UK Catalytic Capital

Case Studies & Executive Summary

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Executive Summary

The What

We define catalytic capital as:

"investment into social purpose organisations and/or funds that is patient, risk-tolerant, concessionary, and flexible (or some combination thereof) in ways that can fill persistent capital gaps faced by social purpose organisations and social impact investment fund managers seeking new markets and attracting new capital."

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The relatively simple definition of catalytic capital belies a complex range of approaches, investing instruments and target outcomes.

We have adapted the MacArthur Foundation definition of catalytic capital for use in the UK to reflect feedback from seventy stakeholders. We define catalytic capital as "investment into social purpose organisations and/ or funds that is patient, risk-tolerant, concessionary, and flexible (or some combination thereof) in ways that differ from conventional investment". As the definition highlights catalytic capital can be deployed directly into social purpose organisations, or, as wholesale investment to support the establishment and development of social investment fund managers and markets. Of the four key descriptors of catalytic capital, the case studies, interviews and research conducted have shown that concessional and risk tolerance has come up as the most important requirement for social purpose organisations and social investment fund managers.

The Why

Catalytic capital

can fill persistent access to capital gaps faced by social purpose organisations and social investment fund managers seeding new markets and attracting new capital.

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Catalytic capital can have a transformative impact at scale, by filling persistent access-to-capital gaps faced by social purpose organisations and social investment fund managers and seeding and developing new social investment markets.

Access-to-capital gaps faced by social purpose organisations and social investment fund managers include insufficient provision of investment, limited provision of smaller investments and support for the provision of smaller investments, investment for innovation, research and development, early-stage social purpose organisations, new investment products and new fund managers, affordable investment, and investment that seeks to improve systemic challenges around inclusion (particularly for Black and Minoritised ethnic-led social purpose organisations). In meeting these access-to-capital gaps, catalytic capital can seed new markets and attract significant volumes of new capital into the social investment market.

The How

part one

A pool of concessionary capital is often needed to structure catalytic capital funds or investments.

Concessionary capital, defined as capital able to take a lower-than-market-rate return for a given level of risk, can be deployed directly as catalytic capital or blended with market-rate return capital and/or with non-concessionary catalytic capital to create catalytic capital funds or investments. The mechanisms that could be used to structure catalytic capital funds or investments include grants, subordinated investment and first-loss capital, tax relief such as Social Investment Tax Relief, and guarantees. Providers of concessionary capital include, among others, government, foundations and high-net-worth individuals

part two

Catalytic capital can be deployed through a range of investment instruments.

Equity[1] and quasi-equity is inherently patient and risk-tolerant investment instruments, and are therefore seen as a natural fit for the deployment of catalytic capital. However, any investment instrument can be used to deploy catalytic capital, including debt, equity, quasi-equity, impact-linked investments, and mixed instruments where grants are deployed alongside repayable investment. Interviews and case studies also highlighted that the way investments are managed is as important as the terms of the instrument, in ensuring catalytic capital is patient and flexible.

The How Much

A potential annual market gap of

£189m to £480m.

While there are pockets of catalytic capital provision in the UK, we estimate a catalytic capital funding shortfall for investment directly into social purpose organisations of around £200m annually.

Our calculations suggest the need for £287m to £578m of catalytic capital provision per year. If we assume a current catalytic capital provision directly into social purpose organisations of £98m, this implies a potential market gap of £189m to £480m. Given significant gaps in the dataset and the fact that new supply will undoubtedly drive an increase in demand, these numbers are highly indicative. That said, the scale of potential demand highlights the need for greater provision. At the wholesale level it is harder to estimate demand as wholesale catalytic capital seeds new markets and investment products. That said, data from Big Society Capital highlights the scale of the opportunity. Since inception, Big Society Capital has made £700m of catalytic capital investments and acted as the cornerstone investor in 44 social investment funds. Over this period the social investment market has grown from £830m in 2011 to £7.93bn at the end of 2021. While we cannot quantify the exact leverage of Big Society's Capital it is clear the £700m has been instrumental in attracting new sources of capital to the market.

Figure 1: Summary of catalytic capital – the what, why and how of catalytic capital

<table>
<tr><th>The What</th><th>Catalytic capital is investment that is one or more of …</th><th>Patient</th><th>Flexible</th><th>Concessionary</th><th>Risk tolerant</th></tr>
<tr><td rowspan="2">The Why</td><td rowspan="2">Catalytic capital addresses access to capital issues for social purpose organisations and social investment fund managers and delivers impact by growing and broadening the social economy.</td><td colspan="4">Affordability – expanding the breadth and depth of social purpose organisations. Innovation, research and development, early stage venture funding. New investment products and new social investment fund managers.
Inclusion – expanding the uptake of social investment by organisations developed and run by diverse groups as well as for solutions looking to grow impact within diverse communities.</td></tr>
<tr><td colspan="2"></td><td colspan="2">Insufficient funding (leverage market rate capital)</td></tr>
<tr><td rowspan="6">The How</td><td rowspan="6">Market rate capital is made concessionary and risk tolerant through a range of structuring mechanisms [Part 1] …

& Patient, risk tolerant, flexible and/or concessionary capital is deployed through a range of instruments [Part 2] as …</td><td colspan="4">Grants – the use of grant funding to act as either a first-loss layer, subsidy or technical assistance
Tax relief – the use of tax mechanisms to bring in new investors.</td></tr>
<tr><td colspan="2"></td><td colspan="2">Guarantees
Subordinated investment
– first loss.</td></tr>
<tr><td colspan="4">Debt – unsecured debt, debt with lower than market interest rates and/or repayment holidays and debt paid over an extended period.</td></tr>
<tr><td colspan="4">Equity and quasi equity – non-withdrawable debt, withdrawable equity, revenue participation agreements.</td></tr>
<tr><td colspan="4">Mixed funding models – grants deployed alongside repayable finance.</td></tr>
<tr><td colspan="4">Impact linked instruments – impact linked loans, success notes.</td></tr>
</table>

Source: The Change Coefficient

The Why Not

A lack of concessionary capital is the biggest barrier to increased deployment of catalytic capital.

This is driven by a range of underlying factors including:

- No common understanding of catalytic capital and its role in the wider investment market.
- Significant competition for concessionary capital.
- Uncertainty over who should be providing catalytic capital.
- Trust deficits and concerns about concessionary capital funding private gain.
- Lack of data and evidence on the value case for catalytic capital, both in financial terms and in terms of the social and environmental impact.
- Lack of co-ordination around the provision of catalytic capital.
- Potential lack of market capacity to deploy catalytic capital effectively and efficiently.
- Unhelpful framing of catalytic capital in the language of subsidy.
- A misalignment between funding approaches and the way catalytic capital is typically structured; providers of concessionary capital tend to fund impact areas, whereas current catalytic capital provision tends not to focus on particular outcome areas.

To address these barriers, we have summarised our recommendation into five categories:

1. **Raising awareness of catalytic capital – market building.**
2. **Building the evidence base.**
3. **Creating structures to ensure the effective deployment of catalytic capital.**
4. **Leveraging the experience of outcome contracts and Social Impact Bonds.**
5. **Showcasing the impact potential of catalytic capital.**

The table below details the recommendations within each category, target outcomes for each recommendation and the barriers addressed. Barriers are repeated where they are addressed by more than one recommendation.
We have resisted assigning recommendations to target stakeholders, in the hope of driving greater collaboration.

Table 1: Recommendations to grow the UK market for catalytic capital and ensure the effective deployment of catalytic capital

Category	Recommendations	Target outcomes	Barriers addressed
1. Raising awareness – market building	• Large-scale annual catalytic capital conference with all stakeholders represented in volume. Panels to showcase catalytic capital deals and funds, case studies from social purpose organisations and social funds that have benefited from catalytic capital highlighting the impact of catalytic capital, and workshops to highlight best practice, particularly around impact reporting, investment decision-making, governance and portfolio management. Roundtables to create opportunities for collaboration. • Publication of an annual market survey detailing existing and planned deployment of catalytic capital broken down by target returns and funding mix, sector/impact focus, geography and access to capital gap(s) addressed.	• Increased awareness and understanding of catalytic capital. • Improved co-ordination and understanding of market activity. • Improved understanding of the need for catalytic capital and its impact on social purpose organisations and social investment fund managers. • Improved identification of gaps in the provision of catalytic capital, particularly across the return spectrum of 0-102% return of capital. • Improved co-ordination and the pooling of larger volumes of concessionary capital. • Catalytic capital established as a distinct approach to investing in social purpose organisations.	No common understanding of catalytic capital. Lack of co-ordination. Uncertainty over who should be funding catalytic capital. Lack of data. Competition for concessionary capital.

Category	Recommendations	Target outcomes	Barriers addressed
2. Building the evidence base	• Development of a standardised dataset to be completed by catalytic capital providers and published in the annual catalytic capital report. The dataset would focus on the impact of catalytic capital on the social purpose organisations funded, e.g. growth in revenues, growth in numbers of people reached, and not seek to standardise outcome metrics across social purpose organisations and funds. • Improved data collection on social purpose organisations in general at both local and central government levels.	• Improved understanding of the impact of catalytic capital on social purpose organisations and their service users/beneficiaries. • Improved understanding of the social and economic value created by social purpose organisations. • More stakeholders are encouraged to provide the concessionary capital needed to deploy catalytic capital (particularly government). • Improved efficiency in the deployment of catalytic capital through the identification of what is and isn't working.	Lack of data. Trust deficit. Focus on impact.
3. Ensuring effective deployment of catalytic capital	• Ensure catalytic capital provision across the return spectrum. • Catalytic capital investment committees to have a balance of social entrepreneurs and those with finance or corporate backgrounds. • All catalytic capital funds to have measures in place to ensure other investors are not crowded out by their provision of catalytic capital (e.g. evidence that investees could not get capital elsewhere). • Evidence requirements on the potential impact of the catalytic capital investment on both the social purpose organisation/fund and its service users/beneficiaries ahead of any investment decision. • Fund managers to be adequately funded to provide the hands-on investment management required to ensure catalytic capital is sufficiently flexible during the life of the investment where appropriate. • Increase funding to fund managers already effectively deploying catalytic capital.	• Catalytic capital meets the needs of social purpose organisations driving growth and sustainable social impact. • Catalytic capital addresses critical access to capital gaps for social purpose organisations. • Catalytic capital is flexible enough to adapt to changing market conditions. • Impact is at the heart of decisions around the deployment of catalytic capital driving efficient allocation of catalytic capital.	Market capacity to deploy. Trust deficit.

Category	Recommendations	Target outcomes	Barriers addressed
4. Leveraging the experience of outcome funding instruments	• Explore mechanisms to encourage local authorities and others to provide catalytic capital, alone or in partnership with social investors, with concessionary capital funded through potential cost savings or cost avoidance. • Explore how outcome metric triggers on investments can increase the provision of catalytic capital to social purpose organisations, by linking concessionary rates, risk tolerance, flexibility and/or patience directly to social outcomes.	• More concessionary funding is secured for deployment as catalytic capital. • Shift the narrative from investments where there is some loss of capital, to impact funding with significant return of capital. • Shift the narrative from subsidy to impact generation.	Language of subsidy. Competition for concessionary capital. Focus on impact. Lack of co-ordination.
5. Showcasing the impact potential of catalytic capital	• Development of a fund with the remit to absorb highly concessionary returns, as required, focused on solving a large-scale social problem such as children's care, where for-profit, private equity backed companies are delivering poor outcomes and poor value for money.	• Attract more concessionary funding for deployment as catalytic capital, by linking funding directly to outcomes and showcasing the power of catalytic capital. • Social purpose organisations are inspired to explore the potential of catalytic capital to support their growth plans. • Create a model for effective collaboration, particularly between the providers of concessionary or risk-tolerant catalytic capital and those seeking closer to a market rate of returns.	Focus on impact. Competition for concessionary capital. Trust deficit.

This collection of case studies has been curated in order to bring to life the spectrum of approaches that catalytic capital can take both here in the UK and internationally.

We hope that it proves to be a useful resource for those that are keen to learn more about the usages of catalytic capital. These case studies have been carefully selected in order to ensure that readers of this report have access to the most relevant examples. They contain information both around how these catalytic capital examples are structured, as well as the key information relating to the lessons learnt and the aspects of the approach that relate to taking a catalytic approach. We have also used a breadth of different examples that both showcases catalytic capital deals and funds. We've also included examples from social purpose organisations and social funds that have all benefited from catalytic capital and illustrate the flexible and differing nature of catalytic capital approaches.

For ease, we have categorised the case studies using a UK, Wholesale and International approach to help readers access these effectively. We have also categorised the different types of catalytic capital that these examples fall under in terms of how they are defined from a catalytic capital perspective. For these case studies, it is also worth noting that risk tolerance includes both being risk tolerant (from a financial perspective) but also tackling perceived market risks that exist.

Key of characteristics:

Flexible

Concessionary

Patient

Risk tolerant

Case Studies

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The Bike Project – tax relief (SITR) creating a pool of concessionary risk-tolerant capital

The Bike Project's mission	Provide refugees and asylum seekers in the UK with refurbished bikes, helping them to access food banks and other critical services as well as improving their general wellbeing.
Why is the funding catalytic capital?	Loans were provided by supportive individuals to The Bike Project, which were concessionary (3% annual interest with a three-year repayment holiday), risk-tolerant (early stage of the venture), and flexible (loans have been rolled over). These loans qualified for the government's Social Investment Tax Relief scheme (SITR), a tax incentive scheme that allows individuals to reduce their income tax liability in the year of the investment by 30% of the amount loaned. Flexible funding from a foundation via a revenue participation agreement was also obtained.
Investee entity type	Social enterprise (registered charity, company limited by guarantee).
Year established	2013
Impact focus	Refugees and asylum seekers in London and Birmingham.
Investment instruments	Social investment tax relief loans, revenue participation agreement.
Investment size	£170k of SITR funding (five individuals providing £10k each in 2013, £120k from four investors in 2020), £50k revenue participation agreement in 2020.
Investment terms	SITR loans: 3% interest rate, repayable over years 3-5. Revenue participation agreement: one-year repayment holiday, % of monthly trading revenue paid up to capped total repayment of 1.2x loan amount.

Key points

1. The Bike Project demonstrates how SITR can create a pool of risk-tolerant concessionary investment to be deployed as catalytic capital. SITR loans were first secured by The Bike Project in 2017 to help build its ecommerce operations. This funding is flexible and concessionary, as shown by:

- The Bike Project was able to secure £50k of funding in 2017, despite the early-stage nature of the venture and lack of collateral. The use of SITR as a mechanism to enhance the risk tolerance of individual investors, allowed The Bike Project to access catalytic capital from individual investors.
- The Bike Project was able to negotiate a 3% interest rate, well below rates it may have paid on an institutional loan, given the early-stage nature of the venture.
- No repayments can be made for three years under the qualifying terms of SITR. This allowed The Bike Project more time to deliver on its growth strategy and to reinvest profits into the business for longer, before having to make repayments.
- SITR loans are made by individuals who typically have a high degree of flexibility over how long they can hold an investment, unlike most social investment funds that have fixed lives beyond which investments cannot extend. As a result, The Bike Project was able to renegotiate the term of the five original £10k SITR loans, from bullet repayments at the end of year 3 to equal repayments spread across years 3-5. This flexibility also extends to the terms of the loans, and in its most recent SITR funding, The Bike Project was able to negotiate clauses that allow repayments to be delayed or funding restructured, should sales fall short of expectations.

2. The challenge with SITR, is that it is not well known to organisations, and access to a network of individual investors is needed. The Bike Project benefited from the founder's exposure to SITR through a fellowship programme, and his ability to find and attract philanthropically minded individuals to invest in The Bike Project.

Creation and structure

The Bike Project's mission is to take second-hand bikes that have been donated, fix them, and give them to refugees and asylum seekers in London and Birmingham. A bike helps recipients access food banks, legal advice, healthcare, education and other services. A bus fare typically costs £23 per week, over 50% of the £40.85 a week that refugees and asylum seekers receive.

The organisation also runs group cycle training for female refugees, skills and maintenance workshops, and a cycling buddy pairing programme. As well as its charitable activities, the organisation sells some of the refurbished bikes to the public through its online bike shop.

The next step in the organisation's evolution is setting up a flagship store in Camberwell, to encourage more people to collect bikes, generate more revenues through the sale of bikes, and encourage local community engagement. This new retail project has been funded via c£120k of SITR funding and £70k in donations. Access to catalytic capital at the point of need has allowed The Bike Project to secure a ten-year retail lease on favourable terms.

Outcomes

Having received capital in a timely fashion, at concessionary rates with a high degree of flexibility, The Bike Project has been able to grow its business, have the confidence and support to take on new ventures (e.g. new retail and community space that it is developing), and not be distracted by capital-raising issues, which shift focus from operations. The network effects of SITR, where passionate philanthropic individuals have in turn promoted investment in The Bike Project to other philanthropic individuals, have also helped. Catalytic capital has been instrumental in The Bike Project being able to give away over 7,500 bikes to refugees so far, with free service and repairs at any time. Revenues at The Bike Project have increased eightfold in the five years from 2015 to 2020.

The Community Shares Booster Fund – supporting organisations to mobilise communities to deploy catalytic capital

Booster's mission	The Community Shares Booster Programme (Booster) provides institutional investment into co-operative and community benefit societies, alongside and on the same terms as community shares. The community shares (often referred to as comshares) leveraged in give local individuals an ownership stake in local community businesses, while the businesses can benefit from much-needed unrestricted funding that is long term, risk-tolerant, patient and flexible.
Why is the funding catalytic capital?	Comshares, and the matched equity investment from the fund that is made on the same terms, are highly patient forms of capital – the shares are non-transferable and although withdrawable under certain conditions (such as providing sufficient notice), withdrawals tend to be low. Income on shares tends to be low (sometimes zero; highly concessionary) with individuals motivated to invest to support the community, rather than achieve a financial return. Capital tends to be risk-tolerant, with each individual on average investing a small amount.
Year established	2013
Investing entity type	Fund
Impact focus	Local community businesses and assets in the UK
Source(s) of capital	Power to Change, Architectural Heritage Fund
Fund instruments	Equity
Investment size	Up to £100k
Investment terms	Booster matches up to £75k-100k of comshares raised with share capital from the fund. Investment is not transferable, but capital can be withdrawn with sufficient prior notice, usually after an initial period in which withdrawals are not permitted. Booster also offered £10k in grants to support them prepare the community share offer (including costs of the Community Shares Standard Mark).

Key points

1. Comshares are a clear example of catalytic capital – they are patient, concessionary, risk-tolerant and often flexible. Comshares engage local people or people united behind a shared cause as shareholders. These investors are typically motivated by a desire to support the community, rather than achieving financial returns. A small return is typically paid on comshares (i.e. highly concessionary). The shares are not transferable but can be withdrawn after a certain period of ownership. Small sums provided by thousands of supportive individuals ensure the capital is often more risk-tolerant than institutional funding.

2. Booster provides matched equity to comshares on the same terms as the community investors, thereby investing alongside the community and taking on shared risk and benefits. Co-operatives and community benefit societies ("businesses" in the context of this case study) receive matched equity investment from Booster: up to £75k comshares for businesses that are readying their share launch, and £100k for businesses that have launched an offer or will do so shortly.

Creation and structure

Booster was launched in 2013 and is managed by the Community Shares Unit, a joint initiative between Co-operatives UK and Locality. It is currently funded by Power to Change and the Architectural Heritage Fund. In addition to providing equity funding, Booster deploys grants to businesses that need development support to get them to share offer launch and analyses and researches how the comshares model can be applied to new places and sectors to strengthen community businesses.

Outcomes

A 2020 report funded by Power to Change and Community Shares Scotland (Understanding a Maturing Community Shares Market) found that in the less than ten years since comshares began in the UK, more than £155m of financing had been raised from c525 investment raises by over 104,000 people supporting more than 440 organisations. Importantly, 92% of businesses that raised finance were still trading, 85% stated that the share offer had a positive impact on their financial performance, and 80% of people that invested attributed their investment to social or environmental benefits of the organisation (less than 20% cited finance returns as the driver). For every £1 invested in community shares, the report found that an additional £1.18 was leveraged via grants, loans and institutional investment.

Booster has played an important part in this market. For every £1 invested by Booster, on average £2.60 of comshares investment has been attracted. Without the combination of Booster investment and comshares, some of the organisations provided with funding may have been unable to find alternate funding, unable to take risks, unable to deliver the impact they have achieved, and been financially unviable.

Case Study Three - Social purpose organisation case study

Fordhall Farm – catalytic capital deployed as community shares

Fordhall Farm's mission	A social enterprise was set up to save Fordhall Farm from redevelopment and restore it to a sustainable, organic farm with traditional farming techniques to act as a learning centre. Fordhall Farm has since expanded to include a café, farm shop, event days, online store, educational visits, free farm walks and accommodation.
Why is the funding catalytic capital?	The founders were seeking patient capital and wanted to build a community through their investor base, so ran a community share (comshare) issue – selling both equity and loans to individuals on concessionary terms (0% interest), that were flexible (loans often converted to donations), patient and risk-tolerant (funding given when the farm was dilapidated and had little income).
Year established	2005
Investing entity type	Social enterprise (industrial and provident society).
Impact focus	Sustainable food production and education.
Investment instruments	Catalytic capital – comshares (£705k of 2005 funding), interest-free loans (£250k). Fordhall Farm also took on a commercial mortgage (£100k) and received donations.
Investment size	£1.1m in 2005, and follow-on funding of £1.5m+ since. Comshares continue to be sold to new members.
Investment terms	Existing comshares cannot be sold and carry no dividend (but can be refunded upon request contingent on the enterprise having sufficient funding); interest-free loans were for five years (most have been converted to donations), 30-year term for mortgage.

Key points

1. Engaging with a community united by a common cause supports the raising of catalytic capital. In 2005, the Hollins family raised £1.1m to buy and update the family farm it had leased for hundreds of years, saving it from redevelopment. The family did this by creating a community of supporters.

- Fordhall Farm accessed catalytic capital in the form of concessionary and patient comshares – lifelong, cannot be transferred or sold, but are refundable with 12 months' notice (only £2k-4k has been redeemed per year and mostly upon the death of a member). In addition, the organisation borrowed £250k in interest-free loans from members that were repayable after five years.
- Funding was risk-tolerant – at the time of purchasing the farm outright, it was in a dilapidated state following years of funding being diverted to legal expenses to fight potential eviction and redevelopment. The vision to turn around the farm was high-risk and further investment was required beyond the £800k purchase price. Comshares tolerated this risk – over 8,000 members provided £705k of funding, an average of less than £100 per person. Surveys conducted by Fordhall Farm confirmed individual investors were motivated by a desire to support the community rather than for financial returns.
- Interest-free loans have been highly flexible – Fordhall Farm leveraged relationships with members to issue £250k of interest-free loans. When loans came due (initially after five years), Fordhall Farm successfully appealed to lenders to treat loans as a donation and earn Gift Aid (c£180k-190k converted to donations), or to roll them over (c£50k-60k extended the loan duration). The organisation has had to repay just c£20k of its interest-free loans.

2. Catalytic capital filled a clear access-to-capital gap for Fordhall Farm, which has allowed the organisation to focus on its social mission. Fordhall Farm originally explored buying the farm via a normal business loan, to then sell part of the farm to help repay the loan, however that would have gone against the organisation's social mission and diluted its ability to deliver impact. Social investment loans were also considered in 2006, but it was uncomfortable taking on the risk of a fixed interest rate loan, when it had little income from the farm.

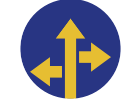
Creation and structure

Fordhall Farm is a sustainable, organic farm in Market Drayton, Shropshire, employing traditional farming techniques. It has been home to the Hollins family for over 700 years. The family had leased the land and had been engaged in over 15 years of legal battles with their landlord, who was seeking to evict them, with pressure from a neighbouring international dairy manufacturer wanting to redevelop the land. The organisation was set up as an industrial and provident society for community benefit.

Outcomes

The catalytic capital received by Fordhall Farm helped save the farm from redevelopment. Through the creation of a membership base of comshare owners, Fordhall Farm has been able to access further rounds of funding. Investment has allowed buildings, equipment and the farm to be restored in a sustainable and ecological way. Fordhall Farm now boasts a farm shop, farm kitchen, an event catering business, event spaces for hire, event days (including educational experience days and site visits), a tenant farmer, an online shop and accommodation 'glamping'). Fordhall Farm is now financially sustainable, having been profitable every year since 2015, and has healthy cash reserves that can be reinvested to increase social and environmental impact. During the summer months the 128-acre site can attract over 25,000 visitors and employs over 100 local people.

Case Study Four - Fund case study



Futurebuilders England Fund – catalytic capital supporting the delivery of public services

Aims of Futurebuilders	Futurebuilders was the UK's first social investment fund of scale and aimed to test the ability of social enterprises in England to take on repayable finance (in the form of loans) and become more involved in delivering public services. Investment aimed to improve organisational development, support more effective public service delivery, and improve outcomes for service users.
Why is the funding catalytic capital?	Funding was provided in the form of loans, grants or a blend of loans and grants, depending on the entity's size. The fund served charities and social enterprises, and investees were only slightly profitable (on average). Loans were long term and highly flexible, with interest and/or payment terms varied for almost half of all loans. A 'rescue pot' of money was also established during the financial crisis, to help investees alongside the fund. Interest rates were concessionary, more than 0.85ppts to 2.75ppts below alternate social investment funding.
Year established	2004
Investing entity type	Fund
Impact focus	Social organisations bidding, winning and delivering public service contracts in England, especially in the health and social care spaces (c47% of funding), as well as education & learning (c26%).
Source(s) of capital	UK Treasury
Fund size	£142m
Investment instruments	Loans only (c12%), grants (c3%), and blend of loans & grants (c85%, with 83% on average of the blend being loans).
Investment size	Loans: average £481k, median £219k, range of £16k to £5.3m
Investment terms	Loans were offered at 2.14% above Bank of England base rates, with an average 13.9-year term. Options in some contracts allowed rates to move from 6% fixed to 3% variable, which was subsequently offered to all investee borrowers.

Key points

1. Futurebuilders was a catalytic capital fund that aimed to prove the ability of larger social enterprises delivering public services to take on social investment. Futurebuilders was highly innovative when it launched in 2004, blending grant and investment to create highly patient, concessionary, risk-tolerant and flexible capital.

For the investor:

- There was no portfolio financial return target set at the outset. However, after the fund had been closed to new investments, it set a target of recovering at least 75% of capital invested.
- Default rates (write-offs and provisions) have been relatively low at 18% (as of December 2021), well below the 25% fund target.
- As of early 2019 and with the fund still having a further 16 years until it is closed, £99m had been paid to HM Treasury, including £72m of capital repayments related to the c£117m repayable financing that was provided to investees. Including c£9m of loan write-offs, c70% of the loan book has been closed within the first half of the fund's life.
- On the repayable financing (loan) component, the fund's IRR was +1.2% as at May 2020. Including grant subsidies together with long-term business support and portfolio management costs, the IRR was -8.1%. The fund's manager, Social Investment Business (SIB), expects the IRR achieved to increase further over time.

For investees (and consequently wider social impact):

- On average, investees employed 16% more staff three years after receiving Futurebuilders' investment, and wages also increased;
- Financial resilience improved with revenues, net assets and cash reaching and plateauing at new highs in the three to four years post-investment, while organisations were also sustainable, and default rates lower than anticipated.
- Further funding and refinancing have since been obtained by investees, including funding similar to that for which investees had been turned down before receiving Futurebuilders' investment. Approximately 13% of investees received £96m of further loans and c64% of investees obtained £285m of further grants.

2. Investee selection is one factor contributing to the fund's outcomes. On average, investees had revenues of £712k and were very slightly profitable (£14.5k, 2% margin), employed 30 staff, and had £498k of assets including £110k cash. Following criticism from other lenders that the fund was distorting the market, part way through the deployment period, Futurebuilders introduced a requirement for organisations to show that they had been unable to obtain funding from at least two mainstream lenders. The remit of the fund was to invest in enterprises that others would not.

Investees also tended to operate in geographic areas of highest deprivation, with 41% of investment deployed to the 20% most deprived areas. While one shortcoming of the fund was a lack of impact measurement built into the fund, the geographic profile of its funding suggests it accelerated potential social impact, which is the goal of catalytic capital.

3. The type of instrument offered to investees, blending grants and loans case by case, contributed to Futurebuilders' success. As repayable finance to social organisations was being tested for the first time, the funding by its nature was highly risk-tolerant. The size of the investee largely determined how much funding was grant and how much was loan, with smaller enterprises/charities receiving a higher blend of grants vs loans.

Funding could be grant-only, loan-only, or a mix of grants and loans. Of the c£142m fund, £17m was deployed as loan-only deals (c12%; 27 deals to 26 unique organisations), £4.6m was grant-only (c3%; 189 deals to 183 unique organisations), while the majority of funding was deployed as blended deals (c85%; £120.6m in 179 deals to 175 unique organisations, with loans on average representing 83% of the mix). The table below shows the mix of grants and loans and how higher blends of grants were used to improve affordability for smaller organisations.

Futurebuilders' mix of grants and loans

Organisational revenues > % Grant component	<£100k	£100k-500k	£500k-1m	£1m-5m	£5m+
0%	0%	8.33%	0%	9.09%	43.75%
0%-10%	0%	4.17%	21.74%	21.21%	6.25%
10%-20%	30%	20.83%	17.39%	48.48%	31.25%
20%-30%	60%	33.33%	34.78%	6.06%	0%
30%-40%	20%	25%	17.39%	15.15%	12.5%
40%-50%	0%	8.33%	0%	0%	6.25%
50%-60%	0%	0%	4.35%	0%	0%
70%-80%	0%	0%	4.35%	0%	0%
Total	**5**	**24**	**23**	**33**	**16**

Source: SIB.

4. Funding terms were highly flexible, patient, concessionary and risk-tolerant, with a further emergency fund aligned to Futurebuilders to be used alongside it.

- Very patient – the average loan duration provided was 13.9 years.
- Highly concessionary – the interest rates on average were 5.45%, well below the average 6.3% for secured loans and 8.2% for unsecured loans from alternate social investment fund intermediaries at the time, according to analysis by the Department for Work and Pensions. The average Futurebuilders' interest rate was 2.14% above Bank of England base rates, which today would reflect a rate of less than 3%. Accounting for the grant subsidies that were blended, the rate would be just 0.55% above base rates. Rates were also reduced over time, largely in response to the impact of the 2008/09 financial crisis.
- Flexibility offered – as the fund did not have the ability to recycle funds, it could not provide additional funding to investees. However, it was able to vary funding terms when investees needed help (after the 2008/09 financial crisis). Approximately half (46%) of all deals were varied from their original terms – of these, 68% revised the interest terms, 18% revised payments and just under 14% revised both interest and payment terms. For example, some investment contracts provided the investee with the option to reduce their interest rate from 6% fixed to a more concessionary 3% variable rate. The fund's investment committee decided to extend this option to all investees out of fairness. Ultimately 15% of all investees who received loans utilised this option.
- A separate rescue pot of money (the Monetisation Fund) was aligned to Futurebuilders in response to the challenging economic conditions after the 2008/09 recession and provided to investees that needed help. £1.1m in grants was provided to 35 investees and £7.4m of 0% interest loans to 47 investees.
- Efficient deployment to investees struggling to find funding elsewhere – unlike the due diligence processes for other funding which could be six to 12 months, Futurebuilders provided funds to investees within a relatively short timeframe. The largest grants went to the smallest organisations, including when blended funding was provided.

5. The fund also stands out for the data and evidence base that it has provided, with ongoing research. The fund, with support from DCMS, has tracked and shared the financial performance and statistics of its investees and portfolio. The evidence base shows how catalytic capital can drive growth and sustainability of social enterprises. This could encourage further catalytic capital and help design funds and future financing. Data has also pointed out what has not worked. For example, deals that involved large property purchases that were dependent on renting out part of the property to repay loans, were less successful on average.

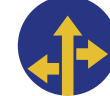
6. The collaborative design of the fund has contributed to Futurebuilders' success. Many stakeholder groups were involved, from government to social enterprises. One potential gap in design was more extensively consulting with local infrastructure bodies.

Creation and structure

Futurebuilders was set up following HM Treasury's Cross-Cutting Review of the Role of the Voluntary and Community Sector in Service Delivery in 2002. The purpose of the government-backed fund was to test providing social investment (in the form of loans) to social enterprises in England to help them bid for, win and deliver public service contracts. Futurebuilders invested in 359 organisations across 403 deals. The health sector was a priority, given the favourable commissioning environment at the time, and the health and social care sectors attracted 47% of Futurebuilders' funding.

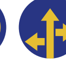
The fund was managed by a consortium (Charity Bank, Unity Trust Bank, Northern Rock Foundation and the National Council of Voluntary Organisations) from 2004-07, and has since been managed by SIB, which disbursed the remaining funds from 2008-10 and managed the loan book.

SIB believes that Futurebuilders was instrumental in demonstrating social investment could be delivered at scale, and showcased the power of social investment to policymakers, given the government was the investor.



Firstport's Catalyst Fund – venture funding

Firstport's Catalyst Fund mission	Create a funding model that closes the funding gap for early-stage Scottish social enterprises.
Why is the funding catalytic capital?	Provides funding for organisations that cannot obtain alternate financing, which is risk-tolerant (high growth potential) and flexible (repayments depend on revenue success).
Year established	2021
Impact focus	Scottish social enterprises without access to alternate funding.
Source(s) of capital	Scottish government provided the fund with concessionary capital.
Fund size	£15m
Required return	The fund is targeting market rate returns on its investments but can absorb lower returns at the fund level to support higher-risk venture investments.
Investment instruments	Revenue participation agreements (quasi-equity)
Investment size	£50k and above
Investment terms	Repayments are typically capped at 1.3-1.5x of the original loan and repaid as 3-4% of monthly trading revenues with a one-year repayment holiday. Investments are typically repaid over seven to ten years.



Key points

1. Several years of research identified the funding gap for c200 social organisations in Scotland each year. These organisations were identified as having the potential to scale and deliver social impact but could not access the social investment needed to do so. Through the business support provided by Firstport and the Social Entrepreneurs Fund, Firstport saw circa 90% of the pipeline of early-stage social enterprises in Scotland (c1,200 per year), and therefore had unique insights as to the access-to-capital gaps faced by social enterprises.

2. Firstport has found that revenue participation with a repayment holiday is an effective instrument for the deployment of catalytic capital. Catalyst Fund investees repay investment as a fixed proportion of revenues with a one-year repayment holiday. The Catalyst Fund invests in enterprises or development projects with high margin potential and works with investees to ensure the repayments are financially viable and will not put undue strain on the business. The revenue share model ensures investor and investee are aligned on growth.

3. The investor in Firstport's Catalyst Fund has provided funding on terms that allow Firstport to deploy catalytic capital, but there are conditions to ensure the efficient allocation of this concessionary funding. Investees typically do not yet have the scale or track record to be able to secure investment. However, to ensure the catalytic capital is efficiently allocated and genuinely meeting access-to-capital gaps, Firstport requires evidence that the investee has been unable to secure commercial investment, typically from their banking provider.

4. Achieving debt-like returns on ventures capital (VC) odds is very difficult. A repayment multiple cap is set at the outset of the loan, based on the financial risk assigned to the borrower, which for an average risk organisation may be 1.3-1.5x. Typically 3-4% of trading revenues (i.e. ex grant income) is repaid each month. The cost is comparable to a ten-year loan with a 12% pa interest rate. While these rates may sound higher than average social investment deals, on a risk-adjusted basis they are concessionary. The Catalyst Fund allows social enterprise models to grow at more modest rates than is typically required by equity investors.

Creation and structure

Firstport is a registered charity and social enterprise, which since 2007 has provided funding and support to social entrepreneurs and social enterprises in Scotland. It aims not only to provide financial support to organisations (including grant funding for socially minded business ideas via its Social Entrepreneurs Fund), but also to help ready them to take on further investment and to improve their processes and financial management through initiatives such as its LaunchMe accelerator programme (for business support and investment readiness). Firstport launched the Catalyst Fund in the summer of 2021, to address the c200 organisations per year it found were falling through the social investment gap.

- **Catalytic capital:** The fund's cornerstone investor is the Scottish government, which provided £15m.
- **Investment allocations:** Each investment is given an overall risk rating, as each rating has a certain allocation at the portfolio level. Financial risk ratings are complemented with ratings that encompass potential impact created, the investee's ability to report on impact, how likely the organisation is to become sustainable and how well it fits within the Catalyst Fund mission, among others.
- **Fund operations:** Organisations send quarterly management accounts to the fund and repay based on the quarter in arrears. If the accounts are not sent (with actual figures), repayments may be based on projections. If estimates are optimistic, it is in the interest of organisations to ensure actuals are sent, otherwise the organisation could overpay. The fund has board observer rights and endeavours to maintain a close and supportive relationship with investees.

Outcomes

The fund currently has a pipeline of c40 businesses that are pre-application. It has made three investments so far in the less than 12 months it has operated – £190k in a biochar water remediation tech business (Sustainable Thinking Scotland CIC), which had been a member of Firstport's investment readiness programme, £50k to build out educational activities and accommodation rentals for an eco-food business (Woodside Arran CIC), and £85k for an ethical garment print and embroidery service business (Wild & Kind CIC) to create jobs and investment in equipment.

Case Study Six - Fund case study

Sumerian Foundation – providing catalytic capital alongside pre- and post-investment business skills support

Sumerian's mission	To support early-stage social enterprises, achieve viable growth and lasting impact at scale, with a focus on those led by people with lived experience and from disadvantaged backgrounds.
Why is the funding catalytic capital?	All investment is in the form of patient and flexible finance, with the nature and terms of each instrument co-developed with the social enterprise to ensure both affordability and suitability with the business model.
Year established	2017
Impact focus	Early-stage social enterprises tackling different dimensions of social inequality in the UK.
Source(s) of capital	HNWIs, Comic Relief, Golden Bottle Trust and Access Foundation
Investee entities	Legal structure agnostic.
Investment instruments	Largely but not limited to revenue participation agreements, profit share agreements and preference shares.
Investment size	Typically of £70k to £140k.
Investment terms	All funding instruments include repayment holidays, all investments are patient (typically seven to 12 years), rates are concessionary by nature of the business models and impact focus, with caps being placed on total capital repaid.

Key points

1. Catalytic capital is deployed as revenue participation agreements, profit share agreements and preference shares, as these instruments typically align with the cash flow profile and business models of most early-stage social enterprises. These instruments are risk-tolerant as well as patient and flexible.

- Based on successful experience in emerging markets, Sumerian recognised a funding gap for early-stage social enterprises in the UK – that were either unable to access investment as they were considered too risky, or else were able to access only fixed rate debt, which lacked the patience, flexibility and affordability they required.
- Sumerian addressed this funding gap through providing a range of 'quasi-equity' instruments (including revenue participation agreements and preference shares structured). The advantage of these instruments is that repayment is linked to performance and cash flow, terms are affordable and concessionary, and no ownership rights are conferred to the investor (unlike traditional equity).

2. Investing in early-stage, high-impact potential social enterprises requires a growth mindset and a transparent process.

- Debt investment is typically based on assessing past track record and evidence of stable cash flow generation, given the focus is less on growth and more on capital protection. Sumerian's view and experience is that an 'equity mindset' is more appropriate to investing in early-stage social enterprises, based on assessing the future growth and impact potential of the business model and the quality of the team to implement this at scale.
- Sumerian always co-develops the nature and terms of any finance with each social enterprise. This helps build understanding of the different types of investment available, as well as ensuring transparency.

3. Pre- and post-investment business skills support is as critical as the type of finance provided.

- Sumerian provides in-house pre- and post-investment business skills support and mentorship, reflecting its own experience of starting and growing small businesses, social enterprises and charities. Typically, the management teams of early-stage social enterprises require help in business strategy, financial management and planning, and thinking about how much and what type of investment they need. Such skills support is provided at a pace suited to the needs of each social enterprise and is key to overcoming the wariness many people have with regard to taking on investment for the first time.
- Offsetting the cost of vital skills support to social enterprises is challenging, given the need to also ensure investment is affordable. Securing subsidy is therefore important, to enable social investors such as Sumerian to provide this essential support to social enterprises, and particularly to those founded and led by people from traditionally disadvantaged backgrounds.

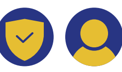
Outcomes

To date, Sumerian has invested in 11 social enterprises located across the UK and is actively seeking to invest in up to 20 further social enterprises tackling different dimensions of social inequality by 2025. Sumerian agrees financial and impact performance metrics with each social enterprise and has recently produced an Impact Report describing key lessons learned, as well as progress against outcomes at the portfolio level.

Case Study Seven - Fund case study using grants to structure a pool of concessionary risk-tolerant capital

The Growth Fund – plugging an access-to-capital gap for small-scale funding

Growth Fund aims	The Growth Fund is a partnership between The National Lottery Community Fund, Big Society Capital and Access, and delivered through a range of social investors. It is designed to provide the finance that charities and social enterprises need for growth or diversifying their business models. The fund is aimed at organisations that are unlikely to have taken on social investment before. The fund aims to address the lack of unsecured, affordable small-scale funding (up to £150k) for English charities and social enterprises. Funding is deployed through social investors and supports the development and growth of social investors.
Why is the funding catalytic capital?	The programme is designed around a market gap. It supports the operating costs of fund managers, which would otherwise have been passed on as higher interest rates or prevented the loans being made at all. Investees are provided with a risk-tolerant, concessionary blend of grants and unsecured loans. The blend also helps lower effective interest rates to investees, which often makes the lending possible. Fund managers are provided with a first-loss layer of grant capital for defaults, allowing them to make more risk-tolerant investments.
Year established	2015
Impact focus	English charities and social enterprises needing small-scale funding (up to £150k) in any sector.
Source(s) of capital	The National Lottery Community Fund (NLCF, c£21m concessionary capital in the form of grants), BSC (c£20.2m investment capital requiring a return) and some other sources of loans fund the programme (c£1.5m).
Fund size	c£43m.
Investment instruments	Loans or blend of grant and loans.
Investment size	Maximum £150k (grant + loans), average £67k (of which 16% is grant).
Investment terms	Loans are unsecured, with an average interest rate of 7.2% (5-12% range) for an average repayment term of 4.25 years (typically ranging from three to six years). Maximum grant component of funding provided is 50% (typically 15-30% of investment is grant, and 73% of loan recipients receive a grant component). (Data as of September 2021.)



Key points

1. Funding is designed to fill an access-to-capital gap for charities and social enterprises. The programme was designed in 2014/15 and seeks to fill a gap in the provision of small <£150k, unsecured loans to charities and social enterprises. The programme focuses on supporting charities and social enterprises taking on investment for the first time and in the early stages of developing or growing trading revenues.

2. Blending capital with a positive return requirement (+c5%) with grants creates a pool of concessionary, risk-tolerant capital. BSC provided c£20.2m of loan capital and NLCF provided c£21m of grants to the programme. This money, which is managed by Access in a wholesale capacity, funds 16 blended finance/catalytic capital funds run by 14 social investors. In turn, these 16 funds provide charities and social enterprises with blended grant and loan investment. Funds are provided to each social investor in three pots for specific purposes. Grant A is an operating cost subsidy for social investors to support the additional cost of making small loans; Grant B a fund-level grant blended with debt from BSC to increase the risk tolerance of the fund and act as a first-loss layer; and Grant C a deal-level blend for investors to provide discretionary grants to investees alongside their loans.

3. The financial challenge of delivering small loans at affordable rates is addressed through Grant A. Grant A supports the fund manager's operating costs. This is needed as operating costs as a proportion of the investment are higher when making small loans, as compared to making large investments. This is because costs per loan such as marketing, due diligence and loan management are largely the same regardless of loan size.

Each fund manager was initially permitted no more than 10% of its grant funding in the form of Grant A (as of September 2021 the average was c9%, a grant of £120k, with the range being £49k to £200k). The subsidy aims to cover the cost of setting up funds and the cost of deployment prior to investments generating sufficient fees and repayments to cover operating costs.

4. First-loss grant layer enables more risk-tolerant capital to be provided to investees. Grant B provides a first-loss layer to fund managers to cushion defaults on investee loans, so that fund managers can repay BSC and other investors who require a positive return on their investment. BSC lent capital at a 5% interest rate. With the onset of Covid-19, BSC has since reduced its rate. Grant B represents 29% on average of the total fund size (loan + Grant B). As of 31 December 2021, only 7% of the aggregate portfolio has been reported as in default – £2.49m out of £35.2m (these figures exclude Grant C).

5. Grant funding is also provided at the deal level to improve affordability. Grant C enables social investors to deploy grants alongside investment at the deal level. The grant component of the investment provided by fund managers to investees cannot exceed 50%. Apart from these conditions, Grant C is highly flexible and discretionary. Almost all fund managers have reported providing blends of loans and grants to investees on a case-by-case basis, which on average represents 15-30% of the investment provided. Some grants are offered on a repayable basis, as flexible, quasi-equity with repayment linked to achieving certain performance targets, while the vast majority are non-repayable. Fund managers acknowledged that the blend helped reduce interest costs for investees (concessionary). Grant C enabled greater focus on impact.

6. Key learnings and evidence from the fund (deployment of the Growth Fund ran to 2022/23) highlight the need for more flexibility around the use and timing of grant funding. Key points included:

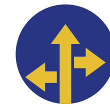
- Fund managers suggested that having three pots of grant with restricted use means the programme is complex and somewhat inflexible. While this may be true, some boundaries around the use of grant funding are needed to support the design process and ensure efficient use of concessionary capital. Furthermore, a degree of standardisation supports effective data collection and evaluation.
- Not having the flexibility to deploy more grants to investees than was originally budgeted and received as Grant C, may have partly limited the flexibility of funding to investees. However, the partnership has responded with post-investment growth support and Covid-19 business support to investees (at their social investors' discretion).
- Some fund managers stated that limiting the amount of Grant A subsidy for operating costs and the time within which it could be drawn down, meant that deployment has been the main driver of activities and decisions, limiting the scope for innovation and post-investment support. The partnership has acknowledged that it would be helpful in future to allow more flexibility in terms of operating costs subsidy and the time for which this is available.

Outcomes

Evidence from the Growth Fund, including independent evaluations, suggests that the blend of finance is helping to address the access-to-capital gap for small, unsecured lending. Funding is flexible and risk-tolerant, and potentially more concessionary than alternative funding (if any) that charities and social enterprises would have been able to obtain. With its continued monitoring and growing evidence base, the programme should help build a better understanding of which parts of the market can support investment at certain levels of subsidy.

As at March 2020, the 16 investment funds have achieved a mixed performance, with six outperforming deployment targets, six underperforming before being reprofiled or restructured, and four funds not being able to achieve deployment targets (all were new to social lending). Five funds had been restructured including one being closed, while two funds have been reprofiled with a higher fund size.

As at the end of September 2021, the programme has funded more than 500 social enterprises across more than 600 investments to date, with £40m of investment deployed. The median investee has £230k of revenues and five employees, and 28% receive Reach Fund or other capacity building support. The average investment size is £67k (16% of which is given as a grant on average, with 73% of recipients receiving some grant) with an average loan term of 4.25 years and 7.2% average interest rate. The geographic regions that have benefited most are the North-West and South-West, and a disproportionately high number of investments have been made into organisations in areas of higher deprivation.



Esmée Fairbairn Foundation – highlighting the importance of organisational culture in the effective and efficient deployment of catalytic capital

Esmée Fairbairn Foundation's mission	The Esmée Fairbairn Foundation (Esmée) aims to improve our natural world, secure a fairer future, and strengthen the bonds in communities in the UK. Esmée does this by taking an impact-led approach to all of its activities and contributing all that it can to unlock change by people and organisations with brilliant ideas who share the Foundation's goals.
Why is the funding catalytic capital?	This case study focuses on the social investment facility that was carved out of Esmée's endowment. The facility has an impact-first culture with investment often being more concessionary, risk-tolerant (subordinated positions, investing when others won't), patient (longer term) and flexible (restructured during the life of the loan/extended beyond the initial term).
Year established	1961; first social investment made in 2008.
Investing entity type	Charitable foundation and one of the UK's first social investors.
Source(s) of capital	Foundation endowment, with a carve-out for social investment.
Fund size	£45m social investment carve-out.
Required returns	Below-market, average return on investments exited has been 2%.
Investment size	£100k to £2m (average £437k).
Investment terms	Often more concessionary (including rates), patient (e.g. ten years) and flexible (e.g. around rates) than other funders.

Key points

1. Esmée's impact-first culture drives its decision-making and use of catalytic capital. In 2008, Esmée carved out £45m from its £1bn endowment for the purposes of social investment. This carve-out has been invested with a clear impact-first approach, which is embedded in the organisation's culture.

- Flexible approach to the type of funding needed – Esmée believes the key to its success has been adopting an impact-first mindset, understanding the issue which needs to be resolved first, and then developing solutions around it with an appropriate funding instrument (including equity-type instruments as well as loans).
- The organisation's culture is based on trust and a 'just get it done' approach. It adopts a risk-tolerant, impact-first mentality – it often funds the unusual and go where others are sometimes unwilling to go. To enable it to do this, the team tries to maintain a balance between low-, medium- and high-risk investments within the social investment portfolio. The current portfolio is split broadly equally among these three levels of risk.
- Flexible when circumstances change – Esmée's investment team consists of three individuals, managing over 80 investments. The size of its team and the culture allow the foundation to pivot when an investment is not working, and to make changes quickly. The staffing of an internal social investment programme providing catalytic capital effectively is a key consideration for foundations.
- There's a focus on simplicity, with easily understood financial solutions and reporting requirements, good communications and a mutual understanding of expectations.
- The foundation can take more subordinated and risk-tolerant positions in an investee's funding structure, or provide funding on more concessionary terms, than others. For example, in 2020, Esmée provided the affordable credit provider Fair for You with innovative funding in the form of a perpetual bond – in this case, capital that is repaid at the borrower's discretion.

2. The organisation benefits from its years of experience as one of the UK's first social investors, constantly applying learning to improve, and sharing its learning with the market to drive social outcomes.

- Sector expertise helps identify market funding gaps – Esmée's social investment pipeline benefits from the sector expertise of its grants team, which helps identify gaps in the market and the open sharing of these ideas with the investment team.
- The foundation uses development grants upfront, to ensure that organisations do not take on social investment before they are ready, and the co-design of solutions helps to form a closer relationship with the investee at the outset.
- Other funders that are not as risk-tolerant will often signpost organisations to Esmée. Many early-stage ideas tend to come directly or indirectly from Esmée's network.
- For Esmée, learning is crucial – there is a culture of reflect, learn and improve. Outcomes are used to prompt learning, which is then applied to future investments. Some of the questions that the team considers, are whether it has used the right form of capital to enable the change it was seeking, whether it is taking enough or too much risk, and how it can better support its portfolio.
- One of the lessons that Esmée has learned with the benefit of having started back in 2008, is the inflexibility of some loan structures, and especially the need to be flexible in the early years of an investment. It now counts just 8% of its capital in debt products with fixed terms.
- Esmée often shares its learning with the market, providing reports and insights that can be useful for new and existing social investors, as well as foundations interested in social investment. For example, Esmée has reported back on what it has learned over the last five years in place-led funding, its first perpetual bond structure, and has also commissioned and shared research (e.g. impact-linked finance).

Creation and structure

The Esmée Fairbairn Foundation was founded in 1961 and is one of the UK's largest independent grant-makers and social investors. Its three main aims are to improve our natural world, to secure a fairer future, and to strengthen the bonds in communities in the UK.

It is one of the first UK foundations to formally make social investments (alongside traditional grant-making), following a £45m carve-out in 2008. Its small investment team leverages expertise both within and outside the foundation.

Esmée is known for being innovative and catalytic, leveraging in funding from other investors, often willing to be more risk-tolerant than other investors, and providing its investees with appropriate forms of capital that are patient, flexible and concessionary.

Its social investment strategy is designed to contribute to its impact goals and focuses on three objectives: 1) impact-first direct investments; 2) influencing the social investment market; and 3) learning and sharing.

Outcomes

The team typically invests c£5m per year and has made over 150 social investments since 1997. With its impact-first approach, Esmée's financial objective is to break even across its portfolio, which is made possible as overheads are covered centrally. Its culture, structure and funding have allowed Esmée to take on more risk than other social investors, providing capital that is often more patient, concessionary and flexible.

Historically, Esmée's social investments have generated a 2% return across 93 exited investments. More important for Esmée, is the significant impact it has delivered..

Case Study Nine - Social purpose organisation case study

Ethex and Energise Africa – the benefits of catalytic capital to drive innovation and growth

Ethex's and Energise Africa's mission	Provide a marketplace for purposeful organisations operating in the UK (Ethex) and Africa (Energise Africa – EA) to raise investment from individuals (i.e. crowdfunding from retail investors).
Why is the funding catalytic capital?	Energise Africa obtained financing in two forms. A contract for services (£750k), which provided start-up finance from UK Aid (managed by E4I) and a pot of highly catalytic investment finance that was flexible, risk-tolerant and concessionary. This investment was endowed to Energise Africa as a grant and was of a sufficient size to avoid repeated smaller capital raises. Funding has been used for match funding, first-loss and scale-up activities. In parallel, P4G supported EA through significant grants through its start-up and scale-up programme and is looking to an equity round under P4G's new (and as yet unannounced) P4G invest scheme. Ethex received development grants to establish itself. However, in general funding has not been sufficient to avoid repeated capital raising. Funding has been less flexible than Energise Africa received (though the threshold for capital repayments has been increased). Most foundation investors provided patient capital (ten years).
Year established	Ethex: 2010 (platform launched in 2013). Energise Africa: 2016 (platform launched in 2017).
Investee entity type	Ethex: not-for-profit social enterprise (company limited by guarantee). Energise Africa: for-profit social enterprise (company limited by shares.
Impact focus	UK and Africa, across all industry sectors.
Investment instruments	Ethex: loans. Energise Africa: grants.
Investment size	£650k in total funding for Ethex. Energise Africa: £650k P4G and £2.5m UK Aid grant (excluding initial contract for services).
Source(s) of investment	Ethex: Foundations and BSC Energise Africa: Virgin Unite, UK Aid, P4G Partnerships
Investment terms	Ethex: loans included a minimum revenue level that triggered capital repayments. ten-year terms. Typical 6% interest rate. Currently being renegotiated. Energise Africa: Grants with business and impact targets.

Key points

Ethex launched in late 2013 as a platform for UK retail investors to buy or sell shares in ethical non-listed companies. The model quickly shifted to helping raise money for organisations, whether that was equity, debt or other forms of financing, and now offers both services. Sister platform Energise Africa was set up by Ethex and Dutch crowdfunding platform, Lendahand, in 2016 to focus on social enterprises and profit-for-purpose organisations operating in Africa.

1. The two platforms are exemplars of the impact catalytic capital can have on the growth and development of social purpose organisations.

- Technology companies like Ethex and Energise Africa often require significant upfront investment (to build platforms and architecture) and the path to breakeven and sustainability can be lengthy. Therefore, 'tech for good' business models typically require risk-tolerant, flexible, long-term patient funding at scale.[30]
- As a not-for-profit company limited by guarantee, Ethex's legal structure prevented it from raising equity, which would have offered the requisite patience and risk tolerance. Its first social investment came from loans from several foundations and other institutional investors. The loans were structured so that the principal was repaid only if revenue was above a certain level. While this was positive and allowed a degree of risk sharing, Ethex found that it was unfeasible to scale up and repay capital when the revenue trigger was reached. It had to restructure the revenue trigger point for repaying capital, as well as later secure a repayment holiday. The debt it received was patient (ten-year term) and while there was some flexibility in the instrument, it was not sufficient for Ethex's needs.
- While there were elements of catalytic capital in the funding that it had received, it was insufficient to take the business model to sustainability. When Ethex has sought further funding, debt has been the instrument on offer. But after lengthy due diligence processes, loans have been rejected by potential funders' investment committees due to perceived risk of piling 'debt upon debt'. Having to repeatedly obtain or renegotiate funding has been a distraction for management and impacted growth.[31]
- In comparison, the Energise Africa platform was set up as a company limited by shares, enabling the organisation to raise equity. Moreover, it has been well funded with appropriate funding from the outset that was highly flexible, concessionary and risk tolerant. Energise Africa received funding from Virgin Unite and UK Aid to help with platform set-up, as well as funds to invest as match funding or provide a first-loss layer for projects on the platform. This funding was later endowed to Energise Africa. While the endowment came with conditions, it can be used flexibly and is of a substantial size, helping Energise Africa avoid a constant cycle of seeking further finance, and being able to adapt to a fast-moving external environment.
- Energise Africa has gone on to secure concessionary finance in the form of a recoverable grant from P4G Partnerships, to build out new services on its platform (e.g. currency hedging and local currency lending). The flexible funding had an original term of two years but was extended for a further two years and came due at the end of 2022. The tangible impact of the platform with over £30m deployed across 15 African countries has led to EA being an exemplar for UK Aid and P4G. It will now rebrand as Energise Earth and expand to fund more impactful organisations across other regions.

2. Ethex and Energise Africa have helped facilitate significant new funding to UK and African purposeful organisations from an untapped source.

- Ethex currently focuses on social enterprises and activities in the UK, while its sister platform focuses on Africa. The two platforms have collectively raised more than £130m of social investment for impactful organisations, representing an impressive 154x leverage.
- Not only have the platforms leveraged in significant funding for purposeful enterprises, but this funding also represents an untapped, new source of funding for the social sector (retail investors).
- Crowdfunded retail money invested via the platforms tends to be patient (eg ten to 15-year terms for loans are common), often at concessionary rates (0-3% rates are common), and risk-tolerant (often funding very early-stage ventures, and largely unsecured).

Outcomes

By 2020, Ethex and Energise Africa had raised more than £130m combined for purposeful enterprises across more than 200 projects via a network of over 20,000 retail investors. More appropriate capital for Ethex could potentially have driven even greater social impact. In contrast, the more favourable and generously sized funding for Energise Africa has allowed management to take risks, such as its project to build new currency hedging and local currency lending services, which have benefited the business and are delivering impact.

Case Study Ten - New investment fund case study

The Fair by Design Fund

Ethex's and Energise Africa's mission	The Fair by Design Fund, managed by Ascension, was set up to invest in scalable companies tackling the 'poverty premium'. An estimated 14.3 million people (22% of the population) in the UK are living in poverty. People in poverty or on low incomes pay on average £490 more each year for the same goods and services as people who are better off financially. For one in ten, this number is at least £780 and some low-income households can end up paying in excess of £2,250 per year when high cost credit comes into the equation. This is the 'poverty premium' – the extra cost of being poor. It's a real and unfair problem, worth over £3.8bn per year in the UK alone. The fund achieves its mission by investing in early-stage, highly scalable technology businesses working to reduce costs across key sectors: energy, financial and digital inclusion, food/health and household, mobility and insurance. It looks for innovations that can scale commercially to the pace and scale of typical venture-backed business, while tackling both the drivers and effect of the poverty premium.
Why is the funding catalytic capital?	Wholesale investment into the fund was both risk-tolerant and patient. While the fund had a clear investment thesis, the concept was unproven – involving an element of uncertainty on the types of business model that would make up the portfolio, and therefore making it hard to predict the return profile. The focus on early-stage, equity investment also increased risk as compared to many social investment funds. The fund was a case study of how a partnership-driven model focused on a clear thesis can galvanise support beyond capital (several LPs have since then opened commercial routes to market for the portfolio). In addition, the fund's pre-seed stage investment helped bring early-stage innovations to a point of traction sufficient to attract subsequent commercial co-investment from downstream investors. The fund's catalytic role was twofold in those cases: 1) it provided for a higher level of risk for very clear, relevant impact propositions which the investment team believed could scale commercially with funding support; and 2), for those pre-seed rounds that were competitive, it allowed the fund to introduce the idea of the impact mission in the founders' brand and value proposition much earlier in their investment journey, thereby influencing the direction of the business in terms of the audience served.
Year established	November 2017 with a ten-year term (deployment started in January 2018)
Sources of capital	Big Society Capital and the Joseph Rowntree Foundation provided £8m, which was the cornerstone of the initial fund, with the team raising another £2m via a second close (including Social Tech Trust, Bank Workers Charity, Barrow Cadbury Trust, Comic Relief, Merchant Taylors Livery Company, Trust for London and HNWIs). A fund extension in 2020 welcomed Nation-wide Building Society as a new cornerstone investor along with the Esmée Fairbairn Foundation and Edinburgh University. The fund has a total of 14 limited partners.

The Fair by Design Fund

Fund size	£14.7m of which £5m was provided by one of the cornerstone investors, BSC. In 2020, BSC then topped this up by £1m to a total of £6m.
Investment instruments	All investment into the fund can be considered catalytic capital. The fund was able to provide equity and debt, however based on the investment propositions seen so far, the team decided to focus on equity instruments only, given the type of risk/return profile of the deal flow presented to it. The fund invests at pre-seed and seed, and follows on as appropriate to Series A. In some cases, equity is provided through convertible loan notes.
Investment size	Average investment size over the life of the fund to date is £400k, with an expectation that the fund will participate in multiple rounds of fundraising. Initial average investment size is £280k.

Key Points

Research originally commissioned by the Joseph Rowntree Foundation[32] found that on average, low-income households pay an extra £490 a year for basic goods and services. This additional cost was termed the 'poverty premium' and the foundation set about building a coalition of partners to eliminate it. The result was the Fair by Design venture fund and accompanying campaign. The fund aims to remove this additional cost by funding high-impact scalable technology ventures; the campaign creates awareness and advocates for changes in policy and regulation.

The multi-sector partnership works across four pillars:

- Ascension, which has a considerable track record in venture investing and venture ecosystems, manages the fund.
- Barrow Cadbury campaigns to influence policy and regulation, as well as to build public support.
- Toynbee Hall embeds the views of experts with lived experience into the investment process.
- Comic Relief supports the team on roadshows to build awareness of key innovations among regional decision-makers.

1. Catalytic capital was critical in establishing the Fair by Design Fund. The Fair by Design Fund's theory of change was clear and indicated significant impact potential, while research into potential investees highlighted demand for this form of capital. That said, the innovative nature of the fund meant there was less evidence as to the fund's ability to generate market-based returns. This was compounded by the fact the fund planned to invest in early-stage social ventures, a market that is inherently risky. The fund therefore required risk-tolerant capital to prove its financial viability and ability to generate sufficient returns.

The fund invests primarily through equity investments. This is necessary, given the early-stage nature of the ventures and their need for flexible patient capital. The wholesale investment into the fund therefore had to be patient and flexible.

2. The well-evidenced impact thesis helped attract a range of catalytic capital investors. The Fair by Design Fund and accompanying campaign had a very clear, well-evidenced theory of change. Impact is measured by the reduction in the poverty premium for each venture, and how many lower-income consumers are benefiting

from the reduction in that poverty premium. It is not possible for all catalytic capital funds to have such simple and clear outcome metrics. However, the clarity of the fund's mission and clarity around venture level outcomes were undoubtedly helpful in pulling together an impressive coalition of partners and funders.

The ambitious nature of the fund in targeting the elimination of the poverty premium, was also likely to have stirred the imagination of potential partners and inspired collective action.

3. The fund highlights the value of systems thinking when designing or making catalytic capital funds or investments. The Joseph Rowntree Foundation and its partners, many of whom have decades of experience tackling poverty and social issues in the UK, identified the need for a holistic systems approach to tackling the poverty premium. Multiple workstreams were identified that would support one another to maximise impact. The approach included: ensuring effective representation for those with lived experience to validate the solutions of potential investees and provide insights throughout the investing and portfolio management process; raising awareness of the poverty premium to encourage new market entrants and behaviour change from large existing providers, for example advocating for social energy tariffs; and advocating for regulatory change.

Outcomes

As of Q2 2022 the fund has invested in 23 companies, benefited1.7m people, and delivered £203m of savings annually for low-income households.

Investees include Wagestream, a financial wellbeing app, marketed to employers, which provides employees with the financial tools to achieve financial resilience through budgeting, streaming, learning and saving features, and Kettel Homes, which helps people build the required deposit and credit history to buy a home.

Big Society Capital's investments into the charity bond market

BSC's mission within the charity bond market	Big Society Capital sought to support the growth of the charity bond market, by creating a backstop facility for charity bonds managed by Rathbones, to encourage more issuances and build an exemplar fund to highlight the financial and social value of charity bonds.
Why is the investment into the fund catalytic capital?	BSC's investment aimed to stimulate growth in the charity bond market by reducing real and perceived risk. BSC's capital reduced the risk of bonds failing because they did not reach their fundraising target, while at the same time reduced the perceived risk of charity bonds by successfully investing in them and creating a financial track record for charity bonds.
Year established	2013
Sources of capital	Big Society Capital and capital from Schroder BSC Social Impact Trust
Fund size	Total current commitments from BSC £32.4m, peak commitments from BSC £50m pre-pandemic.
Investment instruments	BSC funds are invested in charity issued bonds that are typically five to ten years in duration with a 4.01% average yield. Proceeds are primarily used for large infrastructure projects.
Investment size	Average charity bond issue size £10.7m – average investment into a charity bond issue made by BSC £1.5m.

Key Points

Since the first charity bond was launched by Triodos for Golden Lane Housing in 2003, the market has grown to an estimated £440m and now attracts a diverse range of investors, including pension funds and wealth managers. Today charity bonds are recognised as an investment that provides both risk-adjusted returns and social impact; however, this was not always the case.

BSC was instrumental in growing the charity bond market

As with many new instruments, charity bonds suffered from a lack of investor understanding and awareness in the early years of their development. Consequently, it wasn't until 2011 that a second was issued. BSC identified the financial and mpact potential of charity bonds and sought to catalyse further investment into the market by:

- Proving the financial viability of charity bonds – BSC through its charity bond portfolio sought to build an exemplar track record, to demonstrate the perceived risk of charity bonds was higher than the actual risk. BSC initially assumed a 7.5% overall rate of defaults, given the lack of historic data, however the current real default rate has been just 2.9%.
- Charity bond issuances average £10.7m per issue, are funded by multiple investors and are typically used for infrastructure projects. In the early stages of the market there was therefore a risk that issuances might fail if they could not attract sufficient investors. BSC's capital was used to create a backstop facility, to give confidence to both issuers and investors that bonds will reach their target.

Outcomes

The primary outcome of BSC's wholesale catalytic capital investment into the charity bond market, has been to support significant growth in the market from £5.4m in 2012 to £440m in 2021. Intermediaries including Triodos and RCB Bonds have also been instrumental in attracting a range of new investors. New investors include pension funds, retail investors and wealth managers, many of whom are conservative in their approach to financial risk. Given the flow of new capital into the charity bond market, BSC's capital is now rarely needed to support bond issues, and some bonds are even oversubscribed.

The range of charities issuing charity bonds has also grown. While most issuers of charity bonds support disadvantaged communities and individuals, some, such as the Canal & River Trust, serve a broad base. Most charity bonds, by value, have been issued by organisations in housing (55%) and physical health (14%).

Case Study Twelve - New investment fund case study

Schroder BSC Social Impact Trust plc (SBSI)

Schroder BSC Social Impact Trust's mission	The Schroder BSC Social Impact Trust aims to deliver measurable positive social impact, as well as long-term capital growth and income. Through a diversified asset allocation, it seeks to provide low correlation to traditional quoted markets, while addressing significant social issues in the UK.
Why is the investment into the fund catalytic capital?	The trust was designed to provide access to high-impact private markets, investments not available to individual investors in public markets, including closed funds, secondary and co-investment opportunities. In recognition that individual investors increasingly want their money to have a positive impact on society, Big Society Capital partnered with Schroders – and provided a seed portfolio of investments – to create a publicly listed investment trust that democratises access to these high-impact opportunities. Ultimately aiming to attract and enable a new pool of investors. While the trust targets market returns, the fund's initial investors took on the greater risk associated with a new IPO in order to help catalyse the significant impact achievable by scaling the trust over time.
Year established	The trust began investing on 22 December 2020.
Sources of capital	The trust was seeded with an initial portfolio of Big Society Capital investments and investment from Schroders and Cazenove. The trust raised £75m at IPO in December 2020. In November 2021 the trust raised a further £10.8m through a share issuance to a mix of new and existing shareholders. Shareholders of the Trust now include wealth managers, a local government pension scheme, a donor advised und, designated Impact funds, family offices and multi-asset managers.
Fund size	As of 30 June 2022, the trust's net asset value was £89.9m.
Investment instruments	The trust invests in a diversified portfolio of private market impact funds, co-investments and direct investments. The trust invests primarily in three asset classes that were selected to give a diversified set of opportunities: • debt for social enterprises • high-impact housing • social outcomes contracts
Investment size	As of 30 June 2022, the Trust was fully committed to high-impact assets across ten investments – eight direct holdings in funds and two portfolios of investments (a portfolio of nine charity bonds and a portfolio of co-investments in three enterprises). Investments range from c£4m to c£15m, with the Trust's largest investment in Bridges Evergreen Holdings – a patient capital vehicle that makes equity and quasi-equity investments into highly impactful businesses. Investments that are committed but not yet drawn by private market funds are held in listed liquid ESG investments, to mitigate cash drag during longer drawdown periods. As of 30 June 2022, c20% of the trust's assets (£16.8m) was held in liquid ESG investments.

Key Points

1. The need for a listed impact investment product. In designing Schroder BSC Social Impact Trust, Big Society Capital – the portfolio manager – considered there to be market recognition that social impact is better delivered investing in private markets. There was also recognition that investors increasingly seek a positive impact on society with their investments – a survey by Schroders found this to be the case for 70% of investors.

However, access to private market impact investments often means having to access limited partnership fund structures, and this is a genuine barrier for retail and private investors, as well as many UK wealth managers and financial advisers. There is also limited investment expertise in private market impact investing, with investors facing high minimum investment constraints, prohibitively long ramp-up periods and concentration risk.

In light of this, Schroder BSC Social Impact Trust is intended to provide a new and unique proposition, opening access, with a liquid vehicle, to private impact markets for wealth managers and advisers in the UK. By overcoming some of the barriers to high-impact private market investments – such as long ramp-up periods, minimum ticket size, the governance burden of managing drawdown requests – the trust aims to attract new investment from a wider pool of investors previously unable to access this market. While the trust targets market returns – the fund's initial investors, of which Big Society Capital was the lead, took on the greater risk associated with a new IPO, to help catalyse the significant impact achievable by scaling the trust over time.

Outcomes

As of 30 June 2022, the trust has raised £89.9m from wealth managers, donor-advised funds and local government pension schemes – fully committing this capital across ten impact investments.

The trust has financed 160 organisations, benefiting more than 160,000 people, at least 90% of whom are disadvantaged and vulnerable.[34]

Reall Limited – transition to a replicable catalytic capital model to maximise impact

Reall's mission	Reall's remit is to build climate-smart, affordable homes in Africa and Asia (with five focus countries – Pakistan, India, Nigeria, Kenya and Uganda), and to stimulate markets for climate-smart affordable housing.
Why is the funding catalytic capital?	Highly flexible funding with loans converted to grants in certain cases (e.g. very significant depreciation of local currency in which the loan has been made) and concessionary interest rates. A small number of grants in the funding mix also deliver concessionary funding. Loans are risk-tolerant, not just because of the operating conditions of the countries within which they are given, but also because loans are provided in local currency, exposing the investor to currency depreciation.
Year established	Reall Limited was established in 1989 as Homeless International, and over the last decade has transitioned to providing loans from non-repayable grant funding.
Investing entity type	Registered charity (company limited by guarantee)
Source(s) of capital	Foreign, Commonwealth & Development Office (FCDO), and Sida (Swedish International Development Cooperation Agency)
Fund size	Currently cUS$40m loan book. (Since 2001 it has funded $53.4m loans and $22.5m grants across 170 projects.)
Investment instruments	Secured loans, which can be amortising (repaid regularly over the life of the loan) or bullet (repaid in full at the end of the life of the loan), depending on the context of the project. A small portion of funding is via grants (in recent years, less than 5%).
Investment size	Based upon Reall's risk certification of an organisation: up to £500k for a 'basic' organisation, up to £3m for an 'intermediate' organisation, and up to £15m for an 'advanced' organisation. The largest single investment made to date is £5m.
Investment terms	C6-7% interest rate (well below commercial loans in the target geographies), three- to five-year terms, secured against land and property.

Key Points

1. Transformation from grant funding to catalytic capital investment over the last decade. Historically, Reall provided grant funding to civil society organisations for affordable homes projects, n an attempt to help these organisations become more commercial, but this proved challenging. Over the last decade or so, Reall has transitioned to providing investment in the form of loans (grants are less than 5% of the funding mix now) to private sector social enterprises to build and sell climate-smart, affordable homes (average construction cost of US$14,250 per home in the last five years). The transition to largely repayable finance allows Reall to recycle capital and fund further projects to maximise the impact of its catalytic capital.

2. Stringent operating and investment processes ensure the efficient allocation of scarce catalytic capital. Reall identifies partner organisations via a due diligence process (including fraud, financial and anti-terrorism checks). Organisations that pass due diligence are certified as basic, intermediate or advanced, given their track record and other attributes. Once an organisation becomes a certified partner, it can then apply for funding. Reall has stringent criteria for approving investments – projects must be sustainable, commercially viable and meet stringent non-financial criteria to ensure the creation of high-quality, resilient and affordable housing stock. All houses must be EDGE Certified,[35] accompanied by essential services (energy, water, flushing toilets etc), and have tenure and land title deeds passed over once loans are repaid.

Implementing partners operate a pre-sales model, where they collect data on clients before a project is completed, to help assess a buyer's likely behaviour once they have acquired their property. Partners include clauses in sales contracts that ensure properties remain part of affordable housing stock. Anecdotally, home buyers tend to be of a view that it had been such a struggle to get the home and it is so precious to them, that they are unwilling to sell.

In 2018, Reall introduced an eight-step assurance framework – an important part of which is monitoring projects and investments. Reall undertakes annual assurance visits, which look at the quality of homes as well as assessing the financial management of the investees. Of its existing c$40m loan book, approximately half are bad debt provisions of 5% or less, while the other half are problematic and may be converted to grants. All problematic projects pre-date the introduction of Reall's eight-step assurance framework. Problematic loans are managed by a specific department at Reall, which helps to transition the loan towards an exit. When an investee has been acting in good faith, a plan is developed to find an exit, demonstrating the flexibility of the capital that has been provided. Assets can be liquidated, land developed, or alternate contractors can be brought in to finish projects.

3. Investments are highly risk-tolerant, flexible and concessionary.

- While loans are secured against specific land and assets, they are highly risk-tolerant – Reall operates in countries where the risk premium is higher. It has lawyers and teams in each country within which it operates, to liaise with central banks and ensure local legislation is followed, helping ensure funds can be recycled or repatriated. Reall lends in local currency, thereby taking exchange rate risk when any loan repayments are repatriated.
- Funding is very concessional, with interest rates of c6-7%, as compared to local commercial funding rates of above 10%, e.g. Nigeria c16%, Ghana c22%.
- Reall's investments are flexible, especially with circumstances outside the control of the investee. For example, Reall has converted loans to grants where there has been very significant depreciation of local currency. Reall has a credit control department that works with organisations to help them meet their repayment schedules, and to provide necessary adjustments, such as pausing interest repayments during Covid-19. Flexibility is offered only to those partners that have acted in good faith.

4. Outcomes – Reall is proving a model for affordable homes that can be replicated. Reall has built c5,000 homes in the last four years (with over 25k people housed), is creating a model which can be replicated, and is helping strengthen local markets to deliver high-quality affordable housing at scale:

Reall's track record has proved to local banks that mortgages for quality, climate-smart affordable housing are viable. Reall has even partnered with banks to ensure those purchasing affordable housing from Reall investees have access to affordable financing. This not only improves the commercial viability of a project (with a ready means for the homes to be sold once they are complete), but also develops the mortgage markets in operating countries.

Many of Reall's investees have been able to build on their track record with Reall financing, to attract further finance from development finance institutions and commercial loans.

Creation and structure

Reall was established in 1989 (originally called Homeless International) to help alleviate poverty in the emerging markets. In 2001, it launched its CLIFF programme, which unlocked low-income housing at scale through community-led infrastructure partnerships with governments and private developers, firstly in India and then across Africa and Asia. Reall has evolved to focus on a market-based approach, helping not only to build affordable, climate-smart homes via investment in a network of housing developers, but also to broker solutions that unlock markets (e.g. helping banks to develop mortgages for affordable homes).

Reall was funded with grants from the UK's FCDO, and that funding is permitted to be loaned to social purpose organisations for building affordable homes, and the capital that is returned can be recycled for further loans. Since December 2020, Sweden's Sida has provided grant funding to Reall, which can also be used for loans, and can also be recycled, but any recycled funds must be used for projects on the same conditions as the capital was originally loaned.

Case Study Fourteen - International case study

Buen Vivir Fund – collaboration and flat power structures in the deployment of catalytic capital

The Buen Vivir Fund's mission	The Buen Vivir Fund aims to support the needs and aspirations of grassroots groups led by Indigenous Peoples, youth and women that are building the next economy, while at the same time enhancing climate resilience.
Why is the funding catalytic capital?	Investment decisions are made by a Members Assembly, comprising equally investees and investors, focused on funding community projects to maximise impact. Funding is a mix of grant and loans (concessionary). Loan capital must be repaid, but there is no interest payable (instead investees self-determine a pre-agreed 'aporte' payment, to be made if their project is successful). Terms are flexible – investees acting in good faith that cannot make repayments have their payment terms restructured or the loan written off.
Year established	2018 (following inception of the idea in 2016)
Impact focus	Indigenous Peoples, youth and women in Latin America, North America, Southern Africa and South Asia, with a focus on driving impact for all.
Investing entity type	Fund
Source(s) of capital	Eight US-based foundations each committing at least US$12,500 grant capital and $125k investment capital.
Fund size	$1m
Investment instruments	Loans and grants (average mix of 21% grant and 79% loans)
Investment size	$60k average across first nine investment projects.
Investment terms	Loan capital is repaid but 0% interest is required. Instead of interest, investees self-determine an 'aporte' payment to be made if their project succeeds.

Key Points

1. The fund has a collaborative, participatory governance structure with equal roles for investors and investees, which helps to promote the efficient deployment of catalytic capital. The first market gap that the fund was set up to address was the lack of participation of the beneficiaries of impact investment. Thousand Currents, an international NGO based in the US, set up the fund in a way that challenges typical investing power dynamics and economic norms. The fund is governed by a Members Assembly, rather than a board of directors, with investors and partners taking equal roles in decision-making. The Members Assembly comprises ten grassroots partners, eight institutional investors (principally foundations) and one representative from Thousand Currents. Some of the features of the fund's governance and operating model are:

- The fund had two criteria for organisations to be part of the Members Assembly – those whose current work included a focus on alternative economic or financing practices, and those with existing relationships to Thousand Currents or strongly recommended by trusted contacts. Of the ten grass-roots organisations, nine were established Thousand Currents partners.
- The fund invests in grassroots partners, which in turn invest in community-led processes for social change and 'good living' (buen vivir). For example, EduPaz is one of the fund's ten grassroots partner organisations. The Buen Vivir Fund has invested in EduPaz's UMA Fund, and the UMA Fund in turn uses loan capital to finance rural producers to create small enterprises (eg coffee and chicken co-operative businesses).
- Investment applications are reviewed by three to five peers from the Members Assembly. The first step in the investment due diligence process is to evaluate whether the proposed investment is coming from a real community organisation with the will of the community behind it, and that will help the community to become more self-determining and achieve autonomy.
- The Members Assembly prefers all decisions (relating to investment and investment terms, conflict resolution, strategy and membership) to be by consensus of all members. If consensus cannot be reached, decisions are made by majority vote with each member having one vote. Given the make-up of membership, investees in aggregate have a majority.

2. Investment terms exemplify catalytic capital. The second market gap that the fund sought to address, was that despite the increasing diversity of investees, the terms upon which they received social investment were similar. Investments of the fund have the following features:

- Patient, flexible and concessionary – all investments receive a combination of initial grant, investment (to date, all investment has been debt), and multi-year grants that help to support ongoing operating costs of projects.
- Terms are highly concessionary and risk-tolerant, requiring a return of capital but no return on capital (ie 0% interest), so that investors shoulder more of the financial risk. Instead of fixed interest being paid, investees pay a voluntary 'aporte' payment. This is a pre-agreed amount which the investee has determined should be paid upon successful completion of their project. The amount varies by project, but is typically 2-15%. The purpose of the solidarity payment is to benefit future investees and the communities they serve, by passing any growth achieved forward, increasing the available capital for future investment.
- Legal enforceability of investment agreements ensures capital is flexible. Agreements are not designed to be enforced in courts, and instead specify that disputes are resolved by the Members Assembly. If, for example, an investee fails to repay, under its guiding principles, the Members Assembly will determine whether the investee has acted in good faith with conditions outside the investee's control. If the investee has acted in good faith, either repayments will be restructed, or the loan will be written off entirely.

Creation and structure

The Buen Vivir Fund was established in 2018, having been co-designed by Thousand Currents together with donors, grassroots partner organisations and advisers. It was designed to provide a long-term resource for grassroots groups worldwide to create economic initiatives that challenge the economic norms of impact investing, and prioritise buen vivir. 'Buen vivir' is a way of living that is in balance with the natural world, community and generations of the past, present and future.

Outcomes

The fund is currently invested in grassroots groups in Mexico, Guatemala, South Africa, Nepal and India. Its nine projects have been in areas as diverse as housing, healthcare, environmental and climate protection, and small business development for artisans and farmers. Projects collaborate with local communities, and many focus on restoring or preserving Indigenous sovereignty as well as women's rights and leadership. The aportes mechanism with the idea of passing growth on to the next project allows for continued recycling of catalytic capital, while the Members Assembly and governance mechanisms ensure this scarce capital creates the greatest impact possible, with its focus on holistic benefits to communities.

Case Study Fifteen - International case study

Impact-Linked Fund for Gender Inclusive Fintech – Impact-Linked Finance at work

Impact-Linked Fund for Gender Inclusive Fintech's mission	The Impact-Linked Fund for Gender Inclusive Fintech (ILF for GIF) aims to improve financial inclusion for women in Sub-Saharan Africa, Asia, Middle East and North Africa. The fund supports women-led fintechs and gender-inclusive fintechs, increasing cost-effective access to financial services for women. Financial inclusion has been shown to increase female empowerment, decrease extreme poverty and have a positive effect on education, healthcare and nutrition.
Why is the funding catalytic capital?	Financial incentives linked to achieving social outcomes are paid directly to fintechs or embedded in investment terms (lower interest cost), effectively lowering the cost of finance. Investments are risk-tolerant, targeting marginalised women with new or early-stage financial technology products and services. Social outcomes are designed on a case-by-case basis, and in collaboration with the investee.
Year established	2022
Investing entity type	Fund
Source(s) of capital	Swiss Agency for Development and Cooperation (SDC), Austrian Development Agency
Fund size	US$13.4m at first close in March 2022 (target fund size $21m)
Investment instruments	Social impact incentives (SIINC), impact-linked loans, impact-linked convertible loans, impact-linked revenue share agreements, impact-ready matching funds
Investment size	$500k to $5m per transaction
Investment terms	Financial incentives of up to $200k to $1m per investment are provided to investees who have achieved predetermined social impact targets. Incentive payments may be paid directly to the investee or embedded in investment terms (e.g. interest rate reduces according to how much impact is achieved, and potentially results in a negative interest, meaning less than 100% of capital needs to be repaid).

Key Points

1. Tailored approach to catalytic capital – the ILF for GIF provides highly targeted catalytic capital, with financial incentives paid to investees achieving pre-determined social impact targets. The fund is managed by Roots of Impact (a specialised advisory firm pioneering impact-linked finance) and iGravity (advisory and investment management firm). It aims to improve financial inclusion for women in developing economies by growing women-led and gender-inclusive fintechs (such fintechs have been shown to more consistently target female customers). In turn, financial inclusion has been shown to increase female empowerment, decrease extreme poverty and have a positive effect on education, healthcare and nutrition. The ILF for GIF achieved its first close of US$13.4m in March 2022:

- The ILF for GIF provides financial incentives to investees, while crowding in private sector investment through impact-orientated investment manager partners (including Bamboo Capital and Women's World Banking Asset Management). Partners will invest $500k to $5m per deal in women-led and gender-inclusive fintechs. The ILF for GIF then provides targeted financial incentives of $200k to $1m per investment, which 1) incentivise fintechs to tailor their solutions to the needs of marginalised women, and 2) for fintechs already focusing on gender, boost their revenues and profitability, helping to attract additional investment to scale and increase their impact. These incentives ensure capital is provided that is concessionary (payments increase revenue, or interest costs are reduced), and allow investees to focus on less-developed products and services (ie risk-tolerant).
- Capital is flexible – the impact incentive structure is bespoke and designed in partnership with the investee to reflect their context, and in doing so, maximises impact additionality and aligns incentives. Target outcomes could include improved financial literacy and stronger financial health of female clients, vulnerable women served as a proportion of total client base, and livelihood improvements for female clients.
- An independent verifier ensures that all impact data collected and consolidated is correct. Incentive payments may be made directly to the fintech or embedded into investment terms. Initially incentives will be in the form of premium payments or social impact incentives (SIINC) made directly to fintechs. After the initial phase of the fund, incentives will also be embedded into investment terms (e.g. interest rate reduces depending on the scale of outcomes achieved), including impact-linked loans, impact-linked convertible loans, impact-linked revenue share agreements and impact-ready matching funds.

2. ILF for GIF is aiming for $100m of blended finance being made available to investees. In the long term, the ILF for GIF aims to become a fully-fledged blended finance fund. For this fund, philanthropic funders will provide capital in two ways: 1) non-repayable grants to fund outcomes; and 2) a dedicated first-loss funding tranche. The combination of the two is expected to attract funding from the private sector and development finance institutions and allow for increased deployment of catalytic capital.

Creation and structure

The ILF for GIF secured $13.4m in a first close in March 2022 from the SDC and the Austrian Development Agency. The fund is expected to reach $21m at the final close. As a first-of-its-kind fund, it will share its research and learnings to provide a blueprint for other gender-smart financing solutions and impact-linked finance structures. It will work with ecosystem enablers including incubators/accelerators, venture builders and intermediaries, that are specifically focused on marginalised women (e.g. Women's World Banking and Village Capital).

The ILF for GIF will invest in investment-ready, early- to growth-stage fintechs that meet at least one of the 2X Challenge Criteria (e.g. 51% or more women ownership), with high (additional) impact potential and a corresponding growth plan. Fintechs must be willing and able to measure impact metrics (with support). Special focus will be given to fintechs with the ability to serve vulnerable women, such as migrants.
In addition to providing investment funding, technical assistance funding is being made available to fintechs and ecosystem enablers to help with impact measurement and management (with measured impact to be independently verified before financial incentives are paid out to investees).

Outcomes

Gender-inclusive fintechs accounted for just c1% of total fintech capital raised in 2019, according to the Center for Financial Inclusion. Since it began to be measured in 2011, the gender gap for financial inclusion has remained constant in developing economies (whereas it has narrowed in developed economies). Many fintechs tend to focus on targeting early tech adopters, largely perceived to be men, unintentionally ignoring the needs and preferences of female clients. The ILF for GIF is targeting the closure of this gender gap, by accelerating cost-effective and convenient access to financial services for women.