An Excerpt From

Measuring and Improving Social Impacts
A Guide for Nonprofits, Companies, and Impact Investors

by Marc J. Epstein and Kristi Yuthas
Published by Berrett-Koehler Publishers

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Marc J. Epstein
and Kristi Yuthas

More Praise for *Measuring and Improving Social Impacts*

"Measuring social impact is a topic at the top of so many agendas yet with so little real insight about how to make it real, actionable, and meaningful. *Measuring and Improving Social Impacts* is a practical guide for maximizing and amplifying impact. A must-read for those grappling with how to define and evaluate success."

—Paul Bernstein, CEO, The Pershing Square Foundation

"*Measuring and Improving Social Impacts* offers a useful and timely review of the many measurement approaches available to nonprofits, foundations, and impact investors. Epstein and Yuthas provide practical step-by-step guidance along with real-life stories that show how measurement is applied in action and leads to better results."

—Fay Twersky, Director, Effective Philanthropy Group, The William and Flora Hewlett Foundation

"Although this looks like a thorough guidebook for people starting in the field of social change, it is likely to trigger considerable thinking among those who have been involved in philanthropy and the practice of social change for a long time. The desire to bring about social change is quite simple, but doing something about it can be quite complicated—this book helps you to simplify things to achieve your goals."

—Madhav Chavan, PhD, CEO, Pratham Education Foundation

"A fascinating read . . . very valuable to corporate foundations like mine that are grappling with effectiveness at the foundation level and also understanding and measuring the added value for the corporation and its employees."

—Vidya Shah, CEO, EdelGive Foundation, Edelweiss Group, India

"Epstein and Yuthas provide a lucid and compelling framework—a logic model—for investors, civil society actors, corporate leaders, and policy makers to use resources more effectively and yield better social results."

—Rohini Nilekani, Chairperson, Arghyam

"This book is an excellent reference point for social impact investing. Epstein and Yuthas have meticulously researched an impressive cross section of companies, nonprofits, foundations, and individuals to build credible metrics and analytical tools, and they offer useful insights to maximize impact."

—Zarina Screwvala, Founder-Trustee, Swades Foundation

"Epstein and Yuthas offer a clear and highly accessible approach to measuring and creating social impact. Drawing on a diverse array of examples from around the world, they demonstrate that there are no quick fixes and that systematic measurement is essential."

—Alnoor Ebrahim, Associate Professor, Harvard Business School, and author of the award-winning *NGOs and Organizational Change*

"Epstein and Yuthas make sense out of the often confusing world of metrics and performance measurement, offering investors, social entrepreneurs, and donors new perspectives on how to approach the challenge of measurement—and how to convert that challenge into an opportunity! They review a variety of approaches to metrics and give readers the skills needed to go from metrics as measurement to metrics as a tool for creating deeper, more sustained value. A must-have for all leaders serious about maximizing the impact of their organization and capital."

—Jed Emerson, Chief Impact Strategist, ImpactAssets

"This book is a great resource for anyone working to tackle today's complex, global social challenges. Epstein and Yuthas help us ask the right questions, create meaningful measures, and adapt nimbly to test our biggest, boldest ideas and determine if they will deliver the right kind of impact."

—Steven J. McCormick, President and Trustee, Gordon and Betty Moore Foundation

"Too often, donors and investors think of social impact measurement as separate from the 'real work' of doing good. Epstein and Yuthas have developed a clear and practical guide to impact measurement—not just how to do it but how to think about it and integrate it into every aspect of your work. Essential reading for anyone looking to move from good intentions to high impact."

—Katherina M. Rosqueta, Founding Executive Director, Center for High Impact Philanthropy, University of Pennsylvania

"By posing the right questions and providing useful frameworks, Epstein and Yuthas take us on an absorbing voyage of the challenges and solutions available in the field of social impact measurement. The book is a valuable resource for investors keen to generate social impact in a thoughtful, rigorous, and transparent manner."

—Nalini Tarakeshwar, Executive Director, Evidence, Measurement and Evaluation, The Children's Investment Fund Foundation, UK

"Whether your annual philanthropic contribution is $5,000 or $5,000,000, this book is a must-read to move people out of poverty faster! Epstein and Yuthas provide a unique balance of introspection and global insights to ensure that impact, scale, and sustainability are achieved."

—Deval Sanghavi, cofounder and Partner, Dasra Strategic Philanthropy Foundation, India

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A Guide for Nonprofits, Companies, and Impact Investors

MARC J. EPSTEIN
and
KRISTI YUTHAS

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Contents

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Preface

All organizations have social impacts: some are positive and some negative. *Measuring and Improving Social Impacts* is about how you can learn to make decisions that will improve the positive social impact of companies, foundations, nonprofits, and impact investors. In our work with organizations that are interested in impact, we've taken on a variety of roles—sometimes we've served as consultants and advisors, and sometimes we've served as researchers attempting to better understand organizational challenges and to develop or evaluate solutions. As professors, we also have our roles in the academy, researching and writing in addition to teaching and working with students, many of whom share their work experiences with us.

We began our careers focusing on two sets of issues: performance management and ethics. We were trained in performance measurement practices and have applied them broadly in both for-profit and nonprofit organizations. Whether the focus of the organization is on improving the financial bottom line or on improving society, similar issues arise. Organizations want clear answers to questions such as: What are we trying to accomplish? What do we need to do to accomplish these goals? How do we define success? How can we measure success? How will we know when we have succeeded? and How can we do better over time?

What we have seen is that too often, in both for-profit and nonprofit organizations alike, the answers were not clearly understood. In many cases, the questions weren't even clearly articulated. We have focused our work on helping organizations explore these questions to better define, measure, and improve performance.

Throughout our careers we have also focused on the ethical dimensions of organizations. We're concerned with questions such as How can various types of organizations use their resources to address social ills? In our work on corporate social responsibility and sustainability, we help organizations develop ways to manage social, environmental, and financial performance simultaneously. We show businesses how they can improve their social impacts while also looking out for shareholder needs.

Marc has authored or coauthored twenty books, and both Marc and Kristi have published extensively in the areas of corporate social responsibility and sustainability, nonprofit governance and performance measurement, and improving organizational social and financial performance. We have worked in Africa, Asia, and South America with organizations specializing in microfinance, microentrepreneurship, global health, and education for the poor. This international work has allowed us to collaborate with the best for-profit and nonprofit organizations in the world in dozens of countries over many years. All of this work has contributed to the ideas integrated into this volume.

Building on our previous work, we embarked on an enormous additional task for this book. We wanted to understand the views and approaches of the world's leading experts in impact measurement and to better understand how they address the difficult problem of measuring and improving their impact. This project took us to places like New York, Seattle, San Francisco, London, and Mumbai. We talked with small and large foundations, nonprofits, and companies as well as impact investors and high-net-worth individuals.

The result—this book—is about all aspects of social impacts. All organizations have impacts, positive and negative, intended and unintended. Companies can produce products that improve or damage society—or both. Nonprofits can create jobs for some and displace jobs for others. Or they can provide services that have only minor impacts relative to the resources used to create them. Organizations can easily make the mistake of operating in the dark—lacking clarity about the impacts they create or lacking the rigor to produce the impacts they desire. These organizations can benefit from developing better measurement systems that can help them succeed in their missions and improve their impacts.

In retrospect, it seems like we have been preparing to write this book our entire careers. We did not know it when we began the project, but this book has turned out to encompass the work we have been doing for decades. In researching and writing it, we learned a great deal about the importance, processes, and mechanics of deciding what impacts really matter, and then measuring and improving those impacts. Whether this is your first time thinking about impacts or you have years of experience working in the field, you'll learn new things as well.

We are grateful to the more than one hundred leaders whom we interviewed for this project. We especially want to thank Praveen Aggarwal, Sabina Alkire, Anish Andheria, Steve Aos, Doug Balfour, Clara Barby, Steve Beck, Dan Berelowitz, Jeff Bernson, Paul Bernstein, David Bonbright, Amit Bouri, Jeff Bradach, Paul Brest, Arjav Chakravarti, Leni Chaudhuri, Cindy Chen, Michael Chertok, Neelam Chhiber, David Colby, Carmen Correa, Claire Coulier, Monisha Diwan, Poornima Dore, Toby Eccles, John Elkington, Jed Emerson, Richard Fahey, Mike Feinberg, CJ Fonzi, Matthew Forti, Cynthia Gair, Russ Hall, Laura Hattendorf, Lucy Heller, Anne Heyman, Jeremy Hockenstein, Kai Hopkins, Bart Houlahan, Alex Jacobs, Hannah Jones, Tie Kim, Sean Knierim, Tris Lumley, Steven Lydenberg, Anna Martin, Steven McCormick, Carol McLaughlin, Sunil Mehta, Zarina Mehta, Hari Memon, Eve Meyer, Sumit

Mitra, Laurie Mook, Will Morgan, Jodi Nelson, Rohini Nilekani, Sara Olsen, Sally Osberg, Paresh Parasnis, Alexander Pope, Kevin Rafter, Mike Rea, Larry Reed, Gabriel Rhoads, Katherina Rosqueta, Deval Sanghavi, Zarina Screwvala, Vidya Shah, Durreen Shahnaz, Devi Shetty, Paul Simon, Rishi Singh, Lynne Smitham, Sean Sokhi, Padmini Somani, Divya Srinath, James Stacey, Nalini Tarakeshwar, Ben Thornley, Pearl Tiwari, Brian Trelstad, Melinda Tuan, Fay Twersky, Steve Viederman, Sunil Wadhwani, Havovi Wadia, Brian Walsh, Michael Weinstein, Peter White, Allen Wilcox, Peter York, and their colleagues for their time in sharing with us their individual and organizational experiences in measuring and improving social impact. We cannot thank them enough for sharing their work with us as well as their important concerns and contributions for improving social impacts. We would also like to thank the Rice University Shell Center for Sustainability. The Center's generous funding supported our field research and many other aspects of this project.

This book has taken more hours than we want to count. But it could not have been completed without the assistance of others. Hannah Sijia Chen is a bright and diligent researcher who was at the center of this project. Not only her great research support but her work in the management of all of the information from both the published research and the field and interview notes was critical. We are extremely appreciative. We are also grateful for the substantial and excellent administrative support provided by Tatianna Aker at Rice University. Samuel Ireland, Tim Hutchinson, and Maria DeWitt also provided assistance and contributed innovative ideas to the project.

In addition to the experts in organizations and our assistants at the universities that were so critical to our work, we want to thank all of the colleagues who have been so helpful in forming ideas and providing important feedback as we were developing this project; these include Klaus Brinkmann, Cindy Cooper, Srikant Datar, Jesse Dillard, Linda Firth, Francisco Montgomery, Scott Sonenshein, and Sally Widener.

Organizations interviewed for this book include:

Absolute Return for Kids (ARK)
Acumen Fund
Ambuja Cement Foundation
Arghyam
B Lab
Bill & Melinda Gates Foundation
BRAC
Bridge International Academies
Bridges Ventures
Bridgespan Group
Center for High Impact Philanthropy
Chevron Corporation
Children's Investment Fund Foundation
Dasra
Developing World Markets
Digital Divide Data
Earth Capital Partners
EdelGive Foundation
Edna McConnell Clark Foundation
Escuela Nueva
Geneva Global
Godrej Group
Gordon and Betty Moore Foundation
Home Depot
Industree Crafts
International Centre for Social Franchising
James Irvine Foundation
John D. and Catherine T. MacArthur Foundation
KaBOOM!
Karisimbi Business Partners
Keystone Accountability
Kiawah Trust
KL Felicitas Foundation
Legacy Venture
Liquidnet For Good
Magic Bus
Markets for Good
Mercy Corps
MSCI, Inc.
Mulago Foundation
Narayana Hrudayalaya Hospital
Narotam Sekhsaria Foundation
New Philanthropy Capital
Nike
Nissan
Omidyar Network
Oxford Poverty & Human Development Initiative
Pacific Community Ventures
PATH
Pershing Square Charitable Foundation
Plan International
Pratham
Procter & Gamble
Robert Wood Johnson Foundation
Roberts Enterprise Development Fund/REDF
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Rockefeller Foundation
Shujog
Sinapi Aba Trust
Sir Dorabji Tata Trust
Skoll Foundation
Social Finance
SpringHill Equity Partners
Swades Foundation
VillageReach
Washington State Institute for Public Policy
William and Flora Hewlett Foundation

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This book is dedicated to our families. We thank Marc's family: Joanne Epstein, the Firestone family (Simcha, Debbie, Emily, Noah, and Maya), and the Zivley family (Scott, Judy, Amanda, and Katie). We also thank Kristi's family: Kiley, Jackson, and Michaela. Without their patience, support, and humor this book couldn't have been completed.

Marc J. Epstein
Houston, Texas

Kristi Yuthas
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September 2013

Introduction

You are on a hero's journey. You have decided to invest your most valuable possessions—your time, your money, your knowledge—to help others. Not content to sit back and watch, you have joined the effort to tackle some of the world's most difficult challenges: challenges such as poverty, health, climate change, and security. You know that you face enormous odds. Social and environmental problems in both developed and developing countries are immense, and the resources we have available to address them are wholly inadequate to the task. Some of the institutions that help address these problems—governments, NGOs, and corporations—are unable or unwilling to devote anywhere near the resources needed to make meaningful and lasting headway in eradicating serious social problems. Yet you are not giving up. Against all odds, you continue to work diligently or invest generously in the causes you care about, believing that your gifts will make a difference, that you can change the world. And you can.

This book will serve as a guide on that journey. It will help you turn scarce resources into meaningful investments that will, in turn, make significant improvements in society. We have written this book to help you and others like you create the most meaningful impact possible with the resources you control.

There are over one million nonprofit organizations in the United States alone and millions more across the globe. The number, breadth, and depth of these organizations have grown significantly in recent years and will continue to grow. Rapid growth is occuring in social enterprise and impact investing. As social investments flow in, it is essential to figure out ways to make sure that the money will have an impact. The impact investing industry can learn the lessons gained through decades of governmental and nonprofit investments. Both up-front investigation and ongoing assessment are needed to ensure that your investments are on track to create the desired impact.

Traditional profit-oriented corporations, too, have become much more interested in understanding and managing their impacts. Social issues no longer take a back seat to profits, and companies have many boundaries, such as avoiding child labor, that aren't subject to cost-benefit analysis. Almost all of the world's largest companies now routinely monitor social impacts and produce annual sustainability reports. The expectation that companies will contribute to society has never been greater. India has just passed a law that requires large companies to contribute 2 percent of their profits to social causes or publicly explain why there were unable to do so.

But growth in the number of organizations and faith in the good intentions of everyone involved are not enough. Organizations need to develop the ability to know whether they're making a difference and to know how to invest wisely so that they can do better over time.

While working with organizations and industries attempting to create social benefits, we have been surprised over and over again by the difficulties that investors and organizations face in their efforts to make social change. These unpleasant surprises relate to the roadblocks organizations and the social sector encounter in their attempts to produce positive impacts. As Table 1 shows, however, for each surprise there is an emerging opportunity to overcome obstacles and improve performance.

Table 1 Surprises and Opportunities

Unpleasant Surprise	Opportunity
Lack of organizational capacity for performance measurement	Demand for clear social impact strategies and action plans
Lack of incentives and market discipline to develop advanced social impact measurement systems	Pressure to develop measurement systems and increasing resources available for doing so
Lack of serious, significant investment in the social sector	New business and investment models that draw resources into impact markets
Focus on performance measurement is often small subset of organizational impacts	Development of integrated impact models and marketplaces for social impact data

This book is designed for people who are serious about social change and want to put their resources to work in the most effective way. Although the book is packed with a variety of tools and techniques, its core message is simple. To make an impact you'll need to:

- Define what success means to you, and
- Figure out how you'll know when you've achieved it.

Once you've made these key decisions, you'll find it much easier to evaluate your current progress and make changes to improve your performance.

Many investors and service providers are guilty of fooling themselves about the impacts they are making. They do this by assuming that good intentions lead to meaningful actions, by confusing the amount of action with the quality of results, and by basing important decisions on instincts instead of evidence. Perhaps you are guilty of some of these habits; if so, this book will provide you with valuable tools for overcoming them.

One common problem is defining success in terms of what the organization produces rather than the impacts that result. Table 2 shows some examples of goals based on an organization's outputs

Table 2 Goals Based on Outputs versus Goals Based on Impacts

Goals Based on Outputs	Goals Based on Impacts
We want to deliver meals to 10,000 homeless people.	We want to reduce hunger by 5%.
We want to provide 1 million insecticide-soaked bed nets.	We want to reduce malaria by 5,000 cases.
We want to convert 10,000 families from cooking with wood to cooking with gas.	We want to reduce residential CO_2 emissions by 50%.
We want to teach reading to 500 primary school students.	We want to increase literacy in the village by 10%.

compared to goals based on the impacts those outputs create. The distinctions here can be subtle, but it is essential that we focus on impacts for the following reasons: actions don't always have the anticipated results, instincts aren't always correct, and without understanding impacts it is difficult to improve them.

Humans are fallible. Psychological research has shown us over and over again that what we see and hear is strongly influenced by what we believe. Whether we believe the economy is getting better or worse might be influenced by whether we have a job. Whether we believe a school system is good or bad might be influenced by how much our own children seem to be learning. And whether we think our organization's free meals are reducing hunger might be influenced by the heartfelt thank-yous we received when we last served food.

This book will help you gain clarity about the impacts that matter most to you, and it will provide you with methods to measure and improve those impacts. Even for long-term impacts like reducing global warming or poverty that are difficult to measure or to attribute to any one investment or organizational initiative, you'll discover methods for evaluating your potential and actual contributions. Indeed, our purpose is not to try to turn you into a "randomista"—industry slang for those who believe that conducting scientific experiments, or randomized control trials, is the only way to know whether your outcomes are producing impacts.

While such methods can be useful in certain circumstances, there are many ways to use both logic and other forms of intelligence and evidence to evaluate and prove the impacts you are making.

This book's architecture is based on the Social Impact Creation Cycle. We developed the cycle to describe the steps that we believe are most necessary for creating and improving impacts. The cycle is introduced and described in chapter 1 and the steps in the cycle are discussed in depth throughout the book. The cycle is based on the five most fundamental questions faced by companies, and nonprofits, and investors seeking to maximize their social impact:

1. What will you invest?
2. What problem will you address?
3. What steps will you take?
4. How will you measure success?
5. How can you increase impact?

To address these questions, we have developed frameworks, described short case studies of organizational best practices, and provided guides to action. In addition, we have developed an online companion to this book, the Social Impact Self-Assessment tool. The tool will help you answer these five questions and assess your progress on the social impact creation journey. Further information on this self-assessment tool can be found on page 213. The book is divided into five sections:

Part 1: What Will You Invest?

Chapter 1, *The Social Impact Creation Cycle*, describes the Social Impact Creation Cycle and explains how it is used in subsequent chapters to help you define, measure, and improve social impacts.

Chapter 2, *Understanding the Investor*, explores the complex set of motivations that affect investor and donor decisions and the resources that investors can contribute to create impact.

Part 2: What Problem Will You Address?

Chapter 3, *Understanding the Problem*, considers ways investors can choose social causes to support, the approaches for addressing these causes, and the populations or regions to target.

Chapter 4, *Understanding the Investment Options*, surveys options for structuring and targeting investments and describes alternative roles, both active and passive, investors can take in those organizations.

Part 3: What Steps Will You Take?

Chapter 5, *How Social Impacts Are Created*, summarizes the basic avenues through which organizations create positive and negative social impacts—through products and services, through operations, and through investments.

Chapter 6, *Linking Actions to Impacts*, describes the essential ingredients for planning and guiding impact creation: missions, strategies, theories of change, and logic models.

Part 4: How Will You Measure Success?

Chapter 7, *Measurement Basics*, explores basic technical and behavioral concepts associated with measuring performance in general and social impacts in particular.

Chapter 8, *Measurement Approaches*, inventories and describes basic approaches to impact measurement and provides examples of tools used by leading organizations.

Chapter 9, *Measuring Your Impact*, builds on the impact planning discussed in chapter 6 and the measurement foundations in chapters 7 and 8 to provide guidance on how organizations can measure and report social impact.

Part 5: How Can You Increase Impact?

Chapter 10, *Social Impact Measurement Maturity*, describes a five-level maturity model that can be used to assess the qualities of existing impact measurement systems and to guide development of more effective systems.

Chapter 11, *Amplifying Your Impact*, explores ways to increase impact by innovating, scaling your organization, and contributing knowledge and resources to industry and sectorwide efforts to promote impact.

Chapter 12, *Call to Action*, summarizes the significant opportunities that exist to dramatically increase social impact through a careful implementation of the Social Impact Creation Cycle.

The Social Impact Creation Cycle and the book's chapters integrate the experiences from our substantial work in this field, an extensive examination of literature in numerous related fields, and the findings from a large field research project on the measurement of social impacts that included visits and interviews with dozens of leaders in the United States, the UK, and India. The project included both investors and investees. It covered government agencies, nongovernmental organizations, social enterprises, corporate sustainability leaders, and company managers interested in the impact of their ordinary products, services, and supply chains. It also involved leaders in public foundations, corporate foundations, and private family foundations—both large and small. It included some organizations that had well-developed monitoring and evaluation departments, and others that were struggling to create them. All of these organizations—even those known for being measurement experts—discussed a significant need for a book that could provide better guidance on identifying, defining, measuring, and improving social impacts.

You will find many new topics and discussions here that are based on our work with these organizations and are unique to this book. Our affiliations with universities have provided us a vantage point that has yielded powerful insights. Rather than focusing on any particular grantor or grantee, we were able to travel extensively to work with organizations on the ground in many countries. In addition, our university experience has helped us thoroughly ground our work in previous academic and managerial research.

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American Institute of Philanthropy
Annie E. Casey Foundation
Ashoka
AT&T
Bank of America
Beijing LangLang Learning Potential Development Centre
Best Buy
Better Business Bureau
Betty Ford Center
Big Society Capital
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Chrysalis
Coca-Cola Company
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Connected by 25
Coordinated Action Against Domestic Abuse
Creative Commons
Dana-Farber Cancer Institute
D.A.R.E. (Drug Abuse Resistance Education)
Domini Social Investments
Endeavorl
Exxon Mobil
Foodcycle
Foundation Center
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Goldman Sachs
Grassroots Business Fund
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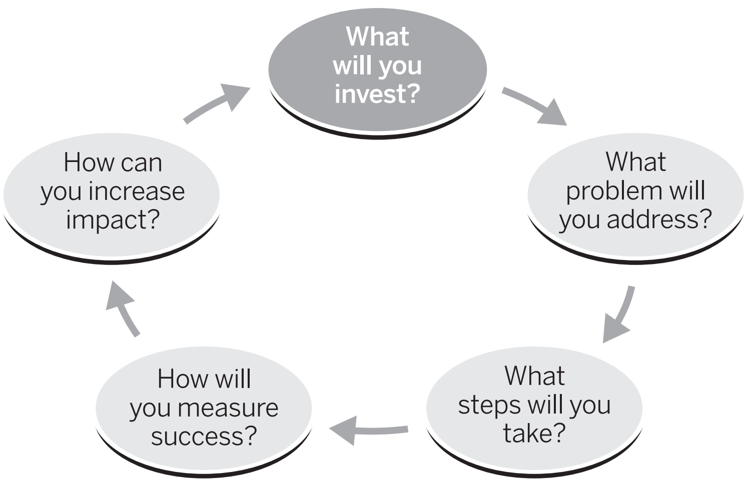
Root Capital
Royal Bank of Scotland
Social Impact Exchange
Society of St. Andrew
Sunlight Foundation
Taj Hotels Resorts & Palaces
The Gym
Tipping Point Community
Toms Shoes
Triangle Consulting Social Enterprise
Triodos Bank
UK Ministry of Justice
Unilever Indonesia
United Nations Children's Fund (UNICEF)
US Agency for International Development (USAID)
US Department of Health and Human Services
US General Accounting Office
US National Taxonomy of Exempt Entities
Venture Philanthropy Partners
Vestergaard Frandsen
VisionSpring
Wal-Mart Stores
Wellcome Trust
Wells Fargo
World Wide Fund for Nature (WWF)

The book is relevant to organizations, large and small alike, that are ready to step up to the challenges of improving their social impact. This includes those with a poor history of measuring social impact along with those with strong leadership that understands the importance of measurement in increasing their social impact. An extensive list of organizations interviewed is included in the preface. In addition, selected examples from a number of organizations (listed on the facing page) are also included in this book

Individuals working in foundations, NGOs, companies, governmental agencies, and social investment firms need better guidance for practice. Program managers in both developed and developing countries and other staff need more guidance on improving operations to increase impact. Even beneficiaries and hands-off donors can benefit from thinking more rigorously about social impacts. By following the steps in the Social Impact Creation Cycle, both investors and organizations can become more rigorous in defining success, understanding the causal relationships between actions and the desired impacts, measuring these impacts, and amplifying the impacts they and other social-purpose organizations can create for the environment and for society.

Over the past decade, stories of wasted money and "dead aid" have been told repeatedly—often with the conclusion that it may be better not to participate in social change at all and to let market forces prevail. But environmental and social problems aren't going away, and the world needs the resources of nonprofits, corporations, and social investors along with the operating expertise of socially concerned organizations now more than ever. These resources must be employed in the smartest, most impactful ways possible—and this needs to happen now. Let's begin that journey.

Part 1
What Will You Invest?



1

The Social Impact Creation Cycle

Every nonprofit, every company, and every investor creates social impacts. If you're reading this book, you are likely among those looking for ways to increase their impacts in order to contribute to social change. When you decide to invest in social impact, you are embarking on a journey that is uniquely your own—no two individuals or organizations begin or end up at the same point, for reasons you'll soon see. This book will serve as your companion and guide, leading you through the complex maze from the initial investment to the changes you seek.

The book is organized around the concept of a cycle, which helps you maximize your social impact by making deliberate and well-informed choices at every step in the journey from investment to impact. We will guide you through these steps and the factors you'll need to think about as you move through each one. Whether you are new to investing in impact or have been doing it for decades, it's important to make sure that the decisions you make are consistent with both your rational beliefs about how impact is most effectively created and your emotional feelings about which impacts have the greatest value. The method we present here provides you with a way to integrate the important components of your interests into a logical and cohesive whole.

The Social Impact Creation Cycle is designed to help you plan for and create the impacts you care about and to avoid creating negative impacts along the way. If you're an investor, donor, or volunteer, understanding this cycle can help you make sure that the organizations you invest in understand and can deliver on their intended impacts. If you're a company or nonprofit, working through the cycle will help you attract the resources most valuable to you and use them most effectively. No matter who you are, the Social Impact Creation Cycle can help you develop the big-picture understanding of how social investments lead to social change.

All kinds of organizations struggle with targeting and achieving their social impact goals. Philanthropic organizations make difficult resource allocation decisions trying to determine which social impact investments and/or donations will maximize benefits for their targeted communities. A foundation may need to decide whether to invest in a for-profit dairy, a nonprofit primary school, or a social enterprise–based health program. A sovereign wealth fund or government agency may reflect on optimizing the social bottom line of its activities for the neediest citizens. Even when a decision is made to invest in a sector such as health, should that investment be in combating malaria or attacking HIV/AIDS? Should the foundation promote new research or concentrate on making proven treatments available? Should it invest in Africa or in the US? Individuals face the same dilemmas when they assess their own social investments. The choices are many, and they are often difficult.

Corporations must often make trade-offs between sustainability and financial performance as they face decisions related to labor practices, environmental responsibility, community activities, and the like. The identification and measurement of the social impacts of these corporate activities often have significant implications for management decisions. Making this work more difficult, inconsistencies in measurement often arise, depending on the corporate function doing the measuring. For example, the sustainability function's metrics may differ from the corporate foundation's metrics, while both may contradict the viewpoint of those running the business's daily operations.

Individuals in the growing field of impact investing face their own challenges as they try to identify social enterprises and other organizations that can produce social impacts while meeting financial return targets. In fact, among the most critical challenges all these actors face is measurement. Social impact is a primary focus of their activities, yet these organizations and individuals are often unclear about how to measure and then improve their impacts. While projecting and measuring financial results is commonplace, most organizations find social impact measurement significantly more difficult. But demands for more careful and complete analysis of impacts are increasing rapidly. One survey shows that more than 80 percent of fund managers agree that impact measurement is important in raising capital,[1] while over 70 percent of grant makers think that foundations do not receive enough performance assessment information.[2] Social impacts are now discussed in corporate annual and sustainability reports as well as in NGO progress reports, foundation annual reports, and external reports to donors, investors, and other parties.

But even when organizations formally evaluate impacts, they do not always do it well. Inter-American Development Bank, one of the world's most highly respected development banks, once reported that fewer than one-sixth of its active projects had collected data on beneficiaries, and that only 3 percent had data on impacts on nonparticipants.[3] That information is essential for assessing the social impacts of these projects.

To meet both internal and external demands for performance information, organizations need more guidance. They need a better understanding of both how to make investment decisions that maximize social impacts and how to use monitoring and assessment to determine how much social impact has been created.

Systematic processes for gathering and analyzing information about impacts are often absent. Nonprofit organizations often use financial metrics of efficiency to evaluate performance when what they really need are measures of program and organizational impacts that they do not know how to obtain. Companies and foundations face similar dilemmas. They do not have all the information they need to make decisions related to the social impact of alternative projects.

Resolving these measurement inconsistencies requires a broader evaluation of a project's social impact. What we need is an industrial-strength tool to capture the entire picture. The Social Impact Creation Cycle provides a comprehensive method that can help you work through these issues to gain a better understanding of the social impact of a project, program, initiative, or organization.

Before we take a closer look at the Social Impact Creation Cycle, it is useful to establish a working definition for some of the terms we use. There aren't yet common definitions for these terms, but understanding how they're used here will help you as you work through the book.

Social impacts are the societal and environmental changes created by activities and investments. Societal impacts include such issues as equality, livelihoods, health, nutrition, poverty, security, and justice. Environmental impacts include such issues as conservation, energy use, waste, environmental health, resource depletion, and climate change. The term "social impacts" is used throughout this book to refer to both societal and environmental changes—positive and negative, intended and unintended—that result from investments.

Investments that create social impacts can take a variety of forms, including time, expertise, material assets, network connections, reputation, and other valuable resources. These investments can be donated, loaned, or invested with the expectation of social returns. For our purposes, if you donate or invest money or other resources, you are an investor. You are also an investor if you work or volunteer for an organization that creates social impacts or advocates for a social cause.

Social purpose organizations are entities that exist solely or partially to create positive social impacts. These organizations include non-profits, foundations, social enterprises, impact and social investing funds, social responsibility units within companies, and governmental agencies.

Social impact measurement is designed to identify changes in social impacts that result from your activities. Most organizations measure the outputs they produce (for example, meals served or jobs created). Social impact measurement assesses the ultimate impacts of those outputs on individuals and the environment (for example, on the quality of life, or survival of species).

A *logic model* is the logical sequence of activities and events through which the resources invested are transformed into desired social and environmental impacts. Organizations use logic models to work through this sequence to ensure that it is well supported before they invest resources.

This book is written with the recognition that your resources are valuable and limited, and that you would like to maximize the social impacts you create with those resources. The ideas and approaches described here will help you gain a better understanding of what impacts you hope to create and how you can best contribute to creating those impacts.

Creating and Measuring Social Impact

This book is organized around the Social Impact Creation Cycle shown in Figure 1. The cycle is built around five questions:

1. What will you invest?
2. What problem will you address?
3. What steps will you take?
4. How will you measure success?
5. How can you increase impact?

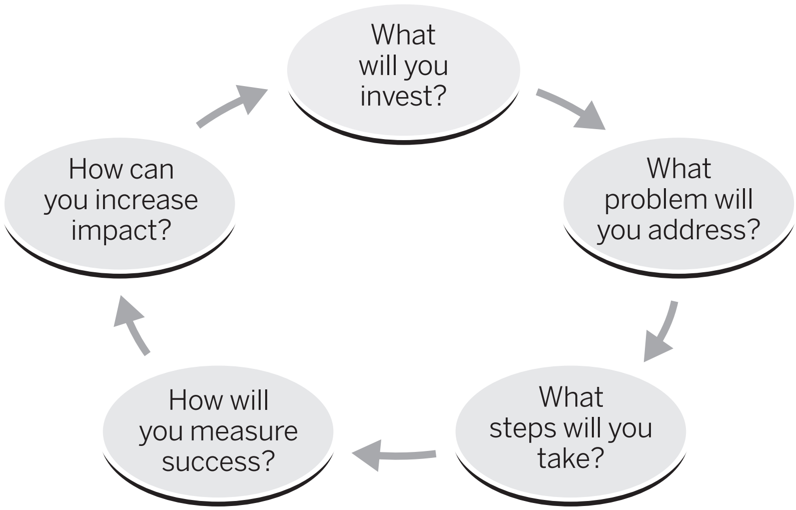


FIgure 1 The Social Impact Creation Cycle

These questions are at the heart of promoting, funding, and managing organizations for maximizing social impact. The cycle applies to funders, whether they are individuals, governments, foundations, corporations, or investors. It similarly applies to operating organizations that provide services or support to or advocate for beneficiaries. Donors and investors focus on how their resources—human, material, and financial—can be best used to produce social impact and which problems should be priorities, while NGO managers and other service providers focus on how to address the social problems they face and how to maximize social impacts. For-profit companies need to focus on identifying and managing the impacts they create for their customers and other stakeholders affected by their actions. But all of these concerns are important enough to be explored by anyone interested in social impacts and the processes through which they are created.

Each group can also benefit from better understanding the interests and challenges of the others. Investors can do a better job when they understand the interests and operations of the organizations in which they invest, and operators can do a better job when they understand the needs and interests of those who fund them.

Some of these topics are rarely discussed, such as the resources and interests of the investor, or why impact measures can't be separated from the values of the individuals and organizations that use them. Also widely recognized but rarely measured are impacts created through sharing best practices and innovations or collaborating on goals. We devote extensive discussion here to those topics that are essential for effective decisions and have typically not been carefully articulated.

Step 1: What will you invest? In this step, you'll first think about your investment goals. Why are you investing? What do you hope to accomplish through your investment? Do you expect social returns alone, or do you want financial returns as well? Do you have other goals, such as strengthening relationships, building your brand, or reciprocating for benefits you have received? You'll also consider what resources you are willing to invest in social change—your time, your money, your expertise, your network.

Step 2: What problem will you address? Next, you'll decide what kinds of problems you are interested in addressing, and whether you will focus on one issue or a portfolio of issues. You will consider which social and environmental causes are most important to you and how you can best serve beneficiaries using the resources you plan to invest. And you'll consider the intervention approaches you wish to support, such as research, services, advocacy, or ecosystem support. You'll decide what types of organizations you're interested in—social enterprises, nonprofits, corporations—as well as how you'll structure your investment in that organization, whether as venture capital, equity, a loan, or a gift. You'll also decide what role you want to play in the organizations in which you invest. Do you prefer to be an outside observer, or do you want to be engaged directly in operations or governance?

Step 3: What steps will you take? Once you have identified your causes, you'll plan for achieving the desired change. Social impacts flow from an organization's mission and culture and can be created by the goods and services offered, by operations, and from passive investments. You'll consider the various ways you'll make an impact through your investments. For desired social impacts you'll develop a theory about which actions can create those impacts, and then generate a logic model or results chain that can show exactly how the organization's actions and outputs are expected to result in positive impacts for stakeholders and the environment. Finally, you'll map out your stakeholders and the effects your organization will have on them, taking particular care to ensure that the interventions you plan are both beneficial to and desired by beneficiaries.

Step 4: How will you measure success? Performance measurement and management systems help you monitor how investments are creating social change. In this stage, you'll consider the purpose of your measurement. Is it to learn how effective your work has been, to communicate expectations, or to satisfy investors' accountability demands? You'll also determine the kinds of measurement approaches that can provide the evidence you seek, whether investigation, analytics, and/or experiments. And you'll make plans for developing a performance measurement system for gathering, analyzing, and using your performance data.

Step 5: How can you increase impact? In this step, you'll evaluate the dimensions of your performance measurement system—the metrics collected, the purpose served, and their relationships with your strategy—with the goal of improving your system to increase your impacts. Finally, you'll consider strategies for growing your organization and its impact. These can include sources of innovation, ingredients needed for successful scaling, and opportunities for collaborating and sharing your capabilities in order to leverage your impact beyond your own organization.

Each element in the Social Impact Creation Cycle in Figure 1 is connected by an arrow, and an arrow connects its last and first elements. The arrows suggest that working through the steps in the cycle is not a one-time process and that you'll return to each question as you repeat the cycle to modify your actions and improve your performance.

The Need for Accountability

Governments are finding it difficult to provide the necessary resources to address social and environmental issues, and the burden is increasingly borne by nongovernmental service organizations, foundations, impact investors, and companies. Those donating to or investing in these organizations are reasonably asking for more accountability for the invested resources—as are beneficiaries and communities that have significant unmet needs. Further, when governments provide tax benefits for these investments, it is reasonable to demand that the money be wisely invested to create as much social impact as possible.

One of the most important activities in which any foundation, NGO, or impact investor can engage is to think through and articulate what achievements are desired and how they can realistically be achieved. A common explanation for lack of effectiveness is that the organization has not been clear enough about its definition of success and lacks a well-defined logic model that would likely lead to that success. Too often we find serious gaps in the logic model and little evidence that activities are likely to lead to the proposed impacts. These logic models need to be supported by empirical evidence, a clear logic, or both. But often they are supported by neither. As you'll see, the Social Impact Creation Cycle helps bring clarity to logic models and thus enhances organizational accountability.

The Impact Measurement Roadmap

Although measuring and increasing social impact are commonly understood to be important, many become mystified by the process of implementing an impact measurement system. Even if you are effectively measuring and managing your impacts now, there are methods to increase your impacts that you might have overlooked. Working through the stages of the impact measurement road map can help you identify these methods and maximize your impacts.

Measuring impacts can be a difficult process and requires careful planning. The Impact Measurement Roadmap, summarized in Figure 2 and discussed in depth in chapter 9, has four steps. In the first step, you'll prepare the measurement foundation by defining the impacts expected to result from the organization's actions as well as other positive and negative impacts. In the second, you'll determine the purpose of your measures and how they'll be used. Based on that information, you'll determine which measures are most critical to your mission and stakeholders, and choose the appropriate metrics. In the last step, you'll develop a performance measurement system for gathering, analyzing, and communicating results and taking actions to improve those impacts.

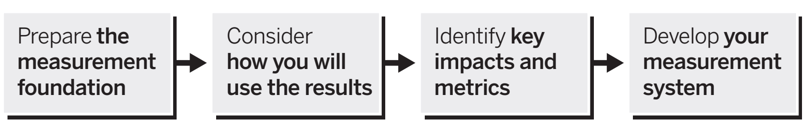


Figure 2 The Impact Measurement Roadmap

Billions of dollars are spent each year by NGOs, governments, and foundations with the explicit intent to make positive social impacts. Many more billions are spent by other organizations such as for-profit corporations that also have significant social impact interests. Too much of this money is squandered. Yes, some is through waste and inefficiency, and that should be eliminated. However, much is squandered by well-intended yet failed attempts to deliver important social changes. That failure can be remedied by careful attention to the five questions we ask in this book.

Although budgets, fundraising, and efficiency are important, social impact is the new bottom line for the social sector. We believe that you can achieve dramatic social and environmental changes through more careful efforts at defining, measuring, and improving your social impacts. Our Social Impact Creation Cycle can provide you with the guidance to do just that.

Action Agenda

1. Determine which of the five questions in the Social Impact Creation Cycle are most important to you right now.
2. Consider how you could improve your current performance measurement system by working through the stages in the Impact Measurement Road Map.

2

Understanding the Investor

What will you invest and what social impacts and other returns do you expect from those investments? Investors face these two key initial decisions when planning their social investments. By thinking carefully about these issues at the beginning of the impact creation cycle, you can maximize the range and depth of your investments and the returns those investments can generate.

A number of organizations recognize the importance of returns to investors and have developed ways to deliver them. For example, some organizations working on behalf of the poor in remote regions show investors firsthand how the resources they provide can change lives. Investors are invited to visit project areas and talk with the people who have directly benefited from their investments. When Sinapi Aba Trust of Ghana began making loans to increase capacity in schools for the poor, the organization invited donors, consultants, volunteers, and office staff to visit the field and see how the investments were working. For many of these visitors, the experience changed their lives. Seeing bright, engaged children in their safe new classrooms gave visible evidence that their investments were indeed making a real difference in the lives of these children. The trip thus gave them an unforgettable personal and emotional experience that forever changed their perceptions of the good that can be done with very small investments.

An often overlooked but critical factor in navigating your social impact investment journey is an understanding of your motivations for investing. This is the first step in making sure that the outcomes you achieve match your intentions. Who are you? What do you care about? What would it take to consider your investment a success? And what will you invest?

This chapter lays the groundwork for answering those questions. Before deciding on a specific cause, project, or partner in which to invest or reinvest, it is essential to recognize your motivational drivers so that your investment outcomes will truly reflect your investment goals. Taking stock of your goals prepares you to make smart, impactful investments that are consistent with your own particular values and interests. Understanding your investment profile also provides stability and continuity to your activities because they are anchored in the essence of your identity as an individual and an investor.

If you're investing on behalf of an institution, reviewing motives will help you ensure that your organization's social impact investments will be consistent with your organization's charter and culture. You'll also run into fewer surprises in outcomes and be less likely to have to backtrack on your investment choices.

You can start the investment process with your own investor preference profile to clarify your vision. Rather than investing out of habit or under the influence of others, begin by identifying what social impact investing means to you. If you are working with an organization, a mission statement will help define the direction of your impact investing and the expected bottom line of your investments.

A clear definition of purpose helps to prioritize potential outcomes that a particular investment might achieve for you or your organization and helps to identify opportunities where you can use your particular skills and interests to make the most impact. Understanding why you invest will help you determine the types of resources you are willing to offer, which can include much more than just money. Experience, advice, or hands-on project-level involvement can all create impacts.

What Motivates Social Investment?

In 2011, Wal-Mart made cash donations to social causes totaling $342 million—more than 4 percent of pretax profits. The company gave more than twice that amount, $617 million, as in-kind donations,[1] and Wal-Mart and the Wal-Mart Foundation gave more than $1 billion in 2012.[2] Other companies also made huge contributions to social causes in 2011: Goldman Sachs gave $337 million, and Exxon, Wells Fargo, Chevron, Bank of America, and JPMorgan Chase all gave more than $200 million. Whether they invest directly in impact or not, companies are increasingly attuned to the social and environmental impacts they create through their normal operating activities. Ninety-five percent of the world's largest 250 corporations now track and report publicly on the social impacts they create—a reflection of the growth in impact-related investment and a willingness to make impacts more transparent.

Individual gifts in recent years have been equally spectacular. The Giving Pledge has enlisted more than one hundred of the world's most wealthy and influential individuals. On the list, you'll find multibillionaire and Microsoft cofounder Bill Gates, Facebook founder Mark Zuckerberg, hedge fund chairman and American business magnate T. Boone Pickens, and founder, chairman, and chief director of Lucasfilm George Lucas.[3] What is The Giving Pledge? It's a commitment made by the world's wealthiest and most influential to donate a majority of their wealth to philanthropic causes. These individuals' donations are huge, as are the donations of their foundations. Since 1994, the Bill & Melinda Gates Foundation has awarded over $26 billion in grant money toward causes including fighting infectious diseases such as malaria and tuberculosis and funding education programs across the United States.[4]

Smaller investors are also generous in their giving. In the United States, more than two-thirds of the money contributed to charitable causes comes from individuals or households.[5] In total, donations added up to nearly $300 billion in 2011 nationally,[6] of which 82 percent were from individuals.[7] In addition, an estimated 10.7 million people are employed in the social sector,[8] and about 64 million Americans volunteered their time to social causes in 2012.[9] Governmental agencies (13.2 percent of the total US economy according to the US Bureau of Economic Analysis) invest vast resources in pursuit of social causes.

Are your investments creating valuable social impacts? It's impossible to tell without a clear understanding of what you're trying to accomplish. Considering your reasons for investing is a good place to start.

Values Drive Investment

What motivates organizations and individuals to be so generous? Why do people crack open their wallets to give their hard-earned money to someone else? When an individual contributes money to a social cause, he or she is making a statement—either public or private—about what is important and valued. In this sense, all social investment is value-driven: giving is a manifestation of one's beliefs.[10] Investors' values drive their social investments regardless of the form or scale of those investments, and whether they are acting alone or as agents of an organization. For investors who have shifted their focus from the act of giving or investing to the outcomes and impacts of those investments, values are perhaps even more important.[11]

What do individuals and organizations hope to achieve through their investments of money, time, and other resources? And what do they expect in return? The answers to these questions are as varied as the people who invest. In most cases, the investor has multiple goals in mind: social impact is the goal that unifies them. Interest and investment in social impact have gained momentum, and contributing to positive social change is at the top of the agenda for an increasing number of individuals and organizations.

Throughout this book, we broaden the use of the term "investment" beyond traditional monetary investments by expanding the range of returns that investors seek and the resources they invest. The social impact investors for whom this book is written seek social returns on their investments, which may complement or totally supplant monetary returns. They expect some kind of social or environmental change to result from their investments. Additional returns that flow from engaging in social investment include personal returns, such as pride in giving or enjoyment of the process of investing.

Goals of Social Investments

Social impact is rarely the only motivation driving investor involvement, and it is useful to both investors and recipients to explore these goals and make them explicit so that investments can best deliver on these goals. A foundation pursuing a social change mission in public health, for example, might make investments in research on aging, caretaker training, and services for the elderly. But that same organization might also invest in local arts organizations in the city where it is headquartered. Thinking about a full range of returns helps make sense of this commonplace practice.

We can think of investment returns as falling into four loose categories: identity returns, process returns, financial returns, and social impact. Figure 3 lists examples of the kinds of returns that characterize each category. There are natural overlaps and interactions among the items we list here, but investors will find that some of these outcomes are more important than others for a particular investment decision.

Each investor is unique, and more than likely, you'll discover that several motivation factors are at work, but the priorities you give them form the driving characteristic. For example, you have agreed to join a university advisory board because you want to help the university improve its impact. But upon reflection, you

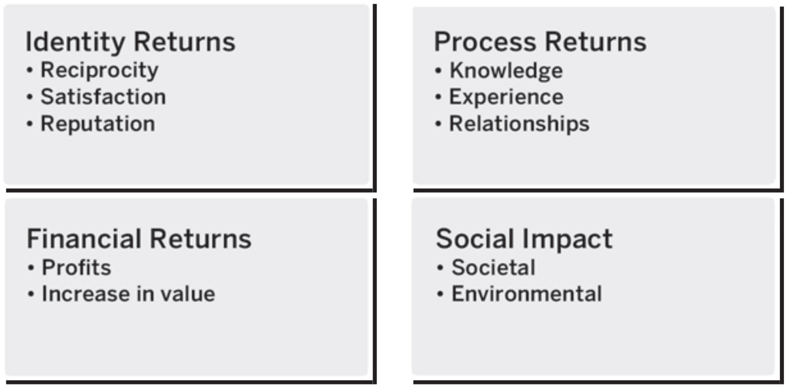


Figure 3 What Motivates Social Investments?

might recognize that the more important reason is that you wish to give your time to the university because you received so much during your student years. Alternatively, your primary interest in serving might be the opportunity to work alongside other high-profile members of the community with whom you would like to develop relationships. Thinking through these goals before deciding where and how to invest and reinvest can help ensure that your investments deliver the results they are intended to deliver.

In addition to financial returns, which are well understood and carefully managed by individuals and organizations of all types, and social impact, which is the focus of this book, we as investors have personal and emotional reasons to invest that are not effectively captured in terms of financial or social returns. *Identity returns* are a direct and often personal reflection on the identity of the individual or organization making the investment. These returns surround our raw desire to give and the emotional benefits that motivate and result from the pursuit of social change. Institutionally, they can include financial return substitutes such as marketing benefits like "branding" (Nike's "Just Do It" campaign, for example) or aligning products with a cause, such is the case with Coca-Cola's alliance with World Wildlife Fund, which is designed to preserve freshwater resources and increase Coca-Cola's water usage efficiency.

Process returns reflect the relationships the investor has with the investee and the transactional and relational gains that accrue to each as a consequence of their relationship. They reflect collaboration and benefits to the organizations involved rather than direct impacts on the final beneficiaries of these investments. *Financial returns* represent increases in cash flows and asset values over time, and *social impacts* represent the social and environmental changes the investor wishes to pursue.[12]

Identity Returns

Identity returns include the personal or emotional returns that accrue as a result of the investment. Many investments are made as a result of an urge to give or may flow from a desire or felt obligation to "give back" in gratitude for the benefits or advantages that have been received. The investment or gift may be motivated by altruistic impulses that are integral to the investor's identity or personal happiness. Reputation among peers and community members can also be a personal return that results from the investor's generosity. For an organization, attaching its name to a social investment can improve the reputation or brand value of the organization. Identity returns fall mainly into three categories:

- *Reciprocity.* The sense of an obligation to repay the community for one's good fortune, or a specific organization for benefits received.
- *Satisfaction.* The emotional benefits associated with the act of making the investment.
- *Reputation.* Community recognition and branding resulting from alignment with certain social investments.

Reciprocity. For many, giving to social causes is akin to settling an obligation or following through on a responsibility to repay for one's good fortune or benefits received from society. Family members and friends of loved ones who have been stricken by disease may support further efforts toward helping others suffering from that disease in gratitude for the support they received. Graduates may express thanks to a university for the education they received. Some expatriates give most to affiliated communities—their home country or the country from which they emigrated, or to institutions in immigrant communities.[13] In some cultures, it is customary to donate a portion of income earned. In several, there is an expectation that a portion of one's time will be spent in service to others. In others, the act of giving contains a spiritual element and is a means through which to express and strengthen spiritual connections and obligations. For example, some Indians give significantly to temples,[14] and nearly half of large individual donations in Asia go to religious institutions. Thus in addition to the direct social benefits to beneficiaries, the investor receives the benefit of feeling that a debt has been repaid or paid forward for the benefit of an organization and the community affected by it.

Satisfaction. From the satisfaction of writing a check to the joy of opening an email and learning about a social impact partner's success to the awe experienced when seeing firsthand the impact of the investment, emotional benefits provide a payoff for the hard work and generosity underlying an investment. Sometimes referred to as a "warm glow," emotional satisfaction can be a result of either the investment itself or the payoff from that investment. While social impact is the goal, satisfaction can be a direct benefit from the act of giving, or it can be a second-order effect that results from the perceived social impact.

Reputation. The people responsible for making investment decisions are social, emotional beings. Thus, the personal outcomes associated with a social investment may also have value for the investor. Participation in fundraising, for example, is an activity that investors may feel portrays them as people worthy of respect within the community. Businesses believe in the substantial benefits of "branded" social involvement. A business may gain brand recognition or be perceived more favorably when it is associated with a social cause. High-profile individuals or organizations may invest strategically to enhance their own reputations by associating themselves with a well-regarded organization. Naming a building or receiving public recognition for a donation, for example, can result in reputational outcomes that can benefit both investor and investee through many avenues.

Thinking ahead about the emotions attached to various aspects of the impact journey can help both in designing interactions and in assigning value to the range of outcomes that may result from the investment.

Process Returns

Process returns are those benefits that flow from the process of engagement in a project. Some investors value the learning opportunities offered through involvement in an investment, such as the acquisition of new knowledge about how a particular operation works on the ground. Others gain from the investing experience itself, as they engage in activities that contribute to the creation of impact or as they interact with beneficiaries. Social investing may also translate into new relationships and networking opportunities. there are three broad categories of process returns:

- *Knowledge.* The information and learning acquired by investing in or working with an organization.
- *Experience.* The skills and understanding gained as a result of the investment.
- *Relationships.* The personal or business relationships formed or strengthened by the collaboration with the target investment.

Knowledge. To the extent that investors are actively engaged in participating in or following the activities of investees, they can enhance their learning and knowledge in a variety of cause- and sector-related areas. Lessons from one set of circumstances can often be applied in another, and innovations can result when learning crosses conceptual or contextual boundaries. The culture of engagement and passion found among many organizations involved in the pursuit of social causes can also be an important source of insights for investees. Because social purpose organizations frequently work in extremely resource-constrained or high-risk, dynamic environments, they often develop the capacity for rapid learning, innovation, and transformation that can be enlightening and useful to investors operating in other environments.

Experience. This can be a strong draw for many investors, since the lessons learned are often transferable to other life situations. They enjoy learning new things or experiencing the differences between theoretical solutions and real results on the ground. Some may be in it for the challenge of evaluating a problem and implementing the solution while learning from experts who instruct them along the way. For both individual and organizations, gaining experience in a particular field can be a major purpose of an investment. It may, for example, be a pilot process where the investor is interested in acquiring the specific workable skills in order to better understand the social impact of the experience, which could be helpful in future projects.

Relationships. Many investments have strengthening relationships as an objective. Religious giving or giving to causes supported by friends or colleagues can build relationships, as can serving on the board or staff of a social purpose organization. The relationships can result in a broad range of benefits for both the investor and the investee. For the investee, these relationships can enhance performance of the board or staff or can provide access to a broader network of investors and resources. Thinking through how investments are likely to affect relationships for both investor and investee can support more effective allocations of resources and effort. From a "deal-making" point of view, an investor may receive tremendous benefits from board appointments, high-powered relationships and networking opportunities, and the like. For example, a senior executive may make a substantial investment in a project and in return be named to the target organization's board of directors, where he or she can form collegial relationships with other corporate leaders and improve his or her social and commercial standing. Supporting a cause promoted by an associate can strengthen relationships with that associate that can result in benefits for the investor and for the investees they support.

Financial Returns

Corporations, impact investing funds, and even foundations and nonprofits seek two bottom lines at once: financial performance and social performance. Financial performance can come from cost management alone, or can be generated through revenues or increases in the values of assets in which investments have been made. The line in Figure 4 shows the range of financial returns typical for various types of investments.

The line shows a continuum from donations that have no expected returns of capital all the way to "financial first" investments, which yield commercial rates of return on the investment. Many donations and grants are simply gifts and yield no financial returns to the investor. Charitable organizations have become increasingly entrepreneurial, however, and their own operations often have revenue-generating components. Although revenue may not cover all of the organization's expenses, this model places them on the part of the continuum in which a portion of the capital invested is returned in the form of financial gains, reducing the demand for ongoing grants or donations.

"Social first" investments hold the middle ground. Investors expect all or most of their capital to be returned, but are willing to accept a rate of return lower than the commercial rate that would be expected based on the riskiness of the investment and general economic conditions. Investors at this level are often

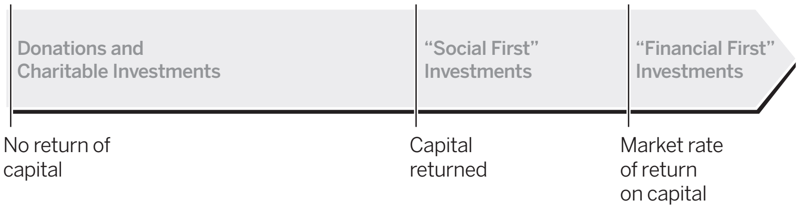


Figure 4 Various Types of Investments

referred to as impact investors, and the capital they invest is sometimes referred to as "patient capital" when it is recognized that the investment may yield a return, but only in the distant future. Many impact investors are willing to sacrifice financial returns because they value the social impact the investment creates. Social enterprises similarly fall into this space. They intentionally seek a combined bottom line in which financial concerns are not the only priority. Social and environmental returns are considered to be among the organization's key priorities, and may be built into the organization's charter or mission. Impact investors and social entrepreneurs may pursue this middle-ground strategy primarily because they wish to maintain capital for future investment, but most social-first investors believe that a quasi-market model is the optimal way to take the first step toward providing long-run solutions to some social problems.

Investments with returns that are equal to or higher than the market rate of return on investment can be thought of as traditional commercial investments. However, use of the term "financial first" investments suggests that financial considerations do not stand alone, and that social concerns also represent significant investment objectives. For example, microfinance has promised investors favorable rates of return, but most investors are also concerned with the impacts of microfinance services on impoverished communities.[15] While financial-first investments may have access to traditional capital markets, they have prioritized social impact as a positive goal to be sought rather than a potential risk area to be managed.

For example, SpringHill Equity Partners is a US financial-first investment manager that is committed to maximizing financial returns while achieving measurable and lasting social impact for its partners. SpringHill searches for small businesses in Africa that serve the poor. For each of its investments, SpringHill targets an annualized return of 10 to 20 percent and generation of a social benefit worth six to twelve times the money it invested.

Traditional corporations and their investors have various motives for valuing social impact. They may be financial-first investors, seeking social returns as a valuable goal independent of financial returns. Or they may be "financial-only" investors who prioritize social impacts because they recognize its increasing importance to stakeholder groups that have the power to influence them financially.

Financial returns may come from a variety of sources that are related to social impacts—reduced energy, materials, or logistics costs, increased brand reputation and customer loyalty, or even reduced cost of capital as investment funds screen out corporations that are seen to be particularly damaging to society or the environment. In contrast, Mulago Foundation funds high-performance social enterprises. The foundation's investment strategy focuses solely on maximizing social impact, so 95 percent of its social impact portfolio is philanthropic, with the remainder being loans.

Social Returns

Throughout this book, we describe methods for defining, measuring, and increasing social returns. We assume that since you've selected this book, you already consider social impact to be a primary investment consideration. Since the remainder of this book is about social returns, we won't go into depth here. But we will discuss trade-offs between social and financial returns. To do that, we'll need some kind of social metric. Here, we'll use a simple rating system to demonstrate how a rating of this type can be useful for evaluating investment opportunities.

Impact First/Financial First Portfolio: KL Felicitas

KL Felicitas Foundation employs a disciplined impact investing strategy to support global social entrepreneurs and social enterprises in addressing poverty.

Its impact investments break down to two general categories:

- *Impact First Investments:* aim to optimize social or environmental returns. Some of them focus on new and high-risk areas in the hope of sizable social or environmental returns. KL Felicitas' Impact First Investments include **Program Related Investments (PRIs)**, which provide low-interest financing, equity investments, etc., and **Corpus Impact First Investments (CIFs)**, which are PRIs made directly from KL Felicitas' corpus.
- *Financial First Investments:* aim for optimized financial returns that generate some social or environmental returns at the same time. KL Felicitas' Financial First Investments include **Mission Related Investments (MRIs)**, which financially support programs aligned to KL Felicitas' mission; **Sustainability Investments (SUIs)**, which offer equity investments to companies or funds focused on sustainability; and **Social Component Investments (SCIs)**, which are equity investments in funds that cycle their profits into social programming.

Source: KL Felicitas Foundation (2013) "Impact Investing Overview," http://klfelicitasfoundation.org/impact-investing-overview/.

Imagine a rating system in which each project is evaluated according to the degree to which it satisfies the investors' social objectives. Our imaginary investor has these potential projects to evaluate:

- Project 1: Fund loans to build for-profit healthcare clinics in Zambia.
- Project 2: Make a grant to support a Nepalese girls' school.
- Project 3: Fund water distribution projects in Tunisia.

To help compare the alternatives, the investor rates them on their social objectives and then plots the resulting social returns score against the expected financial return of each investment. Table 3

Table 3 Comparison of Expected Social Impacts and Financial Returns

Expected Social Impact	Project 1	Project 2	Project 3
Criteria for this investment:	*Clinics*	*School*	*Water*
Addresses difficult-to-serve clients in impoverished regions	6	6	5
Link between actions and outcomes has been evidenced	7	4	7
Capacity to continue program after our investment ends	7	2	5
Total Social Impact Score	20	12	17

Expected Financial Returns	Project 1	Project 2	Project 3
	Clinics	*School*	*Water*
Return on investment	20%	2%	30%

shows how this investor has rated each of the three projects on its social and financial returns. On the criterion of whether the three options would benefit difficult-to-serve clients, the investor gives the first two projects scores of 6, and the third a score of 5. All three projects are capable of reaching difficult-to-serve clients. On the second, which asks whether the intervention had been proven, the investor rated the school project quite a bit lower than the others. That suggests that there was more evidence that the intervention would lead to success for the clinics and the water projects. Finally, on the third, about whether the project could be sustained beyond the investment period, the clinics scored high, the school scored very low, and the water project was in the middle. Overall, the clinics project achieved the highest social impact score, and the water project was second.

Next, estimated financial returns were calculated, and the water project scored higher than the clinics project. Because no single project was highest on both financial and social performance estimates, the investor must now decide which project is superior—the clinics project with a social impact score of 20 and an estimated return of 20 percent, or the water project, with an impact score of 17 and an estimated return of 30 percent. As with all decisions involving social impacts, there is no objective way to determine which project is best—that will depend on the investor's values and interests, and on the specific goals for this project.

Once the expected social performance of each investment has been evaluated, the investments can be plotted on a graph to help the investor see which investment provides the better combination of social and financial returns. Figure 5 shows how the plot might look for this investor.

It is useful to note here that the expected financial returns are an objective estimate that could be made by a financial analyst. This estimate would remain the same regardless of which investor funds the project. Social returns, however, are value based and will vary from investor to investor. Each investor determines his or her own unique set of impact factors that will be used to rate the investments.

Another investor might have completely different criteria for rating the social impacts of these investments, such as which investment empowers girls and women the most or which project best promotes health. This investor might rate the water project highest on social impact, on the basis that access to clean water will reduce disease and free girls from the lengthy daily walk to carry water for the family. No two investors will have identical values, so each must think through his or her own values and preferences in determining social impact priorities. This is an important point, and one we'll revisit.

What Will You Invest?

At first glance, this is an easy question to answer. When we think about investing in social impact, we think primarily about investing time and money. The size and influence of the social sector is often characterized by the number of people working in social organizations and the amount of money given to or spent by these organizations.

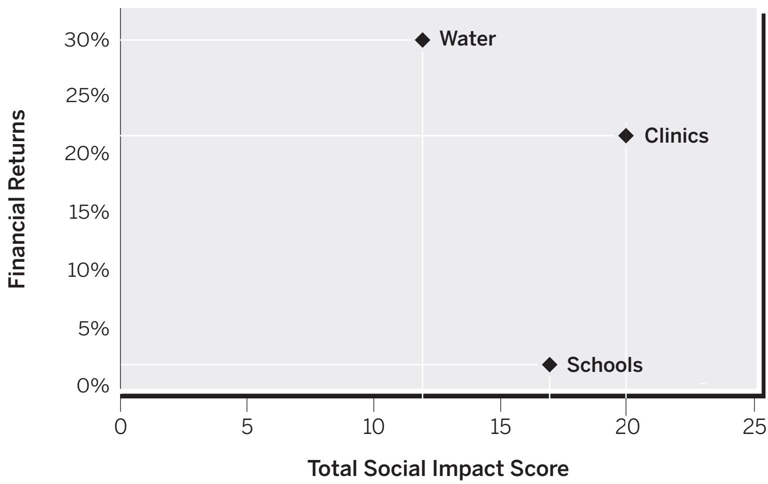


Figure 5 Projects with Different Levels of Return

But thinking about investment only in terms of time and money can paint a picture that is far too narrow, leaving out resources that can be uniquely valuable in creating impact and restricting the amount of impact you are able to create. For example, you may have medical knowledge that can be used in a crisis, you may have access to a building that can be used as a meeting place, you may have a group of colleagues whom you can invite to support a cause, or you may have the business expertise necessary to advise the investee.

Here we'll ask you to take stock of your resources. You'll identify everything that you or your organization has available that might be useful in creating impact. We'll also ask you to think about resources you have that are uniquely valuable, either because they are rare and hard to find, or because they match the needs of a particular recipient.

For example, imagine that you're a dentist with time that you're willing to devote to create impact. You could package food at a local food bank, donate your services to be auctioned off for a church fundraiser, or train dental assistants to provide basic, low-cost care to impoverished people with no access to dental care. These three options might require the same investment of time on your part, but they can have very different impact profiles. None of these options is objectively superior to the others, and your choice will depend on your beliefs and interests as well as the returns you hope to create.

Thinking through your investment options can increase both the resources you're able to invest and the value your investments can generate. With a clearer understanding of what you have to offer and the unique value you can provide, you'll have more leverage. You'll be able to put resources to better use in maximizing the social impact your investments create. When your desire for impact is combined with other goals, understanding the power of your resources can help you increase those returns as well.

Investors must first decide what resources are available for investing. For some, this is simply a matter of deciding how much cash they have available. But you may have a variety of other resources that can be useful in creating social impact. Figure 6 describes some of these resources.

Reputation

Reputation is a powerful resource that is often underappreciated. It's difficult to put a monetary value on reputation, but that doesn't mean that this resource isn't valuable. In fact, sometimes an investor's reputation is the only thing a recipient needs to create impact. An endorsement by a well-respected individual or organization can change everything for a particular organization or even for an entire cause. Betty Ford, wife of US president Gerald Ford, received a great deal of publicity when her struggle with chemical dependency became known in the 1970s. By using her reputation, she was able to gain support for building a clinic and helped reduce the stigma of seeking treatment for dependency problems.

You don't have to be internationally known to have an impact. Your willingness to support a cause can be influential to people who know you—business associates, community members, family, and friends. When kindergarten teacher Joni Huntley donated her hair to Locks of Love, a charity that provides hairpieces for children undergoing medical treatment, many children and parents decided to donate their own hair. In turn, some of their friends and acquaintances donated as well. Many social-purpose organizations don't do extensive advertising, so gifts that lead to increased publicity or a more valuable brand name can be very valuable.

Organizations often have well-known brands that are linked with their reputations for good work. Attaching their name to a project or cause often adds a level of acceptance and legitimacy. Some foundations have been asked to invest a single dollar in an organization, just so that organization could include the foundation on its list of supporters and thereby enhance its credibility.

An investor's network of relationships carries great value. Helping an investee make connections with individuals or organizations in the investor's network can open up a pool of contacts who can provide needed information, assistance, or support. The relationships and networks an investor has formed are sometimes referred to as "social capital," which is arguably more important than financial capital in many situations.

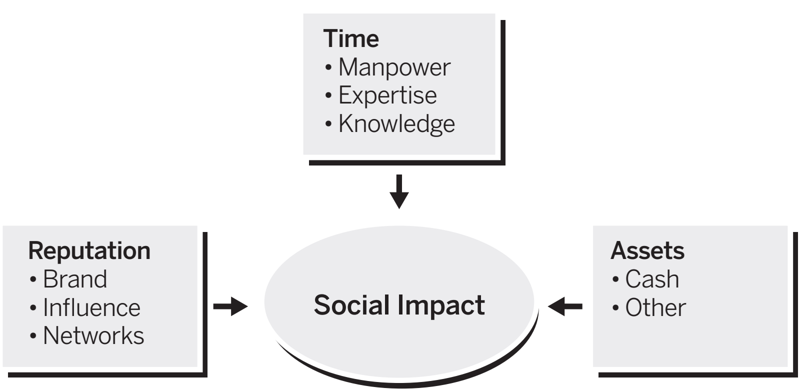


Figure 6 Resources That Can Create an Impact

Time

Working in the social sector is perhaps the most significant investment an advocate of social change can make. Employees making careers in social sector organizations invest their most valuable assets into driving social change—their time, energy, intellect, and emotions. Volunteers also invest time to drive change. They are called to fill a number of positions and responsibilities that either can't be afforded or can't be completed without their help.

Along with time generally comes expertise. While little previous experience is needed for some activities, such as piling up sandbags to protect a village from flooding, most investments of time are made much more valuable because of the knowledge that is invested along with the time. Employees, of course, build expertise and institutional knowledge, which makes their investment of time especially valuable. Volunteers often fill in gaps by providing knowledge, perspectives, and work products that can greatly complement, expand, and diversify the body of resources available for creating impact.

Knowledge developed through investments of time can be stored, shared, and used over again. This knowledge can take the form of policies, procedures, techniques, decision-making tools, and the like. These resources can also be exceptionally valuable to organizations that lack direct access to organizational expertise. Toyota, for example, recently donated its production expertise to The Food Bank for New York City, the largest antihunger charity in the US. Toyota's efforts drastically shortened wait times for meals and improved many processes at the charity.[16]

Research briefs, white papers, position papers, case studies, and other kinds of codified knowledge also represent valuable investments. These investments are often time- and organization-independent, so they have the potential to contribute to social impact in a broad range of circumstances.

Formal intellectual property (IP) can also be invested. An example of the vast impact of IP investments is the GreenXchange program, initially devised by Creative Commons in conjunction with Nike and Best Buy. The program provides a way for companies that have developed sustainability-related patents to share their intellectual property freely without extensive negotiations and legal contracts. Participants in the program can make their patents available for use by organizations, especially in relationship to their research and development functions, in order to enable widespread creation and use of green technologies and models.

Assets

Money, of course, is needed by all individuals and organizations seeking to make a social change. Even if money isn't required to directly produce impacts, it is needed to publicize the program to potential beneficiaries. Obviously, money can provide impacts in many different ways. Later, we'll explore the implications of how monetary investments can be structured—through loans that must be repaid, for example, or donations that do not.

Some investors are able to provide large lump sums of money that can be used for one-time capital projects or large investments that would otherwise be out of reach. Large investments can also be more efficient than many smaller ones, because organizations typically incur fewer costs in securing and managing the investment.

But the timing of monetary investments can also affect their value. Money that is provided in a stream over time can enable the investee to make long-term commitments that wouldn't be possible under more volatile budgetary conditions. Sometimes an infusion of cash that comes right at the beginning of a project can be valuable in getting the project off the ground and making it acceptable to more risk-averse donors. The first investment in a project on the website Kickstarter, for example, can open the gates to further exploration and support by other investors. The final investment needed to launch a project can also be valuable. Money provided at that point can help avoid delays and stress, and can change the emotional climate surrounding a project.

Other assets can be converted to cash as needed by the investee or as specified by the investor. They can also enable the recipient to avoid cash outflows. Gifts of stock, equipment, vehicles, artwork, and the like are common. But assets can also be invested in the form of long-term loans. Rights to use property such as land can be granted in circumstances where the investor wants to retain rights but also wants to use the asset to generate impact.

Communications and technology companies have offered their assets to create impact in times of need. In the event of natural disasters, many technology companies help by enabling people to better manage aid logistics and support communication. For example, AT&T and other wireless services providers agreed to use their phone lines and processing equipment to enable their customers to make donations to Japanese tsunami and Hurricane Sandy victims.

Even assets that might otherwise be discarded can create an impact in the hands of the right recipient. The Society of St. Andrew is a US nonprofit that gleaned (gathered and gave away) over 30 million pounds of food in 2012. In the United States, one-half of all food purchased is wasted.[17] The organization trains restaurant employees on food storage so that their food waste can be stored properly and then picked up by the Society of St. Andrew and given to poor people. Taking a full inventory of investable resources and identifying where those resources are likely to be useful can help investors maximize the impact they are able to create.

Investors who wish to maximize their returns need to spend time thinking about what returns they'd like to see and what they can invest to achieve those returns. By building an investment strategy firmly grounded in both a clear understanding of the range of returns desired and a complete inventory of resources available to invest, you'll be well positioned to achieve your personal goals and maximize the social benefits of your investments.

Action Agenda

1. Decide what kind of returns you want from your investments: identity, process, financial, and/or social.
2. If you're seeking financial returns, decide if you're willing to put social impact first by accepting lower-than-market returns on investment.
3. Take an inventory of valuable resources you can invest to create impact: your reputation, time, and assets.

Measuring and Improving Social Impacts
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