

## Economics in policy-making 4

# Social CBA and SROI

Cost-benefit analysis (CBA) is the predominant tool used to assess whether a project or policy should be undertaken or not.

This briefing looks at how social considerations are incorporated into cost-benefit analysis, and describes the theory of Social Return on Investment (SROI) – a framework for incorporating ‘wellbeing’ impacts into such analyses.

### Why cost-benefit analysis?

Cost-benefit analysis (CBA) is the predominant tool used in welfare economics in order to assess whether an intervention – be it a project or policy – should be undertaken or not. The criterion for an intervention to be undertaken is that its’ benefits outweigh its’ costs.

In some countries, undertaking a cost-benefit analysis for appraising public projects is mandatory, (see for example the US Presidential Executive Order 12291, or [HMT guidance in the UK](#)).

The question, however, is what should be included and excluded in the costs and benefits that are analysed? Should we consider solely financial costs and benefits (simple monetary returns on investment)? Or, should we consider a wider array of costs and benefits – including those not reflected in the ‘market’ such as environmental and social effects?

Traditional cost-benefit analysis has tended to emphasise the economic costs and benefits. Because projects are often driven by the economic imperative to generate jobs and growth, social and environmental

costs and benefits are often treated as secondary considerations. This is despite the fact they are of central concern to individuals and communities.

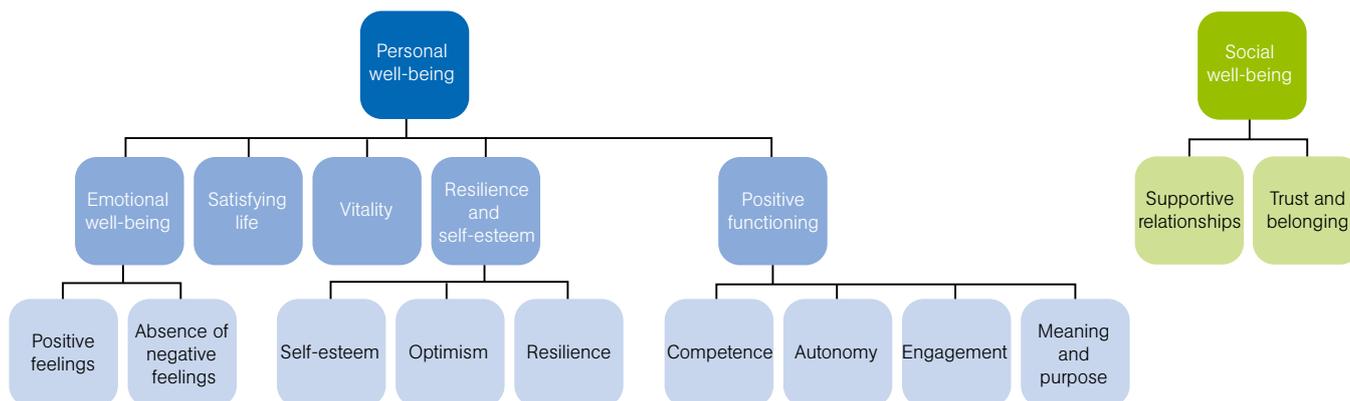
Progressively, alternative types of cost-benefit analysis have developed to complement the conventional method. These include social cost-benefit analysis (Social CBA) and social return on investment (SROI).

### Social CBA

Social cost-benefit analysis is an extension of economic cost-benefit analysis, adjusted to take into account the full spectrum of costs and benefits (including social and environmental effects) borne by society as a whole as a result of an intervention.

However, to compare like-for-like these different types of costs and benefits with economic costs and benefits, they must first be monetarily valued. Once all impacts are translated into the same metric, then the condition for a project or intervention to be undertaken is that the sum of economic, social and environmental benefits outweighs the sum of economic, social and environmental costs.

**Figure 1: Overview of personal and social wellbeing aspects included in nef's National Accounts of Well-being**



The process also entails measuring the indirect, knock-on costs and benefits of an intervention. There are three types of these so-called 'externalities':

- 1 knock-on impacts which are tangible and have a "market" value (e.g. the number of jobs that are indirectly created or destroyed)
- 2 knock-on impacts which are tangible but do not necessarily have a market value *per se* (see *Economics in Policy-making Briefing 3 - Valuing the environment in economic terms*)
- 3 knock on impacts which are neither tangible (in an economic sense) nor have a market value (for example well-being or social capital)

In practice social CBA has often focused on economically tangible knock-on costs and benefits while disregarding well-being perspectives in economics. This disregard has deep roots: in practice (if not in formally stated theory), conventional economics consider societal wealth (market value, economic maximization) as an end, rather than as a means for achieving well-being.

This economic 'truth' has been contested, notably by the Commission on the Measurement of Economic Performance and Social Progress presided by Nobel Laureates Amartya Sen and Joseph Stiglitz (See the **Further reading** box at the end of this briefing for full reference and access to the document).

### Moving a step further: SROI

Social return on investment (SROI) is an adjusted form of social cost-benefit analysis which moves further than conventional analyses. It is strongly grounded in direct stakeholder engagement, to ensure that what matters to the people affected by an intervention is counted and that their voice is recognised and reflected in decision-making. SROI is therefore intended to provide

a better evidence framework for how to achieve good lives and human well-being.

The method emphasises sustainability by taking a long-term view of outcomes and recognising that not doing so can lead to false economies. SROI recognises that economic, environmental and social outcomes are all critical factors in achieving good lives and well-being and should be included in a 'triple bottom-line' approach.

Various aspects of personal and social wellbeing are included and evaluated in SROI; and one way of capturing these elements is through tools such as well-being frameworks. Figure 1 above shows the framework of well-being outcomes, impacts and indicators used in nef's [National Accounts of Well-Being](#).

Taking a well-being perspective does not negate the importance of economic outcomes, but rather stresses their insufficiency for illustrating the positive and negative impacts of an intervention on society in a holistic manner.

A loss of employment, for example, can be expressed in simple monetary terms as a reduction in income and tax revenue. But it could also be expressed in terms of a loss of well-being loss – such as reduced self-esteem, optimism and personal or community resilience. Similarly, the existence of parks or other natural amenities can 'in fine' (ultimately) impact both social and personal well-being in various ways, for example by creating a greater feeling of community.

### Can we put a monetary tag on social aspects of life and well-being?

As mentioned before, both social CBA and SROI require social and environmental impacts to be translated into monetary terms in order to be compared like-for-like with economic impacts.

Putting a monetary tag on non-market goods may be challenging but it is important to recognise that market prices themselves are subjective, variable and inexact. For example, they are often a result of negotiating power rather than, as might be commonly expected, reflective of the real incurred costs.

The intention in SROI is to ensure that all material costs and benefits – economic, social and environmental – are assigned an approximate and evidence-based value. Not to do so is effectively to give outcomes like ‘strong communities’ or ‘self-confidence’, a value of zero in a key decision-making frameworks.

Nevertheless, difficulties of valuation are a key factor impeding the replacement of traditional appraisal and evaluation methods.

Whilst *Briefing 3* was dedicated to methodologies to valuing nature, here we focus on the valuation of social/well-being outcomes.

### **Instrumental vs. intrinsic value**

As in environmental valuation (see *Briefing 3*), well-being outcomes can be valued in two main ways.

First, one can look at the instrumental value of well-being – i.e. its potential to lead to other outcomes that are more easily monetised. For example, many aspects of subjective well-being are associated with reduced risks of heart disease. This effect can be monetised in terms of the reduced costs to the health service of treating heart disease. More directly, increased self-esteem is associated with greater likelihood of finding a new job – so the direct monetary benefits of this in terms of income can be added to an SROI.

But, of course, well-being is not just of instrumental value. People do not want to be happier just because it means they will find a job. It has intrinsic benefit too. This is harder to assess. ‘Willingness to pay’ approaches, used often for environmental valuation (see *Briefing 3*) are not appropriate – you can’t really ask someone how much they would be willing to pay to be happy. But what you can do is assess how much a similar improvement in well-being would cost on the market – a form of what economists call ‘revealed preference’.

So if a self-motivation course that increased self-esteem by one point on a 1 to 10 scale costs £1,000, then a project that increased self-esteem by two points could be valued at £2,000 per person.

Another approach is to use national data sets to see what increase in income is required to increase well-being the amount that is seen in the project being valued. This is best done using ‘panel’ data – i.e. looking at data from people who are interviewed in a survey year on year, and seeing how their well-being changes as their income changes. The problem with this method

is that it tends to lead to very large values – you need a large increase in income to increase well-being. As a result projects increasing well-being are often associated with very high valuations.

### **Benefit transfer**

In practice however, the two kinds of valuation approaches above are too time intensive and costly to implement. That’s why most analysts use ‘benefit transfer’ – which involves drawing values from other studies and applying them to the context in question. This means that “well-being values” used in many SROI analyses are scarcely – if ever – based on direct empirical research.

### **What are the implications of social valuation?**

Valuing social and well-being outcomes poses two main problems: one of a technical nature and another of an ethical/normative nature.

#### **Problem 1: lack of figures**

Social valuation studies are scarce. The lack of robust academic figures creates a problem when it comes to valuing well-being outcomes using “benefit transfer” technique. Similarly, the use of very different “proxy” (substitute) figures to “monetize” social outcomes means that the results of different SROIs are hardly comparable: choosing a high proxy figure can “inflate” or alternatively “underestimate” social benefits thus leading to over or under-claiming.

#### **Problem 2: ethical acceptability**

There is also an ethical question mark over whether we should try to express well-being impacts in market (monetary) terms in the first place. In doing so, we could risk merchandising well-being by creating the illusion that it can be substituted for money. (Remember, in the cost-benefit framework any well-being cost could potentially be outweighed by financial or economic benefits).

## Further reading and useful resources

The International Commission on the Measurement of Economic Performance and Social Progress  
[http://www.stiglitz-sen-fitoussi.fr/documents/rapport\\_anglais.pdf](http://www.stiglitz-sen-fitoussi.fr/documents/rapport_anglais.pdf)

*Seven principles for valuing what matters*  
[http://neweconomics.org/sites/neweconomics.org/files/Seven\\_principles\\_for\\_measuring\\_what\\_matters\\_1.pdf](http://neweconomics.org/sites/neweconomics.org/files/Seven_principles_for_measuring_what_matters_1.pdf)

National accounts of well-being  
<http://www.nationalaccountsofwellbeing.org/learn/download-report.html>

*A guide to social return on investment*  
[http://www.neweconomics.org/sites/neweconomics.org/files/A\\_guide\\_to\\_Social\\_Return\\_on\\_Investment\\_1.pdf](http://www.neweconomics.org/sites/neweconomics.org/files/A_guide_to_Social_Return_on_Investment_1.pdf)

**The Marine Socio-Economics Project (MSEP)** is a project funded by The Tubney Charitable Trust and coordinated by nef in partnership with the WWF, MCS, RSPB and The Wildlife Trusts.

The project aims to build socio-economic capacity and cooperation between NGOs and aid their engagement with all sectors using the marine environment.

## Economics in Policy-making briefings:

- 1 An overview of economics  
**Sagar Shah**
- 2 How economics is used in government decision-making  
**Susan Steed**
- 3 Valuing the environment in economic terms  
**Olivier Vardakoulias**
- 4 Social CBA and SROI  
**Olivier Vardakoulias**
- 5 Discounting and time preferences  
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- 6 Multi-criteria analysis  
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- 7 Beyond GDP: Valuing what matters and measuring natural capital  
**Saamah Abdallah**
- 8 Markets, market failure, and regulation  
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- 9a Finance and money: the basics  
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- 9b What's wrong with our financial system?  
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- 11 Behavioural economics – dispelling the myths  
**Susan Steed**

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