De-mystifying the Hype: Social Investment Update

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I started as Director of Social Finance at Cass CCE around a year ago and from my initial work identified a wide range of barriers to nonprofit organisations using social investment to drive their work. The biggest barrier I identified was charities' ***understanding and knowledge*** about what social investment actually is, which was holding back demand from the sector.

To close this gap, Cass CCE ran a series of four seminars on 'Demystifying the Hype' around social investment last year. The seminars allowed charities to:

1. Listen and learn about social investment and crowd-funding
2. Listen to a practitioner who has done this before and ask questions; and then
3. Have a group conversation with peers about what this might mean and how it could be useful in their context.

We ran three seminars for the charity and nonprofit sector and one separately for the investment community. Speakers such as Andrew Purvis (K-10), Geetha Rabindrakumar (Big Society Capital) and Jonathan Jenkins (Social Investment Business) gave a practitioner's point of view and brought the subject to life. Feedback was exceptional.

This brief note details some of the key learning from those seminars. We will be running these seminars again over the next few months – please attend if you are interested in knowing more.

In summary: What is Social investment?

Social investment is the use of repayable finance to achieve a social as well as a financial return. It can provide a charity with funding for the following:

1. As working capital to support the organisation as it does its business
2. To purchase an asset such as a building for the future
3. To invest in fundraising using reserves to 'gear up' income
4. To invest in a specific project or trading activity – for example setting up a social enterprise
5. By providing funds to other nonprofits – the sector helping itself to grow
6. Funding a change in business model around IT innovation or move to low carbon economy.

We learned that for *charities and nonprofits*, social investment can:

- Provide a new source of funding;
- Fill financing gaps for innovation, growth and infrastructure; and

- Develop sustainability and autonomy.

For *financial investors, social investment* can:

- Enable borrowing to be recycled for onward investment;
- Deepen engagement with communities; and
- Develop new responsible forms of funding.

We had around 120 participants across the seminars, from sceptics to interested parties. We reviewed the feedback comments and overwhelmingly found that people were able to go back to their organisations, peers and Trustees with **greater knowledge** about whether this was a useful tool for them or not and engage in informed conversations. So, what did they see as the opportunities and barriers?

How could you increase your impact through social investment?

Social investment should not be seen as a 'silver bullet' and the theme of each seminar was that business models are key. Social investment cannot be used in every circumstance, but a balanced funding mix from donations, grants and contracts *and* using social investment is key.

Social investment was seen as a tool whereby charities could break free from the cycle of asking donors for donations or grants and establish an autonomy and flexibility in their operating models. Social investment was seen as a more commercial tool which could lead to better focus, better service levels, improved quality of work and could enable the funding of a sustainable infrastructure. However, capital had to be paid back and any business model needed to focus on repaying capital first and foremost.

It also became clear that impact is crucial to social investment. Without measuring outputs and outcomes, you will not be able to prove the benefit of a charities' work and will be unable to find funding. Focusing on impact also brings objectivity and clarity to the focus of an organisation's work.

The ability to take on funding depends on the phase of growth of a charity- it could be innovation capital or it could serve as investment money to take work to scale. Social investment can also provide a long time horizon, say 10 years plus, and the benefit this brings. Innovation money can allow new models to be developed to help our beneficiaries and bring in technology and change. It additionally allows a flexibility in management and the ability to change direction and approach where necessary, which grants sometimes do not.

Overall the seminars identified the key features of social investment as improving sustainability, focusing on impact, providing money for innovation and infrastructure and allowing our work to be taken to scale.

It was seen as an overwhelmingly positive new tool for the sector but one that is not yet well understood.

What are the barriers to you taking on investment?

The key barrier to taking on social investment is seen as the level of understanding within charities and their Trustees regarding this. Charity Finance Directors need to up-skill to be able to take this forward, as do Trustees.

Trustee risk aversion and resistance was highlighted by some, especially in light of recent governance scandals such as Kids Company. There was a general level of concern about something new which could also be seen to be providing a return to commercial organisations when nonprofit organisations exist to reinvest their profits for civil society.

Part of this was also the perception of charities being centred around grants and philanthropy, which creates a barrier to the use of investment. Charities are seen as caring, social and focused on non-financial issues, whereas investment is seen as profitable and wholly financial. To bridge this gap requires conversations which begin to alter the view of social investment as both providing a financial *and* social return – this is critical if we are to bring charities and the investment community together with a common purpose.

There is a perception that with the level of grants going down and donations dropping away, something needs to be done to ensure sustainability of funding. Many saw social investment as a sound new tool. The charity sector however lacks the cross-over talent which talks the language of both charity and investment. Likewise, intermediaries were seen as sometimes focused too much on profit rather than helping charities to understand and develop new business models. Developing understanding, capacity and skills will be key for the future journey.

We heard from several charities that used social investment. It had, in some cases, triggered a rethink about their entire business model. Many urged charities to try piloting ideas. However, this requires a clarity of proposition and focus on return on investment which some funders felt that charities were lacking.

From the investor's side, the size of deals was seen as a barrier. Many small value investments are costly, and take significant management – so maybe simple loans are more effective, cheap and simpler to administer. The seminars also highlighted the fact that there is a significant level of capital available, but often investors do not feel that charities are providing investible propositions. The due diligence behind social investment was seen as costly and complex and currently not streamlined enough.

The investor conversations highlighted the wide range of capital available from mainstream banks, high net worth individuals, foundations and family trusts. The alignment of objective between lender and borrower was seen as key, as was the clear understanding of motivation and any trade-off between social and financial returns.

The management of impact metrics, outcomes and data was seen as a key barrier and the cost of establishing these. On the flip-side many attendees said this was critical to be able to

justify the charities' work. How can you prove the impact of a charity if you can't measure objectively?

Finally, there were issues centred around the investments themselves. How do we create financial products that are right for charities and nonprofits while ensuring a sound financial *and* social return on investment? How do we measure any return on investment when there is both a social and financial component? How do we create exit opportunities for investors, while giving security for nonprofits, and similarly how do we build patient capital that lasts for the long-term?

All of the barriers pointed to well informed consultants and intermediaries helping the sector to evolve. It also pointed to the investment community having an obligation to fund this potential education of charity staff and Trustees.

So on balance was social investment seen as a good or bad thing?

It was obvious from the seminars that for many, the wave of energy for social investment is here and now. However it is not a 'silver bullet' and may not be applicable for all charities. In our assessment, 10-20% of organisations are already engaged with it and exploring how it can work to help them. A further 60% of charities are inquisitive and want to know more.

We are in a fledgling place at the moment with social investment but the opportunity is set to grow massively in future as more organisations identify how social investment can help develop sustainability, scale and greater impact.

More than anything the language barrier needs to be overcome so that investors are able to talk to charities and nonprofits and understand their desire to mix financial and social return. Equally we can create return on investment metrics which manage both financial and social measures.

One thing is certain, the energy wave will only see social investment funds grow and charities making more use of social investment as a tool. Measuring impact and outcomes will be key. As will redefining business models and looking at a balance of donations, grants and contracts *and* social investment to underpin the sector's work.

It looks like this new tool is here to stay.

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