

# Social Impact Bonds & Education in Latin America

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## Social Impact Bonds & Education in Latin America

### Authors:<sup>1</sup>

**David Bloomgarden**, Lead Specialist at the Multilateral Investment Fund (MIF) of the Inter-American Development Bank Group

**Michael Eddy**, Partner, Instiglio

**Zachary Levey**, Associate at the Multilateral Investment Fund (MIF) of the Inter-American Development Bank Group

### Contributing Editor

**Adam Still**, Economic Development and Finance Specialist, GEMS Education Solutions

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<sup>1</sup> The views expressed in this paper are those of the authors and do not necessarily reflect the official position of the Multilateral Investment Fund or the Inter-American Development Bank Group.

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# INTRODUCTION

## ***Expanding access to quality education is vital for economic growth, inclusive development and poverty reduction in Latin America and the Caribbean (LAC).***

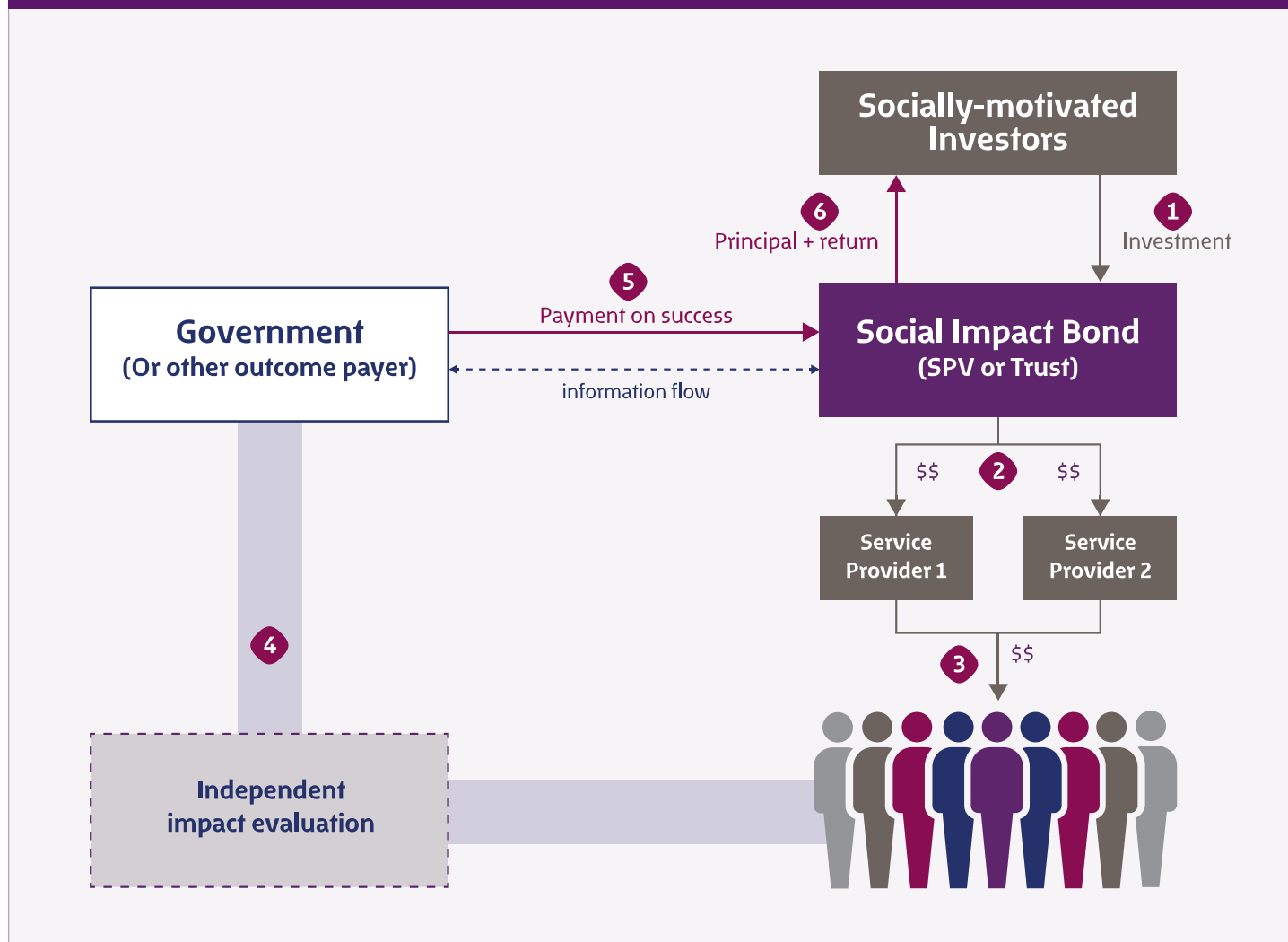
Despite substantial growth in education spending over the last decade, educational outcomes in the region lag behind other regions over the world – from years of school to quality of schooling. Social Impact Bonds may represent a new tool for LAC countries to improve education outcomes. The model is being trialled and expanded in the U.S., Australia, and the United Kingdom, and has the potential to become a transformational, social innovation for LAC. This paper seeks to generate initial discussion on the application of this innovative, social sector, financing model to the education sector in Latin America and the Caribbean. Additionally, it will investigate where, within the education field, a SIB arrangement could apply, and what the opportunities and challenges are, related to bringing Social Impact Bonds to the Latin America context.

# I. SOCIAL IMPACT BONDS: A MARKET-DRIVEN APPROACH TO IMPROVING EDUCATION OUTCOMES

Social Impact Bonds are a new way of driving social innovation to address age-old, social problems confronting today's societies. Social Impact Bonds involve a contract, in which the public sector seeks to buy improved social outcomes. Around this contract, socially-motivated investors – not governments or aid agencies – provide working capital to social sector service providers, allowing them to be able to scale up high-impact, social programmes.

The investors receive a variable return on their investment, based on the degree to which social outcomes improve, which is verified through a rigorous, impact evaluation. If outcomes fail to improve, investors do not recover their full investment, thereby transferring the performance risk of the programme away from government and taxpayers. Figure 1 below illustrates the dynamics of the SIB model.

Figure 1: Dynamics of the SIB Model



A number of actors participate in a Social Impact Bond and comprise what is often referred to as the Social Impact Bond Ecosystem.

- **Outcome payers** commit to paying for pre-determined outcomes (such as school enrolment or employment). If the outcomes are not achieved, the outcome payer may pay less, or not pay at all. In high-income countries, outcome payers have been municipal, state or central-level government agencies. In low and middle-income countries, outcome payers may be governments, but could also be aid agencies or a combination of the two. A Social Impact Bond, with a donor agency as the outcome payer, is sometimes referred to as a Development Impact Bond (DIB).<sup>2</sup>
- **Service providers** implement the programmes, ultimately delivering the social outcomes in the target populations defined by the SIB. SIBs may involve just one service provider, or a small group of service providers, who offer complementary services, as part of a single, support package. Service providers have traditionally been NGOs, but could also be private providers. Service providers can directly interact with investors or rely on intermediaries to help them raise capital. A common criticism for Social Impact Bonds is that the monetary incentives for service providers to succeed are weak, particularly when they are NGOs. While there are potential ways of increasing monetary incentives for service providers, mission-driven NGOs participating in SIBs are taking a major risk, but in a different way. Perhaps the greatest incentive is reputational risk of failure, as a SIB could put at risk their ability to raise money in the future. At the same time, SIBs provide new access to capital and multi-year funding, which could greatly reduce the heavy administrative burdens of being in a perpetual state of fund-raising.
- **Investors** provide the up-front capital to scale social services. For the first Social Impact Bonds, in the UK, the investors were predominately family foundations. However, as the market has developed, there have been more mainstream investors taking part, as well, such as Goldman Sachs.

- **Specialised intermediaries or advisors** facilitate the creation of the deal, bringing together the service providers, outcome payers and investors, to make the deal possible, and to advise on how the SIB should be structured. During the programme, intermediaries also often play the role of performance manager, helping to fully leverage the results-based, contracting model, by supporting organisations to make data-driven decisions, as well as in-course corrections to the programme model, as the programme evolves.<sup>3</sup>
- **An independent auditor or evaluator** determines how much social outcome has been achieved, which subsequently determines the disbursement of outcome payments. To avoid conflict of interest, this role must be independent of the other parties in the deal. The choice of auditor or evaluator, and ultimately, the evaluation methodology used to assess the outcomes of the intervention, is a critical design feature of a SIB.

Social Impact Bonds introduce several, key elements that are distinct from how social programmes are normally funded and implemented:

- **Innovation and Flexibility** – When investment is tied to outcomes, rather than activities, service providers gain greater flexibility to innovate and improve their programmes, resulting in outcomes that really matter. Donations and government contracts often short-change non-profits' internal operations and stifle their ability to experiment and improve their programmes by restricting funds to programme-specific activity.
- **Risk-transfer** – Governments and taxpayers can transfer the risks of programme performance to the private sector, and enhance the **value for money** of a given intervention, by clearly specifying the cost of the measurable outcomes, instead of the inputs, of any programme ex-ante. Governments and development agencies typically purchase social services by making up-front payments to service providers that are weakly tied to performance outcomes. In a SIB, these agencies can make their payments on condition of outcomes, channelling taxpayer money toward programmes that work.

<sup>2</sup> See, Social Finance UK and Center for Global Development. Investing in Social Outcomes: Development Impact Bonds. 2013. Available at: <http://www.cgdev.org/dib>

<sup>3</sup> For example, in the first SIB, in Peterborough, England a consortium of three service providers is delivering integrated services to a population of 3,000 male, short-term offenders. Social Finance, a SIB intermediary, oversees the performance of the programmes and decides if additional

services are needed or existing services need to be adapted. For example, after realising that a small group of ex-offenders had unaddressed mild mental health problems, a fourth service provider was added to deliver mental health services to reduce recidivism. See, Nicholls, A., and Tomkinson, E. Case Study: The Peterborough Pilot Social Impact Bond. Oxford, 2013: Saïd Business School, Oxford University.

Through the ability to transfer risk to the private sector, governments gain greater flexibility to invest in preventative solutions that address root causes of problems.

- **Rigour and evidence** – The social impacts and performance of many, Publicly funded programmes are not rigorously measured and assessed. This makes it challenging for governments to make informed, evidence-based choices about their investments and spending. Social Impact Bonds introduce and demand new levels of rigour into social programmes.
- **Partnership** – SIBs bring governments, private investors, private philanthropy and NGOs around the table to solve a specific problem. This type of partnership arrangement is unique to the SIB model. Beyond partnership and coordination between governments and non-governmental actors, SIBs also facilitate collaboration across government silos, as well as local and national authorities.
- **Accountability and Programmatic Continuity** – Social Impact Bonds provide a mechanism for greater transparency and accountability of governments and service providers. In addition, SIBs provide a mechanism for multi-year funding.

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## IDENTIFYING OPPORTUNITY AREAS FOR SOCIAL IMPACT BONDS

SIBs are not appropriate for every topic area. SIBs will be most successful when they are used in areas where they can generate the greatest value. The following criteria may be useful in determining whether a SIB is a good fit for financing a specific area within education:

- **Measurable results.** Programmes financed by a SIB should be able to produce measurable results within a limited time period. This will allow for careful monitoring throughout, and rigorous evaluation afterwards – thus, objectively determining the success of the programme. This may be a challenge within the education area, where many outcomes are difficult to quantify and may be realised beyond an investor’s time horizon.
- **Promising evidence-based programmes.** Evidence that providers have been previously successful at addressing the social problem, is critical to creating an investable proposition. Service providers should be experienced, have high capacity, and be able to scale their programmes.
- **Ability to attribute results.** Paying for results requires making them measurable. Depending upon the context, this may require constructing control groups comprised of participants who are not receiving the programme.<sup>4</sup> Some programmes may be more difficult to credibly attribute results, than others. For example, a mass-media campaign, that emphasises the value of education, would be difficult to finance through a Social Impact Bond.
- **High net benefits.** Due to the transaction costs involved, SIBs are best for investment in areas with the potential for high net benefits. This will be particularly true in situations where there is a gap in coverage (e.g. early childhood education); where current programmes are delivering poor performance; or where there is an opportunity for direct, cashable savings to the government.<sup>5</sup>

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<sup>4</sup> The most rigorous way to do this would be through a well-implemented randomised control trial, but depending on the context, other types of evaluation may be deemed credible.

<sup>5</sup> In high-income countries, SIBs have generally been focused in this third

area—where there are direct, cashable savings (for example, by reducing the re-incarceration of ex-convicts, or by reducing special education costs). In low and middle-income countries, where social safety nets are generally thinner, these cashable savings may be more elusive.

## II. SOCIAL IMPACT BONDS IN LATIN AMERICA

Latin America's social problems and development needs are changing. A decade of economic growth and good policies has helped cut poverty levels in half, and have contributed to a 25 percent increase in average, real incomes.<sup>6</sup> Yet, substantial, social and economic challenges remain for the region, and social needs are becoming increasingly diverse – in many places, also becoming more acute. Of the region's 600 million inhabitants, more than 80 million people still live in extreme poverty, and over 200 million people are vulnerable to falling back into poverty, living on just \$4 to \$10 per day.<sup>7</sup>

A growing concern for many governments in the region has been how to maximise the value for money in public spending. Each year, governments spend billions of dollars to address the social problems and development needs of the region in areas, such as education, poverty, health services and citizen security.<sup>8</sup> But funding available through public expenditures, development aid and private philanthropy covers only a fraction of the region's needs.<sup>9</sup>

Conventional funding mechanisms for social services are not designed for innovation and limit incentives for delivering results. Governments worldwide typically purchase services based on the quantity of services delivered, rather than the results they produce. In effect, money is disbursed, regardless of outcomes; and failed projects are treated as sunk costs, when and if results are properly measured. Generally speaking, rigorous evaluation of policy measures has played a minor role in Latin America, particularly with regards to measuring and assessing the social impacts of publically funded projects and programmes.

Many, non-governmental providers deliver proven solutions to address the myriad of social challenges confronting the region's poor and vulnerable populations; but often,

they have limited resources and means to scale up their programmes. Additionally, private capital and know-how remain largely on the side lines and are underutilised in the social sector. While interest in impact investing has substantially grown in recent years, there are still few asset types that provide investors with a means of linking their financial return to a social outcome. Beyond nascent, social sector applications of Public Private Partnership schemes, the private sector has not yet taken on the risk-transfer from governments for social interventions.

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### CONSIDERATIONS FOR SIBS IN LAC

Social Impact Bonds offer a new and transformative way for governments in Latin America and the Caribbean to a) invest in social innovation, b) road test new intervention models, c) expand prevention-oriented programmes that can generate savings, and d) incorporate market discipline into the social sector that improve the quality and effectiveness of services for poor and vulnerable populations. While Social Impact Bonds hold great promise for Latin America and the Caribbean, the social service financing model has not been implemented in the region. First-movers in Latin America, who are looking to test SIBs, may face a number of challenges.

#### Transferability

Social Impact Bonds are not plug-and-play, and this will be particularly relevant when transferring SIB intervention models, that may have worked the US and UK, to the Latin American context. Problems will likely have different, underlying causes. In addition, many countries in LAC will not have the same availability of robust and cost-effective data, which is critical to making evaluation of Social Impact

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<sup>6</sup> CEDLAS and the World Bank, 2013. "Socio-Economic Database for Latin America and the Caribbean." <http://sedlac.econo.unlp.edu.ar/eng/index.php>

<sup>7</sup> Nancy Birdsall, Nora Lustig, and Christian J. Meyer, 2013. "The Strugglers: The New Poor in Latin America?" CGD Working Paper 337. Washington, DC: Center for Global Development. <http://www.cgdev.org/content/publications/the-strugglers>

<sup>8</sup> Economic Commission for Latin America and the Caribbean (ECLAC), 2012. Social Panorama for Latin America, 2012. [http://www.cepal.org/publicaciones/xml/8/49398/2012-960-PSI\\_WEB.pdf](http://www.cepal.org/publicaciones/xml/8/49398/2012-960-PSI_WEB.pdf)

<sup>9</sup> For instance, the financing gap for universal pre-K coverage is an estimated US\$14 billion a year. And private philanthropy for social sector programmes, such as health care and education, only amounts to \$3.7 billion USD, for the region.



Bonds feasible and/or cost-effective. In addition, the Multilateral Investment Fund's (MIF) experiences in venture capital suggest that replicating financial structures across different countries can be very challenging, due to both minor and major differences in the legal (or accounting, or fiduciary, etc.) codes.

### **Legal and Regulatory Framework**

Regulatory barriers may exist, which prevent governments from contracting across multiple budget cycles, or contracting conditional upon outcomes. Fortunately, many Latin American countries have implemented legislation enabling Public Private Partnerships (PPPs), which, in many situations, may allow future payments based on certain conditions (e.g. the quality of a road). While PPPs have most typically been used for infrastructure, the same legislation may be relevant for a social service, as well. Another option, pursued by the State of Massachusetts, was to allocate funds, from the current budget year, into an independent Trust, with clear guidelines for payment. Should successful outcomes be reached, the Trust would pay out to the SIB. Should outcomes be reached, only partially or not at all, the Trust would specify an alternative use for the money. These, and other regulatory solutions to Social Impact Bonds, are likely to be jurisdiction specific.

### **Contract integrity**

Credible contract design will be critical to ensuring that the first Social Impact Bonds achieve their social purpose and are not used as an improper subsidy for the private sector, nor result in unintended consequences. If SIBs are to deliver on their promise of enhancing value for money, then one of the key factors will be deciding how to value outcomes which appropriately incentivise results, while not spending more than the government needs to. This process of valuing social outcomes (e.g. how much should the government pay for an "improved test score" or an "at-risk 20 year-old who is now employed"?) is non-trivial.<sup>10</sup> Furthermore, evidence from other results-based financing instruments suggests that poorly designed outcome metrics can result in manipulation of results, crowding out intrinsic motivation or unintended consequences.<sup>11</sup> Both outcome

valuation and contract design will require specialised skills and potentially new ways of doing business for governments, as well as other stakeholders. Failure to design good-quality SIBs – particularly during the first projects – could lead to the collapse of the entire market.

### **Data availability and evidence**

A lack of data availability will likely make Social Impact Bonds both riskier and costlier in Latin America. Social Impact Bonds will be riskier because there are few, evidence-based case studies of rigorously evaluated programme models; and service providers may need greater capacity-building to become 'investment ready'. Social Impact Bonds may be more costly, because of the limited nature and varying quality of existing educational statistics in many countries. Rather than using existing administrative data, SIBs may, therefore, require independent, SIB-specific monitoring and evaluation systems

### **Political economy of the private sector**

The political economy of education may make Social Impact Bonds difficult to implement in areas that are traditionally provided by the public sector. For example, in primary and secondary education the gains from implementing a Social Impact Bond are diffuse.<sup>12</sup> Losses may be perceived as concentrated and falling on identifiable and easy-to-mobilise populations, such as public sector unions. Social Impact Bonds may face fewer barriers when they are used to expand funding in an area where there is currently a significant funding gap (e.g. early childhood education), or in areas where the government already contracts with private providers (e.g. job training in some countries).

### **Local capacity**

In Latin America, there are important gaps in the capacities of the various members in the SIB ecosystem. NGOs and service providers do not often have the ability to be able to engage in the rigorous, data-driven, performance management that SIBs require; nor to be able to meet the accountability that private investors require. Private social investment, philanthropic or commercial, is far less developed in LAC than in the UK or US. In the US, for

<sup>10</sup> For more information on how to value outcomes, see, Investing in Social Outcomes: Development Impact Bonds. The Center for Global Development & Social Finance. The Report of the Development Impact Bond Working Group. (2013). Pg. 77-78

<sup>11</sup> For example, a recent evaluation of a performance-based aid programme which rewarded villages for performance on education and health targets, found that the incentives had a significant impact on

health, but no impact on educational performance. See, Olken, Benjamin A., Junko Onishi, and Susan Wong. Should Aid Reward Performance? Evidence from a field experiment on health and education in Indonesia. No. w17892. National Bureau of Economic Research, 2012.

<sup>12</sup> Broadly speaking, benefits accrue to taxpayers who gain from more accountable use of public money, and to students and their families, who may receive better-quality services.

example, multiple private foundations have helped support much of the early work and research of SIBs. Impact evaluation is also a relatively new concept in the region, where there are a limited number of qualified professionals who may be able to carry out the work required. Finally, in the US and UK, specialised, intermediary organisations, such as Social Finance and Third Sector Capital, have played important roles in advancing the market. In Latin America, the only specialised, Social Impact Bond organisation is Instiglio, based out of Colombia.

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## LESSONS LEARNED FROM PUBLIC PRIVATE PARTNERSHIPS IN LAC

The PPP model, pioneered in the UK and other European countries, has taken root in LAC countries, as the region increasingly turns to Public Private Partnerships to meet the growing need for infrastructure investment. As the traditional PPP model has begun to expand from traditional sectors, such as transport and energy, to new areas in health and education, SIBs can be seen as the next generation of PPPs, evolving from infrastructure services to social services. SIBs share much in common with the PPP model, in terms of their structure and function. Both PPPs and SIBs have outcome payers – normally the government – for which payments are based on the achievement of pre-agreed results. PPPs are based on a partnership embedded in a long-term, contractual relationship among the key players – the government, investors, the intermediary (referred to as the SPV or Special Purpose Vehicle) and the service providers (NGOs or private firms) that are sub-contracted by the SPV to deliver the service and infrastructure.

The Multilateral Investment Fund (MIF) of the Inter-American Development Bank has documented lessons learned from the establishment of PPP programmes, in Latin America and the Caribbean, which are relevant to the development of a SIBs market. In terms of transferability of the PPP model, from Europe to LAC, PPPs are not a one-size-fits-all model. They are based on a sound diagnosis of the local, social and economic environment, local laws and regulations, and the political economy of sectors that can deliver the greatest value for money. Value-for-money should take into account the project's cost benefit and evaluate whether the PPP delivers greater benefit to the public sector, than if the public sector had completed the project using traditional public procurement. PPPs are not formed simply because a government cannot afford a project. The value drivers

behind a PPP are: greater efficiency, effectiveness, innovation, and risk transfer to the private sector.

PPPs are most likely to succeed where the government demonstrates support for PPPs at the highest levels. Projects that are undertaken as a PPP should be identified as a priority of the government, and fit the national development plan for the sector. In addition, there should be an enabling policy framework, or law, that sets out the scope and requirements for PPP investments, as well as dispute resolution and procurement. PPP laws and policies typically include establishment of a dedicated PPP unit, as well as clearly defined roles and responsibilities that separate the functions of promotion, preparation, approval, funding and oversight amongst appropriate, government agencies. In particular, the approval authority should be separate from the agency that procures the PPP. The government needs legal authority to commit funds to the private sector that spans several budget cycles, and where payments are dependent on achievement of results. The private sector needs assurances that government will honour financial obligations to private providers. Colombia, for example, has established a contingency fund for PPPs, so that the private sector will feel more confident that the government will honour its contractual obligations.

Sound governance and transparency are crucial for, not only the quality of a PPP programme, but to also maintain public support. In the Brazilian state of Minas Gerais, for example, the agreed-upon results frameworks of PPP projects are made public, and progress toward their achievement is monitored by the state PPP agency. PPPs are often met with opposition because they are confused with privatisation. For the long-term success of a PPP programme communication between the authorities, the private sector and civil society is critical. In addition to transparency, PPPs should bid on a competitive basis with clear rules that are consistent and known to all bidders.

Governments should also make use of expert advisors who have broad PPP experience. They should also take advantage of donor assistance to ensure good contract design, proper metrics are set, and that third-party dispute resolution and risk transfer are offered. While outside advisors can inform good project design, the government needs to be responsible for on-going contract management to ensure that payments are only made based on independent evaluation of the results. When this function is not already in place, technical assistance from donors should be provided, in order to build the capacity within the government to manage the PPP contract and ensure

compliance with contract metrics and other requirements. Training and sensitisation should go beyond the PPP unit to include all relevant government and private actors in the PPP ecosystem. This will help ensure continuity of the PPP programme after change of government and when MIF funding has ended. Finally, in terms of implementation of PPP programmes, it is considered essential that a pilot project is launched to demonstrate the model, the success of which will be emblematic and impact on the ability to develop a market for PPPs.

Access to local, financial facilities is necessary for local investors to take part in the PPP market. In sub-national governments and smaller economies, banks and pension funds may not be able to support PPP projects. In this case, government financing, or changes in financial regulations to allow pension funds to invest in infrastructure assets, can be helpful. In addition, donor agencies can provide guarantees of payment, in order to leverage private sector investments. While large economies, such as Brazil and Mexico, provide such financial facilities to support PPPs, smaller economies face greater challenges, due to small economic size and fiscal constraints.

As can be learned from experiences at the MIF in providing technical assistance to PPP programs, a SIB programme should include project design, based on risk transfer and value for money, an appropriate regulatory environment, high-level political support, training and communications, and the launching of a pilot project to demonstrate effect and to generate local know-how in the design and implementation of the SIB model.

## III. SOCIAL IMPACT BONDS & EDUCATION

As policy makers, non-profits and social enterprises hope to increase their impact and attract new funding to the field, SIBs can provide advantages where other traditional funding mechanisms fall short. These payment-for-results mechanisms have the potential to enhance value-for-money, attract new funding to finance early intervention, accelerate the adoption of high-impact programmes and incentivise adaptable and differentiated programme delivery at scale.

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### GLOBAL EXAMPLES OF SOCIAL IMPACT BONDS IN EDUCATION

Social Impact Bonds are a relatively new mechanism. While there are over forty Social Impact Bonds now in design or implementation around the world, none have reached completion at the time of writing this white paper. In education, there are thirteen SIBs underway around the world related to vocational education and early childhood education.

#### Workforce development and vocational education

Twelve of the thirteen education SIBs in implementation are in vocational education. In the UK, the Department of Work and Pensions (DWP) has made up to £30 million available to pay for improved employment outcomes for unemployed young people. This led to ten Social Impact Bonds supporting more than 5,000 young people and achieving over 1,500 successful outcomes. Payment metrics for their programmes include outcomes such as the successful completion of 'English as a second language' courses and entry into formal employment.<sup>13</sup>

Two other vocational education SIBs, in the US, were made possible by the US Department of Labor's Payment-for-Success funds, which allocates funding for state-level pay for successful initiatives. Grants were

delivered in the states of Massachusetts and New York to increase employment and reduce recidivism amongst formerly incarcerated individuals.<sup>14</sup>

For example, in Massachusetts, Goldman Sachs and philanthropic investors are providing financing to allow Roca, a non-profit that works in job readiness and life skills training, to expand its evidence based programme to work with up to 1,329 men, aged 17-23, when they leave the juvenile justice system. The Massachusetts Office of Labor and Workforce Development will pay for successful employment outcomes, job preparedness and averted recidivism, as measured by a randomised control trial, conducted by a third party. The majority of the payments will be based on averted recidivism, with the state of Massachusetts paying up to \$27 million if Roca can reduce the number of days of incarceration of this population by 70%. In addition, \$789 is paid in each quarter for each participant who remains in the programme and \$750 for each quarter a participant is employed, compared to a control group.<sup>15</sup> The state of Massachusetts stands to save up to \$45 million by preventing these youth from returning to jail.

#### Early Childhood Education

In 2013, in the United States, the United Way of Salt Lake City, Utah announced the creation of the country's first Social Impact Bond designed to expand access to early childhood education. The investment deal, in which Goldman Sachs and J.B. Pritzker have committed up to \$7 million dollars in investment, could benefit up to 3,700 at-risk children in the state, over multiple years. The intervention is a pre-school programme delivered to 3 and 4-year-olds, who have been pre-identified as high-risk, according to a baseline test. By improving primary school preparedness, the programme aims to reduce downstream utilisation of special education, saving the state and local government millions of dollars. This SIB

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<sup>13</sup> Department for Work and Pensions Innovation Fund. Office of Social Impact Bonds. 2013. Accessed online at [http://data.gov.uk/sib\\_knowledge\\_box/department-work-and-pensions-innovation-fund..](http://data.gov.uk/sib_knowledge_box/department-work-and-pensions-innovation-fund..)

<sup>14</sup> Workforce Innovation Fund website. Accessed online at [http://innovation.workforce3one.org/grantees\\_main](http://innovation.workforce3one.org/grantees_main).

<sup>15</sup> "Fact Sheet: The Massachusetts Juvenile Justice Pay for Success Initiative." 29 Jan 2014. Available at: <http://www.thirdsectorcap.org/>

<wp-content/uploads/2014/01/MA-JJ-PFS-Fact-Sheet.pdf> ; PFS Grantee Summary. Massachusetts Executive Office for Administration and Finance and Executive Office of Workforce Development. Project: The Massachusetts Juvenile Employment and Recidivism Initiative. [http://innovation.workforce3one.org/resources\\_uploads/one-pagers/WIF\\_PFS\\_Grantee\\_Summary\\_MAEOLWD\\_revisions\\_final.pdf](http://innovation.workforce3one.org/resources_uploads/one-pagers/WIF_PFS_Grantee_Summary_MAEOLWD_revisions_final.pdf).

serves to address a cost saving: reducing the attendance numbers, and therefore cost, of elementary school special education programmes. Each year that a high-risk student avoids special education programming during elementary school (through grade 6), there will be payment.<sup>16</sup>

### **Other results-based financing instruments in education**

The UK Department for International Development (DFID) is piloting its first, results-based aid contract with the government of Ethiopia (also called Cash on Delivery). Up to £30 million will be awarded to the Ethiopian government, based on primary school completion and learning (measured as sitting for, and passing, a standardised test). Independent third-party evaluators contracted by DFID will validate outcomes and check whether there was any manipulation of results. The contract has a tariffed structure, which rewards Ethiopia more, for results achieved in emerging regions, as well as with girls.<sup>17</sup>

This contract differs from a Social Impact Bond in that it does not have private investment and it is between an international donor and a government, rather than a government and a service provider (as with a SIB). Nevertheless, many of the design considerations – such as independent verification of outcomes, payment metrics and outcome valuation – can be approached in similar ways.

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## **SOCIAL IMPACT BONDS AND EDUCATION IN LAC**

Each year, approximately \$257 billion is invested in education in Latin American and Caribbean countries.<sup>18</sup> This investment, alongside the Millennium Development Goals, has led to the dramatic expansion of coverage to near universal rates for primary education. Despite the progress, expanded coverage has failed to translate into significant learning gains or necessarily a more prepared workforce. More than 50 million LAC youth are unemployed or underemployed, and LAC countries still trail behind their Asian or OECD colleagues in student performance, even after controlling for GDP.<sup>19</sup>

The current way of financing education does not do enough to reward results, adapt (particularly vocational) education to local labour-market needs or fill the gaps needed to expand coverage in areas such as early childhood, while maintaining quality. New approaches are urgently needed that bring together the best of the public and private sectors to produce a more educated and prosperous future for Latin America's children.

### **Early Childhood Education**

Reducing inequality of social outcomes means levelling the access playing field, in order to boost equality of opportunity, at birth. Children from poor families in the region enter primary school disproportionately less prepared for learning. The first five years of a person's lifetime are the most crucial, in terms of brain development and the creation of cognitive and emotional skills. These children achieve less in school, repeat more, and eventually drop out at an early age. As adults, they earn lower wages and have higher rates of delinquency and crime, causing further economic and social burdens on governments and societies.

There is now strong evidence that what happens in children's first five years of life has an impact on their health, educational success and labour-market outcomes, in the future. The Heckman Curve (figure 2), proposed by the Nobel Prize-Winning economist, James Heckman, posits that investments targeted to the first years of a child's life having the greatest returns, per dollar invested. This is supported by extensive empirical evidence in the US. Promising randomised evaluations from Colombia, Jamaica and other LAC countries suggest that similar results hold for Latin America.

Latin America faces major gaps in coverage and quality in early childhood education. Despite proactive efforts in the last decade, the IDB estimates that closing the gap in access, to early childhood education, will cost an estimated \$14 billion, in LAC alone.<sup>20</sup> The net preschool enrolment rate grew to 65 % in 2008, but shows dramatic differences, by country, with less than

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<sup>18</sup> "Pay for Success and Social Impact Bonds". Community Impact Strategies Ltd. Accessed online at <http://communityimpactstrategies.com/social-impact-bonds-and-pay-for-success/>.

<sup>19</sup> See, DFID. "Business Case." Pilot Project of Results Based Aid in the Education Sector in Ethiopia. Available at: <http://devtracker.dfid.gov.uk/projects/GB-1-202989/documents/>

<sup>20</sup> World Development Indicators. Accessed: 4 Feb 2013

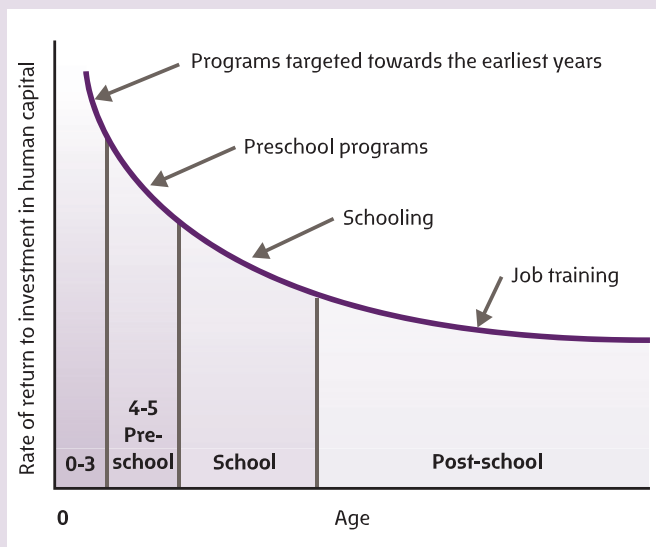
<sup>21</sup> Verdisco, Aimee. "Early Childhood Development: The Need for Regional Indicators." Education. Inter-American Development Bank, 26 Jan. 2010. Web. 28 Jan. 2014.

<sup>20</sup> Verdisco, Aimee. "Early Childhood Development: The Need for Regional Indicators." Education. Inter-American Development Bank, 26 Jan. 2010. Web. 28 Jan. 2014.

**Figure 2: The Heckman Curve**

### Returns to a Unit Dollar Invested

(a) Return to a unit dollar invested at different ages from the perspective of the beginning of life, assuming one dollar initially invested at each age



Source: James Heckman, “The Case for Investing in Disadvantaged Young Children” Big Ideas for Children First Focus, 2008.

30 % of students attending preschool in Guatemala, Honduras, Paraguay and the Dominican Republic.<sup>21</sup> Cuba and Peru are the only Latin American countries that successfully enrol more than 50 % of their three-year-olds.<sup>22</sup> Access widely varies between rural and urban areas: children in cities are 21 % more likely to attend preschool than their rural peers.<sup>23</sup> Socioeconomic inequalities persist. Children from families in the highest quintile of income earners are 39 % more likely to enrol in preschool, than those in the lowest quintile.

### SIBs and Early Childhood Education in LAC

In addition, beyond notable gaps in coverage, **variation in the quality** of services is also an important challenge for the region. An IDB review of early childhood services in LAC states that “Scant evidence

about the quality of existing services suggests that it is heterogeneous and, in many cases, at dangerously low levels.”<sup>24</sup> Early evidence from Brazil confirms that, despite ECD centre receiving similar levels of funding, there is significant variation in quality.

Most approaches to enhancing quality in public sector service delivery require increasing process standards and subsequently trying to monitor and control, based on those standards. SIBs apply a very different mechanism – increasing quality by rewarding results. In some cases, rewarding quality through results-based payments may be more efficient than the cost associated with centrally-organised monitoring and control systems. It may also be more adaptive to innovative approaches that are more effective at the same or less costs.

While primary and secondary education is sometimes viewed as the dominion of the state, early childhood development has enjoyed broader involvement and participation of **third sector service providers** and private sector support. Some of these service providers have developed innovative models that are showing promising results, and could be scaled, with access to new forms of capital.

Nonetheless, using Social Impact Bonds to scale early childhood development programmes faces a **number of challenges** in LAC, most notably, the choice of payment metrics. If a SIB in ECD is going to be an effective mechanism, it must find a way to measure outcomes in a reasonable timeframe that rewards improvements on both cognitive and non-cognitive skills. These metrics should ideally be objective, relatively cheap, difficult to manipulate, while at the same time, predictive of long run, labour-market outcomes. This is difficult to do. While there is strong evidence that investing in a child early years provides the greatest returns, few investors will be willing to wait until the child is old enough to enter the labour market to get paid. In the SIB on early childhood development that was launched in Utah, the payment metric was based upon entrance into special education up through grade 6. This metric was chosen, in part, because (a) a previous evaluation had shown that a programme could successfully prevent entrance into special education

<sup>21</sup> The Millennium Development Goals and the Equality Agenda for Latin America and the Caribbean. Publication no. 623. ECLAC, Aug. 2010. Web. 29 Jan. 2014.

<sup>22</sup> “Access and Equity.” Early Childhood Care and Education Regional Report. Proc. of World Conference on Early Childhood Care and Education, Moscow. United Nations Education, Scientific, and Cultural Organisation, 27 Aug. 2010. Web. 29 Jan. 2014.

<sup>23</sup> “The Right to Education: An Unfinished Task for Latin America and the Caribbean.” Challenges 3 (3 Aug. 2006): 2-12. UNICEF. Web. 20 Jan. 2014.

<sup>24</sup> Araujo, Maria Caridad, Florencia Lopez-Boo, and Juan Manuel Puyana, Overview of Early Childhood Development Services in Latin America and the Caribbean” Inter-American Development Bank (August 2013).

among treated populations; and (b) avoiding special education costs up through grade 6 could finance the totality of the SIB. In cases where a direct, cashable cost savings to the government cannot be found, other value-for-money arguments may need to be used, and payment metrics chosen accordingly. More rigorously demonstrating the **value for money case** of SIBs in early childhood development is case for further research and analysis.

### Primary School Education

Despite facing challenges to improve equity in preschool access, Latin American countries are moving closer to achieving the universal, primary education commitments made in the Dakar Framework for Action and the Millennium Development Goals in 2000. The rate of primary school enrolment in Latin American countries falls only slightly below the average of high-income OECD countries. The average investment by Latin American countries in education for the lowest income quartile is 4.7 % of GDP per capita, compared to 3.1 % of GDP per capita spending in the United States.<sup>25</sup>

Publicly-funded cash transfer programmes, in nineteen Latin American countries, provide subsidies for poor families to help keep their children in school. Other successful interventions include providing free textbooks, additional teacher training and after-school tutoring. The investments in primary education successfully expanded access and increased the quantity of the young students that receive education regardless of their socioeconomic background or geographic location.

### SIBs and Primary Education in LAC

In general, primary education is considered the responsibility of the state. Therefore, Social Impact Bonds may be best suited in areas where there are clear gaps in services or where complementary programmes can enhance educational outcomes, without having to displace the existing programmes. In addition, SIBs and performance contracting may also be relevant in instances where primary education services are already publicly-financed but privately-delivered, such as through voucher programmes. In Chile, the government disburses a per-student payment to private schools

that are accredited by the state. A Social Impact Bond might **go further by not just rewarding schools for putting students in a seat, but also to pay for performance** – ensuring that they are actually learning. Private investment could be useful to help finance and implement school improvement programmes, as well as combine traditional PPPs structures, alongside outcomes-based contracting structures for services provided.

Social Impact Bonds are sometimes called ‘development impact bonds’ when they rely on a donor or aid agency to pay for outcomes instead of a government. In Pakistan, the potential for a donor-financed Development Impact Bond (DIB), in primary education, was explored in a case study that was published in the DIB working group report. The case study considered the use of a DIB to increase educational outcomes, through the expansion of affordable, low-cost private schools. These schools have historically struggled to access the capital they would need to expand and improve their facilities to meet demand.<sup>26</sup>

In the case study, the development impact bond paid schools based on capacity, attendance rates and learning outcomes, enabling these schools to borrow from the future outcome payments, in order to finance their infrastructure expansion. Once these schools are set up, they generally have a healthy cash flow, through affordable student fees. Consequently, expanding low-cost private schools “could potentially offer a scalable and sustainable solution to education in Pakistan.”<sup>27</sup> We are unaware of any progress on furthering the design or implementation of the case study since it was published.

Challenges to implementing such a Social Impact Bond include designing reliable and objective metrics, that avoid manipulation of test scores, and reliably attributing the impact of learning improvements to the schools (vs. other factors). Much research has been conducted on how these metrics might be structured, but challenges still remain.<sup>28</sup>

### Secondary School Education

The high enrolment rate in primary education falls, as students enter secondary school, and further decreases depending on student age and income. Considering trends of other countries with similar GDP per capita, an additional

<sup>25</sup> Breceda, Karla, Jamele Rigolini, and Jaime Saavedra. Latin America and the Social Contract: Patterns of Social Spending and Taxation. Rep. no. 4604. The World Bank, Apr. 2008. Web. 20 Jan. 2014.

<sup>26</sup> CGD and Social Finance, p. 53

<sup>27</sup> Center for Global Development and Social Finance. Investing in Social

Outcomes: Development Impact Bonds. 2013. Pg.53

<sup>28</sup> See, for example, Ladd, Helen F., and Randall P. Walsh. “Implementing value-added measures of school effectiveness: getting the incentives right.” *Economics of Education review* 21.1 (2002): 1-17.

18.7% of Latin American students should be enrolled in secondary education.<sup>29</sup> Grade repetition rates of 21% in Brazil, 13% in Guatemala, and 11% in Nicaragua show the educational challenges ahead for those countries.<sup>30</sup> Among 20 to 24-year-old Latin Americans, only 49% of males and 55% of females have completed 12 years of education.<sup>31</sup> The IDB finds a large decrease in high school graduation correlates with lower family income.

Poor families are more likely to withdraw students from school, so that they may enter the workforce. More than half of students in rural areas do not complete even nine years of schooling. The students who do not complete high school are not able to benefit from free tuition at many public universities.

The low quality of education is another reason students do not stay in school. The 2012 PISA exam, conducted globally to test quantitative, verbal, and scientific abilities amongst 15-year-old students, revealed that Latin American students are failing to reach basic aptitude levels, and are performing comparatively worse than other developed countries. The eight, participating Latin American countries ranked in the bottom twenty, for every section.<sup>32</sup> Every one of those countries had more than 50% of its students scoring in the lowest levels of maths. Results from the 2006 PISA indicated that average performance varied according to economic position because children from higher income levels were 2.3 times more likely than lower income peers to earn level II or higher scores.<sup>33</sup>

The Second Regional Comparative and Explanatory Study (SERCE) found that only 10% of the poorest students pass knowledge and skill aptitude tests, compared to the 50% rate of the highest income students.<sup>34</sup> Location contributes to the education gap, as urban students outperform their peers in rural areas. Poor regional performance may weaken global competitiveness and the failure to pass basic aptitude tests suggests a lack of problem-solving skills necessary in the domestic job market.

## SIBs and Secondary School Education

Afterschool, complementary learning programmes help to improve learning and increase school retention, without relying solely on school-based reform. Afterschool programmes may be more viable for a Social Impact Bond, than school-based reforms, because investors will have greater jurisdiction over independent operators, than they might have over publicly-operated school systems in a school-based reform setting. Interventions targeted at high-risk youth cannot only reduce levels of dropouts, but can also help to reduce entrance into delinquency or youth gangs.

Based on research in the US, the Harvard Family Research Project (HFRP) identified two principles to guide thinking on this growing intervention area. The first being that both school and non-school contexts are critical to children's learning and achievement; and the second being, that learning opportunities and contexts should complement each other.<sup>35</sup>

Like early childhood development interventions, programmes in this area have been shown to prevent negative behaviours later on in a student's life, promote better learning habits, and enhance educational achievement. Integrated family, school, and community services have shown better outcomes for all of the partners involved in the programmes, including schools, with less violent behaviour, and marked improvements in academic outcome.

Other interventions, such as teacher training, may also be strong candidates for SIBs to help public and private schools to improve education outcomes in priority areas. Some of these teaching programmes are supported by third sector organisations and have rigorous evaluations around them showing their positive effects.

Challenges remain, however, to financing these types of programmes through a SIB. First, the intended impacts

<sup>29</sup> "Cross-Generational Perpetuation of Inequality." Regional Preparatory Meeting 2011 United Nations Economic and Social Council Annual Ministerial Review. Proc. of Challenges for Education with Equity in Latin America and the Caribbean, Buenos Aires. ECLAC, May 2011. Web. 25 Jan. 2014.

<sup>30</sup> "The Right to Education: An Unfinished Task for Latin America and the Caribbean." Challenges 3 (3 Aug. 2006): 2-12. UNICEF. Web. 20 Jan. 2014.

<sup>31</sup> "Cross-Generational Perpetuation of Inequality." Regional Preparatory Meeting 2011 United Nations Economic and Social Council Annual Ministerial Review. Proc. of Challenges for Education with Equity in Latin America and the Caribbean, Buenos Aires. ECLAC, May 2011. Web. 25 Jan. 2014.

<sup>32</sup> Bos, María Soledad, Alejandro Ganimian, and Emiliana Vegas. "Cómo Le Fue a La Región?" Issue brief. Inter-American Development Bank, Dec.

2013. Web. 25 Jan. 2014.

<sup>33</sup> Duarte, Jesús, María Soledad Bos, and Martín Moreno. Inequity in School Achievement in Latin America. Rep. no. IDB-WP-180. Inter-American Development Bank, Apr. 2010. Web. 25 Jan. 2014.

<sup>34</sup> Duarte, Jesús, María Soledad Bos, and Martín Moreno. Inequity in School Achievement in Latin America. Rep. no. IDB-WP-180. Inter-American Development Bank, Apr. 2010. Web. 25 Jan. 2014.

<sup>35</sup> Beyond the classroom complementary learning to improve achievement outcomes. Harvard Family Research Project. Accessed online at: <http://www.hfrp.org/evaluation/the-evaluation-exchange/issue-archive/complementary-learning/beyond-the-classroom-complementary-learning-to-improve-achievement-outcomes>.



of secondary school education programmes may be difficult to objectively measure and assign attribution to certain social outcomes, such as entry into youth gangs, delinquency and crime. Second, most secondary schooling in LAC is provided by the public sector. Private voucher school programmes are very limited and oftentimes controversial, thereby limiting the potential for SIBs in secondary education. Third, because there are a number of important, but hard to measure outcomes in secondary education, it is important that SIBs do not distort funding and service provider focus away from these activities. Fourth, some programmes, such as teacher training programmes, when scaled up will need to be able to navigate within potentially contentious political environment, particularly teacher unions in some countries.

### Vocational Education

The region's many vocational training programmes offer mixed-quality services that often do not meet employer demand, churning out graduates with uncompetitive skillsets. In 2012, the workforce consulting company, ManpowerGroup, surveyed<sup>36</sup> 38,000 companies in 41 countries. The survey revealed that one in three employers (34 %) are struggling to find qualified employees. Of the LAC countries included in the survey, employers in Brazil (71 %) are having the hardest time finding staff. In order to sustain LAC growth, countries and companies need to fill the skills gap.

Latin American countries must identify policies that address educational equity and quality, in order to support long-term, social mobility and improve students' workforce preparedness. Students who enter the job market before completing secondary school, and who, therefore, lack specialised skills, are less likely to find work in the formal sector. Colombia, Chile, and Brazil have Vocational Training Institutes (VTIs) that organise internships in return for tax credits in order to expand preparation, increase formal employment and provide technical training to students. Through APROLAB II, Peru reorganises the curriculum and retrains coordinators at more than 50 vocational institutions in order to better prepare students for workforce demands. Many of these programmes focus on training women, underrepresented ethnicities, and students with special needs. Vocational

education can provide more opportunities for low-income students, since only 0.7 % of students, between the ages of 25-29, in the lowest-income quintile, completed higher education by 2010.<sup>37</sup> In addition to expanding programmes to reach a greater number of students, improving the content and relevancy of vocational education is critical to advancing the skills of Latin American workers and making them more competitive in the global job market.

### Vocational Education and SIBs in LAC

A Social Impact Bond, for job training in Latin America, could be modelled on some of the SIBs in the US and UK that are already in design or implementation. As noted above, the majority of these SIBs focus on vocational training and labour-market reintegration amongst ex-convicts or NEETs (Persons Not in Education, Employment, or Training). In high-income countries, these populations have the potential to provide direct, cashable cost-savings to the government, either by averting future incarceration, or by saving money on future unemployment claims and other welfare payments.

Challenges to implementation in Latin America include establishing the high-net benefits of job training programmes and finding investable service providers with evidence of success. Establishing the high-net benefits of job training focused solely around cost-savings (as it is in high-income countries), may be challenging in those LAC countries which don't have as significant a social safety net. The equivalent, cashable savings in LAC countries may not be sufficient to finance the totality of a SIB, and designers may have to make broader, value-for-money arguments. Furthermore, if SIB designers chose to work with ex-offending or NEET populations, evidence of successful de-risked programmes may be a constraint. For example, the Massachusetts SIB works with a service provider that has more than 25 years' experience implementing the programme model in similar communities. The New York State workforce SIB works with a service provider whose programme was rigorously evaluated, showing positive results. Finding similarly well-established and successful service providers may be a challenge in Latin America.

<sup>36</sup> ManpowerGroup Seventh Annual Talent Shortage Survey, May 2012.

<sup>37</sup> The State of Education in Latin America and the Caribbean: Towards a Quality Education for All – 2015. Rep. Regional Bureau of Education for

Latin America and the Caribbean (OREALC/UNESCO Santiago), 29 Oct. 2013. Web. 27 Jan. 2014.

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## PAYMENT METRICS

Choosing appropriate, payment metrics is one of the most critical decisions in the design of a SIB. When payment metrics are chosen well, they promote a high level of accountability, align incentives between stakeholders and ensure that all SIB members are striving towards a common goal. When payment metrics are poorly chosen, they can obscure the measurability of a programme, introduce subjectivity into the evaluation of outcomes and even create perverse incentives that can do more harm than good. Payment metrics must, therefore, be specific, reliable and objective. Special consideration should also be given to avoiding perverse incentives that may incentivise undesired behaviour or could lead to “gaming” or the manipulation of results.

Metrics should also be designed with an eye toward rewarding work with the entire population, as well as avoiding cream-skimming. For example, a flat fee paid for a student who passes a standardised test, will incentivise providers to work with students, who are just on the edge of passing, and to avoid students, who appear to be far from passing. To address this potential bias, a binary indicator (pass or fail) might be transformed into a continuous indicator (test score) which incentivises improvement across the range of learning outcomes. In addition, in some SIB and RBF instruments, outcomes are “tariffed.” For example, particularly disadvantaged or hard-to-reach populations may receive a higher price-per-outcome than other populations

that are easier to impact. This may reflect the fact that the marginal cost of improving outcomes amongst these populations is higher; or it may also reflect equity concerns (valuing improvements amongst those who are worse off, more than for those who are already better off).

The level, type, and cost of measurement should also be considered as they can determine the focus of an intervention and feasibility of an evaluation. Metrics can be established at individual (days in attendance), cohort (test scores in a class), or community (enrolment rates) levels. It is important to anticipate how these measurements will be undertaken and if they can be done objectively and at a reasonable cost.<sup>38</sup>

SIB designers seek to match a cost-effective programme with service providers who are capable of delivering that programme at scale. For programmes that require integrated, or a diverse set of, interventions to achieve outcomes, multiple service providers may be selected and coordinated through a SIB intermediary. For example, for the UK’s first SIB, Social Finance set up the One Service which subcontracted managed services from four service providers, during the tenure of that contract.

In designing Social Impact Bonds, social interventions should be assessed not simply based on their effectiveness (how much they improve outcomes), but on their cost-effectiveness (the cost-per-unit improvement in outcome). Evidence on cost-effectiveness of educational interventions in Latin America is unfortunately relatively sparse.

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<sup>38</sup> Investing in Social Outcomes: Development Impact Bonds. The Report of the Development Impact Bond Working Group. Pg. 72

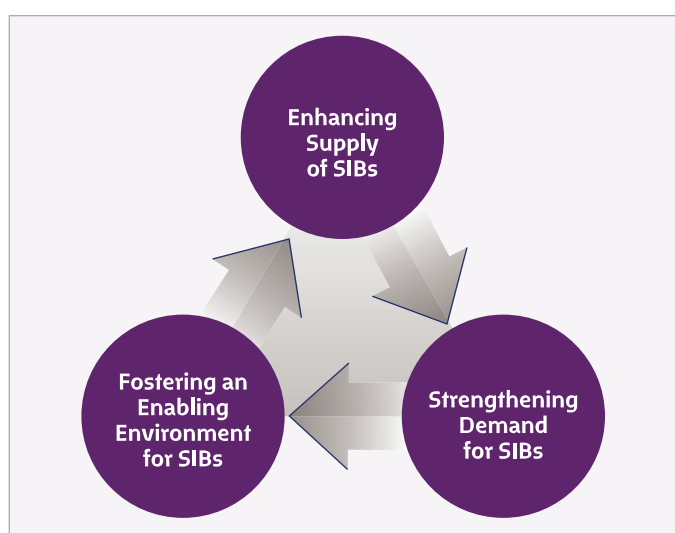
**Table 1: Potential Payment Metrics for Social Impact Bonds in Education**

<b>Early childhood development</b>	<ul style="list-style-type: none"><li>• Reduced incidence of special education in primary school *</li><li>• Peabody Picture Vocabulary Test</li><li>• Bayley Scales of Infant Development</li></ul>
<b>Primary &amp; secondary education</b>	<ul style="list-style-type: none"><li>• Enrolment: # or % of out of school students enrolled in school</li><li>• Retention: % of students who do not drop out and progress in grade level over a given time period</li><li>• Attendance: # of days of schooling induced</li><li>• Learning: Change in learning outcomes (as measured by a standardised test such as PISA or national standards)</li></ul>
<b>Vocational education</b>	<ul style="list-style-type: none"><li>• Entry into employment *</li><li>• Sustained employment (post 6 months, 12 months or 18 months) *</li><li>• Entry level qualification measured on a standardised vocational test *</li></ul>

\* indicates that a SIB currently in implementation uses this or a similar payment metric

## IV. MARKET DEVELOPMENT

Building a market will inevitably entail building a supply of well-structured SIB transactions, enhancing demand for contracting for social outcomes, and creating an enabling environment that allows for a diverse set of organisations and institutions to innovate, take risks and grow within a burgeoning market for social impact.



### Enhancing Supply of SIBs

At this stage of the market development what is needed more than anything is a strong proof of concept in Latin America to establish a series of quality precedents for future SIBs to come. The early stage of the market development will require the active participation of philanthropy to underwrite the costs of market building and support the development of robust pipeline of SIBs over time. A major push around the creation of the initial assets will be needed to support topic research and feasibility studies, data collection and analysis, design of impact evaluations, cash flow modelling and cost-benefit analyses for governments. Overtime, SIBs will increasingly need to be structured around topics that allow for easy replication and contracting. Choosing the right interventions for SIB pilots will establish this trend from the outset. While SIBs can technically be applied to finance a broad array of topics, some topics may be better suited than others.

### Strengthening Demand

Strengthening demand includes investors demand for well-structured SIB projects and government demand for procuring social outcomes. For both investors and governments and prospective investors, awareness

is still very low. With the majority of research and background material in the English language it is very uncommon to find familiarity with SIBs.

Strong signals by governments of the demand for buying social outcomes would greatly help grow the market. One idea has been proposed by several market participants is the creation of a social outcomes fund. The fund, which could be regional or country-focused – would set aside a certain amount of money for the purchase of social outcome. Such a mechanism would provide a strong signal to the market of its size and trajectory. The carbon market and the creation of the early carbon funds at the World Bank may offer some insights for further exploration.

While the initial SIBs can largely be underwritten by philanthropy and socially motivated investors, over time, the SIB market will need to become more liquid and inclusive of more commercially orientated financial institutions. SIBs so far are largely bespoke, have few benchmarks for pricing, provide below market returns, and lack secondary market (e.g. the ability to sell over an exchange). This will need to change over time to broaden the investor pool.

### Fostering an Enabling Environment for SIBs

Most governments will have not have accommodative legal frameworks for SIB contracting and will therefore need to explore possible changes in their legal frameworks. Countries with pre-existing PPP frameworks and well-developed capital markets may be the right place to start. Depending on the country and whether financing for education is held at the federal, state, or municipal level, implementing pay for success in the sector may be challenging. In the US and UK, organisations that have been highly specialised in Social Impact Bonds have played a central role in the market development process – educating governments, structuring and identifying SIBs, building the capacity of service providers. In Latin America, there are a handful of organisations that might fit this profile, but will need seed money and the transfer of knowledge from existing SIB experiences.

These first deals should place a heavy emphasis on limiting the level of confidentiality. Firsts of anything entail high transaction costs and to the extent that these initial experiences can deliver public goods in the form of standardised tools and methodologies, legal contracts, terms sheets, will provide a great boost for the market.

## V. CONCLUSION

Social Impact Bonds may hold great promise for helping resolve some social sector problems in Latin America, but they still have a long way to go. Despite all of the buzz and build-up of the model, the fact remains that Social Impact Bonds are largely unproven to date. In fact, no Social Impact Bonds have actually run their full course from launch to final payment. And in the Latin America, we are at the starting point.

The education sector could be a promising area for SIBs to add value in LAC given the gaps in service delivery, persistent achievement gaps, and a long-standing culture of partnership and shared value between the public and private sectors in many countries. In the US and UK, social impacts bonds have been positioned around their ability to generate savings for government through investment in prevention. For instance, investing in ECD in the US can reduce the number of children entering into costly special education programs. In Latin America, the cost-savings may be difficult to measure and, with education spending on the rise in many countries, savings may be of less immediate concerns to policy makers. For many countries SIBs could increase outcomes, drive innovation and transfer risk.

This paper has attempted to provide some initial thoughts into how Social Impact Bonds could support the education sector in Latin America. The following list of concluding thoughts are for further debate, research and discussion.

1. **More Research** is needed on what are the best SIB topics in education in Latin America. This research should analyse more deeply and on a country basis what are the value drivers and underlying business case for SIBs in the Latin American context, and which countries have the right overall enabling conditions for SIBs in terms of legal framework, education needs, local capacities of service providers, data availability, investor interest and presence, among a host of other things. No one institution can take on this work load, so mobilising a variety of local and international thought leaders on SIBs can help mobilise SIBs from an interesting financing model to a meaningful pilot on-the-ground.
2. **Market Education** can bring Social Impact Bonds into the mainstream discussion on education. Awareness among policy makers and the private sector in LAC is extremely low. There are currently no materials, aside

from a few short one-pagers put out by the IDB, on Social Impact Bonds in the Spanish or Portuguese language. An effort to educate governments, service providers, researchers, and funders with the right communications material and strategies will be an important first step to build local ownership, a necessary condition for developing the first SIB.

3. **Entrepreneurship** is at the core of Social Impact Bonds and plenty more is needed. A market for SIBs will require a range of NGOs, private firms and investors, public authorities, researchers, and philanthropists that are willing to take risks, innovate and transform how social problems are financed and addressed. It will also require a knowledge of finance and a culture of innovation and understanding of local social, economic and political risk factors. These qualities may not be present at first but can be supported by donor assistance and partnership with other more experienced players with expertise and experience in SIBs.
4. **Strong Proof-of-Concept** will help turn sceptics into believers. Currently, there is no tangible example of a SIB in LAC. Nonetheless, while getting the first SIB off the ground is important, finding the right SIB topic within the education sector is equally, if not more, important. Making sure these early SIBs are done right and are well thought out in their structure and justification will be critical for replication and long-term sustainability. What topics are best suited for the first SIB in education in the region and which country(ies) should be targeted is a topic for further research and discussion.

# APPENDIX: SELECTED STUDIES POTENTIALLY RELEVANT FOR SOCIAL IMPACT BONDS IN LATIN AMERICA

**Table 2: Selected evidence-based early-childhood development programs in LAC**

Population studied	Intervention	Quality of Evidence	Outcomes & Impacts	Value Drivers
Infants aged 1-2 in 96 small municipalities in Colombia	Weekly home visit from a <i>madre lider</i> (local “mother leader”) who taught games and other training curricula to encourage family interaction with child and distributed nutritional supplements. Cost would be about US\$ 300-400 per child at scale.	Randomised control trial comparing a treatment and a control group. <sup>39</sup>	Positive impact on Bayley test on language and cognitive development tests and MacArthur-bates assessment of number of words a child can say.  No detectable impact of the nutrition component.	Reduction of remedial education in primary school, medium-term improvement of educational outcomes, Improved long-term labour market outcomes
Children between 9 and 24 months of age in Jamaica	1 hour weekly visits from community health workers over a 2 year period that taught parenting skills and encouraged mothers to interact and play with their children in ways that would develop their children’s cognitive and personality skills.	Randomised evaluation of 4 groups – control, supplementation, stimulation, and supplementation and stimulation. Compared with another group that was not-stunted but controlled for age, sex, and neighbourhood. <sup>40</sup>	Compared with no intervention, stimulation resulted in higher full scale IQ scores and higher scores on the verbal subscale, Peabody picture vocabulary test, verbal analogies, and reading tests. Overall, stunted non-stimulated participants had significantly poorer scores than the non-stunted group on 11 of 12 cognitive and educational tests	
Children aged 7-15 in Uruguay	Uruguayan publicly provided pre-primary education.	Regression on an observational panel dataset. Authors controlled for unobserved household characteristics by exploiting variation in treatment between siblings within the same family. <sup>41</sup>	Positive effect of preschool attendance on completed year of primary and secondary education. A fall in retention rates since the early school years (from age 11 onwards) and a reduction in dropout rates among teenagers (from age 13 onwards).	

<sup>39</sup>. Attanasio, Orazio, Camila Fernandez, and Costas Meghir. “Home Visiting in Colombia: Impacts of a Scalable Intervention.” (2012); Attanasio, Orazio, Emla Fitzsimons, Sally Grantham-McGregor, Costas Meghir, and Marta Rubio-Codina. “Early Childhood Stimulation, Nutrition and Development: A Randomised Control Trial.” Center for the Evaluation of Development Policies. Institute for Fiscal Studies. Mimeo. 15 Jul 2013.

<sup>40</sup>. Walker, Susan P., et al. “Effects of early childhood psychosocial stimulation and nutritional supplementation on cognition and education in growth-

stunted Jamaican children: prospective cohort study.” *The Lancet* 366.9499 (2005): 1804-1807; Gertler, Paul et al. “Labor market returns to Early Childhood Stimulation: a 20 year followup to an Experimental Intervention in Jamaica” University of California Berkeley. 2013

<sup>41</sup>. Berlinski, Sam et al. “Giving Children a Better Start: Preschool Attendance & School-Age Profiles” William Davidson Institute Working Paper Number 860 January 2007.

**Table 3: Selected evidence-based primary & secondary school education programmes in LAC**

Population studied	Intervention	Quality of Evidence	Outcomes & Impacts	Value Drivers
8th grade boys in the Dominican Republic	Information was provided on adult income by education level as well as the return implied by those numbers	Randomised control trial assigned informational intervention to randomly selected villages in the Dominican Republic. <sup>42</sup>	Before the programme, the perceived returns to education were extremely low. Students who received the informational intervention completed an average of 0.20-0.35 more years of schooling over the next four years. Because information is cheap, the programme was extremely cost-effective at about \$32 per additional year of schooling casually induced by the programme. <sup>43</sup>	Higher secondary school graduate rates, greater labour market income

<sup>42</sup> Jensen, Robert. "The (perceived) returns to education and the demand for schooling." *The Quarterly Journal of Economics* 125.2 (2010): 515-548.

<sup>43</sup> Dhaliwal, Iqbal, et al. "Comparative cost-effectiveness analysis to inform policy in developing countries: a general framework with applications for education." Abdul Latif Jameel Poverty Action Lab, 2012.

**Table 4: Selected evidence-based vocational training programmes in LAC**

Population studied	Intervention	Quality of Evidence	Outcomes & Impacts	Value Drivers
Young people between ages 18 and 25 in seven cities in Colombia who were NEET (not in employment, education or training) and were in the lowest deciles of the income distribution	Programme combined classroom with on-the-job training. Programme combined 3 months of classroom training with 3 months of on-the-job training. A small living stipend was also given to enable low-income students to participate during the programme.	Randomised control trial randomly assigned students into the programme. <sup>44</sup>	Employment increased by 6.1 percentage points and paid employment increased by 7.1 percentage points for women. The program had no impact on employment or earnings for men; however it increased likelihood for employment in formal sector for men by 5.3 percentage points.	<ul style="list-style-type: none"> <li>• Reduced unemployment insurance</li> <li>• Reduced incidence on social welfare or social protection schemes</li> <li>• Greater income tax</li> <li>• A better trained more productive labour</li> </ul>
Low-income, poorly educated 16-24 year olds	Classroom and on-the-job training. Followed with an internship at a previously contracted firm.	Synthesis of job training programmes for youth: evidence from six countries in LatAm. <sup>45</sup>	Employment effects range from modest to meaningful –increasing the employment rate by about 0 to 5 percentage points with impact of 6 to 12 percentage points in the employment rate. In most cases there is a larger and significant impact on job quality, measured by getting a formal job, having a contract and/or receiving health insurance as a benefit. However, the effect of job training on employment varies by age, gender and region.	<ul style="list-style-type: none"> <li>• Reduced unemployment insurance</li> <li>• Reduced incidence on social welfare or social protection schemes</li> <li>• Greater income tax</li> <li>• A better trained more productive labour</li> </ul>

<sup>44</sup>. Attanasio, Orazio, Adriana Kugler, and Costas Meghir. "Subsidizing Vocational Training for Disadvantaged Youth in Colombia: Evidence from a Randomized Trial." *American Economic Journal: Applied Economics* 3.3 (2011): 188-220.

<sup>45</sup>. González-Velosa, C., Ripan, L., & Rosas-Shady, D. (2012). *How Can Job Opportunities for Young People in Latin America be Improved?* Inter-American Development Bank: Labor Markets and Social Security Unit (SCL/LMK), Technical Notes No. IDB-TN-345, May 2012



# ACRONYMS

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<b>DIB</b>	Development Impact Bond
<b>DFID</b>	Department for International Development (UK Government)
<b>DWP</b>	Department of Works and Pensions (UK Government)
<b>ECD</b>	Early Childhood Development
<b>IDB</b>	Inter-American Development Bank
<b>LAC</b>	Latin America & the Caribbean
<b>MIF</b>	Multilateral Investment Fund
<b>NEET</b>	Not in Education, Employment or Training
<b>PPP</b>	Public Private Partnership
<b>RBF</b>	Results-based Financing
<b>SIB</b>	Social Impact Bond
<b>VTI</b>	Vocational Training Institutes

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3rd Floor, The Tower Building, 11 York Road, Waterloo, London SE1 7NX  
T +44 (0) 207 593 4040 F +44 (0) 207 593 4041 W [gemsedsolutions.com](http://gemsedsolutions.com)