Are Evaluation Frameworks Keeping up with Innovative Development Financing Instruments?

WRITTEN BY

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In the past decade, social impact bonds (SIBs) and development impact bonds (DIBs) have emerged as a new result-based financing method for program delivery in the social sector. As trillions of dollars have been allotted and ineffectively used for international aid (Moyo, 2011), alternative and innovative approaches to development work have been called upon. Impact bonds promise an innovative funding mechanism for solutions in the justice, education, employment, social welfare, and health industries (Brookings Institution, 2019). They are multisectoral contracts that promote interdisciplinary work across the private, public, and social sectors. The four main players in the impact bond model are the population in need, the investors, the outcome funder, and the service provider (Gustafsson-Wright & Putcha, 2015). For this reason, impact bonds are described as 4-way transactions that tackle stubborn problems in society (McLaughlin, 2011). There have been 206 impact bonds issued across 35 countries in the past 11 years. Of these impact bonds, 194 of them have been categorized as social impact bonds, while the other 12 have been categorized as development impact bonds (Gustafsson-Wright et al., 2021). As SIBs and DIBs are novel and innovative financial structures, they present both opportunities and challenges, many of which relate to their results-based approach and evaluation framework.

The following essay will explore the evaluation dimension of impact bonds. The paper will include background on how impact bonds are structured, an analysis on financing development through impact bonds with a special focus on result-based framework including targets and metrics, concluding with a position regarding findings and recommendations on how to improve the impact bond model. It is important to note that while development bonds have been generally labeled as separate from social impact bonds, they are a form of social impact bond. Development impact bonds differ from typical social impact bonds in two ways: DIBs are issued in low to middle income countries, and their outcome funder is typically a foundation, donor, or development agency, as opposed to a local government. However, in odd cases the government may play a role in repayment upon outcomes achieved by the service provider. For this reason, case studies of impact bonds that have been issued in both developed and developing regions will be included throughout this paper.

BACKGROUND

There are four central components of impact bonds that relate to impact bond evaluation, as described by Gustafsson-Wright and

Putcha (2015): meaningful and measurable outcomes, reasonable time horizon to achieve outcomes, evidence of success in achieving outcomes, and appropriate legal and political conditions. An impact bond is initiated after a social need is identified, and a need for an innovative solution to address it is recognized by the public, private, and social sectors. It is important to note that there is no overarching regulation for impact bond processes and structures; each bond is unique, not only to its context and objectives, but also in how it is established and operates. This allows for a tailored approach to development projects that consider the complexities of a region, its people, and the current issue.

The main stages of the impact bond include a feasibility study, structuring of the deal, implementation, and evaluation and repayment (Gustafsson-Wright & Putcha, 2015). What all impact bonds have in common is that they are structured so that one or more investors raises upfront capital to fund the service provider for the intervention. In this scenario, an outcome funder agrees to engage in the "pay-for-success" impact bond model, which means there are expectations and parameters to pay for positive social change (Maier et al., 2018). The contract can be formed directly between the outcome funder, the investors, and the service provider, but it is more likely to be formed by an intermediary, a broker of the contract who is typically commissioned by the investors, who sets up a special purpose vehicle (SVP) to facilitate the contract and its transactions. The intermediary plays an important role as it is the entity that remains neutral and facilitates negotiations between the other stakeholders. The service provider is either pre-selected to be a part of the bond in an early co-creation setting where negotiations regarding vision and targets take place, or the service provider is chosen through a bidding process that involves less negotiations but in which the service provider appeals to investors or the intermediary by presenting its innovative capacity and promising financial and social return projection. The investors, service provider, outcome funder, and intermediary in most cases, work collaboratively to determine the terms and evaluation framework of the bond.

Terms and targets are determined differently in every impact bond deal, and the extent of negotiations and the dynamic of this phase differs in every case. Stakeholders such as the outcome funder and the investors may have already narrowed down their mutual expectations, but they may also enter this phase willing to negotiate. There are two mainstream impact bond structures, and the structure used determines how the evaluation framework is set. Namely, individual transaction bonds focus on one specific outcome target where repayment is made upon the attainment of one outcome in the set time frame (Gustafsson-Wright & Putcha, 2015). An impact bond may also contain multiple outcome targets, in which case a rate card is issued that establishes payment per outcome attained (Gustafsson-Wright & Putcha, 2015). While performance is typically managed by the intermediary to ensure validity and transparency, external evaluators are always hired for data collection and analysis, or may be hired to validate data collected and analysed by one of the parties involved in the contract (Gustafsson-Wright & Putcha, 2015). In development impact bonds, specifically, external philanthropic organizations sometimes take on tasks related to the evaluation.

ANALYSIS

As the first impact bond was issued in 2010, the field of impact bonds is relatively new and continues to evolve. So, too, have the contrasting views on impact bonds received from academic, civil society, and public commentators. Every impact bond is unique, and this makes it challenging for them to be compared as not only the issues they aim to solve can vary vastly, but the way they are structured and operate can differ too. The following analysis will highlight the different perspectives and evaluation frameworks of impact bonds. While certain aspects will be explicitly positive or negative, there are many aspects which depict tradeoffs or differences in judgement.

Social impact bonds and development impact bonds inherently employ a neoliberal approach as they work towards not only social return, but financial return for the investors providing upfront capital. O'Connor (2016) states a bold claim that impact bonds are "back-handed privatisation mechanisms" (p. 1). She states that "social bonds are a creature of the neoliberal agenda and are the thin edge of the wedge. Behind these experiments is the intent to reorganize funding models for health and social services that will shift responsibility away from the state" (O'Connor, 2016, p. 1). Some scholars and individuals in the field are concerned about the privatization of solutions in the social sector as they claim that impact bonds give investors the chance to profit from social issues (O'Connor, 2016). Capitalist practices such as privatization have contributed to increasing societal inequality, and this inequality has created the very issues that SIBs and DIBs directly address. It is possible that, while impact bonds may work towards solving some societal challenges, they make the rich richer, thus increasing inequalities and creating more social challenges to solve. Conversely, the film The Invisible Heart portrays that funding for interventions, such as the Chicago early education program, would not have been made possible without the support of SIB investors in the private sector (Pequeneza, 2019). Although it may be perceived as an ethical concern of profiting from the marginalized and poor, the capital provided by social impact bonds can make possible net positive social change. Instead, it can then be viewed as not profiting from the vulnerable, but rather profiting from creating solutions that aid the vulnerable. Upfront capital in the form of investment from the private sector, paired with a holistic results-based evaluation framework, may be what actually alleviates poverty, improves livelihoods, and safens living conditions.

EVALUATION FRAMEWORK PROMOTES ADAPTABILITY

The private sector's involvement in social intervention can be advantageous as investors can enhance the capital in the sector through strategic planning and expertise. Impact bonds bring private sector discipline and strength in performance measurement and management (Gustafsson-Wright & Putcha, 2015). The investors encourage service providers to adapt service delivery in order to optimize for desired outcomes (Gutafsson-Wright, 2019). The private sector performance approach is cyclical between monitoring and improvement, as opposed to outdated linear development methods that only conduct a full evaluation at the end of the project and fail to modify the intervention when it is not resulting in adequate change. For example, a development impact bond which targeted girls' education in Rajasthan, India was encouraged to make adjustments when measurements indicated it was not on track to reach its targets. Structural changes were made in the service delivery including more class sessions, more personalized learning, improved curriculum, and home visits from staff of the service provider, Educate Girls, to the students who were absent from school for extended amounts of time (Boggild-Jones & Gustafsson-Wright, 2018). The promotion of adaptability, which was encouraged in order to reroute to reaching results, was credited to render a successful intervention within the assigned time frame.

INNOVATION TO OBTAIN RESULTS

The private sector fosters innovation when changes need to be made in order for the intervention to meet its objectives (Saldinger, 2017). Innovation in cases of impact bonds entails implementing new and unique ideas and changes, which often come with risk, to optimize a component of the intervention (Chamaki et al., 2019). The advantages of innovation in ongoing intervention are credited in the success of the first development impact bond in Latin America and the Carribean (Gutafsson-Wright, 2019). The service provider's ability to reallocate resources in an agile way in order to increase productivity and yield of cocoa and coffee farms contributed to the betterment of livelihoods of Asháninka farmers and their families in the Amazon jungle of Peru (Boggild-Jones et al., 2017).

While the private sector drives innovation, it often also demands innovation that will provide return on investment beyond a single impact bond contract. Investors may have underlying intentions to standardize solutions and evaluation frameworks in order to decrease overhead costs of future social bonds. Maier and colleagues (2018), especially believe that this standardization can make impact bonds more cost-efficient in the future. However, this goal of replicability and scalability can threaten the advantage of context-specific nature of impact bonds.

FINANCIAL MEASURES OF SUCCESS

There is pressure for the intervention to succeed as investors may lose principal, return on principal, or both if outcomes are not met (Gustafsson-Wright & Putcha, 2015). Service providers are also under pressure as they risk their reputation which affects further deals and grants they may obtain, and they often feel that impact bonds are their opportunity to prove their capacity (Gustafsson-Wright & Putcha, 2015). Incentivising payment based on quality of achieved outcomes makes stakeholders rigorous about monitoring and evaluation (Atun et al., 2016). The CEO of Village Enterprise, a service provider of a development impact bond in Uganda that aims to empower microenterprises through building their assets and savings, confirms that when you are paid for performance it becomes even more critical that goals are achieved (Saldinger, 2017). The financial return expectation aspect of impact bonds generates a level of accountability to achieve these outcomes. For this reason, the results-based framework is significantly valued in impact bonds, and, as results will deem whether investors are repaid and in some cases, if service providers will gain a success fee. While the financial dimension of impact bonds can motivate stakeholders to work effectively and creatively towards achieving outcomes, this also means that some good interventions are not pursued because they are not considered to generate significant financial success as they do not meet cost-benefit-ratios that can satisfy investor principal and interest payback (Chamaki et al., 2019).

Expectation of financial return can be attributed to the outcome-driven nature of impact bonds, yet there is also a concern among scholars and those in the field that mission-drift, meaning the drifting away from the primarily intention of social change, may occur as a result of the financial return expectation of the impact bond. At the same time, the investment dimension of the impact bond is also believed to be the most prominent factor of results generation. These results however, are subject to the terms and targets established by the stakeholders during the negotiation and design phase of the impact bond. Typically, the outcome funder wants to establish targets to achieve the most amount of change for the least amount of money, while investors are largely focused on setting targets that are attainable and lower their, and the service provider's, risk of failure. Navigating this negotiation and attempt for balance can be a time and cost-heavy task for stakeholders (Cooper et al., 2014), but once it is completed, targets are generally not changed and evaluation becomes ongoing.

EVALUATION IN INDIVIDUAL TRANSACTION IMPACT BONDS VERSUS RATE CARE-BASED IMPACT BONDS

Gustafsson-Wright and Putcha (2015) state that the simple metric quality of individual transaction impact bonds set a clear focus for the intervention and may also slightly reduce resources needed in evaluation. Meanwhile, rate card-based impact bonds require extensive commercial viability research in order to assess if service providers will be able to achieve multiple outcomes for set prices and require a more layered evaluation framework as multiple targets are established (Gustafsson-Wright & Putcha, 2015). Both types of impact bonds have expensive overhead and transaction costs and in both cases, performance measurement and management is at the forefront of operations.

RELATIONSHIP BETWEEN TARGETS AND DESIRED OUTCOMES

Evaluation frameworks depend on targets established, and the success and failure of impact bonds lies in the link between targets and desired outcomes, as well as targets and sustainable change. There is a risk of misalignment between impact bond targets and desired outcomes. For example, a social impact bond focused on improving conditions at home for at-risk youth in England used an indicator of how many days children spent at the after-care recreational centre, with a target of reducing their days spent there. The contract assumed that this would indicate if homes of at-risk youth became more safe (Pequeneza, 2019). However, the target reached would not necessarily imply that the after-care recreational centre is not needed because youth have been made less vulnerable and can safely be at home, for they could be anywhere, whether it be a safe or unsafe environment, their home or not (Pequeneza, 2019). This is an example of when an evaluation framework and an assigned indicator did not correspond to the actual desired outcome.

However, other impact bonds such as the development impact bond for girls education in Rajasthan, India, have used a comprehensive framework with sound metrics. For example, the project in Rajasthan, India used metrics to evaluate not only the enrolment of girls in schools, but also the quality of education delivered by the service provider, Educate Girls. The development impact bond was contracted between the investor UBS Optimus Foundation that committed $270 000 USD to the intervention, the outcome founder Children's Investment Fund Foundation that agreed to repay the principal and interest to the investor at a 15% internal rate, and a grassroots NGO service provider committed to the right of education among girls in rural India entitled Educate Girls (Boggild-Jones & Gustafsson-Wright, 2018). Meanwhile, Instiglio and IDinsight led independent evaluation services. The terms and targets outlined that 20% of the repayment of outcome was contingent on obtaining 79% of girls education enrolment and 80% of the repayment of outcome was contingent on an increase of 5592 learning levels based on a standardized academic test (Boggild-Jones & Gustafsson-Wright, 2018). The results-based framework was effectively designed and the repayment of outcomes demonstrated that the stakeholders valued the quality of education more than simply the rate of enrolment. Secondly, a control group was used to ensure validity of the increase in learning levels, legitimizing the methodology of the data analysis of this development impact bond. By year three, 92% of girls in the intervention's region were enrolled in school and the intervention had reached 160% of its target to improve the quality of education, as measured by the scores of the academic test (Boggild-Jones & Gustafsson-Wright, 2018). This case illustrates how development impact was achieved through the prioritization of alignment between targets and a community's desired outcomes.

EVALUATION FRAMEWORK: INTENDED AND UNINTENDED CONSEQUENCES

While the girls' education in Rajasthan, India DIB evaluation framework measured intended consequences, and the intervention was considered a success, the unintended consequences of the intervention were not evaluated. Girls were not previously enrolled in school as they took care of their younger siblings and brought extra income for the family in various ways. The framework did not uncover the effects on a girl's household of her school attendance, whether younger siblings are still being cared for, how family dynamics may have changed, and if the family became richer or poorer with her allotting time to studying. Furthermore, the evaluation framework does not include an assessment of the long-term effects of the intervention. Without targets to measure deeper impact, information about unintended consequences of impact bonds will not be captured.

MEASURING LONG TERM EFFECTS

Targets must reflect the sustainability and longevity of a desired outcome. For example, in a development income bond in Colombia which focused on decreasing unemployment rates in a given region, the intervention was effective in placing many people in formal job positions, exceeding targets by 117%, but only 60% of people actually retained their jobs for at least six months (Gustafsson-Wight, 2019). If the evaluation framework had only included a target for job positions obtained, the intervention would be deemed immensely successful; however, as it included a more holistic and long-term measurement that accounted for the future impacts of this intervention, data shows that a job retention issue still remains in the region. This is an example of how, in the impact bond's comprehensive results-based nature, successes and failures are determined by the targets that are set by stakeholders. Adequate targets must be set to understand the long-term effects of an intervention and to evaluate if a desired outcome is truly achieved.

POSITION

The above analysis highlights the multidimensional realities and implications of impact bonds' results-based evaluation methods. The case-to-case nature of each impact bond, which implies its individualized results-based evaluation method, allows for a comprehensive approach to addressing societal issues in a particular community. While there are hesitations in including the private sector in traditional philanthropic, public, or social sector work, it is time to include investors in creating change to leverage not only their upfront capital, but also their strategic and rigorous results-based approach. Impact bonds allow for interdisciplinary teams to set targets together; this collective action can render the most desired outcomes for a community and all of its stakeholders.

Impact bonds are not perfect, but they are malleable in their case-to-case nature, as well as in their incomplete conceptualization which allows for their processes and structures to vary depending on context and issue. While traditional aid has been criticized for creating dependencies and leaving the developing countries worse-off, impact bonds present a possibility for a win-win solution where the intervention is modelled as a deal to leave all stakeholders better-off. While the core structure of impact bonds is efficient, there are adjustments which could be made so the interventions yield better outcomes.

RECOMMENDATION

There is one recommendation which, if actualized, will generate a series of improvements in the overall design, execution, and effects of impact bonds. Inclusion and empowerment of community representatives who are most affected by the impact bond should be prioritized, so that positive outcomes are amplified and evaluations frameworks are made more community-driven.

The impact bond structure is sound as long as the risk and the cost of de-risking is less than the cost of traditional aid financing which generates dependencies and is often referred to as "dead aid" (Moyo, 2011). Innovation as a driving force of the impact bond intervention is excellent, as is its multisectoral collaborative nature, however, the latter can and should be further improved.

The majority of literature does not identify how the individuals at the forefront of challenges are being included in the impact bond contract. For agency-based development, it is crucial that representatives from the given community have a seat at the intermediary table among the other stakeholders. This is critical in the creation of evaluation frameworks as beneficiaries are the ones who know their community's priorities and objectives. They are familiar with the culture and the realities of the conditions, which can aid in developing realistic and relevant targets. Their input would address the issue where there is a misalignment of targets and desired outcomes. The communities closest to the issue may have specialized knowledge on how to modify an aspect of an intervention for it to work. Drawing on the theme of interdisciplinarity of impact bonds, their expertise should be utilized to optimize performance and strive towards achieving results. It is thus in every stakeholder's best interest to include community representatives in impact bond contract design and execution.

If impact bond intervention is community-driven, it can prevent mission-drift and avoid clouding from the pressure of financial return. As certain views depict the ethical dilemma of profiting from the poor, incorporating and valuing beneficiary involvement will ensure that the impact which is generated is genuine and corners are not cut for financial return. Beneficiaries should be so involved in the impact bond that they learn financing and reinvestment strategies, sound results-based framework creation and evaluation, and the tools to recreate and continue the work of the impact bond. This type of capacity-building will create lasting effects for the community and mitigate the risk of dependency created by donors. Ensuring that beneficiaries are represented from the very beginning to the end of the impact bond contract is imperative to a solution which will match the needs of the people who experience the most hardship.

Impact bonds have demonstrated early success as emerging and evolving new instruments that bring private financing to social sector issues. The impact bond structure is fundamentally different from traditional aid structure because of its private sector involvement and investment strategy which promotes a rigorous results-based evaluation framework. As the impact bond model is still fairly new, and even newer in the developing world, more time and research is needed to evaluate its effects on communities. For example, topics such as whether success of interventions is attributed to sound intervention design and execution or because of the financing and disciplined private sector performance mechanisms is difficult to assess, and more work is needed to delve into these answers so that further improvements can be made. Innovation is needed in the development sector right now more than ever as we are faced with inefficiencies and ineffectiveness in a world with growing inequality and an exponentially rising population. Impact bonds offer an alternative to traditional aid programs through their multisectoral approach, strategic financing, and rigorous results-based framework. If their evaluation frameworks reflect the highest interest of the communities they seek to serve, they may pave an impactful future in the development sector.

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