Innovation Caucus

SOCIAL INVESTMENT PARTNERSHIPS

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CONTENTS

Executive Summary 4

Key Terms 5

Context & Background 7

Research Approach & Methodology 7

Understanding of Social Investment 9

Connection between Social Investment and Academic Entrepreneurship 10

Engagement and Operations 12

Market for Social Investment 13

When is Social Investment Best Used? 16

Equality, Diversion and Inclusion 17

Other Support to Realise Impact 17

Alternative Instruments 18

Risk & Mitigation 19

Outcomes and Impacts 20

Impact of social investment 21

Limitations & Future Research 23

Opportunities for Further Development 23

References 24

Appendix 1: Case Studies 26

Appendix 2: Deep Dive Literature Review 30

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About the Innovation Caucus

The Innovation Caucus supports sustainable innovation-led growth by promoting engagement between the social sciences and the innovation ecosystem. Our members are leading academics from across the social science community, who are engaged in different aspects of innovation research. We connect the social sciences, Innovate UK and the ESRC, by providing research insights to inform innovation policy and practice. We champion the role of social science in innovation and enhance its impact. Professor Tim Vorley is the Academic Lead. The initiative is funded and co-developed by the ESRC and Innovate UK..

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EXECUTIVE SUMMARY

This research was undertaken to understand the current potential of social investment to support academic spinouts and innovative businesses. It aimed to build an understanding of the role of intermediary organisations in supporting social investment and the potential it can have to support social science and humanities commercialisation opportunities. The project provided a broad initial consultation and review to scope out possibilities in the social investment market and builds on an earlier review of the literature presented in Appendix 2. ESRC and Innovate UK supported research to understand the potential of social investment. This report provides an understanding of what social investment is, when it is best used and the barriers to achieving successful social impact investment. As part of the research, interviews with stakeholders with diverse perspectives were conducted and deep dive case studies used to bring to life examples of how social investment has worked in practice.

Core findings include that there is not an agreed definition of social investment, but that this allows for necessary flexibility in the use of different mechanisms, modes and designs of investment into social businesses of different types. Social investment is not necessarily a panacea for creating social and economic impact, however, in this report we outline that in particular contexts it is a useful tool when a potential investee has a specific social mission they wish to deliver. It is important that any new social investment funds are flexible in their approach both towards the types of organisations eligible to apply, and the broad social missions targeted. Stakeholders interviewed stressed the importance of further consultation with a range of potential social investees to understand their needs. Social investment impact can be measured on multiple levels.

The findings highlight the opportunity for ESRC and Innovate UK to add to the social investment market through working with existing organisations. Opportunities for development are provided in full at the end of the report and are summarised below:

- In supporting Social Investment Partnerships, there is merit in the ESRC and Innovate UK (as well as UKRI more widely) identifying the high-level priorities in order to give a focus to prospective applicants.
- Any support for future Social Investment Partnerships programmes needs to have a clear social, societal and or environmental challenge or need.
- There are opportunities to promote equality, diversity and inclusion through Social Investment Partnerships programmes. There is scope to engage a broader range of prospective investee groups which are likely to go beyond those attracting investment from traditional sources.
- Any future plans for Social Investment Partnerships that seek to support social enterprise or social ventures need to ensure direct consultation with a cohort of social entrepreneurs and social investors, and have them represented on a steering/advisory group.
- There is an opportunity as a part of any future Social Investment Partnerships to promote partnership and collaboration with existing infrastructures and stakeholders to maximise the value added though projects (i.e. social entrepreneurs, universities, local authorities, trusts, charities and social investment management firms).
- The focus on realising economic return, financial instruments and exit strategies need to be flexible in investment accelerators to allow impact businesses to gain the most from investment.

KEY TERMS

- **Asset lock** – typically a legal provision that ensures that the assets of an organisation do not leave the organisation and are reinvested back into the community or to further the organisation's social mission.

- **Impact investment** – is a narrower term than social investment used to describe the use of venture capital mechanisms (equity, debt or mezzanine finance) in social organisations which put social value created over financial returns, (Glänzel & Scheuerle, 2016; Agrawal & Hockerts, 2019).

- **Mission lock** – a way of locking in social mission without having an asset lock, this usually involves creating a statement in the organisation's articles of association to ensure social mission is central to the organisation's operations.

- **Social business/ventures** - this term will be used to refer to organisations who have a social mission embedded in their organisation but are not asset locked.

- **Social enterprise** – the definition of social enterprise varies across contextual boundaries. This report will refer to social enterprises as organisations who are asset locked, and have a status which does not allow redistribution of profits.

- **Social finance** – is an umbrella term used to describe ways in which capital is used to fund social and environmental outcomes (Nicholls, 2013; Glänzel & Scheuerle, 2016). It covers a full range of mechanisms including social investment – covering investments focused purely on societal outcomes (philanthropic grants, public grants), blended models (impact investing, social impact bonds) to traditional investment (with a financial focus) in social ventures.

- **Social impact** -is a nebulous concept referring to a positive outcome for groups of people due to an action, service, product or policy.

- **Social impact bonds** - are "a type of outcome based contract that incorporates the use of private funding from social investors to cover the upfront capital required for a provider to set up and deliver a service. The service is set out to achieve measurable outcomes established by the commissioning authority and the investor is repaid only if these outcomes are achieved." (GoLab). See Appendix 1 Case 1 for the Peterborough Prison Social Impact Bond Case Study.

- **Social Innovation** – is described as "new ideas (products, services and models) that simultaneously meet social needs (more effectively than alternatives) and create new social relationships or collaborations." (Social Innovation Exchange, 2010, p.18).

- **Social investment** – is a term used to describe capital investments in organisations who aim to have social outcomes. This would cover both impact first and finance first style investments using loans and equity. Although academics in public policy may also use this term to describe an approach to social welfare reform (Harvie & Ogman, 2019) we use social investment to mean the use of capital investment techniques in projects which have targeted and measurable societal as well as economic value (OECD, 2019). Social investment is often confused with socially responsible investment which focuses the use of rankings and metrics on a portfolio approach to investment in the stock market (Roundy et al., 2017, Widyawati, 2020).

CONTEXT AND BACKGROUND

This research was undertaken to understand the current potential of social investment to support academic spinouts and innovative businesses. The project aimed to provide a broad initial consultation and review to scope out possibilities in the social investment market and builds on an earlier review of the literature (which can be found in Appendix 2). ESRC and Innovate UK supported research to understand the potential of social investment. This study and report provides insights into what social investment is, when it is best used, and the barriers to achieving successful social impact investment outcomes. The study draws on existing evidence about social investments and social investment partnerships to identify good practices, as well as exploring what investors expect and how they assess the success of social investments.

The report begins by exploring the differences in understandings of social investment and how it can be used to support academic entrepreneurs. It then explores the ways in which social investment currently operates and potential gaps in the market. This is followed by a section which outlines and attempts to define the different levels of impact that can be achieved by social investment. The report is concluded by a reflection on the limitations of the study (and subsequent opportunities for future research) and opportunities for further development are provided.

This report builds on the 'Deep Dive Review 2020' (Appendix 2) which reviewed the academic and grey literature on social and impact investment, to understand the current state of play in the sector. This study progressed the review of academic and grey literature by adding empirical data from interviews with different stakeholders and a series of deep dive case studies that are summarised in Appendix 1.

According to evidence presented in the Deep Dive Review 2020, access to finance is a barrier to the growth of organisations aiming to maximise their social impact (Glänzel & Scheuerle, 2016). To provide flexible financing which is not linked to specific programmes (which is often the case with grants), impact investing has become a field of attention for policy makers, funders, social economy organisations and academics (Glänzel & Scheuerle, 2016). Simultaneously, there is growing interest from those who own capital in using their resources to create social value as well as financial returns (Nicholls, 2013). Investment is often presented on a spectrum from grant making to traditional forms of investment (such as venture capital) which aim to maximise return on investment (Argrawal & Hockerts, 2019).

Traditional forms of investment may have a societal or social impact, however, the difference between traditional investment and social investment lies in the metrics of success used by each. Social investments require measurable social outcomes whereas a traditional investment typically measures only financial return on investment (Roundy et al., 2017). Social investment and social enterprise/entrepreneurship are closely linked both in practice and conceptually (Roundy et al., 2017), and often social enterprises are the recipients of social investment. However, theories of social innovation suggest that social value can be created outside of social enterprise and the non-profit sector (Franco-Leal, 2020), therefore social investment is not exclusively used to fund social enterprise or the non-profit sector.

RESEARCH APPROACH & METHODOLOGY

This research aimed to enable UKRI to understand the role it could play in supporting social investment and the potential it can have to support social science and humanities commercialisation opportunities. In scoping this possible programme, the study had the following objectives:

- To understand the barriers to commercialisation in areas of high social impact - particularly of the opportunities to support commercialisation of social science and humanities.
- To understand the extent to which an 'Investment Partnership' programme is an appropriate solution, exploring what a programme might comprise of and how it could be designed and implemented. This should include any differences from the existing scheme along with consideration of the needs of the investors and university Knowledge Exchange/Technology Transfer Officers (KE/TTO) leads.
- To understand what can be considered as knowns (existing evidence) and what assumptions IUK and ESRC have around social investors that should be tested.
- To produce case studies in this area.

To address these objectives the study had three phases: i) A comprehensive literature review of the academic literature and evidence and consideration of grey literature including think tank, government, and social investor reports was undertaken; ii) Semi-structured interviews which were conducted with stakeholders engaged with and/or with experience of social investment (Table I outlines categories of stakeholders interviewed); and, iii) a series of deep dive case studies were completed drawing on a range of examples.

Table 1 Interviewees by Stakeholder Type

Stakeholder type	Interviews conducted
Internal stakeholders (UKRI staff members involved in programmes with social aspects)	4
Intermediaries (bodies which support or represent social impact businesses)	3
Universities	3
Social businesses/Investees	2
Investors	6

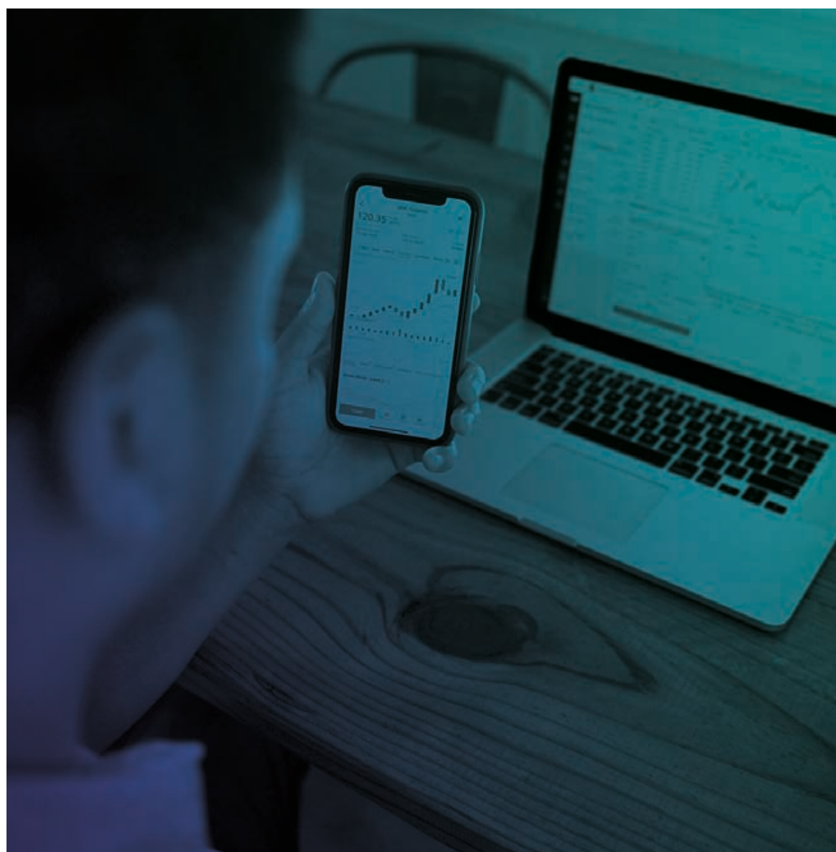
A total of 19 interviews were conducted between December 2020 and March 2021. Interviewees often had multiple roles within the social investment sector hence the breakdown of interviewees discussed in table 1 does not total to 19. Interviews lasted between 30 - 60 minutes. Of the investors interviewed one could be described as a 'traditional investor' associated with a large financial institution, the remaining 5 were 'social investors' in that most of them exclusively provided finance to social impact projects.

Interviews followed a schedule which focused on the role of innovation agencies and innovation policy for supporting social impact, looking at the gaps in the social investment market, barriers to social investment as well as barriers to effective partnership working between different groups (social businesses, investors, intermediaries) working in social investment, and benefits of investment programmes focused on social impact. Interviews were transcribed and thematically analysed. Small themes (or codes) were grouped together to form three broad themes:

- Understanding of Social Investment (covering issues of definitions and language),
- Engagement and Operations (covering detail of programmes and market needs) and
- Outcomes and Impacts (covering issues of impact measurement, and the results of social investment).

These broad themes form the basis of the report.

Collation and analysis of case study materials looked at examples of existing/historic Social Investment Partnerships as well as existing Innovate UK investment partnerships to understand how investment partnerships are funded in general.



UNDERSTANDING OF SOCIAL INVESTMENT

There is not a consensus on a concrete definition of what social investment is, both according to the literature (for example Daggers et al., 2021) and interviewees. Interviewee's awareness and ability to provide a concrete definition of social investment varied. Many answers to the question "what does social investment mean to you?" mentioned the need to consider the social impact of a project which is being invested in but tended to be vague. For example one interviewee answered, "So my understanding is very much around, it's kind of those do good projects. So it's the not for profit stuff. And it's all that societal benefit, kind of that terminology. And investment behind that would be funding to move those ideas or concepts or projects forward" (Interviewee quote). Interviewees emphasised balancing social and economic in some way and the importance of 'values-driven' approaches. The economic and social are often described in grey and academic literature as competing and causing tensions within organisations, however, organisations and innovation which combine the two have been found to have economic and societal impacts.

Understandably, social investors had a more nuanced and concrete idea of what social investment meant, for example:

> *"social investment [...] is primarily a financial instrument, rather than a grant, which is there [...] to provide resources, financial resources [it] also tracks the impact that money makes, as well as trying to make a return or to match the financial targets of the resource [...] the devices, I associate more strongly with social investment, are equity investments, loans, and bonds, social bonds" (Interviewee quote)*

As the quotes above indicate, some interviewees identified social investment as finance for a project or specific type of organisation whereas others discussed it from the perspective of types of repayable finance . Social investment instruments differ from grants in that they are repayable in some way. Many investments in social innovation projects are grants, but differentiating between grants and mechanisms of repayable finance is important in the ways in which social innovations are commercialised.

The variety in definition may suggest that there is a need for a concrete definition to be created. However, in the related field of social enterprise, the plurality and conceptual 'fuzziness' of terms has been described as essential to creating a diverse means of resolving social and societal issues (Seanor et al., 2013) therefore understandings of social investment should be broad enough to reflect this 'fuzziness'. **Broadly speaking then, there are three elements to defining social investment, namely (1) it is a financial mechanism that (2) aims to have a measureable social impact (3) as well as creating a financial return.** The difference between social investment and traditional investment then, is the aim to have a measureable social impact. Furthermore, social investment then differs from grants, in that a financial return must be part of the agreement.

Definitions can limit access to social investment and therefore maintaining a broad perspective allows for more innovative projects to access programmes (adding limitations to access of funding was seen as a major restriction to innovation by interviewees). Semantics and the language used matters to how individuals and organisations associate. Intermediaries saw the process of bridging and ensuring clear communication between investors and investees as a vital role they fulfilled. **Finding a shared purpose through the social mission of the partnerships was key to overcoming cultural and language barriers between sectors**. One interviewee discussed how private investment institutions (such as banks or pension funds) usually wanted the social mission to relate to their core customer base and the interview with a private investor confirmed this. They mentioned interest in social investment that supported Fintech or healthy aging because it related to their core business and thus was aligned. Alignment of purpose also came down to "personal chemistry" (interviewee quote) and the connection individuals within partnerships had to the social mission of the partnership. This echoes findings from Roundy et al. (2017) who suggest that personal values that prioritise social change attract investors to social investment.

Connection between Social Investment and Academic Entrepreneurship

Academic entrepreneurship can contribute not only to economic outcomes but also to societal challenges (Franco-Leal, 2020). Studies of academic spinout organisations have emphasised their ability to create social innovations and create radical solutions to social problems (Franco-Leal, 2020). It has been suggested that academic entrepreneurs are more motivated by creating knowledge which tackles societal challenges, than they are by the economic income they might create through commercialisation of the knowledge (Fini et al, 2018). Academic entrepreneurs can be considered an attractive market for social investment because of three core factors:

1. The academic entrepreneurs' motivation to have impact
2. The prevalence of the impact agenda
3. Academics feeling the need to look for new sources of income as funding is seen as challenging to obtain (Fini et al., 2018; Franco-Leal, 2018)

Interviewees involved in university social investment discussed the privileged position universities had as a trusted institution for both socially driven organisations and government bodies. This could relate to universities' similarities with social investees: both are independent from government, provide a 'common good' (in the universities' case, access to learning and the progress of knowledge) and they are not corporate businesses. Interviewees discussed how universities are well placed to be social impact investors who focus on social impact above financial returns as

> *"[the] pressure for financial return isn't as strong [...] they're more interested in the social return, you still need to generate the money back and a little bit of profit, but we're not looking for 10% a year stuff" (Interviewee quote).*

Interviewees from Universities who were already involved in social investment saw involvement in social investment funds as not only a way of supporting academic spinouts, but also of supporting the local community around them too. Social investment funds were seen by interviewees already involved in university social investment projects as a particularly impactful way for universities to use their standing in the community. Arrangements such as building in staff time in kind were used to top up investments made and the staff time in turn offset the costs of impact measuring social investment funds. Social investment programmes associated with universities are starting to be seen as filling a particular gap in the market as one interviewee described it:

> *"And we have found that [...] University spinouts [...] are particularly disadvantaged in finding the right resources in the social investment market. Because what they do is they build up their proposition within the university. And when then when we spin them out there often at a much later stage than a typical social business would start." (Interviewee quote)*

Examples of how universities are involved in social investment can be found in Appendix 1 Case Study 2, which outlines the work of the Responsible Investment Network – Universities and Cambridge Social Ventures.

Furthermore, interviewees often compared and contrasted technology based innovation with 'people' or 'community' based innovations. Interviewees described that although they believed that technology had a role to play in addressing societal challenges, that services or 'people'/'community' style innovations were best placed to have social impact. Innovate UK and the Industrial Strategy were associated with technology innovation and therefore the investees in particular were unfamiliar with them as they were seen as not relevant to their work. It was felt by interviewees that ESRC's interest in social investment was a positive step as social scientists were perceived as interested in the 'people'/'community' based innovations. Interviewees suggested that large institutions showing an interest in social investment would lend legitimacy to social investment.

ENGAGEMENT AND OPERATIONS

Much of the interview content focused on the operational detail of social investment programmes. The social finance field is made up of the following set categories of actors (adapted from Mulgan, 2015):

PROVIDERS OF CAPITAL (INVESTORS) – the investors, whether individual or institutional, have investment agreements with fund managers or directly with investees which dictates expectations of the investment, which includes returns on investment (social and financial). This includes large charities and trusts who often also have funds to distribute. For example: Big Society Capital has money from Barclays and high net worth individuals that they then invest into other social investment managers such as Big Issue Invest. Investors and fund managers are often categorised as impact first or finance first, or social investors and traditional investors. This is depicted in the literature, and referred to in the interviews as a spectrum (Vert Asset Management 2017; Nicholls 2013; Glänzel & Scheuerle, 2016; Agrawal & Hockerts, 2019). One of the core differences between traditional investors and social investors is the expectations on returns; traditional investment programmes look for an exclusively financial return whereas social investors expect a financial return and a social impact. Other core differences between these investor types are discussed throughout the report and visualisations of the differences between impact first and finance first social investors can be found in the Deep Dive Report (in Appendix 2). **For a successful social investment programme, reflecting this full spectrum of investors is important.**

INTERMEDIARIES (FUND MANAGERS) – fund managers are often used to manage the investments, taking on day-to-day management of funds and managing the investee relationship. In some relationships social fund managers work with investees to embed social impact into their business through creating mission locks with them.

INVESTEES - The social economy in the UK does not have one set legal vehicle to use and organisations work across industries. The variety in legal structure allows flexibility and difference within the social economy. Some key legal structures are outlined below:

- **Company Limited by Guarantee** – a commonly used legal vehicle for charities and social enterprise. This legal structure does not allow a company to sell shares or redistribute profit outside of the organisation. It is often described as 'asset locked' meaning the assets of the company cannot leave the organisation. Companies limited by guarantee which want to operate as a social enterprise often have either charitable status (being registered with the charity commission) or community interest company (CIC) status (regulated by the CIC regulator). Having either of these status attached to a company also requires that they have an asset lock, and report on their social impact to a regulator.

- **Charitable Incorporated Organis**ation (CIO) /Scottish Charitable Incorporated Organisation (SCIO) – this type of organisation usually has a similar purpose to a company limited by guarantee, but this structure means the organisation only has to report to the charity regulator, unlike a company limited by guarantee with charitable status who would be required to file reports with both companies house and the charity regulator. These organisations are also asset locked.

- **Company limited by shares** – is a legal vehicle which is widely used. There is a growing number of social businesses using the company limited by share legal structure. This causes some criticism from the more 'traditional' social enterprise sector who strongly believe in the asset lock requirement. Being a company limited by shares and looking to operate in the social business sector often limits the organisation's ability to access grant funding, as many grant funders require an asset lock. Social investment, however, has a more flexible approach, allowing organisations to take equity investment, normally on the basis of having a mission lock, rather than an asset lock. Organisations such as Social Investment Scotland's SIS Ventures have created programmes to help social businesses legally constitute their missions through their articles of association; this process is described as a mission lock.

- **BCorps** – are organisations who have been through an independent certification process. The BCorp certification requires that the organisation build in a mission lock.

- **Co-operatives and Mutuals** – Co-operative Society Organisations (CSO), Community Benefit Societies (Bencoms) and Friendly Societies are typically described as cooperatives or mutuals and are regulated by the Financial Conduct Authority. Within these organisation types profit must be shared among members or under a community shares arrangement. This type of organisation is not as frequently discussed in interviews as the ones above but is still an important type of social economy organisation.

Investees again are often presented on a spectrum with private companies limited by shares on one side which is closer to that of a private business and organisations with asset locks (CICs, companies limited by guarantee and CIOs) closer to the traditional charity on the spectrum.

BENEFICIARIES – Beneficiaries of social impact projects come from many different backgrounds and can be as broad as the definitions of impact itself. For example, traditional investors targeted beneficiaries for their social impact projects that reflect their normal business customers e.g. banking investors seek to impact potential customers such as those who are excluded from banking through for example socially oriented FinTech.

Market for Social Investment

The market for social investment is broad. It can cover different sectors, organisational forms and size of organisations. However, despite the variety of established instruments and offerings (such as loans and equity deals of varying sizes), they do not meet the needs of all investees. **Interviewees often describe the need for early stage investment for unproven, experimental social innovation.** Despite a strong consensus towards the gap in the social investment market of early stage investment, there was not an agreement on the size of investment for this stage. Suggestions ranged from £500 to £750,000. However, figures between £15,000 and £250,000 were most often mentioned as the size of investment most needed[1]. At this stage, investment is acknowledged as high risk. Thus, interviewees advocated taking a portfolio approach, using blended finance, and being flexible with expectations and adjusting to challenges when they arise.

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1 This could be confirmed by further research into what investees would require.

Flexibility towards criteria of who meets the requirements to be funded is also important. This was discussed in particular in relation to the mission lock vs asset lock discussions. A key consideration when discussing the market for different forms of social investment is the legal entity of the organisation, as this has an impact on the type of social investment that can be offered. Social enterprises often take the legal forms of company limited by guarantee (44% of social enterprises in 2017 were company limited by guarantee according to Social Enterprise UK (2017a). This legal form is described as being 'asset locked' meaning that they cannot distribute profit to shareholders as all profits must be reinvested and used to achieve their social mission. This means that they cannot take on equity financing which has implications for any programme which aims to target social impact through social investment and suggests a requirement for flexibility around mechanisms. **A social investment partnerships approach should consider offering loan and equity options.**

Interviewees described how social investment and encouraging social impact in business goes beyond social enterprise. The legal structure of the business is important when thinking about social investment mechanisms. However, it was not thought by interviewees to be a good proxy for determining social impact. The interviewees discussed that, **in terms of impact it is important to look at how the social mission is embedded in the organisation, how they treat their staff, the supply chain(s) they have and the governance around ethical business than to focus on legal structures.** Social investors describe paying close attention to these factors, as well as how the business approaches equality, diversity and inclusion, and environmental impact. Interviewees described a frustration that social investors at times are too restrictive in determining the social missions they will fund. While defining broad themes was deemed useful, narrowing these too much is exclusionary and makes it difficult for innovative social businesses to apply. One interviewee described this as:

> *"Social impact investors triage themselves by sector, but they also have a theory of change of mission and purpose, which further triages the pipeline of things that they want to fund. So it's not just which sector you working in, you've got to be making your impact in a particular way. And then you've got to match against that impact. And so because of that, because the social investment market is, is much smaller than the mainstream investment market. And because the way in which social investors want to make that impact, their triage means that it really constraints deal flow." (Interviewee quote)*

Although the majority of interviewees discussed the need for early stage social investment, some interviewees also discussed a gap at the other end of the life cycle, needing a larger investment at a later stage. This was discussed by one social entrepreneur interviewee (who is involved in social investment committees also) who noted that her business had reached a limit on social investment but felt that traditional investors would still perceive the amount she requested as a small investment. She noted:

> *"we're at a point where we're not grown up enough to go with the big boys and pension funds, pension funds are not interested in us. But we're too big for the existing social entity. So you know, with 3 million from [social investor] was the biggest deal they've ever done. And [...] we're about to get another half a million from them. So that's three and a half million is the biggest deal they've ever done. And that can't be right. We've capped, we're now maxed out with most of the social investment players. But [...] we're not big enough to [...] comfortably have a 20 million pound chat with a pension fund. We're not big enough for that yet. [...] So that's me talking about two opposite ends of the spectrum, the middle, which is 250k up to 2 million. There's plenty of options for that." (Interviewee quote)*

This study suggests there is also a need to build the market for social investment, particularly aimed at social enterprises who lean towards the 'non-profit' mentality whose founders and/or boards can be reluctant to take on social investment, preferring to access grants. Roundy et al (2017) suggests social investment has to compete with grant finance as well as other sources of income which are available to all businesses meaning that social investment for typically grant dependent organisations will face some resistance

There are regional differences across the UK as to how the social economy (or the market for social investment) functions and what it is made up of. This has implications for the social investment sector. Interviewees based in England mentioned Scotland having a head start on the development and ecosystem of social investment. There was also a perception that there is a North/South divide within England where there is a sense that the south of England focuses on social businesses which take on social investment and have perhaps a more technology focus, to the North of England with a more traditional social enterprise basis which is more reliant on grant funding and service based. This was discussed by interviewees, and confirms theory proposed by Roundy (2020), research conducted by Hazenberg et al (2016) related to the difference in social enterprise ecosystems in the regions of the UK as well as regional reports conducted by Social Enterprise UK (Social Enterprise UK, 2019). To this end, a few interviewees mentioned taking a regional approach, to allow for that contextual difference, and to facilitate the government's levelling up agenda.

When is Social Investment Best Used?

Interviews highlighted the importance of not using social investment to replace grant funding. **Social investment is best used when a project has commercial and social impact potential** rather than to supplant, or turn services which require grant funding, into profit making enterprises. There are times where social investment options are not as favourable as more traditional investment offerings. For example**, interest rates on social investment loans are understood by interviewees to be higher than traditional business banking loans**. This finding was shared in the recent report on Social Investment published by Flip Finance (Daggers et al., 2021) who suggested that Big Society Capital's high requirements for returns set the tone for the rest of the sector. Social investors tend to calculate interest rates on a case by case basis whereas information on traditional bank loans are more fixed and standardised. Although the flexibility of a case by case approach allows for different options for investees it does not allow them the transparency of equal rates to their peers.

Social investment was described as best used for projects which align with a well-defined social mission. Specifying a social mission which unites the investor and investee strengthens the relationship between them, as it facilitates alignment of values (including that value is beyond the financial impact the organisation can have). Alignment of social mission was seen as a means of overcoming language and cultural barriers between sectors and could allow for strong partnerships to be created. Some interviewees described traditional investors as extracting wealth from social investees meaning that they distribute profits outside of the social economy to, for example, wealthy private individuals. However other interviewees, when asked if there would be a preference for social investors who recycled rather than extracted investment returns, said that investees were often more concerned with accessing funds than what would happen to the return afterwards. It was felt that social investment was advantageous for organisations with a specific social focus, as the relationship between investor and investee could be considered stronger because of the alignment on the idea of value (as being beyond the financial). Alignment of social mission was seen as a means of overcoming language and cultural barriers between sectors and could allow strong partnerships to be created. Alignment or misalignment was frequently discussed in interviews within different broad contexts. Alignment with societal challenges can be strategically important to attract investors and investees. Agrawal & Hockerts (2019) find that the specialisation of impact investors towards social and financial value increased the likelihood of alignment between investor and investee and subsequently a more successful relationship.

In the UK there is no single agreed approach to identifying or framing the focus of social, societal and or environmental impacts. While not problematic per se, an agreed approach could help bring greater focus and clarity to the challenges being addressed. This question is one that exists across Government, with different departments and bodies taking different approaches. The UN's Sustainable Development Goals (SDGs) provide one such framework which was frequently mentioned by interviewees, and there was a perception that the UK was behind other countries. Moving forwards, there is a need for greater clarity in the focus of social investment in addressing social, societal and or environmental challenges if it is to get traction with investors and investees.

Equality, Diversity and Inclusion

There is an opportunity to utilise social investment as a tool to promote equality, diversity and inclusion in investment portfolios. Promoting inclusion in investment portfolios can not only encourage diversity in social impact businesses which in turn can create diversity of impact, creating different approaches to societal challenges. Social investment can be flexible for diverse founders and some interviewees suggested that women tended to found socially driven businesses. This is supported by Social Enterprise UK (2017b) who suggest that 21% of social enterprises have a BAME leader and 49% have a woman leading (compared to 5% BAME led private sector SMEs (UK Government, 2019) and 20% women led private SMEs (Carter et al., 2013)). However, the same figures also show that women and BAME leaders tend to run small social enterprises, and larger social enterprises are more likely to be led by white males. (Social Enterprise UK, 2017b). This could be related to lack of access to finance for growth as these groups have traditionally found it difficult to access finance. Furthermore, one interview highlighted that social enterprise is often considered a middle class activity as the founder has to take risk to start up, and what impact does this have on 'left behind' areas and the levelling up agenda.

While woman and BAME leaders are over represented in the social enterprise and social businesses compared to SMEs, there are still barriers to access to finance for social businesses. Often social investment requires a particular legal vehicle (which includes an asset lock). One social investor mentioned that their research had suggested that restricting access to funds to organisations with an asset lock disadvantaged founders from diverse backgrounds. They noted that they had found that founders with diverse backgrounds were more likely to set up companies limited by shares than companies limited by guarantee. Ways of building in diversity to the process of social investment was highlighted as key. One interviewee noted that one organisation in the USA had a programme which was:

> *" So I think it's taking those kind of new and innovative ideas about how to have diversity in the pipeline, from the very beginning, you are actually providing funding to people that find it much more difficult to access, you do have a social impact. And their peers agree with that." (Interviewee quote)*

One way to encourage diversity in social investment applications is to consider using a peer review model where social businesses would be involved in a guiding committee which could also review funding applications, in a similar style to academic funding review processes.

Other Support to realise impact

There is a need for comprehensive soft (or wraparound) support to scale the impact of social investments. Interviewees discussed that structured training, or enforced learning opportunities were less helpful than tailored, one to one support. **Peer support and peer to peer networking were seen as the most important part of additional support for social investment** by social investees and investors. The advantage of creating a specialised social investment programme was seen to be the opportunity to create a cohort who emphasise social impact. There was particular value seen in creating peer cohorts around specific challenges, themes or missions as this allows access to specialised tacit knowledge based on shared interests.

Alternative Instruments

Social investment was discussed by some interviewees as not being innovative enough with the instruments used, relying on models transferred directly from commercial venturing. Interviewees (typically investees and support organisations rather than investors) mentioned the following as alternative financial instruments that new social investment programmes could explore:

- **Revenue based financing** - where the investor takes a percentage of the investees' income until the repayment amount has been returned. Unlike with equity financing, the investor does not have ownership of part of the business, and unlike loan financing, there is no interest on the outstanding balance and the payments are not set as an amount, rather as a portion of income. This is considered a very new form of financial instrument and is similar to quasi-equity.

- **Flexible exit instruments** - such as redeemable equity, whereby a company can buy back shares on exit. This is particularly attractive to social businesses because of the risk to the social impact of exits using traditional models (GIIN).

- **Convertible loans and grants** – allow for the investment to be changed at an agreed upon date. A recent example being the UK government's Future's Fund which was designed as a COVID response fund. It allowed loans to be converted into equity (British Business Bank). Convertible grants are similar in that the grant making body reserves the right to convert the grant into a loan or equity if the company invested in becomes successful (NESTA, 2018).

- **Community shares** - relates to cooperatives business models, who can take on withdrawable share capital and is often used to raise money to buy community assets such as local pubs or finance community energy projects. Community shares do not increase in value, but can decrease in value (Community Shares UK). Community shares projects usually attract small investments from community members. Esmee Fairbairn and the Resonance have underwritten community share raises to support use of this instrument (see Appendix 1, Case Study 3).

- **Blended returns** - where annual financial returns are fixed at a set rate, but adjusted if the social impact is achieved or surpassed

Alternative financial instruments were seen as a means of innovating within the financial system to firstly establish mechanisms of finance which were more suited to social investment, rather than taking existing mechanism and applying them to social investment, an issue identified in the academic literature (Mulgan, 2015). They were also discussed as a way of creating deviations from established pathways and routes. These established routes were described as the 'grant funded' route and the 'venture capital' route. Therefore for example, businesses are set on one established route when they take traditional investment and it is worth further research to explore if alternative mechanisms facilitate switching tracks.

Risk & Mitigation

Risk and risk management is an important part of social investment. The perception is that social investments are riskier, appear riskier to traditional investors, or have different risks to traditional investment. **Risks could generally be categorised along the lines of the two outcomes of social investment: financial return and social impact. Awareness of these risks and how they are perceived is important for those involved in social investment, particularly intermediaries who can act towards derisking social investment (e.g. through grant matching and building reputations of investees).** One interviewee discussed that because of the social impact aspect of the social investment, there were different risks around working ethically with vulnerable populations which must be considered. This could be overcome through working in partnership with stakeholders (or fund managers) who are experienced in the particular social issue. The risks to the ability to generate financial returns for investors is more acute and challenging. There is a lively debate on the role of social investment and the levels of risk it should be comfortable to take which is covered well by Daggers et al (2021). They outline that some social investors think that social investment should only be for high risk social projects, whereas others within the social economy believe that social finance should provide access to finance for social economy organisations. Under this category there is criticism across both social and 'traditional' investors about their willingness to take on risk. One interviewee described how large traditional investors were more risk averse when considering social investment because they do not fully understand the market. However, the same criticism was levelled at social investors by other interviewees and is a core finding of the Adebowale Commission on Social Enterprise undertaken on behalf of Social Enterprise UK (Patton, 2021)

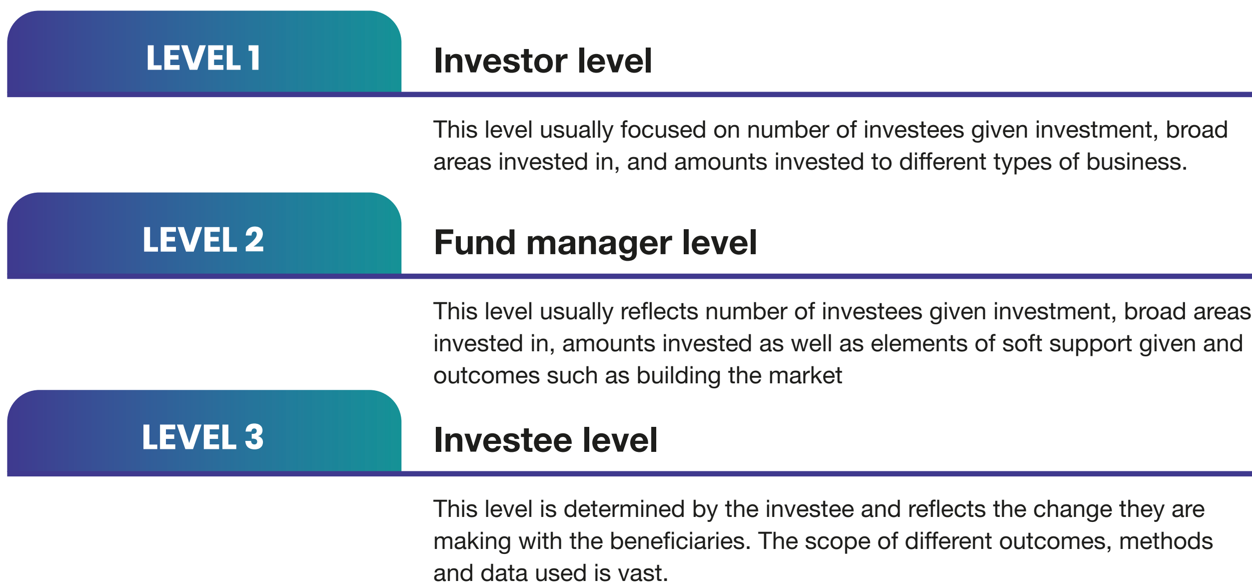
A portfolio approach to social investment is a means of managing risk in social investment. For those involved in running social investment funds, this was described as the main way they ensure they have funds for the future. They acknowledge that some projects will not provide a return on investment but look to others to make up that shortfall. For example, one social investment fund interviewee described mixing funds across more and less risky sectors. The housing sector as a stable and low risk investment with the potential to have financial returns but also achieve social impact, versus investing in new social ventures, which were seen as more risky. However, some interviewees took a dim view of this, saying that social investment should not be based on a traditional VC model where investors accept a set number of projects will fail, but rather should try to ensure more social projects succeed. **Using blended finance and in particular, blending grants with equity/loan finance was seen as a positive way both to encourage investors and to mitigate risk for investors.** Case Study 4 in Appendix 1 on the Healthy Aging Investment Accelerator describes the use of blended finance to achieve a targeted social mission.

OUTCOMES & IMPACTS

Impact measurement is a complex topic, to which there is no established 'one size fits all' solution. It is a lively area of academic research where there remains a lack of consensus (see for example a recent review by Rawhauster et al, 2019). Impact measurement is more than "are you profitable after 3 years" (Interviewee quote). Social investors and investees alike are aware of the burden that social impact measurement can place on investee organisations and thus are usually reluctant to be prescriptive about how impact is measured by investees. Interviewees advocated alignment with a broad framework or allowing investees to suggest their own theory of change, so that the people who understood the business best were able to say what the impact of the business will be or has been. There was a feeling that at times that social investors, because of the dual focus of economic and social, do not balance the application and reporting requirements but rather expect double the amount from their investees. Recipients of social investment are required to justify and report on their economic performance and social impact creating an extra workload that interviewees felt was not recognised at times by social investors.

There are distinct levels to impact measurement in social investment. This is demonstrated in figure 1. The breadth of different ways of measuring investee impact means that it can be challenging to aggregate impact upwards to the fund manager and investor levels. Investees dislike investors 'claiming' their impact outcomes, as there is an issue of attribution. One investor discussed that impact measurement makes impact investing more expensive than traditional investing, saying "it costs like an extra 2% in the funds to be able to track the impact" (Interviewee quote). While a breakdown of this extra cost was not shared, interviews suggested that costs are typically associated with staff time and resource to gather data, and pay for external evaluations.

Figure 1 Levels of Evidencing Impact



The interviews highlighted the best way of conducting social investment partnerships is to establish early, in conversation with the investee, what constitutes 'shared success' for the partnership. This can be aligned to broad missions that the investor has, as this helps build expertise in a specific area for the investors. As one interviewee said: "I think the benefit of specific outcomes is that it should drive expertise in the fund managers in ways that general ones don't because fund managers, generally speaking, or investors have to be experts in the deal." (Interviewee quote). While having this preliminary discussion it is important to also consider what is achievable within the partners own set timescales. Interviewees mentioned that often cross sectorial (public/private/third) partnerships clashed over the timescales of when something needed to be achieved. This was normally discussed around **innovative companies wanting to move fast with projects but being slowed down by the bureaucracy of public sector partners and public sector partners looking to realise social benefits faster than the social innovator could achieve them.** This was noted as one of the big negatives of public sector finance opportunities. One interviewee noted that social investees often are slower to achieve financial and impact outcomes suggesting that 7-10 years is more realistic than a 3 year funding cycle. Therefore patient capital is important.

The metrics of impact measurement set out by any large institution typically sets a tone and direction which has a large influence on what social impact should be achieved, and when deciding on what impact they hope to achieve, organisations such as UKRI must be aware of this power dynamic.

Impact of social investment

Benefits of social investments were discussed by interviewees who described a range of positive results of social investment from different perspectives:

- **Investor benefits:** The institutional corporate investor interviewed mentioned a reputational advantage to engaging with social investment programmes. Social investors discussed how *"government investment, [...] can be a great thing. But actually, if you get social investment, right, you invest 10 million in a fund, and five or 10 years later, that's created all these impacts. And actually, it's created 20 million fund [...]. So your ability to grow the money supply and to therefore grow the impact is massive." (Interviewee quote)*

- **Investee benefits:** Social investment provides access to capital for projects that normally have restricted funding. Targeting investment towards social impact also brings together groups of likeminded people to tackle society's big challenges which was seen as an advantage.

- **Societal benefits:** Interviewees also felt that the potential to unlock more social impact was a considerable benefit of social investment, and though they commented that this was perhaps "sounded silly" (Interviewee quote) or obvious, it was considered central to the reason for social investment.

Interviewees saw this as the natural direction that investment should be taking, due to the changes of increased social awareness, and increasing inequalities. A large organisation such as ESRC and/or Innovate UK working with the social investment sector was received positively, with existing social investors noting that the addition would add legitimacy to the field of social investment and that additional funds to support the social investment market would be good.

Impact of COVID-19

COVID-19 was described as having a significant impact on new programme launches and the pipelines of recently initiated programmes as these have seen delays and slow uptake. However, existing social investors described how COVID-19 had had a positive impact on the sector's ability to collaborate. The COVID-19 support funds required some level of collaboration across the sector and thus put pressure on organisations to work together. There is a sense that there is a renewed focus on social impact in a post COVID world, and that simultaneously public spending associated with grants was going to retract and this would have an effect on funding social projects but mean increased demand for social investment. This on top of growing inequalities highlighted by the pandemic, meant that interviewees highlighted social investment as one tool which would help address these societal issues and is particularly needed at the moment.

LIMITATIONS & FUTURE RESEARCH

This project was a broad exercise exploring the current social investment market. Thus the scope of this report is broad, and therefore has touched on many areas briefly rather than in depth.

One key limitation of the empirical side of the research is that the research focused on investor perspectives in particular, therefore there were few investee and potential investee interviews (1 of each). Investors themselves said:

> *"And I think what they [Innovate UK and ESRC] should do is take a really good selection of these enterprises, businesses and charities and community organisations and say, What do you need?" (Interviewee quote)*

OPPORTUNITIES FOR FURTHER DEVELOPMENT

- In supporting Social Investment Partnerships, there is merit in the ESRC and Innovate UK (as well as UKRI more widely) identifying the high-level priorities in order to give a focus to prospective applicants. Given the emphasis on sustainability in policy and public interest, this could be the focus of Social Investment Partnerships aligned to the SDGs framework.

- Any support for future Social Investment Partnerships programmes needs to have a clear social, societal and or environmental challenge or need. This will maximise the engagement of prospective investee groups, and increase the likely impact of the Social Investment Partnerships programme. The societal or environmental challenge or need, does not have to supersede economic impacts, but must be explicitly stated and measured to be considered social investment.

- There are opportunities to promote equality, diversity and inclusion through Social Investment Partnerships programmes. There is scope to engage a broader range of prospective investee groups which are likely to go beyond those attracting investment from traditional sources.

- Any future plans for Social Investment Partnerships that seek to support social enterprise or social ventures need to ensure direct consultation with a cohort of social entrepreneurs and social investors, and have them represented on a steering/advisory group.

- There is an opportunity as a part of any future Social Investment Partnerships to promote partnership and collaboration with existing infrastructures and stakeholders to maximise the value added though projects (i.e. social entrepreneurs, universities, local authorities, trusts, charities and social investment management firms).

- The focus on realising economic return, financial instruments and exit strategies need to be flexible in investment accelerators to allow impact businesses to gain the most from investment.

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APPENDIX 1: CASE STUDIES

Case Study 1: Peterborough Prison Social Impact Bond

Social impact bonds are vehicles which often employ social investment as part of the financial arrangements. Social impact bonds are payment by results programmes which allow investment into social programmes, delivered by a third sector organisations, funded by an investor and repayments made when social impact is deemed achieved by a public sector partner. The first social impact bond was founded in the UK to reduce reoffending rates at Peterborough Prison in 2010. It was a pilot programme which was to last 6 years. The project had a mix of grant and investment funding. The Ministry of Justice and the Big Lottery Fund agreed to pay a return to the investors if the partnership achieved its targets to reduce reoffending. The partnership was tasked with reducing reoffending by 7.5% across three cohorts totalling 3,000 individuals, or 10%+ of one cohort (Harvie & Ogman, 2019). They achieved a total of 9%, on the first two cohorts. Investors were repaid in full with a 3% per annum return (Ainsworth, 2017).

The pilot programme conducted at Peterborough Prison was cut short after year 2 as a national policy change superseded it (Harvie & Ogman, 2019). The new national programme called Transforming Rehabilitation was based on some of the learning from the Peterborough Social Impact Bond, but then was criticised for returning to provision through large private providers (Ainsworth, 2017). Despite the investment being repaid, the success of the Peterborough Prison SIB is contested. The SIB mechanism was designed to move the risk from public funding to private investment, so if the SIB did not achieve results the public sector would not have paid for an ineffective programme (Harvie & Ogman, 2019). However, the financial results of social impact bonds can be described as “only temporarily bring in new resources to the social sector; in the long term they will mostly absorb public money in a zero sum game” (Harvie & Ogman, 2019, p.993).

Criticisms of the SIB included that it was seen as overly complicated, bureaucratic, and expensive (Ainsworth, 2017). SIB also face a critique which is common to all types of social finance; that it is the commodification of social problems and citizens (Ainsworth, 2017; Roy et al., 2018) and changes the relationship between the social service and the user, as the user is no longer the prime stakeholder, the investor is (Roy et al., 2018). SIBs are an area of the social investment market which is often studied, with the Peterborough Prison Social Impact Bond featuring heavily in many texts of social investment (Nicholls, 2013). One interviewee described how the academic field was much more developed in social impact bonds than in social investments. The interviewee felt that this representation was not representative of practice. A comparison of case studies is provided in table 2.

Case Study 2: Responsible Investment Network - Universities

Members of the Responsible Investment Network – Universities (RINU) use their investments to foster social and responsible innovation. The network is supported by Big Society Capital (the UK's social investment bank), Share Action (a sustainable investment charity) and the Student Organising for Sustainability United Kingdom (National Union of Students sustainability charity). In 2020 the Students Organising for Sustainability United Kingdom gathered details of universities investment and investment policies (SOS, 2020). Three of the founding members of RINU (Cambridge, Oxford and Edinburgh Universities) have investment budgets of £7,849m (SOS, 2020). Other younger universities are also involved in social investment; the University of Northampton, for example, has a total of £21.25m investment under management and £1.25m is currently invested in social impact investments (Big Society Capital).

Cambridge Social Ventures - is a dedicated programme of support for social innovators run by Judge Business School. While Cambridge Social Ventures is open to a variety of businesses who can access training and soft support, they also run a fund specifically for spinout from Cambridge University research or alumni. £20,000 is invested in up to five social impact businesses a year, with returns reinvested in future social ventures (Judge Business School).

Case Study 3: Esmee Fairbairn Social Investment

Esmee Fairbairn Foundation is one of the UK's largest independent funders, founded in 1961 (Esmee Fairbairn). They are primarily a grant giving organisation. In 1997 Esmee Fairbairn made their first social investment, making them a pioneer in the field. Currently they have a £45 million social investment fund which is constituted of returns from previous investments (Esmee Fairbairn).

Partnership with Resonance: Esmee Fairbairn are invested in Resonance who are an investment intermediary. Esmee Fairbairn during their relationship with Resonance have utilised and supported different social investment mechanism such as underwriting community shares, repayable grants, match funding. The investments made by Esmee Fairbairn has managed to leverage further investment through social investment tax relief, community share raises and raises from institutional investors (Esmee Fairbairn).

Case Study 4: Healthy Ageing Investment Accelerator

The Healthy Ageing Investment Accelerator is a programme of investment available to businesses who aim to tackle issues associated with ageing. The programme comprises a combination of grants and private equity finance. Grants are provided by Innovate UK and private investment through such partners as Barclays Ventures, Northstar Ventures and Legal and General. The programme recruited investment partners in 2019 and began funding in March 2020. Investors could apply for a grant allocation from Innovate of between £1million and £6million. Investors were required to invest a sum equal to the grant funding, showing an ability to invest in follow-on funding of 3 times the grant amount by 2025. Partners were not only required to show financial ability to contribute but were discussed as being able to "demonstrate ability to add value beyond their investment", "commit to helping the company grow and scale" and show expertise (UK Government).

Investor partners then identified SMEs and social enterprises to carry out innovative R&D in the field of Healthy Ageing. The competition for investee partners was invitation only. Projects were described as lasting 2 years (2020-2022). Costs of projects (funding and investment) are to be between £100,000 and £1.5million (UK Government). The first round of investee recruitment closed on the 18th of November this year which a second cohort immediately opened and is currently open. There are currently 5 more cohort dates listed (KTN, 2020). The Healthy Ageing Investment Accelerator is part of a three pronged approach to the Healthy Ageing Challenge Investments:

1. Research
2. Investment Accelerator
3. Trailblazers

The rationale behind the investment accelerator approach in general is that evidence suggests that start-ups who have a combination of grant funding and equity investments perform better than those who received either grant funding alone, or equity investment alone (KTN, 2020). Investors are able to bring equity capital, they validate the quality of the company (rather than project), and they have influence, good governance and access to markets (KTN 2020). Private equity is described as reducing the risk for public funders and investors and help to maximise impact

Project Name	Investment mechanism	Lead partner	Partners	Impact Goals	Approach	Size of investment
Peterborough Prison Social Impact Bond	Social Impact Bond	One Service – a consortium of third sector service providers	Providers of capital Esmee Fairbairn Foundation Monument Trust Big Lottery Fund Government Sponsor Ministry of Justice	To reduce reoffending rates	Payment by results	£5m
Responsible Investment Network - Universities	Loans Equity	Big Society Capital ShareAction	University of Cambridge University of Edinburgh Imperial College London University of Leeds University of Aberdeen Jesus College, Cambridge St John's College, Cambridge Trinity College, Cambridge St Anne's College, Oxford	The network supports universities to network, learn, advocate and engage on responsible investment strategies	Portfolio	Total investment budget University of Edinburgh – £820m University of Oxford – £3,729m University of Cambridge - £3,300m
Esmee Fairbairn Foundation	Social Impact bond (1) Equity (8) Secured loan (14) Unsecured loans (29) Quasi Equity (6) Grant (13) Arts Transfer Facility (5) Land Purchase Facility (6)	N/A	Example: Resonance Foundation	1. Impact-first direct investment 2. Influencing the social investment market 3. Learning and sharing	Portfolio, flexible	£100k-£2m (average £437k)
Healthy Aging Investment Accelerator	Blended grant and equity	Innovate UK	Barclays Investment Bank Legal and General Northstar Ventures	everyone to remain active, productive, independent and socially connected across generations for as long as possible to narrow the gap between the experiences of the richest and poorest.	Portfolio	£100,000 and £1.5million

Table 2 Summary of Case Studies

APPENDIX 2: DEEP DIVE LITERATURE REVIEW

Introduction

This document provides a broad overview of the academic and sector based evidence on the topic of social investment partnerships. It outlines the findings from an initial deep dive evidence review conducted between October 2020-January 2021. It provides insights into the field of social investment, by providing definitional clarity on the terms used, outlining the difference between social investment and traditional investment models, highlighting what attracts investors to social investment, and considering what can be learned from existing studies of social investments and known challenges.

Access to finance is a barrier to the growth of organisations aiming to maximise their social impact (Glänzel & Scheuerle, 2016). To provide flexible financing which is not linked to specific programmes (which is often the case with grants), impact investing has become a field of attention for policy makers, funders, social economy organisations and academics (Glänzel & Scheuerle, 2016). Simultaneously, there is growing interest from those who own capital in using their resources to create social value as well as financial returns (Nicholls, 2013). This has led to the development of a series of interrelated concepts, the boundaries of which are contested. For the purpose of this project the following terms will be used as defined below:

- Social finance – is an umbrella term used to describe ways in which capital is used to fund social and environmental outcomes (Nicholls, 2013; Glänzel & Scheuerle, 2016). It covers a full range of mechanisms including social investment – covering investments focused purely on societal outcomes (philanthropic grants, public grants), blended models (impact investing, social impact bonds) to traditional investment (with a financial focus) in social ventures.

- Social investment – is a term used to describe capital investments in organisations who aim to have social outcomes. This would cover both impact first and finance first style investments using loans and equity. Although academics in public policy may also use this term to describe an approach to social welfare reform (Harvie & Ogman, 2019) we use social investment to mean the use of capital investment techniques in projects which have targeted and measurable societal as well as economic value (OECD, 2019). Social investment is often confused with socially responsible investment which focuses the use of rankings and metrics on a portfolio approach to investment in the stock market (Roundy et al., 2017, Widyawai, 2018).

- Impact investment – is a narrower term used to describe the use of venture capital mechanisms (equity, debt or mezzanine finance) in social organisations which put social value created over financial returns, (Glänzel & Scheuerle, 2016; Agrawal & Hockerts, 2019).

The OECD (2019) has noted that social investment can contribute to achieving the SDGs as well as stimulating new approaches to grand societal challenges.

There are four main components to the social finance field which are combined to create social investments:

- “Providers of capital motivated to achieve social (and sometimes financial) returns
- Users of capital, who can deploy it in ways that will achieve social impacts and, sometimes, financial revenues
- Intermediaries who connect providers and users, and may in addition be able to improve the effectiveness with which capital can be used (through knowledge, skills, networks)
- Environment of law, regulation, tax incentives that enables or prevents the alignment of the motivations and rewards of each group” (Mulgan, 2015, p.48)

Recent research on social investment discuss its relationship with social entrepreneurship (Glänzel & Scheuerle, 2016; Lall, 2018; Phillips & Johnson, 2019; Schrötgens & Boenigk, 2017), Islamic finance (Kappen et al., 2019), network roles (Michelucci, 2017), metrics and measurement (Mitchell, 2017), poverty (Rosemann, 2019) as well as exploring the motivations of social investors (Roundy et al., 2017).

Investment instruments are often mapped on a spectrum from value driven to values driven (Vert Asset Management, 2017) or finance first to impact first (Nicholls 2013; Glänzel & Scheuerle, 2016) – see figure 1 for some examples. On the far side of impact first philanthropic grant making and on the opposing side is traditional forms of investment which aim to maximise return on investment (Argrawal & Hockerts, 2019). Traditional forms of investment may have a societal or social impact, however, the difference between the two forms of investment lies in the metrics of success used formally for each type. Social investments require measurable social outcomes whereas a traditional investment typically measures only financial return on investment (Roundy et al., 2017). These illustrative diagrams (shown in figure 1) and definitions are useful conceptually, however, in practice, organisations often use and blend different forms of finance across this spectrum even within one project (Nicholls, 2013) as can be seen in the example below.

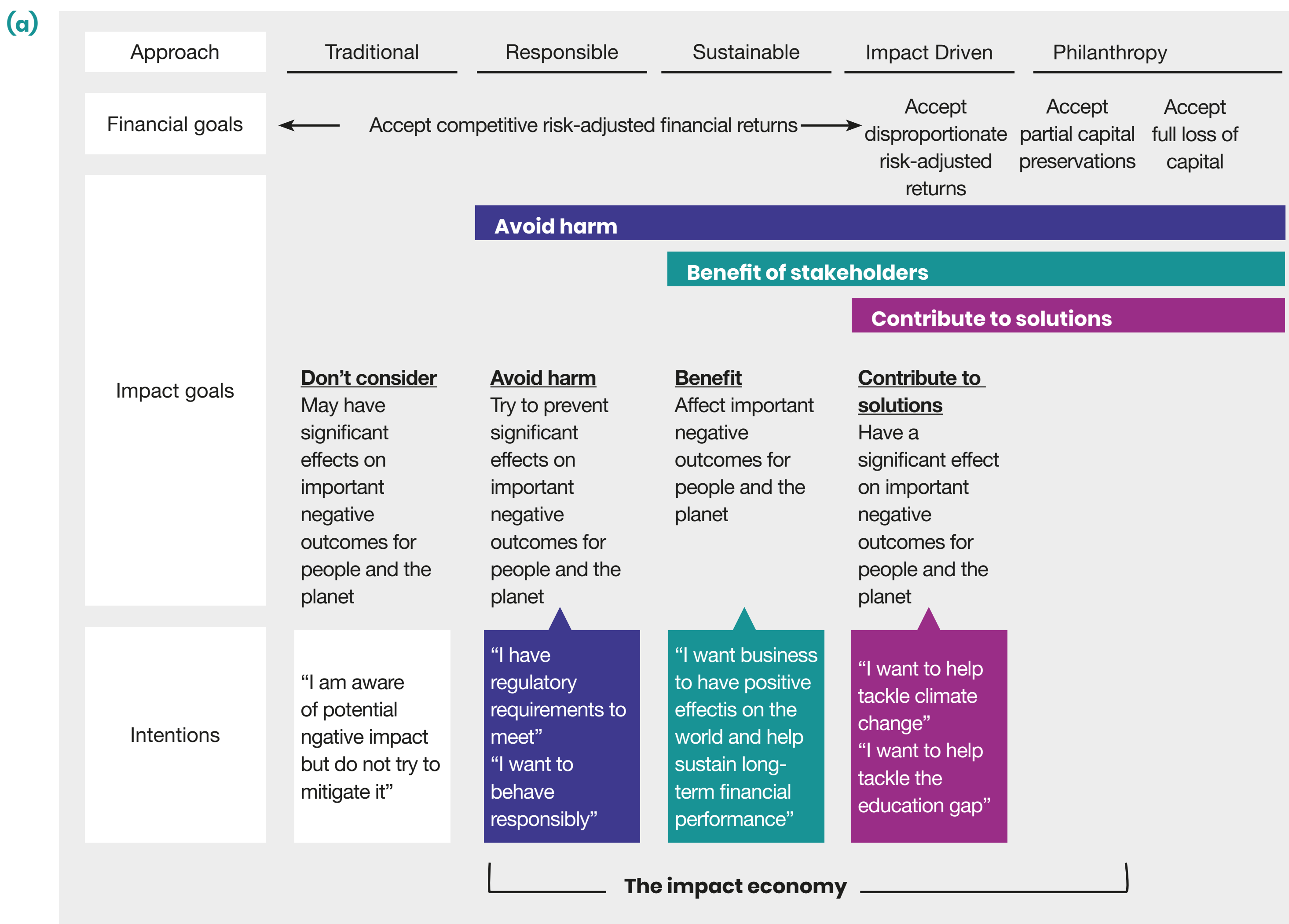
EXAMPLE

Hackney Community Transport took on a combination of social loans, alongside more traditional loans from five providers raising a total of £4,145,000 with 46% coming from social loans and 54% from fixed rate loans (Nicholls, 2013). The social loans were provided on a quasi-equity arrangement where “investors received a 1 per cent share of every £1 million increase in revenues generated over an agreed threshold” (Nicholls, 2013, p.179). The arrangement was called a social loan to overcome legal issues with equity investment in registered charities (Nicholls, 2013)

As the models in Figure 1 show, one of the core differences between traditional investment programmes and social investments is the expectations on returns. Traditional social organisations such as charities and social enterprises are risk averse. The State of Social Enterprise Report published by Social Enterprise UK noted that the most common type of finance applied for was grant funding (82%) and the second most common source was loan finance (24%). Over half of those who had applied for a loan said that it was unsecured (52%). In 2017, 5% of social enterprises surveyed by Social Enterprise UK had applied for equity finance. Low financial returns are more attractive and more in line with the small profit these organisations tend to make yet the GIIN (2020) report suggests that most impact investors seek market rate financial returns. Social ventures have more channels for raising investment than traditional businesses as they are able to apply to a wider range of grant funding than traditional businesses (Roundy et al., 2017). However, venture capital investing has been described as attractive in particular to academic spinouts interested in social innovation as it is seen as a means of creating legitimacy, showing managerial competency and leads to market credibility (Franco-Leal, 2020). There is a perception from those involved in social ventures that providing equity could lead to undermining of the social value they aim to create but Roundy et al (2017) states that because impact investors value both social and financial returns they are unlikely to do so. This suggests that there may be a need to support market development for social investment.

Figure 1 Examples of Investment Models (Sources: (a) Global Steering Group for Impact Investment, 2019, p.4; (b) Bridgespan Group, 2018; (c) Vert Asset Management, 2017, p.3)

(a)



(b)

EXPECTED FINANCIAL RETURN

MARKET RATE

BELOW MARKET RATE

PARTIAL CAPITAL RECOVERY

COMPLETE LOSS OF CAPITAL

–$

Financially Motivated Investment

Socially responsible investments

(e.g. focused on environmental, social justice or corporate governance (ESG) issues or employment)

Intentional, Market Rate, Impact Investments

Below Market Rate Impact Investments

Social Impact Bonds & Devel-opment Impact Bonds

Evidence-Based Impact Invest-ments

Traditional Philanthropic Grantmaking

Evidence-Based Grantmaking

(eg Robin Hood Foundation)

NONE

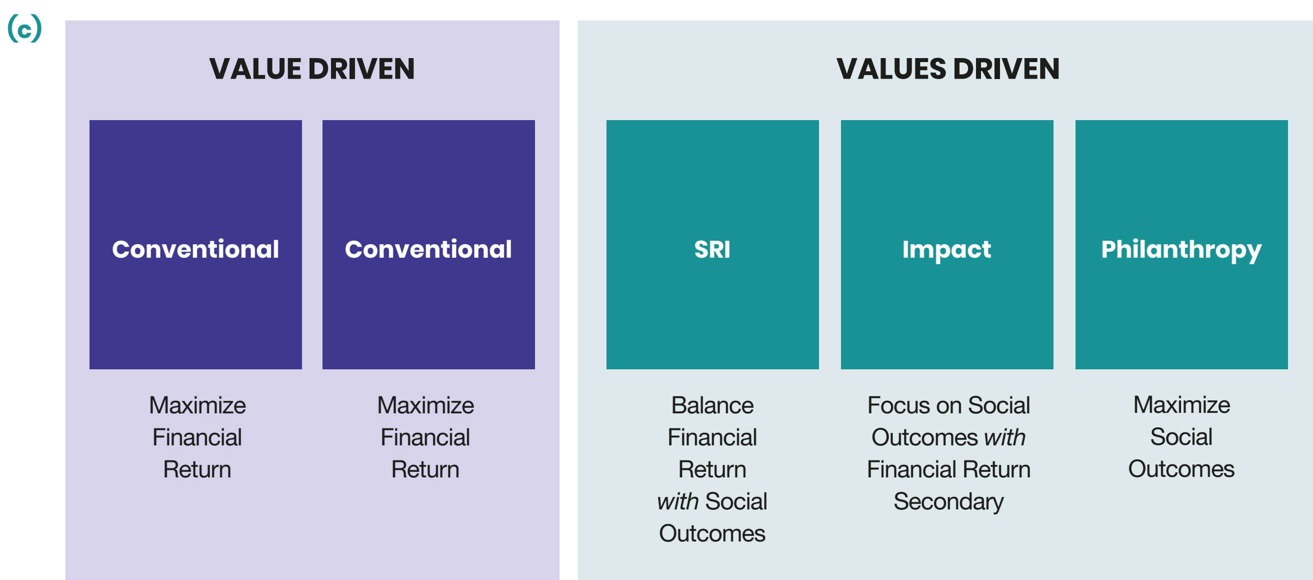
PASSIVE

INTENTIONAL

EVIDENCE-BASED

APPROACH TO IMPACT

(c)



Social investment, social enterprise and institutional logics

Social investment and social enterprise/entrepreneurship are closely linked both in practice and conceptually (Roundy et al., 2017). Often social enterprises are the recipients of social investment. Theories of social innovation allow the idea that social value is created outside of social enterprise and the non-profit sector (Franco-Leal, 2020), therefore social investment is not exclusively used to fund social enterprise or the non-profit sector.

Institutions and institutional logics are frequently used as a lens for exploring social investment and social enterprise, identifying the competing logics present as social and commercial (Glänzel & Scheuerle, 2016; Agrawal & Hockerts, 2019; Hehenberger et al., 2019; Lall 2019). Agrawal & Hockerts (2019) focuses on the relationship between investors and investees and the role of hybrid institutional logics in facilitating their relationships. Although investees and investors face the same competing logics, they have different sources of legitimacy. Agrawal & Hockerts (2019) find that successful relationships can be built between investors and investees through shared appreciation of the social mission (Agrawal & Hockerts, 2019). Lall (2019) suggests that relationships between investors and investees be built through impact measurement which creates legitimacy for the investees with the investors and facilitates self-reflection on the part of the investees. Similarly, Agrawal & Hockert (2019) find that regular social impact measurement increases the likelihood of a successful investor-investee relationship and better performance over the period of the investment.

Commercialisation Agenda and Academic Entrepreneurship

Academic entrepreneurship can contribute not only to economic outcomes but also to societal challenges (Franco-Leal, 2020). Studies of academic spinout organisations have emphasised their ability to create social innovations and create radical solutions to social problems (Franco-Leal, 2020). Furthermore it has been suggested that academic entrepreneurs are more motivated by creating knowledge which tackles societal challenges, than they are by the economic income they might create through commercialisation of the knowledge (Fini et al, 2018). The combination of internal motivation to have impact, funder requirements to adhere to the impact agenda and the need to look for new sources of income as funding is scarce (Fini et al., 2018; Franco-Leal, 2018) means that academic entrepreneurs are an attractive market for social investment.

Table 1 Sub types of investors (adapted from GIIN 2020)

Sub group of investors	% of survey sample
Developed market focused investors	48%
Emerging market focused investors	43%
Private Equity focused investors	28%
Private Debt focused investors	22%
Market rate investors	67%
Below-market rate investors	33%

What makes Social Investment Partnerships attractive to investors?

To understand what attracts investors to social investment it is helpful to understand who social investors are. The Global Impact Investment Network (GIIN) releases an annual impact investor survey report, and in 2020 their report is based on responses from 300 impact investors. This covers asset managers for-profit, asset managers not-for-profit, development finance institutions (government-backed institutions investing in the private sector), diversified financial institutions (including banks and credit union), family offices, foundations, insurance companies and pension funds (GIIN, 2020). According to GIIN (2020) half of the private debt focused investors are below market investor and 80% of private equity focused investors are market rate investors. 61% of investors surveyed by GIIN (2020) only made impact investments, the remaining 39% made both traditional and impact investments. This suggests that some investors could be described as purely interested in impact investment, while others are social investors interested in both financial and social value creation.

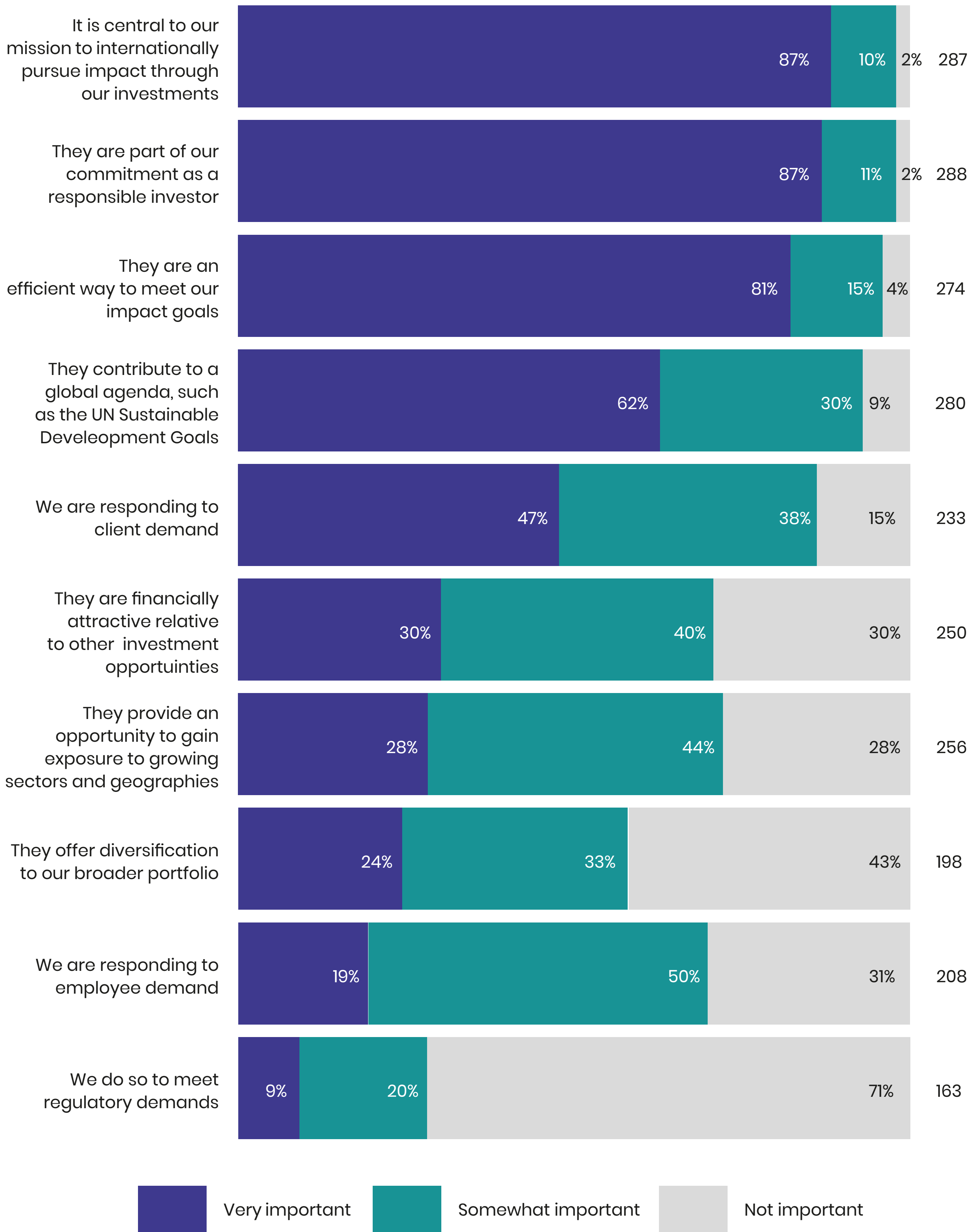
Roundy et al (2017) indicates that impact investors represent a distinct subgroup of investors who are different from other types of investors. Roundy et al.'s (2017) article is one of the few academic studies of impact investors, it notes that impact investors stipulate that impact investments must have financial returns and create social value. If an investment exclusively focuses on one or the other, the impact investors do not consider it an impact investment (Roundy et al., 2017). The investors disagreed as to the balance of social value and financial returns they expected which is echoed in the GIIN (2020) survey which shows that 67% of impact investors expect market rate returns whereas 33% expect below market rate returns.

Roundy et al (2017) explore the personal motivations of impact investors finding that the key motivations were:

- Personal values that prioritise social change
- Belief that market based solutions are effective in tackling social problems
- Belief that impact investment is more flexible than philanthropic grants
- Slow money approach to investment (taking a longer viewpoint of success) (Roundy et al., 2017).

The GIIN (2020) survey respondents outlined the motivations shown in figure 2.

Figure 2 Motivations for Impact Investing Organisations (GIIN, 2020, p.4)



Roundy et al (2017) found that often social investors are focused more on the developing world, this again is echoed in the GIIN (2020) survey. Impact investors evaluate businesses using methods such as looking at the strength of the management team, the opportunities to scale which are common across investment types, however they also look at potential to produce social return on investment which is unique to social investing. Potential investees must be able to communicate both their social and financial value to potential social investment investors (Roundy et al., 2017; Agrawal & Hockerts, 2019).

Challenges for social investment partnerships

Glänzel & Scheuerle (2016) found 8 critical problem areas for social impact investing in Germany, from both the investors and investee perspectives. However despite focusing on one country, some of the broad challenges they found are applicable generally. They organise these problems under three dimensions:

1. Financial returns
    a. Social enterprises experience insecure income models due to a mismatch of highly innovative social enterprises with inflexible public welfare funding structures that impede social impact investments.
    b. Insecure income models due to conflicts between various forms of funding impede social impact investments.
    c. insecure income models due to persistent market failure impede social impact investments.
    d. Social entrepreneurs lacking business skills which impede social impact investments.
    e. Difficulty in accurately perceiving risks impedes social impact investments

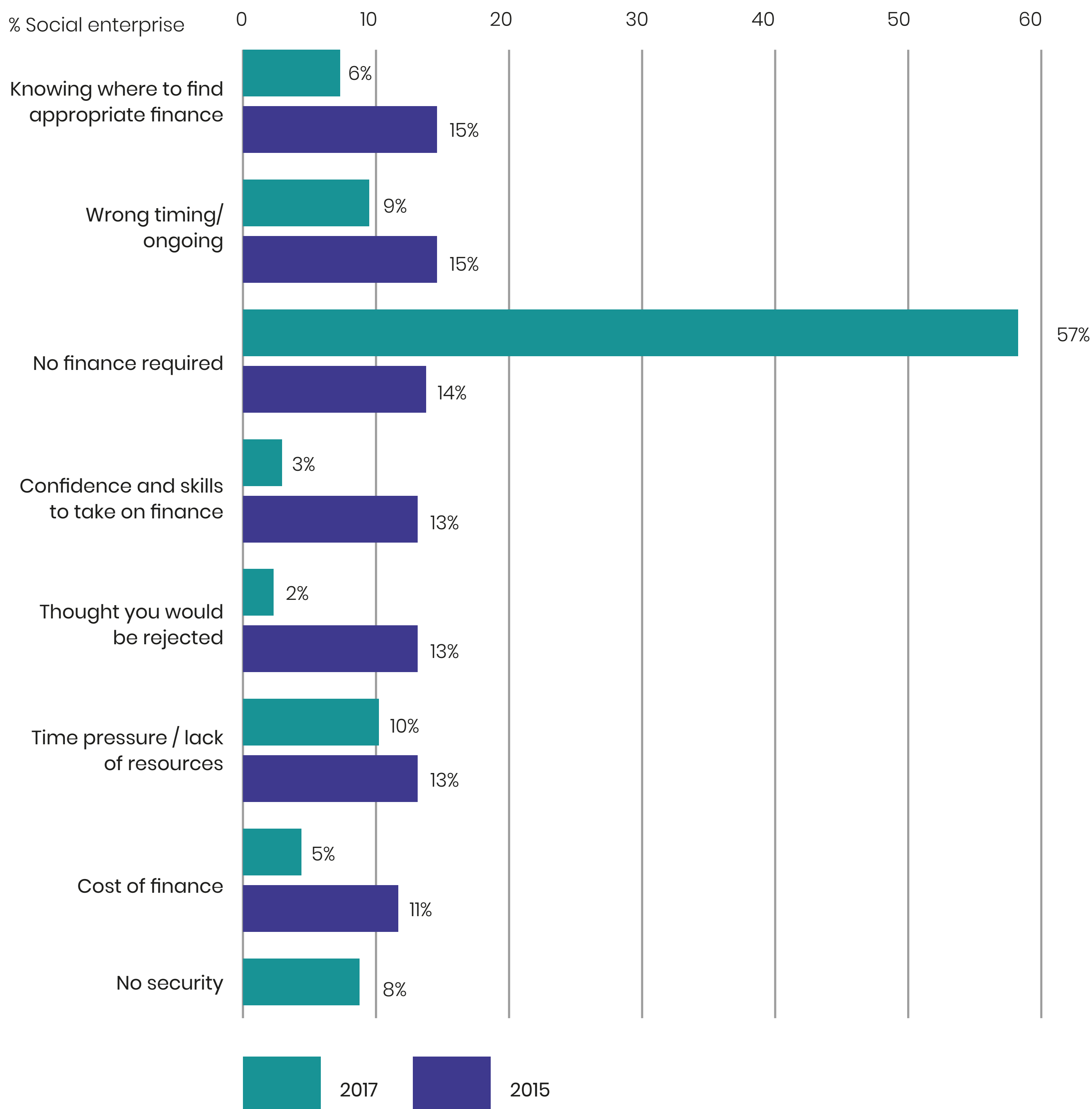
2. Social returns
    a. Inability to adequately value social returns by investors and social venture capital funds impede social impact investments.
    b. The pressure to demonstrate social impact together with a lack of efficient measurement tools impedes social impact investing.

3 Relationships and infrastructure
    a. Deviating language, attitudes and convictions regarding investment capital funded growth of investees and investors, due to different professional backgrounds, impede social impact investment.
    b. The conflict between the need for autonomy of the social enterprise (as a compensation for dimmed financial income prospects) and investor claims for control and co-decision rights impede social impact investments.
    c. Disproportionately high transaction costs and a lack of intermediaries impede social impact investments. (adapted from Glänzel & Scheuerle, 2016)

Mulgan (2015) outlines four challenges to social finance; namely returns, definitions, impact and scale which broadly agrees with some of the challenges identified by Glänzel & Scheuerle (2016). Mulgan (2015, p56) notes that "Traditional tools from finance remain too crude to cope with social realities; meanwhile the management and practice of most third sector organizations still do not fit well into the categories required by investors.". Common challenges identified by the literature on social investment include the measurement and understanding of social impact, the roles of people involved in the investments, the different ideas and difficulty generating financial returns on investment (Mulgan, 2015; Glänzel & Scheuerle, 2016).

A list of reasons social enterprises do not apply for finance can be found in figure 3.

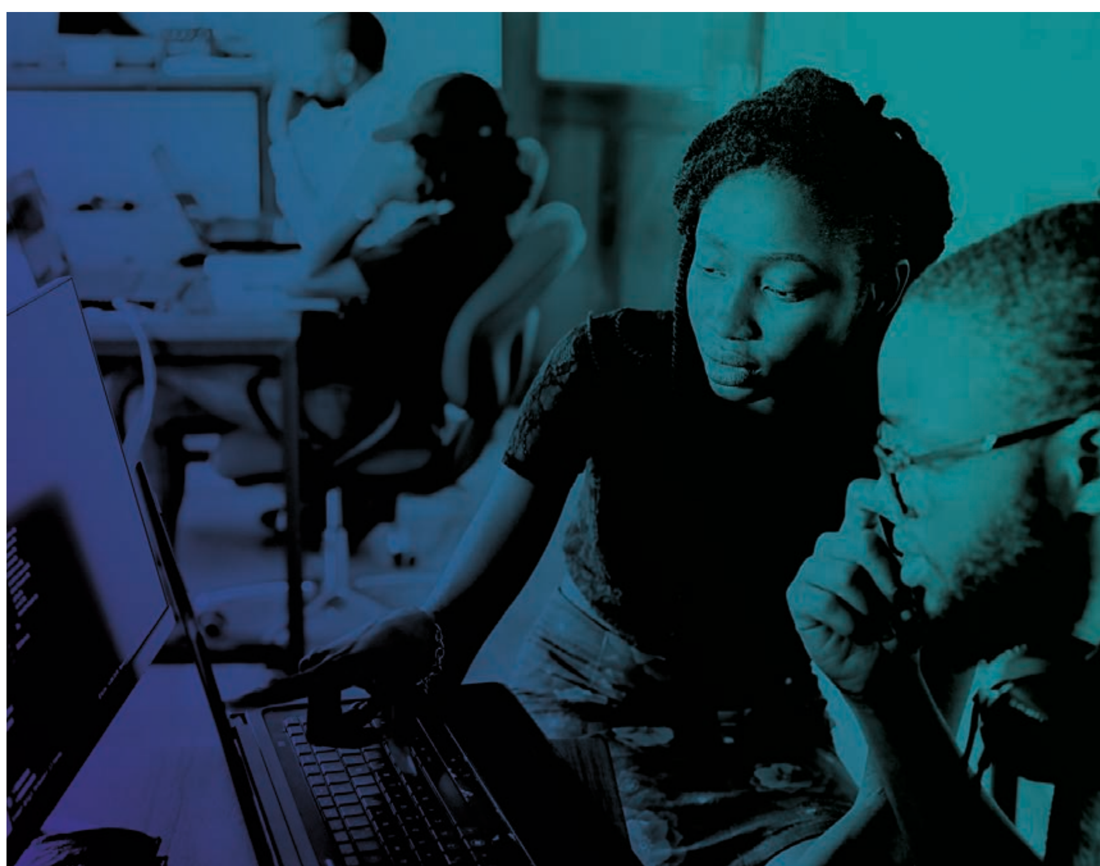
Figure 3 Reasons social enterprises give for not applying for all types of finance (Social Enterprise UK, 2017, p.45)



The real impact achieved by social investment has been questioned (Mulgan, 2015). Glänzel & Scheuerle (2016) note that organisations addressing the most severe social problems often cannot generate enough income to pay off investors, suggesting that projects which are funded by social investment may have less depth of impact, as they target groups that could be considered the 'low hanging fruit'.

The risk of mission drift within the social venture is an area of concern for investees (Roundy et al., 2017). There is a perception that investors would only be interested in financial returns and that there is a risk of the project becoming more traditionally commercial and sacrificing the social impact side of the project (Franco-Leal, 2020). This is particularly relevant, according to Franco-Leal (2020), to academic spinouts aiming to get venture capital to fund a social innovation, they found that close relationships between academic entrepreneurs and venture capitalists reduced the likelihood of the development of a social innovation. Franco-Leal (2020) therefore suggest that impact investors specifically should be sought out and Agrawal & Hockerts (2019) find similarly that the specialisation of impact investors towards social and financial value increased the likelihood of alignment between investor and investee and subsequently a more successful relationship. Organisations who access blended income sources cause some concern if they leverage social investment, in that they could effectually use public money to increase profits of commercial entities.

Glänzel & Scheuerle (2016) emphasise the importance of infrastructure and support to social investments. Many sources agree that the UK is advanced in their development of infrastructure and policy to support social investment (Mulgan, 2015; Glänzel & Scheuerle, 2016; OECD, 2019). For example, support in developing business models which create secure income and support to build general business skills in social entrepreneurs would be beneficial. There is a complex social finance ecosystem which is not yet fully institutionalised (Mulgan, 2015). Mulgan (2015) highlights the creation of 'investment readiness funds' and a programme of capacity building as one key element to the success of social finance.



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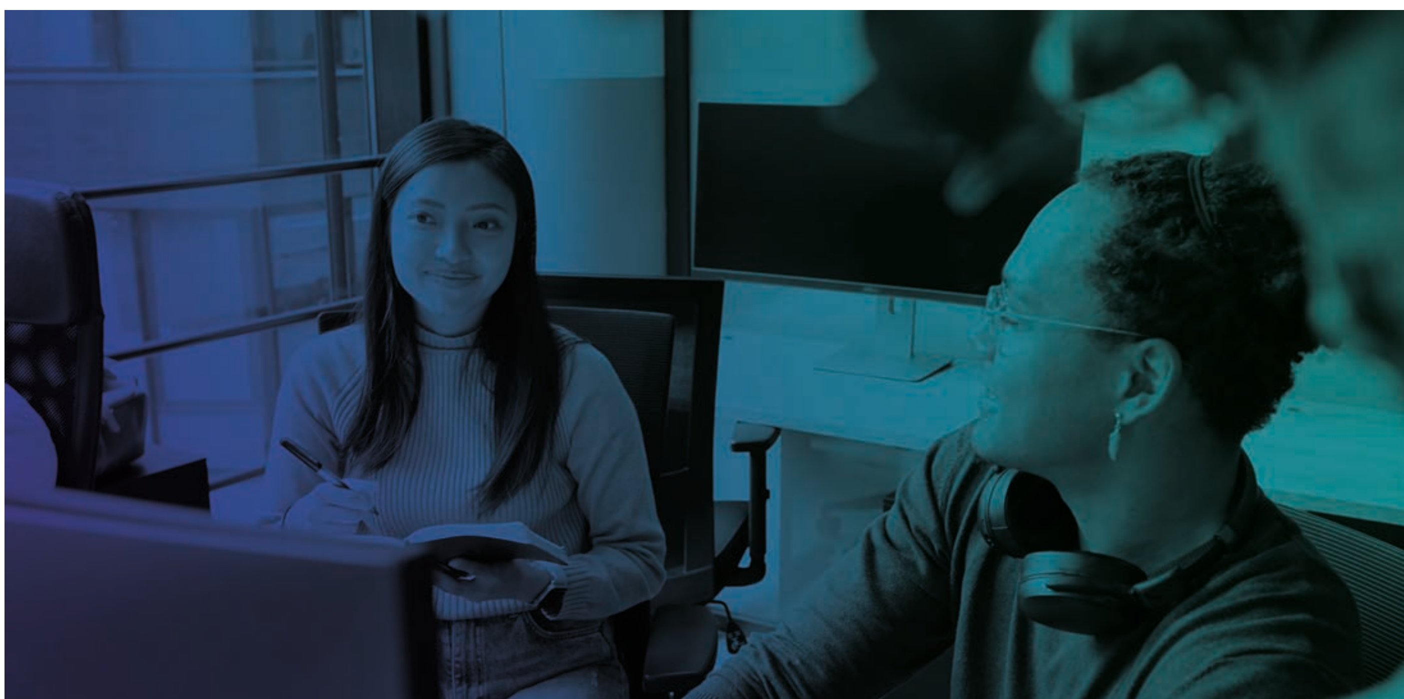

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