APPГ ON CHARITIES AND VOLUNTEERING SOCIAL INVESTMENT
16.00-18.00 13 April 2016, Committee Room 12

David Floyd, Managing Director at Social Spider

- Despite the best of intentions, politicians are often the biggest source of misinformation about social investment (SI), which creates difficulty for organisations seeking to understand how the market works.
- Government backed Big Society Capital (BSC) to expand the market, hoping there would be a big expansion in SI. This hasn’t transpired. There are many examples of where it has worked well, but the market hasn’t changed enough to provide the kind of investment imagined.
- Organisations are seeking a market that doesn’t exist, or entering a market in a state of failure. The challenge isn’t for organisations to understand SI specifically, but rather the wider picture about their business. It isn’t important for organisations to know the intricate details of financial instruments, but it is important to know why they are looking for money, what they will do, and how they will repay it.
- We need to look at how to practically share information and to encourage more discussions between investors, borrowers and policy makers. We need more and better examples of the instances where social investments does work, for example the Freedom Bakery’s use of SI tax relief. Examples give an idea of what is possible in a way that organisations can understand.

John Smart, CFO at HCT Group

- HCT is one of the largest social enterprises in the UK, having used SI to grow to £50m turnover. By bus company standards HCT are small, but they are focused on providing social impact not return to shareholder. HCT use social investment to grow the organisation not for vanity reasons, but to increase the social impact of what we deliver.
- Charities are unable to raise equity so must rely on loans, and the regulator doesn’t allow repayment by profit, only income. HCT has used quasi-equity where the return is linked not only to turnover but also to social impact, allowing a reduced pay rate when social impact targets are met. Borrowing would be cheaper if charities could issue equity, as issuing loan notes every 5 years is resource intensive. Charities incur large legal fees if investors wish to enter or leave a loan, money which could be better spent on increasing impact, which wouldn’t be an issue if their debt could be traded.
- SI loans must be shown as debt on balance sheets, even if the loan doesn’t need to be repaid. This makes the gearing look high which does not help when bidding for government contracts. It would help social enterprises bid for government contracts if their different financing arrangements could be recognised and they were put on an even playing field with commercial organisations.
- HCT have used SI to scale their business, increasing the impact they can deliver. An Increase in the level of Social Investment Tax Relief would be extremely welcome- social enterprise is a vital part of the UK economy and anything to improve it is great.
Geetha Rabindrakumar, Head of Social Sector Engagement at Big Society Capital

- BSC is an independent organisation helping charities access investment to do more of their good work. BSC recognise that the charity sector is so diverse that a range of tools are needed. BSC is a wholesaler who invests in lenders who provide SI products. They also champion the SI market, and encourage more organisations to enter. Some tools are complex, like SI bonds.
- Most SI is actually just a loan for a charity to use as they need, such as organisations like HCT who are scaling up services. We also see an increasing number of community groups using SI to run community assets using community shares.
- Many of those who have accessed SI have increased their impact by scaling up their services or creating new services that wouldn’t have otherwise been commissioned. They are also improving their ability to evaluate and measure impact, and applying this learning to other aspects of their work.
- One barrier is a lack of internal capacity for organisation to fully understand the market - It is great that there are more options now available, but this can mean it is hard to find what suits your needs. Goodfinance.co.uk is a website being developed that will help. The due diligence processes can be very hard and could be simplified.
- Borrower demand is for funding under £100,000, far below available loans. Looking at NCVO’s Almanac, and recent research funded by the Lloyds Foundation, we can see the important role that small- to mid-size organisations play in terms of tackling social problems, yet there is an inequality in their access to finance to allow them to scale. Trusts and foundations are currently looking to SI as a way of making organisations sustainable beyond the life of a grant. We are working to increase access to finance for smaller organisations such as blended finance (Access), support for crowdfunding platforms, and promoting Social Investment Tax Relief.
- SI needs to be shown to be relevant to the issues organisations tackle and the sectors they operate in. Case studies are useful for learning where SI has and hasn’t worked - drawing on the experience of people that have ‘done it’ is key to moving forwards. Key questions need to be asked before questions about products – what are you trying to achieve, do you want to scale/replicate impact and how, and is there a revenue model?
- Working in partnership with others who can connect and translate eg membership bodies, foundations and federated charities. BSC are piloting a product guide with Homeless Link - they know their members and their needs and can provide information about SI that is relevant to their sector.

Seb Elsworth, CEO of the Access Foundation

- Access Foundation was created to encourage the provision of smaller scale loans.
- In SI both parties want some sort of impact as a result of the investment, not just return. The discussion about SI hasn’t always felt relevant- it isn’t an alternative to grant funding, but it is an opportunity to increase trading income. Many organisations can’t quickly move to an entirely trading-based model, but many others can start to build an aspect of trading into what they do, thereby diversifying their funding. Recently there has been a large increase in demand for SI to use as working capital.
- Simplicity of language is important- the leaders of these organisations are not financiers by background, so we need to speak about SI in terms of benefits of them.
- Access provide a blend of a loan from BSC and grant from the Big Lottery Fund to the organisations making loans to charities and social enterprises. This enables lenders to take
higher risks, or to pass on the grant to their borrowers, easing the journey for the organisation. This model makes it possible to lend even though there is a chance of default.

- We are very interested in finding organisations who have the knowledge and expertise on the ground to lend to local organisations. Unsecured loans to organisations who are borrowing for the first time are risky investments, even with the grant built in, so the loans have a 6-12% interest rate. Charities should ignore the headline interest rate and look at their monthly payments and whether it fits for them and what they can afford to repay.
- We are also investing £60m in grant programmes to help organisations to be ready for social investment. To do this we have been consulting on what investment-ready looks like and what characteristics we should be encouraging.

Questions and Answers

- Lord Hodgson: There was too much expectation on SI at the beginning, but these movements take time. Charities should be challenging the regulator to allow investment in charities, those who invest will then have an interest in the future of the organisation. Accountants should be looking at how to deal with balance sheets for social enterprises, as it needs a new approach.
  - DF: The government has responded well to practical challenges, but rhetoric is still a problem. Misleading information from politicians is covered in the newspapers, impacting the expectations of what social investment can offer.
  - SE: The Charity Commission is currently looking at guidance for charities funding non-charities- we think it is important that charities are not discouraged from being able to give to CICs and social enterprises, not just registered charities.

- Camilla Buchanan, social investment team at the Cabinet Office: Flagged the government’s 2016 social investment strategy. The big difference is they are now asking about infrastructure, from the front line, and promoting projects which enable charities to ask ‘how do I grow?’
  - GR: We need to make central and local government more aware of social investment. When charities are interested in using social investment the missing piece is normally a commissioner who needs to be persuaded to commission services differently.

- Angelica Finnegan, Charity Finance Group: Is there a two way conversation happening from the grassroots? Are there products available for organisations who want funding for restructuring?
  - SE: Championing organisations realities is what Access Foundation is for. Our growth fund doesn’t have to be for growth- it can be for restructure, though you do need a revenue stream to be able to repay. Funding could facilitate cooperative work with other organisations, lowering overheads, which would fund the repayments.
  - GR: SI won’t work for all organisations, but it is creating interesting new ways to do things. Government grants have helped community led housing spaces to take on and do up empty properties. These projects have now started to also take on social investment and think about ‘what next’ and help inform development of new ideas.
  - JS: We have found lenders have been happy to talk and to alter their products, as well as provide advice. It is a new market for the lender and the debtor.
  - DF: Funders saying no to organisations means we know there won’t be a commercial market for SI, instead lenders are testing whether there can be a market if they provide smaller blended grants. This is evidence that a two-way conversation is definitely going on.
• Baroness Armstrong: Working with a charity in the North East, people outside of London are being excluded from the conversation. SI bonds are too complex, they need simple goals in order to work, and can’t deal with complex problems or small projects. Organisations shouldn’t ignore the interest on these loans- charities can sometimes get much better rates on the high-street than at the SI bank. The regulator needs to look at the increasing accountability around regulation being placed on trustees, making becoming a trustee seem too high risk.
  o SE: Charities should always use mainstream banks if they have the opportunity, as they can offer much better rates as they operate in a different market- hopefully they will soon operate in the SI market too. Government is the biggest buyer of services, and sometimes the way commissioners behave undermines the rhetoric of the Cabinet Office.
  o GR: Where the conversation is happening is not the same as where the action is happening. There are lots of examples of SIBs outside of London, e.g. the DCLG homeless bonds in Birmingham and Leeds. We are trying to shift the conversation outside of London by creating locally run and hosted networks.
  o DF: Not all SI bonds are equally complicated- some are phenomenally complicated, but some, like the DWP payment system, are incredibly simple.

• Baroness Pitkeathley: Should organisations be working in consortia to take on loans?
• GR: This can work- Ways to Wellness SIB is an example of this- four providers collaborating, overseen by a fifth organisation.

• Susan Elan Jones MP: Should the high street banks be encouraged to be more involved?
  o Simon Bowkett, Exeter CVS: Is risk appetite of lenders in the market too low?
  o GR: Whether risk appetite is too low depends on whose money is being risked- pensions fund money needs a lower amount of risk than a foundation with a social mission. Sometimes there is a need to make the investors aware of how low the risk actually is.
  o SE: Big SI funds are borrowing to lend, so they need to be fairly confident they will be able to repay. Access’s model, using a grant aspect, means they don’t need to get it all back, allowing lenders to try new things.
  o DF: As SI develops lenders judgment is improving, and we will get to a point where banks may think a loan is too risky, but SI lenders won’t, as they have the know-how.

• Local Giving: Asked whether anything will be in place to help micro-organisations come up with achievable goals for investment. 70% of organisations they polled didn’t know what SI was.

• Becca Bunce, Small Charities Coalition: We need to use plain English- people hear about SI bonds and get put off by how complex they sound.
  o SE: Goodfinance.org is a website that addresses this, Access are also funding work on improving accessibility. The confusion can be because we are asking the wrong questions- because of the hype around SI people jump to talking about the final product, but they should talk about the journey and the range of tools available.
  o DF: The simple message about SI bonds that gets through does often put people off- and this is a shame. Most organisation shouldn’t be thinking about bonds, and there are many other SI tools that would allow them to grow.

Next meeting: Charities in public service provision

16.00-18.00, Tuesday 5 July, Committee Room 18, Houses of Parliament

Please RSVP to charitiesappg@ncvo.org.uk if you would like to attend.