

SOCIAL ENTREPRENEURSHIP NETZWERK DEUTSCHLAND E.V.  
CENTRE FOR SOCIAL INVESTMENT (CSI), UNIVERSITY OF HEIDELBERG

# Financing Social Innovation

International evidence



**BMW Foundation**  
Herbert Quandt



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## About CSI

The Centre for Social Investment (CSI) of the University of Heidelberg is an interdisciplinary institution. We actively promote research, teaching and practice transfer. Working towards the sustainable development of society through the interaction of civil society and the social economy with market players and state actors plays a key role for us. Central topics of our work are social innovations, social entrepreneurship, impact investing and impact measurement.

## About SEND

The Social Entrepreneurship Netzwerk Deutschland (SEND) is connecting social enterprises across Germany, to strengthen them and give them a common voice. SEND is building important bridges of the sector to politics, civil society, the welfare economy and commercial economy to drive positive change and to improve the framework for social innovations. With a (constantly) growing network of currently over 800 members, SEND is working towards a society in which all people benefit from progress.

We do so through what we call: **#GemeinsamWirken!** (Working and having impact together)

Our work is supported by the following cooperation partners:

**BMW Foundation**  
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# Why this study matters:

**“Access to finance is one of the greatest difficulties for social enterprises. Given the huge challenges we face as a society, the time has finally come that social and ecological criteria receive more attention in the institutional support of innovation so that we can scale the impact of social innovations.”**

— Katrin Elsemann, CEO Social  
Entrepreneurship Netzwerk Deutschland e.V.

**“The transformation towards sustainability consists of many smaller transformations. To achieve these we need innovative entrepreneurs and investors. These actors need more capital to actively support their innovation efforts. Compared to other countries Germany still has a lot left to do. The next federal government must put specific financing and support instruments for this target group at the top of the political agenda.”**

— Dr. Frank Niederländer, Chair of the National Impact Investing Initiative / Board member BMW Foundation Herbert Quandt

**“In contrast to other European countries, Germany still has no target group-specific financing and support instruments for social enterprises. Such instruments would increase the dynamism of the German social entrepreneurship space and would help it contribute profoundly to innovative solutions that benefit society, as is already the case in other countries.”**

— Karsten Löffler, Executive Director of the German government's Council of Advisors on Sustainable Finance

# Executive Summary

**In recent years, social innovations have received significant recognition in Germany across political parties, policy areas and ministries. However, there is still no holistic strategy for financing and supporting social innovations. This is different in many other countries.**

The recommendations presented in this report are based on an exploratory and comparative study, which systematically assessed the experiences made with such support structures in 10 countries and by 3 international organizations. More specifically, the study is grounded in in-depth interviews with 23 experts. The countries considered in this report exhibit a wide variety of economic and welfare systems, so that the condensed experiences across countries can be transferred to Germany with significant validity. Other countries internationally may benefit from this report, too.

**In Germany there is currently not only a restricted amount of financial resources that social innovators could benefit from—the finance which is available also often fails to meet the needs of this target group. At the same time, the mobilization of both, public and private capital is low.**

Against this background, effective financial support for social innovations should **pursue 4 strategies:**

1. Individual and static support measures are insufficient. The promotion of social innovation must have a process orientation that has the entire development cycle of social innovations in view.
2. The funding must be adequate for different types of social innovators and their respective business and revenue models.
3. Non-monetary support and networks for the dissemination of social innovations should play a central role.
4. Social and ecological impacts must be assessed in a holistic fashion and should be established as core decision criteria within the economy and society.

A complex financial architecture to promote social innovations is necessary to achieve these strategies.

**8 policy instruments** can be used to shape this financial architecture:

1. **Pooling of accelerator grants**  
[to focus on organizations instead of projects]
2. **Tax incentives or premiums for impact**  
[to promote non-market-oriented social innovations]
3. **Guarantees**  
[to balance out risk-reward-impact profiles]
4. **Pay-by-result principle**  
[to promote the maximization of impacts instead of the minimization of costs]
5. **Local Community Investments**  
[to enable citizens to invest in social innovations]
6. **Social procurement & quasi-market building**  
[to create income streams for organizations and exit options for investors]
7. **Opening up existing programmes**  
[to make instruments of established innovation support available to social innovators]
8. **Vouchers for capacity building and networks**  
[to create an ecosystem that is essential for the scaling of social innovations]

Closely linked to the political instruments are **5 financing vehicles** that are already being used successfully in different countries and that could serve as best practices for Germany.

- I. **Accelerator loans & grants**
- II. **Blended non-market finance**
- III. **Social Impact Bonds or Outcome Funds**
- IV. **Community Bonds**
- V. **Blended market finance**

**Accelerator loans and grants as well as blended non-market finance**, primarily aim at leveraging philanthropic capital in order to help non-market social innovators realize their full impact potential. The underlying idea is to use existing financial resources more effectively.

**Social impact bonds or outcome funds** can stimulate innovations in established fields. They promote effective problem solving and prevention instead of standard service provision.

**Community bonds** can help to anchor social innovations locally and to increase citizen's identification with social innovations.

**Blended market finance** helps create an investment case for commercial investors who do not invest in social innovations due to high levels of risk or the lack of an exit option. In order to enable an exit, this financing vehicle may have to be combined with the creation of quasi-markets that can generate income streams for social innovators.

**Our study not only develops the concrete recommendations just summarized, but it also clearly shows how similar political instruments and financing vehicles have been used successfully in other countries.**

**Germany has the opportunity to benefit from our systematic analysis of these experiences as well as our implementation plan for the effective support of social innovations. The country now has the chance to act as a vanguard and role model internationally, if it implements these measures in a timely and coordinated fashion.**

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# Why do we need to think about financing social innovation?

**We are facing immense societal challenges in Germany and globally, which cannot be solved through technological innovations alone.**

Instead, we need sustainable and socially oriented solutions, that is innovations with and for society. Such social innovations need adequate financial support. Promoting social innovations would not only enhance Germany's development towards a socio-ecological market economy, but also help renew the German welfare state and contribute to a diverse, lively and pro-active society.

In May 2020, the German Bundestag adopted a motion to promote social innovations for the very first time. Another important step towards establishing social innovations as a policy priority was the Social Innovation Strategy ([t1p.de/ttsd](https://www.t1p.de/ttsd) [bmbf.de]) developed and published by nine federal ministries in August 2021. The strategy lays out some central goals and options for promoting social innovations. Beyond that, however, there is no holistic approach to financing and supporting social innovations.

## **Social innovation, social entrepreneurship and impact:**

Social entrepreneurs are entrepreneurs who seek to produce social value and benefit by means of entrepreneurial action. They develop new solutions to societal problems and are therefore important drivers of social innovations. The effective support of social innovations, therefore, needs to take the funding needs of social entrepreneurs into account. However, social entrepreneurs are far from the only relevant actors that “do” social innovation. Individuals, established organizations and networks play a central role. If governments are interested in social problem solving and impact, they would do well to recognize and support this diversity and richness of social innovators and support their entire ecosystem and collective impact orientation. Supporting these effectively requires an ambitious and multi-dimensional financial architecture.

**“Given existing and future societal challenges such as demographic change, social cohesion, climate change and digitization, we need approaches that go beyond technical solutions. Social innovations have a big potential to contribute to sustainable solutions.”**

— Motion adopted by the 19th German government  
“Promoting social innovation more intensely and using their potential more efficiently”

**Such a financial architecture  
needs to address three goals:**

- 1. Helping innovative ideas take off**
- 2. Growing innovations with high impact potential**
- 3. Introducing an impact and innovation perspective into established systems**

Recent data show that 90 percent of social enterprises see at least one substantial financial barrier for their organization, for example: lack of patient capital (long duration), lack of adequate start-up finance, lack of adequate growth finance, or difficulties in using public grant finance or subsidies (see DSEM 2020/21 › [t1p.de/7ogr](http://t1p.de/7ogr) [send-ev.de]).

**Many countries across the globe already have public structures and processes for financing social innovation in place, which can serve as examples for Germany.** In our explorative research project, we analysed a wide range of international evidence from 10 countries and 3 international organizations. In particular we conducted in-depth interviews with 23 leading national experts to develop propositions on how to best finance social innovations. [1]

We would like to remark that the countries considered represent a wide range of different economic and welfare systems and that our recommendations are always based on impulses that came from various countries which shared similar challenges or had developed similar solutions. The caveat that experiences from other countries cannot be transferred to Germany, which is often voiced in political discussions about this subject, is therefore effectively addressed in this report.

While our analysis of challenges and recommendations of how to solve them focus explicitly on Germany, many prompts can be applied to the situation in other countries as well, including those for which we gathered evidence. We therefore hope to provide guidance for policy makers and ecosystem shapers globally through this report.

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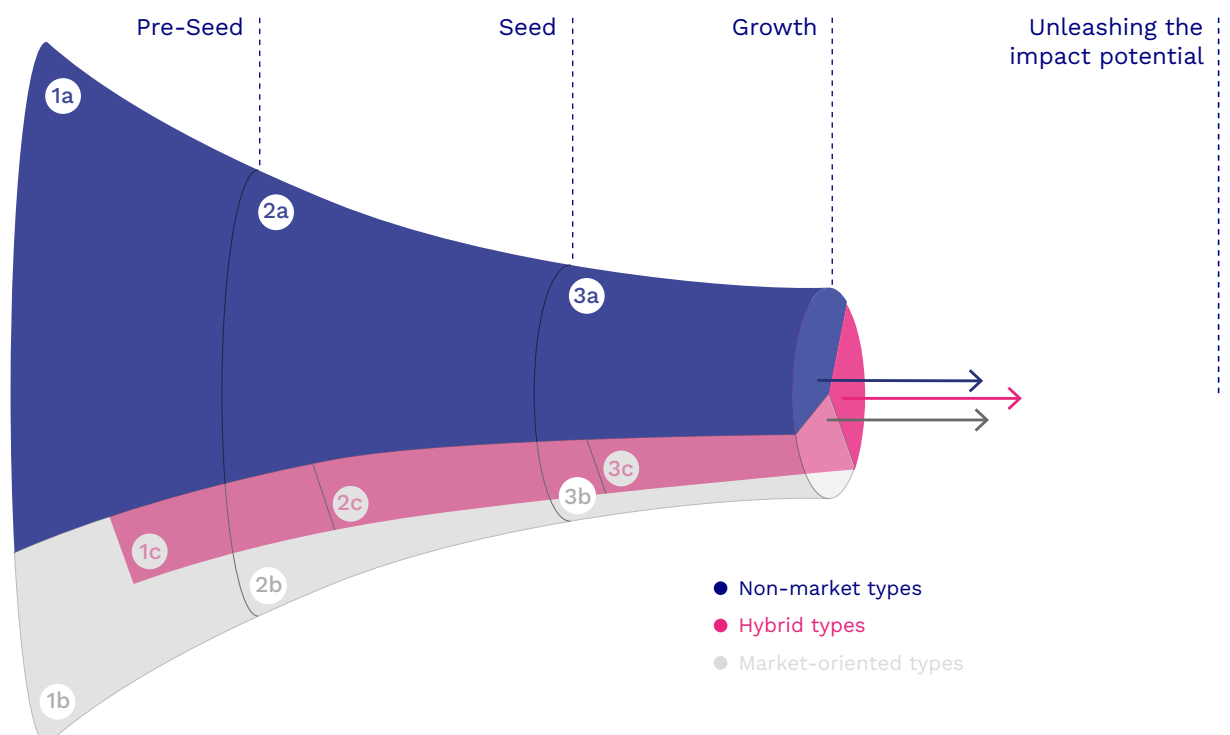
[1] We are mostly referring to finance or financing instead of investments, because we draw on the full range of potential financial support for social innovators, including equity, debt, mezzanine, or grant funding.

# Challenges in financing social innovation

**Supporting and financing social innovation is not an easy endeavour and substantially more complicated than financing commercial innovation. Particular challenges that the effective provision of finance needs to consider are located on two different levels, namely that of the social innovators, and that of the financing landscape.**

To set up target group-specific financing and funding instruments, it is important to differentiate between different types of and phases in the development of social innovators (see **Figure 1**). There are non-market and market-oriented types as well as hybrid types that lie in between the two. Each of the phases and types come with specific needs, which we explain in the following. We also discuss current deficits in the financing landscape for social innovations in Germany.

In this chapter it is becoming evident that approaching the topic from a commercial venture capital lens, which thinks in terms of “investment per venture”, is hardly useful. The support of social innovation is more akin to the public research and development (R&D) support for commercial innovation—and yet it differs in important ways from the latter as we explain here.



**Figure 1** Innovation funnel: Phases and types of social innovators

## Specificities and requirements of social innovators <sup>[2]</sup>

### Life-cycle

Social innovators need a substantially longer time on average to break-even or build a self-sufficient business model than commercial innovators. Financing needs are likely to shift as organizations evolve (from pre-seed to growth), whereby only ventures with a commercial legal form and market orientation (**3b.**) currently draw on the full spectrum of finance (based on DSEM 2020/21 [<https://www.dse.de/7ogr>] data about the use of finance by social enterprises). Non-market organizations are only able to draw on a small fraction of available finance (**1a.-3a.**).

### Income and financing models

Selling socially innovative products and services is a source of revenue to for example social enterprises. In contrast to commercial firms, however, social enterprises typically internalize external effects on society, which makes equal market access more difficult. Therefore, many social innovators always depend on hybrid income or financing sources, which may for example include public subsidies, donations, or revenues generated on public quasi-markets (**1a-c.**).

### Knowhow

Social innovators focus on creating social value and impact. This is why they need different skills and competencies than managers of more mainstream organizations or commercial entrepreneurs. Established start-up support logics, however, are ignorant of these assets. They ignore long-term considerations about externalities, hardly understand innovations that aim for systems change and the huge variety of actors that promote social innovation (entire innovation funnel of **Figure 1**). On the other hand, because social innovators are primarily purpose or social-impact-driven, they may lack financial management skills as well as awareness of financing options and their specificities.

## Deficits in the financing landscape for social innovations

### Availability

First, there is a lack of social mission driven investors, and if providers of finance have a philanthropic orientation, the provided funding is not aligned along the development phases on the innovation funnel. The seed phase is critical, especially for the non-market and hybrid types of social innovators, which often slip into the so called “valley of death” due to a lack of tailored finance (2. phase in **Figure 1**). Second, social innovators often do not represent an attractive risk-return-impact profile for investors. While they may offer a high impact potential, the associated risk is often also high or the expected financial return too low. This is why we need tailored measures to enable more targeted growth funding (3. phase in **Figure 1**).

### Long-term orientation

The financing landscape mostly focuses on relatively short-term financial support rather than a long-term orientation at developing social innovators and social innovations throughout their life-cycle. This hampers the unleashing of the innovations’ full impact potential (goal direction of **Figure 1**).

### Impact orientation

The social and ecological impacts of financial investments are becoming more important on financial markets. However, they as of yet do not serve as central criteria in actual decision making. This is because investors and innovators both have difficulties operationalizing it, despite a large amount and variety of impact measurement tools and efforts at standard setting.

### Ecosystem

Available finance mostly orients at individual market-oriented organizations with the potential for substantial financial returns. The financing landscape is not designed to promote social innovation ecosystems and processes. Such an ecosystem should not only comprise the full diversity of social innovator types presented in the innovation funnel (**Figure 1**), but should also extend to collaborative structures between those and market actors, policy makers, institutions in higher education and civil society.

[2] As mentioned before social enterprises are only one relevant actor of social innovation, but their challenges are proto-typically for the wider challenges of the field.

# Strategies for designing solutions

**Holding the challenges and priority areas above against international experiences in financing social innovation results in four strategies that the public provision and promotion of finance to social innovators should respect.**

## 1 Process orientation instead of individual measures

First, the financing of social innovators needs to be seen as a process rather than a static system. This means the financing must take the potential life-cycle of social innovators and its different stages into account (pre-seed, seed, growth). Only that way, we can ensure that we promote many innovative ideas, while making sure that organizations with the highest impact potential receive special attention.

It is important to realize that there are different fields of social innovation where new models will typically have the character of pre-seed ideas, because the fields are particularly challenging or neglected (for example social inequalities), while others will quickly develop, or by default possess a growth option (for example green tech). It is also important to stress that some social innovators may evolve along these stages over time. Especially for those operating in the challenging fields just mentioned, it is essential that providers of finance ask themselves the question: **“Who will take over in the next phase?”**, in order to ensure continuous thriving of the social innovation. Overall, the evolution of social innovation takes a long time, this is why social innovators need patient capital with long duration, initial grace periods or flexible interest or return expectations.

## 2 Financing all different types of social innovators

The revenue or financing models of social innovators vary strongly in their composition, a circumstance which leads to very different expectations of monetary returns. One of the main reasons is that many social challenges do not offer a straightforward business case, whereas social innovations may offer a tremendous direct or indirect return to society. Also, the beneficiaries of services are often not able to pay for services themselves, so that there needs to be some cross-subsidization logic, that is a third party such as the state or philanthropic organization is paying for the service.

This is why social innovators often mix grants, donations, or service provision on state regulated quasi-markets with market income. Generally speaking, there is some potential for evolution towards market revenues, but a substantial share of social innovators will continue to operate on such hybrid income or non-market income structures. This means that while types and phases are partly related, the life-cycles stages of social innovators do not always co-evolve with their income types. If the political priority is on creating the greatest impact—and so it should be—non-market social innovators should not be disregarded but provided with tailored financial support that responds to their specific needs.

**“None of the great challenges of our time such as climate change, digitization or an aging society can be mastered through technology alone. Such challenges require [...] social innovations. [...] The High-tech-Forum therefore advises the federal government to develop a strategic approach for stimulating social innovation and to mobilize policy action across policy fields. Social enterprises, that is organizations which create social value through means of entrepreneurship, should be strengthened because they are driving forces of social innovation.”**

— Final report of the Hightech-Forum, commissioned by the German government

## 3 Non-financial support and networks

The support of social innovators does not only need to be multi-pronged with regard to providing different finance in different ways for different types of organizations and different stages. It also needs to provide more substantial non-monetary support than we typically see in financing commercial businesses. In-kind support, in some of the countries we studied, was even seen as more essential to social innovators than financial support. The biggest needs for support lie in four broad areas: (1) knowledge about different types of finance and the opportunities and obligations associated with these, (2) business/organizational model innovation to find a sustainable (if mixed) income model, (3) impact measurement, management and reporting. A fourth and independent area is the build-up of networks with scaling partners from the public sector, the social economy, or the market to diffuse social innovations across systems.

## 4 Developing a holistic perspective on impact

Fostering social innovation is not an end in itself. Instead, it is a means to promote more effective problem solving and prevention for society. This is why it is intricately connected to fostering social impact. Unfortunately, and despite much progress on the side of available tools and frameworks (see for example the Impact Management Project › [impactmanagementproject.com](http://impactmanagementproject.com)) managing for highest impact is still not widely established.

To establish impact as the key decision criterion in organizational management and financing decisions alike, we will need incentives for achieving impact. These should be accompanied by the tailored adaptation of impact criteria and a process of organizational learning in this regard, which is needed because of the newness and great diversity of social innovations. In consequence, impact measurement, management and reporting require continuous exchange between the social innovators and finance providers, and ideally a transparent sharing of experiences made in this collaboration. The legal requirement for all types of organizations to report on their impacts would provide a huge push towards prioritizing impact. From an ecosystems perspective, changing the public sector’s own procurement principles towards “buying social” or “buying for impact” would not only incentivize the impact orientation of those the state buys from, but it would flag the importance of creating impact across society.

# W Financial architecture and policy tools

**A well-crafted financial architecture that employs specific policy tools can help fund social innovation effectively and mobilize private capital.**

In this chapter we aim to explain the tools that are essential within the financial architecture and their functions in reference to social innovations.

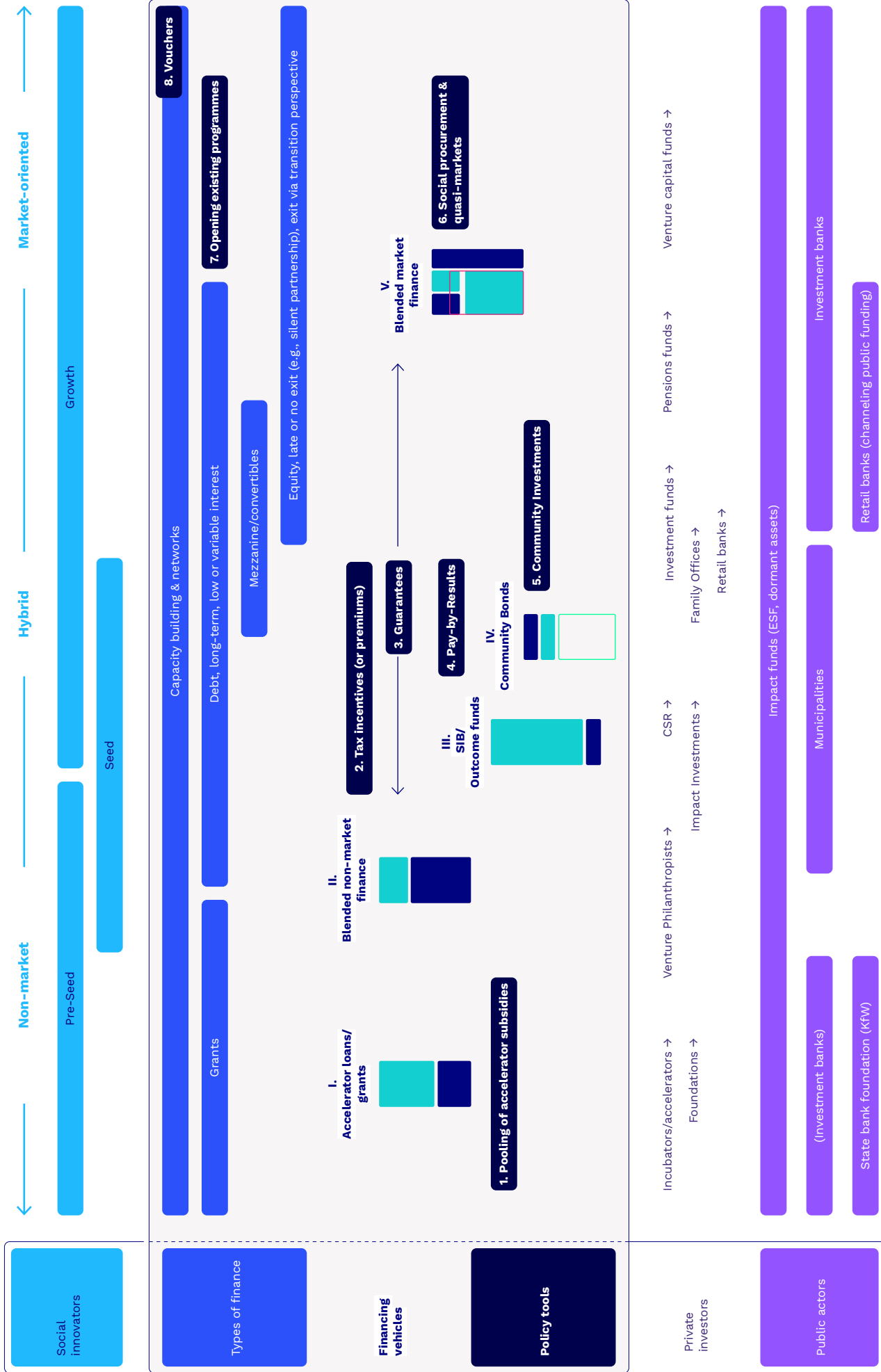
The aim of **Figure 2** is to provide a comprehensive overview of the architecture and to outline how different spheres of action need to be considered in conjunction. For example, the innovation funnel that marked different innovator types and development phases is reimplemented in a different way at the top of the figure. At the bottom of the figure, we highlight the roles played by a variety of private and public actors that can and should co-engage in supporting social innovation. [3] The different types of finance these are able to provide in their co-engagement are also displayed and range from grants to equity.

Eight different policy tools are highlighted and will be explained in more detail below. How these are connected to specific financing vehicles is discussed in **Chapter 5**. Here we only allude to these financing vehicles by numbering and naming them, and by illustrating and locating them via graphic schemes.

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[3] The location of private investors marks their earliest points of potential engagement. They could however engage in the full range of engagement opportunities to their right (marked by the arrow).





**Figure 2** Financing architecture for social innovation

## 1. Pooling of accelerator subsidies:

There is a large number and variety of individual prizes, acceleration programmes and pitch competitions. These stimulate the vibrancy of the social innovation field, but also result in problems. First, such a fragmented landscape produces high friction costs for social innovators, who need to apply over and over again for relatively small amounts of money. Second, acceleration programmes are often designed after the example of commercial incubators and run from 3 months to 1 or 2 years at maximum, which might be insufficient for social innovation ideas to come off the ground and social innovators to get to a proof of concept, for example. Third, any such support typically refers to single projects rather than whole organizations and may thereby block the evolution of more holistic solutions, which typically evolve over time and independent of original project ideas.

Private funders, for example big corporations or private foundations should consider pooling resources, which can be used to provide long-term support to organizations rather than short-term support to projects. The German state bank foundation (KfW Stiftung) could choose to do the same and thereby serve as a role model for private foundations.

Another option for state involvement would be to moderate such a long-term oriented process by defining relevant assessment criteria, ideally together with social innovation actors, for how to channel subsidies and investments into social innovations. It could thereby provide some direction in how to design and govern co-pooled fund structures. Finally, it is quite common that state banks provide non-repayable subsidies for research and development purposes to commercial enterprises. They could engage in similar support for social innovators.

## 2. Tax incentives or premiums for impact:

One reason for a poor mobilization of private capital for social innovators with very high impact potential is that the degree of experimentation and thus the risk of failure is also high, so that funders face the risk of not being able to claim a success. A second reason is that while impactful, some social innovations may not be considered new enough by private funders, who are often interested in signalling their role as vanguards of positive change, which is impossible if the perceived degree of newness is too low. A third reason is that especially individual philanthropists or smaller institutions may not want to channel their investments into a small number of relatively big investments and instead seek diversify their portfolio in favour of a bigger number of smaller investments.

The state could encourage private engagement by offering preferential tax treatment of such investments. Such tax cuts should be linked to impact criteria to help differentiate impactful from less impactful investment types. Instead of tax cuts, the state could choose to pay a premium ex-post, once certain impact criteria are met (see also pay-by-results). By leveraging private finance through substantial public co-investment, the state could level out individual portfolio considerations. Such public co-investment would effectively function like a guarantee and reduce the level of risk that private investors must bear.

### 3. Guarantees:

Another reason for an overall lack of finance for social innovation is that risk-return-impact profiles of investors do not match those of the social innovators who may receive the finance. Risk may refer to potential financial loss, but also to impact risk, that is expected positive effects not materializing, or even time, that is the social innovation taking very long to mature and sustain itself.

The state could issue guarantees to mitigate these problems. This may happen in the literal sense, that is the state takes first loss in case of defaults, or by way of co-investment, for example via state-owned investment banks. Guarantees or guarantee-like structures are relevant to both, blended non-market finance and blended market finance, although there is a different composition of private investors involved. The more commercially viable the options to invest in social innovation become, the more could the first loss function also be taken over by venture philanthropists, foundations or family offices. These would be co-investing with commercially driven investors such as venture capital funds, pension funds, or even retail banks.

### 4. Pay-by-results principle:

A substantial share of the provision of social services, including efforts at problem prevention, happens on highly regulated quasi-markets. They are usually governed by the primacy of cost-efficiency in the provision. This principle is important to remain accountable to tax payers. The downside is there is little room for continuous innovation and almost no room at all for radical innovation.

Social impact bonds or outcomes funds are based on the pay-by-results principle and pursue the idea of attracting private capital to finance such innovation and impact-oriented action. Instead of financing a priori, the state repays private investment plus a premium in case pre-defined impact criteria are achieved, so that the private capital bears the risk of the innovation. Impact criteria are usually pre-defined, but can be adapted, which for example was often the case during the COVID-19 pandemic. The principle serves to distribute risk and to simultaneously promote the impact orientation of involved actors.

## 5. Local community investments:

There is hardly any possibility for citizens to invest in social innovators other than crowd-funding, where the investment often remains limited to the very early phase of a venture. Ways of institutionalizing and extending the ideas underlying crowd-based funding (pooling of resources, risk diversification etc.) are important, not only to extend the available amount of finance but also to strengthen the link between citizens and social innovators, or in fact make citizens co-innovators.

Locally oriented community bonds, for example to support social innovators in a local urban neighbourhood or rural region, would provide a vehicle for place-based innovation. Municipalities could seek to structure such investment opportunities and potentially co-invest. [4]

## 6. Social procurement & building public quasi-market:

Some social innovations will be able to establish themselves as a market product or service that is fully commercially viable. However, many will require a long-term perspective that can only emerge via active state involvement. For example, even debt with low or variable interest and a very long duration will need to be repaid at some point. Equity investments are altogether unlikely, if investors do not have an exit option at all.

The state could engage in two ways to address these challenges. First, market building by the public sector for the mid- to long-term, for instance through implementing an innovation as part of the standard system of social service provision, can help social innovators establish a sustainable and market-oriented income model. This is needed to be able to use debt, equity or mezzanine finance. Second, social procurement is a more universal mechanism the state could apply, which would establish impact and social and ecological criteria as core criteria in public buying decisions. It would not only provide social innovators with new ways of establishing market-based streams of income, but also increase the impact orientation of organizations across societal sectors.

**In addition to the specific types of public funding already mentioned, there are several alternative sources of public finance, which could be used finance social innovations: (1) existing ESF funds of European funds for regional development, (2) dedicated social welfare budgets to promote innovation in (social) service provision, (3) dormant assets, which have been used for public social investments in a number of countries internationally (see a recent policy proposal on using them in Germany › [t1p.de/veeww](https://t1p.de/veeww) [send-ev.de], a legal scoping assessment on its feasibility has recently been completed on behalf of the German government). These funds allow for different sector or geographic focuses, and align with priority areas defined by the sustainable development goals (SDGs).**

## 7. Opening existing programmes:

Not all strategic policy options would require the application of new tools as described above. Germany has a number of established funding schemes to support start-ups such as the KfW preferred-interest loans channelled through retail banks (for example ERP-Gründerkredit StartGeld). However, most of these programmes explicitly exclude organizations with public-benefit orientation from applying for these kinds of support. Besides, the share of social entrepreneurs who use so called EXIST-scholarships for start-up founders appears to be relatively low. [5]

A first and relatively simple measure that policy makers should consider is including non-market social innovators as eligible for established funding programmes. Second and more importantly, the public sector should consider reforming assessment criteria used to make funding decisions to better reflect the complex properties and requirements of social innovators. One example is that success in crowd-funding campaigns [6] should be considered one element of a proof-of-concept, which is not established practice in due diligence checks performed by banks to date. Another area that is in need of reforms is the state aid law, which regulates which organizations may receive funding from state-owned banks and up to which amount. Social enterprises should be explicitly included and the stimulation of social innovation should be established as a key priority.

## 8. Capacity building & networks:

Providing financing alone will not lead to a boost in the social innovation space. Instead, we need coordinated efforts at capacity building and network formation. This applies on both sides, that of the social innovators and that of the potential investors as well as intermediaries. Such capacity and skills building do not only have direct educational benefits, but may prove an effective tool for mitigating financial risk as well as impact risk (impact not materializing or innovations having unintended consequences).

Vouchers for dedicated upskilling, as often used to support commercial innovators, would be an effective instrument. Similar offers should be made to social innovators. However, the skill sets required by social innovators are not only very broad but also specific, for example they lie in the area of impact measurement, which as of now matters much less for commercial entrepreneurs. Due to this circumstance the skill building process for social innovators would benefit from using the expertise of potential match-making organizations (for example impact hubs, accelerators, or social entrepreneurship networks but also more mainstream economic development units or innovation centres), which can establish links between social innovators (or investors) and the providers of training. Besides, the public sector, ideally in collaboration with retail banks, should initiate trainings for investment and bank managers for them to better understand the complex challenges which social innovators face as well as their particular funding needs.

For a market to work, finance providers need to cater to an entire industry or ecosystem, not only individual organizations. A “second layer” of representation of the social innovator scene through meta-organizations or via new institutions could help raise its prominence towards the evolving financing landscape. Furthermore, if state support measures generally addressed the social innovation ecosystem rather than individual organizations, this would promote the evolution and fortification of network structures which are essential for unleashing the collective impact potential of social innovators. It would also position social innovations as a beacon for the economy and society.

[4] The “90/10” solidarity funds in France build on a similar logic but channel employee savings and commercial investment without explicit involvement of public finance, which is why they are not treated in detail here. See: [https://www.finansoL.org/\\_dwl/Study-On-2090-10-20Funds-20FinansoL.pdf](https://www.finansoL.org/_dwl/Study-On-2090-10-20Funds-20FinansoL.pdf)

[5] See: <https://dserver.bundestag.de/btd/18/109/1810907.pdf>

[6] For example, 13,6% of social entrepreneurs use crowdfunding according to DSEM 2020/21.

# V Financing vehicles

**Five different financing vehicles are associated with the policy tools outlined before. These vehicles have been applied in different ways in the countries we analyzed for this study. This is why they can serve as best practices for Germany.**

**Figure 3** displays the structure of these financial vehicles, which appeared in the financial architecture only schematic sketches. In the following chapter, we explain what specific characteristics the vehicles have, list in which countries they are being used and showcase how this is being done.

**“The mission of social entrepreneurs is to find new solutions for the common good. They are therefore important drivers of the reinterpretation of the values that constitute the social market economy within a complex and rapidly changing world. To improve their framework conditions the council of advisors suggests developing a social innovation strategy, opening up existing financial instruments and introducing new ones as well as fostering social innovation and social start-up centres.”**

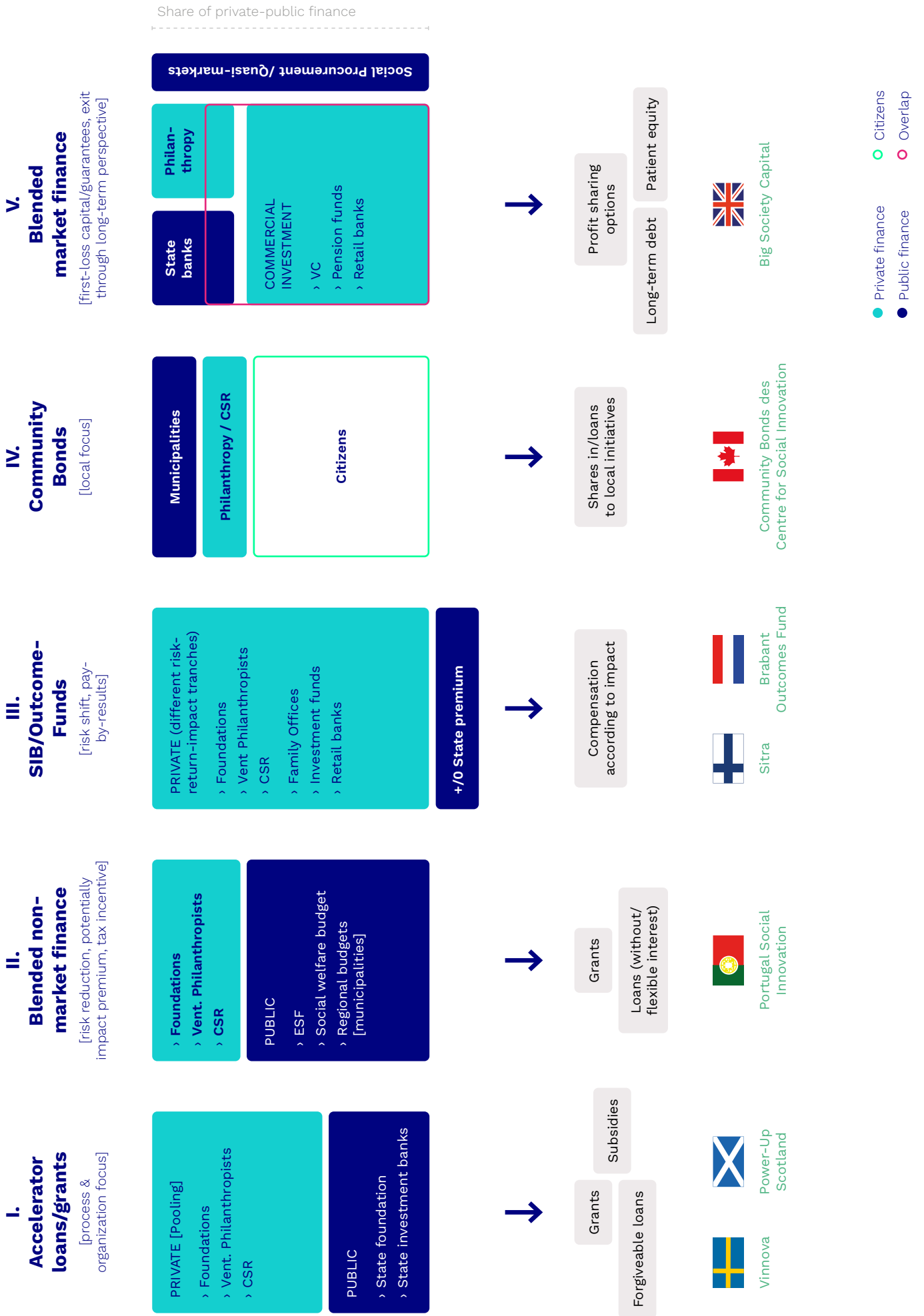


Figure 3 Financial vehicles for social innovation

## I. Accelerator loans/ grants

### Purpose

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- More effective pooling of resources
- Ideally moving from short-term project-oriented to long-term organizational support
- Combining grants or forgivable loans with a process-oriented acceleration programme

### Life-cycle phases

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Especially pre-seed, also seed

### Logic

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The larger share of finance would come from private sources, such as foundations, venture philanthropists or corporates seeking to provide support to social innovators as part of the corporate social responsibility (CSR) initiatives. This could be combined with a substantially smaller share of public funding to form a pool of finance. State foundations such as KfW Stiftung or the state banks, which exist in every German federal state, in analogy to their provision of subsidies for commercial innovation could contribute to the public funding.

### International examples

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#### Vinnova Sweden, Power Up Scotland, Portugal Social Innovation

Power Up Scotland represents a good example of such a multi-sector approach, where among other partners Big Issue Invest co-invested with the University of Edinburgh, while the Scottish state issued guarantees, and Aberdeen Standard Investments provided pro-bono skills building to local social enterprises. Vinnova in Sweden set up a largely grant-based scheme to finance social innovation in civil society organizations. Portugal Social Innovation initiated a dedicated skills-building fund.



## II. Blended non-market finance

### Purpose

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- Risk reduction and increasing appeal for private investors through public co-investment
- Potentially combined with premiums or tax incentives for impact-oriented investing

### Life-cycle phases

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Especially seed

### Logic

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The key principle is to leverage private investment by means of substantial public co-investment, or other incentives such as tax cuts or premiums. Sources for such public investment could be ESF funds, a re-channeling of social welfare budgets for stimulating innovation in social service provision, or regional and municipal budgets to support local innovation.

The types of involved private finance providers would largely mirror that of the accelerator loans/grants. However, in the seed stage of social innovators public investments need to be more substantial. This is especially since the mobilized support should have a long-term orientation and the risk of financial loss would be higher so that risk-return-impact profiles would need to be smoothed out by the public sector. The main types of finance are repayable loans, ideally with flexible interest and long-term option of converting these into equity. In addition, social innovators should be provided with working capital.

### International examples

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#### Portugal Social Innovation

Portugal Social Innovation provides 70% of public leverage to private investments and thereby finances social enterprises and non-profit organizations. The funding is predominantly sourced from ESF sources.

### III. Social Impact Bonds/ Outcome funds

#### Purpose

- Risk shift to private investors, while providing outcomes-based re-payment (plus premium) by the public sector
- Promoting outcome and impact orientation

#### Life-cycle phases

Seed and growth

#### Logic

The basic idea of social impact bonds is to mobilize private finance for promoting innovation, and to outsource public risk. At the same time, SIBs represent a shift in the provision logic from compensating providers and/or investors based on (a) services provided to (b) results achieved. Only when pre-defined impact criteria are met, do investors receive a repayment of their investment, plus a premium. The mobilized investments typically do not go to single organizations but to partnerships of provider, who based on a combination of expertise hope to contribute to more effective problem solving.

Individual local social impact bonds have been criticized for having very high setup and administrative costs, which is why outcomes funds that provide an umbrella to finance several initiatives are becoming the preferred alternative. The range of potential private investors is wide and spans from foundations to retail banks, who will typically have very different individual risk-return-impact profiles and could thus meet the financial requirements of different types of social innovators. A pooling of resources across different risk-return-impact tranches may help lever the overall amount of capital further.

#### International examples

**Brabant Outcomes Fund Netherlands, Portugal Social Innovation, Sitra Finland, local SIB initiatives in many other countries**

The Brabant Outcomes Fund in the Netherlands and Portugal Social Innovation have established smaller scale funds and bonds that grew bottom-up. Because Portugal Social Innovation was not able to pay premiums from ESF funds, the state established tax incentives for private investors. Sitra in Finland instead launched a number of large-scale outcomes funds especially for preventative actions such as lowering the occurrence of Diabetes Type 2 in the Finnish population.

## IV. Community bonds

### Purpose

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— Local, place-based citizen or crowd-investment

### Life-cycle phases

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Seed and growth

### Logic

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Investment opportunities for citizens in social innovation are limited to non-existent. One vehicle for opening such opportunities is the setup of local community bonds that foster place-based investing into social innovations that are located in one's neighbourhood or region. Citizens could for example acquire a share in a building to be acquired by a social enterprise to establish a new cultural hub. A structured fund could also provide loans to several local social innovators. Citizen investments might be leveraged by municipal investments, or by co-investments from local philanthropists or local businesses.

### International examples

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#### Centre for Social Innovation bonds, Canada

The Centre for Social Innovation in Canada has issued a number of such bonds, mainly for asset-based social innovation activities.

## V. Blended market finance

### Purpose

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- Risk reduction for private investors through public first-loss capital or guarantees
- Enabling private exit for equity investments through establishing a long-term perspective

### Life-cycle phases

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Growth

### Logic

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Some social innovators succeed in building models where impact and profits are fully in line. Finding private investors for such models is typically not a major challenge. However, many social innovators, even if ready for growth, offer below market or no financial returns, or contain a high amount of risk both, of financial failure and impact not materializing. Blended finance that taps a variety of financing sources can be effective in making such investments attractive to the widest possible range of investors, spanning as far as pension funds or venture capital funds. Even participation of retail banks and a subsequent offer of individual investments to customers are a viable option.

However, this requires a pooling of finance with different risk-return-impact profiles to get to a balance, which individual investors would not be able to achieve when investing on their own. Guarantee-type or first loss functions could be performed by public investments of state banks or by private philanthropic capital. Such vehicles would enable the provision of long-term debt with flexible interest, mezzanine finance, patient equity or profit-sharing options. Social procurement or public quasi-market building may provide effective exit options for private investors if social innovators are unable to sustain the model through standard market mechanisms.

### International examples

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#### Big Society Capital UK, Canada Fund-of-funds

Big Society Capital UK has been designing variants of such vehicles for a number of years. Canada is in the process of setting up a Fund-of-funds, which is meant to channel investments into a variety of SDG areas.

In addition to the portrayed financing vehicles, **non-monetary measures** of support are essential to the promotion of social innovations.

## Adapting existing and creating new institutions

### Purpose

— Ecosystem building

### Life-cycle phase

Life-cycle phase

### Logic

Ecosystem building requires political ownership of the issues and a national leader, ideally an independent institution that can broker between all involved actors, increase transparency and collaboration in the field, and identify priority areas for action. The EU-Programme for Employment and Social Innovation (EaSI) was built around some of these principles. The foundation of a separate innovation foundation for social innovations, which fosters non-market as well as market-oriented models would be a good opportunity to provide targeted support.

### International examples

#### Le French Impact, EaSI programme of the European Commission, Sitra Finland

Le French Impact is the most prototypical institution performing all these functions, including the early involvement of policy makers in investments to enable legal or institutional changes, if and as they become necessary over time.

#### Some parallels may also be drawn to the UK

where the function is distributed across a variety of actors such as Big Society Capital and its sister organization Good Finance that focuses on knowledge building and transparency, or the national innovation foundation Nesta. Local, federal or national innovation challenges that bring together a variety of stakeholders to identify the most pressing societal problems, offer an experimentation space, and serve to jointly develop potential solutions, can help structuring adequate funding vehicles and channelling the finance. Sitra in Finland has engaged heavily in impact modelling to identify priority areas for investment, for instance by estimating socio-economic costs that can be avoided through investing into innovative approaches to prevent problems from occurring.

**There are many established strategies of how to foster social innovations financially in and outside Europe. Our concrete examples of financing programmes in seven different countries show how social innovation can be promoted in a holistic way.**

All our recommendations are based on our analysis of 23 expert interviews that we conducted in the summer of 2021. We talked to representatives of international organizations, more specifically to the OECD, the European Venture Philanthropy Association (EVPA), the Global Steering Group on Impact Investing (GSG) as well as experts in some countries that are only in a state of emergence of a wider financial support system for social innovation (Italy and Spain). These interviews yielded general recommendations, which were not related to a specific funding programme.

The other interviews focussed on the specific experiences of further countries with their established funding programmes. [7] Here we intend to provide a brief portray of each programme and compare them across a number of dimensions, which we highlighted as essential for arriving at the financial architecture and individual financing vehicles we proposed. **Table 1** provides an overview of the comparison. The relevant dimensions include: target groups, life-cycle stages, types of finance provided, risk management, and impact orientation in the existing programmes. The table and sections are arranged by complexity and multi-facetedness of the instruments applied (in ascending order from left to right).

The overview shows that the principles on which the individual programmes act are very different, but that they also exhibit a significant number of shared traits. Our financial architecture and its corresponding policy tools and financing vehicles are based on a composition of the most promising components we were able to identify.

[7] For Canada we focus on the planned Fund-of-funds, since the community bonds, while a valuable local initiative are not an established scheme. Le French Impact while a major initiative is not a dedicated funding scheme, which is why it is not listed separately in the table.

	Sweden	UK / Scotland	Netherlands	Finland	UK	Portugal	Canada
<b>Programme</b>	Vinnova	Power Up Scotland	Brabant Outcomes Fund	Sitra	Big Society Capital	Portugal Social Innovation	Social Finance Fund
<b>Principle</b>	From base funding to innovation funding	Local social enterprise support	Bottom-up impact evolution	Reform of the welfare state	Building an impact investment market	Designing an ecosystem	SDG-oriented investing
<b>Founded</b>	2001	2018	2018	1967	2012	2014	Planned
<b>Initiator</b>	National government	Local initiative	Regional government	National government	National government	National government	National government
<b>Approx. volume</b>	SEK 55 Mio. (2017-2019, public)	GBP 990000 (2020, public+private)	EUR 1 / 17 Mio. (1. round/planned, public + private)	EUR 64 Mio. (2020, public)	GBP: 115 Mio. (2020, public)	EUR 150 Mio. (2014, public)	CAD 755 Mio. (planned, public + private)
<b>Life-cycle focus</b>	All stages, one vehicle	Pre-seed, seed	Growth	Growth	Growth	All stages, different vehicles	All stages, different vehicles
<b>Target groups</b>	Civil society organizations	Social enterprises	Civil society organizations	Social service providers	Market-oriented social enterprises	From civil society organizations to SMEs	From civil society organizations to SMEs
<b>Types of finance</b>	Grants	Low-interest loans (after successful completion of accelerator & pitch)	Initially classical Social Impact Bond, then outcomes funds	Outcomes fund	Variety of types of finance, market-oriented. Sister organization (Access Foundation) for non-market social enterprises	1. Capacity building programme 2. Pooled grants 3. SIBs 4. Social Innovation Fund (Equity and Debt)	Fund-of-funds, variety of types of finance (market-oriented)
<b>Public funding sources</b>	Rechanneling of civil society funding into innovation funding	State guarantees	Regional government budget	Welfare budget	Mainly dormant assets	ESF, national and municipal funds	Dedicated national funding
<b>Private investors</b>	-	Big Issue Invest, University of Edinburgh, pro-bono consulting by corporates	Initially only foundations, later also banks	Commercial investors	Full range of investors	Full range of investors	Commercial investors
<b>Duration</b>	Variabele	3 years	3-7 years	Variabele	Variabele	Up to 10 years	Tbd
<b>Risk allocation</b>	Government	Government (first-loss)	Private investors	Private investors	Shared risk	Depending on financing vehicle	Shared risk
<b>Impact criteria</b>	Not prominent	Ex-post assessment and reporting	Mutual agreement, adaptable	Pre-defined	Mutual agreement,	Mutual agreement,	Tbd

Table 1 International financing programmes



#### Vinnova, Sweden

### “From base funding to innovation funding”

The programme of the Swedish innovation agency Vinnova represents a shift from a large amount of unconditional base funding to civil society organizations in the context of the Nordic welfare state to a dedicated fund promoting innovative action. Financial support typically comes in the form of grants. There were several initiatives at capacity building to promote innovation and impact orientation in social innovators through dedicated training and other non-financial support, but these elements are not as integrated as in the programmes in many other countries.



#### Power-Up Scotland, UK/Scotland

### “Local social enterprise support”

The Power-Up Scotland programme is strongly focused on social enterprises, typically within a specific local context. After a mentorship phase of 3-4 months start-ups are pitching their progress and may then receive low interest loan funding to put their projects into practice. The state was mainly involved as the provider of first loss guarantees and credibility to the private funders, in particular the well-established social investment fund Big Issue Invest and the University of Edinburgh that chose to invest a share of its substantial financial endowment. The non-financial support provided, especially pro-bono work by Aberdeen Standard Investments and a law firm were regarded, were regarded as almost as important as the provided finance. The prominent local or regional focus was regarded as an asset for engaging all involved stakeholders.



#### Brabant Outcomes Fund, Netherlands

### “Bottom-up impact evolution”

The programme of the Dutch province of Noord-Brabant strongly pursues a bottom-up approach. In a first round of funding the regional government of Noord-Brabant engaged 4 enterprises and 3 investors and channelled € 1 Mio through social impact bond contracts. The second round, which is currently being prepared, aims to provide € 17 Mio. through an outcomes fund that does not only work on pay-by-results principles, but also provides loans and working capital to social innovators. Impact/outcomes criteria, are usually pre-defined, but they may be adapted during the duration of the financing, which was necessary in particular due to the COVID-19 situation. The aim of the involved public and private funding partners is to help the enterprises achieve their impact. The involved actors from public administration also see the fund as a means to implement learnings and establish new decision criteria into public administration, and thus as a tool for institutional change.



#### Sitra, Finland

### “Reform of the welfare state”

The programme is based on the impetus of reforming welfare provision in Finland. Instead of addressing challenges after they occur, Sitra seeks to promote preventative action. The innovation aspect mainly stems from bringing actors together, who would usually not work together, for example private commercial fund managers and coalitions of social service providers. Rather than following the logic of locally embedded impact bonds, Sitra tends to launch tenders with a cross-regional or national remit. Because these are typically sizeable investments and the state is ready to pay a substantial premium when pre-defined impact criteria are met, so as to prevent public welfare expenses in the future, the programme mainly attracts commercial investors who seek near or at market rates of financial return.

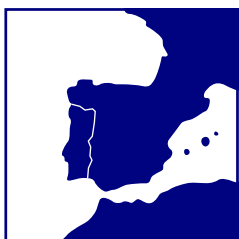




#### Big Society Capital, UK

### “Building an impact investment market”

Big Society Capital was the first programme globally for social innovation, social enterprise and impact that used funds from dormant assets to build up an impact investment market. It channels finance into a wide variety of vehicles that are based on principles of asset pooling and co-investment to engage private investors. The major share of Big Society Capital is dedicated to supporting enterprises that generate a minimum level of market income. However, it also supports non-market social innovators through its sister organization Access Foundation. A remarkable additional component is Good Finance, which focuses on knowledge building, exchange and increasing capacity in the sector. The main goal is to raise awareness among potential investees about financing options as well as the potential opportunities and drawbacks that these options are associated with. Impact goals are typically defined on a case-by-case basis, but through its long years of operation, the programme is moving slowly towards more standardization of impact criteria.



#### Portugal Social Innovation, Portugal

### “Designing an ecosystem”

Portugal Social Innovation is probably the most comprehensive and multi-pronged programme that currently exists. While the Portuguese state initiated it in a top-down approach, it contains elements of flexible adaptation and covers the entire life-cycle and different types of social innovators. There are: a separate skill building programme, a grant programme that tries to lever private philanthropy through a public co-investment share of 70%, and several individual social impact bonds. There is also a social innovation fund that provides debt and makes equity investments into social innovators, whereby the public co-investment is not above a 40% share. The main source of public finance is the ESF, whereby some additional national and municipal funds have been mobilized too. Because ESF funds do not allow for premiums to be paid to investors, the Portuguese state established a 30% tax cut for impact-oriented co-investing. The programme’s objective is not only to finance single organizations, but to support the emergence of a social investment market as well as an ecosystem for social innovations. Impact criteria are essential, but are very much subject to negotiation between the involved parties.



#### Fund-of-Funds, Canada

### “SDG-oriented investing”

The programme in Canada is only in the process of being set up. The Canadian state seeks to make a substantial investment, by which it hopes to leverage even more private capital. Estimates of exact shares and overall magnitude differ, but the projected overall amount is at least CAD 750 Mio. of combined public and private investment. A blended fund-of-funds fed from these sources is then meant to channel finance into more specialized and individual SDG-oriented funds. Some share of the available finance shall also be dedicated to capacity building, networks and advancing investment readiness. While the programme seems to aim to employ a variety of financing vehicles and could thereby provide social innovators with different types of finance, the programme is strongly market-oriented. Impact criteria are likely to be SDG-grounded, but there is no specific information yet.

# WII

## Call to action

Germany and other countries have the opportunity to benefit from the experiences of established funding programmes for social innovation across the globe. **The needs and challenges which social innovations face are clear and there is no perfect response to them. However, any effective solution will need to take the complexities of supporting social innovation seriously.**

We believe the comprehensive financial architecture, policy tools, financing vehicles as well as forms of non-financial support we propose represent a well-rounded package of measures, which are not only realistic but also offer high impact potential. **We hope policy makers will choose to put them into practice in collaboration with a wide variety of stakeholders, who are needed to bring social innovation to fruition.**

# VIII.

## Glossary

### Accelerator

Targeted support programme for start-ups

### Blended Finance

Financing structures that use public finance to leverage private finance

### EaSI

EU-programme for employment and social innovation (EaSI), more information

### First loss

Designates the amount of an investment which is exposed first to any loss suffered on a portfolio of assets

### ESF

European Social Fund, more information › [t1p.de/3zj1](http://t1p.de/3zj1) [ec.europa.eu]

### Mezzanine finance

Hybrid type of finance that combines debt and equity capital

### Dormant assets

Funds held by financial service providers that have not been touched for a certain period of time and where the contact to the original owner has been lost

### Outcome Funds

Fund to finance multiple initiatives based on the pay-by-results principle (see below)

### Pay-by-results

Private capital invested into certain projects is reinvested by the state, if certain pre-defined impact criteria are met

### Pre-seed-phase

First phase in an organization's life-cycle, typically before the organization is formally established

### Seed phase

Second phase in an organization's life-cycle, in which organizations often provide a proof of concept

### Quasi-markets

(Social) service provision that is contracted on a competitive but state-regulated market

### Social Impact Bonds (SIB)

Public-private partnerships to finance organizations or networks with high innovation or impact potential; private investments are only repaid (with a return) if pre-defined impact goals are met

### Social procurement

Public contracts are issued and buying decisions made based on social and ecological instead of cost criteria; colloquially referred to as "buying social" or "buying for impact"

# IX.

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**S E** Social  
Entrepreneurship  
**N D** Netzwerk  
Deutschland