How This Works
PROTOTYPES

FINANCING OUTCOMES THROUGH SOCIAL IMPACT BONDS

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In 1977, Dr. David Olds began testing a home-visiting program that paired nurses with first-time, low-income mothers. The Nurse-Family Partnership (NFP), a community health program that extends from pregnancy through the first two years of a child's life, has since become one of the most effective social interventions.

The results speak for themselves: across three randomized controlled trials, NFP improved birth outcomes, reduced childhood injuries, decreased special education needs, and even lowered rates of criminal activity decades later for participants. However, this program is just serving a small fraction of the 800,000 babies born to eligible low-income, first-time mothers each year in the United States.

So why hasn't NFP become the standard of care?

One reason is because the public and social sectors are largely not currently designed to reward what works or to allocate funding based on outcomes. Rather, funding is typically structured around services delivered.

Social impact bonds can be part of the solution. Social impact bonds sit at the center of three powerful twenty-first century movements: an ever increasing reliance on data and evidence in service of policymaking, the harnessing of capital markets in service of society, and growing momentum around tri-sector models. This partnership model aligns uncommon partners—policymakers, investors, and nonprofit service providers—around a common purpose, further blurring the ever more porous boundaries across the public, private, and social sectors.

In this essay, I discuss how social impact bonds—and the partnerships they foster—manage for performance and create value by tackling the root causes of persistent social challenges to measurably improve the lives of those in need.

DEFINING SOCIAL IMPACT BONDS

Social impact bonds are part of a broader suite of Pay for Success contracting mechanisms, which direct government resources to *outcomes achieved* rather than *services delivered*. Pay for Success approaches, including social impact bonds, performance-based contracts, and outcomes rate cards, all center on the same question: How can the public sector allocate resources more efficiently while improving outcomes for the most vulnerable?

In a social impact bond, intermediaries bring together impact investors, high-impact service providers, and government payers to implement preventative social services that, if successful, will lead to improved social outcomes and reduced government costs, generating both fiscal and intangible value for society.

THE VALUE OF SOCIAL IMPACT BONDS

Social impact bonds rely on an elegant, mutually beneficial framework:

- High-performing nonprofits get access to long-term, flexible funding, which allows them to grow—and links performance to further funding.
- Impact investors are able to reflect their values in their investment portfolios by receiving financial returns only when projects measurably improve people's lives.
- Governments gain a new level of accountability for taxpayer funds by only paying for results.

The end result is a new dynamic yielding multiple winners across sectors and a set of incentives that redirect society's resources toward measurable results for our most vulnerable communities.

WHY HAVE SOCIAL IMPACT BONDS ATTRACTED SUSTAINED ATTENTION?

The Value of Risk Transfer

Social impact bonds transfer performance risk from government to funders. Through social impact bonds, government is able to experiment with promising approaches for preventive programs or meaningfully scale a proven approach, but is obligated to pay *only if* the program works.

Focus on Outcomes vs Outputs

Government spends hundreds of billions of dollars each year to provide health care for sick people, support vulnerable children, help build our workforce, and provide other necessary human services. However, for the most part, government measures outputs, such as the number of people served, volunteer engagement, or money distributed. Outputs do not provide answers to the big question: whether we're moving the needle on our most intractable challenges.

Outcomes are what matter: ex-offenders getting employed and reintegrated into society, students graduating and connecting to the labor force, women delivering healthy babies. Outcomes are what we are after but evaluating, tracking and reporting on outcomes requires not only a significant investment in resources but also a shift in mindset. Social impact bonds provide one way to focus public sector attention and resources on the achievement of outcomes.

Orientation Around Prevention

Social impact bonds allow governments to invest early and upstream, focusing on prevention rather than remediation via the social safety net. Vaccines are cheaper than treating disease; job training and housing cost less than incarceration. And these are only the quantifiable monetary benefits, they do not capture the intangible value of a life better lived.

The Role of Active Performance Management

Through active performance management—a key feature of social impact bonds—project oversight, analyzing programmatic and administrative data, course corrections, financial management, and investor relations—Social Finance and project partners keep a social impact bond on track over the life of the project. Active performance management aligns the interests of governments and service providers in new, productive ways, resulting in closer working relationships and a coordinated focus on project goals.

With a focus on prevention and outcomes, alongside ongoing performance management, social impact bonds help drive systems change in government. Indeed, social impact bonds represent a unique form of impact investment, with financial returns generated by increased efficiency and effectiveness of taxpayer funds.

One powerful example is the Nurse-Family Partnership Pay for Success Project in South Carolina. Launched in April 2016, the project focuses on improving maternal and child health outcomes for 3,200 low-income families state wide in South Carolina over six years. The initiative mobilizes $30 million to expand Nurse-Family Partnership's services, with philanthropic funders committing $17 million to the project and $13 million of federal Medicaid funding via a 1915(b) Medicaid Waiver. All potential success payments repaid by South Carolina will be reinvested in future Nurse-Family Partnership programming.

THE STATE OF THE FIELD

The values of collaboration, responsiveness, and a focus on data position social impact bonds with other parallel global movements, and have captured the interest of policymakers, social sector leaders, and the investor community worldwide.

Since Social Finance UK launched the world's first social impact bond in Peterborough in 2010 aimed at reducing prisoner recidivism, more than 70 projects have launched in 18 countries, with 15 projects here in the United States. Supporters of social impact bonds cross political party lines with at least two dozen states—balanced between red and blue—pursuing social impact bond approaches. A bipartisan congressional coalition has formed around the model to provide federal support for social impact bonds in state and local governments. The federal government has also demonstrated its commitment through support for projects in education, health, housing, employment and reentry support, and veterans' affairs.

CHALLENGES TO THE FIELD

As with any innovation, there are challenges to be addressed and overcome. Tri-sector partnerships over a multi-year timespan require shifts in roles and mindsets on all sides. Structuring social impact bonds can be complex, and to date they have served a limited number of people in need.

The measurement and evaluation process can also pose challenges, but is essential for triggering repayment and guiding future policymaking. In these early years, we have come to understand that we must balance the complexity required to precisely measure impact with the transparency and simplicity required for government payment and broad policymaking.

Critics have pointed to the high costs associated with structuring social impact bonds, but we would argue that these costs are the price of good government at work. Essential components of social impact bond development, such as analyzing available data sources, identifying evidence-based practices, supporting service providers to implement with high quality, and measuring results, are integral to ensuring long-term success as governments work to serve those in need.

Finally, we must not judge the field too early. As the field grows—and as we work to standardize the model—we must be cautious to do so without losing nuance or crowding out needed innovation.

THE EVOLUTION OF SOCIAL IMPACT BONDS

In these early years, we have seen enormous growth and evolution in the model—including a greater diversity of social impact bond structures. New geographies are applying the concept to new issues and adapting the model to work with different sets of partners. Dynamic stakeholder ecosystems and new payment structures are emerging.

We see iteration and innovation happening across three core dimensions of social impact bond design: financial structuring, payer characteristics, and measurement and evaluation. Projects are being developed both as loans and as equity, drawing from a blend of investor types, with an increasing number of outcomes measurements (versus a single threshold), and with regular capital calls instead of lump-sum payments. Projects can have either single or multiple payers, and increasingly, new types of payers — such as health insurers and private institutions — are exploring these roles.

We are also working to create a more nuanced approach toward measurement and evaluation based on project context and stakeholder objectives. Randomized controlled trials, characteristic of many early social impact bonds, are often challenging to implement and can limit the number of people served. Given these constraints, they may play a more limited role in the future, utilized either in tandem with validated outcomes or to inform project learning rather than project payment structures. Such a shift would create additional flexibility, allowing interventions to adapt more rapidly to interim measurements and ongoing outcomes data.

There is no one-size-fits-all social impact bond model; developing the appropriate structure for specific goals and contexts is critical to producing positive and enduring long-term outcomes.

THE FUTURE OF SOCIAL IMPACT BONDS

Six years in, we have built a proof of concept. But these are still the early days of the social impact bond field, as we build and iterate on our collective experiences in service of our most vulnerable communities.

We are mindful that social impact bonds are not a panacea; bringing the best of what we've learned in social science and adapting it to the realities of public sector investments is not a linear process. But we are optimistic that, as we incorporate learnings from the initial social impact bonds, we will continue to advance the field to the next level.

As Robert F. Kennedy remarked, our Gross Domestic Product doesn't always measure what matters: "It measures neither our wit nor our courage, neither our wisdom nor our learning, neither our compassion nor our devotion to our country, it measures everything in short, except that which makes life worthwhile."[1]

We have been valuing what we can measure; with social impact bonds, we can begin to build a market towards financing outcomes and measure what we value most: what makes life worthwhile.

1 Robert F. Kennedy, "Remarks at the University of Kansas," John F. Kennedy Presidential Library and Museum (March 18, 1968), available at https://www.jfklibrary.org/Research/Research-Aids/Ready-Reference/RFK-Speeches/Remarks-of-Robert-F-Kennedy-at-the-University-of-Kansas-March-18-1968.aspx.

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