ANANDA
SOCIAL VENTURE FUND

IMPACT IN MOTION

Impact Investing in education

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About the Ananda - Social Venture Fund

Ananda Ventures (Social Venture Fund I and II) manages 30m and is the first social impact investor with a pan European focus. Social Venture Fund invests in outstanding social enterprises, which provide innovative solutions for urgent social challenges. The Social Venture Funds' active portfolios include "Auticon" a company providing IT consulting delivered by Asperger autists and "VerbaVoice", a mobile transcription solution for hearing impaired People.

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EXECUTIVE SUMMARY

- European countries have a very sophisticated education system for children aged 0-16 years. Their governments provide education services which are free and accessible to all. Although the quality of education is generally good, there are considerable inequalities in opportunity for children from different social and ethnic backgrounds. These inequalities have significant effects on the employability, earning potential and wellbeing (in particular health) of these children in later life.
- Impact investing in education has emerged as a means of reducing inequalities and encouraging equal access for all. As of yet, it accounts for a mere 1‰ of the USD 2.5 trn global education market, the majority of which is dominated by public funding. The impact investment market will increasingly be influenced by the dynamic growth of the European e-learning and ed-tech markets, which attract business angels and commercial investors, such as traditional venture capital funds and large education companies.
- Compared to other funders like government, philanthropic funders and commercial investors, impact investors can perform many important functions in the education market: mobilising new resources, completing gaps in government services delivery, promoting innovation in teaching and learning methods, scaling approaches or tools to increase efficiency, monitoring outcomes and efficiency, and preserving ethical standards.
- We looked at three different segments within the education market: 1.) Core education (e.g. infrastructure in pre-schools, schools and special needs education), 2.) Parallel education (e.g. online/ offline tutoring, mentoring and training, e-learning, games) and 3.) Ancillary services (e.g. technological devices/ multimedia for pupils, teaching and learning management systems for schools and teacher training). Within these three segments, parallel education or ancillary services appear to be the most attractive for impact investors due to their low entry barriers and attractive business models incorporating innovative technologies or new management models. However, scalability in the fragmented school market (B2C) and the difficulty in reaching the most disadvantaged groups who lack the financial resources to pay for B2C business models remain an issue.
- So far, most deals in education are relatively small and most investors still find it difficult to select business models in the growth stage that deliver strong financial returns and, at the same time, target the most disadvantaged populations. Innovative technology and new management models, which will be an important area for investment in the medium term, are only just becoming a focus for impact investors. Investment in technology-based business models is very likely to increase equity investments in the field and co-investments with commercial investors.
- Due to the need for innovative approaches in education, a broad coalition of philanthropic funders, social entrepreneurship initiatives and incubators work on fostering education ventures. With increasing investment opportunities, we expect more specialised investors coming into this sector and existing players to increase their share in education, especially in the UK.
- A growing number of impact investors seek more financially resilient deals of at near market or at market returns. These investors are also more likely to invest in technology-based innovations and often co-invest with commercial investors, such as traditional venture capital funds. Given the Impact investor's focus on social outcomes, mission lock through certain control and veto rights appears to be essential, especially when holding a minority stake.
- Given the continued inequalities of educational opportunity and the need for innovative solutions, impact investing could mobilise new sources of funding and help catalyse innovative approaches to education. It has the potential to improve access and quality of the existing sophisticated education system, especially with regards to most disadvantaged children.

INTRODUCTION

OBJECTIVES AND SCOPE

The objective of this study is to map the current landscape of impact investing in education in Europe, with a view to locating potential intervention areas for impact investors. We define impact investments as investments with a focus on both social and financial returns[1]. This is the third publication of a series of reports which the SVF (supported by Omidyar Network) has initiated with the intention of sharing knowledge and fostering cooperation amongst European impact investors. The first study discussed investable entrepreneurial approaches in the area of long-term unemployment[2], whilst the second analysed impact investments in ageing[3]. This third study will focus on the evaluation of the education sector in selected countries within the SVF's investment scope (i.e. Germany and the UK).

The term education can be defined as *"the acquisition of skills, knowledge and understanding to put individuals in a position to succeed in personal relationships and in society"*[4]. According to this definition, education can be seen as a life-long process, as illustrated in the figure below. For the purpose of this report, however, we focus on education for children aged 0-16 years old, including pre-school, primary and secondary school education.

STRUCTURE

In order to assess impact investment opportunities in the education sector, we have looked at the following key aspects:

- **Education sector:** What are the social challenges facing the education sector in Germany and in the UK? How is education funded in these countries? What are future trends in the sector?
- **Role of impact investing**: What is the role of impact investing in mature European education systems? What is their position compared to other sources of funding like philanthropic capital and traditional venture capital?
- **Investment opportunities:** What are the financial returns and social impacts of investing in the different segments of the education market?
- **Impact investing landscape**: Which types of transactions have been closed by impact investors? Which investors are active in this field? What are the trends going forward?

METHODOLOGY

The study draws on a review of secondary sources as well as on a number of interviews with impact investors and market experts in the field of education, which complemented our internal market intelligence. A full list of interview partners is provided on page 2.

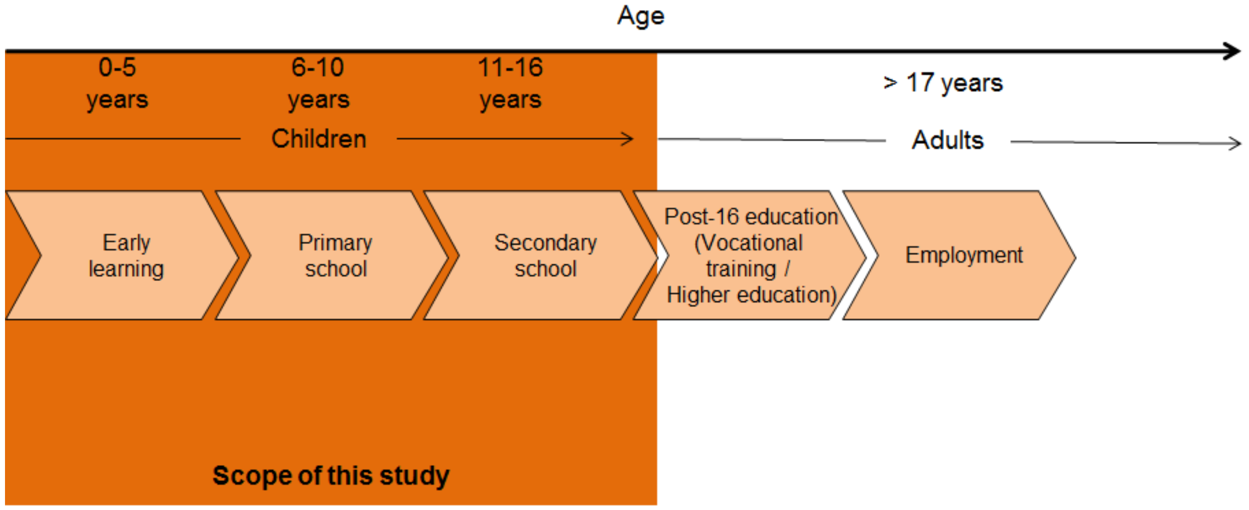

Figure 1: **Overview of the education sector**
Source: Impact in Motion (2014)

EDUCATION SECTOR

SOCIAL CHALLENGES IN EDUCATION

Education is a process of personal and social enrichment. For children between the ages of 0 and 16 years, it can be distinguished between formal and informal education. Formal education is delivered to children in an institutional setting such as pre-schools, primary and secondary schools. Informal education, on the other hand, includes all educational activities delivered outside of this traditional institutional setting, such as youth work, sports clubs or education through media. In this study, we take a look at both fields.

Overall, Western European countries like Germany and the UK have very sophisticated and mature educational systems. Their governments provide educational services that are free and accessible to all. Public expenditure on education in Western Europe is usually around 5-6.5% of GDP. Both Germany (5.3%) and the UK (6.1%) fall well within this range.[5]

Although the quality of education in these countries is generally considered good, children from different social and ethnic backgrounds and children with special education needs face unequal opportunities. Studies show that children from disadvantaged backgrounds already lag behind their peers when they enter the education system. This gap widens as they progress through primary and secondary school. Experts generally agree that by the end of primary school the attainment gap is well established.[6]

Disadvantaged or vulnerable groups with low educational attainment include[7]:

- **Children in poverty:** In Germany as well as in the UK, poverty is the strongest determinant of educational outcome. In the UK, the most frequently used indicator for poverty is children receiving free school meals (FSM). Figure 2 illustrates the attainment gap between children who receive FSM and those who do not. In Germany, children from a low social-economic background are three times less likely to reach higher secondary education ("Gymnasium") than their peers with high socio-economic background.[8]

- **Children from certain ethnic backgrounds**: In Germany children from a migrant background have a lower attainment at school compared to German nationals.[9] UK statistics from the Department of Education reveal that, for example, pupils of Chinese origin score consistently above average, whereas Black children perform below the national average.[10]

- **Children with special education needs (SEN):** Children with special education needs, such as learning and communication disabilities, emotional and behavioural disorders, physical disabilities and developmental disabilities consistently do worse than their peers without SEN, as can be seen in their GCSE score (see figure2).

Other vulnerable groups who display consistently low educational performance include children in care, refugees and teenage mothers.[11]

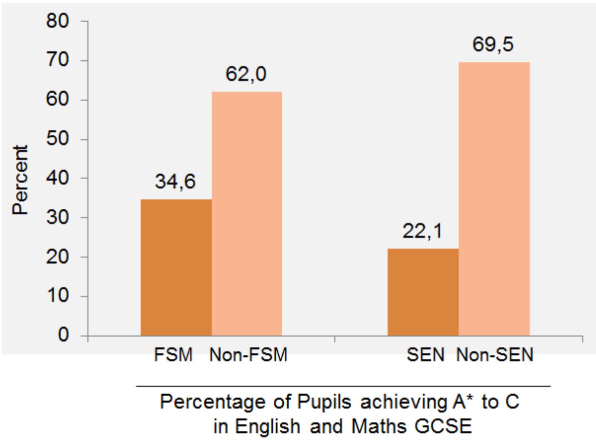

Figure 2: The attainment gap
Source: UK Department for Education (2012)

Unequal educational opportunities have significant consequences for employability, earning potential and wellbeing (in particular health) of these children in later life.[12] Furthermore, the attainment gap has an effect on wider society, incurring significant costs to the public finances through, for example, social benefit and unemployment.

Fair, high quality educational access therefore remains a key concern for Germany and the UK.

EDUCATION FUNDING

The global education market accounted for USD 2.5 trn in 2010 and is largely dominated by public funding.[13] Impact investing has emerged as a means of reducing inequality and improving access to education, but still accounts for a very small share of educational funding. The investment advisory D. Capital Partners estimates impact investing to represent roughly 1‰ of the USD 2.5 trn global education market.[14]

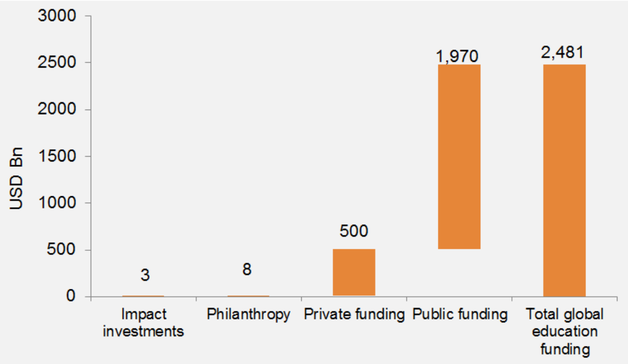

Figure 3: **Global education funding**
Source: D. Capital Partners (2013)

The situation appears to be similar in the countries we looked at. Impact investing in education accounted for GPB 14m[15] of the UK's total education spend of GBP 56 bn[16] in 2012, even though the UK is the most developed impact investing market in Europe.

The total annual German education budget was EUR 175bn in 2012. Impact investing is still a nascent industry, standing cumulatively at EUR 24m in 2012[17], and is therefore yet unable to mobilise large funds to close the attainment gap. We estimate, however, that approximately 20% of the total impact investing market in Germany or roughly EUR 4-5m can be attributable to education.[18] Given the attainment gap and largely flat public education budgets, impact investing could in the future play a more prominent role in covering the needs of disadvantaged populations that are not reached by the current educational system.

Public education funding through the pupil premium (UK)

UK government has successively tried to improve educational outcomes for children from disadvantaged backgrounds through giving the schools more autonomy over budgets and approach, while at the same time holding them accountable for the outcomes. One such measure is the pupil premium, which gives additional funding (GBP 900 per pupil per year) to schools in order to support disadvantaged children. The pupil premium is an important source of funding for social businesses, as we will discuss in the chapter "Investment opportunities".

FUTURE TRENDS

Our research reveals that the development of the education market in Germany and the UK will be determined by growing state education budgets, below expectation educational outcomes and increased use of technology, especially mobile devices. These factors will lead to dynamic growth in the e-learning and ed-tech markets over the medium term fostering the emergence and growth of new businesses in this field and attracting interest from commercial investors, such as venture capital funds (both multi-sector investors as well as education specialists) and large national or international education companies, such as Pearson or McGraw Hill in the UK or Holtzbrinck in Germany.

Overall, these markets appear highly competitive, and it might initially seem as if impact investors will lack the size and experience to play a significant role in them. The next chapter explains, however, how impact investors can add substantial value to technology-based educational markets.

ROLE OF IMPACT INVESTING

Throughout Europe, philanthropic funders (e.g. foundations) have traditionally provided financial resources and strategic support to governments and schools to improve the quality of and access to education. However, impact investors entering the educational sector seeking both financial and social returns are a relatively new phenomenon in Germany and in the UK.

Some claim that impact investing is still relatively new in education compared to other sectors because of "*difficulties privatising short-term gains from an essential public good where benefits are realised over the long-term, and where government can provide free access for all*."[19] Going forward, we expect impact investing to be a valuable complement to the existing funding mix. Due to its focus on both social and financial returns, it can play six important roles which none of the other funders - state, commercial investors in particular venture capital funds, philanthropy - in the market can:

1. **Catalyse and mobilize new funding** for the education sector

   With patient capital from impact investors, education investments can become more viable for commercial investors. Hence, impact investments can help to deploy large scale capital for social businesses in education. One such example is the joint investment of auridis, BonVenture and the SVF which enabled large institutional funding through their investment in *Kinderzentren Kunterbunt* (D) which is described as investment example in the appendix.

2. **Complement government efforts** through direct service delivery

   Even when the government provides education services, they might lack the capacity to address the needs of certain demographic groups. Private investors can fill these gaps by enabling supplemental educational services for example pre-school educational services or education for structurally marginalised groups, such as minorities, ensuring their interaction in society. Big Issue Invest's and Bridges Ventures investment into the *Early Years Learning Foundation* (UK), a nursery provider mainly operating in deprived communities with few nursery facilities, illustrates this very well.

3. **Promote innovation** in teaching and learning methods

   In order to enhance educational quality and efficiency, impact investors can invest in innovations that reduce cost, improve teachers' effectiveness or streamline school management. The use of technology is an extremely powerful tool in this context. A good example of this is Nesta's investment in *Sherston Software* (UK), a provider of educational software for primary school children (see investment example in the appendix).

4. **Scale concepts** in order to enhance educational access and equality

   Impact funds can be used to ensure that the most vulnerable are reached more efficiently in the current educational system. For low-income families, tutoring fees can pose a barrier to improve the educational attainment of their children. As a result, several low-cost online tutoring providers have recently emerged, such as BonVenture's investment *bettermarks* (D). Another example for impact funders enhancing educational access is SVF's investment in *VerbaVoice* (D), a real-time transcription service that allows hearing-impaired pupils better access to education, thus improving educational and social inclusion.

5. **Monitor outcomes and system effectiveness**

   Impact investors could also tackle the existing lack in evidence in efficiency of new education models, as they rigorously monitor and evaluate the outcomes of their investments and benchmark them against other business models in the sector.

6. **Preserve high ethical standards**

   With a trend towards ed-tech start-ups and big data generated by such ventures, there is an increased need for high ethical standards on how to deal with the sensitive data collected in the education process. Some market participants claim that impact investors could play an important role in setting and preserving ethical standards, due to their focus on social impact.

As impact investing continues to grow in the education sector, it will become more effective in fulfilling the roles described above. Going forward, it will occupy an important position between commercial investors, especially venture capital funds who do not focus as much on social impact, philanthropists who do not foster the development of sustainable businesses and the public sector which is more risk adverse to innovation.

INVESTMENT OPPORTUNITIES

MARKET SEGMENTS

Education is a relatively large field for investment. In order to better understand the opportunities in this market, we looked at three distinct segments where potential investees are active (see figure below) and assessed them according to their market attractiveness (i.e. financial sustainability) and social impact potential.

As discussed earlier, social impact in education is closely linked to the ability to reach those most in need. Impact investors will therefore look for business models that reach disadvantaged populations and at the same time show financial resilience.

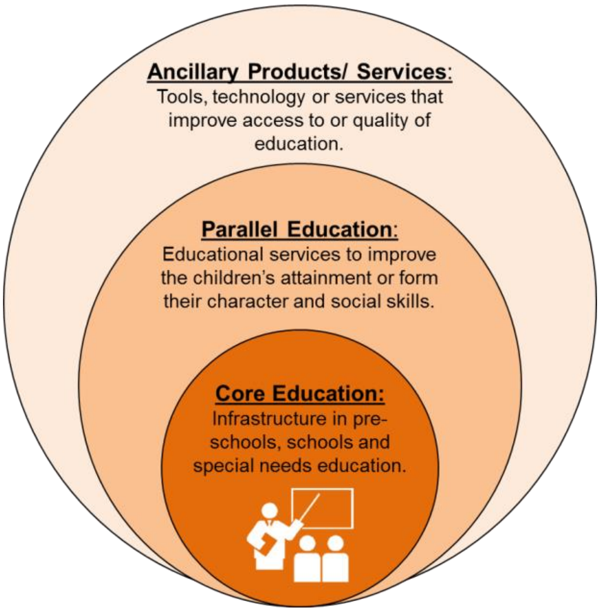

Figure 4: **Education market segments**
Source: Impact in Motion adopted from Kaizen Private Equity (2014)

CORE EDUCATION

The segment **Core Education** includes investments into formal education infrastructure, such as pre-schools and schools. Regulation is relatively high in this segment which poses a significant entry barrier. Moreover, it is difficult to scale due to high fragmentation of the market. We see some investments in this segment, such as BonVenture's investment into *Flachsland Zukunftsschulen* (D), an integrated childcare and school provider or the SVF's investment into the childcare provider *Kinderzentren Kunterbunt* (D).

Due to the large deal sizes, social impact investors find themselves often in a co-investment with traditional investors (especially debt providing banks or public venture capital funds). Financial attractiveness as well as the risk of deals in this segment is moderate and innovative business models are scarce. The most common areas for gaps in public service provision are pre-schooling and special schools for marginalised groups, such as *SchlaU Schule* (D), a provider of schools for refugees.

PARALLEL EDUCATION

Parallel Education can be broadly categorised into services that directly improve school attainment, such as online/offline tutoring and e-learning, or interventions that help children to shape their soft skills, character and other extra-curricular capabilities, through mentoring, coaching, online/offline training and games. This segment is potentially the broadest: it stretches from strongly technology-based services, like ed-tech start-ups that attract interest from the traditional venture capital industry, to interventions working with voluntary mentors that are initially instigated and supported by foundations. The business models in this segment can either target a single disadvantaged individual in need (e.g. tutoring) or provide more general skills and preventative care for a whole group of children (e.g. media training for teenagers). Services can be school or government funded (B2B[20]) as well as paid for privately (B2C).

Overall, this segment is characterised by low entry barriers, a high level of competition and (compared to core education) relatively smaller deal sizes. The challenge in parallel education is to reach scale in the very fragmented school market, which often plays a vital role in distribution, even for B2C business models. Examples for young social businesses in the area include the educational software provider *Sherston* (UK) and the peer-to-peer mentoring programme *Chancenwerk* (D), all described in the appendix.

Social impact in parallel education is most closely linked to the capacity to reach vulnerable groups. Part of the services are paid for by schools (B2B, e.g. through the pupil premium in UK) where reaching disadvantage children is a minor concern, but a substantial number of services are paid for by the families (B2C), at the risk of excluding those most in need. Many financially viable B2B business models additionally target higher income populations with larger spending power and can hence offer a more competitive financial return. The social return in this case can be, however, limited. The ways in which social ventures can bridge the gap between social impact and financial return will be discussed below.

ANCILLARY PRODUCTS/ SERVICES

Ancillary products/ services improve access to or quality of education for all children by providing tools, technologies or services. This can range from multimedia equipment and teaching material to school management systems and teacher training. Examples include technical equipment or aids for the disabled, such as *Insane Logic's* (UK) MychoicePad for people with speech and language problems or *Verbavoice's* (D) real-time speech recognition and visualisation for the hearing-impaired (both described in the appendix). Another sub-segment is school or learning management services, such as *Thirdspace Learning* (UK) an online-learning platform that has moved into school management services. We also see a general trend of increasingly linking originally parallel education products and services with ancillary school management system.

The segment of ancillary products/ services is only slowly coming into the scope of impact investors, as it often only indirectly improves the situation of disadvantaged groups. This segment is mostly comprised of B2B business models, which benefit low income children. There is also lower competition than in other segments and increased possibility for the scaling of business models. Technology-based products such as technical equipment and aids for pupils or school/ learning management services for schools appear to have the most attractive business profiles.

Ancillary products and services often have a very good impact profile as 1.) business models target the ecosystem and are designed to reach a higher number of children and 2.) disadvantaged populations do not pay themselves for the services.

BRIDGING THE GAP BETWEEN IMPACT AND RETURN

Due to the potential challenge between social impact and financial return in the education sector, the question remains: how can one achieve both high social and financial returns? We identified several examples of business models that managed to bridge the gap between impact and financial return:

- **Schools as payer** (B2B): In the UK, social businesses often set themselves up as B2B business models and sell directly to schools in order to reach disadvantaged children. The schools use the pupil premium (see box on page 7) to pay for these products and services. An example of this model would be *Thirdspace Learning* (UK) an online platform to improve numeracy.
- **Government as payer** (B2B, sometimes also referred at as B2G): In the countries we looked at, we have found several possibilities of how government could become the payer for educational products and services and enables that the most vulnerable are met:

  1.) In the UK, there is an increasing trend for payment for result contracts and Social Impact Bonds. Educational outcomes have been a priority for government Social Impact Bond commissioning The Department for Work and Pensions (DWP) has commissioned GBP 30m through its Children Innovation Fund to improve educational outcomes. Social Impact Bonds are a very good vehicle to ensure that most disadvantaged children are reached and that - at the same time - attractive returns for investors are generated. Social Impact Bonds are currently not as popular in Germany as in the UK and no SIB has been signed education for the target group we looked at.

  2.) In Germany, however, there exists the system of "*Bildungsgutscheine*" (education vouchers), which enable children from disadvantaged backgrounds to get government funding for "participation in education", e.g. for tutoring fees or sports courses.

  3.) Sometime, the cost of products and services (especially ancillary products/ services) designed for disabled children could also potentially be reimbursed by public health insurance. This is for example the case for *Verbavoice's* (D) online transcription services for hearing impaired children.
- **Freemiums** (B2C): Social businesses that directly sell to the end-consumer often apply a freemium model where fees from paid services cross-subsidise free access for low income groups. The social business *Insane Logic* (UK) for example follows this strategy, as described in our investment example in the appendix.
- **Low cost services** (B2C): Though most social businesses charge their users, some deliberately set low fees in order to ensure their services remain affordable for low-income users. An example of this strategy is the low-cost online tutoring provider *bettermarks* (D) that undercuts traditional face-to-face tutoring prices.

IMPACT INVESTING LANDSCAPE

The total UK impact investing market has been estimated at GBP 286m in 2012. Roughly 5% or GBP 14m is attributable to education.[21] Compared to other impact investing markets, education starts from a relatively small size and is forecasted to show average growth of almost 40% p.a. In their forecast, BCG reckons that the opening up of public services (increased share of social enterprises) and the increase in direct payments (increase in B2C services) for social service provision are the most important drivers of growth within this segment. The impact investing education sector is expected to reach GBP 37m in 2015 in the UK, mostly driven by the special school segment.

There are currently no forecasts available for the German market, but as stated earlier, we believe that roughly EUR 4-5m are impact investments in education (or 20% of the total impact investing market).[22]

TRANSACTIONS

So far, the majority of impact investing deals in education have been relatively small (< EUR 500k) with "parallel education" being the most popular segment for investing.

According to the investment readiness UK survey undertaken in 2012[23], 22% of youth- and education-focused organisations had taken on repayable investments, with the majority of these being secured loans. This is consistent with our findings that debt financing has been dominating the market so far.

Investment managers in the field report a lack of innovative education businesses that are able to reach the most vulnerable and to provide solid financial returns. Moreover, innovative ventures are often too early stage and have no track record of being investable for the majority of impact investors. In order to build a solid deal pipeline, more and more incubators (e.g. Unltd and Wayra) have recently turned to the underexploited area of education. Philanthropic organisations also play a crucial role in building up a deal pipeline, both as early-stage funders and in conducting and funding research on effectiveness of different approaches to tackle the attainment gap (e.g. The Education Endowment Foundation, UK, Bertelsmann Stiftung, D).

Going forward, it seems that gradually more and more innovative technologies and new management models (especially in ancillary services) are becoming a focus of impact investors. With the opening up of these new areas for impact investing, the share of equity investments is also likely to increase.

A number of examples of impact investments in education in Germany and in the UK can be found in the appendix to this document.

INVESTOR LANDSCAPE

European impact investors usually include education deals as part of their multi-sector portfolios. Overall, there are approximately a dozen active impact investors in education in Germany and in the UK. Most recent investments in the UK have been made by Nesta Investment Management, a new fund that started investing in January 2014 and that focuses on education as one of three outcome areas. Among its first investments were the online learning specialist *Sherston* and *movellas*, an online story sharing community.

In Germany, BonVenture has been the most active player in education. It currently holds five very distinct education investments in its portfolio, namely *Kinderzentren Kunterbunt* (nursery facility provider), *Chancenwerk* (peer-to-peer tutoring), *Rock your Life!* (mentoring), *Flachsland Zukunftsschule* (school provider), and *bettermarks* (online tutoring). SVF recently invested in the UK-based speech and language specialist *Insane Logic* and holds *Verbavoice,* a provider of transcription services for the hearing impaired as well as *Kinderzentren Kunterbunt* (nursery facility provider).

According to their risk / return profile as well as their social impact footprint, we see several types of investors in this sector:

At one end of the spectrum, there are investors who have limited or no return expectations, and who focus only on the most disadvantaged beneficiaries. The business models they invest in target financial sustainability at best. They are more likely to fund interventions that previously had philanthropic funding.

At the other end of the spectrum, a growing number of impact investors, seek financially resilient deals of at near market or at market returns. These investors are also more likely to invest in technology-based innovations and often co-invest with commercial investors, especially traditional venture capital funds. The business models they invest in target a broad range of beneficiaries, including middle-class income beneficiaries, who have the ability to pay for educational services. As these investors also have a very strong focus on social impact, mission lock is key (see box below).

Investor's perspective on mission lock

During our interviews, impact investors raised three main points that seem to be vital in avoiding mission drift, especially when co-investing with commercial investors, such as traditional VCs:

1.) **Invest in social ventures where social impact is the core of the business model**: If social impact is in the core of the business model, the more successful a company is and the more revenue and profit it generates, the more social impact it produces. Hence, there should not be a trade-off between social and financial impact.

2.) **Maintain the mission lock due to control and veto rights:** When negotiating a deal, impact investors should carefully lay down appropriate control and veto rights with regards of the dilution of the mission.

3.) **Monitor and evaluate social outcomes**: The impact investors should establish appropriate outcomes measurement system right after investing and monitor and evaluate social outcomes throughout the investment period, even when holding a minority stake.

Going forward, there will likely be more impact investors in this field as new investment opportunities open up. These will either be traditional funds moving in this direction or new, dedicated players.

Given the trend towards more technology-based business models, impact investors (are also more likely to see themselves co-investing with commercial investors (traditional venture capital funds or large education companies) in the future. Their challenge will be to find high-impact deals and to ensure mission-alignment and keep social businesses on mission, even if they only hold a minority stake.

CONCLUSION

Given the continued inequalities of educational opportunity and the need for innovative solutions, impact investing can mobilise new sources of funding and help catalyse innovative approaches to education. It has the potential to improve access and quality of the existing sophisticated education system, especially with regards to most disadvantaged children.

Impact investors have a broad field of investment opportunities in education, in which they need to consider the risk / return profile as well as the social impact profile of an investment. Innovative businesses which are able to benefit society's most vulnerable, as well as generating near-term returns, can most likely be found in innovative technologies in parallel education and in new management models in the field of ancillary services. These segments are fairly new for education impact investors.

Due to the need for innovative approaches in education, a broad coalition of philanthropic funders, social entrepreneurship initiatives and incubators work on fostering education start-ups. With increasing investment opportunities, we expect more specialised investors coming into this sector and existing players to increase their share in education, especially in the UK.

The review of impact investing opportunities in education led to the following recommendations for investors in the field:

1. **Deals should be sourced more broadly from the educational ecosystem**, especially more in technology-based innovations and ancillary services which have a large scale impact potential and are traditionally not in the scope of impact investors.
2. With more and more social businesses with similar intervention models (e.g. low-cost tutoring) entering the education sector, the **focus on real innovations with a proven outcome** and best-in-class business models which have shown effectiveness in reaching disadvantaged children remain key**.**
3. It is important for an impact investor to **clarify the priorities of impact goals and financial returns** before sourcing education deals. According to their position towards impact and reaching the most vulnerable their search field will vary significantly**.**
4. Impact investors can add a lot of value to education deals by supporting social entrepreneurs as they further their mission by **measuring and evaluating social impact.** They should therefore live up to this role, especially when co-investing with commercial investors.

APPENDIX

Investment example: *Kinderzentren Kunterbunt* (D)

Segment: core education

In 2009, the Social Venture Fund invested in Kinderzentren Kunterbunt, a provider of childcare centres tailored to the needs of working parents.

Social challenge: Germany has a shortfall of over 160,000 childcare places, especially in the West of the country. Existing childcare facilities are mostly inflexible in terms of opening hours and holidays and are therefore unsuitable for working parents.

Business model: *Kinderzentren Kunterbunt* runs over 30 childcare centres providing services to over 2,000 children. The company addresses the needs of working parents by offering extra-long, year-round opening times (6h-20h) and flexible booking times. Moreover, *Kinderzentren Kunterbunt* facilities are conveniently located near major companies, hospitals and industrial areas. In addition, the company offers high quality care, and cutting edge education and professional development opportunities for employees. Fees are within the same range as state-run or religious childcare facilities. *Kinderzentren Kunterbunt* is a social business with the majority of its revenues stemming from government subsidies for childcare places complemented by fees paid by the parents.

Social impact: *Kinderzentren Kunterbunt's* social impact is threefold:

- improved educational outcomes, as well as better physical and mental health for the children,
- equality/ empowerment and increased income for the working parents, and
- increased income and professional development (education) for staff.

Investment: The Social Venture invested EUR 1m to support the development of additional childcare centres. The investment provides short-term liquidity for the renovation and conversion of rental space, funding for facility start-up costs and working capital, thus ensuring and accelerating growth. Other equity investors include the social venture capital fund BonVenture, the social investor auridis and the Bayrische Beteiligungsgesellschaft, a public venture capital fund.

www.kinderzentren.de

Investment example: *Sherston* (UK)

Segment: parallel education

Established in 2012, Nesta Investment Management invested in Sherston Software, a leading provider of innovative educational software designed to motivate children and improve their educational performance.

Social challenge: Educational progression and attainment for children of primary school age within the UK (c.4m children).

Business model: *Sherston's* online learning tool, Planet Sherston, enables children aged 3-11 years to gain access to a large selection of curriculum mapped activities, games and videos, with engaging game-play and adaptive, personalised learning. By setting tasks for each individual child based on their progress, it achieves a better learning outcome. Teachers are able to efficiently assess, provide feedback on and log individual student progress in a time-efficient way. *Sherston* licenses its products to over 800 schools in the UK reaching over 25,000 children by the end of 2013. *Sherston* is an educational technology company that sells its products directly to schools.

Social impact: *Sherston's* products significantly improve children's educational attainment through highly effective, adaptive, personalised learning. Learning progression and success is tracked by a supportive learning management software tool for teachers. Impact with most vulnerable pupils is secured through its B2C business model where schools are the payer.

Investment: Established over 30 years ago, *Sherston* is a leading provider of innovative educational content. In 2013, Nesta Impact Fund invested GBP 750k into the company to support the scale-up of its sales efforts and the initiation of evaluation studies. Sherston's high calibre content and its large market reach created a strong investment case for Nesta.

www.planetsherston.com

Investment example: *Chancenwerk* (D)

Segment: parallel education

BonVenture invested in *Chancenwerk*, an innovative peer-to-peer tutoring and mentoring programme for primary and secondary school children who hail from socio-economically disadvantaged backgrounds.

Social challenge: Children from socio-economically disadvantaged backgrounds (especially immigrants) consistently show lower educational attainment than the average German pupil. Of all pupils aged 12-17 years from socio-economically disadvantaged backgrounds, only 6% attend higher secondary education (Gymnasium), compared to 36% of all children in the same age range in Germany.

Business model: *Chancenwerk* operates with a location-based voluntary tutoring and mentoring model (in schools). By the end of 2013, *Chancenwerk* reached over 2,000 pupils in 16 locations throughout Germany. It forms mentoring teams between students and older pupils or older and younger pupils from socio-economically disadvantaged backgrounds, with the aim of empowering these children to develop the skills they need to succeed in school and in later life. Students and older pupils act both as tutors and as role models for the younger children. The younger children pay a small fee of EUR 10 for 16 hours of tutoring per month, allowing them to access tutoring services they would otherwise not be able to afford. Older students do not pay for tutoring services, but give tutoring in return for receiving tutoring from students. *Chancenwerk* is a leveraged non-profit which partly depends on philanthropic funding. Recently, *Chancenwerk* extended its mentoring services to children at the transition from school to work, where schools or companies pay for *Chancenwerk's* services.

Social impact: *Chancenwerk* closes the attainment gap for children from socio-economically disadvantaged backgrounds, with significant improvement of outcomes not only in educational attainment (school grades), but also in the employability rates and income levels they go on to secure in later life.

Investment: In 2010, BonVenture provided a loan to finance *Chancenwerk's* growth and helped the network in shaping and implementing its growth strategy in Germany.

www.chancenwerk.de

Investment example: *Insane Logic* (UK)

Segment: ancillary products/ services

The language and speech therapy specialist *Insane Logic* is the SVF's first (non-SIB) investment in the UK.

Social challenge: Every year 2.2m people in the UK require support in the area of speech and language. 1 in 10 children in the UK enter school with a speech, language or communication need, with the figure rising to 50% in socially disadvantaged areas. The UK has a shortage of speech and language therapists.

Business model: *Insane Logic* has created MyChoicePad, an educational iPad app that uses symbols and signs with speech to enable choice and communication for children with learning or communication difficulties. *Insane Logic* sells to families, schools and speech and language professionals. It currently reaches approximately 40,000 users throughout the UK, with more than 80% of them being under the age of 18. *Insane Logic* is a social business and distributes its products using a freemium app model. Additionally, B2B training packages for schools or speech and language therapists are available.

Social impact:

- Improved educational attainment and participation (inclusion) as well as increased mental health and self-esteem for children with speech and language need or learning difficulties.
- Increased mental health (family relations) and inclusion for their families through better parental support and participation in the therapy.
- Improved professional development (education) and motivation for the therapists.

Investment: In 2014, the SVF invested EUR 1m in equity in order to expand the development team and to strengthen operations, in particular sales and marketing. *Insane Logic* was an Ultd Big Venture Challenge Winner in 2011 and has been selected to participate in Telefonica's business accelerator program Wayra in 2012.

www.insanelogic.co.uk

Investment example: *Verbavoice* (D)

Segment: ancillary products/ services

In 2011, the SVF invested in *VerbaVoice*, a technology start-up which provides real-time communication services for the hearing-impaired.

Social challenge: Around 300,000 hearing-impaired people in Germany are excluded from many areas of society due to a lack of visual aids. Therefore, hearing-impaired citizens are legally entitled to support through a language and script interpreter, to help them negotiate a range of daily situations. This is cost-intensive, as the interpreters have to travel to each client individually.

Business model: *VerbaVoice* has developed a unique mobile solution which transfers voice into text, thus helping hearing-impaired people to communicate almost in real time. *VerbaVoice* is a hybrid non-profit, with a for-profit social business. It competes on the EUR 1.2bn German market for communication aids for the hearing-impaired with a legal entitlement to governmental sponsorship (through local authorities, integration offices, and the federal employment agency). Furthermore, *VerbaVoice* has built its operational model around the integration of hearing-impaired people- 27% of its staff are themselves hearing-impaired.

Social impact:

- Offering high quality, easy to access real-time speech recognition and visualisation to the hearing impaired, thereby fostering empowerment, equality and inclusion.
- Reduce the cost for access to visual applications for the hearing-impaired.
- Provide high quality work for hearing-impaired people, who are otherwise at risk of being unemployed.

Investment: The total capital needed for *VerbaVoice's* market entry in Germany amounted to EUR 740k, of which EUR 500k was provided by the SVF as lead-investor, with the other EUR 240k coming from the Venture Capital Fund Bayern Kapital. The SVF also supported subsequent funding rounds for *VerbaVoice* and co-invested with KfW, the state-owned German development bank as well as with commercial investors.

www.verbavoice.de

Endnotes

[1] Throughout this report, we define impact investing as any type of repayable investment with a focus on both social impact and financial return, following Melinda Weber (2012), *Impact Investing in Deutschland*, Impact in Motion and Bertelsmann Stiftung.

[2] Stephanie Petrick (2013), *Impact Investing in the area of long-term unemployment*, The Social Venture Fund

[3] Stephanie Petrick et al. (2013), *Impact Investing in ageing*, The Social Venture Fund

[4] Copps, J., (2013), *Outcomes Map education and learning,* New Philanthropy Capital

[5] OECD (2013), *Education at a Glance 2013: OECD Indicators*, OECD Publishing

[6] Loder, John, et.al (2013), *Social Investment in education*, The Young Foundation

[7] Copps, J., (2013), *Outcomes Map education and learning,* New Philanthropy Capital

[8] Autorengruppe Bildungsberichterstattung (2012), *Bildung in Deutschland 2012*

[9] ibid

[10] Copps, J., (2013), *Outcomes Map education and learning,* New Philanthropy Capital

[11] ibid

[12] Loder, John, et.al (2013), *Social Investment in education*, The Young Foundation

[13] D. Capital Partners (2013), *Impact Investing in Education*, ESP Working Paper Series

[14] ibid

[15] Brown, Adrian, et. al. (2012), *The first billion: a forecast of social investment demand*, The Boston Consulting Group

[16] OECD (2013), *Education at a Glance 2013: OECD Indicators*, OECD Publishing

[17] Weber, M. et al.(2012) , *Impact Investing in Deutschland*, Impact in Motion, Bertelsmann Stiftung

[18] Impact in Motion (2014) estimate based on market research.

[19] D. Capital Partners (2013), *Impact Investing in Education*, ESP Working Paper Series

[20] Sometimes also referred to as “B2G“.

[21] Brown, Adrian, et. al. (2012), *The first billion: a forecast of social investment demand*, The Boston Consulting Group

[22] Impact in Motion (2014) estimate based on market research.

[23] Gregory, D., et. al. (2013), *Investment Readiness UK*, ClearlySo, New Philanthropy Capital