Social Return on Investment – for social investing

How investors can use SROI to achieve better results

Cabinet Office
Office of the Third Sector

SROI – for social investing

The SROI Network
Accounting for value

Cabinet Office
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nef
economics as if people and the planet mattered

charities evaluation services

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New Philanthropy Capital

in association with

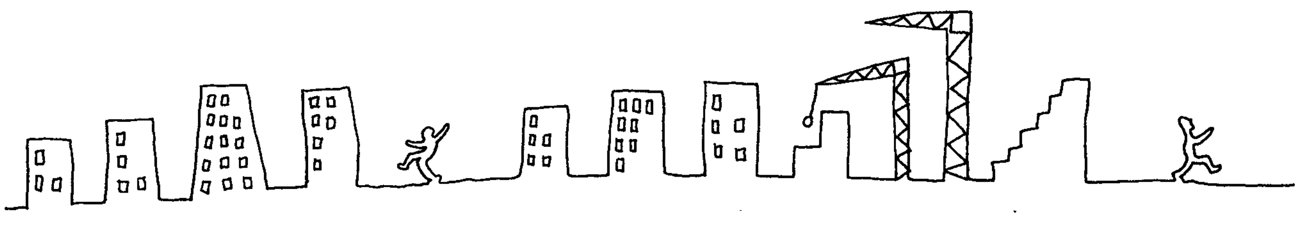
The Scottish Government

Background

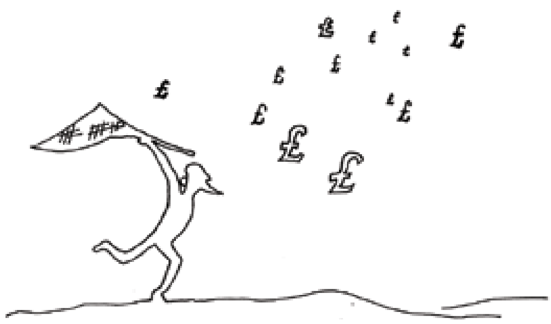
Social investment is about investment made for a primarily social purpose, creating a combination of social and financial value. Any investor will be motivated to a greater or lesser extent by each of these factors and will therefore wish to pursue financial or social return and increasingly a combination – or blend – of both. Socially motivated investment may also generate financial returns and financially motivated investment may generate social returns. There is a growing appetite among investors to understand the broader social value that is being created through their investments.

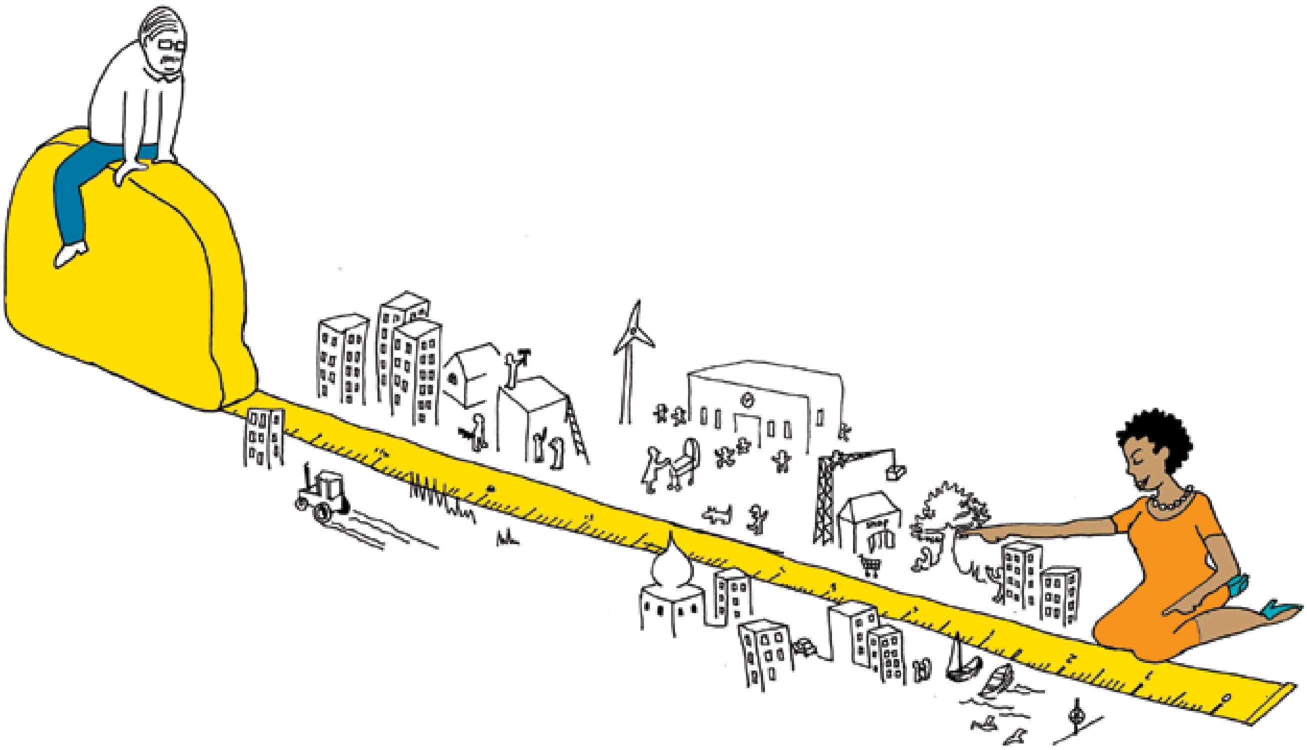
Investment is about deploying capital in order to generate more effective production of goods and delivery of services. When it works, the benefits can accrue to the investor, the investee, to customers and to wider society. Equally, we need to remember that investment can also generate greater social value, which is not necessarily captured in traditional financial flows. This social value may accrue to customers or to beneficiaries, but may also be generated to a sufficient degree so that some of this value can be attributed – or returned – to investors. This is what we mean when we talk about Social Return on Investment (SROI) for investors – helping investors understand the social value they create through their investment activity.

This supplement explains how SROI can be used by investors if they want to integrate SROI approaches into investment decisions and is designed to be read in conjunction with *A guide to Social Return on Investment*.[1]



1 Available from www.thesroinetwork.org





1 Social value, SROI and investment

Social Return on Investment (SROI)

Social Return on Investment (SROI) provides investors with a consistent framework for making better informed decisions. Social investors are interested in the change that their investments create and SROI is designed to help identify and manage this change. Investments in different organisations create many different types of social value and SROI can provide different measures of social value that arise from applying a standard method.

For investors, SROI provides a means to:

- map the full range of impacts a potential investee will create across wider social, environmental and economic outcomes, recognising positive and negative impacts and taking account of deadweight and attribution;
- value these impacts in order to make a comprehensive and informed assessment about value for money;
- build capacity that aims to help organisations improve as well as prove their effectiveness;
- frame the discussion on where these outcomes are relevant to the investor.

Challenges for social investors

SROI can help social investors overcome several challenges:

- how the social value being created in a wide range of diverse activities can be related to measures of social value used by the investor;
- how investees can be encouraged to manage outcomes in ways which do not affect the viability of their businesses;
- how outcomes can be attributed to the delivery of goods or services financed by the investment.

The challenges are not the same for all sources of finance. For example, for social lending, it would be difficult to enforce repayment if outcomes were not achieved and any additional transaction costs of monitoring social value could make the loan uncompetitive with other sources of loan finance.

2 Integrating SROI into equity investment and grants

In general the investment process covers three stages:
- Application;
- Appraisal;
- Monitoring.

Application

The most effective place to start is at the application stage. If an investor is using SROI, then investees need to start thinking about how they will use the finance to create value, based on the principles that underpin SROI. This does not need to be onerous and is often a rephrasing or a reordering of existing questions. SROI is interested in the value of the changes that happen to different stakeholders and so investees should be able to start thinking about value, change and stakeholders right from the start. For example, investees should be able to provide information on who their stakeholders are, how their stakeholders expect to change and how the organisation will measure this change. Putting the right measures in place from the outset is crucial. The emphasis needs to be on measuring outcomes rather than outputs and organisations must be properly resourced to do this.

Appraisal

As a potential investment progresses through the due diligence process, SROI can help:
- allow more clarity about the relationship between financial and social return and on the innovations that provide a competitive advantage;
- appraise the quality of the business on the assumption that a management team that understands and manages social value will be a more effective team.

The first of these is perhaps the most important. At some point in the due diligence process, the completion of a forecast SROI provides a clear statement of what social value is being projected, for whom and with what value. Importantly, it also defines the requirements for management systems and potentially for governance.

An organisation will need to have in place the systems that will generate information to be able to report, and therefore manage, social value. As SROI identifies value for different stakeholders, it will be critical that these stakeholders are involved. The organisation will need to show that it is capable of responding to its stakeholders and this implies that they need to be involved in governance in an appropriate way. Implementation of changes could be part of the investment conditions.

An understanding of the social value being created in financial terms will help prioritise changes and can help the business manage risks and opportunities that are not currently part of trading activity. For example, recognising potential impact on different stakeholders can help identify new markets.

This approach shows the relationship between the investee's objectives and the creation of value. The approach, therefore, ensures that any changes to the investee that may be required are seen to be relevant.

Although SROI results in a ratio, which is the ratio of social return to investment, it is important to be clear where and how this should be used. The ratio by itself should not be used to compare organisations. It is part of the wider story of value that has been described using SROI and it is the comparison of these wider stories that will be useful. In the same way that a financial investor would take a range of different types of information into account, the ratio should not be over-emphasised. It is the starting point, rather than the final destination, in a discussion about value.

The development of a proxy database, as part of the SROI Project, will help with comparability; but even then it should be approached with caution. Even when comparing a forecast return with an evaluative return in the same organisation, it is the assessment of the underlying reasons for the difference that is useful. However, over time, it will be possible to compare the rate at which different ratios change to compare the rate of improvement of different investees.

For more information on the database see **www.sroiproject.org.uk**.

Monitoring

Where the investor has maintained an ongoing relationship as part of the conditions for investment, it is possible to both monitor performance on the creation of value and to provide ongoing support

Where changes to systems are required, the investor can monitor compliance as the first step in being able to compare forecast SROI against actual SROI. Where a business embeds SROI, it is possible to report on performance against budget on both finances and social value.

In addition to the support that can help the business achieve its financial targets, SROI provides a framework for the investor to support the business to achieve its social and environmental targets.

3 Sources of support

There is a range of support available to help you use SROI, including *A guide to Social Return on Investment*, training, consultancy and an indicator bank. The following websites are useful sources of this support.

The SROI Network website contains a range of SROI resources including *A guide to Social Return on Investment*, a full description of the principles of SROI and details of SROI training courses: **www.thesroinetwork.org**. If you have an SROI report you would be happy to share, please send it to the SROI Network and they will include it in their SROI library.

The website of the Scottish Government funded SROI Project contains a range of SROI resources, which will include an indicator bank and information on accredited SROI training: **www.sroiproject.org.uk**.

new economics foundation's website: **www.neweconomics.org**, contains a range of relevant resources, including *Investing for social value: measuring social return on investment for the Adventure Capital Fund*, Lawlor, E. Murray, R et. al.

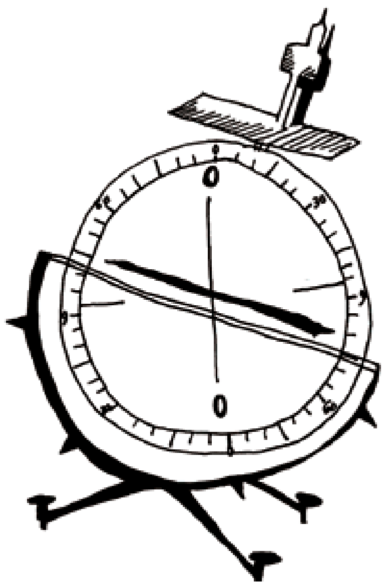
nef consulting provides SROI resources and consultancy for third sector organisations, including details of SROI training: **www.nef-consulting.co.uk**.

Charities Evaluation Services' website contains a range of resources on evaluation and outcomes assessment in the third sector: **www.ces-vol.org.uk**.

National Council for Voluntary Organisations' website contains information and advice on strategy and impact: **www.ncvo-vol.org.uk/strategy-impact**.

New Philanthropy Capital's website contains a range of resources relevant to measuring social value, including SROI, well-being, reporting to funders and full cost recovery: **www.philanthropycapital.org**.

For more information on the **Office of the Third Sector's Measuring Social Value project** go to **www.cabinetoffice.gov.uk/third_sector/Research_and_statistics/measuring_social_value.aspx**.



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