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Impact Bonds: An Innovative Financing Mechanism for Social Development

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Abstract: Artificial Intelligence (AI) has emerged as one of the most transformative and rapidly expanding Even though SIB's usefulness, Social Impact Bond's adoption is still modest. The mismatch between widespread interest and actual application raises interesting questions as to whether we are still in the early adoption stage of SIBs and massive diffusion is yet to come, or we are observing a marginal phenomenon. To throw some light on this issue, the paper provides a review of the cases in which the SIB model has been already applied, exploring the specific configuration employed, with the purpose to identify regular configuration patterns and their deviation from a prototypical structure.

Keywords: Impact Bond, Finance, Social Cause, Development, Organization, Investors.

1. Introduction:

Impact Bonds are an innovative financial Investment approach. It utilizes private capital to fund government projects and public welfare projects. It is a new investment approach towards social problems. There are two types of Impact bonds i.e., social impact bonds and development impact bonds, both the impact bonds are result-based financings for public welfare which results in economic growth and helps transfer risk to investors. Both the impact bonds are similar, just difference comes from who ultimately pays for the outcome. In a social impact bond, the outcome funder/payer is the government, while in a development impact bond the outcome payer is a donor. Social impact bonds are also known as "Pay-for-Success" financing, Payment for Performance, Payment for Result regarding the delivery of public services. Pay for Success initiatives are different from the traditional approach because they are focused not simply on creating additional financial incentives for contractors to produce better outcomes, but more broadly on overcoming the wide set of barriers that are hindering the pace of social innovation. For sure, these obstacles include a lack of performance focus and outcome measurement, but they also include political constraints that prevent the government from investing in prevention, the inability of nonprofits to trail the capital needed to expand operations, and insufficient capacity to develop rapid and rigorous evidence about what works. In some of these new models, the amount of performance risk shifted from taxpayers to those on the hook for producing the outcomes is much greater than under traditional performance contracts, requiring the participation of socially-minded investors to make the projects feasible. Result-based SIBs are

focused on short-term goals and try to solve the social problems fully or partially. For that, every time different evaluation model is prepared. Certain parameters are prepared regarding social impact success to give the return to the investor, If those parameters are fulfilled then return is given otherwise not. e.g.If an impact bond is issued about drop-out of students, then Impact can be assessed through the decrease in drop-out ratio.

Background: First of all, the Impact bond was introduced in the world by the United Kingdom in the year 2010. The purpose of the Impact bond program in the United Kingdom was to reduce the rate of recidivism at Peterborough Prison in Cambridge. Then many impact bonds were issued in the world to fund the welfare projects. In India also some impact bonds were issued over a while. Impact bond in India was introduced in the year 2015 i.e. Educate girls development impact bonds. The purpose behind launching the development impact bond was to improve education for girls in Rajasthan, after that other development bonds were also issued in India and some are in process.

2. What is a Social Impact Bond?

SIBs are funding mechanisms that invest in social outcomes. They have three elements:

- Monetary investment (for example, £x million from local authorities, commercial investors, philanthropists, or foundations)
- A program of actions to improve the prospects of a group (for example support and mentoring service to those leaving prison with the aim to reduce re-offending)
- Commitments by national or local Government, or foundations, to make payments linked to improved social outcomes achieved by the group (for example, re-payment of the $x million original investment and an extra percentage agreed to return, sustained by reduced costs for the Ministry of Justice through reducing re-offending and numbers in prison).

Parties Involved: -

In the Impact bond agreement, there are five parties involved i.e. External Organization (Intermediary), Investors, Service Providers, Independent Assessor/Evaluator, Outcome Funder.

Role of The Parties: -

Service provider	Provide social service in the project e.g., NPO's or NGO's, Public sector service provider
Investors	Provide funds to service providers upfront or throughout the contract e.g., Individual, Trust, Foundation, Public sector entity, etc.
Intermediaries	Raise capital, manage the deal, receive outcome payments and pay investors e.g., government agency, Impact investment firm, etc.
Outcome Funder	Pay for outcomes, determine outcome metrics and repayment Parameters or conditions. e.g., Government agency, foundation, development agency
Evaluators	Assess outcomes of program e.g., independent evaluation firm, Research institution, university, government institution

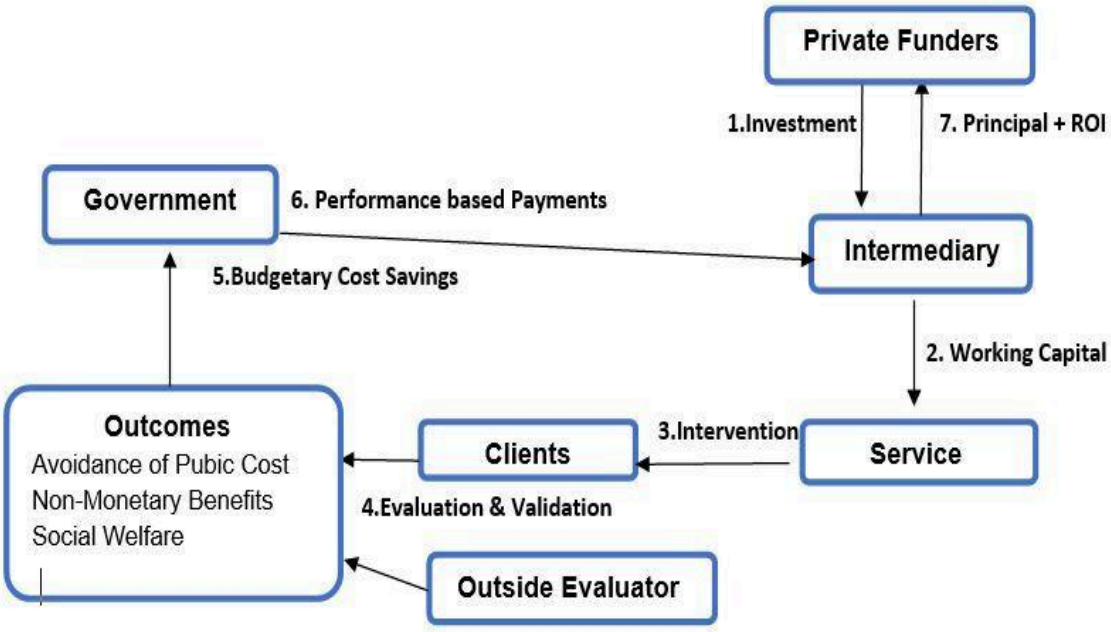
Motivation for Investors

- To test a new and innovative financial model for social services
- Ideal social image and publicity
- Both social and financial return
- Personal morals that focus on positive societal changes

Comparison with Traditional Approach

In traditional social projects, it includes a government agency collaborating or bonding with private NPO's or NGOs to perform the project on the focused group. The objective behind the project was to achieve the benefits, such as avoidance of public cost and other social benefits. If the project is successful, it results in the public-welfare. The modern Social Impact bonds, It is based on the payment for performance or outcome. In this kind of project, Private Investors are also made available by for-profit or social welfare interest and return is depends on the decided parameters achieved or not.

Procedure:



Advantages:

1. They are very prominent in cost-saving and transferring the risk to private investors.
2. It provides evidence-based service.
3. It is useful to transfer costs from the public to the private sector.
4. Impact bonds shift focus to results or performances
5. Impact bond foster novation in the delivery of social services
6. It leads to Performance management which results in the achievement
7. Support Experimental Interventions

3. Case Study: India Educate Girls Development Impact Bonds (2015-2018)

This presents the case analysis of the impact bond Project in India by identifying the parties involved and the benefits, hazards, and safeguards for each party.

Target Population	Children in 166 public schools in 140 villages in Bhilwara District
The target number of beneficiaries	15,000 children (9,000 of them girls)
Service provider	Educate Girls
Investors	The UBS Optimus Foundation (UBSOF)
Intermediaries	Instiglio (project manager, impact bond designer, performance management provider)
Outcome Funder	The Children's Investment Fund Foundation (CIFF)
Evaluators	IDinsight

3.1 Outcome Metrics:

- Enrollment outcomes (20% of outcome payment): number of girls on school rosters in grades 2-8 in the treatment group over 3 years;
- Learning outcomes (80% of outcome payment): Annual Status of Education Report (ASER) measures basic literacy in Hindi, basic literacy in English, and basic numeracy

3.2 Evaluation Method:

- **Enrollment:** A baseline of out-of-school girls was created through household surveys before the implementation of the program; IDinsight independently verifies the accuracy of the enrollment list by sampling a portion of the lists and conducting school and household visits to measure the percentage of out-of-school girls who are enrolled in school rosters after three years.
- **Learning:** IDinsight evaluates learning outcomes through a clustered randomized control trial. The students' learning progress was measured using the ASER assessment. A baseline test was administered at the start of the trial 3 periods to students in Grades 1-5 (the students that will receive the learning intervention in any given year during the lifetime of the project) randomly sampled from schools receiving the intervention and control schools. It measured students' starting grades on a scale of A to E for English and Math, and A+ to E for Hindi. The students are tested again at the end of every school year for three years. The evaluator will then calculate the aggregate learning gains in terms of the number of levels gained on the ASER scale by children in schools receiving Educate Girls' intervention as compared to children in control schools

3.3 Payment Schedule and Amounts:

- UBSOF disburses 50% of investment principal to Educate Girls in 2015 and 50% in 2016; CIFF will disburse one outcome payment of $0–$412,000 to UBSOF in 2018

3.4 Maximum Return:

- Target IRR = 10%, max IRR = 15%; UBSOF pays incentive to Educate Girls equal to 32% of its payment above principal.

3.5 Result:

- More than seven thousand students who studied in the Educate Girls programs gained 8,940 ASER learning levels — the annual survey that aims to provide reliable estimates of children's enrollment and basic learning levels for each district and state in India — more than those in the control village and 160 % of the target.
- The learning gains for students in the Educate Girls schools were 28 percent higher than the learning gains for students in the control schools. Year three gains accounted for more than 6,000 of the overall learning level gains, while years one and two hovered at about 1,400. That translates to students on average gaining 1.08 ASER (Annual Status of Education Report) levels more than those in the control group — a jump linked to, for example, moving from words to paragraphs.

4. Case Study: India (Rajasthan) Maternal and Newborn Health Dib

This presents the case analysis of the impact bond Project in India by identifying the parties involved and the benefits, hazards, and safeguards for each party.

The India (Rajasthan) Maternal and Newborn Health DIB aim to improve the quality of maternal and newborn health services provided through private facilities throughout Rajasthan. The impact bond structure is used to drive efficiencies and harness the novel commercial perspective of investors to improve performance in service delivery. The ultimate aim is to reach a tipping point so that all private facilities across Rajasthan will be incentivized to increase the quality of service delivery. Improved service delivery in private facilities, in tandem with the new Matritva certification process, will enable the government to confidently contract out services to the private sector and facilitate demand-side financing initiatives, leading to a raise in maternal and early newborn survival.

Target Population	Mothers and newborns across the state of Rajasthan
The target number of beneficiaries	At least 300,000 TARGET
Service provider	Hindustan Latex Family Planning Promotion Trust (HLFPPT) Population Services International (PSI)
Investors	80% UBS Optimus Foundation with 20% of the total investment capital being provided by the Implementation Partnership of Palladium, PSI and HLFPPT

Intermediaries	Palladium (Intermediary, design agency, performance manager)
Outcome Funder	USAID, Merck for Mothers, Government of Rajasthan planning to commission outcomes in Year 4 and 5
Evaluators	RFP for independent verification agency currently being evaluated
Technical assistance provider	Instiglio (Performance Management System design inputs), Skotkonung (Information System Development), Social Finance (Deal Advisory and Structuring inputs), Reed Smith (International Legal Counsel), Phoenix (Indian Legal Counsel), Rabin Martin (Strategic Advisory Services to Merck for Mothers).

4.1 Outcome Metrix

Full payment is readiness for JQS - > = 50% of the total points available in each NABH chapter (10 in total) AND 100% of at least 70% (11) of the applicable FOGSI standards (16 in total). Progressive metric (25% of full outcome payment ie $4,500) is >=30% of the total points available in each NABH chapter (10 in total) AND 100% of at least 40% (6) of any of the applicable FOGSI standards (16 in total)

4.2 Evaluation Method: Independent audit

4.3 Payment Threshold: $18,000 per facility that reaches agreed JQS level

4.4 Payment Schedule and Amounts: Six-monthly with $4,500 for each the facility at the progressive stage and the remainder of $13,500 for facilities that reach JQS during that period.

4.5 Maximum Potential Loss of Investment For Investors: No guarantee – payments are per facility ready for accreditation hence full loss is not possible but anything other than reaching the minimum target of 360 facilities at JQS level according to the agreed forecast during the three-year duration will result in losses for the investors.

4.6 Maximum Return: 8% annualized for UBSOF component with 15% return possible for the implementation partnership investment piece.

5. Case Study: Quality Education, India (2018-2022)

This presents the case analysis of the impact bond Project in India by identifying the parties involved and the benefits, hazards, and safeguards for each party.

Given low levels of learning in public primary schools in India, and not enough scalable models to deliver a good quality of learning, this DIB seeks to impact 200,000 marginalized children from 3 states in India. The DIB will finance the implementation of 4 different models in the field: (a) whole school management (b) remedial teaching for children who are behind their

grade level of learning (c) teacher training and (d) school leadership or principal training. Each of these has a diverse level of impact on student learning at a different cost per beneficiary. The end goals are broadly threefold: to improve the learning levels of these 200,000 children, to identify models which work in the field, learn lessons and promote their scale-up, and finally, look to bring the private sector and philanthropic money into development programs that focus on outcomes.

Target Population	Primary school students
The target number of beneficiaries	200,000
Service provider	Kaivalya Education Foundation; Educate Girls; Gyan Shala; Society for All Round Development (subject to final due diligence)
Investors	The UBS Optimus Foundation (UBSOF)
Intermediaries	TBC
Outcome Funder	British Asian Trust, Michael, and Susan Dell Foundation INVESTOR: UBS Optimus Foundation TECHNICAL ASSISTANCE PROVIDER: TBC
Evaluators	TBC

5.1 Outcome Metrix :

- Improvement in literacy and numeracy outcomes over four years.
- Enable primary school students to catch up between [1-2.5] grades over the four years to allow sustained learning outcomes at their grade-appropriate learning level.
- Set-based operational models and global benchmarking targets on effective education initiatives.

5.2 Evaluation Method: Validated administrative data

5.3 Payment Threshold: TBC

5.4 Payment Schedule and Amounts: Approx. 8% per annum on investment amount not to exceed $740,000 if outcome targets are met. Performance reviewed annually. Investors deploy an estimated $1.8 million in year 0, $400,000 in year 1, and $200,000 in year 2, for a total of $2.4 million over 4 years (capped at $3 million) if 100% outcome targets are achieved every year.

5.5 Maximum Potential Loss of Investment For Investors: Subject to Capital Protection sought by UBS Optimus Foundation

5.6 Maximum Return: Returns capped at $740,000 (7% IRR)

Evaluation Methods:

The methods of evaluation have fallen into different categories:

- Validated administrative data,
- Historical comparison,
- Quasi-experimental,
- Randomized controlled trials
- Quantitative benefit-cost analysis to map out transaction costs

6. Challenges, Suggestions, and Conclusion

6.1 Challenges:

1. The payment structure is complex
2. Financial costs of the projected deal and the hours required to make the deal together
3. Availability of measurable and monetizable results are a big challenge
4. Random evaluation method

6.2 Suggestions:

Impact Bonds as a form of CSR: Evaluators opened up to the opportunity that CSR funds are allowed to generate profit, then SIBs can build a bridge between the companies' business and their (sometimes burdensome) CSR activities. The isolation of CSR has equally been subject to criticism by the public just like no CSR activities at all. SIBs can detain the drifting apart of these two spheres by changing the mindset about the role of CSR within the firm. Pilot Project The Haryana Early Literacy DIB is piloting a new method of utilizing CSR funds for outcomes payment in India. The project enables CSR entities to pay for outcomes, instead of inputs and activities.

To achieve Sustainable Development Goals: Impact bonds are a notable way of bringing private capital to accelerate our journey towards SDGs.

6.3 Conclusion:

Nonprofit organizations and governments are often criticized for their lack of innovative efforts and preventative approaches in targeting social problems. Resource and capability constraints are partly to be blamed for the reluctance to invest public money in risky interventions for complicated and contentious social issues. As discussed earlier, social impact bonds enable nonprofit organizations and governments to attract alternative resource providers and to shift the financial risk in social intervention programs. However, the potential winners in social impact bond program initiatives include several parties as well. By conducting a case analysis of the SIF Project, this study highlighted the multiple parties involved, their potential benefits, costs, hazards, and safeguards. Our study suggests that Impact bonds can change the funding scenario in health welfare and Poverty issue-related projects.

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