

EIB Group Risk
Enhancement
Mandate

**Evaluation of the
Social Impact
Accelerator**

September 2020



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Introduction

- This report examines the design, implementation and achievements of the Social Impact Accelerator (SIA).
- The SIA was one of six products funded under the EIB Group Risk Enhancement Mandate (EREM).
- EREM was created in 2013 against the backdrop of a weak economic outlook. The EREM objectives were to increase access to finance for European small and medium enterprises (SMEs) and small mid-caps, and to support the development of financial markets.
- EREM was implemented by the EIF between 2014 and 2018.
- The SIA was initially set up in June 2013, with commitments from the EIF (€50 million), Crédit Coopératif (€1 million) and Deutsche Bank (€1 million). The Finnish group SITRA and the Bulgarian Development Bank also committed €1 million each in the final closing, together with EREM's funding.
- In December 2014, EREM was used to significantly scale up the SIA via an additional commitment of €189 million (8.2% of approved EREM finance).
- This increased the total budget of the SIA to €243 million.
- Under the SIA, the EIF provided equity and quasi-equity financing to social impact funds targeting social enterprises in Europe.
- As of 31 December 2018, the EIF had committed €148 million to 14 impact funds across eight Member States.

2

EIB Group Risk Enhancement Mandate Social Impact Accelerator

SIA features

EIB Group and four external investors
(Crédit Coopératif, Deutsche Bank, Finnish group SITRA and the Bulgarian Development Bank)

Social Impact Accelerator ("SIA") Fund-of-Funds

Investments of €5-15m representing a maximum share of 49.9%.

Social Impact Fund #1

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Social Impact Fund #1

### Eligible Social Impact Funds

- finance commercially viable social SMEs in the European Union
- report on their social impact
- provide investee social enterprises with supplementary advisory support

SIA invested in 14 impact funds across eight Member States: the United Kingdom, France, Germany, Italy, Denmark, the Netherlands, Spain and Belgium

### Eligible Social Enterprises

Investments (mostly equity and quasi-equity) into social enterprises following the Social Impact Funds' own guidelines

Social Enterprise 1...

Social Enterprise n

Social Enterprise 1...

Social Enterprise n

- Must meet the SIA's definition of a social enterprise:
- be an SME as per EU definition
  - seek to achieve social impact and measure it
  - aim towards financial self-sustainability
  - be managed in an accountable and transparent way

Impact funds supported a total of 140 social enterprises at different stages of development and across a variety of sectors

Impact metrics at three levels to measure the progress towards predefined social targets

# Intervention logic of the SIA

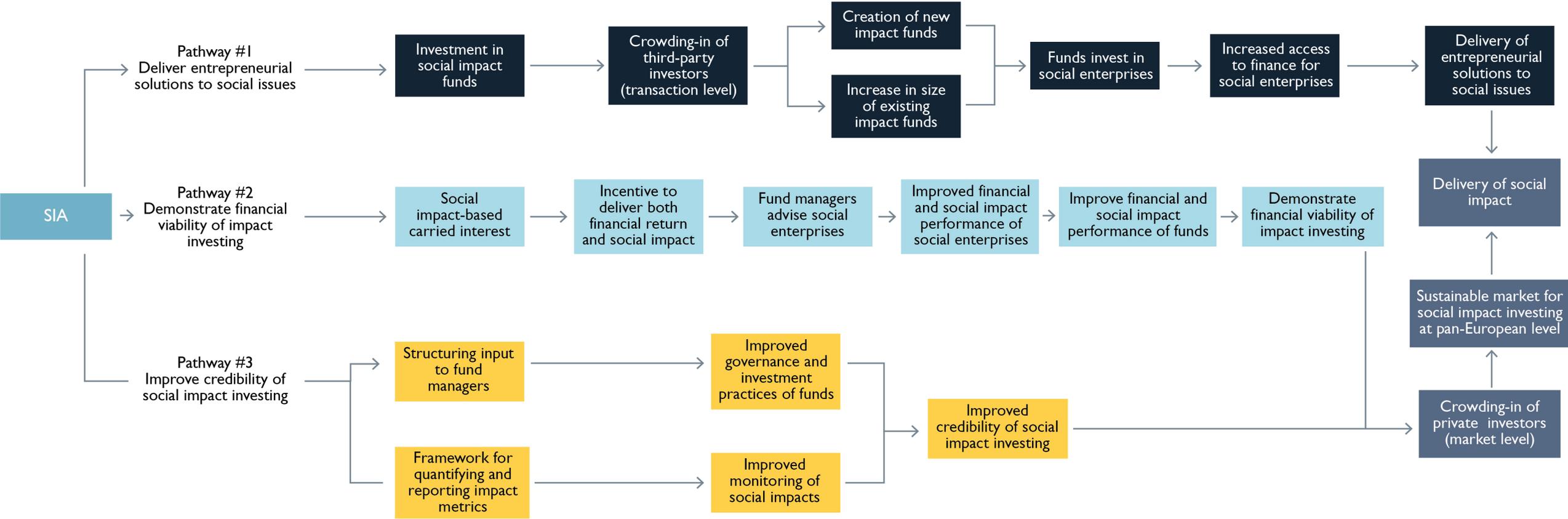
The following slides describe the intervention logic of the SIA. An intervention logic is essentially an illustration of how an intervention is intended to contribute to achieving a number of high-level objectives. It links the main activities carried out to their expected effects and illustrates how these were, in turn, intended to contribute to the high-level objectives. It also identifies the main assumptions that should hold for the effects to occur.

The SIA intervention logic is presented in the form of a diagram (see next slide). This is then followed by three slides explaining in more detail the three pathways identified in the diagram and listing the main underlying assumptions for each pathway.

The intended effects presented in the intervention logic are not all under the EIF's control. As we move from left to right in the diagram, other external factors start to play a much more significant role. Therefore, while the SIA was intended to contribute towards these high-level objectives, it was never expected to generate them alone.

The main objective of the evaluation was to test this intervention logic, including its underlying assumptions. The key findings of the evaluation are presented in section 4.

# SIA intervention logic



*Pathways 1-3 are explained on the next slides*

# Pathway **1** of SIA intervention logic: contribute to the delivery of entrepreneurial solutions to social issues

The EIF intended to address a market gap by increasing the supply of capital available for investment in social enterprises. It did so by investing in social impact funds. The EIF's presence in these funds was expected to crowd in additional investors at the transaction level. The investments made by the EIF-backed funds were, in turn, expected to enable social enterprises to scale up their activities and deliver entrepreneurial solutions to social issues.

## KEY ASSUMPTIONS UNDER PATHWAY 1:

- a) Fund managers are committed to achieving social impact.
- b) There is a lack of adequate funding for social enterprises.
- c) Without the SIA, funds would not have been established at all or only on a smaller scale.
- d) The EIF's presence has a positive signalling effect for other investors.

## Pathway **2** of SIA intervention logic: contribute to demonstrating the financial viability of impact investing

The EIF requested the introduction of a social impact-based carry mechanism in all the funds it backed. This means that fund managers are only entitled to receive the carried interest (i.e. an additional form of remuneration) if, in addition to delivering a significant financial return, they also achieve their predefined social impact targets. This was expected to incentivise fund managers to pay due attention to both financial return and social impact. Fund managers were, in turn, expected to advise social enterprises and provide support to enable them to improve their financial and social performance. The positive financial and social performance of the enterprises translates into positive performance of the funds. This was, in turn, expected to help demonstrate the financial viability of impact investing and thereby attract other investors.

### KEY ASSUMPTIONS UNDER PATHWAY 2:

- a) The assisted funds will achieve a positive financial return.
- b) Without the social impact-based carry mechanism, social impacts delivered by the enterprises would be lower.
- c) Fund managers have the capacity to identify and support promising social enterprises.

# Pathway **3** of SIA intervention logic: contribute to improving the credibility of social impact investing

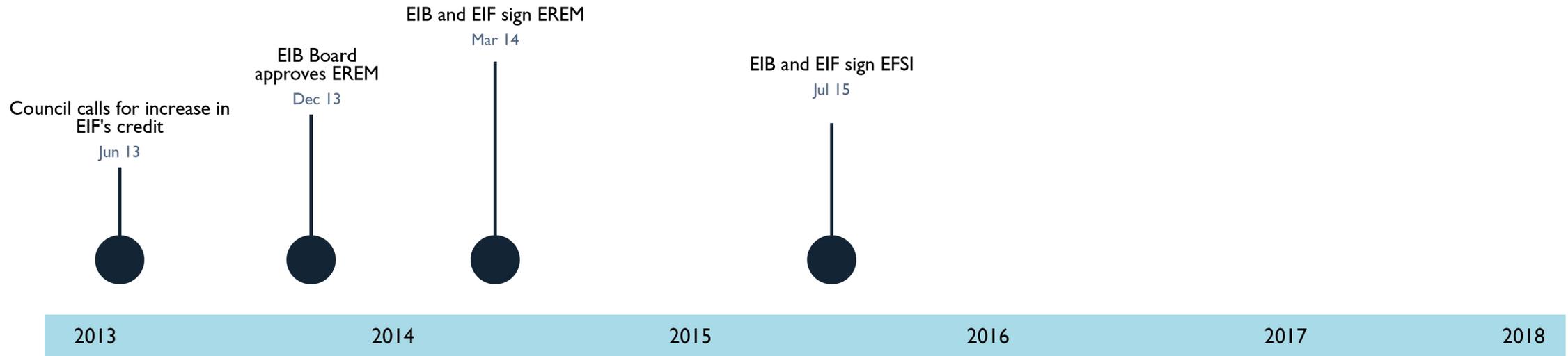
The structuring input (a form of advice) provided by the EIF was intended to improve the funds' governance and investment practices. The social impact measurement methodology introduced by the SIA was intended to help improve monitoring of social impacts delivered by the supported social enterprises. All these effects ultimately aimed to improve the credibility of social impact investing, thus making it more attractive to other investors.

## KEY ASSUMPTIONS UNDER PATHWAY 3:

- a) Fund managers value the EIF's structuring input and market-building activities.
- b) The impact measurement framework is applied in practice by fund managers.
- c) Social impact measurement indicators are good quality and reliable.
- d) EIF-driven governance changes make funds more attractive to investors.
- e) The EIF's impact measurement methodology improves the credibility and attractiveness of impact investing.

# Implementation timeline

- The SIA Agreement between the EIB and the EIF and the first **contract with** an SIA-backed fund manager **were signed concomitantly in December 2014**, shortly after the signature of the EREM Framework Agreement. This was possible because the SIA was already operational before EREM was initiated. EREM topped up the SIA significantly, transforming it from a pilot initiative into a fully developed product.
- The first disbursement at the intermediary level took place one year later, in December 2015, reflecting the time needed by the intermediaries to get organised before starting to invest.



\* EREM funds allocated to the Social Impact Finance (SIF) Instrument increased the EIF's commitment to an existing initiative – the Social Impact Accelerator (SIA).



# 3

## Methodology

# This report is based on...



## Desk research covering:

- **High-level documents:** EREM Framework Agreement and SIA Agreement.
- **SIA transaction-related documentation for all 14 supported funds:** 1) appraisal authorisations, 2) independent opinions, 3) due diligence reports, 4) requests for approval, 5) minutes of EIF Board meetings, 6) contractual documents and side letters, 7) monitoring reports submitted by fund managers to the EIF, 8) EIF monitoring reports on the SIA, and 9) documentation available on the websites, as well as other data available online.



## Literature review of available studies on the impact investment market in the EU:

- Reports by the EIF market research team.
- Studies by the European Commission (2014) and the Joint Research Centre (2018).
- Analysis conducted by other market players (e.g. Big Society Capital, Deutsche Bank, Morgan Stanley).



## Online surveys:

- 12 SIA-backed fund managers (100% response rate). *N.B. under the SIA, 12 fund managers are managing 14 funds.*
- 42 of 101 social enterprises backed by SIA-supported funds (42% response rate).



## In-depth case studies of five of the 14 SIA transactions:

- Case studies were based on a wide range of sources including the documentation of focal funds, in-depth interviews with their managers, survey responses from these fund managers and fund investees, interviews with EIF co-investors in those funds, etc.



## Interviews with wholesale investors:

- Interviewees included a limited number of SIA co-investors, as well as other social impact investors who did not invest in the SIA-backed funds but have knowledge of the EIF's role in the social impact market.

# 4

## **Key findings**

# The SIA was and continues to be a highly relevant product

The main objectives of the SIA were to enhance access to finance for social enterprises in the European Union and to contribute to developing an impact investment market at the pan-European level. The evaluation finds that this objective was highly relevant in 2014 (when the SIA was set up) and will continue to be so for the foreseeable future.



- **A study commissioned by the European Commission shows that the EU impact investment market was broadly classified as “emergent” in 2014.** There were very few social impact funds established in the European Union, while there was high and increasing demand for finance from social enterprises. A range of other sources also concluded that access to finance was challenging for social enterprises.
- **A 2018 study by the Joint Research Centre reported growth in the social investment market since 2014 but concluded that much more development is needed at the pan-European level.** While 16 Member States were still classified as “1” (low maturity), there were already seven Member States classified as “2” (medium maturity) and five markets classified as “3” (high maturity), namely the United Kingdom, Italy, France, Germany and Belgium. It is therefore clear that much more needs to be done to achieve a sustainable social investment market at the pan-European level.
- **The literature also underlines the important role for the public sector in establishing and growing the impact investment market.** In many countries public authorities alone are unable to effectively address the scale and range of social issues, such as provision of childcare, rehabilitation of ex-offenders, and provision of social care or housing. Social enterprises can therefore make an important contribution in these domains. The United Kingdom’s experience demonstrates the important enabling role of the public sector in establishing and growing the impact investment market.

# The SIA was well designed and implemented for helping to establish and expand the impact investment market in the European Union



- **For each transaction the EIF thoroughly assessed the relevance to market contexts.** The transaction documentation shows that considerable thought was put into selecting the funds that could make a solid contribution to developing the impact investment market in their respective countries.
- **The SIA was initially deployed in the more developed EU markets and then gradually expanded to less developed markets.** The first investments were made in social impact funds located in France, the United Kingdom and Germany, followed later by investments in EU countries where impact investing was non-existent (e.g. the Netherlands, Denmark, Hungary and Spain). This is largely explained by the demand-driven approach applied by the EIF. In the opinion of the evaluation team, this was appropriate for the following reasons:
  - The SIA aimed to demonstrate that social investments can also generate an adequate financial return. This was more likely to be achieved by initially supporting more experienced social impact fund managers.
  - The investments in more experienced fund managers also created opportunities for the EIF to capitalise and transfer knowledge to other less experienced fund managers. Some of this knowledge (e.g. on monitoring social impact) was transferred via the EIF's structuring input.
- **The EIF supported shifts from both philanthropy and traditional venture capital to impact investing.** The SIA portfolio of investments includes funds with a previously philanthropic background and funds that moved from traditional venture capital to impact investing. This resulted in a balanced portfolio of investments attracting both managers with prior knowledge of social aspects and managers with knowledge of financial aspects.
- **Five of the 14 SIA-backed funds were managed by first-time teams.** The supported first-time teams are also spread across several countries (the United Kingdom, Germany, Denmark, Hungary and the Netherlands). This shows that while the EIF aimed to select the most capable fund managers who can deliver on the SIA objectives, they also endeavoured to encourage new teams to join the impact investment market.
- **However, the opportunities created by this approach under the SIA have not been fully exploited.** Two of the interviewed fund managers felt that more could be done by the EIF to promote collaboration among SIA-backed funds, thereby encouraging knowledge transfer and networking in the market, which was also one of the SIA's initial objectives.

# In the absence of SIA investment, the funds would have been much smaller in size. Many funds would not have closed or would have struggled to operate



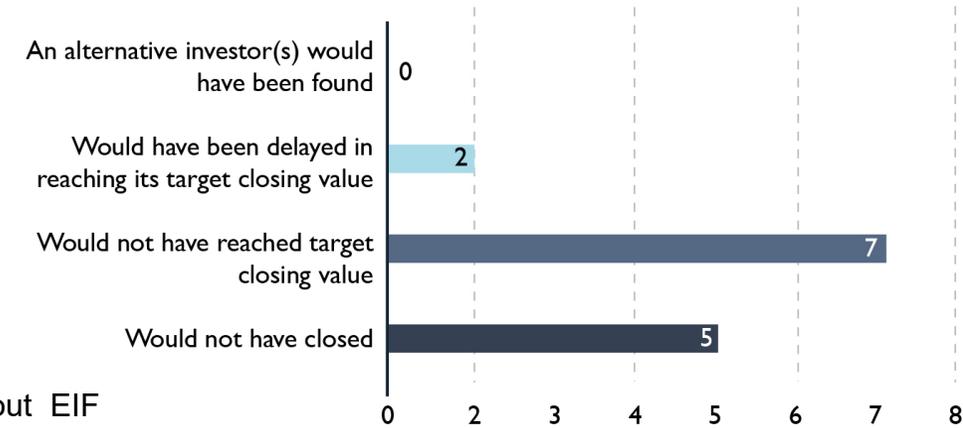
- **None of the SIA-backed funds believed they would have been able to find an alternative investor to the EIF.** They believed that, without the EIF, their fund would have either not closed (five cases) or would not have been able to reach its target closing value (seven cases).
- **The main reason is the absence of other public and/or private investors willing to invest at this scale.** When asked why their funds would not have closed or reached the target closing value, the fund managers indicated that no other public or private investors were willing to invest at the scale the EIF did. They also said that eight out of 12 fund managers remarked that other investors would have reduced their contributions, making the funds even smaller.



## The evidence from the case studies confirms the survey results:

- In all five cases reviewed, the funds would have been much smaller in size without EIF investment.
- Some fund managers believed they may have been able to rely on other smaller investors to partially compensate for the EIF's absence. However, in all cases this would have taken more time, delaying the start of the investment process and increasing the fundraising costs.
- One fund would not have been able to operate effectively because they could not afford to employ a good investment team. The other four funds would have been able to operate but with a significantly less skilled team. As one fund manager commented, "a sub-scaled fund is a sub-skilled fund."
- Institutional investors would have reduced their contributions in the EIF's absence due to the 10% exposure limit that most of them apply. Since it is clear in all cases that fund size would have been much smaller without the EIF, those institutional investors applying the 10% rule would have reduced their contributions accordingly to stay within their maximum exposure.

## What would have happened in the absence of EIF investment? (multiple answers possible)



Source: Survey of SIA-backed fund managers



- The documentation review also identified examples of SIA-supported funds trying unsuccessfully to close prior to EIF investment. They only succeeded following the investment by the EIF.
- The evaluation also found examples of other investors committing subject to a minimum fund size, which would have been very difficult to reach without the EIF investment.

# SIA provided a positive signal to other investors



- All 12 fund managers strongly agree that the EIF investment signalled the quality of their fund.
- Nine out of 12 fund managers agree and/or strongly agree that the EIF's presence attracted private investors that would not have otherwise invested in the fund.
- Nine out of 12 fund managers agree and/or strongly agree that other investors reduced their due diligence given the EIF's presence.

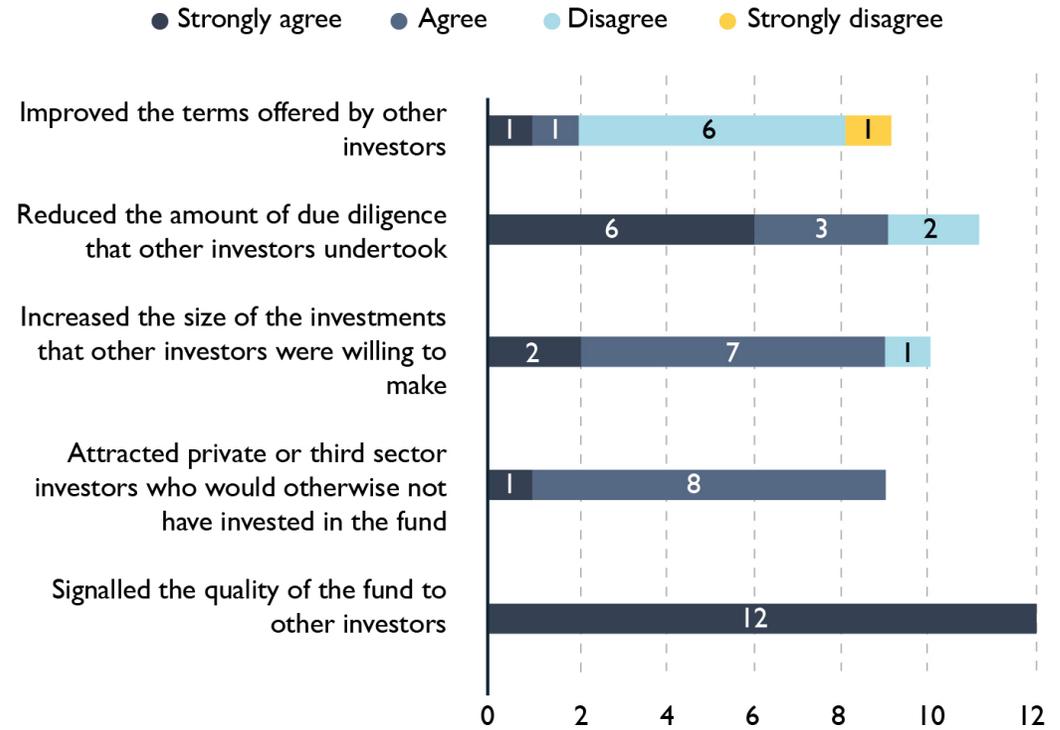


- **All five case studies confirm that EIF investment signalled the quality of the fund to other investors.** This is largely due to the EIF's reputation as a large professional organisation with many investments and extensive experience, which make the EIF well trusted among investors. This trust means that smaller organisations (such as some family offices) that either lack capacity for thorough due diligence or do not see the need for it are more willing to invest in a fund if the EIF is present.



**The interviewed co-investors agreed that the EIF's presence signalled the quality of the funds.** They believed the EIF's experience of venture capital and the breadth of its investments make the EIF a serious organisation, such that any fund it invests in should be taken seriously. The co-investors did concede that they would have invested in those funds anyway, and have performed due diligence, as per standard practice. Nonetheless, the EIF investment raised their confidence in the funds.

## To what extent do you agree/disagree with the following statements on the impact of the EIF?



Source: Survey of SIA-backed fund managers

# There is no evidence of the SIA having a crowding-out effect

The analysis presented on the previous slides clearly suggests that the EIF acted as a catalyst and significantly helped the fund managers in their fundraising process. Nevertheless, the evaluation tried to identify cases where the EIF's presence may have unintentionally crowded out other investors. This was assessed using two different lines of enquiry:

- 1) Whether the sheer size of the EIF investments may have resulted in the funds reaching a size considered excessive by some investors, thereby dissuading them from investing in the funds.
- 2) Whether some of the governance changes induced by the EIF via its structuring input or the association of the EIF with public sector funding may have deterred some investors from investing in those funds.

As illustrated below, the evaluation could not find any evidence supporting either of these hypotheses.



**The documentation review suggests that the EIF has been wary of the potential risk of crowding out other investors and appropriately managed this risk:**

- The SIA allowed for investments up to 49.9% of a fund's shareholding. SIA participation reached this maximum in only four of 14 cases. In all other cases it was significantly below this level (20-35%). In all four cases where the SIA invested 49.9%, the fund managers were clearly struggling to reach the minimum size.
- The funds that closed at a higher size typically had lower SIA participation. The evaluation also noted that some of the renowned SIA-backed funds received considerably lower SIA investment compared to other funds.
- The evaluation could not find any cases where investors committed subject to a maximum fund size. On the contrary, investors typically committed subject to a minimum fund size to avoid spreading resources too thinly over a large number of funds, which would, in turn, result in high management costs for the investors. This strongly suggests that the EIF investments did not crowd out other investors.

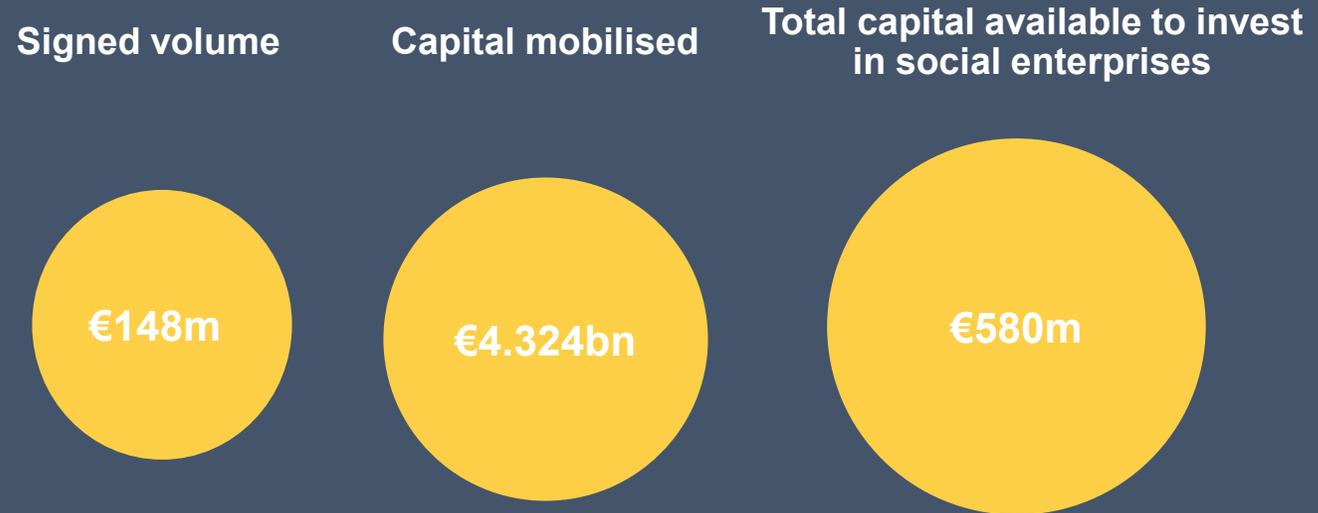


The case studies do not show any evidence that changes proposed by the EIF were received negatively by other investors. In one case some investors were unsure about the EIF's requirement to use the social impact-based carry mechanism, and were concerned this may divert attention from financial performance. However, this mechanism was seen neither by the investors nor the fund managers as a factor that could potentially crowd out investors. Similarly, none of the interviewed fund managers and co-investors raised any concerns that the EIF's association with public sector funding may have crowded out investors.

# The SIA has increased the availability of finance for social enterprises beyond initial expectations

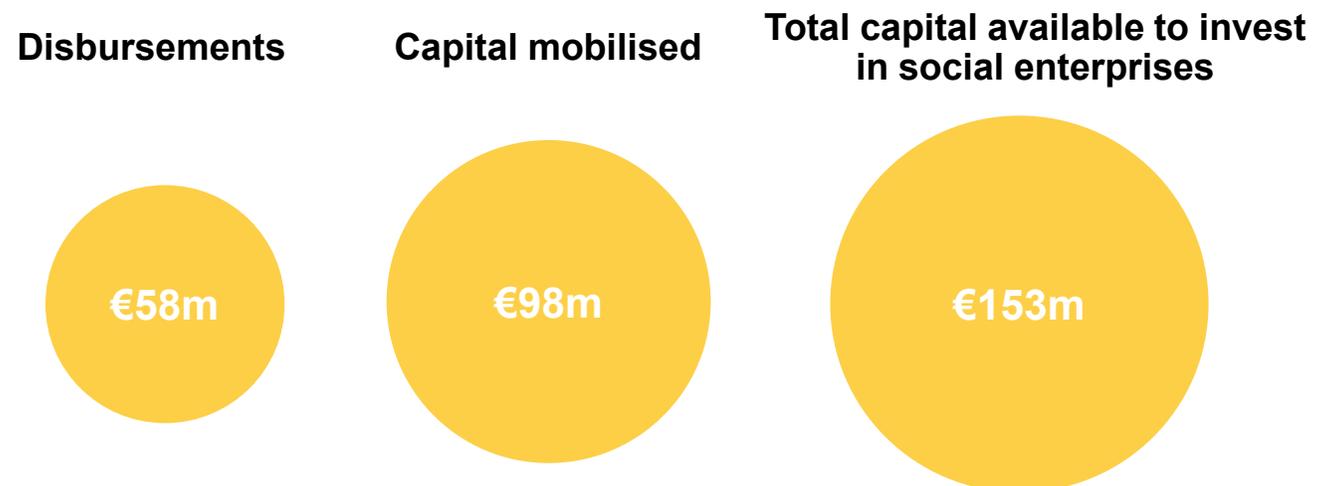
The SIA invested in 14 funds located in eight EU Member States. The prior expectation was that these funds would invest in social enterprises an amount double the size of the SIA investment. At the end of 2018, the total capital made available by the SIA-backed funds was approximately €580 million, which is approximately four times the amount invested by the SIA.

*N.B. Total capital available = signed volume + capital mobilised (from other investors).*



Regarding the funding that has already reached the 140 supported social enterprises, the amount is three times the amount disbursed by the SIA.

*N.B. Total capital invested = SIA disbursements + capital mobilised (from other investors).*



# Most of the SIA-backed social enterprises claim they would not have been able to access finance from other sources under the same conditions and within the same time frame



**The SIA did not specifically aim to support social enterprises that could not otherwise access other sources of finance.**

SIA-backed fund managers were not expected to invest in social enterprises that faced difficulties accessing finance. Instead, they were expected to invest in the most promising enterprises that could deliver both social impact and financial return. This is coherent with what the SIA aimed to demonstrate, namely that investments in social enterprises can generate an adequate financial return, thereby attracting new investors and advancing this market segment towards sustainability. Despite this, for most supported social enterprises, the SIA-backed investments were important for financial and non-financial reasons, as explained below.



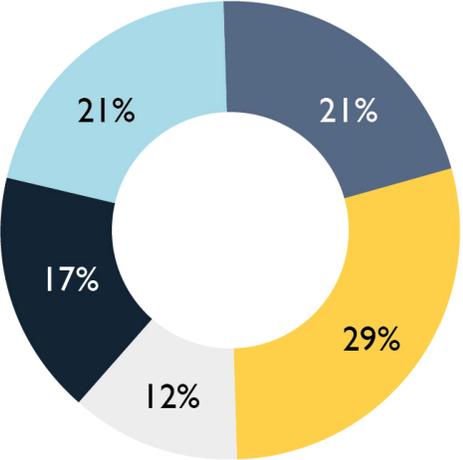
**58% of the social enterprises highlighted the financial importance of the SIA-backed investments.** While most of the social enterprises would have had access to an alternative source of finance, this would typically not have been under the same conditions or within the same time frame.

**21% of the social enterprises did not believe the SIA-backed investments were critical from a financial standpoint but they did report a range of non-financial benefits.**

These social enterprises would have been able to obtain the same sized investment from another source around the same time, but preferred the SIA-backed funds because they:

- offered other non-financial benefits, such as business support and networking;
- demonstrated commitment to long-term impact;
- offered better terms and conditions.

## What would have happened if your organisation had not received investment from the SIA-backed fund?



- Obtained the same sized investment from another source, around the same time
- Obtained the same sized investment from another source, but with a delay
- Obtained a smaller investment from another source
- Would not have obtained an investment/loan
- Don't know/Prefer not to answer

Source: Social enterprise survey



### The case studies confirm the survey results:

- Later-stage investors in particular felt that many of their investees could have got funding from mainstream venture capital or angel investors.
- Social enterprises preferred SIA-backed funds because these funds are managed by social investment specialists who better understood social enterprises' needs.

# SIA-supported enterprises delivered entrepreneurial solutions to social issues

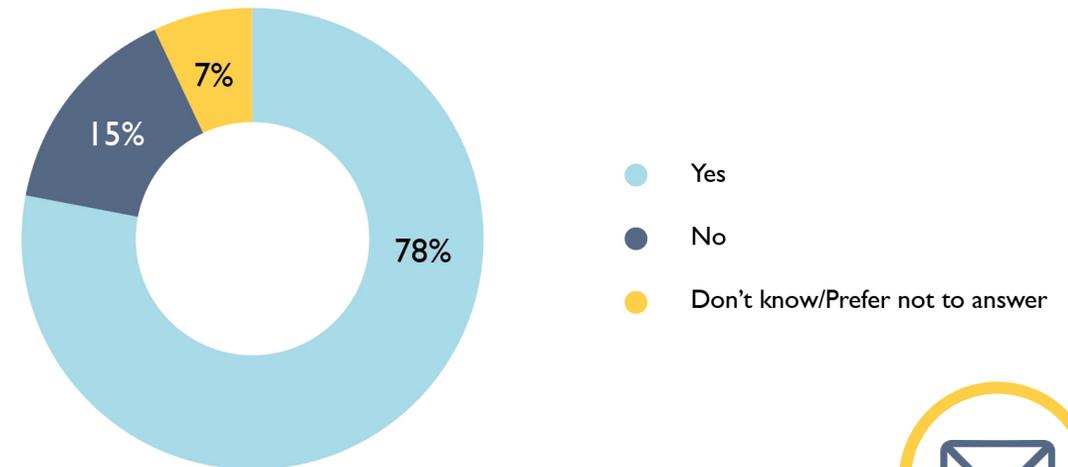


- The SIA aimed to contribute to delivering entrepreneurial solutions to social issues by supporting funds that invest in enterprises in one or more of the following categories:
  - Seek to resolve a social issue through supplying a specific service or product.
  - Deliberately employ marginalised people.
  - Operate in a socially deprived area creating local growth and opportunities.
- 13 of the 14 funds in the SIA portfolio aimed to support companies that seek to solve a specific social issue. Four of the 14 funds also aimed to support companies falling under the other two categories, while only one fund focused exclusively on creating growth in socially deprived areas. Therefore, the vast majority of social enterprises in the SIA portfolio focused on solving social issues (category 1).
- The documentation review and survey results demonstrate that the vast majority of supported enterprises clearly specify the social issue they seek to address and provide very convincing arguments on how their business aims to do good.



Selecting promising social enterprises is the key job of the funds, and evidence suggests they are careful with their investment decisions in terms of both social and financial performance. The funds also provide social enterprises with support that they typically find useful, such as in planning, recruitment and resourcing.

## Does your organisation consider itself to be a social enterprise?



Source: Social enterprise survey



## Social issues addressed by SIA-backed social enterprises (examples):

- “Help rare disease patients develop access to new treatments”
- “Offer quality home care services to the elderly”
- “Cognitive behavioural therapy for sufferers of mental health disorders”
- “Train and hire (50 plus) unemployed people and reduce CO<sub>2</sub> emissions using electric cars”
- “Defend web users from online hate”
- “Help police to identify serial criminals”
- “Empower people and recycle materials”
- “Mentor youth and refugees”
- “Help children develop digital skills”
- “Help to reduce water usage”

Source: Social enterprise survey

## Only one of the 14 SIA-backed funds invested in companies that deliver positive social impact but may also be associated with negative social impact



- This fund invested in companies that operate in disadvantaged urban areas, creating jobs and providing training for local residents. Those companies also contribute to the budgets of local authorities (by paying local taxes) and therefore help them increase revenues. The fund invested in a range of retail businesses (e.g. supermarkets, flower shops, car repair shops) but also in a range of traditional fast-food restaurants.
- While this fund undoubtedly brought benefits to those disadvantaged urban areas, the investments made in the fast-food restaurants can also be considered harmful to those communities. A 2014 study by the World Health Organization ([link](#)) found a strong and positive association between fast-food consumption and obesity, and suggested that hindering the spread of fast-food consumption might help to mitigate the obesity epidemic. The WHO study also points to numerous other studies that confirm this association.
- The literature review and interviews with fund managers confirm that one pressing issue for the impact investing market is the lack of clarity on what constitutes a social enterprise. This issue clearly cannot be solved by the EIF. However, investments such as those referred to above do not help to clarify the concept.
- This isolated case suggests a potential risk of conflict between the three categories of companies supported under the SIA (see the first bullet point on the previous slide). For instance, companies that hire marginalised people or those investing in deprived areas might deliver goods and services that can be seriously associated with doing harm. While all companies deliver some form of negative social impact, this must not be significant in the case of social enterprises.

## The EIF typically provided structuring input (defined as a form of advice) on a wide range of governance and investment decision-making aspects under the SIA



### The EIF's reported inputs were as follows:

- Help to sharpen funds' investment strategy.
- Increase awareness of structural features in the design of the fund, enabling improvement of the return profile and thus enhancing funds' fundraising potential.
- Influence on the fee structure and the target fund size, making the funds a more attractive proposal for other investors.
- Help to improve funds' governance structures.
- Introduction of social measurement metrics and the social impact-based carry mechanism.
- Introduction of key-person clauses, thereby limiting the risk of key staff turnover.
- Changes in the duration of the investment period.
- Impact on operating expenses, improving the return prospects and consequently the fundraising potential of the funds.
- Revision of the fee offset structure.
- Introduction of incentive schemes to improve the alignment of interests between investors and fund managers.
- Help to restructure the team set-up of the funds.

# The structuring input provided by the EIF was appreciated and resulted in positive change

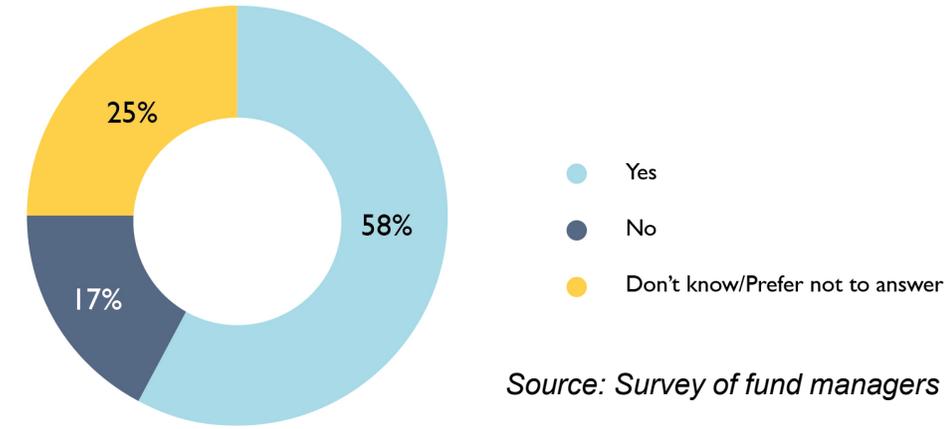


- The survey of SIA-backed fund managers suggests that the majority of funds received structuring input from the EIF.
- The vast majority of the funds that received structuring input found it to be very useful.
- Those fund managers also reported that they introduced changes as a result of the EIF structuring input.



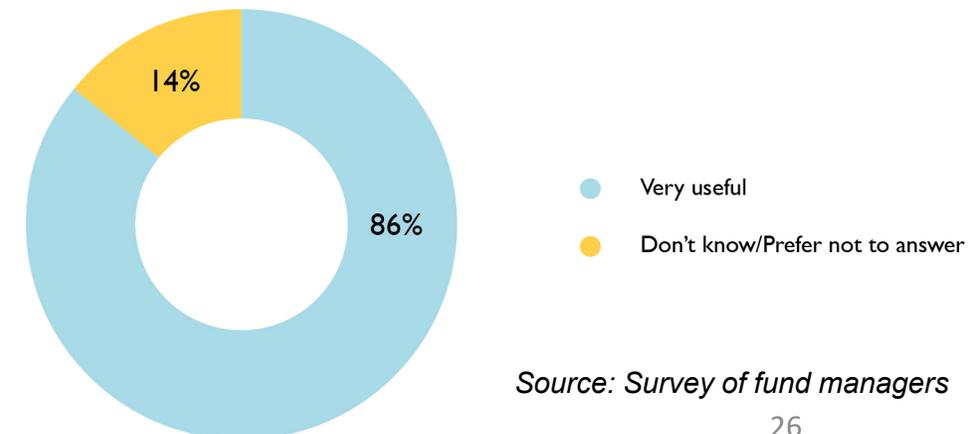
- There was mixed evidence in the case studies, doubtless reflecting the prior experience of the funds (which was mixed), their internal cultures and their willingness to adopt what the EIF presented as good practice.
- The EIF encouraged some changes in governance and investment decision-making that were valued by the fund managers and that they believed had made them more professional. Examples include:
  - Support for improving the monitoring of social impact (this was particularly appreciated).
  - Support for restructuring team set-up.
  - Introduction of incentive schemes to improve the alignment of interests.
  - Help to sharpen the investment strategy.
- The EIF also induced a number of changes that were less appreciated by the fund managers but may have positively affected fund governance. These were:
  - Introduction of key-person clauses.
  - Emphasis on the independence of the management team.
- However, while the majority of funds appreciated EIF inputs overall, some downplayed the EIF's role, believing that the changes were minor and might well have been made anyway.

## Did your organisation receive structuring input from the EIF?



Source: Survey of fund managers

## How useful was the advice you received?



Source: Survey of fund managers

## One of the changes introduced by the EIF in all SIA-backed funds was the so-called “social impact-based carry mechanism”



- Under the social impact-based carry mechanism, a fund manager is only entitled to receive the carried interest (an additional form of remuneration) if, in addition to achieving financial performance that surpasses a predetermined hurdle rate, the fund also achieves certain social impact targets.
- Social impact performance is measured and judged using predefined indicators and targets set at the social enterprise level and then aggregated at the fund level using predefined weightings for each indicator.
- The social impact-based carry mechanism thus adds an additional condition for distribution of the carried interest, compared to the traditional practice in venture capital markets where only financial performance is considered.
- The mechanism was, therefore, expected to incentivise the fund managers to focus on reaching financial targets and achieving social impact targets.

# The social impact-based carry mechanism did not influence the magnitude of social impact but did strengthen monitoring of and helped maintain focus on social impact



- Nine of the 12 fund managers believed that the social impact-based carry mechanism had a moderate or large impact on the quality of the monitoring of social impact.

- However, the fund managers were less convinced that the social impact-based carry mechanism affected the magnitude of the social impact achieved by their investees.



- The documentation review and interviews with the EIF and fund managers show that the mechanism can impact the revenues of fund managers but not those of entrepreneurs, who are ultimately responsible for managing the business. Therefore, the incentive is not passed to the entrepreneurs.

- The evaluation also noted that the social impact data reported by fund managers are not independently verified, which means the data may not always be fully reliable. However, it would be very difficult to introduce such verification without impacting on management costs.

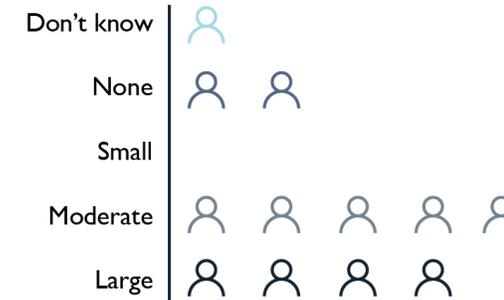


- None of the case studies provided evidence that the social impact-based carry mechanism affected the social impacts achieved. This was primarily because the fund managers were already very committed to supporting their investees. The achievement of social impact was also mostly down to the motivation and enthusiasm of the social entrepreneurs, who would not change their behaviour according to how the fund managers earned money. Indeed, many of the social entrepreneurs did not even know that the mechanism existed.

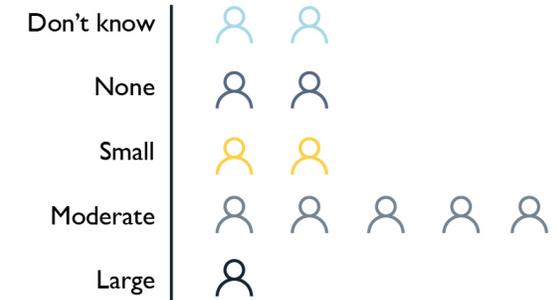
- However, the case studies suggest that the mechanism positively influenced the quality of social impact monitoring and had other positive effects such as enhancing the credibility of fund managers in the eyes of other investors and of their investees. The case studies also suggest that the enhanced attention paid to monitoring caused social entrepreneurs to focus their minds on the impact they achieve, rather than taking it as a given.

## What impact (if any) did the social impact financial incentives used by the EIF have on the following aspects of the delivery of the fund?

The quality of monitoring of investees' social impact



The magnitude of investees' social impact



Source: Survey of SIA-backed fund managers

## Were there any negative impacts of the social impact financial incentives used by the EIF?



Source: Survey of SIA-backed fund managers

# The SIA was generally managed in a very efficient manner but contracting was often slower than expected



**The SIA helped to quickly get money to the social investment market.** The EIF topped up an existing pilot product for which processes and procedures were already in place. This facilitated the speed of delivery and helped to achieve economies of scale.

**Despite being very rigorous, the due diligence process was conducted relatively swiftly.** Completion of a due diligence report took on average 3.1 months. There were some differences between transactions but no major discrepancies.

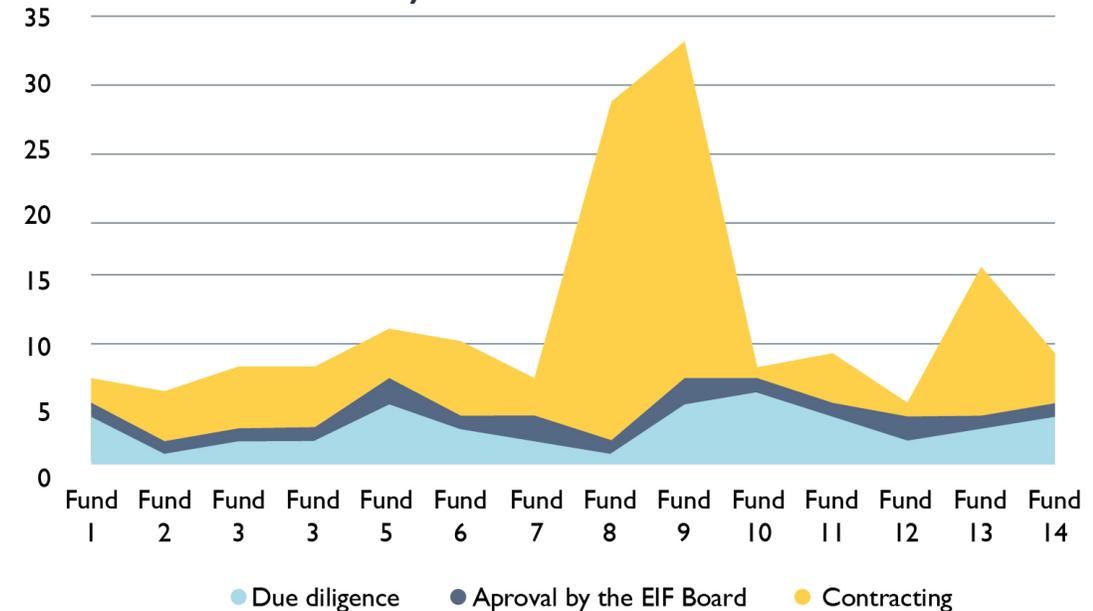
**The approval of transactions was also obtained in a short time period.** The average duration was 1.2 months.

**However, contracting took longer** and also varied between funds. The average interval between approval by the EIF Board and contract signing was 7.5 months, although this is heavily influenced by two transactions for which it took more than two years to sign the contract. For some transactions it actually took longer to sign the contract than it took to conduct due diligence and get EIF Board approval.



Some of the interviewed fund managers confirmed that while due diligence on and approval of transactions were swiftly conducted, the delay before signing the contractual documentation was longer than they would have expected. The main reason indicated by the fund managers was the insufficient capacity of the EIF's legal department to handle an increasing number of transactions.

## Conclusion of the SIA transactions (approx. duration by phase – expressed in # of months)



Source: Review of SIA transaction documentation

## The SIA was well coordinated with EFSI, but the existence of two separate definitions of “social enterprise” did not help



**For most of the evaluation period, the SIA was the only EIF product that envisaged investments in social impact funds.** Therefore, there was no scope for coordination and complementarity with other EIF products until 2017, when EFSI Equity social impact investment instruments were introduced.

**For each SIA transaction signed since 2017, complementarity with EFSI was systematically considered in the documentation.** SIA investments focused on funds that invest in later-stage social enterprises (or a combination of early and later-stage), while EFSI investments focused on early-stage social enterprises or non-profit organisations through payment-by-result schemes.

**In one case, SIA funding was used to complement EFSI funding.** The SIA-backed fund created a side fund focused on investments in startup and early-stage, high-risk-profile social enterprises. EFSI funding was used to invest in the side fund, while the SIA invested in the main fund, which focused on later-stage social enterprises.

**Despite good coordination overall, the SIA and EFSI each have their own definition of “social enterprise”.** The two definitions are not radically different but nevertheless have their own specific characteristics. As evidenced by the literature review and the interviews with SIA-backed fund managers, one of the current challenges of the social investment market is to agree on common terminology. The differences in terminology make it very difficult, if not impossible, to measure the precise size of available social impact finance in the European Union. Setting a definition applied by all market participants is not something the EIF can do. However, the use of two definitions within the EIF does not help to clarify the concept.

# Recap of key messages

- The SIA was and continues to be a highly relevant product.
- The SIA was well designed and implemented to help establish and expand the impact investment market in the European Union.
- In the absence of the SIA investment, the funds would have been much smaller in size; many would not have closed or would have struggled to operate.
- The SIA provided a positive signalling effect for other investors.
- There were no cases in which the EIF crowded out other investors.
- The SIA has increased the availability of finance for social enterprises beyond initial expectations.
- Most of the SIA-backed social enterprises claim they would not have been able to access finance from other sources under the same conditions and within the same time frame.
- SIA-supported enterprises delivered entrepreneurial solutions to social issues.
- Only one of the 14 SIA-backed funds invested in companies that deliver positive social impact but may also be associated with negative social impact.
- The structuring input provided by the EIF was appreciated and resulted in positive changes.
- The social impact-based carry mechanism did not influence the magnitude of social impact but did strengthen monitoring and helped to maintain focus on social impact.
- The SIA was generally managed in a very efficient manner but contracting was often slower than expected.
- The SIA was well coordinated with EFSI, but the existence of two separate definitions of “social enterprise” did not help.

# 5

## Lessons learnt

## What works?

- **The EIF operates in a market where there is a clear gap.** In 2014, the impact investment market was virtually non-existent across Europe, with the exception of the United Kingdom. There was only one wholesale investor in the market, Big Society Capital, which was focused on the UK market. The EIF took on the role of a pan-European wholesale investor.
- **The EIF used a smart market entry strategy** by first focusing on more developed markets like the United Kingdom and France to gain experience, build a track record and establish its credentials, and then expanding to other markets in need of support.
- **Funds are carefully selected and subject to intensive due diligence**, the quality of which is recognised in the market. The EIF also supported a mix of first-time and established teams to achieve a balanced portfolio.
- **The SIA helped to quickly get money into the social investment market.** The EIF topped up an existing pilot product for which processes and procedures were already in place. This facilitated the speed of delivery and helped to achieve economies of scale.
- **The innovations introduced by the EIF were applied in a clever manner.** The main innovation is the social impact-based carry mechanism. Some market participants were concerned that it might create perverse incentives. However, under the SIA, the social impact-based carry mechanism played a beneficial role without introducing any perverse incentives.

## What could be done differently?

- **Intensify expansion of the SIA to less developed markets.** Although the initial strategy was clever, only eight Member States have been reached by the SIA so far. Any further geographic expansion of the SIA will be subject to the availability of resources for the EIF and will be influenced by demand factors in the markets. However, we believe that the EIF is well positioned to influence the development of demand, so more determined marketing of the product in less developed markets may facilitate such expansion.
- **Better manage the risk of negative social impact occurring alongside positive impact.** As already explained, this issue was only encountered in one isolated case. However, with some of the recent SIA transactions aiming to support businesses hiring marginalised people or operating in disadvantaged areas, this risk might increase. Establishing some form of commitment from fund managers to avoid investments that could be associated with doing harm may reduce this risk going forward.
- **Intensify efforts to promote knowledge sharing among SIA-backed funds and investors.** The EIF is the only pan-European wholesale investor in this asset class. It is, therefore, in a good position to encourage knowledge sharing among market participants. Such efforts have already been made but to a very limited extent, so there are opportunities for the EIF to play a stronger role in this respect.
- **Choose one single EU definition for “social enterprise”.** Reaching agreement on what constitutes a social enterprise has been challenging for not only the social investment market as a whole but also the EU institutions. This resulted in the EIF adopting two slightly different definitions of the same term for two different products (SIA and EFSI). Agreeing on one single definition should help to eliminate some of the confusion.
- **Reduce the time required from transaction approval to contracting.** This period has varied significantly between transactions and was often longer than expected. If feasible, some streamlining of procedures and strengthening of legal capacity by the EIF might help to improve efficiency.

## Items for consideration

### **1) Establish a single definition of “social enterprise”.**

The EIF currently uses two definitions of “social enterprise”: one for the SIA and the other for EFSI. While the two definitions are not radically different, they nevertheless have their specific characteristics. Their dual existence is explained by the difficulty of reaching an agreement with the European Commission. In the wider context, a range of different definitions are used for this term in the social investment market, creating confusion. The EIF is not in a position to establish a universal definition. However, establishing one definition agreed among EU institutions would be a positive step in this direction.

### **2) Actively promote knowledge sharing and networking between SIA-backed fund managers.**

The SIA invested in a range of social impact funds that now cover both mature and less mature markets, and both experienced and slightly less experienced fund managers. Some funds have stronger knowledge of social aspects while others are stronger on the financial side. There are therefore opportunities to encourage learning among the SIA-backed funds. The EIF already organised an event in 2017 to encourage such exchanges. Although this was positively received, no subsequent events have been organised and some interviewed fund managers felt that the EIF could do more to promote such exchanges.

### **3) Introduce safeguards to mitigate the risk of SIA-backed social enterprises being seriously associated with doing harm.**

All SIA-backed social enterprises are delivering some form of positive social impact. The vast majority are also not involved in any activities with a negative social impact. However, in one isolated case investments were made in companies that most people (and indeed researchers) would associate with doing harm, despite also contributing to social good. While some level of unintended negative impact on society or the environment is probably unavoidable in any business, social enterprises should not be seriously implicated in doing harm. Otherwise there may be reputational risks for the funds and indeed for their investors, including the EIF.

Particularly exposed to this risk are those funds whose strategy is to invest in companies located in disadvantaged areas or who hire from among marginalised groups, irrespective of the business.

# Evaluation of the Social Impact Accelerator

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The evaluation of the Loan Funds Instrument was undertaken as part of a broader evaluation of the [EIB Group Risk Enhancement Mandate \(EREM\)](#) carried out by the Operations Evaluation Division of the European Investment Bank (EIB), under the supervision of Sabine Bernabè, head of evaluation. Charu Wilkinson (external consultant) led the team responsible for evaluating the Social Impact Accelerator, composed of Adrian Costandache (evaluator) and consultants from ICF.

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