ICRC Humanitarian Impact Bond for Physical Rehabilitation:

A case study produced as part of the independent evaluation of the Department for International Development's Development Impact Bond Pilot Programme

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“Today’s humanitarian challenges are immense, causing suffering for many millions of men, women and children around the world. This funding instrument is a radical, innovative but at the same time, logical step for the ICRC. It is an opportunity not only to modernise the existing model for humanitarian action, but to test a new economic model, designed to better support people in need.

We hope that once the pilot project is proven, it will demonstrate that non-traditional financing models can work. There is great potential for investments that are built around improving the social, environmental and economic conditions so that humanitarian action advances in impact, effectiveness and scale in ways never seen before.”

Peter Maurer, ICRC president (News release September 2017)

Summary

TIME PERIOD:
July 2017 – July 2022

THEMATIC AREA:
Physical rehabilitation in humanitarian contexts

COUNTRIES:
Mali, Nigeria, and the Democratic Republic of Congo

TARGET POPULATION:
Persons with physical disabilities in Mali, Nigeria, and the Democratic Republic of Congo

OUTCOME METRIC:
Staff Efficiency Ratio (SER), calculated by the number of beneficiaries having regained mobility thanks to a mobility device, divided by the number of local rehabilitation professionals.

LOAN VALUE:
26.09 million CHF

SERVICE PROVIDER:
International Committee of the Red Cross

OUTCOME FUNDERS:
The Swiss Confederation ('Switzerland')
The Kingdom of Belgium ('Belgium')
The Republic of Italy ('Italy')
The United Kingdom ('UK')
La Caixa Banking Fondation ('La Caixa')

INVESTORS:
Munich Re, Lombard Odier pension fund and charitable foundations and others

This case study report covers the ICRC Humanitarian Impact Bond for Physical Rehabilitation, which funds the building of three new physical rehabilitation centres in Mali, Nigeria and Democratic Republic of Congo (DRC). As a part of the HIB, ICRC is also piloting efficiency improvement measures testing and building a Digital Centre Management System (DCMS).

The case study report focuses on the Humanitarian Impact Bond (HIB) model and early successes and lessons learned during the design and set up phase of the HIB. It summarises findings from consultations undertaken as part of the DfID commissioned independent evaluation of the DIBs pilot programme. Consultations were undertaken between July-November 2018 with the main stakeholders involved in the design and set up of the HIB. This included the service provider, outcome funder, investors, and advisor. A full list of consultations is set out at the end of the case study.

The ICRC HIB launched in July 2017 and will conclude in July 2022. The funders have committed a maximum of 26.09 m CHF to the intervention, the majority of which is payable in 2022 depending on the results of the programme. The social investors provide the working capital to launch the centres, paying a total of 18.6 m CHF. The final amount payable by the outcome funders depends on the Staff Efficiency Ratio, calculated by the number of beneficiaries having regained mobility thanks to a mobility device, divided by the number of local rehabilitation professionals. The returns are scaled to incentivise efficiency savings. If the new centres operate less efficiently than past centres, the investors will make a loss on their investment and ICRC will be liable to make a loss payment; however, if the centres deliver more efficiently, then the investors will recover their investment and can make a moderate return.

ICRC led the development of the HIB. ICRC designed the HIB with the support of Kois, and led the discussions with potential outcome funders. Funding from outcome funders was lower than initially expected. ICRC started approaching investors at the end of 2016. The main focus of negotiations was the outcome metric, outcome target, interest rate and capital protection and timing of payback. Contracting was a particular challenge as the legal frameworks in Switzerland and Belgium had no provisions for the HIB model.

The key enablers to the set up of the HIB was the strong leadership of ICRC and its partners, the development of a clear outcome metric, sufficient evidence for the intervention, data to build up the business case, the strong reputation and track record of ICRC and financial and private sector expertise within ICRC. Challenges included identifying outcome funders, making the necessary shifts within outcome funders and ICRC to accommodate the HIB and adapting the social impact bond (SIB) model to the humanitarian sector.

The key lessons learned were that:

1. HIBs should be developed to meet a specific need;
2. It is important to test the legal feasibility of operating a HIB at an early stage of the process;
3. Additional time and costs are required to manage multiple investors and donor requirements;
4. Investors need to be involved at an early stage;
5. Outcome metrics need to be designed to reflect existing data;
6. There needs to be flexibility in terms of understanding what an impact bond is, in terms of the structuring of the impact bond and the roles of different stakeholders; and
7. There are trade-offs between undertaking negotiations in a bilateral or more collaborative fashion.

The main advantages were that the HIB provided longer term upfront capital to ICRC, brought together existing ICRC partners and new partners, brought in private sector finance which enables the funding of the DCMS and efficiency improvement measure testing, in addition to the three new physical rehabilitation programme centres. The main disadvantages were that the HIB was complex to design and expensive to set up. There is mixed opinion about the extent to which the HIB led to a more careful and rigorous design of the intervention.

The following sections cover the DIB's model and the intervention funded, the history of development, the enablers and challenges to setting up the DIB, the lessons learned and advantages and disadvantages to using the DIB before concluding.

Intervention

The International Committee of the Red Cross (ICRC) is an impartial, neutral and independent organisation that manages humanitarian operations in conflict zones through its national delegations in over 80 countries. The ICRC Humanitarian Impact Bond (HIB) funds the following activities:

1. Build 3 new Physical Rehabilitation Programme (PRP) centres to provide people with physical disabilities with mobility devices and physiotherapy in countries with significant unmet needs (Mali, Nigeria, Democratic Republic of Congo);
2. Train local staff to deliver high quality physical rehabilitation services in these centres;
3. Pilot and rigorously assess efficiency improvement measures (EIM) across eight[1] existing ICRC PRP centres, and build a Digital Centre Management System (DCMS) with the aim of improving efficiency and maintaining quality patient outcomes; and
4. Use the DCMS and improved operational protocols based on the findings from the efficiency improvement measure testing to operationalise the three new centres.

ICRC is delivering the intervention within its Physical Rehabilitation Program (PRP)[2] using the same reporting structure and procedures.

1 Cambodia, Pakistan, Myanmar, Zinder and Niamey in Niger, Mali, Togo, Madagascar

2 The PRP has been operating since the 1979, formerly the Physical Rehabilitation Unit

HIB Model

> **The ICRC Humanitarian Impact Bond is the first humanitarian bond, so named because it is an impact bond operating in a humanitarian context. The HIB launched in July 2017 and will conclude in July 2022.**

The funders have committed a maximum of 26.09m CHF, which is made up of 10.0m CHF from the Swiss Confederation; 9.31m CHF (8.7m EUR) from the Kingdom of Belgium; 3.21m CHF (3.00m EUR) from the Republic of Italy; 2.50m CHF (2m GBP) from the United Kingdom and 1.07m CHF (1m EUR) from La Caixa Foundation. The final amount payable by the funders will be based on the results of the programme, payable in September 2022, with the exception of La Caixa's EUR 1m funding, which will be payable upon the successful construction of the centres.

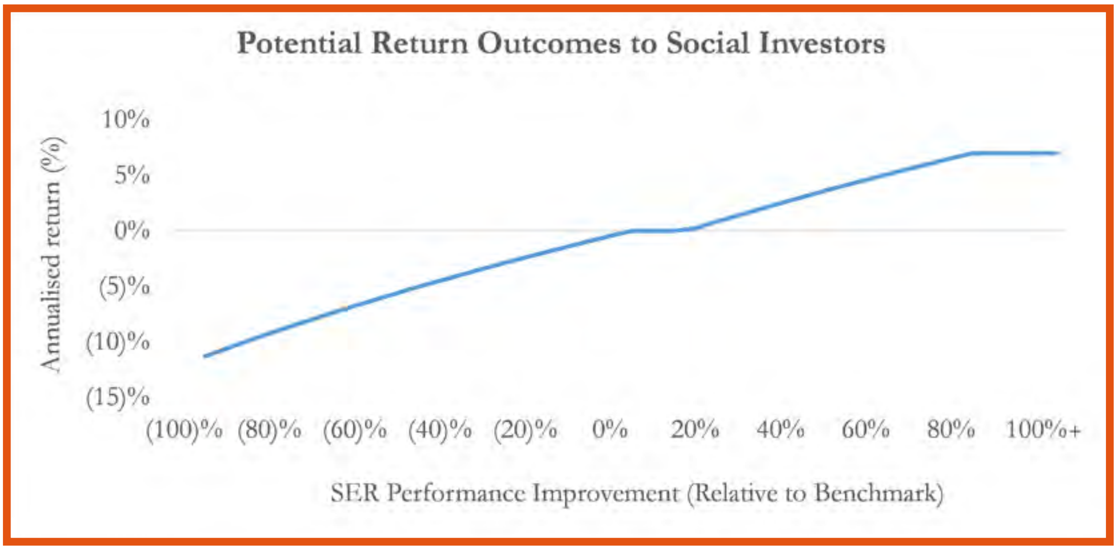
As the outcome funders only pay at the end of the project, the social investors provide the working capital to launch the centres. New Re (the cornerstone investors) provided 10m CHF, and the other private investors identified by Lombard Odier, the placement intermediary, provided 8.60m CHF. This was paid in two equal tranches, in July 2017 and July 2018.

Amounts payable by the outcome funders, and therefore returns to social investors, will be based on the Staff Efficiency Ratio (SER), calculated by the number of beneficiaries having regained mobility thanks to a mobility device, divided by the number of local rehabilitation professionals. The SER in the final year of the programme will be compared to the baseline SER (established from historical data from other comparable ICRC centres in Africa). ICRC's self-reported results data, which will be used to calculate the SER, will be verified by an independent auditor. The auditor will visit a 5% sample of beneficiaries to confirm that they have regained mobility, based on a standardised physical functionality test used by ICRC.

The returns are scaled to incentivise efficiency savings. If the new centres operate less efficiently than past centres (or do not open), the investors will make a loss on their investment and ICRC will be liable to make a loss payment corresponding to 10% of investor capital. However, if the centres deliver more efficiently, delivering services to more people with the same resources, then the investors will recover their investment and can make a moderate return.

If the outcome measure is less than or equal to one (i.e. there is no improvement in the SER of the HIB centres relative to the baseline centres), the ICRC will make a first loss payment to the investors of 10% of the commitments. The return to the investors ranges from a loss of 11.3% per year (equating to a loss of 40% of their initial commitment) if there is a 100% deterioration in the SER compared to the benchmark, to a return of 7.0% per year (equating to 134.5% of the commitments) if there is a 80% performance improvement. Returns are calculated inclusive of the 2% annual coupon payments, that is, the annual interest paid to investors based on the amount owed. Figure 1 below sets out the range of potential returns to investors.

Figure 1: Range of Potential Returns



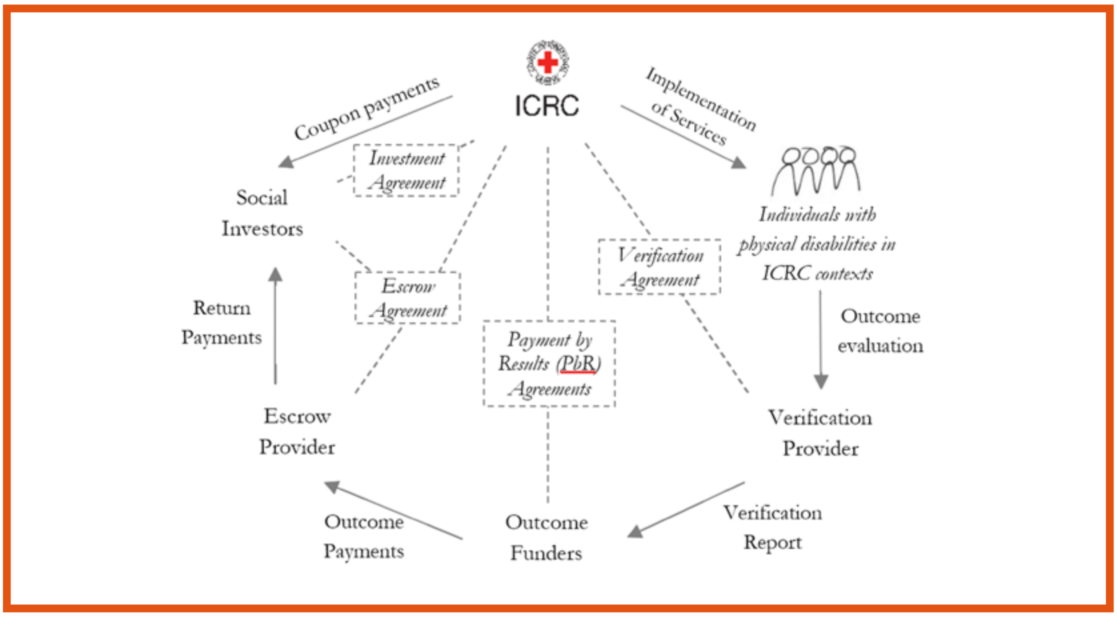
Source: ICRC Summary of the Transaction

The payment made by the outcome funders will be made to the Escrow Account, governed by the terms of the Escrow Agreement between the ICRC, the social investors and the Escrow Bank, which sets out that all withdrawals and transfers relating to the final payments will be done in accordance with the contractual agreements, as set out above.

The Operating Review Committee Meeting (ORCM) meets twice a year, for the ICRC to inform stakeholders on the progress of delivery. Additionally, ICRC reports quarterly on the use of the funds, and leads on performance management of the intervention.

ICRC has a direct contract with both the outcome funders and the investors, and Figure 2 below summarises the contractual relationships:

Figure 2: ICRC HIB Structure



The table below sets out the roles played by the stakeholders within the ICRC HIB:

Table 1: ICRC HIB Stakeholders

DESIGNER	ICRC and Kois
SERVICE PROVIDER	ICRC
SERVICE USERS	Users of new ICRC centres, and the 8 pilot centres
GOVERNMENTS	Local governments in Mali, DRC and Nigeria
OUTCOME FUNDERS	Swiss Confederation; Kingdom of Belgium; Republic of Italy; United Kingdom; La Caixa Foundation
INVESTORS	Munich Re, Lombard Odier pension fund and charitable foundations and others
OUTCOME VERIFIER	Philanthropy Advisors
LEGAL ADVISORS	Norton Rose Fulbright and Oberson and Abels

Background

ICRC had been exploring new ways to bring in private donors and access innovative financing, and the idea of using a HIB first arose from a discussion between ICRC and Kois. ICRC discussed this with its traditional donors and also sought new ones.

Various discussions at various levels were held with various governments. For example, the President of the ICRC led strategic discussions with the Swiss and Belgian governments, with whom there were already broader discussions on income diversification and innovation. The Swiss and Belgian governments were interested in supporting ICRC to test this new funding mechanism, which was seen as a potentially useful way to build stronger relationships with the private sector and contribute to the closing of the financing gap. Building on strong, existing partnerships, the Belgian government, followed by the Swiss government made a political commitment to supporting ICRC. ICRC received a grant from the Government of Netherlands of 1.2m EUR to cover the costs incurred during the set up phase.

ICRC also discussed this with new donors. The World Bank expressed interest. However, as ICRC had not previously worked with the World Bank, it proved too challenging to navigate both a new funding mechanism and a new relationship.

Design of intervention

ICRC decided that the Physical Rehabilitation Program (PRP) should be the focus of the HIB, as it had strong 'measurability' and extensive amounts of historical data. Kois was commissioned to undertake a feasibility study, and, following that, to support ICRC in developing the HIB instrument. Kois worked with ICRC to identify a way in which the PRP data could be used to develop an outcome metric as well as well as to improve the efficiency of operations. Feasibility studies for building and operation of new PRP centres was undertaken in nine locations. Within these, ICRC identified five centres which fit within the constraint of an impact bond, which were namely operationalisation within the 5 year timeframe of the impact bond and security and cost constraints.

Identification of outcome funders

ICRC led the discussions with potential outcome funders. The La Caixa Foundation was one of the early backers of the HIB, and represented a new donor for ICRC. Additionally, the Swiss and Belgian governments, already committed, supported ICRC with reaching out to other potential donors. A side event was held at the World Economic Forum and other bilateral donors and foundations were contacted in an attempt to recruit additional outcome funders. While there was interest in the model generally, there was limited uptake from other donors because of the concerns with the risk of using a relatively untested model and a model that did not necessarily fit within their existing structures and funding mechanisms.

The exceptions were DfID, who were interested in learning lessons from the piloting of the HIB and included it within its DIBs pilot programme and the Italian government. The list of confirmed outcome funders was finalised towards the end of 2017, and the lower than anticipated level of funding from outcome funders meant that only three centres were eventually funded through the HIB, instead of the five originally planned for.

Identification of investors

ICRC started discussing the impact bond with investors at the end of 2016, when a number of the terms of the impact bond had been agreed with the outcome funders confirmed at that stage. As a 'bond' is a particular market product within Switzerland, ICRC had to call the HIB Program for Humanitarian Impact Investing (PHII) when approaching investors. ICRC led the bilateral discussions with the investors. The names of the investors were not shared with the other actors until confirmed, for confidentiality reasons. The investors included the cornerstone investor, Munich Re and its subsidiary New Re, and other investors identified by the placement intermediary, Lombard Odier.

Investors undertook a comprehensive risk assessment and due diligence, the process through which an organisation's strengths and weaknesses are assessed by a potential investor considering investment. This was used to generate a credit rating for ICRC, which was used as a basis for the investment decision.

Negotiations

ICRC, with Kois support, designed the proposal and model, which was presented to outcome funders and investors to review. ICRC led the negotiations on the terms of the HIB. ICRC led most of the negotiations directly with the other actors, though there was some collaboration between the investors themselves and the outcome funders, in particular between the Swiss, Belgians and UK governments, to discuss contract modalities.

The following terms were the main focuses of the negotiations:

Outcome metric: There was a wealth of data on the PRP, which was used to explore potential outcome metrics. The challenge was to find a metric that would take into account diversity, given the range of contexts where ICRC operates PRP centres, and which would make use of the historical data available. The metric adapted the cost-saving focus of social impact bonds (SIBs)[3] in the UK to improved efficiency, which was considered more relevant to the humanitarian sector and ICRC's operating model. A key discussion was on the trade-offs between efficiency and attribution in the design of the outcome metric, and balance between focusing on outputs and outcome.

ICRC and Kois jointly designed the SER. The formula was designed to make physical rehabilitation centres comparable between each other and to prevent perverse incentives. Stakeholders commented that it is a comprehensive measure, 'boiling down' something complex into a number that can be compared across centres. It also takes into account the majority of activities and outcomes funded within the PRP programme, and considers the quality of delivery by focusing on the outcome of regained mobility. Furthermore, the HIB activities are intended to make a difference not only in the three new centres, but also across the entire PRP. Hence, the outcome metric which focuses on efficiency, instead of number of outcomes reached, is useful in capturing whether the DCMS and EIM testing is leading to increased efficiency, and the likely value of the capital investment for the broader PRP. However, the SER does not capture the effects of certain ICRC activities, such as supporting beneficiaries with social inclusion and participation programmes, mental health and sport activities. The SER focuses on mobility regained, and does not monitor delivery against social inclusion outcomes or longer term social and economic inclusion outcomes.

Outcome target: ICRC worked with Kois in order to set an ambitious yet feasible maximum SER, aligned with the maximum potential rate of return. Firstly, ICRC and Kois set a benchmark SER, using historical data from comparable Africa PRP centres. The target SER was set based on the percentage improvement between the global best performing and average centres, based on 2015 PRP centre data.

Interest rate and capital protection: These two terms were discussed iteratively between the stakeholders. A balance was needed between the risk premium paid and risk taken.

The payment model aligns SER improvement with the interest rate, which results in alignment of increased efficiency (and correspondingly, beneficiaries reached) with increased return for the investor.

In terms of the maximum return corresponding to the target SER, as a starting point, Kois provided ICRC with interest rates for investments in India as a benchmark, as well as interest rates used within the existing Educate Girls DIB. The key consideration was what would be acceptable to investors, and what would be accepted by the public as 'reasonable' and 'defendable'. Common ground was agreed around 7%. One outcome funder noted that 2% was too low and 15% too high, and 7% seemed to be a middle ground. Another outcome funder commented that an informal benchmark used was the 3-5% interest rate on a risk free loan, against which the maximum 7% return seemed reasonable.

In order to balance this return with the risk, ICRC and Kois decided to introduce an element of capital protection. This was an area of contention, as it reduced the risk transferred to investors. In order to balance the different preferences of the different actors, it was agreed between stakeholders that 60% of investors' capital would be protected, with ICRC covering the first 10%.

ICRC presented potential investors with these draft terms. To test the acceptability of the risk and return profile, investors compared the proposed 7% return with the risk profile of the investment, using insurance models to calculate acceptable levels of return, and concluded that the return proposed was acceptable.

3 There are three different types of impact bonds. depending on the funder and context of implementation. Social Impact Bonds (SIBs) were the first types, and inspired DIBs (DIBs) and Humanitarian Impact Bonds (HIBs). While broadly comparable in their basic principles and setup, SIBs refer to impact bonds in which the outcome funder is the government of the country in which the intervention is implemented. These types of bonds have been developed in high, middle and low-income countries. DIBs are impact bonds typically implemented in developing countries, where the outcome funder is a donor agency or foundation often operating in a different country. HIBs are essentially DIBs operating in humanitarian situations.

Timing of payback: The majority of outcome funding is payable at the conclusion of the HIB, and aligned with the SER. There were many discussions on how to structure the deal. A first tranche repayment linked to the construction of the centre was proposed. There were two considerations around this. One outcome funder expressed an opinion that this detracted from the impact bond mechanism, and made it more similar to a grant. On the other hand, another outcome funder pointed that the milestone was still linked to a tangible output, and the earlier repayment would have made the deal cheaper, as it would have reduced the interest component of the repayment to investors. As not all outcome funders agreed with two payment milestones, ultimately the majority of the deal reverted to one outcome funder payment at year 5, with the exception of La Caixa's contribution of EUR 1m, which is pledged for when ICRC meets the construction milestone.

Contracting: Contracting was a particular challenge. Challenges including legal frameworks in certain countries not having provision for the HIB model and restrictions on the ability of donors to pay interest to a social investor. These challenges required extensive time to navigate on the part of al actors. Finally, there were certain Swiss legal and tax issues affecting ICRC, including considerations of whether a non-profit organisation's issuance of an impact bond is admissible under Swiss law or other legal sources such as the organisation's constitution, requirements regarding the public offering of bonds and implications for withholding tax.[4]

While ICRC and Kois originally intended to have one contract, ultimately different contracts were needed for each outcome funder, due to their different requirements and respective legal frameworks. On the other hand, the investors agreed upon one investor contract which was signed by all investors.

4 https://www.obersonabels.com/sites/default/files/articles/Jusletter_swiss-legal-and-tax-_39c1e236ee_en.pdf

There were a number of enablers, which facilitated the setting up of the HIB. These are set out below. We have structured these around the LOUD framework , which identified the critical success factors to launching a SIB in the UK (collective leadership; clear outcomes; shared understanding; and data). It is interesting to note that these same enablers in the UK existed for the ICRC HIB.

Enablers

1 Collective Leadership:

- **Strategic (between members of the leadership team)**;

Stakeholders generally agreed that ICRC built strong relationships with all actors, which facilitated the setup of the impact bond. Furthermore, the political commitment of the Belgians and the Swiss to support the ICRC, and the commitment from senior leadership with the ICRC to launch the HIB, was crucial for enabling the launch of the impact bond.

- **Organisational (between these leaders and their internal stakeholders)**

There was strong commitment to using the HIB within ICRC and a number of outcome funders, and significant staff time was dedicated to exploring and launching the HIB. While there was originally not a set team with ICRC working on it, the roles became clearer, and a core team was set up.

There were some reservations with using the HIB within the ICRC and outcome funders. In order to gain buy-in, there was significant work done to explain the HIB model and the reasons for exploring this innovative mechanism of financing.

2 Clear outcomes – measurable outcomes and linked to overall objective of the intervention.

Kois supported ICRC with the development of the SER, which enabled measurement of outcomes as well as efficiency improvements with reference to benchmark data, one of the key objectives of the intervention. The use of a physical functionality test enables a focus at the outcome level, and the quality of outcomes.

3 Shared understanding of the policy 'problem' and sufficient evidence for the intervention so that it is credible or knowledge-based.

The PRP has been running since 1979, and hence there is strong evidence for the approach, and established policies, procedures and systems in place. It was noted that the majority of stakeholders were already convinced of the value of the PRP. The DCMS and efficiency improvement measures testing were the new component of the HIB. ICRC had some evidence of the potential of using efficiency initiatives, at certain 'case study' centres.

4 Data to build up a business case, including data on the eligible cohort and outcomes likely to be achieved.

Benchmark data on 163 PRP centres was used by ICRC and Kois to develop the target outcomes, as well as for the investors to calculate the risk of their investment. The PRP model and use of the physical functionality test to measure regained mobility is well established, the monitoring an evaluation system and expected outcomes clearly defined.

5 Other factors

Service provider track record and reputation: Another key factor that enabled the launch of the HIB was the strong reputation of ICRC. Certain outcome funders expressed the fact that they thought they would not have been able to test this funding mechanism with any other service provider, given the potential reputational risk. However, given ICRC's strong reputation, and the fact that they have 'everything to lose' should something go wrong, conversely, this reduced the reputational risk for outcome funders.

Credit score and due diligence: Munich Re undertook a due diligence review of ICRC in order to assess its risk profile. ICRC received an adequate credit score.

Financial and private sector expertise: The support of an ex-banker within the ICRC team also facilitated discussions with the private investors, as he knew how to work with investment bankers and non-traditional stakeholders.

Challenges

Firstly, one stakeholder commented that a challenge was that there was already a commitment to using the HIB and the PRP programme. Instead of matching programmes to the most appropriate financing mechanism and responding to donor requirements, and taking a 'responsive process of designing', the commitment to using the HIB and PRP was 'constructing it the wrong way round'. The stakeholder commented that it would have been better to identify if there were stakeholders interested in funding this type of funding mechanism and the PRP. Instead, it proved challenging to raise the target level of outcome funding, due to reservations with taking part in the untested HIB mechanism.

Secondly, the use of a HIB involved a significant shift, especially for outcome funders and service providers, and innovative thinking of how the HIB might fit within existing frameworks and systems:

- **Legal and taxation frameworks:** The different applicable legal and tax frameworks within the respective countries meant adaptations were needed to accommodate the HIB;
- **Internal buy-in:** There were concerns within some of the outcome funders and ICRC that the HIB was 'making money off the poor', and extensive discussions were needed to explain the purpose and rationale.
- **Skill set:** Some outcome funders noted that there was a lack of experience and expertise within their organisations in results based financing and development finance, which required a lot of learning 'on the job'.
- **Systems:** Systems within some of the outcome funders and ICRC were not set up to operate on a multi-annual budget, which was a challenge in terms of accounting and budgeting. Furthermore, ICRC rarely receives funding which is 'tightly' earmarked and generally does not operate projects which is directly financed by a specific donor. Accommodating the HIB required adaptation within the organisation.
- **Diverse donor requirements:** It was challenging and very time-consuming to find alignment between the requirements of the outcome funders.

Thirdly, it was a challenge to adapt the SIBs model to the humanitarian sector. There was tension between developing a 'pure' impact bond, and ensuring the HIB was adapted to the sector and needs of actors. One stakeholder commented that the development of the HIB took a long time because original models were 'textbook' impact bonds, which were not 'marketable':

- One outcome funder noted that a key internal justification for testing impact bonds was that it enabled risk transfer to the private sector. However, there were payments linked to milestones, and capital protection for investors, which reduced the risk transfer and meant the HIB was less 'pure'.

- It was challenging to adapt the SIB to the humanitarian world and ICRC's model of operation. ICRC was wary of investors having a say in the project, something that was a pillar of the SIB model. ICRC operates independently, and is unable to allow donors or investors to drive the selection and design of projects, or the implementation process. As such, the governance structures in place are intended to serve as a transparency mechanism and provide investors and outcome funders with information about the progress against targets, instead of as a mechanism to enable investors and outcome funder to influence delivery.

- One stakeholder also noted that ICRC led bilateral discussions, which meant the process was more efficient. However, other stakeholders noted that more collaborative discussions would have supported the development of a shared understanding of the impact bond. One outcome funder also noted that the deal was relatively finalised when they were reviewing it, and hence there was limited scope to influence the terms. A frustration noted was that for a period, outcome funders could not see the terms offered to other outcome funders and investors, and hence the outcome funder could not be certain that the terms offered were the same across the different actors.

Building on the challenges faced in designing and launching the ICRC HIB, stakeholders shared a number of lessons learned:

1 **HIBs should be developed to meet a specific need:** In the case of the ICRC HIB, it was first decided to use a HIB, and then the project was designed. Rather, the HIB should be considered if it enables service providers to access funding in a sector where outcome funders are interested in funding using an outcomes based approach. This will enable the matching of programmes to the right funding mechanism.

2 **It is important to test the legal feasibility** of operating a HIB at an early stage of the process, and identify potential taxation implications.

3 **Use of a financing structure or pooled funding** mechanism that enables investors and/or outcome funders to finance/fund an intermediary may reduce inefficiencies arising from the need to manage multiple investor and donor requirements.

4 **Investors want to be involved earlier,** so that they are still able to feed into the design of the terms and conditions of the impact bond.

5 **Outcome metrics also need to be designed to reflect data,** and returns to the investor and outcome funder should be aligned. Historic data is needed to model risk, for impact bonds to be 'investible'. Calculation of risk is crucial for putting a price tag on the investment.

6 **There needs to be flexibility** in terms of understanding of what an impact bond is. Not all components will be applicable to all contexts and organisations. Organisations take part in impact bonds for different reasons, and the impact bond needs to be adapted with this in mind. For this HIB to launch, it was necessary to reformulate the role of the investor and governance structures, and modify the impact bond structure to introduce non-private investors, capital protection and payments linked to milestones.

7 **There are trade-offs** between undertaking negotiations bilaterally or in a more collaborative approach. A more bilateral approach, with defined terms, can make the process more efficient, but result in a lack of a shared understanding of the objectives of the impact bond.

Advantages

The following were cited by stakeholders as advantages to using the HIB during the set up phase.

- **The HIB brought in additional private sector finance, which provided upfront capital to ICRC, which enabled it to participate in an outcomes based contract.**
  The HIB attracted financing from private sector investors, which enabled the outcome funders to pay on results. While ICRC is also involved in other results based payment contracts, the significant upfront capital required meant it would be unlikely to enter into the HIB model had there been no investors.

- **The HIB brought together existing ICRC partners, as well as new partners (La Caixa and private investors) around aligned interests.**
  Private investors are brought in 'closer to delivery' through participation in the operating review committee. One outcome funder said that an ambition was for investors to change their opinion of the risk of investing in conflict and humanitarian areas. The HIB also gave ICRC the experience of working with intermediaries and new actors, and going through the due diligence process. One stakeholder commented that this was an avenue for ICRC to build relationships with the private sector and show the private sector how it could get involved in philanthropy. On the other hand, another stakeholder thought the investors were there primarily to enable the outcome funder to pay only based on results, and that engagement with philanthropic arms of private sector actors was done through different avenues and contact points.

- **The HIB de-risks outcome funds and enabled the funding of the efficiency measures improvement testing component, to bring innovation to improving the efficiency of the PRP.**
  Outcome funders pay on results, reducing the risk of outcome funds not delivering results. One outcome funder noted that this was especially relevant given the capital investment required for the DCMS and efficiency improvement measures testing, and the risk that these measures do not translate into increased efficiency, and increased beneficiaries reached. The outcome based contract transfers the risk to investors, while at the same time incentivising these components of the programme to lead to real efficiencies. Given these factors, the outcome funder stated that it was preferable to fund this using an outcomes based contract, and that they would have been unlikely to fund the programme on an input basis. This also has wider implications, and benefits funding from other donors, which can be used for less risky activities.

- **The HIB brought in longer term funding for ICRC.**
  While the funding is more tightly earmarked than funds normally accepted by ICRC (down to the country and project level), the HIB funding is for five years, which provides more flexibility in terms of transferring funds between years, and more security in committing to longer term projects (such as the DCMS and EIM).

Additionally, going forward, the following advantages were expected:

- **The HIB requires and enables ICRC to look at data and explore how it can be used to bring more efficiency to the programme.**
  ICRC operates in a rather decentralised fashion, and looking at data across the PRP enables a better understanding of the drivers of efficiency, and facilitating comparison across centres. This is expected to be useful to support the improvement of efficiency in a systematic way.

- **There was difference in opinion of the role of the governance structures.**
  Some stakeholders thought that the requirement to be accountable to investors and donors, as well as the skills with the ORCM would drive efficiency. However, certain investors commented that their role on the ORCM was simply to obtain an update to ensure the investment was accurately valued in their accounts, and to monitor delivery. Other stakeholders commented that the role of the ORCM was not to influence ICRC's implementation and mode of delivery, as this would pose a danger to ICRC's independence.

- **The ability to test a new funding mechanism, and its applicability in the humanitarian sector.**
- **For outcome funders, the ability to test a more outcome focused way of funding, and to set target outcomes.**

Disadvantages

In terms of disadvantages of using the HIB, stakeholders cited that it was complex to design and expensive to set up. However, whether this poses a true disadvantage depends on whether the benefits outweigh the costs. Stakeholders commented that one should be careful with what we are comparing with. The HIB costs can be better put into perspective if we consider how much a change management project costs. Similarly, an outcome funder noted that a HIB 'externalised' certain costs which were hidden when delivered under a normal grant, for example costs of the outcome funder to launch a call for proposal, review bids and undertake feasibility studies to explore potential topics and themes.

The focus on the SER may introduce the risk of 'cherry picking' of beneficiaries or services provided, if staff feel pressurised to adapt the beneficiaries supported or services provided in order to meet the SER targets. However, there are key mitigations in place. ICRC's core approach is to deliver neutral, independent and impartial humanitarian action. For this reason, other stakeholders have no say in the way the project is implemented. Furthermore, the project is operating under ICRC's standard PRP procedures and ICRC has purposefully ensured that PRP centres and staff have nothing to gain by delivering a higher or lower SER. Furthermore, the SER relies on regained mobility, which incorporates an element of quality.

Other

There is mixed opinion about the extent to which the HIB led to a more careful and rigorous design of the intervention. There are three components of the design process, which was affected by the use of the HIB to varying degrees:

- **Selection of HIB centres and design of the PRP intervention was done using the standard PRP procedures.**
  Feasibility studies were done in potential centres. Normally, ICRC goes on to fund all centres deemed feasible. In this case, centres more suited to the constraints of an impact bond were selected to be funded by the HIB, and ICRC sought to fund the other centres through other funding. The PRP intervention will integrate the efficiency initiatives tested during the EIM testing phase.

- **Design of outcome targets and outcome metric involved a rigorous design process.**
  It involved the design of an outcome metric that drew on existing centre data, prevented perverse incentives and enabled comparison between PRP centres. The process also involved analysis of drivers of efficiency and analysis of the potential scale of improvements possible, which was used to develop a target outcome and return profile. The HIB provided the framework and incentives to systemise existing data management, so that it could be used for the design of the outcome targets and metric. In order to attract investors and outcome funders, ICRC was also required to present and justify these targets and metrics. One outcome funder commented that they thought ICRC was more 'business-like' and provided more detailed project reporting during the HIB process.

- **Design of the DCMS and efficiency improvement measures testing elements, which are key components of the HIB, is being undertaken during the first phase of the HIB.**
  The testing of the measures in the 8 centres before roll-out in the 3 new centres enables course correction and adaption. There is mixed opinion about the extent to which this can be attributable to the HIB. One stakeholder commented that the HIB finances these components, but that nothing is done differently in comparison to what would have been done if it were financed differently.

The ICRC HIB is the first HIB. It successfully launched in July 2017, and enables the financing of the development of three new PRP centres, and the testing of DCMS and efficiency measures. It is one of the few impact bonds that has brought in financing from commercial, private investors.

The focus of the HIB is on increasing the efficiency of the PRP, and the outcome metric is linked to increased efficiency compared to an established benchmark instead of outcomes achieved, though with increased efficiency, increased outcomes are also expected. The HIB aligns outcome funders, investors and ICRC incentives to improve efficiency.

The main challenges to developing the HIB was the difficulty with contracting due to the applicable legal and taxation frameworks in place in the countries of the outcome funders, the lack of expertise at the start of the project within ICRC and the outcome funders, and the difficulty of adapting the SIB model to the humanitarian sector and ICRC's operational model. Furthermore, some compromises on the terms have been necessary, which some outcome funders are uncomfortable with, for example, the element of capital protection.

The ICRC HIB was nonetheless able to launch due to the strong commitment of ICRC to testing the HIB, and the strong support of key outcome funders throughout the development. Additionally, the PRP had a large amount of historical data which was crucial for developing the outcome metric and target outcomes, and enabling the calculation of risk and return.

The next case study will be published following the next research wave, in the third quarter of 2020. The focus of the next research wave will be on progress in delivery of the HIB, and how the use of the HIB is affecting delivery.

Stakeholders Consulted

- ICRC
- Kois
- Munich Re
- Swiss Agency for Development and Cooperation
- UK Department for International Development