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Social enterprise

Creating a hub for innovation in society

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Growing pains

As Britain begins to recover from the financial crisis, charities and social enterprises are seeking ever-more innovative ways to fund projects and services which are of benefit to society. You only need look to the launch of Big Society Capital and social impact bonds – which are helping to reduce reoffending rates, improve our health and protect vulnerable children – to see just how much benefit this type of funding has to offer.

Recent government estimates suggest there are 70,000 social enterprises in the UK, employing a million people. The sector's contribution to the economy has been valued at over £24bn. Yet social enterprises claim access to finance is one of the biggest barriers to growth that they have.

This supplement explores the obstacles facing the entrepreneurs, investors and financiers and looks at the type of infrastructure needed to facilitate investment.

Our round-table discussion looks at the role of government in mitigating risks for investors and financiers – attracting more of them to the market – and how they can be encouraged to be more innovative with financial products. ●

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ARTICLES

First published as a supplement to the New Statesman 6-12 December 2013.

The paper in this magazine originates from timber that is sourced from sustainable forests, responsibly managed to strict environmental, social and economic standards. The manufacturing mills have both FSC and PEFC certification and also ISO9001 and ISO14001 accreditation.

COVER DESIGN BY LEON PARKS

Why the social enterprise movement must sharpen its teeth

by Sean Worth

The sector needs to start agitating for a change in attitude and a much more radical opening up of government provision

Social enterprise was once touted as the next big thing in public service reform: an ethos-driven alternative to hiring private outsourcing firms that could transform outdated state provision. While social enterprise has expanded modestly in the public realm, it has seen only a fraction of the near 50 per cent growth in public outsourcing contracts since 2010. So what's holding the sector back? And how can social enterprise become a major force for service delivery, as its advocates argue it can.

Because social enterprises compete like businesses, but aren't usually driven by the need to maximise shareholder value, the movement's leaders have sold social enterprise as something of a cuddly alternative to for-profit provision. They have even been openly critical of private firms delivering public services. In doing so, they have only fed the view that non-state provision is somehow politically controversial. This feeds the go-slow attitude in government to service reform and bolsters the vested interests who oppose all outsiders, including social enterprises, delivering state services.

This is exactly why social enterprise remains so niche and poorly understood and it's here that the biggest change in attitude has to take place. Frankly, the sector needs to start agitating for a much more radical opening up of government provision.

The bulk of public attitude research, including my own published earlier this year, shows it's what people want. The evidence is that they favour an open field of non-state providers being allowed to deliver services, and this view is especially strong among the poorest service users. People don't want a free-for-all; they want competition to be sternly regulated in the interests of service users, but some polling even shows a majority of current public sector staff want to see poor services taken over by outside providers, including businesses.

> What matters most are the results, not what sector they are from

What matters most to people are the results, not what sector they are from. However, there is evidence that social enterprises are favoured over other suppliers in some areas, especially "front-line" provision such as education. This should be the biggest target for the social enterprise sector. If more people want social enterprises running their services, then the movement should stop feeding the idea that opening them up is controversial and start agitating for more competition – as the evidence is that they're well placed to succeed in it.

There will be technical issues to deal with to tackle the problems which place social enterprises at a disadvantage in public sector markets. These are well known and range from higher VAT and pensions costs to a bias in outsourcing contracts to large firms with big balance sheets who are deemed safer to deal with.

Ultimately, if ministers want a mixed economy where social enterprises and charities, as well as small business providers, can deliver services, they must intervene more strongly to make it happen. A mixed economy of provision will take years to evolve, despite the new Social Value Act, which will allow commissioners to take the social profile of a bidder into account when deciding a contract winner. If it is ministerial policy to see the contribution of social enterprises and others grow, they need to more actively consider forcing it, as they did with stipulating that a quota of contracts should go to small businesses. This should be for a transition period only until the genuinely mixed market they want emerges.

This need not penalise other sectors as all should grow. Our public sector, as currently configured, simply cannot last. On one hand, we have all the main political parties agreed on curtailing public spending after the 2015 election, while on the other, we are seeing unprecedented demands forecast on public services as our population grows and ages. This will force services to get worse unless they are reformed, and opening them to delivery by the best possible providers is the least that should be done.

The debate over this remains stuck in the 1970s, with attempts to bring new providers into areas like the NHS and education seen as tantamount to reckless "privatisation". The rational antidote to this view can, fortunately, be found in what ordinary people tell us they want from their services – if only our politicians would listen.

The stars are aligning for the social enterprise sector to really take off. People clearly want more choice and control over the public services they use, and social enterprise has a potentially winning role to play in that. To get to that point, however, the sector needs to start clamouring much more aggressively for the change people want.

Sean Worth is a former Downing Street special adviser on public services reform and is a visiting fellow of the think tank, Policy Exchange supported by RBS

Why social enterprises find mainstream finance elusive

by David Treacher

The latest estimate by BIS puts the number of social enterprises in the UK at 70,000, employing about one million people. According to *The People's Business* report from Social Enterprise UK, 48 per cent of social enterprises sought to raise some form of external finance in the past 12 months, twice the proportion of SMEs. However, 39 per cent of social enterprises cited access to appropriate finance as the single largest barrier to their growth and sustainability.

At the same time, we are seeing an explosion in social investment. Boston Consulting Group's report *The First Billion* found a base of just £165m of social investment deals in 2011, but asserted that demand could reach £750m in 2015, and around £1bn the following year.

So why do so many social enterprises find it hard to access finance, particularly mainstream finance?

New tools for assessment

Put simply, mainstream finance (big banks) is not set up to assess social enterprise effectively. And social enterprises are not set up in a way that effectively engages mainstream finance.

From a bank's perspective, we have £32bn of debt in our SME loan book. Our systems and processes are set up for mass-market, well-established, clearly understood business models. Despite rapid growth in social enterprise, this sector remains niche, specialised and different. Current processes and policies to assess credit-worthiness are not always the right tools because returns generated by social enterprises are not just monetary; they are also social. Mainstream finance evaluates risks and opportunities based on financial returns, sustainability of the organisation and ability to repay.

Social returns – the raison d'etre of social enterprise – cannot be used to inform the decision. Social enterprises heavily reinvest their cash or reduce price to achieve social returns, and it can be hard to assess the flexibility of this reinvestment. Since they must still pass the same financial hurdles as any other company to access mainstream finance, it is no surprise that many struggle, particularly those below £1m turnover, which accounts for 82 per cent of UK social enterprises. Social lenders, such as community development finance institutions (CDFIs) and charities such as the RBS MicroFinance Fund, go some way to counteract this – being smaller and more agile in their decision-making. Funds available through these channels can be competitively priced as they are often supported by government funding and/or grants.

> Helping social enterprises become investment ready is as much of a feature . . . as the finance itself

Helping social enterprises become "investment-ready" is as much of a feature of the access-to-finance debate as the finance itself. *The People's Business* found 73 per cent of social enterprises rated their internal capability as high, but only 32 per cent rated business capability highly in accessing external finance, suggesting a disconnect between running the business *vs* reaching out for external funding.

Lack of information

In the absence of adequate assessment tools, an alternative would be to use credible, robust information to facilitate performance benchmarking, helping financiers assess risk and return. But there is a lack of consistent and coherent information from social enterprises to help investors make these comparisons. While initiatives such as the RBS Social Enterprise 100 (SE100) index, or the recently launched Social Enterprise Stock Exchange, go some way, it will take time (and a significant increase in scale) before these initiatives can be genuinely useful investor tools.

When it comes to the flow of money into social investment, there is not enough data on risk and return at a portfolio level. This is made worse by a highly fragmented and immature market, with products, providers and investors all relatively new to the principles of social investment. Again, initiatives are emerging – for example, the EngagedX index, the world's first financial index and data platform for social impact investing, which is being developed with support from RBS and others. But there is still a long way to go.

Any business needs access to the right skills, expertise and markets/customers in order to ensure growth and sustainability. Public, private and third-sectors are working to help expedite growth and sustainability of social enterprise. Every gap and mismatch has an initiative or project seeking to address it. There are many reasons to be hopeful.

David Treacher is managing director, Public Sector & Charities, Corporate Banking, RBS

Going for growth: how can we increase investment?

Access to finance is one of the biggest barriers to growth for social enterprises, but getting advice and hearing of others' experience can be just as vital in developing long-term capacity

Jon Bernstein Ladies and gentlemen, thank you for being here. Let's go to Nick Hurd first.

Nick Hurd There is growing recognition that this sector is an economic force, employing a lot of people, many of them in difficult places, many who might otherwise be challenged in the job market. It's also a space where we're recognised as being a world leader and it's hugely relevant to the big challenges from the government perspective. How do you meet public demand for better services when you've got a lot less cash? We want to help social enterprises grow their top line by creating opportunities for revenue, but we're also very keen to open up new opportunities at the local level, to take over assets and services. It's complicated and requires a culture change.

A large part of what we're doing is trying to create conditions for investment to come in and help. Mainstream capital markets don't work for this, hence the creation of Big Society Capital, with much more money than the market could absorb. In March 2014, we're following that up with a tax break for social investment because we want to sweeten the blend between financial return and social return. We're busy trying to address the fundamental challenge which is the flow of credible things to invest in. There are two streams at work.

One is grants that are designed to nurture a pipeline of investment-ready opportunities from start-up through to where they can take on £500k of investment, nurture entrepreneurial talent and help it on to the next stage. Then we have "social impact bonds", which are a series of contracts that are valuable in creating space for genuine social innovation and bringing in risk capital to finance new interventions in often complex areas, so risk is shared or transferred between commissioners and investors. We have 13 or 14 of these bonds, with 13 or 14 in the pipeline. If we can start building an evidence base around new interventions and old complex spaces, we can open up more opportunities.

The last time I looked, there were 12 different sectors of social policy involved in the social impact bonds, including childcare, drugs and alcohol, homelessness and adoption. We want to create a hub of expertise and knowledge-sharing.

Peter Ibbetson We are the leading high street bank in this sector. In terms of why you do it, there'll be a shareholder drive that says there are commercial reasons; or you do it for corporate social responsibility (CSR) reasons. The reality is you probably do it for both. There are 70,000 social enterprises in the UK, employing about one million people; logically, a quarter of those will bank with our group. The only people we're going to be able to rely on to say "this bank is doing the right thing now" are the customers. So that's a good commercial reason.

You do it through funding, to the extent you can. RBS has its microfinance fund; that's moderately small lent to social enterprises. You do it in commitment from the staff – our staff are engaged in social enterprise support, advice, volunteering. You do it in advice and support to bodies who are engaged in it, so strong support to the Community Development Finance Association (CDFA) and Social Enterprise UK (SEUK) for example – RBS is a founding member of both.

So why isn't it a lot easier? I was at a dinner last night, with a guy who's in private equity. I said to him: "If a bank lends 100 loans, how many do you think could go wrong before the bank's in trouble?" The view out in the high street is 15-20, and this guy said 15. The answer is: just over one. High street banks are just that – high volume, high street lenders – and so they need a lot of data to show the money will come back. Because, if it doesn't come back, the bank will go out of business.

At the moment, it is hard to assess social enterprises – especially smaller ones – in the mainstream model. A social enterprise venture is left with three challenges: where does finance come from? How do I find out where it is? I think that's one of the biggest challenges we have. Third, having found out where it is, where is the mentoring and advisory support to help me be successful?

Jon Bernstein Peter Holbrook, help me out with a workable definition of what a social enterprise is, please.

Peter Holbrook It's a business where the primary social purpose is articulated in its governing rules, and mostly it's controlled in the interests of the people or the community it's there to support.

Jon Bernstein There was a report commissioned by the Cabinet Office this year where 24 per cent of small and medium-sized enterprises (SMEs) self-identified as social enterprises. But, actually, only 6 per cent had a good match.

Peter Holbrook I think it depends on how the question is framed. If you ask: "Do you have a social role?", of course smaller businesses operating in communities have a social role in providing local services, employing local people, spending money in the local economy. So it's how the questions are framed. But this discussion will be coming to a conclusion, particularly from a European Commission perspective, and as public awareness grows.

Jonathan Jenkins We're exhausted by the definition debate. As social investors, if we invest in a private company, we have to be careful where the benefit is going. Some of the most exciting things I've seen are in structures I can't touch with social investment that has government or charitable money in it. I think that REDS10 was on the edge of what was "social" or not.

Paul Ruddick We were advised to stay as a limited company that makes a profit with a social purpose. People need to go into this market to make money otherwise you won't get investment.

We set up REDS10 out of frustration regarding young Londoners. They were unemployed long term, with no training. We employ the young people and subcontract to all the subcontractors for a period of time. They get two or three years of their apprenticeship, a trade, a qualification; they can go on to employment. We operate similarly to a recruitment company so we had to set up like that. We spend a lot of our money on training young people or getting them to go to work – we have a huge pastoral support team.

PHOTOGRAPHER SOPHIA SCHORR-KON

"We want to create a hub of expertise and knowledge-sharing"
Nick Hurd

We put in our own money. In the first year, no one wanted to look at us, so we raised some venture capital. In the next round of funding we won the Big Venture Challenge, which gave us £150k, and that attracted another investor. We're at a third stage of investment raising at the moment, talking to a couple of people around the table about where we go next. We're profit-making now, we've been around for three years, we've got a big contract with contractors, but it's still not very clear cut which route to go down.

I do have an issue with Big Society Capital lending money to intermediaries – the intermediaries then loan it to us at a much higher rate. And they might want a chunk of equity as well. You think, "well, that may not be the best for us."

Matt Robinson Social enterprises and charities should get the best financing deal they can get, and if that's not from social investors, then the social investment market is needed. Cost in the market is an issue partly because it's still so small. The predominant channel linking social enterprises with investors and wholesale money like ours is through fund structures – they're expensive, particularly when they are very small.

We also need to look at other channels, which could include getting mainstream banks in, maybe with a partnership, or use other ways to help mitigate risk. Also there's newer channels like crowd funding, and some of the things that Funding Circle have done with the business finance partnership.

Kate Markey One of the things that I'm hearing here is around transparency. We need to look at the level of deals that are actually happening versus the pipeline that is being seen by intermediaries, and what is actually being turned away and why. It's critical for potential investees to understand that. As a very nascent sector, social investment finance intermediaries (SIFIs) need to be able to communicate that.

Jon Bernstein So the wholesalers like Big Society Capital provide the capital, and then you deal directly with the central organisations.

Kate Markey Absolutely. The sector's structure needs to change.

Caspar Mackay One of the things that's come up is the appropriateness of the funding. And the types of capital that social investors typically have. We have to conserve our capital to repay our investors. We take more risk than mainstream banks because we're much closer to the sector, but if one needs to take on more risk, we need the type of ▸

funding that would allow us to do that and that means we need a tranche of grant funding that will sit alongside, to effectively take that first loss. We recently launched a corporate social venture (CSV) fund, for very early-stage businesses, and it's 50 per cent grant-funded; there will be losses and I suspect they will be quite significant. If we're taking debt-financing from an organisation such as RBS, we cannot afford to take those types of risks.

It's also about the deal size. A deal from me to do a half a million pounds for ten years costs the same as me doing one for £50k. You may ask for a six-month funding; I prefer to do it for ten years, and I can do it at a cheaper rate, because I know that I'm going to get the money back over that period of time and can spread it out. If people want us to do smaller deals, we need some revenue support.

Jon Bernstein Rupert, your organisation looks at and indexes the risk and the rewards of social enterprises.

Rupert Evenett Our working hypothesis is what I call "nailing the myth of risk" in the sector. If you compare social enterprises with commercial SMEs, startup for startup it doesn't feel like the financial risks or the operating risks are necessarily higher. You've got very good entrepreneurs in social enterprises, who are very good at dealing with risk, precisely because they're good at dealing with the often quite flaky operational risks and the types of situations a lot of social enterprises are in. Like-for-like in the financial sector, it doesn't feel like the risk is any greater.

I'm a great believer that data unlocks capital, and what we really need is more data that says: "This is a market that is reasonably investable, it's got reasonable returns, even before you get to the social returns, and when you add in social returns it's a premium return market for not-bad risk." Now, that sounds quite attractive.

Sophi Tranchell Divine Chocolate was incorporated in 1998, and we were set up by Twin Trading, which also previously set up Cafédirect. We had investment from The Body Shop, and from Christian Aid, and then from the Department for International Development (DfID). Because we had a loan guarantee that was from the Crown we could go through a conventional bank (RBS) and that meant that we could have a very conventional relationship with a commercial bank that offered us competitive rates on commercial tools; we've had invoice discounting, which grows with us as a retail business. That's been enormously helpful because I haven't had to spend my time raising money – I've had access to something that's growing with us. We've also had access to forward currency buying at a commercial rate. We paid back the loan, we paid back the interest, we pay VAT on every product we sell, we pay corporation tax.

The idea that Divine Chocolate was going to launch in one of the most competitive markets and mature markets in the world and survive as a farmer-owned chocolate company was deeply implausible. Everybody who invested in the company wrote it off. Because of those people taking that bet, we're here today.

Peter Holbrook I'm really keen that someone looks at the loan books over the past ten or 15 years, to see whether the nature of social enterprises "de-risks" them. When you seek finance in traditional routes, you're just placed on the same algorithm as a traditional business. Anecdotally, we believe social enterprises and charities pose a lower risk. But we need evidence, and we're probably at a point where we can do some reviews of the loan books from a whole variety of funding mechanisms.

Peter Ibbetson You just said something fundamental Peter: social enterprises don't have the same balance sheets as high street businesses. Generally in the marketplace, if you borrow for your company, you give a director's guarantee; it keeps you very focused on your financial obligations. My experience in the Social Enterprise Loan Fund was that we never went for directors' guarantees. Parallel to that, your repayment rate in social enterprises is higher than you get in mainstream. If somebody could come out and convince us that the risk is better in social enterprise than the mainstream, that'd be really interesting.

So, where do you get the financial support for social enterprises? For me, it breaks down into three or four areas. Charitable stuff, so those that do the £15 a month thing; and those that, as in Sophi's case, took a great leap of faith and wrote off the money because they believed in it. The next line is personal individuals, crowdfunders. But people generally put money in something because it's getting a return. If you brought out a tax break and said to a 40 per cent tax payer "put money into the social enterprise into your area, you can offset that against your income, at 40 per cent", you will get a bundle of people putting money in. You can incentivise people to do that for their community.

The third area I would go to is government. What I don't know is what you value every £1 that government puts in by way of intervention in the context of what good it does in the community. From a political perspective, it need not necessarily be getting your cash back with a 4 per cent return. It may be that we create another 50,000 jobs or we take people off benefits. Then you get the banks and, as I've already said, they currently find this a difficult area to assess.

So there are four ways. You've got to look at each of the components and work out what the reason is for each of those.

Nick Hurd We're trying to build something different. We're trying to prove the proposition is that you can invest for social progress *and* get your money back, with a return. So actually we're trying to construct something that's completely different from the mindset that you've just set out.

Jonathan Jenkins The UK has the most supportive enabling environment for social investment by a *mile*. We have a wholesale bank of size; we have supportive technical assistance intervention, so we've got the investment readiness. The market just needs time, to understand where it works best. Kate picked up on "culture". We need commissioners to get much more comfortable with the social impact bond models. We need to see a move from the traditional models to more mission-related investing. It's time to deliver. Banks putting risk capital to work in this market are Deutsche Bank, JP Morgan, Bank of America, Goldman Sachs. Notable by their exception are the UK clearing banks. It's our job to give them the data and the comfort to actually put more money to work in the space.

Wray Irwin The bit that gets missed is that you can do good *and* make a profit. But on the demand side, there is a total lack of understanding of how the market works, so transaction costs that investors have to get involved with in terms of due diligence prices a lot out of the market.

There's also something to address on the supply side. Is it developing new models that can address some of these issues in this market, or are we trying to retrofit mainstream models within the sector? There seems to be a bias towards that. So we're looking at how the two are coming together over the next couple of years in a European research project.

Caroline Julian In terms of "rigour", intermediaries can play a key role. Our recent research on the growth of social enterprises in church and faith-based initiatives shows, it is an untapped opportunity. New social intermediaries such as Resurgo Social Ventures are in a better position to know who would be worth investing in. I wonder whether there's room for more partnerships to boost the growth and really ensure that we do have some rigor and do reduce that risk.

Matt Robinson For the social enterprises and charities who have some track record, the loan books are long enough to look at eight to ten years of data. Maybe they could pull in more mainstream channels.

Kate Markey For me, these charities are absolutely the kind of organisations that we should be supported to take on social lending. Use that data to persuade their boards, who may have issues attached to risk, about how that could transform their mission and their impact.

Peter Holbrook The Cabinet Office has been doing some fantastic work to move this agenda forward. But some of the other offices like the Department for Business, Innovation and Skills (BIS) need to get with this programme. BIS allocates tens of billions in grant funding. It should open up existing funds to ensure that they are social enterprise-proofed. You can't just look to one government department to innovate and create new financial products.

The Social Value Act created a market that rewards good social value creation, and government can do more to strengthen markets that create these types of outcomes. My mum isn't particularly socially liberal, but she would love a social ISA. Better pension fund disclosures, more retail products for smaller investors, so they can invest in their local communities and in the social infrastructure of this country – I think that would resonate with people who are fed up with the financial services industry.

Nick Hurd The market is dominated by specialists and we are trying to expand the range of people who get involved. The good news for Peter's mum is that, in about two months, she will be able to invest in a genuine social ISA.

Social impact bonds have increased largely because of the Department for Work and Pensions (DWP) innovation fund. When we knocked on the doors of the 39 local enterprise partners, we found a really worryingly small percentage were even thinking about social enterprise in terms of their social inclusion strategy. We've engaged with that.

PHOTOGRAPHER SOPHIA SCHORR-KON

> "You need financial instruments as diverse as the sector"
> Peter Holbrook

We haven't really talked enough about capacity to absorb investment within the less mature element of the social enterprise movement. The National Citizens' Service, which is a £200m market now, could only absorb and scale up because of the capacity-building support they had – in their case from Social Business Trust – which has brought in pro bono expertise from the private sector. There are other models out there; it's a very important part of the landscape. We have lots of social enterprises; but very few big ones.

Sophi Tranchell Government can make sure that it doesn't over-regulate unlisted shares because that is going to make things more difficult. These are the people who are actually prepared to take high risks in startups in the way that doesn't mean we have to give directors' guarantees when we're not going to get any money out of it. I don't own shares in Divine so why should I put my home on the line for the government?

Rupert Evenett On the early stage stuff, grants and social investments are linked. A key success factor in investments we've seen is where grants have been alongside, or in an earlier stage of the investment.

As an industry, we could be collaborative and mutual about this and create a data infrastructure for social investment. Then we can all share each other's confidential highly sensitive data in a trusted way, mutually owned and collaboratively run, of as well as for the sector – a social enterprise in itself; that it just nails it.

Jon Bernstein Clearly financial return is relatively easy to measure. How do you know you've had social return?

Kate Markey Investors see the change created for the beneficiaries of the social enterprise. What change happens? What you can take credit for? What would have happened anyway?

Caspar Mackay Many organisations are actually not measuring outcomes – the outcome of apprenticeships is not training, it's employment – sustained employment.

Caroline Julian To respond to Peter Holbrook's point about government departments, there's a very interesting role government can play. Quite a bit of our research recently has been about communities that set up co-operatives to generate their own electricity. One of ▸

the key models we've found is a joint venture where developers and private businesses have said to a community "own part of our wind farm" or hydro-scheme; or communities have approached the developers and said we want to buy X per cent of your shares and invest that; so there's a role for government to facilitate those partnerships and that growth.

Sophi Tranchell In the alternative energy market people are investing in the thing they can see. They're investing in their local community, not paying for a lot of finance people to get rich.

Peter Holbrook You need financial instruments that are as diverse as the sector is. We need to be slightly patient but we need to keep our foot firmly on the accelerator and keep innovating different instruments to meet the broad spectrum of social enterprises looking for finance.

Jonathan Jenkins Whoever cracks retail wins, and a big part of the solution is data. The social investment community has to find a way to feel comfortable in investing in for-profit or profit-with-purpose organisations or we're never going to shift the £600m plus leverage into the market because the current capacity can't absorb that degree of capital.

Matt Robinson At the moment, social investors are predominately government and foundations who have invested in lieu of grant making. We will know a lot more in the next couple of weeks about whether tax relief will help crack the retail nut. Then there are pension funds. I suspect there are some movements led by local authority groups and they will fit part of the capital curve for the long-term climate. So, crack those three and we could be motoring.

Wray Irwin There's a perception that this is a niche market of specific organisations and isn't for everybody, so the big leap is getting it into mainstream consciousness. Then addressing that risk perception through developing better skills in the organisation, but seeing it as part of a mixed portfolio of investment.

Paul Ruddick I run a social enterprise SME and a private SME and, to me, the social enterprise is a much higher risk. The social SME is more complicated; there are different drivers. When raising money on the social side, you have to go through this whole circle of social impact. It absorbs time and resources. I think that needs to be recognised in the early start funding. There needs to be a grant. It's just a difficult beast.

Kate Markey I go back to my point about transparency; data will be absolutely critical. We're trying to create something new here; I have a sense that we're all desperately rushing. But we're trying to create social change and it's about creating a sustainable market. I recognise the balance of mission and enterprise; I've come across some very good people from the social sector who are very commercially driven; hopefully, they are the ones we're going to support.

"I'm a great believer that data unlocks capital"
Rupert Evenett

Caspar Mackay Scale is critical. Most of the organisations in this sector are sub-scale. What I would like to see is much coming more from government on building skills in the organisations. Lots of support comes from outside organisations, but as soon as that support is over, the team moves on and works with someone else and the reality is that they haven't built the ability of writing bids or raising finances that they need for the longer term.

Peter Ibbetson Risk and data are key. When the bank loans money it needs to know that it will get the money back at some stage, otherwise its business model is unsustainable. Unless, of course, you can genuinely demonstrate (which comes back to the data point) a measurable value in not getting that money back – that is, the value is created or returned in another way because your investment is delivering against another objective.

Nick Hurd Post-financial crisis there is a shift in social values towards much greater interest in the values of organisations we do business with or who employ us. A very socially responsible generation is coming through. There is a sense of movement; movements need leadership.

I think we're recognised as a world leader in this area. The prime minister had lots of stuff he could have put on the G8 agenda and he put social investment on it. Lots of people were thinking "What?!" Actually, the response from other countries has been fantastic; they want to learn more about this.

Don't lose sight of the fact that, of the flagship organisations that have put up the £600m, no taxpayers' money is involved; £400m of it came from dormant bank accounts, handed over voluntarily by the banks; and £200m of risk capital was put in by our four biggest banks.

My hope is that they don't look on it simply as an exercise to keep government quiet, but regard it as a laboratory, an opportunity to learn about a new market and to see the commercial opportunity that Peter talked about. Or, more laterally, see the possibilities in what organisations like Lloyd's are doing, getting their people out to communities to learn by sharing their own learning, and building capacity in social enterprises. It is about trying to make something that isn't dominated by social investment geeks but is a wider movement that incorporates all elements of society.

Jon Bernstein Thanks Nick, and thank you all very much.

PHOTOGRAPHER SOPHIA SCHORR-KON

Success requires a complex blend of strategies

by Mark Boleat

There is a mismatch between the type of capital that is offered by investors and that which is required by most social enterprises

Britain has been home to a thriving entrepreneurial culture since the Romans founded the settlement of Londinium almost two millennia ago. During this time, the exciting opportunities opening up to entrepreneurs have changed markedly, with apples replaced by apps, and wool by widgets.

Less obvious, but equally significant, is the shift in attitudes towards entrepreneurship. More investors today are interested in leveraging capital to change lives as well as generate financial returns. As approaches change, social impact investment is a growing area where the UK can take a lead. Recent research by Barclays found that, of the UK's growing number of small and medium-sized firms, whether social or not, only 5 per cent seek finance from banks, with 11 per cent preferring to borrow from family and friends! Clearly, alternative funding sources are vital to financing entrepreneurial growth.

Traditional investors are looking for near-market returns on their investments

A recent report from Sonen Capital suggests that an impact investment portfolio can now compete with – sometimes outperform – its traditional asset allocations. Potential investors, from pension funds to charity foundations, which the City of London Corporation has spoken to prioritise receiving near-market returns, although security of return of capital was more important than dizzying double-digit returns.

This is where guarantees, underwriting, or mixed repayable and non-repayable finance can help create suitable finance packages. The growing number of funds emerging, in part catalysed by Big Society Capital's wholesale finance, has been a response to the preference for investors to make larger-scale investment opportunities. Investors also sought evidence of a track record and a clearly defined exit strategy from their investments. Any preference for debt financing would help this. Lastly, investors also needed to know that the expected social returns were tracked and generated, but generally were less concerned about how impact was measured.

The growing interest from investors was reflected at the recent Global Impact Investing Network conference held at the Guildhall which brought together more than 300 interested investors from 35 countries. Deutsche Bank has allocated capital to impact activities in 2011, and several others have created their own impact funds or function. Excitingly, demand has come from charities such as Scope, Golden Lane Housing and Broadway, which have created bonds offering new institutional and individual retail investors fixed rate returns of 2-5 per cent. Hopefully, the tax relief for social investment expected in next year's Budget, will help further encourage individual investors, as long as they can access the interesting social investment products.

Initiatives are under way to help track performance in this sector; a pilot scheme called EngagedX is developing a performance index of historic deals, with a view to getting closer to being able to identify and even price the risk of a social investment. The Social Stock Exchange, launched at the G8 conference, shines a light on listed companies that measure their impact and deliver value to society and the environment.

So what is really holding back the market? There is a mismatch between the type of capital offered by investors and that needed by most social enterprises. Working capital, which helps them bid for and deliver contracts, is in short supply. Only £10m of the £202m of social investment dispersed in 2012 was in the form of working capital. The rest is all secured lending against, or for, purchasing an asset. The effect is that social enterprises miss out on contracts to deliver the outcomes society so needs.

More fundamental is the potential hesitancy about the role of social investment. What kind of services does society want and need? Do our social enterprises provide and articulate their ability to deliver benefits over private-sector mainstream competitors? Is it finance that holds them back? Only then should we consider whether social investment is part of the answer.

Growing interest from mainstream investors signals a new financing source, which seeks to create measurable social and financial returns. Yet investment is only one tool to ensure the sustainable growth of social enterprises. Other resources – people, buildings and information – all have a role to play in helping to transform our society and economy for current and future generations. Only then can our entrepreneurial culture thrive for the years to come.

Mark Boleat is policy chairman at the City of London Corporation

Thinking outside the box

These social enterprise stories deftly show how "business" and "social good" can come together when they eschew traditional corporate social responsibility

The Wise Group – partnerships for a fairer society

For 30 years the Wise Group has been transforming lives and tackling social, economic and environmental issues in communities. Its vision is to realise people's potential, create a fairer society and contribute towards sustainable economic growth.

What started as a local project in Glasgow (its headquarters are still there) has developed to deliver services and meet the needs of communities across Scotland and the north-east of England. Most of its work comes from competitive tendering for contracts from government departments and agencies.

The group works with public-, private- and third-sector agencies and organisations to meet shared goals. It also supports other social enterprises by involving them in the delivery of contracts that can help them fulfil their potential. Partnership working is an essential component of everything it does, and it has invested significant resources in ensuring that its values are central to its identity. Its belief is that this is realised through the commitment, capabilities and behaviours of staff. This involves a focus on culture through leadership and individual capacity building as the drivers of excellent performance.

In 1983, the Wise Group developed a response to high unemployment in what was, at that time, known as the intermediate labour market. This involved retraining long-term unemployed people in the skills that could be used to undertake valuable work in communities. Initially, this involved insulating social housing, landscaping and environmental improvements. Participants gained new skills, real work experience and support with job searching. Since then, it has helped more than 40,000 people move off benefits and find employment. Clearly, this has financial benefits for individuals and families, but customers also say that paid work has led to increased self-confidence, and improved health and wellbeing. These factors have an impact on enhancing performance in the workplace.

Over the past 30 years, the Wise Group has improved the insulation in thousands of houses, helping householders make energy efficiencies and save money on fuel bills. Now it manages home energy advice centres for the Emery Saving Trust, fuel poverty projects for local authorities and other green energy work.

For the past eight years, the group has been pioneering an approach to reducing reoffending by employing mentors to work with short-term prolific offenders on release from prison in Scotland. The aim is to help them to reintegrate with their families and communities as a first step to transforming their lives and changing their behaviour. The majority of the mentors are ex-prisoners or ex-offenders.

Laurie Russell, chief executive of the Wise Group, says: "Our success is based on having committed staff, strong partnerships with local authorities, housing associations, community organisations and employers. We have a reputation for delivering excellent performance and outcomes with a demonstrable social impact, and have a proven track record of providing innovative, quality services and solutions. We have delivered contracts for government at different levels and developed internal quality and governance systems for measuring the impact of contracts. We also use social return on investment and social accounting to quantify our impact."
thewisegroup.co.uk

Divine – owned by cocoa farmers, made for chocolate lovers

Divine is a chocolate company on a mission to deliver a sublime experience to chocolate lovers everywhere, while raising the bar on what it means to trade fairly with farmers, and do business better.

Back in 1997, a cocoa farmers' co-operative in Ghana called Kuapa Kokoo ("good cocoa farmers" in the local Twi) voted at its AGM to set up a chocolate company to access a share of the valuable UK chocolate market. Twin, an NGO specialising in helping smallholder farmers organise and access the Fairtrade market who had worked with Kuapa Kokoo since 1993, came to the UK to find potential investors in this new idea – a farmer-owned chocolate company.

Pauline Tiffen, one of the original team at Twin, remembers: "Emboldened by pulling off Cafédirect and moving into profit after three to four years, we packed the Divine proposition with our most politically perfectionist dreams of bringing cocoa farmers closer to consumers, and changing the way chocolate is both seen and eaten. We were determined to take on the handful of global chocolate giants."

This bold vision compelled Anita and Gordon Roddick to come on board, and so The Body Shop, along with Twin, were the first shareholders of the Day Chocolate Company (named after Richard Day who played a great part in helping the co-op set up), which was established as a limited company in 1998, with the additional support of Christian Aid and Comic Relief. A unique piece of developmental finance support from the Department for International Development, which guaranteed a bank loan, enabled Kuapa Kokoo to own 33 per cent of the business, a first for cocoa farmers.

The company was established "to improve the livelihood of smallholder cocoa producers in West Africa by establishing its own dynamic branded proposition in the UK chocolate market, putting it higher up the value chain". Building the brand was key to added value and a brand agency was commissioned to find the right name, launched as the Divine Fairtrade bar.

The first managing director was Sophi Tranchell, a young marketeer burning with a desire to see social justice at the heart of business. In 2006, The Body Shop, staying true to its vision to see cocoa farmers empowered and benefiting from their business, handed over all its shares in the company to Kuapa, making it the largest shareholder with 45 per cent of the business. On 1 January 2007, Day Chocolate changed its name to Divine Chocolate Ltd to more closely align the company with the brand. That year Divine handed over the first profit dividend to the farmers.

While Divine Chocolate has been growing past the £7m point, Kuapa Kokoo has been flourishing, growing its membership to 65,000 and investing hundreds of thousands of pounds of Fairtrade premium and Divine dividend in its farmers, improving their living standards, and growing their business.

Owning their own chocolate company, with representatives on the Divine board, has delivered more than additional income to the farmers. They have a direct influence on how the company is run, and have been able to use their company share as collateral to attract loans at preferential rates. They have also been able to gain a stronger voice and influence in the industry.

Divine Chocolate is proud to have mobilised consumers, and catalysed real change in the world of chocolate – creating a market and a supply chain that encouraged Cadbury's to convert its Dairy Milk brand to Fairtrade, soon followed by Nestlé (KitKat) and Mars (Maltesers). Divine has brought social enterprise into the mainstream, proving the commercial viability of business models with money and decision-making in the hands of the many, not the few. The company aims to further increase availability in the UK and grow worldwide (there is a sister company in the US, and distribution in Canada, Europe, Asia and Australia).
divinechocolate.com

Five Lamps – tackling financial exclusion

In September 1987, Margaret Thatcher took her famous "walk in the wilderness" on the site of the former Head Wrightson steelworks in Thornaby, Stockton-on-Tees. Some two years previously, a small community project called Thornaby Impasse had been established to support the young local men affected by the steelworks closure back into employment. In 1989, the name changed to Five Lamps, recognising a prominent local landmark and meeting place. Now, still based nearly 400 yards from the spot where Mrs Thatcher was iconically photographed, Five Lamps has developed into one of the most successful social enterprises in the North of England.

The initial focus on the Thornaby community has been succeeded by a truly regional footprint. Five Lamps' range of social, economic and financial inclusion projects and programmes now spans the area from Berwick to South Yorkshire and impacts on some 25,000 people each year.

The Five Lamps service portfolio is continuously evolving. Management is always looking to meet need identified in the organisation's work in the most disadvantaged communities. Current services include providing unsecured personal loans to individuals unable to access affordable credit or mainstream financial services; support for the long-term unemployed and for families with complex needs; business start-up mentoring and coaching; youth services; managing a regional loan fund to bring houses up to a decent standard; providing access to finance schemes for new businesses; energy savings advice; supporting pre-release prisoners; delivering a MyBnk franchise to promote financial literacy in schools and refurbishing empty properties in County Durham and Darlington.

The CEO, Graeme Oram, joined the organisation in 2002 and says, "We offer a particularly diverse range of services which are becoming increasingly integrated. Our customers are able to use any of our services to access others. This is particularly the case for our financial inclusion customers. What bank can you go to where you might find support to turn a hobby into a business or progress into your first job for 15 years or achieve your first formal educational qualification? We are driven to create possibilities and change lives."

The success that Five Lamps has enjoyed has been predicated on a long-term strategic shift from grant-reliance to earned income from contracts and, more recently, from being able to finance initiatives from its own balance sheet. From being 100 per cent reliant on grants in 2002, the organisation was 98 per cent funded by earned income by 2009.

Contract performance and growth were particularly strong but management was keen to better demonstrate the impact that Five Lamps made on its customers' lives.

Leaders meet Muhammad Yunus in Bangladesh

Graeme Oram explains, "We featured in the initial RBS SE100 Growth Index in 2010, but were amazed that only a handful of organisations in that list achieved a full score for impact measurement. We committed, there and then, to produce social accounts and were delighted that we were shortlisted in 2011 and won the RBS SE100 Impact Champion in 2012. Social accounting has transformed our business in so many ways."

The economic impact of Five Lamps is strong. This year, nearly 2,000 people will leave benefits into jobs and business start-ups; financially excluded individuals will receive over 15,000 loans totalling nearly £6m, enabling money to be recycled in local communities; the first phase of 35 refurbishments of empty homes will create local jobs as well as placements and tasters for young people and most programmes will strip away barriers to economic inclusion.

Graeme recognises the challenges that social enterprises face as they seek growth to scale, "Too many social enterprises are unable to access finance at the point of growth or may be too one-dimensional to spread risk. We are working in a period where our services are needed more than ever, yet there are fewer, typically bigger contracts, that social enterprises can bid for.

"We are fiercely ambitious. We have built what I believe to be a unique service portfolio. We have built a positive corporate CV – IIP Gold; Best Companies 2011 and 2012; Impact Champion 2012; Ernst & Young 'Social Entrepreneur of the Year' North 2013 and recently shortlisted for Local Enterprise Agency of the Year; but most importantly we have built a team of brilliant people committed to changing lives. We seek to be brilliant partners."

fivelamps.org.uk

Wavelength – access to world-class leadership

Wavelength was created five years ago with the goal of changing the world for the better through business. Wavelength is active now in Europe and the US and works with ambitious business leaders, entrepreneurs and social innovators from across sectors to build their knowledge, insights, resilience, connectivity and networks.

In the UK, Wavelength runs a membership club called Connect which each year brings together 120 leaders from some of the country's most successful brands, such as Dyson, Rolls-Royce, Sainsbury's and John Lewis and a wide range of social enterprise CEOs and founders from across the country. The business operates a cross-subsidy model and, although they pay less, the social enterprise leaders are not in the room as supplicants but as equals.

One of the three founders is Liam Black, one of the UK's best known social enterprise leaders. He has founded and led some dozen social businesses including Jamie Oliver's Fifteen which, with the celebrity chef, he grew into a global brand.

Says Liam: "I made so many mistakes when I was starting and scaling enterprises. One big reason for me to create Wavelength was to offer social entrepreneurs access to the world-class quality of leadership learning and connectivity which is taken for granted in the higher echelons of the private sector. There is a leadership deficit in the social enterprise world and, if it is to come out of the margins, we need leaders who know how to create fantastic customer service, how to attract and retain great talent, how to maintain innovation at scale. This is best learned by looking at how world-class businesses actually do it, not by reading books or attending conferences to listen to gurus. So we bring entrepreneurs, innovators and business leaders from all over the world – India, Silicon Valley, and Nairobi – to provoke, teach and partner.

"We try through Wavelength to help them fast track their learning and make the partnerships which can take them from local player to market leader."

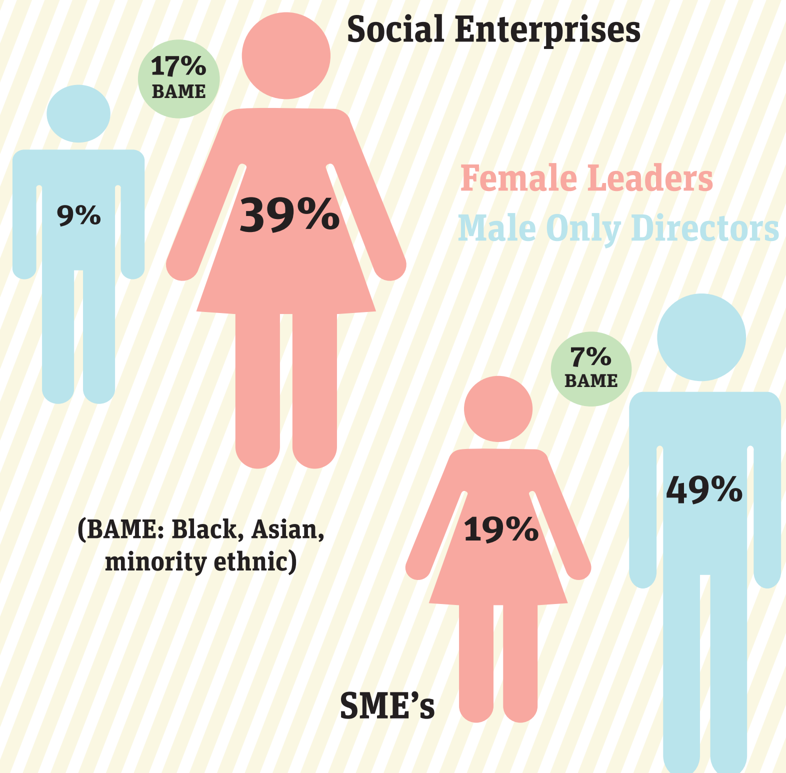
Liam believes that scalable social innovation is more likely to happen in the messy often uncharted territory between sectors, and part of Wavelength's mission is to convince business leaders that they must go far beyond traditional models of corporate social responsibility. And they go to some lengths to do this – having, for example, taken over 50 leaders to Bangladesh to see first-hand what the Nobel Peace Prize laureate Muhammad Yunus is learning in his social business partnerships with multinationals such as Danone.

"Whatever you call it – shared value, corporate social innovation – big companies will have to move on from the binary view of a world in which here there is 'business' and over there 'social good'. But this is huge leap for leaders in their mid-forties who have been formed by business schools and a corporate culture which has as, Yunus puts it, a one-eyed view of the world and humanity. Through Wavelength, we are trying to help create that generation of leaders which the world so badly needs to find new ways of creating wealth which does not destroy the environment and create inequality.

"We believe in experiential learning," says Liam, "in leaders learning from leaders and the power that lays in bringing people together whose paths would never cross in day-to-day business."

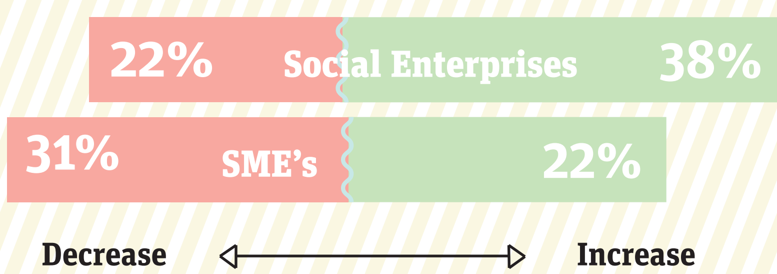
www.thesamewavelength.com

Leaders of social enterprises come from more diverse communities than those of traditional SMEs



Predicted growth of the social enterprise investment market

Social enterprises have seen more increases in turnover than SMEs in the last 12 months



Where social enterprises work: by level of deprivation compared to SMEs

Band	1	2	3	4	5
Social Enterprises	38%	26%	14%	9%	7%
SME's	12%	19%	21%	26%	22%

Most deprived ⟷ Least deprived

Sources: State of Social Enterprise Survey 2013 (SEUK/ RBS)/Source: Small Business Study 2012 (BIS, 2013)/ The First Billion (Boston Consulting Groups/Big Society Capital, 2012)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