power to change | business in community hands

Power to Change and blended finance

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September 2021

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1. Introduction: setting the scene

Experimentation, or ‘flying lots of kites’, has been a central part of Power to Change’s approach to learning how best to support community businesses (Dobson et al. 2020). In addition to its main grant funding programme, it has also invested its funds within several social investment schemes, exploring the potential of subsidised, repayable finance to help achieve its aims. This report explores two of those schemes, provided in partnership with Social and Sustainable Capital (SASC) and Key Fund, to deliver blended finance to community businesses. It provides an overview of blended finance and the social investment market, drawing on existing published material, before providing an account of the two schemes developed by Power to Change and its partners, drawing on interviews with representatives from each organisation. It also offers some key learning points and reflections on the potential future direction of blended finance in the field of community businesses.

2. The social investment market

The definition of social investment has been much discussed (Bruyn, 1987; Owen, 1990; Caroe, 2015). In general terms social investment aims to achieve a sustainable financial return, as well as social impact, mirroring the so-called 'double bottom line' ascribed to social enterprises (SEUK, 2020; Leslie et al. 2020). Social investment is also considered to be delivered primarily to 'social sector organisations', defined by the Dormant Accounts Act as organisations that exist "wholly or mainly to provide benefits for society or the environment" (Leslie et al. 2020, p.4). According to the definition provided by Power to Change, community businesses are organisations set up to be accountable to their community and use the profits they generate to deliver positive local impact (Power to Change website). As such, community businesses can be seen as a subsector of social enterprises, and hence part of this wider 'social sector' (Teasdale, 2010).

Similarly, this report is primarily concerned with formal lending from social lenders, often referred to as Social Investment Finance Intermediaries (SIFI). It is worth noting, however, that many charities receive a range of mainstream finance from banks as well as more innovative forms of social investment in the form of community shares or crowd funding (Floyd and Gregory, 2017). Not all lending to Community Businesses, therefore, will be 'social investment'. Their common focus on disadvantaged people and areas, however, will often mean that they lack the financial means to access mainstream credit markets at standard interest rates, or that they find they are rejected from mainstream banks entirely. This means they may require the more favourable terms sometimes offered by social lenders.

The Good Finance website[1], set up to improve the level of information available on social investment, suggests that some of its advantages include being able to spread expenditure over a longer term, with a predictable time frame, and have greater flexibility to use the funding for internal investment and growth. Grants, in contrast, can be short term, have multiple strings attached, and prioritise the goals of funders over recipients, preventing long term planning or internal investment. Although early discussions around social finance were arguably subject to a degree of hype, it is recognised that it is no panacea, and only makes sense for some organisations some of the time (Elsworth, 2020). First and foremost, social investment only makes sense if there is an income stream that the investment will help to grow, and which will fund the loan repayments.

1 https://www.goodfinance.org.uk/

The size of the social investment market in England overall has been estimated as increasing from £165 million in annual transactions in 2010/11, to £1.1bn by the end of 2018 (Leslie et al., 2020). One of the major drivers of this growth has been the establishment of Big Society Capital to act as an investment wholesaler in 2012 (Elsworth, 2020). Big Society Capital has funded numerous SIFIs to supply finance and investment readiness programmes to social organisations. It was relatively successful at increasing the overall supply of capital, however, there was concern that investment finance was generally at too large a scale and unaffordable for smaller organisations, which includes most charities and social enterprises (Mackey, 2012).

£165m → £1.1bn

The size of the social investment market in England overall has been estimated as increasing from £165 million in annual transactions in 2010/11, to £1.1bn by the end of 2018 (Leslie et al., 2020).

One explanation for social investment failing to spread to the wider social sector, particularly smaller organisations, was that the organisations themselves lacked ‘investment readiness’. In response to a 2012 Big Lottery survey, investors reported a lack of suitable financial skills among potential investees as a major barrier (Mackey, 2012). Investors also reported the difficulties involved in appropriately pricing the risk involved in small investments and the transaction costs involved in agreeing bespoke terms, often with few existing templates or examples to draw on. Other stakeholders, some of whom provided support services to help match investors with investees, argued for a change in mind-set away from a “traditional charitable model to a business model” (p4).

One of the interviewees for this report, however, rejected in strong terms the narrative that social sector organisations’ financial capabilities were to blame for any lack of uptake of social finance. They argued that social sector organisations were no less financially literate or capable, on average, than their private sector counterparts, whilst often operating in tougher funding and policy conditions. Whilst there would always be exceptions, they suggested that if well run social organisations were provided with the right support and guidance, the capabilities of most social organisations need not itself be a major barrier.

> **“ Social investment loves to blame the charities for their lack of success. Like Coca Cola blaming customers for not liking its drinks. Bonkers in my view… The responsibility is on us, to make it digestible and understandable. If we’re trying to get people to use finance and they’re not taking it, chances are it’s because it’s not structured right.**

This view reflects that of the investees and potential investees surveyed in the 2012 Lottery research. These respondents were much more likely to suggest that the type of finance on offer, or a lack of reliable revenues to repay the loan, was the most significant barrier. In contrast to the finance that some organisations had actually received, those interested in future investments appeared most interested in loans less than £100,000, with a grant element, and without asset-based security requirements (Mackey, 2012). Significant numbers also appeared to be ‘self-selecting’ out of the process of applying for loans, rather than being rejected. Only around half recognised a skills gap within their organisation as a major barrier and those that did were more likely to identify bespoke business and financial planning support as more important than ‘investment readiness’ courses. Even after the establishment of Big Society Capital, there remained ongoing concerns that the social finance on offer was too centred on large deals and investors’ needs, rather than those of the social organisations themselves (Leslie et al. 2020).

2.1 Blended finance

One of the solutions put forward to broaden the appeal of social investment and grow the market is the idea of ‘blended finance’ (Leslie et al. 2020). Blended finance, in its simplest conception, combines both repayable and non-repayable forms of funding. This ‘blending’ can occur at different levels: the fund level, the deal level, or unstructured within a front-line organisation. The overall idea is that the grant funding (the non-repayable subsidy), or equivalent subsidy such as guarantees, makes the loan element (the repayable capital) less risky and more palatable for either the investor and/or the investee (it also reduces the overall risk to the lender and recipient organisation). Previous examples of blending at various scales have included the Adventure Capital Fund (£2m), the Arts Impact Fund (£7m) and on a notably larger scale, Futurebuilders (£145m). In another example, Social and Sustainable Capital (SASC) established the £30m Third Sector Loan Fund by blending finance from the Social Investment Business (SIB) Foundation, Big Society Capital and Santander, to offer unsecured lending to organisations without assets to secure a loan against (Elsworth, 2016). Key Fund also have a long history of using blended deals, stretching back as far as 2002, arguably making them pioneers in the field.

A major milestone in the development of blended finance was the establishment of Access in 2015, with a £60m endowment from the Government, explicitly to help address some of the concerns over the lack of smaller, riskier loans, using various models of blended finance. It established the Growth Fund using £22.5m of Big Lottery Grant funding and £22.5m in loan funding from Big Society Capital, to help increase demand for social investment. It aimed to encourage more risk bearing investments to a wider range of organisations, without necessarily any assets to provide collateral, and of less than £150,000 (Access Foundation, n.d.). As with Big Society Capital, Access does not make investments itself, but provides grant subsidy and subsidised capital to SIFIs, who then set the terms of the investments offered to social organisations.

Subsidising SIFIs' capital funding with grants was intended to counterbalance both the higher relative transaction costs for smaller deals, and to absorb some of the risk associated with making unsecured loans to sub-sectors of organisations without a history of repaying finance (Access Foundation, n.d.). It was hoped that by compensating for this knowledge gap, SIFIs would be able to afford to provide more preferable loan terms, whilst building up a stronger knowledge base for evaluating and pricing future investment decisions.

One of the interviewees for this report, however, was somewhat sceptical of this 'fund level' blending, arguing that it tended to benefit the fund manager more than the investee. They also argued that the amount of subsidy available wasn't necessarily enough to make a major difference to the risk they faced as a lender, as even with the grant component they would still stand to lose a large amount of capital if a loan had to be written off. As such, the interviewee preferred blending at the level of the investment deal itself, in line with the blended finance schemes described in the next section of this report. This means loan finance can be made more appealing to social organisations by advancing a combination of loan and grant directly to the investee. This was the model of many of the investments that occurred under the Futurebuilders programme (Wells et al 2010), and it was also hoped that SIFIs would pass on part of the grant funding received as part of the Growth Fund.

Investees may seek a non-repayable element to the investment because they consider borrowing the entire amount of capital unaffordable, or to cover an anticipated delay until their business model starts to create a surplus and allow repayments. In some respects, this is what many organisations have attempted to achieve on their own through by blending a mix of different funding sources 'in the wild' (Maitland Hudson et al., n.d.). Whilst social organisations may be adept at combining fundraising, this can be time consuming and somewhat risky compared to simply borrowing at a more sustainable level and set of terms to begin with (Access Foundation, n.d.).

Finally, the investee organisation can also be subsidised in other ways less obvious than a direct grant. Softening the terms of an investment can occur before a loan is awarded, for example if the loan is unsecured or offered at below market interest rates. It can also happen after a loan has been drawn down as part of partial write offs, through repayment holidays, or even various forms of business support and advice ('funder plus' support). Collectively these different forms of support may be referred to as 'patient' lending, distinct from the commercial finance market. As an example, Power to Change's 'More than a Pub' programme offered combined loan and grant packages of up to £100,000 to cover capital costs, as well as capacity building support in the form of expert advice and networking, and bursary grants to cover development costs (Power to Change, 2020b). Seb Elsworth (2020), the Chief Executive of Access, suggests that whilst there has been some progress towards increasing the supply of smaller-scale unsecured lending, many organisations would still benefit from more patient and longer-term finance. For most social enterprises, he suggests that this will inevitably require some form of subsidy, as they are unable to raise large amounts on commercial terms as they are risk averse and require longer to repay.

£100,000

Power to Change's 'More than a Pub' programme offered combined loan and grant packages of up to £100,000 to cover capital costs, as well as capacity building support in the form of expert advice and networking, and bursary grants to cover development costs (Power to Change, 2020b).

Dawn Austwick, the former CEO of the National Lottery Community Fund (SASC, 2018) agreed in a contribution to SASC's 2018 impact report that blended finance can work well and create win-win situations, particularly when funding capital costs such as purchasing a new building or expanding service delivery capacity, which can lead to new revenue. She also suggested that relying on 'mission driven' social enterprise as lenders, such as Key Fund and SASC, was an important part of this model to counter fears about the potential 'seepage of funding out of the 'doing good' sector' (p. 14). One of the interviewees for this report acknowledged that this was a concern amongst some grant makers but pointed out that they set interest rates with the sole aim of recovering the capital, and that the grant element was passed in on in full to the charity. This ensures that funds are recycled within the social economy as far as possible. The interviewee also pointed out that subsidising investment activity was normal in mainstream business, such as the guarantees offered by the British Business Bank on loans to small and medium sized businesses.

3. Power to Change's approach to blended finance

Power to Change has developed a range of blended finance support in partnership with SIFIs and other investors, offering finance to organisations meeting their definition of a community business and able to demonstrate both beneficiary and wider community benefit. Maitland Hudson et al. (n.d.) suggested that Power to Change have taken an intentionally experimental approach, focussed on providing grant income at the deal level. Without subsidy, they suggest that community businesses would struggle to attract investment, given that they often operate in challenging business environments, at a small scale, and can take considerable time to start breaking even. This means they may struggle to finance a loan at the point of application, despite having a viable business plan in the longer term. To encourage sustainability, the grant funding was intended to be offered on a one-off basis, providing the minimum amount needed as a last resort where other options such as community shares were not possible (Maitland Hudson et al., n.d.). The remainder of this report provides further detail on the two blended finance schemes conducted with the partner SIFI organisations Key Fund and Social and Sustainable Capital (SASC). Power to Change set up a partnership with Social and Sustainable Capital (SASC) in 2015, which has ultimately provided £3.53 million of loans and £923,000 in grants as part of six bespoke, blended finance deals[2]. The size of these deals fell between £260,000 and £800,000 in terms of the loan element, and between £80,000 and £250,000 in terms of the grant component. Interest rates varied slightly depending on the level of risk, between 6.25 per cent and 8 per cent, and the grant component constituted 16 to 25 per cent of each deal overall.

Power to Change has also supported two waves of investments with the Key Fund. The first included 24 deals agreed between 2015 and 2019, including £1.8 million in lending from Key Fund's existing funds, alongside £1 million in grants provided by Power to Change.

£2.8 million

This makes a total of £2.8 million in funding and all but £100,000 of the deals agreed were ultimately disbursed. The deals ranged in size between £10,000 and £300,000 for the loan component, and £7,500 and £100,000 for the grant element. These loans were smaller than those provided with SASC and were targeted specifically at organisations in the poorest three deciles on the Index of Multiple Deprivation. Most were deals around capital expenditure, such as property.

2 Two further blended deals were also arranged by the partnership, one prior to the scheme being formalised and the other by retrospectively providing a grant to an existing investee, making a combined total of £7.03m in lending and £1.5m of grant for the partnership between 2015 and 2018.

Power to Change has also continued to work with Key Fund on a second wave of investments, with nine agreed to date from February 2019 onwards. For these, Power to Change have provided the capital for both the grant and the loan components, with Key Fund continuing to arrange and distribute the funding. These investments include a further £919,800 in loans and £394,200 in grants, totalling to £1.3 million.

£35,000 → £175,000

They range in size between £35,000 and £175,000 for the loan component and between £50,000 and £250,000 for the grants. At the time of writing £786,000 has been defrayed.

In addition, a further £872,762 has been leveraged from external sources, mainly in the form of additional grants, but also three deals which include overdrafts or mortgages from external lenders and two including community share offerings. In contrast to the first wave of loans, four of these deals were intended to supply working capital.

Key Fund suggested that they were most likely to make a loss on the smallest loans, meaning a smaller number of larger loans were necessary to provide a balance across the portfolio. Regardless of scale of funding, support contributed to non-financial benefits for organisations and their beneficiaries. The grant component also generally constituted a higher proportion of the overall deal compared to the SASC investments, ranging from 25 per cent to 50 per cent, with one exception at 15 per cent.

3.1 Approach to the grant element

For both partnerships, Power to Change aimed to take an experimental approach to the grant element, using it for a variety of purposes. These included providing revenue as part of new business development, making a loan more affordable, financing an asset purchase or transfer, or supporting part of a more complicated, multi-party deal.

The model deployed by SASC explicitly avoided using the grant to de-risk the loan for themselves. Potential investees were required to pass SASC's normal, rigorous due diligence process and engage in detailed discussions around a sustainable business plan. The main barrier to investment was intended to be scenarios in which the capital required, and subsequent repayments, were simply too high for the business plan to service or the community business to afford. So, whilst an £800,000 mortgage might be affordable for the borrower alongside a £200,000 grant funded deposit, a £1 million loan would not.

SASC suggested that their blended investments had worked best when funding the purchase of an asset, which would then lead to a new or expanded income stream. In most cases, this asset was a building or housing, either for social housing, accommodation for vulnerable groups, or as a base from which to offer further services. This provided a relatively clear route to funding repayments, compared to investments in marketing, research, or other activities. The grant element was also able to act as a deposit against the repayable mortgage, which ensured that on successful investments the grant element would be kept in full by the charity, helping to allay any fears of the grant subsidising a private return on investment.

Two of SASC's deals also funded community owned solar farms, which were able to generate a surplus that could then be spent locally to benefit deprived communities. These provided a useful area of overlap between the strategic goals of both Power to Change and SASC. In some cases achieving this overlap had been a challenge, as SASC often delivered investments to professionally managed voluntary organisations operating in deprived areas. These organisations may have less direct community control and be more reliant upon state funding than trading income, given the inherent economic challenges of operating in deprived areas (see Clifford, 2012).

Most of Key Fund's deals were also asset based, with fewer deals than expected based around a service without a linked asset. They suggested that this might be related to the nature of community businesses, which often coalesce around a particular building or venue, such as pubs, shops, and community centres. Because the Key Fund deals were smaller than those from SASC, however, they were less likely to cover the full costs of a property. Examples given instead included funding building works to allow disabled access or funding an additional post until a community business began to break even. More emphasis was also placed on transitional finance, which allowed the grant to fund high expenditure with a social impact prior to the community business breaking even. Key investment areas were employment and training, health, access to services, networks, and community facilities.

3.2 External investment

The two partners differed somewhat in their optimism regarding the potential for involving external, commercial investment. The two community energy deals by SASC incorporated an additional £6.9 million of external investment from other organisations, with a ratio of external to internal finance of 3.7 and 4.7. This was reportedly quite unusual, however, due to the need for very clear cashflows and asset values to attract external lenders, and the need for the SIFI to take additional risk as a junior lender.

Key Fund reported that they often provided finance alongside other lenders and had a long-term track record of unlocking external finance, filling loan to value gaps and enabling bigger deals with other investors, often with a leverage ratio of 1:1.

£872,762

This was reflected in the further £872,762 in external funding leveraged as part of their second wave of loans, nearly matching the £919,800 in loans funded by Power to Change, alongside the £394,200 in additional grants.

Deals including external lenders only worked, however, where terms such as the cost and duration were balanced fairly between the different lenders, avoiding Key Fund absorbing too much of the overall risk. This higher degree of external finance may reflect the smaller size of the loans, offered to smaller earlier stage organisations, compared to the higher amounts of capital involved in the SASC loans.

3.3 Partnership approach

Both Key Fund and SASC felt that an extremely positive aspect of Power to Change's approach was their commitment to work in partnership with experienced, established providers. Both suggested that the supply side of the social investment market had become increasingly crowded over recent years, increasing overall market spending on fixed costs and overheads, including regulation. Funders wishing to become involved in social investment were tempted to set up their own investment fund, rather than working through existing SIFIs. This made the latter's own business models more precarious, as they operated on relatively thin margins and required a certain scale of operations to break even. By working with established providers, Power to Change helped to contribute towards longer term market sustainability as well as taking advantage of their partners' expertise and economies of scale. This approach allowed them to distribute cash to community businesses that needed it quickly and cost-effectively, whilst maintaining due diligence.

Key Fund suggested that Power to Change's enabling approach allowed them to take advantage of their greater reach into deprived areas, developed over a long history of operation.

70 → 80%

Key Fund were reportedly able to consistently achieve between 70 and 80 per cent of deals in the three most deprived deciles of areas, something that was comparably difficult to achieve through large scale grant making.

Indeed, some of the investees had previously been turned down by Power to Change's main grant programme, whereas Key Fund had been able to spend more time working with these applicants one-on-one to develop bespoke blended deals. Similarly, SASC suggested that by delegating control over the due diligence process, Power to Change had made life easier and less complicated for investees and been able to take advantage of their already well-developed procedures.

The potential downside of a delegated approach is that Power to Change operated at one step removed from the investment process and therefore the potential learning opportunities involved. This was mitigated, however, by a close working relationship between the fund managers and the key contact at Power to Change, as well as a comprehensive data sharing arrangement that allowed Power to Change to further analyse the loan books.

3.4 Implications of COVID-19

The economic and wider social context has changed dramatically since the two blended finance schemes were established and the deals agreed. COVID-19 and its impact are creating urgent and severe pressures on many community businesses' revenue. Trading income has been hit by lockdown measures and reduced consumer confidence, investment returns have fallen, and community fundraising has become more difficult without face-to-face interaction (CFG et al. 2020; King et al., 2020). Reserve levels and working capital are, therefore, likely to have already come under severe pressure as restrictions continued. Many community businesses will also have seen their human resources impacted as staff and volunteers were either shielding, isolating, or becoming ill due to the pandemic. The full impact on community businesses will take time to play out. Not all will have been able to access the business support on offer from the Government, including the furlough scheme or the Coronavirus Business Interruption Loan Scheme. Demand on many services is also likely to have increased.

The COVID-19 pandemic has, therefore, introduced a great deal of uncertainty into the social investment market, with lockdown measures undermining the previously held belief that trading would lead to more independence and resilience compared to grants or government contracts. Although the longer-term spending plans of Government remain uncertain, organisations with low liabilities and higher levels of grant income currently appear to have been hit less hard than their more trading focused counterparts. It is too early to tell whether this might be temporary, or the start of a longer-term trend.

Regardless, the risk appetite across the social sector has undoubtedly diminished, due to understandable uncertainty about being able to afford repayments. This has reportedly led to something of a freeze in the social lending market, though Key Fund have continued to make blended deals as part of the second wave of their partnership with Power to Change. Another exception, according to SASC, has been demand for funding for housing, which if anything has increased amongst social organisations who want to provide accommodation to vulnerable or disadvantaged tenants as a result of the COVID-19 pandemic. Housing benefits provide a reliable income stream from which to make repayments, and in many areas of the country support a reasonable return for investors. Unlocking the wider market is likely to require both an improvement in trading conditions and further investment in 'patient money' that could provide extremely flexible terms and conditions. To afford this model of finance inevitably requires a significant degree of subsidy in the form of non-repayable capital.

In terms of existing investments, SASC suggested that although the pandemic was still at a relatively early phase, it had in many ways validated their lending model, and by extension the investments conducted in partnership with Power to Change. While terms had been eased on a couple of SASC's loans in the short term, none were reportedly at major risk due to the pandemic. This was put down to the due diligence process and the requirement for a clear, sustainable income model to support repayment. Similarly, Key Fund suggested that while many organisations across their entire portfolio had required changes to their terms, such as six-month interest only repayment holidays, very few were yet in severe financial difficulty. Much uncertainty remained, however, particularly around the timescales involved in the pandemic.

Both interviewees suggested that COVID-19 could, however, also result in an overall contraction in the supply side of the market, at least in terms of the number of fund managers. As described above, both felt that there had been a rush to set up new funds in recent years, but that the inherent difficulty of assessing proposals, added to the circumstances of the pandemic, was likely to lead over the next year to some reorganisations, mergers, and exits from the market. Although disruptive, this could lead to some positives if the market was able to consolidate and further refocus its offer around more patient lending.

3.5 The future

The interviewees for this report agreed that the potential for patient investment was likely to outstrip supply in the short to medium term, especially given the effects of the COVID-19 pandemic. In order to increase the supply of flexible, patient finance, including blended loans, ongoing subsidy is always likely to be necessary. Both Key Fund and SASC welcomed the relatively unique role that Power to Change had been willing to play as a grant provider, but noted it was ultimately limited by its spend-out endowment and, in relative terms at the national scale, its limited resources. Given the recent funding extension for Power to Change's work and a new five year strategic plan to 2025, there may be further opportunities for Power to Change to repeat similar experiments in this area and to work alongside other funders to establish funding mechanisms as part of the recovery of communities from the pandemic. Meanwhile, Power to Change continue to work with a small group of community businesses to explore what optimal models of finance might look like. For example, they are currently working with Social Investment Business to 'swap out' some loans from their portfolio, replacing them with more patient, subsidised forms of finance.

Both partners also felt that despite the relative success of their programmes, other voluntary sector funders were also unlikely to adopt the same model fully or at scale. Partly, this is a comparable result of limited resources, particularly in the context of COVID-19. Many funders have offered large amounts of emergency grants, while endowment investment returns will be adversely affected by economic conditions. More fundamentally, trusts and foundations may also be deterred by the fear of subsidising private profit discussed previously.

This suggests that blended finance at scale would ultimately rely on central government, potentially through the National Lottery distributor. Access provides one mechanism via which this could be achieved and appears to be placing a greater recent emphasis on blending at the deal level – a lesson from prior evidence and from Power to Change's investment in this area. The interviewees pointed out, however, that whilst Access funding was at a greater scale than Power to Change, its endowment of £60 million would still only stretch so far, especially when broken down regionally and over multiple years.

Blended investments from both Power to Change and Access can, therefore, arguably achieve the greatest impact by helping to build a stronger evidence base, aiming to demonstrate its social impact and the potential cost savings to the Exchequer. This will involve analysts observing closely how the loans made under both schemes develop over the longer-term. Related developments such as the Social Economy Data Lab[3], and a renewed interest in the long-term impact of Futurebuilders[4], may also be helpful developments in this collective endeavour.

3 https://socialeconomydatalab.org/about-sedl/
4 https://futurebuilders.socialeconomydatalab.org/

4. Conclusion

This report set out to provide an account of Power to Change's approach to blended finance, focussing specifically on two schemes set up with the partners with SIFI SASC and Key Fund. Its findings are largely based on discussions with the key players involved from these three organisations.

Power to Change and its two partner organisations clearly view the experiments in blended finance as a general success. It is not yet possible to assess the long-term return on investment or organisational outcomes, but the key parties involved all appear optimistic despite the huge upheaval from the COVID-19 pandemic.

Several important points have stood out to the research team. First, with the possible exception of Access funding, the blended finance offered by Power to Change was able to offer something very distinctive within the social finance market. This will undoubtedly have helped to make the case for blended finance, providing a useful stock of empirical evidence that analysts can draw upon in coming years. This learning component may provide the greatest legacy of Power to Change's blended finance stream, given that it lacks the scale to fundamentally change the market on its own.

None of the parties involved in these schemes would suggest that blended finance is the only suitable model of finance for community businesses or provides any form of panacea. The partners were all in agreement that it formed a limited but useful part of a wider shift to more patient finance. In some cases, mainstream commercial finance will be viable without subsidy. In others, pure grant funding may remain the only viable option. Where blended finance can make a substantive difference, however, is in opening a segment of the social investment market that would otherwise simply not have been viable. By combining both the grant and loan element, it is possible in the right circumstances to achieve greater social impact than either would have been able to achieve independently.

Blended finance appears to require a particular form of investment opportunity to work, in most cases seeming to require an associated asset linked to a new or expanded funding stream. This often matches well, however, with the place-based focus of community businesses. Housing and accommodation are an important sector with considerable potential. Enabling the purchase of buildings can also enable new services to be delivered. In either case, the route to both impact and repayment appear relatively clear. The deals involving community energy also provide an interesting area of potential growth given the anticipated growth to the renewables market. For smaller sized deals, construction work, renovation, vehicles, or IT equipment may all be able to unlock greater social impact, while blended finance can also help community businesses to bridge temporary gaps in their business model, either at the start of their lifespan, or during economic shocks such as the COVID-19 pandemic.

The potential to leverage additional external funding from commercial lenders remains somewhat unclear. On the one hand Key Fund and SASC both successfully involved at least some external finance, but there are potential risks to social lenders acting as junior partners in deals if the financial risk is not distributed fairly. External involvement may also heighten concerns from more traditional funders that grant income will end up subsidising private interests. This is an area that would benefit from further research and examination, but clearly there are risks being balanced against the potential social impact that could be unlocked by greater access to finance in some cases.

Ultimately, the key parties interviewed for this report agreed that a social finance market built around the concept of patient and flexible lending, including blended deals, would rely on Government support and subsidy. This argument has only gained more weight with the COVID-19 pandemic, which has radically increased the uncertainty involved in lending and repaying capital. To unlock this support, a much stronger evidence base is likely to be required that subsiding social finance can provide, in the right circumstances, greater social impact than providing the grant funding directly. Power to Change's experiments in this field are a welcome step in this direction, but a much larger cohort of loans is likely to be necessary to make the case conclusively. This creates a chicken and egg scenario in which the evidence base and the lending both rely on one another. The performance of the Power to Change portfolio, the results from the Growth Fund evaluation, research visiting Futurebuilders investments, all have a role to play. The eventual direction of the social investment market, however, as it has since its inception, is likely to remain ultimately a question of Government policy.

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