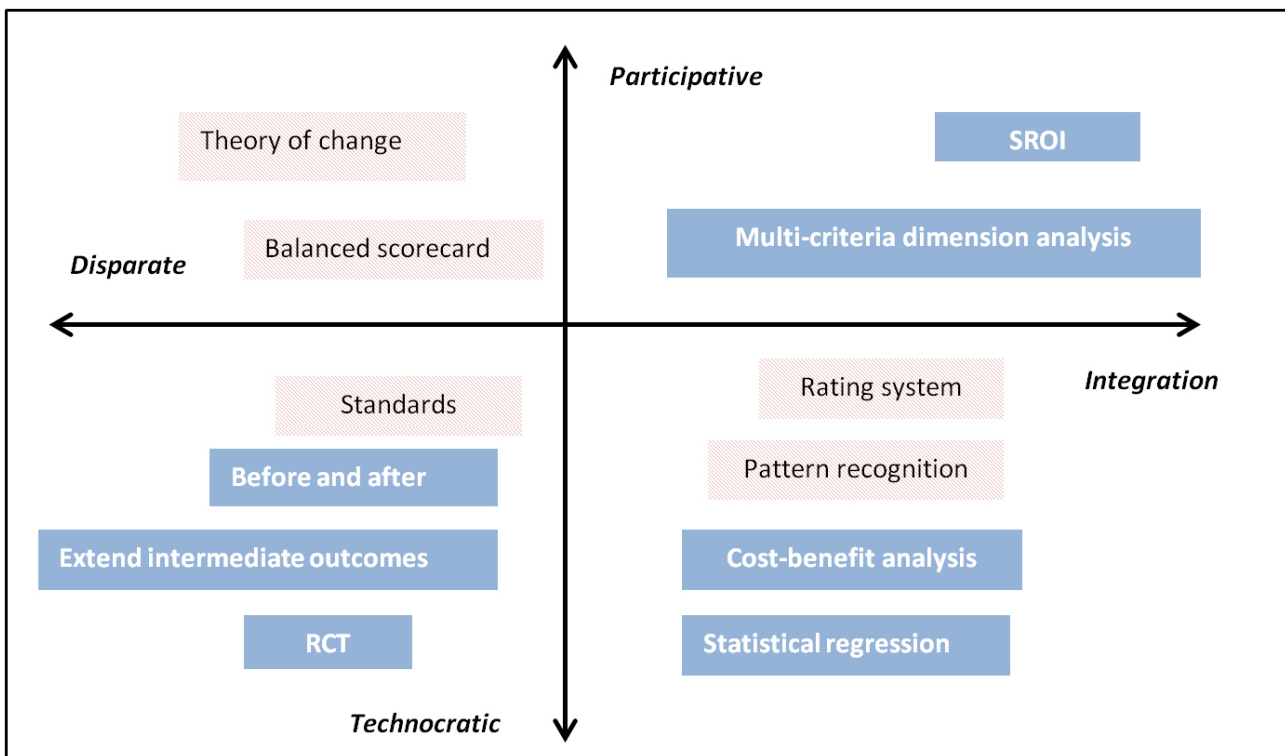
⁵ See <http://iris.thegiin.org/materials/microfinance-metrics-mix-and-sptf>

- Appropriate collections practices;
- Ethical staff behaviour;
- Mechanisms for redress of grievances; and
- Privacy of client data.

2.5 Assessing volatility in outcomes (outcome risk)

A new area for assessment that emerged from the interviews was that of ‘impact risk’. This is the measure of how likely an organisation is to remain faithful to the methods and approach that underpin an intervention’s success. Where an intervention has been well evidenced (and where external circumstances do not differ and substantially affect results), it may not be necessary to re-do all the same data gathering during the investment period, but instead monitor the systems and processes as indicators of whether

Figure 5 Characteristics of selected techniques for measuring impact



Key: No adjustment for changes in outcomes Assess changes in outcomes

the same approach is indeed being taken. Only two of the investors we interviewed raised the issue of impact risk, and stated that it is a key part of their assessment criteria.

One argued that a substantial minority of impact investors were at risk of replicating interventions with respectable financial prospects but poor evidence of impact, giving themselves easy to hit metrics that failed to capture the extent of real change for clients and society.

The other outlined their approach, which is to assess the likely volatility in outcomes with respect to the standard of evidence available, rather than using statistics of past (or modelled simulation) volatility. Three levels of evidence are used: if the logic chain of the impact creator is strongly supported by general evidence, then the intervention scores a level 1; if there is observational evidence from the particular intervention, then it scores a level 2; the availability of directly relevant RCT or other high quality evidence puts the intervention at a level 3.

However, although most investors' processes were not systematic, the basic principles are reflected in other more standard assumptions made by investors – where social impact is an implicit part of an organisation's service or product offering then financial success implies that they are delivering the impact that their commissioners or service users are expecting.

2.6 Single metric of impact and/or the integration of financial and non-financial return

Among our sample of interviewees, social and financial returns were generally considered as separate dimensions, rather than items of value that could be readily synthesised into a single metric. For instance, one investor was developing a balanced scorecard approach based on a social dimension (promoting the 'quality of being human'); effectiveness; efficiency; relevance to need; equity; accessibility; and capacity for system change. Another investor, working in the microfinance arena, explicitly identified a possible

negative relation between financial and social value, by creating a 'traffic light' system that raised concerns if financial profitability was high due to clients being charged high interest rates.

With such disparate impact areas and themes to consider, it can be seen why the integration of many different social returns into a single metric alone was seen as difficult by many interviewees (even in the case of a Social Impact Bond scheme, with payment against a specific metric, it was generally felt useful to track a number of indicators, some qualitative, that presented a more holistic picture of progress).

Only one interviewee saw it as possible to compare different social goals against one another, and even they used a framework that very much relied on expert judgement. One investor that had spent much time considering SROI felt that its key strengths were in initiating debate and providing insight into the most important aspects of the value created by the activities, much as the logic chain process does (though in a less top-down way), rather than providing a quantified fixed 'Answer'.

Instead, a much more popular approach was to take a single social metric, and track performance against this as well as financial outcomes. PhiTrust, for example, tracks CO₂ offsets in its Alter Eco investment; the scale of employment of people with disabilities at its ecodair investment; and the number of socially inclusive jobs created at its La Varappe investment.

2.7 Causal linkages between activity and outcomes

Investors differed in how they used the term 'impact' to infer a proven causal relationship with the intervention or activities provided by their investees. Impact was consistently used in the context of an underlying impact value chain or logic model, but sometimes this impact was inferred rather than proven, and perspectives differed between an assumption of better outcomes per se; and a desire for a proven and measurable link between activities and changes in outcomes.

One microfinance investor we spoke to argued that there is strong evidence for microfinance generally improving access to finance, so enabling individuals to rise out of poverty when entrepreneurial opportunities arise, or at the very least, enabling them to mitigate the worst effects of volatility in income. The implication was that impact studies, and measures of social outcomes, were not needed. Instead, the focus was on fidelity to good standards of practice and the volume of appropriate loans made.

A perspective of an automatic link was also seen in respect of various renewable energy supplies (such as wind power); as well as in a social enterprise promoting environmentally-friendly travel. Hackney Community Transport (HCT) operates commercial bus routes in London, and is an investment of Bridges Ventures. HCT reduces the need for car journeys through the use of buses and community group transport, and makes particular efforts to employ people in areas of traditionally high unemployment.⁶ Hence, HCT argues that commercial success naturally implies a corresponding increase in the beneficial social impact.

One investor argued for close links in the short-term, but uncertainty over long-term linkages. That investee gave the example of microcredit to farmers in Kenya, often as a means to buy dairy cattle. The immediate effect is that the farmers have access to capital to finance their work, and this was seen as beneficial in itself. The extent to which they escaped poverty, however, was seen as highly dependent on sometimes volatile external circumstances – whether farmers could gain fair access to markets for dairy products; whether corruption was under control; the effects of weather and external competition.

Microfinance also highlighted possible tensions between ‘analytical rigour’ and ‘analytical resilience to different conditions’. One interviewee dismissed results from a randomized control trial by saying “we do our investing in different geographies, with different clients, using different loan standards and different processes. The RCT

⁶ <http://www.bridgesventures.com/investment/hct-group> Accessed 26/11/2013

is irrelevant.” Similarly, another interviewee described those looking for academic standards of robustness as “aiming for the impossible”.

In a similar way, underpinned by a ‘theory of change’ perspective, Quadia relies upon a large amount of qualitative and contextual data to inform its judgements; visiting the business, speaking to beneficiaries and experts, and using international initiatives and industry goals as benchmarks, as well as drawing up specific metrics for each investment.

By contrast, at the ‘hard edged’ end of the spectrum, an investor on social impact bond projects spoke of the vital need to see a track record with a proven and measurable link between the organisation’s intervention and the targeted impact - which in this instance related to education attainment, ongoing employment and training. Such an approach sometimes makes use of ‘intermediate outcomes’ (such as increased confidence, or an increased sense of purpose in life among the clients); but one interviewee stressed that while such intermediate outcomes were very useful, it was the ‘hard, final outcomes’ such as education results and employment that were what really counted.

This question of appropriate methodological practice on what should be aimed for and what can be aimed for in terms of evidence on causal linkages highlighted major differences of opinion between interviewees. Some investors with a strong quantitative metrics perspective were dismissive of ‘case by case’ approaches, arguing that they were ‘not really impact investors’ and that their approach was too often reminiscent of ‘throwing mud against the wall and seeing what sticks’. The different perspectives to evidencing causal links can be viewed in terms of positioning across a spectrum for ‘standards of evidence’, identified by the UK impact investor, NESTA, based on the work of the Social Research Unit at Dartington⁷ which is set out below in Table 1.

⁷ <http://www.nestainvestments.org.uk/our-approach-to-impact-and-evidence/our-standards-of-evidence/>

Table 1 – NESTA Impact Investment Fund’s Standards of Evidence

Level	Investor expectation of the investee
Level 1 – Account of Impact	A potential investee can clearly say what a product or service does and why this may have a positive impact on one of our outcomes in a logical, coherent and convincing way.
Level 2 – Correlation	At this stage some data is being collected which show a positive impact on the users of the product or service, but it is not confirmed that the investment caused this.
Level 3 – Causation	Here we will expect to see that the positive change amongst the users of the product or service is happening because of the product or service.
Level 4 – Independent Replication	The claims behind a product or service will have been validated, such as through an independently conducted evaluation. At Level 4 we would also expect to see that the product or service can deliver this positive impact at a reasonable cost.
Level 5 – Scaled	To reach this point it is clear that the product or service can be operated by someone else, somewhere else and on a large scale, whilst continuing to have positive and direct impact on the outcome, and whilst remaining a financially viable proposition.

NESTA Investment Management accepts that many investees will initially have little more than a narrative description of their social impact; but pushes strongly for before-and-after evidence within a period of about 18 months, and looks to see evidence with respect to a control group within three years. A medium to long term goal is that all its investees will have a complete specification of their service, allowing high fidelity replication.

Similar views were held by other respondents: one felt that there were ‘major flaws’ in respect of attitudes to attribution; another that it would take perhaps five years to get much more widespread use of RCT or ‘similarly rigorous’ approaches in impact investing.

One investor queried whether investing to develop impact systems was the most effective use of their investor’s funds, when it could instead be used to finance expansion or growth, which would potentially have a more direct effect on the scale of reach. A comment frequently heard was that investors very much hope that their investees would themselves appreciate the value of better impact measurement in strengthening their operations and refining their strategies.

2.8 Differences in pre-investment and post-investment assessment

We found few examples of investors who undertook the same level of impact assessment after funds had been invested as they did during the due diligence process. The reasons for this varied – some argued that it was too resource intensive for either or both the investee and the investors; others felt it was an ineffective use of investor funds or not particularly relevant given the investor’s approach to impact. A further issue mentioned by two investors was the lack of impact understanding and skills across investment teams. Investment managers tend to be drawn from the mainstream finance sector, with assessment of impact being left to a dedicated professional who may sit alongside, or more often outside the core team managing the investments.

While data on outcomes and performance was received on a regular basis, few of the investors had the resources to revisit or examine the impact evidence in detail after the initial investment. It was commented by several investors that there was no surplus funding available after delivering the return to the investor and covering management costs. It was suggested by one

investor that venture philanthropy organisation are in a different position and more likely to have ultimate funders for whom spending money on impact systems is consistent with achieving their objectives. For instance, one organisation with a strong social stance, Big Issue Invest, supports its investees during the first year of an investment to access pro bono support or find alternative sources of funding to finance the development of appropriate tracking systems.

One investor believed that a more efficient use of resources was to help the investee to embed their social mission across their entire business model and by improving its operational capacity which will give it a greater likelihood of long term growth and impact. One major exception to this occurred with Social Impact Bond investors. At least one of these made clear that it took an ongoing close look at performance, and had mechanisms in place to raise concerns with the impact creator to ensure that satisfactory results were obtained. It is important to note that in the case of social impact bonds the financial return is explicitly linked to the social returns so ongoing tracking of output and outcome metrics is fundamental to the design of the investment.

For investors who are satisfied by an organisation's capacity to deliver impact a more critical focus of impact metrics is to ensure there is no mission drift. Typical practice – as is undertaken by the DOB Foundation, for example - is to select a number of bespoke KPIs which cover outputs, outcomes as far as possible, and mission adherence. No attempt is made by such investors to integrate social and

financial return into a coherent single metric as highlighted by several interviewees.

Some investors, such as some of those we spoke to who are investing in 'clean fuels', see no role for outcome metrics at all. They are content that the desired impact (on reducing greenhouse gases) will follow, and see no need to reinvent the wheel by requesting another impact study. Operational competence, growth and model fidelity were of great importance. Microfinance, for instance, has well established standards for client protection which many interviewees mentioned.

Bank of America Merrill Lynch (BAML) provided an example of the approach undertaken by a mainstream financial organization with respect to sustainable business models. BAML have a target of achieving \$50 billion of business between 2012 and 2022 that "address climate change, reduce demands on natural resources and advance lower-carbon economic solutions" – as part of their normal economic transactions, rather than as a dedicated investment approach. BAML commission a 'top four' consultancy firm to conduct an independent assessment of the expected environmental impact of a transaction, but feel that the sheer scale of their environmental investments would make more tracking of impact post-investment highly burdensome.

By contrast, there are other investors who adopted some standard outcome metrics that constituted their core approach, supplemented by bespoke metrics to capture a more rounded picture. The most ambitious attempt that we are aware of is that being piloted by PGGM (see box 1).

Box 1 PGGM's pilot study of SER measurement

PGGM is a pension fund administrator and investment manager in the Netherlands. It has developed a standard template, applicable to targeted ESG investments in all asset classes, to collate impact information and report to clients annually.

The template has a clear logic: it establishes the global environmental and/or social challenge an investment is intended to address, sets out the process by which the fund expects to deliver the desired impacts (the 'theory of change'), and, based on the theory of change, defines investment-specific output metrics that each fund manager is asked to report on.

The reporting template also covers: whether and how each investment has generated additional direct impacts and contributed to wider sector development; the policies and procedures the manager uses to manage ESG issues, including negative ESG effects and risks; and potential issues of concern to PGGM and what the manager is doing about them (source: PGGM case study, PRI²).

Every investor that we spoke to expected its investees to submit an annual impact report outlining its performance versus agreed key performance indicators. Phi Trust Partenaire requires investees to report output metrics on a half yearly basis with a full impact report encompassing outcome measures on an annual basis. One reason for the relatively infrequent reporting is the regular informal contact with their investees; other investors requested more regular progress reports - investors in social impact bonds are likely to receive information on a timescale ranging from weekly to quarterly.

2.9 Groups and networks to enhance impact measurement practice

Groups and networks (such as IRIS) were seen as potentially promoting better practice in respect of generating shared outcome metrics; disseminating information; and creating partnerships for research. The recent GIIN Investor Forum that took place in London 2013 was referred to as having been a positive platform for sharing best practice and educating the wider impact investor community of issues underpinning impact assessment. It should, however, be noted that a caveat was raised by one investor, who spoke of a risk that umbrella groups could be 'more talk than action'. Nonetheless, potential for improvement though was identified, particularly with respect to three themes which we consider in turn.

Developing usable and better quality outcome metrics

These are seen as an area of much active work over recent years. The microfinance industry has a high degree of buy-in to the social performance taskforce standards, and reporting of that data in a shareable way. Views seem split on future directions however - some microfinance investors said they would value more granular data; others were sceptical of taking standardised metrics too seriously.

The work of Big Society Capital in gathering directories of metrics (Ogain et al, 2013) has also been seen as a key step. Several investors found these metrics listings to be a useful resource,

and an effective prompt in thinking of new ways of measuring outcomes.

Nonetheless, most investors were sceptical of the value of introducing a single measure of impact whilst the majority of investment funds continue to invest across a broad range of impact areas. It was felt that any resulting indicators would be at best misleading (as the underlying context for investment and market conditions would be overlooked) and at worse a case of comparing apples and pears.

Many investors agreed that outcomes in some key themes, such as loneliness, were still difficult to quantify, and investors felt that it was often beyond their capabilities, or at least "not their job", to create new metrics of this kind. The majority of investors interviewed felt that this remained an area where more effort could be undertaken.

Disseminating information

Data availability and possible computer applications was raised by many interviewees. Of those who took more of the 'case by case' perspective, the main request was for the development of practical tools to allow those on the ground to collect data in a way that was not too onerous, but effective, including 'near neighbour' benchmarks.

Several interviewees raised the valuable role that meta-analyses could play, particularly when it could authoritatively highlight powerful messages as to 'what works'. In this context, the synthesis study disseminated by the Education Endowment Foundation toolkit⁸ was noted as a clear, simple, effective star rating system (a similar, though more academic perspective can be seen in John Hattie's 2009 book 'Visible Learning', published by Routledge). It was, however, felt by at least one investor that 'trusted intermediaries' were essential to fulfil the potential of this strand of work, and that, unfortunately, the history of 'commons initiatives' was not encouraging.

⁸ <http://educationendowmentfoundation.org.uk/toolkit/>

Partnerships for research

A small number of investors in our sample are making substantial efforts to be much more rigorous in their approach. They aim to raise standards of evidence and practice to the levels they feel generate ‘real knowledge’. They are generally to find ways to get the most ‘high quality’ evidence (most notably Randomised Control trials, and to a lesser extent multiple replication), although they often struggle to fund such research activities themselves.

Indeed no impact investors we spoke to are doing anything that could be described as an impact study as part of their ordinary investment process, with the exception of some investors in social impact. Instead they were forging alliances with others who might fund the impact study element, including research councils and charities – though sometimes hampered by central governments not doing enough to improve access to longitudinal, individual (but anonymized) citizens data.

3. CONCLUSIONS

The organisations interviewed represent only a small selection of impact investors in Europe, and were not chosen on a random sample basis, which rules out the possibility of making definitive judgements. The measurement practice and insights provided through the interviews do, however, provide an independent perspective on the six propositions outlined on page 1 of this paper. The extent to which these propositions are supported, rejected and/or amended are discussed in turn below, as well as other findings in respect of impact measurement methodology.

An emerging typology for distinguishing impact investors

From our analysis of how interviewees incorporated impact measurement into their investment process, we suggest that there is emerging typology for distinguishing between impact investors. This can be broken down into three distinct approaches: those that are focused on system building, those that assess each investment on a case by case basis, and those that follow the evidence of what works. It is important to note that while this typology will drive how an investor approaches an individual investment, they are not mutually exclusive and it is possible as an

investor to adopt one, two or all three approaches. For instance, an investment fund may invest in social enterprises on a case by case basis, but also be an investor in a social impact bond.

System builders

A few investors - Bridges, Impetus – PEF, NESTA, and Triple Jump – appeared to be advocates of a ‘system building’ approach. Their view was that a rigorously well specified and replicable approach is the right way to attack their chosen goal, though much more analysis was needed to achieve this. These investors are very interested both understanding exactly how and where the intervention works, and developing the best evidence for it. They do this to improve their own allocation of capital, but perhaps more importantly to facilitate the scaling of the idea. They tend to put the most resources into measurement, reach for the most rigour, and have the most standardised outcome metrics. As generating high quality evidence is costly, investors in this area tend to either be highly socially minded, or have alternative sources of funding (most notably, trusts and foundations).

Case by case

Investors such as DOB, Social Venture fund, and Alterfin tend to see the ‘most rigorous’ measurement practices as inappropriate. Instead, their focus has been on understanding the particular context around a given intervention. General metrics tend to be chosen on a case by case basis, and need to be interpreted in the context of expert judgement informed about that locality. Investors in this space, such as Big Issue Invest or Phi Trust Partenaire, are more likely to adopt a pragmatic approach to monitoring impact and caution the need for systems and processes to be proportionate to the benefits they achieve. In a similar vein, Ashoka treats each social entrepreneur as different, and looks individually at the contribution that each Fellow has made to achieving social change.

Evidence followers

Our interviews have highlighted a third category not indicated in Reeder and Colantonio (2013),

namely ‘evidence followers’, who believe that they are applying a technique that is already well evidenced and well specified, and that further evidence would be redundant, or that the impact is so obvious that it does not need it. These investors are more interested in measures of fidelity to the operational model, and operational stability and execution than in impact studies. This includes clean tech investors, as well as investors in some of the more recent social impact bonds – for example the recent Essex social impact bond, where the intervention in question has a well-established evidence base that is informed by RCTs as well as other analyses.

Forms of measurement practice culture

Those interviewed included some that were passionately in favour of treating impact measurement as a practice that should be applied on a deep qualitative basis, taking contextual factors heavily into account. Equally, the interviewees included some that were passionate about using sophisticated analysis to get a ‘better handle on what works’.

Such views were anticipated in the first working paper of this series. What was not anticipated was a third category, ‘evidence followers’, who were confident of a direct link between finance on the one hand, and social and environmental return (SER) on the other, and so felt it much less useful to measure SER.

This third category was particularly predominant around those that were major investors in ‘clean energy’ technology, where outcomes such as reductions in CO₂ emissions can be engineered with precision. What is less clear, however, is the extent to which those engaged with addressing social problems can justify that social impact must proportionately follow economic impact. An important case of that assumption coming under question is microfinance; after highly publicised cases of clients committing suicide as a result of taking on too much debt⁹, this field is taking serious steps (led by initiatives such as the ‘Social Performance Task Force’), towards taking

⁹ <http://www.theguardian.com/world/2011/jan/31/india-microfinance-debt-struggle-suicide>

the subtleties of ethics and context much more seriously.

Concepts of what should be measured and covered within ‘impact’ and ‘non-financial return’ or ‘wider value’ are far from settled

Interviewees had a highly varied range of attributes covered within impact. Some, such as NESTA, put emphasis on empowerment in priority groups (older and young people). Others felt that the most important attribute was the ability to increase employment in target areas. Some felt that indirect long-term systemic effects were crucial; others neglected these in favour of direct effects here and now.

What is most striking to the authors of this paper, however, is the low level of engagement that impact investors seem to have with the ultimate beneficiaries of their social impact. It may well be that they share the priorities of the impact investor, but this should not be assumed to be the case. While SROI was not a tool widely used by the investors interviewed, its methodology of asking views from a wide range of stakeholders implies fewer assumptions are being made as to what impact should be valued.

In addition, the connections, actual or perceived, between non-financial and financial returns are a key factor in determining what impact gets measured, and the effort put into measurement. Such a connection is clearest with social impact bonds, where financial return is explicitly linked to one or more metrics of social outcomes, and the effort placed on evaluating this link can therefore be very substantial. By contrast, a comment by Triodos Investment Management that ‘we see profit as proof of a healthy organisation, but not as an end in itself’, puts the financial and non-financial on a more level footing, where each are viewed as important in themselves, as well as for their relationship to one another.

Conceptual frameworks have often downplayed the category of risk

Our interviews showed signs that investors are beginning to place greater importance on impact risk, with emerging frameworks that explicitly

take this issue into account by looking for ‘robust evidence’ on what works. Similarly, investors with a focus on social impact bonds tend to take a close look at both the robustness of the evidence, and the extent to which it highlights volatility in outcomes. Data on past track records is being used to predict what is likely to happen to outcomes and associated payments. Such explicit modelling of outcome risk remains the exception rather than the rule, however, among impact investors.

Use of ‘subjective’ as well as ‘objective’ outcomes

Perhaps as a consequence of different measurement cultures, our interviewees showed different levels of willingness to adopt ‘subjective’ outcomes in their assessments. For instance, while Ashoka is happy to include a relatively subjective term such as ‘ethical fibre’ in its decision-making, other investors are much more comfortable at assessing such objective effects as ‘the extent of reoffending’, and find it hard to measure intrinsic motivation and wellbeing.

The conceptual case for creating a single metric of value is highly contested

Those interviewed for this paper showed little, if any, enthusiasm for creating a single metric of (social) value. Much more emphasis is instead being placed on the development of suitable scorecards that can capture the elements that are felt by investors to be of most value in the given investment under consideration.

Tensions between bespoke and standard measurement systems

Our group of interviewees clearly showed that tensions between bespoke and standardised measurement systems remain prevalent. For instance, on the one hand one investor cautioned against expecting too much from IRIS’s attempts to standardisation, because investees have too much flexibility to choose an indicator that puts them in a good light; and too much flexibility in how they assess the chosen indicators. By contrast, on the other hand another investor argued that it was only through more standardisation and benchmarking that ‘real learning’ would take place. Resolving this tension will be a major challenge for those institutions (such as IRIS / GIIN and Big Society Capital) that

are currently doing the most to promote greater standardisation in measurement.

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