Initial observations on blending debt and grant from the Growth Fund

Summary data and analysis from 13 live Growth Fund applications, as of 1 December 2016

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Aims of the Growth Fund

The Growth Fund is designed to provide **small scale affordable unsecured loans for charities and social enterprises**. The organisations intended to benefit are likely to be at early stages of growth or developing their trading income, and probably have not have taken on social investment before.

Access manages the Growth Fund in a **wholesale capacity**. That means that we **work through social investors**, who apply to us and who run funds and make loans and other social investments to charities and social enterprises. Those **investments will be under £150,000** and may also include a grant for the charity or social enterprise.

Across its portfolio as a whole, the Growth Fund seeks to achieve a **geographical spread** of users and end beneficiaries **across England**, as well as support a **range of social issues**.

Previously this type of finance has not been readily available, mainly because social investors have not felt able to afford to make these small loans. Those investors are usually borrowing money themselves in order to on-lend so they need to be confident they will get repaid. However lending of this type has been seen as too high risk. The operating costs of managing a high number of small loans is also expensive. Therefore many of these investors have tended to only offer larger investments.

The Growth Fund **tackles this availability gap by blending loan and grant funding for social investors**. The grant allows those investors to offer these smaller loans because it:

- Helps to contribute towards the costs of making lots of loans; so that the social investor can afford the proportionally higher transaction costs (this use of the grant is a small proportion of the total grant amount) thus reducing the risk for them in managing the fund (we call this Grant A).
- Allows them to be able to afford for some of the loans to fail; by blending grant and debt in the fund the social investor can afford for the portfolio as a whole not to break even and therefore will be willing to take greater risk on the loans that they make, thus reducing the risk of the provider of debt in the fund not getting their money back (we call this Grant B).
- Allows them to offer grant along side loans to charities and social enterprises; so that total investments may be more affordable for the borrowing organisation, thus reducing their risk of not being able to manage the repayments (we call this Grant C).

The grant must total less than 50% of the overall investment into the social investor.

The Growth Fund blends **£22.5m of grant from the Big Lottery Fund** with at **least £22.5m of loan funds from Big Society Capital.** Loan funds may also come from some other sources. Access manages the end to end programme on their behalf.

In addition to providing relevant finance to over 600 organisations, Access's goals in delivering the Growth Fund are to make a significant contribution to the learning about how grant subsidy can best be used to develop the social investment market (our learning strategy is available here). This report is an initial contribution to this agenda and analyses what can be learned from the first wave of applications in terms of the demand for social investment that those applicants are experiencing from charities and social enterprises, and how grant and debt can best be blended to meet that demand.

Structure of the Growth Fund

Loan into the fund (from BSC or other lender)

Grant into the fund (from BLF, in three parts: A, B & C)

Social Investor

Grant A
Pot for **covering costs** of making small loans

Pot for **lending**

Loan layer gets repaid to BSC (or other lenders)

Grant B
Grant layer **allows for the fund to afford defaults**

Grant C
Pot for **making grants** to charities or social enterprises

Loan

Grant

Charity or Social Enterprise

- Loan or loan + grant blend of under £150k
- Unsecured
- For growth, to help with cash flow, to stimulate income generating activities
- Typically 3-6 year repayment
- Interest of c. 6-12% APR on the loan

Update on progress

As of 1 December 2016:

- Three funds have been launched totalling £14.2m;
- Five funds, totalling £13.8m have had an offer of investment made and legal documents are being finalised; and
- Five funds, totalling £20.1m are currently in a development or due diligence process and are subject to further approvals by the Joint Investment Committee (of Access, the Big Lottery Fund and Big Society Capital).

The data in this pack come from the 13 applications listed above. For the purposes of highlighting the main trends we have not separated this cohort by their current status in our process. Given that a number of these are still subject to due diligence not all these funds may launch, or there may be changes in the fund size and balance of loan and grant prior to a fund launching.

In total we have received 51 expressions of interest of which 29 organisations have been invited to apply to the Growth Fund and of these 22 are still in the portfolio or pipeline.

We have developed three portfolio themes to help us balance the range of applications we receive and ensure that we have a diverse portfolio. These are outlined on slide 7.

Range of organisations applying

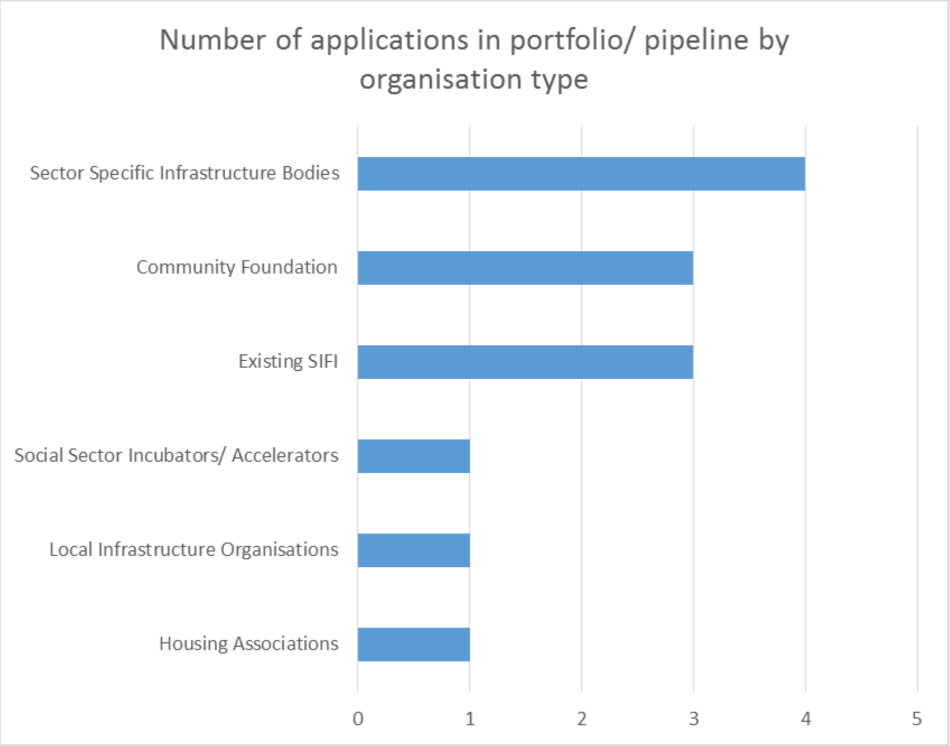
An explicit aim of the Growth Fund is to expand the range of organisations who are able to offer loans to charities and social enterprises. We believe that this may help increase the reach of social investment products and help social investment opportunities to be more relevant to the context and markets in which charities and social enterprises are operating.

In early 2016 we worked with New Philanthropy Capital to assess the range of organisations who might be a good fit for the Growth Fund. You can see the report here.

Expressions of interest have been received from (in descending order of frequency):

- Existing social investors
- Sector specific infrastructure bodies
- Community Foundations
- Local infrastructure organisations
- Start-up social investors
- Responsible Finance Providers
- Credit Unions
- Social sector incubators and accelerators
- SME investors
- Charitable foundations
- Housing associations
- Universities
- Delivery charities

Of the 13 applications in this dataset:



Geographical spread

The majority of the total applications for the Growth Fund so far have been place based.

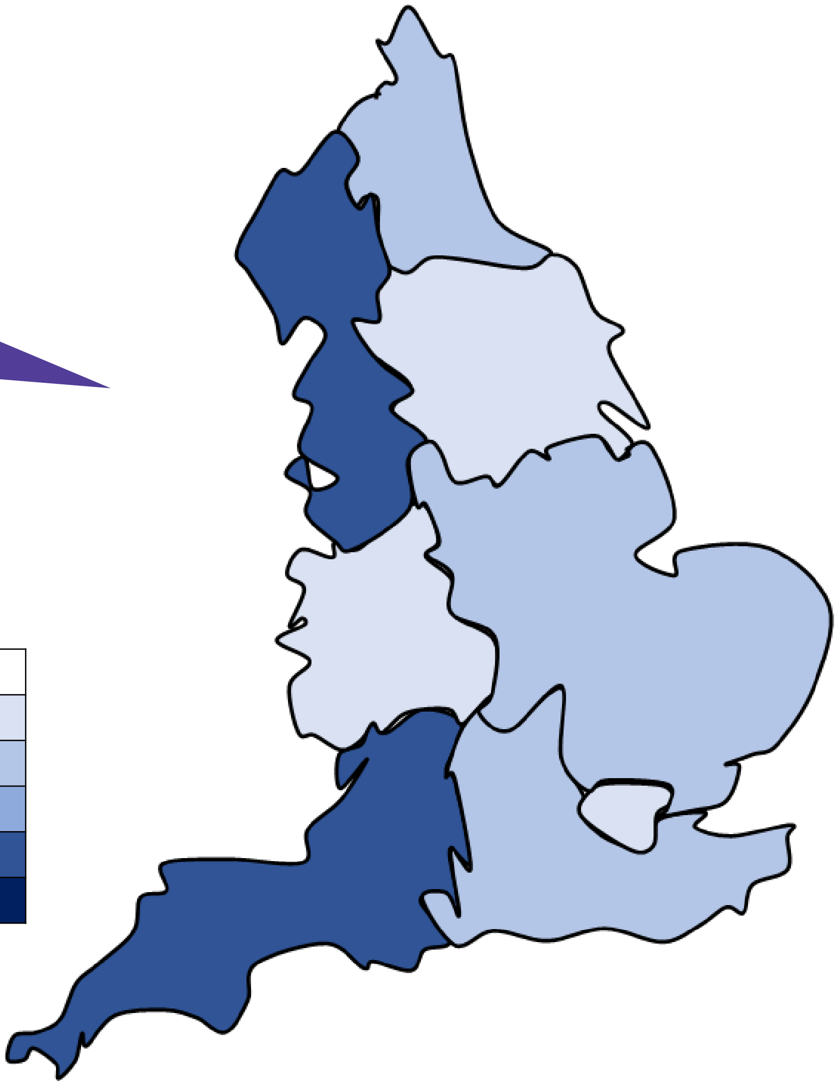
Of these 13 applications:

- 4 are focused on a local authority or combined authority area
- 2 are focused on an English region
- 1 is focused on multiple English regions
- 6 are England-wide

Number of funds which cover each region:

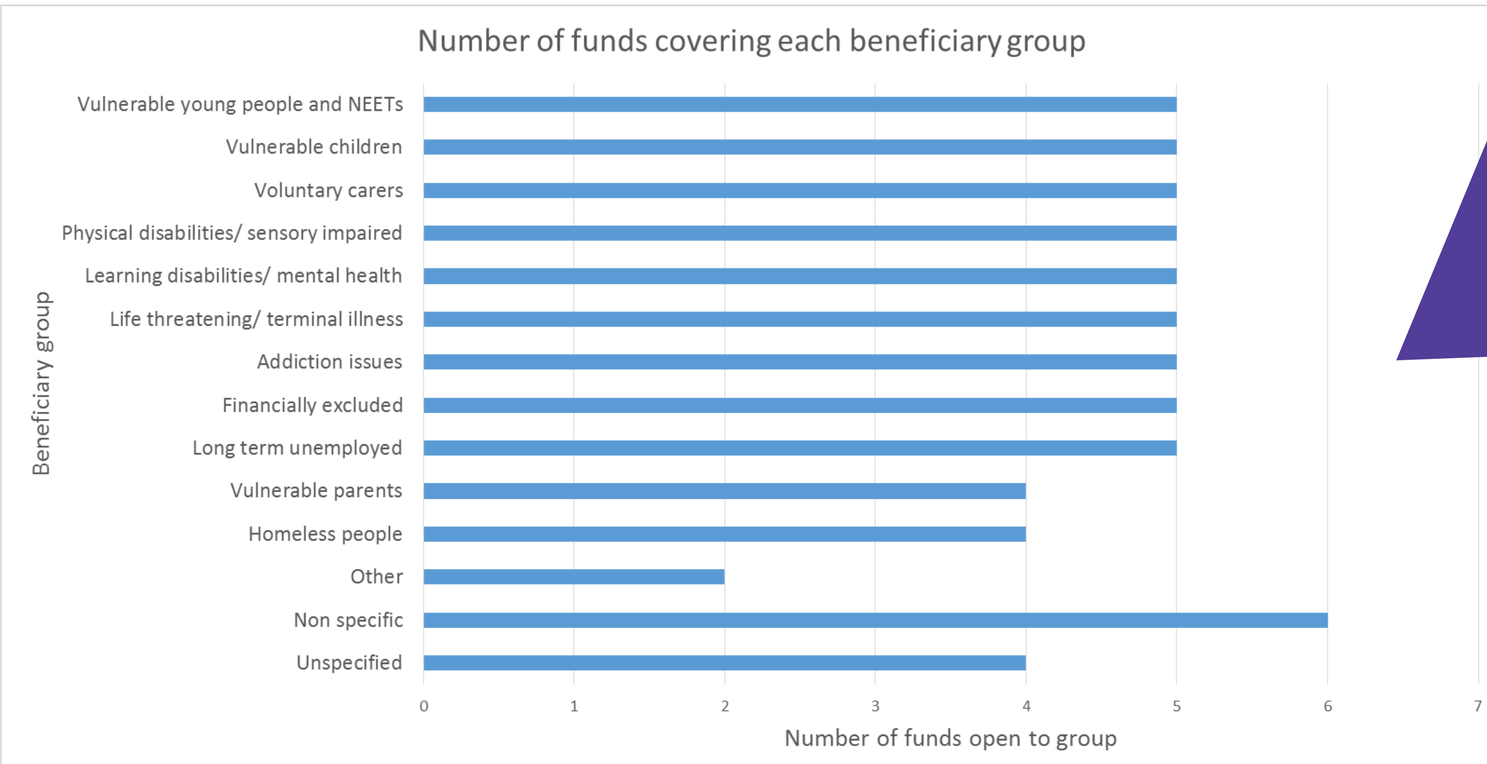
This map shows the geographical coverage of the 13 funds by the number of funds which cover each area. Funds which are England-wide are shown as covering all regions.

≤5
6
7
8
9
≥10



Beneficiary groups

Given the data provided at EoI stage, there are no clear trends in the impact areas being targeted by all of the applicants to the Growth Fund, with the majority of applicants seeking to establish non-specific funds.



The graph shows the frequency of each impact area as selected by the 13 applicants when they submitted their EoI. Each applicant can select as many outcome areas as they want.

The vast majority of the 13 funds are covering multiple impact areas.

Two have exclusively a health and wellbeing focus and one is focused on homeless people.

Our three portfolio themes

The Joint Investment Committee has defined three portfolio themes for the Growth Fund, outlined below. These may overlap, so some applications fit within multiple themes.

- Efficiency: Social investors who can meet current demand from charities and social enterprises for smaller unsecured loans in an efficient way
- New Approaches: Social investors who offer creative and relevant new products for charities and social enterprises, or new ways of delivering social investment to the sector
- Reach: Social investors who can offer social investment to, and make it relevant for, groups of charities and social enterprises who have not been able to benefit to date

Overall we have seen a good mix of applicants across our three themes, with more of the earlier applications coming under the Efficiency theme and more categorised as New Approaches and Reach as the programme has developed.

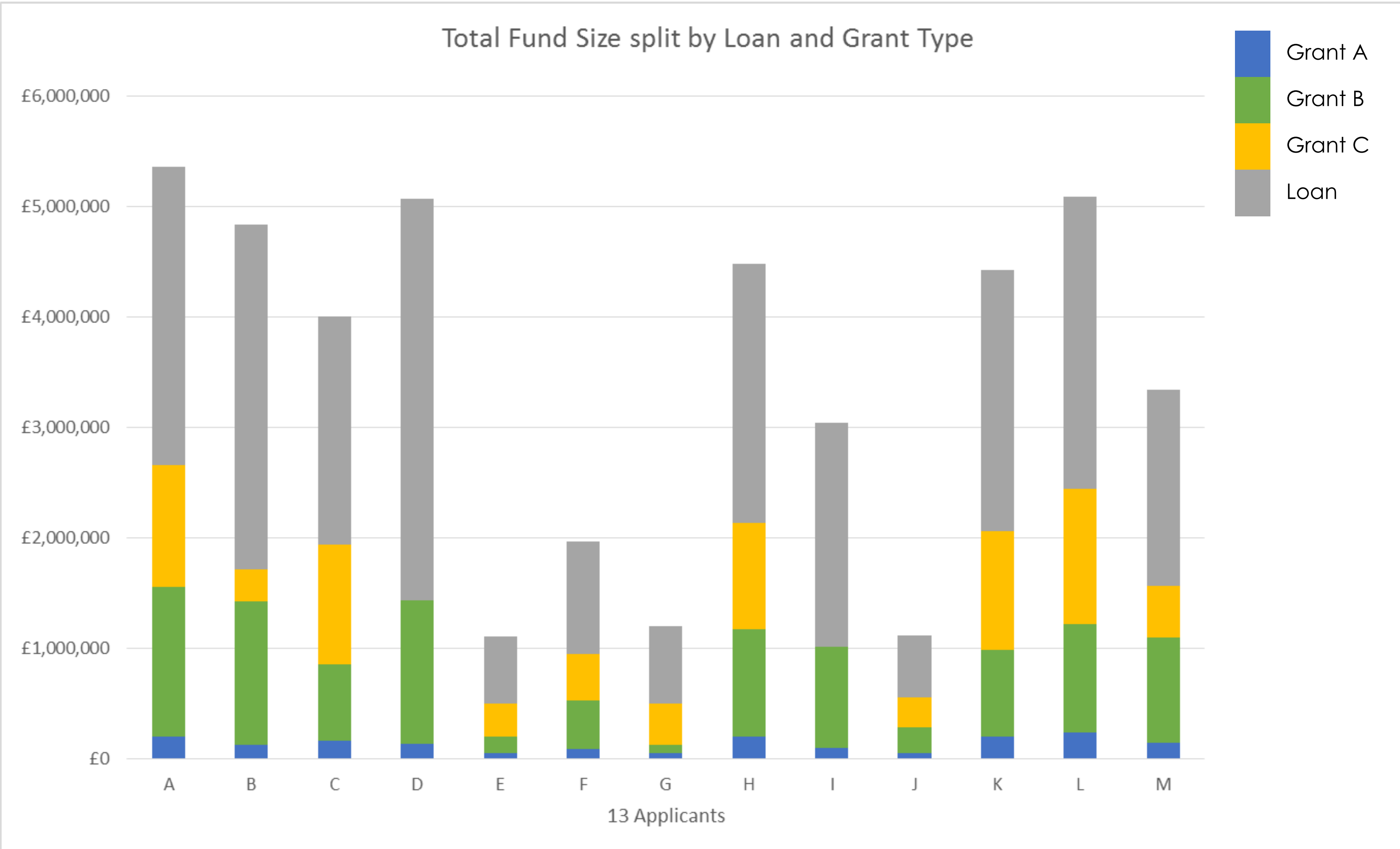
Trends and lessons in applications in each of the strategic themes		
Applications which fall into the **Efficiency** theme are typically from existing social investors. The Joint Investment Committee has indicated that it does not expect to make many more investments under the Efficiency strand.	Most **New Approaches** are offering a new model of intermediation, usually related to the existing relationship we would expect the social lender to have to the potential borrower (e.g. as a member of a trade body or network). We have not seen many applications which propose to offer any alternative product, such as a risk product, rather than a simple loan.	Most **Reach** applications have focused on a specific geography, on the basis that the social investor being place based will help them to access local networks more effectively.

Summary data from the 13 applications

	Mean	Min*	Max	Range*
Total fund size	**£3,465,560**	£1,113,654	£5,359,489	£4,245,835
… of which total Access grant into the fund	**£1,500,807**	£504,651	£2,662,589	£2,157,938
… of which Grant A (subsidy to help cover operating costs)	**£136,523**	£50,000	£244,000	£194,000
… of which Grant B (subsidy to cover losses in the fund)	**£781,407**	£77,098	£1,358,589	£1,281,491
… of which Grant C (grant made available alongside loans to charities and social enterprises)	**£582,877**	£270,000	£1,228,500	£958,500
… of which total loan into the fund	**£1,964,753**	£558,891	£3,626,594	£3,067,703
Total pot for loan making (Grant B plus loan into the fund)	**£2,746,160**	£770,979	£4,927,438	£4,156,459
Average size of loan to be made by the fund	**£62,231**	£25,000	£100,000	£75,000
Number of loans to be made by the fund	**56**	21	138	117
Grant A as a proportion of total fund size	**4.1%**	2.6%	5.0%	2.4%
Proportion of Grant B in the total pot for loan making	**27%**	10%	35%	25%
Proportion of charities and social enterprises receiving a grant alongside a loan (Grant C)	**71%**	36%	100%	64%
Average size of grant (funded by Grant C) to charity or social enterprise (where present)	**£16,974**	£7,000	£30,000	£23,000
Average size of grant (funded by Grant C) made to a charity or social enterprise as a proportion of average loan size (where present)	**32%**	17%	50%	33%

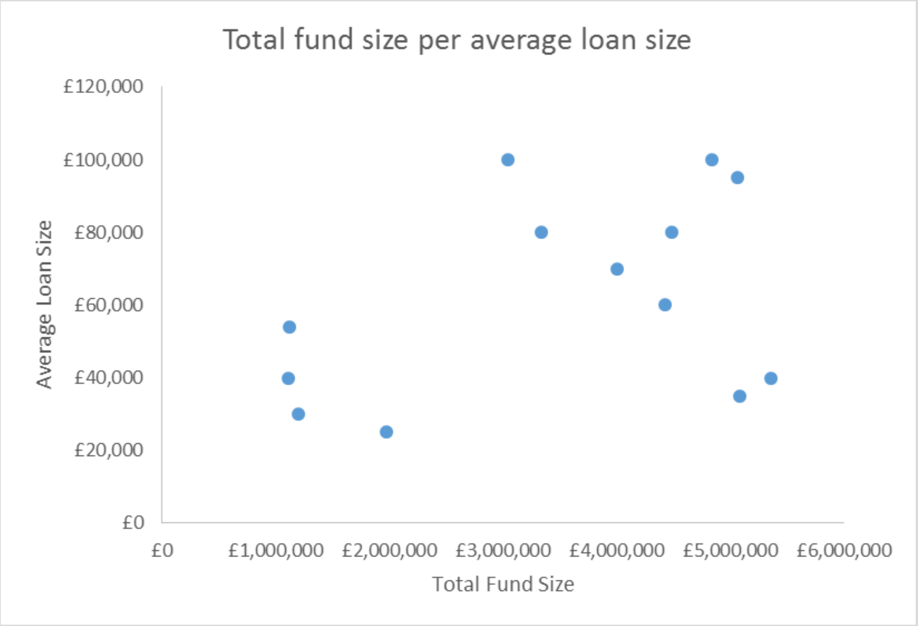
* Values of 0 have been excluded from the min and range calculations

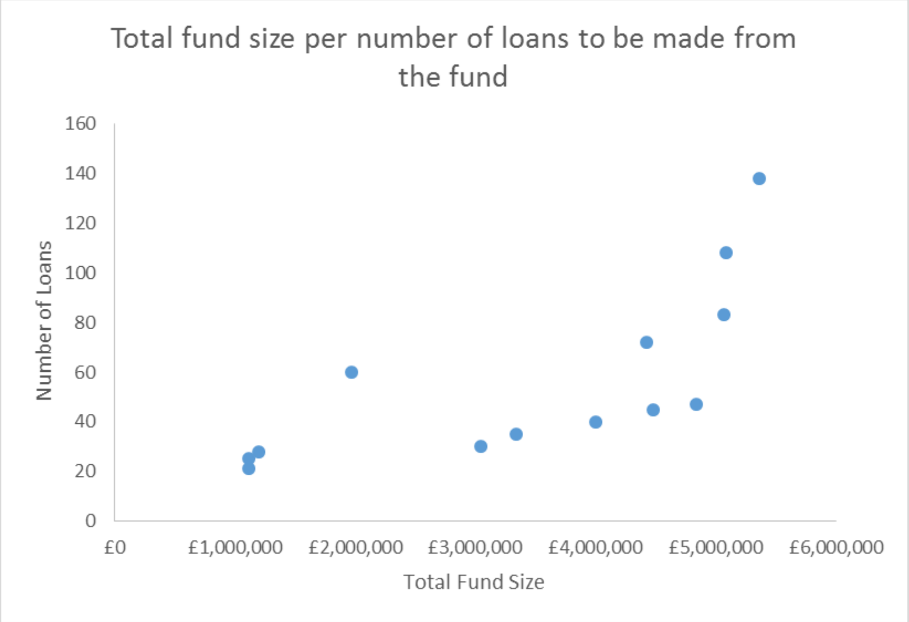
Range of fund sizes and grant/loan composition



Fund size by average loan size and number of loans to be made

Unsurprisingly given the £150k ceiling on loan/ loan plus grant size which can be made by the Growth Fund, there is a clear positive correlation between fund size and the number of loans to be made.





However there appears to be no relationship between total fund size and average loan size. This reflects that a wide variety of different markets are being served by social investors delivering the Growth Fund.

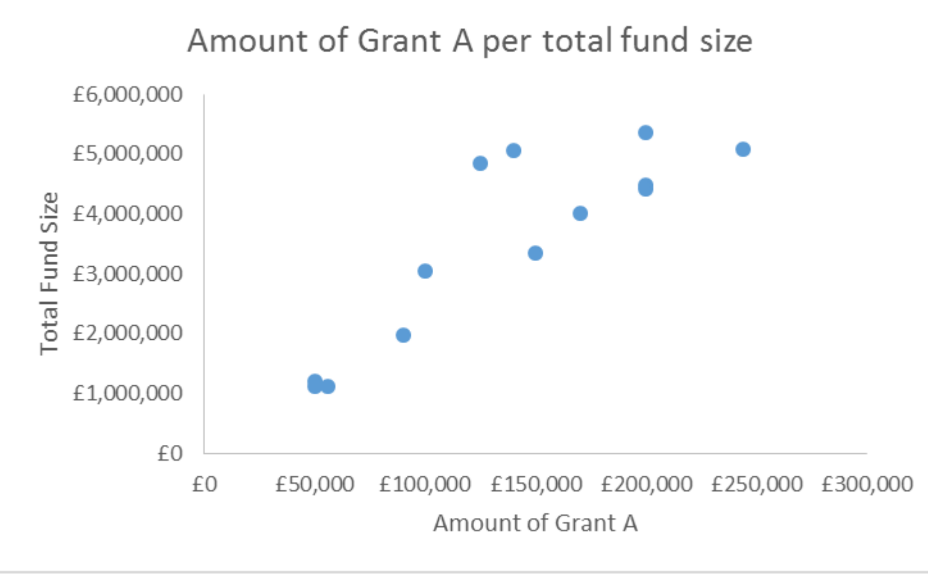
Role of grant in supporting operating costs for social investors

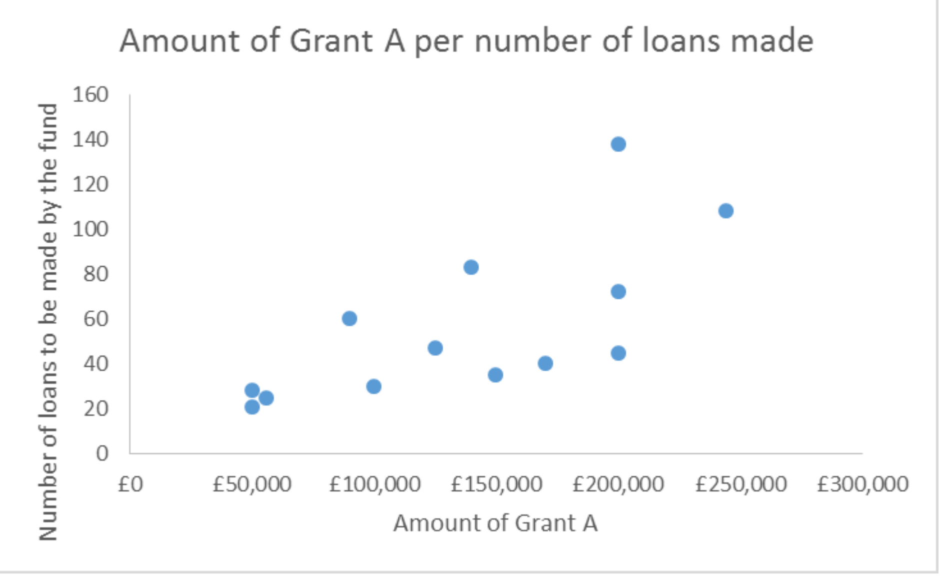
Social investors delivering the Growth Fund earn the majority of the income they need to run their fund from interest and fees which they charge on the loans they make. Access recommends that this is in the range of 6-12%. However, Access recognises that building and managing portfolios of small loans is expensive and may require additional support, in particular in the early months of running a fund.

The Growth Fund therefore offers a grant to the social investor to provide additional support for the operating costs of running the fund. We call this Grant A.

In these 13 applications we have seen Grant A as an average of 4.1% of the total fund size requested. The range is 2.6% to 5% of total fund size, which equates to a range of £50,000 to £244,000.

Each applicant is awarded an amount of Grant A based on the specific need outlined in their application. However, the graphs below show clear correlations between the amount of Grant A requested and the total fund size, as well as the total number of loans expected to be made from the fund.





Summary: The 13 applications anticipate requiring an operating cost subsidy of an average of 4.1% of the fund size in addition to the income they generate from interest and fees to be able to make sub-£150k loans to charities and social enterprises

Role of grant in blending with debt in the fund

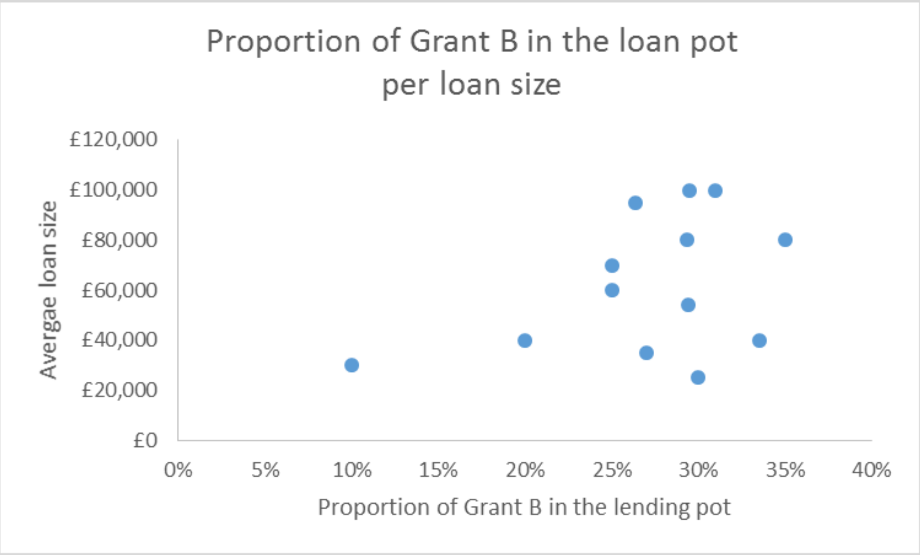
Our hypothesis is that, to be able to make loans to charities and social enterprises who can benefit from taking on social investment, but who lack security or a track record, the social investor needs to have the capacity to lose money.

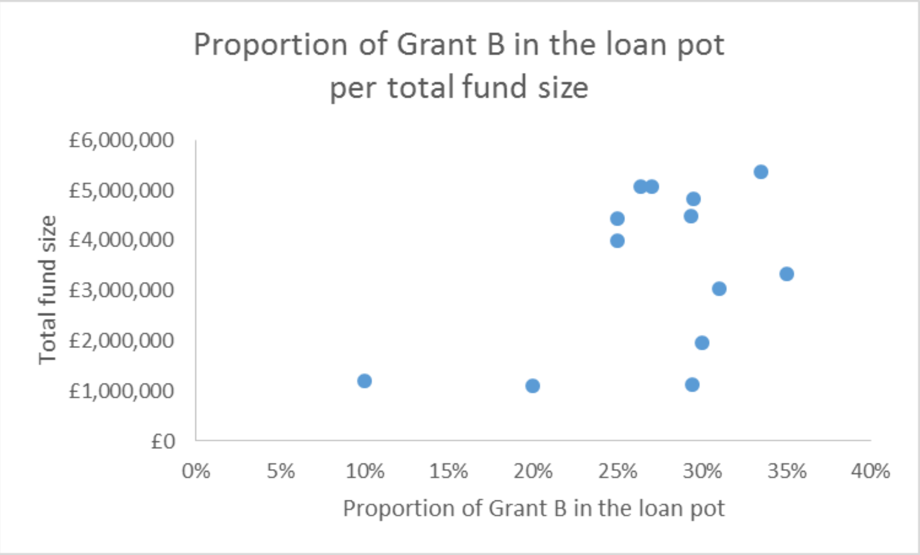
The Growth Fund blends Grant B with the debt from Big Society Capital to finance the loans which the social investor makes. Each loan made comprises a fixed proportion of Grant B and BSC loan, allowing the portfolio as a whole to be able to afford defaults.

Note that some funds include other co-investors and alternative investors investing on the same terms as BSC. These additional loans have been grouped together for the purposes of this report. BSC's return is fixed at a maximum of 5%.

On average the pots for lending are comprised of 27% Grant B and 73% loan. The highest proportion of Grant B is 35% and the lowest is 10%.

The proportion of Grant B and BSC loan is largely driven by default assumptions and is awarded based on the individual business plan reviewed by the Joint Investment Committee. These default assumptions will vary significantly depending on the market being targeted by the social investor. However the data from the 13 applications does not appear to show a clear correlation between the proportion of Grant B in the lending pot and either the average loan size or the total fund size.





Summary: The 13 applications show there is an anticipated need for between 10% and 35% (mean 27%) subsidy in the loan pot to ensure that the lenders receive back their capital and expected return.

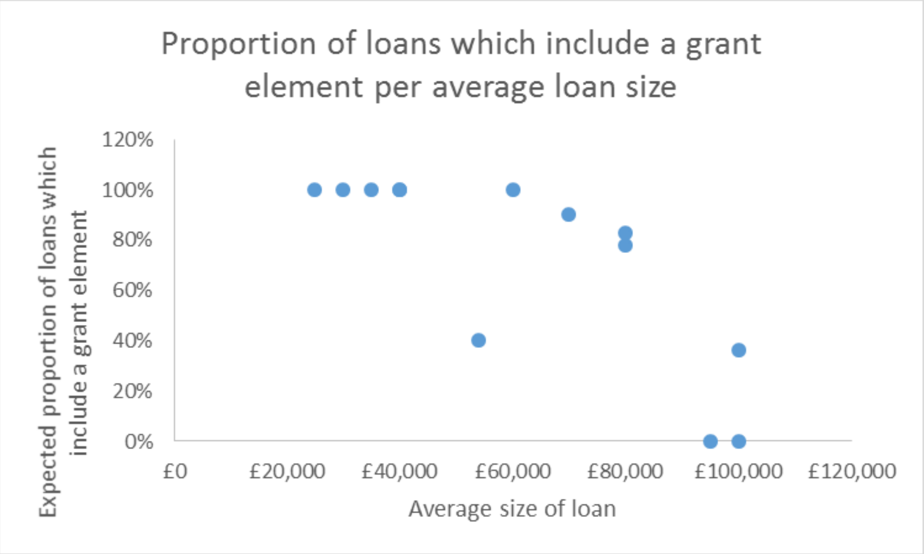
Role of grant in blending with loans for charities and social enterprises

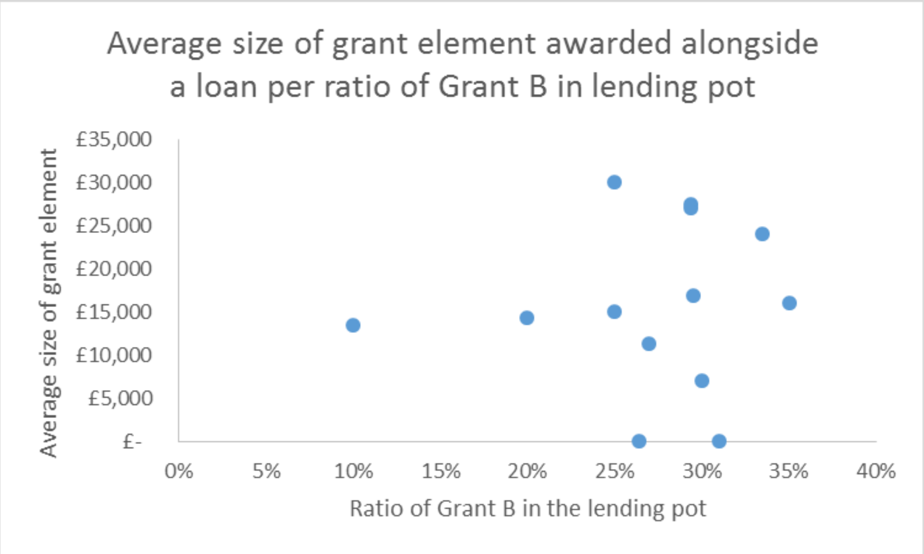
Charities and social enterprises who could benefit from taking on social investment but who have not borrowed before may be reluctant to do so or be concerned about affordability. The Growth Fund offers social investors the ability to make grants alongside loans to charities and social enterprises to reduce the risk for the borrower and make the loans more affordable. We call this Grant C. The loan to the charity or social enterprise must always be larger than the grant, and the total of the loan and any grant must be less than £150k.

11 of the 13 applicants plan to utilise Grant C. Overall an average of 71% of the loans made will include an element of grant to the charity/ social enterprise. Six of the social investors plan to make grant available to all borrowers.

The size of the grants will average £16,974, with the largest expected grants of £30,000 and smallest of £7,000 (a significant range). This equates to the grant being worth an average of 32% of the loan, with a range of 17% to 50% across the 11 applications which will use Grant C.

Grant C is awarded to social investors based on the need demonstrated in their application. From the 13 applications there appears to be a trend that the larger the average loan size, the fewer charities and social enterprises are offered a grant. However, there does not appear to be any correlation between the size of grants awarded alongside loans with the use of Grant B in the pot for lending (which is driven by anticipated default rates). Therefore social investors do not appear to be using grants alongside loans to mitigate riskier deals.





Summary: 71% of the loans to be made by these 13 social investors will be made alongside a grant to the charity/ social enterprise. Of those deals, the grant will be worth an average of 32% of the loan.

Next Steps

- The data in this report come entirely from the applications made by 13 social investors and the offers which the Joint Investment Committee for the Growth Fund has made. It shows what is expected to happen, but none of us know exactly how these funds will perform.
- Social investors who are funded by the Growth Fund will provide summary data each quarter to Access. From Q1 2017 Access will use these reports to construct a quarterly dashboard showing real progress of the Growth Fund.
- The Growth Fund is also being comprehensively externally evaluated during its life. This will provide the opportunity for broader lessons to be captured which will benefit charities and social enterprises as well as social investors.
- For more information on the details of the Growth Fund and how to apply please see https://access-socialinvestment.org.uk/growth-fund/for-social-lenders/