Innovative Finance for Education

Case Study

India Education Outcomes Fund

A Case Study

Archana **Mehendale**
Ajay **Singh**

NORRAG Network for international policies and cooperation in education and training
Réseau sur les politiques et la coopération internationales en éducation et en formation

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TISS Tata Institute of Social Sciences

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ABOUT THE PROJECT

This case study is a result of the COFER Innovative Financing in Education and Development: Case Studies and Multi-Media Material for E-Learning project, partially funded by the swissuniversities Development and Cooperation Network (SUDAC) under the development of 'Consortia for Education and Research (COFER)'. The consortium is composed by the following partners: NORRAG, an associate programme of the Graduate Institute, Geneva, University of Fribourg (Switzerland), Zurich University of Teacher Education (Switzerland), Universidad Nacional de General Sarmiento in Buenos Aires (Argentina), Beijing Normal University (China), Tata Institute of Social Sciences in Mumbai (India), University of Cape Town (South Africa).
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ABOUT TISS

Tata Institute of Social Sciences (TISS) in its 80-year history has served as an institution of excellence in higher education that continually responds to changing social realities through the development and application of knowledge towards creating a people-centred, ecologically sustainable and a just society. It has 21 schools and 45 research centres spread across four locations in India. The Centre for Education Innovation and Action Research (CEIAR) is a multidisciplinary centre focusing on quality education, innovation, education technology, teacher professional development, education law and policy. It is part of international knowledge sharing partnerships, such as the SUDAC-IFE consortium and TPD@Scale Coalition for the Global South among others. Its flagship program Connected Learning Initiative has been widely published and has won the UNESCO-King Hamad Prize for the Use of ICTs in Education (2017) and the Open Education Award for Excellence (2019).

ACKNOWLEDGEMENTS

The development of this teaching case study would not have been possible without the contribution and support of many individuals and organizations. The authors would like to especially thank the representatives of Social Finance India for their insights, reflections, contributions and ideas. Additionally, this work would not have happened without the full-fledged support and valuable guidance from Satyajit Salian, Head – Education, Tata Trusts. The authors would also like to acknowledge all the respondents who gave time despite their busy schedules to share their perspectives on the subject; representatives from Central Square Foundation, Educational Initiatives, IndusInd Bank, Kaizen Private Equity, Language Learning Foundation, Nishith Desai Associates, Social Finance India, and Tata Trusts.

NORRAG

Network for international policies and cooperation in education and training

Réseau sur les politiques et la coopération internationales en éducation et en formation

20, Rue Rothschild l P.O. Box 1672
1211 Geneva 1, Switzerland
+41 (0) 22 908 45 47
norrag@graduateinstitute.ch

NORRAG Case Study, July 2020

NORRAG is supported by

Schweizerische Eidgenossenschaft
Confédération suisse
Confederazione Svizzera
Confederaziun svizra
Federal Department of Foreign Affairs FDFA
Swiss Agency for Development and Cooperation SDC
Education Unit

OPEN SOCIETY FOUNDATIONS

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INSTITUT DE HAUTES ÉTUDES INTERNATIONALES ET DU DÉVELOPPEMENT
GRADUATE INSTITUTE OF INTERNATIONAL AND DEVELOPMENT STUDIES

This work was presented at a panel discussion on "Innovative Financing Case Studies and Debates in the New PPP Aid Architecture" as part of Graduate Institute Education Series #1, organized by NORRAG in collaboration with IHEID on 30 January 2020, and has benefited from questions and remarks of the participants. The feedback received from members of this inter-university partnership has helped shape and improve its content and presentation. Arushi Terway from NORRAG not only provided valuable guidance and support but also peer-reviewed earlier drafts of this document. Munaf Merchant and Padma M. Sarangapani provided overall support to anchor this work at TISS. Anouk Pasquier Di Dio and Alexandru Crețu supported the final production of the case study.

This teaching case study highlights the idea and design of IEOF which is still under development and is based on interviews conducted in November 2019. It may be used by itself or along with the accompanying videos on the subject. Teaching Notes accompanying the case study may be referred to for laying the learning objectives, structuring class discussion, providing additional readings and engaging participants in exercises.

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EXECUTIVE SUMMARY

The 2030 Agenda for Sustainable Development resolved to create universal literacy and provide inclusive, equitable, and universal access to quality education at all levels. It also called for a revitalized global partnership for realizing the implementation targets by 2030. The report of the Education Commission in 2016 estimated that the global funding gap to ensure quality education for all children was USD 1.8 trillion per year. In India, the size of the financing gap is estimated to be USD 740 billion for the period 2015-2030. Although the government remains to be the single largest contributors of education financing, its allocation of 3.4% of the GDP (USD 63 billion annually) falls short of the 6% target enunciated in the national education policy and the Education 2030 Framework for Action.

There is an increasing involvement of the private sector to fill in the gap. India has seen an expansion of private spending on education. Out of a total of USD 133 billion annual market of education in India, the annual private expenditure is USD 56 billion. With India's economic growth and global positioning, it is no longer deemed as a poor, developing country. As a result, foreign aid inflows to education in India have declined. The statutory obligation of Corporate Social Responsibility (CSR) has helped release funds from the private sector for social causes. India is also seen as one of the most attractive markets for impact investing worldwide.

This case study showcases the design and the process of establishing a catalytic platform, the India Education Outcome Fund (IEOF) of Social Finance India (SF-IND), aimed at providing sustainable and innovative funding at scale to deliver educational outcomes. The IEOF is still under development but readers of this case study can learn about what is involved in setting up such a platform by understanding the issues encountered, choices made and implementation mechanisms being considered for adoption in the marketplace.

Social Finance India (SF-IND) was established in 2018 as a nonprofit organization dedicated to harnessing capital to address social challenges, with the financial support of Tata Trusts and the Global Steering Group for Impact Investment (GSG). It is part of the Social Finance Global Network (SFGN). SF-IND set up the IEOF with an aim to create transformational impact in Indian education through funding USD 1 billion of outcomes-focused activities by 2030. As far as the status of education is concerned, India has achieved access and participation of children in education and the major challenges are those of learning crisis and equity concerns.

The IEOF platform differs from existing traditional funding mechanisms of education as well as the typical impact bond structures on education. It is designed to address and overcome the problems and limitations currently experienced in these funding arrangements. As a marketplace, it is intended to create impact at scale and address the limitations of individual, bespoke development impact bonds (DIB) and structuring processes. As a platform, IEOF works towards bringing efficiencies and thereby lowering administrative costs.

The IEOF has identified five thrust areas on which innovative financing mechanisms are being developed. They are: Early Childhood Education, Foundational Learning Skills, Secondary Learning, School to Workforce transition, and Inclusive education (learning and intellectual disabilities) thereby covering the entire spectrum of the education sector. Work on these thrust areas is conducted through a phased manner that is planned over the course of ten years aligned with the Sustainable Development Goals deadline of 2030.

The IEOF is still under development. It has currently:

- Developed and convened all partners to launch the first-in-the-world innovative structure with their first pilot impact bond
- Developed a strategy to deploy outcomes funds over a ten-year period
- Conducted thorough due diligence to evaluate 150+ service providers
- Consulted with industry experts to validate the approach
- Secured commitments for risk capital
- Evaluated multiple forms of funding engagement for risk and outcome funders

The process of setting up the marketplace has involved the following key aspects:

- **Ensuring the supply of high-quality interventions.** This is done by conducting a service provider landscape analysis, two rounds of due diligence and using a decision tree to determine what interventions are “DIB-able”[1].

- **Securing investments and pricing outcomes.** This involves raising the risk capital for funding the mechanisms. This will be done by a private equity firm working in the education sector. Determining outcomes and pricing them is an important exercise. Given the existing gap in reliable data to help this process, the IEOF has adopted a two-wave approach, wherein Wave 1, existing proven programs will be scaled, and evaluated to set a benchmark for success and prices per outcome. In Wave 2, there will be a greater emphasis on the competitive cost of an outcome and service providers will bid on specific outcomes through a rate card approach. Determining payment metrics is challenging and is based on certain guiding principles.

- **Designing financing mechanisms.** Given the absorptive capacity of the sector, needs of the sector and prevailing regulatory regime, the IEOF has designed pooled DIBs that would operate in each of the thrust areas bringing efficiencies through scale. It may also explore alternate mechanisms such as Social Impact Incentives and Social Success Notes. A DIB with an unconventional structure has been launched in 2020.

- **Formulating contracting structures.** One of the most complex challenges in an innovative financing mechanism is the formulation of contracting structures. The IEOF is considering direct and intermediated structures. As an intermediary, the IEOF is the key agency which contracts with all parties and coordinates the mechanism.

- **Planning for Monitoring, Evaluation and Capacity Building.** The process of setting up the ecosystem also involves putting in place a robust system of performance management to ensure that the investment risks are minimized, empaneling independent evaluators who can assess if the intended outcomes have been achieved and if payouts can be made. Additionally, the process also involves providing service providers with incentives and capacity building to work within the new ecosystem.

During this process, stakeholders have encountered several issues and challenges. The case study discusses two types of issues.

Organization-related issues are those that affect the establishment and work of the IEOF. These include getting the right kind of people to work with IEOF, working through a top-down process to sell the idea and get the key decision-makers or influencers excited and convinced before working with other stakeholders, and the need to place greater emphasis on grit among all stakeholders so that they do not abandon the process mid-way but make it work till the end.

There are also mechanism or instrument-related issues. First, the impact bond as an instrument is not an appropriate answer for all educational challenges. Since not all outcomes are easily measurable, there is a concern that impact investing will fund and take up only those programs that aim to achieve measurable outcomes and leave out programs that are worthwhile but cannot be easily measured with the existing tools. This may lead to a segmentation of the education sector, where certain challenges and various organizations are DIB-able. The second issue is that between supporting experimental or proven initiatives, there is a challenge to search for that sweet spot which balances the two. The question which needs to be assessed on a case-by-case basis is ‘how much risk is acceptable to the parties involved?’ Third, there is a strong criticism that the idea of tapping into nonconventional funding is not occurring because it is the same philanthropic funding that is getting tapped and channelized into impact bonds. Fourth, the legal, tax and regulatory norms in India impose a number of restrictions on philanthropies, foundations, CSRs that are trying to engage with the new ecosystem. Fifth, the cost of setting up the ecosystem and its claimed efficiencies are issues that deserve further study. Factors such as readiness of the sector, pipeline of DIB-able programs, regulatory norms, and the availability of investors and outcome payers create serious impediments to scaling, thereby making the process inefficient. Lastly, planning for sustainability of the IEOF platform is also a challenge, given that the business model for funding the IEOF as an intermediary has not been tested yet.

Video 1: What is India Education Outcomes Fund?

1. A ‘DIB-able’ intervention is one in which the DIB model is identified as a suitable approach to tackle that social issue. To determine if a DIB should be adopted, Social Finance India assesses whether there is a clear specific target group, defined outcomes, identified interventions that can achieve those outcomes, consistency in the plan to achieve the outcomes, and potential to achieve value for money and/or outcomes in case payment is conditional to it.

1

CONTEXT

The 2030 Agenda for Sustainable Development (United Nations General Assembly resolution 70/1, 2015) resolved to achieve universal literacy and provide inclusive, equitable, and universal access to quality education at all levels. It also called for a revitalized global partnership for realizing the implementation targets by 2030. The report of the International Commission on Financing Global Education Opportunity (2016), or the Education Commission, estimated that the global funding gap to ensure quality education for all children was USD 1.8 trillion per year. In India, the size of the financing gap is estimated to be USD 740 billion for the period 2015-2030 (Bhamra et al., 2015).

Although the government remains the single largest contributor of education financing, its allocation of 3.4% of the GDP (USD 63 billion annually) falls short of the 6% target enunciated in the national education policy and the Education 2030 Framework for Action. This gap in funding poses a threat to the opportunity of reaping the demographic dividends. India has also seen an expansion of private spending on education by families. Out of a total of USD 133 billion annual market of education in India, the annual private spending is USD 56 billion (Kaizen, 2014).

There is an increasing involvement of the private sector to fill in the funding gap. This investment is evident in the core education (provision of K-12 and college), parallel education (preschools and tutoring) and in ancillary education (textbooks, education technology, etc.) accounting for nearly USD 55 billion annually (Kaizen, 2014). With India's economic growth and global positioning, it is no longer deemed as a poor, developing country. As a result, foreign aid inflows to education in India have declined. There is a greater emphasis on the mobilization of domestic resources. The statutory obligation imposed by The Companies (Amendment) Act, 2014 on the corporate sector to spend 2% of their average net profits of three years for social causes, commonly referred to as Corporate Social Responsibility (CSR), has helped release funds from the private sector. India is also seen as "one of the most attractive markets for impact investing worldwide. High demand for investments is likely to continue as a result of a growing population, underlying economic growth, stable financial markets with a strong rule of law, combined with large unmet social needs" (Pandit & Tamhane, 2017, p. 13).

On the other hand, although access and participation in schooling have been largely achieved, the learning crisis is seen as the biggest challenge in the education sector with national standardized tests such as National Achievement Surveys and Annual Status of Education Reports showing poor learning outcomes. Inequities in education also pose complex challenges to the Indian education system. On this background, the focus of educational interventions is becoming more outcomes-focused and results-driven. The success of Educate Girls DIB, the first Development Impact Bond (DIB) on education in Rajasthan, stirred national and international interest in the new mechanism among different stakeholders.

It is on this background that the process of setting up an ecosystem for innovative financing through pay-for-success kind of mechanisms needs to be understood. This case study showcases the design and the process of establishing a catalytic platform, the India Education Outcome Fund (IEOF) of Social Finance India, for providing sustainable and innovative funding at scale to deliver educational outcomes. The IEOF is still under development but readers of this case study can learn about what is involved in setting up such a platform by understanding the various issues encountered, choices made and implementation mechanism adopted in setting up the marketplace. Such a focus on the design and process is expected to generate discussion and reflection on the potential and challenges involved in setting up an ecosystem for innovative financing in India.

2

ESTABLISHMENT OF SOCIAL FINANCE INDIA

Social Finance India (SF-IND) was established as a nonprofit organization with the financial support of Tata Trusts. Its mission is "to harness capital to address social challenges where outcomes are poor, where the system is acknowledged to be failing and where the costs of failure are high" (Social Finance India et al., 2019, p. 29).

It is part of the Social Finance Global Network (SFGN), with sister organizations in the United Kingdom, United States, Israel and the Netherlands. Started in 2007, the Social Finance UK pioneered outcome-based financing with the Social Impact Bonds and was founded by Sir Ronald Cohen, who brought in his experience in private equity and the work he chaired on the Social Investment Task Force for the HM Treasury. Being directly involved in over a quarter of all the impact bonds and being in an advisory capacity for a vast majority of the other impact bonds across the world, Social Finance was already established as subject matter experts in impact bonds and innovative financing.

By 2017, there was a realization that individual, bespoke impact bonds with one service provider, one outcome payer, and one or more risk investors have an inherent limit to what they can scale up. The costs involved in contracting, performance management, outcomes assessment became high and inefficient. Therefore, preference towards large-scale commitments from outcome payers for longer durations, allocating funds to different services providers, and managing the whole flow of money by an entity like Social Finance or an Outcomes Fund, was considered to be a worthwhile proposition for India. So, in August 2017, in a meeting between Sir Ronald Cohen and Mr. Ratan Tata, Chairman of Tata Trusts[1], the need to establish an entity that would anchor outcome-focused financing at scale and align with the achievement of the Sustainable Development Goals in India came up. Tata Trusts is one of the largest philanthropies in India and has given USD 303.5 million between 2013-15 for various developmental activities (OECD, n.d.). Mr. Tata expressed interest in supporting the establishment of the entity in India (Tata Trusts education lead, interview). Sir Cohen reached out to some of the people associated with the education sector and the social sector in India and constituted the Board. He also met with officials at the Niti Aayog, the national planning agency, and bureaucrats to understand the potential for such structures in India and was convinced that the challenges confronting the education sector in India can be addressed by outcome-based innovative structures offered at scale. Thus, Social Finance India (SF-IND) came into being in 2018 with the support of the Tata Trusts and the Global Steering Group for Impact Investment (GSG). Even before the organization was officially set up, the core team of the SF-IND was coming together. During the launch of SF-IND in October 2018, two funds of USD 1 billion each were announced – the India Education Outcomes Fund (IEOF) and India Impact Fund of Funds (IIFF).

From March 2019, the SF-IND is solely focused on the IEOF which is meant to build an ecosystem for impact investing in the Indian education sector. The IEOF is the first fund of its kind in India that aims to catalyze private, social and government sectors and to work at scale. The IEOF is expected to raise and disburse USD 1 billion to education outcomes through innovative financial instruments by convening partnerships across investors, service providers and outcome funders to address India's most pressing education challenges.

1. The Tata Trusts has been one of the oldest, largest and non-sectarian philanthropies in India working across various portfolios and regions of India. It comprises allied Trusts and philanthropies. According to the Annual Report 2018-19 of Sir Dorabji Tata Trust & Allied Trusts, USD 66.59 million were disbursed as grants with eight percent going towards education projects. According to the Annual Report 2018-19 of Sir Ratan Tata Trust & Allied Trusts, USD 156.35 million were disbursed as grants with six percent going towards education projects.

3

THEORY OF CHANGE

The idea of setting up IEOF as a marketplace for innovative financing mechanisms emerged in response to the key problems confronting financing of education in India and its value propositions have been established in comparison to the traditional financing mechanism in place. Let us look at each of these, before reviewing IEOF theory of change.

Problem Statement

The IEOF responds to two key problems related to the financing of education in India. These problems can be categorized as (a) problems with regards to government allocation to education, and (b) problems faced by the nongovernmental organizations working in the education sector.

Government allocation to education

As mentioned earlier, the current government spending on education is insufficient to meet the targets set by the SDGs. Furthermore, budget allocations are restricted, with a large proportion going into teacher salaries and administrative costs, and only a small proportion allocated towards improving the quality of education and trying new ways of working. Government bureaucracy also creates a challenge to bring different stakeholders together to work on shared goals and targets at scale.

Problems faced by nongovernmental organizations

Nongovernmental organizations run a number of educational interventions in the education sector in India. Although they work at a small scale and cannot replace the government in its responsibility of providing and financing education to all, they offer innovative programs that can help improve access and quality of education. One of the problems faced by those working in the school education sector is the insecurity about receiving funding and continued funding to implement their programs. Even the funding that is provided is likely to be restrictive in terms of what inputs and activities can be funded and what cannot. Organizational leaders spend considerable time with fund-raising leaving less time to provide strategic direction and leadership to the implementation effort. Organizations need greater flexibility to innovate, design strategies and scale, along with opportunities to synergize and link with other stakeholders. Organizations have traditionally focused on delivering inputs and focusing on the process, and there is an increasing requirement from the donors for greater accountability for the production of outcomes.

Value Propositions

The IEOF platform differs from existing traditional funding mechanisms of education as well as the typical impact bond structures on education. It is designed to address and overcome the problems and limitations currently experienced in these funding arrangements.

At present, most of the traditional grant-making in education is costly with individual contracts, is input-based, and has a relatively smaller focus on the production of outcomes. Furthermore, the outcomes are likely to be fragmented across outcome areas, reducing the potential of creating impact. In comparison to traditional individual program funding, the value proposition of IEOF can be summarized as follows:

1. Central contracting capability: will help reduce contracting costs by using a common central mechanism to disburse funds across multiple programs;
2. Encouraging price competition: will lead organizations to deliver quality outcomes using the most economically efficient means;
3. Mitigating performance risk: will aggregate outcomes achieved across a portfolio of programs;
4. Open-ended India-specific data development: will build a centralized repository of knowledge that can help inform future scaling of interventions;
5. Adaptive management styles: will raise the odds of success by measuring and changing course during an intervention and responding to reality on the ground
6. Catalyzing sustainable funding: will be enabled by creating a larger platform of specialist working capital, creating a longer-term stable source of funding and capacity building for service providers (Social Finance India et al., 2019, p. 79).

The IEOF is a marketplace intended to create impact at scale. It is designed to be different from a typical impact bond structure or Development Impact Bonds Version 1.0. As seen in Figure 1, Version 1.0. of Development Impact Bonds (DIB) generally start with an investor providing working capital to a service provider. The investor can be anybody willing to take the initial 'risk' of covering the costs of a program upfront. The service provider could be a nonprofit or a for-profit social enterprise that implements the program with the help of the working capital and reaches a set of targeted beneficiaries. The outcome evaluator is a third-party independent agency that assesses the outcomes achieved and submits a report to the outcome payer. An outcome payer is a body that has contracted to pay the investors their principal amount invested and an interest based on the results achieved. When the outcome payer is the government, it is called a social impact bond. In some cases, outcome payers also pay incentives to the service providers based on the results achieved. Each DIB is designed and structured with contractual obligations about agreed outcomes and targets, timeframes, payments, evaluation metrics and methods and other details.

As a marketplace, the IEOF is designed to create impact bonds at scale and address the limitations of impact bonds Version 1.0. Its value proposition can be summarized as shown in Figure 2. In terms of the commissioning structures, typically, impact bonds have been

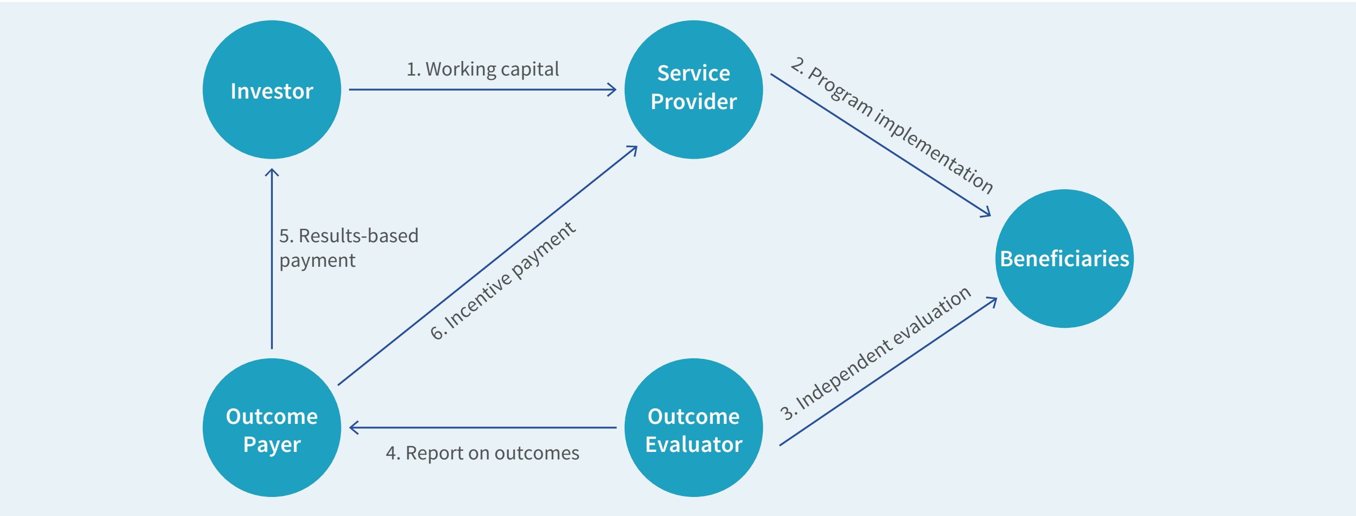

Figure 1: Structure of Development Impact Bonds Version 1.0. Adapted from Ziswiler, M., & Terway, A. (2019). Tackling the global education crisis: the UBS Optimus Foundation's use of social finance. In N. Y. Ridge, and A. Terway (Eds.), Philanthropy in Education (pp. 54-69). Edward Elgar Publishing. CC License.

structured as individual, bespoke deals, with lengthy negotiations and structuring processes. The IEOF seeks to accelerate the contracting time by developing pooled funds and thereby lowering administrative costs. The "IEOF will move impact bonds from one-off agreements to working at a greater, more efficient scale." (Social Finance India et al., 2019, p. 22) The standardization of processes will bring down the costs, and using a rate card approach will allow multiple contracts per issue area. Impact bonds at scale will be able to create a larger pool of outcome funds by offering multiple similar contracts per issue/area. The overheads of contracting as well as the high costs of evaluation can be reduced when offering impact bonds at scale. In other words, while Impact Bonds V1.0. work as small and expensive pilots today, the IEOF is a cost-effective and efficient platform that will deliver impact at scale.

The IEOF Theory of Change is shown in Figure 3. As mentioned earlier, the overall vision of IEOF is to create transformational impact in education in India through funding USD 1billion of outcomes-focused activity by 2030. Its mission is to create an ecosystem that

Impact Bonds V 1.0.		IEOF – Impact Bonds at Scale
Bespoke, individually designed contracts - with most DIBs designed in isolation/ 'reinventing the wheel'	→	More standardized contracts, processes, legal structures - building and sharing public goods for efficient structuring and commissioning
Small scale, pilot contracts, with small pot of outcome funds relative to the contracting cost	→	Larger pools of outcome funds per rate card, allowing larger DIB contracts and/ or to 'plug and play' across multiple similar contracts per issue or area
Individual projects - that each requires all the overheads associated with structuring an impact bond	→	Pooled funds for programs - commission multiple contracts, and central expertise and resources to structure contracts
High cost, bespoke M&E program (e.g., RCTs)	→	Cost-effective evaluation, leveraging technology and existing evaluation frameworks to ensure M&E can be achieved at high quality and low cost

Figure 2: Impact Bonds Version 1.0. versus Impact Bonds at Scale. Adapted with permission from Social Finance India, India Education Outcomes Fund, GSG. (2019). India Outcomes Fund Prospectus 2019 (p.22).

can launch scalable outcomes-focused solutions to address India's pressing education challenges with the help of skilled service providers, investors and funders. Its current strategic priorities are: first, to raise risk capital and outcomes funds to invest across multiple interventions; second, to design strong delivery, evaluation and performance management with all stakeholders; and third, to identify and scale proven high-impact and high-potential interventions.

The outputs that will be delivered include (a) prioritized investment opportunities, based on proof of scalable impact, (b) financial instruments to mitigate risk for outcome funders and risk investors, (c) a robust performance management framework for a phased approach, (d) a clear platform for engagement to facilitate strong working relationships with all partners, and (e) strong relationships with state governments to mobilize investments at scale.

The outcomes that IEOF aims to achieve are: funding to scale proven impact is catalyzed and aligned with national priorities; a portfolio investment model is created to maximize the potential for all investors; outcome funder money is stretched further by having them pay only for outcomes achieved; funding under corporate social responsibility is innovatively and effectively utilized; and an ecosystem of accountable service providers, investors and funders able to work at scale is created.

VISION
To create transformational impact in Indian education through funding USD $1BN of outcomes focused activity

MISSION
To create an ecosystem of skilled service providers, investors and funders to operationalize scalable, outcomes-focused solutions that address India's pressing education challenges

STRATEGIC PRIORITIES
- Raise DIB funds to operate opposite risk outcomes funds to invest across multiple interventions
- Design strong delivery, evaluation and performance management with all stakeholders
- Identify and scale proven, high-impact and high-potential interventions

OUTPUTS
- Prioritized investment opportunities, based on proof of scalable impact
- Financial instruments to mitigate risk for outcome funders and risk investors
- A robust performance management framework for a phased approach (Wave 1 and Wave 2)
- A clear platform for engagement to facilitate strong working relationships with all partners
- Strong relationships with state governments to mobilize investments at scale

OUTCOMES
- Catalyzed funding to scale proven impact, aligned with national priorities
- A portfolio investment model to maximize the potential for all investors
- Outcome funder money will go further, through paying only for outcomes actually achieved
- Innovative and impactful uses of corporate social responsibility funding in India
- An ecosystem of accountable service providers, investors and funders able to work at scale

Figure 3: IEOF Theory of Change. Adapted with permission from Social Finance India, India Education Outcomes Fund, GSG. (2019) India Education Outcomes Fund Prospectus 2019 (p. 46).

4

KEY ACTORS, ROLES AND LINKAGES

The bringing together of various stakeholders assumes a central place in the IEOF approach. Figure 4 shows the various actors involved in the SF-IND and IEOF and their roles and interlinkages.

Board of Directors - The Board of Directors was constituted at the very beginning and provides an overall leadership and direction to the SF-IND. The Board brings together long-standing experience and credibility in social finance, business, entrepreneurship, institution building and the development sector.

Knowledge Partners - The knowledge partners provide advice and guidance on impact investing, the education sector and the legal system. They have offered pro bono support to SF-IND on various tasks during the initial period.

Donors - The Tata Trusts is the main donor to SF-IND. It is providing funds for developing the ecosystem and supporting the establishment costs of SF-IND and also costs of putting together the constructs.

SF-IND-IEOF Team - The core team of SF-IND-IEOF manages all responsibilities associated with setting up the IEOF platform and is responsible for liaising with all stakeholders.

Steering Committee - A Steering Committee has been set up to provide oversight and guidance on the impact bonds. This consists of key stakeholders. The performance management reports to the Steering Committee on the progress of the funds.

Risk Investors - The IEOF has contracted Kaizen Private Equity to raise funds on the risk investment side. In addition, the IEOF can also contract other entities, including foundations, to cover the risks of investments made as performance guarantors.

Outcome Payers - The outcome payers could be CSRs, foundations and donors. The long-term goal is to have the government as an outcome payer.

Service Providers - The service providers are organizations that have been identified by the IEOF through landscaping analysis and due diligence. The service providers could be working on any of the five thrust areas of the IEOF. They could be nongovernment organizations or social enterprises.

Third-Party Evaluators - A third-party evaluators are selected through a process of competitive selection.

Beneficiaries - The ultimate beneficiaries are the children, youth, teachers, teacher educators, communities and others who will benefit directly from the program interventions.

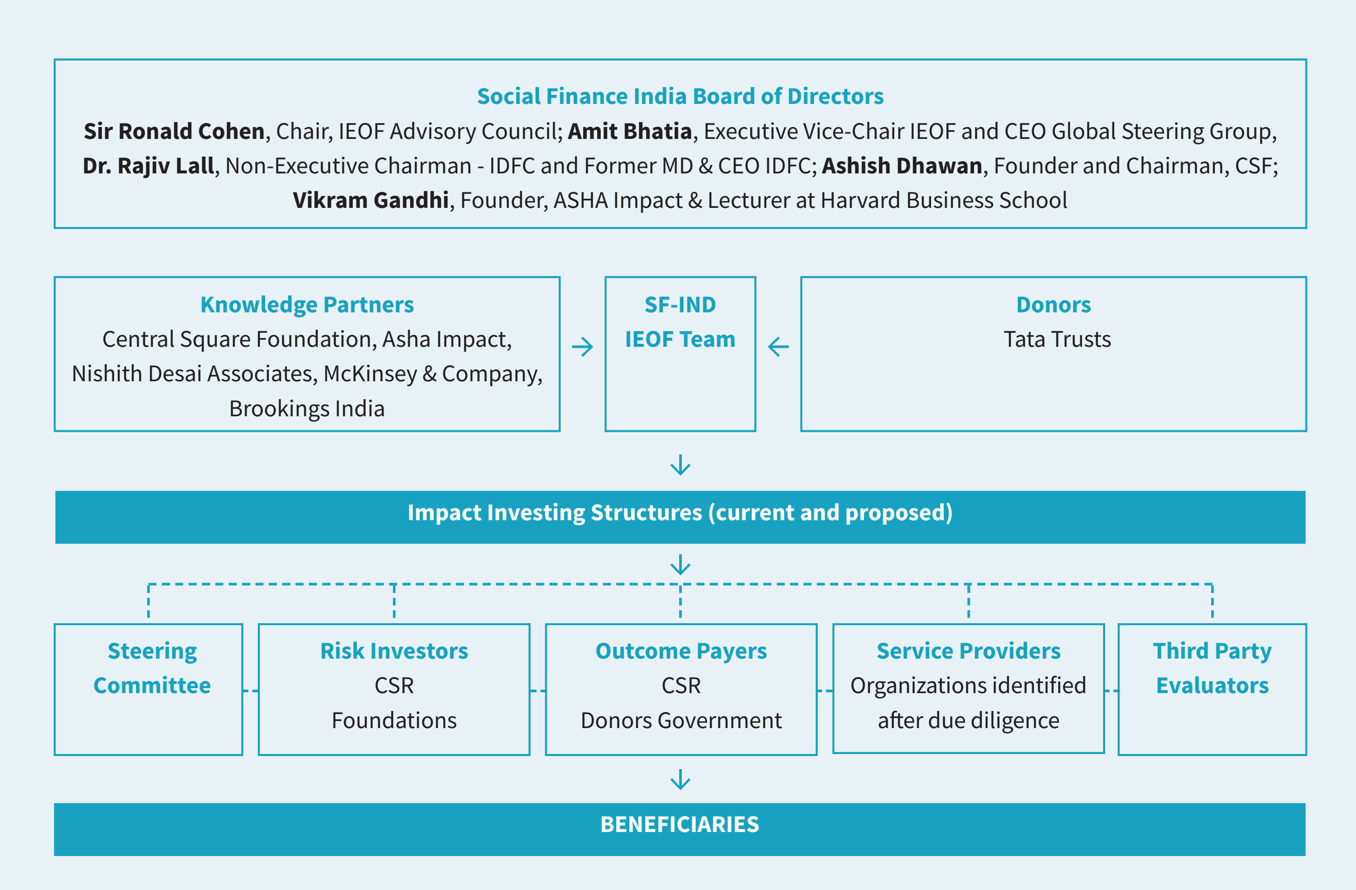

Figure 4: Key stakeholders of SF-IND-IEOF. Based on interview with SF-IND-IEOF lead, information contained in Social Finance India, India Education Outcomes Fund, and GSG (2019). India Education Outcomes Fund Prospectus 2019 (p. 27, 30 & 44) and Social Finance India website https://socialfinance.org.in/partners/

5

APPROACH

Keeping in mind the Sustainable Development Goals, the IEOF has identified five thrust areas on which innovative financing mechanisms will be developed.

They are:

1. Early Childhood Education
2. Foundational Learning Skills
3. Secondary Learning
4. School to Workforce transition
5. Inclusive education (learning and intellectual disabilities).

Work on these thrust areas is being done in a phased manner. Currently, the focus of the interventions is improving the quality of education in government schools. In order to help achieve impact at scale, the phased approach is planned over the course of ten years aligned with the SDG deadline and involves three phases. The objectives and focus of each of these three phases are given in Table 1 below.

Table 1: Phased approach to achieving impact at scale

Phase	Objectives and Focus
4 years – Build-up phase (2020-2024)	• Demonstrate how the IEOF constructs deliver better outcomes • Bring in the element of measurability into the sector • Make the constructs work with all the entities involved, including service providers, outcome payers and risk investors • Create enough evidence for an "outcomes rate card" and come out with an approach of pricing outcomes that can also interest the government • Work with philanthropies, foundations, corporates as investors or outcome payers • Target INR 150-200 crores (USD 2-2.6 million) commitment per year
3 years – Ramp-up phase (2024-2027)	• Reach out to wider and deeper - across the corporate community, number of states • Target INR 300-350 crores (USD 3.9 – 4.5 million) commitment per year
3 years – Consolidation phase (2027-2030)	Involve government, with a couple of impact bonds where the government is an outcome payer

Currently, the IEOF has chosen to start its first impact bond in the area of foundational learning skills in Haryana.[1] Some of the design considerations of the DIB are presented later in this case study. Overall, the IEOF has currently:

- Developed and convened all partners to launch the first-in-the-world innovative structure with their first pilot impact bond
- Developed a strategy to deploy outcomes funds over a ten-year period
- Conducted thorough due diligence to evaluate 150+ service providers
- Consulted with industry experts to validate the approach
- Secured commitments for risk capital
- Evaluated multiple forms of funding engagement for risk and outcome funders

In the following sections, we will take a closer look at the process of creating the ecosystem and understand the various design components that go into laying the foundation.

1. The Haryana DIB was announced on July 20, 2020.

6

PROCESS OF CREATING THE ECOSYSTEM

Setting up the IEOF as a marketplace for innovative financing in India has involved preparations of over eighteen months. During this time, various design components were established, ideas were tested out and challenges identified.

The process has involved:

- Ensuring the **supply of high-quality interventions**
  - Service provider landscape analysis
  - Due diligence
  - Determining what are DIB-able interventions

- Securing **investments and pricing outcomes**
  - Risk capital
  - Pricing outcomes and rate card approach
  - Payment metrics

- Designing **financing mechanisms**
  - Pooled DIBs
  - Social Impact Incentives
  - Social Success Notes

- Formulating **contracting structures**
  - Role of intermediary

- Planning for **monitoring, evaluation and capacity building**
  - Performance management
  - Independent Evaluation
  - Capacity Building

Let us take a closer look at each of these components and the issues being addressed.

Supply of high-quality interventions

Even though India has numerous organizations and social enterprises working in the education sector, identification of high-quality interventions and service providers that can absorb innovative funding and deliver impact at scale is a crucial task. Using the work of Cooley and Ved (2012) on scaling organizations, the IEOF has developed a thorough process of evaluation of the service providers which involves three stages as shown in Figure 5. At first, the IEOF conducted a **service provider landscape analysis** which entailed secondary research of organizations working in a particular thrust area, interviews with donors, impact investors and philanthropists to check the extent of endorsement and the financial support for a given organization, and screening the list of service providers with experts from the sector. This landscape analysis covered over 150 organizations. Based on the list of organizations validated through the landscape analysis, around 80 organizations were identified for due diligence. The second and third stages involved due diligence. This included checking the legal and governance standing, finances, ability to deliver and measure impact, risk management and details related to the program (see Annex 1 for a broad framework guiding assessment of organizations). After this, 38 organizations were selected for primary research to evaluate existing program data, field operations, feedback from existing donors and capability to scale. The main objective of the due diligence process is to identify service providers that:

- Are aligned with the objectives of the fund
- Have strong leadership and governance capabilities
- Have one or more programs that have demonstrated positive results and can be scaled
- Have the capability to expand delivery that working at scale entails
- Have an absorptive capacity for a capital influx
- There is a recognition that an impact bond mechanism is not appropriate for all education interventions (SF-IND-IEOF lead, interview and Tata Trusts education lead, interview).

The IEOF uses a **'decision tree' to determine what interventions are DIB-able**. The criteria on which the decision tree is based are identification of a specific target group and outcomes,identification of interventions that can achieve the outcome, consistency of achieving the outcomes, potential to achieve value for money and/

or potential of achieving outcomes if payment is conditional to the achievement of outcomes. (SF-IND-IEOF lead, interview). This is informed by the decision tree on DIBs prepared by Social Finance (Social Finance, 2016).

The 'decision tree' also helps to identify what kind of financing mechanism (an impact bond or others like social impact incentives or social success note) would work based on who is assuming the risk and who is paying for outcomes. It also provides a pathway for those who do not meet the criteria to explore alternatives (SF-IND-IEOF lead, interview).

Landscape Analysis

A compilation of the active organizations based on secondary research

Interviews with key donors, impact investors and philanthropists to map the level of endorsement and financial support for a given SP

Screening the list with a host of experts from key sector experts

→

Due Diligence Step 1

Service Provider Assessment on:
- Legal standing and governance
- Organizational finances
- Track record
- Ability to deliver impact
- Program details
- Risk management
- Partner relations

→

Due Diligence Step 2

Data evaluation to assess the feasibility of scaling-up and efficacy of delivery

In-depth assessment matrix includes:
- Organization's financial absorptive capacity
- Resource capacity to train and expand
- The ability to credibly innovate within their programming
- The ability to align with state education goals

Figure 5: Process of due diligence. Adapted with permission from Social Finance India, India Education Outcome Fund, GSG. (2019). India Education Outcomes Fund Prospectus 2019 (p. 63)

Securing investment and pricing outcomes

At the initial stage, SF-IND deliberated on how risk capital could be mobilized. The options being considered were as follows: first, SF-IND directly undertakes setting up of the Fund which will do the risk investing portion; second, SF-IND approaches potential individual risk investors on a case-by-case basis; and third, SF-IND does not get involved in this and gets another entity to handle the risk investments. The SF-IND selected the third option of working with an entity with an experience of fundraising and fund deployment in the education sector. They chose to work with Kaizen Private Equity, which already had two Education Sector Funds and was setting up another debt impact fund[1] focused on education. Kaizen expressed their desire to commit a certain proportion of the Kaizen Edu Finance Fund (KEF) raised to IEOF constructs as the risk investors. The KEF is a blended financial instrument which takes commercial capital and impact capital into the fund and is currently used for giving loans to affordable private schools. Philanthropic agencies are also partnering with Kaizen and funding performance-linked rewards in schools.

The SF-IND kept this engagement with Kaizen Private Equity on the risk side as 'non-exclusive', which means that on a case by case basis, if SF-IND found other investors that were excited about some opportunities, SF-IND would reserve the option of working with the other investors (SF-IND-IEOF lead, interview). From the perspective of Kaizen, the IEOF is a subset of the Edu Finance Fund which is a 150 million dollar fund with a 50 million green shoe option.[2] The target is to have the funds ready in 2020 so that whenever IEOF puts forth a construct that requires investment, Kaizen is ready with funds (Kaizen Private Equity partner, interview). According to the respondents from Kaizen and SFI-IND, currently, the risk investors are more likely to be foundations, philanthropies that do not mind taking the risks that they would have taken in any case, and would be happy if their funds get stretched further. The risk investors can, however, also be private capital interested in both social as well as financial returns. As the respondent from Kaizen pointed out, the commercial investors are not interested in dealing with the government but are more likely to invest in an instrument of the IEOF where the outcome payer is still a private entity and hence, there is an assurance of getting safe returns (Kaizen Private Equity partner, interview).

Currently, the regulations do not allow Corporate Social Responsibility funds to be invested in risk funds and they are more likely to come as outcome payers than as risk investors because they are required to spend money within the financial year and receiving returns would amount to not having spent the money at all. It should also be noted that by clubbing the process of raising risk capital with the KEF, the IEOF has attempted to keep the cost of raising risk capital low. Otherwise, if the IEOF were to do it on their own, the cost of raising risk capital would have been disproportionate to the amount raised for funding education interventions (Kaizen Private Equity partner, interview). However, investors are interested in seeing a definite pipeline of projects since they do not want their capital to sit idle.

In addition to securing investments, another key part of the process of establishing the outcome fund structure and building the marketplace is determining how outcomes will get priced. The pricing of outcomes requires data about the outcomes and reliable evidence on what it takes to produce those outcomes, which is currently lacking. Therefore, the IEOF sees the process of pricing outcomes happening in two waves as depicted in Figure 6. The first wave is intended to build outcome investment ecosystem and the second wave will launch standardised outcome rate cards. In Wave 1, existing proven programs will be facilitated to scale using impact bonds, will get evaluated and set a benchmark for success that will help determine the price per outcome. In Wave 2, the IEOF will operate a more developed fund, putting greater emphasis on the competitive cost of an outcome, wherein service providers will bid on specific outcomes through a rate card approach (Social Finance India et al., 2019, p. 21).

Wave 1: Building the outcome investment ecosystem →

- Pooled Impact Bonds
- Individual Impact Bonds

Wave 2: Launch standardised outcome rate cards

- Large scale Impact Bonds
- State government engagement

Figure 6: Building the market for impact bonds at scale. Adapted with permission from Social Finance India, India Education Outcomes Fund, GSG. (2019). India Education Outcomes Fund Prospectus 2019 (p.68)

Developing a rate card requires outcomes to be priced in a way that they are valid and fair and where there are several challenges involved (see Figure 7). The first round of impact bonds would help address the current gaps in data and would also help in establishing parameters for reasonable and fair pricing. This would factor in differences in the cost and efficacies of programs delivered across geographies and the varying complexities imposed. Determining risks and pricing them is another challenge and this includes factors in the external environment that can affect the implementation of programs viz. political scenario, changes in policy and agenda of the government, natural conditions and so on. In addition, the prevailing practices and mindset in the development sector focus on costing the inputs rendered rather than the outcomes that will be produced. This requires a paradigm shift in the way that makes stakeholders view the costs of producing outcomes.

The IEOF approach to pricing outcomes involves ensuring that the service providers are rewarded fairly and sustainably so that the costs, risks, and uncertainty in pricing are factored in. The thumb rule in this regard is that wherever the targeted results have been achieved, "risk of over-paying will be favored over the risk of underpaying" (Social Finance India et al., 2019, p. 79). The IEOF plans to create incentives for improving program efficiency and securing success. Over time, this will also help improve value for money by creating competition to improve program delivery and achieve scale.

To summarize, the IEOF approach towards pricing outcomes is based on two key concepts that are central to the IEOF fund design approach (Social Finance India et al., 2019, p. 53). They are:

1. **Rate card for outcomes:** After the IEOF administers multiple impact bonds, it would have adequate experience, evidence and data to be able to develop a standardised pricing mechanism in the form of a "rate card" which will specify a standard "price per outcome". This will help to reduce the costs of determining what the outcomes would cost every single time procurement is instituted.

2. **Market for outcomes:** once the pricing of outcomes is standardized and there is transparency across the service providers, risk investors and most importantly the outcome payer which could be the government, it would be easier to bid for outcomes and to raise capital.

Challenges in Pricing Outcomes

- There is a lack of data on how to price an outcome
- Existing programs spend very differently to one another
- Risks are often difficult to price accurately
- There needs to be a mindset shift from 'input' to 'outcome'
- Systemic improvements will need due focus

Pricing IEOF Outcomes Fairly

- Reward providers fairly and sustainably
- Intrinsic delivery costs & risks associated
- Risk of over-paying is favored over the risk of underpaying
- Create incentives for continuous program improvement and innovation
- Providers and investors who improve cost efficiency or success rates should be rewarded
- Drive improvements in value for money (VFM) over time
- Create price competition between providers
- Rewarding better program execution and greater volume

Figure 7: Pricing Outcomes: Challenges and IEOF Strategy. Adapted with permission from Social Finance India et al. (2019) (p. 79-80)

However, there is a concern that the cost calculated for producing a particular outcome may not take into account the groundwork put in by the service provider in terms of reaching out to government officials, community mobilization, rapport-building, and so on. These efforts that lay the ground and create conditions for success may not be calculated when pricing outcomes (service provider, interview). As a result, the cost of producing an outcome may be more than what is indicated on a rate card.

Another key component of setting up the ecosystem is defining the payment metrics which are aligned with the objectives of the program and helps to establish the payment mechanism for the achievement of outcomes. The SF-IND does not want the outcomes fund to compete with commercial investment sector for the risk investors with the expectation of 15-20% returns. According to the IEOF Lead, the objective is to have the returns more muted and aligned with social returns and to keep the costs of contracting, legal fees, performance management and program assessments less than 10-15%. This will ensure that the structure itself does not become very expensive. This also builds on the lessons learned from the Educate Girls DIB in Rajasthan which was recognized as being "expensive relative to the cost of the program" and which acknowledged "opportunities to streamline" the costs (IDInsight, 2018, p. 11). One of the recommendations from the process evaluation of Educate Girls DIB was that in order "to reduce transaction costs, future DIBs should look to replicate common frameworks and leverage contract templates" given that the "transaction and administrative costs and the time and effort commitments made during DIB design and implementation are viewed to be disproportionately high" (UBS Optimus Foundation, 2018, p. 19). The IOEF is, therefore, trying to reduce the time it takes to structure the impact bonds to 4-5 months which is very ambitious compared to the time taken to structure impact bonds in other contexts. These measures will bring down the costs and thereby improve returns on investments for the investors.

Specifically, in terms of payments to investors on the achievement of outcomes, selection of payment metrics is an important component of the structure that requires the alignment of all stakeholders. The guiding principles being used by the IEOF for determining what results would qualify for payments to the investors getting triggered are shown in Figure 8. The guiding principles seek to address concerns with regards to the clarity and ownership of the metrics, balancing measurement of outcomes with a few outputs, rewarding gains based on improvement with an equity angle, using standardized metrics for comparability and striving to measure outcomes that go beyond the metrics of literacy and numeracy.

Financial Mechanisms

Structuring an appropriate mechanism that responds to the current requirements and motivations of different stakeholders within the regulatory mandates has been an interesting, yet a challenging piece of the entire process. At present, one of the key mechanisms that the IEOF intends to put in place for channeling the investments is the mechanism of **pooled DIBs**. This also allows the IEOF to align its products with the maturity and readiness of the education sector. The absorptive capacity of the service providers currently poses a challenge. In the education sector in India, there are not many service providers who can take in significant amounts of money and utilize it to deliver their programs. Thus, the pooled DIB, wherein multiple service

Guiding Principles in the selection of payment metrics	
Use a simple basket of metrics to drive the right behaviors	• Simple and understood by providers and investors • Needs to incentivize a broad range of objectives
Majority of payment for outcome metrics, with some for outputs	• Transfer risks and incentives to providers and investors • Output metrics will be minimum • Inputs, if required, will be outside the main contractual framework
Reward all learning gains, using a 'distance travelled' approach	• Payment would be a direct function of total improvement attributable to the intervention • Will also have additional equity incentive • Binary and threshold approaches will not be used
Use comparable and standardized metrics where possible	• For example, Learning Adjusted Years of Schooling (LAYS), developed by the World Bank is a metric that could be used
Measure (and pay for) a broad range of what matters in a child's development	• Capture breadth of learning beyond academic skills • Research would be done on developing suitable metrics to measure the socio-emotional skills, IT skills, citizenship skills, and other 21st century skills.

Figure 8: Guiding Principles in the selection of payment metrics . Based on Social Finance India, India Education Outcome Fund, GSG. (2019). India Education Outcomes Fund Prospectus 2019 (p 80-81) with permission.

Video 2: Need for Capacity Building of Education Service Providers. Satyajit Salian, Head of Education, Tata Trust

providers working on the same issue are brought together make up a reasonable size, is a mechanism that IEOF has designed to address this challenge of low absorptive capacity among the service providers. For example, as IEOF Lead points out, many entities have the capacity to absorb INR 10 crores (USD 1.3 million) per year but may not have the capacity to take in INR 20 crores (USD 2.6 million) in a year. Hence, the pooled funds are expected to be a specific size of around INR 100 crores (USD 13 million) so that three service providers over three years can each utilize around INR 10 crores (USD 1.3 million) per year.

Pooled funds would be created around service providers working in the same sub-area within the broader intervention thrust areas. For example, under the broader intervention area of early childhood education, if four service providers are working on the sub-area of teacher training, and if there are 5 CSR or foundations who are willing to give funds, then a pool can be created around them. Each pool is expected to be USD 10-15 million pool. This mechanism would allow IEOF to match the current levels of maturity of the sector and use a step-ladder kind of approach which allows the stakeholders to grow. The scale that is envisioned in the pooled structures would bring multiple service providers together to work in a manner that their complementarities are leveraged or the adjacencies of their interventions (either geographical or functional) are put to work together. However, creating pools and bringing entities together that share the goals and have complementarities is a challenge (SF-IND-IEOF lead, interview).

"Although the primary focus of IEOF is to establish the impact bond market and ecosystem within the education system in India, the fund may explore alternate pay-for-success models in the initial stages" (Social Finance India et al., 2019, p. 81). The illustrative structures of social impact incentives and social success notes being considered are shown in Figure 9.

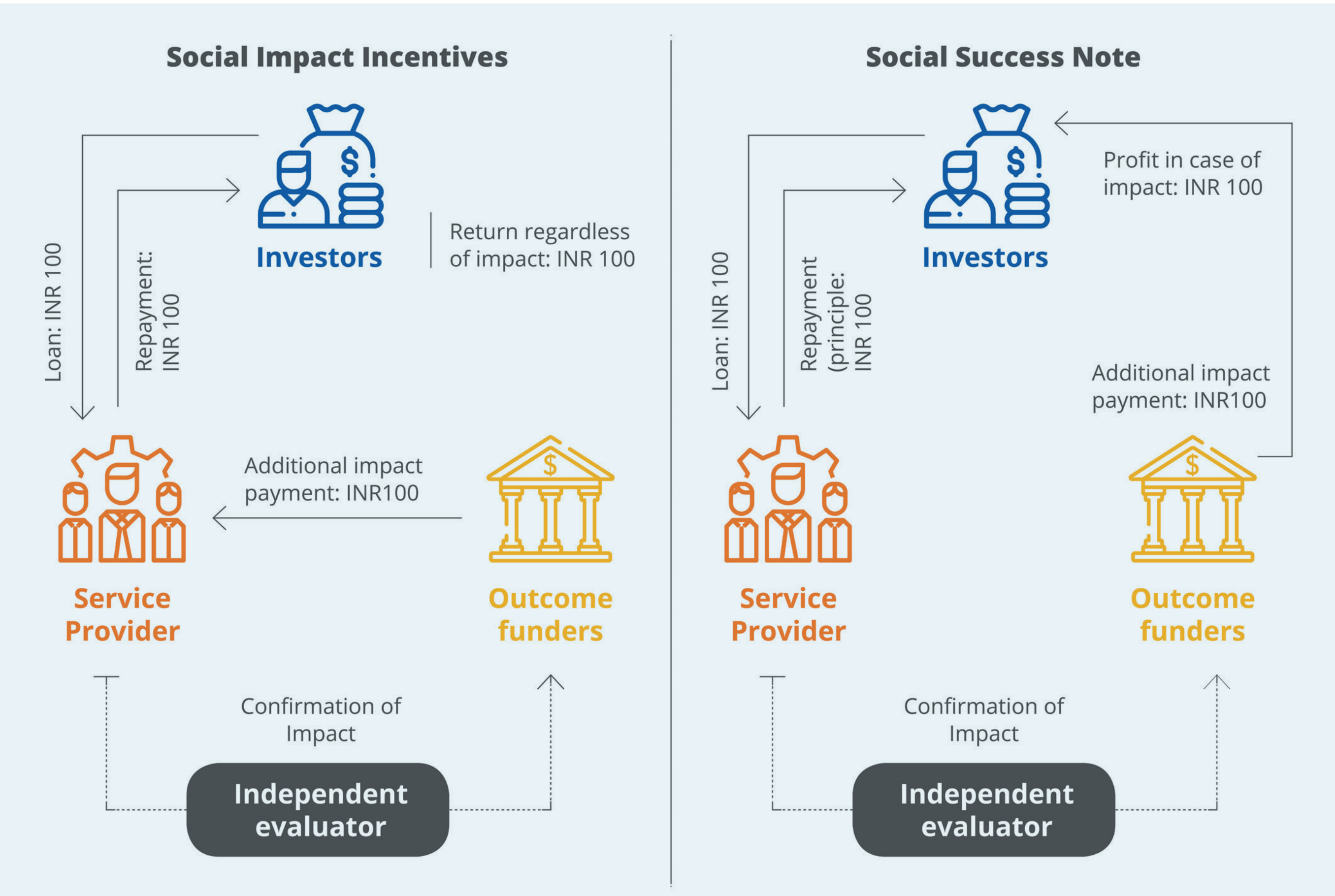

Figure 9: Social Impact Incentives and Social Success Notes. Reprinted with permission from Social Finance India, India Education Outcomes Fund, GSG. (2019). India Education Outcomes Fund Prospectus 2019 (p. 81)

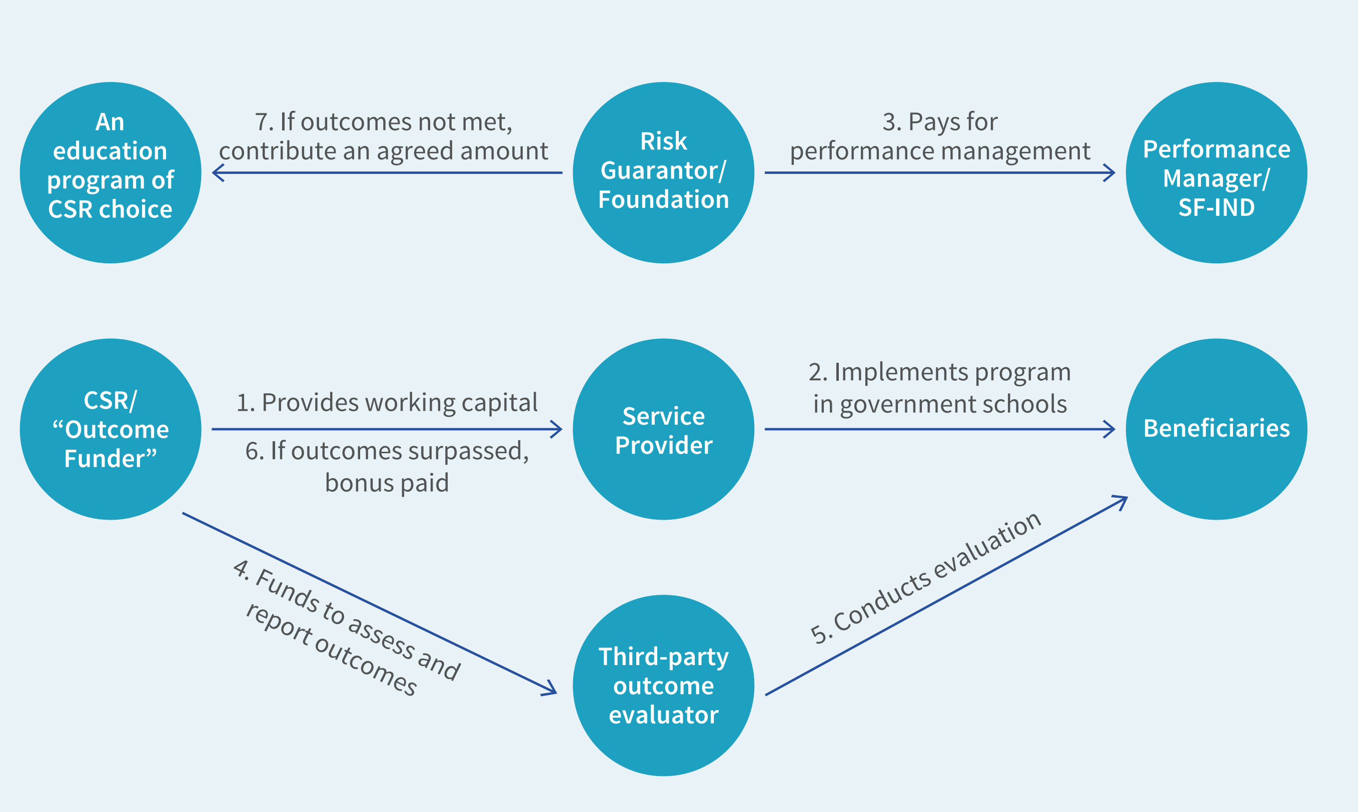

Figure 10: Unconventional structure of the Haryana DIB

In a **social impact incentive mechanism**, the investor will provide a loan to the service provider. After the independent evaluator assesses and confirms the achievement of the intended outcomes, the service provider would repay the loan to the investor and the outcome funders would provide an additional incentive or an impact payment to the service provider. Even in the event that the outcomes are not achieved, the service provider would return the loan amount to the investor. The mechanism of **social success note** is slightly different. The investor loans an amount to the service provider who returns the loan to the investors at the end of the program. The outcome funder would make an additional impact payment to the investors as a profit in case of impact. Whatever the mechanism considered, the IEOF plans to prioritize targeted outcomes and evaluate the risks assigned to risk investor and service providers on a case-by-case basis.

Given that the main focus of Wave 1 is to create an evidence base of what works and at what cost, the IEOF has launched a **DIB** in Haryana to improve early language literacy in government schools. It adopts a unique structure and leverages the CSR funding which is available on an annual basis and which legally cannot attract returns. The process of constructing the DIB has involved working within the confines of the legal framework governing the CSR funding, the requirements of the key stakeholders, while trying to achieve all the benefits which accrue from pay for success/ outcomes-based approaches. The structure of the DIB is therefore unconventional, as reflected in the steps involved (see Figure 10).

As mentioned earlier, the mandatory CSR in India generates funds annually that the IEOF can use for innovative financing and for making the existing funds go further. However, the CSR funds cannot be used for risk investment since Indian regulations prohibit corporates from receiving returns on their funding. However, the CSR can come as outcome funders. In the case of the Haryana DIB structure, the IEOF has inverted the paradigm. The ‘outcome funders,’ in this case the CSR of a private corporation, will give working capital upfront to a service provider, a nonprofit organization, to implement their early language literacy program in government schools. There is a risk guarantor, instead of a risk investor as seen in typical DIBs, who guarantees that the outcomes would be met. This risk guarantor is a grant-making foundation which has earlier funded the service provider and is reasonably confident that the intervention will produce the outcomes. In order to ensure that the risk of failure is further reduced, the risk guarantor will support SFI-IND to play the role of a performance manager. The CSR/ ‘outcome funder’ will support third-party evaluation. If the outcomes are surpassed, the CSR will give an unrestricted incentive bonus to the service provider. If the outcomes are not achieved, the risk guarantor would contribute an agreed amount to an education program suggested by the CSR/‘outcome funder’ because, as mentioned earlier, the CSR cannot receive any returns from the risk guarantor on the funds it has invested.

Data Dashboard

- Define key performance indicators
- Build data dashboards for collection and evaluation of data
- Provide data-driven insights on the Service Providers and fund performance

Field Visit

- Conduct regular field visits to closely monitor on-ground operations and solicit feedback from beneficiaries
- Provide strategic support to service providers

Reporting

- Periodic reporting to Steering
- Committee on performance updates
- Challenges in operations
- Proposed innovations and mid-course correction

Figure 11: Performance Management Component. Adapted with permission from Social Finance India, India Education Outcomes Fund, GSG. (2019). India Education Outcomes Fund Prospectus 2019 (p. 96).

According to the IEOF, a structure like this does not exist and it is first of its kind. A large part of the process of setting up the ecosystem is to actually come up with innovative ways of structuring the mechanisms that will have takers among the risk investors, outcome funders and service providers. There is no repository of different kinds of structures that can be floated, hence these are created in-house. Although purists may not call this structure an impact bond, it does everything that an impact bond does and shares characteristics of a traditional DIB, which is focused on outcomes, puts a certain penalty for underachievement of outcomes, and a certain incentive for overachievement after a third-party conducts an assessment. In this inverted structure, the risk of program failure is shifted to a risk guarantor, who has to pay back only if the outcomes are not achieved. There is also full focus on regular program/performance management to ensure that everybody is aligned towards delivering the outcomes (SF-IND-IEOF lead, interview). This may usher in a new way of designing DIBs where philanthropists or foundations provide initial seed grants to nonprofit organizations and social enterprises to experiment. Once they are confident about the ability of the programs to deliver outcomes or scale-up, they could come in as risk guarantors. This would release their funds for supporting other fledgling and innovative programs. The available CSR funds can be invested in programs that are focused on achieving outcomes and promises to bring efficiency and effectiveness in CSR funding. Thus, the structure is envisaged to see many programs innovated and scaled up wherein early-stage grantors becoming guarantors of programs, and new funds are brought in to pay for scaling, thereby having a multiplier effect. Most importantly, this structure also complies with the current regulatory framework because both the CSR/ 'outcome funder' and the risk guarantor are bodies that cannot receive returns on investments made.

Monitoring, Evaluation and Capacity Building

In order to build the capacity of service providers to deliver results and ensure that the program is progressing as intended, an important function that the IEOF will take on is that of **performance management**. This will entail building dashboards for monitoring key performance indicators, collecting data and generating data-driven insights into the performance of the program and the fund. The performance manager will also visit the field, review challenges, assess progress on the ground first-hand, and provide strategic support to the service provider wherever required (see Figure 11). Based on this, the performance manager will report to the Steering Committee constituted for the specific mechanism on the progress, and mid-course corrections suggested. The SF-IND will provide a performance management team consisting of a Senior staff/Director, Manager and an Analyst with a total capacity of 70-100% total full-time equivalent assigned to performance management. The role of the performance management is crucial because it is meant to reduce the risk of failure and facilitate achievement of outcomes. The specific responsibilities of the performance manager with regards to the stakeholders are outlined in Annex 2.

Evaluation is key to any pay-for-success mechanism given that it determines if the outcomes have been achieved and the basis for triggering payments to investors. However, in India, there is a dearth of agencies with the required expertise. Those with financial and evaluation expertise may not necessarily be competent to measure educational outcomes. Furthermore, some of the service providers may not be open to subjecting themselves to evaluation and their reluctance could stem from various reasons, ranging from the fact that they already get third-party assessments done or they do self-evaluation. The availability of data on whether the intervention has led to outcomes is a critical issue. For triggering payments based on outcomes, it is important that attribution is significant and clearly demonstrated. This can be a challenge because organizations may not want to subject themselves to rigorous Randomized Control Trials (RCTs) kind of evaluations (SF-IND-IEOF lead, interview).

The IEOF is partnering with leading third-party evaluators, selected through a bidding and empaneling process, to conduct a rigorous evaluation of outcomes. It also intends to focus on driving standardization so as to benefit from economies of scale. Consistent processes and data collection systems will be used across the whole IEOF portfolio of programs, as well as consistent metrics within each stage of the education life cycle, in order to meet the imperative for high quality, low-cost evaluations. Evaluation costs will be targeted at 5% of the contract value and get capped at 10% (SF-IND-IEOF lead, interview). The high costs associated with outcome testing is a matter of concern and although over the years this would come down, the possibility of using existing assessment measures like the National Achievement Survey or the School Education Quality Index to measure the outcomes of impact bonds is being explored (Tata Trust education lead, interview).

A significant part of developing a marketplace for innovative financing of education is to develop the **capacities of the service providers**. This becomes important because the nature of the financing mechanism is different from the traditional grant-giving mechanism that most service providers are familiar with. Moreover, the documentation, monitoring and evaluation requirements are far more robust than what service providers may have implemented while availing traditional grants. Therefore, the IEOF has been putting capacity building expenses upfront in the grant agreements and emphasizing it in the conversations with outcome payers. For example, in the case of the DIB in Haryana, in the scenario of overachievement of outcomes, there will be an incentive in the form of unrestricted funding by the CSR which is the outcome payer. This will incentivize over-achievement by the service provider. As an illustration, if it is a program costing INR 15 crores (USD 2 million) over 3 years, 20% (INR 3 crores or USD 400,000) could be given as unrestricted grants on the overachievement of outcomes, which is a significant amount for a lot of entities. In addition, the IEOF is also ensuring that funds for capacity building are factored in the program budget (SF-IND-IEOF lead, interview).

1. The impact investment providing debt funds to private educational enterprises.
2. A 'green shoe option' allows for over-allotment of shares than initially planned by the issuer in case the demand is higher than expected.

7

PERSPECTIVES ON ENGAGING KEY ACTORS

The process of identification and selection of stakeholders has been a key part of the initial work. The landscape analysis of service providers helped the IEOF to understand the ongoing work in the education sector, understanding their funding requirements, the programs that were on top of their pile, and also their capacity building requirements.

SF-IND is involved in reviewing the **service providers** and identifying the programs that have demonstrated certain success at some level and can be scaled up or a combination of 2-3 programs to deliver even a higher or bigger outcome (SF-IND-IEOF lead, interview). There is a firm belief that impact bonds are neither for all organizations nor for all the programs (SF-IND-IEOF lead interview, Tata Trusts education lead, interview). Service providers have been the most excited among all the stakeholders because if funds are committed for 3-4 years, it frees them to work towards their mission in a focused manner (SF-IND-IEOF lead interview, Tata Trusts education lead, interview). However, there is a reputational risk for the service provider in the sense that the effectiveness of its program is being tested and thus, failure to deliver outcomes may get seen unfavorably by the stakeholders as well as the government which is providing its schools to deliver the program (Tata Trusts education lead, interview).

When **Tata Trusts** came in with the initial support of setting up SF-IND in order to explore and create an impact investment ecosystem in India, it brought in decades of its experience, networks and understanding of the sector. For one of the biggest philanthropic bodies in India, this is only one small part of their overall grant portfolio but the engagement has changed the way it is looking at their other projects from an outcomes-focused lens. The transformation of the development sector in the form of greater accountability, focus on outcomes and flexibility to innovate are the main reasons why the Tata Trusts is supporting the SF-IND in setting up the IEOF. There are specific outcomes that the Tata Trusts expects from the SF-IND. The expectation is that SF-IND would create a reputation in the sector to raise funds from the private sector and eventually from the government. The SF-IND has targets on the ability to raise fund, their sustainability plan, and other parameters of building the ecosystem (Tata Trusts education lead, interview).

CSRs are an important part of the IEOF imagination. The IEOF has identified the states where they believe they should be initially focusing and it is predominantly linked to where the CSR monies are going right now. It is adopting more of top-down approach for leveraging CSR funds, which means that instead of starting with regions which require the most funding, the IEOF is identifying regions where the money is deployed now and converting that general CSR grant commitment into an outcomes-focused commitment (SF-IND-IEOF lead, interview). It is expected that this would snowball and create more interest in CSR investment in innovative financing for education.

In an impact bond structure, there is an interesting dynamic between the **risk investors** and the **outcome payers**. The risk investors would say 'we need to prove this as an instrument. So, let us not keep very stringent targets. Let success be shown'. But it is important for outcome payers to start pushing back saying 'no', if you showcase that every DIB is a success, then outcome payers will start becoming suspicious. While it is easier to mobilize risk investments, finding outcome payers is more challenging because it would entail payment of returns to investors which all entities may not be able to commit to. Currently, the outcome payers are either the foundations and philanthropies or the CSR funding. However, the ultimate goal of SF-IND is a scenario where the government comes in as an outcome payer. From the IEOF point of view, the target is to create a scenario where 5% of the government budget becomes outcomes-based over the next 2-3 years and raise it to 20% by 2030 (SF-IND-IEOF lead, interview). Although the SF-IND has started engaging with **the government**, the government is not involved but "is watching" (Tata Trusts education lead, interview). There are some officials who are interested and there are those who see this as making profit from the social sector and do not want to have investment bankers coming in. Some think that the presence of Tata Trusts brings a sense of comfort and increases credibility (Tata Trusts education lead, interview). There is a firm belief that until the government gets engaged, these structures will not achieve the potential and scale that they can and that they should. If it is left at only CSR and philanthropies, then the scale will remain very limited (SF-IND-IEOF lead, interview; Tata Trusts education lead, interview).

However, there are various challenges to the government involvement at present. Firstly, the government procurement is a very different process. Secondly, the government could also have concerns about the quality of service providers selected because it has its own process and criteria to work with nongovernmental organizations. Additionally, the government itself is involved as a service provider in education, given that education is a core sector. If the government has to be involved, it would entail reallocating the budgets in a particular manner and being open to a certain kind of scrutiny. Lastly, the government may have issues with the assessment methodologies being used because it is a commentary on its schools. This is likely to be more difficult in areas of early childhood education and primary education where the indicators and assessments are more complex (SF-IND-IEOF lead, interview).

Video 3: Lessons from designing the India Education Outcomes Fund. Satyajit Salian, Head of Education, Tata Trust

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CHALLENGES, CONCERNS AND LESSONS

During the first year of its work, the SF-IND and its stakeholders have been confronted with teething issues, have had some preliminary concerns and have confronted some challenges. This section summarizes some of them and presents them in no particular order of significance.

Organization-related

1. Given the unique blend of human resource requirements, getting the right kind of people to work on the IEOF as the work expands is a big challenge. People from finance sector need to be sensitized to the social sector and vice versa. There is a learning curve for those coming from the finance sector because the efficiencies they expect in the finance world do not exist in the social or the development sector. In fact, the mandate for the finance professionals is to bring in those efficiencies into the development sector. There can be a culture shock for those who are coming in from the finance industry. The entire articulation and language are different and it takes time for mutual learning to occur. There is a paucity of those with expertise in financial structuring, who can raise funds and market the concept (SF-IND-IEOF lead, interview; Tata Trusts education lead, interview).

2. Almost all the work that is done at the IEOF is new and no one has the experience of having done it before. There is no template or a repository from where structures can be borrowed. Therefore, an IEOF kind of a platform requires those who are capable of ideating and also those who are ready to work hands-on and get into the details (SF-IND-IEOF lead, interview).

3. There was an initial delay in starting the DIB due to initial teething troubles. There was an early inertia and aligning all the different stakeholders was a challenge. One of the lessons learned is that it is a continuous teaching process and a process of selling a new concept. It is also a top-down process and the key decision-makers or key decision influencers need to get excited and convinced first before working with other stakeholders (SF-IND-IEOF lead, interview).

4. There is also a realization that institutionally, there needs to be a greater emphasis on grit and in making sure that all the stakeholders persist and make it work till the end. One cannot let go of organizations saying that they are not performing so can drop out of the construct. One of the lessons is on how tightly contracts are written and what are the clauses that will ensure that all parties are at it till the end. It is necessary to not make it easy to drop things and see things through. Furthermore, it is crucial to make sure that the aspects of the finance world that allow one to get out of the losses quickly do not drive the social sector. This is important because the moment things are dropped half-way, the government is likely to become more reluctant to adopt such structures at scale. The government cannot afford to drop things and get out of the underperforming districts. Hence, contracts need to have tighter controls over bail-outs (Tata Trusts education lead, interview).

Instrument-related

1. The impact bond as an instrument is not an appropriate answer for all educational challenges. Many times, deep and significant work may be done by smaller or niche-focused NGOs because they have grassroots connections. Sometimes they are not capable of absorbing the kind of funding that an impact bond seeks to bring or have outcomes which can be measured without a huge expense being incurred. There is also a problem of measurability since not all outcomes are easily measurable and hence there is a concern if impact investing will fund and take up only those programs that aim to achieve measurable outcomes. That may leave out programs that are worth pursuing but which cannot be easily measured or quantified with the existing tools (Tata Trusts education lead, interview). This may lead to segmentation of the sector itself, where certain challenges are “DIB-able,” and certain organizations are “DIB-able” (Tata Trusts education lead, interview).

2. Between supporting experimentation and proven initiatives, there is a challenge to search for that sweet spot which balances the two. The question that needs to be assessed on a case-by-case basis is how much risk is acceptable to the parties involved. Currently, one of the concerns is that a proven model will start getting replicated in this form and the impact bonds will be used to scale up programs that have demonstrated proof of concept.

However, if the program is too risky then impact investor will not put funds and if it is too well known as an idea that works, the outcome funder will not see the need for a risk investor and may directly fund the organization. That dynamic is very important to understand and maintain (Tata Trusts education lead, interview). However, scaling up also involves risks and innovation and would require risk investments. One of the key challenges for the IEOF is to be seen as a neutral agency with the credibility to help determine that the outcomes that are being aimed at are at the right level (SF-IND-IEOF lead, interview).

3. There is a strong criticism that the idea of tapping into nonconventional funding is not occurring because it is the same philanthropic funding that is getting tapped and channelized into impact bonds. The key is to convince the government to fund the outcomes and tap into the private risk capital. The actual risk investors will be companies who have the dual bottom line- not just financial but also social bottom line. When the philanthropic organizations serve as risk investors in the impact bond structure, they offer a “nuanced charity” because they can keep reinvesting the funds to get multiple outcomes with the same funding. They are able to provide the up-front funding for programs that have some risk of not achieving all the promised outcomes and would therefore not receive funding from conventional funders. On the other hand, it saves government funds that may have been invested in programs that may not yield the promised outcomes. Some may not see this as a financial innovation or an instrument at all as it does not bring additional funding into the education sector. However, these innovations aim to improve efficiency and produce outcomes and therefore make the existing funding for education go further.

4. The legal, tax and regulatory norms in India impose a number of restrictions on philanthropies, foundations, and CSRs trying to engage with the new ecosystem. There are restrictions on who can invest, who can reap returns, how monies can be invested as well as restrictions on repatriation of returns to offshore investors. Since the marketplace is envisioned to unlock new capital, it has to straddle between the commercial imperatives and social imperatives and balance the regulatory norms applicable to the financial sector as well as to the charities. Since the IEOF is currently leveraging CSR funds for its Haryana DIB, the regulatory hurdles that impinge the designing process include corporations not being able to commit the exact amount that they can allocate in say Year 3, because they cannot predict what their profits would be in Year 3, or corporations not being able to invest and receive payouts (DIB risk guarantor, interview).

5. The cost of setting up the ecosystem and its claimed efficiencies are issues that deserve further study. The argument of efficiency, in contrast with bespoke transactions, will apply only when there is scale and a number of pooled funds or other mechanisms in operation that share the administrative and transaction costs, thereby creating efficiency. At present, the question of what constitutes scale and a scale large enough to result in efficiencies is ambiguous. In other words, there is a lack of clarity on what is the tipping point at which scale of the ecosystem starts showing gains of efficiency. Because until that tipping point is reached, the costs of setting up IEOF and its financial mechanisms, the process of raising capital, time and efforts spent on coordinating multiple stakeholders are likely to be more expensive than what it would have taken to design one-off bespoke deals. While achieving scale is imperative to bring efficiency gains, what must also be noted is that factors such as readiness of the sector, the pipeline of DIB-able programs, regulatory norms, and availability of investors and outcome payers create serious impediments to scaling.

6. Planning for the sustainability of the IEOF platform is also a challenge. Currently, the IEOF has received three years of funding from the Tata Trusts to create the marketplace. Once that is achieved, the SFI-IND and the IEOF would act as an intermediary in the ecosystem. Given that these are early years, the business model for funding the intermediary is not tested yet. If the costs of an intermediary are to be borne by all parties involved, it would make it an expensive structure. However, as SFI-IND Lead pointed out, experience shows that intermediaries generally take up performance management roles because it is a role that is integral to the mechanisms. The role of an intermediary is more defined in the private equity world and borrowed from there. However, it has not been tried in the social finance space in India.

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CONCLUSION

India, with its size, complexity and challenges of the education sector, requires additional resources in order to achieve Sustainable Development Goals. Innovative financing is still a new concept and the costs of structuring one-off Development Impact Bonds are well-documented.

The IEOF, as an innovative financing platform aimed at catalyzing outcome-focused funding structures at scale, makes an interesting case. It is focused on creating an ecosystem and has brought together an initial set of stakeholders that will work on high-impact interventions. Its target of raising USD 1billion of outcomes-focused activity by 2030 is ambitious and tapping new sources of funding will remain a challenge. Its ability to create pooled funds among organizations working on a common area, to design new structures that comply with regulatory standards, and to demonstrate an efficient and effective model for its own sustainability would be worth studying in future.

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APPENDIX

Annex 1: Broad framework for assessment of organizations

Broad area	Parameters
Organizational Details	Focus areas
Organizational Standing	Registrations, approvals, certifications from various regulatory and tax authorities and documentation on compliance.
Leadership	Structure, vision and mission, theory of change and alignment with the IEOF structure
Organizational Structure	Staff, partners, capacities, roles, workplans, diversity
Policies and Processes	Internal policies on human resources, decision-making, expenditures and accounting, assets, procurements, audits,
Operations	Information systems, government relations, ability to create impact, current programs, risk management, fundraising,
Monitoring and Evaluation	Practices, results, reporting methodology,
Scalability and Sustainability	Resource intensity, constraints to growth, donor base, cost comparability

Based on interview with SF-IND-IEOF lead.

Annex 2: Responsibilities of performance management towards stakeholders

Stakeholder	Responsibility
Risk investor & Outcome Funder	Centralized monitoring: Performance managers will supervise all stakeholder partnerships to drive continuous improvement, establish clear key performance indicators, conduct performance management reviews and report to the Steering Committee
Risk investor and service provider	Managing and responding to risk: Performance managers will help service delivery partners identify and address implementation risks and challenges while giving investors valuable insight into operational realities
Risk investor	Enabling investors to become leaders in innovative finance: Considering that impact bonds are a recent development, performance managers will support investors navigating their role in the program. Additionally, they can help investors build capability for future deals
Risk investor and service provider	Supporting adaptive management: Performance managers have to understand the factors influencing the results of the program and help implementation partners adjust it, if need be
Impact community	Generating lessons learned: Learnings generated from on-ground engagements must be captured and shared with the impact community to magnify the social return from the program
Analysis of the data to provide final result	Standard practices, uniform reporting templates are used to understand data and draw insights from it

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NORRAG Case Study, July 2020

NORRAG
Network for international policies and cooperation in education and training
Réseau sur les politiques et la coopération internationales en éducation et en formation

20, Rue Rothschild l P.O. Box 1672
1211 Geneva 1, Switzerland
+41 (0) 22 908 45 47
norrag@graduateinstitute.ch

@norrag

@norrag.network

www.norrag.org/ife