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MAPPING THE SOCIAL IMPACT INVESTING MARKET IN GERMANY

An Overview of Opportunities in the Education Space

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The Impact Investing Policy Collaborative (IIPC) strives to grow impact investing markets by building a global network for policy research and innovation. The IIPC helps its members – investors, public officials, advocates, researchers and related communities – better identify and support policies that lead to more robust and effective capital markets with intentional social and environmental benefits.

The IIPC achieves these goals through several activities, including research awards that support the exploration of new areas – geographies and topics – to cultivate greater interest in the field and further expand the network of researchers and advocates considering impact investing policy issues. This publication was commissioned as part of the IIPC research program.

The IIPC is convened by PCV InSight and the Initiative for Responsible Investment at the Hauser Institute for Civil Society Harvard University, with initial support from The Rockefeller Foundation. The IIPC network relies primarily on its members from over 30 countries to provide local knowledge and insights into impact investing policy that are then shared globally.

EXECUTIVE SUMMARY

Impact investing – defined as “investments made into companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return” by the Global Impact Investing Network (GIIN) – is on everyone’s lips these days. It is being talked about as a promising means to help solve the world’s social and environmental challenges. The report at hand investigates the status quo of the German social impact investing market with a particular focus on educational measures that could help solve some of Germany’s most pressing issues, namely unequal educational opportunities, long-term unemployment and relative poverty. Our research shows that social impact investing – at large and in the educational space in particular – is still in its infancy in Germany. It is driven by very few players and the government’s involvement is limited, to date.

- **Investors:** Investors in the German social impact investing market – at large and in the educational space – mainly comprise high net worth individuals (HNWIs). They may invest either directly in social enterprises or via product providers such as Germany’s two social venture capital funds, tuition or real estate funds. But even for these wealthy individuals investment opportunities are limited and intransparent, and independent advisory is lacking.

Retail investors face even more limited opportunities to engage in social impact investing in Germany – at large and in the educational space. Based on our research, no dedicated social impact investment product or funding platform exists for retail investors in Germany to date. Retail investors are essentially limited to opening accounts with Germany’s value banks.

In January 2012, the Kreditanstalt für Wiederaufbau (KfW) launched its financing program for social enterprises. Under this program, the development bank provides equity financing between EUR 50,000 and 200,000. A necessary requirement is the existence of a co-investor (a natural person or legal entity). At the time of the writing of this study, the KfW had committed eight deals; no investment in the education sector had been committed. The participating co-investors represented a broad range of players, including welfare organizations, social venture capital funds, and wealthy individuals.

Otherwise, institutional investments are practically nonexistent in the German social impact investing market, according to our research. Only very few German foundations practice social impact investing due to – among other issues – legal uncertainty, a lack of (foundation-specific) standardized investment products and advice, and the absence of rating services. Yet, the Benckiser Foundation is currently implementing Germany’s first social impact bond together with its subsidiary Juvat gGmbH. Moreover, a group of experts consisting of the chairmen of twelve German foundations has been brought together to discuss the potential of foundations to engage in impact investing, and to clarify the regulatory challenges involved. The group’s insights will be published in a guideline on impact investing for German foundations. In addition, the expert group is developing a pilot fund specifically suited to the investment needs of foundations.

No significant activity could be identified on the part of other institutional investors, most notably pension funds. This is not surprising given their fiduciary duties, combined with the scarcity of standardized investment products, their size and illiquidity, and their typically unfavorable risk-adjusted financial returns.

- **Intermediaries:** Social impact investing products (in the education space) are primarily offered by value banks (such as the GLS Bank) and specialized asset managers, including Germany’s two social venture capital funds (Bon-Venture and the Social Venture Fund), real estate fund managers active in the property development of childcare facilities or schools (e.g., Habona Invest) and tuition fund managers (e.g., Brain Capital). Commercial banks do not (yet) offer social impact investing products (for education) in Germany.

Besides the scarcity of standardized investment products, our research reveals that there is a lack of transparency into investable opportunities in the social impact investing market. Independent advisory and rating services are absent, as is a dedicated funding platform allowing German (retail) investors to invest in German socially-motivated organizations (broadly and in education in particular) with a financial return expectation. Efforts to set up a social stock exchange are underway, however.

- **Investees:** Investable opportunities for social impact investing – at large and in the field of education – are limited in Germany. This is oftentimes ascribed to the strong state provision of social services combined with beneficiaries' limited ability (or willingness) to pay.

Hybrid, layered investment structures and performance-based payment schemes, like the much-celebrated social impact bonds, might provide a remedy, making 'uninvestable' organizations investment-ready. Overall, potential for social impact investing in education is seen in particular in support activities and preventive measures for which public funds are limited or unavailable.

- **Government:** The federal government's involvement in the development of the German social impact investing market has been limited thus far. Its Engagement Strategy and the resulting Multistakeholder Conference organized by the Federal Ministry of Family, Senior Citizens, Women and Youth (BMFSFJ) constituted a first step in anchoring the social entrepreneurship discourse at a national level, touching also on financing issues. Moreover, the BMFSFJ mandated the KfW to develop its financing program for social enterprises (see above).

Germany's first social impact bond is currently being implemented in close collaboration with the municipalities and the federal state of Bavaria. Despite Germany's federal structure – which gives significant power to the federal states – we were not able to identify any other significant social impact investing activity in education on the federal state level. This is particularly surprising given that educational policy is generally the purview of the federal states. Additional municipalities and federal states will likely become involved as increasing numbers of social impact bonds are developed, however.

A number of stakeholders in the field are demanding more government involvement. Based on our research, we identified two main strategies for the German government and federal states to promote social impact investing in general and with regard to education. On the one hand, the government could initiate discourse and assess the potential for social impact investing in Germany through the commissioning of research reports, the establishment of a dedicated taskforce and/or the organization of expert roundtables involving a large number of stakeholders. On the other hand, it could support sector building, for which a number of specific measures have been suggested, including more flexibility and certainty for foundations, tax incentives for social impact investments, and the creation of more investable opportunities through guarantees, funding programs and the like.

It is important to remember, however, that opinions regarding the ideal level of government involvement differ, given the range of political views in Germany.

We are not arguing for the replacement of the welfare state, which has served Germany well. However, we believe that targeted social impact investments in carefully selected areas might effectively complement the government's activities. Social impact investing should not be discussed as a universal remedy or an end in itself, but as a supporting means to help solve the social challenges Germany faces. We are eager to see how the German social impact investing market will develop over the coming years.

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1. INTRODUCTION

1.1. Defining impact investing

In 2007 and 2008, the Rockefeller Foundation invited leaders in finance, philanthropy and development to its Bellagio Center in Italy to discuss the need for and possibility of a global investment industry aiming for social and environmental impact.¹ These meetings coined the term impact investing² and eventually led to the formal constitution of the Global Impact Investing Network (GIIN) in 2009.³

The practice of investing for a combination of financial and social/environmental return predates the term impact investing. While the phenomenon has received much attention from politics, media and society lately, it has existed for quite a long time. Examples include the Commonwealth Development Corporation in the UK or the World Bank's International Finance Corporation (IFC), which have existed since 1948 and 1956.⁴

Despite its long-standing history, impact investing appears to have reached a new level of attention as of late. Driven by resolute action, it is transforming into a new global industry that brings together “the disparate and uncoordinated innovation in a range of sectors and regions”.⁵ A supporting eco-system has been emerging – including investor networks (especially the GIIN), impact reporting and investment standards (e.g., IRIS), rating agencies (e.g., GIIRS), online databases of investment products (e.g., ImpactBase), etc. – which is further driving the development of the sector.

Governments around the world have been a key driving force in developing the sector. Over the last years, several governments have taken decisive action to propel national impact investing markets, most prominently the UK. In April 2012, it launched Big Society Capital, a “social investment wholesaler” with the mission to help develop a well-capitalized and sustainable social investment market in the UK.⁶ With access to funds of up to GBP 600 million, Big Society Capital invests in social investment finance intermediaries, which provide capital to social sector organizations.⁷ In addition, the UK developed the first social impact bond (SIB), an outcomes-based contract in which public sector commissioners pledge to reimburse private investors, who pre-finance prevention and early intervention services, if the intended social outcome (e.g., lower offending rates) is achieved.⁸ That is, investors only recover their investment (including a financial return) if there is a significant social impact. Please consult the info box in section 2.1 for more information on social impact bonds.

Despite this high interest in impact investing by governments, practitioners, the media and society at large, a universal impact investing definition remains a work in progress.⁹ Some argue in favor of a broader definition in order to avoid constraining deal flow and excluding possible market participants¹⁰, while others fear that a broader definition might dilute the concept and render it meaningless.¹¹ Lastly, a third group questions whether a clear definition is necessary at all given that the industry is still in its early development stage.¹²

In general, the debate regarding the definition and boundaries of impact investing hinges on the required social impact and financial return level, the characteristics of investees as well as the boundaries and overlap with related concepts.

- The question of what qualifies as an impact investment with regard to the “**social impact hurdle**”¹³ is the subject of heated debate. Generally, any investment could be said to have a positive social impact, yet not all should be labeled as impact investments.¹⁴ For example, there are some who consider any investment in a poor area impact investing.¹⁵ Others argue against such a broad application of the term.¹⁶
- In addition to the impact component, there also seems to be disagreement regarding the **expected level of financial return for an impact investment**. While some equate impact investing with market-rate returns, others associate it with below-market-rate investments. The commonly accepted view seems to be, however, that impact investments may range from preserving the invested principal to market-rate or even above-market-rate returns.¹⁷ What appears to be (largely) unchallenged is that pure grant making does not qualify as impact investing.¹⁸
- Moreover, there appears to be a lack of clarity around the **required characteristics on the part of the investee**, most notably whether impact investing is limited to social sector organizations, that is, organizations whose first priority is the delivery of social impact rather than economic value.¹⁹
- Lastly, there is also confusion on the **terminological level**. Alternative terms such as ‘social investing’ are often used interchangeably with impact investing. Furthermore, the boundaries of related concepts such as (socially) responsible investing are not clear-cut.²⁰

It is not the goal of this research to resolve this conflict. Nevertheless, a market mapping calls for a clear working definition. For the purpose of this report we have, thus, decided to comply with the impact investing definition provided by the GIIN:

*Impact investments are investments made into companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets, and target a range of returns from below market to market rate, depending upon the circumstances.*²¹

In our view, this is justified given that the meetings from which the GIIN originated coined the term impact investing, and that the GIIN is perceived as “the de facto impact investment industry body, promoting standardised reporting, transparency and advancement of the industry”²².

The above definition rules out pure profit-maximizing investing as well as traditional charitable giving. However, it is the common view that impact investors may prioritize either social/environmental or financial objectives. As such, impact investors are commonly classified as impact first or financial first investors (see illustration 1).

Throughout the study, we will use the term social impact investing to refer to impact investments, which are focused on social rather than environmental issues.

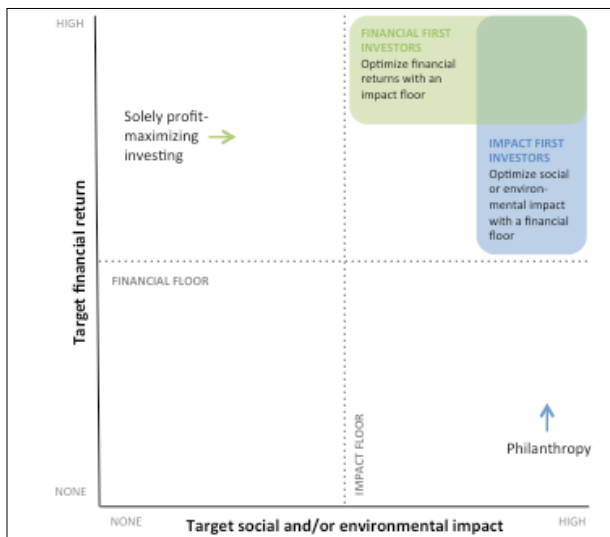


ILLUSTRATION 1: IMPACT INVESTOR CLASSIFICATION (FREIREICH & FULTON, 2009).

1.2. The promise of impact investing

Lately, impact investing has received publicity for a number of reasons.

The world population continues to wrestle with a myriad of problems, including poverty, climate change, HIV/AIDS, and a lack of clean water – just to name a few. While these issues all merit urgent action, the resources traditionally used to tackle them are limited. Foreign aid from Western countries was reduced significantly in 2011.²³ Many developed country governments are facing high debt levels and need to reduce deficits going forward.²⁴ At the same time, philanthropic financial resources are not inexhaustible. As Judith Rodin, President of the Rockefeller Foundation, has said, “If you put a price tag on all the social and environmental needs around the world, it is in the trillions. All of the philanthropy in the world is only \$590 billion. So, the needs far exceed the resources.”²⁵ Given that public and philanthropic funds are insufficient to solve all societal problems, there is a clear need to mobilize private capital.

In addition to being limited, philanthropic giving is also often short-lived. While donations are the cheapest form of financing for organizations, they are also the least sustainable.²⁶ In 2011, philanthropic giving was unstable and even declined in some areas.²⁷ What is more, both government and philanthropic funding come with significant drawbacks, including long waiting times, limited financing of overhead costs, short-term and lack of follow-on financing, and a lack of incentive structures to foster financial self-sufficiency.²⁸

Lastly, investors seem to be increasingly receptive to the concept of impact investing, an indispensable requirement for its success. The current financial crisis has left investors doubtful about the risk and return profiles of traditional investments²⁹ and caused them to reconsider risk by integrating additional factors such as environmental, social and governance (ESG)

criteria in their decision making process³⁰. A number of studies support the growing interest in impact investing: According to the third annual survey on the impact investment market co-authored by J.P. Morgan and the GIIN, the participating organizations (including foundations, development finance institutions, pension funds and family offices) had invested a total of USD 36 billion in impact investments when the survey was taken, with USD 8 billion invested in 2012 and investments of USD 9 billion planned for 2013.³¹ For foundations in particular, impact investing provides an interesting avenue to pursue their objectives as it allows them to leverage their philanthropic funds and recycle them for additional projects and investments, yield social and environmental impact not possible with grants (e.g., build a credit history) and align the investment of their endowment with their mission.³² Such a combination of asset management and project work could serve as a multiplier of the impact a foundation can have – despite falling interest yields.³³

While impact investing cannot – and should not – be expected to replace government activity and philanthropic giving, the authors of this study believe that impact investments in carefully selected areas could complement these traditional funding sources.

1.3. The German market as the object of study

As indicated in the title, this report focuses on the German social impact investing market. In our view, Germany is an important object of study for a number of reasons, from both macro and microeconomic perspectives.

With a GDP of USD 3.4 trillion in 2012, Germany maintains the world's fourth largest (and Europe's largest) national economy, and significantly leads its closest competitors, France (USD 2.6 trillion) and the UK (USD 2.5 trillion).³⁴ So far, Germany has navigated comparatively well through the financial crisis. Its economic success has even increased its political influence in Europe and many look to Germany "as a shining example".³⁵

Nevertheless, there might be room for social impact investing. Although Germany does comparatively well in terms of indebtedness compared with the other Organisation for Economic Co-operation and Development (OECD) countries (see illustration 2), the Federal Ministry of Finance also plans to continue its endeavors to reduce the structural deficit³⁶ which is placing limits on the social budget.

General government gross debt in % of GDP, 2011

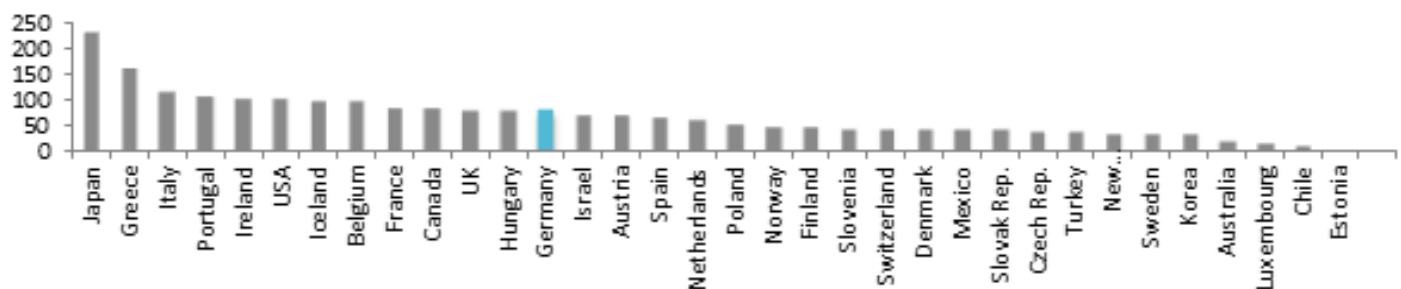


ILLUSTRATION 2: GENERAL GOVERNMENT GROSS DEBT AS A PERCENTAGE OF GDP FOR OECD COUNTRIES (IMF, 2012).³⁷

At the same time, demographic change is resulting in a mismatch of contributors and retirees, reducing tax income and contributions while leading to higher retirement payments.³⁸ The municipalities are particularly suffering from this mismatch.³⁹

Although quality of life in Germany is relatively high compared with other countries – for instance, Germany ranks among the top ten countries with a view to several categories of the OECD's Better Life Index⁴⁰ – the nation does face several challenges, including the risk of poverty, long-term unemployment and unequal educational opportunities.⁴¹ As a social market economy, the government has traditionally played an important role in the provision and financing of social services. Accordingly, the German population expects the state to address and solve these social issues. This stands in stark contrast to more developed social impact investing markets like the USA and the UK where the state has played - and is expected to play - a less active role.

DIGRESSION: Germany – a ‘Sozialstaat’

The so-called ‘Sozialstaatsprinzip’, which could be translated as social state principle, is anchored in article 20 of the German constitution.⁴² In the German language, the term ‘Sozialstaat’ is distinct from the term ‘Wohlfahrtsstaat’ (engl.: welfare state): Typically, a ‘Sozialstaat’ is associated with a leaner social security system, which is limited to certain core functions, whereas the ‘Wohlfahrtsstaat’ grants the state more comprehensive competencies to intervene in the market (e.g., in the form of greater redistribution of wealth).⁴³ In Germany, the term ‘Wohlfahrtsstaat’ is typically associated with the Scandinavian system.⁴⁴

Esping-Andersen distinguishes three types of welfare state regimes: the liberal, the conservative and the social democratic. Liberal welfare states are characterized by “means-tested assistance, modest universal transfers, or modest social-insurance plans”. Typical examples are the USA, Canada and Australia.⁴⁵ Social democratic welfare states, on the other hand, “promote an equality of the highest standards, not an equality of minimal needs” translating into “universalistic programs”. The best examples for this type of welfare state regime are the Scandinavian countries. Germany falls in the group of conservative welfare states, which are located between the two extremes, together with Austria, France and Italy. In these countries, “private insurance and occupational fringe benefits play a truly marginal role [while...] the state’s emphasis on upholding status differences means that its redistributive impact is negligible”. The principle of subsidiarity plays a fundamental role.⁴⁶

Germany’s public expenditure as a percentage of GDP highlights its greater welfare orientation compared with liberal welfare states. In 2013, Germany’s public social expenditure as a percentage of GDP was 26.2% compared with 23.8% in the UK, 20.0% in the USA and 19.5% in Australia.⁴⁷

According to data from the Johns Hopkins Comparative Nonprofit Sector Project dating from 1996, the German state also plays a much more important role in the financing of nonprofit organizations (NPOs). While the public sector contributed 68.2% to the NPOs’ revenue, it was only 29.6% for the USA and 39.8% for the UK. In these liberal welfare states, private giving (18.6% and 12.0% versus 3.9%) and private fees (51.8% and 48.2% versus 27.9%) played a much more important role in funding NPOs. This can be ascribed to the principle of subsidiarity and the resulting “elaborate collaborative relationship between the state and a wide variety of nonprofit organizations”.⁴⁸

Germany’s welfare system rests upon the “permanent cooperation of public-sector and non-statutory agencies”.⁴⁹ The latter are known as the ‘Freie Wohlfahrtspflege’ and primarily consist of six central voluntary welfare organizations, namely Arbeiterwohlfahrt, Deutscher Caritasverband, Deutsches Rotes Kreuz, Diakonisches Werk der EKD, Paritätischer Wohlfahrtsverband and the Zentralwohlfahrtsstelle der Juden in Deutschland.⁵⁰ In their entirety, the non-statutory welfare organizations are the largest provider of social services in Germany.⁵¹ They are particularly prominent in the area of nursery schools, ambulatory care, retirement and nursing homes as well as hospitals.⁵² In 2008, they operated 102,393 facilities and employed 708,523 full-time and 833,306 part-time employees.⁵³ The non-statutory welfare organizations are financed through a combination of three sources. Firstly, they receive fixed care charges for certain services they provide (e.g., hospitals, nursing homes, etc.) either from the recipients, who might be able to claim back the charges, or directly from the public welfare agencies for services covered by social insurance. Secondly, they receive public grants-in-aid for investments in building facilities or the financing of their operations based on the public-law obligation of provide appropriate support for voluntary welfare organizations. Thereby, the form and extent depend on the field of work as well as the federal state, district and municipality. Lastly, internal funding is provided through volunteering, cash and in kind donations, welfare stamps, and lotteries.⁵⁴

Finally, there is also growing appetite for sustainable investment among both private and institutional investors in Germany. The German market for sustainable investments has been growing at an annual growth rate of 28 percent since 2005; in 2011, the market amounted to EUR 63 billion (1.2% of the overall investment market).⁵⁵ Estimated at EUR 84 million⁵⁶, impact investing still makes up a tiny fraction of the market.

Although the term impact investing is not yet in broad use, and market expertise rests with very few individuals and organizations, there is growing interest in social impact investing in Germany. In 2012, the KfW launched a financing program for social entrepreneurs, social venture capital funds have emerged over the last decade, German foundations are increasingly interested in social impact investing and a few have been experimenting with it, and social impact bonds are being discussed and implemented.

1.4. Social and environmental issues in Germany

In Germany, compared with the OECD average, the average household net adjusted disposable income (USD 28,799 vs. USD 23,047 per year), the employment rate⁵⁷ (73% vs. 66%), the level of education⁵⁸ (86% vs. 74%), the average student skills⁵⁹ (510 vs. 497 points) and the water quality (93% satisfaction vs. 84%) are significantly higher, while the hours worked (1,413 hours vs. 1,776 hours per year) and the level of air pollution (16 µg/m³ of PM10 vs. 21 µg/m³) are significantly lower.⁶⁰

Nevertheless, Germany still faces major challenges. A study by the Bertelsmann Foundation finds that Germany is considered only average in terms of social justice when compared to other OECD nations.⁶¹ This reality is linked strongly to deficits regarding the prevention of poverty (esp. income and child poverty), access to education and labor market inclusion (esp. of the long-term unemployed and low-qualified), among other issues.⁶² Other recent reports also list these issues as focal challenges.⁶³

To some extent, these three fields are interrelated. In 2010, 15.8% of the German population was at risk of entering poverty, an increase of 3.1 percentage points compared with 2005.⁶⁴ Both unemployment and educational qualification are strong determinants of poverty risk. In 2010, 67.8% of all unemployed persons in Germany were at risk of entering poverty compared with 7.7% of the working population and 14.0% of the retired population.⁶⁵ Similarly, 25.8% of the low-qualified were at risk of entering poverty compared with 7.7% of those with a high and 14.7% of those with a medium level of education according to the International Standard Classification of Education (ISCED).⁶⁶

Unfortunately, the German education system performs poorly in terms of equality of opportunity. Educational success depends heavily on a child's parentage and socio-economic background; among the OECD countries, this relationship is more pronounced only in Austria, France, New Zealand, Belgium and Hungary.⁶⁷ However, unequal access to education and social poverty create a vicious circle: without access to education, there will be no social advancement.⁶⁸

Related to this cycle of inequality is the issue of labor market inclusion. In general, Germany performs relatively well in terms of employment, unemployment and youth unemployment rates compared with other OECD countries.⁶⁹ Nevertheless, it is much more difficult for low-qualified people and immigrants to find a regular job in Germany.⁷⁰ Moreover, long-term unemployment is a serious issue in Germany: every second unemployed person is affected by long-term unemployment; the only OECD country with a higher long-term unemployment rate is Slovakia.⁷¹ This is particularly problematic as long-term unemployment is one of the key contributors to poverty.

In sum, one's level of qualification is an important determinant for the likelihood that one will face (long-term) unemployment and poverty. As such, a quality education is a key preventive measure, empowering individuals to lead autonomous lives.

Given strained public budgets, targeted social impact investments might be a fruitful way to support and complement the efforts of the government (and philanthropy). Social impact investing could free up additional financing which could be channeled into preventive measures or less conventional and untested interventions for which there is oftentimes limited public financing. Social impact investing might further promote a results orientation, leading to a more efficient and effective use of funds. Lastly, social impact investing might also engage a broader group of stakeholders, thus fostering civil society and promoting a shared sense of responsibility.

As outlined above, educational measures are key to fighting some of Germany's most pressing social problems. Accordingly, this report will focus primarily on social impact investments in the German education sector. Thereby, we will take a broad perspective on education spanning early child education as well as educational measures targeted at (re-)integrating low-qualified adolescents, immigrants or the long-term unemployed into the labor market. Instead of analyzing areas that might be most promising for social impact investments – for example, because the impact is easy to measure or because there are no established players in a certain space – we have opted for the alternative route, focusing on an area where we believe social impact investing might be most needed and effective. Naturally, there are very few specialized players in this nascent field; this study therefore also provides an overview of the German social impact investing market at large.⁷² We are convinced that such a sector-based approach is legitimate – if not absolutely necessary – given the heterogeneity of the impact investing field. A sector-based approach to impact investing is also favored by other research institutions dedicated to the growth of the market; for instance, in a recent report by the Omidyar Network⁷³ or the Centre for Social Investment at the University of Heidelberg⁷⁴.

1.5. Goals, methodology and structure

Market mappings typically combine three elements: descriptive (definition of the market's boundaries and description of entities and their functions), analytical (conclusions based on description) and prescriptive (recommended actions).⁷⁵

The study at hand consists of three building blocks (see illustration 3), which aim to combine these three components.



ILLUSTRATION 3: THREE BUILDING BLOCKS OF THIS RESEARCH (OWN ILLUSTRATION).

The basic goal of the first two sections – the market review and the role of the government – is to provide a description of the status quo. These sections also entail an analytical element. The last section is mainly prescriptive; it points out what is lacking and what could be done on the part of the government to build a more robust and effective social impact investing market.

The report targets a broad audience including socially motivated investors and financial players, social entrepreneurs and third sector organizations, philanthropists and foundations, policy makers, academics and the general public at large.

In terms of methodology, we combine two research approaches: We draw upon insights from desk research (covering academic and practitioner contributions, media reports and websites) as well as qualitative in-depth interviews with twelve experts in the field, spanning a wide range of players including social venture capital funds, foundations, development banks, private banks, social entrepreneurs and social entrepreneurship support organizations. By combining these two research approaches we hope to provide as complete a picture as possible. It is our goal to offer an indication of the current state of the German social impact investing market with a focus on the education sector at large. The report does not claim, however, to be exhaustive with a view to the existing activity in the field.

2. MARKET REVIEW

This chapter provides an overview of the state of the German social impact investing market (rather than the ecological), its most relevant players and their activities. As mentioned in the introduction, our main focus lies on impact investments in the education space in the broader sense. Since only very few players – especially on the investor and the intermediary side – focus exclusively on the education sector, this market mapping also provides valuable insights into the German social impact investing landscape at large.

In order to map the market players, we applied a framework that helped us identify and classify them. When we started with this project, our review of the existing literature did not reveal a ready-made framework that we could apply to the German social impact investing market. Consequently, we decided to create our own framework. Based on the market structure common to traditional capital markets and drawing from a number of scholarly inquiries and practitioner reports on the SRI and impact investing market, respectively, we have come up with the following classification (see illustration 4).

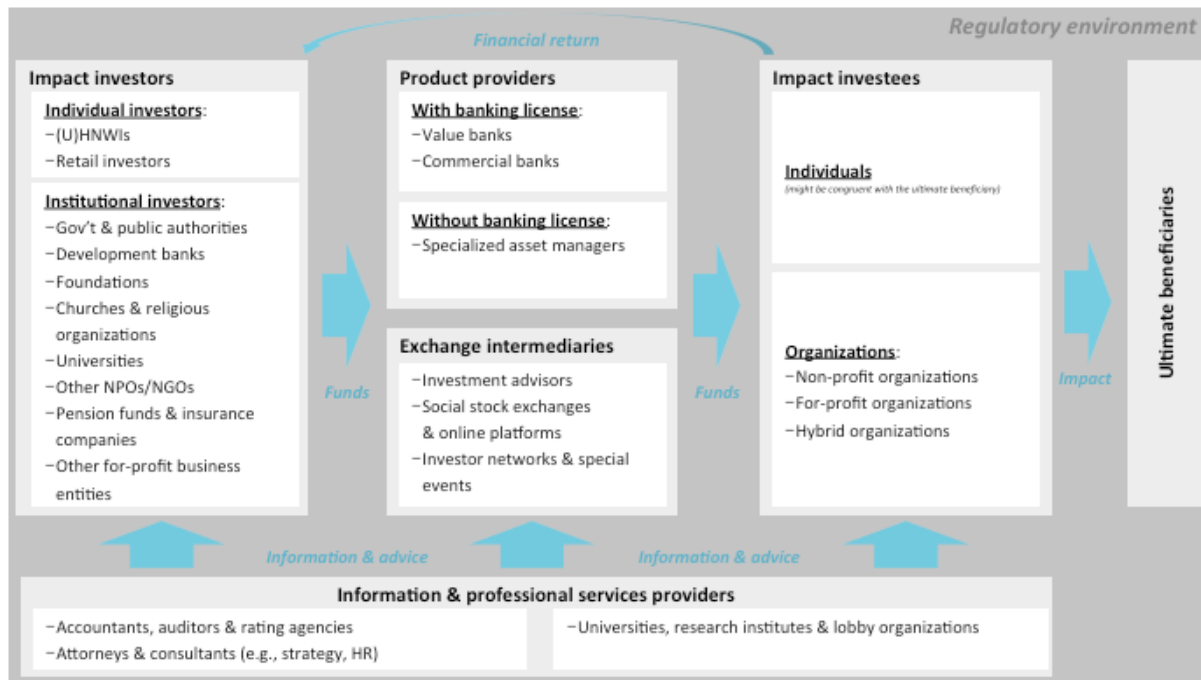


ILLUSTRATION 4: CLASSIFICATION OF IMPACT INVESTING MARKET PLAYERS (OWN ILLUSTRATION).

Many of these players (may) perform different roles and could therefore be assigned to different categories. Government is a good example: While it may be a key social impact investor, it also plays an intermediary role by providing either an enabling or hindering regulatory environment for social impact investing.⁷⁶

2.1. Investors

Social impact investors are those individuals and organizations that make the deliberate choice to allocate the capital they control to a social impact investee – either directly or via a product provider. Our framework distinguishes between individual investors and institutional investors (i.e. organizations). This distinction is not only common in the traditional capital markets but also in the socially responsible investment (SRI)⁷⁷ and impact investing⁷⁸ space.

We have limited this market review to German social impact investors – that is, social impact investors headquartered in Germany – who are invested in German social impact investments. Please also note that the government will be discussed separately in chapter 3. Lastly, we will focus this review on investors who are actively looking for investment opportunities with an explicit social impact. As demanded by the GIIN's impact investing definition provided above, the intent for non-financial impact must be a clear and explicit part of the investment strategy. Such an approach excludes, for instance, purely commercially-motivated loans to socially-motivated organizations.

A. Individual investors

With a view to the individual investor space, we distinguish between (ultra) high net worth individuals ((U)HNWIs) and retail investors. Such a volume-based segmentation approach does not only make sense because of its popularity but also because HNWIs have access to certain types of investments that smaller retail investors do not.⁷⁹

i. (Ultra) High net worth individuals

(Ultra) High net worth individuals ((U)HNWIs) are extremely wealthy individuals. Definitions vary. The World Wealth Report, for example, defines HNWIs as individuals with funds of at least USD 1 million available for investment; UHNWIs, on the other hand, are individuals that can invest USD 30 million or more.⁸⁰

Ultra high net worth individuals and family offices have served as pioneers in and promoters of the microfinance sector, and are also playing an important role in the development of the impact investing industry.⁸¹ They do not need to comply with the same level of fiduciary duty as institutional investors, and thus have greater flexibility with their investment strategy.⁸² They can freely decide whether to pursue more of an impact first or a financial first strategy, and whether or not to focus on (a) certain sector(s) or impact objective(s).⁸³

In general, wealthy individuals can either invest directly or indirectly. One way to invest directly is by becoming a social business angel. Business angels are unrelated private investors that invest in new and growing businesses.⁸⁴ It is more common for business angels to invest in early stage ventures than for venture capitalists (VCs), who tend to become involved at later development stages.⁸⁵ Over the last few years, a number of social business angel networks have emerged, including UK-based ClearlySo, Netherlands-based Pynwymic and US-based Investors' Circle and Toniic.⁸⁶ In Germany, no such network has existed until very recently. In 2013, Germany's first social business angel investment club was established under the name 'Ashoka Angels Network'. Based on their individual investment preferences, the club members are presented with investment opportunities from Ashoka's⁸⁷ network at regular intervals. So far, this network only includes members of Ashoka's Support Network (ASN); yet, it is supposed to be opened up to external members in the short term. Outside of this investment club, a few other players organize events to bring together impact investors and investees. One example is 'Social Business meets Angel' organized by the BMW Foundation together with BonVenture, the Social Venture Fund and the Social Entrepreneurship Akademie.⁸⁸ Besides investing directly, wealthy individuals can access the entire range of product providers described in chapter 2.2.

Based on our desk research and expert interviews independent advisors (other than product providers such as social venture capital funds) that can provide unbiased counseling to wealthy individuals willing to engage in social impact investing are practically inexistent in Germany. There is much activity in the field, however, and established players have recognized their clients' interest in impact investing. The Berenberg Bank, Germany's oldest private bank, for instance, has recently published a study on impact investing together with Beyond Philanthropy⁸⁹ and hosted an impact investing conference for interested clients and other stakeholders. In a similar vein, there is also a lack of independent rating services for impact investment opportunities.

In general, wealthy individuals are starting to think about impact investing in two different ways in Germany. The first school of thought consists of impact first investors. These individuals consider impact investing an effective complement to philanthropic giving. Given their oftentimes entrepreneurial background, they believe in the power of enterprises to help solve social and/or environmental problems. They tend to favor enabling self-help rather than pure charity. Such investors may, for example, either engage as direct investors in social enterprises or invest in a social venture capital fund, which might not provide for competitive financial returns.

The second group consists of individuals who think of impact investing as an alternative to traditional (SRI) investments. For this group, capital preservation and (somewhat) competitive returns are key. Based on our research, investment opportunities for this type of impact investor are limited in the education space in Germany, given the scarcity of investable social enterprises and the typically high transaction costs. Impact investments yielding competitive returns might be more common in other areas, most notably the environmental space. Based on our research, education and real estate funds as described below in section 2.2 present one of the few investment opportunities in education for financial first investors.

ii. Retail investors

Retail investors without the financial resources of (ultra) high net worth individuals face even more limited opportunities to engage in social impact investing in Germany, especially in education. Social venture capital funds require substantial investments.⁹⁰ Other social impact investment products described in section 2.2 are subject to strict investor protection rules due to their risk profile.⁹¹ Impact investments typically come in the form of private debt or equity rather than investments in listed companies.⁹² As a result, they can usually only be actively offered to qualified and institutional investors.⁹³ Moreover, there is currently no social stock exchange where small investors could readily buy and sell shares or bonds.

In the UK, the FSE Group and Social Finance have just launched the first diversified, professionally managed, fully listed social impact investment product for UK retail investors.⁹⁴ No such product exists in Germany, to date.

The same is true for peer-to-peer micro lending or crowd funding platforms with a financial return expectation. In November 2013, Social Impact GmbH and Startnext, supported by the Deutsche Bank Foundation, launched a German crowd funding platform for social start-ups.⁹⁵ Similar to Startnext⁹⁶, which focuses on creative projects, Social Impact Finance only allows for financial support in return for a pre-sale or a gift, but thus far does not offer 'proper' financial investments.⁹⁷ Along the same lines, Betterplace⁹⁸ only allows for donations in (education) projects in Germany pursuing a social and/or environmental impact; it does not provide a financial return.

A platform like MicroPlace, where US residents have the opportunity to invest in companies that create positive impact domestically and abroad with a financial return ranging from 0.5 to 4.5% and a minimum investment of USD 20,⁹⁹ does not exist in Germany, to date. Although Kiva allows German social impact investors to provide interest-free microloans to people without access to financial services starting from USD 25, it does not allow for social impact investments in Germany.¹⁰⁰

German retail investors willing to engage in social impact investing may open up an account with a value bank such as the GLS Bank. At GLS Bank, clients may choose in which sector (housing, energy, alimentation, education or social) the bank invests their savings. GLS also offers savings bonds in the education space. The bank's activities are described in more detail in chapter 2.2.

B. Institutional investors

Institutional investors form a "heterogeneous group of organizations"¹⁰¹. Based on an extensive review of impact investing and socially responsible investing (SRI) literature we derived the following list of institutional impact investors: Governments and public authorities, development banks, foundations, churches and religious organizations, universities, other non-profit organizations (NPOs) and non-governmental organizations (NGOs), pension funds and insurance companies as well as other for-profit business entities. As noted above, the role of the German government with regard to social impact investing will be discussed separately in chapter 3.

i. Development banks

Understanding that freely available financing for social entrepreneurs – especially growth capital – was limited¹⁰², the Federal Ministry of Family, Senior Citizens, Women and Youth (BMFSFJ) mandated the KfW development bank to create a financing program for social enterprises.¹⁰³ The program was launched in January 2012.¹⁰⁴

Under this program, the KfW development bank provides equity financing between EUR 50,000 and EUR 200,000 to social enterprises, which aim to solve social problems in Germany with a proven innovative business model that they would like to scale. The business model is expected to be self-supporting in the medium- to long-term. The focus is put on the social return rather than the achievement of a market-rate financial return. A necessary requirement for the KfW to invest is the existence of a co-investor, which can be a natural person or a legal entity (e.g., business angels or foundations). The form, conditions and term follow the specifications of the co-investor. The KfW does not get involved in the management of the social enterprise but expects the co-investor to coach and support with regard to managerial and financial aspects. Amongst others, the program explicitly lists education, poverty reduction and integration as focus areas.¹⁰⁵

What is worth noting is that the KfW follows a different social enterprise understanding than the EU. The EU definition requires a primacy of the social objective and a limited distribution constraint on profits.¹⁰⁶ Although the KfW

requires that the solution of the societal issue constitutes the investee's core business¹⁰⁷, social enterprises may retain or distribute profits without any constraints. Besides the direct provision of financial resources, the KfW program is also designed to leverage debt financing by (commercial) banks through the establishment of a solid equity base.¹⁰⁸ More broadly, the KfW financing program for social enterprises aims to develop a financial market for social enterprises in Germany.¹⁰⁹

At the time of the writing of this study, the KfW had committed eight deals, with additional deals in the pipeline. To date, no investment in the education sector has been committed. The participating co-investors represent a broad range of players, including welfare organizations, social venture capital funds, and wealthy individuals. The financing program is designed as a pilot, which has just been prolonged for another year until the end of 2014.

Overall, the KfW development bank is very pleased with the quality and number of the applications and committed deals. The acceptance and feedback of both social enterprises and co-investors is very positive. While the KfW program helps social enterprises overcome the so-called 'valley of death', co-investors profit from risk sharing and a quality control. The program is further seen as a success as it allows the involvement of the established welfare organizations. For instance, the Diakonie Baden serves as a co-investor in one of the eight committed KfW deals.¹¹⁰ As such, it is a product combining both worlds: the welfare organizations and the social entrepreneurs that exist outside the established structures.

Ashoka, the world's largest support organization for social enterprises, also welcomes the initiative. Felix Oldenburg, managing director of Ashoka Germany, explains that this program serves as an international role model, as it would invite social investors to finance social enterprises in a way that is most suitable for their independent growth.¹¹¹ One of our interview partners acknowledged that the program might not yet be perfect, but also pointed out that it signals a paradigm shift.

However, we have also heard some criticism; for instance, that the program does not engage in smaller-scale investments. As explained above, the KfW program provides growth capital for social enterprises with a proven business model. It does not finance start-ups. The KfW development bank does offer loans of up to EUR 100,000 to start-ups with its KfW StartGeld.¹¹² This product is not available for non-profit organizations, however.

Another point of criticism was that it is very difficult to find investable deals in Germany. If one finds such a deal, the incentives to share the financial return are limited, especially because successful cooperation usually comes with high costs and a great deal of effort.

ii. Foundations

As briefly mentioned above, foundations are expected to be a driving force in the development of the impact investing market for a number of reasons. Impact investing allows foundations to leverage their philanthropic funds and recycle them for additional projects, yield social and environmental impact not possible with grants (e.g., build a credit history) and align the investment of their endowment with their mission.¹¹³ Such a combination of asset management and project work could serve as a multiplier of the impact a foundation can have – despite falling interest yields.¹¹⁴

Foundations in the USA and the UK have been practicing impact investing for several years.¹¹⁵ The supporting infrastructure and regulatory environment in these countries make it easier for foundations to engage in impact investing while complying with the legal requirements.¹¹⁶

Differences in legislation

US foundations are required by law to use at least five percent of their assets to support the foundation's charitable purposes.¹¹⁷ To ensure that this requirement does not lead to highly risky investments, so-called "jeopardy investments" are ruled out.¹¹⁸ US foundations may, however, make so-called program-related investments (PRI); that is, investments whose primary aim is to support the foundation's charitable purposes, which may involve greater risk and typically yield lower financial returns than traditional investment.¹¹⁹ Oftentimes, these program-related investments are made from the foundation's program budget.¹²⁰

In contrast, the German legislation gives priority to the preservation of capital.¹²¹ A foundation's investment activities may not lead to the reduction of its – real or nominal, depending on the federal state law – capital stock. This provision places high demands on an investment's financial return, risk and liquidity, and thus limits opportunities to use the capital stock for impact investments that do not provide for market-rate financial returns. No provision comparable to the US PRI provision exists in Germany, to date.¹²²

In principle, there is great potential for (educational) social impact investing in the German foundation sector. The German foundations' assets are estimated to amount to more than EUR 100 billion.¹²³ What is more, 15.3% of the German foundations engage in education according to their statutes.¹²⁴ However, very few foundations currently practice impact investing.¹²⁵ The reasons are manifold. First of all, many foundations are concerned about whether impact investing is in line with the founder's vision and the legal requirements, especially their fiduciary duties. Moreover, they are concerned about the risks (esp. loss of capital) associated with this unfamiliar investing practice. A lack of standardized investment products (esp. foundation-specific fund offerings), and (foundation-specific) advisory and rating services is exacerbating the situation. Direct investments, on the other hand, put high requirements on foundations' personnel in terms of time and level of expertise. Lastly, given the legal uncertainty, impact investments oftentimes require lengthy coordination with the regulatory authorities to ensure that they comply with the law. The foundations that do practice impact investing today typically invest in projects they have already been engaged with.¹²⁶

Examples of German foundations practicing impact investing include the Bewegungsstiftung, the BMW Stiftung Herbert Quandt, the Bürgerstiftung Dresden, the Eberhard von Kuenheim Stiftung, the GLS Treuhand e.V., the Schweisfurth-Stiftung, the Social Business Stiftung, and the Stiftung Nord-Süd-Brücken.¹²⁷ Both the BMW Stiftung Herbert Quandt and the Eberhard von Kuenheim Stiftung are invested in a tuition financing fund by Brain Capital.¹²⁸ Moreover, both foundations have reviewed their investment guidelines to provide more opportunity for impact investing and had a research agency (Oekom Research) review their investment portfolios. It is the foundations' explicit goal to foster impact investing in Germany and encourage other foundations, corporations, banks and profit organizations to engage in the discussion and investment practice.¹²⁹ The Stiftung Frühkindliche Bildung supports projects and initiatives related to early childhood education, child care and childhood education; it is planning to use 2% of its EUR 6 million endowment capital to provide loans to daycare centers in the future.¹³⁰ Lastly, the Auridis gGmbH has, amongst others, provided interest-free loans from its program budget to two social enterprises active in early child development; one of them being Kinderzentren Kunterbunt which will be featured in section 2.3.¹³¹

Moreover, the Benckiser Foundation – together with its subsidiary Juvat gGmbH – is currently implementing Germany's first social impact bond. The social impact bond will address the challenge of connecting a defined number of unemployed adolescents from a certain region that could not be reached by existing offers of the employment agencies to the labor market. The bond is expected to yield a financial return of three percent altogether.

DIGRESSION: What is a social impact bond?¹³²

A social impact bond is an innovative instrument to finance welfare and other social services.¹³³ Four key players are involved in the social impact bond model: A financial intermediary raises funds from private investors, which it passes on to the service providers so they can cover their operating costs.¹³⁴ The government, in turn, is obliged to make a payment to the financial intermediary if the previously agreed performance targets are met; the financial intermediary uses these funds to reimburse the investors and pay out a financial return.¹³⁵ Thereby, the level of the financial return depends on the amount of impact generated.¹³⁶ Illustration 5 illustrates this network of relationships.

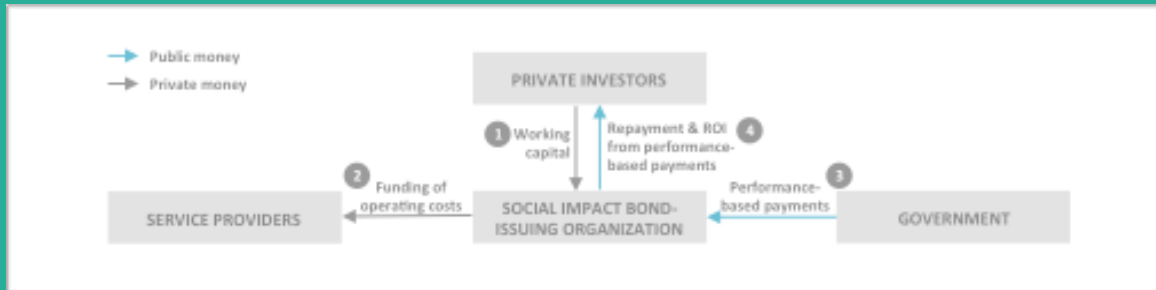


ILLUSTRATION 5: SOCIAL IMPACT BOND MODEL (LIEBMAN, 2011).

With a social impact bond, public funds are only utilized if there is a measurable impact; the financial risk lies with the private investor.¹³⁷ Despite their attractiveness, social impact bonds also come along with a number of challenges: Amongst others, one must identify an area where the achieved impact is great enough to justify the financial return for the private investors.¹³⁸ In addition, the impact must be reliably and credibly measurable and clearly defined, requiring a basis of comparison.¹³⁹ The impact measurement is particularly challenging if there is an attribution problem, for example, because the target group is participating in a number of different programs unrelated to the social impact bond.¹⁴⁰

The world's first social impact bond was launched by Social Finance UK with a volume of GBP 5 million in 2010 to fund a reentry program for short-sentenced prisoners leaving the UK's Peterborough prison.¹⁴¹ By the time of the writing of this report, fourteen other social impact bonds had been launched; twelve in the UK, one in Australia and one in the USA.¹⁴²

A recent study lists a number of measures that could help foster impact investing by German foundations. Among other proposals, it suggests that interested foundations seek discussions with the federal ministries and parliaments, as well as the regulatory and fiscal authorities (e.g., in the form of workshops or expert discussions) to inform them about impact investing and explain that foundations need more assurance that they comply with the legal requirements.¹⁴³ Ideally, this would lead to written recommendations or a manual on the legal situation; a role model is a guideline – “Charities and Investments Matters” – published by the UK Charity Commission in 2011.¹⁴⁴ Please note that other views exist according to which impact investing by German foundations is not permissible under the current regulatory framework and would require the adaption of the legal regulations.

Since the publication of the above-cited study, there has been significant movement in the field. In 2013, the Association of German Foundations (‘Bundesverband Deutscher Stiftungen’) brought to life a group of experts consisting of the chairmen of twelve German foundations, under the direction of the Eberhard von Kuenheim Stiftung, in order to discuss the potential for impact investments by German foundations and clarify the regulatory challenges. The insights from this group's conversations will be published in a guideline on impact investing for German foundations to be released in 2014. Given that social impact investment opportunities for foundations are very limited in Germany, the expert group is developing a pilot fund specifically suited to the investment needs of foundations. The pilot fund is being developed in consultation with the relevant regulatory authorities, auditors, etc. to ensure that the investment of a foundation's endowment capital in the fund is in line with the regulatory requirements. The fund will focus on social impact investments in the education space. The goal is to design the fund as a role model so it can be replicated (by others) for other impact areas

iii. Churches and religious organizations

Efforts to align religious beliefs with investment practices have existed for at least several hundred years.¹⁴⁵ Religious organizations were the first to set up responsible investment funds.¹⁴⁶ Just to give a few examples: In the UK in the early 1900s the Methodist Church launched a fund that avoided investments in specific sectors, and in 1984 the Quaker-affiliated insurance company Friends Provident established its Stewardship Fund.¹⁴⁷ In 1991, Germany's church bank EKK launched its KD Fonds Öko-Invest.¹⁴⁸ At the same time, religious organizations make up an attractive and important investment group given the financial resources they control and need to invest.¹⁴⁹

Lately, however, churches have come under pressure. As increasing numbers of people turn away from organized religion, churches' incomes suffer. Many churches are forced to compensate losses by seeking higher financial returns from their asset management, potentially crowding out social impact considerations. Moreover, special investment restrictions apply to German churches by law or statutes, including the requirement for investments to generate a positive return at a low risk level so that the nominal capital can be maintained and the requirement that investments can be liquidated short-term.¹⁵⁰

A study on the responsible investment practices of religious organizations across the world revealed that impact investing is relatively common among religious organizations, however; only, 23 percent of the surveyed organizations stated that they do not engage in impact investing.¹⁵¹ It is worth noting, however, that impact investing was defined quite broadly and included, for instance, enterprises with policies to promote fair trade or to make direct investments in developing countries. Community development (53%), microfinance (47%) and affordable housing (42%) were the most commonly cited projects.¹⁵² Moreover, the survey results suggest that many religious organizations are ready to accept lower financial returns when engaging in impact investing.¹⁵³

Unfortunately, no such study exists for the German market. Although Schaefer assessed the ethical investment practices of German non-profit organizations, including religious organizations, at the beginning of this century, the research does not allow for making inferences about social impact investing practices.¹⁵⁴ Accordingly, we know little about whether – and to what degree – religious organizations in Germany practice social impact investing.

iv. Other institutional investors

A research team from Tellus Institute has recently investigated the state of environmental, social and governance (ESG) investing by US college and university endowments. The study finds that “endowments on the whole look more like laggards than leaders in the institutional ESG investing space”.¹⁵⁵ The research team was not able to identify a college endowment that actively and materially engages in impact investing.¹⁵⁶ To the authors' best knowledge, no such study exists for German universities. As the USA are a pioneer in impact investing, similar results can be expected for the German market, however.

Non-profit organizations (NPOs) and non-governmental organizations (NGOs) also present possible social impact investors. Research shows that the general willingness of German non-profit organizations to integrate ecological and/or social investment criteria into the investment process is significant.¹⁵⁷ NPOs and NGOs are an interesting object of study in that they can fulfill the role of both investors and investees. As we have seen, a local branch of one of the welfare organizations, the Diakonie Baden, has engaged as a co-investor in the KfW financing program. Apart from this, we know little about the engagement of German NPOs and NGOs in social impact investing.

Despite the enormous sums of money they manage, pension funds and insurance companies appear to be marginal players in the social impact investing sector – both globally and in Germany. This can be ascribed to the fact that these players' investment activities are subject to very strict fiduciary duties and that the social impact investing market is in a very early stage of development. Pension funds and insurance companies are required to obtain a certain minimum financial return – difficult to secure given the oftentimes small and illiquid transactions. The authors were able to identify two German pension funds active in social impact investing in the education sector: the Versorgungswerk der Wirtschaftsprüfer and the Rheinische Zusatzversorgungskasse. Both are invested in study funds by Brain Capital. Chapter 2.2 describes the fund's business model in more detail. Institutional investors might further invest in property funds focused on real estate for childcare facilities and the like (see chapter 2.2 for more detail). Views differ, however, on whether such funds qualify as social impact investments.

Lastly, social impact investing could present an interesting avenue for other for-profit businesses. Thereby, one has to distinguish financial business entities (i.e. financial institutions) and non-financial business entities, which

manufacture products and/or provide non-financial services.¹⁵⁸ An example of a non-financial for-profit business engaging in social impact investing is the Tengelmann Group¹⁵⁹. Since 2009, Tengelmann Ventures GmbH, a 100% subsidiary of the Tengelmann Group, has been funding start-ups with a focus on e-commerce and social commerce concepts, market places as well as internet and web 2.0 technologies.¹⁶⁰ To our knowledge, the portfolio does not include a social impact investment in education. Similarly, the Deutsche Druck- und Verlagsgesellschaft (ddvg), a media holding company owned by the Social Democratic Party (SPD) of Germany, founded Tivola Ventures together with Christopher Koeppler.¹⁶¹ Tivola-Ventures provides growth capital to digital offerings with a social or societal impact in the area of sustainability, education, family, health, renewable energies, or environmental protection.¹⁶² In June 2013, Tivola-Ventures made its first investment in an online marketplace for sustainable products.¹⁶³

In terms of German financial intuitions, Deutsche Bank, for instance, launched a GBP 10 million impact investment fund in 2011.¹⁶⁴ This Impact Investment Fund I invests in social enterprises – inter alia in the education space – via intermediaries, and complements its CSR activities in the UK.¹⁶⁵ It does not include investments in Germany, however, and therefore does not constitute part of this analysis.

2.2. Intermediaries

Intermediaries are “organisations [that] broker supply into demand, as well as help create market demand”.¹⁶⁶ They are indispensable for a market to function efficiently as they facilitate transactions.¹⁶⁷

Emerson and Spitzer distinguish three types of intermediaries in the social capital markets: Financial intermediaries, exchange intermediaries and information and professional services providers.¹⁶⁸ We adopt this trichotomy, but substitute financial intermediaries with product providers, a classification we find more intuitive. This is in line with a framework on socially responsible investment markets by Benijts, where he explains that the “SRI market is bound by those individuals and organizations buying and selling socially responsible financial products”.¹⁶⁹ Benijts further explains that these products can be either investment funds or saving products (comprising savings accounts and deposits as well as certificates of deposit).¹⁷⁰

We will thus draw a distinction between product providers, exchange intermediaries and information and professional service providers. A recent study on the current state of impact investing in Germany offers a somewhat similar intermediary classification; it distinguishes between product providers, brokers and enablers.¹⁷¹

A. Product providers: As the term suggests, product providers are organizations that develop and market impact investment products to interested impact investors, i.e. the sellers of impact investing products. We further distinguish between product providers *with* a banking license and those *without* one.¹⁷² In the impact investing market, product providers with a banking license primarily comprise value banks and commercial banks, while the product providers without a banking license mainly consist of specialized asset managers.

B. Exchange intermediaries: Exchange intermediaries are organizations that bring together investors and investees but do not develop and market impact investment products. They include investment advisors, social stock exchanges and online platforms as well as investor networks and special events.

C. Information and professional services intermediaries: This last group of intermediaries forms a heterogeneous collection of players, which provide information and professional services to investors, product providers and exchange intermediaries as well as investees. This group comprises accountants, auditors and rating agencies, attorneys and consultants as well as universities, research institutes and lobby organizations.

The review focuses on players who explicitly aim to foster and support social impact investing. Again, the primary focus lies on social impact investments in the German education sector – defined broadly. Along the lines of Brown and Swersky¹⁷³ this review only considers traditional commercial players if they explicitly engage in social impact investing. That is, the analysis would, for example, exclude organizations that ‘accidentally’ make commercial loans to socially-motivated organizations as part of their general business activities.

A. Product providers

As stated above, product providers are organizations that develop and market impact investment products to interested impact investors, i.e. the sellers of impact investing products. We distinguish product providers *with* a banking license and those *without* one. We will first look at product providers with a banking license, namely, value banks and commercial banks. Subsequently, we will examine product providers without a banking license, that is, specialized asset managers.

i. Value banks

Value banks – also called alternative or sustainable banks – assume the same function as commercial banks in the traditional capital market: They take on deposits from savers and use the funds to provide loans to borrowers.¹⁷⁴ Given their focus on social sector activities, value banks typically have a superior understanding of existing business models and the specific needs and requirements of social sector investees vis-à-vis traditional banks.¹⁷⁵

The Social Investment Manual co-authored by the Technische Universität München and the Schwab Foundation for Social Entrepreneurship lists a number of value banks around the world. The list includes only one value bank with headquarters in Germany, the GLS Bank.¹⁷⁶ This is also the only German member organization in the Global Alliance for Banking on Values (GABV).¹⁷⁷ When searching for ‘Alternativbanken’ (the German translation for value banks) on Google, we find three other organizations with headquarters or branches in Germany: EthikBank, Triodos Bank and UmweltBank.¹⁷⁸ We will focus this review on the GLS Bank as it is Germany’s first social and ecological bank¹⁷⁹, considers itself a loan specialist in the education sector¹⁸⁰ and generally serves as a very good example of a value bank’s business model and product offering.

Founded in 1974, the GLS Bank (‘Gemeinschaftsbank für Leihen und Schenken’ which translates as “community bank for loans and gifts”) had a balance sheet of EUR 2.7 billion at the time of the writing of this study, an increase of 20 percent compared with 2011. The bank currently finances around 20,000 projects and businesses. Thereby, the focus lies on “cultural, social and ecological projects, which try to tackle challenges in our society by developing creative solutions”, including independent schools and kindergartens, institutions using therapeutic pedagogy, or projects for the unemployed. Savers can draw on the usual range of financial products, that is, current accounts, savings accounts, savings certificates, investment funds and bank membership. Savers can choose the area in which their money gets invested, including the education space. They further have the possibility to opt for reduced interest payments for their savings, allowing the GLS Bank to make loans to charitable projects at an interest rate only covering the basic loan administration costs of the bank (2.5% p.a. in 2013).¹⁸¹ The bank co-operates with GLS Treuhand and GLS Beteiligungsaktiengesellschaft (BAG). Founded in 1961, the GLS Treuhand¹⁸² (“GLS Charitable Trust Foundation”) is an association of almost 300 (as of May 2012) charitable organizations focused on fundraising, consultation regarding private legacies and transforming business into charitable capital. It acts as a charitable trust administering various foundations. With the five “Foundations for the Future” (‘Zukunftsstiftungen’) it is also engaged in the area of education (besides agriculture, development aid, healthcare and social welfare). GLS BAG, on the other hand, was founded in 1995 as a subsidiary of the GLS Bank. It assists companies seeking equity capital for renewable energy and the social economy. Its share capital amounts to EUR 3.2 million.¹⁸³ By the end of 2012, the GLS Bank had financed projects and organizations in the education sector, including independent schools and childcare facilities, with a volume of more than EUR 269 million, amounting to 19% of the overall financing volume.¹⁸⁴ As mentioned above, the GLS Bank considers itself a loan specialist in the education sector, its establishment actually goes back to the financing of a school.¹⁸⁵ Our interviews further revealed that the GLS Bank considers itself an impact investing pioneer in Germany.

ii. Commercial banks

Besides these specialized banks, conventional commercial and private banks have also started to realize that impact investing is a topic that is of great interest to their clients, especially to (U)HNWIs with an entrepreneurial background. Our conversations in the context of this study (and beyond) revealed that there seems to be a change in values – investors are actively looking to invest responsibly and, where possible, with an active social impact objective.

In Germany, commercial banks do not yet offer social impact investment products focusing on German investees in the social sphere. While the Berenberg Bank recently launched Impact Ventures UK, a closed-ended fund aim-

ing to raise GBP 30 million to be invested in impact investments with a focus on employability, education and child poverty amongst others, together with LGT Philanthropy, the social impact is to be created entirely in the UK.¹⁸⁶ The bank has no comparable product in place for the German space. Similarly, Swiss-based UBS recently launched an impact investing private equity fund with a volume of just over CHF 50 million.¹⁸⁷ Via the underlying funds, the fund of funds provides equity capital to small and medium-sized businesses (SMEs) in emerging and frontier markets active in healthcare, education and access to finance, amongst others.¹⁸⁸ The fund's first investment was in an education fund in India with the goal of providing low-cost, high-quality education to the emerging middle class.¹⁸⁹ Besides investing directly in the fund, investors may also co-invest with UBS outside of the fund and take part in the due diligence to learn about the process.¹⁹⁰

In the course of our interviews, the question emerged whether commercial banks are the right type of financial intermediary to launch social impact investment products. Given the tough regulatory requirements they have to comply with, it is easier for them to invest their own funds than their clients'. Although German commercial banks are interested in the field, there appears to be a strong view among some that specialized asset managers might be more suitable to develop social impact investing products.

Naturally, commercial banks are most likely to also serve social impact investees as a part of their overall business. However, there is no particular focus on this segment and no specialized offerings appear to exist.

iii. Specialized asset managers

Investment funds bundle funds from investors and invest these in certain asset classes, thereby reducing transaction costs and risks through diversification.¹⁹¹ Social impact investing funds do not yet exist across all asset classes in Germany to date. However, some real estate and social venture capital funds as well as decided thematic funds in the field of tuition have emerged over the last years.

- **Tuition financing funds**

A few investment funds exist in the area of education in Germany. The first group consists of tuition financing funds. We could identify three organizations offering such funds in the German market: Brain Capital GmbH, Deutsche Bildung AG and CareerConcept. All three aim to enable students to pursue an academic career independent of their socio-economic background. After graduation, students are committed to pay back the tuition fees through an income-dependent payback scheme. Brain Capital GmbH was founded in 2005.¹⁹² To date, it manages 15 funds with assets under management of almost EUR 60 million supporting more than 900 students at six universities.¹⁹³ Three pension funds, nine foundations and 150 individual investors¹⁹⁴ have provided capital; the Landesbank Baden-Württemberg (LBBW) provides collateral for the institutional investors.¹⁹⁵ The financial return amounts to approximately six to seven percent per annum.¹⁹⁶ Deutsche Bildung launched its second education fund in 2012. Equity investors contributed EUR 10 million, which are expected to be leveraged with debt investments of up to EUR 15 million. A predecessor of Deutsche Bildung launched the first fund in 2007, which will mature in 2015; it attracted equity investments of EUR 7 million. The financial return for the Deutsche Bildung funds amounts to approximately six to seven percent per annum.¹⁹⁷ Lastly, CareerConcept, which was founded in 2002, has implemented eight education funds, to date, and has a planned capital of approximately EUR 40 million.¹⁹⁸ The financial return also ranges between six and seven percent per annum like for the other two players.¹⁹⁹

- **Real estate funds**

Based on our research, we can attest a growing interest in investments in the real estate of organizations that would be considered social impact investees in the education space. Examples are the KinderWelten I & II funds by Luxembourg-based AviaRent Capital Management, which invests in real estate for early childhood care.²⁰⁰ The predicted continuous distribution for the funds is 7%, the target return 8% to 10% for a term of 10 years.²⁰¹ The same organization's EduCare I fund pursues the same business model but focuses on the set-up and/or purchase of schools (typically schools with an international orientation or private schools) and educational institutions (possibly including adult education) with a predicted dividend of 5.25 percent and a target return of 7-10 percent for a term of ten years.²⁰² Given that AviaRent is headquartered in Luxembourg

it does formally not form part of this market review, however.

Along the same lines, the German-based Habona Invest's Kita Fonds 01 invests in the real estate of daycare centers in Germany, which are then leased out to professional carriers.²⁰³ The fund volume amounts to approximately EUR 39.42 million, the minimum investment is EUR 10,000, the targeted return 5.5% percent p.a.²⁰⁴

It is debatable whether such investments should be considered social impact investments or not. While a recent study by the Centre for Social Investment (CSI) argues against it as the objectives of such real estate funds and, thus, the investors were primarily commercial and because they would not invest directly in the social enterprises but only in their real estate, one could also consider these investments financial first impact investments. This appears to be in line with Bridges Ventures' impact investing understanding, which considers its property funds thematic (rather than impact first) impact investments.²⁰⁵ Similar to AviaRent and Habona Invest, Bridges Ventures' newest property fund, the CarePlaces Fund, invests in the building of high-quality care homes for the elderly.²⁰⁶ According to the GIIN definition employed in this report, there is no foundation for why such real estate investments should not be considered impact investments, especially since the possibility to "make a lasting contribution to society with [one's] investment" is stressed in the marketing materials of these funds. A more narrow interpretation of impact investing – as appears to be dominant in the German market based on our interviews – might e.g. require the real estate to be lent at a preferential rate to the social enterprises. The mere development of real estate does not necessarily guarantee the development of affordable and high-quality (early child) education offerings accessible to all ranks.

- **Social venture capital funds**

Social venture capital funds are specialized social investment funds pursuing a venture capital approach. Called to life in the 1990s, social venture capital has gained increased media attention ever since.²⁰⁷ Just like their counterpart in the traditional capital market, social venture capitalists typically provide operational support and grant access to their networks aside from mere financial resources, oftentimes in the form of equity.²⁰⁸

Germany is home to two social venture capitalists, the Social Venture Fund and BonVenture. While BonVenture focuses on social enterprises in German-speaking countries (i.e. Germany, Austria and Switzerland)²⁰⁹, the Social Venture Fund invests internationally²¹⁰.

Founded in 2010,²¹¹ the Social Venture Fund invests in social enterprises in the growth and expansion phase with a proven and successful business model²¹² in the following fields: Alleviation of human suffering (e.g., fighting poverty, supporting orphans), work and education (e.g., innovative education concepts, training of marginal groups) and building of lasting means of subsistence (e.g., renewable energy, energy efficiency, sustainable agriculture, water supply).²¹³ The Social Venture Fund rules out any investments in turnarounds and pure measures of job preservation.²¹⁴ Debt and mezzanine capital are the most common forms of funding, although debt capital is only provided if it is combined with a participation in the organization's success (e.g., a convertible loan); equity investments typically take the form of preferred shares and minority investments and are only made if exit chances do exist (e.g., through a trade sale).²¹⁵ The fund's investors mainly include wealthy individuals and families, family offices, foundations, asset managers as well as church and development banks.²¹⁶ In terms of investments in the education sector, the Social Venture Fund is invested in Kinderzentren Kunterbunt, a nationally and municipally recognized non-profit community service institution that operates more than 30 daycare centers in Germany, which are adapted to the needs of working parents and whose services are offered at affordable market prices.²¹⁷ Kinderzentren Kunterbunt will be discussed in more detail in section 2.3.

Germany's first social venture capital fund, BonVenture, was founded in 2003 by a number of families.²¹⁸ The organization funds social enterprises in the start-up, early or expansion stage in Germany, Austria and Switzerland, which provide solutions and services in the following areas: Innovative social services and products for marginalized groups, employment and education as well as children, young people and the elderly; transparency and social development; ecology (new eco-friendly technologies and services, protection of nature and species, nutrition and consumer protection and environmental protection). Like the Social Venture Fund, BonVenture rules out investments in turnarounds and projects which merely aim to secure jobs. In addition

to equity, mezzanine financing and loans, BonVenture also provides grants. Its investments range between EUR 200,000 and EUR 1 million per project. Grants are typically available from EUR 10,000 to EUR 50,000. At the investor level, any profits are donated and re-invested. Investors are either limited partners or can make tax-deductible donations and charitable contributions.²¹⁹ BonVenture's portfolio comprises several organizations active in the education sector including bettermarks, Chancenwerk, Kinderzentren Kunterbunt and Rock Your Life.²²⁰ These organizations will be discussed in more detail in section 2.3.

B. Exchange intermediaries

Exchange intermediaries are organizations that bring together investors and investees but do not offer own impact investment products to impact investors. They include investment advisors, social stock exchanges and online platforms, as well as investor networks and special event

i. Investment advisors

Investment advisors who are specialized – or at least knowledgeable – in social impact investing are still rare in Germany. As previously mentioned, some product providers – most notably the social venture capital funds – have developed competencies to advise investors on social impact investing. Independent, specialist social impact investment advisory firms do not yet exist in Germany to date, however. Ashoka Germany has recently launched its Financing Agency for Social Entrepreneurs (FASE).²²¹ The FASE provides investors (and donors) access to an open pipeline of social impact investing deals, which it tries to match according to investor preferences.²²² So far, this pipeline is limited to Ashoka fellows, but it will be opened up to external parties in the near future.²²³

In the near term, advisors involved with SRI or philanthropy might extend their business scope and move into the related field of social impact investing. Possible entrants from philanthropy might include Phineo, Active Philanthropy or panta rhei. Phineo currently offers consulting services on which non-profit organizations and projects suit a particular donor's or foundation's philanthropic objectives.²²⁴ Active Philanthropy is a charitable organization that provides a platform for donors to exchange ideas and experiences.²²⁵ Panta rhei is a consultancy for foundations advising on the creation and management of foundations.²²⁶ A possible candidate from the SRI space is oekom research, a rating agency providing responsible investment services to a number of institutional investors (including churches, foundations, insurance companies) and financial services providers.²²⁷

ii. Social stock exchanges and online platforms

On a stock exchange, investors can readily buy and sell shares and bonds issued by companies, which in turn have access to a large pool of capital.²²⁸ As such, a fully functioning social stock exchange could be an attractive and efficient financing option for mature social entrepreneurs with a proven business model and a significant demand for funding.²²⁹

Currently, there are a number of initiatives underway to set up fully functioning social stock exchanges.²³⁰ Recent research has analyzed five emerging or existing impact investing exchange platforms, namely: Nexii (Mauritius), the Social Stock Exchange (London), the Impact Investment Exchange Asia (IIX; Singapore), the SVX (Ontario) and the Kenya Social Investment Exchange (KSIX; Nairobi).²³¹ The research reveals that all of these platforms operate as primary market facilitators; that is, they connect potential investors with (for-profit and non-profit²³²) investees, although non-profit investees are rare among these exchanges.²³³ Secondary transactions are expected to become available in the near future for shares of for-profit enterprises on some of these exchanges, namely Nexii, the IIX and the Social Stock Exchange, while IIX will also allow for the trading of bonds of non-profit enterprises.²³⁴ Currently, as a first step, the platforms serve as 'clearing houses', allowing investors to find impact investees.²³⁵ Moreover, currently opportunities tend to be more profitable, asset-backed investments.²³⁶ Interestingly, the majority of the platforms are delaying their launch dates as the regulatory process proves to be more complex than initially anticipated.²³⁷ Aside from the regulatory process, the valuation of social enterprises is another key issue.²³⁸

In Germany, a Berlin-based team is working on the development of a social stock exchange under the name NExT SSE (New Ethical eXchange and Technologies Social Stock Exchange) together with the Humboldt-Viadrina School

of Governance.²³⁹ The project team is in the process of preparing an online platform, which will feature social ventures looking for funding.²⁴⁰ The organization is also working out the legal requirements with the German federal financial supervisory agency, BaFin, to set up a ‘real’ stock exchange.²⁴¹

The above remarks show that current offerings rather resemble funding platforms. Such funding platforms fulfill the same role as stock exchanges – i.e. bringing together capital supply and demand – but do not allow for trading.²⁴² As mentioned above, a specialized platform that allows German investors to make social impact investments in German socially-motivated organizations does not yet exist: Betterplace, Social Impact Finance and Startnext do not (yet) allow for social impact investments that generate a financial return or at least repay the invested capital. Given the absence of social stock exchanges and funding platforms, there is limited transparency on investable opportunities in the German social impact investing market.

iii. Investor networks and events

As mentioned above, a specialized impact investor network has only been established very recently in Germany. In 2013, Germany’s first social business angel investment club has been founded under the name ‘Ashoka Angels Network’. So far, this network is only open to members of Ashoka’s Support Network (ASN). Yet, the investment club is supposed to be opened up to external members in the short term.

Besides this investment club, there are several events with the purpose of connecting impact investors and investees. One is ‘Social Business meets Angel’ organized by the BMW Foundation together with BonVenture, the Social Venture Fund and the Social Entrepreneurship Akademie.²⁴³ Additionally, evobis and netzwerk nordbayern organized a venture conference focused on innovative social enterprises on behalf of Germany’s KfW in January 2013.²⁴⁴ Ten social enterprises had the chance to make a pitch.²⁴⁵

C. Information and professional services providers

Information and professional services providers form a heterogeneous group of organizations providing support services for investors, intermediaries and investees. For our purposes, we distinguish between three groups of information and professional services providers. The first group consists of accountants, auditors and rating agencies, who “help market participants trust each other’s representations of value”, thus lowering transaction costs.²⁴⁶ The second group comprises attorneys and consultants. While consultants (e.g., HR or strategy) provide crucial services to make social sector organizations more effective and efficient and potentially investment-ready, attorneys lend their support with regard to legal issues, with a view to both the set-up of socially-motivated organizations and investment deal structuring. The last group consists of universities, research institutes and lobby organizations that help drive the impact investing discourse, support the development of critical infrastructure and make the concept known to the general public and, thus, potential investors.

i. Accountants, auditors and rating agencies

Accountants, auditors, and rating agencies “help market participants trust each other’s representations of value”.²⁴⁷ In this context, impact measurement is a key concern for impact investors. Accordingly, the Global Impact Investing Network (GIIN) is developing and promoting a common framework for the performance reporting of impact investments called IRIS (Impact Reporting and Investment Standards).²⁴⁸ IRIS is working in conjunction with the Global Impact Investing Ratings System (GIIRS)²⁴⁹, which follows a ratings and analytics approach similar to Morningstar investment rankings and Capital IQ financial analytics for the assessment of the social and environmental impact of companies and funds.²⁵⁰

Similarly, the Social Reporting Standard (SRS) originally developed by the Technische Universität München and the University of Hamburg aims to provide a “structure for the impact-orientated reporting of social activities”.²⁵¹ The SRS has been adopted by a number of key organizations in the German social impact investing market including Ashoka, Auridis, BonVenture, Phineo, and the Schwab Foundation.²⁵² To further build trust in the market, Phineo provides an independent evaluation of non-profit projects, accrediting those projects, which they consider particularly effective, with a quality seal.²⁵³ A rating agency assessing both financial and non-financial aspects does not yet exist in Germany based on our research. Our interviews revealed that such a rating scheme would be particularly beneficial for foundations as it might allow them to avoid lengthy clarifications for individual investments to ensure that they comply with the legal requirements.

ii. Attorneys and consultants

Ashoka is one of the key promoters of social entrepreneurship in Germany. It provides its fellows with financial as well as non-financial support. With a view to the latter, Ashoka connects its fellows with its pro bono partners who provide legal support, strategy consulting, and communications trainings as well as infrastructure and office space.²⁵⁴ In 2012, Ashoka co-founded Talents4Good, a recruitment agency for jobs and projects with a social impact.²⁵⁵

Moreover, Ashoka's FASE does not only provide investment advice to investors but also offers consulting to social entrepreneurs. It helps social enterprises become investment-ready, advises them regarding an appropriate financing strategy and mix, supports the development of necessary documents (e.g., information memoranda), identifies and contacts potential investors and coordinates and accompanies the financing process including the negotiations.²⁵⁶ Thereby, the FASE aims to build innovative, hybrid financing structures bringing together philanthropy and social impact investors²⁵⁷, covering the entire spectrum of available financiers, including business angels, family offices, foundations, banks, corporations, and public authorities.²⁵⁸ Such innovative hybrid financing structures might allow social impact investors to invest in organizations that might not be investable otherwise. The innovative financing structures will be made public to serve as role models and encourage similar deals, thereby reducing transaction costs.²⁵⁹ So far, the FASE's services are limited to Ashoka fellows; they will also be offered to other social enterprises in the near future, however.²⁶⁰ FASE's activities work against the limited pipeline for social impact investments in Germany – be it because of a lack of investment-ready investees, or unattractiveness of existing investor offerings. Based on the belief that the mere feed-in of additional investment capital is not sufficient to build a flourishing social impact investing market in Germany, the FASE tries to find investment instruments that suit the specific situation of the investee.

Besides Ashoka, there are a few other organizations in Germany that offer support to socially-motivated organizations. One such example is iq consult, an Ashoka fellow. Iq consult supports social enterprises with a number of services related to the founding and management of social enterprises.²⁶¹ Similarly, Phineo offers a complementary analysis of non-profit organizations with a view to their impact orientation, advantages and disadvantages of the organizational structure, or control mechanisms.²⁶² Another example is the Social Entrepreneurship Akademie, a cooperation of the four university-based entrepreneurship centers in Munich, which aims to educate social entrepreneurs and changemakers through qualification programs and trainings as well as start-up consulting and coaching.²⁶³

iii. Universities, research institutes and lobby organizations

A number of German universities have begun including impact investing in their research agendas. (This report, for instance, was written by a PhD candidate in impact investing together with her supervisor from the University of Hamburg.) The Technische Universität München has developed a social investment manual for social entrepreneurs together with the Schwab Foundation for Social Entrepreneurship²⁶⁴ and is engaged in research on social investment, especially social venture capital. As mentioned above, the University of Hamburg and the Technische Universität München have also co-developed the Social Reporting Standard (SRS). A number of other universities are involved in research on social entrepreneurship and/or social investment, including, amongst others, the University of Heidelberg (Center for Social Investment), the Leuphana University in Lüneburg, the European Business School in Oestrich-Winkel and the Zeppelin University in Friedrichshafen.

In terms of lobby organizations, the Global Impact Investing Network (GIIN) is clearly the most prominent global player. In Europe, the European Venture Philanthropy Association (EVPA) promotes the expansion, effectiveness and impact of venture philanthropy and social investment throughout the continent. So far, no such lobby organization for impact investing exists on a national level. Ashoka (especially with its FASE), the Bertelsmann Foundation, Impact in Motion, or the Association of German Foundations (including a few pioneering foundations) have probably come closest to such an organization. While much has been said about Ashoka and FASE and the Association of German Foundations, we would like to provide some more detail on the work of the Bertelsmann Foundation and Impact in Motion at this point.

The Bertelsmann Foundation is a member of the GIIN and has just signed an open letter on the occasion of the G8 Social Impact Investment Forum in London in June 2013 together with more than 90 other foundations, inves-

tors, financial services providers and development agencies from around the world. In this letter the Bertelsmann Foundation argues in favor of a close collaboration between governments and private investors to develop an international impact investing market. With its project ‘Social Investment: Financing Social Change’ the foundation aims to better understand the necessary requirements for social investments to benefit the public and social sector. The goal of the project is twofold. On the one hand, the foundation aims to “build a better understanding and awareness of social investment and to assess the opportunities and limitations that social investment approaches present to relevant stakeholders” based on roundtables with different stakeholder groups and through the production and targeted dissemination of background research, surveys and analyses. On the other hand, the Bertelsmann Foundation conducts feasibility studies to analyze specific areas of application for social investment, especially the potential of social impact bonds in Germany. Thereby, the focus is on four areas: the rehabilitation of young ex-offenders, the transition from education and training into the labor market, the system of care for the elderly and services for children, and young people and their families. In June 2013, the Bertelsmann Foundation brought together around 30 banks to discuss the potential for impact investing from the viewpoint of German financial services providers and investors. It further organized an international workshop on social investment together with the OECD in Berlin in May 2013.²⁶⁵

Impact in Motion promotes impact and mission investing in Germany and Europe. To this end, Impact in Motion pursues three strategies. Firstly, it conducts research and launches publications on impact and mission investing. As such, Impact in Motion published the first German studies on both impact²⁶⁶ and mission investing²⁶⁷. It is currently working on a feasibility study for social impact bonds in Germany. Secondly, Impact in Motion talks about impact and mission investing at conferences and events, brings together relevant actors and supports with consulting services. Lastly, Impact in Motion pioneers the impact investing market in Germany through the implementation of lighthouse projects, such as the Social Venture Fund.²⁶⁸

2.3. Investees

It is beyond the scope of this research to provide a complete map of the social impact investment opportunities in the German education sector. Instead, we intend to illustrate the spectrum of (possible) investments and highlight a few successful examples demonstrating that social impact investing does have (at least some) potential in the sector.

As mentioned in the introduction, a clear-cut definition of impact investing is lacking and understandings vary. A more narrow view might limit impact investments to social organizations such as charities and private enterprises with an explicit social purpose and a limited constraint on the profit distribution to shareholders.²⁶⁹ Such a view excludes the majority of private sector organizations, especially those who aim for profit maximization, and coincides with Big Society Capital’s scope of market activity.²⁷⁰ A broader understanding of impact investing might not put any limitations on the receiving organization – aside from intent for non-financial impact – but define impact investing as solving societal problems and creating non-financial impact. In one way or another, both non-profit and for-profit organizations may qualify as recipients of impact investment capital.

Moreover, the social entrepreneurship movement has led to a blurring of sectors. Elsewhere, new legal forms – such as the UK’s Community Interest Company (CIC) or the US Benefit Corporation (B-Corp) and Low-profit Limited Liability Company (L3L) – have emerged. In Germany, no such specialist legal form for social entrepreneurship organizations exists to date; social entrepreneurs oftentimes get by with hybrid structures combining non-profit and for-profit legal forms to accommodate the needs of the different types of financiers.²⁷¹

As previously mentioned with regard to the tuition financing funds (see section 2.2), individuals may also qualify as social impact investees. Accordingly, our framework lists individuals as well as non-profit, for-profit and hybrid organizations as potential investees.

It appears to be a common view that there is little room for market-based solutions to social problems in Germany given the strong and established welfare state. This is in line with findings by the Boston Consulting Group (BCG), which attributes the immature state of the German social impact investing market to the strong state provision of social services.²⁷² This is particularly true for the education sector with its established players and structures, the oftentimes complementary services and the inability or unwillingness of the target group to pay for the received services. As such, it is not surprising that a lack of investable opportunities has been oftentimes cited as a key barrier for more social impact investing in Germany. We have also heard this more than once during our expert interviews.

Examples of current social impact investments in the German education sector

In general, investable social enterprises that can deliver a financial return appear to be limited in Germany.²⁷³ This may be partly due to the high impact typically expected from a social entrepreneur or impact investee.²⁷⁴ Nevertheless, there are a few lighthouse social enterprises in the German education sector that have managed to attract impact investing capital. We present several examples below.

Kinderzentren Kunterbunt is one of the showcase examples for hybrid financing models in Germany. Organized as a charitable limited liability company (gGmbH), it aims to provide childcare services geared to working parents, offering extended, flexible and year-round opening hours.²⁷⁵ Accordingly, this organization not only addresses the shortage of daycares in Germany (which becomes especially apparent with the guaranteed daycare for under-threes operational as of August 2013), but also the challenges working parents face with existing offerings.²⁷⁶ The organization aims for a self-supporting financing model based on contributions from parents and their employers, annual membership fees from its circle of supporters and subsidies from municipalities, federal states and the federal republic.²⁷⁷ Both the Social Venture Fund (with EUR 1 million²⁷⁸) and BonVenture have invested in Kinderzentren Kunterbunt. Furthermore, the foundation Auridis provided an interest-free loan to the organization (see section 2.1).

As mentioned above, BonVenture has a number of other education-related social entrepreneurs in its portfolio, including bettermarks, Chancenwerk, and ROCK YOUR LIFE! While Chancenwerk and ROCK YOUR LIFE! have non-profit legal forms, bettermarks is organized as a regular limited liability company.

Chancenwerk e.V., a registered society, was established to help disadvantaged pupils of all cultural backgrounds succeed at school. Based on the notion that role models have a positive effect on young people's educational success, Chancenwerk has developed an innovative, self-supporting mentoring program. Under this program, seniors receive two private coaching lessons per week from university students free of charge. In return, they support younger pupils with their homework. For this service, the younger pupils pay EUR 10 per month (16 sessions).²⁷⁹ BonVenture supports Chancenwerk through a milestone-dependent loan.²⁸⁰

ROCK YOUR LIFE! gGmbH (a charitable limited liability company) organizes coaching partnerships between pupils in their last two years of 'Hauptschule' (lower secondary level schools) and university students. It is the stated objective of these mentoring relationships to motivate the Hauptschul-pupils to enroll for training courses for jobs they may be interested in. ROCK YOUR LIFE! aims to make a contribution towards greater social mobility and more equal educational opportunities. A support network of partner companies provides traineeships and internships.²⁸¹ By November 2013, BonVenture held ten percent of the shares of the gGmbH.²⁸²

Bettermarks GmbH, a conventional limited liability company, offers an online learning system, which makes it easier for pupils to study mathematics at home. One of Bettermarks' objectives is to improve the skills in mathematics, regardless of a student's socio-economic background, and without having to resort to expensive private tuition.²⁸³ BonVenture supports Bettermarks through an equity investment.²⁸⁴ Besides BonVenture, a number of other private investors have invested in Bettermarks, including the KfW, and the media companies Holtzbrinck and NZZ.²⁸⁵

The GLS Bank had financed over EUR 269 million (19% of the overall financing volume) in projects and organizations in the education space by the end of 2012. Examples in Germany include the daycare center Kila Kindertraum Prenzl'berg (a registered society), the Aktive Schule Leipzig (a registered society) or the Freie Schule Bredelem (its carrier Bildung, Leben und Natur e.V., is organized as a registered society).²⁸⁶

In general social impact investments in education comprise the creation of affordable daycares to address the scarcity of childcare centers and thus solve an important societal issue in Germany, the financing of independent schools, educational publishing houses, advanced training institutions or non-profit organizations working in education.²⁸⁷ Similarly, a recent report on social entrepreneurship in Germany considers, among other projects, daycare centers, independent schools and labor market integration offerings as social entrepreneurship activities and potential targets for social impact investors.²⁸⁸

One can observe a growing interest in investments in the real estate of organizations that could be considered impact investees in the education space. Funds like KinderWelten I & II by AviaRent or Kita Fonds 01 by Habona Invest invest in the real estate of daycare centers in Germany. It is debatable whether such investments should be considered social impact investments or not. While a recent study by the Centre for Social Investment (CSI) argues against it as the objectives of such funds and, thus, the investors were primarily commercial and because they would not invest directly in the social enterprises but only in their real estate, one could also consider these investments financial first investments as described in the introduction just like Bridges Ventures deems its property funds impact investments.²⁸⁹ According to the GIIN definition,

there is no foundation for why such real estate investments should not be considered social impact investments, especially as the possibility to “make a lasting contribution to society with [one’s] investment” is stressed in the marketing materials of these funds. A more narrow interpretation of impact investing might require the real estate to be lent at a preferential rate to the social enterprises. The mere development of real estate does not necessarily guarantee the creation of affordable and high-quality (early child) education offerings accessible to all ranks.

Making ‘uninvestable’ organizations investment-ready

Market-based, self-sustaining business models are rare in the education space, or at least in some fields of it²⁹⁰, either because of the extensive offerings on the part of the welfare state, or the inability to pay on the part of those who need those services most (e.g., under-educated sections of the population or children from educationally disadvantaged backgrounds). However, impact investing aims for a financial return (or at least the return of the invested principal), which requires the generation of a financial surplus on the part of the investee.

The new Financing Agency for Social Entrepreneurship (FASE) aims to overcome this issue by providing support for the development of investable business models and designing hybrid, layered investment structures tailored to the individual organization. The latter may include a combination of donations and social impact investments, and may enable investors with stricter regulatory requirements to engage in social impact investing. The FASE could thus be said to follow the view expressed by the directors of Ashoka, Mark Cheng and Felix Oldenburg: one “should start from what it takes to help the solution grow rather than what it takes for the solution to fit the investment.”²⁹¹ Other organizations such as the Social Entrepreneurship Akademie (SEA; see section 2.3) also support the creation of viable social entrepreneurship business models.

Furthermore, performance-based payment schemes such as social impact bonds (see information box in section 2.1) might make it possible to channel private investment into organizations that would otherwise not be investable. In the UK, the Department for Work and Pensions’ Innovation Fund was launched in 2012 to support payment-by-results programs aiming to get disadvantaged adolescents into further education and employment.²⁹² The program comprises ten separate social impact bonds, which differ in size and scale.²⁹³ As seen above, a social impact bond targeting the (re-)integration of unemployed adolescents into the labor market is currently being implemented in Germany. Other areas of application could be the reduction of absenteeism in schools (approx. 3% of all students in Germany (i.e. more than 300,000) are estimated to be absentees²⁹⁴), the prevention of high-school drop outs (8% of the students per age group²⁹⁵) or the prevention of adolescents without a training qualification (approx. 150,000 per year²⁹⁶). In all three cases, effective offerings, robust outcome metrics, data for comparison, and a clearly defined target group do exist. Moreover, the topics are of great interest to both the public sector and potential private investors. Lastly, the associated costs might be relatively small compared with the potential public sector value, both in ideological and financial terms. For every age cohort for which the number of adolescents without a training qualification cannot be halved, the resulting follow-up costs were recently estimated to amount to EUR 1.5 billion on the part of the government budget, for example.²⁹⁷ This last point is an important one: obviously, the transaction costs of a social impact bond have to be carefully assessed and compared, and cannot outweigh other (traditional) forms of financing.

In principle, the different stakeholders in Germany seem to welcome the idea of social impact bonds. For the public authorities, they provide a risk-free means to finance additional and experiment with new interventions to address the country’s social challenges. As such, there seems to be a general openness to the idea. For potential investors, social impact bonds may provide a relatively secure impact investment product (if structured, for example, like the social impact bond in New York City where Bloomberg Philanthropies provided a loan guarantee so that Goldman Sachs will be repaid a portion of its loan, independent of the program’s outcome²⁹⁸; otherwise, the financial risk associated with a social impact bond may be in fact relatively high). For investees, social impact bonds open up an additional financing source and provide a means to compete with the established welfare organizations, which are oftentimes seen to be treated preferentially by the public authorities.²⁹⁹ Naturally, it remains to be seen how readily social impact investors will embrace social impact bonds in Germany and how the initial pilot programs will perform.

It must be noted, however, that not all social organizations are willing to take on investment capital. There are concerns about the risks associated with investments, whether it’s the inability to pay back a loan, the unwillingness to take on shareholders and give up voting rights, or the fear that investments might scare away volunteers and donors. Such a stance is legitimate. Nevertheless, independent advice should be available for organizations that do seek assistance.

2.4. Overview of German (educational) social impact investing landscape

Illustration 6 summarizes the above findings. The illustration integrates (some of) the identified players active in the German social impact investing market in the education sector in our proposed framework.

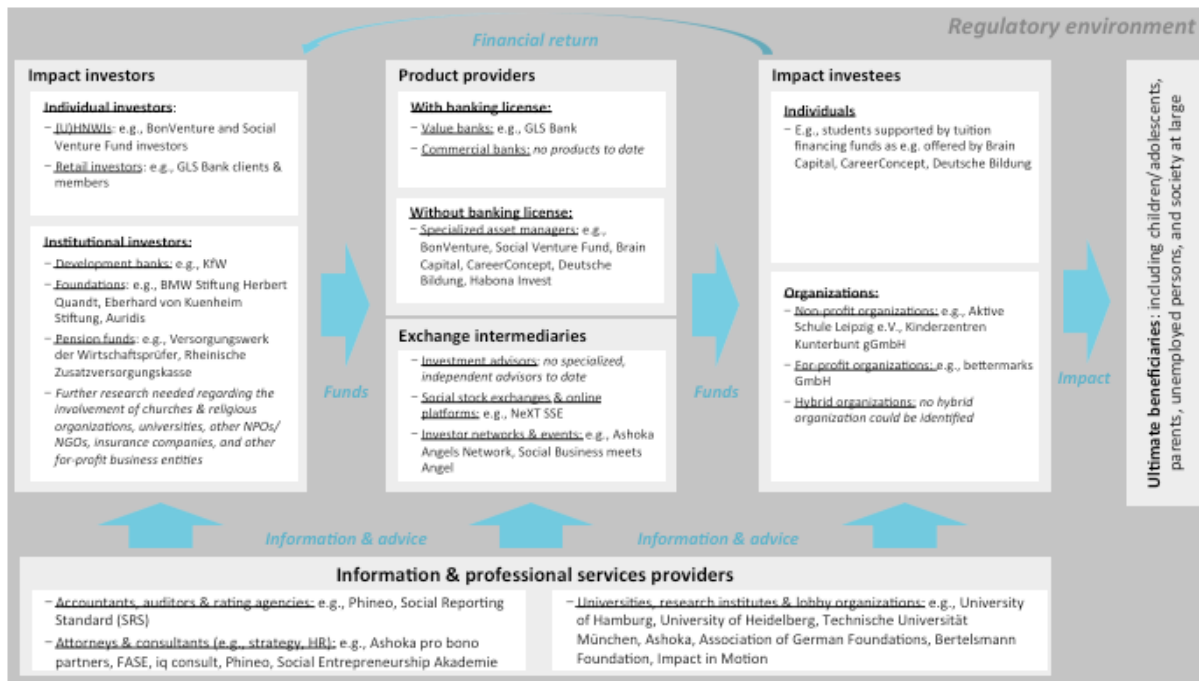


ILLUSTRATION 6: PROMINENT PLAYERS IN THE GERMAN (EDUCATIONAL) SOCIAL IMPACT INVESTING MARKET.

3. ROLE OF THE GOVERNMENT

3.1. Germany

Germany's National Engagement Strategy

In October 2010, the German Cabinet adopted the National Engagement Strategy ('Nationale Engagementstrategie'), which pursues four strategic goals: better alignment of activities to foster social engagement on the part of the federal government, the federal states and the municipalities, active involvement of foundations and commercial enterprises, greater recognition of volunteers and better general conditions for volunteer work.³⁰⁰

The policy acknowledges the important role social entrepreneurs play in the field of social innovation and recognizes that social entrepreneurs and social entrepreneurship stakeholders, such as impact investors and support organizations, have not been systematically engaged in the dialogue about social innovation and engagement, thus far.³⁰¹ It is the explicit goal of the National Engagement Strategy to support social enterprises and improve the general conditions for their work.³⁰²

A number of activities have resulted from the National Engagement Strategy. The Federal Ministry of Family, Senior Citizens, Women and Youth (BMFSFJ) organized a Multi-stakeholder Conference on the subject of 'Encouragement and Dissemination of Social Innovations in Germany' ('Förderung und Verbreitung von sozialen Innovationen in Deutschland') with approximately 200 participants from politics, public administration, foundations, welfare organizations, social enterprises, academia and the business community in February 2013.³⁰³ In order to improve the general conditions for social entrepreneurship and the dissemination of social innovation, a number of initiatives were being discussed and will be further developed and implemented by the BMFSFJ together with relevant stakeholders, namely:

1. Further development of social incubators that consult social innovators from the beginning, coach and help them navigate relevant networks.

2. Further dissemination of a social reporting standard, which documents the impact of social innovations.
3. Leverage of the support potential of foundations in scaling social innovations.
4. Assessment how to foster the cooperation between the established welfare organizations and social entrepreneurs.³⁰⁴

Against the backdrop that appropriate financing for social entrepreneurs – especially growth capital – was limited³⁰⁵, the BMFSFJ mandated the KfW development bank to develop a financing program for social entrepreneurs.³⁰⁶ The program was launched in January 2012.³⁰⁷ Please see chapter 2.1 for more information on the KfW financing program.

Developments on the federal state and municipality level

As mentioned above, the Benckiser Foundation – together with its subsidiary Juvat gGmbH – is currently implementing Germany's first social impact bond in close collaboration with the municipalities and the federal state of Bavaria. Despite Germany's federal structure – which gives significant power to the federal states – we were not able to identify any other material impact investing activity in the education space at the federal state level. This is particularly surprising given that educational policy is generally in the purview of the federal states. It can be expected that more municipalities and federal states will become involved as more social impact bonds are being developed, however.

3.2. European Union

Social Business Initiative

The European Commission's Social Business Initiative was established as part of the Single Market Act, which was adopted in 2011 to spur the European economy and create jobs.³⁰⁸ It is the aim of the Social Business Initiative to create an environment, which is conducive to the creation of social businesses.³⁰⁹

As such, the initiative comprises three sets of priority measures:

1. Measures to improve access to funding for social businesses
2. Measures to improve the visibility of social businesses
3. Measures to improve the legal environment of social businesses³¹⁰

With a view to the first priority, that is, improved access to funding for social businesses, the Commission proposed four key actions³¹¹:

1. Development of a European regulatory framework for European Social Entrepreneurship Funds
2. Promotion of microcredit in Europe
3. Development of a European financial instrument to improve access to funding for social businesses
4. Introduction of an investment priority for social enterprises in the ERDF³¹² and ESF³¹³ regulations

The European Social Entrepreneurship Fund legislation (EuSEF) was adopted by the European Parliament in March 2013. This legislation introduces a new European Social Entrepreneurship Fund label that aims to facilitate cross-border fundraising. Eligible funds can be marketed across the European Union ("pan-EU marketing passport") as long as they comply with the EuSEF criteria. They must allocate the majority of their investible capital (at least 70%) to "Social Undertakings" (i.e., social sector organizations). It must be the explicit focus of the fund to make a measurable and positive social impact with its investments. The funds must further institutionalize procedures to monitor and measure the social impact of their investments and comply with transparency requirements regarding their investment policy, targets, manager compensation and profits.³¹⁴ The European financial instrument will become operational in 2014 and will comprise EUR 85 million to be dedicated to social entrepreneurship over the period of 2014 through 2020.³¹⁵

To support social enterprises, the European Investment Fund (EIF) has launched the Social Impact Accelerator (SIA), which is “the first pan-European public-private partnership for social impact investing”, together with a number of private sector investors, including Crédit Coopératif and Deutsche Bank. This fund of funds, aiming to mobilize an initial EUR 60 million, is a pilot, which aims to provide social enterprises with equity financing. It further strives to strengthen the existing market infrastructure for social impact investing.³¹⁶ As such, it fulfills a similar role as Big Society Capital.³¹⁷

4. OBSTACLES AND OPPORTUNITIES FOR SOCIAL IMPACT INVESTING IN THE GERMAN EDUCATION SECTOR

The above sections show that the social impact investing market is still in its infancy in Germany and driven by a relatively small number of players – not only in the education sector. This is in line with findings by the Boston Consulting Group (BCG). To assess the maturity of different social impact investment markets, BCG developed the International Social Impact Investing Index (ISI³), which assesses a market along four dimensions: 1) market activity, 2) quality of the market infrastructure and technologies, 3) range of financial products available and 4) strengths of the policy and regulatory framework.³¹⁸ According to this index the German social impact investment market is in its early stage of development similar to that of France, Japan and Italy; the UK and the US are the leaders in the field – the former as the clear market leader, the latter as a fast follower.³¹⁹ Australia, Israel and Canada are found to be emerging social impact investment markets and, thus, more developed than the German market.³²⁰

In this last section, we describe some challenges and opportunities to social impact investing in the German education sector and point to a few promising avenues the German government might consider to promote social impact investing – generally and specifically to combat education-related challenges.

4.1. The potential for social impact investing in the German education sector

Overall, the views regarding the potential for social impact investing in the German education sector are mixed. There is broad consensus that unequal educational opportunities and issues resulting from poor education such as (long-term) unemployment and relative poverty are among the greatest issues Germany is struggling with. There is further agreement that public funds and philanthropic giving might not be sufficient to solve these issues and that traditional activities and structures might not be enough to deal with these problems effectively and efficiently. Targeted social impact investments complementing the government’s activities would not only free up additional financial resources to deal with these problems but might also lead to a greater results-orientation and foster experimentation with new approaches and different service providers.

On the other hand, there also appear to be a number of hurdles for social impact investing in the German education sector:

- It might be difficult for market-based offerings to succeed given the competition with the **established welfare institutions** that have an extensive infrastructure. This presents a key difference to many developing countries and emerging markets and, in parts, also to the Anglo-Saxon countries. In some of these countries social security systems tend to be less comprehensive or social services are largely delivered by the private sector.³²¹ Although the established welfare organizations may support the scaling of social entrepreneurship (as is, for example, the case with the Eltern AG³²²), they may also present an impediment for market-based models. First of all, the established welfare organizations typically have an advantage in the “quasi markets” and public tenders due to their nationwide infrastructure and scale.³²³ Secondly, there might be resistance from various stakeholders towards new players. The local public administration, for example, might have a preference for how things are currently done (i.e. a status quo bias).³²⁴ At the same time, established social services providers might come under pressure if social entrepreneurs are able to provide more effective and/or less expensive social services or preventive measures.³²⁵
- Another impediment for market-based models in the education space is the limited **willingness to pay for educational services** as these are oftentimes available free of charge. Moreover, those, who need the services most (e.g., children from educationally disadvantaged backgrounds), might not have the **ability to pay** for the services.

- The **assessment of interventions in the education space** is challenging. On the one hand, effects often only become visible in the long-term and are typically complex to measure. On the other hand, there might be an attribution problem, that is, the target population might be exposed to a number of interventions, which makes it difficult to assess the effectiveness of the different measures. This presents a particular challenge to the development of social impact bonds.
- Social impact investments in education might face particular **problems given the German federal system**. Schooling and education are within the domain of federal states rather than the federal republic. This might make it particularly difficult for performance-based schemes like social impact bonds. Those who have to pay for an intervention might not be the ones who will ultimately benefit most from the cost savings.
- Lastly, there are **ethical problems** related to social impact investing in Germany. There appears to be a general distrust against the ‘economization’ of the social economy among the German population. Given the comparatively high taxes, the Germans generally expect the state to address social issues and provide social services. Unlike in the USA or the UK social impact investing has a negative connotation in Germany; profit-making from solving social issues is considered unethical, even if it is only marginal and far below the corresponding market rate.

Nevertheless, there might be room for impact investing in the German education space, especially because it is an area of great interest among both philanthropists and foundations. This potential might not lie in the core activities the government has a legal obligation to fulfill. According to our conversations and secondary research, the potential might rather lie in support activities and preventive measures for which public funds are limited or not available at all, although the consequential charges must be borne by the state. As seen above, such activities could aim for the reintegration of absentees into the school system, the labor market qualification of disadvantaged adolescents or long-term unemployed, and the like.

Yet, there are a number of organizations whose business model might not be sufficient for them to break even. This might be particularly true for the education sector. Performance-based payment schemes like social impact bonds are therefore considered a potentially effective avenue to help solve education-related issues in Germany, such as the reintegration of the unemployed into the labor market. For the public authorities they provide a risk-free means to finance additional, and experiment with new, interventions to address the country’s social challenges. For potential investors social impact bonds may provide a relatively secure impact investment product (if structured, for example, like the social impact bond in New York City where Bloomberg Philanthropies provided a loan guarantee to Goldman Sachs³²⁶). For investees they open up additional financing and provide a means to compete with the welfare organizations, which are oftentimes seen to be treated preferentially. Naturally, it remains to be seen how readily impact investors will embrace social impact bonds in Germany and how the first pilots will perform. It is also crucial to note that the transaction costs of a social impact bond have to be carefully assessed, compared and cannot outweigh other (traditional) forms of financing.

Impact investing is not a replacement of the welfare state; social impact investments might effectively complement government activities. As such, it is important to involve the established players and leverage the existing structures, especially the welfare organizations. For instance, under its financing program the KfW made a co-investment together with the local branch of a welfare organization. We believe this is a promising sign. Welfare organizations might be particularly interested in preventive and support measures for which public financing is limited – both as investors and investees.

4.2. How the government could promote social impact investing

This study shows that the government’s engagement in the social impact investing discourse has been very limited, to date.³²⁷

The Engagement Strategy and the resulting Multi-stakeholder Conference were a first step in anchoring the social entrepreneurship discourse at a national level, also touching upon financing aspects. Furthermore, the Federal Ministry of Family, Senior Citizens, Women and Youth (BMFSFJ) mandated the KfW development bank to develop a financing program for social entrepreneurs, launched in January 2012 (see section 2.1).³²⁸

In our conversations, the limited involvement and interest in social entrepreneurship and social impact investing on the part of the political parties, individual members of the Parliament and the ministries has been criticized by some. The German government is perceived as passive; the dialogue around social impact investing has occurred sporadically, and (mostly) in the absence of government representatives. Germany is far away from a disciplined public dialogue on social

impact investing as it is being carried on in the UK. However, it appears to be the common view that the UK model is not transferable par for par and that such a centralistic top-down approach might not be feasible – or even advisable – in Germany, inter alia due to the country's federal structures. Nevertheless, access to politicians at both the national and federal state level is deemed critical for the development of a flourishing social impact investing market in Germany by most.

Based on our conversations and secondary research two main areas emerged how the German government and federal states could promote social impact investing – at large and specifically in the education space. On the one hand, it could initiate discourse and assess the potential for social impact investing in Germany. On the other hand, the government could support sector building, for which a number of specific measures were suggested including more flexibility for foundations, tax incentives for social impact investments and the creation of more investable opportunities. Opinions regarding the desired involvement of the government and the effectiveness of such an involvement differed, however.

Initiate discourse and assess potential for social impact investing in the specific German context

The government faces a number of options of initiating dialogue. One of the easiest ways is by commissioning research reports. It could further set up a social impact investing taskforce as has been done, for example, in the UK or Canada. Alternatively, the government could convene roundtables bringing together a larger and broader group of stakeholders at regular intervals to discuss the potential for social impact investing in Germany. Such a series of events could be designed similarly to the Multi-stakeholder Conference and should involve national ministries and politicians, the federal states and municipalities, the welfare organizations, private investors, financial intermediaries, investees and academics. Potentially, it would make sense to anchor these roundtables on the federal state – rather than the national – level given Germany's federal structure.

Research reports, a social impact investment task force and/or regular roundtables could help develop a context-specific social impact investing understanding for the German market. Amongst others, they might address questions such as:

- How should social impact investing be defined? Should it, for instance, be defined around organizational characteristics of the investee (e.g., a primacy of social objectives and the existence of a limited distribution constraint³²⁹), or should it rather follow the KfW approach, which focuses on the solution of societal problems but does not require a primacy of the non-financial mission or a limited distribution constraint?
- In which areas is there need and potential for social impact investing in Germany? Should and could social impact investments be used to finance services which are currently provided by the government or should they rather be used to finance interventions that would not be provided otherwise? Should and could social impact investments be used to deliver services which are guaranteed by the government or should they only be used for services which are delivered voluntarily? Which (type of) investors could cover which area?
- What constitute current hurdles and obstacles for social impact investing? What are other governments doing to overcome these hurdles? What are best practices? Should social impact investing be supported by government policy? If yes, how?
- Are there any legal barriers to social impact investing in Germany? Are new legal structures needed for social impact investees (similar to the Charity Interest Company (CIC) in the UK or the low profit limited liability company (L3C) in the USA), for example?

The views are mixed how effective a social impact investing task force or expert roundtables would be, however. Some consider such a 'democratic' approach crucial to bringing all important stakeholders on board and making sure that social impact investing and new financing structures are not considered an alien element and threat, which would lead to their boycott. According to this group, such a broad engagement might also help overcome the issue that currently knowledge, expertise and experience rest with very few actors and that discussions of the topic always involve the same individuals and organizations.

Another view is that the interests and worldviews are so diverse that such meetings would not result in any tangible outcomes and that such discussions would be lengthy, delaying actual action. Instead, these people call for a bottom-up approach. Small, successful pilot projects should create compelling facts that make the benefits and potential of social impact investing obvious. This would lead to a change of thinking on the part of the public authorities, which would then, as a result, initiate the necessary reforms.

Support sector building

a. More flexibility and certainty for foundations

Foundations have played an important role in the development of social impact investing markets elsewhere. A prominent example is the Rockefeller Foundation. Foundations are far more engaged in social impact investing in the USA or the UK. The legitimacy of social impact investing by German foundations is disputed. While some argue that it is generally permitted, others believe that the current regulatory framework makes it challenging for foundations to engage in social impact investing.

One way or the other, there is a call for action on the part of the supervisory authorities to rule out this uncertainty. Ideally, there were precise statutory rules on the analogy of the US Internal Revenue Code 4944 C or an explicit commentary or guideline by the regulatory authorities on the analogy of the activities by The Charity Commission for England and Wales. The fact that the supervision of foundations rests with a number of institutions in the federal states – rather than one main supervisory authority on the national level – renders the situation quite complex. Expertise and interest in social impact investing appear to differ significantly across these authorities.

There are also critics of this call for action on the part of the supervisory authorities. Although the suggested commentary would be desirable, they deem it naïve to hope for such a statement. The critics do not expect the supervisory authorities to make a concrete statement regarding the legitimacy of social impact investments by foundations.

b. Tax incentives for social impact investments

Another government action that was recommended in our conversations was the implementation of tax incentives for social impact investments. If a social impact investment comes along with an attractive risk-return ratio, it would be plausible to assume that it will receive funding. Yet, there are promising social impact investments – in terms of non-financial impact – with a less attractive risk-return ratio, either because the organization will never be able to generate a (competitive) financial return due to its business model, because the volume is too small and, thus, the transactions costs too high, or because the (perceived) risk is deemed too great. In order to promote investments in such opportunities, the government might consider tax incentives analogous to the tax reliefs for charitable donations. Where impact investments come with no financial return or below-market rate returns, they are similar to donations and should, thus, receive equal treatment according to the proponents of such a measure. In the UK, a tax relief for investments in social enterprises is currently under development.³³⁰ Tax incentives would, however, require a clear definition of what constitutes an eligible social impact investment; they must avoid windfall gains of investments that would take place anyway.

c. Help create investment opportunities

Our research shows that there appears to be a limited pipeline of investable deals for social impact investors – this seems to be particularly true for the education space. This can be traced to a lack of suitable financing instruments and/or a lacking investment-readiness on the part of the investees. Both aspects are closely intertwined.

Due to the limited number of established social impact investors and intermediaries in Germany, they can dictate the investment terms³³¹ – along the lines of ‘sink or swim’. There is no competition for the best investees.³³² These financing terms might not be suitable for many potential investees, however. Some activities might not allow for self-sustaining business models but might add incredible non-financial impact, nonetheless. Simply pumping more money of the same nature into the market is not the right solution to make these organizations investment-ready. For this reason, the Financing Agency for Social Entrepreneurship (FASE) has started to develop hybrid financing structures that meet the specific requirements of individual investees.

At the same time, the FASE helps investees develop investable business models. Socially-motivated businesses commonly require significant support to become investment-ready. Oftentimes, their founders and managers have little knowledge of business concepts and financing structures. Germany faces a lack of incubation centers and organizations supporting the scaling of socially-motivated organizations, however. As discussed above, the set-up of additional incubation centers was also discussed during the Multi-stakeholder Conference. Two of our interviewees suggested that the German government should consider setting up an Investment and Contract Readiness Fund like the UK government has done. One of the interview partners argued that similar start-up support was also provided in the commercial space.

Moreover, it was also suggested in our interviews that the government might provide guarantees to encourage and enable

investments by private investors in investees that might otherwise not attract private investment capital.

Some criticize the limited availability of funding in the lower five-digit range.³³³ The social venture capital funds and the KfW program described above provide financing for proven business models that would like to scale. The government might, thus, consider mandating a funding program in this range.

Lastly, social impact bonds might also help channel investments in organizations that would otherwise not be investment-ready. The development of social impact bonds – in particular, in the education sector – requires a close cooperation with the (federal) states' public authorities and/or the municipalities. They should actively support the investigation and implementation of such innovative structures, e.g., by naming topics where such projects might be most promising and by making sure that funds exist that allow making the payment if the desired impact is achieved.³³⁴ Small-scale successful pilot projects might eventually lead to a change of thinking and public reforms.

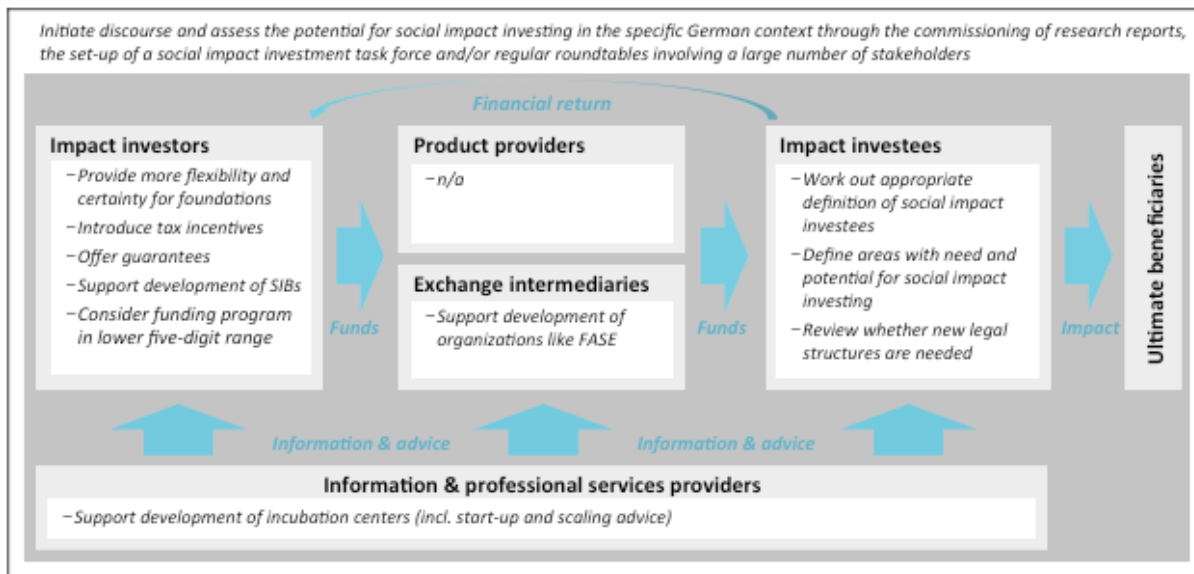


ILLUSTRATION 7: SUGGESTED ACTIVITIES ON THE PART OF THE GOVERNMENT.

5. CONCLUSION

This study investigated the status quo of the German social impact investing market with a particular focus on educational measures that could help solve some of Germany's most pressing issues, namely unequal educational opportunities, long-term unemployment and relative poverty. Our research shows that impact investing in the social space – at large and in the field of education in particular – is still in its infancy in Germany and driven by very few players. The government's involvement is limited, to date.

More government involvement is being demanded by a number of stakeholders in the field. Based on our conversations and secondary research two main areas emerged how the German government could promote social impact investing – in the overall market and specifically in the education space. On the one hand, it could initiate discourse and assess the potential for social impact investing in Germany through the commissioning of research reports, the set-up of a dedicated taskforce and/or the organization of expert roundtables involving a large number and diverse group of stakeholders. On the other hand, it could support sector building, for which a number of specific measures were suggested including more flexibility and certainty for foundations, tax incentives for social impact investments and the creation of more investable opportunities through guarantees, funding programs and the like. There are multiple views on the desired involvement of the government in the topic and the effectiveness of such an involvement.

A number of exciting projects – including social impact bonds and hybrid financing structures – are currently under development. It is to be seen how these products will be embraced by investors and how they will perform.

While we are not lobbying for the replacement of the welfare state, we nevertheless think that targeted social impact investments in selected areas might effectively complement government activities. Social impact investing must not be discussed as a panacea or an end in itself. It must be seen as a supporting means to help solve the social challenges Germany is facing. We are excited to see how the German social impact investing market will develop over the coming years!

APPENDIX A: OVERVIEW OF CONDUCTED EXPERT INTERVIEWS

We would like to express our sincere thanks to the following individuals with whom we had the chance to conduct in-depth interviews:

- Jake Benford, Senior Project Manager Program 'Zukunft der Zivilgesellschaft', Bertelsmann Stiftung
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- Martina Erlwein, Associate Director, Berenberg
- Dr. Dr. Christoph Glaser, CEO, Benckiser Stiftung Zukunft
- Friederike Hagenbeck, Berenberg
- Rainer Höll, Managing Director, Ashoka Germany
- Martin Link, Vice President Product Management Innovation & Private Equity, KfW
- Stefan Schwall, Founder and Executive Board Member, apeiros e.V. as well as Founder and CEO, apeiros Gbr.
- Rod Schwartz, CEO, ClearlySo
- Björn Strüwer, Senior Advisor Social Finance, Ashoka
- Dorothee Vogt, Investment Manager, BonVenture
- Berenike Wiener, Referatsleiterin Stiftungsmanagement und Corporate Sektor, Bundesverband Deutscher Stiftungen

ENDNOTES

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- 5 Freireich & Fulton, 2009.
- 6 Big Society Capital, 2013.
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- 37 The figures for Hungary, Israel, Japan, Korea, Switzerland, Turkey and the United States are IMF staff estimates.
- 38 BPB, 2012b.
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- 41 Chapter 1.4 discusses these challenges in more detail.
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- 44 Ullrich, 2005.
- 45 Ullrich also labels the UK and Ireland liberal welfare state regimes (Ullrich, 2005).
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- 61 Schraad-Tischler, Hellmann & Azahaf, 2011.
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- 130 Schneeweiss & Weber, 2012.
- 131 Schneeweiss & Weber, 2012.
- 132 For a good overview on social impact bonds also see: Scheck & Hoechstaedter, 2014.
- 133 Nicholls & Tomkinson, 2013.
- 134 Liebman, 2011.
- 135 Liebman, 2011.
- 136 Nicholls & Tomkinson, 2013.
- 137 Cabinet Office, 2013c.
- 138 Liebman, 2011.
- 139 Liebman, 2011.
- 140 Mulgan, Reeder, Aylott & Bo'sher, 2011
- 141 Social Finance Inc., 2012.
- 142 Cabinet Office, 2013a.
- 143 Schneeweiss & Weber, 2012.
- 144 Schneeweiss & Weber, 2012.
- 145 Louche, Arenas & van Cranenburgh, 2012.
- 146 Louche, Arenas & van Cranenburgh, 2012.
- 147 Louche, Arenas & van Cranenburgh, 2012.
- 148 Louche, Arenas & van Cranenburgh, 2012.
- 149 Louche, Arenas & van Cranenburgh, 2012.
- 150 Schaefer, 2004.
- 151 Louche, Arenas & van Cranenburgh, 2012.
- 152 Louche, Arenas & van Cranenburgh, 2012.
- 153 Louche, Arenas & van Cranenburgh, 2012.
- 154 Schaefer, 2004. Schaefer's (2004) research shows that, among the NPOs, religious organizations are the dominating group in terms of SRI investing.
- 155 Humphreys, 2012.
- 156 Humphreys, 2012.
- 157 Schaefer, 2004.
- 158 Fabozzi, Modigliani, Jones & Ferri, 2002.
- 159 A German-based multi-sector retailer operating in 18 countries (Tengelmann, n.d.).
- 160 Tengelmann Ventures, n.d.
- 161 Tivola-Ventures, 2013a.
- 162 Tivola-Ventures, 2013b.
- 163 Tivola-Ventures, 2013b.
- 164 Deutsche Bank, 2011.
- 165 Deutsche Bank, 2011.
- 166 Nicholls & Pharoah, 2008.
- 167 Emerson & Spitzer, 2007.
- 168 Emerson & Spitzer, 2007.
- 169 Benijts, 2010.
- 170 Benijts, 2010.
- 171 Weber & Scheck, 2012.
- 172 Benijts, 2010.
- 173 Brown & Swersky, 2012.
- 174 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 175 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 176 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 177 GABV, 2013.
- 178 Bankwechselbündnis, 2012.
- 179 GLS Bank, 2013b.
- 180 GLS Bank, 2012b.
- 181 In 2012, more than 7,000 customers passed on their interest rate so that EUR 51 million could be invested at a reduced or without any interest rate (GLS Bank, 2013b).
- 182 GLS Treuhand was already mentioned in section 2.1 as one of the foundations engaging in impact investing in Germany.
- 183 All of the above information on the GLS Bank stems from: GLS Bank, 2013b.
- 184 GLS Bank, 2012a.
- 185 GLS Bank, 2012b.
- 186 Gosling, 2013.
- 187 UBS, 2013.
- 188 UBS, 2013.
- 189 UBS, 2013.

- 190 UBS, 2013.
- 191 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 192 Brain Capital, 2010a.
- 193 Brain Capital, 2010a.
- 194 To date, 150 private individuals have contributed equity capital between EUR 10,000 and EUR 500,000 per person (Brain Capital, 2010b). The debt financing structure is particularly apt for the requirements of institutional investors; to date, three pension institutions (including Versorgungswerk der Wirtschaftsprüfer and Rheinische Zusatzversorgungskasse) and nine foundations have invested up to EUR 10 million each (Brain Capital, 2010b).
- 195 Brain Capital, 2010a.
- 196 Von Hiller, 2012.
- 197 All of the above information on Deutsche Bildung stems from: von Hiller, 2012.
- 198 CareerConcept, n.d.
- 199 Von Hiller, 2012.
- 200 AviaRent Capital Management, n.d. b.
- 201 AviaRent Capital Management, n.d. b.
- 202 AviaRent Capital Management, n.d. a.
- 203 Habona Invest, n.d.
- 204 Habona Invest, n.d.
- 205 Bridges Ventures, 2013.
- 206 Bridges Ventures, 2013.
- 207 Miller & Wesley, 2010.
- 208 Miller & Wesley, 2010.
- 209 BonVenture, n.d. a.
- 210 Social Venture Fund, n.d. g.
- 211 Social Venture Fund, n.d. g.
- 212 Social Venture Fund, n.d. b.
- 213 Social Venture Fund, n.d. c.
- 214 Social Venture Fund, n.d. d.
- 215 Social Venture Fund, n.d. a.
- 216 Social Venture Fund, n.d. f.
- 217 Social Venture Fund, n.d. e. Please note that the Social Venture Fund might have other portfolio companies in the education sector which are not displayed on its website.
- 218 Heister, 2010.
- 219 All of the above information on BonVenture stems from: BonVenture, n.d. a.
- 220 BonVenture, n.d. b.
- 221 FASE, n.d. d.
- 222 FASE, n.d. a.
- 223 FASE, n.d. c.
- 224 Phineo, 2010a.
- 225 Active Philanthropy, n.d..
- 226 Panta rhei, n.d..
- 227 Oekom research, n.d..
- 228 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 229 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 230 Spiess-Knafl & Achleitner, 2012.
- 231 Mendell & Barbosa-Vargas, 2013.
- 232 Except for the Social Stock Exchange.
- 233 Mendell & Barbosa-Vargas, 2013.
- 234 Mendell & Barbosa-Vargas, 2013.
- 235 Mendell & Barbosa-Vargas, 2013.
- 236 Mendell & Barbosa-Vargas, 2013.
- 237 Mendell & Barbosa-Vargas, 2013.
- 238 Spiess-Knafl & Achleitner, 2012.
- 239 Breidenbach, 2011.
- 240 NExT SSE, n.d.
- 241 NExT SSE, n.d.
- 242 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 243 BMW Stiftung Herbert Quandt, n.d.
- 244 Netzwerk Nordbayern, n.d.
- 245 Netzwerk Nordbayern, n.d.
- 246 Emerson & Spitzer, 2007.
- 247 Emerson & Spitzer, 2007.
- 248 GIIN, 2013b.
- 249 GIIN, 2013b.
- 250 GIIRS, n.d.
- 251 SRS, n.d. a.
- 252 SRS, n.d. b.
- 253 Phineo, 2010a.
- 254 Ashoka Deutschland, n.d.
- 255 Talents4Good, n.d.

- 256 FASE, n.d. c.
- 257 FASE, n.d. d.
- 258 FASE, n.d. b.
- 259 FASE, n.d. d.
- 260 FASE, n.d. c.
- 261 Iq consult, n.d.
- 262 Phineo, 2010b.
- 263 Social Entrepreneurship Akademie, n.d..
- 264 Achleitner, Spiess-Knafl, Heinecke, Schöning & Noble, 2011.
- 265 All of the above information on the Bertelsmann Stiftung stems from: Bertelsmann Stiftung, n.d. a; Bertelsmann Stiftung, n.d. b.
- 266 Weber & Scheck, 2012.
- 267 Schneeweiss & Weber, 2012.
- 268 All of the above information on Impact in Motion stems from: Impact in Motion, n.d.
- 269 Such an understanding forms, for example, the basis for research by Brown and Swersky (2012) on the UK social investment market. Please note that this definition applies to social investment rather than impact investing. Yet, these two are mentioned as synonyms in the report.
- 270 Brown & Swersky, 2012.
- 271 Beyond Philanthropy, 2013; Friemel & Oldenburg, 2013.
- 272 BCG, 2013.
- 273 Schneeweiss & Weber, 2012. This is also in line with the findings by: Weber & Scheck, 2012.
- 274 In this context, one of our interview partners mentioned that the social impact required from a social entrepreneur or an impact investee, respectively, is typically much higher in Germany compared with other markets. Investments in SMEs, which have a purely economic impact in underserved areas would typically not be considered impact investments in Germany, which might be the case elsewhere. Along the same lines, please also see the commentary on the real estate funds in section 2.2.
- 275 Kinderzentren Kunterbunt, n.d..
- 276 Social Venture Fund, n.d. e.
- 277 Meuter, 2010.
- 278 EVPA, 2012.
- 279 All of the above information on Chancenwerk was retrieved from: BonVenture, n.d. b.
- 280 BonVenture, 2012.
- 281 All of the above information on ROCK YOUR LIFE! was retrieved from: BonVenture, n.d. b.
- 282 ROCK YOUR LIFE!, 2013.
- 283 BonVenture, n.d. b.
- 284 BonVenture, 2012.
- 285 Bettermarks, 2010; Gribnitz, 2013.
- 286 GLS Bank, 2013a.
- 287 Schneeweiss & Weber, 2012.
- 288 Scheuerle, Glänzel, Knust & Then, 2013.
- 289 Bridges Ventures, 2013.
- 290 Scheuerle, Glänzel, Knust & Then, 2013; Täubner, 2013; Then, Scheuerle & Schmitz, 2012.
- 291 Cheng & Oldenburg, 2013.
- 292 Big Society Capital, n.d. a.
- 293 Cabinet Office, 2013b.
- 294 Schwall, 2011.
- 295 Schwall, 2011.
- 296 Allmendinger, Giesecke & Oberschachtsiek, 2011.
- 297 Allmendinger, Giesecke & Oberschachtsiek, 2011.
- 298 Chen, 2012.
- 299 Work by the Mercator Forscherverbund on social entrepreneurship in Germany supports the notion that the established players oftentimes have an advantage both in the “quasi markets” and in public tenders given their comprehensive infrastructure and scale (Then, Scheuerle & Schmitz, 2012).
- 300 BMFSFJ, 2010.
- 301 Bundesregierung, 2010.
- 302 Bundesregierung, 2010.
- 303 BMFSFJ, 2013.
- 304 BMFSFJ, 2013.
- 305 Also see Spiess-Knafl, 2012.
- 306 BMFSFJ, 2011.
- 307 BMFSFJ, 2011.
- 308 Saltuk, 2011.
- 309 European Commission, 2011.
- 310 European Commission, 2012.
- 311 European Commission, 2012.
- 312 European Regional Development Fund. The ERDF funds enterprises (esp. SMEs) to create sustainable jobs, infrastructure projects, and financial instruments meant to promote local development in the EU (Saltuk, 2011).
- 313 European Social Fund. The aim of the ESF is to increase employment and job opportunities in the EU (Saltuk, 2011).

- 314 All of the above information on the Social Entrepreneurship Fund label was retrieved from: EVPA, 2013.
- 315 European Commission, 2013.
- 316 All of the above information on the fund was retrieved from: European Investment Fund, 2013.
- 317 Saltuk, 2011.
- 318 BCG, 2013.
- 319 BCG, 2013.
- 320 BCG, 2013.
- 321 Scheuerle, Glänzel, Knust & Then, 2013.
- 322 For more information see: Scheuerle, Glänzel, Knust & Then, 2013.
- 323 Then, Scheuerle & Schmitz, 2012.
- 324 Scheuerle, Glänzel, Knust & Then, 2013.
- 325 Scheuerle, Glänzel, Knust & Then, 2013.
- 326 Chen, 2012.
- 327 This is in line with findings by the Boston Consulting Group: BCG, 2013.
- 328 BMFSFJ, 2011.
- 329 The European Commission (2012), for instance, defines a social business/enterprise as an undertaking “whose primary objective is to achieve social impact rather than generating profit for owners and shareholders, which uses its surpluses mainly to achieve these social goals, [and] which is managed by social entrepreneurs in an accountable, transparent and innovative way, in particular by involving workers, customers and stakeholders affected by its business activity”.
- 330 For more information see: HM Treasury, 2013 or Worthstone, 2013.
- 331 Scheuerle, Glänzel, Knust & Then, 2013.
- 332 Scheuerle, Glänzel, Knust & Then, 2013.
- 333 Scheuerle, Glänzel, Knust & Then, 2013.
- 334 Our interviews suggested that there might be issues around the creation of reserves.

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