Social Investing – from Hype to Impact?

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Much is happening in the UK and in other countries. This article focuses on the European context where the EU has set as a priority social entrepreneurship and social investment. This is building of a long tradition associated with the social economy. Steps are being taken to ease cross border social investment. Euclid has played a strong role, along with others, in supporting this movement.

Impact investment is blossoming. What started as a fad for idealists is gradually becoming a mainstream concept often discussed by fund management hotshots and company executives. The concept itself is certainly appealing. Investors are realising that they have the possibility to help solve some of the world's most pressing social problems and make a profit at the same time.

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In the aftermath of the financial crisis, the old debate of whether financial markets can become a force for social good has been rekindled. For all of the buzz around it, the blend of investment thinking and social aims is hardly innovative. Some ethically responsible investors have long filtered their investments to ostracise arms-trading companies, cigarette-makers or hyper-polluting firms. Now, rather than simply excluding businesses through positive or negative screens, investors can target those explicitly set up to create a deliberate *positive* social impact that is measured with the same rigour as their financial returns.

During the past several years the world has seen a surge in the social enterprise and social investment movements – and some specific initiatives, such as social stock exchanges and social impact bonds. These new trends are to some extent a reimagining of the tradition of the social economy in parts of Europe for a new economic age. Impact investing may even come to be seen as an alternative means to pursue the aims of the Welfare State.

In this sense, the EU seems to have taken up the torch. Social entrepreneurship and the European social economy as a whole were identified as priority issues within the Europe 2020 strategy and the Social Business Initiative to support territorial, social and

economic cohesion. The European Commission also supported the second Active Europe conference (Krakow, November 2011), which saw social bankers and alternative financiers from across Europe set out to design bottom-up recommendations on how the EU can most effectively support the social economy. Social businesses, they rightly claimed, struggle to find sufficient, stable funding.

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In that same meeting, a taskforce led by Euclid Network and FEBEA (European Federation of Finance and Ethical and Alternative Banks) was established to further develop the guiding principles into a working model for a European Social Investment Facility (ESIF). A communiqué addressed to Michel Barnier, Commissioner for Internal Market and Services, was also composed. Centred on the common industry principles that should underpin an ESIF to radically catalyse more social financing in Europe, this initiative showcased the value of bottom-up and industry-led engagement to inform policy. The work of the ESIF task force also helped to shape a new European Commission Group of Experts (GECES) on the Social Business Initiative.

The aim is to show how EU funds can be used to attract private capital for social investment. Some steps have indeed been taken in the right direction. The European Social Entrepreneurship Funds (EuSEF) regulation[1] created an optional 'passport' which should eventually allow managers of social entrepreneurship funds (those where at least 70% of the capital received from investors is spent in supporting social businesses) to market their funds across Europe. The regulation intends to streamline cross-border fundraising, as well as standardise compliance, transparency and reporting requirements for investment in social businesses. It will also make it easier for socially conscious investors to identify funds that focus on European companies contributing to smart, sustainable and inclusive growth.

Although progress has been made, much remains to be achieved. Unfortunately, information on the much-needed, detailed regulatory framework to set the EuSEFs in motion is still to be released. Talks on the ESIF did help inform the European Investment Fund (EIF) when it established a Social Impact Accelerator (SIA) to pilot how the EU could use its funds to leverage in private capital for social investment. Operated by the EIF since May 2013, the SIA operates as a 'fund-of-funds' dedicated to investing in social impact funds which strategically target social enterprises across Europe. While it is still too soon to celebrate the success of the operation, and it will take some time until social entrepreneurs see actual money coming their way, there is reason enough to see the glass as half full.

Nevertheless, all this good work has not yet succeeded in tackling some of the most-pressing problems standing in the way of impact investment. The first of these is the blurred concept of 'social enterprise' or 'social business'. Although the EU has adopted its own working definition[2], practitioners still use both terms interchangeably or sometimes to mean different things. It is difficult to regulate a sector when no single definition for it has been agreed upon. Wendy Kopp's Teach for America or Bill Drayton's Ashoka would surely feature in a list of social businesses, but what about private universities or a doctor's private practice? So far everyone seems to concur that a social entrepreneur's main measure of success should not be wealth creation but mission-related social impact.

Which leads us to a second conundrum. Arguably the biggest obstacle to the creation of sustainable impact investment is the lack of a common measure of how much good has been done. In other words, how do you gauge how many lives have been impacted upon by a single investment? Billionaire philanthropists such as Bill Gates have focused on finding better metrics for the results of their programmes but no major breakthroughs have yet been made. The GECES group recently published its first paper on social impact measurement[3], which now serves in the EU as a foundation for further work in the field. However, a practical toolkit for implementation is yet to be developed.

This explains why, in spite of this impact investment craze, many remain sceptical as to its effectiveness. There is a widespread view that impact investment tends to underperform the market. A glance at Muhammad Yunus's Grameen Bank's financial statements will prove that there are exceptions to the rule.

The assumption – generally accurate – is that to achieve the greatest social impact, it is often necessary

to take high levels of investment risk. But let's not forget that running a start-up, be its main aim social or not, is risky by nature. There is no need to point the finger only at those people with the innovative ideas to address major societal problems. The most reasonable policy is, then, to accept and manage that risk as you would with any other business. Better impact measuring techniques should help to remind investors that today's impact investment is as much about generating good returns as it is about the companies' social benefits.

Such techniques will also prove critical to weigh up the success of social impact bonds (SIBs), a public-private investment instrument that is now being tried out in a few locations. It is hoped that SIBs will be able to tackle some thorny social issues while keeping public budgets tight.

The concept started in 2010 in the UK with a prisoner-rehabilitation initiative in Peterborough, where the British government aimed at transferring the risk of the programme from the public to the private sector. In a nutshell, public authorities will pay out only if the programme meets specified targets. Certain pre-determined milestones trigger the payments. There is of course the possibility that investors will not get their money back. On the other hand, if all works according to plan, they could earn a hefty annual interest, with the possibility of extra profits. In the meantime, the State, due to higher productivity, keeps its pockets fuller. While final results are not yet known, and SIBs probably need to become more like regular debt instruments, there seems to be reason for anticipation.

Evidently, such developments in Brussels will take time. But twenty-first century societal challenges such as an ageing population, fiscal constraints and rising pressure on natural resources require a multi-stakeholder approach and, above all, swift action. The European Commission should press ahead to make it easier for the rare breed of social entrepreneurs to succeed in their aims of making the world a better place.

[1] *Published in the Official Journal of the EU in April 2013.*

[2] *"A social enterprise is an operator in the social economy whose main objective is to have a social impact rather than make a profit for their owners or shareholders. It operates by providing goods and services for the market in an entrepreneurial and innovative fashion and uses its profits primarily to achieve social objectives. It is managed in an open and responsible manner and, in particular, involves employees, consumers and stakeholders affected by its commercial activities. The Commission uses the term 'social enterprise' to cover the following types of business:*

- those for which the social objective of the common good is the reason for the commercial activity, often in the form of a high level of social innovation;

- those where profits are mainly reinvested with a view to achieving the social objective;

- and where the method of organisation or ownership system reflects their mission, using democratic or participatory principles or focusing on social justice" ('Social Business Initiative; European Commission; 2011; 682 final; pp. 2-3).

[3] *'Proposed Approaches to Social Impact Measurement in European Commission legislation and in practice relating to: EuSEFs and the EaSI'; GECES Sub-group on Impact Measurement; 2014.*