



Growing the social investment market:
Investment Readiness in the UK



Growing the social investment marketplace: Investment Readiness in the UK research summary

Stock code: BIG-socialinvTB
ISSN: 1744-4756 (print)
1733-4764 (online)
Print: Belmont Press
Written by: Tara Mackey, Policy and Learning, Big Lottery Fund

Further copies available from:

Phone: 0845 4 10 20 30
Textphone: 0845 039 02 04
Email: enquiries@biglotteryfund.org.uk

Accessibility

Please contact us to discuss any specific communication needs you may have.

Our equality principles

Promoting accessibility; valuing cultural diversity; promoting participation; promoting equality of opportunity; promoting inclusive communities; reducing disadvantage and exclusion. Please visit our website for more information.

We care about the environment

The Big Lottery Fund is working towards sustainable development and the use of sustainable resources.

Our mission

We are committed to bringing real improvements to communities and the lives of people most in need.

Our values

We have identified three values that underpin our work: making best use of Lottery money, using knowledge and evidence and being supportive and helpful.

You can find out more about us, our values and the funding programmes we run by visiting our website www.biglotteryfund.org.uk

The Big Lottery Fund is committed to valuing diversity and promoting equality of opportunity, both as a grantmaker and employer. The Big Lottery Fund will aim to adopt an inclusive approach to ensure grant applicants and recipients, stakeholders, job applicants and employees are treated fairly.

© Big Lottery Fund, September 2012

Introduction

Social investment is an area of increasing importance for Government, funders and the voluntary, community and social enterprise sector (VCSE). The Big Lottery Fund is interested in this market as part of our commitment to being an intelligent funder and our wider role in building a stronger sector. Social investment can offer new financing tools and access to new sources of capital to enable VCSE organisations to operate on a more sustainable footing. Lack of investment readiness is often referred to as a barrier to growing the social investment market but there has been little work specifically addressing the issue of investment readiness across the UK.

The Big Lottery Fund commissioned ClearlySo in partnership with NPC to study what investment readiness support is needed and what it should look like in the four countries of the UK. The research considered what investors and others look for in an attractive investment, and what BIG and others can do to give groups (or investees) the best possible chance to reach this position. This is BIG's summary of the findings from the main report, which is available on our website at:

www.biglotteryfund.org.uk

Investment readiness: a definition

In this study 'investment readiness' refers to the conditions required for an investor to consider a group suitable for investment. What it means to be investment ready will vary from one group to another and their readiness or lack of readiness is often determined by the perceptions of the investor.

How the study worked

As part of the research, 7,420 VCSE organisations from the Big Lottery Fund's grantee database and ClearlySo's membership database were surveyed; 1,255 organisations completed the survey. The researchers also carried out a literature review and over 40 interviews with investors, intermediaries and support providers across the four countries of the UK. Five case studies were conducted to provide further practical insights into the steps taken by organisations to secure investment. These can be found on our website: www.biglotteryfund.org.uk

Differing perspectives

Investors' perspectives

Investors are diverse, and include mainstream commercially-focused investors, individuals, the public sector, philanthropic institutions and foundations.

Investors reported significant challenges with investment readiness, particularly noting the lack of suitable financial skills among potential investees as a critical barrier. Investors also identified wider problems in the market such as a general lack of understanding of the concept and the appropriateness of social investment; the absence of filtering systems¹ which meant that organisations often approached investors too early; poor coordination and lack of signposting to appropriate support sources; and the relatively complex deals available for relatively small sums of finance sought.

“Potential investees need clear signposting about type, stage, sector and suitability for investment”

Suzanne Biegel, Catalyst at Large

The research highlights that investors would also benefit from support throughout the process of brokering a deal with VCSE investees. The problems faced by investors include pricing an investment, costing in the risk and deciding on the detailed agreements. The shortage of templates and examples for investors to draw on, combined with the current lack of due diligence across the sectors, adds to these problems.

Intermediaries' perspectives

A range of intermediaries were interviewed as part of the research. Intermediaries are specialist organisations with a commitment to social goals. Their role is to match finance, skills, technologies and networks. Those interviewed included support providers, grant-makers and public bodies.

“There are different needs for small organisations, ambitious ‘scalable’ organisations and asset backed community businesses”

Hugh Rolo, Locality

Concerns from intermediaries chimed closely with those cited by investors, including a lack of coordinated support and a need for peer support, coaching or mentoring. In contrast to the focus from investors on a lack of understanding of the financial model, intermediaries spoke of the challenge of changing mindsets from the traditional charitable model to a business model. Intermediaries suggested that improved generic information (for example, on products and sources of finance) and early stage diagnostic tools should be offered before expensive bespoke support.

Investees' perspectives

The research indicates potential demand for investment readiness support from the VCSE sector to be about 70,000² or more organisations in the next five years. Their plans and the type of finance they seek will inform the preparation of appropriate investment readiness support. In total 1,255 organisations responded to the survey, generating one of the largest sources of UK data on potential demand for social investment.

The next section of this summary sets out perspectives and priorities of VCSE groups.

¹ Filtering systems include any process that helps an organisation to understand and assess their own levels of investment readiness.

² This is an extrapolated figure from our survey, see main report at our website www.biglotteryfund.org.uk

What VCSE groups said

VCSE survey: pursuing social investment finance

The survey filtered respondents into five exclusive groups – those who:

- had secured repayable finance³
- had sought but had been unsuccessful in securing repayable finance
- are currently seeking repayable finance
- are not currently looking for repayable finance but are interested to see if it is suitable
- are not looking for and not interested in repayable finance.

Figure 1: Pursuit of social investment by VCSE organisations

A Successfully secured repayable finance	21% 259
B1 Tried but not yet successful in securing repayable finance	7% 86
B2 Actively seeking repayable finance	8% 95
B3 Not currently looking for repayable finance but interested to see if it is suitable	22% 272
B4 Not looking for and not interested in repayable finance	43% 543

Total number of VCSE respondents to survey: 1255

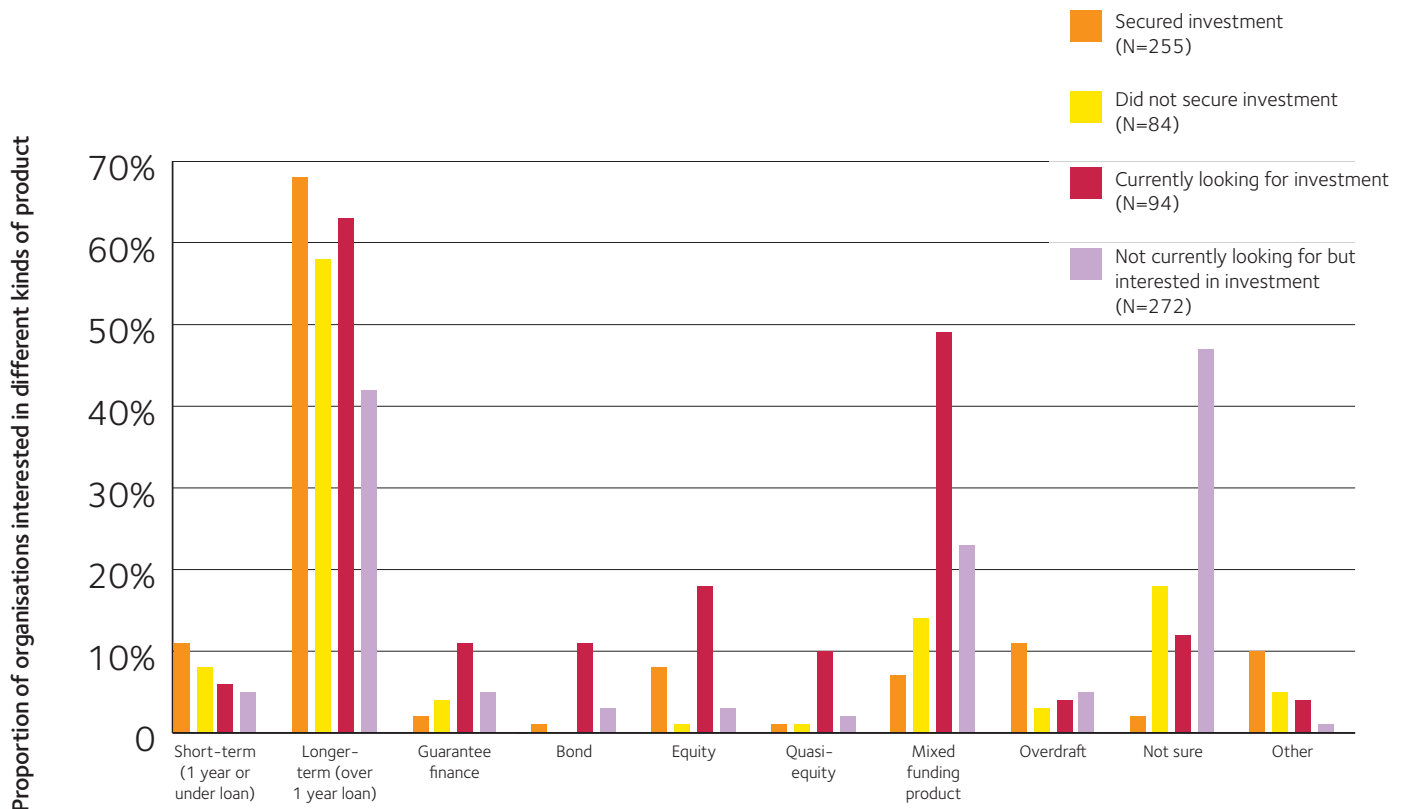
***Total does not add up to 100% due to rounding**

³ Repayable finance was defined as “any form of financial support, including equity, provided with the expectation that some or all of it is repaid—with or without interest, dividends or revenue participation”.

What VCSE groups said

Demand for different types of finance varied across different groups. There appears to be a mismatch between the types of finance that organisations have actually received and what organisations who are looking hope to secure. For example, only 7 per cent of respondents have secured a mixed funding product – defined in the survey as a combination of different types of finance such as loans and grants – but 49 per cent of those currently looking are interested in securing this type of finance. The same disparity is true for equity⁴ and quasi-equity⁵ with much higher proportions interested in securing these types of finance than have actually received them. Figure 2 sets out these differences.

Figure 2: The type of finance that organisations are interested in securing



⁴Equity investments are for a stake in an organisation, usually in the form of shares.

⁵Quasi-equity investments are a mixture of loans and equity investments. There are no shares involved. Instead a fixed percentage revenue return is usually agreed.

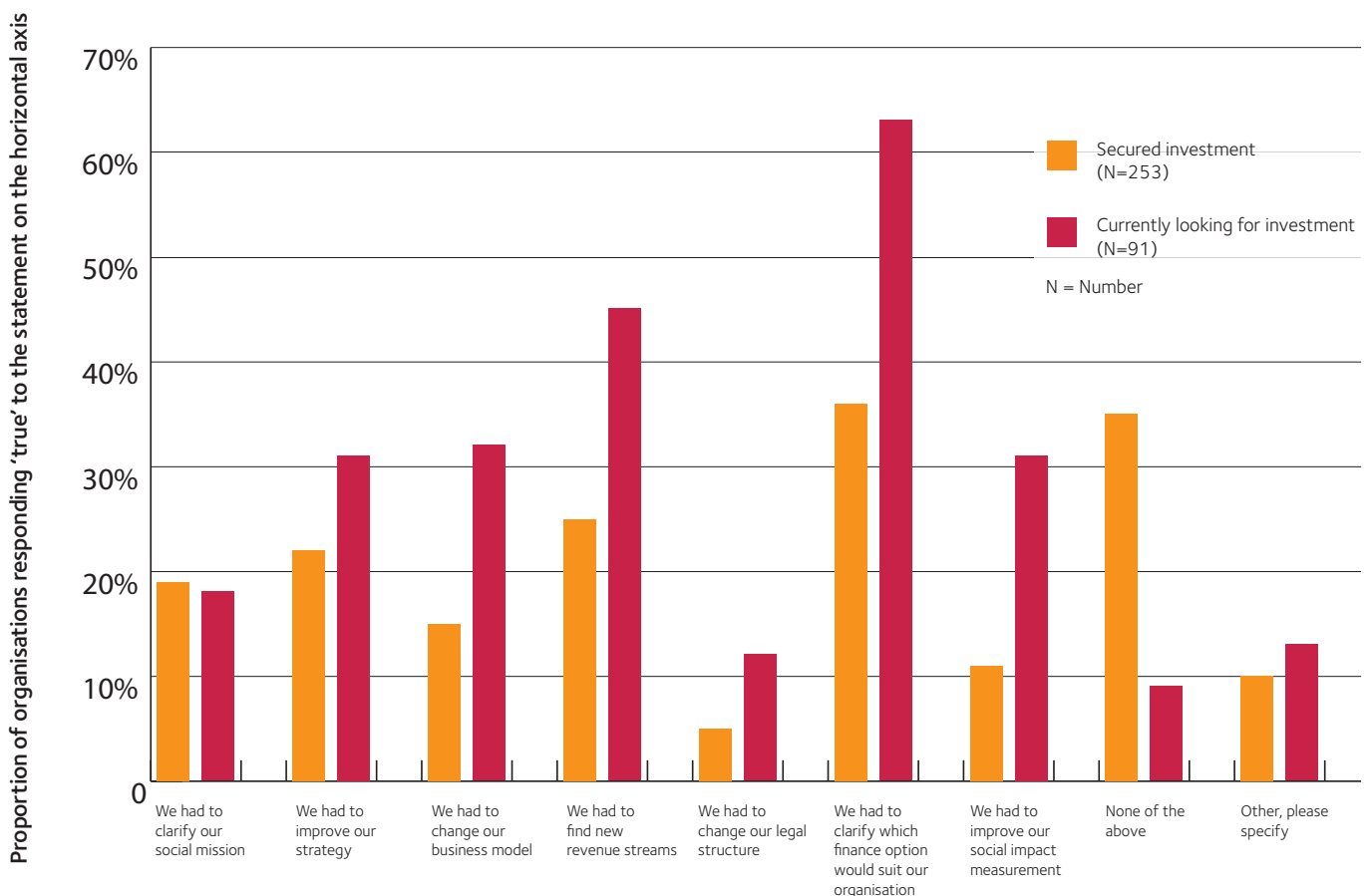
What VCSE groups said

Survey respondents are most interested in investment between £10,000 and £100,000. Those who are currently seeking investment were more inclined to seek larger amounts than those who had already secured investment or had failed to secure investment in the past.

Just under half of those surveyed are not interested in investment. Three-quarters feel that charitable money should be spent on delivery, not on repaying loans. However, 70 per cent of this group are interested in new ways of doing things and new ways of financing them but 63 per cent agree that they are not able to generate the surpluses required to take on repayable finance.

Organisations seeking finance are making significant changes in order to become investment ready. Clarifying which financial options would suit their organisation was a key step both for those who had already secured investment and those still seeking investment. Improving social impact measurement and changing business models was cited as something they would do more frequently by those currently seeking investment than those who had already secured investment.

Figure 3: Steps taken by organisations to become investment ready



Why are some organisations failing to secure investment?

Of those 86 survey respondents who were unsuccessful in securing investment, 32 per cent were not successful because their organisation decided to withdraw from the process, rather than for other reasons; 44 per cent abandoned the process before approaching investors. This suggests that even though the investor perception is that too many organisations are approaching investors before they are ready, some organisations are self-filtering out of pursuing repayable finance.

Almost half (47 per cent) of those that did not secure investment believed that they did not lack any of the financial, marketing, business or finance skills presented to them in the survey. For the 53% that did recognise they were lacking in some of the skills listed, marketing skills were identified as their top skill type for improvement.

What external support are investees using and finding useful?

Of the external support that they received, organisations that secured investment found bespoke business and financial planning the most useful, whereas 'investment readiness support courses' and 'online mentoring' were perceived to be the least useful.

Those that did not secure finance still found bespoke business planning useful and those currently seeking investment suggested that a step-by-step guide to getting into social finance was the most useful. In terms of the external support that they would like to receive, all those open to seeking investment agreed that a step-by-step guide to getting into social finance would be the most useful.

Mismatches between investor and investee perspectives

There are mismatches between investor and investee perceptions about investment readiness. These mismatches can be categorised as follows:

1. Mismatches in the perception of skills and attributes required for investment readiness
2. Mismatches between the availability of support and what is required by groups
3. Mismatches between access to support with organisations' ability to draw on it
4. Mismatches between investor and intermediaries' perception of levels of financial acumen, and investees' own perceptions of their financial skills
5. Mismatch in the importance placed on a viable revenue model. Investors and intermediaries felt this was key. The support required by investees to develop a strong revenue model is bespoke and costly and therefore difficult to find.
6. Mismatch between the type of capital demanded (high risk) and the available supply (asset-backed capital).

Conclusions

The study identified some mismatches between the views of various stakeholders, as summed up in the box on the previous page. Any attempt to overcome the problem of investment readiness will need to take account of these. The study highlights the need to develop sector based expertise and measurement alongside new approaches to investment support across the UK.

Development of sector based expertise and measurement

Investors have different perspectives on the importance of social impact: for the mainstream bank lenders, there are few if any demands as to how impact is generated or measured. For social investors, the creation of social benefit as a primary purpose of the organisation is a 'filter' through which potential investees must pass. Beyond that, the creation or measurement of social impact is rarely a deal-breaker. Evidence of the measurement of social impact was not seen by investees as a major barrier to securing finance. In the specific case of public sector commissioning under payment by results (PbR) contracts, social impact measurement is a critical issue. VCSEs need to be able to show that they can create, replicate and price the real cost of their outcomes correctly in order to secure and deliver a public sector contract.

There is a need for specific sector-based expertise, which is currently in very short supply. In Scotland, a few mainstream private sector intermediaries are helping to fill the expertise gap as the country enters the PbR marketplace. Northern Ireland and Wales are not fully involved in this agenda as yet, but England has a chance to pilot approaches to outcomes measurement that may be replicable by others in the future.

Different approaches to investment support across the UK

In general, the picture of previous and current support varied across the four countries of the UK and was influenced by how support was financed, and whether it was closely connected to local need and to the supply of capital available. **Northern Ireland** has managed to deliver a more coordinated structure to investment readiness provision than other countries, making good use of its smaller but tighter networks across the sector. In **England**, the abolition of regional governments may influence the use of networks to support social investment. **Wales** faces issues raising investment awareness within its strong community-based organisations. **Scotland** could benefit from undertaking a mapping exercise, by sub-sector or locality to examine the full extent of the provision and gaps of support as well as the market opportunities open to VCSEs, as a basis for designing suitable investment readiness provision. There could be scope for different countries of the UK to take the lead in developing investment support according to areas of specific interest and according to the supply of the type of investment that actually exists.

Design and develop investment readiness support

Investment readiness programme design should be flexible enough to fill the gaps and mismatches described above. It should consider where it can provide generic support, particularly for the earlier stages of investment preparedness as opposed to where specific provision is necessary. Categorising investment support into generic and bespoke provision can help make support as cost-effective as possible.

Conclusions

Support could be structured across any one or more of three different approaches:

1) Sub-sector specific approach

Meeting the specific needs which organisations operating in any given sub-sector (for example, care for the elderly, education and training) have to secure investment.

2) Skills gap approach

Identifying the skills that are required by the VCSE sector, and providing these skills across the board to all – but in different stages of intensity or at different levels. For example financial skills, marketing skills and business strategy skills.

3) Stages of an organisation's development approach

Examining the investment readiness needs of an organisation at different stages in its business cycle. For example, organisations at start-up and early stage may need support around market analysis. Different intensity of provision may be required according to the stage of an organisation's development.

The development of the Office for Civil Society's Investment and Contract Readiness Fund, which will use government grants to support larger, more ambitious organisations in England, will prove a useful source of learning. Investment readiness tools need to provide filtering and signposting, and identify ways to distinguish between the specific needs of early stage organisations which are small but ambitious for growth and those which are small but will remain locally based.

The research indicates that external support often leads to a greater chance of securing investment. This reinforces the need to provide well-designed support to those for whom social investment could be beneficial.

Next steps

The research recognises that social investment is not suitable for all VCSEs, and should not be seen as a cure for all the current difficulties faced in financing VCSEs. However, where social investment offers the potential for organisations to create new, extended or different ways of delivering their goods and services, then there is an important role for funders and intermediaries to play to help them secure this. Much can be done to improve and tailor the support offered to organisations to give them the skill sets they need to secure repayable finance.

In line with policy directions from the Cabinet Office covering UK-wide spending, the Big Lottery Fund will continue to ensure "the distribution of funds strengthens and increases the capacity of the social investment market for supporting public benefit and social action".

This study is helping to inform BIG's future social investment interventions as our country and UK funding portfolios continue to consider their longer term plans. It has already informed the development of a new England fund relating to early stage investment readiness support for VCSE organisations. Recommendations made in the report are currently being considered for action.

The full research report can be found on our website: www.biglotteryfund.org.uk

