New Specialist Sources of Capital for the Social Investment Market

RESEARCH REPORT CITY OF LONDON CORPORATION

SOCIAL INVESTMENT RESEARCH COUNCIL

The Social Investment Consultancy

LE London Economics

New Specialist Sources of Capital for the Social Investment Market is published by the City of London Corporation, on behalf of the Social Investment Research Council. The author of this report is The Social Investment Consultancy in association with London Economics.

The Social Investment Research Council, which launched in October 2013, is formed by Big Lottery Fund, Big Society Capital, Citi, City of London Corporation and the Cabinet Office. It is a coordinated initiative which draws together research commissioners from key organisations in the social sector.

April 2014

PO Box 270
Guildhall
London EC2P 2EJ

www.cityoflondon.gov.uk/economicresearch

Contents

Foreword

The UK social investment market is continuing to develop and grow, surpassing £200m in value for the first time in 2011/12. With this growth comes a corresponding need for finance, and concerns that a lack of appropriate finance - particularly risk finance in the short term - may pose a barrier to market growth.

Our five organisations, the founding members of the Social Investment Research Council, are therefore delighted to have jointly commissioned this research to explore potential new pools of capital for the social investment market. This report focuses on eight institutional investor groups to explore their motivations and potential for engagement – charitable organisations, corporations, faith-based organisations, family offices, housing associations, insurers, pension funds and university endowments. In particular, the research explores their drivers for making investments and the current barriers to them engaging with social investments.

The report highlights that, across all eight of the investor groups explored, there is a strong belief in the potential to increase their social investment activity, but that the type of investment opportunities they seek will differ. This willingness to engage reflects a trend increasingly apparent in the market - that some key groups of institutional investors are becoming more interested in achieving social impact as well as financial returns.

The research also identifies two key opportunities offered by the social investment market over the next five years, which will most likely appeal to different groups of investors: an opportunity for risk investments, estimated at circa £500m, and an opportunity for investments in less risky, more established social industries with track record, estimated at circa £5bn. By considering these two very different segments – the higher risk and established ends of the market – this report suggests ways in which a more targeted engagement and marketing strategy could be helpful.

In the case of the £500m higher risk investment opportunities, the research indicates that charities, corporations, housing associations and family offices are more likely providers of capital. These investors are motivated to create impact as an objective of their investment activities or in their approach to service delivery. The larger, more established '£5bn' end of the market is likely to be supported by a pioneering group of local authority pension funds, who require large investment sizes and have created dedicated allocations to support social investments. Family offices and charitable endowments are also potential financiers, where they have capacity to consider larger investments in sectors that are close to their current areas of focus.

The report also highlights, however, challenges to their engagement with the market – such as a lack of performance track record for many social organisations, lack of awareness of investment opportunities, and a need for credible investment advice; these issues are by no means insurmountable, and this report offers some basis for addressing them.

This research serves a key role in both highlighting the opportunities for engaging with new investor groups, as potential sources of capital for the UK social investment market, and presenting ways in which this might be done. In addressing this key supply-side issue for the market, the report provides a valuable contribution towards a key 'gap' in market knowledge.

The Social Investment Research Council welcomes this report and accompanying investor group profiles. The research contributes to our key purpose as a Council of producing practical research to support the development of the social investment market. In highlighting key opportunities and barriers, this research provides valuable insights into how best to convert interest in social investment to action from a range of institutional investors.

Robert Annibale
Global Director
Community Development & Inclusive Finance

Mark Boleat
Chair, Policy & Resources Committee
City of London Corporation

Kieron Boyle
Head of Social Finance
Cabinet Office

Nat Sloane
England Chair
Big Lottery Fund

Nick O'Donohoe
Chief Executive
Big Society Capital

Headline findings

- Eight institutional investors groups - charitable organisations, corporations, housing associations, insurers, faith-based organisations, family offices, pension funds, and university endowments – were examined. These investors were each selected as their engagement with social investment is largely under-researched to date.
- These investor groups control total combined assets of over £687bn. This research finds that to date, their social investments can be estimated at £500m in total, at the upper end.
- Across all the investor groups, there is a strong belief in the potential to increase their social investment activity over the next five years.
- Tapping into this interest requires an understanding of investors' motivations and underlying investment priorities i.e. are investors motivated foremost by the social impacts of investments, or more commercially-driven?
- It can be helpful to think of the social investment market as a spectrum with two types of investment opportunity at each end:
    1. The need for risk finance capital required to support UK social sector organisations, estimated at circa £500m.
    2. A separate, multi-billion pound opportunity to invest in more established social industries - estimated as the 'next £5bn' of investment capital, to help scale up and grow the market.
- These two 'ends' of the market will attract different investors with different priorities.
- The research indicates that charities, corporations, housing associations and family offices who are primarily motivated to create impact as an objective of their investment activities or approach to service delivery, are most likely to be the prime providers of the £500m in risk capital required in the coming years.
- The larger, more established 'next £5bn' end of the market is most likely to be supported by a pioneering group of local authority pension funds who require large investment sizes and have created dedicated allocations to support social investments, as well as family offices and charitable endowments with capacity to consider larger investments in sectors that are close to their current areas of focus.
- Investors also identify challenges to engaging with social investment, including:
    - Lack of clarity around definitions of social investment and investment products;
    - Perceptions of the market as risky, and unfamiliarity due to an emerging track record;
    - Expected low return rates comparative to other investments;
    - Size of large enough, good, 'investable' opportunities;
    - Core social mission as a strong influencer over investment decisions;
    - A disassociation between ethical/socially responsible investment (SRI) activities and social investment (not a natural 'stepping stone');
    - Access to/availability of credible advice;
    - Confusion among asset owners as to who is responsible for identifying social investments as an option – advisers or clients.
- There is potential to engage investors' interest in social investment through targeted approaches that consider their overall investment approach and which 'end' of the market they are most likely to support – £500m in risk capital or the next £5bn in established investments.

Executive summary

As part of its 2013/14 research programme, the Social Investment Research Council commissioned The Social Investment Consultancy in association with London Economics, to undertake research to identify and understand new potential sources of capital – specifically, looking into institutional investors – for the UK social investment market.

This executive summary provides an overview of the research and its key findings, and the subsequent recommendations.

Purpose of the research

The UK social investment market has grown in recent years, surpassing £200m in value in 2011/12[1]. As the market continues to grow, there is a corresponding need for finance among social sector organisations, and particularly, demand for early-stage 'risk capital' – forecast to reach £550m by 2015[2]. This has raised concerns that a lack of appropriate finance may pose a significant barrier to market growth[3].

The social investment market to date has largely been financed by government, social banks and Social Investment Finance Intermediaries (SIFIs) (encompassing Community Development Finance Institutions, CDFIs), overwhelmingly in the form of secured lending (90% of the lending to the market in 2011/12)[4]. In addition there is evidence that the market is increasingly attracting finance from alternative sources such as individual philanthropists and angel investors[5], alongside some support from institutional investors including charitable and corporate foundations, certain pension funds, family offices and housing associations. These institutional investor groups represent potentially deep pools of capital for the market, which – if mobilised effectively – could make a transformative difference to the amount of risk capital available. However, there is still a general lack of knowledge about the interest among these institutional investors in making social investments, which factors contribute to institutional investors' decisions on whether or not to invest in the market, how they differ from other groups of investors, and what steps might, if taken, help establish these groups more fully as social investors.

This research therefore seeks to better understand and develop a fuller picture of UK-based institutional investors, the scope of their involvement with social investment[6] to date, what motivates them to make investments, and what the current barriers are to them engaging with the social investment market. In essence, to answer the question 'Is the social investment market looking in the right places for new sources of capital, or have some key groups been overlooked?', and importantly, do they face similar or different barriers to engagement, and are these easier to overcome than those already identified by previous research? While the research does not reflect an objective measure of barriers to social investment, it seeks to understand the perceived and experienced barriers, as identified by institutional investors.

---

[1] ICF GHK with BMG Research (2013).
[2] Brown & Swersky (2012).
[3] See Brown & Swersky (2012) and ICF GHK with BMG Research (2013).
[4] ICF GHK with BMG Research (2013).
[5] The 2012 Big Venture Challenge for example uncovered new potential investors for the market. See Howells, Miller & Fox (2012).
[6] For the purposes of this study, social investments are defined as investments that intend to create positive social or environmental benefits in addition to financial return (JP Morgan, 2012).

Institutional investors examined in the research

Much previous research has been undertaken on the appetite of key mainstream financial institutions for engaging in social investment[7], and revealed certain barriers which the market and social sector is working to address. This research looks at previously under-researched institutions who might also be interested in engaging with the market. Therefore, the following eight institutional investor groups active in the UK are examined as potentially 'untapped' pools of capital:

- Charitable organisations;
- Corporations;
- Faith-based organisations;
- Family offices;
- Housing associations;
- Insurers;
- Pension funds; and
- University endowments.

These asset holders were chosen because there is less known to date about their appetite for and perceptions of social investment, but they all have some reason to be interested in investing for social outcomes – alignment with core social mission, for example, particularly in the case of charitable organisations and faith-based organisations.

This research explores each of these groups separately as distinct investors, through a combination of in-depth, desk-based market research and 'deep-dive' interviews with key organisations within each investor group. It is recognised that there are likely to be some common perceptions and experiences across some or all of the groups, and these are also explored briefly. For example, some of these groups share common legal structures - most university endowment and faith-based organisations, and many housing associations for example, are also charities and therefore face the same legal obligations in relation to their investment decisions[8]. Where such overlapping considerations occur, they are highlighted in the report, but for the most part this research treats each group as distinct, based on their specific characteristics.

General trends and key findings

Institutional investors' appetite to engage in social investment

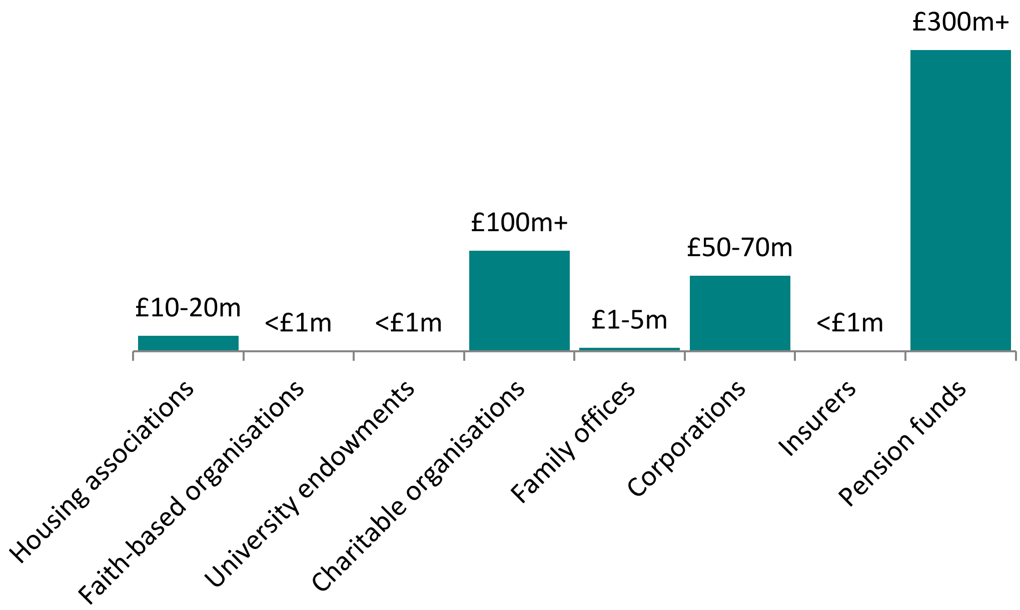
Based on market research, the eight institutional investor groups examined in this research are found to control combined assets of over £687bn. In terms of their involvement with social investments to date, the research indicates this can be estimated at around £500m in total[9], at the upper end (see Figure 1). Clearly then there is potential for engagement with social investment among the institutional investors examined in this research.

---

[7] For example Buckland (March 2014); Bridges Impact (January 2014); Baker & Goggin (March 2013); Gregory, Hill, Joy & Keen (July 2012); and City of London Corporation, Big Lottery Fund & City Bridge Trust (July 2011).
[8] Of note is the Law Commission's consultation paper on charity law and social investment, published on 24th April 2014. See: http://lawcommission.justice.gov.uk/consultations/charity-law.htm
[9] Note that this £500m is calculated using a wide definition of social investment as any investment intended to have social/environmental impact in addition to financial return, including for example investments made through corporate CSR programmes. It is therefore larger than the figure presented for the size of the market - £200m in value in 2011/12 – which is calculated using a narrow definition of finance to social sector organisations from Social Investment Finance Intermediaries (SIFIs) only.

The interviews undertaken as part of this research[10] found there is a strong belief across the eight investor groups in the potential to increase their social investment activity in the next five years. However, the interviews also reveal there is a lack of clarity over what this activity might look like, the risks involved in making social investments at present, and what a 'social investment' is and what it is not.

Figure 1: Estimated commitments by UK institutional investors to social investments to date[11]



The need for social investment capital and opportunities to invest

Having established there is interest among institutional investors in social investment, this research considers how to improve investors' engagement with the market. It suggests it might be beneficial to think of the social investment market as a spectrum, providing two different sets of opportunities at either end. The opportunity at one end derives from the need for risk finance capital to support UK social sector organisations in the coming years. Based on previous research[12], this demand is estimated at circa £500m in risk capital. Within this report, this risk finance end of the market is referred to as the 'next £500m'. The second opportunity, at the other end of the market spectrum, is a separate, multi-billion pound opportunity to invest in less risky, more established, and therefore by comparison more mainstream and 'commonplace', social industries[13]. Within this report, this is estimated as the 'next £5bn' of investment capital, to help scale up and grow the market for social investment more generally.

[10] Forty one interviews were carried out in total - 36 with investment officers across the eight institutional investor groups, two interviews with advisers and three with relevant market stakeholders.
[11] Includes only known investments into funds or opportunities marketed as 'social investments'. See also footnote 9.
[12] Brown & Swersky (2012).
[13] Within this research, 'established' social industries refer to those less risky industries with some track record of performance, including but not limited to – sustainable forestry, microfinance, clean tech, social housing, healthcare, sustainable and environmental industries.

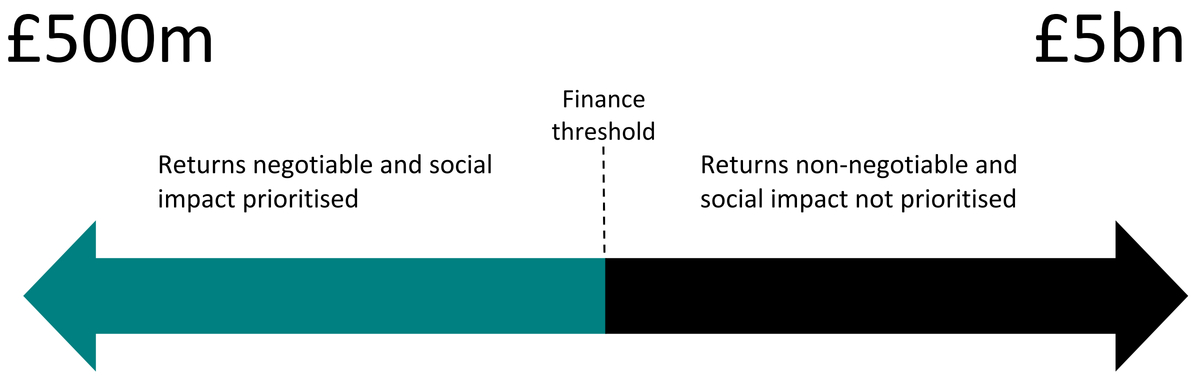
The two financial thresholds of £500m and £5bn presented here are approximate markers only, to aid the analysis of the research findings and inform discussion about how to help grow the social investment market through institutional investor engagement. The main purpose of referencing these two 'ends' of the social investment market is to help to illustrate for the reader that the market requires different types of finance and accordingly, different types of action to meet these separate finance needs. Neither the £500m or £5bn thresholds represent targets for the market, nor are these thresholds presented as definitive.

These two 'ends' of the market can be difficult to differentiate fully until viewed from investors' perspectives. The risk finance end is less well-known, has less of a track-record and can require investors to 'go the extra mile' to conduct due diligence on early stage investments, new markets and innovative products. Generally, investors provide 'risk' social finance because they are driven to do so for the positive social impacts, as an alternative or complement to philanthropic grants, rather than because they think it is the most effective way to generate a financial return (though this doesn't necessarily mean there is no capital protection, either).

Conversely, the second set of opportunities is quite different – it includes bigger opportunities in established industries (such as environmental, green and clean tech, forestry, social housing etc.) with less risk. It is easier for investors to consider products against mainstream options, and to make a decision to invest where there is confidence that risk-adjusted return requirements can be met.

This spectrum of investment opportunities combined with investor intentions is set out in Figure 2.

Figure 2: Spectrum of investor intentions and willingness to compromise financial returns, linked to potential future sources of capital for the market



Understanding the motivation to invest: different personality types emerge

Following the above, this research highlights that social investment is approached emotionally as well as rationally by investors. Alongside an analysis of risk-adjusted returns, the decision of whether to engage with social investment is also a question of values and of how the institution is, or should be, connected to society.

Efforts to engage investors can therefore be counterproductive if investors' motives are not considered. More conventional investors looking for strong-performing funds in established markets, such as sustainable forestry, will not necessarily be attracted to those more innovative investment opportunities such as social impact bonds and risk equity deals. They may even be dissuaded from engaging with social investment if the market is perceived as too strongly associated with some of these riskier aspects. Therefore, to engage these more commercially-minded investors – those most likely to provide the next £5bn in established investment capital – the more mainstream and 'commonplace' aspects of the social investment market offer needs to be emphasised i.e. that there are social investment opportunities that are similar to other financial deals which such investors are used to considering in established asset classes.

Conversely there are some investors who consider social investment as a potential alternative to philanthropic grants, and will only engage with the market if the investment is made exciting and clearly supports innovation (therefore being more likely to invest in 'riskier' social investment opportunities, providing the next £500m in risk capital).

In analysing the different attitudes and approaches to social investment, the research identifies seven 'personality types' among the institutional investors interviewed. To be effective, any attempt to encourage investors to engage with social investment will need to take these personality types into account. The personality types are defined in detail in chapter 2.

New opportunities - the most likely new sources of capital for the UK social investment market

Following the analysis above, the two 'ends' of the market (£500m risk finance at one end, £5bn established investment capital at the other) will attract different investors with different personality types.

From this research, it is possible to (indicatively) identify that charities (using social investments as a tool to help deliver their missions), corporations (through corporate social responsibility (CSR) programmes), housing associations and family offices who are motivated to create impact as an objective of their investment activities or approach to service delivery, are most likely to be the prime providers of the £500m in required risk capital in coming years.

The larger, more established £5bn end of the market is most likely to be supported by a pioneering group of local authority pension funds who require large investment sizes and have created dedicated allocations to support social investments, as well as family offices and charitable endowments with capacity to consider larger investments in sectors that are close to their current areas of focus (see Table 1).

While this research identifies which investor groups display the most potential for engaging with these different ends of the social investment market, it does not prioritise which are more likely to engage, than others.

Table 1: Indications for institutional investors most likely to engage with each 'end' of the social investment market

Next £500m in risk finance	Next £5bn in established social investments
Most likely to come from:	**Most likely to come from:**
• Charitable organisations • Corporations • Family offices • Housing associations	• Charitable organisations • Family offices • Pension funds
Potential interest in the longer-term from:	**Potential interest in the longer-term from:**
• Insurers	• Faith-based organisations • University endowments

The research indicates that faith-based organisations and university endowments generally prioritise their investment decisions in direct accordance with their core social mission and maintaining the long-term sustainability of their organisation. Therefore while they are not among the investor groups most likely to provide new sources of social investment capital in the near future, they are interested in social investment and should not be overlooked in attempts to encourage institutional engagement with the market. In the longer term, the most likely entry point to social investment for faith-based organisations and university endowments will be through commitments towards the £5bn end of the market, in established social investments.

While insurers are similarly focused on ensuring their investment strategies match their long-term liabilities to customers, they are more likely to make long-term investments in-house rather than into marketed social investment funds. Therefore insurers, as consumer-facing businesses, might potentially be engaged to provide risk finance to social sector organisations through CSR finances rather than investment activities, towards the £500m end of the market.

Investors' perceptions of the challenges of social investment

Institutional investors are interested in social investment, and the above analysis is indicative of which groups are likely to be most responsive to attempts to engage them with the market.

However, institutional investors also identify a number of challenges or barriers to engagement. These largely mirror those identified by banks, investment funds and other institutional investors in previous research, suggesting there are clear areas for progress for the market and social sector organisations. The main barriers identified are listed below, in no particular order (these are set out in detail in chapter 2).

Definitions of social investment and investment products, and the need to unpack what is meant by the social investment market.
Across all investor groups, even the more knowledgeable/experienced investors express a need for greater clarity around how social investment is defined and what comprises investment products in the market.
Perceptions of the market as risky, arising from lack of clarity over the concept of social investment, and unfamiliarity due to a limited track record.
On the whole, perceptions of the market are currently suffering as a result of investments labelled as 'social', being more strongly associated with the market's riskier elements. For example, investment opportunities in microfinance, sustainable forestry, and social housing, among other areas, have been available for years at a scale most institutional investors could engage with. However, investors tend to relate 'social' investment opportunities solely to more innovative products, such as social impact bonds and equity investments into social sector organisations. Though these are only some of the social investment products on offer, they have generated the most press in recent years and institutional investors for the most part, also associate these with risk and philanthropy, over competitive commerce.
Expected low return rates comparative to other investments.
Linked to the perception of risk, the rate of return of social investments is identified as a barrier, particularly among those investors who are more commercially-minded and/or have a fiduciary duty to maximise financial returns when making an investment.
Size of large enough, good, 'investable' opportunities.

Investors with large portfolios tend to have minimum investment size requirements, many of which are much larger than most social investment opportunities. Again however there is greater potential for these size requirements to be met among the more mainstream social sector funds, of which investors could be made more aware.
The need to prioritise social mission.
Though not a 'barrier' to social investment as such, a key consideration for those investors that are tightly bound to a core social mission, is the need for social investments to fit within the scope of their social mission. This consideration can therefore act as a constraining factor in some cases[14].
A disassociation between socially responsible/ethical/sustainable investment, and social investment.
Institutional investors' engagement with ethical or socially responsible investment (SRI) activities does not necessarily correlate with social investment activity. This suggests that SRI is not an obvious 'stepping stone' to social investment and approaches to engage investors therefore need to be independent of their SRI portfolio.
Poor access to/availability of credible advice on making social investments.
Linked to investors' perceptions that the social investment market is 'new', 'unfamiliar' and 'risky' is the fact that investors feel lacking in their own ability to make educated decisions and that there is an absence of accessible marketplace advisers. Investors are looking for advisers and product managers whom they see as credible and trustworthy – a perception that is often tied to familiarity and a track record. Investors are therefore more likely to consider investment opportunities that are presented to them by an organisation or adviser that they have previously worked with, or which has a strong reputation in the market. A barrier here is that investors interviewed mentioned being generally unaware of where such credible sources can be found. This challenge might be linked to the difficulties in undertaking due diligence in propositions in the social investment market.
Confusion around who is responsible for identifying social investments as an option – advisers or clients.
Another key barrier identified by those investors who rely on fund managers/financial advisers to inform their investments, is confusion around who – the client or the adviser – should be bringing investment opportunities to the table.

Summary of challenges and barriers

For the most part, these barriers are not particularly new, but have been identified in previous research and for other asset holders as well as the investor groups explored in this research.

However, this report adds a new dimension to tackling these barriers through a targeted engagement and marketing strategy. By thinking of the market as a spectrum, with each end offering two key investment opportunities – at one end, an opportunity for £500m in risk capital and at the other end, an opportunity for £5bn in more established social investment market finance – the needs of different investor groups can be more readily matched with the available opportunities.

[14] The Law Commission published on the 24th April a consultation report on charity law and social investment. In the paper the Commission recognises the current legal framework does not easily accommodate social investments and there is uncertainty among some charity trustees as to how social investments 'fit' with their charitable missions. See: http://lawcommission.justice.gov.uk/consultations/charity-law.htm

Although there is a risk of segmenting an already small and somewhat impenetrable marketplace further, this approach is suggested as a targeted marketing strategy to reach and engage with potential investor pools of capital, as opposed to a comprehensive strategic approach for the social investment marketplace as a whole. The £500m and £5bn opportunities also represent extreme ends at either end of the market, and there will be a range of opportunities between each end.

Recommendations

A set of practical recommendations have been produced from the research findings (set out in more detail in chapter 11). These take into consideration:

- The appetite for social investments identified by institutional investors;
- The challenges and barriers to engaging with social investment, perceived by investors;
- Potential opportunities for social investment in the future; and
- Practical considerations around how to take advantage of these opportunities, at either 'end' of the social investment market.

<table>
<tr><th colspan="2">Recommendations to raise the next £500m in risk finance social investments</th></tr>
<tr><td colspan="2">1. Further clarity on how to encourage charitable foundations to make social investments from their endowments, in line with trustees' fiduciary obligations[15]</td></tr>
<tr><td colspan="2">• Exchange best practice through case studies amongst foundations on how to use their finance to help provide the risk capital needed by social sector organisations.
• Encourage foundations to create and support the development of social investment opportunities in the future.
• Draw on the experience of foundations in creating social impact in understanding how social returns are generated and measured.</td></tr>
<tr><td>Barrier addressed: Lack of clarity around definitions of social investment, and the need to unpack what is meant by the social investment market[16].</td><td>Target institutions:
• Charities;
• Faith-based orgs;
• Universities.</td></tr>
</table>

[15] Also of note here is the Law Commission's consultation into charity law and social investment, published on 24th April. See: http://lawcommission.justice.gov.uk/consultations/charity-law.htm

[16] This barrier is consistent with other research undertaken on behalf of the Charity Commission between July 2012 and March 2013, into the regulatory risks, challenges and opportunities which charities face in regards to social investment. One of the research findings was a lack of clarity among some charities of the application of charity law when making social investment decisions. See: http://www.charitycommission.gov.uk/news/charities-and-social-investment-190313/

<table>
<tr><th colspan="2">Recommendations to raise the next £5bn in established social investments</th></tr>
<tr><td colspan="2">2. Improve awareness and understanding of the more mainstream and ‘commonplace’ elements of social investment</td></tr>
<tr><td colspan="2">• Emphasise the more established elements of the social investment market to improve awareness of these investment options among more commercially-driven investors.
• Potential to sub-divide the market into innovative, riskier products and more mainstream options, to help tackle perceptions of risk and unfamiliarity.</td></tr>
<tr><td>Barrier addressed:
• Lack of social investment knowledge and unfamiliarity with the market.
• Lack of clarity around definitions and the need to unpack what is meant by the social investment market.</td><td>Target institutions:
Universal.</td></tr>
<tr><td colspan="2">3. Single place for tracking</td></tr>
<tr><td colspan="2">• Continue to build on existing work, such as Global Impact Investing Network’s (GIIN) ‘Impact Base’ to create a central resource such as a website to showcase the largest funds across a variety of sectors and publish performance data against a benchmark.
• Incorporate ability to browse current deals and top performing funds.</td></tr>
<tr><td>Barrier addressed:
• Lack of social investment knowledge.
• Lack of performance track record.
• Perceptions of risk and uncertainty.</td><td>Target institutions:
Universal.</td></tr>
<tr><td colspan="2">4. Tagging social investments for mainstream financial tools</td></tr>
<tr><td colspan="2">• Create functionality to ‘tag’ social investments within commonly-used financial tools
• Enable users to filter and compare opportunities and fund performance on same platform as all other investments.</td></tr>
<tr><td>Barrier addressed: Lack of performance track record.</td><td>Target institutions:
Universal.</td></tr>
<tr><th colspan="2">Recommendations to raise finance at both ends of the market</th></tr>
<tr><td colspan="2">5. Increase opportunities for sharing experiences for education, peer-to-peer learning and awareness-raising</td></tr>
<tr><td colspan="2">• For example, education and awareness-raising opportunities could be provided through closed roundtable sessions between peers to share experiences, ask questions and raise issues, in confidence.</td></tr>
<tr><td>Barrier addressed: Lack of social investment knowledge and poor awareness of investment opportunities.</td><td>Target institutions:
Universal.</td></tr>
<tr><td colspan="2">6. Need for evidence to capture data</td></tr>
<tr><td colspan="2">• Further research is required to produce evidence to profile, recognise and track deals done outside social investment funds, e.g. by corporations and housing associations, to build evidence base and encourage further movement within sectors; this would help create a multiplier effect by learning and experimentation</td></tr>
</table>

<table>
<tr><td>Barrier addressed: Lack of social investment knowledge and associated need for better information flow.</td><td>Target institutions:
• Corporations;
• Pension funds;
• Insurers.</td></tr>
<tr><td colspan="2">7. Asset owners mandate fund managers to consider social investment</td></tr>
<tr><td colspan="2">• Asset owners with an interest in social investment opportunities should stipulate to their advisors/fund managers, a mandate to seek out and present social investment opportunities to them.</td></tr>
<tr><td>Barrier addressed: Confusion among asset owners around where responsibility lies for raising social investment opportunities.</td><td>Target institutions:
Universal.</td></tr>
</table>

The way forward

The research findings highlight that the UK social investment market needs time and success stories to help it grow and develop a clear track record. In addition, clarity around the different types of social investment opportunities and the dissemination of clear, un-filtered performance information will help move the sector as a whole forward. Credible financial advice that is easily accessible to asset owners is also a key issue, alongside the need for asset owners to proactively identify their interest in social investment to their advisers.

By understanding the marketplace as a spectrum, with each end offering different opportunities, this research helps to identify potential ways for institutional investors to engage with the market, in line with their motivations and in reflection of the limitations each investor group might face. Such an appropriately-targeted approach, if applied, is likely to be more successful than a ‘one size fits all’ approach.

The recommendations include suggestions for how to grow general market confidence in social investment and how to target specific groups of investors – the ‘low-hanging fruit’ – capable of contributing to the next £500m in risk investments and the next £5bn in established investments.

1. Introduction

1.1. Report structure

This chapter provides a brief introduction to the research in terms of the research objectives, the institutional investor groups examined and the research methodology. Chapter 2 provides an overview and analysis of key trends across institutional investors. Chapters 3 to 10 provide a profile for each investor group in terms of their: (i) size by investable assets and segmentation; (ii) overall investment history; (iii) current engagement with social investment; (iv) motivating factors; and (v) barriers to making social investments. For each group, steps to engage them further as social investors are considered, as well as what type of social investment products are most likely to be compatible with their broad investment goals. The final chapter of the report presents general conclusions from the research findings and detailed, practical recommendations covering all eight investor groups. The interview schedule used in this research is contained in Annex One. Annex Two consist of one page 'profiles' for each of the institutional investor groups explored in this research.

1.2. Context and research objectives

This research project was commissioned by the Social Investment Research Council, to identify and understand new potential institutional sources of capital for the UK social investment market. In doing so the research seeks to build on existing evidence on the appetite of key mainstream financial institutions to engage in social investment[17]. This previous research revealed certain barriers which the market is working to address. This research looks at other groups of asset owners who might also be interested in engaging with social investment, and if so, what challenges they might face in doing so. In essence then, the research seeks to answer the question 'Is the social investment market looking in the right places for new sources of capital, or have some key groups been overlooked?' Following this, the research considers whether these new sources face similar or different barriers to market engagement, and whether these are easier or harder to overcome than those already identified.

The UK social investment market has grown in recent years, surpassing £200m in value in 2011/12[18]. Recent data suggests there are an estimated 688,000 social sector organisations in the UK (when including sole traders), with a GVA contribution of £18.5bn[19]. As the market continues to grow however there is a corresponding need for finance among social sector organisations, and particularly demand for early-stage 'risk capital'. With demand for risk capital forecast to reach £550m by 2015[20], there has been a concern that a lack of appropriate finance may pose a significant barrier to market growth. While previous research has examined the approach of various groups of asset holders towards social investment, this research looks at previously under-researched financial institutions, to establish if there are potential untapped sources of capital which are 'ripe' for involvement if provided with the right triggers.

The social investment market to date has largely been financed by government, social banks and Social Investment Finance Intermediaries (SIFIs) (encompassing Community Development Finance Institutions, CDFIs), overwhelmingly in the form of secured lending (90% of the lending to the market in 2011/12)[21]. In addition there is evidence that the market is increasingly attracting finance

---

[17] For example Buckland (March 2014); Bridges Impact (January 2014); Baker & Goggin (March 2013); Gregory, Hill, Joy & Keen (July 2012); and City of London, Big Lottery Fund & City Bridge Trust (July 2011).
[18] ICF GHK with BMG Research (2013).
[19] BMG Research (May 2013).
[20] Brown & Swersky (2012).
[21] ICF GHK with BMG Research (2013).

from alternative sources such as individual philanthropists and angel investors[22], alongside some support from institutional investors including charitable and corporate foundations, certain pension funds, family offices, and housing associations. These institutional investor groups represent potentially deep pools of capital for the market, which – if mobilised effectively – could make a transformative difference to the amount of risk capital available. However, there is still a general lack of knowledge about the interest among these institutional investors in making social investments, which factors contribute to institutional investors' decisions on whether or not to invest in the market, how they differ from other groups of investors, and what steps, if taken, might help establish these groups more fully as social investors.

As such, this research seeks to better understand and develop a fuller picture of UK-based institutional investors, the scope of their involvement with social investment[23] to date, what motivates them to make investments, and what the current barriers are to them engaging with the social investment market. While the research does not reflect an objective measure of external barriers to social investment, it seeks to understand through interviews the perceptions and experiences of the barriers faced by institutional investors, and is underpinned with market research.

1.3. Institutional investors

Institutional investors – in the broadest sense – are organisations which pool together large sums of capital to invest on behalf of others. While the scope, size, and objectives of organisations that fit within this definition vary, this study focuses on eight institutional investor groups active in the UK, and which have been less fully researched to date in their attitude towards social investment:

- Charitable organisations;
- Corporations;
- Faith-based organisations;
- Family offices;
- Housing associations;
- Insurers;
- Pension funds; and
- University endowments.

These groups were selected due to their potential to make social investments as indicated by some initial activity with social and/or ethical investment; the size of capital potentially available to invest; and because, for the most part, they are discrete groups which share common characteristics on account of similar motivations, or other regulatory or structural factors. It is worth noting for example that some of these investor groups share common legal structures - most university endowment and faith-based organisations, and many housing associations for example are also charities and therefore face the same legal obligations in relation to their investment decisions. Where such overlapping considerations occur, they are highlighted in the report, but for the most part this research treats each group as distinct, based on their specific characteristics.

[22] The 2012 Big Venture Challenge for example uncovered new potential investors for the market. See Howells, Miller & Fox (2012).
[23] For the purposes of this study, social investments were defined as investments that intend to create positive social or environmental benefits in addition to financial return (JP Morgan, 2012).

1.4. Research methodology

The research was conducted in two stages. The first consisted of market research and reviewing secondary materials to develop an overall picture of the size, segmentation and investment trends across each of the eight investors groups, and to develop initial hypotheses about their likelihood to engage with social investment.

This market research was supplemented by, 'deep-dive' interviews with key investors from each group conducted in person or by telephone. A semi-structured interview approach was used to allow interviewees to expand on their responses, and explore new areas for discussion not included in the interview schedule (see Annex One for the interview schedule).

1.4.1. Interview sample

Forty one interviews were conducted in total - 36 interviews with representatives from institutional investor organisations (see Table 2), two with investment advisers, and three with relevant market stakeholders. Based on initial market research, groups were prioritised for interview based on their perceived likelihood of making social investments in the medium term as well as the depth of information currently available. Groups for whom less information was available were prioritised for further interviews. In all cases, organisations within the five largest in their sector participated.

Within each group, target organisations were identified based on: (a) any initial activity with social investment and/or ethical investment[24]; (b) size of investment portfolio and (c) potential status as 'first-movers' due to being recognised market leaders or influencers in their sector. In each case, the chief investment officer or individual responsible for investments (e.g. charity trustee) was contacted in the first instance. The identity of interviewees and their organisations has been kept confidential.

Table 2: Number of interviews per institutional investor group

Investor Group	Number of interviewees
Charitable organisations	5
Corporations	6
Faith-based organisations	3
Family Offices	5
Housing associations	5
Insurers	2
Pension funds	5
University endowments	5

It should be noted that the interview sample is not sufficiently large to provide statistically significant data. For this reason, quantitative data for each of the sub-groups has not been included in the analysis. However, in aggregate, certain key themes and responses emerge which are consistent within and across the investor groups. They also reflect previous research into the barriers faced by other potential investor groups[25].

[24] It was hypothesised that involvement in ethical and/or social responsible investment might predispose investors to consider social investments.
[25] See footnote 17.

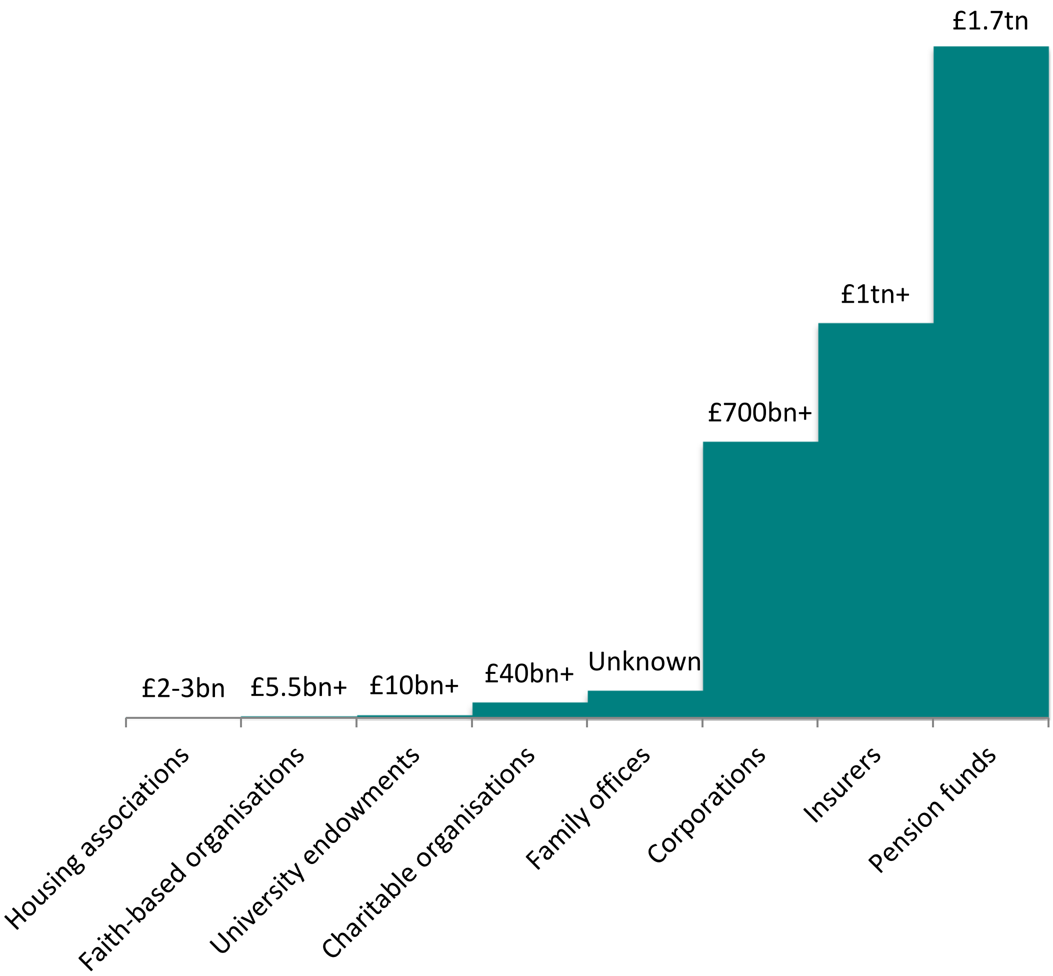
2. Overview of key findings across the investor groups

This chapter sets out the key findings of the research, first providing an overview of the investor groups examined, followed by the main trends and common perceptions identified by institutional investors. It goes on to consider the implications of the findings for each of the eight institutional investor groups. Issues specific to each group are explored in detail in the following chapters.

2.1. Profile of institutional investors

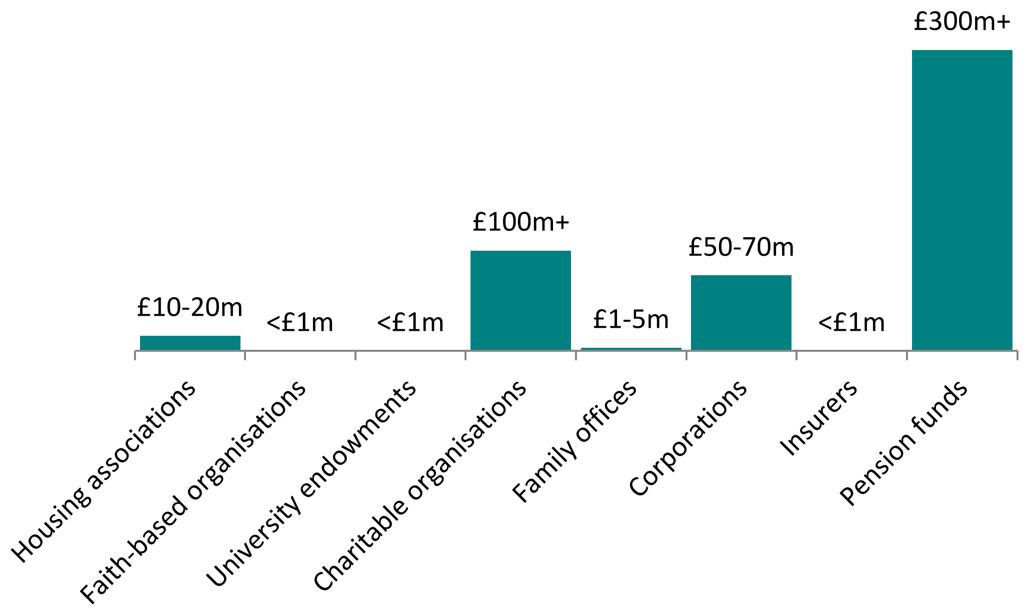
The investors participating in this research control combined assets of over £687bn. Figure 3 provides an indication of the size of each investor group, based on their investable assets. Figure 4 provides estimates for the amount of social investment capital committed to date by each investor group[26]. This illustrates there is clear potential for these investors to become active social investors over time, provided they receive the support they require.

Figure 3: Total investable assets per institutional investor group



[26] Note this is an indicative estimate only and includes only known investments into funds or opportunities marketed as 'social investments'. Note that this £500m is calculated using a wide definition of social investment as any investment intended to have social/environmental impact in addition to financial return, including for example investments made through corporate CSR programmes. It is therefore larger than the figure presented for the size of the market - £200m in value in 2011/12 – which is calculated using a narrow definition of finance to social sector organisations from Social Investment Finance Intermediaries (SIFIs) only.

Figure 4: Estimated commitments by UK institutional investors to social investments to date[27]



2.2. Attitudes to social investment: intentions drive expectations

- Broadly, investors can be divided into those that primarily view social investment as a way of generating social impact; and those that are more commercially-driven and prioritise financial returns, but recognise social investment provides additional social benefits.
- It can be helpful to think of the social investment market as a spectrum providing two types of investment opportunity at either end, and a range of opportunities between. One 'end' is the need for risk capital to finance social sector organisations. The other is for investment in less risky, more established, mainstream social industries.
- Investors that prioritise social impact are most likely to favour risk finance opportunities. Commercially-driven investors are most likely to favour established investments with more likelihood of stable returns.
- To encourage investors to engage with social investment requires tailored approaches which consider these attitudes to social investment and motivations for investing.

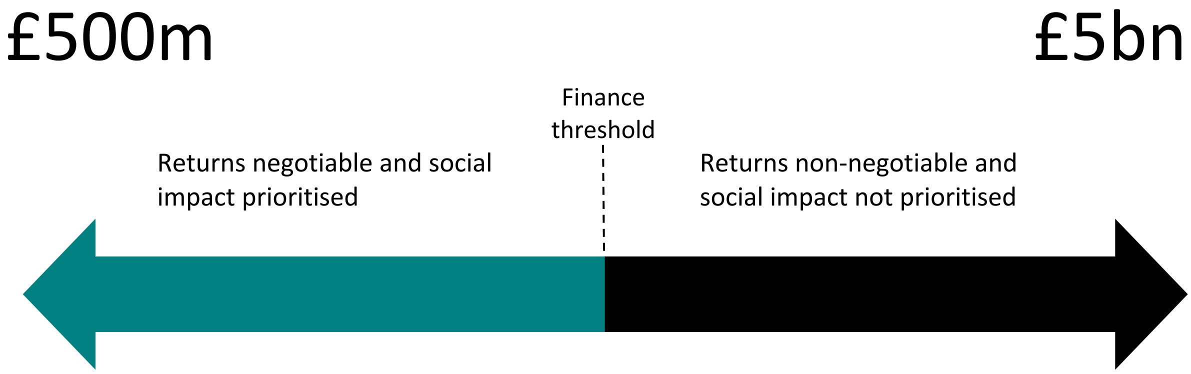
In exploring the perceived motivations and potential barriers to social investment among institutional investors, the research finds that social investment is approached emotionally as well as rationally. Alongside an analysis of risk-adjusted returns, the decision of whether to engage with social investment is also a question of values and of how the institution is, or seeks to be, connected to society.

Related to this question about purpose, this research identifies two different approaches to social investment, reflecting whether an investor group prioritises social impact or financial returns in their investment decision. At one end, social investment is seen as a more sustainable alternative or complement to philanthropic grants in achieving social goals and impacts; alternatively, at the other end of the spectrum, social investment is viewed as a more positive way than traditional investments to make the same or a similar amount of financial return with the added benefit of

[27] Includes only known investments into funds or opportunities marketed as 'social investments'. See also footnote 26.

social impact. These differences in approach among investors lead to different points of engagement with social investment (see Figure 5).

Figure 5: Spectrum of investor intentions and willingness to compromise financial returns, linked to potential future sources of capital for the market



Only by considering their intentions can we understand the specific needs of different investors, and what is needed to grow their engagement at different ends of the social investment market. (These approaches to social investment are deliberately presented here as distinct 'either/or' ends of a spectrum, to help illustrate the analysis. Of course in reality, investors might occupy any point along the spectrum and can also shift in their approach away/towards either end.)

Corresponding with these approaches to social investment, the market can be thought of as a spectrum with two distinct 'ends'. At one end, there is demand for risk capital to finance UK social sector organisations, estimated at circa £500m (based on previous research)[28]. Considering the nature of the finance required – risk capital – it is likely that this end of the market will attract those investors who prioritise social impact over financial return when making investments. The other end of the market, however, presents an opportunity to invest in more established, mainstream or 'commonplace' social industries such as sustainable forestry, microfinance and clean tech, which are therefore considered less risky. This opportunity is estimated at around £5bn of investment capital[29], and would likely attract those commercially-minded investors for whom financial returns are a priority and social impact a secondary consideration (this is illustrated in Figure 5). Figure 6 depicts the different ends of the social investment market spectrum, providing a few examples of the asset classes and products broadly available to investors from each end of the spectrum.

This analysis suggests that efforts to engage investors can be counterproductive if investors' motives are not considered. More conventional investors looking for strong-performing funds in established markets will not necessarily be attracted to those more innovative investment opportunities such as social impact bonds and equity deals. They may even be dissuaded from engaging with social investment if the market is perceived as too strongly associated with some of these riskier aspects. Therefore, to engage these more commercially-minded investors – those most likely to provide the next £5bn in established investment capital – the more mainstream and 'commonplace' aspects of the social investment market offer needs to be emphasised i.e. that there are social investment opportunities that are similar to other financial deals which such investors are used to considering in established asset classes.

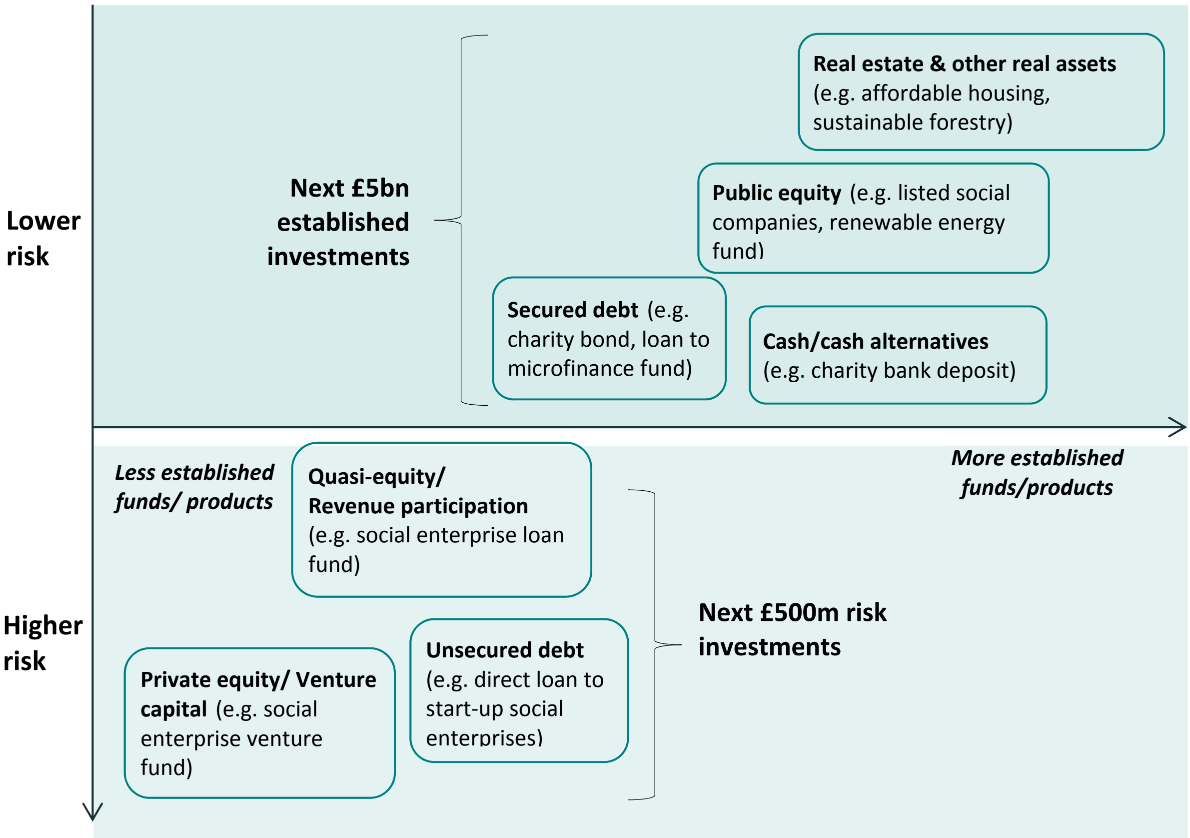
---

[28] Brown & Swersky (2012).

[29] As noted in the executive summary, these two financial thresholds of circa £500m and circa £5bn are presented as approximate markets, to help guide an understanding of how demand for different types of finance in the social investment market might be met through different activities and different sources.

Conversely there are some investors, such as the family offices and charitable foundations interviewed, who consider social investment as a potential complement to philanthropic grants, and will only engage with the market if the investment is made exciting and clearly supports innovation (therefore being more likely to invest in 'riskier' social investment opportunities, providing the next £500m in risk capital).

Figure 6: Example social investment opportunities in different asset classes and at different 'ends' of the social investment market spectrum



Clearly then, these findings suggest that a key factor to help increase levels of social investment interest and activity among institutional investors is to understand the different drivers which play a role in shaping their investment decisions. The research findings suggest that, with a few exceptions, most investors have one primary objective for their assets, which either will or will not enable compromise on financial returns to achieve impact. Tailored approaches which reflect these different mind-sets would need to be developed to help grow the engagement of institutional investors with the social investment market.

2.3. Social investment 'personalities'

There are seven personality types which influence investors' approach to social investment.

Considering the above analysis, it is possible to categorise organisations interviewed for this research into 'personality types' which reflect their emotional attitude and approach to social investment as well as more practical considerations. These seven 'personalities' are detailed in Figure 7 – five take an active role in making investments, and two are passive and typically defer, or react to others. Some personalities are more likely to occur in certain investor groups than others (see Table 3). Understanding the personality types is paramount when engaging with investors and considering what the emotional, non-structural limitations on growing the market might be.

Figure 7: The seven social investment personality types

Returns negotiable and social impact prioritised

Active personalities

'Go the extra mile'

These individuals want to believe that social investments can deliver competitive financial performance and are prepared to work harder to find opportunities to do just that. They care about the success of the sector and the impact of their finances, and if it means taking on additional risk, spending additional time or – in the short term – making below-market return rates, they will do it to pursue the bigger goal. Their whole portfolio is open to social investment opportunities, although most will not make their portfolio exclusively social.

'Allocation but not integration'

This group wants to engage as pioneers in social investment and are committed to the market but remain wary of potential risks. These investors have made an allocation for social investments within their portfolio and will make financial trade-offs with this portion of their assets. However, the rest of their portfolio is 'off-limits 'at present.

Finance threshold

'Benefit of the doubt'

This group of investors wants social investment opportunities to meet a comparable investment profile to traditional investment opportunities and then, all things being equal in terms of performance, they will prioritise social over conventional investments.

'All being equal but…'

This group thinks of themselves as the same as the '*Benefit of the Doubt'* investors but in practical terms find it difficult to engage with social investment. They tell themselves that if all were equal, they would prefer social investment but their inherent discomfort with their own knowledge means such opportunities cannot command the same confidence as more traditional ones. They are highly unlikely to make social investments, though they have no formal policy against it.

'Conceptually implausible'

This group has a strict investment structure which they see as counter to social investment, and which make specific social investments feel impossible. The most common issue is heavy investment in funds that don't/won't/can't include social criteria so they have no flexibility to engage within their current strategy, which they are committed to. There is also a sub-group that sees legislation as a key hurdle, the general attitude being "So long as we have to maximise returns we can't look at social investment because screening means less choice , which means limiting return opportunities."

Passive personalities

'Don't leave me behind'

This group is stronger in some sectors than others. In this group, no one will want to be the last fund in their sector that doesn't have a good answer to why they aren't socially investing when others are. Social investment is considered somewhat of an inconvenience – something they may have to react to if everyone else does, but they'd prefer to get on with their jobs otherwise.

'Ask the finance guy'

This group devolves autonomy to money managers, specialists, lawyers or financial advisers and hold themselves unaccountable for questions over social investment. Many organisations have advisors who emphasise the regulatory challenges and that it's best to stay away from social investment if you want maximum financial return. This group see themselves as detached from a responsibility to engage with the market, having a qualified representative who generally doesn't include social investment in the portfolio.

*Personalities most likely to contribute to next £500m risk finance**

Personalities most likely to contribute to next £5bn established

Returns non-negotiable and social impact not necessarily prioritised

Table 3: Social investment personalities matched to institutional investors

Investor group	Key personality type(s)
Charitable organisations	• 'Allocation but not integration'; • 'Benefit of the doubt'; • 'All being equal but…'; • 'Ask the finance guy'; • 'Don't leave me behind'
Corporations	• 'Allocation but not integration'; • 'All being equal but…'; • 'Don't leave me behind'
Faith-based organisations	• 'Benefit of the doubt'; • 'All being equal'; • 'Ask the finance guy'; • 'Don't leave me behind'
Family offices	• All seven personality types
Housing associations	• 'Go the extra mile'; • 'Allocation but not integration'; • 'Benefit of the doubt'; • 'All being equal but…'
Insurers	• 'Benefit of the doubt'; • 'All being equal but…'
Pension funds	• 'Allocation but not integration'; • 'Benefit of the doubt'; • 'All being equal'
University endowments	• 'Benefit of the doubt'; • 'All being equal but…'; • 'Conceptually implausible'

2.4. Institutional investors' perceptions of social investment and the barriers to engagement

As illustrated in section 2.1, there is clear potential for the institutional investors examined here, to provide capital to the social investment market, with some groups already doing so. In addition, interviews with key representatives from each investor group, revealed an interest in social investment and the potential to become more actively involved with the market.

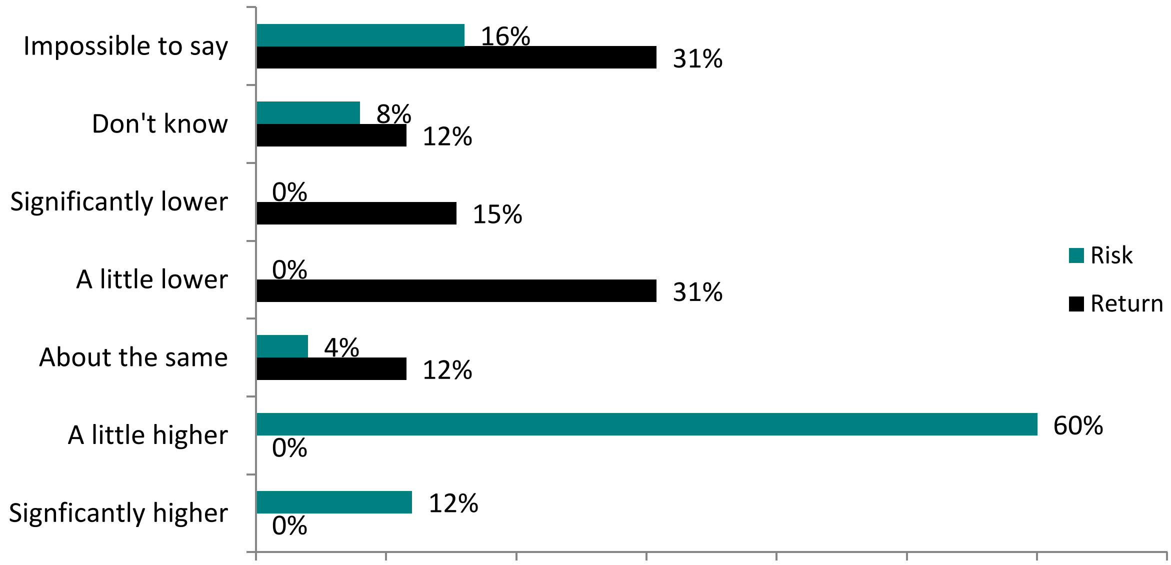
However, investors also identified a number of key considerations and challenges which they perceive as barriers to their involvement with the social sector. These are explored in detail below.

2.4.1. Perceptions of the risks

Institutional investors feel uncertain about the performance of social investment products, partly linked to a lack of performance track record in the market. This leads to perceptions of social investments as 'high risk'.

Figure 8 compares responses to a question on risk perception of a social investment vis-à-vis a developed market bond, to help pinpoint investors' views of relative risk. It shows that the majority of investors interviewed (72%) view social investments as riskier than conventional investments because they are relatively new and unproven – there is a degree of uncertainty around them. When asked for their impressions of the performance of social investment products[30], over 40% of interviewees feel it is either 'impossible to say' or that they 'don't know' how returns would compare against equivalent financial products. Whilst it may seem encouraging that there are a number of 'on the fence' respondents who should be open to influence, this group is actually divided between those who are resistant to considering social investments because of the lack of information available, and those who feel that they have a lot of information and are making an informed analysis in stating it is 'impossible to say'.

Figure 8: Perceptions of typical risk and return profiles of social investments vis-à-vis developed market bonds



For institutions for whom compromising financial returns is not an option (frequently the case for large investors who have clearly defined income requirements and risk profiles they are legally bound to manage), social investment can therefore present challenges. Interviewees consistently identified that they seek a track record on which to base investment decisions, and that this is largely lacking within the current marketplace (see also Figure 9). This is partly linked to the nascent nature of the market - and with more social investment funds coming into existence, there are more opportunities for performance and proof of concept to be developed. However, others feel that while they have seen some track record, it is not sufficiently strong to merit their attention. The investment advisers interviewed also commented that in some cases, even within those social sectors offering larger investment opportunities – such as clean tech and microfinance – investment performance has at times been lower than expected[31]. This is not to say that modest, positive track records in these sectors will not be able to attract institutional investment, but rather that the risks and returns on offer may not appeal to those who invest primarily to maximise returns.

---

[30] NB. Question was asked in two parts: (1) Thinking about the social investment products you've heard of, do you think the typical investment performance of these products is higher, the same or lower than developed market bonds? (2) Thinking about the social investment products you've heard of, do you think the typical risk profile of these products is the higher, same or lower than developed market bonds?

[31] For example, while the global clean tech sector has shown overall positive growth since the financial crisis, the sector is characterised by a high turnover of companies (e.g. globally, the sector saw the creation of 68 new public pure-play clean tech companies in 2012 and the loss of 63, representing a churn of over 20%) and is significantly impacted by external factors, such as government subsidies and stimulus funding which can rapidly influence growth sectors and profitability. See Ernst & Young (2013).

2.4.2. It is important to unpack the different aspects of the social investment market

Confusion around definitions of social investment and investment products also underpins perceptions of the market as 'risky'.

Many respondents expressed a lack of clarity around what is meant by the term 'social investment'. Several interviewees who rate themselves as having good knowledge of the market suggest that lower-risk products with track records can be found if the definition of social investment is considered to include, for example, microfinance and social housing bonds. However, given the wide spectrum of asset classes and products with different track records included under the 'social investment' label,[32] interviewees generally feel there is no clear, identifiable track record or risk profile for the market as a whole.

"The managers don't have enough track record to answer that… Though the message is you're targeting benchmark returns or a little below. They're riskier because there's no established track record." – Corporation

This lack of a clear definition of what comprises social investment tends to lead the less-informed to assume it is inherently riskier than other investments. In addition, the focus by industry press and the market itself in recent years on profiling more innovative social investment products such as social impact bonds and investments in social enterprises, has – whether intentionally or not – generated an association with newness and unfamiliarity in the minds of institutional investors. Many commented that they feel the sector is risky because it is largely 'new' and 'unproven'.

This reinforces the idea that thinking of the market as a spectrum offering two types of opportunity at either end - its more innovative investment options end (next £500m) and its more established options end (next £5bn) - can be beneficial in developing a dialogue that institutional investors can understand, to encourage their engagement with social investment. Investors can then be matched to social investment options according to their motivations and investment attitude. Such a targeted approach would help to maximise the likelihood of investors' engagement with the market.

2.4.3. Lack of accessible information and advice

Investors feel unfamiliar with social investment and therefore unable to make informed investment decisions.

Investors were asked to rank to what degree different factors are barriers to their organisation's ability to make social investments (see Figure 9 for aggregate responses)[33]. Across all institutional investor groups, the most common barriers cited are (1) unfamiliarity with the sector, (2) lack of a track record of financial return, and (3) perceived risks. These responses dovetail closely with the overriding perception that social investment is a 'new' and 'unproven' sector, about which institutional investors do not feel they have an acceptable level of knowledge. As one pension officer explained, "The biggest risk to an investor is not understanding what you are investing in."

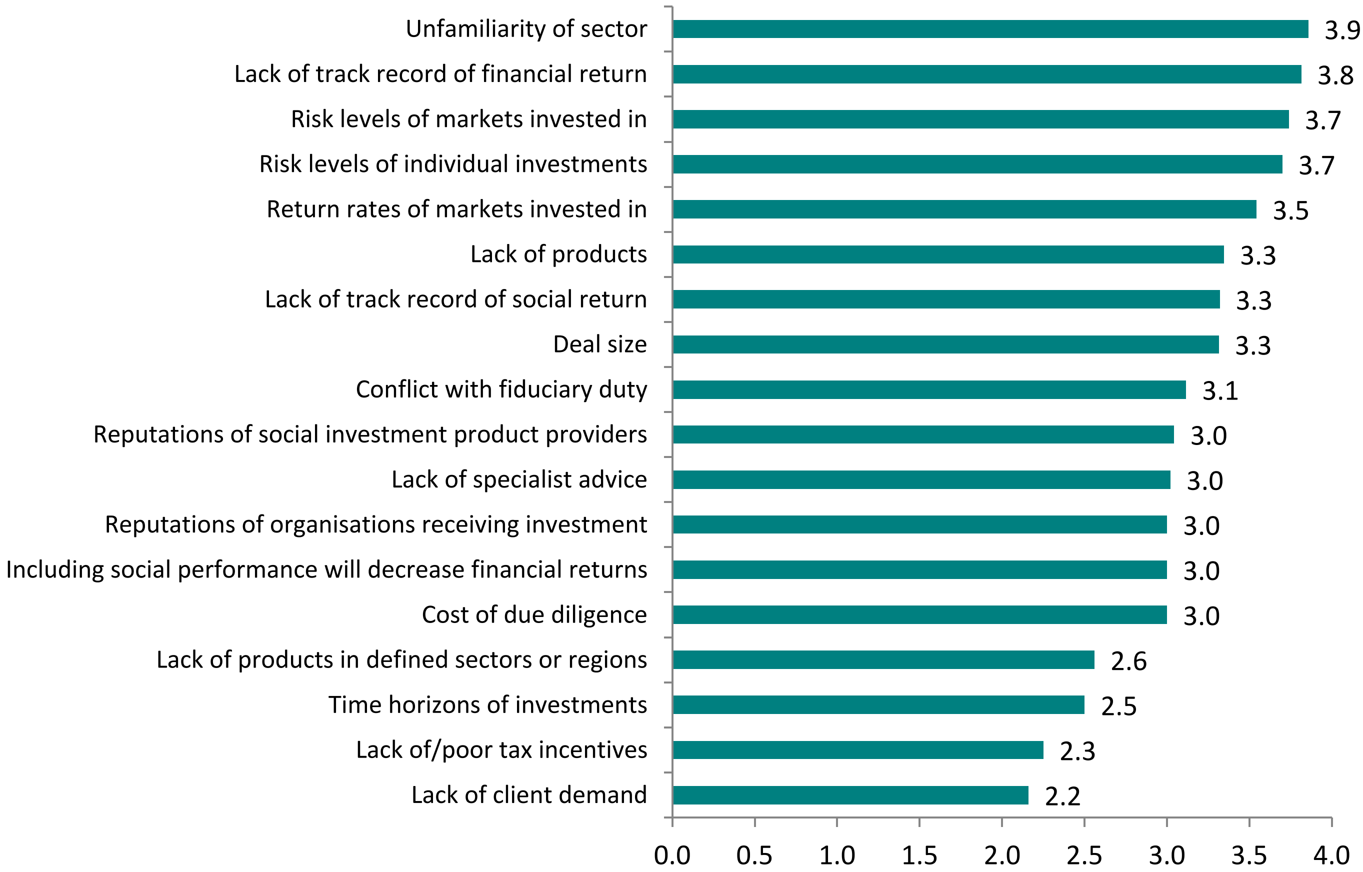
The main barriers identified by institutional investors here correspond with those identified by other investors in previous research. These include the need for an acceptable return rate, considerations

[32] Within the interviews, 'social investments' were defined broadly as any investments that intend to create positive social or environmental benefits in addition to financial return. As such, more established asset classes such as microfinance and sustainable forestry were included in the discussion.

[33] Interviewees were asked to rank to what extent each of the elements listed was a barrier to their organisation's ability to make social investments or do more social investment. 1 indicated low significance and 5 indicated a barrier being highly significant.

around deal size, and perceptions of risk levels where a track record is not yet available/only starting to emerge. Some of the barriers (such as compliance or due diligence), if carried out internally, can be hard for market players to tackle from outside the institution. Figure 9 also shows that the investors included in this research perceive there to be a shortage of investment opportunities, which in part may be because of the lack of specialist advice bringing opportunities to their attention. It is necessary to raise the visibility of social investment opportunities among institutional investors, and critical to this will be to work with advisors to ensure social investment is considered in their portfolio. This point around availability of information and awareness of investment opportunities, is reflected again later in the research, in considering investors' preferred product characteristics (see Figure 11) and the need for asset owners to set the agenda (see section 2.4.7)

Figure 9: Barriers to making social investments



NB. Values represent average scores on a scale of 1-5, with 5 indicating this was considered a highly significant barrier.

2.4.4. Return and familiarity are key

Interviewees were presented with example social investment products and asked which they would most likely invest in (see Table 4). The products were presented to interviewees first without, and then with, their expected return profiles. Some of the products offered deliberately below market returns while others performed competitively. The products are organised by whether they would potentially contribute to providing the next £500m in risk finance for the sector or the next £5bn in established social investments, though the opportunities were not presented to interviewees along this split.

Table 4: Preferred social investment products

Product description		Number of respondents selecting product
Example products contributing towards the next £500m risk investments		
Sustainable Growth Fund: A 10-year, limited partnership providing growth equity to SMEs in sectors with underlying social or environmental needs. Typical subscription £5m, max. subscription £10m.	*First preference*	7
	Return information: Successful exits to date have range from 12-16% IRR.	9
Healthcare Fund: A minimum, 5-year, limited partnership providing equity or equity-like capital to social enterprises at all stages of development that will help improve access and quality of healthcare provision, especially for the most disadvantaged. Typical subscription £5m, maximum subscription £12m.	*First preference*	9
	Return information: Successful exits have ranged from 3-4% IRR.	2
Community Finance Business: A 5-year, direct equity investment into a Community Development Finance Institution (CDFI) providing affordable financial products and services to financially excluded individuals. Typical subscription £100k, maximum subscription £500k.	*First preference*	5
	Return information: Expected to repay capital with return profile of <1%.	3
Example products contributing towards the next £5bn established investments		
Sustainable Forestry Fund: A 15-year, limited partnership private equity fund focused on sustainable forestry management. Typical subscription £5m, maximum subscription £20m.	*First preference*	8
	Return information: Expected return profile circa 14-16%.	8
Microfinance Fund: A minimum 5-year fund focused on increasing access to financial products and services for low-income people through providing equity and debt finance to microfinance institutions. Typical subscription £500k, maximum subscription £5m.	*First preference*	5
	Return information: Expected annual return of 6-9%.	4
Charity Bond: A 5-year, ethical savings bond with a capped return selected by the investor. Any additional returns are distributed to a charity of the investor's choosing. Typical subscription £1-2m, maximum subscription £20m.	*First preference*	1
	Return information: Capped return offered currently up to 10%.	0

As Table 4 shows, the UK-focused Healthcare Fund is the most popular investment product on initial consideration. Respondents expressed they feel healthcare is a growing sector in the UK and hence an interesting investment opportunity. However, once provided with the return profiles for each of the products, interest in the Healthcare Fund drops off significantly, and the two most preferred products are those offering the highest returns – the Sustainable Growth Fund and Sustainable Forestry Fund.

Knowledge about the investment sector tends to fuel initial interest, though return rates are the ultimate determining factor when all information is available. This general approach of making investments in areas investors have access to knowledge about is summed up by one pension officer in explaining his product preferences:

> *"The ones that are of interest [microfinance and sustainable forestry] are because they are more established asset classes. We feel we could get a better understanding of them and look at data etc. I would have thought they could be good diversifiers for our current portfolio. The others I have little understanding of and am not sure how much understanding could get."*

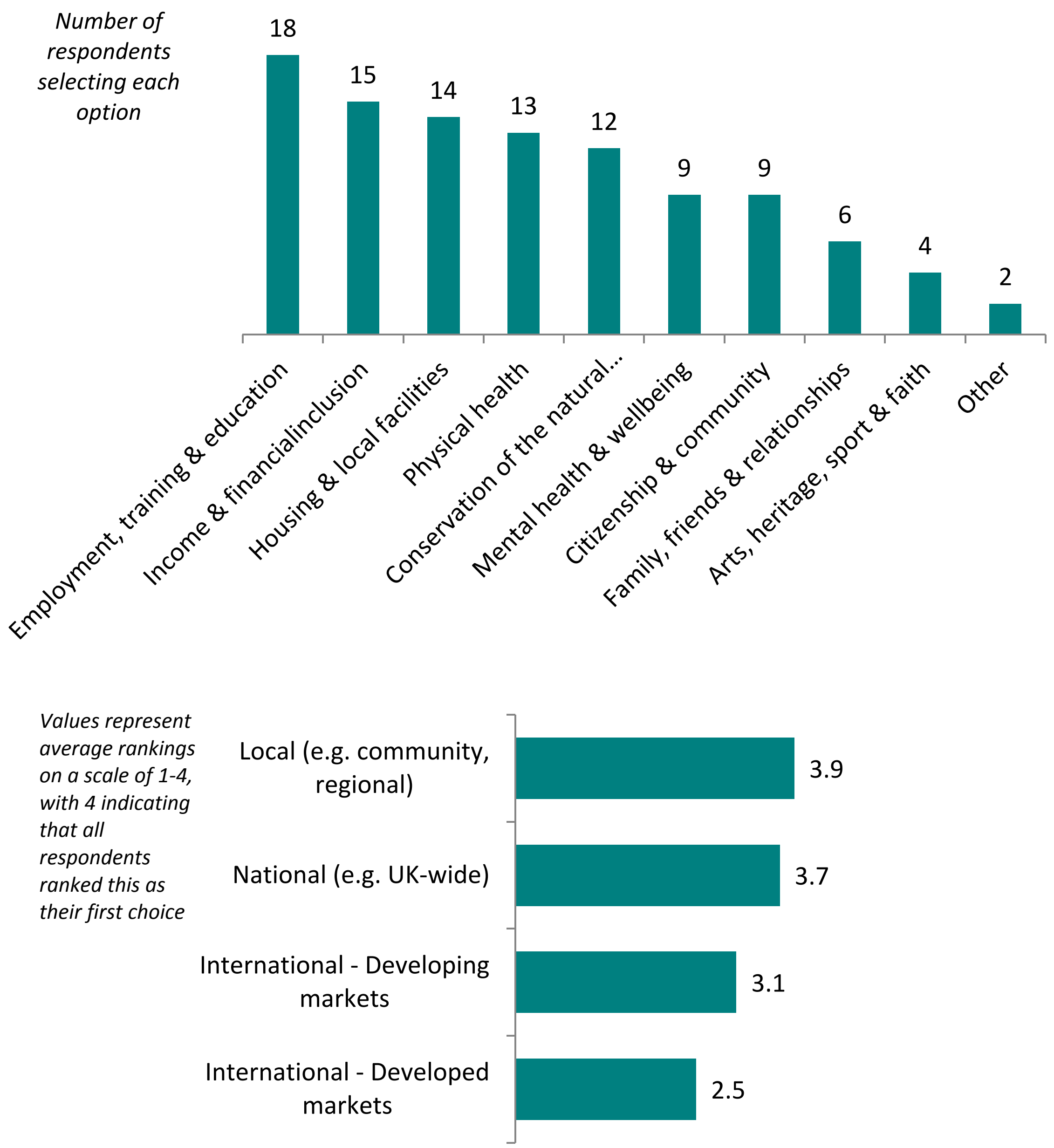
2.4.5. Social investments need to be aligned with current activities

Investors were asked about their attitude toward preferred geographies or cause areas for making social investments[34]. The overwhelming trend is the closer to their current activities, the better. Local and national (UK) investment opportunities are prioritised over international opportunities, which fits a broader pattern of investors looking to invest in things they know well and/or where they can exercise oversight easily. However, the response set is influenced by housing associations and local authority pension funds which, by their nature, have a local focus (and in the case of housing associations, some of which are charities, there are legal requirements to invest in accordance with core mission objectives).

It is not a surprise therefore that the sectors that most appeal to the investors interviewed tend to be those which they have an inherent professional connection to – with employment, training & education; income & financial inclusion; and housing & local facilities being the most popular target areas for making social investments (see Figure 10). Those investors who have active grant-making portfolios – such as charitable foundations, or housing associations with budgets for community programming – look to make social investments in the same sectors as their current grant-making (in line with legal obligations to consider core mission and programme objectives when making investment decisions). At the other end of the spectrum, those who are more commercially-driven, tend to want to make social investments in the same areas as their commercial investment activity, such as local authority pension funds wanting to make investments in regional infrastructure projects. In the case of the latter, this ties in to the fact that such investments are in the interests of the pension fund beneficiaries. That is, these investments seek to benefit local authority employees, (indirectly, through investment in local areas), who in turn are the beneficiaries of the pension funds.

[34] NB. Interviewees were asked, 'If your institution were to make/is making social investments, would you have any preferred sectors or geographies?' and presented with the options above. Sector categories are adapted from Big Society Capital's Outcomes Matrix. See: http://www.bigsocietycapital.com/outcomes-matrix

Figure 10: Preferred sectors and geographies for social investments



2.4.6. The people matter

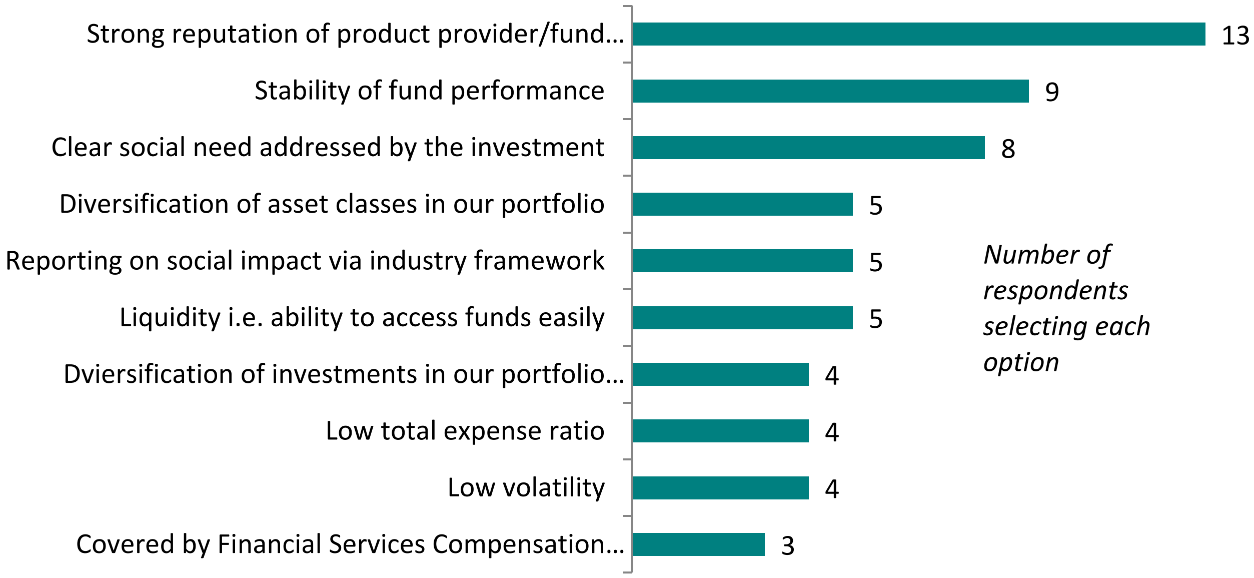
A strong credible reputation among product providers and fund managers is key to influencing investment decisions, more so than the product. However investors feel there is a lack of credible information sources and are therefore largely unaware of suitable investment opportunities.

Investors' perceptions that the social investment market is 'new', 'unfamiliar' and 'risky' can also be linked to the fact that investors feel lacking in their own ability to make educated decisions, and that there is an absence of accessible marketplace advisers.

This is reflected in the finding that, when asked what product characteristics would be most important when considering a social investment, interviewees identified 'strong reputation of product provider/fund manager' as the most common influencing factor (see Figure 11). There is a lack of awareness among the institutional investors interviewed of credible advisers and funds (where credibility is based on previous experience and track record). This represents a key barrier to investment. It is not surprising then, that investors consider the manager of a fund or product more important than the product itself i.e. a track record, familiarity and credibility from the provider of the investment opportunity, are most valued by investors when making investment decisions. Many institutional investors are prepared to sacrifice product track record if the product is provided by an organisation and/or adviser who brings with them a track record of strong performance.

This challenge around the need for credible product providers/lack of awareness of reputable investment opportunities, might be linked to the difficulties in undertaking due diligence in propositions in the social investment market. This implies that efforts to market products to institutional investors might be more effective if done by established names and investment houses.

Figure 11: Preferred product characteristics



Connected to the perception that there are few sources of credible advice of which investors are aware, there is a strong feeling that learning about and/or sourcing social investment opportunities is disproportionately resource-intensive relative to the size and number of investment opportunities available at present. This perception is driven by the feeling that there are few places to find and compare available deals, that the information available is not comparable to the documentation institutional investors are used to reviewing, and that the market as a whole is difficult for non-experts to understand and navigate.

2.4.7. Advisers are key influencers, but asset owners set the agenda

There is confusion among asset owners and advisors as to whose responsibility it is to identify social investment opportunities, which leads to a lack of awareness where suitable opportunities arise.

From the above discussion it is clear that the institutional investors examined in this research, generally feel unable to make educated investment decisions; are confused about what social investment actually means; and feel there is a lack of accessible, credible advice to assist their decision-making. This challenge around a lack of information and awareness of investment opportunities is dual-pronged, in that investors first find it difficult to identify credible advisors and second, social investment generally does not feature strongly among advisers' portfolio of recommendation.

Considering the importance of credible advisers and information, it is notable that the research found that typically, the larger an investment portfolio and/or the less in-house capacity an institution has to manage its investments, the more likely the institution is to be working with intermediaries to make investment decisions. Investor groups most likely to be using financial intermediary structures are universities, charitable organisations and faith-based organisations, and also some pension funds and family offices.

Financial intermediation involves asset owners delegating responsibility for investment decisions to asset managers, with investment consultants and others playing supporting roles in arriving at decisions. The asset owners' wishes are generally codified in investment mandates, which direct asset managers on how the portfolio should be invested.

Interviews with investment consultants and advisers working with institutional investors reveal a lack of clarity about whose responsibility it should be to demand or supply social investment opportunities. Asset managers generally feel it is the responsibility of asset owners to set out their goals related to social investments, and that it is not their role to suggest social investments, in the absence of this being raised as a priority by the asset owner. As one investment consultant expressed, *"We have a part to play in this debate, but it's not our job to sell this to clients. There is no mandate to talk to all clients every year about [social investment]. Clients set committee agendas."*

> *"My advice to other pension funds looking to do [social investment] would be that it starts with the trustees, challenge your consultants, get an allocation, and then look at how to invest that allocation." - Local authority pension fund investment officer*

Furthermore, asset managers face a slew of incentive-based, regulatory and other barriers that make it difficult to consider social investments where there is no clear mandate from clients to do so. For example, an asset manager interested in making social investments may worry about the impact such investments will have on the returns of their fund relative to the benchmark against which the fund is evaluated, but not know where to find the information to address this concern. These factors point to the view that it is the responsibility of asset owners to 'demand' social investment, and therein create an obligation for asset managers to become knowledgeable on and source suitable investment opportunities.

However, interviews with asset owners who have delegated responsibility for executing investments to asset managers, reveal there is no such clarity on this question of roles. A few institutions expressed that they feel disempowered to look at social investments until asset managers bring them opportunities to consider. These institutions tend to be among the more cautious, 'passive' investor types, and trust asset managers to know better than themselves which investment opportunities are compatible with the portfolio targets and strategy.

Confusion is disempowering, and this evident lack of clarity on who is responsible for suggesting and/or demanding social investment, presents a barrier for many asset owners and managers, preventing an initial conversation around whether social investment may be a possibility. This trend suggests that the most practical route for engaging more investors who do not manager their assets directly, lies in educational efforts focused on asset owners. For example, clearly communicating to asset owners that they hold the responsibility to lead on social investments and offering practical advice on how to do so – such as on how to codify a preference for social investments in an investment mandate or create an allocation within a portfolio.

2.4.8. Social investment doesn't (necessarily) follow ethical/socially responsible investment

Investors disassociate ethical/socially responsible investment and social investment. Doing one does not necessitate a natural 'stepping stone' to the other.

It had been hypothesised that investors might make a linear progression from practicing ethical/socially responsible investment strategies[35] to considering social investments. Unexpectedly then, the interviews highlighted that there is seemingly little correlation between the two, and that institutions with strong ethical investment practices and/or social missions seem to be approach this as distinct to social investment.

On the one hand, many institutions who do not apply any screening to their investment portfolios see no reason why they can't still invest in something that is socially positive, particularly if it provides a good financial investment opportunity or could be supported through a philanthropic allocation. Alternatively, while investors who apply negative and positive screens to their portfolios see this as good investment practice, social investments which involve some sacrifice on returns, is not seen as good investment practice.

On the whole, ethical investors – which include a number of faith-based organisations as well as some charities – recognise the opportunity to achieve their organisational mission through investment. This tends to be through a more passive approach – by prioritising investment opportunities which avoid any negative impacts and/or are aligned with organisational values, rather than investments which create direct impacts. This suggests that SRI is not an obvious 'stepping stone' towards social investment and therefore the approach to engage investors in social investment needs to be made independently of investors' SRI portfolio holding, even though there may be some overlap with the investor base.

2.4.9. Social missions influence investment decisions

Investment decisions are shaped by institutional investors' core social missions and must be in alignment. In some cases then a social investment opportunity might not meet mission requirements, despite having a positive social impact, and cannot be taken up.

Another interesting finding is that institutions with identifiable, core social missions – such as university endowments and faith-based organisations – are not necessarily more predisposed towards social investment than other investor groups. This is particularly the case among university endowments - managers generally agree that the purpose of the fund's assets is to generate sufficient funds to finance the institution's activities and ensure its longevity and long term sustainability foremost, rather than to support external mission-led organisations. For such investors, the need to meet core organisational mission objectives through their investment portfolio means that while being socially-driven, these organisations are also required to maximise financial returns from their investment, for the long term sustainability of their organisation.

The exceptions to this trend are some charitable foundations and housing associations that have allocations for supporting community activities and/or making grants to external organisations to achieve impact. These investors do see an opportunity to consider financial trade-offs to make social

---

[35] Ethical or socially responsible investments (SRI) policies generally apply negative screening criteria to avoid investments in certain industries that are considered harmful – such as tobacco or armaments – and/or may also apply positive screening criteria to target investments in companies or industries based on strong environmental, social or governance practices.

investments in the same areas as their current grant-making or community investments, once again in line with the law on programme-related investments.

2.4.10. Summary of investor perceptions

The analysis in this section suggests there are a number of considerations which institutional investors perceive as barriers to their engagement with social investment. A number of these can be linked to overarching themes – lack of education, awareness and therefore certainty; limitations from having to prioritise other factors such as financial returns or core mission; and an emphasis on credible sources of advice and information.

2.5. How to create transformation and grow the market

- Among institutional investors there are perceived challenges to social investment.
- These are not insurmountable and there are also opportunities for engagement. These can be divided into opportunities to engage as providers of the next £500m in risk finance, and/or as providers of the next £5bn in established investments.
- The next £500m in risk finance is most likely to come from housing associations, charitable organisations, family offices and corporations (in no particular order), with potential interest from insurers in the longer term.
- Charitable organisations, family offices and pension funds (in no particular order) are most likely to provide the next £5bn in established investments, with potential interest from faith-based organisations and universities in the longer term.

The analysis in section 2.4 highlights that in many areas, the social investment market does not meet institutional investors' expectations or their needs. A lack of track record, uncertainty about market performance and sometimes lower levels of performance than some commercially-focused institutional investors might be looking for, are particular barriers to engaging investors who are already reluctant to make financial trade-offs. This also raises wider questions around improving the financial performance of the social investment market; which, though important, is beyond the scope of consideration in this research.

Despite such challenges, there are opportunities for new institutional investors to engage with the social investment market. On the one hand, even without significant change, social investment levels are likely to increase modestly as more investors seeking to generate social impact (i.e. those likely to provide the next £500m in risk finance), connect purpose-driven assets to purpose-driven investment opportunities. Opportunities also exist for the more conventionally-minded investors (i.e. the next £5bn of investment) - those social investment opportunities which are more in line with conventional investments need to be emphasised and communicated better to investors, so they are more accessible, in the way all financial investment opportunities should be. This also links to one of the findings that institutional investors require better clarity around how social investment is defined and what it means, for them (see section 2.4.2). This could help to accelerate the pace and size of the investments in the near future.

It is arguable then, that strategies to grow the social investment market need to be developed with a view to bring investors in at the most appropriate 'end' of the social investment market, given their personality types and investment requirements. It is outside the scope of this research to explore which option is most effective for the market – i.e. whether it is better to get as many new investors into the market as possible and, by extension, look to grow both ends of the market simultaneously, or prioritise identifying investors for one end of the market where need is greatest. However, there is evidence that the largest gap between available sources of finance and demand in coming years is likely to be at the risk-equity end of the market.[36]

2.5.1. Which institutional investors are most likely to engage with each 'end' of the market

Table 5 indicates which of the eight institutional investor groups examined in this research, might be the most likely sources of capital – both the next £500m and the next £5bn – for the UK social investment market. Though helpful in identifying which investor group might be most likely to engage with the market, it is worth bearing in mind this analysis is indicative of expressed interest among interviewees, themselves a small sub-sample of the institutional investor population.

Table 5: Indications for institutional investors most likely to engage with each 'end' of the social investment market

Next £500m in risk finance	Next £5bn in established social investments
Most likely to come from:	**Most likely to come from:**
• Charitable organisations (using social investments as a tool to help deliver their missions) • Corporations • Family offices • Housing associations	• Charitable organisations (using social investments as a tool to help deliver their missions) • Family offices • Pension funds
Potential interest in the longer-term from:	**Potential interest in the longer-term from:**
• Insurers	• Faith-based organisations • University endowments

The research indicates that faith-based organisations and university endowments generally prioritise their investment decisions in direct accordance with their core social mission and maintaining the long-term sustainability of their organisation. Therefore while they are not among the investor groups most likely to provide new sources of social investment capital in the near future, they are interested in social investment and should not be overlooked in attempts to encourage investor engagement with the market. In the longer term, the most likely entry point to social investment for faith-based organisations and university endowments will be through commitments towards the next £5bn in established social investments end of the market. For faith-based organisations, managed funds offer exposure to more established social investment products in areas that match with their broader ethics, such as investment opportunities in environmental funds (e.g. sustainable forestry) as well as community infrastructure, and potentially microfinance. Universities are most likely to invest in opportunities that offer competitive returns.

While insurers are similarly focused on ensuring their investment strategies match their long-term liabilities to customers, they are more likely to make long-term investments in-house rather than into marketed social investment funds. Therefore insurers, as consumer-facing businesses, might

[36]Forecasting demand for social investment, it was found that demand will be focused on higher-risk financial products, such as unsecured lending and quasi-equity, as commercial capital providers will steer clear of supplying these products to social sector organisations due to their limited understanding of social business models. Consequently, this is the area where social investors are most needed to fill the gap in supply (Brown and Swersky, 2012).

potentially be engaged to provide risk finance to social sector organisations through CSR finances rather than investment activities, towards the next £500m end of the market.

2.6. Sources of capital for the next £500m in risk finance

This section provides detail on how to engage the most likely sources of capital for the next £500m in risk finance. The following section provides an overview of likely sources of capital for the next £5bn of investments into more established asset classes and social investment products. It is not obvious that one end of the spectrum is necessarily more 'ripe' or achievable than the other at this stage, though this might change if momentum is gained in specific investor groups or markets.

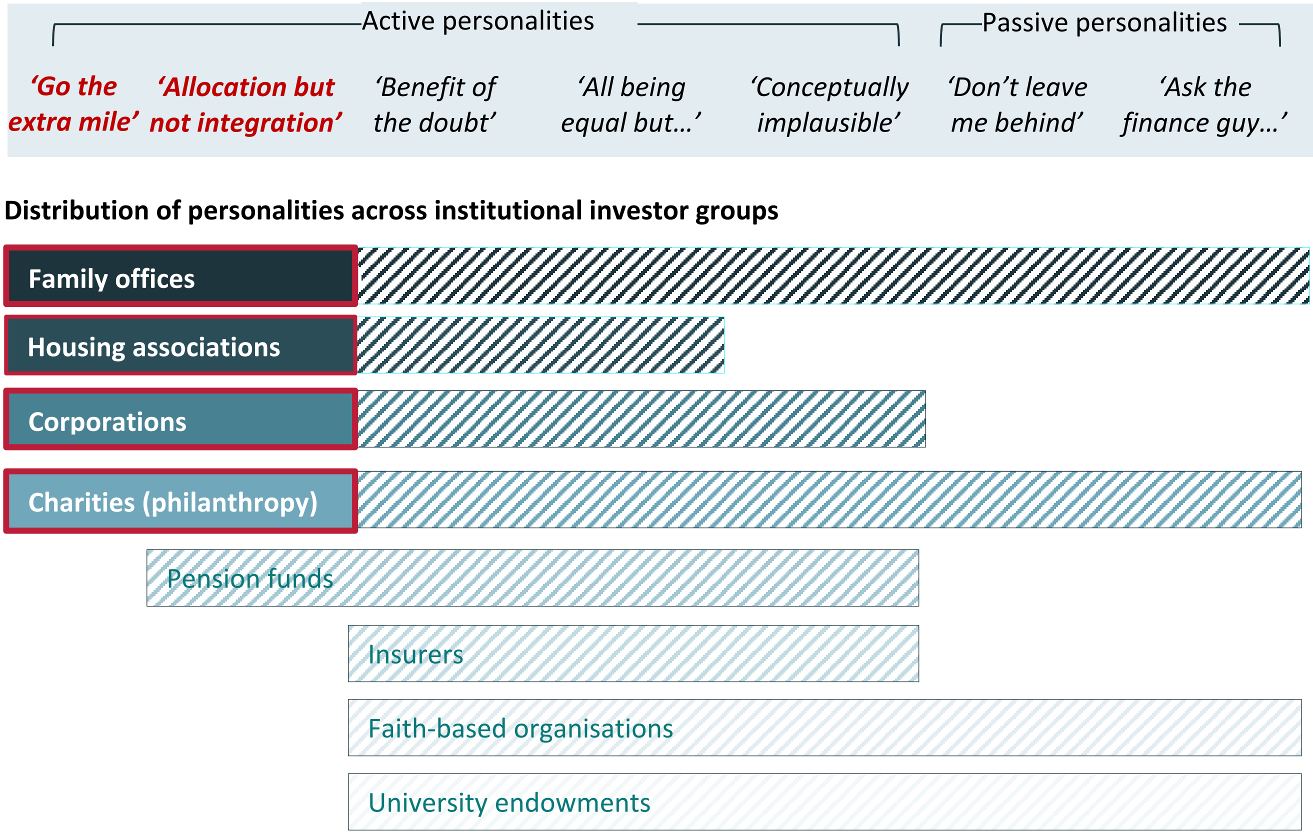
Growth for the £500m risk finance end of the market is most likely to come from investors who currently fit or can be moved to become 'Go the extra mile' or 'Allocation but not integration' social investors (see Figure 7). These are investors who have the degree of control over their assets to consider being flexible on financial returns with a portion or all of their portfolios, and who are motivated to consider impact as an objective of their investments. Given the absorptive capacities at the risk finance end of the market, these will likely be medium-size institutions capable of considering six-to-seven figure deal sizes, or institutions of any size that can consider making such commitments through dedicated philanthropy and/or community investment portfolios.

Figure 12 summarises the distribution of personalities across the eight investor groups examined in this research, with those most likely to be sources for the next £500m in risk finance highlighted in bold. The largest concentration of 'Go the extra mile' investors at present are found among a subset of **family offices** and **housing associations** who believe strongly in social investment and are able to consider integrating it across their approach to investing or enacting service delivery.

Additionally, there are a number of investor groups with active philanthropy portfolios – **charitable foundations, corporations** through their CSR programmes, and family offices – who have set aside a portion of their finances to be 100% impact/0% return, which can potentially be shifted into social investments. It is these investor groups which will prove the most fruitful sources when looking at where to raise the next £500m of risk finance investments.

The following sections set out specific steps that could be taken to encourage active engagement by these four investor groups to raise the next £500m in risk capital for the UK social investment market.

Figure 12: Sources of capital for the next £500m in risk finance



2.6.1. Steps to engage family offices

Recent sector developments suggest there is potential for family offices – and the associated businesses and foundations that they may control – to become major contributors to social investment. The family office sector is made up of highly individual organisations that span the complete spectrum of attitudes toward social investment. Yet, with the most flexible 'fiduciary duties' of any group, family offices have the potential to approach social investment at scale.

As private institutions, family offices are not an easy group for external market players to engage with and also tend to be fairly insular in their search for recommendations and advice. As a result, **sharing of stories, ideas and experiences across peers** is likely to be an effective means of supporting an existing group of family office pioneers to create awareness among other family offices and pave the way for a larger, second wave of social investors.

Free access to information on social investment options and performance, and **profile-raising of those family offices that are leading the way would support such peer-to-peer sharing**. Some global platforms such as 'Ask the Circle', founded in 2009 by a Swiss family office, provide such a family office-only forum to share experiences and ask questions. Other networks - such as ClearlySo Angels and Tonic - are open to family offices as membership networks through which they can discover investment opportunities. However, many of the family offices interviewed for this research commented that having to pay to access such networks creates a challenge, particularly for those who are interested in learning about social investment opportunities but are yet to become 'Go the extra mile' personalities actually committed to allocating funds. **Building relationships and reputations** within the sector, **supporting regular closed, small events** to connect pioneering family offices with 'Benefit of the doubt' personalities, and then, **supporting family offices to talk amongst**

themselves will therefore help to mould their future activity within the social investment market (see chapter 7 for more detail).

2.6.2. Steps to engage housing associations

Housing associations are most interested in social investments that support their business activities or contribute to their community priorities[37], such as supporting increased employment and financial literacy amongst residents. Housing associations are already making innovative social investments and supporting the social sector[38], as a way to improve service delivery and fulfil their mission (see chapter 3 for more detail).

Developing case studies of social investment activity then, that can be shared across the sector, will help increase activity and awareness about utilising operating capital to procure from, partner with, or acquire new social business providers. As the housing association market does not have much spare investment capital but primarily reinvests operating surpluses back into core activities, specific examples of deals, local partnerships with social enterprises, and case studies of success will be key to help increase social investment activity.

Events which profile case studies of partnerships between housing associations and social enterprise will help to raise awareness and aid learning within the sector through others' experience. These and other tailored forms of engagement with housing associations would build on work previously accomplished at **workshops and at regular industry conferences.** Closed meetings between housing associations that are both doing and considering making investments into social businesses would also help to increase momentum among this investor group.

A **platform could be developed that matches social businesses to the locations, community priorities, and procurement needs of housing associations, to help ensure that partnerships meet both housing associations' and social enterprises' needs**. Such a platform could be made available on industry websites or in regular newsletters/publications profiling available investment and/or business partnership opportunities with social enterprises and social investment funds, which can be searched regionally or by focus area. This may well help identify more 'Go the extra mile' investors and support those who are already undertaking such activity to dedicate more operating capital to the market.

2.6.3. Steps to engage corporations

The research uncovered a subtle difference in corporations' approach to social investment, relating to the nature of their business operations. For example, financial services corporations are more likely to approach social investment by developing proprietary products, or setting up investment funds, in line with their core business. On the other hand, corporations providing goods and services are more likely to approach social investment as part of their CSR programme and/or philanthropic

---

[37] As noted previously, where housing associations are also charities, this approach to investment is in line with legal requirements for charities.

[38] London and Quadrant Housing for example in 2012 invested £10m in a social investment fund, the Real Lettings Property Fund – see 'Housing association puts £10m into social investment fund for homeless people', Third Sector Online, 6th November 2012. Available at: http://www.thirdsector.co.uk/Social_Enterprise/article/1158381/Housing-association-puts-10m-social-investment-fund-homeless-people/
See also Big Society Capital's blog post 'How housing associations are boosting the growth of the social sector', 28th November 2012. Available at@ http://www.bigsocietycapital.com/blog/how-housing-associations-are-boosting-growth-social-sector

activities. Currently little is known on this emerging pattern, so while it is of interest there is a need for further research in this area.

For the most part however, corporations' current engagement with social investment is found to be in the form of innovative philanthropy and staff engagement. While separate to 'real' commercial activity, given that there are a growing number of UK businesses getting involved in this space, there will likely be further growth in risk-finance social investments from this group. While the upper limit of businesses' corporate social responsibility (CSR) budgets indicates the net amount invested will be unlikely to exceed nine figures, proportionately corporations may well make up the biggest increase for risk investments of all the investor groups considered here.

Celebration and awareness-raising of corporations with successful and innovative social investment programmes will help encourage others to do the same. Although CSR has come to be an expectation of businesses, innovative models can be a point of differentiation – **positive press, awards and recognition for example** can help boards maintain, launch or expand investments in this area.

Corporations are also interested in **conversations with non-competitor businesses** which are successfully engaging in social investment, in order to share experiences and best practice. CSR departments and corporation foundations tend to enjoy sharing practice quite openly, in a suitable environment. Roundtable conversations between peers, as well as **publishing profiles of successful corporation social investment programmes** will likely be popular amongst businesses and lead to more confident action.

It also might be possible to create a **skilled volunteering and/or social investment incubator 'package'** particularly for medium-size businesses to help connect them with enterprises to mentor in their sector. Some pioneering companies have already set up such incubator programmes, such as Téléfonica's technology incubator Wayra which supports tech-based social enterprises[39], and Centrica, which has launched the UK's first energy-focused social investment fund in partnership with Wayra[40]. Businesses could be asked to commit capital into a growth investment fund, in a similar way to how Big Issue Invest and others have structured opportunities for corporations. This will help more businesses who are currently interested in social investment, but lack the capacity within their CSR functions or philanthropy budgets to set up their own funds to still get involved with the sector (see chapter 8 for more detail).

2.6.4. Steps to engage charities

Many charitable organisations are already looking at utilising social investment as a tool to deliver their outcomes. A few first-mover foundations already fall into the 'Allocation but not integration' personality type, and foundations collectively have allocated circa £100m+ into the market. At the same time, the research found that interviewees in the charity, faith-based organisations and universities groups, are more likely to be influenced by the actions of their peers than the other investor groups.

Inevitably, charities' approaches to social investment are influenced by the legal requirements governing how charity funds are invested[41]. Currently, the law is such that charities may either invest

[39] See: http://wayra.org/unltd/

[40] See: http://ignitesocialenterprise.com/

[41] In considering the legal obligations of charities and how this influences their investment decisions, it is also worth highlighting that most university endowments, faith-based organisations and many housing associations, are also charities in legal form – and therefore will also have to abide by the same investment duties as charities.

to further their charitable purpose and/or invest where the financial return is superior (i.e. maximised). Therefore, a social investment which is considered to fall outside a charity's charitable mission, with an inferior (financial) return, is not legally permitted. (It is worth noting that the Law Commission is currently reviewing charity law, and has published a consultation paper into charities and social investment[42]. While the paper does not suggest changing the governing principle that charities' investments should support their core purpose around providing public benefit (as this essentially is the reason for a charities existence), the Commission does recognise that some charities are uncertain about how to accommodate social investments alongside this principle, and proposes potential ways to address this, including introducing a new statutory power to make social investments, and the creation of a 'checklist' tool to aid charities' investment decisions. These and other proposals are under consultation however and as such the future outcomes are currently unknown.)

What is unique to charitable foundations is the opportunity to use their skill at creating social impact through their grant programmes, to establish how their combined uses of finance can help to complement their overall mission more effectively. The use of grants in social investment will certainly play a role in reaching the £500m higher risk capital either through underwriting, first loss, guarantee or as grants.

Charities' investment decisions also tend to be influenced by their peers. Therefore intimate **charity networks** can serve to build confidence in the market and lead to an **exchange of strategy and due diligence** that can lead to growth, as has been seen with the Social Impact Investors Group, co-chaired by four grant-making foundations, and which provides a valuable 'share and learn' opportunity for participants (see section 6.7). **Showcasing endowed charities that have used an 'Allocation but not integration' approach** to test the waters with their endowment capital, and arguably achieve impact more efficiently than otherwise, could also be a palpable way to encourage further activity. Similarly, profiling **case studies where charities have successfully recycled capital otherwise intended for grants** could encourage more social investments by charities at the risk end of the market (see chapter 6 for more detail).

2.7. Sources of capital for the next £5bn in established investments

Looking at where larger sums of money otherwise intended for mainstream, commercial investments could be raised, there are a few pioneering 'Allocation but not integration' personality types among **charitable foundations** that have created allocations for social investments within their endowment portfolios, as well as some **local authority pension funds** that have created allocations for social investments on their balance sheets (see chapter 10 for more detail on pension funds).

In both instances, these allocations are a small portion of these institutions' overall investment portfolios (i.e. less than 1%) and so pose little risk to overall returns, hence enabling these institutions to meet their fiduciary duties. However, given the scale at which many such institutions invest, such relatively small allocations can nevertheless add up to make a significant difference to the amount of capital available for the market. Given the minimum deal sizes required by such institutions, these institutions are likely to invest in areas that can absorb large deals – such as housing and infrastructure.

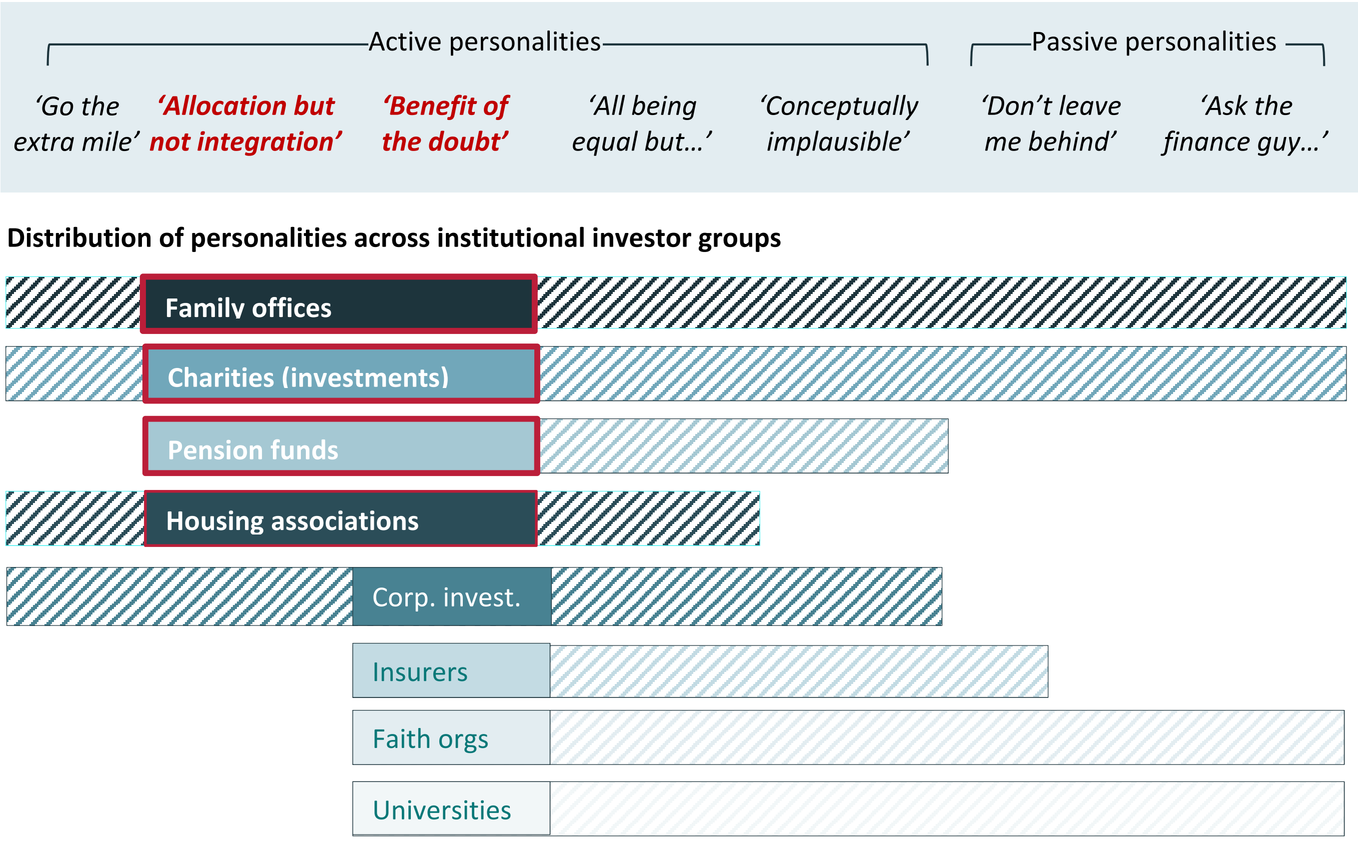
Figure 13 shows the distribution of personalities that are most likely to contribute towards growing the more established end of the social investment market (highlighted in bold). There is scope to

[42] The Law Commission review of charity law commenced in March 2013 and is ongoing at the time of publication. On 24th April the Commission published a consultation paper considering the legal framework for charities considering social investments. See: http://lawcommission.justice.gov.uk/areas/charity-law.htm

encourage more 'Benefit of the doubt' charitable endowments and pension funds to create allocations for social investment with a portion of their portfolios, through providing evidence and promoting the experience of peers who have already experimented with such an approach. In addition family offices and housing associations within larger, more established asset classes can potentially be engaged.

Family offices are highly individualistic organisations with greater control over their assets and – by extension – greater freedom to take a less conventional approach to investing. From a global perspective, family offices have been pioneer investors in many emerging asset classes, with many specialising in investing in, for example, alternatives or emerging markets. In the impact investment space globally, there have been instances of family offices structuring multi-million pound microfinance and green energy funds, suggesting that UK family offices may similarly be engaged to take a values-based approach to investing in these more established sectors.

Figure 13: Sources of supply for the next £5bn in established investments



There are additionally a number of 'Benefit of the doubt' personalities among the remaining investor groups – in particular, insurers (see chapter 9), university endowments (see chapter 5) and faith-based organisations (see chapter 4). These institutions may well be moved to consider social investments where they can be shown evidence of comparable track records, size and diversity of investment deals available alongside equivalent commercial opportunities. However, as there has been less movement in these groups to date, it is more likely that growth in the near term will be amongst those institutions that can be influenced by current peers' activity and experience to date.

2.8. Summary

This chapter provides an overview of the key trends across the eight investor groups explored in this research. While investors expressed an appetite to engage with the social investment market, the findings suggest there are also a number of areas for consideration. Briefly, these include:

- An understanding of the intentions underpinning investment decisions – are investors commercially-minded, prioritising financial returns or focused on achieving social impacts through their investments?
- In the case of the latter, a core social mission can actually act as a constraint to social investment which might be seen as beyond scope.
- The need for clarity around how social investment is defined and what comprises investment products in the market.
- The need for more information from trusted sources such as financial advisers, and awareness that these sources are available.
- The lack of a track record for the social investment market, and linked to this, a general sense of unfamiliarity and uncertainty – which in turn leads to an association with high risk.
- A disassociation between socially responsible/ethical/sustainable investment, and social investment – activity in one does not correlate to activity in the other.
- Confusion around who is responsible for identifying social investments as an option – advisers or clients.

Yet, the research also identifies a number of positive opportunities for institutional investors, across the spectrum of intention and personality type, to engage with the social investment market. These opportunities can be divided into those who can be encouraged to provide the next £500m in risk finance in the near term (family offices, housing associations, corporations and charitable organisations), and looking further ahead, those which might play a key role in providing the next £5bn for the market (charitable organisations, local authority pension funds and family offices).

The remainder of this report presents in detail findings from both the market research and interviews for each institutional investor group, exploring further the issues identified here. This is followed by the conclusion, and practical recommendations for engagement (divided between the £500m and £5bn 'segments' in the market) in chapter 11.One pager profiles for each of the investor groups, are provided in Annex Two.

3. Housing associations

3.1. Overview

Housing associations are not-for-profit institutions that provide social housing. Their **interest in social objectives**, such as reducing unemployment and improving community welfare, makes them potentially fruitful sources of capital for social investment.

There are around 1,700 housing associations in the UK which vary in size from those providing single digits of social housing to those providing tens of thousands of homes. While such diversity means housing associations **differ greatly in terms of their available capital** pools for investment, to date both small and large housing associations have been involved in making social investments.

As an institutional investor group, there is a **high concentration of 'Go the extra mile' personalities** among housing associations who strive to use all available resources – including investment capital – to further their core community missions. Social investments are generally **tied to the immediate communities where housing associations operate**.

Housing associations' involvement in social investment is also shaped by the amount of capital they have to invest. Most housing associations are **heavy borrowers rather than creditors**, and – as charities or social enterprises themselves – tend to reinvest any operating surpluses into developing further housing stock. However, many associations do set aside **sizeable community budgets** to support the delivery of **programmes benefitting tenants and often the wider communities** surrounding their properties. These budgets may be a fruitful source of capital for social investment where opportunities can be found that help fulfil housing associations' community priorities, for example around improving tenants' health or financial literacy.

The vast majority of housing associations are **best suited to making small to medium-size direct investments into social enterprises or highly localised funds** that can support their community objectives. Many housing associations **view social investment as a way of improving service delivery** – such as through acquiring social enterprises that can provide key services to the organisation or its tenants. However, recent increases in operating surpluses demonstrate the potential for some of the larger housing associations to devote substantial resources to **investments in external funds**, as London &Quadrant Housing have done (see Figure 15).

3.2. Sector size and segmentation

There are approximately 1,700 housing associations in the UK that collectively provide around 2.5 million homes[43] and own assets of over £118bn[44]. The majority of housing associations' assets are social housing, but they also own a small proportion of commercial properties which they use to cross-subsidise social housing activities.

Housing associations differ by legal entity, with some registered as charities and others registered as industrial and provident societies[45], trusts, cooperatives or companies. Housing associations receive government grants, mainly for new house building, but generally their day-to-day activities are financed through rent and service charges. Due to a decline in government subsidies, they are having to become increasingly financially independent.

---

[43] National Association of Pension Funds (2013).
[44] Million Homes (2013).
[45] HMRC (2014).

Housing associations vary in size from those providing single digits of social housing units to those providing tens of thousands. There are some very large housing associations: the largest 20 housing associations own more than 30% of the housing stock of all housing associations in the UK[46], whilst the largest 10 housing associations each have a turnover ranging from £150m to just over £400m (see Table 6).

Other than some of the largest, housing associations generally have a regional or local focus, and consequently are particularly focused on social outcomes in the communities in which they work. They also tend to have significant knowledge about the needs of their local communities. This regional and local focus is likely to influence housing associations' decisions on social investment.

Investment in community projects and support for social enterprises currently comes from both large and small housing associations. Smaller housing associations have potential to play an important role in social investment, as their local coverage makes them important sources of finance to the communities they serve. However, it is the largest housing associations that are likely to be the most fruitful sources of social investment, since they generate the largest surpluses and therefore have the largest capital pools to draw from. Table 6 summarises the stock of housing, turnover and regional coverage of the ten largest housing associations (in Britain).

Table 6: Ten largest housing associations by stock of housing

	Stock of housing (number of houses)	Turnover in 2012 (£m)	Region
Sanctuary Group	79,011	408	Nationwide
Circle	63,500	346	Midlands and South-east
London and Quadrant (L&Q) Housing Trust	67,000	330	London and South-east
Places for People Group	62,000	340	Nationwide
The Guinness Partnership	60,200	266	Nationwide
Affinity Sutton Group	57,000	268	England
Home Group	55,000	304	Nationwide
The Riverside Group	53,573	292	Nationwide
Together Housing Group	35,000	153	North of England
Symphony Housing Group	39,164	150	North-west of England

Source: The Guardian, 'In profile: Britain's largest housing associations', 2012

Housing associations also differ in their potential commitment to social investment. They are a broad group of social landlords who each interpret the reach of their mission in a different way. For example, one of the interviewees contrasted housing associations that are 'real estate players', who largely focus on their balance sheet and are therefore diversifying their housing stock to generate market rents, with those more focused on retaining their social mission and purpose, and who are therefore more likely to make investments that directly help their tenants. It is important to acknowledge such variation within one investor group – though this report generally focuses on investor groups as a whole, the differences within groups should not be overlooked.

[46] Ethical Money (2012).

3.3. Characteristics of investment approach

Typically, housing associations do not have large amounts of capital available for investment: they tend to be major borrowers rather than creditors, and their ability to channel capital to the investment market is also limited by the fact that they are often charities or social enterprises themselves, so generally operating surpluses are invested back into house building or into projects in local communities[47].

> *"We don't generate huge amounts of surplus cash. We tend to go to the bond market to get money to re-invest in social housing. We generally are looking at improving our operating margin so that we can borrow more. Any cash we have leftover is invested in short-term money market funds."*
>
> *"We don't stockpile cash; we reinvest in our communities and house building projects."*
>
> *– Housing associations*

In recent years, however, housing associations have made significant operating surpluses, suggesting there is some potential for increased investment. Housing associations posted net surpluses of over £2bn in 2012/13, representing a rise of 259% over three years[48]. The largest 30 housing associations made a combined surplus of £947m, with L&Q housing association alone making a surplus of £118m[49].

The proportion of housing association surpluses that could be available for social investment is limited by the fact that surpluses are traditionally invested in house building or local community projects. In particular, housing associations have purposely built up their operating surpluses in recent years to act as a buffer and enable them to continue house building programmes in the face of cuts to government grants – central government spending on affordable homes has recently been cut from £3bn a year to £450m[50].

When housing associations do have surpluses available for investment or charitable donations to communities, they may consult social housing beneficiaries in setting priorities for how to allocate funds.

> *"Our local neighbourhood priorities come from the bottom up… We have a participatory governance structure wherein resident committees draw up area plans to tell us what their priorities are." - Housing association*

3.4. Social investment history

Housing associations have extensive involvement in community investment and engagement with social enterprises. The National Housing Federation[51] found that housing associations invested £746.5m in 'community investment' in 2010/11. This investment was in a variety of areas including projects to create jobs and help people into work; improve learning and skills; improve health and well-being; and improve community spaces. However, whilst it is clear housing associations see their finances as a vehicle for furthering their mission, their current level of engagement with social investment has so far been limited.

Big Society Capital[52] note that there are three main ways housing associations are currently boosting growth in the social enterprise sector:

- Procuring services from social enterprises;
- Spinning out or acquiring social enterprises; and

---

[47] Richardson (2012).
[48] Social Housing (2012).
[49] Inside Housing (2013a).
[50] Financial Times (2012).
[51] National Housing Federation (2012).
[52] Big Society Capital (2013).

- Investing capital in social enterprises, or *social investment*.

3.4.1. Procuring services from social enterprises

Due to their interest in community outcomes, housing associations are frequently involved with social enterprises, either through prioritising procurement from them, providing business support services, or by setting up or acquiring them. In time, housing associations' involvement with social enterprises may be found to increase further with the passing of the 2012 Social Value Act, which requires public bodies (including housing associations) to consider how the services they commission affect the 'economic, social and environmental well-being of the area'[53]. One housing association interviewed reported that, in response to the Social Value Act, they have already increased contractual work with social enterprises (though insufficient time has passed to know the full effects).

> *'We have a training centre with a franchise we bought... some trades-people elect to do courses alongside our residents and pay premium rates, which cross-subsidises our activities.' – Housing association*

Examples of housing sector organisations prioritising procurement from social enterprises include construction company the Wates Group, a major contractor for many housing associations, who awarded contracts with a total value of £625,000 across 56 different projects to social enterprises, and the Accord Group, who actively 'procure from local SMEs and social enterprises'[54].

3.4.2. Spinning out and acquiring social enterprises

Housing associations often see spinning out and acquiring social enterprises as a way to ensure their investments benefit their tenants. Some specific examples are given in Figure 14.

Figure 14: Examples of housing associations spinning out or acquiring social enterprises[55]

- Thames Valley, Shepherd's Bush, Gateway and Sentinel housing associations jointly launched the Academy4Training social enterprise in January 2012. Academy4Training is an independent training and employability social enterprise delivering certificated courses enabling residents of the housing associations to gain qualifications preparing them for employment in the housing sector. It developed from Thames Valley housing association's internal training centre.
- In 2008 Aspire housing association acquired PM Training, which it runs as a social enterprise, providing training to individuals with the aim of helping them find employment.
- Riverside ECGH have developed a number of social enterprises with the aim of providing opportunities for homeless people to gain work experience and gain training qualifications. Their social enterprises include Force4Change, a landscaping social enterprise, and Veterans Artisan Bakery, a training bakery for ex-service personnel, and a waste recycling company.
- Plymouth Community Homes have four projects operating as social enterprises, including a window-manufacturing factory, a high quality joinery, a metal fabrication workshop and a sign shop.

---

[53] Richardson (2012).
[54] Op. cit.
[55] Enterprising Futures (2012), Academy4Housing (2013) and Richardson (2012).

3.4.3. Social investment

Despite housing associations' commitment to community investment and supporting social enterprises, there has so far been little involvement by housing associations in social investment, in the sense of providing capital that gains financial as well as social returns. However, one significant example is L & Q's £10m investment in the Real Lettings Property Fund, which aims to provide housing for the homeless (see Figure 15).

A second example is the Accord Group's involvement in two funds aimed at tackling youth unemployment and fostering entrepreneurship. Initially, Accord Group launched the 'A-Fund', which aimed to foster the talent and potential of Birmingham's young 'entrepreneurs and change-makers'[56]. In 2013, the Accord Group followed this up with the Hub Launchpad, a £3m incubator programme aimed at providing direct investments and pre-start up support to over 1,500 social enterprises. The programme received £1.5m from the Government's Social Incubator Fund and is being run by the Accord Group.[57]

Figure 15: The Real Lettings Property Fund[58]

In November 2012, London & Quadrant (L&Q) housing association, the housing association that posted the largest surplus in 2012/13, announced it would invest £10m into the Real Lettings Property Fund.

This fund is being used to buy homes in London to be let by homelessness charity Broadway, with the aim of moving people from hostels or temporary accommodation.

The Real Lettings Property Fund is managed by a social investment organisation, Resonance, with the aim of providing a 'commercial risk-adjusted return' alongside a 'real social impact'. One of L&Q's main reasons for investing in the Real Lettings Property Fund is that its aims are closely tied to L&Q's mission.

3.5. Motivating factors

3.5.1. Concern for social outcomes

A significant motivating factor behind housing associations' current and potential future involvement in social investment is their very high level of interest in social outcomes in the communities in which they work. Housing associations' focus on social objectives such as reducing unemployment and community development makes them ideal partners of social enterprises.

Of the investor groups interviewed for the research, housing associations are the most likely of all to feel it was their 'role' to make social investments.

The research shows that housing associations are likely to be particularly attracted to social investment when it is aligned with their own mission, and when it benefits the residents in the areas in which they work.

"I think its fundamental – because social investment is linked to social innovation, which in turn is about tackling endemic, systemic problems where the government and charities have not made in-roads."

"Anything we do would have to be in the communities where we operate."

"We are very local operators and keen on localism."

"Our engagement with social businesses is all about homes and communities... it has to have a strong link to our mission; this is a crucial part of our investment strategy."

– Housing associations

---

[56] Richardson (2012).
[57] Accord Group (2013).
[58] Third Sector (2012), Resonance (2013).

The Green Light Report[59] identified significant interest in investments in social enterprises among housing associations. The report found that 91% of housing associations interviewed were particularly interested in social enterprises that 'create employment for tenants', whilst other priority areas were addressed NEETs (young people not in education, employment or training) and reducing financial exclusion. Meanwhile, the investment by L&Q in the Real Lettings Property Fund demonstrates housing associations' interest in social investment that helps reduce homelessness.

3.5.2. Increasing operating surpluses

The largest 30 housing associations made a combined surplus of just under £1bn in 2012/13, with L&Q alone making a surplus of £118m[60]. L&Q's large surplus allowed it to allocate £10m in social investment to the Real Lettings Property Fund, expecting to combine a 'commercial risk-adjusted return' alongside a 'real social impact'.

However, there are also reasons to expect that the increase in housing associations' operating surpluses will not necessarily allow them to increase social investment. Due to housing associations' role as social enterprises, operating surpluses are generally invested into house building or directly into community projects[61]. In fact, one of the main reasons that housing associations have attempted to increase surpluses in recent years is to allow them to continue house building in the face of cuts in government grants. As a result, housing associations are increasingly investing in private housing that they rent or develop for market sale and use the proceeds to cross-subsidise other activities[62]. Lastly, during interviews with housing associations, they stressed that the availability of cash surpluses for investment is further limited by the uncertainty of their future income streams.

3.6. Barriers to investment

3.6.1. Size of available capital pools

One of the most significant barriers to housing associations increasing their social investment is the size of the capital pools that they can devote to financial investments. As described above, housing associations are typically net borrowers rather than creditors, and their recent surpluses have been built up mainly with the intention of investing them in house building. Therefore, the portion that could be allocated to social investment is likely to be limited.

Nevertheless, given the size of the recent surpluses of the largest housing associations, any social investments housing associations do make could still represent a sizeable contribution. For example, L&Q's recent £10m social investment is equal to 5% of the estimated UK social investment market in 2011/12[63].

> *'We see ourselves as potential delivery partners for social investments. We're heavy borrowers rather than investors, but we have lots of knowledge of communities' – Housing association*

[59] Richardson (2012).
[60] Inside Housing (2013).
[61] Richardson (2013).
[62] Inside Housing (2013).
[63] The size of the UK social investment market was estimated to be £202m in 2011/12. See ICF GHK with BMG Research (July 2013).

3.6.2. Is social investment the role of housing associations?

A related consideration is whether housing associations see social investment as part of their role. Whilst the National Housing Federation found that housing associations invested £747m in 'community investment' in 2010/11, only a portion of this was social investment in the sense of generating both social and financial returns. It may be that since housing associations are themselves social enterprises, they have been less concerned about the financial return on their investments, than the social outcomes.

A concern for housing associations is that there is a trade-off between increasing social investment and their traditional approach of charitable investments in communities. Housing association interviewees expressed concern that prioritising social investment might then involve reducing other forms of supporting social outcomes through direct community involvement. Others felt that they were more suitable to be recipients of social investment – as not-for-profit organisations serving vulnerable communities – than providers of capital themselves.

For many housing associations then, branching into social investment requires a re-assessment of their role. In doing so, housing associations may well face internal barriers, as management then has to be convinced that social investment should be part of the role of the organisation. As noted above, for housing associations to see social investments as part of their role, the investment has to be closely aligned to their priorities; that is, local and focussed on employment or other benefits for residents.

> *"A reason for not doing [social investment] is there is an existing alternative approach for doing this. We get demand from our communities to do a lot of things, and until recently there's been available funding to respond to these demands."*
>
> *"The major barriers are finding an appropriate company with a viable business plan, and convincing [the management] that making social investment is part of their role."*
>
> *– Housing associations*

3.6.3. Influence of regulators

A final potential barrier to housing associations' involvement in social investment is the influence of regulators. During the interviews conducted for the research, some housing associations expressed that they felt regulators would prefer them to focus their activities on social housing, rather than engaging more broadly with social investments. However this was not identified as a concern by a majority of interviewees, nor was it identified as a major constraint.

3.7. Opportunities to engage

3.7.1. Key personalities

There are a significant number of 'Go the extra mile' personality types amongst housing associations who see their role as community anchors extending to how they manage their assets. Housing associations who view themselves in this light are likely to be the strongest partners of social enterprises.

However, there are also a substantial number of housing associations who view their role as more narrowly focused on the core, day-to-day operations of supplying housing and collecting rents. These organisations undertake fewer community programmes than their peers and are more likely to be 'Benefit of the doubt' or 'All being equal, but…' personalities when it comes to social investment. Essentially, they are unlikely to consider making social investments unless they can be directly tied to meeting business growth or financial goals (for those housing associations that are registered charities, this focus can also be linked to charities' legal obligations when making investments in terms of core mission focus and/or maximising financial return).

3.7.2. Where will they contribute?

Overall, apart from some of the largest, housing associations are most likely to consider making direct investments into local social sector organisations which can help achieve their community priorities and/or support service delivery. Housing associations focus on a broad range of community issues – from improving tenants' mental health and well-being, through to supporting safer communities and spaces. As such, housing associations are well-placed to contribute to supplying the next £500m in risk investments to social sector organisations, across a wide range of sectors.

Associations with significant operating surpluses may be in a position to consider social investments in larger funds in related sectors – for example, local infrastructure or housing facilities for non-tenants. There is thus also some potential to engage larger housing associations to grow the more established end of the social investment market.

3.7.3. How can they be engaged?

Among the larger housing associations that do have surpluses that could potentially be channelled into social investments, activities aimed at fostering discussion and debate within housing associations as to whether and how social investment fits with organisational aims could be an effective way of encouraging engagement with the market.

In the interviews with housing associations, several managers noted the importance of raising the profile of social investments within their sector. This could be achieved through developing case studies of social investment activity, to could be shared across the market, and/or through events aimed at profiling social investment opportunities and learning from the experience of other housing associations that have made social investments. Tailored forms of engagement with housing associations would build on work previously accomplished at workshops and at regular industry conferences. Closed meetings between housing associations that are both doing and considering making investments into social businesses would also help to increase momentum among this investor group.

There is also a need for social investment opportunities to be closely matched to the mission and priorities of housing associations, such as those aimed at employment, financial inclusion and homelessness. A platform made available on industry websites or in regular newsletters/publications profiling available investment opportunities, which could be searched regionally or by focus area, could enable housing associations to match themselves to appropriate social enterprises/funds/investment opportunities.

4. Faith-based organisations

4.1. Overview

Faith-based organisations are for- or not-for-profit institutions concerned with practicing a particular faith and its connected values. As investors, the primary concern of faith-based organisations is to maintain ethical standards in line with members' belief systems. As such, faith-based organisations are **strong proponents of socially responsible investment** (SRI).

Despite being the most ethically-minded of any of the investor groups profiled in this research, faith-based organisations on the whole have had **little exposure to social investment** to date. Funds connected to the Church of England tend to be managed in a **largely conservative, risk-averse** fashion focused on meeting the long-term income needs of the Church – a priority that is unlikely to change in the near term.

As such, faith-based organisations have **little to no ability to compromise on financial returns** – their investment decisions are shaped by their advisers, who do not believe excluding particular industries will impact returns. Faith-based organisations therefore largely fall into the **'Benefit of the doubt'** or **'All being equal but…' personality types**, being sympathetic to social investment's community impact goals but also feeling they are unable to consider moving finance into such vehicles until the market offers improved financial returns. Many faith-based organisations also **outsource their investment management** due to a lack of capacity to manage funds in-house such that the sector has several '**Ask the finance guy'** personalities.

Consequently, faith-based organisations are **unlikely to engage with the riskier or more innovative elements** of the social investment market. It may be possible to **mobilise Church 'grant' portfolios** for **small investments** into community-based social sector organisations **supporting the Church's community action goals**. However, given the risk-averse nature in which much of Church's capital is invested, the most likely area for Church capital to gain further exposure to social investments in the near term will be at the more established end of the marketplace. In particular, it is possible to imagine Church capital being invested through **managed funds which may provide some exposure to proactive social investments** in sectors such as microfinance, which fit with the Church's values while making up a sufficiently small portion of overall investment portfolios, to ensure income targets are met.

Islamic finance institutions are more of an unknown quantity in the social investment space, with a large amount of the capital invested in current UK funds **controlled by foreign asset owners**. The nature of Islamic finance implies that such funds will **never support extensive risk-taking** at the more innovative end of the social investment market. However, with the growth of Islamic banks and financial institutions serving more and more UK consumers, it is possible to imagine Islamic finance growing over time to support **social infrastructure projects** or charity/social enterprise bonds where the latter can be structured to be compliant with sharia law.

4.2. Sector size and segmentation

In the UK, many faith-based organisations are registered charities with permanent endowments or investment portfolios[64]. As of March 2014, there were 32,446 faith-based charities registered with

[64] As such, many faith-based organisations will also be required to comply with charity law. The Law Commission is currently reviewing the legal framework around charities making social investments and published a consultation paper on the matter on 24th April 2014. See http://lawcommission.justice.gov.uk/consultations/charity-law.htm

the Charity Commission in England and Wales[65], representing around 20% of the charity sector. Apart from charities, faith-based organisations may also be for- or not-for-profit financial service providers that invest clients' money in line with a particular set of religious values.

Within the faith-based sector there are two major segments in the UK: Christian charitable organisations, both within and outside the Church of England; and providers of Islamic/sharia-compliant finance. While these groups are similar in employing religious values as a basis for setting investment strategies, they differ significantly in their investment motivations, approaches and screening processes, and as such are considered separately in turn in this chapter.

4.3. Christian faith-based organisations

In the UK, the Church of England is the key faith-based organisation with significant investment capital. Through its three key investment arms – the Church Commissioners, the Church of England Pensions Board and the CBF Church of England Funds managed by the CCLA[66] – the Church owns assets worth well over £5.5bn which generate around 15% of total Church income[67]. The Church in Wales similarly controls around £34m in assets through its Common Investment Fund[68].

Outside of the Church of England, there are a number of Christian organisations, such as Methodist and Catholic churches and charities, which hold smaller pools of capital and tend to invest through fund managers. The CCLA is the largest fund manager for such organisations and manages a £1bn+ Charities Official Investment Fund (COIF) which several non-Church of England faith groups invest in alongside other charitable organisations.[69]

4.4. Characteristics of investment approach

The unifying characteristic across faith-based investors is a strong commitment to ethical investment in line with religious principles. More than any other investor group examined in this research, faith-based organisations apply a consistent set of requirements when making investment decisions that frequently go further in their exclusions and positive engagement targets than their secular counterparts. For example all faith-based organisations that participated in the study applied negative screens to their portfolios, and several also took a strong interest in environmental, social and governance (ESG) performance and engagement with companies.

"People assume the Church will make mixed motive investments, and come up against the income requirement. The Church doesn't make grants, it has programmes to run and clergy to pay. The income requirement is not flexible." – Investment adviser

4.4.1. The Church of England

The Church of England is an operating charity, with endowed funds whose primary purpose is to generate income for the Church's activities, pay clergy salaries, and pay retired members of the

[65] Total number of registered charities with 'religious activities' listed as part of charitable activities as of 14 March 2013. See Charity Commission for England & Wales: http://www.charitycommission.gov.uk/find-charities/
[66] Collective investment schemes managed by the CCLA in which circa 15,000 Church of England parishes, dioceses, schools and other church charitable trusts are required to invest. The CCLA itself is owned by its church and charity clients (The Church of England, 2013).
[67] The Church Commissioners for England (2013).
[68] The Church in Wales (2013).
[69] Interview with investment adviser.

clergy's pensions. As such, all Church of England funds have set income targets – the Church Commissioners Fund, for instance, targets a return of RPI + 5% per annum over the long-term[70].

In line with this strategy, the Church's portfolio is skewed towards asset classes that provide strong, long-term returns and rising income over time. A large portion of the Church's current portfolio is invested in property and listed equities and – while the various investment bodies are prioritising keeping more liquid assets at hand – much of the Church's portfolio is relatively illiquid. While this means Church bodies are able to take a longer-term view and are more comfortable than other investors with less liquid assets, the lack of a sizable allocation for alternatives and difficulty in 'freeing up' current capital for new investments means the scope for higher-risk, private-equity style investments is limited.

As such, investment advisors familiar with Church-linked funds tend to view faith-based organisations as a particularly 'conservative and risk-averse sector'. As one advisor commented, "Listed equities were considered way too risky [for the Church] when they were emerging"[71]. Investment decisions tend to be driven by a desire to keep income predictable and to secure the future of the Church in the long-term.

Church-linked funds and faith-based organisations are strongly committed to pursuing an ethical investment approach. The Church states that the way it invests 'forms an integral part of the Church of England's witness and mission'. As such, all Church funds aim to avoid 'profiting from, or providing capital to, activities that are materially inconsistent with Christian values'[72]. The specifics of the Church's investment criteria are set with the advice of its in-house, Ethical Investment Advisory Group, and broadly consist of a series of negative screens to avoid investments in any companies where a significant portion of business activity involves gambling, alcoholic drinks, tobacco, the production or distribution of pornography, high interest rate lending or human embryonic cloning[73].

Beyond these exclusions, the Church investment bodies also apply positive screening criteria, expecting the companies they are investing in to exhibit responsible employment practice, respect for human rights and the environment, and good corporation governance. Through the Ethical Investment Advisory Group, the Church monitors its investments against these criteria and pursues a policy of ongoing engagement, with the potential for such engagements to end with divestment if sufficient progress is not made[74].

[70] The Church Commissioners for England (2013).
[71] Interview with investment adviser.
[72] Op. cit.
[73] Church of England (2013).
[74] Op. cit.

4.4.2. Other Christian denominations

Beyond the major Church investment funds, a number of smaller faith-based organisations also apply ethical investment approaches through their fund and manager selections. For example, the CCLA launched an ethical Charities Official Investment Fund (COIF) Fund in 2009 (see Table 7) with a view to targeting faith groups who are outside the Church of England but also have strong ethical investment goals. The fund has generated strong interest from clients and grown to a size of over £100m in under five years. The CCLA estimates about 80% of the organisations in the fund are non-Church of England faith-based organisations.[75]

4.5. Social investment history

Despite being the most active 'ethical' investors of any group, faith-based organisations have not been highly active in making social investments. Apart from some exposure to more established social investment products through pooled funds, Church capital has not, to date, had much interaction with the UK social investment market.

Table 7: COIF Charities Ethical Investment Fund

In 2009, the CCLA launched the COIF Charities Ethical Investment Fund as a more proactive, ethical investment alternative for clients invested in its £1bn+ COIF Fund. The decision to launch the Ethical Fund was taken in response to a consultation period with clients over their investment goals, which found that clients weren't entirely satisfied with the 'fulcrum point' of how their money was invested, and desired to see a more proactive approach to ethical investment.

The Ethical Fund aims to be a suitable, 'all-in-one' long-term fund for charities, delivering rising income through providing a long-term total return to investors of inflation plus 5%. The Fund applies negative as well as ESG screening criteria, and follows a client-led engagement agenda which has, for example, engaged with UK companies on the living wage. While the majority of the portfolio is invested in diversified global and UK equities, the portfolio includes a specific allocation for 'high impact investments' in sectors such as microfinance, immunisation bonds and timber which make up approximately 1% of the portfolio.

Example 'high-impact' investments

- *Triodos Microfinance*: Fund providing loans and equity to microfinance institutions and banks in Asia, Africa and Latin America that have gone through the first stage of growth and demonstrate a financially sustainable approach towards providing financial services to underserved client groups.
- *The Forest Company*: Fund investing in sustainable forest plantations (timber) in South America.

While the initial aspirational target set for the performance of high impact investments in the portfolio was 2%, CCLA reports these investments have quickly outperformed this target (due largely to the strong performance of renewables vis-à-vis fossil fuels) and the Fund is now looking to increase its allocation and raise the aspirational target for high impact investments to 5%. The Fund has grown from a size of £60m at launch with 10 seed funders to serving over 200 clients with over £100m invested.[76]

On the supply side of the market, in 2013 a faith-based charity launched the sector's first charity bond in the form of the London Missional Housing Bond. The bond has been developed by three Christian charities to finance the purchase of affordable housing for some of their workers in the

[75] Information obtained from interview with investment adviser.
[76] Information obtained from the CCLA. Also see CCLA (2013).

most disadvantaged communities in London. The bond aimed to raise £2m in its first round and offers investors fixed rates of interest of between 1-2% based on the amount and length of their investment[77].

Additionally, local churches have a strong community action role, and many Church-based organisations run – or have the potential to run – aspects of public service delivery. A July 2013 report published by ResPublica examining the scope of the Church's social work, documented evidence of churches throughout the country undertaking direct intervention work supporting ex-offenders through to migrant workers and vulnerable young adults, and sometimes contracting with government to do so[78]. The same report argued that such Church-led social initiatives should be considered an untapped social investment opportunity, and recommended that the Church Commissioners, Church of England Pensions Board and CCLA set aside a percentage of the returns on their investments to invest in Church-based social ventures that have the potential to generate returns and achieve social impact[79].

While such a proposal essentially suggests the Church investment bodies ought to experiment with social investment internally through supporting Church-linked social enterprises out of their 'grants' portfolio rather than through their investments, it may nevertheless prove a more palpable way forward for faith-based investors to become comfortable with less-established social investment products.

4.6. Motivating factors

4.6.1. Community impact

In its role as a community-based institution, the Church sees itself as being for the benefit of the community and historically has prided itself on being at the forefront of 'social transformation'. Social investment thus arguably could be an attractive opportunity for faith-based organisations to use funds to generate social returns in the community where this link can clearly be made.

"Locally – it would be preferred to achieve impact [in our community], it would give purpose and reasoning for doing it." – Faith-based organisation

Among the faith-based organisations interviewed for the research, there was a strong preference for community-focused investment opportunities within sectors of priority interest to the Church. Housing & local facilities, and income & financial inclusion were the most popular sectors for considering investment opportunities, as these are also areas where the Church's community activism has focused. As one faith-based investor explained, if a social investment opportunity could be shown to be "Closely aligned to the Church of England aims, [this] might make up for some increased risk or reduced return" and "Would make it easier." The investor went on to explain that for example, a community finance business offering affordable credit would be of strong interest, even if it were offering below market rates of return, as combatting high-interest rate lending is a priority for the Church.

77 Affordable Christian Housing (2014).

78 For example, the report documents a case study of a church in a rural market town which began offering free English language classes to migrant workers delivered by church volunteers as a response to issues around community cohesion, which has grown into a government-funded programme (Noyes and Blond, 2013).

79 Op. Cit.

4.7. Barriers to investment

While the social mission of the Church and its extensive experience with considering non-financial goals when making investments are potentially strong motivating factors for making social investments, the barriers to faith-based organisations actually doing so at present are significant.

4.7.1. Fiduciary duty and income requirements

As operational charities, fiduciary duty and income requirements are writ large in the minds of faith-based organisations when considering investment opportunities. As such, any investments which might lead to a reduction in overall return are considered impalpable. As one investor explained:

> *"The basis of our ethical restrictions is that we are not limiting our return by excluding certain investments. If we didn't believe that to be the case, that would potentially be a problem with the regulator. [With considering social investments], if the returns and risks were similar we would probably give it a full hearing. However, if the financial return was slightly less. I think we would go for a conventional investment. Fiduciary duty trumps all."*
> *- Faith-based organisation*

Given that British society is becoming more secular and the Church's sources of income from donations by parishioners are declining, the importance of the Church's investment portfolio for generating income for its work and longevity, is increasingly important. As such, there is unlikely to be any flexibility in the medium-term around income targets, and the current perception that social investments largely offer rates of return that are below the Church's minimum requirements, is a therefore a notable barrier to faith-based organisations' engagement with social investment.

4.7.2. Investment management structures

Another set of barriers for faith-based organisations is the chain of intermediation between the 'value-driven' members of the clergy who might be interested in community impact and those who actually enact investment decisions on their behalf. As many faith-based organisations outsource their investment management, there is a general lack of ability to consider investment opportunities outside those that are presented by fund managers. Similarly, one investment adviser pointed out that – apart from the large, internally managed Church funds – many members of the clergy aren't confident with managing investments. Hence, they often take steer from wealthier members of their diocese, who frequently are from a financial services background and end up managing investments much as they would in a commercial financial institution (i.e. largely without active consideration of social investments).

In the case of the CCLA ethical fund profiled above, the fund was set up proactively by the CCLA to offer an investment vehicle it thought would appeal to the values of its existing clients, rather than being asked to do[80]. The movement into the fund has been encouraged by the CCLA directly marketing the ethical fund to existing customers, who already have trust in the CCLA's investment management capability and – given the fund's largely conservative approach only exposing a fraction of the portfolio to high-impact investments – are confident the fund can still meet their income needs. Such experience helps to demonstrate the extent to which fund managers are important gatekeepers and influencers for faith-based organisations.

[80] Interview with investment adviser.

4.8. Opportunities to engage

4.8.1. Key personality types

As implied above, most faith-based organisations fall into the 'Benefit of the doubt' or 'All being equal but…' personality types. They are sympathetic to social investment and may share many of the community impact goals of social sector organisations. However, their income requirements are such that currently they do not feel they can sacrifice any financial returns in order to make higher-risk investments.

There is also a strong presence of passive personality types in the faith-based sector, including institutions who fully outsource their investment management with a list of 'what not to do', and thereafter assume an 'Ask the finance guy' attitude, trusting asset managers to know best how to invest to meet income needs. There is also a segment of 'Don't leave me behind' personalities, who are less concerned with investment questions altogether and would rather focus on their day-to-day activities, but nevertheless do not want to be out of step with Church institutions when thinking on investment policies changes in any significant way.

4.8.2. Where will they contribute?

Faith-based organisations may well be inspired to support Church-linked social enterprises through their 'grants' portfolios. A certain amount of the Church's investment income is redirected to support its members' community action work. Where this finance could be channelled into locally-focused social investment opportunities that help the Church achieve its social action goals, this may be a palpable way for faith-based investors to get started with making direct investments into social ventures.

Particularly where such investment opportunities may have grown out of Church social initiatives[81], it is conceivable for a virtuous cycle scenario to develop in which the Church could invest in its own members' social ventures and recycle funds that otherwise would have been given away at 0% return for community action work. However, given the funds the Church has available, these commitments will likely be relatively small and sporadic where they do happen. As such, they are likely to go unnoticed in contributing towards the greater £500m+ in risk investments required by the sector.

The more likely entry point for sizeable commitments from faith-based investors will be through managed funds offering exposure to more established social investment products in areas that match with the Church's broader ethics, such as investment opportunities in environmental funds (e.g. sustainable forestry) as well as community infrastructure, and potentially microfinance.

4.8.3. How can they be engaged?

As implied by the discussion above, it may be possible for fund managers to market more established social investment products as opportunities which fit within the Church's current portfolio allocation and ethical investment goals.

Similarly, the CCLA's strategy of exposing a small portion of a larger fund to more established social investment products may provide a way for clients to become comfortable with these products, as a way to meet with their income targets and fulfil their values, while not taking on what could be seen

[81] For example, Resurgo Social Ventures, which has experience successfully managing Payment by Results contracts to fund its work getting young people into employment, was founded through St. Paul's Church in Hammersmith and still has strong links to the Church. See: http://resurgo.org.uk/

as unacceptable levels of risk. As many faith-based investors are ‘Ask the finance guy’ types, the impetus to consider such opportunities may have to come through asset managers suggesting these options, or otherwise efforts to educate and influence faith-based investors to ask their asset managers to structure such opportunities.

Finally, while faith-based organisations face similar challenges to their secular charity counterparts surrounding restrictions on trustees’ ability to consider non-mission-aligned social investments, they do think of themselves as a separate and distinct ‘group’. Interviewees expressed an interest in learning what other Church and faith-based organisations are doing on social investment and discussing issues together, feeling that they shared more in common with other Christian denominations and investors than with the charity sector more broadly. This implies that faith-based organisations could benefit from closed roundtables and discussions, and may well move as a group towards making social investments if and when their peers get involved.

4.9. Islamic finance

In addition to a large group of organisations connected to the Christian faith, another sizable source of faith-linked finance domiciled in the UK is the Islamic finance market. While it unfortunately was not possible to engage with any Islamic finance institutions directly as part of the research for this report, the remainder of this chapter considers briefly the typical investment approach of such organisations and the likelihood of UK-based Islamic finance institutions engaging with the social investment market in the medium term.

4.9.1. Sector overview

With over £11.4bn of reported assets invested in sharia-compliant funds at the end of 2012[82], the UK is the leading western country for Islamic finance. UK financial institutions have been offering sharia-compliant products since the mid-1980s to cater to the investment needs of Middle Eastern clients. However, the size of the market has grown rapidly in recent years, with the total value of sharia-compliant assets growing by 150% from 2006 to 2013. There are currently over 20 international banks operating in the UK offering sharia-compliant products, while many of the country’s largest accountancy, consulting and professional service firms now have Islamic finance specialists in their teams[83].

While the largest volume of this activity has been driven by a desire to attract foreign investors to undertake major infrastructure projects through sharia-compliant funds, such as the financing of the Shard and redevelopment of Battersea Power Station in London, there are also institutions targeting domestic customers with sharia-compliant products, such as current accounts and mortgages offered by the Islamic Bank of Britain or Lloyds TSB. With Islam being the fastest-growing religion in the UK[84], the demand for such consumer products and services – and the connected amount of capital placed in them – is likely only to grow.

[82] UK Trade & Investment (2013).
[83] Op. cit.
[84] In the 2011 Census, Muslims were the second largest religious group in England and Wale with 2.7 million people, an increase of 1.2 million from 2001 (from 3% to 5% of the population). While Christianity remained the largest religious group, the number of people identifying themselves as Christian declined over the same period by of 4.1 million from 72% to 59% of the population Office for National Statistics (2013).

4.9.2. Characteristics of investment approach

On the whole, Islamic finance adopts a long-term equity orientation, with the global Islamic finance market composed primarily of *sukuk* (Islamic bonds)[85]. Given the fundamental principles behind Islamic finance, which requires the equitable sharing of risks and prohibits interest-based lending, equities have been the most compatible investment strategy.

While Islamic finance institutions are similar to the Church in applying uniform exclusions to lines of business activity that are considered incongruous with Islamic values, the content of these restrictions varies significantly. Sharia-compliant funds may not be invested in any businesses involved in the production of pork products, gambling, pornography, or the production of alcohol. Furthermore, as money is not considered of value and the taking of interest is forbidden in Islamic law, sharia-compliant funds cannot invest in any non-tangible assets or projects which involve high levels of uncertainty – where risks would typically be offset by charging high interest rates. As a result, investments in most conventional financial services are excluded[86].

4.9.3. Motivating factors

Apart from these restrictions, Islamic finance has several socially positive goals which can be seen as potential motivating factors for considering social investments. The central tenant of Islamic economics is to develop a just and egalitarian society where all individuals can develop to their full potential, and contribute to growing the prosperity of the community as a whole[87]. As such, investments that would help promote social justice or improve the well-being of the community are positively encouraged.

While several experts have pointed to such tenants as providing a strong rationale for Islamic finance to engage with, for example, affordable finance, the Islamic finance sector as a whole has not as yet provided many opportunities for investors to positively support such activities. As one financial analyst familiar with the Islamic finance market in the UK commented, the institutions active domestically are not applying any ESG or other positive screening criteria at all – the basis of their approach is to apply negative exclusions and invest primarily in large companies. However, the same interviewee suggested that – while the foreign investors who comprise the majority of the sharia-compliant capital invested in the UK are unlikely to be motivated by supporting UK social causes – there may well be scope to engage British Muslims in investing or saving their money with vehicles that support social issues that resonate with the domestic Muslim community. These might include initiatives supporting education, social mobility or combatting payday lending, for example[88].

4.9.4. Barriers and opportunities

As a result of the unfamiliar investment tools and goals of the Islamic finance sector, many UK social investment funds and social enterprises to date have shied away from approaching the market as a potential source of capital. While it is still the case that most investors in the UK Islamic finance market are effectively located outside the UK – and hence more likely to focus their philanthropic interests and social development activities elsewhere – the growing strength of the British Muslim community implies there may well be scope to consider what consumer products may be developed to appeal to the social justice goals of British Muslim savers and depositors. Structuring such

[85] Unlike conventional bonds, which represent interest-bearing debt, sukuk create the right to receive payments from underlying assets or business ventures based on contracts recognised under the principles of Islamic law.
[86] McKenzie (2012).
[87] Bennett and Zamir (2013).
[88] Interview with financial analyst.

products will of course require taking special consideration for the requirements of sharia law as it relates to financial products and services, though the success of existing UK banks in developing such products demonstrates this is not an insurmountable barrier.

5. University endowments

5.1. Overview

Many UK universities have significant endowment funds, comprised mainly of gifts and donations that are invested in perpetuity to finance a proportion of the annual running costs of the universities.

Whilst many universities have ethical or socially responsible investment policies, these **tend to focus on 'negative' investment criteria**, such as a commitment not to invest in tobacco or weapons manufacturers, rather than 'positive' investment criteria, such as a commitment to make social investments. In contrast to many large charitable foundations managing endowments, universities **do not use investment income to fund 'grants' portfolios** to support external social causes. Investment income is focused wholly internally, and hence the most realistic source of capital for social investment will be through universities' mainstream investments.

One of the key motivating factors for university endowment funds is **maximising investment returns**, so any social investments must fit with this objective[89]. Of the eight groups examined in the research, university endowment managers are the **least likely to have had prior exposure to and/or experience with social investment**, with many expressing concerns over social investments' ability to deliver competitive returns. **A few universities are 'Benefit of the doubt' types**, see themselves as having a community role and feel they would prefer social investments where they can be shown to offer equitable financial returns. However the **majority of universities are more likely to fall under the 'All being equal but…'** personality type, with limited knowledge and reservations about making social investments. Outside the few largest endowment funds, most universities also take a **passive approach to investing,** with many outsourcing their investment management and/or investing in asset classes that require minimal oversight, such as indices, which do not enable adding criteria for social or environmental impact.

These realities contribute to the view that the remit of university endowment funds' investment objectives is sufficiently narrow that they are **unlikely to consider making social investments in the near term**. Where and when universities do consider making social investments, it will likely be at the more established end of the marketplace and/or into products with strong track records that enable these investments to be judged on financial performance first and foremost.

Nevertheless, universities are **public-facing institutions with diverse stakeholders** spanning faculty staff, students, and funders. As such, they **can be motivated by reputational concerns** and may well move as a group if there is an increase in activity towards making social investments amongst their peers. Growing the **engagement of this group will therefore require a long-term approach,** focused on providing the data and evidence required to emphasise the mainstream elements of social investment, as well as offering investment opportunities which compete favourably with university's commercial investments.

5.2. Sector size and segmentation

University endowment funds are a relatively concentrated investor group, with few large university endowments and many much smaller ones.

---

[89] As noted previously, this can also be linked to the fact that many university endowment funds are also registered charities and subsequently required to comply with legal obligations on investing charity funds. This includes investments having to be aligned with core mission and/or maximise financial returns.

The UK universities with by far the largest endowment funds are Cambridge and Oxford. Both universities have central endowment funds as well as individual endowment funds belonging to each of the colleges. As of July 31st 2012, the central endowment funds were valued at £873m[90] and £855m[91] at Cambridge and Oxford respectively, whilst including the colleges' endowment funds gives total endowment funds at the universities of £4.9bn and around £3.7bn respectively.

Some individual colleges at Cambridge and Oxford have very significant endowments. Trinity College Cambridge, for example, has a larger endowment fund than all of the institutions of the University of London combined, whilst four other colleges have larger endowments than any of the universities in the UK other than the University of London (see Table 8 and Table 9).

Other university endowment funds are significant but of a smaller magnitude. The university with the third largest endowment fund is the University of London with £593m. Again the University of London is a composite institution, with individual institutions managing their own endowment funds. The largest individual endowment fund is King's College London's fund of £125m. Four other universities have endowment funds over £100m: Edinburgh, Manchester, Glasgow, and Liverpool.

Table 8: UK university endowment funds with endowments over £100m (at 31st July 2012)[92]

University	Size of endowment fund
Cambridge University	£4.9bn*
Oxford University	£3.7bn*
University of London	£593m
Edinburgh University	£238m
Manchester University	£154m
Glasgow University	£129m
Liverpool University	£121m

*The figures for Cambridge and Oxford Universities include the endowment funds of individual colleges

Table 9: Endowment funds of the five largest Oxford and Cambridge colleges (at 30th June 2012)[93]

College	Size of endowment fund
Trinity College, Cambridge	£691m
St John's College, Cambridge	£344m
St John's College, Oxford	£341m
Christ Church College, Oxford	£310m
All Soul's College, Oxford	£245m

5.3. Characteristics of investment approach

University endowment funds often have an investment board who are responsible for guiding the overall investment strategy and asset allocation, and managing specific assets through a combination of an in-house investment team and external investment managers. This is similar to pension funds (see chapter 10).

The overarching aim of endowment funds is to provide long-term funds for their university, so their investment approach is based on ensuring long term returns. University endowment funds are

[90] Cambridge University Reporter (2012).
[91] University of Oxford (2012a).
[92] The Cambridge Student (2013), University of Oxford (2012b), University of Edinburgh (2012),University of Manchester (2012), University of Glasgow (2012).
[93] Trinity College Cambridge (2012), St John's College Cambridge (2012), University of Oxford (2012b).

primarily concerned with meeting these financial targets; as one investment officer stated "we have absolutely no non-financial objectives."

University endowment funds differ over the extent to which they screen investments. Of the investment officers interviewed, the majority stated that they do not actively screen investments. Some investment officers stated that they had occasionally been influenced by student protests which have led to some changes in investment policy, for example a change of policy on investment in arms manufacturers. However, other investment officers stated that student pressure has little influence on their investment policies.

5.3.1. Ethically and socially responsible investment policies

In recent years several university endowment funds have developed 'ethical' or 'socially responsible' investment policies. These policies are typically based on 'negative' investment criteria, such as commitments not to invest in companies involved in the arms trade. Ethical investment policies demonstrate the importance of ethical considerations over how university endowment funds are invested.

The majority of university endowment funds now have some form of such policy in place, the highest profile exception being the Cambridge University Endowment Fund. Some examples of endowment fund's ethical investment policies are detailed below.

- Oxford University set up a Socially Responsible Investment Review Committee (SRIRC) in 2008 'To review the university's policy on socially responsible investment and its implementation'. An example of the SRIRC intervening in the university's investment practices came in 2010 when the Committee recommended the 'Divestment from any company engaged in the manufacturer [sic] of arms that were banned by UN conventions (e.g. landmines, cluster bombs)'[94].

- Ethical investment policies may be closely related to the mission or values of the university. For example, Queen Mary's ethical investment policy states that it will avoid investments in businesses that conflict with the 'charitable aims of the college'. University College London (UCL) commits to not make investments which 'might conflict, or be inconsistent with the aims, objects or activities of the university'. For example, they would not invest in the tobacco industry, since this would be in 'conflict with UCL's research into cancer'.

5.4. Social investment history

Currently, there has been little involvement of university endowment funds in social investment. However, one example is the investment by two Oxford colleges, All Souls College and Merton College, in the Bridges Ventures Sustainable Growth Fund[95]. This fund provides capital for SMEs in areas including health, education and skills, and ensures that over 80% of investments are located 'in the most deprived 25% of the UK'. The fund allows investors to make financial returns alongside social returns.

One development which demonstrates the potential for university endowment funds to engage in non-traditional and riskier investments, is the UCL's creation of a £25m fund to be invested in start-ups and spin-out technology from UCL, mainly in the area of biomedical research. The fund enables the endowment fund to take an equity stake in start-up enterprises, with the aim of encouraging entrepreneurship and leveraging further capital sources in the long-run. The fund demonstrates that if there is a strong commitment within the university endowment fund's investment committee,

---

[94] Socially Responsible Investment Review Committee (2010).
[95] Bridges Ventures (2013).

they have the potential to make investments driven by motives other than maximising financial return.

5.5. Motivating factors

5.5.1. Investment performance

The primary motive for all university endowment funds when making investment decisions is to use an approach which, as the Cambridge University Endowment Fund puts it, is "Intended to maximise total investment return"[96].

In interviews, endowment fund investment officers expressed that the most important factors to them for evaluating an investment are stability of fund performance, low volatility, risk diversification and the reputation of the product provider or fund manager. To be attractive to university endowment funds, social investments must offer attractive financial investments that compete with the other potential investments endowment funds are faced with.

Even when ethical or socially responsible investment policies have been put in place, most universities are keen to ensure that doing so will not compromise their investment returns. For example, Queen Mary's University's investment policy states that its "Ethical Investment Policy is intended to be entirely consistent with the duty to secure maximum returns from the investment of charitable funds"[97].

> *"If social investment options meet a risk-adjusted return benchmark, driving into a source of return that is sustainable and different from pure equity, then we would consider it, but not for other reasons... they would have to be good financial investments." – Endowment chief investment officer*

Where social investments offer competitive risk-adjusted returns, there may be interest from university endowment funds, as demonstrated by the investment by All Souls and Merton Colleges in the Bridges Ventures Sustainable Growth Fund.

5.5.2. Response to student pressure

Some universities' investment policies have previously been shaped by pressure from students. For example, following a campaign by students the UCL Ethical Investment Review Committee have recently agreed to convene to consider ethical concerns over its investments in the fossil fuel industry[98]. Following pressure from students, the University of Edinburgh agreed to withdraw funds from a company producing drones[99].

> *"At the urging of students, we have been asked to look at our SRI strategy, but because of our decision to adopt a passive management approach, it has been impossible to select anything of the sort." - Director of finance*

Student pressure could therefore be an influencing factor towards university's involvement in social investment in the future, if this were a significant concern to student groups. However, during the interviews with university endowment fund managers, several expressed that they felt student pressure had a limited effect on their investment decisions. In addition, student pressure is mostly been associated with divesting funds that they perceive to be doing harm rather than making social investments.

---

[96] Cambridge University Reporter (2012).
[97] Queen Mary, University of London (2010).
[98] London Student (2013).
[99] The Guardian (2013).

5.6. Barriers to investment

5.6.1. Is social investment the role of university endowment funds?

Many of the investment officers interviewed felt that it is not necessarily part of the core role of university endowment funds to make social investments. Many felt that their responsibility lies first and foremost in ensuring an appropriate financial return on investments to provide funds for the university in the future, and that this aim should not be compromised by attempts to further other objectives. Most stated that they would treat social investments equally to other investments with the same financial return, though some expressed a level of scepticism about the quality of such investments opportunities.

The perception that social investment may be beyond the role of university endowments can be linked to the fact that university endowment funds have a charitable status, and therefore are required to abide by charity law regulation on the use of their funds for investment. This limits investments to those that are aligned with core charitable purpose and/or produce superior financial returns[100].

> *"We would give it lower priority against other investments - We might be less inclined to, because one has to be sceptical about whether having a social objective might distract you from creating a good financial return." – Endowment chief investment officer*

Other investment officers highlighted internal barriers that would have to be overcome to allow the endowment fund to make social investments. A change in policy that committed the fund to social investment would require the agreement of the investment board, and investment officers felt that even if some members were committed to social investment, they would face scepticism and opposition from some other members who might regard social investment "As capable of detracting from our investment performance rather than adding to it".

5.6.2. Knowledge of investment opportunities

A significant barrier to universities' involvement in social investment is their lack of knowledge of social investment opportunities and of how to compare social investments with other investments. This was similarly found to be the case with pension funds, discussed later in the report (chapter 10).

> *'There is probably a degree of ignorance – it is not something that investment managers have brought to our attention.' – Endowment chief investment officer*

Several investment officers interviewed stated that they had very little knowledge of social investment opportunities. This may have led to misconceptions about the opportunities available and the association of social investment with only 'impact-first' products. As discussed above, most university endowment funds would be willing to consider social investments with competitive financial performance. Therefore, increasing the knowledge of investment officers of more commercially-focused social investment opportunities, may be effective in increasing their involvement with social investment.

[100] As noted earlier, at the time of writing the Law Commission is reviewing charity law and has recently published a consultation paper on the legal framework around charities making social investments, which will apply to those university endowments which are also registered charities. See http://lawcommission.justice.gov.uk/consultations/charity-law.htm

5.7. Opportunities to engage

5.7.1. Key personality types

Due both to a lack of available funds for external 'grant-making' and investment objectives which do not enable compromise on financial return requirements, the most sympathetic of university endowments funds fall into 'Benefit of the doubt' personalities. However, the lack of knowledge and awareness of social investment within the sector means that, at present, many more universities are 'All being equal, but…' personalities – not yet convinced that social objectives will not undermine investment performance and looking for solid evidence before they change this perspective.

5.7.2. Where will they contribute?

As implied by the above, universities are therefore unlikely to contribute towards the next £500m in risk investments for social sector organisations. They have no external-focused grant funds which could potentially be redirected towards such investments, and their return-driven investment approach does not enable making financial trade-offs to consider social impact.

The investment of two Oxford colleges into the Bridges Venture Sustainable Growth Fund demonstrates that if social investments are attractive financial investments brought by fund managers with strong track records, universities can be motivated to consider them. It is hence possible that university endowment funds could make commitments towards the next £5bn in established social investments where opportunities can be provided that offer competitive returns. The interviews suggested universities also are generally agnostic as to what sectors such investments might be in, as they do not have any particularly strong social preferences outside supporting their own institution. Universities, however, are less motivated to consider social investments at present than some of the other investor groups considered in this research.

5.7.3. How can they be engaged?

University endowment funds are one of the least knowledgeable investor groups on social investment opportunities. This current lack of information suggests a potentially important role for the social investment market to play in increasing the flow of information to endowment managers and investment committees. Meetings or events where endowment managers or investment committee members can learn about opportunities to make competitive social investments and share experiences could be an important way to increase universities' knowledge of and, by extension, likelihood to consider making investments in the sector.

Mostly, however, university endowments will be encouraged to engage with social investment through greater emphasis of the more mainstream aspects of the investment opportunities, and the evidence and documentation to support this, to allow them to consider social investments as they do their commercial investments.

6. Charitable organisations

6.1. Overview

Charities are not-for-profit organisations established exclusively for charitable purposes – such as the alleviation of poverty or advancement of education – which provide an identifiable public benefit as prescribed by law.

Several UK charities **manage large endowments to fund programme delivery** and/or grant-making, and seek to redirect all income generated effectively to achieve social impact. As a result, charitable organisations have been of particular interest to social investment funds due to their socially-focused raison d'être.

Social investment in the charitable sector is **pioneered by a few 'Allocation but not integration'** personality types who have created allocations within their endowment portfolios to make social investments. These allocations generally are **sufficiently small to pose little overall risk** to the endowment's financial performance, and also can only be invested in the same areas as charities' grant-making activities.

In line with legal obligations governing how charities can invest their funds, the vast majority of charities' involvement with the social investment sector to date has been in the **same areas as charities' programmes**[101]. Support has not come primarily from redirected investment capital but rather **from redirected grant capital**. Most charities prefer therefore to make social investments on a **case-by-case basis** where this is viewed as the best way to support a particular cause and/or organisation. As identified earlier in this report, though treated as distinct in the research, most university endowments and faith-based organisations and many housing associations, are themselves charities (and therefore subject to the same legal requirements).

At present, the charity sector has **strong potential to contribute towards the next £500m in risk investments,** through funds redirected from grants portfolios or modest endowment allocations. These will comprise both direct investments into social sector organisations as well as funds operating in the same areas as charities' grant-making and/or programmes.

Charities are influenced by the investment activities of their peers. Therefore to encourage their engagement with social investment opportunities will also involve continuing to **share experience and evidence** across those charities who are involved in social investment and those considering it as a potential method for achieving mission.

6.2. Sector size and segmentation

As of September 2013, there were 163,361 charities registered in England and Wales. While the sector as a whole reported combined income of nearly £61bn in 2013, the vast majority is held by a relatively narrow segment of large organisations. Only 1.2% of all charities – 1,918 organisations –

---

[101] Charities are allowed by law to make investments into areas that are not aligned directly with their core mission, but only where the investment meets the criteria of maximising financial return i.e. would generate superior financial returns to an alternative, mission-aligned investment opportunity. The Law Commission published in 24th April a consultation paper on charities and social investments. While this general principle of investments in alignment with charitable purpose is unlikely to change, the Commission recognises there is some uncertainty for charities within the current legal framework, and proposes ways of addressing this. At the time of publication the outcomes of the consultation are unknown. See http://lawcommission.justice.gov.uk/consultations/charity-law.htm

reported income of over £5m in 2013 and they accounted for nearly 70% of all income in the sector[102].

In terms of their ability to make significant investments, it is useful to distinguish between grant-making trusts and foundations, and fundraising and operating charities. While the former have been more active in making social investments to date due to their larger investment portfolios – which arguably afford greater room for risk-taking and experimentation with social investment products – several operating charities have also shown an interest in experimenting with social investment or have launched social investment funds in recent years.

6.2.1. Grant-making trusts and foundations

Charities whose main activity is to provide grants and support to other organisations that deliver charitable activities are broadly classified as trusts and foundations. Although such organisations are by no means solely funded through the proceeds of their own investment activities – with the largest grant-making foundation in the UK, the Big Lottery Fund, relying solely on contributions from the National Lottery – several of the largest foundations do derive a significant amount of their income from managing large endowments (see Table 10). The last available estimate valued the total combined investments of the top 500 grant-making trusts and foundations at £40.7bn[103].

Table 10: Top 10 UK trusts and foundations by investment income[104]

Charity	Account year	Total investments	Investment income
1. Wellcome Trust	Sep-13	£14.5bn	£2.6bn
2.Children's Investment Fund Foundation	Aug-12	£2.1bn	£80.7m
3. The Leverhulme Trust	Dec-12	£2.0bn	£64.2m
4. Garfield Weston Foundation	Apr-13	£7.2bn	£44.5m
5. The National Trust	Jul-13	£992.2m	£25.2m
6. The Wolfson Foundation	Apr-13	£671.3m	£21.3m
7. Paul Hamlyn Foundation	Mar-13	£611.9m	£16.0m
8. The Health Foundation	Dec-12	£637.1m	£15.1m
9. Esmée Fairbairn Foundation	Dec-12	£806.5m	£11.8m
10. The Henry Smith Charity	Dec-12	£737.6m	£10.2m

6.2.2. Fundraising and operating charities

By contrast, charities that directly deliver programmes and services, and generate their own income through public or private donations, memberships, trading activities or a combination thereof can be classified as fundraising and operating charities. Although traditionally thought of as less wealthy than their trust and foundation counterparts, at least three fundraising charities – Cancer Research UK, the British Heart Foundation and Oxfam[105] – outranked all foundations apart from the Wellcome Trust in terms of their total income generated in 2013.

However, much of this finance is in the form of restricted income donated to support specific programmes or cover operating costs which will be spent on short-term cycles. As such, while fundraising charities may have impressive turnovers and decent-size investment portfolios in a few

[102] Charity Commission (2013).
[103] Pharoah (2011).
[104] All data taken from latest year-end annual reports and financial statements available.
[105] Cancer Research UK reported income of £536.6m in 2013, Oxfam took in £367.9m and The British Heart Foundation reported £263.6m – available via companies' public filings.

cases, their total investable capital is notably less than that of the largest grant-making trusts and foundations. As Cathy Pharoah notes in a market overview of the UK's top charities, while 96% of the top 500 fundraising charities in the UK receive at least some income from investments, this amounts to over £1m annually for only 14 such charities and is worth less than half a million for the majority remaining[106].

6.3. Characteristics of investment approach

On the whole, grant-making trusts and foundations tend to be return-driven in their approach to managing their investment capital. While this does not always imply a strategy to maximise returns at all costs, charity trustees are legally bound to ensure the foundation has sufficient funds to meet its income needs year-on-year, and to ensure the perpetuity of endowment capital if the charity has a permanent endowment[107]. In practice, this means that all foundations have defined target returns for their investment portfolios.

> *"Loads of foundations have been killed by inflation. You can really get this wrong. Our Governors rotate and sometimes new ones come in and may ask whether we should or shouldn't be doing this or that, but in the end their goal is to say "Under our watch, the future of [the Trust] is just as healthy" – that's what they want their legacy to be."- Grant-making foundation*

While charity trustees have overall responsibility for investment decisions and are left to decide whether to manage this oversight internally or externally, in practice all but an exceptional few outsource their investment management to third party fund managers or advisers. This is generally due to a lack of resource and/or time in-house, with many charity trustees having full-time jobs, and staff often lack the resources and specialist information needed to manage a large investment portfolio. As a result, charitable organisations as a whole tend to be largely cautious and 'passive' investors, with their trustees generally involved in setting the high-level strategy but not involved in taking investment decisions on an active daily or weekly basis.

6.4. Social investment history

While as investors, charities generally are foremost preoccupied with meeting their own income needs to fund in-house charitable programmes and ensure their continuing existence, UK charitable trusts and foundations have been playing a growing role in the social investment market over the past decade. A report on the topic published by the Association of Charitable Foundations (ACF) in October 2013 estimated that charitable foundations have allocated at least £100m in capital to social investments over the 10 years leading up to 2013, with circa £50m of this capital already committed to specific deals.[108]

A small group of 10 foundations with endowments exceeding £100m have accounted for nearly 90% of all activity – with the likes of the Esmée Fairbairn Foundation and the Tudor Trust backing early social investment funds such as Bridges Ventures and CAF Venturesome. The ACF report's authors observe that this is in part due to the fact that foundations with larger endowments have greater flexibility to experiment with a portion of their portfolio without putting critical programme funding

[106] Pharoah (2011).

[107] The Charity Commission's guidance to trustees states that charities with 'a permanent endowment must keep the capital fund invested' and 'only income earned from the investment of the capital fund can be spent on the charity's aims' (Charity Commission for England & Wales, 2011).

[108] Jeffrey and Jenkins (2013).

at risk, though also due to the fact that they typically have more members of staff able to dedicate time to learning about and managing social investments[109].

In terms of where the finance for social investment comes from on charities' balance sheets, while a few 'pioneers' are currently making social investments out of their endowment portfolios, most foundations' experience with social investment to date has been as an alternative to grant-making. As several interviewees who have made social investments explained, they view social investment as one amongst a number of tools they can use to support initiatives that achieve their charitable aims. As such, these foundations' motivations for making social investments are less about the financial returns they might receive – and more about the social impact the finance would help to create as the most appropriate vehicle to support an organisation at a given point in time, and in achieving the foundation's mission objectives.

> *"We've done lots of guaranteeing loans and underwriting capital construction projects over the years. We see it as a flexible way we can help organisations be successful, a way we can help organisations we're also supporting philanthropically. We've made these decision on the basis that there will be a benefit to organisations here and now, without an expectation of returns. Who knows what the returns will be? We're not thinking "this will make us rich."'*
>
> *- Grant-making foundation*

Figure 16: Esmée Fairbairn Foundation's Finance Fund

In 2008, the Esmée Fairbairn Foundation launched a Finance Fund to be a 'social impact first' fund that invests in charities, social enterprises and intermediaries with the objective of generating a financial return along with a social impact. In line with the Foundation's aims, the Fund aims to improve the quality of life throughout the UK by supporting organisations working in the arts, environment, education and learning, and social change. The Fund also has the unique objective of aiming to build the social investment marketplace by supporting the development of products and intermediaries in the sector.

The Esmée Fairbairn Foundation's journey to setting up the Finance Fund began over a decade earlier when it started making direct loans to charities in 1997, mostly in response to requests from grant recipients for support that grant money couldn't help with – for example, financing the purchase of a building. Esmée Fairbairn ran a loan fund for several years before deciding to allocate £21m towards setting up a dedicated social investment fund in 2008 – which was created through a £15m new allocation from the endowment fund and £6m which had been recycled from previous investments. The Fund today has grown to a potential size of £35m and its investments sit on the Foundation's balance sheet as programme-related investments. At the end of FY 2012, £11.9m had been allocated to specific deals through the Finance Fund representing .015% of the Foundation's total portfolio investments[110].

Example investments

- *Social Finance Ltd Impact Bond for Children in Care*: A social impact bond commissioned by Essex County Council to deliver multi-systemic therapy to children at risk of going into care. Repayment will be based on the programme successfully reducing the number of care placement days for this cohort against a historical benchmark.
- *Social Justice Centre*: Loan to the Social Justice and Human Rights Centre, providing office space to charities and social enterprises.

---

[109] Jeffery and Jenkins (2013).
[110] Esmée Fairbairn Foundation (2013).

Despite their apparent advantages of scale, foundations with large endowments are not the only charitable organisations currently making social investments. Among fundraising charities, Oxfam launched its own Small Enterprise Impact Investment Fund in 2012 to invest in local financial intermediaries in developing countries that provide support to small and medium companies. The fund aims to reach a size of $100m and – in the case of Oxfam – allows the organisation to pursue its mission of eradicating poverty through providing capital to entrepreneurs in under-served markets[111].

6.5. Motivating factors

6.5.1. Mission alignment

The Oxfam fund serves as a good example of the common motivating factors for charitable organisations in making social investments. Overwhelmingly, mission tends to be the biggest factor determining what charities invest in and where (partly because of the legal framework governing charities' investment decisions). In the ACF study, over 75% of the foundations which had already made, or decided to make, social investments had done so in the same area as their existing grant programmes. In practice this will often mean investing in the same organisations which the foundation has previously provided with a grant, as this meets requirements for the investment to be aligned with the foundation's core mission[112]. This correlates strongly with how charitable organisations as a group understand the potential role of social investments, as well as the responsibilities of trustees.

Unlike some of the other investor groups profiled in this study, who may view social investment as a socially positive way of generating wealth they are planning to use for other purposes, charitable organisations see social investment as a pro-active tool for achieving their organisational missions. This understanding is partly underpinned by legal requirements – charities are not permitted to make social investments outside of their grant-making areas (i.e. any investments outside the scope of their charitable purposes), *unless* they can be justified on a purely financial basis (i.e. the investment is maximising financial return). Of course, a charity can make a social investment outside of their charitable purposes *if* it meets the financial investment criteria of maximising financial return. This legal requirement around mission alignment relates to the fact that charities exist to further their particular charitable purposes, rather than any charitable purpose generally.

> *"The only way we could get them [social investments] in our portfolio would be if we could quantify the reduction in return by the benefit to our human health goals. This is the only way you could get our Investment Team to look at a reduction on financial return."- Grant-making foundation*

This legal requirement is reflected in the Charity Commission's guidelines on the subject of 'programme-related investments' (PRIs). In CC14, the Commission's updated guidance to trustees on investment matters published in 2011, programme-related investments are defined as investments that allow 'a charity to *directly further its aims* and, at the same time, potentially achieve a financial return.'[113] Therefore social investment opportunities must, as with all investments, meet this intention for the charity to consider making the investment.

Given the uncertainty surrounding the expected return profile for many social investment products in the market at present, most charities' view is that the only opportunities for them to legally

[111] Vibeka (2012).
[112] Jeffery and Jenkins (2013).
[113] Italics author's own, Charity Commission for England & Wales (2011).

consider ‘social investments’ are in areas directly aligned to their charitable aims within their investment portfolio, or as an alternative to making a grant in the programme side of their portfolio. This view was reflected in the interviews conducted with charity trustees and directors and reflects an accurate understanding of charities’ legal obligations, unless it is the case that trustees can justify making a social investment outside the organisation’s core purpose on pure financial grounds (i.e. maximising financial returns) – which social investments are unlikely to provide such justification for.

6.6. Barriers to investment

6.6.1. Legal considerations

The discussion above alludes to what is arguably one of the largest areas for consideration for charities at present. As one foundation staff member explained:

> *“The law at the moment says that you have to invest to maximise financial return, and doesn’t even say that needs to be risk-adjusted financial return. With mixed motive investments, it’s not clear what the underlying law says. It seems to indicate that you can invest in line with your charitable aims, but that can be quite limiting for many.”*
>
> - *Grant-making Foundation*

Note the Law Commission, at the time of publication, is looking at charity trustee investment powers and duties in relation to mixed purpose social investment (i.e. an investment pursuing both a social and financial return)[114]. The Commission has recently published a consultation paper, acknowledging there is uncertainty for some charities around the legal framework governing their social investment decisions, and proposing possible ways of addressing this. This includes a suggestion to introduce a new statutory power for charities to make social investments, accompanied by a (non-exhaustive) list of factors for charities to consider. These suggestions are under consultation at the time of publication and therefore it is unknown whether and how the legal framework will change in the future. The core principle of charities’ investments having to be aligned with their core purpose of producing a public benefit, will not change however.

Of course, where a potential reduction in returns is not present, charities are free to consider social investments like any other financial investments. However, the ACF study found that most of the foundations engaged in social investment to date had found their social investment portfolios tended to produce risk-adjusted returns below those of their conventional investments. As one participant in the ACF study identified, this does not build support for the view that social investments could be seen as an acceptable alternative to investments rather than grant-making[115].

However, this is not to say that given time, and market development, social investments are unable to produce risk-adjusted returns on par with conventional investments. In addition, many of the ACF study participants found lower risk-adjusted returns acceptable, provided that the lower return was balanced by a higher-risk-reward investment in another part of the portfolio, or if investment had been the best way to support a particular project at the time.

---

[114] See: http://lawcommission.justice.gov.uk/consultations/charity-law.htm
[115] Jeffery and Jenkins (2013).

6.6.2. Lack of capacity

Beyond the legal considerations and the perception that social investment opportunities at present offer rates of return that are below the targets set for many charitable funds, interviewees also cited internal resources as being a barrier to making social investments. As most endowments are managed externally and overseen by trustees who often also have full-time jobs, there is generally a lack of capacity to learn about social investments and think them through in a strategic way.

> *"Resourcing is an issue – even a large trust might be run by a trustee when they get home in the evening after work. A challenge for a lot of trusts/foundations is the way people are allocated – they will often have grant-making staff in-house and investment managers handling things externally. Most don't have many staff as they strive to be efficient to get the money to beneficiaries. So there's generally a lack of capacity to think it through." - Grant-making foundation*

6.6.3. Opportunity cost

Perhaps as a result of the fact that most social enterprises and product providers have initially targeted charities as hypothetically more sympathetic investors, the interviews uncovered that charities in particular feel more pressured than other institutions to consider social investments. Charities also felt that the default position of funding social programmes through their grants is one through which a lot of social impact can be created, and which isn't necessarily less effective than making social investments. As one foundation director explained, "The default position is an easy one – there is a queue of people at the door for grants, there is a lot of demand', and 'There's no evidence that impact investment creates greater social value than grant-making."

6.7. Opportunities to engage

6.7.1. Key personality types

The UK charitable sector is split in its stance towards social investment. Among organisations with significant investment capital, a small core of pioneers have taken an 'Allocation but not integration' approach to making social investments out of their endowment portfolios. A much larger group fall within the 'Benefit of the doubt' and 'All being equal, but…' personality types. While not against social investment, these personalities feel that it is not the most appropriate form of investment where it does not present many opportunities in line with their core programmes, or allow for maximising financial returns.

Finally, there are a number of passive personality types amongst charities who outsource investment management due to a lack of capacity and/or interest in investment matters in-house. Others are 'Don't leave me behind' types, conscious of not wanting to be caught out as the last organisation in their sector to not be investing in line with accepted norms, but also unlikely to take an active interest in socially investing until they feel others in their sector are also doing so.

6.7.2. Where will they contribute?

As most charities will consider supporting social investment through grants portfolios rather than with investment capital, they will be motivated by the potential impact social investments can achieve in their core areas of focus rather than by financial performance. As such, charities are likely sources to contribute towards the next £500m in risk investments required by social sector organisations. These will likely come in the form of both direct investments into such organisations and funds which are sufficiently 'tailored' to be viewed as in line with charities' individual missions.

There are also a number of ‘Benefit of the doubt’ investors amongst charitable organisations who would prefer to make socially-positive investments over commercial ones where it can be assured that these investments will meet portfolio income requirements and, by extension, fiduciary duties. It is hence also possible to see charities contributing towards the next £5bn in established investments through their investment portfolios where these opportunities can be presented as sound financial opportunities.

6.7.3. How can they be engaged?

There are a few relatively straightforward things that can be done to make social investments both more attractive and feasible for charities in the short- to medium-term. Education and awareness-raising examples and case studies of where charities have made social investments would help charities to better identify and understand the opportunities available to them, and how to practically go about making social investments. This could to enable charities to look more flexibly at how finance can be deployed across their investment and grants portfolios, while keeping in line with their legal duties to consider core mission, financial return and broader public benefit.

Secondly, the interviews for this report indicated that charities could be more motivated to consider social investments if they could be shown to be a more efficient vehicle for achieving mission vis-à-vis grant-making. Research examining the overall social return on investment for programme-related investments made directly out of investment portfolios vis-à-vis the social return of an equivalent grant in the same area - taking into account the amount of money that has been be invested to ‘finance’ the grant amount - could be useful to inform this debate.

Thirdly, the restrictions on foundations considering below-market returns for social investments in areas outside their charitable aims indicates that, in certain instances, where social investment products have more established track records and present a strong financial offer, it may be more productive to not to market them explicitly as ‘social’ opportunities at all. One interviewee, who has extensive experience marketing social investment products to charitable foundations, relates that many foundations get stuck on considering whether a product is sufficiently within their social aims to invest in, rather than looking at the business case as a good investment opportunity. Somewhat paradoxically, whereas selling the ‘investment story’ of a particularly lucrative social product might appeal to the charity’s investment objectives, marketing the same product as a ‘social investment story’ within an area of impact different from a charity’s own may actually create a barrier where there need not otherwise be one[116].

Lastly, the interviews shed light on what could help charities and their trustees to overcome current knowledge gaps and lack of understanding of the social investment market. Almost all interviewees were aware of and cited as helpful the ‘Social Impact Investors’ Group’ (SIIG), a sector-specific forum to learn about social investment. The Group is co-convened by the Trust for London, Lankelley Chase, Esmée Fairbairn, and Friends Provident foundations, and holds closed meetings three times a year among foundations to discuss common issues related to social investment and share experiences. The Group also holds three to four market information days annually which invite social enterprises and product providers to pitch, and invite other trusts and foundations to listen in. As one of the convening organisations relayed:

> *‘’The feedback has been that it’s been very helpful to people – it’s helped us learn together. At the market information days, it helps people build confidence that they can look at an investment proposition and take a decision on it. To build the confidence that you can say to someone “why are you making it difficult for me to see the numbers?” and feel that you can*

[116] Conversation with market stakeholder, January 2014.

> *ask sensible questions. Co-learning is very useful… It is there to be a go-to place so you can hear about what's going on.'*
>
> *- Grant-making foundation*

Such initiatives which support mutual learning and experience-sharing in confidence across peers should be supported and encouraged, as they currently provide the most trusted way for potential new and existing investors with hesitations about social investment to move up the learning curve.

7. Family offices

7.1. Overview

Family offices are private wealth management advisory firms established by ultra-high-net-worth individuals (UHNWIs)[117] exclusively to manage a single family's, or a group of families,' wealth.

The most **significant influencing feature** of any family office's investment strategy is the needs of the **wealth owner(s)**. As such, family offices are highly individualistic organisations and no two operate in the exact same way. Family offices **span the entire spectrum of investor personalities** identified in this research. Some are willing to consider adjusting their return targets to **pursue a 'Go the extra mile', values-based approach** to investing across their portfolio, while other family offices focus on wealth preservation and do not undertake philanthropy.

That said, much of the investment history and unique characteristics of family office structures makes them **better suited as a group than others to take on the risk and 'patient capital' requirements** to contribute towards the next £500m in risk finance market investment opportunity. Depending on their size, family offices may contribute towards this demand **through their philanthropy portfolios or core investments**.

The very large size of some family offices – in particular, large multi-family offices – also indicates that contributing towards the next £5bn in **established social investments will be the most plausible entry point for some**. Internationally, many family offices have been involved in supporting more established social sectors including microfinance and sustainable agriculture. These opportunities may well prove most suitable to those family offices which require larger investment sizes and/or managed funds to invest in, given the **relatively modest capacities of most family office investment teams**.

As a largely **insular sector built on personal relationships** and recommendations, growing the participation of UK family offices in social investment will require efforts to be spent on relationship-building. Family offices will be encouraged by **hearing about the experience of peers** with social investment and how such approaches can contribute to building a family's legacy. While their highly individual goals indicate that family offices are **unlikely to move as a sector** towards making social investments, the **greater flexibility of their capital**, interest in 'unconventional' investments, and belief amongst many in a values-based approach to investing, makes them a **priority group to engage to grow both ends** of the social investment market in coming years.

7.2. Sector size and segmentation

While family offices vary widely in their size, structure and range of services managed in-house, any wealth management firm that does not offer its services to the public, provides advise exclusively to family members, and is wholly owned and controlled by them, is considered a family office[118]. The private nature of family offices means little public data is available on their total numbers or assets, though it is estimated there are currently over 1,000 family offices across Europe[119]. Zurich and Geneva have traditionally been popular locations for High Net Worth Individuals (HNWIs) to set up private offices, though a growing number of family offices have opened in London in recent years.

---

[117] Ultra-high-net-worth individuals are defined as having over USD $30m/GBP £18.6m in investable assets, excluding primary residence, collectibles, consumables, and consumer durables. For definition see Capgemini & RBC Wealth Management (2013).
[118] For definition, see Capgemini and RBC Wealth Managament (2013).
[119] Family Offices Group (2011).

Family office structures have been growing in popularity due in part to the repercussions of the 2007/08 financial crisis – family offices were affected less than private banks and hedge funds, and many HNWIs were left distrusting of banks[120]. Specialist wealth management consultants Scorpio Partnership estimate there are currently around 100 multi-client family offices active in London in addition to over 300 single family offices[121].

The rise of family offices also is correlated with the rising numbers of wealthy individuals globally. Despite the economic downturn, the world's population of HNWIs and their aggregate investable wealth hit record levels in 2012 – with an estimated 12 million individuals worldwide holding over £620,000 in investable assets. In Europe, there are approximately 3.1 million HNWIs with investable assets worth £8.1trn in total[122]. Within the European market, the UK has the second highest concentration of HNWIs (after Germany) with approximately 465,000 persons qualifying as such[123].

While a precise profile of family offices as a group is therefore difficult to obtain, it is nevertheless clear that the growing preference of Ultra-HNWIs for using such vehicles to manage significant wealth makes family offices a potentially deep pool of capital to be 'tapped' into.

Family offices are generally classified as either single-family offices or multi-family offices, with some differences in approach that may impact their likelihood to consider certain asset classes.

7.2.1. Single family offices

A single family office is an organisation built exclusively to support the wealth management needs of a specific family. Single family offices typically employ a small team of dedicated wealth management professionals who – depending on the family's needs – may provide advice on estate planning, evaluating investments and performing due diligence, tax advisory, as well as philanthropy management. As a result of the costs associated with employing dedicated talent across these disciplines[124], a single family office generally only becomes affordable for individuals with over £62m in investable wealth[125].

From the perspective of HNWIs, the advantage of using a family office as opposed to a wealth management firm is that a family office provides a comprehensive, 'one-stop-shop' for all information and advice related to wealth management. A single family office also can be tailored to meet a specific family's investment and other wealth management goals – with several family offices, for example, specialising in and investing in alternative assets[126].

7.2.2. Multi-family offices

As the label would suggest, multi-family offices provide family office services to more than one family group. Such firms may serve anywhere from two to 500-plus clients, and for this reason are sometimes thought of more as 'boutique' wealth management firms. Multi-family offices still provide a range of custom services to clients while helping HNWIs achieve economies of scale through, for example, jointly affording some services that would not be feasible otherwise. As such, multi-family offices can become affordable to HNWIs with investable wealth of circa £30m or less.

---

[120] Capgemini (2012).
[121] Sherwoood (2008).
[122] Figures converted from CapGemini & RBC Wealth Management (2013) data using Bank of England year-end exchange rate.
[123] CapGemini & RBC Wealth Management (2013).
[124] Family office running costs are often estimated at >£700k/year.
[125] Figures converted from CapGemini (2012) data using Bank of England year-end exchange rate.
[126] Family Offices Group (2011).

7.3. Characteristics of investment approach

While family offices vary widely in their size, investment philosophy, charitable goals, and reliance on in-house vs. external investment advice, there are some broad differences in the way single and multi-family offices take investment decisions that are relevant in assessing their potential appetite for social investment. Compared with multi-family offices, single family offices "Often take less conventional positions and adopt highly intentional, tailored investment programmes, given longer term financial time horizons, discretionary wealth, limited reporting requirements or need for public 'fiduciary' conservatism, and shorter chains of decision-making"[127].

> *"It might be slightly easier for family offices to get involved because of their nature - we are dealing with living donors who can explicitly say what they would like to do with their capital. They can be more willing to align their philanthropic values with their investment approach." – Single family office*

In other words, single family offices are frequently their own fiduciary, and can make and alter their investment decisions with significantly less constraints than institutions managing wealth on behalf of a wider group of stakeholders.

For this reason as well, single family offices or small multi-family offices are more likely than other investor groups to take a 'passion' approach to investing – focusing on investments in markets or geographies of special interest to principal family members. As one London-based multi-family office director serving 10 families explained, "Some clients have objectives for their money – restrictions as well as negative and positive imprints they'd like reflected in their portfolio. As we have a small number of clients, we can develop something bespoke to their goals."

Furthermore – and a key consideration for assessing the 'fit' of social investment products with family offices' investment goals – family offices typically have longer time horizons than other institutional investors. The primary objective of family offices is to preserve family wealth over generations rather than, for example, having to pay out a defined return on a regular basis. As such, family offices can generally tolerate greater levels of risk and volatility in pursuing longer-term rewards, and historically have played a role in pioneering new asset classes.

> *"As a family office we can have longer time horizons than other institutional investors. Other institutions are quite time limited and want the return of their capital and a return in 5-10 years. Although we offer exists [from our fund] we advise clients to take a long-term view and don't expect anyone to redeem. This tends not to be taken up unless someone passes away." - Single family office*

For example, in the development of venture capital (VC) towards an asset class, VC funds benefited significantly from the less risk-averse behaviour of family offices. As many family offices are initially set up by successful entrepreneurs themselves, family offices have also played a key role in providing finance for small and medium enterprises. Many thus distinguish family offices based on where they are in their 'life cycle' – with those that have been established more recently, often still having entrepreneurial individuals who enjoy being involved in investment decisions and have an appetite for risk-taking.

Reflecting this pioneering quality further, family offices also have taken a lead in recent years in making investments in frontier markets – for example with regard to investments in Africa - due to their possession of 'patient capital' which can be invested for the longer-term, in so doing realising double-digit returns 5-10 years onwards[128].

---

[127] Nicklin (2012).

7.4. Social investment history

For the reasons outlined above, family offices can be seen both as a 'wild card' investor group – reasonably opaque and with diverse characteristics due to strongly individual investment goals – and also potentially as the most predisposed for social investment. Due to their greater appetite for risk, lack of institutional constraints and maverick approach to experimenting with new asset classes and markets, family offices may be the best suited investors for the more innovative, equity-like investments on offer in the social investment market at present.

The experience of family offices with social investment to date implies the latter is a well-shared perspective among those who have been involved in marketing social investment products to multiple investor types[129]. Particularly when looking at the development of social investment globally, numerous family offices and foundations have been at the vanguard of testing new social investment products and approaches. As one family officer adviser working with families across the UK and Europe expressed, compared to five years ago "The interest [in social investment] is huge, there's loads of hype and interest."

In some cases, as wealth holders have become knowledgeable on social investment there have been cases where they have instructed their family officers to make specific investments on their behalf. In addition, some family offices have set up dedicated social investment funds for their clients where they saw an opportunity to appeal to clients' values. As one large family office which had set up a multi-million pound impact fund for family members explained:

> *"We had some clients interested in microfinance seven to eight years ago. We were asked to monitor private investments, which was relatively inefficient, so we decided that we might be able to get enough interest from our clients to create a product and structure an explicitly impact- orientated fund. That took three years to set up. Structuring the legal framework was the most difficult because we have [family members] in so many different locations, but then it only took three to four months to fundraise. Less than 10% of our clients are in the impact fund, but we only approached those we thought would be interested because of their current investment profile, and within that group we experienced almost no pushback. We marketed the fund as impact first and asked for a long-term horizon, but it is structured as a liquid fund, so clients can get out every quarter if they want. They can also invest as little as €50 so we made it a low barrier to entry."*
>
> *- Single family office*

While the experience above is unique in that it involved a highly proactive family office with significant capital willing to do considerable work to structure a social investment opportunity, those who know the family office space, believe the frequency of such cases will grow. One London-based adviser working with a group of UK family offices was aware of at least 10 who had already make social investments, and felt that several more will be ready to make social investments in the next three to five years:

> *"I think [the amount invested by family offices] will increase significantly - the movement into impact investment will be led by families and some retail investors as well. One of the issues right now is just that there is no track record or a limited track record. Once this improves families who have a real passion and different type of capital will be able to enter the market more readily." - Family office adviser*

---

[128] Cohn (2013).
[129] See, for example, Balandina (2010).

Figure 17: Willows Investments

One particularly prominent example of a family-managed social investment fund headquartered in the UK is Willows Investments[130], set up in 2007 by Stephen Brenninkmeijer of the Brenninkmeijer family, (founders of the C&A clothing chain in 1841).

Willows Investments makes convertible debt and equity investments into privately-held companies, as well as providing capital to private equity and debt funds, to support market-led approaches to social challenges. The fund focuses primarily on investments in developed markets and takes a priority interest in businesses providing access to finance, education and healthcare solutions as well as investments in social enterprises.

Example investments

- *Fair Finance*: London-based social business providing affordable financial products and services to individuals who are typically excluded by mainstream banks.
- *Social Stock Exchange*: Platform to showcase and measure the impact of listed companies which have a social or environmental impact.

Stephen serves as the main Principal for Willows Investments. Since starting making social investments with his own wealth a decade ago, he has played an active role in helping the larger Brenninkmeijer family's family office set up a €100m impact investment fund through encouraging other family members to experiment with social investment through moving 5% of their portfolio into the fund.

7.5. Motivating factors

While the scope for diversity across family offices is significant, there are some common motivating factors that may increase their propensity to try social investment.

"The reasons family offices will get involved are that they want more out of their investments – you are expressing your worldview through your investments… they want sustainability and solutions." - Family office adviser

7.5.1. Values-based approach to investing

Firstly, because the personal interests and passions of senior family members often play a strong role in influencing what sectors and asset classes the family office's investment arm considers, it is common for family offices to take a values-led approach to investing. As one multi-family office commented, "A lot of family offices are starting to look at [social investment] because of the links between financial return and one's personal values."

Advisers commented that the impetus to get involved in social investment "Is almost always the family's values and wanting something beyond financial return." Others commented that families' frustrations with philanthropy and typical modes of wealth creation following the financial crisis might also motivate them to try something different.

"One of the reasons [family offices can do social investments] is that they can make decisions quicker and easier. My client does a microfinance fund. It's his money. He wants to do good with it. He is able to say, "Yup $1m," whereas for institutions the process is much longer." - Investment consultant

[130] For further information, see http://www.willows.uk.com/

7.5.2. Availability of managed funds

In terms of the types of investment products that would appeal to family offices, there is a preference for investing in managed funds over undertaking direct investments. As one family office adviser explained, most small family offices only have two to three staff members and adopt a passive management approach for their portfolios, so offering managed fund options would be key:

> *"Many wouldn't think of a bank or intermediary, they would think of investing in a fund with others where they could spread the cost and time effort. There needs to be an actively managed portfolio for them to consider it because, let's face it, it does require higher due diligence and most small offices manage most of portfolio passively – they do manager selection."*
>
> *- Family office adviser*

7.6. Barriers to investment

While the entrepreneurial spirit of a founder may predispose family offices to have greater appetite for risk investments into early-stage enterprises, many family offices still often find direct investments into social enterprises too difficult given the limited due diligence and oversight capacities of often small family office teams. A lack of available managed fund opportunities thus was cited as a barrier.

> *"Accessing advisors and knowing who to trust are really important for family offices – this is true in any advisory work, it takes time, relationship building, and recommendations from others who they trust. Because the industry is so new there isn't this longevity. A lot of families don't have much time to give, and they don't want to have to pay to join a network and research things." – Family office adviser*
>
> *"Getting started is the biggest barrier – figuring out, 'where do I begin?' It's quite a daunting thing, who do you trust and turn to? Without a track record it's hard to know where to go for advice. Many are looking to see other families lead." – Family office adviser*

7.6.1. Reputations of fund managers

As an industry built on personal recommendations, the lack of specialist advice was rated the most frequently by interviewees as a barrier to family offices making social investments. Many advisers and family office staff themselves commented that it is difficult to know where to go to for advice in the social investment space. A family office considering getting involved in a new sector or asset class would typically look first for a recommendation from a friend or other family office for an adviser to work with, though interviewees expressed that such individuals are hard to come by in the social investment space.

7.6.2. Lack of knowledge

Interviewees also suggested that a lack of straightforward resources and opportunities to learn about social investment is a barrier for many family offices. A principal family member who had made social investments commented, "Amongst family offices, the main barrier at present is a lack of knowledge. They would do it if they knew more." At present interviewees feel that getting involved requires significant time and resources, both because there is a lack of clarity around what social investment means, and because social investment opportunities aren't always presented in the same way or using the same language as the commercial opportunities which family offices are used to.

7.7. Opportunities to engage

7.7.1. Key personality types

Family offices are the most diverse of the investor groups examined in this research. Organisations span from 'Go the extra mile' personalities who have made commitments to investing 100% of their portfolios socially, to those with strong wealth preservation goals, and little/no consideration of social impact.

7.7.2. What will they contribute towards?

Family offices that have active philanthropy portfolios and/or are led by asset owners who are 'Go the extra mile' personalities have the potential to contribute towards the next £500m in risk finance investments. Family offices' long-term outlook enables them to consider less liquid investments, and their social interests are sufficiently diverse that they can consider – or be motivated to consider – social investments in a wide range of sectors. However, given the often limited capacities of family office investment teams, these opportunities will typically need to be presented through managed funds rather than direct investments.

Family offices also have strong potential to contribute towards the next £5bn in established social investments. Many family offices specialise in investing in alternative asset classes as well as real assets. Hence, larger investment opportunities in sectors including sustainable forestry, agriculture or social housing/infrastructure could be of interest particularly to larger family offices.

7.7.3. How can they be engaged?

Building on the insight that education and awareness of social investments are key barriers to engagement for family offices, one way of overcoming this would be private, knowledge-sharing events, which bring together both family offices that have had experience with making social investments and others wanting to learn about the sector. The family offices interviewed commented that a few of the social investors' networks they are part of are the single most useful resource for learning about social investment, chiefly because they could *"Pick up best-practices from peers and learn from how they're approaching different issues."*

The family office space is strongly focused on relationship-building and personal recommendations, and gaining the trust of this group and building the reputations of fund managers will take time. However, the strength of values-based approaches to investing, the greater flexibility of capital, and lower internal barriers to doing something 'new' compared to other investor groups, indicates that time invested in educating family offices and support on their journey to making social investments, may well produce generous pay-offs.

Family offices have the ability to influence other family offices, and while their actions are unlikely to have a ricochet effect on larger investor groups, they are arguably one of the most promising groups for increasing their investment activity at both ends of the social investment market in the short- to medium-term.

8. Corporations

8.1. Overview

Corporations are large businesses or groups of businesses authorised to act as a single legal entity.

While corporations have potential as valuable sources of capital and – in the case of financial services firms – conduits to wealth owners, the **majority of UK corporations' involvement** with social investment to date has **not been through core business streams but rather via their corporate social responsibility** (CSR) initiatives. **Social enterprise** and investment have become **popular themes** for corporation community engagement programmes, with a noticeable uptake in the amount of finance and in-kind support committed by UK businesses to the market over the past three to five years in particular. Though, it is also worth noting a difference in corporations' approach to social investment, based on the nature of their core business operations i.e. financial services corporations are more likely to develop proprietary products or set up investment funds with social investment aspects, whereas consumer goods and services companies might primarily use their products and/or CSR activities, to engage with social enterprises.

Within the CSR and corporate community engagement streams of activity, **several corporations have taken an 'Allocation but not integration'** approach to social investment, creating portfolios to make direct investments into social sector organisations and/or funds **frequently in sectors related to their own professional expertise**, and often including a strong element of **staff engagement and/or in-kind giving** with their programme of support. While the sums available within these 'investment' portfolios are generally redirected from CSR budgets rather than business investments, encouraging the further growth of this activity could substantively increase the amount of capital available for the next £500m risk investments to social sector organisations.

At the **more established end** of the social investment market, corporations tend to be less interested in investing in external funds and show a **preference for making such investments in-house** – for example, banks taking decisions to invest in renewable energy as part of standard business activity. While not considered a flow into the social investment sector in the traditional sense, capturing such investments into 'social' sectors by mainstream businesses could **help towards building an evidence base for social investment performance** and increase awareness amongst peers and competitors of opportunities to make social investments 'in-house'. While they are not passive investors per se, many corporations exhibit elements of the 'Don't leave me behind' personality type, **keen to not fall behind their industry** in their support for innovation, or for their reputation among consumers to fall behind competitors'.

As such, corporations can potentially be targeted as a **priority group primarily for raising the next £500m in risk finance** capital for the social investment market, with a focus taken on how to structure investment funds and skilled volunteering opportunities for more UK businesses keen to support social enterprise.

8.2. Sector size and segmentation

As of year-end 2013, there were 7,000 large businesses in the UK employing more than 250 staff, and 1,144 businesses with a turnover of greater than £1bn[131]. As an investor group, corporations have widely different financial management strategies and investment goals. While some may focus on achieving business growth through mergers and acquisitions, others focus on investing internally through exploring what new business streams or products can be incubated in-house. Others in the

[131] Rhodes (2013).

financial services industry focus on managing investments to achieve returns both for clients and their own balance sheets. As such, it is difficult to speak of a unifying 'investment strategy' across UK corporations.

8.3. Characteristics of investment approach

To obtain a picture of the amount of capital potentially held by UK businesses to invest at a given point in time, it is perhaps helpful to look at businesses' cash reserves[132]. Recent estimates put the total value of cash reserves held by private non-financial companies[133] at as much as £729bn – equivalent to over 45% of UK GDP[134]. However, the majority of this cash is held in bank deposits and short-term, highly-liquid investment holdings which businesses can draw on as needed to invest in growth or cover shortfalls, making this resource ineligible for the vast majority of social investment opportunities.

Alongside mainstream investment allocations that some corporations have, there are several other routes through which corporations can and do engage with the social investment market. One specific route for financial services organisations for example, is to develop proprietary products and/or encourage clients into the social investment market as a means to facilitate the flow of capital. For corporations providing consumer/business to business goods and services, there is the opportunity to look at their own procurement, investment and/or business growth strategies as potential touch-points to engage with social sector organisations – examining, for example, where it might be possible to procure from or invest in social purpose businesses and social enterprises. Finally, many businesses run corporate social responsibility (CSR) and/or sustainability programmes with explicit goals of creating value for communities beyond the business. The total value of worldwide community investment spend by the largest 300 corporate donors in the UK was £2.6bn at last estimate in 2009/10[135].

8.4. Social investment history

It is out of corporate social responsibility funds that the vast majority of corporate engagement with the social investment market has taken place to date. Social investment and social enterprise have become an increasing focus for UK businesses over the past five years, with a steady stream of new business-supported incubators and social enterprise programmes springing up across multiple industries.

Particularly within the financial services industry, several large corporations - for example RBS and Deloitte (see Figure 18) - have set up social enterprise incubator programmes and/or investment funds in recent years as part of their CSR portfolios. Given their own business expertise in providing finance and consultancy services to support business growth, backing enterprise-based solutions to social and environmental challenges has both a strong alignment with in-house knowledge and – frequently – business communication goals.

---

[132] The money that businesses keep on hand to meet short-term or emergency funding needs.
[133] Private sector companies that produce goods and services for the market and do not primarily deal in financial assets and liabilities.
[134] Gregory and Masters (2012).
[135] Figure includes value of in-kind donations where reported by the business (Pharoah, 2011).

Figure 18: Deutsche Bank Impact Investment Fund[136]

In November 2011, Deutsche Bank launched its first 'Impact Investment Fund', an up to £10m fund providing finance to UK-based social enterprises via intermediaries with the aim of generating both a positive social impact and financial returns. The Fund is to be invested over three years and repaid over 10 years.

As well as making investments in areas connected to Deutsche Bank's CSR programme goals, the Fund seeks to play a role in developing the social finance market. A representative from Deutsche Bank described it as 'a CSR activity sitting in the business line', which draws on the expertise of the bank's private equity and charities teams to analyse potential investment opportunities and assess and monitor social impact.

Example investments

- *Big Issue Invest Social Enterprise Investment Fund LP*: Fund providing medium to long-term growth capital to organisations using socially-driven and sustainable business models that are improving the lives of the most disadvantaged communities and individuals in the UK.
- *Bridges Ventures Fund III:* Fund providing growth capital to small and medium sized businesses in sectors where underlying social or environmental need.

Interest in social investment is not limited to the financial services industry however, with other flagship initiatives such as Wayra, telecomm provider Téléfonica's technology incubator, launching a highly visible partnership with UnLtd in 2013 to invest in tech-based social enterprises in the UK, now in its second year[137]. Also in 2013, energy company Centrica launched the UK's first energy-focused social investment fund in partnership with Wayra. The 'Ignite' fund will be a £10m fund to support social entrepreneurs in the energy sector with specialist business support and a minimum of £50k investment[138].

8.5. Motivating factors

The motivating factors for businesses to get involved in supporting social investment are several-fold, and span a combination of business growth, internal staff engagement, and external communication and CSR goals.

8.5.1. Contribution to society

More than any other group examined in this research, the business directors interviewed feel social investment is a market their organisation should be involved with supporting. One CSR director suggested that businesses are better placed to take risks with their capital than some other groups, and that it is the role of business 'to lead the way' in developing innovative new financial products and markets.

"Yes, absolutely it is our role [to make social investments]. Big business has been seen as an evil player in its overall role in society. Supporting disruption, change and willingness to operate differently are hugely important - innovation isn't coming from big companies"
- Corporation director

[136] Deutsche Bank (2013).
[137] See: http://wayra.org/unltd/
[138] See: http://ignitesocialenterprise.com/

8.5.2. Internal and external engagement goals

There was also a strong feeling that social investment fits well with staff engagement goals for several businesses. Particularly for millennial employees[139], who believe strongly that businesses must make a positive contribution to society, businesses see a direct opportunity for staff to do skilled volunteering placements supporting social enterprises in similar sectors, or with general business support needs. As one financial services firm stated, "We are acutely aware that this must be on the agenda, and there is a desire from within the team to gain an understanding of social investment. A number of individuals within our team want [the business] to invest in and mentor social enterprises."

> *"We started [the social investment fund] because we were interested in maybe developing a product for clients but we have to learn about the space first. We want to test and understand this market to see if it could be a client strategy."- Corporation director*

8.5.3. Product development

Beyond social investment fitting well with staff engagement goals, a few interviewees in the financial services industry affirmed that part of the drivers for them to get involved with the market is developing client products. Particularly for financial services firms which offer a range of investment management and philanthropy advisory services, there was a view that social investment could become a potential diversifier for attracting or maintaining clients. Hence it was important to begin up-skilling staff now to develop an understanding of the market, and to have capacity to advise on social investments if client demand grows.

8.5.4. Competition

Lastly – and perhaps an unanticipated driver for UK corporations to get involved with social investment – is the desire to not get left behind by peers. One CSR director with an existing social investment fund stated for example, "Three years ago, I would have said we were ahead, but now everyone wants to engage." Another corporation foundation director whose organisation is considering setting up a social investment fund explained, "As an industry, banks follow other banks. People are now asking us, "Where are you [on social investment]?"'

8.5.5. UK-focused opportunities

There is indication that businesses' preferred areas for investment could map well with opportunities in the UK market. Geographically, there was a strong preference amongst interviewees for considering UK-based social investment opportunities, as this is the target market for CSR and communications activities at present. Some – though not all – prefer to invest in sectors that dovetail with their CSR programme themes, or alternatively those which they are already familiar with investing in through their mainstream business.

> *"On geography – it would have to be national. We have a duty to the UK market and our citizens (customers) would say similar things." - Corporation director*

[139] For reference, see Deloitte's annual Millennial Survey tracking the views of young people in full-time employment on the role of business in society conducted across 20+ countries globally. The findings of the survey series point to a growing trend amongst younger employees wherein '75 percent of the global workforce by 2025' will 'want to work for organisations that foster innovative thinking, develop their skills, and make a positive contribution to society.' Deloitte (2014).

8.6. Barriers to investment

Clearly there is a strong opportunity to build on the existing positive interest from UK corporations for supporting social investment. However, corporations also identified challenges in moving beyond their – ostensibly – 'philanthropy' portfolios - to invest larger sums of business and client capital in social investments.

8.6.1. Lack of performance track record

Firstly, a lack of performance track record was frequently cited by corporations as a significant barrier to them doing more in terms of social investment. As consumer and/or client-facing businesses, many corporations stake their reputations and future business projections on their ability to deliver on what they promise. Hence, while corporations are open to using some business capital otherwise intended for charitable programmes to take risks and gain exposure to developing a new market, this is not an option that they would consider in the same way for their own core or client's capital.

"For a bank, reputation is a massive issue. You can't offer things to clients that are unproven." - Bank director

"Risk and reputation are the main factors. We tend to be quite risk averse, and want to uphold our own reputation." - Corporation director

8.6.2. Reputational risk

On this point, businesses in wholly separate industries raised a range of concerns around reputational issues being a barrier to them making social investments, as a relatively innovative form of investment. Business concerns ranged from not wanting to invest in a deal that could potentially go wrong and then being 'seen as the evil organisation who made it go wrong', through to not wanting to be seen to be profiting from services paid for by taxpayers. As one bank director explained:

> *"In the UK, with [social impact bonds] there is a potential issue with making equity-style returns out of services paid for by taxpayers. Even if you have helped make government services more efficient, making money out of it can be seen as problematic from a reputational standpoint. It's harder to attract any blame if you gave the money as a grant rather than an investment. The media can pick up on anything done in the public market in the UK."*
>
> *– Bank director*

Managing the reputational risks associated with any public-facing activity by corporations in the social investment space thus is an important element to consider for those looking to engage business support in this area.

8.6.3. Preference for a DIY approach

When it comes to social investment, many corporations preferred to seek out or create their own investment opportunities rather than to invest in third party funds. A corporation foundation director expressed:

> *"The reason we don't engage with social investment funds is that we do our own. We don't need a framework to get involved, we adopt a DIY approach, spending a significant amount of time going into schools, colleges etc. and helping to get people into work. We are keener on direct investment rather than just placing a load of money into a generic fund."*
>
> *– Corporate foundation*

In line with this theme, several corporations pointed to activities within their core business streams which could be defined as social investment, but currently are not labelled as such. This is primarily because such investments are made internally, in line with core business activities, rather than being invested in external funds. The examples offered range from consumer banks that had made significant loans to charities and social enterprises, through to businesses making significant investments in sectors such as green energy or microfinance that others would typically label as social or impact investments.

> *"In ways, we are already doing a lot. As a bank we are Europe's largest investor in energy efficiency, as well as food sustainability. We also have over £1bn in impact investing as a bank, including microfinance [globally]. We do a lot that has a social return even if it doesn't fall under the lens of being called 'social investment' in this context." - Bank director*

While businesses on the whole are positive in their stance towards social investment, such statements reveal underlying confusion with the way social investment is currently defined, recognised and recorded.

8.7. Opportunities to engage

8.7.1. Key personality types

A select number of UK corporations have taken an 'Allocation but not Integration' approach to social investment through their corporate philanthropy or CSR portfolios, creating allocations separate from mainstream investments which can be then be invested with impact as an overriding objective. The growing interest in social enterprise amongst UK businesses indicates that more corporations could potentially move into this category through their CSR budgets in coming years.

When considering their mainstream investments, businesses tend to fall more into 'All being equal, but…' personality types, preferring to assess the risks and potential opportunities in social sectors themselves, and make investments directly rather than through marketed social investment funds. While businesses don't tend to be passive in their investment approach, there are nevertheless groupings in each industry which fit 'Don't leave me behind' personalities, keen to stay in step with consumer expectations of their sector, and similarly benefit from any 'buzz' generated around businesses supporting innovation in social enterprise.

8.7.2. What will they contribute towards?

Corporations are most likely to contribute towards providing the next £500m in risk investment capital to the market, largely through budgets otherwise intended for community programmes. These commitments will mostly take the form of direct investments into social sector organisations that corporations may also take an interest in providing in-kind support to and/or mentoring. However, the experience of Deutsche Bank's fund also indicates some corporations may prefer to make investments into managed funds which are more comparable to how they would traditionally invest, i.e. client's money.

Corporations may well also increase their investment activity in 'established' social sectors such as social housing or renewable energy in coming years, though this activity is less likely to be directed through marketed funds. Rather it is more likely to be undertaken internally where businesses see a strong opportunity to support growth.

8.7.3. How can they be engaged?

As outlined above, there is a strong opportunity to capitalise on the current enthusiasm for social investment amongst UK corporations, through finding practical ways for them to both place capital into the market and lend their staff skills and expertise.

Corporations see a strong opportunity to support the development of the social investment market through lending their advice and experience to help professionalise the quality of products coming forward as well as to support individual social sector organisations. It might be possible to create a skilled volunteering and/or social investment incubator 'package' for businesses, to help connect businesses with enterprises to mentor in their sector. Businesses could be asked to commit seed capital into collective social enterprise funds as an entry point, in a similar way to how Big Issue Invest and others have structured opportunities for corporations. Externally-managed programmes could provide an attractive way for businesses to send their staff to learn about social investment by engaging directly with it.

Another way of building momentum and awareness among businesses in support of the market might be to recognise the investments into social industries that UK corporations already make, but which are not currently labelled as 'social investments' as they are not investments into external funds. There is a basis therefore for greater awareness and profiling of those UK businesses which are involved in social investment as part of their business operations, and increased recognition for those making transformative investments into the social sector. Through creating greater awareness and building the evidence base around successful investments, other businesses and investor groups could both be inspired to look at the market more seriously and/or consider how to create more social value through the way they ordinarily invest and operate.

In summary, while the total amount of capital put into the social investment market to date by UK-based corporations has been relatively modest relative to the size of their total assets, many corporations have become important champions of social investment and – in some instances – been important cornerstone investors in social investment funds. Continuing and growing businesses' contribution to the market in the medium term will need to be with a view as to how businesses can support their own staff engagement and communication goals through supporting social investment, while also finding ways for them to lend meaningful expertise that will bring additional benefit to the marketplace.

Apart from having an obvious strong financial and business skillsets to lend to developing the overall quality of the market, many consumer-facing businesses have valuable brands as well as expert marketing and communications teams. The value of, for example, Ben & Jerry's putting the stories of social entrepreneurs they have invested in on the sides of their ice cream cartons, is arguably greater in building public awareness of social investment than comparably much larger investments made by private funders[140]. More than other investor groups examined in this research, businesses need to be thought of flexibly in this way as both potential investors and proactive supporters of market development.

[140] See: http://www.joinourcore.com/

9. Insurers

9.1. Overview

Insurance companies are the **second largest institutional investor group** in the UK and form a significant source of funds that is currently relatively 'untapped' for social investment.

Insurers are primarily motivated in their investment decisions to **maximise long-term financial returns**, as well as ensure that their investments **match their liabilities to their clients'**. While large insurers **have made investments into social sectors in the UK** – including, for example, long-term investments in affordable housing and healthcare infrastructure – the size of their minimum investment requirements means that it is **often easier for insurers to 'go it alone'** in structuring opportunities in these sectors rather than engage with social investment product providers.

Insurers primarily fit into **'Benefit of the doubt' and 'All being equal, but…'** personality types. They are sympathetic to investment opportunities which positively impact communities, and in particular any which may **reduce their long-term liabilities** in areas such as, for example, **health insurance pay-outs**. However, their long-term liabilities are such that they can only consider social investments where such products offer **equivalent financial returns to the mainstream, fixed income assets** insurance firms typically invest in.

Growing the engagement of insurance companies in the social investment market will therefore involve presenting opportunities that are **directly comparable in their documentation, risk and return profiles** to the commercial investment opportunities insurers are used to considering in, for example, the corporate bond market. As such, insurers are more likely to contribute towards growing the **more established end** of the social investment market through investing in relatively low-risk, fixed income assets (e.g. stocks in companies operating in social sectors), and through structuring their own approach rather than investing in externally-managed funds.

Similar to the wider corporate sector, insurance companies are frequently **consumer-facing businesses** and have CSR programmes which **could be approached to provide smaller sums of risk finance** to social sector organisations. For example, Legal & General have set up a loan fund to social enterprises in their CSR portfolio. Other insurance companies could potentially be engaged further in this regard – perhaps providing affordable insurance to social sector organisations which would otherwise struggle to secure, for example, facilities insurance as a CSR initiative. The **largest commitments** from insurers, though, are likely to surface once there are **sufficiently established and diversified** social investment opportunities in fixed income assets.

9.2. Sector size and segmentation

Insurance companies held 22% of all UK assets under management as of the end of 2012[141]. The insurance sector is composed of some very large insurers – for example, Legal & General Group, Prudential and AVIVA all have over £300bn in assets under management – alongside a number of smaller insurers, many of which also have sizeable capital pools. Table 11 shows the largest UK insurers for life, composite and non-life insurers.

An important distinction regarding potential involvement in social investment could be between life and non-life insurers (as well as composite insurers which provide both life and non-life insurance). As life and non-life insurers are exposed to different risks, they may take a different view on the social investments that are appropriate for them.

---

[141] IMA (2013).

Table 11: Largest UK insurers by assets under management[142]

	Total assets under management at end of 2012 (£bn)
Life insurers	
Legal & General Group Plc	343.8
Prudential Plc	303.4
Resolution Limited	127.7
Friends Life Group Plc	127.6
Royal London Mutual Insurance Society Ltd	38.6
Composite insurers	
AVIVA Plc	308.1
Old Mutual Plc	142.1
AXA UK Plc	*
General Accident Plc	*
Swiss Re GB Limited	*
Non-life insurers	
Royal Bank of Scotland Group Plc	1,312.3
RSA Insurance Group Plc	21.7
Direct Line Insurance Group Plc	11.6
QBE European Operations Plc	10.8
British United Provident Association Limited	9.8

*Data on assets under management not available using Bloomberg®

9.3. Characteristics of investment approach

Interviews conducted with insurers' investment officers gave significant insight into their investment approaches. Firstly, insurers invest to maximise long-term returns. The ideal investment period depends on the liabilities they are faced with, so may differ between insurance companies. However, in particular for life insurers they may be very long; one investment officer stated a typical investment horizon of around thirty years. In addition, again driven by the need to match investments with their liabilities, insurers are predominantly interested in the fixed income asset classes.

9.4. Social investment history

Market research suggests that insurance companies have so far had little involvement in social investment. A report by the World Economic Forum[143] for example states that insurance companies are currently not very active in the impact investment sector.

Despite this broader trend, there are some examples that suggest insurance companies may be showing an increased interest in social investment and other impact investments[144]. One high-profile insurance company currently involved in impact investing is Zurich Insurance. Zurich has "Pledged a low-risk $1bn impact investment into green bonds to diminish the effects of climate change"[145]. One of the key motivations for Zurich in engaging in impact investing is that they may help to limit Zurich's insurance risks. Because of its exposure to 'social and environmental challenges', Zurich is

[142] Bloomberg®
[143] World Economic Forum(2013).
[144] Impact investing is defined by the Global Impact Investing Network (2014) as 'investments made into companies, organizations, and funds with the intention to generate measurable social and environmental impact alongside a financial return'. Social investing is therefore a subset of impact investing.
[145] Social Enterprise Buzz (2014).

looking to make impact investments that have a 'targeted, positive and measurable impact on society and the environment, but also generate a financial return commensurate with risks'[146].

Zurich's experience may also highlight one of the problems for insurers in making impact investments. Zurich, and other insurance companies, have a preference for fixed income investments, since they best match up with their liabilities. Securities such as green bonds may offer the best class of investments for insurance companies, yet this limits the range of investments insurance companies can make.

In the UK, one insurance company that has been involved in impact investment is Legal & General. Alongside investments in social housing and green energy, in 2013 they committed to invest £15bn over ten years in 'transport and energy projects, house building, property and education'[147]. This investment suggests the vast size of funds insurance companies can potentially devote to social investment and other impact investments (see Figure 19). In addition, alongside the Charities Aid Foundation, Legal & General set up SE-Assist[148], a fund that provides interest free loans to social enterprises, as well as Legal & General employees providing expertise by acting as mentors.

Figure 19: Legal & General's Infrastructure 'Impact Investment' Fund

In 2013, Legal & General announced that it would invest £15bn over 10 years in a long term UK infrastructure investment programme, focused on 'transport and energy projects, house-building, property and education'.

The fund has also made investments in care homes and in hospitals. In December 2013, Legal & General invested £70m to acquire 13 care homes which are let to Methodist Homes, and committed to invest £89m as part of a consortium to build the new Royal Liverpool University Hospital.

Legal & General found infrastructure investments an attractive asset class because it has the potential to provide productive investments with 'an excellent match for [their] long-term liabilities' whilst creating 'roads, schools, and hospitals which benefit the UK population'. Legal & General have decided to invest funds themselves directly rather than through an investment fund.

Sources: Legal & General (2013), Telegraph (2013).

9.5. Motivating factors

9.5.1. Maximising risk-adjusted financial returns

This research has found a major consideration for institutional investors, including insurance companies, is maximising the risk-adjusted financial returns on their investments. Insofar as impact investments offer a risk-adjusted financial return that rivals other potential investments, they will be attractive to insurance companies.

In the interviews conducted with insurers' investment officers for this research, investment officers were keen to stress that they make investments for the long-term, and ensure that investment periods match with their liabilities. In particular, life-insurers have a long-term horizon; one investor quoted a typical investment horizon of thirty years.

[146] World Economic Forum (2013).
[147] The Telegraph (2013).
[148] For more information, see https://se-assist.co.uk/se-assistance/

Because maximising financial returns is of primary importance to insurers, the investment officers interviewed stated they would consider social investments in exactly the same as any other investment with the same financial returns. Therefore, for social investments to be attractive to insurers, they must foremost meet financial performance criteria.

9.5.2. Minimising risks the company is exposed to

"As the social impact bond market matures, I could see there being an interesting opportunity to look at ways for insurers to de-risk life and medical insurance claims."- Investment officer

An added incentive for insurance companies to make social investments could be that they may help to reduce risks that insurers are exposed to. For example, as discussed above, one of the motivating factors behind Zurich's impact investments aimed at providing environmental benefits, was reducing climate change risks, which Zurich is exposed to.

So for example, social investments that provide physical and mental health benefits could be particularly attractive to health and life insurers. One of the investment officers stated that the development of financial instruments that allowed insurers to make social investments that reduced risks of life and medical insurance claims would be very interesting. However, though this potential was identified, they felt that such developments were still a long way off.

9.6. Barriers to investment

9.6.1. Fiduciary obligation

"[Social investment bonds] are like 'trying to plug a power station into an individual's home'. We don't have the time to do the due diligence on such small deals." - Investment officer

As with pension funds (discussed later in chapter 10), investment managers for insurers have a fiduciary obligation to maximise investment returns for their investors. The World Economic Forum (2013) states, "If there is an expected trade-off between profit and purpose, liability-constrained investors will not invest given their fiduciary responsibilities." The fiduciary obligation of insurance companies further reiterates the point that for social investment to be attractive to insurance companies, financial performance is a priority.

9.6.2. Minimum investment size

Many insurance companies manage very large funds, and have very large typical investment sizes, ranging from £8m to £17m[149]. Such investment sizes are typically larger than the size of social investments, even those typically sought by the largest impact investment funds (£2m to £7m)[150]. As the due diligence and supervision costs to the insurer do not change with the size of the investment, insurers therefore often consider it too costly to make smaller investments.

The view that the deal sizes of social investment opportunities are a constraint for insurers was backed up by the interviews conducted with investment officers. According to one investor, "The due diligence time required for a £10m investment is the same as the time required for a £100m investment." Since it consumes a significant amount of staff time to make a small investment, it is considered more efficient to make the larger investment, reinforced by the fact that insurers were not found to prioritise social impact in their investment decisions.

[149] World Economic Forum (2013).
[150] Op. cit.

9.6.3. Availability of appropriate asset types

A further challenge to insurers' involvement with social investment is the availability of appropriate asset types. As discussed above, insurance companies may be particularly interested in fixed income assets, and therefore less likely to directly in equities or in social investment funds. However, one of the investment officers interviewed for the research stated that they also feel there is a lack of suitable investment products available. This may be partly linked to a lack of awareness of investment opportunities, identified as an issue by other investors interviewed for this research.

9.6.4. Knowledge of investment opportunities

Linked to a potential lack of awareness is investment managers' lack of knowledge of investment opportunities, which can be a barrier to insurers' engagement with social investment. Insofar as there are social investments with comparable financial returns to other investments, that may be attractive to insurers, it is essential to ensure investment managers also know about them.

There may also be challenge in altering investment managers' perceptions about social investment opportunities, to demonstrate that they are attractive financial instruments.

> *"Institutionally there is too much time spent on explaining social return, and not enough time spent on making it look like a bland, mainstream bond."* – *Investment officer*

9.7. Opportunities to engage

9.7.1. Key personality types

On the whole, insurers tend to fall into 'Benefit of the doubt' or 'All being equal, but…' personalities in terms of their attitude towards social investment. Though they do not have negative perceptions of social investment, they have long-term liabilities to meet and limited flexibility on financial returns has they need to achieve impact through their mainstream investment portfolios.

9.7.2. What are they likely to contribute towards?

Insurers are focused on matching their investment strategies with their long-term liabilities to customers, and as such will likely only consider making significant investments into well-established social investment products in fixed-income assets – for example, listed equities in social companies, social enterprise/charity bonds, and infrastructure investments. Where they make such commitments however, these are likely to be done in-house rather than invested into marketed social investment funds.

As with corporations more broadly, many insurers are consumer-facing businesses and may potentially be engaged to provide risk finance to social sector organisations through CSR finances rather than investment activities. As such, it may be possible to engage their support for supplying the next £500m in risk finance investments, though not through targeting their sizeable assets under management as might be assumed.

9.7.3. How can they be engaged?

Insurers will be primarily attracted to social investments as investment opportunities rather than for their 'impact' objectives. Therefore there is a need to emphasise the mainstream and more commercial aspects of social investments, so they are more comparable to the relatively low-risk investment opportunities insurers are accustomed to making. As one investment officer stated, "All these investments need to look and smell like another financial vehicle."

In the short-term, it may be possible to raise funds for risk finance through insurance companies' CSR portfolios. Tapping into significant funds for social investment in the long-run, however, will require the development of asset types that meet the needs of insurers - that is, fixed income assets that exceed minimum investment limits. Pooled investment funds could be important in matching insurers' large investment sizes with the smaller social investment opportunities.

In the longer term, there may be an opportunity to use insurance model itself, as a product developer, to help towards developing appropriate social investment products. For example, the use of underwriting of the likelihood of certain outcomes, where there is considerable risk of delivery. This is an emerging potential area that requires more consideration however and cannot be commented on in detail here.

10. Pension funds

10.1. Overview

The UK pension fund sector is the third-largest in the world (after the US and Japan), with a total of £1.7tn assets under management at the end of 2012[151] - equivalent to 112% of UK GDP. Pension funds, therefore, form a very large potential capital pool which is currently relatively untapped for social investment. **If just 0.012% of UK pension fund assets were allocated to social investment this would double the size of the UK social investment market**[152].

While some UK pension fund have demonstrated interest in making social investments – with a **pioneering group of local authority pension funds carving out allocations** to create the sector's first £100m+ impact fund in 2013 – there are barriers to pension funds making social investments. Given their size, many pension funds have **investment size requirements around £50m+** that far outstrip the absorptive capacity of any funds in the sector at present.

Pension funds also have **significant liabilities** in terms of long-term commitments to make pay-outs to pensioners, and consequently have strictly defined portfolio income requirements that are overseen by industry regulators and actuaries[153]. **Fiduciary requirements are perceived** by many to be **non-negotiable** and as such most pension funds fall into '**Benefit of the doubt'** or **'All being equal, but…**' personality types in their stance towards social investment. They do not feel they can look at any investment opportunities that are not unambiguously strong financial investments.

Nevertheless, several pension funds – and particularly **those with a connection to local communities and/or the public sector** – do feel motivated to consider social investment opportunities, with a few institutions already fitting the **'Allocation but not integration'** personality type. The commitments made by pension funds pursuing such approaches are **likely to be in the more established end of the social investment market**, and in **asset classes which can absorb sizable investments**, such as infrastructure.

Growing the engagement of pension funds further towards considering such opportunities will require both **capturing and sharing the experience of sector first-movers** – for example, around how to structure an allocation for social investments within an investment portfolio while meeting fiduciary obligations, and how to reduce the costs of due diligence on smaller investments. It will also require improving upon some of the challenges identified through the experience of these first movers to see where, for example, funds of funds can be structured to enable pension funds to make large investments in areas outside energy or infrastructure, where they already have significant portfolio exposure.

10.2. Sector size and segmentation

UK pension funds invest in a variety of assets, both in the UK and in global markets. Just under half of UK pension fund assets are held in equities and just over a third in bonds[154]. Other than small cash

---

[151] Value in dollars from Towers Watson (2013) converted to pound sterling using the Bank of England end of year exchange rate.
[152] Estimated by City of London (2013).
[153] It is worth noting here the Law Commission's review of the law around fiduciary duties of pension fund trustees – see http://lawcommission.justice.gov.uk/areas/fiduciary_duties.htm
[154] Towers Watson (2013).

holdings, the remainder of assets are held in alternative investments, which includes social investing[155].

10.2.1. Local authority pension funds

One group of pension funds that have made social investments are **local authority pension funds** (LAPFs). LAPFs are for employees working for local government as well as a whole range of other organisations, including Parish Councils, educational establishments, charities and other public bodies. There are 99 UK local authority pension funds, with total assets under management of £148bn as of March 2013[156].

Of particular relevance to encouraging social investment is the regional and local focus of LAPFs. Since their coverage is based on local authority boundaries, LAPFs may be more actively concerned with welfare, in particular in their local area, than other pension funds. Encouraging social investment by LAPFs may therefore ensure regional coverage of social investment.

10.2.2. Defined benefit and defined contribution pension schemes

An important distinction in pension funds is between **defined benefit** and **defined contribution** pension schemes.

- Defined benefit pension schemes promise a specific income on retirement[157]. The pension fund manager is free to make investment choices for their assets under management but whatever the result of these investment choices they must honour the agreed income on retirement.

- For defined contribution pension schemes income on retirement is not fixed but instead depends on factors including the amount paid in and the fund's investment performance[158]. Since income on retirement depends on investment performance, defined contribution pension schemes may offer members a degree of choice over how investment decisions are made, such as high or low risk options, or ethically or religiously-designed schemes.

The importance of the distinction between defined benefit and defined contribution pension schemes for social investment lies in the fact that consumer choice may be a more powerful factor driving investment decisions for defined contribution pension schemes. This is because consumers may choose to invest in schemes that fit better with their ethical views on investment choices, even if such schemes have lower expected returns or higher risks than other pension schemes.

As the Law Commission[159] notes, by offering ethical pensions as a choice, defined contribution schemes may produce a lower return on investments without compromising the fund managers' fiduciary responsibility 'providing that each member has given information consent'. An individual can thereby make personal choices about their pension without affecting other colleagues' pensions. The importance of such consumer choice can be seen in the success of 'green' and 'ethical' pension funds (see Figure 20).

One major exception to the rule that defined benefit pension schemes are potentially less likely to be interested in ethically-motivated investment decisions is the case of local authority pension

[155] Social Finance Limited (2012).
[156] National Association of Pension Funds (2013).
[157] Money Advice Service (2013).
[158] Op. cit.
[159] Law Commission (2013a, 2013b).

funds, as discussed above. Whilst many LAPFs are defined benefit pension schemes, fund managers may be motivated to make social investments for reasons other than consumer choice.

Currently, the majority of pension fund assets under management are held in defined benefit pension schemes, with only 26% held in defined contribution schemes[160]. For each of the three largest UK pension funds – BT Group Plc., Universities Superannuation Scheme Ltd and Royal Mail Group – the vast majority of their assets under management are in defined benefit schemes[161]. However, recent changes in the pensions sector, including the introduction of auto-enrolment and the closure of many defined benefit schemes[162], are expected to lead to rapid growth of defined contribution schemes. Spence Johnson[163] project that defined contribution pension scheme assets with triple over the next 10 years.

10.3. Characteristics of investment approach

Whilst investment approaches differ across pension funds, typically the LAPFs and other pension funds interviewed for the research have an investment board or committee which is responsible for determining the overall investment strategy, including asset allocation. For the LAPFs, local councillors sit on the investment committee.

Pension funds differ over whether they manage specific investments in-house or through external investment managers, or a combination of the two. For example, some funds use external investment managers only in areas where they feel their internal investment team are lacking in expertise; while others use external investments to manage all of their assets.

10.3.1. Socially responsible investment and ‘green’ and ‘ethical’ pension funds

The relatively recent focus on socially responsible investment (SRI) in the pension sector, and the development of ‘green’ and ‘ethical’ pension funds, demonstrate the importance of social and ethical considerations in shaping pension funds’ investment approach.

Socially responsible investment has become an important issue for many pension funds, with many funds developing their own responsible investment policies in recent years[164]. Such policies typically focus on environmental, social and governance (ESG) issues. A survey of 20 of the largest UK occupational pension schemes found that all stated some form of commitment to ESG issues, (though only six had signed up to the United Nations Principles for Responsible Investment)[165].

Several pension funds have also developed specific green and ethical pension schemes to cater to investors’ concerns over how their funds are invested without compromising the fund managers’ fiduciary responsibility[166]. Many such funds are based on ‘negative’ investment criteria, such as a commitment not to invest in weapons or tobacco manufacturers or traders. However, several others, for example the Standard Life Ethical Pension Fund and the Scottish Life Ethical Pension

[160] Towers Watson (2013).
[161] At least the vast majority of their assets under management, although recent changes may mean they have opened up to new defined contribution schemes.
[162] Towers Watson (2013) predict that all FTSE 100 defined benefit schemes currently open to accrual will be closed in the next decade.
[163] Johnson (2012).
[164] FairPensions (2009).
[165] Op. cit.
[166] Law Commission (2013).

Fund, also include 'positive' investment criteria, such as commitments to prioritise investment in green energy firms[167].

Whilst this research revealed no fund in the UK currently has a commitment to social investment, the developments outlined suggest a potential future role for such funds, if they can be used to appeal to a niche set of investors. The experience of TIAA-CREF pension fund in the USA for example, demonstrates this possibility. A survey of TIAA-CREF members identified a high level of interest in the social and environmental impacts of investments. In response TIAA-CREF developed a Proactive Social Investing Framework that seeks to make impact investments with 'clearly defined social and environmental benefits' across four themes: affordable housing, community and economic development, renewable energy and climate change, and natural resources[168].

10.4. Social investment history

UK pension funds' current activities in social investment are limited. The only examples uncovered from this research of UK pension funds directly addressing social investment, is the commitment of five LAPFs to invest up to £50m each in the Investing4Growth initiative (see Figure 20); investments in Bridges Ventures Funds, and a handful of investments in sectors such as social housing documented by Social Finance Limited[169]. There are also some further examples internationally, such as TIAA-CREF (discussed in section 10.3).

10.4.1. Examples of social investment

The Investing4Growth initiative targets investments that have a 'positive economic, social and environmental impact', and is a potential first mover in pension funds' involvement in social investment.

However, the scheme also highlights some of the difficulties associated with pension funds' involvement in social investment. Many of the proposals for social investments fall below the scheme's minimum investment size of £25m[170]. In conversations with pension funds involved in the scheme, investment officers highlighted that they feel the investment opportunities with the greatest social impact are most likely to fall below this threshold. Many of the opportunities for larger investments come from green energy and infrastructure projects, the benefits of which are of less interest to LAPFs, and some are investments they may have considered in any case, outside of the Investing4Growth initiative.

To address this issue of investment size, which raises associated issues around relatively high due diligence costs, the pension funds involved in Investing4Growth have begun sharing due diligence and supervision costs. Currently, the pension funds involved in the initiative are also considering the creation of a larger portfolio comprised of smaller social investments[171]. These options could potentially allow them to lower the minimum investment size and make these investments. However, such developments require significant coordination between pension funds.

There is evidence that LAPFs are also engaging in social investments outside of the Investing4Growth initiative. Social Finance Limited[172] surveyed 47 pension funds (just under two thirds of which were LAPFs) on their current and future activities in impact investing. Impact investments are those that

---

[167] EIRIS (2008).
[168] Social Finance Limited (2012).
[169] Op. cit.
[170] PIRC (2013).
[171] Op. cit.
[172] Social Finance Limited (2012).

'generate a measurable, beneficial social and environmental impact alongside a financial return'[173], and therefore include social investments. The report found that three UK pension funds currently had investments in social housing, 10 in green energy, whilst 11 had made 'other' impact investments. Several other pension funds also stated that they expected to make impact investments in the coming years.

One case where non-LAPFs have made social investments the USS Pension Fund's investment in the Bridges Social Ventures Fund which, alongside financial returns, aims to 'deliver social returns both on a geographical and sector-specific basis'[174]. In this case, USS's main motivation for the investment was the financial return offered rather than the social returns. This case demonstrates that if social investment opportunities can offer investment profiles that rival those of non-social investments, pension funds are likely to be more willing to invest than otherwise.

Figure 20: Investing4Growth Initiative[175]

In May 2013 five of the largest LAPFs (Greater Manchester, West Yorkshire, West Midlands, South Yorkshire and Merseyside Pension Funds) announced they would be investing up to £50m each in investments that would 'have a positive economic, social and environmental impact in the UK... whilst meeting their investment return and risk strategies'. In addition, they stated a 'preference for the investment impact to include deprived geographical communities and areas with challenging economic and social issues'.

As of October 2013, 31 submissions for proposed investments had been submitted to the pension funds by asset managers, including green energy, infrastructure, venture capital and social enterprise investments. Whilst the final allocation of investment has not yet been confirmed, the process so far highlights the following issues regarding local authority pension funds' involvement in social investment:

- The majority of submissions for larger investments were for green energy or other infrastructure investments: seven out of the 10 proposals for investments over £100m were for energy investments, whilst of the five submissions requesting between £50m and £100m all were infrastructure-related.
- Submissions for investments with a 'greater focus on higher impact on local communities' (those that most closely conform to conventional understandings of social investment) tended to be small and consequently many fall below the minimum investment threshold of £25m. The investment threshold has been set at this level because of 'due diligence and on-going supervision costs being disproportionately high relative to the scale of the investment'.
- Because many of the smaller investments were those most closely related to impacts on local communities, some funds are considering the possibility of 'creating a portfolio of a number of individual investments and sharing due diligence and supervision costs between pension funds'. As of October 2013, the sponsoring funds had agreed to undertake a more detailed review of seven specific opportunities to assess whether a portfolio could be created that allows and institutional return 'at or above the specification level' alongside an acceptable investment and due diligence process.

[173] Global Impact Investing Network (2014).
[174] Bridges Ventures (2008).
[175] Investing4Growth (2013), PIRC (2013).

10.5. Motivating factors

10.5.1. Investment performance

Research suggests that a primary motivating factor for pension funds' investment in any asset is its investment performance: the expected return and the level of risk involved. In a study of local authority pension funds, the Smith Institute[176] found that 'maximising returns remains paramount for all funds' and that whilst 'funds stated that they would be interested in developing impact investment in the future' this is provided that the 'rate of return and the right risk profile could be achieved'.

This is reflected by the pension fund investment officers interviewed for this research - the majority stated that their primary concern in making investments is the expected return and associated risk. Several fund managers also stated that, since their funds have a long term focus, they could cope with some volatility, and therefore the short-term stability of investment returns are a lesser concern. The primary importance to pension funds of investment performance suggests that for social investment to play an important role, it must be as strong financial performance investments such as in the Investing4Growth initiatives and the Bridges Social Venture Fund.

Since social investments may be viewed by pension funds as relatively risky, they may have to offer significantly higher than risk-free returns to attract investment from pension funds. Social Finance Limited[177] in their survey of pension funds found that the average pension fund would expect a minimum net annualised return of 200bps above a risk-free return from a developed-market bond or equity investment in an impact investment.

10.5.2. Diversification

Another important motivating factor behind pension funds' investment decisions is the diversity of the investment portfolio. Investment managers highlighted diversification and the consideration of how an asset fits with the rest of their portfolio, as important considerations for any investment decision.

Some fund investment officers highlighted that, since the factors determining risk for social investments could be quite different to those determining risk for traditional equity investments, social investments could be an appropriate tool for diversifying a portfolio. One investor highlighted that, for example, traditional instruments may have risks associated with inflation rates, whereas a social impact bond's risks could be dependent purely on social outcomes, such as reoffending rates. In practice, however, due to difficulties around a proven track record about social investments' performance, it may be difficult for pension fund investment managers to know in advance whether social investments will in fact provide such diversification benefits.

10.5.3. Focus on local communities

Local authority pension funds have direct links to localities since local councillors sit on their investment committees and their customers are drawn from the local area. LAPFs may therefore have some reason to give priority to investments that have social benefits as well as financial returns, particularly if these social benefits are felt in the local area.

> *"If it's happening locally, it's an incentive."*
>
> *"The purpose of local councils is to improve the social and economic well-being of their environments."*
>
> *– LAPF investment officers*

[176] The Smith Institute (2012).
[177] Social Finance Limited (2012).

> *"We would give [a social investment] higher priority. We are sceptical that we can ever perfectly compare two investments, but we would view positively that added [social] benefit." - Pension fund investment officer*

LAPFs' focus on local communities is an important consideration as to whether they should be classed as 'all being equal' or 'benefit of the doubt' investor types (see chapter 2). Whilst the majority of fund investment officers interviewed stated that they would not prioritise a social investment opportunity over another investment opportunity with the same expected return and associated risk, some stated that social impact would be an important consideration. Clearly then there is variation in the extent to which social impact is prioritised in pension funds' investment decisions, across the group.

10.5.4. Customers' ethical concerns

The importance of customers' ethical concerns in driving the establishment of ethical and green pension funds has been discussed (see section 10.3). It is possible that in the same way, pension funds could develop schemes with positive social investment criteria to appeal to a specific niche of investors, as has been done by TIAA-CIAA in the US. Such schemes would have the benefit of allowing investors to accept lower expected returns, thereby allowing pension fund managers to make social investments which also meet fiduciary obligations to meet clients' interests.

However, from the interviews conducted with investment officers, there was no evidence that there is likely to be a development of social investment-focussed ethical pension schemes soon. One pension fund investment officer described ethical pension funds as an area of little innovation. They stated that defined contribution pension funds feel obliged to offer these types of funds so as not to be left behind by other pension funds, rather than to actively reach out to new potential customers. The design of ethical pension funds is therefore generally based on matching what other funds offer.

10.6. Barriers to investment

10.6.1. Fiduciary obligation

The fiduciary obligation of pension fund managers requires them to act 'in the manner which he/she considers to be in the best interest of the client, regardless of personal beliefs or preferences'[178]. This fiduciary obligation will therefore need to be considered by pension funds when considering whether or not to make social investments. For the most part, this is taken to mean that a pension fund cannot choose to invest for ethically-driven reasons if doing so sacrifices the optimal risk-return profile for the fund. However, that is not to say that social investments are counter to this fiduciary obligation, particularly in cases where clients have expressed an interest in social impact, just that financial performance is also a key consideration.

The Social Finance Limited[179] survey found that 'the biggest barrier to impact investing is the discomfort that many investment managers feel in light of their fiduciary duty. Many believe that they must maximise returns for their members.' Meanwhile, the Smith Institute[180] found that fiduciary responsibility was the main barrier to extensive impact investments among LAPFs, since 'The question of social return cannot intrude on return or on fiduciary responsibilities... no funds said they would be prepared to accept lower returns in exchange for achieving social benefit.'

[178] ClearlySo (2011).
[179] Social Finance Limited (2012).
[180] The Smith Institute (2012).

The interviews conducted for this research suggested that, due to their interpretation of this fiduciary duty as an obligation to maximise investment returns, many fund managers feel that it is not their role to undertake social investments. They feel that social investments are something that they should consider on their financial merits, but not something that they should prioritise.

> *"[Social investment] is not our role; the fiduciary duty we have is to ensure a return on our investment "– LAPF investment officer*

However, this view was not uniform across the pension fund group. Some investment officers did not view their fiduciary obligation as an obstacle to social investment. One investment manager viewed fiduciary obligation as a challenge, in that social investments must meet certain criteria to be considered, but this still leaves considerable scope for making social investments.

Perceived uncertainty around the precise implications of fiduciary obligation for investment decisions can therefore be identified as a barrier to pension funds' engagement with social investments. This is supported by the Law Commission (2013a) which recently stated that 'great uncertainty remains as to the extent to which fiduciaries can take into account social, ethical and environmental factors'. However, as stated above, this uncertainty is not to say that social investment is incompatible in light of pension funds' fiduciary obligations. This is supported by previous research – for example by ClearlySo[181]which argued that the fiduciary obligation requires investors only to 'generate at least market-level returns' rather than maximise profits and 'this may allow room for a wider consideration of the environmental and social consequences of an investment'.

10.6.2. Lack of knowledge of social investment products

One cited reason for the lack of social investments from the pension fund sector is a lack of knowledge of investment opportunities and of how to analyse the investment profile of social investments, as raised by other investor groups examined here. Indeed, Social Finance Limited[182] found that 40% of pension fund managers surveyed had not heard of any form of impact investment, and 50% of those, did not know how to evaluate the associated risk and return. The Smith Institute[183] found that 'impact investments were perceived to be more resource-intensive, in terms of management and the knowledge requirement of trustees, than conventional investment practices' and that funds believed that 'this area was largely untested, requiring more information on the historic levels of risks and rates of return to be generated'.

> *"There is a lack of awareness about anything that might be available in social investment. We have the resources but we don't know much about the sector." – LAPF investment officer*

The Smith Institute[184] report goes on to argue that investment consultants could play an important role in increasing knowledge of social investment opportunities for LAPFs: 'It was widely considered that the development of alternative investments, including those for wider economic benefit, would require external consultancies to 'push' on these types of issues (such as social impact investments) if they were to have future traction'.

---

[181] ClearlySo (2011).
[182] Social Finance Limited (2012).
[183] The Smith Institute (2011).
[184] Op. Cit.

10.6.3. Minimum investment size

A final barrier to social investment identified in this research, is pension funds' minimum investment sizes, which are set to minimise costs of due diligence and supervision costs. During the interviews with pension fund investment officers, many stressed that a key barrier to making smaller investments, which social investments typically are, is the cost of due diligence. Whilst minimum investment sizes vary across pension funds, many investment officers stated that it would be very difficult for them to make investments smaller than around £5m. In many cases the ideal was to find investment opportunities of £50m+ where the investment did not represent more than 10% of a fund, excluding all sub-£500m funds.

For the Investing4Growth initiative, the pension funds set the minimum investment size at £25m, yet many of the social investments proposed fell below this threshold. Surveys have also found that other pension funds are likely to require significant minimum investing sizes for social investments. Social Finance Limited[185] found that just six out of 32 funds that quoted a minimum investment size were prepared to consider investments under £10m, whilst another 13 had a minimum investment size of between £10m and £20m. Below such investment sizes, pension fund managers view the costs of due diligence and supervision as prohibitively high. The problem may be made more acute by pension funds having little knowledge about social investments. Therefore, it may be the case that if pension funds begin to make more social investments, their due diligence and supervision costs would fall, allowing them to accept lower minimum investment sizes.

10.7. Opportunities to engage

10.7.1. Key personality types

As demonstrated by the experience of the Investing4Growth initiative, there are already first movers in the pension fund sector who have adopted an 'Allocation but not integration' approach – carving out an allocation for social investment that will not compromise overall portfolio return requirements, but enables the institution to actively search for social investment opportunities. Other local authority pension funds could potentially also be engaged to experiment with such an approach.

The majority of pension funds beyond this group are 'Benefit of the doubt' or 'All being equal, but…' personality types. They are willing to consider social investments, but also interpret their fiduciary duty as such that they generally steer clear of investments that they feel do not offer competing returns to their mainstream investments.

10.7.2. Where will they contribute?

Given their size and liability requirements, pension funds are most likely to contribute towards the next £5bn in established social investments. These will likely be in sectors that can absorb large sums of capital, such as infrastructure funds or energy projects.

10.7.3. How can they be engaged?

Local authority pension funds are likely to be the most engaged pension funds in social investment in the short-term due to their focus on local community welfare. The Investing4Growth initiative appears to have been successful in enabling LAPFs to make social investments and suggests the potential for further similar initiatives to extend LAPFs' social investment activities.

---

[185] Social Finance Limited (2012).

The Investing4Growth initiative also demonstrates some important lessons for LAPFs' future engagement with social investment. Firstly, for social investments to meet the minimum investment size required by pension funds, there may be a need to form pooled funds of social investments, or further develop mechanisms for sharing the costs of due diligence and supervision across pension funds.

Secondly, the Investing4Growth initiative demonstrates the need for platforms to help pension funds find appropriate social investment opportunities. Some of the pension funds outside of the Investing4Growth initiative that were interviewed, feel they would potentially be interested in social investment opportunities but have not been approached with these. Similarly, among the LAPFs involved in the Investing4Growth initiative one of the most positive aspects of the experience was that, through jointly soliciting requests for proposals, it exposed the LAPFs to investment opportunities they had not previously heard about. A lack of knowledge of the social investment market and available investment opportunities is therefore a key issue that needs to be addressed for this investor group.

There are other important developments necessary to overcome the knowledge barriers that exist to LAPFs matching their investable funds to social investment opportunities. There are already some developments in this space. For example, the Pension and Investment Research Consultants (PIRC) have organised a seminar with precisely the aim of linking pension funds with impact investment opportunities from 'established institutional asset managers and managers new to working with pension funds'[186]. Pension funds interviewed also expressed that they find events and meetings useful ways of learning about new investment opportunities.

In the long-run, to attract larger pension funds other than LAPFs into the market, the financial performance aspect of social investments also needs to be highlighted. A key part of this is providing documentation up to commercial standards so that investment managers can analyse social investments as they would any other financial investment.

[186] PIRC (2014).

11. Conclusion and Recommendations

11.1. Potential new sources of supply

This research has highlighted that segments within each of the eight institutional investor groups examined, present potentially lucrative sources of capital for the UK social investment market. There are common barriers both within and across groups. However, one significant insight from this research is that, as well as asking 'which group next' in the search for new sources of supply, there is also a need to ask 'which personalities are where' in looking at how to engage new investors likely to come in at either/both the £500m in risk finance and £5bn in established investments, ends of the social investment market.

11.1.1. Where will the next £500m of risk social finance come from?

As indicated by the analysis presented in preceding chapters, the largest concentration of 'Go the extra mile' investors at present are to be found among a subset of **family offices** and **housing associations** who both believe strongly in social investment and are able to consider integrating it within their approaches to investing and enacting service delivery. Additionally, there are a number of investor groups with active philanthropy portfolios – **charitable foundations, corporations** and family offices – who have set aside portfolios intended to be 100% impact/0% return which can potentially be shifted into social investments. It is these investor groups which will most likely prove to be the most fruitful sources for raising the next £500m of risk finance for social sector organisations.

11.1.2. Where will the next £5bn of 'established' social investment come from?

Looking at where larger sums of money otherwise intended for mainstream investments could be raised, there are a few pioneering 'Allocation but not integration' personality types among **charitable foundations,** as well as **local authority pension funds**. These are the investors who are willing to try social investment with a portion of their investment portfolios which is sufficiently small to pose little risk to overall returns – enabling them to meet their fiduciary duties – but which enables them to get started in the sector. While a £50m allocation for social housing may seem relatively insignificant to a £10bn+ pension fund, such allocations could add up quickly to make a transformative difference to the amount of capital available for opportunities to invest in the more established end of the social investment market spectrum.

Similarly, many **family offices** have a history of specialising in investing in alternative and real asset classes. Particularly for large family offices, the larger deal sizes which can be found in more establishes sectors such as social housing or green energy may be more suitable to their investment strategies than opportunities at the higher risk end of the market.

11.1.3. Who else could be engaged?

While not all investor groups have obvious early adopters within them, there are 'Benefit of the doubt' investors present within each of the groups explored in this research. Therefore there is a large pool of potential capital available from those who would be happy to prioritise social investments over traditional investments, but simply don't yet have the information or choices they need to ensure they could meet their financial requirements in doing so.

Capturing and sharing the experiences of early adopters, as well as those who are making social investments outside of the marketed 'social finance' funds, will be essential to building the evidence base needed to shift larger numbers of 'Benefit of the doubt' and 'All being equal but…' personalities into a position where they feel confident making social investments.

11.2. Recommendations

A set of practical recommendations have been developed, based on the research findings for the eight investor groups and accompanying analysis of the key barriers they identify to engaging with social investment. These recommendations are framed around increasing uptake of social investment at both ends of the social investment market (£500m in risk finance, £5bn in established investments) as well as the market as a whole (see Table 12 for an overview). The recommendations take into consideration:

- The appetite for social investments identified by institutional investors;
- The challenges and barriers to engaging with social investment, perceived by investors;
- Potential opportunities for social investment in the future; and
- Practical considerations around how to take advantage of these opportunities, at either 'end' of the social investment market.

Table 12: Overview of recommendations

<table>
<tr><th colspan="2">Recommendations to raise the next £500m in risk finance social investments</th></tr>
<tr><td colspan="2">1. Further clarity on how to encourage charitable foundations to make social investments from their endowments, in line with trustees' fiduciary obligations[187]</td></tr>
<tr><td colspan="2">• Exchange best practice through case studies amongst foundations on how to use their finance to help provide the risk capital needed by social sector organisations.
• Encourage foundations to create and support the development of social investment opportunities in the future.
• Draw on the experience of foundations in creating social impact in understanding how social returns are generated and measured.</td></tr>
<tr><td>Barrier addressed: Lack of clarity around definitions of social investment, and the need to unpack what is meant by the social investment market[188].</td><td>Target institutions:
• Charities;
• Faith-based orgs;
• Universities.</td></tr>
</table>

[187] Also of note here is the Law Commission's consultation into charity law and social investment, published on 24th April. See: http://lawcommission.justice.gov.uk/consultations/charity-law.htm

[188] This barrier is consistent with other research undertaken on behalf of the Charity Commission between July 2012 and March 2013, into the regulatory risks, challenges and opportunities which charities face in regards to social investment. One of the research findings was a lack of clarity among some charities of the application of charity law when making social investment decisions. See: http://www.charitycommission.gov.uk/news/charities-and-social-investment-190313/

<table>
<tr><th colspan="2">Recommendations to raise the next £5bn in established social investments</th></tr>
<tr><td colspan="2">2. Improve awareness and understanding of the more mainstream and ‘commonplace’ elements of social investment</td></tr>
<tr><td colspan="2">• Emphasise the more established elements of the social investment market to improve awareness of these investment options among more commercially-driven investors.
• Potential to sub-divide the market into innovative, riskier products and more mainstream options, to help tackle perceptions of risk and unfamiliarity.</td></tr>
<tr><td>Barrier addressed:
• Lack of social investment knowledge and unfamiliarity with the market.
• Lack of clarity around definitions and the need to unpack what is meant by the social investment market.</td><td>Target institutions:
Universal.</td></tr>
<tr><td colspan="2">3. Single place for tracking</td></tr>
<tr><td colspan="2">• Continue to build on existing work, such as Global Impact Investing Network’s (GIIN) ‘Impact Base’ to create a central resource such as a website to showcase the largest funds across a variety of sectors and publish performance data against a benchmark.
• Incorporate ability to browse current deals and top performing funds.</td></tr>
<tr><td>Barrier addressed:
• Lack of social investment knowledge.
• Lack of performance track record.
• Perceptions of risk and uncertainty.</td><td>Target institutions:
Universal.</td></tr>
<tr><td colspan="2">4. Tagging social investments for mainstream financial tools</td></tr>
<tr><td colspan="2">• Create functionality to ‘tag’ social investments within commonly-used financial tools
• Enable users to filter and compare opportunities and fund performance on same platform as all other investments.</td></tr>
<tr><td>Barrier addressed: Lack of performance track record.</td><td>Target institutions:
Universal.</td></tr>
<tr><th colspan="2">Recommendations to raise finance at both ends of the market</th></tr>
<tr><td colspan="2">5. Increase opportunities for sharing experiences for education, peer-to-peer learning and awareness-raising</td></tr>
<tr><td colspan="2">• For example, education and awareness-raising opportunities could be provided through closed roundtable sessions between peers to share experiences, ask questions and raise issues, in confidence.</td></tr>
<tr><td>Barrier addressed: Lack of social investment knowledge and poor awareness of investment opportunities.</td><td>Target institutions:
Universal.</td></tr>
<tr><td colspan="2">6. Need for evidence to capture data</td></tr>
<tr><td colspan="2">• Further research is required to produce evidence to profile, recognise and track deals done outside social investment funds, e.g. by corporations and housing associations, to build evidence base and encourage further movement within sectors; this would help create a multiplier effect by learning and experimentation</td></tr>
<tr><td>Barrier addressed: Lack of social investment knowledge and associated need for better information flow.</td><td>Target institutions:
• Corporations;
• Pension funds;
• Insurers.</td></tr>
<tr><td colspan="2">7. Asset owners mandate fund managers to consider social investment</td></tr>
<tr><td colspan="2">• Asset owners with an interest in social investment opportunities should stipulate to their</td></tr>
</table>

advisors/fund managers, a mandate to seek out and present social investment opportunities to them.	
Barrier addressed: Confusion among asset owners around where responsibility lies for raising social investment opportunities.	**Target institutions:** Universal.

11.2.1. Recommendations to raise the next £500m in risk finance for social sector organisations

Encouraging new investors to commit to opportunities for the next £500m risk investments required in the form of equity, quasi-equity and unsecured lending to social sector organisations, will involve a different approach to raising the next £5bn in established capital. The risk levels and deal sizes involved at the £500m end of the market will be such that this group will be comprised predominantly of investors who have active 'philanthropy' allocations and therefore, for whom financial returns will not necessarily be the main priority (though still a consideration).

Focus thus needs to be placed on finding investors that have the potential to become 'Go the extra mile' or 'Allocation but not integration' personalities, but who are not currently making social investments due to a lack of knowledge, or a perception that they are not able to consider such opportunities. Predominantly, institutions in this latter situation are organisations registered as charities.

Recommendation 1: Further clarity on how to encourage charitable foundations to make social investments from their endowments, in line with trustees' fiduciary obligations.

Target institutional groups: Charities; Faith-based organisations; University endowments.

Top target investor personalities: 'Ask the finance guy'; 'Don't leave me behind'

Charitable organisations, also encompassing some university endowments and faith-based organisations, require further clarity and guidance on the law relating to their use of their endowments for social investment[189].

The law allows for any charity assets to be invested in a mixed purpose social investment, as long as it contributes to the delivery of the charity's purposes for the public benefit. However, where the benefit of the investment sits outside the mission of the endowment, there is less clarity and perceived flexibility for trustees of charitable foundations to invest, if this investment is expected to generate a reduced financial return than a comparable alternative. Therefore whilst many trustees are sympathetic to social investment opportunities, trustees largely perceive their fiduciary duties for the management and preservation of the endowment to override any social benefit that could be generated.

There is clearly a 'sweet spot' offered by investments which offer a comparable financial rate of return to a 'non-social investment' and also generates social benefit. Over time therefore it can be anticipated that, as the social investment market is perceived to deliver comparable returns to mainstream opportunities, a much larger proportion of UK charitable endowments will be invested in the broader public interest through such social investments. There are some examples of charitable foundations making social investments from the endowments on the premise than an

[189] Of note here is the Law Commission's consultation into charity law and social investment, published on 24th April. The Commission recognise there is uncertainty among some charities on the legal framework and have made a number of proposals to address this. See: http://lawcommission.justice.gov.uk/consultations/charity-law.htm

opportunity is expected to meet a certain financial threshold (largely determined by current interest rates and/or market trends) as well as generating identifiable social benefit in any area of interest to the trustees[190].

Arguably the journey to this point will come through building on what is already possible for trustees to engage in social investment. We note in other parts of this report that there is not a natural progression into social investment via socially responsible investment. Other recommendations set out in this report aim to help create this momentum (see below). Clarifying guidance and case studies to help with this information, would be welcomed.

11.2.2. Recommendations to raise the next £5bn in established social investments

To support growth at the more established end of the social investment market (i.e. those social sector industries which have some track record and performance), where larger and/or more conservative institutions are most likely to enter, three recommendations are made, aimed at increasing the accessibility of information on social investments and addressing perceptions of the sector as being 'too high risk' for these more 'conservative' institutional investors.

Recommendation 2: Improve awareness and understanding of the more mainstream and 'commonplace' elements of social investment.

Target institutional groups: Universal.

Target investor personalities: 'Benefit of the doubt'; 'All being equal but…'; 'Ask the finance guy'

> *"It might help to get people started … like having a housing association bonds fund, which is a safer investment than American debt… Right now everything looks very high risk and like something we've never done before. It takes a lot of time to learn about and it's not easy for people to say yes to." - Charitable foundation*

A key research finding is that there is a lack of knowledge of the market among the institutional investor groups, which links to a sense of unfamiliarity with social investments and confusion around exactly what the concept means, and what does and doesn't count.

For investors who are more commercially-minded and prioritise financial returns, the prominence of a discourse around more innovative models and high impact social investments therefore presents somewhat of a barrier to engagement. To these more traditional investors, innovation reads across as 'risk', and consideration of social return reads as 'below market returns' (whether true or not, this is the perception among such investors). It is recommended then, that better efforts are made to educate institutional investors, particularly the more commercially-driven, about the range of social investment opportunities available, some of which within the more established social sectors, are more in line with mainstream investment opportunities. There are a number of sectors that do have track records as well as significant capacity for the larger scale investments required by large institutions.

In addition, when communicating about social investment to investors about investment opportunities at the more 'established' end of the market, it would be beneficial to emphasise the

[190] For example, since its inception in 2012, the City of London Corporation through its Social Investment Fund has so far committed over £3m from its £20m allocation for social investment. While they are not directly related to the mission of the original endowment, but they still present a viable social investment opportunity.

market's more conventional elements, such as microfinance and healthcare funds, clean tech, sustainable forestry and affordable housing investments. This would help to engage commercially-driven investors, by relating to what they know and feel familiar with.

One way of doing so might be to sub-categorise social investment opportunities when presenting these to potential investors. For example one sub-category could be for 'Social finance innovation', including less proven or higher risk products such as social impact bonds, this would then be distinct from 'mainstream social investment' products in microfinance, clean tech, sustainable forestry etc. Such clarity on what social investment encompasses and what options are available at the more conservative end of the market will be essential to engaging a large subset of institutions that require stability of returns and significant minimum investment sizes before they can start engaging with the market. Although there is a risk of segmenting an already small and somewhat impenetrable marketplace further, this approach is suggested as a targeted marketing strategy to reach and engage with potential investor pools of capital, as opposed to a comprehensive strategic approach for the social investment marketplace as a whole. The £500m and £5bn opportunities also represent extreme ends at either end of the market, and there will be a range of opportunities between each end.

Recommendation 3: Single place for tracking - top funds and deals.

Target institutional groups: Universal.

Top target investor personalities: 'Allocation but not integration'; 'Ask the finance guy'.

A lack of information and track record for social investments was identified by a number of interviewees as a barrier to engagement, as this also linked to perceptions of risk and uncertainty of performance. Interviewees felt that making sense of where and how to enter the market at present is a time-consuming and convoluted process.

It is therefore recommended that the market develops a single, dedicated place to allow investors and other interested parties to find out about and compare social investment deals. The market needs a publically available, unfiltered analysis of social investment performance for funds of significant size.

The Global Impact Investor Network (GIIN) in 2013 launched 'Impact Base'[191], a global directory of social investment funds and products, which is provided online, is searchable and free of charge to GIIN members. This is a key resource, of which many of the institutional investors interviewed were not aware, suggesting a need for more effective communication and targeting to a wider range of asset holders than might currently be the case.

It is recommended then that building on GIIN's work, a publically available 'plain English' website be developed which shows the largest funds across a variety of social sectors – affordable housing, clean tech, microfinance, etc. – and publishes their individual and cumulative performance against a fair benchmark. The site could also include a feature to showcase the top 10 or top 50 performing funds, and provide information on new deals as well 'innovative social finance' performance (as per Recommendation 2). By building on existing international databases such as Impact Base, a comprehensive track record of performance in social investments can be developed, which in turn will help inform risk analysis for the market.

[191] See: http://www.impactbase.org/

This site would be unique in that at its core, it would offer a straightforward analysis of how the biggest funds are doing with a fair comparison to broader markets. Only through transparency and access to unfiltered information can trust and confidence be built.

Such a development could also serve to increase demand from asset owners for social investment, through giving the public direct links to investment opportunities and the information asset owners need to push asset managers to consider the space more seriously. Indeed, there are people interested in social investment who are currently 'scared off' by not having any information to take to their 'finance guy', whether that be a fellow trustee, investment consultant, or pension manager.

Recommendation 4: Tagging social investments for mainstream financial tools.

Target institutional groups: Universal.

Target investor personalities: 'All being equal but…'; 'Benefit of the doubt'.

Building on Recommendation 3, and in follow up to the findings around a lack of performance and track record data, the third recommendation is for the development of a platform – similar to those provided by Bloomberg, The Financial Times Fund and ETF Screener, or Morningstar – which tracks the performance of global indices, companies and funds across different assets classes and sectors. In addition such a platform would allow the tagging of social investment opportunities, and for users to filter opportunities that contain that tag within the options they are looking at.

Such a development would help to integrate social finance into the mainstream as a marketing strategy, particularly appealing to the more commercially-driven investors, and those likely to provide the next £5bn through established investment opportunities, to the social investment market.

> *"Institutionally there is too much time spent on explaining social return, and not enough time spent on making it look like a mainstream bond. Because of what it does, a lot of time is spent on explaining the social impact…at the moment, people assume it's risky and different, that it takes time to understand. All these products just need to look like another financial vehicle. When it becomes mainstream it will get invested in because a lot of funds just invest in everything."- Insurer*

Some initiatives, such as the Social Stock Exchange, have already made valuable efforts to group together investment opportunities in listed companies which are also social businesses. The findings from this research highlight however that such tools are primarily of benefit to investors who are already 'Go the extra mile' or 'Allocation but not integration' personalities, and as such are willing to proactively search for social investment opportunities. A platform of the type identified here would help to pique the interest of the many more investors who are 'Benefit of the doubt' or 'All being equal but…' personalities – those willing to consider a social investment over a conventional one if it offers equivalent risk-adjusted returns, but not necessarily committed to actively seeking out such opportunities. Mainstream integration which brings opportunities more directly to these investors through the tools they are already using to search for investment opportunities, is arguably an effective and as yet 'untapped' potential way reach these investor personalities. It would also help to overcome the perception of insufficient track records and available opportunities that are currently holding these investors back.

11.2.3. Steps to raise finance for both ends of the marketplace

The following recommendations have been made as they have the potential to help increase the uptake of social investment at both the £500m risk capital and £5bn established ends of the market, and as such would be targeted at investors likely to come in at either level.

Recommendation 5: Increase opportunities for sharing experiences for education, peer-to-peer learning and awareness-raising.

Target investor groups: Universal.

Target investor personalities: 'All being equal but…'; 'Benefit of the doubt'; 'Ask the finance guy'.

A key research finding was that institutional investors are often influenced and encouraged by the activities of their marketplace peers. Nearly every investor interviewed expressed interest in hearing from peers in their sector who are experimenting with or committing to social investment. If investors are modest social investment sceptics – the 'Benefit of the doubt' or 'All being equal but…' personality types – they want more evidence than they have, and are most interested in hearing from other organisations in their sector. Similarly, if they are 'Ask the finance guy' types who feel unclear on whether social investment is appropriate for their portfolio, hearing from organisations in their own sector who have considered the same questions and faced similar challenges, will be most effective in encouraging them to engage with social investment.

> *"Closed meetings are most interesting – I prefer round tables. The education part is important. Often the social investment industry assumes people know everything." - Corporate foundation director*
>
> *"Meetings with other institutions in my sector – I would love this." - University endowment trustee*
>
> *"Getting the right knowledge at the right time is important. It's about getting up the learning curve and meeting those who know what they're doing, and aren't over-motivated to sell." – Family office*

To this effect, there is demand among institutional investors for greater 'share and learn' opportunities among peers, in a confidential setting, such as closed roundtables. Small group settings with 10-15 participants in which they can ask questions with no sales people present appeals to interviewees, and offers an opportunity to engage those personality types who are on the fence or uncertain, but have the potential to become social investors.

Such educational opportunities can appeal to both those considering entering the market through larger, more established asset classes – such as pension funds wanting to hear from other pension funds that have included social infrastructure projects in their portfolios – as well as those considering riskier, high-impact investments who want to learn from peers who have found ways to create an allocation that allows for this risk-taking and/or had positive experiences with creating impact through investments vis-à-vis philanthropy.

Recommendation 6: Call for evidence to capture data – celebrate, recognise and track.

Target institutional groups: Housing associations, Corporations, Pension funds, Insurers**.**

Target investor personalities: 'All being equal but…'; 'Benefit of the doubt'; 'Don't leave me behind'.

Many interviewees identified the need for a better flow of information on social investment. Partly this is due to a lack of awareness among institutional investors of what information is available - there is more going on than most realise in the social investment marketplace. Partly this is also due to a lack of clarity around what precisely 'social investment' comprises of i.e. what investment deals fall under this label.

For a market in need of proof of concept and track record, it is recommended that investment activity that falls outside the community of organisations actively promoting social finance, is not lost. Some examples of such social investment activity include:

- Housing associations are successfully closing a high volume of social finance deals as part of their service delivery strategies, but these often aren't checked, reported on or profiled in the same way as those that come from dedicated funds exclusively seeking social investment opportunities.
- Banks have some of the largest 'social investment' funds in sectors including microfinance, healthcare, and renewable energy, but these are not explicitly classified as social investments as such because they have developed as a consequence of normal business activities[192].

These types of investment deals are not currently recognised as social investment per se. We would recommend a broader, more inclusive approach to analysing and profiling deals, which accounts for the broad spectrum of investments. This does raise wider issues around the question of intentionality, and how important this is in defining what counts as a social investment. Though this research does not seek to address this issue, it is suggested here that for those organisations that haven't explicitly identified social impact as their first priority when making investments, but nonetheless do generate some degree of social impact through their investments, should be recognised as such. Those investors that don't see themselves as prioritising impact – or, in the case of housing associations, doing anything other than 'business as usual' – but are indeed doing deals and moving money in the social sector, still need to be engaged with so that they can inform the market, alongside other more obvious social investment champions.

Improved marketing and awareness-raising to make available case studies of where social investment is working and to celebrate those that go the furthest in creating impact, through in-house funds or business acquisitions, will help investors in similar sectors to see further opportunities of how social investment could work within their organisation. This demonstration effect and the provision of information direct to trustees, directors or principals could influence and empower asset owners to consider how to do more with their assets for the social sector. .

Recommendation 7: Asset owners mandate fund managers to consider social investment.

Target institutional groups: Universal.

Target investor personalities: 'Ask the finance guy'.

A key finding here, in line with previous research, is that among asset owners there is confusion as to who is responsible for raising social investment opportunities. Asset owners tend to feel that this is the role of their financial advisers, while advisers feel they are bound to respond to their client's needs, as identified by the client.

To help address this challenge, it is recommended that asset owners, who want to know of the opportunities available to make social investments, ensure that their advisors and fund managers bring these to their attention. This needs to be stipulated as part of the contract: this does not bind an investor to any opportunity but it ensures that the advisor is mandated to be informed on these options.

[192] For example, Legal & General's UK Infrastructure Fund has committed £15bn to making in investments in underserved areas of the social economy based on consultation with charities and specialists in health, education, affordable housing and other key areas.

References

Academy4Housing (2013). 'About – Academy4Housing'. Available at http://www.academy4housing.com/about/#.UswSZPRdWaJ [Accessed 07/01/2014]

Accord Group (2013). 'Government-backed social incubator will help hatch enterprises of the future'. Available at http://accordgroup.org.uk/articles/307-Government-backed-social-incubator-will-help-hatch-enterprises-of-the-future [Accessed 07/01/2014]

Affordable Christian Housing (2014). 'London Missional Housing Bond'. Available at http://affordablechristianhousing.org/bond/ [Accessed 08/01/2014]

Baker, L. and Goggin, N. (March 2013). 'Charities and Social Investment: A Research Report for the Charity Commission', Institute of Voluntary Action Research (IVAR). Available at http://www.charitycommission.gov.uk/media/170711/social_investment.pdf [Accessed 09/01/2014]

Balandina, J. (2010). 'Guide to Impact Investing for Family Offices and High Net Worth Individuals'. Available at http://www.guidetoimpactinvesting.net/files/6513/3626/1126/WebsitePdF1.pdf [Accessed 01/02/2014]

Bennett, M. and Zamir I. (2013). 'How socially responsible investing can help bridge the gap between Islamic and conventional financial markets'. The World Bank Treasury. April

Big Society Capital (2013). 'How Housing Associations are Boosting the Growth of the Social Sector'. Available at http://www.bigsocietycapital.com/blog/how-housing-associations-are-boosting-growth-social-sector [Accessed 07/01/2014]

Blond, P. and Noyes J. (2013). 'Holistic Mission: Social action and the Church of England'. ResPublica. July

BMG Research (May 2013). 'Social Enterprise: Market Trends. Based upon the Small Business Survey 2012.'Report for Cabinet Office. Available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/205291/Social_Enterprises_Market_Trends_-_report_v1.pdf [Accessed 09/01/2014]

Bridges Impact (January 2014). 'Shifting the Lens: A De-risking Toolkit for Impact Investment'. Report for Bridges Ventures and Bank of America Merrill Lynch. Available at http://www.bridgesventures.com/news/shifting-lens-new-report-bridges-bank-america-merrill-lynch-de-risking-impact-investments [Accessed 09/01/2014]

Bridges Ventures (2008). 'New Social Entrepreneurs Fund launched by Bridges Ventures'. Available at http://www.bridgesventures.com/news/new-social-entrepreneurs-fund-launched-bridges-ventures [Accessed 10/01/2014]

Bridges Ventures (2013). 'Bridge Ventures closes third Sustainable Growth Fund above target'. Available at http://www.bridgesventures.com/news/bridges-ventures-closes-third-sustainable-growth-fund-above-target [Accessed 09/01/2014]

Brown, A. And Swersky, A. (2012). 'The First Billion – A forecast of social investment demand'. BCG report for Big Society Capital. Available at https://www.bcg.com/documents/file115598.pdf [Accessed 09/01/2014]

Buckland, L. and London Business School (March 2014). 'Social Impact Strategies for Banks: Venture Philanthropy and Social Investment'. Report for European Venture Philanthropy Association (EVPA). Available at http://www.evpa.eu.com/knowledge-centre/publications/evpa-publications/ [Accessed 09/01/2014]

Cambridge University Reporter (2012). 'Reports and Financial Statements for the Year Ended 31 July 2012'. Available at http://www.admin.cam.ac.uk/reporter/2012-13/weekly/6289/section4.shtml#heading2-15 [Accessed 09/01/2014]

Capgemini (2012). 'The Global State of Family Offices'. August

Capgemini and RBC Wealth Management (2013). 'World Wealth Report 2013'. January

CCLA (2013). 'COIF Charities Ethical Investment Fund: Report and Accounts Half Year ended June 2013'.

Charity Commission for England & Wales (2011). 'Charities and Investment Matters: A guide for trustees (CC14)'. October

Charity Commission for England & Wales (2013). 'Sector facts and figures at 30 September 2013', http://www.charitycommission.gov.uk/about-charities/sector-facts-and-figures/ [Accessed 14/01/2014]

Church Commissioners for England (2013). 'Church Commissioners Annual Report 2012'. April

Church in Wales (2013). 'Common Investment Fund Annual Report and Financial Statements: Year ended 31 December 2012'

Church of England (2013). 'Ethical Investment Advisory Group Annual Review 2012/2013'

Church of England Ethical Investment Advisory Group (2013). 'Statement of Ethical Investment Policy'. November 2013.

City of London, Big Lottery Fund & City Bridge Trust (July 2011) 'Investor Perspectives on Social Enterprise Financing'. Available at: http://www.cityoflondon.gov.uk/business/economic-research-and-information/research-publications/Pages/default.aspx [Accessed 06/01/2014]

ClearlySo (2011). 'Investor Perspectives on Social Enterprise Financing'. Report prepared for the City of London Corporation, City Bridge Trust and the Big Lottery Fund by ClearlySo. July

Cohn, C. (2013). 'With plenty of money and time, family offices eye risky markets.' Reuters, 4 October

Corpus Christi College Cambridge (2013). 'Ethical Investment Policy'. Available at http://www.corpus.cam.ac.uk/wp-content/uploads/old/policy-investment-ethical.pdf [Accessed 09/01/2014]

Deloitte (2014). 'Big Demand and high expectations: The Deloitte Millennial Survey'. Deloitte. January

Deutsche Bank (2013). 'Deutsche Bank supports social enterprise'. Available at https://www.db.com/unitedkingdom/content/en/social_investments.html [Accessed 14/01/2014]

EIRIS (2008). 'The EIRIS Green and Ethical Funds Directory'. January

Enterprising Futures (2012). 'Enterprising Futures Corporation Strategy 2012-15'. Available at http://www.pmtraining.org.uk/uploads/PDF%20Uploads/Enterprising%20Futures%20Corporation%20Strategy%20-%20May%202012.pdf [Accessed 07/01/2014]

Esmée Fairbairn Foundation (May 2013). 'Annual Report & Accounts 2012'.

Ernst & Young (August 2013). 'Cleantech industry performance: Global cleantech public pure-play (PPP) company analysis'.

Ethical Money (2012). 'Investing in Social and Affordable Housing'. Available at http://www.madinvesting.com/media/affordable%20housing.pdf [Accessed 06/01/2014]

FairPensions (2009). 'Responsible Pensions? UK Occupational Pension Schemes' Responsible Investment Performance 2009'. April

Family Offices Group (2011). 'The Family Office Report'. Available at http://familyofficesgroup.com/Report.pdf [Accessed 13/02/2014]

Financial Times (2012). 'Social Housing Sector Makes £1.4bn Surplus'. Available at http://www.ft.com/cms/s/0/858c6488-406e-11e2-8f90-00144feabdc0.html#axzz2piqWibZk [Accessed 07/01/2014]

Global Impact Investing Network (2014). 'About Us'. Available at http://www.thegiin.org/cgi-bin/iowa/aboutus/index.html [Accessed 12/03/2014]

Gregory, D., Hill, K., Joy, I., and Keen, S. (July 2012) 'Investment readiness in the UK', for Big Lottery Fund and New Philanthropy Capital. Available at https://www.thinknpc.org/publications/investment-readiness-in-the-uk/ [Accessed 09/01/2014]

Gregory, M. and Masters C. (2012). 'Ernst & Young ITEM Club Special Report: Business Investment'. Ernst & Young. November

HMRC (2014), 'Particular bodies: industrial and provident societies: background'. Available at http://www.hmrc.gov.uk/manuals/ctmanual/ctm40505.htm [Accessed 13/03/2014]

Howells, G., Miller, S., and Fox, T. (November 2012) 'Attracting Early-Stage Social Investment', for UnLtd Big Venture Challenge. Available at http://unltd.org.uk/wp-content/uploads/2013/01/UnLtd_Research_Publication_Number6_bvc_nocrops.pdf [Accessed 06/01/2014]

ICF GHK with BMG Research (2013). 'Growing the Social Investment Market: The Landscape and Economic Impact' for Big Lottery Fund, Big Society Capital ,the City of London and Her Majesty's Government. Available at http://www.cityoflondon.gov.uk/business/economic-research-and-information/research-publications/Pages/Growing-the-social-investment-market.aspx [Accessed 06/01/2014]

IMA (2013). ‘Asset Management in the UK 2012-13’. Available at http://www.investmentfunds.org.uk/research/ima-annual-industry-survey/ [Accessed 12/02/2014]

Inside Housing (2013a). ‘Housing association surpluses soar by 60 per cent to nearly £1 billion’. Available at http://www.insidehousing.co.uk/finance/housing-association-surpluses-soar-by-60-per-cent-to-nearly-%C2%A31-billion/6529611.article [Accessed 06/01/2014]

Inside Housing (2013b). ‘Landlords take private rent plunge’. Available at http://www.insidehousing.co.uk/finance/landlords-take-private-rent-plunge/6526566.article [Accessed 21/01/2014]

Investing4Growth (2013). ‘Requirements’. Available at http://investing4growth.co.uk/requirements [Accessed 06/01/2014]

J.P. Morgan (2012). ‘Impact Investments: An emerging asset class’. November

Jeffery, N. and Jenkins R. (2013). ‘Research Briefing: Charitable trusts and foundations’ engagement in the social investment market’. ACF. November

Johnson S. (2012). ‘Growth in DC assets will be 11.6% pa’. Broad Brush (14). December

King’s College London (2009). ‘Ethical Investment Policy Statement’. Available at http://www.kcl.ac.uk/college/policyzone/assets/files/finance/EthicalInvestmentPolicyStatement.pdf [Accessed 09/01/2014]

Law Commission (2013a). 'Fiduciary Duties of Investment Intermediaries: Initial Questions'. Available at http://lawcommission.justice.gov.uk/docs/fiduciary_duties_short_May2013.pdf [Accessed 28/01/2014]

Law Commission (2013b). 'Fiduciary Duties of Investment Intermediaries'. Consultation Paper No. 215. October. Available t http://lawcommission.justice.gov.uk/docs/cp215_fiduciary_duties.pdf [Accessed 28/01/2014]

Legal and General (2013). ‘Legal and General Makes First Major Care Home and Hospital Investment. December. Available at http://www.legalandgeneralgroup.com/media-centre/press-releases/2013/group-news-release-1208.html [Accessed 22/01/2014]

London Student (2013). ‘UCL ethics board to convene over £14.4m invested in fossil fuels’. Available at http://london-student.net/news/12/09/ucl-ethics-board-convene-14-5-invw/ [Accessed 09/01/2014]

Mair, V. (2012). ‘Oxfam launches its first investment fund’. Available at http://www.civilsociety.co.uk/finance/news/content/11363/oxfam_launches_its_first_investment_fund [Accessed 15/01/2014]

McKenzie, D. (2012). ‘Islamic Finance’. UK Islamic Finance Secretariat. March

Million Homes (2013). ‘What is the future of housing associations?’. Available at http://www.millionhomes.org/news-and-views/by-topic/what-is-the-future-of-housing-associations/935 [Accessed 06/01/2014]

Money Advice Service (2013). 'Defined contribution pension schemes'. Available at https://www.moneyadviceservice.org.uk/en/articles/defined-contribution-pension-schemes [Accessed 12/03/2014]

National Association of Pension Funds (2013). 'Investment Insight: Social Housing'. March 2013. Available at http://www.napf.co.uk/PolicyandResearch/DocumentLibrary/~/media/Policy/Documents/0302-Investment-Insight-Social-Housing%20b.pdf [Accessed 06/01/2014]

National Association of Pension Funds (2013). 'Local Government Pension Scheme 2013: Investing in a changing world'. Available at http://www.napf.co.uk/PolicyandResearch/DocumentLibrary/0309_Local_Government_Pension_Scheme_2013_-_Investing_in_a_changing_world_An_NAPF_report.aspx [Accessed 07/01/2014]

National Housing Federation (2012). 'Building Futures: Neighbourhood Audit: Summary and Key Findings'. Available at http://www.birmingham.ac.uk/Documents/college-social-sciences/social-policy/IASS/research/building-futures.pdf [Accessed 05/01/2014]

Nicklin, S. (2012). 'The Power of Advice in the UK Sustainable and Impact Investment Market'. Bridges Ventures. June

Office for National Statistics (2013), '2011 Census: Detailed Characteristics for Local Authorities in England and Wales Release'. May

Oxford University Gazette (2008). '19 March 2008: University Acts'. Available at http://www.ox.ac.uk/gazette/2007-8/weekly/190308/acts.htm [Accessed 09/01/2014]

Pharoah, C. (2011). 'Charity Market Monitor 2011: Tracking the funding of UK charities'. CaritasData

PIRC (2013). 'Investing4Growth Update'. Available at http://investing4growth.co.uk/files/Investing4growthUpdateReport21October2013.pdf [Accessed 09/01/2014]

PIRC (2014). 'Impact Investing Seminar Programme'. Available at http://pirc.co.uk/news-and-resources2/events-1/impact-investing-seminar-programme [Accessed 21/02/2014]

Queen Mary, University of London (2010). 'Statement of Ethical Investment Policy'. Available at http://www.arcs.qmul.ac.uk/policy_zone/finance/ethical_investment_policy.pdf [Accessed 09/01/2014]

Resonance (2013). 'Real Lettings Property Fund'. Available at http://www.resonance.ltd.uk/funds/real-lettings-property-fund/ [Accessed 07/01/2014]

Rhodes, Chris (2013). 'Business Statistics: Commons Library Standard Note', House of Commons Library, 14 November

Richardson, M. (2012). 'Green Light: Creating Jobs Through Social Enterprise'. A report for the National Housing Federation and the Aspire Foundation

Scottish Life UK (2013). 'Scottish Life UK Ethical Pension Fund'. Available at http://www.scottishlife.co.uk/scotlife/UploadedFiles/5WD0143Ethical_Fund.pdf [Accessed 10/01/2014]

Sherwood, B. (2008). 'London lures family offices of super-rich'. *The Financial Times*. 4 August

Social Enterprise Buzz (2014). 'Zurich confirms interest in impact investing, but has little appetite for risk', Available at http://www.socialenterprisebuzz.com/2014/01/07/zurich-confirms-interest-in-impact-investing-but-has-little-appetite-for-risk/ [11/01/2014]

Social Finance Limited (2012). 'Microfinance, Impact Investing, and Pension Fund Investment Policy Survey'. October

Social Housing (2012). 'UK surpluses break through £2 billion mark as inflation and efficiencies bolster balances'. Available at http://www.socialhousing.co.uk/Special_Reports/UK_surpluses_break_through_2_billion_mark_as_inflation_and_efficiencies_bolster_balances [Accessed 07/01/2014]

St John's College Cambridge (2012). 'Annual Report and Financial Statements for the year ended 30 June 2012'

St John's College Oxford (2010). 'Benefactors' Report Sources and Uses of Funds'. Available at http://www.sjc.ox.ac.uk/3085/benefactorsMT2010.pdf.download [Accessed 09/01/2014]

The Cambridge Student (2013). 'Cambridge's endowment funds make it Britain's richest university'. Available at http://www.tcs.cam.ac.uk/news/0030480-cambridges-endowment-funds-make-it-britains-richest-university.html [Accessed 09/01/2014]

The Guardian (2008). 'Ethical Investment Tips'. Available at http://www.theguardian.com/money/2008/may/21/ethicalmoney.investmentfunds [Accessed 12/03/2014]

The Guardian (2012). 'In Profile: Britain's largest housing associations'. Available at http://www.theguardian.com/housing-network/2012/jun/08/housing-association-profiles [Accessed 07/01/2014]

The Guardian (2013). 'Edinburgh University ends funding for US drone component maker'. Available at http://www.theguardian.com/education/2013/sep/29/edinburgh-university-ends-funding-drone [Accessed 09/01/2014]

The Smith Institute (2012). 'Local Authority Pension Funds: Investing for Growth'. September

The Socially Responsible Investment Review Committee (2010). 'Recommendation to Council on Divestment from Arms Manufacturing Companies'. Available at http://www.admin.ox.ac.uk/media/global/wwwadminoxacuk/localsites/councilsecretariat/documents/srirc/C1032.pdf [Accessed 09/01/2014]

The Telegraph (2013). 'Legal & General in £15bn infrastructure pledge for UK but HS2 will miss out'. Available at http://www.telegraph.co.uk/finance/newsbysector/constructionandproperty/10220975/Legal-and-General-in-15bn-infrastructure-pledge-for-UK-but-HS2-will-miss-out.html [Accessed 26/02/2014]

Third Sector (2012). 'Housing association puts £10m into social investment fund for homeless people'. Available at http://www.thirdsector.co.uk/Social_Enterprise/article/1158381/Housing-association-puts-10m-social-investment-fund-homeless-people/ [Accessed 07/01/2014]

Towers Watson (2013). 'Global Pension Assets Study 2013'. January

Trinity College, Cambridge (2012). 'Annual Report of the Trustees and Accounts for the Year Ended 30 June 2012'. Available at http://www.trin.cam.ac.uk/show.php?dowid=1597 [Accessed 09/01/2014]

UK Trade & Investment (2013). 'UK Excellence in Islamic Finance'. UK Trade & Investment. October

University College London (2012). 'UCL Investment Policy'. Available at http://www.ucl.ac.uk/finance/finance_docs/investment_policy.htm [Accessed 09/01/2014]

University of Edinburgh (2006). ''Socially Responsible Investment' – The Agreed Approach'. Available at http://www.docs.sasg.ed.ac.uk/GaSP/Governance/SociallyResponsibleInvestment.pdf [Accessed 09/01/2014]

University of Edinburgh (2012). 'Reports and Financial Statements 2011-12'. Available at https://www.wiki.ed.ac.uk/download/attachments/68630228/uoe_reports_fin_statements_11-12.pdf [Accessed 09/01/2014]

University of Glasgow (2012). 'Reports and Financial Statements 2011-12'. Available at http://www.gla.ac.uk/media/media_253124_en.pdf [Accessed 09/01/2014]

University of Manchester (2012). 'Financial Statements for the year ended 31 July 2012'. Available at http://documents.manchester.ac.uk/display.aspx?DocID=14943 [Accessed 09/01/2014]

University of Manchester (2013). 'Policy for Socially Responsible Investment'. Available at http://documents.manchester.ac.uk/display.aspx?DocID=659 [Accessed 09/01/2014]

University of Oxford (2012a). '2011/12 Financial Statements'

University of Oxford (2012b). 'Financial Statements of the Oxford Colleges (2011-12)'. Available at http://www.ox.ac.uk/about_the_university/facts_and_figures/college_finances12.html [Accessed 09/01/2014]

World Economic Forum (2013). 'From the Margins to the Mainstream'. A report by the World Economic Forum Investors Industries Prepared in collaboration with Deloitte Touche Tohmatsu

Annex One: Interview schedule

Part A: Knowledge of social investment

[Protection of information statement to be read to interview participants]

The purpose of this research is to better understand UK institutional investors' views on and experience with social investment, with the particular aim of identifying and understanding both the positive factors and the barriers to making social investments among different institutional investor groups. The objective is not to study individual positions, but rather common trends and divergences across a sample of organisations in different investor groups. Your individual response will not be published or shared with any third party, nor will your organisation be identified in the published report.

1. On a scale of 0-5, where 0 represents no knowledge and 5 represents significant knowledge, how much do you feel that you know about social investment? (*Classify response)*

   - ☐ 5 - I have significant knowledge of social investment
   - ☐ 4 - I have substantial knowledge of social investment
   - ☐ 3 - I have moderate knowledge of social investment
   - ☐ 2 – I have some knowledge of social investment
   - ☐ 1- I have very little knowledge of social investment
   - ☐ 0 - I have zero knowledge of social investment
   - ☐ I have zero knowledge/Not interested

2. Thinking about the social investment products you've heard of, do you think the typical investment performance and risk of these products is higher, the same or lower than developed market bonds? If possible, please indicate the difference in percentage terms if you are aware.

   Investment performance: (*Classify response)*

   - ☐ Significantly higher
   - ☐ A little higher
   - ☐ About the same
   - ☐ A little lower
   - ☐ Significantly lower
   - ☐ Don't know

   Risk: (*Classify response)*

   - ☐ Significantly higher
   - ☐ A little higher
   - ☐ About the same

☐ A little lower

☐ Significantly lower

☐ Don't know

Part B: Investment approach

3. What is the approximate size of your investment portfolio at present (total AUM)?

4. If you had to give 3 defining characteristics of your investment approach, what would they be?

5. How are your investment decisions structured? E.g. Do you have an in-house investment team or do you use fund managers?

   Is this the same for setting strategy, including setting financial and non-financial investment objectives and undertaking any monitoring against them?

6. Before we discuss pro-active social investments, it would be useful to understand whether you already apply any screening criteria to your investments, such as negative screening to avoid certain industries, ESG screening, or other socially responsible or sustainability criteria.

   Which of the following best describes your institution's approach to screening investments? (*classify response)*

   ☐ We apply screening to the entirety of our portfolio

   ☐ We apply screening to a portion (__ %) of our portfolio

   ☐ We do not apply any screening criteria to our portfolio

   (If relevant) Could you please briefly describe the approach you apply?

7. Do you consider the overall social and environmental impact of your portfolio? What influence does it have on investment decisions and strategy?

8. We are now going to talk specifically about social investments[193] - what has your institution's involvement been with social investment to date?

9. How would you describe your institution's approach to social investments? For example, do you dedicate a portion of your portfolio to social investments, do you consider them for the entirety of your portfolio but not designate a significant amount that must be invested, etc.? *(Classify response)*

   ☐ We dedicate the entirety of our portfolio to social investments

   ☐ We dedicate a portion (__ %) of our portfolio to social investments

   ☐ We consider social investments for the entirety of our portfolio though do not designate an amount that must be invested in social investments

[193] Offer definition if needed: Social investments are investments that intend to create positive social or environmental benefits in addition to financial return. Examples would be social housing or a clean tech fund. For definition, see J.P. Morgan Global Research, 'Impact Investments: An emerging asset class', November 2010.

- ☐ We consider social investments for a portion (__ %) of our portfolio though do not designate an amount that must be invested in social investments
- ☐ We do not consider social investments for our portfolio
- ☐ Given our investment strategy, it is impossible to consider social investments.

10. *(If not dedicating 100% of portfolio to social investments)* Thinking about your core investments/the portion of your portfolio that is not dedicated to social investment, if you were presented with an investment opportunity that offered the same financial return profile as another investment in the same market but also provided some societal benefit, such as an investment in a clean energy company, how would you consider this opportunity alongside other investment opportunities? For example, would you give it higher priority, treat it the same, or give it lower priority? (*Classify response)*

    - ☐ We would give it higher priority against other investments
    - ☐ We would treat it equally against other investments/no preferential treatment
    - ☐ We would give it lower priority against other investments
    - ☐ We would not consider it for our core investments
    - ☐ We would make specific considerations given that it is a social investment

11. How would you describe your approach to seeking out social investment opportunities? For example, would you want to be brought a social investment option for everything in your portfolio, only shown a social investment product if it offers close to competing returns, only shown a product if it offers better than competing returns, or not at all, etc? *(Classify response)*

    - ☐ Bring me a social investment option for everything
    - ☐ Bring me a social investment option if it offers close to competing returns
    - ☐ Bring me a social investment option if it offers competing returns
    - ☐ Bring me a social investment option if it offers better than competing returns
    - ☐ Do not bring me a social investment option
    - ☐ Our investment strategy does not give us the flexibility to ask for social investment options

12. Would a criterion for choosing advisors be that they know of and can advise on making social investments? *(Classify response)*

    - ☐ Yes
    - ☐ No
    - ☐ Not sure

13. Do you anticipate that your level of investment in social investments will decrease, stay the same or increase in the next 3-5 years? (*Classify response)*

    - ☐ Decrease significantly

☐ Decrease a little

☐ Stay the same/No change

☐ Increase a little

☐ Increase significantly

(If relevant) How much do you imagine it will rise/fall by and what is the reasoning behind this?

14. *(If not already covered in preceding discussion)* Do you consider that it is the role of institutions such as your own to invest in social investments?

    ☐ Yes

    ☐ No

    Why or why not?

15. Compared with your peer organisations (e.g. other LAPFs, other university endowment funds), do you perceive that you do more social investing, about the same amount, or less social investing? (*Classify response)*

    ☐ We do more social investing than our peers

    ☐ We do about the same level of social investing as our peers

    ☐ We do less social investing than our peers

    ☐ Don't know

16. Assuming you could achieve your target return, how much social investment do you think you should be doing as a % of your portfolio?

17. What do you consider to be the main barriers to your ability to make social investments/do more social investment at present and why?

18. To what extent are each of the elements listed below barriers to your ability to make social investments/do more social investment at present? Please rank from being of low significance to highly significant to your organisation. *(Provide table to complete)*

	Low Significance	→		**High Significance**	
Risk levels of individual investments	1	2	3	4	5
Deal size	1	2	3	4	5
Cost of due diligence	1	2	3	4	5
Time horizons of investments	1	2	3	4	5
Return rates of markets invested in	1	2	3	4	5
Risk levels of markets invested in	1	2	3	4	5
Unfamiliarity of sector	1	2	3	4	5
Lack of specialist advice	1	2	3	4	5
Lack of products	1	2	3	4	5
Lack of track record of financial return	1	2	3	4	5
Lack of track record of social return	1	2	3	4	5
Belief that increased social performance will decrease financial performance of portfolio	1	2	3	4	5

Reputations of social investment product providers	1	2	3	4	5
Reputations of organisations receiving investment	1	2	3	4	5
Lack of/Poor tax incentives	1	2	3	4	5
Lack of client demand	1	2	3	4	5
Conflict with fiduciary duty	1	2	3	4	5
Lack of products in defined sectors or regions	1	2	3	4	5
Other:	1	2	3	4	5

19. Leaving aside the external barriers we've been discussing, are there any internal barriers to your institution's ability to make social investments that you can identify at present? Could you please briefly describe these barriers and why you think they arise?

20. Apart from investing capital, are there other ways you feel your institution could be involved in developing the social investment market? For example, by developing products, conducting research, serving as a guarantor, etc.?

Part C: Favoured product characteristics

21. Thinking about the social investment products described below, which would you be most likely to consider and why? (*Provide handout)*

- ☐ **Sustainable Growth Fund:** A 10-year, limited partnership providing growth equity to SMEs in sectors with underlying social or environmental needs. Typical subscription £5m, maximum subscription £10m.

- ☐ **Charity Bond:** A 5-year, ethical savings bond with a capped return selected by the investor. Any additional returns are distributed to a charity of the investor's choosing. Typical subscription £1-2m, maximum subscription £20m.

- ☐ **Healthcare Fund:** A minimum 5-year, limited partnership providing equity or equity-like capital to social enterprises at all stages of development that will help improve access and quality of health care provision, especially for the most disadvantaged. Typical subscription £5m, maximum subscription £12m.

- ☐ **Community Finance Business:** A 5-year, direct equity investment into a Community Development Finance Institution (CDFI) providing affordable financial products and services to financially excluded individuals. Typical subscription £100k, maximum subscription £500k.

- ☐ **Sustainable Forestry Fund:** A 15-year, limited partnership private equity fund focused on sustainable forestry management. Typical subscription £5m, maximum subscription £20m.

- ☐ **Microfinance Fund:** A minimum 5-year fund focused on increasing access to financial products and services for low-income people through providing equity and debt finance to microfinance institutions. Typical subscription £500k, maximum subscription £5m.

22. Looking again at these same products with their return profiles included, would your preferences be the same? Why or why not? (*Provide handout)*

- ☐ **Sustainable Growth Fund:** A 10-year, limited partnership providing growth equity to SMEs in sectors with underlying social or environmental needs. Successful exits to date have ranged from 12-16% IRR. Typical subscription £5m, maximum subscription £10m.

- ☐ **Charity Bond:** A 5-year, ethical savings bond with a capped return selected by the investor (currently up to 10%). Any additional returns are distributed to a charity of the investor's choosing. Typical subscription £1-2m, maximum subscription £20m.
- ☐ **Healthcare Fund:** A minimum 5-year, limited partnership providing equity or equity-like capital to social enterprises at all stages of development that will help improve access and quality of health care provision, especially for the most disadvantaged. Successful exits have ranged from 3-4% IRR. Typical subscription £5m, maximum subscription £12m.
- ☐ **Community Finance Business:** A 5-year, direct equity investment into a Community Development Finance Institution (CDFI) providing affordable financial products and services to financially excluded individuals. Expected to repay capital with return profile of <1%. Typical subscription £100k, maximum subscription £500k.
- ☐ **Sustainable Forestry Fund:** A 15-year, limited partnership private equity fund focused on sustainable forestry management. Expected return profile circa 14-16%. Typical subscription £5m, maximum subscription £20m.
- ☐ **Microfinance Fund:** A minimum 5-year fund focused on increasing access to financial products and services for low-income people through providing equity and debt finance to microfinance institutions. Expected annual return of 6-9%. Typical subscription £500k, maximum subscription £5m.

23. If your institution were to make/is making social investments, would you have any preferred sectors or geographies? If yes, what are the reasons behind this preference? (please rank all that apply with 1 being the most preferred option) (*Provide handout)*

Sectors:

- ☐ Employment, Training and Education
- ☐ Housing and Local Facilities (e.g. social housing)
- ☐ Income and Financial Inclusion
- ☐ Physical Health
- ☐ Mental Health and Well-Being
- ☐ Family, Friends & Relationships (e.g. family support services, social care)
- ☐ Citizenship and the Community (e.g. safe communities, participation in public life)
- ☐ Arts, Heritage, Sport & Faith
- ☐ Conservation of the Natural Environment (e.g. renewable energy)
- ☐ Other:

Geographies:

- ☐ Local (e.g. community/regional)
- ☐ National (e.g. UK-wide)
- ☐ International – Developed markets

- ☐ International – Developing markets
- ☐ Other:

24. What is the minimum level of individual investment size that you consider / would consider for social investing? What would the ideal investment size be?

25. Assuming a social investment product could offer you the following, which would be the most important to you as an investor? (Please pick your top 3) (*Provide handout)*

- ☐ Stability of fund performance (e.g. no negative return months and stable annualised return)
- ☐ Low volatility (annualised volatility <1%)
- ☐ Low total expense ratio (<2%)
- ☐ Liquidity i.e. ability to access funds easily
- ☐ Reporting on social impact via industry framework
- ☐ Clear social need addressed by the investment
- ☐ Strong reputation of product provider/fund manager
- ☐ Covered by Financial Services Compensation Scheme
- ☐ Diversification of asset classes in our portfolio (e.g. adding new asset class, such as microfinance)
- ☐ Diversification of investments in our portfolio (e.g. by sector, geography)
- ☐ Other:

Part D: Information needs

26. Where do you currently find out information on social investment? Are there any sources/meetings that you find particularly useful and why?

27. Is there any specific information you would need to see to from social investments to consider them on an equal footing with your other investments?

28. Which of the following activities would appeal to you as an opportunity to learn about social investment (please rank those that appeal in order): (*Provide handout)*

- ☐ Dinners/breakfasts on social investment with sector experts
- ☐ Articles/media coverage on social investment
- ☐ Meetings with social investment fund managers/SIFIs
- ☐ Visits to social enterprises/social businesses
- ☐ Closed meetings with other investors/institutions in my sector
- ☐ Meetings with other investors who prioritise social investment
- ☐ Other:

29. While we’ve been talking around the topic for the past hour, what we’re really interested to understand from these interviews is why investors like yourself aren’t doing more social investments. Is there anything further you can tell us about why you people like you aren’t doing more social investing at present?

Thank you for your time. As a reminder, all your responses from this discussion will be kept anonymous and we will be sure to share a copy of the report when it is released at the end of March.

Annex Two: Investor profiles

The following pages consist of one page 'profiles' for each of the eight institutional investor groups explored in this research:

- Charitable organisations;
- Corporations;
- Faith-based organisations;
- Family offices;
- Housing associations;
- Insurers;
- Pension funds; and
- University endowments.

These profiles present an overview for each investor group on the following:

- Motivations and influences for social investment;
- Barriers to engaging with social investment;
- Opportunities to engage the investor group;
- Investment history;
- Key sector statistics - including total assets, likelihood of engaging with social investment, and which end of the market they're most likely to engage with.

Charitable organisations

Charities' social investment decisions are influenced largely by internal capacities, alignment with core mission and programmes, and legal considerations. Growth is more likely to come from grant portfolios than investments in the medium-term, however there is opportunity for charities to consider social investment as part of their investment portfolio.

Overview

Several of the largest grant-making foundations in the UK derive a significant portion of their income from managing endowments, a proportion of which in theory could be allocated to social investment.

Within the UK charity sector there are a few social investment pioneers who have made specific allocations out of their investment portfolios. However, most charities' engagement with social investment to date has not been through their investments but rather as an alternative to grant-making. Charities, therefore, often have to maintain a careful balance between social investment and grant-making.

An additional consideration for charity trustees is their fiduciary duty to ensure investments are aligned with core charitable aims and/or produce sufficient investment returns to meet income needs.

Motivating/influencing factors

- **Investment performance** – charities must ensure sufficient income for grant-making and perpetuity of endowment capital; all foundations have defined target returns for investment portfolios .
- **Mission-alignment** – social investment is influenced by the mission of the endowment, if the investment is not likely to offer comparable financial returns.

Barriers to social investment

- **Lack of clarity of legal considerations** – some charities require further guidance as to how social investments can be aligned with legal obligations.
- **Lack of capacity** – endowments are externally managed, trustees are busy people, and staff often lack the resources and specialist information.
- **Opportunity cost** – high demand for grants needs to be balanced alongside social investment opportunities.

Opportunities to engage charitable foundations

- **Further clarity** on how charitable foundations can make social investments from their endowments.
- **Continue to build on the sharing of best practice** among foundations and encourage foundations to create and support the development of social investment opportunities in the future.
- Support **co-learning initiatives** across peers.

Sector statistics

Number:
160,000+ registered charities in England and Wales

Total investable wealth:
£61bn total sector income 2013
Investments of top 500 foundations worth £40bn+

Likelihood to engage with SI:
Medium

Likely to contribute to:
Next £500m risk investments:
- Direct investments into organisations and funds in same areas as programming.

Investment history

- UK charitable foundations have allocated over £100m to social investments since 2003.
- Greatest activity among grant-making foundations with large endowments though also some activity among operational charities.
- Tend to be impact-driven when making social investments in same areas as programming.

Corporations

Social investment has become an increasing focus for UK corporations. While most see it as a CSR activity (largely due to the lack of track record at present), corporations can be partners for helping to further professionalise the social sector and a source of moderate capital growth.

Overview

While the total amount of social investments to date by UK-based corporations has been modest relative to the size of their total assets, many corporations have become important champions of social enterprise and – in some instances – have been important cornerstone investors in social investment funds.

Growing businesses' contribution to the market in the medium term will need to be with a view as to how businesses can support their own engagement goals through supporting social investment, and contribute meaningfully to professionalising the sector.

Motivating/influencing factors

- **Contribution to society** – feeling that it is the role of business to take risks and support development of innovative financial products and sector.
- **Internal and external engagement goals** – demand for skilled volunteering opportunities supporting social enterprise, strong fit with sustainable/responsible business communication goals.
- **Product development** – opportunity to learn about social sector with view to developing proprietary products (financial services industry).
- **Competition** – as more businesses get involved with supporting the market, competitors feel compelled to engage.

Barriers to social investment

- **Lack of track record** – businesses cannot offer products to clients that are unproven; documentation in social investment sector perceived to not be up to professional standards.
- **Reputational risk** – as public-facing companies, reputational concerns about not wanting to attract negative press for failed investments or making profits.
- **Preference for DIY** – some prefer to make own investments rather than invest in third party funds; social investment may already be on balance sheet through investments in green energy, microfinance, etc.

Opportunities to engage corporations

- Create **incubator programme 'package'** for businesses to match themselves with social enterprises to mentor and invest in collective fund.
- **Showcase DIY social investment** already done by businesses through call for evidence, recognise best-in-class initiatives to build track record and inspire peers.
- **Encourage opportunities to invest in the supply chain** offered by social enterprises: this type of investment directly affects the revenue of a social enterprise.

Sector statistics

Number:
1,144 UK businesses with £1bn+ turnover in 2013

Total investable wealth:
£729bn estimated value of cash reserves held by private non-financial companies
£2.6bn total corporate community investment spend

Likelihood to engage with SI:
Medium/High

Likely to contribute to:
Next £500m risk investments
- Direct investments and funds supporting social enterprise.

Investment history

- Social enterprise has become a popular focus area for CSR activity, with a noticeable uptick in the amount of finance and in-kind support committed by UK businesses over past 3-5 years.
- Corporations have been important cornerstone investors in several social investment funds.
- While financial services industry has been most active to date, 2013 saw launch of social enterprise investment funds and incubators by O2/Téléfonica (telecoms) and Centrica (energy).

Faith-based organisations

Faith-based organisations are a largely conservative, risk-averse group of investors with a strong ethical stance. While many have community action goals, any social investment activity is likely to be at the very established end of the sector or via community portfolios.

Overview

As investors, the primary concern of faith-based organisations is to maintain ethical standards in line with clients' or members' belief systems. As such, faith-based organisations have been strong proponents of socially responsible investment practices.

Despite being the most 'ethical' of any investor groups profiled in this report, faith-based organisations are largely conservative and risk-averse in their investment approach, preferring managed funds that meet their income needs, for their long-term sustainability.

Church groups are most likely to engage with social investment as part of their social action portfolio, i.e. charitable works, or via modest exposure through ethical managed funds.

Motivating/influencing factors

- **Stability of fund performance** – investment strategy focused on achieving stable returns and rising income over time.
- **Community impact** – many churches see themselves as being for the benefit of the community, with an interest in addressing local issues.

Barriers to social investment

- **Income requirements** – due to falling income from direct giving, income targets for investment portfolio are relatively inflexible.
- **Investment management structure** – with the exception of Church Commissioners and CofE Pensions Board, most outsource investment management; clergy often ack confidence in managing investments so tend to defer to fund managers to present opportunities, who largely adopt a traditional commercially-driven approach i.e. don't' actively seek social investment opportunities.

Opportunities to engage faith-based organisations

- Expose faith-based capital to the social investment market through including **more established social investment products in managed ethical fund** portfolios.
- **Encourage investment in Church-linked social enterprises** out of community action budgets as easier entry points o test the market.

Sector statistics

Number:
32,000+ faith-based charities in England & Wales

Total investable wealth:
£5.5bn+ Church of England funds

Likelihood to engage with SI:
Low/Medium

Likely to contribute to:
Next £5bn est. investments:
- Listed equities or well-established products (e.g. micro-finance) through managed funds.

Investment history

- Little involvement with social investment, though some exposure to established products through pooled ethical funds.
- On supply side, Church charities launched London Missional Housing Bond in 2013 to finance affordable homes for Christian workers.

Family offices

Family offices are a 'wild card' investor group with highly individualised investment goals. However, their longer time horizons, greater appetite for risk than other investors, and ability to take a 'passion' approach to investing, makes them a lucrative source of potential capital.

Overview

Family offices are private wealth management advisory firms established by ultra-high-net-worth individuals, exclusively to manage a single family's, or a group of families' wealth. While the highly individualistic nature of family offices means that no two share the same investment goals, family offices have been pioneers in making social investments globally as well as in the UK.

Due to their greater appetite for risk-taking, longer time horizons, and ability to take a values-based approach to investing, family offices are one of the better suited investor groups to consider the more innovative, equity-like investments on offer in the UK social investment market .

Motivating/influencing factors

- **Values-based approach to investing** – wealth owners better able to express personal values and interests through family office structure.
- **Appetite for risk** – many family offices founded by successful entrepreneurs and mavericks; sector played key role in pioneering venture capital market.
- **Longer time horizons –** due to goal of preserving wealth across generations.
- **Lower internal barriers** to decision-making due to proximity to wealth owners.
- Preference for investing in **managed funds** due to small staff teams.

Barriers to social investment

- **Reputation of fund managers** - industry built on personal recommendations and relationship-building; social investment fund managers are not well-known at present.
- **Lack of knowledge** – lack of straightforward resources and opportunities to learn about social investment; family offices want to hear from other families who have done it.

Opportunities to engage family offices

- Hold **closed knowledge-sharing events** with family offices who have made social investments to facilitate co-learning.
- Focus on **building the profile of fund managers and advisers** – spend time networking and relationship-building in family office circles.

Sector statistics

Number:
400+ Family Offices active in UK
c. 100 Multi Family Offices
300+ Single Family Offices

Total investable wealth:
Unknown

Likelihood to engage with SI:
Medium/High

Likely to contribute to:
Next £500m risk investments:
- Managed funds.

Next £5bn est. investments:
- Opportunities in alternatives, real asset classes.

Investment history

- Pioneer group in making social investments globally, including several incidences of 100% impact portfolios.
- Growing interest in social investment among UK family offices though modest activity to date.
- Investments to date have primarily been in managed funds, though also some direct investments into social enterprises.

Housing associations

Housing associations have a strong commitment to the welfare of their residents. They have traditionally invested mainly in community programmes, in line with their business activities and community priorities, but increasing surpluses provide opportunities to broaden into social investment.

Overview

Housing associations are not-for-profit institutions that provide social housing. Their interest in social objectives, such as reducing unemployment and improving community welfare, makes them potentially fruitful sources of capital for the social investment market.

Historically, housing associations have been more likely to invest surpluses in house building and in community projects. However, recent increases in operating surpluses demonstrate the potential for the largest housing associations to devote substantial resources to social investment, as L&Q housing association have done.

Motivating/influencing factors

- **Concern for social outcomes** – housing associations are particularly concerned with the welfare of their tenants and local communities, in particular social goals such as increasing employment and reducing financial inclusion.
- **Increasing operating surpluses** – the largest housing associations are seeking new opportunities to finance broader activities, including social investment.

Barriers to social investment

- **Size of available capital pools** – Housing associations are typically net borrowers rather than creditors; with changes to public funding, surpluses available for social investment is uncertain.
- **Clarity on role** – Housing associations are themselves social enterprises and could potentially be recipients as well as providers of capital; increasing social investment could require mission shift and/or clarification on housing associations' relationship with the social sector.
- **Influence of regulators** – Some housing associations feel that regulators would prefer them to focus their activities narrowly on social housing rather than engage more broadly, though this isn't a widely-held or especially pressing concern.

Opportunities to engage housing associations

- Develop **case studies** of social investment activity, hold **workshops** and **knowledge-sharing events** to learn from other housing associations' experiences with social investment and discover new opportunities.
- Create a **platform on industry websites** profiling available social investment opportunities.
- Ensure that social investment opportunities **match the mission and priorities** of housing associations.

Sector statistics

Number:
1,700 in UK, providing 2.5m homes

Total assets:
£118 bn+ (mostly tied up in social housing stock)
£2bn+ in operating surpluses

Likelihood to engage with SI:
Medium/High

Likely to contribute to:
Next £500m risk investments:

- Direct investments into local social enterprises/funds supporting community agendas or service delivery.

Investment history

- L&Q housing association invested £10m in the Real Lettings Property Fund.
- Strong history of community investment – housing associations invested £746.5m in communities in 2010/11.
- Wide-ranging support for social enterprises, either through procuring from them, by setting them up or by acquiring them.

Insurers

Insurers manage very large funds and subsequently have a preference for making large investments in fixed income assets. To make social investment attractive to them, there needs to be appropriate asset types with a proven track record on offer.

Overview

Insurance companies are the second largest institutional investor group in the UK, and form a significant source of funds that is currently relatively untapped for social investment.

Insurers are primarily concerned with maximising investment returns. However, they are also concerned with matching their investment horizon to their liabilities. Consequently, they are characterised as preferring long-term investments and fixed income asset classes. Involvement in social investment would have to be with a view to meeting these requirements, or otherwise could be structured through CSR portfolios.

Motivating/influencing factors

- **Investment performance** – social investments that offer risk-adjusted financial returns that rival insurers' other potential investments will be attractive to insurers.
- **Minimising exposure to risks** – social investments that, for example, reduce physical health risks for life insurers, could prove attractive. Appropriate products are limited to date , but some are under development.

Barriers to social investment

- **Fiduciary obligation** – insurers cannot place social goals ahead of maximising investment returns.
- **Minimum investment size** – typical minimum investment sizes are generally around £10m to £20m.
- **Lack of appropriate asset types** – insurance companies prefer fixed income asset classes.

Opportunities to engage insurers

- **Emphasise the mainstream aspects of social investment** - insurers need to see the track record of social investments, and to assess expected performance in the same way as with any other financial investment.
- **Potential to build on insurers' role as product developers** to help develop appropriate social investment products.
- In the long run, there needs to be development of **pooled funds** offering **larger investment sizes** and **appropriate asset types.**

Sector statistics

Total investable wealth:
22% of UK assets under management

Segmentation:
Largest insurers have > £300bn assets under management

Likelihood to engage with SI:
Low/Medium

Likely to contribute to:
Next £5bn est. investments
- Fixed income assets.

Investment history

- In 2013, Legal and General committed to invest £15bn over ten years in 'transport and energy projects, housebuilding, property and education'.
- Internationally, Zurich Insurance invested $1bn in green bonds to diminish effects of climate change because of their exposure to 'social and environmental challenges'.

Pension funds

Pension funds are primarily concerned with financial performance and meeting long-term liabilities. However, Local Authority Pension Funds' concern for local communities may make social investment an increasing priority for the sector.

Overview

The UK pension fund sector is the third-largest in the world. If just 0.012% of UK pension fund assets were allocated to social investment this would double the size of the UK social investment market.

Pension funds are primarily concerned with financial performance, and generally will not consider financial trade-offs to achieve impact.

One exception is Local Authority Pension Funds (LAPFs), who have a special interest in local community welfare. They may consider the impact of social investments, provided they make an acceptable threshold return.

Motivating/influencing factors

- **Investment performance** – the primary motivating factor for pension funds' investment in any asset is investment performance; social investment must be produce comparative financial returns.
- **Diversification** – social investments could potentially be an effective way for pension funds to diversify their portfolio; however, social investments need a stronger track record before this benefit becomes a reality.
- **Concern for local communities** – LAPFs' concern for local community welfare means they will consider they impact of social investments, as long as they meet a required threshold return.

Barriers to social investment

- **Fiduciary obligation** – fund managers cannot place social goals ahead of the goal of maximising expected returns of the fund.
- **Lack of knowledge** – pension funds generally lack knowledge of specific social investment opportunities, and feel they do not know how to evaluate social investments in comparison with traditional asset classes.
- **Minimum investment size** – small investments require high due diligence and supervision costs relative to their size, so pension funds are often not willing to make social investments under £10m.

Opportunities to engage pension funds

- Create more schemes to enable LAPFs to **reach out to social investment opportunities.**
- Create **vehicles for pooled funds** and **mechanisms for shared due diligence costs** across pension funds.
- **Emphasise the mainstream aspects of social investment** – pension funds need to be able to assess social investments as with any other financial investment.

Sector statistics

Total investable wealth:
£1.7tn assets under management at the end of 2012

Local authority pension funds:
99 funds with total of £148bn assets under management

Likelihood to engage with SI:
Medium

Likely to contribute to:
Next £5bn est. investments
- Asset classes able to absorb large investment sizes e.g. energy, infrastructure.

Investment history

- Five Local Authority Pension Funds have agreed to invest up to £50m each in the Investing4Growth initiative.
- USS pension fund and Merseyside Pension Fund invested in the Bridges Ventures Sustainable Growth Fund.
- A number of other impact investments, including in green energy and social housing are supported by a small number of international pension funds.

University endowment funds

University endowment funds are generally managed conservatively. As an investor group they are relatively uninformed about social investment opportunities. They are likely to make social investments only on the basis of financial performance, to help achieve their core mission of long-term sustainability.

Overview

University endowment funds are invested in perpetuity to finance a proportion of the annual running costs of the universities.

The primary concern is maximising investment returns, so any social investments must fit with this objective. The investment by two Oxford colleges in the Bridges Ventures Sustainable Growth Fund demonstrates that if social investments are considered good financial investments, they will be attractive to university endowment funds.

Motivating/influencing factors

- **Investment performance** – the primary motivating factor for investment decisions is to maximise investment returns; social investment must provide comparative financial returns to other investments.
- **Response to student pressure** – universities' investment policies have previously been shaped by student pressure; however, as yet there have been no examples of student pressure leading to the adoption of positive investment screening practices.

Barriers to social investment

- **Is it their role?** – many university investors feel their role is foremost to maximise investment returns for the university, not to prioritise other social goals.
- **Knowledge of investment opportunities –** university endowment funds are some of the least knowledgeable of investor groups on social investment.

Opportunities to engage universities

- **Meetings and events** to engage university endowment funds in conversations about social investment and stimulate debate internally about the role they can play.
- **Emphasise the mainstream and more commonplace elements of social investment –** university endowment funds need to see the track record of social investments, and to assess expected performance in the same way as with any other financial investment.

Sector statistics

Total investable wealth:
7 UK universities have endowment funds worth >£100m

Concentration:
Very few large endowments – Oxford and Cambridge have funds of £3.7bn and £4.9bn respectively

Likelihood to engage with SI:
Low

Likely to contribute to:
Next £5bn est. investments:
- Competitive funds with track records; agnostic on sector.

Investment history

- Two Oxford colleges invested in the Bridges Ventures Sustainable Growth Fund.
- UCL's fund demonstrates that university endowment funds can make risky investments aiming to support mission-related goals.

New Specialist Sources of Capital for the Social Investment Market

RESEARCH REPORT CITY OF LONDON CORPORATION APRIL 2014

The City of London Corporation is a uniquely diverse organisation with three main aims:

- to support and promote the City as the world leader in international finance and business services
- to provide high quality local services and policing for those working in, living in and visiting the Square Mile
- to provide valued services to London and the nation as a whole, including its role as one of the most significant arts sponsors in the UK.

The City of London Corporation is playing a pivotal role in raising the profile of the social enterprise and social investment sector. The City of London's Economic Research programme provides analysis on issues affecting the City.

For more information visit **www.cityoflondon.gov.uk/socialenterprise** and **www.cityoflondon.gov.uk/economicresearch**

The Big Lottery Fund's overarching social investment goal is to play a catalytic role in developing the social investment marketplace. This is based on the belief that social investment offers new financing tools and access to new sources of capital to enable Voluntary, Community and Social Enterprise (VCSE) sector organisations to operate on a more sustainable footing, so they can better provide their services to people and communities most in need.

Big Society Capital is the world's first social investment bank.

Big Society Capital was launched in April 2012, with an estimated £600 million of capital, £400 million of which will be from unclaimed assets left dormant in bank accounts for over 15 years, and £200 million from the UK's largest high street banks.

Big Society Capital's mission is to develop the social investment market in the UK by investing in social investment finance providers and by acting as a market champion. By improving access to finance for social sector organisations, and by raising investor awareness of investment opportunities that provide a social as well as a financial return, Big Society Capital will be instrumental in connecting the sector to capital markets.

The **Cabinet Office** supports the Prime Minister and Deputy Prime Minister, and ensures the effective running of government. It is also the corporate headquarters for government, in partnership with HM Treasury, and takes the lead in certain critical policy areas. This includes responsibility for growing the social investment market, helping the voluntary sector succeed and work with the state, and making it easier for people to give time and money to good causes.

Citi, the leading global bank, has approximately 200 million customer accounts and does business in more than 160 countries and jurisdictions. Citi provides consumers, corporations, governments and institutions with a broad range of financial products and services, including consumer banking and credit, corporate and investment banking, securities brokerage, transaction services, and wealth management.

Citi's commitment to inclusive finance spans the bank's businesses, products, functions, and geographies to capture all of Citi's work connecting previously underserved consumers with the formal financial system and providing the necessary guidance on how to use financial products responsibly. Expanding access is at the heart of Citi's inclusive finance work, which is advanced by linking the core capabilities of every Citi business unit in a shared effort to broaden financial inclusion, achieve economic empowerment and fuel sustainable growth for underserved communities. Key to these efforts is a robust social investment market that directs capital to ideas and solutions that create value for both investors and society.