THE ROLE OF SOCIAL FINANCE TO SUSTAIN SOCIAL INNOVATION: AN EMPIRICAL ANALYSIS ON SOCIAL IMPACT BONDS

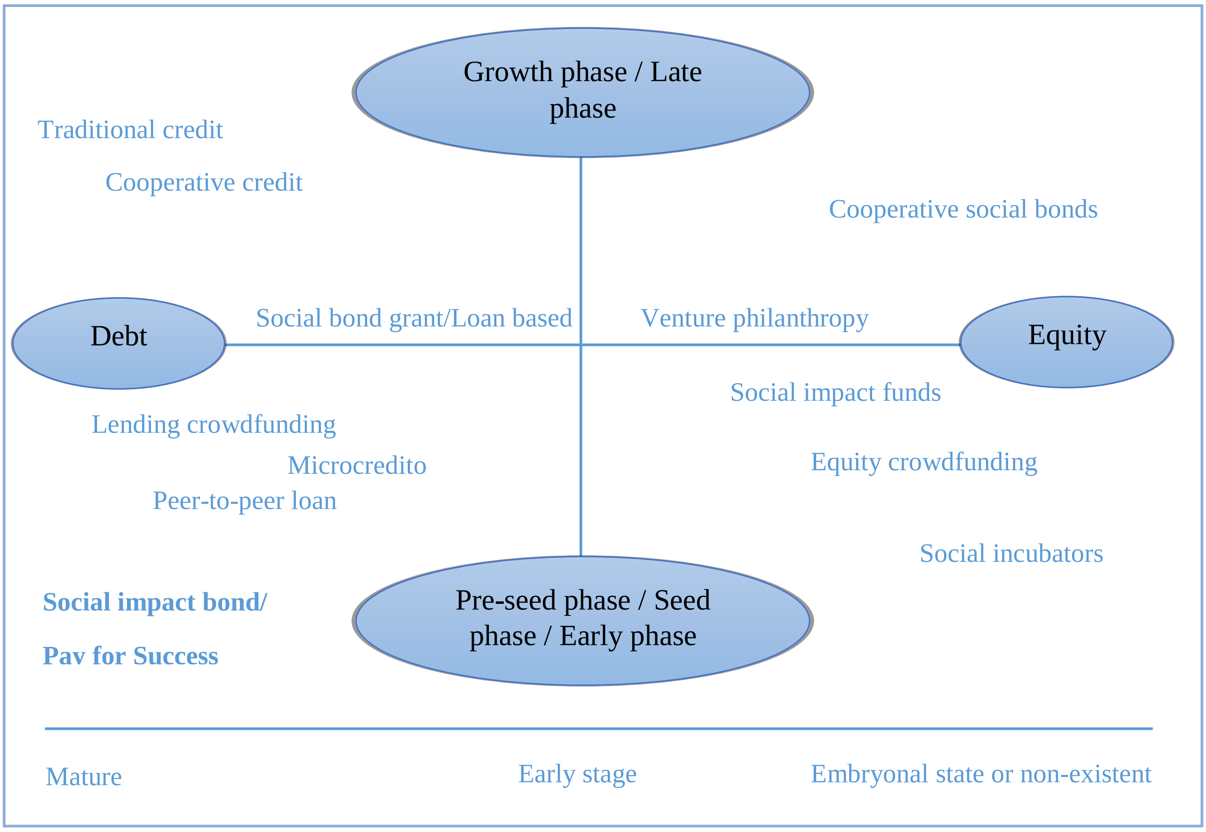
Key words: *social innovation, social finance, social impact bond*

Over the past few years, there has been a growing interest by the scientific community and policy makers in the concept of social innovation. Generally, la social innovation expresses “an ability to answer to emerging needs with new forms of actions and relationships” (Murray et al., 2010). The term is applied to an extremely heterogeneous set of initiatives and organizations, which ranges from the interventions of the third sector to the actions of for profit organizations with a marginal social impact.

The reconfiguration of public expenditures on welfare policy is one of the main drivers for the development of new forms of financing useful for social innovation (Azemati et al. 2013). Public funds allocated to welfare policies have been progressively reduced, particularly in highly developed economies and countries. This situation has led scholars, practitioners and policy makers to address the necessity of identifying innovative funding models capable of attracting private financial resources to be channeled towards the improvement of the sustainability of welfare systems (Azemati et al. 2013; Social Impact Investment Task Force 2014; Del Giudice 2015).

Accordingly, social innovation becomes a field of connection among the needs for social services, the inadequacy of the resources available to the public decision-makers and the interest of the financial world that identifies a new potential market in the welfare deficit. Specifically, the historical juxtaposition charity against profit no longer exists and an overlap area encompassing the category of Social Impact Investments is delineated. Social Impact Investments are defined as “(all those) investments which intentionally aim to the reaching of measurable social goals and to the generation of measurable economic returns” (Social Impact Investment Task Force 2014). The term "impact investing" refers to the specific branch of finance whose aim is to sustain investments whose specificity can be retraced in the coexistence of social goals and economic returns and in the qualification of the specific trade-off. In the broader context of Social Finance, impact investing is one of the emerging asset classes (Martin 2013; Trotta et al. 2015). However, a clear classification of the social impact investing instruments does not still exist. They are generally divided into equity and debt instruments and involve both mature and in embryonal phase financial instruments (Figure 1).

Figure 1 – The instruments of Social Impact in Italy (Social Impact Investment Task Force, 2014, p. 41)

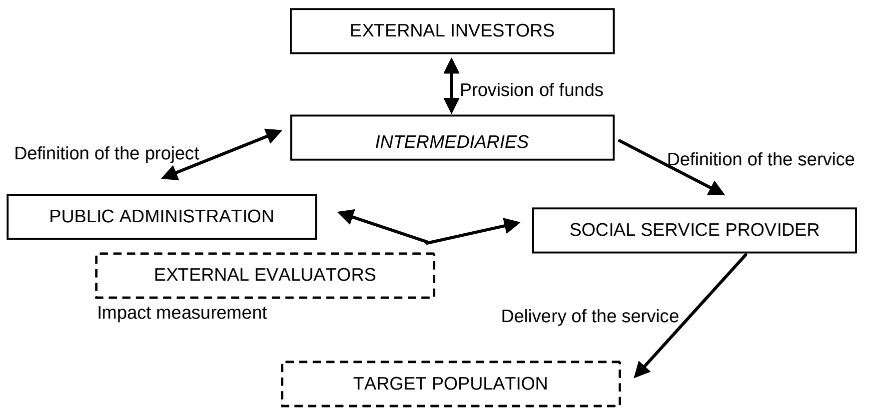


These financial innovations reveal the affirmation of a new financial market (social investment landscape) able to satisfy the financial needs typical of social innovation. The new market is not a replication or an extension of existing financial instruments and products that are no longer adequate (Kickul & Layons, 2015) but is destined to become an emerging research topic in the field of finance (Mendell & Nogales, 2009).

In our work, we intend to discuss the role of social and sustainable finance that can lead to social innovation and we focus on one of the most important and innovative form of funding of social programs within the financial markets: the Social Impact Bond (SIB). Up-to-date, 107 SIBs have been implemented worldwide (Instiglio; Social Finance), from the launch of the first pilot SIB in UK (Peterborough, HMP Social Impact Bond) in 2010.

SIBs are an innovative way to finance social programs, introducing a new form of public-private partnership to provide social services (Jackson, 2013; Nicholls, 2013; Stoesz, 2014; Liang et al., 2014). SIBs can be stylized as a principal-multiagent relationship that involves at least four parties (Cabinet Office, 2015; Fraser et al., 2016) (see Figure 2): a public administration (PA), a service provider, external investors (EI) and specialized intermediaries (INT). Two further actors, represented in the dotted boxes in Figure 2, are required for a SIB to be fully implemented: the external evaluators and the final beneficiaries.

Figure 2 – SIBs' stylized structure



Source: Del Giudice A. and M. Migliavacca, (2018)

SIBs are the financial response to the New Public Management's emphasis on outcome-based contracts in the public sector and an evolution of public-private partnerships (PPPs). Despite their name, SIBs are not exactly bonds but future contracts on social outcomes and can be funded either by debt, equity or donations (Humphries, 2013; Joy & Shields, 2013). They differentiate each other on the basis of financial features (e.g., *amount* of the issue, maturity of the SIB in years, technical form used to transfer financial resources from the investors to the SIB beneficiaries: grant/donations, equity or debt) and contractual structures (e.g., the presence of an SPV, the number of underwriters, local or central authority sponsoring the SIB issue, the social issue addressed), that are both crucial characteristics in complex public-private relationship (Quélin et al., 2017).

This research, after describing SIBs financial futures and contractual structures, specifically, focuses on social issue addressed by each SIB (the social purpose of the SIB), as a relevant aspect of the contractual structure, with the aim to investigate, through a cross-country analysis, whether specific social issues are dominant in such countries and not in others. To put it differently, we study the relation between social issue and country of issuance.

To test our hypotheses, we collect contractual and financial data (Arena et al., 2016; Quélin et al., 2017) from Social Finance UK, Instiglio and Non Profit Finance Fund, we managed to retain 67 SIBs out of a total of 107 globally issued.

The present work contributes to the current literature on the effective use of financial instruments in different welfare policies and has implications for both entrepreneurs and policy makers whose aim is to set up an effective and successful industry for social innovation.

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