

Committee:	Date:	Item No.
Social Investment Board	18 th September 2013	
Subject: Progress Report	Public	
Report of: Chief Grants Officer	For Decision	
<u>Summary</u>		
<p>This paper provides an update on your Fund's dispersal rate since it was established in October 2012.</p> <p>It introduces a longer paper on options for a high-risk, high-impact social investment fund and how this may help you achieve your aims.</p> <p>It provides details of running costs incurred so far in management of your Fund.</p> <p>Recommendation:</p> <p style="padding-left: 40px;">That you receive the report and note its contents.</p> <p style="padding-left: 40px;">That you authorise officers to prepare a paper to Common Council reporting on the first year of your Fund</p>		

Main Report

Disbursal Rate

1. When Common Council approved the aims and objectives of the City of London Corporation Social Investment Fund (hereafter 'the Fund') it agreed a target dispersal rate of £2m by end of October 2013. You have already made £1.3m of investments, and today's meeting recommends a further £800,000 - £1m for your approval.
2. Depending on the outcome of today's meeting, and the ability of investees to meet your conditions, you could slightly exceed the target dispersal rate and you may wish officers to prepare a short update to Common Council reporting progress made to date. A similar dispersal rate for likely for the second year of your Fund as the market continues to 'warm up'.
3. It is taking time to generate deal flow and, as noted in your 20th June meeting the investment pipeline shows a large number of opportunities which are not yet ready for Board consideration. This reflects a market which is still at an early stage of development and should not cause concern. Some commentators have drawn comparisons between dispersal rates in social investment and that of pioneering venture capitalists such as Apax Partners who took twelve years to reach £10m under management.

4. Officers are examining the most promising proposals for both direct and indirect investment opportunities. Where investment funds are brought to your meeting, accompanying papers will examine fee structures and the degree to which the investment fund can report on the underlying assets they invest in. Based on experience to date, it can take several months between first contact with the Fund and receipt of a final investment proposal.

High Risk-High Impact Allocation

5. Further to the request at your meeting on 20th June 2013, today's papers include options for allocating funds for high risk, earlier stage, and potentially high impact investments that may not be secured by assets.
6. Your Fund has been welcomed by peers in the social investment market and has generated favourable comment from several mainstream financial institutions. The City of London's active role as a social investor is helping to achieve the Corporation's goal of establishing London's position as a global hub for social investment.
7. One of the objectives of your Fund is to develop the social investment market. As of September 2013 the market is very much a work in progress. Whilst progress has been made in terms of the supply of social investment finance, much more work is needed in order to attract a wider range of investors (both institutional and individual), expand the pool of investment-ready products, improve deal-sourcing facilities, and strengthen the quality of market data.
8. Social investment in the UK is currently characterised by high transaction costs, an absence of standardised products and, arguably, an overemphasis on the financial rather than social return on each deal. There is also currently a mismatch between the capital available and the finance needs of most social purpose organisations as most investors seek secured loans whilst investee demand is largely for unsecured funds.
9. Data on deal flows show that the majority of social finance is currently issued as secured lending to organisations with evidence of a reliable revenue stream and a track record of high performance. However, few social purpose organisations have a strong asset base on which to secure their lending. These organisations are also frequently prevented by their legal structures from offering the kinds of equity stakes that may be sought by venture capitalists. A 2013 study by Social Enterprise UK found that access to finance remained the top barrier to growth for the majority of social purpose organisations.
10. As noted at your 20th June 2013 meeting there is a funding gap in the market. Research from the Big Lottery Fund and Big Society Capital indicates that whilst there will be demand for approximately £1bn social investment over the next five years, this will largely be for unsecured debt.
11. Social investment is likely to remain a relatively small and niche market unless more finance is made available for early stage investment either in new organisations or new ventures.

12. As discussed at previous meetings, there is scope for you to play a valuable role by providing finance for high risk, potentially high impact social investment propositions. Providing some support to this section of the market is likely to be welcomed, benefit the City of London's reputation as a progressive social investor and, in the longer term, increase the number of deals reaching you for larger investment.

Running Costs of the City of London Corporation Social Investment Fund (October 2012 – September 2013)

13. Common Council assigned responsibility for Fund administration to the Chief Grants Officer of City Bridge Trust. The Trust publishes details of your investment criteria, acts as first point of contact for prospective investees, and works actively to source prospective deals. City Bridge Trust staff work closely with colleagues in the Chamberlain's Department to appraise individual investment proposals, and with the Economic Development Office which leads for the Corporation on social investment policy.
14. It is a requirement of Common Council that all investment opportunities be subject to a third party financial review, and you have appointed three advisory firms to undertake this work so far (Social Finance Limited, the FSE Group, and a partnership between the Social Investment Business, Investing for Good, and the Good Analyst). The Trust manages these relationships and average spend per investment review has been £3,000, with £12,000 spent in total between October 2012 and September 2013.
15. Legal costs have been incurred for each investment, with the majority of chargeable hours delivered by City Solicitor's Department. In the case of one investment, officers instructed a third party firm to undertake a legal review. So far £27,430 of internal and £4,000 of external legal costs have been incurred.
16. In addition, the Trust has incurred fees for the development of an investment management database, but this has been done as cost-effectively as possible by building on existing Corporation systems. The Trust has spent £1,200 on IT so far.
17. The Fund has also benefitted from the input of the Social Investment Advisor, who is paid for by Policy & Resources and City Bridge Trust Committee. Her contract with the City of London is due to expire in March 2014.
18. City Bridge Trust and Chamberlain staff time on the Fund has not been identified separately so far, but the first year of operations this new initiative has required significant input as appraisal and administrative systems are established. Continued time is needed to source and evaluate deals. The Trust will be carrying out its comprehensive business planning this autumn, however it is likely approximately 3.5 days per week of City Bridge Trust staff time will be needed over the next 12 months to manage the Fund. The Trust has reviewed staffing roles to ensure this work can be met in the short-term, but it will be necessary to seek additional administrative support to help with the time-consuming process of placing and monitoring investments once approved by your Board.

19. Total fees outlined above, net of staffing and the Social Investment Advisor total £44,630, or 3.4% of the value of investments placed to date:

Independent advisory fees	£12,000
Legal fees	£31,430
IT costs	£1,200
Total	£44,630

20. Fees and staffing (with the exception of the grant to cover costs of the Social Investment Advisor) have been met within City Bridge Trust's local risk budget which was set at its current level prior to the establishment of the Fund. This is not sustainable in the medium / long-term. As noted in the 25th October 2012 paper to Common Council, the ongoing nature of the Fund means that the Trust will seek approval from the Policy & Resources Committee for an uplift in this budget.

Recommendation:

That you note the contents of the report.

That you authorise officers to prepare a paper to Common Council reporting on the first year of your Fund

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Report written: 2nd September 2013