New Philanthropy Capital

NPC perspectives

SROI for funders

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Executive summary

Social Return on Investment (SROI) is a type of economic analysis that provides a framework for measuring social value. The SROI ratio represents the social value created for each £1 invested. Integral to this is the process of listening to stakeholders and understanding and valuing outcomes, either using evidence that a charity has already collected, or forecasting potential future returns.

Should you carry out an SROI?

Putting a financial value on social outcomes can help funders to find out if an organisation is worth investing in, understand the impact that grantees are having, and identify where organisations need help.

For SROI to be really useful, funders have to consider whether they find value expressed in financial terms compelling, and whether their grantees' other stakeholders will find an SROI analysis useful. Many organisations undertake an SROI to attract funding, but it is worth checking first that other potential funders would be interested in the charity's results being presented in this way.

Funders can also apply SROI to themselves, as a way of understanding the value they add to their grantees beyond the money they disburse. Yet as funders' impact can be difficult to quantify, they have to consider to what extent their full value will be captured by an SROI, and may choose instead to use elements of the SROI framework to highlight particular areas of impact.

Increasing the benefits of SROI

Involving stakeholders and doing accurate economic analysis takes time and specialist skills, so funders should be prepared to make a considerable investment for SROI to be done well.

Funders can help to increase the benefits of SROI by investing in better measurement systems, making more of the 'valuing outcomes' element of SROI (understanding the value stakeholders place on different outcomes), and developing more robust financial proxies.

SROI is a useful tool, as long as it is supported by in-depth consultation with stakeholders and good outcomes measurement. Before SROI can achieve its full potential, more investment is needed to help charities to collect evidence of their impact. Funders have a key role to play here, both by funding charities to do more measurement and by encouraging charities to report on their outcomes.

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1. Introduction

Social Return on Investment (SROI) is a framework for measuring social value. Often name-checked, not yet widely understood, SROI has attracted a lot of attention recently, particularly in the third sector. These days it seems any conversation about results measurement inevitably turns to SROI, not least because its implications of value for money and 'social return' resonate with the rhetoric of the new government.[1] Some charities see SROI as the answer to all of their measurement problems—a way of demonstrating the value of what they do in the financial terms they think funders will understand. Others in the sector see SROI simply as an expensive fundraising tool that misses the real point of what charities do. To many charities and funders, what is actually involved in an SROI analysis and what it can be used for is still a bit of a mystery.

As an organisation with nine years' experience in the field of charity effectiveness, New Philanthropy Capital (NPC) has been asked several times for its perspective on SROI and this has prompted us to write this position paper.[2] The paper has been written specifically for funders, and complements an earlier paper written for a wider audience.[3] In it, we seek to provide an informed, independent, pro-measurement voice within the debate, and to offer a starting point for a more nuanced discussion about how and when SROI is best used.

A useful tool

NPC believes that SROI has the potential to be an incredibly useful tool for funders and charities in understanding and increasing charity effectiveness. However, it is held back by the low levels of evidence of results in the charity sector. This lack of evidence is particularly acute for charities who do a lot of campaigning, or whose outcomes are largely subjective, such as improvements in well-being. SROI is an approach that demands evidence—it can help charities identify where more evidence is needed, but it does not tell charities how to collect this evidence. SROI will not reach its full potential until there is more investment in improving the evidence base of the sector.

Understandably, in the current funding environment charities want numbers fast. The cuts, when they come, are likely to be quick and deep. Charities want to demonstrate that they are a good investment for any money left over. But for an organisation without a history of collecting data on its effectiveness, SROI is not going to be a shortcut to the level of evidence required by HM Treasury—it will be a lengthier process requiring input from a range of stakeholders from beneficiaries to funders.

More than a final financial ratio

NPC also believes that the potential benefits of SROI as a management tool are not being exploited enough. SROI is often viewed as being all about the final financial ratio, that is the social value created per £1 invested. This attracts scepticism and criticism, and means many of its benefits are overlooked. SROI is a process of understanding and valuing impact, and should be used by funders to understand where their impact and that of their grantees is greatest and how they could improve what they do. SROI does not have to be seen as an 'all or nothing' approach; charities and funders should use those elements of SROI that are most useful to running their organisations.

This paper sets out our position on how and when SROI is most useful, based on our experience of working with funders and charities and on our understanding of SROI in principle

[1] See www.hm-treasury.gov.uk/spend_index.htm. NPC is also involved in two projects to help the UK and Scottish governments support the development of a standard approach to SROI.
[2] The production of this paper is supported by the Measuring Social Value project and NPC's core funds.
[3] Heady, L. (2010) *Social Return on Investment position paper*, New Philanthropy Capital.

and practice. We discuss what we see as the defining characteristics of SROI, and seek to clarify and set straight some common misunderstandings.

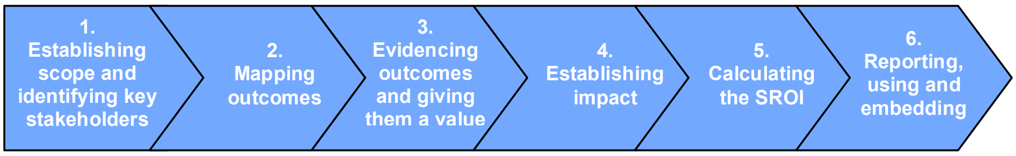
2. What is SROI?

SROI is a type of economic analysis rooted in cost-benefit analysis.[1] The six stages of SROI are outlined in Figure 1, and more detail is given in Appendix B. An example is given in Box 1. The analysis results in a financial value being put on a charity's results, while allowing the charity to understand their key outcomes and involve stakeholders along the way. In practical terms, this allows charities to add together the values of all of their outcomes and to compare the total value created for stakeholders to the money required to achieve those results. This is summed up in the SROI ratio, usually expressed as 'for every pound spent, Charity A creates Y pounds of social value'.

But what does it mean for a charity to create social value? One way of thinking about it is to ask whether the stakeholders would rather receive money directly or receive whatever service it is that the charity offers. For example, giving £100 to a lonely pensioner might improve their life in the very short term; they could use the money to pay for services or buy goods or might just appreciate the extra financial security it gives them. But giving £100 to a charity that runs social activities for pensioners might help that person to form and maintain lasting friendships. Some of the older people with whom the charity works feel that the 'social value' that they receive is far in excess of £100. The goal of SROI is to *quantify* this value—to say by *how much* it exceeds the financial inputs (if, indeed, it *does* exceed them).

This is just one way of thinking about SROI, but for NPC it is the way that best encapsulates how creating value relates to the choices people make when they are giving money away. By putting outcomes in financial terms we see whether particular activities are worth the money that we spend on them, from the perspective of the stakeholders.

Figure 1: The six stages of SROI



Some critics of SROI believe that putting a financial value on what charities do misses the point. You lose so much if you think of charities in purely financial terms. However SROI is as much a process of listening to stakeholders, understanding what outcomes are most important and how they are valued, as it is about expressing value in financial terms. SROI should never be the only way to look at what a charity achieves,[2] but we also think that putting a financial value on social outcomes makes it easier to prove that they are worth investing in. For example, we all know that the environment is important. But it was not until environmental economists managed to value the environment, and compared this value to the costs of protecting it, that governments were motivated to act to combat global warming.

[1] This view stems from NPC's background in economic analysis. SROI could equally be viewed as a type of accountancy and shares much with the social accounting tradition.

[2] NPC assesses the effectiveness of organisations on six elements: activities, results, leadership, people and resources, finances, and ambition. For more information, see *The little blue book*: www.philanthropycapital.org/publications/improving_the_sector/charity_analysis/Little_blue_book.aspx.

Box 1: Measuring the value of older people volunteering

Here, we set out an example of the SROI process. The stages correspond to the six stages of SROI outlined in Figure 1 and Appendix B.

Stages 1 and 2: Identifying stakeholders and mapping outcomes

A charity that provides volunteering opportunities for older people is embarking on an SROI. It starts by speaking to the older people who volunteer, people who donate money and those who benefit from the volunteering—those 'key stakeholders' who it thinks will be helpful in identifying what value it creates. After consulting these stakeholders to understand the impact of the charity, it creates an impact map detailing what goes into running its services (the 'inputs'—staff time, rent etc.), and the benefits for the different stakeholders (the 'outcomes'). It decides at this stage to focus on the older people who volunteer and the Primary Care Trust (PCT). Following the principles of SROI, the charity involves stakeholders in considering which outcomes are material and acknowledging negative as well as positive changes.

For the older people who volunteer, the main input is time. The output is the number of hours spent volunteering. Outcomes are more interesting—many volunteers remark how much happier they feel and mention the friends they have made. Some report improved physical fitness, particularly those participating in activities such as gardening. One older woman mentioned that she is no longer depressed since she became a volunteer. The PCT is interested in preventative care for older people, and funds the charity because it sees volunteering as a good way to reduce depression and improve physical health. The charity then analyses which outcomes are different and which are part of a chain of events. For example, improved physical health is part of a chain of events that leads to improved fitness so these outcomes must be considered together.

The charity collects some data to corroborate these outcomes. It gives a questionnaire to volunteers to assess their general levels of well-being when they join the programme, and every subsequent year. Initial results suggest improvements in well-being, particularly in relation to friends and community. A local doctor provides objective evidence that her patients show improvements in their mental and physical health after becoming volunteers.

Putting some numbers on these inputs, outputs and outcomes is the next stage. In terms of inputs, the cost per volunteer is low, at around £150 per volunteer a year. The charity decides not to value volunteer time as an input. Outputs are also relatively easy to track—the charity's monitoring data indicates that its 200 volunteers devote on average 300 hours of their time a year.

Stages 3 and 4: Evidencing outcomes and establishing impact

Outcomes are trickier. The charity wants to use the SROI analysis to increase the amount of money it, and similar projects, get from the local PCT. So, ideally, the charity would like a robust 'willingness to pay' study (see **Error! Reference source not found.**) that gives improvements to older people's well-being a financial value from a stakeholder perspective. In the absence of this, it goes back to the local doctor who mentioned the health improvements in her patients and asks her some further questions. From this conversation, the charity is able to estimate conservatively that, for its volunteers, hospital overnight stays have reduced by a third and use of Accident and Emergency departments by almost a quarter. It also estimates that physiotherapy and occupational therapy appointments have reduced by 10%. The charity is sure to ask the doctor what she thinks would have happened if her patients had not been volunteering.

Stage 5: Calculating the SROI

All this adds up—using data on the rates of all of these for older people in its local areas, and costs taken from local NHS data, the charity estimates a total saving of £48,000 over the past year. Comparing this to its total costs of £30,000, it calculates a social return on investment of £1.60, just considering these benefits. It also tests some of the main assumptions in the model. This is essentially a valuation from the perspective of the PCT.

Stage 6: Reporting, using and embedding

The charity writes a report on its SROI, which it uses to secure longer-term funding from the PCT. But the charity is also conscious that improvements in well-being, one of the main elements of its theory of change, have not been valued for the older volunteers, and so plans to do a small willingness to pay survey for next year's SROI. The charity hopes that being more transparent and accountable to its stakeholders will improve the quality of its service.

Focused on stakeholder perspectives

SROI is not just economic analysis. Before you get to the number crunching, first you need to establish what to measure and how to value what you measure. This process is based on stakeholder perspectives, as Box 2 discusses. (Box 3 sets out other types of economic analysis.)

Box 2: Is SROI just another name for cost-benefit analysis?

To an economist, SROI looks a lot like cost-benefit analysis. However, cost-benefit analysis refers to a very broad approach—comparing the costs of some particular action with its benefits, and expressing both costs and benefits in financial terms. SROI can be seen as a particular approach to cost-benefit analysis with an emphasis on stakeholder involvement. As outlined in the principles of SROI (see Appendix B), SROI explicitly casts the net very widely, involving stakeholders at every stage, from deciding what indicators to use to putting financial values on outcomes.

Cost-benefit statements and SROI statements look exactly the same ('for every pound spent, Charity A creates Y pounds of social value') and so an interested stakeholder would have to look at the process of the calculation to understand whether it really was a statement of SROI.

Understanding the benefits to a wide range of stakeholders is a standard part of cost-benefit analysis as practised by the government and other agencies. However, it is not standard to involve stakeholders to the same extent as in SROI. In principle, this could make a big difference. For example, consider the decision about whether to close a rural post office. A standard cost-benefit analysis might conclude that the costs of running the post office outweigh the benefits in terms of sales generated and may miss potential benefits to local residents, because they have not been consulted during the analysis. But an SROI might conclude the opposite, as the value to an older person of having a regular point of contact in the community is taken into account.

Guided by principles

SROI is based on seven principles: involve stakeholders; understand what changes; value the things that matter; only include what is material; do not over claim; be transparent; and verify the result. These principles underpin how SROI should be applied, and following them is critical to completing a good SROI. (A fuller explanation of the principles is given in Appendix B.) Adhering to these principles is key to the credibility of SROI. Indeed, almost all of the problems with the interpretation and use of SROI stem from not following the principles properly.

Based on past or future return

SROI analysis can be done using evidence that a charity has already collected or to forecast potential future returns. In the former case, the SROI represents value that a charity has already delivered. In the latter case, the forecast could be based on evidence from another project or on historical evidence from the charity. Forecast SROIs are becoming more common as a result of the lack of outcomes data in the charity sector. Any forecast SROI should be considered alongside other organisational information that would be likely to affect its future impact.

Box 3: Other types of economic analysis

Cost-benefit analysis is an approach to assessing the case for a particular project or course of action by weighing up the total expected costs against the total expected benefits. Both costs and benefits are expressed in financial terms. 'For every £1 invested in Columba 1400 [a social enterprise], £2.50 of social value is created' is an example of a cost-benefit statement. SROI can be thought of as a special type of cost-benefit analysis where there is an explicit attempt to value costs and benefits from the perspective of stakeholders who are often excluded from investment decisions (see Box 1 for more details).

Cost-effectiveness analysis is similar to cost-benefit analysis—results are compared to the money required to achieve them—except that results are not given a financial value. 'For £45, Beatbullying helps a child learn how to ignore playground bullies' is an example of a cost-effectiveness statement. This highlights an important point: quantifying outcomes is not the same as giving them a financial value.

Break-even analysis shows how successful a charity would have to be in order for the social value of its work to outweigh its costs. For example, take a charity helping young people to find employment. Let's say that young people value employment at £10,000 and it costs £1,000 for every person the charity works with. This means the charity will only have to be successful 10% of the time in order to break even.

3. Common misconceptions about SROI

The SROI ratio represents actual financial returns

The 'SROI ratio' is the final point of an SROI analysis that represents the *social value* created for each £1 invested. This is how much stakeholders (including beneficiaries, the government, the employees of the charity) value the service. It does not represent an actual financial return.

Some of the value a stakeholder puts on a service will be based on how it improves their emotional, social and physical well-being (eg, feeling less lonely or in better health). Some of it will be based on cost-savings related to using fewer services (eg, improvements to a patient's mental health mean he or she is less reliant on healthcare), and some of it will be based on expectations of higher income (eg, the beneficiary earning a higher wage or reducing their debt or the government collecting more tax).

Lower spending on services and higher income can represent actual financial returns.[1] Improved emotional, social and physical well-being are valued very highly by stakeholders, and so this value is put into financial terms for the purpose of the SROI calculation. However, they do not represent real cash savings.

It is also important to note that a financial return to one stakeholder may be a financial loss to another stakeholder. For example, increasing access to benefits *increases* the income of the person receiving benefits, but *increases* the cost to the taxpayer. It is standard in cost-benefit analysis not to include cash transfers of this kind. However, it is often interesting to highlight the competing interests of different stakeholders, even if they cancel each other out.

SROI is a way of measuring outcomes

Although the process of carrying out an SROI requires the measurement of outcomes, it does not say how these outcomes should be measured. Its principles state that outcomes should be measured in ways that are meaningful to stakeholders, but what is meaningful will obviously vary from stakeholder to stakeholder. Suppose a charity you support is interested in measuring what difference it makes to a child's self-esteem. What questions should it ask? To whom should it ask these questions? When should it ask these questions? SROI does not provide any guidance here; the charity would need to use a tool like NPC's well-being questionnaire.[2]

The need for better measurement in the charity sector, particularly for subjective outcomes is a serious one. It is a fact of life that things that are easier to measure are more likely to be counted. SROI goes some way to addressing this tendency by insisting that all material outcomes are considered. In practice, however, the practicalities mean that outcomes for which there are not established methods for measurement or valuation are likely to get less prominence. For example, when NPC looked at the costs and benefits of providing services to disabled children and their families, the calculated return was negative or close to zero because there was no way of measuring and valuing the human and emotional benefits of reducing parental stress within the budget available.[3]

That SROI does not solve the measurement problem is not a criticism—SROI is not intended to prescribe measurement techniques. However, good measurement is crucial to a good SROI, and more investment in helping charities to measure is needed before SROI can reach its full potential.

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[1] In reality, it is very difficult to translate lower use of services into cashable savings—if crime goes down in an area it is more likely that police time will be deployed elsewhere, rather than less being spent on the police.
[2] See www.philanthropycapital.org/publications/improving_the_sector/well-being/ for more details.
[3] Copps, C. and Heady, L. (2007) *What price an ordinary life?* New Philanthropy Capital.

4. What can SROI tell me about my grantees?

Demonstrating the value that an organisation creates for its stakeholders can help a funder to understand the impact of its grantees, and also to identify where an organisation might need help. How useful an SROI is for you as a funder will depend on the following:

- Do you find value expressed in financial terms compelling?
- Will your grantees' other stakeholders find an SROI analysis useful?
- Do your grantees have the necessary ingredients to do an SROI?
- Will the SROIs of your grantees be comparable?

The following helps funders think through these questions in order to determine how useful and accurate an SROI analysis would be for them.

Do you find value expressed in financial terms compelling?

SROI presents the social value a charity creates in financial terms by attaching financial proxies to their outcomes (see Box 4). **Outcomes have different values depending on the perspective of the stakeholder.** For example, a child may value having fun more than learning maths, but from the perspective of society it is important that children grow up with the necessary skills to get a good job.

Because of this difference in values between stakeholders, some funders may wish to simply compare the outcomes achieved with the cost of achieving them. For example, *'25 more young people with sustained jobs and 30 fewer young people committing crime for £100,000.'* This would allow funders to consider for themselves what value they would place on each outcome. This kind of analysis is known as cost-effectiveness analysis (see **Error! Reference source not found.**) and can be carried out using stakeholders to define outcomes in the same way that SROI does.

Will your grantees' other stakeholders find an SROI analysis useful?

In our experience, the most common reason for charities to undertake an SROI is to attract funding. If you are funding a charity to undertake an SROI for this reason, **it is worth checking that other potential funders would be interested in the charity's results being presented in this way**. SROI is often most powerful where a charity delivers outcomes that fall across traditional policy boundaries (for example, mental health and employment), or delivers outcomes beyond those it is contracted to deliver. SROI is a good way to highlight these benefits if they are not already being valued by funders. However, there must be a client-driven perspective, not only to ensure that the time and cost are worthwhile, but also to maintain enthusiasm throughout the project.

A funder should consider whether SROI would be a useful way of improving a charity's capacity for understanding its own impact. SROI can, and should, be used as a management tool, to help staff to understand the difference they are making and improve their services. To ensure this does happen, it is important to consider whether the organisational culture would allow SROI to be embedded into everyday practice. It is worth reiterating that a funder should not think that SROI will solve a charity's measurement problems on its own.

SROI does not tell you how to measure outcomes, and so the charity may need additional support in this area.

It is also worth checking whether the beneficiaries of the charity would find an SROI useful. Given the principles of SROI, it follows that **the findings of an SROI analysis should be interesting and relevant to beneficiaries**. Going through the SROI process in a transparent way makes an organisation more accountable to those it is trying to help.

Box 4: Valuing outcomes and financial proxies

Often, it is not easy to assess directly the value various stakeholders place on outcomes: stakeholders' views may change depending on how recently the outcome was achieved; beneficiaries may have communication difficulties; or a charity may be too far removed from them to ask their opinion. Hence SROI makes frequent use of financial proxies. These are estimates of value based on anything from how much that outcome would save the taxpayer (eg, how much reducing crime saves the police service) to how much a stakeholder would be willing to pay for a similar service (eg, a charity that hosts friendship circles for disabled people might look at the cost of professional party organisers).

Here, we summarise the most common methods for finding financial proxies to use in an SROI analysis. Financial proxies may be constructed using one or a combination of these approaches. The right proxy depends on the audience and who will be using the SROI.

Willingness to pay (WTP)

The amount that consumers are willing to pay for a little more of a service or an outcome shows how much consumers value getting that little bit more of the service or outcome. The amount consumers are willing to pay depends to a large extent on the levels of income available to them, so valuations are usually obtained by averaging across income groups. WTP values can be found through surveys or by observing people's behaviour when confronted with different prices. The government uses WTP in its values for time, health outcomes and environmental impacts.

Service costs

These values are based on how much the government pays in service costs. The value of an outcome corresponds to the service costs saved by the government, for example,, hospital bed spaces saved due to better health.

Market value

This is the cost of services on the open market, for example,, the price of a flat or a team-building course. These costs are often lower than willingness to pay estimates as competition normally drives prices down below what people are willing to pay.

Do your grantees have the necessary ingredients to do an SROI?

The first ingredient needed for an SROI is the ability of the charity to **engage its stakeholders**. If the charity's beneficiaries are very far removed from the charity (as is the case for many campaigning charities) or they have serious communication problems, then the charity may struggle to involve these stakeholders throughout the necessary steps. Asking vulnerable beneficiaries to assess their 'willingness to pay' (see **Error! Reference source not found.**) might not be appropriate.

The second ingredient needed is **quantitative data** to back up the charity's theory of change. The data requirements to assess past social return are quite demanding. Ideally, the charity needs quantitative data on inputs, outputs and outcomes, which is collected systematically. This data should reflect the priorities of stakeholders. The charity should also have data that gives some idea of 'what would have happened anyway', allowing for the fact that some change would have been achieved without the charity's help.

The final ingredient is whether the charity has **outcomes that can easily be given financial values**. It is fairly straightforward to give financial values to outcomes that can be linked to cost savings.[1] For example, if the outcome is reduced offending, then criminal justice system costs are saved. Outcomes that generate income can also usually be given a financial value. For example, if the outcome is someone getting a job, then income is created for the individual and the state. But it is much harder to give other outcomes, particularly more subjective outcomes such as an elderly person feeling safer, a financial value. The current state of research means that many of these outcomes are under valued, or not valued at all.

The better the ingredients of the SROI, the more accurate the analysis will be. In practice, charities with good data and outcomes that are easy to put in financial terms can produce analysis that help them to understand where they are creating the most value and where they can improve. If the SROI is being performed for an external audience, accuracy will need to be higher than for an internal audience.

If all of the grantees in a particular funding programme have the necessary ingredients for SROI then **funders can add up the individual SROIs to get a feeling for the overall social return of a grants programme.** This is one of the major benefits of expressing all outcomes in the same terms. The experience of funders in attempting to do this kind of analysis is that it works best with strategic grants for concrete, long-term projects with well-defined and simple objectives.

However, NPC has never seen an SROI analysis that is so accurate that it could be used for comparison between charities.

Will the SROIs of your grantees be comparable?

There are three main sources of error in the final SROI ratio: error from not including all important outcomes; error from measuring outcomes; and error from placing financial values on those outcomes. Even in the best case scenario, these errors introduce so much uncertainty into the calculation that **any funder should be very wary of using SROI ratios to compare charities**. However, SROI is more than this final ratio and funders can still use SROI analyses to compare different charities' most important outcomes and how they are viewed by their stakeholders.

If two charities are measuring their outcomes in the same way and using the same financial proxies for these outcomes then a comparison of ratios may be more meaningful. Even so, any difference would have to be large before it could be considered to point towards a genuine difference in social value created. Also how and what a charity measures in an SROI is determined by stakeholders, so it might be considered a bit of a coincidence if two charities did end up measuring the same outcomes in the same way. Funders may wish to consider relaxing some of the stakeholder requirements, or getting the stakeholders of different charities together to think about how outcomes should be measured, if they wanted to ensure that different charities are measuring and valuing the same outcomes in the same ways.

If grantees are measuring their outcomes in the same way, this will also make it easier for them to share information with each other and learn from each other's experiences.

[1] The difference between marginal and unit costs may be difficult to separate. For more details see: Cabinet Office (2009) *A Guide to Social Return on Investment*.

Any decisions made on the basis of SROIs should be rigorously tested using a sensitivity analysis to ensure that funders are aware of which assumptions might be driving their results.

5. What can SROI tell me about myself?

We normally think about SROIs being done by charities, but they can also be done by funders. Many funders are interested in understanding the value they add for their grantees, beyond the money they disburse. There is a growing body of evidence to suggest that the way a funder funds has a direct impact on the effectiveness of its grantees. Funders can use SROI in much the same way as their grantees, to understand where they are having the most impact and how this impact is valued by its stakeholders from grantees, to beneficiaries of grantees and potential donors.

Funders are often one step removed from the final beneficiaries of their money and their impact on their grantees can be difficult to quantify. This means that funders that wish to do an SROI will have to consider to what extent their full value will be accurately captured by a standard SROI. They may instead consider using elements of the framework to highlight particular areas of their impact. For example:

- A funder could use the first two stages of SROI, identifying stakeholders and mapping outcomes, to clarify its theory of change, regardless of whether a full SROI analysis is then completed. Any funder should have a clear theory of change, and ideally one that considers stakeholders' perspectives. A clear theory of change is the best way to start thinking about how to measure impact.
- A funder could also use the first two stages of SROI to work out what aspects of its work to measure. As discussed above, SROI is not, however, going to help funders with the 'how to measure' question.
- Funders can use steps of SROI to conduct alternative forms of economic analysis (see Box 3). A funder without outcomes that can easily be given financial values but which can be quantified—for example, increased partnership working—could still conduct a cost-effectiveness analysis. Funders without outcomes that can be easily valued or quantified —for example, a funder that lobbies government on behalf of its grantees—can still present a qualitative description of their impact alongside their costs.
- Funders that have several stakeholders or that deliver several material outcomes that can easily be given financial values, can use the SROI principle of valuing what matters (see Appendix B) to compare how various stakeholders value different outcomes. This could help the funder decide which outcomes to concentrate on if there was the possibility of expanding a particular funding approach or if some funding streams had to be cut.

6. The cost of conducting an SROI

Involving stakeholders and conducting accurate economic analysis takes time and specialist skills. This makes SROI resource intensive (although the same could be said for other forms of evaluation or financial accounting). As REDF, the US venture philanthropy organisation that developed the original approach to SROI, noted in a recent article: *'Current approaches to SROI continue to be people- and expertise-dependent.'*[1]

It is difficult to come up with a general estimate for how much an SROI costs but some important factors influencing price include:

- the scope of the SROI analysis;
- the skills of the staff within the charity or funder;
- whether the charity or funder does the analysis itself or hires an external consultant;
- data availability on outcomes and benchmarks;
- current measurement processes;
- timescale over which outcomes are measured; and
- the audience for the analysis.

For SROI to be done well, funders should prepared to make a considerable investment over a long time period, possibly several years. However the time investment into SROI must stand in proportion to the project investment. It will take time for a charity or funder to develop a measurement system that truly captures its social impact in a robust way. The organisation undertaking the SROI must be willing to undertake intensive interaction with stakeholders and incorporate any lessons from the project.

The most important consideration is how to use SROI in such a way that it maximises the benefit for the organisation. SROI can help a charity or funder better understand its impact, its cost base and the value it delivers. A charity or funder that understands these things is in a better position to improve its services and make a strong case to its stakeholders.

If the cost of a complete SROI is prohibitive then charities or funders may wish to explore selecting those elements that they find most useful (as discussed in the previous section).

[1] Gair, C. (2009), *SROI Act II: A Call to Action for Next Generation SROI*, REDF.

7. Areas for development

The improvements set out in this section would increase the benefits of SROI, increase its credibility, and reduce its costs, thus making SROI a practical option for more charities.

Improving measurement systems

Charities need better measurement systems to make the most of SROI. The SROI framework relies on evidence of charities' results, and often the analysis has to use whatever evidence is available. Frequently, NPC sees SROI analyses where the evidence used is poor quality. One of the common criticisms of SROI is '*garbage in, garbage out*.'

Better measurement systems would help charities to collect quantitative data more easily, and the data would be better quality. This would mean an SROI was more useful, more credible to an external audience, and cheaper to do. This is particularly the case for subjective outcomes. It is still the case that the highest SROI ratios come from services that reduce crime or increase employment—two outcomes that are very easy to count and have a long history of being valued financially. If we are to truly prove the full value of what charities can deliver we need to get better at measuring what has often been viewed as immeasurable; from better family relationships to increased confidence or decreased loneliness.

More broadly, NPC sees better evidence of charities' results as key to making the charity sector more effective. Improving measurement is difficult, but NPC believes that this is necessary in order to understand and increase the value of charities' work.

Using SROI as an organisational tool

NPC has heard many examples where SROI has been used to help a charity think more about its impact and measure the outcomes of its work. This is a great advert for capturing evidence of outcomes but it does not make the case for the third stage of SROI: assigning financial values to outcomes. Often the final expression of financial value is seen as little more than a fundraising tool.

NPC believes that more use could be made of the 'valuing outcomes' element of SROI, by both charities and funders. For example, such analysis could be used to look at the trade-off between doing intense work with just a few people, compared to more 'light touch' work with more people. Understanding the relative value their stakeholders place on different outcomes should help charities to decide which activities to scale up and which should be lower priority. In order for this to happen there need to be more examples of charities or funders that have found SROI useful for making internal decisions.

Some funders are currently using SROI, either for themselves or for their grantees, and are finding it a useful addition to their existing funding processes. However, its use by funders is far from widespread. Even funders who are very keen on outcomes measurement do not necessarily see the benefits of SROI. NPC would like to work with funders to discover when SROI would and would not be useful for them.

Developing robust financial proxies

NPC believes a standard approach to using financial proxies is needed,[1] and there needs to be more development of financial proxies for subjective outcomes. This would increase the

[1] By this, we mean a standard approach to using and combining proxies calculated in different ways, rather than calculating financial proxies in the same way. This standard approach should account for the fact that different proxies will be appropriate for different audiences and in different contexts.

credibility of SROI and its comparability across organisations. See **Error! Reference source not found.** for more details on financial proxies.

The Measuring Social Value project, funded by the Cabinet Office,[1] and the SROI Project, funded by the Scottish government,[2] are working jointly to develop a database of indicators and financial proxies. This database will assess the quality of various financial proxies. It should help to make SROI more credible as it will be clear where financial proxies have come from and how reliable they are. It should also make SROI cheaper as less time would be needed to research potential proxies.

To complement this database, NPC believes that more research should be done to improve and develop new financial proxies used for subjective outcomes. This would mean that charities could accurately value all of the outcomes of their work. However, as previously acknowledged, valuing subjective outcomes is incredibly difficult, and this would require significant investment.

SROI analyses often find returns of 100% or more. This is primarily because many charitable activities are genuinely valuable and taking a multi-stakeholder approach will increase the calculated level of return. However, such high returns can give rise to scepticism and so a clear, consistent and transparent use of proxies, plus some realism that returns can sometimes be negative, is essential for credibility.

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[1] www.cabinetoffice.gov.uk/third_sector/research_and_statistics/measuring_social_value.aspx
[2] www.sroiproject.org.uk/

Conclusion

NPC has long sought to increase the level and quality of evidence in the charity sector, and we have experience of doing several types of economic analysis (see Appendix A). We believe that SROI has an important role to play in encouraging the collection and analysis of evidence. SROI's emphasis on stakeholder perspectives resonates with NPC's belief that charities should be judged by what they achieve for their beneficiaries.

SROI is useful to funders that want to express the impact of their grantees in financial terms, to help build the capacity of grantees to think about their impact, or to think about how they increase the impact of their grantees beyond disbursing grants. However, SROI needs to be supported by good outcomes measurement and in-depth consultation with stakeholders. The cost of an SROI will depend upon whether a charity already does those things, or whether even with effort, the nature of its work allows it to gather sufficient data. If a charity does not have these things, SROI may not be appropriate. SROI is also not appropriate for comparing the effectiveness of a number of organisations because of the wide range of approaches currently used to create SROI ratios.

In order for SROI to achieve its full potential, first we need to invest in helping charities to collect evidence of their impact. This is particularly urgent in the case of measuring subjective outcomes. Funders have a key role in improving measurement in the charity sector, both by funding charities to do more of it and by encouraging charities to report on their outcomes.

To increase the potential for SROI to improve organisations, the expression of outcomes in terms of financial values should be used to gain a deeper understanding of the value of each element of a charity's work. More work needs to be done with funders to understand the most effective ways for them to use SROI.

To increase the credibility of SROI, the use of financial proxies should be standardised, and more research is required into proxies for subjective outcomes.

Each of the elements of SROI have something to offer charities and funders in terms of understanding their value. Depending on the data and resources available, a complete SROI analysis will not be suitable for everyone. But NPC believes that funders and charities should take advantage of those elements of SROI that are most useful to them. Whatever approach is taken, organisations should adhere to the principles of SROI to ensure the credibility of any analysis they do.

For more information on NPC and SROI, please contact Lucy Heady on 020 7785 6334 or lheady@philanthropycapital.org.

Appendix A: NPC and economic analysis

NPC has experience of doing several types of economic analysis to understand the value of charities' work. Here are just a few examples:

Valuing potential: An SROI analysis of Columba 1400 **(2008)**

Columba 1400 is a social enterprise that works to make the most of young people's potential by running leadership academies for young people. NPC's analysis highlighted that Columba 1400's success in preventing young people from becoming unemployed means that they will earn higher wages throughout their lives.

What price an ordinary life?: The financial costs and benefits of supporting disabled children and their families **(2007)**

This report is NPC's submission to HM Treasury's 2007 Comprehensive Spending Review on services for disabled children and their families. The report shows how reducing stress for parents of disabled children can deliver real financial benefits. However, services to the families of disabled children can be expensive, and without evidence of how much they reduce stress, we cannot tell if they are cost-effective.

Misspent youth: The costs of truancy and exclusion **(2007)**

This report is NPC's cost-benefit analysis of two charities working to combat truancy and exclusion. Our analysis reveals that while early intervention means that many more young people are helped than will later develop behavioural problems, the huge costs of these problems means that it is still far more cost-effective to take a preventative approach.

Hard knock life: Violence against women **(2008)**

Hard knock life is a guide for charities and funders interested in helping victims of violence against women. The report includes an analysis of the huge cost of violence against women, both in terms of the human and emotional costs and the services provided to victims.

Trial and error: Children and young people in trouble with the law **(2010)**

This is NPC's guide for charities and funders interested in youth offending. The report highlights the savings to be made from keeping young people out of the youth justice system.

All of the financial proxies generated during these projects are available as part of the SROI database at www.sroiproject.org.uk.

Appendix B: Principles and stages of SROI

The seven principles of SROI[1]

There are seven principles that underpin how SROI should be used:

1. **Involve stakeholders.** Stakeholders should inform what gets measured and how this is measured and valued.
2. **Understand what changes.** Articulate how change is created and evaluate this through evidence gathered, recognising positive and negative changes as well as those that are intended and unintended.
3. **Value the things that matter.** Use financial proxies in order that the value of the outcomes can be recognised.
4. **Only include what is material.** Determine what information and evidence must be included in the accounts to give a true and fair picture, such that stakeholders can draw reasonable conclusions about impact.
5. **Do not over claim.** Organisations should only claim the value that they are responsible for creating.
6. **Be transparent.** Demonstrate the basis on which the analysis may be considered accurate and honest, and show that it will be reported to and discussed with stakeholders.
7. **Verify the result.** Ensure appropriate independent verification of the account.

The six stages of SROI[2]

SROI analysis involves six stages:

1. **Establishing scope and identifying key stakeholders.** It is important to have clear boundaries about what your SROI analysis will cover, who will be involved in the process and how. Often service users, funders and other agencies working with the client group are included in an SROI.
2. **Mapping outcomes.** Through engaging with your stakeholders you will develop an impact map (also called a theory of change or logic model) which shows the relationship between inputs, outputs and outcomes.
3. **Evidencing outcomes and giving them a value.** This stage involves finding data to show whether outcomes have happened and then giving them a monetary value.
4. **Establishing impact.** Those aspects of change that would have happened anyway or are a result of other factors are taken out of the analysis.
5. **Calculating the SROI.** This stage involves adding up all the benefits, subtracting any negatives and comparing the result with the investment. This is also where the sensitivity of the results can be tested.
6. **Reporting, using and embedding.** This vital last step involves verification of the report, sharing findings with stakeholders and responding to them, and embedding good outcomes processes.

[1] Cabinet Office (2009) *A Guide to Social Return on Investment.*
[2] See www.sroiproject.org.uk for more details.

New Philanthropy Capital

New Philanthropy Capital (NPC) is a consultancy and think tank dedicated to helping funders and charities to achieve a greater impact.

We provide independent research, tools and advice for funders and charities, and shape the debate about what makes charities effective.

We have an ambitious vision: to create a world in which charities and their funders are as effective as possible in improving people's lives and creating lasting change for the better.

For **charities**, this means focusing on activities that achieve a real difference, using evidence of results to improve performance, making good use of resources, and being ambitious to solve problems. This requires high-quality leadership and staff, and good financial management.

For **funders**, this means understanding what makes charities effective and supporting their endeavours to become effective. It includes using evidence of charities' results to make funding decisions and to measure their own impact.

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