BIG SOCIETY CAPITAL

The Solutions Collective

Insights Forum 2

Catalytic capital: Can it enable truly innovative social investment?

Session agenda:

'Catalytic capital – what is it and what is its role in making social lending work better?'
- Amir Rizwan, Big Society Capital

'Catalytic capital in action – what does this mean in practice to an investor and the investee?'
- Denise Holle, Joseph Rowntree Foundation (JRF)

Slides used during the session can be found here

Recording of presentations can be accessed here

Note due to the commercial sensitivity of some of the presentation and discussion only an abbreviated version is available retrospectively

Context

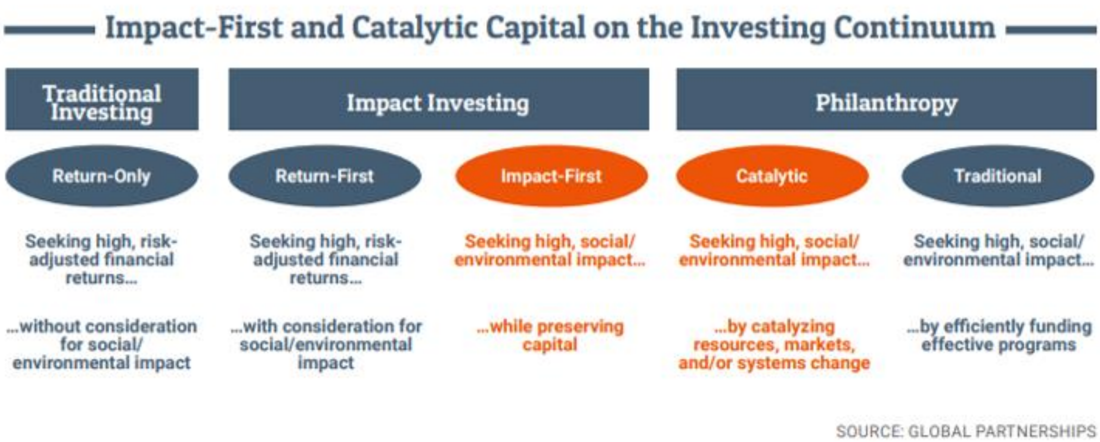
Understanding the difference between concessionary capital and catalytic capital was a clear learning objective and discussion point.

Whilst catalytic capital can be concessionary, it is not the only consideration and works where there are capital gaps.

Definition

"Catalytic capital accepts disproportionate risk and/or concessionary return to generate positive impact and enable third-party investment that otherwise would not be possible." Catalytic capital seeks to address capital gaps, i.e., investment opportunities that mainstream commercial investment markets fail to reach, partially or fully, because they do not fit the risk-return profile or other conventional investment norms and expectations that such markets require.

Where catalytic capital works



The history

- In places such as the US there is government legislation in place which has driven the availability of this type of capital
- Increasing research including the recent [Reclaiming the Future : Commission on social investment]() has highlighted where demand for finance is out of step with supply
- There is potentially a lack of understanding about what catalytic capital is and how it can be structured effectively
- How it differs from purely concessionary capital and who the suppliers of this capital might be
- The Association of Charitable Foundations (ACF) and Big Society Capital are currently [conducting research to better understand how to grow the supply of catalytic capital in the UK]() with their report due to be published in September

The supply

- Traditionally providers of this sort of finance have come from grant making trusts and foundations
- We need to debunk the myth that all catalytic providers must be from just philanthropic sources
- Current providers include:
  - Providing government/Local Authority/Public Services
  - Cornerstone investors including wholesalers such as Big Society Capital and the Access Foundation
  - Private investors – including High Net Worth (HNW) investors and family offices

The application

- Traditionally providers of this sort of finance have come from grant making trusts and foundations
- Examples of types of structuring where catalytic capital can provide investment which can service the business model requirements include but are not limited to:
  - Blended finance – grant and investment
  - Concessionary rates
  - Patient longer term debt
  - Flexible product structuring (debt converted to equity or repayable grant)
  - Equity like – revenue participation
  - Sharia compliant lending
  - Market building - cornerstone investment (high risk/return tolerance)

The opportunity

- Ensuring more enterprise centric finance is available to meet the needs of social enterprises and charities is a key goal for the social lending strategy
- The challenge is in bringing more investor's capital into the market to supply this. Three key areas outlined in the discussion are the investor's understanding of:
  - Return – this is generally well understood however the return needs to be adjusted depending on the risk e.g., local authority off setting return against cost savings or benefits to other services.
  - Risk – is poorly understood often because the business model does not perform as more traditional commercial models e.g., things that are not well understood or familiar are often assigned as being too risky as an easier option/opt out
  - Effort – where the risk and return are acceptable to pools of existing investors but where the time and effort and considered to be outside of scope. e.g., smaller investments

Key insights:

- The importance of widening the base of providers of catalytic capital and not placing the burden on trusts and foundations – exploring the adoption curve
- Another element of risk for consideration is time – how long investors are prepared to wait or tie up capital in catalytic deals
- We need to be clear, open and more comfortable with an appropriate level of return and whether it is justified for the level of risk being incurred. To better understand the trade offs with concession and understand the clearing point or tolerance for both sides whilst not just 'accepting' the current norms
- What are the practical steps we need to take collectively to move the boundaries for investors around risk/return/effort & time

Catalytic capital raised during the discussion or speaker presentations that have influenced or further informed your thinking around the subject of catalytic capital?

'There is a balance between investing directly and via pooled vehicles. This is relevant to the resource we have but is also balanced on the expertise that fund managers can offer to individual enterprises. But impact is agnostic. We shouldn't be focused on the financial structure but on the impact that the investment can make.'

Denise Holle, Head of Social Investment, Joseph Rowntree Foundation (JRF)

Other reading and resources referenced during the discussion or for additional context:

- Catalytic Capital Consortium MacArthur Foundation
- Social Lending: https://bigsocietycapital.com/latest/social-lending-ambitions-direction-and-levers/
- https://shiftdesign.org/content/uploads/2018/11/Social-Investments_with-Philanthropic_Capital.pdf
- https://shiftdesign.org/content/uploads/2020/05/Beyond-Demand-Report_Shift_EsmeeFairbairn.pdf
- Tideline - https://tideline.com/wp-content/uploads/2020/11/Tideline_Catalytic-Capital_Unlocking-More-Investment-and-Impact_March-2019.pdf

Our Social Lending Strategy

We want to see a social lending market that meets the needs of a diverse range of social purpose organisations and investors alike. To do this we are exploring a range of tools and levers including the use of guarantees, tax, catalytic capital in order to increase the supply of concessionary capital.

We recognise the importance of partnership and of ensuring that user insight and lived experience are embedded in our design and development processes. The Solutions Collective is an initiative to support the growth of the social lending market in the UK.

Suggested Solutions Collective Future Topics:

1. Convening social enterprises (as potential investors) around the usage of guarantees to learn from each other – approached E3M as a potential partner
2. Convening trusts and foundations and social investors (non-T&F) to discuss using charitable funds to guarantee social investment clearly targeting excluded people, organisations and communities - approached Association of Charitable Trusts as a potential partner
3. Tax reliefs and putting tax to work to increase access to finance
4. Sharia compliant social lending structures

Register your interest for future Solutions Collective events or suggest topics here