

CAPITAL INVESTMENT

PRIVATE FINANCE
FOR SOCIAL
PROBLEMS



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GLA CONSERVATIVES
GREATER LONDON AUTHORITY

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EXECUTIVE SUMMARY

London's social enterprises are growing and many are increasingly choosing social investment as the prime financial means of funding their activities but at present, the social investment market is dramatically underperforming. If the current demand for social investment was met through the recommendations outlined in this report, London's social investment market would grow from £142m to £332.5m - an increase of 233 per cent. This growth has the potential to generate in excess of £3.6bn regional economic gross value added (GVA), and safeguard almost 200,000 full time equivalent (FTE) jobs within the next three years. Without intervention, London's social investment market could be worth in excess of £28bn by 2030, and therefore any efforts to assist the market today could have huge positive returns in the future.

Social impact bonds (SIBs) are a type of social investment that has the potential to offer significant savings to public sector bodies, while making returns for private investors, and supporting a range of socially beneficial programmes (see Fig. 1). A London-wide SIB to reduce the number of adolescents in care could help over 10,000 vulnerable young people and generate savings of over £0.4bn each and every year after the project's inception¹. Moreover, with 'over 65' being the fastest growing age group in London², care for the elderly will become increasingly important, and as a result, social initiatives to improve end of life care for cancer patients in London could producing savings of as much as £16.9m per annum³. In addition, if a London-wide SIB programme to reduce the number of crack/opiate users was instigated, over 62,000 people could receive practical help, reducing pressure on public services, and saving government up to £9.4bn over the drug-users' life times.

The Mayor has engaged as a willing participant in the social investment market, commissioning a SIB to reduce homelessness and assist rough sleepers, but clear leadership has yet to materialise. If London's social investment market is to grow to its full capacity, the full support of City Hall will be needed to break down market barriers that exist for London's social enterprise, investors, and public bodies. This report therefore makes the following recommendations:

To support potential commissioners:

- 1. Coordinate London's governing bodies:** The Mayor should use his influence to bring London's governing bodies (boroughs, London Councils, NHS, police, etc.) together to become social finance co-commissioners, share expertise, and mitigate the reputational risks they face

1. Data from <https://www.gov.uk/government/statistics/children-looked-after-in-england-including-adoption> and <http://www.socialfinance.org.uk/impact/young-people/>

2. <http://www.londoncouncils.gov.uk/londonfacts/default.htm?category=2#ref27>

3. Data from file://homedata/home\$/echristie/Downloads/Variationsinplaceofdeath_FINAL_forlaunchAugust2010_1.pdf and <https://www.mariecurie.org.uk/commissioning-our-services/why-marie-curie/impact>

in doing so.

2. Re-evaluate procurement policy: The Mayor should ensure that a commitment to encouraging social enterprises is included within the GLA Group procurement policy and re-evaluate the suitability of the current models of social procurement.

3. Investigate the potential for Local Impact Funds: Local public bodies should be encouraged to consider the potential for Local Impact Funds and involve the local community in the social investment process. The London Enterprise Panel could play a key role in coordinating such initiatives.

To encourage new types of investor:

4. Commit pension funds: The London Pensions Fund Authority should adopt a French-style '90/10' rule for investments, such that ten per cent of a fund must be directed towards social enterprises. The two per cent increase that this would entail should be targeted specifically at London's social enterprises as this would help generate £1bn GVA and nearly 60,000 jobs.

To ensure social enterprises are investment ready:

5. Develop a social investment plan: The Mayor should develop a long term plan for expanding London's social investment market which should be published and become a key Mayoral Plan going forward.

6. Create an online social investment platform: An easily accessible online portal should be created to partner social enterprises with financial institutions. Investors and intermediary organisations should be able to freely advertise relevant opportunities and events on the new portal. The portal should also provide social enterprises with a mechanism through which to bring ideas forward to the GLA Group, promoting a bottom-up, civil society-centred approach to meeting London's social challenges.

7. Develop a comprehensive bank of case studies: This online portal should also be used to encourage peer-to-peer learning, both between social enterprises in London and other UK cities. This could also be used to stimulate collaborations between organisations with similar social missions.

Fig. 1: Social Impact Bonds (SIBs)

SIBs are a financial tool designed around bringing a commissioner, an investor, and a delivery organisation (social enterprise) together and reform the delivery of public services to favour a market-based approach (Fig. 3 demonstrates this diagrammatically). As the delivery agency uses a sum of money, fronted by an investor, to achieve a predefined set of outcomes. As these outcomes are met, the commissioner (usually a public body), will pay the investor a return. A project will only be commissioned if the delivery agency will be able to achieve the social goal for a lesser cost than the commissioner acting alone.

SIBs improve the social outcomes of publically funded services by making funding conditional on achieving results. Investors pay for the project at the start, and then receive payments based on the results achieved by the project. Rather than focussing on inputs and outputs, SIBs are based on achieving social 'outcomes' that are predefined and measurable.

Because payment is based on results rather than process, there is more room for innovation and greater freedom to demonstrate that solutions work. The result is better outcomes for the public and reduced costs to the government.

<https://www.gov.uk/social-impact-bonds>

INTRODUCTION

London is often lauded as one of the world's most desirable cities in which to live and work, but like any major city London faces significant challenges. London's population is rapidly expanding; there are perceptions that a growing number of young people are suffering from social exclusion, that the aging population is increasingly struggling with mobility, and that families on lower incomes are facing a life of poverty. Public services are already operating at near-full capacity and while government will always play a vital role in alleviating many of these social pressures, budgets are limited; Londoners are increasingly taking up the mantle for themselves by tackling these problems head-on through social enterprise. There are over 180,000 small and medium-sized enterprises (SMEs) with social and/or environmental aims in the UK, 15 per cent of which operate in London⁴. As well as the myriad social benefits associated with social enterprises, their economic value has been measured at approximately £55bn, and they provide two million jobs nationwide⁵.

Social enterprises can only provide their vital economic and social contribution if sufficient finance is secured. Social enterprises need finance to scale up, to diversify, and to pilot new goods and services. Some of this finance is derived from grants or philanthropic donations, but social enterprises are increasingly seeking alternative funding methods such as through social investment. Social investment refers most generally to the provision and use of capital with the aim of generating both social and financial returns, and can include loans, equity, bonds, as well as other financial instruments⁶. In 2011, the UK social investment market was valued at just under £200m but with growth predicted to expand the market to £750m by the end of the year, it is a market with huge potential⁷; this is shown by the rapid expansion of similar markets elsewhere such as the US community (social) investment market, which grew 540 per cent between 2001 and 2011 from \$4 billion to \$25.8 billion in assets⁸. If London's social investment market continues on its current trajectory, even without assistance it could be worth over £28bn by the end of 2030⁹. Predictions of the current shortfall in UK social investment vary from £300m to as much as £1bn a year, in excess of the £750m expected supply; 19 per cent of this exists in London¹⁰. If the social investment demand surplus could be met through the recommendations outlined in this report, there is the potential for regional GVA in excess of £3.6bn, and the safeguarding or creation of almost 200,000 full time equivalent (FTE) jobs over a three year investment period.

The social investment market has received considerable Government backing over recent years, such as through the formation of Big Society Capital – the world's first wholesale social investment bank – but despite this, and even with the UK's strong position as a world financial capital, London has yet to truly make a name for itself as the global centre for social investment, with many of its social enterprises struggling to raise sufficient finance to establish themselves as competitive businesses. Social investors and financial intermediaries have experienced obstacles, largely stemming from a lack of market awareness or investment readiness (which must include impact readiness¹¹) among many of the Capital's fledgling social enterprises. Investors have also voiced concerns about a lack of market coordination or peer support, and would-be commissioners cite time and monetary cost implications, along with reputational risk of failed projects, as barriers to greater market engagement.

4. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/205291/Social_Enterprises_Market_Trends_-_report_v1.pdf

5. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/353044/CO_Social_investment_background_one-pager_July_2014.pdf

6. <http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 4.

7. <http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 5.

8. <http://skollworldforum.org/2011/02/07/size-of-the-social-capital-market/>

9. The UK market could be worth £148bn.

10. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 6.

11. http://www.bigsocietycapital.com/sites/default/files/pdf/Building%20the%20Capacity%20for%20Impact_September%202014_Final.pdf

LONDON'S SOCIAL INVESTMENT MARKET

Social enterprises – businesses with an environmental or social mission – contribute over £55bn to the UK economy and provide employment for more than two million people¹². The London Plan estimates that in 2011 there were over 3,400 social enterprises operating in the Greater London area, contributing £8.25bn GVA and providing 104,500 jobs¹³.

There are a number of different bodies providing support for the country's growing number of social enterprises. Nationally, support for social enterprises is coordinated through Social Enterprise UK. Social Enterprise UK is a membership body which acts as the voice for social enterprise, undertakes research, provides information and tools, shares knowledge, builds networks, raises awareness, and campaigns to create a business environment where social enterprises can thrive¹⁴. In 1998, Social Enterprise London (SEL) was established as the strategic agency for the development of social enterprise in London. As the first social enterprise agency in the UK, SEL worked with individuals, enterprises, organisations, government, and other statutory bodies to provide enterprising solutions to social and environmental challenges as well as created new ways of doing business¹⁵.

Although well supported by various agencies, social enterprises still face multiple and varied challenges in their successful operation, including financing growth, competing for public sector contracts, and combating a general lack of awareness of their missions. While much funding is achieved through grant applications and philanthropic donations, social investment is fast emerging as the financial tool of choice for social enterprise, and is a growing market in its own right.

Social investment refers to the provision and use of repayable finance to generate both social and financial returns¹⁶. Social investment can occur in a variety of forms including loans, equity, and bonds. The benefits of social investment accrue from the dual returns generated from the combination of improved outcomes for society, and profit for investors. The social investment market helps social enterprises raise capital that they might find it difficult to secure from traditional investment sources, enabling them to scale up, to diversify or pilot new goods and services, or acquire assets. The social investment market is currently valued in excess of £200m a year¹⁷ but is estimated to increase to £750m by the end of 2015¹⁸.

The benefits of social investment come not only from enabling social enterprises to fulfil their mission; it is also predicted that at a regional level, a three year social investment of £10,000 generates six additional FTE jobs and over £110,000 GVA¹⁹. High net worth individuals, charitable trusts, social and ethical banks, public bodies, development finance institutions, and certain financial institutions such as pension funds or investment houses, have all engaged in social investment to date²⁰. City of London Corporation data shows that 89 per cent of current social investors anticipate increasing their social investments over the next two to three years, with just under half of all social investors being located in London or the South East²¹.

There is strong government backing for supporting social enterprises and growing the social

12. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/353044/CO_Social_investment_background_one-pager_July_2014.pdf

13. <https://www.london.gov.uk/priorities/planning/london-plan>

14. http://www.socialenterprise.org.uk/about/about-social-enterprise/FAQs#what_is_seuk

15. http://en.wikipedia.org/wiki/Social_Enterprise_London

16. <http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 4.

17. <http://www.socialenterprise.org.uk/policy-campaigns/policy/social-investment>

18. <http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 5.

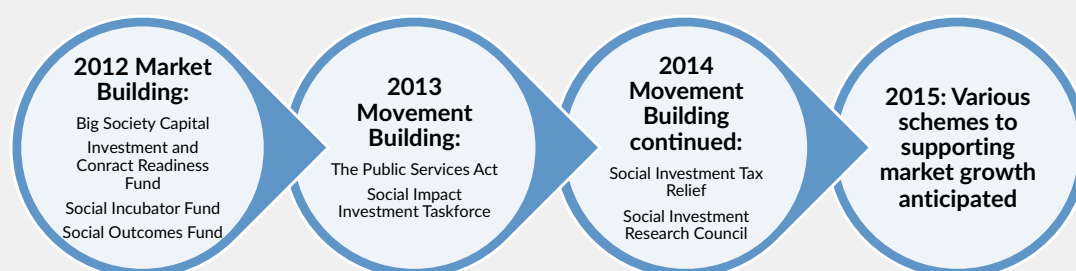
19. <http://www.cityoflondon.gov.uk/business/economic-research-and-information/research-publications/Documents/research-2013/Growing-social-investment-market.pdf>

20. <http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 6.

21. <http://www.cityoflondon.gov.uk/business/economic-research-and-information/research-publications/Documents/research-2013/Growing-social-investment-market.pdf>, p. iii.

investment market. In 2011, 'Growing the Social Investment Market: a Vision and Strategy' set out the Government's ambition to support the social investment market, highlighting the need for an increased supply of lenders, demand for social ventures, and more infrastructure to create an enabling environment²². Since this time the Cabinet Office has supported a number of initiatives, as shown in Fig. 2. These programmes have all contributed to recognition of the UK as a global market leader in social product design. SIBs, first trialled in Peterborough²³ (see Fig. 3), are now being adopted internationally; the Social Stock Exchange was opened in 2013²⁴; Big Society Capital is a unique institution and a world first; charity retail bonds have been raising interest nationally and abroad²⁵; and it was under the UK's premiership that social investment was added to the G8 agenda.

Fig. 2: Social Investment Initiative Timeline



Big Society Capital (2012): The world's first wholesale social investment bank; initially capitalised with £600m to grow the social intermediary market. Big Society Capital ensures that charities and social enterprises can find appropriate and affordable repayable finance to meet their capital needs.

Investment and Contract Readiness Fund (2012): A £10m fund to provide capacity building support to established social ventures. Grants were awarded to social ventures with high growth potential that could deliver a positive social impact.

Social Incubator Fund (2012): A £10m fund to support social incubators providing support to early stage ventures.

Social Outcomes Fund (2012): A £20m fund to support Social Impact Bonds that deal with complex social issues where no single commissioner can justify making all of the payments.

The Public Services (Social Value) Act (2012/2013): Aimed at promoting diverse supply chains, the Social Value Act requires public sector commissioners to think about the social value of their procurements.

Social Impact Investment Taskforce (2013): Established during the UK presidency of the G8 to bring together government officials and senior figures from the worlds of finance, business, and philanthropy to stimulate the development of an effective social impact investment market.

Social Investment Research Council (2013): A coordinated initiative which draws together research commissioners from key organisations in the social investment market from public, private, and social sectors.

Social Investment Tax Relief (2014): Announced at Budget 2014 to unlock retail investment and improve incentives for social investors. Individuals making and eligible investment can now deduct 30 per cent of the cost of their investment from their income tax liability.

22. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/321483/2014_Social_Investment_Strategy.pdf

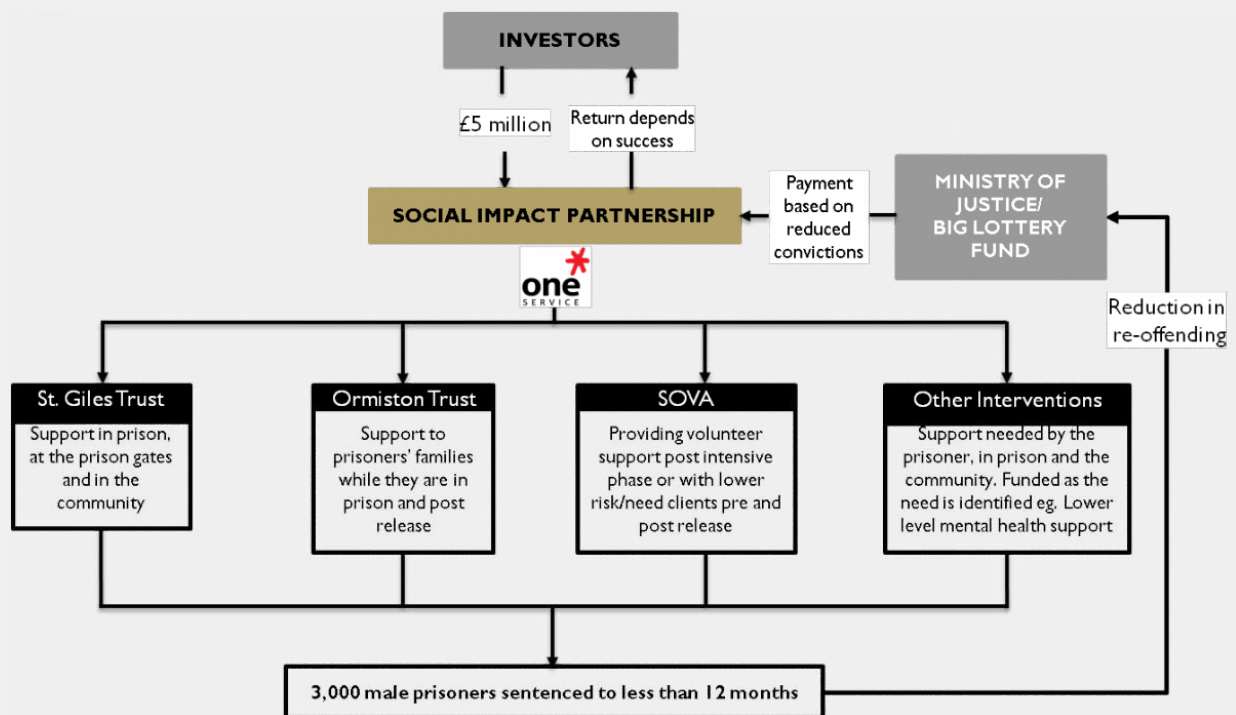
23. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/341684/peterborough-social-impact-bond-report.pdf

24. <http://socialstockexchange.com/>

25. <http://www.bigsocietycapital.com/>

Fig. 3: Peterborough Social Impact Bond

- Peterborough SIB was designed to address the challenge of preventing short sentenced prisoners from reoffending after their release.
- A consortium of six organisations came together to offer a tailored service focussing on the immediate needs of released prisoners.
- The £5m trial programme supported 3000 male prisoners to help them move away from a life of crime.
- Reconvictions fell by over eight per cent and should the project have reached completion, investors would have made a return of between 7.5 and 13 per cent by 2016.



Source: From a presentation by David Hutchison, CEO of Social Finance, 2012, republished on http://data.gov.uk/sib_knowledge_box/ministry-justice-offenders-released-peterborough-prison
<http://www.socialfinance.org.uk/one-service-delivers-results-for-peterborough-prisoners/>
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/325738/peterborough-phase-2-pilot-report.pdf

The Mayor of London has also shown considerable backing for social investment, commissioning a SIB to reduce the number of people sleeping rough on London's streets²⁶. As the first SIB to appear in London, the Greater London Authority's (GLA) London Homelessness Social Impact Bond (LHSIB) was launched in November 2012, and designed to bring new finance to aid a cohort of rough sleepers not targeted by existing social interventions. The LHSIB targeted 831 entrenched rough sleepers by providing a personalised and flexible approach to help them reconnect with society, finding them stable accommodation and employment, improve their general health, and providing repatriation support if necessary²⁷. The first interim report was published in September 2014 with largely positive results, both providers performing particularly strongly against the entering stable accommodation outcome²⁸. The Department for Communities and Local Government (DCLG) was also able to make a number of recommendations that should further improve performance for the second phase of delivery.

Following in the Mayor's footsteps, a number of other SIBs have been trialled in the London

26. <https://www.london.gov.uk/priorities/housing-land/tackling-homelessness-overcrowding/rough-sleeping/social-impact-bond-for-rough-sleepers>

27. https://www.london.gov.uk/sites/default/files/Qualitative_Evaluation_of_the_London_Homelessness_SIB.pdf, p. v.

28. https://www.london.gov.uk/sites/default/files/Qualitative_Evaluation_of_the_London_Homelessness_SIB.pdf

area including Tri-borough Children's Services²⁹ and Westminster Family Recovery Programme³⁰. Intermediary organisations such as Social Finance - a non-profit seeking to bring government, social investors, and social enterprises together to tackle social issues in the UK - report continual rises in the number of approaches they receive from social enterprises and would-be commissioners seeking to investigate whether social investment is right for them³¹. City of London Corporation has long since been an active player in London's social investment market, producing regular research and most recently launching The City of London Corporation Social Investment Fund - a £20m fund offering loan finance, quasi-equity and equity, that provides development and risk capital to organisations working towards charitable ends or with a social purpose, and helps develop the social investment market³².

With an ever growing number of players, and an increased awareness among social enterprises, London's social investment market cannot help but expand. There are a number of organisations, including Big Society Capital, Big Lottery Fund, Social Finance, SEL, and City of London Corporation, which are all seeking to support social enterprises by growing the social investment market, and progress is being made. These organisations have dramatically improved the spread and availability of knowledge and have provided practical assistance to those seeking to enter the market. However, there are some problems in the market that, with their limited resources and lack of remit, they are powerless to resolve: the ready availability of social investment finance remains limited; the private sector has yet to fully engage and understand social investment as a desirable element of their portfolios; there is still a lack of awareness of opportunities among London's social enterprises; social enterprises struggle to share their learnings and improve market understanding; and there is a perceived reputational risk among would-be commissioners should their social investment not deliver the expected returns. The Mayor has engaged as a willing participant in the social investment market but clear leadership has yet to materialise. If London's social investment market is to grow to its full capacity, the full support of City Hall will be needed to break down the market barriers that exist for London's social enterprise, investors, and public bodies.

SUPPORTING THE MARKET

There is significant national support for expanding the social investment market, but London's market currently lacks coordination, which leaves many social enterprises without sufficient levels of finance. This is hindering a market with massive potential for growth and job creation. The current shortfall in UK social investment is measured at between £300m and £1bn a year, 19 per cent of which is in London³³. If the demand for social investment could be met, London's social investment market could add £28bn GVA and support an additional 1.5m jobs by 2030. The failures that have resulted in this social investment gap are not inherent. Central and local government, as well as investors and investees themselves, must all act in unison to close the gap and grow the market. London is a unique global city, and is well placed to act as a world leader in demonstrating best practice for the provision of social investment.

SUPPORTING PUBLIC BODIES AND LOCAL COMMUNITIES AS POTENTIAL COMMISSIONERS

Public bodies are useful organisations through which social enterprises can receive direct support. The Boston Consulting Group and The Young Foundation's 2011 survey highlighted that many future opportunities for social investment will be based on outcomes-based contracts issued by

29. <http://www.eif.org.uk/wp-content/uploads/2014/03/Social-Investment-Triborough.pdf>

30. <https://www.westminster.gov.uk/frp-family-recovery-programme>

31. <http://www.socialfinance.org.uk/>

32. <http://www.citybridgetrust.org.uk/CBT/KnowledgeSharing/Social-Investment.htm>

33. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 6.

the public sector³⁴.

In London, boroughs, the NHS, the police, and others, are all granted government funds to enable them to fulfil their respective tasks and achieve the most desirable social outcomes. While each of London's public bodies has a distinct role, in many cases their fields of desired influence can overlap, with social problems generating costs to more than one player. Where public bodies have sought to influence social problems through social investment, they have often encountered difficulties thrown up by the cross-relevance of these problems to other public bodies; substance abuse provides an excellent example of this. Substance abuse has a range of social costs: substance abusers need treatment, which is costly to the health services; substance abuse is often linked to criminal behaviour, which is costly to the police and justice services; and substance abuse can cause problems within families and lead to unemployment, which is costly to social services and boroughs. The Government spends approximately £1.1bn a year on drug treatment, alongside money that goes toward reducing drug-related crime, and providing employment and housing benefits³⁵. The figure can be broken down into 70 per cent costs to the criminal justice system, 20 per cent to drug treatment and ten percent to the benefits system. In cases such as this, social investment is an unviable option as no single public body would be willing to pay out for all the costs of a programme that has such clear cross-organisational benefits.

While allocating cost savings can be a difficult task, it is by no means an impossible one, and one that greater market coordination and strong leadership could drastically help to mitigate. Social Finance predicts that the current cost of a crack/opiate user to the Government is £150,000³⁶. With approximately 62,780 crack/opiate users in London³⁷, if the fiscal beneficiaries of a reduction in the number of substance abusers could be brought together, the estimated savings to the commissioners resulting from reduced pressure on a range of public services can be estimated at as much as £9.4bn over a drug-user's life time³⁸.

In addition to greater coordination, potential commissioners will need practical help to engage in the social investment market. Stakeholders have expressed concern that commissioners do not yet have the skills and capabilities necessary to instigate appropriate deals and contracts with social enterprises³⁹. To an extent, this problem will disappear as commissioners gain experience, but in the meantime, any assistance to public bodies looking to become commissioners, whether it be in coordination, knowledge sharing, risk management, or training provision, can only serve to strengthen the social investment market.

The GLA has made a start, progressing beyond its own SIB to help entrenched rough sleepers, moving towards developing a London-wide SIB to better meet the needs of adolescents of the edge of care. However, if cross-borough projects such as this are to develop, the Mayor must play a more prominent role. If the GLA could develop a strong precedent for cross-organisational collaboration, there are limitless possibilities for socially orientated project developments. A London-wide effort to reduce the number of adolescents in care would assist over 10,000 vulnerable young people and could generate savings of over £0.4bn each and every year after the project's inception⁴⁰⁴¹. With over-65 being the fastest growing age group in London⁴², care for the elderly will become increasingly important; social initiatives to improve end of life care for cancer patients in London would allow more elderly people to receive treatment at home, while at

34. <http://youngfoundation.org/publications/lighting-the-touchpaper-growing-the-market-for-social-investment-in-england/>, p. 22.

35. http://www.socialfinance.org.uk/wp-content/uploads/2014/05/SF_DRUGS_REPORT.pdf, p. 4.

36. <http://www.local.gov.uk/documents/10180/5920754/Introduction+to+Social+Impact+Bonds+-+Health,%20Social+Care+and+Addiction/293f328a-c5d3-4a59-9ea8-9ad5370fd7e3>

37. <http://www.hscic.gov.uk/catalogue/PUB12994/drug-misu-eng-2013-rep.pdf>, p. 16.

38. A variety of programmes over the UK would target 298,752 users, saving as much as £44.8bn.

39. <http://youngfoundation.org/publications/lighting-the-touchpaper-growing-the-market-for-social-investment-in-england/>, p. 22.

40. The annual cost to Local Authorities of children entering care is approximately £2bn.

41. Data from <https://www.gov.uk/government/statistics/children-looked-after-in-england-including-adoption> and <http://www.socialfinance.org.uk/impact/young-people/>

42. <http://www.londoncouncils.gov.uk/londonfacts/default.htm?category=2#ref27>

the same time producing savings of up to £16.9m per annum⁴³. The Mayor, lacking the budget to front the cost of multiple social initiatives, should use his influence to bring London's various bodies together to become co-commissioners of their own social investment initiatives, provide expertise, and mitigate the reputational risks they face.

Indirectly, public procurement procedures in the UK are often used to encourage social enterprises and other SMEs. The Social Value Act 2012 was designed to open up more opportunities for social enterprises to win bids for the delivery of public services. It requires public bodies to consider the economic, environmental, and social benefits of any services they commission and provides justification for government commissioners to specifically include social impact in their procurement decisions⁴⁵.

The GLA Group responsible procurement policy stipulates that the £8bn a year spend on goods and services in London should be used as a mechanism for promoting wealth creation, social development, and environmental improvements⁴⁶, but makes no specific commitment to supporting social enterprises. Evidence shows that every £1 of public sector expenditure invested in social enterprise creates £6.25-£8.33 GVA compared to £3.57 GVA across all markets⁴⁷. If the GLA Group committed just five per cent of their procurement budget to purchasing from social enterprises, they would generate almost £2bn additional GVA than by purchasing through standard procurement measures.

The UK National Advisory Board to the Social Impact Investment Taskforce (the Advisory Board) has called for the promotion of new culture of government procurement, having observed that current procurement models are not well-designed for programmes that address complex human needs. Their research shows that commissioned services tend to procure for services that follow well established patterns and that don't allow for flexibility or adaptation, which tends to lead to rigid programmes that are unsuitable for social enterprise⁴⁸. The GLA Group procurement policy should be re-evaluated to ensure that the current models of procurement used are the most suitable, and amended to include a stronger commitment to encouraging social enterprises.

Support for the social investment market need not only come from government; local communities have a valuable role to play in helping themselves resolve pressing social issues that affect them. In September 2013, The Social Investment Business Group launched 'Place based social investment: a prospectus for growing the local social economy', which outlines a strategy to bring social investment to the community level⁴⁹. The Social Investment Business Group has worked to develop a new financial product to help bridge the £2bn funding gap between demand and supply: the Local Impact Fund (LIF).

LIFs are designed such that local finance is used to fund local social enterprise, and work on the premise that this investment can only function when accompanied by appropriate investment readiness and business support (two areas in which investors believe social enterprises are chronically failing). There is already evidence of a growing link between Local Enterprise Partnerships (LEP's) and social enterprise. The Black Country LEP, for example, has been working to create a Social Enterprise Zone (SEZ) to provide a platform for local social enterprises to flourish, supporting economic growth and creating jobs in their local area⁵⁰.

43. Data from <http://www.endoflifecare-intelligence.org.uk/view?rid=71> and <https://www.mariecurie.org.uk/commissioning-our-services/why-marie-curie/impact>

44. In England, this figure would be approximately £158m per annum.

45. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 23.

46. <https://www.london.gov.uk/sites/default/files/Responsible%20Procurement%2011%20RP%20Policy.pdf>

47. <http://www.sibgroup.org.uk/lif/prospectus/>, p. 11.

48. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p.30.

49. <http://www.sibgroup.org.uk/lif/prospectus/>

50. Ibid.

The Social Investment Business Group has called for action to integrate the proposed LIFs with existing SEZ's as well as other local representative bodies. There is an expectation that the project could attract significant EU funding⁵¹ as well as investment from a variety of national and local stakeholders⁵². As the project establishes a track record for success, investing options could be opened up to pension funds and local individuals through crowdfunding platforms. London, as the site of the first SEZ in the UK, and with its many different local bodies, has much to gain by better enabling Londoners to improve their local areas through supporting the future use of community-based initiatives like LIFs.

SUPPORTING SOCIAL ENTERPRISES BY ENCOURAGING NEW TYPES OF INVESTOR

Financial investors and intermediaries have traditionally been seen as the driving force behind the growth in the social investment market. The Government has built institutions to fill the role of financial intermediary and provide sufficient market capital but their resources are limited. If the social investment market is to continue to expand beyond a level which government can support, the private sector will need to be brought on board to provide the additional finance and close the funding gap.

There is a clear role for the private sector as a social investor, but the social investment market is immature, which makes the task of calculating risk, and therefore market returns, all the more challenging; private investors have thus far played a limited role in the social investment market. In order to encourage investment, potential investors need to be fully aware of the risk and return associated with the product. Social investments are increasingly being designed with social investors in mind. SIBs, which make up a large proportion of all social investments, were designed to include a distinct role for private investors as the providers of upfront capital for socially motivated projects.

At present, social enterprise and government have played a dual role in funding SIBs, filling the role of the private investor in order to demonstrate the value of this new investment model. As current projects start producing returns, the data must be made readily available and advertised within the private sector in order to facilitate better understanding, reduce uncertainty, and aid the design of more attractive social investments to tempt more private social investors into the market⁵³. This would assist the social investment market dramatically, rebalancing risk from social enterprises and public bodies toward the private sector, who in turn should be financially compensated.

Most social impact bonds are still in the early stages but returns for investors are predicted from the current programmes. Essex County Council SIB required a minimum commitment of £100,000 to be paid over three years and is currently predicting a likely return of up to and above ten per cent per annum (p.a.)⁵⁴ and the Golden Lane Housing charity bond, which required a minimum commitment of £2,000 over three years, offered a likely return profile of four per cent p.a.⁵⁵. Since the end of the Peterborough trial SIB, designers of social investment models have sought to reduce the time in which an investor can expect to receive a pay-out to 12-18 months. This change by financial intermediaries is expected to significantly increase the appeal of social investing.

Central government too, is increasingly seeking to encourage private investors to engage in the

51. The European Union is looking to include social investment in its Europe 2020 job creation agenda (<http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 6)

52. Ibid.

53. <http://youngfoundation.org/publications/lighting-the-touchpaper-growing-the-market-for-social-investment-in-england/>, p. 20.

54. http://www.bigsocietycapital.com/sites/default/files/pdf/Social%20Investment%20Market%20Compendium%20Oct%202013%20small_0.pdf, p. 8

55. Ibid.

market, and reduce the dominance of government funds and charitable trusts. Social Investment Tax Relief (SITR) was introduced on any investment made after April 2014, offering 30 per cent income tax relief to individual investors making social investments⁵⁶. SITR has the potential to prompt up to £480m of new capital to small scale social organisations by providing a financial incentive for individual investors to supply social investment capital⁵⁷. It is therefore vital that schemes such as this are well advertised by all agencies operating in the social investment sector.

The Cabinet Office envisages the development of retail products such as Social ISAs, and social pension plans over time and as a track record and consumer confidence is established⁵⁸. The first steps have been taken to open the social investment up to pension funds as another investment source but mainstream pensions options will need to be made available if this is to truly take off⁵⁹. In September 2014 the Advisory Board called for legislation requiring all pension funds to offer a social investment pension option⁶⁰. Legislating for just one per cent of UK pension fund assets to be allocated to social investment would give the market a £23.9bn boost⁶¹. This is equivalent to over 14.3m FTE jobs and £262.9bn GVA.

The French '90/10 rule' legislates that savers must be offered the choice of a fund in which ten per cent of their money is invested in environmentally and social responsible companies, and used to finance social enterprises, co-operatives, and housing associations⁶². Research shows no evidence that these funds do not perform at least as well as 'just-for-profit' funds⁶³. By adopting French-style pension regulations, the UK could give a significant boost to social enterprises. Local Government Pension Schemes (LGPSs) are the obvious funds to lead a shift towards a similar system in the UK. The London Pensions Fund Authority (LPFA) lists producing 'an overall positive impact on stakeholders and society' as one of its five strategic objectives⁶⁴. From an investment perspective, this means developing investment strategies that take account of environmental, social, and corporate governance (ESG) issues. LPFA already incorporate ESG into their investments, to the sum of around eight per cent of their assets⁶⁵. A two per cent increase, to match French pension fund investments, could give a huge boost to the local economy if targeted at London's social enterprises. LGPSs nationally could give similar boosts to their local economies. By committing just one additional per cent of their £4.8bn fund to ESG investments, LPFA, as the UK's largest Local Government Pension Fund (LGPF), could help to generate £528m GVA and nearly 30,000 jobs over a three year investment.

SUPPORTING INVESTORS BY ENSURING SOCIAL ENTERPRISES ARE INVESTMENT READY

Numerous private institutions are looking to enter the social investment market and many of those already operating there are looking to expand their activities. A City of London Corporation survey found that 89 per cent of London's financial institutions operating in the social investment market were looking to increase their future social investments⁶⁶. This, combined with the increased demand for social investment from approximately £200m to £750m over the next

56. <http://www.bigsocietycapital.com/social-investment-tax-relief>

57. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 24.

58. <http://www.cityoflondon.gov.uk/business/supporting-local-communities/Documents/a-brief-handbook-on-social-investment.pdf>, p. 12.

59. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 28.

60. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 33.

61. Ibid.

62. Ibid.

63. Ibid.

64. <http://www.lpfa.org.uk/Admin/Public/Download.aspx?file=Files%2FFiles%2FAnnual+Reports%2F2014%2F140930+Summary+Annual+Report.pdf>

65. <http://www.lpfa.org.uk/How-we-invest/RESPONSIBLE-INVESTMENT.aspx>

66. <http://www.cityoflondon.gov.uk/business/economic-research-and-information/research-publications/Documents/research-2013/Growing-social-investment-market.pdf>, p. iii.

year, should have resulted in rapid market expansion, but instead growth is stalling. Investors are reporting significant challenges to full market engagement, leaving them able to meet just half of demand expressed by social ventures⁶⁷. A survey commissioned by Big Lottery Fund found that investors and financial intermediaries perceive a significant lack of investment readiness among social enterprises, particularly relating to their limited financial skills and understanding of basic business models⁶⁸. Investors also identified wider problems in the market such as a lack of general understanding of the concept of social investment, as well as an absence of filtering systems to prevent organisations approaching investors too early⁶⁹. These findings were echoed by The Boston Consulting Group and The Young Foundation who reported that half of their survey respondents identified 'lack of attractive ventures to invest in' as their biggest barrier to growth, blaming a lack of business understanding and poor financial skills within the sector⁷⁰.

The Advisory Board has stressed the importance of improving the capacity of social organisations to appropriately use investment to scale their impact⁷¹. Investors and intermediaries alike have called for this to be facilitated through better market coordination that includes clear signposting to appropriate finance sources for organisations seeking social finance, as well as increased opportunities for peer support⁷². They further suggested that improved generic information and early stage diagnostic tools should be made readily available to social enterprises to help them avoid devoting their limited capital to expensive bespoke support in engaging in a process that is ultimately not right for them⁷³.

The Mayor, through the GLA Group, plays a coordinating role in London, managing the cross-borough implementation of transport policy, policing, and fire services, etc. The Mayor is therefore well-placed to play a role in coordinating London's social investment market. A long term plan needs to be developed for expanding London's social investment market and supporting social enterprise, helping them to become investment ready. This would be most easily achieved through the creation of an online portal. Such a portal should provide social enterprises with authoritative, sector relevant, information about social investment generally, give clear signposting to appropriate financial sources, and advertise relevant opportunities and events in London. There are existing external resources which such a platform could direct enterprises to. An online platform could additionally be used to provide information about other social investment endeavours, both between social enterprises in London and other UK cities, as well as foreign counterparts. This could also be used to stimulate collaborations between organisations with similar social missions.

67. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/210408/Social-Investment-Report1.pdf, p. 5.

68. <http://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&frm=1&source=web&cd=2&ved=0CCwQFjAB&url=http%3A%2F%2Fbiglotteryfund.org.uk%2Fglobal-content%2Fresearch%2Fuk-wide%2Fgrowing-the-social-investment-market-investment-readness-in-the-uk&ei=s9jAVOe9IlzmaqLhgZgO&usg=AFQjCNFUTAa10YxEUvN3WHJGU1H-jZDfw&bvm=bv.83829542,d.d2s>, p. 4.

69. Ibid.

70. <http://youngfoundation.org/publications/lighting-the-touchpaper-growing-the-market-for-social-investment-in-england/>, p. 18.

71. <http://www.socialimpactinvestment.org/reports/UK%20Advisory%20Board%20to%20the%20Social%20Investment%20Taskforce%20Report%20September%202014.pdf>, p. 28.

72. <http://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&frm=1&source=web&cd=2&ved=0CCwQFjAB&url=http%3A%2F%2Fbiglotteryfund.org.uk%2Fglobal-content%2Fresearch%2Fuk-wide%2Fgrowing-the-social-investment-market-investment-readness-in-the-uk&ei=s9jAVOe9IlzmaqLhgZgO&usg=AFQjCNFUTAa10YxEUvN3WHJGU1H-jZDfw&bvm=bv.83829542,d.d2s>, p. 4.

73. Ibid.

“It was not until we looked to expand a project using social investment that we, at Addaction, really understood what was involved in the process.

“At the time, we were looking to expand a family services project to support parents with substance abuse problems. The project offers individually designed ‘care packages’, taking into account the needs of the whole family and had proved very successful in the sites it was already established in.

“After much research, we found that the way in which we deliver services to people with complex needs was extremely difficult to fit into a social investment model. In order to even become eligible, a great deal of work was needed to understand how we would have to adapt our service delivery model and what additional resources would be required (for example, more extensive data analysis).

“Although social finance proved unsuitable for that particular project, Addaction now feels confident of its investment readiness for the future. If we were to start a new project, we would strongly consider social finance as an option.

“While we successfully made the necessary changes, many other small social enterprises that could benefit from social investment will not be able to do as Addaction did.

“Mayoral support for social investment in London’s voluntary sector will be necessary if that market is to grow.”

Charlotte Simpson, Social Investment Project Manager, Addaction

“As a financial intermediary operating in the social finance sector, we have found some lack of awareness within the voluntary sector of how well-developed and active the investment market is, such that some good ideas may not yet have been brought forward.

“The Mayor should take a lead and encourage London’s social enterprises to bring innovation forward and encourage commissioners to engage with the innovators proactively.

“Any well-structured initiative that improves the impact readiness of social enterprises would be strongly welcomed by London’s financial sector.”

Jim Clifford OBE and Chris Theobald, BWB LLP

CONCLUSION

Social enterprises provide vital support to Londoners, working in some of the Capital's most deprived communities. In order to expand their operations, social enterprises need sufficient funding which they are increasingly seeking through social investment. Increasing the social investment market would not only generate significant social gains, but economic gains too, in the form of additional GVA and job creation. The Mayor has engaged as a willing participant in the social investment market but clear leadership has yet to materialise and demand for social investment is going unmet. If London's social investment market is to grow to its full capacity, the full support of City Hall will be needed to break down market barriers that exist for London's social enterprise, investors, and public bodies.

This report therefore makes the following recommendations to support social enterprises and grow the social investment market:

To support potential commissioners:

- 1. Coordinate London's governing bodies:** The Mayor should use his influence to bring London's governing bodies (boroughs, London Councils, NHS, police, etc.) together to become social finance co-commissioners, share expertise, and mitigate the reputational risks they face in doing so.
- 2. Re-evaluate procurement policy:** The Mayor should ensure that a commitment to encouraging social enterprises is included within the GLA Group procurement policy and re-evaluate the suitability of the current models of social procurement.
- 3. Investigate the potential for Local Impact Funds:** Local public bodies should be encouraged to consider the potential for Local Impact Funds and involve the local community in the social investment process. The London Enterprise Panel could play a key role in coordinating such initiatives.

To encourage new types of investor:

- 4. Commit pension funds:** The London Pensions Fund Authority should adopt a French-style '90/10' rule for investments, such that ten per cent of a fund must be directed towards social enterprises. The two per cent increase that this would entail should be targeted specifically at London's social enterprises as this would help generate £1bn GVA and nearly 60,000 jobs.

To ensure social enterprises are investment ready:

- 5. Develop a social investment plan:** The Mayor should develop a long term plan for expanding London's social investment market which should be published and become a key Mayoral Plan going forward.
- 6. Create an online social investment platform:** An easily accessible online portal should be created to partner social enterprises with financial institutions. Investors and intermediary organisations should be able to freely advertise relevant opportunities and events on the new portal. The portal should also provide social enterprises with a mechanism through which to bring ideas forward to the GLA Group, promoting a bottom-up, civil society-centred approach to meeting London's social challenges.
- 7. Develop a comprehensive bank of case studies:** This online portal should also be used to encourage peer-to-peer learning, both between social enterprises in London and other UK cities. This could also be used to stimulate collaborations between organisations with similar social missions.

“London is in a strong position to develop its own thriving social investment market. It has the opportunity to learn from other developments across the UK, like the Local Impact Funds, to drive a market based on local needs. It can coordinate across many boroughs and services helping target the most complex social problems and align them to social value. It has unique established corporate and financial relationships and can deploy its pension for good. This strategy for London’s social investment market is therefore very welcome. With the Mayor’s strong and public lead, the power of social investment can be harnessed to make a better London for everyone.”

Simon Rowell, Big Society Capital



FEEDBACK

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