3 Takeaways Podcast Transcript
Lynn Thoman
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Ep 37: Investing in Positive Social Outcomes with Social and Career Impact Bonds: Tracy Palandjian

INTRO male voice: Welcome to the 3 Takeaways podcast, which features short, memorable conversations with the world's best thinkers, business leaders, writers, politicians, scientists and other news-makers. Each episode ends with the three key takeaways that person has learned over their lives and their careers. And now your host and board member of schools at Harvard, Princeton and Columbia, Lynn Thoman.

Lynn Thoman: Hi everyone, it's Lynn Thoman. Welcome to another episode. Today, I'm excited to be here with Tracy Palandjian. Tracy is CEO and Co-Founder of Social Finance, which mobilizes capital to drive social progress. I'm excited to learn how impact investing works and what Pay for Success really means. I'm also excited to learn how well social impact bonds have improved outcomes from improving high school graduation to reducing recidivism by people released from jail. Welcome, Tracy, and thanks so much for our conversation today.

Tracy Palandjian: Great to be with you, Lynn.

LT: Great to be with you, too, Tracy. Tracy, what are social impact bonds and Pay for Success bonds, and why is there a need for them?

TP: Pay for Success movement is part of a much broader movement, what I would call the braiding together of impact investing and evidence-based policy making. It's at the end of the day, all about how do you reallocate incentives, realign risks, so that you can get better outcomes for the community. Social impact bonds and career impact bonds are two of these tools that our firm, Social Finance, which is an impact investing non-profit brought to this country over the last 10 years, and we're just really excited to see how these instruments can bring together the best of government and the best of markets in service of our communities.

LT: Can you give us an example of a social impact bond?

TP: A social impact bond brings together several uncommon partners to the table, government, traditional non-profits who serve vulnerable members of our community, impact investors in a way that is designed to deliver measurable outcomes for our communities. For contacts, why is a social impact bond even needed? And I would start by saying that the reason why we face these massive social and environmental challenges, whether it's education inequities or health disparities or workforce development issues, is not because our public sector and our philanthropic sector are not focused on these challenges. In fact, if you look at how much our government spends on solving these issues it's actually quite an astounding amount of money. Peter Orszag and John Bridgeland, working in different administrations, one R and one D, came together and wrote a really interesting article called Moneyball for Government, and they basically said that less than 1% of money being spent on social programs, the nearly $1 trillion annual spend on social programs, whether it's an after school program or a homeless assistance program, or a job training program, that less than 1% of that spend actually delivered outcomes throughout communities rather, government spends money on outputs.

TP: How many people are enrolled, how much is your program, how many hours are in your program? Rather than focusing on outcomes, what actually happens to these people, what happens to their lives after they go through these programs? So the social impact on is specifically targeting this chief challenge that our policy makers face, which is how do you reorient our public spending, our taxpayer spending towards outcomes instead of outputs? And that is where the impact investor comes in, and the typical social and background arrangement... I'll give you a specific example, which is a deal that we launched in the State of Massachusetts back in 2017, where the state realized that immigrants and refugees really power our local economy, in fact, in some sectors, immigrants and refugees make up more than half of the workforce in hospitality, in a lot of the services industries. Yet our spending on Adult Basic Education, on upscaling and job re-training is just not getting the kind of results that we want.

TP: So partnering with the outgoing Governor Deval Patrick and the incoming Governor Charlie Baker, we devised a social impact bond with investor capital, almost $13 million from investors to a vast array of institutions and individuals and family offices, the $13 million went toward a fantastic program delivered by a partner, Jewish Vocational Service, which seeks to serve 2,000 immigrants and refugees in the Greater Boston area in various job training programs. Becoming a certified nursing assistant, becoming a pharmacy technician, etcetera. And how do the investors get their money back? We have signed a performance-based contract with the State of Massachusetts that basically stipulates success of this program, in this case, job placement and wage mobility of these participants measured at their pre-program wages and their post-program wages after two years. And not to get wonky but it's measured through a randomized controlled trial, so the most rigorous of evidence, and that is how our investors get their money back based on the outcomes of these 2,000 lives, and we're really pleased to say that the results are extraordinary. People are earning 3,000 to 7,000 depending on the program more than the control group, and people's lives are getting better. And they're going up the economic ladder, and our investors also stand to get their money back and at really great rate of return.

LT: Congratulations, Tracy, that's phenomenal. Can you tell us about the range of social impact bonds over the last 10 years, what have they been used for?

TP: Yeah, social impact bonds have been a global movement, they are now over 200 social impact bonds in over 30 countries. The United States is the largest market with around 30 or so social impact bonds launched mobilizing several hundred million dollars in the United States, and the global market is obviously much bigger. It is still a young movement, it is all about making better use of our public resources, by using the discipline and the rigor of markets to help realign those incentives and reallocate risks. We're also really excited to have launched another Pay for Success vehicle called the Career Impact Bond which is all about getting people upscaled and rescaled into the jobs of the future. And in that particular arrangement, in the career impact bond, we typically work with, sometimes with government and sometimes without, but all focus on upscaling the individual into skills and sectors that remain recession resilient, like IT and green energy and health care.

LT: How well have social impact bonds worked over the last 10 years?

TP: It's still a work in progress. As you can imagine, Lynn, all these arrangements, whether it's a social impact bond or a career impact bond, they are multi-year arrangements. It takes time to enroll a person into the program, it takes time to go through the program and importantly, not just measure what happened to the person right after the program. But also over time. Are their livelihoods better, are their families better off? The track record of "completed deals," if you will, is still sparse because there aren't that many deals that have been finished, but we're really encouraged by the results, and especially in this current moment of high-governed budgets, again, rising social need, we just feel that these new vehicles that are focused on outcomes is more important than ever.

LT: There was a social impact bond launched a couple of years ago, there was a lot of publicity for Goldman Sachs. It was designed to reduce recidivism. People being released from jail to reduce the rate at which they committed new crimes. What happened to that social impact bond? Was it successful in reducing recidivism? Did Goldman get their money back? How do you think about it?

TP: Well, I am commenting on other people's deals, and that's always a danger. 'Cause I only know as much as I know because Social Finance was not involved in that social impact bond at all. It was launched, I believe, in 2012 by the Bloomberg administration. Goldman Sachs as the sole investor in the deal with a significant credit enhancement by Bloomberg Philanthropies, it was a beautifully constructed and designed deal and incredibly well-intentioned because it was focused on reducing recidivism for folks leaving Rikers Island Jail. The headline is that the deal did not intend to reduce the recidivism metrics that they intended to achieve, and that the program was terminated early as a result. And Goldman Sachs lost money, Bloomberg Philanthropies also wrote a check, but the program worked as intended because the whole point about Pay for Success is that government doesn't pay for a program that didn't work, and the investors would stand to lose their money if the program didn't work. So it's definitely played to the principles of Pay for Success. But I would also comment that Rikers Island is an extremely challenging environment to implement any kind of program, and lo and behold, we're sitting here in 2021, the population of Rikers has gone down and it's heading in the right place, but when this program was being implemented, seven, eight years ago, it was just a really challenging place to do any kind of program.

LT: Can you talk about the range of areas that social impact bonds have been used for?

TP: We've worked with a lot of health applications, I would say that workforce development, worker re-training stand high on the list. We've also worked on early childhood programs, we have an amazing program in South Carolina that's focused on zero to three, prenatal to three. It's also been used outside of the country to think about disability issues and actually in the continent of Africa. There are some really exciting applications in Australia and in the European Union on health and education and workforce development. So the applications are quite broad, but it's also not a panacea, it's not intended to solve every social problem, and it only works where there can be clear metrics defined, and when there is a willing government payer.

LT: You mentioned that there are about 200 social impact bonds now, outstanding, can you give us a sense of the total dollars?

TP: It's probably around half a billion dollars, the deals outside of the United States are smaller, the United States deals are larger, and we have much to owe to a historic piece of legislation that we were cultivating since the Obama years, which got signed into law in 2018, and that's called the SIPPRA, the Social Impact Partnerships to Pay for Results Act. There $100 million has been set aside and being administered by Treasury to support state and local governments to pursue more of these Pay for Success projects, and we're really excited to see how this legislation is going to be reinvigorated in the Biden administration, and it's just a really exciting public-private partnership, evidence-based policy making, a set of principles playing out in this piece of legislation.

LT: What's next for social impact bonds and Pay for Success? What are you most excited about?

TP: I cannot tell you how excited I am about the career impact bond application. Career impact bonds are 100% focused on skills training. I think that, Lynn, you and I spend a lot of our adult lives thinking about college, being middle class, that college is going to be an important silver bullet to put a lot of people into economic well-being. And I think that we're all quite disconcerted about the sobering facts that college attendance has contributed to this ballooning student debt crisis, $1.7 trillion of student debt held by more than 40 million Americans. And that many people start college, take on that debt and actually don't graduate with the appropriate skills to thrive in the 21st century economy. And many people take on the debt and don't even end up with a degree.

TP: And we're very focused on middle skills training at Social Finance now, and even amidst the pandemic, Lynn, there are almost 7 million unskilled job openings across the country. More than half of them are great jobs with good benefits, with upward mobility. I would call them, these jobs fall into the middle skills arena, jobs that require skills training beyond the high school degree, a certificate in Advanced Manufacturing, a license in truck driving, a diesel mechanic certificate, a credential in software engineering and UX design and cybersecurity, all these amazing jobs that need specialized training and skills training that take maybe a three-month program or a nine-month program, and yet these are jobs that can catapult people up that economic escalator to achieve economic well-being for their families. And the career impact bond is very much focused on enabling low-income students, people who are shut out of these great opportunities to get the skills to land these jobs in the economy and a financial arrangement that is no risk to the individual.

TP: So that's a career impact bond which is basically student-friendly, income share agreement, and we're really excited about how we can contribute to an equitable recovery by helping more people get the skills to achieve financial stability.

LT: Tracy, before I ask you for your three key takeaways, is there anything else that you would like to talk about that you haven't already touched upon?

TP: A lot of our work is powered by impact investors, and this is a big group of people and extremely heterogeneous, Lynn. And I recall that there are a lot of impact investors who are excited about achieving a double bottom line, yet increasingly, as this field evolves and proliferates, I think that there are a lot of impact investors who are thinking about impact with more nuance, with a greater commitment to impact transparency, impact measurement and making sure that the impact is there. You might have heard about impact washing in this very rapidly growing field of ESG investing and impact investing. And I would just highlight that increasingly there are more and more people who are really focused on the impact that they are after, and just because you're investing in a company that's in education doesn't necessarily mean that you'll achieve impact. Industry definition is typically not the right definition around an impact investment, and I'm really encouraged about the sophisticated conversations that are taking place right now on how do you define impact, how do you measure for that impact and how do you importantly manage for that impact over time, so that everyone around is held accountable to making sure that we're achieving impact for our communities.

LT: Everybody is focused on that right now. How do we actually achieve the results that we want?

TP: Exactly.

LT: Tracy, last question, what are the three key insights or takeaways that you'd like to leave the audience with today?

TP: Such a great question, Lynn, and I could go in so many different directions. I think my first takeaway is the importance of incentives, it sounds quite old-fashioned to say, incentives matter. But if you think about our social challenges out there, I think that we have a lot to gain by rethinking incentives, how to identify incentives and risk, and then reallocate our resources to realign incentives better. We need to think about who pays, who benefits, who bears the risks, and align incentives in our markets and systems in a way to have people and communities at the heart of it, rather than thinking about how would the financial incentives win alone for investors. But really rethinking, how does everyone win, but at the end of the day, holding the impact on individuals and on communities as the North Star of the overall system. So that will be my first takeaway, Lynn. And as you can see, our social impact bond and our career impact bond mechanisms are really at the heart of it, all about incentive realignment.

LT: And Tracy, your other two key takeaways?

TP: We talked a little bit about impact investing and this exciting and growing movement and I guess my second takeaway, Lynn, would be that ESG and impact investing is a rich and growing space, and there are now so many exciting approaches across all asset classes. And I would encourage people to really be committed to thinking about impact and to think about impact in a way that shouldn't be thinking about trade-offs. Like impact-first investment, for example, shouldn't just mean, as some people fear, bad investing that you don't care about financial returns. What we really want people to really focus on is, how do you make sure that the returns that matter most should be measured in lives change, not simply in financial gain? So that is what I would encourage people to do is not to compromise social impact for financial return as we enter into this brave new world of impact investing.

LT: Yes, and for those unfamiliar with ESG, it's environmental, social and governance. Tracy, your third takeaway.

TP: My third takeaway maybe is going to be less succinct, if you will, Lynn. What I've learned most about the last 10 years on this journey, having co-founded Social Finance 10 years ago, is that cross-sector and cross-silo collaboration is more important than ever. We face some significant and daunting social and economic challenges, and we really need to reach across divides and bring uncommon partners together around common causes. And no one actor can act alone to address these problems at scale and in a meaningful way. So we really need to come together across sectors, across disciplines, across political lines, to learn from one another to have that same North Star. And I'm always reminded of this book, I don't know if you've read it, Lynn, called Range. The author is David Epstein, he writes about why generalists triumph in a specialized world. I would say that most of the modern 20th century specialization has been the name of the game in business, this could sometimes lead to narrow thinking in academia, specialization and depths of knowledge has always been heralded. And then one could even argue that specialization may have played some role in the 2008 financial crisis because people weren't thinking across systems and across markets as many of these systemic issues when undetected.

TP: I think that this might be the era for generalists, how do you think about taking the best of different sectors, the best of policy, the best of markets, and bring different people with different thinking together to solve common challenges? And I always say to young people, if you really want to have a career in social impact and social change, you should really try to build a diverse set of experiences and interdisciplinary skills, because these are the skills of our time to solve these very complex and inter-related and interdisciplinary challenges. That is probably my last takeaway, not a succinct one, but I hope you get what I mean, Lynn. [chuckle]

LT: Tracy, this has been terrific, thank you so much for our conversation today, and thank you for all you're doing to improve outcomes for everyone.

TP: Thank you so much, Lynn. It's always great to be with you.

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