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## Guide to Reading the SROI Reports

The SROI Reports published by REDF are designed to provide the context for understanding the social return on investment for each REDF Portfolio social purpose enterprise. The following is a guide to understanding and analyzing the metrics included in the SROI Reports. The SROI Reports incorporate the SROI metrics, business data, and social impact data and provide analysis of these areas. Viewed as a whole, the SROI Report is similar to a for-profit stock report. It summarizes the performance of a social purpose enterprise so that investors, funders, and other interested parties can quickly assess its performance on business, social, and blended business and social bases.

In the same way that for-profit investors look to more than one indicator when assessing the performance of a corporation, philanthropic investors may now make funding decisions based on an intelligent mix of business, social impact, and socio-economic return measures. The SROI Reports also provide a way for practitioners to show the blended social and economic returns generated by funders' philanthropic investments.

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## SROI METRICS — FIGURE A

Each SROI report includes a table of SROI metrics (Figure A). The purpose of the SROI metrics is to show the monetizable return on an investment in a social purpose enterprise. In order to do this, one must understand how much was invested in the social purpose enterprise, how much monetizable value was created, and then one must compare the investment to the value created. This comparison is shown in the Index of Return (Index). The Index is calculated as follows:

$$\text{INDEX OF RETURN} = \frac{\text{VALUE CREATED IN THE FUTURE}}{\text{INVESTMENT TO DATE}}$$

Ideally, an investment should have an Index greater than one. An Index of one means that for each dollar invested, one dollar of value has been created. A higher Index of Return implies a more efficient use of the investment. For example, an Index of 40 would mean that for each dollar invested, \$40 of value is created. An Index of Return less than one does not necessarily imply a poor investment. It is possible that the enterprise creates other types of value that are not measured in the SROI metrics. The full SROI report provides context to help the investor determine whether or not this is the case.

The SROI metrics measure two types of value created by social purpose enterprises – Enterprise Value (the financial return from the business), and Social Purpose Value (the monetizable public cost savings and new taxes generated by individuals while employed by the social purpose enterprise). Looking at these values separately enables the investor to have a deeper understanding of the impact of the investment. The Blended Value is the total

monetizable value of the social purpose enterprise. REDF recognizes that social purpose enterprises create other types of value which are difficult to monetize, occur after the employee has left the enterprise, or accrue to family members of the employee. We affirm the validity of these other types of value and hope that the other sections of the report help to illustrate some of the additional value created.

### INVESTMENT TO DATE

This is the total value of all past and current investment in today's dollar.

### ENTERPRISE VALUE AND INDEX

The Enterprise Value is the total cash that the business is expected to generate in today's dollar, assuming that the business continues indefinitely. This benefit excludes social operating expenses and subsidies<sup>4</sup>. Enterprise ABC generates \$419,153 in Enterprise Value. Improving profitability, managing working capital more efficiently, and/or reducing capital expenditures can increase Enterprise Value.

The Enterprise Value is then compared to the total investment in the Social Purpose Enterprise of \$442,550 to calculate the Enterprise Index of Return. The resulting Enterprise Index is 0.95. In arithmetic terms Enterprise Index = Enterprise Value of \$419,153 ÷ Investment of \$442,550 = 0.95. This means that for each dollar invested in the enterprise, \$0.95 of financial value is created. In some cases (like Enterprise ABC) the Enterprise Index may be less than one. It is important to recognize that the Enterprise Value is only a portion of the value created by the social purpose enterprise. In some cases, creating a business environment appropriate to the target population may result in low

<sup>4</sup>Social operating expenses are the costs of providing extra supports and supervision to target employees. Subsidies are grants provided to the social purpose enterprises.

Figure A: Enterprise ABC SROI Metrics

1999		INDEX OF RETURN
Enterprise Value	\$419,153	00.95
Social Purpose Value	\$20,861,055	47.14
Blended Value	\$21,230,208	47.97
Investment to date	\$442,550	

financial returns. For example, some enterprises may provide crucial training for living wage jobs, but may not be of a scale to make the enterprise financially viable. The narrative of each report provides the context to judge whether this is the case.

#### SOCIAL PURPOSE VALUE AND INDEX

Social purpose enterprises provide a public benefit by enabling target employees to reduce their use of public benefits and services<sup>5</sup> and increase their contribution to income taxes. Social Purpose Value is a measure of net social benefit. It is the dollar amount (in today's dollar) of the public cost savings and increased tax revenue generated by individuals while they are employed at the social purpose enterprise, less the cost to support these individuals within the social purpose enterprise, assuming that the business continues indefinitely. Enterprise ABC will generate almost \$21 million in public savings and tax revenue (Figure A). Social Purpose Value can be improved by increasing the number of target employees served, increasing the public savings per employee, generating greater improvements in wages, or reducing the cost of supporting the target employees.

When the Social Purpose Value is compared to the total investment to date of \$442,550 in

the social purpose enterprise, a Social Purpose Index of 47.14 results. These means that for each dollar invested in the social purpose enterprise, there are public cost savings and increased tax revenues of \$47.14. In some cases, the social purpose index may be low, or even less than one. In these cases, it may have been beneficial for employees to increase their use of social services. For example, homeless individuals may be eligible for services they have not received. An increase in the use of services may be beneficial for this group, however, it will result in a lower Social Purpose Value and Social Purpose Index. Like the Enterprise Index, the Social Purpose Index only represents a fraction of the value created by the investment in the social purpose enterprise.

#### BLENDED VALUE AND INDEX

This is the total value generated by a social purpose enterprise over its lifetime. This is calculated as Enterprise Value + Social Purpose Value - Debt. Loans must be repaid to debt holders out of the value created; therefore the combined value must be reduced by this amount. Enterprise ABC has \$50,000 of debt (not shown). Therefore the Blended Value is \$21,230,208. When this value is compared to the Investment to Date of \$442,550, a Blended

<sup>5</sup>Public benefits and services include TANF, GA, SSI, food stamps, food banks, case management, community clinics, mental health treatment, housing services, emergency rooms, legal services, department of corrections, substance abuse treatment, and medical services.

Figure B: Enterprise ABC Employment Profile

Number of Target Employees	68
Percentage of Target Employees	80%
Hourly Wage Range	\$5.75-\$7.50

Index of 47.97 results. This means that for each dollar invested in the Social Purpose Enterprise, almost \$48 of monetizable value is created. In and of itself, the Blended Index is simply a ratio that measures how much an investment is “returning” above the investment that was put into it, assuming all past, present, and future investors receive their required rate of return. Making improvements to the Enterprise Value or Social Purpose Value, as described above can increase the Blended Value and Blended Index of Return.

A low Index of Return is not necessarily a poor investment. First, the value measured in SROI metrics is limited to changes in employees that occur during the social impact tracking period<sup>6</sup>. However, the value of the supported employment experience is not limited in this way. For example, if supported employment enables someone to obtain a living wage, significant value is created for that employee and his or her family beyond his or her tenure with the social purpose enterprise. Next, the SROI results should be understood within the context of the particular target population served. Supported employment will impact people with developmental disabilities differently than people struggling with drug addiction, therefore the resulting value that can be created will be different. Finally, SROI metrics are affected by the particular industry of the social purpose enterprise. For example,

manufacturing businesses are generally more capital intensive than service businesses. Therefore they require greater investment. The value created by the supported employment provided by a higher-capital business may not all show up in the SROI measures of value. Thus, it is critical to understand the SROI metrics in the greater context of the social purpose enterprise. The other sections of the SROI reports provide this context.

#### EMPLOYMENT PROFILE — FIGURE B

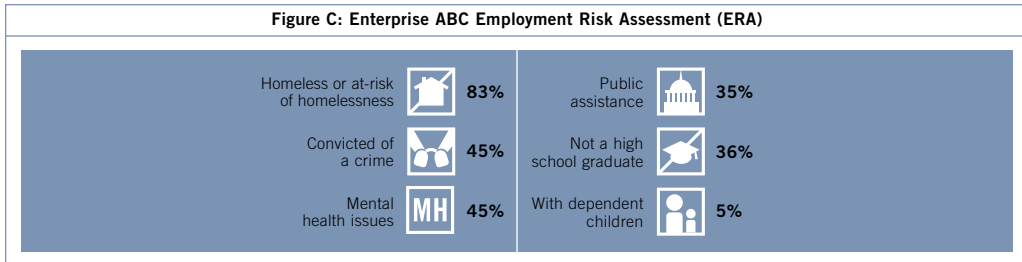
This section of the SROI Report gives a snapshot of the agency’s target employees. The metrics are relatively self-explanatory (Figure B). However, it is important to understand that social purpose enterprises are created to provide supportive employment for a particular population of people. Examples of target populations include people with psychiatric disabilities and homeless individuals. Due to the skill level of many target populations, it is usually necessary to supplement the work force with employees from outside the target population. The wage range described in this section reflects wages of target employees only.

#### EMPLOYMENT RISK ASSESSMENT (ERA) — FIGURE C

The ERA provides information regarding the employment risk profile of the enterprise’s

<sup>6</sup>In the 1999 SROI reports, most target employees were tracked for six to fourteen months. Ultimately, all target employees will be tracked for 24 months total.

Figure C: Enterprise ABC Employment Risk Assessment (ERA)



target employee population. It addresses the question, “What makes one employee more risky to hire than another?” For example, most people would agree that hiring a homeless individual is a riskier employment proposition than hiring an individual who has a stable housing situation. Similarly, hiring an individual with a history of mental illness is often considered riskier than hiring an individual who has not suffered from this disability.

The ERA provides important context for interpreting SROI metrics. Certain populations, such as homeless individuals, may increase their use of some social services as they improve their lives, resulting in a lower Social Purpose Value and Index. By looking at the ERA, an investor can see the challenges a social purpose enterprise takes on in employing its target population, and what types of issues it is helping its employees address. For example, we can see that 83% of Enterprise ABC’s employees were homeless before hire. Additionally, a significant number had been convicted of a crime, had not graduated from high school and had mental health issues. This provides a context in which to compare ABC to other social purpose enterprises employing individuals with barriers to employment. Furthermore, it enables the social investor

to quickly understand what population the enterprise is serving.

All ERA categories, many of which are listed in Figure C, represent the employees’ situation at the time they were hired by the social purpose enterprise. Some groups have customized ERAs, not defined below. ERA data was gathered during interviews at the time of hire.

#### HOMELESS OR AT-RISK OF HOMELESSNESS

This refers to the percentage of target employees who either lived in a temporary setting<sup>7</sup>, lived on the streets, used housing services in the 6 months before hire, or identified housing as a barrier to getting or keeping a job.

#### CONVICTED OF A CRIME

This value shows the percentage of target employees who have been convicted of a crime at any time prior to hire.

#### MENTAL HEALTH ISSUES

This refers to the percentage of target employees who have mental health issues as indicated by their answers to three different questions addressing mental health, use of mental health services, and mental or emotional health being a barrier to getting or keeping a job.

<sup>7</sup>Temporary settings include SRO hotel, transitional living facility, group home, institution (treatment facility, hospital, detention center, etc.), shelter, or sofa surfing.

Figure D: Enterprise ABC Social Purpose Results

SOCIAL PURPOSE RESULTS (PER TARGET EMPLOYEE)	1999
PUBLIC SAVINGS	\$15,644
NEW TAXES	\$1,815
WAGE IMPROVEMENT	\$12,097
FINANCIAL IMPROVEMENT	\$9,849

**PUBLIC ASSISTANCE**

Public Assistance reflects the percentage of target employees receiving Temporary Assistance to Needy Families (TANF), food stamps, General Assistance (GA), or Supplemental Security Insurance (SSI)<sup>8</sup>.

**NOT A HIGH SCHOOL GRADUATE**

This shows the percentage of target employees (who were above 18 years of age) who had not graduated from high school or received a GED equivalent.

**WITH DEPENDENT CHILDREN**

This value specifies the percentage of target employees who have dependent children.

**SOCIAL PURPOSE RESULTS — FIGURE D**

Social Purpose Results reflect the public savings and the benefits to the individual. These results are based on interviews with each of the target employees close to their time of hire and follow up interviews at 6-month intervals over the next 24 months.

**PUBLIC SAVINGS**

Public savings are calculated as the reduction in the use of TANF, GA, SSI, food stamps, food banks, case management, community clinics, mental health treatment, housing services, emergency rooms, legal services,

department of corrections, substance abuse treatment, and medical services. The figure listed is the average reduction for a target employee for a one-year period.

**NEW TAXES**

This value reflects the incremental increase in income taxes (assuming a 15% tax rate) that results from increased income from work per target employee over a one-year period.

**WAGE IMPROVEMENT**

This shows the average change in income per target employee for a one-year period.

**FINANCIAL IMPROVEMENT**

Financial Improvement measures how much better off an individual employee is while working for the social purpose enterprise by comparing the current after-tax earnings to the total income from welfare and work that the employee received at their time of hire. Financial Improvement is calculated: Current after-tax pay minus income from work and public assistance before working at the social purpose enterprise. It is important to recognize that employees may incur additional costs due to their new employment (i.e. transportation and childcare) that will have to come out of their financial gains. The larger the financial improvement, the more likely there is a net benefit for the target employee.

<sup>8</sup>Enterprises that primarily employ youth used household data to assess the use of public assistance, or used custom ERAs to assess the percentage of youth living in very low-income neighborhoods.

Figure E: Enterprise ABC Enterprise Financials

ENTERPRISE FINANCIALS	1998	1999	2000P
SALES	\$233,004	\$537,789	\$708,957
GROSS MARGIN	70%	69%	65%
NET MARGIN (BEFORE S&S) <sup>1</sup>	5%	-4%	-4%
NET MARGIN (AFTER S&S)	82%	10%	0%

## ENTERPRISE FINANCIALS — FIGURE E

### SALES

Sales represents money paid by customers in exchange for the goods or services provided by the social purpose enterprise. Sales do not include grants or subsidies. Historical, current and projected sales data are included to highlight the enterprise's progress.

### GROSS MARGIN

This is operating profit (sales minus the cost of goods sold) divided by sales. Gross margin is a good indicator of the profitability of the enterprises' core operations, aside from depreciation, overhead, and other expenses. A high gross margin suggests that the social purpose enterprise will have a better chance of being self-sustaining because it has more room to cover social operating expenses and overhead. For example, Enterprise ABC has a gross margin of 69% in 1999. This means that 69% of sales revenue can be used to support overhead expenses and the social mission.

### NET MARGIN BEFORE SUBSIDIES AND SOCIAL OPERATING EXPENSES (S&S)

This is a good indicator of the profitability of the enterprise, including both cost of goods sold and operating overhead expenses. This ratio is calculated before subsidies and social operating expenses are taken into account and

can be viewed as what the true business operating margin would be without a social mission. This is calculated:

$$\frac{\text{NET MARGIN BEFORE S\&S}}{\text{NET MARGIN BEFORE S\&S}} = \frac{\text{NET INCOME BEFORE S\&S}}{\text{SALES}}$$

### NET MARGIN AFTER SUBSIDIES AND SOCIAL OPERATING EXPENSES (S&S)

This margin shows the profitability with additional revenues in the form of subsidies and with the additional social operating expenses of operating an enterprise with a social mission.<sup>9</sup>

## SOCIAL PURPOSE ENTERPRISE INDICATORS — FIGURE F

These metrics demonstrate the social purpose enterprise's progress on its social mission over time (Figure F). In some cases, historical (1998 and 1999) as well as projected (2000P) data are shown to help the investor understand the progress and goals of the enterprise. Other values are projected as if the enterprise will operate indefinitely. These values are shown in today's dollar.

### TOTAL EMPLOYEES/TOTAL TARGET EMPLOYEES

This metric compares the total target employees to the total number of employees throughout the enterprise.

<sup>9</sup>Net margin after S&S can be higher or lower than Net Margin before S&S. If the subsidies are greater than the social operating expenses, it will be higher. If the reverse is true, it will be lower.

Figure F: Enterprise ABC Social Purpose Enterprise Indicators

SOCIAL PURPOSE ENTERPRISE INDICATORS	1998	1999	2000P
TOTAL EMPLOYEES / TOTAL TARGET EMPLOYEES	29/25	84/68	83/70
FTE EMPLOYEES / FTE TARGET EMPLOYEES	7.5/4.5	22.5/15	27/18
SOCIAL OPERATING EXPENSES PER TARGET EMPLOYEE	\$1,160	\$828	\$1,053
TOTAL PROJECTED INVESTMENT			\$566,177
TOTAL PROJECTED SOCIAL SAVINGS AND NEW TAXES			\$22,434,361
TOTAL PROJECTED SOCIAL OPERATING EXPENSES			\$1,573,306
TOTAL PROJECTED CONTRIBUTION TO PARENT			\$0

**FTE EMPLOYEES / FTE TARGET EMPLOYEES**

Full-time work is not appropriate for many of the target employees of social purpose enterprises, as they participate in other programs aimed at helping them improve their lives. This measure shows the full-time equivalent positions available within the social purpose enterprise.

**SOCIAL OPERATING EXPENSES PER TARGET EMPLOYEE**

This shows how much the enterprise spends on support for each target population employee including extra training and supervisory time (regardless of whether they are full or part-time positions). This is calculated as: Social Operating Expenses ÷ Number of Target Employees.

**TOTAL PROJECTED INVESTMENT**

This is the additional cash needed by the social purpose enterprise if all of its social and operating costs are not covered by sales. This value is projected forward (assuming that the business continues indefinitely) and is shown in today's dollar. This value is based on the current business plan and projections for the social purpose enterprise. It is possible that the environment could change or that unexpected opportunities could arise that will require additional investment in the future.

**TOTAL PROJECTED SOCIAL SAVINGS AND NEW TAXES**

This reflects the total projected value of the cost savings to society and the new income taxes in today's dollar.

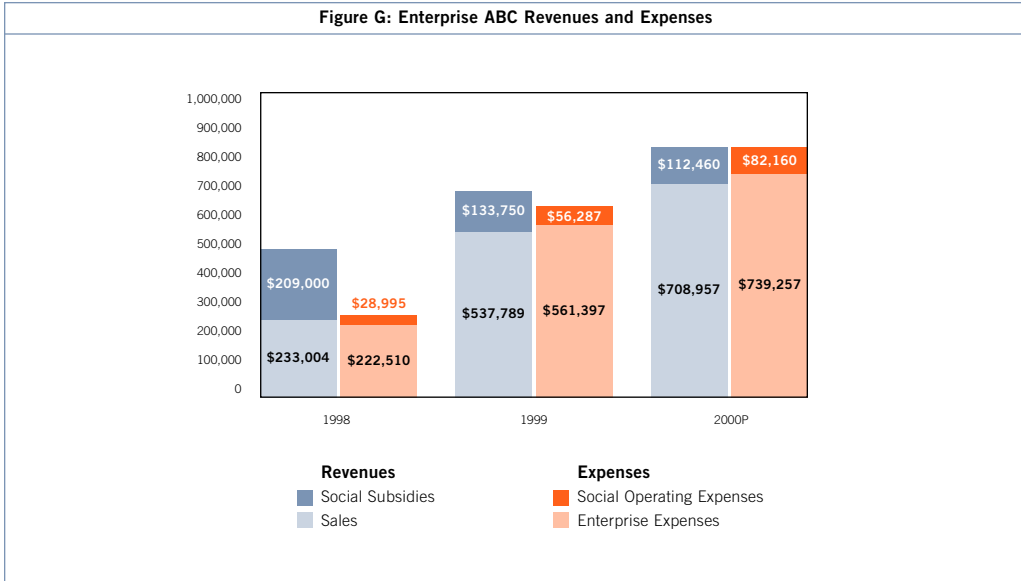
**TOTAL PROJECTED SOCIAL OPERATING EXPENSES**

This represents the total cost to provide supported employment over the enterprise's lifetime in today's dollar. A higher value could mean that the enterprise employs more people, or that its target population requires more support.

**TOTAL PROJECTED CONTRIBUTION TO PARENT**

When the enterprise's sales exceed all of its social and operating costs, the business can contribute the excess to its parent agency. This value is projected as if the business will continue indefinitely and is shown in today's dollar. A value greater than zero means that the business is expected to become financially self-sufficient at some point in the future. It is important to recognize that a value of zero does not imply that the social purpose enterprise is a bad investment. A particularly capital intensive business or an enterprise serving highly challenged employees may reasonably require ongoing subsidies to cover its enterprise

Figure G: Enterprise ABC Revenues and Expenses



or social costs. Also, a high value for contribution to parent does not imply that additional investment is not needed. It is possible that the enterprise will not be profitable enough to make that contribution to the parent for several years. The total projected investment listed in Figure F is necessary for the enterprise to reach its contribution goals.

**REVENUES AND EXPENSES — FIGURE G**

The bar chart in Figure G illustrates the relationship between the Enterprise Revenues and Expenses and Social Subsidies and Social Operating Expenses. Within each pair, the bar on the left shows revenues received and the bar on the right shows expenses incurred by the social purpose enterprise. Ideally revenues should exceed expenses. Each bar is divided into a top and bottom portion. The bottom of each bar is related to the enterprise (sales or

enterprise expenses), while the top reflects the social purpose (subsidies or social operating expenses). Social operating expenses are likely to increase as the business grows and more members of the target population are employed. Subsidies, on the other hand, should begin to decrease if the business is becoming more self-sufficient. However, if the business is expanding, additional subsidies may be needed to cover capital expenditures.

**Detailed information on the development of REDF's SROI metrics can be found in REDF's SROI Methodology paper. If you are interested in calculating these SROI metrics for your own organization, a user-friendly SROI Excel model can be downloaded from [www.redf.org](http://www.redf.org)**