



HM Government



Growing the Social Investment Market: The Landscape and Economic Impact

RESEARCH REPORT



Report prepared for the City of London, Big Lottery Fund, Big Society Capital, and Her Majesty's Government by ICF GHK in association with BMG Research

JULY 2013



HM Government



Growing the Social Investment Market: The Landscape and Economic Impact

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by ICF GHK in association with BMG Research

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Foreword

The social investment market is fast developing, providing an innovative way of enabling the delivery of services to society. By unlocking private capital to help finance social sector organisations, the market allows these organisations to support disadvantaged individuals and groups, generating social benefits.

The UK is successfully establishing itself as a global leader in using social investment to address social problems and has led the way in the development and implementation of innovative products. This is exemplified by the successful first G8 Social Impact Investment Forum hosted by the UK in June 2013.

Our respective organisations - Big Lottery Fund, Big Society Capital, City of London Corporation, and Her Majesty's Government- are committed to working together to support the UK social investment agenda. We are delighted to have jointly commissioned this research report. It provides a robust scrutiny of the size and characteristics of the UK social investment market, one year on from *Lighting the touchpaper*, the initial analysis of the social investment market. In addition, this report presents detailed evidence of the positive economic impact of the market. This is the first time an economic impact assessment on social investment has been conducted, and when considered alongside the social impact of the market, the results give weight to the business case for social investment.

Following the success of the G8 Forum, this report is timely in demonstrating the scale and speed of growth in the social sector. In 2011/12 an important milestone was reached - the market surpassed the £200m mark in value for the first time, showing growth of almost a quarter in a year, with the concomitant greater social good that can result from this market growth. We would expect subsequent research to show even greater growth, taking into account the investment contributions made by Big Society Capital since its launch in April 2012.

The very nature of social sector organisations means they have positive social impacts in their localities. However, as this report demonstrates, the market also has economic value, nationally and regionally. At a gross level, over their lifetime, the 765 reported investments made in 2011/12 will result in the creation/safeguarding of 340 social ventures, 6,870 UK FTE jobs, and £58m in Gross Value Added (GVA) contribution to the economy.

The report highlights more nuanced aspects of the UK social investment market. Smaller Social Investment Finance Intermediaries (SIFIs) are leading the way in product innovation, having completed a number of small deals across a range of new and interesting products. Clearly, opportunities do exist for greater funding of these organisations to help them reach scale and sustainability. There is also evidence of greater coverage of the English regions and Devolved Administrations, which both reinforce London's presence and highlights other growth within the UK. There is however, heavy concentration among lenders, with seven SIFIs providing 90% of social investment capital - and an increasing proportion of this is secured lending. This raises strategic questions for our organisations, for investors, and for policy makers in developing the financing options that meet social ventures' needs.

Each of our respective organisations is actively involved in supporting the UK social investment market. The launch of Big Society Capital has provided the world's first wholesale social investment fund with capital of £600m with which to help build the sector. Having deployed £30m to date, Big Lottery Fund is an increasingly active

grant maker and social investment support provider. The Fund intends to commit a further £100m to catalyse social investment in support of more sustainable social ventures, to the ultimate benefit of people and communities most in need.

The City of London has created its own social investment fund of £20m, and has so far made three investments. The Corporation operates a 'buy social' policy to procure goods and services from social ventures and is working to encourage other businesses to do so too. It is also supporting social ventures through its own City Action programme.

The UK Government remains committed to its role in developing a bigger, sustainable social investment market. Significant progress on social investment has been made in the past 12 months, with highlights including a commitment to a tax relief for social investment, establishing a £10m Social Incubator Fund for early-stage social ventures, creating a £20m Social Outcomes Fund for Social Impact Bonds, and funding the newly-launched Global Social Entrepreneurs Network. The UK has 13 operational Social Impact Bonds, 10 of which have been delivered by the Department for Work and Pensions's £30m Innovation Fund.

The UK Government's commitment to social investment is an important part of the Government's Social Justice Strategy, which is aimed at tackling the causes of poverty and enabling disadvantaged individuals and families to make positive, lasting changes to their lives. The growth of the social investment market is a key indicator¹ in delivering the Government's Social Justice Objectives.

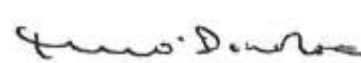
Our organisations reflect a range of perspectives and expertise. We look forward to working closely with other partners to build on the growing energy and commitment to this sector. We commend this report for providing much needed data to help understand the shape and scale of the UK social investment market and the positive social and economic impacts it is delivering across the UK.



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¹ HM Government (2012) *Social Justice Outcomes Framework*, Department for Work and Pensions.

Headline findings and key trends

- In 2011/12, the UK social investment market grew by almost a quarter from 2010/11 to £202m through 765 deals.
- Of the 29 SIFs actively investing in 2011/12, four large social banks and nine large SIFs investing greater than £1m accounted for 97% of the market by value.
- The volume and value of deals reveals the social investment market was highly concentrated in a relatively small number of SIFs in 2011/12.
- There is evidence of greater coverage of the English regions and Devolved Administrations, which both reinforces London's presence and highlights other developing areas within the UK. This indicates substantial diversity in the geography, sector and social outcomes of investments.
- There has been an increase in secured lending as a proportion of the total market value, from 84% in 2010/11 to 90% in 2011/12, making this the predominant lending form. Nevertheless, a greater diversity of social investment products was on offer in 2011/12.
- The majority of SIFs (89% of respondents) expected to increase their investments in social ventures over the next two to three years.
- This report clearly demonstrates the value of the social investment market, not just in social terms but also the economic benefits, by undertaking a robust economic impact analysis for the first time.
- At a gross level, over the lifetime of their finance period, the 765 investments resulted in the creation or safeguarding of 340 social ventures, 6,870 FTE jobs, and £58m in annual GVA contribution to the UK economy.
- At the level of the regional economy, a three year social investment of £10,000 would generate almost six net additional FTE jobs and over £110,000 net additional GVA in the region.
- Almost all SIFs continued to report their plans to grow investment, with half planning to partly achieve this through the launch of new products.
- There is potential for more funding provision for the many smaller SIFs, which offer unsecured lending products, to help these SIFs extend their reach to a wider range of social ventures. There are also new types of funding source available for social ventures to access.
- It is important to be aware that growth constraints on the development of the social investment market remain.

1 Executive summary

In January 2013, Big Lottery Fund, Big Society Capital, City of London Corporation, and Her Majesty's Government commissioned ICF GHK in association with BMG Research, to:

- Assess the size and characteristics of the UK social investment market as of March 2012; and
- Calculate the (gross and net) economic impact of UK social investment, measured through Social Investment Finance Intermediary (SIFI) lending activity, in terms of UK jobs, businesses, turnover and Gross Value Added (GVA), over the financial year April 2011 to March 2012.

The research methodology included a survey inviting all known SIFIs in the UK to participate, and a survey of social ventures² who have received social investment.

1.1 Why was the research commissioned?

While social investment activity is increasing, data in this nascent market is still limited. Working in partnership, the organisations named above sought to address this need by commissioning this research to build on previous research³ to bolster the evidence of the market and assess its development over time. This report also presents for the first time, a detailed and robust analysis of the economic impact of the UK social investment market, at a national and regional level.

In 2012 there were an estimated 180,000 SME social enterprise employers in the UK⁴, rising to 688,000 when including sole traders⁵, developing innovative and sustainable ways to deliver goods and services and tackle some of our most entrenched social problems. They are creating jobs, employing around two million people in 2012 and contributing some £55bn to the UK economy⁶, bringing wealth into communities and helping to rebuild the economy.

Social ventures could achieve greater social impact if they were able to expand existing goods and services, take up new opportunities and reach scale. To do so, they need access to the finance they require: 'social investment'. Most recently,

² Social ventures operate across a range of markets and span a range of organisations including charities which trade, social enterprises, and community organisations. They are not defined by legal form but rather by their objective - which is to deliver social results, as opposed to that of private sector businesses which is to generate profit for owners or shareholders. Social ventures can, and do, operate in a commercial way but are distinguishable by the fact that they use the majority of any surplus generated to further their social objectives. Additionally, social ventures are independent from Government.

³ Specifically, this report considers 2010 /11 data on the social investment market. See: Boston Consulting Group (BCG) & The Young Foundation (2012) *Lighting the touchpaper: growing the market for social investment in England*, <http://youngfoundation.org/publications/lighting-the-touchpaper-growing-the-market-for-social-investment-in-england/>

⁴ Cabinet Office (2013) *Social enterprise: market trends, based upon the BIS Small Business Survey 2012*, BMG Research, <https://www.gov.uk/government/publications/social-enterprise-market-trends>

⁵ Ibid.

⁶ Ibid.

CDFFA/RBS Group (2013) estimated the potential funding gap for social ventures to be in the order of £1.3bn and £2.1bn per annum⁷.

To help fill this gap, and as the UK marketplace for social investment has grown, an emergent base of specialist Social Investment Finance Intermediaries (SIFIs) – including social banks and Community Development Finance Institutions (CDFIs) – has developed.

1.2 What did the research find?

1.2.1 Size and characteristics

Over the financial year period April 2011 to March 2012, the UK social investment market grew by almost a quarter from 2010/11 to £202m per annum through 765 deals.

- A total of 29 SIFIs were identified as active social investors in 2011/12, led by four large social banks, and nine large SIFIs who invest more than £1m per annum. Two thirds (19) of the investing SIFI population classified themselves as Community Development Finance Institutions (CDFIs).

The volume and value of deals reveals the social investment market was highly concentrated in a relatively small number of SIFIs in 2011/12.

- The three largest organisations accounted for 81% of total investment (by value) in 2011/12, and seven organisations accounted for 91% of investment;
- The four social banks accounted for 82% of total investment, up from 70% of the market in 2010/11 – although only 30% of the total number of investments;
- After the social banks, the nine large SIFIs (investment greater than £1m), accounted for 15% of the social investment market by value, equivalent to £30m, and 56% of the total number of investments; and
- The 16 small SIFIs (investment under £1m) experienced significant growth in line with the market (an increase of around a quarter from 2010/11), but still only accounted for 3% of total social investment (just over £6m of investment) and 14% of the total number of investments.

There is evidence of greater coverage of the English regions and Devolved Administrations, which both reinforces London's presence and highlights other developing areas within the UK. This indicates substantial diversity in the geography, sector and social outcomes of investments. The pattern was of no dominance of one sector, region or social outcome, suggesting there is diversification across the social investment market (see Figure 3.4 and Figure 4.5 in main report).

- The Devolved Administrations and English regions were served by at least three quarters of investing SIFIs, reflecting that the majority of SIFIs serve national markets; and
- Most SIFIs offered a variety of business support, capacity building and investment readiness activities alongside direct investments.

⁷ CDFFA & RBS Group (2013) *Mind the finance gap: evidencing demand for community finance*, ICF GHK, <http://www.cdfa.org.uk/wp-content/uploads/2013/01/Mind-the-Finance-Gap-summary-report.pdf>

There has been an increase in secured lending, and in 2011/12 this was the predominant form of investment. Nevertheless, a greater diversity of social investment products was on offer in 2011/12. Investor types included individuals and angels, and commercial financiers - alongside the still dominant social banks (using deposits) and Government. In particular:

- Secured loans as a proportion of the total market value increased from 84% in 2010/11 to 90% in 2011/12 (£182m in total). This was led by social banks who invested almost entirely in secured loans, meeting their requirement to invest customer deposits for a predictable return;
- Unsecured lending saw a reduction in total value from 2010/11 and accounted for 5% of the market (compared to 11% in 2010/11) and just over £10m;
- Large SIFs provided the greatest amount of unsecured lending as part of a broad range of products, though secured loans still accounted for half of their investment;
- Quasi-equity/equity-based investments accounted for less than 3% of the social investment market value in 2011/12, down in actual value and proportion (from 5%) of the market in 2010/11. There were just over 40 quasi-equity and equity-based investments in 2011/12, worth around £5m in total;
- Small SIFs as a group had the greatest diversity in their investment portfolio, with almost 40% of investments taking the form of equity investments, and a further 17% taking the form of Social Impact Bonds; and
- The majority of SIFs (89% of respondents) expected to increase their investments in social ventures over the next two to three years.

1.2.2 Economic impact

This report presents the first ever robust analysis of the economic impact of the UK social investment market, over the financial year period April 2011 to March 2012. A total of 99 recipients of social investment – social ventures – provided data for this analysis. An overview on the characteristics of the social ventures surveyed is provided in section 5.2.

The economic impact analysis was carried out in accordance with HMT Green Book guidance (see Annex two), and at both a national and regional level. An assessment of both gross and net 'additional' economic impact is provided, such that the economic impact which is measured is truly additional.

Though important, the economic impact analysis figures need to be considered alongside the fact that the driving purpose for social ventures is to generate social impacts. These impacts also generate financial and social returns.

1.2.2.1 Gross economic impact

Gross economic impact is the impact reported by businesses *before* taking into account additionality considerations (deadweight, displacement, leakage and multipliers).

At the gross level, over their lifetime, the 765 investments will result in the creation or safeguarding of:

- **340 social ventures;**
- **6,870 FTE jobs;**

- **£58m** in annual Gross Value Added (GVA) contribution to the UK economy; and
- 220 social ventures were prevented from closure by the 765 investments provided by SIFIs (gross). 1,840 jobs (gross) were subsequently preserved.

1.2.2.2 Net economic impact (additional)

Net additional economic impact takes account of deadweight ('would it have happened anyway without this investment'), displacement ('did you just replace a local competitor'), leakage ('was some of the economic impact of your activity felt outside the target area') and economic multiplier effects ('did the economic impact stay in the area and get re-spent again...and again'). This allowed a calculation of the truly additional contribution of the social investment to the economy. For example, it could be said that the financial returns generated by a social venture could have just as easily been produced by a local competitor and therefore, these returns would not be considered truly additional to the economy, as they would have happened in any case, with or without the SIFI investment.

As the net figures take into account additional economic activity, they will generally be substantively lower than the gross level figures. Spatial scale is a key consideration within an economic impact assessment, since the additional factors described above vary depending on the geographic unit of analysis.

At a regional level, displacement was relatively high (social ventures serve local and regional markets rather than, say, being exporters of goods and services). The 'flip-side' of this, however, is that supply chains also tend to be local and regional, which adds to the economic multiplier of expenditure in the regional economy.

The net additional economic impact generated by SIFI investments at a regional scale were:

- **210 social ventures** created/safeguarded;
- **3,550 FTE jobs** created/safeguarded over the whole finance period; and
- **£23m** in *annual GVA* contribution at the regional economy level.

At the level of the UK economy as a whole, net additional economic impact is much reduced, primarily due to the very high level of displacement, since social ventures mostly compete with other UK businesses.

- **30 social ventures** were created/safeguarded;
- **610 net additional FTE jobs** were created/ safeguarded; and
- Some **£4m** of net additional *annual GVA* was added to the UK economy.

The value of the social investment required to generate one unit of net additional economic impact:

- A social investment of just over £10,000 achieves one net additional national FTE job. A three year social investment of £10,000 would generate almost £19,000 net additional GVA in the national economy over the three year period.
- At the level of the regional economy, the economic impact of social investment is substantially greater. For example, the same three year social investment of £10,000 would generate almost six net additional FTE jobs and over £110,000 net additional GVA in the region.

1.3 What are the implications of these findings?

This report clearly demonstrates the value of the social investment market, not just in social terms but also the economic benefits, by undertaking a robust economic impact analysis for the first time. This additional economic impact for the UK economy needs to be considered alongside the wide-ranging social benefits the market delivers.

Notwithstanding the growth of almost a quarter in social investment totals in 2011/12, SIFIs reported that they met only around half of expressed demand by social ventures. Almost all SIFIs continued to report their plans to grow investment, with half planning to partly achieve this through the launch of new products.

While it is clear that not all expressed demand equates to investible propositions, failure to meet such demand implies the loss of a substantial range of social benefits and impacts, and reduced economic growth in the UK economy. There is potential for more funding provision for the many smaller SIFIs, which offer unsecured lending products, to help these SIFIs extend their reach to a wider range of social ventures. There are also new types of funding source available for social ventures to access.

However it is important to be aware that growth constraints on the development of the social investment market remain.

Previously, *Lighting the touchpaper* reported that the quality of investment propositions brought forward by social ventures remained a substantial barrier to market growth, alongside the 'distortive' effect of grants and 'soft' finance in 'crowding out' social investments. However, in the absence of sufficient identified high risk unsecured social investment, grants are in effect playing this role, possibly unintentionally and without an investment mindset. It is therefore important to investigate the way in which grants can be best used to help bridge this finance gap, for the growth of social ventures, without creating artificial dependency.

These two issues continue to be the top two constraints in the social investment market identified by SIFIs in 2011/12. At an individual organisational level, these constraints were reflected in SIFIs reporting high transaction costs as the top developmental constraint, followed jointly a lack of attractive investment opportunities and variable commissioning practice by Government.

In recognition of this, each of the commissioner organisations are actively involved in on-going support for the UK social investment market, through a range of initiatives and funding arrangements.⁸

⁸ For more information on current activities by Big Lottery Fund, Big Society Capital, City of London Corporation, and Her Majesty's Government, see back cover.

2 Introduction

In January 2013, Big Lottery Fund, Big Society Capital, City of London Corporation and Her Majesty's Government commissioned ICF GHK Consulting, in association with BMG Research, to assess the size and characteristics of the UK social investment market as of 31st March 2012, and its economic impact.

2.1 Growing the social investment market

In 2012 there were an estimated 180,000 SME social enterprise employers in the UK⁹, rising to 688,000 when including sole traders¹⁰, developing innovative and sustainable ways to deliver goods and services and tackle some of our most entrenched social problems. They are creating jobs, employing around two million people in 2012 and contributing some £55bn to the UK economy¹¹, bringing wealth into communities and helping to rebuild the economy¹².

It is generally accepted among social ventures¹³, Government, the European Commission¹⁴ and stakeholders that social ventures would be able to achieve more – expanding existing goods and services, taking up new opportunities and reaching scale – if they had access to the finance they require ('social investment'). Most recently, for example, CDFA/RBS Group estimated the potential funding gap for social ventures to be in the order of £1.3bn and £2.1bn per annum¹⁵.

What is social investment?

Social investment is the provision and use of repayable finance to generate social as well as financial returns. Social investment may occur in a variety of forms (or products) such as loans, equity and bonds.

Social returns are improved outcomes for society and range substantially – from, for example, improved individual health to employability amongst disadvantaged groups, to provision of community goods and services, to the community impact of reduced carbon emissions.

Financial returns imply that the social investor will be able to get their

⁹ Cabinet Office (2013) *Social enterprise: market trends, based upon the BIS Small Business Survey 2012*, BMG Research, <https://www.gov.uk/government/publications/social-enterprise-market-trends>

¹⁰ Ibid.

¹¹ Ibid.

¹² See, for example, Social Enterprise UK (2011) *Fightback Britain: a report on the State of Social Enterprise Survey 2011*, http://www.socialenterprise.org.uk/uploads/editor/files/Publications/Fightback_Britain.pdf; and HMG (2013) *Social Justice: transforming lives one year on*, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/192019/CM_8606_Social_Justice.pdf

¹³ Social ventures operate across a range of markets and span a range of organisations including charities which trade, social enterprises, and community organisations. They are not defined by legal form but rather by their objective - which is to deliver social results, as opposed to that of private sector businesses which is to generate profit for owners or shareholders. Social ventures can, and do, operate in a commercial way but are distinguishable by the fact that they use the majority of any surplus generated to further their social objectives. Additionally, social ventures are independent from Government.

¹⁴ See http://ec.europa.eu/internal_market/social_business/index_en.htm

¹⁵ CDFA & RBS Group (2013) *Mind the finance gap: evidencing demand for community finance*, ICF GHK, <http://www.cdfa.org.uk/wp-content/uploads/2013/01/Mind-the-Finance-Gap-summary-report.pdf>

money back in the future with a return. By this definition, grants, donations and other funds with no expectation of being paid back are not social investments.

Social ventures operate based on business models that create both social and financial returns. Social investors expect to create social value through their investment, though the desired balance of social and financial returns will vary across different types of investor. Social investors are, therefore, usually willing to accept financial returns that are below market rates in exchange for social returns.

Social Investment Finance Intermediaries (SIFIs) predominantly attract money from social investors and use it to make direct investments into front-line social ventures. Many SIFIs also offer a range of other business support services. A major type of SIFI are social banks – defined as an organisation that takes deposits and invests these for financial and social returns.

Front-line social ventures are the recipients of social investment. They use the investment to finance their operations and activities to create the financial and social value which form the returns to investors. Examples of social ventures are social enterprises, Community Interest Companies, co-operatives and charities.

Adapted from Boston Consulting Group & The Young Foundation (2011) Lighting the touchpaper: growing the market for social investment in England. A report for Big Society Capital.

An emergent base of specialist Social Investment Finance Intermediaries (SIFIs) – including social banks and Community Development Finance Institutions (CDFIs) – has developed seeking to fill the finance gap, and the UK marketplace for social investment has grown steadily since the mid-2000s. Nevertheless, the Government's social investment strategy in 2011 identified continued barriers to growth in the social investment market including the supply of appropriate finance, the pipeline of investment ready demand, and the development of a robust and efficient market infrastructure¹⁶.

Given this, in 2012, Big Society Capital (BSC) was established as the first dedicated wholesale financier of social investment and to act as a further catalyst to market development. The commissioner organisations of this report, along with others, recognise the need for more robust up-to-date information on how the social investment market is developing, and greater clarity on the economic and social impact achieved as a result of social investment. In its 2013 update report, the Government has set targets for the UK to diversify the investor base, support more targeted investment readiness, open up the market, maximise the impact on economic growth, and drive the global agenda¹⁷. This report contributes by addressing the economic impact of the UK social investment market.

¹⁶ Cabinet Office (2011) *Growing the social investment market: a vision and strategy*, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/61185/404970_Social_investmentMarket_acc.pdf

¹⁷ Cabinet Office (2013) *Growing the social investment market: 2013 progress update*, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/205295/Social_investment_strategy_update_2013.pdf

In 2010/11, total social investment in England stood at £165m by Social Investment Finance Intermediaries (SIFIs)¹⁸.

This total was dominated by six institutions who accounted for roughly 90% of investment. Four of the six institutions were social banks – given their lending practices this meant that over 80% of investment in 2010/11 took place through secured lending.

In 2010/11, potential future growth in funds under management for the next three years was expected to be 35% per annum, representing total capital expansion in the order of £650m¹⁹. These figures form an indicative baseline comparison for this report, one year on.

2.2 Research scope and objectives

The overall aim of this research has been to provide robust data on the size, characteristics and economic impact of the UK social investment market as of 31st March 2012.

In doing so, the research aims to support the growing social investment market through the provision of an up-to-date evidence base on market developments and economic impact – and in so doing further develop the ‘business case’ for social investment across the stakeholder community.

The Terms of Reference for the research outlined five detailed objectives:

1. To identify the full scope of the UK social investment market by sector, region and type of organisation;
2. To review the size and characteristics of the UK social investment market as of 31st March 2012, and draw comparisons with the market status in 2011;
3. To identify similarities and differences in size and characteristics of the social investment market between the different regions of the UK economy;
4. To assess and provide robust statistical data on the (gross and net) economic impact in the financial year period April 2011 to March 2012 of SIFI lending activity in terms of UK jobs, businesses, turnover and Gross Value Added (GVA) created and safeguarded, with due consideration of the additional factors such as displacement, deadweight loss, leakages and the relevant multiplier effects; and
5. To provide lessons for developing the SIFI market in the future.

As a very close proxy to the UK social investment market, the research has focused on the investment activities of UK SIFIs and the broader social venture lending of Community Development Finance Institutions (CDFIs). Other market infrastructure, including business support, was not included within the scope of the research. Nor were investment contributions by Big Society Capital, launched in April 2012, included as they are beyond the timeframe of this research.

2.3 Research methodology

Alongside meetings and reporting to the commissioner organisations, the research methodology comprised:

¹⁸ Boston Consulting Group & The Young Foundation (2011) – Op Cit.

¹⁹ Ibid.

- **Stage 1 – Information and data scoping:** information was collated on the potential population of SIFIs making social investments in the qualifying period, and contact details for the social ventures within which they invested.
- **Stage 2 – Fieldwork:**
 - **A survey of SIFI social investment activity:** a total population of 141 potential SIFIs²⁰ were contacted to assess the scale and scope of their social investment activity (Annex one, available separately online²¹, provides a copy of the survey tool). In total, 29 SIFIs undertaking social investment were identified.
 - **A survey of social ventures (recipients of social investment):** undertaken through three channels (Annex one, available separately online, provides a copy of the survey tool). A telephone survey of social ventures was undertaken by BMG Research; where telephone details did not exist, social ventures were emailed an e-survey to complete by ICF GHK and, in a small number of instances SIFIs directly emailed their investee social ventures clients newsletters, etc. with a link to the e-survey. A total of 99 responses were received²².
- **Stage 3 – Data analysis:** was carried out against the objectives of the research to prepare a market assessment of the UK's social investment sector for the financial year period April 2011 to March 2012 (and in comparison with 2010/11) and a calculation of the economic impact of SIFI social investment in 2012.

2.4 Structure of this report

The remainder of this report is structured as follows:

- Section three provides a short overview of the sector;
- Section four analyses the UK market place for social investment in 2011/12, measuring its size and characteristics;
- Section five provides an overview of the economic impact of social investment, including consideration of the additionality of these benefits; and
- Section six presents conclusions.

A series of Annexes provide supporting material:

- Annex one (available separately online) provides the survey instruments used in the research;
- Annex two provides details of the economic impact assessment methodology (including additionality calculations); and
- Annex three provides a list of organisations who were engaged in the research.

²⁰ This included and extended the SIFIs contacted in the 2010/11 *Lighting the touchpaper* research.

²¹ Annex one is available to download separately at:

<http://www.cityoflondon.gov.uk/business/economic-research-and-information/research-publications/Pages/default.aspx>

²² A response rate of 49% of eligible contacts was achieved for the telephone survey and around a third for the ICF GHK online survey. Where SIFIs notified their clients directly, the precise response rate is unknown but an informed estimate suggests it was lower.

3 UK Social Investment Finance Intermediaries, 2011/12

This section of the report presents an overview of key features of the SIFI sector in the UK in the financial year period April 2011 to March 2012. Themes covered include: size and organisational characteristics, investment services offered and their geographical coverage, and the external sources of funds and finance for SIFI activities.

3.1 The UK SIFI population

3.1.1 SIFIs undertaking social investment, 2011/12

The survey methodology was designed to produce a comparative data set to that produced in the 2010/11 *Lighting the touchpaper* assessment of social investment²³. It should be noted, however, that this update survey covered all of the UK and not just England and was more extensive in its initial search for any organisations engaged in social investment in 2011/12.

This research included contacting all of those organisations in the previous *Lighting the touchpaper* research and includes responses from all of the largest organisations. Nevertheless, the two samples are not totally comparable. This report, therefore, has taken great care in any individual comparisons between the two samples – closely assessing such comparisons and the robustness of messages produced from a generally conservative standpoint.

In February 2013, all UK organisations who were known to have a potential interest in social investment activity (whether as investors and/or intermediaries) were contacted/surveyed to confirm any social investment activity in frontline social ventures in the period April 2011 to March 2012.

In total, 141 organisations were contacted. Of these:

- A total of 80 organisations confirmed that they were not social investors in the period 2011/12; and
- A further five organisations had withdrawn from the market or ceased trading since 2010/11²⁴.

Of the remaining 56 organisations, no confirmation of activity was received from 27 organisations. In the vast majority of these cases, it is believed that they were not active social investors in 2011/12 and, of the few that were, only limited investment activity had taken place (if any, less than five investments per year). These 27 organisations were therefore not included in the research.

29 UK SIFIs were confirmed as actively investing in 2011/12.

This included social banks, Community Development Finance Institutions (CDFIs) and other Social Investment Finance Intermediaries (SIFIs).

In comparison, *Lighting the touchpaper* identified 24 organisations who had undertaken at least one social investment in the period 2010/11 in England (see sections 3.3 and 4.3 for the geographical distribution of investments).

²³ Boston Consulting Group & The Young Foundation (2011) – Op Cit.

²⁴ This is due to a mix of mergers, ceased trading and decisions to exit the social investment market.

3.2 Organisational characteristics of SIFIs who made social investments

3.2.1 Organisational form

Of the 29 social investors identified:

- Four were social banks, defined as an organisation that takes deposits and invests against a social mission;
- Nine were SIFIs with annual investments over £1m; and
- There were a total of 16 SIFIs with annual investments under £1m (including one mainstream bank).

Of these 29 organisations, 19 are Community Development Finance Institutions (CDFIs).

3.2.2 Legal form

The SIFIs have a large variety of legal forms ranging from Trusts, to Companies Limited by Guarantee (with or without charitable status), Industrial and Provident Societies, Companies Limited by Shares, Community Interest Companies and Limited Liability Partnerships.

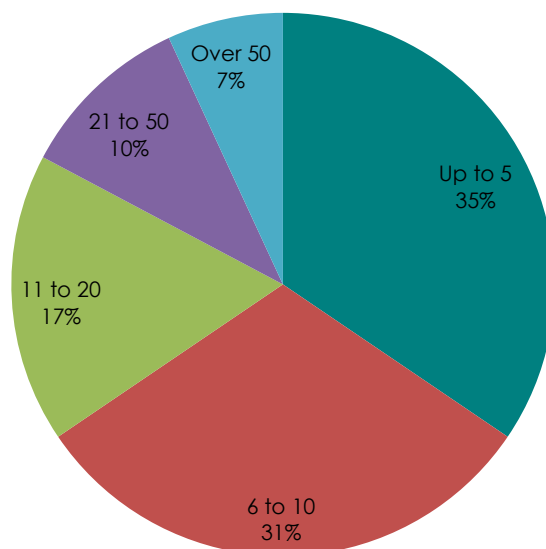
3.2.3 The number of employees at SIFIs

SIFIs were asked how many people were employed in their organisations (Figure 3.1). Consideration was taken of those instances where social investment comprises only a small part of the business activity of the organisation.

In 2011/12, total numbers employed across 29 SIFIs equalled around 430 FTE individuals. In almost 70% of cases, SIFIs employed up to 10 individuals – but none employed less than two.

A like-for-like comparison for a sub-sample of SIFIs across the years 2010/11 and 2011/12 found an average annual increase of just less than one additional FTE position per SIFI.

Figure 3.1 The number of people employed at SIFIs who make social investments (full time equivalent – FTE), 2011/12



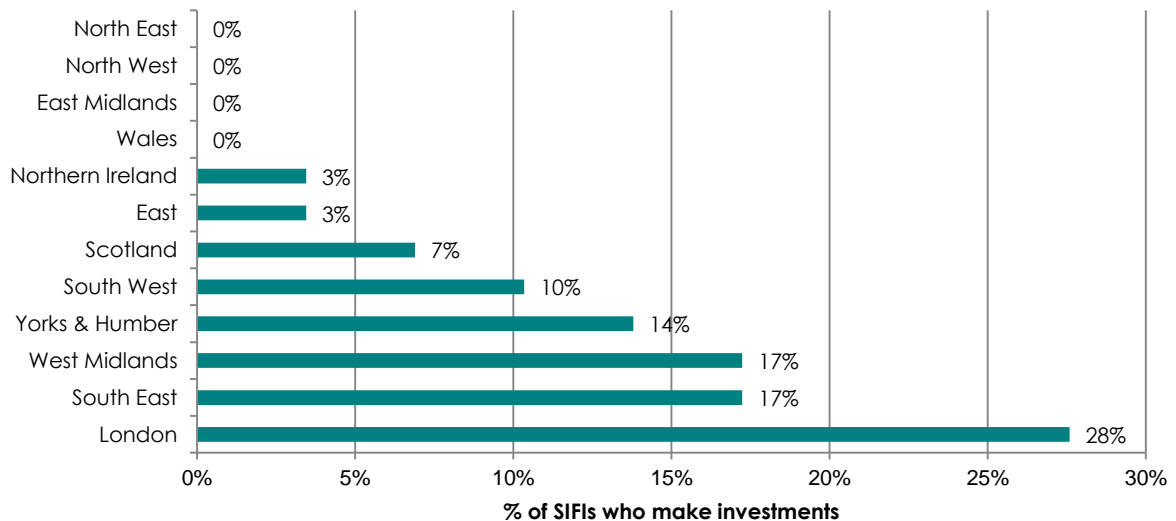
Note: FTE calculated on the basis that one part time position is equal to 0.5 FTE. Base = 29 SIFIs.

3.3 The geographical footprint of SIFIs

3.3.1 The location of investing SIFIs

For the first time, the location of the headquarters of all 29 SIFIs that were known to make investments during 2011/12 was mapped (Figure 3.2).

Figure 3.2 The location of the headquarters of the 29 SIFIs who made investments, 2011/12



In total:

- Just over a quarter of all organisations were headquartered in London, and just under half of all social investors were centred in either London or the South East;
- West Midlands, Yorkshire and Humber and South West all had a handful of SIFIs each headquartered in their region (between three and five SIFIs); and
- No SIFIs reported they had headquarters in the North East, North West, East Midlands or Wales²⁵.

3.3.2 The geographical coverage of SIFIs

SIFIs were asked about the geographical scale of their investment activity (i.e. where they were prepared to invest). Figure 3.3 shows the proportion of SIFIs who were local (only invested in a single Local Authority area), regional (only invested in a single region/Devolved Administration), national (invested in more than one region/Devolved Administration or UK-wide), or international (invested in UK and at least one other country).

²⁵ Although it is believed that maybe one or two SIFIs (if not actual social investors in 2011/12) do exist in each of these regions.

Figure 3.3 Where SIFIs were prepared to make social investments, 2010/11 and 2011/12



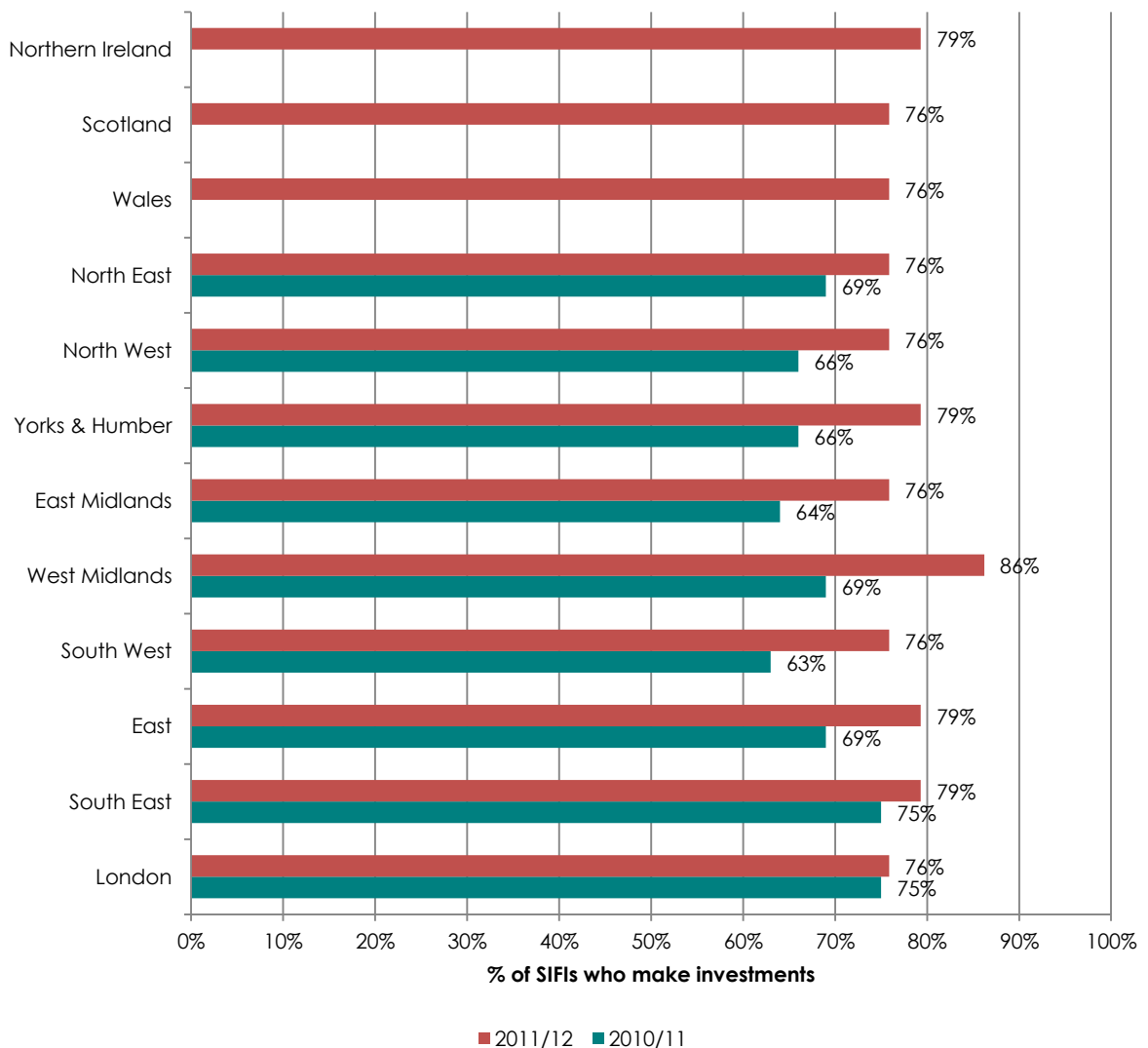
2010/11 source: *Lighting the touchpaper*; 2011/12 source: ICF GHK survey. Base = 29 SIFIs.

Figure 3.3 highlights that, within the UK, the geographical scale of planned SIFI investment is growing in size – from local to regional and from regional to national. Intentions to invest internationally have, however, reduced slightly²⁶.

Figure 3.4 shows the proportion of SIFIs in 2011/12 who were prepared to invest in each of the UK regions/Devolved Administrations (note that this is not the actual geography of social investments – instead see Figure 4.5 later). Comparison is made with available data for 2010/11 (England only).

²⁶ It should be noted, however, that sample numbers are very small at this level of disaggregation and therefore cannot be applied to the SIFI population more generally.

Figure 3.4 The proportion of SIFs who were prepared to invest in each of the English regions (2010/11 and 2011/12), and the Devolved Administrations (2011/12 only)



2010/11 source: *Lighting the touchpaper*; 2011/12 source: ICF GHK survey. Base = 29 SIFs.

Key points of note are:

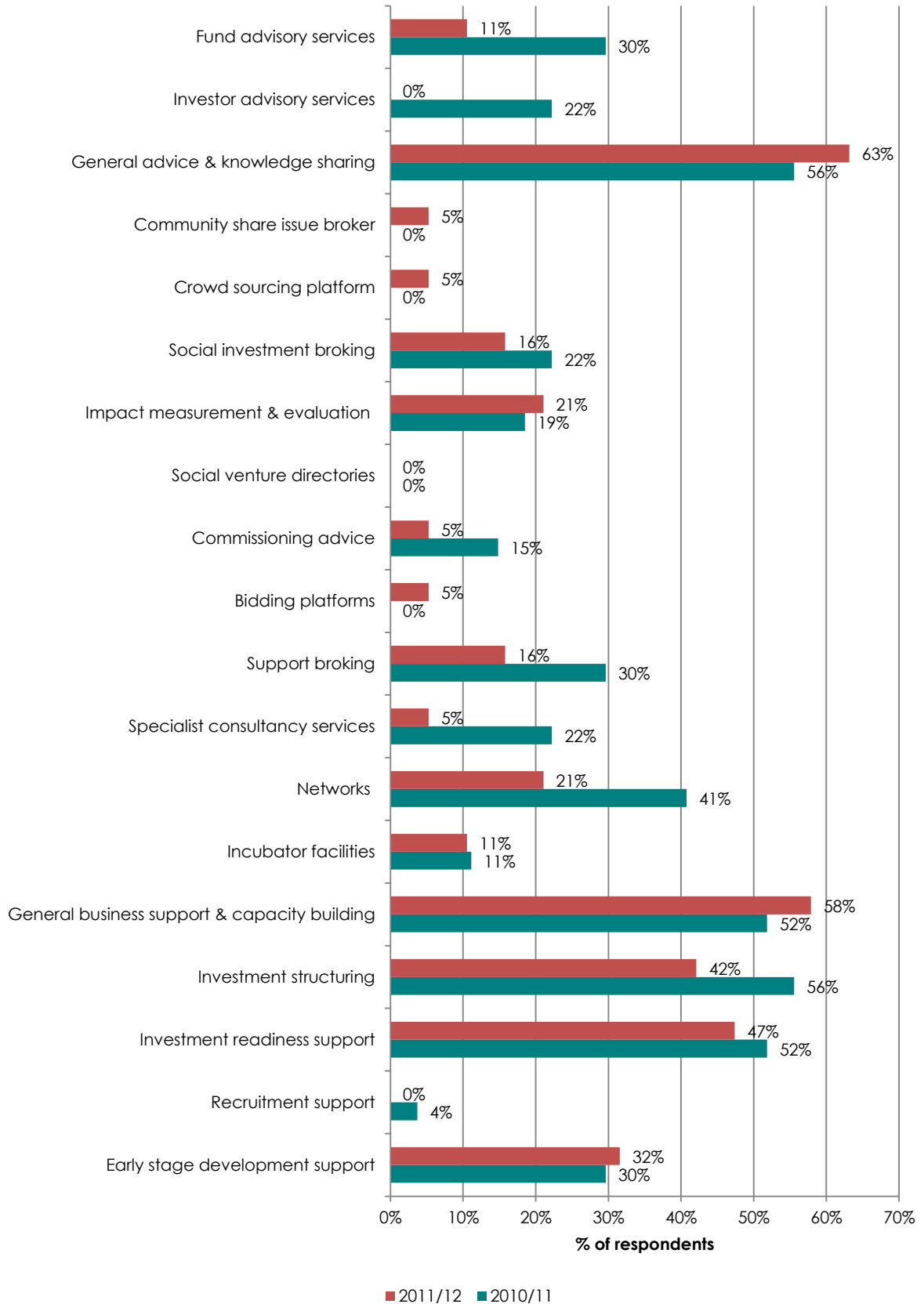
- Two thirds of SIFs who made investments in 2011/12 operated UK-wide and each of the Devolved Administrations is served by at least three quarters of the SIFs;
- Coverage across the English regions improved slightly between 2010/11 and 2011/12. In 2010/11, the least-served English regions had around two thirds of SIFs willing to invest within them; by 2011/12 none of the English regions were served by less than three quarters of SIFs; and
- The West Midlands was the most-served UK region, with just over 85% of all SIFs indicating that they would invest there (a combination of the nationally-oriented SIFs together with a handful of SIFs that only invested in the West Midlands).

3.4 Products and services offered

Alongside direct social investment, Figure 3.5 shows the proportion of SIFIs who reported that they offered a selection of other types of product and services:

- As in 2010/11, in 2011/12 all SIFIs reported that they offered at least one product or service in addition to direct social investment;
- In 2011/12, just under two thirds of SIFIs provided some form of generic advice and knowledge sharing to social ventures, and over half provided business support and capacity building. There were no clear patterns by type of SIFI and these proportions were similar to those reported in 2010/11;
- Similarly, just under half of SIFIs offered investment readiness advice in 2011/12, as was the position in 2010/11;
- In contrast, the most noticeable shift over the period 2010/12 is the reduction of various forms of advisory and broking services; and
- Provision of recently emergent products and/or new forms of delivery was low, with just 5% of survey respondents (equal to one organisation) reporting that they operated crowd sourcing or bidding platforms. Nevertheless, in 2010/11 none of the SIFIs reported providing either of these services.

Figure 3.5 The proportion of SIFs who offered selected non-investment products and services, 2010/11 and 2011/12



2010/11 source: *Lighting the touchpaper*; 2011/12 source: ICF GHK survey. Base = 19 SIFs.

3.5 Sources of finance

3.5.1 External finance accessed by SIFs who made social investments in 2011/12

Investing SIFs in 2011/12 were asked to indicate the sources of external finance that they accessed.

An increasing diversity of sources of finance for on-lending was evident compared to 2010/11, although exact figures remain elusive due to confidentiality issues. Deposits at the social banks remain core finance sources and there was evidence of Trusts and Foundations continuing to experiment in the social investment market, alongside nascent signs of individual and angel investment into SIFs. In addition, Big Society Capital (through the interim Big Society Investment Fund) was beginning to emerge.

SIFs had also been successful in accessing commercial funding from mainstream banks (not social banks). In the majority of cases, however, commercial funding had not been sought as current sources of funding were sufficient and/or organisations were restricted by their legal form.

Virtually all investment sources were UK-based and very few SIFs suggested that they expected to access overseas funding in the next two years.

While responses to this question were limited, it can be seen that Government funds were no longer dominant in the profile of investment sources. Where Government did have a high profile, it was as a source of revenue (not capital) alongside other non-departmental public bodies, Trusts and Foundations. In addition, the use of reserves to support revenue and capital finance was notable amongst a number of SIFs.

3.6 Summary

- A growing number of organisations are involved in the social investment market. Actual SIFs *undertaking social investments in one year* was around 30 organisations.
- In 2011/12, this group of SIFs was led by four large social banks, followed by nine SIFs who invest more than £1m per annum. Two thirds of the investing SIFI population classify themselves as Community Development Finance Institutions (CDFIs).
- Just over a quarter of investing SIFs are headquartered in London and half in London and the South East.
- The Devolved Administrations and English regions are served by at least three quarters of investing SIFs, reflecting that the majority of SIFs serve national markets. Virtually no SIFs invest just locally and very few SIFs invest internationally.
- Most SIFs offer a variety of business support, capacity building and investment readiness activities alongside direct investments.
- There is evidence of a growing diversity of sources of finance for SIFs – including the emergence of individual and angel investor types – alongside the still dominant social banks (using deposits).

4 The UK social investment market in 2011/12

This section of the report presents an overview of key features of the social investment market in the UK in 2011/12. Based on the SIFI survey, and continuing a simple segmentation of SIFIs based on type and investment size, themes covered include the value and volume of social investment, types of investment undertaken, and the geography, sector and social outcomes of lending.

SIFI experience of market demand, trends in investment volumes, constraints and sustainability are also considered.

4.1 The value and volume of the UK social investment market

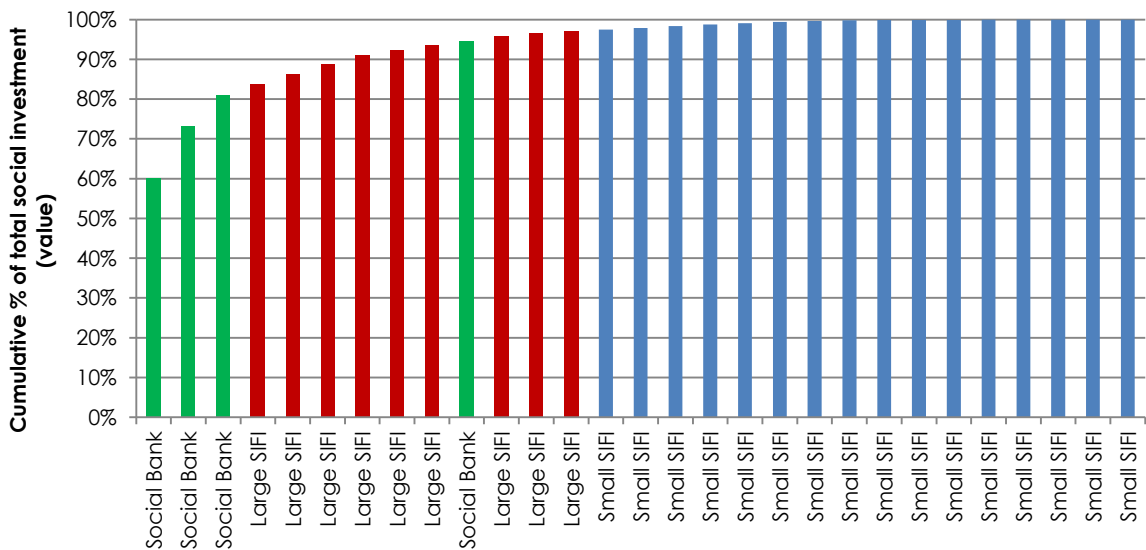
4.1.1 The value of the UK social investment market

In 2011/12, the value of social investments in the UK market reached £202m.

This compares with a figure of £165m of investment in England in 2010/11, identified in *Lighting the touchpaper*²⁷.

The 29 SIFIs making social investments in 2011/12 ranged from social banks, through all sizes of CDFI, to small investment funds (Figure 4.1).

Figure 4.1 Cumulative share of total social investment (by value) for SIFIs who make social investments, 2011/12



Base = 29 SIFIs.

²⁷ Notably, this growth in social investment may be set against figures for bank lending to SMEs during the same period. Whilst bank lending values, at over £70bn, swamp those of social investment, SME lending by banks during this period contracted in comparison to social investment growth (see, for example, <http://www.bankofengland.co.uk/publications/Pages/other/monetary/additionaldata.aspx>).

Figure 4.1 illustrates that:

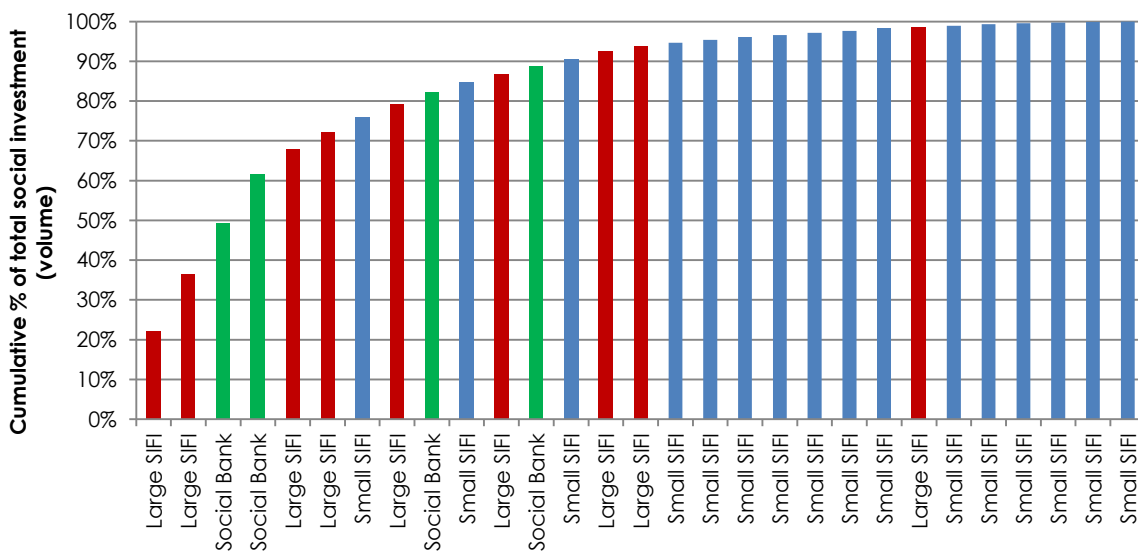
- The market remains highly concentrated. The three largest organisations accounted for 81% of total investment (by value) in 2011/12, and seven organisations accounted for 91% of investment;
- The four social banks accounted for 82% of total investment, up from 70% of the market in 2010/11. Indeed, 2011/12 investment by the four social banks matched the size of the whole social investment market reported in 2010/11;
- After the social banks, the nine large SIFIs (2011/12 investment greater than £1m), accounted for 15% of the social investment market (by value), equivalent to £30m; and
- The 16 small SIFIs (2011/12 investment under £1m) have experienced significant growth in line with the market (an increase of almost a quarter from 2010/11), but still only accounted for 3% of total social investment (just over £6m of investment).

4.1.2 The volume of the UK social investment market

In 2011/12, 765 social investments were made by SIFIs²⁸.

Compared to the value of investment, the number of social investments was slightly less concentrated – though eight SIFIs still accounted for almost 80% of all deals in 2011/12 (see Figure 4.2).

Figure 4.2 Cumulative share of total social investment (by the number of investments) for SIFIs who made social investments, 2011/12



Base = 29 SIFIs.

²⁸ No comparable figure exists for 2010/2011.

Table 4.1 Value and volume of the UK social investment market, 2011/12, by SIFI type

Type of SIFI	Total value of investments	% of total value of investments	Total no. of investments	% of total no. of investments	Average investment size	Range of no. of investments
Social bank	£166m	82%	229	30%	£723K	15 to 97
Large SIFI	£30m	15%	427	56%	£71K	3 to 170
Small SIFI	£5m	3%	109	14%	£56K	1 to 30
All investors	£202m	100%	765	100%	£264K	1 to 170

Base = 29 SIFIs.

It can be seen that the:

- Four social banks accounted for 82% of the market by value, but only 30% of the total number of investments. This implies an average investment size of circa £723,000. None of the social banks made more than 100 investment deals in the year;
- Nine large SIFIs accounted for 15% of the market by value and 56% of the total number of investments. This implies an average investment size of circa £71,000. A total of eight of the nine large SIFIs made more than 10 investment deals in the year 2011/12, and two of the nine large SIFIs made over 100 deals; and
- 16 small SIFIs accounted for 3% of the market by value and 14% of the total number of investments. This implies an average investment size of circa £56,000. Investment deals done ranged from one a year to 30 a year (with 10 of the 16 undertaking less than five deals a year).

4.2 Types of social investment product

As the financial and business needs and legal structures of social ventures differ to those in the mainstream, products are often adapted and structured to meet the sector's specific requirements. The main types of social investment are outlined in the box below.

Types of social investment product

Debt finance usually takes the form of loans, both secured and unsecured, as well as overdrafts and standby facilities. Generally these require a borrower to repay the amount borrowed along with some form of interest, and sometimes an arrangement fee.

Secured loans or mortgages take security over a property or asset. This may be the property or asset that is being bought with the loan itself, or other assets held by the organisation. If an organisation defaults on its debt, the lender can sell the asset to recoup its loan.

Unsecured loans do not take security over an organisation's assets. Because the risk for the lender is greater, interest rates are usually higher than for secured loans. Unsecured loans are generally the most needed form of repayable capital for social sector organisations, because few of

them have enough assets to use as security.

Equity investment usually takes the form of shares issued to an investor in exchange for capital. Unlike debt, equity finance is permanently invested in the organisation. The organisation has no legal obligation to repay the amount invested or to pay interest. Equity investors usually invest in organisations that they believe will grow. In return they expect to receive dividends paid out of the organisation's earnings and/or capital gain on the sale of the organisation or on selling their shares to other investors.

Quasi-equity investment: Sometimes debt financing is inappropriate for social sector organisations, especially in the high risk start-up phase. Equally, equity investment may not be possible if the organisation is not structured to issue shares. A quasi-equity investment allows an investor to benefit from the future revenues of an organisation through a royalty payment which is a fixed percentage of income. The investor may, however, gain nothing if the organisation does not perform. This is similar to a conventional equity investment, but does not require an organisation to issue shares.

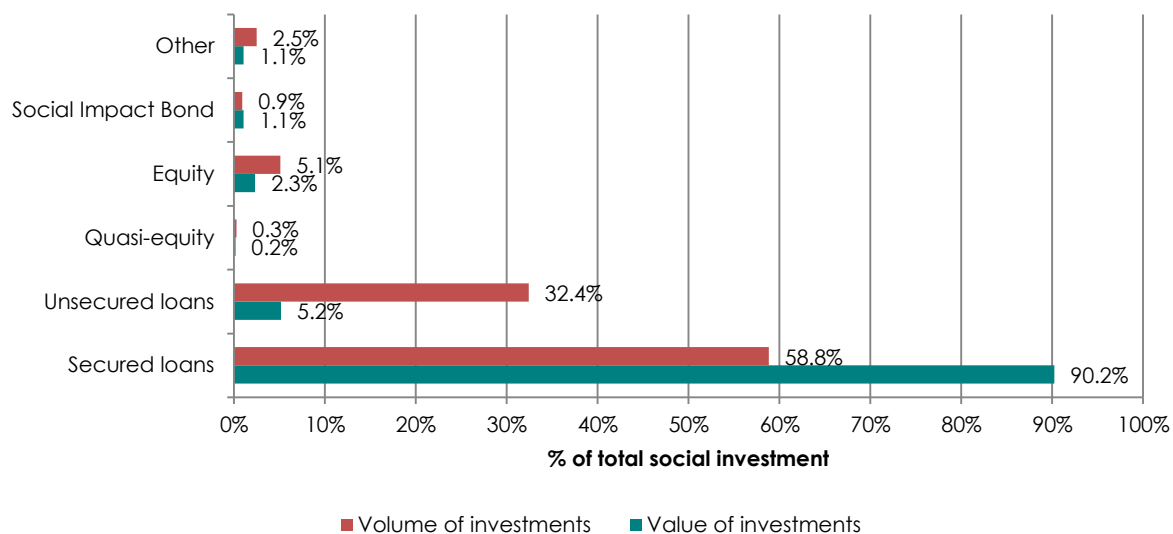
Social Impact Bond is a form of outcomes-based contract in which public sector commissioners commit to pay for improvement in social outcomes (such as a reduction in offending rates, or in the number of people being admitted to hospital) which deliver a saving to the public purse. The expected public sector savings are used as a basis for raising investment for prevention and early intervention services that improve social outcomes. Social Impact Bonds (SIBs) are not bonds in the conventional sense. While they operate over a fixed period of time, they do not offer a fixed rate of return. Repayment to investors is contingent upon specified social outcomes being achieved. In terms of investment risk, Social Impact Bonds are more similar to that of an equity investment.

Adapted from <http://www.bigsocietycapital.com/what-social-investment>

4.2.1 Types of social investment product by value and volume

Figure 4.3 shows the proportion of investment (by value and volume) by types of social investment product:

Figure 4.3 Types of social investments in 2011/12 (as a proportion of total value and total volume of all investments)



Base = 29 SIFs.

Looking at Figure 4.3 and data on 2010/11 from *Lighting the touchpaper*, it can be seen that:

- Secured loans as a proportion of the total market (by value) increased from 84% in 2010/11 to 90% in 2011/12 (£182m in total);
- Unsecured lending has seen a reduction in total value since 2010/11 and now accounts for 5% of the market (compared to 11% in 2010/11) and just over £10m;
- Quasi-equity and equity-based investments accounted for less than 3% of the total social investment market (by value) in 2011/12, down from 5% of the market in 2010/11. Quasi-equity investments recorded the largest drop: from 3% of the market in 2010/11 to just 0.2% of the market in 2011/12;
- There were just over 40 quasi-equity and equity-based investments in 2011/12, worth around £5m in total; and
- *Lighting the touchpaper* did not report on the Social Impact Bonds (SIBs) issued in 2010/11. Data from the 29 responding SIFs identified six SIB investors, who invested in seven of the SIBs created in 2011/12. The reported total value of just over £2m (equal to 1% of the market) appears to under-report the total social investment required from existing Social Impact Bonds.

Table 4.2 Types of social investments in 2011/12 (value and as a proportion of total value invested), by category of social investor

Type of investor	Secured loans	Unsecured loans	Quasi-equity	Equity	Social Impact Bond	Other	Total
Social bank	£165.5m	£0.3m	£0.0m	£0.0m	£0.0m	£0.0m	£165.8m
Large SIFI	£15.6m	£8.8m	£0.1m	£2.6m	£1.1m	£2.1m	£30.3m
Small SIFI	£1.3m	£1.4m	£0.2m	£2.1m	£1.0m	£0.0	£6.1m
All investors	£182.4m	£10.5m	£0.3m	£4.7m	£2.1m	£2.1m	£202.2m
Social banks	99.8%	0.2%	0.0%	0.0%	0.0%	0.0%	100%
Large SIFIs	51.5%	29.0%	0.4%	8.5%	3.6%	7.0%	100%
Small SIFIs	21.9%	22.7%	3.3%	34.9%	17.1%	0.1%	100%
All investors	90.2%	5.2%	0.2%	2.3%	1.1%	1.1%	100%

Base = 29 SIFIs.

In summary:

- Social banks invest almost entirely in secured loans, meeting their requirement to invest customer deposits for a predictable return;
- Large SIFIs provide a broad range of products, although secured loans still accounted for half of investment, with almost a third of investment by these organisations made up of unsecured lending; and
- Small SIFIs as a group had the greatest diversity in their investment portfolio, with almost 40% of investments taking the form of equity investments, and a further 17% taking the form of Social Impact Bonds.

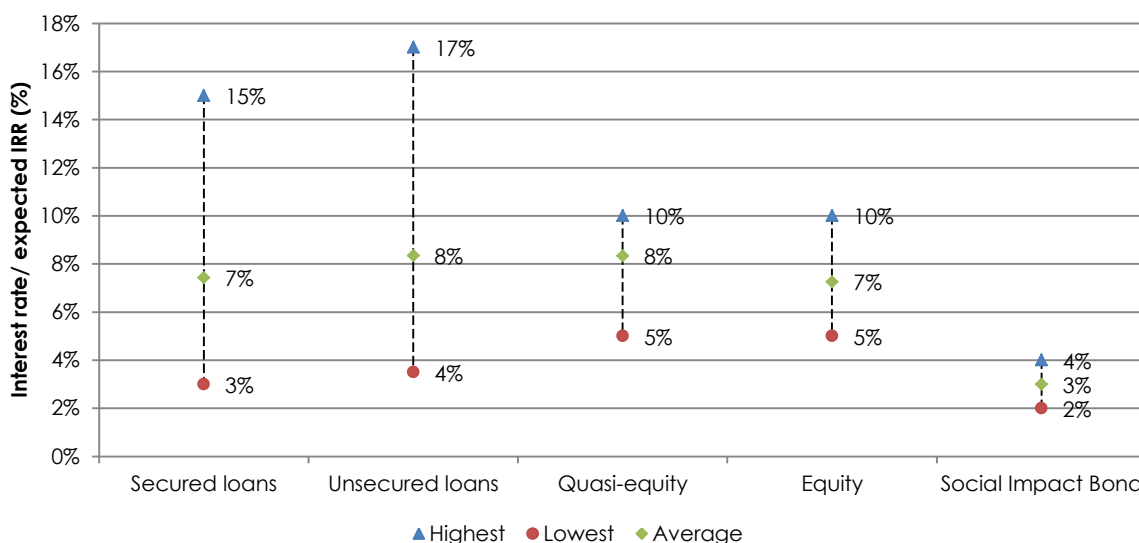
4.2.2 Interest rates and expected internal return on investment from social investments

Responses were received from 14 SIFIs on expected rates of return with some, on the face of it, surprising results (see Figure 4.4).

Average expected returns by investment type are surprisingly similar across all investment types, at 7% to 8%, with no strong differentiation between secured and unsecured loans and between debt and equity. The exception is Social Impact Bonds with an expected Internal Rate of Return (IRR) of 3%, though it should be noted that this data relates to just two SIFIs, and should thus be treated with caution. Nevertheless, there is a substantial range in returns across product providers.

It is notable, however, that these findings are not entirely out of line with those in *Lighting the touchpaper* which noted the immaturity of the market, the wide variation in expected returns and the substantially different risk/return calculations being undertaken within and across products.

Figure 4.4 Highest, lowest and average interest rate charged (loans) and expected IRR (quasi-equity, equity and SIBs), 2011/12



Base = 14 (secured loans); 13 (unsecured loans); 3 (quasi equity); 4 (equity); 2 (SIB) SIFIs.

Where data allowed, further analysis by SIFI type (Table 4.3) does show that social banks charged the lowest average interest rates on loans, while small SIFIs charged the highest interest rates.

Table 4.3 Average interest rate charged on secured and unsecured loans by different types of SIFI, 2011/12

Type of SIFI	Average interest rate charged	
	Secured loans	Unsecured loans
Social bank	6.5%	7.5%
Large SIFI	7.1%	7.6%
Small SIFI	7.9%	9.3%
All investors	7.4%	8.3%

Base = 29 SIFIs.

4.2.3 Demand for social investment

For the year 2011/12, SIFIs were asked to indicate the proportion of requests for social investment that they had received and that they were able to meet (Table 4.4). In two thirds of cases, SIFIs reported that they were able to meet less than half of expressed demand for social investment. None of the SIFIs met more than 70% of their prospective customers' requests for social investment.

Whilst sample sizes are small, data suggest that large SIFIs are able to meet more requests for finance than small SIFIs. Some 43% of large SIFIs were able to meet at least half the request for finance that they received, whereas only 25% of small SIFIs were able to meet the majority of the requests they received.

Table 4.4 The proportion of requests for social investment that were met by different types of SIFI, 2011/12

Type of SIFI	% of requests for investment that are met									
	0-10%	11-20%	21-30%	31-40%	41-50%	51-60%	61-70%	71-80%	81-90%	91-100%
Social bank	0%	0%	0%	0%	0%	100%	0%	0%	0%	0%
Large SIFI	14%	14%	14%	14%	0%	29%	14%	0%	0%	0%
Small SIFI	0%	13%	13%	13%	38%	25%	0%	0%	0%	0%
All investors	6%	13%	13%	13%	19%	31%	6%	0%	0%	0%

Base = 1 (social bank), 7 (large SIFI), 8 (small SIFI).

4.3 The geography, sector and expected outcomes of social investments

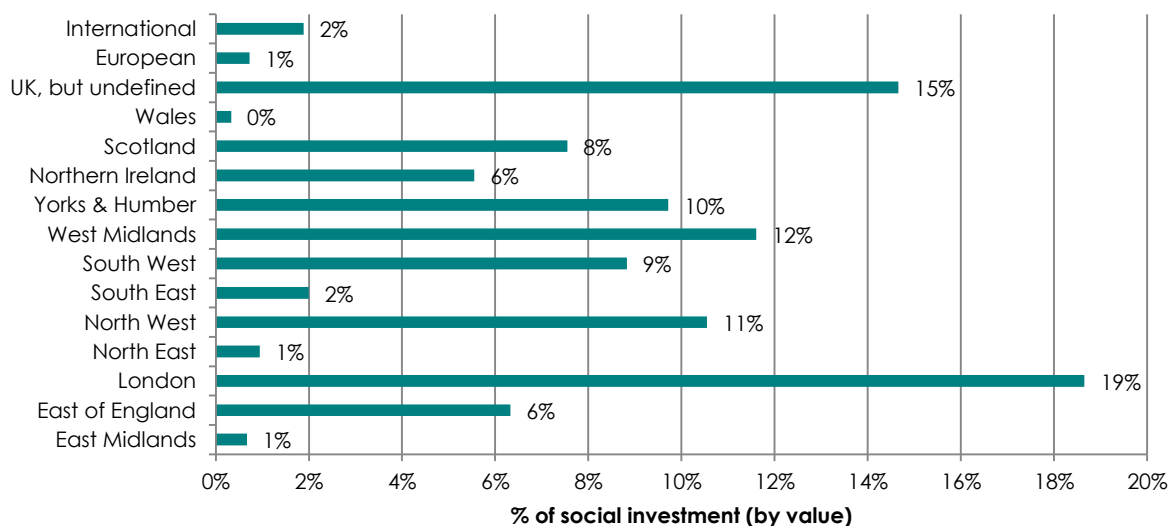
4.3.1 The geography of social investment

Figure 4.5 provides some indication from the available data of the regional geography of social investment in the UK.

It suggests that, while all regions are covered through the presence of national providers (see Figure 3.4), the actual distribution of investment varies substantially by region/Devolved Administration (though note that some SIFIs did not provide a regional disaggregation of their investments and so these results should be treated with caution).

The greatest concentration of social investment is in London, which accounted for 19% of total investment by the sample of 18 SIFIs who answered this question. Some 3% of investments were made outside of the UK.

Figure 4.5 The geography of social investment (by value), 2011/12



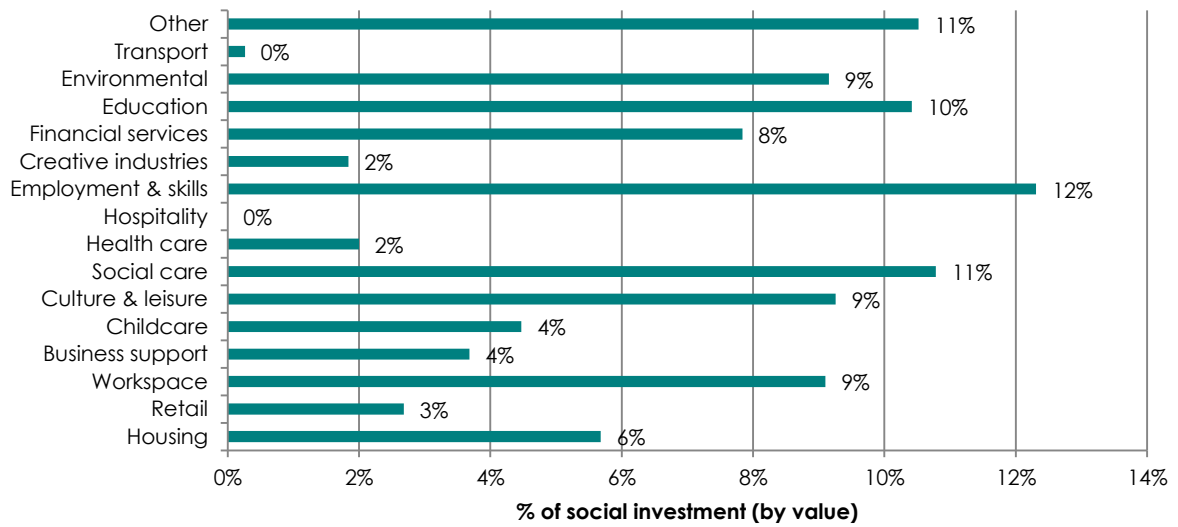
Base = 18 SIFIs.

4.3.2 The sectors of social investment

Figure 4.6 provides an overview of the sectors in receipt of social investment by SIFIs in 2011/12. No sector accounted for more than 12% of investment by SIFIs, highlighting the diversity of the sectoral distribution of SIFI investment. Sectors with

between 8% to 12% of investment included: environmental, education, financial services, employment and skills, social care, culture and leisure, and workspace.

Figure 4.6 The sectors of social investment (by value), 2011/12

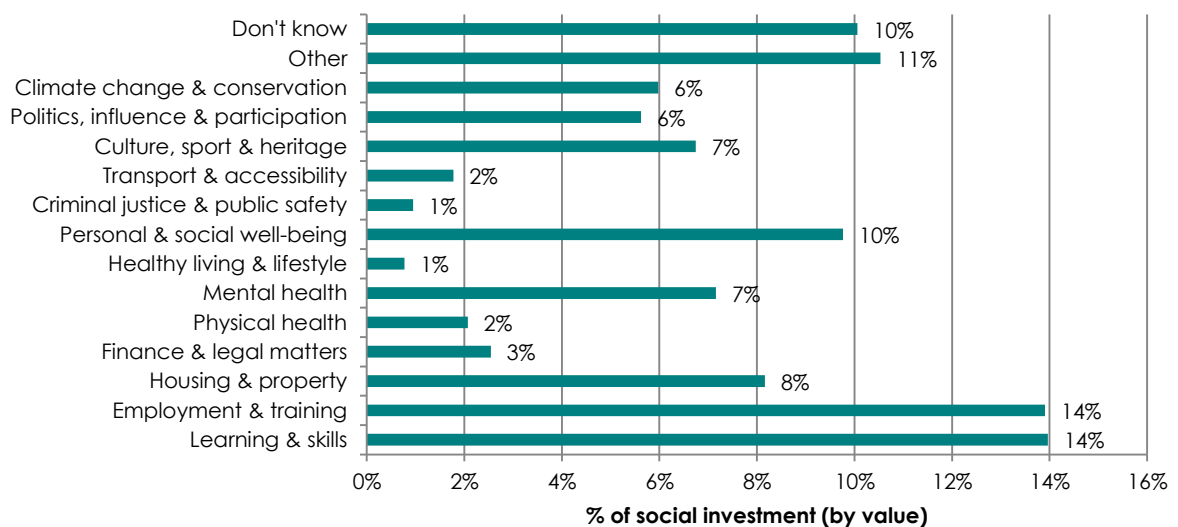


Base = 18 SIFs.

4.3.3 The expected outcomes of social investments

SIFs were asked to estimate the proportion of social and environmental outcomes generated by their social investments (Figure 4.7). Learning and skills, and employment and training were identified as the two commonest outcomes of social investments (just over a quarter of investment was expected to generate these results). A wide range of social and environmental outcomes were expected, reflecting the diversity of the organisations/activities funded by SIFs.

Figure 4.7 The expected social and environmental outcomes generated by social investment (by value), 2011/12



Base = 18 SIFs.

4.4 Social investment and SIFI sustainability

Operational sustainability describes the extent to which a SIFI is able to cover its operational costs (mainly staff and overhead costs) in undertaking social investment through income generated through its core activities (usually taken to be the interest earned on loans or the return generated from equity investments, together with any other fees and charges associated with investment activity).

Operational sustainability is thus a key measure of whether or not a SIFI can 'survive' independently, or whether non-earned external income (for example, grants or investments) is required in order to cover day-to-day running costs. Note that this is distinct from financial sustainability, which measures the extent to which earned income can cover both operational costs and also losses to a SIFI's capital base through debt write-offs. Financial sustainability has not been measured as part of this research.

In order to measure operational sustainability, SIFIs were asked to provide data on the 2011/12 value of their:

- Operational costs²⁹ incurred through social investment activities; and
- Revenue generated from social investment returns and fees and charges.

Operational sustainability was calculated for each SIFI and is expressed as income as a percentage of expenditure (where a value over 100% indicates that a SIFI can cover all of its expenditure through income). *Note that this calculation only relates to the social investment related share of a SIFI's income and expenditure.*

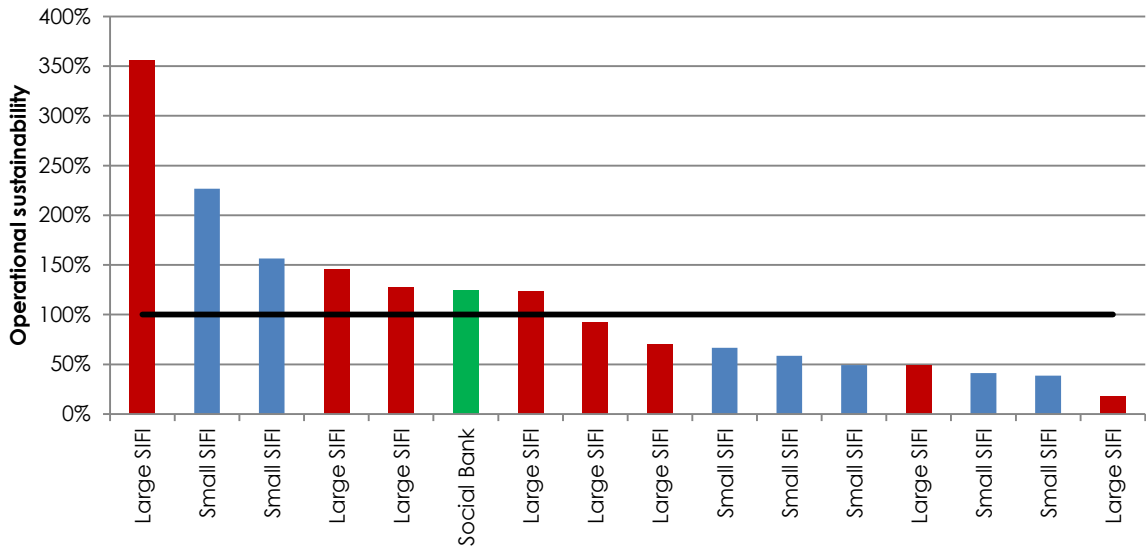
Many SIFIs also undertake non-social investment related activities (for example, lending to other types of enterprise, non-financial services, etc.) which would result in additional income and expenditure. Figures for operational sustainability thus do not reflect the position at an *organisational* level, only the position within the 'business unit' that is responsible for social investment.

Indicative analysis of sustainability can be undertaken across the SIFIs that responded to the survey and provided data on their costs and income (16 organisations). As Figure 4.8 shows:

- Just under half of the SIFIs that provided financial data covered their social investment related operating expenses through earned income in 2011/12;
- Generally, social banks are understood to be operating on a sustainable basis. The one social bank that provided the necessary financial data covered its social investment costs through earned income;
- Of the eight larger SIFIs (investment over £1m) who provided data, half were covering their social investment costs through earned income (and in some cases generating a considerable surplus), and an additional one almost achieved sustainability in 2011/12. One large SIFI was only able to cover 18% of its social investment costs through earned income; and
- Of the seven smaller SIFIs (investment under £1m) who provided data, two were able to cover their costs, and five were not. Smaller SIFIs are thus slightly less likely to demonstrate operational sustainability within their social investment activities than larger SIFIs.

²⁹ Including staff costs, insurance, utilities, rent, consumables, and travel expenses. Capital investments are excluded, but depreciation charges are included.

Figure 4.8 The operational sustainability of selected SIFIs who make investments, 2011/12



Base = 16 SIFIs.

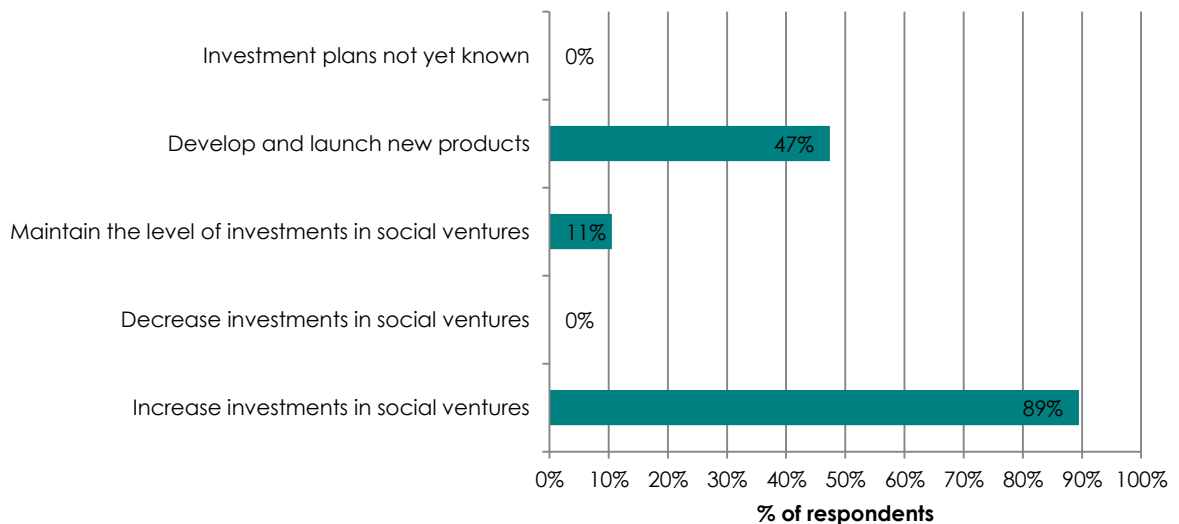
4.5 Future investment plans and constraints in the social investment market

SIFIs were asked questions about their ambitions for future investment activities, and whether they expected to experience any constraints that would hinder their abilities to meet these ambitions.

4.5.1 Future investment plans

SIFIs were asked to indicate their investment plans for the next two to three years (Figure 4.9).

Figure 4.9 Planned social investment activity over the next two to three years



Note: Survey respondents could provide more than one answer. Base = 19 SIFIs.

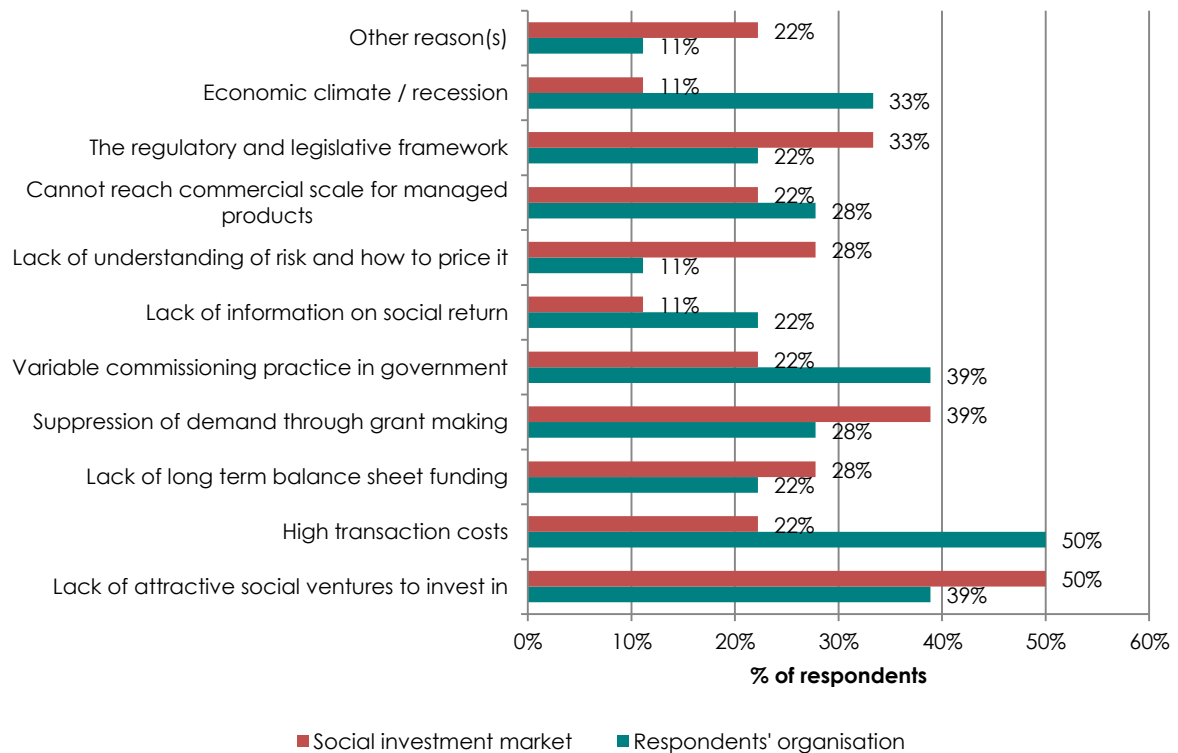
Overall:

- The vast majority of SIFIs (89% of survey respondents) expected to increase their investments in social ventures over the next two to three years;
- No SIFIs planned to decrease the scale of their investing, and 11% expected to maintain their investments at their current level; and
- Just under half of all SIFIs expected to develop and launch new products over the next two to three years.

4.5.2 Anticipated constraints on growth in the sector

SIFIs were shown a selection of potential constraints on future growth in the social investment sector, and were asked to indicate which of these they considered the biggest constraints on the growth of: a) their organisation and b) the social investment market more broadly (see Figure 4.10).

Figure 4.10 The proportion of SIFIs who make investments who see selected constraints on growth as the biggest constraint(s) facing their organisation and the social investment market as a whole



Note: Survey respondents could provide more than one answer. Base = 18 SIFIs.

In summary:

- As regards their own *organisations*, SIFIs identified high transaction costs (50% of survey respondents), variable commissioning practice in Government (39% of respondents) and a lack of attractive investment opportunities (also 39% of respondents) as the biggest constraints on growth.
- High transaction costs were reported to result from issues with levels of investment readiness amongst social ventures. SIFIs noted that considerable staff time was

required for each social investment, particularly where applicants needed support to develop their business plans.

- As regards the *social investment market*, the biggest constraints reported by SIFIs were a lack of attractive investment opportunities (50% of survey respondents), and suppression of demand through grant making (39% of respondents).
- Both of these issues relate to the level of demand for investment amongst social ventures, in particular demand from viable operations. As shown in Table 4.4, most SIFIs were unable to meet most of the applications for investment that they received. SIFIs identified problems with the investment readiness of applicants as reasons for rejection, and also highlighted issues with the levels of capitalisation of social ventures, as well as for one SIFI a perception that social ventures lacked appropriate business skills (instead focussing on their social impact)³⁰.
- In some instances – such as high transaction costs and commissioning practice – SIFIs identified constraints that they believed were a major issue for their specific organisation, and substantially less so for the sector as a whole; and
- Conversely, SIFIs also identified constraints which were not a major issue for their organisation, but which they saw as a barrier for the sector as a whole (for example, understanding and pricing risk and regulatory and legislative framework).

4.6 Summary

- UK social investment reached £202m in 2011/12 representing growth of up to a quarter on the previous year.
- Total investments continue to be dominated by a small number of major SIFIs. Three social banks accounted for 80% of the market and seven SIFIs (including the social banks) account for just over 90% of the market. Nevertheless, substantial growth in investment values was evident across SIFIs of all sizes.
- This increase in investment activity was reflected in SIFI employment – which reached around 430 FTE employees involved in social investment activity in 2011/12 and an average increase of one member of staff per SIFI on the previous year.
- In 2011/12, 765 social investments were made by SIFIs, of which almost 80% were made by eight SIFIs. This eight included a mix of social banks, large and small SIFIs. Annual investments across the SIFI sector ranged in number from one to 170 investments.
- By value, secured loans increased to 91% of the total market (£182m). In contrast, the value of unsecured lending and equity-based investments placed in the market reduced. Only just over 40 equity-based investments were completed in 2011/12.
- Diversity of investment products is offered by large and small SIFIs alike, social banks are focused almost entirely on secured lending.
- Average expected returns by investment type are surprisingly similar

³⁰ See also Big Lottery Fund/Clearly So/NPC (2012) *Investment readiness in the UK*, <http://www.thinknpc.org/publications/investment-readiness-in-the-uk/>

across investment types, at 7% to 8%. Nevertheless, there exists a substantial range in returns expected across product providers.

- Two thirds of SIFIs met less than half of their investment requests in 2011/12 and virtually all plan to increase their investment activity over the next two to three years.
- Indicative data on investment patterns suggests that there is substantial diversity in the geography, sector, and social outcomes of investments, which both reinforces London's presence and highlights other developing areas within the UK.
- Where reported, half of SIFIs were operationally sustainable with the smallest investors least likely to be sustainable.
- The top two growth constraints in the social investment market were identified as the quality of investment propositions and suppressed demand through ventures achieving grant funding.
- The top two growth constraints noted by respondents in relation to their own organisations were high transaction costs and, jointly, the quality of investment propositions and variable commissioning practice in Government.

5 The economic impact of social investment

This section of the report presents an overview of the economic impact of social investment in the UK. It begins with an analysis of the characteristics and access to finance behaviour of recipients of social investment, drawing on the results of the survey of social ventures (recipients of SIFI investment). The survey results and analysis form the basis of a robust and comprehensive assessment of the economic impact of UK social investment.

5.1 The survey of social ventures

As reported in section 2.3, response rates achieved by the social venture survey were strong where direct contact channels were available between the research team and the social venture (i.e. telephone survey or direct e-survey). In total, 99 completed survey responses were received.

Assuming that the population (i.e. the number of social investments made across the SIFI sector in 2011/12) amounts to 765 investments (see Table 4.1 earlier), the results of the survey have a confidence interval of between +/- 5.2% and +/- 9.2% at a 95% level of confidence³¹. The results of the survey are thus statistically robust.

There is some evidence that the characteristics of the achieved sample do not precisely match the characteristics of the population as a whole, though it should be noted that data for the population are based on aggregated (and in some cases averaged) data as reported by SIFIs in the SIFI survey. Ultimately, then, the full and exact characteristics of the population are not known in the sense of basic data collected directly on every social investment client in 2011/12. Overall, it would appear that the achieved sample is slightly skewed towards social ventures based in the Yorkshire and Humber who received relatively small amounts of investment in the form of unsecured loans. In the following sections it is noted where this skew may have had an impact on the findings.

5.2 Characteristics of social ventures

5.2.1 Whether organisations were social ventures

There is an on-going debate about how best to define a social venture. Government and other parties within the social venture sector currently tend to utilise an approach that focuses on the purpose of social ventures, rather than seeking to define them according to their legal status. Following this approach, we asked survey respondents whether they met the three criteria:

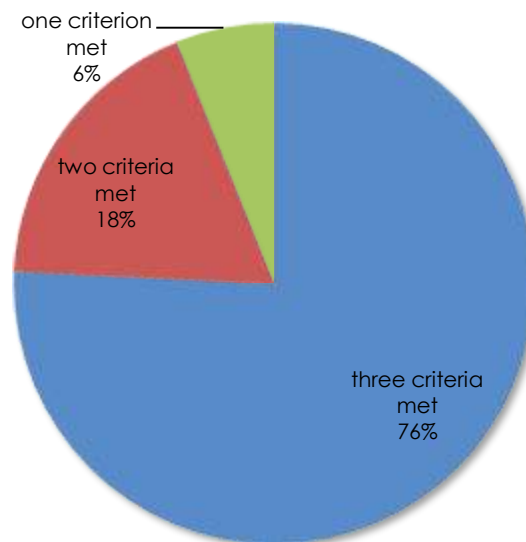
- Whether they considered themselves to be a social venture;
- Whether they generated more than a quarter of their income from trading activities; and
- Whether they used their trading surpluses to further their social or environmental goals.

³¹ The exact confidence interval depends on the answers to individual questions. If 90% of respondents pick a particular answer then the confidence interval is +/- 5.2%, whereas if 50% of respondents pick a particular answer then the confidence interval is +/- 9.2%

Responses to each of these three criteria are set out below. Figure 5.1 summarises the proportion of respondents to the survey who met between one and three of these criteria (no social ventures met none of the criteria):

- Around three quarters of respondents met all three criteria of a social venture; and
- Just 6% of respondents only met a single criterion.

Figure 5.1 The number of criteria defining a social venture that are fulfilled



Base = 99 social ventures.

5.2.1.1 Whether survey respondents considered themselves to be a social venture

Survey respondents were asked if they felt that their organisation matched the following definition:

A business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners³².

Most survey respondents (95% of the 99) stated that their organisation matched the above definition, with the remaining 5% not classifying themselves as a social venture.

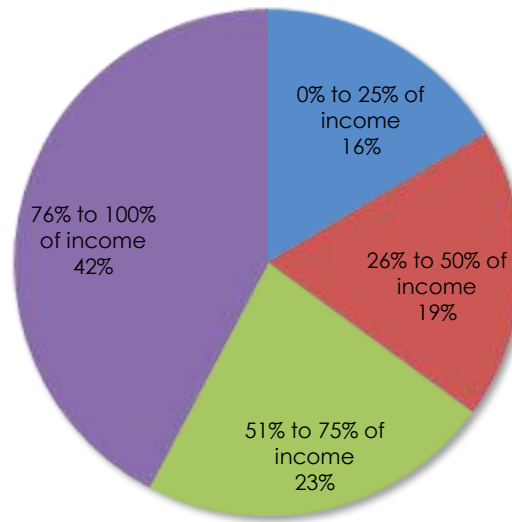
5.2.1.2 Whether social ventures generated more than a quarter of their income from trading activities

Social ventures were asked to indicate the proportion of their income that was generated from trading activities (Figure 5.2):

- Some 16% of survey respondents generated less than a quarter of their income from trading activities, and therefore did not meet the criterion; and
- Just under two thirds of social ventures generated over half of their income from trading activities.

³² DTI (2002) *Social enterprise: a strategy for success*.

Figure 5.2 The percentage of income of social ventures that is generated from trading activities



Base = 97 social ventures.

5.2.1.3 Whether social ventures used their trading surpluses to further their social or environmental goals

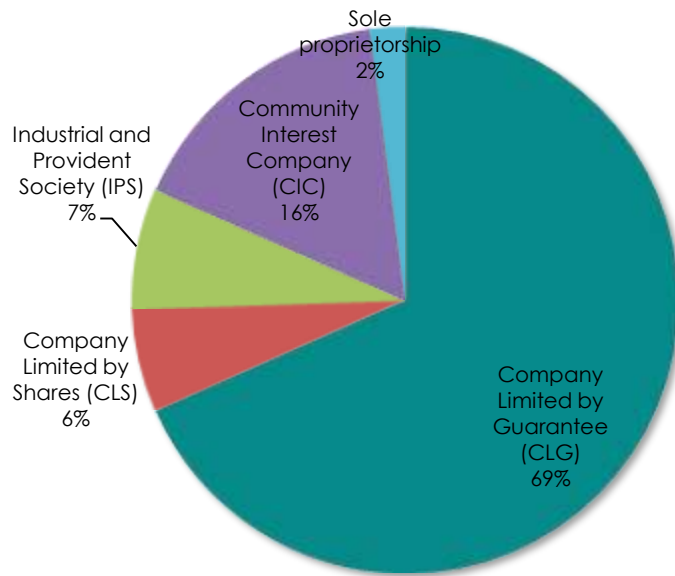
Social ventures were asked whether they use the majority of the surplus or profit from their trading activities to further their social or environmental goals. The vast majority (93% of survey respondents) indicated that this was the case.

5.2.2 Legal form and type of organisations

Social ventures were asked to specify their organisation's legal status (Figure 5.3) and how their organisation might be classified (Figure 5.4):

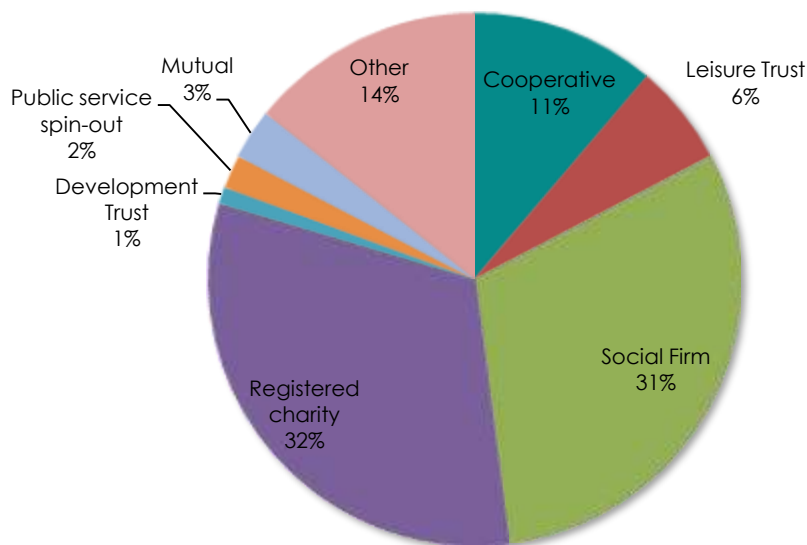
- As regards their legal status, over two thirds of social ventures reported that they were Companies Limited by Guarantee, with a further 6% classed as Companies Limited by Shares;
- Community Interest Companies (CICs) accounted for 16% of social ventures, with a small minority (7%) classed as Industrial and Provident Societies; and
- There was greater diversity in terms of organisational types (note this is not a legal definition, and is instead how social ventures describe themselves). Around a third of social ventures classed themselves as social firms, and a further third were registered charities.

Figure 5.3 The legal status of social ventures



Base = 98 social ventures.

Figure 5.4 A breakdown of social ventures by organisation type

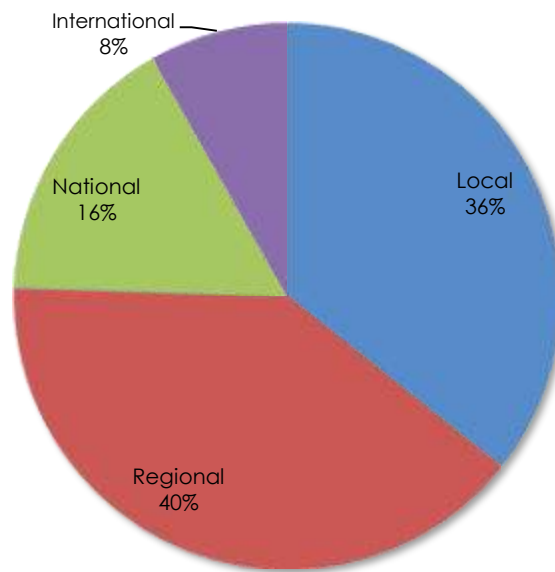


Base = 98 social ventures.

5.2.3 Geography of organisations

Social ventures were asked to outline their geographical area(s) of operation, which is equivalent to the extent of the markets that they served (Figure 5.5):

- Social ventures were largely local or regional organisations; collectively over three quarters of survey respondents reported that they served local or regional markets; and
- Just 8% of social ventures operated internationally (i.e. exported their products and services).

Figure 5.5 Geographical areas of operation of social ventures

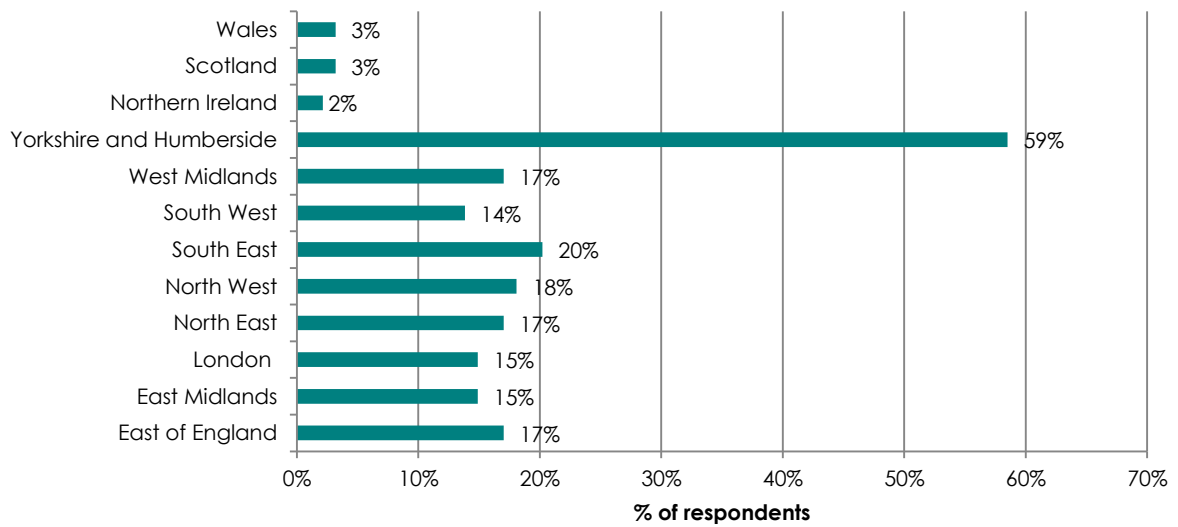
Base = 98 social ventures.

Social ventures were also asked to specify the regions/Devolved Administrations in which they operated (Figure 5.6):

- Yorkshire and Humberside accounted for over half of respondents (59%), with the remainder of social ventures distributed across the rest of the UK (the three Devolved Administrations accounted for the smallest share of survey respondents); and
- Comparing Figure 5.6 (the geography of respondents to the social venture survey) with Figure 4.5 (the geographical spread of investments reported by SIFs) suggests that Yorkshire and Humberside is over-represented amongst survey respondents³³.

³³ This is one example of where it is believed that the finding has been skewed by the respondent sample.

Figure 5.6 Geographical regions of operation of social ventures

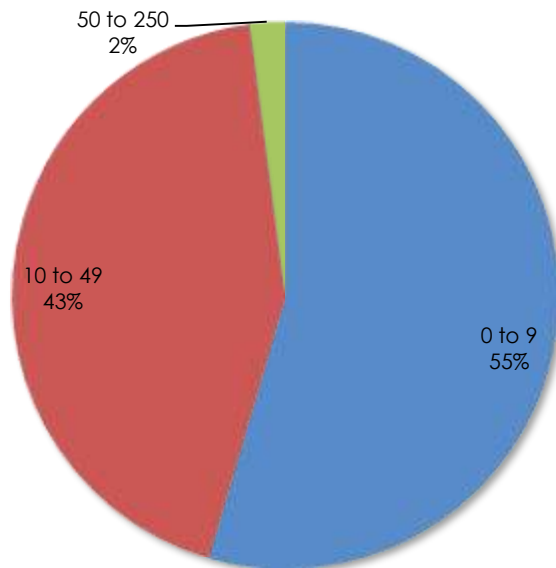


Base = 94 social ventures.

5.2.4 Size of organisations

Social ventures were asked to report their employment and turnover at the time of the survey (i.e. May 2013). As Figure 5.7 shows, most organisations that receive finance from SIFs are small, with the majority employing between nought and nine people (55%), and most of the remainder employing between 10 and 49 people.

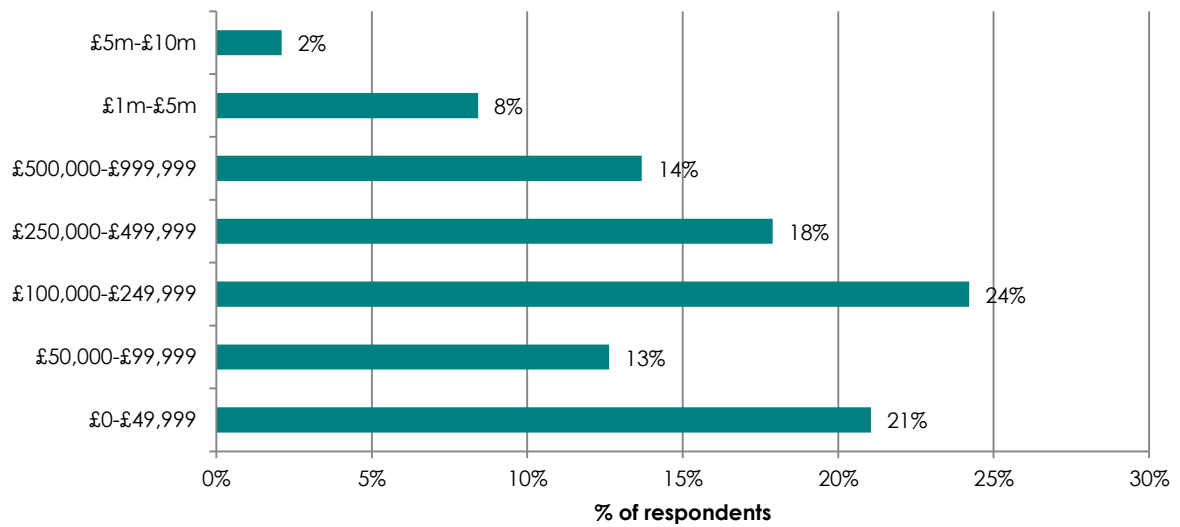
Figure 5.7 The number of people employed by social ventures (full time equivalent)



Base = 99 social ventures.

Figure 5.8 shows that most social ventures were also small in terms of their annual turnover, with 58% of survey respondents generating income of under £250,000 a year. Just 10% of survey respondents reported annual turnover in excess of £1m.

Figure 5.8 The annual turnover of social ventures



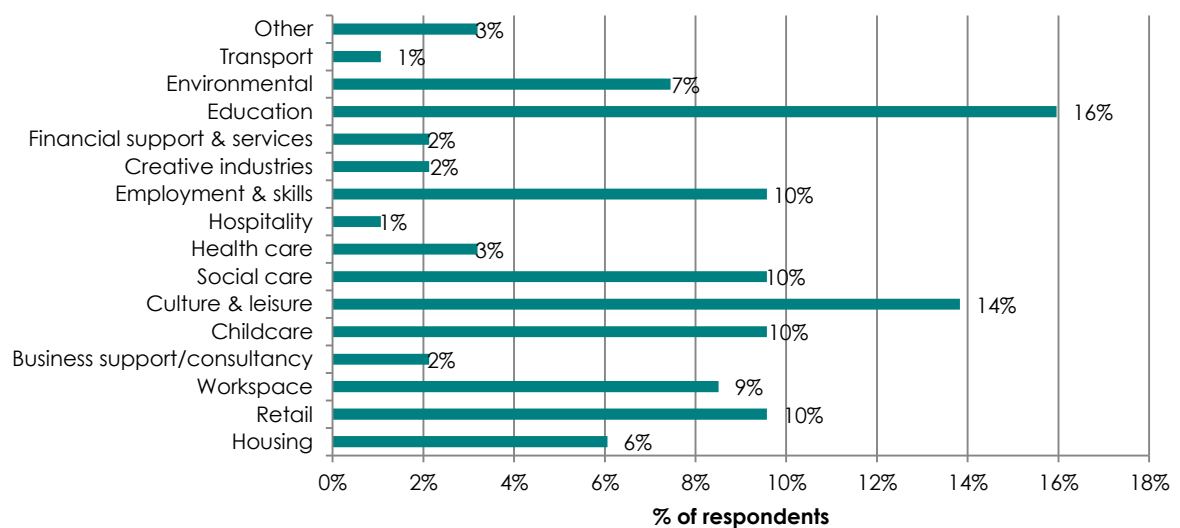
Base = 95 social ventures.

5.2.5 Sector of organisations

Social ventures were asked to specify the sector of operation of their organisations (Figure 5.9):

- There was considerable diversity across sectors, with education and culture and leisure the two most common sectors for social ventures (accounting for 16% and 14% of respondents respectively); and
- Again, reporting by survey respondents (Figure 5.9) can be compared with the sector of social ventures as reported by SIFs (Figure 4.6). The match is reasonable, suggesting that the sample of social ventures is fairly representative of the sector of the population of social ventures as a whole.

Figure 5.9 The sector of operation of social ventures



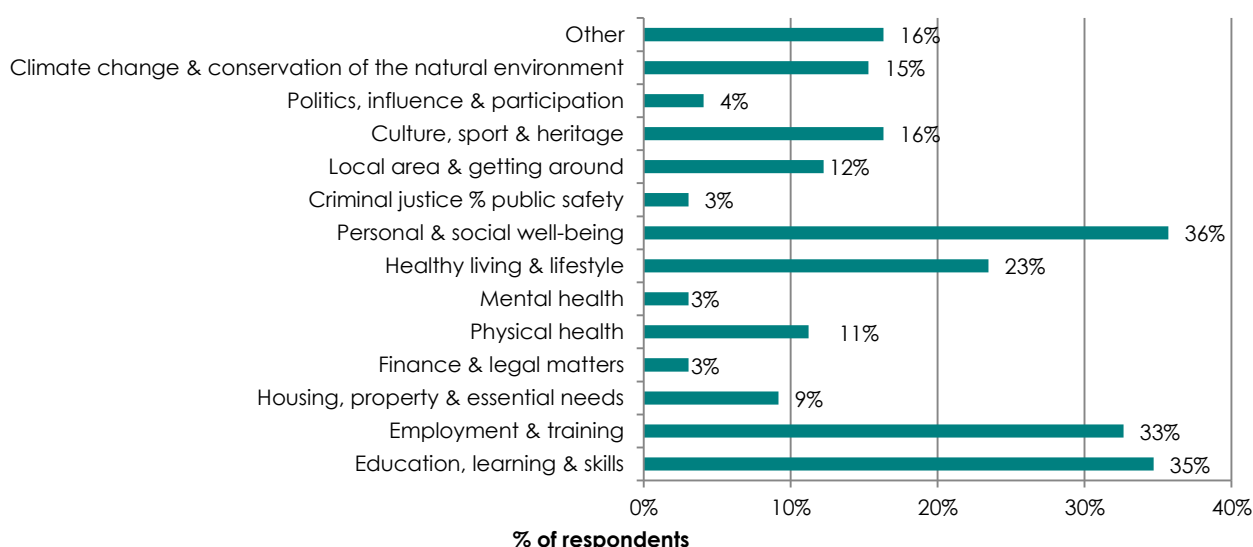
Base = 99 social ventures.

5.2.6 Social and environmental objectives of organisations

Social ventures were asked to indicate their social and environmental objectives (Figure 5.10):

- There was considerable diversity in the social and environmental objectives of survey respondents; and
- Over a third of social ventures said that their objectives included the following:
 - Personal and social well-being (36%);
 - Education, learning and skills (35%); and
 - Employment and training (33%).

Figure 5.10 The social and environmental objectives of social ventures



Note: Survey respondents could provide more than one answer. Base = 98 social ventures.

5.3 Profile of finance accessed by social ventures

Social ventures were asked a number of questions about the investment that they had received from SIFs over the period April 2011 – 31st March 2012.

5.3.1 Type of investment accessed

Social ventures were asked to indicate the type(s) of investment they had accessed (Figure 5.11 and Figure 5.12):

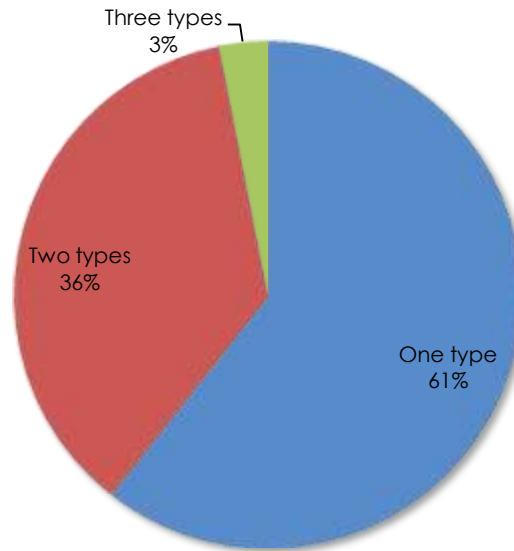
- Social ventures could access more than one type of investment, with around 60% of survey respondents indicating that they only received a single type of investment. Of these organisations, unsecured loans were the most common form of investment accessed (38% of the total sample had only received this type of product)³⁴;
- Around a third of survey respondents indicated that they had received two types of investment simultaneously from their SIFI. The most common combination of

³⁴ Given the results on the share of volume of loans by products reported by SIFs (see Figure 3.3), this suggests an under-representation in the sample of secured loans.

investment products was a grant plus an unsecured loan (25% of the total sample); and

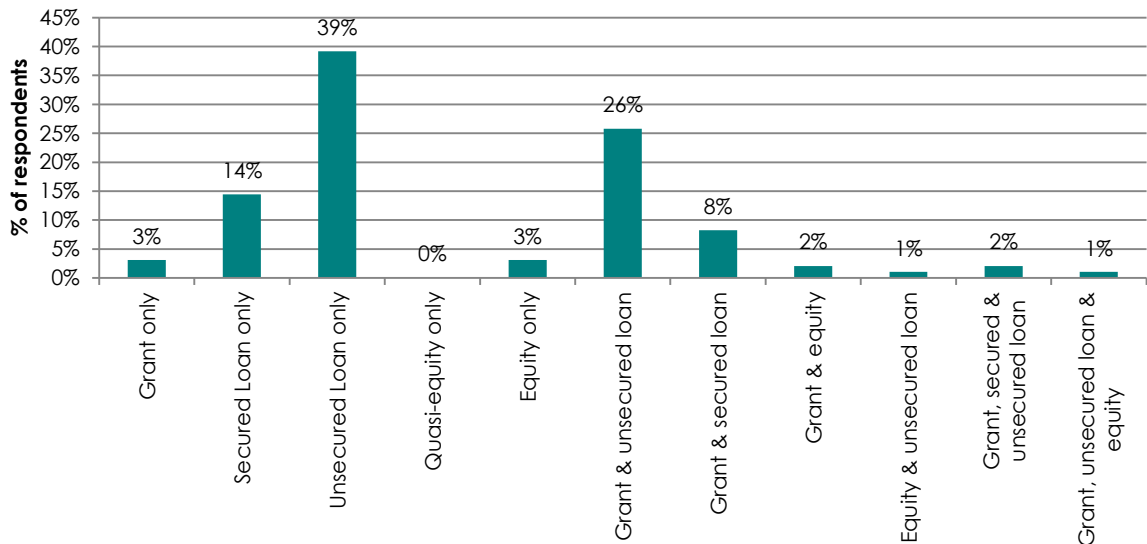
- A small minority of social ventures (3% of the total) had received three different types of investment simultaneously. A combination of grants, loans and equity were accessed.

Figure 5.11 The number of types of investment accessed by social ventures



Base = 99 social ventures.

Figure 5.12 The type(s) of investment accessed by social ventures



Base = 99 social ventures.

5.3.2 Size of investment

Table 5.1 shows the size of the investment received by social ventures:

- Social ventures that received one type of investment on average received a larger amount than those social ventures that received combinations of financial products (average size £86,400 compared to £41,100);

- Loans received by social ventures ranged in size from just £1,000 to £600,000. Secured loans were larger on average than unsecured loans, and loans received as a single standalone financial product were larger than if they were provided in combination with other financial products (e.g. the average size of a secured loan on its own was £124,700, compared to £18,200 if it was provided alongside another type of investment); and
- Equity investments ranged in size from £5,000 to £470,000, with an average size of £162,000 when provided on their own (or £15,400 if provided in combination).

Table 5.1 The minimum, maximum and mean average size of the investment received by social ventures

	One investment type				Multiple investment types			
	Min. size	Max. size	Median average	Mean average	Min. size	Max. size	Median average	Mean average
Grant	10,000	460,000	106,700	152,800	5,000	300,000	31,800	25,000
Secured loan	10,000	600,000	120,000	124,700	2,000	70,000	18,200	8,000
Unsecured loan	3,000	600,000	25,000	53,000	1,000	30,000	6,500	5,000
Quasi-equity	15,000	470,000	242,500	242,500	n/a	n/a	n/a	n/a
Equity	6,000	470,000	20,000	162,000	5,000	70,000	15,400	11,000
All types	3,000	600,000	30,000	86,400	7,000	350,000	30,000	41,100

Base = 41 (grants), 22 (secured loans), 65 (unsecured loans), 2 (quasi-equity), 6 (equity) social ventures.

5.3.3 Interest rate and IRR on investment

Social ventures were asked to report the actual interest rate that they were paying on their secured/unsecured loans, and those social ventures in receipt of equity or quasi-equity investments were asked to report the actual Internal Rate of Return (IRR) of the investment (Table 5.2):

- The average interest rate that social ventures reported paying on secured loans was very close to that which they paid on unsecured loans (6.3% and 6.4% respectively). Furthermore, interest rates ranged from 3% to 13.5% for secured loans, and from 4% to 12.6% for unsecured loans. This suggests that SIFs do not charge markedly different interest rates depending on whether social ventures are able to provide security (Figure 4.4 – interest rates reported by SIFs – suggests something similar); and
- As regards equity investments, the average IRR reported was 4.25%, within a range of 0% to 10% (but for a very small sample).

Table 5.2 The minimum, maximum and mean average interest rate (loans) or IRR (equity or quasi-equity) of the investment received by social ventures

Type of investment	Minimum interest rate/IRR	Maximum interest rate/IRR	Mean average interest rate/IRR
Secured loan	3.0	13.5	6.37
Unsecured loan	4.0	12.6	6.30
Quasi-equity	n/a	n/a	n/a
Equity	0.0	10.0	4.25

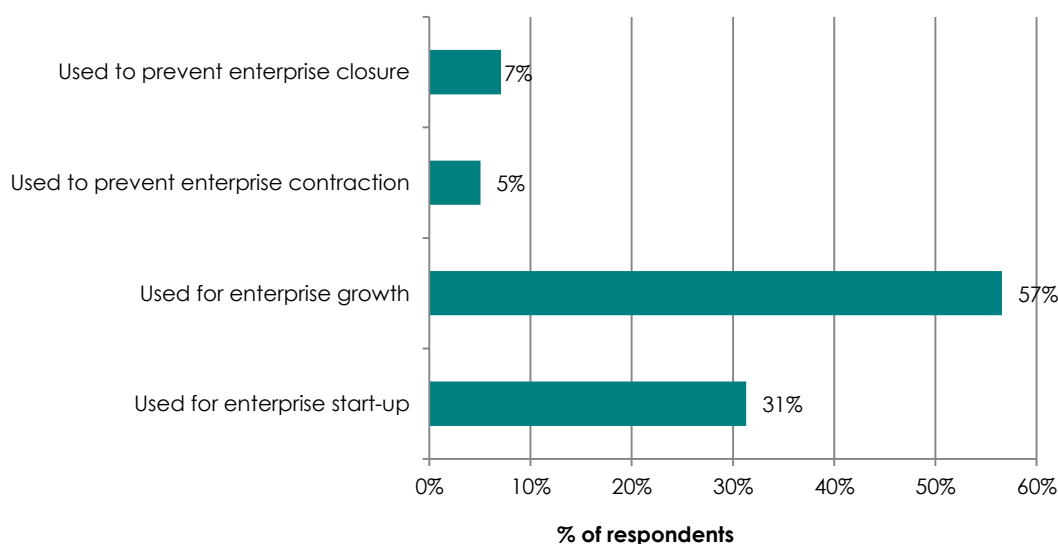
Base = 15 (secured loans), 43 (unsecured loans), 4 (equity) social ventures.

5.3.4 Purpose of investment

Social ventures were asked to state the purpose of the investment they had accessed, in terms of how they had utilised the capital (Figure 5.13):

- Over a half of social ventures (57%) stated that they had utilised the finance they had accessed for the purpose of venture growth;
- Of the remaining social ventures, most (31% of the total) had used the finance they had received for venture start-up. Of these social ventures, 41% (equal to 7% of the total sample of survey respondents) reported that their business would not have started if they had not received investment from their SIFI; and
- A total of 13% of survey respondents reported that their investment had been used to prevent venture contraction or even closure. Of the social ventures that accessed investment in order to prevent closure, 100% indicated that their business would have closed if they had not been able to access their SIFI investment.

Figure 5.13 The purpose of the investment accessed by social ventures



Base = 99 social ventures.

5.4 Pre-investment access to finance and applications to other investors

Social ventures were asked to describe the investment that they had sought to access around the same time as they had accessed investment from a SIFI.

5.4.1 Whether social ventures had sought to access finance from other sources

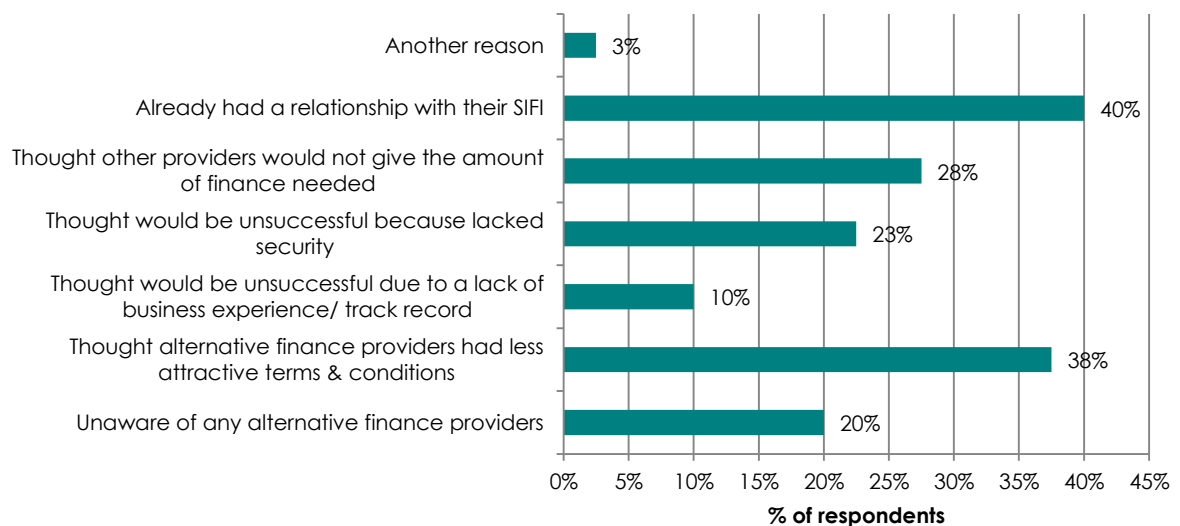
Just over half of social ventures (60% of the 99) stated that they had sought to access finance from alternative sources around the same time that they accessed investment from their SIFI.

5.4.1.1 Social ventures that had not sought finance from other sources

Those social ventures who indicated that they had not sought to obtain finance from other sources (40% of the 99) were asked to give the reason(s) as to why this was the case (Figure 5.14):

- The most common reason provided by social ventures for not having sought to obtain finance from alternative sources was that they had a prior relationship with their SIFI (40%);
- A further 38% of social ventures reported that they had not applied for funding from alternative finance providers because the terms and conditions offered by their SIFI were more favourable;
- In some cases social ventures did not apply for funding from alternative providers because they believed that they would be unsuccessful. A lack of security was the most common reason for this belief, mentioned by around a quarter of survey respondents who had not sought finance from an alternative provider; and
- Around a fifth of social ventures indicated that they were not aware of any alternative providers of investment, suggesting that understanding of the finance markets is poor within some organisations.

Figure 5.14 Why selected social ventures had not sought finance from other sources



Note: Survey respondents could provide more than one answer. Base = 40 social ventures who had not sought access to finance from other sources.

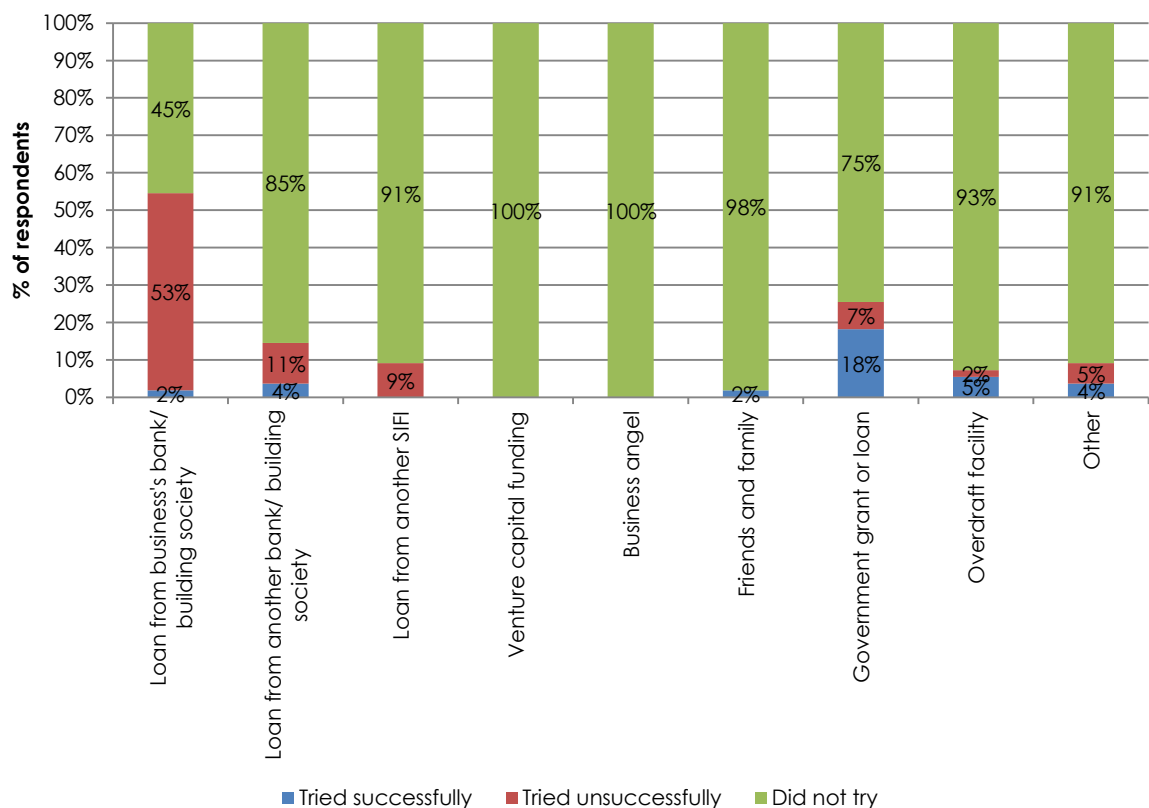
5.4.1.2 Social ventures that had sought finance from other sources

The majority of social ventures (60%) had sought finance from alternative providers around the same time that they accessed investment from their SIFI. Figure 5.15 presents a range of alternative sources of finance, and shows the

proportion of survey respondents who reported that they had sought to access finance from each source, together with the outcome:

- The most commonly used alternative source of finance was a loan from the organisations' banks/building societies. Some 55% reported that they had attempted to access a loan from their bank/building society, though just 2% of survey respondents had been successful;
- A smaller proportion (15%) of social ventures had tried to obtain a loan from another bank/building society, and around 4% had been successful;
- Social ventures had more success in accessing loans or grants from Government; around 25% had sought finance in this way, and over half (18% of the total sample) had been successful; and
- There is little evidence that social ventures 'shop around' within the SIFI sector, with just 9% of social ventures indicating that had sought loan finance from more than one SIFI. As also shown in Figure 5.14, this would suggest that social ventures tend to build relationships with a single SIFI.

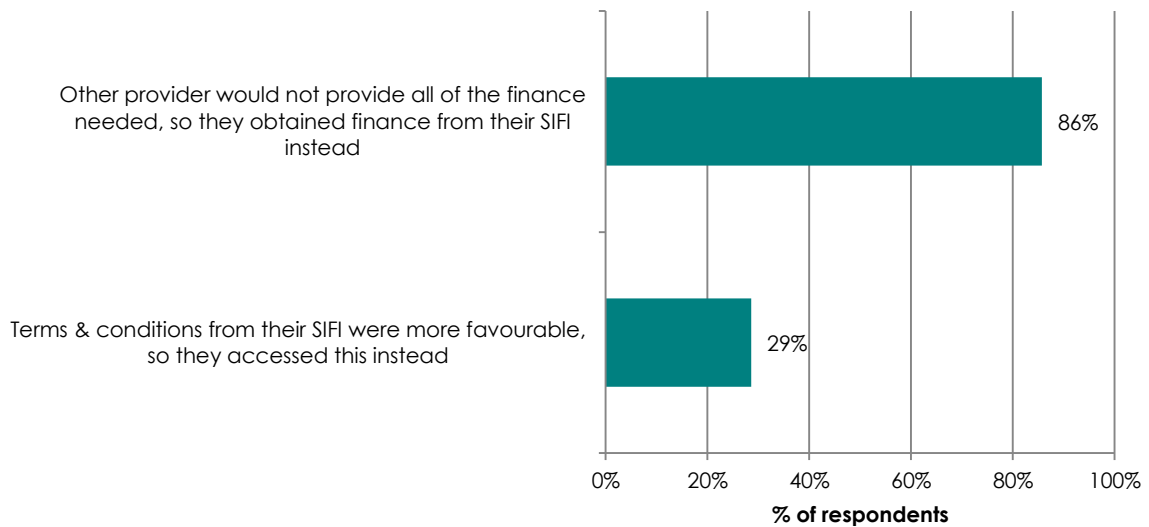
Figure 5.15 Alternative sources of finance that selected social ventures sought investment from, and the outcome



Base = 55 social ventures who had sought access to finance from other sources.

Social ventures who indicated that they had been *successful* in their attempt(s) to access finance from alternative sources around the same time that they accessed investment from their SIFI were asked to indicate why they had also applied for finance from their SIFI (Figure 5.16).

Figure 5.16 Why selected social ventures had applied for SIFI funding having successfully sought to access finance from other sources



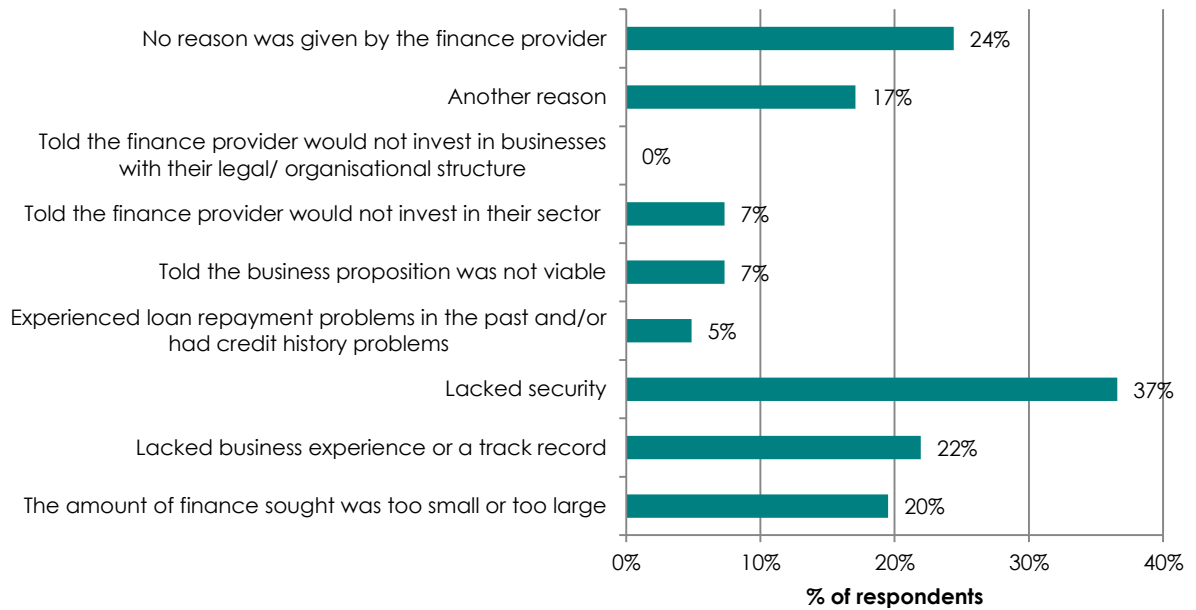
Note: Survey respondents could provide more than one answer. Base = 14 social ventures who had successfully sought to access finance from other sources.

Whilst the sample was small (just 14 organisations), this suggests that in most cases the alternative provider would not provide all of the finance required, and so the social venture used their SIFI instead. In almost a third of cases (29% of social ventures who successfully applied for finance from another provider), the SIFI was selected as it was able to offer more favourable terms and conditions (see also Figure 5.14, where the quality of the terms and conditions offered by SIFIs was identified as an important reason for not seeking finance from other types of provider).

Social ventures who said that they had been *unsuccessful* in their attempt(s) to access finance from alternative sources around the same time that they accessed investment from their SIFI were asked to indicate why this may have been the case (Figure 5.17)³⁵:

³⁵ Research (see GHK (2010) *Evaluation of Community Development Finance Institutions*) has indicated that applicants do not always know/understand why they were unsuccessful in an application for finance, so these results should be treated with caution as they are self-reported.

Figure 5.17 Why selected social ventures were unsuccessful in accessing finance from specific other sources



Note: Survey respondents could provide more than one answer. Base = 41 social ventures who had unsuccessfully sought to access finance from other sources.

In total:

- A lack of security was the most commonly identified reason as to why social ventures had been unsuccessful in an application for investment from an alternative provider (mentioned by 37% of social ventures), with a further 22% of social ventures reporting that a lack of a track record had been a reason for an unsuccessful application;
- A fifth of social ventures reported that they had been rejected because the amount of finance they had requested was too small or large; and
- Around a quarter of social ventures reported that no reason had been given by the alternative provider for the rejection of their application.

5.5 Economic impact of social investment

A key task for this research was to carry out an assessment of the economic impact of SIFI social investment activity. The following provides a short summary of the impact assessment methodology employed before setting out the gross and net economic impact generated as a result of SIFI investment activity. Finally, the relationship between social investment and economic impact is considered.

5.5.1 Economic impact assessment methodology

This economic impact assessment of social investment has been designed to be compliant with Government guidance on assessment methodologies, as set out

in the HM Treasury Green Book³⁶ – including the preferred use of a robust social venture survey to calculate impact.

The economic impact considered: the stock (number) of social ventures, impact on employment (FTE), impact on business income (turnover), and, impact on Gross Value Added (GVA). Data on economic impact was obtained from the results of the telephone and e-survey of 99 social ventures that had received investment, and then grossed up to represent the total population of 765 investments in 2011/12³⁷.

Assessment of both gross and net economic impact is provided (taking full account of additionality) and, for the purposes of this research, the economic impact of SIFI investment has been presented at two spatial scales: *the region* (defined as an area up to 50 miles from a social venture's main centre of operations); and, at a national level i.e. *the UK*.

The methodology of economic impact assessment

This economic assessment involved totalling three separate impact streams:

- 1) **The (direct) impact** (on jobs, turnover, etc.) of social investment into a social venture through its ability to produce more goods and services;
- 2) **The (indirect) impact** (on jobs, turnover, etc.) of a social venture's spending in the supply chain in order for it to deliver its goods and services; and
- 3) **The further (induced) impact** (on jobs, turnover, etc.) from the spending of suppliers and their employees.

Adding up these impact streams allows a calculation to be made of economic impact on the whole economy and not just the social ventures themselves.

The economic impact considered: the stock (number) of social ventures, impact on employment (FTE), impact on business income (turnover), and impact on gross value added (GVA).

This assessment, then, gives a gross calculation of economic impact but, in accordance with HM Treasury best practice, a 'net calculation' should be undertaken, such that the economic impact which is measured is truly additional ('additionality').

What is meant by this is that the impact assessed is only that of additional economic activity; for example, a social venture may have grown anyway without the investment and/or it has merely won work from a local competitor (who therefore does less economic activity to

³⁶ HM Treasury (July 2011) *The Green Book: appraisal and evaluation in Central Government*, at <https://www.gov.uk/government/publications/the-green-book-appraisal-and-evaluation-in-central-government>

³⁷ As noted in section 5.1, the results are statistically robust with a confidence interval of between +/- 5.2% and +/- 9.2% at a 95% level of confidence.

the same amount as that won by the invested social venture) and so on³⁸.

Full economic impact assessment, then, involves calculation of both gross and net economic impact which takes into account additionality considerations – deadweight ('would it have happened anyway without this investment'), displacement ('did you just replace a local competitor'), leakage ('was some of the economic impact of your activity felt outside the target area') and economic multipliers ('did the economic impact stay in the area and get re-spent again...and again').

This implies that the net economic impact will (generally) always be less than the gross economic impact – and quite often considerably less (for example, retail expenditure moving from one new shopping centre to another).

It highlights also that spatial scale is a key consideration within an economic impact assessment, since the additionality factors described above vary depending on the geographic unit of analysis (the 'target area'). For example, the larger the economic area the more likely you are to be taking work from a competitor (reduced additionality), but also the more likely that your supply chain will be within the economic area (reduced leakage and greater additionality). It can be seen, then, how the 'additionality ratios' vary across sectors, geographies and types of economy.

Annex two provides full details of the calculation of additionality ratios based on survey responses and which formed the basis of the calculation of gross and net impact presented in the following section.

5.5.2 Gross economic impact

Gross economic impact is the impact reported by businesses *before* taking into account the additionality considerations (deadweight, displacement, leakage and multipliers).

Table 5.3 shows the gross economic impact of SIFI investments to date (as at May 2013), and once the finance periods of the investments have finished:

- Over the lifetime of their finance period, the 765 investments provided by SIFIs had resulted in:
 - The creation/safeguarding of a total of 340 social ventures (gross);
 - The creation/safeguarding of 6,870 FTE jobs (gross); and
 - The creation/safeguarding of just under £200m of *annual* turnover, equal to £58m in *annual* GVA (gross).
- Reflecting the economic climate, a key impact of financing social ventures was to ensure the continued survival of businesses, and thus employment and turnover. As at May 2013, the closure of a total of 220 social ventures had been

³⁸ Although in this instance whilst the quantitative gain may be zero there may a qualitative gain – for example, where a new venture has won work because it is more innovative (social innovation), is more efficient (lower cost for same product/service) and, especially pertinent in the case of social ventures, generates social impact which may not have occurred otherwise.

prevented by the 765 investments provided by SIFIs (gross). This had subsequently preserved some 1,840 jobs (gross).

Table 5.3 Gross economic impact of SIFI investment

	Impact generated to date (May 2013) (A)		Impact generated by end of investment period (B)	Cumulative total (A + B)
	Created	Safeguarded	Created	Created & safeguarded
Businesses	120	220	0	340
Jobs (FTE)	2,930	1,840	2,100	6,870
Annual turnover (£)	£73,010,000	£48,100,000	£77,450,000	£198,560,000
Annual GVA (£)	£21,410,000	£14,100,000	£22,710,000	£58,220,000

Base = 765 social investments.

5.5.3 Net additional economic impact

Net additional economic impact was calculated using the additionality ratios produced (see Annex two) to take account of deadweight, displacement, leakage and economic multiplier effects. These are a calculation of the truly additional contributions of the social investments to the economy.

At a regional level, displacement was relatively high (social ventures serve local and regional markets rather than, say, being exporters of goods and services). The 'flip-side' of this, however, is that supply chains also tend to be local and regional which adds to the economic multiplier of expenditure in the regional economy.

Table 5.4 shows the net additional economic impact generated by SIFI investments **at a regional scale**.

Table 5.4 Net additional economic impact of SIFI investments (regional scale)

	Impact generated to date (May 2013) (A)		Impact generated by end of investment period (B)	Cumulative total (A + B)
	Created	Safeguarded	Created	Created & safeguarded
Businesses	70	140	0	210
Jobs (FTE)	1,530	730	1,300	3,550
Annual turnover (£)	£41,770,000	£17,830,000	£17,290,000	£76,900,000
Annual GVA (£)	£12,250,000	£5,230,000	£5,070,000	£22,550,000

Base = 765 social investments.

At a regional economy level, the 765 investments by SIFIs generated the following net additional economic impact:

- 210 social ventures created/safeguarded;
- A total of 3,550 FTE jobs created/safeguarded over the whole finance period; and

- Some £77m in *annual* turnover either created/safeguarded, equivalent to £23m in *annual* GVA.

The figures provide evidence for the strong and substantial economic impact of investment at regional level, especially in terms of job creation and venture creation.

Table 5.5 shows the net additional economic impact generated by SIFI investments **at the level of the UK economy as a whole**.

At the level of the UK economy, net additional economic impact is much reduced, primarily due to the very high level of displacement, since social ventures mostly compete with other UK businesses. Though note that they may have delivered unmeasured cost savings to customers, which would generate productivity improvements and, of course, social returns – and which are not considered here. Multipliers are high and leakage not an issue – the economic footprint of the social ventures was essentially contained within the UK economy.

Table 5.5 Net additional economic impact of SIFI investments (national scale)

	Impact generated to date (May 2013) (A)		Impact generated by end of investment period (B)	Cumulative total (A + B)
	Created	Safeguarded	Created	Created & safeguarded
Businesses	10	20	0	30
Jobs (FTE)	250	170	190	610
Annual turnover (£)	£6,120,000	£5,700,000	£1,040,000	£12,860,000
Annual GVA (£)	£1,800,000	£1,670,000	£300,000	£3,770,000

Base = 765 social investments

In summary:

- A total of 30 social ventures were created/safeguarded at a UK level as a result of the 765 social investments;
- 610 net additional FTE jobs were created/safeguarded; and
- Some £4m of net additional *annual* GVA was added to the UK economy as a result of the SIFI investment.

5.5.4 The relationship between social investments and economic impact

Table 5.6 shows the value of the social investment required to generate one unit of net additional economic impact:

- At a regional economy scale, around £30,220 of investment will create/safeguard a social venture, whilst only £1,840 is required to create/safeguard one net additional FTE job. These costs compare favourably with, for instance, regional business support initiatives delivered by the former Regional Development Agencies, where it was estimated that the cost per net

additional business created was £74,200, and the cost per net FTE job created was £8,300³⁹;

- At a national level, substantially more investment is needed in order to generate economic impact, reflecting the high level of displacement. Around £212,520 of investment is required in order to support the creation/safeguarding of a social venture, and £10,680 is needed in order to support the creation/safeguarding of a FTE job. Under the highly efficient Enterprise Finance Guarantee, for example, the cost at UK level per net additional FTE job was estimated to be £1,800, though the cost per job for its predecessor initiative – the Small Firms Loan Guarantee – was put at £7,750⁴⁰; and
- At a regional level, £0.28 of social investment generates £1 of net additional *annual GVA* – although £1.69 is required at national level.

Table 5.6 The value of social investment required to generate one unit of net additional economic impact (economic impact over the lifetime of the finance period)

Unit of economic impact	Value of social investment required to generate one unit of net additional impact	
	Regional scale	National scale
One business	£30,220	£211,520
One FTE job	£1,840	£10,680
£1 of annual turnover	£0.08	£0.49
£1 of annual GVA	£0.28	£1.69

Table 5.7 shows the net additional economic impact generated by £1,000 of social investment. For example:

- £1,000 of social investment into a social venture results in the creation/safeguarding of half a job and £3,500 of net additional *annual GVA* at the level of a regional economy; and
- At the level of the UK economy, the equivalent £1,000 generates a tenth of a job and £600 of net additional *annual GVA*.

Table 5.7 The net additional economic impact generated by £1,000 of social investment (economic impact over the lifetime of the finance period)

Unit of economic impact	Net additional impact generated by £1,000 of social investment	
	Regional scale	National scale
Businesses	0.03	0.00
Jobs (FTE)	0.54	0.09

³⁹ PWC for BERR (2009) *Impact of RDA spending – National report – Volume 1 – main report*; pg. 34., <http://www.berr.gov.uk/files/file50735.pdf>

⁴⁰ Allinson, G. Robson, P. and Stone, I. (2013) *Economic evaluation of the Enterprise Finance Guarantee (EFG) Scheme*, pg. 78, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/85761/13-600-economic-evaluation-of-the-efg-scheme.pdf

Unit of economic impact	Net additional impact generated by £1,000 of social investment	
	Regional scale	National scale
Annual turnover (£)	£12,100	£2,000
Annual GVA (£)	£3,500	£600

It is important to note that data on the turnover and GVA created/ safeguarded as a result of social investment are **annual**; in other words, £1,000 of investment will result in the creation/safeguarding of this turnover/GVA every year. It is reasonable to assume that the turnover impact of an investment would persist for more than one year, and thus to calculate the total GVA impact of social investment by SIFs it is necessary to factor in the duration or persistence of this annual impact.

We have **conservatively** assumed turnover/GVA impact will aggregate over the duration of the investment term (in practice, it is likely that impact would persist further beyond this). Table 5.8 shows the cumulative net additional GVA impact generated by £1,000 of social investment across investment terms of between one and six years. A discount rate of 3.5% per annum has been applied in order to calculate the net present value of this future stream of benefits⁴¹.

It can be seen, for example, that a five year investment term would see a £1,000 social investment generate £16,570 of net additional GVA at the regional level over the period and £2,770 at the national level.

Table 5.8 The cumulative net additional GVA impact generated by £1,000 of social investment, and how this varies depending on the duration of the investment term

Duration of investment term	Cumulative net additional GVA impact generated by £1,000 of social investment	
	Regional scale	National scale
1 year investment term	£3,550	£590
2 year investment term	£6,970	£1,170
3 year investment term	£10,280	£1,720
4 year investment term	£13,480	£2,250
5 year investment term	£16,570	£2,770
6 year investment term	£19,560	£3,270

5.5.4.1 Sensitivity analysis and caveats

The above pages (and Annex two) provide a full, transparent and robust assessment of the economic impact of social investment fully compliant with HMT Green Book expectations. For those who are not used to such assessments it can be seen that the methodology – whenever applied – requires a certain level of

⁴¹ Discounting is used in order to measure the value society attaches to present, as opposed to future, consumption, taking account of the possibility of catastrophic risk and reflecting individuals' preference for consumption now, rather than later. A 3.5% discount rate has been used (HM Treasury Green Book Guidance) – Op Cit.

recognised technical assumptions about evidence base, types of economy, causality and so forth. These have been carefully considered for this assessment and there are only three specific issues in terms of sensitivity analysis of results:

- It is known that the sample of social ventures was slightly skewed towards younger and smaller social ventures more likely to take a variety of investment products other than secured loans. This may have inflated the impact figures to a small extent concerning enhanced venture and job creation especially by a growing company – compared to, say, a slightly larger venture taking a large secured loan (mortgage) to buy a building;
- The survey respondents do not, of course, include any social ventures that may have defaulted on their loan (and likely folded) – although default rates are known to be significantly lower amongst social ventures compared to the general business population; and
- We have erred on the side of caution in terms of the persistence effects of investments and their impact on ventures. These effects might be expected to go beyond the length of time of the finance period. This is undoubtedly a conservative position to hold in terms of future benefits and impact.

Social investment, SMEs and economic impact

A similar economic impact assessment exercise to this report was undertaken in 2010 to measure the economic impact of the CDFI sector⁴². CDFIs lend to all types of SME (social enterprises and purely commercial organisations) that, in the main, are ‘viable but unbankable’. The 2010 assessment both illustrated and concluded that the CDFI sector offers value for money for public investment given its target markets, economic and social outcomes.

The impact at regional scale for CDFI lending and social investment are shown in the below table (the CDFI evaluation did not measure national impact).

Notably, it can be seen that investment in social ventures by SIFIs (including CDFIs) generated more economic impact per £1,000 of investment than was the case for investment by CDFIs in the ‘unbankable’ SME population as a whole.

Unit of economic impact	Net additional economic impact per £1,000 of investment (regional scale)	
	SIFI economic impact (2013)	CDFI economic impact (2010)
Businesses created/safeguarded	0.03	0.01
Jobs (FTE) created/safeguarded	0.54	0.06
Annual turnover (£) created/safeguarded	£12,100	£3,900
Annual GVA (£) created/safeguarded	£3,500	£800

⁴² BIS/OCS/GHK (2010) *National Evaluation of Community Development Finance Institutions*.

Care should be taken with these results – especially as these results are based on surveys of business undertaken in 2013 and 2010, under very different economic conditions. It is also known that CDFIs tend to invest in riskier SMEs than would be the case for social ventures – given the different nature of market failures in mainstream finance for the two cohorts – and almost certainly that CDFIs invest more in sole traders and micro businesses (many of whom will not grow).

Nevertheless, the 'direction of travel' is quite clearly a message which places social investment squarely alongside other economic development initiatives in terms of its economic impact.

Source: BIS/OTS/GHK (2010) National evaluation of Community Development Finance Institutions; ICF GHK (2013) Growing the social investment market: the landscape and economic impact

5.6 Summary

- **The survey of social ventures** provides a detailed profile of the nature of the organisations that access investment from the SIFI sector. Almost all consider themselves to be social ventures, most are small (employment and turnover), the majority serve local or regional markets, and almost all operate within the service sector. Most of their profits are used to further their social and/or environmental goals, and there is considerable diversity in their objectives, which range from social/community outcomes, through environmental and conservation aims, to personal development and training objectives.
- Loans were the most common financial product accessed by social ventures, with a small number receiving equity investments. A sizeable proportion of survey respondents had accessed combinations of types of investment product, with grants and loans forming a frequent combination. Finance was typically used to support venture growth, though a substantial proportion of social ventures used SIFI support to enable them to start-up (and would not have done so without this investment).
- The majority of social ventures had sought to access finance from another source around the same time that they accessed investment from their SIFI. The social ventures who did apply for finance from an alternative provider (typically their bank or building society) were usually unsuccessful.
- Some social ventures only applied to their SIFI for investment, whilst others were successful in other applications but chose their SIFI instead.
- **This report provides the first comprehensive attempt to assess the economic impact of UK social investment. The gross economic impact over the lifetime of the finance period for the 765 investments provided by SIFIs, were:**
 - The creation/safeguarding of a total of 340 social ventures;
 - The creation/safeguarding of 6,870 FTE jobs;

- The creation safeguarding of just under £200m of annual turnover, equal to £58m in annual GVA; and
- As at May 2013, the closure of a total of 220 social ventures was prevented and subsequently some 1,840 jobs preserved.
- **At a regional economy level, net additional economic impact** was:
 - 210 social ventures created/safeguarded;
 - A total of 3,550 FTE jobs created/safeguarded over the whole finance period;
 - Some £77m in annual turnover created/safeguarded, equivalent to £23m in annual GVA;
 - Around £30,220 of investment will create/safeguard a social venture, whilst £1,840 is required to create/safeguard one net additional FTE job; and
 - £0.28 of social investment generates £1 of additional annual GVA
- **At the level of the UK economy, net additional economic impact** was much reduced, primarily due to the high level of displacement:
 - A total of 30 social ventures were created/safeguarded at a UK level as a result of the 765 social investments;
 - 610 net additional FTE jobs were created/safeguarded;
 - Some £4m of net additional annual GVA was added to the UK economy;
 - Around £10,680 is needed in order to support the creation/safeguarding of a net additional FTE job; and
 - £1.69 of social investment is required to generate £1 of additional annual GVA.
- **Over a three or five year investment term**, £1,000 of social investment would generate:
 - £10,280 (three years) or £16,570 (five years) of net additional GVA at regional level; and
 - £1,720 (three years) or £2,770 (five years) of net additional GVA at national level.

6 Conclusions

6.1 The growing UK social investment market

In 2011/12, the UK social investment market grew to £202m per annum through 765 deals, reflecting growth of almost a quarter from the 2010/11 market value figure of £165m in England.

This growth was evident across the full range of social banks, small and large SIFIs and totalled an increase of almost a quarter in value on the previous year; close to the previously expressed ambitions of the SIFI sector to grow by 35% per annum⁴³.

Market developments suggest that the pool of SIFIs who “have the necessary scale and performance characteristics to accept meaningful capital injections from Big Society Capital”⁴⁴ has increased slightly.

However, whilst the diversity of social investment products on offer grew, actual usage in the market remained very limited – with secured lending increasing its dominance.

Uncertainty exists, also, on the ability of the social investment market to meet demand in 2012/13.

6.1.1 The SIFIs

Whilst a handful of SIFIs exited the market, it would seem that they were replaced – including by the tentative entry of a mainstream bank. In sum, investment totals increased substantially to over £200m whilst overall numbers of investing SIFI remained static and their employment of staff increased slightly.

Overall:

- Social banks remained the dominant players in the social investment market (over 80% of the market – almost entirely comprised of secured lending using deposit funds);
- Social bank dominance of the social investment market is, however, under increasing ‘challenge’ from a set of almost a dozen large SIFIs whose volume and value of deals continues to grow substantially. This growth is based upon a broader portfolio of products – although secured lending remains the dominant product followed by unsecured lending – which is, in turn, based upon an increasing diversity of sources of finance; and
- A tail of small SIFIs exist, most of whom are not operationally sustainable at present. The evidence suggests, however, that it is within these SIFIs that the greatest diversity of products may be on offer.

Given that the social banks and large SIFIs are almost all national in their coverage, on the face of it there appears to be substantial provision of social investment finance across the Devolved Administrations and English regions. Furthermore, the evidence available suggests that SIFI investments are not concentrated in any one region (or Devolved Administration), within any one

⁴³ See Boston Consulting Group & The Young Foundation (2011) – Op Cit.

⁴⁴ Ibid. p.9.

sector, or to achieve any one set of social and environmental outcomes. This both reinforces London's presence and highlights other developing areas within the UK.

Almost half of SIFs reported operational sustainability in 2011/12, although it was harder to achieve for the smallest SIFs.

In conclusion, market developments suggest that the pool of SIFs who "have the necessary scale and performance characteristics to accept meaningful capital injections from Big Society Capital"⁴⁵ has increased slightly.

6.1.2 The products on offer

In terms of value, secured lending has increased its share of the social investment market to over 90% of the market.

This growth in this share of secured lending was driven both by an increase in investment values and an actual decrease by value in unsecured lending and equity-based investments. Fewer than 50 equity-based investments (3% of total social investment) were made in 2011/12. Quasi-equity is a tool that could be used to provide capital to charities or social ventures who do not offer share capital, but this only represented by 0.2% of the total value of social investment.

Diversity of products offered was most evident amongst a few SIFs (large and small) – who dominated both equity and Social Impact Bond offerings in terms of deal volume.

In conclusion, whilst the diversity of products on offer grew, actual usage in the market remained very limited – with secured lending increasing its dominance.

6.1.3 Expressed demand and investment plans

Investment totals saw a substantial increase between 2010/11 and 2011/12 and SIFs reported that, in most cases, they met only around half of expressed demand by social ventures. Almost all SIFs continued to express their plans to grow their investments, with half planning to achieve this partly through the launch of new products.

Previous research⁴⁶ has evidenced that there is a 'mismatch' in the social investment market in terms of the type of capital sought (high risk, unsecured capital) and the most readily available capital on offer (secured).

This evidence of a mismatch between demand from social ventures for high risk capital and supply is reinforced by the research findings presented in this report.

6.2 The economic impact of the growing UK social investment market

This report provides the first comprehensive attempt to assess the economic impact of UK social investment.

Over the lifetime of the finance period for the 765 investments provided by SIFs, the gross economic impact were:

- The creation/safeguarding of a total of 340 social ventures;
- The creation/safeguarding of 6,870 FTE jobs;

⁴⁵ Boston Consulting Group & The Young Foundation (2011) – Op Cit. p.9.

⁴⁶ Big Lottery Fund/Clearly So/NPC (2012) – Op Cit.

- The creation/safeguarding of just under £200m of annual turnover, equal to £58m in GVA; and
- As at May 2013, the closure of a total of 220 social ventures had been prevented and some 1,840 jobs preserved.

Concerning the generation of net economic impact, it would cost:

- Around £30,220 of social investment to create/safeguard a social venture, and £1,840 to create/safeguard one net additional FTE job at regional level;
- Around £211,520 of social investment to create/safeguard a social venture, and £10,680 to create/safeguard a FTE job at national level; and
- £0.28 of social investment at regional level and £1.69 of social investment at national level to generate £1 of net additional GVA.

Over a three year investment term, £1,000 of social investment would generate:

- £10,280 of net additional GVA at regional level; and
- £1,720 of net additional GVA at national level respectively.

The UK social investment market is offering strong investment and finance support to UK social ventures across the (generally service) economy. This includes a substantial number of start-ups. This is especially important given the evidence in this report which shows that the majority of social ventures continue to be rejected for finance from other (generally mainstream finance) sources.

This report provides the first comprehensive assessment of the economic impact of social investment across a number of impacts – both at the scale of the regional and national economy.

At a **regional economy level**, net additional economic impact was:

- 210 social ventures created/safeguarded;
- A total of 3,550 FTE jobs created/safeguarded over the whole finance period;
- Some £77m in annual turnover either created/safeguarded, equivalent to £23m in GVA;
- Around £30,220 of investment will create/safeguard a social venture, whilst £1,840 is required to create/safeguard one net additional FTE job; and
- £0.28 of social investment generates £1 of additional GVA.

At the **level of the UK economy**, net additional economic impact was much reduced, primarily due to the high level of displacement:

- A total of 30 social ventures were created/safeguarded at a UK level as a result of the 765 social investments;
- 610 net additional FTE jobs were created/safeguarded;
- Some £4m of net additional GVA was added to the UK economy;
- Around £10,680 is needed in order to support the creation/safeguarding of a net additional FTE job; and
- £1.69 of social investment is required to generate £1 of additional GVA.

6.3 The business case for social investment

6.3.1 Social investment: responding to growing demand and delivering economic and social outcomes

The ability of social ventures to create wealth and balanced economic growth, deliver innovative goods and services (especially in public services), promote social and environmental change and support the poorest and most disadvantaged in society has been increasingly demonstrated in the last decade. This ability has been recognised by successive Governments in recent times (through, for example, their creation of social enterprise strategies and action plans) and a range of policy and market drivers continue to create the conditions for the sector to expand.

In turn, the social sector is responding – creating new and re-energised forms of start-up (for example, Community Interest Companies, social firms, charities which trade, and co-operatives). Earned income from consumers is now the largest income stream for social ventures and, in 2010/11, over half the income of the voluntary sector was achieved through traded income⁴⁷. In 2012 a smaller proportion of social enterprises received income through grants and donations – 15% of social enterprise SME employers reported doing so in 2012, down from 23% in 2010⁴⁸.

Alongside entrepreneurship, innovation and skill, such growth has only been achieved through access to investment and finance. Moreover, it is generally accepted among social ventures, Government, the European Commission and stakeholders that social ventures would be able to achieve more – expanding existing goods and services, taking up new opportunities and reaching scale – if they had access to the finance they require ('social investment').

This report provides further evidence that the UK social investment market continues on its path to maturity – growing apace and reaching £202m in value in 2011/12 comprising 765 deals. Such growth has been delivered by an ever strengthening cohort of around 30 investing SIFs (including social banks and CDFIs), in total providing UK-wide coverage and an increasing diversity of social investment products.

Nevertheless, the majority of these SIFs report that they were able to meet fewer than half of the requests they received for social investment in 2011/12 – and secured lending increased at the expense of unsecured lending and equity based investments. Most recently, for example, CDFA/RBS Group estimated the potential funding gap for social ventures to be in the order of £1.3bn and £2.1bn per annum⁴⁹.

Whilst this report, then, provides tentative evidence that the supply of finance to SIFs may have improved over the last 12 months or so, it also reaffirms the continued barriers to growth of a lack of a pipeline of investment ready demand, and a mismatch in the funding sought by social ventures and this which is on offer, and the only early development of a robust and efficient market infrastructure⁵⁰.

⁴⁷ See ICF GHK for CDFA & RBS (2013) – Op Cit.

⁴⁸ BMG Research for Cabinet Office (2013) – Op Cit.

⁴⁹ ICF GHK for CDFA & RBS Group (2013) – Op Cit.

⁵⁰ Cabinet Office (2011) – Op Cit.

6.3.2 Social investment: responding to demand and contributing to the UK economy

Alongside the social returns, which are the *raison d'être* of social investment, this report provides an understanding and an estimate of the contribution of social investment to the UK economy – its economic impact.

As the social investment market grows, it is important to develop robust metrics for economic as well as social impact to measure the full return on public and other investment and to instil confidence and secure investment and funding over the longer term. Whilst substantial work continues to create frameworks to measure, monetise and value the social outcomes of social investment⁵¹, there has been no up-to-date, comprehensive and robust attempt to assess the economic impact of social investment.

This report has calculated that the gross economic impact over the lifetime of the finance period for the 765 investments provided by SIFs was:

- The creation/safeguarding of a total of 340 social ventures;
- The creation/safeguarding of 6,870 FTE jobs;
- The creation/safeguarding of just under £200m of annual turnover, equal to £58m in GVA; and
- As at May 2013, the closure of a total of 220 social ventures and the potential loss of some 1,840 jobs had been prevented.

At a regional economy level, net additional economic impact was:

- 210 social ventures created/safeguarded;
- A total of 3,550 FTE jobs created/safeguarded over the whole finance period; and
- Some £77 in annual turnover either created/safeguarded, equivalent to £23m in GVA.

At the level of the UK economy, net additional economic impact was reduced, primarily due to the high level of displacement:

- A total of 30 social ventures were created/safeguarded at a UK level as a result of the 765 social investments;
- 610 net additional FTE jobs were created/safeguarded; and
- Some £4m of net additional GVA was added to the UK economy.

At the national level, the high level of displacement implies that social ventures are more active in competing for markets within the UK economy, rather than creating new markets.

6.3.3 The business case for social investment: valuing the full economic and social benefits and impact of lending activity

The social investment market exists because there are a substantial and growing number of social ventures who cannot access investment and finance from commercial markets – or can only do so on terms which do not consider the value of their social outcomes. In contrast, and explicitly, social investment is the

⁵¹ See, for example, <http://inspiringimpact.org/>

provision and use of repayable finance to generate *social* as well as financial returns.

Whilst work has continued to refine the measurement and valuation of the social returns generated by social ventures, to date, no corresponding comprehensive assessment has been undertaken of the additional value of the economic impact of social investment.

This report provides such an assessment – and to the extent that social investment is shown to deliver both substantial and efficient economic impact (especially concerning jobs, and at the regional level).

For example, at the regional level it costs around £30,220 of social investment to create/safeguard a (net) social venture, only £1,840 to create/safeguard one net additional FTE job and only £0.28 to generate £1 of net additional GVA. Similarly, it costs only around £10,680 to create/safeguard a net additional FTE job at national level.

Or, put another way, over a three year investment term, £1,000 of social investment would generate £10,280 of net additional GVA at regional level; and £1,720 of net additional GVA at national level.

Furthermore, it is the term 'additional economic impact' which is the key here. In the BIS/OCS (2010) *National evaluation of Community Development Finance Institutions* it was concluded that whilst the business case for investment could be made on the economic impact generated by the sector, the lack of valuation of its additional social impact implied under-reporting of, for example, the return on public investment that CDFIs can deliver. In contrast, the reverse argument is true for social investment.

The business case for social investment

This report has calculated the significant economic benefit and impact of social investment generated for the UK economy – and even more notably at regional level.

This economic impact should be understood as in addition to the value of the social benefit and impact whose delivery is the core objective of social ventures.

The business case for social investment should then be understood as one of: competing effectively in the face of continued growth of demand, delivering wide-ranging social benefits and impact, and in so doing creating significant additional impact for the UK and its regional economies.

It is within this decision framework that the full value of social investment and any reporting of return on (public) investment should be considered.

6.4 Constraints and barriers to growing the market

The social investment market continues to grow – at a steady rate and when lending in the general economy to SMEs continues to flat line at best. SIFI provision continues to expand – with some evidence of a small amount of healthy 'churn' and 'herding' with parallel investor portfolios amongst providers – and amidst the continued introduction of new products.

Our research indicates that a wide range of organisational structures and types exists within social ventures, including small community groups that seek to deliver local services to high growth potential start-ups that could achieve national scale. These different organisations require different types of finance depending on their ambitions and organisational stage. Indeed, distinct types of investors are likely to be required at each stage of an organisation's development.

Nevertheless, the evidence in this report suggests that there is room for development in the market. Currently there are less than a dozen substantial providers of social investment and deal value is dominated by social banks offering secured loans. Overall, the value of equity based products reduced in 2011/12. The similarity of rates of return across products remains puzzling and, on the face of it, contradictory, and is set alongside the substantial variation in rates offered by providers. SIFIs remain the only choice for finance for large numbers of (rejected) social ventures but they rarely 'shop around'. Whilst SIFI coverage is national, there are indications that regional presence remains limited especially when seeking a diversity of product.

In turn, SIFIs report difficulties in meeting demand – but also note the lack of attractive social ventures to invest in and the current high transaction costs of deals – and sustainability remains an on-going challenge.

With the exception of the provision of secured debt, social ventures may potentially remain unable to access the right type of finance for their organisation. To date, equity has tended to be neglected by social investors due to the organisational structure of social ventures (i.e. a lack of profit distribution mechanisms), inability of business models to generate returns that reflect the investment risk and lack of exit opportunities (i.e. no route to Initial Public Offering (IPO), few potential trade buyers, no secondary investment market). The equity gap is potentially restricting the development of (particularly high growth potential) social ventures because equity allows more flexibility as an early stage financing tool than debt⁵².

Big Society Capital is already taking a lead in product development within the sector and there are a variety of opportunities where Government and other providers of capital could intervene. This could include, for example, encouraging greater appetite from social ventures for alternative types of finance, and reducing grant dependency, by introducing convertible grants (to equity) and/or contingent debt (convertible to a grant). The potential for angel investment in the social investment market is yet to be fully realised and there is a need to increase the supply of risk capital, for example through the development of angel networks and related activities and even new financial engineering instruments made available through European Structural Investment Funds.

This is not to say that both progress and initiatives to overcome barriers are not evident. SIFIs in this report seemed less concerned with the supply of finance as Big Society Capital ramps up. During 2012/13 the UK Government has sought to make it easier for social ventures to grow by making it easier for them to access funding. It has introduced, for example, a £20m Investment Readiness Programme including:

⁵² The launch of the Social Stock Exchange in June 2013, aims to address this equity gap.

- A £10m Investment and Contract Readiness Fund (ICR) to help established social ventures secure social investment and bid for public service contracts; and
- A £10m Social Incubator Fund, which specifically targets social incubators and will help them provide investment and support to early stage social ventures.

Also, the £20m Social Outcomes Fund will provide top-up payments that unlock Social Impact Bonds or payment by results projects that work on complex and expensive social issues. Meanwhile, in Europe, the Social Business Initiative will soon support the development of new European funds and financial instruments for social ventures.

These and other initiatives will support market development including the key issue of the need to reduce transaction costs for SIFs, and a broader strengthening of their business models around the combination of investment and financial and business services.

In conclusion, the social investment market continues to grow healthily alongside the sector it serves. If, since 2010/11, there is nascent evidence that capitalisation and supply of funds may be easing with the tentative appearance of new investor groups (and Big Society Capital), evidence remains that the continued demand for social investment is:

- Not matched by the investment readiness of that demand; and
- Remains constrained by the infrastructure and capacity of the market and its intermediaries to respond.

At the present time, for every social investment deal that is not completed, this report shows that a considerable set of economic as well as social impacts are lost to UK society and its economy.

Annexes

Annex 1 Survey instruments

A1.1 Mapping social investment: survey of Social Investment Finance Intermediaries, 2011/12

A1.2 Economic impact of social investment

Available separately online at: www.cityoflondon.gov.uk/economicresearch

Annex 2 Economic impact assessment methodology

The economic impact assessment was designed to be compliant with Government guidance on assessment methodologies, as set out in the HM Treasury Green Book⁵³. Specifically, there are two key considerations:

- *The impact assessment should focus on impact as opposed to output*: output is the measure of the scale of SIFI investment activity; impact describes the changes within social ventures that result from this investment activity. The following economic impacts have been measured:
 - Impact on the stock of social ventures, measured through the number of social ventures created and safeguarded (i.e. preventing from closing) as a result of SIFI investment activity;
 - Impact on employment, measured through the number of FTE jobs created and safeguarded in social ventures supported by SIFI investment activity;
 - Impact on business income, measured through the annual turnover of social ventures supported by SIFI investment activity; and
 - Impact on Gross Valued Added (GVA), measured through the GVA created and safeguarded as a result of SIFI investment activity. GVA has been calculated by applying a ratio of GVA-to-turnover to the annual turnover created and safeguarded within social ventures as a result of SIFI investment activity⁵⁴.
- These impacts have been selected as the standard measures of the economic impact of an intervention, but it should be noted that social investment by SIFIs will generate other economic impacts that it is not been possible to calculate. For example, social ventures may be able to provide products and services more efficiently than other businesses, in which case customers would benefit from lower costs and, of course, they generate social returns. Measuring this impact, however, would require fieldwork with the customers of social ventures, which was not possible within the parameters of this research.
- *Both gross and net economic impact needs to be calculated, taking into account additionality considerations*: HM Treasury Green Book Guidance stipulates that the following additionality factors should be taken into account when measuring net economic impact (explored in more detail below):
 - *Deadweight*: the proportion of impact that would have been achieved anyway, and thus cannot be attributed to SIFI investment activity;
 - *Displacement*: the share of impact that have been achieved at the expense of other businesses within the target area;

⁵³ HM Treasury (July 2011) The Green Book: Appraisal and Evaluation in Central Government; available at <https://www.gov.uk/government/publications/the-green-book-appraisal-and-evaluation-in-central-government>

⁵⁴ The ratio (0.293:1) was derived from the 2011 Annual Business Inquiry (total GVA divided by total turnover), available at <http://www.ons.gov.uk/ons/publications/re-reference-tables.html?edition=tcn%3A77-276587> (Annual Business Survey 2011P - sections A-S: UK Business Economy)

- *Leakage*: the proportion of impact that benefit individuals or businesses outside of a target area; and
- *Economic multipliers*: further economic impact generated through the additional expenditure of assisted social ventures (e.g. through their supply chains), or the employees of assisted social ventures.

The method of approach employed for the economic impact assessment has been based on a number of other assumptions and considerations:

- Gross impact data have been obtained from the results of the survey of social ventures. Recipients were asked to report:
 - Employment and turnover when they received their investment, at the time of the survey, and also to estimate what their employment and turnover would have been at the time of the survey had they not received their investment. On this basis it was possible to calculate the employment and turnover/GVA creation and safeguarding that could be attributed to the SIFI investment (as opposed to wider economic conditions);
 - Whether the investment they received had enabled them to start their business or prevented it from closing, on which basis it was possible work out the number of businesses created/ safeguarded as a result of SIFI investment; and
 - Whether they believed that their employment/turnover would increase through to the point in time at which their financing period would finish (if it had not already done so), in order to take into account future economic impact of outstanding investments.
- Spatial scale is a key consideration within an economic impact assessment, since the additionality factors shown above vary depending on the geographic unit of analysis (the 'target area'). For the purposes of this research, the economic impact of SIFI investment has been presented at two spatial scales:
 - *The region*: defined as an area up to 50 miles from a social venture's main centre of operations; and
 - *The UK*.
- In order to calculate the economic impact of the social investment market as a whole, the impact obtained from the survey of social ventures were grossed up. In the absence of data on the number of outstanding investments in the UK, we have grossed up on the basis of the number of investments known to have been made in 2011/12 (i.e. 765 investments).

Measuring additionality

Additionality is a measure of the extent to which the intervention in question (i.e. SIFI investment activity) generates impact that would not have happened in the absence of the intervention (i.e. if social ventures had not accessed finance from SIFIs). Measuring additionality requires quantification of: deadweight, displacement, leakage, and economic multiplier effects. The measurement of each of these additionality components was based on primary research with businesses carried out through the social venture survey (see Table A2.1 for a summary of the methodology). Additionality was calculated for each individual

survey respondent, and summed to provide a figure for the net economic impact of the social venture sample as a whole.

The overall additionality ratios for each of the components of additionality are shown in Table A2.1 which provides values for additionality at both a regional and national scale:

- Deadweight, at 16% was relatively low, highlighting the fact that for the most part, social ventures believed that they could not have accessed the investment that they received from their SIFI from another source. This suggests that market failures in the provision of finance to social ventures are still a significant problem;
- Displacement was high, particularly at the level of the UK economy, where an estimated 95% of economic impact was generated at the expense of other businesses (whether social ventures or not). This is not surprising given the nature of most of the social ventures surveyed, which tended to serve local or regional markets. It should be noted, however, that there may be economic benefits to displacement, for instance if social ventures are able to deliver products and services more efficiently than other businesses (which may be why they are able to compete), since this would generate – unmeasured – cost savings amongst their customers; and
- Just as social ventures tended to compete on a local/regional scale, so they also sourced supplies locally and served local markets. As a result, the multipliers associated with investing in social ventures were high (particularly at a national level), as supply chain expenditure generated additional ‘waves’ of economic benefits.

Table A2.1 Overview of the additionality components used in the economic impact assessment

Additionality component	Regional scale	National scale	Summary of methodology
Deadweight (minus)	16%	16%	<ul style="list-style-type: none"> • To measure deadweight, social ventures were asked whether they could have accessed the investment that they received from their SIFI from another source: <ul style="list-style-type: none"> ○ If they could have accessed the same amount of finance in the same time period, deadweight was assumed to be 100%; ○ If they would have had to access less finance, social ventures were asked to identify how much less, and deadweight was assumed to be this figure as a proportion of the finance they accessed from their SIFI; ○ Some social ventures believed they could have accessed the same amount of finance but at a different

Additionality component	Regional scale	National scale	Summary of methodology
			<p>point in time. Where the delay was 12 months or longer, deadweight was assumed to be 0%; where the delay was less than 12 months, or if they could have accessed finance quicker had they not used their SIFI, deadweight was assumed to be 100%;</p> <ul style="list-style-type: none"> ○ If they could not have accessed finance, deadweight was assumed to be 0%; ● Deadweight was applied to business impact, employment impact, and turnover/GVA impact.
Displacement (minus)	53%	95%	<ul style="list-style-type: none"> ● Social ventures were asked to estimate the proportion of their direct competitors who were located within 50 miles of their centre of operations, and who were located within the UK; ● Displacement was applied to business impact, employment impact, and turnover/GVA impact.
Leakage (minus)	10%	0%	<ul style="list-style-type: none"> ● Social ventures were asked to estimate the proportion of their employees who resided beyond 50 miles of their centre of operations, and who resided outside of the UK; ● Leakage was only applied to employment impact, as other impacts are considered fixed.
Economic multipliers (plus)	66%	92%	<ul style="list-style-type: none"> ● Social ventures were asked to estimate the proportion of their customers and suppliers who were located within 50 miles of their centre of operations, and who were located within the UK. The proportion of suppliers was multiplied by the proportion of customers to produce a composite multiplier estimate; ● Economic multipliers were applied to business impact, employment impact, and turnover/GVA impact.

Annex 3 Organisations engaged in the research

ABI Associates - Faith in Business 'Phoenix Fund'	Esmee Fairbairn Foundation
Acorn (Hull Business Development Fund Ltd)	Ethex
Aspiren	Finance South East
Association of Charitable Foundations	Finance South Yorkshire
Aston Reinvestment Trust	Finance Wales
Avon CDA	First Enterprise Business Agency
Barrow Cadbury	Foundation East
BCELF	Friends Provident Foundation
BCRS Small Business Loans	Goole Development Trust
Bethnal Green Ventures	HBV Enterprise
Big Issue Invest	HSBC
Bond for Hope Limited	Impetus (Marches Rural Reinvestment Trust)
Bradford Enterprise Agency	Investing for Good CIC
Bridges Ventures	ISE
Bristol Enterprise Development Fund	Jane Ryall - Success for social enterprise
Bromley by Bow Centre	Key Fund
Building Change Trust	Lancashire Community Finance
Business Mind Social Purpose	LankellyChase Foundation
CAF Venturesome	Lincolnshire Community Foundation
Capital For Enterprise	Lloyds TSB
Capitalise Business Support Ltd	Local Partnerships
Charity Bank	Locality
City Bridge Trust	London Rebuilding Society
ClearlySo	Marmanie Impact Investing Advisory
Communitites for Renewables	Moneyline Yorkshire
Community Action Network (CAN)	MSIF
Community First	NESTA
Community Foundation Network	New Economics Foundation
Co-operative and Community Finance	Norfolk & Waveney Enterprise Services
Coventry and Warwickshire Reinvestment Trust	North Lincolnshire Developments
Cumbria Community Asset & Reinvestment Trust	North London Community Finance
CWCDA	North London Credit Union
Deutsche Bank	North Staffordshire Risk Capital Fund
Development Trusts in Northern Ireland	Northamptonshire Enterprise Ltd
Donbac	Northern Pinetree Trust
East Lancs Moneyline	Nottingham Business Venture
East London Small Business Centre	NPC
Eastside	Numbers 4 Good
Ecology Building Society	Panahpur
Enterprise Solutions Northamptonshire	Parity Trust
Entrust	Plunkett Foundation
	Private Equity Foundation

Rathbone Greenbank	Spirit of Enterprise
RBS	The Five Lamps Organisation
Resonance/ Community Land & Finance CIC	The Hub (Westminster)
Rootstock Ltd	The School for Social Entrepreneurs
Santander	The Social Business Trust
Shaftsbury partnership	The Social Enterprise Loan Fund
Shared Impact	The Social Investment Business
Sheffield Co-operate Development Group Limited	Triodos Bank
Sirius	Ulster Community Investment Trust
Social Enterprise London	Unity Trust Bank
Social Enterprise NI	UnLtd
Social Finance Ltd	Volans
Social Investment Scotland	WCVA
Social Stock Exchange	WEETU
	West Yorkshire Enterprise Agency

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is a uniquely diverse organisation with three main aims:

- to support and promote the City as the world leader in international finance and business services
- to provide high quality local services and policing for those working in, living in and visiting the Square Mile
- to provide valued services to London and the nation as a whole, including its role as one of the most significant arts sponsors in the UK.

The City of London Corporation is playing a pivotal role in raising the profile of the social enterprise and social investment sector. The City of London's Economic Research programme provides analysis on issues affecting the City.

For more information visit www.cityoflondon.gov.uk/socialenterprise and www.cityoflondon.gov.uk/economicresearch

The Big Lottery Fund's overarching social investment goal is to play a catalytic role in developing the social investment marketplace. This is based on the belief that social investment offers new financing tools and access to new sources of capital to enable Voluntary, Community and Social Enterprise (VCSE) sector organisations to operate on a more sustainable footing, so they can better provide their services to people and communities most in need.

Having run several funding initiatives to support social investment since 2010, the Big Lottery Fund will be launching two major new funds this summer. Big Potential will be a £10m fund for VCSE organisations to move towards investment readiness and so improve their sustainability, capacity and scale to deliver greater social impact. The second initiative is a £40m Commissioning Better Outcomes fund to support the development of social impact bonds and other outcome-based investment instruments.

Big Society Capital is the world's first social investment bank. Big Society Capital was launched in April 2012, with an estimated £600 million of capital, £400 million of which will be from unclaimed assets left dormant in bank accounts for over 15 years, and £200 million from the UK's largest high street banks.

Big Society Capital's mission is to develop the social investment market in the UK by investing in social investment finance providers and by acting as a market champion. By improving access to finance for social sector organisations, and by raising investor awareness of investment opportunities that provide a social as well as a financial return, Big Society Capital will be instrumental in connecting the sector to capital markets.

The **Cabinet Office** supports the Prime Minister and Deputy Prime Minister, and ensures the effective running of government. It is also the corporate headquarters for government, in partnership with HM Treasury, and takes the lead in certain critical policy areas. This includes responsibility for growing the social investment market, helping the voluntary sector succeed and work with the state, and making it easier for people to give time and money to good causes.

The **Department for Work and Pensions** (DWP) is responsible for welfare and pension policy and is a key player in tackling child poverty. It is the biggest public service delivery department in the UK and serves over 20 million customers. In March 2012, HM Government published the cross-government strategy 'Social Justice: transforming lives', setting out its aspiration for Social Justice, which is led by DWP. The strategy set out our commitment to growing the social investment market, which will help unlock private capital to tackle deep rooted social problems.

Growing the Social Investment Market: The Landscape and Economic Impact