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Growth Fund Independent Evaluation

Update Report 2: Summary Report

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Up to 2020, the Growth Fund had made good progress. It had plugged a gap in the supply of social investment for voluntary, community and social enterprise orgsanisations (VCSEs). This in turn was strengthening VCSEs' financial resilience and increasing their ability to support a wider set of service users. It had increased the number of social investors in this space and increased social investor capabilities. Some aspects of the programme have, inevitably, been more successful than others. Perhaps the most challenging aspect of the programme has been supporting new and sub-sector specialist social investors to operate financially viable investment funds. There is, therefore, much to take from the Growth Fund into future blended finance programmes, and areas to experiment with further.

The Growth Fund is facilitated by an innovative partnership between The National Lottery Community Fund, Big Society Capital and delivered by Access (collectively known as the Programme Partnership). Launched in 2015, it offers unsecured loans and grants of up to £150,000 to organisations which are unlikely to have taken on social investment before. In 2016, Ecorys and ATQ Consultants were commissioned to evaluate the programme. This Update Report 2 is the second evaluation report, and reports on the progress and impact of the Growth Fund up to the end of 2020. It is a Summary Report; a Full Report is also available.

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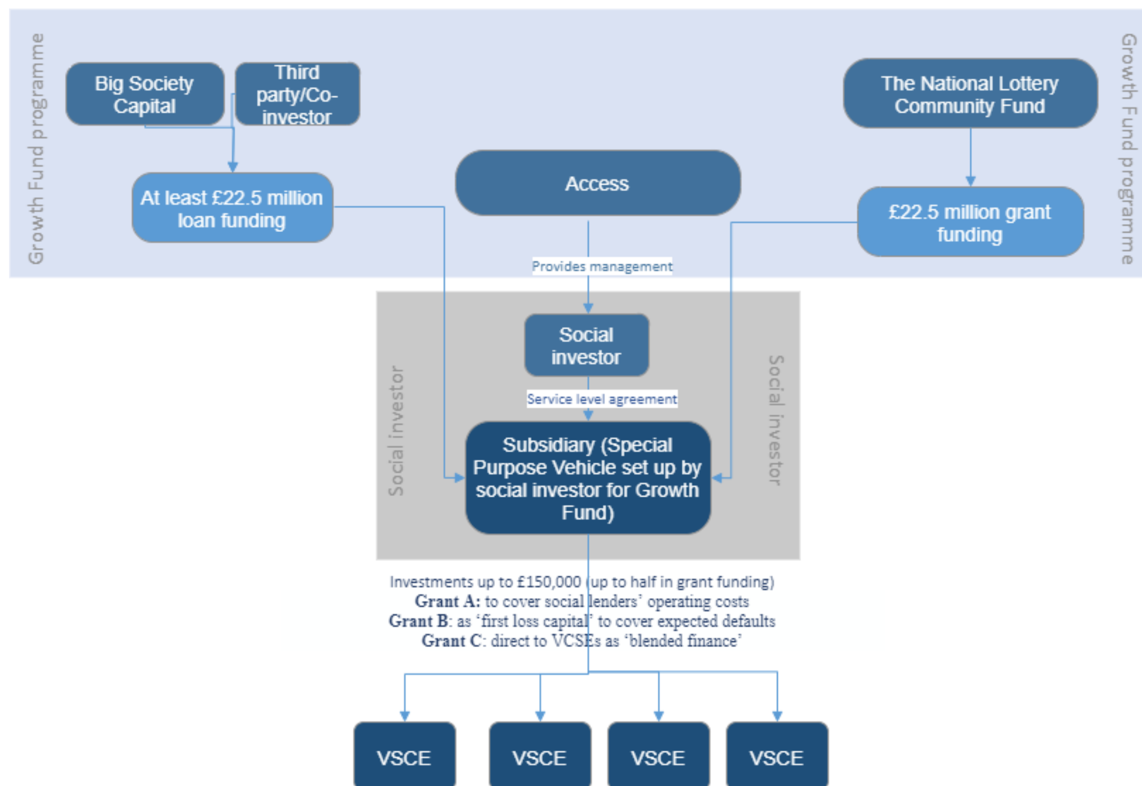
The Growth Fund and evaluation

- In the Growth Fund, The National Lottery Community Fund provides grant funding of £22.5 million, and Big Society Capital provides loan funding of at least £22.5 million. Third party investors (or co-investors) are able to invest alongside the grant. The management of the Growth Fund is led by Access. Investments of both loans and grants are made into 16 funds run by 15 social investors (one investor runs two funds), who then make loans and blended loan/grant packages into voluntary, community and social enterprise organisations (VCSEs). The social investors are expected to repay the loan to BSC, including interest. Part of the grant funding from The National Lottery Community Fund helps to underwrite some of the capital, based on estimates of a likely default rate. Figure 1 provides an overview of the structure of the Growth Fund.

Figure 1: Growth Fund structure

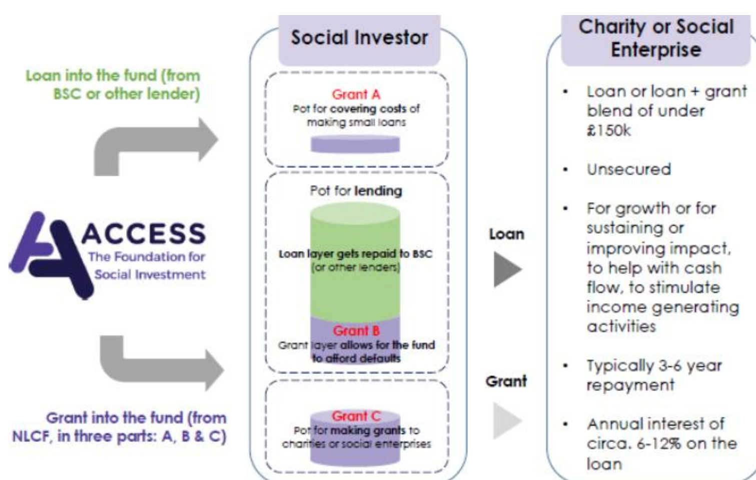


- The National Lottery Community Fund commissioned Ecorys UK, in partnership with ATQ Consultants, to evaluate the Growth Fund. The evaluation runs until 2022, and aims to assess and track the effectiveness of the Growth Fund in enabling a wider group of charities and social enterprises to successfully access social investment, become more resilient and deliver greater social impact. The following activity took place up to February 2021 and fed into this report:
  - Case study visits to 13 VCSEs that received social investment (five visited twice)
  - Analysis of Growth Fund Management Information up to September 2020. This contained information on 795 loans and grant applications from VCSEs
  - VCSE surveys – baseline n=108; two annual surveys (2019, n=46; 2020, n=41)

- Consultation with one unsuccessful VCSE applicant[1]
- Consultations with 13 social investors
- Consultations with three unsuccessful social investor applicants
- Consultations with seven people from the Programme Partnership.

- The Growth Fund uses the grant in three ways, known as Grants A, B and C. These are summarised in Figure 2 and detailed below:
  - Grant A helps to contribute towards the costs of making lots of small loans; so that the social investor can afford the proportionally higher transaction costs that can often exceed interest / fee income at this level
  - Grant B allows investors to be able to afford for some of the loans to fail; by blending grant and debt in the fund the social investor can afford for the portfolio as a whole not to break even and therefore will be willing to take greater risk on the loans that they make.
  - Grant C allows investors to offer grant alongside loans to VCSEs; this reduces the amount of loan finance required so that revenue streams are robust enough for repayment.

Figure 2: The National Lottery Community Fund grant uses



Progress in delivering the Growth Fund

The Growth Fund is increasing the supply of small-scale, unsecured social investment

- Up to September 2020 the Growth Fund social investors had deployed 505 loans and grants to 419 VCSEs. The total amount deployed was £31,773,091.
- Around a third (31%) of successful VCSEs delivered employment, education, and training activities, and a fifth (20%) delivered activities relating to mental health and wellbeing (see Table 1).

[1] Due to engagement access issues the evaluation team has not managed to interview unsuccessful VCSE applicants. The evaluation team is working with the Programme Partnership to resolve this issue.

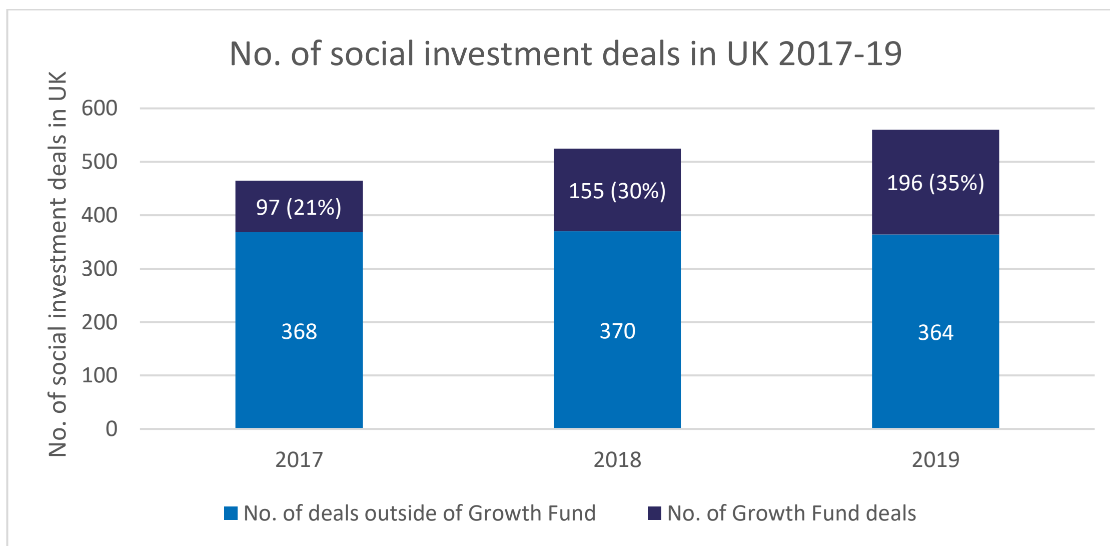
Table 1: Category of activities delivered by VCSEs

Category of activity	Percentage (%)
Employment, education, and training	31
Mental health and wellbeing	20
Mixed	15
Physical health	12
Housing and local facilities	8
Citizenship and community	7
Other	7

Source: Growth Fund Management Information (n=424)

- Stakeholders interviewed for the evaluation saw this as an impressive achievement, especially when this is considered within the wider landscape of social investment in the UK; Growth Fund deals accounted for over a third (**35%**) of all social investment deals recorded in BSC deals data in 2019 (Figure 3).

Figure 3: Growth Fund deals, as a percentage of all deals in UK for which deal-level data is available



Data source: BSC deals data: https://public.tableau.com/profile/big.society.capital#!/vizhome/DLD2019/Who. This is based on deal-level data only; the wider market is larger than this. Chart produced by Ecorys.

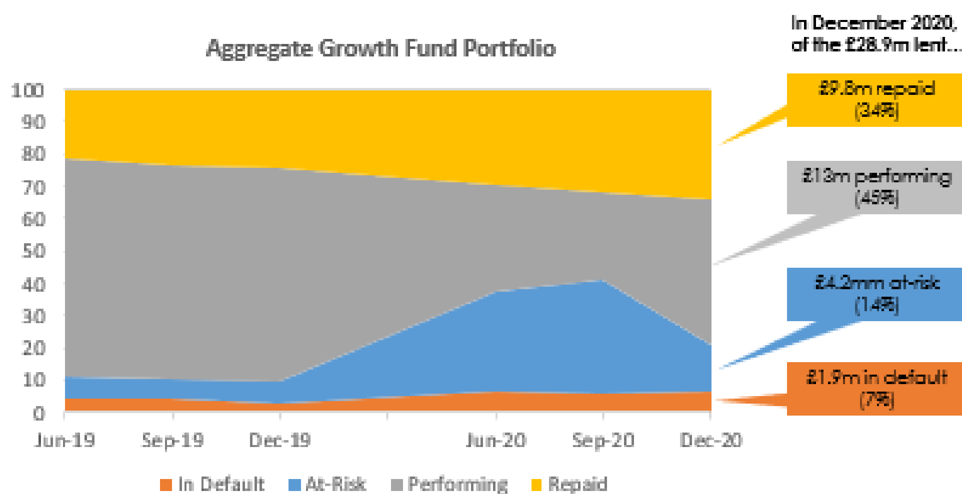
- There was significant variation in the progress of different social investment funds against projections. Stakeholders felt that the main challenge was in converting 'latent' demand for loans into 'actual' demand, which took far longer and more resource than first anticipated.
- It is too soon to draw conclusions on the success or otherwise of loan repayments.
- The Partnership has realised that although they all support the over-arching aim of the Growth Fund, they have different views as to how the Growth Fund should have been structured and which aspects should be prioritised during decision-making. There was general agreement that future similar programmes should avoid such a complex partnership structure, and that instead there should be one organisation with core responsibility and decision-making in relation to the grant giving (though views on what this should look like varied).

Responding to Covid-19

There was unanimous praise for how the Programme Partnership responded to the Covid-19 crisis.

- It is clear from the evidence that the pandemic impacted all VCSEs in some way, with some able to adapt their business model and keep operations going, while others had to reduce or stop their service offer.
- While some VCSEs were able to keep afloat financially, others struggled during the pandemic and had to take action to respond to financial challenges.
- Investors re-appraised their portfolios following the lockdown, and by June 2020 30% of Growth Fund loans were deemed at risk (though this was a precautionary measure recognising the uncertainty surrounding the pandemic)
- The Programme Partnership introduced a raft of changes to the Growth Fund in response. This included: financial breaks that enabled social investors to offer capital and interest repayment holidays; additional finance (providing additional Grant A and Grant C from The National Lottery Community Fund); freezing of BSC interest accrual to social investors during the six months after March 2020; and easing of administration requirements so investors could focus on providing direct support to VCSEs. When the six month interest-free period on social investors' BSC capital came to an end in September 2020 a further adjustment was agreed by the Growth Fund funding partnership, to provide greater flexibility going forward. This comprised: reducing overall interest accrued for repayment to BSC by the Growth Fund's social investors, by reducing future interest rate accruals on both current outstanding capital and future borrowing from 5% to 2%; and sharing any upside to this return 50/50 between the social investors and BSC. Because of the actions put in place by the Growth Fund and wider actors (i.e. the Government and other funders), overall in 2020 there was no substantial impact on VCSEs' ability to repay the Growth Fund loans. The percentage of loans deemed at risk by social investors reduced, and by the end of 2020 this had dropped to 14%, as social investors re-structured some of the loans (Figure 4). However, there are fears that things could prove more challenging for the funds in 2021 and beyond.

Figure 4: Performance of Growth Fund loans



Source: Access.

- Starting in July 2020 the Programme Partnership worked with the social investors to make a set of further changes to funds. All funds were reforecast and many were significantly restructured, including various changes to deployment period lengths, repayment period lengths, grant amounts/ ratios, and total fund size. Some funds chose to extend their deployment periods whilst others opted to wind-down and close early.

- There was unanimous praise for how the Programme Partnership responded to the Covid-19 crisis, from members of the Partnership and social investors. The Partnership was able to overcome challenges around decision-making and acted in a swift and collaborative manner. Social investors felt the Partnership could not have done more.

Impact of Growth Fund on investors

The Growth Fund has increased the number and capability of social investors operating in this space. Most hope to continue lending to this market in the future, potentially creating a sustained impact

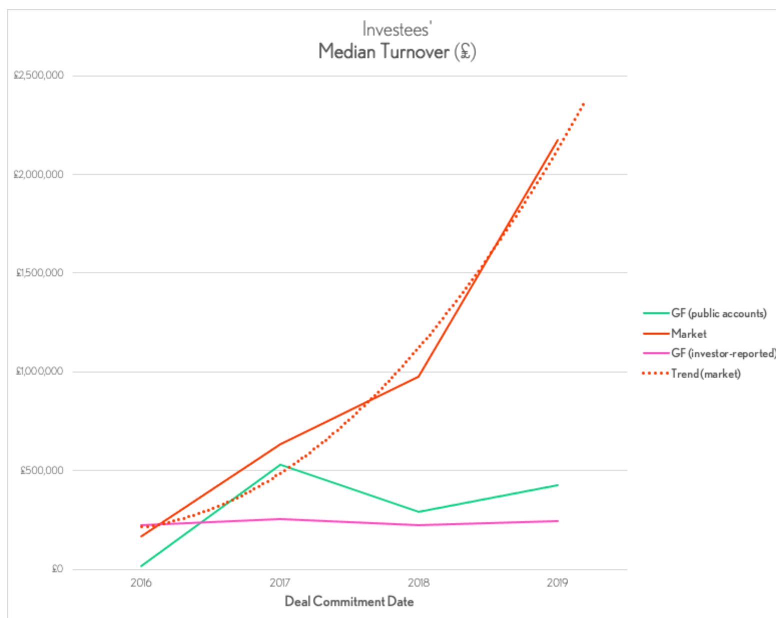
- The Growth Fund Theory of Change with respect to the social investors posits that, with the support from the grant subsidy, capacity and lending activity will increase. This will lead to improved social investor capabilities and sustained interest in the provision of unsecured lending to the sub<£150k loan market. This is so far proving to be broadly correct.
- The Programme partners successfully engaged with 15 social investors and broadened the number of players in the market. Not surprisingly, their experiences of managing respective funds has been mixed.
- The main reasons for the different experiences were a combination of factors, including levels of prior loan book management experience and specific sector and/or geographical focus. Generally, more experienced and more 'generalist' funds were more successful in deploying against their original projections, with organisations new to social investment and/or funds with a specific location and/or sector focus deploying below their forecasts.
- The experienced social investors and some of the new and specialised social investors intend to continue lending in this space after Growth Fund. Four social investors either have not, or will not, carry on. Given it was never expected that all organisations would continue to operate, at this point in time we deem that this means the Growth Fund has achieved its objective of garnering sustained interest in lending to the <£150k market. However, the social investors not continuing are all ones that set up new investment arms to deliver Growth Fund and so, in this respect, the sustainability of social investors operating as stand-alone Growth Fund partners is in question. All of the more experienced social investors that hope to carry on have diversified investment revenue streams and enjoy economies of scale through managing a variety of different investment programmes.
- For all social investors, the experience of managing a blended fund of this scale had increased their respective organisational capacity and capability. Even for those social investors not choosing to continue, the skills and experience gained will be applied in their grant management activities.
- What all of this shows is that becoming a new social investor is a challenging and time-consuming endeavour – whilst some will succeed and stay committed to the space, others will struggle and decide it is unviable. This creates a dilemma for those wishing to grow the social investment space – especially if the belief (supported to some degree by these evaluation findings) is that more specialist organisations add value to the sector. The Growth Fund appears to have shown that 'specialist' social investors can support in extending the reach of social investment, but that it can be problematic if a programme has too many new and specialist funds within it, especially given that viability can be an issue if these funds are too small or the number of sector organisations within their remit are too few. The lesson learnt here is to continue to build on the specialist knowledge of sector specific organisations, but consider carefully how this is done; this could include involving them without them necessarily being the social investors themselves.

VCSEs' business models and applying to the Growth Fund

VCSEs accessing the Growth Fund are substantially smaller than VCSEs accessing wider social investment. Whether the Growth Fund has reached VCSEs that were not able to access investment in the past is less clear

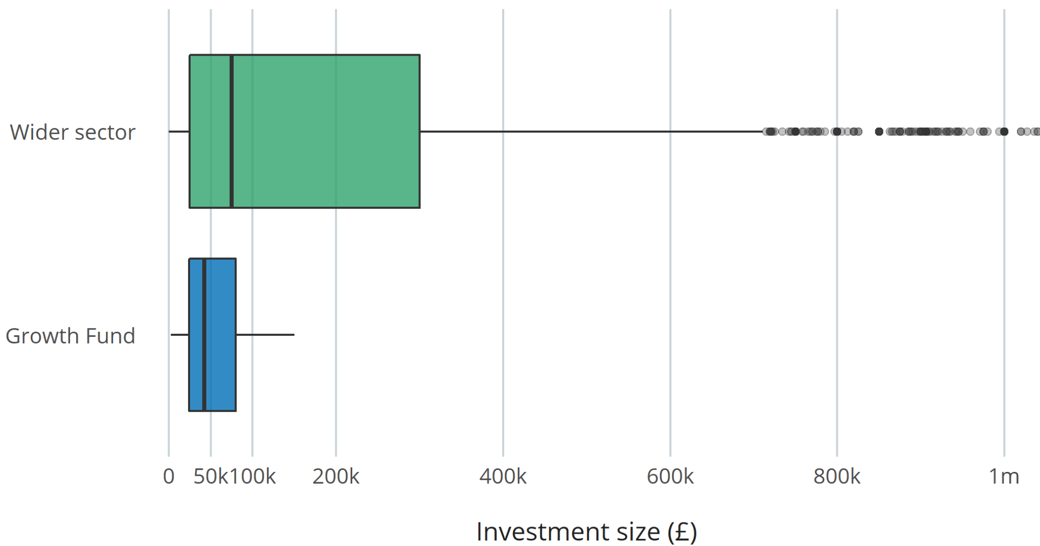
- Growth Fund VCSEs are targeting a wide range of different beneficiaries through their work, with nearly a fifth (18%) working primarily with vulnerable young people and 15% with people living in poverty and/or financial exclusion.
- VCSEs accessing the Growth Fund are substantially smaller than VCSEs accessing wider social investment; Growth Fund has supported organisations with, on average, half the income and 1/8th of the assets of those who normally attract social investment (Figure 5). The Growth Fund is also providing much smaller-sized loans than the wider sector – the median-sized loan in Growth Fund was £42,450, compared to £75,000 in the wider sector (Figure 6).

Figure 5: Comparison of median turnover between VCSEs accessing Growth Fund and the wider social investment market



Source: A tale of Growth Fund and the market. Curiosity Society

Figure 6: Comparison of investment size in Growth Fund and wider social investment sector



Y-axis truncated to £1,000,000 but maximum investment size for wider sector is £100,000,000

Data source: BSC deals data: https://public.tableau.com/profile/big.society.capital#!/vizhome/DLD2019/Who. Chart produced by Ecorys. Growth Fund deals = 505. Wider sector deals = 4,393. Wider sector deals cover 2002 to 2020; Growth Fund 2017 to 2020. We did not filter wider sector deals so they covered a similar time period because 25% of the deals did not include a date, and these were typically lower deal sizes. Therefore filtering by date would have excluded these deals, which would have skewed the results. Horizontal line shows range of deal sizes. Each box shows the 'middle 50' – i.e. the deals 25% either side of the median. Thick vertical line shows the median.

- Whether the Growth Fund has reached VCSEs that were not able to access investment in the past is less clear; some VCSEs have accessed small-scale loans in the past, but these may have been secured. Qualitative evidence suggests a nuanced picture, and there is evidence that some VCSEs would not have been able to access investment without the Growth Fund, whereas for others, they felt the Growth Fund provided another investment option for them. Some suggested that they would have gone to a commercial lender had they been unsuccessful with accessing social investment, although they could not be certain whether they would have been successful at securing a loan from another (social or commercial) investor.
- It is our understanding that VCSEs were not assessed on whether they could access other forms of investment, social or otherwise. It is our view that to maximize the value-for-money of blended finance programmes then the eligibility criteria should state that it is only available to VCSEs that cannot access other forms of (non-subsidised) investment, and this should be assessed at the application stage.
- Whilst the Growth Fund did plug a gap overall, there is evidence to suggest it did not plug the full gap, as the design of the Growth Fund meant it could mainly offer unsecured loans; other research has argued that there are other gaps in the supply of social investment, specifically around patient capital and quasi-equity products.[2]
- VCSEs took on Growth Fund loans and grants for a variety of reasons, related to their business model. Figure 7 presents a typology we developed based on the Growth Fund research to show how VCSEs appear to need or use different financing types at different stages of their business model development. Often loan finance was the preferred option because it could be used more flexibly than a grant.

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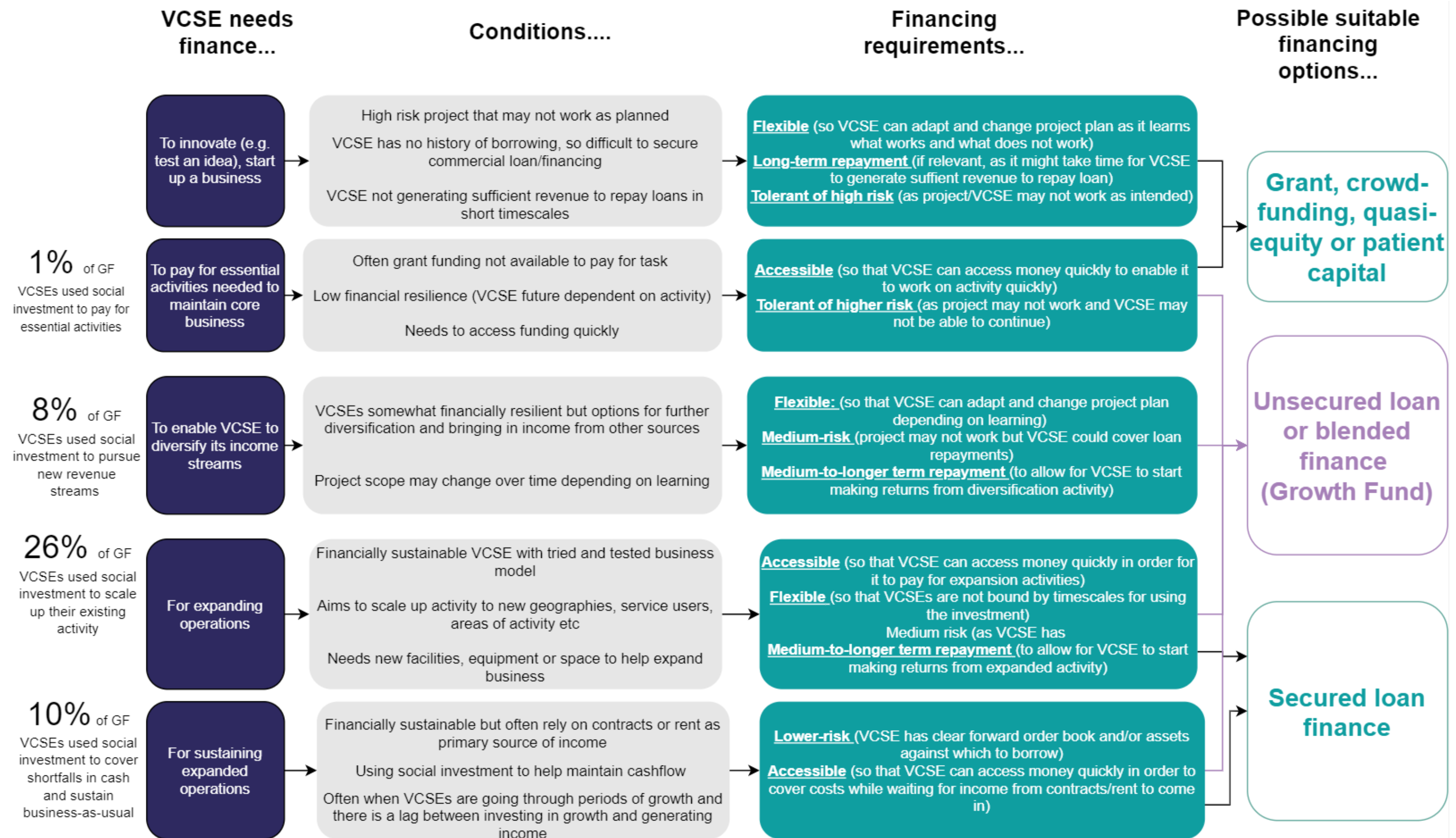
[2] Salaway, M 2017. Social Investment as a new charity finance tool: using both head and heart. See: *https://www.cass.city.ac.uk/__data/assets/pdf_file/0007/358864/CCE-Social-Investment-as-a-new-charity-finance-tool-using-both-head-and-heart-Report-May17.pdf*

Figure 7: VCSEs' use of financing types at different stages of business model development



Sources: Growth Fund Evaluation Case studies and Growth Fund Programme Monitoring Data. Building on wider research; Salway (2017): Social Investment as a new charity finance tool: using both head and heart; Flip Finance (2017) Risk Finance for social enterprises and charities. Percentages represent the percentage of VCSEs reporting this finance need in the baseline survey. Percentages do not total 1% as other uses of finance also reported.

VCSEs' experiences of the Growth Fund loans and grants

VCSE have had a positive experience, both during the application and re-payment stages.

- The loan application process for successful VCSEs was generally positive. VCSEs valued their investors' alignment with their mission, regular communications about progress of their application, and reaching agreed terms and conditions. VCSEs were less positive about the evidence required to demonstrate social impact, and the clarity of the application form and requirements.
- Qualitative evidence indicates that VCSEs generally used their loans as they intended to in their business plan. Where changes to repayment plans had been made, it was due to a change in VCSEs' business needs, changes in project timescales, and VCSEs generating less revenue than expected (both pre- and during Covid).
- Grant C – the grant that investors could pass down directly to VCSEs to use flexibly alongside their loans – tended to be used in several ways: to reduce the cost of loan repayments; to purchase new or upgrade existing buildings, facilities or equipment; to develop the organisation; and to cover core costs. The extent to which Grant C was reported by VCSEs as 'essential' varied. It seemed to be most important for those using it to lower the costs of their loans.
- Most VCSEs' experiences of repaying loans was also positive. VCSEs reported positive ongoing engagement with investors, and particularly valued the responsiveness of the investor, their understanding of VCSEs' business and clear, regular communications. However, several VCSEs felt the annual reporting requirements were at times complex and some found it difficult to evidence their social impact.
- The fact that Grant C was deemed most essential when used to pay the loan interest raises some interesting questions for the design of future blended finance programmes. Some VCSEs felt the interest rates were quite high, and wider research highlights high interest rates as a barrier for VCSEs accessing social investment[3]. It needs to be borne in mind that the purpose of the interest rates is to cover the investors' operating costs (and returns to the wholesale investor) – which are in-part covered by the Grants A and B respectively. A possible alternative design option, then, would be to use some of the Grant C money to increase Grant A. This would mean more of the investors' operating costs would be covered by the grant, meaning they would not have to charge so much interest. It is possible, though, that such a re-design, with less available Grant C, would be *less* attractive to VCSEs, as some reported being attracted to Growth Fund because of the grant element. This is something worth exploring in future blended finance programmes.

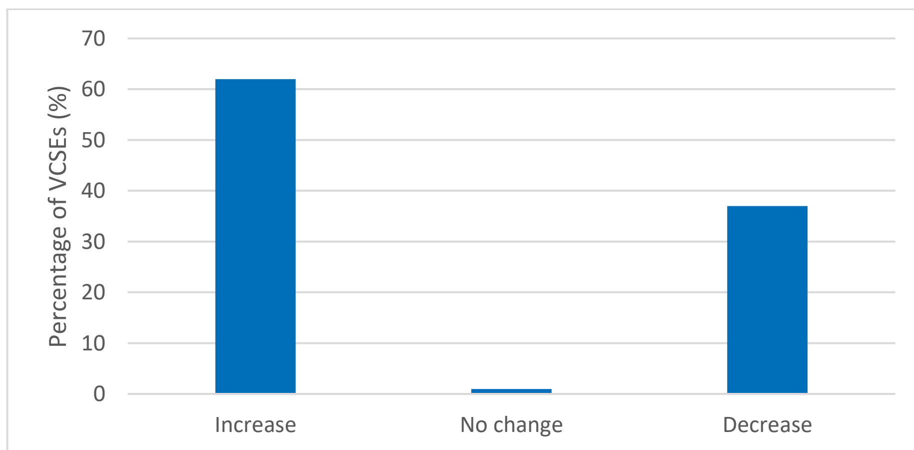
[3] Comic Relief, 2019. *What's in it for us? A Report on Small Charities and Social Investment.* See: https://www.goodfinance.org.uk/latest/post/report/comic-relief-whats-it-us-report-small-charities-and-social-investment

Impact of Growth Fund on VCSEs' financial resilience and social impact

Overall, VCSEs' financial resilience grew after taking on Growth Fund finance; the majority of VCSEs attributed this growth to the Fund. VCSEs also reported that it helped them increase their social impact

- VCSEs reported that 'financial resilience' could be measured in terms beyond the 'hard' financial metrics such as income or net assets. Other important indicators included: the extent to which VCSEs could demonstrate their repayment history; the extent their income streams were diversified; their stability (in terms of cashflow and number of full-time equivalents); and the extent to which they were self-sustaining (i.e. not reliant on grants).
- Evidence suggests that two thirds of 150 VCSEs increased their income (where data was available) after accessing Growth Fund social investment (Figure 8). However, over a third saw a decrease. It has not been possible to compare income changes between Growth Fund VCSEs and similar VCSEs in the wider sector due to limited available data on other VCSEs' income and net assets. However, most VCSEs in the survey and case studies attributed increases in income to the social investment.
- Diversifying income streams often contributed to increased revenue. Furthermore, VCSE managers often highlighted that the process of researching into and testing approaches to diversifying their income sources led them to have a better understanding of their organisation's business model and how they could continue to develop it in the future.

Figure 8: Change of direction in VCSEs' income from baseline to March 2020



Source: Growth Fund VCSE Management Information (n=150).

- There appeared to be no net positive impact on net assets, with 51% of VCSEs seeing an increase in net assets, with 47% seeing a decrease.
- Social investment had helped some VCSEs to maintain their cashflow to ensure they could keep covering their core costs while growing their business. 42% of 157 VCSEs for whom data was available grew their number of FTEs, though 27% saw a decrease.
- VCSEs saw an increase in 'intangible assets' (i.e. those not recorded on a balance sheet) acquired through the social investment, including improved staff working conditions, upskilled staff, a better or more well-known brand, and intellectual property. The unsecured nature of loans enabled VCSEs with no repayment history to build theirs up, thus increasing their ability to borrow again in the future.

- Over a third of survey respondents (31 out of 81) said that the social investment had reduced their reliance on grants to 'some degree'; four said that it reduced their reliance on grants to a 'significant' degree. There was both qualitative and quantitative evidence that suggests that social investment is contributing to increased beneficiary reach (in terms of geography, new beneficiaries and new types of beneficiaries), and increased quality of provision.
- Table 2 overleaf provides examples from the case studies of how the Growth Fund finance had boosted VCSEs' financial resilience.
- There were variations in how VCSEs were measuring outcomes. The level of variation in data availability, quality and types of outcomes reported makes it difficult to aggregate the data and report meaningfully on the overall social impact achieved by the Growth Fund. The Programme Partnership is still interested in VCSEs reporting on their core social impact, as it provides assurances that the Growth Fund is investing in socially-motivated organisations. However, we do not think the assurance value is proportionate to the effort required to collate the data, nor would it be legitimate to use such data to claim attribution of investee's core business impact to the investment, and so we would recommend to the Programme Partnership that it ceases collating it. This is not to say that they should stop seeking assurance of organisations' social motivations or trying to assess how the social investment is *contributing* towards social impact; instead we recommend that assurance is better gained through investor due diligence (pre and post deal) and, that gauging the programme's contribution to VCSEs' social impact is better captured through the evaluation surveys and case studies.

Conclusion

- Overall, the Growth Fund had made good progress up to the end of 2020. It had increased the number of social investors in this space, broadened the reach of social investment and increased social investor capabilities. It had plugged a gap in the supply of small-scale social investment for VCSEs. This in turn was strengthening VCSEs' financial resilience and increasing their ability to support a wider set of beneficiaries
- Some aspects of the Growth Fund programme have, inevitably, been more successful than others. Perhaps the most challenging aspect of the programme has been supporting new and sub-sector specialist social investors to operate financially viable investment funds. Many lessons have been learnt along the way, including:
    - It is important for organisations considering funding a blended finance programme to be explicit in their priorities for the programme
    - It is more challenging and resource-intensive to expand the social investment market than originally envisaged
    - It is challenging to aggregate social impact across diverse fund portfolios. Measuring the contribution of investments to social impact at a programme level is better captured through evaluation surveys and case studies than through attempting to aggregate VCSEs' reporting of diverse business-wide social impact numbers that are not solely attributable to the investment.
- There is, therefore, much to take from the Growth Fund into future blended finance programmes, but also areas to experiment with further, including:
    - The most effective and efficient way to use sector-specialist organisations to grow the reach of social investment
    - The best way to ensure programmes are targeted at those that need blended finance the most
    - The best way to blend the loans to VCSEs with grants
    - How to offer a broader set of products to meet VCSE needs, such as patient capital.

- In Figure 9 we reflect on the degree to which the original Theory of Change We have coded the ToC to highlight where there is evidence to support (or not) the elements of the ToC. We have coded the text as dark green where there is a good level of evidence from the evaluation that this element of the ToC is occurring. We have coded in light green where there is some evidence that this element of the ToC is occurring, but there is some nuance to this element – we have included the nuance in supporting text to the side of the diagram. We intended to include red text where elements of the ToC were not occurring – as can be seen, there were none of these. This coding shows that, overall, the Growth Fund Theory of Change is appearing to be correct, and the expected impact is occurring. There are some nuances in some elements that require highlighting, and designers of future similar programmes should bear this mind.

Table 2: Financial resilience of different case study VCSEs' business models by 'purpose of social investment'.

Purpose of social investment	Expected impact on financial resilience	Actual impact on financial resilience	Counterfactual (what would have happened without social investment)
Paying for essential activities	In this case financial resilience was low at the point of application and the organisation was operating at a budget deficit. The VCSE needed to undertake the specific project (a marketing campaign) to raise awareness of its business, to try and maintain its current beneficiaries as well as attract new ones	Very good – the social investment contributed to increased income and enabled the organisation to transition from operating at a budget deficit to a surplus. Due to this the VCSE expanded its team and is positive about future financial resilience.	This organisation would have likely struggled a lot without the funding – they needed it to keep their business afloat. The manager here also reflected that the social investment was 'key' to catalysing their ability to generate enough income for the project to be self-sustaining.
Diversify income stream	Social investment would enable VCSEs to increase the sources of income, thus reducing reliance on any one source of income (usually grant)	Mixed – one VCSE was, to a large extent, still reliant on its grant funders (especially for core operations), and the other said that it was in a positive place financially; the renovation of its café meant they could sell more goods, attract more people, and therefore brings in more income.	The organisations would have looked for funding elsewhere, however they also felt they would not have been able to secure a grant for the work that they did, so they would likely be less financially resilient.
Expand business	Many of these VCSEs felt that they were financially resilient prior to applying for social investment.	Mixed – one VCSE had said they had expanded their business, which led to increased income. Some	Generally, the VCSEs thought they would not have been able to grow at the same rate as they had done with the social

	These VCSEs thought that social investment would help increase their resilience as it would enable them to expand their reach geographically, or increase the number of beneficiaries reached, which would in theory increase their income.	VCSEs said they had increased income, as well as built up their assets to enable them to borrow against in the future. Others felt less sure, and while they had expanded their businesses, they were not meeting their expected numbers yet, which meant that income was lower than anticipated.	investment. For some, it would have slowed their growth, and for others the growth would not have happened (their organisation would have plateaued). For those that felt their financial resilience had increased, they were not sure if they would have been at the same level without the social investment.
Maintain cashflow	These VCSEs needed social investment to plug the gap between outgoings (e.g. overheads and salaries) and income (e.g. from contracts or rent). One was a fairly new VCSE with low reserves, whereas another had huge lags with cash coming in as part of contract work. These organisations felt that social investment would allow them to continue to develop their offers, while covering the core costs.	Good – organisations here were generally still financially resilient, with regular income and stability (i.e. maintained cashflow).	The Growth Fund came at the right time for these VCSEs. Two would have been in trouble financially. One said that their business would have failed because they would not have been able to keep themselves afloat until the future revenue came in. Another VCSE said that they would have failed on the delivery of a contract, because they needed the social investment upfront to bring in staff to deliver the contract.

Figure 9: Revisiting the Growth Fund Theory of Change