Investment readiness and sustainability: Social investment as a third sector panacea?

POLITECNICO DI MILANO

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Structure

- In this seminar we will explore:
  - Research overview.
  - UK social investment context.
  - Investment readiness & sustainability.
  - The case-study investment readiness support programme.
  - Methodology.
  - Results & discussion.
  - Implications.
  - Further research.

Research Overview

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- Seeks to explore investment readiness in the UK ‘voluntary, community and social enterprise’ (VCSE) sector. Specifically in relation to:
  - Social investment.
  - Grant funding support programmes.
  - UK policy vis-à-vis social investment.
  - VCSE sustainability.

- Utilises data gathered from a UK investment readiness support programme (IRSP):
  - IRSP offers VCSEs grants to increase their IR.
  - Seeks to build capacity in the support provider market.
  - Seeks to increase deal-flow in the social investment market.

UK Context

- UK VCSE sector includes over 160,000 organisations, contributing £43.8 billion to the economy and employing 827,000 people (NCVO, 2016).

- The UK VCSE sector has increasingly been seen as a legitimate deliverer of public services in the last 20 years & as a means of reducing social inequality (Austin et al., 2006; Amin, 2009; Haugh and Kitson, 2007).

- Policy-makers have promoted a vision of a VCSE sector that is more business-like, entrepreneurial and better governed (Macmillan, 2011; Wells, 2012).

- Focus on new methods of financing public service delivery:
  - Social Impact Bonds (currently 32 in the UK).

UK Context Cont'd

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- Policy-makers are encouraging VCSEs to focus on investment as a means to achieve sustainability, scale the business, and achieve greater impact (Wells, 2012; Hazenberg, Seddon and Denny, 2014; Moore et al., 2012).

- Creation of Big Society Capital:
  - £600m social investment wholesaler.
  - Capitalised with £200m from banks and £400m from dormant bank accounts.

- Social Investment Tax Relief:
  - 30% income tax rebate on investments made.

- Outcomes-based commissioning:
  - Creation of the Government Outcomes Lab (www.golab.bsg.ox.ac.uk).

Social Investment Markets

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- Social Finance involves investment in social ventures (SVs) based upon a 'blended value' return model (Emerson, 2003)…

- The 'Social Investment Market' (SIM) is the market-place in which this takes place & involves three elements (Nicholls, 2010a)…
  - ***Supply-side:*** *'*Social Investors' who provide finance to SVs either directly or indirectly through intermediaries (i.e. social banks, charitable funds & the UK government).
  - ***Demand-side:*** SVs that seek investment either for start-up, sustainability or scaling-up purposes (i.e. social enterprises, charities, cooperatives, social businesses) (Nicholls & Murdock, 2011).
  - ***Intermediaries:*** SIFIs that provide support to the supply/demand sides of the SIM and provide links between both.

- Evenett & Richter (2011) state that at the present time the SIM is an intermediary market, dominated by SIFIs.

Prior Research on Social Investment Markets

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- Academic research into social investment is a growing but still nascent area still dominated by policy documents & practitioner reports (Nicholls, 2010a; Moore et al., 2012).

- However, growing literature now exploring different models of social investment [see: Nicholls & Daggers (March, 2016) for a good overview of research in the area].

- Existing research suggests that VCSEs are characterised by:
  - Lack of business skills (Bugg-Levine & Emerson, 2011).
  - Poor governance structures (Hines, 2005; Hill, 2011).
  - Business plans that lack detail (Howard, 2012).
  - Lack of knowledge of social investment (Hazenberg et al., 2014).

- This has been termed as a lack of ***investment readiness***.

Investment Readiness

- Gregory et al. (2012:6) define ‘investment readiness’ as *‘…an investee being perceived to possess the attributes, which makes them an investible proposition by an appropriate investor for the finance they are seeking.’*

- Conceptions of investment readiness in the SIM are similar to those found in mainstream finance literature:
  - Business proposal viability (Mason & Harrison, 2001).
  - Management team strength (Kollman & Kuckertz, 2010).
  - Desire to seek investment (Deakins *et al.*, 2008).
  - Personal Relationships (Wilson *et al., 2007).*

- However, there are also other areas that are important that are unique to the SIM & ‘blended return’ (Emerson, 2003).
  - Social Impact (although no standardised framework or evidence of this social impact are required).
  - Willingness to take risks (SVs are seen as risk-averse).
  - Diversity of income streams (Hazenberg et al., 2014).

Sustainability

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- Sustainability is also a growing concern when assessing the ‘health’ of the VCSE sector.

- VCSE sustainability is based upon (Jenner, 2016):
  - Organisational resilience & robust organisational structures.
  - Enhanced marketing strategies.
  - Network and partnership formation.
  - Increased & diversified commercial revenue.

- Social venture sustainability is dependent on the ability to *‘gain resources and legitimacy, create co-operation between institutions and develop internal managerial and organisational capabilities’* *(*Sharir, Lerner and Yitshaki, 2009:90).

Sustainability cont'd

- Social venture sustainability occurs through the facilitation of access to the ***most appropriate resources*** that facilitate increased commercial & social impact growth (Jenner, 2016).

- Through this analytical lens, it can be argued in many ways that investment readiness and sustainability are ***effectively the same concept***.

- Therefore, this research seeks to argue that:
  - Investment readiness support programmes are an ***effective means*** of bolstering VCSE sustainability.
  - However, the dominant narrative in the UK centred on social investment as the main means to achieve sustainability is misguided.

- Indeed, the wider policy narrative around social investment ignores the needs of the majority of VCSEs in a way that can be dangerous to the future sustainability of the sector.

IRSP

- IRSP is a £10m fund that offers grants to VCSEs seeking to become investment ready:
  - VCSEs seeking investment up to £500,000 in value are eligible.
  - Grant funding of up to £75,000.
  - Funding to be used to pay for specialist consultancy support from approved support providers to build capacity in:
    - Governance and management.
    - Financial accounting.
    - Market awareness.
    - Business planning & modelling.
    - Social impact measurement.
    - Develop investor networks.

  - Seeks to offer 250 grants over a 5 year period.
    - Currently 3 years into the programme.

IRSP 7 Stages

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1. **Online registration:** Through the programme web portal.
2. **Online diagnostic tool:** Completed by the VCSE, this online tool automatically assesses investment readiness;
3. **1:1 support advisor session:** Carried out by a specialist programme advisor to further assess investment readiness;
4. **Selection of a 'support provider':** The VCSE selects from a list of 'approved providers'.
5. **Submission of a grant application:** Detailing the investment readiness work to be completed and the grant funding required.
6. **Assessment of grant application:** Applications can be rejected, accepted or asked for revisions and resubmission;
7. **Post-grant work**: Completed with the support provider to develop investment readiness (if successful) up to 12 months post-award.

- The Diagnostic Tool was developed by a Programme Partner based upon their work in the VCSE sector over the last 10 years.

Methodology

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- The research seeks to assess the efficacy of the IRSP in increasing the investment readiness & sustainability of VCSEs.

- Adopts a mixed-methods approach to this evaluation utilising:
  - Quantitative organisational demographic data captured through the Diagnostic Tool (n=527).
    - Data analysed in SPSS v22.0.
  - Qualitative data in the form of semi-structured interviews held with VCSEs, Providers & other key stakeholders (n=22).
    - Data analysed utilising narrative method (Feldman, 2004), in relation to the 7 stages of the programme.

- 5 core themes, namely: ‘Programme efficacy’; ‘Provider/VCSE values’; ‘Investment Readiness and Sustainability’; ‘Panel Decisions’; and ‘Social Investment’ emerged from the interviews.

- Final research aims to at least double these sample-sizes.

VCSE Organisational Data

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Table 1 – VCSE Demographic Data							
Demographic Variable		*N*	*Mean*	*Median*	*SD*	*Min.*	*Max*
VCSE age (years)		507	14.09	7.81	16.72	<1	112
Turnover		506	£1.18m	£277,500	£3.15m	£0	£41.3m
Net profitability		357	£30,194	£3,000	£85,495	£-79,924	£997,637
Total assets		503	£927,668	£109,079	£4.05m	£0	£60.64m
Total debt		454	£240,386	£17,025	£776,123	£0	£10.84m
Investment needs		511	£599,555	£250,000	£4.15m	£0	£90m
Income diversity *(% of income from top 2 customers)*		480	66.3%	70%	26.5%	1%	100%
Public sector reliance *(% of income from public sector)*		410	51.4%	50%	31.8%	0%	100%
Staffing	FT	518	14	3	48	0	847
	PT	516	15	3	49	0	847
	Volunteers	513	127	10	1605	0	35000

Nb. N < 527 as some organisations did not complete all parts of the diagnostic tool.

VCSE Trends

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- The data in Table 1 reveals that:
  - **Investment need** is significant when compared to turnover.
  - **Profitability** is low, making the servicing of debt difficult.
  - **Income diversification** is poor, with a heavy reliance on two or less contracts (70%).
  - **Volunteer reliance** is also high, with over 3 volunteers to every member of FT staff.
  - **Asset to debt ratios** are good, with relatively high asset and low debt levels (6/1 ratio).

- Based on this data, the investment readiness of the VCSE sample can be considered low due to poor financial stability.

- This data identifies why the majority (77.5%) of UK social investments take the form of secured lending (Robinson, March 2016).

IR Diagnostic

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Table 2 – VCSE DT Scores			
Factor	*N*	*IR Score*	*SD*
Investment readiness score	467	53.7%	18.8%

N < 527 for the overall data as some organisations did not complete all parts of the diagnostic tool.

- Diagnostic Tool scores for the VCSEs also demonstrate the overall low IR of the sector:
  - A score of 70% is considered the minimum to be considered investment ready.
  - VCSEs scored only 54% on this tool at application.
  - VCSEs scored particularly low in:
    - Governance and leadership (51%).especially in relation to the board's strategic control (44%).
    - Social impact measurement (41%).

VCSE Weaknesses

The weaknesses surrounding governance/leadership & social impact measurement were also exemplified in the qualitative data:

"We haven't really paid that much attention to our governance systems and how we manage ourselves over the years because we've just been two blokes doing what we do." (P17 – VCSE)

"The areas that the consultancy support came in was around doing a skills audit with our board……and here we'd got an external organisation who were offering us some advice about the mix of skills on the board." (P20 – VCSE)

"I think with [VCSE]*, they came in and they were kind of like, 'Social Impact, what's that?' you know. And so I think what we managed to do in that six months was to create framework for them…to help them understand what their social impact might be."* (P13 – Provider)

Sustainability & Scale

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However, the data also revealed the need to develop sustainability in ways that were not often related to securing social investment:

Income diversification: *"We have quite a forward thinking board of trustees of the charity, they had rightly recognised that the income streams were changing and that we needed to move with the times, and we needed to be proactive."* (P20 – VCSE)

Capacity Building: *"It's not just about becoming investment ready. Yes, that is the focus of the programme but actually there's a whole lot of spin-offs in terms of the capacity building and strengthening and the culture change within the organisation which is a bi-product of the investment readiness journey."* (P15 – Provider)

Scaling Problems: *"It's not always about scaling up, actually……It's about creating the opportunity for generating a mixed portfolio of income……it's not about increasing your turnover, it's about becoming more profitable……"* (P16 – Provider)

Social investment as a policy panacea

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- Growing state retrenchment in tackling social problems due to budgetary constraints means a robust VCSE sector is critical.

- There is a clear need for social investment as evidenced by the increase in deal-flow of 20% per annum over the last 5 years (Robinson, March 2016).

- However, the focus on social investment as the main tool of scaling the VCSE sector is a mistake, that ignores:
  - The lack of suitability of investment for many VCSEs.
  - Not all organisations can or want to scale their product.

- Sustainability should be the focus with broad tools utilised to support this (Sharir, Lerner and Yitshaki, 2009; Jenner, 2016).

- The smaller-end of the VCSE sector is potentially the most in need for this support (Macmillan, 2015).

Further Research

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- This study is ongoing with data collection to continue for a further two more years. This aims to:
  - Increase the dataset in size, with broader samples of qualitative data and a larger quantitative dataset of organisational demographics.
  - Longitudinal case-studies will also be carried out to assess the long-term impacts
  - Longitudinal data is also being captured utilising the diagnostic data.
  - Wider perspectives of policy-makers is also being sought.

- Additional research is also needed in this area to explore:
  - The investment readiness of the wider VCSE sector including larger-scale organisations.
  - Identifying alternative methods of driving sustainability outside of IRSPs.
  - Exploring alternative models for social investment, outside of the Anglo-Saxon sphere.

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Thank you
for listening

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