



UK SOCIAL INVESTMENT – OPPORTUNITIES, CHALLENGES, AND ‘CRITICAL QUESTIONS’

EVIDENCE PACK

November 2016

INTRODUCTION TO THE EVIDENCE PACK

This document has been prepared as part of a review of the social investment landscape in the UK. It contains a collection of perspectives and analyses, and has been developed in much the same spirit as Big Society Capital's earlier Social Investment Compendiums ([2013](#), [2014](#)).

The intention is to understand the opportunities, the challenges and the 'critical questions' facing social investment in future. As a result, this document differs slightly from the previous Compendiums in that the document more explicitly speculates on future developments.

This exercise is part of a broader strategic review that BSC has now started and will continue in 2017. This will inform our thinking on our strategic direction and future activities. We aim to use this broader view of the 'social investment' landscape to help us understand where to focus, through identifying where we can make the biggest difference and where we are most needed. We also hope it is useful as part of a broader conversation within social investment about how and where it can deliver the greatest impact.

This document should be read in conjunction with the document "***UK social investment – opportunities, challenges and 'critical questions'***" which can be found [on our strategy webpage](#)

DISCLAIMER

This document and accompanying note provides our view of the UK social investment landscape. We offer this as an invitation to comment, agree with or challenge the information and views contained in it, and welcome all views.

This document deliberately includes some material that may be found challenging to some – not everything will be ultimately agreed with (or right!), but we thought it's time to put some real questions on the table to get some views about what's really happening in social investment.

This document is intended to focus on social investment, not on BSC. The scope has not been much broader than social investment, for instance we have not considered macroeconomic trends in detail.

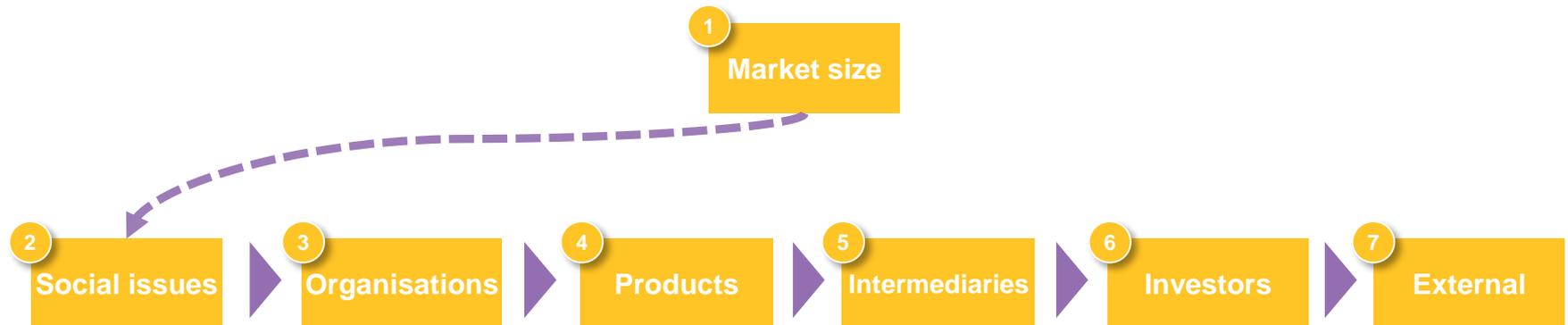
Big Society Capital has developed this document from publicly available sources and our own efforts. This is not meant to be a 100% precise description of the state of social investment nor necessarily a statement of Big Society Capital's views on social investment. This document is not reflective of particular interests of BSC.

Please do send us any corrections or any suggested changes to more accurately reflect the state of the market if you think appropriate.

SOCIAL INVESTMENT TODAY CAN BE CONSIDERED ACROSS SEVERAL KEY PARTS

This section investigates the state of social investment today.

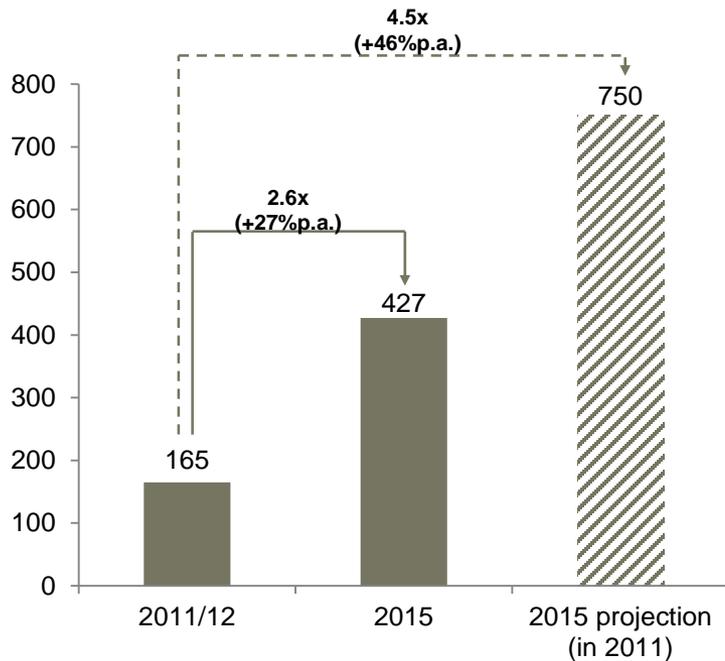
It reviews the market size and then details the state of social investment through examining different components of the market (components described below).



THE SOCIAL INVESTMENT MARKET HAS GROWN WELL BUT REMAINS SMALL VERSUS OVERALL IMPACT MARKET

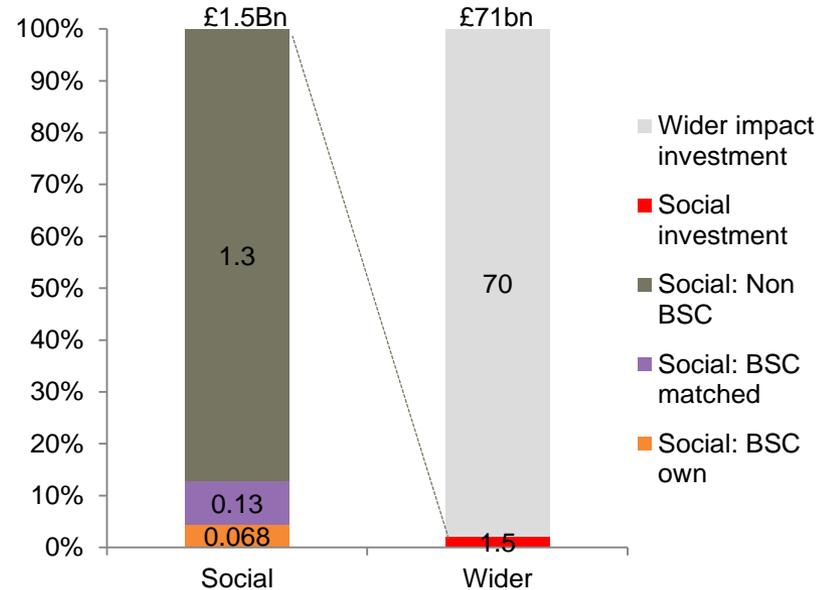
Yearly amount of total social investment made in the UK grew 2.6x since 2011 to £427m in 2015, but fell below initial projections

Flow: Yearly amount of total social investment made (UK, by year, £m)



Social investment market size estimated at £1.5Bn, of which 13% BSC related; Wider impact market estimated at £71Bn

Stock: Total amount of social investment outstanding (UK, 2015, £Bn)



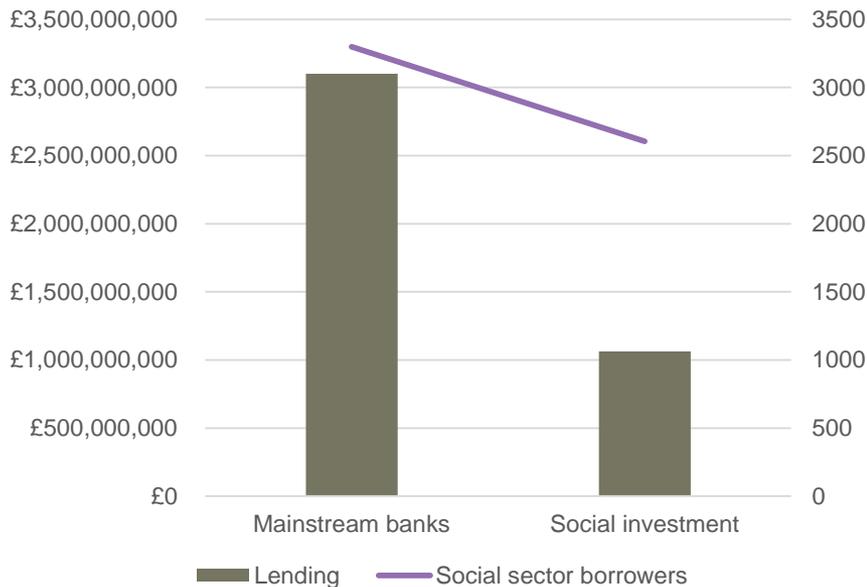
Note: Wider impact investment is predominantly Housing Association debt, some bank lending to charities, and ethical/sustainable bond funds

SIZE OF SOCIAL INVESTMENT IS NOW SIGNIFICANT COMPARED TO LENDING FROM MAINSTREAM BANKS

Mainstream bank lending estimated at £3.1bn to charities and social enterprises, though to mainly larger organisations for secured lending...

... however pricing in social investment appears more competitive than mainstream

Mainstream vs social investment



Note: This analysis excludes social investment in profit-with-purpose organisations

Product	Social investment interest rate (APR) ⁽²⁾	Comparable SME rates ⁽¹⁾
Sub £150k unsecured (incl. Access)	6.5 – 12%	<ul style="list-style-type: none"> • CDFI micro & SME loans (average £29k): 13% • Funding Circle high risk loans: 11 – 18% • Growth loans + £500k: 8 – 15% (per British Business Bank analysis)
£150k+ unsecured	7 – 12%	
Sub £500k secured	2.5% over base to 6.5% managed	<ul style="list-style-type: none"> • Commercial mortgage best buys per Moneyfacts website: 1 – 6% margin over base • Increasing competition from banks for larger loans is reducing margins for social banks
£500k+ secured	Base rate + 2 – 4%	
SITR	1.5% - 7%	Based on a small number of deals so far

Source: The Forest for the Trees: UK Banks Investment in Social Investment, Flip Finance (2016), The Size and Composition of Social Investment in the UK, BSC (2016)

(1) Source: Responsible Finance Survey 2015, Funding Circle website, BBB Growth Loans Report 2015
 (2) Source: Access ranges; BSC unsecured loan fund pricing ranges, BSC investee business plans and latest lending data

THERE IS CONSENSUS FROM COMMENTATORS ON MANY OF THE CURRENT AND EMERGING SOCIAL CHALLENGES

2

The population of the UK is **ageing** with complex knock-on effects...

- By 2037 there will be 2.74 working age adults for every pensioner, compared to 3.21 in 2012
- By 2035 over 24% of the population will be aged 65 and over, up from 18% in 2015.
- The related issues are myriad: significant increase on isolation and loneliness; number of dementia sufferers could rise by over 100%, in the next thirty years
- Costs of dealing with these circumstances will leave huge shortfall in current budgets

The **poor are getting poorer**... and inequality has consequences

- Rising cost of living means many households will be unable to afford to heat their homes adequately over the next few years, resulting in “heat versus eat”; poor families hit hardest
- 37% of children who receive free schools meals achieve five A – C’s at GCSE compared to 64% of children that do not receive them
- The nature of work is changing with zero hours contracts and micro jobs. 10% of the labour force are underemployed and want to work more hours.

The UK’s **population is growing** quickly – and this is set to continue...

- The UK population is projected to increase by 9.7 million over the next 25 years, from an estimated 64.6 million in mid-2014 to 74.3 million in mid-2039 (subject to future changes to immigration policy)
- While a larger population increases the size and productive capacity of the workforce, it also increases demand for education, healthcare, and housing
- Rising costs of adult social care and children’s services may strain council budgets

Housing remains an important issue...

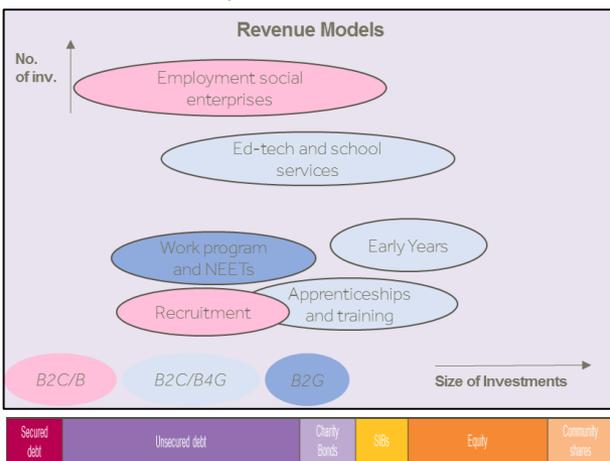
- Number of households placed in temporary accommodation has risen by a quarter to 64,000 in 2015
- ‘Generation rent’ is increasing due to the shortage of affordable housing
- Potentially an increased focus on the role of the housing market in tackling poverty: a secure, affordable home is the first step on the route out of poverty

Lifestyle factors, particularly for the most disadvantaged, predicted to lead to **significant health issues**...

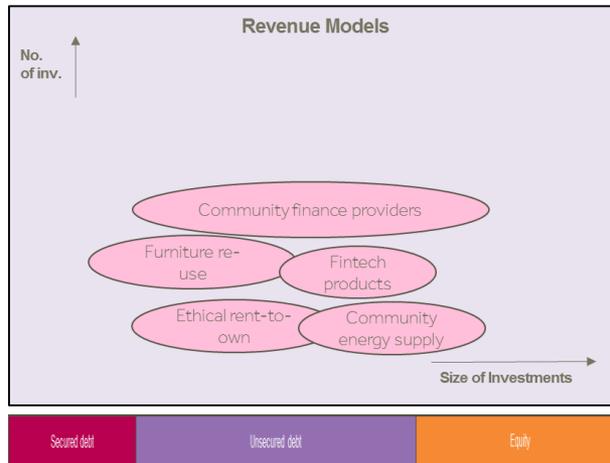
- Recent forecasts on childhood obesity suggest that a quarter of boys and girls could be obese by 2050
- Standards of health are unlikely to reach pre-recession levels in the short to medium term, as many of the worst-off households will not be able to afford to improve their nutrition
- One million people over 65 years old are malnourished or at risk

SOCIAL INVESTMENT IS SUPPORTING A RANGE OF REVENUE MODELS ACROSS SOCIAL ISSUE AREAS...

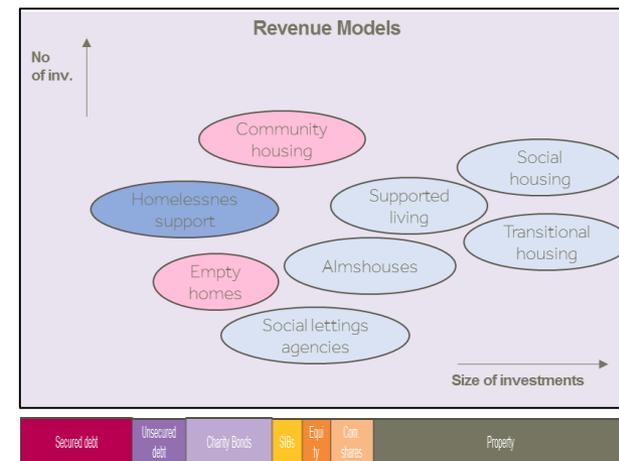
EMPLOYMENT, TRAINING & EDUCATION



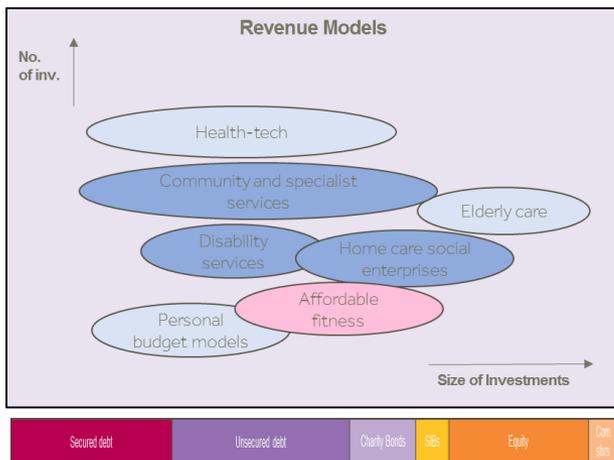
FINANCIAL INCLUSION



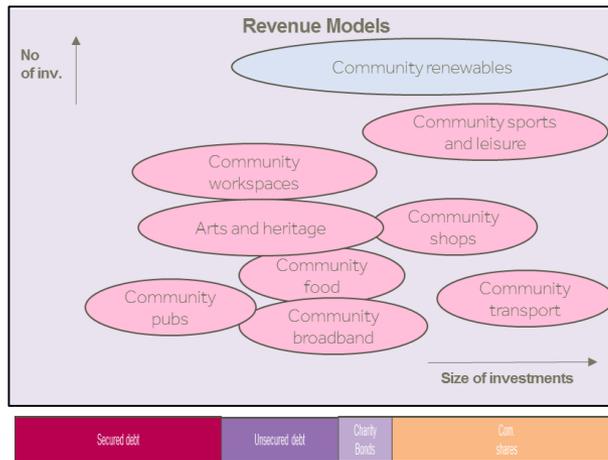
HOUSING



HEALTH & SOCIAL CARE



COMMUNITY, ARTS, SPORTS & HERITAGE



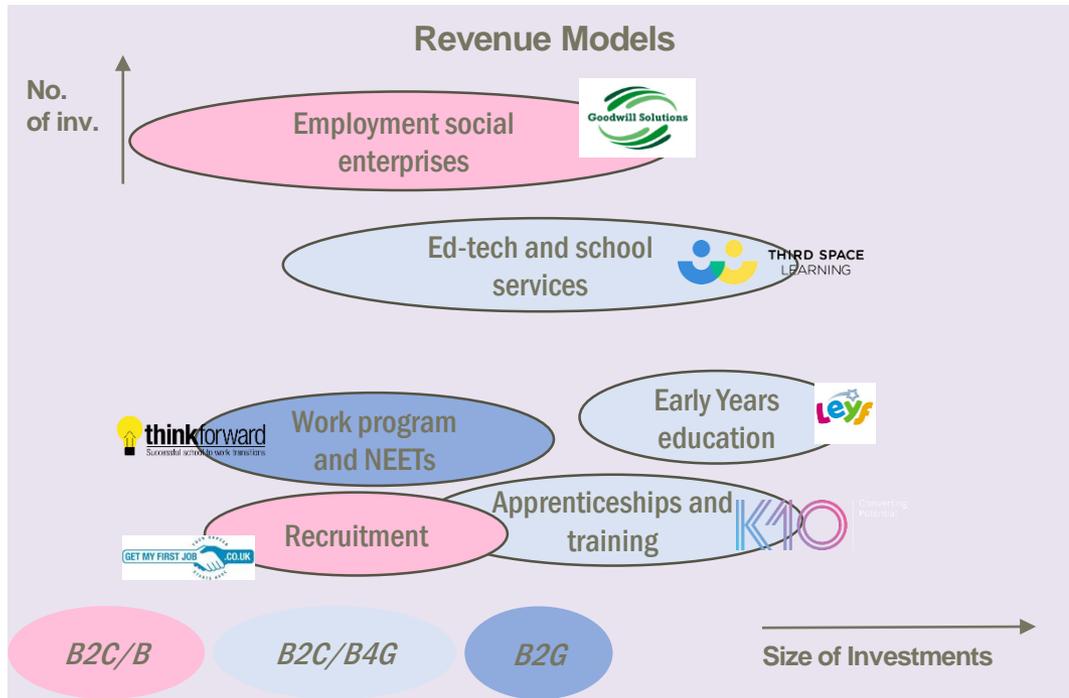
Key Lessons:

- B2G: Few revenue sources direct from Govt e.g. outcome based commissioning
- B2C/B4G: Many opportunities in revenue sources from Govt but decided by others
- B2C/B: A number of consumer markets but highly competitive

EMPLOYMENT, TRAINING AND EDUCATION...



Significant differences remain in the educational attainment and employment prospects of people from disadvantaged backgrounds. These differences cement social immobility and long term inequality.



BSC Investments (end 2015)
90 investments of £38.7m

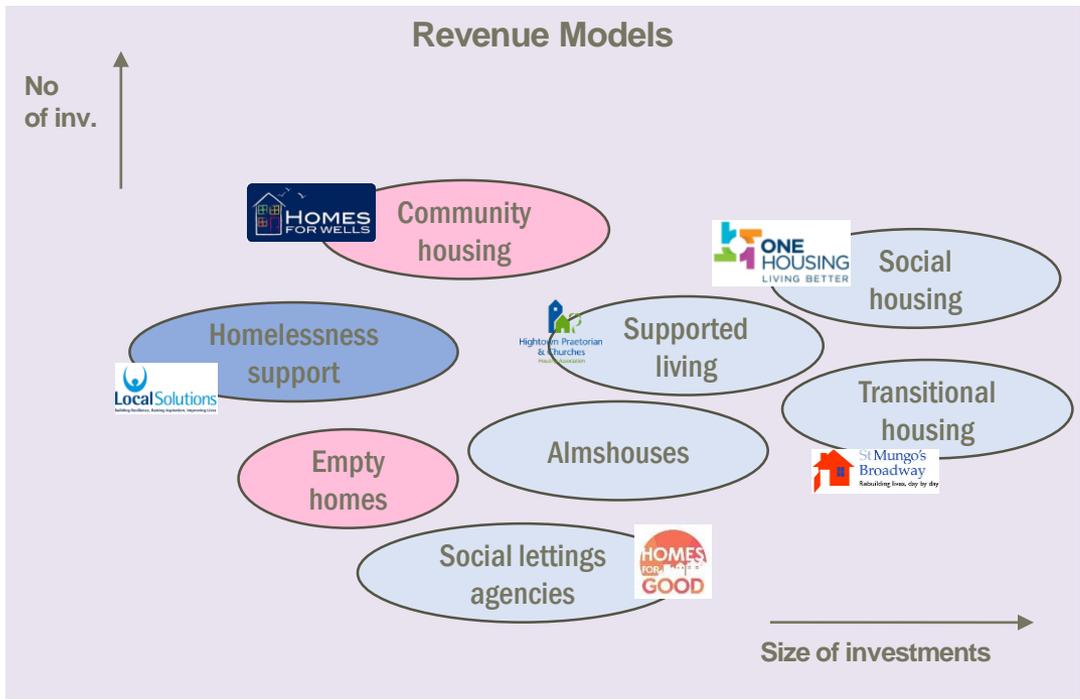
Active Fund Managers

- Themes**
- Employment socent and ed-tech dominate
 - Some Early Years investments with growth expected through increase in free childcare hours.
 - Less investment in commissioned services
 - Stresses in apprentice models from policy changes.

HOUSING...



The UK is in the midst of a housing crisis, especially for less well-off families and people with additional support needs. Poor housing can then have a knock-on effect on many other aspects of people's lives.



BSC Investments (end 2015)

45 investments of £99.5m

Active Fund Managers

resonance

Cheyne Capital

RETAIL CHARITY BONDS

SALAMANCA Group

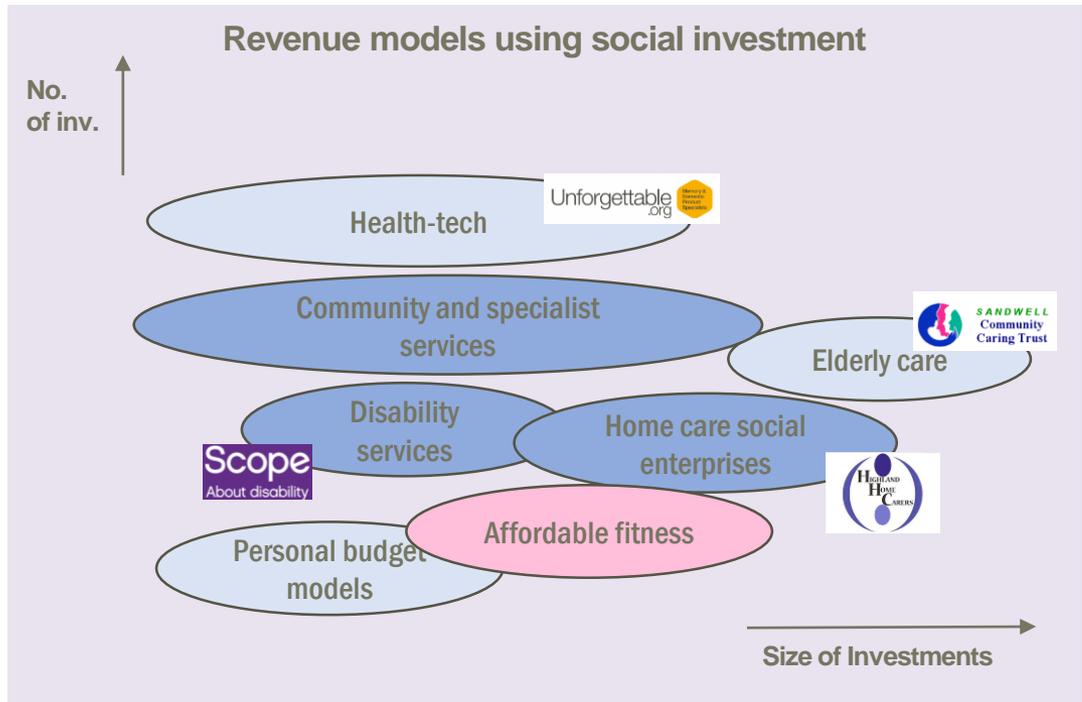
Charitybank

- Themes**
- Emerging off-balance sheet alternatives for HA's
 - Significant demand for development capital & skills into higher impact models
 - Pickup in CLT projects, often w community shares
 - Future challenges from supported living changes

HEALTH AND SOCIAL CARE...



The health and social care system in the UK is under severe strain with increasing demand from an ageing population, more people living with long term conditions and an increase in social isolation.



BSC Investments (end 2015)

40 investments of £25.8m

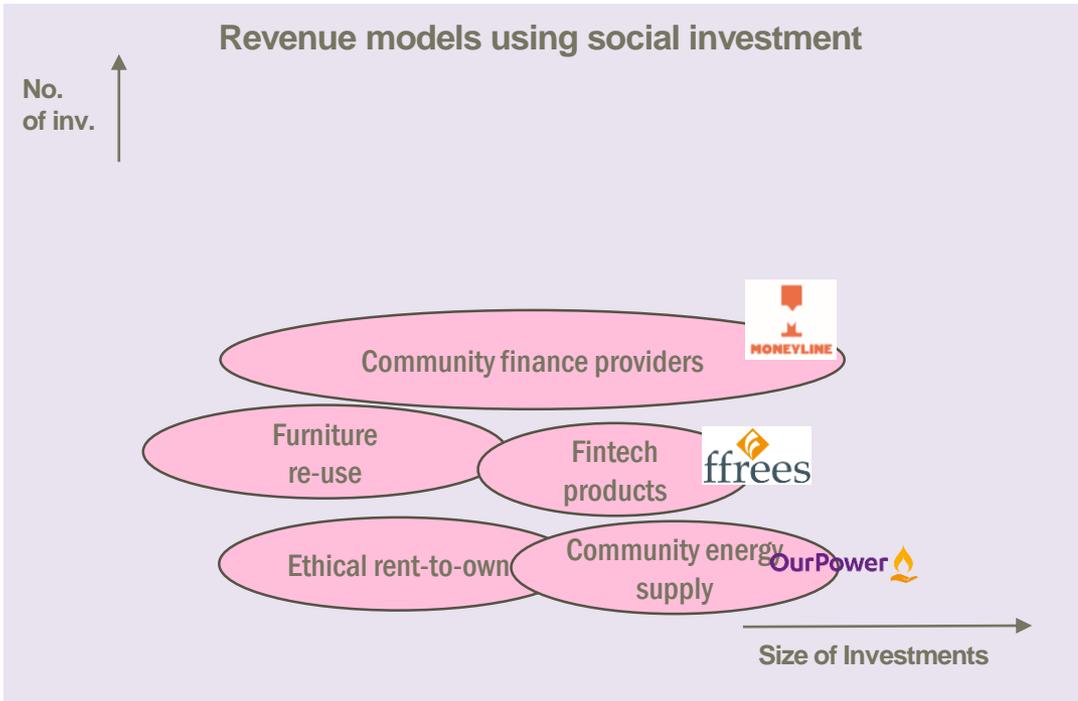
Active Fund Managers

- Themes**
- Less social investment being used than expected
 - Health-tech inv's thru angels & venture funds
 - Some unsec. loan demand from comm. health orgs
 - Impact focus tends to be broader than BSC target
 - Larger spin-outs accessing commercial secured debt

FINANCIAL INCLUSION...



Four million low-income households have poor access to mainstream financial services and two million adults don't have a bank account. Financial exclusion is a major contributor to the poverty premium.



BSC Investments (end 2015)

10 investments of £12.1m

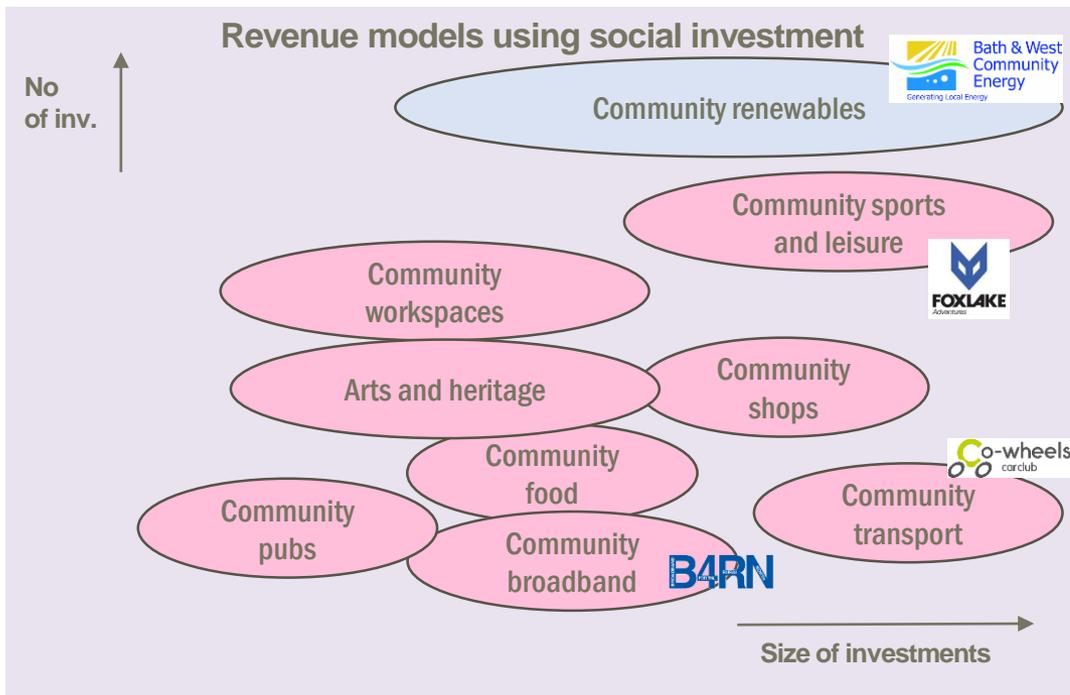
Active Fund Managers

- Themes
- Community finance providers mkt share still tiny and vulnerable to EU support disappearing
 - Many models shifting from history of grant support
 - Fintech models emerging, though often impact-light
 - Furniture re-use orgs using loans to expand
 - Poverty Premium fund aims to catalyse new models

...AND COMMUNITIES, ARTS, SPORTS & HERITAGE



Local people are best placed to develop solutions to local problems. Arts, heritage, sports and faith can improve health and wellbeing and strengthen community links.



BSC Investments (end 2015)

66 investments of £35.1m

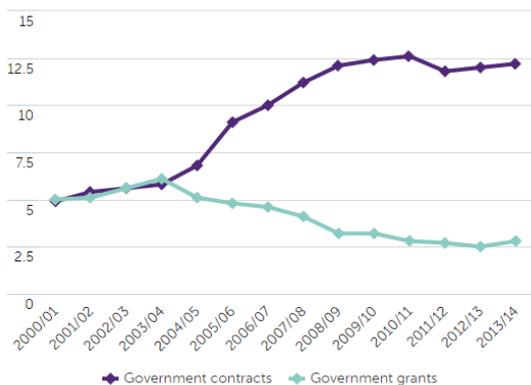
Active Fund Managers

- Themes
- Significant activity with over 300 comm. share issues
 - Renewable models the biggest, but policy shifting
 - Benefits of local solutions to local problems, but investment timetables often long and challenging
 - Power to Change role significant going forward

PUBLIC SECTOR CONTRACTS ARE A LARGE PORTION OF SECTOR REVENUES, THOUGH A CHALLENGING ENVIRONMENT FOR MANY

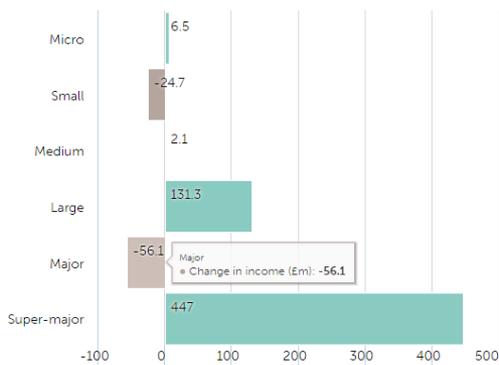
Govt now five times more likely to provide contracts than grants...

Income from government contracts and grants, 2000/01 to 2013/14 (£bn, 2013/14 prices)



... whilst overall Govt funding is stabilising, the largest charities are the main beneficiaries

Change in government income by income band, 2012/13 to 2013/14 (£m, 2013/14 prices)



Even though there are some bright spots, significant barriers remain to increasing participation of social sector in Govt services

Culture

- Govt commissioners and procurement traditionally risk averse
- Limited commissioner capacity
- Social Value Act not seen transformational change

Programme design

- MOJ Transforming Rehabilitation Programme required company guarantees, which are prohibitively expensive
- Work and Health Programme looks unlikely to make it easier for social sector

Dispersed commissioners

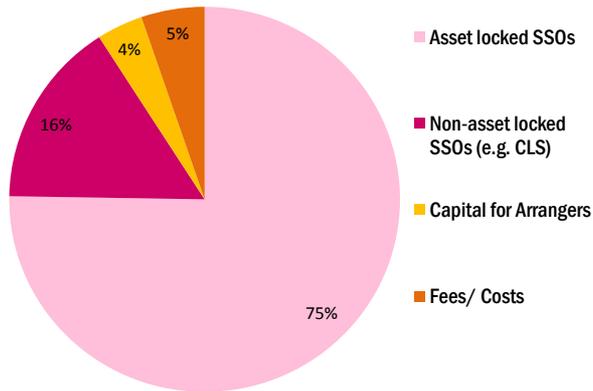
- Local Authorities are increasing commissioners of social services, but highly dispersed
- Diverse body of Local Authority commissioners are somewhat fragmented
- Reduced local authority commissioner funding

IN PRACTICE, FOCUS ON THE 'MOST DISADVANTAGED' BUT COULD EMPHASISE OTHER IMPACTS TOO



SOCIAL SECTOR STILL DOMINATES BSC AND BROADER INVESTMENTS BUT OTHER FORMS ALSO PRESENT

75% of drawdown so far has gone to asset locked organisations, with a minority to non-asset-locked



Source: BSC internal data, 2016

But BSC has also supported a number of intermediaries who invest outside the traditional regulated social sector:

Impact Ventures UK



70% of social investment market fits within broad BSC definition of social sector

Table 1. UK Social investment (segment A) – outstanding value £m and # organisations benefiting end 2015⁷

Segment		£m	% total value	# investments	Description
A1. SOCIAL INVESTMENT - BIG SOCIETY CAPITAL FOCUS – of which		1,062	70%	2,656	
SME CHARITY FINANCE (40%)	Social bank lending	545	36%	1,264	Loans (normally with security) from UK Social Banks to charities and social enterprises
	Non-bank lending	158	11%	858	Non-bank lending via specialist funds and other channels to charities and social enterprises
SOCIAL INNOVATION (3%)	Equity-like capital	32	2%	123	Capital for growth via specialist funds and other charities to charities and social enterprises
	Social Impact Bonds	14	1%	18	All Social Impact Bonds
PARTICIPATION (6%)	Community shares	98	6%	353	Community shares, mostly issued by community benefit companies
	Social investment tax relief	1	0.1%	9	Social Investment Tax Relief enabled investments
SCALE (14%)	Charity Bonds	88	6%	18	Bonds issued by registered charities targeting social impact and with explicit impact measurement
	High impact social property	130	9%	14	Capital for service delivery by charities and social enterprises involving property
A2. SOCIAL INVESTMENT - PROFIT WITH PURPOSE		462	30%	807	All types of investment in profit-with-purpose companies
A. SOCIAL INVESTMENT – TOTAL		1,525	100%	3,463	

These results show that the part of social investment emphasised by the four strands of Big Society Capital's current strategy (segment A1) covers over two-thirds (70%) of the overall value of social

Source: The size and composition of the social investment market. BSC, 2016

QUALITATIVE EVIDENCE OF INTEREST AND DEMAND FROM THE SOCIAL SECTOR

3

Organisations

In our market championing work, we've seen increased levels of interest and engagement over recent years – although this may take time to translate into demand:

- ▶ Those that have used social investment are **positive about the difference it's made** in terms of impact delivered – and our experience suggests many are likely to seek further investment, and to advocate to peers, albeit also keen to share their learnings around challenges.
- ▶ End-users of social investment appear **keen to play a role in shaping its future** including by supporting market championing projects (e.g. Family Action, P3, Preston Road Women's Centre) and/or influence public sector commissioning utilising social investment (e.g. Catch22, CLARE CIC in Belfast)
- ▶ Many organisations that have used social investment talk of it **supporting new ways of working** that can strengthened their organisations (e.g. St Mungo's, CASA Homeless Link supporting their members to consider social investment)
- ▶ Evidence of **tangible progress** going through different funds at different stages of investment (e.g. Oomph going from Big Venture Challenge to NESTA, and St Mungo's Real Lettings to National Homelessness Property Fund)
- ▶ SITR has **opened up social investment** to social sector organisations that may not have seen themselves as relevant for investment a few years ago (e.g. Portsoy Community Enterprise in Scotland, Fareshare SW)
- ▶ Increased level of engagement, understanding & interest in social investment at sector events
- ▶ Now see charities looking for **social investment experience when recruiting new Board members**, and in considering their strategy

The logo for Catch 22, featuring the word "catch" in a lowercase, sans-serif font above the number "22" in a large, bold, black font.The logo for CLARE, featuring a stylized "C" made of colorful segments (red, yellow, green, blue) to the left of the word "CLARE" in a bold, red, sans-serif font. Below "CLARE" is the tagline "Creative Local Action, Responses & Engagement" in a smaller, black font.The logo for St Mungo's, featuring the text "St Mungo's" in a bold, orange, sans-serif font. Below it is the tagline "Ending homelessness Rebuilding lives" in a smaller, black font.The logo for Oomph!, featuring the word "Oomph!" in a white, bold, sans-serif font with a blue exclamation mark, set against a solid blue square background.

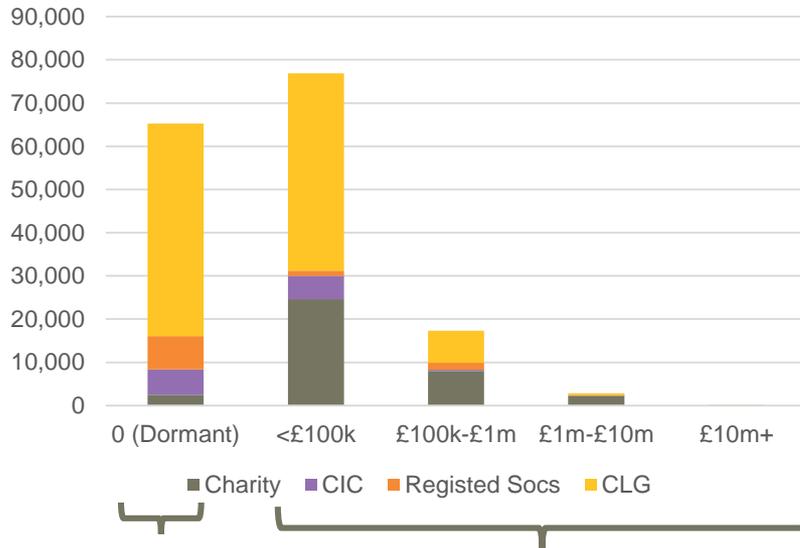
THE INVESTIBLE UNIVERSE FOR REGULATED SOCIAL ORGANISATIONS MAY HAVE AN UPPER LIMIT

Whilst the overall number of reg. social sector orgs may seem large, with over 260,000 and 100,000 incorporated ...

... it may be that there is an upper limit of number of investees in the low tens of thousands (c. 2.5-4.5 x current size)

*includes both potential investees through banks and social investment, indicative market sizing

Regulated SSOs (by number)

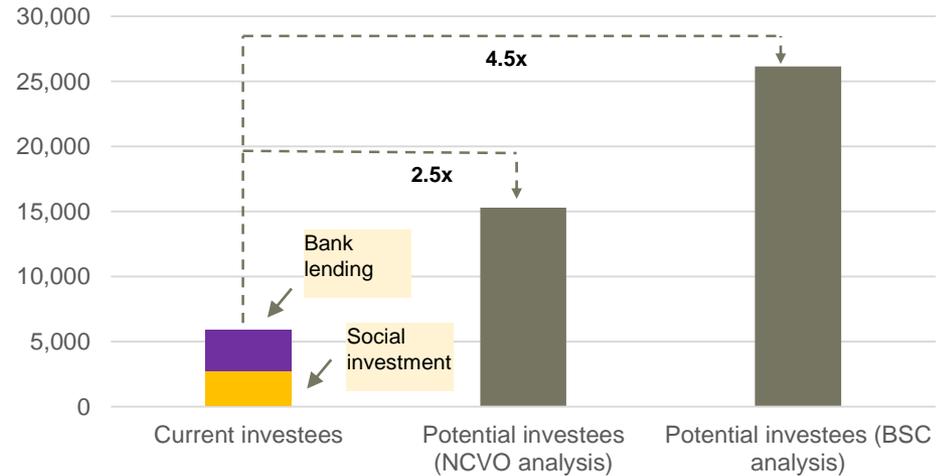


Not operating Incorporated, non-dormant organisations

Note: This includes social companies limited by guarantee, previously not included in definition of regulated social sector, as data was not available and there is no specific social regulator. They were calculated for the NCVO report

Source: NCVO, Understanding the capacity and need to take on investment within the social sector, 2016, Companies House dataset

No. of investible organisations



**Conservative assumption that investees from social investment not same as bank lending

NB: Demand for finance is dependent on the scale of capital need as well as the number of organisations

Note:

- NCVO analysis: Calculated with reference to tangible assets
- BSC analysis: Calculated with reference to incorporated organisations with revenue >£100k

Sources: Size and composition of social investment market, BSC, 2016
The Forest for the Trees, FlipFinance, 2016

WITHIN 'REG. SOCIAL SECTOR', ALREADY FEW MORE ORG TYPES THAT COULD HAVE MORE SOCIAL INVESTMENT FOCUS

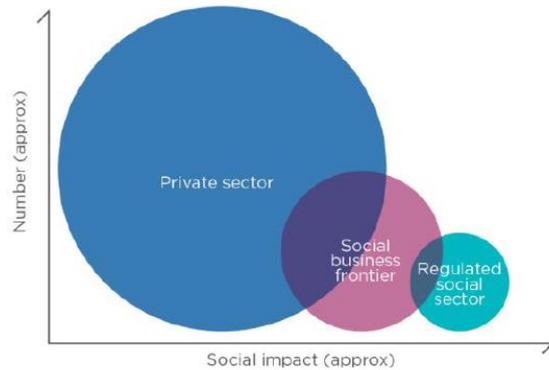
Economic interests based	Employee-related	<ul style="list-style-type: none"> Worker/Employee owned co-operative 	<div style="background-color: #FFD700; padding: 10px; text-align: center;"> Potential greater focus? </div>	 
	Consumer-related	<ul style="list-style-type: none"> Consumer co-operative Buying group 		 
	Producer-related	<ul style="list-style-type: none"> Co-operative consortium (service or marketing co-operative) 		 
Sector based (particularly basic needs)	Food & agriculture	<ul style="list-style-type: none"> Agricultural co-operative Community Supported Agriculture (CSA) 		    
	Finance	<ul style="list-style-type: none"> Credit union Community Development Finance Institution (CDFI) Community finance society 		
	Housing	<ul style="list-style-type: none"> Housing co-operative Tenants and residents association 		
	Energy	<ul style="list-style-type: none"> Community energy projects 		
	Health & social care	<ul style="list-style-type: none"> Health and social care co-operatives 		
Place and community based	Local community (geographical)	<ul style="list-style-type: none"> Community co-operative Community business or enterprise Development trust 		<div style="background-color: #FF8C00; padding: 5px; text-align: center;"> BSC engages with most so far </div>  
	Interests based community	<ul style="list-style-type: none"> Club Leisure & Cultural Trust Supporters' trust 		

PROFIT-WITH-PURPOSE STILL EMERGING FORM – MAY BE LARGE, BUT INVESTMENT NEED STILL UNCLEAR

3

Organisations

The mission-led business market may be of significant size



- Estimates using the BIS Small Business Survey suggest that there may be ~100,000 social businesses delivering social impact outside the regulated social sector
- However, we estimate that c. 80% may have revenues less than £100,000, and therefore the total number of organisations may be similar to the estimates of investible organisations in the regulated social sector (~20-30k; slide 18)

Strong emerging interest and energy in profit with purpose movement...



- >~100 B Corps now registered in UK
- Appealing to smaller companies, however some interest from multinationals e.g. Unilever

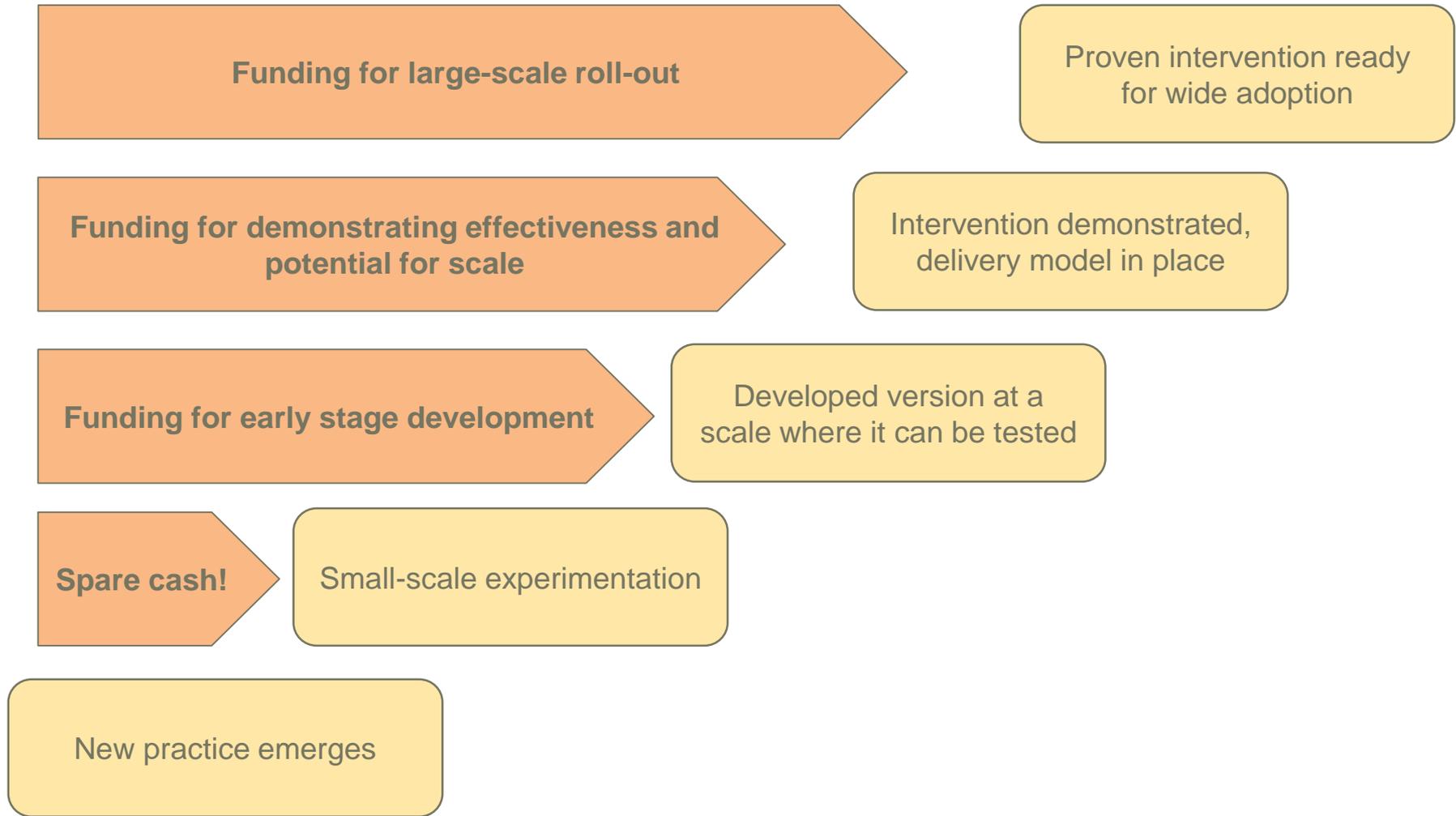


- Social investment team mission-led business review
- New PM reportedly encouraging 'responsible business'

... however still many unknowns

- Social impact delivered by profit-with-purpose hard to define
- Investment requirements hard to define as yet, though presuming greater growth capital
- Evidence of market failure of investment hard to find as yet: might mainstream finance provide all that is needed?

DIFFERENT FUNDING IS NEEDED AT EACH STAGE OF DEVELOPING A NEW SOLUTION FOR A SOCIAL PROBLEM



BSC EXISTING COMMITMENTS HAVE TARGETED INCREASING PRODUCT DIVERSITY...

BSC committed investments



 BSC significant role in establishing/expanding

Social Investment Market (outstanding investments)



No. of orgs

1264

858

18

18

123

353

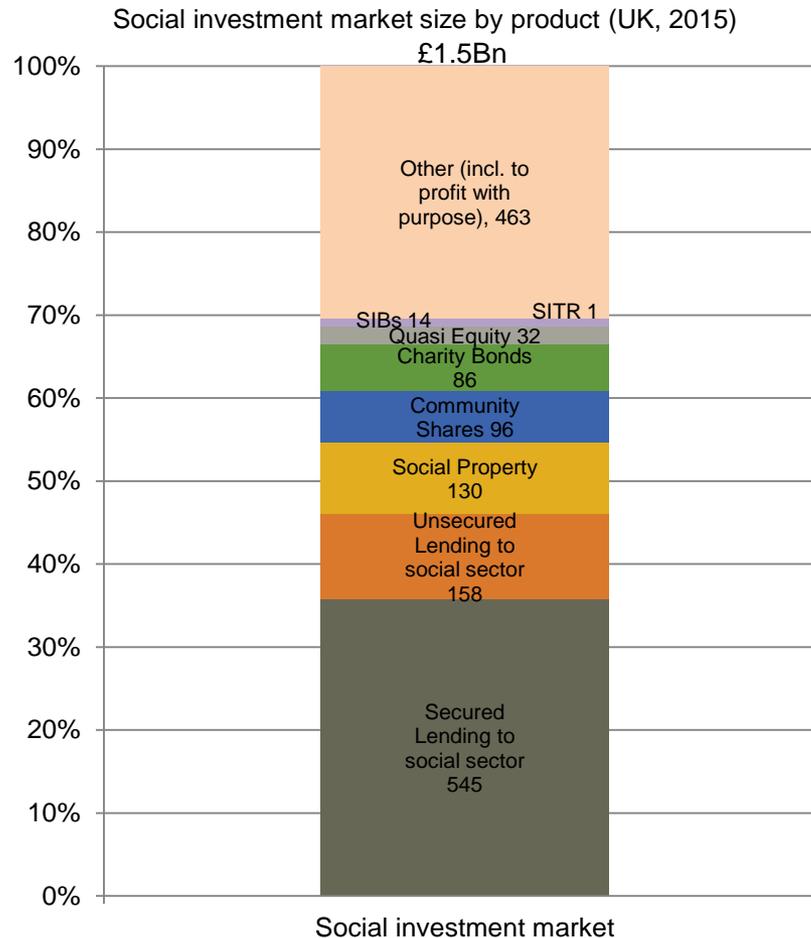
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...HOWEVER FEEDBACK SUGGESTS SOME PERSISTENT GAPS REMAIN FOR SMALL AND TAILORED PRODUCTS

Prior to BSC: Social investment was largely secured lending

- Prior to BSC, the social investment market consisted of:
- Largely secured lending, dominated by 4 social banks
- Small amount of 'unbankable investments' e.g. Futurebuilders ~£20-30m per year
- Other key players (e.g. CAF Venturesome) providing risk capital

Today: Wide range of products; secured lending to social sector still largest product category but only 1/3 of total



Future: large product gaps still remain

- **Access** to finance and **affordability** remain problems for social enterprises and charities
 - Working capital and cash flow
 - Riskier growth capital for early stage
- **Products are not fitting some in the sector**
 - Need for smaller scale (<£100k), cheap, risky, long term
 - Potential for quasi equity, invoice funding, factoring and blended finance (Access)
- A lack of appropriate products is **not the only reason** for demand for finance not being met
 - Often social investment is not appropriate
 - Other barriers are significant (e.g. lack of information, risk appetites)

DIVERSE RANGE OF EMERGING PRODUCTS MAY HELP ADDRESS SOME GAPS

Blended finance



Access will offer new blended finance products mixing grants and loans, focusing on:

- Unsecured loans (blended at fund level)
- Grant and loan products
- Quasi-equity products (e.g. revenue participation agreements)

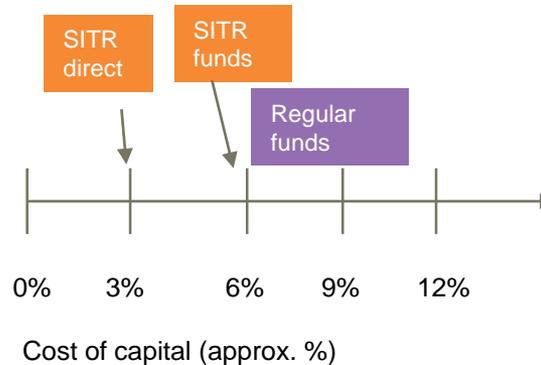
Early Access deals	Grant (from BLF)	Loan (from BSC)	Co-investment
1 First Ark	£2m	£2m	-
2 Resonance	£1.7m	£2.7m	£400k
3 Keyfund	£2.7m	£2.7m	-

Social Investment Tax Relief products



SITR now two years old has seen **30 deals** of total **£3.4m**.

30% tax incentive has encouraged development of new risk return products reducing cost of capital



Source: SITR: Two Years On, NPC, 2016

Crowdfunding products

Examples:



Crowdfunding platforms (e.g. the three above) have taken off in last few years, with rapid increase in investment and number of platforms.

Products have diversified into loans, equity, rewards, and many products combine a number of these.

FUNDING FOR NON-FINANCIAL SUPPORT FOR CHARITIES AND SOCIAL ENTERPRISES HAS CHANGED AND DECLINED OVERALL

Past: Several grant funding programmes; mainly gov't & BLF

Today: Funding available but different and smaller; mainly BLF & Access

Name	Provider	Year	£m
Investment and Contract Readiness Fund	Office for Civil Society, SIB	2012-'14	£13m
Impact Readiness Fund	Office for Civil Society, SIB	2016	£3m
Social Incubator Fund	Office for Civil Society, Big Lottery fund	2012	£10m
Building A Sustainable Infrastructure Service (BASIS)	Big Lottery Fund	2006	£157m
ChangeUp	Central gov't, Capacitybuilders	2004-'11	£200m
Assist	Big Lottery Fund	2011	£6m
Supporting Change and Impact	Big Lottery Fund	2011	£50m
Transition Fund	Central gov't, Big Lottery fund	2010	£100m
Transforming Local Infrastructure	Central gov't, Big Lottery fund	2011	£30m

Name	Provider	£m
Big Potential Breakthrough & Advanced	Big Lottery Fund	£20m
City Bridge Trust Stepping Stones	City Bridge Trust	n/a
Access Reach Fund	Access	£2m
Access/PTC Impact Management Programme	Access Power To Change	£3m
Power To Change Leadership Dev't	Power To Change	n/a
(various programmes)	UnLtd	n/a
"Grants Plus"-models: foundation provides grant and non-financial support	Various foundations	n/a



>£550m historically



Future looks like much less grant funding available for non-financial support

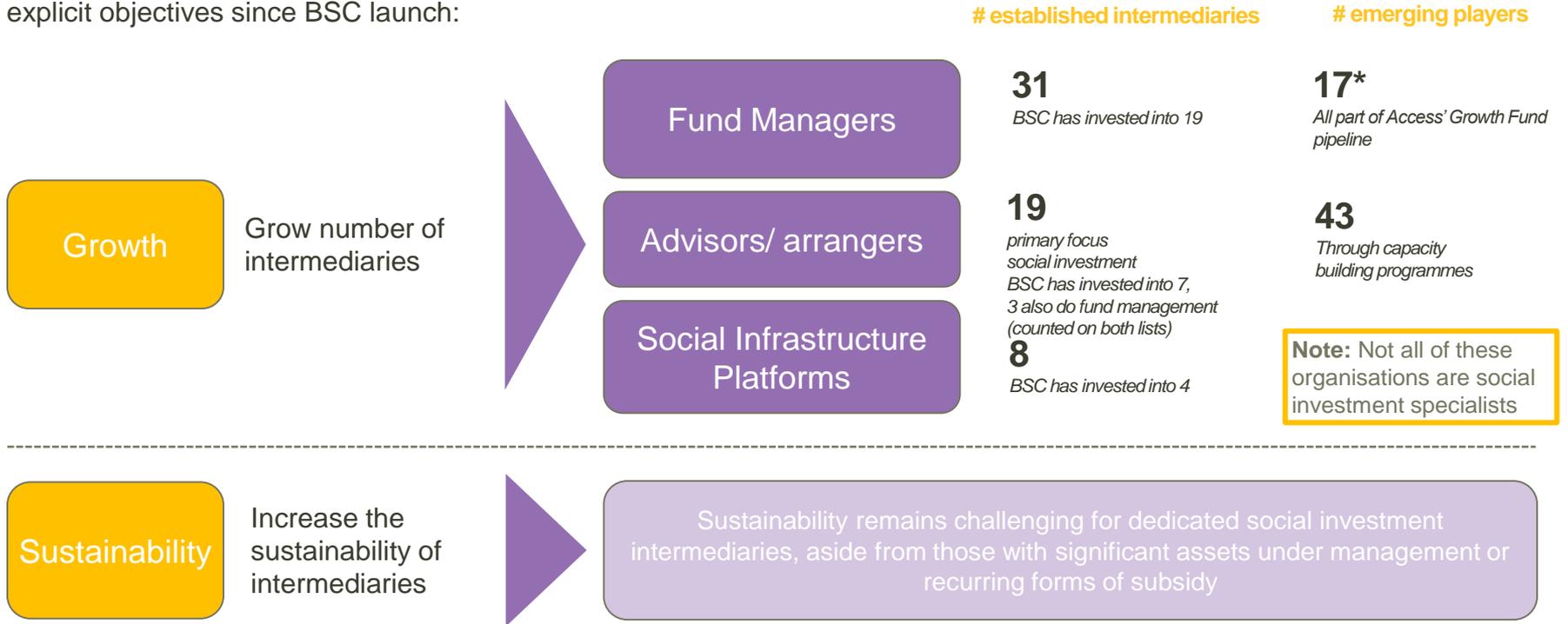
EVIDENCE POINTS TO OTHER KEY BARRIERS FOR ORGANISATIONS IN ACCESSING FINANCE

Barrier to finance	Underlying drivers	Potential solution	BSC Existing initiatives
<p>Lack of information on suitability of finance and where to access</p>	<p>Lack of transparency on cost for social ventures to benchmark pricing</p>	<p>Development of goodfinance.org and increased transparency on cost of capital across products</p>	<p>✓</p>
	<p>Business models of SIFIs do not support the resource requirement of origination in nascent market</p>	<p>Support for intermediaries (and other organisations) to build pipeline and widen engagement with possible investees</p>	
<p>Affordability due to lack of profitability of certain business models</p>	<p>Increasing reliance on government contracts but reduction in profitability of those contracts</p>	<p>Engagement with government on impact of public sector contracting on charity sector</p>	<p>✓</p>
	<p>Need for equity like funding at earlier stages of organisational development but more interest in debt finance</p>	<p>Blended capital for parts of the sector where profitability is temporarily lower (start ups, smaller orgs)</p>	<p>✓</p>
<p>Risk appetite of investors</p>	<p>Unproven nature of business models</p>	<p>Guarantees or first loss for fund managers to increase risk tolerance for investing in marginal business models</p>	
<p>Risk appetite of organisations to take on finance due to uncertainty in paying it back</p>	<p>Lack of understanding of social investment amongst trustees and concerns around conflict with mission</p>	<p>Engagement with charity trustees to improve understanding of social investment</p>	<p>✓</p>
	<p>Volatility of funding environment and lack of equity on balance sheet to support fluctuations</p>	<p>Targeted blended approaches in the form of grant/loan products that reduce risk of taking on finance</p>	<p>✓</p>
	<p>Lack of financial skills to understand future business risks and ability to pay back loan</p>	<p>Support for intermediaries to provide capacity building</p>	<p>✓</p>

THE INTERMEDIARY MARKET IS NOW DECENT SIZE, WITH MANY NEW PLAYERS EMERGING

Only a basic strategy for developing intermediaries proposed thus far

Govt and BSC have focused on two explicit objectives since BSC launch:



Note: We classify an intermediary as an organisation that provides, facilitates or structures financial investments for charities and social enterprises and/or provides investment focused business support to charities and social enterprises.

We have NOT included a number of wider infrastructure organisations that exist in the UK that are in some way connected to the social investment market. These include (but aren't limited to) membership bodies, education bodies, research houses and think tanks. We are also not looking at other social investors who may invest directly into social sector organisations or via intermediaries themselves e.g. foundations, trusts and corporates.

Source: Growing the social investment market: A vision and strategy, HM Government, Feb 2011, Big Society Capital website

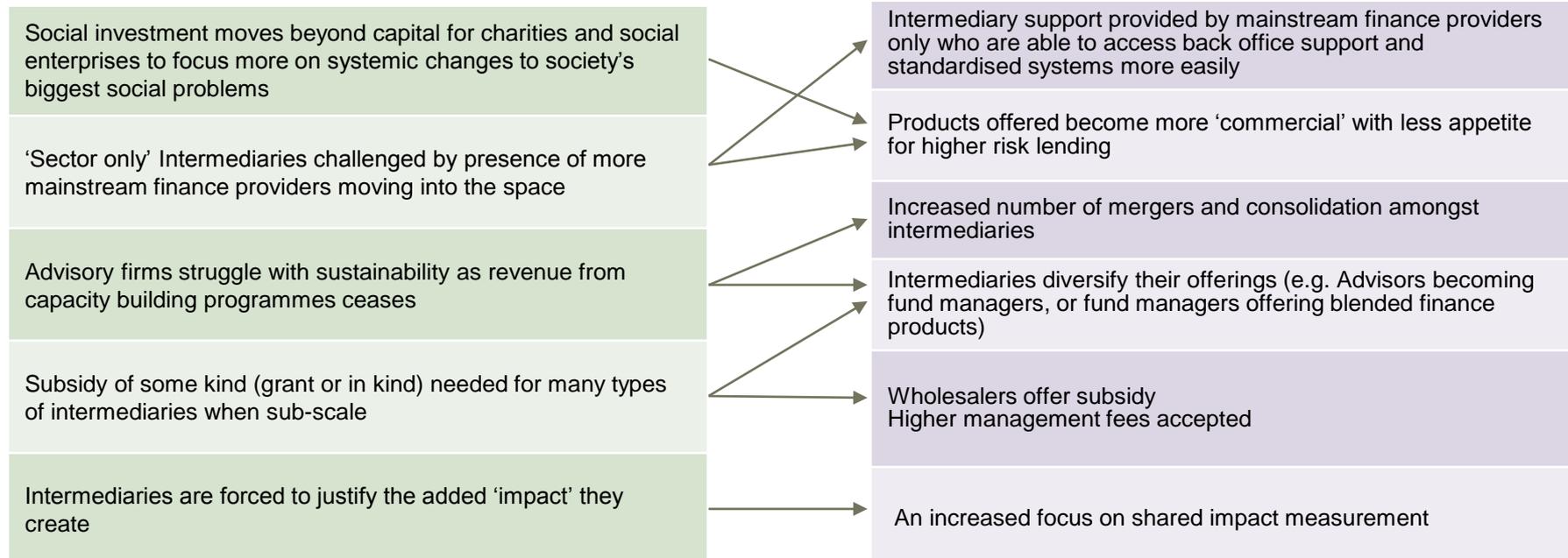
INTERMEDIARIES ARE FACING CHALLENGES THAT MAY DRIVE BIG CHANGES IN THE FUTURE LANDSCAPE

Current Challenges for some organisations

<ul style="list-style-type: none"> • High transaction costs 	<ul style="list-style-type: none"> • Lack of policy experience / resources
<ul style="list-style-type: none"> • A mismatch between supply and demand, in differing ways across products and sectors 	<ul style="list-style-type: none"> • Lack of understanding of true running costs and need for subsidy
<ul style="list-style-type: none"> • Lack of effective data management systems 	<ul style="list-style-type: none"> • Lack of trust between different intermediaries (particularly advisors and fund managers)
<ul style="list-style-type: none"> • Difficulty in recruiting and retaining quality staff with the appropriate experience 	<ul style="list-style-type: none"> • Lack of fundraising skills / knowledge

Possible Future Challenges

Possible Consequences

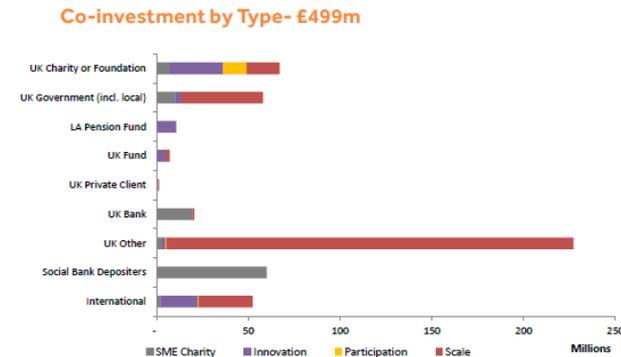


THE INVESTOR LANDSCAPE LOOKS DIFFERENT TO WHAT WAS IMAGINED

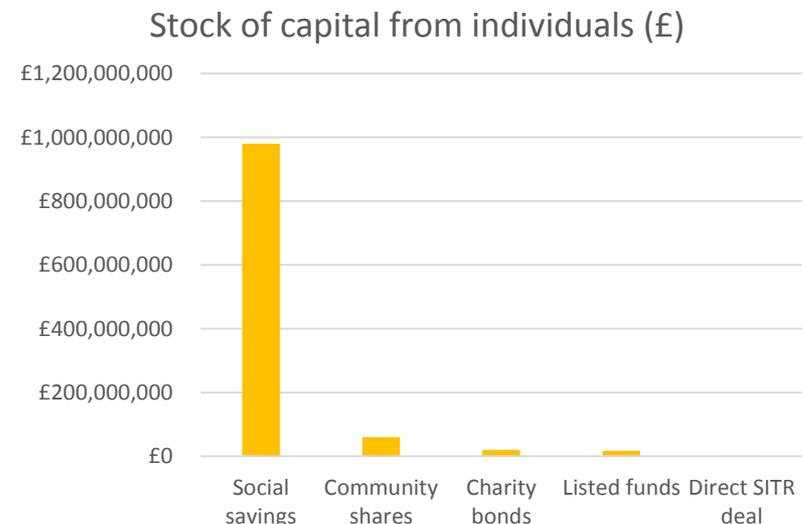
In 2014, we explored the interest of a range of different investors...

Investor group	What we have learnt & key takeaways
Corporates	Significant awareness raising needed. Ambition to access capital through internal channels other than CSR function has proved challenging. Likely to be legal form agnostic and focus on global
Housing Associations	Mostly supporting local projects through grants. A number of collaboration projects into SI did not come to fruition. Their own status has also changed significantly.
University Endowments	Have made "impact investments e.g. Bridges Ventures but less able to make below market return social investments.
Local Authority Pension Funds	Have made some impact investments, mostly those with potential to deliver market returns, are scalable or in asset classes where the risk is understood e.g. property or uncorrelated (e.g. SIBs)
Corporate Pensions	Pension consultants have shown some interest in impact investment – scalable investments and market return needed
Financial Institutions	Propriety funds (Axa, Deutsche Bank) tend to be global & have only a small allocation to the UK with limited appetite for below market return investments (IVUK, BII, and BV SIB Fund have received inv from these funds)
Individuals	HNW & affluent groups have made the most SI to date through social savings, Sitr and charity bonds. UHNW and family offices have strong appetite for impact investments but more global interest, although increasingly interested in funds. Retail interest in SI but lack of savings & appropriate inv products a barrier. Sitr useful in attracting socially motivated HNW & affluent groups to become social investors
Private Banks & Wealth Advisors	Significant regulatory barriers when pursuing investment channels. Refocus efforts around Sitr & philanthropic capital

...in 2016, UK foundations and Govt remain the key co-investors outside of 'scale' investments...



...and a surprisingly large number of individuals are engaged in social investment, but mainly through social bank deposits



Source: Positive Investing Report, Ethex, 2015

THE RANGE OF INVESTORS HAS GROWN, BUT LARGE POOLS STILL LIMITED IN FOCUS ON SOCIAL INVESTMENT

6

Investors

The 3 'buckets' of investor groups have provided a useful frame, although at present there isn't a clear cut analysis to link each group or sub-group to the ideal underlying investment types:

Impact led organisations

- **Trusts & Foundations** – blended finance, issue area experts, SIIG
- NEW** • **Settlor Led Foundations** – a different approach to more traditional foundations, similar to family office
- **Operational Charities** – e.g. Macmillan around specific issues
- NEW** • **International Foundations** – those interested in UK for innovative models they can take back
- NEW** • **Corporate Foundations** – A route to financial institutions
- NEW** • **NHS Foundations** – Potential health partners, grant plus/venture philanthropy

Channels to individuals

- **Crowdfunding** – Tax relief opportunities and beyond (**Affluent / Retail**)
- NEW** • **Donor Advised Funds** – philanthropic capital, can take risk, possible grant layer (**HNW / Affluent**)
- NEW** • **Family Offices** – issue specific and through our membership of Tonic (**UHNW / HNW**)
- NEW** • **Angel Investors** – issue specific and tax relief (**HNW / Affluent**)
- **Wealth Managers** – SITR, DAFs, distributors of products, education (**UHNW / HNW / Affluent**)
- **Financial Advisers** – SITR, distributor of products, education (**HNW / Affluent**)
- **Fund Managers (Long term savings)** – Social ISA or Social Pension (**Retail**)

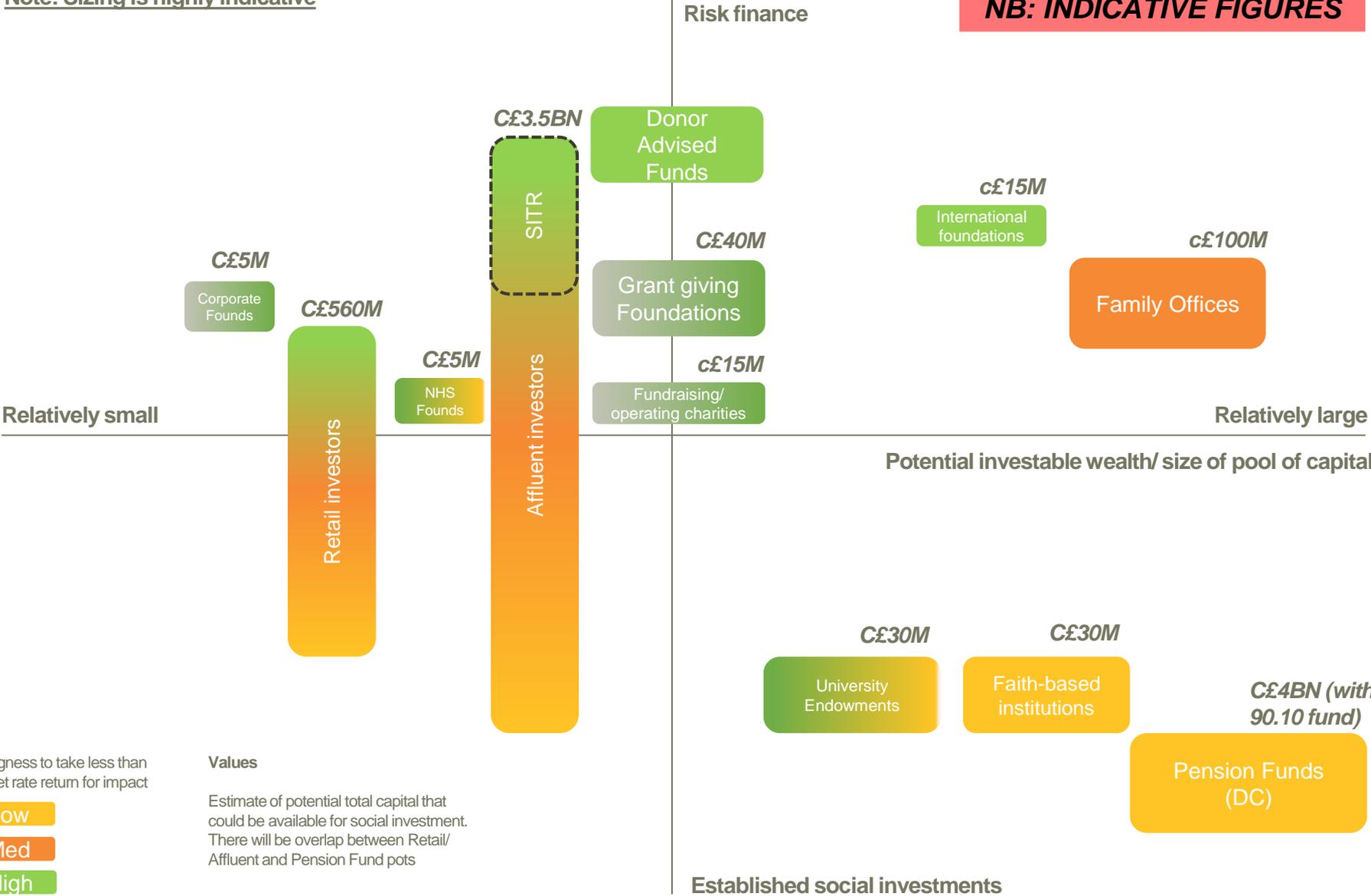
“Motivated” Institutions

- NEW** • **Faith based group** – An area to explore – Vatican initiative, Church of England support of Credit Unions
- NEW** • **University Endowments** – student body interest, focus on innovation, subset with impact investment
- **Venture Fund Managers** – SITR, Social VCT, themed scalable funds
- **Local Authority Pension Funds** – those with interest in social impact
- **Corporate Pension Funds (DC)** – those where the corporate has a “shared value” interest
- **Mainstream Financial Institution interested in Impact** – scalable, as investment manager, own impact fund that might have a small allocation to UK and SI
- **Corporates** – Through BIC and in conjunction with corporate foundation engagement

THE LARGER POOLS OF CAPITAL ARE OFTEN LESS PREPARED TO TAKE RISK OR REDUCED RETURN

Note: Sizing is highly indicative

NB: INDICATIVE FIGURES



Willingness to take less than market rate return for impact

- Low
- Med
- High

Values

Estimate of potential total capital that could be available for social investment. There will be overlap between Retail/Affluent and Pension Fund pots

OUTSIDE THE MARKET, EXTERNAL FACTORS ARE INFLUENCING THE SHAPE OF THE MARKET

7

External

Market trends challenging original hypotheses about how the market works

DIY social investment emerging

- Increasing interest in social organisations raising money directly from investors e.g. Freedom Bakery, FlipFinance
- Smaller organisations favour reduced fees and direct contact with interested investors

Government priorities may be focused elsewhere

- Recent Govt changes meant loss of traditional social investment champions (e.g. PM) and may need new ones
- New Government keen to see the impact of social investment demonstrated
- Govt messaging around 'just managing' rather than the 'most disadvantaged' people, traditionally the focus of social investment

Financial sector focusing on impact investment

- Less direct social investing from financial institutions than originally expected
- Financial sector instead increasing focus on 'impact investment' through listed products outside of BSC remit

International

- Range of countries now trying to build versions of BSC, including Australia and Portugal – Global Steering Group now at 14 countries
- Social impact investment achieving growing media attention in USA amid greater communications drive

Stewardship roles changing

- New host of governance mechanisms developing e.g. Social Investment Forum, UK advisory board, BSC advisory board, BSC intermediary advisory group

DIY SOCIAL INVESTMENT



HM Government



SOCIAL IMPACT INVESTMENT TASKFORCE



SOCIAL INVESTMENT FORUM

OTHER COUNTRIES OFFER INSIGHT INTO POSSIBLE DIFFERENT SHAPES OF SOCIAL INVESTMENT MARKET

7

External

Market Insight

Questions for UK Social Investment



USA

- Strong CDFI presence, both in number (>1000) and scale (~20 with >\$1bn in assets)
- Bolstered by dual role in financing housing as well as social enterprises

Should social investment prioritise a core of large strong intermediaries, including through infrastructure?



Australia

- Impact investment development led by financial institutions, with federal Govt lagging behind (NSW Govt piloting SIBs)
- Largescale finance available for social infrastructure in addition to social enterprises

Should social investment target greater independence from public sector?



Portugal

- Need to develop broader range of products for social enterprises (incl. grant/loans)
- Joined-up approach to investment readiness pivotal to stimulating sustainable demand

Should social investment be more focused on early stage pipeline, including product innovation?



France

- Holistic, ecosystem approach to involving retail investors (products, certification, ...)
- Innovative sources of capital supply (e.g. >€4bn in "90/10" solidarity savings funds)

Would a systemic focus on standardising and 'regulating' investor-facing products be effective?

EXTERNAL COMMENTARY INCREASINGLY HOLDING SOCIAL INVESTMENT TO ACCOUNT

7

External

Sector commentators challenging BSC itself on transparency

Alternative Commission on Social Investment

50 recommendations for social investment, focusing on:

- Greater transparency;
- Changes to BSC to spend down its capital;
- Focus on individual investors; and
- Making social investments within and by social sector itself – DIY investments



NPC

NPC's 2015 Manifesto:

- Called for more transparency especially around BSC's social impact and investment framework
- Also questioned whether BSC's financial return target is too high

Media commentary challenge SIBs, talk about tech and say its time to get real



"Essex was also the first local authority to trial a [social impact bond](#). In hindsight, although he said it worked, and resulted in considerable savings, Hill sounds only moderately enthusiastic, possibly because investors wanted the bond spent on a particular group of families so they could see if their dosh was what made the difference. Although Hill says he might use social investment again, it's clear (it) ... does not sit comfortably with him."



"While they're trying to figure that out, fintech start-ups are attracting customers with the likes of digital wallets, social media payment apps and social investment opportunities"



"Now is the stage in social investment where we're going to find out whether it's hype or whether it's real," says Jonathan Jenkins, chief executive of the Social Investment Business.

THANKS FOR READING

For further discussion on the future of social investment, please refer to the accompanying document “***Reviewing the landscape of UK social investment – opportunities, challenges and ‘critical questions’***”

It can be found [on our strategy webpage](#)